PRIVATE WEALTH MANAGEMENT

PWM CONNECT 2nd Edition 2024

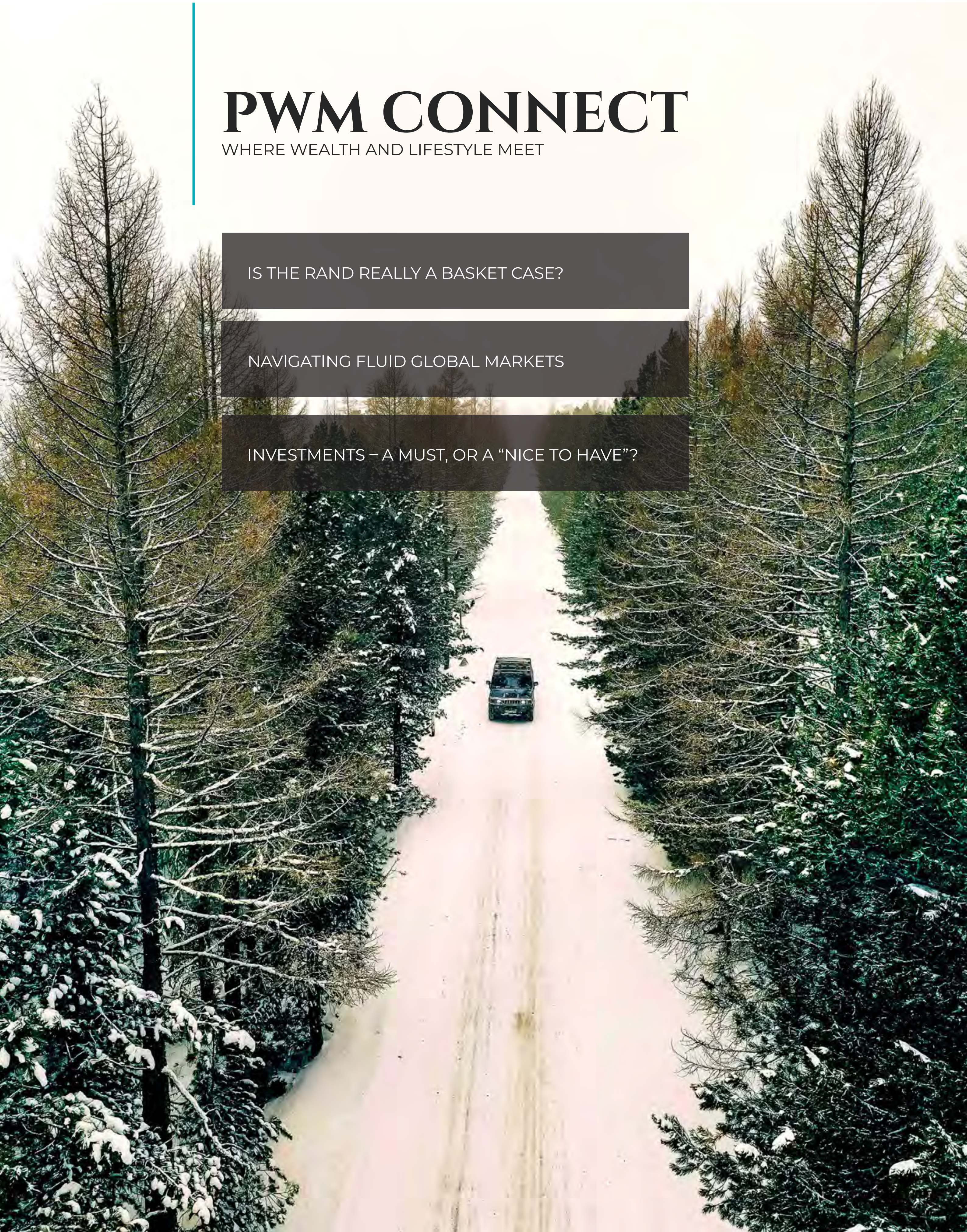
PWM CONNECT

WHERE WEALTH AND LIFESTYLE MEET

IS THE RAND REALLY A BASKET CASE?

NAVIGATING FLUID GLOBAL MARKETS

INVESTMENTS – A MUST, OR A “NICE TO HAVE”?



WHAT'S INSIDE

A WORD FROM PIETER

Welcome to the second edition of PWM Connect, curated exclusively for our clients.

As we embrace the winter season of 2024, we reflect on the recent successes of our second annual business conference, where we gathered our product partners to present on market trends and share contemporary thought leadership.

Amidst these discussions, we couldn't ignore the recent South African elections and the potential impact on local markets. This significant event has sparked insightful conversations among our partners, enhancing our understanding of the evolving economic landscape.

Our commitment to collaboration and growth extends beyond the conference. We're excited to showcase articles from our partners in our newsletter, providing you with strategic knowledge to ensure you remain ahead in your financial journey.

- M&G navigated the complexities of global markets, offering strategic insights into its global balanced portfolios.
- Allan Gray dissected the innovative two-pot system, emphasising its role in safeguarding retirement fund savings.
- Just SA unveiled a forward-thinking, blended retirement income solution which combines living and life annuities to adapt to changing market dynamics, ensuring flexibility in retirement planning.

I trust that you will find this edition with its diverse content interesting.

Enjoy the read!

Kind regards

Pieter Bester
CEO

IS THE RAND REALLY A BASKET CASE?

By Izak Odendaal | Chief Investment Strategist | Old Mutual Wealth

The rand rallied following the election and the formation of a centrist Government of National Unity (GNU), which is likely to be positive for South Africa's medium-term economic growth prospects.

However, at the end of June, the rand still traded at R18 to the dollar. When it was introduced as a decimal currency in 1961 at a rate of two rand to one South African pound, one dollar cost R0.72. In 1981, the rand traded one-to-one to the US dollar.

Today, an American needs only five US cents to buy a rand. To many, this is the ultimate indicator of decline. Exchange rate changes also poses particular questions for people making investment decisions as they head into retirement.

As always, however, some perspective is helpful.

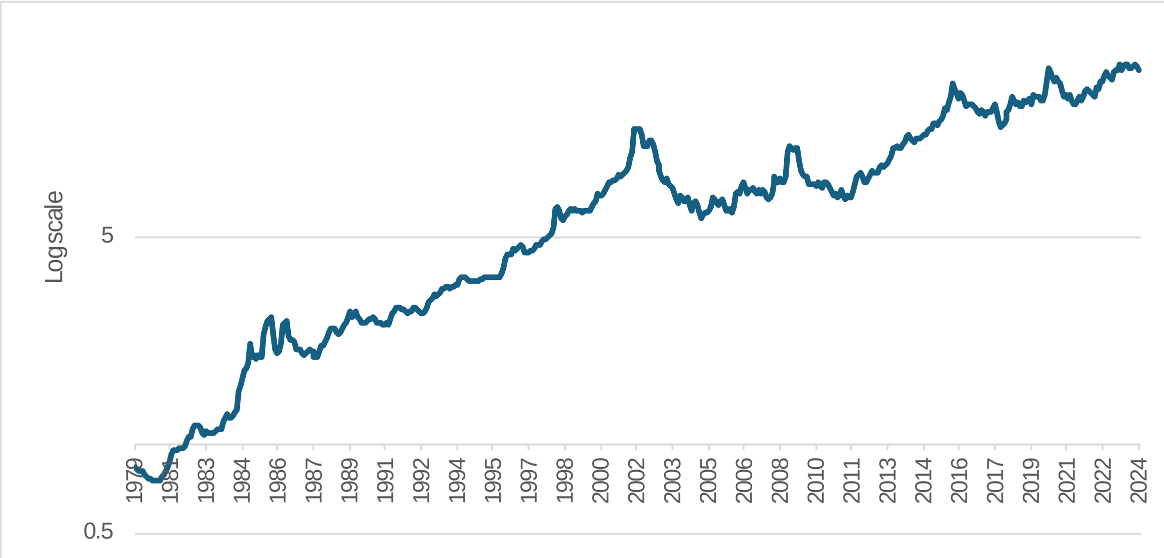
The rand-dollar exchange rate was controlled by the government until 1981, when the peg was abandoned and the exchange rate was largely (but not completely) left to the market. The rand depreciated at a faster pace between 1980 and 1994 (12% per year) than from 1994 onwards (6% per year). Drawing the chart on a log scale makes that clear. In fact, the pre-1994 picture is flattering, since it was a period of extremely harsh capital controls (contravention of which was punishable by jail time) and a parallel currency for use by foreigners, the financial rand, that traded at a steep discount to the commercial rand in use domestically. In other words, Chart 1 actually understates the extent of the currency weakness. The financial rand was finally abolished in 1995 and it now trades free of any intervention. Capital controls have been greatly relaxed. For practical purposes, exchange controls do not apply to most individuals anymore.

In other words, a weak rand is not something to blame on the current government, since the rand fell much faster prior to the transition to democracy.

So why does the rand weaken over time? In simple terms, South African inflation has been consistently higher than US inflation over the past 43 years, so you would expect the rand to decline. This is the theory of purchasing power parity, which implies that the exchange rate adjusts over time to equalise price levels between two countries.

The rand has, in fact, on average fallen a bit more than inflation differentials would predict – a factor we can probably ascribe to it being a highly traded currency of an economy that persistently runs current account deficits and therefore always needs to import capital. It has suffered several blow-out episodes (1985, 2001, 2008, 2015, 2020), when fundamentals go out the window and investors indiscriminately sell the rand during times of global financial stress.

CHART 1: THE RAND-DOLLAR EXCHANGE RATE



SOURCE: LSEG DATASTREAM

Government policies since 1994 have not helped, however. Inadequate infrastructure, especially persistent electricity shortages, drive up the cost of doing business and reduce global competitiveness. Despite the Reserve Bank's best efforts, inflation averages much higher than in the US. Even though the government sets the Reserve Bank's 3% to 6% target range, it has been one of the biggest inflation culprits, with a range of administered prices consistently rising faster than CPI, such as electricity and municipal tariffs. The government has also given generous above-inflation wage increases to its employees, which in turn puts upward pressure on private sector wages, again weighing on competitiveness. All this implies that the rand will probably continue to follow a weakening trend over the long term.

However, it will not necessarily depreciate at the same pace over the next decade as over the previous 10 or so years. Remember that the rand was strong relative to underlying fundamentals back in 2011. The taller you are, the harder the fall, and the rand fell rapidly from that point (around R6,70 per dollar in mid-2011). Today the rand is weak, limiting the downside. In fact, from current oversold levels, it could very well strengthen to a more neutral level over the next year or so before resuming the longer-term weakening trend.

The other key point when considering an exchange rate is that there are two parts: the rand and the dollar in this instance. The dollar appreciated against virtually all currencies from 2011 onwards and is now strong across most measures. In other words, a bet that the rand will fall as much over the next decade as over the previous decade implies that the dollar will continue to strengthen to a similar extent from current levels, which seems unlikely.

Unfortunately, getting the timing of exchange rate moves right is nearly impossible. All we can do is identify points where the currency is trading at extremes – very strong or very weak – and position portfolios accordingly. When the rand is very strong, it makes sense to increase global exposure, and when the rand is weak, we can increase local exposure in anticipation. Or rather, given the persistent negativity towards South Africa in recent years, the weak currency has been a compelling reason not to fully join the rush offshore.

It is also useful to compare the performance of the rand versus other emerging market currencies.

Why is it that the rand trades at around 18,40 against the dollar (an '18-handle' in the jargon), while the Thai baht trades at around 36, the Indian rupee at around 83 per dollar and the Chilean peso at around 900?

Most of these countries experienced rampant inflation at some point, which caused a plunge in the value of their currencies against the dollar. Yes, the rand has been weak, but it pales in comparison with the experience of other emerging markets at various points in the past half century. For some, the dire collapse is still underway. The Argentine peso lost 95% of its value in the past five years and the Turkish lira 81%, while the rand lost 20% of its value.

But it gets worse. Both the peso and lira are 'new' currencies. The current version of the lira was introduced in 2005 after a bout of runaway inflation. In the case of Argentina, the 1992 peso was the fifth currency of the 20th century. The new president, Javier Millei, wants to abandon the worthless peso altogether and simply use the US dollar as legal tender.

From 1967, Brazil has had four different currencies: the cruzeiro, the cruzado, the cruzado novo, the cruzeiro real, and – from 1994 to the present – the real.

Chile adopted its peso in 1975, replacing the escudo 1 to 1 000 (the escudo replaced an earlier peso in 1960 at 1 to 1 000).

Indonesia introduced a new rupiah at 1 to 1 000 old rupiah in 1965 and at 378 to the dollar. Today it trades at 16 546 per dollar (that is sixteen-and-a-half thousand!). To its credit, Indonesia has improved its economic fundamentals, and the rupiah has been remarkably stable in recent years.

Mexico introduced a new peso in 1993 at 1 to 1 000 old pesos and 3 to the dollar. It currently trades at around 16,80 per dollar.

TABLE 1: HOW MUCH MORE 1 US DOLLAR COSTS IN SELECTED EMERGING MARKET CURRENCIES COMPARED TO JANUARY 1995

ARGENTINIAN PESO	84 984%
TURKISH LIRA	79 403%
NIGERIAN NAIRA	6 240%
RUSSIAN ROUBLE	2 289%
EGYPTIAN POUND	1 292%
PAKISTAN RUPEE	799%
INDONESIAN RUPIAH	611%
BRAZILIAN REAL	488%
SA RAND	433%
COLOMBIAN PESO	366%
HUNGARIAN FORINT	232%
MEXICAN PESO	206%
INDIAN RUPEE	164%
CHILEAN PESO	135%
MALAYSIAN RINGGIT	84%
POLISH ZLOTY	63%

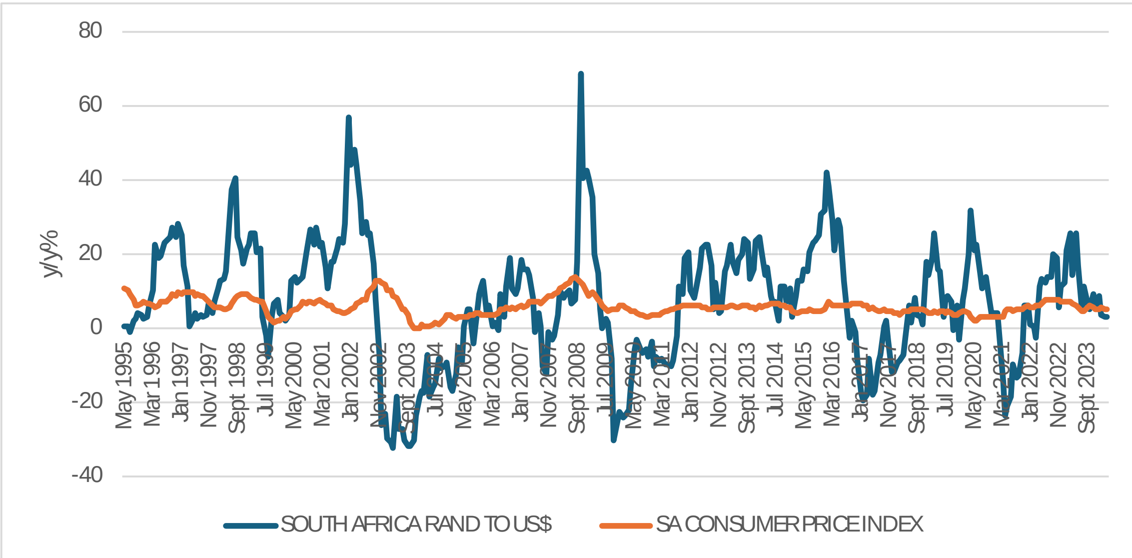
SOURCE: LSEG DATASTREAM

In other words, compared to its true peer group, the rand is not nearly the basket case it is often made out to be. South Africa has had a mild inflation history compared to these other countries, who have often resorted to money printing to fund the government. As can be seen in neighbouring Zimbabwe, the resulting hyperinflationary episodes wipe out domestic savings and wreak economic havoc.

With a credible and independent Reserve Bank focusing on keeping inflation under control, the odds of a spectacular rand collapse remain slim. Also important is a sophisticated domestic financial system and deep and liquid local markets. Over the years, the 'original sin' of many emerging markets is the inability to borrow in domestic markets, forcing them to turn to international lenders.

The fact that South Africans must pay 433% more for a US dollar today compared to 1995 does imply a loss of international purchasing power, but remember that local incomes have also increased over this period, faster than the rand has depreciated. The dollar income of the average South African worker is about 50% higher than in 1995. Moreover, the pass-through of rand weakness to domestic inflation is never 100%, in fact, the Reserve Bank estimates pass-through is usually 10% to 20%. In other words, only a portion of rand weakness shows up in domestic inflation. As Chart 2 illustrates, in 2001 the rand was 60% weaker than in 2023 (a positive number on the chart means a weaker rand on a year-on-year basis), but inflation peaked at 11% a few months later. Local prices are not as sensitive to the exchange rate as is often assumed.

CHART 2: ANNUAL CHANGES IN THE RAND-DOLLAR EXCHANGE RATE AND DOMESTIC PRICES



SOURCE: LSEG DATASTREAM

Export sectors obviously benefit from a weaker dollar, as do South Africans who invested abroad. This is where the rubber hits the road. How much should currency views influence offshore investment decisions? It should not be the only factor.

For one thing, the time horizon matters. For a long-term 'strategic' investment in international markets – say 20 or 30 years – today's exchange rate is virtually irrelevant. Over shorter horizons, there is always the possibility that the rand can strengthen and hurt offshore returns. Secondly, do not obsess over the current exchange rate while losing sight of valuations. At the current moment, the rand is cheap, but so are South African equities and bonds. Therefore, a switch to offshore assets implies selling a cheap rand and cheap local equities and/or bonds. Ultimately, it is the underlying investment (equities, bonds, property) that must do the hard work of generating returns. Exchange rate movements are a cherry on top (or a bitter aftertaste). Sizable offshore exposure is always prudent for local investors because of the much greater opportunity set of international shares and bonds to invest in. But it is always a balancing act, weighing up the respective return outlooks of local and international asset classes with the risks posed in each case. It is never just about the rand.

BE AWARE OF THE SHIFTING GOAL POSTS

By Andrew Whitewood | Managing Director | PWM Wealth Management

One day last week, I sat back and reflected a little on life. I have been in the financial services industry for over a decade now. I have a beautiful wife and two very busy little twin girls running around at home. I am in a fortunate position – privileged, some might call it – but I am grateful for what I have and for what we as a family have worked for.

The world as we know it is definitely changing in some respects. People are most definitely living longer, therefore people need to work longer or save more – a rather simple equation. Climate change is real – we just need to look at the tornado in KZN and the drought turned into flood in the Eastern Cape.

However, some things stay the same. I read articles about how expensive the property market currently is in Europe, how expensive the property market is in Cape Town, etc. My parents bought our family home in Gqeberha before I was born for R25 500. My father was only earning like a couple of hundred rands a month. They had to live, pay the bills, and still save. They experienced interest rates in the twenty-odd per cent range – we are fighting against interest rates ranging in the early double digits. Unfortunately, life is not a simple straightforward straight line.

We are living in a world of instant gratification, which is very distracting. Our family loves to order online and the 'Uncle' rings our bell to deliver our purchase. However, when we talk about financial planning, saving, retirement planning, etc. we need to have a structure, a plan – we need to be committed.

As I stated earlier, some things are changing and some things are staying the same. We need to start saving earlier to benefit from compound interest, we need to save more than the so-called '15% rule', as we are going to live longer. We need to be open-minded to the fact that when we are forced to retire at 63, we might well need to reinvent ourselves to generate some sort of income in our later lives.

We are also seeing a big shift around us, where younger families are building flats on their properties for parents. This makes sense: the elderly folk are close by, they can help out with the little ones when needed, it cuts down on family overheads and leads to a nice yield-generating asset on succession.

In closing, we need to be aware of the shifting goal posts. However, we also need to stop focusing on all the negative headlines and focus on ourselves, what we can do and control in order to assist ourselves with enjoying our financial journey.

NAVIGATING FLUID GLOBAL MARKETS

By Sandile Malinga | CIO of Multi-Asset | M&G Investments

With a disappointing first quarter of 2024 behind us, many South African investors may be thinking about adding global exposure to their portfolios in an attempt to enhance their potential returns. To get it right, global investing requires a long-term view, careful analysis and diversification, and patience in the face of the continuous, unpredictable fluidity of financial markets. So what does this fluidity look like at the moment? How are we at M&G Investments viewing it and investing for the best outcomes in our global balanced portfolios?

At M&G we don't rely on forecasts in making our investment decisions. Instead we use fundamental valuation-based analysis to build robust, well-diversified portfolios that can deliver strong returns no matter what scenario plays out in the global markets. Then we take advantage of short-term market mispricing to add extra value. Here's how our global balanced portfolios are currently positioned.

LEANING INTO THE EAST

Looking at China, not too long ago it was considered that the country would lead the global economy out of the Covid recession. Instead, it has faced much slower-than-expected growth and very negative investor sentiment, resulting in an (in our view) indiscriminate sell-off in equities in late 2023 and early 2024. Of course, we like narratives such as these because that's often when we find tactical investment opportunities. Indeed, believing in the country's stronger long-term growth prospects, we found some excellent opportunities to buy high-quality global companies at cheap valuations. We are maintaining a tactical overweight Chinese equity position in many of our global funds.

There are also some interesting aspects to Japan at the moment. The strong performance of Japanese equities in the past year has proved beneficial for our global balanced portfolios, where we have been tactically overweight these assets before taking profits more recently. In March, the Bank of Japan's historic interest rate hike to implement a positive real interest rate, and the easing of its yield curve control policy, have presented more opportunities for investors. However, these changes also merit some . There is a chance that the higher government bond yields could attract investors away from Japanese equities, adding selling pressure to the market.

AN ECLECTIC MIX OF EQUITIES

Beyond Asia, we are overweight European stocks on valuation grounds, but try to avoid the UK for the same reason. We are also overweight Latin America, where we're invested in a diverse range of companies. We have had opportunities to buy companies trading on attractive P/E ratios of anywhere from 9X earnings, provided the country's macro backdrop is positive for growth, inflation is under control, and the currency is quite cheap.

We're tilted away from sectors with high valuations in the US and, overall, are underweight the relatively expensive US market, instead favouring non-US markets. During Q1 2024 we moved to be slightly more defensive in our overall portfolio positioning given the phenomenal rally in equities that has been underway, without underlying fundamentals really improving as well. As a consequence, we took some profits in global equities (such as from our overweights in US and European financials) and used the proceeds to increase our cash holdings. This has given our funds an overweight position in global cash, with more agility when buying opportunities arise.

30-YEAR US TREASURIES OFFER RARE REAL RETURN

Currently about 25% of our portfolio is invested in global bonds, of which around 60-65% are US securities, even though the US Treasury has been issuing bonds quite aggressively. We have found that the relationship between supply and demand has very little to do with where actual spot rates or yields are trading. Currently, long-dated US Treasuries are paying a real yield of 1.5%-2.0% for the first time in a very long time, and they perform well when interest rates are falling and the world is worried about risk. We are holding a mix of 30-year US Treasuries, 20-year UK gilts and 30-year JGBs (with the Japanese yield curve quite steep), as well as sovereign bonds from select Latin American countries where yield spreads are attractive. As for corporate credit, in our view yields are not compensating investors adequately for the risk involved, and have a small underweight exposure in these assets.

From the above, it is clear that from a global perspective our portfolios are rather cautiously positioned, with an overall neutral to slightly underweight exposure to global equities and a high degree of careful diversification across both US and non-US equities. We also have solid exposure to longer-dated sovereign bonds in select countries, and are overweight cash. And while this may be our current "best-view" fund positioning, the key to earning the greatest prospective returns from fluid global financial conditions is to invest for the long term in well-diversified, risk-aware portfolios grounded in fundamental asset valuations, where active managers can also add value through shorter-term mis-pricing opportunities.

OPINION PIECE - RETIREMENT SAVINGS

THE TWO-POT SYSTEM AND YOUR SAVINGS WITHDRAWAL BENEFIT

By Jaya Leibowitz | Manager Retail Legal | Allan Gray

First published in October 2023, updated February 2024.

Big changes to the South African retirement system are coming, which may change how you interact with your retirement savings – including the ability to access a portion of your investment in an emergency. Jaya Leibowitz reminds us not to lose sight of the importance of preserving retirement savings, and s investors against dipping into these funds unnecessarily.*

Commonly referred to as the “two-pot system”, the new rules applicable to retirement funds, proposed to launch on 1 September 2024, will require all future contributions made to retirement funds, including the Allan Gray Retirement Annuity Fund and the Allan Gray Umbrella Retirement Fund, to be split into two portions: two-thirds of your contribution will be allocated to a retirement component, which must be preserved until you retire, while the remaining one-third will be allocated to a savings component, from which you will be able to withdraw once per tax year prior to your retirement (referred to as a “savings withdrawal benefit”). The withdrawal amount will be limited to the value in the savings component at the date of withdrawal.

The main idea behind this new system is to promote the preservation of retirement fund savings until retirement, while also providing retirement fund members with some access to their savings in times of need before they reach their retirement age.

The most recent draft of the amendments to legislation requires that, when the new system is implemented, a portion of the savings in a member’s existing retirement fund account, amounting to the lesser of 10% or R30 000, must be allocated to their savings component. This means that existing members who need access to cash will be able to access a savings withdrawal benefit shortly after implementation.

While access to one savings withdrawal benefit per year may come as a welcome relief to many who genuinely need it, if you are able to, you should rather use (or set up) a separate emergency fund for this purpose and do what you can to preserve your retirement investment for its intended purpose: to provide you with an income in retirement.

IMMEDIATE IMPACT OF ACCESSING A SAVINGS WITHDRAWAL BENEFIT

In terms of the new legislation, a savings withdrawal benefit will be included in the member’s gross income for the tax year in which that benefit was accessed. This means that the amount withdrawn will be taxed at the member’s marginal tax rate. If you are unemployed and have no income in the year of the withdrawal, you would be able to withdraw up to R95 750 from your savings component tax-free (this is the tax threshold for South African tax residents under the age of 65). As mentioned above, the maximum amount available for a savings withdrawal benefit will be the amount that has accumulated in the savings component (contributions plus growth, less any costs) at the date of the withdrawal. However, if you are earning, it is important to understand that because it is included in gross income, the withdrawal amount could push you into a higher tax bracket. This tax treatment aims to discourage individuals from accessing a savings withdrawal benefit when they have other sources of income and don't really need to dip into their retirement fund savings.

By way of example: Sally is a 35-year-old full-time employee with a taxable income of R370 000. Based on the 2024/2025 income tax table (see Table 1), her tax liability will amount to R59 997 (R42 678 + 26% of the amount above R237 100 – primary rebate of R17 235). If Sally decides to access a savings withdrawal benefit of R25 000, she will be pushed into a higher tax bracket and will be liable for tax of R67 722 (R77 362 + 31% of the amount above R370 500 - primary rebate of R17 235).

TABLE 1: PERSONAL INCOME TAX RATES FOR THE 2024/2025 TAX YEAR

Taxable Income	Tax Rate
R0 – R237 100	18% of taxable income
R237 101 - R370 500	R42 678 + 26% of taxable income above R237 100
R370 501 - R512 800	R77 362 + 31% of taxable income above R370 500
R512 801 - R673 000	R121 475 + 36% of taxable income above R512 800
R673 001 - R857 900	R179 147 + 39% of taxable income above R673 000
R857 901 - R1 817 000	R251 258 + 41% of taxable income above R857 900
R1 817 001 - above	R644 489 + 45% of taxable income above R1 817 000

NOTE: REBATE ARE DEDUCTIBLE FROM TAX PAYABLE: R17 235 PER YEAR FOR ALL INDIVIDUALS; R9 444 FOR TAXPAYERS AGE 65 AND OVER; R3 145 FOR TAXPAYERS AGE 75 AND OVER.

LONG-TERM IMPACT OF ACCESSING A SAVINGS WITHDRAWAL BENEFIT

Accessing a savings withdrawal benefit at any time prior to retirement may have a far bigger impact than you realise. If you are young, you may think that you will have plenty of time to save the amount that you have withdrawn, but not preserving that investment will cost you more than you may think as you will miss out on the power of compounding. Often referred to as the "eighth wonder of the world", compounding means you earn returns today on the returns you earned yesterday, over and above the amounts of money you contribute.

If, for example, you plan to retire at age 65 and decide to take a savings withdrawal benefit of R50 000 at the age of 35 to spend on a holiday or a few months of fun, you could lose out on up to R870 000 that would have been used to provide you with an income during retirement. That's a big difference. (Total investment growth assumed is 10% per year for 30 years – inflation at 6% plus 4% – and the investment is assumed to grow at a steady rate; no volatility is taken into account).

EMERGENCY WITHDRAWALS

Despite the above, there may be urgent reasons why a member of a retirement fund who does not have an emergency fund may need to access their savings withdrawal benefit – such as to pay for medical expenses, pay off outstanding debt or fund basic living costs during a time of unemployment. Before going ahead with a withdrawal, consider the questions below and talk to your independent financial adviser:

1. Do you really need the withdrawal amount to pay for something important? If yes, do you need the full amount or could you reduce it?
2. What is your marginal tax rate likely to be in the year of the withdrawal and how might the withdrawal amount impact your overall tax liability?
3. How much tax are you likely to pay on the withdrawal itself?
4. How is the withdrawal likely to impact your long-term savings towards retirement?

STAYING INVESTED IS KEY

Wherever possible, retirement fund members should avoid accessing their savings withdrawal benefit. If you have another source of capital and/or income and do not have essential expenses that you would not otherwise be able to afford, always maintain your investment in your retirement fund. Staying the course will significantly impact the amount of money you will have to provide you with an income during your retirement.

*Note: This article is based on the most recent draft of the proposed amendments to legislation. The final legislation assented to by the president may differ from the current draft, which may impact the information and examples set out above.

HOW TO CUT YOUR COAT ACCORDING TO YOUR CLOTH IN RETIREMENT

Article by Jaco Pienaar | Business Development Manager | Just SA

If you are approaching retirement and trying to figure out what retirement income product to buy once you retire, consider the adage that it's always best to cut your coat according to your cloth.

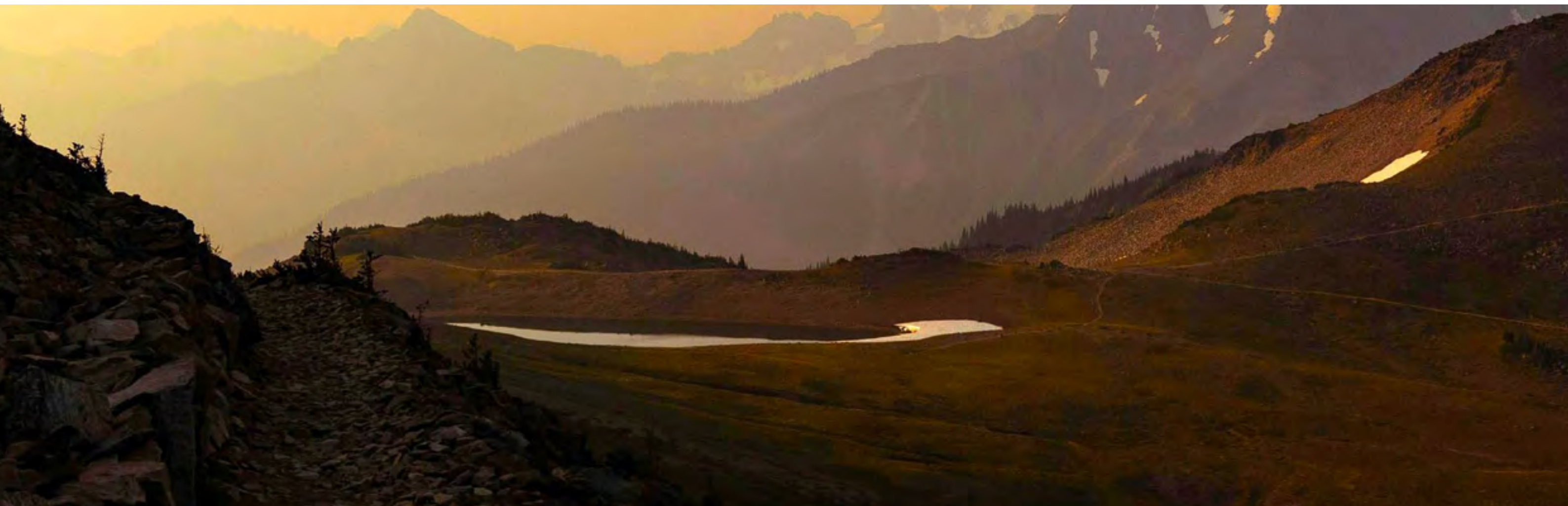
South Africans are notoriously poor savers which means that when it's time to retire, many of us haven't saved enough to be able to spend liberally in our leisure years. Instead, we have to sharpen our budgeting pencils and see how we can cut down on costs. However, it's easy to avoid this exercise and decide instead to cut a larger amount from your savings 'cloth' in your early retirement; but then you might not have enough cloth to complete the coat!

Budgeting for retirement starts with dividing your expenses into essentials, such as housing, food, water and electricity, transport, and your phone; and non-essential or discretionary expenses. These could be things like expensive holidays, regularly eating out, and buying luxury goods.

Then, you need to choose a retirement income product that at the least guarantees to cover your essential expenses for life. Historically, retirement options were limited to either a life or a living annuity. Each has its advantages and its disadvantages.

A living annuity allows you to decide how much income to draw from your investment annually, as long as it is within the regulated limits of 2,5% to 17,5% per year. While this offers retirees great flexibility, it also comes with potentially great risk. There is no guarantee that your income will last as long as you do – you might run out of money if you draw too much too soon. Also, because your capital goes up and down with investment markets, so can your income.

Life annuities, on the other hand, are an insurance product. They offer less flexibility, but greater security, as your income and annual increases are priced in at the start. With a life annuity, you're guaranteed a monthly income for life, which never decreases, eliminating the risk of living longer than your retirement nest egg can cover.



The retirement landscape has evolved, and choosing an annuity for retirement is no longer an ‘either or’ decision. There are new-generation, blended annuity solutions that can be tailored to suit your unique circumstances and risk appetite when you retire.

If you value the flexibility that comes with a living annuity but want to access a higher, sustainable monthly income that a life annuity offers, a blended annuity could be the right solution. This innovative concept combines the benefits of a living annuity and a life annuity in one investment vehicle. You decide how much of your investment is allocated to the living annuity and how much is allocated to the lifetime income portfolio.

An added benefit is that a blended annuity removes the threat of increasing drawdown risk (having to draw more of your living annuity money as your money runs out). This is because the stable income from the guaranteed life annuity component gives you a safety net. So, if assets you are drawing from the living annuity portion ever become depleted, your income from the life annuity will never fall below the guaranteed income level.

Just SA’s annuity solutions address important gaps left by traditional providers of life and living annuities in South Africa. Speak to your PWM financial planner to find out more.

INVESTMENTS – A MUST, OR A "NICE TO HAVE"?

By Charl Coetzer | Financial Planner | PWM Pretoria

INTRODUCTION

Investments are something most people have heard of and understand to some extent. We know that investments are important and can bring financial rewards if approached correctly. But how do you know what types of investment are appropriate at different stages of your life cycle?

Before we look at different types of investment, it is important to take note of the following:

- **GOALS –** The type of investment that you are going to choose will depend on your financial goals. The first step will be to clearly define your financial goals so that you have a clear understanding of your current financial position and the financial outcome you want to achieve.
- **RISK –** Risk refers to the uncertainty surrounding the outcome of your investments and the chances of something happening that will impact your investment negatively. Some people are inclined to take more risk than others. You must accept the fact that there are always investment risks, and the higher return you want, the more risk you must take. That is why it is important to understand the concept of risk, market volatility and different levels of risk for different types of investments. Generally speaking, younger persons can afford to take more risk as they are able to invest for a longer period.

Considering the myriad investment types and products available, investment decisions can be quite daunting.

The following questions arise when pondering this matter:

» How will it impact me financially?

» What risks must I be aware of, and can I afford to take risks?

» What if I just keep my money in a savings account?

It is important to understand that every type of investment has its place depending on the investment goal and time horizon. It is necessary to have a savings account, but keeping all your money in a bank account will not be wise over the long term, as your capital value will depreciate due to not keeping up with inflation. The income tax implications may also be substantial.

Diversification is therefore key, as is the implementation strategy. For a young person looking to get a financial plan in place, certain types of investment may deserve priority. Your financial plan also needs to be adjusted as your circumstances change. Human life expectancy is increasing, which means that you must provide sufficient income for a longer retirement phase. As higher inflation, interest rates, property and fuel prices, along with a weaker rand over the last few years impact investments more and more, it is very important to start saving from a young age selecting the right investment vehicles to help your financial situation improve and make your life goals attainable.

There is a wide range of investment products. Let's take a look at three investment vehicles that are crucial to consider for a favourable financial outcome over the long term:

1. RETIREMENT ANNUITIES

Retirement planning is an important part of holistic financial planning. It is easier to reach your retirement goals if you start saving towards retirement when you are young, due to the power of compound interest. When contributing towards a retirement annuity fund you will enjoy the same tax benefits as allowed for pension and provident funds. This investment vehicle will provide an income when you retire.

Key features of a retirement annuity policy:

- You can only invest in Regulation 28 compliant funds. (There are limitations on the percentage of funds allocated to each asset class within the fund – e.g. you cannot have more than 75% equity exposure.)
- The earliest that you can access (retire from) a retirement annuity is at age 55 (unless you become disabled at a younger age).
- Generally speaking, a maximum of up to one-third of the retirement savings may be taken as a lump sum on retirement (however, you don't have to take any amount as a lump sum).
- The first R550 000 of the lump sum received on retirement will be taxed at 0%, effectively making it tax free. (Please note that this amount of R550 000 is cumulative over your lifetime, and any other lump sums previously received from other retirement annuity, pension, provident or preservation funds or a severance payment received from an employer will impact your tax liability).
- On retirement, you will be required to use the remaining capital value (after the payment of the lump sum, if any) to buy either a life annuity or a living annuity that will provide an income.

Life Annuity:

A life annuity is paid at a fixed rate including various options – e.g. inflation-linked increases, increases at a fixed percentage per year, or a "level" income without annual increases. The last option will provide you with the highest income initially but will lose purchasing power over time, as your income will not be increased annually. You will receive a guaranteed monthly income for life, with the income levels being dependent on the type of life annuity chosen. This is a good option for investors with a very low risk appetite and who don't want to worry about the volatility of the markets.

Living Annuity:

This type of annuity is riskier being subject to market risk, but has more growth potential. Your monthly income from this annuity will depend on your chosen percentage drawdown from your annuity value. A percentage drawdown of between 2.5% and 17.5% of your capital value is allowed, with the flexibility to adjust the drawdown percentage once a year. A sustainable drawdown percentage is around 4% per year. It is not smart to withdraw a big percentage, as the aim is to allow your capital to grow while funding your monthly income from the proceeds of your invested capital. By opting for a sensible drawdown rate, you will be able to sustain your income, otherwise you run a serious risk of depleting your capital before you die. Bear in mind that, unlike a life annuity, a living annuity does not offer a guaranteed income for life. Although there is more risk associated with the living annuity, it can be a very good option if you have saved enough throughout your life, partnering with your financial planner and withdrawing a sustainable percentage per year to make sure that you don't run out of capital.

2. LINKED INVESTMENTS

Along with saving enough for your long-term goals like retirement, another part of holistic financial planning is to take care of your short- and medium-term financial goals, such as saving for a wedding, a car or a deposit on a house. People often keep money in a savings account. While it is necessary to have money in a savings account that is instantly accessible for emergencies (preferably the equivalent of three to six months' salary), the growth potential is smaller and the tax consequences may not always be advantageous. Apart from cash in a savings account, a linked investment (e.g. a unit trust investment) should also be considered.

Key features of a linked investment:

- This type of investment is flexible and will help you fund your short- to medium-term goals. It provides better potential growth than a savings account and your money is accessible within a few days.
- Your linked investment can be diversified to mitigate risk.
- It gives the everyday investor an opportunity to have exposure to the world's biggest companies through units.
- Although there is more risk than with money market instruments (including savings accounts), linked investments could provide excellent growth potential.
- There is no limit on the amount or number of withdrawals from the investment.
- Depending on your financial goals, time horizon and risk appetite, you can invest in anything from conservative funds all the way to 100% pure equity funds, as you are not subject to Regulation 28 of the Pension Funds Act.

It is a good choice to start investing money in a linked investment as soon as possible, even if it is only a small amount at first. The longer the money is invested, the better the chances are for higher returns.

3. TAX-FREE INVESTMENTS

Another investment vehicle to consider is a tax-free investment. This product is advantageous in that it is not subject to income tax, dividends tax or capital gains tax.

» Currently, maximum R36 000 may be contributed per tax year, with a lifetime contribution limit of R500 000. This is important to note, as any contributions in excess of these limits will be taxed at 40%.

» It is a flexible investment vehicle as there are no limits on withdrawals. You are allowed to withdraw funds any time you want. However, you cannot replace any withdrawn amounts, as it will constitute an excess contribution as explained above.

» Your contributions will be subject to market movements depending on which funds you have invested in. Therefore, it is important to start saving towards a tax-free investment as soon as possible to allow your contributions to grow over the long term, eventually reaping the benefits of withdrawing the capital plus growth thereon completely free of tax.

It is wise not to view a tax-free investment in the same light as a savings account or linked investment, as it is ideal to contribute towards the R500 000 lifetime limit as quickly as possible (within the annual limits) and leave the capital in the account for as long as possible to maximise the tax-free return on your capital value. Money market instruments, and linked investments to some extent, are more suitable for short-term goals.

IN CLOSING

The importance of saving from a young age cannot be stressed enough. The three types of investment discussed in this article are important to consider in kickstarting your financial planning journey.

Always keep a cool head when it comes to finances, consider the various options carefully and be patient about growing your wealth. Rome wasn't built in a day. Returns on investments take time.

When you and your financial planner have a good understanding of your current financial situation and your financial goals, appropriately utilising the above (as well as other types of investment depending on your goals) will go a long way in ensuring that your financial planning journey is off to a good start!

COMPANY NEWS

By Michelle Matthews | Portfolio Manager | Old Mutual Wealth Private Clients

Media and entertainment giant, Walt Disney reported interim 2024 results, which although in line with prior guidance, did not impress the market, sending the share price down nearly 10% on the day. Over the six-month period, revenue was flat at US$46.5bn, while cost saving and efficiency initiatives drove a 28% increase in adjusted diluted earnings per share. Including a once-off US$2bn goodwill impairment related to the contribution of Star India and entertainment assets to a JV with Reliance in India, diluted EPS fell 26%. Revenue in Disney's Direct to Consumer (DTC) segment continued to grow strongly at 14% however, this growth did not offset sustained declines in the traditional linear networks and content sales and licensing. As a result, overall revenue growth was below 1%. Group profitability, however, was driven by DTC, as both Disney+ and Hulu began to generate profits, with ESPN+ being the only DTC platform to incur an operating loss during the second quarter.

Free cash flow generation recovered strongly, allowing for a US$1bn share buyback during the second quarter and supporting future dividend prospects. While the financial performance was in line with expectations, management's guidance for the third quarter underwhelmed as DTC and Experiences are expected to report modest operating income growth, if any. This is due to the timing of costs, particularly, the launch of a new cruise ship and payment of ICC cricket rights, relative to the comparable period. Despite this, management increased their FY 2024 adjusted EPS growth expectations from 20% to 25%.

Global luxury goods company, Richemont reported a resilient 2024 full year performance with constant currency sales and operating income growth of 8% and 13%, respectively. The group's performance was driven by double-digit growth in sales of jewellery (+12%) and leather goods and accessories (+10%), while specialist watches remained relatively subdued. The group benefitted from a lower impairment to YNAP as well as lower finance costs, which drove a notable recovery in earnings per share. Proceeds of warrants exercised last year added to the group's already substantial net cash position, which supported the Board's proposal of a 10% increase in the group's ordinary dividend to CHF2.75 per share.

As of 1 June 2024, after nearly six years as group Chief Executive Officer, Jerome Lambert will resume his former role as Chief Operating Officer and current Van Cleef and Arpels CEO, Nicolas Bos will assume the Group CEO position.

AWARENESS

Self-care is the cornerstone of wellness

'Self-care' is a term commonly thrown around, but what exactly does it mean, and how – if used effectively – can it serve as the foundation of our holistic wellbeing?

Let's define it

The US National Institute of Mental Health (NIMH) defines self-care as "taking the time to do things that help you live well and improve both your physical and mental health". Moreover, health and wellness platforms Verywell Mind and Everyday Health add that self-care is the "conscious act people take to promote their physical, mental, and emotional health" and the act of caring for oneself so that you're "healthy, well, able to perform your job, help and care for others" and accomplish what you need to do daily.

Everyday Health warns that self-care may be mistaken for self-indulgence or selfishness, but the NIMH recognises that self-care "looks different for everyone, and it's important to find what you need and enjoy."

How to better self-care

The Mayo Clinic reminds us - we are "worth special care". Integrate these NIMH-recommended self-care practices into your routine:

- **Regular exercise:** even 30-minute daily walks can help boost and improve your mood and health.
- **Hydrate and eat regular, healthy meals** to improve your daily energy and focus.
- **Prioritise sleep** and keep a schedule to ensure you get sufficient sleep.
- **Find relaxing activities;** relaxation and wellness programs or apps like **LiveWell** can help you incorporate meditation and breathing exercises into your routine.
- **Set goals and priorities;** decide what tasks need to get done and which can wait.
- **Practice gratitude daily.**
- **Focus on positivity;** identify and challenge your negative and obstructive thoughts.
- **Stay connected** to loved ones and reach out for support.

To honour International Self-Care Day (July 24), how have you incorporated these activities to promote your wellbeing?

For more self-care advice, use your LiveWell mobile app for effective health and wellbeing tips and ways to track your daily exercise and sleep goals.

LiveWell By ZURICH

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