Volume 11, No. 09,
September 2015

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 SEPTEMBER 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

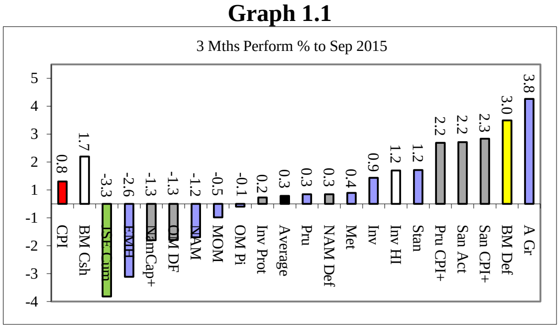
In **September** the **average prudential balanced portfolio** returned -0.39% (Aug: -0.83%). Top performer is Allan Gray (1.04%); while Momentum (-1.01%) takes the bottom spot. For the 3 month period Allan Gray takes top spot, outperforming the 'average' by roughly 3.5%. On the other end of the scale EMH Prescient underperformed the 'average' by 2.9%.

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.

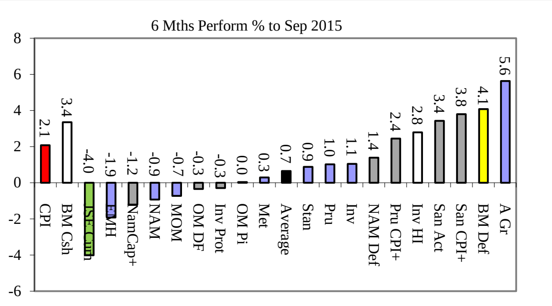
Below is the legend to the abbreviations reflected on the graphs:

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)

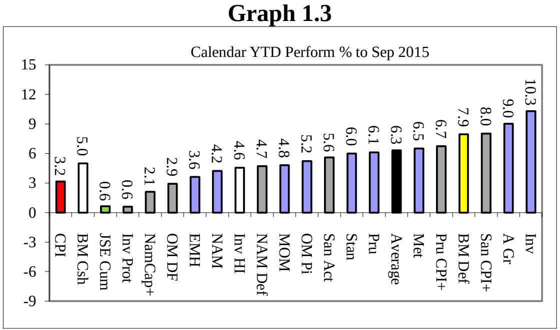
Graph 1.1



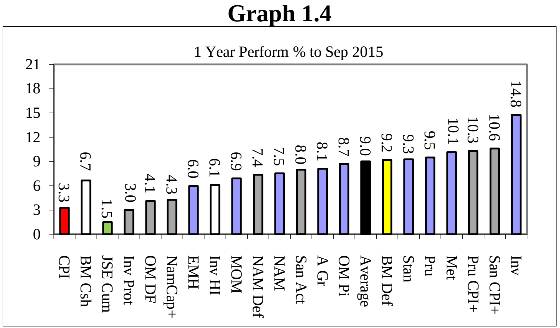
Graph 1.2



Graph 1.3



Graph 1.4



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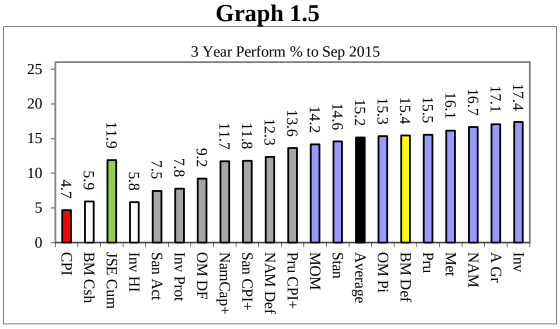
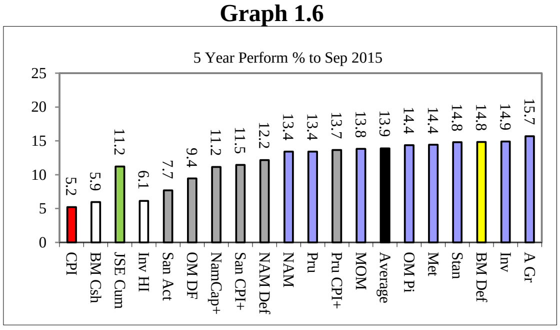
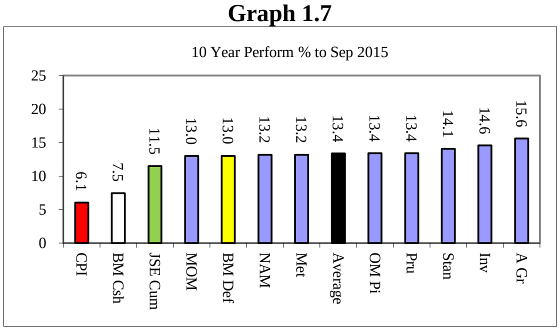
Graph 1.5



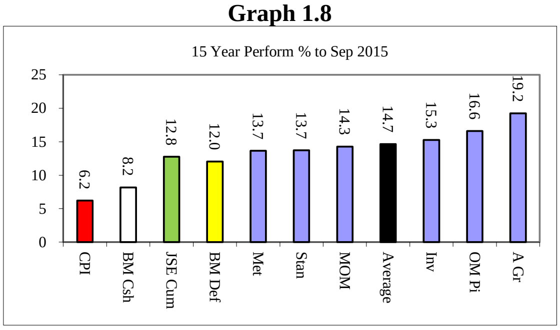
Graph 1.6



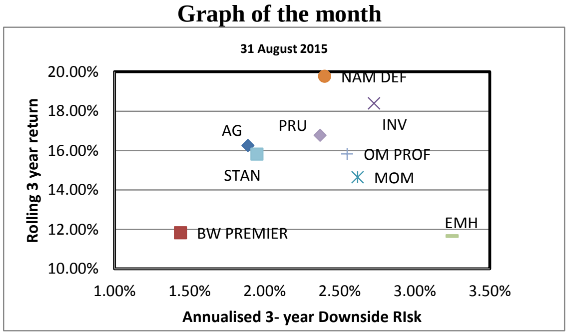
Graph 1.7



Graph 1.8

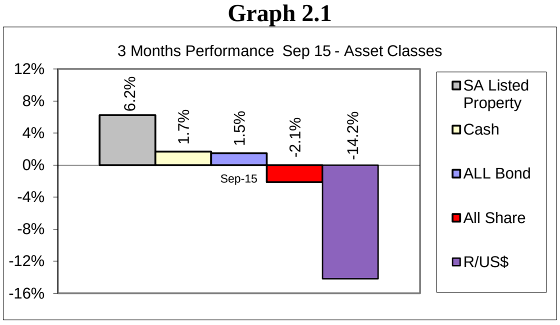


Graph of the month

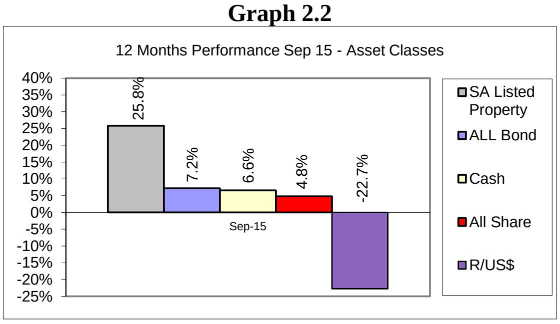


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

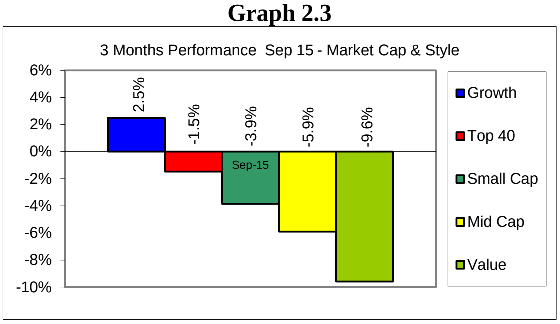
Graph 2.1



Graph 2.2



Graph 2.3



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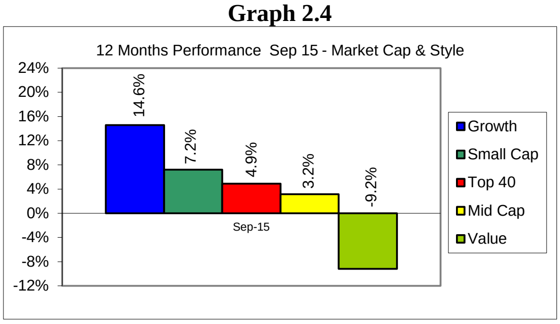
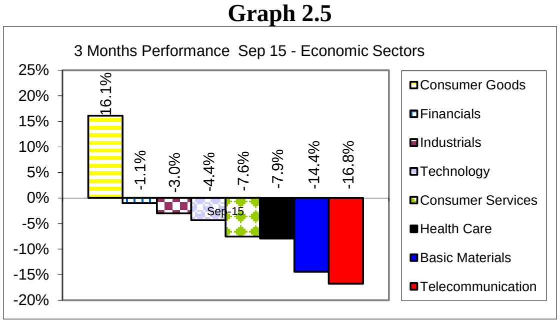
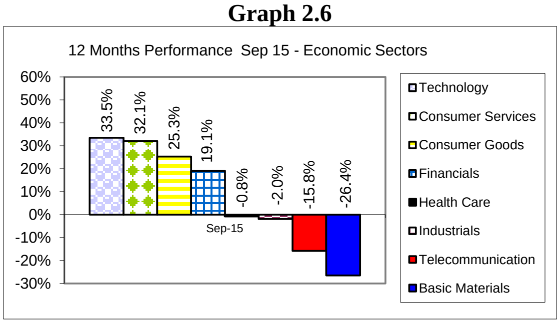
Graph 2.4



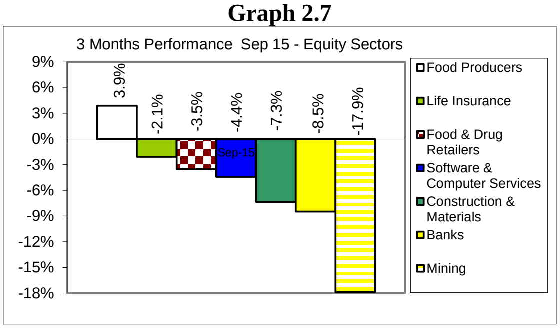
Graph 2.5



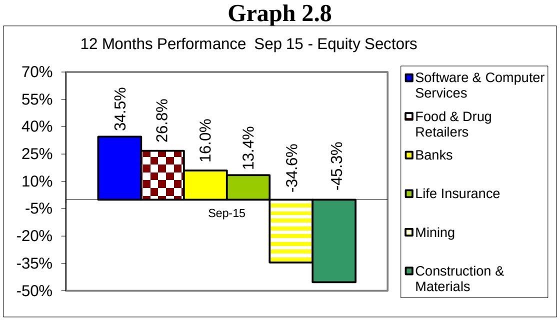
Graph 2.6



Graph 2.7



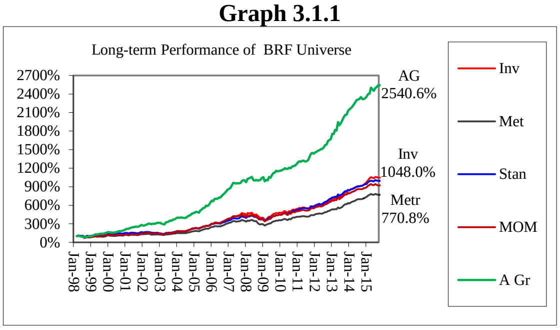
Graph 2.8



3. Portfolio Performance Analysis

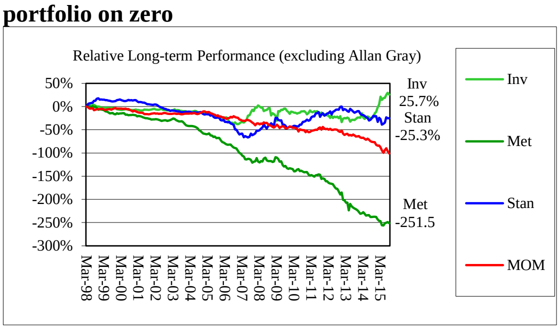
3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

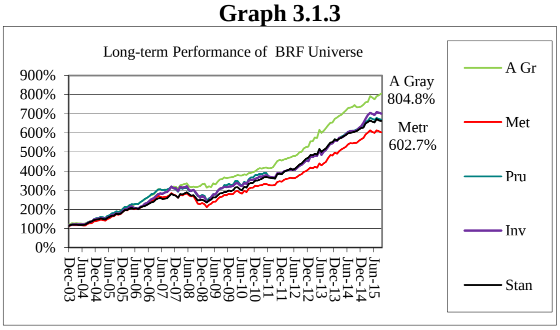


Graph 3.1.2

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

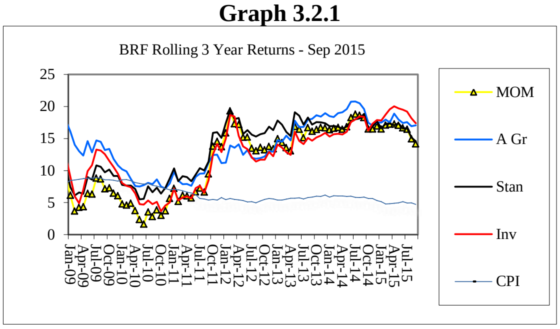


Graph 3.1.3



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

Graph 3.2.1



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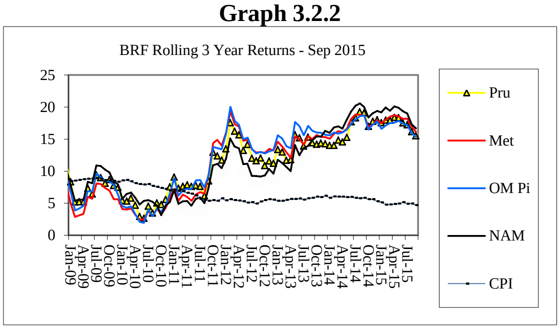
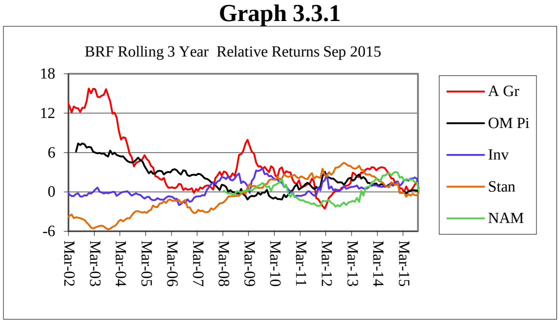
Graph 3.2.2

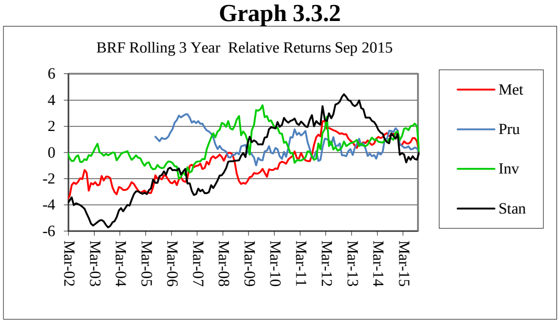


3.3. 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

Graph 3.3.1

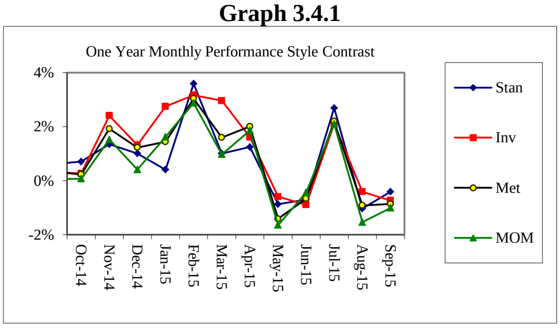


Graph 3.3.2

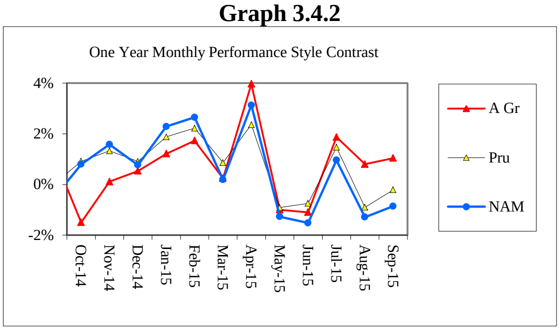


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

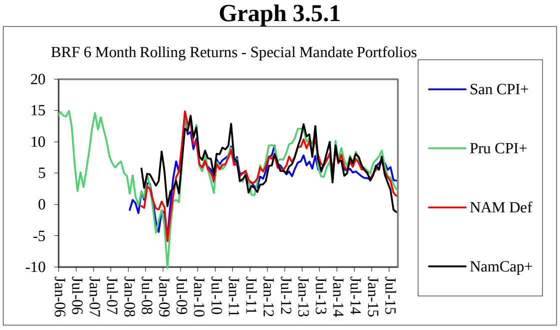


Graph 3.4.2

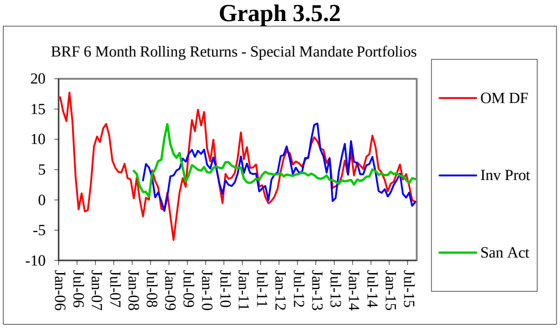


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

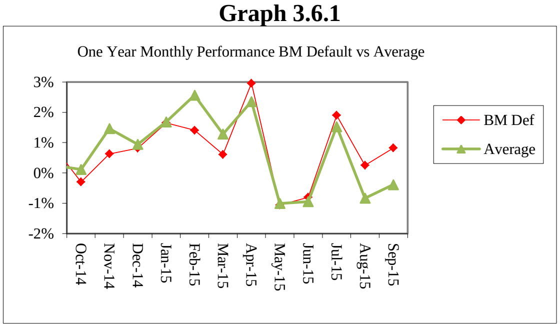


Graph 3.5.2



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

Graph 3.6.1



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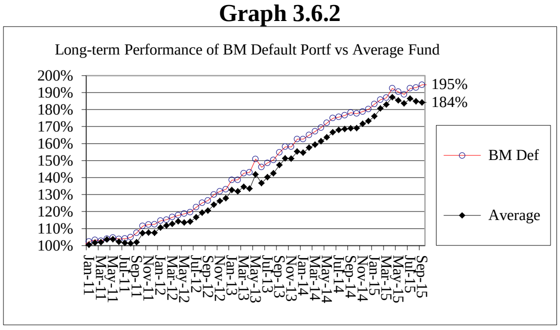
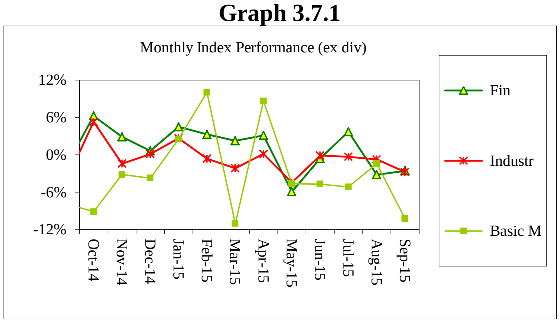
Graph 3.6.2

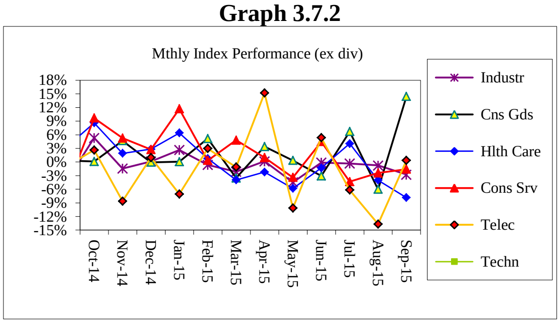


3.7 One year monthly performance of key indices (excluding dividends)

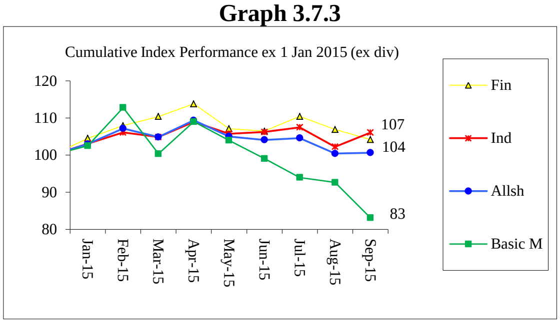
Graph 3.7.1



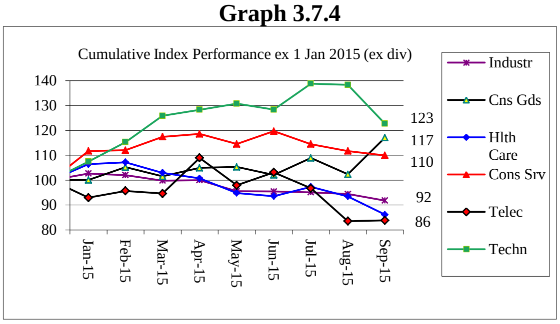
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio – Facts in figures

Table 4.1

Portfolio	Default portfolio	Average pru man portfolio
5 year nominal return - % p.a.	13.9	13.9
5 year real return - % p.a.	9.6	8.7
Equity exposure - % of portfolio	47.3	62.0
Cumulative return ex Jan 2011	94.5	84.1
5 year gross return target - % p.a.	5	6
Target income replacement ratio p.a.	2	2
Required net retirement contribution - % of salary	13.0	11.6

The above table reflects the actual returns 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.

Table 4.2

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	5.3%	8.0%	9.0%
Best annual performance	6.7%	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	5.8%	16.8%	17.0%

The table above presents one year performance statistics. It highlights the performance differences between the 3 portfolios over the 3 years October 2012 to September 2015. This gives an indication of volatility of the performance of these 3 risk profiles.

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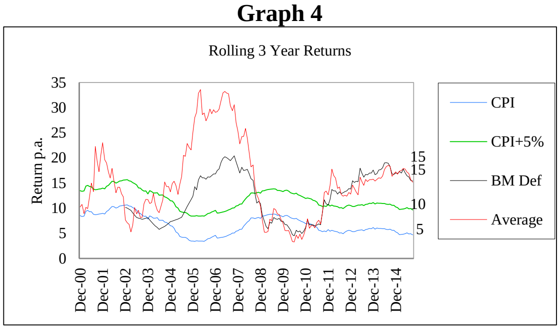
Graph 4



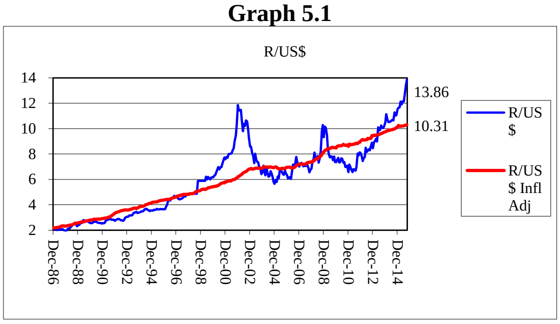
Graph 4 measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end September was 15.4%, the average was 15.2% vs CPI plus 5% currently on 9.7%.

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 10.31 to the US Dollar while it actually stood at 13.86 at the end of September. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

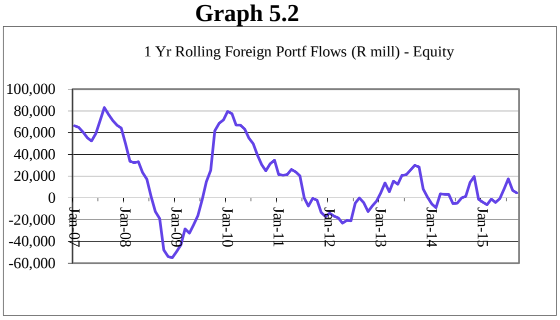
Graph 5.1



Rand continues to weaken with foreign capital outflows

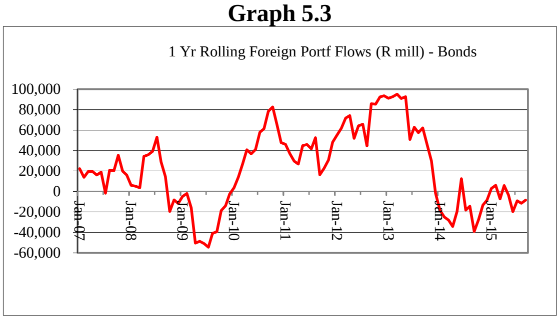
Graph 5.2 reflects a flow of capital into South African equities on a rolling one year basis, with a net inflow of 4.6 bn on a year-on-year basis at the end of September (inflow of R 6.8 bn year-on-year to end August). The month of September experienced a net outflow of R 0.08 bn. Since the beginning of 2006, foreign net investment in equities amounts to R 202 bn (end August R 202 bn). This represents roughly 1.7% 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 8.4 bn over the past 12 months to end of September (outflow of R 11.5 bn over the 12 months to end of August). Since the beginning of 2006, foreign net investment in bonds amounts to R 208 bn (to August just over R 215 bn). The month of September experienced a net outflow of R 6.2bn.

Graph 5.3



The net outflows of foreign capital from equity and fixed interest securities was R 3.8 bn for the rolling 12 months to end September 2015 (outflow of R 4.7 bn to end August 2015), compared to an outflow of R 37.7 bn for the 12 months to end September 2014 (outflow of R 14.4 bn to end of August 2014). Since the beginning of 2006, total net foreign portfolio inflows amounted to R 411 bn (August R 417 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 11.9% per year since January 1987, and this excludes dividends of 3%. Namibian inflation over this period of just over 28 years was 8.4% per year. This is equivalent to a growth in real terms of 3.5% p.a. over this period, excluding dividends, or around 7% including dividends.

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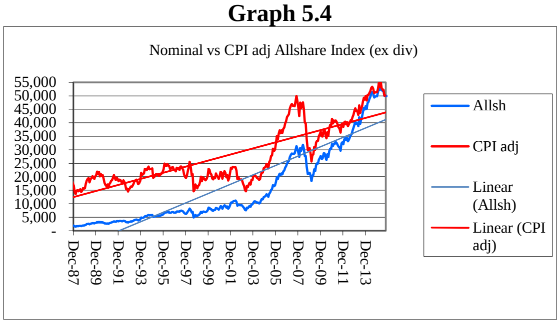
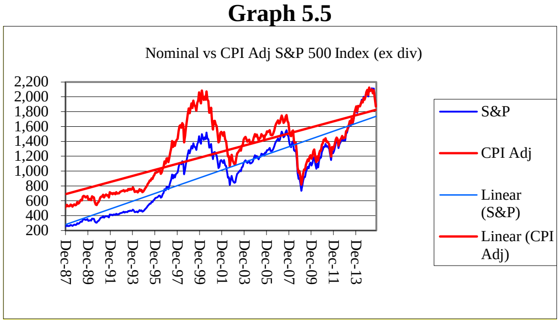
Graph 5.4



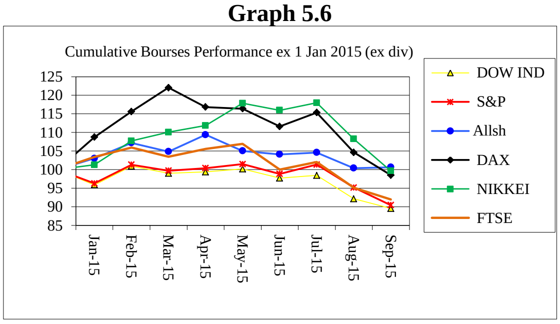
Graph 5.5 reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 6.9% per annum, over this period of just over 28 years. US inflation over this period was 2.7%. This is equivalent to a growth in real terms of 4.2% p.a. over this period, excluding dividends.

Graph 5.5



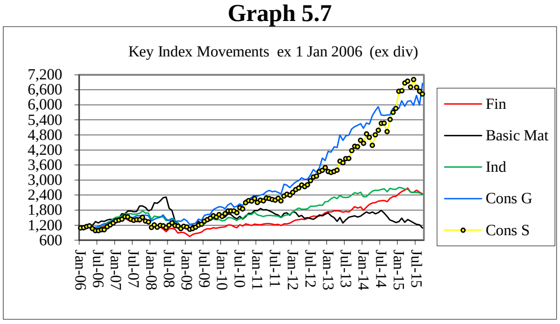
Graph 5.6 provides an interesting overview of some of the major global share indices, showing up the Allshare and the NIKKEI as the top performing share indices.

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 Goods: 21.8%; Consumer Services 21.0%; Financials 9.6%; Industrials 9.5%; and Basic Materials 0.9%.

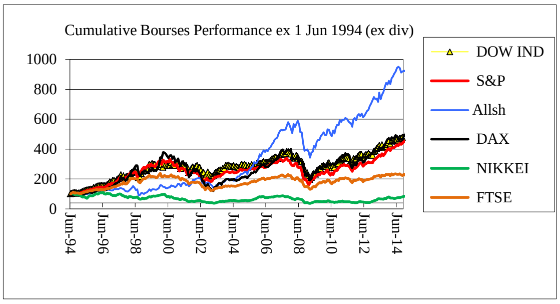
Graph 5.7



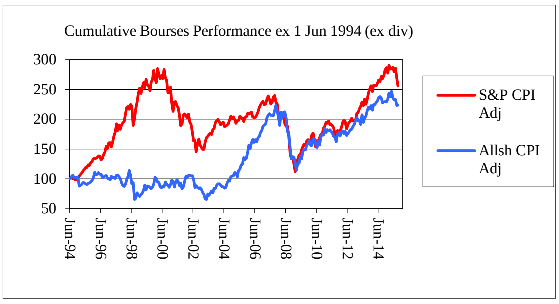
6. Don't lose perspective

By Tilman Friedrich

With information technology having managed to create a network of instant information flow across the globe, it is commonly accepted that we all suffer from information overload. We are losing perspective and in consequence are exposed to making conclusions and decisions based on a distorted view of developments in global financial markets. Take the following graph –



It depicts the movement of a number of large global stock exchanges. It's a very busy graph despite only covering 6 stock exchanges. But at first sight it may lead one to identify 3 trends. Firstly on the downside, the Nikkei that has not moved anywhere over this period of over 20 years and secondly, on the upside, the JSE Allshare Index that was in a flying mode. But look at the next graph for perhaps a bit more perspective –



Here we have only the Allshare measured against the US S&P 500 that is in the middle of the crowd in the top graph. This graph now removes the impact of inflation

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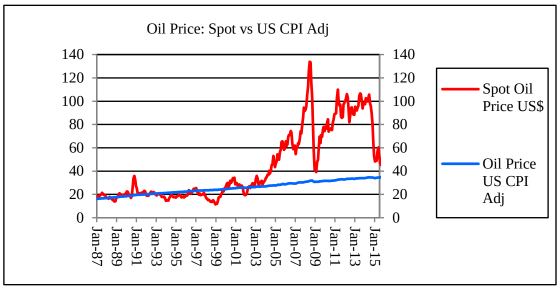
that can distort the picture significantly as one can see from comparing these two graphs. Now the Allshare has actually de-linked from the S&P 500, having been quite closely aligned from 2007 until 2012, but both trend lines are still very similar. So, we can now conclude that the Allshare has actually not become airborne as the top graph seems to indicate but has been moving very much in line with other bourses, except that the local inflation rate has been substantially higher throughout. Can we say that both markets are expensive? Well what should be driving stock prices, if anything? Talk to any business person and he will tell you that their business should grow at least in line with the economy. The S&P 500 index insinuates that the economy has grown by 4.5% per annum over this 20 year period while the Allshare index suggests that the economy has grown by only 3.9% per annum. It is probably true that these figures are not directly comparable as SA listed companies are probably serving a different economy than US listed companies, latter being much more globally focused. We would argue that these two bourses may be expensive but they are certainly not ridiculously expensive based on what this graph allows one to conclude.

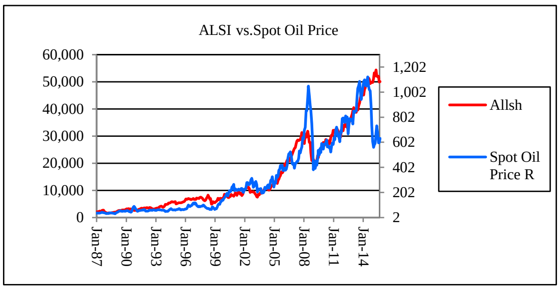
Now let's turn to oil, the commodity with the biggest impact on global financial market. At its current price of US$ 50 per barrel, the global oil market is equivalent to around 2.5% of the global GDP. At its peak of US$ 140, it was equivalent to close to 7% of global GDP. GDP being a function of money supply and the velocity of money flows, the steep increase of the oil price certainly heated up the global economy while its more recent decline will obviously have the opposite impact.

The following graph reflects the spot oil price as against the oil price of 1987 adjusted for US CPI.



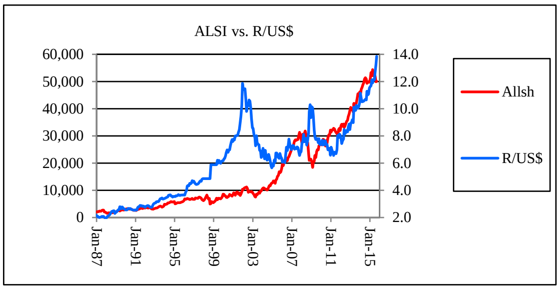
One may conclude from this graph that there was a close correlation between the CPI adjusted price of oil at its 1987 level and the market price until around 2003 when became airborne for reasons we have been speculating on in previous newsletters, until it started its steep decline in the middle of 2013. If one gives the CPI adjusted price the benefit of the doubt of it not fully reflecting all cost drivers in the oil industry, one can conclude that at current levels, it has reached a fair level relative to its 1987 level.

As suggested above, oil is a key driver of the global economy and should thus also be a key driver of global bourses. The following graph considers this assertion.



Clearly, the SA Allshare index has been very, very closely correlated to the oil price, adjusted for the depreciation of the Rand over this 29 year period, until the bottom fell out of the oil price in the middle of 2013. What can we deduce from this picture? If the Allshare index will revert to being closely correlated and if the oil price currently reflects a normal price level, the Allshare should decline to 30,000 from its current level of 50,000. This sounds quite far-fetched although it will be difficult to fault the principles. Let's assume then that the Allshare will rather takes a breather until the oil price in Rand has caught up again as the result of a gradual depreciation of the Rand and the increase in the cost of producing oil at a rate of 5.5% per annum, taking the past year as our point of reference. What will this mean? It will mean that it will take about 12 years until the two trend lines are in synch once again! The oil price in Rand will then be around R 1,100 per barrel as opposed to its current price of around N$ 650.

Finally let's look at another key economic indicator, the Rand/ US$ exchange rate and try to make some assertions on this. The below graph depicts that Allshare index and the Rand/ US$ exchange rate –



Interestingly these two lines are also very closely correlated for most of the time. Having concluded from the previous graphs that the Allshare index could decline to 30,000 this graph tells us that if this were to happen the Rand could strengthen to 8. Let's once again say this is far-fetched and believe correction will only happen through the correction of the oil price in Rand taking the past 12 months as frame of reference for its future trend. In 12 years' time when the Rand price of oil has caught up with and Allshare index of 50,000, the Rand is expected to have depreciated to around 22 to the US$.

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 SEPTEMBER 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.

The question is whether we will face a 12 years' catch-up game or whether there is anything else that can accelerate the flow of money and get the global economy going again? Interest rates are extremely low, so is inflation while consumption is simply not responding to the massive money supply into the financial markets since the financial crisis. Things being as they are, the accelerator function of oil does not offer an effective mechanism. It's hard to think of any other commodity of global dimensions that will achieve this result without any massive upheaval - or is this what we are witnessing with the massive refugee crisis in Europe, the human labour commodity?

Conclusion

Nothing in the global economy has changed fundamentally since last month's newsletter. It appears that central banks have spent their last arrow in the quiver in terms of promoting global growth and there is nothing we can see at this point of time that will get global growth going once again. The investor should therefore continue to focus on real returns rather than absolute returns to increase his wealth slowly and steadily. With an inflation rate of around 3% one should be quite content if one manages to achieve an investment return around 8% per annum. The investor's investment time horizon is an important consideration. As an active fund member one should not shun equities but should be cautious, spread the risks as far as the law allows and focus on stock picking.

7. Important notice and disclaimer