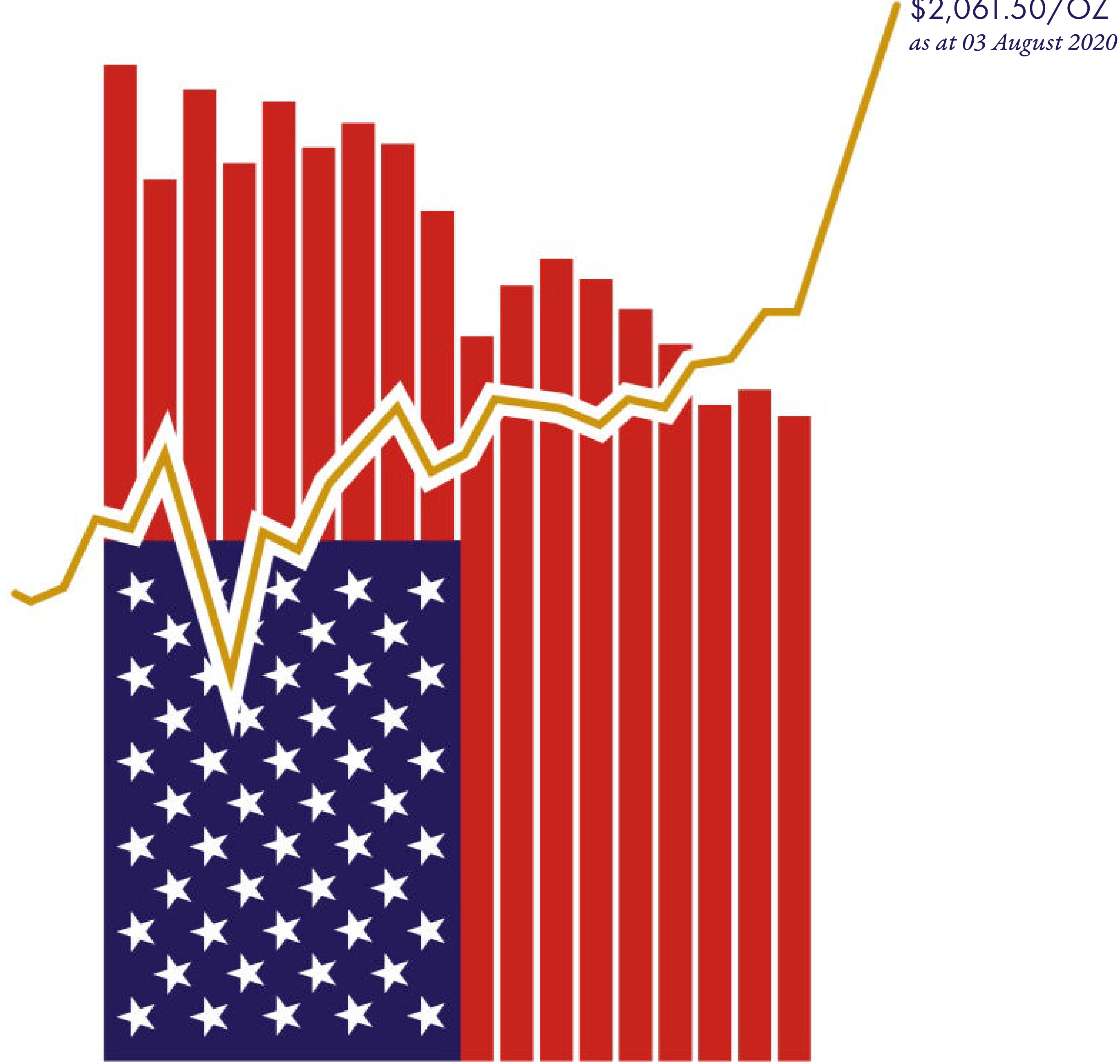

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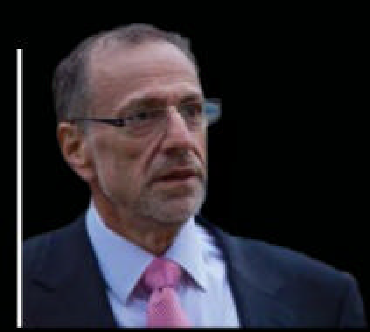

SPOTLIGHT

MICK DAVIS ON THE FUTURE OF MINING

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THE MASTERS

The only major always played on the same course, the Masters has been home to some of the greatest moments in golf history since 1934. From the drive up Magnolia Lane, to the ceremonial opening tee shot, to the miracles at Amen Corner, golf's legends will always live on at Augusta National. And as the next generation makes its mark, a victory there will always stand at the pinnacle of golf. Rolex celebrates the return of championship golf at this year's historic November Masters.

#Perpetual

THE MASTERS TOURNAMENT
AUGUSTA NATIONAL GOLF CLUB
12 TO 15 NOVEMBER 2020

OYSTER PERPETUAL DAY-DATE 40
IN 18 CT WHITE GOLD

from the editor

JANA JACOBS

On 21 October, the Orlando electricity substation in Johannesburg went down, causing a widespread power outage in the city that affected several areas. The cause wasn't clear. As it seems to be the best source of updates when it comes to municipal problems, residents scoured the City of Joburg's Twitter feed for news on the cause and the estimated time of repair.

Power was eventually restored approximately six hours later. By power outage standards, this is a walk in the park compared to durations of over 24 hours – which also happened during that week in other suburbs of Johannesburg.

These severe power outages (not related to load shedding) have become an unacceptably regular occurrence in Joburg, and the ripple effect this has is immense.

One being that residents were also left without water. Due to the lack of electricity, Rand Water's Eikenhof pump station couldn't operate, which meant that all Hurst Hill reservoirs were almost empty. Over a week after the initial power outage, residents are still being urged to use water sparingly. Some had little to no water for days. Some ten hospitals, including Helen Joseph and Baragwanath, were affected. Water tankers were dispersed, and local ward councillors were left desperate as no answers were forthcoming from the mayor or the city regarding the crisis.

What this highlighted is just how concerned we should be about the effects of water shortages – not just because of poor infrastructure. An opinion piece published by Sowetan Live in August, points to estimates "that Johannesburg and even South Africa as a whole could run out of water as soon as 2030 if more effort is not put into conserving water and changing the attitudes and behaviours of Johannesburg's citizens".

According to data from Rand Water on 28 October, The Vaal Dam, Gauteng's main water supply, was at 28.7% of full capacity.

As illustrated by Cape Town's water crisis two years ago, water-saving efforts need to be spearheaded by city management. Strategies need to be put in place because we cannot rely on snow- or rainfall to fill our dams.

It is still not clear why citizens had to wait so long for water to be restored after the Orlando outage. What is clear is that we need city management to do more than update us via social media. And we need to wake up to the fact that Johannesburg needs a plan. ■

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By Johan Fourie

ECONOMY

What sport can tell us about inequality

Strengthening economic freedom (and institutions) may support a reduction in a country's inequality.

Sport is often a microcosm of broader patterns in society. Sport can also say something about the economic incentives in society. Take the relationship between a country's inequality and its economic performance. Most of us would argue that inequality hurts growth; that a highly unequal society inhibits the productive potential of those at the bottom of the income distribution. Some, though, would say that inequality, even severe inequality, is a necessary condition of economic freedom: those with the best ideas or best talents must rise to the top and be rewarded for their skills and their appetite for risk – the incentive effect. Identifying just which of these two effects are most important, though, is a precarious exercise, full of knotty measurement issues.

However, what we can measure quite accurately is Olympic performance – the number of medals per capita. Can we discern which of these two effects are dominant when analysing the relationship between inequality and Olympic medals? Let's begin by assuming that the rich and poor are equally endowed with sporting talents in any society. For an athlete to reach the level of Olympic medallist, however, requires thousands of hours of practice. It also requires access to facilities, money and time. It is more likely that the rich would have access to these resources than an extraordinarily talented but poor individual. It follows, then, that in a highly unequal society, only a small proportion of people would have access to the kinds of resources that would allow them to become Olympic athletes. Similar to economic performance, the expected relationship between Olympic medallists in a country would be negative.

But it's not that simple. Winning an Olympic medal also brings monetary rewards, which are disproportionately larger for the poor (relative to their incomes) than the rich. This creates a strong incentive for the poorest to participate in sport and invest effort, especially if the road to other forms of wealth are even more treacherous. Put differently: If good schooling is essential to study at university and qualify for a professional occupation, it would be rational for a kid from a poor neighbourhood to invest time and effort into becoming a marathon athlete where the barriers are not as high. It could therfore be that inequality induces greater participation in sport, leading to more Olympic medallists – the incentive effect.

So which effect is larger? A forthcoming paper in the *Journal of Institutional Economics* by economists Vadim Kufenko and Vincent Geloso, tests this relationship empirically on the 2016 Rio Olympic Games. Controlling for many things, including the size of the population and the country's previous Olympic performance, the authors indeed find a negative relationship between inequality and Olympic medallists, but with an important condition: it is only true for countries that are economically unfree. To measure economic freedom, they use the Economic Freedom of the World database, a ranking produced by the Fraser Institute in Canada. For countries that score high on this list, the authors find no relationship between inequality in countries with economic freedom and Olympic medals won.

How to explain this? Kufenko and Geloso argue that in countries with strong property rights – an important component of the economic freedom index – the rewards of one's efforts are secure. In fact, it may encourage more effort, in sharp contrast to weak property rights regimes, where the returns to one's investment can be easily expropriated. In this way sport outcomes mirror broader incentives in society. When social mobility is low, when the poorest see no reason to invest in themselves, no reason to put in extra effort – the case for many societies around the world where property rights and other institutions are weak – then those at the bottom of the income distribution are unlikely to invest. Inequality would then lead to sub-optimal outcomes. But when institutions are strong, when there is reward for effort, return on investment, then inequality will not stand in the way of development. The focus, suggest the authors, should be on improving the institutions rather than directly addressing inequality.

Another type of inequality that has received a lot of attention in recent times is the gender gap. A new paper by economist Maryam Dilmaghani in the *Journal of Comparative Economics* asks why it is that in Vietnam the number of candidate master chess players is 47 women for every 100 men, when in France and Sweden it is far more unequal – 3 women for every 100 men. She attributes it to communism: "The present paper provides strong evidence for the influence of contextual factors on female attainment in chess. The fact that post-Soviet countries and Mongolia largely stood out alongside China, Vietnam, and Cuba, supports the possibility of persistent effects for sociopolitical institutions. Particularly, it may be the case that by making gender-role attitudes less traditional, the socialist institutions have steered women towards investing in activities that have been traditionally male dominated."

> But when institutions are strong, when there is reward for effort, return on investment, then inequality will not stand in the way of development.

Differences in the incentives of communist and capitalist regimes help to explain the gap. In most capitalist countries, gender equality efforts focused predominantly on social welfare, providing maternity leave and other such measures to support pregnancy and childcare. Communist countries, by contrast, explicitly promoted female labour force participation, often at the cost of women's fertility choices. That also explains why fertility rates are below replacement levels in most former communist regimes. The lower levels of gender inequality in the former communist countries could easily be interpreted as a sign of success today, but it would have come with substantial limits on women's fertility choices.

Chess, just like the Olympics, exposes how institutions shape inequality – and how addressing inequality requires a careful understanding of the historical context in which that inequality is embedded. ■

editorial@finweek.co.za

Johan Fourie is professor in economics at Stellenbosch University.

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in brief

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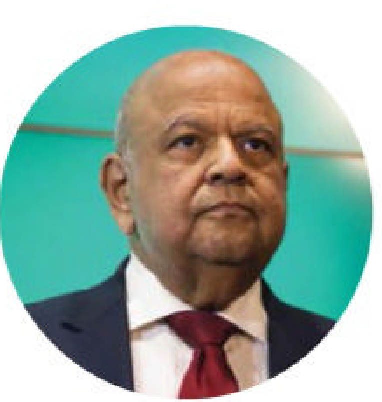
>> The influence of the Chinese economy's remarkable recovery *p.13*

"FOR ONCE, WE CAN TALK ABOUT AN SOE WITHOUT TALKING ABOUT BAILOUTS."



Pravin Gordhan

— **Public enterprises minister, Pravin Gordhan,** applauded Transnet for posting "excellent results". Transnet reported a 1.3% increase in revenue to R75.1bn and a net profit of R3.9bn for its financial year to the end of March 2020. This was marginally below the revenue growth of 1.6% it posted for the previous financial year, but it came largely from tariff increases for port and rail users, which averaged 2.9% for its latest reporting period. The company's auditors gave Transnet a qualified audit opinion.

"Do we just unilaterally stand down and not choose to use the same tools that Republicans did in the majority?"

— **Chris Murphy, a Democratic senator representing Connecticut,** following the confirmation of Amy Coney Barrett as justice of the US Supreme Court by the nation's Senate, according to Hill.com. Barrett replaced Justice Ruth Bader Ginsburg, who died in September. The confirmation comes less than two weeks before the US presidential election and the court now has a 6-3 conservative vote. The Democrats said they'll consider increasing the number of Supreme Court seats from its current nine to gain a liberal majority on the bench.

"A candidate that ticks all the boxes."

Tsakani Maluleke

— **ANC MP and chairperson of the Standing Committee on Appropriations, Sfiso Buthelezi,** said that the deputy auditor-general, Tsakani Maluleke, was "the best of the best" among candidates that were interviewed to take over from the outgoing auditor-general (AG) Kimi Makwetu, whose seven-year term ends on 30 November. Maluleke was nominated by parliament as the new AG from 1 December, making history as the first woman recommended for the post. Though the recommendation was a unanimous decision across party political divides, it must go to the National Assembly for final adoption.

EDITORIAL & SALES

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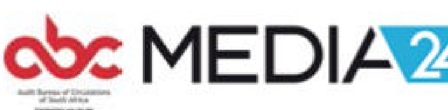


Cabinet approved measures to support the domestic ferrochrome industry, including through an export tax on chrome ore. Jackson Mthembu, minister in the presidency, said interventions also include the usage of energy-efficiency technologies in smelters, and the adoption of cogeneration and self-generation technologies. Last year, South Africa supplied 12.5m tonnes of chrome ore to China, which accounts for 83% of China's total chrome imports, according to Reuters. Companies that mine and process chrome in SA include Glencore, Merafe Resources, Samancor Chrome, Tharisa, and Jubilee Metals (also see p.12).

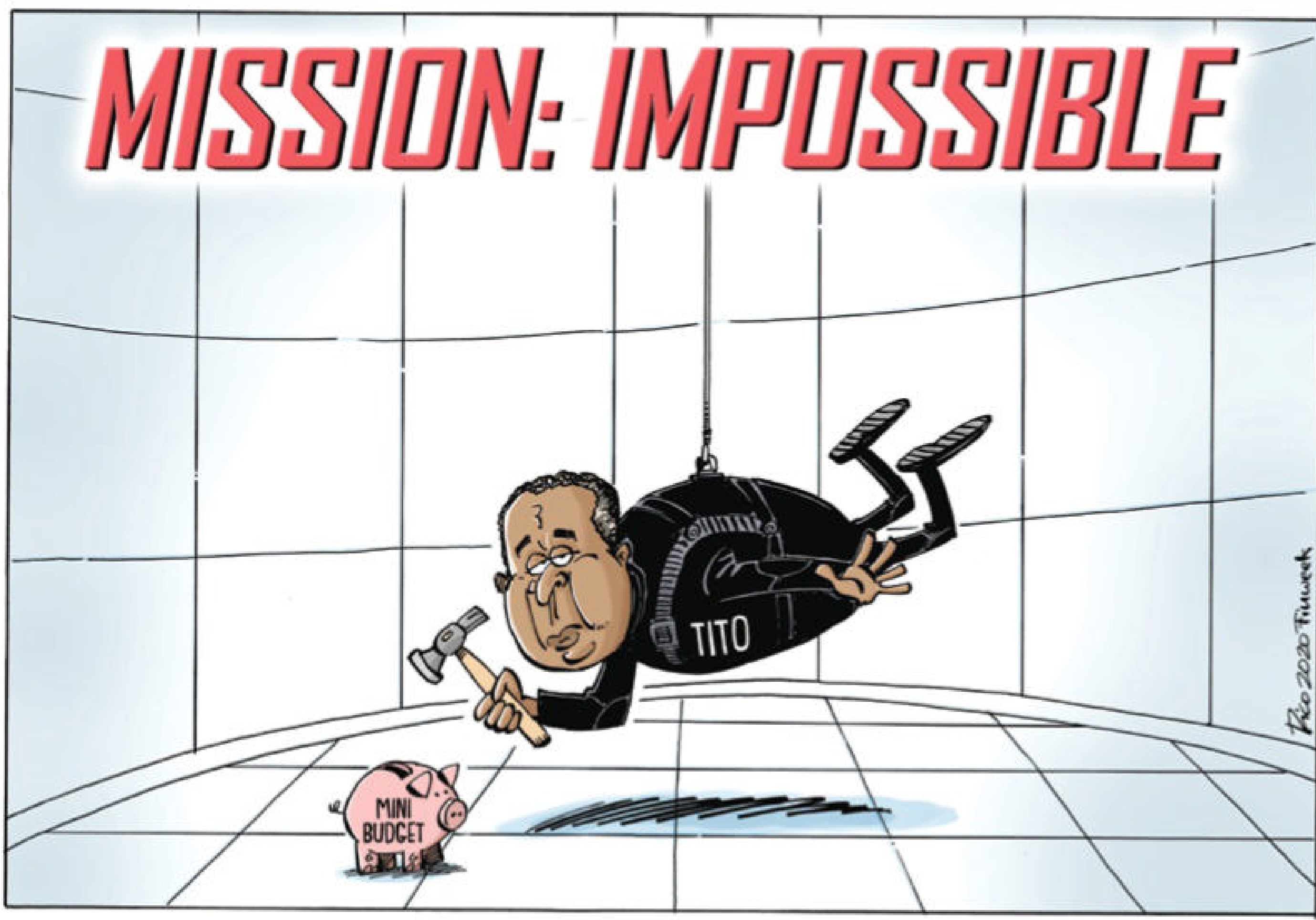
SA's consolidated fiscal deficit is set to widen further than projected in June's emergency Covid-19 budget as a third-quarter rebound in economic growth will not boost tax receipts enough, a Reuters poll found. A median of 21 economists, polled between 15 and 20 October, forecast a budget deficit of 15.9% of GDP this financial year, 0.2 percentage points wider than expected by finance minister Tito Mboweni in June. The poll saw the deficit narrowing to 10% of GDP next year and then to 9% in financial year 2022/23. SA's gross debt will climb to 92% of GDP by 2023/24, the Reuters poll showed, just shy of the 100% level, which Mboweni warned it could exceed in 2025.

Important issues, such as rural safety and job security have been used for cheap politicking according to the Agricultural, Food, Fishing and Retail Industry Workers' Union. It said politicians have been riding on the Senekal murder saga. Various politicians and organisations gathered in the Free State town of Senekal as racial tensions threatened to spill over following the murder of Brendin Horner. The 21-year old farm manager's body was found in an open field in early October.

Photos: Gallo/Getty Images | twitter.com

DOUBLE TAKE

BY RICO



ONLINES SALES SKYROCKET

361%

Pharmaceutical retail chain Clicks said that its online sales soared 361% in the second half of the year as consumers chose to shop closer to home and less frequently through the lockdown and opted for home delivery to avoid the risk of contracting Covid-19. CEO, Vikesh Ramsunder, told IOL that although the online growth in the second half was off a low base, the platform had become their largest and fastest-growing store. Online sales growth had slowed a little with the easing of lockdown restrictions, but the growth remained "exponential", he said. The retailer also increased its final dividend by more than a third (also see p.32).

30-YEAR LEASEHOLDS

896 farms

Agriculture, land reform and rural development minister, Thoko Didiza, announced that 896 state-owned farms measuring 700 000 hectares would be released on 30-year leaseholds to advance land reform. BusinessLIVE reported that about a third of the 700 000ha the government said it would make available for land reform is already occupied by communities and black farmers, some of whom now fear they will be forced to vacate the land. Didiza said all beneficiaries who have been allocated state land and who have signed lease agreements will be subjected to a compulsory training programme.

IN THE UIF KITTY

R50bn

Labour minister, Thulas Nxesi, told parliament that through the Unemployment Insurance Fund's (UIF) Covid-19 Temporary Employee Relief Scheme (TERS), over R49bn had been disbursed in benefits in the form of over 11m payments since the beginning of the lockdown. Nxesi said R23bn was disbursed in Gauteng (in 5m payments) and R484m was disbursed in the Northern Cape (in over 100 000 payments). At the same time, R7.5bn was disbursed in 1.3m payments in normal UIF benefits. He also said that the UIF now has around R50bn available.

THE WORLD'S LARGEST LISTING?

$34bn

Chinese financial technology company, The Ant Group, controlled by Alibaba's founder Jack Ma, is set to sell $34bn of shares on the Shanghai and Hong Kong stock exchanges in what could be the world's largest listing, the BBC reported. If successful, the listing will value Ma's stake at $17bn. The company is expected to list some time during the first week of November. This will propel Ma's wealth close to $80bn and cement him as the richest person in China, the BBC reported.

By Timothy Rangongo

Mastering the real world, virtually

AxioVR designs customised virtual reality paradigms to help clients prepare for, and understand, real-life situations.

Virtual reality (VR) technology has given us the ability to design and simulate environments in two or three dimensions (2D or 3D) that are interactive and can be explored in real time. VR headsets allow us to be completely isolated from outside stimuli and become immersed in a virtual world. It can also place us in situations we would otherwise be fearful of in real life – which is where AxioVR comes in.

"We found that VR is the perfect platform to stimulate patients and subjects to elicit fear or a response from them," says Gideon Burger, co-founder of AxioVR about how they create safe virtual environments wherein subjects are exposed to their fears, such as heights or even public speaking.

AxioVR is a spin-off of Axiology Labs, a company started by Burger that provides and services psychophysiological recording equipment for scientists, teachers and researchers across the African continent.

When Burger expanded the company's offering to include VR hardware, he attempted to design virtual environments, but quickly realised design was not his forte. Burger approached Natalie Roos, a fine arts major who had designed spaces for the Hyatt and Marriot hotels, among others, to co-found AxioVR together with Dr Stefan du Plessis.

Du Plessis, a clinical neuroimaging researcher at Stellenbosch University jumped on board as co-founder and research director. Du Plessis uses VR as an assessment tool for his research in stress sensitivity and abnormal neurodevelopment seen in schizophrenia.

"We aim to create situations where the psychological effect is the same as the real deal, without putting the subjects at risk of any physical harm," explains Roos.

For an individual that grappled with a fear of public speaking, for example, AxioVR created a virtual auditorium and placed the participant at a podium where they were to deliver a speech that they were not prepared to give.

"We started heightening his senses with the opening of a curtain and 600 people staring back at him in VR. As he started his speech, we increased the intensity by either having a cellphone ringing, or the crowd mumbling to make the subject increasingly nervous," explains Roos.

Throughout the entire ordeal, the AxioVR team tracks, monitors and records the electrical signals from the user's heart and electrical activity in the brain with biofeedback equipment, creating publishable data to help in curbing the particular phobia.

"We aim to create situations where the psychological effect is the same as the real deal, without putting the subjects at risk of any physical harm."

"We have done a fear of heights paradigm, where we created a giant warehouse and had the subjects stand on a platform that starts rising as we monitor signals such as heart rate. We have had people crawling on the floor, that is how lifelike it is," says Roos.

The sky isn't the limit

It is not just phobias that AxioVR assists with. The team also designs VR software applications according to clients' specifications. For example, training the team of a mining or construction company on maintenance procedures or visualising a large construction project to get the almost real view of it. VR systems can be installed onsite with the provision of training services.

"I don't just get a design brief, create a world and then check back in after three months. We work closely together with the clients," says Roos. "Everything usually starts off with a storyboard, like a blank canvas. We check in with the client to go over whether they like the idea or not, incorporating their suggestions."

According to Burger, the team bootstrapped their way right up to when the company started receiving orders. "We received some support from researchers — we build a specific world based on what the researchers need."

AxioVR has developed for the Stellenbosch, Cape Town and Nelson Mandela universities. "Where we are currently really involved is at Nelson Mandela University's new medical school. They have just ordered their first VR headset," says Burger.

One research project with Stellenbosch University that the team is currently busy with, is creating a drug addiction paradigm. Upon wearing the VR headset, subjects find themselves in a house where crack cocaine is bought and sold, complete with drug-taking paraphernalia, alcohol and drug dealers and users loitering about.

The experiment is an attempt to better study addiction by analysing the responses of addicts when immersed in triggering spaces. "There are a lot of drug addiction studies and research, but the context is not always suited to that of South Africa's," explains Roos, who is charged with designing the space to make it as realistic as possible – specifically within the SA context.

AxioVR has also been approached for non-research projects, such as working on chewing gum brand Stimorol's activation of new peppermint and mango flavours.

"We ended up creating a rollercoaster ride that starts in the city and drops the subjects in a cave filled with exploding mangoes. We took them up buildings and into the sky where we had peppermint flavours blowing at them."

Photos: Supplied | unsplash.com

Gideon Burger
Co-founder
of AxioVR

Natalie Roos
Creative director and
co-founder of AxioVR

The brand activation ended up being a 4D experience with the inclusion of scents, vibrating chairs that gave a feeling of movement, actual bubbles that subjects could touch and the release of moisture when they hit the water.

The chewing would become even more intense as all these things happened, recount Roos and Burger. Though the team managed to secure another contract with the brand based off this experience, the Covid-19 pandemic has put activations on the backburner.

Creating new learning experiences

Apart from a funding round that is coming up shortly, AxioVR also received some project funding from the Technology Innovation Agency, according to Burger. "That has all been focused on the specific modular platform that we as a company see as having potential to enable us to roll out globally."

Dubbed the Axio Academy, it is the company's VR approach to medical teaching that the team wants to take global. "We are really invested in Axio Academy," says Roos.

"The first module is on the central nervous system. We are taking a boring textbook and creating images where users can see the central nervous system in 3D."

Students will be able to interact with organs, such as the brain. They will be able to virtually touch and turn it, as well as work through slides of magnetic resonance imaging (MRI) scans –a type of scan that uses strong magnetic fields and radio waves to produce detailed internal images of the body. The module will also include quizzes that enable students to track their learning progress.

However, here, the pandemic has also presented the team with a business lesson: not everybody in South Africa can afford a VR headset. The team realised that although a university might have a VR headset for their labs, during lockdown universities had to make plans to acquire and distribute laptops to students that normally rely on campus computers.

"So, we are working towards turning the Axio Academy into a platform that could work on 2D flatscreens or smartphones, so that we do not disadvantage people without VR headsets," explains Burger.

He says students will be able to rely on their smartphones to complete the curriculum and get the full VR immersive learning when on campus. ■

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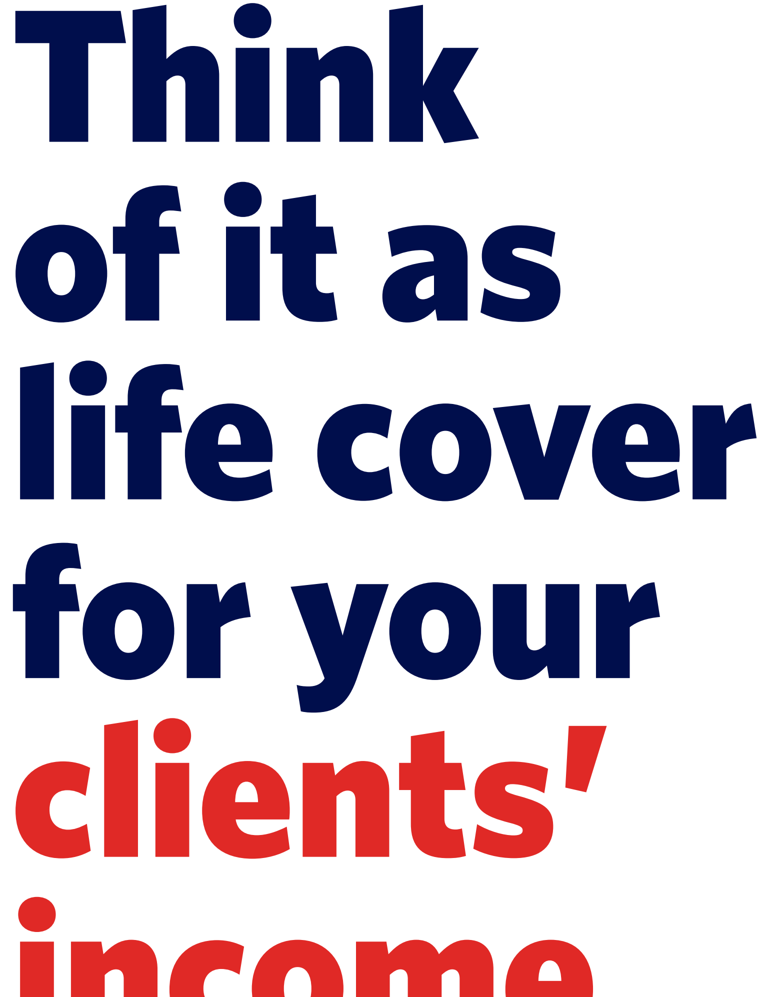

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BRAVE/6453/MOM/E

By David McKay

MINING

Outdated notions of beneficiation won't cut it

Central to the government's industrialisation policy is the concept of beneficiation, which experts believe is inherently flawed.

One proposal that might bail out South Africa's ferroalloys industry is that Eskom agrees to a long-term power purchase framework in which there is tariff relief in return for smelters reducing consumption during peak demand periods.

Ferrochrome and ferromanganese production consume baseload power 'when people are sleeping', but it will vanish at the current rate of inflation. According to the Minerals Council of SA, electricity tariff hikes have culminated to about 500% over the last decade.

In the meantime, the government has papered the cracks with an export tariff that would charge mainly Chinese buyers more for chrome ore – the stuff ferrochrome producers put in a furnace to make the higher-value ferrochrome, used in the fabrication of stainless steel.

China buys about 85% of its chrome ore requirements for smelting in its furnaces from SA, which is by far the world's biggest producer of the mineral. Given SA controls chrome production, it should be industrialising it too.

This is the notion behind the holy grail of the government's industrialisation policy: beneficiation, a word of worrying provenance, according to Martyn Davies, managing director of Deloitte's unit for emerging markets and Africa.

"I've never heard it anywhere else I've travelled," he told the Joburg Indaba conference in October. Applied to the ferroalloys sector, beneficiation holds that instead of exporting chrome ore, SA should be investing in the entire value chain ultimately producing stainless steel sinks.

But it's a flawed concept, said Davies. "It assumes there's a competitive advantage on having minerals in the ground that then confers a competitive advantage. I don't think that's right."

"Beneficiation is very state centrist; it's naïve economically," he said. The most competitive steel mills globally are in Japan, China and South Korea, none of which have iron ore resources, for instance.

"This government and ANC are wedded to economic theories that made sense in the seventies, and maybe the eighties when SA was isolated and had no choice but to diversify horizontally and vertically," said Claude Baissac, CEO of Eunomix Research, a management consultant.

Davies and Baissac believe a better policy would be to invest the proceeds from exportation of ore into sectors – some not connected to mining – that can compete globally, and to reinvest in so-called human capital, as well as the reallocation of export income into minerals exploration. (An improved minerals cadastre, for instance, is something the government can do short-order).

In any event, the notion that SA does not beneficiate is false, according to Roger Baxter, CEO of the Minerals Council. About 95% of SA's cement is manufactured locally using locally produced minerals; 80% of domestic steel consumption is provided internally, the balance related to specialised steel grades only because SA doesn't have long enough production runs.

> "Beneficiation is very state centrist; it's naïve economically."

The list goes on: 50% of chemicals consumption is produced domestically; even 9% of the world's catalytic converters, the driving force behind the meteoric rise in palladium and rhodium, is produced in SA.

"I'm tired of this notion that SA isn't adding value," Baxter said. "If we create the right enabling framework where the commercial opportunities exist, SA will extract the right investment in the types of areas. But we can't be all things to all people."

A protective import tax is a step in the right direction, but it's not reform. That requires restructuring Eskom and stabilising investment codes. For now, the ferroalloys sector is hoping that the government's proposed tax is weighty enough for it to work. "About 40% should do it," says one industry source.

That wouldn't be out of keeping with industry norms. China, the flywheel of the world's mineral demand, applies a 35% export tax on its copper and zinc concentrate market in order to allow it to go some way to supplying itself from domestic sources. ■

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Martyn Davies
Managing director of Deloitte's unit for emerging markets and Africa

Claude Baissac
CEO of Eunomix Research

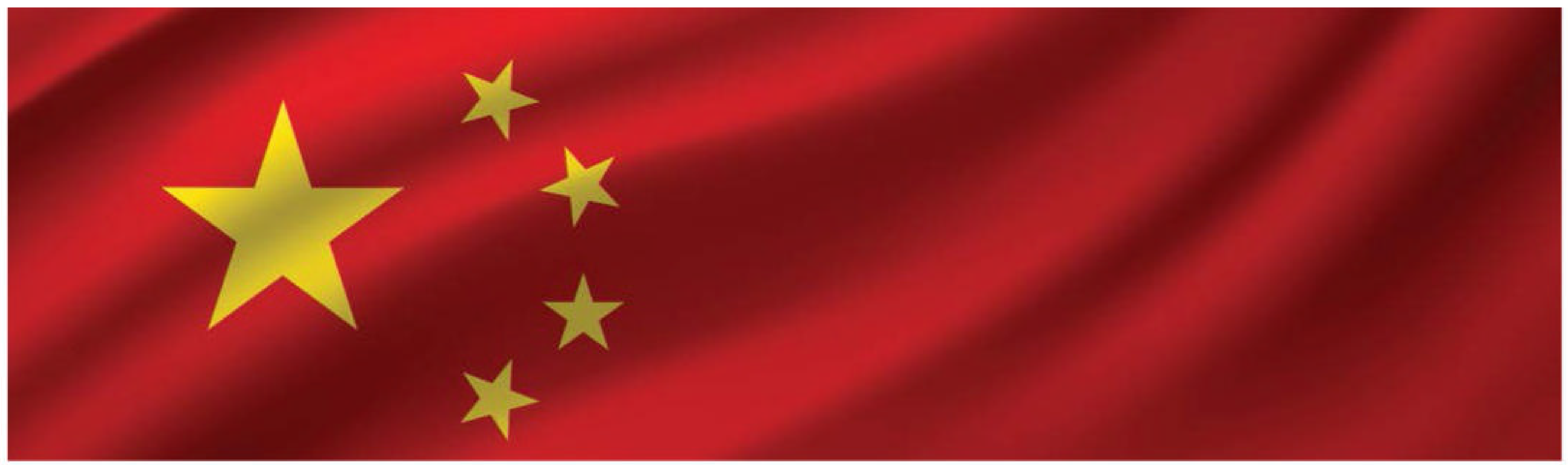
Photos: Archive | eunomix.com

By David McKay

MINING

China to the rescue again

Mining investors look forward to a 'boring' earnings season next year.



Glencore CEO, Ivan Glasenberg, made some telling comments recently on a possible work life for himself once he leaves the Swiss miner and minerals marketer, which he's run with an ironclad hand for the last 20 years.

"When I leave here, I want to go into a totally different business, where the business drives the multiples, and not the market," he said at the *Financial Times* (FT) Commodities Mining Summit in October.

Glasenberg has been preparing for his exit from Glencore for a year at least. When he does step down, he'll be the last of the so-called 'Billionaires Club' – the key executives who helped bring Glencore to the London Stock Exchange in 2013 and became fabulously rich as a result.

Notwithstanding this, mining has its limitations – principally the fact that exogenous factors influence market valuations. Mining firms are price-takers, for instance; they are also affected by pulses in economies, such as China.

Thankfully for mining firms, the Chinese economy has experienced a remarkable recovery in the months after the Covid-19 pandemic infected developed economies. "It's been identical to the 2008 crisis: the world stopped, but China kicked in," said Glasenberg. "Whatever we're losing in the western world, China is making up."

Diamond sales were 10% to 15% higher year-on-year, according to Mark Cutifani, CEO of Anglo American – a sure sign consumer markets in China had recovered, he said. "It's been remarkable and a very good sign," he said.

These comments, by two of the world's largest mining firms by value, echo the comments of investment analysts who think the mining sector dodged a bullet after the first major resurgence of the Covid-19 disease.

Commenting prior to third quarter production numbers from mining firms, BMO Capital Markets said it was looking forward to a more sedate period. "After a volatile year and with the backdrop of the US general election midway through the reporting period, we think a 'boring' or slightly positive forward-looking earnings season will be welcome," it said.

Diamond sales were
10%
to
15%
higher year-on-year.

Mark Cutifani
CEO of Anglo American

And so, it has proved, at least so far. The Bank of America (BofA) describes Anglo American's third quarter numbers in terms of "... the worst is over".

Attendees at the London Metals Exchange Week commented on the 'normalisation' of copper demand. The effect was to push the copper price to highs of $7 000 per tonne. Copper is viewed as an important bellwether for all metals in the mining complex.

Recent statistics from the World Steel Association show that global crude steel production increased by 2.9% year-on-year, driven primarily by growth in Chinese production, which is 10% higher year-on-year. Chinese production was offset in the overall numbers by a 6.8% contraction in production in the rest of the world, according to Goldman Sachs.

According to Morgan Stanley, in a note titled *Copper zooms ahead*, "... copper's market fundamentals remain broadly supportive of a high copper price – featuring low inventories, a market deficit that persists through 2021, recovering end-use markets and heightened supply risk".

The possibility of supply risk, however, remains a real one. Cutifani said Anglo had lost three months in development at its $5.3bn Quellaveco copper development in Peru because of a Covid-19 shutdown in March. It cut capital costs by $1.5bn as part of its response to Covid-19, including $300m from the three-month shutdown.

Cutifani said at the FT conference the group was likely to be relatively unscathed by the delay: It was already three months ahead of schedule so now it was 'on time'.

It's not a view entirely supported, at least by his rival Glasenberg, who commented (in jest, one supposes): "Maybe I'll hang around a bit longer, just to see if Mark is able to develop Quellaveco on time." The project, which is slated to produce some 300 000 tonnes a year of copper, is timetabled for first production in 2022. ■

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Photos: Shutterstock | Gallo/Getty Images

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FUND IN FOCUS: PRESCIENT CHINA BALANCED FUND

By Timothy Rangongo

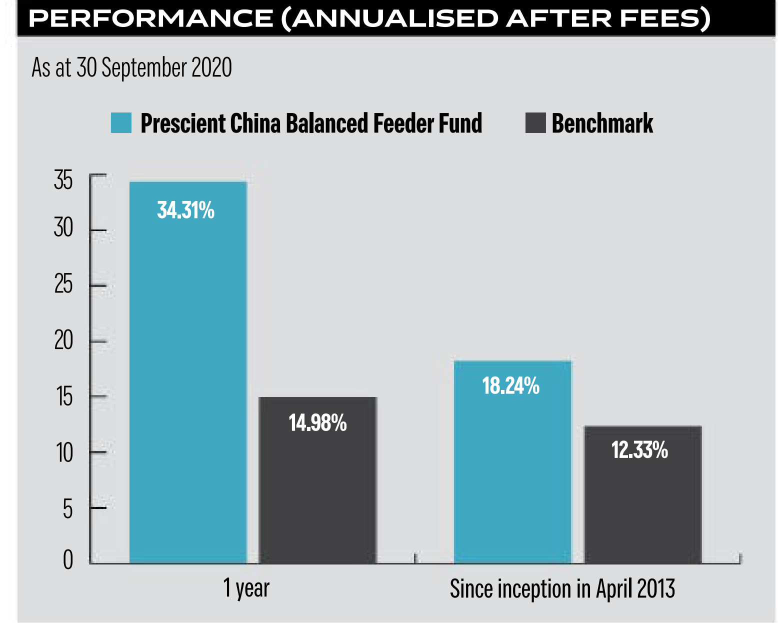
Riding the Chinese market rally

The fund aims to generate capital growth and outperform Chinese inflation by 3% over the long term.

FUND INFORMATION	
Benchmark	China CPI + 3% (in rand)
Fund managers	Liang Du and Shaun Hu
Fund classification	Worldwide – Multi-Asset – Flexible
Total investment charge	1.87%
Fund size	R238.3m
Minimum lump sum/ subsequent investment	R10 000/R1 000 per month
Contact details	0800 111 899/info@prescient.co.za

TOP 10 HOLDINGS AS AT 30 SEPTEMBER 2020		
1	Kweichow Moutai	4.4%
2	Ping An Insurance	4.4%
3	Wuliangye Yibin	2.3%
4	China Securities	2.2%
5	China Merchants Bank	2%
6	Midea Group	1.9%
7	Jiangsu Hengrui Medicine	1.8%
8	Haitong Securities	1.4%
9	Gree Electric Appliances	1.4%
10	CITIC Securities	1.4%
	TOTAL	**23.2%**

PERFORMANCE (ANNUALISED AFTER FEES)



Fund manager insights:

The Prescient China Balanced Feeder Fund predominantly invests in mainland China equities (70.87% of asset allocation), bonds (28.61%), money market and derivative instruments with an active asset allocation approach. The fund aims to generate capital growth and to outperform Chinese inflation by 3% over the long-term.

The fund's stock selection process is quite different from that of conventional asset managers according to Tian Pan, head of products and business development at Prescient China. "We use advanced mathematical modelling and technical factors to make our selection."

Examples of Prescient's considerations include selecting companies that offer exceptional quality, that are cheap and stable – as measured by the mathematical modelling. The models not only look at how individual stocks perform, but also at how they blend with one another as part of a bigger portfolio of typically at least 150 stocks.

Based on the mathematical analysis and modelling, they select a portfolio of stocks that they believe will have the highest chance of consistently beating the Chinese CSI 300 Index.

The fund's largest holding, Kweichow Moutai, is presently the world's largest distiller and the world's most valuable liquor company, having surpassed Diageo in April 2017. The company's share price rose dramatically this year (more than 20%, according to data from Refinitv), pushing its value to new highs.

China, where the Covid-19 pandemic originated, will be the only major economy to grow this year, the IMF predicted. The world's second-largest economy is forecast to expand 1.9% in 2020, compared with growth of 6.1% last year. China's growth will accelerate to 8.2% next year, the IMF estimates.

What helped the Chinese market rally, according to Pan, is that the market started off being cheap due to all the bad news from the China-US trade war. He says if we look at how the Chinese stock market is priced currently, the market is still not considered expensive compared with its own history. There's some inkling that current trends may continue in future.

Though the fund may hold instruments listed in Hong Kong, it surprisingly does not hold any Tencent stock. "South African investors already have quite a large exposure to Tencent through Naspers*, so it may not be in their interest to hold even more Tencent," Pan tells *finweek*.

Why *finweek* would consider adding it:

Apart from delivering robust returns and consistently beating its benchmark, China's market has the potential to outperform the rest of the world over the next market cycle. Mainland China stocks offer diversification benefits for SA investors. Unlike other China products on the market, there are 'no lock-ins,' meaning clients have full access to their money when they need it. ■

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REUNERT

By Simon Brown

Readying for the spend

Reunert has been under pressure. The stock trades at 2004 price levels, but the market may be seriously mispricing this share. Even as Reunert cuts its interim dividend in half, its dividend yield is in the double digits.

Reunert has ICT and defence businesses, but what's interesting to me is the engineering unit that, in part, manufactures and supplies cabling. All the talk about infrastructure spend is focusing on the construction stocks (the few left on the JSE) and those, such as PPC and Afrimat that supply the sector. I certainly like the investment case for these stocks.

But a large part of the infrastructure spend will be power related as Eskom's capacity gets boosted and Reunert will be able to supply cabling for the distribution of electricity. Further, it will do so at a much lower risk and higher margin. The construction companies always have contract execution risk, whereas Reunert will merely be a supplier of the cabling (much like Afrimat and PPC with cement). This is a much lower risk as they'd get paid and make their margins – regardless of how the construction is going. ■

Last trade ideas

BUY Metrofile
22 October issue

BUY Sea Harvest
8 October issue

BUY Aspen Pharmacare
24 September issue

BUY PSG
10 September issue

EOH

By Moxima Gama

Near-term pullback on the cards

EOH, a South African-based technology and communications technology service provider in Africa, was once the market's favourite in 2015 when it tested an all-time high at 18 000c/share. But the bullish momentum turned bearish the following year, dropping significantly in 2017 after news of unethical practices surfaced. In 2019, EOH blacklisted 50 business partners in a corruption crackdown. The group appointed an auditing firm to probe the malfeasance. This after Microsoft's decision to terminate its relationship with EOH after a whistleblower lodged a complaint with the US Securities and Exchange Commission over a dodgy tender involving a software licensing agreement with the SA department of defence. Its share price fell to 465c/share – last seen in 2006.

The share price has been trading sideways after breaching the resistance trendline of its long-term bear trend in April 2020. On 23 October, EOH's share price gained almost 17% after the technology group announced it has significantly narrowed the full-year loss due to efforts to cut and stabilise their operations.

EOH's share price gained almost 17% after announcing it has significantly narrowed the full-year loss.

How to trade it:

EOH has been trading sideways between 410c/share and 495c/share since August 2020. On 23 October it breached resistance at 495c/share – thus triggering a buy signal. With the three-day relative-strength index (3D RSI) currently overbought, a near-term pullback is on the cards. If support is retained firmly at 495c/share, go long as upside towards 630c/share would then be possible. Increase long positions above that level as EOH could gain further to next resistance at 800c/share. ■

editorial@finweek.co.za

Last trade ideas

BUY Reunert
22 October issue

BUY Transaction Capital
8 October issue

BUY Tiger Brands
24 September issue

BUY Massmart
10 September issue

Photos: Archive | reunert.co.za

By Moxima Gama

CURRO

Approaching buying levels

52-week range:	R4.61 - R18.70
Price/earnings ratio:	20.91
1-year total return:	-45.31%
Market capitalisation:	R4.22bn
Earnings per share:	R0.49
Dividend yield:	0.99%
Average volume over 30 days:	351 241

SOURCE: IRESS

SOURCE: TradingView

Curro, the private education company controlled by PSG, saw its share price slide by more than 75% over the past five years. The company, among others to reduce debt, announced a R1.5bn rights offer to shareholders in June, which was 85.3% subscribed for. PSG underwrote the offer and took the balance of the new shares, pushing its holding in the company to 60% from 55.4% prior to the offer.

Outlook: The share price is regaining upside within its major bear trend – a sign that buyers are trickling in. This upside commenced in June when the rights offer was announced.

On the charts: Curro is points away from the resistance trendline of its long-term bear trend. Breaching that trendline would mark the end of pessimistic sentiment and a gain in investor confidence – leading to a rise in the share price.

Go long: The resistance trendline would be infiltrated above 1 180c/share and a positive breakout of the bear trend would be confirmed above 1 520c/share (a key support level dated back to 2013) – go long. However, with the three-week relative strength index (3W RSI) currently overbought, Curro may reverse below the trendline as the 3W RSI corrects. If support should hold above 900c/share (655c/share), a breakout would be on the cards. Long positions could be increased above 2 055c/share as upside to next resistance at 2 925c/share (2 865c/share) could then follow.

Go short: A reversal through support at 730c/share (655c/share) would merely extend the current bear trend and Curro could retest its all-time low at 465c/share. ■

STADIO

Ending its long-term bear trend

52-week range:	R0.75 - R2.54
Price/earnings ratio:	13.17
1-year total return:	-34.32%
Market capitalisation:	R1.29bn
Earnings per share:	R0.12
Dividend yield:	-
Average volume over 30 days:	457 945

SOURCE: IRESS

SOURCE: TradingView

Private higher education company, Stadio, controlled by PSG, said in August that its student numbers jumped 10% during the fiscal year through 30 June while its revenue rose 15% to R468.2m. However, the group has swung into a R78m loss from a profit of R52m previously, due to write-offs of existing brands as it shifts to a single brand under the name Stadio.

Outlook: Stadio's share price held at 75c/share and although it's trading sideways, its bullish 3W RSI is suggesting that the bulls are returning.

On the charts: Stadio has breached the resistance trendline of its long-term bear trend and is currently trading between 200c/share and 75c/share. If support holds firmly at 115c/share, a positive breakout would be in the offing and Stadio would embark on a new bull trend.

Go long: A good buy signal would be triggered above 200c/share – thus confirming a positive breakout of the bear trend. Such a move could see Stadio's share price gaining towards the next resistance at 325c/share. Long positions could be increased above that level as buying should persist further to the 425c/share resistance mark.

Go short: Resistance encountered at 200c/share would extend the sideways trend. Downside through 115c/share could see Stadio retest its all-time low at 75c/share, in which case refrain from going long. ■

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Moxima Gama has been rated as one of the top five technical analysts in South Africa. She has been a technical analyst for 12 years, working for BJM, Noah Financial Innovation and for Standard Bank as part of the research team in the Treasury division of CIB.

By Simon Brown

STRATEGY

Technical analysis tools for long-term investing

Buying a share at the 'right' price is the only thing an investor can control in the investment process. Looking at some charts may sharpen returns in the long term.

In the 22 October issue of *finweek*, I wrote about how I am trying my hand at trading local equities for the first time in over a decade. Some aspects of my index trading have helped (discipline and risk management), but stocks are more volatile and need a different approach to my index trading methods.

What I didn't expect was how spending the extra time looking at equity charts for buy and sell signals would get me thinking about my long-term investment portfolio.

I have written before about how, as long-term investors, the only part of the entire investment process we really control is what to buy and then, most importantly, what price to pay. This is about valuations and buying great, quality companies at great prices.

After buying the stock at what our valuation tells us is a great price, we have no real control over the price subsequently. The future profits and dividends from the company are absolutely beyond our control. How the market responds to the news cycle – both big picture and company specific – and what happens to the share price as a result, is beyond our control too.

My foray into equity trading has me thinking about the price being paid for a specific stock. Sure, the fundamentals are what matters for a long-term investor. It is how we identify a stock and how we decide on the price we're happy to pay. But why not also use some charts to help determine what that price should be?

In my experience, fundamental investors consider technical analysis and reading the charts to be a voodoo science that offers no value to a long-term investor. But I have some thoughts on this.

Say, for instance, I find a stock I think would be a great addition to my long-term portfolio and, having done my valuation, it happens to be trading at or even below that valuation level. I would jump in and buy – happy that I had a great company at a great price. But what if the price has been falling and continues to fall? Usually I'd be kicking myself for not waiting and missing the cheaper entry point. But I never considered bringing some chart analysis into the equation to help me identify the current trend of the price. And this is what I want to introduce to my existing approach.

I am not looking at the technical analysis of the chart to give me a buy signal or try and get me out at the top of a trend. Rather, I want to use some quite simple technical analysis to help me determine the direction of the existing trend when I am buying for my long-term portfolio.

So, when I find that great stock and I like the price, I'll check the chart. It may tell me that currently the trend is downwards, hence I may get a better price in the days or weeks ahead. I remember sitting on an investment committee for a unit trust, and the fund manager was buying a stock that just kept falling and falling. The chart clearly showed the immediate price trend to be down, yet they were buying all the way down.

So, I am going to revisit the last couple of years of buying and see if some technical analysis could have helped. It's nothing fancy and I need to do more digging as to which analysis tool I will use. Something simple like moving averages help to identify the current trend. Even weekly charts can give a sense of the share price direction.

My overall selection process and valuation methodology will remain unchanged, but if this idea works, I'll get better entry prices on my long-term investments, which will give me better returns over time. ■

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In my experience, fundamental investors consider technical analysis and reading the charts to be a voodoo science that offers no value to a long-term investor. But I have some thoughts on this.

Photo: Shutterstock

By Simon Brown

PORTFOLIO MANAGEMENT

How to handle the shock of a market collapse

The Covid-19-induced market crash in 2020 may have been the first you experienced, but it won't be the last. Learn from it so that panic won't rule your decision-making next time.

2020 has been many things, none of them what we expected. I remember hearing about this new coronavirus in mid-January. Early reports were certainly worrisome and I was keeping half an eye on developments in China. Then, in early March, on the day the first case was announced in South Africa, I was in Durban doing a presentation on the possible impact the virus – which we now know as Covid-19 – could have on local and global markets.

We'd changed the topic of the presentation a few days earlier, as the magnitude of the virus became apparent. But even then I totally underestimated the actual impact. But I did make two predictions at that Durban event. Firstly: the impact on markets would be real, with a drop of over 30% very likely. Secondly: global economies would go into recession.

But looking back at my presentation, I realise that I was totally wrong about the actual size of the impact on the global economy. I had massively underestimated how bad it would be. For example, lockdowns led to the leisure sector having zero revenue for some six months and the industry now faces at least another two-year struggle to recover.

During this pandemic, I have also written about how to manage a portfolio in preparation for what was coming. My strategy included exiting second-tier and high-debt stocks and I continued to buy my monthly exchange-traded funds (ETFs), even as markets were collapsing in February and March.

Now, as the entire world fully enters pandemic response mode, investors can look back at the Covid-induced market collapse and ask ourselves some hard questions about our investments and our emotional response to that collapse.

For me, personally, 2020 was the fifth market collapse I have experienced. The first being back in 1987 (days after buying my first shares) and the most recent in 2008/2009. So, as markets fell this time around, I managed not to panic. I reviewed my portfolio and sold some stocks. Some of these exits proved to be inspired; others not so much, because the companies and sectors seem to have recovered strongly since the March lows. My above-mentioned strategy of continuing with my monthly ETF purchases is something I always do, regardless, and they're looking great after the buys at the March lows.

So how was your collapse? For those who only entered the market since the lows of March 2009, this would have been your first experience. How did it feel?

Was it scary? Surely it was, especially if it was your first encounter with falling markets. But did you panic and sell everything? Did you panic and stop investment contributions? Fear is fine, but panic can mean serious losses – especially if one sold during those March lows.

If this was your first market collapse, know that the fear and panic will become less intense every time this happens. I panicked in 1987 and a little less so with the next one in 1998. But dig deeper into how you felt. Was the fear that you'd lose everything? That your retirement would be cancelled? That you owned the wrong stocks with far too many high-risk shares that still haven't recovered?

Use this market collapse to review how your emotions were affected. Look at how it played out and ask if you need to make any changes to your overall portfolio construction. Do you have too much in risk areas of the market? Do you have enough diverse ETFs? Do you have enough cash to get through a tough period?

The pandemic still has some way to go, but we should start evaluating our response with regard to our investments. And if you did panic, don't stress. You'll be smarter next time because another collapse is a certainty – even if we don't know when or why. ■

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Use this market collapse to review how your emotions were affected. Look at how it played out and ask if you need to make any changes to your overall portfolio construction.

Photo: Shutterstock

By Schalk Louw

GOLD

Is there something brewing?

It doesn't matter if you see gold as an investment or a bubble waiting to explode, the fact that it must be monitored, can no longer be denied.

Data is used everywhere these days. The upcoming US presidential election is a perfect example of this. Polls are updated literally on an hourly basis, to see if Trump or Biden will become the next US president. As with weather forecasts, which also rely on data, polls are not always correct (just ask Hillary Clinton), but it helps us to make more informed decisions. I don't want to discuss the upcoming US elections, as more than enough time and reports have been dedicated to it. I rather want to discuss a secondary subject related to these elections, namely gold, and a few interesting phenomena currently manifesting in the data surrounding the metal.

Is red the new gold?

Since the Bretton Woods monetary system came to an end in 1971, the need for central banks to purchase gold also basically came to an end. It is for this exact reason that the US still has the same number of tonnes in gold reserves today, as they had in 2006. And Britain took it one step further by selling nearly half of their gold reserves between 2000 and 2002, leaving them outside of the top ten countries with the largest gold reserves. There have been many debates on whether a gold standard will make its appearance again at some point in the future. But what really interests me, is the fact that Russia and China have both been massive gold buyers over the last decade (see table).

Of the 5 172 tonnes in gold that have been purchased by central banks over the last ten years (up to 30 June 2020), Russia bought 1 544 tonnes, and China bought 893 tonnes. That means that nearly half of all central bank gold purchases were made by these two countries. It makes you wonder why...

Passivity also helped

As an investment, gold still tickles the fancy of prominent investors, but not necessarily in the form of direct gold investments. Even Warren Buffett recently made headlines by announcing that Berkshire Hathaway purchased 20.9% of gold miner Barrick Gold's shares (valued at roughly R12.5bn). But when it comes to gold investments, the purchase of gold bars remains the most popular. Of the 13 280 tonnes in gold demand for investment purposes over the last decade (up to 30 June 2020), 66% was purchased in the form of gold bars. But the interesting part of this doesn't lie in the 66%. It lies in the fact that only 11% of total demand was purchased by exchange-traded funds (ETFs). Why is this so interesting?

CENTRAL BANKS RANKED BY LARGEST GOLD RESERVES (IN TONNES)

	August 2020	Third quarter 2010	Change
United States	8 134	8 134	0%
Germany	3 364	3 402	-1%
Italy	2 452	2 452	0%
France	2 436	2 435	0%
Russia	2 300	756	204%
China	1 948	1 055	85%
Switzerland	1 040	1 041	0%
Japan	765	765	0%
India	658	558	18%
Netherlands	613	613	0%

SOURCE: World Gold Council

56% of total gold purchases for investment purposes, were made by ETFs in the last 12 months ended 30 June.

Well, although ETFs only made up 11% of gold demand over the last decade, 56% of total gold purchases for investment purposes were made by ETFs in the last 12 months ending 30 June. Is this just the herd effect, or perhaps much wiser purchases?

A thing of beauty is a joy forever if you can afford it

It is true that gold has become a political play ball over the years, but its main use is still for jewellery. More than 50% of all gold purchases over the last ten years (ending 30 June) have been made for the purposes of jewellery manufacturing. Thus, of the 1 110 tonnes in average quarterly gold demand, about 555 tonnes per quarter was purchased to make jewellery. The question I have, is what effect Covid-19 had – and still may have – on jewellery stores and manufacturers over the next few months.

Unfortunately, not unlike the rest of the world economy, the effect has been incredibly negative. For the first quarter of 2020, gold demand for jewellery declined to 321 tonnes, and in the second quarter, it declined even further to 252 tonnes. This explains why a share like Richemont is still trading 25% lower in Swiss Franc terms today (by 19 October) than its share price of five years ago (October 2015). Can this create a possible investment opportunity for investors? I think so.

It doesn't matter if you see gold as an investment or a bubble waiting to explode, the fact that it must be monitored, can no longer be denied. The data simply points to many things brewing under the surface. ■

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Schalk Louw is a portfolio manager at PSG Wealth.

Photo: Shutterstock

finweek
FUND FOCUS
YOUR QUARTERLY REVIEW OF SA FUNDS
NOVEMBER 2020
FINDING THE RIGHT INVESTMENT FILTERS
GETTING ON TRACK FOR 2021

By Leon Kok

OVERVIEW

All is not lost: How to start 2021

The fallout of Covid-19 may take many forms – from lacklustre local equity returns to the printing of money. Steering through these waters will require grit.

The past ten months have arguably been among the most problematic economically and financially since the Great Depression that followed the 1929 stock market crash.

And if ever there has been a need to go back to basics, it's now. But that said, it's not always easy identifying the best strategies, funds and/or stocks to emerge from quagmires, such as the present one.

Conversely, there is much to be said for the superb advice from the likes of Warren Buffett, such as knowing what you're investing in, identifying securities and products that will stand the test of time, and keeping a long-term mindset.

Perhaps the most predominant message emanating from portfolio managers and analysts this quarter is the need to maximise your offshore exposure. Not only are domestic earnings and prospects under enormous strain, but sadly our government is principally out of its depth in holding the fort.

Allan Gray's Sandy McGregor, in an excellent opinion piece, points to our fiscal deficit having grown so large that it's currently consuming our national savings in their entirety, and, even on the most optimistic projections, threatens to crowd the private sector out of domestic capital markets for years to come.

McGregor unequivocally warns that SA does not have the freedom to replicate developed economies in printing money.

The worst consequence of this phenomenon is hyperinflation, almost always the result of government ineptitude and fiscal irresponsibility, where price increases are rapid (usually more than 50% a month) and out of control. Among the worst cases historically are post-war Hungary and Yugoslavia; more recently Brazil and Zimbabwe; and most recently Venezuela.

According to the IMF, Venezuela's hyperinflation rate last year was a virtually unimaginable 9 586%.

Sasfin chief investment officer (CIO), Philip Bradford, also displaying considerable grit, points to the world having changed so dramatically that most balanced or pension funds in SA are out of sync with the realities of the situation. He is particularly critical of Regulation 28, which restricts them to a maximum 30% offshore exposure, forcing them needlessly towards underperforming domestic equities.

And if you think that cash is perhaps the place to be, he questions that notion too. He says that it's no longer the hiding place it was previously and could end up an atrocity with an accompanying and almost inevitable likelihood of money printing.

However, you might consider exposing yourself to Bradford's Sasfin BCI Balanced Fund, which is quite different to the ordinary and has boasted a 71% cumulative return since inception in 2013 and an annualised 6.5% during the past five years. It's ranked in the top three in the multi-asset medium equity category over most periods.

Marc Lindley, product specialist on the Ninety One investment platform, warns that if you intend making adjustments to your portfolio, beware of cashing in your retirement funds, paying the requisite tax, and redeploying the proceeds in a discretionary offshore investment.

This approach could be problematic, he says. It involves making an irreversible decision, and the net amount for investment offshore could be infinitely less than you expect. For example, a pre-retirement withdrawal of a R5m pension fund would result in nearly R1.7m of its value being lost to tax. This is the equivalent of starting the new investment with a 34% drawdown on day one. Much, of course, will depend on individual client circumstances.

A retirement annuity, on the other hand, allows for the full value to be preserved on death if the beneficiary takes over the annuity in their own name.

Which brings us to the importance of consulting an astute professional financial adviser before making irreversible decisions. According to PSG Wealth's CIO, Adriaan Pask, it's imperative to choose one who can guide you rationally, and help you see the bigger picture.

Regrettably, the SA financial sector has a history of brokers that sell products where the focus is presumably more on commission than on necessarily helping clients, he says.

Essential is that your broker treats you fairly, can add value, and that you're comfortable about the services you're paying for.

Among the costliest mistakes in the 'un-advised' client space is following performance alone and/or buying high and selling low, he adds.

We also spotlight the Ninety One Global Strategic Feeder Fund, which has notched up a spectacular annualised 14.5% return during the past decade, and the Coronation Global Emerging Markets Flexible Fund close on its heels with an annualised 13% over the same period. Both globally driven, they're up with the best and pride themselves on their persistent professionalism. ■

Leon Kok is an independent writer on public policy and investment markets.

Fund Focus will celebrate its 15th anniversary in 2021 and we pay tribute to all past and present finweek teams and contributors for their enormous energy and input. Special thanks to current acting editor Jana Jacobs and her band for their magnificent performance under 2020's extremely difficult circumstances. Wishing all our readers and supporters a wonderful year ahead.

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30 Last Word Headwinds that could become tailwinds

By Leon Kok

MARKETS

Bulking up on equities

The Ninety One Global Strategic Managed Feeder Fund has a proven track record spanning 17 years.

A fund well worth considering by those looking for offshore exposure is the Ninety One Global Strategic Managed Feeder Fund, managed out of London by Philip Saunders and Iain Cunningham.

The advantages of credible offshore multi-asset funds, of course, are that they can benefit from a broad international opportunity set and spread an investor's exposure by asset class, credit quality and currency to provide more stable returns.

The Ninety One Global Strategic Managed Feeder Fund launched in September 2003 and has R4.2bn under management. The fund has notched up a solid performance record, namely an annualised 14.5% return over ten years, 10.01% over five years and 18.1% over one year. On a quarterly basis, it turned in 7.3% in the first quarter and 10.8% in the second quarter of this year.

Its best annual return was 45.2% in 2013 and its worst -8.8% in 2008. It has been in positive territory for all but two of its 17-year existence.

Philip Saunders
Manager of the Ninety One Global Strategic Managed Feeder Fund

We spoke to Philip Saunders, who began his career in 1981 at Guinness Mahon & Co in London and specialised in fixed income and currency management before moving to a multi-asset role after Investec acquired the business. Prior to entering the financial services business, he graduated from Cambridge University with a degree in history.

What's given your fund an edge?

Firstly, we have an excellent, well-resourced and experienced multi-asset team and many of us have worked together for years. In its original form, the fund itself was launched in 1988. Secondly, we have always adopted an unbiased global approach in terms of both currency and underlying asset exposure and continue to evolve and improve our investment processes.

Finally, I think that we are good at integrating top-down macro considerations with more granular 'bottom-up' security selection. Taken together, this gives us the confidence to take high conviction views over the medium to longer term and ride out shorter-term market volatility. In short, I think that we've done a good job for our investors and fully intend to continue doing so in the future.

Your overriding objective and benchmark?

To grow capital and income over the long term. That encompasses outperforming the 60% MSCI World Index and the 40% CITI World Government Bond Index measured over a market cycle.

Your asset allocation?

The rand-based Global Strategic Managed Feeder Fund feeds directly into the Ninety One GSF Global Strategic Managed Fund, which is a globally diversified multi-asset fund with exposure to fixed income, cash, convertible securities and equities. Equity exposure is currently limited to 75% of the portfolio. Equities, of course, are the major source of returns, but they are also the riskier portion of the overall portfolio.

Any peculiarity regarding your team's investment style relative to its peers?

In equities we are relatively style agnostic – we are neither value nor growth investors – which means that we are less exposed to cycles of style underperformance. This has allowed us to achieve consistent returns over time.

We take a flexible, high-conviction approach and are prepared to deviate significantly from the reference benchmark. We pay particular attention to the longer-run structural themes that have powerful influences on the behaviour of economies and markets, such as technological disruption and the rise of China.

The new cycle ahead of us?

In many ways this represents a continuation of the old cycle, punctuated of course by the impact of Covid-19. However, we are certainly in a new 'mini cycle' and the level of fiscal and monetary support is unprecedented, so we are currently running with a very pro global growth, pro equity stance in the fund. We are beginning to favour Asian equities – particularly consumer-facing companies – and are now strategically overweight. We struggle to find medium-term value in bond markets, consequently exposure is limited, and duration is short. Dollar strength is now ebbing as dollar real interest rates decline, so we are positioned accordingly.

Any comments on the markets going forward?

The 60:40 global equity to bond benchmarks have been tough to beat in recent years because of the dominance of the US equity market, the so-called FAANG effect within that market, coupled with a strong dollar and government bond market strength in response to financial repression. But cycles change and we anticipate that the dominance of these factors will ebb.

Hence, we have been steadily increasing cyclical exposure in equities, running with low levels of bond exposure and reducing exposure to the US dollar. Somewhat controversially we think that US pressure on China will be a spur to growth there and across Asia and the quality of the companies listed in that region continues to improve.

To what extent have major technology stocks contributed to your performance?

Significantly. The adoption of internet-based business models has become ever more pervasive and we have deliberately favoured stocks on the right side of that change and not just in the tech sector per se.

Two biggest technology stocks that have contributed to your performance?

Alphabet Inc and Alibaba. They are both extraordinarily profitable and scalable businesses that have delivered excellent returns to shareholders.

Alphabet is a unique company, and this is still not fully reflected in the price in our opinion. Earlier this year it became the fourth US company to reach a $1tr market value, entering the trillion-dollar companies club for the first time. It's ranked number 15 in the Fortune 500 rankings of the largest US corporations by total revenue.

Alibaba, likewise, is the world's largest retail and e-commerce company and has the sixth-largest global brand valuation. Two years ago, it became the second-largest Chinese company by breaking the $500bn valuation mark. ■

Photo: Supplied

By Marc Lindley

RETIREMENT ANNUITIES

’Til death do us part ... with your capital!

Reallocating your retirement savings may end up benefitting the taxman and not your retirement.

Regulation 28 of the Pension Funds Act of 1956 – designed to protect retirement savings from imprudent exposure to riskier assets, including offshore assets – has frustrated some local investors of late. Local returns have lagged offshore returns, and some have argued that a discretionary investment fully offshore would be preferable to a retirement vehicle, limited as it is by regulation 28.

However, a previous article, penned by Ninety One deputy managing director Sangeeth Sewnath, discussed the impact of regulation 28 on portfolio returns and concluded otherwise. He argued that the tax benefits associated with a retirement fund potentially compensate an investor for any outperformance that might be enjoyed by increasing your offshore exposure beyond what is allowed by regulation 28, in a discretionary investment. He investigated a 30-year investment and drawdown cycle, consisting of a 15-year phase of contributions to a retirement annuity and then a 15-year spending phase, converting the consequent savings into a living annuity, so creating an income.

His calculations demonstrated that an unrestricted discretionary portfolio would need to outperform a regulation 28-compliant retirement fund portfolio by approximately 2.5 percentage points over the full 30-year period to leave an investor better off. Generating an extra 2.5 percentage points consistently over an extended period is exceedingly difficult to do.

Additionally, upon dying, the associated fees and taxes can have a huge negative impact on the remaining value of a discretionary portfolio, making the case for a retirement annuity or retirement fund even more compelling.

A retirement fund is incredibly powerful in preserving the value that can be transferred to a beneficiary on death, as it may provide protection from executor fees (up to 4.03%), capital gains tax (CGT) of up to 18% and estate duty (up to 25%). A discretionary investment can provide no such protection unless the benefit passes to a spouse on death. (It should be noted, however, that the next time the benefit changes hands, the full executor fees, CGT and estate duty would be incurred.)

Not only have local assets disappointed, but speculation about the potential for the introduction of prescribed assets has further depressed sentiment surrounding retirement fund savings. Together, this has fueled a trend, which has meant some investors have reduced their contributions to retirement funds and allocated the capital to offshore discretionary investments instead. More concerning, we have also seen some investors cashing in retirement funds, paying the tax, and redeploying the proceeds in a discretionary offshore investment.

In our view, this latter approach could be extremely dangerous. It involves making an irreversible decision, with very certain negative consequences, in fear of a change that is at this stage uncertain. When withdrawing capital from a retirement fund, the impact of the withdrawal tax tables can significantly reduce the net amount available for the offshore investment. As an example, a pre-retirement withdrawal of a R5m pension fund benefit would result in nearly R1.7m of its value being lost to tax. This is equivalent to starting the investment with a 34% drawdown on day one.

THE MATERIAL IMPACT OF TAXES AND EXECUTOR FEES

Millions

MSCI World NR USD (offshore investment) — Ninety One Opportunity A class (RA)

Withdrawal tax; Estate duty, Executors’ fees, Capital gains tax; R12 146 464; R9 604 419

Source: Morningstar and Ninety One. Performance net of fees. Starting value in offshore discretionary investment adjusted to reflect current withdrawal tables assuming the client had no disallowed contributions remaining on death. Two percentage points per year of total return for offshore investment assumed to come in the form of after-tax dividends. At death CGT, executors’ fees and estate duty deducted from end value in offshore investment, assumes R3.5m abatement used elsewhere.

The impact of this is illustrated in the accompanying graph. And while offshore equities remain our preferred asset class across our multi-asset capabilities, it is unlikely that the trend experienced over the past decade will persist at the same magnitude into the long-term future.

Over the ten years to end December 2019, global equities outperformed the Ninety One Opportunity fund by 7.4 percentage points in rand terms, and thus provided a perfect tailwind for an offshore investment strategy. Despite this significant outperformance, however, it would have taken more than eight years before the offshore discretionary strategy starts to move ahead of the retirement fund investment, due to the reduced starting value. The other consequence of taking funds out of a retirement product and placing them in a discretionary investment means that those funds now form part of your estate. Therefore, when you die the fees and taxes associated with death have a destructive impact on the total value that can be received by your beneficiaries.

A retirement annuity, on the other hand, allows for the full value to be preserved on death if the beneficiary takes it over as an annuity in their own name.

Thus, we believe clients should fully consider the significant financial planning benefits presented by retirement annuities before deciding how they allocate, or reallocate their savings. As outlined, the outperformance required to compensate for the lost tax benefit is extreme, while factoring in the estate planning benefits make a retirement annuity almost impossible to beat.

The extent of the benefits will vary based on individual client circumstances, so as always, we suggest investors consult their financial adviser before making irreversible decisions. ■

Marc Lindley is a product specialist at Ninety One’s investment platform.

Photo: Shutterstock

By Leon Kok

STRATEGY

Choosing your investment vehicle

Cash is now like a safe car with a top speed of only 30km/h. In the same vein, bonds are also relatively safe, but can reach a top speed of 120km/h, delivering better returns than 'super-safe' cash.

The world is rapidly changing and now may be the time to seriously re-examine your approach to asset allocation, according to Philip Bradford, Sasfin's chief investment officer and multi-award-winning portfolio manager.

He points out that during the 1980s, interest rates in the US, UK and Europe were mostly between 10% and 20%, and currently they're zero or even negative. Locally, they're close to their lowest in history and seem destined to remain there for some time.

Over that same period globally, stock markets generally did well, with the JSE being one of the best performers in the world, he adds. And significantly, despite recent poor performance, it remains one of the top performers over the past 120 years.

Bradford notes further that the US stock market, after delivering zero returns from 2000 to 2010, rocketed during the past decade, but is unlikely to maintain anything like that momentum in the decade ahead.

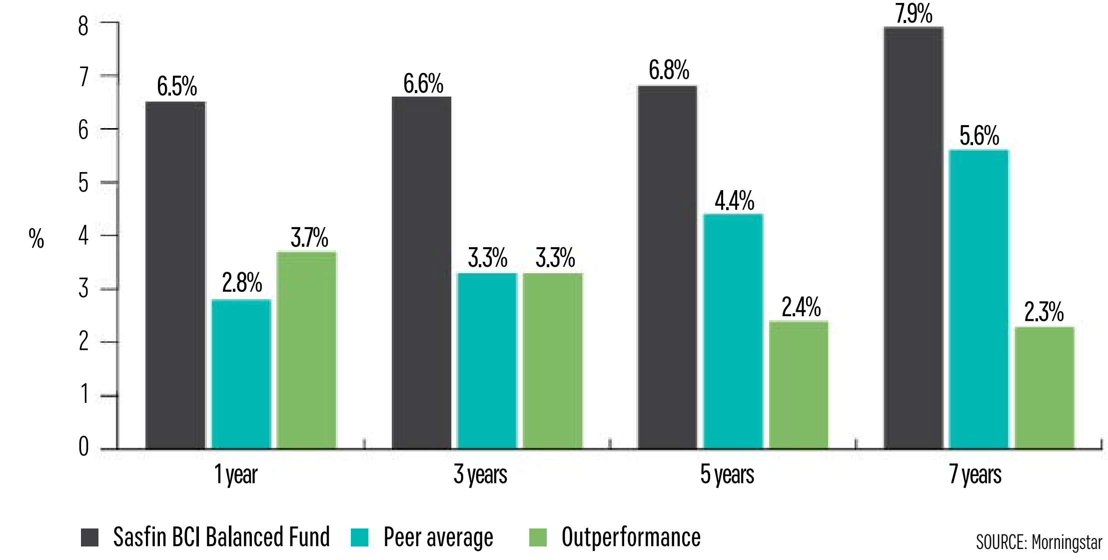
Against this backdrop, he asks: "Given that interest rates are at all-time lows in most places around the world, and with the prevailing uncertain economic and stock market outlook, does it still make sense to repeat the way you invested during the past 30 years?"

South African investors were generally spoiled during that period, he says. "Our stock market, bonds and even cash averaged double-digit returns per year, comfortably beating inflation. Many investors continue to assume that given this situation, they ought to comfortably outperform inflation by more than six percentage points per year into the future if most of their retirement savings are invested in the JSE.

"This has resulted in SA pension funds typically placing 65% to 75% of their assets in stock markets, with the large majority of that in the JSE and much less to global equities. Obviously, this hasn't paid off in the recent past because even cash has beaten the local stock market by a mile".

While recognising this, Bradford's team adapted their investment strategy to the changing environment. "In the Sasfin BCI Balanced Fund during the past six years, for instance, we significantly reduced our investors' local equity exposure in favour of both high-yielding local bonds and foreign equities, culminating in exceptional returns and the fund winning a coveted Morningstar award earlier this year.

SASFIN BCI BALANCED FUND (PERFORMANCE ENDING 30 SEPTEMBER 2020)



"Particularly poignant is that certain local bonds are more attractive than ever, currently yielding between 11% and 12%. Meanwhile, excellent opportunities on the local stock market have significantly reduced or become less attractive".

This means, says Bradford, that some local bonds in the fund now provide a guaranteed return of eight percentage points above current inflation. It's extremely attractive considering that the riskier stock markets typically return a mere five to six percentage points above inflation.

> "Certain local bonds are more attractive than ever, currently yielding between 11% and 12%."

"Most pension funds, I believe, should consider changing their asset allocation policies to take advantage of this. The Sasfin BCI Balanced Fund currently has only 15% invested in the local stock market, compared with the average SA pension fund manager's 40% or more invested in local equities. Clearly, Bradford says, when bonds with much lower risk deliver better returns than you might have hoped from local equities, it doesn't make sense to take more risk than you need to.

He also humorously likens domestic equities to an old Ford Cortina XR6: "Really fast in the 80s and 90s, but not a reliable bet in 2020."

Another reason for most pension fund managers being excessively exposed to local equities is that they're bound by pension fund regulations, Bradford says. "These rules restrict a fund's offshore exposure to 30%, which almost forces a manager of a fund with a high growth target to be overly skewed towards domestic equities.

"And inimically the FTSE/JSE All Share Index currently has little exposure to the SA economy, essentially being a largely global index with very concentrated exposure to a handful of companies".

Looking forward, Bradford reiterates that the outlook for local and global equities is uncertain and cash is no longer a safe hiding place that will provide high returns like it did in the past.

"I believe that investors should have the majority of their equity exposure invested offshore and most of their local exposure in SA in bonds that pay very high interest. In SA you no longer need to take inordinate risk to comfortably beat inflation."

"Cash is no longer an option because the rates are close to 3% and are likely to stay low for a long time", he says. "So, ironically, cash has become a riskier investment in that it virtually ensures that you won't achieve your retirement goals. "It's like a very safe car with a top speed of 30km/h, whereas with bonds you are also relatively safe, and the vehicle is comfortably able to travel at 120km/h." ■

By Christo Lineveldt

OFFSHORE

Do you have sufficient emerging market exposure outside of SA?

One of the pioneers in emerging market investing has outperformed the MSCI World Index by more than 100%.

For many South African investors, the thought of investing in other emerging markets (EMs) may seem counterintuitive. Some would argue that you have enough EM risk, already living and earning income in one. But there are many compelling reasons to consider actively managed exposure to EMs outside of South Africa.

Take advantage of long-term trends that are not apparent in SA

More than a decade after we launched our specialist EM equity funds back in 2007, we remain bullish on the long-term prospects for EM equities. The key structural drivers supporting EM growth are still in place and we continue to find attractive stock-picking opportunities in multiple geographies.

The EM universe is full of businesses that can take advantage of growth tailwinds that are absent from the developed world, and only mildly present in SA. The rising wealth trend has catapulted hundreds of millions of consumers into the middle class, meaning that they have growing discretionary spending power that has far-reaching consequences across industries, such as travel, insurance and personal transport. Growing personal wealth also drives a premiumisation trend, where consumers display a preference for branded items, such as luxury goods and fine wines and spirits. Finally, the formalisation trend means that we will continue to see many sectors, such as food retail and financial services, grow at the expense of informal competitors, allowing industry leaders to continue growing their market share.

Don't I get EM exposure through a global equity fund?

EMs are chronically underrepresented in these portfolios. Global equity benchmarks typically devote about 87% of their exposure to developed markets and 13% to EMs. However, the global economic reality is that, while more than 80% of the global population live in EMs, these countries still only represent approximately 50% of global GDP and 20% of equity market capitalisation.

As many global equity funds largely ignore or typically under research some of the most exciting and fastest-growing EM investment opportunities, we believe that actively managed portfolios that benefit from an extensive research effort across the full EM opportunity set can thus add significant value to SA investors who are looking to gain exposure to the best opportunities in these markets.

Accessing EM opportunities with Coronation

Investors can access full exposure to EMs in rand or dollars through our actively managed specialist equity EM funds. However, most investors may prefer exposure to these markets through a flexible mandate, where the fund manager decides on the optimal allocation to EMs on your behalf, such as the Coronation Optimum Growth fund.

The fund pioneered the uniquely flexible worldwide multi-asset mandate 21 years ago and provides an attractive entry point for investors wanting to benefit from the EM opportunity set. Optimum Growth's investment universe includes local, EM and developed market assets and is unconstrained by fixed strategic asset allocation limits.

Since its launch in March 1999, its managers have made good use of the inherent flexibility of its worldwide mandate, delivering more than double the return of the MSCI World Index over this period. ■

Christo Lineveldt is an investment specialist at Coronation Fund Managers.

THE POWER OF ALPHA IN A FLEXIBLE MANDATE

Growth of R100 000 invested on 15 March 1999
(Coronation Optimum Growth Fund vs. the MSCI World Index)

Outcome when invested in the index*
R801 000

Outcome when invested in Coronation Optimum Growth
R1.1m
+
R801 000

R1.9m**
MORE THAN DOUBLE
the index after all fees

SOURCE: Performance fees quoted net of fees from Morningstar as at 30 September 2020 for a lump sum investment with income distributions reinvested.
*MSCI World Index
**Since inception of the A-class in March 1999

For detailed information on the retail class of Optimum Growth, refer to its comprehensive fact sheet.

Photo: Shutterstock

> The EM universe is full of businesses that can take advantage of growth tailwinds that are absent from the developed world, and only mildly present in SA.

By Sandy McGregor

OPINION

The dangers of printing money

Sandy McGregor, portfolio manager at Allan Gray, debunks modern monetary theory and examines if it provides a solution to economic woes.

Modern monetary theory, or MMT as it is often called, is a new term for an old idea. Its proponents argue that a state, which issues fiat money does not have to resort to taxation and borrowing to pay its bills. It can fund itself simply by printing money. While there are numerous historical examples of unfunded fiscal spending being followed by hyperinflation and economic collapse, the modern supporters of what would previously have been regarded as economic heresy, say this time it is different.

The simple truth is that central banks in the US, Europe and Japan have been applying the precepts of MMT for the past decade and in responding to the Covid-19 pandemic have abandoned any sense of traditional financial prudence.

The US Federal Reserve (the Fed) has been the most aggressive, increasing its balance sheet from $4tr to $7tr over the three months following the market meltdown in March. Most of this $3tr of new money has been used to fund an exploding federal fiscal deficit. The balance sheets of the Fed, European Central Bank and Bank of Japan have collectively increased by $6.3tr this year. MMT has arrived almost by accident. Its longer-term unintended consequences pose a grave risk to the financial stability of the global economy.

The political allure of unconstrained government spending

For centuries, a golden rule of public finance has been that a state should live within its means. Fiscal spending should not exceed sustainable tax revenues and prudent borrowing. The wisdom of this precept was confirmed when governments tried to sustain economic growth by Keynesian deficit spending into the recession triggered by the first oil price shock in 1973. The consequence was damaging inflation, which was only brought under control in the early 1980s when the Fed raised dollar interest rates to levels that caused a serious recession. Following this bad experience, financial prudence again became the guiding principle of public finance.

In recent years, in many countries the political leadership has become increasingly restive about the constraint on government spending imposed by what generally have been regarded as prudent targets for fiscal deficits and the appropriate stock of government debt relative to GDP. This is not restricted to the political left, which usually favours increased expenditures. In the US, the Republican Party has pushed through major tax cuts and in the UK, Prime Minister Boris Johnson has abandoned Margaret Thatcher's legacy of fiscal conservatism. Usually the justification offered is pressing need, for example to combat climate change, to meet the growing cost of healthcare as the population ages, renovating ageing infrastructure and expenditures to address poverty. The argument against these expenditures has been that, however desirable, they are unaffordable.

The present orgy of spending financed by printing money sets an alarming precedent. It seems to give the lie to the idea that public spending must not exceed available resources. Politics is like water. It flows downhill by the easiest path. The rapidly developing habit of using central banks to finance governments is going to be difficult to break. MMT is a dangerous drug to which political elites can easily become addicted.

The developed economies of the northern hemisphere can pursue imprudent fiscal policies because in the current deflationary environment they can get away with it, at least in the short term. They have large, diverse and robust economies. In the case of Europe and Japan, they have external surpluses, so are less vulnerable to capital flight. The US enjoys the inordinate privilege of the dollar being the world's reserve currency. Even though in all likelihood these nations are creating serious problems for the future, they have the freedom to be irresponsible without immediate adverse consequences. The same does not apply to emerging markets and, in particular, does not apply to South Africa.

SA's immediate problem is a paucity of domestic savings. In recent years we have been trapped in economic stagnation. There is widespread agreement that escaping from this unhappy situation will require increased investment by productive enterprises. Unfortunately, our fiscal deficit has grown so large it is currently consuming our national savings in their entirety and even on the most optimistic projections threatens to crowd the private sector out of domestic capital markets for years to come.

Foreigners who invest in emerging markets are particularly neurotic about governments that are unconventionally imprudent. They wish to avoid investing in a country that will become the next Zimbabwe, Venezuela or Argentina. Among the warning signals that would prompt instant capital flight is funding the government through the central bank by printing money. If SA started doing this, an exodus of capital would make financing its fiscal deficit more difficult and expensive. Even the dollar has weakened 8% following the Fed's massive creation of money earlier this year. The rand would be much more vulnerable. There is a lot of foreign money in SA, including about R500bn in government bonds, the owners of which could panic. The rand would weaken with inflationary consequences, which would force the Reserve Bank to increase interest rates. While there would be immediate short-term costs, even more damaging would be the long-term consequences of exclusion from international capital markets. Who in their right mind would invest in a country, which is adopting the policies that bankrupted Zimbabwe?

> The present orgy of spending financed by printing money sets an alarming precedent.

While funding SA's fiscal deficit is a formidable challenge, we do not have the freedom to copy developed economies and print the money. To do so would make matters even worse. MMT is not for us. ■

Sandy McGregor is a portfolio manager at Allan Gray.

Photo: Shutterstock

By Adriaan Pask

FINANCIAL ADVICE

Avoid costly mistakes by using a trusted financial adviser

Behavioural change and teamwork are key to securing enhanced long-term returns.

Regrettably, the South African industry has a history of brokers that sell products, where the focus was presumably more on commission than on necessarily helping clients. That said, it would be short sighted to discard the value of advice purely based on that perception, and then fly solo. Investors can actually be more comfortable with advisers. In recent years, regulators have been working to make the financial services industry more credible and passed an array of legislation to ensure that customers are not just treated fairly, but that they also understand the services they are paying for.

However, the real solution is finding a financial adviser that you feel adds value. There are numerous studies, which show that investors who use advisers perform better than those who don't, even after paying advice fees. A 2019 study from Vanguard found that "based on our analysis, advisers can potentially add about 3% in net returns". This is based on a variety of factors, which include an adviser offering behavioural coaching, teaching investors to be strategic with withdrawals, effectively allocating assets to meet the investor's goals, strategic rebalancing and the implementation of cost-effective strategies (see **graph 1**).

Advisers can provide valuable artillery

In times like these a good financial adviser should offer clients two pieces of valuable artillery – the ability to guide them rationally, and to see the bigger picture. These are the greatest tools an investor can hope for in an environment that has beaten investors down and has severely tested them.

Too often we see investors obsess over fund performance numbers as published through a wide variety of mainstream media and commercial publications. Yet, there seems to be too little cognisance of the fact that, even if you were to find the best fund portfolio, odds are the average investor's experience was, or is, and probably forever will be, very different. That is because investing is a process that is susceptible to human emotional interference. Investors rarely remain undeterred by news or market movement, and simply remain invested. Instead, they can panic, or make poor decisions, for whatever reason.

A 2018 study by Dalbar states that "there is no shortage of research (see **graph 2**) showing how investors are often their own worst enemies, sabotaging themselves by making emotional decisions or resorting to market timing and performance chasing".

This is exactly where a good financial adviser can be valuable. In tough times, an adviser should guide and advise you how to avoid making mistakes; to think rationally about your investments, your goals, and how to achieve them. Typical mistakes that are avoided through this process are often the costliest mistakes we see in the 'un-advised' client space – following performance or buying high and selling low.

Large asset managers have opened funds for direct investment in line with market demand, and there is nothing wrong with that. An investor has choices, and they must just understand what they are paying for, and what they are not paying for; what risks are they mitigating, and which risks they are not mitigating. By going direct, you reduce your costs, which is good, but what are the risks of going it alone? What are the risks that you will have to navigate yourself?

If you are comfortable with your answers to these questions, then you are always able to invest without the help of an adviser, but it is unlikely that you will generate superior returns. Even the best fund managers in the world operate in teams, precisely because checks and balances, as part of an overall process, help to counter our individual biases. ■

Adriaan Pask is the chief investment officer of PSG Wealth.

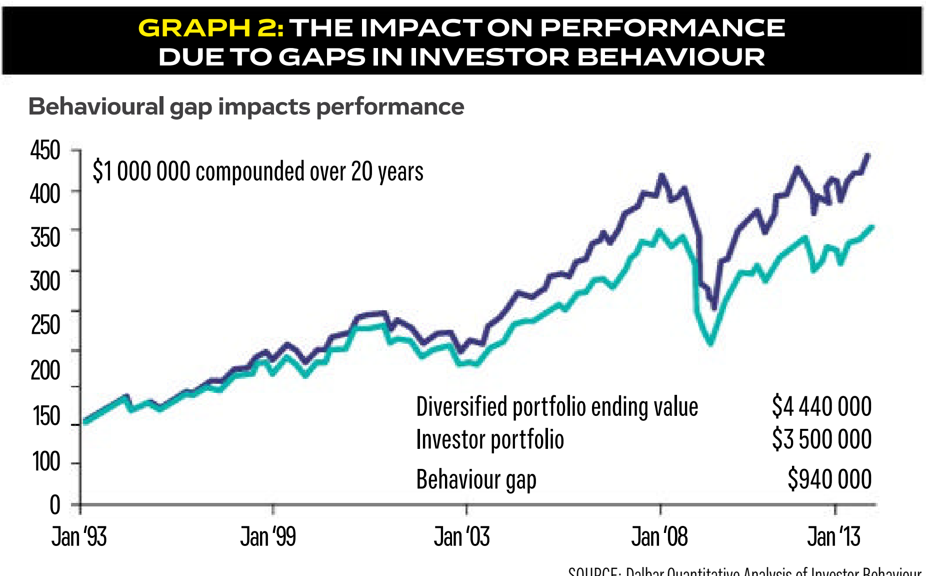
Photo: Shutterstock

GRAPH 1: ADVISERS COULD ADD 3% TO INVESTORS' NET RETURNS

1.5% Behavioural coaching
0.55% Being strategic with withdrawals
0.38% Effective asset allocation
0.6% Strategic rebalancing and cost-effective implementation
0.0 0.3 0.6 0.9 1.21 1.5

SOURCE: Vanguard – Putting a value on your value.

GRAPH 2: THE IMPACT ON PERFORMANCE DUE TO GAPS IN INVESTOR BEHAVIOUR



SOURCE: Dalbar Quantitative Analysis of Investor Behaviour

FUND PROFILE

The PPS Global Equity Fund

Providing investors with access to a top international investment manager.

In the current market conditions, offshore investing has become vital in diversifying your investment portfolio, as it offers an opportunity to adequately benefit from a greater investment universe. When you have offshore exposure, it means that you're spreading your risk – or diversifying – geographically. Diversification across different asset classes, asset managers, geographical locations or investment strategies means that at any point in time you have exposure to an element in your portfolio that, when optimally combined, should act in a complementary way. Your portfolio is therefore better able to withstand fluctuating market conditions, creating smoother returns over the long run.

But investing offshore can be a difficult landscape to traverse with various ways to do so. Some of the common approaches are through opening an offshore bank account, or investing in unit trusts that offer offshore asset class exposure. When selecting unit trusts, an important aspect to consider is choosing an asset manager with extensive knowledge and experience to navigate the large universe of stocks and markets available, while having a keen understanding of the global market place and where to find value. As a multi-manager, we spend a substantial amount of time finding exceptional asset managers through our extensive quantitative and qualitative research screening and selection process. We embarked on this process to find a partnership manager for our newly launched offshore solution, the PPS Global Equity Fund (US$) and the PPS Global Equity Feeder Fund (ZAR), as part of our PPS Partnership Fund range. The manager selection for this fund bears testimony to our process, having partnered with one of the largest and oldest managers in the world.

Capital Group was founded in the US in 1931, during the Great Depression. Today, they are one of the world's largest active managers, with

$2.1tr

under management.

Introducing Capital Group – partnership manager for the PPS Global Equity Fund

Capital Group was founded in the US in 1931, during the Great Depression. Today, they are one of the world's largest active managers, with $2.1tr under management (as at December 2019) in equity, fixed income and multi-asset portfolios. They are an employee-owned private company that is solely focused on investment management. They have a strong focus on global equities, which they have been managing since 1953, and they started managing the first emerging market equity fund in 1986. Global equities account for the majority of their assets under management.

Backed by an in-house research team consisting of more than 400 investment professionals globally, a dedicated team of experienced portfolio managers oversee the strategy for the PPS Global Equity Fund. These portfolio managers are based across the globe, giving the team a truly global focus.

What makes Capital unique?

Capital employs a multi-councillor approach to investing by allocating a portion of the fund to each of the portfolio managers and a portion to the research team. This approach seeks to achieve the best of both worlds: the high conviction of individual managers and the diversification of a team approach.

Collectively, the portfolio managers have a median of 29 years' industry experience, and 28 years of experience with Capital (as at December 2019). Due to the long tenure of the portfolio managers, the principal investment officer has an excellent knowledge of the individual portfolio manager's investment philosophies and style, ensuring the portfolio is diverse in terms of style and allocations. Each portfolio manager is given the freedom to express high convictions in their allocations. The multi-councillor approach can be likened to the way we as a multi-manager combine the skills and expertise of managers.

How this manager creates wealth

Capital is a well-established manager with a strong performance history through various market cycles. Their time-tested strategy has uncovered opportunities from changing patterns of world trade for 45 years. Using a bottom-up, research-driven approach that focuses on a combination of early stage and established multinationals, has fared well over the years. A multi-councillor approach to investing helps to diversify the fund to ensure smoother returns over the investment horizon, reducing factor and style biases.

Capital has an established track record across different strategies, delivering long-term growth through the market cycles. We believe we have found an exceptional manager who shares a passion for creating wealth, who understands the value of multi-management and how diversification can ensure smoother returns over the long term.

Offshore investing made accessible

As an investor, you may not have the resources or appetite to research offshore investment options. Investing in the PPS Global Equity Fund and the PPS Global Equity Feeder Fund (ZAR) gives you access to a top international investment manager with a proven track record through various market cycles. Speak to your financial adviser about diversifying offshore within your holistic financial plan. ■

*Contact your PPS Investments accredited financial adviser or call us on **0860 468 777** (0860 INV PPS) or email us at **clientservice@ppsinvestments.co.za***

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By Leon Kok

OUTLOOK

Headwinds that could become tailwinds

Emerging markets may yet see a strong rebound next year.

Many friends, colleagues and associates I meet these days seem to have been completely paralysed by the present situation.

Their biggest fear is that the world financial system is headed for collapse. This is underpinned, for instance, by various research outfits beckoning that, while the first Covid-19 wave has wreaked havoc, a second one could be far worse.

The huge slump that could follow, they argue, could take a huge bite out of your nest egg. They propose that you ought to start financial distancing at the very soonest to protect your money. The worst-case scenario could be a sink-or-swim situation over the next few years.

These contentions are often compounded by successive news broadcasts, each more disturbing than the last.

But what's new? We've been through this before, notably the collapse of the Soviet Union in the late 1980s, the bombing of New York's World Trade Centre in 1993, the 1998 Asian financial crisis, the rising threat of radical Islam, the 2008 financial collapse, and Greece and Italy's singular crises more recently.

The extreme projections may or may not materialise, but there is also a case to be objective and prudent in your approach.

Ideally, one needs to be invested across the planet (not being dependent on one particular geography); be exposed to companies that provide day-to-day necessities, such as Unilever, Johnson & Johnson and Nestlé; have sound long-term performance records; and can bank on dividend yields in the region of, say, 3%.

The outlook for Asia Pacific, for instance, looks particularly promising, with a likely regional GDP rebound of about 6.6% next year, which includes China at 5.4%, Vietnam and Cambodia at 6% each, and Singapore at 3%. Japan, of course, will remain a laggard due to constrained monetary policy and deflationary dynamics.

In the West, a projected 4.5% economic growth for the US is not unreasonable. The re-election of Donald Trump may well benefit US stocks (tax hikes averted, more protectionism), and a victory by Democratic presidential candidate Joe Biden could possibly benefit non-US shares (more harmonious foreign and trade relations). Any significant dislocations after the elections could provide good buying opportunities.

For instance, the second stage of the post-coronavirus economic recovery should favour undervalued cyclical value stocks over expensive technology and growth stocks.

Europe's recovery should continue over the coming quarters. It is more exposed to global trade than the US and ought to be a beneficiary of a rebound in Chinese demand. In the UK, Brexit will dominate the outlook.

Broadly, my choice at this point would be diversification into a top-rate emerging market (EM) vehicle, such as the Coronation Global Emerging Markets Flexible Fund. EMs are growing at superior rates relative to their developed counterparts and collectively comprise 60% of the global economic pie. The IMF, for instance, forecasts that collectively, EM GDP growth will contract by 3% this year but rebound by close to 6% next year.

Attractions include ongoing favourable demographic and productivity trends; faster growing consumption than in developed economies; commodity prices are likely to rise, especially if supply has been curtailed as a result of the Covid-19 crisis; direct funding by central banks currently of fiscal stimulus programmes; and the dollar is likely to be less buoyed by its status as a 'safe haven', given that it's largely overvalued.

Managed by Gavin Joubert and Suhail Suleman, the Coronation Global Emerging Markets Flexible Fund has generated an annualised 13% over ten years, 16.1% over five years, 9% over three years, and 25.4% in one year.

Over the past 14 years Coronation has built a global and global emerging market (GEM) team of 18 investment professionals with detailed stock coverage. The process started with the launch of the investment house's GEM funds in 2007, followed by the launch of global funds like Coronation Global Managed in 2009.

Besides being a well-resourced and experienced team by international standards, the house's knowledge of global stocks grew consistently, enabling a continued delivery of attractive risk-adjusted returns for investors.

Joubert and Suleman concede that they expect difficult times ahead in several EMs from an economic perspective, particularly those with poor country balance sheets and weak economies, such as SA and Brazil, but emphasise that they're extremely selective with stock selection in these countries. Even within them, some companies will benefit tremendously from the acceleration in digital adoption in many industries, a by-product of the Covid-19 crisis.

China, on the other hand, is considered one of the better bets, partly because it locked down hard and early, partly because its economy was reasonably strong before Covid-19, and it boasts attractive fundamentals. Some 35% of the Global Emerging Markets Flexible Fund is invested in China, and 40% if Naspers* is included.

EMs are growing at superior rates relative to their developed counterparts and collectively comprise **60%** of the global economic pie.

India has the second-largest country exposure at 9.5%, with 6% of this invested in financials. Russia is third at 9.1% with four investments, notably X5 Retail, Magnit, Yandex and Sberbank.

Developed market exposure (domiciled in developed markets but with large EM exposure of sales or profits) is currently 15.5%, which is lower than its 12-year average of 17%.

The largest positive contributors to performance in the second quarter of this year were Wuliangye Yibin and JD.com (China); Magnit and Yandex (Russia); and MercadoLibre (Latin America).

Holdings that have been marginally reduced include Naspers*, Alibaba, NetEase, Tencent and Taiwan Semiconductor. The only new buy has been Hong Kong Exchanges and Clearing (HKEX), which is the monopoly stock exchange operator in Hong Kong. ■

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By Lucas de Lange

JSE

The bull raises its head

Government should seek the advice of a prosperous Japan when it comes to bringing about sustainable recovery.

Over the past few weeks there has been a considerable improvement among the top 100 shares on the JSE – measured by market cap.

This is reflected in the fact that 51% of the shares are currently lying above their 200-day exponential moving averages (EMAs), which means that the bull has now asserted itself for the first time this year, even though it has only just managed to do so. In October, only 30% of these shares were trading above their 200-day EMAs. How bad things have been is evident from the fact that only 4% of the top 100 was lying above their 200-day EMAs during the difficult lockdown in March and April.

There have been major changes on the list of the strongest shares after mining counters, especially gold and platinum, have been setting the pace for quite some time. Montauk Holdings, which specialises in renewable biogas-fuelled energy projects, is now on top of the list. Montauk reports that it has been given the green light by the Reserve Bank to list on the Nasdaq in the US. It will retain a secondary listing on the JSE. It hopes to move to the Nasdaq early in 2021.

Among the weakest shares, property groups are dominant, with only Nampak and Sasol – two South African industrial giants that are both experiencing serious headwinds – to keep them company.

Some property companies are, however, making positive sounds. There have been statements that rental collection and foot traffic have improved at retail centres since the lockdown levels have been eased. But judging by the position of major property groups in the table, investors still seem to be sceptical, even though government is hoping to get growth and jobs up and going based on President Cyril Ramaphosa's recently announced plan.

From comments made by economists and business leaders it is, however, evident that they are disappointed as the drive will be managed by the state. As economist Dawie Roodt has said: The government has as yet not succeeded with a single project. Jonathan Oppenheimer, grandson of the late Harry Oppenheimer (in his day, one of the ten richest men in the world) who headed up Anglo American for many years, probably expressed it best at the *Financial Times* Africa Summit in October. He called on governments to focus more on attracting investments and creating jobs rather than trying to manage the economic recovery efforts using bureaucratic rules. Set boundaries and then step aside so that people can innovate and be dynamic, he urged.

It is interesting that this is precisely what gave rise to the framework for the 'miracle' that took place in a devastated Japan after World War II. The country's leadership decided, with the support of its American occupiers, to leave the recovery of the economy in the hands of entrepreneurs, mainly subject to a good, independent legal system (the American Supreme Court acted as role model). The involvement of the government would be limited. The result was astounding: The economy grew on average by 9.75% a year over the next 20 years. (SA did, however, also muster an average growth rate of 9.3% from 1963 to 1968.) The big winner was Japan's automotive industry. The growth rate here was about 29% a year from 1966 to 1972 in the midst of fierce competition. Even education was mainly reserved for the private sector, which led to courses being designed to meet the needs of the economy.

In the area of labour, the trade unions developed a positive plan. They designed a system of specialised committees to constantly promote productivity. This greatly benefitted companies and obviously did wonders for relations with employers.

Japan's decision to follow a free market system to help it recover from a devastated economy caused it to become one of the most prosperous countries in the world up until today. ■

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

STRONGEST SHARES*

COMPANY	% ABOVE 200-DAY EMA
MONTAUK	85.2
CARTRACK	61.1
TEXTAINER	54.2
NORTHAM PLATINUM	35.1
ARM	34.6
MC GROUP	33.9
ROYAL BAFOKENG PLAT	26.4
SIBANYE-STILLWATER	24.3
ITALTILE	21
IMPALA PLATINUM	19.8
SHOPRITE	18.4
MPACT	16.9
CAPITEC	16
TRANSACTION CAPITAL	14.7
TIGER BRANDS	14.2
GOLD FIELDS	11.8
KUMBA IRON ORE	11.8
MASSMART	11.3
PAN AFRICAN RESOURCES	10.8
ZAMBEZI PLATINUM PREF	10.4
HARMONY	10.3
RMI HOLDINGS	9.7
DISCOVERY	9.6
WOOLWORTHS	9.1
CLICKS	8.7
PSG KONSULT	8.3
ANGLO AMERICAN	7.9
PEPKOR HOLDINGS	7.3
AVI	7.2
PROSUS	5.7
NASPERS	5.3
MEDICLINIC	5.1
PICK N PAY	4.9
TFG	4.8
MONDI	4.7
DRDGOLD	4.2
SPAR	3.8
SIRIUS	3.7
ABSA GROUP	3.7
CORONATION	3
RICHEMONT	2.7
VODACOM	2.3
IMPERIAL	2
MR PRICE	1.8
SAPPI	1.5
SOUTH32	1.5
THARISA	1
EQUITES	0.6
MERAFE RESOURCES	0.5
STANDARD BANK	0.4
EXXARO	0.1

WEAKEST SHARES*

COMPANY	% BELOW 200-DAY EMA
HAMMERSON	-95.4
NAMPAK	-61
FORTRESS B	-48.7
VUKILE	-40
REDEFINE	-35.5
SASOL	-31.4
CAPITAL & COUNTIES	-29.8
NEPI ROCKCASTLE	-23.4
RESILIENT	-19.8
INVESTEC LTD	-19.4
ASTRAL	-19.1
GROWTHPOINT	-19
INVESTEC PLC	-18.9
LIBERTY HOLDINGS	-16.4
REMGRO	-16.2
HYPROP	-15.1
OLD MUTUAL	-15
RCL	-14.7
BARLOWORLD	-12.8
MOMENTUM METROP	-10.6
NEDBANK	-9.8
BIDCORP	-9.4
ASPEN	-9.2
REINET	-9.2
BAT	-9.2
MTN GROUP	-9
TELKOM	-9
SANLAM	-8.9
VIVO	-8.5
RHODES	-7.5
GLENCORE	-6.7
ANGLOGOLD ASHANTI	-6.2
LIFE HEALTHCARE	-5.8
TRUWORTHS	-5.1
BIDVEST	-5
QUILTER	-4.5
SANTAM	-4.4
AB-INBEV	-4.3
OCEANA	-3.3
SUPER GROUP	-2.6
DIS-CHEM	-2.4
JSE	-2.3
FIRSTRAND	-2.2
DISTELL	-1.9
KAP INDUSTRIAL	-1.9
BHP	-1.7
INVESTEC AUSTRALIA PROPERTY FUND	-0.8
NETCARE	-0.5

BREAKING THROUGH*

COMPANY	% ABOVE 200-DAY EMA
IMPERIAL	2
MR PRICE	1.8
SAPPI	1.5
EQUITES	0.6

*Based on the 100 largest market caps.

Photo: Archive

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 recent market developments.

BALWIN PROPERTIES

Balwin's lifestyle estate, 'The Reid', in Linbro Park.

Residential boost

Balwin Properties' results show a tough six months to 31 August as it struggled to operate during the lockdown and headline earnings per share slumped by 56%. The company did, however, declare a dividend of 19.6c/share, showing confidence from the board as far as cash flow is concerned. Balwin also finds itself well positioned with the surge in demand for home sales in the market below R1.5m on the back of the decades-low prime lending rate of 7%. The company has several estates under development and while some of them are at higher price points, there has been improving demand and I think Balwin will likely see continued increases in sales. It will manage this increased demand by ramping up construction and while for a long time I preferred Calgro M3 in the home builder space, Balwin is now looking like the better investment.

CORONATION

Profit expected to rise

Coronation Fund Managers* released a market update on 14 October, which showed assets under management (AUM) remained pretty much flat at the end of September when compared with the end of June. In addition, the company expects headline earnings per share (HEPS) to be between 10% and 20% higher with some one-off benefit that if removed would have seen HEPS by 5% to 15% higher. The company pays pretty much all its HEPS as a dividend, so the forward dividend yield is at around 9.5%. The update is in line with my expectations and this remains one of my preferred financial services stocks.

The company expects headline earnings per share to be between

10%

and

20%

higher.

METROFILE

Buyout collapse

As soon as the previous issue of *finweek* hit the shelves with my *House View* on Metrofile* as a buy, the delisting offer at 330c was withdrawn. The reason cited in a Sens announcement on 16 October was the inability of the buyers to travel from Australia to conclude the due diligence process. Now to be sure, getting 330c apiece for my Metrofile shares would be great. But, as I noted in the previous issue, the company is in a much better position than it was a year ago, with debt reducing, dividends growing and a robust business model. So, while I won't receive 330c/share, I'm happy to continue holding for the long term – which is usually my preferred position as opposed to being forced out for a quick buck by a delisting offer.

CAXTON

Cash flush

Caxton announced the sale of Octotel and RSAWeb for R433m on 16 October. This compares with Caxton's market cap of about R1.7bn. For the year ended 30 June, the company had R1.7bn in cash on hand, according to its financial statements. The tangible net asset value (TNAV) after the disposal will be 1 434c a share while the share price was around 460c at the time of writing. Does this company hold value or is it a value trap? The trick, as I always say, is to ask what will unlock the value? A special dividend from the proceeds of Octotel and RSAWeb would certainly help. But maybe the board would rather buy a new asset in the digital space, where they have some operations, but still mostly remain focused on printing and publishing. So, it really depends on what they buy, and I will be watching from the sidelines.

OMNIA

Sale will refocus fertiliser giant

Omnia has announced the proposed sale of its US operation, Oro Agri, for just under $150m. Oro Agri was a fair profit centre for the group, but the sale is at a decent profit after Omnia paid about $100m in early 2018. The business was not a core asset for Omnia and the sale leaves the company's management to focus on their South African operations. The cash will also further strengthen the balance sheet after the R2bn rights issue of late last year. From a company that looked to be teetering on the brink of business rescue, its management has done an excellent job in turning it around. Operating in the mining and agricultural space still has its challenges but Omnia is well placed to return to some level of its former glory; it was once a much-loved stock for most SA Inc investors and traded at over R200/share in 2014 compared with the current R42.

Photo: RDF Photo for Balwin Properties

18+

WHAT IS
AVAXHOME?

AVAXHOME -

the biggest Internet portal, providing you various content: brand new books, trending movies, fresh magazines, hot games, recent software, latest music releases.

Unlimited satisfaction one low price
Cheap constant access to piping hot media
Protect your downloadings from Big brother
Safer, than torrent-trackers

18 years of seamless operation and our users' satisfaction

All languages
Brand new content
One site

We have everything for all of your needs. Just open https://avxlive.icu

ETFS

Bonds fund to pay out return

Absa has announced a change to its local government bond exchange-traded fund (ETF), the Newfunds GOVI ETF (share code NFGOVI). It tracks the top ten government bonds and previously has always reinvested any distributions straight back into the bonds that paid. But, from November, it will not reinvest the interest; instead it will pay them out. Overall, it has no impact of the total return of the ETF, but if you especially wanted distributions reinvested, then you can have a look at the NFILBI. This ETF does reinvest the dividends but is a slightly different as it invests in inflation-linked bonds (also called linkers) rather than the nominal government bonds.

CLICKS

True quality comes at a price

Clicks' full-year results through 31 August, released on 22 October, again showed the quality of this company. Sales rose 9.6%, HEPS jumped 13.7% and the year-end dividend was 37.6% higher, although the company did skip its half-year dividend. Clicks had cash of over R2bn with virtually no debt at year-end. As always, however, I will caution that the stock is expensive – to be honest it has always been expensive. I checked my notes from five years ago when I wrote that Clicks' shares were expensive at a price-to-earnings ratio (P/E) of 27 times. Now the P/E is at 30 times and the shares price surged by 150% over the period. The answer, I suppose, is that one pays for quality and that true quality creates great investments.

Photos: Archive | clicksgroup.co.za

CASHBUILD

Riding pent-up demand?

In an operational update to the market on 22 October, Cashbuild said that revenue for the three months ending September (the first quarter of their financial year) was up 22%. This is a massive number, but I do wonder if it can be sustained as some of this increase related to the pent-up demand from the hard lockdown. But I also think a lot of people, now working from home, are tired of that cracked tile or old paint job and have been fixing things, which will let up once we're all done remodelling. The surge in home sales will continue to help, but I do think by the end of Cashbuild's financial year (June 2021) we'll probably only see revenue higher by around 10% to 12%. This will still be impressive, but not as grand as 22%.

EOH

Market surprised

EOH's trading update for the year through 31 July, released on 22 October, saw the share price surge by more than 17%. The market was surprised by the nature of the news. Although EOH will remain loss-making for the reporting period, at its core the loss in the second half is substantially smaller than the first half and EOH should be profitable in the next financial year ending 31 July 2021.

> Clicks had cash of over R2bn with virtually no debt at year-end.

DISTELL

Massive debt reduction

Distell released an operational update for the three months through 30 September on 20 October. It had lots to say, most of it good, but there was only one number that stood out: the reduction in net debt. Distell started the quarter with R5.9bn in net debt and ended at R4.2bn. That's a massive reduction, which can only have come from cash generation. If it continues, debt will be gone by year-end in June 2021. This will likely not happen as Distell uses cash for other things too. This is another business that seems to be in better shape after the hard lockdown than it was before.

COMBINED MOTOR HOLDINGS

Gearing up for future profits

Combined Motor Holdings had a very tough set of results for the six months through August as it only got back to selling vehicles in early June. But what we can see in this, and many other cases, is that companies have really come out of the initial stages of this pandemic looking a lot better from an operational point of view. Costs have been cut, loss-making operations were closed or sold and as the economy improves this will lead to better margins and profits in the years ahead. In the case of Combined Motor Holdings, the real hard work has been done in its car rental business that is now about 50% smaller than before, but will potentially make almost as much profit as when it was twice as large. ■

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** The writer holds shares in Metrofile and Coronation.*

By Maarten Mittner

ECONOMY

Will inflation pick up in the US?

The shift to the services economy, with large inputs of a technological nature, may be the reason why low inflation is so sticky, despite the printing of money.

The pressure on authorities to implement additional fiscal stimulatory measures to augment easing monetary policies from the central bank has reached a new crescendo in the US.

But consensus on a new fiscal package to boost the economy has been elusive.

The big question is whether additional fiscal measures will lead to an uptick in inflation as anticipated by some analysts, and so provide renewed support for equity markets.

It was predicted that the massive stimulus measures of 2008 and 2013 would at some point lead to increased inflation in the US. But that has not happened, even in an environment of full employment. The US Federal Reserve (the Fed) has already indicated it overestimated the effect of higher inflation following through from the stimulus actions, even though it still believes inflation could rise in future.

At this stage, the Fed is still sticking with easing policies by making it clear that rates will remain at or around zero for some years to come. But, in addition, it has set a target for inflation to pick up over the medium term as the economy recovers and demand improves.

The productivity gains from the economic resurgence in China, together with the cheaper production methods of the big tech companies, are usually cited as reasons why inflationary pressures remain muted. Low wage growth, despite strong consumer spending, has also helped.

So, the question is really: What happened for the Fed to adopt this stance as lower demand in the present pandemic environment could further inhibit inflationary growth?

Annual inflation has been ticking up slightly in the US, from 1% in July to 1.4% in September. But does it indicate a structural change? Unlikely, at this stage. Equity markets remain elevated, but there does not seem to be an overriding concern of some higher inflation in the future.

This might be because no one is really anticipating that happening. But ditching austerity and embarking on greater fiscal stimulatory measures at least holds the promise of higher inflation in future. This should, theoretically, boost equity prices.

However, the reality has been that markets have risen over the past decade in a low inflationary environment. Easing monetary policies have been the real driver.

In the past, massive money printing from central banks eventually led to higher inflation, which was an important driver of equity gains on markets. Today, less so. Tech companies have recorded significant gains in a low inflationary environment.

In the 1970s and early 1980s inflation was a huge issue in the US as it reached

25%

in the 1970s.

Photo: Shutterstock

In the 1970s and early 1980s inflation was a huge issue in the US as it reached 25% in the 1970s. Inflation was brought down in the Reagan years, first with the tough remedy of high interest rates, which nearly decimated the US manufacturing sector, followed by lower rates that acted as an incentive for greater consumer spending and rising imports. This resulted in the US finding itself in the dilemma it is in now by consuming more than it produces.

Yet, inflation remains low and markets continue to climb, bar a few hiccups. Inflation has become much less of an issue, as the level remained low thanks to cheap imports. Now, ironically, the Fed has revived the inflation spectre, albeit on a moderate level, as an indication that slightly higher inflation would reflect improved economic conditions.

It is questionable if this stance will work. Some analysts suspect it might even just be a ruse from the Fed to ward off any deflationary build-up.

In the past, inflation was defined as too much money chasing too few goods. There is certainly enough money in the US in circulation at present to chase the goods.

But there may not be that many goods around to chase. With algorithms now regarded as a means of production in a predominantly services economy, there is much less inflationary pressure than in the past, when real inputs of steel and concrete and human sweat acted as inflationary push factors.

The digital economy has created a whole new playing field.

The operations of the big tech companies have had a deflationary tendency, due to the cheaper outline of digital communication and manufacturing processes. And for demand to increase in the US, consumers need more money. Which is not the case as wages remain low and debt levels high.

Some value investors have come to the fore, saying that the time for undervalued stocks will arrive if inflation, and interest rates, rise commensurately. However, it is difficult to see how higher interest rates might support traditional stocks, as another layer of costs is added on companies already struggling with existing expenses and competitive disadvantages.

And, as Japan has shown, there is little incentive to bring down debt levels with increased inflation. Inflation over time is beneficial for a reduced debt burden. But the price might be too high for governments to consider.

Higher inflation may not materialise for some while yet in the US. And markets seemingly do not need higher inflation to continue any upward trajectory. ■

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THE OUTLOOK FOR SA'S MAJOR LIFE INSURERS

When Covid-19 hit our shores, the impact on South Africa's listed life insurers was inevitable. **Jaco Visser** takes a look at how these companies took extreme caution in providing for the uncertainties of the coronavirus pandemic and why these shares may start to pose opportunities for resilient investors.

As the end of 2020 fast approaches and global economies attempt to recover from the economic fallout of government-mandated lockdowns, Covid-19 continues to remain a threat to the world's population as many countries brace for a second season of disease and death. Lest we forget that the Great Flu of 1918 and the Hong Kong Flu of the late 1960s took two seasons to mutate themselves into oblivion. Indications are that South Africans will experience a second peak in infection at the height of the summer in January or February 2021. The northern hemisphere is currently grappling with its second surge in infections.

Amid this pandemic, life insurers play a key role in ensuring the financial posterity of families affected by the disease. The importance of life insurers during a time of crisis, such as this, can't be more clearly illustrated than by the date on which the Suid-Afrikaanse Lewens Assuransie Maatskappij Beperk (Sanlam) was founded: 8 June 1918. According to the US Centers for Disease Control and Prevention, the first signs of the Great Flu, also called the Spanish Flu, were recorded in military personnel in the Spring of 1918 – a month or two before Sanlam's founding.

This is not to imply that Sanlam was founded due to the Great Flu (which was an avian influenza and labelled the H1N1 virus in later times), but one can stand to reason that the scare of death boosted an infant company, which is today the fourth-largest listed financial services business on the JSE.

Life insurers take on the risk of longevity – how long an insured will live – in return for a regular premium and undertakes, legally, to pay an insured sum of money when the insured succumbs. Such a premium is decided upon after taking various medical, work and other factors of the insured into account. Prevalent morbidity and mortality factors in a society are also part of a life insurer's actuaries' calculations. When a pandemic strikes, such as the current coronavirus, these calculations are adjusted. In layman's terms: the actuaries need to predict future deaths with historic experiences and best estimates.

An exercise in caution

There is a saying that a central bank needs to be a boring and predictable institution to ensure a country's monetary (and to an extent production) stability. One can easily extend that reasoning to life insurers: they need to be boring institutions with the ability to honour death, dread disease, funeral and disability policy

TABLE 1: COVID-19 DEATH PREDICTIONS AND RECENT FINANCIAL PERFORMANCE OF SA LIFE INSURERS

	Forecast Covid-19 deaths	Headline earnings per share growth	Estimated earnings growth excluding Covid-19 impact*
Liberty	54 000	>-100% (loss-making)	-42%
Old Mutual	National projections	-67%	-4%
Momentum	Actuarial Society of SA projections	>-100% (loss-making)	15%
Sanlam	17 000 – 28 000	-41%	18%
Discovery	60 000	>-100% (loss-making)	25%

* Estimated operational earnings excluding Covid-19 consequences (market impact, expected economic losses and additional mortality provisions.) Not strictly comparable as each insurer is affected differently.

SOURCE: Obsidian Capital

agreements with insured people. Because people generally now live longer, life insurers' financial longevity needs to stretch for decades into the future. A 25-year old who agrees to life cover with an insurer can potentially live to the ripe age of 85 years. Will the life insurer still be in business in 60 years' time and be able to honour the policy?

The longevity of life insurers has come to the fore during this pandemic – with its concomitant media hype – and many investors would have been anxious to see how South African life insurer's deal with the inevitable fallout. The cold, hard fact is that Covid-19 would leave death in its wake and as a result, life cover claims would inevitably increase. There are, however, two sides to the same pandemic coin. One: claims for death cover jumps; two: due to fear (whether hyped or not) more people scramble to have life cover in place.

So what has the experience among SA's life insurance companies been thus far as the country continues to battle the coronavirus pandemic?

Sanlam, Discovery, Old Mutual, Momentum Metropolitan and Liberty are South Africa's largest listed insurers. OUTsurance isn't listed, but is also a significant player in this field. All of these companies have reported their six-months or full-year results through June.

A standout from these results was the caution that many life insurers applied to predict the financial impact of the coronavirus pandemic. In plain terms: What will the 'claims experience' be amid the uncertainty of the pandemic's duration and whether morbidity among South Africans will increase? Some raised provisions through their income statements,

such as Liberty Holdings, which established a R3bn pandemic reserve. (See **table 3** on p.39)

Although SA's death rate has not come close to the predictions made earlier this year – by late October, the number of deaths stood at around 19 000, as opposed to estimations that it would be up to 48 000 by end November – the current and potential Covid-19 death rate has implications for life insurers.

"SA's listed insurers will suffer financially should death rates exceed those embedded in the pricing of their existing life insurance policies," said Obsidian Capital in a recent research note. "If they expect this to happen, then they are required to make provision for those deaths when they report their financials." (See **table 1** for a comparison between the life insurers' forecasted mortality rate and the impact of the pandemic on their earnings.)

It was, however, not only the uncertainty of how the pandemic would play out that weighed on life insurers. They were already beset by macroeconomic headwinds when the coronavirus hit SA's shores.

Finding growth when consumers are constrained

As traditional life insurance and income protection policies usually cover those consumers with assets and a job, the dearth in employment that hangs over SA has had an impact on writing new business for life insurers. Or, to protect market share, they had to concede margins to offer better premiums as South Africans shopped around to get this grudge purchase at the cheapest possible price.

"The diminishing spending power of the consumer will affect all industries," Royce Long, a director and portfolio manager at Obsidian Capital, tells *finweek*. "Discretionary spend will be under the most pressure. As always, the better businesses always manage to 'make a plan' and emerge in a better relative position. We have been surprised at just how well some domestic businesses managed their operations during the Covid-19 lockdowns. Reported results have been better than expected, largely due to good management as there has been no assistance from the economy. Unfortunately, a shrinking economy places pressure on all domestic businesses and sustainable top-line-driven growth will be hard to achieve."

Against this backdrop of increasingly financially strained South African consumers, there remains a massive shortfall in life cover among the population. The Association for Savings and Investment South Africa conducts an insurance shortfall study every three years in partnership with True South Actuaries and Consultants. The 2019 Insurance Gap Study shows that SA's 15.6m earners (those who receive an income) had a life cover shortfall of R15.4tr in 2019 compared with R7.3tr in 2010, and a disability cover shortfall of R19.3tr in 2019 compared with R11.1tr in 2010. According to the study, SA earners need more than R24tr in life cover while the policies in force only cover about R9tr.

SA earners need more than **R24tr** in life cover while the policies in force only cover about **R9tr.**

The question, then, is how life insurers will tap into this huge market – which is more than one and a half times as big as the current life policies in force? The pandemic has led to the increased use of online sales channels by consumers who were either forced to stay at home or scared to venture outside. It is, however, also a reality that SA's population has a low internet penetration as data costs – especially for those living in rural areas and where fibre networks haven't been rolled out – remain prohibitively expensive. Nevertheless, the march to a more digitised society is happening. And that may have consequences for life insurers.

Sarine Barnard
Analyst at Ninety One

Royce Long
Director and portfolio manager at Obsidian Capital

"It might be helpful to refer to the short-term insurance industry to think about this question," Sarine Barnard, an analyst at Ninety One, tells *finweek*. "Short-term insurance is ahead of life insurance in terms of direct selling without the use of an adviser (although most of that happens through call centres with only a small percentage a full digital experience)."

The experience in this industry is that while it is easy to sell products like vehicle insurance directly to consumers, for more complex products – such as commercial insurance – there is still a need for an adviser to help find the right solution, Barnard says. OUTsurance started out with a pure direct model but has now started to build an agency force to sell into the commercial market for that exact reason, she says.

"The general consensus about life insurance is that it will be more of an omnichannel model," Rella Suskin, head of research at Benguela Global Fund Managers, tells *finweek*.

And that seems to be the view of life insurers too. "We believe that face-to-face interaction with customers still plays a significant role, even in a digital age, so we view the role of the financial adviser

Photos: Supplied

as critical," Liberty said in an emailed response to questions. "Equally important is the role of technology to augment the human experience. This balance matters to us because if technology does the heavy lifting, our financial advisers can focus on what technology can't do: being there for clients, anticipating adversity and helping clients to take the hard decisions."

Going forward, the state of the SA consumer's wallet will be instrumental in where and how life insurers will regain growth.

"Growth will be constrained, plus the insurers also have to deal with the payment of excess mortality claims on the life side and business interruption claims on the non-life side," says Barnard.

"In such a difficult environment, the winners will be those companies who focus on retaining and cross-selling to current customers as well as gaining market share through a better client experience and product proposition."

On the other hand, insurers, such as Momentum Metropolitan, continue to see growth opportunities.

"There is still much scope within our existing client base," says Francois De Ravel, general manager for coastal provinces and the Free State at Momentum Financial Planning. "Yes, it is, however, a challenge to operate in a shrinking market, fighting to retain market share, but we have no choice; we have to adapt and look forward while never ignoring the lessons learned during this most challenging time. We are fortunate because people will always need advice to ensure their financial wellness. The quantum of business may be affected for a certain period, but this will bounce back. The reality is that we have all had to reset expectations by an additional two to three years."

Winners and losers among the life insurers

SA's listed life insurance sector is split between two behemoths in terms of market capitalisation: Sanlam and Discovery on the one hand, and three smaller players – Old Mutual, Momentum and Liberty Holdings – on the other. The market cap of Sanlam, for instance, is larger than the three smaller players combined. The two large insurers are trading at relatively high forward price-to-earnings ratios, while the three smaller insurers seem extremely cheap on that valuation. Insurers report the measurement of embedded value, due to the nature of long-term insurance contracts, as an indication of their value (see **table 2**).

SANLAM

Market cap: R120.8bn
Forward P/E ratio: 13.33
Share price movement year-to-date: -31.8%

Sanlam's half-year results through 30 June showed a marked decline in headline earnings per share as the company wrote off R7.6bn in goodwill for two international assets. Saham, which operates in 33 African countries and the Middle East, saw Sanlam acquire the remaining 53% it didn't own for $1bn in 2018. Most (R5.8bn) of Sanlam's R7.6bn in write-offs was to impair Saham.

"They have written off most of the premium paid-for synergies with only a third of the impairment for direct economic impacts," Rella Suskin, head of research at Benguela Global Fund Managers, tells *finweek*. "They still expect to realise synergies, but it will take longer, given economic growth impacts from Covid-19. Sanlam paid upfront for the Saham synergies and this has highlighted the dangers of doing so."

It is also probably important to note that before the coronavirus pandemic, Sanlam said that progress on extracting synergies was already slower than anticipated at Saham, said Suskin. "After buying Saham at a price-to-earnings (P/E) ratio of 22 to 23 times and subsequently writing down 18% (R2.8bn) of the original R15.4bn in goodwill (just relating to synergies), together with the considerable work still to be done with the business, I think Sanlam overpaid for Saham."

In an emailed response to questions, Sanlam said the uncertainty around the outcome of the pandemic, together with the impact of lower oil prices on economic recovery, have prompted it to write down the value of assets in Africa, Lebanon and India.

TABLE 2: VALUE MATRIX OF LIFE INSURERS

Insurer	Market cap	Embedded Value	Discount to embedded value
Sanlam	R120.8bn	R129.3bn*	-6.6%
Discovery	R82.8bn	R73.1bn	+13.2% (premium)
Old Mutual	R51.7bn	R67.8bn	-23.7%
Momentum Metropolitan	R22.9bn	R38.5bn	-40.5%
Liberty Holdings	R17.7bn	R35.4bn*	-50%

* Sanlam and Liberty report group equity value; share prices as at 27 October 2020.

SOURCE: Latest (interim or full-year) financial statements of companies.

"These include, inter alia, part of the value paid for Saham Finances due to the expected slowdown in economic growth across the business footprint, as well as the deteriorating political and economic environment in Lebanon," the company said. "We remain confident that the synergies from the Saham acquisition can be realised, but will take longer than originally anticipated and that our operations are well positioned to benefit from the economic recovery going forward."

Regarding the valuation of Sanlam's share price, at a forward P/E of around 13 times and historic dividend yield of 6.1%, Obsidian Capital's Long reckons it's reasonably valued in an absolute sense, but expensive compared with other insurers. "It has consistently grown its dividend over the years," he says. "While the short-term results might be under some pressure, we do believe the dividend will remain largely intact."

DISCOVERY

Market cap: R82.8bn
Forward P/E ratio: 15.32
Share price movement year-to-date: +2.7%

Discovery's share price movement this year has shown the resilience of this company's target market – the affluent.

"The affluent life insurance sector has proven to be very resilient during the COVID-19 pandemic," Riaan van Reenen, CEO of Discovery Life, tells *finweek*. "Pandemics highlight the need and value of life insurance in providing financial security during extremely uncertain times."

The life insurance business contributed R1.87bn (41%) of Discovery Group's operating profit before investments in new initiatives through 30 June, according to its financial statements. This is the largest contributor to this measure of profitability.

"Around 40% of profits come from the health administrative business," says Ninety One's Barnard. "This is a very defensive business and has done better than most others in the current environment, still growing profits by 2% in the first six months of 2020 – with everyone scared of Covid-19, membership of the medical scheme was resilient over the past six months." In addition, Discovery's UK Health business and its SA short-term insurance business also benefitted from reduced claims due to

TABLE 3: CAPITAL COVER RATIOS AND COVID-19 PROVISIONS OF SA'S LISTED INSURERS

Insurer	Cover ratio 30 June 2020	Covid-19 provisions
Sanlam Group	187%	R1.3bn
Discovery Life	172%	R2bn
Old Mutual	182%	R2.79bn
Momentum Metropolitan	185%	R1bn
Liberty Holdings	183%	R3bn

SOURCE: Latest (interim or full-year) financial statements of companies.

Covid-19. In the case of the SA short-term insurance business, less vehicle claims were experienced due to reduced driving on the back of the lockdowns. The UK Health business saw much lower hospital utilisation for non-Covid related illnesses, she says.

OLD MUTUAL

Market cap: R51.7bn
Forward P/E ratio: 4.35
Share price movement year-to-date: -43.8%

Old Mutual's remaining 19.9% stake in Nedbank cost the company dearly as the lender's share price more than halved since the beginning of the year. This forced Old Mutual to write off R8.6bn in the value of Nedbank. The lender's stake, at a stock market valuation of R10.4bn, now comprises more than a fifth of Old Mutual's market capitalisation.

The company provided for R2.79bn in response to the pandemic. "The mortality component of this provision could well be overstated," says Obsidian's Long. "Should the market recover, other market-related unrealised losses could unwind."'

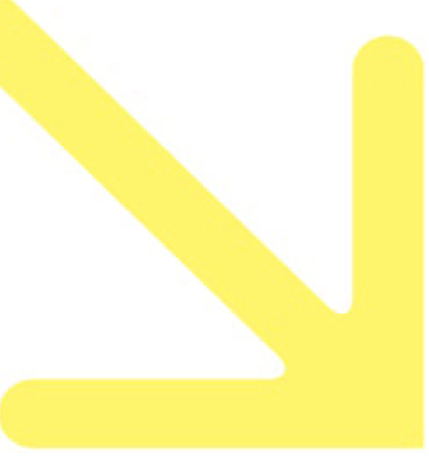
Suskin shares this view of Old Mutual being overly cautious. "Old Mutual is anticipating an increase in lapses, mortality and morbidity in the second half (of the financial year) hence the provision raised – this is reasonable and increasing provisions is becoming a more common theme," she says. "I am, however, sceptical as to the quantum of the provision and the timeline associated with it."

With its forward P/E ratio of around four times and historic dividend yield of about 7%, Long believes the share is attractively priced.

Rella Suskin
Head of research at Benguela Global Fund Managers

Riaan van Reenen
CEO of Discovery Life

Photos: Supplied



"I think it was the right step to make a prudent provision and illustrate that despite the provision, the solvency of the company is not impaired, thereby ensuring confidence from clients to continue to invest with Liberty."

MOMENTUM METROPOLITAN

Market cap: R22.9bn
Forward P/E ratio: 6.78
Share price movement year-to-date: -30.3%

Momentum Metropolitan's share price has also not been spared the brunt of the pandemic. It slid by almost a third this year. The company's net insurance premiums declined by R3.5bn in the year ended 30 June compared with the previous comparable period. This was mainly due to a R3bn decline in life insurance premiums received, according to the financial statements for the previous book year. This was countered by a R1bn increase in non-life insurance contracts during the same period. Net insurance benefits and claims remained constant at R27bn compared with the previous year's R26.95bn.

With regards to income on the company's investments, Momentum received R1.4bn less in dividends from listed entities. This is proof of the subdued economic and operational environment of listed SA companies. On the other hand, dividend income from non-listed companies increased by R1bn. In total, Momentum's investment income increased marginally by R354m in 2020 compared with the previous financial year.

Momentum made a R983m provision for future effects of the coronavirus pandemic.

LIBERTY HOLDINGS

Market cap: R17.7bn
Forward P/E ratio: 5.59
Share price movement year-to-date: -50%

Liberty's share price was the hardest hit this year, losing half its value (or R17.7bn). The company provided for a R3bn coronavirus pandemic reserve to cover future claims and expenses related to the disease. The pandemic reserve covers the increased mortality due to Covid-19, plus the increased lapses (called reduced persistency), says Ninety One's Barnard. The Liberty provision does look high relative to what was provided by other companies, she says.

"You have to bear in mind though that Liberty was the first of the insurers to publish its results in early August, shortly after the Covid-19 mortality claims peaked – they didn't know at that stage that claims were peaking, so they had to be prudent," Barnard says. "On the persistency side – trying to estimate the impact of Covid-19 on persistency is an extremely difficult exercise because there are no historical examples that you can use as a benchmark for how this is going to play out. I think it was the right step to make a prudent provision and illustrate that despite the provision, the solvency of the company is not impaired, thereby ensuring confidence from clients to continue to invest with Liberty."

In an emailed response, Liberty said they remain financially sound and well capitalised with their capital cover ratio at 183%, which is the upper end of the capital coverage target range after accounting for operational and investment market impacts and the establishment of the R3bn pandemic reserve.

"Despite our strong capital position, significant uncertainty currently exists around the outcome of the Covid-19 virus in SA in the short term and its economic consequences, and we will continue to monitor the full impact as it unfolds," the company responded.

At current valuations, the stock seems cheap. "In our view, the current valuations look attractive relative to its last reported group equity value of R128.80 (per share) in June 2020," says Suskin. "This is a massive discount. In the short term, the stock might rerate if the claims experience and new business comes through better than expected."

Over the long term, the company will need to regain market share, which it predominantly lost to Discovery, she says. ■

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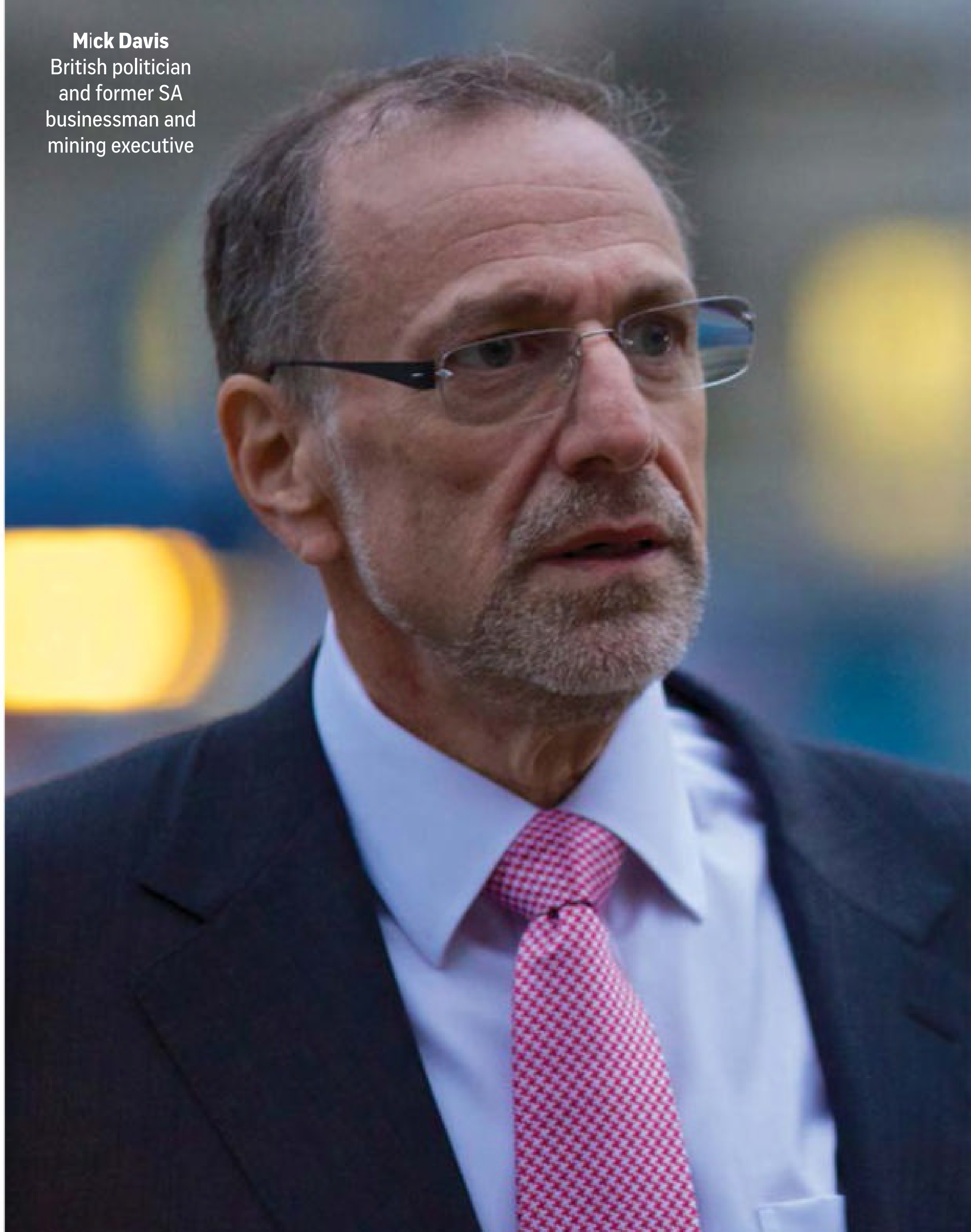
>> **Management:** The legal implications of monitoring employees in the age of working from home *p.44*

PROFILE

By David McKay

Mick Davis: A history of steely determination

Former South African businessman turned British politician, Sir Mick Davis, has an impressive history in the mining industry. At the Joburg Inaba, held in October, he recounted his career and shared his insights on the current mining landscape.



Mick Davis
British politician and former SA businessman and mining executive

Photo: Gallo/Getty Images

It's not often that Mick Davis, knighted by the UK's queen in 2015, has been called an asshole; at least, not to his face. Enter Bernard Swanepoel, the former CEO of Harmony Gold, who first bumped into Davis during the 1980s, early in their respective careers.

"When I first met you at Genmin [General Mining], I thought you were an asshole," said Swanepoel, who was about to pose online audience questions during the Joburg Indaba conference he convenes, and at which Davis was a star turn. "Then I got to know you, and I realised you were a clever asshole."

If Davis was taken aback, it didn't show, maintaining to a tee his reputation as a cool customer.

A former colleague recalls a work-related dinner with Davis that was carried off in an awkward, near-complete silence; conversation difficult, and certainly not encouraged by Davis. Anecdotes of this ilk have led to a reputation that Davis is icily cold, a view assisted by his (highly successful) managerial style, which was to decentralise management functions and delegate responsibility to the mining operations.

In a frank interview with Fiona Perrott-Humphrey, a banker for UK banker Rothschild & Co, Davis touched on what he nearly acknowledged was a character flaw. "One of the biggest challenges if you've had years of success is arrogance. The arrogance of success that not only are you convinced that everything you're doing is right, but you're convinced that people who observe you, think that you are right as well," he said.

The most significant moment where this happened for Davis was in underestimating the opposition investors would put up to a £240m

While not necessarily advocating a return to major deal-making, Davis nonetheless believes that by not investing sufficiently in growth, mining firm valuations will eventually suffer.

pay-out and incentive scheme he'd proposed in 2012. The scheme was for employees of his company, Xstrata following its £60bn merger (or takeover, as some call it) with Glencore, the Swiss-headquartered commodity miner and trader.

As part of the package, Davis was set to benefit to the tune of £29m in a three-year retention incentive once the merged company was created, which he would head. The incentive scheme never happened and, following four months of acrimony, and a falling out with Ivan Glasenberg, Glencore's CEO, Davis left the company – a turn of events he described as a career nadir.

"The lowest point, without a doubt, was the ultimate merger or takeover by Glencore of Xstrata. Everything that I built up was essentially snatched away and that was a tough thing to actually deal with," he said.

It's arguable whether Davis has really recovered from those events. He re-emerged in 2016, having raised at the time half a billion dollars in a private equity fund mischievously named X2 Resources, hinting at his previous success at Xstrata. But X2 Resources closed in 2017, having failed to make a single investment, citing a lack of decent opportunities.

Davis describes his career as one of unrequited ambition. As a young auditor, he felt he should have been made a partner, but management thought he was too young. After serving a period as Eskom's financial director in the 1990s he was "passed over" for position as CEO, so he left. Davis was in his mid-thirties.

Then came seven "fantastic" years as chief financial officer of Billiton, joining the equally ambitious Brian Gilbertson. The two took the company to a London listing in 1997 – among the first major SA companies to do so – followed by its merger with Australia's BHP, creating the largest mining firm at that time.

"There are four people who claim they brought Billiton to London: [Brian] Gilbertson, myself, Adrian Coates [a well-known banker in London, then at HSBC] and Davis," said former JP Morgan banker Ian Hannam. "The answer is: it was Davis. He saw the opportunity and managed to persuade Gilbertson that it would create a platform to build a new company to rival Rio Tinto."

The arrival of South Africans on the London Stock Exchange drew some uncharitable comparisons among the locals. In a 2006 article by *The Guardian,* a fund manager is quoted remembering Billiton executives rolling up in the city: "I saw these guys with their nasty South African suits and dodgy haircuts and thought: 'These guys won't be world-beaters'. How wrong I was."

In fact, Davis was not only able – with Gilbertson and team – to turn Billiton into a leading mining firm, but he also became absorbed into British high society, initially as a donor to the Conservative Party, and later as the party's treasurer and CEO.

But the crowning glory was the bachelor knighthood conferred on him, at the behest of then prime minister, David Cameron, for services to holocaust commemoration and education. Davis describes the moment as "a bolt out of the blue" as he hadn't felt he'd done anything to deserve it.

"I really was quite overwhelmed by it as, I guess, everybody who gets these things ... but nevertheless, it was a great experience to get and I was knighted at Windsor Castle, and the whole experience was very special." He adds, though, that it doesn't seem to change the way people relate to him (Bernard Swanepoel included!). "My wife said she was a dame before I was knighted."

Ivan Glasenberg
CEO of Glencore

As CEO of Xstrata, a company that listed in London during 2002, Davis participated in more than

40

transactions.

A blockbusting deal-maker

Davis is known in the mining industry as a doer of deals, normally blockbuster events. As CEO of Xstrata, which listed in London during 2002, Davis participated in more than 40 transactions. One that didn't pass muster was the £41bn "merger of equals" with Anglo American, then managed by Cynthia Carroll. Carroll brought innovation to the stuffy Anglo set, especially an intolerance for mine fatalities which, in its way, foreshadowed the modern investment focus on environmental, social and governance (ESG) factors. But the company was suffering in other areas: It had overpaid for a large iron ore deposit in Brazil and had lost key technical skills.

Davis scented blood, but the merger was voted down by shareholders, and Anglo's board rallied around Carroll to defeat the notion of a nil-premium bid, which was later taken up by Glencore in its merger proposal to Xstrata. Notwithstanding this setback, and his controversial exit from Glencore-Xstrata, Davis' reputation as an aggressive, growth-focused empire builder has tended to stick.

Today, he says, the mining industry may be missing

a beat. While not necessarily advocating a return to major deal-making, Davis nonetheless believes that by not investing sufficiently in growth, mining firm valuations will eventually suffer.

According to PwC, there were seven 'mega-deals' worth over $1bn in 2019, but only three in 2020 to date, suggesting mining firms are more conservatively set out, focusing instead on dividends – and perhaps guilty of too much focus on meeting the short-term return goals of investment managers rather than honouring the long-term obligations of the orebodies they mine.

Davis warns this could be a mistake. "Mining majors have addressed their fundamental costs and all of them have done a fantastic job; making themselves more resilient as a result," said Davis. By holding back investment programmes, mining management had satisfied the needs of the investment community.

"Therein lies their biggest challenge going forward. Directors and management teams have not focused on this very simple proposition: Every day they take something out of the ground, and unless you do something that replaces that, you end up withering."

Cost savings provided some value, but more value comes from investment. "The ability to create value depends upon the options you have available in your portfolio," he said.

"I fear that this very focused approach on returning cash to shareholders in the form of dividends and capital returns has not, in fact, taken into account sufficiently the need to reinvest and so has not created optionality," he added.

The present focus

Little is known of the beneficiaries behind Niron Metals, registered in the UK in 2018 but which has Davis as a partner along with former De Beers' marketing executive Varda Shine and Marcos Camhis, a Greek fund manager – both board members of Niron Metals. This time around, Davis isn't planning a new round of major deal-making, preferring instead to focus on smaller investments of an organic type.

But Niron Metals, however, has landed Davis in fresh controversy, having teamed up with Beny Steinmetz of Beny Steinmetz Group Resources (BSGR) infamy, a company that in 2018 lost a long-fought $2bn arbitration case with Brazilian miner, Vale. The lawsuit related to contested iron ore mineral rights in West Africa's Guinea. A 'sting operation' recently 'proved' a former Vale iron ore executive knew of the risks involved in Guinea's iron ore prior to its investment with BSGR, which was the contestation in the lawsuit. Or so Steinmetz contends. Steinmetz is therefore hoping to have the matter reopened.

A similar arbitration between BSGR and the government of Guinea was suddenly called off in 2019, with the two sides agreeing Beny Steinmetz develop the Zogota iron ore deposit in the country instead. This is Niron Metals' challenge: it's not an easy task. Time and again, the private sector has failed to get the freight and mine logistics right in the former French colony.

Varda Shine
Board member of Niron Metals and former marketing executive at De Beers

Marcos Camhis
Board member of Niron Metals

Photos: Gallo/Getty Images | www.fosassetmanagement.com

Davis, however, doesn't necessarily see a return to large-scale corporate work; not as a swan-song or grand industry farewell moment, or anything like that. In any event, it's uncertain whether Davis' quick-fire growth style is appreciated anymore. Investors representing 20% of Rio Tinto's shareholders firmly rejected the Anglo-Australian group's choice of Davis for chairman in 2017. According to reports at the time, shareholders shivered at the thought of retention and incentive awards that proved his undoing in the Glencore-Xstrata deal.

Davis acknowledged times have changed. The emergence of ESG as a key metric for mining investment is a gamechanger, and reflects developments in wide society. "I find my children have a much greater social awareness, social conscience that, perhaps, I had when I was their age," he said.

"They're much more focused on creating public good in society as opposed to simply furthering the amount of money they can make, and things like that. And that's a very noble thing."

As for the mining sector at large, it hasn't recovered from the capital excesses and subsequent collapse of the so-called China-inspired super cycle. From about 2000, China's economy racked up double-digit GDP growth year after year, incentivising demand until the 2008 financial and economic crisis. That period of massive growth and collapse left a sour taste in the investment mouth, but it also catalysed negative views towards the mining sector, and big capital among society at the same time, as environmental consciousness was intensifying.

Owing to this failure of branding, the industry has been somewhat ignored and has subsequently been unable to attract young talent in the kind of numbers it wants. Davis, though, looks at the matter differently. "The vitality of resources to the growth of mankind is absolutely fundamental and that's what we need to concentrate on and demonstrate," he said.

"We do not need to be ashamed of how we managed our environmental impact as an industry. There are certain companies that should be ashamed, but we as an industry do not need to be ashamed of how we're tackling this. I think that there's a great story to be told and we need to go out and tell it."

"Thank you Sir Mick," chimed in the conference's Swanepoel – which, coming from him, struck one as rare praise indeed! ■

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By Amanda Visser

The ethics of monitoring your employees

Checking on employees in the age of working from home has legal consequences for businesses to consider.

Corporate surveillance – the use of digital tools for employee monitoring – is not a new concept and there certainly is no shortage of tools available.

However, following the global outbreak of the coronavirus, companies have increased their use of these tools – mainly to stem the initial fear of productivity losses when thousands of people started working from home. Companies are well advised to take all the legal and ethical considerations into account when introducing additional surveillance tools.

Although something is legal, one should not jump to the conclusion that it is ethical, says Deon Rossouw, CEO of the Ethics Institute. "Apartheid was legal, but it certainly was not ethical."

Deon Rossouw
CEO of the Ethics Institute

SA legislation

In South Africa employers are generally permitted to monitor employee performance and productivity. The applicable pieces of legislation for the surveillance of people and their electronic communication include the Protection of Personal Information Act (POPIA) and the Regulation of Interception of Communications and Provision of Communication-related Information Act (RICA), notes Nozipho Mngomezulu, partner in the technology, media, telecommunications and intellectual property practice of law firm Webber Wentzel.

Nozipho Mngomezulu
Partner in the technology, media, telecommunications and intellectual property practice at Webber Wentzel

In terms of POPIA, employees should be made aware that their performance and productivity is being monitored by the employer and the employer should provide reasons for doing so to the employee.

RICA prohibits the interception of communications unless a specific exemption can be established. According to Mngomezulu, a business may intercept any indirect communication when it relates to the business or takes place during the carrying on of the business.

Lenja Dahms-Jansen, a senior associate in the employment and benefits division of Bowmans, says any person who is convicted of an offence in terms of RICA, which includes unlawfully intercepting a communication, may be liable to a fine of up to R2m or a prison term not exceeding ten years.

Notwithstanding the exceptions, employers do not have an unrestricted right to monitor employees' behaviour, she warns. Employers may not require employees to grant them access to their private email or social media accounts or seek to gain access to such private accounts by unlawful or dishonest means (by hacking the accounts or creating impersonation accounts).

"It would not, however, be unlawful or unethical for an employer to access an employee's social media profile in circumstances where the profile is open to the public, as no privacy settings are in place," says Dahms-Jansen.

Baker McKenzie's employment practice head, Johan Botes, says the employer will always be on the back foot if they are found to have collected and stored private information that is clearly not work related, even if it was done on the company network or during office hours.

"However, the employer will be allowed to collect and retain data during a time when the employer had a reasonable expectation that their employees should be furthering their business interests," says Botes.

BULGING OVERTIME BILLS

The glaringly obvious predicament with the remote workforce is the lack of control over working hours and the value of the work done, says Webber Wentzel partner Dhevarsha Ramjettan.

She says considering the financial implications of overtime, the employer is well within their rights to implement policies and procedures that govern and are implemented solely for the purpose of monitoring the overtime work.

"Policies can be implemented that only allow for overtime to be paid out where it has been approved beforehand by the employee's manager," she says.

Yolandi Esterhuizen, compliance manager at Sage Africa & Middle East, says the wage rate for overtime is set at either one and a half times the normal rate or twice the normal rate, depending on whether the overtime was worked on a normal working day, or a Sunday or public holiday.

She adds that the Basic Conditions of Employment Act provides that companies can ask that senior managers; travelling sales staff who regulate their own hours of work; employees who work less than 24 hours a month for an employer; and employees earning more than the annual earnings threshold (currently R205 433.30 a year) work overtime without compensation. ■

Good practices

Monitoring internet sites visited to see whether they are unwarranted or prohibited in terms of company policy is permissible. In many instances the employment contract also provides for a general consent in terms of the monitoring of electronic communications for business purposes.

"A good practice in this regard is to reinforce the message through continued notifications of the terms and conditions in the employment contract. The intention behind this is to ensure that employees have a reasonable expectation and appreciation at all times that their electronic communication activities are monitored," says Botes.

He adds that as a rule, the employer should refrain from monitoring employee activities 'after hours'. This will certainly erode the 'business rational exception'.

Even if there is more fluidity in working hours and the employer may meet the legal threshold to monitor employee communication after hours, the question is whether it is ethical to do so, says Botes.

Erosion of trust

Rossouw says there is a case to make for surveillance, but then it should deal with increased safety and protection against loss or damage.

When it is aimed at improved productivity – or to create the perception of 'busyness' – it presents more problems than solutions.

Besides having a negative impact on the morale and commitment of people, it also undermines trust. "You are basically telling your employees that you do not trust them, and you are going to watch them. And you are going to do it even in the privacy of their own homes," says Rossouw.

Anastasia Vatalides, head of Werksmans Attorneys' labour and employment practice, agrees. "Employers cannot become policemen and women."

Obviously not everybody is professional and driven. There are those who will leave early or take longer lunches and chat endlessly with colleagues when the manager is not in the office.

"Those issues have also manifested in this virtual environment and in some instances, they have been exacerbated by excuses, such as load shedding or poor connectivity to exploit the situation," says Vatalides.

The alternative

Rossouw says corporate surveillance is typically extrinsic motivation or fear-based compliance. The alternative is intrinsic motivation, where people do the right thing out of conviction and not because someone is watching. They understand the purpose of the organisation and what their role and responsibilities are to achieve it.

"In these instances, you will often find that people are working too hard, not because of over-surveillance, but because of over-motivation." ■

editorial@finweek.co.za

Photos: Supplied

Fancy yourself a general knowledge whizz? Then give our first quiz of November a go! You can complete it online via fin24.com/finweek from 2 November.

1. **True or False?** The South African government approved an export tax on chrome ore.
2. Struggling state-owned agricultural lender Land Bank asked government for an extra R10bn. In what year was the Land Bank founded?
   - 1912
   - 1997
   - 2008
3. **True or False?** The SABC is launching a streaming service.
4. The Hawks crime investigation unit was established as an independent directorate within which institution?
   - South African Revenue Service
   - South African State Security Agency
   - South African Police Service
5. Who was appointed as the new auditor-general of South Africa?
6. To which area is Anglo American moving its Johannesburg headquarters?
   - Sandton
   - Rosebank
   - Waterfall City
7. **True or False?** No permit is required to harvest abalone in SA.
8. How much did the JSE fine Steinhoff International for breaching listing requirements?
   - R7m
   - R13m
   - R27m
9. **True or False?** Exxaro is buying a 24.4% stake in Vedanta Zinc International's Black Mountain Mining operations from the IDC.
10. Which SA city is known as the 'Jacaranda City'?

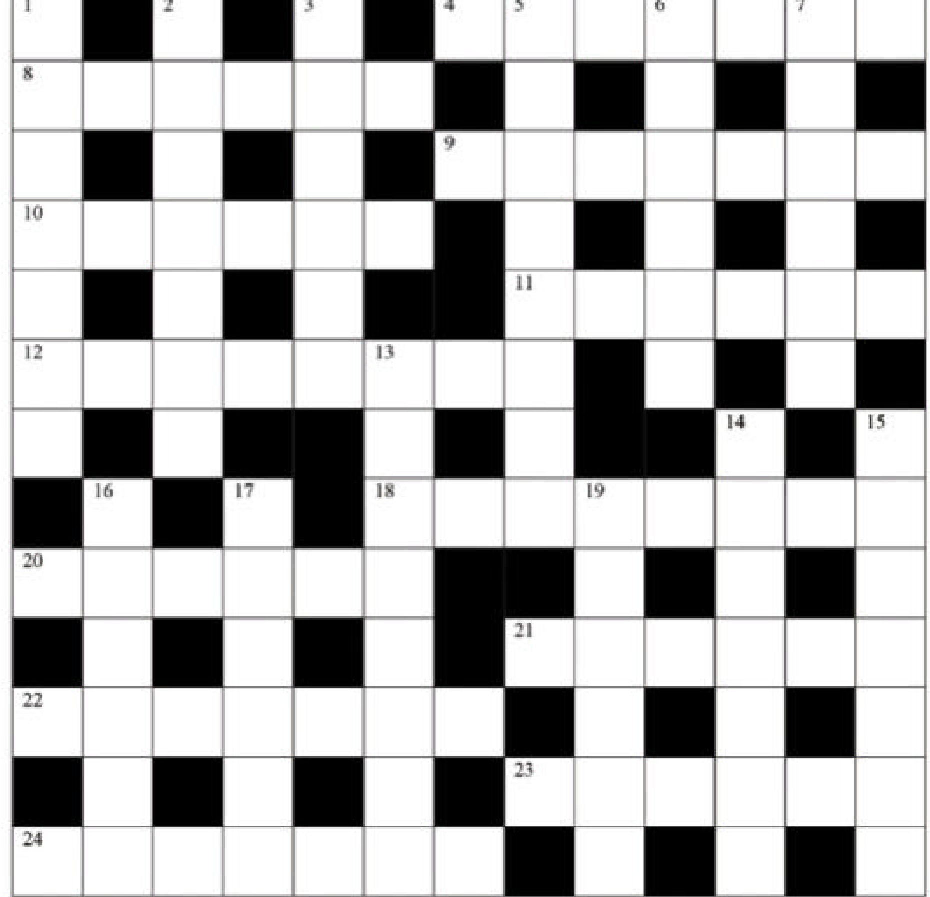
CRYPTIC CROSSWORD — NO 764JD

ACROSS

4 Cheeky monkey, sadly, hangs on to other animals (7)
8 Accountant into criminal practice (6)
9 Understanding things writer can achieve (7)
10 Directions concerning identification of sea goddess (6)
11 Earthly god gone again out of the woods (6)
12 Why does it matter two broke with faith? (4,2,2)
18 Unsound state according to World Body representative broadcast (8)
20 Crash warning latest (4,2)
21 It's a tragedy the way the operating system's put together (6)
22 Leading dealer at state bank (7)
23 Nobleman accepting the point, can relate to the subject (4,2)
24 & 5 Down Cure in the cabinet (7,8)

DOWN

1 Disappointment for fast traveller (3,4)
2 This triangle is foreign but not unknown (7)
3 In foul mood having to embrace theory (6)
5 See 24 Across
6 Each having a gun (6)
7 Be fast with mailshot locally (6)
13 & 14 Sorry state of hot and suffering organisers (8,7)
15 Gift having been posted earlier (7)
16 Watch over old boy's summerhouse (6)
17 Live quartet on the radio earlier (6)
19 Plantations in Thailand offer a service to extract rubber (6)



Solution to Crossword NO 763JD

ACROSS: 1 Not a hope; 5 Dahl; 9 Steam; 10 Tonnage; 11 Dart; 12 Insomnia; 13 Tender-hearted; 18 Mindless; 19 Iota; 20 Aphasia; 21 Using; 22 Sips; 23 Desserts

DOWN: 2 Outrage; 3 Adapted; 4 Put in the shade; 6 Against; 7 Leeward; 8 Angora; 13 Tomcats; 14 Nunship; 15 Enlist; 16 Reissue; 17 Extinct

On margin

Self-serving healers

This issue's isiZulu word is *isangoma*. The purpose of *isangoma* is to heal and protect people in the community. *Izangoma* (plural) have a direct line to ancestors. Some are herbalists but not all are. *Izanyanga* (medicine men) are primarily the herbalists. *Isangoma* is definitely not a witch doctor. Witchcraft is the arena of *umthakathi*. Speaking of *abathakathi* (plural), can the *umthakathi* who put a spell of forex and Bitcoin scammers on me lift it now? It's enough.

A new colloquial term doing the rounds is "*slayngoma*" – a fashionable, Instagram-loving sangoma.

I have a question: Is being *isangoma*, and getting paid for it, a second job – moonlighting?

At the rate people are becoming *izangoma*, job interviews should go like this:

Employer: Do you think you might have a calling in future? Does anyone in your family have a calling? Tell me about your dreams. No, not your hopes and ambitions. Dreams that you have, while you sleep.

A few years back, a sangoma friend called me to tell me that my ancestors had contacted his ancestors to tell them to tell him to tell me I have a calling. I told him to tell his ancestors not to listen to those drunks and junkies, as my lineage has a long history of substance abuse.

Seriously though, can all ancestors be trusted? I am not sure about this and suspect I would make a bad one – a lazy one. My general response would be "I am dead. Leave me in peace. What does rest in peace mean to you? Come on."

I also wouldn't trust PPE scammers to make good ancestors – they are just too selfish, and will be busy, trying to buy Gucci, Ferrari and Moët in the afterlife, instead of helping those they were tasked to help. It would be a mess.

– *Melusi's #everydayzulu* by Melusi Tshabalala

Bea @lavafairys
Whoever put the "s" in lisp is wrong for doing that.

Vamp Capital @RampCapitalLLC
Is it selfish to only care about my own stocks?

Pinky Sithole @PinkySithole17
202 days of lockdown. I remember cupcake lying to us that it would be 21 days.

> **Kristia van Heerden** @kristiavh
> 21 days was the deposit. This is the balloon payment.

Colin Barrett @ColinBarrett82
Massive respect to everyone still experiencing time as a linear sequence.

Mark @TheCatWhisprer
One day I hope to be wealthy enough to not do a doubletake every time I see abandoned furniture on the side of the road.

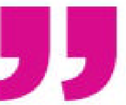
Jim Acosta @Acosta
Obama at event for Biden: "Can you imagine if I had a secret Chinese bank account? ... They'd call me Beijing Barry."

Abbi Crutchfield @curlycomedy
I did that thing where you insist on wearing makeup during the pandemic, and now the inside of my mask looks like I chloroformed a clown.

Elizabeth Windsor @Queen_UK
Covid restrictions mean that only six people will be able to attend the Liberal Democrat conference this year. Which, ironically, is more than usually attend. #LibDemconf

"Paths are made by walking."

– Franz Kafka, Bohemian novelist (1883 - 1924)



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