



financial services group

MONTHLY MARKET REPORT APRIL 2011

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APRIL 2011 COMMENTARY

Introduction

There has been much in the headlines since we last issued a Monthly Market Report that is noteworthy. The nuptials of a certain Royal Couple and the death of Osama bin Laden amongst them. However, headlines are more useful to those media sources looking to gather them, to political commentators looking to pursue a particular agenda or to economists looking for somewhere to hang their hats than they are for the purposes of investment management. And given their nature and frequency there are more than enough headlines for all the media-mongers, politicians and economists amongst us.

Naturally, we're more than happy to let those groups of individuals grapple over the headlines whilst we step back and look at the larger issues. Issues that don't confine themselves to the top-half of a newspaper, that don't constrain themselves to a particular month, geography or season. Just what then - after what has been a rather lengthy introduction - are the broader issues that face us?

Global Oil Security

The unrest that has spread across the Middle East and North Africa has far more of an impact on investment management by transmitting itself through the oil price than it has through the struggle for democracy. Given the military-elite component in the outcome of many of these countries' civil disturbances we'd argue that regime change is hardly a democratic process at all, in some cases it's hardly humanitarian.

Markets are amorphous beasts but there is one thing we can be certain of and that is that markets dislike uncertainty immensely. The uncertainty currently present in the MENA region transmits itself into the oil price as a risk premium; a premium charged for uncertainty related to global oil security and exacerbated by a fair-sized element of speculation. A higher oil price translates very quickly into global inflationary pressure; not solely through the price of transportation alone but also through the price of transportation's effect on everything that must be transported. Which is pretty much *every thing*.

For the most part an investment portfolio should seek to provide inflation-adjusted returns. The higher inflation goes the more risk a portfolio needs to take on to accommodate for this, or the more comfortable investment managers and their clients must become with investment portfolios that only just exceed inflation or perhaps even fall below the inflation rate for a period of time.

**Brent Crude Spot Price
Daily, Jan 10 - May 11**



— OIL BRENT CRUDE ICE S/BARREL [Close] (113.26)

Debt

We've written extensively in previous issues of this Report on the debt situation facing most developed, first-world markets (most particularly the US, the UK, Japan, Ireland, Greece and Portugal) so we won't retread that ground. We would like to note, however, that the UK's hard-line austerity measures have begun to pay off. The latest measure of GDP in the UK came in at a miserly 0.5%. How is that a good thing you might ask? GDP generated by government was -0.5%; that of the private sector was around 1%. Solving sovereign debt issues is going to be a combination of curtailed government spending (austerity measures) and the growth of the private sector, plus a few other factors (time, inflation, productivity amongst them).

Roughly speaking, the expected long-term return of the stock market is equal to dividends, plus inflation, plus GDP-growth, plus the change in the rating of the market. Companies are holding onto cash so dividends are low; we already know inflation rates are low; GDP rates are coming in lower than expected. That leaves a change in rating as the sole remaining potential driver of stock market returns. Relying on rating changes to drive returns in an investment portfolio is risky business, more so when ratings are at or above their historic averages as they are now. The current environment requires a greater degree of patience and a rapier-like response when markets fall below historic ratings levels. Increasing equity exposure at such a time may just be a winning strategy.

Related to debt, the euro

EURUSD
Daily, Jan 10 - May 11



As market participants wrestle with the *relative differences* between countries; particularly between that of the US and euro-region, we can reasonably expect to see meaningful moves in the exchange rates of the currencies between them. Trying to forecast just which way either country will go, and therefore whether that countries' currency will appreciate or depreciate relative to another is a fool's game. Maintaining a diversified exposure to currencies in an offshore investment portfolio is likely to be a rather smart idea. So is being honest about whether offshore exposure is a play on the rand or a true attempt at diversification. If it is about playing the rand then expect to experience periods of elation and misery, probably in equal amounts, over the next few years. If it's truly about diversification then make an attempt not to covert foreign holdings into rand terms for valuation purposes. Doing so is likely to allow you to sleep far better.

Conclusion

We've shared with you three broad issues that face us at present and we've done so in fairly forthright fashion. Not all of these issues will affect your investment portfolio and if some of them do they may affect you to a greater or lesser extent than illustrated here. It is of critical importance that you work through these issues with your financial advisor in the light of your own personal circumstances, objectives and risk appetite.

APRIL 2011 DATABANK

	Index Value	Last Month	Year-to-Date	1 Year
SA Repo Rate	5.50%	0.00%	0.00%	-1.00%
JSE ALSI	32,836	1.96%	2.23%	14.67%
ALBI	346.0	2.26%	0.66%	9.41%
R157	7.64%	7.82%	7.31%	8.04%
USDZAR	6.56	-2.91%	-0.95%	-3.34%

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