BENCHTEST

Volume 4, No. 8, August 2008

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 August 2008

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 now also available on our website at www.rfsol.com.na.

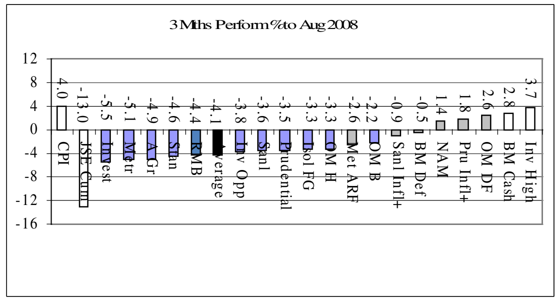
1. Review of Portfolio Performance

In August the average prudential balanced portfolio returned 1.79% (July minus 1.3%). Best and worst performance **for the month** was delivered by Old Mutual (2.63%) and Metropolitan (0.72%), respectively. A superficial analysis of these managers' performance does not explain Metropolitan's underperformance satisfactorily and would thus require further investigation. Old Mutual added some value through a high property and lower equity exposure, as well as a favourable spread across the various equity sectors. Its current asset allocation should add some out performance in our view under prevailing conditions.

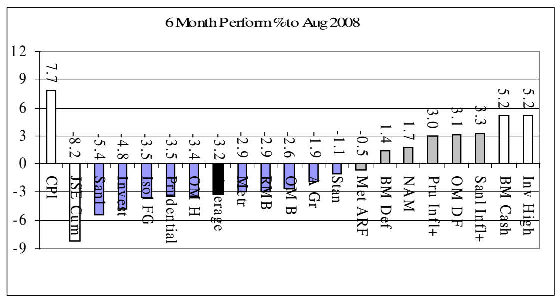
Graphs 1 to 7 reflect the performance for periods from 3 months to 10 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no colour bars), the average of prudential balanced portfolios (black bar) and the CPI (red checked bar). Benchmark investors should take note of the performance of the default portfolio (red and grey bar), which represents a combination of Prudential Inflation Plus and Metropolitan Absolute Return. Here is the legend to the abbreviations reflected on the graphs:

Benchmarks	
Namibian Cons Price Index	CPI Cum
JSE Allshare Index	JSE Cum
Benchmark Default Portfolio	BM Def
Average Portfolio (prudential, balanced)	Aver
Special Mandate Portfolios	
Sanlam Cash	BM Cash (no colour)
Investec High Income (IBA)	Inv High (no colour)
Metropolitan Absolute Return	Metr ARF (grey)
Prudential Inflation Plus	Pru Infl+ (grey)
Old Mutual Dynamic Floor	OM DF (grey)
Sanlam Inflation Plus	Sanl Infl+ (grey)
Namibia Asset Management	NAM (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Invest (blue)
Investment Solutions Focused Growth (multi manager)	Isol FG (blue)
Prudential Managed	Prudential (blue)
Metropolitan Managed	Metr (blue)
Old Mutual Profile Balanced	OM B (blue)
Old Mutual Profile Growth	OM H (blue)
RMB Managed	RMB (blue)
Sanlam Managed	Sanl (blue)
Stanlib Managed	Stan (blue)

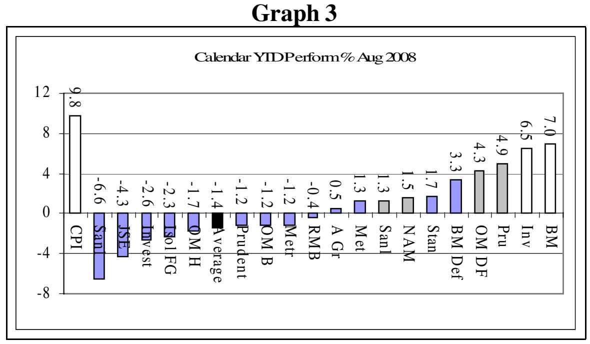
Graph 1



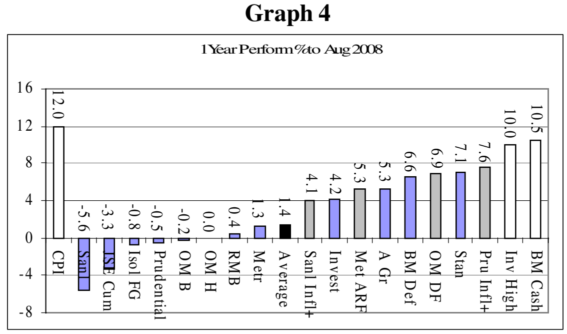
Graph 2



Graph 3



Graph 4



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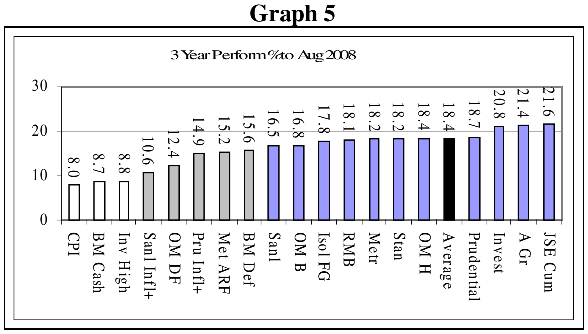
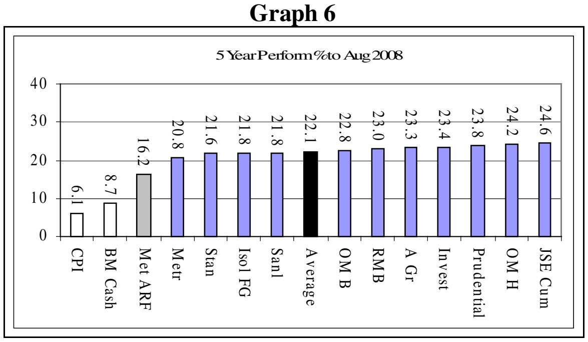
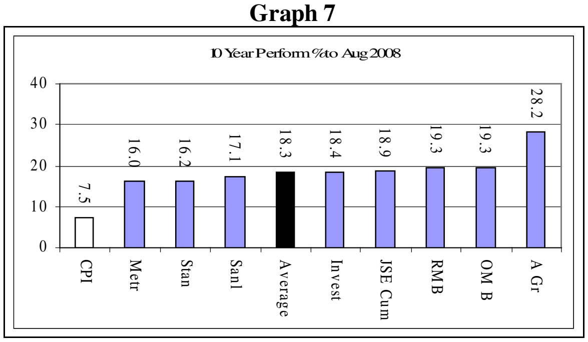
Graph 5



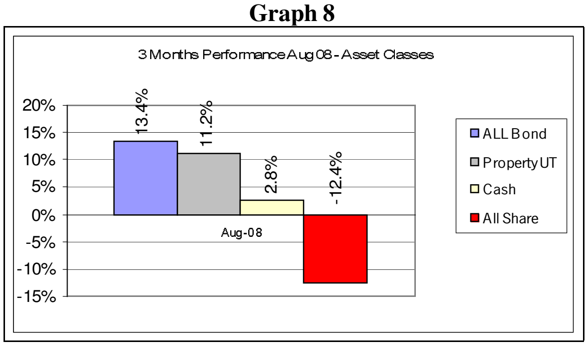
Graph 6



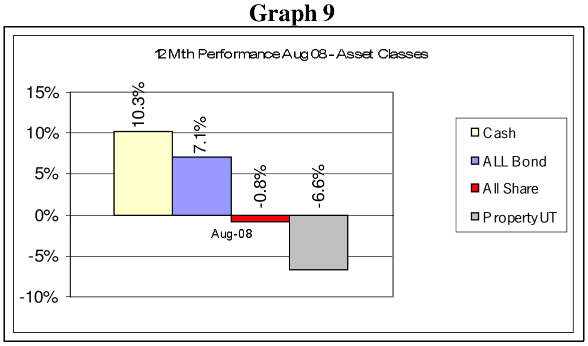
Graph 7



Graph 8

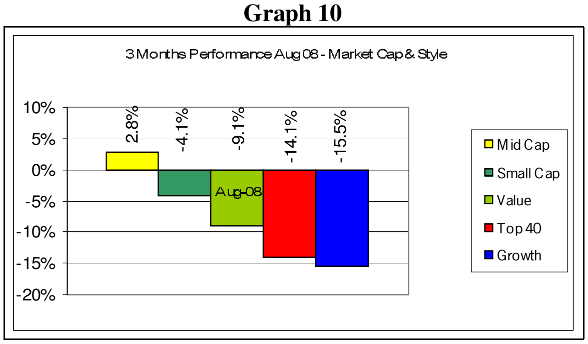


Graph 9



Graph 10 and **graph 11** reflect a significant change in rankings, over 3 and 12 months, of type of company and market capitalization, occasioned by the prevailing volatility. Since our large caps are predominantly resource companies, the decline in the resources indices is reason for the under performance of our large caps.

Graph 10



2. Review of Performance of Key Indices (index performance by courtesy from pointBreak/Deutsche Securities)

Graph 8 and **graph 9** this time show major changes in the order of asset classes in terms of performance, including dividends, over the quarter and the 12 months. Property and bonds have further moved up the ranks from 12 months to latest quarter as the result of interest rates holding firm with an expectation of a decline in the medium term. The Allshare index was the worst performer for the latest quarter and second worst performer for the 12 months.

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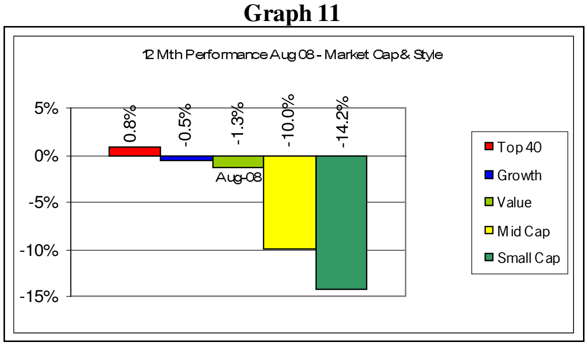
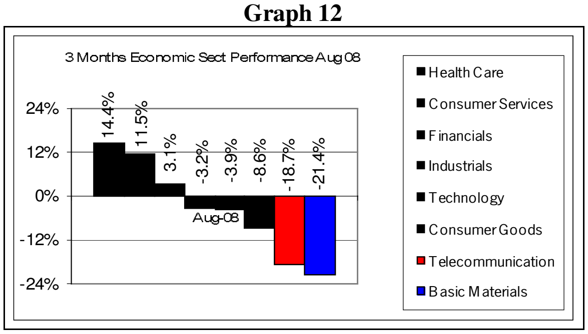
Graph 11

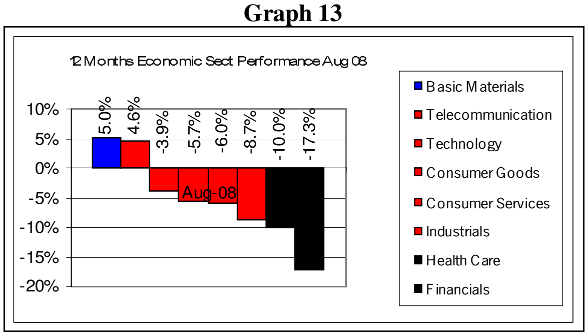


Graph 12 and **graph 13** depict the performance of the main equity sectors. Evidently some equity sectors are holding their own and have out performed cash by a wide margin and even the best performing asset class, for the quarter. Evidently too, Basic Materials have moved from top position for the year to bottom of the log for the quarter.

Graph 12

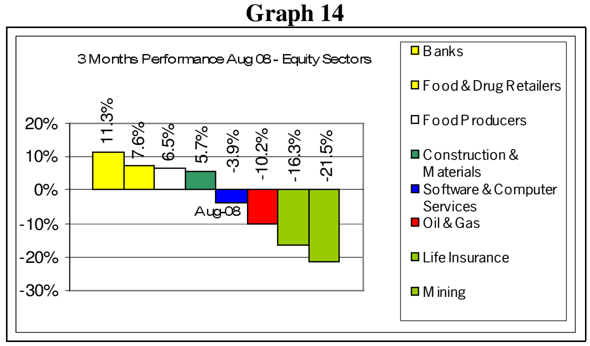


Graph 13

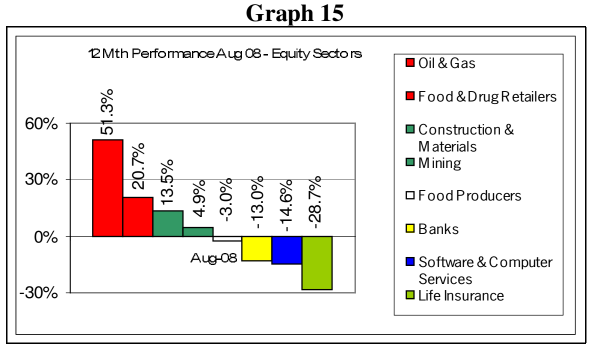


Drilling down one level into the main equity sectors, **graph 14** and **graph 15** show that resources have lost steam over the more recent past in sympathy with the decline in the oil price. The construction sector has run out of steam now as well, still producing returns for the quarter of 5.7% and a 13.5% over the past 12 months.

Graph 14



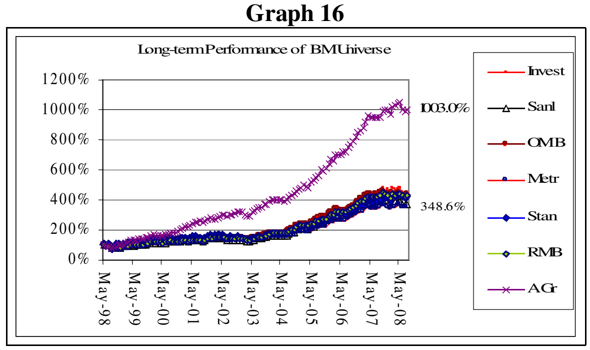
Graph 15



3. Portfolio Performance Analysis

Namibian prudential balanced portfolios essentially only acquired their own identity in 1998 when changes were brought about by regulation 28. **Graph 16** and **graph 17** reflect cumulative performance of these portfolios since April 1998 and since January 2003, respectively. The conclusions should be self evident. Take note of the decline in returns since May 2008.

Graph 16



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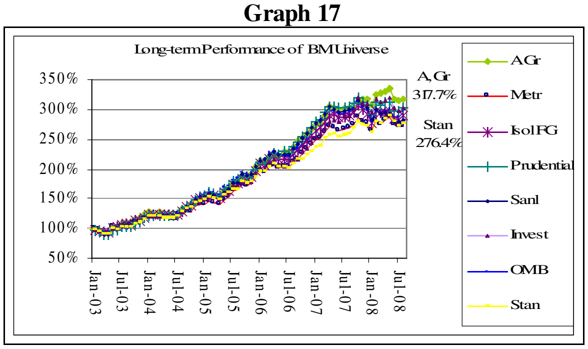
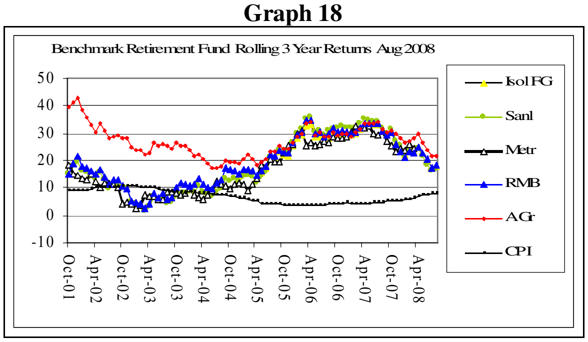
Graph 17

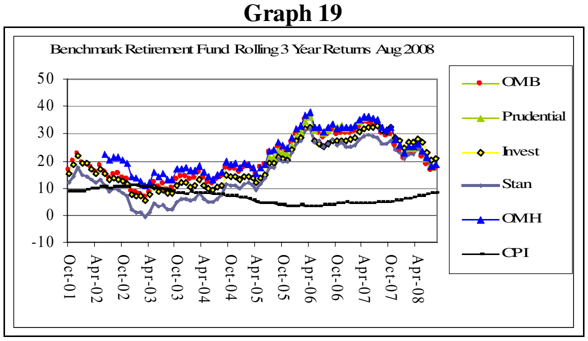


Graphs 18 and graph 19 reflect rolling 3 year returns since October 1998. For long-term projection and planning purposes the general assumption is that prudential balanced portfolios should outperform the CPI by between 3% and 5%, which has over this period only been achieved throughout by Allan Gay. Evidently the gap is closing but is still in the region of between 8% and 12%.

Graph 18

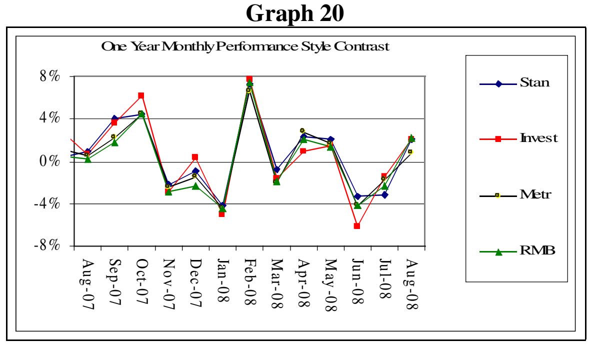


Graph 19

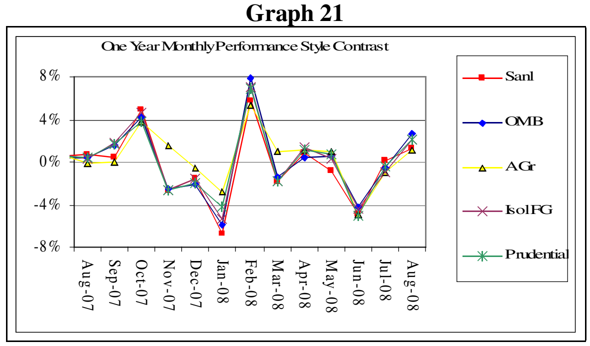


Graph 20 and **graph 21** depict the monthly performance of the prudential balanced portfolios in this survey. It shows that managers do generally perform very similarly but it also affords the opportunity to identify odd trends for further investigation and for drawing conclusions about expected future performance and historic skills of the managers. Allan Gray appears to be back on a more familiar trend of cutting the peaks and troughs.

Graph 20

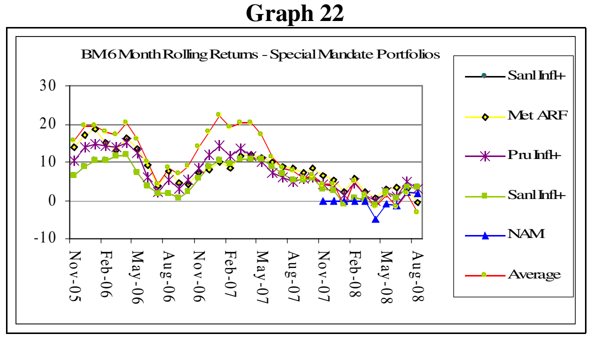


Graph 21



Graph 22 puts some focus on the 'special mandate portfolios' in relation to the average prudential balanced portfolio, in terms of 6 month rolling returns. **Graph 23** depicts the monthly performance of the Benchmark default portfolio in relation to the average prudential balanced portfolio. These graphs should give the investor a pretty good feel for what he can expect in terms of performance volatility and relative performance over the long term from the 'special mandate portfolios' vis-à-vis the average prudential balanced portfolio. In essence these portfolios have around 20% lower equity exposure for the benefit of less volatile but in the long term, in theory, around 2% lower returns.

Graph 22



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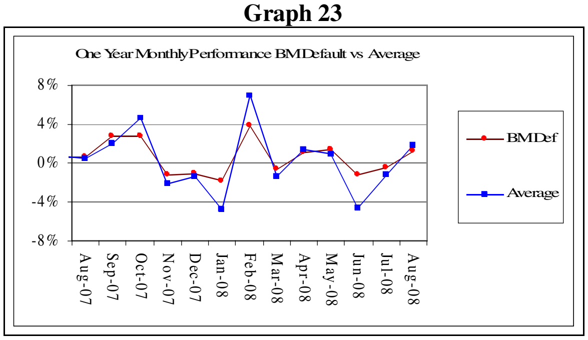
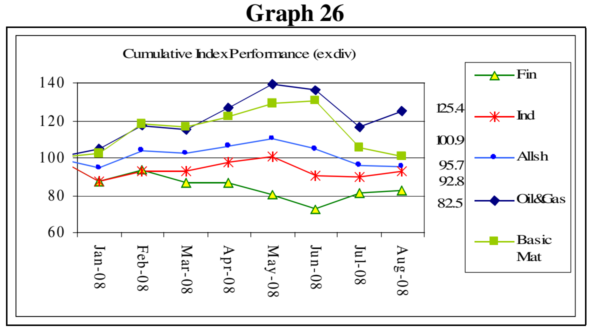
Graph 23

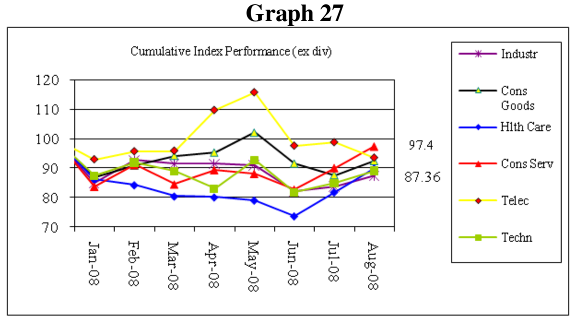


Graph 26

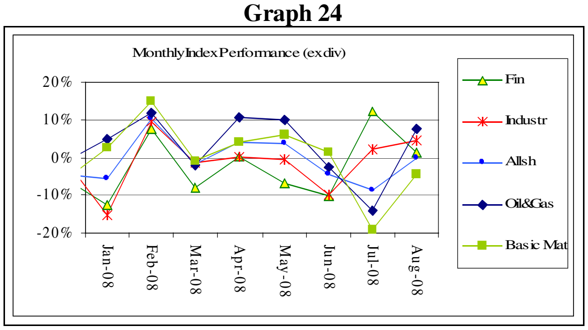


Graph 24 and **graph 25** afford the investor the opportunity to compare managers' monthly performance (as depicted in graph 20 and graph 21) against various equity sectors and to draw his conclusions regarding a manager's investment style and philosophy. **Graph 26** and **graph 27** serve a similar purpose, but with regard to cumulative performance since January 2008.

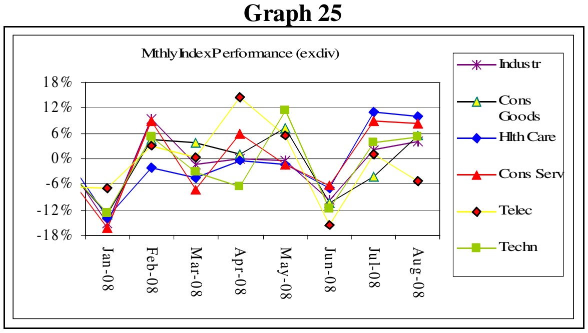
Graph 27



Graph 24



Graph 25



4. A Contrarian Preview Of The Next 12 Months

For the past few years, the oil price has been the defining factor in the global economy in our view and our expectations are significantly dependent on how it will behave going forward. We side with those commentators that believe the oil price has been driven by speculation. Evidently, speculation was pretty much unchecked and probably the result of excessive legislative leeway. In the US all of a sudden now everyone seems to realizes this and there is consensus that this must be checked. Now there is the looming threat of new accounting conventions being formulated by the FASB with regard to hedge funds. Interestingly, lobbying by banks has apparently retarded the implementation thereof. So banks have been given a bit of a reprieve to get their house in order for bringing highly geared hedge fund onto their balance sheets, but of course, at the moment they can't really afford to! Will they have to dispose of their prime assets to reduce their gearing to more acceptable levels now, and if so how will this impact on the values of such assets? Too no avail for Lehmann brothers though, and how many more to follow?

Should the oil price enter a new era of lower levels as we now believe it would, it should produce a stronger US

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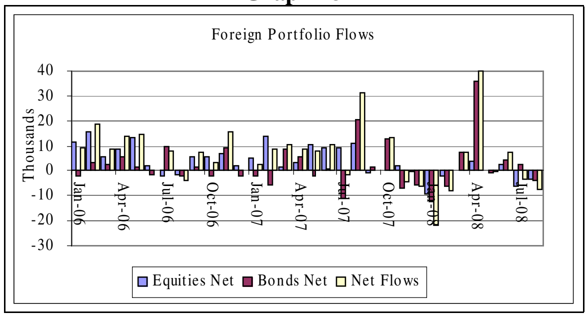
Dollar which in turn will result in a weaker Rand/Namibia Dollar. The question is where it will find a comfortable level. Having strengthened from US$ 88 to US$ 100 over the past few days, we believe at that level, there is still a huge flood of money seeking investment, which cannot easily be absorbed by global financial markets without continuing to fuel bubbles all over, causing lots of uncertainty and volatility. It seems this money avalanche is propping up the US Dollar and keeping interest rates down in the US at this stage. Oil producers are losing at lot of their gains in the US again. It would seem to us that the global financial system has to be re-engineered as it was clearly incapable of dealing with this situation. Speculation is one thing and can be checked but does it make sense to have all global trade denominated in one currency? It will take a long time before all the damage and harm done by this crisis has worked itself out of the system and one can only hope that some positive lessons will flow from this debacle.

It will, still take a long time before a lower oil price will start impacting positively on rising price levels globally. Inflation, and hence higher interest rates, is likely to be around for quite some time. The consumer, particularly in the US, will still be under pressure for a while and this should put a lid on global demand for resources, as we have started to experience. This should lead to greater stability and predictability to return to global financial markets.

The global financial crisis and its knock-on effects, including the impact on sentiment, are still very much with us and will be felt for some time to come. The US Federal Reserve lending rate is currently at 2% and the next move in interest rates will be upward rather than any further reduction in view of inflation picking up pace in the US. This should strengthen the US Dollar and indicates that it is probably around its trough at present. Higher US interest rates should result in a weaker Rand/Namibia Dollar unless it coincides with further rate increases locally, the likelihood of which is diminishing.

In South Africa we have seen equity markets, and other asset classes for that matter having been boosted by massive inflow of foreign capital which also lent support to the Rand, despite SA's pretty significant current account deficit. **Graph 28** shows that the interest of foreign investors in local equities has faded away. Evidently the flow into bonds is highly volatile, but is purely a function of interest rate arbitrage and produces high exchange rate volatility.

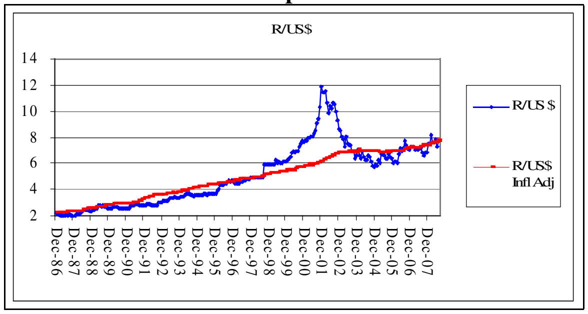
Graph 28



Graph 29 indicates that on the basis of fundamentals, the Rand was overvalued in US$ terms since 2003, probably driven by high commodity prices and high foreign portfolio flows chasing primarily our resources stocks. Currently the Rand stands at around 7.68, representing a slight overvaluation against an inflation adjusted 7.75 per **graph 29**. At the current inflation differential between the US and SA, i.e. 4% vs 12%, the Rand should weaken slightly from its current level to 7.94 by the end of the year.

We would expect inflation in SA and Namibia to outpace inflation in the developed economies which will cause the Rand to depreciate in the medium to long term.

Graph 29



Graph 30 shows clearly to what extent the South African share market had departed from the US market, despite the recent correction, far off its US peer. Does this represent one of the bubbles that are waiting to burst or does it simply represent one asset category that has moved towards price equilibrium more instantaneously? Many analysts do not believe this to be a bubble though and we would agree, provided we see a stable oil price going forward. Considering that resources are the main culprit for the major departure since middle of 2004, the other indices,

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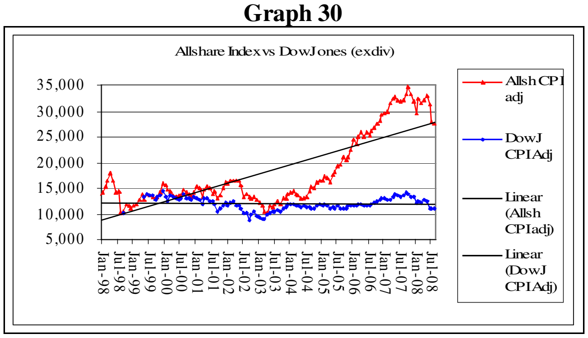
and Financials in particular, are historically seen at reasonable levels.

Graph 30



5. Conclusion

In our opinion, the higher inflation era we have entered is here to stay for quite some time and more so in developing countries. We believe that interest rates are likely to remain fairly stable from here on with some upward potential still. We expect the higher local inflation rate and any reduction in interest rates to result in ongoing slow depreciation of the Rand. We also believe that high volatility in markets will remain for the time being although we see this starting to subside. Due to higher inflation and interest rates, the pressure on consumers will remain. We do not expect the oil price to resume its trajectory, but rather to remain stable with the potential for a further decline. Many measures that have and are still being taken to replace oil with other energy sources will gradually reduce consumption and demand over the next couple of years. In the mean time there will be more pain than pleasure in the markets. Under these circumstances and taking a long-term view such as the typical pension fund should take, we would invest in real assets such as property, deep value and inflation hedged and Rand hedged shares.

Cash currently hardly produces any real return, in Namibia at least, and has lost much of its attraction. In view of our expectation for inflation to remain at its recently found levels, with a slight risk of it still trending upward and fairly stable interest rates going forward, bonds in our view start becoming more attractive. Property has been punished over the past year but should do well as an inflation hedge, given that it may still experience a short-term negative impact should interest rates increase. Weighing up foreign markets against local markets, we expect our markets to bear more negative potential than foreign markets, excepting commodities that are likely to track the movement in the oil price and are thus likely to be under pressure. Developing countries should experience the increase in energy and food prices more negatively than developed countries where in the latter case, a smaller portion of disposable income is applied to consumption. A logical consequence of these expectations is that one should be fully invested offshore. Locally, these expectations would favour selective high yielding equity, property (industrial) and bonds.

6. 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.