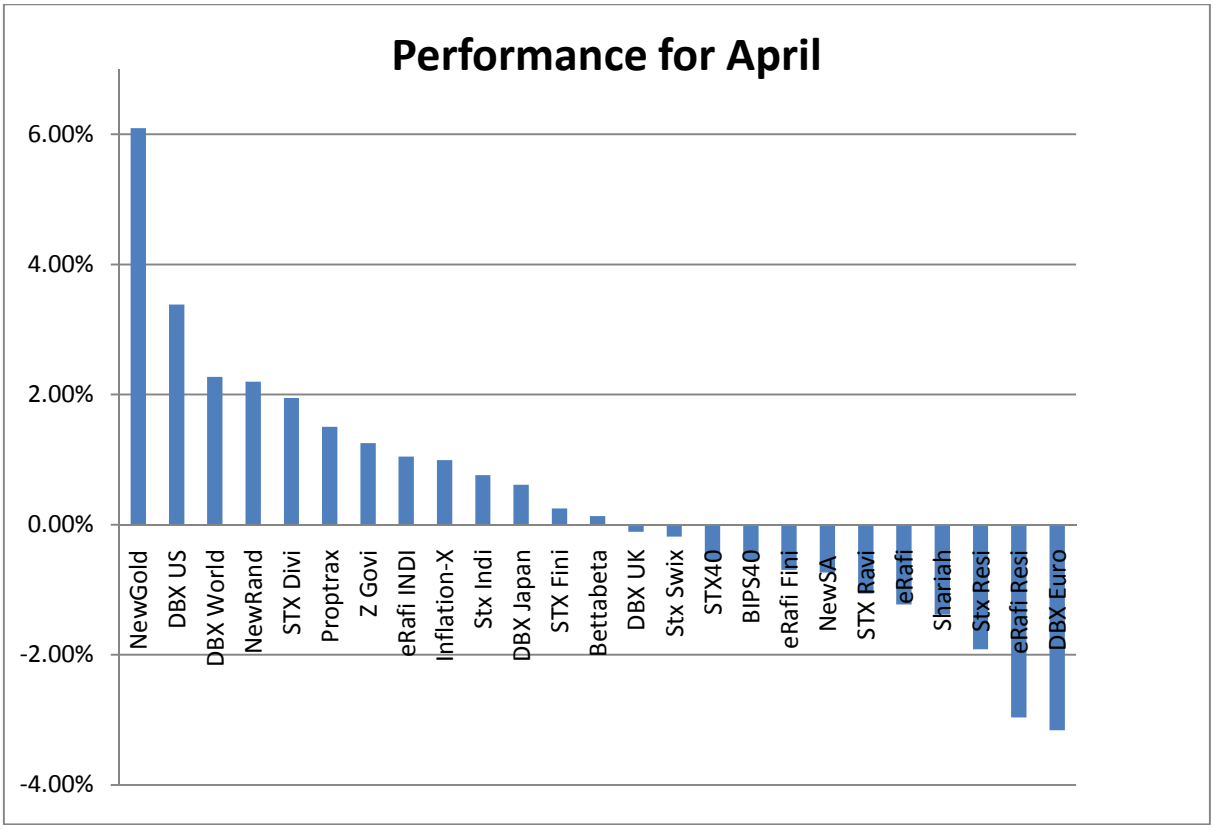
AND JUST WHEN YOU THOUGHT BLUE SKIES WERE UP AHEAD...

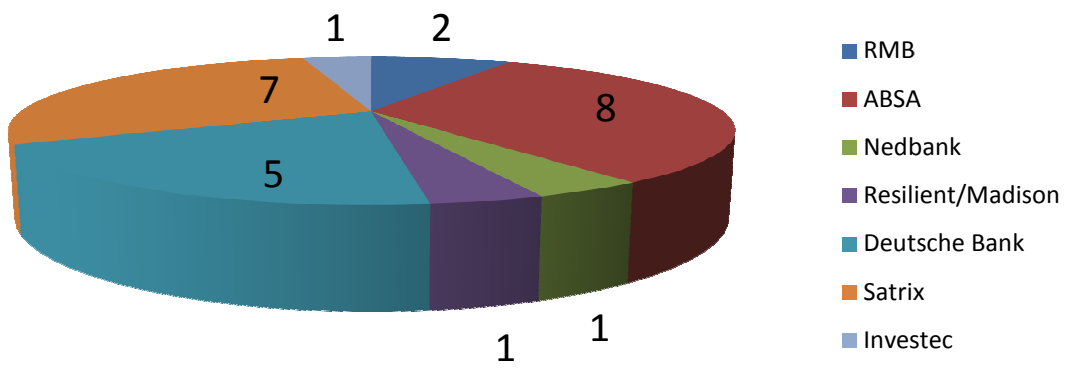
In last month's ETF watch, we noted how the Top 40 index, a year on from the bottom of its debt induced depression, had mocked all doomsayers and pessimists with a positive 7.6% return for the month. The message was clear and delivered in the style we've come to expect from our precocious emerging market index: Risk? What risk? But before you could say Eyjafjallajokull and get odds from your local bookie on Julius Malema and Goldman Sachs being in the same boat (that boat being called K-A-K, Mr Blankfein) dark clouds came-a-looming and suddenly global investors weren't quite the high stakes poker players they thought they were post the month of March. The bull run, like that planned excursion to London for the winter, came to a grinding halt.

We then had all the sniffling from doomsayers telling us how the market had run too hard, how it was time for a correction and how the cloud over Europe was going to be around for 18 months potentially grounding all flights and in the process freezing the global economy ....blah blah blah. But markets are funny things. Ben Graham's metaphor of the market being described as a manic depressive little character (like Gollum if you will) that comes knocking on your door with prices linked to his depressed or elated state-of-mind, and rarely based on any rational, measured thought, seems more meaningful with the events of March and April in context. So surprisingly to some, it did come to pass that the world and her economy did continue, shaken but not stirred, and South Africa, despite noteworthy efforts from the extreme right and left, did not descend into an all out racial war. The World Cup too, remains on track. So how did our ETFs do?



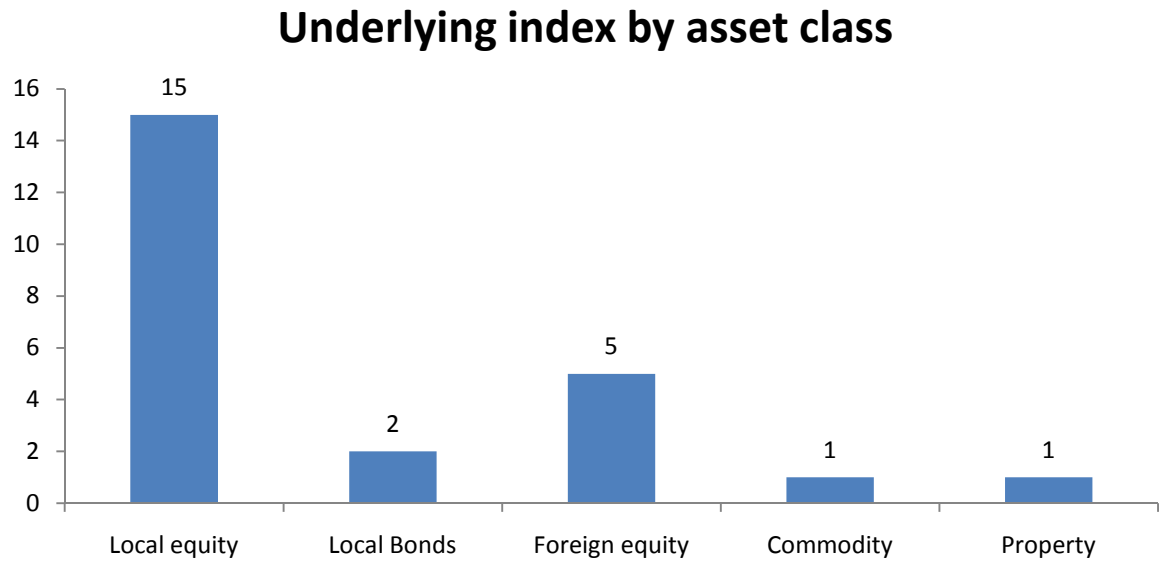
The Top 40 index posted a modest loss of -0.79%. This was followed by the usual mob: Satrix 40/Bips 40 both followed with declines of -0.54%. Mr Market clearly got the better of the fundamental strategies because the ABSA eRAFI and the Satrix RAFI both declined by over 1%. The newcomer, Nedbanks Bettabeta enjoyed some steady trade in its first full month on the exchange with 72,000 units changing hands, and a slight gain of 0.13% to get its foot in the door. Its intellectual equivalent, the Satrix Swix, posted a decline of -0.18%. The common link comes in the result the two are trying to achieve, and that is to further diversify a very resources heavy index like the Top 40. The Bettabeta does this by giving each of the 40 companies an equal weighting of 2.5% in the index. That means a relatively smaller company like Nedbank has just as much effect on the performance of the index as the gigantic BHP. So the playing fields get levelled. Consequently you get a more even spread between the different categories of shares which include Financials, Resources, Industrials and Consumer Goods followed by a smattering of Telecoms, Oil and Healthcare.
The Swix instead tries to achieve this by reducing the weighting of the big shares that have a large amount of foreign owners (these are usually the big resource giants that have their main listings elsewhere). The foreign component of their market cap is therefore excluded when calculating their respective size within the index. The objective of both is not so much to effect a change in performance, but rather to achieve a more even diversification.

Number of ETFs per Issuer



As we know, its lekker when those resource okes show up to a party because you're always guaranteed fireworks, but when the tide turns, it may not be so wise to be too reliant on them. This was certainly the case this month when the Resource index declined by -1.75%. Consequently the eRafi Resi and Satrix Resi were almost the worst performers for the month with losses of -2.96% and -1.92% respectively. The wooden spoon award goes to holders of the DBX Euro, which declined by -3.16%. This is largely in response to the dire state of Greece's finances, which will certainly necessitate a bail out. The misery for DBX Euro holders YTD now totals a cumulative loss of -12%. With all this fear and loathing around, Gold spotted its chance to wipe the smile off the faces of all those blue-eyed optimists, and this resulted in the ABSA Newgold posting a heartwarming 6.10%. 2nd and 3rd place went to DBX US and DBX World (both Dollar denominated, as I mentioned last month - pay attention) with positive gains of 3.40% and 2.27%. They did get by with a little help from their friends though – the Rand depreciated by 1.5%.

All this month-to-month focus exhausts this author and detracts from the real advantages of ETFs. That is a. You don't need to monitor them like a futures position in Simmer and Jack because they follow the entire market and b. You don't need to spend time figuring out which ones to buy and which ones to sell, because they follow the market. All you have to do is figure how your portfolio be allocated by sitting down with a good financial advisor and deciding on the spread between equity, bonds, property and cash, as well as the mix between foreign and local exposure. This should take an hour tops per year. Then you setup the debit orders to automate the transfer of cash from your bank account into your investment account every month (again this will take an hour tops). After all the hard work is done hand over responsibility to our good friend 'compounding interest' whose as reliable as all hell, and watch him work his magic over years, preferably decades (if you're on the lighter side of WW2). That's why ETFs are really called passive investments.



The benefits of a regular monthly contribution to a cheap index tracker (commonly referred to as Rand-cost averaging) cannot be overstated. I challenge anyone in the world of finance to offer a more sage piece of investment advice. And just remember who you received this from, yours truly.

Glossary – or Dummy's Guide – for you red-hot keen rookies

ETF or Exchange Traded Fund: Is a financial instrument that is listed on and trades through the JSE (Johannesburg Stock Exchange – if you're really battling with the Greek!) just like a share does, but instead of tracking the performance of a single share, it can track a whole range of things – anything from an index (a group of shares) to a commodity price, an exchange rate, and even instruments listed on other exchanges – like a bond index.

This makes the business of getting exposure to an industry or sector very easy, because instead of having to buy 15 different shares to get exposure to the Financial sector for instance, you now buy just one instrument - The Satrix Fini. And all the usual benefits that accrue to the owners of the underlying shares, also accrue to the owners of the ETF, namely dividends, interest etc .

Market Cap: short for market capitalization. This measures a company or instruments Total Value and is calculated by multiplying the no of shares in issue by the ruling price (or last traded price).

For example the market cap of the Satrix 40 is calculated as follows:

265,491,441 X R23.24 = R6,278,885,587 or R6.2bn for short. The Market Cap varies as soon as the price changes.

Tracking error: When using an indexing or any other benchmarking strategy like buying an ETF, the amount by which the performance of the portfolio differed from that of the benchmark expressed as a percentage is the tracking error.

Hedging: Protecting your portfolio by taking opposing bets, for want of a better word. If you hold a large portion of your wealth in Rands, and want to protect this value against any decline in the Rand/Dollar exchange rate, you would hedge yourself by buying US Dollars. That way what you lose on the swings you make up on the roundabouts! See also **uncorrelated returns**.

Uncorrelated returns: If one share/instrument performs well during a particular period and another one declines, we then refer to both of them as being uncorrelated. An excellent example is Gold, which typically does well by producing positive or flat returns while share prices collapse, usually in times of uncertainty.

Volatility: is the rate at which prices change or fluctuate. When prices or markets are volatile it usually indicates that there is a lot of uncertainty regarding economic developments. Consequently there exists a vacuum and no clear trends (be they upward or downward) exist. Analysts use volatility indexes to assess the willingness or unwillingness of investors to buy shares and other financial instruments.

Top 40 Index: The 40 largest companies listed on the JSE by value or market cap. The companies make up this index based on their proportional size or weighting,so in other words if you're Bakkies Botha or BHP Billiton you make up the biggest proportion of the team. The Top 40 Index then measures the collective performance of the share price of these companies.

Total expense ratio (TER): Is what you pay the issuer to administrate the ETF on your behalf (and you thought they were doing it for free, Ha!). This cost is expressed as a percentage of the value of your portfolio per annum. This is usually calculated daily and debited once a quarter. Much of the benefit of using ET's is that they are generally on a like-for-like basis much cheaper than using unit trusts.