



The end of the world or the end of an era?

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In summary

René Grobler, Sales Director and Head of Investec Asset Management's Retail division discusses how against a backdrop of low growth, low interest rates and rising inflation, investors are questioning where to find real returns.

- Over the last 10 years most investors earned decent returns just by being in the market, with equities returning 15.2% (ALSI), South African bonds 10.8% (ALBI) and cash 9.2%. Looking ahead, we have had to accept the fact that the outlook for investment returns in 2012 is not as rosy.
- Economists paint a bleak picture of the global economic landscape in 2012. According to a recent survey of 83 economists polled by the Financial Times, the coming year will rival 2009 for economic weakness, as output is hit by the continuing debt crisis in the Eurozone.
- There are a few key investment themes investors should bear in mind when considering their portfolios in the New Year.

Sales Director



René Grobler

The end of the world or the end of an era?

Most of us consider the age-old predictions of the “end of the world” in 2012 to be nothing more than amusing water-cooler banter. However, for many investors it certainly may feel like the end of a golden era of global growth and solid investment returns. Over the last 10 years most investors earned decent returns just by being in the market, with equities returning 15.2% (ALSI), South African bonds 10.8% (ALBI) and cash 9.2%. Looking ahead, we have had to accept the fact that the outlook for investment returns in 2012 is not as rosy.

Economists paint a bleak – if not downright depressing – picture of the global economic landscape in 2012. According to a recent survey of 83 economists polled by the Financial Times, the coming year will rival 2009 for economic weakness, as output is hit by the continuing debt crisis in the Eurozone. Three times more respondents thought the economic outlook would deteriorate than those believing it would improve in 2012.

On the global stage the Eurozone drama continues to unfold, with the probability of a break-up increasing and recession looming. The US economy may surprise on the upside, but the country – in the midst of political paralysis – is still highly exposed to the crisis in Europe and domestic challenges. Emerging economies are expected to continue to support the global economy, contributing up to 80% of growth in 2012. A Chinese hard landing, while unlikely, would certainly exacerbate the situation. Nevertheless, a muted growth outlook for the US and Europe would have a knock-on effect on Chinese exports and coupled with concerns regarding a possible credit bubble and increased labour costs, we could see this significant economy losing momentum.

In South Africa, slow developed market growth, a Eurozone recession and a slowdown in China would mean lower global demand for South African exports and could well lead to disappointing growth locally. Inflation remains sticky at around the 6% mark with interest rates expected to remain lower for longer.

Following a decade of double digit returns and against a backdrop of low growth, low interest rates and rising inflation threatening to erode returns, many investors are struggling to adapt and are questioning where to find real returns. There are a few key investment themes investors should bear in mind when considering their portfolios in the New Year.

- Firstly, expect volatility in the markets to continue. Investors would be well served to settle in for the long haul and take a longer-term view on their portfolios since risk asset returns are expected to continue their rollercoaster ride in the

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short term. A meaningful investment horizon of three to five years should be considered when constructing a portfolio.

- Secondly, be prepared to take on more risk to achieve meaningful real returns. The heydays of sitting in a risk free asset class such as cash and earning good returns are a thing of the past. Even traditional assets expected to provide “risk free returns” such as government bonds (particularly in the Eurozone) have recently earned the reputation of delivering “return free risk”. After tax and inflation, money market returns are negligible and offshore they have turned negative. Investors have been forced further up the risk curve into other asset classes such as equities in the search for real returns.

Protected equity funds with an absolute return and capital preservation focus provide the opportunity to earn good after tax returns by exposing the investor to other asset classes such as equities while providing downside protection. Investec Asset Management’s Absolute Balanced fund, as an example, is an attractive alternative for risk-averse investors who want to earn cash-beating returns. The fund invests in a mix of South African equities, bonds and money market instruments with a focus on generating positive returns for investors on a consistent basis. It aims to preserve wealth in real terms, regardless of whether markets are rising or falling.

- Markets may well go sideways over the medium term, leaving those who bought market indices with disappointing returns. With anaemic growth conditions, markets could very well be at the same place they are now in two years’ time. Buying the market in these conditions could lead to stagnation, and managers will need to work harder to pick quality assets to deliver good returns. However, the equity markets do offer attractive investment opportunities for those who know where to find them and managers with good track records as stock-pickers and active asset allocators will be in demand. Tiger Brands (one of the top 10 holdings of the Investec Opportunity fund) serves as a good example of a quality company with a strong balance sheet and good dividend yield. The company delivered earnings of 15.9% in 2011 (EBIT) and is currently trading at a discount relative to global peers.
- Lastly, quality counts! In this volatile and uncertain environment, investing in quality businesses with robust business models and strong balance sheets is imperative. Many of the big brands locally and globally are currently trading at attractive levels, have proven track records to weather the storms and many provide significant exposure to the growth in emerging markets. Investec Asset Management’s local flagship Opportunity fund, Cautious Managed fund and the Global Franchise fund (all three managed by Clyde Rossouw) are good examples of funds that invest in quality companies with consistent dividends and earnings growth. Quality investments will provide some level of comfort in volatile times; investors can find further peace of mind by entrusting their hard earned savings to quality investment managers with proven track records.

Important information

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