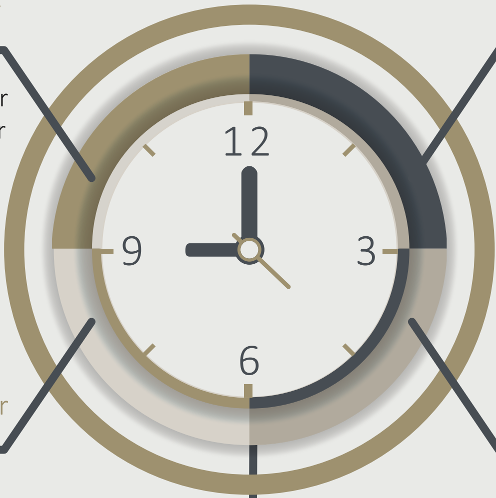
PSG Wealth

IMPACT OF POLITICAL MOVES ON INVESTMENTS

By now most are aware that President Jacob Zuma has replaced the well-respected Nhlanhla Nene with a new minister of Finance, the relatively unknown, Desmond van Rooyen.

Zuma made this cabinet shuffle only a few days after two ratings agencies downgraded the country's sovereign credit rating. Fitch changed its rating from BBB to BBB-, one level away from junk status and the lowest investment-grade rating. While Standard & Poor's retained the country's BBB-rating, but changed its outlook from stable to negative.

Impact on decision



Friday, 4 December

Ratings agencies, Fitch and Standard & Poor respectively cuts SA's sovereign credit rating and changed its outlook from stable to negative.

Tuesday, 8 December

12-noon: The rand weakens against the dollar after current account data showed that SA's current account deficit widened as expected to 4.1% of gross domestic product (GDP) in the third quarter from 3.1% in the second quarter.

Wednesday, 9 December

9am: R14.54 to the dollar
11am: Rand weakens after CPI data
5pm: R14.97 to the dollar
8pm: President Zuma fires finance minister Nhlanhla Nene. Rand weakens to low of R15.48 to the dollar after Zuma's announcement.

Thursday, 10 December

6am: R15.06 to the dollar
5pm: R14.47 to the dollar

Friday, 11 December

8:22am: R15.46 to the dollar
11am: R16.05 to the dollar

Sources: Reserve Bank, Treasury, JSE, Reuters

Market's reaction

Naturally markets have reacted badly to the news. Bond yields have shot up, listed banking and property shares have come under significant pressure, and the rand has weakened considerably.

The rand traded at some of its lowest levels this morning (R16.05 to a dollar) and added further fuel to the media-fire, with screaming headlines stating for example "With the treasury broken, will SARS and the reserve bank follow?"

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Impact on portfolios

Although we did not expect this week's political surprise, we have been aware of the depressed domestic economic environment for some time. For this reason our portfolios follow a diversified approach, especially offshore, to weather these domestic storms.

From an investment perspective we have long been emphasising the merits of offshore investment, especially so in relation to equity investment. The domestic economy has been under pressure for some time and we expected offshore firms to outperform in developing countries where economic recovery has been robust. The expectation was also for the rand to depreciate with an increasing inflation differential over time, further re-enforcing the investment merits of offshore investment.

In addition we have been light on government bonds, longer duration fixed interest investments and listed property. The general aversion was away from fixed interest instruments that are sensitive to the expected interest rate hikes.

Lastly, our portfolios remained fairly well diversified across various geografies, asset classes, sectors, and securities. We made a conscious effort to construct more diversified portfolios in anticipation of increased market turbulence.

Looking ahead

The most important thing that investors can do now, is not to panic. Investment decisions have been outsourced to appropriately skilled money managers that are best equipped to make the most appropriate investment decisions.

Despite the weak rand we retain our offshore equity weightings. The longer term investment case remains intact. We remain weary of selected areas within the local and offshore fixed interest markets and remain short duration with low interest rate risk.

With equity markets under pressure it is likely that there will be some indiscriminant selling. This often provide investors with some buying opportunities. That said, it is time to be thorough on research and selective on investment.