IBF

INSTITUTE OF BEHAVIORAL FINANCE

Monthly Investor Confidence Index

August 2011

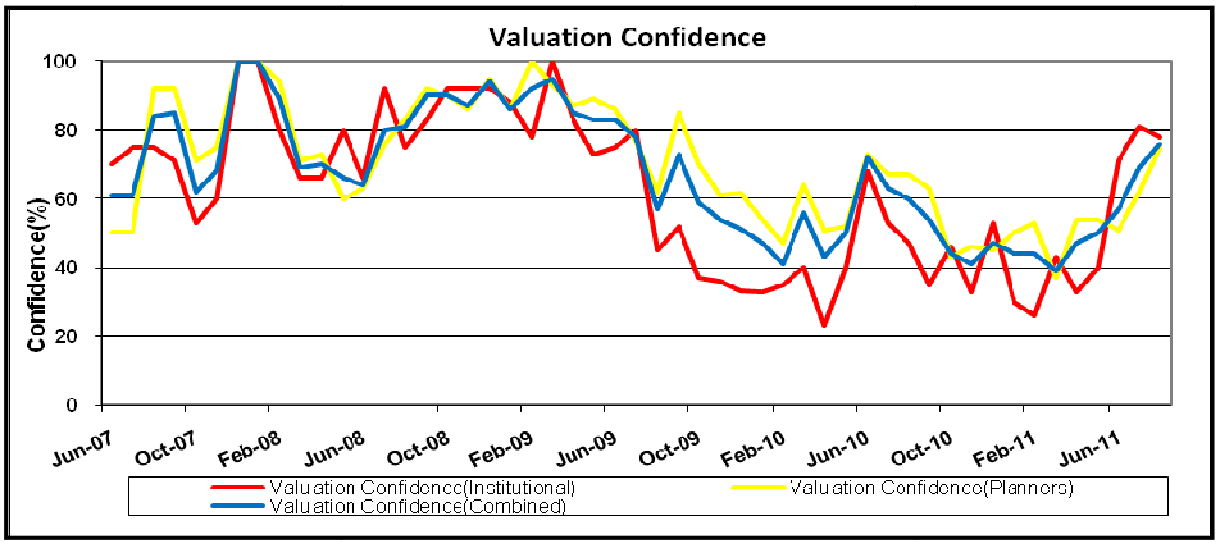
For further information please call Gerda van der Linde, Executive Director on 082 881 6159 or Cobus du Plessis on 083 303 5127.

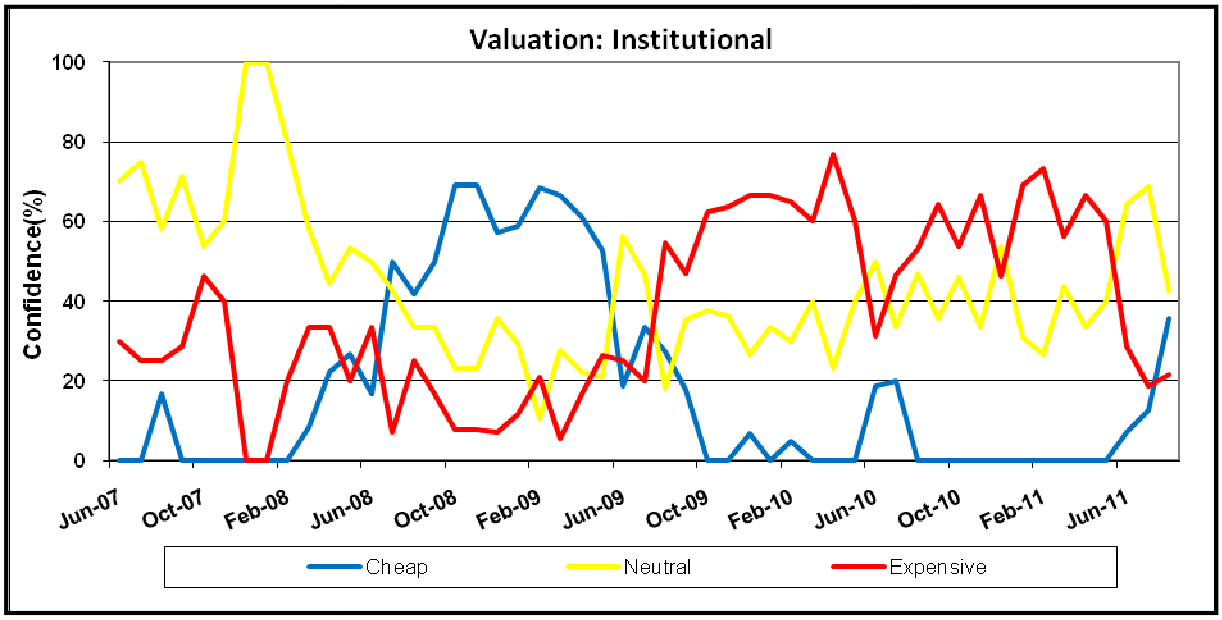
PROFESSIONAL INVESTORS HAVE A POSITIVE FUTURE VISION OF MARKETS

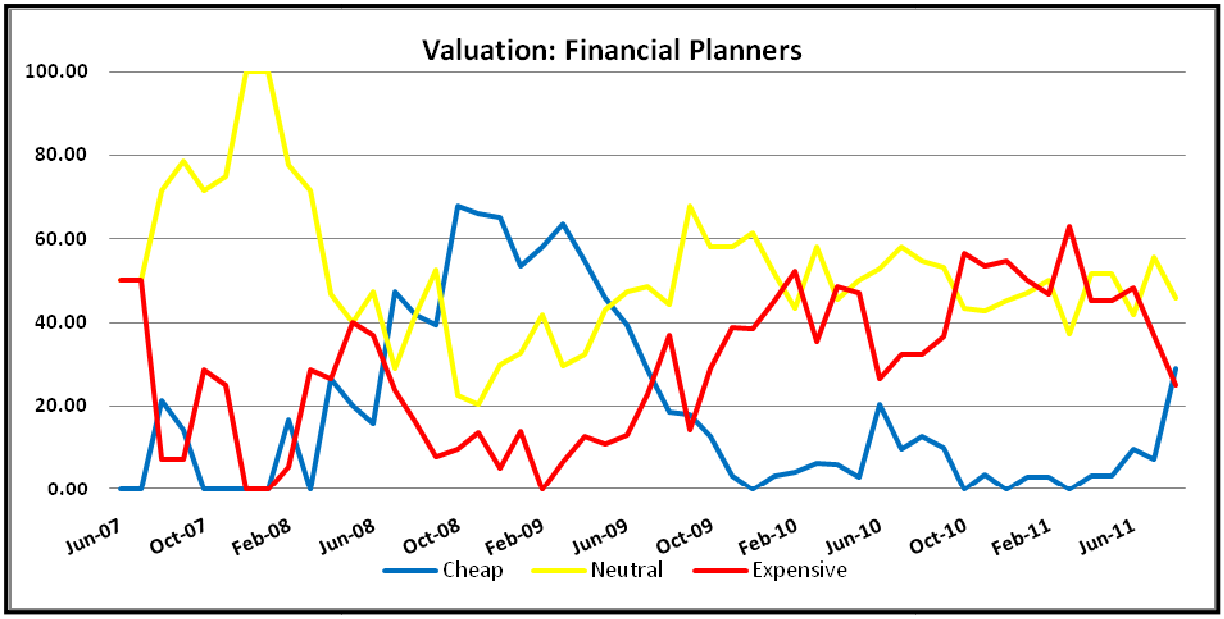
Press Release by Theo Vorster, chairman of the IBF and Gerda van der Linde, Executive Director

Executive Summary

- Despite the recent spate of volatility on the local and global stock markets, most institutional investors and financial advisors participating in the Investor Confidence Index (ICI) survey no longer believe the local stock market to be expensive. Only 21% of institutional investors still regard the local stock market to be expensive. This is in stark contrast to the 73% in February this year.

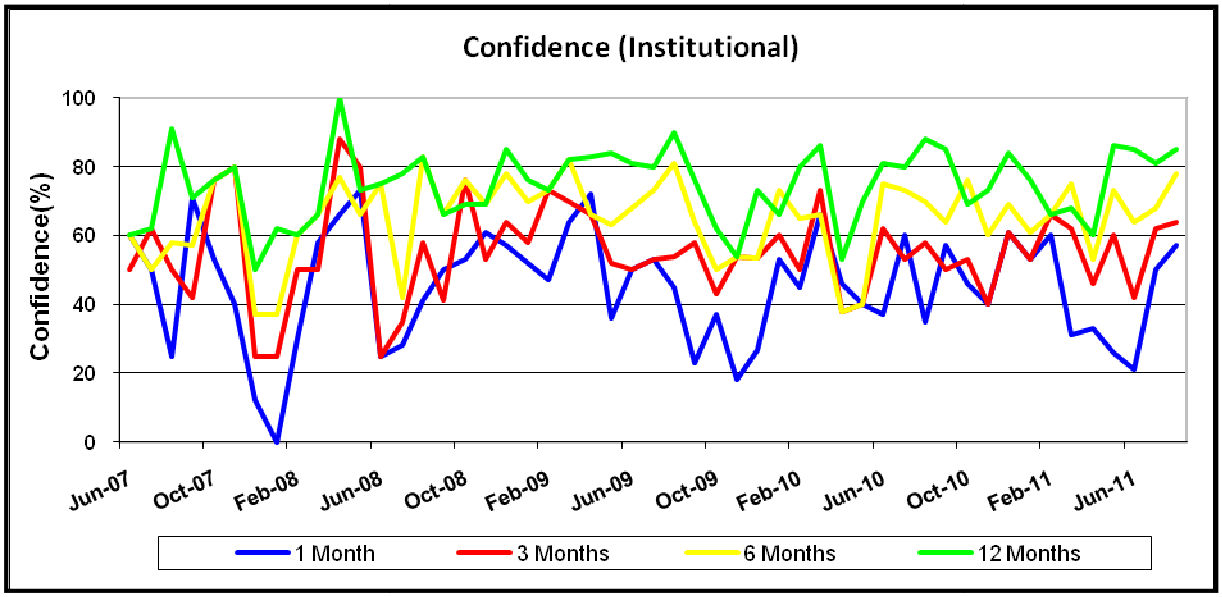


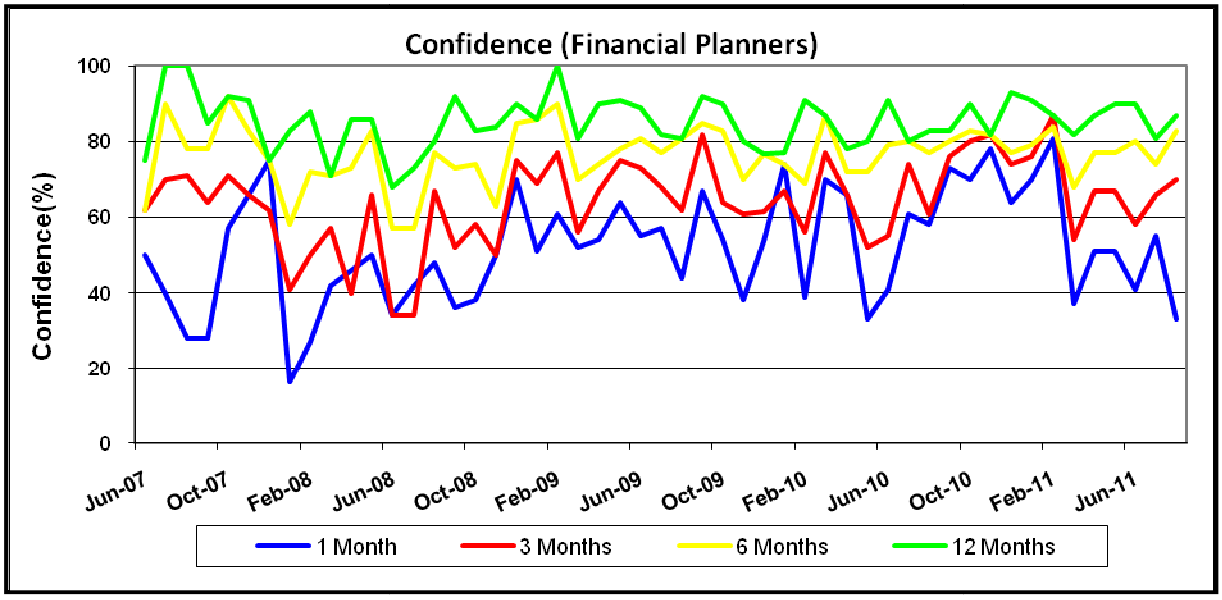


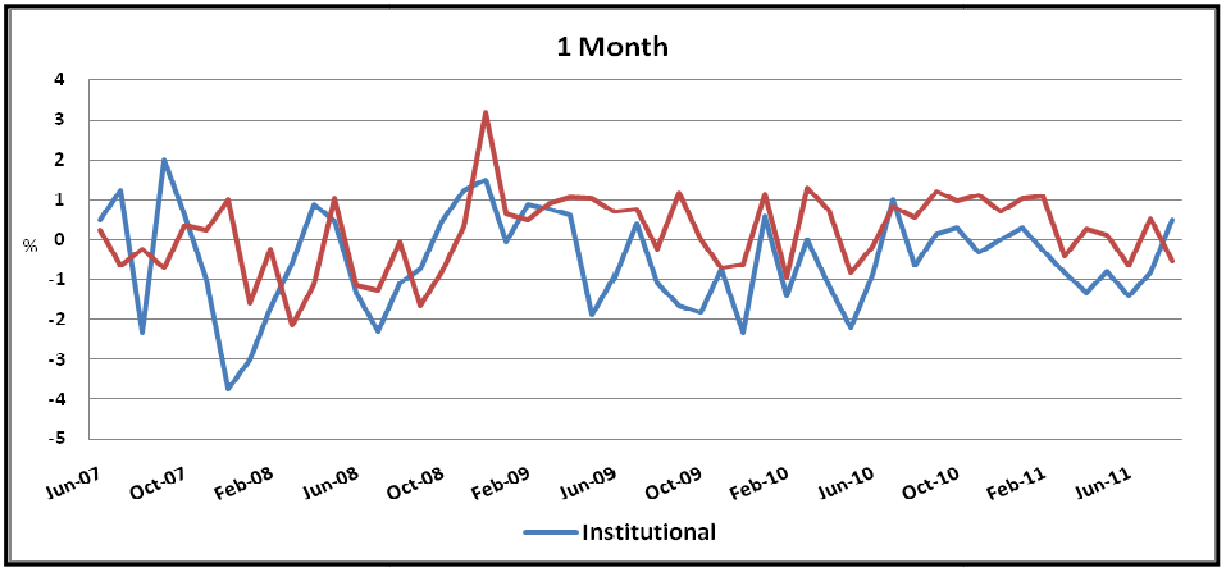


- The same trend is evident from the financial planners, with only 25% regarding the local stock market to be expensive, down from a high of 63% in March this year. The last time we experienced similar confidence levels, reflected by the Valuation Confidence Index by both groups of participants, was in August 2009. With 36% of institutional investors regarding the local stock market to be cheap, there must be several buying opportunities for the well-informed investor.

- For the first time since October 2008, institutional investors show higher confidence levels than the financial planners regarding the JSE All Share Index ending positive over the next one, three, six and 12 months.




Confidence (Financial Planners)
Confidence(%)
100
80
60
40
20
0
Jun-07
Oct-07
Feb-08
Jun-08
Oct-08
Feb-09
Jun-09
Oct-09
Feb-10
Jun-10
Oct-10
Feb-11
Jun-11
1 Month
3 Months
6 Months
12 Months


1 Month
%
4
3
2
1
0
-1
-2
-3
-4
-5
Jun-07
Oct-07
Feb-08
Jun-08
Oct-08
Feb-09
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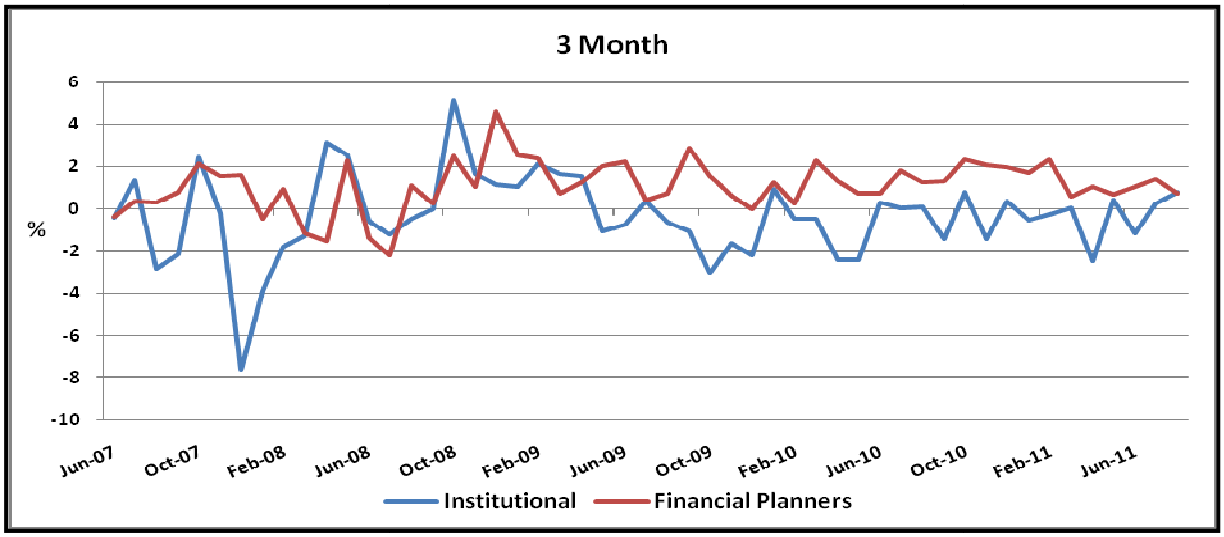
Jun-11
Institutional


3 Month
%
6
4
2
0
-2
-4
-6
-8
-10
Jun-07
Oct-07
Feb-08
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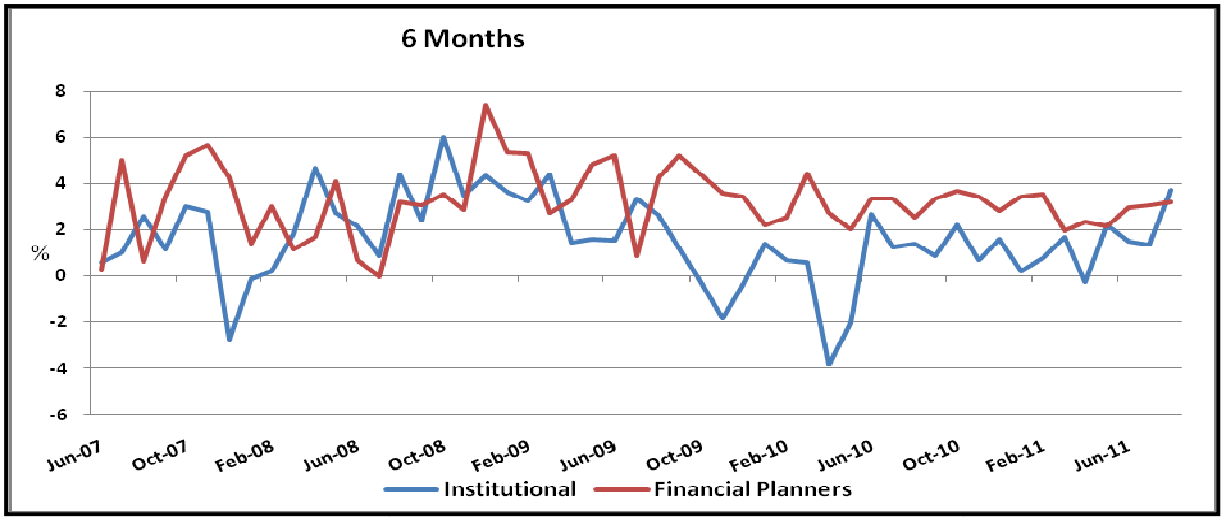
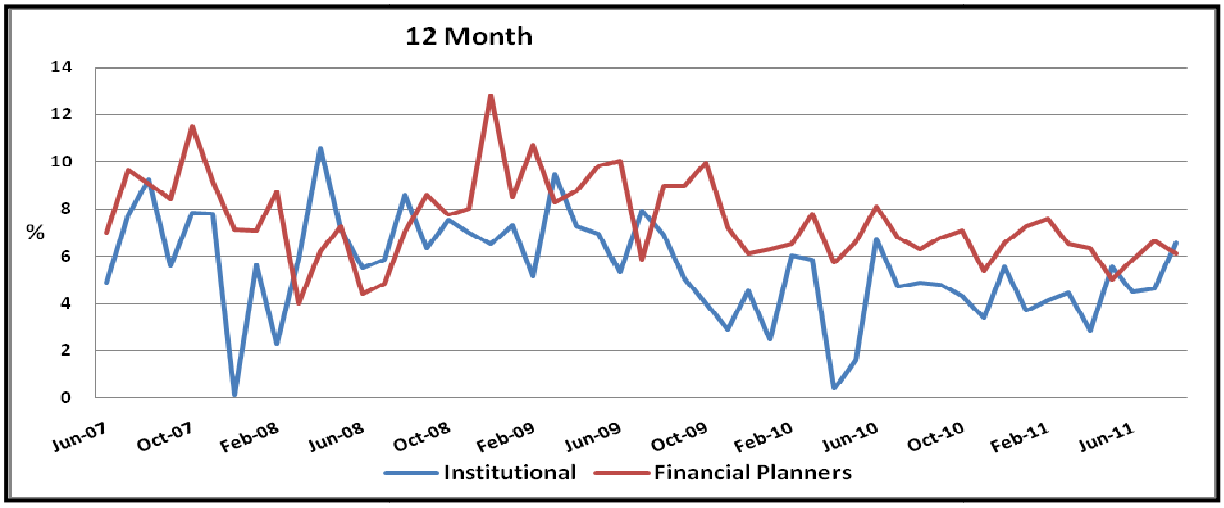
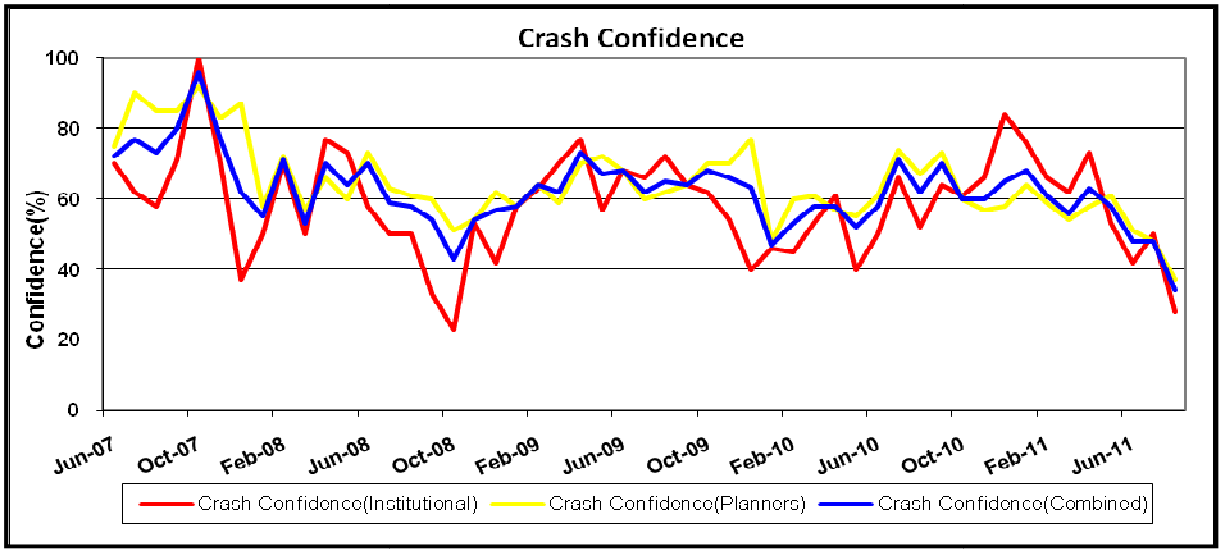
Institutional
Financial Planners



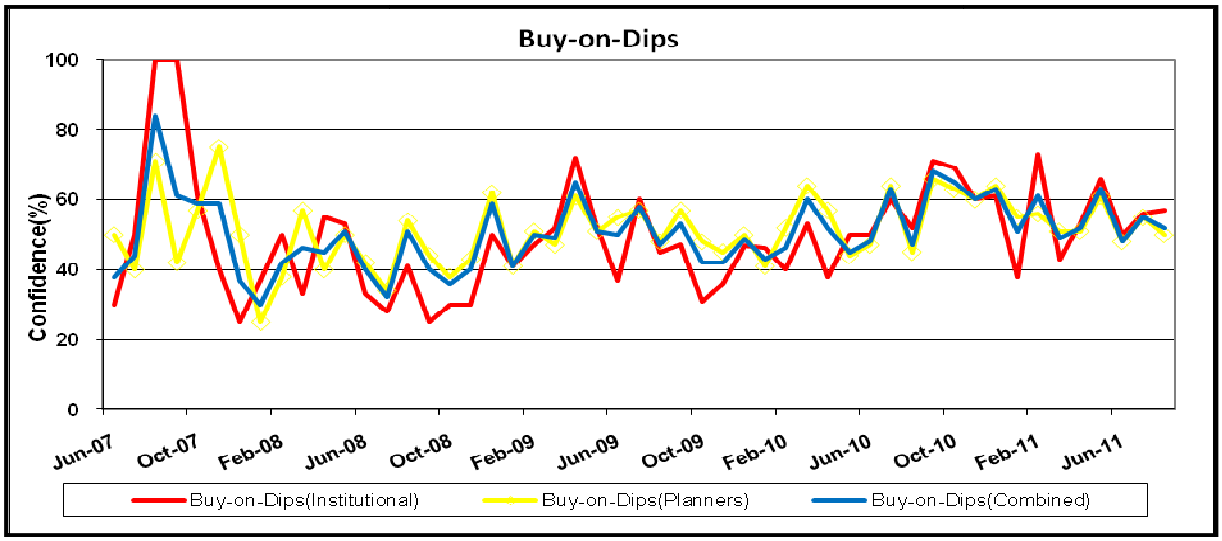


- In stark contrast with the optimism shown in the mentioned two indices, participants showed less confidence in the Crash Confidence Index. Only 28% of institutional participants and 37% of financial planners believe there is a less than 10% chance on a market crash occurring. Apart from October 2008, this is the worst level of confidence by institutional investors and the worst ever for the financial advisors.



That said, it is not all gloom and doom, as the predicted likelihood of a market crash occurring, as seen by all the participants, is only 21%. This sentiment may be due to the influence of the growing uncertainty in global markets and how it will influence the local market.

- Participants are divided on what will happen on the JSE All Share Index the day after a 3% drop in the ALSI. Only 52% of participants expect that a positive movement will occur the day after such an event.



Key Insights

The participants from the financial planner group are clearly more influenced by the volatility of the past month. Financial planners may be more prone to the recency bias, which contributes most to weak performance expectations. Recency is the tendency to rely too heavily on current information when making predictions about the future. For example, if prices are going down today investors believe the worst is yet to come. Right now, most commentators in the media are forecasting doom and gloom, influencing investors negatively.

Indications are that institutional investors and, to a lesser extent, financial advisors believe the market to be fairly valued, moving towards trading below fundamental value. It is therefore possible that those investors holding this opinion will start buying slowly into the JSE All Share looking for attractive opportunities.

We are well aware that investors need to trust institutions and financial advisors, and need to believe in equity markets and a strong economy in order to have the confidence to start investing money in the stock market again. We also know that not doing so will leave investors poorer in the long run due to the declining value of money over time. We can only hope that investors will get in the right spirit – finding trustworthy and well qualified financial advisors who can guide them in making wise investment decisions to suit their needs, goals and financial risk tolerance.

Survey Method

Confidence in the share market is much harder to pin down than consumer confidence, since the judgments people make about the share market are among the most involved of any that they must make. People interested in the stock market often tend to view themselves as playing a game against other share market investors, trying to guess when shares will do well before others do, so that they can profit from this knowledge. Many people who follow the share market watch the numbers every day, and many popular magazines, television, and radio shows follow the share market closely. Thus, there is likely to be more complexity to people's views about the share market than there is about their decisions whether to save more now or whether to buy a new sofa, which consumer confidence indexes emphasize.

It should also be recognized that investor confidence is only one of many forces on the market. Share prices are of course determined by supply and demand, and there are numerous factors that affect these, fundamental factors, legal, tax-related, demographic, technological, international, as well as other psychological factors related to attention, regret, anchoring, and availability. Indices of share market confidence can therefore only play a supportive role in trying to understand market events.

The indices of investor confidence that we have derived do not all move in the same direction through time, or even approximately so. Forming a simple average of the different indices to produce one overall share market confidence index would thus be arbitrary. Instead, we report here different investor confidence indices. Each is measured in percent, as a percent of respondents who report holding a certain view.

Data

A questionnaire is send the second Monday of every month to a sample of investment professionals. These include economists and portfolio managers form institutions as well as financial planners whose main focus is investments. Respondents need to answer 4 questions only by indicating in what direction and by what percentage they think the market will change. The questions are shown below as well as an indication of how the index is calculated.

1. **One-Year Confidence Index**

Question: How much of a change in percentage terms do you expect in the JSE All-share Index during the following periods: one month, the next three months, the next six months and the next year?

The index is calculated as the number of respondents giving a number **strictly greater than zero for the "In 1 Year"**. The index therefore reflects the percentage of the sample that expects the JSE All-Share Index to end positive over the next X months.

2. **Buy-on-Dips Confidence Index**

Question: If the All-Share were to drop by 3% tomorrow, what would you think the All-Share would do the day after tomorrow?

Three options are available namely Increase (%), Decrease (%) or stay the same. The Buy-on Dips Index is the number of respondents that **choose an Increase** as a percentage of the total number of respondents. The index therefore shows the percentage of the respondents expecting a rebound the next day should the market drop by 3% in one day.

3. Crash Confidence Index

Question: What do you think is the possibility of a catastrophic market crash (like 28 October 1928) occurring during the next six months?

An answer of between 0% and 100% may be given, with 0% meaning it will not happen and 100% it is sure to happen. The index is the percentage of respondents who think that the **probability is less than 10%.** Therefore shows the percentage of respondents who attach little probability to a stock market crash in the next 6 months

4. Valuation Confidence Index

Question: Stock prices in South Africa, when compared with measures of true fundamental value, are too low, too high, or just right?

The valuation index is the number of respondents who **choose too low or just right** as a percentage of the total number of respondents. It therefore reflects the number of respondents who think that the market is not too high.