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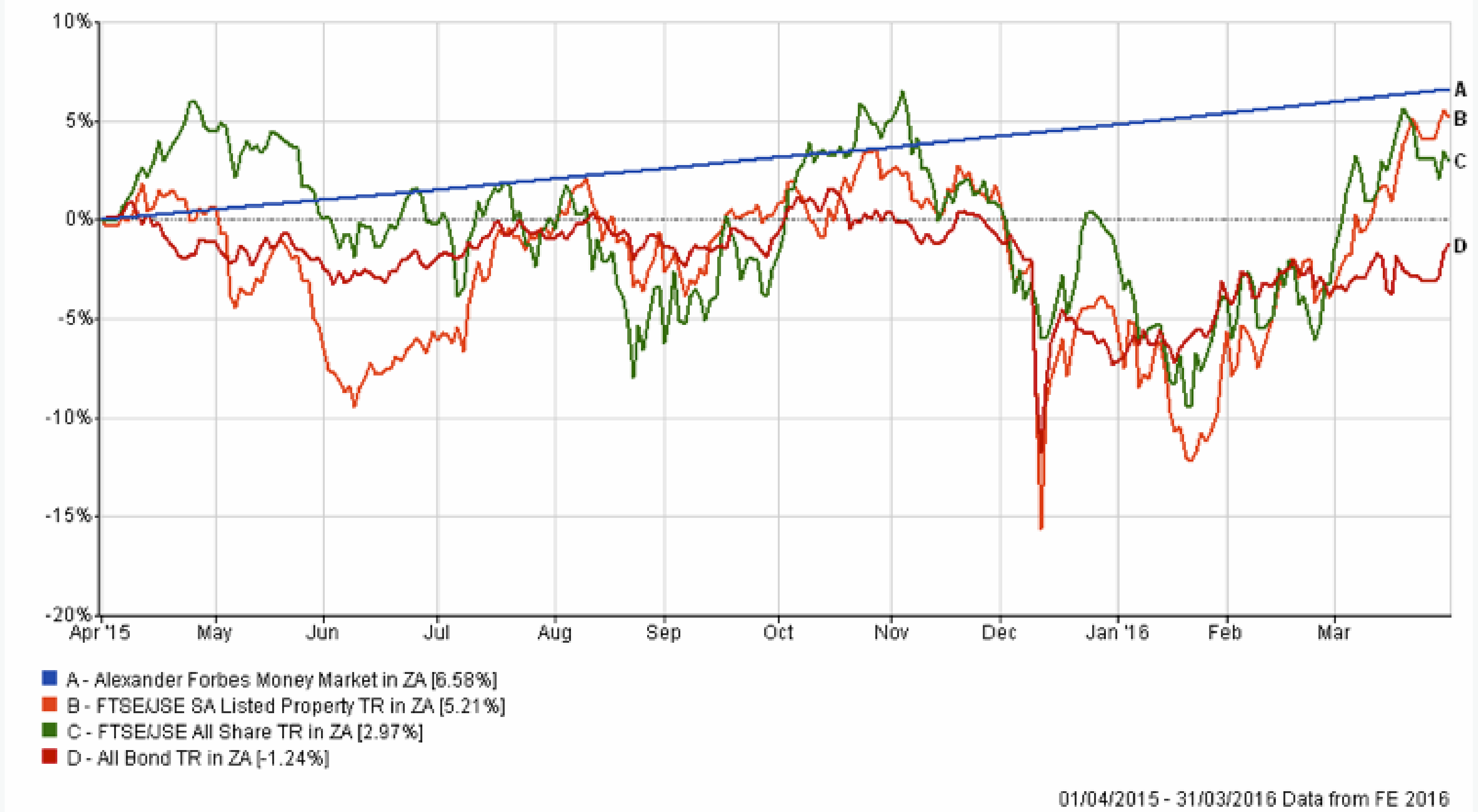
CLIENT NEWSLETTER **APRIL 2016**

Investing In a Volatile, Low Return Environment

Investors that have committed capital to the market in the past year to 18 months are finding it tough to stay invested. The JSE has been incredibly volatile, delivering single digit returns over the period. Bonds were hit very hard following the firing of Finance Minister, Nhlanhla Nene, delivering a negative 5% return over the year. While cash returns have been increasing on the back of rising interest rates, they remain low, and below inflation.

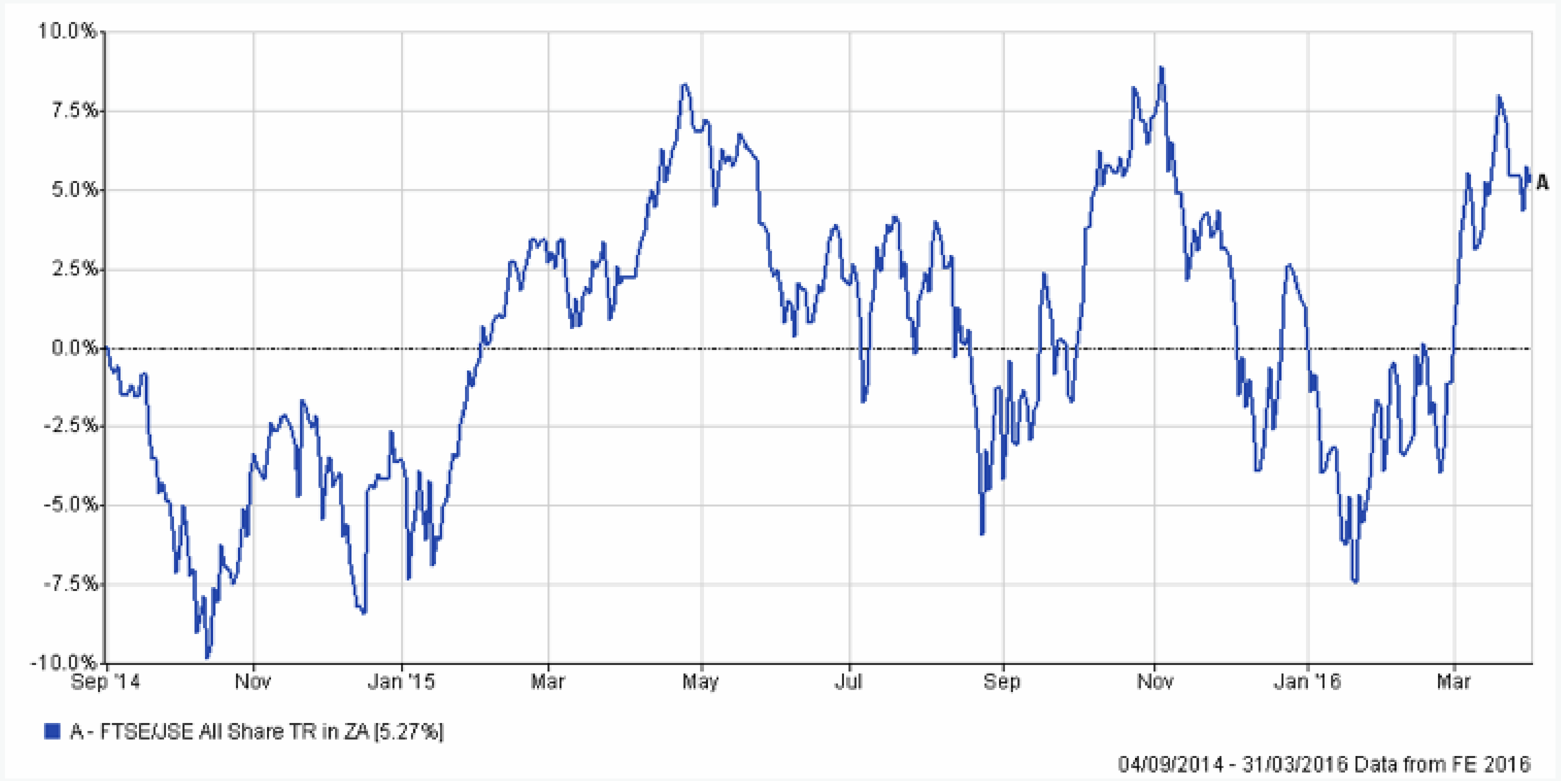
Low returns have not been for South African investors only. US and European investors currently earn less than 1% interest on deposits in the bank. It is estimated that 65% of government bonds globally yield lower than 1% per annum at the moment, up from 29% in 2010. This suggests that investors are prioritising capital preservation over return on capital at the moment.

Returns from the various asset classes are shown below:



The best performing asset class over the past year has been cash (money in the bank), followed by listed property, then shares, then government bonds. Bonds are considered a low risk asset class, but the firing of the finance minister caused bonds to lose close to 12% in the two trading days that followed, and for the asset to deliver its first annual loss since the financial crisis.

The other feature of the market that warrants more consideration is that of volatility. The JSE has delivered 5.3% since 04 September 2014, which was when the strong upward movement in the market ended. However, as shown in the graph below, the JSE has seen massive up and down movements during that time.



The major movements are summarised in the table below:

Start Date	End Date	Market Movement
04 September 2014	15 October 2014	- 10.0%
15 October 2014	27 April 2015	+20.1%
27 April 2015	24 August 2015	-13.3%
24 August 2015	04 November 2015	+15.7%
04 November 2015	21 January 2016	-15.0%
21 January 2016	18 March 2016	+16.7%

The challenge that investors face in a volatile, low return environment often centres on decision making when it comes to their portfolio and with any new capital that they may want to invest. Many investors know intuitively that by investing when prices are low they can make a higher return over time. They have seen the excess returns made by investors that invested during previous crisis and market crashes. However, when investors find themselves in that environment, they cannot seem to look past the short term noise and invest, or remain invested. This is human nature and consistent with other similar behaviours.

A study was done many years ago where a group of people were asked a question a week before they needed to actually make a decision. They were told that when they met a week later, they would have to choose between a piece of fruit or a chocolate for their afternoon snack. At that point, 74% of the audience indicated that they would opt for a piece of fruit. A week later when faced with the decision at the tea break, over 70% of the audience ended up having chocolate for their afternoon snack, and not a piece of fruit. What this study showed is that will power is a lot easier when 'exercised in the future'. This probably explains why so many people do not keep their New Year's resolutions or stick to that diet. The other finding from this study was that decision making in the present is often very different to what people thought they would have decided. So most investors know that they should remain invested even when markets get bumpy and returns disappear, because invariably volatility subsides and returns normalise. However, when in the midst of volatility and low returns, emotions tend to dominate and decision making often becomes less prudent.
This is not surprising when it comes to investments. We are acutely aware of the fact that the money that clients have invested with us is the outcome of years of hard work and sacrifice. That money will be needed to fund retirement, a child's education, a dream home, or that long overseas holiday. So it is understandable that emotions take over when things are not going well. The fear of not achieving those financial objectives grows. However, our fiduciary responsibility to clients demands that we do not get caught up in emotion or in prevailing market conditions. We need to keep a calm head and ensure that decision making by clients is always based on sound judgement and is the best decision for the long term.

Our approach during these volatile market and economic times is as follows:

◊ monitor the economy and markets even closer than normal,
◊ engage with the fund managers more than we usually do,
◊ increase the number of opportunities for client interaction where clients can raise the issues that concern them, or get more insight into what is happening around them. We recently had Stanlib fund manager, Paul Hansen, present to clients on the national budget. Other presentations are scheduled for later in the year
◊ convert our annual client letter into a quarterly letter aimed at dealing with various aspects of a volatile, low return environment, and
◊ encourage clients to proactively contact us if they wish to discuss any aspect of their investment.

It is only through increased dialogue and by actively engaging with the issues of the day that we believe that clients will ultimately make better decisions during this time, and achieve their financial goals and aspirations over time.

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