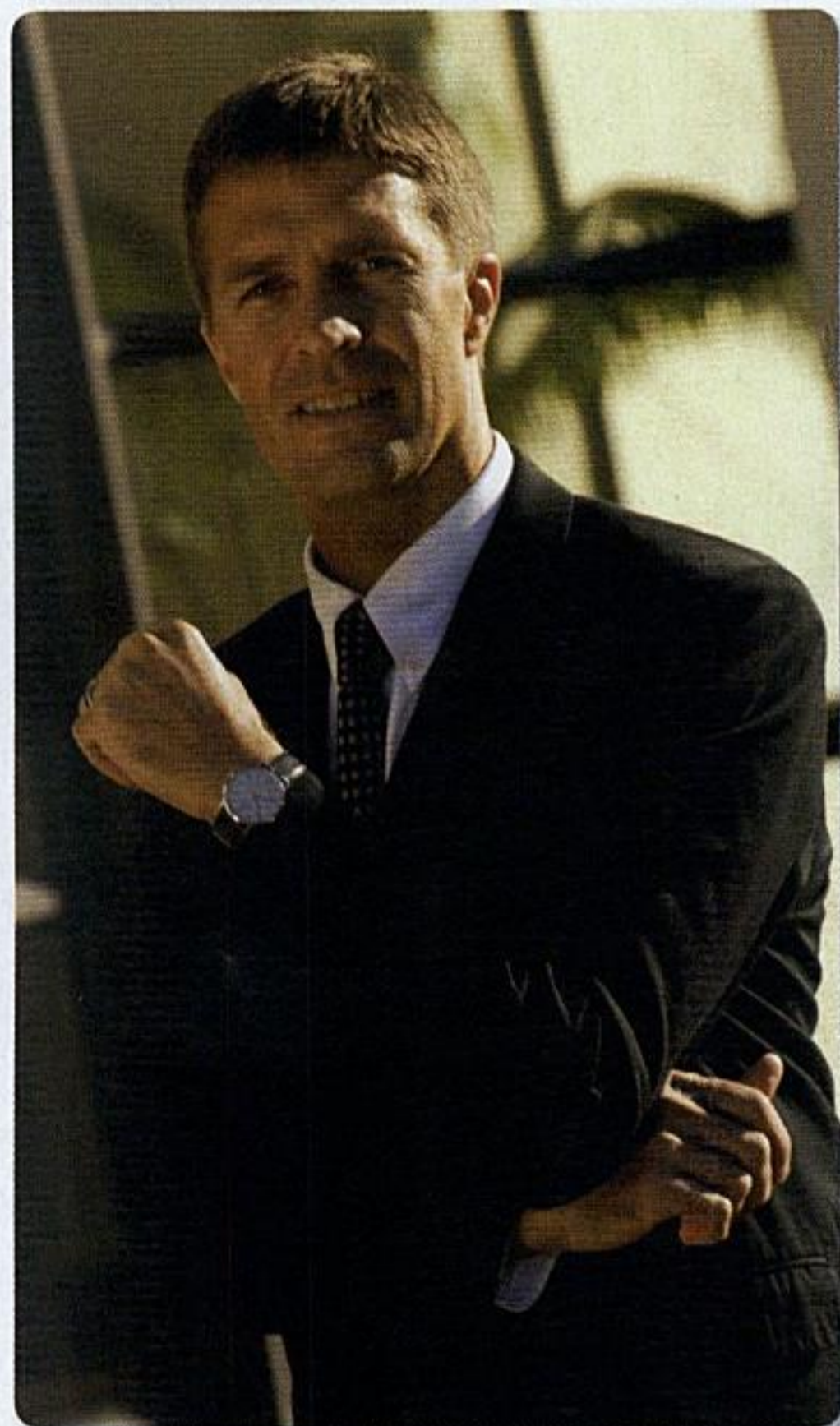


| INVESTOR CONFIDENCE |

## Market confidence takes a bath

Investors have slightly reduced their return expectations

**THE MARCH SURVEY** of the Sanlam Investment Management (SIM) investor confidence index highlights the negative swing in investor confidence in recent months. After a more than 20% drop in the JSE all-share index between October 2007 and January 2008 it recovered to its previous high by March. That alone could have driven investors to conclude that market valuations were too high, says Frederick White, head of research at SIM. The survey is conducted monthly among a range of investment professionals.



A clear change in sentiment against SA Inc.  
**Frederick White**

"In addition, the clear change in sentiment against SA Inc – as evidenced by the selloffs in the rand, the bond market and SA industrial and financial shares (relative to the all-share) this year – could have led to a conclusion that investors would require a bigger premium in terms of returns from equity investments, at least in the medium

term until some issues have been resolved," says White.

"Those issues could include evidence that electricity supplies won't limit economic growth potential too much, proof of macro-economic policy stability following large-scale leadership changes in SA's leading political party, general global concerns about global credit markets and the potential knock-on to global growth."

SA investors have slightly reduced their return expectations for the local equity markets. However, even that conclusion hides some big differences in the changes between the two main groups of investors. Among institutional investors there were increases in expected returns while among advisers there were drops in expectations.

"Furthermore, the declines in the expectations among advisers were large

urement was the worst since inception, but it remains the institutional investors that are the most worried about a crash.

"Despite not being the worst crash measurement since index inception for this group the average probability of a crash did rise to a relatively high 20,4%, with more than half of that group deeming the chance of a crash to be more than 10%. Combining that measurement with the expected returns discussed above gives you some insight into the possible base case and worst case expectations large institutional investors currently hold for equity markets," says White.

There seems to be a contradiction in the fact that on the one hand investors' expected returns have increased while their short-term bias has decreased (although it's still clearly present), while on the other they see a much bigger risk of an equity market meltdown. "You could read into that they observe the

### Electricity supplies won't limit economic growth potential too much.

enough to bring their average return expectations below that of the institutional group for each of the measurement periods – an unusual development, given the inherent positive bias one would expect from that group," says White.

"It should be highlighted that the improved return expectations among institutional investors still don't make them bullish: to the contrary. There's still a prominent short-term bias, with average one- and three-month returns still below zero and even on the one-year return the average expected by this group is a mere 5,9% – basically keeping up with inflation and leaving it to the dividends to provide investors with a real return."

The survey also found growing concerns about the prospects of a market crash, particularly among institutional investors. SIM's crash confidence index declined by 18 points to 53 in March 2008. This index measures the number of respondents seeing a probability of more than 10% that a crash could occur over the next six months. Among investment advisers the crash meas-

aggressive and substantial measures by the US Federal Reserve and other central banks and – as a "base case" – have raised the probability that those would overcome the troubles introduced by the credit markets, thereby avoiding a drawn out US recession and avoiding a global recession and consequently rescue equity markets," says White.

At the same time there are concerns about the knock-on effect of a US recession, while SA-specific fears are contributing to very muted return expectations, slightly below trend.

The uncertainty surrounding the "victory" over the credit monster will be resolved over roughly a six-month period and hence investors don't foresee a market rally in the short term.

The worst case scenario is clearly one where credit problems aren't overcome, economic hardship is much worse than expected and equity markets decrease very strongly, as they did in the market crash preceding the Great Depression – and the probability of that outcome has increased to 1-in-5 – a scary thought indeed, says White. ■