Financially Talking

October 2009

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OLD MUTUAL

Time to review your investment portfolio

Pieter Hugo
MD, Old Mutual Unit Trusts

Investors are undoubtedly facing some extremely challenging decisions. As I communicated in our January edition of Financially Talking, when markets rally, they tend to do so rapidly. The Johannesburg Securities Exchange (JSE) has been no exception – after falling over 40% to its lows in February 2009, it has already rebounded some 37% (as at 30 September 2009).

While this is good news for those who remained invested in the markets through what's been called the "subprime crisis", it is important to realise that this rise does not take your investments back to square one. Briefly, if you invested R100 and it lost 40% of its value, your remaining R60 would need to grow by 66% to get back to R100. That is why it can often be detrimental to move out of shares after the market has fallen: ironically, the stock market offers the best place, over time, to regain these losses as historically it has proven to be the growth engine of our investment world.

Sadly, throughout this period many investors abandoned those unit trusts that have exposure to shares, with 57% of new investments going into fixed interest funds. Money market funds remained the most popular fixed interest funds and while they should form part of a well-diversified portfolio, they are not designed to provide long term growth significantly in excess of inflation. And, while many investors have benefited from abnormally high real interest rates in South Africa in the recent past (read Peter Brooke's article on page 4), our view is that this will not necessarily be what the future holds for us.

As anticipated, the SA Reserve Bank has been trying to stimulate the economy, cutting interest rates by five percentage points since December 2008. With interest rates now at ±7% and inflation currently running at 6.4%, the real return of cash is close to zero.

After significant events over the past year, like declining inflation, interest rate cuts and the fall and subsequent partial recovery in the stock markets, it is now an appropriate time for investors to assess whether their current investments are correctly positioned to achieve their objectives.

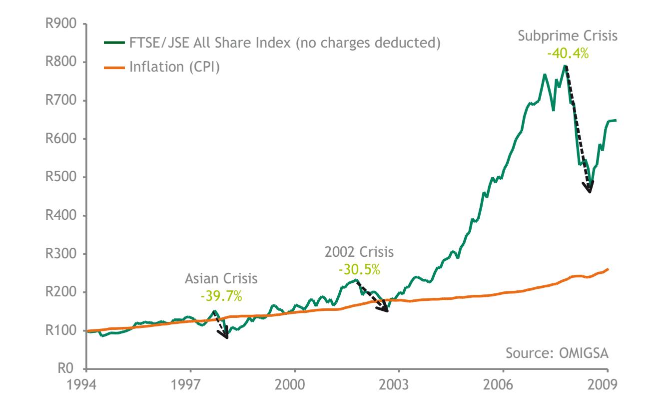
Stimulating the economy by lowering interest rates

Lower interest rates mean less of one's income goes towards paying off debts – leaving more money to spend on goods and services. This increased demand for goods and services is one way lower interest rates boost the economy. However, lower interest rates have other consequences... one being that the returns earned on money market funds drop in line with the rate at which banks lend out money.

While many investors shy away from shares because of the major falls experienced in the markets from time to time, all evidence points to the importance of including (some) shares in your portfolio. To illustrate this, we calculated that a R100 investment in our stock market, made 15 years ago, would have grown to R665 by the end of September 2009. That's a return of 13.5% a year (vs. average inflation of 6.5%) over a period that experienced:

- The Asian crisis: Our market fell 39.7% and took 19.5 months to recover to pre-crash levels (30 April 1998 to 15 December 1999).
- The 2002 crash: The market fell 30.5%, taking 20 months to regain its value.
- The 2008 subprime mortgage crisis: We experienced a drop of over 40.4% from May 2008 to February 2009. With the recent recovery, the cumulative loss from May 2008 to 30 September 2009 was 18.2%.

R100 invested 15 years ago
(30 September 1994 to 30 September 2009)



Time to review your investment portfolio (continued)

It is extremely difficult to try and time the investment markets. One of the biggest advantages of investing in unit trusts is that you can let the experts make those difficult asset allocation decisions on your behalf. With these “asset allocation” unit trusts, the fund manager decides on the exposure to the various asset classes, like shares, listed property, bonds and cash. As market conditions change, the fund manager will increase or reduce exposure to the various asset classes to achieve the fund’s objectives over the long term.

Where do the income investors go?

For income investors unable to tolerate any volatility (ups and downs) in the capital value of their investment, money markets remain a good option. However, as I’ve explained previously, the risk these investors face is that their investment growth may not outpace inflation over time, especially if they draw an income.

There are alternative income-focussed funds available that seek to offer a relatively high, sustainable level of income as well as opportunities for capital gains. One such fund is the Old Mutual Enhanced Income Fund, which aims to deliver this via controlled exposure to instruments like inflation-linked bonds, preference shares, property and other bonds.

With the wide range of unit trusts available to investors, you can find the one that best matches your risk and growth/income needs. The table below shows a sample of funds that we offer. Note how the funds that place greater emphasis on providing an income hold a higher percentage of their portfolio in money market instruments. As the focus on growing capital increases, so the component invested in shares rises.

Did you know?

The Old Mutual Money Market Fund was ranked in the top quartile over 1, 2, 3 and 5 years to 30 September 2009. It remains an excellent parking bay for short term investors, or those seeking to maximise income without any capital volatility.

Fund portfolios as at 30 September 2009	Fund Category	Money Market/ Cash	Bonds	Listed Property	Shares
Old Mutual Money Market Fund Aims to provide a high level of income with no capital growth or loss.	Fixed Interest - Money Market	100%	-	-	-
Old Mutual Enhanced Income Fund Aims to provide an income with some capital growth.	Fixed Interest - Varied	65%	30%	1%	4%*
Old Mutual Stable Growth Fund Aims for moderate capital growth with some income.	Asset Allocation - Low Equity	21%	33%	8%	38%
Old Mutual Balanced Fund Aims for a higher level of capital growth with some income.	Asset Allocation - Medium Equity	9%	12%	8%	71%

*Preference shares

If you are unsure how to structure your portfolio to ensure that you meet your financial needs, I recommend you speak to your Old Mutual Financial Adviser or your broker. But whatever your financial needs, rest assured that there is a fund, or combination of funds, to suit your needs.

Past editions of Financially Talking can be found under the Media Centre at www.omut.co.za.

Economic recovery delayed until 2010

Rian le Roux
Chief Economist at Old Mutual Investment Group (SA) (OMIGSA)

As we lag the global cycle, the near term prospects for South Africa's economic growth remain relatively weak. Although signs of stabilisation are mounting, I believe our economy is unlikely to see a decent recovery until next year.

We had expected a stronger recovery in the second half of this year, but it now looks as though the headwinds facing our economy are more daunting than initially anticipated.

Headwinds:

- Sluggish global growth;
- Inflation has remained higher for longer;
- Consumers' finances continue to be under pressure;
- The strong rand is hurting our manufacturing and mining exports; and
- The benefit of lower interest rates (i.e. more money in the system) is partially offset by tight bank lending standards and higher public sector (education, municipal and electricity) charges.

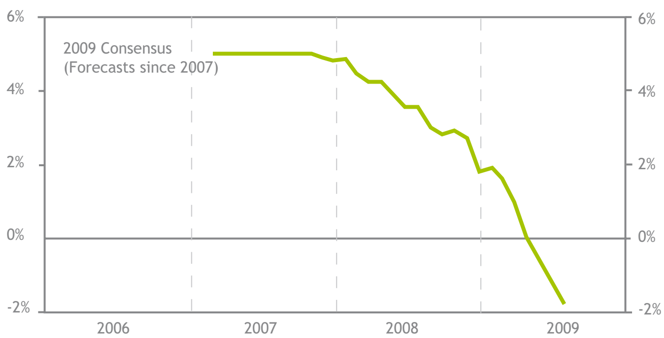
Cost increases, plus high wage settlements, are also putting pressure on the medium term outlook for inflation (CPI). Although we have recently seen some declines in raw food prices and the strong rand has helped keep import prices lower, CPI looks unlikely to fall within the Reserve Bank's 3%-6% target band this year. Nevertheless, I expect the gradual downtrend to continue, and we could see a low of just above 6% in the latter part of the year.

As a result of these headwinds, we are expecting a reduction in economic growth with gross domestic product (GDP) falling by around 2.0% this year, and a recovery of about 2.0% next year (this forecast includes the likely positive impact of the World Cup).

With growing concerns among both local and foreign investors about South Africa's true longer term growth potential, the new government will have to take tough and decisive action as a matter of urgency to address the obstacles to higher growth and job creation in South Africa over the medium to longer term.

On the positive side, there have been some signs of stabilisation appearing in our economy. Car and commercial vehicle sales are showing some improvement, and electricity production and new manufacturing orders from purchasing managers (as reflected in the Kagiso Purchasing Managers Index) have also picked up. And the effects of the cumulative 5 percentage point cut in interest rates have yet to be fully felt by consumers and businesses, which should help bolster the economy in the coming months.

2009 GDP FORECASTS – REVISED SHARPLY LOWER



Source: OMIGSA, IRIS

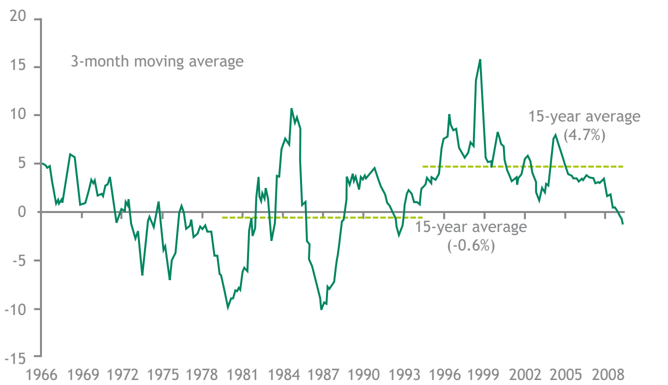
In the quest for income, don’t bet against the world recovery

Peter Brooke
Portfolio manager of the Old Mutual Stable Growth, Real Income and Flexible Funds

With real interest rates both locally and globally expected to remain unattractively low (and even negative) for quite a long time, it’s a mistake for investors to continue to bet on cash to grow their capital ahead of inflation.

Instead, as economic growth slowly reappears around the world, growth assets should remain at the core of investors’ portfolios, as they offer by far the greatest chance for the best real returns over the near and longer term.

Real SA Cash Yields



Source: OMIGSA

In South Africa now, our effective real (above inflation) interest rates are near zero, with inflation at 6.4% and cash at $\pm$7.0%. Cash (money market) yields are now below those of bonds and property for the first time in 3.5 years. Historically our real cash yields have been phenomenally high, averaging almost 5% over the past 15 years (refer to the graph above). But those days are gone: over the next couple of years real interest rates will be closer to 2%, which is more consistent with international trends.

The devastating impact of these low interest rates on existing savers cannot be ignored, particularly because they are used to receiving fat returns on a relatively low risk investment. These investors will have a desperate need to augment their cash yields, by adding other asset classes like bonds, property, preference shares or equities. If an investor risk profile allows, investing in shares is still a good option for those with a longer investment horizon, whether that is via higher risk unit trusts fully exposed to shares or via those unit trusts only partially invested in shares, like balanced or defensive funds.

The days of high real money market yields are over.

Our stock market has already posted some good gains since its low point in March 2009, and is now above its historical average in terms of valuations. Although it is still likely to produce attractive real returns over the medium to longer term the market is no longer cheap. We are forecasting a 7% real return from local shares over the next five years. This is somewhat lower than the 8% we expected at the beginning of the year (Financially Talking, January 2009) reflecting the selective value available in the market.

This forecast incorporates my concerns around the ability of South African corporates to grow their earnings as strongly into the future, due largely to soggy global growth and the much higher earnings base they are working from.

Still, recent data shows the global economy is already starting to stabilise as the unprecedented policy stimuli from governments take effect. It’s clear that the system is unclogging. Banks are lending more, investor risk appetite is improving and consumers are starting to benefit from low interest rates. Internationally, there is a wall of uninvested cash waiting to find a home since real cash yields are so unattractive, which will support stock market recoveries. Sitting in cash could be an expensive mistake.

Real interest rate
This is the interest rate earned minus the inflation rate (e.g. an interest rate of 7% minus an inflation rate of 6% equals a 1% real return).

Offshore shares also look more attractive than the local market, due to their current cheap valuations relative to historic levels. I am expecting an 8% real return from this asset class over the next five years, with a preference for emerging markets given their stronger economic growth prospects. Foreign shares have been the worst performing asset class over the last 10 years and many investors are starting to give up on it. This would be a mistake.

REAL RETURNS EXPECTED OVER NEXT FIVE YEARS

Investment Type (asset class)	Real Return	View	Comment
SA Market		N	
Equity	7.0%	N	Good long term real return. Concerned about real earnings growth.
Property	6.0%	+	High yield of 9% but expect tough 18 months. Longer term winner.
Bonds	3.0%	N	Looking interesting in the next year but longer term concerns about inflation.
Cash	2.0%	–	Lower real returns in next decade. Negative after tax.
Offshore Market		N	
Equity	8.0%	+	Cheap compared to history. Prefer emerging markets in long term.
Bonds	2.0%	–	No inflation risk in short term, but low nominal returns.
Cash	0.0%	–	Downgraded as rates fall sharply.

N = Neutral + = Positive – = Negative

The prospects for **local property** shares have deteriorated in recent months due to falling property valuations and tenant troubles. I expect a rough 18 months ahead for the sector. However, over the longer term property remains a valuable asset for a portfolio, with its forecast yield of 9% underwriting a real return of 6% over the next five years.

Meanwhile, **bond yields** have improved due to the recent sell-off and should produce a real 3% return over the next five years, just ahead of cash. Investment-grade corporate bonds are more attractive, although they are much less liquid. And cash, with a projected real return of only 2% through 2013, is of least preference for a portfolio.

Investors need to understand that returns from most asset classes, but especially cash, will be lower for the foreseeable future. This is also a concern for defensive funds*, which can hold more than half their assets in cash. To compensate for this and meet their long term return goals, investors will be forced to take on more risk, or they need to reduce their income and return expectations and make lifestyle changes.

It's important for you to take a longer term view and recognise that you need to consider investing in a unit trust which exposes your money to higher return assets, more than ever before.

* Prudential Low Equity category as at 31 March 2009

Communication update

Did you know that you can opt to receive your correspondence via email? This means you receive your statements sooner and, by avoiding the use of paper, enables us to be kinder to the environment.

If you want a more frequent update on your portfolio or to review completed transactions, you can log on to our secure site and check on your account. You can also transact online and access different reports, including capital gains tax and income statements. Visit www.omut.co.za and click "register" at the top of the page to enjoy the convenience of managing your portfolio online.

Keep it up to date

Please ensure that we have your correct cellphone number and other personal details on record, and remember to inform us whenever they change. This will help to ensure that you always stay in touch with your investments.

Get what you want

- Call 0860 234 234 (+27 21 503 1770) to speak to our skilled client service consultants during office hours or obtain investment values via our automated system (any time of the day or night). Remember to have your account number on hand.
- Visit us at www.omut.co.za to view and transact on your portfolio, get detailed fund information or download our transactional forms (to buy, sell or switch units).
- Fax your requests or completed forms to +27 21 509 7100.
- Email queries to unittrusts@oldmutual.com (we respond within 24 hours).
- Visit your nearest Old Mutual branch and speak to one of our accredited financial advisers.

Getting a head start really pays

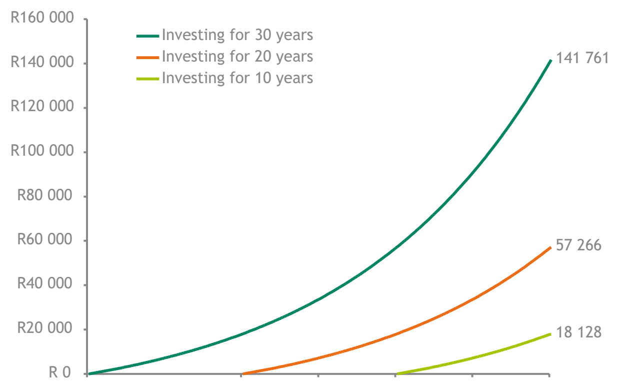
Did you know that when investing, your money is working for you… through a simple concept called compounding growth?

Compounding simply means making money on your original investment as well as on the gains made in following years (i.e. growth on growth over time). For example, if you invested R1 000 at a growth rate of 10% a year, it would be worth R1 100 at the end of the year. If you reinvested that extra R100, the following year's earnings would be based on the original R1 000 as well as on the R100 and so on.

Investing on a regular basis puts you in an excellent position to secure your future financial wellbeing and maximise the time spent in the market. A simple concept, yet it is only effective over the long term. Take a look at the graph of three R100 monthly investments started at different times, but all growing at a flat 8% a year.

While the contributions over the 30-year period were three times more than over 10 years, thanks to compounding the investment grew to be worth over **seven** times more!

The powerful effect of investing over the long term
R100 a month growing at 8% a year



Source: OMIGSA

Grow your wealth through a monthly investment plan

Few of us are lucky enough to have a lump sum handy to invest in the market today. But investing smaller amounts over time can be just as effective a way to build wealth, without making too dramatic an impact on your budget. Investing on a regular basis also eliminates the need to try and time the market as you benefit from rand cost averaging – buying more units when markets are cheaper and fewer units when prices rise. By practising this strategy you can enjoy all market conditions – as a falling market provides a good buying opportunity and a rising market sees the value of your investments increase.

Unit trusts offer you the flexibility to change your monthly investment as your circumstances change – without you incurring penalties. We also offer the option to have your debit order amount automatically increased each year, helping you combat the ravages of inflation.

Increasing your debit order in line with inflation has a huge impact on the final value of your investment. While R250 invested for 10 years would have grown to R45 321 today (assuming 8% growth), the same monthly debit order automatically increasing by 6% a year would have grown to R57 576 (with a current investment amount being R422,37 a month). So if you have not reviewed your debit order in a while, ask yourself if your investments are keeping pace with inflation.

For your convenience, we have enclosed a debit order investment form with your account statement. Alternatively, you can call us at 0860 234 234 to add to or amend your current monthly investments.

TAKE ADVANTAGE OF OUR SPECIAL OFFER

You can invest in any of our equity or asset allocation funds from a monthly minimum of R250 (normally the minimum monthly investment is R500 a month). This offer is valid until 31 January 2010 and is only available to our existing clients.

Use this opportunity to add a new fund to your existing portfolio or save for a goal like your children's education.

For information on our range of funds and the investment details of each, please speak to your financial adviser, visit www.omut.co.za or call us at 0860 234 234.

And **remember!** The best time to start investing is **today.**

New funds available

In 2008 Old Mutual purchased a majority stake in Futuregrowth Asset Management. Merging the strength of the Old Mutual Investment Group's existing fixed interest capabilities with those of Futuregrowth resulted in the largest fixed interest capability in the country. The success of this merger is further evident in the performance track record of the funds they manage*.

Combining these businesses also resulted in us expanding the wide range of funds offered by Old Mutual Unit Trusts. The following funds are now available to you and their performance track record is included in the table on your right.

The Futuregrowth Albaraka Equity Fund, a joint venture with Albaraka Bank, is managed in strict accordance with Shari'ah (Islamic) law. The fund seeks to provide medium to long term outperformance of the FTSE/JSE Shari'ah Index.

The Old Mutual Active Quant Equity Fund invests in a range of shares with the aim of providing capital growth and a higher return than the average general equity fund. It is managed using a proprietary quantitative investment process.

The Old Mutual Futuregrowth Global Index Fund of Funds invests in a spread of international index funds across the globe. It aims to provide investors with a return corresponding to the return of the Morgan Stanley Capital International (MSCI) World Index.

For more information on these and other funds speak to your broker or Old Mutual Financial Adviser. Alternatively you can find information at www.omut.co.za or you can speak to one of our client service consultants at 0860 234 234.

* Over one year to the end of September 2009 the Old Mutual Bond Fund ranked 9/17, the Old Mutual Income Fund 1/3 and the Old Mutual Money Market Fund 4/22.

Fund	TER# (%)	Performance % p.a. 1 year	3 years	5 years	Risk Rating
Active Quant Equity Fund A	2.50	8.2	6.6	17.7	4
Balanced Fund R	1.30	7.3	7.3	15.8	3
Bond Fund R	0.87	9.3	7.8	8.3	3
Capital Builder Fund A	0.92	10.9	-	-	2
Dynamic Floor Fund A	1.01	9.6	8.2	12.1	3
Enhanced Income Fund A	1.14	10.2	9.8	10.7	2
Financial Services Fund R	1.15	15.9	7.8	18.5	5
Flexible Fund R	1.38	10.9	8.9	18.0	4
Four Plus Capital FoF A	2.23	8.4	7.4	9.5	3
Four Plus Global FoF A	2.39	-2.4	-2.0	8.9	4
Four Plus Growth FoF A	2.00	6.8	5.5	13.4	3
Four Plus Secure FoF A	2.05	9.0	8.6	7.5	2
Futuregrowth Albaraka Equity Fund A	1.72	6.7	0.3	13.9	5
Futuregrowth Global Index FoF R	1.48	-12.7	-4.1	6.7	4
Global Bond Feeder Fund A	1.73	8.1	6.2	8.8	2
Global Equity Fund A	2.09	-16.4	-9.4	4.8	4
Global Technology Fund A	2.53	5.7	-1.4	6.3	5
Gold Fund R	1.15	8.6	-0.2	9.6	5
Growth Fund R	1.14	12.6	11.2	20.3	4
High Yield Opportunity Fund A	1.41	15.4	6.9	16.8	4
Income Fund R	0.86	11.2	10.1	9.1	1
Industrial Fund A	1.40	12.5	10.4	19.4	5
International Growth FoF A	2.89	-8.5	-5.6	5.3	4
Investors' Fund R	1.12	8.6	7.8	18.4	4
Mining & Resources Fund R	1.14	0.9	13.5	27.4	5
Money Market Fund A	0.68	10.6	10.3	8.9	1
RAFI® 40 Tracker Fund A	0.92	13.8	-	-	4
Real Income Fund A	1.40	11.8	8.9	-	2
SA Quoted Property Fund A	1.43	18.6	15.0	22.8	4
Small Companies Fund R	1.14	2.6	4.5	18.0	5
Stable Growth Fund A	1.17	10.8	-	-	2
SYmmETRY Balanced Fund of Funds A	1.78	11.8	9.4	16.0	3
SYmmETRY Defensive Fund of Funds A	1.44	8.0	8.5	13.0	2
SYmmETRY Equity Fund of Funds A	1.49	12.8	6.5	18.1	4
SYmmETRY Fixed Interest Fund of Funds A	1.19	9.2	9.2	8.8	2
Top 40 Fund A	0.74	6.3	4.5	17.3	4
Top Companies Fund R	1.15	11.7	9.1	18.2	5
UK Money Market Feeder Fund A	0.59	-17.9	-2.1	4.1	1
Value Fund R	1.14	11.0	8.7	18.4	4
South Africa CPI		6.7	9.0	7.3	

All figures in the publication sourced (unless otherwise stated): Morningstar. Lump sum investments to the end of September 2009, distributions reinvested and NAV-NAV prices used (i.e. initial charges excluded). Income is reinvested on the ex-dividend date. Actual investment performance will differ based on the initial fees applicable, the actual investment date and the date of reinvestment of income. Past performance is not necessarily an indication of future performance. Old Mutual Unit Trusts has been licensed by the JSE Securities Exchange SA to use the FTSE/JSE Top 40 Index name. # TERs (total expense ratios) are as at 30 June 2009. Contact our Service Centre at 0860 234 234 to obtain copies of the updated fact sheets, or visit www.omut.co.za and click on "Fund Information & Prices" and select "Fees & Charges". Risk ratings do not take the impact of currency fluctuations into account.