

An abstract graphic on the right side of the page consisting of a network of glowing blue lines and dots, resembling a molecular structure or a data network, set against a dark blue background with light particles.

PRINCIPLES FOR
DISCIPLINED INVESTING

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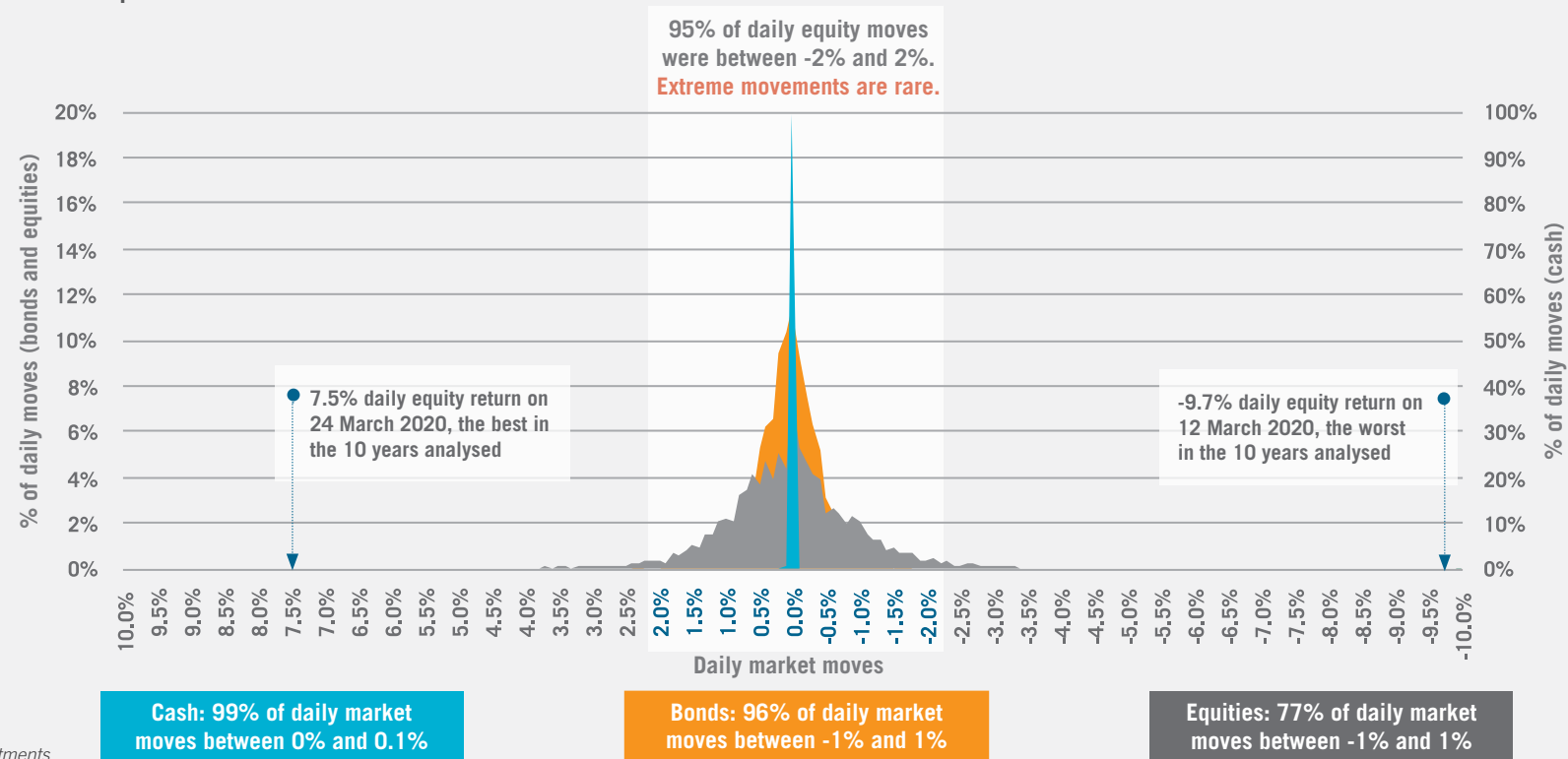
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1 VOLATILITY IS ALWAYS PRESENT, SELDOMLY EXTREME

It's normal for investments to come with some risk and market volatility



Daily market moves from 1 April 2011 to 31 March 2021



Source: Alexander Forbes Investments

Volatility represents the fluctuation of asset prices and the magnitude by which those asset prices could swing. Drastic bouts of market volatility can make even the most experienced investors anxious. The reality is that volatility and investing go hand-in-hand - it's 'normal' for investments to come with some risk and market volatility.

The above chart shows the daily market movements of the FTSE/JSE All Share, All Bond and STeFI Composite indices over the past 10 years. **It reminds us that although volatility is a daily occurrence, a different perspective of its fluctuations shows a relatively tranquil scene.**

The biggest price swings are a seldom occurrence that should not exaggerate the risk and uncertainty pinned on the anticipated long-term value of an investment – an insight that may be forgotten during intermittent bouts of extreme volatility in the market. The roller coaster ride that comes with investing will have its ups and downs. Putting market volatility into perspective will determine whether you panic during the ride or stop your emotions from winning over reason.

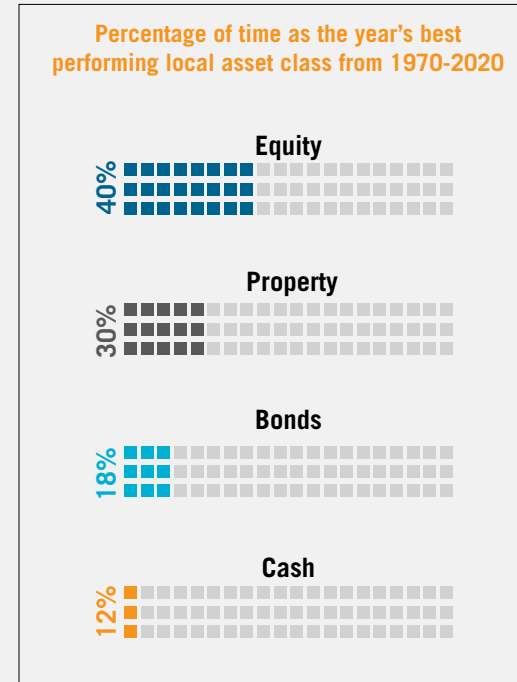
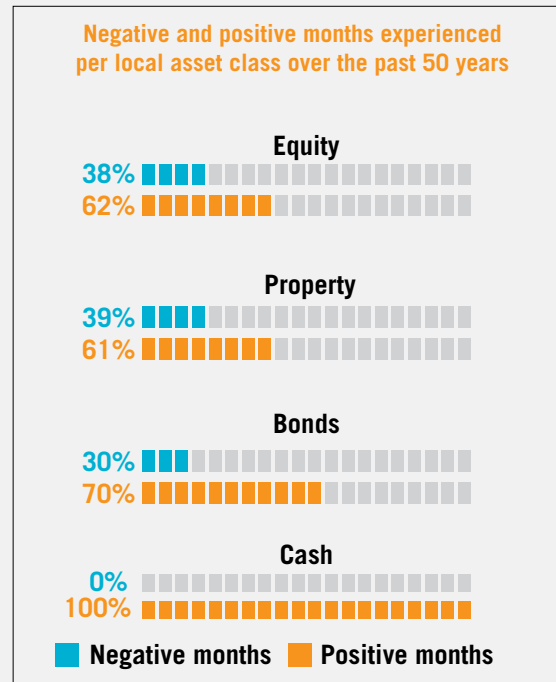
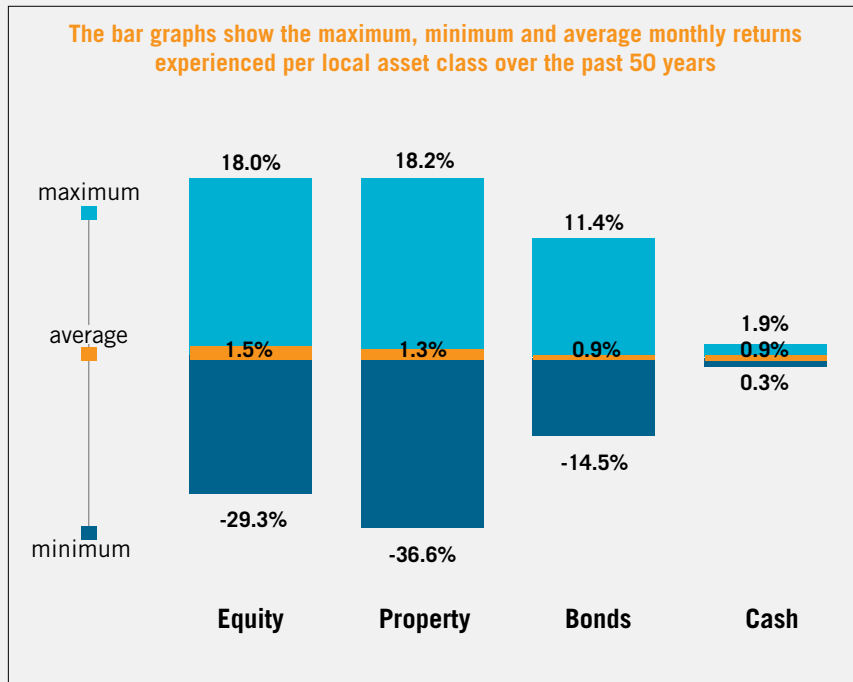
The market as a whole is probably best described by Benjamin Graham in his book *The Intelligent Investor*. Benjamin explains: "One needs to see the market as a grumpy, depressed or moody person. His behaviour can be wild and irrational. One day he is joyful and puts a high value on his businesses. During this time, he will only sell you a piece of the business at a very high price. At other times, he is grumpy and depressed and not very fond of his businesses, and is willing to sell you a piece at a cheap price. And other times he might just be stable and neutral. The problem is that one never knows in what mood he will be in. Regardless of this, Mr Market will be there the next day with a new range of prices for his businesses."

This demonstrates that the market can be 'emotional' – and this is why you shouldn't be. Trying to keep up with the emotions of the market will leave you coming off second best. Instead, remembering that volatility is always present but seldom extreme can help crowd out value-destroying investment behaviour and strengthen a commitment to your investment goals.



2 WITH GREAT RISK COMES GREAT EXPECTED RETURNS

Inflation-beating returns require the right balance over the long term



Source: Alexander Forbes Investments

A commonly used adage in investing is that the greater the risk, the greater the expected return – the key to unlocking better risk-adjusted returns is to strike the right balance between the two.

An important aspect to this is that all asset classes behave differently. This is because each asset class has a different risk-return profile. These risks are associated with liquidity (cash), regular fixed payments (bonds), and company ownership (equities). **While investors follow their natural instinct to avoid risk during times of heightened market volatility, they often avoid or reduce their exposure to growth assets such as equities. Our natural instincts, however, can sometimes let us down.**

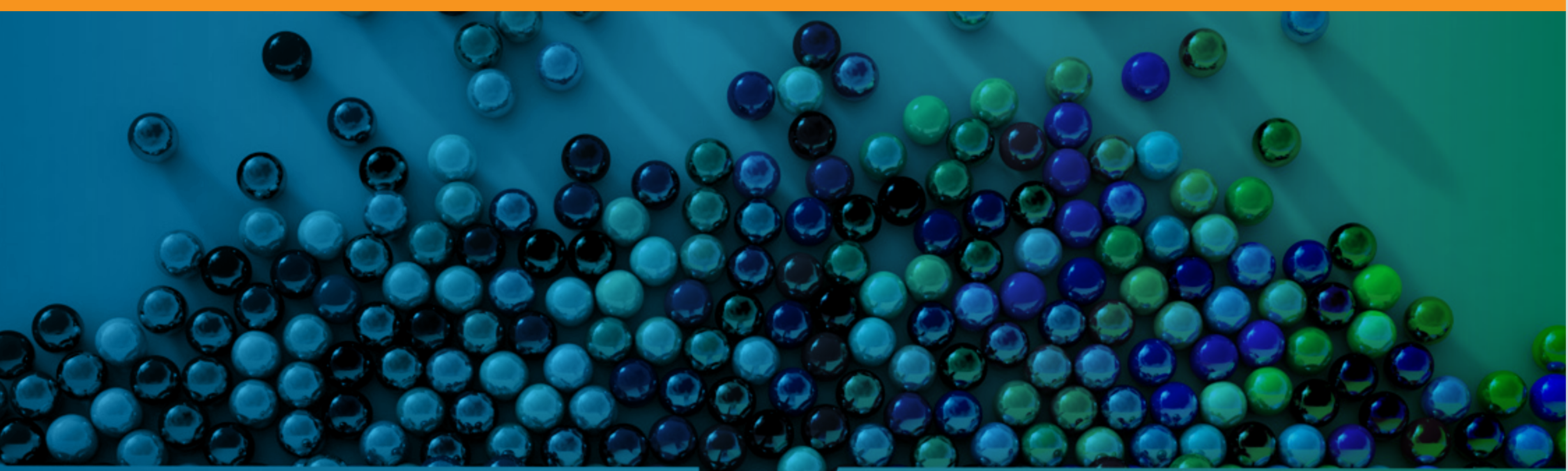
The charts above reveal some interesting insights on our local financial markets over the past 50 years ending 31 March 2021.

Although the wide range of returns experienced by growth assets can be unsettling at first sight, these assets have delivered the most impressive performance relative to bonds and cash over the past 50-year period. In fact, not only did growth assets deliver better average monthly

returns relative to the other asset classes over this period, they shared the highest percentage as best performing asset classes, even though they experienced the most negative months. Minimising the turbulence that comes with investing, solely in equities, can be achieved by spreading investment risk across various asset classes.

This is known as **diversification**.

Investors should be reminded of the important distinction between the management of assets and the saving of assets. The objective of achieving inflation-beating returns over the long term has to be balanced with a complementary mix of growth and defensive assets. This will help structure a diversified investment strategy that aims to grow and protect savings, converting it into wealth over the medium-to-longer term.

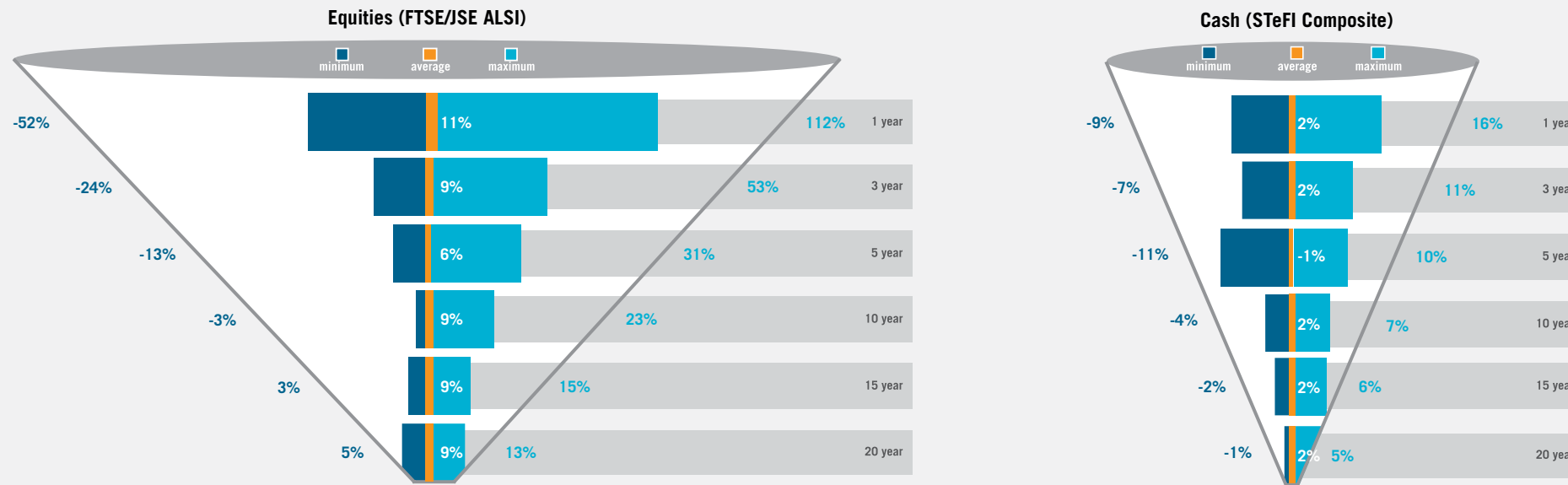


3 THE FUNNEL OF DOUBT

The range of return outcomes reduces significantly over time

Funnel of doubt – equities vs cash

Real investment returns from local shares and local cash over the past 60 years.



Although the ‘funnel of doubt’ narrows the longer you invest, local cash returns haven’t beaten inflation as much as when you invested in local shares.

Source: Alexander Forbes Investments

The funnel of doubt shows a range of return outcomes associated with a particular investment type or asset class over time.

Characteristically, asset classes display a wider range of return outcomes in the short term, which then reduces significantly over longer investment periods.

The funnel of doubt charts shown above illustrate the range of return outcomes experienced in local equity and money markets over the past 60 years. The relatively stable returns of defensive assets, such as cash, may seem to be the safe and attractive option to investors. It may be natural for investors to think that they are getting the best possible outcome by investing in defensive investments –, these investments exhibit a narrow range of potential return outcomes. However, the extent to which these assets can grow your savings may not be enough to achieve your long-term investment goals.

Investments into growth assets, such as equities, can exhibit a wider dispersion of potential return outcomes over time (such as a wider funnel of return outcomes). This may be unnerving for investors, but these assets are more likely to produce the higher inflation-beating returns that investors require to grow their wealth and meet their long-term investment objectives.

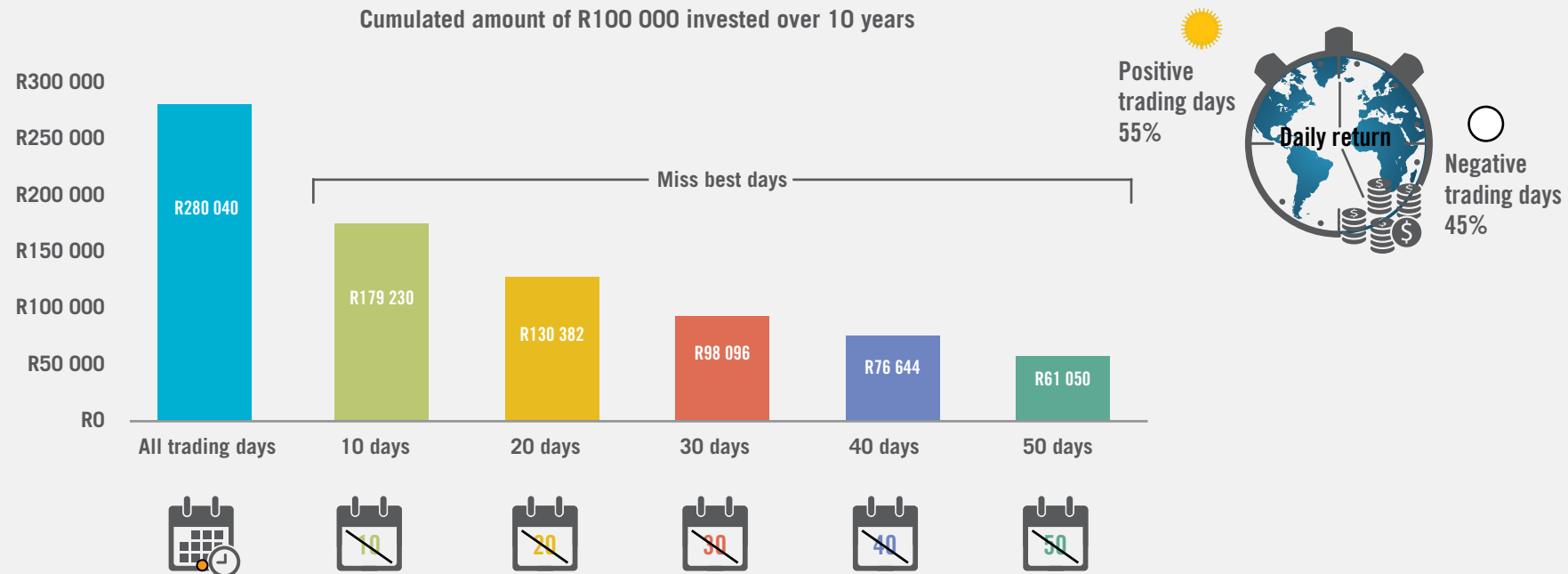
The funnels of doubt show the highest, average and lowest real returns over rolling 1-, 3-, 5-, 10-, 15- and 20-year periods experienced in the past 60 years. They illustrate that in the past 60 years, as the time horizon increases (i.e. from 1 to 20 years), the range of returns experienced decreases hence reflecting a funnel of doubt that appears wider at the top and narrow at the bottom.

The funnel of doubt serves as an important reminder for investors that investing is not always a question of ‘either-or’ but rather ‘both-and’, in the sense that investing should be viewed as taking complementary approaches that can help investors preserve capital as well as the purchasing power of their capital over time.

4 SOMETIMES DOING NOTHING IS DOING SOMETHING

Time in the market or timing the market?





Source: Alexander Forbes Investments

Thomas Robert Dewar, a Scottish whisky distiller from the 1800s, coined the phrase ‘sometimes doing nothing is doing something’. While Mr Dewar was referring to the whisky ageing process where the unique flavour is developed, the phrase also applies to investments.

Investors’ emotions see-saw when markets go down. Their emotions could drive impulsive investment decisions that ultimately, like the event that sparked them, end in undesirable outcomes. When markets crash, feelings of doubt and uncertainty intensify, and investors scramble to protect their hard-earned savings. This is when you see investors rushing to cash in their investments or to change their investment strategies – cash being the preferred destination. But what if their actions are mis-timed, or market conditions improve and investors unintentionally miss one, two or ten of the best days in the market? What impact would this have on their investment over time? Historically, we’ve seen the markets recover significantly following drastic downturns. They often go on to post inflation-beating performance returns.

The chart above is based on the South African stock market, represented by the FTSE/JSE All Share Index from 1 April 2011 to 31 March 2021. It shows the impact on investments when investors try to time the market and, in the process, miss some of the market’s best performing days.

Scenario 1: If an investor missed the 10 best trading days in the market out of the 10 years analysed, R100 000 invested on the starting date would be worth R179 230.

Scenario 2: An investor who kept their money invested for the entire 10-year period would have seen the original investment of R100 000 grow to R280 040.

The investor who did not attempt to time the market would have almost double the amount of money than the investor who missed the 10 best trading days by trying to time the market.

Even more extraordinary is that if an investor had missed the 30 best days in the market, the investment would only be worth R98 096 – less than the amount of R100 000 invested 10 years ago. Despite there being no consistent means of predicting what markets will do, many investors still attempt to time the market in an attempt to either avoid market downturns or capture the gains of market rallies.

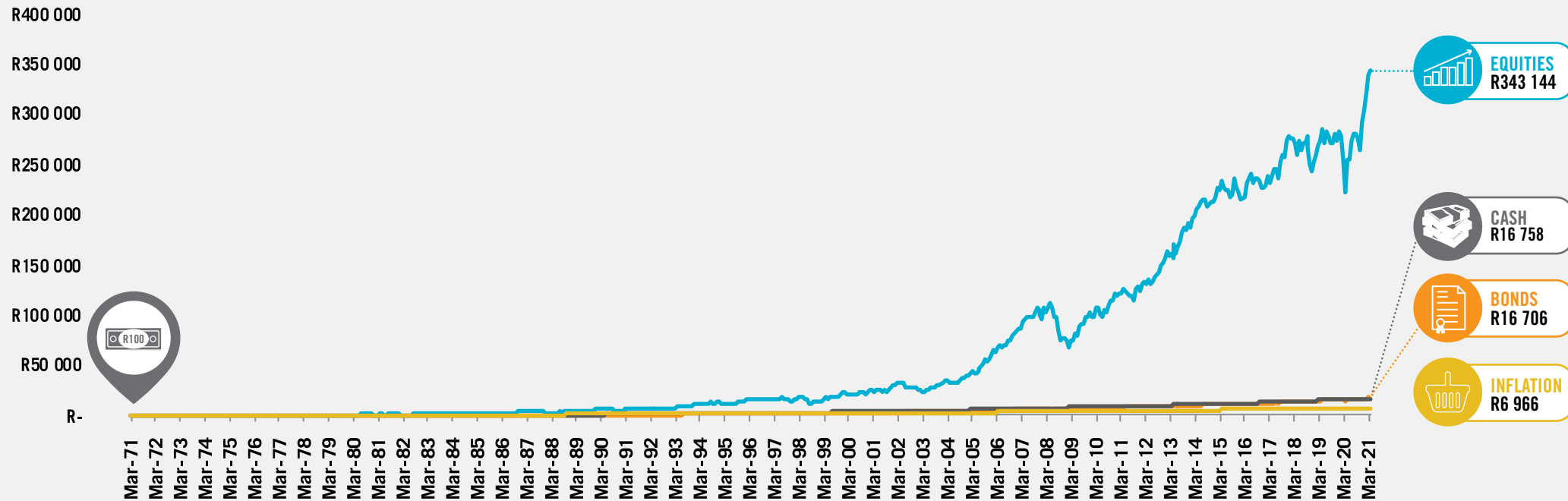
In reality, attempting to time the markets is very much the same as Mr Dewar’s philosophy for making whisky. Changing an investment strategy that is designed with the long term in mind because of perceived short-term risks or gains often ends in missed opportunities or even losses. If you stick to your long-term investment plan and do nothing when others are prematurely opening the proverbial cask of whisky, your retirement years could very well be spent savouring a perfectly matured single malt.

5 EQUITIES ARE THE PLACE TO BE

Especially if time is on your side



If you invested R100 in the different asset classes 50 years ago



Source: Alexander Forbes Investments

Growing your wealth doesn't come from stashing cash in cupboards, under mattresses or under the foot of a tree. Although this might seem like a good idea during times of market volatility and unfavourable returns, it can destroy your investment's value.

It's impossible to have your entire portfolio performing optimally at all times. We know that different asset classes behave differently over time and during different market cycles. **You need your money to work hard for you.** Growth assets like equities have consistently shown to achieve an investment return (including capital growth and income) that outperforms inflation.

Outperforming inflation is key to investment success. It means that your savings and investments stay ahead of inflation, minimising its ability to eat away at the purchasing power of your hard-earned rands and cents.

The chart above shows the value of R100 invested over 50 years in various asset classes. Defensive assets like cash and bonds aim to achieve more stable returns relative to growth assets. However, these asset classes offer very little protection against the rand-erosion qualities of inflation. The desire to achieve inflation-beating returns over the long term must be balanced with a diversification strategy that has a complementary mix of growth and defensive assets. Growth assets aim to stay clear of inflation as best they can, but this typically means that investors should expect volatility and a wider dispersion of returns when investing in these assets. This is the short-term cost investors pay for long-term inflation-beating returns.

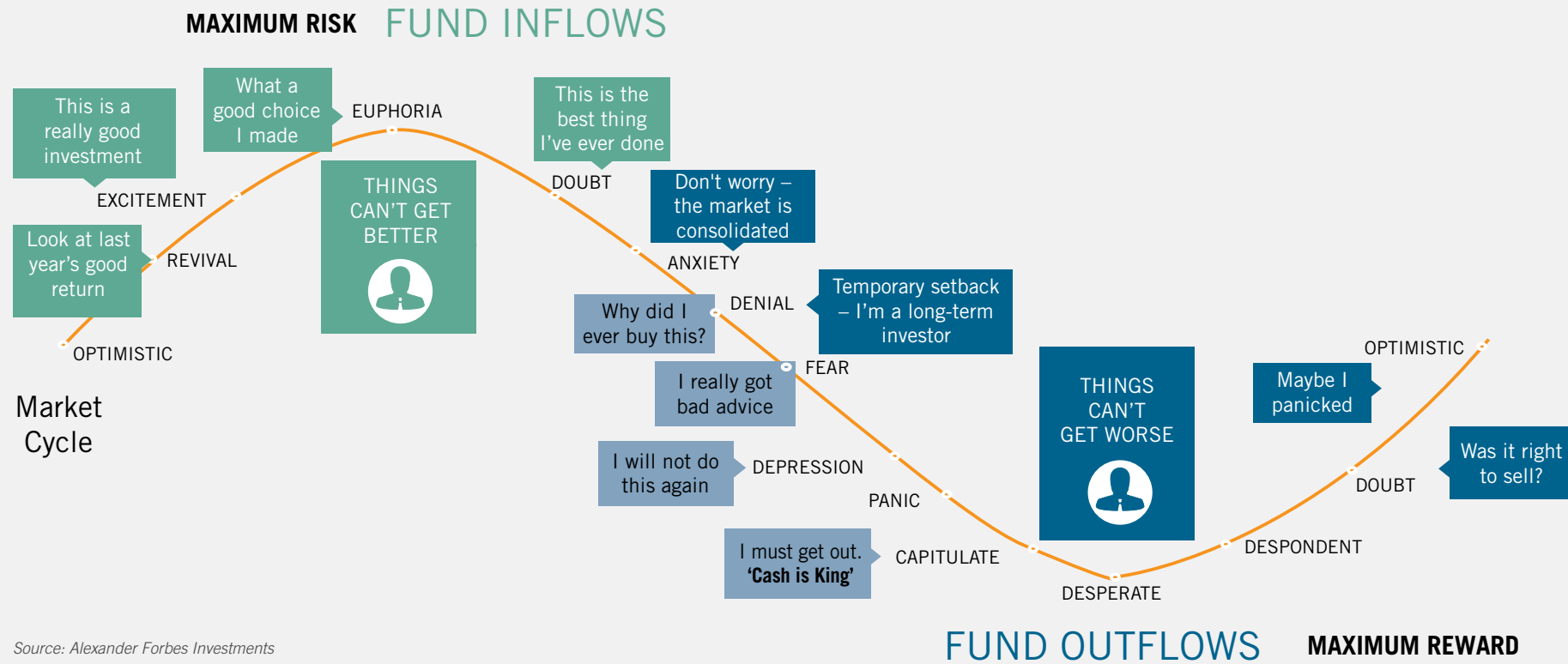
Investors should be reminded of the important distinction between the management of assets and the saving of assets. It's important to structure a holistic and diversified investment strategy that aims to grow and protect your savings while converting them into wealth over the medium-to-longer term.

6

THE UPS AND DOWNS, TWISTS AND TURNS

Investing can be a roller coaster of emotions





Source: Alexander Forbes Investments

You've probably heard your adviser, consultant or even financially savvy friends say that returns don't come in a straight line. The market will have good days and will have bad days. Investors anticipate bumpy rides along their investment journey, but they don't always understand just how bumpy it can get from time to time.

Investing can send you on a roller coaster ride of emotions that may lead to poor investment decisions. The bottom line is that markets go through cycles – sometimes they're up, and sometimes they're down.

It's during these cycles of the investment journey that you experience fear and greed, two of the main drivers of the biggest behavioural mistakes you can make when investing.

Your investment's underperformance can lead you to feel remorse, regret, fear and ultimately panic. **It's during these times that you need to resist the urge to disinvest.** You need to trust that your investment strategy will capitalise on markets because your investment is positioned to deliver when markets turn.

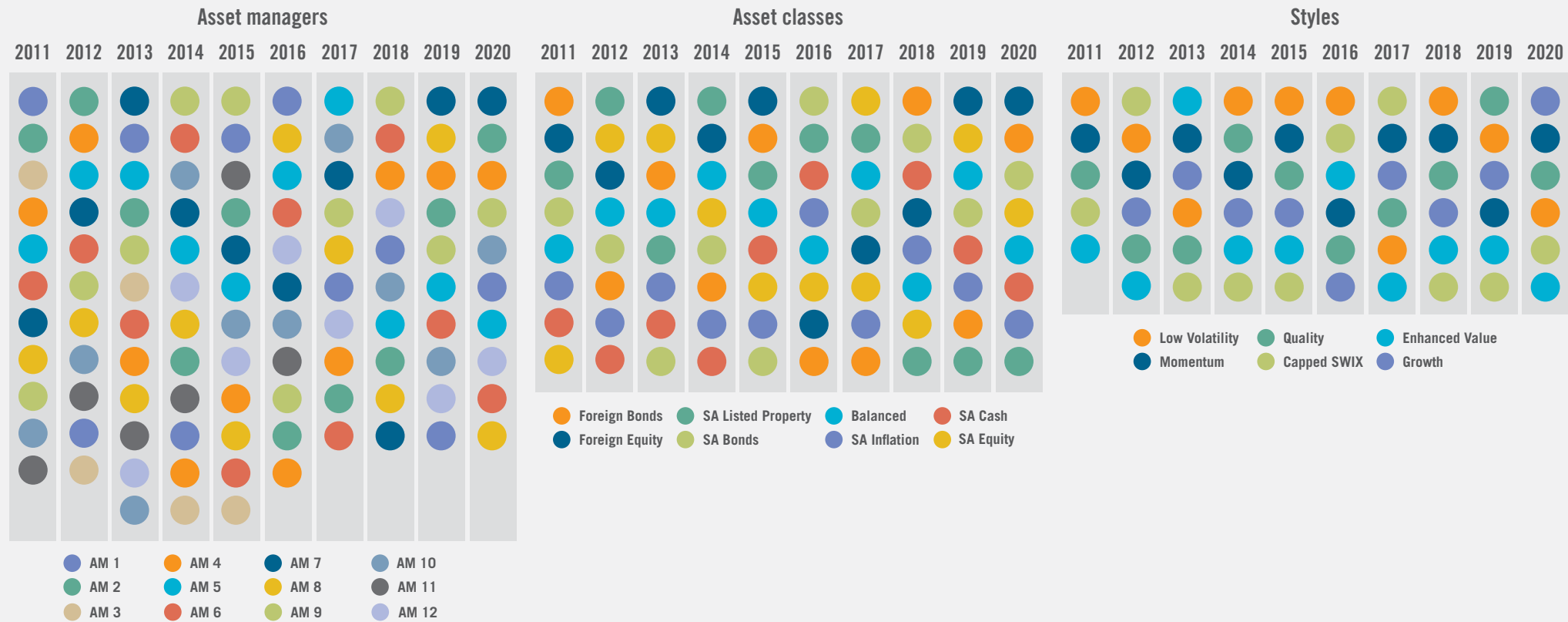
Similarly, if your investment has outperformed for several months and you feel the need to cash in your investment or to invest more money in the same asset class (for example investing more in equities), you will create concentration risk in your portfolio. This may put your investment at risk. Additionally, when you buy top performing asset classes, you pay more. This will erode your investment value further down the line.

When panic sets in, or you feel the urge to invest more in an outperforming asset class, talk to your consultant or financial adviser. They are there to ensure your investment is still on track to meeting your objectives. **Don't panic, don't monitor the markets, and do not focus on short-term performance.** Expert advice on the management of your assets and investment choices at the right time could be the difference between an abandoned or misplaced investment strategy that fails, and one that ultimately rewards.



7 WHAT GOES UP WILL COME DOWN

Basing decisions on past performance causes accidents



Source: Alexander Forbes Investments

Basing investment decisions on past performance is a common mistake many investors make. The search for the best asset manager, asset class or style consumes a lot of time as most investors anxiously compare their investments against how their peers are performing at a particular point in time. After all, no one wants to have a little while their peers have it all. And just as you think you have 'it', the markets change and today's top performers become tomorrow's runners-up.

It's a natural tendency for investors to follow the hot stocks, and the most popular asset classes and asset managers of the moment which ultimately leads them to switching into the next best thing – especially if it is hyped by the media. Investors can lose focus when assets move in and out of their favour during different market cycles.

The tables above show how different asset managers, asset classes and styles perform over time. Different asset managers, asset classes and investment styles enjoy different degrees of success depending on prevailing market conditions.

Despite the numerous warnings on the dangers of investing your money based on past performance, investors are still easily tempted to switch to the next best thing. Choosing the winners and focusing on being part of the best performers of the time, all the time, is a losing battle.

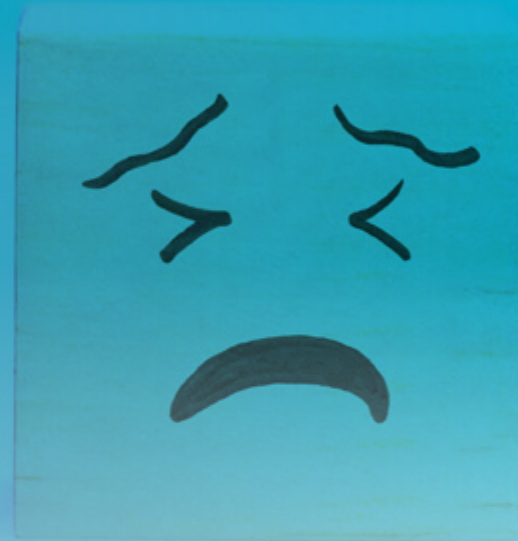
While investing has no guarantees, spreading investments across different opportunity sets means that you can get exposure to different market cycles simultaneously, helping reduce the overall investment risk of your investments and help smooth short-term market volatility. This is because it is unlikely that all investments will move in the same direction, at the same rate and at the same time in response to a specific market event.

Investors should focus on their investment goals. A clear understanding of your investment goals will help determine an appropriate investment plan and blend of investments that is right for your needs and risk profile.

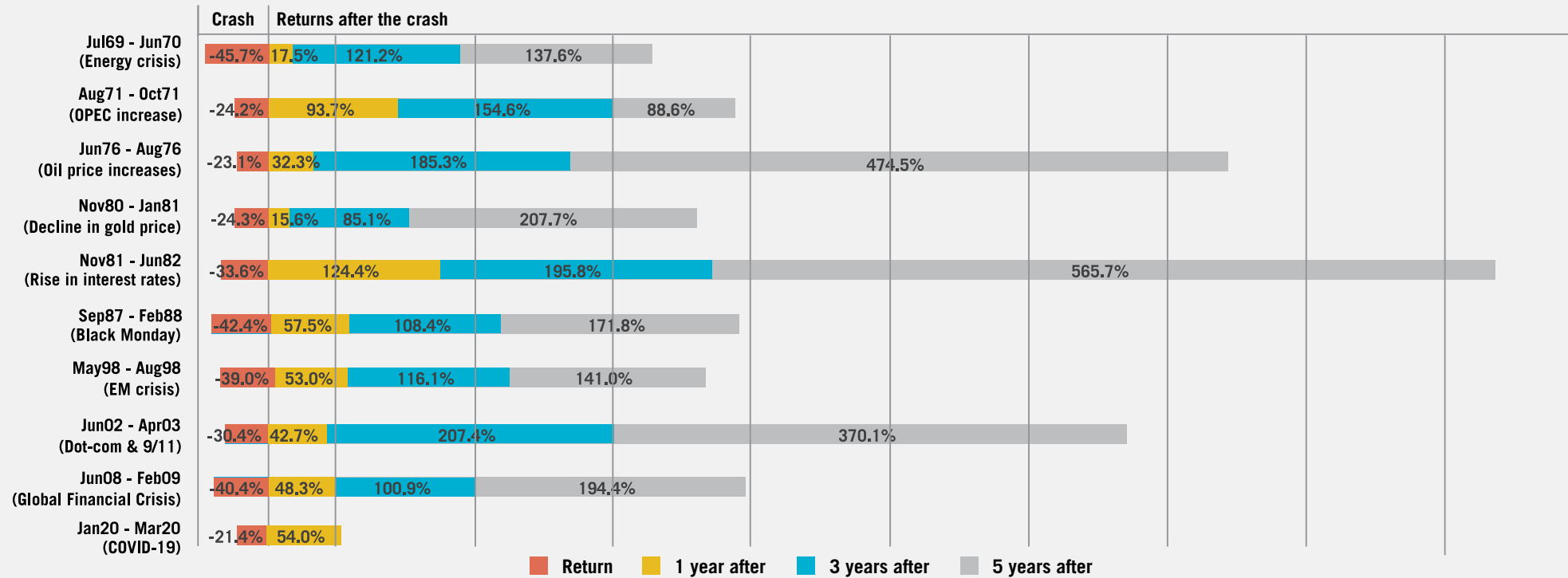


TAKING THE GOOD WITH THE BAD

A history of market recoveries after significant crashes



History of the South African equity market



Source: Alexander Forbes Investments

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You get market fluctuations, and then you get market crashes. When markets crash, feelings of doubt and uncertainty are intensified and the only thing you are certain of is the need to cash out and protect your investment. The fear of loss is felt much stronger than the joy of gain and it can cause investors to lose perspective. Taking out your money during a time when the market is showing signs of extreme uncertainty seems like the rational thing to do – until not being invested in the bad days also means not being invested in the good days.

The chart above shows the negative performance experienced during a market crash in the South African equity market and the subsequent performance gains once the markets had improved. In all of them, bar two, the 1-year return post the crash recovered the losses experienced during the crash.

Based on historical evidence, the best returns are made at the end of a market crash. Even if you sell at the beginning of the crash, you will still experience great losses – losses that you could have recovered if you remained invested for the duration of the crash. Each downturn is an opportunity for an upturn to happen. The more days that are missed during a subsequent downturn, the steeper the investment losses will be.

The markets can be a scary place at times, but long-term investors shouldn't panic. The chart illustrates why remaining invested is not only convenient, but vital. The gains experienced over the long term outweigh the losses experienced in the short term.

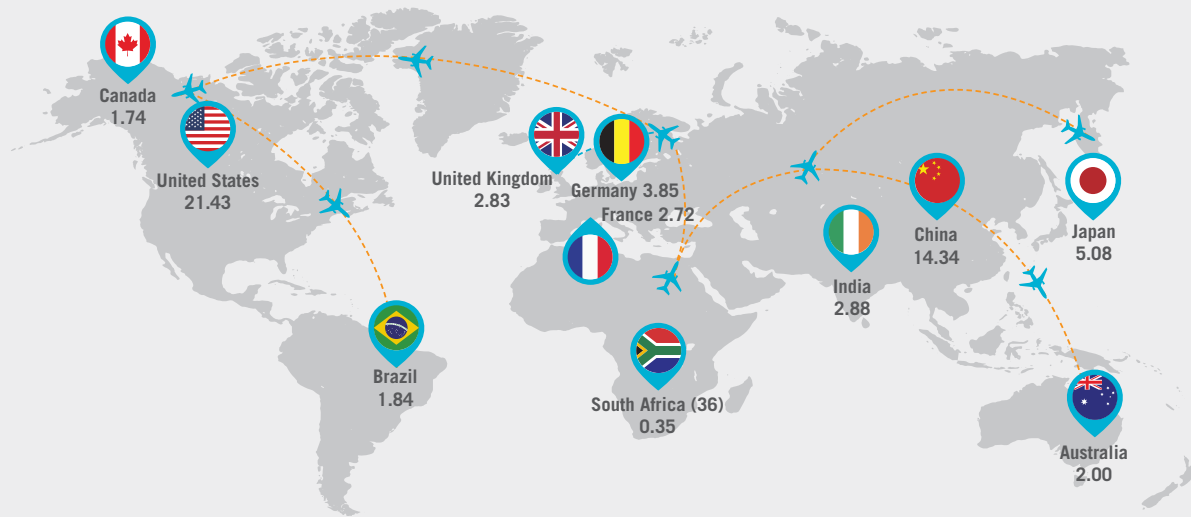
Trying to anticipate the highs and lows of the market is a harmful way of going about your investment journey. **The journey does not need too much of your participation – it just needs your patience.** When market activity makes you panic, speak to your financial adviser or investment consultant to find out how you can stay on track to ultimately achieving your investment outcomes and securing your financial well-being.



9 GO GLOBAL

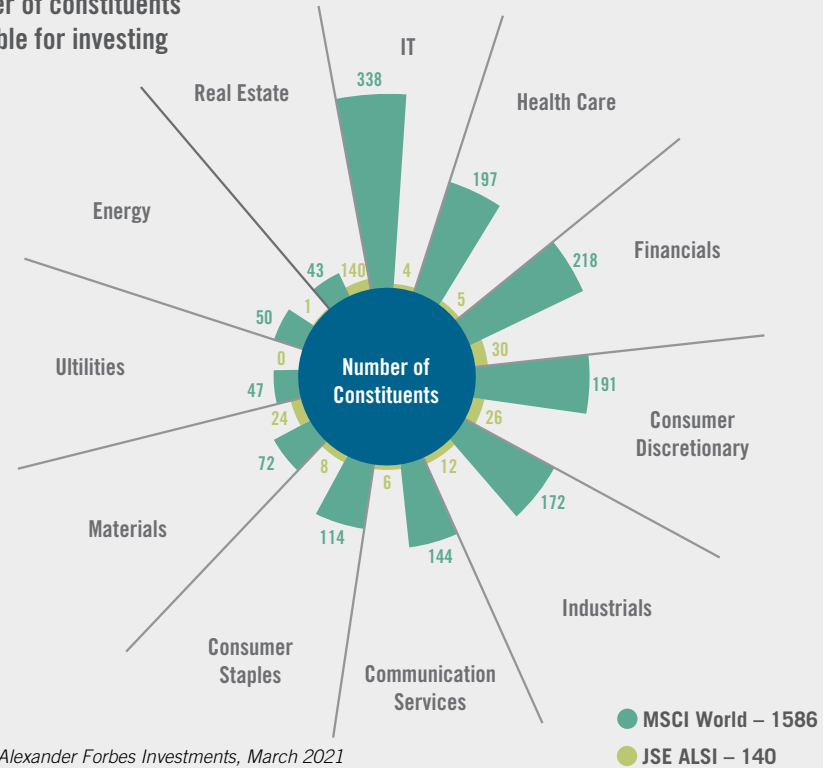
Going beyond borders can be daunting, but it has its benefits

GDP per country (in \$Bn)



Source: World Bank, as at end 2019

Number of constituents available for investing



Source: Alexander Forbes Investments, March 2021

Going beyond borders can be a daunting, but exciting, experience – both for travellers and investors. The charts above illustrate the gross domestic product (GDP) of each country featured and the number of constituents available in the world index as compared to that in South Africa in each sector. It clearly demonstrates the broad and diverse value potential that investors can leverage from, outside of South Africa. This is why investing globally can play a significant role in further diversifying your investment plan, lower your investment risk and possibly contribute to your savings and investment growth.

Capitilising on global markets

There are a number of reasons investors look beyond borders – they could be thinking about risk and return, have currency concerns or want to diversify their investments.

Access

Some sectors (technology and utilities sector) or asset classes are not available, or are underrepresented, in the South African market. Going global not only gives local investors access to broader opportunity sets across countries, markets and asset classes, but also an investment interest in global companies, such as Apple, Google and Microsoft, which are not available in our local equity market.

Reduced risk

South Africa’s local equity market is among the world’s most concentrated. With this in mind, going global could provide the diversification needed to manage or reduce the concentration risk of your investments, overall.

Protection

South Africa’s specific risk and volatility can be a major driver of currency risk and currency-induced inflation. Going global can help investors protect their investments against short-term currency movements that are highly unpredictable.

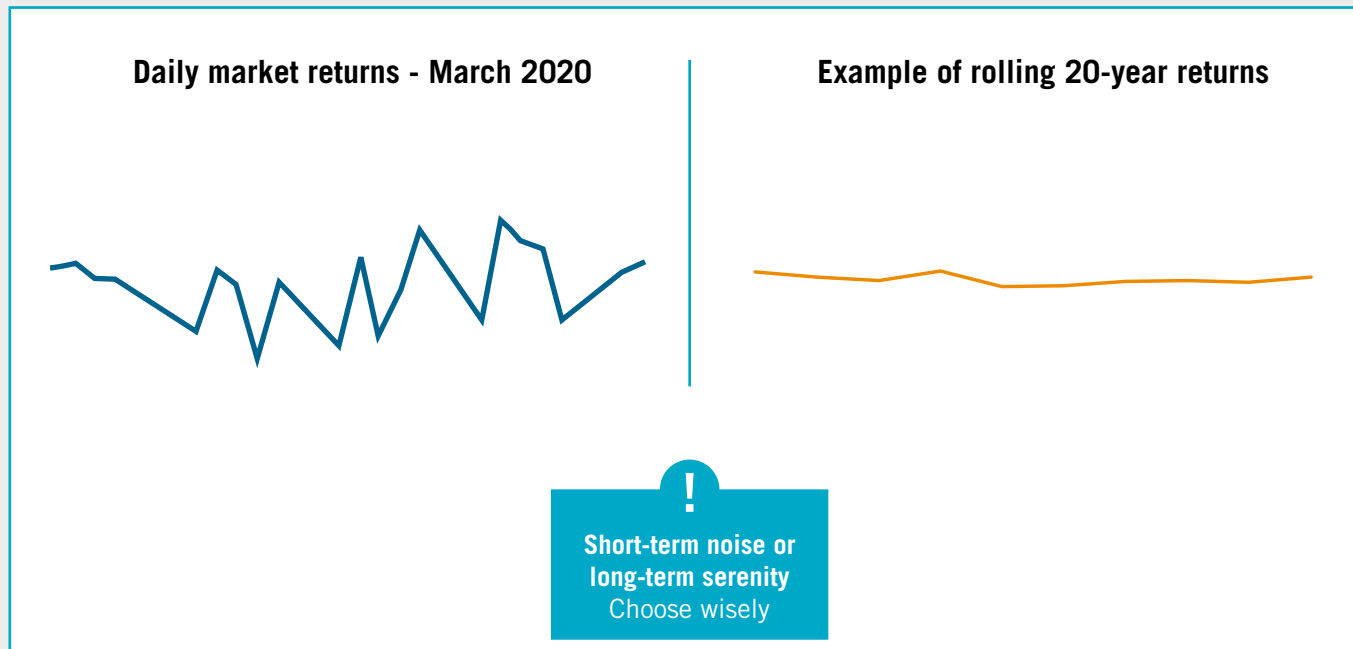
So the question then is not “Should investors have offshore exposure?” but rather “How much offshore exposure is enough?” It’s important that you speak to an accredited financial adviser before you make any investment decisions. You must keep your overall risk objective and risk profile in mind – this will inform how much global exposure is right for your needs and risk appetite.



10

SHORT-TERM NOISE OR LONG-TERM SERENITY?

Choose wisely



Source: Alexander Forbes Investments and Bloomberg

You may recently have heard or seen this quote by Vladimir Lenin on social media: **“There are decades where nothing happens, and there are weeks where decades happen.”**

During weeks where decades happen, markets violently swing up and down, painting a scary picture for investors. These turbulent times can send you on a roller coaster of emotions and may prompt you to make impulsive decisions that may lead to poor investment outcomes. That is because during these ups and downs investors commonly experience fear and greed, two of the main drivers of the biggest behavioural mistakes they will make during their investment journey.

However, if you take a step back and observe markets throughout the decades, you will notice a more serene picture. The short-term ‘noise’ is substantially muted and the investment journey suddenly seems a lot smoother and enjoyable. The bottom line is that markets go through cycles – sometimes they are up and sometimes they are down. Paying too much attention to these ups and downs can cause you sleepless nights.

When panic sets in, or you feel the urge to invest in more of the same thing, talk to your consultant or financial adviser. They are there to protect you from yourself and to ensure the actions you take keep you on track to meeting your short- or long-term objectives. Expert advice on the management of your assets and investment choices could be the difference between an abandoned or misplaced investment strategy, and one that ultimately rewards. Choose wisely.

WE'RE HERE TO HELP

Sometimes asking the experts for help is the best choice. Registered and qualified financial advisers can help you take stock of your personal circumstances, understand your options and make good decisions that give you the best chance of reaching your goals.

Getting professional, personalised advice, at the right time, can:

Help you decide which of your goals to prioritise.

Assist with identifying the solutions or services that can help you achieve these goals.

Improve your chances of financial success throughout your life and in retirement.

The value of getting personalised financial information advice from one of our financial well-being team members should not be underestimated. To see how we can help inform better decisions and improve your well-being success, contact **My Money Matters Centre**:

Financial advice **MY MONEY MATTERS CENTRE**

Telephone: 0860 000 381 | Email: mymoneymatters@forbes.com

Are you a member of a retirement fund administered by Alexander Forbes? Contact us for any queries related to your fund:

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