REICHTEC PRIVATE WEALTH

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Loss Aversion

Loss Aversion refers to the tendency which people have to avoid making a loss. Studies have shown that Psychologically losses are more than twice as powerful as gains.

This is actually a major stumbling block with Investors – even a well-diversified portfolio will drop in value from time to time, and this creates the urge to reduce "risk" or the allocation towards the assets which have dropped in value.

This is not just "theory" but happens in practice. Several fund managers have shown data which illustrates that when their funds have underperformed for a period there has been a net "outflow" and that this reverses only AFTER a period in which there is outperformance.

The problem is that the investors who exit have already experienced the reduced return and only return after the fund has outperformed – and hence miss the period of good performance.

Industry figures also suggest that over the past year or so many people have moved to more conservative funds as the returns here have been better than more aggressive funds and without the associated volatility. The real risk is that they will only return too late after the more aggressive funds have already significantly outperformed the conservative funds.

I don't know what the future holds, but I do know that the local equity market is certainly "cheaper" than it was three years ago – the market has essentially moved sideways over this period while earnings have increased. I don't advocate taking on additional risk, but avoid the trap of becoming too conservative.

Offshore Investing

South African investors are only too aware of how volatile (and at times "fragile") the Rand can be. Offshore exposure is a great "diversifier" but the question is how to include this given the Exchange Controls in place in South Africa.

The "easiest" way is to invest in a "Rand-Denominated" fund where the underlying investments are in offshore assets. Here there is no need to go through the exchange control process of converting Rands into $, GBP or Euros. The asset management fees on these funds do tend to be a little bit higher and the funds can only be paid out into a South African bank account.

It is also possible to invest in foreign currency denominated Unit Trust funds. Here it is necessary to go through the exchange control process to convert to the foreign currency (or use existing offshore money). There are some small tax advantages to direct offshore funds and the asset management fees do tend to be a bit lower, but there is a cost to the exchange control process.

A final consideration with the direct offshore funds is ease of transactions and how they are treated in your Estate. Many of the direct offshore funds are domiciled in one of the Channel Islands. It can be very difficult to transact and in the event of your death your local executor may not be able to distribute these assets. There are solutions to these challenges but ensure you are well informed about the consequences.

Market Outlook

Locally the biggest event looming is the ANC Elective conference in December. I am certainly not going to try to predict the outcome but it is certainly currently being portrayed in the media as a battle between good and evil.

I have my own view about politics and politicians so I would rather say that it is a contest between "really rotten" and "slightly less rotten". The market will almost certainly "celebrate" any victory by someone whose surname does not contain "Zuma".

Whoever wins is going to have to deal with the crisis facing virtually all SOE's (State Owned Enterprises) which have become the feeding trough of the politically connected elite. These entities are making huge losses are they are run incredibly inefficiently.

At the same time SARS seems to be in "crisis" with revenue collections well below target. Just like your own budget, if you earn less you either must spend less or else you must borrow more.

Spending less is a problem for politicians as giving below-inflation increases to civil servants and social grant beneficiaries makes you very unpopular with people who vote. Considering that many politicians are probably unemployable outside of politics it is hardly surprising that politicians make "popular" decisions to stay in power rather than the hard decisions which are in the best long-term interests of the country.

Increasing borrowing is much less of a problem when an economy is growing, but when there is a recession or stagnation then this can become uncontrollable in a very short time.

Internationally the biggest threat currently is the tension between North Korea and America. Neither country seems to have a calm level-headed leader and both are armed with Nuclear weapons.

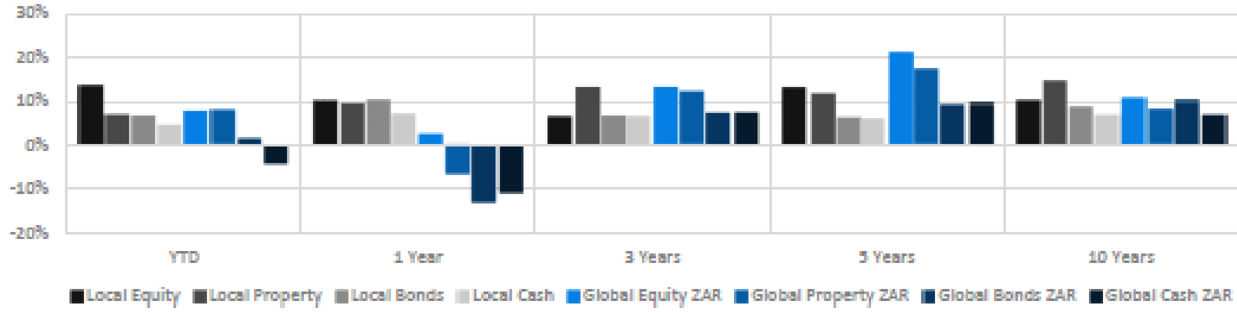
Economically however the World as a whole seems to finally be getting a bit better. There has been moderate growth in virtually all major economies for the first time since 2008.

As always, the advice is simple. Make sure you have a diversified portfolio, live within your means and don't panic. There will be volatility but the volatility creates opportunities for those who maintain cool heads and punishes those who don't.

Market Flash

31 August 2017

Asset Class Performance (ZAR)



Asset Class	Index	YTD	1 Year	3 Years	5 Years	10 Years
Local Equity	FTSE/JSE All Share	13.6%	10.2%	6.6%	13.1%	10.2%
Local Property	FTSE/JSE SA Listed Property	6.9%	9.4%	13.0%	11.7%	14.6%
Local Bonds	Beassa ALBI	6.7%	10.2%	6.7%	6.3%	8.6%
Local Cash	STeFI Call Deposit	4.6%	7.0%	6.4%	5.8%	6.7%
Global Equity	MSCI All Country World	7.8%	2.6%	13.2%	21.2%	10.9%
Global Property	MSCI ACWI/Real Estate	7.9%	-6.6%	12.0%	17.1%	8.1%
Global Bonds	JPM GBI Global Traded	1.7%	-12.9%	7.5%	9.3%	10.0%
Global Cash	ICE LIBOR 1 Month	-4.3%	-10.9%	7.4%	9.4%	6.9%

SA Inflation Outlook

Core inflation (headline inflation excluding food, beverages and energy) declined from 4.8% y/y in June to 4.7% in July, while headline inflation (excluding the food category), dropped around 4% y/y in July 2017.

Should inflation numbers continue to track lower and remain well within the SARB's targeted range of 3% to 6%, we could see additional rate cuts towards the latter end of the year.

ZAR vs USD

In comparison to a basket of EM peers, the rand is still one of the best performers against the dollar on a twelve-month rolling basis, second only to the Czech Koruna. For the year to the end of August, the rand strengthened by close to 6% to the dollar – refer to Chart 1 (right).

Chart 1 : ZAR vs USD

SA Market Overview

The local market continued its upward trend after a strong July and the JSE/FTSE All Share Index closed 2.6% higher during the month. The main contributors during the month were resources and telecommunication stocks, while beverages and industrial engineering were the main detractors. The FTSE/JSE Resources Index rose 6.5% in the second half of the month, supported by higher metal prices, due to Chinese demand holding up well.

Two significant new highs were reached during August with the FTSE/JSE All Share Index breaking through the 56,000 level for the first time, and Naspers breaching R 3,000 a share.

Interestingly, less than four years ago Naspers raced to R 1,000 a share which, at the time, was perceived as being overvalued. Little did anyone know that it would continue its trot, not only delivering excellent returns to its loyal shareholders, but also dominate the local benchmarks. (Currently, Naspers makes up 17% of the All Share and 21% of the SWIX indices respectively).

Global Market Overview

- In the US, the S&P 500 edged up by 0.3% during the month, supported by positive macroeconomic data. US second quarter GDP growth was revised upwards to 3% (annualized)
- In Europe, the stronger euro caused some headwinds for the equity markets, resulting in the MSCI EMU dropping by 0.5% during the month. In the UK, however, it was altogether a different story and strong mining and defensive stocks contributed to the FTSE All Share Index advancing by 1.4% during August
- Asia ex Japan continued its bullish trend for the year and recorded another month of positive gains. During August, Thailand (healthcare) and China (consumer staples) took the lead within the Asian markets
- Emerging markets outperformed developed markets during August, mainly due to strengthening commodity prices