



# OLD MUTUAL WEALTH JOURNEY

## WELCOMING THE NEW YEAR WITH OPTIMISM

At the start of the year, there is always greater confidence that the challenges of the past will not repeat themselves.

Even though it could be easy for SA investors to be bearish given the news headlines, price increases across the board and increasing load shedding, there are also many positive factors. Analysts believe that the interest rate cycle is nearing its peak if inflation continues to drop back into the target range. Finance Minister Enoch Godongwana's Budget Speech was also broadly positive, with many praising the incentivisation of rooftop solar, energy support packages as well as relief in terms of personal income tax.

## FOCUSING ON THE LONG TERM

As always, we approach investing as a long-term game and believe that a sound investment plan can lead to higher returns over time. It's important to ignore the noise, avoid short-term emotional decisions, and focus on what you can control. By adopting different portfolio strategies, investors can remain invested during the ups and downs without sacrificing (too much) sleep.

## MAKING AN IMPACT ON THE GLOBAL AGENDA

Old Mutual recently attended the annual meeting of the World Economic Forum (WEF), an international organisation that connects leaders from business, government, society and academia, engaging in forward-looking conversations to address the state of the world and discuss priorities for the year ahead. We are proud to be part of these discussions and working with a broad spectrum of global decision-makers to develop frameworks, ideas and approaches that address some of the world's most pressing and complex challenges.

## SCOOPING AWARDS

Old Mutual Wealth was recognised at the inaugural Asset TV Audience Choice Awards.

We received the following awards:

- Most Watched: Roundtable (Retail) – Tax Efficient Solutions with Tiaan Herselman as panellist
- Most Watched: DFM Session – Asset Allocation with Roland Gräbe as panellist
- Most Watched: Person (Overall) – Roland Gräbe.

These awards reflect our commitment to supporting the planner community in adapting to our ever-changing environment and producing thought leadership content that is as informative as it is engaging.

## ANOTHER SUCCESSFUL HARD QUESTIONS CAMPAIGN

We kicked off 2023 with the next phase of our very successful Hard Questions campaign, focusing on building generational wealth. In this series, our team of wealth and investment specialists answer some hard questions about how your money can work as hard as you do, to help you build wealth for generations to come. Their answers are based on collective insights and extensive research that considers all facets of life. Whether your goal is to grow your wealth, generate income or preserve and pass on capital, our focus on generational wealth ensures your legacy will last for generations to come. Make sure you visit [www.oldmutual.co.za/wealth/hq-buildingwealth](http://www.oldmutual.co.za/wealth/hq-buildingwealth) for some insightful content and views from our experts, who have been creating wealth for decades.

## PARTNERING WITH YOU

Thank you for your continued support and for allowing us to be part of your wealth journey. We remain committed to ensuring that our strong, skilled investment teams, robust business processes and risk-aware approach will provide you with peace of mind as we partner with you on your wealth journey.



**FARHAD SADER**

MANAGING DIRECTOR OF  
OLD MUTUAL WEALTH

# CONSIDER THE DIVERSIFICATION BENEFITS OF HEDGE FUNDS

NOSIBUSISO NGQONDOYI | HEAD OF HEDGE FUNDS AT OLD MUTUAL MULTI-MANAGERS

*During periods of consistent market decline, long-short equity hedge fund managers enjoy distinct advantages over traditional long-only equity fund managers because they can profit from declining share prices.*



For the fourth consecutive year, the Old Mutual Multi-Managers Long Short Equity Fund of Hedge Funds was recently named the best fund of funds over 10 years at the HedgeNews Africa Awards 2021, with a net annualised return of 11.9% and a Sharpe Ratio of 0.90.



The South African hedge fund industry boasts a successful track record since the launch of the very first hedge fund more than 25 years ago. Over the last decade, the median equity long-short hedge fund has outperformed traditional equity funds by more than 1% per annum net of fees (to end of December 2022) raising questions about the low exposure that retail investors have to this alternative, listed asset class.

In this context, widening the hedge fund offering to retail investors could allow ordinary South Africans to benefit from a different source of return that is largely uncorrelated with the other asset classes in their portfolios.

Although South Africa's hedge fund industry has over R80 billion in assets under management, it has made little headway in attracting individual investors, with around 95% of the industry's assets held by institutional investors, predominantly pension funds. Much still needs to be done to educate investors about hedge funds before the status quo can change.

Hedge funds are described as funds that allow fund managers to generate returns from both buying and selling of various asset classes. In the long-short equity hedge fund space, fund managers can thus profit from increases in share prices, and from selling shares that they expect to fall in price, also known as "short selling".

To illustrate this, over the period June to September 2022, the JSE All Share Index was down almost 10% compared to the median return of local long-short equity hedge funds, which was up more than 1% over the same period, while the Old Mutual Multi-Managers Long Short Fund of Hedge Funds delivered a 4% return, an almost 15% outperformance compared to equities over the same period, net of fees. This is because the mechanisms of short selling create other value opportunities for hedge fund managers.

Hedge funds generate excess returns for clients because when you short a share, you effectively borrow that share and sell it in the open market with the view that the share price will fall, and later buy it back at a lower price. The fund manager can use the cash generated from the sale to

amplify fund returns by, for example, increasing exposure to shares that are expected to increase in value.

Financial advisers and fund managers have three motivations to encourage retail investors to increase exposure to hedge funds:

- 1** First, the hedge fund industry is mature and well regulated. Hedge funds have been available locally for almost three decades and have been regulated alongside traditional unit trust funds since 2015, when they were included under the Collective Investments Schemes Control Act.
- 2** Local managers have extensive skill in managing hedge funds across a range of investment mandates.
- 3** Fees have come down significantly since the early days.

Due to asset managers reaching critical mass we have seen a halving of the base fee, with increased competition driving down the performance fee when fund managers exceed their targets. Funds of hedge funds are usually able to negotiate even lower fees with hedge funds managers. Unit trusts can take advantage of this because they pool clients' investments, which sets them up perfectly to take advantage of the above.

The performance from the hedge fund space has been stellar and is reported net of fees. While fees are a key consideration it makes sense to focus on the value added by a well-diversified fund of hedge funds to an investor's portfolio. The fact that some investors have zero exposure to hedge funds is a lost opportunity.

As a planner-led business, we encourage investors to seek professional advice from a qualified and an accredited financial adviser on how hedge funds could enhance their overall investment portfolios for a better outcome in navigating the complex world of hedge funds, rather than doing so unassisted.

# THE BIG BUDGET THEMES

IZAK ODENDAAL | INVESTMENT STRATEGIST AT OLD MUTUAL MULTI-MANAGERS

Most people think of the Budget as a speech, but it is actually a 280-page document.

It is useful to step back and focus on four overarching themes.

## 1. GET GROWTH GOING

The starting point for the Budget is a projection of economic growth, on which assumptions about tax revenue growth can be based. These forecasts must be sensible if the Budget is to have any credibility. Treasury expects real economic growth of 0.9% this year, 1.5% in 2024 and 1.8% in 2025.

The 2023 Budget emphasises the fragile state of the economy, highlighting the devastating toll of load shedding and a crumbling logistics network, both due to inefficient state-owned enterprises. The tax breaks for rooftop solar installation, with businesses being able to reduce taxable income by 125% of the cost of solar panels, will support economic growth in the short term. The less-generous incentive for households can help persuade a few undecided homeowners.

The debt relief for Eskom includes Government taking over its interest and capital repayment commitments over the next three years at R186 billion, absorbing R70 billion of Eskom's debt directly. This will give Eskom more room to breathe financially and invest in transmission capacity. Fixing the operational and governance side of things still has a long way to go.

## 2. FISCAL CONSOLIDATION COMMITMENT REMAINS

The commitment to fiscal consolidation remains. Despite a looming election, Government is dedicated to getting its debt under control by increasing spending discipline. As of this year, projected non-interest spending will be less than tax revenues. However, spending on interest remains substantial, and this is precisely why fiscal consolidation matters. Failure to reduce borrowing means the debt service burden will continue to rise, squeezing out other important areas of spending. Already, almost 20 cent of every tax rand goes to debt service costs. It is not sustainable to allow this to continue growing.

## 3. KEEPING THE GOLDEN GOOSE ALIVE

Another theme is that Treasury is mindful of not taxing the economy, particularly the middle class, to death. There have

been calls for a basic income grant, but there is no money and we are rather likely to see a continuation of the R350 per month Covid social distress relief grant.

No new tax increases were tabled apart from the usual sin tax increases on tobacco and alcohol. Keep in mind that sin taxes are not percentage-based taxes. In a period of high inflation, the easiest thing for Treasury to do would be to let inflation push people into higher tax brackets, thereby quietly creaming off a few extra rands. Instead, Treasury will raise the tax brackets by 4.9% foregoing R15 billion in personal tax revenue. This is the largest amount of "fiscal drag" relief in many years.

## 4. THE HOW

The prudent way in which Treasury manages debt is another theme that gets little attention. It has always kept foreign currency borrowing low, and it will continue to be around 11% of the total. Otherwise, a weak rand would lead to a rising debt burden.

Treasury also tries to spread the debt out across different maturities, so that it doesn't face the problem of a large portion of debt maturing at once. It also didn't assume that the commodity price windfall of the past two years will persist, and just as well, since these prices are now normalising following the disruptions of the pandemic and then the war in Ukraine.

The transparency of the budget process is also crucial. Treasury publishes monthly data on government revenue and spending so investors know exactly what is going on.

### WHAT ARE THE INVESTMENT IMPLICATIONS?

The asset class most impacted by the Budget is bonds. The 2023 Budget should put a floor under the bond market's rating and is another important step towards winning back the market's trust. South African bonds should continue to deliver decent real returns as the yield is well above inflation, with inflation likely to be reasonably well behaved over the medium term.

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