INTUITION
25 NOVEMBER 2022

Is your hindsight faulty?

I am a highly qualified armchair critic. I can spot every rugby referee's simplest of blunders. My son constantly reminds me that the referee cannot hear me when I shout at him to correct an error. Then there is the occasional instance where my bellowing is interrupted by a commentator or referee demonstrating a better understanding of the laws than me. I choose not to wave those errors around too wildly. If we are all honest, everyone makes them. The quick judgment based on perception or feeling with little empirical evidence or research to back it up. The Harvard House philosophy, in seeking growing income streams from equity and property, will expose clients to greater volatility in choppy markets. This easily leads people to believe that they would have been better off elsewhere, but does the science support that feeling?

Robin Gibson

I remember my early years at Harvard House - the world was in turmoil. The Asian Crisis crashed currencies in the East, Standard Bank had to write off a big loan in Russia when the Rouble collapsed and for the next 6 years, the stock market went nowhere. It felt a little like today. Hope was a scarce commodity!

I still wonder where clients who opted to abandon a growth-oriented, dividend-focused portfolio in favour of a steady, smoothed alternative would be had they exercised some patience. Lost opportunity is very hard to measure. "What-if" scenarios belong to the realm of spreadsheets.

I couldn't help but think of those clients when sitting in front of another one recently. These clients have been invested with us since late 2007, their portfolio funded from the proceeds of a Liberty Investment and Investec unit trusts. They outlined their concerns, the large swings in the monthly market value on their statement (up R90,000 one month, down R115,000 the next – I know your swing is bigger!). The initial investment was just shy of R250,000 and currently oscillates around the R780,000 level.

The client was suggesting that a cash move was a better idea as retirement is now their reality. They even suggested that they would have been better off in cash. We started to delve into the history of the portfolio.
Between October 2007 and January 2009 the portfolio did very little, ending that month with a value of R254,059.

SPEED READ

- **We have had 3 crises in 5 years. The culmination of State Capture with those ethics unfolding in a few listed companies, the Covid Pandemic, and finally the acceleration of global inflation exacerbated by the Russian-Ukraine conflict.**
- **When comparing all 10 and 15-year investment periods on the JSE (full calendar years only), the period ending 31 December 2021 has fallen to among some of the lowest returns in history.**
- **Many an investor will have felt that the volatility endured has not been worth it and a more conservative Balanced Fund (by far the most popular investment fund category in the Unit Trust sector – also known as Multi-Asset High Equity Fund) or a cash investment would have been a better bet.**
- **A recent review with a longstanding client who was in this mental space took an interesting turn as we examined the portfolio relative to the alternatives.**

Then came the February 2009 Global Financial Crisis crash. At the end of February, the portfolio was a dismal R160,996. It finished 2009 at a value of R239,452. A simple cash investment would have grown to R304,831! The client couldn't remember this experience at all.

We continued to explore the idea that cash would have been a better bet. Using historic 1-year fixed deposit rates as a proxy for cash, we examined how such an investment would have grown by the end of October 2022. The data is reflected in the chart below. Quite clearly, despite two market crashes, their equity portfolio has delivered a substantially better outcome than cash over the medium term.

Fixed Deposit vs Inflation				
Year	Fixed Deposit Rate	End value	Inflation	Inflation-Adjusted Value
*2007	10.2%	R254,250	9.0%	R253,750
2008	10.4%	R280,692	9.5%	R277,856
2009	8.6%	R304,832	6.0%	R294,528
2010	7.0%	R326,170	3.6%	R305,131
2011	6.7%	R348,023	6.4%	R324,659
2012	5.7%	R367,791	5.7%	R343,165
2013	4.9%	R385,702	5.8%	R363,068
2014	5.4%	R406,530	5.1%	R381,585
2015	5.6%	R429,296	8.0%	R412,073
2016	7.4%	R461,064	6.9%	R440,424
2017	7.2%	R494,260	4.7%	R461,124
2018	7.6%	R531,824	4.5%	R481,874
2019	7.3%	R570,647	4.0%	R501,149
2020	5.4%	R601,462	3.1%	R516,685
2021	3.8%	R624,318	5.9%	R547,169
*2022	8.0%	R665,939	***11.8%	**R579,934
*Not full years.				
** StatsSA Figures (October estimated)				
*** Full year extrapolated				

This table demonstrates the historic trajectory of the same initial R250,000 invested in a one-year fixed deposit as well as adjusted for inflation.

The client then suggested that they had alternative investments that had fared better. Familiar with the approach of the alternative adviser, I questioned whether the perception was a scientifically calculated one or one established by "feel". The client admitted to not having done any empirical calculations of comparison. The perception merely arose because in the client's mind the alternative investment didn't appear to drop as radically as the Harvard House portfolio. We would concede that this is what makes cash investments so attractive to clients – your value never goes down. She also conceded that while Harvard House reported monthly, she only received a quarterly statement from the other adviser so was unlikely to see the interim movements. We would not contest this perception, but we do believe we should compare the outcomes. We have mentioned before that we run a model in the background that tracks South Africa's largest unit trust funds. (Note that these two funds are the biggest unit trusts by assets under management and each individually exceeds the value of the largest money market fund. Therefore, by implication, they are the preferred route for most South African investors). Both of these funds have exceeded the returns generated by the competitor with whom our client was invested. Their 10-year and 15-year history of performance is contained in Fig. 2.

Selected Balanced Fund Returns				
	10 Year Return	Ranking	15 Year Return	Ranking
Fund 1	9.38%	7	9.29%	1
Fund 2	8.87%	14	8.92%	5
Balanced Fund Class (average return & # of funds)	7.68%	75	7.53%	38

This table reflects the returns achieved by South Africa's two biggest unit trusts, which both happen to be balanced funds – which fall into the "Multi-Asset High Equity" category.

Harvard House talks about the cost of investing as one of our three key differentiators. Unit trust performance figures are always quoted net of asset management fees since daily pricing is calculated net of fees. However, what is seldom seen is the impact of the investing platform used by advisers and the adviser fee. Our model takes this into account and in this model example, we have used an adviser and platform fee of 0.5% per annum each, excluding VAT.

The chart below plots the history of the Harvard House portfolio against the equivalent value had this client opted for the balanced unit trust approach. We would make several observations:

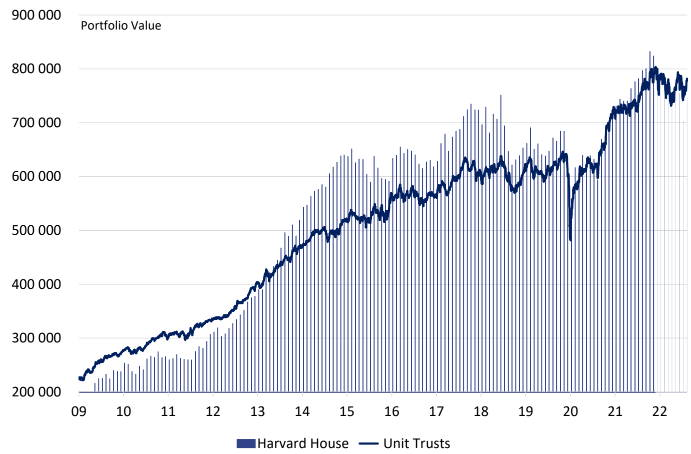
1. Volatility is higher with Harvard House. The range between the highs and lows is pronounced in times of market crisis and more muted with balanced funds.
2. While volatility is lower, it appears the balanced funds do not give as good a protection as may be perceived versus an equity-only portfolio.
3. In a rising market, the Harvard House portfolio significantly outperforms the balanced fund, as much as 10% - 15% better. Given that valuations are at multi-year lows on many shares and the Harvard House share

portfolio is so close to the valuation of the balanced funds, the outlook for the next couple of years for the portfolio is very promising.

4. We have modeled this illustration on two of the best-performing funds in the sector. The picture would look much worse had you had greater exposure to cash, bonds, or even worse-performing funds.
5. Just because your other investments don't appear to be going down as much, or because they invoke less fear, doesn't mean they are doing better or are best positioned for the future. This client's wealth has not been compromised despite how they feel. In fact, maybe they should assess their other portfolios more carefully to ensure that they aren't being lulled into a false sense of security.

In summary, we do understand that our monthly reporting and exposure to growth asset classes (equity and listed property) produces more volatility. However, in the long run, as long as you are not overdrawing your income. you are still likely to have a far better investment outcome than what can be generated from cash or even the best of the more conservative funds available.

LONG-TERM INVESTMENT COMPARISON



This chart plots the Harvard House month-end portfolio values versus the daily portfolio price if the client had been invested via an adviser on a platform into South Africa's two biggest unit trust funds.

Sometimes, it is best to simply go to the beach and not look at one's portfolio.

Topic: **The World in 2023**

The world and financial markets have lurched from one crisis to the next over the past few years.

Will 2023 be any different?

Join us as we look ahead to what the new year may hold.

Natal Midlands	
Date:	24th of November 2022
Venue:	Oasis Conference Centre, 72 Main Road, Howick
Morning Time:	10am for 10.30am
Evening Time:	5.30pm for 6pm

Johannesburg	
Date:	6th of December 2022
Venue:	Rosebank Union Church, Cnr William Nichol and St Andrews Road, Hurlingham
Time:	7am for 7.30am

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For more information on the range of products and services offered by Harvard House Investment Management and its associated companies (including Harvard House, Chartered Accountants), or for any financial advice, please contact the Company at:

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