Volume 6, No. 6, June 2010

Benchmark Retirement Fund

MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 30 JUNE 2010

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.

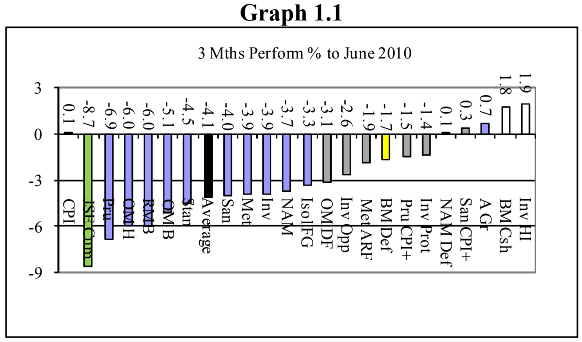
1. Review of Portfolio Performance

In **June** the **average prudential balanced portfolio** returned minus 1.67% (May minus 3.1%). Best and worst performance **for the month** was delivered by Allan Gray (minus 0.06%) and RMB (minus 2.82%), respectively.

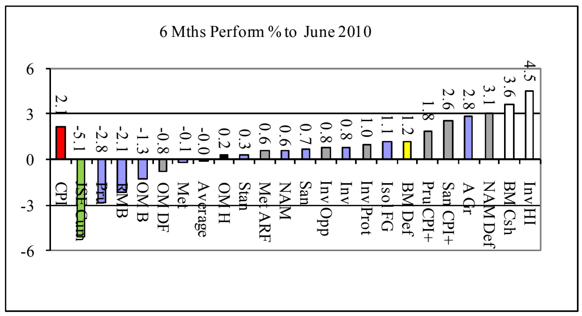
Graphs 1.1 to 1.7 reflect the performance for periods from 3 months to 10 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no colour bars), the average of prudential balanced 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 Metropolitan Namibia Absolute Return. Below is the legend to the abbreviations reflected on the graphs:

Benchmarks	
Namibian Consumer Price Index	CPI Cum (red)
JSE Allshare Index	JSE Cum (green)
Benchmark Default Portfolio	BM Def (yellow)
Average Portfolio (prudential, balanced)	Aver (black)
Special Mandate Portfolios	
Money market	BM Csh (no colour)
Investec High Income (interest bearing assets)	Inv HI (no colour)
Investec Protector	Inv Prot (grey)
Investec Opportunity Fund	Inv Opp (grey)
Metropolitan Absolute Return	Met ARF (grey)
Prudential Inflation Plus	Pru CPI+ (grey)
Old Mutual Dynamic Floor	OM DF (grey)
Sanlam Inflation Plus	San CPI+ (grey)
NAM Coronation Balanced Def	NAM Def (grey)
Market related portfolios	
Allan Gray Balanced	A Gr (blue)
Investec Managed	Inv (blue)
Investment Solutions Bal Growth, prev. Focused Growth (multimanager)	Isol FG (blue)
Prudential Managed	Prud (blue)
Metropolitan Managed	Met (blue)
NAM Prudential Balanced	NAM (blue)
Old Mutual Profile Balanced	OM B (blue)
Old Mutual Profile Growth	OM H (blue)
RMB Managed	RMB (blue)
Sanlam Managed	San (blue)
Stanlib Managed	Stan (blue)

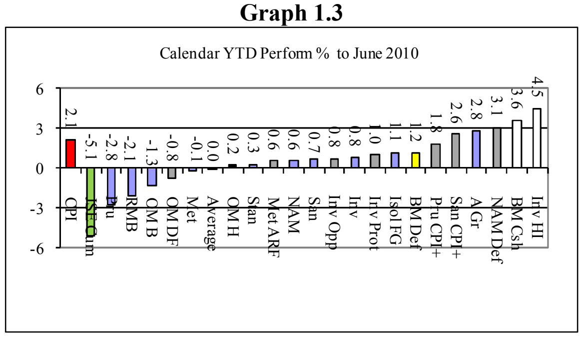
Graph 1.1



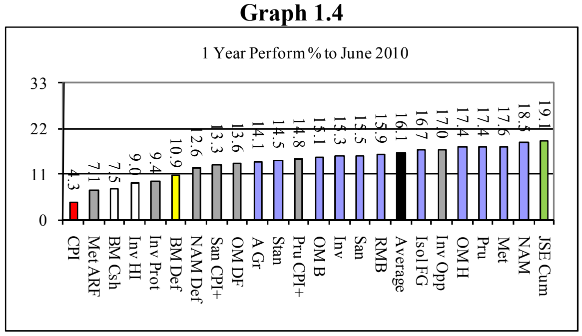
Graph 1.2



Graph 1.3



Graph 1.4



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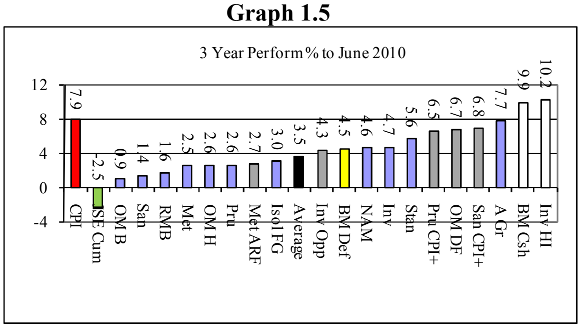
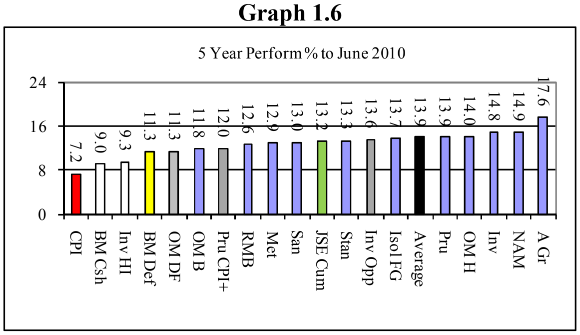
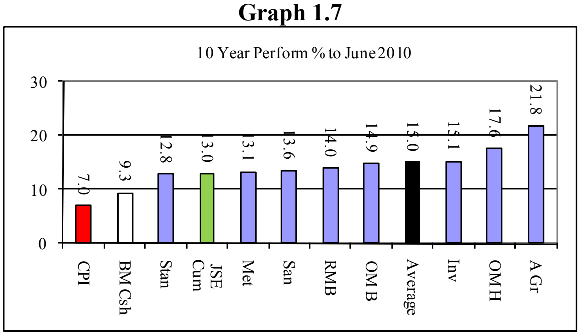
Graph 1.5



Graph 1.6



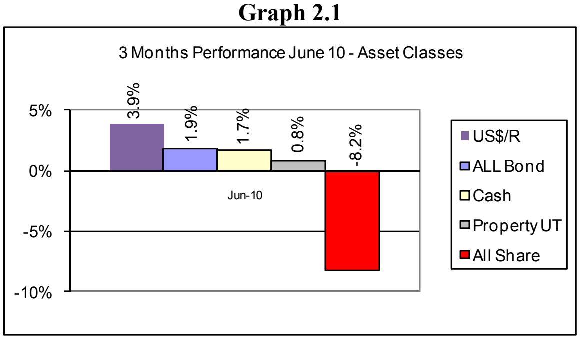
Graph 1.7



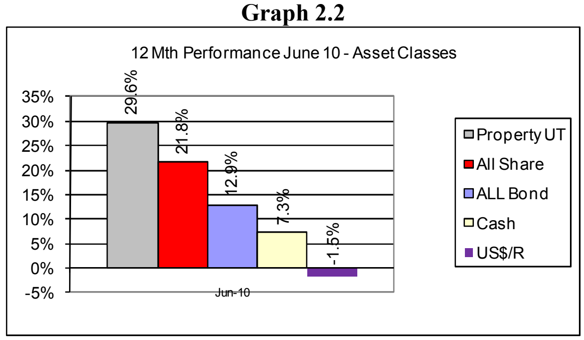
2. Performance of Key Indices

Performance of Key Indices (index performance by courtesy from pointBreak/Deutsche Securities)

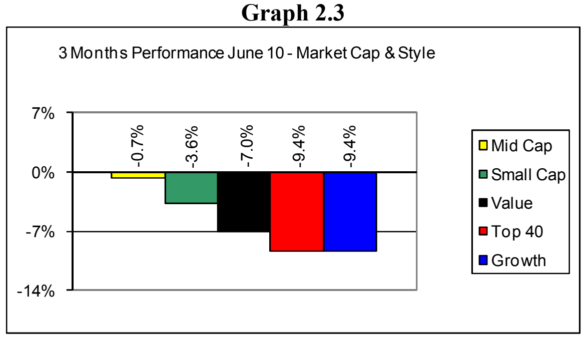
Graph 2.1



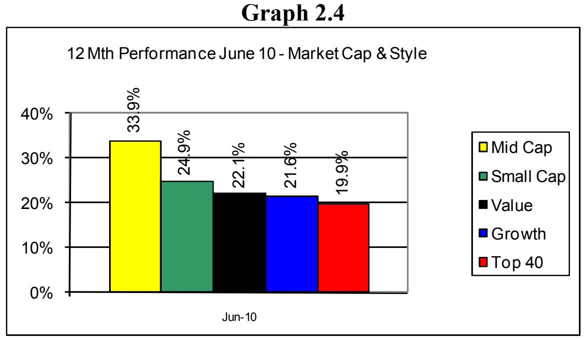
Graph 2.2



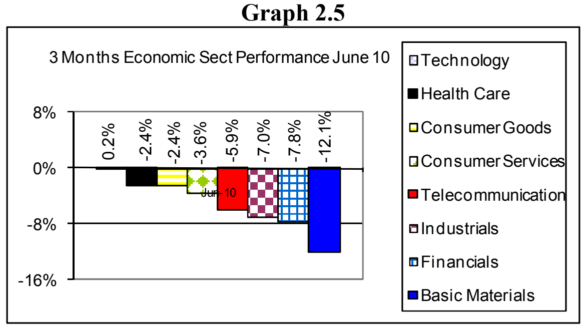
Graph 2.3



Graph 2.4



Graph 2.5



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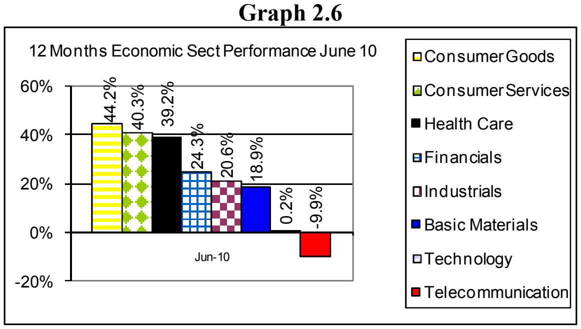
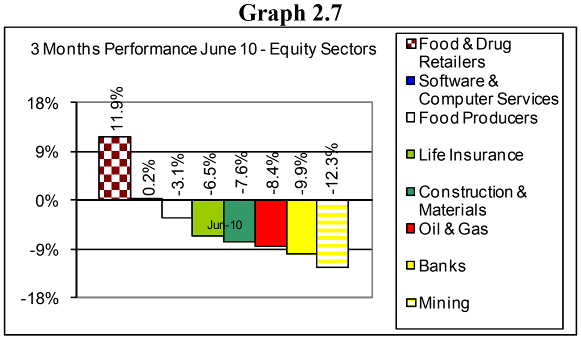
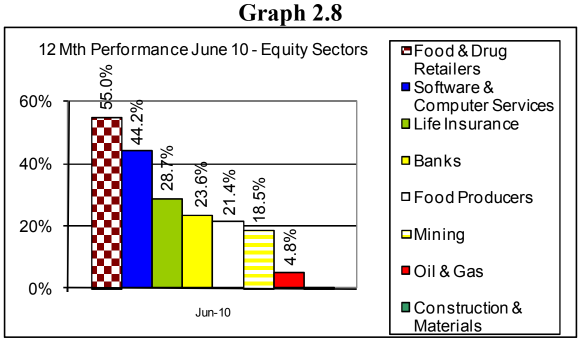
Graph 2.6



Graph 2.7



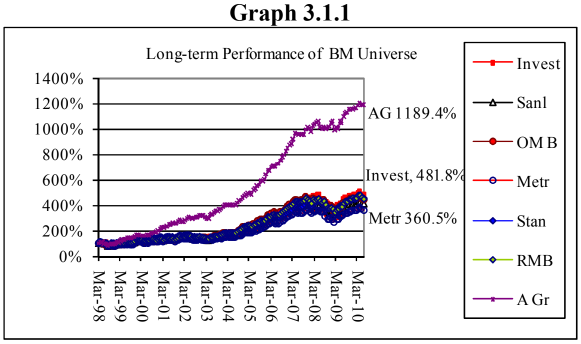
Graph 2.8



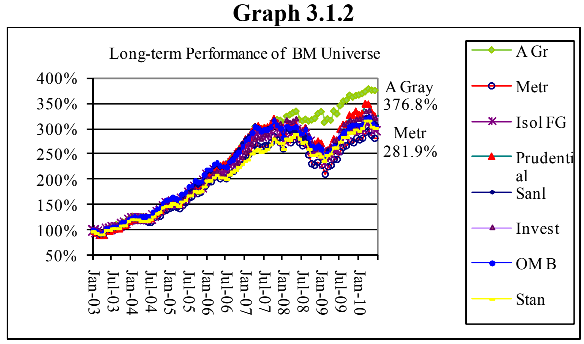
3. Portfolio Performance Analysis

3.1. Cumulative performance of prudential balanced portfolios

Graph 3.1.1

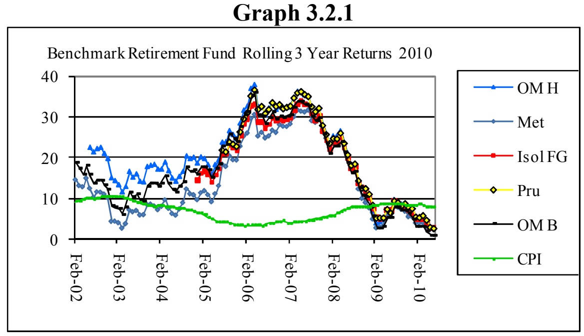


Graph 3.1.2

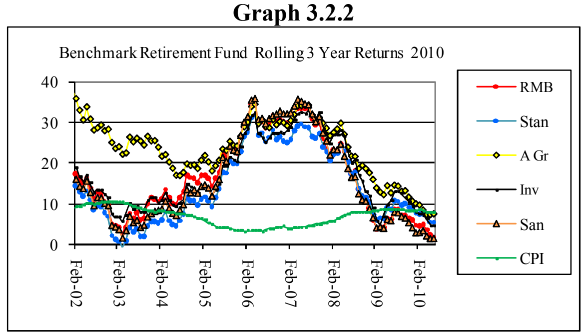


3.2. 3-year rolling performance of prudential balanced portfolios relative to CPI

Graph 3.2.1



Graph 3.2.2



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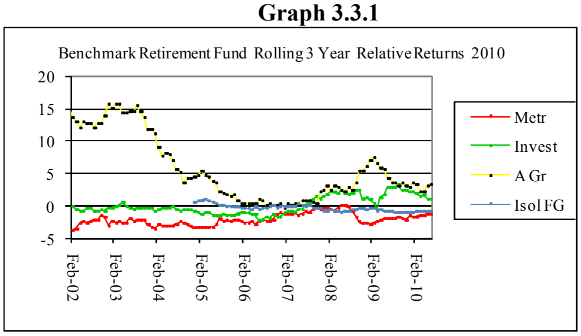
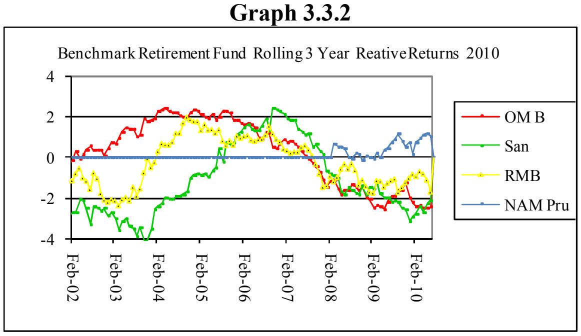
3.3. 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

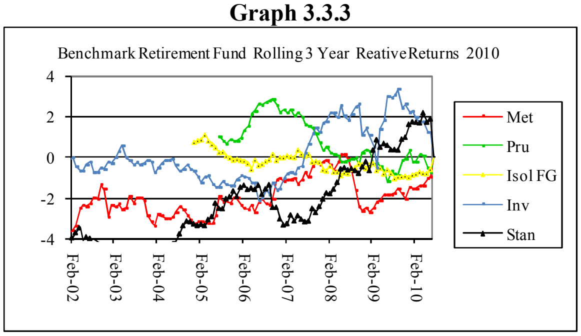
Graph 3.3.1



Graph 3.3.2

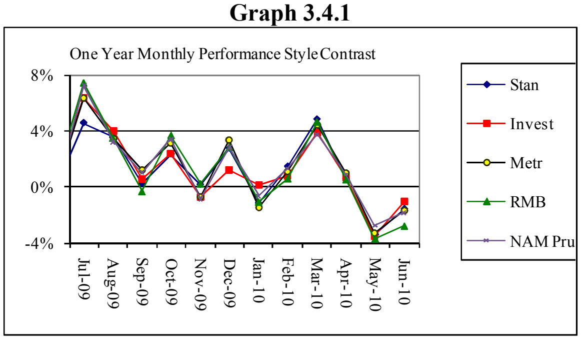


Graph 3.3.3

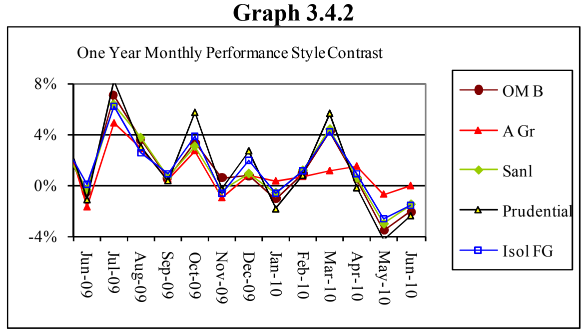


3.4. Monthly performance of prudential balanced portfolios

Graph 3.4.1

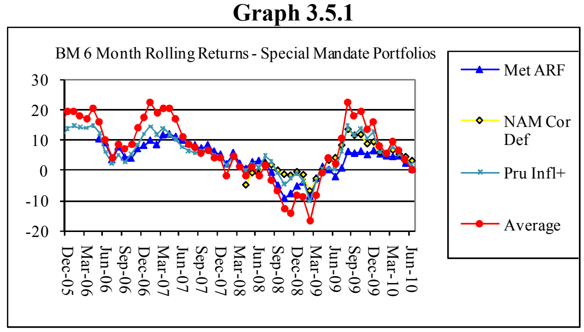


Graph 3.4.2

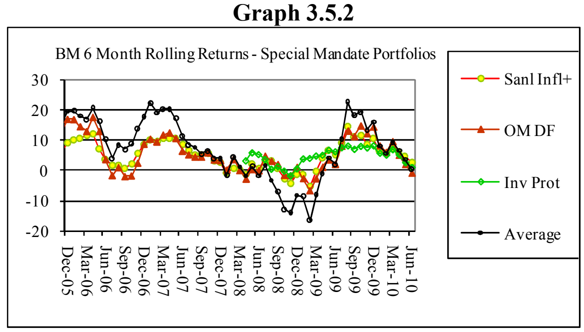


3.5. 6-month rolling returns of 'special mandate' portfolios

Graph 3.5.1

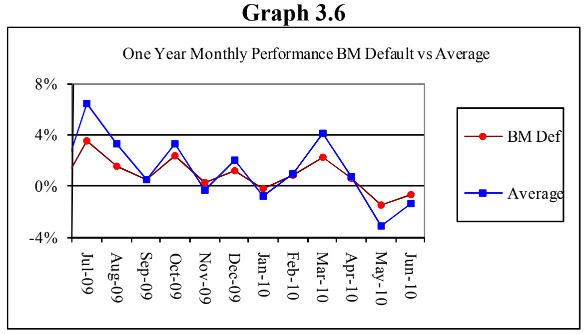


Graph 3.5.2



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

Graph 3.6



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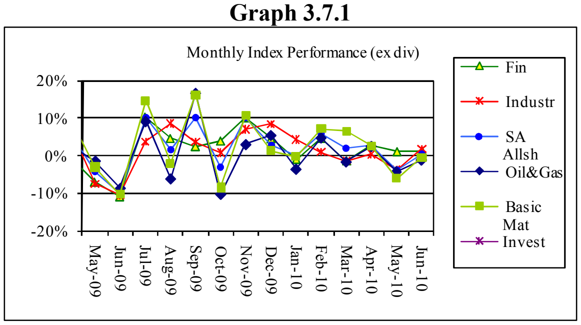
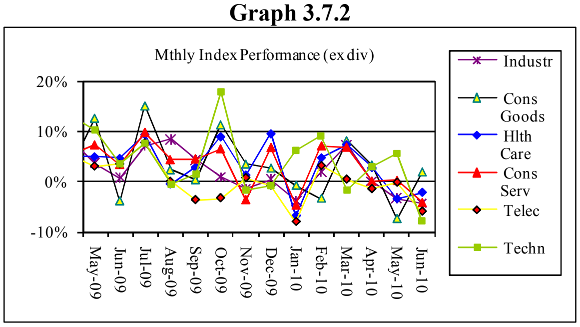
3.7 Monthly and one year cumulative performance of key indices (excluding dividends)

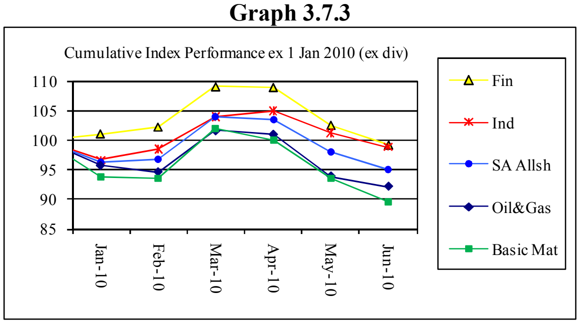
Graph 3.7.1



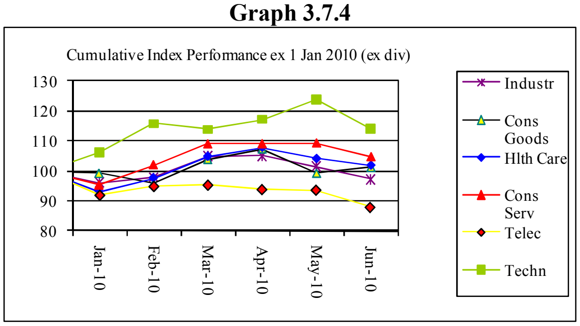
Graph 3.7.2



Graph 3.7.3



Graph 3.7.4



4. The Benchmark Default Portfolio

Graph 1.6 shows that the average prudential balanced portfolio returned 13.9% p.a. in nominal terms, or 6.7% p.a. in real terms, over the past 5 years while the Benchmark Default portfolio returned 11.3% p.a. in nominal terms, or 4.1% p.a. in real terms. The past 5 years reflect returns very close to expected long-term returns. The long-term performance differential of 3% p.a., between the Default portfolio and the average prudential balanced portfolio, is probably representative of a realistic long-term expectation. We would expect the average prudential balanced portfolio to deliver a real return of roughly 6% per year and the Default portfolio to sacrifice around 2% to 3% for the benefit of lower volatility, thus an expected real return of around 4% per year.

The Money Market portfolio returned 7.5% and the Default portfolio returned 10.9%, gross for the one year to end June. The more 'risky' average prudential balanced portfolio returned 16.1% gross over this period. A fee of roughly 0.75% p.a. still has to be deducted from all but the Money Market Portfolio. The performance of the prudential balanced portfolios is significantly more volatile than that of the Default portfolio, which produces significantly more volatile performance than the Money Market portfolio. The table below presents one year statistics over the 3 years July 2007 to June 2010:

Table 4.1

Measure	Money Market	Default Portf	Average Prud Bal
Worst annual performance	7.5%	- 8.0%	- 19.1%
Best annual performance	12.1%	20.8%	32.6%
No of negative 1 year periods	n/a	10	11
Average of negative 1 year periods	n/a	- 3.7%	- 10.3%
Average of positive 1 year periods	10.1%	11.2%	16.0%

This table represents the different characteristics of the three types of portfolio quite well. The Default portfolio is a more conservative investment aimed at minimising negative returns and with a long-term return objective of inflation plus 4%.

It is very important, though, 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!

5. A Contrarian Preview Of The Next 12 Months

Global equity markets have experienced a dramatic recovery to the end of the first quarter but moved into a more volatile territory of late with three poor months April, May and June in a row.

Looking at the global economic environment from the consumer's point of view, it is hard to see any reason for it to move back to the levels last seen before the financial crisis. A recovery from the overly negative sentiment

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however, was to be expected, is in place and is given much prominence in the media. Despite low global interest rates, unemployment and debt remains at high levels restraining consumer sentiment and consumption.

The US recently released its latest budget estimates that project a budget deficit of 10% of GDP, way above a globally accepted norm of 3%, while its sovereign debt is somewhere around 60% of GDP. In Europe this picture is not any better, in many cases substantially worse. The fiscal and monetary situation in Japan is beyond any normal person's imagination while China, although in sound economic state, is really significantly dependent on producing for the US and European consumer.

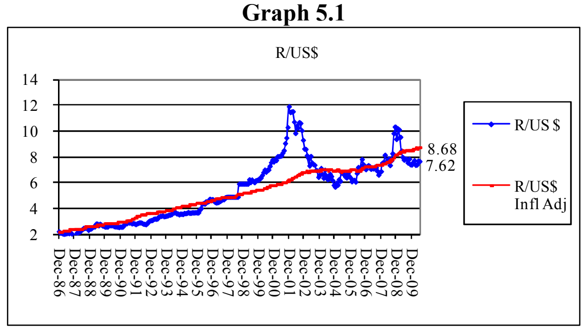
Our expectation is that there will not be a meaningful turnaround in global consumer spending for another year or more. Under these circumstances, government revenues from taxes will not show any meaningful growth. It is difficult to envisage how countries will reduce their debt levels without raising taxes, thereby retarding economic growth and/or creating inflation. How will governments fund their budget deficits and service their debts? John Mauldin talks about another 'debt super cycle'. It gets way too complex for the man in the street, but thinking about his rationally, it probably means that as long as no-one withdraws his investment and there are no huge global flows of capital, one will be able to muddle through until consumer sentiment improves, the consumer starts spending again and inflation can set in to establish fiscal and monetary equilibrium.

We believe that it will take globally coordinated policy measures to maintain stability in the markets and to correct the existing economic imbalances. Whilst such coordinated measures are indeed in progress, there will still be many surprises that will pose challenges to an orderly unwinding process and that will be the cause of continuing volatility in global financial markets. This will not be a good time to be invested in volatile assets and focus should be on high yielding assets.

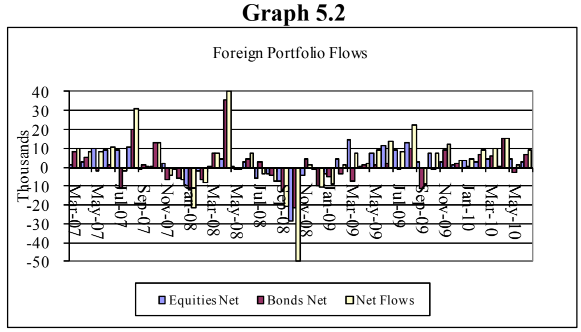
Graph 5.1 indicates that the Rand is fairly valued at 8.68 to the US Dollar. This is based on adjusting the two currencies by the respective inflation rates. By this measure the Rand is significantly overvalued and it is hurting local manufacturing, exports and employment. Global investors in search of yield conceivably will be looking around the globe to acquire companies in growing economies such as the so called BRIC countries but also South Africa. There is currently talk about two foreign banks negotiating with Old Mutual on the acquisition of Nedbank, as one example. This transaction in itself should strengthen the Rand, if it should materialize and others are likely to occur as well.

Graph 5.2 indicates that foreign equity purchases in SA remain subdued and we expect this to persist for an extended period of time thus inhibiting the growth of our local equity markets. For the year to end of June, the FTSE/JSE still experienced a massive net inflow of R 55 billion (R 66 billion, 12 months to end May), compared to a net outflow of R 16 billion for the year to end June 2009 (net outflow of R 25 billion, year to end May 2009).

Graph 5.1



Graph 5.2



Graph 5.3 shows to what extent equity markets have recovered in nominal terms since their low at the end of February 2009. The down turn to end June 2010 has in the mean time reversed in July to date.

Graph 5.4 reflects the same statistics but adjusted for US and SA inflation respectively. Inflation adjusted, the Allshare has grown by 4.6% per annum over more than 12 years, since December 1997.
Over the past 12 months, the 1 year trailing SA Allshare P:E nearly doubled, gaining 7.9 points to 16.1 from its bottom of 8.2 at the end of February 2009. The S&P 500 P:E in comparison is on 17.7.

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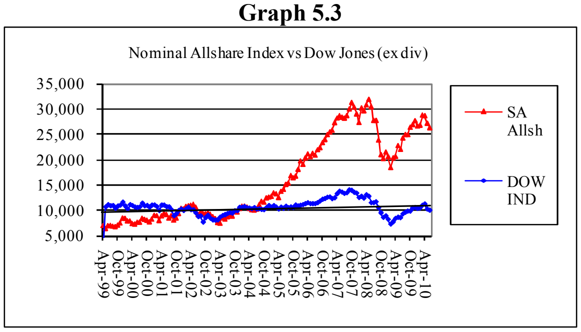
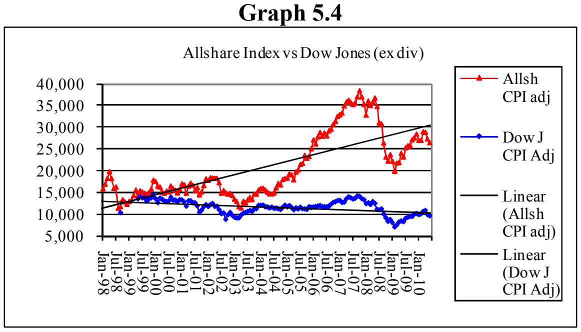
Graph 5.3

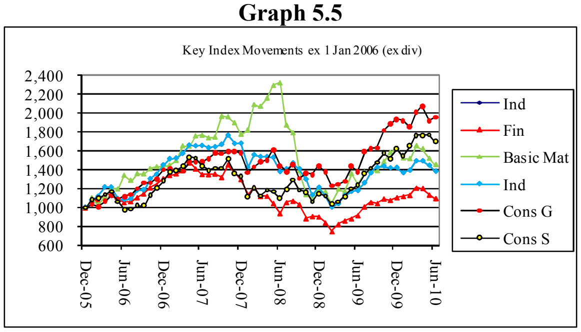


Graph 5.4



Graph 5.5 provides an interesting overview of relative movement of the key equity sectors on the FTSE/JSE since December 2005 when these indices were first introduced. From this the investor should be able to deduce which sectors offer greater value and which one's offer less value on the basis of fundamentals.

Graph 5.5



6. Conclusion

In our view, global equity markets are probably fairly valued, but are likely to produce pedestrian growth for the next 12 months and longer, with considerable volatility. While some global interest rates have already been raised they will remain at low levels for a while, to start picking up once consumer demand picks up meaningfully. This we do not expect to happen within the next 12 to 24 months. We now expect the Rand to remain pretty strong for a while and weakness to only surface once global economies to start picking up steam.

In terms of local equity sectors, **graph 5.5** indicates that consumer goods and consumer services had a good run. We do not expect too much joy out of these sectors anymore and these should hence be underweight. On the basis of fundamentals, one should be overweight financials and industrials locally, while commodities should be neutral to underweight. We believe that the performance of most conventional asset classes will be muted. We expect equities in general to perform sluggishly but stock picking can add value. Property is a high yielding asset class and should deliver superior returns in the current environment.

A lack of sparkling local investment opportunities and the current Rand strength suggests that one should be overweight offshore assets, more specifically in growing economies such as the BRIC countries.

For pension funds, a conservative balanced portfolio with a fair spread across equities, bonds and property and a high foreign exposure is our call for now.

7. Important notice and disclaimer

Whilst we have taken all reasonable measures to ensure that the results reflected herein are correct, Benchmark Retirement Fund and Retirement Fund Solutions Namibia (Pty) Ltd do not accept any liability for the accuracy of the information and no decision should be taken on the basis of the information contained herein before having confirmed the detail with the relevant portfolio manager. The views expressed herein are those of the author and not necessarily those of Benchmark Retirement Fund or Retirement Fund Solutions.