Volume 14, No. 6
June 2018

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 JUNE 2018

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

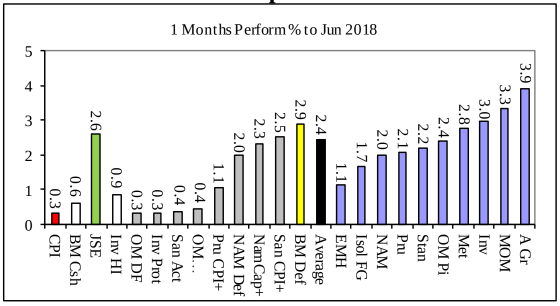
In June 2018 the average prudential balanced portfolio returned 2.45% (May 2018: -1.61%). Top performer is Allan Gray (3.92%); while EMH Prescient (1.13%) takes the bottom spot. For the 3 month period, Allan Gray takes top spot, outperforming the 'average' by roughly 1.92%. On the other end of the scale Investment Solutions underperformed the 'average' by 1.09%.

Graphs 1.1 to 1.10 reflect the performance for periods from 1 month to 20 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 represents a combination of Prudential Namibia Inflation Plus, Sanlam Inflation Linked and Allan Gray Namibia Balanced Funds.

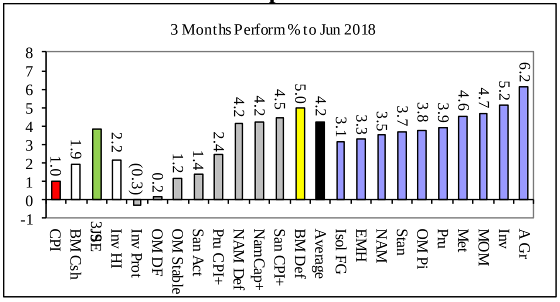
Below is the legend to the abbreviations reflected on the graphs:

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)
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)
Smooth bonus portfolios	
Old Mutual AGP Stable	OM Stable (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)
Investment Solutions Bal Growth (multimanager)	Isol FG (blue)

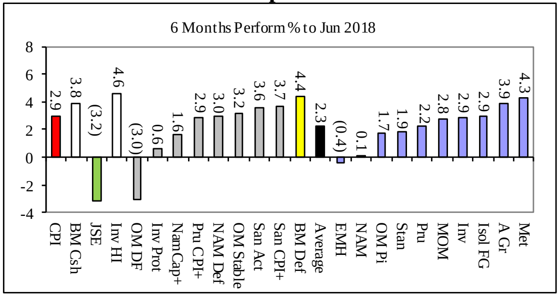
Graph 1.1



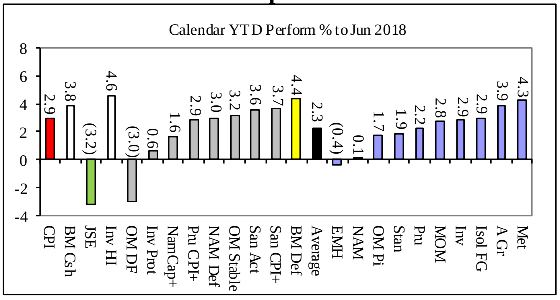
Graph 1.2



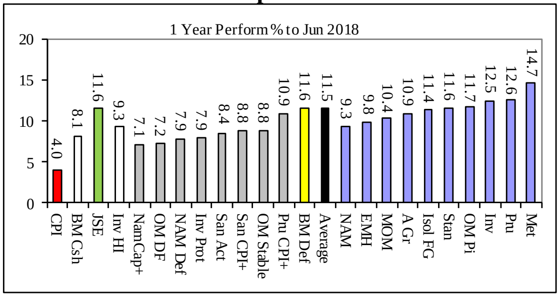
Graph 1.3



Graph 1.4



Graph 1.5



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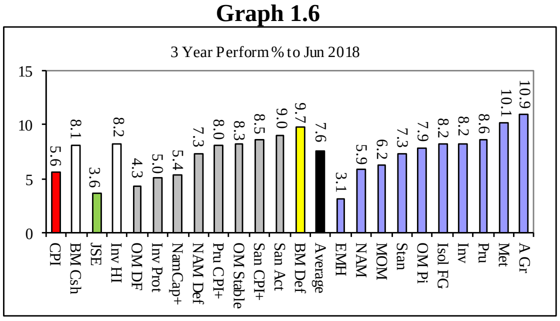
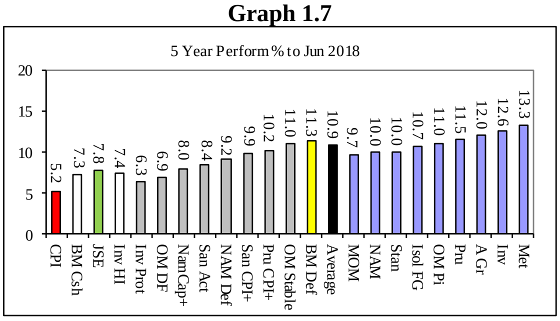
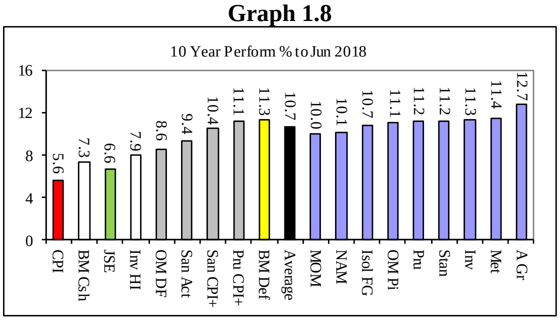
Graph 1.6



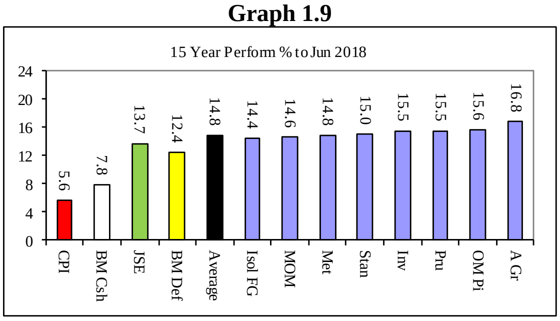
Graph 1.7



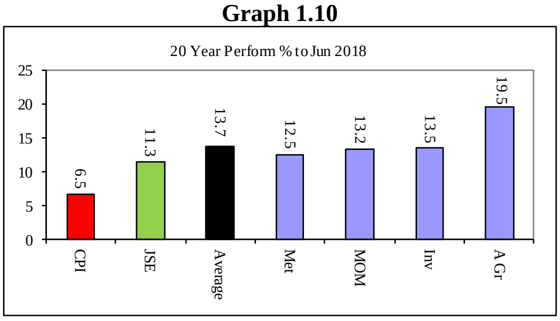
Graph 1.8



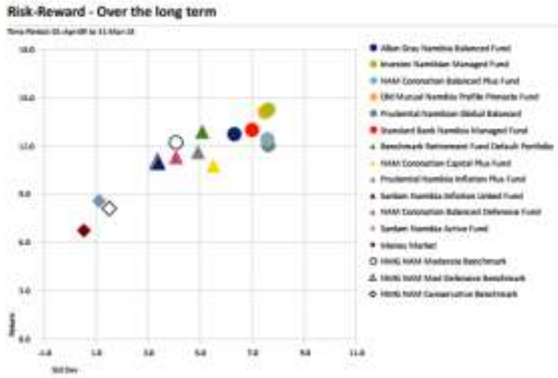
Graph 1.9

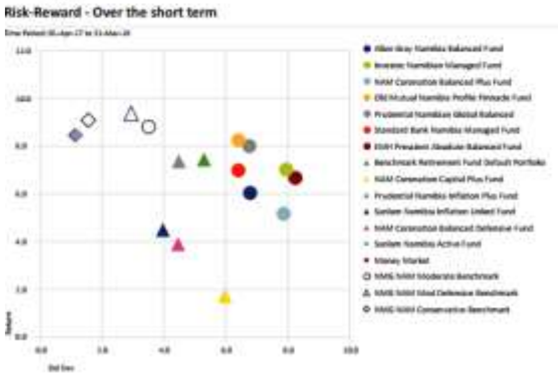


Graph 1.10



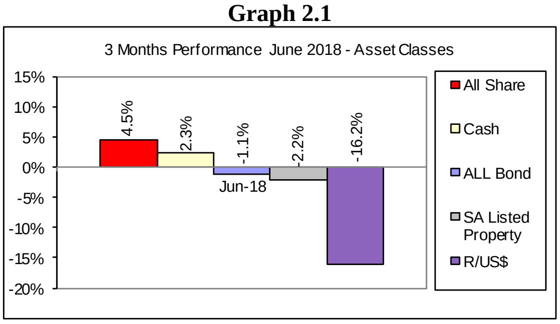
Risk/ Return



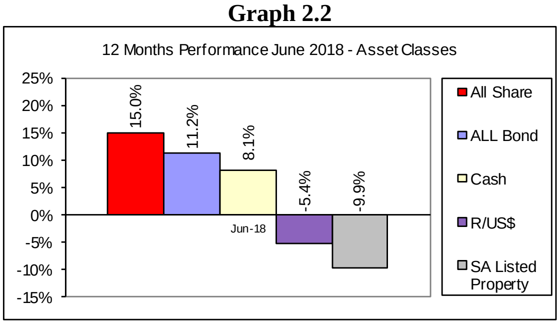


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

Graph 2.1



Graph 2.2



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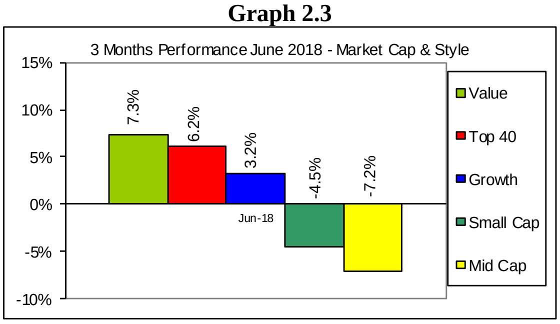
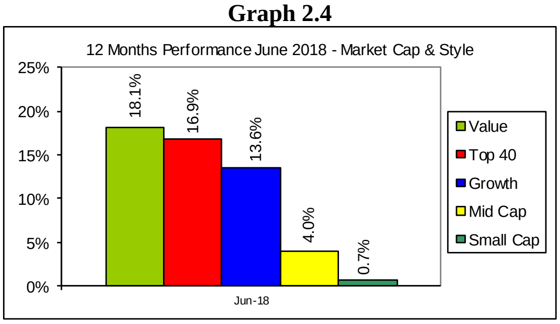
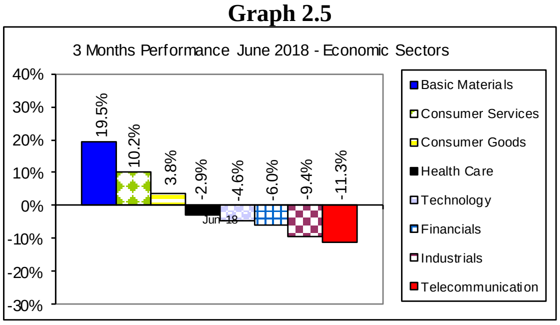
Graph 2.3



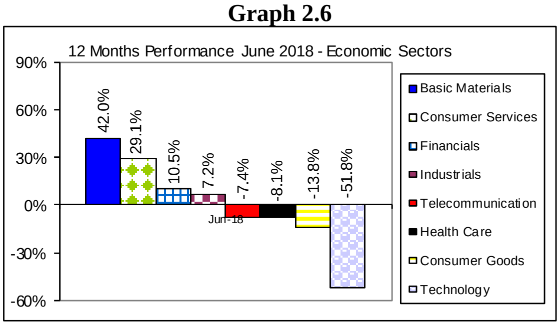
Graph 2.4



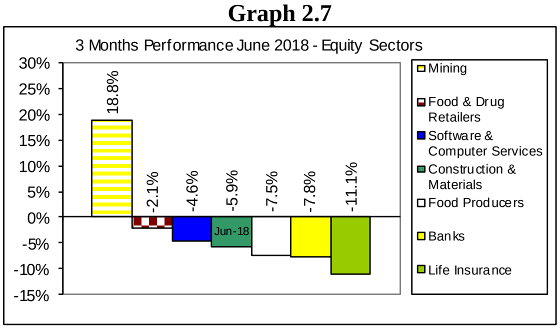
Graph 2.5



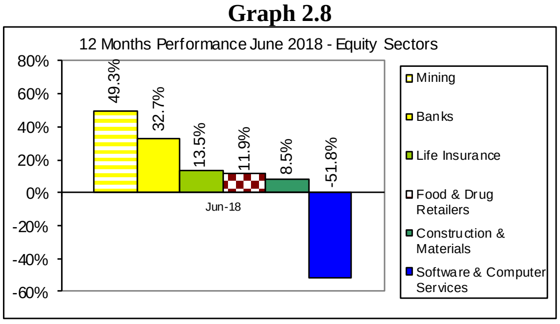
Graph 2.6



Graph 2.7



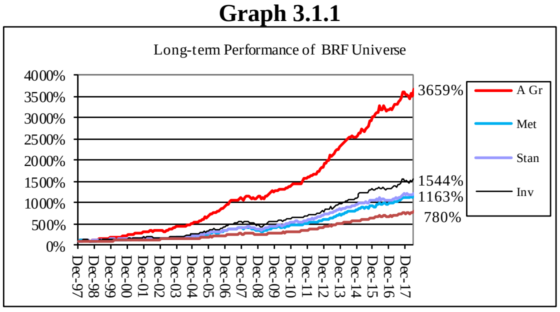
Graph 2.8



3. Portfolio Performance Analysis

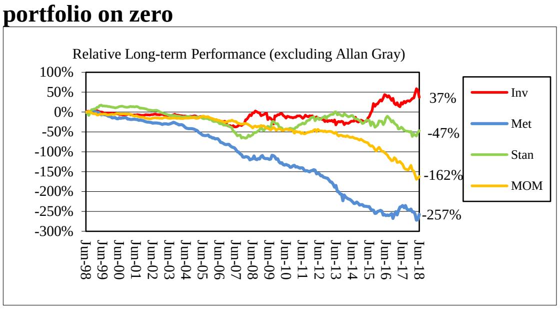
3.1 Cumulative performance of prudential balanced portfolios

Graph 3.1.1

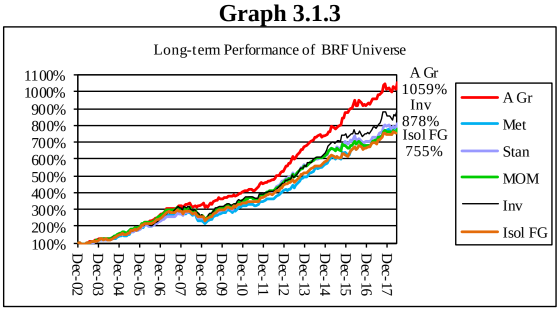


Graph 3.1.2

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



Graph 3.1.3



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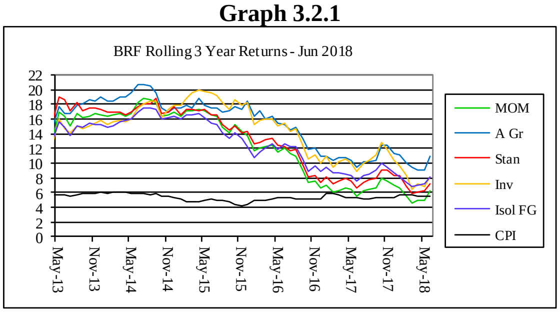
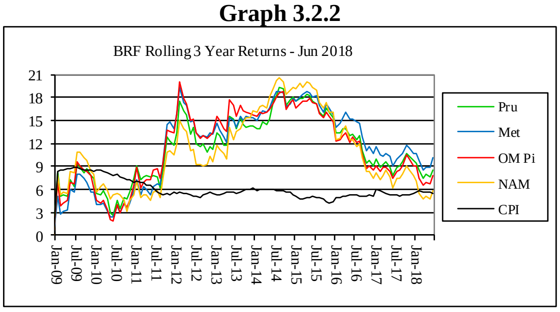
3.2 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1

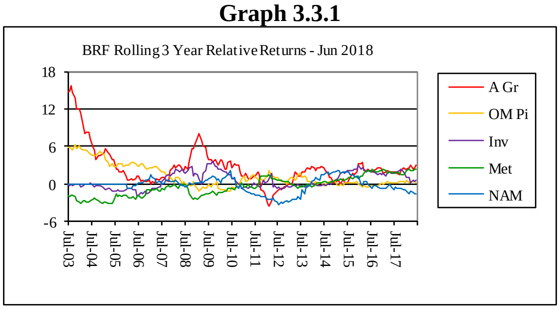


Graph 3.2.2

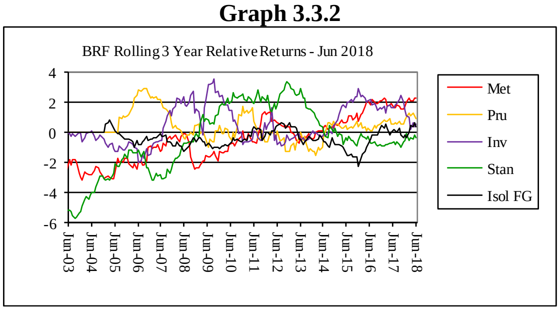


3.3 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

Graph 3.3.1

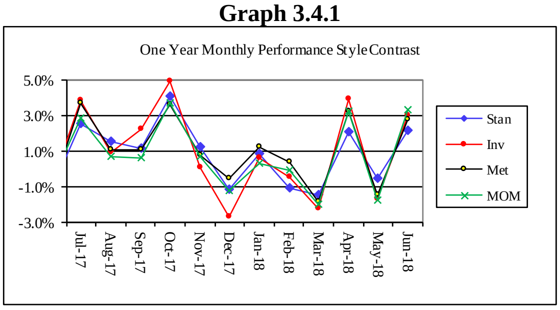


Graph 3.3.2

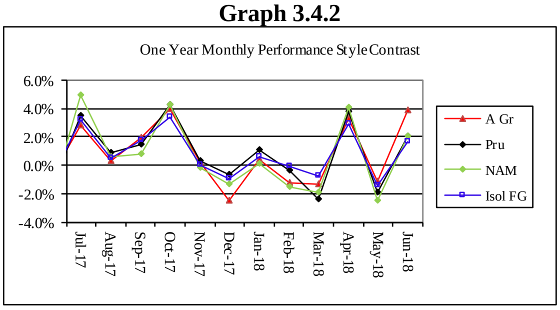


3.4 Monthly performance of prudential balanced portfolios

Graph 3.4.1

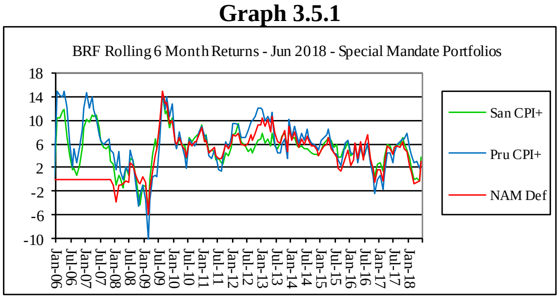


Graph 3.4.2

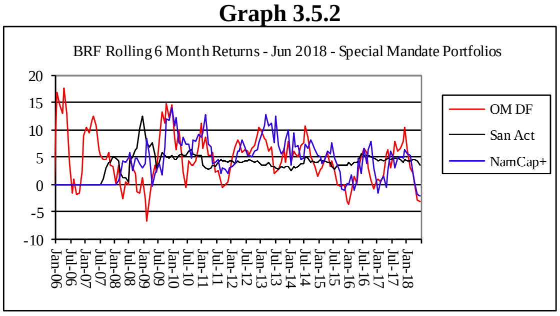


3.5. 6-month rolling and cumulative returns of 'special mandate' portfolios

Graph 3.5.1



Graph 3.5.2



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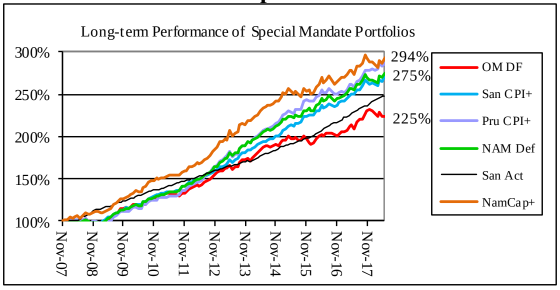
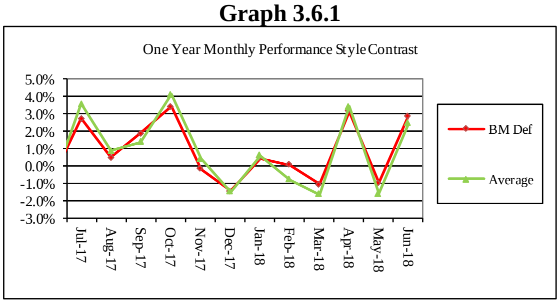
Graph 3.5.3

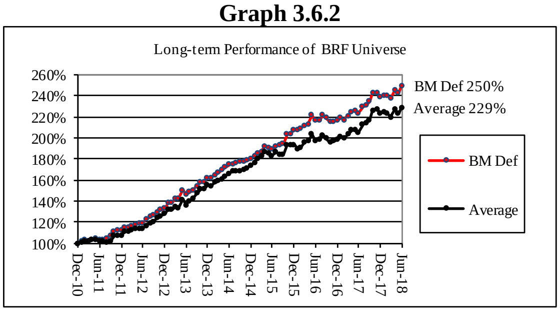


3.6 Monthly and cumulative performance of 'Benchmark Default' portfolio relative to average prudential balanced portfolio

Graph 3.6.1

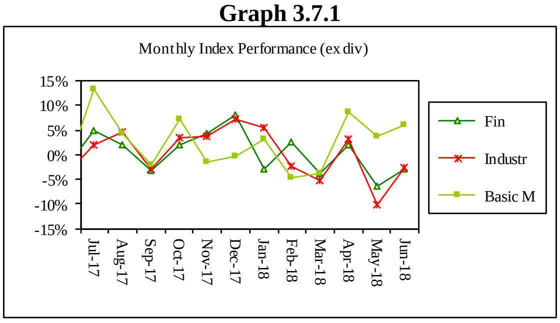


Graph 3.6.2

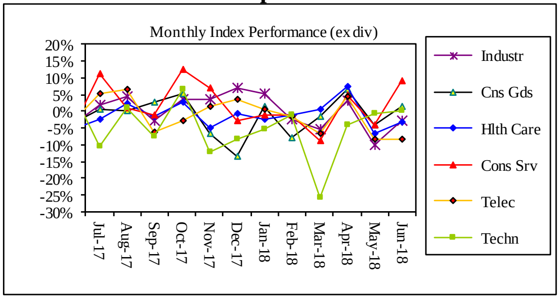


3.7 One year monthly performance of key indices (excluding dividends)

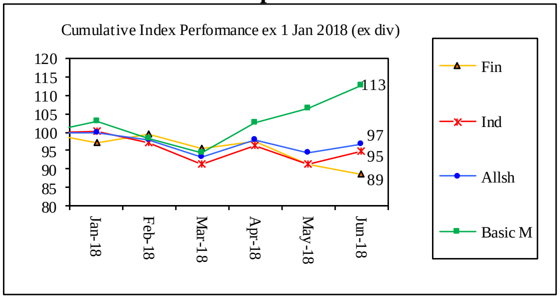
Graph 3.7.1



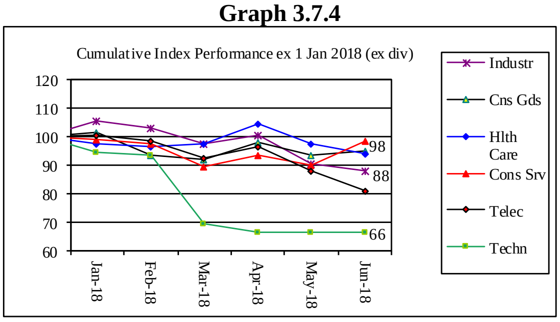
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio – Facts in figures

Table 4.1

Portfolio	Default portfolio	Average Prud Bal
5 year nominal return - % p.a.	11.3	10.9
5 year real return - % p.a.	6.1	5.7
Equity exposure - % of portfolio (qtr end Mar 2018)	46.4	66.6
Cumulative return ex Jan 2011	149.6	128.7
5 year gross real return target - % p.a.	5	6
Target income replacement ratio p.a. - % of income per year of membership	2	2.4
Required net retirement contribution - % of salary	13.0	11.6

The above table reflects the actual returns of the Default Portfolio versus target returns required to produce an income replacement ratio of 2% of salary per year of fund membership that should secure a comfortable retirement income.

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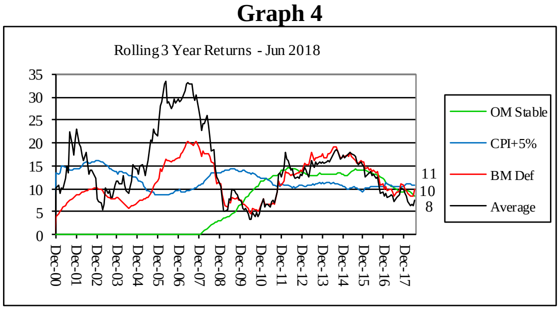
Table 4.2

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.9%	8.3%	6.2%
Best annual performance	8.1%	16.2%	16.9%
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	7.0%	11.7%	10.6%

The table above presents one year performance statistics. It highlights the performance differences between the 3 portfolios over the 3 years July 2015 to June 2018. This gives an indication of volatility of the performance of these 3 risk profiles.

Graph 4

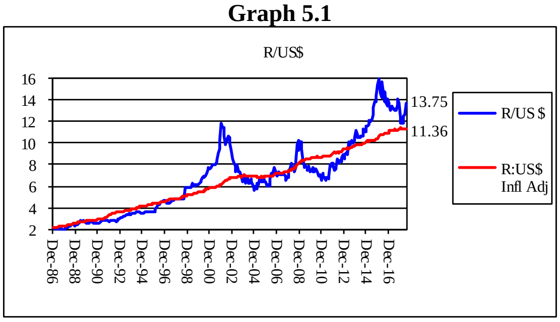


Graph 4 measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end June was 9.7%, the average was 7.6% vs CPI plus 5% currently on 10.6%.

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 at fair value at 11.36 to the US Dollar while it actually stood at 13.75 at the end of June. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

Graph 5.1

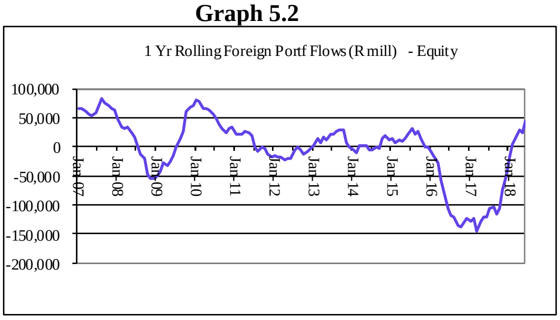


The Rand weakened by 8.25% in June with net foreign investment outflows from bonds and equities of R 29.3 bn. Over the past 12 months the Rand weakened by 5.37%. Net inflows of foreign capital into equity and fixed interest securities over the past 12 months amounted to R 20.7 bn (inflow of R 29.6 bn to end May 2018).

Since the beginning of 2006, total net foreign portfolio inflows amounted to R 325.1bn (May R 354 bn).

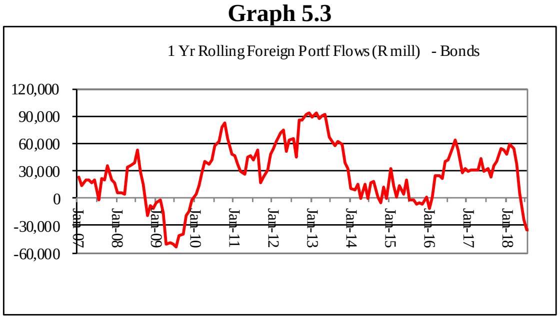
Graph 5.2 reflects a net inflow of capital into South African equities on a rolling one year basis, of R44.3 bn at the end of June (inflow of R 24.1 bn year-on-year to end May). The month of June experienced a net inflow of R 1.0 bn. Since the beginning of 2006, foreign net investment into equities amounts to R 26.2 bn (end May net investment of R 25.1 bn). This represents roughly 0.18% 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 23.6 bn over the past 12 months to end of June (inflow of R 5.6 bn over the 12 months to end of May). The month of June experienced a net outflow of R 30.3 bn. Since the beginning of 2006, foreign net investment in bonds amounts to R 298.9 bn (to May R 329.3 bn).

Graph 5.3



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 11.3% per year since January 1987, and this excludes dividends of 3%. Namibian inflation over this period of 30 years was 8.1% per year. This is equivalent to a growth in real terms of 3.2% p.a. over this period,

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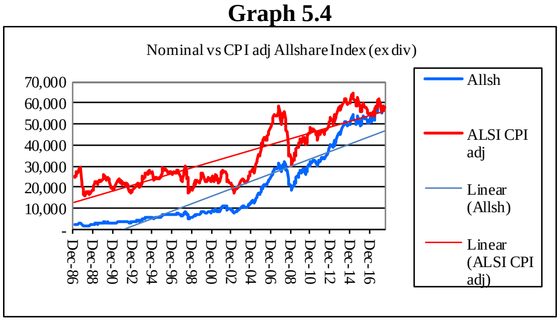
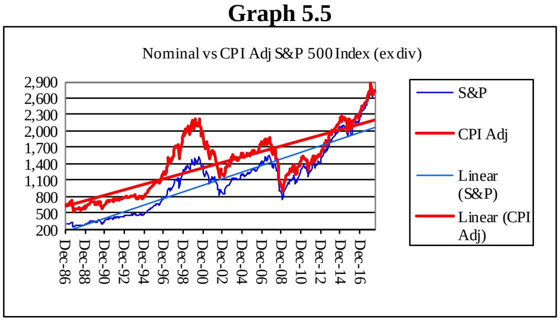
excluding dividends, or around 6.2% including dividends.

Graph 5.4



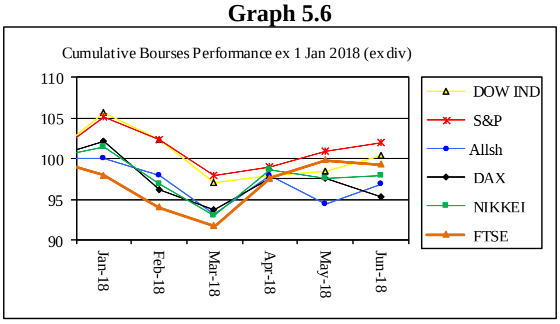
Graph 5.5 reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 7.6% per annum, over this period of 30 years. US inflation over this period was 2.6%. This is equivalent to a growth in real terms of 5.0% p.a. over this period, excluding dividends.

Graph 5.5



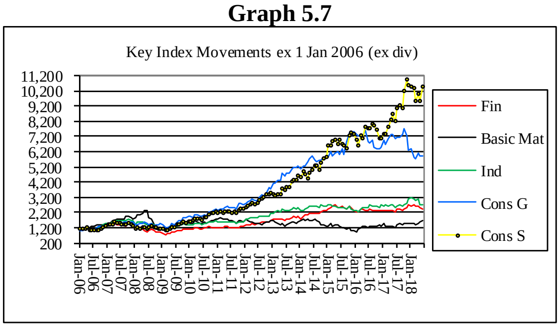
Graph 5.6 provides an interesting overview of some of the major global share indices, showing up the Dow Jones as the top performing index indices since the start of 2018.

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: 20.5%; Consumer Goods: 15.2%; Industrials: 8.2%; Financials: 7.2%; and Basic Materials: 4.2%.

Graph 5.7



6. **A more conservative portfolio for now should let you sleep more peacefully!**
by Tilman Friedrich

In previous newsletters we have regularly made the point that we cannot expect investment returns to 'normalise' until the artificially low interest rate environment has been normalised by the central banks of this world and here we really refer to those of the US, Europe and Japan (not being close enough to what is happening in China). The US of cause will lead the trend and its trend is currently to lift interest rates. Going by history, a spread of between 1% and 2% between US CPI and the Fed Rate will indicate that interest rates are back in 'normal territory'. The rest of the world will have no choice but to follow suit.

The relevance of a normalised interest rate environment is that returns of all other asset classes should start normalizing in other words, returning to inflation beating returns of all asset classes except perhaps cash, up to inflation plus 6% to 8% on equities. Until we reach normality we will see lots of volatility particularly in the more volatile asset classes and we will see similar returns on the various asset classes. This is also what we showed in last month's column where we looked at the period 1 July 2014 to 31 May 2018. In such scenario, a more conservative portfolio structure should offer more peace of mind as it will avoid the painful draw-downs of the more aggressive portfolios.

This is exactly what the trustees of the Benchmark Retirement Fund did with its Default Portfolio when they decided to pair the Prudential Inflation Plus portfolio with the Sanlam Inflation Linked portfolio on a 50:50 basis of 50% of the portfolio in October last year. This appears to have worked out quite well for the portfolio since October 2017, given that it is a very short period. Over this 9 month period the Default Portfolio returned 6.2% compared to the return of the average manager's 5.3%. Graphs 1.1 to 1.6 above cover this period and mirror the positive outcome of the reduction of risk affected in the Default Portfolio.

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 JUNE 2018

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.

The US Repo rate is currently 2%, while US CPI was 2.9% at the end of June. This relationship should be the inverse of what it is meaning that based on current CPI, a US Repo rate of around 4% would indicate a normalised interest rate environment. At the more recent rate of upward adjustment of the Repo rate we are still looking at around 4 years until we reach this point but let's keep an eye on this.

With these expectations, the Rand and local interest rates will remain under pressure for the next 4 years and this will also impact negatively on local inflation. Low returns and rising interest rates will also impact negatively on the consumer.

Conclusion

Equities remain in a phase of a long drawn-out correction to last another two to four years, as interest rates in the US are moving to more normal levels again. We do not see any conventional asset class that is equities, property, bonds and cash that offers exciting prospects in the near future. Solid companies purchased at fair value should be able to produce reasonable real returns. This remains the time for stock pickers who can identify value in the universe of the various asset classes. And, once again we caution investors not to expect double digit returns for the next few years. Rather take comfort with an inflation beating return in the region of 4% to 5%, which currently means a return of between 8% and 10%. Take comfort with such a return and try to lock in such opportunities when they present themselves.

The relatively strong Rand still offers an opportunity to diversify offshore. In the light of announced changes to regulation 28 that require the Namibian exposure of pension fund investments to be lifted to 45%, the investor faced the dilemma of investments being highly concentrated in Namibia. The SA allocation will effectively be restricted to 25%, the balance of 30% invested offshore. This in itself presents an imbalance in the typical pension fund portfolio, too much being required to be invested in Namibia. Discretionary assets should thus now be expatriated to improve this imbalance.

Amongst the various equity sectors, commodities have been in the doldrums for quite some time now and should benefit from a slowly improving global economy and are thus expected to offer fair prospects for 20

Important notice and disclaimer

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