23 May 2017

Dear Members,

DEBSWANA PENSION FUND BUSINESS BRIEF - MAY 2017

This is the first of three high level reports on the primary key performance indicators of the Fund that we will endeavour to give you during 2017 and subsequent periods as a complement to the normal Fund communique. This is in response to your cited desire (as per past survey outcomes) to be kept more regularly informed on Fund investment and financial performance outside of annual reporting. We trust that you will find the business brief informative, and should you need to discuss or understand the report further please contact your usual Member Relations Officers.

1. INVESTMENT PERFORMANCE

Market performance – Year ended 2016

Result Summary

During the year ended December 31, 2016, the Debswana Pension Fund assets increased 3.16 percent (gross) to P6.565 billion. The respective investment portfolios delivered similarly as follows;

Fund	12 month	36 month	60 month	Since Inception (Aug 2004)	Target
Market	3.48%	9.38%	14.51%	13.90%	CPI+5%
Conservative	2.42%	8.55%	10.83%	11.53%	CPI+3%
Pensioner	2.36%	8.85%	12.37%	13.05%	CPI+4%
Contingency	2.81%	8.97%	13.78%	15.50%	
Fund	**3.04%**	**9.07%**	**14.37%**	**15.75%**	**CPI+5%**
Inflation	**3.01%**	**3.30%**	**4.27%**	**7.09%**	

Declining returns

In the short-term results (12 months), there is a notable under-performance (relative to target-refer to table) across all portfolios with the highest yielding portfolio barely meeting inflation. The decline in the 2016 returns can be explained as follows;

Global Markets

Politics, policies and sentiment guided markets in 2016 on a volatile road. The year started with a drop in equity markets worldwide after the US started a rate hiking cycle in December 2015. The downturn was moderated as the Fed then stepped away from hiking and the simultaneous introduction by China of various pro-growth policies. Towards the end of Q1, prospects of recovering growth led to commodity prices ticking up in the second quarter and resource shares regaining a little of their three year-long fall. The markets were again negatively affected by the UK's vote to exit the EU in the June 23rd, 2016 referendum, and consequently tracked sideways during Q4, 2016 which saw Donald Trump's somewhat surprising victory in the US elections and accompanying uncertainty. With a Federal Reserve Bank interest rate hike looming on the horizon for much of the period (and realized in December), bond markets were notably unsettled. Government bond yields moved higher, and yield curves steepened during the Q4 albeit off a very low base.

Throughout 2016, the dollar remained supported against most major currencies, though towards the latter part of the year, the commodity price rise saw a strengthening of Emerging Markets currencies such as Russia, Brazil and South Africa whose economies are resource oriented. Given the South African Rand strength and the 50% exposure to ZAR in the BWP currency PEG ratio, the BWP strengthened against the dollar by 5.23%. This had the effect of wiping out the muted positive dollar returns from global equities and dragging global bond market performance into negative territory.

Local markets

The year of 2016 was unpleasant for the local equity market. The market continued to fall towards the end of the year driven by large cap counters in the banking and consumer sector. The Domestic Companies Index (DCI) (including income) was down -11.38% in 2016. Financial companies performed poorly, with Standard Chartered and First National Bank as the key laggards. Both banks traded under cautionary statements relating to the impact of the liquidation of the state-owned BCL copper-nickel mine ahead of the upcoming earnings reporting season. The BCL liquidation has had adverse effects on the economy, affecting both the private sector, the parastatals and general market sentiment. On the positive side, property companies registered strong performance over the year, partially offsetting other negative sector of the index.

Bond yields fell across the curve after the August, 12 2016 policy rate cut of 50 bps, with possible over-reaction as the market approached the September and December Government bond auctions. Yields rose subsequently at the September auction, before receding by about 10 bps across the curve at the end of 3rd quarter. To close the year, in the secondary market, the yield curve negatively tilted in the 4th quarter with yields falling around the maturity range of BW010. Government bonds yields reflect the weak economic conditions, the positive inflation outlook, and supply constraints.

Rates on money market instruments remained low during 2016 as the Bank Rate was reduced in August 2016. Expectations are that Bank of Botswana will continue with supportive monetary policy on account of the fragile local economy and the uncertain world economic outlook.

Implications

The Fund remains profitable over the long term as reflected in the medium to long term results, and it is important that members always remember that a pension fund must adopt a long term investment view with respect to assessing its financial soundness. However this does not suggest that the short term view must be ignored. This requires vigilance in monitoring performance, hence the Board of Trustees and Management of the DPF remain equally concerned by the ongoing market volatility both globally and locally, and are fully committed to doing everything necessary to mitigate where possible against potential market downturns, mainly through strategic and tactical investment policies. As an example, the Fund is in the process of implementing an Asset Liability Modeling strategy which is aimed at ensuring that the Fund grows at a rate adequate enough to enable it to meet its future liabilities.

Below is the historical investment returns of the DPF

Year ending 31 December	Market Channel	Conservative Channel	Pensioner Channel	Fund	Inflation
2005	32.9%	21.0%	26.9%	31.2%	11.4%
2006	33.9%	20.9%	27.9%	32.4%	8.5%
2007	16.6%	15.3%	17.5%	16.8%	8.2%
2008	-15.2%	-6.2%	-7.3%	-12.9%	13.7%
2009	15.9%	16.5%	15.2%	15.7%	5.8%
2010	7.5%	7.4%	7.1%	7.4%	7.4%
2011	10.6%	10.7%	11.7%	10.9%	9.2%
2012	16.7%	11.1%	13.8%	15.4%	7.4%
2013	28.9%	17.7%	22.1%	26.0%	4.1%
2014	11.5%	9.7%	11.0%	11.2%	3.8%
2015	13.6%	10.9%	12.6%	13.1%	3.1%
2016	3.01%	3.41%	2.69%	2.91%	3.0%
12 year annualised return (2005 – 2016)	**13.9%**	**11.3%**	**13.0%**	**13.5%**	**7.1%**

Year to date results and 2017 Outlook

Based on the unaudited market price movements obtained in the first quarter of 2017, The Fund anticipates an equally sluggish performance for the year 2017 as was 2016.

Unit Price Movements December 2016 to March 2017			
	Market portfolio	Conservative Portfolio	Pensioner
Net return (net of expenses)	**2.51%**	**1.10%**	**1.02%**
YTD Inflation	**3.00%**	**3.00%**	**3.00%**

We shall give the next performance update by end of Q3 2017.

2. FINANCIAL PERFORMANCE 2016

The Fund made a surplus of P 205 million in the current year as compared to P 772 million in the previous year; a decline of 72% which was mainly due to a number of factors but mainly the following:

Revenue

a. Share of profits from private equity loan investment declined by P5.3 million (83%)

b. Unrealised foreign exchange loss in 2016 amounted to P195 million compared to a gain in 2015 of P554 million, thereby registering a decline of P749 million; this being the major cause of a significant drop in the surplus for 2016. The BWP strengthened against the USD during the year under review. The Fund's USD denominated assets translated at opening BWP/USD rate of 11.2359 and closing USD rate of 10.7296 resulted in P195 million foreign exchange loss in 2016

Unrealised fair value gains increased from P77 million in 2015 to P249 million in 2016 (69%) due to a good performance in the global financial market. The increase predominantly pertained to offshore investments at P324 million and a loss of P75 million on onshore/local investments. This performance neutralised the impact of a significant loss resulting from foreign exchange fluctuations between the US Dollar and Botswana Pula currencies.

Expenditure

c. **Pensions to retired members**: increased from P109 million in 2015 to P122 million in 2016 due to pension increases which effected in July 2016, as well as new engagements;

d. **Lump-sums on retirement**: these increased from P52 million in 2015 to P81 million in 2016 because most of deferred members who attained 50 years of age cashed in their 33.33% commutations going into retirement;

e. **Offshore investment management fees**: The fees increased from P21 million in 2015 to P54 million in 2016 due to a growth in investments.

Control environment

The December 2016 Internal Audit was of the opinion that the internal controls at Debswana Pension Fund (DPF) were generally adequate, and effective to provide reasonable assurance that risks were being managed appropriately and objectives would be met. Seven audits were issued as at December 2016 as follows:

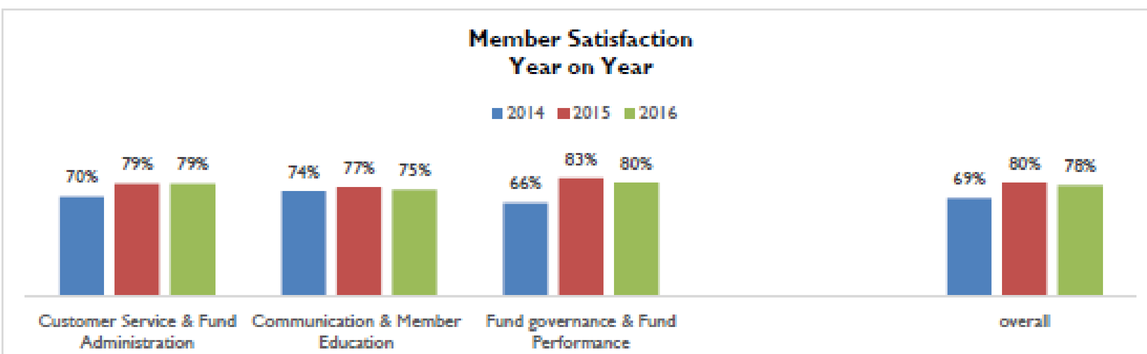
i. Pensioner payroll – Good
ii. Procurement process Follow Up – Moderate
iii. New Benefits Administration System Implementation Project – Good
iv. Unit Pricing– Moderate
v. Investment Management – Good
vi. Cost per member Management – Moderate
vii. Board Governance – Moderate

External audits were completed in Q1 of 2017.

3. BUSINESS PARTNERS/STAKEHOLDER ENGAGEMENT

According to the 2016 stakeholder satisfaction surveys, members and business partners are generally satisfied with DPF service with a recorded improvement since 2014. Satisfaction levels between 2015 and 2016 have stagnated with a slight decline on the member outcome in particular.

	Overall summary scores		
SURVEY	2014	2015	2016
Member satisfaction	69%	80%	78%
Business Partners Satisfaction	78%	83%	83%



The Fund implements annual communication plans aimed at both member education and stakeholder engagement objectives. The Fund targets a 75% satisfaction rate in line with globally recognised customer service satisfaction benchmarks.

Year to date – stakeholder engagement plan

The 2017 Communication plan is in progress with some of the major communication initiatives such as **a Member engagement tour of the participating employers**, **Pensioners conference** and **deferred members' Annual meeting** scheduled for the June-October period.

4. INTERNAL PROCESSES & PEOPLE

On the administration front the Fund is operating optimally with most of our efficiencies realised. Regarding people, the Fund is fully resourced albeit for a couple of vacancies arising from both attrition and restructuring.

A full annual report on 2016 performance will be released before the end of Q3 2017.

Sincerely

Mpho Mphafe-Fish
CHIEF EXECUTIVE OFFICER (ACTING)