

# MARKET INSIGHT

## Targeted Market Commentary from Simeka Consultants & Actuaries

Second Quarter 2011

The low returns reported in this quarter are not unexpected, given the expectations already reflected in asset prices and their growth since 2008. As positive indications such as local economic growth (GDP) at 3,7% are reported, further negative reports are received. These negative reports include higher creeping local inflation (of 5%), higher wage increases and countries such as Greece and Italy struggling to meet their commitments. The reality is that balance sheets which were hurt with the crisis of 2008 cannot be rebuilt overnight. Rebuilding requires a sustained period of budgetary constraint (austerity) and careful resource management.

This quarter also marked the end of the USA's quantitative easing programme in which a further US\$600bn of liquidity was provided to the markets. Although some sense of stability has been achieved in markets, politicians will now have to deal with the fact that they will not have the resources to apply to their promised projects – some of those promises being long-term commitments to pensions and health services which make the task so much more difficult.

At face value, it seems as if corporates have reacted well, maintaining or improving profitability and restructuring their balance sheets. With significant cash on balance sheets, the prospects of more investment, merger and acquisition activity has improved.

The movements in exchange rates, despite some volatility, have been marginal over the last quarter.

### Market Commentary

The FTSE/JSE All Share index was marginally down over the quarter, but still 4,8% higher than three years ago on 1 July 2008 and 33,7% higher than on 1 October 2008! Bond yields have drifted lower over the quarter as inflation expectations moderated, which again demonstrates the value of a diversified portfolio of retirement assets.

The trend in offshore equity markets over the quarter has also been sideways.

The price of oil has moderated slightly over the quarter as focus on the crises in the Middle East and North Africa shifted.

Subsequent to quarter-end, the price of gold has rallied again to over US\$1 600. This support is not only due to debt problems in Europe and the USA, but also due to strong buying from India and the east.

### Manager Review

With the decrease in volatility, the differences in returns achieved by asset managers have correspondingly become smaller over shorter periods. Year-to-date returns on balanced portfolios ---- 4,6% and 1,5%. Returns by the large managers on their balanced portfolios over a five year period have been between 15% p.a. and 9,5% p.a. respectively.



Some comments on asset manager performance are:

- Stanlib has maintained its recovery and has the strongest performance of the large managers' balanced funds under Herman van Velze, who joined early in 2009, over the last two years. Longer-term performance through the debt crisis is however still lagging.
- Close on Stanlib's heels is Prudential, which now posts strong upper half results over all periods up to five years.
- Coronation and Sanlam have delivered strong performances in the recent past, close on the heels of Stanlib and Prudential.
- Investec's strong longer-term performance numbers have carried them through but after lagging last year, the year-to-date performance number is again promising.
- The merger of RMBAM and Metropolitan is an ongoing process and progress was dented when Romeo Makhubela decided to join Vunani recently. Unfortunately, these changes still reflect in the performance numbers.
- Allan Gray has maintained its conservative positioning in the markets. Its performance numbers over 12 months are now lagging their whole peer group, but 3-year and 5-year numbers are still in the upper half in comparison to its peers.
- RE:CM is a manager that states an objective of deep negative returns and although their 12-month number lags, shorter-term numbers and performance through the debt crisis of 2008 on a 3-year and 5-year basis are strong.

## **Outlook**

As governments find their way through a difficult process of dealing with debt, we expect that markets will swing with short-term sentiment. The full valuation of equities, high commodity prices and the sustainability of low interest rates have moderated return expectations of most asset managers. The harvesting of dividends, rent and coupons is therefore an important part of returns at the moment. The optimum timing of investments offshore and achieving better diversification in portfolios are likely to affect portfolios in the short term. A diversified approach favouring equities over the long term is still advocated.

## **Other Developments**

Asisa has recently launched its Code for Responsible Investing (Crisa). This code is the second of its kind that has been accepted in the world, after the UK Stewardship Code and is an expansion of the UN Principles of Responsible Investment. It is based on five principles including:

- incorporation of sustainability considerations, including environmental, social and governance considerations in investment decisions;
- demonstration of ownership responsibilities, even if one is a passive investor;
- promotion of a collaborative approach to implement the principles of Crisa;
- recognition and management of conflicts of interest; and
- transparency and disclosure of policies.