BENCHTEST

Volume 5, No. 6, June 2009

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 JUNE 2009

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.

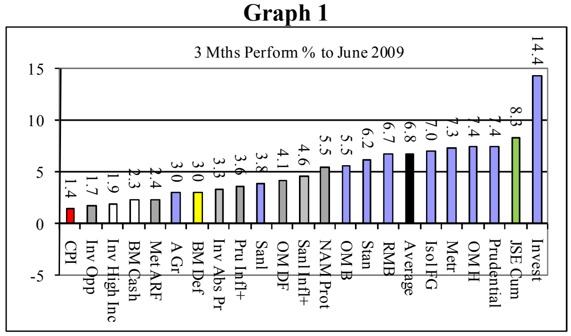
1. Review of Portfolio Performance

In **June** the **average prudential balanced portfolio** returned **minus 0.25%** (4.69% in May). Best and worst performance **for the month** was delivered by Investec (0.71%) and Allan Gray (minus 1.71%), respectively. Analysing the performance of these two managers relative to the average manager, Allan Gray should have underperformed the average manager by 0.48%, as a result of being roughly 10% overweight consumer goods and 6% underweight financials but diluted down to 0.25% through a 9% underweight local equities and loosing another 0.5% through an 11% overweight to offshore assets. Again, Allan Gray produces a significant projection error of 0.7% for the month, presumed to be the result of its stock picking being quite different from the average portfolio. Investec lost 0.75% through a 4.5% underweight Oil & Gas which was made good through its 7% underweight Basic Materials. It added 0.9% through its 10% overweight Industrials and Consumers.

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), 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 represents a combination of Prudential Namibia Inflation Plus and Metropolitan Namibia Absolute Return. Below is the legend to the abbreviations reflected on the graphs:

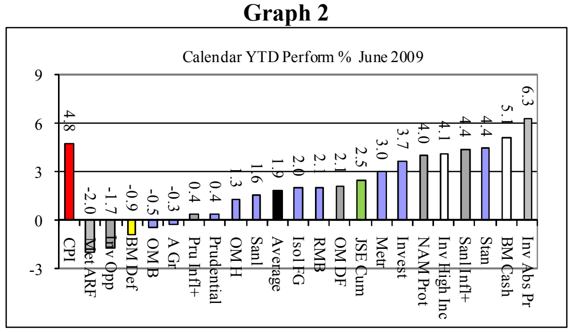
Benchmarks	
Namibian Consumer Price Index	CPI Cum (red)
JSE Allshare Index	JSE Cum (green)
Benchmark Default Portfolio	BM Def (yellow)
Average Portfolio (prudential, balanced)	Aver (black)
Special Mandate Portfolios	
Sanlam Cash	BM Cash (no colour)
Investec High Income (interest bearing assets)	Inv High (no colour)
Investec Absolute Protector	Inv Abs Pr (grey)
Investec Opportunity Fund	Inv Opp (grey)
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 Prot (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Invest (blue)
Investment Solutions Balanced Growth, prev. 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

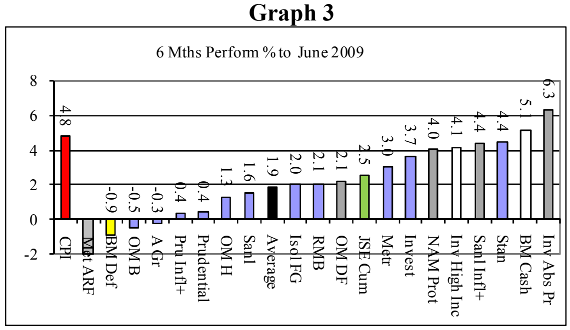


Note: The apparent out performance by Investec is not a true reflection and results from the correction of significantly understated performance in March, corrected in April. True performance for this quarter is 11.6%.

Graph 2



Graph 3



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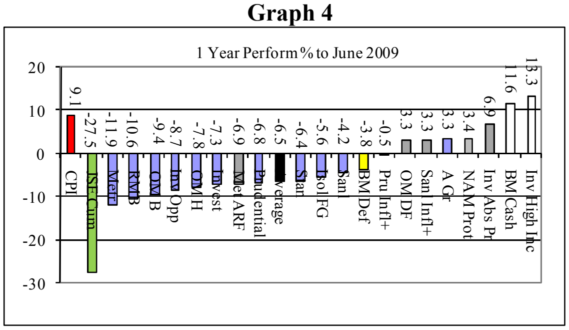
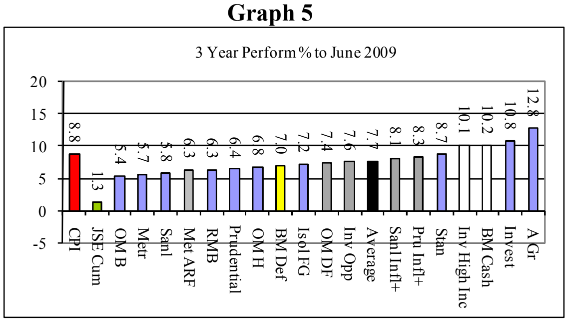
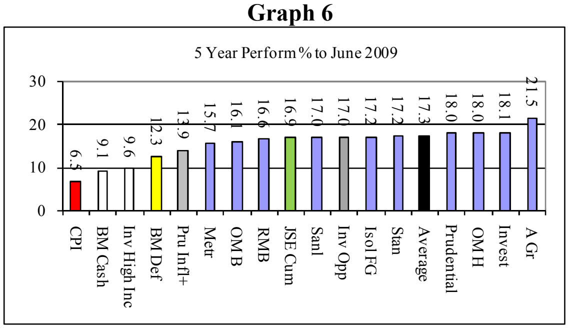
Graph 4



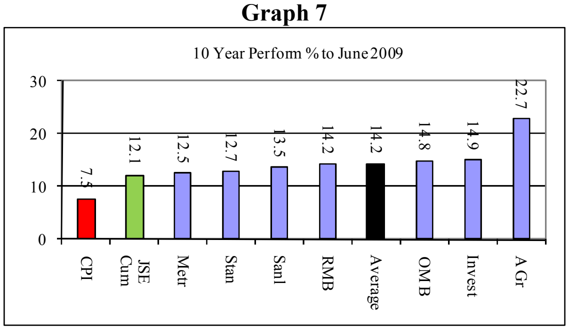
Graph 5



Graph 6

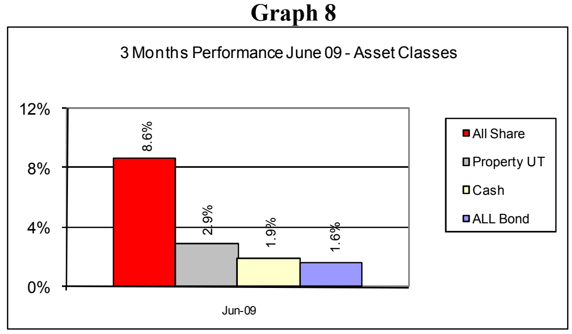


Graph 7

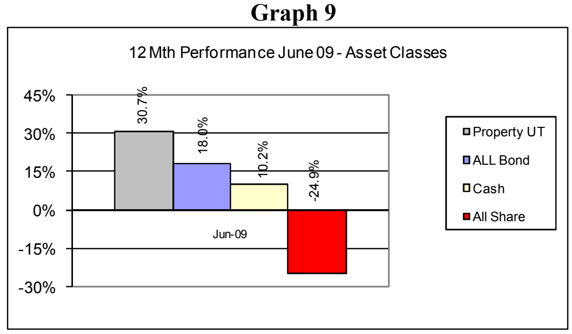


2. **Performance of Key Indices** (index performance by courtesy from pointBreak/Deutsche Securities)

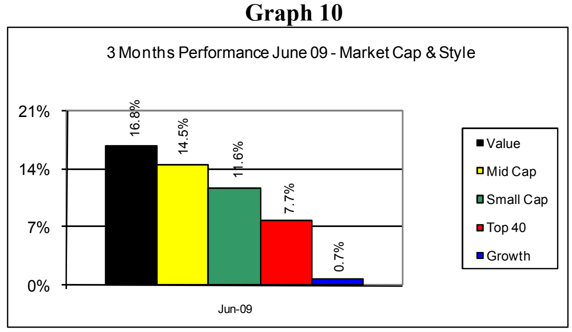
Graph 8



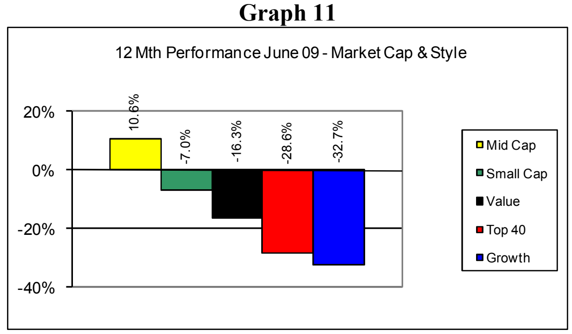
Graph 9



Graph 10



Graph 11



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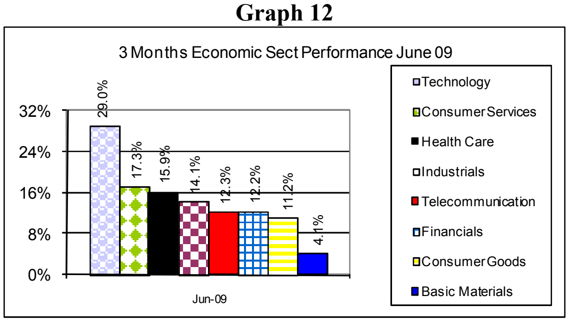
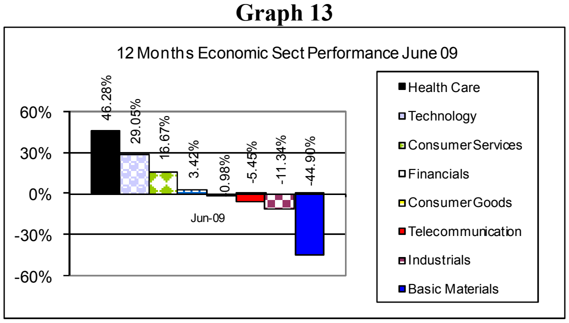
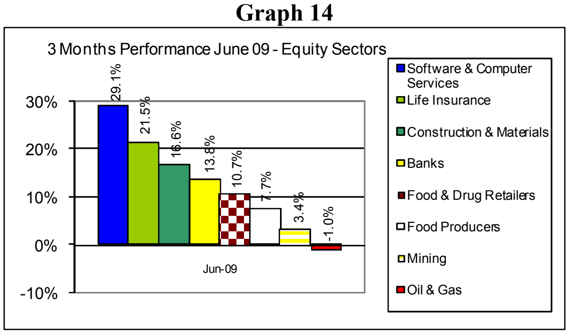
Graph 12



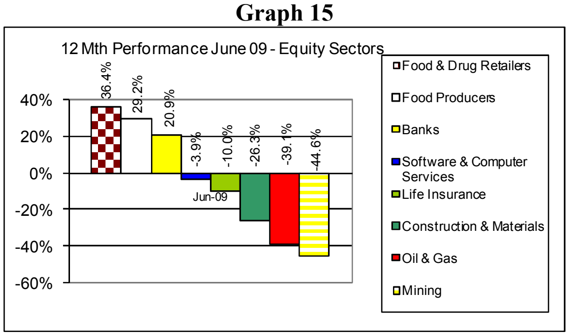
Graph 13



Graph 14



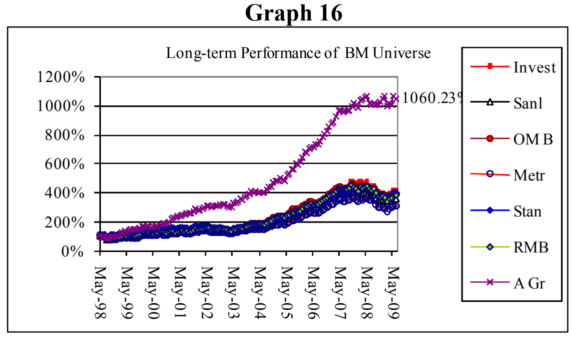
Graph 15



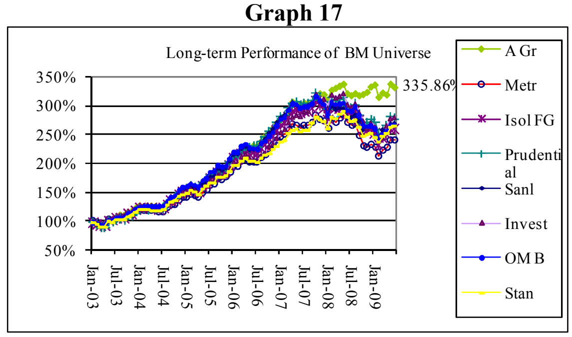
3. Portfolio Performance Analysis

3.1. Cumulative performance of prudential balanced portfolios

Graph 16

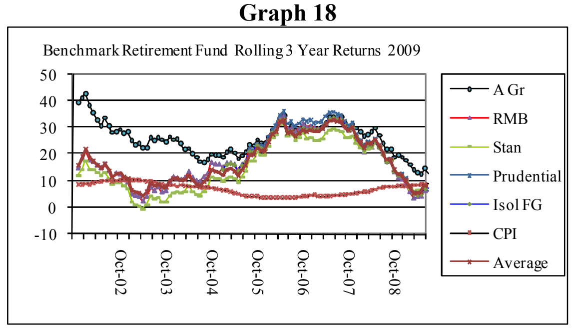


Graph 17

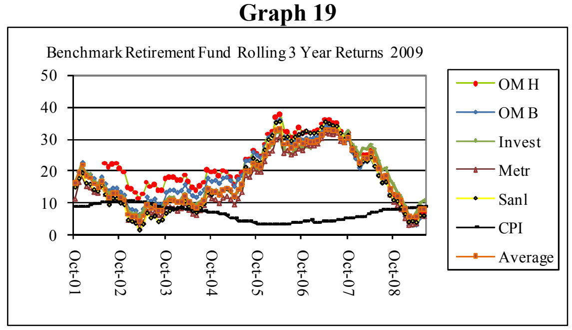


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 18



Graph 19



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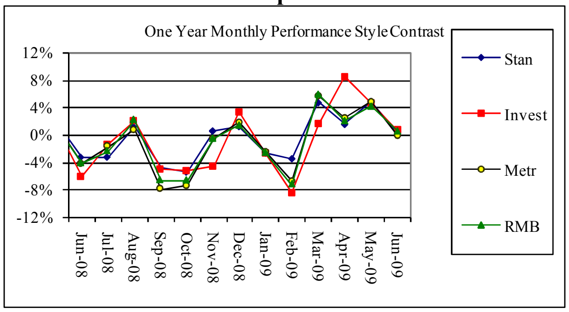
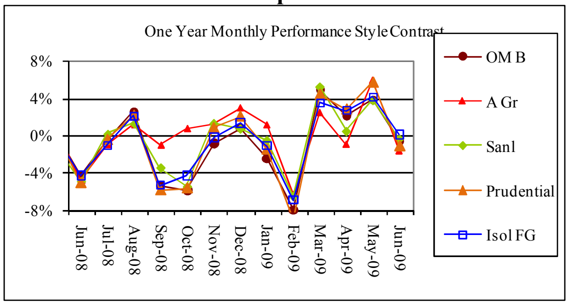
3.3. Monthly performance of prudential balanced portfolios

Graph 20

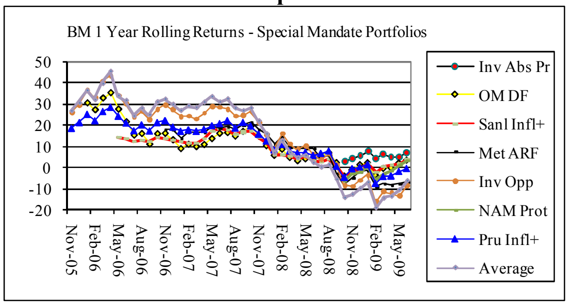


Graph 21



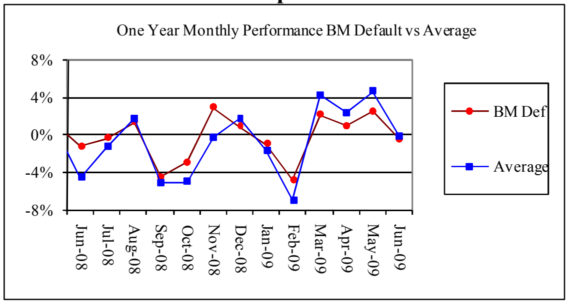
3.4. 6-month rolling returns of 'special mandate' portfolios

Graph 22



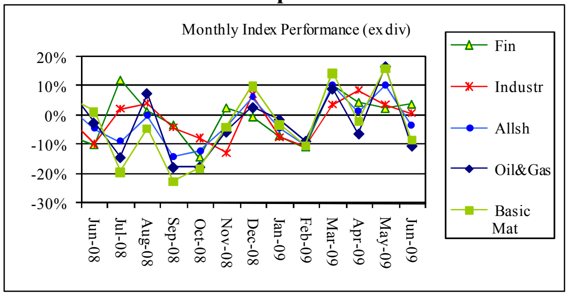
3.5 Monthly performance of 'Default' portfolio relative to average prudential balanced portfolio

Graph 23

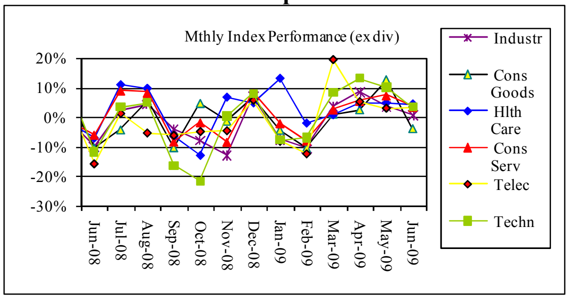


3.6 Monthly and one year cumulative performance of key indices (excluding dividends)

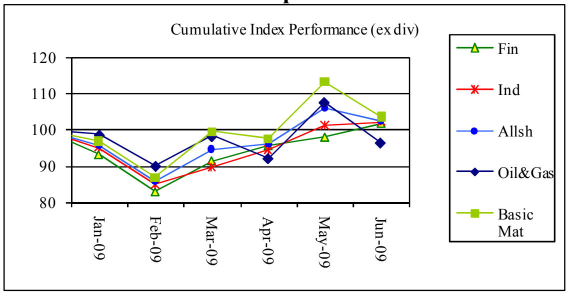
Graph 24



Graph 25



Graph 26



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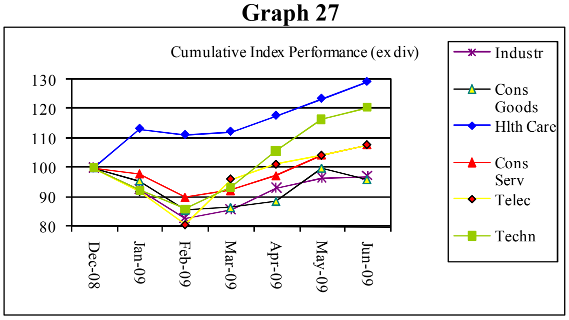
Graph 27



4. A Contrarian Preview Of The Next 12 Months

Most investors will be asking how the current financial crisis will evolve over the next year and what investment decisions need to be taken in anticipation of these developments. We prefer to take an unfounded, positive view and to assume that the coordinated global approach to address this crisis will produce positive results, at least in the medium term. Certainly the measures taken have prevented abject panic and effectively underpinned investor confidence. The huge amounts that have been allocated to address the global financial crisis, are a concern though. We would expect these creating yet unknown stresses in the global financial system, the consequences of which cannot be foreseen yet but are bound to be severe.

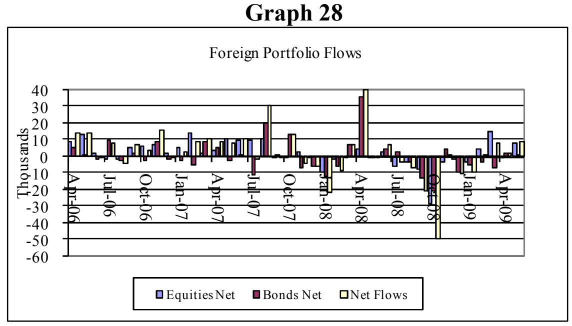
Setting a long-term investment horizon, we have thus moved back into the prudential balanced portfolios at the end of April 2009 in the belief that markets have corrected and should be around or past the trough. Those invested in the Benchmark Default Portfolio might wish to reconsider their position now. Graph 5 shows that the average prudential balanced portfolio returned 17.3% in nominal terms, or 10.8% in real terms, over the past 5 years while the Benchmark Default portfolio returned 12.5% in nominal terms, or 5.8% in real terms. This is a significant underperformance at first sight. The question is whether the past 5 years are representative of what the investor may expect in the long-term. Certainly, the past 5 years have seen a significant peak and a severe trough in equity markets. Considering the growth in local equity markets of roughly 10% per year in real terms, it is clear that this growth has been substantially above the long-term growth of only 3.4% since 1960. This indicates that the performance differential between the Default portfolio and the average prudential balanced portfolio is skewed in favour of latter portfolio and one should expect this differential to be significantly smaller in the long-term.

We are skeptical and concerned about the fact that the oil price has reached US$ 70 again and do not believe this is warranted based on cost of production, probably still well below 30 US$ a barrel. It seems speculation is surfacing again and that this will start blowing up a fresh bubble unless measures are put in place soon to avoid a recurrence of the severely painful experience we have all just gone through. At the current price level, 'windfall' profits of around US$ 100 billion a month or US$ 3.3 billion a day is 'transferred' from the global consumer to the custodians of the beneficiaries' wealth, presumed to be largely US financial institutions. These financial institutions will once again be looking for investment opportunities globally and this is also borne out by the return of foreign capital flows into South Africa as depicted by **Graph 28**. This situation will have to be monitored closely as it may have a major effect on global financial markets.

Unless legislation is put in place soon to prevent a recurrence of unchecked speculation and leveraging, we expect a rapid recovery of all speculative assets and equities more specifically. This is the more unlikely scenario though. The more likely scenario is that legislators globally will indeed put measures in place and that there will then be a consumer driven, gradual recovery of global financial markets.

The first signs of a recovery in global economies now surfacing, we would expect global asset prices to start recovering. We also expect global interest rates to have reached their bottom and to start turning upwards. Both these developments should put pressure on global inflation rates. The global interest environment will not entice foreign investment in local bonds. This being the more speculative investment capital, we would expect lower exchange rate volatility. As far as exchange rate is concerned, **Graph 29** indicates that the Rand is fairly valued at 8.47 to the US$. At its current level of around 7.70, it is slightly overvalued.

Graph 28



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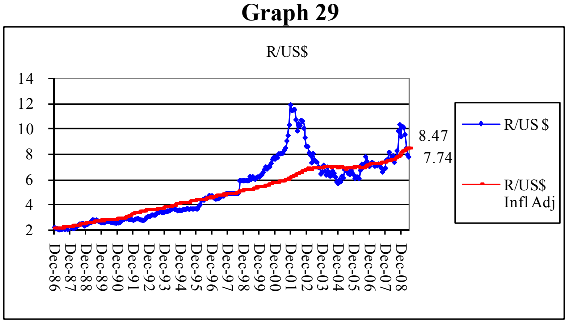
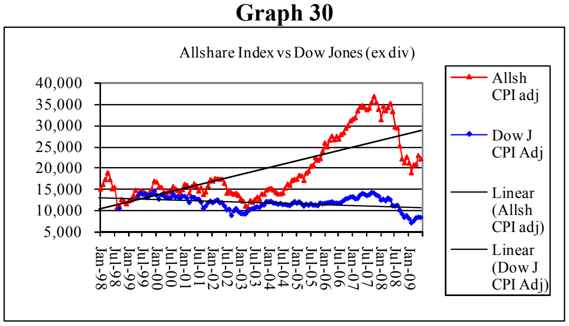
Graph 29



Graph 30 indicates that equity markets seem to have bottomed. The S&P 500 P:E ratio increased dramatically from 28.4 at the end of March to 128.2 the end of June as the result of collapsed earning. The South African Allshare P:E gained 2.4 points to 10.6 from its bottom of 8.2 at the end of February. The strong run in equity markets we have seen over the past 3 months, may be the result of a correction of overly negative expectations prevailing until recently.

Graph 30



5. Conclusion

On the basis of fundamentals, it would seem that global markets are now in more stable and sustainable territory. It would seem that the measures taken by governments to counter the financial crisis have been more effective than what was generally expected. As the result we expect equities to return to the top of all asset classes in terms of performance over the next year. The improvement in global economies should also be beneficial for property while an expected incline in global interest rates will be negative for all interest bearing assets. In terms of equity sectors, our view would indicate on the basis of fundamentals, that consumer goods and services and basic materials should be overweight in one's portfolio.

As was pointed out above, based on a long-term investment horizon, we have moved back from the more conservative absolute return portfolio to the prudential balanced portfolio. Typically retirement funds have a long-term investment horizon with respect to their membership and should hence consider taking on more risk now. Since we are of the opinion that equities should outperform fixed interest investments over the next year, only a very short term investment horizon of a few months would justify investment in cash.

Taking our view of a Rand now being overvalued, it offers an opportunity to raise the offshore exposure again in order to achieve a fair spread of investment in global equity.

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.