

“The cost of reacting to weak markets”

Investors were mostly disappointed with returns in 2016 as a combination of weak local equity markets and a recovery in the rand led to low single digit returns across a wide range of funds. By way of comparison, the main industry sectors are shown below, highlighting the fact that all of the main fund categories delivered negative returns relative to inflation for the year.

Sector	Return for 2016 (ZAR)
Conservative Balanced Funds	3.7%
Moderate risk Balanced Funds	1.2%
Local Equity Funds	3.2%
Offshore Balanced Funds	-8.4%
Offshore Equity Funds	-7.8%
SA Inflation	7.0%

Table 1: Net returns after fees. Source: Fundhouse; FE Analytics

A common reaction we see from investors is to question the investment strategy in place with their financial planner, and to naturally seek corrective action. This approach and reaction is the single largest way in which to erode long term investment returns. Let us explain by means of three illustrations.

Chart 1 below highlights the consequences of reacting to weak markets by withdrawing from long term savings portfolios and investing in safer alternatives such as cash or bank deposits. Investment returns are unfortunately not earned in a straight line, they are lumpy and as such investors need to be present in the market to experience these lumpy returns.

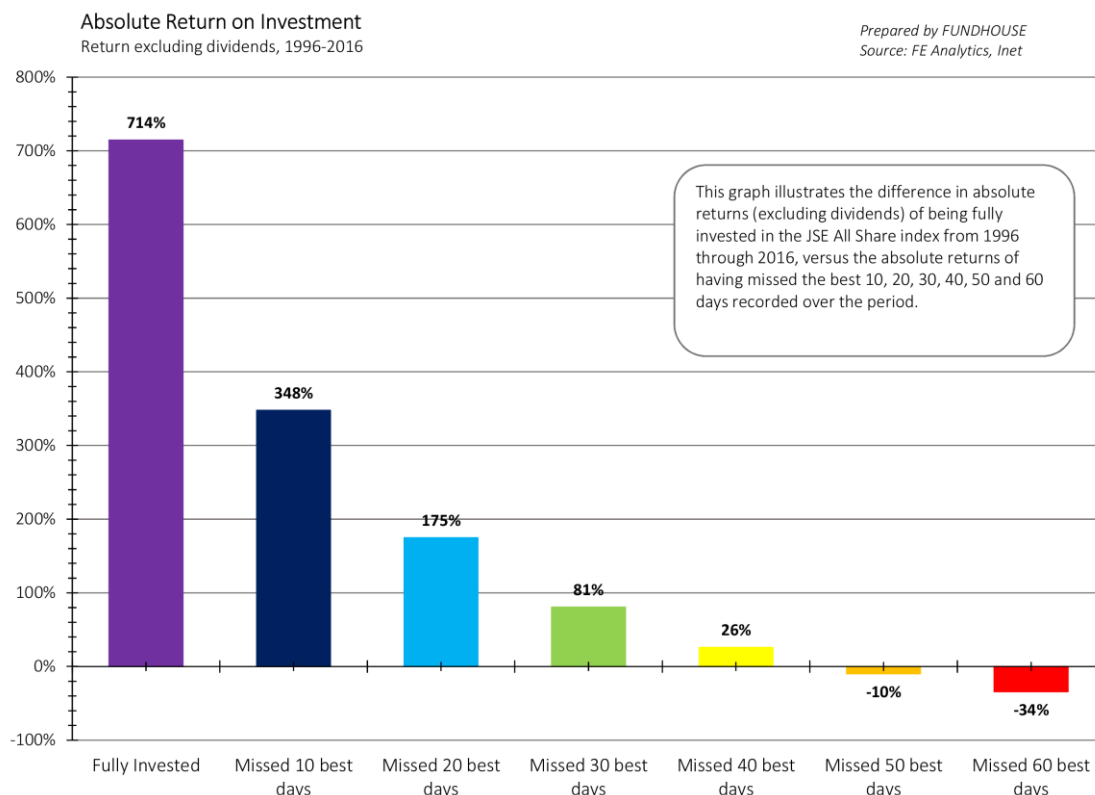


Chart 1: Consequences of missing the best days on the JSE 1996 – 2016. Source: Fundhouse

If you had missed (eg. not been invested in shares because you moved your investments to cash) just the 10 best days in the local share market over the past 20 years, you would have halved your total investment return! This escalates to total return losses (ie your ending capital would have been less than your starting capital) if you missed the 50 best days on the market.

The second example is to demonstrate the range of returns you may expect as an investor over any given year, relative to the longer term savings objective of your portfolio. In Chart 2 below we show that over the past 25 years, an investor could have experienced a return net of inflation of between plus 44% and minus 30% over a 12 month horizon for a balanced retirement fund. This compares with the minus 5.8% real return similar investors experienced in 2016 – clearly things can get a lot worse! Also to note that if you roll the poor experience of 2016 just one month forward, investors received inflation-matching and in some cases, inflation-beating returns over 12 months.

However, by remaining invested, this range of returns narrows to between positive 4.3% and 12.9% after inflation, when held over a 10 year horizon. It pays to stay the course.

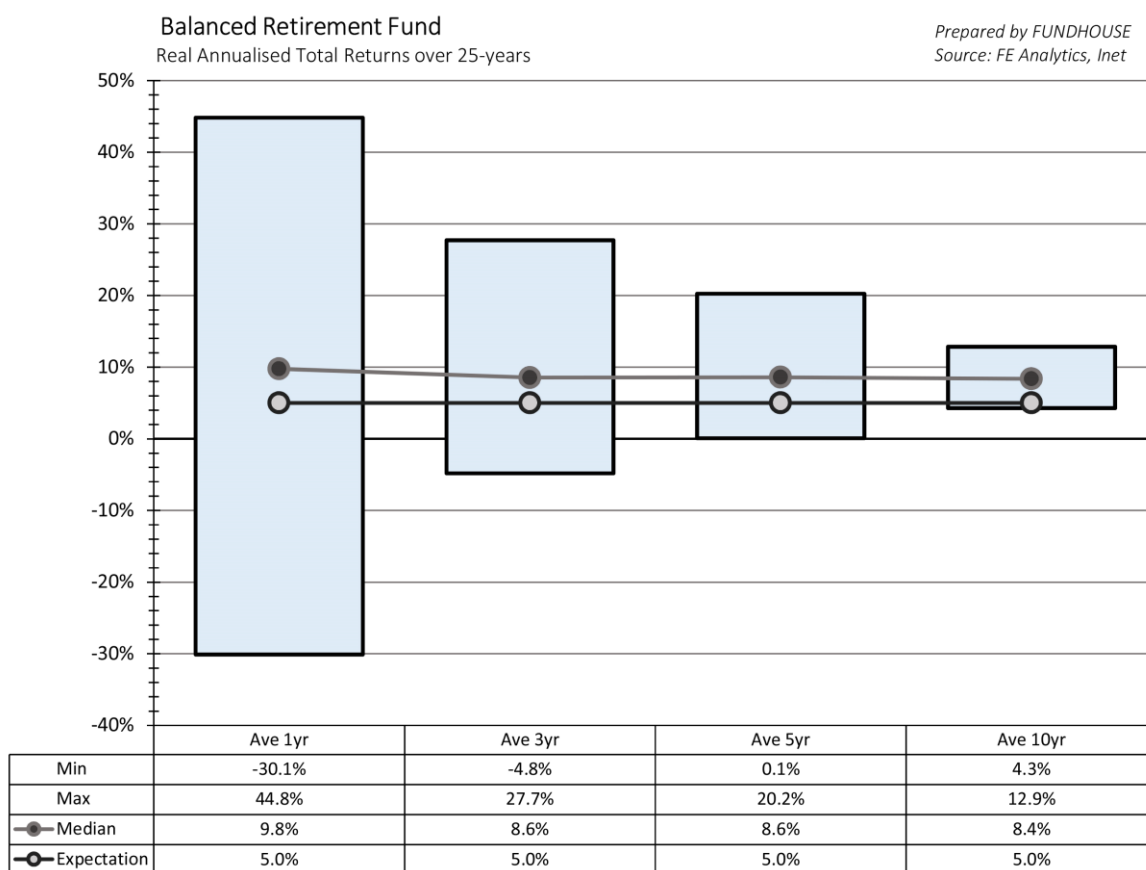


Chart 2: range of expected returns net of inflation: Source: Fundhouse

The last illustration is to highlight exactly how difficult it is to try and time the market. If you consider how an asset class which is this year's best performer, was often last year's worst performer (and potentially next year's worst too), it hopefully makes sense that responding to markets without a strong fundamental investment case is also, mostly, a sure way to erode wealth. Chart 3 below shows the winners and losers each year for the past 10 years:

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	YTD	January
Emerging Markets 35.1%	Global Bonds 41.7%	Emerging Markets 42.2%	SA Listed Property 29.6%	Global Bonds 28.9%	SA Listed Property 35.9%	Global Equities 56.4%	SA Listed Property 26.6%	Global Cash 34.4%	SA Bonds 15.4%	SA Equities 4.3%	SA Equities 4.3%
SA Listed Property 26.5%	Global Cash 39.2%	SA Equities 32.1%	SA Equities 19.0%	Global Cash 22.4%	SA Equities 26.7%	Global Cash 23.8%	Global Equities 15.9%	Global Equities 32.8%	SA Listed Property 10.2%	Emerging Markets 4.0%	Emerging Markets 4.0%
SA Equities 19.2%	SA Bonds 17.0%	SA Listed Property 14.1%	SA Bonds 15.2%	Global Equities 15.3%	Emerging Markets 24.2%	SA Equities 21.4%	Global Bonds 11.1%	Global Bonds 29.7%	SA Cash 7.4%	SA Listed Property 1.6%	SA Listed Property 1.6%
SA Cash 9.4%	SA Cash 11.7%	SA Cash 9.1%	SA Cash 6.9%	SA Listed Property 8.9%	Global Equities 21.7%	Global Bonds 20.2%	SA Equities 10.9%	Emerging Markets 14.0%	SA Equities 2.6%	SA Bonds 1.4%	SA Bonds 1.4%
Global Bonds 6.1%	SA Listed Property -4.5%	Global Equities 3.5%	Emerging Markets 6.8%	SA Bonds 8.8%	SA Bonds 16.0%	Emerging Markets 20.2%	Global Cash 10.7%	SA Listed Property 8.0%	Emerging Markets -1.9%	Global Equities 1.0%	Global Equities 1.0%
Global Equities 5.7%	Global Equities -19.8%	SA Bonds -1.2%	Global Equities 0.4%	SA Cash 5.7%	Global Bonds 9.6%	SA Listed Property 8.4%	SA Bonds 10.1%	SA Cash 6.5%	Global Equities -5.1%	SA Cash 0.6%	SA Cash 0.6%
SA Bonds 4.3%	SA Equities -23.2%	Global Bonds -14.8%	Global Bonds -5.2%	SA Equities 2.6%	SA Cash 5.6%	SA Cash 5.2%	Emerging Markets 8.0%	SA Equities 5.1%	Global Bonds -9.9%	Global Bonds -0.3%	Global Bonds -0.3%
Global Cash 2.1%	Emerging Markets -36.9%	Global Cash -19.8%	Global Cash -9.8%	Emerging Markets -0.5%	Global Cash 5.5%	SA Bonds 0.6%	SA Cash 5.9%	SA Bonds -3.9%	Global Cash -11.1%	Global Cash -1.3%	Global Cash -1.3%

Key:

SA Cash - SteFI
SA Bonds - BEASSA All Bond index
SA Listed Property - SA Listed Property Index
SA Equities - All Share Index
Emerging Markets - MSCI Emerging Markets Index
Global Cash - 3m USD Libor
Global Bonds - Barclays Global Bond Index
Global Equities - MSCI World Index

Chart 3: asset class winners and losers. Source: Fundhouse

Over shorter horizons the investment markets can be frustrating, so it is worth paying attention to what we can control: ensuring we have a suitable financial plan in place; that our chosen fund managers are well equipped to deliver for us over time, and last but not least, that we are conscious of our own behavioural biases which can cause real damage to an investment portfolio.

31 January 2017

Sector		3m	YTD	1yr	3yr pa	5yr pa	10yr pa	5yr Vol ¹	10yr Vol ¹
LOCAL MARKET INDICES (In Rands)									
FTSE/JSE All Share Index (ALSI)	ZAR	4.7%	4.3%	10.3%	8.5%	12.7%	10.7%	10.3%	15.1%
FTSE/JSE SA Listed Property	ZAR	2.4%	1.6%	15.4%	18.1%	16.6%	15.0%	14.3%	15.5%
SA All Bond Index (ALBI)	ZAR	1.0%	1.4%	11.9%	8.6%	7.2%	8.0%	7.9%	7.5%
SA Cash Index (SteFI)	ZAR	1.9%	0.6%	7.5%	6.7%	6.1%	7.3%	0.2%	0.6%
Balanced Benchmark ²	ZAR	3.4%	2.7%	7.5%	9.5%	13.0%	10.9%	6.2%	6.2%
SA Inflation (1 month lag)	ZAR	1.2%	0.4%	6.8%	5.8%	5.7%	6.1%	1.4%	1.4%
GLOBAL MARKET INDICES									
Global Equity (MSCI World)	USD	6.4%	2.4%	17.1%	6.0%	9.9%	4.0%	11.1%	16.5%
Emerging Markets Equity (MSCI EM)	USD	0.8%	5.5%	25.4%	1.4%	0.2%	2.5%	15.5%	23.5%
Global Bonds (Barclays Global Bond Index)	USD	-3.3%	1.1%	2.3%	-0.2%	0.1%	3.5%	4.6%	5.9%
Global Cash	USD	0.2%	0.1%	0.6%	0.3%	0.3%	1.1%	0.1%	0.5%
MAJOR INDICES BASED TO RANDS									
FTSE/JSE All Share Index (ALSI)	ZAR	4.7%	4.3%	10.3%	8.5%	12.7%	10.7%	10.3%	15.1%
Global Equity (MSCI World)	ZAR	6.4%	1.0%	-0.7%	12.8%	22.6%	10.6%	13.3%	13.8%
Emerging Markets Equity (MSCI EM)	ZAR	0.8%	4.0%	6.3%	8.0%	11.8%	9.0%	12.0%	15.7%
SA All Bond Index (ALBI)	ZAR	1.0%	1.4%	11.9%	8.6%	7.2%	8.0%	7.9%	7.5%
Global Bonds (Barclays Global Bond Index)	ZAR	-3.4%	-0.3%	-13.2%	6.3%	11.7%	10.1%	12.7%	14.6%
COMMODITIES									
Gold (US Dollars)	USD	-5.0%	4.2%	10.2%	-0.8%	-6.9%	6.5%	17.2%	19.4%
Gold (Rands)	ZAR	-5.0%	2.7%	-6.6%	5.6%	3.8%	13.3%	18.7%	21.8%
Currencies (positive return = Rand weakening)									
Rand / Dollar	ZAR	-0.4%	-1.6%	-15.6%	6.4%	11.6%	6.4%	14.2%	16.5%
Rand / GBP Pound	ZAR	2.4%	0.2%	-25.3%	-2.7%	6.7%	1.8%	14.1%	15.2%
Rand / Euro	ZAR	-2.1%	0.6%	-15.9%	-1.2%	7.4%	4.5%	12.7%	13.7%

Spot Rates

31-Jan-17		6-Feb-17	Latest Quarter	1 Year Ago	5 Years Ago	10 Years Ago	20 Years Ago
Rand/US\$	Rand	13.28	13.69	15.46	8.07	6.97	4.68
Rand/GBP	Rand	16.55	16.70	22.55	12.53	13.66	8.02
Rand/EUR	Rand	14.27	14.44	16.80	10.46	9.25	5.56
Rand/Aus \$	Rand	10.15	9.89	11.25	8.24	5.52	3.72
Libor 6m \$	US\$	1.34	1.32	0.85	0.81	5.37	N/a
Prime	Rand	10.50	10.50	9.75	9.00	12.50	20.25
Repo Rate	Rand	7.00	7.00	6.25	5.50	9.00	N/a
All Bond Index Yield	Rand	8.93	8.98	9.38	8.49	9.71	14.62
Gold (\$/oz)	US\$	1,235.30	1,150.60	1,060.82	1,564.35	636.75	367.65
Palladium	US\$	768.00	676.00	547.00	630.00	324.00	116.50
Platinum	US\$	1,014.00	903.00	891.00	1,394.00	1,135.00	370.50
Oil (Brent Crude) \$	US\$	55.95	56.82	37.28	107.22	59.61	22.74
SA Inflation	Rand	N/a	6.80	5.20	6.10	5.80	9.40

data provided by Profile Data Analytics and INET BFA