BRENTHURST WEALTH MANAGEMENT

INVESTMENT REPORT

ISSUE EIGHTY TWO
AUGUST 2009

THE TRIUMPH OF THE OPTIMISTS

By Magnus Heystek—Investment Strategist

Congratulations to all clients of Brenthurst Wealth.

If ever there was a time for our clients to panic and head for the hills, the six months or so from September 18 to 3 March 2009 was going to be it.

Everything that could possibly go wrong on global financial markets did; from the collapse of Lehman Bros. through to the global credit crunch, the tanking property market, swooning commodities, plunging oil, equities, bonds, spiking Libor-rates, soaring unemployment.......

It wasn't always comfortable and there were, no doubt, searing questions asked about our investment strategies.

With very few exceptions most of our clients stuck to their investment strategies. Our message to clients was straightforward: panic was not an option and a well-diversified investment portfolio was the best way to ride out the storm.

Several of our selected funds actually increased in value over this period of time, such as the Investec Value Fund, for example.

The turnaround in markets since the beginning of March has been spectacular, but not surprising. Market sentiment was extremely fragile and it was a time for buying not selling. Long may it last.

HOW MOST RETAIL INVESTORS MISSED OUT ON THE UPTURN

Should a surgeon operate on his own child? Should an investor invest his own money?

The emotional aspect of investing money, especially retirement capital, is an issue which was once again highlighted during the recent stock market volatility.

Warren Buffett has often in the past referred to the "stable emotional framework" which he considers as a prerequisite to being a successful investor.

The major difference, of course, is that Buffett has a life-long history of investing money in the billions of dollars, whereas most retail investors are often dealing with this issue for the first time in their lives and, by and large, are not prepared for it.

CAPE TOWN INVESTMENT SEMINAR: UPDATES ON MARKETS

DATE: THURS, 27TH AUG 2009
TIME: 15H30 FOR 16H00
VENUE: BOUNDARY TERRACES, BRIDGE HOUSE, 1 MARIENDAHL LANE, NEWLANDS, CT
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Also, for most retail investors, what they have invested is all that stands between them and penury.

Countless studies all over the world have proven consistently that retail investors are particularly bad at timing investment markets. In many instances, investors are their own worst enemies, not the volatile markets.

Retail investment figures for SA in the first quarter of this year prove this once again. In all a total of R17,8 billion was invested into SA's unit trusts with only R100 million flowing into equity funds. By far most of new money being invested was destined for money market and bond funds, missing out on the sharp upturn which started in April. Equity funds have recovered by between 25 and 40% since the bottom, while money market and bond investments have been left trailing badly.

The danger now is that investors will once again be late to the party, just as the band stops playing.

At the end of March 2009 SA's investors had more than 50% of their investments in collective investing in bonds and money market funds' R350 billion out of total of R677 billion.

Bonds and money market instruments have beaten equities over a 12-month period to end March, but lags badly over longer periods of time.

In the May-issue of the Brenthurst Wealth-newsletter we expressed the courageous view that equity markets had entered into a new bull market phase. This view was based on several facts not least the extremely low valuations after the sharp sell-off in February and March this year.

History also shows that reacting post event to sell-offs in markets is normally damaging to long-term investment returns.

A flight to the deemed safety of cash instruments not only incurs an opportunity cost when markets recover but also a capital gains tax in the case of discretionary investments.

Investments in retirement products such as living annuities, retirement annuities and preservation funds, fortunately do not pay capital gains taxes when switches are made.

Retail investors who panicked in the midst of the global turmoil not only have missed the upturn, but could also face a nasty CGT-bill when the time comes to submit tax returns. Ouch and ouch again!

The further surprise drop in interest rates earlier this month means an even lower return for investors with their savings in money market and other savings instruments. From rates above 12% a year ago investors are now getting no more than 7% or so. After tax the return is around 4%, hardly enticing and substantially less than the average rate of inflation at 7%. Long term this is not the way to go....

THE AFTERMATH OF SECULAR BEAR MARKETS

Is it a short-term rally within a greater bear market rally or is the start of a new bull market in investment markets? This question seems to have divided the investment community into two, distinct camps, each vigorously defending their position.

WHO DO YOU BELIEVE?

US investment banking group Morgan Stanley earlier this month produced a very interesting research report which analysed the profile of 19 major secular bear markets, across many sectors and many countries. These bear markets included the US in the 1930's, the US and Europe in the 1970's, gold in the 80's and Japan in the 1990's.

Each involved a peak-to-trough decline of at least 40% lasting at least a year. The median of these bear markets involved a decline of 57% over 30 months. The most recent bear market between June 2007 and March 2009 was very typical; will its aftermath also be?

The usual rebound rally is 71% over 17 months. The current one has been “only” 48% over five months. Structural bear markets are usually followed by a strong rebound, typically from the moment that the authorities take strong decisive action. Often the rebound rally peaks at or prior to a change in the interest rate cycle. Sometimes the peak in the rebound rally anticipated a rollover in the growth cycle or coincided with a period of local currency strength.
Essentially Morgan Stanley’s bottom line is that the current rebound rally may have some further to run, but is likely to stall before the first Fed rate hike, widely forecast for the third quarter of 2010, followed by a trading range lasting for about 5 years.

The conclusion is that active tactical asset allocation around all asset classes will be more important than ever for the next five years. The Morgan Stanley research shows that the average trading range in this next period was 52% wide, meaning that superior returns can be achieved by adopting flexible and adjustable investing strategies rather than dogmatic buy-and-hold ones.

LESSONS TO BE LEARNT FROM THE CREDIT CRUNCH

Have investors actually learnt any lessons from the credit crunch and the subsequent global recession?

US households have been on a borrowing binge since the days of Harry S Truman in the White House 57 years ago. Over that time debts have risen more than 3,5 times faster than their incomes. The savings ratio, i.e. the proportion of household income stashed away for a rainy day, plunged from 15% at the end of the 1980’s to zero by the middle of 2007.

At the time, who couldn’t blame them? When house prices are rising all the time why would you worry about other investments? After all, you live in your own personal ATM. When you needed money you just tapped your local bank for a further increase in your mortgage bond.

And why bother saving when the stock was doing the job very well for you? Between 1982 and 2007 the Dow Jones industrial average index shot up a staggering 14 times. You didn’t have to be Warren Buffett to make a decent return.

But those days are well and truly over. US household wealth (like most other parts in the western world) has evaporated over the last 18 months to 2 years, tumbling by almost $11 trillion to the end of March this year.

Despite its recent rally the stock market is still down by more than a third from its peak, while home prices keep falling.

So it’s no surprise that everything is now changing around. In short, debt is now bad and savings are good.

US personal debt was growing at double digit rate three years ago, but is now actually falling. It’s a process called deleveraging. In the first quarter of 2009 US household and company debt shrunk by 0,7%, the first time this has happened since 1952.

For a society whose prosperity is built on an ever-increasing spiral of debt, this is a very painful adjustment, with a lot of collateral damage.

Collateral damage? This is just an academic expression for bankruptcy, liquidations, job losses and declining asset values.

The other side of the coin is that the US savings rate has started recovering-right back to 6,9%. John Mauldin from Millennium Wave Advisors reckons it will climb to 9%. In the absence of rising incomes will this mean that consumption spending, which makes up 70% of the US economy, will decline by 9%.

Therefore any investment strategy that presupposes a return to normal consumption expenditure patterns is doomed to fail.

Focused on your long-term success.

HOW TO INVEST GOING FORWARD?

Here's some advice from one of the world's top investment managers, Dr. Mark Mobius head of the Templeton Emerging Markets-franchise, a position he has held for more than 20 years.

- Keep an eye on value.
- Don't follow the herd.
- Be patient.
- Drip-feed your money into the market.
- Examine your own situation and your appetite for risk.
- Diversify your portfolio.
- Don't listen to your friends or neighbours when it comes to investments.
- Don't believe everything you read in newspapers/in the media, things tend to be exaggerated.
- Go into emerging countries because that is where the growth is.
- Look at countries where populations are relatively young.

INVESTMENT SEMINAR: CAPE TOWN

MOMENTUM AND BRENTHURST WEALTH MANAGEMENT TAKE GREAT PLEASURE IN INVITING YOU TO OUR NEXT CAPE TOWN INVESTMENT SEMINAR, THURS 27TH AUG. TOP SPEAKERS WILL PRESENT "**UPDATES ON INVESTMENT MARKETS**"

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OUR GUEST SPEAKERS ARE:

- **WAYNE MC CURRIE:** SENIOR PORTFOLIO MANAGER **RAND MERCHANT BANK**
- **MAGNUS HEYSTEK :** INVESTMENT STRATEGIST **BRENTHURST WEALTH MANAGEMENT**
- **MICHELLE BURGER:** CERTIFIED FINANCIAL PLANNER **BRENTHURST WEALTH MANAGEMENT**

Booking is essential to reserve seating!

FOR MORE INFORMATION ON FINANCIAL MATTERS DO NOT HESITATE TO CONTACT ANY OF OUR HIGHLY QUALIFIED FINANCIAL PLANNERS.

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