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INDUSTRY OUTLOOK 2011

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The world in 2011 will continue to be a very different place from what it was prior to the Great Recession of 2008. There is likely to be further divergence between the growth paths of developing and developed markets and, within the developed world, economic performance between countries will differ widely.

In terms of the evolution of a two-tiered world, developed economies will struggle with growth and excesses in many forms, while the fast growing emerging world will benefit from sound policies and above trend growth rates.

Global

The big economies, struggling with structural changes, are expected to find that policymakers' tools aren't as effective as they used to be, as we saw with stimulative monetary policy that failed in terms of creating economic thrust and preventing deflationary conditions. And with interest rates at or near zero, there is not much scope for further rate relief.

With signs appearing toward the end of 2010 that the global recovery was faltering, some market participants started pricing in the possibility of a double-dip recession. Peripheral Europe's sovereign risk concerns are a factor in this regard, and in the US the employment backdrop remains weak with further deterioration in the housing market.

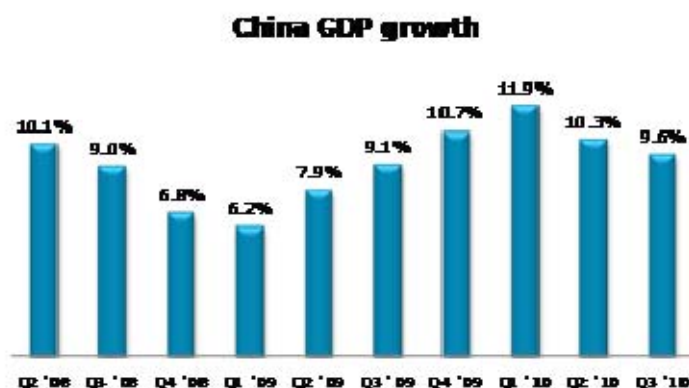
US inflation has been trending lower, notwithstanding expectations that the Fed's easy monetary policy would have been inflationary. Core consumer price inflation has moderated to 0.8% on a year-on-year basis with some models indicating that it could go into

deflationary territory due to the lack of pricing power and excess capacity that persists in the economy.



Although growth momentum slowed and the US employment backdrop remains weak, US consumer spending was resilient towards the end of 2010 when corporate profits remained strong, manufacturing activity continued expanding and consumer spending grew at a steady rate. The fortunes of the US dollar can be expected to continue dominating currency markets.

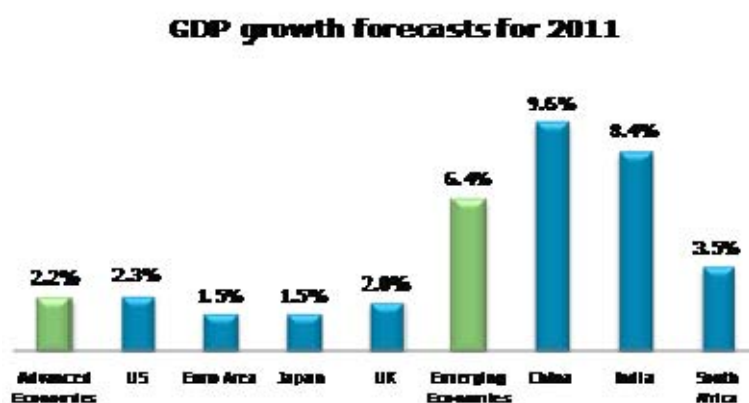
It's a mixed bag in Europe where some growing economies, like Germany, have made up for the weak performance of peripheral Europe where sovereign credit concerns remain. While the Japanese economy has shown some signs on growth, industrial production remains under pressure due to the appreciation of the yen. In China, strong domestic demand and higher industrial production should continue to foster growth.



Decision makers in advanced economies find themselves in unprecedented waters, but their commitment to deal with persistent economic weakness, through additional rounds of quantitative easing or lower for longer interest rates, underscores a positive outlook. The combination of modest growth, very low inflation and highly accommodative monetary policy is not only supportive for equities, but also for emerging markets.

More quantitative easing will ensure that the global economy remains cash-flush and that the search for higher returns remains intact. There is a mountain of cash chasing yield and the fundamental global shift underway from the low-yielding west into the higher growth rest will continue to benefit emerging market assets, both bonds and equities.

The IMF predicts that emerging and developing economies will grow by 6.4% next year while advanced economies are collectively expected to grow by a mere 2.2% over the same period. The chances of a double-dip recession are slim.



Source: IMF, World Economic Outlook October 2010

Growth and inflation in developed markets are likely to remain low and any additional stimulus from quantitative easing will be positive for equities which, from a valuation perspective, are cheap compared to bonds.

South Africa

On the domestic front, economic growth will largely depend on the global arena. The International Monetary Fund predicts that the South African economy will grow by 3.5% in 2011.

Manufacturing activity might struggle over the short term and inflation will continue on a decelerating path, providing the Reserve Bank with an ideal opportunity to cut interest rates. The rand's strength has been a headache and our currency is likely to remain relatively strong.

Novare is bullish on the outlook for equities. Firstly, the equity market will benefit from a record low discount rate with the possibility of further declines. Secondly, South African companies are experiencing a recovery in earnings, with growth expected to exceed many other emerging market economies. Thirdly, the share market is trading on an attractive forward valuation when taking into account expected earnings growth. And lastly, the domestic equity market is under owned, not only by foreign investors in relationship to their emerging market benchmark, but also by domestic asset managers when you look at pension fund assets.

The domestic bond market will benefit from the improved fiscal position, strong global demand, low international bond yields and the relative attractiveness of domestic bond yields compared to other emerging market bond yields. A further interest rate cut would contribute even further to the domestic bond market's return. Listed property will benefit from the lower interest rate environment and improved income growth.

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