



# INSIGHT

Investment perspectives from the Harvard House Group

## BULLS, BEARS & BAGUETTES

Taking stock of market conditions

Michael Porter

Harvard House Investment Management

July 2014



# Markets are still expensive

In absolute terms, the PE is at the top end of its historical range

## JSE All Share Index – PE Ratio



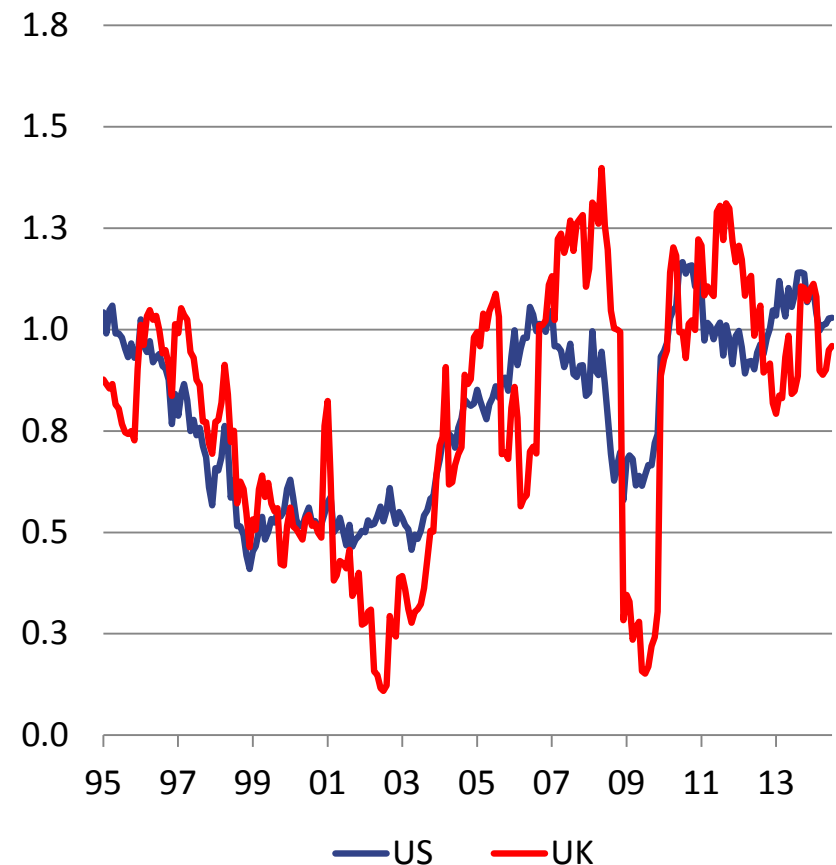
# The JSE compared to its peers

Expensive relative to other EM, but in line with DM

### PE: JSE rel to MSCI EM



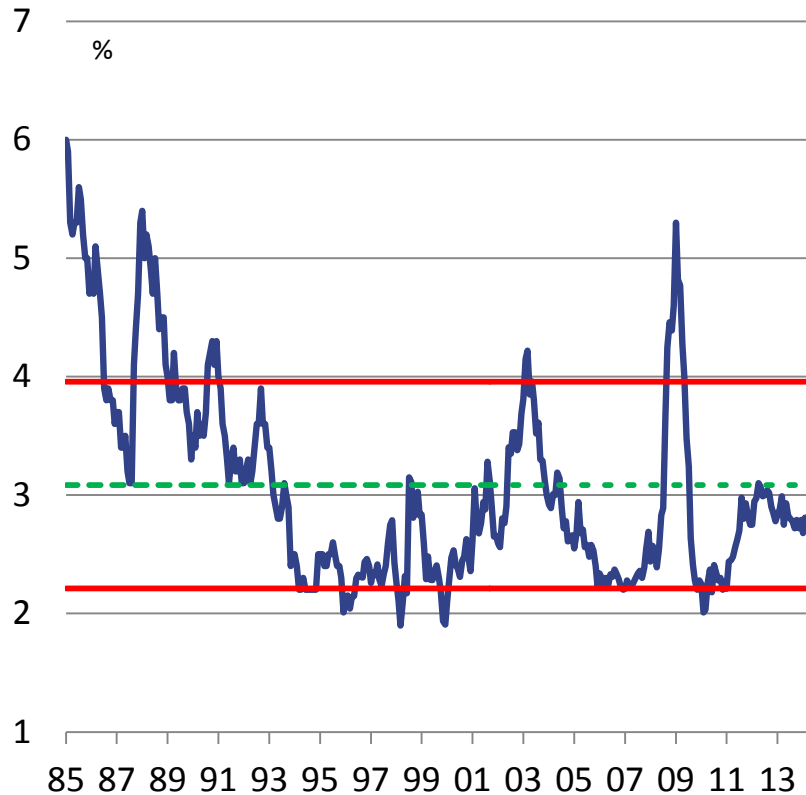
### PE: JSE rel to US / UK



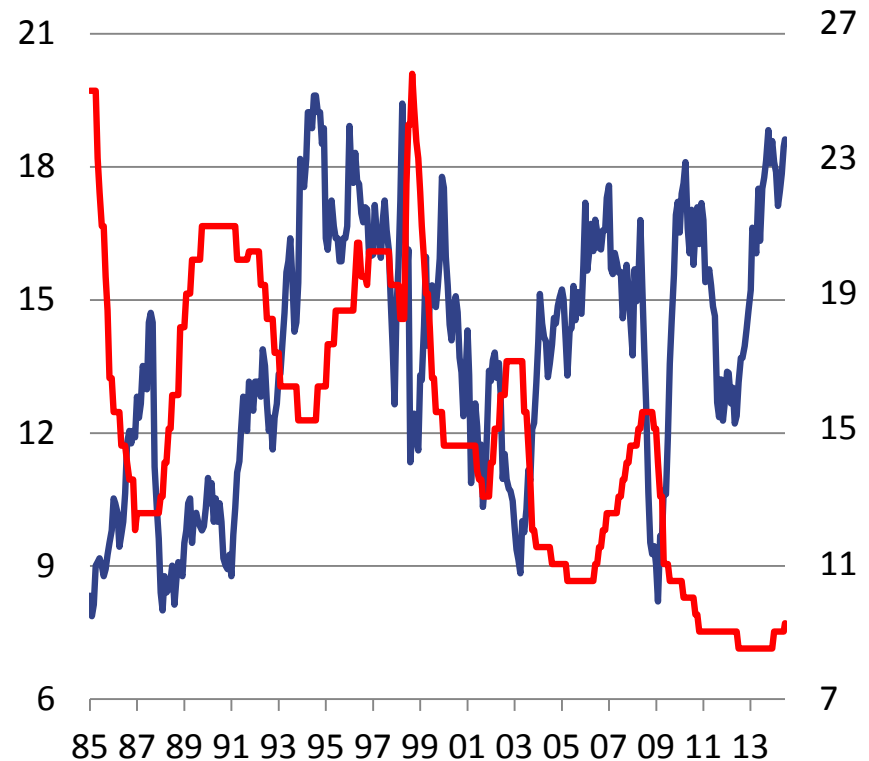
# Can the high PE Ratio be justified?

Expensive relative to other EM, but in line with DM

## JSE Dividend Yield



## PE & Interest Rates



— JSE PE (Left) — Prime Rate (Right)

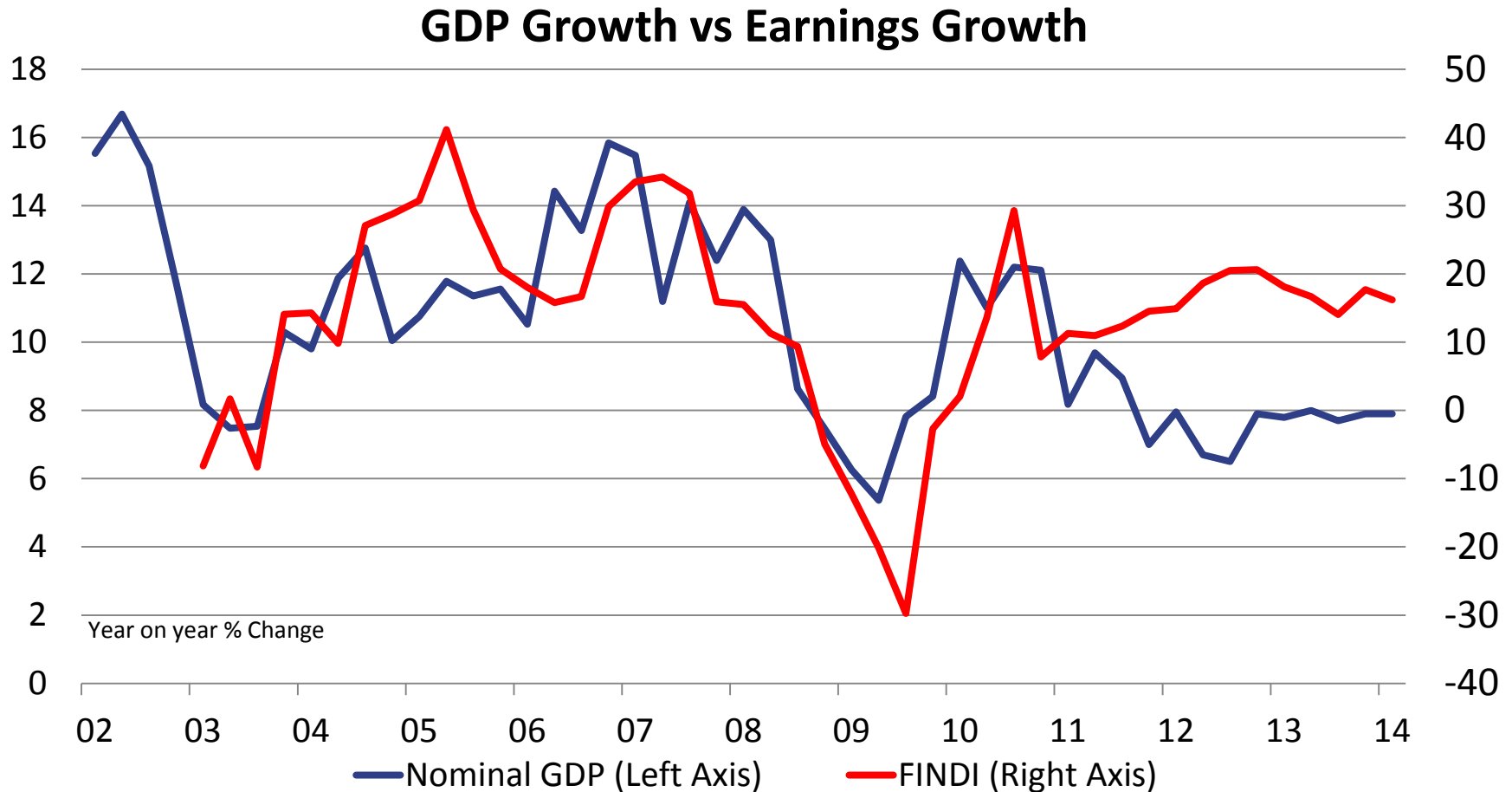
# Analysing returns for 2014

Returns in SA have been driven by earnings growth, not valuations

	JSE All Share	UK FTSE 100	US S&P 500	MSCI EM
Total return (YTD)	12.2%	1.1%	7.6%	7.3%
Proportion of Return from:				
- Rising profits	10.4%	-13.1%	0.7%	-8.9%
- Rising PE Ratio	0.2%	12.2%	5.8%	14.5%
- Dividends	1.6%	2.0%	1.2%	1.6%

# Earnings Growth & GDP

Is earnings growth possible given the state of our economy?



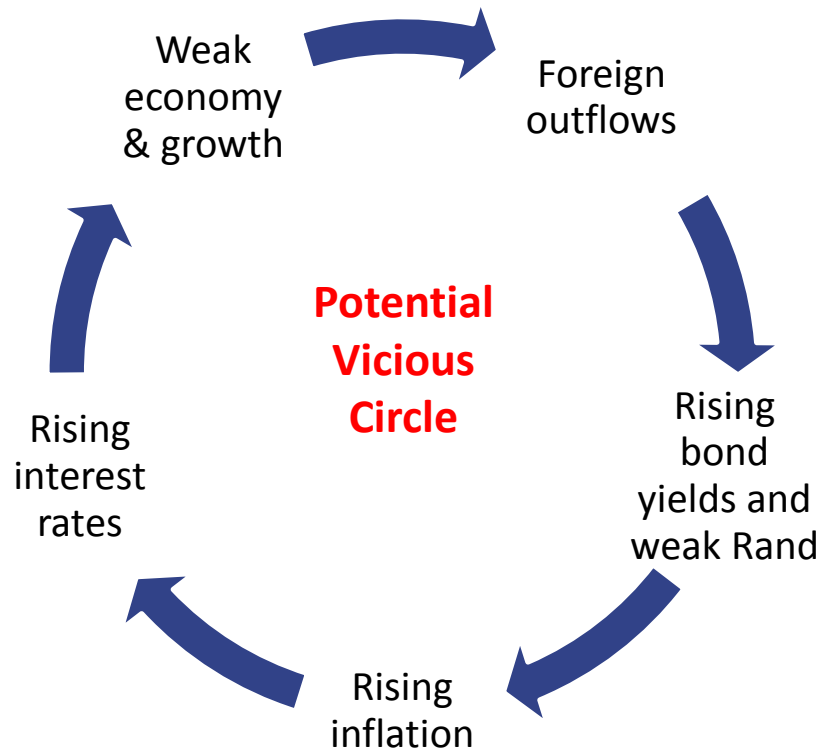
# SA Companies are diversifying

Local companies are externalising in search of growth

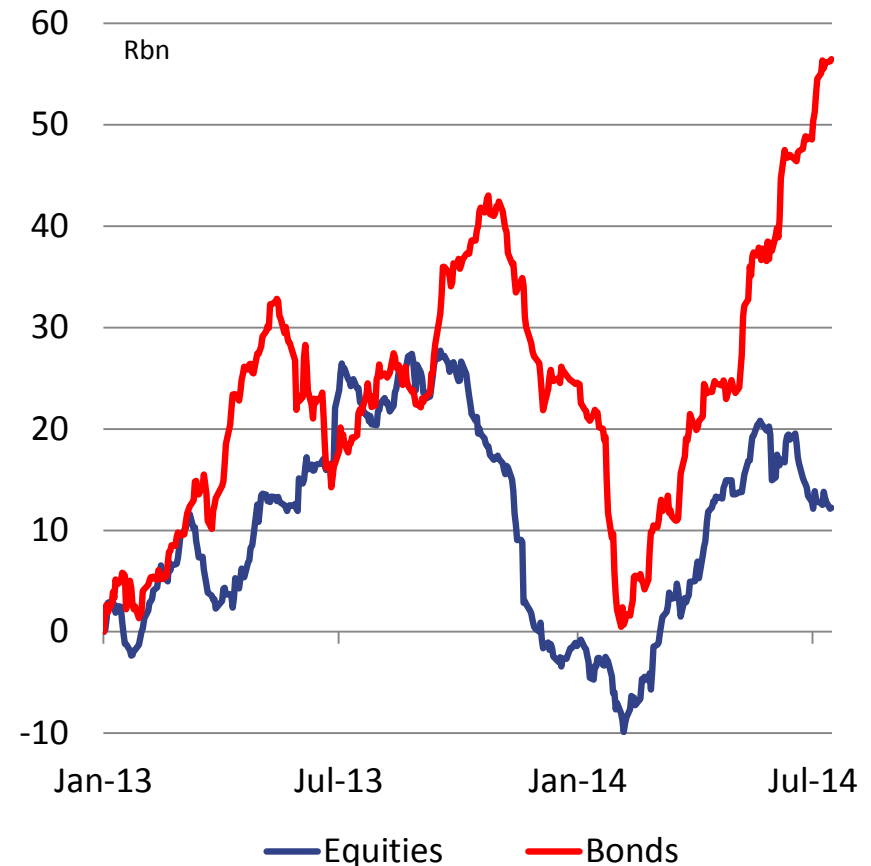
% of Revenue from Outside SA	2010/11	2013/14	% Increase
Aspen	47%	70%	49%
Barclays Africa	0%	14%	-
Bidvest	47%	56%	19%
Growthpoint Properties	9%	25%	178%
Mediclinic Group	55%	63%	15%
MTN Group	69%	71%	3%
SABMiller plc	74%	85%	16%
Shoprite Holdings	11%	13%	18%
Steinhoff International	60%	70%	17%
Tiger Brands	10%	25%	150%

# What is on our minds?

Is South Africa facing a potential Credit Rating downgrade?



## Foreign Investment in SA





# Other local issues

Cogs in the wheel that will determine near term direction of markets



Pressure on consumer spending

- interest rates
- Electricity costs
- Strikes (no work no pay)



Government finances & future tax increases



Wage growth post strike season

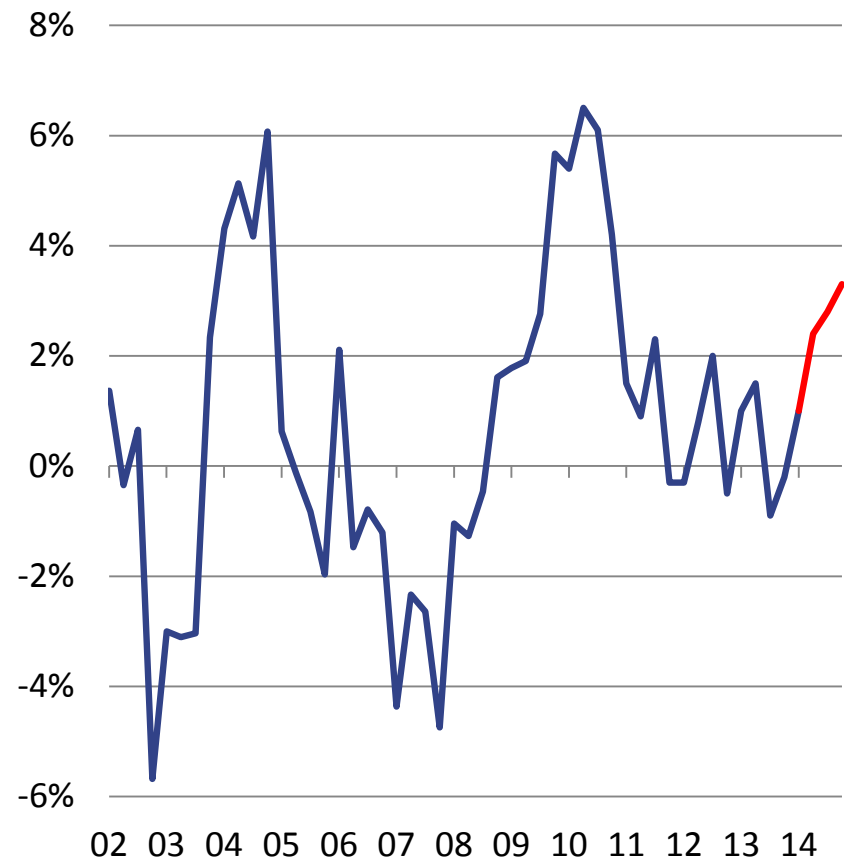


Accelerating global growth



Medium Term Budget and ANY progress on NDP

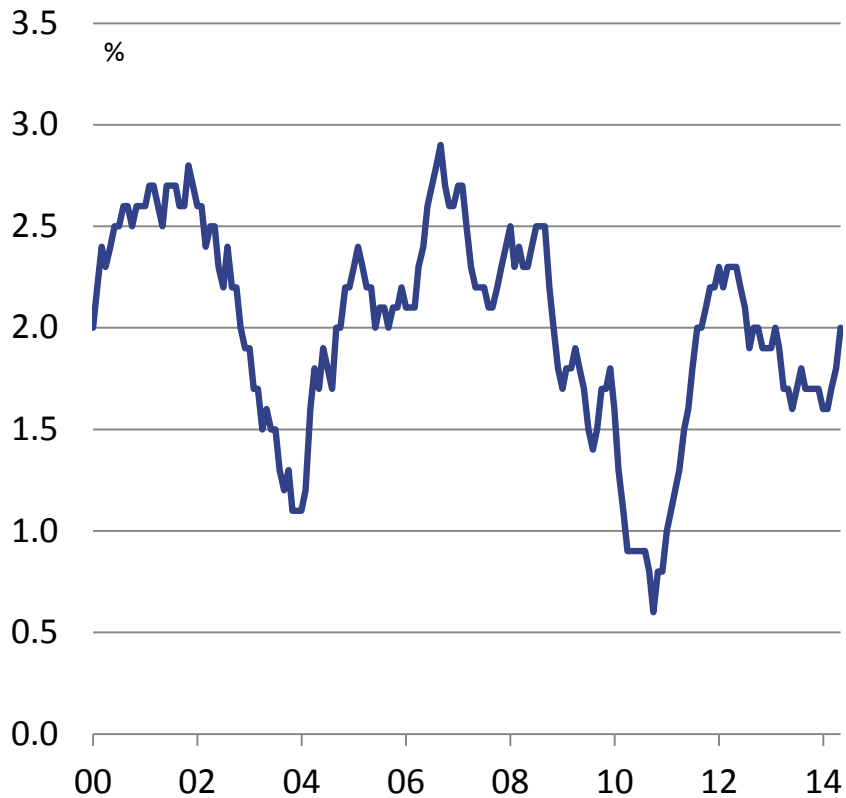
## Real Wage Increases in SA



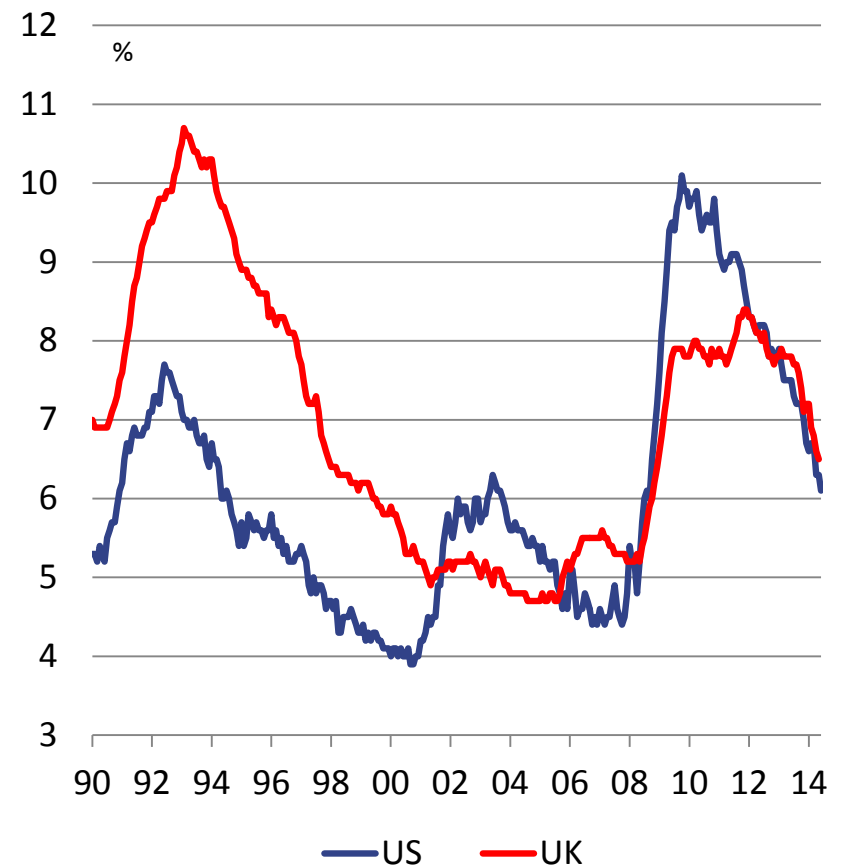
# The elephant in the room

When will developed countries start raising interest rates?

## US Inflation







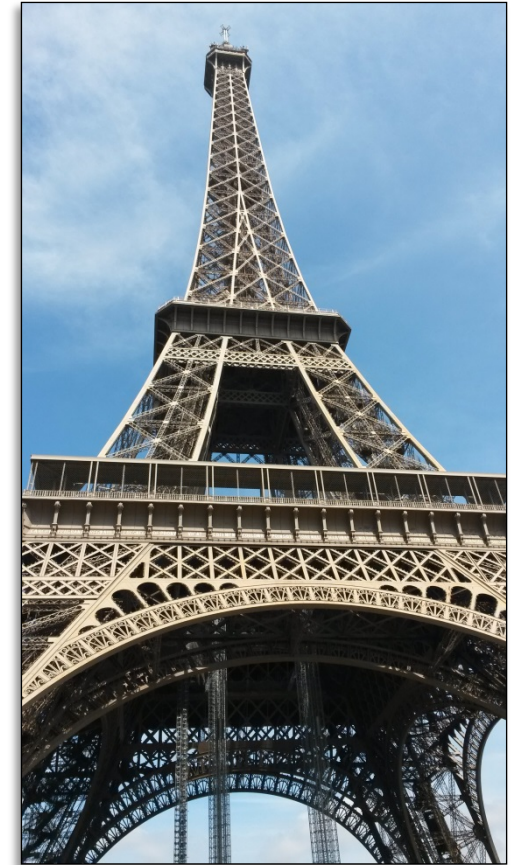
## Unemployment Rate



# Insight from offshore

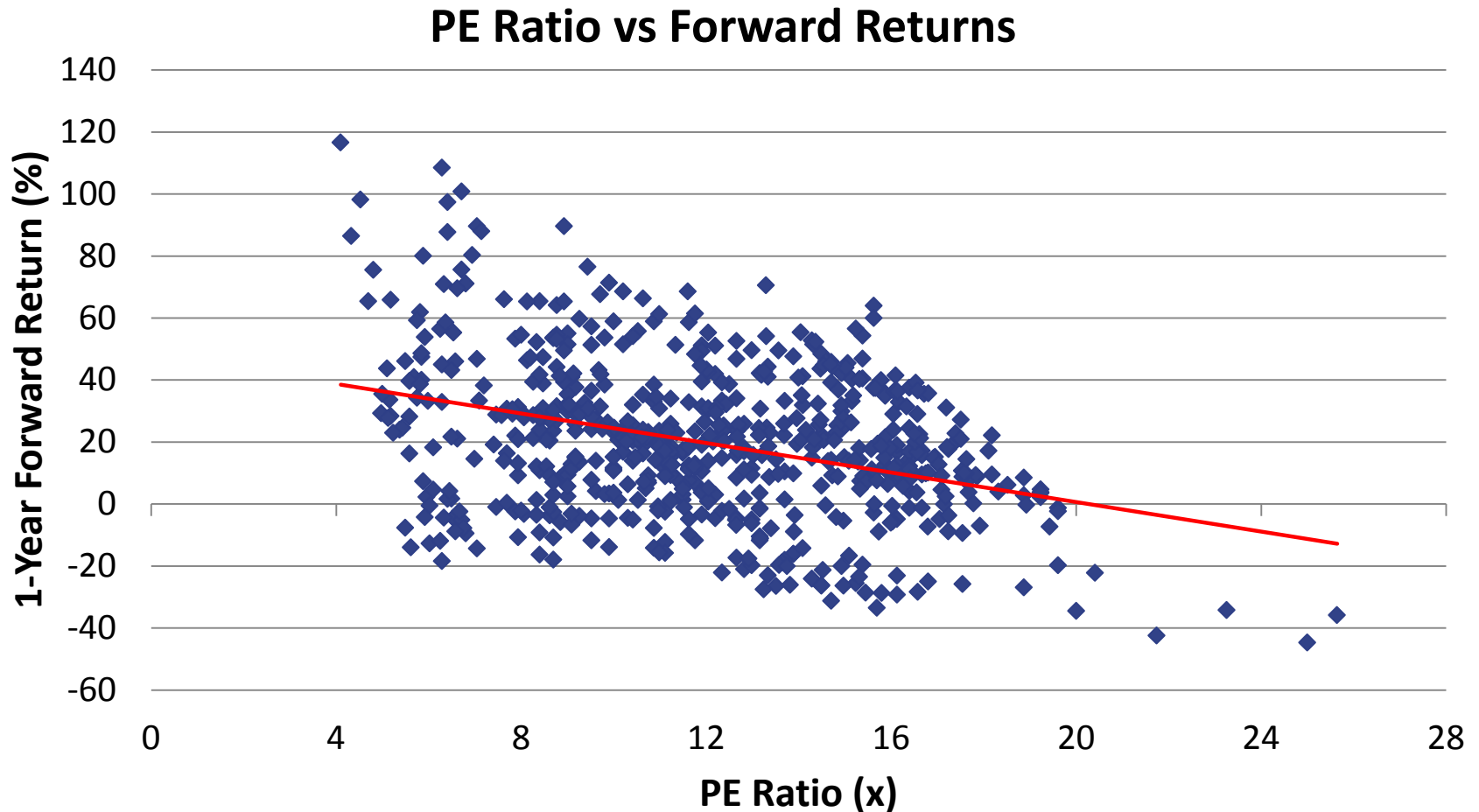
The mood was downbeat

-  **Downbeat mood**
  - Conditions are tough
  - Run hard to stand still
-  **Currencies are playing havoc with reported results**
-  **But secular growth drivers of higher global consumption remain firmly intact:**
  - Emerging markets remain growth engine
  - Positive population dynamics
  - Wealthy middle class
-  **Intense focus on:**
  - growth through innovation, and
  - Reducing costs through productivity (It, logistics)



# The big picture: valuations and returns

Entry point is important for successful investing



# Putting it all together

A summary of our views for the next six months

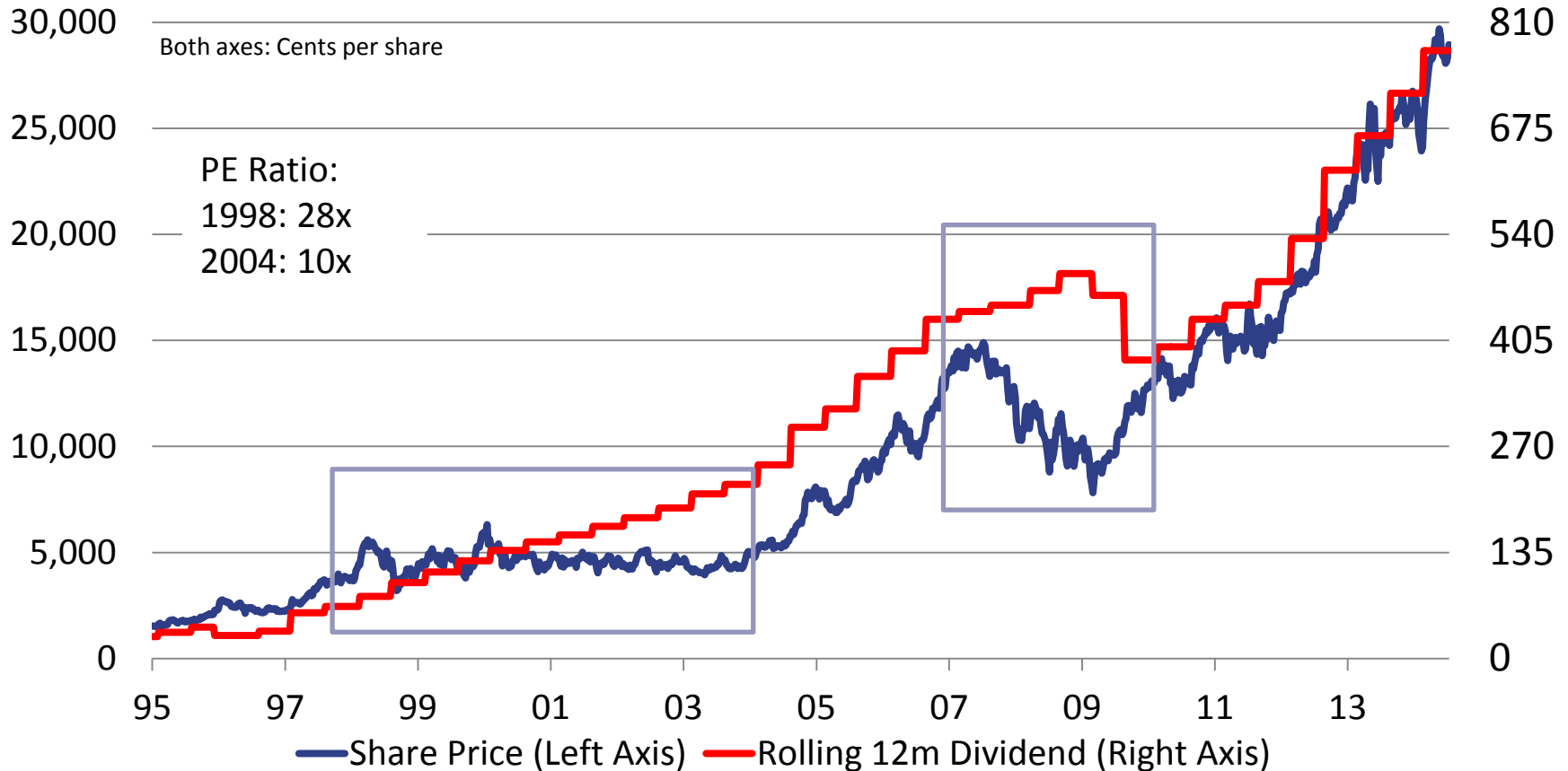
-  In absolute terms, markets are high
-  Short term direction is highly dependent on profit growth. Reporting season will set the tone.
-  Random events can often be catalyst for a sell-off (Ukraine, Middle East etc)
-  What action are we taking:
  - Cautious. No need to rush in
  - Take profits where there are excessive returns
  - Have some cash available should markets fall.



# HH Investment Philosophy

Income comes into its own during stagnant markets

## Bidvest: Share Price & Annual Dividends





# INSIGHT

Investment perspectives from the Harvard House Group

## Q & A

Please feel free to ask questions

Thank you for listening