Volume 11, No. 05,
May 2015

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 MAY 2015

By T H Friedrich – Managing Director, Retirement Fund Solutions Namibia (Pty) Ltd

The monthly review of portfolio performance, as set out in this issue, is also available on our website at www.rfsol.com.na.

1. Review of Portfolio Performance

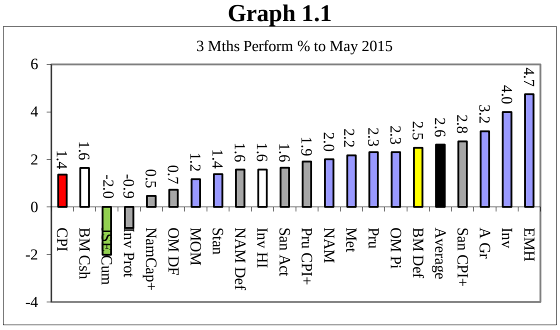
In **May** the **average prudential balanced portfolio** returned -1.01% (Apr: 2.36%). Top performer is EMH Prescient (-0.38%); while Metropolitan (-1.41%) takes the bottom spot. For the 3 month period EMH Prescient takes top spot, outperforming the 'average' by roughly 2.1%. On the other end of the scale Momentum underperformed the 'average' by 1.4%.

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 Namibia Balanced Fund.

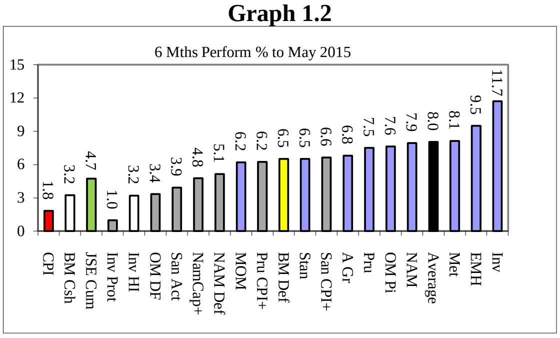
Below is the legend to the abbreviations reflected on the graphs:

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 Active	San Act (grey)
Sanlam Inflation Linked	San CPI+ (grey)
NAM Capital Plus	NamCap+ (grey)
NAM Coronation Balanced Def	NAM Def (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
EMH Prescient Balanced Absolute	EMH (blue)
Investec Managed	Inv (blue)
Prudential Managed	Pru (blue)
Metropolitan Managed	Met (blue)
NAM Prudential Balanced	NAM (blue)
Old Mutual Pinnacle Profile Growth	OM Pi (blue)
Momentum Managed	MOM (blue)
Stanlib Managed	Stan (blue)

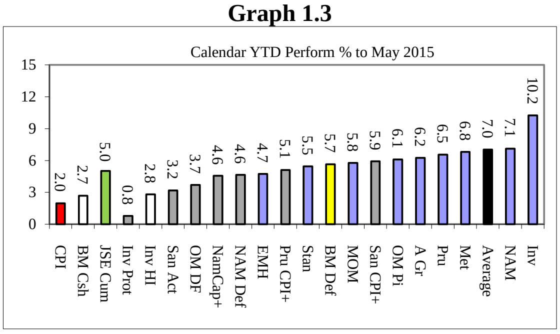
Graph 1.1



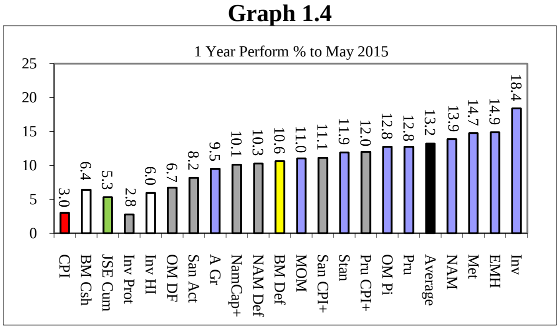
Graph 1.2



Graph 1.3



Graph 1.4



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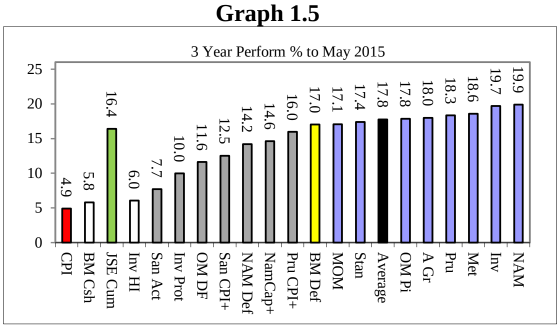
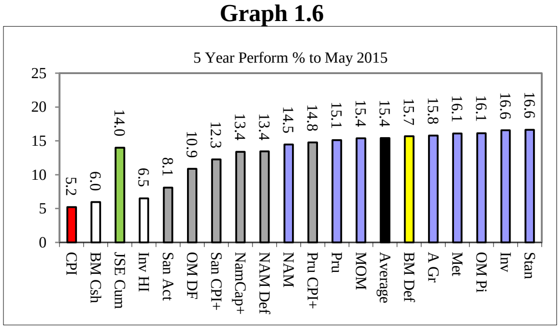
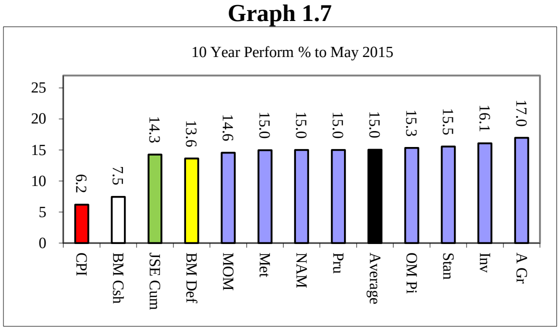
Graph 1.5



Graph 1.6

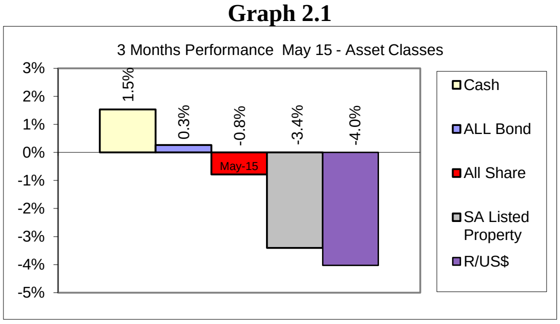


Graph 1.7

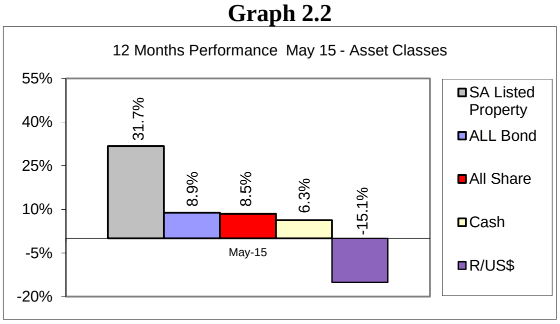


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

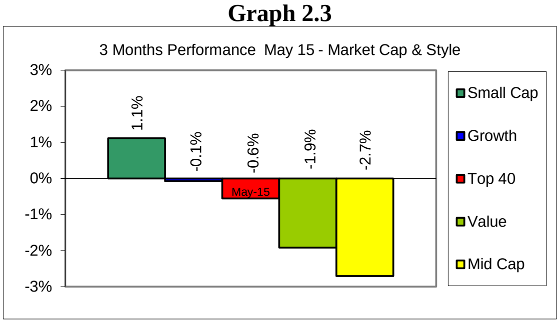
Graph 2.1



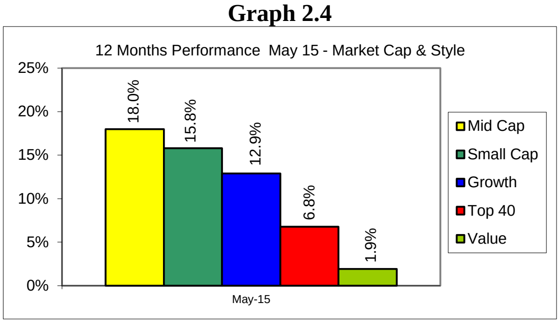
Graph 2.2



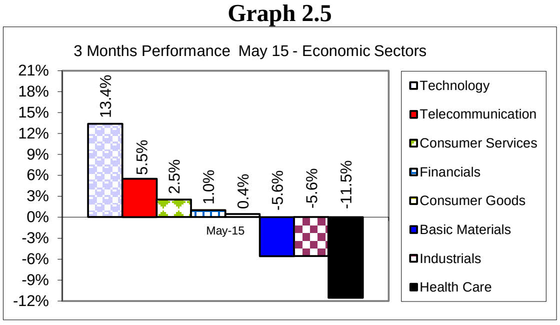
Graph 2.3



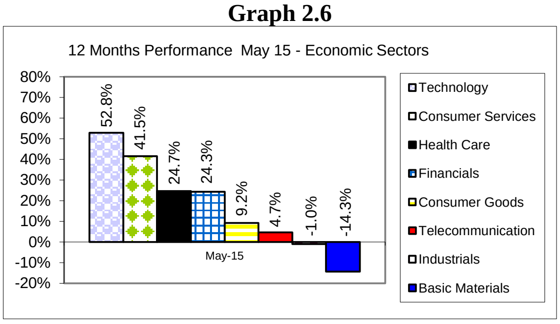
Graph 2.4



Graph 2.5



Graph 2.6



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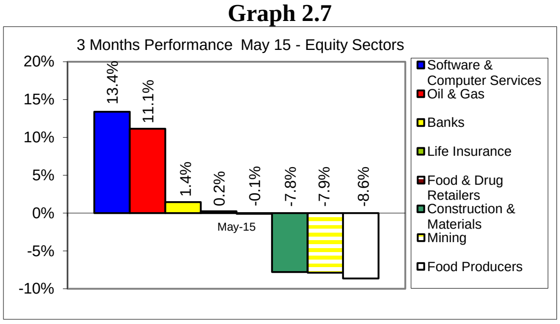
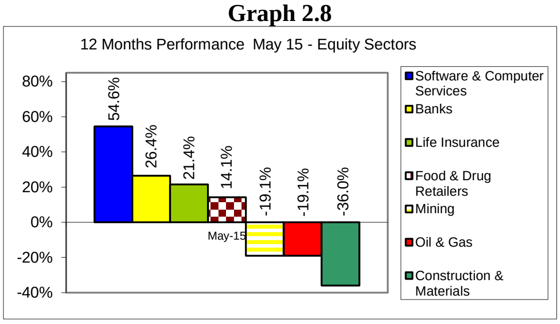
Graph 2.7



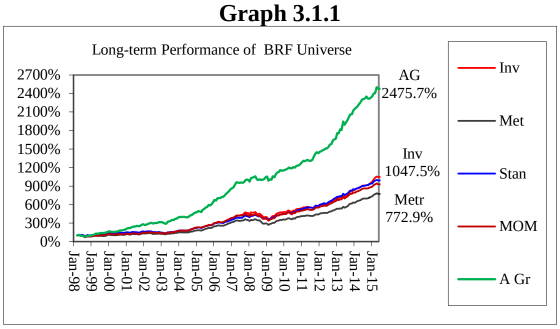
Graph 2.8



3. Portfolio Performance Analysis

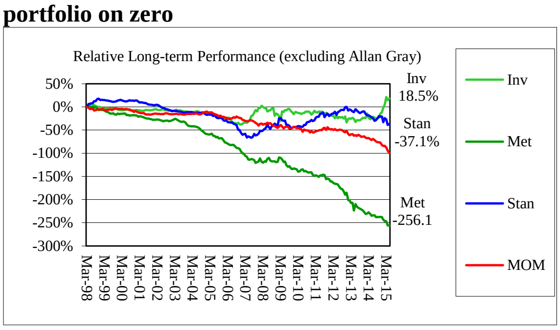
3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

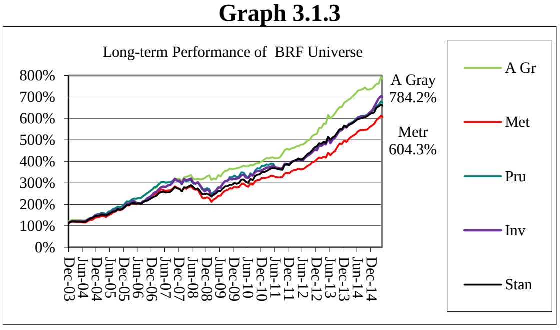


Graph 3.1.2

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

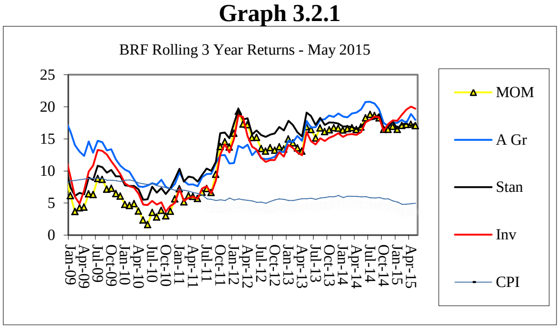


Graph 3.1.3

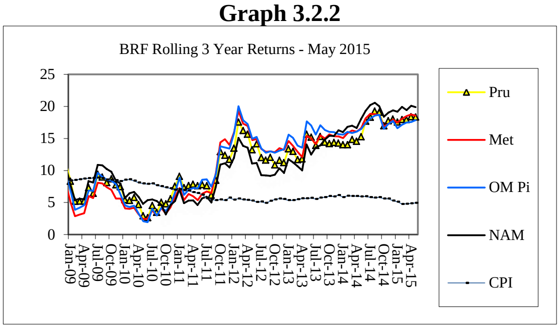


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1

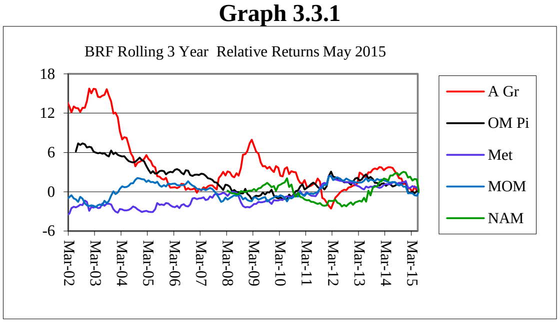


Graph 3.2.2



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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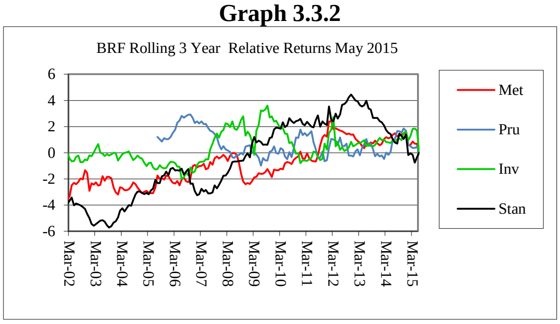
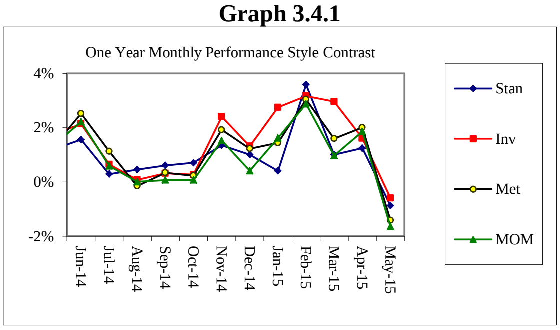
Graph 3.3.2

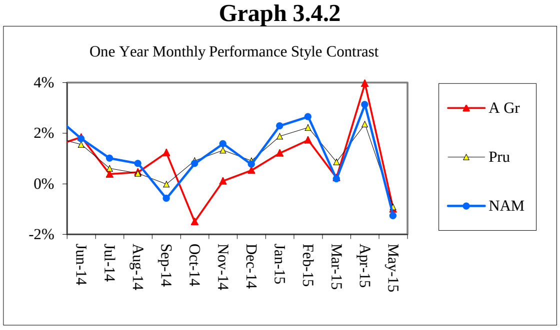


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

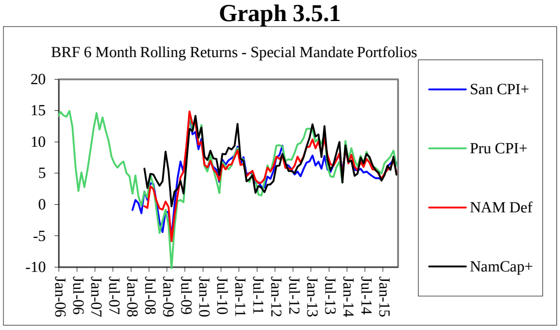


Graph 3.4.2

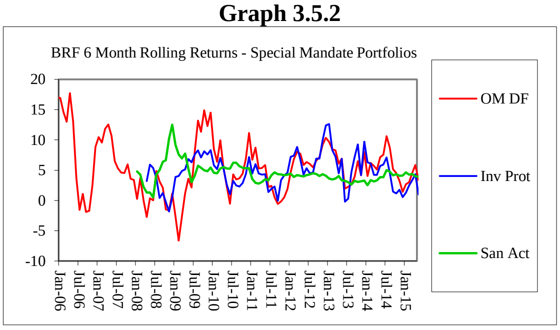


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

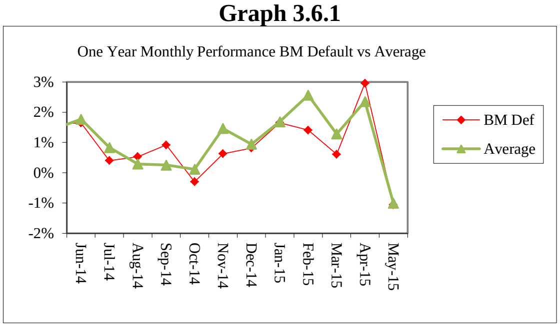


Graph 3.5.2

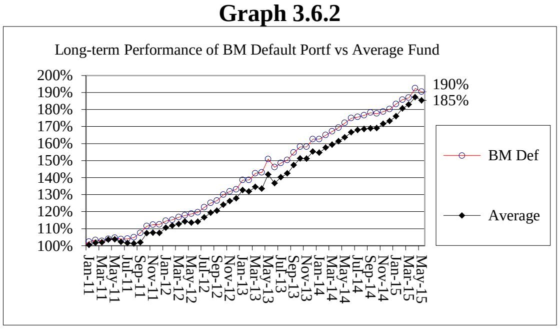


3.6 Monthly and cumulative performance of 'Benchmark Default' portfolio relative to average prudential balanced portfolio

Graph 3.6.1

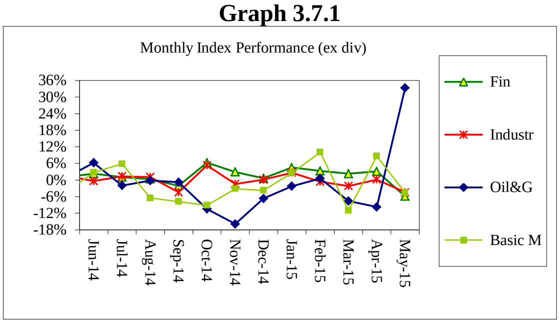


Graph 3.6.2



3.7 One year monthly performance of key indices (excluding dividends)

Graph 3.7.1



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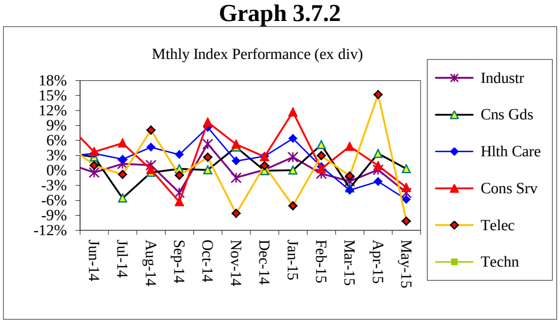
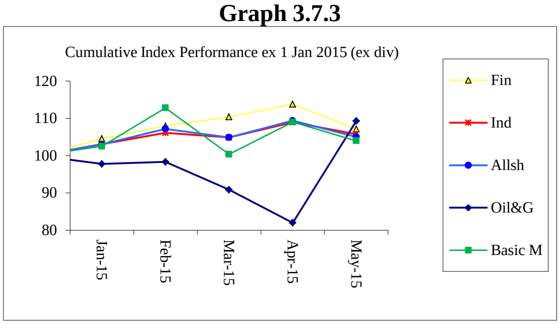
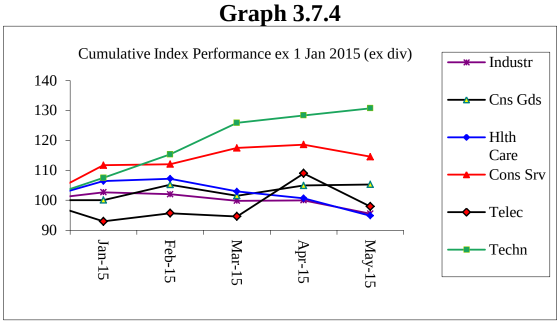
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio

Graph 1.6 shows that the average prudential balanced portfolio returned 15.4% p.a. in nominal terms, or 10.2% p.a. in real terms, over the past 5 years while the Benchmark Default portfolio returned 15.7% p.a. in nominal terms, or 10.5% p.a. in real terms. The Benchmark Default portfolio is designed to produce a less volatile performance but also lower returns than the average prudential balanced portfolios with its significantly lower equity exposure (49.8% vs. 61.8% of the average prudential balanced portfolio, as at the end of March 2015) and the lower risk it consequently entails for the investor. It should be expected to underperform the average prudential balanced portfolio at times when shares outperform other asset classes and vice versa.

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 exceeding the expected long-term goal significantly over the past 5 years.

We would in the long-term 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 exceeded noticeably. The default portfolio returned a cumulative 90.4% compared to 85.4% for the average prudential balanced portfolio over this 53 month period from January 2011 .

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 2012 to May 2015:

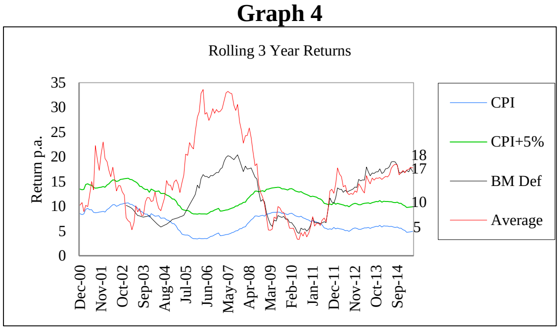
Table 4.1

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.3%	10.6%	11.5%
Best annual performance	6.4%	27.1%	25.0%
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	5.7%	17.7%	17.6%

The Benchmark Default portfolio is a more conservative investment portfolio 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.

Graph 4



Graph 4 measures the success of the Benchmark Default portfolio in achieving its long-term gross investment

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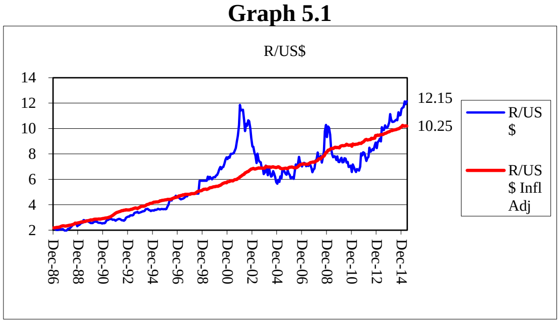
return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end May was 17.0%, the average was 17.8% vs CPI plus 5% currently on 9.9%.

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 10.25 to the US Dollar while it actually stood at 12.15 at the end of May. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

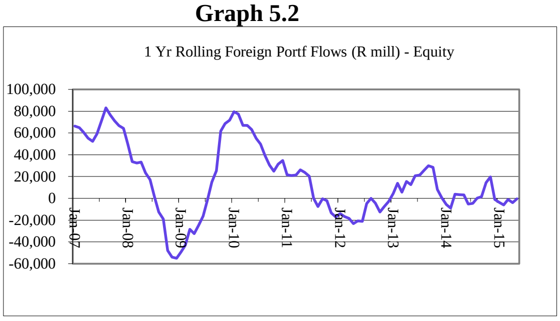
Graph 5.1



Rand supported by foreign capital inflows

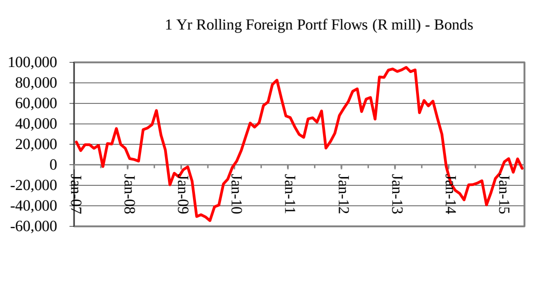
Graph 5.2 reflects a flow of capital out of South African equities on a rolling one year basis, with a net outflow of 0.4 bn on a year-on-year basis at the end of May (outflow of R 4.0 bn year-on-year to end April). The month of May experienced a net inflow of R 5.0 bn. Since the beginning of 2006, foreign net investment in equities amounts to R 186 bn (end April R 182 bn). This represents roughly 1.5% of the market capitalization of the JSE.

Graph 5.2



Graph 5.3 on a rolling one year basis reflects foreign portfolio outflows in respect of SA bonds of R 3.5 bn over the past 12 months to end of May (inflow of R 6.0 bn over the 12 months to end of April). Since the beginning of 2006, foreign net investment in bonds amounts to R 217 bn (to April just over R 218 bn). The month of May experienced a net outflow of R 0.1 bn.

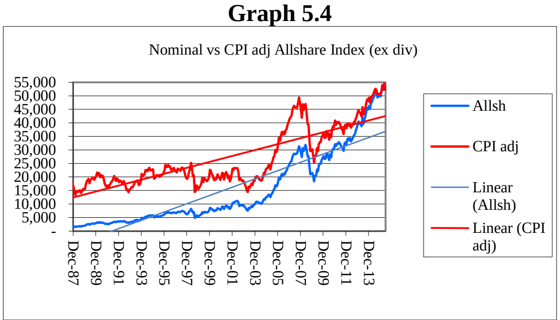
Graph 5.3



The net outflows of foreign capital from equity and fixed interest assets was R 3.9 bn for the rolling 12 months to end May 2015 (inflow of R 2.0 bn to end April 2015), compared to an outflow of R 16.4 bn for the 12 months to end May 2014 (outflow of R 30.9 bn to end of April 2014). Since the beginning of 2006, total net foreign portfolio inflows amounted to R 404 bn (April R 399 bn).

Graphs 5.4 reflects the movement of the JSE since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. In nominal terms, the JSE grew by 12.2% per year since January 1987, and this excludes dividends of 3%. Namibian inflation over this period of just over 28 years was 8.4% per year. This is equivalent to a growth in real terms of 3.8% p.a. over this period, excluding dividends, or around 7% including dividends.

Graph 5.4



Graph 5.5 reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 7.5% per annum, over this period of just over 28 years. US inflation over this period was 2.7%. This is equivalent to a growth in real terms of 4.8% p.a. over this period, excluding dividends.

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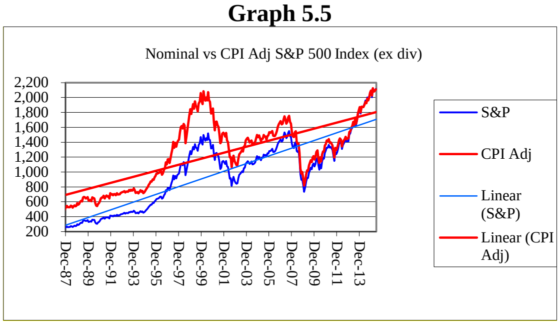
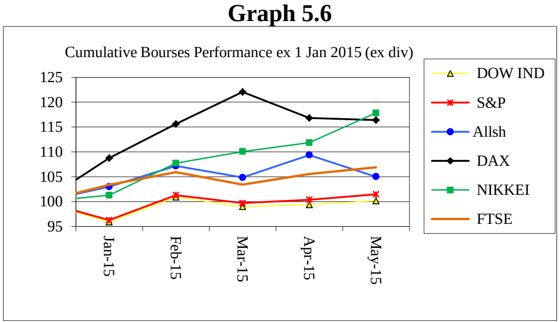
Graph 5.5



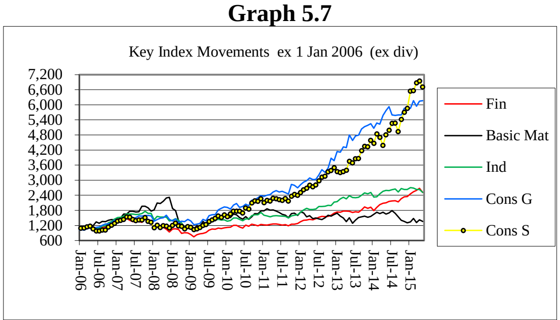
Graph 5.6 provides an interesting overview of some of the major global share indices, showing up the NIKKEI and the DAX as the top performing share indices.

Graph 5.6



Graph 5.7 provides an 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. Annualised returns for these indices since the beginning of 2006 were: Consumer Services: 22.4%; Consumer Goods 21.3%; Financials 10.3%; Industrials 10.3%; and Basic Materials 3.3%.

Graph 5.7



6. Be on the winning side and keep out of the cross fire by Tilman Friedrich

Life remains interesting as the banal saying goes. No too long ago we first heard about the 'peak oil' theory and were made to believe that from now on the supply of oil will start to decline. This was of course supported with scientific analyses of the largest oil producing areas in the world. On 14 June 2015, Moneyweb posted an article 'the world is facing its longest oil glut in at least 3 decades' vividly underpinned with colourful graphs, of course. Just using another source, the picture looks quite different. 'Energy Briefing: Global Crude Oil Demand & Supply' by Yardeni Research, Inc shows that there are different measures that produce different results. Measuring demand and supply on a 12 month average, rather than a monthly basis, as the latter report does, is a more convincing reflection. This does not really support the story of a huge oil glut. In fact it shows that there is still a small short supply on a 12 month average basis, given though that the gap between demand and supply has declined. A few years ago global media focused our attention on the life threatening ozone hole. Have you heard anything about this phenomenon recently? The last I heard, as recent as last week, is that the ozone hole has virtually disappeared. Nowadays the topic everyone talks about is climate change, caused by carbon emissions, and of course it is once again threatening the existence of mankind! I really became deeply troubled when I read this headline 'A child borne today may live to see humanity's end'. My goodness I thought to myself, I am O.K. but what about my grandchildren? Yes, the world is evidently experiencing climate change, just think how mild our current winter has been, so it can only go to support the apocalyptic prognoses that we are approaching the end of mankind. So do not worry to save up for retirement because you will not live to enjoy the fruit of your hard work!? Well, what can we believe? Are we experiencing a media supported global strategy to unsettle mankind? Why do we experience an ongoing war all around the Mediterranean? On the one side we are witnessing ongoing wars waged for the sake of a better world, of good against evil of course - whichever side you take - that uproots millions of people and exposes them to untold hardship. At the same time we are witnessing European countries buckling under the siege of refugees uprooted in the war torn Middle East. Just a few years ago all these countries were peaceful. But in the eyes of some beholders, this was not the point. The point was that these did not have a democratic government, were ruled by oppressors and possessed weapons of mass destruction. Are the oppressed and democracy deprived better off today, would you want to be one of them? What has happened to our morals, if we support wars for the purpose of installing democracy, if we drag leaders of some countries to the ICC for crimes against humanity while others of much greater relevance get away unscathed?

Now what does this have to do with investing and financial markets? Well as I pointed out before, one has to try understanding the global context to draw conclusions for your personal situation and how you should invest. Assuming that we are witnessing a global propaganda war where our media are used as a pawn to achieve global strategic goals, we would come to the conclusion that we should consume news and information with great circumspection. We should try to read the story behind the story and what it is likely to aim at. With this perspective, there is currently really only one global player that has the means and the will to advance his global strategic objectives and his interests. What would you do if you were in this position? You would obviously try to secure this position in every way and every respect and your purpose would be to advance your wellbeing above that of anybody else. What would be your biggest threats that could prevent you from achieving your objective? On the macro level, it would evidently be countries that want to, and potentially have the means to challenge you and to break the shackles of global hegemony. On the micro level it's the threat of being deprived of free access to resources you need, the threat of business competitors outsmarting your own businesses, while at grass roots level it could be a strong globally popular philosophy that gets the masses on the move against your interests.

Taking a longer term view and following the foregoing argumentation, the investor would want to be on the winning side and should try to keep out of the 'cross fire'. Being on the winning side, at least for the foreseeable future, is a 'no brainer' and requires no further elucidation. For the shorter term, just choose the right asset classes. In this regard be cautioned by the article 'Radishes, onions and the stupidity of debt' by Toni Sagami in this link…. The wisdom of not putting all your eggs in one basket, of course, remains true. Spread your risk and try to keep out of the 'cross fire'. Here you may wish to refer to the article 'Stand back, China's bubble will burst' by Clive Crook in this link.

For the longer term, keeping out of the cross fire means that one should invest in well managed, smart economies that are of limited global strategic relevance. Let Namibia be one of these smart economies that manages to keep out of the cross fire. For the longer term, the whole Eurasian continent is likely to be in the cross fire, pity Europe with its demographic apocalypse that adds to its woes.

In the short to medium term we will see no major changes in monetary policy probably until early to middle of 2016. We will witness market wobbles as seen recently where a mere faint hint of the US Fed considering a rate hike already set market into a tail spin. We should see a gradual value rebalancing between asset classes as the interest rate environment will gradually be normalised. As a result equity markets are likely to experience only pedestrian performance for years to come, but one should at least expect low real returns as opposed to fixed interest investments that will be shunned until rates have reached normal levels once again.

On this basis we do not expect any major swings in investment market for the next 2 years plus, given no political upheavals impacting investment markets.

Our investment view remains unchanged

The local investor should invest in equity and property in preference to fixed interest assets, talking only about conventional asset classes. Stock picking should prove to make the difference in returns and will be a prerequisite for out-performance of a portfolio. Turn down your return expectations, focus on inflation and aim to outperform inflation rather than aspiring for high absolute returns as these will not be achievable without taking significant risks.

With the expected upswing in consumer sentiment over the next year or two, is likely to be preceded by an upswing in commodities and to be followed closely by and upswing in financials. A soft Rand and a depressed local economy suggest that the investor should continue to diversify offshore. Lowly geared Rand hedge companies should benefit from increasing interest rates and improving consumer sentiment in developed economies.

7. Important notice and disclaimer