



## Newsflash

A new month and the 43<sup>rd</sup> issue of Viewpoint from FP.

This document will be made available on our website  
[www.financial-partners.biz](http://www.financial-partners.biz)

## Table of Contents

- |                             |              |
|-----------------------------|--------------|
| <b>1. March 2010 Review</b> | <b>1 – 5</b> |
| <b>2. Focus</b>             | <b>6 – 9</b> |
| <b>3. Important Notice</b>  | <b>11</b>    |

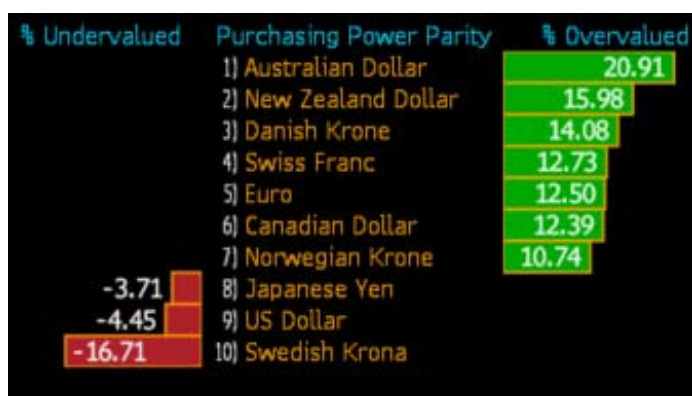
RMB Asset Management International Limited (Registered as a company in England under Reg. No. 3733094 with offices at 5<sup>th</sup> Floor, 20 Gracechurch Street, London, EC2V 0BG is authorised and regulated by the Financial Services Authority and is a member of the FirstRand Group.

Parallel universes - that is how the world within which bonds and equities operate could be described now. During March and into April equity markets continued to strengthen on the back of improving economic news, as well as better than expected company results. Bonds, on the other hand, did not sell off significantly as one would have expected on the back of deflation fears starting to recede and sovereign risk increasingly coming under the spotlight.

On the macro economic front the United States' economic outlook still warrants some caution given the weak labour market and accompanying frail growth in money supply and credit extension. Even though the recession officially ended nine months ago the economic environment still seems somewhat vulnerable. The immense fiscal and monetary response to the credit crisis certainly put a stop to freefalling asset prices, but has not yet proven to trigger a sustainable recovery in confidence and more importantly spending. Based on our latest assessment it seems more and more unlikely that the Federal Reserve will raise interest rates this year. As mentioned before deleveraging is indeed a multi-year event. In the United Kingdom the election date has been announced as May the 6th, and the latest polls indicate that the Tories are unlikely to gain a clear majority at the polls. For the first time in the country's history debates between the leaders of the three main parties – the Conservatives, Labour and Liberal Democrats are being aired on national television. With two of the debates completed as we write it seems as though

Nick Clegg of the Liberal Democrats has managed to use the opportunity to raise his party's profile – so much so that the likelihood of a hung parliament has increased. In the short term this does not augur well for the Pound Sterling, although it is clear that whoever is in power following the election will have to significantly reduce government spending. The currency seems to be significantly undervalued against its European neighbour at the moment, which may present an attractive buying opportunity to the risk aware investor. The chart below shows the valuation of the Pound versus a number of other major currencies on a purchasing power parity basis, using the consumer price indices as inflation measure:

**Fig.1 Purchasing Power Parity (base currency GBP)**



On the other side of the English Channel the European Monetary Union member states (albeit with some assistance and encouragement from the International Monetary Fund) have continued to try and put some kind of rescue plan together for their Greek compatriots. The detail of the plan has not quite been finalised, but its success (or failure) will certainly be tested on 19 May when the first of Greece's 2010 bond repayments is due in the form of the maturity of a €8.5 billion 10 year bond. Other European countries' government finances have also come under the spotlight with the spreads of credit default swaps (essentially the insurance premium against default) of Portugal and some Eastern European countries blowing out to fresh wides in recent days.

For the Japanese stock market to make significant gains a sustainable recovery in the domestic economy is required, as opposed to the current green shoots that are visible.

A weaker Japanese Yen would certainly support such an economic revival, and with China now taking up the position as Japan's number one export destination (see this month's FOCUS) market commentators are certainly gaining optimism. Longer term the burgeoning industry consolidation could add to the impetus, but this will take longer to impact corporate profitability, especially in the retail sector. As is the case in the United States significant employment gains and a resumption of domestic credit extension will be required in order to provide certain domestic sectors with a new found investment catalyst.

The economic outlook for emerging markets is somewhat rosier than their developed counterparts as the 'sweet spot' of strong growth and reducing inflation returned to emerging markets. Growth remained robust, but the feared pick-up in inflation did not materialise. Annual inflation actually fell compared to the previous month in many emerging markets. Asset prices reacted with a commensurate positive move as local equities, bonds and currencies did well during the month. The returns were supported by significant capital flows, which are increasingly focused on emerging market debt denominated in local currency. The reaction of central banks to these conditions is taking on different shapes, with some Asian central banks starting to normalise policy rates. On the other hand central banks in Africa, Russia and emerging Europe are using better inflation news to justify further rate cuts.

In March global equity markets surged ahead following weakness in the first six weeks of the year. After lagging for most of the 2009 recovery the Japanese equity market is now the best performer for the year to date, adding 8.8% in local currency terms, and only a little less (8.4%) in US Dollar terms. Emerging equity markets erased their January and February losses, but still lag its developed counterparts by a little under 1% since the start of the year. This was not totally unexpected as equity indices of most emerging markets are now being valued at a higher price to book ratio than most of the major developed bourses. Over the long term it is not that easy to find detractors in the fundamentals

of emerging markets. Economic growth is robust and on the increase, inflation is well behaved (at least for now), business and consumer confidence is high and central banks are still providing ample support to the markets through the provision of liquidity.

With the exception of government paper which was broadly weaker across the globe, bonds managed to still produce positive returns in spite of the buoyant equity markets. This was partly due to the decrease in yield spreads of investment grade bonds over government bonds, as well as the additional yield earned on especially high yield bonds in the US and Europe. In spite of an extremely strong performance in 2009 the latter still offers value to investors with the ability to take

somewhat higher risk, but without the appetite for pure equity exposure.

Global property securities performed in line with equity markets, as improving economic conditions are starting to create a better environment for property development. Agricultural commodities remain the laggards for the last 15 months, and this sector does not appear to hold a lot of value at the moment. Gold has also not added any significant performance to portfolios in the first quarter of 2010.

In April the first quarter reporting season will provide an indicator to the health of the corporate sector, which remains one of our main investment themes for 2010.

## Asset Class Performances

| Asset Class/Region                  | Index  | Currency | Mar 2010 | YTD 2010 |
|-------------------------------------|--|----------|----------|----------|
| <b>Equities</b>                     |  |          |          |          |
| United States                       | S&P 500 NR   | USD      | 6.0      | 5.2      |
| United Kingdom                      | FTSE All Share TR                                    | GBP      | 6.8      | 6.4      |
| Continental Europe                  | MSCI Europe ex UK NR                                 | EUR      | 7.6      | 3.5      |
| Japan                               | Topix TR   | JPY      | 10.4     | 8.8      |
| Australia                           | S&P/ASX 300 TR                                       | AUD      | 5.7      | 1.3      |
| Global                              | MSCI World NR  | USD      | 6.2      | 3.2      |
| Global Emerging Markets             | MSCI World Emerging Markets TR                       | USD      | 8.1      | 2.4      |
| <b>Bonds</b>                        |  |          |          |          |
| US Treasuries                       | JP Morgan United States Government Bond Index TR     | USD      | -0.9     | 1.1      |
| US Treasuries (inflation protected) | Barclays Capital U.S. Government Inflation Linked TR | USD      | 0.1      | 0.5      |
| US Corporate (investment grade)     | Barclays Capital U.S. Corporate Investment Grade TR  | USD      | 0.3      | 2.3      |
| Us High Yield                       | Barclays Capital U.S. High Yield 2% Issuer Cap TR    | USD      | 3.0      | 4.5      |
| UK Gilts                            | JP Morgan United Kingdom Government Bond Index TR    | GBP      | 0.9      | 1.1      |
| UK Corporate (investment grade)     | Merrill Lynch Sterling Non Gilts TR                  | GBP      | 1.9      | 4.0      |
| Euro Government Bonds               | Citigroup EMU GBI TR                                 | EUR      | 0.6      | 2.2      |
| Euro Corporate (investment grade)   | Barclays Capital Euro Aggregate Corporate TR         | EUR      | 1.0      | 3.3      |
| Euro High Yield                     | Merrill Lynch Euro High Yield 3% constrained TR      | EUR      | 5.1      | 9.0      |
| Australian Government               | JP Morgan Japan Government Bond Index TR             | AUD      | -0.2     | -0.1     |
| Japanese Government                 | JP Morgan Japan Government Bond Index TR             | JPY      | -0.9     | 0.7      |
| Global Government Bonds             | JP Morgan Global GBI                                 | USD      | -1.8     | -1.1     |
| Global Bonds                        | Citigroup World Broad Investment Grade (WBIG) TR     | USD      | -1.0     | -0.8     |
| Global Convertible Bonds            | UBS Global Convertible Bond                          | USD      | 3.4      | 2.7      |
| Global Emerging Market Bonds        | JP Morgan Global EMBI+                               | USD      | 2.1      | 3.6      |

| Asset Class/Region               | Index                              | Currency | Mar 2010     | YTD 2010          |
|----------------------------------|------------------------------------|----------|--------------|-------------------|
| <b>Property</b>                  |                                    |          |              |                   |
| US Property securities           | MSCI US REIT TR                    | USD      | 10.0         | 9.7               |
| UK Property securities           | FTSE EPRA/NAREIT United Kingdom TR | GBP      | 5.7          | -0.9              |
| Europe ex UK Property securities | FTSE EPRA/NAREIT Europe ex UK TR   | EUR      | 7.0          | 6.4               |
| Asia Property securities         | FTSE EPRA/NAREIT Asia TR           | USD      | 4.9          | 0.8               |
| Australian Property securities   | FTSE EPRA/NAREIT Australia TR      | AUD      | 2.6          | 0.7               |
| Global Property securities       | FTSE EPRA/NAREIT Global TR         | USD      | 6.6          | 3.0               |
| <b>Currencies</b>                |                                    |          |              |                   |
| Euro                             |                                    | USD      | -0.9         | -5.7              |
| Sterling                         |                                    | USD      | -0.4         | -6.1              |
| Yen                              |                                    | USD      | -4.9         | -0.4              |
| Australian Dollar                |                                    | USD      | 2.5          | 2.1               |
| Rand                             |                                    | USD      | 4.4          | 0.3               |
| <b>Commodities</b>               |                                    |          |              |                   |
| Commodities                      | RICI TR                            | USD      | 0.7          | -2.3              |
| Agricultural Commodities         | RICI Agriculture TR                | USD      | -6.2         | -9.8              |
| Oil                              | ICE Crude Oil CR                   | USD      | 4.6          | 4.4               |
| Gold                             | Gold index                         | USD      | 0.7          | -0.8              |
| <b>Interest rates</b>            |                                    |          |              |                   |
|                                  | Last meeting                       |          | Current rate | Change at meeting |
| United States                    | 16 March 2010                      | USD      | 0.25%        | 0.00%             |
| United Kingdom                   | 8 April 2010                       | GBP      | 0.50%        | 0.00%             |
| Eurozone                         | 8 April 2010                       | EUR      | 1.00%        | 0.00%             |
| Japan                            | 7 April 2010                       | JPY      | 0.10%        | 0.00%             |
| Australia                        | 6 April 2010                       | AUD      | 4.25%        | 0.25%             |
| South Africa                     | 26 March 2010                      | ZAR      | 6.50%        | -0.50%            |

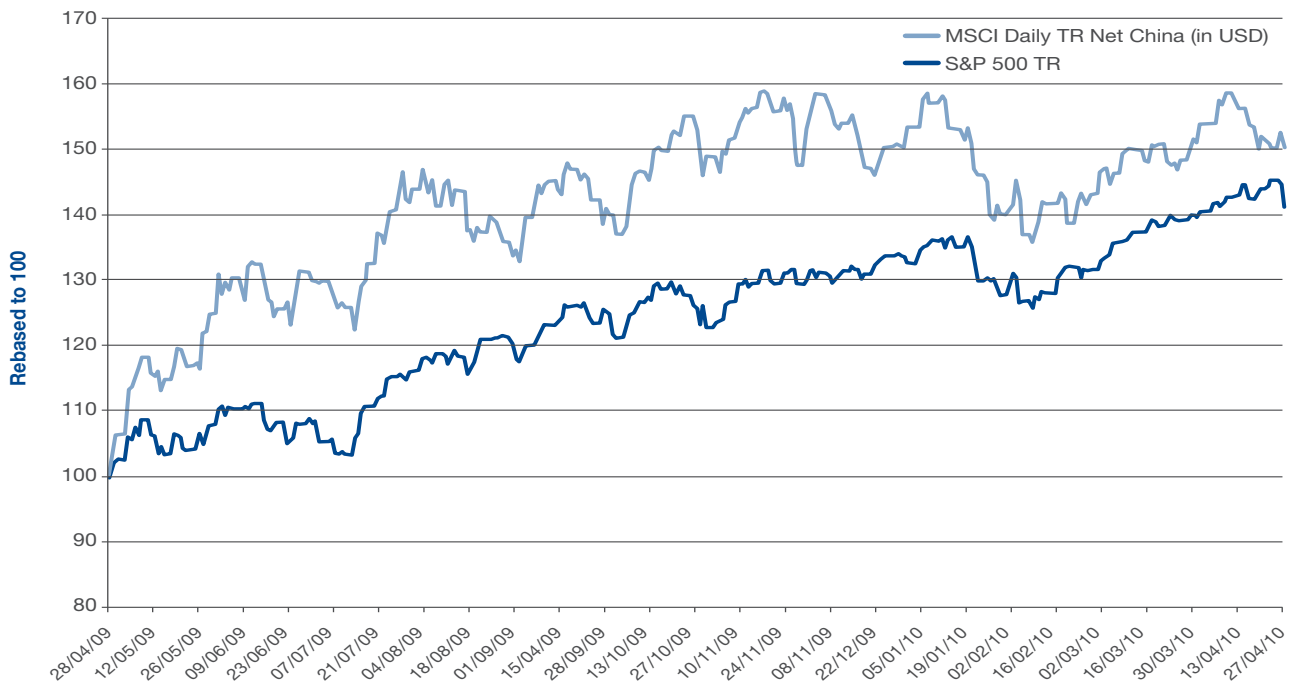
Source: Lipper Hindsight, April 2010

## FOCUS – If China sneezes...

In the history of the world the eruption of Eyjafjallajökull (or what is more commonly known as “that Icelandic Volcano”) may not go down as the biggest of its kind, but it certainly had European regulators at the highest level of alert. Whether their shutdown of most of the European airspace for five days was totally warranted to prevent aerial disasters we will probably never know, but that it had an impact on the movement of travellers around the globe cannot be disputed. Incidentally, the last eruption of this tongue twister volcano was in December 1821, and it lasted for 14 months.

FOCUS – the implications on the global economy of a slow down in China. Will the rest of the world catch a cold if China sneezes?

Conventional wisdom states that investment markets typically lead the economy by around 6 to 12 months. On this basis it is a good start to look at the MSCI China Index to get an idea of what has happened to Chinese equity market performance over the last 12 months (and as a reference we add the S&P 500 in USD terms):



Baekdu Mountain, also known as Changbai Mountain in China, is a volcanic mountain on the border between North Korea and China. It last erupted in 1901, and has been quiet ever since. Whether it has any significance (apart from being in China) and whether it will erupt any time soon is a matter of speculation, and so is the state of the Chinese economy, the date for the revaluation of the Chinese Renminbi, or central bank tightening. Which leads us into the topic of this month's

It is interesting to note that Chinese equities (measured in US Dollar terms) have underperformed US equities significantly since the start of the year (-2.0% versus +6.8%), but for the rolling twelve month period to the last week in April it has kept ahead (+50.3% against +41.3%). On the premise that the economy mimics markets, but with the typical lag mentioned above, it would not be surprising to see a slow down in the Chinese economy over the next twelve months

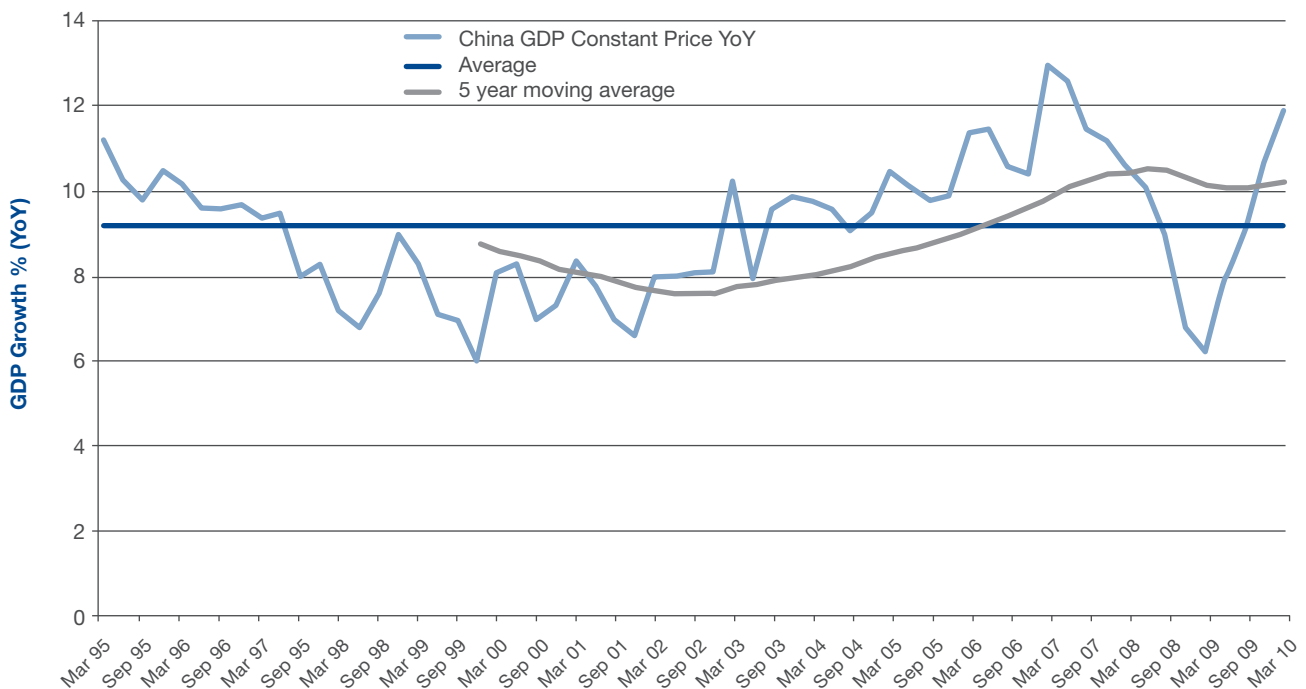
and this seems to be priced into Chinese equity markets right now. Another indicator that supports this thesis is the year on year change in China's gross domestic product (GDP). Incidentally China now makes up 8% of the global economy. Industrial production has grown by more than 20% in the year to January 2010, which is the highest growth rate since 1995 when China started to publish this indicator. Fixed investment has surged by a little under 27% in January and February and retail sales are up by almost 18%.

Lastly exports have grown by 46% year on year at the end of February 2010. The information above indicates a current GDP growth rate of between 12 and 13%, which is significantly higher than the five year moving average of 10%.

Also, on the back of massive monetary and fiscal stimulus GDP grew by 8.7% in the 2009 calendar year. This is somewhat higher than the government's target rate of 8%, and this in a time when most of the world's economies are growing way below their respective policymakers' target rates. As firm believers of mean reversion we can certainly see the economic growth rate of China slowing down, and the question that then remains is whether this will be an

emergency landing a soft glide on to the runway. Up to now the Chinese policymakers were able to keep the economy intact through the global crisis, which certainly points to a soft landing. Unfortunately current market pricing indicates much more of a tumultuous touch down, as reflected in the nearly 15% drop in equity markets from early January to early February. This may be result of the recent announcement by their housing minister who stepped up measures to dampen the nation's property price rises. He announced tougher regulations on the sales of uncompleted apartments by developers, adding to the curbs on loans for third-home purchases, increased down payment requirements and higher mortgage rates which were all announced since the start of the year. If these brakes to economic growth are applied to harshly it may cause GDP growth to not only revert to the mean but overshoot on the way down. This in turn could have a negative effect on commodity prices and risky assets.

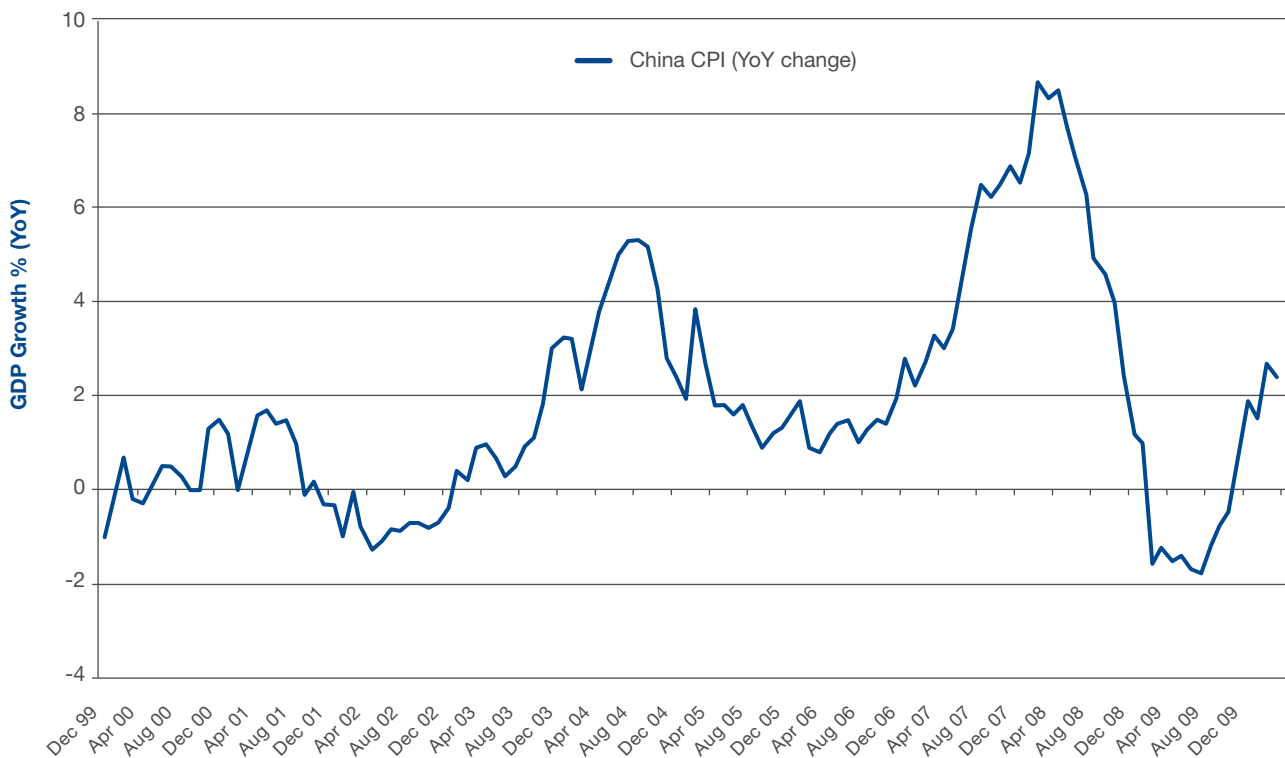
Another factor that the Chinese government needs to consider very carefully is the effect that an acceleration of inflation may have on economic growth. The relaxed credit extension environment that has been forced upon banks by the policymakers has created an environment that certainly



lays the foundation for an increase in asset prices, if not goods and services in general. They have certainly attempted to reign in the spending capacity (especially in the property sector) with the measures mentioned above, but if economic growth remains well above trend inflation may just start to pick up. This would lead to a harder application of the economic brakes, which could upset the fine balance that currently exists between a nurturing environment for asset price growth whilst not allowing the economy to overheat. As the graph below illustrates inflation is not a concern at the moment, but recent history has shown that it does not take long to become one.

last decade, and around 90% of the total growth in copper demand. Similar trends also hold for nickel and zinc. Based on these numbers the major commodity exporters such as Australia, Canada, Norway, Brazil and Chile come to mind and would certainly be worried about developments in the Chinese economy. If both commodity prices and the level of commodity exports to China were to fall it would have a leveraged effect on these countries. Similarly oil exporters in the Middle East would struggle on the back of a decrease of oil prices.

The flipside of a decrease in commodity prices is of course that other commodity importers outside of China stand to



So, on the premise that China may in all likelihood slow down but not to levels much below year on year economic growth of around 8%, what does that mean for the world economy? Clearly the exporters to China would stand to lose if economic growth returns to its long term trend. China has absorbed about 30% of the increase in global oil production over the

benefit from downwards pressure on these markets. It would also lead to a reduction in inflationary pressures, especially in the global emerging economies, which could allow central banks to keep interest rates lower for longer and therefore retain the current favourable monetary environment which is geared towards growth.

Not discounting the importance of China as a commodity importer, it should be noted that about 60 percent of Chinese imports still consist of manufactured goods, machinery and transport equipment. It therefore comes as no surprise that Japan (at 12.8% of total imports) is China's largest trading partner from an import point of view. The land of the rising sun therefore stands to lose more than others on the back of slower economic growth.

It is clear that the expected return to trend growth in China (without overshooting on the downside) would put pressure on commodity prices, but as it makes up (only!) 8% of global economic activity it would have relatively less of an effect on global GDP.

In summary it is probably fair to assume that:

- It is unlikely that China would have a hard landing as economic growth returns to its long term trend of between 8% and 9%.
- The market seems to have priced in a bumpy landing which could lead to positive surprises if Chinese policymakers manage the landing better than expected.
- A slowdown in China would have a bigger effect on the distribution of global income (with some economies gaining when others are losing) than on the overall level of global GDP.

Lastly we consider the effect of the scenario sketched above on equity and bond markets. A fall in commodity prices would have a detrimental effect on equities, and particularly so on companies in the material and resource sectors. Chinese equities could be the big loser, but commodity exposed currencies such as the Canadian and Australian Dollar, Brazilian Real and Russian Ruble also stand to come under pressure.

Government bond yields may drift up on the reduction of Chinese interest in US treasuries, but on the other hand falling commodity prices (lower inflation) and slower global growth (larger output gaps) would lead to central banks around the world maintaining easy monetary policies. The risk aversion that comes along with an economic slowdown in China could also support government bond valuations. On the balance of probabilities a deceleration in the Chinese economy could be bullish for bonds.

*Click here for:*



**Disclaimer:**

*Simply click on the link of the company that you are interested in. By clicking on any external links provided on this website, you will leave the Financial Partners site and be re-directed to an external organisation's website.*

*As Financial Partners is not responsible for any content or activities associated with any external website accessed by hypertext links appearing on this website, and as such content has been independently developed by third parties and is outside of our control and subject to change without notice, Financial Partners hereby disclaims any representations, warranties, or guarantees made on external websites.*

*Further, Financial Partners does not guarantee the correctness or suitability of such information or of any other linked information presented, referenced, or implied. Any hyperlink from this website leading to another website should not be interpreted as an endorsement by Financial Partners of that website, its organisation, or of its products or services.*

*Financial Partners does not accept responsibility for any loss, harm, or damage, however caused, for information by third party organisations with links appearing on this website. Clicking on any of the following external links constitutes a signature of your consent to the above disclaimer. If you disagree with all, or part of this disclaimer, use of the external links provided below is strictly prohibited.*

## Important Notes

RMB Asset Management is the trading name for RMB Asset Management International Limited. This document does not constitute an offer or solicitation to any person in any jurisdiction in which it is not authorised or permitted, or to anyone who would be an unlawful recipient, and is only intended for use by original recipients and addressees. The original recipient is solely responsible for any actions in further distributing this document, and should be satisfied in doing so that there is no breach of local legislation or regulation. The information is intended solely for use by our clients or prospective clients, and should not be reproduced or distributed except via original recipients acting as professional intermediaries. This document is not for distribution in the United States.

Prospective investors should inform themselves and if need be take appropriate advice regarding applicable legal, taxation and exchange control regulations in countries of their citizenship, residence or domicile which may be relevant to the acquisition, holding, transfer, redemption or disposal of any investments herein solicited.

Any opinions expressed herein are those at the date this material is issued. Data, models and other statistics are sourced from our own records, unless otherwise stated herein. We believe that the information contained is from reliable sources, but we do not guarantee the relevance, accuracy or completeness thereof. Unless otherwise provided under UK law, RMB Asset Management does not accept liability for irrelevant, inaccurate or incomplete information contained, or for the correctness of opinions expressed.

We caution that the value of investments in discretionary accounts, and the income derived, may fluctuate and an investor may incur losses, including a loss of the principal invested. Past performance is not generally indicative of future performance. Investors whose reference currency differs

from that in which the underlying assets are invested may be subject to exchange rate movements that alter the value of their investments.

Our investment mandates in alternative strategies and hedge funds permit us to invest in unregulated funds that may be highly volatile. Although alternative strategies funds will seek to follow a wide diversification policy, these funds may be subject to sudden and/or large falls in value. The illiquid nature of the underlying funds is such that alternative strategies funds deal infrequently and require longer notice periods for redemptions. These Investments are therefore not readily realisable. If an alternative strategies fund fails to perform, it may not be possible to realise the investment without further loss in value. These unregulated funds may engage in the short selling of securities or may use a greater degree of gearing than is permitted for regulated funds (including the ability to borrow for a leverage strategy). A relatively small price movement may result in a disproportionately large movement in the investment value. The purpose of gearing is to achieve higher returns associated with larger investment exposures, but has concomitant exposure to loss if positive performance is not achieved. Reliable information about the value of an investment in an alternative strategies fund may not be available (other than at the fund's infrequent valuation points).

Under our multi-management arrangements, we selectively appoint underlying sub-investment managers and funds to actively manage underlying asset holdings in the pursuit of achieving mandated performance objectives. Annual investment management fees are payable both to the multimanager and the manager of the underlying assets at rates contained in the offering documents of the relevant portfolios (and may involve performance fees where expressly indicated therein).

*RMB Asset Management International Limited (Company Registration No. 3733094) is a member of the FirstRand Group, and has its registered office at 20 Gracechurch Street, London, EC3V 0BG.*

*RMB Asset Management International Limited is authorised and regulated by the Financial Services Authority in the United Kingdom, and is an authorised Financial Services Provider pursuant to the Financial Advisory and Intermediary Services Act 37 of 2002 in South Africa.*

© RMB Asset Management International Limited 2008