Volume 6, No. 4, Apr 2010

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 APRIL 2010

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.

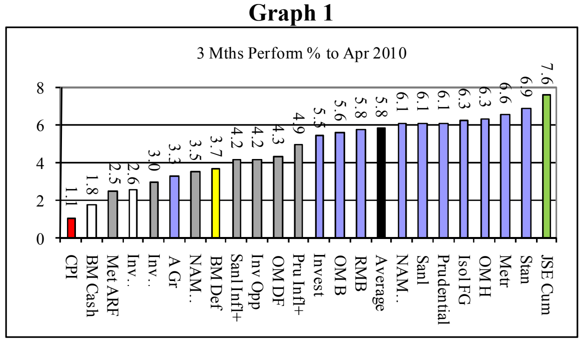
1. Review of Portfolio Performance

In **April** the **average prudential balanced portfolio** returned a meager 0.68% (March 4.13%). Best and worst performance **for the month** was delivered by Allan Gray (1.47%) and Old Mutual (0.45%), respectively. We haven't seen Allan Gray on top spot for a while. The weakening of the Rand and the poor performance of resources has benefited Allan Gray's relative performance in April.

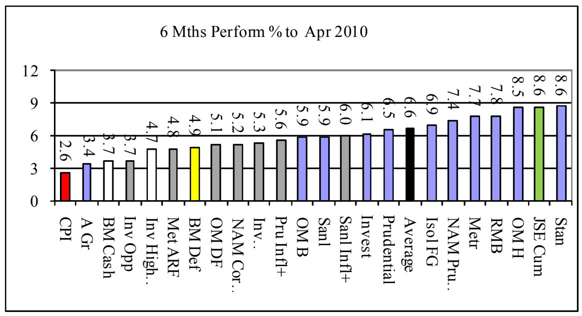
Graphs 1 to 7 reflect the performance for periods from 3 months to 10 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no colour bars), the average of prudential balanced 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	
Money market	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)
NAM Coronation Balanced Def	NAM Cor Def (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Invest (blue)
Investment Solutions Bal Growth, prev. Focused Growth (multimanager)	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)

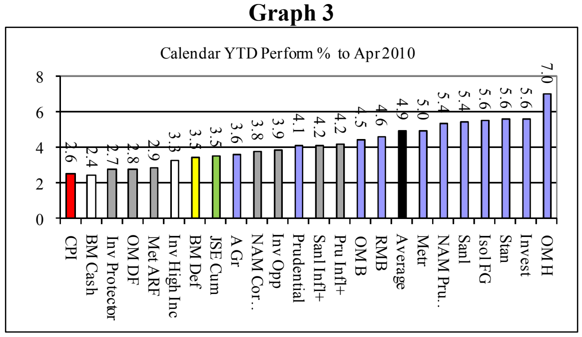
Graph 1



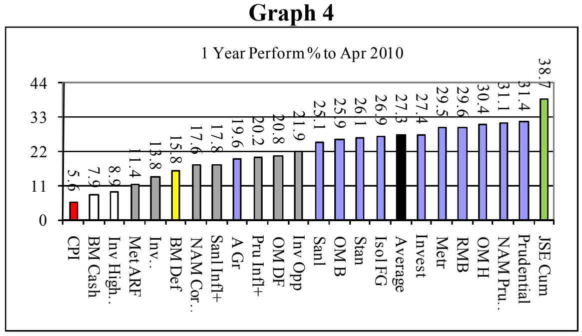
Graph 2



Graph 3



Graph 4



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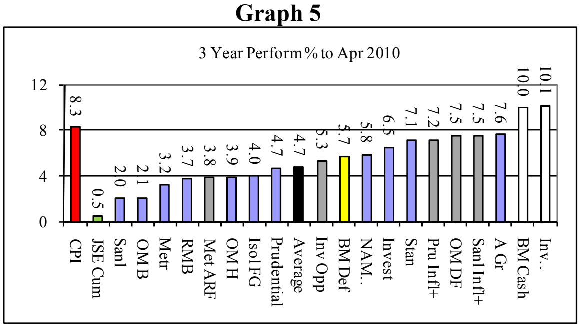
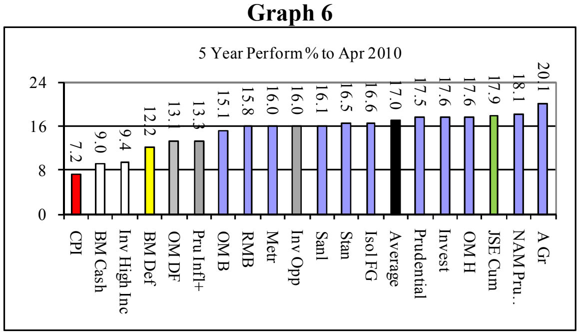
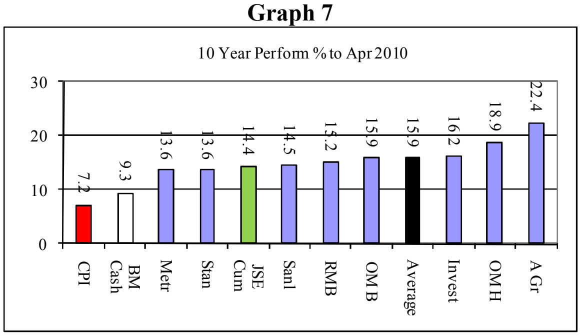
Graph 5



Graph 6

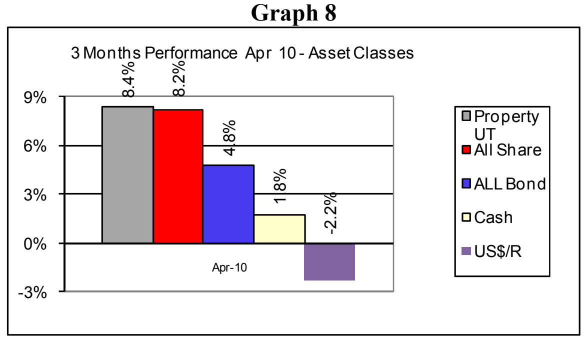


Graph 7

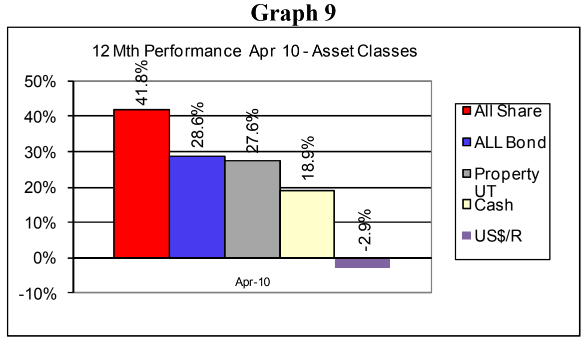


2. **Performance of Key Indices** (index performance by courtesy from pointBreak/Deutsche Securities)

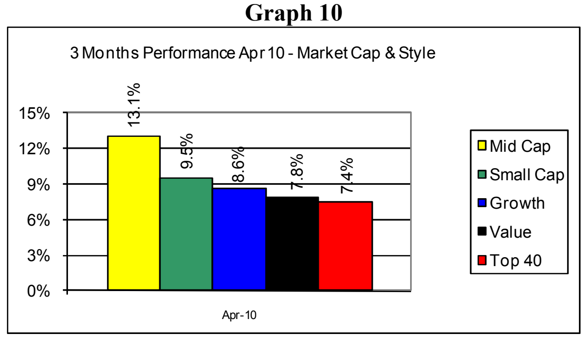
Graph 8



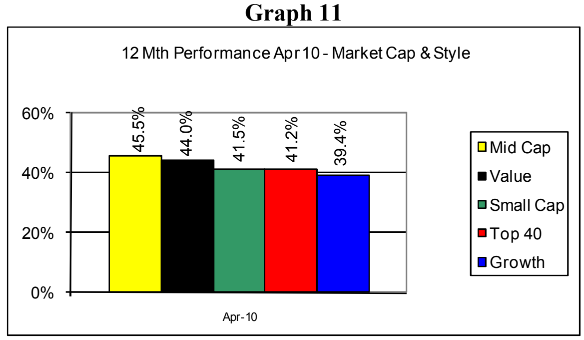
Graph 9



Graph 10



Graph 11



Graph 12

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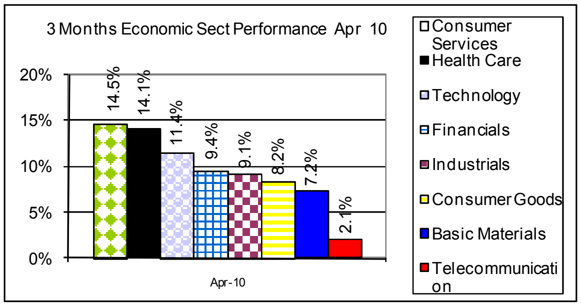
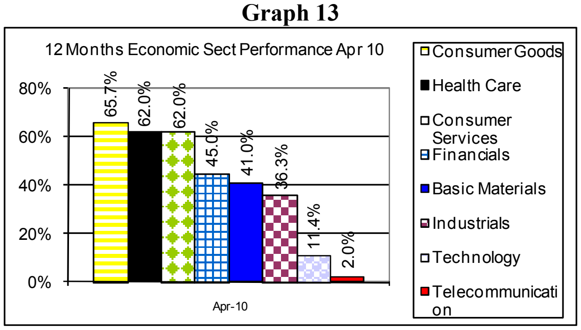
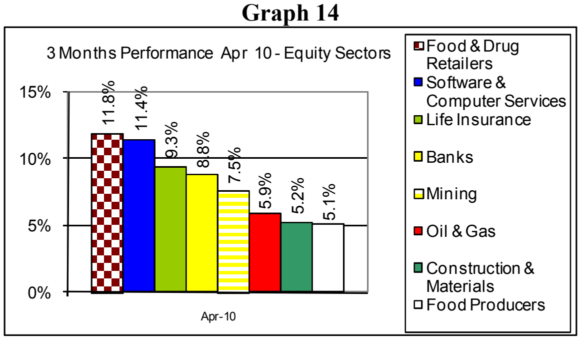


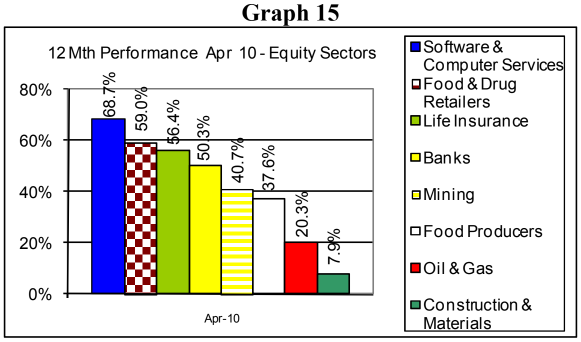
Graph 13



Graph 14



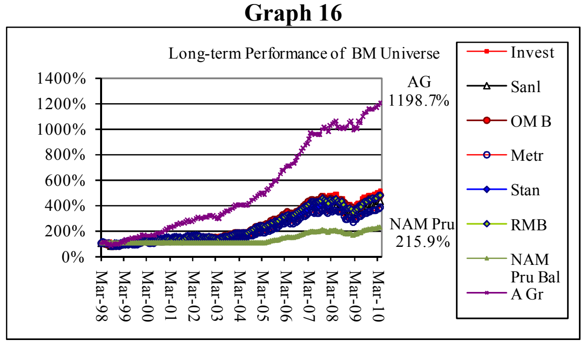
Graph 15



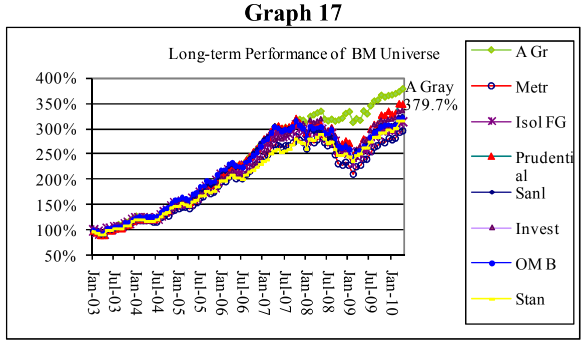
3. Portfolio Performance Analysis

3.1. Cumulative performance of prudential balanced portfolios

Graph 16

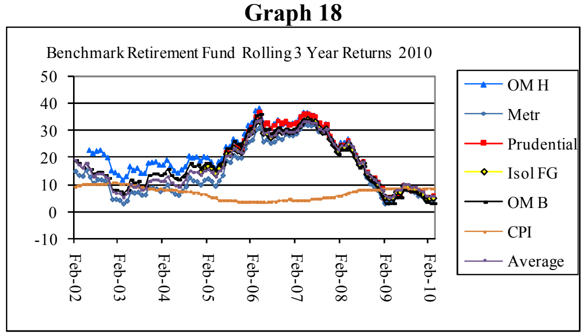


Graph 17

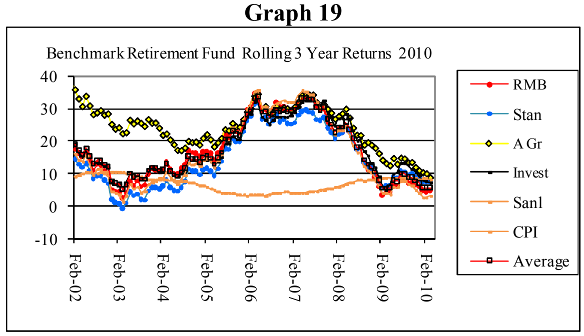


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 18



Graph 19



3.3. Monthly performance of prudential balanced portfolios

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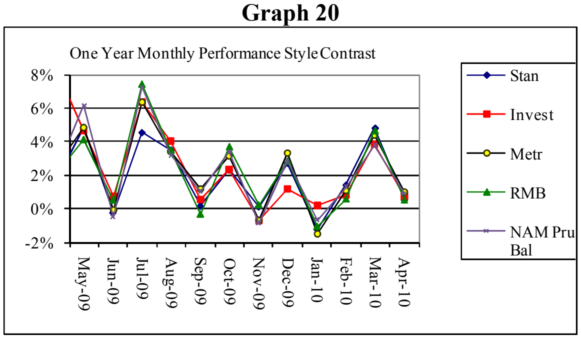
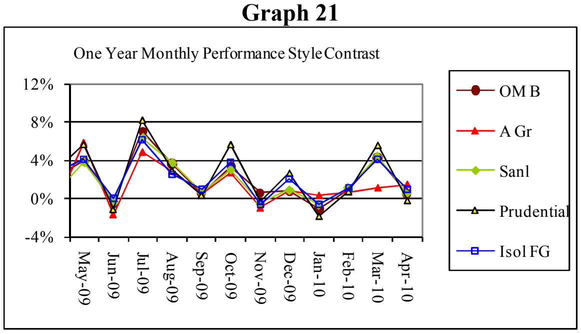
Graph 20

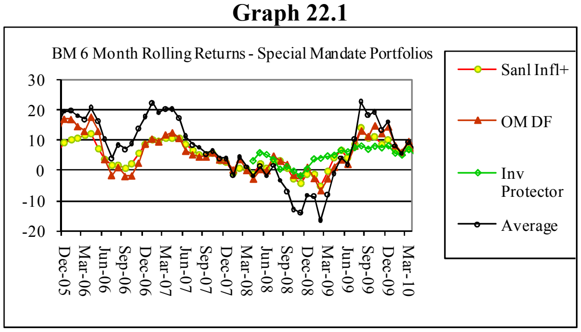


Graph 21

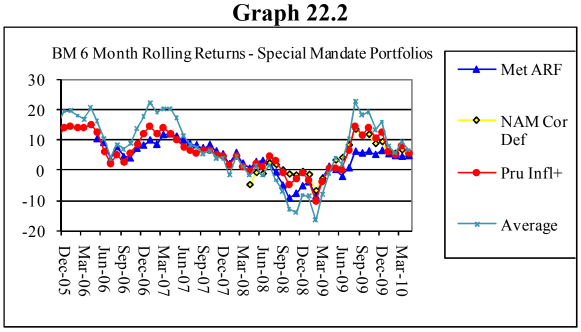


3.4. 6-month rolling returns of 'special mandate' portfolios

Graph 22.1

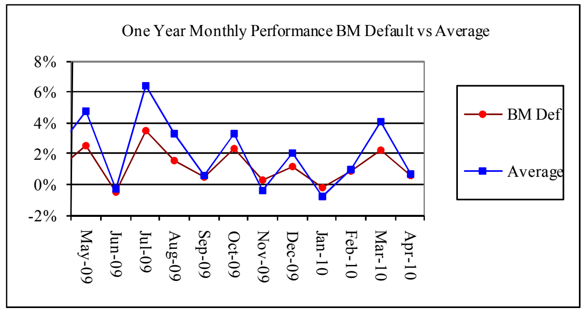


Graph 22.2



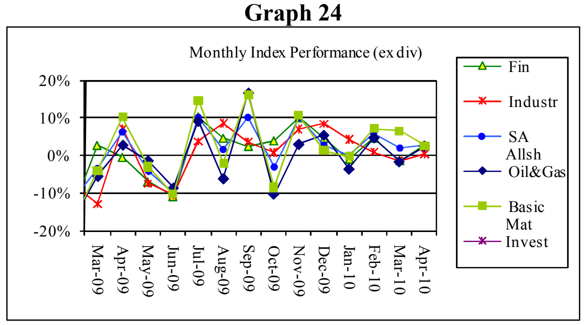
3.5 Monthly performance of 'Default' portfolio relative to average prudential balanced portfolio

Graph 23

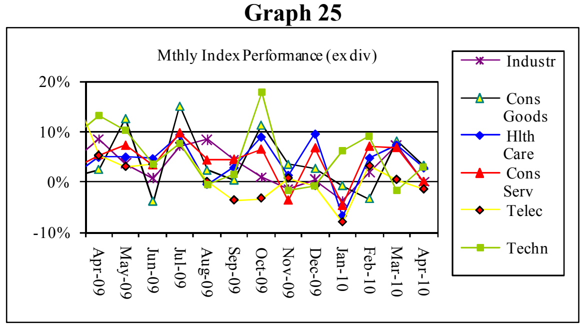


3.6 Monthly and one year cumulative performance of key indices (excluding dividends)

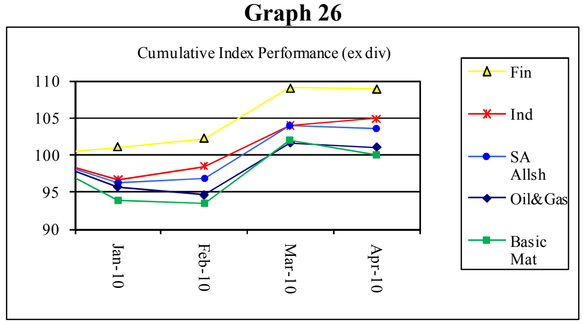
Graph 24



Graph 25



Graph 26



Graph 27

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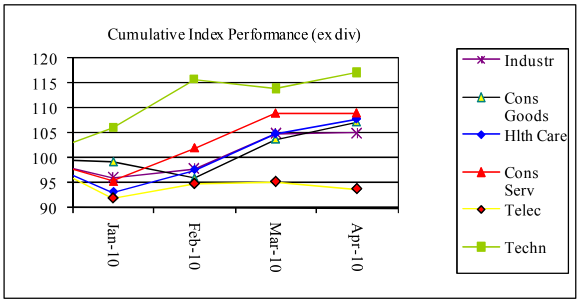

4. The Benchmark Default Portfolio

Graph 6 shows that the average prudential balanced portfolio returned 17% in nominal terms, or 9.8% in real terms, over the past 5 years while the Benchmark Default portfolio returned 13.8% in nominal terms, or 6.6% in real terms. The past 5 years one again reflect a return significantly above expected long-term returns and also distort the expected long-term performance differential between the Default portfolio and the average prudential balanced portfolio, slightly skewed in favour of latter portfolio. We would expect the average prudential balanced portfolio to deliver a real return of roughly 6% per year and the Default portfolio to sacrifice around 2% for the benefit of lower volatility, thus an expected real return of around 4% per year.

The Money Market portfolio returned 7.9% and the Default portfolio returned 15.8%, gross for the one year to end April. The more 'risky' average prudential balanced portfolio returned 27.3% gross over this period. A fee of roughly 0.75% p.a. still has to be deducted from all but the Money Market Portfolio. The performance of the prudential balanced portfolios is significantly more volatile than that of the Default portfolio, which produces significantly more volatile performance than the Money Market portfolio. The table below presents one year statistics over the 3 years May 2007 to April 2010:

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	7.8%	5.7%	4.7%
Best annual performance	10.2%	20.5%	33.2%
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	9.2%	12.7%	16.3%

This table represents the different characteristics of the three types of portfolio quite well. The Default portfolio is a more conservative investment aimed at minimising negative returns and with a long-term return objective of inflation plus 4%.

It is very important, though, 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!

5. A Contrarian Preview Of The Next 12 Months

Global equity markets have experienced a dramatic recovery to the end of the first quarter but moved into more volatile phase of late. In the light of the status of global economies and historically low interest rates, we believe that equity markets are unlikely to produce any further meaningful positive returns in 2010 assuming the more likely of two scenarios referred to below.

As shown in **Graphs 13 and 15** the main indices on local markets have produced somewhere between 2% ('Telecommunication') and 69% ('Software & Computer Services') and the Allshare delivered a return of 42% over the 12 months to April 2010, including dividends. This compares well with the returns delivered by the DOW Jones (34%), the DAX (27%), the Nikkei (25%) and the Hang-Seng (36%). SA historic P:E was 17.5 at the end of April, on par with its highest point since January 2007 (17.6). The historic S&P 500 P:E was 17.4 at the end of April, compared to 18.1 in January 2007.

More likely scenario:

- Governments will be take measures to curb speculative trading of commodities and equities (Germany has unilaterally taken the first step).
- Crude price will revert to cost based levels, in our expectation somewhere around 60 US$ (currently around US$ 70).
- Global fiscal stimulus will be removed as economies start recovering.
- Unwinding of the global sovereign debt bubble will be a long drawn out process.
- Global interest rates will start rising.
- Global taxes will start rising.
- Consumer sentiment will be dampened.
- Portfolio flows will be diverted from equities to interest bearing assets (see graph 29).
- Equity markets will move sideways with a risk of a downward correction (as we have seen since the end of April).
- The Rand will weaken as global interest rates rise and portfolio flows are diverted from commodities and equities to other asset classes and as higher risk premiums are placed on smaller economies (as experienced in May).

Less likely scenario:

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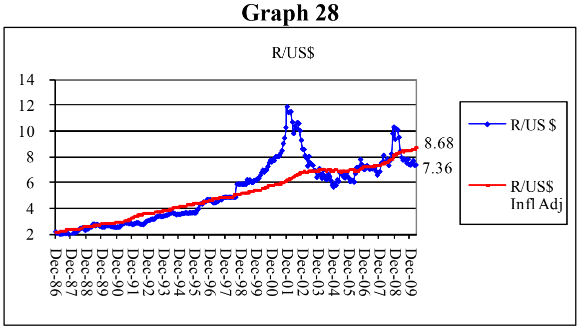
- Speculative trading in commodities and equities will remain unchecked.
- The oil price continues to be driven by speculation to levels above 100 US$.
- Another bubble develops in commodity and asset prices.
- Consumer balance sheets will experience a rapid recovery asset prices are blown up.
- Although consumers are likely to be weary of venturing into another spending spree for a while, risk appetite is likely to increase again a year or so down the track.
- Global interest rates will remain low as consumers are reducing debt levels.
- The Rand will remain strong as the result of the demand for commodity based stocks and interest rate arbitrage.

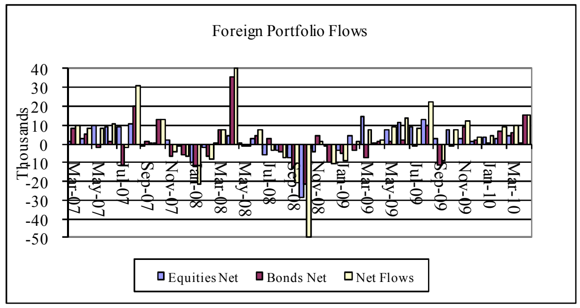
Graph 28 indicates that the Rand is fairly valued at 8.68 to the US. Our more likely scenario expects a weakening of the Rand over the course of 2010 as the result of the inflation differential, an increasing risk premium likely to be attached to weaker currencies and a redirection of foreign portfolio flows. Should the Rand weaken from its current level of around 7.60, to 8.7 over the course of 2010, this would represent a potential return on a US$ investment of around 14% all else being equal.

Graph 29 indicates that foreign equity purchases in SA have receded of late and given our outlook based on the more likely scenario, this should persist for an extended period of time putting pressure on the Rand and on local equity markets. For the year to end of April, the FTSE/JSE still experienced a massive net inflow of R 67 billion (R 67 billion, 12 months to end March), compared to a net outflow of R 32 billion for the year to end April 2009 (R 28 billion, year to end March 2009).

Graph 28

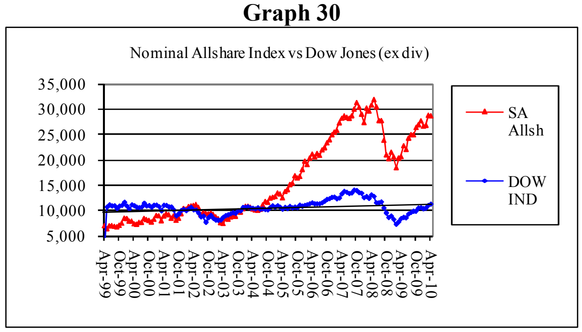


Graph 29

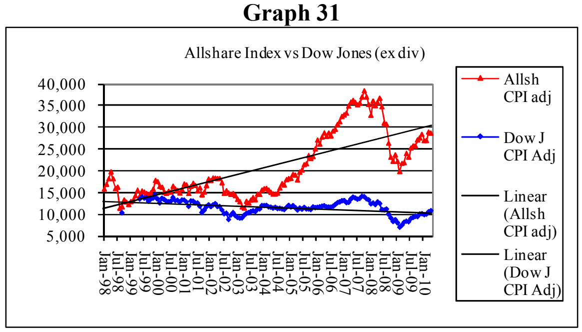


Graph 30 shows to what extent equity markets have recovered in nominal terms since their low at the end of February 2009. The DOW Jones Industrial Index is now back at 80% of its September 2007 peak, while the SA Allshare already reached 90% of the May 2008 peak.
Graph 31 reflects the same statistics but adjusted for US and SA inflation respectively.
Over the past 12 months, the 1 year trailing SA Allshare P:E more than doubled, gaining 9.3 points to 17.5 from its bottom of 8.2 at the end of February 2009.

Graph 30



Graph 31



6. Conclusion

Despite a correction in May, in our view, global equity markets are still in risky territory, have probably run ahead of themselves and are likely to produce no or negative growth for the next 6 to 12 months. Global interest rates will remain stable for another 3 months or so, to start picking up from thereon, and consumer demand will be subdued for the next 12 to 24 months, while the Rand should weaken further once global interest rates do start rising.

An expected incline in global interest rates in the medium term will be negative for interest bearing assets for a while. In terms of equity sectors, our shorter term view would indicate on the basis of fundamentals, that consumer goods and services should be overweight to neutral in one's portfolio, while commodities should be neutral to underweight. We expect financials to return to the higher quartiles later in the year once the interest cycle has turned. With a weakening Rand and an improvement in global economies, industrials should start producing better performance over the next 12 months. In this environment the performance of most conventional asset classes will be muted. We do not expect equities in general to perform but stock picking can add value. Hedge funds should also be able to produce positive returns in this scenario. As far as precious metals are concerned, we expect prices do decline in US$ terms. Due to our expectation of the Rand depreciating, this will offset the decline in prices to produce a muted return for the year.

A lack of prospective investment opportunities suggests that one should be overweight offshore assets, specifically cash exposure under current circumstances. Taking our view on the Rand, an investment in the US$ could produce a return of between 5% and 15% over the remainder of 2010. For pension funds, a conservative balanced portfolio with a high foreign and high local cash exposure is our choice for 2010. Property should also start showing improved performance from here on.

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.