GTC

Formerly Grant Thornton Capital

August 2014

Market Update

Global

August saw U.S. markets roaring ahead with the S&P 500 closing the month at a record high 2003.37 points. The index gained 3.77% for the month with mergers and acquisitions providing the catalyst. The Dow Jones gained 3.23% and the NASDAQ 4.82%.The FTSE 100 gained 1.33% as U.K. GDP rose 0.8%. The Dax Composite rose 0.69% despite Q2 GDP contracting 0.2%.The Japanese Nikkei 225 closed 1.26% lower. The MSCI Emerging Market Index rose 2.07% slightly outperforming the MSCI World Index which rose 2.0%.

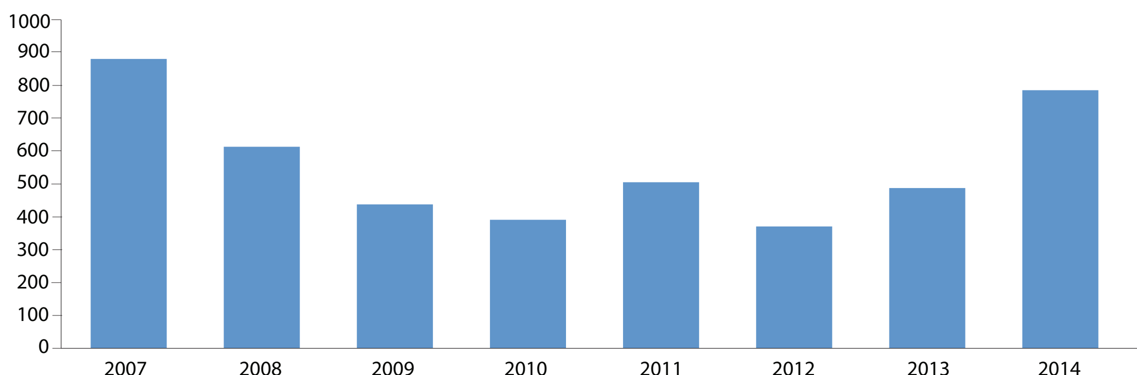
There was an insatiable demand for U.S. equities during the month with the S&P 500 leading the pack. Mergers and acquisitions were a key factor to this market exuberance coupled with dramatic Q2 GDP which was estimated at 4.0 %.Manufacturing was particularly strong with the housing market showing early signs of some recovery. U.S. durable goods orders jumped a massive 22.6% in July thanks to bumper demand for Boeing aircraft.

However some concerns began to emerge regarding a possible earlier introduction of policy tightening by the Federal Reserve as most of the leading economic indicators continued to display vigorous growth. Even the prospect of rising base rates in 2015 only helped spur on the financial sector with banks tipped to enjoy increased interest margins.

The recovery in the U.S. in Q2 was far greater than initially reported with GDP growing at a revised annualised rate of 4.2%.Business spending grew more than expected and U.S. based corporations posted higher profits. Corporate profits after tax were up 6% from theQ1.

The quarter on quarter rise comes after two successive quarters of declining profits. Real personal consumption increased 2.5% in Q2 compared to an increase of 1.2% in Q1. Durable goods increased 14.3% versus 3.2% in the previous quarter.

US Mergers and Acquisitions



Source: Money.cnn

Federal Reserve Chair Janet Yellen speaking at the Jackson Hole central bank symposium cautioned that the Fed should move cautiously in deciding when to raise interest rates given the current state of the U.S. labour market.

Yellen laid out in detail why she feels the unemployment rate alone is inadequate to evaluate the strength of the jobs market and why the Fed needs to step gingerly. Yellen's comments underlined how the Fed was still wrestling with the complexities of the labour market in the aftermath of the 2007/2008 financial crisis. Financial market reaction to Yellen's remarks was muted. Encouraging signals regarding the health of the U.S. economy continued to offset worries over global geo-political tensions and weaker economic data from the Eurozone.

Eurozone equities delivered positive returns in August after a negative month in July. Equity gains were supported by increased speculation that further stimulus measures such as quantitative easing (QE) would be introduced by the European Central Bank (ECB). The ECB kept monetary policy unchanged at its August meeting but President Mario Draghi said at the Jackson Hole central bank summit that the ECB would use all available instruments to stabilize prices and also pointed to a long term decline in inflation expectations within the Eurozone.

The strengthening of the U.S. dollar versus the Euro provided further support for European equities. The provisional reading of Eurozone annual inflation for August came in at a 5 year low of 0.3% down from 0.4% in July. Geo-political events in Ukraine continued to haunt European markets with the ever present threat of further sanctions being imposed on Russia curbing investor confidence.

The potential threat of gas supplies from Russia being disrupted did little to inspire confidence. What started in Europe four years ago as a banking and sovereign debt crisis has become a growth crisis of serious proportions enveloping Europe's three largest economies. Germany is teetering on the brink of recession, France's economy is stagnant and Italy's GDP shrank 0.2% in Q2 against 0.1% in Q1 officially confirming it is now in recession. Of major concern is that these three countries account for two-thirds of Eurozone GDP.

After faltering in the first week of the month U.K. equities recovered in line with global markets as speculation grew that the ECB was considering introducing quantitative easing. Cyclical sectors led the market higher as the risk-on sentiment favoured equities geared to economic recovery while the market got an additional lift as expectations of an early interest rate hike receded.

The Japanese equity market weakened sharply in August before recovering some lost ground to close down just 0.9% for the month. Economic data released during the month was far weaker than expected. The impact of the consumption tax hike was clearly impacting longer than expected. Japan the world's third largest economy had a negative GDP of 1.7% in Q2.

Growth in China's vast manufacturing industry weakened in August suggesting that the recovery in the world's number 2 economy is losing momentum and that Beijing might well be forced to introduce further stimulatory measures to maintain economic growth.

The HSBC PMI fell to a three month low of 50.3 from 51.7 in July indicating that manufacturing companies are experiencing a slowdown in demand. China's economy has been struggling to stabilise after having achieved double-digit growth over the last decade.

Earlier in August data showed that China's exports had accelerated but that imports were markedly down suggesting a significant downturn in private domestic consumption. China's leaders earlier this year unveiled mini stimulus measures aimed at boosting areas such as housing and railways. Beijing will need to somehow prop up growth if the full year expectations of a 7.5% increase in GDP are to be achieved.

The authorities are desperately trying to steer economic growth away from relying so heavily on exports and foreign investment to a more balanced economy where private domestic consumption plays a bigger role.

Domestic

After a volatile performance in August the JSE/FTSE ALSI ended on a weaker note closing down at 50959.02 points having lost 0.46% for the month. The top 40 index declined 0.85% for the month. The best performing sector was Fixed Line Services which returned 15.06% followed by Non-Life Assurance which gained 10.07%.The worst performing sector was General Mining which lost 8.04% followed by Industrial Metals which lost 7.88%. It was a particularly difficult month for resources.

News of little cheer but at least on a more positive note was that GDP for Q2 came in at a positive 0.6% after a negative 0.6% in the previous quarter. The main contributors to the improvement were general government services, transport, storage and communications each contributing 0.4%.Mining and quarrying saw a 9.4% decline Q/Q. South Africa's trade balance recorded a R6.884 billion deficit in July after a revised R469.8 million deficit in June. Manufacturing fell 2.1% Q/Q reflecting weak consumer demand.

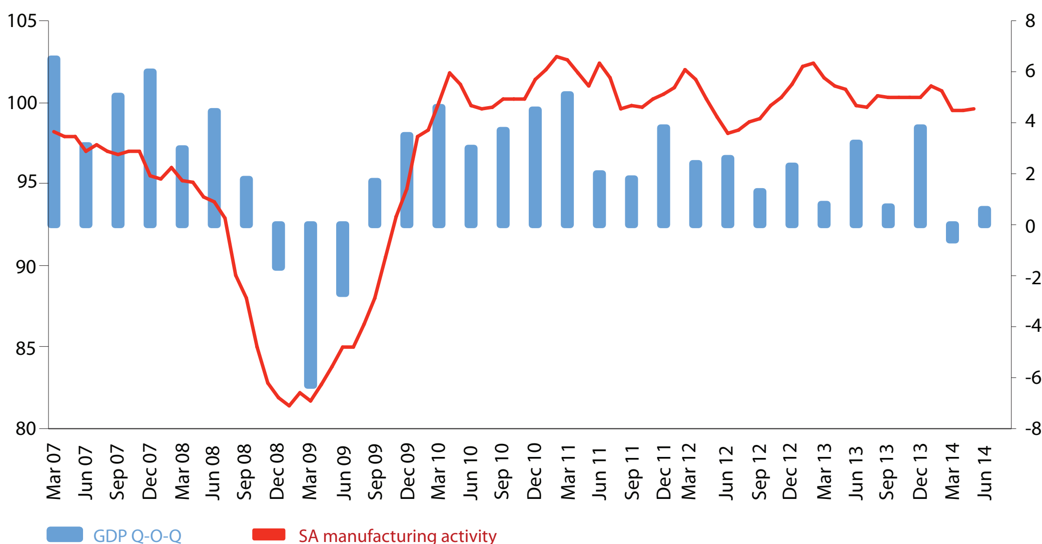
The story of the month was undoubtedly the demise of African Bank Investments Limited (ABIL) which had issued an earlier trading update which was far worse than expected. The group announced a loss of at least R6.4 billion as well as the immediate resignation of the CEO Leon Kirkinis who had been at the helm for 23 years.

It also announced that it would have to raise at least another R8.5 billion in order to remain solvent. Reaction from the South African Reserve Bank (SARB) was swift and sure, placing ABIL under curatorship under the control of Tom Winterboer of Price Waterhouse's financial services division. The outcome is that ABIL will effectively be split into two - a good bank and a bad bank. The good bank will be underwritten by a consortium of the major local banks who will underwrite the raising of R10 billion in new capital.

The good bank has a book value of R26 billion net of portfolio impairments making it a viable business. The bad bank will be housed in a vehicle supported by SARB who will pay R7 billion for it. Book value net of impairments is R17 billion. This will house the non-and underperforming assets. Under the deal struck by SARB, shareholders will be the biggest losers. First time holders of senior debt instruments and wholesale deposits will be forced to take a 10% haircut of around R5 billion.

Since the global financial crisis and in terms of the 2008 Basel agreement both shareholders and bond holders are required to bear some of the loss should a bank default. As a consequence of the ABIL default Moody's downgraded five of the major local banks not in terms of their balance sheet strength but rather in terms of their exposure to sovereign debt as well as adverse trading conditions going forward.

SA Leading indicators vs GDP Q-O-Q



Source: GTC/StatsSA

GTC Fund Performances - August 2014

Investment portfolios	3Mth	6Mth	12Mth	2Year*	3Year*	4Year*	5Year*
GTC Fixed Income B	3.64%	6.15%	7.84%	6.01%	5.51%	5.98%	6.39%
GTC Wealth Accumulator FOF B	3.21%	8.16%	17.08%	16.04%	13.59%	13.33%	13.13%
GTC Capital Plus FOF B	2.23%	6.11%	12.34%	10.65%	9.51%	8.48%	8.17%
FTSE/JSE All Share Index (ALSI)^	2.86%	8.84%	22.69%	21.85%	19.96%	18.74%	16.94%
FTSE/JSE Shareholder Weighted Index (SWIX)^	4.40%	11.61%	25.78%	22.00%	21.17%	19.71%	17.86%
BEASA All Bond Index (ALBI 1-3 year)^	1.40%	3.35%	4.93%	3.55%	4.59%	5.35%	8.78%
Cash (SteFi)^	1.10%	2.14%	4.00%	3.82%	3.91%	4.04%	4.37%
GTC Conservative Absolute Growth (R)	1.58%	4.00%	10.65%	20.71%	19.11%	15.56%	21.12%
GTC CAG's Composite Benchmark (R)^	1.33%	1.30%	11.10%	17.20%	18.22%	14.21%	10.14%
R/$ Exchange rate	0.83%	-0.48%	3.78%	12.39%	14.72%	9.77%	6.42%
GTC Global Conservative Absolute Growth ($)	0.93%	2.81%	8.50%	7.43%	5.76%	6.59%	5.34%
GTC Global CAG's Composite benchmark ($)^	0.49%	1.79%	7.03%	4.25%	3.02%	4.02%	3.47%

* Annualised ^Benchmark returns include 1,5% fees Not all fund class returns are shown. Class B refers to indirect investments

The **GTC Fixed Income Fund** has delivered outperformance against the Cash (SteFI) and Bond (ALBI 1-3 year) benchmarks over all periods. Inflation eased to 6.3% on the back of a decline in food prices.

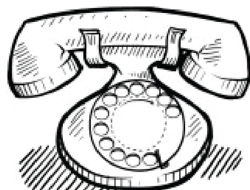
The **GTC Wealth Accumulator FoF** continues to participate in the strong positive returns delivered by the equity market while maintaining a defensive position should the markets sell off.

The **GTC Capital Plus FoF** has achieved healthy outperformance of its inflation relative target (CPI+3%) over the past year. The significant absolute return exposure ensures that the Fund captures upside equity return while focusing on avoiding losses over 12 month periods.

The **GTC Conservative Absolute Growth Fund** (USD and Rand classes) continues to deliver outperformance against its benchmark over all of the analysis periods displayed. The fund has captured a significant portion of the upside afforded by equity markets while still maintaining its capital protection objective.

Further information

Contact us



Head - Consulting Services
Jeff Morgan-Hill
T +27 (0) 11 322-4804
E jmhill@gt.co.za

Head - Investment Analytics
Clive Eggers
T +27 (0) 11 322-4844
E ceggers@gtc.co.za

Head - Healthcare
Jill Larken
T +27 (0) 21 322713 8504
E jlarken@gtc.co.za

Head - New Business Development
Roger Schärges
T +27 (0) 11 322-4507
E rscharges@gtc.co.za

Executive - Private Client Wealth Management
Jenny Williams
T +27 (0) 11 322-4532
E jwilliams@gtc.co.za

Executive - Employee Benefits Consulting
Toy Otto
T +27 (0) 11 322-4644
E totto@gtc.co.za

Chief Operating Officer
Farhadh Dildar
T +27 (0) 11 322-4821
E fdildar@gtc.co.za

Chief Executive Officer
Gary Mockler
T +27 (0) 11 322-4512
E gmockler@gtc.co.za

Compliance Officer
Dale Nussey
T +27 (0) 11 322-4828
E gmockler@gtc.co.za

GTC

Formerly Grant Thornton Capital

www.gtc.co.za

© 2014 GTC (Pty) Ltd. All rights reserved.
An Authorised Financial Services Provider. FSP731.