

# NEWSLETTER

September 2018

## MARKET OVERVIEW

Markets have been volatile this year, mainly due to global events. South Africa has not been spared from the volatility, as it has one of the most liquid foreign-exchange markets in the world (see chart below). Because of this, SA is highly susceptible to negative investor sentiment, especially towards emerging markets. Although most global economies are achieving decent or even strong economic growth, investor sentiment, especially outside the USA, was negatively impacted by events such as:

- + The ongoing trade war between the US and the rest of the world
- + Turkey's economic crisis. They raised interest rates to 24%
- + Argentine Central Bank hiking interest rates from 15% to 60%
- + Increasing short-term interest rates in the US
- + Higher bonds yields in the US
- + Political uncertainty in Italy

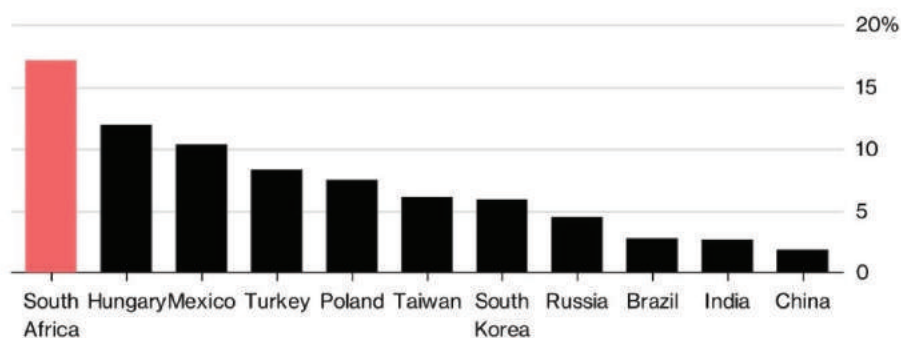
Domestic factors such as land expropriation without compensation, uncertainty around economic policies and negative economic growth created additional strain on local markets. There seems to be a positive change in domestic politics. President Cyril Ramaphosa announced a stimulus package to ignite economic activity, restore investor confidence, prevent further job losses and create new jobs. Markets received this well. Below is some of the key announcements.

- + Boost tourism and business travel by revising the visa requirements
- + Finality on the revised Mining Charter
- + Allocation of radio spectrum to reduce data costs
- + Reprioritisation of public spending to support job creation
- + Formation of an infrastructure fund
- + Bolstering the healthcare sector

## The Price of Liquidity

South Africa's active foreign-exchange market makes quick exits possible

■ Daily forex turnover as percentage of annual GDP



Source: Renaissance Capital

Bloomberg

<b>JSE All Share</b> -2,17%   55 789,76 ▼	<b>MSCI World (USD)</b> 4,98%   2 188,19 ▲	<b>MSCI EM (USD)</b> -1,09%   1 046,40 ▼	<b>SA Bonds</b> 0,81%   616,24 ▲
<b>SA Property</b> -1,01%   1 914,01 ▼	<b>CPI (q/q)</b> 1,12%   108,40 ▲	<b>Gold</b> -4,90%   1 186,82 ▼	<b>Platinum</b> -3,10%   816,09 ▼
<b>Oil</b> 9,80%   84,95 ▲	<b>£/R</b> 2,10%   18,55 ▲	<b>€/R</b> 2,30%   16,47 ▲	<b>\$/R</b> 2,80%   14,22 ▲

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## HOW DO WE CONSTRUCT PORTFOLIOS IN SUCH A VOLATILE ENVIRONMENT?

The aim of the Naviga portfolios is to deliver **consistent above average performance**. The consistency of returns reduces the timing risk of investing in the Naviga portfolios. Consistency is achieved by combining managers with different investment philosophies and investment styles. We aim to select managers with an investment philosophy and process that should result in outperformance (alpha) over the long term. Their investment style will, however, not necessarily always deliver alpha over the short term, as different investment styles typically rotate in and out of favour over time. By combining managers with different investment styles, consistency of investment outcomes can be improved over the short term. Boutique Investment Partners, the investment consultant of the Naviga portfolios, employs a multi-style QVMS (Quality; Value; Momentum and Size) approach (illustrated below) to construct portfolios. They categorise fund managers according to these prominent investment styles and blend them together to create the most robust portfolios possible. The Naviga portfolios will always aim to have an

exposure to all of these investment styles. We may, however, tilt the portfolio to a specific investment style within prudent limits during certain stages of the market cycle when a particular style or styles are expected to outperform others.



## EXAMPLE OF COMBINING MANAGERS WITH DIFFERENT STYLES

The Foord Balanced Fund (orange) and Investec Opportunity Fund (green) underperformed the peer group average (black) since Q3 of 2017 until February 2018 due to the quality and defensive nature of their funds (graph 1 below). We, however, maintained an exposure to these funds to balance the different investment styles in the Naviga portfolios as discussed above.

Subsequently, these funds were one of the top performing funds during a volatile market since March 2018, justifying their retention and taking a longer-term view on manager performance (graph 2 below). Forecasting markets over the short-term is impossible and, therefore, it is essential to maintain a balanced exposure to the different investment styles.

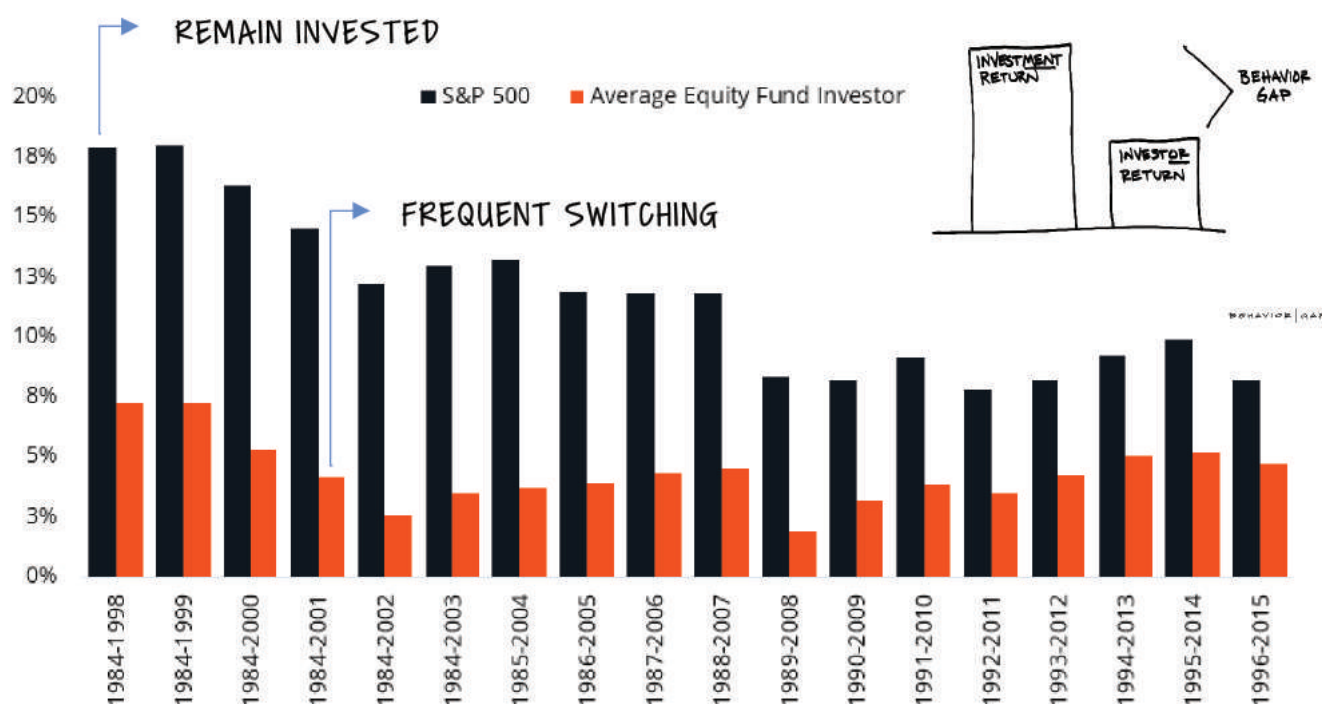


## TIMING THE MARKET AND FUNDS

The example above illustrates the risk of trying to time the markets or funds. As illustrated in the chart below, the average investor consistently underperformed the S&P 500 by 4% - 18%. Not many funds, however, underperformed the market by more than 4% (according to a study by Vanguard).

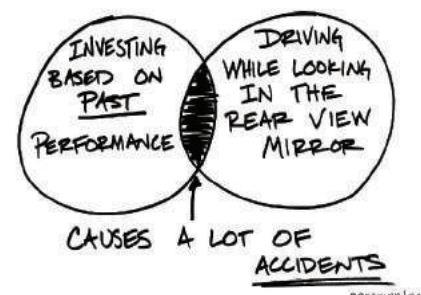
So why did investors underperform? The difference in the return achieved by investors versus the returns from funds, can be explained by switching between funds. Persisting with the long-term strategy of the portfolio, will improve the return for investors.

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Source: Quantitative Analysis of Investor Behavior by Dalbar, Inc. (March 2014) and Lipper

"The retention rate data for equity, fixed income and asset allocation mutual funds strongly suggests that investors lack the patience and long-term vision to stay invested in any one fund for much more than four years. This short-term retention does not adhere to a prudent, long-term strategy..." - Dalbar, Inc.



## CONCLUSION

Investing in well-diversified portfolios like the Naviga Portfolios continue to be the best approach to follow for achieving long term investment goals, especially against the backdrop of exceedingly difficult markets. The Naviga Portfolios are actively monitored, and changes implemented when necessary in response to market prospects and conditions. **Over-reactions to short term market movements are however avoided.** Investors can therefore rest assured that their investments are being prudently managed with an eye on the long term.