SIMEKA CONSULTANTS & ACTUARIES

June 2013

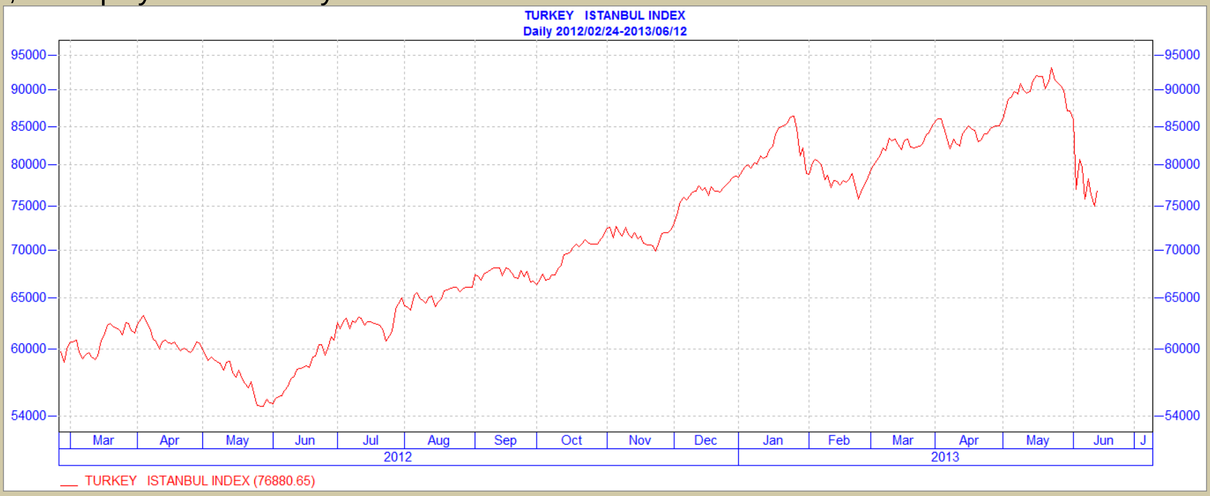
MARKET insight

Targeted market commentary

The state of financial markets

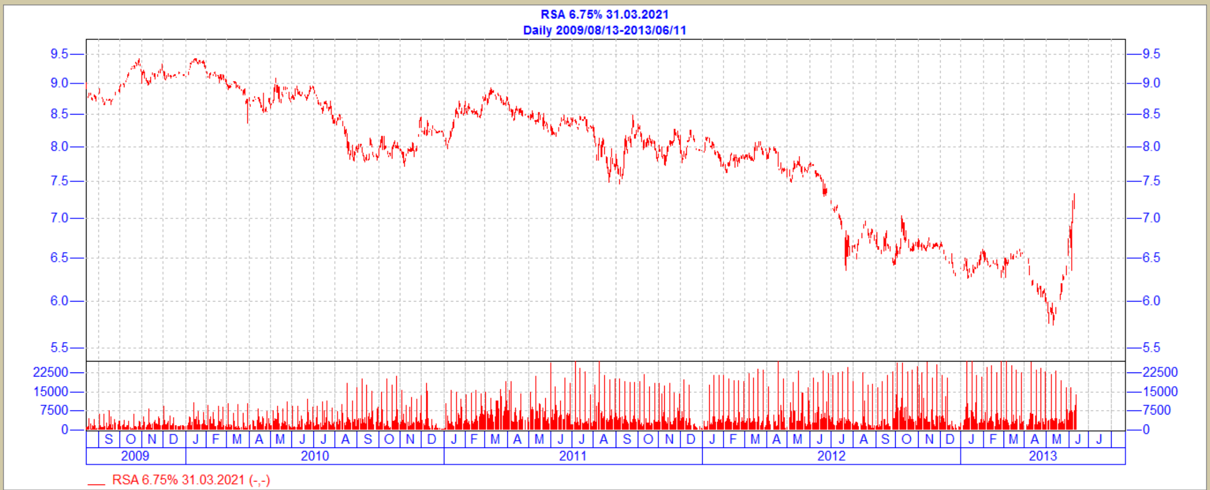
The recent volatility in financial markets around the world is the result of investors reassessing expectations of economic growth and market valuations.

In Brazil, the Bovespa came 12.9% off the recent high in May and more than 22% off the high achieved in January. To date, the Brazilian real weakened by 8% in 2013. In Turkey, where civil unrest currently prevails, the equity market fell by 17.5%.

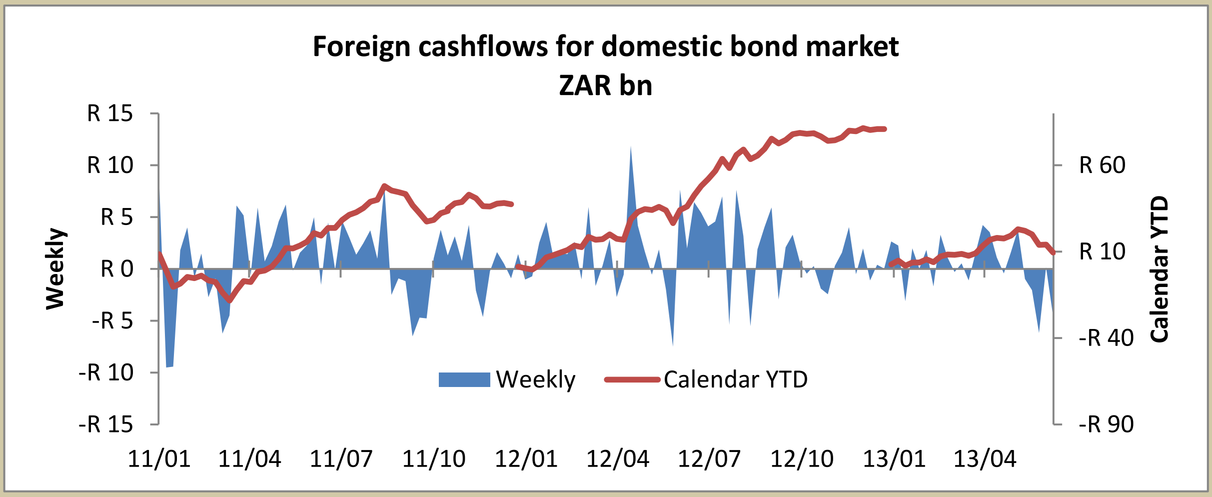


In the same period the Japanese nikkei was down 15% and the Dow Jones Industrial softened by 2.5%. The United States 10 government bonds yield softened to above 2.2% from levels experienced in the most recent months (1.7%).

Since May 2013, South African equities are down by nearly 6%, bonds yields are up by approximately 2% resulting in capital losses on the prices of bonds and the rand has weakened by nearly 13%.

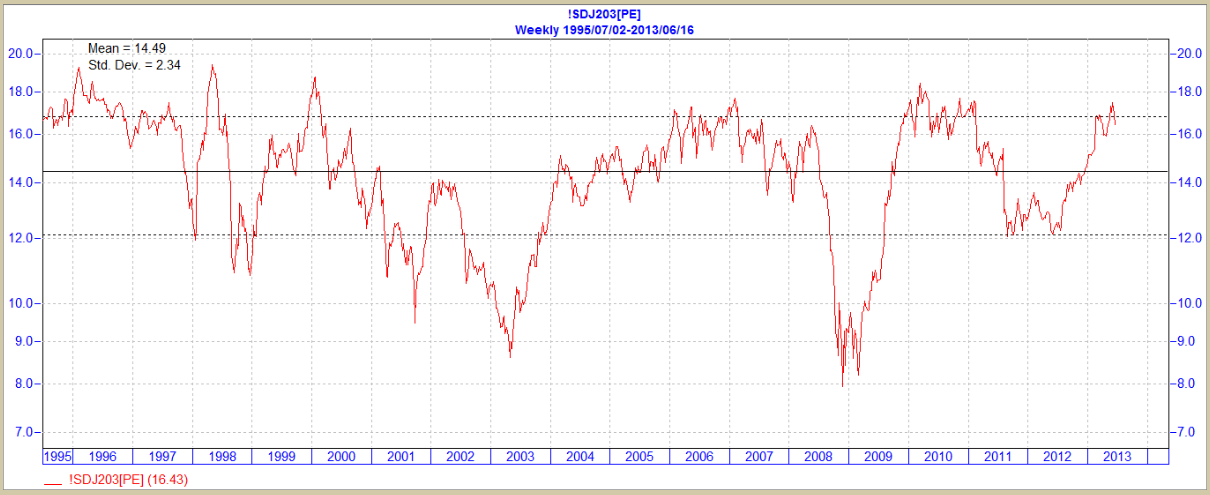


Recent drops brought financial markets in line with economic realities, and investment opportunities in developed markets were generally viewed more favourably. Global investors reduced emerging market bond and equity allocations in favour of investments in established markets. Considering that emerging markets were generously valued after strong price increases in 2012 (and in certain cases in 2013) the recent downward adjustment is not out of place.
In South Africa, domestic bond yields increased following concerns about industrial action, slower than expected GDP growth and worrying deficits on the current account and budget. Foreign investors have reduced exposure to South African bonds by R13.6 billion since May 2013.

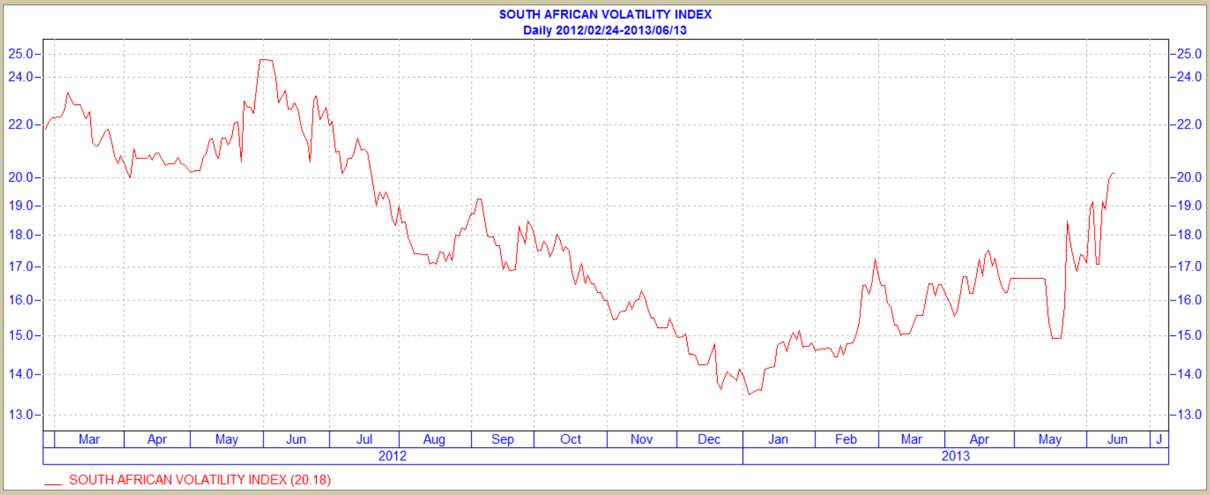


Before the recent increase, bond yields were at historically low levels which could not be sustained indefinitely. At present levels, bond prices are much more attractive than previously and we expect that some investors may align their portfolios accordingly.

Similarly, it is difficult to justify a price-earnings ratio of nearly 17 times for the FTSE/JSE All Share index in the present economic environment and the downward move of the index is not surprising.



The fear gauge of the South African equity market, the South African Volatility Index has also recently increased from 13.8% in January to 20.2%. The increase reflects expectations of unsettled conditions to prevail in the equity market.



The question asked by many retirement fund members is whether the unsettled markets represent the "new normal?" We don't believe this to be the case. Concerns about increased liquidity represented by quantitative easing will continue. The timing and volume of the various quantitative easing programs are likely to impact on financial markets in the short-term.
The longer term concern is how much more quantitative easing can be absorbed in the economies. We expect volatility in bond yields from time to time until long-term sustainable levels have been reached. This will no doubt have a sobering influence on equity prices from time to time.

In addition, the better investment outlook in established markets presents investors with favourable risk-adjusted investment opportunities, often at the expense of emerging market exposure. Typically areas subject to social and labour upheaval are avoided by investors.

We expect that the domestic equity market will continue to reflect these uncertainties, but that ultimately a more positive outlook will prevail.

Retirement fund members should look to invest according to their long-term strategy to meet their ultimate objective. Members approaching imminent retirement should continue to exhibit caution and remain invested in lower risk strategies, while younger members should continue to invest in growth strategies with equity exposure underpinning the strategy.

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