

**INVESTMENT REPORT: FEBRUARY 2011**

**22 02 2011**

**Review: 2010 ; - Local Markets:**

Equity markets globally, as well as our local JSE closed the year on strong positive levels. (See graph)



From this graph it is clear that the first part of 2010 resulted in a rather bumpy ride for equities. (After the strong performance of 2009.) The last few months delivered the returns that resulted in a successful year for equities on the JSE.

The results of the various sectors are as follows: (As reported by Sanlam – Glacier on 10 01 2011)

INDEX	CLOSE	1 Year	3 Years * (PY)
All Share	31 929	18.3 %	6.2 % ( 3.5 %)
Financial	21 936	18.1%	4.5 % ( -5.3 %)
Industrial	32 144	24.3 %	4.5 % ( 6.3 %)
Resources	30 522	10.6 %	1.7 % ( 12.7%)
Property	392.21	31.4 %	12.2 % ( 11.6%)
All Bond	345.51	15.5 %	10.3 % ( 5.8 %)
Cash	251.00	7.0 %	9.2 % ( 10.1%)

(\* 3 years – annualized returns )

Although 2010 was not such a good year for resources, all the other equity sectors did well. Listed property was again the star performer with bonds (Government and Corporate) doing very well. From the 3 year statistics, it is clear that the impact of the 2008/2009 financial crisis, still weighs heavily on the medium term results.

**INTERNATIONAL MARKETS:**

International markets performed well and, in general showed continued recovery from early 2009. However, the performances were more subdued than that of 2009.

INDEX	CLOSE	1 Year	3 Years
MSCI World	1 281.41	9.7 %	(- 6.0 %)
S & P 500 (Intern)	1 271.50	14 %	(- 3.4 %)
FTSE 100 (Brittan)	5 984.33	10.6 %	(- 1.9 %)
DAX (Germany)	6 142.30	19 %	(- 3.9 %)
Nikkei (Japan)	10 541.04	(- 0.1 %)	(- 10.5 %)
<b>MSCI EM (Intern)</b>	<b>1 147.14</b>	<b>15.9 %</b>	<b>(- 2.2 %)</b>
Australia	4 812.00	(- 1.4 %)	(- 9.0 %)
Brasilia	70 057.20	2.1 %	4.7 %
India	19 691.81	12.8 %	(- 1.6 %)

The DAX in Germany was the top performer of 2010. (Of the developed economies). Emerging markets, which includes SA, also performed well in general. Of the so-called new economies, the BRIC countries, India (13%) and Russia (14%) managed to deliver positive returns but the Brazilian and Chinese financial markets disappointed with no or very low returns. This is despite the fact that these countries actually achieved high economic growth percentages for 2010. (8% +). This is a typical example of little correlation between economic growth and the performance of equity markets. This however does not often happen, since economic growth is normally the foundation of performance on equity markets.

It is clear however, that similar to the local JSE results, the 3 year statistics are still mostly in the red. (Although not as badly as a year ago!)

In short, as far as international financial markets are concerned, fund managers had a more difficult time than in 2010 to find value and generate returns on equity markets. After the rapid recovery in 2009, especially the second half of the year, consolidation on markets during 2010 had to be expected.

### **EXCHANGE RATES**

Our SA Rand continued strengthening against the currencies of our primary trading partners during 2010. AS in 2009, exposure to international funds and assets, did not really add value for investors in terms of SA Rand value. This applied to offshore funds as well as local asset allocation and international funds. Keep in mind though that this exposure is critically important for diversification purposes. As explained in the previous paragraph, international markets did perform reasonably well and many funds invested in, did deliver good returns in the offshore currency of the particular fund. Exchange rate movements are mostly cyclical, and investors should not be over concerned about the impact thereof.

	30 12 2006	30 12 2007	30 12 2008	31 12 2009	<b>31 12 2010</b>	<b>- VJ %</b>
R / \$	R 7 - 01	R 6- 87	R 9-35	R 7.39	<b>R 6.61</b>	<b>89%</b>
R / Euro	R 9 - 25	R 10 -12	R 13- 34	R 10.61	<b>R 8.84</b>	<b>83%</b>
R / £	R13 - 72	R 13 -57	R 13- 96	R 11.92	<b>R 10.28</b>	<b>86%</b>

### **PRESENT ECONOMIC ENVIRONMENT: - INTERNATIONAL**

The so-called BRIC countries; - Brazil, Russia, India, and China, continued their stellar economic growth in 2010. China surpassed Japan as the second largest economy in the world, in 2010. Years before initially expected! Europe seems to slowly recover from their financial and economic woes, with France and especially Germany taking the lead, not only economically, but also in terms of Euro leadership. (Probably to the frustration of the British). The financial situation of some of the Euro Countries is still going to be a headache for some time. (Greece, Spain, Italy, Ireland, etc)

Asia, Vietnam, Singapore, South Korea, etc performed well in terms of their economies. Japan is still the “sleeping” economic giant of the east! In terms of economic growth and the performance of their stock market (Nikkei), nothing really exciting happened.

The USA surprised in the last couple of months with good recovery economic data as well as company results. This also reflects in their stock market results as mentioned earlier. Could it be that the “lost decade” in terms of the US markets and economy, is over? Is the US economy going to stand up to the challenge of the “new” economies taking the world by storm? Some analyst are pointing out that the “tick up” in US economic data is mostly the result of Government incentives and aid packages. Could be, but many fund managers are now seeing value on US financial markets again.

The overthrow of governments in the Middle East and surrounding area has been in the news lately, and is still headline news at present. Tunisia was a surprise event – for the international world, Egypt followed and from there, the upheavals and demand for change of governments, spread to various neighboring countries. (Bahrain, Libya, Yemen, Iran, etc).

### 3.

It seems that this wave of change is mostly inspired by the dire need of the populations of these countries to get rid of poverty AND tyrant dictators of many years and to then establish democratic leadership. The question is whether this will actually materialize. Where is this going to end? Who will be the real beneficiaries of possible change? Time will tell. In the mean time these events has not really affected international financial markets, BUT it could spell possible real risk for the international economy. The price of OIL is already affected by the events. The risk of this instability in the Suez Canal area can only mean trouble. At present it seems that Libya could be the watershed to determine in which direction events will unfold. Again, time will tell!

In general, world economic conditions are still improving (since May 2009), and this fact is to the benefit of investors worldwide. The increasing price of OIL and rising inflation in many leading economies are concerns and can lead to price increases in a world with many border line economies and very poor countries. Despite this, the leadership of many leading economies, as well as certain smaller growing economies, is dedicating all their efforts to stimulate economic activities, create jobs, uplift their people and fight poverty. This effort is now more visible than in previous years when governments were often more concerned with enriching themselves and increasing their international political and military power. This renewed worldwide focus on economic growth creates opportunity for companies to grow and perform. In this lies the value for our fund managers and off course, our investors. With our present “Strong” SA Rand, it is important to take advantage of this situation and diversify investments to include international exposure or assets.

#### **LOCAL ECONOMIC FACTORS**

Our local economy is also showing encouraging signs of recovery to sustainable positive growth, although not at an impressive rate. (Approx 2.5%+ for 2010 – waiting for final data). Economic data released since the beginning of the year are clearly indicating increased economic activity as well as consumer spending. (e.g.; - vehicle sales). Certain government policies, practices and administrative aspects are still a major constraint to economic growth. Politically inspired policy statements, financial and political power play, poor administration, lack of financial discipline and control, etc., plays a major part in discouraging economic and business confidence and performance.

Despite these “challenges”, SA companies and business sector has performed very well in a very challenging economical environment. By setting worldwide best practice standards and seeking innovative solutions to achieve successful results, many companies recently released very positive financial results. This is also reflected in the performance of the JSE..

The fact that SA was invited a while back to join the BRIC countries as an economic entity (or group), must however be taken with a pinch of salt. (To be the “S” in the “BRICS”!). Our economy is not, by far, on the scale of the economies of the existing “BRIC” group. Although our government seems very impressed with this development, our economy can only be of very little immediate value to these countries. The BRIC countries and especially CHINA sees SA as a long-term proposition for a stake in Africa, to the benefit and wealth of their own people. Although there are very definite benefits for our local economy to have seemingly “preferred” exposure to these larger economies – the protection of own rights and resources will have to be guarded vigilantly.

South Africa should rather compete (and compare itself) with economies of similar size (GDP);

	POPULATION	EXPORTS % of GDP	GDP/ PP / USD \$	UNEMPL %
Argentina	40 mil +	24 %	\$ 8 235	7 %
Thailand	67 Mil +	77 %	\$ 4 043	1 %
Venezuela	28 Mil +	30 %	\$ 11 246	7 %
Malaysia	30 Mil +	100 % +	\$ 8 209	4 %
Denmark	54 Mil +	54 %	\$ 62 118	4 %
<b>SOUTH AFRICA</b>	<b>49 Mil +</b>	<b>35 %</b>	<b>\$ 5 678</b>	<b>25 %</b>

( Stats provided by Trading Economics)

4.

Even against these economies listed in the table above, we compare rather poorly in terms of productivity and employment statistics. The result of this is an extraordinary tax burden on a few South Africans to finance the welfare of the majority of our population.

### **IMPACT OF ECONOMIC and MARKET ENVIRONMENT ON PORTFOLIOS**

Although historical returns do not necessarily indicate future performance, the following results may be an indication of the return potential of certain funds in 2010.

	<b><u>1 Year</u></b>	<b><u>3 Years</u></b>	<b><u>5 Years</u></b>
INCOME FUNDS	9 %	9.5 %	9 %
INCOME FUNDS (Var. Strategy)	12 %	10 %	9 %
BOND FUNDS	16 %	10 %	7.5 %
PENSION: LOW EQUITY	5 %	8.5 %	10.5 %
PENSION: MEDIUM EQUITY	10 %	8 %	11 %
ASSET ALLOCATION – TARGET RETURN	13 %	10.5 %	12 %
PROPERTY FUNDS	25 %	13 %	15 %
GENERAL EQUITY FUNDS	16 %	7 %	14 %
WORLDWIDE FUNDS(Equity Allocation)	(-9 %)	2 %	7 %
<b>MONEY MARKET FUNDS</b>	<b><u>-6.7 %</u></b>	<b><u>-9 %</u></b>	<b><u>8.8 %</u></b>

NB. These results are averages (annualized) by close calculation on primary selected funds utilized by GERBER & LOUW, in above categories, for our investment clients. (As at **12 01 2011**) (Portfolio cost not included – approx 0.5% to 1.25%)

### **PERFORMANCE OF SELECTED FUNDS AND PORTFOLIOS: 2010**

Fund managers mostly took a more cautious approach to investment opportunities, asset class and sector diversification in general, in the post financial crisis period. (From early 2009). For this reason, investors should not directly compare the returns from the funds they invest in, to the returns from certain indexes, in a specific year. Most of the fund managers we regard as our first choice managers, invest with a medium to long term view. It is therefore quite possible that such a fund could seem to underperform in a specific year. For example some of the Allan Gray funds in 2010. Investors should not be alarmed by this situation and there is absolutely no reason to consider changes to fund compositions on portfolios because of this. Medium to long term results of these funds attest to this.

Attached is a document with the performance data of selected funds in 2010. These are the funds that you as investor, to a more or lesser extend, were exposed in your portfolios. We only provide the results of our primary selected funds. In certain cases other competitive funds are utilized. Keep in mind that funds in the same sector are not always directly comparable in terms of strategy followed. Please note that the returns are net of costs in the funds, but not in your portfolios. Depending on your investment amount, portfolio company, etc., your portfolio has a cost component of on average between 0.5% and 1.25%pa.

I would again, strongly recommend that you focus on the 3 and 5 year annualized returns to really evaluate the value and competitiveness of a particular fund. Short term results can be very misleading

Thank you for your continued support. Regards,

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