



financial services group

# MONTHLY MARKET REPORT JULY 2010

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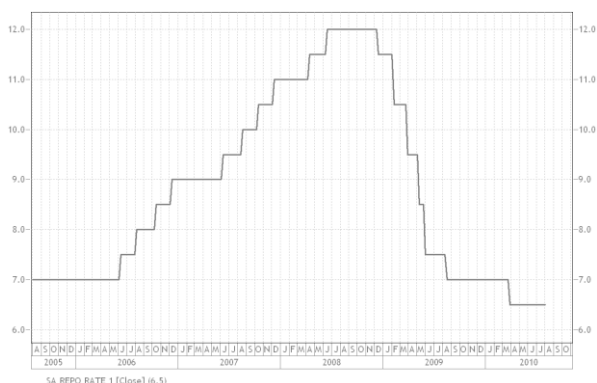
## JULY 2010 COMMENTARY

### Introduction

The print version of this Report contains a table setting out the most recent month's performance of a small sample of economic indicators (the repurchase rate and the rand-dollar exchange rate, for example) as well as those indicator's year-to-date and 12 month movements which we, for the most part and especially so in the electronic version of this Report, largely ignore. Short-term market movements for the purposes of long-term portfolio management are largely irrelevant. They are, in most instances, completely random. However, we always keep a close eye on them and July's movements deserve more airtime than dinner table conversation can provide.

### The South African Repurchase Rate

SA Repurchase Rate, Weekly  
Jul 05 - Jul 10



It's not often that the continuation of the status quo merits attention. South African interest rates were left unchanged at the July meeting of the Reserve Bank, a decision in line with our view on interest rates for the remainder of the year. However, NFB Asset Management is not alone in commenting on interest rates. There was a large swathe of the investment community forecasting, in some cases calling for, an interest rate cut of 50 basis points. Whilst we continue to believe that interest rates will remain at these levels for the remainder of the year - particularly whilst certain labour force groups continue to argue for salary increases way above current inflation rates - the chances of an interest rate decrease have increased further.

These increased odds can be attributed to four key factors:

- Rising unemployment (in excess of 25%) and potentially sluggish economic growth;
- Anemic credit growth - private sector credit extension is barely at 1% year on year,
- Decelerating consumer inflation - the annual change in CPI, most recently recorded at 4.2%, has rapidly returned to the inflation target range of 3 to 6% and
- Continued rand strength (see following paragraphs), which has contributed to the favourable inflation environment.

Private Sector Credit Extension, Annual Change, Weekly  
Jul 05 - Jul 10

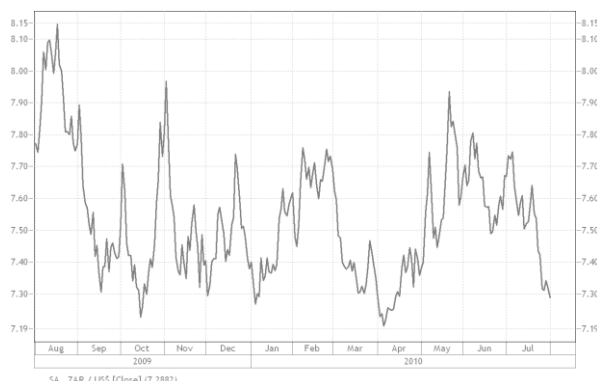


### USDZAR; rand strength

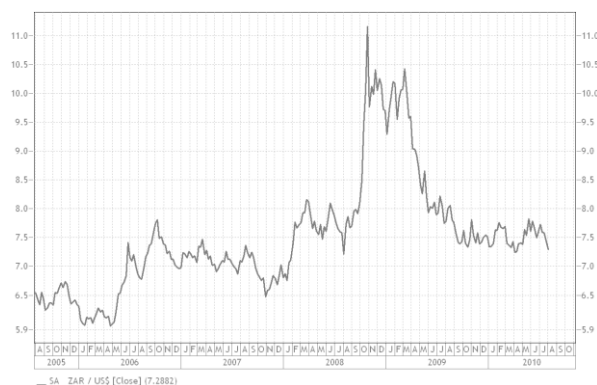
The rand's recent strength has been remarkable. We have included two charts with this Report to place rand strength in context. The first chart is a daily reading of the rand versus the dollar for the last year; you'll note two things: the unusually tight trading range (between 7 and 8) and rand strength since May 2010. The second chart is a weekly reading of the rand-dollar. Again there are two noteworthy items: first, that the rand has been at these levels since 2006 (excluding, of course, 2008's sell-off), and, second, that the rand has tested the 7.20 level three times in the last year or so. 7.20 is proving to be a barrier of some significance, which, if broken, opens a path through to 6.50.

The most recent rejection of the 7.20 level came about as a result of comments during the first week of August 2010 from the ANC that short-term capital inflows should be taxed. Talk like this reminds us of Ben Bernanke lowering the market's interest rate expectations simply by stating that interest rates would be lower for longer without actually lowering interest rates themselves. Weakening the rand through rhetoric, though somewhat unpalatable at times (particularly when of the economically inexplicable variety), is to be expected. Whether rand weakness rather than revenue income is the objective of this commentary remains to be seen. Foreign portfolio inflows for the year-to-date have amounted to an astounding R75bn-odd, most of which has found a home in the bond market (see further commentary below).

USDZAR, Daily  
Jul 09 - Jul 10



USDZAR, Weekly  
Jul 05 - Jul 10



### Destination: SA Bonds

An astonishing R20bn of foreign portfolio inflows hit the South African bond market during July 2010. It should, therefore, not be terribly surprising that the bond market is one of South Africa's best performing asset classes for 2010 (returning just short of 10%). The great risk inherent then is that these inflows could just as quickly turn to outflows. In addition, these inflows are artificially lowering interest rates; which then gives the South African interest rate environment the appearance - though not necessarily the reality - of lower interest rates to come.

### JULY 2010 DATABANK

	Index Value	Last Month	Year-to-Date	12 Months Ago
SA Repo Rate	6.50%	0.00%	-0.50%	-1.00%
JSE ALSI	28,355.21	7.98%	2.49%	16.89%
ALBI	328.81	4.12%	9.97%	12.98%
R157	7.58%	8.03%	8.39%	8.37%
USDZAR	7.29	-4.95%	-1.51%	-6.23%

All charts and data are sourced from I-Net Bridge.