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INVESTING IN UNCERTAIN TIMES

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South African investors (at least those who pay no or little tax – such as retirement funds) have had a long period of remarkably good investment returns relative to inflation.

Over the last 10 years, the median (mid-ranking) asset manager in our Global Balanced investment survey category produced a gross-of-fees return of 15.7% p.a., compared to inflation for the same period of just under 6% p.a. This means that, even after fees and other costs and taxes, the typical retirement fund with a market-linked portfolio should have achieved real returns (returns in excess of inflation) of around 8% p.a. over this period. This is a much better outcome than we might have hoped for, 10 years ago.

All the main domestic asset classes – equities, the listed property sector, bonds and cash – produced good gross returns relative to inflation over this 10-year period. Only the returns on foreign investments, measured in Rands, would have disappointed, but for much of this period retirement funds were prevented from holding more than 15% of their assets offshore in any case.

Of course the journey has not always been a smooth one. There were difficult times in 2002 and early 2003 (and before that, in 1998) and also during the first stages of the “global financial crisis” in 2008 and early 2009. (Between June 2008 and February 2009, some Global Balanced portfolios lost as much as 25% of their value, although they recouped these losses quite quickly after that.) And it remains to be seen whether last month’s “relief rally” will be sustained or not.

We need to recognize however that the future will not look exactly the same as the recent past. The effects of the “global financial crisis” may take many years to work through the global financial and economic systems, as consumers and Governments gradually reduce their indebtedness, and it is by no means clear exactly how this will unravel.

One big change that we may be experiencing in South Africa is the transition from a time when real interest rates were quite high (i.e. when the returns on cash investments, before tax, were significantly higher than inflation) to a time of low or even negative real interest rates. This is bound to create new challenges for investors.

Therefore it seems prudent to assume that the coming years are unlikely to be as good for our retirement funds, and other investors, as the last 10 or 15 years have been (when taken as a whole). Real returns could be significantly lower and once again the journey is unlikely to be smooth. For most investors a strategy of sensible diversification will probably be the most suitable, where one aims to capture returns from a variety of different sources. This should certainly encourage retirement fund Trustees to make use of their ability to invest up to 25% outside South Africa, if they are not already doing so.

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