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Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 JULY 2012

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.

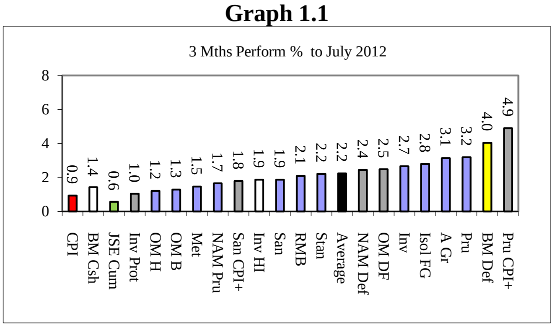
1. Review of Portfolio Performance

In **July** our **average prudential balanced portfolio** returned 2.42% (June minus 0.47%). Top performer is Investec (2.84%), while Allan Gray (1.48%) takes bottom spot.

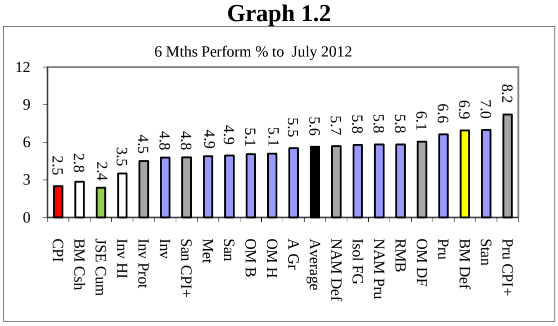
Graphs 1.1 to 1.7 reflect the performance for periods from 3 months to 10 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no color bars), the average of prudential balanced 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. 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 Csh (no color)
Investec High Income (interest bearing assets)	Inv HI (no color)
Investec Protector	Inv Prot (grey)
Investec Opportunity Fund	Inv Opp (grey)
Prudential Inflation Plus	Pru CPI+ (grey)
Old Mutual Dynamic Floor	OM DF (grey)
Sanlam Inflation Plus	San CPI+ (grey)
NAM Coronation Balanced Def	NAM Def (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Inv (blue)
Investment Solutions Bal Growth, (multimanager)	Isol FG (blue)
Prudential Managed	Prud (blue)
Metropolitan Managed	Met (blue)
NAM Prudential Balanced	NAM (blue)
Old Mutual Profile Balanced	OM B (blue)
Old Mutual Profile Growth	OM H (blue)
RMB Managed	RMB (blue)
Sanlam Managed	San (blue)
Stanlib Managed	Stan (blue)

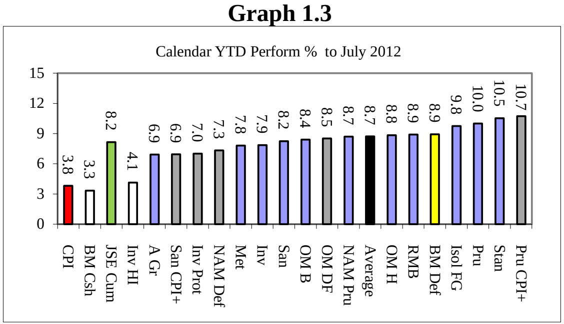
Graph 1.1



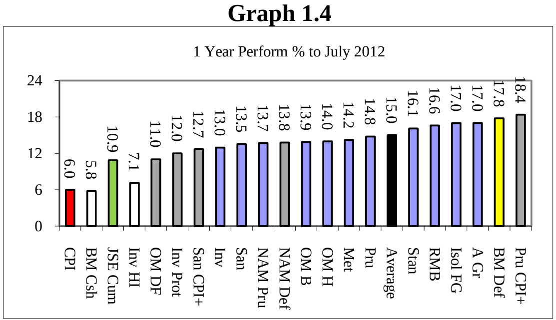
Graph 1.2



Graph 1.3



Graph 1.4



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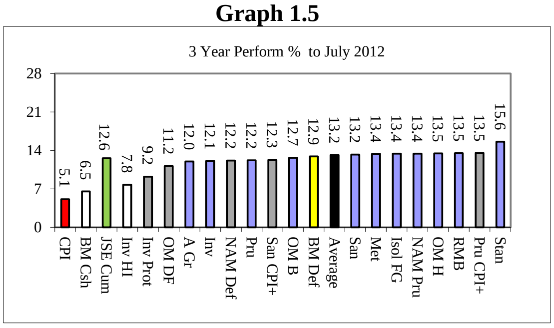
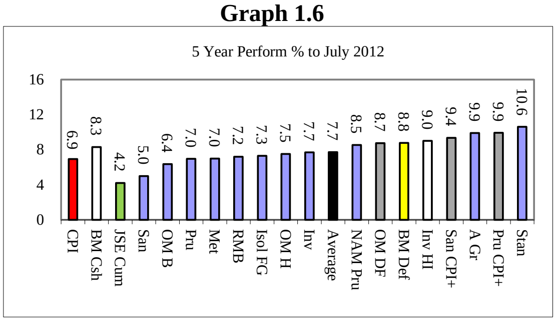
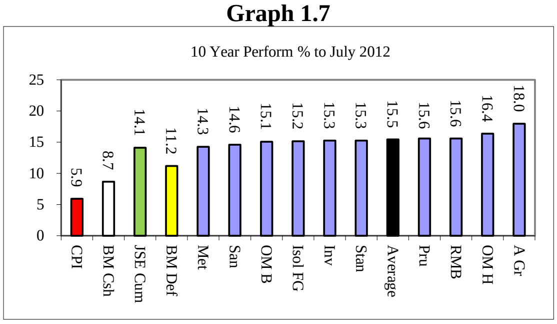
Graph 1.5



Graph 1.6

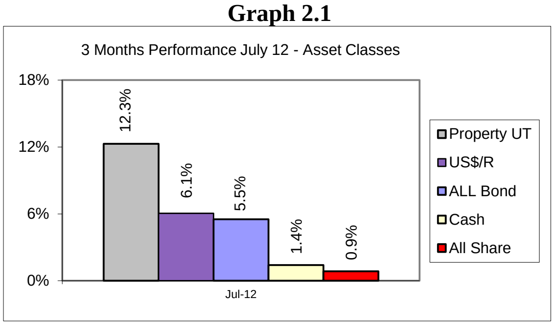


Graph 1.7

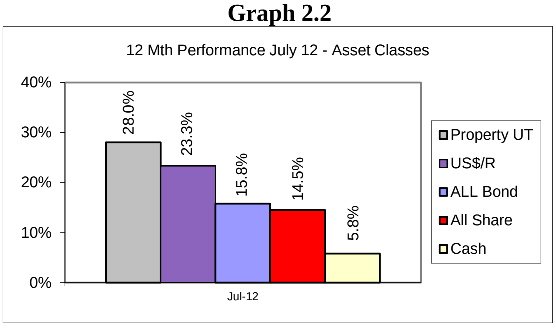


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

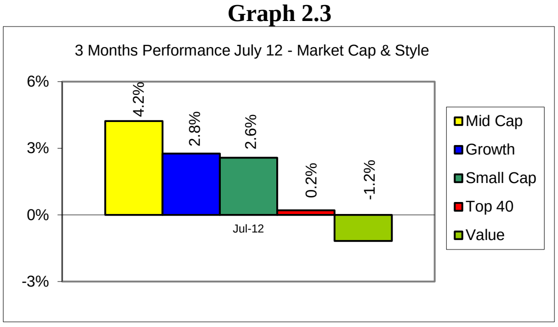
Graph 2.1



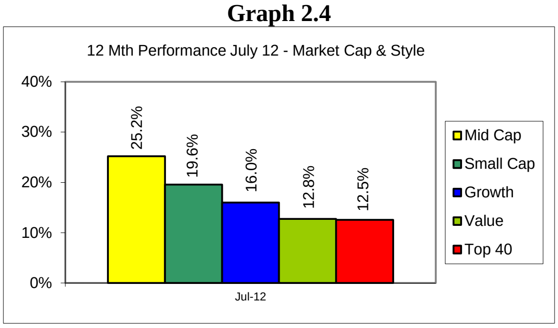
Graph 2.2



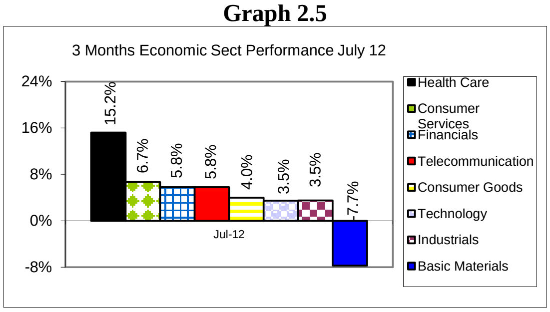
Graph 2.3



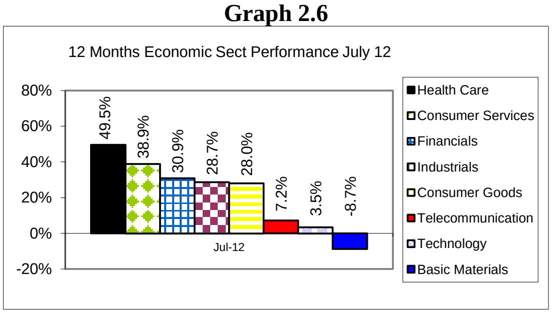
Graph 2.4



Graph 2.5



Graph 2.6



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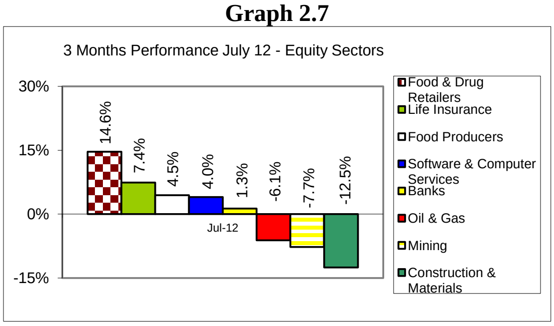
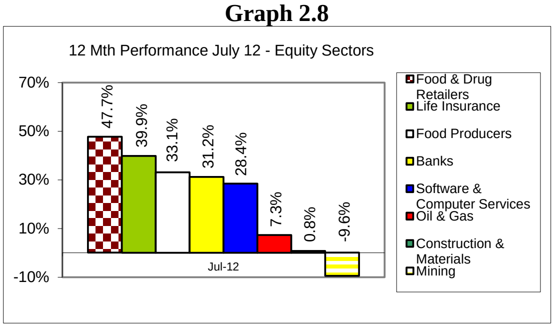
Graph 2.7



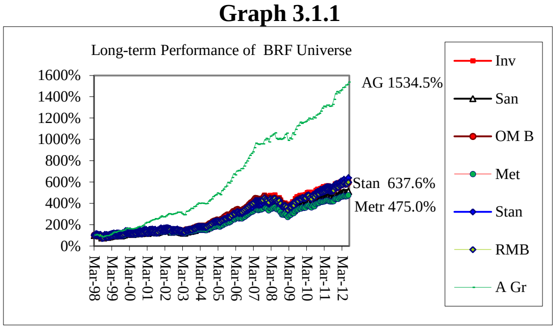
Graph 2.8



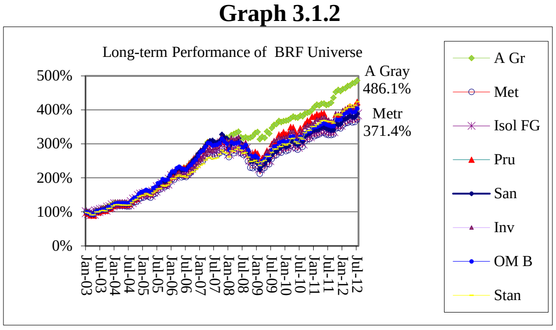
3. Portfolio Performance Analysis

3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

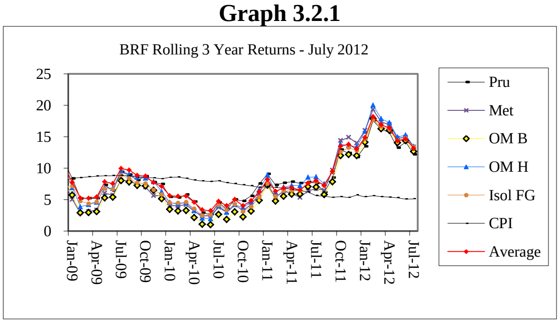


Graph 3.1.2

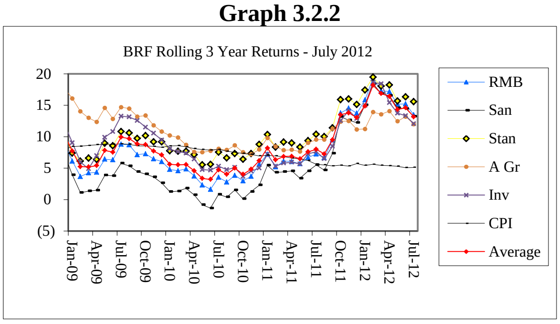


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1

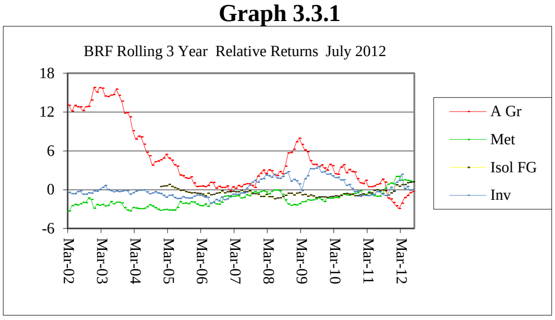


Graph 3.2.2

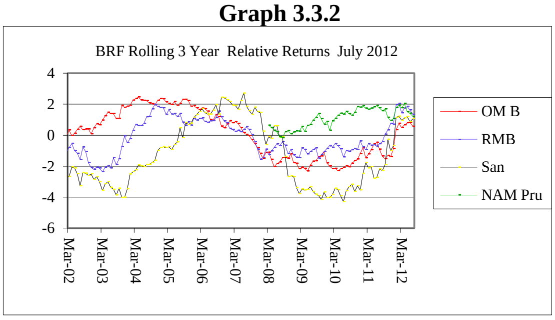


3.3. 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

Graph 3.3.1



Graph 3.3.2



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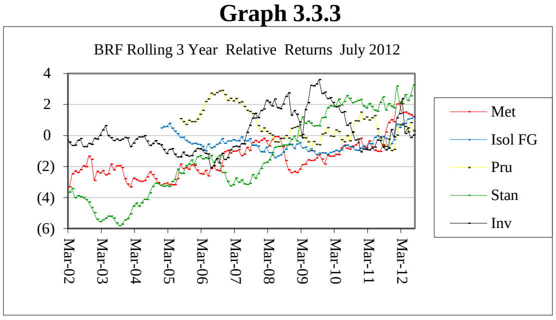
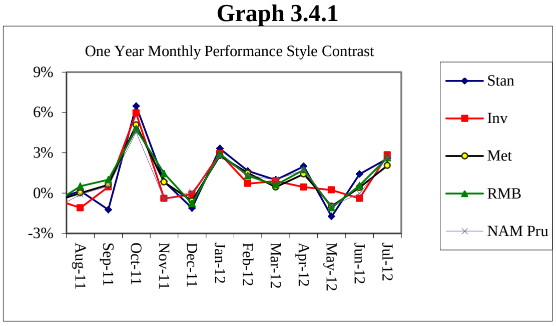
Graph 3.3.3

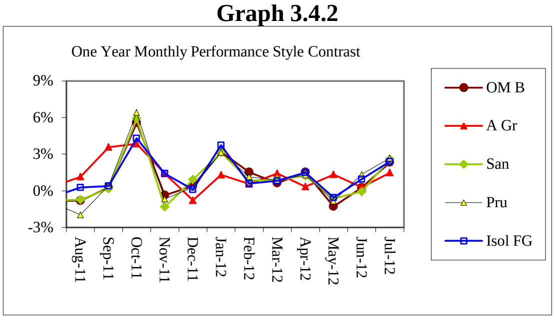


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

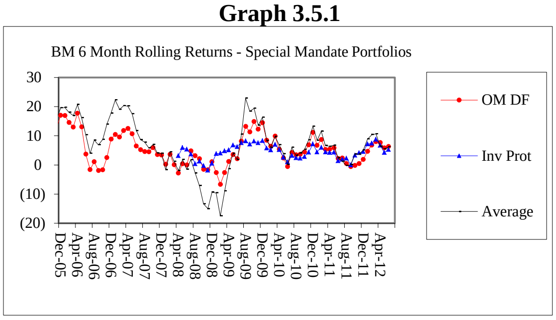


Graph 3.4.2

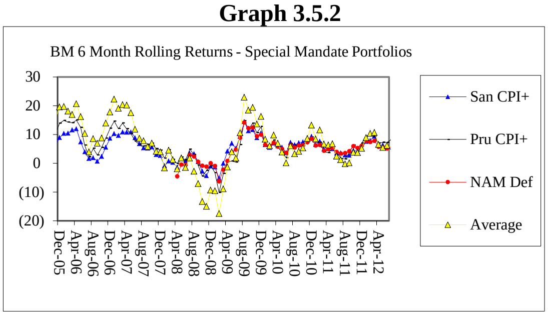


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

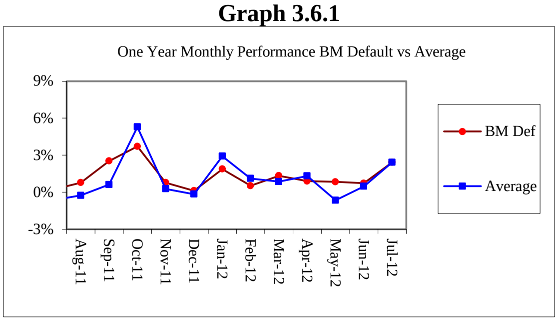


Graph 3.5.2

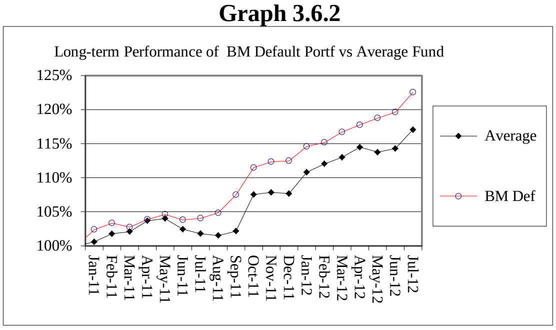


3.6 Monthly and cumulative performance of 'Default' portfolio relative to average prudential balanced portfolio

Graph 3.6.1

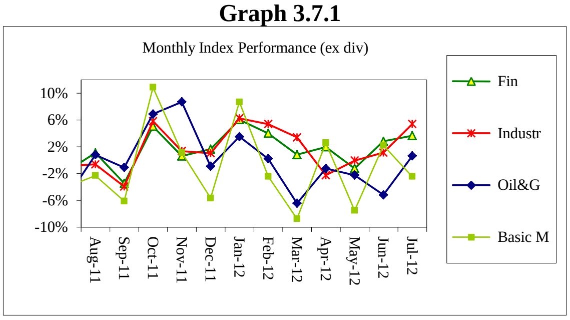


Graph 3.6.2



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

Graph 3.7.1



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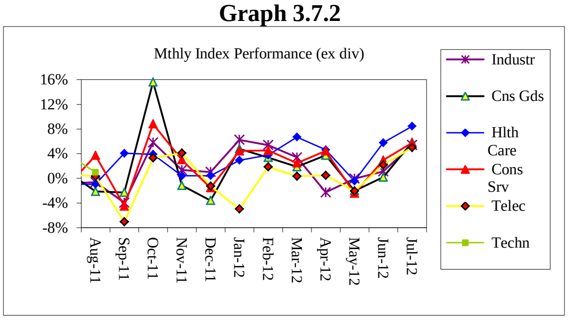
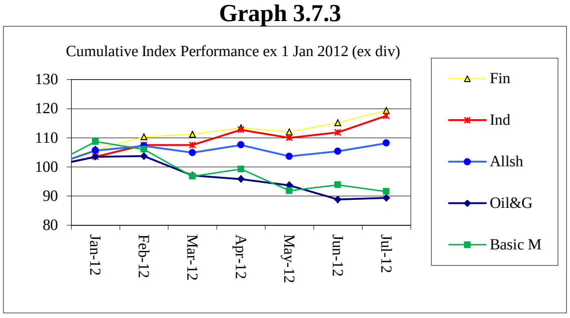
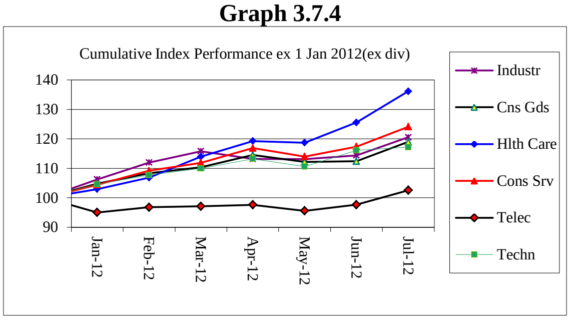
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio

Graph 1.6 shows that the average prudential balanced portfolio returned 7.7% p.a. in nominal terms, or 0.8 % p.a. in real terms, over the past 5 years while the Benchmark Default portfolio returned 8.8% p.a. in nominal terms, or 1.9% p.a. in real terms. 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 trailing the expected long-term goal significantly over the past 5 years.

Having raised the risk profile of the Default portfolio effective the start of 2011, by replacing Metropolitan ARF with Allan Gray, we would expect the Default portfolio to sacrifice around 1% for the benefit of lower volatility, thus an expected real return before management fees (typically 0.75%), of around 5% per year. Since this change was effected, the default portfolio returned a cumulative 22.5% compared to 17.1% for the average prudential balanced portfolio over this 17 month period.

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 August 2009 to July 2012:

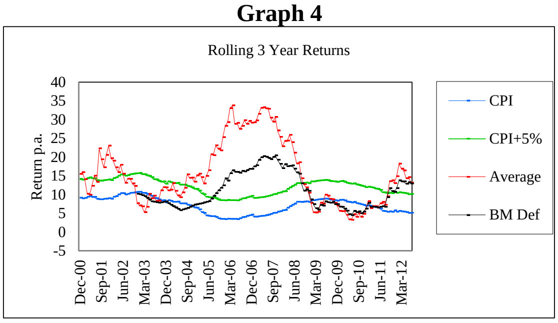
Table 4.1

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.8%	0.2%	1.3%
Best annual performance	10.8%	17.8 %	30.2%
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	7.2%	11.7%	13.9 %

The Benchmark Default portfolio is a more conservative investment 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 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. It shows that since September 2008, both the Benchmark Default portfolio as well as the average prudential balanced portfolio were lagging inflation plus 5% and at times even inflation but have surpassed inflation plus 5% since October 2011.

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

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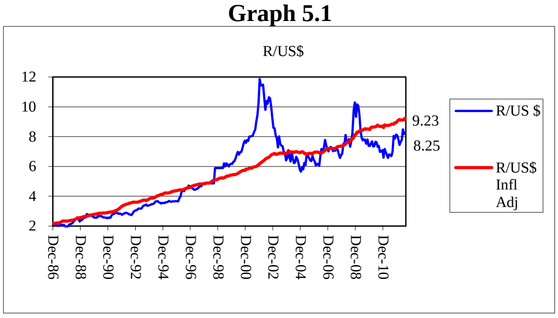
fairly valued at 9.23 to the US Dollar while it actually stood at 8.25 at the end of July. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

Graph 5.1

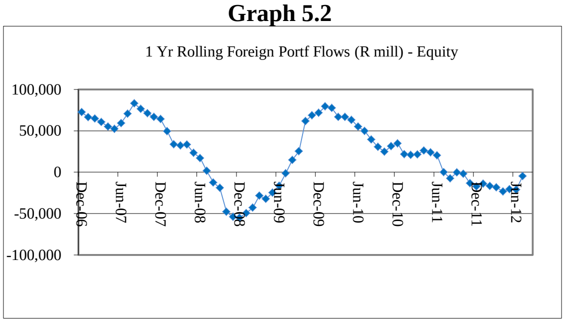


Support of the Rand from foreign capital flows continues, mainly through bond purchases

Graph 5.2 reflects a more steady but negative flow of capital out of South African equities on a rolling one year basis, with a net outflow of R 4.8 bn on a year-on-year basis at the end of July (outflow of 21.2 bn to end June), the trend having been downward since peaking in January 2010 with a one year inflow of R 79.5 billion. Since the beginning of 2006, foreign net investment in equities amounts to N$ 170 billion. This represents roughly 2.5% of the market capitalization of the JSE.

The fiscal easing measures of the Eurozone are likely to provide an artificial underpin to the Rand through continued foreign inflows into local financial markets, more specifically into the bond market though.

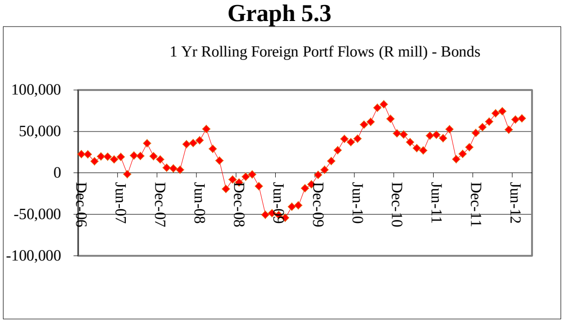
Graph 5.2



Graph 5.3 on a rolling one year basis, reflects a much more volatile foreign portfolio flow into bonds of R 65.7 bn over the past 12 months to end of July (R 64.2 billion over the 12 months to end of June), well below the previous peak of R 82.6 billion in October 2010. Since the beginning of 2006, foreign net investment in bonds amounts to N$ 180 billion.

It will be interesting to see what the impact of the recent reduction of the repo rate by SA Reserve Bank will be on these flows.

Graph 5.3

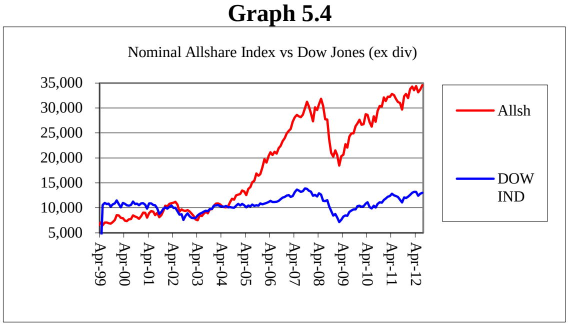


The net inflow of foreign capital into equity and fixed interest assets was R 61 bn for the 12 months to end July (inflow of R 43 bn to end June), compared to R 41 bn for the 12 months to end July 2011 (R 41 bn to end June 2011). Total net foreign portfolio flows amount to N$ 350 billion since the beginning of 2006.

Graph 5.4 reflects the movement of the JSE and the DOW Jones since May 1999, the financial crisis being clearly visible. In nominal terms the JSE passed its month end peak of before the financial crisis, while the DOW Jones is still substantially below its previous peak. In nominal terms, the JSE grew by 13.6% per year, while the DOW Jones only grew by 1.6% per year, over this period of just over 13 years, dividends excluded. Namibian inflation over this period was 7% per year in contrast with US inflation of 2.5%.

Graph 5.5 reflects the same statistics but adjusted for US and SA inflation respectively. Since May 1999 the JSE Allshare Index has grown by 6.6% per year above inflation, over this period of just over 13 years, and this excludes dividends of somewhere in the region of 2% to 4%. In contrast, the DOW Jones declined by 0.9% per year above inflation over this period, also excluding dividends.

Graph 5.4



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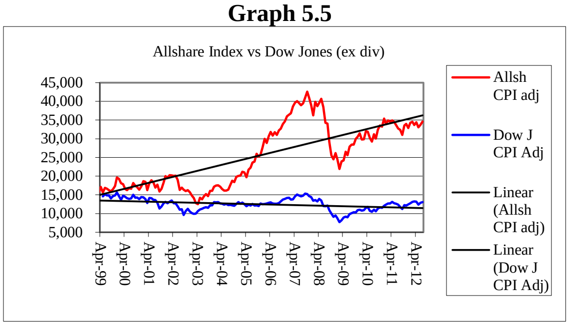
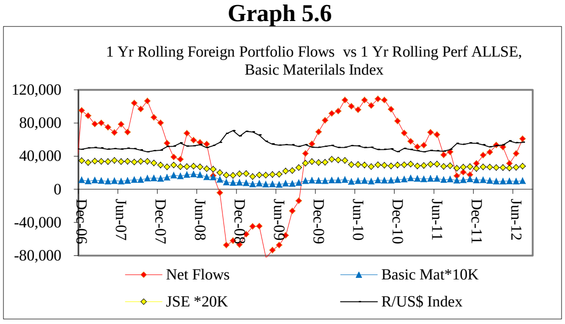


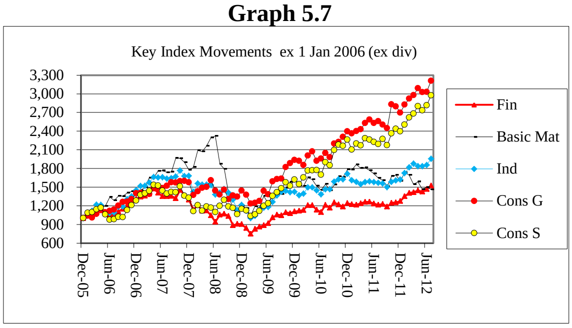
Graph 5.6 overlays the R/US$ exchange rate, the trendline of 1 year rolling returns of the JSE and of the Basic Materials Index on 1 year rolling total portfolio flows. It does show a correlation between the value of the Rand, the Allshare and the Basic Materials Index and foreign portfolio flows although it appears that the Basic Materials Index is much less correlated than the other indices.

Graph 5.6



Graph 5.7 provides an interesting 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.

Graph 5.7



6. Conclusion

The severe economic woes of Europe just do not seem to end and will be around for quite some time. The US is in no better position and is still alternating between recession and some green shoots in the economy while every now and then, the prospects of further monetary stimulus raising its head. Consumer sentiment has certainly shown little signs of improvement in the US while it is still in reverse gear in Europe. China which has enjoyed double digit growth over an extended period has experienced a significant decline in economic growth to an official 7.6% for the latest quarter. What has driven our economy and that of other developing countries is in reverse gear and is unlikely to improve for an extended period of time.

In earlier newsletters we made reference to the tail winds that benefited local financial markets, caused by the financial crisis in developed countries. Exceptionally low interest rates offshore have produced a flood of money flowing into our and other developing countries in search of yields, resulting in a strong currency and low interest rates. Low interest rates no doubt encouraged the consumer to over extend his debt which in turn would have resulted in high property prices and unsustainable consumption levels. In the article 'Running out of luck Down Under' Jonathan Trepper provides a review of the Australian economy. The Australian situation as described, can be mirrored upon our economies and should be food for thought for any investor with a longer-term investment horizon. This exceptionally interesting article can be accessed via this link.

We consequently believe that our equity markets are unlikely to show the type of growth we have seen since the start of 2009, although we still expect our markets to produce reasonable returns. Interest rates are still likely to remain low for some time, cash probably zero or negative in real terms. Any recovery of the Rand should be used as an opportunity to diversify offshore and to invest in equity markets that were particularly hard hit by negative sentiment rather than economic fundamentals. These can mainly be found in Europe where negative investor sentiment has punished most equity markets severely. With discounts to fair value up to as high as 64% (Italy) at end of July, Europe offers a compelling investment opportunity.

Graph 5.7 indicates that local consumer goods and consumer services had an excellent run over this period of over 6 years relative to the other sectors and are in our view in unsustainable territory. We do not expect too much more joy out of Consumer Goods and Consumer Services anymore and these should hence be underweight.

On the basis of fundamentals, one should be overweight position in local Industrials and Financials that have not seen the growth of the consumer sectors. Basic Materials should offer some buying opportunities although as a sector we do not foresee it showing any significant recovery in the medium term. With the prospect of declining interest rates, property should also offer fair returns in the medium term.

We believe an assertive balanced portfolio with an overweight in equities and property and underweight bonds and cash should be appropriate under current circumstances. A high foreign equity exposure to the US, and particularly Eurozone countries where markets experienced a dramatic decline as the result of negative investor sentiment, is our call for the next year.

7. Important notice and disclaimer

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