Volume 11, No. 04,
April 2015

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 APRIL 2015

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

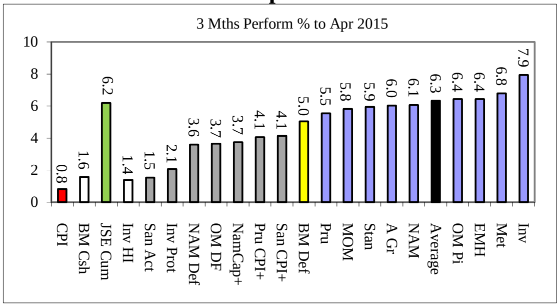
In **April** the **average prudential balanced portfolio** returned 2.36% (Mar: 1.28%). Top performer is Allan Gray (3.97%); while Stanlib (1.25%) takes the bottom spot. For the 3 month period Investec takes top spot, for the sixth consecutive month, outperforming the 'average' by roughly 1.6%. On the other end of the scale Prudential underperformed the 'average' by 0.80%.

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 Namibia Balanced Fund.

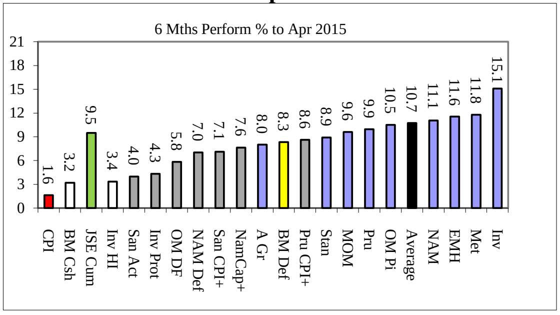
Below is the legend to the abbreviations reflected on the graphs:

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)
Investec Protector	Inv Prot (grey)
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)
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)

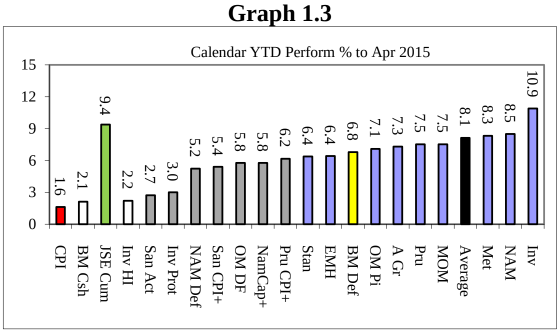
Graph 1.1



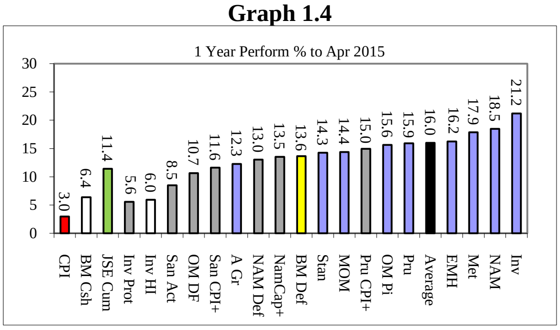
Graph 1.2



Graph 1.3



Graph 1.4



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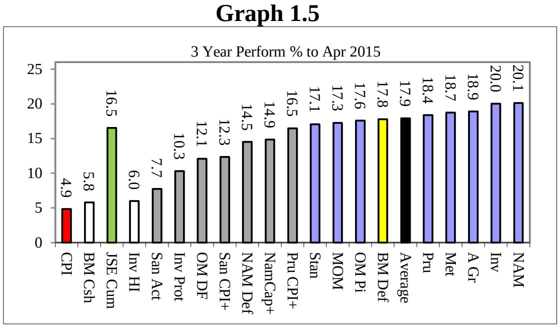
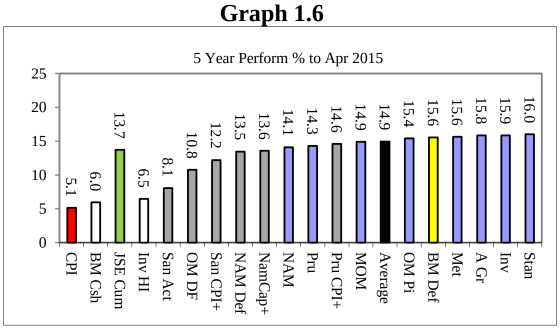
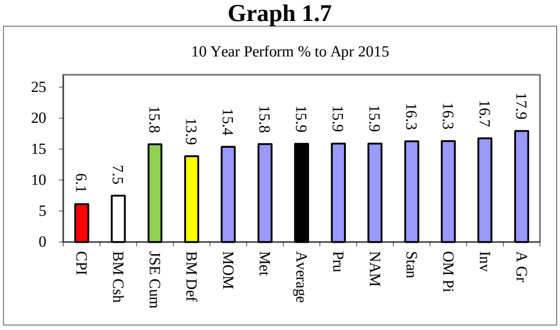
Graph 1.5



Graph 1.6

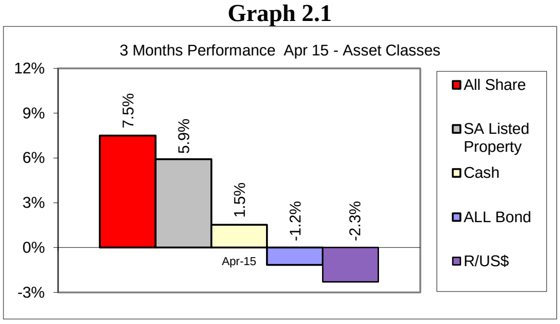


Graph 1.7

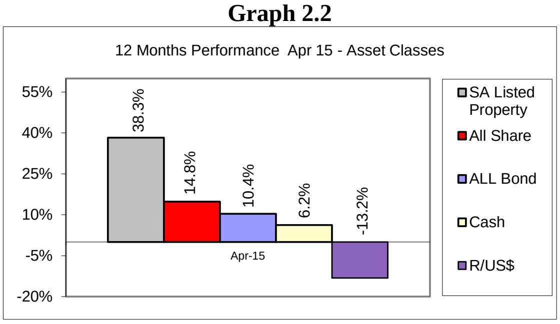


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

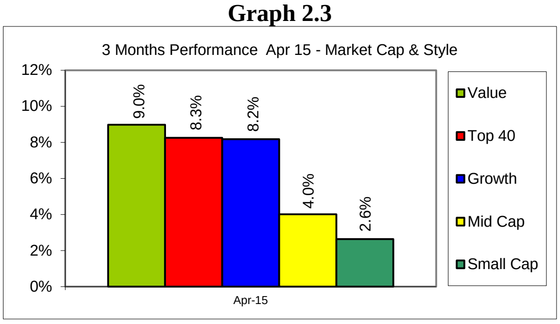
Graph 2.1



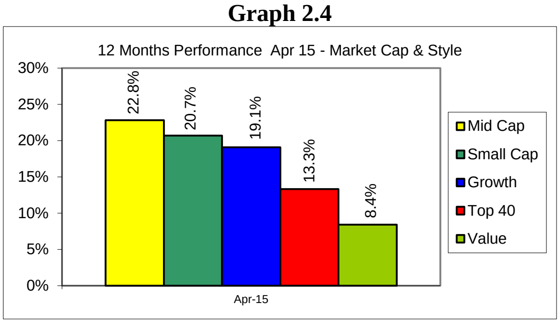
Graph 2.2



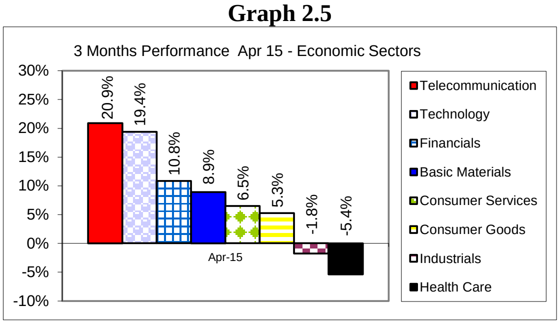
Graph 2.3



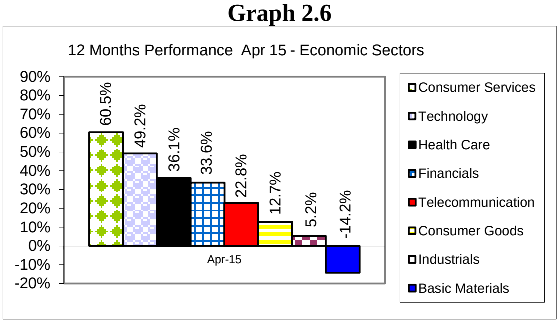
Graph 2.4



Graph 2.5



Graph 2.6



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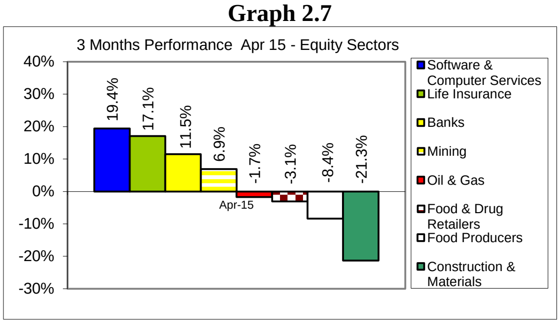
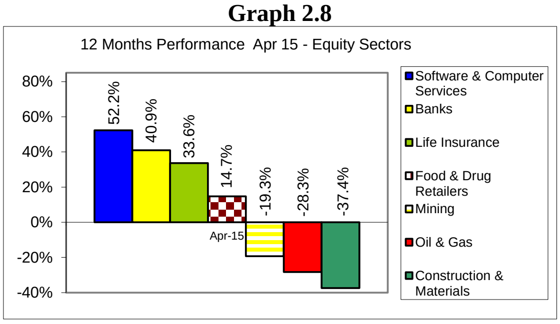
Graph 2.7



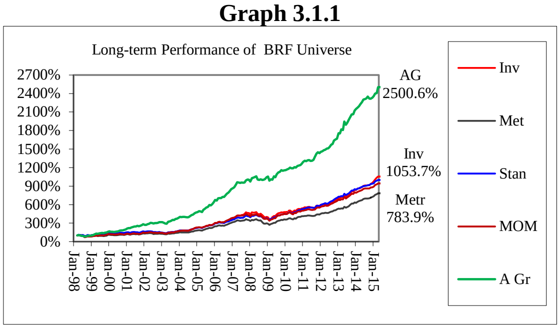
Graph 2.8



3. Portfolio Performance Analysis

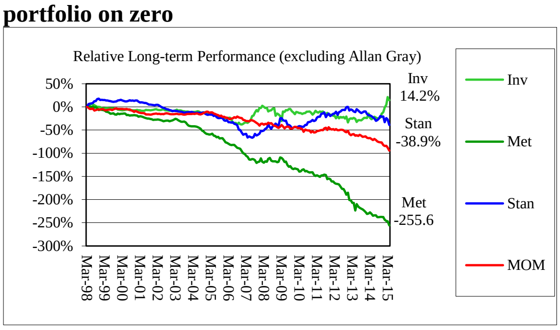
3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

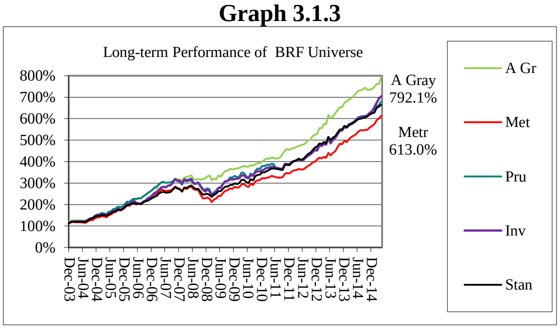


Graph 3.1.2

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

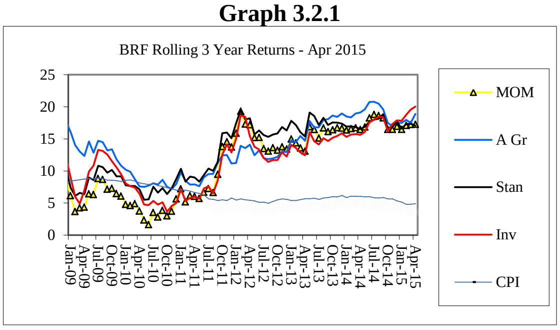


Graph 3.1.3

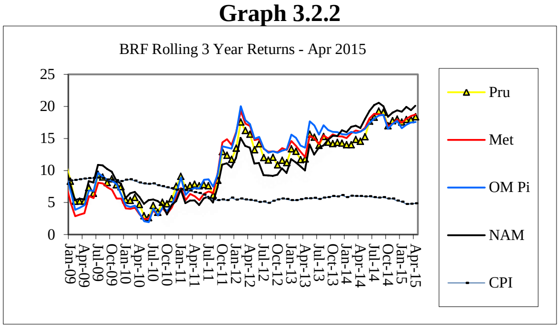


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1

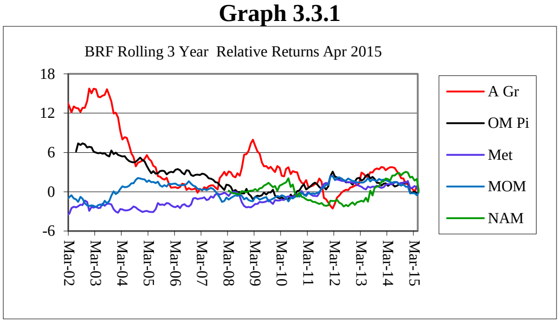


Graph 3.2.2



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

Graph 3.3.1



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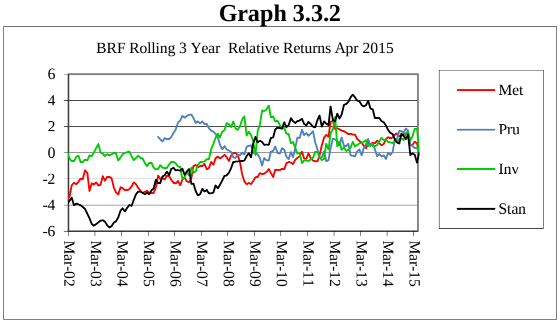
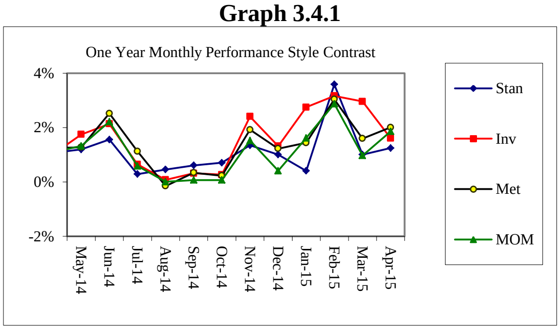
Graph 3.3.2

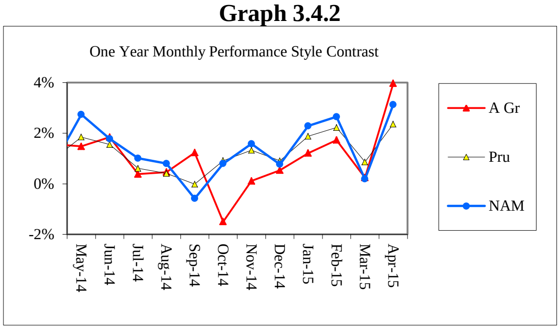


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

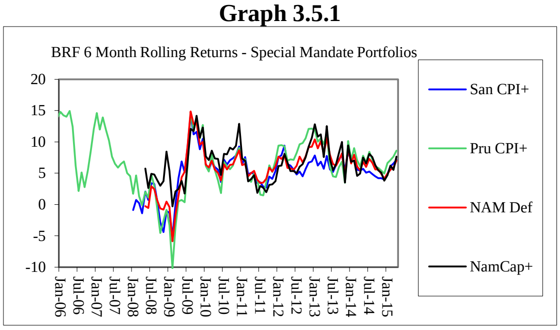


Graph 3.4.2

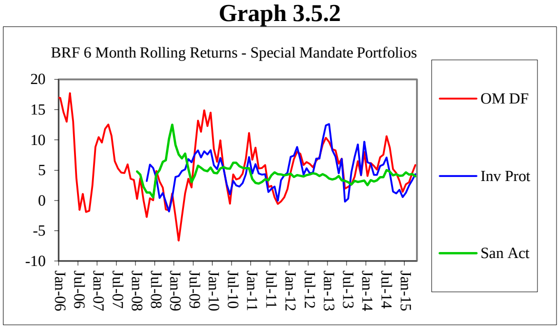


3.5. 6-month rolling returns of ‘special mandate’ portfolios

Graph 3.5.1

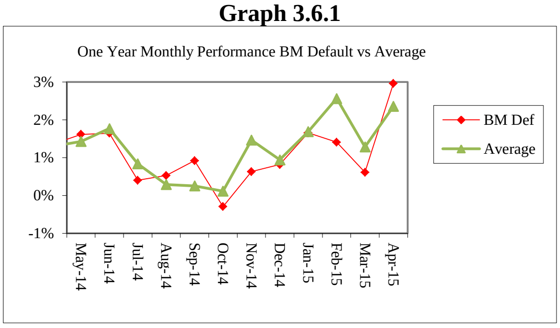


Graph 3.5.2

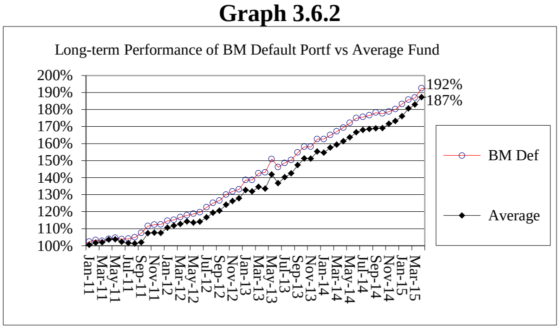


3.6 Monthly and cumulative performance of ‘Benchmark Default’ portfolio relative to average prudential balanced portfolio

Graph 3.6.1

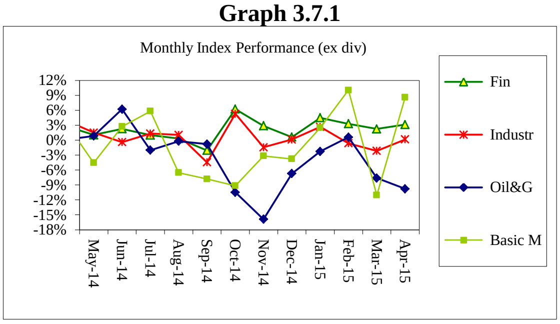


Graph 3.6.2



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

Graph 3.7.1



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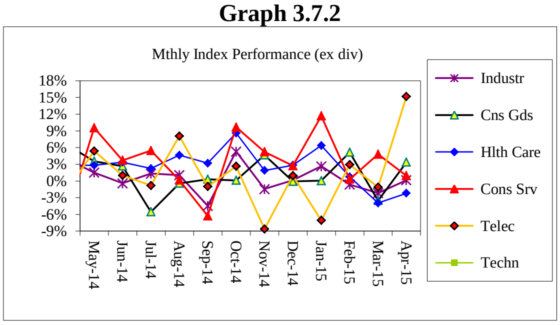
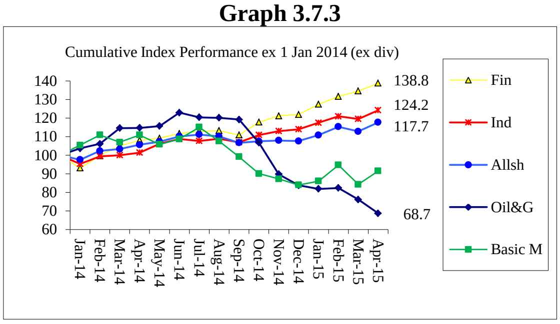
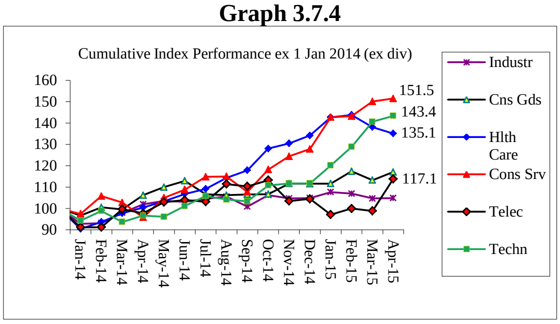
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio

Graph 1.6 shows that the average prudential balanced portfolio returned 14.9% p.a. in nominal terms, or 9.8% p.a. in real terms, over the past 5 years while the Benchmark Default portfolio returned 15.6% p.a. in nominal terms, or 10.5% p.a. in real terms. The Benchmark Default portfolio is designed to produce a less volatile performance but also lower returns than the average prudential balanced portfolios with its significantly lower equity exposure (49.8% vs. 61.8% of the average prudential balanced portfolio, as at the end of March 2015) and the lower risk it consequently entails for the investor. It should be expected to underperform the average prudential balanced portfolio at times when shares outperform other asset classes and vice versa.

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 exceeding the expected long-term goal significantly over the past 5 years.

We would in the long-term expect the Default portfolio to sacrifice around 1% return for the benefit of lower volatility compared to the average prudential balanced portfolio, thus an expected real return before management fees (typically 0.75%), of around 5% per year. Over the past 5 years this performance objective was exceeded noticeably.The default portfolio returned a cumulative 92.4% compared to 87.2% for the average prudential balanced portfolio over this 52 month period from January 2011 .

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 May 2012 to April 2015:

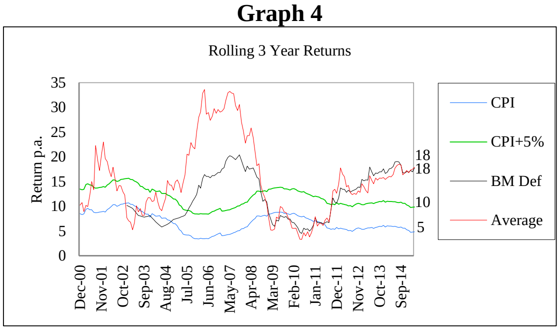
Table 4.1

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.3%	10.8%	9.4%
Best annual performance	6.4%	27.1%	25.0%
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	5.7%	17.8%	17.5%

The Benchmark Default portfolio is a more conservative investment portfolio 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

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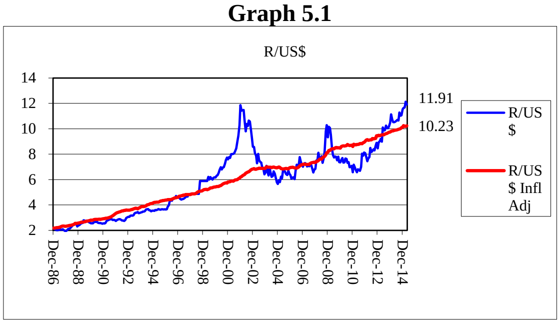
return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end April was 17.8%, the average was 17.9% vs CPI plus 5% currently on 9.9%.

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 fairly valued at 10.23 to the US Dollar while it actually stood at 11.91 at the end of April. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

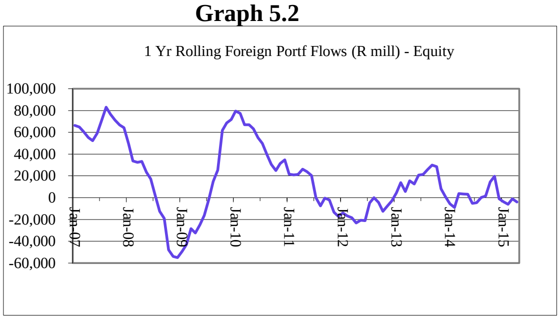
Graph 5.1



Rand supported by foreign capital inflows

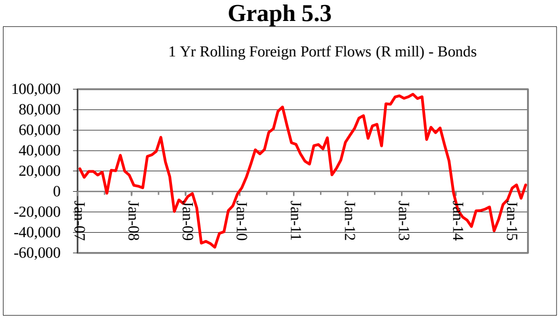
Graph 5.2 reflects a flow of capital out of South African equities on a rolling one year basis, with a net outflow of 4.0 bn on a year-on-year basis at the end of April (outflow of R 1.0 bn year-on-year to end March). The month of April experienced a net inflow of R 6.4 bn. Since the beginning of 2006, foreign net investment in equities amounts to R 182 bn (end March R 175 bn). This represents roughly 1.5% of the market capitalization of the JSE.

Graph 5.2



Graph 5.3 on a rolling one year basis reflects foreign portfolio inflows in respect of SA bonds of R 6.4 bn over the past 12 months to end of April (outflow of R 6.6 bn over the 12 months to end of March). Since the beginning of 2006, foreign net investment in bonds amounts to R 218 bn (to March just over R 199 bn). The month of April experienced a net intflow of R 17.4 bn.

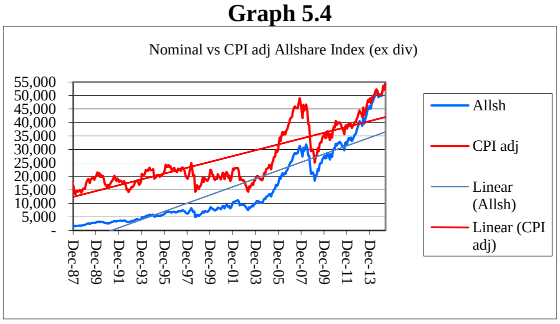
Graph 5.3



The net inflows of foreign capital from equity and fixed interest assets was R 2.4 bn for the 12 months to end April 2015 (outflow of R 7.6 bn to end March 2015), compared to an outflow of R 30.9 bn for the 12 months to end April 2014 (outflow of R 24.2 bn to end of March 2014). Since the beginning of 2006, total net foreign portfolio inflows amounted to R 399 bn (March R 375 bn).

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 12.4% per year since January 1987, and this excludes dividends of 3%. Namibian inflation over this period of just over 28 years was 8.5% per year. This is equivalent to a growth in real terms of 3.9% p.a. over this period, excluding dividends, or around 7% 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 7.4% per annum, over this period of just over 28 years. US inflation over this period was 2.7%. This is equivalent to a growth in real terms of 4.7% p.a. over this period, excluding dividends.

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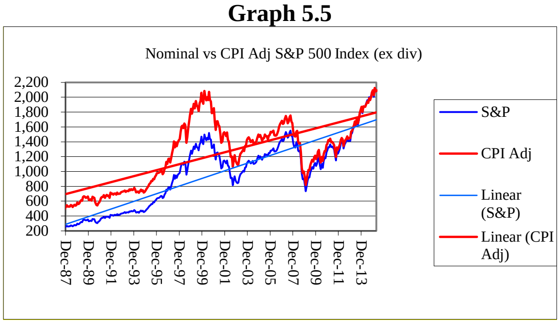
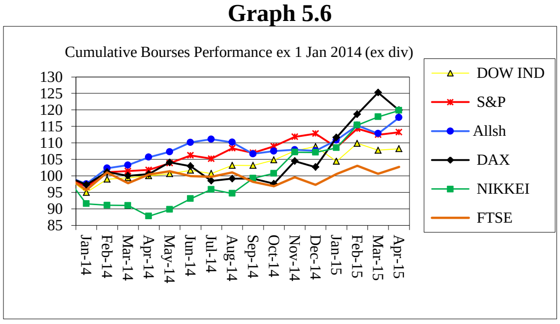
Graph 5.5



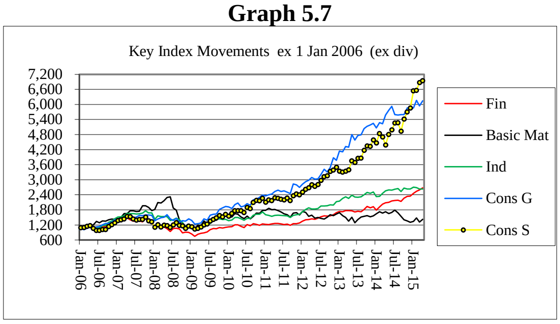
Graph 5.6 provides an interesting overview of some of the major global share indices, showing up the DAX, and the NIKKEI as the top performing share indices.

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: 23.1%; Consumer Goods 21.5%; Financials 11.1%; Industrials 10.9%; and Basic Materials 3.9%.

Graph 5.7



6. Global market sailing in calmer waters

As in the previous month, there has once again been very little change in some of the key global economic indicators during April. WTI (West Texas Intermediate) oil price in US$ increased by 17%, but as the result of the strengthening of the Rand against the US$ by 2% from 12.14 to 11.91, it only increased by 15% in Rand terms from R 593 to R 681. 12 Month foreign investment portfolio flows and the SA trade balance have changed insignificantly over the month, but represent a significant outflow of R 105 billion over the past year. Of course we know that interest rates have not changed either overseas or in SA, and the imminence of the US repo rate changing is as far or as close as it was 6 months ago.

Investment markets are currently very much a hostage of global monetary policy and market movement is a function of how much money is pumped into the system, for how long, by central banks. Although the US economy started to respond positively to the Fed's stimulus measure, it seems as if the phasing out of these measures has put the economic recovery into a wobble the final direction of which is not clear at this stage.

Tracking the performance of the Japanese Nikkei and the German Dax as reflected in graph 5.6 above, the impetus of the quantitative easing programmes are quite evident and the SA equity market has been the beneficiary of some overflows. Markets and currencies will remain a hostage of these intervention programmes for some time to come.

The termination of quantitative easing in the US followed by the introduction of quantitative easing by the ECB and continued money printing by the BOJ resulted in the general strengthening of the US$ against other currencies, amongst others the Rand. By our measure it should be on about 10.2 as opposed to the actual exchange rate of 11.9.

Will the Rand be able to recover to a more realistic value? As we have reported above, foreign investors have all but disappeared from the SA market while the trade balance is in negative territory. China, as major consumer of SA commodities is busy restructuring its economy and GDP is in reverse gear offering no hope to SA for improving commodity export volumes. In addition, the World Bank is expecting all main commodity price indices to decline in 2015. In fact metals and agriculture is expected to then move sideways until 2020 while only energy prices are forecast to experience a slight recovery until 2020. So there will be no saving grace for SA for yet a while, no significant support for the Rand or for any delayed increase in interest rates should the Fed decide to raise its repo rate. In addition SA is of course struggling with its power supply that does not exactly support an export driven economic expansion.

As suggested in our previous newsletter, the only alternative for investors currently is to weather the period of quantitative easing employed in the Eurozone and Japan. This means that we will see no major changes in monetary policy probably until early to middle of 2016. To ease over–indebted developed countries out of their debt problem, any evolving economic growth is likely to be retarded by a simultaneous increase in interest rates.

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By T H Friedrich – Managing Director, Retirement Fund Solutions Namibia (Pty) Ltd

This scenario would mean that we will move into a cycle of gradually and slowly increasing interest rates over an extended period, slow economic growth and gradually increasing inflation. As a result equity markets are likely to experience only pedestrian performance for years to come, but one should at least expect low real returns as opposed to fixed interest investments that will be shunned until rates have reached normal levels once again.

On this basis we do not expect any major swings in investment market for the next 2 years plus, given no political upheavals impacting investment markets.

Our investment view remains unchanged

In this phase of economic adjustment the local investor should invest in equity and property in preference to fixed interest assets, talking only about conventional asset classes. Stock picking should prove to make the difference in returns and will be a prerequisite for out-performance of a portfolio.

Investors should forget about double digit annual return and focus on investing to out-perform inflation. With an inflation rate in the region of 4%, the investor should be comfortable with a return of between 4% and 10% p.a. over the next few years.

With the expected upswing in consumer sentiment over the next year or two, one should see the demand for consumer goods and hence commodities increasing again. A weakening Rand and a depressed local economy suggest that the investor should continue to diversify offshore. An investment in depressed foreign economies and bourses should be biased towards the consumer while any investment in stocks on bourses already at high levels should focus on finding value rather than on any particular sector.

On the basis of fundamentals, local sectors and shares driven by foreign investors over the past few years, such as consumer goods and consumer services should now be switched for those shunned by them, primarily basic materials, financials and industrials. From a macro economic perspective the weakening Rand should advantage Rand hedge shares, exporters and manufacturers locally.

7. Important notice and disclaimer