



financial services group

MONTHLY MARKET REPORT JANUARY 2011

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License No. 25962

JANUARY 2011 COMMENTARY

Short-Term Distracters

Investing should be done with a long-term mindset. Investing when done with a short-term mindset is speculating, the results of which can be and often are disastrous. Here's a short, though naturally incomplete, list of current events that over the short-term may distract the unwary investor:

- Demonstrations in Egypt. Decades of oppression and the loss of life are tragic and a sad blight on the condition of humanity, a full discussion of which is beyond the scope of this Report. Thus far around 97 people have been killed in demonstrations across five major Egyptian cities against the 30-year long reign of President Mubarak. Markets, however, have barely reacted, surprisingly so for this is just the kind of short-term distracter markets usually fall prey to, though there was a brief period on Monday the 31st of January when markets in the East were taking a turn for the worse; that period has since passed.
- Q4 2010's equity market performance. Of the JSE All Share Index's 19% total return for 2010 half came in the final quarter of the year. Much the same can be said of other equity markets around the world. Whilst such strong performance is always welcome, suddenly investing into equities on this basis is foolish particularly in terms of our local equity market whose valuations were already looking full going into the last quarter of last year.
- The rand's performance since the middle of December 2010. The rand has enjoyed around two years of marvelous strength relative to the major currencies around the world, a further chunk of which was achieved in December 2010's thin markets. Much of this performance was as a result of foreign portfolio inflows which sought yields that simply weren't available in their home countries. The last four or five weeks have seen around R10bn flow back out of our country. Remember, one swallow does not a summer make. Also remember that currencies can be notoriously fickle.

Medium-Term Considerations

And now, as you might very well expect, for a list of medium term market circumstances that should have long-term investors' attention but that don't necessarily provide for immediate investing opportunities:

- Rolling European sovereign and banking system bailouts. We coin the term 'rolling bailouts' to deliberately invoke memories of South Africa's rolling blackouts as our mind's eye sees a series of economic lights being turned off across Europe. First there was Greece and then, during 2010, there was Ireland. We can reasonably expect that further countries will join the list of those benefiting from the trillion-dollar European Stabilisation Fund, think Belgium, Spain and Austria, perhaps even Italy. As they do we can then reasonably expect German influence to become even further entrenched.
- Global interest rates. Developed markets are likely to stay at these multi-generational low levels for some time longer; whereas some developing markets have already begun to either lift interest rates, raise reserve requirements or some combination of both (think Russia, China, India and Australia in this space). We are particularly interested in three sets of interest rates: US long-term rates which have ratcheted higher rather than lower post-QE2 as their bond markets begin to price in the long-term costs of quantitative easing; South African interest rates where the next move is likely to be up, though not before the first half of 2011 has passed, and rates as set by the European Central Bank which are rumored to be on the rise. Beware: global interest rates, as well as inflation rates, will not be at these ridiculously low levels for ever. Be cautious of anchoring yourself and your investment portfolio to current market conditions.
- Rising food prices. A combination of rising global prosperity, larger population sizes, moves up the diet curve and food for ethanol, to note a few of many causes, is likely to result in substantially higher food prices. Expect a resultant knock on effect for inflation in years to come. Similar comments can be made of basic human needs: shelter, water, electricity and transport too.

Ultra Long-Term Trends

To round out our discussion here is a short list of one or two, amongst many more, ultra long-term issues that will affect investors:

- The continued rise to ascendancy of China and India. In particular we look to their development of an internally-focused; consumer-orientated economy. If achieved, this could turn the nature of global trade on its head. Instead of importing raw materials and turning these into products for consumption by the West, China may find its import mix consisting of both raw materials and final products produced by the West. China's surpluses may then move out of her accounts and into those of Western countries who so desperately need to rebalance their economies and, more specifically, their economies' books.
- Social benefits. In order to balance their economies some pain will have to be taken. Pain postponed is pain inflated. Pain taken immediately has been acutely demonstrated most recently by the performance of the UK economy which registered negative growth in Q4 2010 whilst the rest of the world recorded fairly healthy growth rates. This is as a result of some rather severe austerity measures enacted post the Credit Crisis. The UK of today reminds us of the Canada of a generation ago which took its medicine and is in much better shape today. These are but two countries from around the world that have addressed or are beginning to address the promises made to their citizens. Expect many more - particularly Western - countries to do so by lowering benefits whilst raising taxes.
- Population pyramids. Western countries - and here the leader is actually in the East (Japan) -are aging. As a result they will begin to lack the workforce required to do the heavy lifting in terms not only of production but also of generating taxes. Expect to see immigration criteria change drastically to encourage youthful, aspirant workers to those aging countries.

Through a short-, medium- and long-term approach we've highlighted some of the major investment risks visible in the present moment. The key then is not to understand and appreciate every single one of these risks, as well as all of those we haven't mentioned, which is essentially impossible, but to appropriately position your investment portfolio so that your personal appetite for risk is matched with the risks your portfolio might be exposed to. If you can do that you are a long way ahead of the investing crowd. Maintaining your investment focus and displaying some fortitude if, and more likely when, these risks present themselves will put you even further ahead.

JANUARY 2011 DATABANK

	Index Value	Last Month	Year-to-Date	1 Year
SA Repo Rate	5.50%	0.00%	0.00%	-1.50%
JSE ALSI	31,398.75	-2.24%	-2.24%	17.70%
ALBI	336.40	-2.14%	-2.14%	12.20%
R157	7.88%	7.31%	7.31%	8.38%
USDZAR	7.18	8.40%	8.40%	-5.80%

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