

MARKET OVERVIEW - JULY 2010

SOUTH AFRICA

ECONOMY AND MARKETS

INTEREST RATES

The repo rate has remained at the 30 year low of 6,5% and prime overdraft at 10%, with inflation at a low 4,6%, but quite probably nearing the bottom of its cycle. Unadjusted Money supply growth came in at 1,4% year on year, private sector credit at 0,8% year on year. This reflects a very slow recovery, but is at risk of a set back. Against this weak backdrop, there is definitely no haste for the Reserve Bank to increase rates at this stage. There is a small possibility of a further cut in rates by the Reserve Bank on the 22nd July.

INFLATION

The CPI number for May slowed further to 4,6% from 4,8%. This was in line with general expectations. This is the lowest level since May 2006, as food inflation was at 0,1%, while furniture, appliances and vehicles had deflation year on year. Upward pressure is coming from administered prices which gained 12,1% year on year. The expectation is that inflation will start to pick up in the second part of 2010 with Eskom's 25% tariff increase kicking in.

CURRENCY ZAR/USD



	J203 ALSI	J210 Resource 20	J211 Industrial 25	J212 Financial 15	J253 Property	RSA Bonds ALBI
June 2010	-3.2%	-4.2%	-2.4%	-3.7%	1.1%	0.3%
12 Month return	21.8%	16.7%	24.8%	22.2%	29.0%	9.9%
Current PE (Price/Earnings)	16.7	20.6	18.3	11.2		
Long Term PE (Price/Earnings) 10 years	14.0	14.9	14.8	11.9		
Current DY (Dividend/Price)	2.3%	1.6%	1.7%	3.8%		
Long Term DY (Dividend/Price) 10 years	2.8%	2.8%	2.1%	3.8%		

SA Asset Class Performance

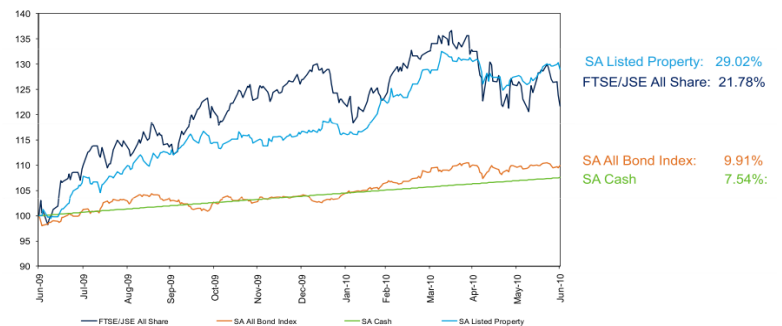
The chart alongside provides a reflection of the performance of the main asset classes over the past 12 months.

Despite the 3 year numbers reflecting cash generating 9.79% compounded and the JSE essentially flat at 0.25% per annum, the last 12 months has been a truer reflection of the ranking of returns that investors can expect over the longer term.

This is cash providing the lowest return of 7.54%, bonds being slightly higher risk (as can be visually seen in the more volatile graph) producing 9.91% and local equities, being even more volatile producing 21.78%.

Local listed property has been a fantastic investment over the last 12 months, gaining 29%.

As we reflected last month, over the last 40 years, the most consistent producer of real returns over 10 year periods has indeed been equities.



FIXED INCOME AND PROPERTY

MONEY MARKET

The 3 month Jibar - the Johannesburg Interbank Agreed Rate - which had moved down last month to around 6,6%, fell further on the generally bearish outlook from Reserve Bank governor. The 3 month Jibar rate, which drives money market rates has declined to 6,57%. The latest rates were 6,22% for SAFEX overnight, 6,43% for 1 month Jibar, 6,57% for 3 month Jibar, 6,77% for 6 month Jibar, and 7,1% for 1 year Jibar.

BOND MARKET

The bond market gained 0,3% for the month of June and just short of 10% for the last 12 months. For the year to date bonds have gained 5,6% and are still outperforming equities. The yield on the R157 has fallen back again in line with the firmer rand, declining to 7,68% from its recent level over 8%. The All Bond yield was at 8,86% at month end with the implied inflation running at 5,88%.

PROPERTY MARKET

Listed property gained 1,1% for June after declining in May, but has since gone on to increase in July in line with the equity market and the decline in longer dated bond rates. The generally muted outlook for inflation and the prospect of low interest rates has kept local property attractive. At the end of June the historical yield for listed property was at 8,16% and the forward yield at 8,83%, down from 9,19% at the end of May. Relative to bonds and equities, property is attractive but at higher risk.

JSE ALL SHARE INDEX - technical



The decline over the second quarter on the JSE left the overall index with a pattern that is known as a head and shoulders pattern. This pattern started developing from the end of 2009 and a break through the 26300 level could have seen a far sharper decline.

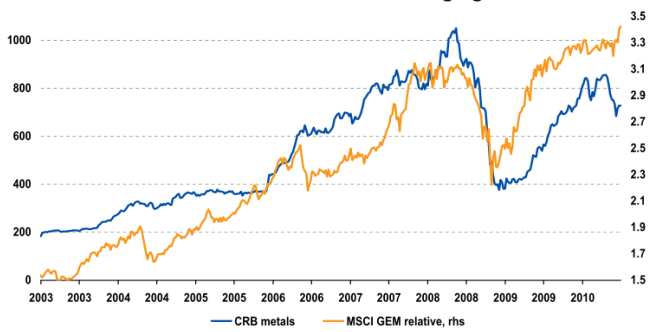
Thus far the overall index has held up. Essentially, however, the JSE has been moving sideways over this period of time, frustrating investors.

As we noted last month the 200 day moving average is always an important technical level. The JP Morgan technical analyst has the current trend of the JSE, Financial, and Industrial sectors as sideways, with Resources going down.

There are a number of sectors that remain attractive from a technical perspective, including automobiles, beverages, chemicals, engineering, fixed telecom, food producers and retailers, general industries, gold, healthcare, leisure goods, personal goods, pharmaceuticals, real estate, and software.

LOCAL MARKETS RELATIVE TO GLOBAL MARKETS

CRB/Reuters Commodities Index vs. Emerging Markets Index



Source: Franklin Templeton

Last month we had a chart from BCA - a respected global investment house, charting various asset class bubbles over the last 50 years. The asset bubble that dominated the 1990's was information technology and related, while the bubble that dominated the first decade - not necessarily to the same extent as others - was commodities.

The chart alongside reflects the correlation between commodities, as measured by the CRB/Reuters Commodity Index and the Emerging Market Index.

While this does not always hold true, some of the constituents of the Emerging Market Index are Brazil, Chile, China, India, Korea, Russia, South Africa, and Turkey.

We know that the commodity cycle drives the JSE. While there are a number of attractive industrial and financial companies, the major driver of the local economy remains commodities.

The second chart gives a very clear indication of just how correlated the local JSE has been with Emerging Markets over a period of 5 years. The same typically holds true over varying dates.

JSE vs Global Developed vs Emerging Markets



Source: Investec and I-Net Bridge

An investment on the JSE has more than doubled, compounding at 16.25%. Other Emerging Markets have performed in a similar way, while Developed Markets, measured in rand terms have moved sideways, essentially losing investors money relative to cash.

The flow of funds into Emerging Markets and specifically South Africa has been positive with a ten year monthly average of R2.43 billion into SA equities. June was slightly higher than this average at R3 billion net purchases.

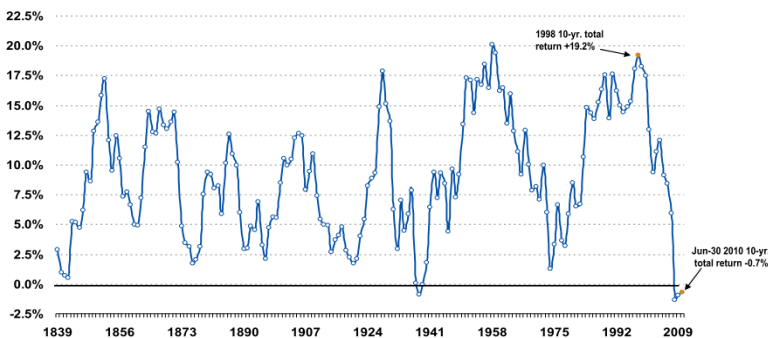
GLOBAL MARKETS

The relative charts above give a clear indication of where the action has been over the last 5 years and even extending back to 10 year. Following the market peak both in nominal terms and with extreme valuations in 2000, investors in developed markets, sustained a subsequent period of negative returns. The first chart below plots the 10 year compounded annual total return. The first thing to note from this very long term chart is that over most 10 year periods, investors have enjoyed positive returns. The only 2 periods where investors experienced negative 10 year annual returns, was post investing at the 1929 peak and the 2000 market peak.

The second thing to note is the cyclical nature of 10 year returns. While an investor may not always enjoy the peak 20% compounded returns, having a longer term investment horizon and avoiding times of extreme poor values, will heighten the possibility of a good outcome.

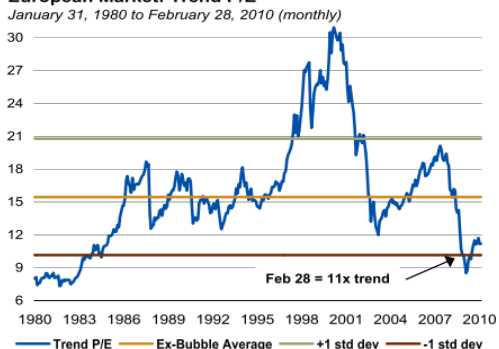
The 2 charts below depict the trend price to earnings multiples of the European and US markets. In the case of the US chart this data goes back to 1954. The 10 year extremely poor performance that US investors - and indeed global investors - have incurred, correlates with a derating of the market to below its longer term average. These valuation charts give a clear expression of how expensive prices were in the late 1990's and early 2000's, with a clear impact on the subsequent 10 year poor performance. While there is no guarantee that from this level investors will experience improved performance, history indicates that the probability of superior performance is definitely heightened from starting points of cheaper valuations.

S&P Stock Market Composite 10-Year Compound Annual Total Return (Including Reinvested Dividends), Data 1830 to June 30, 2010

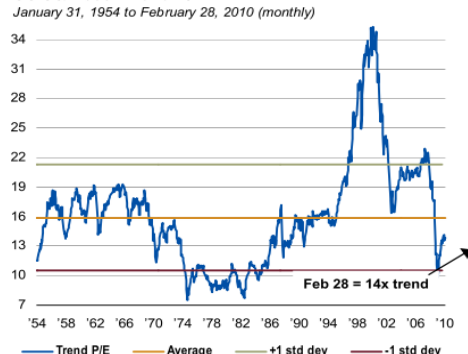


Source: Franklin Templeton

European Market: Trend P/E

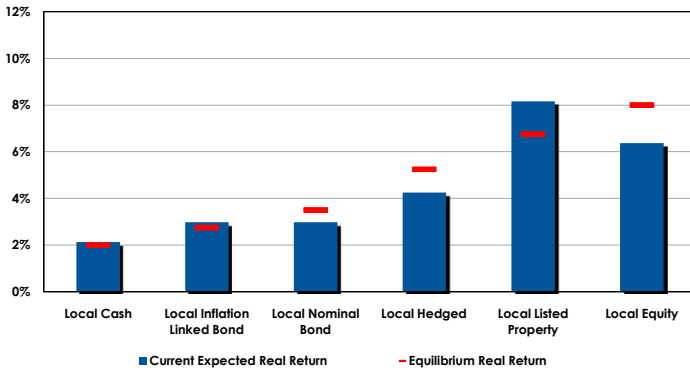


US S&P 500: Trend P/E



LONG TERM EXPECTED REAL RETURNS

RSA Asset Valuations



This table provides an indication of the current expected real returns from local assets relative to longer term real rates from the assets.

- Cash in absolute terms is close to historical averages, but relative to longer run inflation expectations is not too appealing. Money market rates are around 6,6%.

Historical inflation is running at 4,6% while the implied inflation is around 5,88%. Real yields on 13 year inflation linked bonds have been static at just under 3%.

- Bond yields declined over the last month with the lower inflation and an outside possibility of a further rate cut. The shorter dated R157 is trading at 7,7% down from over 8%, while the longer dated R204 at 8,44% down from 8,75%. The 10 year Bond exchange yield was at 8,86% at the end of June, up slightly from 8,73%. Looking at the implied inflation our assessment is that bonds are trading at fair value.

- At face value local listed property continues to remain attractive. It is trading on an historical rolled yield of around 8,16% down from 8,43% at the end of May and on a forward yield of 8,83%. Assuming that the annual dividend growth can at least match inflation, then this yield appears attractive. Potential vacancies going forward are one of the major risks in this asset class.

- With the decline in prices over the last 2 months, local equity has moved to slightly more attractive levels. Using historical data and adjusting current earnings back to a longer term trend, our expected 5 year real return from the current valuation is a real 6,37% per annum. This is lower than the long run average of around 7,5% to 8% real.

HOUSEVIEW

LEGEND - RELATIVE TO FAIR VALUE

Very Cheap	++
Cheap	+
Fair Value	=
Expensive	-
Very Expensive	--

ASSET CLASS OUTLOOK

Local Equity	-
Local Property	-
Local Fixed Income	=
Local Hedged	=
Global Currencies	++
Global Equity	=
Global Fixed Income	--
Global Alternative	=

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