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*Wishing all our clients a safe and prosperous 2016*

Brief Overview

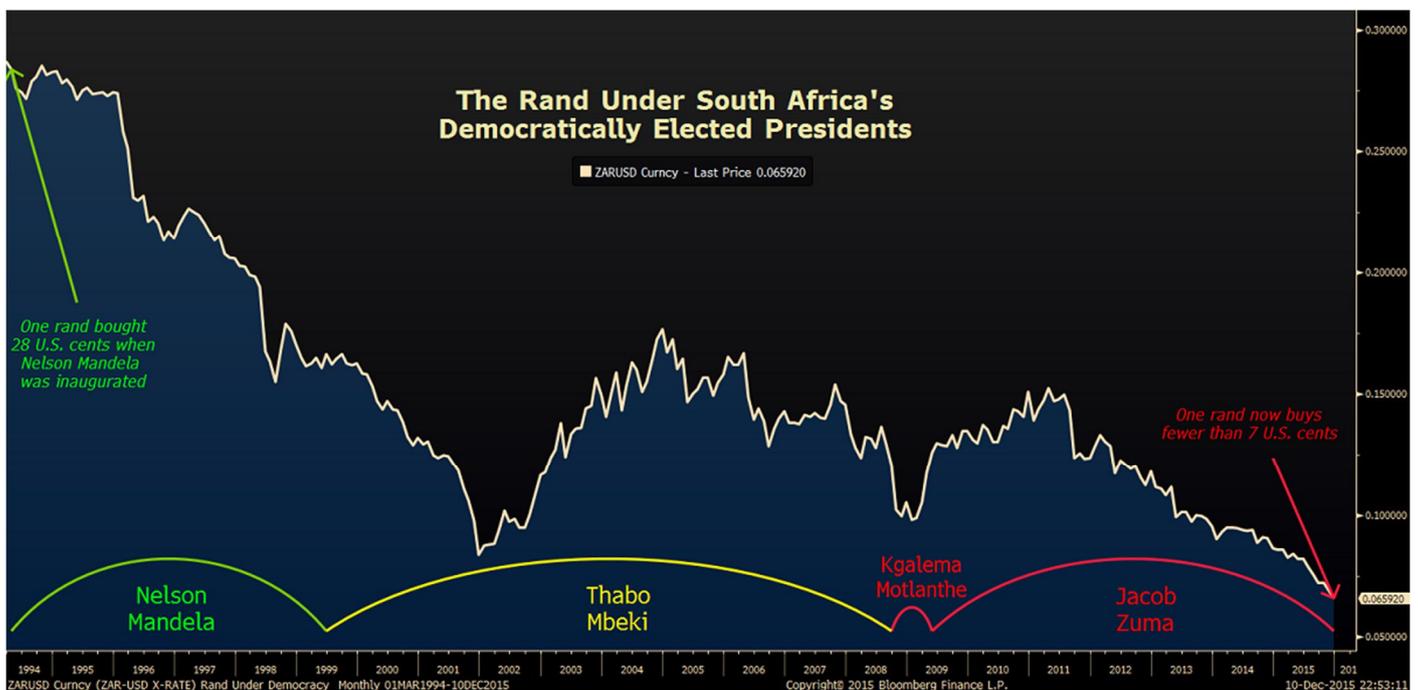
- **Global Markets:** This past year the average Global Equity fund lost USD**3.5%** and the average American Bond fund lost USD**0.9%**. It was an extremely difficult year for global investors, and the first week of trading in 2016 proved no different – the Dow Jones Industrial Index realised its worst opening week since it was formed in 1896.
- **JSE/FTSE:** The JSE/FTSE All Share index rose 5.13% for the year.
- **South African Rand:** The Rand lost **25.66%** against the US dollar in 2015, capitulating in the last quarter after China devalued its currency and President Zuma fired Nhlanhla Nene.
- **Credit Ratings:** South Africa was downgraded by all the major rating agencies and is now one notch above junk status – profound repercussions await should it be downgraded further.
- **Anglo American:** The bellwether South African mining share, Anglo American, was slammed this past year – down approximately **70%**.
- **MTN:** The Nigerian authorities fined MTN USD3.9 billion. The share fell **40%** in 2015.
- **Dow Jones Industrial Average and S&P500 of America:** Both of these indices were slightly negative for the year.
- **Federal Reserve of America:** The Federal Reserve eventually raised interest rates by 0.25% in December, and indicated their intention for 4 more hikes in 2016, exerting even more pressure on Emerging Market currencies.
- **Allan Gray:** We had an excellent year for our local clients. Our simple theme over the past 5 years was to be cautious on South Africa and have as much money offshore as legislation and clients' risk profiles allowed. Fortunately, it worked pretty well this past 12 months!
- **Coronation Portfolio Managers:** Our cautious option had a very good year and the aggressive Global Emerging Markets strategy kept its head above water in volatile markets.

- **Franklin Templeton:** We had another difficult year as we still patiently wait for an opportunity to invest our clients US Dollars into our preferred markets. In light of the carnage in Emerging Markets and global oil shares, we are extremely excited about the opportunities that are appearing.



## South African Rand

Let us kick off with the Rand!



Courtesy Bloomberg

Every individual client portfolio we manage – other than the few clients in Money Market – has as much offshore exposure as possible and thus has benefitted from the falling Rand. The amount of offshore exposure differs for each client – it depends on existing legislation, the client's product, investment objectives, risk profiles and monthly income needs if any.

Having plunged **25%** against the US Dollar, the Rand is one of many Emerging Market currencies that has fallen dramatically throughout the year (see chart below), but it is admittedly one of the worst performers. Furthermore, the global currency fallout has not been confined to Emerging Market currencies: The Aussie dollar is down **10%** against the US dollar, and the Canadian dollar – known as the “loonie” – is down approximately **20%** against the USD, amidst a rout in energy prices that sent crude oil down about **40%** in 2015.



Courtesy INET BFA

Unfortunately, President Zuma exacerbated the fall in the Rand in December by replacing Nhlanhla Nene with David Douglas Des Van Rooyen, and then again with Pravin Gordhan.

We are a little concerned that betting against the Rand has become one way traffic. There were no experts when the Rand was trading at R8.00/USD, but now it has become a “slam-dunk” to assume the Rand and other Emerging Market currencies will fall indefinitely. Whilst that may well be the case, it is worth reminding clients that on the two previous occasions the Rand sank to all-time lows, (see again Rand chart above) there was a huge rebound over a period of years.



When any asset class is falling or climbing persistently, as Emerging Market currencies are at the moment, all the evidence generates a compelling argument to “jump on board”. History however, is littered with investors making poor decisions at exactly the wrong time.

There are a couple of reasons why Emerging Markets and their currencies may rebound, and in our opinion the market is overlooking them at the moment. Here are a few that investors should be aware of:

- 1. If the Rand keeps falling, the South African authorities might hike interest rates sharply, thus making it more attractive for investors to hold Rands and earn higher interest than they can elsewhere. If that does happen, believe us, it will not be a pleasant experience (as those of you who were around in the Eighties and the Emerging Market crisis of 1998 will attest to).*
- 2. The ANC may run out of patience with President Zuma and recall him like they did to Thabo Mbeki - we assume this would be a Rand positive.*
- 3. The Federal Reserve in America may assert that it made a policy error by raising interest rates in December and/or the American economy could stumble - and if they indicate that there are no further rate hikes on the way or start another QE regime by printing money, the US Dollar could fall precipitously against all currencies.*

We do not believe the Federal Reserve in America will continuously hike interest rates in light of the market mayhem that has greeted the New Year, and we do not believe that the American economy and Global economies are strong enough to withstand higher interest rates indefinitely.

Despite our concerns about the Rand rebounding, we are not going to do anything rash and will continue with our existing theme: A very cautious stance on South Africa and as much exposure to offshore assets allowable. Please remember however, that ***changes of trend can occur at any time***, and we can assure you that no-one rings a bell to let you know.



## Global Investment Opportunities are being created in this crisis

*The safest and most potentially profitable thing is to buy something when no one likes it. Given time its popularity, and thus its price, can only go one way: **Up**. - Howard Marks*

If one can ignore the incredible market and currency volatility, there are some fantastic opportunities brewing in Global Equity markets at the moment – and we intend taking advantage of them! We have identified a new option in addition to a cheap asset class that keeps getting cheaper (and already offers a compelling investment opportunity in our opinion) – China.

But first, we will focus on the predominantly American opportunity.



## Natural Resources

The Oil price has plummeted since 2014 when the Saudis increased production to tackle the growing threat of American Shale producers using new technology and grabbing their market share. Oil shares have been absolutely crushed. Exxon Mobil, Occidental, Chevron, Royal Dutch Shell, BHP Billiton, Marathon, Schlumberger and Sasol all now trade at a **40-60%** discount to their highs in 2014 – a very attractive investment opportunity in our opinion.

If we had offered you a similar discount on the top oil producers in the world at their peak in 2014, no single investor would have turned us down. Over the past 18 months the price war in the oil universe has intensified and we are gradually being presented with the best buying opportunities of these companies in a generation.



Below is a chart of the Franklin Templeton Natural Resources Fund which allows our Franklin Templeton clients' access to these undervalued companies. Ideally we would like to buy when the prices fall to the low of the panic of 2008.



Courtesy INET BFA

Locally, it is our intention to target the excellent opportunities arising in the oil space when we begin offering bespoke share portfolios through *Investec Wealth and Investments* to our clients. Two South African companies, Sasol and BHP Billiton – are prime candidates.

Sasol



BHP Billiton



Courtesy INET BFA



China

Successful investing is not easy and great long term investments do come with a serious bout of initial discomfort – we took immense strain when we started taking money out the country at R6.00/USD and it stayed there for a couple of years, but with perseverance and patience that strategy eventually paid off.

Right now, the world's most unattractive investment one could consider would be China. On the contrary, most investors believe that the best place to have your money invested are American Technology companies.

It is astonishing that two American companies – Amazon and Google – are now valued more than **ALL** the 143 Chinese companies that comprise the China Enterprises Index. Bear in mind that these top 143 companies span all sectors of the world's second largest economy.

Amazon has also hardly ever declared a profit, and it trades at a P/E Ratio of over 900. The China Enterprises Index trades at an average PE ratio of 7.13 times earnings. Furthermore, Amazon has never declared a dividend – the China Enterprises Index generates an USD4.25% dividend every year for its investors.

We did not expect Chinese shares to get cheaper, but this has only strengthened our resolve to own this market, as the upside over the next couple of years is enormous.



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Lead. Don't Follow.



Courtesy INET BFA

When you buy or own shares that are so cheap and have already fallen so far – and the same applies to global oil companies or any permanent asset class for that matter – you reduce the chances of a major loss and you increase the chances of making a healthy profit: It is common sense! We call that a “margin of safety” in our industry and it is very sound investing practice. Asia, China and Oil are cheap, and they are not going to disappear anytime soon.

We thank you for your patience, your wonderful support and we wish you all the very best for 2016.

Kind Regards

Mike Carruthers