NFB FINANCIAL SERVICES GROUP

PROFICIO
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FROM THE CEO's DESK

I have commented historically on the extraordinary volatility somewhat uniquely typical of our South African capital markets. The last few months have certainly endorsed this view!

Our currency has moved in wild gyrations between an extraordinary R17/$ to less than R14/$ and most recently to above R15/$. The JSE All Share Index and some leading shares in our market are also displaying remarkable volatility.

I have recently commented on Anglo American. Notably, I've done this not as an equity specialist, but rather as an investor and advisor, reflecting on a stalwart of the JSE, almost predictably declaring reasonable dividends, displaying established and enshrined behavior at the helm in South Africa, weathering all that markets and politics could throw at them.

Reflecting on more recent gyrations makes interesting reading. Anglos peaked at R556.01 on 19/6/2008, dropped to a low of R53.30 on 20/1/2016 and has since recovered to R135.00. Had you sold at the top, bought at the bottom and sold again now, this would have given you a rather handsome return! But, just imagine the party who'd done the opposite!

Getting this right is near impossible, but displays the amazing range of a so called "Blue Chip".

What becomes obvious to me is that our investment landscape offers returns comparable to other global markets, but with a higher risk attached. We need to factor this risk into our investment thesis and make very sure that we consider the point I made recently about adding diversity to portfolio construction. Investments are not only about growth in value. They also need to provide income, as tax efficiently as possible and in some instances security or even guarantees.

Where portfolios are large enough, one has the luxury of investing in "riskier" assets like shares and property where the dividends and income provide more than enough income. This allows the owner the comfort that they can simply sit out any weak or bear markets as the likelihood of prices recovering, and indeed achieving real growth, is fairly certain.

Global investment is not for sissies! I often comment to clients who display a conservative orientation and profile, that whilst they see the sense of going offshore, once there they ask that we deploy funds quite conservatively, which I find rather strange! Noting the currency volatility above would have me believe that the mere decision to go offshore is "aggressive".

Further to this, I like to ask the question as to what the ultimate purpose of these funds is. Whilst being owned by the investor, they are often the "insurance policy" in case South Africa does a Zimbabwe, or eventually intended for future generations, perhaps to educate children or grandchildren, or to help family set up offshore if need be. This extended investment term allows me to suggest the use of portfolios, either through a fund, or direct to a stockbroker where a diversified, dividend earning equity portfolio is utilised. I also think that offshore property has become interesting. Not a 'buy to let' property, rather a fund consisting of a portfolio of commercial and industrial properties or a Real Estate Investment Trust (REIT as they are called globally). This has been attractive for a few years now, and is particularly interesting given low hard currency interest rates, allowing these funds to apply their expertise in finding good properties, use leverage (given low borrowing rates) and locking in good tenants with upwardly adjusting rentals. Overseas, one often finds leases being signed for much longer periods than we are used to in SA. Ten year, fifteen year and longer leases are commonplace. I guess this is a price we South Africans pay for the poor governance and consequent tentativeness witnessed in tenants resisting lease terms much longer than five years! The other point to remember is that if you opt for cash type investments you are currently likely to end up with nearly no return after the tax man has enjoyed his bite at the cherry.

Complementing this rather more "aggressive" strategy, and for those seeking less volatility, both overseas and locally, NFB offers a series of Multi-Asset Solutions. These very popular solutions offer an actively blended mix of shares, property, cash, bonds. The attraction of these is that we have acknowledged experts watching markets, funds and managers all the time. They are inclined to re-balance, remove and replace underperforming funds or specific assets and do so in an unemotional way, lessening the behavioral risks

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Mike Estment CFP® professional
BA / Chief Executive Officer
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COM(E)MOTION

A little while ago I converted, via my discretionary foreign allowance, some rands into US dollars to ultimately invest in global equity unit trusts. Doing this regularly for my clients, I knew (without having to think too much) which funds I would use, and anticipated converting the currency at whatever the prevailing exchange rate was at the time - all my paperwork was ready. I always tell my clients that they should not get caught up in the exchange rate guessing-game and only in ten years' time would it be appropriate to assess if the decision was reasonable.

Foreign investing should typically have a long-term horizon especially when considering the long duration of currency cycles. What actually happened was that I looked at the exchange rate every five minutes for about three days trying to time the conversion whilst considering Mr Zuma and Co, the EFF, US elections, Russian unrest, Turkish turmoil, growth in China, and where my children would be educated....to name but a few. I spoke to my wife about the aforementioned and she proceeded to ask me how I approach this with my clients. The very next morning I took my own, long–standing advice and converted the currency. In case you are wondering (I know I would be), I exchanged my funds at R15.31/USD and invested in the Investec Global Franchise Fund and the Nedgroup Global Equity Fund. Please do not take my investment choices as advice as they are particular to my needs, objectives and circumstances.

My personal investment story leads me into two themes I would like to cover in this editorial:

1. Tactical versus strategic allocations… and emotional investing
2. Long-term investment environments… and emotional investing

Tactical versus strategic allocations

A strategic allocation is the long-term core allocation of a portfolio. This encompasses your split between rand and non-rand assets (local versus offshore) as well as your asset allocation: the allocation between cash, bonds, property, shares and alternative assets. These allocations will only vary slightly over time. In getting closer to retirement it may be that your portfolio requires you to start identifying between income and growth assets.

The externalisation of my personal funds was a strategic decision; I needed to increase my non-rand exposure to get to my target rand versus non-rand exposure. When making strategic decisions you need to take emotion out of play and deploy your assets in accordance with your target allocations. Your investment portfolio is a long-term (hopefully 15, 25 or even 50 years) relationship and over that amount of time your entry point should not make much difference. This does not mean you should invest blindly, ignorant of the current economic and political climate. It does mean though that you need to be committed. For example, if you feel that currencies are out of kilter then you could convert in two or three tranches, but you must give yourself a time line to do this in and stick to it. Trying to time markets often just leads to never doing anything and then going backwards in terms of the real value of your funds.

A tactical allocation differs as here you could try and time markets when you believe an asset class is incorrectly priced. A tactical deployment in most instances would not account for much more than a 4-5% shift. An example here, again using currency as it remains topical, would be to have converted US dollars back to rand when the exchange rate was over R16 to a dollar and then back to dollars again at R14.50. If you do ever make changes like this, you may want to reverse the trade later on to bring your portfolio allocations back in line. As an aside you should also consider the tax consequences of these types of changes as they may outweigh any gains.

Getting proper and well thought out advice when formulating your strategic allocations is critical. Current market conditions could quite easily lead even seasoned investors to have a sense of unease and steering towards a portfolio that is inappropriately biased (too cautious? too much offshore?). Rather than doing this you could phase your funds in, to rand-cost-average of a period over time, to get to your target allocations. Importantly, do not make any major changes to your portfolio due to sentiment; you are likely to get the timing wrong. Rather make changes when there is a fundamental shift in personal or investment circumstances.

A last point is that markets are, as are a lot of things in life, cyclical. The longer you invest for, the smoother these cycles are.

Long-term investment environments

Whilst I have spoken a lot around sticking to your guns there are drivers of change. There could be, at times, a number of these drivers and I will touch on but a few.

Oil

Oil was around $100 dollars a barrel in late 2014 and since then we have seen prices drop to between $20 and $50. The current environment is one where we could see prices at or below current levels in the not too distant future (what will the impact of Tesla be?). There would be winners and losers if this happens and this could guide where and how we invest i.e. what was appropriate historically may not be in the future. One of the losers is Russia who lose around $2bn for every $1 fall in the oil price; oil and gas account for 70% of its exports. A winner here could be Europe where their struggling economy could use any help it can get; there are some studies that say for every 10% drop in the oil price there is a 0.1% increase in economic output. A long-term structural change in the price of oil could change the profitability of certain companies, countries and currencies; this could necessitate a look at the inclusion or lack thereof of such counters in your portfolio.

Brexit

Until an event occurs almost all discussion around it is speculation. One of the much spoken about impacts of a Brexit is the potential negative impact on London property prices due to the influence of the financial sector which would shrink if it happens. Current or future investment in this sector may need to be addressed and adjusted. The market has already, to a degree, reacted, and whilst some may see this as an exit sign, others may see the 'sale' sign and climb in.

At the moment, there is a lot going on, both locally and internationally, in the political and investment market environments. It is easy, as I did, to get caught up in the hype. The old adage of 'sleep on it' is a good idea; take the time to mull over the persistency of the situation. If there is a shift that will be enduring or at least long-term, then your portfolio may need to be adjusted accordingly. Most of you will invest in some type or types of managed solutions; thankfully in these instances most of the decision making around market shifts is left to the fund managers and their teams, and we in turn, oversee them.

To coincide with my personal long-term strategic rand and non-rand allocation I chose to expose myself to funds that allocate largely to global blue-chip equity, with a conservative bias, as I feel the long-term investment environment for this broad sector is conducive to above inflation growth.

Be patient and try not rush in to any major portfolio adjustments when emotions are running high. Good luck.
Should you require assistance or advice with regards your investment allocations, please contact a Private Wealth Manager at one of our NFB offices in Johannesburg, East London, Port Elizabeth, Stellenbosch or Cape Town. ■

"Recent developments on the economic and political fronts have combined to allow us to provide a very interesting guaranteed and tax free income to appropriate portfolios."

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FROM THE CEO's DESK

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typically displayed by us as individual investors (we like to sell when everyone sells, and buy when everybody is buying - quite the opposite to portfolio managers who prey on weakness and sell into strength).

On a slightly different, but no less relevant tangent, we recently had Herman Mashaba, DA candidate for Mayor of Johannesburg, participate in a seminar. He and other South Africans like our very special Thuli Madonsela, and Chief Justice Mogoeng Mogoeng deserve special mention. They are proud, steadfast South Africans. They are also trailblazing folk, intent on rescuing our country back from the incredible injustices and practices of a morally, if not monetarily, bankrupt leadership. If our children and their children are to live here in a safe, democratic country taking care of all of its people we need to support their efforts and each do our own bit in supporting these modern day gladiators. Recent behavior by banks, leading accounting firms and other service providers, in denying their services to companies associated to the Guptas is also commendable.

The economic impact has been reduced in relevance, with societal and moral issues dominating the decision making. These actions give me, and I trust you, hope and belief in a future for all. Who knows, maybe we will start signing twenty year leases in the Rainbow Nation and recover our status as a destination of choice for Global business and tourism! Experts suggest that as much as 40% of the Rands' weakness can be attributed to "South Africa specific" issues. If these were remedied, the world recover from its economic indigestion and start importing resources, and Emerging Markets regain their "mojo", might the Rand return to levels last seen in the mid-2000's?

We didn't believe that possible when Kevin Wakeford suggested it would last time the rand blew out to current levels, and he instigated the so called "Commission of Enquiry into the Rand". This wasn't caused by anything other than a stable outlook, fiscal discipline, the world falling in love with Emerging Markets, and a big resource demand from China and others.

Just consider this, as I said foreign investment calls are not for sissies! ■

"They [NFB's series of Multi-Asset Solutions] are inclined to re-balance, remove and replace underperforming funds or specific assets and do so in an unemotional way, lessening the behavioral risks typically displayed by us as individual investors."

RETIREMENT SAVINGS  AND DIVORCE

I recently assisted a friend who was going through a divorce. Financial planning is usually the last thing on one's mind when dealing with all the emotions, money matters, kids and changing circumstances, but it is important to consider how retirement benefits are dealt with in these situations, so that you are able to plan and adequately make provision for your retirement.

The current position in terms of the Divorce Act: a pension fund is permitted to pay a portion or all of the "pension interest" to the member's former spouse (referred to as the non-member spouse).

What does "pension interest" mean?

a. In respect of a member of a pension, provident or preservation fund: the total benefit to which the member would have been entitled to in terms of the fund rules, if their fund membership has ended on the date of the divorce by virtue of resigning from the fund.

b. In respect of a retirement annuity fund: the total amount of the member's contribution to the fund up to the date of the divorce, together with a total amount of annual simple interest (at the official prescribed rate), provided that this does not exceed the fund return.

For example:

Let's say a member's retirement annuity fund totals R1 200 000 as at the date of divorce, and the member contributed R50 000 pa since becoming a member 10 years ago. The amount that will be considered as pension interest is

R50 000 x 10 years, plus
15,5% pa simple interest =
R926 250 as your pension interest amount. The court will award either the total pension interest amount or a portion of it to the non-member spouse.

So it's important to calculate the value of the pension interest when negotiating the divorce settlement and not the value of the retirement fund.

Also important to note is that a life annuity or a compulsory life annuity (generally regarded as compulsory money), are not retirement funds and not included in the definition of pension interest, and therefore cannot be awarded to a non-member spouse upon divorce.

"How fund administrators deal with the division of retirement funds"

If you are getting divorced, and intend claiming against your spouse's retirement fund benefit, it is important that your claim meets specific conditions as set out in the Divorce Act or the Pension Funds Act. A fund will only make a divorce payment if the divorce order is binding on the fund and meets all of the criteria:

1. The divorce order must specify the pension interest assigned to the non-member spouse. In other words, the percentage or amount of pension interest must specifically be stated in the decree.
2. The fund must be identified by name or at least identifiable from the order. A simple reference to the member's "retirement fund" will not suffice.
3. The fund must be ordered to pay the non-member spouse. In other words, there must be an order to pay, and the order must be directed at the fund;
4. The divorce order must be valid, i.e. issued by a High Court, regional court or divorce court.
5. The member must still be a member of the fund on the date the divorce is granted.

If the divorce order does not meet all the criteria and is not binding on the fund, the administrator of the fund should inform the non-member spouse accordingly. In this instance, the member and the non-member spouse cannot come to an agreement between themselves. The court order must be amended.

What are the non-member spouse's options upon being awarded an amount from a retirement fund?

a. Take the full amount awarded as a cash lump sum (taxable);
b. Take a portion as a cash lump sum and transfer the balance to an approved preservation, pension, provident or retirement annuity fund;
c. Transfer the full benefit amount awarded to an approved preservation, pension, provident or retirement annuity fund.

Taxation

The non-member spouse who elects to receive a cash lump sum is liable for tax on the payment as per the withdrawal lump sum tax table.

If no lump sum is taken and the pension interest is transferred to another retirement fund, then no tax is due. The proceeds will be taxed in the hands of the non-member spouse, upon withdrawing or retiring from the fund at a later stage.

Should you have any queries or would like assistance with your retirement planning, please do not hesitate to contact an NFB Private Wealth Manager at one of our NFB offices in Johannesburg, East London, Port Elizabeth, Stellenbosch or Cape Town. ■

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KNOWLEDGE INTO **WEALTH**

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