Volume 13, No. 09
September 2017

# Benchmark Retirement Fund

## MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 SEPTEMBER 2017

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

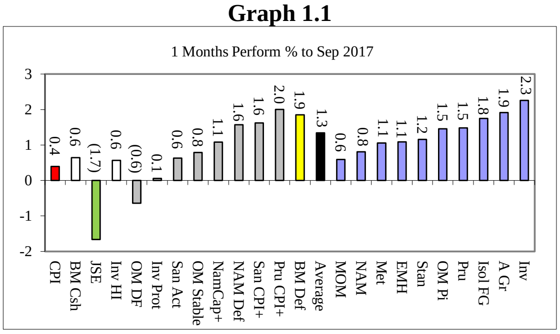
In September the average prudential balanced portfolio returned 1.35% (August: 0.85%). Top performer is Investec (2.26%); while Momentum (0.59%) takes the bottom spot. For the 3 month period, Investec takes top spot, outperforming the ‘average’ by roughly 1.30%. On the other end of the scale Momentum underperformed the ‘average’ by 1.69%.

**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 represents a combination of Prudential Namibia Inflation Plus and Allan Gray Namibia Balanced Fund.

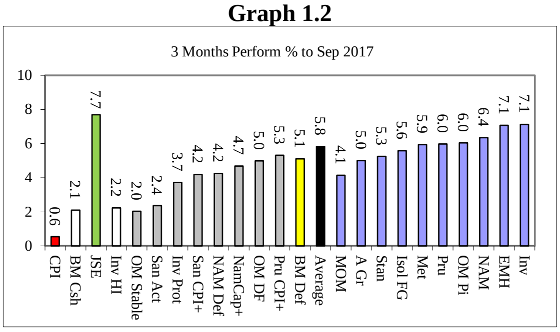
Below is the legend to the abbreviations reflected on the graphs:

| | |
|---|---|
| **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) |
| **Smooth bonus portfolios** | |
| Old Mutual AGP Stable | OM Stable (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) |
| Investment Solutions Bal Growth (multimanager) | Isol FG (blue) |

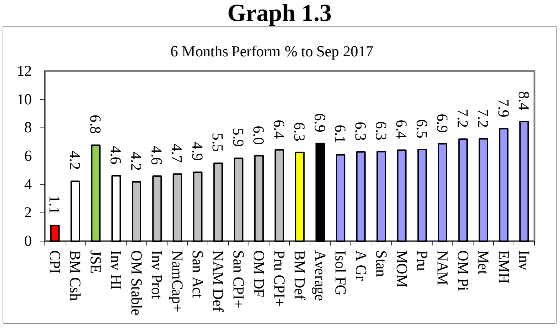
**Graph 1.1**



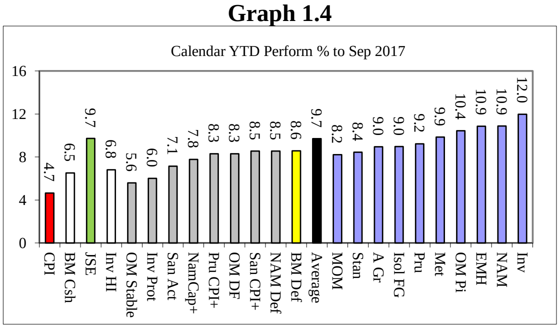

**Graph 1.2**



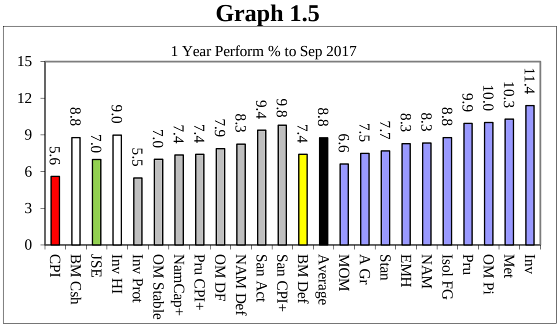

**Graph 1.3**




**Graph 1.4**




**Graph 1.5**



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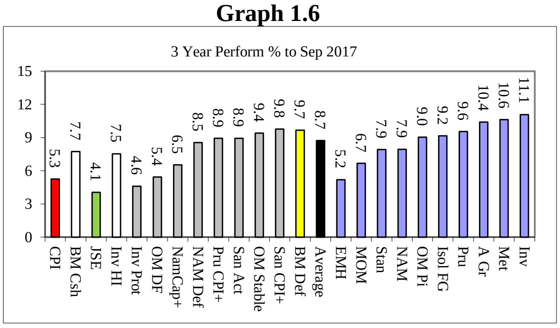
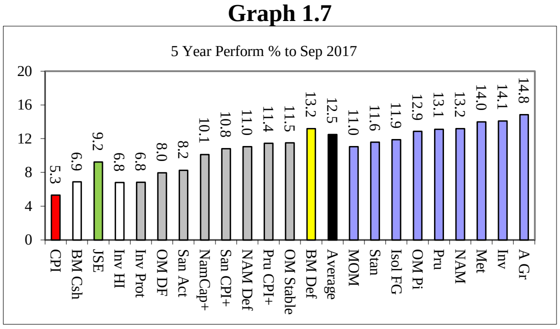
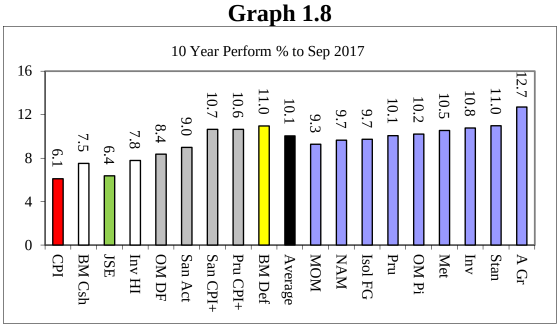
**Graph 1.6**



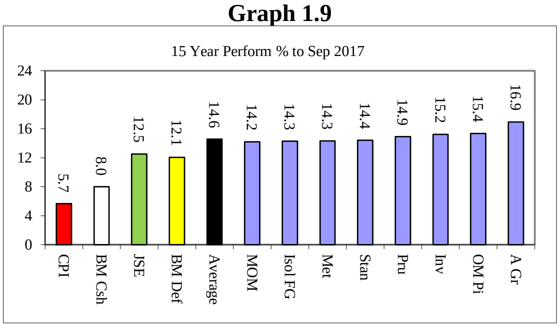

**Graph 1.7**



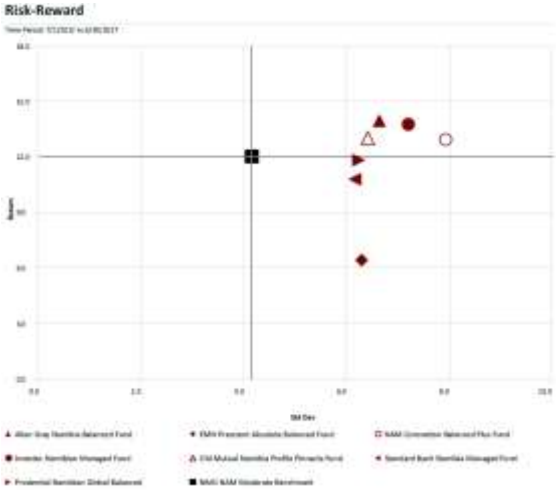

**Graph 1.8**




**Graph 1.9**

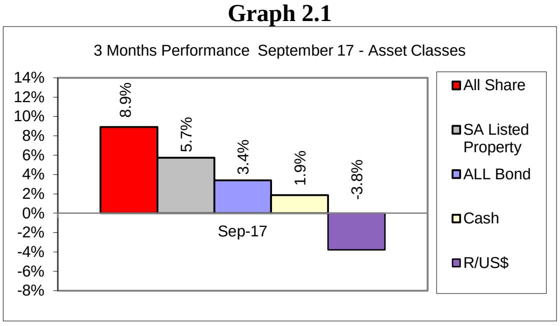



**Risk/ Return**

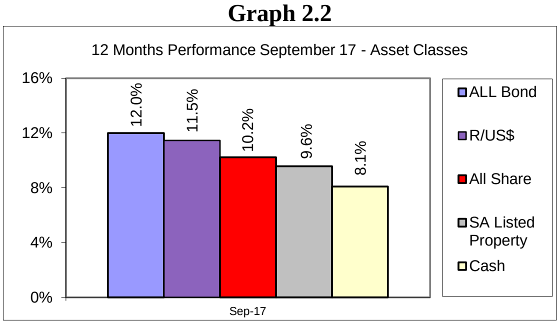



## 2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

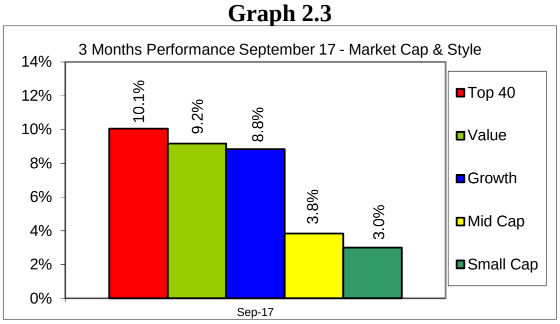
**Graph 2.1**




**Graph 2.2**




**Graph 2.3**



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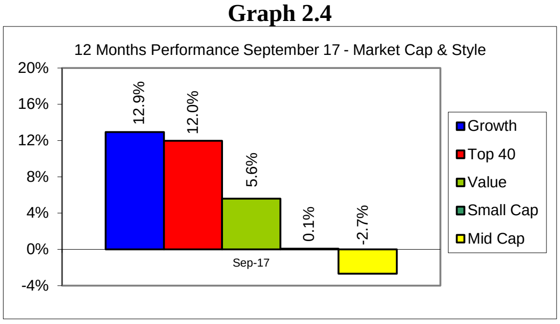
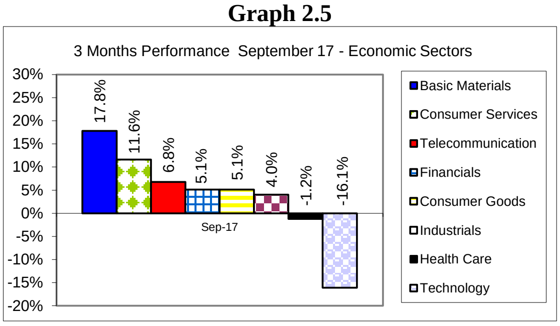
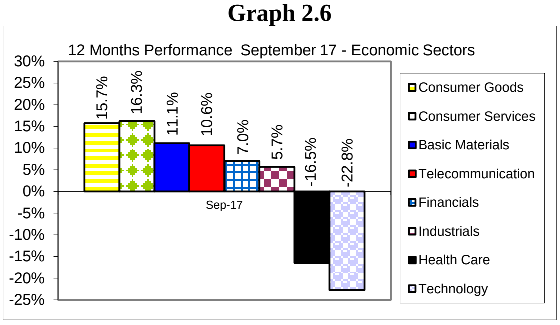
### Graph 2.4



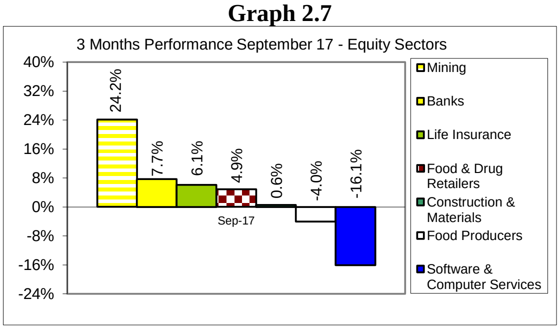

### Graph 2.5



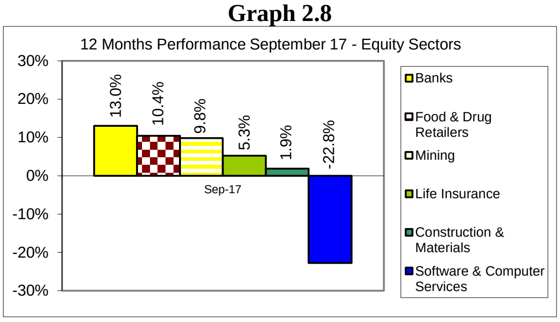

### Graph 2.6




### Graph 2.7



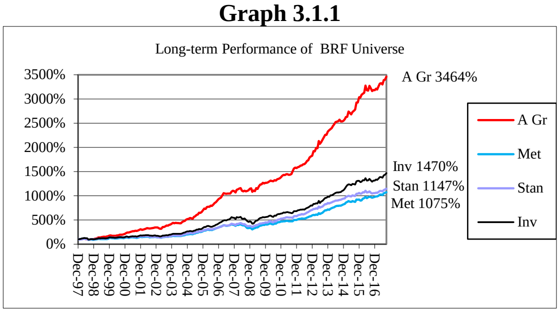

### Graph 2.8




## 3. Portfolio Performance Analysis

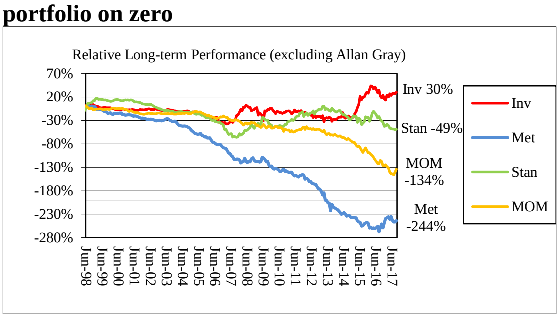
### 3.1 Cumulative performance of prudential balanced portfolios

### Graph 3.1.1

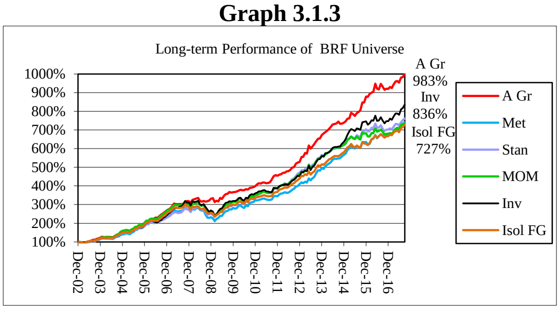



### Graph 3.1.2

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

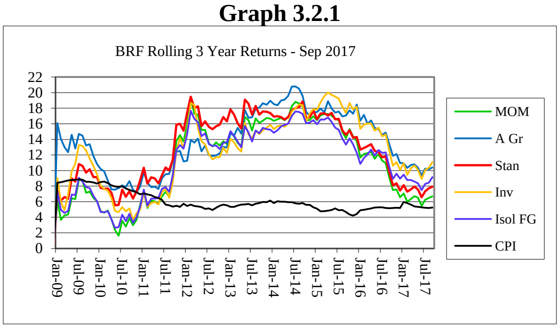



### Graph 3.1.3




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

### Graph 3.2.1



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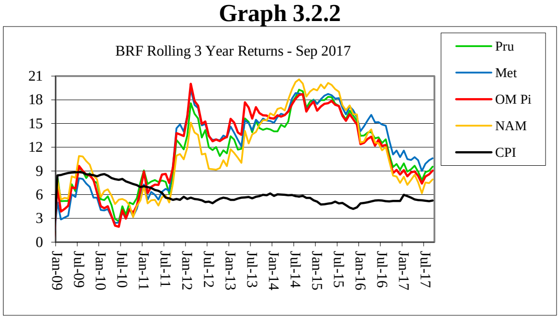
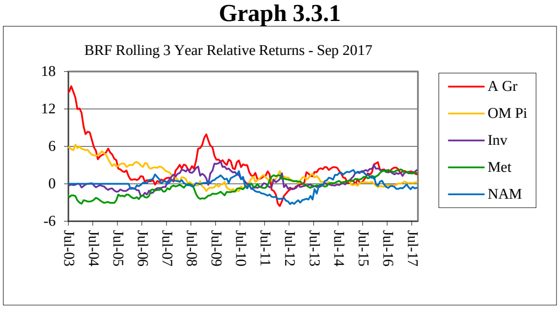
**Graph 3.2.2**

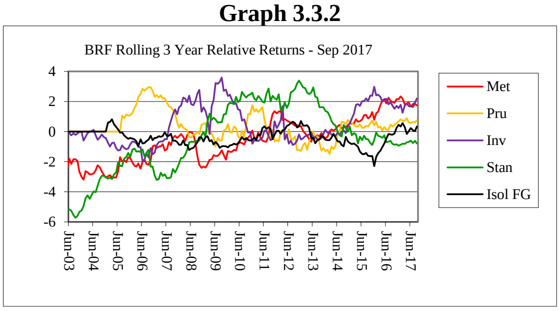



### 3.3 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

**Graph 3.3.1**

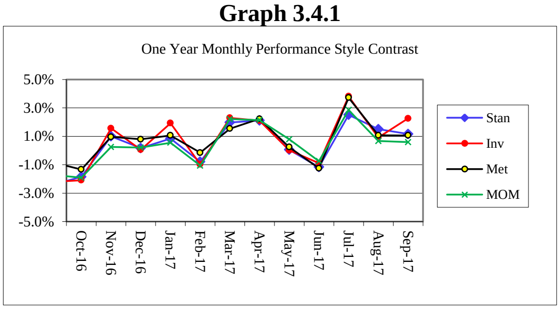



**Graph 3.3.2**

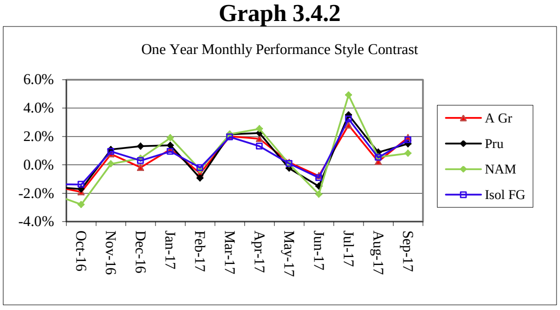



### 3.4 Monthly performance of prudential balanced portfolios

**Graph 3.4.1**

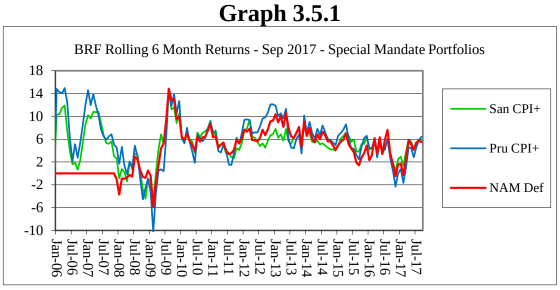



**Graph 3.4.2**

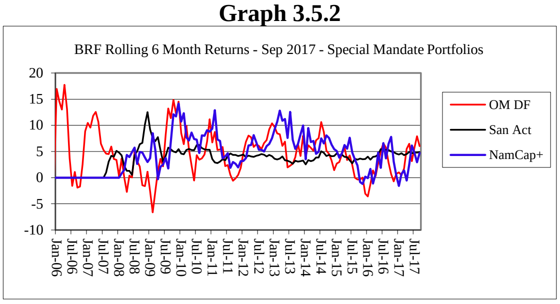



### 3.5. 6-month rolling and cumulative returns of 'special mandate' portfolios

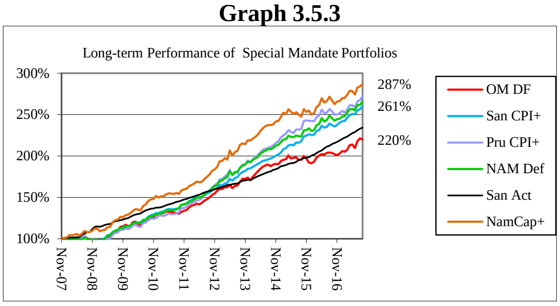
**Graph 3.5.1**




**Graph 3.5.2**




**Graph 3.5.3**



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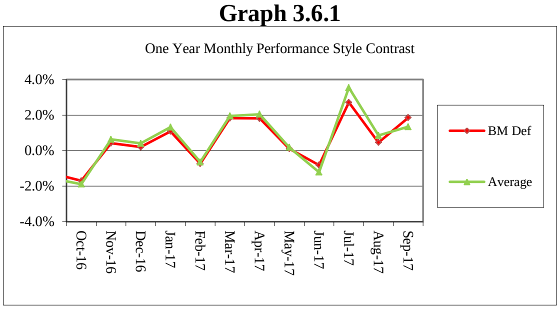
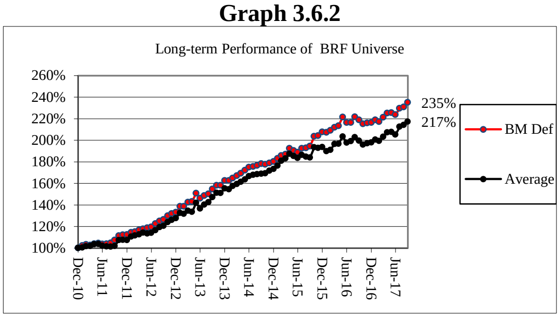
### 3.6 Monthly and cumulative performance of 'Benchmark Default' portfolio relative to average prudential balanced portfolio

**Graph 3.6.1**

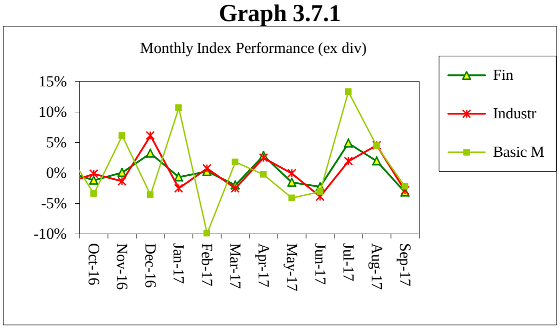



**Graph 3.6.2**

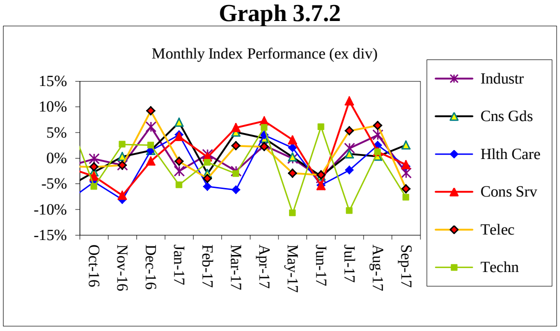



### 3.7 One year monthly performance of key indices (excluding dividends)

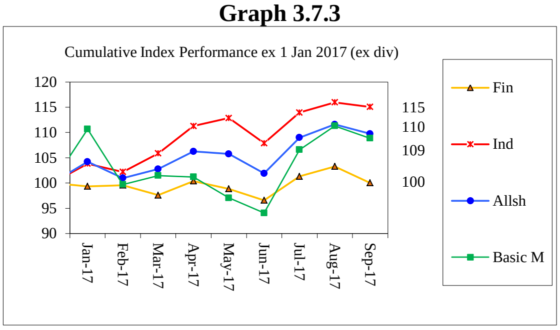
**Graph 3.7.1**



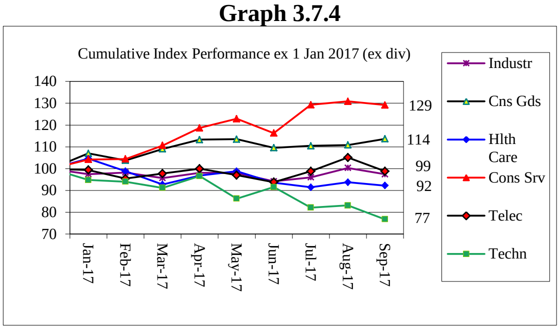

**Graph 3.7.2**




**Graph 3.7.3**




**Graph 3.7.4**




### 4. The Benchmark Default Portfolio – Facts in figures

**Table 4.1**

| Portfolio | Default portfolio | Average Prud Bal |
|---|---|---|
| 5 year nominal return - % p.a. | 13.2 | 12.5 |
| 5 year real return - % p.a. | 7.9 | 7.2 |
| Equity exposure - % of portfolio (qtr end Jun 2017) | 50.5 | 56.2 |
| Cumulative return ex Jan 2011 | 135. | 117.2 |
| 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 of the Default Portfolio 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 | 5.7% | 8.5% | 7.2% |
| Best annual performance | 7.7% | 17.8% | 18.0% |
| 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 | 7.3% | 9.8% | 8.5% |

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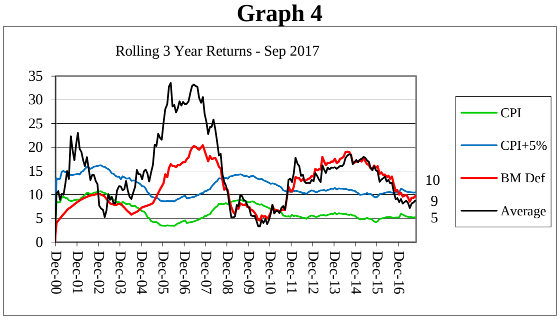
The table above presents one year performance statistics. It highlights the performance differences between the 3 portfolios over the 3 years October 2014 to September 2017. This gives an indication of volatility of the performance of these 3 risk profiles.

**Graph 4**



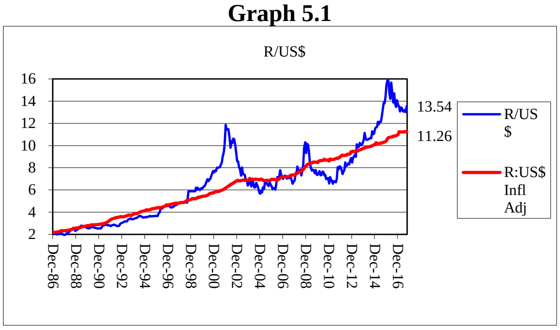

**Graph 4** measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3 year basis. It also shows rolling 3 year returns of the average prudential balanced portfolio and rolling 3 year CPI. The Benchmark default portfolio 3 year return to end September was 9.7%, the average was 8.7% 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 at fair value at 11.26 to the US Dollar while it actually stood at 13.54 at the end of September. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

**Graph 5.1**

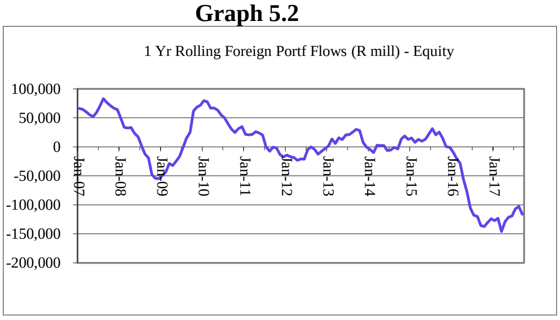



The Rand weakened by 4.07% in September with net foreign investment outflows from bonds and equities of R 10.567 bn. Over the past 12 months the Rand strengthened by 1.32%. Net outflows of foreign capital from equity and fixed interest securities amount to R 80.3 bn (outflow of R 80.4 bn to end August 2017).

Since the beginning of 2006, total net foreign portfolio inflows amounted to R 316bn (August R 327 bn).

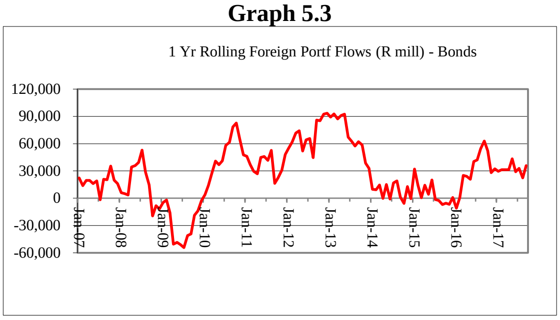
**Graph 5.2** reflects a net outflow of capital from South African equities on a rolling one year basis, with a net outflow of R 116 bn on a year-on-year basis at the end of September (outflow of R 103 bn year-on-year to end August). The month of September experienced a net outflow of R 26.1 bn. Since the beginning of 2006, foreign net disinvestment from equities amounts to R 33.4 bn (end August net investment of R 7.3 bn). This represents roughly 0.22% 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 35.9 bn over the past 12 months to end of September (inflow of R 22.3 bn over the 12 months to end of September). The month of September experienced a net inflow of R 15.5 bn. Since the beginning of 2006, foreign net investment in bonds amounts to R 349.3 bn (to August R 333.8 bn).

**Graph 5.3**




**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 11.42% per year since January 1987, and this excludes dividends of 3%. Namibian inflation over this period of 30 years was 8.23% per year. This is equivalent to a growth in real terms of 3.19% p.a. over this period, excluding dividends, or around 6.19% including dividends.

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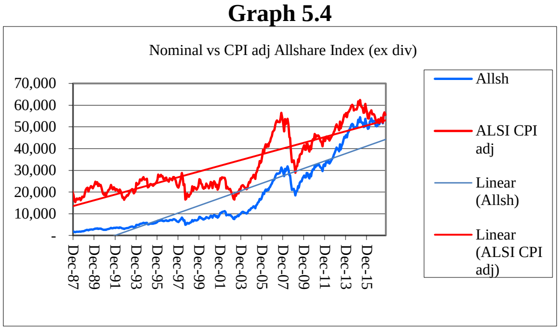
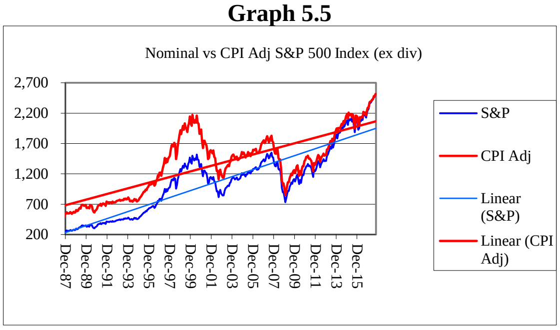


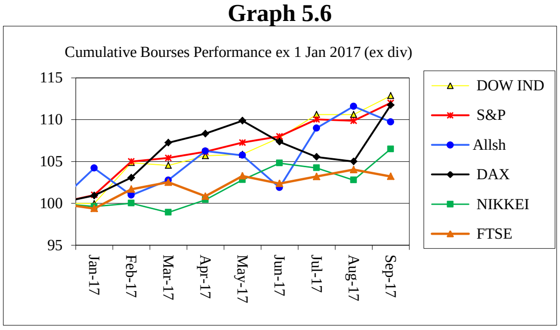

**Graph 5.5** reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 7.5% per annum, over this period of 30 years. US inflation over this period was 2.6%. This is equivalent to a growth in real terms of 4.9% p.a. over this period, excluding dividends.

**Graph 5.5**



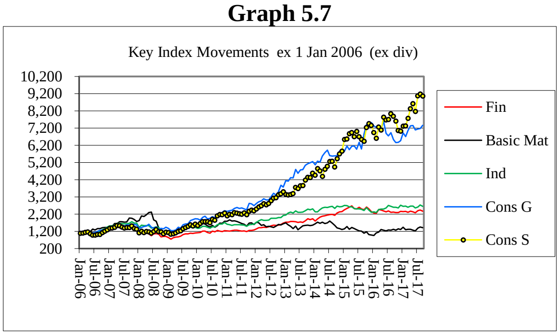

**Graph 5.6** provides an interesting overview of some of the major global share indices, showing up the Dow Jones, DAX, S&P 500 and FTSE as the top performing share indices since the start of 2016.

**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: 20.5%; Consumer Goods: 18.4%; Industrials: 8.6%; Financials: 7.6%; and Basic Materials: 3.0%.

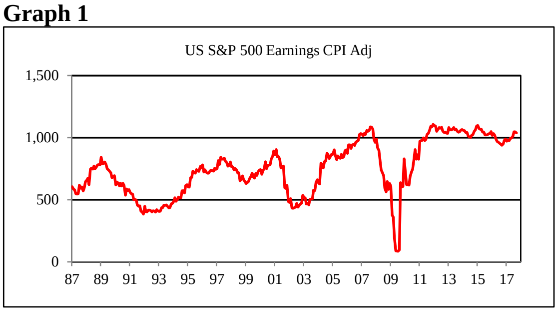
**Graph 5.7**




6. **Do markets have any room to rise further?**
by Tilman Friedrich

The price of equities is a function of earnings and the rating investors attach to the earnings stream, or in short the price: earnings ratio. So let us investigate earnings and the price: earnings ratio to get a better feel for future growth prospects of the equity markets. Since the US equity market has by far the largest market capitalization, let's look at the US equity market, more specifically the S&P 500 as its proxy and the SA equity market, as the one closest to home.

**Graph 1**




**Graph 1** above reveals a few facts about the US equity market. Firstly, earnings in real terms over the past 30 years have generally been moving between 500 and 1,000, on average they were around 750. Secondly the graph shows that real earnings moved sideways with some volatility until 2004 to then rise steeply from 500 at the start of that period to just over 1,000 by 2008. Thirdly it shows that earnings have reached a peak of just over 1,000 and have been moving sideways with a slight declining trend since the beginning of 2008 and a brief slump following the global financial crisis. Real earnings on 1,000, are thus currently around 25% above their 30 year average. This indicates that the US equity market is more likely to decline to its average earnings than growing further.

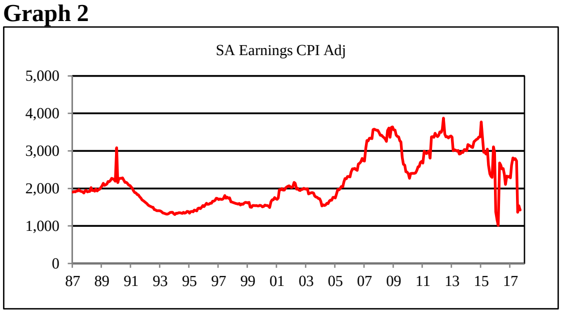
# Benchmark Retirement Fund

## MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 SEPTEMBER 2017

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

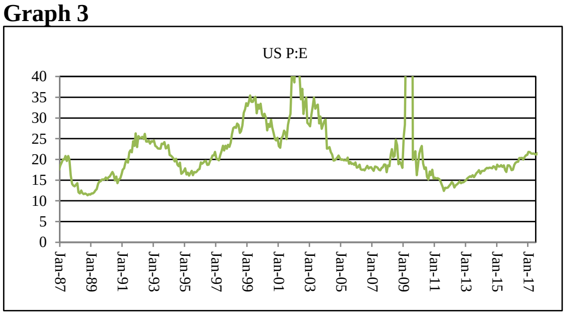
The monthly review of portfolio performance, as set out in this issue, is also available on our website at www.rfsol.com.na.

**Graph 2**



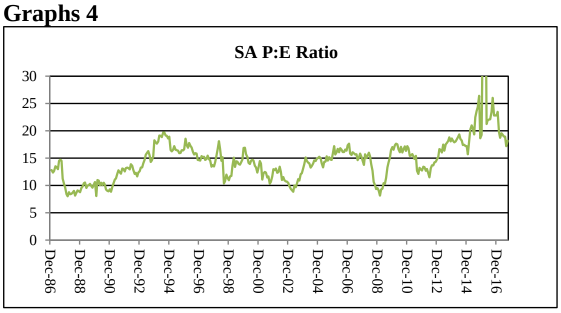

**Graph 2** reflects a very similar picture for the SA Allshare Index. SA real earnings have been moving sideways from 1987 up until 2004 when it started to move up steeply as the result of the commodity boom up to 2008 when they reached the level of around 3,500. Since 2008 earnings became quite volatile, dipping to around 2,200 in the aftermath of the global financial crisis but by-and-large remaining at a level well above 3,000 until 2015. Since 2015 earnings steeply declined to their current level of around 1,400 in sympathy with the fall-out in world commodity prices.

**Graph 3**



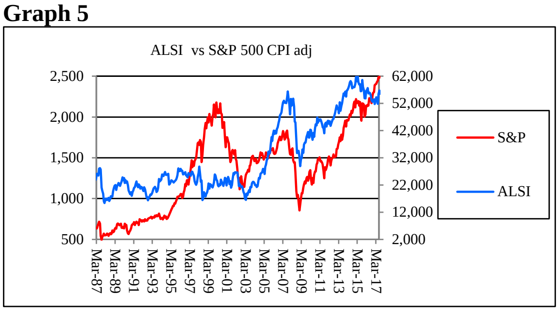

Now let's consider the US P:E ratio depicted in **graph 3** above. Over this 30 year period the average is around 22 and this is its current level but it has gradually increased from around 13 in 2012.

**Graphs 4**




The SA P:E ratio as per **graph 4** above is around 15 on average over this 30 year period while its current level is 18, having declined from a peak of just above 25 in 2015.

**Graph 5**




If we now look at the CPI adjusted S&P 500 versus the SA Allshare Index in **graph 5** above we see that these indices are fairly well correlated barring the period from 1995 to 2003 when the US market reflects both a steep increase followed by a steep decline. We see that both markets increased steeply post global financial crisis in 2008. In the US the initial increase was driven by a steep increase in earnings until 2012 and was thereafter supported by an increase in the P:E ratio from below average to average again. In SA the market increase from 2009 to 2015 was driven by a less marked increase in earnings and a steep increase in the P:E from around 15 to around 25 by 2015. Unlike the US, SA earnings declined sharply from 2015 while the P:E ratio also dropped from 25 to 18 currently.

The conclusion one can reach from the above graphs is that the US market has reached a 30 year peak as far as real earnings are concerned but is on a normal P:E ratio. Will US investors be prepared to pay more for the earnings stream of US companies, thus lifting the P:E ratio and the index without an increase in earnings to lift the S&P 500 further or to counter act any decline in earnings? We believe that this may well be the case in the face of increasing interest rates and the absence of alternatives. Overall though with the prospect of declining earnings, an increase in the P:E ratio is unlikely to impact much on the price level and we would thus rather see a sideways movement until interest rates have reached a normal level. We will thus see no impetus for global bourses coming from US euphoria.

In SA current real earnings represent a 30 year low while the P:E ratio is still about 20% above its 30 year average. Will investors be prepared to once again pay more for the earnings stream of SA companies? This would depend on foreign demand for SA equities which is currently non-existent. The probability is thus that earnings should start picking up while the P:E ratio is likely to decline. Here too we are thus unlikely to see any growth in SA equity price levels until earnings have picked up by around 25% to around 1,750.

### Conclusion

Interest rates are on the rise in the US and any country that does not want to fall behind the US to see

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investment capital leaving and their currency weakening, will be forced to raise interest rates. The same applies to SA and Namibia of course. A weak currency is good for our competitiveness on global level and should assist job creation and economic growth. Consumer sentiment and demand should improve as our exports increase as the result of a weak currency. This in turn should afford the SA Reserve Bank the opportunity to lift interest rates gradually.

Since our currencies have already weakened significantly more recently and are undervalued by our measures as depicted by graph 5.1in paragraph 5, it is probably not a good time to move money offshore at this juncture while anyone who needs to repatriate offshore capital should probably do it now.

However, offshore diversification still remains a must for reducing your chances of losing and improving your chances of better returns and should be considered once our currencies have strengthened. Pension fund investments are contractual obligations and you cannot change certain parameters, such as prescribed investment limits. You are also likely to be overweight Namibia with your total assets so you should use your liquid discretionary capital to diversify your risk away from Namibia. As far as local investments are concerned, in the short-term there is little to choose between the more and the less volatile asset classes in our opinion. We retain our preference for equities over cash and would be wary of bonds in the medium term although there may still be opportunity in the shorter term while SARB may still reduce interest rates against the global trend.

### 7. Important notice and disclaimer