Dry Associates Investment Newsletter

May 2016

Buffalo, Maasai Mara (Courtesy: J. Dry)

Dear Investor,

The global economy continues to grow but at a snail's pace. The World Bank says global growth was 2.4% in 2015 – less than the 2.6% recorded in 2014. The Bank projects a similarly uninspiring 2.9% expansion in 2016.

These figures, of course, mask a wide range of economic scenarios being played out regionally and nationally. The fall in global demand has disproportionately affected emerging market commodity producers, their currencies and near term economic prospects. China is being forced to rethink its export-lead economic model. Other BRICs have political problems impacting their economies. The developed economies are in their own quandary trying to stimulate consumer demand with interest rates already at zero. So it's going to be a while.

The US Market

So it's no wonder that the US stock market is cautious and volatile. In January 2016, the Dow Jones Industrial Average (DJIA) fell 14%. It has since risen to within 1.4% or 250 points of its all time high of 18,351 reached on May 19, 2015. It is now trading at 17,891 as we write this newsletter per the chart below:

Source: www.bigcharts.com

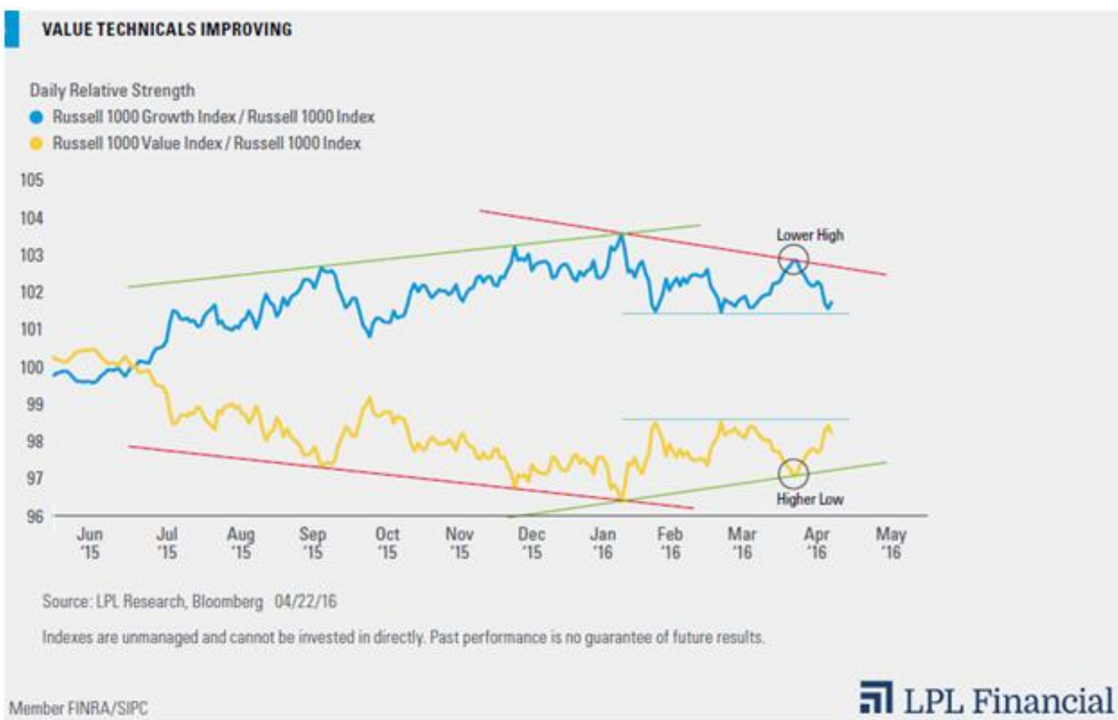
We still like the US market for a number of reasons. First, it's obviously denominated in US dollars which continue to appreciate against almost all other currencies. Second, the US economy is still in recovery mode. The US economy is expected to grow 2.6% in 2016 [versus 1.7% for the Euro area and 2.2% for the UK according to the IMF]. And third, the Federal Reserve continues to be accommodative putting off any interest rate hike until at least June 2016. Investors can get broad expose to the US market through the Franklin Templeton US Opportunities Fund.

Changing Trends in the US Market

There are many investment philosophies but two of the most enduring are value versus growth. The value philosophy was laid out by Benjamin Graham in 1934 in his book *Security Analysis*. Its leading proponent today is Warren Buffet. This investment philosophy seeks out undervalued equities whose share prices are temporarily trading below their historical valuation. These undervalued equities (often evaluated through their Price/Earnings ratios) are purchased and held until there is a reversion to their historical valuation.

The growth investment philosophy, on the other hand, espoused by investors like Peter Lynch who grew the Fidelity Magellan Fund from $20 million to $14 billion between 1977 and 1990, focuses on growth stocks. These are fast growing stocks like Facebook, Amazon and Netflix.

Value investing has not been particularly profitable over the past decade. Recently, however, it appears there may be a trend reversal. This would imply increased investment is low valued companies such as energy and financials versus the higher valued technology and consumer discretionary stocks, for instance. LPL Financial has captured this possible trend reversal by comparing the Russell 1000 Value Index (an index of 1000 low valued securities) to the Russell 1000 Growth index (an index of 1000 high growth securities). The Russell 1000 Value index has outperformed the growth index by 2.6% year to date (see Value Comeback? www.lplfinancial.lpl.com) per the following graph:



Exposure to this value investing philosophy can be done through Franklin Templeton's Mutual Beacon Fund.

The Case for Gold?

Much has been written about the vast amounts of public and private debt being accumulated the world over. Even before the subprime mortgage crash of 2008, central banks were taking on prodigious quantities of debt as domestic budget deficits soared. The US government, for example, now owes $18.8 trillion in public and intergovernmental debt. This is more than the US Gross Domestic Product in 2015 of $18.1trillion. And after the 2008 financial crisis, developed nation central banks have engaged in massive QE (quantitative easing) essentially printing money to try to stimulate domestic consumption.

In addition, many foreign countries like China and Japan are engaged in a deliberate attempt to devalue their own currency in order export more to improve their trade position. With so many countries trying to devalue, there is an evitable "race to the bottom".

So, we think there is a case to be made for gold as an asset class in an investor's portfolio - one as an insurance policy against a depreciated local currency and two as a potentially profitable investment.

Jim Rickard in his new book "*The New Case for Gold*" has some interesting thoughts on the subject. What, he suggests, would happen if the discipline of gold were introduced to stop this seemingly out of control world of increasing debt and depreciating currencies. To quantify the price of gold he suggests that if you take a mere 40% of the global money supply (that is, 40% X M1 (M1 is defined as coins, paper currency and checking accounts) and divide this by the 35,000 tons of official gold held by central banks, the price of gold would be $10,000 per ounce. Gold closed at $1,186 on Friday, April 30, 2016. And if you liquefied all world debt and derivatives in gold, price per ounce would be $50,000!

So, if you're convinced by this sort of thinking, Franklin Templeton offers a Gold and Precious Metals Fund. The fund is made up of stocks in 58 gold producing companies around the world. The fund price is pretty much on the floor although it has increased 43% (from a very low price) year to date.

Franklin Templeton Investment Funds

Franklin Gold and Precious Metals Fund

Sector Equity
LU0496367417
31 March 2016

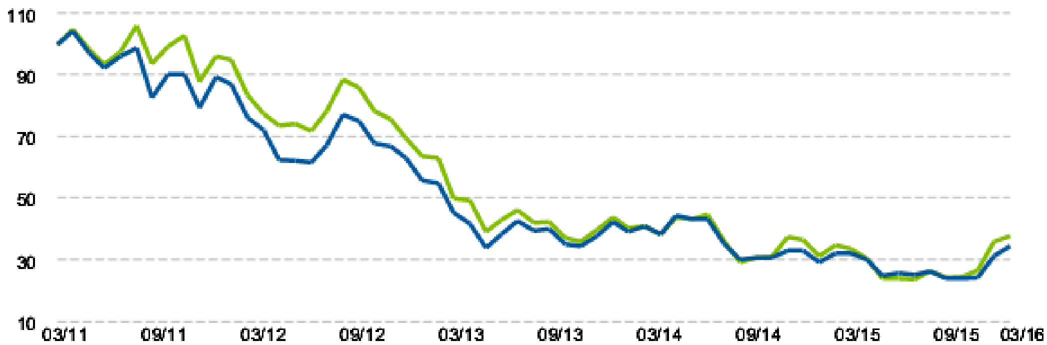
Fund Fact Sheet

estors.

Performance

Performance over 5 Years in Share Class Currency (%)

Franklin Gold and Precious Metals Fund A(acc) USD   FTSE Gold Mines Index



Performance in Share Class Currency (%)

	Cumulative								Annualised
	1 Mth	3 Mths	6 Mths	YTD	1 Yr	3 Yrs	5 Yrs	Since Incept	Since Incept
A(acc) USD	10.31	43.62	37.18	43.62	18.23	-37.06	-65.32	-57.20	-13.36
A(acc) EUR	5.26	36.61	34.41	36.61	11.61	-29.18	-56.90	-50.00	-11.05
I(acc) USD	10.27	43.63	37.50	43.63	19.31	-35.39	-63.78	-54.90	-12.59
Benchmark in USD	5.06	52.99	58.19	52.99	20.65	-40.35	-62.23	-56.43	-13.10

Source: www.franklintempleton.com

Elsa's Kopja Safari Lodge, Reading Room, Meru National Park (Courtesy: J. Dry)

Kenyan Fixed Income Market

Recent Troubles in the Kenyan Banking Sector

The big news, of course, was the closure of Chase Bank on 7th April 2016. Coming within nine months of the closure of Imperial Bank (13th October 2015) and Dubai Bank (14th August 2015), the Kenyan financial sector has been severely tested.

The re-opening of Chase Bank on 27th April, 2016 has come as a welcome relief to thousands of customers and investors. We sense that stability (and sensibility) are returning to the sector.

We don't know all the facts surrounding Chase Bank's closure so we won't speculate but we trust lessons have been learned and the financial sector is better for it. Now, our wish and our clients' fervent wishes are quite simple "please, no more surprises".

Yields on Fixed Income Securities

Kenya remains a high interest rate environment. While there's been a significant shift of funds to Tier I banks and government paper since the closure of Chase Bank, within this environment there continues to be strong competition for funds keeping lending rates high. The government and the private sector continue to compete for funds. Some prevailing interest rates as at 5 May 2016 are as follows:

Average Commercial Bank Deposit Rate	8.02%	Source: CBK (Dec 2015)
91 day Treasury Bill Rate	8.52%	Source: CBK
182 day Treasury Bill Rate	10.45%	Source: CBK
365 day Treasury Bill Rate	11.74%	Source: CBK
Average Commercial Paper Borrowing Rate	15.50%	Source: Dry Associates
Average Commercial Bank Lending Rate	18.30%	Source: CBK (Dec 2015)

Launch of Dry Associates Unit Trust Funds

In light of the recent problems in the banking sector, Dry Associates decided to delay the launch of its unit trust offerings. However, the situation is stabilizing and we shall be launching within the next several weeks. These funds, being offered in Kenya shillings and US dollars, are being structured to provide attractive returns and the safety investors expect from a diversified offering of quality assets.

Kenyan Stock Market

The Nairobi Securities Exchange has two major indices – the NSE 20 Share index and the NSE All Share index. The NSE 20 share index captures performance for 20 of the larger companies and the All Share index captures performance of all listed securities. Both are essentially flat year-to- date.

However, going back to 1st January 2015, the NSE 20 share index is down 22% and the All Share is down only 10%. The All Share index is shown below:

Source: www.mystocks.co.ke

It is evident that several of the bigger listed companies like Kenya Airways and Mumias Sugar which are prominent in the 20 Share index pulled down that index. Other firms in the broader All Share index have not done nearly as badly. But it is obvious that the Kenyan securities market has not been a money maker for the past couple years.

Nevertheless, many of these listed companies, for example, Safaricom, we believe are long term winners. We continue to purchase companies like Safaricom in our pension funds on a monthly basis using "dollar cost averaging" to build a position in this and other counters in the banking and insurance sectors in particular. Over time, these well managed companies will, we believe, add real value to patient portfolios.

Sincerely,

Dry Associates Ltd

10th May 2016

Mzima Springs, Tsavo West (Courtesy: J. Dry)

Dry Associates Ltd
Dry Associates is an Investment Group in Kenya and offers a wide range of products and services.

Private Wealth Management | Unit Trusts | Commercial Paper | Investment Advisory Services | Pension Fund Management | Offshore Funds | Consulting | Corporate Finance | Treasury Management | Portfolio Management

For more information visit our website: **www.dryassociates.com** or speak to us directly on **+254 (0) 705 799-971 / (0) 705 849-429 / (0)738 253-811 / (020) 445-0520/1**

We hope you enjoy this months Investment Newsletter

Our mailing address is:
Dry Associates Investment Group
Brookside Grove
P. O. Box 684 - 00606
Nairobi, Kenya