Benchmark Retirement Fund

Volume 12, No. 5,
May 2016

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 MAY 2016

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

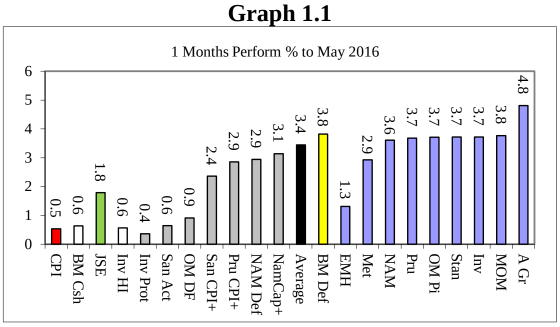
In **May** the **average prudential balanced portfolio** returned 3.44% (Apr: 0.12%). Top performer is Allan Gray (4.81%); while EMH (1.31%) takes the bottom spot. For the 3 month period Namibia Asset Management, takes top spot, outperforming the 'average' by roughly 2.8%. On the other end of the scale EMH underperformed the 'average' by 3.0%.

Graphs 1.1 to 1.9 reflect the performance for periods from 1 month to 15 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.

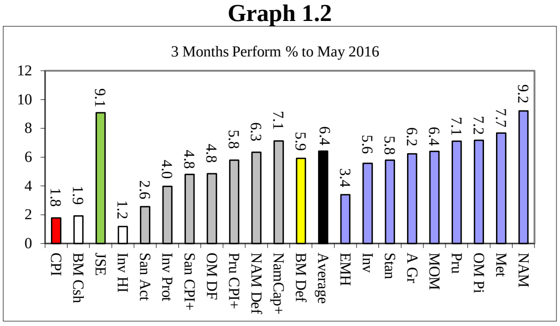
Below is the legend to the abbreviations reflected on the graphs:

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)
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)

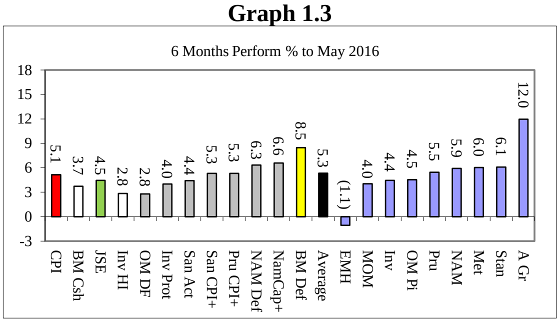
Graph 1.1



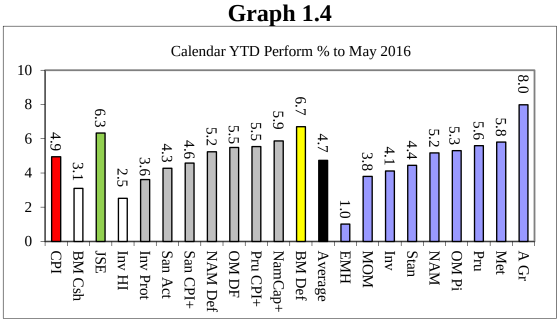
Graph 1.2



Graph 1.3



Graph 1.4



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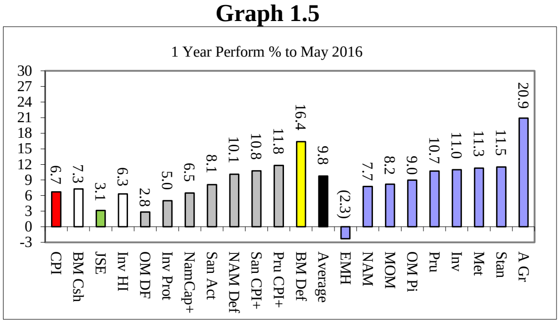
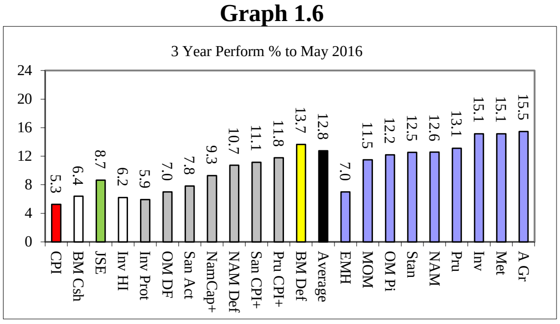
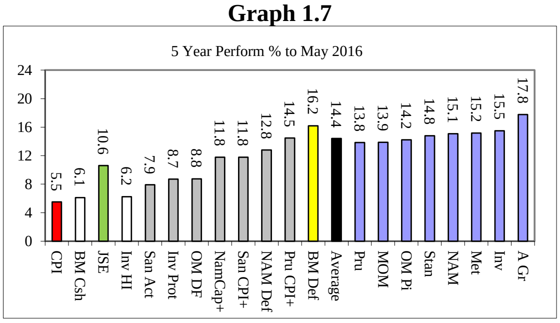
Graph 1.5



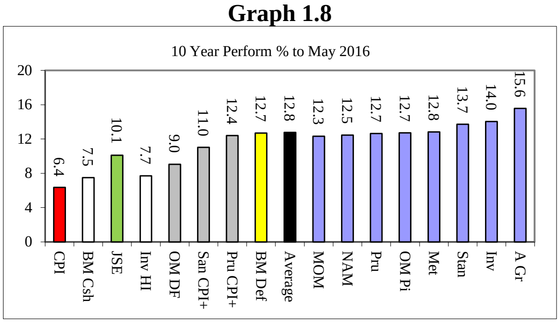
Graph 1.6



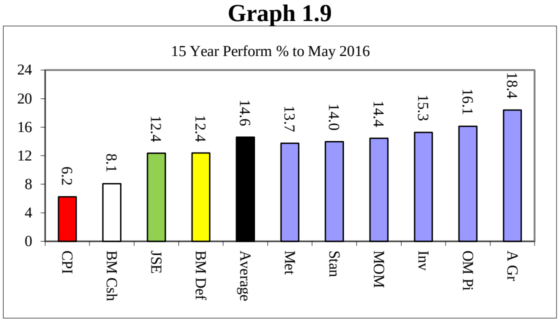
Graph 1.7



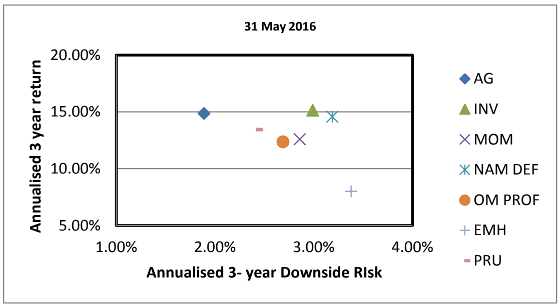
Graph 1.8



Graph 1.9

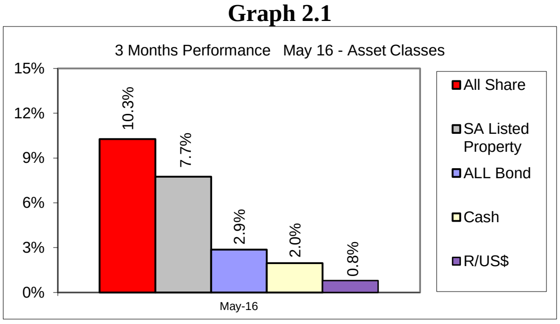


Risk/ Return

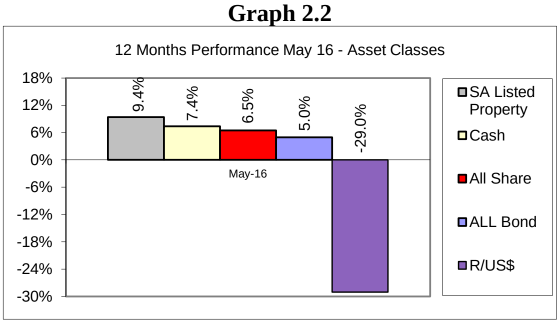


2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

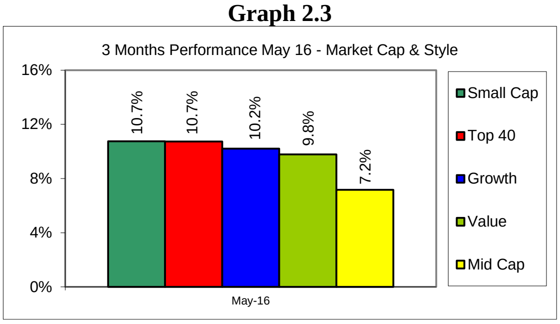
Graph 2.1



Graph 2.2



Graph 2.3



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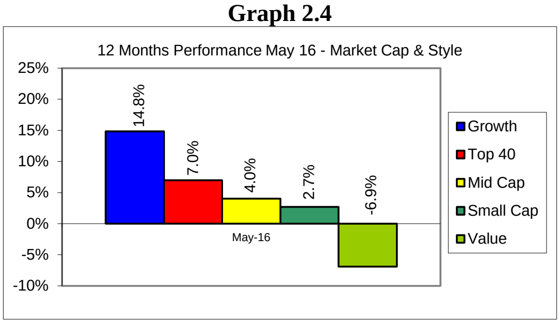
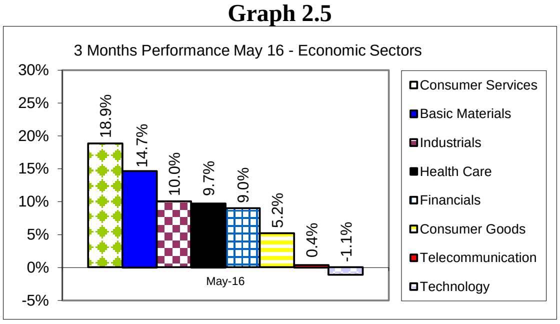
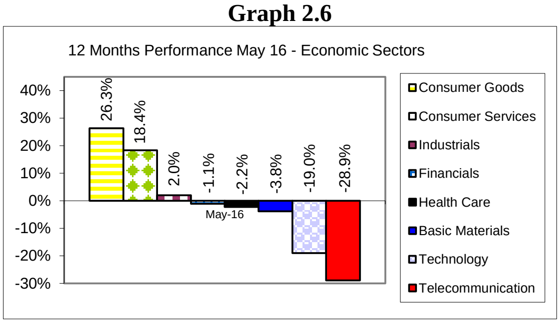
Graph 2.4



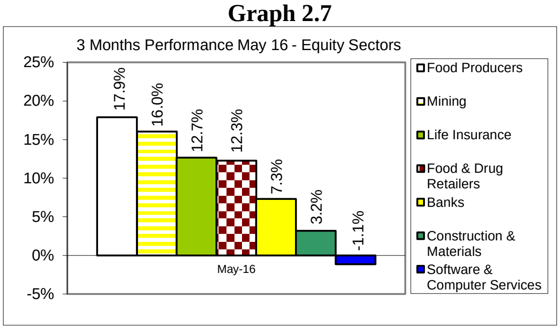
Graph 2.5



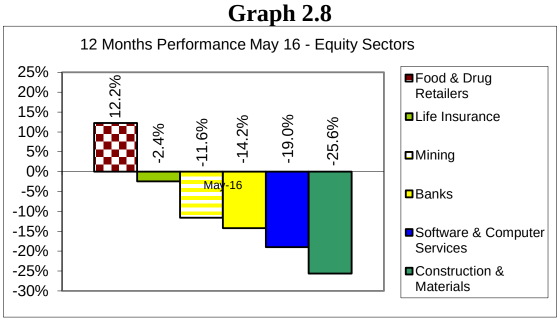
Graph 2.6



Graph 2.7



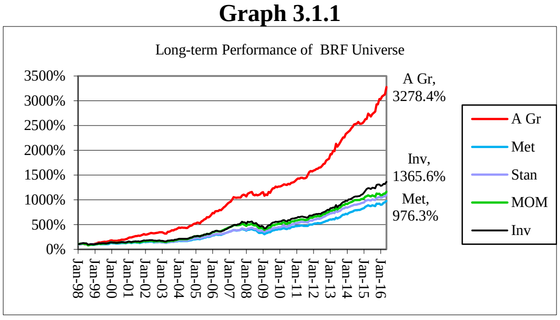
Graph 2.8



3. Portfolio Performance Analysis

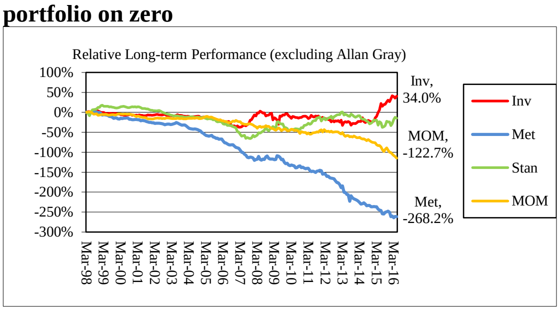
3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

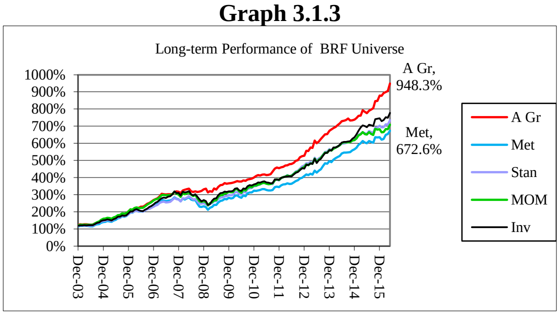


Graph 3.1.2

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

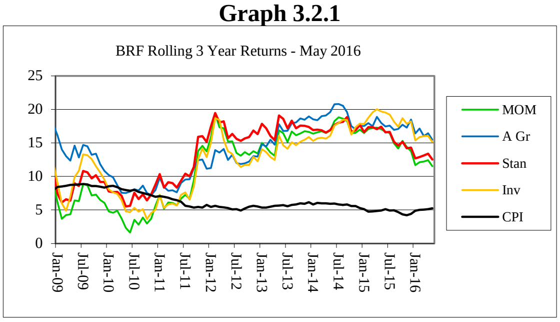


Graph 3.1.3



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

Graph 3.2.1



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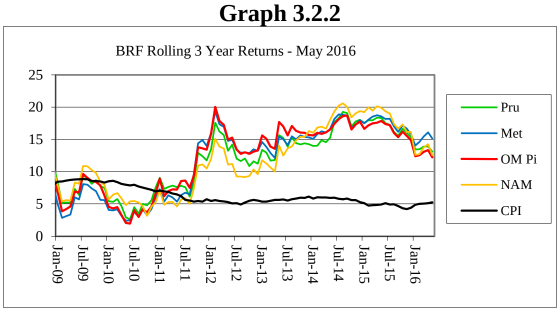
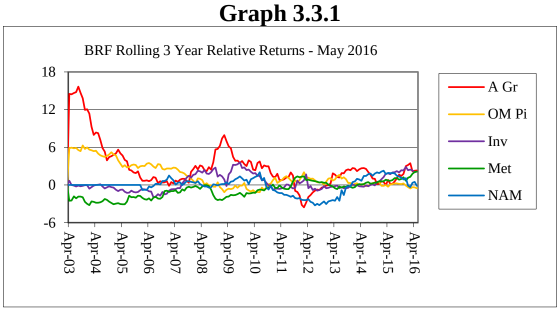
Graph 3.2.2

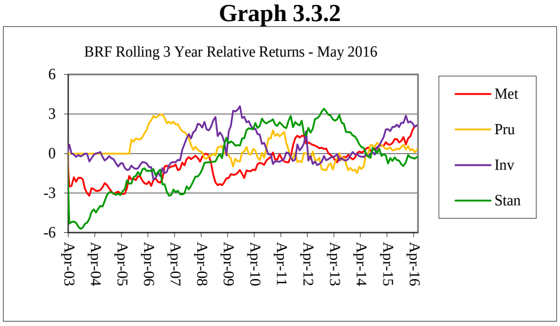


3.3. 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

Graph 3.3.1

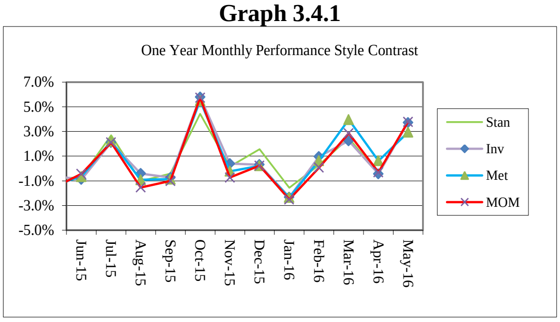


Graph 3.3.2

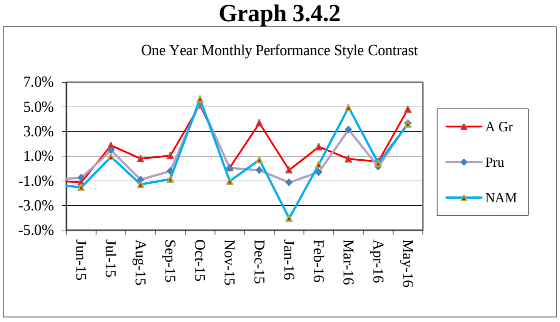


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

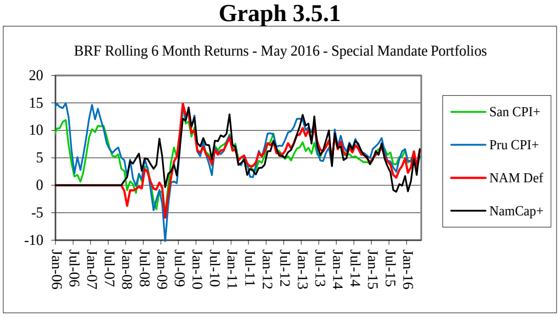


Graph 3.4.2

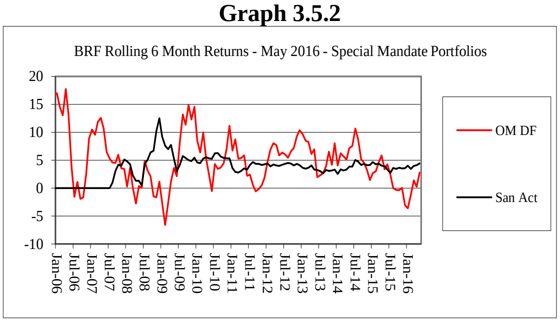


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

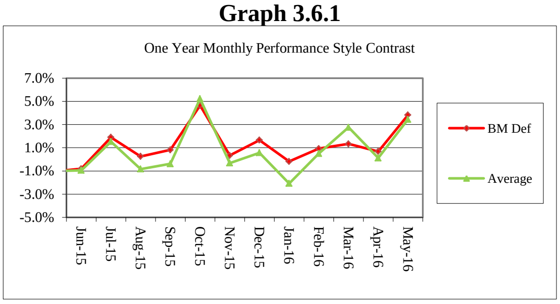


Graph 3.5.2



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

Graph 3.6.1



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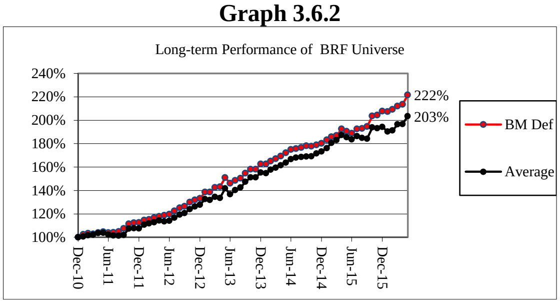
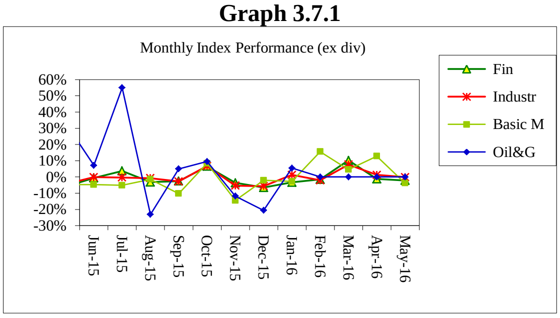
Graph 3.6.2

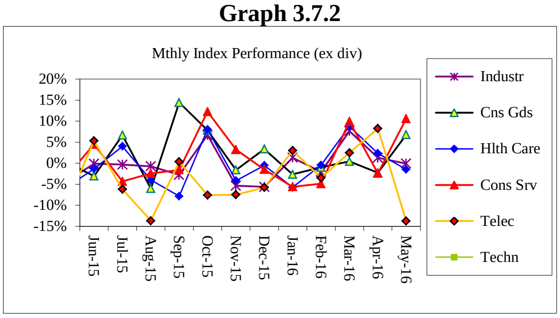


3.7 One year monthly performance of key indices (excluding dividends)

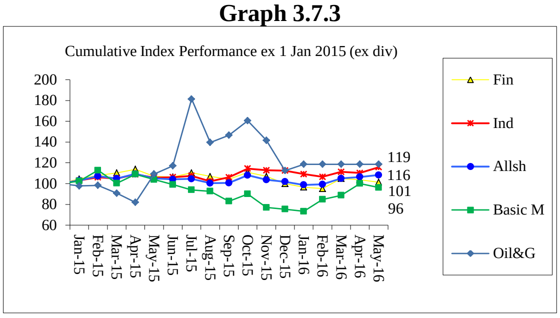
Graph 3.7.1



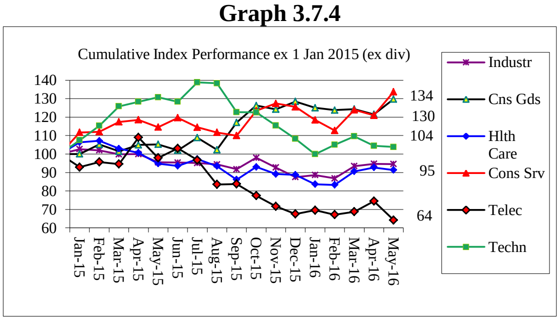
Graph 3.7.2



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.	16.2	14.4
5 year real return - % p.a.	10.7	8.9
Equity exposure - % of portfolio	49.7	55.9
Cumulative return ex Jan 2011	121.6	103.5
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 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	5.6%	13.7%	12.8%
Best annual performance	6.4%	19.1%	18.5%
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%	16.7%	16.0%

The table above presents one year performance statistics. It highlights the performance differences between the 3 portfolios over the 3 years June 2013 to May 2016. This gives an indication of volatility of the performance of these 3 risk profiles.

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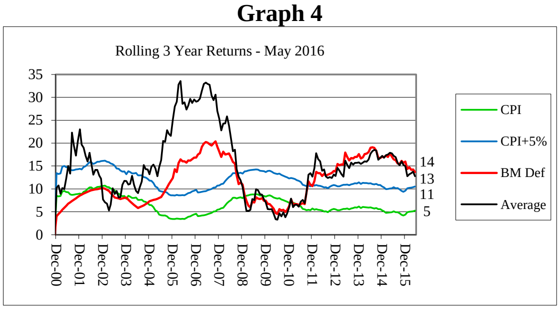
Graph 4



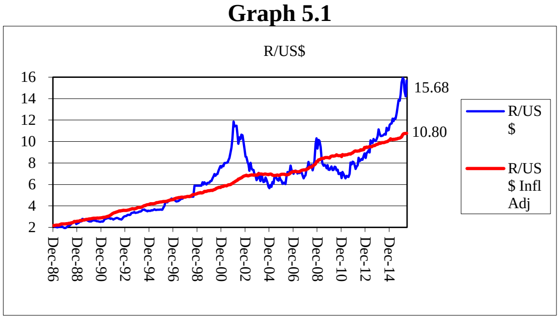
Graph 4 measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end May was 13.66%, the average was 12.78% vs CPI plus 5% currently on 10.49%.

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 undervalued at 10.80 to the US Dollar while it actually stood at 15.68 at the end of May. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

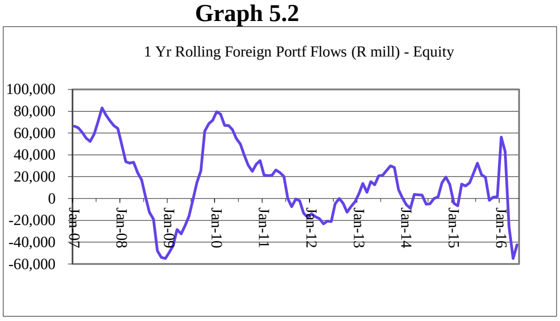
Graph 5.1



Rand strengthens despite foreign capital outflows

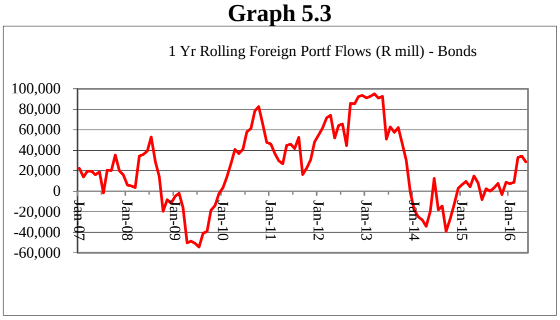
Graph 5.2 reflects a net outflow of capital from South African equities on a rolling one year basis, with a net outflow of 42.5 bn on a year-on-year basis at the end of May (outflow of R 55.0 bn year-on-year to end April). The month of May experienced a net inflow of R 16.7 bn. Since the beginning of 2006, foreign net investment in equities amounts to R159 bn (end April R 142 bn). This represents roughly 1.0% 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 R28.5 over the past 12 months to end of May (inflow of R 34.2 bn over the 12 months to end of April). Since the beginning of 2006, foreign net investment in bonds amounts to R 257 bn (to April just over R260 bn). The month of May experienced a net outflow of R 3.4.

Graph 5.3



The net outflows of foreign capital from equity and fixed interest securities was R14.0 bn for the rolling 12 months to end May 2016 (outflow of R 20.8 bn to end April 2016), compared to an inflow of R 22.4 bn for the 12 months to end May 2015 (inflow of R 26.5 bn to end of April 2015). Since the beginning of 2006, total net foreign portfolio inflows amounted to R 416 bn (April 403 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 29 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 6.5% including dividends.

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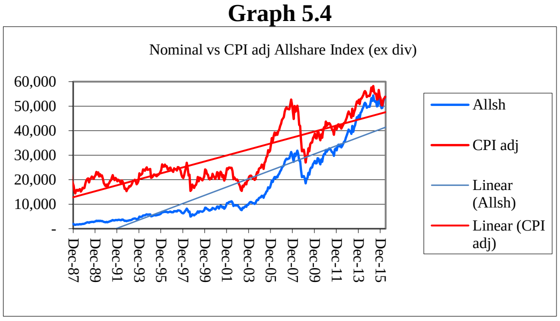
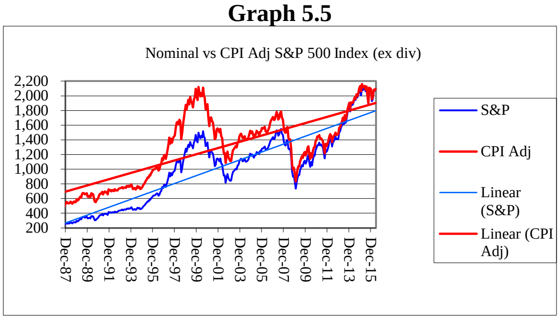
Graph 5.4



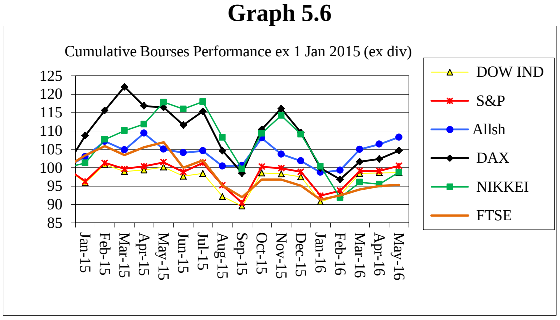
Graph 5.5 reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 7.2% per annum, over this period of just over 29 years. US inflation over this period was 2.7%. This is equivalent to a growth in real terms of 4.5% p.a. over this period, excluding dividends.

Graph 5.5



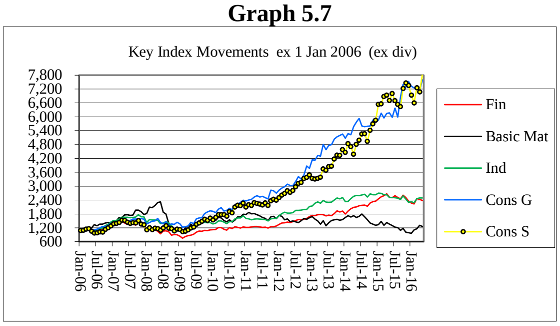
Graph 5.6 provides an interesting overview of some of the major global share indices, showing up the Allshare and the DAX as the top performing share indices.

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: 22.0%; Consumer Goods: 21.7%; Industrials: 9.2%; Financials: 8.8%; and Basic Materials: 2.3%.

Graph 5.7



6. Brexit – I can't hear it anymore

(by Tilman Friedrich)

So the unthinkable happened. The British electorate was wrongfully given the opportunity to express its opinion democratically. The remainder of the EU should never allow a referendum on EU membership anymore as the electorate is not objective in contemplating on such decision, said a renowned French political commentator on TV the evening of the British referendum. What a blatant contempt and disenfranchisement of the European electorate. Can one still be surprised about the electorate's skepticism towards this construct?

Former Prime Minister David Cameron, who probably tried to blackmail the EU into granting special concessions to Britain, eventually could not go back on his threat of a referendum which he probably was quite convinced, would go his way. He had no choice but to resign after this serious misjudgment of the attitude of his electorate towards the EU. As every coin has two sides the Brexit also has two sides and for anyone to pretend to understand exactly which side economically is the better one for Britain is preposterous. At the end of the day it was a decision between regaining and giving up political autonomy. The pride of the Brits evidently prevailed against the wishes of the whole political establishment of the EU the US and whoever else thought it opportune to try and influence the British voter from outside.

The EU is a political construct as was acknowledged by many renowned politicians before so its intention was never to deliver economic benefits and all the arguments based on economic considerations were misleading from the start. Britain now needs to be consequent and execute its regained political autonomy by capitalizing on the opportunities that are created by the EU's systemic weakness and flawed decisions such as for example filling the void the EU created on the Russian market. Britain should now be much more flexible, can act much more swiftly and offer more consistent policies in its interests than the EU will be able to. At the end of the day an economy must be supported by a strong political will, in which regard Britain will certainly be able to offer a lot more than a politically fragmented EU, and

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that is unlikely to change for many decades to come. Germany as the strongest economy in the EU does not have the political backbone to lead the EU while France as politically probably the strongest force does not have the economic backbone to lead the EU unlike Britain that could well have played that role.

So what is the implication for the pension fund member and investors? Well firstly, do not look at your investments for the next week or so. Markets are currently distorted in our opinion, by unfounded panic and fear. Any economic effects will really only be discernible over the next 2 to 5 years. Britain was one of the countries with an above average wealth in the EU. This implied that its wealth would have been further and further diluted towards the average within the EU umbrella. Britain will continue to use its Pound as it has hitherto – no change in this regard. Coming into Britain as a European may imply you will have to go through immigration control – but what really is the difference with Europe where the threat of terrorism has de facto re-introduced immigration controls? British tax laws and other trade related legislation will be as well aligned with those of the EU as they currently are and can be even better aligned if necessary, so the Brexit should present no impediment in this regard. Once the EU has managed to establish a single statutory, monetary and fiscal environment, there is nothing preventing Britain to adapt its own environment if this is in its interests. Britain should effectively be able to offer the best of both worlds now. A break-up of the EU would of course create a totally different scenario. It seems to be a great opportunity right now to capitalise on the week Pound and invest in Britain.

We do not believe that the Brexit will impact on the global economy once markets have digested the new reality. It may well cause shifts in the global economy, probably many in favour of Britain at least in the medium to long term. We would therefore now rather bet on Britain in terms of investment than on the EU and do this in the short to medium term when opportunities of under-valued assets will no doubt arise as the shifts will occur and until they have been digested by the British economy.

The global economy of course has not changed and remains in the doldrums. The US Fed will not raise interest rates further at this stage as its policy measures have failed to establish a sustained growth trend in the economy. This problem of cause was exacerbated by the steep drop in the oil price that has taken a lot of steam out of the fracking industry, and other related industries and has put a cap on job creation that was well on its way. For the same reasons we once believed that the steep incline in the world crude prize was irrational we believe that the steep decline is as irrational and probably politically motivated. The motivation seems to be in forcing countries that refused to subordinate themselves into submission, e.g. Russia, Iran, Venezuela etc. So far this strategy has borne some results but not without a significant measure of self-mutilation. It would seem that the best accelerator to global growth is an increase in the prize of crude to sustainable levels once again. This should certainly accelerate the velocity of money flows. However, it is likely the political objectives behind the sharp oil price deceleration have not been achieved and hence we and the global economy cannot yet look forward to the ‘throttle’ being opened again. Any indication of deflation is likely to also change views as governments will find it very hard to deal with a deflationary environment. This means the global economy will remain sluggish but who knows maybe an outsider for US president and a Britain outside the EU may bring about some global political changes?

Conclusion

In view of our expectation of a continued sluggishness of the global economy, yield will be hard to get by. The basic principles are to spread risk and to look for value in assets that generate high yields. Focus on achieving real returns of inflation plus 4% to 5%, i.e. be content with returns of between 10% and 12% for the next 12 months.

7. Important notice and disclaimer