MANAGEMENT

HOW TO ACE YOUR **FIRST 100 DAYS**

RETIREMENT ANNUITIES

A **TAX-SMART TIP** FROM PSG'S SCHALK LOUW

SHARE VIEWS ON:

VODACOM
TRENCOR
PPC

ENGLISH EDITION

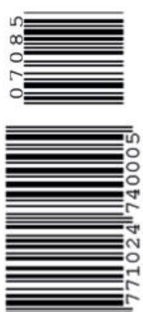
finweek

FIND US AT: fin24.com/finweek

16 February 2017

PLAYING DIRTY WITH CLEAN ENERGY

HOW GOVERNMENT IS PUTTING JOBS AND INVESTMENT AT RISK



DON'T LET **BIG DATA** BAFFLE YOU

CELL C

THE POWER IS IN YOUR HANDS

MORE PEOPLE SWITCH TO CELL C THAN ANY OTHER NETWORK

1. **We have the best customer service of any mobile network in SA.**
   Hellopeter.com Index (hpi).

2. **Our fight to reduce call rates has saved South Africans R47 billion.**
   Centre for Competition, Regulation and Economic Development (CCRED) at the University of Johannesburg via competition.org.za 12 July, 2016.

3. **We exclusively offer Wi-Fi Calling* to broaden local in-building connectivity and reduce international roaming costs.**

4. **Cell C was the first mobile operator in South Africa to offer customers free Facebook and basic Internet services through Facebook's Free Basics.**

5. **We're connecting homes to our lightning-fast C-Fibre* network.**

Visit cellc.co.za/coverage for more information.

*LTE-Advanced, Wi-Fi Calling and C-Fibre are subject to coverage availability determined by area.

Terms and Conditions apply.

10006894

from the editor

JANA MARAIS

How should one invest in the age of Trump? US hedge fund manager Seth A. Klarman's views on this issue have set Wall Street abuzz after *The New York Times* published extracts of his January letter to investors. In the letter, Klarman warned about the "perilously high valuations" of the equity market, saying investors were discounting the major risks brought by US President Donald Trump's proposed policies.

Klarman runs Baupost Group, a hedge fund based in Boston, which manages about $30bn. He is highly regarded in the investment world and has an impressive track record: he's lost money in only three of the past 34 years, according to *The New York Times.* At the moment, about 30% of his fund's money sits in cash, it reported.

Looking at equity markets around the world, Klarman's view seems to be a dissenting one – global equity markets continued to rally in January on the expectation that Trump's policies will bring about faster economic growth, lower taxes and deregulation in the US. The JSE, for example, returned 4.3% in January – more than in the entire 2016 – mainly thanks to strong resource and industrial stocks. The MSCI All Countries World Index returned 2.7% in US dollar-terms in January, following a 2% gain in December.

Klarman, however, believes Trump is very bad news for investors, who have been "mostly ignoring the risks from America-first protectionism and the erection of new trade barriers", he said, also cautioning against Trump's proposed tax cuts. "The big picture for investors is this: Trump is high volatility, and investors generally abhor volatility and shun uncertainty. Not only is Trump shockingly unpredictable, he's apparently deliberately so; he says it's part of his plan," Klarman wrote.

Old Mutual Multi-Managers' Dave Mohr and Izak Odendaal echoed similar sentiments in a recent investment note, saying while the outlook for the US economy remains positive, policy uncertainty is high. "The modern era has never before experienced such unpredictability from the Oval Office," they said.

If things go wrong, Klarman believes it could spell the start of the decline of the dollar as the dominant global currency, a rapid rise in interest rates and inflation, and global malaise.

Oxford Economics also warned that 2017 may be a tougher year than people expect, with global spending power expected to grow by 2.2%, the weakest rate in eight years. Consumers in many countries will face higher interest rates and fuel costs and weak wage growth. Their advice? Keep those belts tightened. ■

contents

Opinion

4 Paradiplomacy and paranoia

The week in brief

6 News in numbers
8 Cash for your car

Marketplace

9 **Fund Focus:** Rewarding long-term investors
10 **House View:** Tax-free portfolio, DRDGold
11 **Killer Trade:** Is Trencor headed for calmer waters?
12 **Simon Says:** Kumba Iron Ore, Vodacom, Dawn, Hudaco Industries, PPC
13 **Invest DIY:** The ins and outs of doubling up on shares
14 **Investment:** Best-kept secret: Direct shares in your retirement annuity
15 **Technical Study:** Lonmin is rapidly burning cash
16 **Directors & Dividends:** Dealings and payouts

Collective Insight

17 **Information Overload:** Navigating your way through the noise
18 **Introduction:** Coming to grips with big data
20 **Insurance:** What is the big deal about big data?
22 **Decision-making:** Age of automation
24 **Analysis:** Welcome to the Second Information Age
26 **Facing the Unknown:** Algorithms versus human judgment – whom do we trust?
28 **Active Management:** Information deluge the new normal
31 **Investment Strategies:** Big data in investment finance: A cautionary comment
33 **Conclusion:** Beware the noise

Cover

34 **Energy:** Government plays dirty with renewables

In Depth

38 **Commodities:** Mining on the up

On the money

40 **Spotlight:** Shwe's fashion revolution
42 **Insurance:** Keep those back-to-varsity blues at bay
43 **Technology:** Amazon's e-book policy puts the squeeze on publishers
44 **Management:** How to ace your first 100 days
45 Crossword and quiz
46 Piker

EDITORIAL & SALES

Editor Jana Marais **Deputy Editor** Anneli Groenewald **Journalists and Contributors** Simon Brown, Dan diBartolomeo, Peter Fabricius, Moxima Gama, Lloyd Gedye, Delphine Govender, Natalie Greve, Jana Jacobs, Niel Joubert, Charlie Mathews, David McKay, Neesa Moodley, Leevania Naicker, Daniel Polakow, Jon Pienaar, Bradley Preston, Ainsley To, Tony van Niekerk, Hannes Viljoen, Helena Wasserman **Sub-Editors** Stefanie Muller, Katrien Smit **Office Manager** Thato Marolen **Layout Artists** Beku Mbotoli, Tshebetso Ditabo, Zandri van Zyl **Advertising manager** Paul Goddard paul@fivetwelve.co.za **Sales Executive** Tanya Finch tanya@fivetwelve.co.za **Publisher** Sandra Ladas sandra.ladas@newmediapub.co.za **General Manager** Dev Naidoo **Production** Angela Silver angela.silver@newmediapub.co.za Rae Morrison rae.morrison@newmediapub.co.za

Published on behalf of Media24 by New Media Publishing (PTY) Ltd Johannesburg Office: Ground floor, Media Park, 69 Kingsway Avenue, Auckland Park, 2092
Postal Address: PO Box 784698, Sandton, Johannesburg, 2146 **Tel:** +27 (0)11 713 9601 **Head Office:** New Media House, 19 Bree Street, Cape Town, 8001
Postal Address: PO Box 440, Green Point, Cape Town, 8051 **Tel:** +27 (0)21 417 1111 Fax: +27 (0)21 417 1112 **Email:** newmedia@newmediapub.co.za
Executive Directors **Group Commercial Director:** John Psillos **Managing Director:** Bridget McCarney **Non Executive Director:** Irna van Zyl
Printed by Paarlmedia and Distributed by **On The Dot** Website: **http://www.fin24.com/finweek** Overseas Subscribers: **+27 21 405 1905/7**

ENQUIRIES

SUBSCRIBERS
087-740-1019
subs@finweek.co.za

Fax
0864-575-918

SHOPS
0861-888-989
assistance@onthedot.co.za

Share your thoughts with us on:

@finweek finweek finweekmagazine

FINWEEK SUBSCRIBES TO THE SOUTH AFRICAN PRESS CODE WHICH COMMITS US TO JOURNALISM THAT IS TRUE, ACCURATE, FAIR AND BALANCED. IF YOU THINK WE ARE NOT COMPLYING WITH THE CODE, CONTACT THE PRESS OMBUDSMAN AT 011-484-3612 OR ombudsman@presscouncil.org.za © FINWEEK 2011 ALL RIGHTS RESERVED. TO INQUIRE ABOUT PERMISSION TO REPRODUCE MATERIAL CALL OUR ARCHIVE AT 021-406-3232.

By Peter Fabricius

INTERNATIONAL RELATIONS

Paradiplomacy and paranoia

Leaders of the DA recently met with foreign dignitaries abroad. The ANC's overreaction to these events reveals confusion in government's foreign policy – and considerable insecurity on the part of the ANC.

During the past few weeks, South Africa has witnessed two notable examples of what foreign-policy pundits call "paradiplomacy" – the conduct of foreign relations by entities in a country other than the national government.

First the DA's Tshwane mayor Solly Msimanga visited Taiwan to meet his counterpart in the capital Taipei, and a few weeks later DA party leader Mmusi Maimane travelled to Israel to meet the country's prime minister, Benjamin Netanyahu.

The ANC exploded. Msimanga was accused of undermining the ANC's One China policy – i.e. the policy that Taiwan is a "renegade province", not a separate country. Maimane was blasted for imperilling the ANC government's supposed policy of isolating Israel. Some within the ruling party even cried treason. Msimanga hastened to explain that he had not been conducting alternative foreign policy but was merely trying to boost investments in his city. Maimane explained that he had met Netanyahu only to help advance the two-state solution to the Middle East crisis – which the ANC government also officially endorses. He said he had also hoped to meet Palestinian Authority President Mahmoud Abbas, but this had not come off.

This brouhaha exposed confusion in the ANC government's policies. When asked how Maimane had violated government policy, official spokespeople could only cite President Jacob Zuma's remarks at the ANC's 105th birthday celebrations that "we firmly discourage travel to Israel for causes not related to fostering peace in the region". But that was Zuma enunciating ANC rather than government policy, presumably. And Maimane had said he was in Israel precisely to foster peace.

Meanwhile, in Taiwan, the government itself maintains a de-facto embassy, though it is officially called a "liaison office".

Former DA leader Tony Leon, who later served as South Africa's ambassador to Argentina from 2009 until 2012, sees several contradictions. "Zuma told me prior to my Argentine appointment that 'it was important for SA to be represented by faces other than the ANC.' True then and not now, alas."

He also notes that his embassy spent a great deal of time arranging visits to Argentina by provincial and municipal politicians, mostly from the ANC.

Conversely, one could add, the ANC did not complain when, during the 1980s, many US cities, pension funds and universities contradicted US President Ronald Reagan's policy of "constructive engagement" with apartheid South Africa by disinvesting their own funds from this country.

Leon also recalls that when he was DA leader, he visited Israel and met then Palestine leader Yasser Arafat and Israeli Prime Minister Ariel Sharon. He also visited Taiwan twice and met the Dalai Lama in India. He comments: "No ANC outrage then of any sort. So what has changed?"

Solly Msimanga
Mayor of Tshwane

Mmusi Maimane
Leader of the DA

Tony Leon
Former leader of the DA

Perhaps what has changed is that the ANC has grown increasingly insecure as its power erodes and therefore has become more jealous of its prerogatives over foreign policy.

Msimanga's visit to Taiwan no doubt rubbed salt in the wounds of its loss of the capital city in last August's local government elections.

Though Maimane and Msimanga firmly denied they were conducting separate DA foreign policy, would it have been legitimate if they had been?

Leon certainly thinks so. "SA's foreign policy is incoherent, haphazardly implemented and its first principles are often honoured only in the breach.

"It is completely appropriate for the official opposition to pursue foreign policy objectives consonant with its own values, especially as the party now controls four major cities and one province. The 'treason charge' is utterly spurious..."

Foreign policy pundits are not quite as unequivocal.

Brazilian foreign policy academic Carlos Milani has noted in an article for the SA Institute of International Affairs (SAIIA) that, globally, diplomacy is becoming increasingly decentralised, with sub-national entities – whether lower levels of government or other interests, such as businesses – conducting more of their own foreign relations.

Milani believes that ultimately such diplomacy should be guided by the foreign policy set by the national government. However, he also says national governments should formulate foreign policy in consultation with these other entities and in pursuit of the genuine national interest – not the interest, as is so often the case, of a narrow elite.

So, are SA's Middle East and China policies really in the national interest? Or are they much more an expression of the ruling ANC's ideological whims?

China is undoubtedly important to all of us. But is it necessary for the government to be so cringingly slavish that it bars visits from the Dalai Lama to SA, for instance, just in case this might offend Beijing? (Government has still not had the courage to admit it had done so.) And does the government not undermine its own ambition to be a neutral broker in the Middle East by so clearly manifesting its preference for the Palestinians? Revealingly, just as Maimane was venturing into the Middle East, Zuma chose not to renew the contracts of his two special envoys to that region. Surely this is an implicit admission of failure?

In light of such frustrations and embarrassments, government should actually welcome the injection of fresh ideas and initiatives from elsewhere in the country into foreign policy. ■

editorial@finweek.co.za

Peter Fabricius was foreign editor of Independent Newspapers for 20 years, writing on African and global issues. He has been writing weekly columns for the Institute for Security Studies (ISS) since 2013.

Gallo Images/Getty Images

GOLF DIGEST IS ON SALE NOW!

Golf Digest

FEBRUARY 2017 R38
OUTSIDE RSA:
R33.33 (EXCL TAX)

5 FAST FITS FOR HIGH HANDICAPS

XTREME BOB
PRICEY CLUBS AND CRAZY GOLF GAMES

TURKISH DELIGHT

3-WOOD V 3-HYBRID

RICKIE'S DISTANCE TIPS

GET BETTER IN 8 SECONDS

WIN A R7 000 TAYLORMADE M DRIVER

9 771025 053005 02255

Subscribe to South Africa's best golfing magazine

CALL 0860 100 999 / **EMAIL** subs@magsathome.co.za / **SMS** "GD" to 40573

in brief

>> **TREND:** A fast way to get cash for your second-hand car p.8

Seth A. Klarman
Value investor and founder of the Baupost Group

"IF THINGS GO WRONG, WE COULD FIND OURSELVES AT THE BEGINNING OF A LENGTHY DECLINE IN DOLLAR HEGEMONY, A RAPID RISE IN INTEREST RATES AND INFLATION, AND GLOBAL ANGST."

– **Seth A. Klarman,** value investor and founder of the Baupost Group, which manages $30bn, warns clients in a letter about investing during the age of US President Donald Trump. While stocks have rallied on Trump's win, Klarman warned of "perilously high valuations", saying investors focused on the potential benefits of stimulative tax cuts while ignoring the risks of America-first protectionism and the erection of new trade barriers, nytimes.com reported.

"WE'VE HAD AN INDUSTRY [IN SOUTH AFRICA] THAT'S BEEN SHRINKING FOR 20 YEARS. IF WE ARE GOING TO STOP THE ROT, WE NEED A DOCUMENT AND A FRAMEWORK THAT ENCOURAGES INVESTMENT."

– **Anglo American CEO Mark Cutifani** in an interview with the *Financial Times*. The mining industry is eagerly awaiting the publication of a new mining charter and amendments to the Mineral and Petroleum Resources Development Act (MPRDA) in the coming months. Cutifani described the next three to four months as the "most important for the South African mining industry in 150 years", it reported.

Mark Cutifani
CEO of Anglo American

Gallo/Getty Images

"It is a truism in South Africa that to transform society you must first transform the mines."

– The *Financial Times* in an editorial on the future of South Africa's mining industry, which it says "hovers between revival and accelerating decline". The paper said there is "little doubt" the outcome will depend on the outcome of deliberations on a new mining charter, which is aimed at accelerating transformation in the sector. The mining sector accounts for 10% of GDP and employs nearly half a million people.

THE GOOD

Former FirstRand CEO and current chairperson of the National Student Financial Aid Scheme (NSFAS), Sizwe Nxasana, and a team of professionals working on a pro bono basis, are making good progress on a project to design and build a new student funding scheme to address the needs of poor and "missing middle" students, *Business Day* reported. The Ikusasa project, which will cost an estimated R45bn a year, will be a partnership between the private sector and government, via NSFAS. It is aimed at plugging various gaps in the NSFAS model that have been highlighted by #FeesMustFall protestors.

THE BAD

The long-struggling mobile operator Cell C has seen its corporate credit rating downgraded by Standard & Poor's (S&P) to D, its lowest junk rating, after it missed interest payments in January on its €400m senior secured bonds that are due in 2018. Cell C is in the midst of capital restructuring plans, which include Blue Label Telecoms buying a 45% stake in the business. Blue Label said it will provide a market update on the process by the end of February, declining to comment on the S&P matter, Moneyweb reported.

THE UGLY

President Jacob Zuma's decision to deploy 441 soldiers to the Parliamentary precinct in the week of his State of the Nation Address to help the police in maintaining law and order has been rightfully condemned by opposition parties, defence and legal experts. Mpho Kwinika, president of the SA Police Union, perhaps summed it up best: "If the national police commissioner says he can deal with the threats, why bring in the army and, if he can't, how grave are the threats, when were they learnt of and why hasn't the public been told of these threats?"

DOUBLE TAKE

BY RICO

RIO TINTO IN SHARE BUYBACK

12%

Diversified miner Rio Tinto announced a higher-than-expected dividend on 8 February and said it would repurchase $500m of its shares as a recovery in commodity prices boosted results, ft.com reported. The group posted a 12% increase in pre-tax profit to $5.1bn for the year to end December, while net debt fell 30% to $9.6bn. Its iron ore operations accounted for 90% of underlying earnings. "With costs and spending now under control, miners are in a sweet spot as the extra revenue from higher commodity prices flows straight through to the bottom line," ft.com reported. (Also see page 38.)

CHINESE RESERVES DROP

$2.998tr

China's Central Bank said its foreign exchange reserves declined to $2.998tr in January, putting it below the psychologically important $3tr level, and significantly below the nearly $4tr in June 2014, nytimes.com reported. The decline is mainly attributable to the Central Bank's attempts to prop up the value of the renminbi. More broadly, it also shows the direction of the Chinese economy – "the era when the world rushed in to invest in China to build factories or apartment buildings – generally, to get a piece of the action – is fading", it reported. It still runs trade surpluses of between $40bn and $60bn a month.

SUBSCRIBE NOW

SAVE UP TO 40%

FINWEEK IS SOUTH AFRICA'S LEADING WEEKLY INVESTMENT AND FINANCIAL MAGAZINE. WE DELIVER IN-DEPTH REPORTING ON BUSINESS AND THE ECONOMY, EQUIPPING OUR READERS TO MAKE SOUND INVESTMENT AND BUSINESS DECISIONS.

BUY NOW AT MYSUBS.CO.ZA

PRINT EDITION
SUBSCRIPTION OPTIONS*:
1 YEAR: R1872.50 – 40% = R1124
6 MONTHS: R936.25 – 30% = R656
3 MONTHS: R486.85 – 20% = R390
OFFER EXPIRES ON 31 MARCH 2017.
*INCLUDES ALL POSTAGE OR DELIVERY COSTS, SOUTH AFRICA ONLY.

CONTACT US:
TEL: 087 740 1019
FAX: 086 298 3809
SUBS@FINWEEK.CO.ZA

DIGITAL EDITION
SINGLE ISSUE R29.90
12 MONTHS – MONTHLY R100
3 MONTHS – ONE-OFF R290
6 MONTHS – ONE-OFF R575
12 MONTHS – ONE-OFF R995
OFFER EXPIRES ON 31 MARCH 2017. IF AT ANY TIME YOU CHOOSE TO DISCONTINUE YOUR SUBSCRIPTION, CALL 0861 697 827 OR EMAIL SUPPORT@MYSUBS.CO.ZA.

trend

By Jana Jacobs

Cash for your car

CarZar is an online platform where South Africans can sell their cars for cash, quickly and conveniently.

"Our mission is to empower customers to sell and buy used vehicles seamlessly," says CarZar co-founder and joint managing director, Fernando Azevedo Pinheiro, in an interview with *finweek.*

Having first-hand experience of the pitfalls and difficulties that come with selling a second-hand car in South Africa, Brazilian-born Pinheiro decided that there had to be a better, simpler way to go about this transaction.

When it came to selling his car, he failed to find a single dealership in Cape Town, where he is based, that was willing to take it off his hands. When he eventually managed to sell it, it was for much lower than the car was actually worth – and the offer came from a Johannesburg dealership.

After meeting Michael Muller, who is joint MD of CarZar and has also experienced the joys of selling a car, the model began to take shape, and the two co-founders secured their first round of funding from SilverTree Capital.

"We launched version 1.0 in April 2016 – it was very basic. We really believed in the model and we wanted to make it happen fast, so we acted quickly," explains Pinheiro.

And so the CarZar journey began. This online platform allows South Africans to sell their cars, at competitive prices, quickly and conveniently.

Potential sellers simply go onto the CarZar website, enter the make, model and year of their vehicle, as well as its mileage, and a selling price range is generated. Should the seller be happy with the range, CarZar sends a fully trained, professionally equipped team of inspectors to assess the car, after which the selling price is confirmed.

The CarZar service is completely free for sellers; the business generates revenue by selling the vehicles to its extensive network of dealerships at a mark-up.

The dealerships that CarZar works with can rest assured that the vehicles they purchase are vouched for as well. "We take full responsibility for the vehicle inspection. If there is something wrong with the car that we did not pick up, we assume responsibility," says Pinheiro. In this (rare) scenario, the dealership receives a discount or is fully refunded.

Michael Muller and **Fernando Azevedo Pinheiro,** joint MDs of CarZar.

Moving into the fast lane

Pinheiro and Muller didn't have auto industry experience and they had to learn all about buying and selling cars, as well as build up a network of dealerships. But, says Pinheiro, this wasn't the biggest challenge when it came to CarZar.

"Learning to buy and sell cars was not the tricky part, educating customers on how pricing and valuation works, was. Sometimes they don't understand the reason for the price that is offered to them, since they don't take into consideration the reconditioning costs of the vehicle and that retail price includes operational costs as well as profit of the dealership."

> "We take full responsibility for the vehicle inspection. If there is something wrong with the car that we did not pick up, we assume responsibility."

Sellers tend to expect that their car will fetch its book value, but, explains Pinheiro, this is just a benchmark and at the end of the day, a vehicle's market value tends to be far below that.

While it makes sense for insurance companies to use the book value of a vehicle in order to determine premiums (the higher the value of your car, the higher the premium you have to pay), this can lead to an overstated value, and expectation from the seller. Pinheiro's aim has been to show customers that it is far more beneficial to sell a car for a fair price, and have the cash in hand. Further, by using CarZar, the seller has more freedom of choice than they would if they simply traded their vehicle in and became locked into a particular dealership, according to him.

Shifting gears

CarZar has proven its economic viability to its funders, and has secured three rounds of funding since launching.

The CarZar team is happy with the young company's performance, and Pinheiro believes they are on the right path to furthering the business.

"In 2016 we had about 6 000 online bookings through our site, excluding enquiries we received offline. And we have been growing at around 30% per month," he enthuses.

As for expansion plans, the vision is ambitious, but Pinheiro insists that they want to perfect the business model in SA before scaling up.

"We like to dream big," says Pinheiro. "We really believe in this model. Our vision is to be the biggest car wholesaler in Africa."

He believes there is a great number of opportunities on the continent, but on the immediate agenda is establishing a presence in all of the major metros in SA – currently CarZar only operates in Cape Town and Johannesburg.

When asked how long before African expansion becomes a reality, Pinheiro says that they will operate in SA for another year or two before tackling other markets. "Once we are an established brand in SA, we will be big enough, have a strong team, and will be able to manage operations here and abroad." ■

editorial@finweek.co.za

Image: Supplied

market place

THIS WEEK:

>> **House View:** Tax-free portfolio, DRDGold *p.10*
>> **Killer Trade:** Smoother sailing ahead for Trencor? *p.11*
>> **Simon Says:** Views on Kumba Iron Ore, Vodacom, Distribution and Warehousing Network, Hudaco Industries, PPC *p.12*
>> **Invest DIY:** When is it a good idea to double up on a stock? *p.13*
>> **Investment:** How to include shares in your RA *p.14*
>> **Technical Study:** Lonmin's woes not over *p.15*

FUND IN FOCUS: INVESTEC EQUITY FUND

By Niel Joubert

Rewarding long-term investors

The fund aims to provide a total return (the combination of income and capital growth) by investing in equities.

FUND INFORMATION:

Benchmark:	87.5% Alsi + 12.5% MSCI AC World NR
Fund managers:	Rhynhardt Roodt and Chris Freund
Total expense ratio:	2.06%
Fund size:	R7.8bn
Minimum lump sum / subsequent investment:	R10 000 lump sum / R500 per month
Contact details:	0860 500 900

TOP 10 EQUITY HOLDINGS

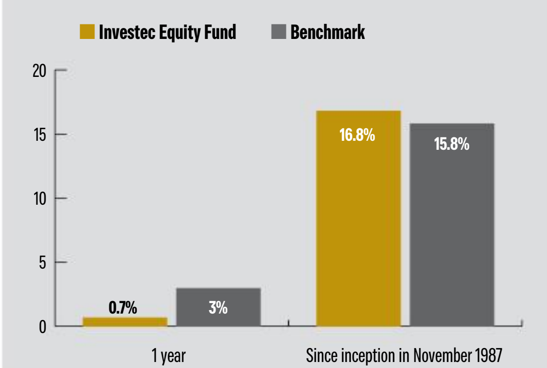
As at 31 December 2016:

1	Sasol	6.7%
2	Tiger Brands	6.6%
3	FirstRand	5.5%
4	Naspers*	5.2%
5	British American Tobacco	4.8%
6	Steinhoff	3.7%
7	BHP Billiton	3.5%
8	Sappi	3.2%
9	Tongaat Hulett	3.2%
10	Investec plc	2.8%
	TOTAL	**45.2%**

*finweek *is a publication of Media24, a subsidiary of Naspers.*

PERFORMANCE (ANNUALISED AFTER FEES)

As at 31 December 2016:



Fund manager insights:

Financial market volatility highlights the importance of having portfolio managers who have strong stock selection skills, says Chris Freund, head of SA Equity & Multi-Asset and portfolio manager at Investec Asset Management.

The Investec Equity Fund has a track record of solid long-term performance and recently was awarded the Special Raging Bull Award for the top-performing domestic equity fund over the past 21 years.

The Investec Equity is an actively managed equity fund for investors seeking capital growth over the long term. As shares are considered a higher-risk asset class, it is important to have a long-term investment horizon. Equity funds can be volatile over the shorter term, but with time, as corporate earnings grow, tend to comfortably outperform lower-risk investments like cash and bonds, says Freund.

According to him, the fund has a unique stock-picking philosophy, the cornerstone of which is identifying reasonably valued shares where expectations of future profits are being revised upwards (positive revisions).

"Conversely, we want to avoid shares where consensus profit expectations are being lowered (negative revisions) and where valuations are excessive."

Key to this methodology is ensuring the sustainability of these changes in profitability, a task that Investec considers both from a bottom-up or stock-specific perspective as well as a top-down view of broad economic conditions.

Freund says the net result of this approach is designed to deliver more consistent outperformance of market indices. According to him the levels of volatility in 2017 will be below the at times "almost seismic volatility of 2016" and hence investors can look forward to the resumption of better returns.

"The outlook for South Africa (economically and politically) is tentatively more positive than what it was a year ago. We believe there are investment opportunities among stocks with exposure to these improving fortunes — banks, food producers and select retailers," he states.

"By remaining consistent in our philosophy of investing in companies receiving positive earnings revisions that are trading at reasonable valuations, we certainly expect to add value for our clients in 2017."

Why *finweek* would consider adding it:

The Investec Equity Fund was awarded a Special Raging Bull Award for the Best South African Equity General Fund on straight performance for 21 years to 31 December 2016.

The fund has rewarded long-term investors – it has outperformed the FTSE/JSE All Share Index (Alsi) over very long periods – and over 21 years it provided an annual average return of 15.9% versus the 13.7% from the Alsi.

It has achieved this with less "heart failure" risk, as annualised volatility has been approximately 1.5% lower than the JSE averages. ■

editorial@finweek.co.za

TAX-FREE PORTFOLIO

BUY SELL HOLD

By Simon Brown

Make sure your tax-free allocation is maxed out

January is gone and February is roaring past, which means that the tax year-end is fast approaching, and with that your last opportunity to invest your full tax-free annual allocation for this tax year.

Each individual is allowed to invest R30 000 into a tax-free account every tax year and if you haven't as yet invested the full R30 000 and you have some extra cash waiting to be invested – do it before the end of February.

Come March, the annual allocation will reset for another R30 000 (unless the minister increases the amount, something I doubt he'll do).

I have been buying CSEW40* and DBXWD* in equal weights and come March I will add PTXTEN*, reweighting the portfolio to 40% each to CSEW40 and DBXWD, with PTXTEN taking the remaining 20%.

A last point, we're now two years into tax-free investing and the returns of most exchange-traded funds (ETFs) have been modest. But remember, for a long-term investor two years is not even getting started as we'll be invested for decades. ■

**The writer owns CSEW40, DBXWD and PTXTEN.*

Last trade ideas

BUY Kumba Iron Ore
9 February issue

BUY CSEW40
2 February issue

BUY Richemont
26 January issue

SELL Ellies
19 January issue

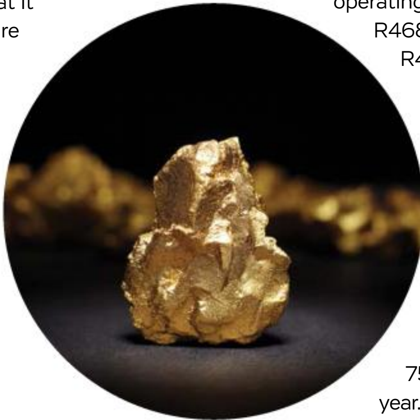
DRDGOLD

BUY SELL HOLD

By Moxima Gama

Recovery on the cards

DRDGold, a low-cost producer of gold from the retreatment of old mine dumps around Johannesburg, announced in a trading update on 6 February that it expects earnings per share for the six months to end December to be between 76% and 96% lower than in the corresponding period in 2015. This is driven in part by an increase in operating costs in the December quarter and costs related to the clean-up and closure of some Crown Mines sites, the company said.



DRDGold's fortunes are closely tied to the gold price, which has gained about 9% since Christmas to trade at nearly $1 230/ounce at the time of writing on 7 February. There's room for further upside if the US Federal Reserve retains a hawkish stance on interest rate increases at its next meeting in March. On the charts gold spot is recovering within its major bear trend and has potential to rise to $1 300/ounce before encountering major resistance, which could prolong the primary bear trend. In all, it is expected to be a bumpy ride for gold prices this year.

The group said it expects to produce between 136 000 and 140 000 ounces of gold in the year to end June, with cash operating costs of between R468 000/kg and R482 000/kg. At the time of writing, the rand price for gold was trading at about R583 000/kg.

How to trade it:
DRDGold surged after trading out of its long-term bear trend and confirming a positive breakout above 755c/share in March last year. However, resistance encountered at 1 210c/share has triggered current downside, with support retained at 520c/share. If that level holds firmly and DRD recovers above 755c/share, go long. Gains back to 1 210c/share could then ensue.

Breaching that 1 210c/share key level would end a long-term consolidation and kickstart the ascending phase of a huge bottoming-up pattern. Upside to 2 175c/share would be possible. Watch the gold spot price simultaneously in order to take in profits on sharp reversals. Refrain from going long if downside persists through 520c/share. ■

editorial@finweek.co.za

Last trade ideas

BUY Kumba Iron Ore
9 February issue

BUY MTN Group
2 February issue

BUY Richemont
26 January issue

BUY Aspen Pharmacare
19 January issue

DRDGold's fortunes are closely tied to the gold price, which has gained about 9% since Christmas to trade at nearly $1 230/ounce at the time of writing on 7 February.

Gallo Getty Images/iStock Images

By Moxima Gama

TRENCOR

Is Trencor headed for calmer waters?

The investment holding company took a sharp knock when Hanjin Shipping declared bankruptcy, suffering losses as a result. However, some believe the shipping industry could start recovering in the near future.

Globally, the shipping industry has been under pressure, due in part to a slowdown in demand from China, the world's largest importer of bulk commodities. In addition, an oversupply of vessel capacity has also affected shipping rates, with Drewry Maritime Research estimating that the global shipping industry has been operating at a loss since the end of 2015.

As a result, a number of shipping giants has gone bankrupt in the past two years, including South Korea's Hanjin Shipping Co., which had links to the JSE-listed Trencor.

Trencor is an investment holding company with interests in operations that focus on owning, leasing, managing and trading marine cargo containers worldwide, as well as related finance activities. Its assets include a 48.04% stake in Textainer, one of the world's largest lessors of intermodal containers based on fleet size. Textainer is listed on the New York Stock Exchange.

Hanjin made up 6.4% of Textainer's total carrying capacity at the time of its bankruptcy. This led to a delay in the publication of Trencor's financial results last year, in breach of its listing requirements, and leading to a threat from the JSE to suspend its listing. Trencor said at the time that it was difficult to assess the financial effect of the Hanjin bankruptcy.

52-week range:	R25 - R52.50
Price/earnings ratio:	-
1-year total return:	6.3%
Market capitalisation:	R6.8bn
Earnings per share:	-R0.87
Dividend yield:	7.8%
Average volume over 30 days:	58 059

SOURCE: INET BFA

It reported a $64m loss in the third quarter, and warned in November that its loss per share for the year to end December will be more than 20% bigger than in 2015. The group announced in January that CEO Jimmy McQueen, who has been with the group for four decades, will retire in June. He will be replaced by Hennie van der Merwe, a former managing director of Trencor, Reuters reported.

Sentiment on a recovery in the shipping industry is mixed. Maersk Line believes 2017 will be a critical year for the shipping industry's recovery as new alliances, mergers and partnerships enter into effect. Conservative analysts target 2020 for a complete turnaround, with a mild change in 2017, as oversupply levels out.

More cargo shipping companies might leave the market, which will lessen the competition on the sea.

Technical view:
Trencor has fallen from an all-time high at 8 475c/share in 2014 to a low at 2 500c/share in December 2016. Support retained at 2 500c/share triggered upside through the second resistance trendline of its long-term bear trend (confirmed above 3 720c/share). However, gains to the major resistance trendline may be limited by the mega-overbought three-week relative strength index (RSI).
Go long: A near-term correction triggered by the extended three-week RSI is pending. However, support retained above 3 040c/share should extend the current uptrend towards the major resistance trendline. A positive breakout out of the long-term bear trend would be confirmed above 5 260c/share – with potential to complete a 100% retracement to the all-time high at 8 475c/share in the medium to long term. Investors could go long at any level above 3 370c/share, once the RSI has corrected, and increase positions above 5 250c/share. Note that Trencor trades in huge weekly ranges, therefore a reasonable stop-loss must be retained.
Go short: A reversal below 3 040c/share could see Trencor retest the 2 500c/share key support level. ■

editorial@finweek.co.za

Moxima Gama has been rated as one of the top five technical analysts in South Africa. She has been a technical analyst for 10 years, working for BJM, Noah Financial Innovation and for Standard Bank as part of the research team in the Treasury division of CIB.

TRENCOR

SOURCE: MetaStock Pro (Reuters)

By Simon Brown

Simon's stock tips

Founder and director of investment website JustOneLap.com Simon Brown is *finweek*'s resident expert on the stock markets. In this column, he provides insight into the week's main market news.

KUMBA IRON ORE

Settlement with Sars is good news

Kumba has agreed to a settlement with the South African Revenue Service (Sars) of R2.5bn. The initial claim almost a year ago was for R5.5bn, so the final amount is a hefty reduction and the company had set aside R1.5bn. That leaves R1bn to pay and if it was paid in the year to end December 2016, it would have led earnings to drop by about 12%. Not insignificant but totally affordable, and the 8% decline in the share price on the day seems overdone, especially as the payment is well down on the initial proposed R5.5bn. I still think this stock has more decent upside.

VODACOM

Overpriced for now

The Vodacom update shows a mature company that is ex-growth. Data is growing but data prices are down 15.4%, while voice revenue continues to decline, off another 6.2%. Vodacom is fast becoming a utility and we're seeing this globally with the US mobile carriers trying to find new revenue, but I remain skeptical about this plan. Being a utility is not a bad thing; in fact, at the right price it's a great addition to a portfolio. I'd want to buy Vodacom on a price-to-earnings ratio (P/E) of around 12 times and a dividend yield of around 6.5%, which at current earnings equates to a price of some R115. (At the time of writing on 6 February, the stock was trading at R149.)

DAWN

Follow your rights

For a long time Distribution and Warehousing Network (Dawn) was a darling on the JSE, trading at highs of above 2 300c less than a decade ago. But now it's below 200c and doing a massive rights issue at 100c to raise R350m. This rights issue is fully underwritten by Coronation, Ukhamba Holdings, RECM and Calibre Ltd. RECM is underwriting R201m of the issue, while Ukhamba is only taking R49m. Ukhamba holds almost 32.25% of Dawn, and this issue will dilute its holding; perhaps it simply doesn't have the cash to follow its rights. But RECM potentially taking a large slice of Dawn post the issue is noteworthy and show that it is confident that management can get the company back on track. With shares at 180c and rights at 100c I would follow my rights if I was a shareholder.

With shares at 180c and rights at 100c I would follow my rights if I was a shareholder.

HUDACO INDUSTRIES

Solid results, but treading water

Considering the environment the company operates in, the Hudaco results were very solid with headline earnings per share (HEPS) up 5%, the dividend maintained and a return on equity of 21%. If you consider that earnings were down some 20% at mid-year, the second half was excellent. It's not surprising that the stock is trading at 12-month highs, and on a P/E of 10 times and a dividend yield of almost 5%, the company is not expensive. The spike in commodity prices has helped, as has the stronger rand, with the latter helping to reduce the amount of cash being tied up in inventories. But how will it grow further? Treading water with a 5% increase in HEPS is fine, but we need mining and manufacturing to start kicking higher before Hudaco can soar. So, while a decent stock to hold, growth for the next few years may continue to be modest until the local economy starts growing at a decent rate again.

Treading water with a **5%** increase in HEPS is fine, but we need mining and manufacturing to start kicking higher before Hudaco can soar.

PPC

Rest of Africa helping the balance sheet

The PPC trading update was unsurprisingly a mixed bag with South Africa under pressure while the new operations in Democratic Republic of Congo and Ethiopia are both expected to start sales in the first half of this year. This will be a ramp-up so full production will likely only start in 2018. Zimbabwe, Rwanda and Botswana recorded a 9% increase in sales and with another R1bn arriving late last year (this from a BEE deal to follow from the rights issue cash pile) the balance sheet should be looking much better. SA remains its weak link but the expansion into the rest of Africa is on track so far. ■

editorial@finweek.co.za

By Simon Brown

FUNDAMENTALS

The ins and outs of doubling up on shares

So you're already holding a specific share via an exchange-traded fund or unit trust. Is it a good idea to buy the share on its own too? Simon Brown explains how he'd work out the answer to that question.

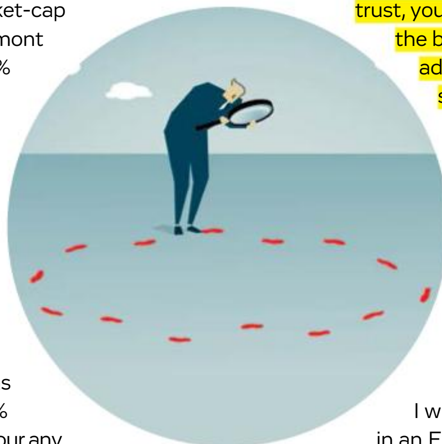
I often get asked about buying a share that already exists within an exchange-traded fund (ETF) or unit trust you hold. For example, you have a Top40 ETF but you do want to specifically buy Richemont* as well. The concern is that you're duplicating the Richemont holding.

The answer is that you have to know your ETF. So let's set the ground rules and gain a deeper understanding of what we're doing.

Determining the weighting of the stock in the ETF

First, what shares do you have within your ETF portfolio? We need to look through the ETF (or unit trust) and see what it holds. Equally important is knowing what the weighting of each stock is.

If you hold a normal market-cap weighted Top40 ETF, Richemont has a weighting of almost 8% in the index, while an Indi25 ETF has just over 13% in Richemont. These are very different levels, and that is exactly why it has important to know your ETF and why you need to look inside to see exactly what it contains.



It is also why I prefer the equally weighted CSEW40*, as each stock has the same 2.5% weighting and it does not favour any one stock over another, effectively leaving the favouring of individual stocks to me rather than the index weighting.

So, the ETF you hold will to a large degree determine whether you should be adding a specific stock to your individual stock portion of your portfolio.

With the Top40 and Indi25 examples above I would be cautious about adding extra Richemont shares as you already have a fair holding of the stock. Rather look at those stocks that have a low weighting – below 1% – and see if it is worth increasing the stake in any of them and leave the already large holdings as they are, using just the ETF for your position.

Look at those stocks that have a low weighting – below 1% – and see if it is worth increasing the stake in any of them.

The ETF within your portfolio

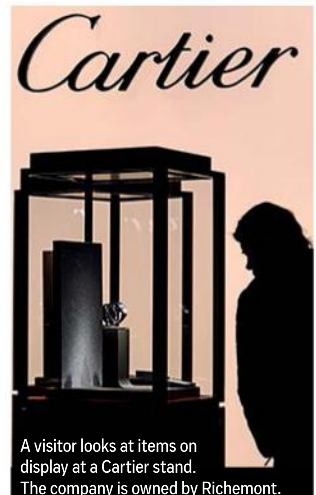
But what is also important is how much the ETF or unit trust makes up towards your total portfolio. In my case ETFs are just over 50% of my total portfolio with another 30% going into 10 to 12 quality shares. So, if I held only CSEW40, the ETF part of my portfolio would result in a holding of 1.25% in Richemont (the ETF is half of my portfolio and the ETF holds 2.5%, so half of that is 1.25%). This is a small percentage, which gives me enough room to add to the stock if I think it is one of the best to own.

Having looked through your ETF or unit trust, you then decide what the best of the best stocks to add are, and by adding you are up-weighting these stocks within your portfolio. So I do add an extra position in Richemont as it is a stock I believe will perform well over the long term. But note that I don't go crazy, adding only another 3% to 4%, which would give Richemont a total weighting of between 4.25% and 5.25%.

So the bottom line is that I will add a stock that is already in an ETF or a unit trust I hold to my portfolio, but only after some digging to see what percentage of my overall portfolio it makes up. And as always I prefer the equally weighted ETF as it lets me decide which stocks to up-weight rather than deciding for me based purely on the market cap of the stock. At the end of the day I hold only six Top40 stocks, meaning the remaining 34 stocks in the Top40 sit at their ETF weighting. These six stocks are the ones I consider to be the best of the best. ■

editorial@finweek.co.za

The writer owns CSEW40 and Richemont shares.



A visitor looks at items on display at a Cartier stand. The company is owned by Richemont.

Gallo Getty Images/iStock Images

If you hold a normal market-cap weighted Top40 ETF, Richemont has a weighting of almost 8% in the index while an Indi25 ETF has just over 13% in Richemont.

By Schalk Louw

RETIREMENT

Best-kept secret: Direct shares in your retirement annuity

There are tax benefits if you structure your retirement annuity in a certain way.

The 28th of February doesn't only mark a very important date for most companies who face financial year-end, but also for countless personal taxpayers. Before you lose hope when thinking of the massive task that lies ahead of you, however, I would like to focus on the advantages of tax returns that most taxpayers are often not fully aware of.

I have made several references to the Matryoshka doll (aka Russian nesting doll) in the past, by discussing how investment products often remind me of these dolls. The concept is based on one doll (or investment product) that fits into another, which fits into another, and another, and so on. Eventually, the accumulated fees attached to these "nested" products become so unattractive that the product gains nothing but a bad reputation. Although many product providers have made an effort to keep costs low, we still find that in some instances they can add up.

Retirement annuities (RAs) are one example of this. But why? Let's start by taking the dolls apart:

- The costs attached to an RA itself;
- In many cases, an RA is invested in a Fund of Funds, which as the name suggests, is one unit trust that invests in other unit trusts, that each comes with its own overhead costs;
- The costs attached to the unit trusts used within the RA.

So, you have all these layers upon layers of cost structures attached to the product, when all the investor actually wants is the last little doll, namely shares, property shares or bonds. If the layers aren't managed carefully, the costs can potentially add up. Investors are still wary of RAs, but they do offer tremendous "nesting" benefits in terms of tax.

Can the layperson structure their RA in such a way that they too can invest in the last doll called direct shares? The answer is yes.

A Personal Share Portfolio (PSP) allows you to tailor your own bespoke share portfolio as part of your retirement investment strategy. Most RA platforms in SA now offer the solution for a portfolio manager to choose a selection of local and international shares, which, as a direct share portfolio, can be included in your retirement investment and be actively managed. This solution offers quite a few advantages, including:

TAX ADVANTAGES

No capital gains tax or income tax is payable within a retirement annuity, so you can have exposure to direct shares within your RA, without the usual tax implications attached to a separate direct equity portfolio (which does not form part of your RA).

PERSONAL ATTENTION

Unlike many asset management companies, many stockbroking companies offer you direct access to portfolio managers.

COST-EFFECTIVENESS

The current average total expense ratio for general equity unit trusts amounts to 1.56% per year with additional performance fees attached to many of these funds. In most cases, personal share portfolio management fees start from 1.14% (incl. VAT), which can be reduced on a sliding scale based on the value of your portfolio, with no performance fee charges.

ESTATE PLANNING

RAs hold many advantages for estate planning, including a potential 3.5% saving in executor's fees.

One of the main advantages of an RA that is also invested in direct shares is probably the fact that you have more control over your investment composition. The reason for this is that any RA is subject to Regulation 28 of the Pension Funds Act. I will discuss this in further detail in my next article, but in short, Regulation 28 means that within an RA, you will be subject to certain restrictions in terms of the weights you will be allowed to allocate to different asset classes.

> One of the main advantages of an RA that is also invested in direct shares is probably the fact that you have more control over your investment composition.

Based on historical data, it is a well-known fact that shares held within an RA certainly offer the best long-term growth potential. For a young investor looking to invest directly in shares, the problem is two-fold. Firstly, Regulation 28 restricts the investment in direct shares (both locally and offshore) within a RA to 75%.

Another problem is that if you choose to invest in equity-based unit trust funds, you should know that very few of these funds can actually invest 100% of the fund in direct shares, simply because of cost recovery and the fact that it has to have the capacity for withdrawals to be made. By including the extra doll called unit trusts in your RA, the possibility of you reaching that 75% is unlikely. By investing directly in shares, however, you have more control, which means that you can reach your 75% target.

The good news is that this option is now available to most investors, which can definitely give your RA a huge boost in terms of performance. ■

editorial@finweek.co.za

Schalk Louw is a portfolio manager at PSG Wealth.

Gallo Images/iStock

By Lucas de Lange

COMMODITIES

Lonmin is rapidly burning cash

The market is also not impressed by Sibanye's proposed Stillwater deal.

Judging by Lonmin's quarterly report, which was issued at the end of last month, there is good reason for it being the weakest share among the larger issues on the JSE for so long, as measured by the difference between its price and its 200-day exponential moving average (EMA). It's once again running out of cash with a net cash position of a mere R49m at the end of December after spending R106m on working capital and capex in the quarter. In addition to the problem of a low platinum price, it's also sitting with several other headaches such as labour problems. The Marikana albatros, which will have its fifth anniversary later this year, will hang around its neck forever.

Although it's an important company as the third-largest platinum producer, there is little interest among other platinum and mining groups to become involved in it. For example, Neal Froneman, CEO of Sibanye Gold, who is very active in purchasing assets and who is seen as a potential saviour, says that he is not interested in loss-makers. He is currently interested in buying the Stillwater Group in the US, and he has indicated that he intends a rights issue of $1.3bn (about R17.2bn) to partly finance the deal. Under current conditions, the total price will be in the region of R30bn. About 78% of Stillwater's reserves consist of palladium, the price of which has risen by more than 40% over the past year. According to Froneman, it is Stillwater's profitability that has made it attractive as it will improve Sibanye's cash flow.

Commodity shares are still the top performers on the JSE. A new arrival, Tharisa plc, heads the list. It's an integrated resources group with its head office in Europe, and contrary to Lonmin, it has had excellent results for its local platinum and chrome mines in its financial year to September. It has exceeded all its production targets.

Only Barloworld and Datatec appear among the top 10 performing shares. Barloworld benefits from the recovery in commodity prices as an equipment supplier to the mining industry, while Datatec has rocketed up in the midst of an exceptionally high turnover.

The PSG Group, which performed strongly in 2015 before it started tumbling in November – by about 41% to reach a low of R165 a year ago – is once again one of the strongest shares. The reason is evident – it's due to the good results attained by Capitec and Curro. The latter has improved earnings per share for the year to end December by a whopping 52% to 67%.

Among the weakest shares, the Botswana retailer, Choppies, still stands out. Currently, it's lying about 60% below its high reached in August 2015. Sibanye is the third-weakest on the list. The market is apparently not impressed by its platinum plans. Its price dropped sharply when the proposed Stillwater deal was announced. At the same time, there is also pressure on gold shares. Gold Fields, Pan African Resources and Harmony are also among the weakest shares.

There is an interesting phenomenon among the shares that have broken through: Clicks, Imperial, Pioneer Foods, Standard Bank and FirstRand are all lying close to their 200-day averages, which is regarded by many analysts as a support level where buying could be worthwhile. ■

editorial@finweek.co.za

Lucas de Lange is a former editor of *finweek* and an author of two books on investment.

STRONGEST SHARES*

COMPANY	% ABOVE 200-DAY EXPONENTIAL MA
THARISA	53.1
ASSORE	45.9
KUMBA IRON ORE	42
ARCELORMITTAL	34.4
ANGLO AMERICAN	26.2
GLENCORE	26.1
ARM	22.4
EXXARO	19.4
BARLOWORLD	19.4
DATATEC	17.9
SOUTH32	17.6
ASTRAL	17.1
AVENG	16.8
PSG	15.7
NORTHAM	15.1
REBOSIS	14.4
KAP	12.3
SAPPI	11.96
BHP BILLITON	10.2
TELKOM	9.7
ADCOCK INGRAM	9.7
RHODES FOOD GROUP	9.2
CAPITEC	9.2
TIGER BRANDS	8.4
GRINDROD	8.4
RICHEMONT	8.2
DRDGOLD	8
TFG	7.9
TONGAAT	7.4
MASSMART	6.74
WBHO	6.7
STEINHOFF	6.3
SA CORPORATE	6.2
FORTRESS-A	5.98
AMPLATS	5.97
RCL	5.3
NEDBANK	5.04
VUKILE	4.69
SANTAM	4.6

*Based on the 100 largest market capitalisations

BREAKING THROUGH*

COMPANY	% ABOVE 200-DAY EXPONENTIAL MA
CLICKS	4.04
MMI HOLDINGS	3.7
BLUETEL	2.8
IMPERIAL	1.9
PIONEER FOODS	1.6
TEXTON	1.56
STANDARD BANK	1.43
FIRSTRAND	1.4
INVESTEC PLC	1.13
SUN INTERNATIONAL	1.1

Goats graze in the vicinity of the Marikana platinum mine, which is owned by Lonmin.

WEAKEST SHARES*

COMPANY	% BELOW 200-DAY EXPONENTIAL MA
LONMIN	-46.3
CHOPPIES	-26.6
SIBANYE	-22.4
CAPCO	-18.6
PPC	-17.3
GOLD FIELDS	-16.1
ITU PLC	-15.8
PAN AFRICAN	-13.3
MPACT	-12.7
HARMONY	-11.7
WOOLIES	-8.1
MR PRICE	-7.9
NAMPAK	-7.5
LEWIS	-7.3
ANGLOGOLD ASHANTI	-7.3
CORONATION	-7.1
SUPER GROUP	-6.96
RBPLAT	-6.5
MTN GROUP	-5.2
LIBERTY HOLDINGS	-5.2
LIFE HEALTHCARE	-5.2
TRUWORTHS	-5.04
REMGRO	-4.8
NETCARE	-4.6
TSOGO SUN	-4.4
NEPI	-4.3
SPAR	-4.1
OLD MUTUAL	-3.9
M&R HOLDINGS	-3.6
REINET	-3.4
GROUP FIVE	-3.3
CITY LODGE	-3.3
RMI HOLDINGS	-3.1
VODACOM	-1.9
SASOL	-1.7
EMIRA	-1.5
ASPEN	-1.2
SANLAM	-1.2
BARCLAYS AFRICA	-1.1
DISCOVERY	-1.05

Gallo Images/Getty Images

DIRECTORS' DEALINGS

COMPANY	DIRECTOR	DATE	TRANSACTION TYPE	VOLUME	PRICE (C)	VALUE (R)	DATE MODIFIED
AFRIMAT	GJ Coffee	7 February	Purchase	108,401	3065	3,322,490	7 February
AFRIMAT	GJ Coffee	7 February	Sell	44,444	3065	1,362,208	7 February
ARGENT	TR Hendry	6 February	Purchase	15,000	470	70,500	7 February
ARGENT	TR Hendry	2 February	Purchase	2,621	470	12,318	6 February
ARGENT	TR Hendry	3 February	Purchase	3,420	474	16,210	6 February
ARGENT	TR Hendry	3 February	Purchase	3,205	476	15,255	6 February
CALGRO M3	BP Malherbe	25 January	Sell	2,000,000	1750	35,000,000	1 February
EFFICIENT	AP du Preez	4 January	Purchase	20	550	110	6 February
EFFICIENT	AP du Preez	5 January	Purchase	4,980	550	27,390	6 February
EFFICIENT	AP du Preez	6 January	Purchase	15,000	550	82,500	6 February
EFFICIENT	AP du Preez	19 January	Purchase	5,000	515	25,750	6 February
EFFICIENT	MM du Preez	4 January	Purchase	20	550	110	6 February
EFFICIENT	MM du Preez	5 January	Purchase	4,980	550	27,390	6 February
EFFICIENT	MM du Preez	6 January	Purchase	15,000	550	82,500	6 February
EFFICIENT	MM du Preez	19 January	Purchase	5,000	515	25,750	6 February
LIFE HEALTHCARE	L Bekker	2 February	Sell	47,366	3395	1,608,075	7 February
LIFE HEALTHCARE	F Patel	2 February	Sell	12,707	3395	431,402	7 February
LIFE HEALTHCARE	PF Theron	2 February	Sell	35,086	3395	1,191,169	7 February
LIFE HEALTHCARE	PP van der Westhuizen	2 February	Sell	10,469	3395	355,422	7 February
LIFE HEALTHCARE	KA Wylie	2 February	Sell	25,703	3395	872,616	7 February
NETCARE	S Chetty	31 January	Sell	7,644	3243	247,894	3 February
PIONEER FOODS	PM Roux	6 February	Exercise Options	30,509	16602	5,065,104	8 February
PIONEER FOODS	PM Roux	7 February	Exercise Options	30,509	16710	5,098,053	8 February
PRESCIENT	S Bailey	30 January	Sell	8,000,000	99	7,920,000	1 February
SEPHAKU	RR Matjiu	2 February	Sell	423,000	290	1,226,700	3 February
SOVEREIGN FOOD	E du Preez	1 February	Sell	20	875	175	7 February
SOVEREIGN FOOD	E du Preez	3 February	Sell	59,980	875	524,825	7 February
TREMATON	A Groll	31 January	Purchase	101,000	280	282,800	2 February
TREMATON	A Groll	27 January	Purchase	186,000	286	531,960	1 February

BEST AND WORST PERFORMING SHARES

SHARE	WEEK PRICE (c)	CHANGE (%)
BEST		
Visual	14	55.56
SilverBridge	332	32.80
Imbalie	13	18.18
BSI Steel	39	14.71
Tharisa	2600	13.04
WORST		
Phoenix	43	-17.31
NVest	250	-15.25
Oando	26	-13.33
Acsion	710	-12.88
WG Wearne	7	-12.50

INDICES

INDEX	WEEK VALUE	CHANGE* (%)
JSE ALL SHARE	52 181.90	-1.74
JSE FINANCIAL 15	14 669.51	-1.33
JSE INDUSTRIAL 25	66 713.77	-1.22
JSE SA LISTED PROPERTY	632.48	-0.99
JSE SA RESOURCES	19 592.17	-3.52
JSE TOP 40	45 366.88	-1.83
CAC 40	475 447	-0.84
DAXX	1 154 944	-0.94
FTSE 100	718 622	1.11
HANG SENG	2 333 157	0.06
NASDAQ COMPOSITE	567 421	0.56
NIKKEI 225	1 891 078	-1.24

*Percentage reflects the week-on-week change.

P/E RANKING

SHARE	FORECAST
PAN AFRICAN	5.11
ASSORE	6.04
ARM	6.52
SOUTH32	6.92
M&R HOLDINGS	7.31
KUMBA IRON ORE	7.49
TEXTON	7.76
LIBERTY HOLDINGS	8.02
RAUBEX	8.24
BARCLAYS AFRICA	8.75

DIVIDEND RANKING

SHARE	F'CAST DPS (C)	F'CAST DY (%)
TEXTON	105	12.9
EMIRA	143	10.0
REBOSIS	125	9.8
ACCPROP	58	8.9
REDEFINE	93	8.6
FORTRESS-A	136	7.9
CORONATION	504	7.8
SA CORPORATE	43	7.6
GROWTHPOINT	195	7.5
PAN AFRICAN	19	6.8

EPS RANKING

SHARE	F'CAST (C)	F'CAST AS %*
NASPERS-N	6144	2.9
BAT	4742	5.6
ASSORE	4592	16.5
SASOL	3812	9.9
CAPITEC	3320	5.6
KUMBA IRON ORE	2651	13.1
TIGER BRANDS	233	5.8
NEDBANK	2321	10.2
MONDI LTD	2300	7.8
BHP BILLITON	2088	9.2

*Forecast EPS as a percentage of current share price

Assore's Khumani iron ore mine near Kathu in the Northern Cape.

Christopher Cory
CEO of Assore

All data as at 12:00 on 8 February 2017. Supplied by INET BFA.

Images: www.assmang.co.za

finweek

COLLECTIVE INSIGHT

INSIGHT INTO SA INVESTING FROM LEADING PROFESSIONALS

FEBRUARY 2017

INFORMATION OVERLOAD

NAVIGATING YOUR WAY THROUGH THE NOISE

Inside

18 Coming to grips with big data

20 What is the big deal about big data?

22 Age of automation

24 Welcome to the Second Information Age

26 Algorithms versus human judgment – whom do we trust?

28 Information deluge the new normal

31 Big data in investment finance: A cautionary comment

33 Beware the noise

By Delphine Govender

INTRODUCTION

Coming to grips with big data

As the investment industry – like the rest of the world – is inundated with data, it is important to keep a clear head in order to deal with the deluge of information effectively.

This first edition of *Collective Insight* for 2017 potentially has its own little irony. It is packed with information to explain the situation that we as investors find ourselves in: we are exposed to just too much information! Information overload indeed.

Jonathan Spira, author of the book *Overload,* said: "After 15 years of studying the problem of information overload I was so overloaded I had to find something else to do."

Our objective with this edition is hopefully not to aggravate the problem but to raise awareness instead. We want to provide readers with a clear and focused construct for understanding and coping with the ongoing bombardment of information we experience. This way we trust you can ultimately establish a framework and a filter for determining what is worth paying attention to and what is just noise.

While many of us might feel "information overload" is the product of a 21st century existence – a time when we are faced with a barrage of endless email, instant messaging, social media updates and website search results – the term was coined as far back as 1964 by author Bertram Gross in his book *The Managing of Organisations.*

What has evolved in the past decade, however, is that the sheer volume of information has increased by an unimaginable order of magnitude. So much so, that whole new industries have emerged in their own right just to analyse this information in terms of its volume (amount of information), its velocity (speed at which information is generated) and its variety (the type of information). The reason? To establish whether some form of pattern or trend in the information can be determined and in so doing predict how the information will be used, especially in decision-making. And so we had the ascent of "big data".

"Today, in the 21st century, investing is about asking the right question. You're no longer going to be a good database. You're going to be a good search engine."

So how exactly did we get here?

When I started out as a fresh-faced investment analyst some 19 years ago, what seemed to make a "good analyst" back then was someone who spent days and weeks just sourcing relevant information from hard copy annual reports (which we received in the post), digging through newspaper clippings and getting their hands on various hard-to-get industry reports in order to understand a company better than the average market participant.

Fast forward to 2017 and for the analysts of today, accessing information in any form provides no edge at all. Instead it's the art of determining from all the information you have at your disposal what matters and what doesn't.

Chief investment officer of US investment firm Ariel Investments, Rupal Bhansali, put it well when she recently said in an interview: "The battleground is no longer having access to information. That was yesteryear's investing. Today, in the 21st century, investing is about asking the right question. You're no longer going to be a good database. You're going to be a good search engine. The answers are there to be found. It's the right questions to ask. We're not looking for information. We're looking for insights."

Our first three articles focus on the current state of play in a world of information overload. Leevania Naicker, Bradley Preston and Tony van Niekerk explain in their respective articles how we got to this point of the "Second Information Age" and what "big data"; "artificial intelligence" and the "information arms race" mean and the impact they have on investors and their decision-making.

Does more information mean markets are more efficient?

The cornerstone of the notion of efficient markets is that share prices reflect all relevant and known information, implying that it should be virtually impossible to encounter fundamental mispricing in shares. It follows therefore that if more information is now widely available today versus any other period before, this should mean that markets should be considerably more efficient and the case for active management should be fundamentally challenged. Yet looking at the returns in markets and across investment managers just last year in the South African stock market, we see this has definitely not been the case. So more information (often objectively generated) also *doesn't* mean better investment decisions?

To help us understand this reality better, the fourth article by Ainsley To explains why humans' innate behaviour can work in a counter-balancing way when we are faced with using new tools to interpret and act on information. To observes that humans tend to show a bias towards still using forecasts by other humans even when provided with clear evidence beforehand that statistical algorithms do better.

Daniel Polakow provides an explanation for why he believes the case for active management is still relevant, though he is adamant that active managers must evolve in the approach that they apply at this time of information deluge. Specifically, Polakow explains the concept of cross-sectional volatility and how this is affecting and influencing the active returns generated by South African managers.

Dan diBartolomeo also cautions investors about relying on the purported benefits of big data in investment decision-making in an indiscriminate way. He argues that any automated processes analysing data and information must be sensibly supervised to establish how and when they can lead to a genuine information advantage.

The final analysis

More and more we hear of people "unplugging" or going through "digital detoxes". This seems to be a conscious attempt to acknowledge that the wall of information hitting us daily – even hourly or by the minute – is simply just too much of a good thing. Perhaps all that is required is a middle ground and a set of relatable guidelines to navigate this dramatic increase in the flow of information.

In the closing article therefore Hannes Viljoen of Investment Solutions provides exactly this action plan. Viljoen reminds investors that the more things change, the more they stay the same. No matter the environment we face, long-term investment goals and strategies rarely need to change dramatically in the face of new, but irrelevant information. The challenge is to hold the course with the understanding that the majority of information coming at us is entertainment and not insight. ■

Delphine Govender is a co-founder and chief investment officer of Perpetua Investment Managers. She is a qualified CA (SA) and a chartered financial analyst (CFA).

PLEASE SEND ANY FEEDBACK AND SUGGESTIONS TO CABOTA@AFORBES.CO.ZA.

finweek publishes *Collective Insight* quarterly on behalf of the South African investment community. The views expressed herein do not necessarily reflect those of the publisher. All rights reserved. No part of this publication may be reproduced or transmitted in any form without prior permission of the publisher.

Convenor

Anne Cabot-Alletzhauser
Head of Alexander Forbes Research Institute

Editorial Advisory Committee

Delphine Govender
Chief Investment Officer, Perpetua Investment Managers
Petri Greeff Executive – Special Projects, RisCura
Patrice Rassou
Head of Equities, Sanlam Investment Management
Heidi Raubenheimer
Faculty at University of Stellenbosch Business School
Steve Watson Investment Marketing Director, Investec Asset Management
Di Turpin
Independent Consultant
Nerina Visser
ETF Strategist and Adviser
Muitheri Wahome
Head: Technical Solutions, Investment Solutions

Gallo Getty Image/iStockphoto

By Leevania Naicker

INSURANCE

What is the big deal about big data?

Big data has the potential to drastically change the life and non-life insurance industries.

By definition, big data is a broad term for data sets so large or complex that they require new forms of processing to enable enhanced decision-making, insight discovery and process optimisation. These new forms of processing transform information, allowing us to see it differently and more effectively.

The sheer volume, velocity and variety of information created in capital markets is ideally suited to big data-enabled capabilities. Predictive financial modelling is transformed from simple, constrained regressions to whole population analytics connecting the dots in patterns never seen before. But it doesn't stop there. The social media, web, music, video and voice universes (and countless others) can be overlayed on the traditional capital markets universe, opening the door to a whole new galaxy of predictive possibilities.

In the world of investing, it not only affects the behaviour of market participants, but also the way in which market participants are observed. For example, big data allows the adviser to see how a retail investor's travel destinations, buying behaviour and online gaming tendencies build a picture of their willingness to take on risk. It gives the adviser better context on the investor. In fact, through machine learning, big data replaces the adviser altogether.

The big deal about big data is that it affects everything and everyone. It is changing the way in which society advances. It is the next "industrial" revolution and we have little control over where it will take us.

Shaping our view of investable assets

In behavioural finance theory, we learnt that it is simply impossible for every individual to possess perfect information about every possible outcome for every single decision. Bounded Rationality is the idea that when individuals make decisions, their rationality is limited by the information they have access to, the limitations of the human mind and the limited amount of time available to make that decision. As big data-enabled capabilities expand, these limitations tend to zero.

The advent of big data analytics changes the way in which we see and invest in the market. It allows us to translate vast amounts of information into robust models that can help to achieve higher returns. Various companies are building models based on the use of big data – such as models that analyse the language in news articles, corporate filings and broker research; or predictive models that use big data to formulate statistical models and forecast outcomes. The latter could result in more accurate forecasts and more predictable variances.

Already, we can see how big data has the ability to shift our perceptions of risk and return. If we are able to predict risk more accurately, is the asset still considered risky? Will big data yield traditional risk measures obsolete? As the information age pushes the boundaries of Bounded Rationality, these are the types of questions to consider.

Big data wins begin with finding the right partner. It is the crossover and sharing of data that transforms information into something magical.

Big data's impact on the insurance industry

Big data has the potential to drastically change the life and non-life insurance industries. Mortality tables will be a thing of the past as averages won't predict the life expectancy of a population but, rather, each individual will have their own expiry date based on the food they eat, their genetic make-up, their ancestral DNA and the diseases that come with it, their movements and exercise routine and their stress levels derived from chemicals released in the body.

Similarly, non-life insurers such as vehicle insurance companies have already found ways to evaluate their customer's driving ability, rewarding them for "good driving habits" and penalising them for bad ones by adjusting the premiums they pay.

This alters the insurance industry's risk tolerance and liquidity constraints because their ability to predict their liability becomes more accurate. In turn, it changes the way in which these institutions invest their assets.

As institutional funds make up the majority of investments in capital markets, this will have far-reaching effects on its composition.

Using big data smartly

Big data wins begin with finding the right partner. It is the crossover and sharing of data that transforms information into something magical. Like health insurance companies partnering with supermarkets to monitor healthy food purchases, or global information companies partnering with data analytics companies to create alpha-generating models – these relationships breed more useful data. In the same vein, the investment landscape will change as partnerships with seemingly unrelated industries create synergistic bonds, making their combined earning potential greater than the sum of their parts. ■

Leevania Naicker is an account manager for Thomson Reuters in Cape Town.

Getty Images/iStock Images

9361/E

IT DOESN'T TAKE 2 HOURS 30 MINUTES

TO PERFORM SWAN LAKE

IT TAKES 20 YEARS

Margot Fonteyn is regarded as one of the greatest ballerinas of all time. By the time she was twenty years old, she had performed Swan Lake as the prima ballerina. For her it was a lifetime of sore feet, straight backs and lifted chins. Sticking to a goal, day in and day out. At Allan Gray we value this kind of commitment. It's the same philosophy we apply to investing and it has worked well for our clients for 42 years.

Call Allan Gray on 0860 000 654 or your financial adviser, or visit www.allangray.co.za

ALLANGRAY

LONG-TERM INVESTING

Allan Gray Proprietary Limited is an authorised financial services provider.

By Bradley Preston

DECISION-MAKING

Age of automation

Recent advances in machine learning and the emergence of 'big data' present challenges and opportunities for fund managers and their clients.

The widespread adoption of smartphones; falling costs of data storage and computing; as well as centrally hosted applications that are able to record user interaction has led to businesses generating, storing and processing significantly more data than historically possible. For example, Facebook disclosed in 2013 that over 4.75bn items, status updates, wall posts, photos, videos, and comments, were shared on its platform each day.

These new large data sets have led to significant opportunities to gain analytical insight and to train new machine-learning models to do anything from recognise you in a photo to recommend new shows to you on Netflix – raising the question of how this data could be used by investment managers and traders to find predictive "edge" in financial markets.

In 2016, AlphaGo, a machine-learning application developed by Google's DeepMind, beat Lee Sedol, the world champion at the board game *Go.* If DeepMind can teach a computer to play a complex board game such as *Go* better than any human, could it not learn to pick stocks better than your average analyst?

Information arms race

The history of investment management has always been an arms race for information, analytical ability and technology. Early in his career, Warren Buffett used to visit Moody's offices to copy historical financial data by hand from their library. Alan Dresher, an analyst at pioneering hedge fund A.W. Jones, would go to the Securities and Exchange Commission (SEC) offices the day a company's financial results were released to receive them in person, while the rest of the market waited for copies to be posted to them. Twenty years later, when the first Bloomberg terminal was released, this information became effortlessly available electronically, eradicating this potential source of edge for the likes of Buffett and Dresher.

As markets and technology have evolved market players have had to adapt, as their previous source of edge is eroded or democratised through technology.

More recently, multifactor models and smart beta products have automated the process of earning various risk premia*, offering a cheaper alternative to fund managers who may have been doing little more than buying cheap stocks based on measures such as price-to-earnings ratios or price to book. In fact, in a recent paper, the team at quantitative manager AQR Capital claims to be able to systematically replicate the investment styles of a range of managers from Warren Buffett to Bill Lynch and George Soros by employing a multifactor-based approach.

New tools

A multitude of data providers are offering new data sources to analysts and fund managers based on non-traditional sources of data. For example, a number of companies offer analysis of satellite images to gain insight into anything from the number of vehicles parked outside retail stores to the size of oil stockpiles, offering real-time estimates of economic and earnings releases that are only released with a time lag.

With the growth of e-commerce, millions of product prices are available in real time on websites. The Billion Prices Project at MIT collects prices from hundreds of online retailers around the world to conduct economic research in real time.

Another area of progress is in processing text. Quantitative analysis and computer models have often been limited to dealing purely with numbers in the past, but the ability of computers to interpret text is progressing quickly. Ranging from emails to annual reports and research reports, the financial services industry creates large volumes of text, more and more of which is being analysed by computers.

What are the implications?

Investment managers and their clients need to understand their sources of competitive edge and how emerging technology will impact these. Fund managers either need to embrace these technologies and data sources or focus on conducting detailed, differentiated analysis that can't be automated by machines.

Gallo Getty Image/iStockphoto

The Billion Prices Project at MIT collects prices from hundreds of online retailers around the world to conduct economic research in real time.

Fundamental managers who are capturing simple risk premia will continue to be challenged by algorithmic and smart beta products which can replicate these simplistic strategies cheaper, faster and more objectively.

Similarly managers who rely on exploiting informational advantages over short time horizons may be at risk as more and more data and computing power is brought to bear on co-incident predictions of economic releases or earnings announcements. ■

Bradley Preston is Chief Investment Officer: Listed Investments at Mergence Investment Managers.

*A **risk premium** is the minimum amount of money by which the expected return on a risky asset must exceed the known return on a risk-free asset in order to induce an individual to hold the risky asset rather than the risk-free asset.

Your financial peace of mind is our priority

www.alexanderforbes.co.za

A licensed financial services provider

By Tony van Niekerk

ANALYSIS

Welcome to the Second Information Age

Today's society suffers from information overload, but companies stand to profit massively if they can sift through the vast tracts of data and use the resulting information effectively.

It was Shakespeare who wrote in his romantic comedy *The Twelfth Night*: "There is no darkness but ignorance." In business today ignorance probably implies not successfully exploiting information.

Forget the Fourth Industrial Revolution. I suggest we focus on what I would like to call the Second Information Age.

The velocity, scope and systems impact of this Fourth Industrial Revolution are fuelled by masses of data producing an oversupply of information. We now have IT and electronics. Both the masses and individuals are producing data too. This ultimately results in an unstoppable flow of information. During the First Information Age, it was all about accumulating information. In the Second Information Age it will be those who are best at harnessing information who will be the winners.

Harnessing information implies that we have taken petabytes of data and filtered it so we arrive at something useful – information. It is this process that I find most fascinating and which, in my opinion, very few people have mastered. The challenge is that, to find the true value in the masses of data we sit on, one has to start with a client solution in mind and also start from the point of raw data.

CHICKEN OR THE EGG? If you start from only the point of the current product set, you will probably miss the disruptive innovation that might be lurking inside the data. However, if you start with only the raw data, the sheer volume and scope of possibilities might overwhelm you. In financial services we mostly limit our innovation possibilities in this way. We look at our current product set and then search the available data or gather more data to find ways to optimise what we currently do.

If, at the same time, we scan the data landscape without our current product set as the starting point, but with client solutions in mind, we might just stumble on real innovation.

> In the Second Information Age it will be those who are best at harnessing information who will be the winners.

The reason Google is interested in getting involved in insurance is not just because it has access to masses of potential clients, but because the company has mastered the art of tracking and understanding client behaviour, using information gleaned from tons of data.

Google probably knows where you will go on your next holiday before you have made the final decision yourself. Google has seen how many of your friends have been to that destination and how many of their photos you "liked", how many times you have visited sites regarding that destination or priced flights to that destination. The tech giant also knows what restaurants you visit, which hotels you stay in, when you usually travel, and where. Google is even able to determine your risk-taking behaviour by tracking how many times, and by how much, you exceed speed limits, through your use of its GPS on Google Maps.

Take all this, plus the artificial intelligence (AI) it employs to transpose your behaviour over the behaviour of billions of Google users, and it can not only accurately predict what your budget is for that holiday, but even which restaurant you will visit while in Zanzibar. This is what traditional insurers are up against.

As Facebook founder Mark Zuckerberg explains: "People have really gotten comfortable not only sharing more information and different kinds, but more openly and with more people."

NOW WHAT? An important aspect of this Second Information Age is that ownership of data and information is not that important anymore and, in the case of many insurers, could be a drawback in the quest for innovation.

Information should holistically be used for the following purposes:

- **Enhancing the client experience:** Really knowing the client enables a fast take-on/claims process and the ability to accurately price without needing too much information from the client herself.
- **Collaborating with clients to customise the solution:** Trov is a great example of customisation with its "insurance on demand" platform.
- **Effectively communicating with the client to build trust and increase retention:** Lemonade and Friendsurance are great examples of where trust is created.
- **Building a community:** Social media and sharing platforms such as Facebook, Airbnb and Tripadvisor are so successful because they stimulate communication between members/clients within the community and allow them to advise one another. This in turn also increases trust and knowledge about client preferences.
- **Ticket to the game:** Identify the various AI (artificial intelligence) platforms according to your specific needs to access the most suitable "intelligent information".
- **Hygiene factor:** The ability to filter, analyse, draw conclusions and effectively apply, at incredible speed.
- **Competitive edge:** User experience.

Welcome to the Second Information Age, where nothing is secret and everything happens fast. ■

Time of Industrial Revolutions

REVOLUTION	YEAR	CHARACTERISTIC
1st	1784	Steam, Water, Mechanical production
2nd	1870	Division of labour, Electricity, Mass production
3rd	1969	IT, Electronics, Automated Production
4th	?	Cyber-physical Systems

SOURCE: World Economic Forum

Tony van Niekerk is the owner and editor of *Cover Publications*, South Africa's longest-running financial services trade publication.

Y&R1507271

African beginnings Global opportunities

With more than R1.5 trillion* under management, Investec Asset Management has transformed over 25 years from strong roots in Africa, to become a truly global asset manager. We offer a diverse range of investment strategies from global equities, fixed income and multi-asset investment to specialist capabilities in emerging and frontier markets, commodities and resources. While our perspective and presence are global, it is our distinctive African heritage that sets us apart.

For more information, contact your financial advisor, call us on **0860 500 900** or visit **www.investecassetmanagement.com**

Out of the Ordinary®

Investec Asset Management is an authorised financial services provider. *Source: Investec Asset Management as at 31 December 2015.

By Ainsley To

FACING THE UNKNOWN

Algorithms versus human judgment – whom do we trust?

Studies have shown that computers are more efficient and more often correct than humans, yet we still prefer to have a person doing the work. This could pose a problem as asset managers increasingly incorporate computer algorithms into their strategies.

“big data is like teenage sex: everyone talks about it, nobody really knows how to do it, everyone thinks everyone else is doing it, so everyone claims they are doing it.” – Dan Ariely

It has been known for some time that in many environments, simple algorithms (on a far smaller scale than in AlphaGo) can be adequate substitutes for, and in some cases outperform, human decision-making. A 2000 meta-analysis by William Grove *et al* titled *Clinical versus Mechanical Prediction: A Meta-Analysis* highlighted 136 studies across a diverse number of fields (including medical diagnosis, academic performance, and parole success rates amongst others) where there was evidence that a systematic decision-making process can perform the same tasks more accurately by avoiding some of the behavioural pitfalls in human judgment.

A further observation was that the only time that humans performed better was in cases where they had better information than the models. With the deluge of data now available, the human advantage of having better information has been inverted, and we are seeing an increased reliance on the tools we build to interpret and act on new information. In asset management, this has manifested itself in a more prominent distinction between discretionary and systematic strategies.

The problem is that the decision of choosing between a human or an algorithmic strategy has been shown to be biased in its own right. In their appropriately titled 2014 paper *Algorithm Aversion: People Erroneously avoid Algorithms after seeing Them Err,* Berkeley Dietvorst *et al* looked at the decision-making of a number of subjects who were given a choice between relying on a human forecaster or an evidence-based statistical algorithm. There were many facets to the study, with a key finding being that the subjects showed a bias towards human forecasts even when given evidence beforehand that the algorithm did better.

The subjects showed a bias towards human forecasts even when given evidence beforehand that the algorithm did better.

As data analysis is increasingly systematised to accommodate larger datasets, algorithm aversion may pose a number of future problems as well as exacerbating existing difficulties for investors.

Short-termism

A particular quirk of the results in Dietvorst's article is that the subjects' reactions to algorithmic errors were much more unforgiving than when their human counterparts made errors. People are more likely to abandon an algorithm than a person for making the same mistake.

Many of us who have used a GPS system when driving can relate to this – if you run into traffic on the way to work and you decide to take an alternate route but the journey ends up being much longer than if you hadn't, it is highly unlikely you would never again trust your own judgment in a similar situation. But if your traffic-sensitive GPS was the one to suggest an alternative route that ends up taking you longer, you're much more likely to lose confidence in the system going forward.

Performance-chasing and investor short-termism have long been an issue for the industry. As investment strategies become increasingly systematic, the lack of patience regarding algorithms could potentially make the problem worse. All strategies, whether systematic or discretionary, go through periods of underperformance. The challenge is ensuring that the benefits of using algorithms in investing (such as avoiding behavioural biases at the portfolio level) are not offset by bad behaviour at the investor level as markets become more data driven.

Transparency

People are even less likely to use algorithms if transparency makes it obvious that the algorithm will make errors, despite the absolute results being better than a human alternative. This creates a dilemma for intermediaries who use systematic strategies as they may present a

situation where full transparency may not be in clients' best interest if their bias might lead them to worse potential outcomes.

In a 2006 article titled *Do Patients trust Computers?* Marianne Promberger and Jonathan Baron found that patients are less willing to follow a recommendation when they were told it was from an algorithm than when they were told the same recommendation from a physician. They note that this can be partly attributed to an enhanced feeling of responsibility on the part of the subject – they feel they have delegated responsibility when a physician is involved but are still responsible if the recommendation was from a computer.

In his study *Adding your Two Cents May Cost a lot over the Long Term*, Joel Greenblatt of Gotham Capital fame found a great example of this in 2012. Greenblatt's "magic formula" for screening stocks [a combination of enterprise value/earnings before interest and tax (EV/EBIT) and operating return on invested capital (EBIT/IC)] became so popular that he opened his brokerage firm, Formula Investing, in 2009 on the back of client demand.

He gave clients access to his quantitative screening tool utilising his formula but he also gave them two options for using it – they could either follow the algorithm or be allowed to overlay their own discretion on which of the stocks in the screening they wanted to include or exclude.

After two years there were marked differences in performance for the two groups – while his full strategy beat the S&P500 by over 20%, clients who used his formula but combined it with their own judgment returned less than the index. These are examples of how transparency can also cause problems when they run into the common human trait of overconfidence. When faced with an imperfect algorithm that has a known error rate versus our own unknown human error rate, there is a tendency for us to be overconfident in our ability to do better.

Joel Greenblatt
Founder of Gotham Capital

People are even less likely to use algorithms if transparency makes it obvious that the algorithm will make errors, despite the absolute results being better than a human alternative.

Steve Jobs
Late co-founder, chairman and CEO of Apple

Investment dogma

Another subtle problem posed by algorithm aversion is that the use of algorithms is often at the heart of controlled experiments in finance literature. Providing an objective test for the validity of an investment strategy by definition requires that you control for other variables, including discretionary judgment.

For Fama&French to document the long-term evidence that value investing is a profitable strategy, they had to use an objective measure of value (book-to-market in this instance) and implement systematic long/short equity portfolios to control for company size. A disdain of algorithms could lead to a disdain of objective evidence, without which your body of knowledge cannot progress beyond your own blind faith.

Demographics might perhaps play a role in this instance. It is plausible that "digital aliens" who are less comfortable with technology are more likely to suffer from availability bias when faced with a choice between quantitative long-term evidence and qualitative human judgment ("Well actually, I knew a guy who got rich day trading leveraged oil ETFs."). Perhaps until more "digital natives" occupy the investment decision-making process, there will be a persistent overreliance on the most opaque "black box" in investing – the human brain.

As James Grant of *Grant's Interest Rate Observer* once said: "Progress in science is cumulative; we stand on the shoulders of giants. But progress in finance is cyclical; in money and banking, especially, we seem to keep making the same mistakes."

Conclusion

Steve Jobs often quoted a study by S.S. Wilson titled *Bicycle Technology* from the March 1973 issue of *Scientific American*, comparing the efficiency of locomotion for various species on the planet. In the natural world they found that the condor was the most efficient animal in terms of the amount of energy required to travel a kilometre.

Yet the species that had come to dominate the planet, the modern human, was far less efficient than a number of other animals. However, when including artificial systems, top of the list in terms of efficiency was a man on a bicycle – better than the condor and five times more efficient than the human alone.

The brilliance of our species is not in our natural capabilities but in our ability to design tools as extensions of ourselves to adapt to the challenges we face. The computer is the bicycle for the mind. And those on foot may well find that in clinging to their tree of experience, they will miss the forest of knowledge. ■

Ainsley To is an analyst for the multi-asset team at Credo Capital, undertaking cross asset research in asset allocation as well as fund selection.

Gallo Getty Images/iStockphoto

By Daniel Polakow

ACTIVE MANAGEMENT

Information deluge the new normal

Although things have become tougher on the ground for active managers, the fraternity will consolidate in South Africa, with survivors being those who become overtly more scientific in their investment process going forward.

Never in the history of mankind have we had access to as much information flow as we do today. With the advent of global connectedness comes the assumption that more information makes for more efficient markets, better decisions and lower risk. And more efficient markets naturally lead to fairer investing and happier investors (although not always happier fund managers).

But I don't think this is the case currently. I'm going to argue that the environment for active management is getting more difficult, in no small part due to this information deluge, but is also becoming more fraught with risk. I am an advocate of active management, but a form that is entrenched in a framework that calibrates and updates intelligently over time to a changing backdrop, rather than one beholden to any antediluvian paradigm. And it is this type of active management that we anticipate will separate the survivors from the casualties, on average, under these increasingly difficult conditions – and for some time to come.

So, why are things getting progressively tougher on the ground for active managers? The short- to medium-term opportunities in the South African market, across most tradeable asset classes, have for all intents and purposes been trampled. We are witnessing an evolving homogenisation in the way investors, and machines, respond to the same data. Foreign investors are key to the South African puzzle currently and have been becoming increasingly so for many years. There is far more "information", agreed, but the useful "signal" is fading. The ears pointing to such information are, across the board, getting better at listening and responding appropriately.

Understanding cross-sectional volatility

Let's examine the opportunity set manifest in the South African equity market. This entails an understanding of dispersion.

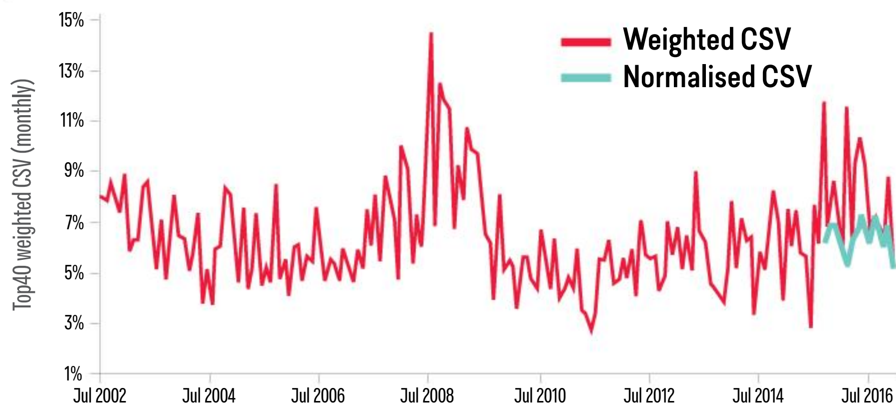
If, over any time period, say a month, Remgro increases by 2% and Bidvest falls by the same amount (-2%), a portfolio manager who was long (or overweight) Remgro and short (or underweight) Bidvest would make a sizeable profit (up to 4% if the bets were of the same size). Conversely, a portfolio manager with the wrong view would make a similarly sized paper loss. The spread between Remgro and Bidvest is what is crucial here.

What if Remgro was up 2% and Bidvest up 1.9%? What if this compression in constituent returns was systematic (i.e. across the market)? So, regardless of the portfolio manager's positioning, profits or losses would all converge to much the same outcome. All managers' performance would start to look the same.

Across equity indices we quantify this spread. We call it cross-sectional volatility (CSV) and it measures the dispersion in the behaviour of the underlying equity constituents. Figure 1 above captures CSV for the Top40 most liquid stocks on the JSE since 2002 to December 2016. The CSV presented here is weighted. We also present the normalised CSV from mid-2015, and I'll talk about that in a little while.

I've heard investment professionals comment that dispersion deflation is of no relevance to them. Much like a cannon ball with your name on it is not concerned about your appreciation of Newtonian physics. How is CSV relevant to active management, you ask? Consider the standard deviation of the active returns of the Large Manager Watch (LMW) domestic equity fund universe for the last decade in Figure 2 on the next page. The y-axis reflects the extent to which managers have been different to each other,

FIGURE 1: EQUITY OPPORTUNITY SET (CSV)



SOURCE: Prescient Securities

Fund managers are delivering active returns that are increasingly similar to each other and the benchmarks around which they are measured – regardless of their skill.

Getty Images/iStock Images

RAGING BULL AWARDS

WE DID IT!
WE'VE WON THIS
5 YEARS
IN A ROW

The Old Mutual Global Equity Fund has won the Raging Bull award for Best (SA-Domiciled) Global Equity General Fund five years in a row. What's more, the fund is currently a top quartile performer over 1 to 21 year investment periods and since inception. Another good reason you should invest where the fund managers invest.

Speak to an Old Mutual Financial Adviser or your broker about investing alongside our fund managers or call 0860 INVEST (468378).

www.oldmutualinvest.com/asinvested

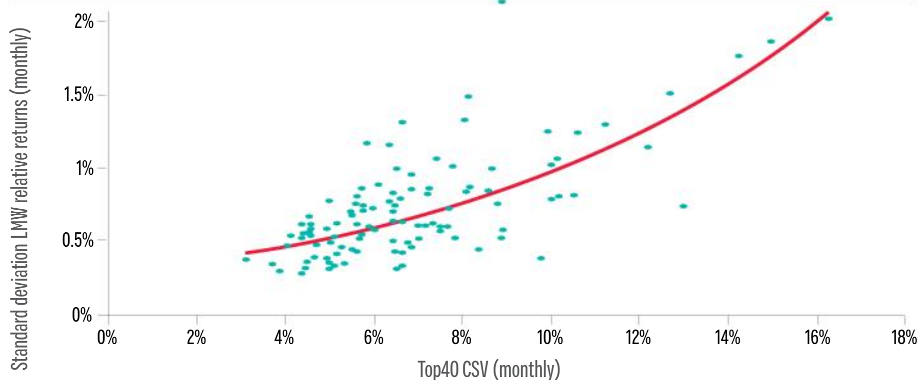
DO GREAT THINGS

OLDMUTUAL
INVESTMENT GROUP

*Global General Equity Category. Source: Morningstar as at 31 December 2016. Inception Date: 17 May 1995.
Old Mutual Investment Group (Pty) Limited (Reg No 1993/003023/07) is a licensed financial services provider, FSP 604, approved by the Registrar of Financial Services Providers (www.fsb.co.za) to provide intermediary services and advice in terms of the Financial Advisory and Intermediary Services Act 37 of 2002. Old Mutual Unit Trust Managers (RF) (Pty) Ltd (OMUT) is a registered manager in terms of the Collective Investment Schemes Control Act 45 of 2002. The fund fees and costs that we charge for managing your investment are accessible on the fund's Minimum Disclosure Document (MDD) or table of fees and charges, both available on our public website, or from our contact centre. Some funds hold assets in foreign countries and therefore may have risks regarding liquidity, the repatriation of funds, political and macro-economic situations, foreign exchange, tax, settlement, and the availability of information. Please contact us for risks specific to each country. The Net Asset Value to Net Asset Value figures are used for the performance calculations. The performance quoted is for a lump sum investment and in respect of the Old Mutual Global Equity Fund. The performance includes income distributions prior to the deduction of taxes and is reinvested on the ex-dividend date. Actual performance may differ as a result of actual initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Past performance is not a guide to future performance. Annualised returns are the weighted average compound growth rate over the performance period measured. The actual highest, average and lowest12-month return figures since inception to 31 December 2016 are 75.0% (highest), 15.6% (average) and -40.3% (lowest). Morningstar and Old Mutual Investment Group calculated the performance of the fund as at 31 December 2016. Old Mutual is a member of the Association for Savings & Investment South Africa (ASISA). Market fluctuations and changes in rates of exchange or taxation may have an effect on the value, price or income of investments. Since the performance of financial markets fluctuates, an investor may not get back the full amount invested. The Raging Bull award was received on 25 January 2017. Full details and the basis for the award are available from Old Mutual Unit Trust Managers.

FCB10022192JB/E

FIGURE 2: LMW FUNDS PERFORMANCE DIFFERENTIALS VS CSV



SOURCES: Prescient Securities and LMW

after the influence of their benchmark has been removed. On the x-axis, we plot CSV.

This relationship is remarkable in terms of its relevance. And it is not limited to equities – the picture for the nominal bond universe is equally compelling, for example. The message is essentially the same across asset classes. Fund managers are delivering active returns that are increasingly similar to each other and the benchmarks around which they are measured – regardless of their skill.

The risk factor

We recently emerged from a protracted deflated CSV backdrop – one that started after the global financial crisis. And against this deflated backdrop, active managers need to take larger active risks to differentiate themselves. It is increasingly understood that thematic rather than fundamental drivers are driving the market in the short and medium term. And so the risks that need to be assumed in the short and medium term are undiversifiable bets on themes. To be clear, these are not risks that will land you in trouble with your investors momentarily. These are the types of bets that will shut businesses down on the back of investor losses, or propel a manager into stardom. Failing to take risks will result in forced mediocrity and herding, to a greater extent than evidenced historically. Dispersion deflation is a terrible homogeniser – it is to the fraternity of active management as the Nutribullet is to kale family vacations.

It is perhaps not surprising that asset consultants, frustrated at the emerging "pull to the median" of their custodian funds' performance, are motivating for bigger bets. Implicit here is the assumption that the odds remain the same and that larger bets can be placed without inefficiencies. But the truth is that bigger bets within our already concentrated South African benchmarks are often impossible without taking undue risk, and also that the odds themselves continue to decrease.

If you look at Figure 1, you might argue that we are again in a medium- to high-CSV backdrop – but you'd be incorrect in assuming this signals a renewed diversified investment opportunity set. If one looks closely at what drives CSV, we find that over the last two decades the drivers of CSV are understandable from both a statistical and macroeconomic perspective. Yet something significant has changed. What we currently find is a mixture of two distinct processes. The first, as per normal, is keeping dispersion subdued. This can readily be attributed to the forces of globalisation and South Africa's positioning in the flow of global capital. This has remained largely invariant since 2013.

The second process is the focus of this article and is more perverse. It is the dramatic rise of concentrated idiosyncratic (i.e. stock specific) risk in the South African equity market. The price action experienced by large-cap single names that are the subject of out-of-the-ordinary news streams are amplified. Examples are SABMiller up 26.7% in September 2015 (corporate action); Anglo American up 65% in February 2016 (restructure); Naspers up 18.3% and MTN down 17.8% in May 2016 (Tencent earning surprise, and Nigerian litigation proceedings, respectively); BHP Billiton and AngloGold up 15% and 14.4% respectively in November 2016 (presumed renewed rotation into resources). These moves are what is accounting for the artificially inflated CSV. These movements are unpredictable and undiversified, and do not signal reprieve for active managers. The normalised CSV depicted in Figure 1 is what actually persists in terms of the local equity investment opportunity set. ■

Daniel Polakow is a director and head of research at Prescient Securities. He is also an associate professor at the University of Cape Town.

THE OUTLOOK

So, how can I conclude that there remains a useful place for "active" in South Africa? Simply put, there are enduring inefficiencies in the South African market – you just need to know where to look, and how best to access and exploit them. Some of these require a stronger quantitative lens or alpha foraging using a wider range of asset classes. Others require a contrarian-termist view or a flair for financial engineering (i.e. derivatives). But the majority simply require an adaptation of conventional investment thinking to be more attuned to the facts above, and the different strengths inherent in one's investment process. If you are an active fund manager, you'll be aiming to understand why some stock picks are unlikely to differentiate you from your peers. And if you want to understand why some risks are not worth taking currently whereas others are, you will need to better align your placement of active risk (what we term "risk-budgeting") with the empirical reality in the markets.

The lethargy that characterises a large proportion of the active fund management fraternity indicates that most have not fully come to terms with the new norm. My contention is that the active fraternity will consolidate in South Africa, with survivors being those who become overtly more scientific in their investment process going forward. It's disingenuous for investment professionals to believe that what worked previously will work yet again. And that's not just my point of view – it's become patently obvious in the numbers. ■

By Dan diBartolomeo

INVESTMENT STRATEGIES

Big data in investment finance: A cautionary comment

Beware the pitfalls of using big data to predict the future.

The investment industry has quickly embraced the concept of "big data" as the next way in which professional investment managers will gain advantage both over their peers, and over purportedly less sophisticated investors. Certainly there have been some investment entities – such as the Renaissance organisation – that have achieved great success by supposedly recognising patterns in the flow of events within, and exogenous to, financial markets.

On the other hand, many organisations that have based strategies on the big data concept have dramatically underperformed expectations. For example, on 9 January Bloomberg News carried a story reporting the poor 2016 performance of the various funds managed by the BlackRock "Scientific Active Equity" group. According to the article, "SAE is made up of more than 90 investment professionals, including 28 PhDs and numerous data scientists".

Unlike physical sciences, finance is "hand of Man, not hand of God". The geopolitical, economic and regulatory circumstances that impact financial markets change daily, sometimes in small and benign ways, but sometimes in profound ways. Those circumstances, known and unknown, exert a powerful impact on the usefulness of the assumption that statistical patterns when observed carry material meaning. It would seem useful to recall this quotation from the play *The Doctor's Dilemma*, written by George Bernard Shaw:

Images: Supplied Getty Images/iStock Images

Even trained statisticians often fail to appreciate the extent to which statistics are vitiated by the unrecorded assumptions of their interpreters... It is easy to prove that the wearing of tall hats and the carrying of umbrellas enlarges the chest, prolongs life and confers comparative immunity from disease. A university degree, a daily bath, the owning of thirty pairs of trousers, a knowledge of Wagner's music, a pew in church, anything, in short, that implies more means and better nurture... can be statistically palmed off as a magic spell conferring all sorts of privileges... The mathematician whose correlations would fill a Newton with admiration, may, in collecting and accepting data and drawing conclusions from them fall into quite crude errors by just such popular oversights as I have been describing.

False positive bias

Beyond simply using big data techniques to uncover new information of potential usefulness, investment practitioners then routinely evaluate the strategic importance of such information through investment simulations known as "back-tests". Unfortunately, this is where the investment research process based on big data goes awry, as these simulation tests are deeply biased so as to offer "false positive" outcomes in a preponderance of cases.

The problem of "false positive bias" exists not only when big data is involved, and not only when addressing financial markets. Scientific and professional journals in all fields are supposed to be rigorous in vetting scientific claims. But if 50 teams of medical researchers study a given issue, and two studies claim to have found the same important result, those two studies will be published, as they confirm each other. *The fact that 48 teams of comparable researchers did not find this result goes unpublished and unnoticed.*

In asset management, strategies have been driven by either the human business judgment of fundamental investors, or the statistically driven results of quantitative investors. Traditionally, quantitative strategies have been based on hypotheses grounded in fundamental concepts. So too can many big data strategies be grounded in fundamental concepts. For example, if we use satellite imagery available on the internet to count the number of vehicles in the parking lot of a large retail store, this could be very valuable in making a forecast of the store sales.

On the other hand, strategies could be based solely on the fact that we can use powerful computers to find

patterns in large data sets that have hopefully gone unnoticed by others. When we formulate strategies based purely on big data, the process of validating the usefulness of a strategy must be dramatically more rigorous than when large data sets are being employed to more efficiently implement what is otherwise a theoretically and intuitively appealing investment thesis.

If anyone tells you to believe the results from a conventional back-test, they are a liar, a fool or both. Three key research studies have shown that investment models that appear valid and likely to be successful can be constructed from entirely random information that is known in advance to have no predictive ability.

In their seminal research study, David Bailey *et al* define a back-test as "a historical simulation of an algorithmic investment strategy". Their paper was aptly titled *Pseudo-Mathematics and Financial Charlatanism* (*Notices of the American Mathematical Society*, 2012).

Other studies such as *Random Matrix Theory and Financial Correlations* by Lourent Laloux *et al* (*Mathematical Models and Applied Sciences*, 2000) and *Testing strategies based on Multiple Signals* by Robert Novy-Marx (2016) (http://bit.ly/2jzeOIx) confirm the potential for valid-looking models to be created out of meaningless random data.

Back-testing

The whole concept of back-testing rests on the idea that history can be our guide to the future. There are extreme assumptions that the passage of time in financial markets is such that the range of events that might happen is the same as the range of events that has happened. In their article *Does Historical Performance Predict Future Performance?* (*Financial Analyst Journal*, 1995) Ronald Kahn and Andrew Rudd show that this is a very weak assumption.

Almost all back-tests are look-ahead biased either in raw data or strategic concepts. Implicitly we are saying: "If I knew then what I know now, we would have performed well." In his book, *A Brief History of Time*, the physicist Stephen Hawking said that one of the proofs that time only goes forward is that "otherwise, we could invent a computer that would report tomorrow's stock prices". Look-ahead bias in "data snooping" exercises can be substantially reduced by using databases that provide "point-in-time data" so you are seeing information (e.g. company financial statements) as they would have been at the time.

Simulations assume that a given financial market participant could have traded without any alteration in the course of past events. Given that every buyer must have a seller and vice versa, this idea is just silly. It is doubly silly for large institutions that must do large transactions that will create obvious changes in the balance between supply and demand for a particular financial asset.

Most quantitative models for investment management rely on a series of parameters to formulate return expectations or do portfolio construction tasks. With the widespread availability of cheap computer power, there is an overwhelming urge to carry out many tests so as to find the best combination of the parameters. It is much like the process of "conspiracy theory" where putting together unrelated facts in the right way seems to offer a coherent explanation of events. Carried to an extreme, this process is often automated as "machine learning".

Ronald N. Kahn
Global head of Scientific Equity Research at BlackRock

Investment models that appear valid and likely to be successful can be constructed from entirely random information that is known in advance to have no predictive ability.

Andrew Rudd
Former CEO of Barra

Conventional simulation tests have extremely low statistical power. Most tests simulate over the history that was actually experienced. There is rarely any testing of how a strategy would have done over the infinite number of other paths the evolution of history might have taken. There is no context to judge whether the sequence of events that we lived through was typical or improbable. In *Three Classic Errors in Statistics, from Baseball to Investment Research*, Ronald Kahn (*Financial Analyst Journal*, 1997) offers some excellent examples of how low probability events are routinely misinterpreted. For example, at first glance it might seem extremely rare that someone would win a large lottery prize repeatedly. However, when you consider how many people have already won large prizes, and the large amount they can afford to spend buying more lottery tickets, this seemingly extreme event is seen to be expected.

Most investment models have multiple parameters. The greater the number of parameters, the larger the testing period must be to validate the process. Usually, the required amount of history is simply non-existent. Alternatively, we can revise upward our requirements for statistical significance in considering simulated results to reflect the number of alternative parameter specifications we have tried, as in Campbell Harvey and Yan Liu's 2013 article *Backtesting* (http://bit.ly/2kuXDHz).

A very useful reality check on expectations derived from simulations was provided by Leigh Sneddon in *The Tortoise and the Hare: Portfolio Dynamics for Active Managers* (*Journal of Investing*, 2008). This technique provides a way to analytically forecast the long-term performance (alpha, Sharpe ratio, etc.) of a strategy conditional on the forecasting power (IC) of the "signal". Given whatever you believe your information coefficient will be, the long-term performance is predictable given certain assumptions.

We are still in the early days of the application of big data to investment decision-making. Much can be done to sensibly "supervise" the automated analytical processes that seek to find advantage in big data with respect to financial markets. If strategies based on the insights provided by big data are to succeed, the level of rigour being applied to evaluation of in-sample and simulated out of sample results must be far higher than today's common practice. ■

Dan diBartolomeo is president and founder of Boston-based Northfield Information Services, Inc., which develops quantitative models of financial markets. diBartolomeo, a visiting professor at Brunel University, has published more than 30 books, book chapters and research journal articles.

By Hannes Viljoen

CONCLUSION

Beware the noise

How should investors navigate the dramatic increase in the flow of information? What is important and what isn't?

What is the one thing that investor Warren Buffett and Chinese President Xi Jinping have in common? They always keep their eye on the long-term goal and avoid making rash decisions based on short-term information.

Buffett tells the story of a farm that he bought north of Omaha in 1986. He bought the farm for a "cheap" price, below what a failed bank had lent against the farm a few years earlier. Some 30 years later the farm tripled its earnings and has increased in value considerably. Buffett still owns the farm and in an interview with CNBC he said that if someone had shown him a daily price on the farm, as is the case with any listed stock, he might have done something stupid, like sell the farm, and missed out on the considerable profit he has made over the long term. His advice: "Ignore the chatter [...] and invest in stocks as you would in a farm."

Think long-term investing

Every five years the People's Republic of China releases a new five-year plan. The current plan runs from 2016 to 2020 and contains goals that the country aim to achieve over the five-year period. It has been rumoured President Jinping keeps a summary of the main goals with him. Whenever he needs to make an important decision he takes out the summary in order to remind himself what the country's goals are, and makes the decision accordingly. What we can learn from him is that if you keep the end goal in mind it will minimise the risk of making rash short-term decisions.

In November 2016, the number of Google searches per second was roughly **2.3m.**

Information and data have become more readily available as time has gone by. According to an article released by DMR (expandedramblings.com), in November 2016, the number of Google searches per second was roughly 2.3m.

As the availability of information has increased, the average holding period of stocks actually decreased. US Senator Mark Warner recently stated in an interview: "The average time someone used to hold a share or stock back in the 60s was eight years. Now, the average time is four months."

Moneyweb, one of South Africa's business, financial and investment websites, published 12 070 articles in 2016 alone. So is all this data valuable information or just additional noise?

Nate Silver, author of *The New York Times* bestseller *The Signal and the Noise*, said "noise is what distracts us from the truth". This is particularly relevant in the investment arena and could be rephrased as "noise is what influences our emotions to perceive information as having a long-term impact on financial markets when it in fact does not".

How do you navigate through all this information and data? How do you make sure your emotions don't get the better of you and result in rash, often wrong, investment decisions?

Generally, there are three ways in which to invest. The first, doing it yourself, the second via an asset manager and the third with the aid of a financial adviser.

As a personal investor, the temptation to succumb to market noise is arguably the greatest. Behavioural finance suggests that it takes disciplined people to take on this pursuit on their own.

Investing via an asset manager transfers some of the short-term decision-making risk to a hopefully experienced team of professionals. There is however still risk of chasing short-term performance through regularly switching between managers, an exercise that has been shown to actually destroy value.

Investing with the aid of a reputable financial adviser allows you to interact with someone who can act as a gatekeeper, someone who can calm fears in times of market turmoil and help you keep your eye on the long-term goal.

Whichever avenue you choose there are certain steps you can follow that will keep you focused and help you avoid making emotional investment decisions:

SET YOUR GOAL, DEVISE A STRATEGY AND STICK TO IT. The goal can be long term for retirement purposes, medium term in saving for your children's education or even saving for short-term unexpected expenses. Either way, once a strategy is determined there will be very few market events that should alter that strategy.

Always ask yourself: "Does this piece of information warrant a change to my strategy in order to reach my goal?" A reduction in interest rates should not affect your strategy, so too the expected GDP growth rate or the price of petrol. If goals change, so should the strategy, rarely otherwise.

FOCUS ON WHAT YOU CAN CONTROL. You can control the asset allocation of your strategy, the managers selected to manage funds, your financial adviser and even security selection if you manage your own portfolio. Focus on what is controllable and make sure they are incorporated in your strategy correctly.

You can't control the actions of an asset manager, the outcome of the US presidential election or the interest rate decisions of the South African Reserve Bank. Devise a strategy and stick to it.

CONSIDER SEEKING THE GUIDANCE OF A FINANCIAL ADVISER. We seek the help of a doctor when we are sick, however, when it comes to investments – and in particular when we save for retirement – we need to engage with a professional before we get sick.

If we tend to retirement issues when we turn 60 or 65 it usually is too late and the patient is often terminally ill by then.

REALISE THAT THE MAJORITY OF INFORMATION IS ENTERTAINMENT, NOT DATA. There is nothing wrong with keeping up to date with what is currently going on in the world, however this news is often short term, and some events may stir up emotions. Such events should not change your strategy in order to reach your goal, short or long term. Keep an open mind and distinguish entertainment from useful information.

In conclusion, when a piece of information triggers an emotion that inclines you to think about buying or selling, recognise that such an emotion was triggered. Remind yourself of your goal and the strategy that was set in place to reach that goal. And if the status quo has not changed, sit back, enjoy the entertainment, and leave the farm be. ■

Hannes Viljoen, CFA, CFP, is a senior manager in the technical solutions team at Investment Solutions.

By Natalie Greve

GOVERNMENT DIRTY WITH REN

Research by the Council for Scientific and Industrial Research (CSIR) shows that renewable energ water intensive and less polluting – yet government's proposed long-term energy strategy for th of energy generation.

While global energy planners increasingly turn to progressive sources of renewable energy (RE) to satiate energy demand, South Africa's department of energy (DoE) appears inexplicably reluctant to enhance the volume of RE in the country's energy mix.

As the DoE continues the development of the Integrated Resource Plan (IRP) – the country's overarching long-term energy plan – an alarming assertion has been made by Dr Tobias Bischof-Niemz, head of the Council for Scientific and Industrial Research's (CSIR's) Energy Centre.

Bischof-Niemz, who was both a member of the Ministerial Advisory Council on Energy as well as a member of the team that designed the IRP 2010/2013 for Eskom, appears puzzled at the department's apparent reluctance to lift seemingly superfluous limits to the volume of RE that can be added to the national energy mix on an annual basis.

Furthermore, the department seems to be overlooking substantive evidence demonstrating that increasing the amount of RE into the long-term energy plan will significantly drive down energy development and running costs.

Such a claim, made by the head of a state-funded research and technological innovation body intricately involved in the design of the IRP, raises critical questions about government's energy policy motivations.

Addressing the civil society cohort during a workshop at public interest law firm Section27 last month, Bischof-Niemz explained that the IRP updated base case, released in November last year, includes a self-imposed limitation on the amount of wind and solar photovoltaic-(PV-) generated energy that can be built and added to the grid on a yearly basis.

The annual build constraints for new capacity for wind are set at 1 600 megawatt (MW) and solar PV at 1 000MW, while no other technology is limited.

"There is no technical explanation given for the limits to renewables and the limits don't grow as the grid grows. For example, according to the IRP

Dr Tobias Bischof-Niemz
Head of the CSIR's Energy Centre

Crescent Mushwana
Principal engineer at the CSIR

Photovoltaic panels in the Sishen solar park, operated by Acciona SA, in Kathu, in the Northern Cape.

T PLAYS
EWABLES

gy is a feasible option for South Africa – being cheaper, less
e most part snubs renewables for nuclear and other forms

base case, in 2020, renewables will comprise 2% of the grid, dropping to 1.2% in 2050, so our ability to add renewables over time actually decreases.

"There is no explanation as to why there is a limit and why the limit decreases in relative terms. There is no policy decision that imposes limits, which were put in place by the IRP design team that sits in the DoE. We just can't figure out why the limit is in place," he opines.

> "There is no scientific doubt that solar PV and wind is the cheapest new-build mix for the SA power system."

CSIR principal engineer Crescent Mushwana added that the news of the limitation on renewables came as a "shock" to him.

"I've worked in Eskom and, from studies, there is no justification for the limits. If you look at the document as it stands, there is no explanation," he said.

Solar PV penetration in countries leading the global RE charge is 2.5 times that of SA's plan for 2050, while wind penetration in these countries is almost twice that of SA's plan for 2050.

The South African Renewable Energy Council (Sarec) adds that the DoE has given "no single rational explanation" for the constraint on the allocation of solar and wind technologies.

"As Sarec, we have found that neither the DoE nor Eskom want to engage in an open way on this issue despite many requests from many different stakeholders. We can only hope that they feel obliged to do so through the IRP public participation process," the body states.

Least-cost scenario

Bischof-Niemz and Mushwana's positions are premised on a wind and solar PV resource aggregation study in which the CSIR lifted the limits on renewables and simulated the energy-generation capabilities of a hypothetical renewable generation fleet. The costs in the model included all capacity-related costs, such as capital expenditure, operational and maintenance costs, as well as fuel.

Government's draft IRP base case for 2050, which is based on 30% coal, 32% nuclear and around 27% hydropower and renewables would cost R580bn a year, emit 200m tons a year of CO^2 by 2050 and would require 40bn litres of water a year.

The draft IRP carbon budget, which outlines a larger proportion of nuclear power and assumes a 33% renewables mix, would also cost R580bn a year, but emit 100m tons a year of CO_2 and require 16bn litres of water a year.

"It would also make South Africa's nuclear fleet one of the largest in the world, surpassed only by France," remarked Bischof-Niemz.

In contrast, the CSIR's reoptimised model, which was designed with a tool used by energy systems design operators "around the world", puts solar PV at 25% of the energy mix, wind at 54% and the remainder from natural gas. It would cost R490bn a year, emit 70m tons a year of CO_2 by 2050, and use 11bn litres of water a year.

"The results show that the least-cost model is the CSIR case, which is largely based on solar PV and wind. The reoptimisation scenario is R70bn cheaper by 2050 than the current IRP base case. We asked the DoE for what their results were when they lifted the RE limits and they came to the same conclusion as us.

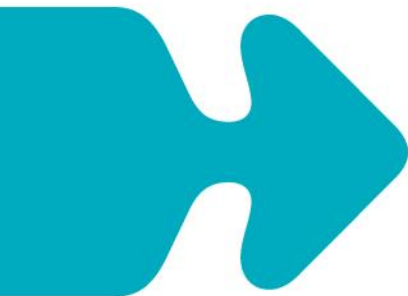
"There is no scientific doubt that solar PV and wind is the cheapest new-build mix for the SA power system," Bischof-Niemz contended.

Hasty opposition

Firing back, the DoE has accused critics of its IRP base case of premature disapproval.

Speaking to *finweek*, DoE chief director of electricity Jacob Mbele says the plan is currently in its consultative and design phase, and is far from being finalised.

According to an irate Mbele, the constraints on RE were first introduced in the original draft



IRP in 2010. At the time, while RE penetration was accelerating on a global scale, it remained a relatively unutilised energy source in SA.

During a later policy adjustment phase, a decision was taken to maintain the limitations in order to allow SA to meet its greenhouse gas emission reduction targets.

While adamant that these maximum RE thresholds may, during later iterations of the plan, be lifted, Mbele fails to adequately clarify why they were retained in the first place.

The 2016 draft IRP currently in the public domain is based on several assumptions that may be amended following the ongoing public consultation phase, which ends on 31 March, he holds.

"If you go through this process without consultation, and you only consult with the final product, it causes confusion, because when you want to discuss the plan, people are still questioning the assumptions that led to the plan.

"We have not made a decision [on renewables]. The base case is one of the scenarios. There has not been a decision to maintain the limitations. We've maintained them in the [2016] base case because they were there in 2010. So we're not saying that it's right [the plan]. At this point, it's not about the correctness of the plan, but the ability of the plan to adapt and that your assumptions can change. We cannot argue about the plan when there is no plan on table," he contends.

The department plans to update the draft IRP base case with inputs from the consultation phase and expects to deliver a balanced scenario IRP plan by the end of August.

The capacity question

While resolute that the RE limitations may yet be lifted, Mbele maintains the DoE and Eskom's long-held position that grid capacity constraints are hampering the connection of renewables to the grid and that RE remains inherently unreliable and unstable.

Noting that the current debate should focus on solving grid restraint issues rather than RE policy constraints, he reiterates that the lack of adequate connection points at which to connect isolated RE projects to the grid must be taken into account during the energy planning process.

"We have to look at issues of grid constraints which are preventing good power projects from coming through. A simple transmission line can take between five and 10 years to develop, because of the paperwork, and land owners saying 'not in my backyard', which forces us into a process of land expropriation.

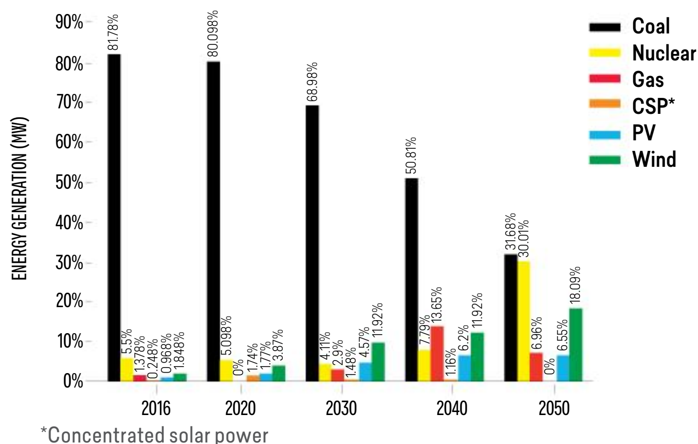
"Lines that have been planned for years are not even on the ground. Not because of Eskom's doing, but because land owners don't want to give servitude. So those are some of the considerations when we talk about grid constraints," Mbele says.

But Bischof-Niemz said that there was no scientific study in place to substantiate government's claim of grid constraints or that renewables were an unreliable source of energy, particularly for SA's industrial base.

"The stability claims can be made, but then you need to be very specific about what you mean and there is no study to support this assertion. We feel that no limit can be implemented without a study.

"Government's argument that it cannot maintain and build an industrial base on renewables is incorrect, as a certain mine isn't powered by a certain energy source, such as a wind farm – the energy is aggregated," he argued.

PROJECTED PERCENTAGE OF ENERGY MIX ACCORDING TO THE DEPARTMENT OF ENERGY'S BASE CASE SCENARIO



SOURCE: Department of energy's Integrated Resource Plan Update of November 2016

Eskom's headquarters at Megawatt Park in Johannesburg.

Images: Supplied Getty Images/Waldo Swiegers/Bloomberg Gallo Images/Mail & Guardian/Madelene Cronjé Gallo Images/Beeld/Denvor de Wee

There was no scientific study in place to substantiate government's claim of grid constraints or that renewables were an unreliable source of energy, particularly for SA's industrial base.

Sarec adds that the DoE's position that the constraints are prudent owing to grid constraints in the Northern and Eastern Cape are unfounded.

A "cursory" analysis of Eskom's Generation Connection Capacity Assessment for 2022 would indicate that there is currently more than 70 gigawatt (GW) of connection capacity around the country.

"And then Eskom's interim CEO, Matshela Koko, says that a system with 150GW (actually the IRP least-cost unconstrained scenario calculates that we need to construct 110GW by 2050) of variable RE generation can never be stable. Practical experience in Ireland, Spain and California would indicate the complete opposite," states the council.

The nuclear factor

So what could government's motivation be for apparently snubbing RE in favour of more traditional, costlier and less environmentally friendly energy sources? Sarec believes the answer lies in the DoE's highly-criticised nuclear energy programme.

"Sarec's position is that the only reason that an artificial constraint has been placed on renewable energy is to allow for the related artificial insertion of 20GW of nuclear power. There is no policy framework that supports the RE limit and it is due instead to a political intervention on what is supposed to be a purely techno-economic process," it asserts.

Mail & Guardian reported last month that Eskom's stalling on signing government-brokered deals to buy renewable energy from private producers, encouraged to develop capacity after outages over the past eight years, could hobble the country's industrial base. It also puts an estimated 15 000 possible jobs at risk.

The energy utility refused to sign power purchase agreements (PPAs) with 37 preferred renewable power bidders, all of which fell within the pre-construction phase after a duly fulfilled government-led renewable energy independent power producer procurement programme (REIPPPP). The energy project has secured nearly R200bn in investment thus far.

"Such non-compliance with duly undertaken power procurement has consequences beyond the RE industry, in that side-stepping policy introduces risk for other IPPs currently preparing to bid for the DoE's already issued or forthcoming requests for proposals," Sarec said at the time.

In a legal opinion letter, senior counsel at law firm Webber Wentzel confirm that preferred bidders are entitled to approach a court to enforce Eskom's signing of PPAs.

"In our opinion, Eskom cannot sidestep the binding determination of the [energy] minister [Tina Joemat-Pettersson]; they are bound by the Ministerial determination, which includes signing the PPA," stated Advocate David Unterhalter.

"The only reason that an artificial constraint has been placed on renewable energy is to allow for the related artificial insertion of 20GW of nuclear power."

Legal opinion further confirmed that ministerial determinations were binding on Eskom and that the utility has no discretion to impose further conditions on preferred bidders.

Eskom's reticence over renewables contrasts with its enthusiasm to find bidders for nuclear plants, which some claim has a nefarious political undertone, driven by President Jacob Zuma.

Sarec further suggests that a desire by Eskom to maintain its hegemony over the South African electricity supply industry and renewable energy could be behind government's apparent distaste for RE.

"The least-cost unconstrained scenario of the IRP would see [Eskom's] share of the South African generation fleet fall to 6% by 2050, whereas the DoE's proposed base case scenario allows it to maintain 61% ownership.

"In addition, acceptance of the least-cost unconstrained scenario would essentially accelerate the logic of the restructuring of the South African energy supply industry and the ultimate demise of Eskom's vertically integrated monopoly model," it points out. ■

editorial@finweek.co.za

Matshela Koko
Acting CEO of Eskom

Tina Joemat-Pettersson
Minister of energy

David Unterhalter
Advocate at Webber Wentzel

MINING ON THE

Commodity prices have been recovering, restoring investor confidence in the mining sector. Will South African miners also benefit?

It's time to revisit the investment clock, the diagram reproduced by Investec Securities and printed by *finweek* in the 4 August 2016 issue to show how the mining market was nearing 4PM – that time on the dial representing the end of the slump in the mining cycle (*Tide could be turning for mining – or not*).

According to the bank, time has flown and we're somewhere around 5PM, which is the point just before the mining market moves into boom again.

Metal prices have stabilised, the industry is recapitalised, debt has fallen, and there's that start of merger and acquisition (M&A) activity; at least, in the gold market.

With a boom, at 6PM, come cash takeovers to be followed by new flotations and rising exploration which, sadly, prefaces a new period of rising debt... And we all know what happened the last time the mining sector became heavily indebted.

Said Investec: "Whilst we have seen all the signs that signal a mood of cautious buying, we believe the mining market overall has not yet had sufficient encouragement to signal a move to blanket buying."

But the feel-good factor is back.

"I have spent more time talking to international investors wanting exposure to JSE-listed companies in last six months than in quite a while," said Tim Clark, head of the diversified mining team at Standard Bank's SBG Securities.

"We think that some prices of the bulk commodities [coking coal] and some of the less liquid markets [manganese] have risen to a point where they are a little bit high. So we have some downside from the current levels," said Clark. "But in aggregate, we are positive." He thinks prices will rise for base metals, energy, and bulk products, and even platinum group metals (PGMs), which are forecast to revive around 2018.

The recovery in iron ore prices has been spectacular. Once languishing around $40/t in 2016, the price is now double that at the time of writing, a 180° turnaround that means most, if not all, iron ore producers are making money again when 30% were underwater last year.

The factor behind the improvement is inevitably China, where GDP growth has stabilised following an increase in 1998 from 7% to 14% annual growth in 2007. Growth plummeted with the world economic and financial crisis, but regained ground reaching double-digit figures by 2010. It then slid again to 7% in 2015. Throughout much of 2016, China's economy grew at "only" 6.7%.

"For the first time in years, there is a mood of cautious optimism in the mining industry with commodity prices on the rise, shallow growth returning to different end-markets, and most mining companies in a better cost position than in the recent past," said Deloitte in its 2017 mining report.

So where are South African mining firms in this recovery? Well, it might be worth dwelling on where they were during the so-called down-cycle. Surprisingly, SA Mining Inc. should have been better off than most during the metal and mineral

INVESTEC MINING CLOCK

1997, 2008, 2011, 2016
Government raises taxes
CRASH
Aggressive selling
Initial shock
New flotations – large
Cost-cutting
Paper takeovers
Company liquidations
Dividends cut
Asset write-downs
Debt rises
Credit agencies downgrade
SELL
LOOK
BUY
Metal prices stabilise
Recap of industry
Rising exploration
Debt falls
Cautious buying
M&A
New flotations – small
BOOM
Cash takeovers
2004-2007, 2010-2011

Timeline so far
12 to 1 o'clock: Oct 2011 - Apr 2015
1 to 2 o'clock: Apr 2015 - Aug 2015
2 to 3 o'clock: Aug 2015 - Sep 2015
3 to 4 o'clock: Sep 2015 - Apr 2016
4 to 5 o'clock: Apr 2016 - Oct 2016

SOURCE: Clock concept courtesy of Lion Selection Group

The recovery in iron ore prices has been spectacular. Once languishing around $40/t in 2016, the price is now double that at the time of writing, a 180° turnaround.

Tim Clark
Head of diversified mining at Standard Bank's SBG Securities

Image: Supplied

UP

By David McKay

price lows owing to the weakening profile of the rand against the dollar.

SBG research shows that in the past five years, metal prices in rand increased while they plummeted globally. For instance, the price of coal is 36% higher since December 2011 to December 2016 whereas it is 20% weaker in dollar. Only iron ore has weakened in rand – down 10% – over that time while platinum is 14% higher compared to a 33% weakening in dollar.

The Chamber of Mines has long lamented the increase in administrated costs such as electricity, falling productivity, the rising wage bill, and obfuscating mining policies as key factors why SA mining was, generally speaking, underwater during 2016.

So while the Investec clock is a helpful device, it doesn't quite chime with SA conditions.

As Deloitte's Andrew Lane observed: "Governments of resource-rich countries are grappling with the issue of how to equitably distribute the returns from their resource endowments to investors, governments and communities."

That's putting it politely given the lack of clarity over the mining charter and the Mineral and Petroleum Resources Development Act, the mining sector's centrepiece legislation, as well as overzealous safety shut-downs and corruption. Lane does add: "There are no simple answers to this."

But Clark insists SA's local problems are simply one piece of a global puzzle in which politics has become more volatile. "There has been a lot of investor interest in SA," he said. "The normal issues that you get around the world are questions that are being asked about SA investor interest such as whether mining firms can retain their mining licences. Hopefully, we will get some regulatory certainty over time, but we do tend to beat ourselves up a bit," he said. ■

editorial@finweek.co.za

Lonmin stumbles once more

Ben Magara
CEO of Lonmin

The platinum miner hopes for higher prices as it faces operational challenges and a cash crunch.

Red flags are being raised over Lonmin's ability to avoid leaking cash notwithstanding a restructuring in which 6 000 jobs – about 15% of its workforce – were shed last year, and hundreds of millions in rand cut from its capital expenditure bill.

This is the platinum mining company that required a $407m recapitalisation at the end of 2015 by means of a rights issue which was eventually supported by the Public Investment Corporation (PIC), principally in an effort to save the jobs of some 30 000 workers employed in Rustenburg.

According to Christopher Nicholson, an analyst for RMB Morgan Stanley, Lonmin recently unveiled additional plans to improve its business – described as a desperate attempt to "pull on every last lever", but each with a negative consequence.

He commented: "Lonmin remains in a difficult position – struggling with operational underperformance and deeply free cash flow (FCF) negative after capex. Management highlighted various remedial actions; however, each comes with a potential negative consequence, in our view."

Lonmin CEO Ben Magara said in a commentary to the firm's fourth quarter operating numbers that restructuring efforts at its Rustenburg premises hadn't been as successful as planned, a setback exacerbated by heavy absenteeism over the year-end holiday period.

In an effort to counter absenteeism, Lonmin is to rehire about 500 contract workers at affected areas, but while this will help keep Lonmin on track for its output guidance of between 650 000 and 680 000 ounces, it will be a stretch to hit its cost targets.

Magara – who mysteriously pulled out of the Mining Indaba conference held in Cape Town early in February – also said the company would revisit the firm's capital projects with a view to cutting budgets. While this would preserve some cash – cash on hand fell $124m to $49m in the first quarter of its financial year – production would be affected in about 18 to 24 months.

Another remedial measure unveiled by Magara was to redeploy certain mining crews from developing activities to mining activities over a period of some six to 10 months. While Lonmin has roughly 22 months of immediately available ores, such a measure would negatively affect its future mining flexibility.

The upshot is that Lonmin's Magara is in survival mode in the hope that platinum group metal (PGM) prices revive. Ironically, Lonmin's measures may be a positive contributing factor in this regard as its output is expected to fall.

Nicholson said that Lonmin's business plan reflects volumes falling to below 600 000 ounces in 2019 from 669 000 ounces in concentrate now. "The longer spot market prices persist, the greater the downside risk to this plan, in our view. This is broadly positive for the platinum market balance," he said.

René Hochreiter, an analyst for Noah Capital Markets, is more positive on Lonmin, saying in a recent report that the next three quarters will always be better than the first, which is traditionally affected by the holiday downtime.

"COO Ben Moolman [together with Ben Magara and Mike da Costa, executive vice-president of business support] is responsible for an incredible revival in the efficiencies of Lonmin in FY 2016," said Hochreiter, adding that the rights issue of 2015 was not a necessity but had been a function of effective "blackmailing" by the banks. He acknowledged, however, that Lonmin's cash cost target of some R900 per tonne was unlikely to be met for the year, having already registered R1 350/t in the first quarter.

Said JP Morgan Cazenove in a recent report: "Lonmin's balance sheet is currently comfortable [...] Yet at current PGM prices we estimate net debt rises to $28m and $261m in the 2017 and 2018 financial years and estimate negative ebitda [earnings before interest, tax, depreciation and amortisation] in both years." ■

on the money

THIS WEEK:

>> Personal finance: Insuring your student child's valuables p.42
>> Technology: Publishers take on Amazon over e-books p.43
>> Management: Making the most of the first 100 days in a new job p.44

ENTREPRENEUR PROFILE

By Charlie Mathews and Jon Pienaar

Shwe's fashion revolution

Julia Franco's social enterprise has reinvented her life and taught her about the meaning of money, work, community and fashion.

Once upon a time, 33-year-old Julia Franco studied fashion in Milan and had a dream job working for the Italian icon Roberto Cavalli. These days you will find her working to disrupt the fashion industry alongside refugees in Durban under a new socially conscious label called Shwe.

"I think that fashion can make a strong political statement, and that's how Shwe started," Franco says, adding: "It is not really about what we make, but how we make it. I try to use Shwe as a statement that asks why so many people are excluded from fashion when they shouldn't be. Everyone dresses themselves and has the right to express and communicate. Everyone should be integrated into and represented in fashion, because everyone has a voice."

Franco first encountered traditional African seshweshwe (also written as seshoeshoe) fabric when she followed her boyfriend from Italy to South Africa, just under five years ago. It was love at first sight, and the diversity of patterns and colours inspired her to craft a new place for herself in the world of fashion.

"When I first arrived in SA, I started to look for a place to fit in," Franco explains. She had a lot of opportunities with a local retailer, but decided against it "because of what cut-rate retail clothing is doing to the industry".

A sociologist friend introduced her to some social justice organisations in Durban that assist refugees and the destitute, and Franco's path became clearer.

The Wearable Library: Shwe is a social enterprise that gives voice to Franco's philosophy that fashion is a form of communication. Each garment has a tag that tells the story of the person who made it. Currently some 64 people are employed at one of a handful of Shwe's hubs in Durban's city centre.

"I arrived at the Denis Hurley Centre in Durban with fabric and we started straight away, and I became a part of the sewing group. I learnt to sew with the group by taking a three-month course with them. It was a very interesting and humbling experience," she says.

Julia Franco
Social entrepreneur and founder of Shwe

Currently some **64** people are employed at one of a handful of Shwe's hubs in Durban's city centre.

Situated at the Emmanuel Cathedral in Durban's inner city, the Denis Hurley Centre acts as a refugee reception for people who travel to SA to escape poverty, violence or political instability. The centre runs a number of programmes to support refugees, including a clinic, training programmes and an employment agency that tries to secure jobs for them.

Getting started

It took a year to set the social enterprise up, and on 1 December 2015, Franco opened an e-commerce site at thewearablelibrary.com. "We had just one sample of each garment, and it took another two months to set up a production flow of sorts," she explains.

Six months later the social entrepreneur travelled to the UK to get support for the initiative. Trips to the US and Brazil followed. Today Shwe has a range of women's clothing that retails in boutiques in Europe, the US and Brazil.

Franco shares her Italian fashion experience, and ensures that the garments are fit for global sale. In keeping with her socially conscious approach, Franco insisted from the outset that the seamstresses be paid a good living wage. Payment is made on a per-item basis, so those who put in a full day's work can maximise their earnings, while some refugees prefer to work part-time, as this enables them to attend college or university.

Shwe's approach is in stark contrast to the often cut-price strategies in the garment industry. These

Images: Jon Pienaar

SHWE

include outsourcing manufacturing to sweatshops in countries that have poor or no regulation, like China and Bangladesh. For Franco, this is not an option: she prefers to make less profit, and to ensure that people who work on Shwe are well paid.

Lessons

So what is the most important thing Franco has learnt from this endeavour? "The biggest lesson I've learnt from Shwe is that you can't do anything like this by yourself. It is a group effort. We have 64 women linked directly with Shwe, and every single woman is important to the whole process," says the social entrepreneur, who explains that Shwe recently did a collaboration with the Durban University of Technology.

"The university helped to teach the women in our group to learn the basics, like doing a good finish and putting in zips. It was a beautiful project, but also very emotional.

"When we arrived at the university, we discovered that some of the refugees had never been to school before. Any kind of school. That is when I realised that this was beyond just giving a profession to someone. That this is about hopes and dreams. That it is about community and us as a group helping and supporting each other," Franco explains.

When it comes to talk about the bottom line, Franco says she isn't in this for the money. "I've lost money setting this up, and I invest everything that comes in. Because it is always a matter of deciding to take a bigger salary or helping five more people. I always want to help more people. If you want money in fashion, it would be best to take a traditional job or open an individual brand, and not create a social brand."

Franco says that what inspires her is being part of a group and the sense of community she gets from working with Shwe.

"I get to work with women who have survived the trip from Burundi, who have walked to Johannesburg. Women who today can feed their children because Shwe exists. These women are the Shwe brand, not me. I just do the selling and the organising. I feel quite humble and thankful to be a part of something that is bigger than me, that is about the new world of fashion," Franco explains.

Challenges

There have been a lot of challenges since Shwe has become fully operational.

"A big lesson has been to understand what work means. Everyone sees work differently. What's been important is to define what work means to people individually, and to align this with the requirements to make the project viable. Everyone we work with comes from different generations, different backgrounds, and different countries, so finding a way for these individuals to work as a cohesive group has been both a challenge and a big learning experience," she says.

"If you don't organise well, you will pay for this through stress, or by having to run around more than you should."

"The challenge of cash flow is also very real because we have big dreams, but a limited budget. We want to try and fit so many things in, but we do have bills to pay."

Franco says that the operation takes a lot of organising and driving around, and that sound logistics are important. "My father always had this saying that goes: 'If the head doesn't think, the body pays for it.' If you don't organise well, you will pay for this through stress, or by having to run around more than you should."

It took a year for Shwe to become a sustainable project. The online shop is ticking over nicely, and Franco has managed to sell to a growing number of international stores.

"In November 2016 we started to become profitable, which is gratifying and important to our long-term growth."

The fashion brand is now a sustainable social enterprise that gives refugee women an opportunity to work in fashion and earn a living wage, while taking a socially conscious local fashion label across the world. ■

editorial@finweek.co.za

By Neesa Moodley

INSURANCE

Keep those back-to-varsity blues at bay

University students head back to campus this month but before you, as a parent, breathe a sigh of relief, you need to ensure that your children's valuables have been properly insured.

Typically, a student's laptop could cost anything from R4 000 to R23 000, a tablet between R1 000 and R9 000 and a smartphone between R1 300 and R11 000. "Textbooks can set a student back up to R7 000 per semester. And many students travel by bike, an inexpensive mode of transport – except for the set-up fees, which can go as high as R20 000, depending on the model," says Attie Blaauw, personal lines underwriting manager at Santam.

And no matter how extensively a house is covered, electronic equipment or any possessions that are "on the move" will not typically be covered by your insurance policy, he says.

"The premiums of a household insurance policy are determined by how secure the house is, for instance whether it is in a secure estate and whether the property has burglar bars, etc. As soon as the equipment is off the primary residence premises, it needs to be insured differently," he cautions.

So how should a student's possessions be insured?

Mandy Barrett of insurance brokers and risk advisers Aon South Africa, says there is a common misconception that the contents of students' residences are uninsurable because this is regarded by insurers as a "communal area", and therefore presents a much higher risk.

"While this may be true in some cases, particularly with off-the-shelf, commoditised types of insurance products, it's quite possible to arrange affordable cover for these risks linked to your household contents or vehicle cover. However, you can expect this cover to be subject to certain insurer restrictions such as forcible and violent entry," she says.

Barrett points out that a potential pitfall to watch out for is where the value of an item specified in the policy is not listed at its replacement value. "If this is the case, you could find the insurer only partially pays out in the event of a claim on the basis that the item was underinsured," she says.

A good practice is to make photocopies of receipts for high-value items such as laptops and bicycles so that you have an electronic copy of your proof of purchase. Bear in mind that the replacement costs are likely to escalate over time and the replacement values on your policy should be updated each year to allow for inflation.

Remember that while your insurance premium may increase slightly to cover specified items, it is well worth it when it comes to claim time and avoiding costly repair or replacement charges.

Attie Blaauw
Head of personal lines underwriting at Santam

Car insurance

If your child is fortunate enough to drive a car, it is important that the insurance policy on the car specifies that the child is the regular driver. Blaauw notes that this applies to children who live at home and drive to campus daily as well as those who live on campus.

This is particularly important because if the regular driver is not correctly or truthfully declared in your insurance policy and a different individual who drives the vehicle regularly is involved in an accident, your claim may be rejected or not paid in full.

"When it comes to insuring a student vehicle, make sure you have cover at least for balance of third party, fire and theft, with perhaps additional personal liability top-up cover, given the risk of major claims in the event of an accident or incident where the young driver is proven to be negligent," Barrett says.

Nthabiseng Moloi, head of marketing and brand at MiWay, agrees, saying that if you have failed to correctly specify the regular driver on your car insurance policy, the insurer has the option to void the cover as though you never had a policy in place. This is because the incorrect information means that your risk cover was incorrectly assessed and you would have been paying the incorrect premium. While it might be tempting to choose this option so that you have a lower premium, it is not worth the risk of losing your cover entirely. ■

editorial@finweek.co.za

Neesa Moodley has been a personal finance journalist for 12 years. You can find more of her articles at www.moneyissues.co.za

Image: Supplied Getty Images/iStock Images

By Lloyd Gedye

E-BOOKS

Amazon's e-book policy puts the squeeze on publishers

As the dominant player in the e-book industry, Amazon has turned the traditional publishing industry upside-down. Now the publishers are trying to fight back.

For many authors who have had their manuscripts ignored by major publishing houses, self-publishing is a great way to get their books out to the public. If their books do sell, they stand to make significantly more money than through a normal publishing deal. An author who publishes their work via the traditional route can make up to 30% in royalties on book sales; a self-published author through Kindle makes 70% in royalties.

Meanwhile the Kindle Storyteller Prize, worth £20 000, has been announced. It will be awarded to an author who publishes their book of no less than 5 000 words through Kindle Direct Publishing between 20 February and 19 May 2017.

Self-publishing success stories include, of course, *Fifty Shades of Grey* author E.L. James, whose real name is Erika Mitchell. She first attracted attention publishing *Twilight* fan fiction as Kindle books. She has since sold over 100m copies of the *Fifty Shades* trilogy and in 2014 topped *Forbes'* list of highest-earning authors with earnings of $95m.

Amazon publishes about 4m e-titles a year, about 40% of which are self-published. Reportedly, more than a third of the top 100 Kindle books being sold are self-published. Books within the crime and psychological thriller genres, which remain very popular among readers, dominate the self-publishing scene.

Amazon publishes about 4m e-titles a year, about 40% of which are self-published.

However, over the past few years big publishers in Europe and America have been crying foul. The media has repeated their claims that e-book sales declined for the first time in 2015 and continued to decline in 2016. What they are not saying is that e-book sales are not declining as a whole – they are actually increasing. Instead, it is the share that belongs to these major publishing houses that is declining.

Sales of self-published e-books, on the other hand, are rising. Major publishing houses have increased the prices of their books, and many in the industry claim that this is a major contributing factor to the decline in sales.

Before 2010, the major issue for many publishers was that Amazon controlled pricing and insisted on selling e-books at $9.99, when the publishers wanted a higher retail price for their e-books.

When publishers tried to negotiate new contracts with Amazon that allowed them to control the price of e-books, the online retail giant responded with heavy-handed tactics such as delaying deliveries of their books to customers and removing standard discounts from certain publishers' books.

But pressure mounted and eventually the e-tailer agreed to new contract terms. The result was that prices rose. Amazon was still seen as a dominant company in the e-book market and in 2015 the European Commission launched an anti-trust investigation.

Amazon controls about 75% of the US e-book market, and is the largest e-book retailer in Europe too. The investigation focused on books in English and German, the largest markets for e-books in Europe.

The commission argued at the time that Amazon's e-book contracts with publishers, which stipulated that they must give Amazon terms as good as those of its rivals, could violate European law and may have dampened competition from other e-books distributors. The commission was concerned about "discount pool" conditions, which linked potential discounts on e-books to their corresponding prices at rival sellers.

The day after the news of Amazon's new literary award broke, so did the fact that the company had agreed to change key conditions in its publishing contracts with authors.

In a bid to escape a drawn-out investigation and potential fine, Amazon offered not to enforce any of the controversial clauses in question for the next fives years and would allow contracts containing the discount pool clause to be terminated with 120 days' notice. European publishers have a month to comment on Amazon's offer.

In the UK, where Amazon has a 90% share of the e-book market, chief executive of The Publishers Association, Stephen Lotinga, has also called for action from authorities, stating that with Brexit a few years away, the country's authorities could no longer rely on the EU to deal with these issues.

"When a business reaches such scale, if left unchecked, it is almost inevitable that they will use their dominance in such a way to ensure the status quo does not change and thereby prevent real competition in the marketplace," he said.

It's becoming clear that while Amazon, a digital disruptor, has managed to break some of the stranglehold of the major players in the publishing industry, concerns are mounting that it is developing a stranglehold of its own. ■

editorial@finweek.co.za

Gallo Getty Images/iStockphoto

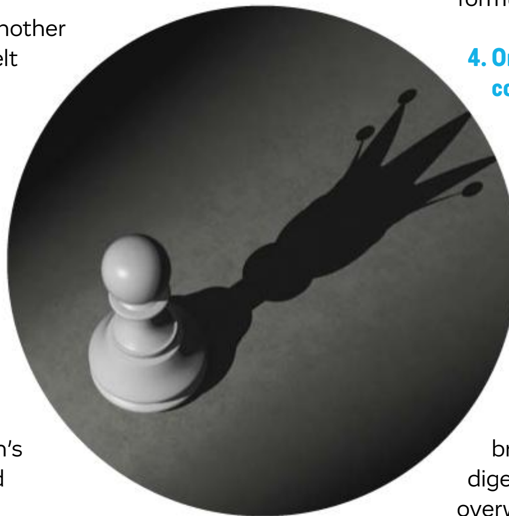
By Helena Wasserman

How to ace your first 100 days

You have a small window of opportunity to make your mark in a new leadership position. Here's how to have the best possible start.

The first 100 days in a top job have become an important milestone, with everyone from South Africa's public protector to the new US president currently being scrutinised on their performance during this key period.

In fact, the milestone dates back to another US president. When Franklin D. Roosevelt took office in 1933, he faced the Great Depression, a banking catastrophe and a devastated economy. Within 100 days, he established key initiatives (including a famed jobs programme) that would reverse the ruin. Since then, the 100-day standard has become a key measure of success.



Here's how to make your mark in the early days:

1. Learn names. "Remember that a person's name is to that person the sweetest and most important sound in any language," Dale Carnegie famously said. "Respect and acceptance stem from simple acts such as remembering a person's name and using it whenever appropriate." In fact, this should be part of your homework *before* you start a new job. Along with learning as much as you can about the company's positioning (particularly its pricing and strategy, and what competitors are doing) before you join, compile a photo book with the names and profile pictures of the people you will work with.

2. Be clear on what you are supposed to achieve by confirming your goals with your new boss or the board. If the company is in crisis, you will be expected to move fast and take drastic action.

3. Don't focus on firefighting. You will be faced by an onslaught of immediate problems and urgent tasks. Getting caught up in day-to-day management is tempting: from the outside, you look busy and dynamic. Resist this and focus instead on the bigger picture. You need to make sure the company is on the right track. Step back, and spend most of your time in the first 100 days devising a clear strategy for the future. Spend time with your team members and ask them for their input on how costs can be reduced, performance improved and revenue increased. Ask stupid questions. This will give your new colleagues a chance to demonstrate their domain knowledge. Also do your own on-the-ground research before you formulate a strategy.

4. Once you have a clear strategy, set up concrete targets for the short, medium and long term. Make sure that your team understands what the strategy is, and why these targets are important. Repeat the strategy over and over again; it is only with repetition that people will internalise what they need to achieve. Make sure the goals are achievable, and celebrate success. Set up quick wins (for example, lowering the costs on a project) for the first 100 days. Success is energising. Also, break down problems into smaller, more digestible projects, to avoid people becoming overwhelmed by all the challenges.

5. Accept that you won't be universally loved. Your new approach and strategy probably won't be roundly welcomed and there will be plenty of detractors. Stay calm when encountering criticism.

6. Show that you trust your team. Once you have conveyed your strategy, don't micro-manage the implementation, says Professor Tommy du Plessis, director of the North-West University School of Business and Governance.

Professor Tommy du Plessis
Director of the North-West University School of Business and Governance

7. Establish solid relationships. This should be your top priority. Understand what motivates each person on your team and work hard to connect with them. Without strong relationships, you won't be able to rally people behind your strategy and create an environment where information flows freely. Build trust with each person and don't show favouritism.

8. Create a communication channel. Consider sending a weekly email to your team with some of your personal experiences. This can be an important platform to reinforce the new strategy, and will also help you counter rumours and make you more accessible to employees.

Images: Getty Images/iStock Images commerce.nwu.ac.za/business-and-governance/tommy-du-plessis

Ask stupid questions. This will give your new colleagues a chance to demonstrate their domain knowledge.

9. Get out of your office. Connecting with people where they work will give you a clear idea of operational challenges.

10. Accentuate the positive. Avoid negative language and fearmongering. Celebrate what has been built in the business and don't criticise those things that make employees most proud.

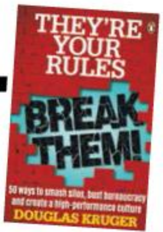
11. Don't dither. The first rule of swimming with sharks: don't bleed. After gathering all the facts, take decisive action and don't backtrack.

12. Make the hard calls as soon as possible. If retrenchments or closing a department is unavoidable, do it within the first 100 days. Also, get rid of the dissidents. While it may sound cruel, your first priority is to rally your team around a strategy and not to accommodate naysayers and armchair critics, says Du Plessis. Make changes within your team *before* you get bogged down with the weight of relationships. Don't delay the inevitable; instead get it behind you as quickly as possible.

13. Whatever you do, don't redecorate your office or spend company money on making things more comfortable for yourself. This sends out the wrong message in these straitened times. Instead of buying new furniture for your office, focus on things that will make life better for your team members.

14. Don't forget your clients. Often in the transition process during the first 100 days, employees are so distracted by the internal changes that clients are neglected, says Du Plessis. "From the start, make sure that employees stay focused on clients." ■

editorial@finweek.co.za



This week, you can win a copy of *They're Your Rules – Break Them: 50 Ways to Smash Silos, Bust Bureaucracy and Create a High-Performance Culture* by Douglas Kruger. To enter, complete the online version of this quiz, which will be available on fin24.com/finweek from 13 February.

1. **True or false?** The fall armyworm has also destroyed crops in neighbouring countries.
2. **True or false?** Madonna performed during halftime at this year's Super Bowl.
3. Supply the missing word: Dawn stands for Distribution and Warehousing ________
4. Who is Betsy DeVos?
   - A Dutch presidential candidate
   - A local entrepreneur
   - A US businesswoman and philanthropist
5. On what date did this year's State of the Nation Address take place?
6. Which of these countries' flags does not have a cross on it?
   - Sweden
   - Tonga
   - Mexico
7. In economic jargon, what is the opposite of a hawk?
8. Under which country was a "lost continent" discovered recently?
   - Iceland
   - Mauritius
   - Mongolia
9. **True or false?** Cell C has been downgraded to a D credit rating by Standard & Poor's.
10. Who is the mayor of Tshwane?

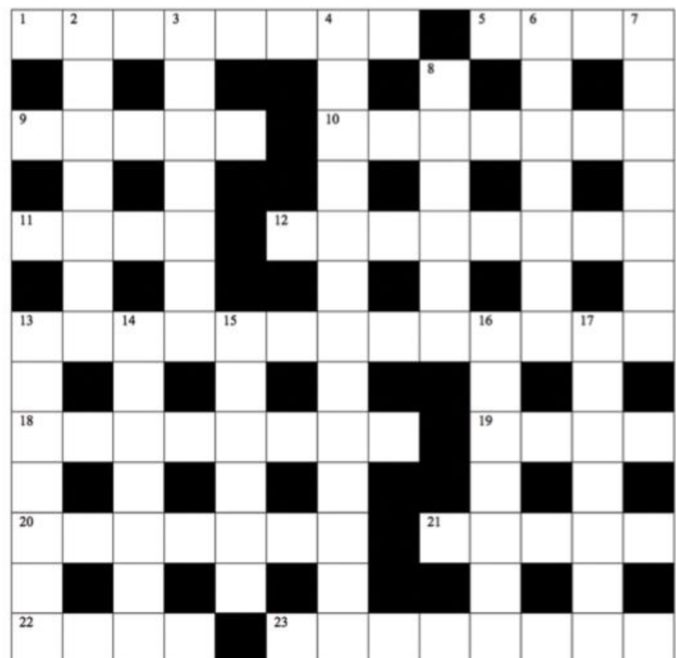
CRYPTIC CROSSWORD NO 667JD

ACROSS

1 Particular remedy (8)
5 Union card (4)
9 Go over again, over the top (5)
10 See format of disc, errors and omissions excepted (7)
11 Pooh-pooh four-hundred or so (4)
12 Woman provided with ultimate way to make salt (8)
13 Man in charge of swine is madly in love (4,4,5)
18 Fond of seclusion in the bedroom? (8)
19 Put together a dismal return throughout (4)
20 Maize core is source of starch loaf (7)
21 Balancing half the viewers time (5)
22 Clean chair cover (4)
23 Tied dry grass therein (8)

DOWN

2 Exact summary to a point (7)
3 Danced with tea boy (3-4)
4 Nervy brides incline to be difficult to make out (13)
6 Sheltered place in grounds to fish (3,4)
7 Where to go to sleep (3-4)
8 Judge hopes to rehabilitate exiled brother (6)
13 More Charlie back from front of vehicle pod (7)
14 An officer made a mistake, one right away which got fixed (7)
15 Ruler overcharge improper (6)
16 Forgive without hesitation for cancellation (7)
17 The French multinational's direction is to hand over to laymen (7)



Solution to Crossword NO 666JD

ACROSS: 1 Prerogative; 9 Impulse; 10 Miler; 11 Maori; 12 Verbals; 13 Recede; 15 Smooth; 18 Enamour; 20 Estop; 22 Drier; 23 Set free; 24 Cross swords

DOWN: 2 Repro; 3 Rallied; 4 Greave; 5 Timer; 6 Volcano; 7 Firm friends; 8 Grasshopper; 14 Clavier; 16 Maestro; 17 Crisis; 19 Ogres; 21 Tired

On margin

A hazard of air travel

A flight attendant sees a suspicious couple on board, and decides to report it to the pilot immediately.

"Sir, I think we have a case of human trafficking! The female passenger looks pretty frightened and the man she is with looks dangerous!"

The pilot responds: "Patricia, I've told you before. This is Air Force One..."

Academia

An eccentric philosophy professor gave a one-question final exam after a semester dealing with a broad array of topics.

The class was already seated and ready to start when the professor picked up his chair, set it on his desk and wrote on the board: "Using everything we have learnt this semester, prove that this chair does not exist."

Fingers flew in furious fashion. Some students wrote more than 30 pages in one hour attempting to refute the existence of the chair.

One member of the class, however, was up and finished in less than a minute.

When the grades were posted, the rest of the group wondered how he could get an A when he had barely written anything at all.

His answer consisted of two words: "What chair?"

Work life

I called an old school friend and asked what he was doing. He replied that he was currently working on the aqua-thermal treatment of ceramics, aluminium and steel under a constrained environment.

I was impressed, until I learnt on further enquiry that he was washing dishes with hot water under his wife's supervision.

In short

A guy in a crematorium asks the minister: "Do you have the WiFi password, please?"

The minister snaps: "Have you no respect for the dead?"

The guy responds: "Is that upper or lower case?"

I'm ordering a chicken and an egg from Takealot...

I'll let you know.

"I don't think you're the kind of '*business disruptor*' we're looking for."

Mzu @Mzukisi_Qobo
Deng Xiaoping: "It doesn't matter whether the cat is black or white, as long as it catches mice, it is a good cat." I hope Nel catches Zuma.

Darrel Bristow-Bovey @dbbovey
Entrusting Seabelo Senatla to the Stormers is lending a Bernini sculpture to a troop of chimps in boxing gloves, hoping it'll come back in one piece.

Dirk de Vos @DirkdeVos
Would be great if Zwane & whole of ANC would familiarise themselves with just 1 thing: A risk-adjusted required return on investment.

REW @therealeatwood
Years later, I find my old maths teacher. She nods: it's time.

She writes: 1 ÷ 0 =

We watch through the window as the explosions begin.

Ruan Jooste @DURITZ79
Screw the Big Mac Index. The true value of the rand is reflected at a vending machine. It is worth nothing.

Sipho Kings @SiphoMcD
You know you're not in the 1% when the button to make your car go faster is the one that turns the aircon off.

oh please @ohpeetie
It's 27 outside. Oh great, even the weather is younger and cooler than me now.

"With lies you will go far, but not back again."
– Yiddish proverb

BUREN

It's my time

Bacher & Co

011 372 6000
For a stockist list visit: www.bacherco.co.za

Smart gets real

Linking with your smartphone

CITIZEN Bluetooth Watch brings you smart functionality plus the essential elegance of an analogue timepiece, it keeps running as long as there is light and has a 4-year power reserve.

CITIZEN and Eco-Drive are trademarks or registered trademarks of Citizen Watch Co., Ltd.

CITIZEN

BETTER STARTS NOW

www.citizenwatchshop.co.za | 011 257 6000 | info@cjr.co.za | CitizenPromaster