CREDO NEWS

ISSUE 11 . SUMMER 2012

Ferdinand Foch and the art of investing

Is there any good news left?

The more I see, the less I know for sure

Best Ideas Portfolio

Credo Property

Continues to find value as it completes 2 more acquisitions

Message from the CEO

Roy Ettlinger - CEO, Credo Group

WE ARE ALL IN THE SAME BOAT

Let the games begin

Welcome to our summer 2012 Olympic edition of CREDONEWS

We are now half way through 2012 and summer in London hasn't yet started. Nor it seems have the European politicians, who continue to "kick the can down the road", instead of picking it up and dealing with it, which is not to say that politicians elsewhere are addressing the very real and urgent worldwide economic issues. The immediate crisis is, however, the European one. Certainly others will follow.

The UK press also deflects attention away from the importance of these issues by its continuing unabated "banker bashing" and complaints about "fat cat pay". The "shareholder spring" against CEO remuneration has begun and we are witnessing institutional shareholders voicing their concerns and voting against top executives' corporate remuneration packages, sometimes justifiably, other times less so.

The cries from the many about the inequality in society, are growing louder (this week focussing on individual tax avoidance schemes) and there is clearly a growing expectation that the rich should shoulder ever more of the burden for those less well off.

Whilst those who can afford to do more, bear at the very least, a moral obligation to assist the needy of society, it is worth considering some basic rules of economics, which I was reminded of recently and which I have reproduced below:

"The 5 basic rules of economics:

1. *You cannot legislate the poor into prosperity by legislating the wealthy out of prosperity.*

2. *What one person receives without working for, another person must work for without receiving.*

3. *The government cannot give to anybody anything that the government does not first take from somebody else.*

4. *You cannot multiply wealth by dividing it.*

5. *When half of the people get the idea that they do not have to work because the other half is going to take care of them, and when the other half gets the idea that it does no good to work because somebody else is going to get what they work for,*

that is the beginning of the end of any nation."

So whilst the current environment has many challenges, we are all in the same boat. Our children all face an economy with fewer jobs and fewer opportunities and a Europe that is once again threatened with rising social anger as austerity measures begin to take their toll, while some of the scenes we see on our television screens are perhaps reminiscent of Europe back in the 1930's. Does history teach us anything?

It is undoubtedly true that in times like these, fortunes are both made and lost. We at Credo are continually striving to identify and then take advantage of the opportunities for you our clients and it is very much our focus to preserve our clients' capital and to advise and assist our clients to maximise appropriate opportunities that may surface. Credo's new Chief Investment Officer , Deon Gouws explains in more detail why he believes that now may be the time to invest, on page 4.

Our Best Ideas Portfolio ("BIP") recommendations have proven fairly resilient (see page 6) and Credo's Fixed Income Desk led by Rupert Silver has identified corporate bonds that currently offer good value (see page 8). The ability to invest directly into our BIP and Corporate Bond portfolios within the Old Mutual tax-efficient wrapper is proving to be a popular investment choice amongst our South African resident clients (see page 9). During the last quarter, we have made two very interesting property investments (see page 10) and we have recently invested in a new private equity venture (see page 13).

As always, I thank my colleagues and staff for the hard work and effort that they continually demonstrate in ensuring that we can do our utmost to look after our clients.

We can only hope that while we await the lighting of the Olympic torch in London and the utterance of the words "Let the games begin", the European political leadership stops their game playing and starts making the tough decisions necessary to resolve the urgent and very real issues we face today.

It seems however, as if the Emperor may be fiddling whilst Rome burns.

Diego Barbieri / Shutterstock.com

From Deon's desk

Deon Gouws - *CIO, Credo Capital*

Ferdinand Foch and the art of investing

To many investors, it may appear as if the world is falling apart in economic terms as we speak.

Is there any good news left?

Europe has been a mess for years now, with the so-called PIIGS falling like dominoes as their respective states of relative bankruptcy become increasingly evident. As a result, no serious commentator seems to give the euro any chance of surviving as a unifying currency in its present form much beyond the end of the second quarter of 2012.

The UK confessed to a double-dip recession a couple of months ago, which no doubt played on voters' minds in the recent local government elections – causing the biggest downturn in fortunes of prime minister David Cameron and his coalition since originally being chosen to govern the country a short two years ago (even though it feels like an eternity has passed since then). Not to mention all the austerity measures beginning to bite in the UK… is it really possible to shrink your way to greatness?

Emerging markets have also started failing us, with the much-publicised BRICS economies seeming to run out of steam. The most significant of these, China (set to take over as the world's largest economy within perhaps the next five years or so), has probably been the biggest disappointment, with a property bubble bursting and growth suddenly slowing – all leading to a drop in fortunes of, specifically, commodity companies around the world.

The only real glimmer of hope appears to emanate from the United States – even though every jobs report that surprises on the upside seems to be followed by at least three further economic indicators missing expectations (in spite of the fact that these have already been revised downwards a few times in succession).

Part of the reason for all the doom and gloom is of course the fact that the prospects for global banks still appear to be unexciting. Normally major drivers of world economic growth (and consequently also some of its main beneficiaries), the big banks, on balance, are still loathe to lend (except of course to those who don't actually need any funding!) – a consequence not only of a very different risk appetite following the 2008 financial crisis, but also a function of regulatory regimes that are stricter than ever before. In addition, fears still abound as far as the relative health of bank balance sheets is concerned: how much are those bonds issued by bankrupt governments and counter-party banks with exposure to dodgy property developments on the Costa del Sol, really worth?

It is therefore understandable that many investors no longer have any appetite for risk. There is perhaps no better illustration of this than the popularity of "safe haven" alternatives such as German treasury bonds, the yields of which recently turned negative – meaning that investors are literally paying the government to borrow money from them (thereby going one significant step for mankind further than simply hiding a few euros under the mattress).

Against this dire background, I am reminded of the famous words of Marshall Ferdinand Foch at the time of commanding the French Ninth Army during the First Battle of the Marne in 1914:

"Hard pressed on my right. My center is yielding. Impossible to maneuver. Situation excellent. I attack."

Not only did this contrarian approach (and the surprise tactics that were part and parcel of it) yield successful results and lead to an eventual German retreat a few weeks after Foch uttered the famous words nearly a century ago, but I also believe that it provides a useful point of departure in terms of articulating investment strategy during troubled economic times such as the present. This ultimately leads to a conclusion in terms of which the time is probably right to selectively start increasing one's exposure to risky assets (specifically equities).

I am fully cognisant of the fact that equity markets can take a "leg down" from current levels – if the truth be told, we should in fact all recognise that this is always a possibility, regardless of market conditions, index levels or economic news-flow (just consider the after-effects of an "unknown unknown" such as September 11).

Having said that, I also believe that carefully adding to one's equity exposure in the present environment is likely to reward the patient investor over time. Global indices are trading well below levels seen five years ago and now seem relatively cheap in terms of practically every metric – this, in spite of the fact that constituent companies have, on balance, grown profits strongly and improved their balance sheets considerably over this period.

I do not know exactly how the European situation will ultimately play out – if I did, I would probably be able to make a lot of money as a fortune-teller (if not be a recipient of the Nobel Prize in Economics!).

But after all is said and done, Europe will continue to exist, Europeans will still wake up in the morning, drink coffee, eat breakfast and get on with their lives (even if somewhat less comfortably than before). And there will be world-class companies that continue to sell food and drink and medicine and transport and airtime to those people on a daily basis (not to mention all those other consumers in different parts of the world who are somewhat less affected by the debates in Brussels and Berlin) – and many of these companies now trade at pretty compelling multiples.

If one has a diversified portfolio of attractively valued, quality counters (such as Credo's Best Ideas Portfolio), I therefore believe that it's probably best to ignore the market swings that we've seen recently. With a very high probability, I would argue that a portfolio such as this should provide an investor with inflation-beating capital growth over the longer term (not to mention quite a healthy dividend yield on a consistent basis in the interim).

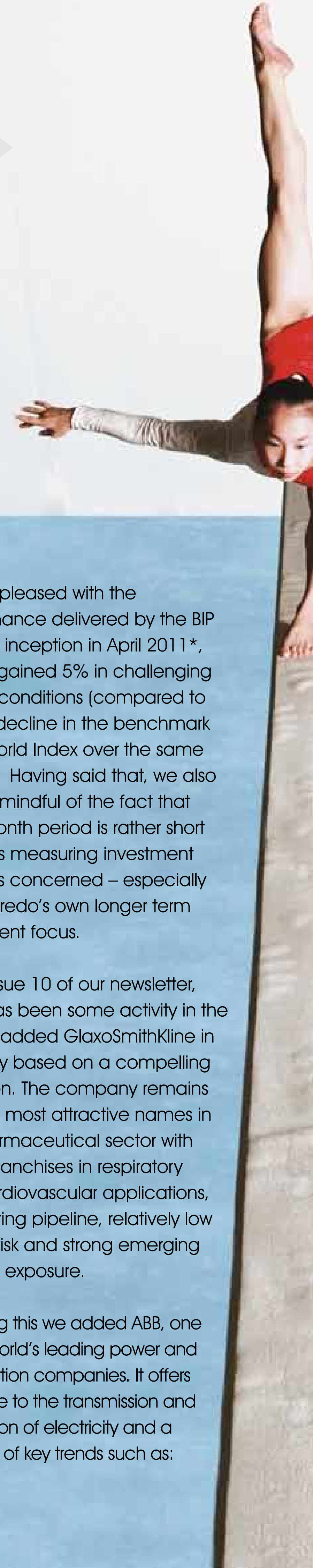
Hard pressed on my right, the center yielding… impossible to maneuver?

Situation excellent: I invest.

Asset Management

Rikky Shoker - *Relationship Manager, Credo Capital*

The more I see, the less I know for sure...



This year markets have once again endured a roller coaster ride. We began 2012 on a bullish note: US data was surprisingly to the upside, concerns over a Greek exit were swiftly brushed under the carpet – for the time being at least – and a co-ordinated easing programme led by US and European central banks saw liquidity flow into risky assets at an unprecedented rate. The S&P500 posted the largest first quarter gain since 1998 - though from deeply oversold levels - and many of the stocks held in the Best Ideas Portfolio (BIP) either hit new highs or broke out of multi-year trading ranges.

Despite the growing optimism, hiding under the covers was a very different reality. Storm clouds continued to brew over Europe, US growth was still trending below average and the Chinese economy moderated somewhat. Academics often refer to this as an inefficient or irrational market; a tendency for prices to overshoot to the upside (or downside for that matter) taking many casualties along the way. As John Maynard Keynes eloquently put it:

"The market can stay irrational longer than you and I can stay solvent."

Asset prices can sometimes trade above or below their true intrinsic values for years. A virtue of good asset management is to identity these inefficiencies as and when they occur.

Although typically random in nature, markets have recently appeared to exhibit a degree of predictability. A strong end to Q4 precedes an even stronger Q1, which then sets the stage for a volatile Q2 and correction for much of Q3 and so on. This year has been no exception to the rule. The mantra to "sell in May and go away" appears to be operating like clockwork and at the time of writing this article, a correction seemed to be well under way.

As reported in April, we remained cynical of the rally and adopted a cautious stance. Unsurprisingly, a potential break-up of the European Union is back on the cards coupled with a simultaneous slowdown in global economic activity. Which of these two events is the cause or effect remains to be seen.

We are pleased with the performance delivered by the BIP since its inception in April 2011*, having gained 5% in challenging market conditions (compared to a 10% decline in the benchmark MSCI World Index over the same period). Having said that, we also remain mindful of the fact that a 14 month period is rather short as far as measuring investment returns is concerned – especially given Credo's own longer term investment focus.

Since Issue 10 of our newsletter, there has been some activity in the BIP. We added GlaxoSmithKline in February based on a compelling valuation. The company remains one the most attractive names in the Pharmaceutical sector with strong franchises in respiratory and cardiovascular applications, a maturing pipeline, relatively low patent risk and strong emerging markets exposure.

Following this we added ABB, one of the world's leading power and automation companies. It offers exposure to the transmission and distribution of electricity and a number of key trends such as:

A BALANCED APPROACH

increasing demand for reliable and efficient electricity, particularly in emerging markets; structural growth of automation; and the replacement of rapidly ageing global power infrastructure in the US and Europe. The stock continues to trade close to trough P/E multiples on 11.5x and offers exposure to a robust structural theme.

Finally we removed Procter & Gamble in May, having held the company for over 12 months. During this period the stock struggled to break out of a multi-year trading range owing to an unexpected deterioration in sector fundamentals. As a result we identified a consumer staple peer (Diageo) that offers an even stronger growth profile, wider economic moat and similar valuation. Diageo is the world's largest spirit company with 30% global market share and arguably the strongest brand portfolio in the sector. Given that 40% of sales are generated from emerging markets, the company is well exposed to a growing global middle class which is set to double by 2020. Diageo is also benefiting from the structural growth in spirit consumption in key developed markets, such as the US, where they are number one.

Looking forward, we acknowledge that downside risks seem to have risen sharply – although one could argue that they were never entirely removed. The spectre of a Greek exit is once again up for debate, although less likely given the risk of wide spread contagion that this might cause. Furthermore the US economy has once again hit a soft patch and the data coming out of China continues to point to a slowdown. Nevertheless we believe the BIP is well positioned to weather any forthcoming shocks to the global economy or markets: we remain well diversified by region, currency and industry; the portfolio has a large weighting to core defensive names that are more likely to protect capital in the event of any turmoil; most of the companies we own boast strong balance sheets with large cash reserves; and our stocks benefit from a diversified earning base with a relatively low dependence on Europe.

For the remainder of the year, we expect markets to remain volatile. We can't ignore the potential for a Lehman's type event; even though we would argue that investors seem better prepared this time around. As such, in the current environment we believe it's important for investors to remain rational, especially since markets rarely do. Share price movements are very much driven by daily news' flow and macroeconomic data as opposed to underlying company fundamentals. To quote John Lennon:

"The more I see, the less I know for sure..."

We are strong proponents of this view. Such noise usually creates panic/euphoria as investors overreact to short term news' flow. But it also presents potentially lucrative opportunities, where asset prices detach from fundamentals. As a result, we remain on our guard and maintain our disciplined long term approach to investing. We expect a number of market dislocations going forward and will be well positioned to respond as they arise.

(*) Performances based on pricing as at 14/06/2012.

Rupert Silver *- Senior Portfolio Manager, Credo Capital*

Focus on Fixed Income

Most bond investors simply want a steady and positive return to complement an equity portfolio or perhaps as a lower risk alternative. Where in the fixed income world should an investor position himself when searching for the best return relative to the risk he is prepared to tolerate? Whilst it's impossible to know what the future holds, there are certain areas that currently offer superior relative value:

1) Stay Corporate: Government bonds have been in a bull market now for 30 years which must end at some point. The current yield on the UK 10 year Gilt is 1.7% and on the US30 year Treasury is 2.7%. The long term investor is not being rewarded and is losing purchasing power against current inflation rates. He also faces significant downside risk in the event of rising rates. Corporate and financial issuers do however offer the returns that Sovereigns lack and arguably in some cases with less risk!

2) Aim for the middle: The BBB space is where companies are adequately funded, risk remains low but returns are highly attractive. As a general rule the AAA/AA bonds are highly correlated to the Government bond market, so yields are low and sensitivity to interest rate movement is high. With anaemic growth and much uncertainty, the environment is not right for Junk bonds/high yield, which tend to outperform when the economy is strong.

3) Don't go too long (unless handsomely compensated): A recent Morgan Stanley study shows one half of the excess return generated by US corporate bonds can be generated in a 7 year portfolio! In the UK it appears that these excess returns can be found up until 9 or 10 years at most. Investors who buy longer than this are taking unnecessary interest rate risk for only slightly higher returns.

4) Better the devil you know: Whilst the European crisis may eventually blow over there is too much uncertainty at the moment. We feel much more comfortable investing in the UK and the US, particularly when investing in financial bonds.

5) Insurers are in the "sweet spot": Financials still offer much higher returns than corporates but volatility is certainly higher in this space and rightly so! We feel comfortable owning the major banks to significantly enhance returns. The real sweet spot however lies with the Insurers. These bonds tend to give returns almost as high as banks but don't have the funding issues and risks associated with banks which can be subject to a "run."

Of course any good portfolio needs diversity and never more so than in the current environment. Some bond investors have strict parameters around which they have to invest. Maybe they can only buy certain sectors, bonds rated above a certain level, bonds paying a specific amount or perhaps bonds redeeming at a specific date to offset other liabilities. For those investors who are not restricted in this way, the guideline above is not a blueprint for every fixed income portfolio but a good place to be positioned if you have some flexibility or seek some direction.

Investors looking for an example of the above might look at the Old Mutual 8% 2021. It ticks all the boxes above and offered at par gives Investors a fixed 8% p.a. in Sterling. The Bonds are Investment Grade, have less than 9 years to run and usually have good liquidity.

Email rsilver@credogroup.com for more information.

***Alan Noik** - Managing Director, Credo Capital*

Credo and the Old Mutual Investment Portfolio

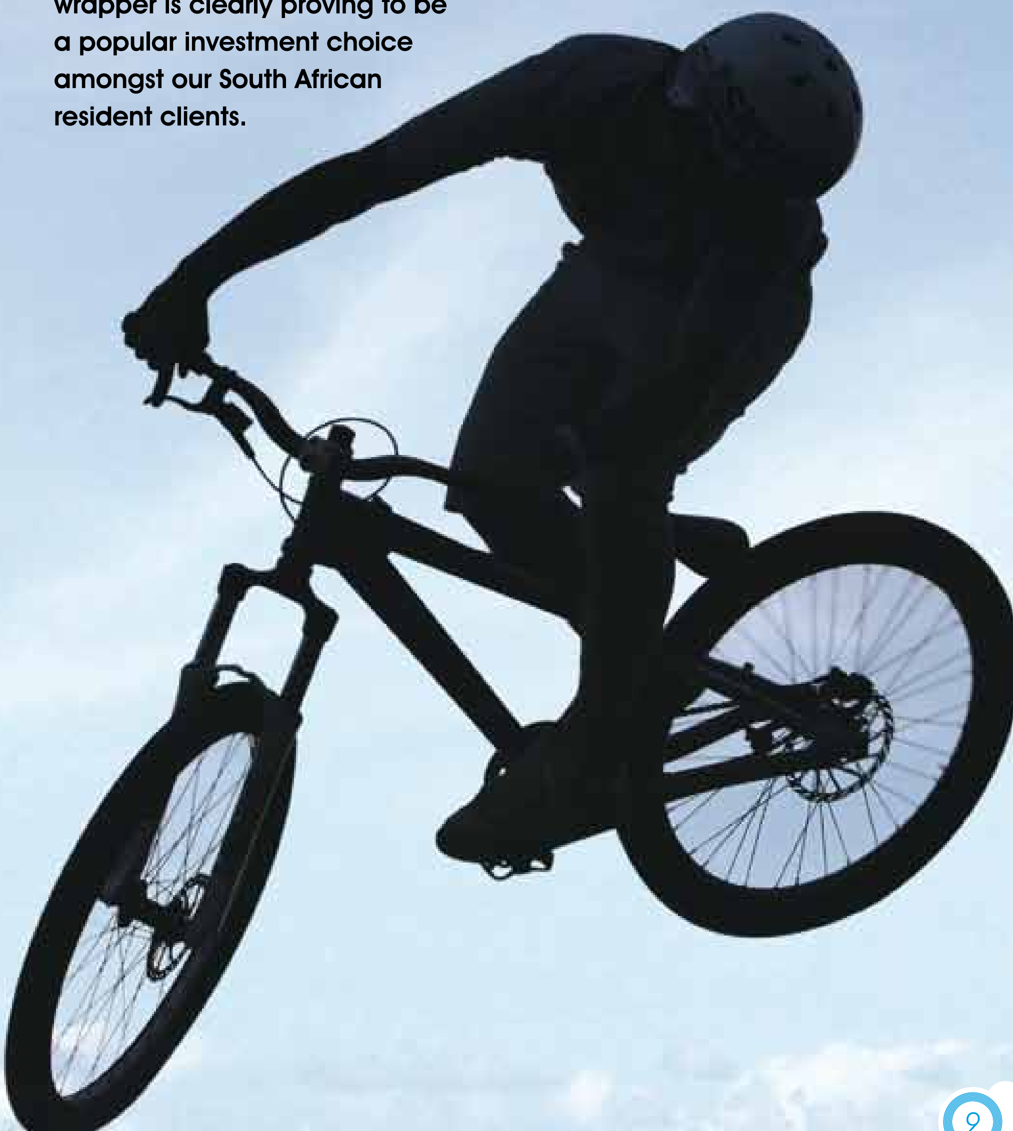
Since being appointed as a preferred investment manager for the Old Mutual International Investment Portfolio, Credo Capital has presented this opportunity to over 600 financial advisors and private clients at a national road show which covered 6 of the major financial centres in South Africa.

The Investment Portfolio allows South African resident investors to consolidate and manage their offshore investments within a single, highly tax-efficient wrapper.

The Investment Portfolio is issued by Old Mutual Isle of Man, which is part of the Old Mutual Group, with Old Mutual Plc being a FTSE 100 company. From a South African tax payer's point of view the tax benefits are significant – the biggest advantage of the tax-wrapper is the ability for South Africans to invest overseas tax-free.

Since the launch in March we have seen good inflows, particularly into our Best Ideas Portfolio and into our Corporate Bond portfolios. The ability to invest directly into global companies within a tax-efficient wrapper is clearly proving to be a popular investment choice amongst our South African resident clients.

For more information on this investment opportunity please contact your Relationship Manager.



Gavin Rabinowitz - *MD, Credo Property Group*

Credo Property continues to find value

"There is definitely a two tier market in the UK - London and the rest!"

London has been more resilient than the rest of the United Kingdom as the weight of money from overseas and UK investors continues to look for a safe haven. Foreign investors continue to invest in both commercial and residential property in London. Prices for commercial property in prime locations are commanding record high prices. In our opinion, this is hard to justify especially where there is weak tenant demand and no real rental growth. Residential property in good locations is attracting high prices. We believe this trend will continue with the increased uncertainty in Europe.

Credo has recently invested into a joint-venture vehicle which purchased a substantial freehold office building in central London on a short lease. The intention is to benefit from the strong demand for good quality central London residential property through submitting a planning application for a change of use to residential flats and, if successful to either sell the site with the benefit of the planning permission or to carry out the residential refurbishment and then sell the units.

"The strategy is to buy office space off sensible capital values and then change the use to the more valuable residential."

Credo has also invested in another joint-venture vehicle that has acquired a freehold retail warehouse in the major retailing and commercial centre of East Anglia. The property is leased to a good tenant with 3 years remaining and was acquired for a purchase price that reflects a net yield of 11.25%. The intention is to negotiate with the current and potential tenants of the property for a lease extension or grant of a new lease.

This opportunity provides a strong cash return with the possibility of capital appreciation once a new lease is agreed.

We believe that 2012 will offer a significant buying opportunity for these types of real estate transactions which we hope will provide strong returns to our investors.

If you are interested in these or further property opportunities please contact your Relationship Manager or email: grabinowitz@credogroup.com

RAISING THE BAR

Sportsphotographer.eu / Shutterstock.com

Stockbroking

Kim Simon - *Relationship Manager, Credo Capital*

MyCredo

Trade order entry

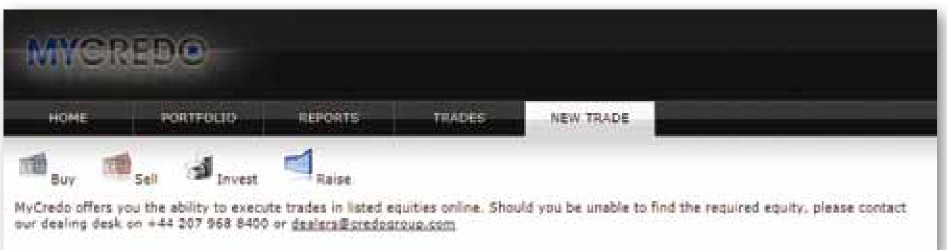
MyCredo continues to provide our clients with a secure, seamless online reporting tool.

MyCredo now offers a trade order entry function for the Private Client.

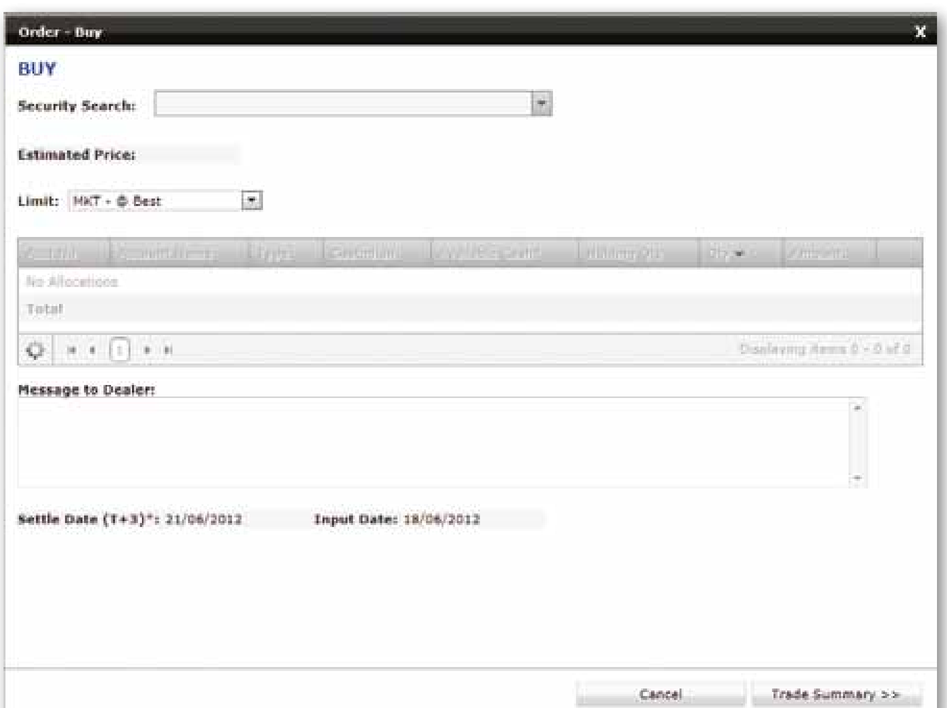
The client has the ability to enter their own trades for the purchase or sale of listed equities on the main global exchanges. In time, we aim to expand the spectrum of securities available through this function.

MyCredo app

At Credo we always try to remain on top of our game. With that in mind we are proud to announce the imminent release of our MyCredo mobile app which will be available on Apple and Android devices.



Online trading options



Trade submission form

Portfolio valuation view

Private Equity

Barry Stillerman - *Relationship Manager, Credo Capital*

Private Equity for Private Investors

During these difficult economic times, we are constantly seeking added value opportunities for our clients. This may come in the form of a bespoke property investment or a private equity situation that offers the prospects for capital growth.

The withdrawal of banks from the financing of small and medium enterprises has prevented the expansion of many UK businesses that have a good product range. This gap is currently being filled by private investors funding private companies.

Investors must recognise the higher risks involved and lack of liquidity but a small allocation of funds to a well spread range of private equity investments can add value for investors seeking a higher risk and reward returns. In addition, there are attractive tax benefits that may be available.

It is necessary to approach private equity investments with caution and adopt a carefully considered strategy in the selection of potential targets companies. The criteria used includes seeking businesses that have a competitive advantage with sound honest management in a growth sector and an exit plan that is likely to be attractive to investors.

By way of illustration, a recent private equity investment that we have arranged is in Haberman Products Ltd. The company was founded by Mandy Haberman, a successful inventor. Her success was borne out of necessity as her third child was borne with a cleft palate and, at the time, there was no bottle on the market for babies with this feeding difficulty. Mandy invented a bottle that overcame this problem and her invention is still used in hospitals today.

Mandy Haberman

Some years later she invented the first non-spill drinking cup. Her Anywayup cup took the market by storm both in the UK and in overseas markets.

Mandy and her team have now invented another ground-breaking baby feeding product that is shortly to be launched. The unique feature of the product is that during use, the teat remains filled with milk, not air (just like a breast) responding to suckling, not sucking (just like a breast).

It works as nature intended and so naturally reduces the problems caused by the artificial action of other bottles. It reduces nipple confusion, enabling mother and baby to switch more easily between the breast and bottle. Dads can help out at night and a mother's career does not have to be put on hold.

This new invention sets a new standard in colic reduction. It also promotes natural feeding rather than over feeding associated with the market leading bottles. It is at least as simple and intuitive to use and clean as the market leaders. There are also planned 'development stages' to support the rapid developments of a baby.

The UK economy needs the growth of private UK businesses that can grow profitably and expand their workforce, taking more people off the dole. More needs to be done at Government level to unblock the lack of finance to industry but in the meantime private equity investments can help the economy. Equity stakes are easier to negotiate when the market has stalled.

A carefully selected mix of private equity investments can add value for the appropriate investor while still keeping within the chosen risk profile so long as the portfolio is a small part of assets held.

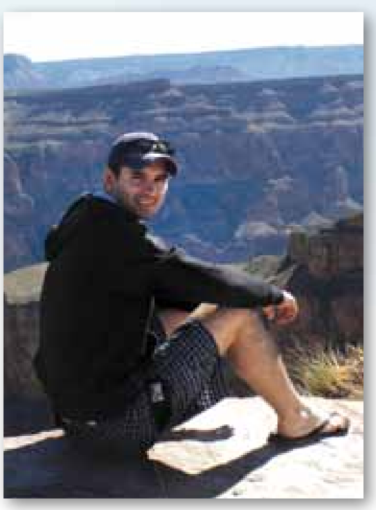
Company News

Sara Ettlinger *- Director, Credo Property Group*

It's all about the team

The Credo Team grows again: our two new employees will expand our team in our London office.

Ainsley To joined Credo as a Research Analyst from Stamford Associates where he was an Investment Analyst. He has also previously worked as an Associate at Fidelity International and an Analyst at Bloomberg LP. Ainsley graduated from Imperial College London and went on to complete Level III of the CFA programme in June 2010. Being a well-rounded individual, his hobbies include football and more football.



Gareth Crosland joined Credo as a Junior Relationship Manager. He is a South African Chartered Accountant who trained with Ernst & Young in Cape Town prior to joining Credo. He is originally from Zimbabwe but moved to South Africa to complete his undergraduate and postgraduate degrees at the University of Cape Town. Gareth is interested in most sports but particularly rugby, cricket and beach volleyball.

Golf Day 2012

"A day was spent in a round of strenuous idleness" as Credo held its 2012 golf day at Brocket Hall which claims to be one of the finest and most exclusive golf clubs in the United Kingdom. The winners of the day were Alan Noik, Steven Isaacs, Richard Jaffee and Sean Steyn.

The winners: Alan Noik, Steven Isaacs, Richard Jaffee and Sean Steyn

The runners up: Colin Froman, Jeff Maze, Nelius Kriel and Arnie Witkin with Roy Ettlinger

Credo makes the news... Follow us.

Credo Executives have continued to share their successes, experience and views in many publications in the UK and South Africa.

Deon Gouws, Credo's CIO, comments on the state of the institutional fund management industry in South Africa, and motivates why he shares in the excitement about Africa as an investment destination. *"Africa has the potential for significant growth through import substitution, intraregional trade as well as traditional export markets."* (Afrikaans business magazine, Finweek in South Africa.)

Rupert Silver, Credo Capital's head of fixed-income desk was interviewed for Investors Monthly in South Africa about the market in corporate debt in which he states *"Corporate debt has been very popular since 2009 and we don't think this will change much. With equity markets broadly flat over 10 years and with cash giving next to nothing, the relatively high yields available on trusted corporations seem very attractive to many private investors, who aren't in the main worried about the ups and downs in the market so long as they continue to 'clip coupons'."* (Clipping coupons refers to the constant income that is earned from the coupon payments made on corporate bonds.)

Jarrod Cahn, Senior Portfolio manager was interviewed for Moneyweb South Africa about the rumours of a Pick n Pay /Woolworths Australia tie up. In addition in February 2012, Citywire's stocktake column featured Jarrod talking about the Credo Best Ideas Portfolio in which he advises that the shares of *"credit card providers and luxury goods are the ones to watch".*

Alan Noik, MD Credo Capital was featured as Citywire's "Gatekeeper" and explains that: *"Transparency and performance are what it's all about when selecting a fund for our clients. We like to meet often with the fund managers and monitor performance closely. The moment we feel things are slipping, we act quickly and decisively."* Alan also featured in Investors Monthly commenting that *"With the poor past performance of some offshore funds, some see better value in direct equity holdings. Our high-conviction portfolios include 15 to 20 of these blue-chip stocks."*

To keep up with our news as it happens, check out our:

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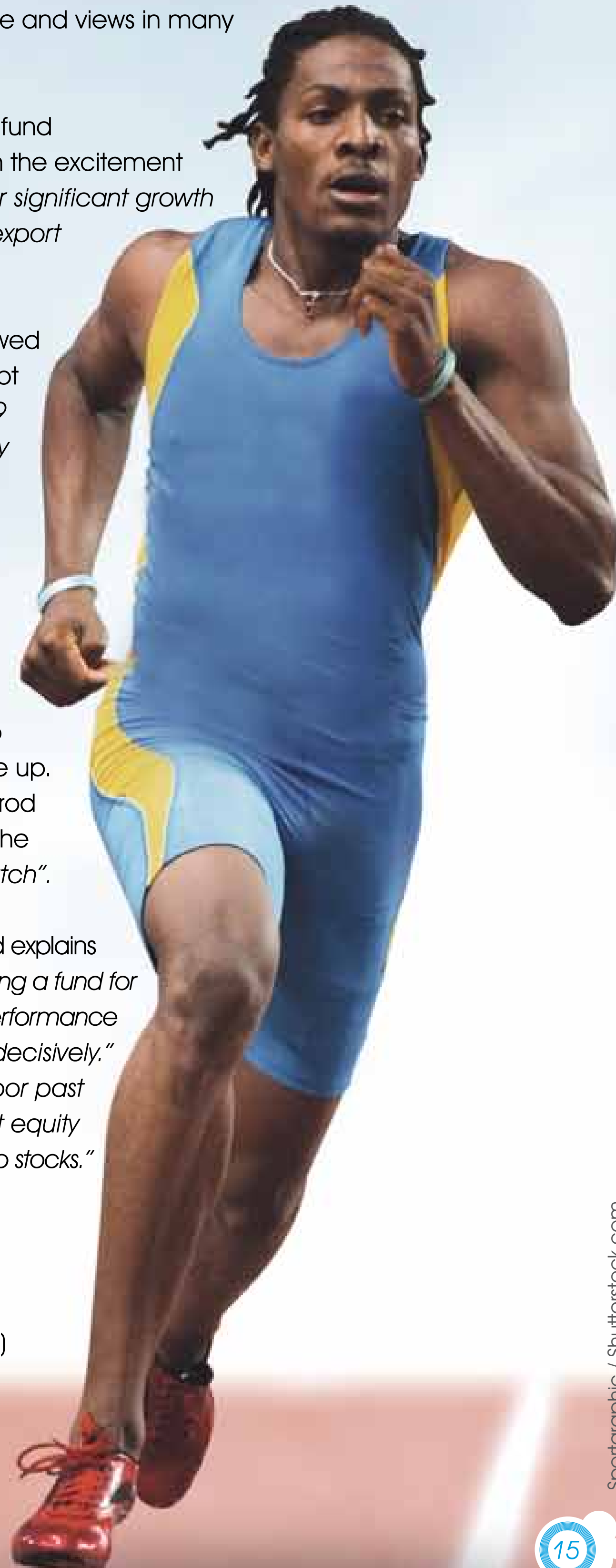

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