



NEWS RELEASE

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A CREDIBLE PLAN FOR EUROPE COULD SEE A SUSTAINED RALLY IN EQUITIES

The rally experienced by global markets this week, following progress in dealing with the persistent euro-zone sovereign debt crisis, could be sustained if European authorities support what appears to be a good plan with workable detail on solving the debt crisis and recapitalising beleaguered banks.

Commenting in his economic report for the third quarter of 2011, Francois van der Merwe, Head of Macro Research at Novare Investments, said: "The world has been gripped by fears of a total meltdown in the euro-zone banking system, and the possibility of a renewed global recession.

"But some recent economic data have been surprisingly upbeat, indicating that economic conditions might not be as grave as initially thought. Although not overly cheap, shares are looking fairly attractive. While there are heightened global macro risks, most of these have already been priced into shares. Company earnings will come under pressure, but we still believe that they will be able to show positive earnings growth."

He added that global bonds had benefitted from risk aversion and the flight to safety with yields on US Treasuries, for example, pushed to all-time lows.

"While central bank policy, lower economic growth rates and an inflation slowdown might all support lower bond yields, we feel that 10-year government bond yields close to 2% do not reward enough for holding the instruments for the expected duration. Also, we take into consideration that equity dividend yields are currently in excess of bond yields. Over the next twelve months, we believe equities will outperform bonds."

On the domestic front, van der Merwe said the South African economy would not be spared the effects of the global growth slowdown. Growth projections have already been revised

down and it is mostly the cyclical sectors of the economy that will be affected, while defensive sectors are expected to remain resilient.

Interest rates are likely to remain unchanged over the next twelve months, even though inflation might breach the upper limit of the Reserve Bank's targeted band before trending down again.

"A slowdown in global growth should help contain some inflationary pressures, but it remains to be seen what effect the depreciation of the rand will have on imported inflation. The rise in administered prices and wages will continue to weigh on inflation, while the rand's recent and sudden weakness again illustrated the importance of offshore diversification," he said.

From an equity market valuation perspective, van der Merwe said the FTSE/JSE All Share Index is probably the cheapest it has been in the last two years. "While it might get even cheaper, we believe it is attractively valued, given that company earnings should continue to show double digit growth. And the domestic equity market should be supported by the Reserve Bank's accommodative monetary policy stance."

The South African bond market will find support from the global growth slowdown, low interest rates, and an attractive yield differential compared to other countries' bond markets. It is, however, vulnerable to upside risks from inflation, global risk appetite and fiscal slippage.

Over the next 12 months, bonds should outperform cash, which is expected to provide a very low return above inflation.

Said van der Merwe: "The short-term outlook for financial markets is continued volatility and an increased risk of policy and political errors. We are, however, confident that officials will find the necessary solutions to stem the tide, but we are mindful that because global structural issues will take an extended period to unwind, many developed economies will continue to face headwinds in the years to come."

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Note: Novare Investments' Third Quarter Economic Report can be obtained at www.novare.com