GRINDROD ASSET MANAGEMENT

INVESTMENT REVIEW

NOVEMBER 2011

"It's so much easier to suggest solutions when you don't know too much about the problem."

Malcolm Forbes, publisher of Forbes Magazine

ECONOMIC OUTLOOK

The European sovereign debt crisis has intensified in the past month, prompting co-ordinated action by central banks to provide liquidity to ailing European banks in an attempt to stem the tide. The US Federal Reserve (Fed), together with the European Central Bank (ECB), the Bank of England and the central banks of Canada, Switzerland and Japan lowered the premium banks pay to borrow dollars by 0.5% and extended these dollar swap lines to February 2013. It is hoped that this action will "ease strains in financial markets and thereby mitigate the effects of such strains on the supply of credit to households and businesses and so help foster economic activity", according to a statement issued by the Fed.

At the same time, the People's Bank of China cut banks' reserve requirements by 0.5%, unlocking almost RMB400 billion in liquid capital. While these moves restored some confidence in financial markets, as evidenced by a strong rally in global equities, it still does not address the heart of the problem – high levels of government and household indebtedness. If anything, it encourages more borrowing and threatens to exacerbate the problem.

Index	November %	12m %	YTD %
Dow Jones	0.8	9.4	4.0
S&P 500	-0.5	5.6	-0.8
FTSE 100	-0.7	-0.4	-7.8
EuroStoxx50	-2.0	-9.0	-13.7
Nikkei 225	-6.2	-15.1	-17.5
Hang Seng	-9.4	-21.8	-21.9
Australia	-4.0	-10.5	-13.7

Source: I-Net Bridge

In South Africa, the Monetary Policy Committee (MPC) of the South African Reserve Bank (SARB) opted to leave official interest rates unchanged when they met for the last time in 2011. Although the decision was not unexpected, there were some market commentators calling for interest rates to be lowered as the situation in Europe deteriorated, thereby jeopardising South Africa's economic recovery. The MPC did acknowledge the European situation but highlighted the fact that the risks to the inflation outlook were now to the upside, after the Rand's significant depreciation against the US dollar (*chart 1*) and that consumer inflation would likely remain above 6% for longer than previously estimated.

The MPC's decision was vindicated as consumer inflation reached 6% in October. However, third quarter GDP growth (*chart 2*), at just 1.4%, was significantly lower than forecast and raised questions about the sustainability of the economic recovery in South Africa, particularly in light of lower economic activity in Europe (South Africa's largest trading partner by region).

MARKET OUTLOOK

Although most global equity markets finished the month in the red, the numbers would have been significantly worse were it not for a late rally in response to the coordinated efforts of central banks around the world to ease strains in financial markets. The S&P 500 index gained 7.6% in the final week of November, while the DJ EuroStoxx 50 index gained 10.4% over the same period (*chart 3*). Banking stocks in Europe lead the gains, with Société Générale advancing 20.1% and BNP Paribas adding 18.8%. Year to date, the Dow Jones Industrial Average is the only major stock index registering gains, while the Hang Seng Index is off more than 20% (*chart 4*). US equity markets have been supported by Fed stimulus measures throughout 2011 and now look relatively expensive.

Global bond markets succumbed to intense selling pressure as investors sought to offload bonds issued by a number of European countries. The yields on Italian government bonds maturing in ten years time rose above 7% for the first time since the introduction of the Euro. The Citigroup World Government Bond Index declined by 1.51% when measured in US dollars, although the non-Euro World Government Bond Index increased by 0.3%, highlighting the extent of the problems in European sovereign debt markets.

Index	November %	12m %	YTD %
All Share	1.6	11.7	5.1
Resources	2.1	6.6	-1.0
Financials	0.8	10.3	5.4
Industrials	1.5	17.1	11.1
Property	-0.9	9.1	6.7
Bond	0.0	9.9	8.0
Cash	0.5	5.8	5.2

Source: I-Net Bridge

South Africa's equity market posted a modest gain of 1.6% during November (*chart 5*). The Rand weakened by 2% against the US dollar, providing some support for Rand hedges. As a result, the Resources sector gained more than 2%, outperforming both Financials and Industrials. Consensus earnings forecasts are largely unchanged and continue to point to a 23% increase in earnings in 2012, followed by 13% growth in 2013. As a result, the one year forward price:earnings (P/E) ratio on the JSE All Share Index has remained unchanged at 10.1x, with the Resources sector on a forward P/E of 7.9x, Financials on a forward P/E of 9.0x and Industrials on a forward P/E of 13.6x. The one year forward dividend yield has declined slightly and has now dipped below 4%.

The South African bond and listed property markets underperformed equities in November as yields on longer dated government bonds edged up slightly (*chart 6*). The forward yield on South Africa's listed property sector increased to 8.2%, despite a number of small earnings downgrades after companies lowered their expectations for income growth next year.

"We wish all our clients a happy, successful and prosperous 2012"

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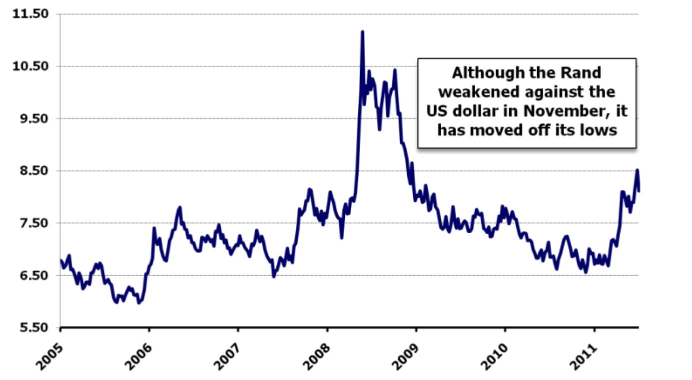
GRINDROD ASSET MANAGEMENT **INVESTMENT REVIEW**

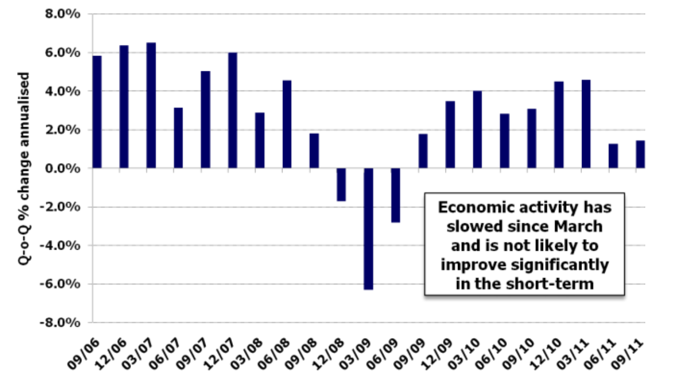
CHARTS

Chart 1: Rand/US$ Exchange Rate



Source: I-Net Bridge

Chart 2: South African GDP Growth

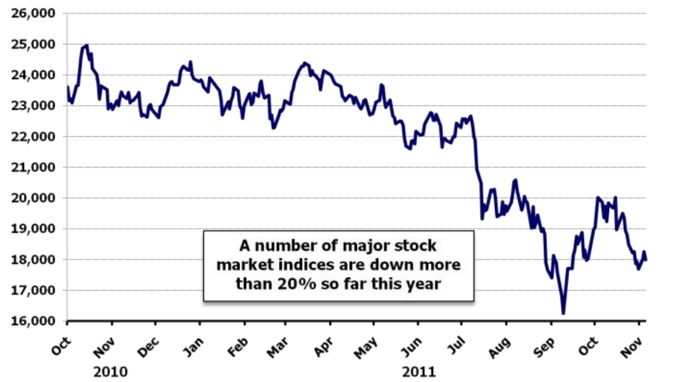


Source: I-Net Bridge

Chart 3: DJ EuroStoxx50 Index

Source: I-Net Bridge

Chart 4: Hang Seng Index (Hong Kong)

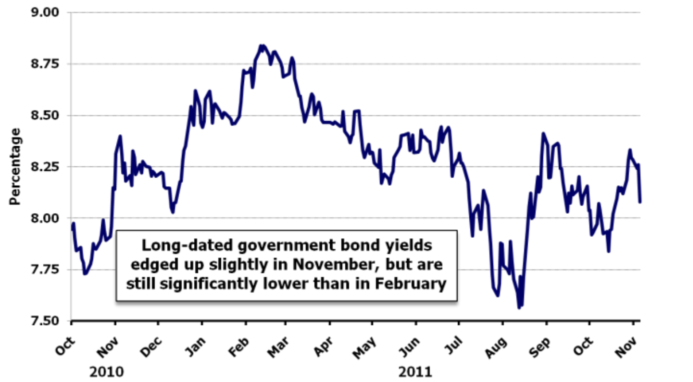


Source: I-Net Bridge

Chart 5: FTSE/JSE All Share Index

Source: I-Net Bridge

Chart 6: South African Long-Dated Government Bond Yield



Source: I-Net Bridge

Ian Anderson, CFA, CAIA
Chief Investment Officer

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