



THE ENIGMA OF THE JSE BULL

Brenthurst Wealth Team

Despite business confidence recording very low scores the Johannesburg Stock Exchange (JSE) is powering on to reach new heights, hovering close to 36 500 points. While a bull market is not totally out of kilter with the rest of the world, compared to what is happening on the ground locally, the performance is somewhat baffling.

The eyes of the world were trained on South Africa during the Marikana platinum mine strike and subsequent shootings, with international media on the site reporting the tragic events to the world.

The day after 34 miners died in the shootings, adding to the list of ten already dead, the All Share index of the JSE took a slight dip on the gloomy realities casting a shadow over the country.

Just more than a week later, however, the JSE reached new record highs - despite the deadly strikes at the platinum mine. Also despite forecasts of a further deepening of the global economic crisis originating in Europe. Locally, despite business confidence, as measured by the South African Chamber of Commerce and Industry (SACCI), reaching its lowest levels in more than a decade.

On the last Monday of August the JSE All Share Index rose to 35 897.69 points. At the time the All Share Index and the Top 40 Index have gained 12% since the start of the year and was a far cry from the levels of around 25 000 points it was at in 2009.

RECORDS AMIDST THE GLOOM

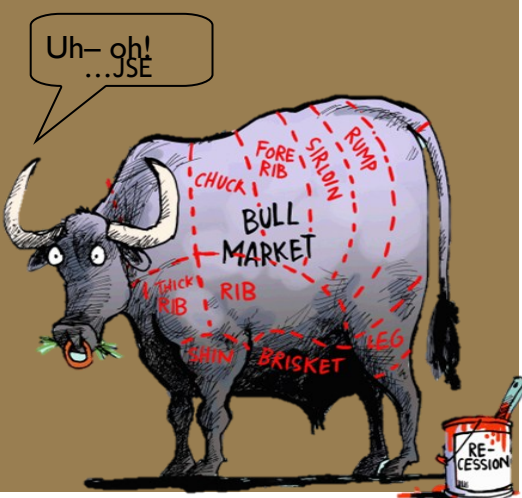
The growth has been surprising, with analysts being quoted in the media as calling it "odd"

The global economy is not healthy and back home here in South Africa economic growth forecasts have been adjusted lower a couple of times, now standing at only 2.6% growth expected for the year.

On the local exchange, however, it has been an especially good year for retailers with some stocks up 40% since January.

While the equities on the JSE continue to reach perplexing new heights, business confidence in the country is at lows last seen more than a decade ago.

When SA Chambers of Commerce and Industry (SACCI) released its Business Confidence Index (BCI) for July, it was at its lowest level in 12 years.



In this issue

JSE IS POWERING TO REACH NEW HEIGHTS

RECORDS AMIDST THE GLOOM

THE BCI - WHAT DOES IT MEASURE?

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When it released the index, then at only 90.9 points, the chamber said that it noticed with concern the slowdown of economic growth on a global scale and the widespread downward revision of expected growth rates for South Africa.

"This is especially concerning when the effect that this will have on trade and the current account of the balance of payments is considered," it said.

This means that business confidence is now again at levels last witnessed when the Growth, Employment and Redistribution Plan (GEAR) was still in place. Many plans have followed since, but still the country is grappling with high unemployment where a quarter of the population who is able to and wants to work, can't find employment.

How is it possible that in the mid of all of this, the JSE is breaking records almost on a weekly basis?

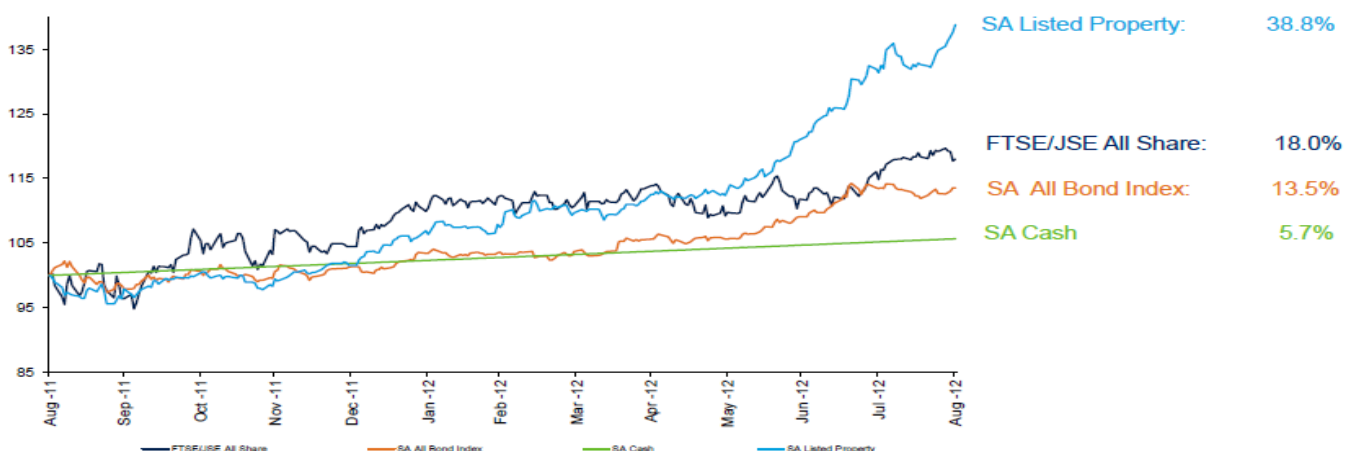
THE BCI - WHAT DOES IT MEASURE?

The BCI is generated monthly by SACCI to measure the level of business confidence within the South African economy. It is important to note that it is a market-related index that reflects not what business is saying, but what it is doing and experiencing. It is therefore not an opinion/perception-based index. It is likely that in any one month the business mood will be influenced both positively and negatively by various developments in the economy. The BCI seeks to reflect the net results of these influences, SACCI states.

The BCI is a composite weighted index of thirteen sub-indices. Various economic indicators are used to compile the thirteen sub-indices. The indicators that are monitored have been judged by business to have the greatest bearing on the business mood. These are:

- AVERAGE MONTHLY WEIGHTED EXCHANGE RATE OF THE RAND AGAINST THE US DOLLAR, THE EURO AND THE BRITISH POUND AS WELL AS THE VOLATILITY OF THE RAND EXCHANGE RATE
- CORE CONSUMER INFLATION RATE FOR METROPOLITAN AND URBAN AREAS
- THE REAL PREDOMINANT PRIME OVERDRAFT RATE
- RETAIL SALES VOLUMES
- RATE OF CHANGE IN REAL CREDIT EXTENSION TO THE PRIVATE SECTOR
- AVERAGE WEIGHTED US DOLLAR PRICE OF GOLD AND PLATINUM
- MERCHANDISE IMPORT VOLUMES
- MERCHANDISE EXPORT VOLUMES
- NEW VEHICLE SALES
- LIQUIDATIONS OF COMPANIES AND CLOSED CORPORATIONS
- VOLUME OF MANUFACTURING PRODUCTION
- REAL VALUE OF PRIVATE SECTOR BUILDING PLANS PASSED, AND
- ALL-SHARE PRICE INDEX OF THE JSE SECURITIES EXCHANGE

SA ASSET CLASSES' RETURNS (12 MONTHS TO END AUG 2012)



	2009	2010	2011	Q1 2012	Q2 2012	July 2012	Aug 2012	YTD
ALSI	32.13%	18.98%	2.6%	6.00%	0.98%	2.71%	2.74%	12.95%
ALBI	-0.99%	14.96%	8.8%	2.36%	5.20%	3.98%	0.07%	12.05%
SA Cash	9.13%	6.93%	5.7%	1.38%	1.39%	0.48%	0.46%	3.75%
Listed Property	14.07%	29.62%	8.9%	8.03%	10.31%	8.60%	5.65%	36.71%

Source: I-Net Bridge

THE DISCREPANCY

A while ago at the Investec Global Insights Forum a panel discussion gave some insights into what might be causing the discrepancy between the highs of the JSE and the lows of the BCI, and it seems it all comes down to the relevance and importance of the foreign investor on the JSE.

According to John Biccard, portfolio manager at Investec Asset Management who looks after the Investec Value Fund, the reason for the discrepancy is because the marginal buyer in the South African equities market is a foreign investor. “They are the ones that drive share prices,” he explained. Foreigners are very active on the local exchange with about 40% of our equities in their hands and about 50% of all bonds, Biccard says.

He argues that these foreigners’ faith in perpetual growth on the exchange comes from the belief that the South African consumer has undergone a structural change, but Biccard does not share this belief. He says that South African consumers have added debt to boost their expenditure and the rest of the growth is driven by a bull market in commodities.

“We would have a structural change only if we created 1 million new jobs per year,” he said.

He agrees that there is clearly a split between what’s happening on the ground and the performance of the JSE, adding that the realities of what is going on in companies simply just does not support some of them having a Price-Equity (PE) ratio of 25 and even higher. Another factor could be, he says, that foreign investors are simply so “revolted” by their own situation back home, with dismal economic forecasts, that they see South Africa as a quite promising destination for investment.

Other commentators have stated that foreigners have had a major role in the sharp increase in especially defensive and industrial equities on the exchange. They also seem to really like retail equities with these stocks having moved far past their historical valuation levels in the last year and is now in line and even more expensive than their international and other emerging market peers.

Underpinning this trend is the belief that there is reason for foreigners’ optimism about South African listed equities - solid companies with strong balance sheets, healthy profit growth and good prospects of growth in a growing upcoming market. The Africa factor also does not hurt.

But why does the BCI not reflect this? It is not opinion-based, or so it boasts. Then this solid performance by companies should come through strongly in the study, shouldn’t it?

During the same panel discussion at Investec, Clyde Rossouw, also a portfolio manager at Investec Asset Management, indicated that it is also important to note that a few of the big companies on the JSE make very little of its money in South Africa - like Naspers who have significant interests in the East.

Biccard especially is currently supporting the view that you should rather take your money offshore. He says 11 years ago the average PE ratio on the JSE was at 7, while globally it was at 25. Now it has evened out around 13, with certain high-flying JSE stocks already at 17 and some even as high as 25, while stocks in Germany for example are at 13.

It could all change in a second, but will it?

Given the liquidity of being invested in shares it could mean that if foreigners decide at the drop of a hat to withdraw, that the JSE could take a serious knock.

Biccard warned that the risk lies in the possibility for commodity prices to fall another 10%. This will immediately widen the country’s trade deficit and with investors stepping away there will be no foreign investment to fund the deficit on the current account. The rand could weaken, imports will become expensive, pushing inflation up and causing the next movement in interest rates to be upwards.

This will put enormous strain on South Africans, who Biccard argues, is financing their consumption through debt.

WHERE WILL IT END?

You could however argue, that if something like Marikana has not chased away the foreign investors, it remains to be seen what would.

The JSE could remain strong towards the end of the year, or it could become clear that South Africa’s exchange is not the only safe haven or destination for those investors who seek higher yield.

It would perhaps be prudent to start looking at the pricing of equities and considering diversifying offshore where price-earning ratios are not as high as some of the darlings on the JSE.

UPCOMING INVESTMENT SEMINARS - "POLITICS OF PARALYSIS"



STEVE WATSON - Client Director 10 yrs with the firm, 15 yrs experience. Steve works with both retail and institutional clients and intermediaries, doing a great deal of public speaking. Prior to joining the company in 2001, Steve worked at Corona Fund Managers for 5 years, where he developed his interest in macro-economics. Steve holds a Bachelor of Arts degree, a Higher Diploma in Education and a Master of Business Administration (Wales) degree, where his thesis focused on the impact of legislative change on the retirement fund industry in South Africa, following the Myners Report in the United Kingdom.



LOUIS NIEMAND - Product Specialist, 7 yrs with the firm, 12 yrs experience. As a member of the investment team, Louis' primary role is to provide investment-related support to Investec Asset Management's clients, both institutional and retail distribution channels. Acting as a 'proxy' for portfolio managers, Louis is responsible for communicating the investment philosophy, process, and performance of Investec Asset Management's different SA Equity Strategies. Before joining the firm in May 2005, Louis worked at Investment Solutions from early 2003 where his responsibilities included market and economic research, portfolio management on the tactical asset allocation products and client communications. In March 2000, Louis joined Sage Life as an investment marketer, and served as a member of their asset allocation team. Louis graduated from the University of South Africa with a Bachelor of Arts (Honours) (Cum Laude) degree in Economics and a Bachelor of Arts (Honours) degree in International Politics. Louis is a CFA charter holder.

TOPICS OF DISCUSSION

"POLITICS OF PARALYSIS"

HOW POLITICS HAS TAKEN US DOWN OUR CURRENT ECONOMIC PATH AND HOW IT WILL HAVE TO LEAD US OUT OF THE WOODS.

HOW TO AVOID INVESTMENT SCAMS

JOHANNESBURG SEMINAR:

STEVE WATSON & MAGNUS HEYSTEK

DATE: WEDNESDAY, 26 SEPTEMBER 16:00 - 17:45

VENUE: 100 GRAYSTON DRIVE, SANDTON, **INVESTEC HEAD OFFICE**

RSVP: +27 11 799 8100 reception@brenthurstwealth.co.za

PRETORIA SEMINAR:

LOUIS NIEMAND & MAGNUS HEYSTEK

DATE: WEDNESDAY, 03 OCTOBER 16:00 - 17:45

VENUE: WATERKLOOF GOLF CLUB, JOHANN RISSIK DRIVE, **WATERKLOOF**

RSVP: +27 12 460 0340 yolandi@brenthurstwealth.co.za

CAPE TOWN SEMINAR:

STEVE WATSON & MAGNUS HEYSTEK

DATE: WEDNESDAY, 10 OCTOBER 16:00 - 17:45

VENUE: 36 HANS STRIJDOM AVE, FORESHORE, **INVESTEC OFFICE**

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