FP FINANCIAL PARTNERS

VIEWPOINT

www.financial-partners.biz | Vol. 30 | Feb 2009

Newsflash

A new month and the thirtieth issue of Viewpoint from FP.

This document will be made available on our website www.financial-partners.biz

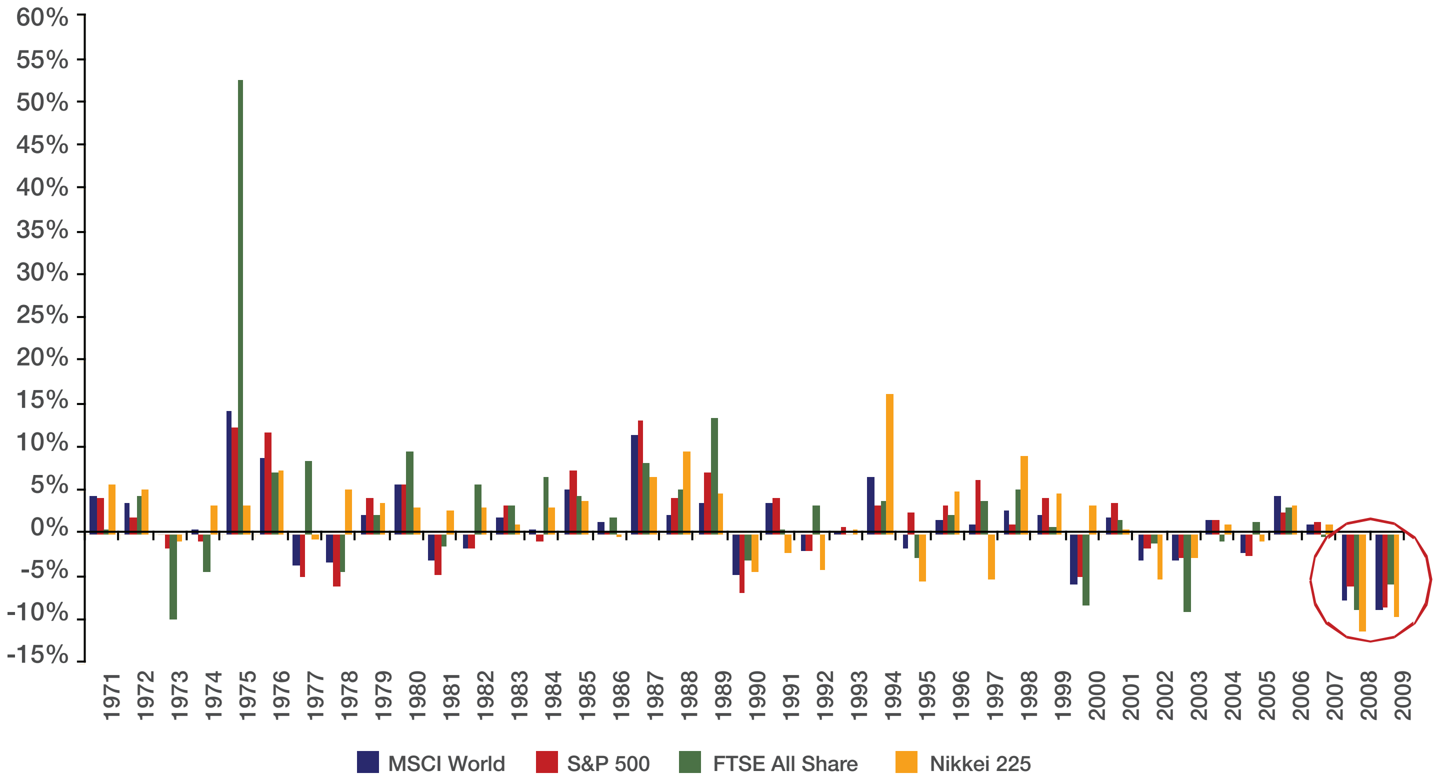
Table of Contents

Produced in association with RMB Asset Management International Limited (trading as RMB Asset Management), authorised and regulated by the Financial Services Authority (UK).

Many equity investors would be forgiven for checking on their calendars whether it is actually 2009, or for some reason we have entered a 'groundhog year' and are in fact back at the start of 2008. January 2009 produced much the same as January 2008, with both the MSCI World and S&P 500 indices respectively having their worst start to the year in the 39 years since 1971. The FTSE (in Sterling) and the Nikkei (in Yen) recorded their fifth and second worst January performances over the same period. This is probably a sign that equity markets are not going to be as quick out of the blocks this year like many investors had hoped, but few would have expected.

The major equity indices eroded their December 2008 gains and then some while investor sentiment remained negative during the month of January 2009. The major moves (measured in local currency with January 2008 number in brackets) were MSCI World -8.8% (-7.6%), S&P 500 -8.5% (-6.1%), FTSE All Share -5.8% (8.7%) and the Nikkei losing -7.6% (-8.8%). Continental Europe's equities were down -5.8% (-12.2%) and global emerging markets suffered a significant loss of -6.5%, albeit much less than January 2008's dismal -12.5% start to the year. It is interesting that the same absolute change in index points that caused the MSCI World to lose nearly -9% this January would have been a (mere!) -5% move last year in the corresponding month.

The outlook for equities remains bleak, although some market commentators are now starting to venture talk of stability, if



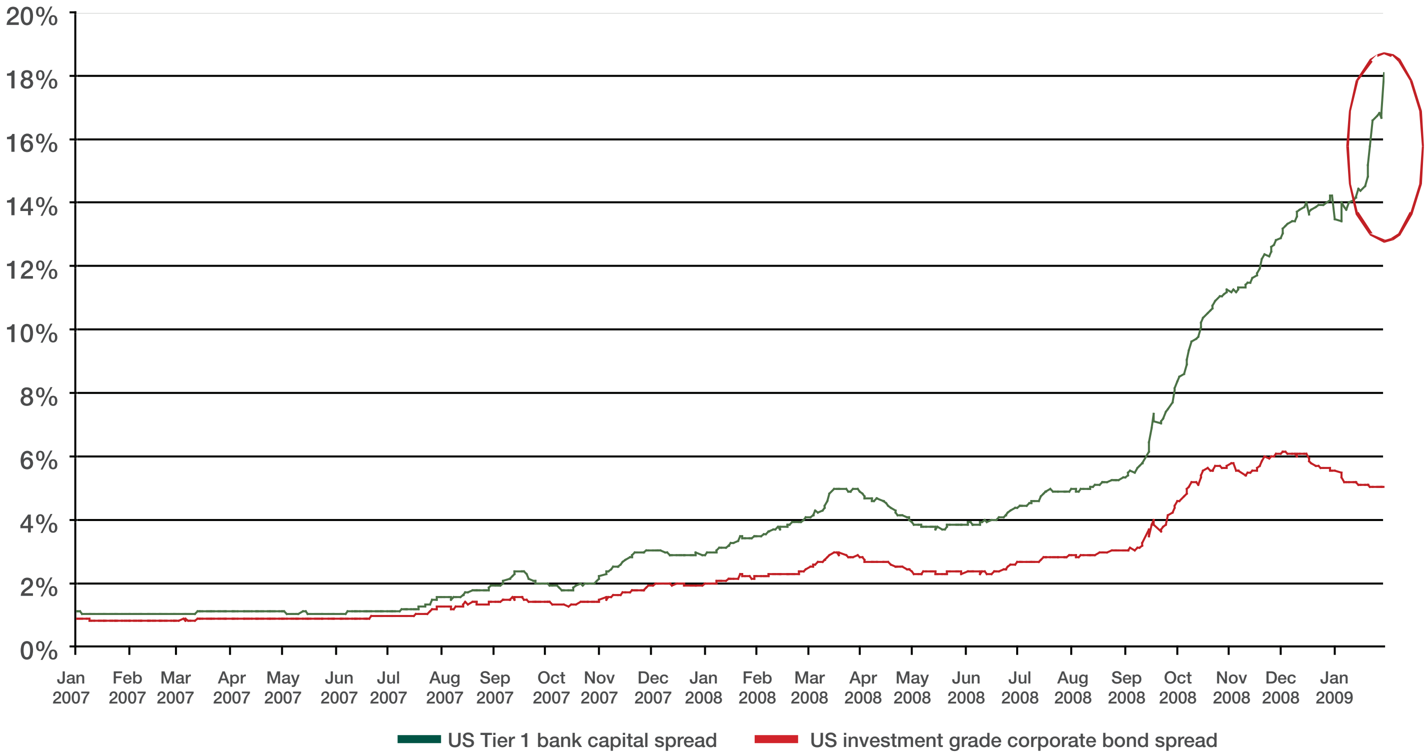
Source: RMB Asset Management / Bloomberg. January 2009

not a feeble recovery, towards the second quarter of 2009. Despite this, we are still very cautious of adding too much risk too early, and remain broadly underweight equities across the range of mandates that we manage.

In December's Viewpoint we referred to the more pronounced downside risk associated with government bonds, and in January 2009 yields in US Treasuries started to rise from their historical lows. Spreads of corporate bonds over government issues started to slowly decrease, but were unable to counter the rise in government debt yields. The result was that bonds across the risk spectrum gave up some of their end of year gains, with US bonds down 3.2% for the month, European bonds down -1.1%, Japanese bonds down -0.6% and globally government bonds (as measured by the CitiGroup World Government Bond Index) gave up -4.3% in US Dollar terms. The consensus pick amongst investors seems to be corporate bonds which should provide solid returns in the year to come, if buyers of this asset can steer clear of the sector and company specific risk associated with some of the issues in the market.

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

Option adjusted spread (US tier 1 bank capital vs invesment grade corporate bonds)



Source: RMB Asset Management / Bloomberg. January 2009

One fixed interest asset class that has kept on producing poor returns is tier 1 bank capital where the spread over sovereign moved up by approximately 5% during January, with the resulting decline in capital value hurting investors in this asset class. The continuous stream of bad news, surrounding UK and US banks in particular, did not bode well for the valuations of the lower levels (equities and tier 1 debt) of banks' capital structures. Other investment grade corporate bond spreads remained fairly stable over the same period resulting in a decoupling of the spreads of tier 1 bank capital from other investment grade issues.

Listed property has still not shown its defensive colours and continued to exhibit volatility greater than the equity market at the start of the year. US Real Estate Investment Trusts (REITs) lost 17.8% for the month, eroding most of the gains it managed in December. Real estate in the United Kingdom fared worst posting a -21.6% return for the month when measured in Pounds Sterling. Asian properties, as measured by the FTSE/EPRA Real Estate Asia index (in US Dollars) fared slightly better by giving up slightly less than -9%, with the same indicator for Europe staying almost flat for the month at -0.5%. In the previous edition we reported that the outlook for 2009 is bleak while credit extension remains tight.

US Dollar strength continued (or perhaps more accurately, lack of weakness...) into January and early February, with the euro being the notable loser (-8.65% for the year to 16 February 2009). Having already lost more than a quarter of its value against the greenback in 2008, the Pound Sterling has held up well against the dollar year to date, posting a small gain of 0.3% in January. Of the major currencies very

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

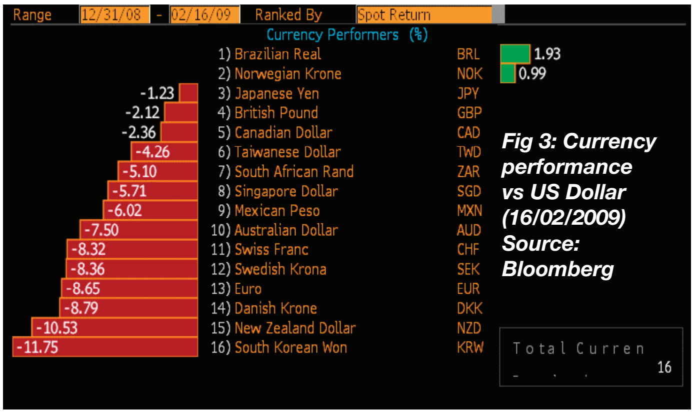
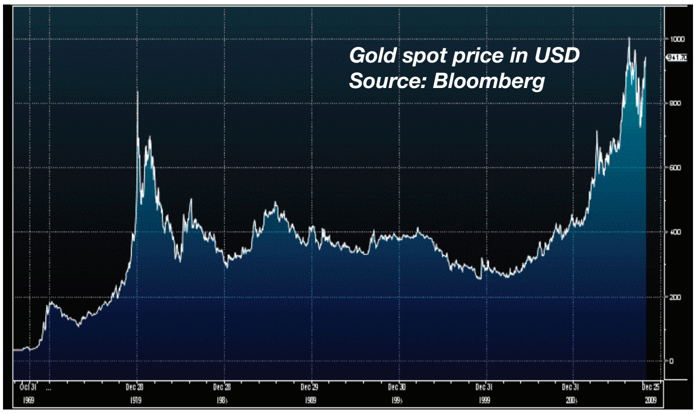


Fig 3: Currency performance vs US Dollar (16/02/2009) Source: Bloomberg



Gold spot price in USD Source: Bloomberg

few seem to be in any great shape and our advice would be to run investments close to currency benchmarks as foreign exchange rates are certain to exhibit a fair amount of volatility in 2009.

Hard and soft commodities, as measured by the Rogers International Commodity Indices, lost -5.1% and -2.9% respectively from the start of the year. With commodity prices falling so much and so sharply as they did during 2008 some stability may start to return to these markets, and investors may start to find a number of tempting investment opportunities amongst the various commodity types. Crude oil came off its most recent lows and gained 13.3% during the month. Gold also produced a positive performance during January (up 6.8% in US Dollar terms), but unlike oil it is not bouncing off a recent low, but rather approaching its all time high of a little more than USD1000 per fine ounce. In our Focus section we explore the case for investing in gold in times like these.

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

Asset Class Performances

Asset Class Performance (%)	January 2009
US Equities $	-8.5
UK Equities £	-5.8
Cont. European Equities €	-5.8
Japanese Equities Yen	-7.6
Global Equities $	-8.8
Global Emerging Markets Equities $	-6.5
US Bonds $	-3.2
European Bonds €	-1.1
Japanese Bonds Yen	-0.6
Global Bonds $	-4.3
US REITs (property) $	-17.8
FTSE EPRA Real Estate UK £	-21.6
FTSE EPRA Real Estate EU ex UK €	-0.5
FTSE EPRA Real Estate Asia $	-8.8
Euro vs. US Dollar	-7.8
Sterling vs. US Dollar	0.3
Yen vs. US Dollar	0.9
Rand vs. US Dollar	-9.4
Commodities $	-5.1
Agricultural Commodities $	-2.9
Oil $	13.3
Gold $	6.8

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

FOCUS

Gold!

Gold! Gold! Gold! Gold!
Bright and yellow, hard and cold
Molten, graven, hammered and rolled,
Heavy to get and light to hold,
Hoarded, bartered, bought and sold,
Stolen, borrowed, squandered, doled,
Spurned by young, but hung by old
To the verge of a church yard mold;
Price of many a crime untold.
Gold! Gold! Gold! Gold!
Good or bad a thousand fold!
How widely it agencies vary,
To save - to ruin - to curse - to bless -
As even its minted coins express:
Now stamped with the image of Queen Bess,
And now of a bloody Mary.

Thomas Hood (1789 – 1845)

For many centuries gold has fascinated humankind endlessly. It has symbolised many things – it has been used as money, it is a highly sought after precious metal, it enhances the beauty of many a neck or arm (especially around this time of the year…) it is used in sculptures and other ornaments and is seen as a store of value. It also formed the basis for the Gold Standard before the collapse of the Bretton Woods system in 1971.

Investment scholars have debated the virtues of gold as part of a diversified portfolio at length, and in our Focus section we aim to provide some indication of the circumstances under which gold would offer a superior risk return profile to other assets and would therefore add to the efficiency of a diversified portfolio.

First we will look at the correlation of gold price performance with other asset classes. Over the period 1992 to 2008 gold has exhibited very low correlation with any of the other major asset classes. Even during the market volatility of mid 2007 to 2008 the gold price managed to mind its own business by plotting its own way, with correlation to other asset classes increasing, but remaining below 0.5. The table below show the correlation of gold with other assets during these two periods:

	1992 to 2008	Jul 2007 to Dec 2008
US Equity	-0.07	0.20
US Treasuries	0.07	0.46
US Investment Grade	0.10	0.49
US High Yield	0.10	0.49
US Loans	0.02	0.19
US Property	0.24	0.33

With this information at hand we can conclude that gold could add diversification benefits to a balanced portfolio. The question that still remains is whether gold will be able to add to the performance of the portfolio, and how risky is it to invest in gold.

Over the period January 1968 to January 2009 the gold price has increased by 8.4% per annum, with inflation over the same period around 4.7% per annum. The price history can however be divided into three distinct periods. The first period is January 1968 to January 1980, when the gold price increased by an annualised 30.3% to reach USD850 per fine ounce. The next period ended in April 2001, with the decline in the gold price coming to -5.5% per annum. Lastly the gold price increased by 18% per annum from April 2001 to February 2009, in the process going over USD1000 in March 2008 for the first time. Volatility in the gold price has also increased markedly over the last couple of years, with the three year standard deviation moving up from around 13% in December 2003 to 21.5% in December 2008.

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

Source: Bloomberg, January 2009.

The price of gold, like most other commodities, is ultimately driven by supply and demand. Given that most of the gold that has ever been mined still exists in some form or another, and the fact that annual gold output is on the decline, the gathering and disposal plays a large role in the price. This is distinctly different from the pricing mechanism for other commodities.

Of the annual gold production about 80% goes into non-investment uses such as jewellery (68%), dentistry and other industrial uses (13%). The rest is channelled to retail investors and exchange traded gold funds. With slowing economic conditions (even in India, which accounts for about a quarter of the consumer demand), one would expect a decrease in the demand for gold in non-investment uses.

Investor sentiment also plays a large role in the performance of the gold price. If, during times of low or negative real interest rates, investors are not adequately compensated for the risk that they carry in equities, bonds and other asset classes, the demand for gold may increase. This is what happened during the stagflation period in the 1970s when the gold price hit USD850 per fine ounce. Uncertainty about the economic outlook may also increase the demand for gold, which could have a marked influence on the price of gold. If economic uncertainty is accompanied by deflation the role of gold as a store of value is emphasised even more. Many investors would be willing to hold gold as a store of value (without growth) rather than holding equities which traditionally do not fare well when real prices are expected to decrease and dividends are cut or stopped due to a recession or depression.

Many investors fled to the US Dollar as a safe haven during the market turmoil of 2008. The US Government, however, has the ability to turn on the printing presses in order to provide quantitative easing, which would lead to a depreciation of the greenback versus other currencies. Gold, as a safe haven,

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

does not have the same drawback, as gold producers cannot increase the supply of gold in the same way. Gold, viewed in this way, could be seen as the ultimate safe currency, and its value cannot be diluted or manipulated by a government that uses its currency as a tool to manage inflation.

Gold was also used as a safe haven during the Great Depression, Wold War II and subsequent oil crises, and may just prove to be the case in 2007 to 2009. Its price is driven by supply and demand, which in turn depends very much on market sentiment and the extent to which investor demand increases more than the decline in consumer demand.

In conclusion it is fair to say that gold seems to be a somewhat defensive asset from an investor sentiment point of view, but the recent volatility suggests that it could add more risk to a well-diversified portfolio than intended. The fundamental analysis certainly supports the case to purchase gold if investors decide that they prefer a store of value to other risky assets. One concern is however the speed at which investor sentiment turns, as this could have a sudden and sharp influence on the price of gold. The paradox is therefore that gold can easily enough be seen as a store of value, but in reality exhibits more volatility than one would expect from such an investment. For the investor that can stomach the tumultuous ride adding gold to your portfolio in 2009 may just be worth its weight in, yes, gold!

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. January 2009.

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 it is possible that 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 Two London Bridge, London SE1 9RA.

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.