

# Investec Opportunity Fund

As at 31 May 2010



## Market review

Doubts about the health of the global recovery and governments' ability to service large debt burdens weighed heavily on risk assets in May. The flight to safety followed the usual path, with equity markets ending sharply lower and developed market debt closing mostly firmer. The EUR750bn bailout package to Southern European states provided temporary relief, but proved insufficient to reintroduce renewed confidence into global markets. Returns in May and the year to date remain in negative territory, with emerging markets outperforming the larger markets. Portfolio flows into emerging markets remained positive with investors seeking higher yields and the superior growth offered by developing economies. The recent retracement of the euro's strength against the US dollar is symptomatic of the narrow focus on current concerns about Greece, while the ramifications of the sovereign debt crises may be far bigger and much longer in duration than currently anticipated. Central banks remained on hold, as the precarious state of the recovery constrains a normalisation of rates. The market continues to speculate about the next policy move in China, after softer property activity and disappointing trade data imply a moderation of Chinese growth near term.

Risk aversion got the better of metal prices, with copper (-6%), aluminium (-6.7%), oil (-14.3%) and platinum (-9.6%) closing the month weaker. Gold remains in favour and continues to trade near historical highs. The MSCI World Index closed 9.5% weaker, while emerging markets lost 9.2%. Brazil (-10.9%), Russia (-11%) and Korea (-12.2%) saw double digit losses, with China (-5.4%) the strongest performer. The MSCI SA Index lost 7.3% in May. The Nikkei (-11.7%) was the worst performer amongst the larger equity markets, the S&P closed down 8.2% and the FTSE 100 lost 6.6%. The DAX outperformed, ending 2.5% weaker.

The local growth trajectory remains positive. The Reserve Bank kept interest rates on hold at historical lows, citing continued downward pressure on inflation and renewed fears that concerns about country balance sheets were likely to depress the recovery. Year on year activity data comparisons remain high, boosted by the impact of accommodative policy and the weak base in 1H 2009. House price inflation is showing signs of turning positive, but credit demand and transaction activity remains weak. The local bond market sold off on the back of weaker emerging markets despite better than expected fiscal data. A sharply weaker currency and lower commodity prices added to the downdraft. The bond market did however bounce off its intra month low on better than expected inflation data and somewhat calmer global markets. The All Bond Index (ALBI) closed down 0.4%. The listed property sector was the worst performer (down 2.2%) giving up some of its gains year to date. Landlords remain cautious on the outlook for direct property with margin pressure and tenant quality the primary concerns.

The local equity market finished 5.1% lower, to push this year's market return back into negative territory. The rand's weakness provided limited support to resource investors, with the sector substantially underperforming. The sector lost 6.5% as a result of weaker general miners and the platinum sector, down 9.0% and 7.8% respectively. Gold, buoyed by the firm bullion price closed up 6.6%. Telco's (-0.1%), technology (5.8%) and retail (1.1%) were other outperforming sectors. Beverages (-8.8%), personal goods (-6.9%) and the paper sector (-8.1%) were the laggards.

## Portfolio review

We have not been entirely surprised by the broad market correction. Unfortunately two of the portfolio's large holdings did not help performance this month despite our cautious positioning.

Assore's share price lost 13% in market value as perceptions around peak pricing for iron ore and manganese took hold. The manganese price, which is still trending up from the lows still looks sustainable. It is well below its normal value, and even at the current rand/dollar exchange rate, the share price is implying an iron ore price below \$70/t, against a market price of \$147/t. We still see considerable long term value in the share price despite the market's view.

Samsung Electronics has delivered strong results. The share price however dropped by 20% despite rising microchip prices, below normal margins, prodigious free cash flows and a single digit earnings multiple. We simply think that either the world economy is about to implode, with dire consequences for many cyclical businesses on double digit multiples, or the share price is overdone.

On the positive side, the holding in physical gold continues to outperform both gold shares and the markets. We cannot see how the local gold shares' dynamics of falling production volumes, rising costs, increased capital commitments and constrained profitability will lead to gold share price outperformance. As South Africa's gold production declines over the next several years, we see a continued rise in the rand price of gold, and that is the exposure we chose to hold.

## Portfolio positioning

The South African equity exposure is at 42% while total equity exposure is 56% when including the foreign equity exposure. We have substantial liquid resources in the fund and will judiciously apply these funds where and when suitable.

Collective investment schemes in securities (unit trusts) are generally medium to long term investments. The value of participatory interests (units) may go down as well as up and past performance is not necessarily a guide to the future. Fluctuations or movements in exchange rates may cause the value of underlying international investments to go up or down. Unit trusts are traded at ruling prices and can engage in borrowing and scrip lending. Forward pricing is used. Quantifiable deductions are the initial fee whilst non-quantifiable deductions included in the net asset value price may comprise brokerage, MST, auditor's fees, bank charges, trustee and custodian fees. Commissions and incentives may be paid and if so, would be included in the overall costs. A schedule of fees and charges and maximum commissions is available on request from the company/scheme. If required, the portfolio manager may borrow up to 10% of the market value of the portfolio to bridge insufficient liquidity. Unit trust prices are calculated on a net asset value basis, which is the total value of all assets in the portfolio including any income accrued and less any permissible deductions from the portfolio. Different classes of units apply to the fund and are subject to different fees and charges. Fund valuations take place at approximately 16h00 SA time each day. Purchase and repurchase requests must be received by the Manager by 16h00 SA time each business day. Performance figures are based on lump sum investment (if applicable). This portfolio may be closed in order to be managed in accordance with the mandate (if applicable). \* Inward listings are shares that are listed on the JSE but regarded by the SA Reserve Bank as foreign investments. A notable example is British American Tobacco (BAT) which used to be held via Remgro and Richemont, both being domestic. BAT was unbundled at the end of October 2008 and inward-listed on the JSE. The presence of inward-listings in the Fund does not therefore mean that the Fund's investment strategy has changed in any way. Please note that with effect from 1 February 2009 the annual management fee on B class units increased by 0.285% (incl. VAT). The risk profile is a measure of volatility, i.e. how the absolute return of the fund varies. Note that there are other risks in the fund, which are not reflected in this rating. \*\* The TER shows the percentage of the average Net Asset Value of the portfolio that was incurred as charges, levies and fees relating to the management of the portfolio. A higher TER ratio does not necessarily imply poor return, nor does a low TER imply a good return. The current TER can not be regarded as an indication of the future TERs.

A copy of our performance fees FAQ is available at [www.investecfunds.co.za](http://www.investecfunds.co.za). Investec Fund Managers SA Ltd is a member of the Association for Savings & Investment SA.

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