

Investment Outlook for First Quarter 2012

2012 will be a pivotal year in many respects. We shall see elections and possibly new leaders in the USA, France, Russia and China (by politburo appointment rather than elections). In addition, changes could come in Japan and Thailand. The Middle East will continue to be dominated by political unrest, and the oil price will reflect this concern. Although in the short term the US Dollar has staged a strong recovery against the Euro especially, but also all other currencies and commodities, we do not expect that this will alter the long term trend of decline.

The outlook for the Global Economy in 2012 is currently dominated by pessimism and downgrades stemming from the uncertainty about Europe and European banks, and how that will affect the global credit situation. We therefore have to temper our customary optimism about Asia and Emerging Markets with a sober assessment of what a decline in growth in Europe, and probably in China, may mean for markets and for key commodities. The latest reports from China indicate a sharp fall in the overheated property markets in major cities, with transaction volumes dropping quickly and prices in some cases falling by 25%. Urbanisation will continue to be a major trend. Our November conference in Hong Kong focussed on the shift in the Chinese economy towards the consumer and this still represents a very significant opportunity for retail, travel and tourism, financial products, as well as other personal consumer items. Experience has taught us that it is usually more rewarding to play Chinese demands indirectly, through companies listed in Hong Kong or elsewhere, than directly in the Shanghai market. Both growth and inflation will fall in 2012 compared to 2011 and this will enable the Chinese authorities to ease their tight money policy for the depressed Shanghai A share market to stage a recovery.

India has seen the worst performance recently, made more depressing for investors by the sharp fall in the Rupee, to 53 Rupees to the Dollar, or down 20% in the last year. The combination of a higher oil price, high inflation and interest rates, a slowdown in industrial production and a lack of confidence in the New Delhi government (which withdrew its plan to reform the retail sector recently) has depressed sentiment among Bombay investors. Our recent strategy call concluded that the Rupee was now oversold, as well as the market, but few are prepared to bet on Indian shares recovering strongly. In some sense, this is the epitome of the Emerging Market dilemma – that growth continues at 6-7% - but share markets (and currencies) disappoint investors.

While it is impossible to time the recovery, we see some signs of hope. The US economy is bottoming out, export orders remain strong, and the emerging markets will eventually reflect this recovery. South East Asia continues to perform relatively well, with Indonesia, Thailand and Malaysia all out performing the Asian benchmark on strong corporate earnings, regionally and with some help from China.

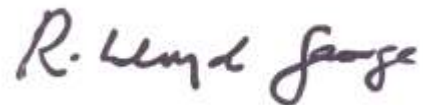
In Latin America we see no political change and continued economic growth, although the uncertainty over commodity markets will certainly affect Brazil (Iron Ore), Chile and Peru (Copper and Gold), and Argentina (Oil, Gas and Agricultural commodities). Nevertheless, the new oil finds in the Southern Hemisphere have helped sentiment and the financial

position of Brazil is stronger than we have ever seen it. The Real should fall against the US Dollar to a more competitive rate and this will help the export industry, although our focus is really on the domestic consumer in Brazil, as it is in Asia.

Recent events in Russia have also created a climate of political uncertainty, with the election in March 2012 not being such a foregone conclusion for Putin. Both the Rouble and the market have weakened and the market remains clouded, although the oil price as always will be the key indicator for Russian Equities. Eastern Europe is affected by the slowdown in Western Europe, as too is Turkey, which has both inflation and currency weakness to contend with. In South Africa we have focussed our investment on healthcare and consumer opportunities, which have performed well in the face of the falling Rand and difficulties in the mining sector.

In preparing for the New Year we have reviewed all our key positions to focus on strong cash flow and balance sheets, good dividend yields and dividend cover, and leading market positions. We are very conscious of downside risks, whether in currencies or in specific geographies and sectors. The key note is the conservation of capital and good income yields. Everything is now connected in the investment world and it is very difficult to find non correlated assets, except possibly in the Frontier markets. We must expect the unexpected and focus on good stock selection as a defence against the macro instability which we will continue to experience.

We wish all our clients and readers a very happy Christmas and successful year of the Dragon.



Robert Lloyd George
19th December 2011