Volume 9, No. 5, May 2013

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 MAY 2013

By Tilman Friedrich, Managing Director and Thoms Kaber, Wealth Consultant of RFS

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1. Review of Portfolio Performance

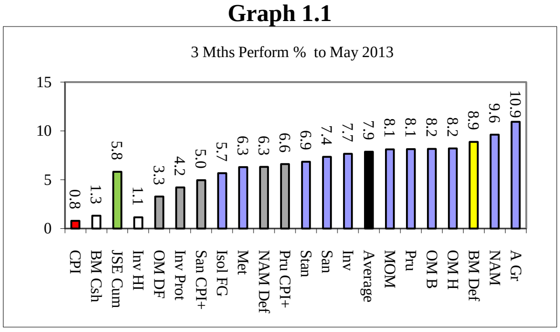
In **May** the **average prudential balanced portfolio** returned 6.25% (April minus 0.59%). Top performer is Namibia Asset Management (8.33%), Investment Solutions (4.56%) takes bottom spot.

Graphs 1.1 to 1.7 reflect the performance for periods from 3 months to 10 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no color bars), the average of prudential balanced portfolios (black bar), the JSE Allshare Index (green bar), and the CPI (red bar). Benchmark investors should take note of the performance of the default portfolio (yellow bar), which now represents a combination of Prudential Namibia Inflation Plus and Allan Gray.

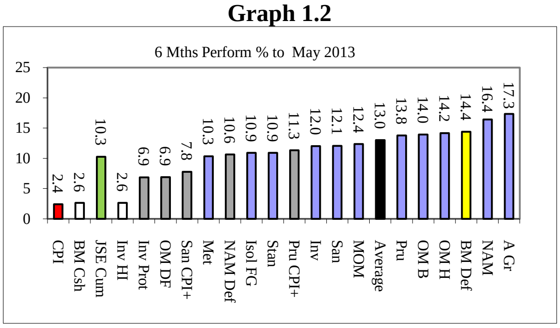
Below is the legend to the abbreviations reflected on the graphs:

Benchmarks	
Namibian Consumer Price Index	CPI (red)
JSE Allshare Index	JSE Cum (green)
Benchmark Default Portfolio	BM Def (yellow)
Average Portfolio (prudential, balanced)	Average (black)
Special Mandate Portfolios	
Money market	BM Csh (no color)
Investec High Income (interest bearing assets)	Inv HI (no color)
Investec Protector	Inv Prot (grey)
Prudential Inflation Plus	Pru CPI+ (grey)
Old Mutual Dynamic Floor	OM DF (grey)
Sanlam Inflation Plus	San CPI+ (grey)
NAM Coronation Balanced Def	NAM Def (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Inv (blue)
Investment Solutions Bal Growth, (multimanager)	Isol FG (blue)
Prudential Managed	Pru (blue)
Metropolitan Managed	Met (blue)
NAM Prudential Balanced	NAM (blue)
Old Mutual Profile Balanced	OM B (blue)
Old Mutual Profile Growth	OM H (blue)
Momentum Managed	MOM (blue)
Sanlam Managed	San (blue)
Stanlib Managed	Stan (blue)

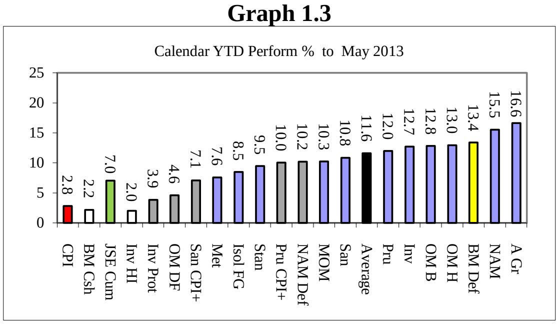
Graph 1.1



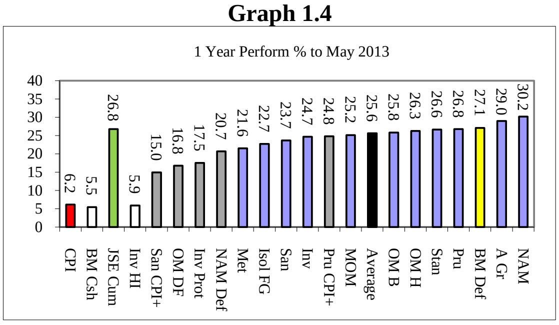
Graph 1.2



Graph 1.3



Graph 1.4



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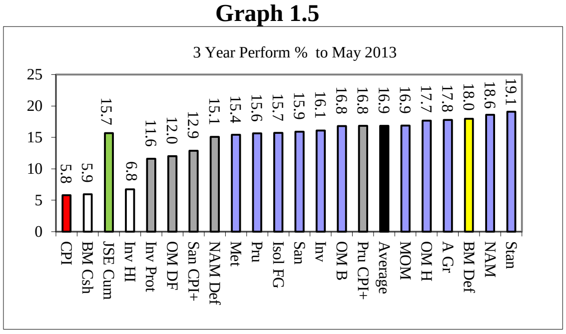
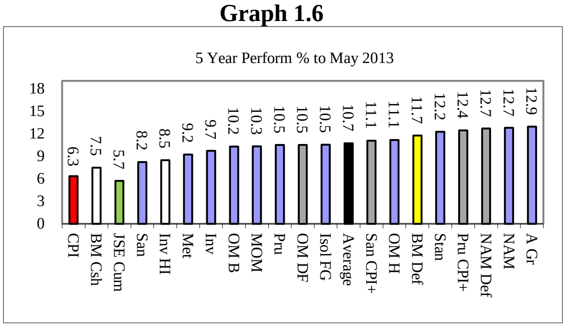
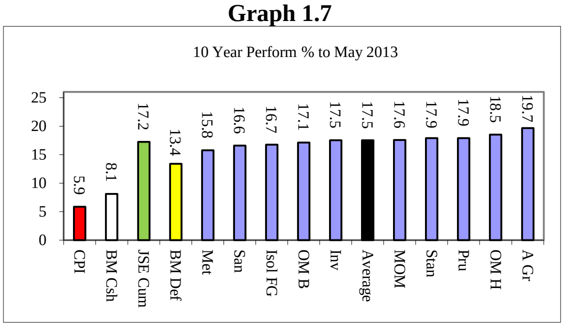
Graph 1.5



Graph 1.6

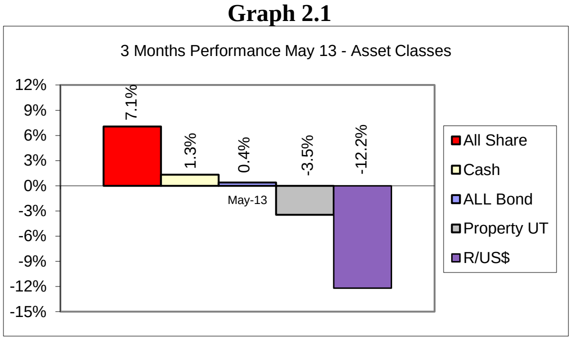


Graph 1.7

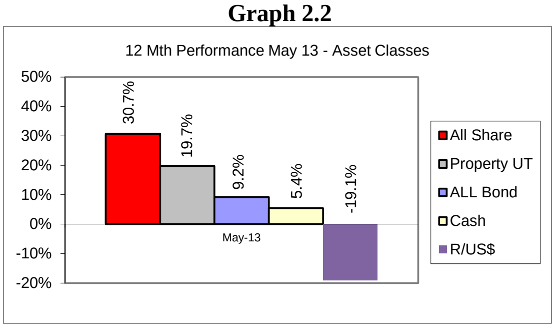


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

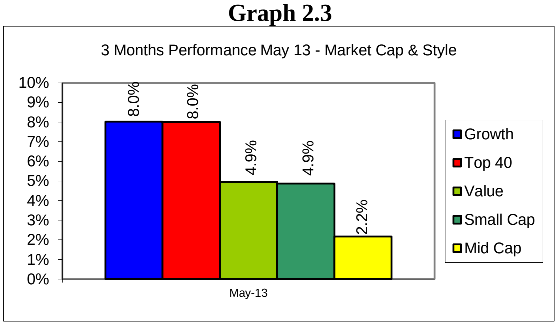
Graph 2.1



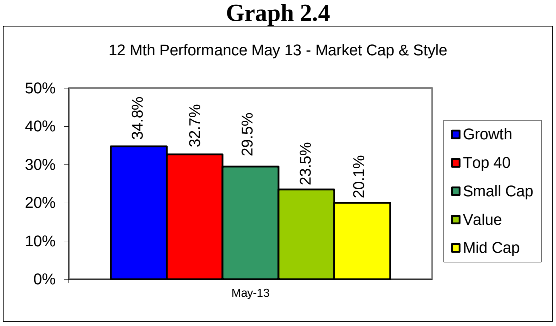
Graph 2.2



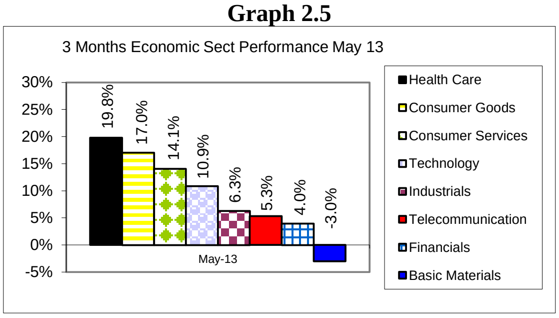
Graph 2.3



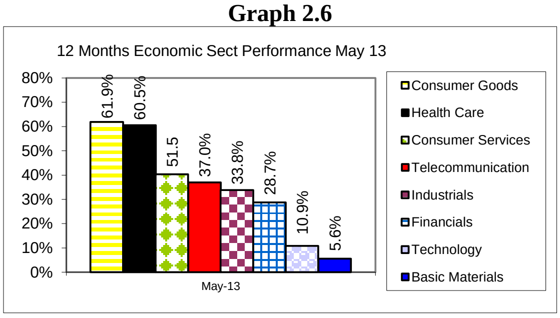
Graph 2.4



Graph 2.5



Graph 2.6



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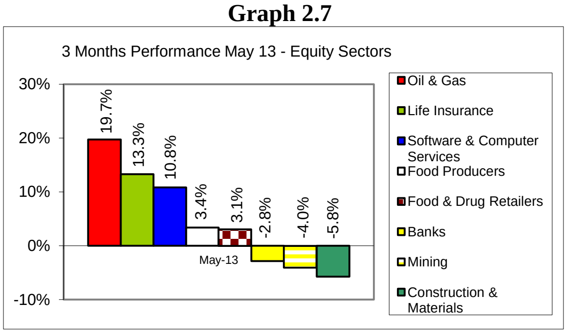
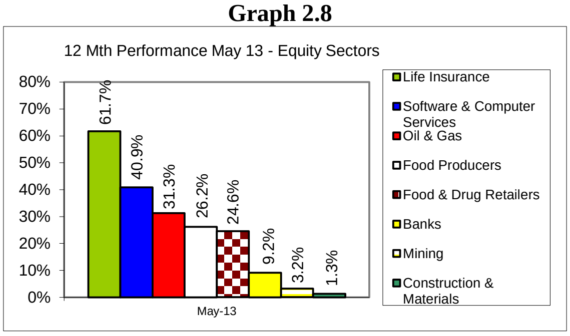
Graph 2.7



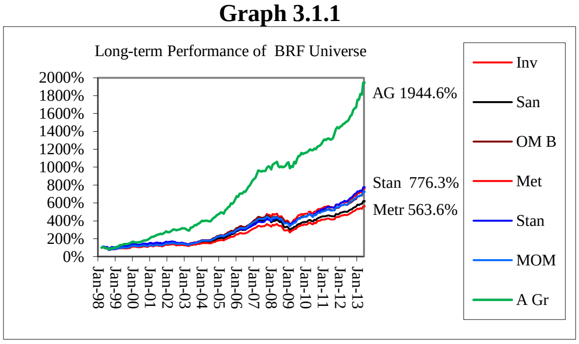
Graph 2.8



3. Portfolio Performance Analysis

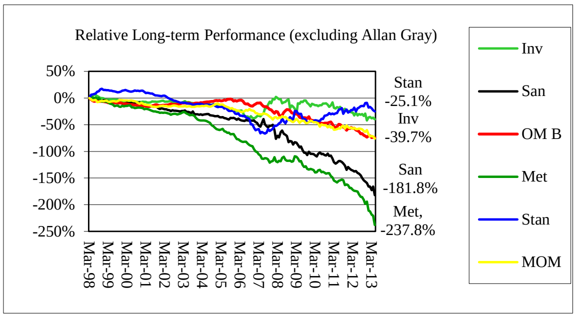
3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

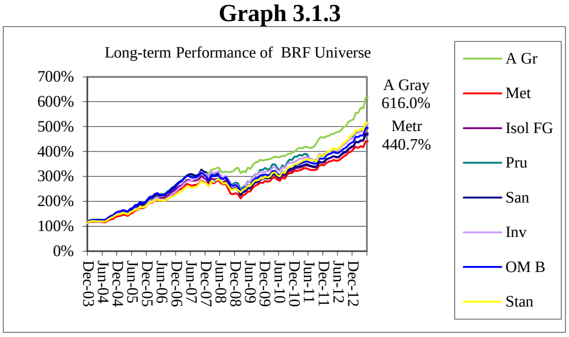


Graph 3.1.2

Cumulative performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

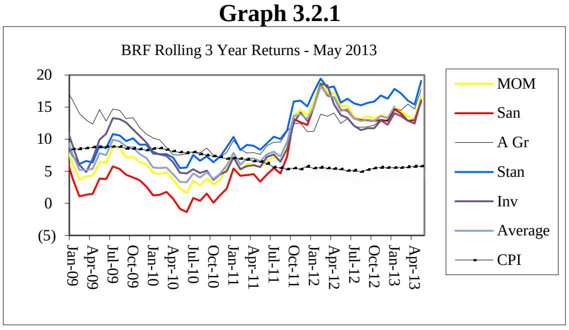


Graph 3.1.3

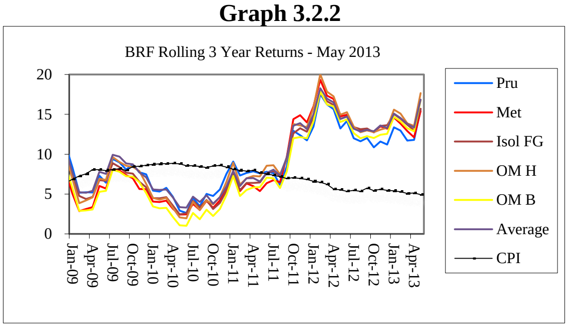


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1

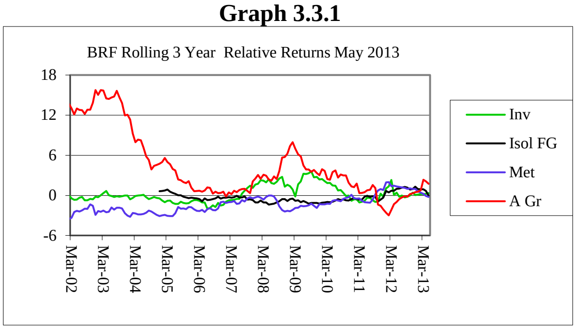


Graph 3.2.2



3.3. 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

Graph 3.3.1



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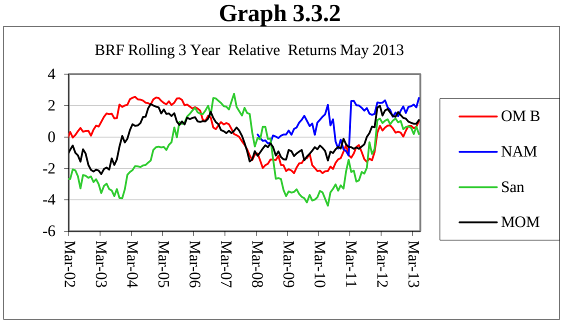
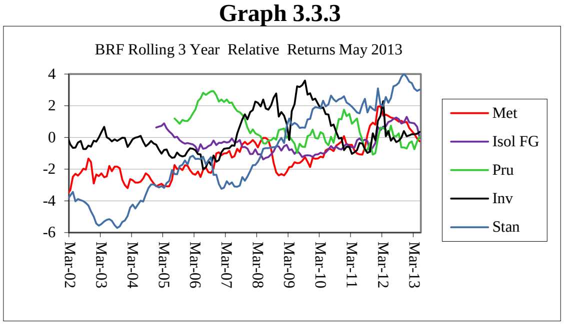
Graph 3.3.2

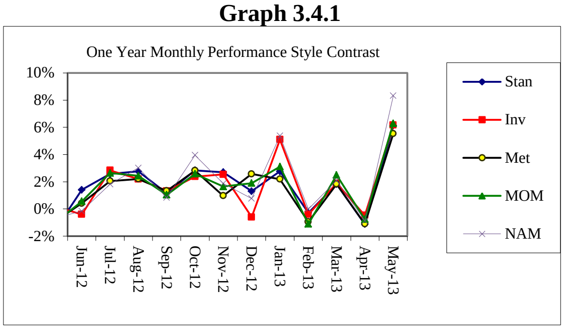


Graph 3.3.3

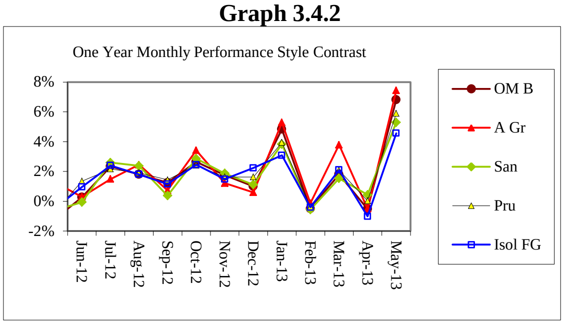


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

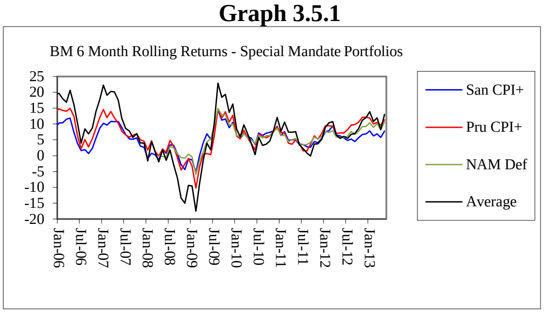


Graph 3.4.2

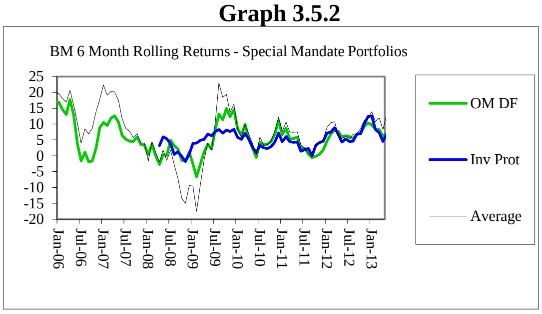


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

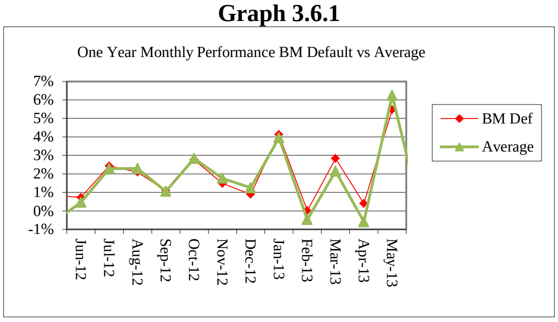


Graph 3.5.2

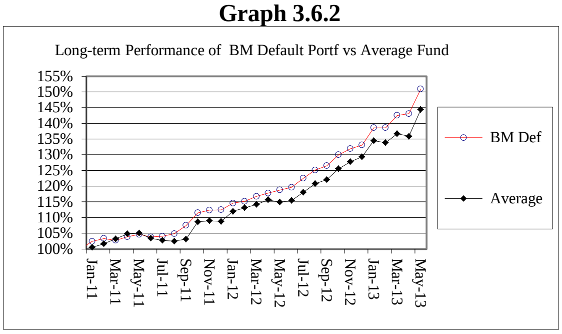


3.6 Monthly and cumulative performance of 'Benchmark Default' portfolio relative to average prudential balanced portfolio

Graph 3.6.1



Graph 3.6.2



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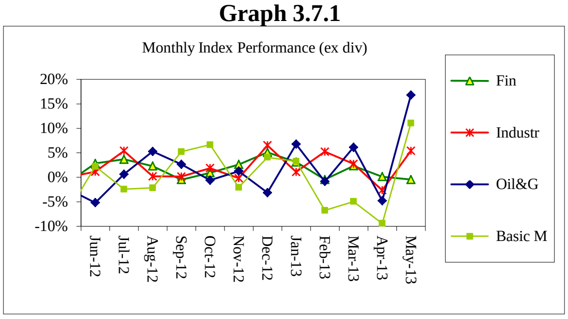
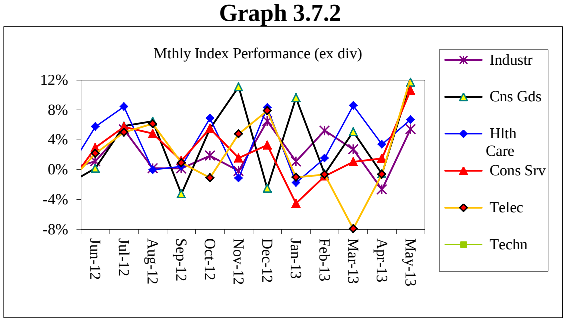
3.7 Monthly and one year cumulative performance of key indices (excluding dividends)

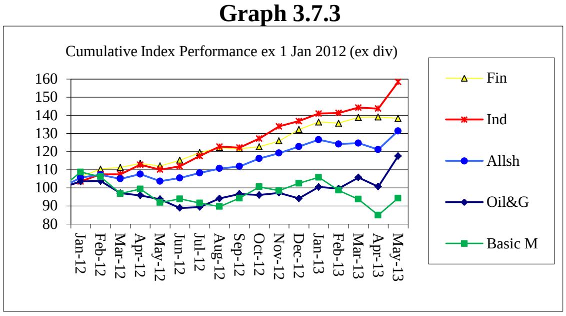
Graph 3.7.1



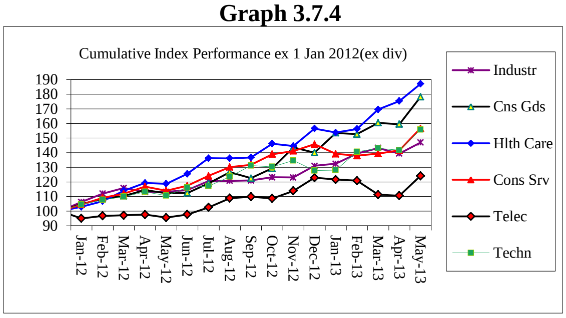
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio

Graph 1.6 shows that the average prudential balanced portfolio returned 10.7 % p.a. in nominal terms, or 4.4% p.a. in real terms, over the past 5 years while the Benchmark Default portfolio returned 11.7% p.a. in nominal terms, or 5.4% p.a. in real terms. This outperformance of the average manager by the Benchmark Default portfolio is quite remarkable considering its substantially lower equity exposure (49.0% vs 62.8% as at the end of May 2013).

Considering that the average prudential balanced portfolio should deliver a real return before management fees (typically 0.75%), of roughly 6% per year, these portfolios are currently trailing the expected long-term goal over the past 5 years.

Having raised the risk profile of the Default portfolio effective the start of 2011, by replacing Metropolitan ARF with the Allan Gray Investment Trust, we would expect the Default portfolio to sacrifice around 1% return for the benefit of lower volatility compared to the average prudential balanced portfolio, thus an expected real return before management fees (typically 0.75%), of around 5% per year. Over the past 5 years this performance objective was achieved. Since this change was effected, the default portfolio returned a cumulative 41.7% compared to 37.4% for the average prudential balanced portfolio over this 29 month period.

Relative to the default portfolio, the performance of the prudential balanced portfolios should be more volatile due to a significantly higher equity exposure and its performance should be much closer correlated to that of the overall equity market. The default portfolio should produce a significantly more volatile performance than the money market portfolio. The table below presents one year performance statistics over the 3 years June 2010 to May 2013:

Table 4.1

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.5%	9.2%	7.4%
Best annual performance	7.5%	27.1 %	25.6%
No of negative 1 year periods	n/a	0	0
Average of negative 1 year periods	n/a	n/a	n/a
Average of positive 1 year periods	6.3%	14.5%	14.0 %

The Benchmark Default portfolio is a more conservative investment aimed at reducing negative returns and with a long-term return objective of inflation plus 5% before fees and roughly 4.3% after fees.

At this rate of return, the net contribution towards retirement by both, member and employer should be roughly 13% of remuneration, in order to achieve a reasonable income replacement ratio of 2% per year of service. It is very important that employers invested in the default portfolio are comfortable with these investment characteristics and that they should be able to create comfort amongst their employees as well.

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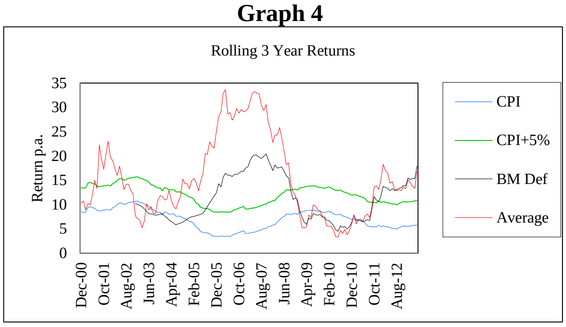
Graph 4



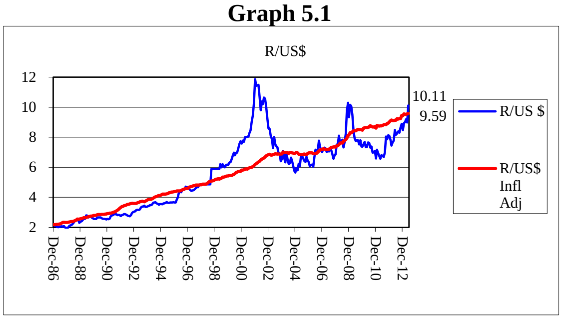
Graph 4 measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. It shows that since September 2008, both the Benchmark Default portfolio as well as the average prudential balanced portfolio were lagging inflation plus 5% and have surpassed inflation plus 5% since October 2011, Benchmark default portfolio currently on 18.0%, the average on 16.9% vs CPI plus 5% currently on 10.8%.

5. Review of Foreign Portfolio Flows and the Rand

How is the Rand doing?

Graph 5.1 indicates that the Rand by our measure is fairly valued at 9.59 to the US Dollar while it actually stood at 10.11 at the end of May. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

Graph 5.1

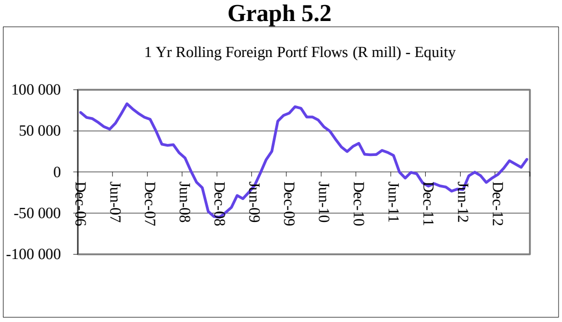


Rand under pressure due to foreign capital outflows

Graph 5.2 reflects a steady slightly positive flow of capital into South African equities on a rolling one year basis, with a net inflow of R 12.6 bn on a year-on-year basis at the end of May (inflow of R 15.5 bn to end April). Since the beginning of 2006, foreign net investment in equities amounts to N$ 184 billion (end April R 183 billion). This represents roughly 2% of the market capitalization of the JSE.

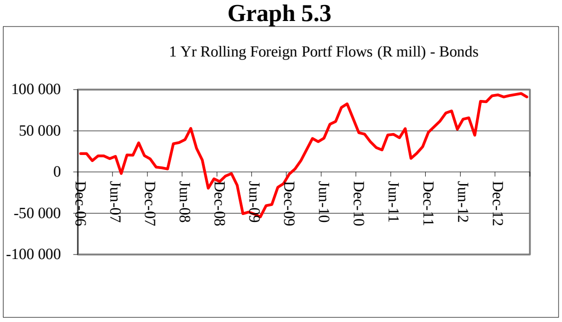
Revaluations of emerging economies combined with a possible let up of fiscal easing measures in the US has led to significant capital outflows out of South Africa. Local bond yields are on the rise and many foreign investors are seeking value elsewhere. This sell off of emerging markets has put pressure on the exchange rate. The declining trend in foreign portfolio flows and the pressure on the Rand is likely to persist and to increase as the prospect of the tapering off of intervention by the Fed becomes ever more likely.

Graph 5.2



Graph 5.3 on a rolling one year basis, reflects a fairly steady foreign portfolio flow into bonds of R 92.5 bn over the past 12 months to end of May (R 91.0 billion over the 12 months to end of April). Since the beginning of 2006, foreign net investment in bonds amounts to just above R 240 bn (to April just below N$ 245 bn).

Graph 5.3



The net inflow of foreign capital into equity and fixed interest assets was R 105 bn for the 12 months to end May 2013 (inflow of R 107 bn to end April 2013), compared to R 31 bn for the 12 months to end May 2012 (R 51 bn to end April 2012). Since the beginning of 2006, total net foreign portfolio flows amounted to N$ 424 billion (April R 428 bn).

Graph 5.4 reflects the movement of the JSE and the DOW Jones since May 1999. In nominal terms the JSE passed its month end peak of before the financial crisis of 31,841 (May 2008), while the DOW Jones at the end of January for the first time matched its previous peak of 13,896 (Sep 2007). In nominal terms, the JSE grew by 14% per year, while the DOW Jones only grew by 2.4% per year, over a period of just over 13 years, dividends excluded. Namibian inflation over this period was 7% per year in contrast with US inflation of 2.5%.

Graph 5.5 reflects the same statistics but adjusted for US and SA inflation respectively. Since May 1999 the JSE Allshare Index has grown by 7% per year above

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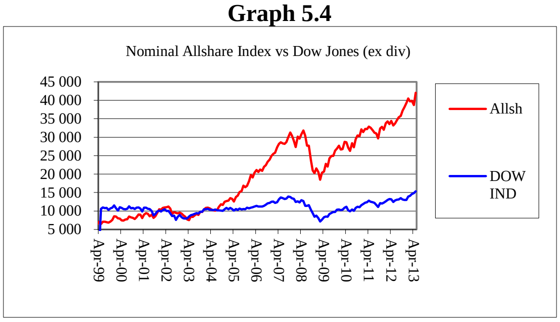
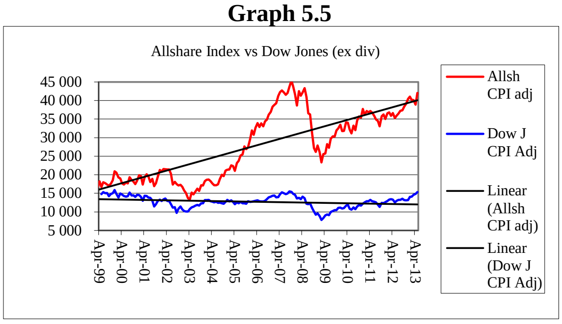
inflation, over this period of close to 14 years, and this excludes dividends of somewhere in the region of 2% to 4%. In contrast, the DOW only managed to match inflation over this period, also excluding dividends.

Graph 5.4

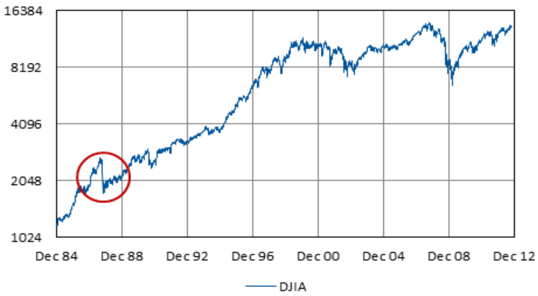


Graph 5.5



Graph 5.6

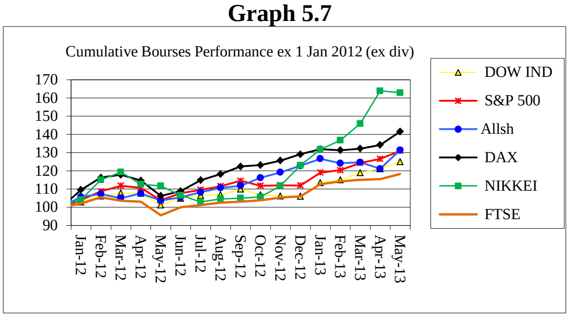
The Dow Jones Industrial Index, over the longer term:



Graph 5.6 places the data as per graph 5.4 into a better perspective, showing that graph 5.4 actually starts measuring the DOW Jones just after it had reached a peak around 1998.

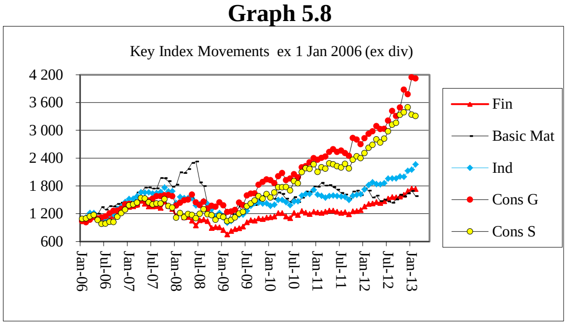
Graph 5.7 provides an interesting overview of some of the major global share indices, showing up the NIKKEI and the DAX as the top performing share indices.

Graph 5.7



Graph 5.8 provides an interesting overview of relative movement of the key equity sectors on the FTSE/JSE since December 2005 when these indices were first introduced. From this the investor should be able to deduce which sectors offer greater value and which one's offer less value on the basis of fundamentals.

Graph 5.8



6. Conclusion

We have been concerned about the exaggerated growth of local equity markets as the result of fiscal and monetary intervention by governments and reserve banks across the globe for some time. This intervention has resulted in large flows of capital into emerging markets such as South Africa, in search for higher yields outside the low interest rate environments of the developed world.

For us in Namibia, equity and equity investors benefited from a strong Rand and borrowers from low interest rates. Those that invested offshore or in fixed interest instruments suffered.

It becomes ever more evident that the tide is busy turning. Interest rates will increase further over time and the trend of the Rand will remain negative. The time is now approaching for borrowers to realize their equity investment, while equity is still at elevated levels, to pay off debt because the return on equity investment is likely to move lower than interest on loans.

The current global economic environment is unlikely to show strong growth in any particular area. Momentum, theme or growth investment philosophies are likely to underperform a value philosophy. While we expect equities to produce only pedestrian performance, it should still outperform local fixed interest instruments that are expected to be punished in anticipation of rising interest rates.

A globally well diversified portfolio, comprising an assertive equity exposure of value companies in the consumer and technology sectors with strong cash flows and high dividend yields, some property exposure of properties with similar characteristics and low gearing are really the asset classes we believe can deliver satisfactory returns over the next one to two years. In terms of the weighting of the equity exposure we believe that foreign equity should be overweight relative to local equity.

7. Important notice and disclaimer

Whilst we have taken all reasonable measures to ensure that the results reflected herein are correct, Benchmark Retirement Fund and Retirement Fund Solutions Namibia (Pty) Ltd do not accept any liability for the accuracy of the information and no decision should be taken on the basis of the information contained herein before having confirmed the detail with the relevant portfolio manager. The views expressed herein are those of the author and not necessarily those of Benchmark Retirement Fund or Retirement Fund Solutions.