BRENTHURST WEALTH MANAGEMENT

INVESTMENT REPORT

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BEWARE THE WILTING EASTERN DRAGON

In this issue

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Global Markets AND SA ECONOMY

Not long ago it was normal for China to record annual economic growth rates of 10% and more. In 2007, just before the global economic crisis, China's growth in gross domestic product (GDP) was an astounding 11.4%. To show the contrast existing at that time, consider that other side of the globe in the United States a 2% growth rate was something to be celebrated.

Even through the economic crisis in 2008 and 2009, when the United States recorded negative growth rates for most of the quarters during those two years, China's economy was still full steam ahead at growth rates of 9.6% and 8.7%.

It seemed that nothing could stop the Eastern Giant. It took its place as the world's second largest economy after the United States and cemented its position as the world's fastest growing major economy, with growth rates averaging 10% over the past 30 years.

It is also a fact that most economies of the world are now inextricably linked and exposed to developments in the Chinese economy.

The country is now the world's largest exporter and second largest importer of goods. Odds are that your country is importing something from, or exporting something to China.

South Africa is no exception to this rule. As an economy that is still, to a large extent, rooted in commodities, South Africa is even more exposed to economic events and movements affecting the Chinese economy.

China is already South Africa's biggest single-nation export market, while South Africa is, for the moment, China's biggest trade partner.

If then suddenly the international media is debating a "hard" or "soft" landing for China, South Africans should pay attention.

Whether the latest economic woes causes China's growth rate to drop down to 9% or even have it decelerating further to about 7%, a slowdown in China will have an impact on South African economic growth and by extension on the investment portfolios and performances of locally invested South Africans.

Although the link to China is strong, contagion effects of a slowdown in other economies should also not be ignored by South African investors.

Since the recession hit the globe in 2009, the core trio of the BRICS countries – China, India and Brazil – have fuelled the world economy. Although still expecting growth rates that European countries, for example, would drool over, these economies are all slowing down.

A forecast of about 8% for China is still high by Western standards, but it is far below the 10.4% and 9.2% achieved in 2010 and 2011.

In the latest quarter ending March, India's growth slowed to an annual rate of only 5.3%, indicating a much sharper deceleration in this economy. The credit ratings agency Standard and Poor's recently warned that India's sovereign rating could be affected negatively.

Brazil's economy showed almost no growth in the first quarter of this year, with an annual rate of only 0.2% clocked by the South American powerhouse.

So how will a slowdown in China, to a greater extent, and India, to a lesser extent, hit the South African economy?

THE COMMODITIES LINK

On a recent trip to South Africa, China-based Standard Bank economist Jeremy Stevens, was quoted in the press as saying that an economic deceleration in China may have profound negative effects on the commodities driven economies of Africa.

He said that African economies should be concerned as they are now even more sensitive to developments in China than before.

"A deceleration in the Chinese economy would spell trouble for African economies. This would mean weaker commodity prices, and African economies have largely been dependant on strong Chinese demand for its resources," CAJ News quoted Stevens.

On the Standard Bank blog the Standard Bank team highlighted some of the other comments from Stevens.

He stated that with South Africa being the most externalised economy on the continent and because of its close trade ties with China, it could be hurt the most if the "hard landing" (a growth rate of below 7%) scenario occurs.

Stevens said export volumes will fall, which would affect the trade balance and our ability to finance the current account deficit. The rand can be expected to depreciate; investor sentiment would become negative, and equities markets would feel the pinch, the blog team states.

He suggested that African economies need to diversify more and stop being overly reliant on commodity exports to mitigate these risks.

In the last couple of decades South Africa has diversified its economy substantially with the major contributing sector moving gradually away from the primary (mining, agriculture, fishing and forestry) to the tertiary services sector. Still, the economy is at risk if one of the largest commodity consumers starts facing economic difficulties.

INDIA AND ITS IMPORTANCE FOR SOUTH AFRICA

During a recent visit by Indian president Pratibha Patil to South Africa, both nations once again pledged their support to increase bilateral trade.

Patil was accompanied by a government minister, four parliamentarians, various officials and a very large business delegation as Indian business also eyes Africa as a growth opportunity.

South Africa and India see themselves as strategic partners, cooperating in various forums such as the BRICS grouping, IBSA (India, Brazil, South Africa) and the BASIC (Brazil, South Africa, India, China) climate change-specific forum.

Trade between the two countries already stood at R48.2bn in November 2011 for the year, with South African exports at R21.9bn and imports from India at R26.3bn.
To show the perceived importance of bilateral trade between the two nations a trade target of R111bn is set to be reached by 2014.

WHAT DOES A SLOWDOWN MEAN LOCALLY?

A slowing economy in China, as well as in India, will impact on export volumes – especially commodity exports bound for China.

This will have numerous consequences. Firstly companies relying on these exports will face pressure on their earnings, recording lower profit growth figures and impacting on the share prices of listed companies and dividends payable to shareholders.

Secondly, lower exports mean a weaker trade balance, with South Africa likely to struggle to finance the current account deficit.
The rand could depreciate, which over the medium term could to some extent balance out the negative effect of lower commodity exports – as a weaker rand means cheaper exports.

On balance though, in such a situation the equities market is likely to feel the pinch, as the Standard Bank team states on the blog.

Again the prudence of a long term strategy for investment needs cannot be over-emphasised. Especially when retirement planning is the focus, rash decisions based on short-term fluctuations should be avoided at all costs.

With understanding comes peace of mind. If you understand the characteristics of the asset classes you are invested in and how they are likely to react in specific market conditions, you will feel better equipped to make informed decisions in downward cycles.

HARD OR SOFT?

It remains to be seen how the Eurozone troubles will affect the growth rate in both China and India, as well as other emerging markets.

Analysts are split between those who foresee a gloomier picture of slower growth, and those who are still optimistic that it will only be a slight dip before recovering.

Meanwhile the reality in South Africa is that economic growth forecasts have already been adjusted downwards to only 2.7% and the rand has fallen from its strong position of around R7 to the dollar to R8.40.

The impact can of the slowdown has thus already filtered through to the South African economy, but the performance of the JSE All Share index still astounds with levels of around 33 500, significantly up from the below 29 000 levels of mid 2011.

The fact remains that South Africa will not escape unscathed, but the prospects of growth in sub-Saharan Africa are still a lot healthier than in the Western economies.

CPT INVESTMENT SEMINAR 11 JULY: RIDING OUT THE STORM!

FOR MOST OF LAST YEAR BRENTHURST WEALTH ADVISED A MUCH LARGER EXPOSURE TO OFF-SHORE MARKETS, PARTICULARLY EQUITIES IN DEVELOPED COUNTRIES.

SINCE THE MIDDLE OF 2011 THE RAND HAS DROPPED BY MORE THAN 20% AGAINST MOST MAJOR CURRENCIES WHILE CERTAIN ASSET CLASSES IN DEVELOPED COUNTRIES, NOTABLY TECHNOLOGY AND BIOTECHNOLOGY, HAVE RECORDED HANDSOME RETURNS, IN SOME CASES IN EXCESS OF 30% YEAR- ON- YEAR. WE FEEL VERY VINDICATED BY THIS RECOMMENDATION.

AT OUR UPCOMING SERIES OF SEMINARS WE WILL BE UPDATING OUR CLIENTS ON THE OUTLOOK FOR LOCAL INVESTMENT MARKETS AND WHETHER LOCAL INVESTORS NEED TO CONTINUE EXTERNALIZING THEIR INVESTMENT PORTFOLIOS.

CAPE TOWN: INVESTMENT SEMINAR, WEDNESDAY 11 JULY

PAUL HANSEN: Director: Retail Investment Marketing - Investments
B.Com (Wits), MBA (UCT), US Stockbrokers license.

Paul Hansen has been in the asset management/investment business for 32 years, including 9 years in the United States and 16.5 years with STANLIB.

Experience includes research (as an analyst), as well as institutional (pension funds, insurance funds) and retail portfolio management (private individuals and unit trusts).

Has won 11 Raging Bull awards for unit trusts under my management.

Currently managing 5 STANLIB risk-profiled local fund of funds (Aggressive to Conservative), as well as STANLIB International Fund of Funds (Aggressive, Balanced, Conservative) Regular participant on radio (SAFM every weekday morning and TV.

UPCOMING CPT SEMINAR: 11 JULY 2012 BOOK NOW

KEY PRESENTERS INCLUDE:

- **PAUL HANSEN: STANLIB**
  RETAIL INVESTMENT MARKETING, INVESTMENTS
- **MAGNUS HEYSTEK: BRENTHURST WEALTH**
  DIRECTOR & INVESTMENT STRATEGIST

CAPE TOWN SEMINAR:	11 JULY 2012	
DATE:	WEDNESDAY, **11 JULY**	**16:00 - 17:45**
VENUE:	LIBERTY LIFE, THE ESTUARY,CENTURY BOULEVARD, CENTURY CITY	
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