INTERMEZZO

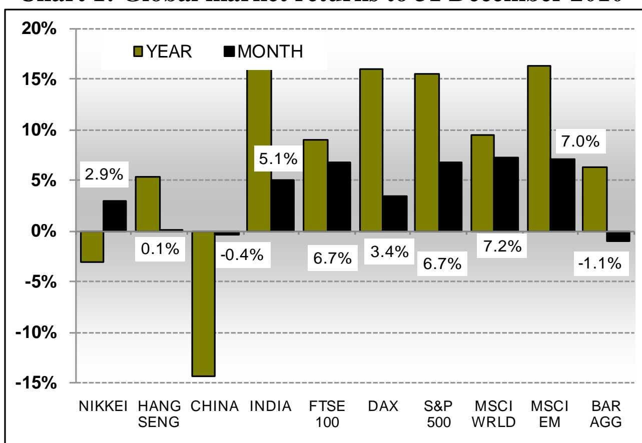
MAESTRO

11th Edition | January 2011

December in perspective – global markets

December was very much like September, which I termed a "stealth bull month" at the time. That is certainly true of developed markets, which have surprised many, including ourselves, by their recent returns *relative to emerging markets*. Without much fanfare developed markets slowly but surely posted another profitable month, although the thin volume and Silly Season mean one needs to take the movements with a pinch of salt. Nevertheless, undeterred by another Chinese interest rates hike and spurred on by the announcement of another huge (nearly $1 trillion) fiscal stimulus by the US authorities, markets crept up steadily throughout the month to post decent returns for December. To put the September and December "stealth months" into perspective, the combined return of the US and MSCI World index, for example, for these two months is 16.3% and 17.0% respectively, which must be seen in the context of their total 2010 returns of 15.5% and 9.6% respectively. In other words, without September and December (and July for that matter) global equity returns for 2010 would look very poor indeed. If you exclude the returns for March, July, September and December the MSCI World index return for 2010 would be -18.2%. Put differently, these four months alone produced returns of 33.9% - the remaining eight months of 2010 were awful. You can imagine where this type of market behaviour left "clever" investors who were trying to "time the market".

Chart 1: Global market returns to 31 December 2010

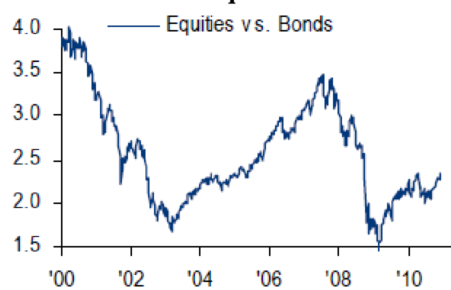


Be that as it may, global equity returns were positive in December. The MSCI World and Emerging market indices rose 7.3% and 7.0% respectively. Large gainers included the US and UK markets up 6.7% each, France 5.4% and Germany 3.4%. Emerging markets continued to lag, as they have done for most of the final quarter. Asian markets were particularly soft. China declined 0.4% and Hong Kong rose 0.1%. India rose 5.1% and Brazil 2.4% while Russia gained strongly on the back on the firmer oil price, ending the month up 10.8%. Speaking of oil, although the dollar was weak – it declined 3.0% and 0.5% against the euro and sterling respectively – commodity prices were very strong in any event. Part of the strength was due to a more positive view on the global economic outlook due to the US fiscal stimulus announcement. Oil rose 10.3%, palladium 13.5% and silver 12.9%. Copper rose to an all-time high, while agricultural commodities were also strong. The CRB and S&P GSCI commodity indices rose 7.1% and 8.2% respectively, showing just how strong commodity prices were and underlining the concern we expressed last month about inflation pressures lifting their heads. We suspect the latter will develop into one of the most influential factors in the year ahead. Table 2 at the end of this edition depicts the usual MSCI (dollar) returns while Table 3 depicts a selection of additional returns – the full table will be included in our Quarterly Reports.

Charts of the month

Seeing that we have just put another year behind us, I thought it would be useful to take at a look at a few charts that capture major features of the investment environment in 2010. The charts are accompanied by only a little comment, as they mostly tell their own story. At the end of this edition, I have also included Table 4 and 5, which are very informative. One of the main reasons for *Intermezzo's* existence is to edify its readers and teach them (and us) more. We refer to MSCI indices widely, and I thought it useful to show their make-up (Table 4) as well as the respective sectoral make-up of the underlying components (Table 5). They make for nice references into the future, and sourced per kind favour of Merrill Lynch, as are the charts.

Chart 2: Global equities versus bonds



Outperformance by global equities of bonds gathered pace towards the end of the year. The trend since 2000 though, is very informative. Refer also to Chart 5.

Source: Merrill Lynch

What's on our radar screen?

Here are a couple of items we are keeping a close eye on:

- *The SA economy:* one of the notable features on the SA investment landscape in December was the publication by the National Treasury of the new exchange control limits, announced in principle in the October mini-budget. With effect from 2011 Investment Managers (such as Maestro) are now able to remit 35% of their assets offshore (previously 30%), collective investment schemes 35% (30%) and retirement funds 25% (20%). Non-investment and

INTERMEZZO

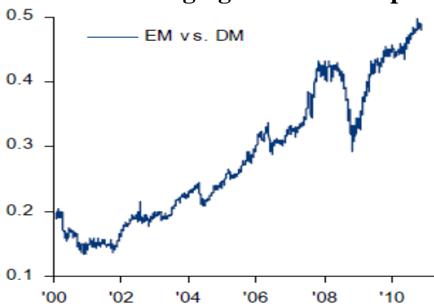
MAESTRO

11th Edition | January 2011

investment linked life insurers' limits were raised to 25% (20%) and 35% (30%). A few years ago this would have led to an immediate and sharp decline in the currency, but the only effect now was to push the rand even firmer – the rand rose 7.2% against the dollar in December. Spare a thought for the authorities and exporters who would feel more comfortable with a firmer rand; despite the exchange control changes and the numerous rate cuts this year, which traditionally would have weakened the rand, so far this year it has only known one direction – up. The rand rose 11.3%, 19.0% and 14.8% respectively against the dollar, euro and sterling in 2010.

- *The US economy:* a factor supporting equity markets and depressing bond markets during the month was the $1 trillion stimulus package announced by the Obama administration. It consisted of a two-year extension of the Bush era tax cuts as well as a surprise 2% cut in payroll taxes. We are inclined to get too glib about large numbers these days, so let's say that slowly: the US administration, already facing a budget deficit that some argue is out of control, added another *$1 trillion of debt* which will have to be financed during the next two years. The hope is that the stimulus will stimulate the economy, lift it out of the quagmire and alleviate the high unemployment. Time will tell how successful this stimulus will be; it was immediately greeted by credit agencies' "long-term concern" about the US credit outlook and the security of its triple A credit rating. Still on the US economy, third quarter growth was revised (the third and final revision) from 2.5% to 2.6%.
- *The Chinese economy:* you may remember the scare that Chinese inflation caused last month, when it rose to 4.4% in October. Well, in November it increased further to 5.1%, higher than the expectations for an annual rate of 4.7%. That immediately prompted the authorities to increase the banks' reserve ratio requirements by another 0.5% to 18.5% - the third within a month and the sixth increase this year. In true Chinese fashion, the authorities waited until Christmas day before raising interest rates by another 0.25%.

Chart 3: Emerging versus developed equity markets



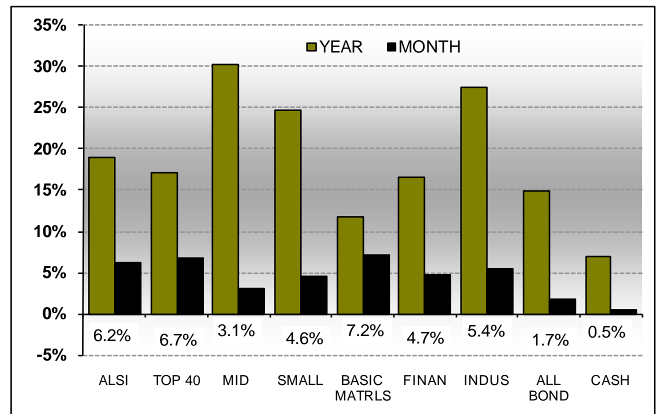
Source: Merrill Lynch

In "post-crash" terms, emerging markets have comprehensively outperformed developed markets since November 2008. The longer term trend since 2001 is clear.

December in perspective – local markets

The more positive stance on the global economic outlook, initiated by the US fiscal stimulus, ensured that the basic material sector led the SA market higher. The basic material index rose 7.2% despite the rand's 7.2% gain against the dollar. Despite the gold price flirting with its all-time high (gold rose only 1.9% on the month) the Gold mining index rose only 2.0%. The financial and industrial indices rose 4.7% and 5.4% respectively, all of which translated into a 6.2% rise in the All Share index, bringing its gain for all of 2010 to 19.0%. With basic material (mining) shares leading the charge, mid and small cap returns were always going to struggle to keep up with their large cap brethren. The latter rose 6.7% versus the 3.1% and 4.6% gains in the mid and small cap indices. This is in contrast to the US returns across the market cap spectrum; the US large, mid and small cap returns for the month were 6.7%, 6.4 % and 7.6% respectively. The annual 2010 returns for the SA large, mid and small cap indices were 17.2%, 30.3% and 24.7% respectively. The All bond index benefitted from the firmer rand, rising 1.6%, more than the cash return of 0.5% but still woefully short of the equity market returns.

Chart 4: Local market returns to 31 December 2010



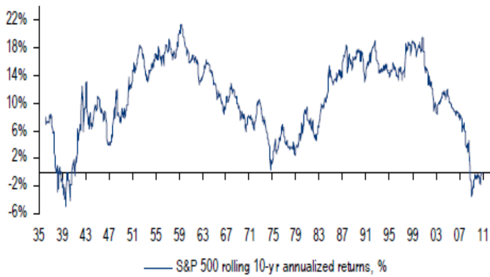
A few quotes to chew on

I thought the following was a very synoptic view on the past few years in global investment markets and economies. It came from *Guy Monson, CIO of Sarasin and Partners*: "For much of the last two years, fears of renewed economic collapse in the aftermath of the 2008 credit crisis have provided a rather convenient excuse to delay the tough economic and political decisions that most of us know are needed to stabilise and rebalance global growth. Central banks have instead done most of the heavy lifting, flooding their economies with credit and propping up domestic bank balance sheets regardless of the quality of the underlying assets deposited with them. While there has been much talk of reducing yawning deficits, few actual cuts have been implemented, with politicians justifying the delay on the grounds that to remove government demand now could upend today's fragile recovery. Even in the booming

capitals of Asia, where growth is again near record levels, rising food and energy costs along with surging domestic asset prices are lifting inflation to worrying levels. Few regional policy makers, though, are really ready to allow their currencies to appreciate by anything like the amount needed to offset these imported costs, for fear of undermining export-led growth models and losing competitiveness to their neighbours."

Chart 5: US equities: 10-year annualized rolling returns

Despite positive 2010 returns, US equity investors still lost money over the last ten years; an astonishing phenomenon that textbooks never warned investors about.

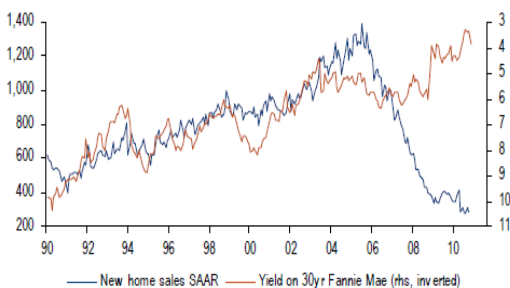


Source: Merrill Lynch

Much has been written about the policy of quantitative easing (QE), including by ourselves. Given the turmoil that it has caused in bond markets in particular in recent weeks, some further comments are worth listing here. *Guy Monson from Sarasin* again: "There is a growing chorus of disapproval at this high-jacking *(sic)* of the US sovereign bond markets (supposedly the benchmark from which so many global assets are priced). Domestically, the newly enfranchised Republican Tea Party members are keen to curtail the Fed's interventionist "big government" powers and are talking openly in Congress of the Fed's folly. At the same time across the oceans and continents, politicians are speaking out against the "clueless" policy stance of the US central bank. If early signs of success are not evident, political resistance to these policies could gain momentum."

Chart 6: US mortgage rate trough coincides with lows in housing sales

Merrill Lynch put it so aptly, " if you can't stimulate the US consumer through lower interest rates, who can you stimulate?" Investors are waiting for a meaningful improvement in the US housing, labour and lending markets. (Note that the right hand scale on the Chart, i.e. the 30-year Fannie Mae mortgage rate is inverted) .



Source: Merrill Lynch

Another event that elicited a lot of comment during the month was the Obama administration's $1trillion stimulus. *Dan Greenhaus, chief economic strategist of* US investment bank *Miller Tabak* had this to say: "One cannot dismiss the longer-term budget implications of this deal. Adding nearly a trillion dollars to the debt over just the next two years without a concurrent plan to reduce the debt in the medium term is in many respects the height of irresponsibility."

The *Lex Column* in the Financial Times had the following to say on the topic. "President Obama says the latest deal will help 'parents and students and other folks help manage their bills'. Indeed. Ordinary people find it easier to keep their financial house in order when the federal government shows no sign of doing the same."

We continue to be concerned about the degree of debt, sovereign debt in particular, in developed markets. This is expressed in our **Big Picture Themes** of *Sovereign Risk* and *The Lost Decade*, which refers to the debt-induced spiral of low or no growth faced by the US economy. In an excellent article about the experience of Latin America in the 1980s, *Komal Sri-Kumar, chief global strategist at Trust company of the West*, concludes with the following words. "The Latin American experience also suggests that there will be adverse implications of European debt and equity markets. The deterioration in debt ratios will discourage voluntary lending to the affected Eurozone counties and, in the absence of the functioning capital markets, those governments will become permanent supplicants for official aid. Poor economic growth prospects will damp equity market performance as well because an increasing percentage of savings will be destined toward debt service rather than domestic investments. The vicious cycle of austerity, declining GDP and worsening debt ratios means that there will be no self-correcting cure for the malaise in debt and equity markets. In the absence of debt reduction, the 2010s could become a "lost decade" for some Eurozone countries, much like the 1980s turned out to be for Latin America.

Source: FT.com

INTERMEZZO

MAESTRO

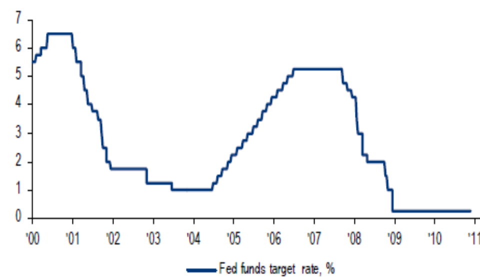
11th Edition | January 2011

In similar vein, *former IMF Chief Economist and now economics professor at Harvard, Kenneth Rogoff*, had this to say about whether the peripheral Eurozone countries could avoid sovereign debt restructuring. “Ultimately a significant restructuring of private and or public debt is likely to be needed in all of the debt-distressed Eurozone countries ... Already facing sluggish growth before fiscal austerity set in, Portugal, Ireland, Greece and Spain face the prospect of a “lost decade”, much as Latin America experienced in the 1980s. Latin America’s rebirth and modern growth-dynamic really began to unfold after the 1987 “Brady Plan” orchestrated massive debt write-downs across the region. Surely, a similar restructuring is the most plausible scenario in Europe?”

In a very succinct article in the Financial Times entitled “Europe cannot default its way back to health” *executive European Central Bank (ECB) board member Lorenzo Bini Smaghi* provided compelling reasons why simple and quick defaults, either on the parts of banks or sovereigns (EU member countries), do not provide the solution to the current sovereign crises wracking the Eurozone. I thought his opening lines were profound: “Among many things we have learnt from the crisis is that governments and financial markets find it difficult to understand each other. Governments cannot grasp why the markets lose confidence in the state of public finances so quickly and regain it so slowly, after a long period of fiscal consolidation. The markets, for their part, are mystified by the failure of governments to take simple and timely steps to sort out the problems they face.” He ends off with the following: “To understand what is happening in Europe, economics textbooks are useful but the history ones even more so”. If you would like a copy of the article, please let me know.

In a similar vein, *Financial Times columnist Philip Stevens* wrote an excellent article entitled “On the way to a new global balance”, which began as follows; “We are living through one of history’s swerves. A multipolar world has been long predicted, but has always seemed to be perched safely on the horizon. Now it has rushed quite suddenly into the present. Two centuries of western hegemony are coming to a close rather earlier than many had imagined. The story is unfolding in dry economic statistics. Next year, just as this year, the economies of the rising states – China, India, Brazil, Turkey, Indonesia and the rest – are likely to grow by 8% or more. Debt-burdened advanced nations will mostly struggle to expand by more than 2%. The pattern is well established. The global divide is between slow and fast-growing nations as much as between the rich and the rising. The geopolitical balance is adjusting accordingly ... The lazy way to describe the new geopolitical landscape is one of a contest between the west and the rest – between liberal democracies and eastern market economy autocracies. Neat as such divisions seem, they miss the complexities. A more sanguine view of the world looks to the Group of 20 nations as an instrument to forge a broader consensus about east-west and north-south co-operation ... The rising nations prize state power over international rules, sovereignty over multilateralism. The transition to a new order is likely to see more rivalry and competition than co-operation. The facts of interdependence cannot be wished away but they will certainly be tested. It is going to be a bumpy ride. A pity then, that much of the west seems intent on hiding under the bedcovers.”

Chart 7: Federal Reserve funds target rate (%)



Source: Merrill Lynch

Ultra-loose US monetary policy saturated global markets with liquidity, which has been good for equity markets. The Fed is likely to keep rates around 0% for all of 2011.

For the record

Table 1 lists the latest returns of the mutual funds under Maestro’s care. You can find more detail, including the latest [Maestro Equity Fund Summary](), by visiting our website at www.maestroinvestment.co.za. Returns include income and are presented after fees have been charged. From the beginning of next year we will include the returns of our retirement funds in this table.

Table 1: The returns of funds under Maestro’s care

	Period ended	Month	Year to date	Year
Maestro Equity Fund	Dec	**4.7%**	**18.4%**	**18.4%**
Maestro equity benchmark *	Dec	6.3%	19.6%	19.6%
JSE All Share Index	Dec	6.2%	19.0%	19.0%
Maestro Long Short Equity Fund	Nov	**-2.3%**	**4.6%**	**3.2%**
JSE All Share Index	Nov	-0.5%	12.0%	15.3%
JSE Financial and Indus 30 index	Nov	-0.9%	15.3%	18.6%
Central Park Global Balanced Fund ($)	Nov	**-2.2%**	**1.9%**	**0.3%**
Benchmark**	Nov	-1.1%	4.3%	4.9%
Sector average ***	Nov	-1.9%	3.8%	3.8%

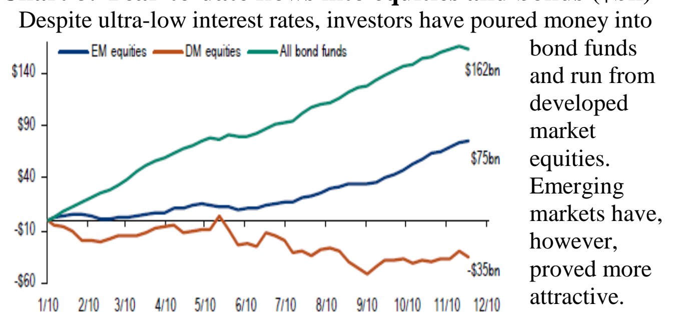
* 50% JSE Top 40 Index, 50% JSE Financial & Industrial 30 Index
** 40% MSCI World Index, 20% each in Barclays US Aggregate Bond Index, Credit Suisse Tremont Hedge Index and 3-month US Treasury Bills
*** Lipper Global Mixed Asset Balanced sector ($)

MAESTRO INTERMEZZO
11th Edition | January 2011

More odds and ends
The following don't really fall into the File 13 section, as they are quite relevant to the prevailing investment environment. In no particular order, then:

- *Capital raising in emerging markets*: despite the equity market volatility and, at least on some developed markets, mediocre returns, 2010 may go down as a record year for raising capital by global companies. The latest figures I have (mid-December) show that $255.3bn have been raised in 1 199 initial public offerings (IPOs). This compares to the record of $295bn raised in 2007 from 2 014 IPOs. Ironically 2010 already holds the record number of IPOs that were pulled at the last moment – no less than 180 in total, up from 125 last year. Of the capital raised so far this year, three IPOs (Agricultural Bank of China, AIA Group in Hong Kong and GM in the US) account for nearly a quarter of the capital raised. Asia has been the most popular region for IPOs this year, confirming our **Big Picture Themes** of *The Shift in power from the West to the East* and *The Coming of Age – the rise of emerging markets*. So far Hong Kong has raised $52.8bn in IPOs compared to the US's $42.0bn. Mainland Chinese exchanges have raised $66.9bn. China and Hong Kong have thus, between the two of them, raised almost triple the amount of capital that was raised on US markets through IPOs.
- *The interconnectedness of the European banking system*: one of the reasons we remained concerned about sovereign developments in the Eurozone is the nature of the relationships between the countries. They are inextricable, intertwined and very complex. One could be forgiven for seeing the Irish sovereign crisis as isolated; it is, after all, only the 15th largest economy in the EU. But consider this: Irish banks are very exposed to many of the weak regions in the Eurozone, which complicates matters furthers. Despite their relatively small foreign network, Irish banks together make them the fifth largest lender to Italy; together they have lent, and are thus exposed to the tune of $40.9bn of Italian credit. They are also the fifth, fifth and seventh largest lenders to Portugal, Greece and Spain respectively, which shows just how intertwined the region is. In addition, German and French banks have very large exposure to Irish banks. According to the Bank of International Settlements (BIS), German and French banks alone have $138.6bn and $50.1bn exposure to Ireland respectively, and $36.8bn and $53.5bn to Greece. So if something happens to the Irish banking system, which may yet still happen, and which may have happened much sooner where it not for the $85bn bailout recently ($46bn of that went directly to Irish banks), German and French banks would have been in a lot of trouble (some would argue more trouble than they are already in) despite the fact that those economies are in better health than Ireland's. We have said it before and will continue saying it for a long time yet: we are not yet out of the Great Financial Crisis and the banks and more importantly certain Eurozone countries still hold more risk than the market is pricing in. The issue of *Sovereign Risk* will remain high on our **Big Picture Theme** list for 2011.

Chart 8: Year-to-date flows into equities and bonds ($bn)
Despite ultra-low interest rates, investors have poured money into bond funds and run from developed market equities. Emerging markets have, however, proved more attractive.



Source: Merrill Lynch

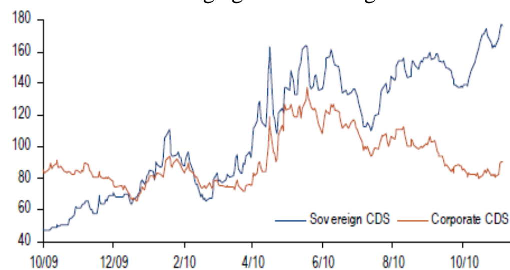
- *Tragedy follows ill-gotten gains*: the media love scandals and reporting bad and bizarre news. As consumers of their output it is important that we check ourselves periodically to realise afresh that for every scandal, there is a tragic human side accompanying it; real-life cases of wrecked dreams, lives and families. A good example of this was the case in 2008 when Porsche tried to steal a march on VW by cornering the VW share market through the use of derivatives. The episode, driven by a CEO whose ego knew no end, brought Porsche to its knees. But perhaps the saddest outcome was the death of German billionaire Adolf Merckle, the patriarch of the family dynasty of Heidelberg Cement fame, who threw himself in front of a train when the debt he accumulated shorting the VW share price threatened to bring the family empire to an end. Sadly, this month I'm sure you read about the tragedy that followed in the wake of the world's biggest scandal, the Madoff Ponzi scheme. Bernie Madoff's eldest son, Mark, aged 46, was found dead in his New York apartment on the anniversary of his father's arrest. He had hanged himself from a metal pipe in his living room. Although the two Madoff sons were under federal investigation and had been sued by the Trustees representing the victims, they had not yet been charged. Mark Madoff leaves behind his wife and a young son. There are seldom any winners in these situations, despite all the ill-gotten gains and publicity.
- *Banks – more capital calls coming:* we have been wary of banks after the financial crisis, fearing that the true state of their balance sheets has not yet been revealed and that in due course they will have to raise capital to prop up the latter. In late December the Basel

Committee on Banking Supervision, the international banking watchdog, finalised its "Basel III rule book", which has set the new capital and liquid requirements for banks. The requirements which have emerged as a result of the new regulations are quite staggering. Firstly, the *capital requirements* have, not surprisingly, been tightened. In terms of the new requirements banks have to set aside tier one capital of 7% (the definitions of tier one capital have been changed). By way of reference, the top 91 banks in the world currently have only 5.7% of (redefined) tier one capital (11.1% under the old definition), leaving them short of $577bn of equity; they have until 2019 to meet this requirement. Secondly and more urgently, "Basel III" contains a new requirement that they have sufficient 30-day liquid investments. The shortfall in respect of this *liquid requirement* by the same 91 banks, is a staggering $2 287bn ($2.3 trillion). More importantly banks have only four years (by 2015) to establish the necessary investments to meet this requirement. Apart from the likelihood of further capital raising by the banks, these new requirements also have significant implications for bonus payments to staff and dividend payments to shareholders. It is not surprising then that the financial sectors of major markets have lagged overall returns. The S&P Financial sector return for 2010 was only 4.8% while that of the overall market (S&P500) was 15.5%. Although less affected by the financial crisis, SA banks also lagged the returns of the overall market; the financial index rose 16.6% in 2010 versus the All share index return of 19.0%.

- *The US "muni" market* – this is not a market we claim to have an intimate knowledge of and certainly not one we cover regularly. However, recent developments in the US municipal bond market are causing us some "angst" and we are watching it closely, given its size ($2.9 trillion) and relevance to US consumers. In November the US *muni* market registered its worst monthly decline (-2.2%) since the collapse of Lehman Bros in September 2008, when it declined 4.7%. There are two main factors behind the recent trauma in the muni market: firstly the recent very sharp rise in the Treasury (bond) market has seen a flood or new issues coming to the market (hence over-supply) and secondly, fears over possible defaults by cash-strapped states and cities. US investors invest in this market as its yields are usually higher than Treasury yields and the income received is tax-free in one's own state. But as US bond yields have risen (and prices fallen) and the state of cities and US states deteriorated, so fears have grown of possible defaults by issuers, who are struggling with budget deficits and under-funded public pension schemes. In the last two weeks of November, investors withdrew $5bn from this market. All we can say for now is that we will be "watching this space" for further signs of investor distress. Given its size and importance it may yet become a "hot topic" (read "destabilizing factor") in the year ahead.

Chart 9: Governments are rated worse than corporates

As confidence in governments and politicians waned steadily, so the cost of insuring against sovereign debt default has increased steadily throughout the year and is now much higher than the cost of insuring against corporate failure.



Source: Merrill Lynch

File 13: Information almost worth remembering

Some questions that remained unanswered

Having had some time away from my desk and being able to reflect on the past year, a couple of questions remain unanswered in my own mind. They include:

- How can America continually gripe about China's supposed "manipulation" of their currency, yet the Fed employs a deliberate policy of manipulating the level of US interest rates and, indirectly, the dollar? Talk about the pot calling the kettle black!
- How can one solve a problem, initially caused by excess debt, by adding even more debt? Take Ireland and Greece for example; politicians' solution to their debt-induced problems was to lend them more money i.e. to increase their indebtedness further. Am I missing something?
- Whatever happened to the Eurozone bank stress tests, which we mocked at the time? If they were of any substance and not a useless PR exercise, why did Ireland need a second bail-out? Remember that the bulk of the rescue package proceeds went to Irish banks to boost their balance sheets.
- If the intention of QE 2 was to lower US interest rates and the US's official policy is in favour of a strong dollar, why then, since the announcement of the actual QE2 policy of the Fed, has the yield on the 10-year bond moved from 2.5% to 3.5% and the dollar fallen from 1.30 to 1.34 to the euro? Dare I say it again ... am I missing something?

China's high-speed railway

Some of you may have heard of China's achievements in the realm of high speed railway. To date, its investment in high speed railway has totalled 7 531km of track, more than the total high speed track than the rest of the world put together. A journey from Wuhan to Guangzhou used to take

10 hours by the 1 068km of conventional route, but now takes less than three hours; a similar length journey in the US, from Washington DC to Chicago, takes 18 hours on Amtrak. Within the next decade the Chinese government wants to connect 70 of its main cities, servicing more than 90% of the population. China's investment in existing rail infrastructure across the mainland had risen six fold since 2005, to $124bn this year.

One cannot fear what you don't know
As is often the case in the event of a crisis, the *extent* of the crisis only becomes clear after the event, when the details are released into the public domain. So it is with the Fed's action at the height of the financial crisis in 2008, details of which were released by the Fed last month. Many of you would have read them already, but the point I wish to emphasize here is the sheer extent of the support the Fed provided to the market. We all suspected that the numbers were large, but I continue to be amazed at *how* large the numbers are. It adds substance to the fact that the 2007/9 "Great Financial Crisis" was the largest and most severe one in living memory. When you look at some of the details, it is not hard to see why. Consider a selection of them, below:

- The Fed provided support a total of $3.3 trillion by means of 21 000 transactions between 2007 and 2010
- Ironically, a large portion of the support actually went to foreign banks. (*Ed*: one wonders what US taxpayers feel about that.) The Bank of Scotland, RBS, Societe Generale, Dresdner Bank, Landesbank of Germany and Dexia, all European banks, were all among the ten largest users of the Term Auction Facility (TAF), the facility through which the Fed provided loans of up to three months duration, between December 2007 and 2010, when it closed.
- Barclays borrowed a cumulative $232bn from the TAF – that is simply an extraordinarily large number! In SA terms, that equates to R1 624 trillion!
- In the days leading up to the demise of Lehman Brothers, as private funding for many banks dried up, the Fed support was the greatest. Barclays' largest single day drawdown was $47.9bn, on September 18 – that's just over R1 trillion in one draw down on one day!
- Morgan Stanley also relied heavily on the Fed, drawing between $35bn and $47.6bn *per day* in October 2008.
- Merrill Lynch drew heavily, too, borrowing $33.2bn on September 26; and this amount did not fall below $10bn until December 24.
- Similarly Goldman Sachs used all the facilities at their disposal. Their demand from the Fed peaked at $18bn per day on October 15, 2008, and their daily demand peaked in September at $10bn.

Yet another victory for Emerging Markets
I just have to draw your attention again to the outcome of the FIFA World Cup soccer awards in early December. Even in non-financial terms our **Big Picture Theme** of *The Coming of Age – the rise of emerging markets* is proving prescient. After having been humiliated during the award of the 2016 Olympics (which went to Brazil), developed markets had, yet again, to swallow hard as the 2018 Soccer World Cup was awarded to Russia. Then, adding insult to injury, the 2022 World Cup Final went to Qatar. After 2010, most South Africans will appreciate more fully what it means, economically and otherwise, to host a World Cup Soccer Final. Spare a thought then for Brazil, which faces challenges not dissimilar to those of South Africa in the lead up to the final, such as ageing and inadequate infrastructure, as it works towards hosting both the World Cup Soccer Final in 2014 and the 2016 Olympic Games. The "Age of Emerging Markets" as a theme within the investment world, has a long way to run yet.

The more things change, the more they stay the same.
I must thank you for being so patient and tenacious in having made it to the end of yet another long *Intermezzo*. Your perseverance will be rewarded by a commitment on my part of return next month to the shorter versions that are usually the norm. But I beg your indulgence for one last snippet, this time from a book I read during the holidays about the life of a very remarkable man, Gustav Mahler. It is a fascinating book, which yields more insight into one of the most obsessive and enigmatic composers of all time; a man whose life and music still pose more questions than they provide answers to. I dare you to read it, but be warned, you too, might fall under the spell of Mahler ... and your life will not be the same again. So then, in closing, herewith an excerpt from "Why Mahler? How one man and ten symphonies changed the world" by *Norman Lebrecht*, published by Faber and Faber in 2010. Incidentally there are many, more intriguing quotes and excerpts from the book that I would love to have shared, but in the interests of time I will only share this one. The reason for selecting it will become obvious as you read it – no mention of Mahler here, but it paints the time that he first arrived in the US.

"New York, not yet a wonderful town, is having a year of record influx, 1.25 million immigrants, 11 745 on a single day. The population hits four million. A telegraph link is established to Ireland, allowing newcomers to wire home. The first electric train service runs out of Grand Central Station. The first taxicab plies for trade. The Plaza Hotel opens on Central Park and the windows of Fifth Avenue are a theatre of dreams. It is a year of limitless diversions ... Suddenly, prosperity turns delusional. The Knickerbocker Trust Company's involvement in a fraudulent bid to corner the copper market brings a clamour of depositors to its doorstep, at Thirty-Fourth Street and Fifth Avenue. On 24

MAESTRO
INTERMEZZO
11th Edition | January 2011

October, in The Panic of 1907, bank shares dive and Wall Street trembles. Financiers John Pierpont Morgan and John D. Rockefeller save the day. 'If people will keep their money in the banks, everything will be all right,' declares Morgan as the Knickerbocker president, Charles T. Barney, shoots himself. Ten days later, a leading firm of brokers cannot pay its bills. On Saturday morning, Morgan gathers fifty bankers in his library and, through the weekend, hammers out a deal, which President Theodore Roosevelt okays seconds ahead of the Monday bell. The knife-edge tension leads to the creation of a Federal Reserve to monitor monetary stability. But nothing is fixed. Nothing ever is."

Table 2: MSCI returns to 31 December 2010 (%)

	2010	H2'10	Q4'10	Dec'1
Thailand	50.8	38.4	5.7	3.5
Peru	49.2	45.1	16.6	4.0
Chile	41.8	39.7	5.5	3.0
Colombia	40.8	24.2	-5.6	2.8
Malaysia	32.5	22.8	4.4	5.2
Indonesia	31.2	15.5	-1.1	3.5
South Africa	30.7	39.9	12.6	14.7
Philippines	30.3	23.2	-3.8	9.0
Mexico	26.0	29.2	16.3	5.7
Korea	25.3	32.0	12.8	11.1
EM EMEA	**20.9**	**33.2**	**10.0**	**10.9**
Hong Kong	19.7	26.3	4.3	0.6
Pakistan	19.5	20.8	20.7	9.1
India	19.4	17.3	2.0	7.6
Singapore	18.4	21.9	6.2	4.7
Turkey	18.4	21.5	-7.9	-3.0
Taiwan	18.3	35.8	17.4	12.5
Russia	17.2	31.7	16.5	11.1
EM Asia	**16.6**	**22.6**	**6.9**	**6.2**
MSCI EM	**16.4**	**25.4**	**7.1**	**7.0**
AP ex Japan	**15.0**	**25.4**	**7.1**	**6.7**
Japan	13.4	17.6	12.0	7.5
Poland	12.6	39.9	3.8	10.3
EM LatAm	**12.1**	**26.8**	**5.3**	**6.0**
Morocco	10.8	12.3	4.0	6.9
Australia	10.0	32.8	8.9	10.5
MSCI DM	**9.6**	**22.9**	**8.6**	**7.2**
Egypt	9.5	15.4	4.9	6.6
Brazil	3.8	24.2	2.6	6.6
China	2.3	10.8	0.7	-0.7
Czech	-7.4	11.3	-3.5	8.1
Hungary	-10.7	15.1	-9.4	8.0

Source: Merrill Lynch

Table 3: A selection of 2010 returns

	2009 (%)	Sept quarter (%)	Dec quarter (%)	2010 (%)
Japan	12.9	-0.1	9.2	2.9
Hong Kong	52.2	11.1	3.0	5.3
Germany	23.9	4.4	11.0	16.1
UK	22.1	12.9	6.3	9.0
US (S&P500/ large cap)	27.1	10.7	10.9	15.5
S&P Mid cap index	35.0	12.7	13.1	24.9
S&P Small cap index	23.8	9.3	16.0	25.0
MSCI World index	***27.0***	***13.2***	***8.6***	***9.6***
Brazil	82.7	13.9	-0.2	1.0
Russia	128.6	12.6	17.4	22.5
India	81.0	13.4	2.2	17.4
China	80.0	10.7	5.7	-14.3
MSCI Emerging market	***74.5***	***17.2***	***7.1***	***16.4***
JSE All share	***32.2***	***13.3***	***9.5***	***19.0***
JSE All share ($)	***65.9***	***24.5***	***15.4***	***32.4***
Basic materials	40.9	7.0	15.8	11.7
Financial	28.0	15.1	-0.1	16.6
Industrial	31.0	18.5	7.8	27.4
Large cap (Top40)	31.8	13.4	9.9	17.2
Mid cap index	35.7	13.2	6.6	30.3
Small cap index	28.3	10.1	11.3	24.7
All Bond index	***-1.0***	***8.1***	***0.6***	***14.8***
Cash	***8.9***	***1.7***	***1.5***	***6.9***
Barcap US Agg. Bond index	6.1	2.5	-1.3	7.8
Barcap Global Agg. Bond index	N/A	7.3	-1.3	5.5
US 10-year bond	-12.2	4.5	-5.8	1.3
Cash (US dollar)	0.1	0.0	0.0	0.1
Brent (Oil)	94.1	9.7	15.1	21.6
Gold	27.6	5.1	7.9	27.7
Silver	57.5	17.8	38.8	80.3
Platinum	62.7	8.5	5.6	20.1
Palladium	114.1	28.5	39.1	102.8
Copper	151.3	23.1	20.0	31.0
Nickel	70.00	20.4	7.1	34.5
Baltic Dry index	288.2	6.5	-30.8	-41.0
CRB Com index	23.5	11.0	12.5	13.9
S&P GS Commodity index	61.6	8.9	14.4	18.4
Euro dollar	3.2	11.5	-1.7	-6.5
Sterling dollar	12.3	5.3	-0.6	-3.1
Rand dollar	25.6	9.9	5.4	11.3

Issued by: Maestro Investment Management (Pty) Ltd, Box 1289, Cape Town, 8000. Maestro Investment Management is an Authorised Financial Services Provider operating under Licence number 739 granted by the Financial Services Board on 12 November 2004. The information and opinions in this document have been recorded and arrived at in good faith and from sources believed to be reliable, but no representation or warranty is made to their accuracy or correctness. Maestro accepts no liability whatsoever for any direct, indirect or consequential loss arising from the use of this document or its contents. Please do not reproduce wholly or in part, distribute or publish this document without the consent of Maestro.

Table 4: MSCI global equity market weightings

Market cap weightings as at 1 January 2010

	MSCI Mkt Cap, $bn	MSCI Weight
North America	**11,525**	**46.1**
Canada	1,055	4.2
US	10,470	41.9
Europe	**4,715**	**18.9**
France	1,128	4.5
Germany	826	3.3
Italy	354	1.4
Netherlands	274	1.1
Spain	470	1.9
Sweden	258	1.0
Switzerland	786	3.1
Europe other	619	2.5
UK	**2,207**	**8.8**
Japan	**2,110**	**8.4**
Pacific Rim	**1,261**	**5.0**
Australia	860	3.4
Hong Kong	239	1.0
Pac Rim other	162	0.6
Emerging Markets	**3,157**	**12.6**
Brazil	549	2.2
China	581	2.3
India	243	1.0
Korea	413	1.7
Russia	206	0.8
South Africa	225	0.9
Taiwan	369	1.5
EM other	572	2.3
	24,975	100.0

Table 5: The equity world by sector weight

MSCI Sector weights as a percentage of region; market cap weightings as at 30 November 2010

	Mkt cap (US$bn)	Total	Energy	Materials	Industrials	Cons. Disc.	Staples	Healthcare	Financials	IT	Telecom	Utilities
ACWI	26,140	100.0	11.1	8.9	10.7	10.1	9.7	8.3	20.5	12.1	4.8	4.0
DM	22,572	100.0	10.6	8.0	11.2	10.6	10.1	9.5	19.7	12.0	4.3	4.1
N. America	**12,386**	**100.0**	**13.3**	**5.4**	**10.1**	**10.4**	**10.0**	**10.3**	**16.4**	**17.7**	**3.1**	**3.2**
US	11,196	100.0	12.0	3.7	10.6	11.1	10.7	11.4	14.7	19.3	3.2	3.4
Canada	1,190	100.0	25.7	22.2	5.4	4.1	2.9	0.6	32.0	3.1	2.8	1.2
Europe	**6,456**	**100.0**	**10.3**	**10.5**	**10.9**	**9.1**	**12.8**	**10.1**	**21.3**	**2.8**	**6.8**	**5.5**
Eurozone	2,443	100.0	8.3	8.6	11.1	11.6	10.1	5.7	22.9	3.1	8.8	9.7
France	973	100.0	11.7	7.7	14.6	16.9	11.1	8.0	16.3	2.8	4.0	6.8
Germany	837	100.0	-	15.3	15.6	17.2	4.1	11.0	16.8	6.2	4.3	9.6
Spain	326	100.0	5.4	0.4	6.5	5.4	-	0.5	41.2	0.4	26.8	13.2
UK	**2,193**	**100.0**	**18.6**	**14.4**	**5.0**	**5.6**	**14.5**	**8.5**	**21.0**	**0.8**	**7.3**	**4.2**
Japan	**2,270**	**100.0**	**1.5**	**7.7**	**20.1**	**19.6**	**5.2**	**5.6**	**17.0**	**13.7**	**4.1**	**5.6**
Pacific ex-J	**1,111**	**100.0**	**4.5**	**17.2**	**8.2**	**5.2**	**7.6**	**2.0**	**47.7**	**0.6**	**3.1**	**3.9**
Australia	874	100.0	6.3	29.4	4.3	2.1	10.1	3.2	41.9	0.5	1.3	0.9
Hong Kong	311	100.0	0.3	-	11.0	11.9	-	-	63.2	1.1	0.5	12.0
GEM	**3,569**	**100.0**	**14.1**	**14.5**	**7.3**	**6.8**	**6.8**	**0.8**	**25.6**	**12.7**	**7.8**	**3.4**
EM Asia	**2,073**	**100.0**	**10.1**	**9.5**	**9.6**	**7.8**	**5.3**	**0.9**	**26.3**	**21.3**	**6.5**	**2.5**
China	654	100.0	17.7	5.6	7.7	5.4	5.8	0.8	38.5	5.2	11.6	1.6
Korea	482	100.0	3.0	13.8	16.1	15.1	4.5	0.5	15.4	27.3	2.7	1.5
Taiwan	393	100.0	0.8	13.2	4.0	3.0	1.8	-	14.6	58.0	4.6	-
India	282	100.0	14.4	10.1	10.5	5.1	5.8	4.1	26.9	17.1	0.5	5.4
EMEA	**648**	**100.0**	**24.8**	**17.4**	**3.6**	**5.9**	**4.6**	**1.3**	**28.3**	**0.2**	**10.5**	**3.5**
South Africa	263	100.0	9.7	27.0	4.5	13.5	5.7	2.1	24.9	-	12.6	-
Russia	224	100.0	54.2	15.1	-	-	3.3	-	15.7	-	6.1	5.6
LATAM	**848**	**100.0**	**15.7**	**24.6**	**4.7**	**5.3**	**12.2**	**0.1**	**21.7**	**1.1**	**9.0**	**5.6**
Brazil	566	100.0	22.1	25.4	3.3	4.6	9.0	0.1	26.2	1.7	2.4	5.2
Mexico	164	100.0	-	16.7	5.0	9.9	25.6	-	5.9	-	37.0	-