

## What is the long-term regarding investment?

*The Harvard House team attended an investment conference last week that featured Morgan Housel as a guest speaker. Morgan is a very well-known financial writer and his recent book “Psychology of Money” has sold well over half a million copies worldwide. One of his slides held this quote: “If your expectations grow faster than your income, you will never be happy with your money”. Possibly this could be rewritten that if your expectations grow faster than your portfolio then you will never be happy with your asset manager! We believe our role is always to give context, so what follows will be a few examples either of our own or reworked from others we have seen to contextualise long-term investments.*



**Robin  
Gibson**

We would argue that long-term investing has only one objective and that is to provide investors with the opportunity to be financially independent. What does that mean? Well, some call it retirement, but very simply financial independence is when an individual no longer needs to sell their time or skills in return for money to meet their day-to-day consumption requirements. Two scenarios drive investors’

behaviour around this definition to cause them to act differently. Firstly, greed is normally driven by an early outsized investment success or sight of another individual’s success. Secondly, the investor who started too little too late and now requires a compounding miracle to sustain a level of financial independence (or a perceived right to stop selling their time).

At this point, the investor expects an unreasonable level of return or takes an outsized risk. This is compounded if they are drawing an unreasonable level of income from their investments (even in almost the best of circumstances this is a portfolio killer!). Chart 1 below illustrates the best and worst compound return for the JSE ALSI over selected periods. (The chart does not reflect every possible period, but works off all periods starting from 1 January). Historically the JSE has delivered anything between +90% and -25% across all 1 calendar year periods since 1960. Even over 5-year periods, the worst period demonstrates a very disappointing return of just 5.4%. We are fairly certain that if we were able to chart every 5 years in the last 51 years (not just the ones starting on the 1st January) there would have been several 5-year periods that delivered negative returns. What this chart demonstrates is that the long term is not 3 years, 5 years, or even 10 years, because the worst 10-

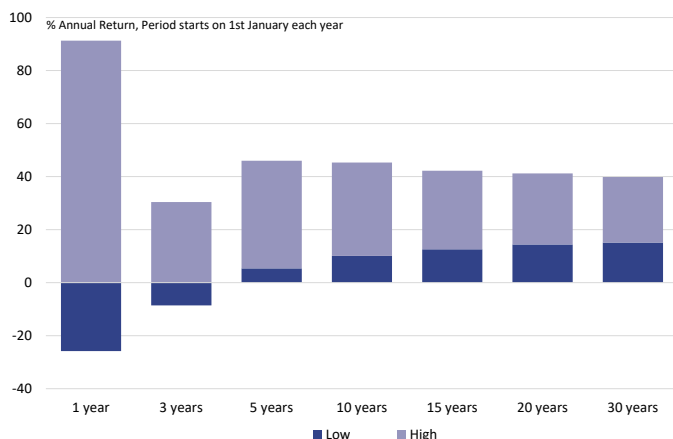
### SPEED READ

- Morgan Housel writes, “If your expectations grow faster than your income, you will never be happy with your money”.
- We live in the data revolution where information is instant and widely available. We also live in the world of convenience where we expect to get what we want almost instantly. Sadly this has made us rather short-term focused on most things and this has spilt over into our investing habits – to our detriment.
- Successful investing (as opposed to greedy speculation or get rich quickly) remains a very long-term exercise that requires living through disappointing periods. Compounding as a concept is very unlikely to be advanced by technological progress.

year period is still disappointing (at just 10.1%). When 15, 20, and 30 year periods are considered then the difference between the worst and the best reduces significantly. Bear in mind that the last 12 years are included in these three ranges and they include the GFC (Global Financial Crisis), the Zuma era, and the continuing Covid 19 crisis (no, it isn’t over).

Consider Warren Buffett as an example. At all times in the last 25 years he has been one of the top 5 wealthiest men in the world. Thousands stream to Omaha in the USA to attend his Berkshire Hathaway annual general meeting to glean titbits of sage advice from Warren and his ace sidekick, Charlie Munger. Buffett and Munger have been joined at the hip for generations, and they both always appear on the stage together and Buffett often implies that Munger is an equal, at least on investment nous. This is

## JSE ALSI WORST & BEST RETURNS



*Equity returns vary widely when measured from year to year, but the range reduces significantly as the time frame grows longer.*

supported by the returns on Munger's hedge fund between 1962 and 1975. Yet the two men's net worth could not be further apart. Buffett is worth north of \$80 billion (even after giving away more than \$20 billion!) yet Munger is not quite worth \$2 billion.

There is a simple reason – Munger has eight (one passed away aged 9 leaving only 7 to reach adulthood) children and Buffett only had three. Children have to be the most expensive investment known to man (although the return is beyond monetary, don't get me wrong). However, more than that Buffett started investing when he was just 11 years old while Munger only started his law practice at age 38 (Warren was aged 32 at that point) and at the same time start to invest money rather successfully. Buffett and Munger started working together in the early '60s. Buffett was already an active investor of more than 20 years, Munger only about 5. Munger's record is as impressive as Buffett's so it's not about return, it's about time. At 65 (1995) Buffett was worth about \$17 billion. By 2020 this had ballooned to over \$100 billion. The foundations for this though were built in his understanding of compound interest back in 1941 aged 11 years.

You see, just like we demonstrated in my article dated August 13th, 2021, you don't have to have the best return to reach your goals, what is much more important is to compound in the markets over time. Sadly we have become very short term in our thinking, American companies report every quarter, newspapers publish monthly comparative performance yet all the most successful and meaningful things are built over generations of sustained input during every season— careers, businesses, families, wealth.

Let's do a fun, frivolous exercise to demonstrate this time difference's effect. Berkshire Hathaway has grown by 18.3% per annum from 1965 to 2021. So let's take Charlie Munger's \$2 billion back to 1965. What would you have needed to invest in 1965 to get to \$2 billion today? The answer is \$76,555. Charlie Munger would have been 41 years old. Now let's take that value and adjust it back by inflation to when Munger was 11, in 1935. US inflation between 1935 and 1965 was 2.8% per annum. So at 11, Munger's \$76,555 would have been equivalent to \$33,082. Now let's take that \$33,082 and roll it forward with the S&P 500 return (12.25%) until 1965 and then with Berkshire Hathaway's return (18.3%) until 2021. The result? \$33.5 billion, nearly 17 times greater than his current \$2 billion. Time truly is the great wealth maker in stock markets.

To extend this fun little exercise to the South African context, let's take R1 million in today's money and calculate the equivalent amount of money adjusted for inflation in 1961. From that base, I have assumed that the funds were invested in the JSE All Share Index and show the value of that investment over each ten-year period. The table below reflects the inflation rate and market average return over the decade, the inflation-adjusted equivalent at the start of the decade (based on a starting value of R1 million in 2021), and what the market value today would be if that sum had been invested into the JSE at the start of the decade and left to compound.

JSE LONG TERM RETURNS				
Year	Inflation	Inflation Adjusted (Value of R1 million inflation adjusted)	JSE Return (Over next decade)	2021 Market Value
2021		R1,000,000		
2011	4.91%	R612,627	10.10%	R1,674,935
2001	5.50%	R353,899	16.90%	R5,182,252
1991	8.08%	R158,177	16.80%	R12,283,924
1981	13.50%	R41,316	24.50%	R36,275,823
1971	10.14%	R15,051	26.90%	R188,979,549
1961	2.57%	R11,643	14.30%	R605,737,173

*60 years of compounding creates almost unbelievable numbers. R11,643 invested in 1961 would have grown to R605 million had it just been left to compound, with all income reinvested.*

The takeaway for every investor is that time is your greatest friend in investing. It takes time to build portfolios and over time we reap rewards. You cannot short circuit these principles and to try largely results in calamity and disappointment. This is not to say people will not have periods of success or momentary windfalls - they most certainly will - but history proves these individuals will be few and far between.



Please note, due to the concerns over the 3rd wave of Covid, Harvard House has decided to cancel our Insight presentations until further notice.



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**Topic:** n/a

### Natal Midlands

Date:	TBC
Venue:	Fernhill Hotel Midmar / Tweedie Road Howick
Morning Time:	10am for 10.30am
Evening Time:	5.30pm for 6pm

### Johannesburg

Date:	TBC
Venue:	Rosebank Union Church, Cnr William Nichol and St Andrews Road, Hurlingham
Time:	7am for 7.30am

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Performance figures quoted for the portfolio is from Morningstar, as at the date of this document for a lump sum investment, using NAV-NAV with income reinvested and do not take any upfront manager's charge into account. Income distributions are declared on the ex-dividend date. Actual investment performance will differ based on the initial fees charge applicable, the actual investment date, the date of reinvestment and dividend withholding tax. Performance fees do not apply to any funds managed by Harvard House. The manager does not provide any guarantee either with respect to the capital or return of the portfolio. A schedule of fees, charges, and maximum commissions are available on request from the manager.

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