ASSET MANAGEMENT

September Quarter Commentary

Matt Brenzel

INTERNATIONAL

The ANC has learnt that in delaying the disciplining of Julius Malema, the problem has become bigger than it ever should have. Similarly, world political and financial leaders have taken far too long in addressing the financial malaise that continues to dog financial markets. Indecision is often governed by two issues: lack of understanding and self-interest. Nothing illustrates this more than the congressional debate around the US debt ceiling earlier this year. The resultant cost? – Trillions of dollars of losses in asset values. What is needed now more than ever, is the same kind of selflessness that led to the Marshall Plan of the 1940's. European economies were decimated after WWII; a soft target for a Russia intent on spreading communism into weakened states. America realised that the only way to prevent this from happening, was to supply sufficient aid to enable Europe to rebuild itself. As Secretary of State, George Marshall said, "It is logical that the United States should do whatever it is able to do to assist in the *return of normal economic health* in the world, without which there can be no political stability and no assured peace. Our policy is directed not against any country or doctrine but against *hunger, poverty, desperation, and chaos*. Its purpose should be *the revival of a working economy* in the world so as to permit the emergence of political and social conditions in which free institutions can exist" (my italics and what the world needs now). The plan cost $13bn and required the bi-partisan support of the Democrats and the Republicans – which it got. Obviously, there was opposition, but ultimately it was implemented and the result was that for all Marshall Plan recipients, output in 1951 was at least 35% higher than in 1938. The time for talking is over.

Universally weaker across all periods

INDICES (US$)	Quarter	YTD	12 Months
MSCI World	-17.9%	-15.1%	-8.0%
MSCI Emerging	-23.2%	-23.5%	-18.1%
MSCI China	-25.7%	-26.3%	-25.8%
MSCI India	-20.3%	-27.6%	-26.1%
MSCI SA	-17.7%	-22.0%	-12.2%
MSCI USA	-14.5%	-10.1%	-0.7%
MSCI Europe	-23.0%	-17.8%	-14.4%

EM hit by stronger $ and weaker commodity prices.

Difference in political will.

Best country	Quarter	Worst country	Quarter
Peru	-5.2%	Greece	-46.9%
Pakistan	-7.1%	Hungary	-44.4%
Philippines	-7.6%	Austria	-37.9%

Best country	Year	Worst country	Year
Indonesia	-2.4%	Greece	-55.2%
Ireland	-3.1%	Hungary	-39.4%
Switzerland	-6.1%	Egypt	-38.6%

Best sectors	Sept	Worst sectors	Sept
Tech Hardware	-5.2%	Materials	-18.2%
Health Care	-5.3%	Diversified Financials	-14.8%
Telecom	-5.6%	Energy	-12.2%

Broadly defensive

Best sectors	Year	Worst sectors	Year
Software	3.5%	Diversified Financials	-21.5%
Retailing	2.3%	Banks	-21.3%
Health Care	1.2%	Insurance	-16.2%

Top strategy (US only)	Quarter	Worst strategy (US only)	Quarter
Divi yield	-4.1%	Hi beta	-31.5%
ROCE	-14.8%	Low price	-29.3%
ROE	-14.9%	Low PEG	-25.4%

Top strategy (US only)	Year	Worst strategy (US only)	Year
Divi yield	10.8%	Low price	-17.1%
ROCE	4.0%	Hi beta	-16.3%
ROE	3.5%	Upwd earnings rev.	-9.0%

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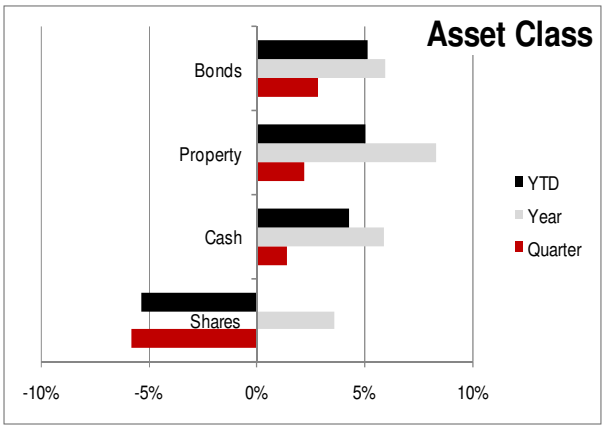
LOCAL (*Ranking of the following 6 graphs is based on performance in the Quarter. Shaded rankings in the tables are based on weighted contributions.*)



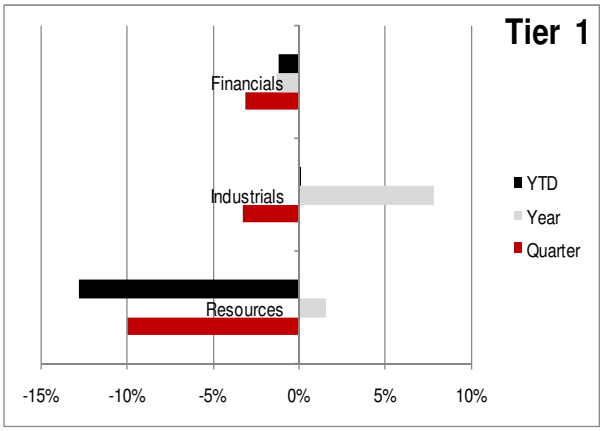
ALSI	%ch Qtr	Rank	ALSI	%ch Year	Rank
AngloGold	19%	1	SAB Miller	15%	1
GoldFields	26%	2	GoldFields	18%	2
SAB Miller	6%	3	Sasol	7%	3
Billiton	-19%	166	Billiton	-5%	166
Anglos	-18%	165	Standard	-16%	165
Richemont	-18%	164	Anglos	-3%	164
Property	**%ch Qtr**	**Rank**	**Property**	**%ch Year**	**Rank**
Acucap	10%	1	Growthpoint	3%	1
Redefine	2%	2	Acucap	8%	2
Resilient	4%	3	Resilient	4%	3
Growthpoint	-3%	19	Emira	-11%	19
Emira	-12%	18	Hyprop B	-52%	18
Hyprop B	-29%	17	Redefine	-1%	17
Bonds	**%ch Qtr**	**Rank**	**Bonds**	**%ch Year**	**Rank**
3-7 Years	3.4%	1	Infl.-Linked	9.2%	1
Infl.-Linked	3.0%	2	3-7 Years	8.6%	2
7-12 Years	3.0%	3	1-3 Years	8.5%	3
1-3 Years	3.0%	6	7-12 Years	6.6%	6
12+ Years	1.9%	5	Cash	5.9%	5
Cash	1.4%	4	12+ Years	2.0%	4

Q1: resources in.
Q2: resources out.
Q3: resources out.
Billiton proves that liquidity overrides ratings during fearful times

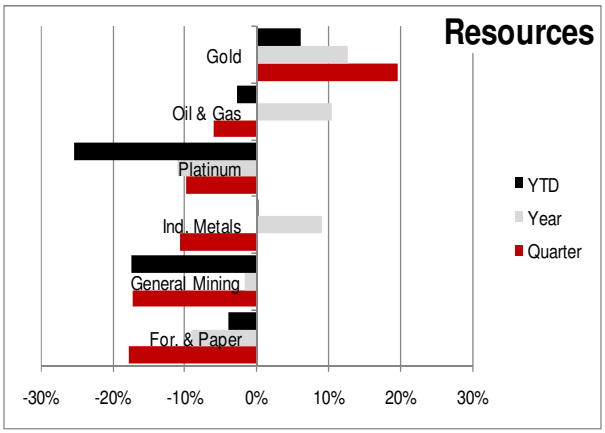
Guaranteed earnings allocation to Hyprop A accentuates volatility of the B share.

Belly of the yield curve outperformed in the quarter.

Shares were well-and-truly on the back foot as continued lack of resolution of the problems in Greece and the USA plague markets. Add to the mix worries about the impact of failing property developers on the Chinese banking sector, and it's no wonder that risk aversion is high and rising. The hunt for yield remained the enduring theme.



All three tier 1 sectors were in negative territory in the quarter. Interestingly, only the Financial sector achieved negative returns in all three measurement periods.



RESI10	%ch Qtr	Rank	RESI10	%ch Year	Rank
AngloGold	19%	1	GoldFields	18%	1
Goldfields	26%	2	Sasol	7%	2
Exxaro	-4%	3	Anglogold	5%	3
Billiton	-19%	10	Billiton	-5%	10
Anglos	-18%	9	Anglos	-3%	9
Impala	-10%	8	Impala	-9%	8

Top- and bottom 3 by-and-large the same over both periods.

Prior to September, Resource counters had been exceptionally weak given the resilience of commodity prices, discounting some kind of crack in the latter. This expectation was finally realised in September, with commodities down by between 8% (Aluminium) and 28% (Silver). Even the traditional "panic hedge" – gold – was off by 11% in the month.

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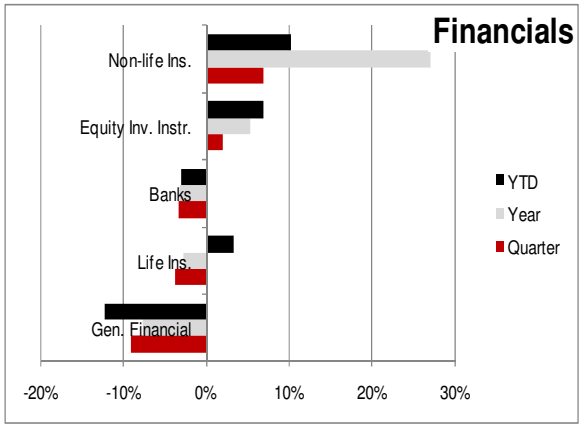
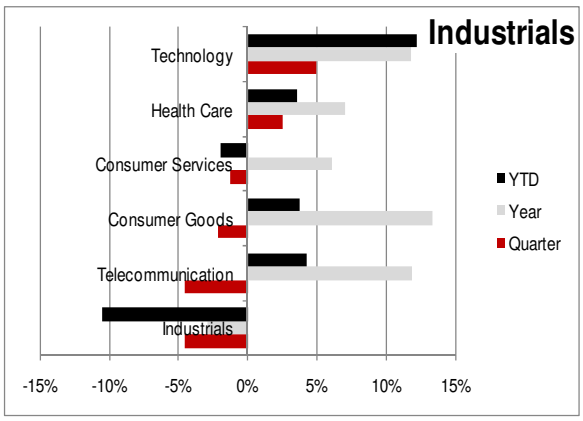


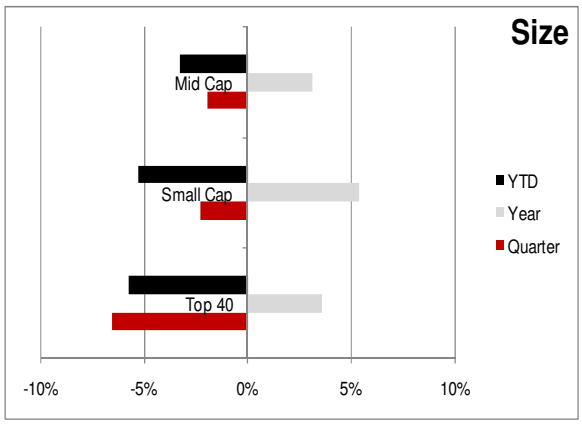
FINI15	%ch Qtr	Rank	FINI15	%ch Year	Rank
Liberty Hldgs	11%	1	Sanlam	3%	1
Reinet	3%	2	Liberty Hldgs	13%	2
Discovery	3%	3	Reinet	6%	3
Standard	-7%	16	Standard	-16%	16
Old Mutual	-9%	15	Old Mutual	-16%	15
Investec plc	-21%	14	FirstRand	-9%	14

An interesting switch is in play as Old Mutual continued to lag after a considerable rerating run at the beginning of 2011. Focus turned to Liberty Holdings which is attracting better quality business and had been too conservative in its value-in-force assumptions. Reinet benefitted from its holding in British American Tobacco.



INDI25	%ch Qtr	Rank	INDI25	%ch Year	Rank
SAB Miller	6%	1	SAB Miller	15%	1
Shoprite	11%	2	MTN	5%	2
Woolies	18%	3	Richemont	6%	3
Richemont	-18%	26	Sappi	-34%	26
MTN	-8%	25	Arcelor Mittal	-28%	25
Naspers	-8%	24	Imperial	-7%	24

Technology (mainly EOH – see below) and Healthcare were the only two Industrial sectors to have been in during all periods reviewed. On a weighted basis, SABMiller proved that bear markets are thirsty work and the retailers were once again in vogue, shorter term. Richemont has been surprisingly volatile: outperforming in August and reversing strongly in September.



Top40	%ch Qtr	Rank	Top40	%ch Year	Rank
AngloGold	19%	1	SAB Miller	15%	1
GoldFields	26%	2	GoldFields	18%	2
SABMiller	6%	3	Sasol	7%	3
Billiton	-19%	42	Billiton	-5%	42
Anglos	-18%	41	Standard	-16%	41
Richemont	-18%	40	Anglos	-3%	40
Mid Caps	**%ch Qtr**	**Rank**	**Mid Caps**	**%ch Year**	**Rank**
Life Health	10%	1	Life Health	34%	1
Liberty Hldgs	11%	2	Barlows	29%	2
Spar	7%	3	Metorex	97%	3
Sappi	-31%	61	Sappi	-34%	61
Imperial	-13%	60	Murrays	-42%	60
Netcare	-13%	59	PPC	-27%	59
Small Caps	**%ch Qtr**	**Rank**	**Small Caps**	**%ch Year**	**Rank**
EOH	22%	1	EOH	64%	1
Durban Deep	28%	2	Super Gp	42%	2
Cashbuild	9%	3	Pinnacle	79%	3
Group 5	-14%	63	Group 5	-29%	63
Dawn	-27%	62	Raubex	-42%	62
Afgri	-12%	61	City Lodge	-21%	61

Construction avoided (except Cashbuild).

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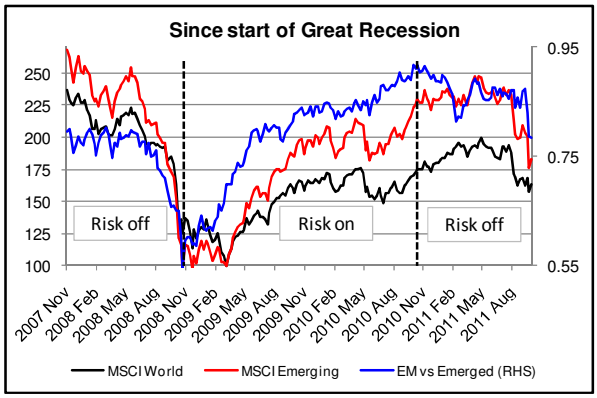
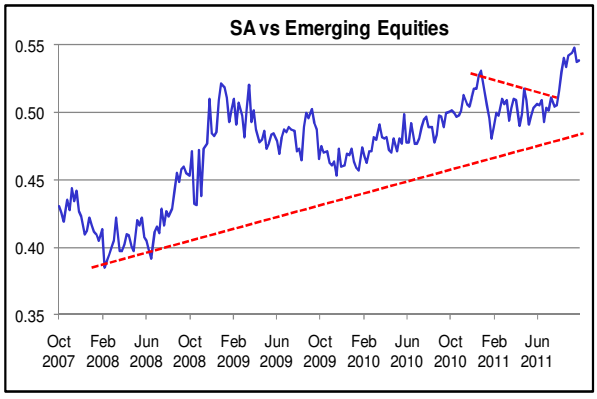
SOME OTHER THOUGHTS

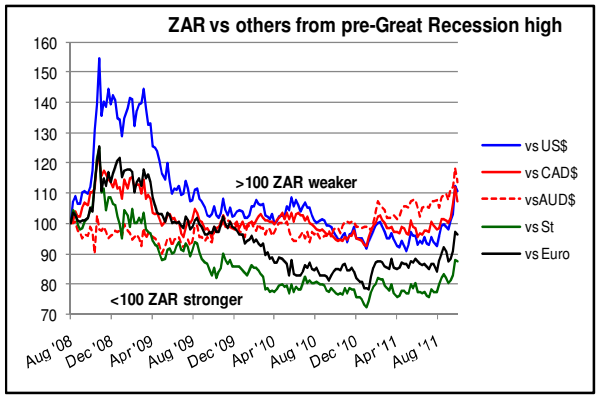


- Investors are bombarded on a daily basis with huge volumes of data, research and opinion, which often dulls the ability to make informed decisions and to take longer term views. Thus one day is termed as "risk on" while the next as "risk off" depending on whether shares are rising or falling. We believe that this definition of risk is too broad and that a better way of determining when risk is either on or off is when Emerging Markets ("EM") outperform Developed Markets ("DM"). Whilst many argue the case that growth prospects of EM are better than those for DM, the reality is that EM still trades at discounts to DM and have higher betas (i.e., EM outperform when risk is on and underperform when risk is off). The graph above illustrates this point quite clearly. The black and red lines plot the performances of the DM and EM share indices, indexed to the DM low in March 2009. The blue line plots the relative performance of EM against DM. The risk off phase is generally characterised by a flight to the US$ and gold bullion, the outperformance of government and corporate bonds and a selloff in equities. From a share market perspective, the lead is given by the EM. Thus October 2007 indicated the turn in risk appetite, with EM (led by China) falling hard until the end of 2008. DM only bottomed out in March 2009, but we would argue that risk appetite had turned more positive given that the high beta EM had stabilised and had started to outperform DM on the upside once again. EM did relatively better for almost 2 years to the day. Despite the fact that equities continued their upward march until April 2011, we would argue that a turn in risk appetite was already indicated in November 2010 when DM started to outperform, driven by the perception that QEII would have a more enduringly positive effect on the US share market on the one hand and the tighter monetary response to the surge in inflation in EM, on the other. By deduction therefore, the next risk on phase will occur when EM once again starts to outperform and that will only happen once the US$ loses its safe haven status;



- In my time in the investment markets, it has been a rare occurrence when SA is afforded an overweight status by international fund managers. Those who have had a perennial underweight allocation to SA within their EM portfolios will therefore have lost out on a 45% relative outperformance by our market over the past 3 years (chart alongside: MSCI SA vs MSCI EM, US$-terms). About half of this would have been the result of a resilient Rand which strengthened from about R8/$ to R6.50/$, and the other half would have been owing to share price appreciation. SA has traditionally been viewed as a low-Beta market and this is borne out by the fact that it has continued to outperform in a highly volatile investment environment.

- The Rand – the progression of which since August 2008 is plotted alongside - has surprised most analysts and will continue to do so for many years to come. Many have argued at various times in the cycle that the Rand is either under- or overvalued against the currencies of our trading partners. What has confounded has been the ability of the Rand to remain either too strong or too weak for extended periods of time relative to traditional measures such as purchasing power parity. In 2010, the rand was one of the world's strongest performing currencies, gaining 12% against its trading partners, 11% against the US dollar and 20% against the euro. Sizeable portfolio inflows driven by the hunt for yield powered the Rand. Some fade in the strength of our exchange rate occurred during 2011, accelerating in August and September. From the end of August through to its worse midday close on the 23rd of September, the rand lost 12% on a trade-weighted basis, 15% against the dollar and 10% against the euro. Whilst there has been some clawback since, weakness has been driven by a further collapse of risk appetite due to concerns about sovereign debt sustainability in advanced economies – mainly the euro zone and the USA, as well as worries about a sharply weakening property development market in China.



The weaker currency has provided some protection to local investors, with foreigners bearing the brunt of lower equity prices. Thus in local terms, the All Share Index fell by "only" 4% in September, whereas the currency impact raised the losses in US$- and Euro-terms to -14% and -11%, respectively. The Rand therefore acts as a shock-absorber during periods of market weakness. The flip-side is that imported prices will have an inflationary impact on local costs. Should the Rand approach the more appropriate purchasing power parity value of R9/$, the pain will intensify.

There is little doubt that there will be no respite in risk aversion until the right – and most likely, unpopular – decisions are made and implemented in addressing problems in the US and Europe. Until then, equity market volatility will remain high.
