Weekly Investment Update

23 March 2016

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Market moves

Performance: 15/03/2016 to 21/03/2016	Return (Cumulative)
Local Markets	
All Share TR ZAR	2.60
Ind/Financials TR ZAR	5.03
Ind/Industrials TR ZAR	3.77
Financials&Indl 30 TR ZAR	3.07
Ind/Basic Materials TR ZAR	0.76
Gold Mining TR ZAR	1.15
SA Listed Property TR ZAR	2.11
Beassa ALBI TR ZAR	-0.70
Commodities	
Oil Price Brent Crude PR	2.40
LBMA Platinum AM PR USD	
Gold London AM Fixing PR USD	-3.51

The week ahead

Domestic

23 Inflation Rate

25 Good Friday

International

23 US: New home sales

25 Japan: Inflation Rate

Macro

ZA

SARB raised the repo rate by 25bps to 7%, its third straight hike, as policymakers voiced concerns about growing inflation pressure despite a worsening growth outlook. Inflation reached a 17-month high of 6.2% in January, above its target of 3-6%.

Germany

Producer prices in Germany dropped by 3% YoY in February, missing market consensus of a 2.6% drop. Prices declined for energy (-9.4%) and intermediate goods (-2.2%). In contrast, cost rose for non-durable goods (+0.2%), capital goods (+0.7%) and durable consumer goods (+1.4%).

Russia

The Bank of Russia left its benchmark one-week repo rate unchanged at 11% on 18 March, saying inflationary risks remain high due to developments in the oil market and budget uncertainties. Policymakers also said rates may stay high for longer than previously planned, aiming to bring inflation to target.

Markets

Best performer

For the week was Nampak who gained 21% after the release of their operational update. Following restructuring initiatives over the past two years, the group can now withstand its challenging trading environment. All sectors across the group delivered an improved performance supported by improved volumes.

Worst performer

For last week was Kumba Iron Ore and African Rainbow Minerals, each losing 15%. Both are exposed to the iron ore price which dove 2.25% last week according to the 62% Import Fine Ore index.

Sectors

The Non-Life sector representing short-term insurance group Santam gained 13.2% last week. Industrial Metal & Mining was the worst performing sector losing 15% in the same period.

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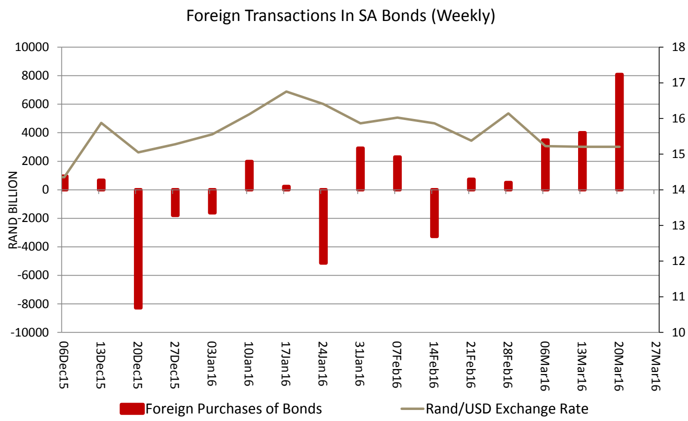
Macro note

Are rising interest rates really that bad for bond investors?

Rising interest rates and expectations for economic recovery are just a few activities which impact bond prices. As interest rates change, so do the values of all bonds in the marketplace. In general investors start running from bonds when interest rates start to rise. Just as bond prices go up when yields go down, the prices of bonds you own now will generally drop as yields and interest rates go up. However, not all bonds lose value (to the same extent) when interest rates rise. Generally speaking, the longer the bond's maturity, for example a bond that matures in ten years versus another that matures in two years, the more it's affected by changing interest rates. A ten-year bond will usually lose more of its value if rates go up than the two-year note. Also, the lower a bond's "coupon" rate, the more sensitive the bond's price is to changes in interest rates.

However, South Africa's higher interest rates are in fact creating opportunities for foreign investors. In most developed countries such as the U.S and Europe bonds offer yields of 1% or lower. Foreigners have again started buying local bonds since the middle of January. (See graph 1). In South Africa they could get a yield of about 9% a year, compared to below 1% yields in their own markets. Larger capital inflows, a stronger rand, rising bond prices and lower yields are just a few of the benefits awaiting the South African economy when foreigners continue to buy our bonds.



Source: I-Net Bridge

Bottom line

The exposure of portfolios to bonds in the current environment of rising interest rates should be fairly limited to money markets instruments and short-dated bonds. However, current inflation expectations are that inflation will peak early next year at just over 7% per annum. Bonds with slightly longer maturities of two- to three-years currently trade at yields of about 9% per annum (about 2% higher than the 7% per annum of money market instruments). These instruments are not so severely affected by further increases in yields, and to fix a yield of 9% for the next two years are becoming more attractive. It will become even more attractive with every increase in yields. One should not become so risk adverse and so focused on only money market instruments that one misses these golden opportunities at fairly low prices.

Market note

Investec confirms market expectations

Investec confirmed market expectations stating that adjusted operating profit is likely to be marginally ahead of the previous year in Pounds Sterling. A solid increase in neutral currency is, however, expected. Currency and equity market weakness and volatility over recent months have impacted Investec's overall results, particularly their Wealth & Investment and Asset Management businesses. Overall group results have been negatively impacted by the depreciation of the average ZAR/GBP exchange rate of approximately 17% over the period. Investec is expected to release their results for the year ending 31 March 2016 on 19 May.

During their investor pre-close briefing on Friday (18 March) Investec management focused on developments within the group's core business areas of the financial year ending 31 March 2016. The second half of the group's financial year has seen increased macro uncertainty in its key operating geographies. Net new fund inflows and reasonable levels of activity in its banking businesses have, however, supported a sound operational performance.

- Against this backdrop, the UK Specialist Banking business is expected to report results substantially ahead of the prior year, whilst the South African Specialist Banking business is expected to report results comfortably ahead of the prior year in rands.
- Wealth & Investment is expected to report results marginally ahead of the prior year, whilst Asset Management is expected to report results behind the prior year. Both divisions have continued to experience net inflows of GBP1.2 billion and GBP3.2 billion, respectively.

Management remains confident in the group's positioning supported by their strong client franchise, digital strategy and stable recurring income base, which should sustain earnings through varying market conditions.

Some financial features include:

- Recurring income as a percentage of total operating income is expected to be approximately 71% (2015: 74%)
- Third party assets under management decreased 6% to GBP116.2 billion – flat on a neutral currency basis
- Customer accounts (deposits) increased 2% to GBP23.0 billion – an increase of 14% on a neutral currency basis
- Core loans and advances increased 4% to GBP17.9 billion – an increase of 17% on a neutral currency basis
- Cash balances remain strong. Currently the group holds GBP11.3 billion in cash and near cash balances (GBP6.2 billion (R135.4 billion) in Investec Limited and GBP5.1 billion in Investec plc which amounts to 40% of its liability base
- The total income statement impairment charge is expected to be approximately 20% lower than the prior year
- Growth has been driven largely from mortgage loans to private clients and lending to high net worth clients, senior secured corporate loans and fund finance. The corporate book is well diversified across sectors. UK & Other total loan book grew GBP898 million to GBP8.0 billion at 29 February 2016. The Southern Africa total loan book grew from ZAR37 billion to ZAR219 billion at 29 February 2016.

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Previous publications

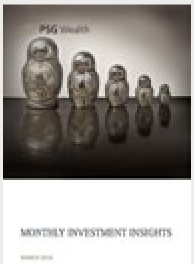
Daily

Published on a daily basis

Weekly

16 March
9 March
1 March
23 Feb
11 Dec
20 Nov
16 Nov

Monthly



March 2016
Feb 2016
Dec 2015
Nov 2015
Oct 2015
Sept 2015
Aug 2015
July 2015
June 2015
May 2015

Quarterly

Summer 2015
Spring 2015

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