

MACROSOLUTIONS

INVEST WITH PERSPECTIVE



SAVINGS & INVESTMENT MONITOR



JULY 2016

RIAN LE ROUX

DO GREAT THINGS



WHO SAVES AND WHY?

Households

- Forgoing current consumption to enhance future consumption
- So, HH's save to finance *future big expenses & retirement*

Companies

- Savings = undistributed profits
- These retained profits used to finance *replacement & expansion*

Government

- Saving = tax revenue > current spending
- Excess tax revenues finance *physical & social infrastructure investment*

As a Nation

- Saving = HH's + Co's + Govt
- Savings finance *Investment*

A FEW IMPORTANT REMINDERS

Saving and investment interplay

- Sufficient saving is a necessary, *but not a sufficient*, prerequisite for investment
- Or, without savings, investment cannot occur (or little saving = little investment)
- *But, sufficient savings do not guarantee that investment will occur*

For investment to occur, macro-conditions must be conducive, e.g.

- Good macro-economic conditions and prospects
- A business-friendly environment, incl. policy certainty and predictability (at macro and industry levels), good infrastructure, bureaucratic efficiency, political stability, entrenched property rights, etc, etc

Excess savings over investment will either seek a home elsewhere (abroad) or be returned to shareholders

REVISITING MY KEY MESSAGES OF THE PAST FEW YEARS



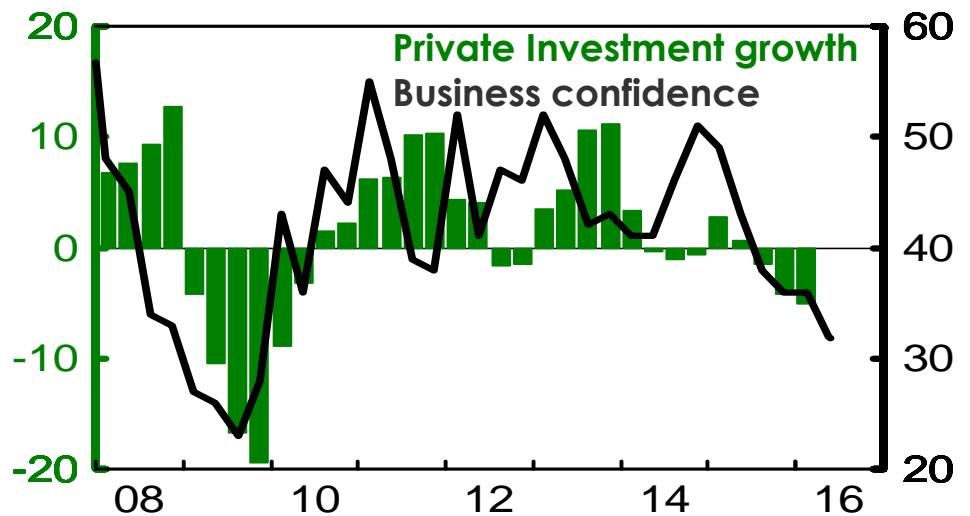
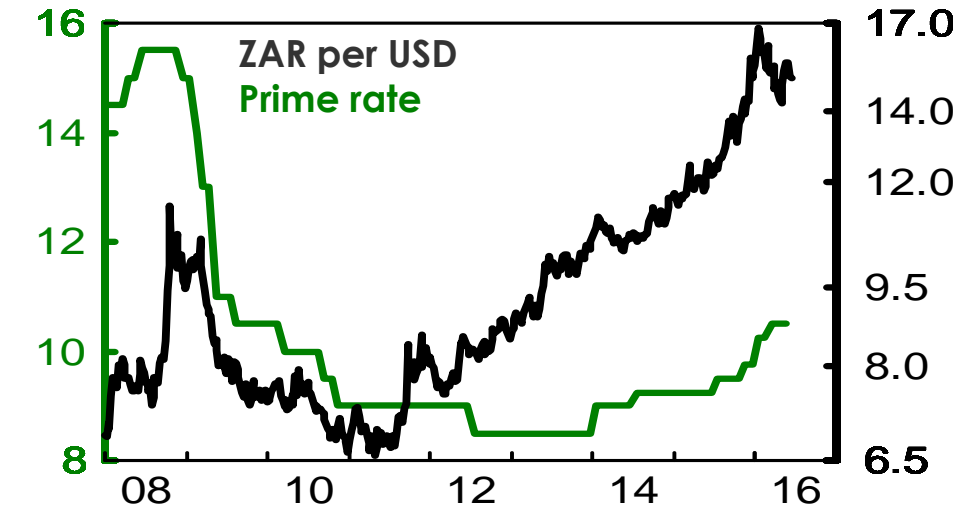
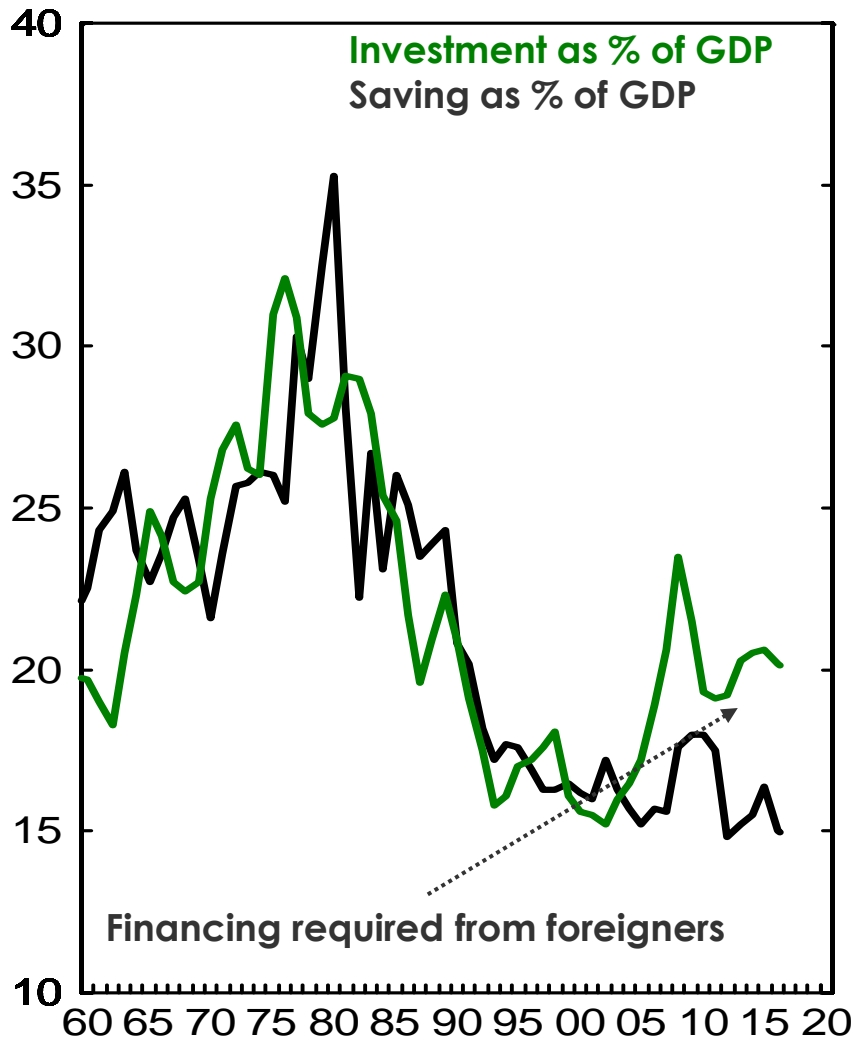
On the overall growth and savings environment at a macro level

- SA, as a nation, saves too little – *it will eventually cause pain somewhere, likely severe*
- SA's weak economic growth performance is a huge risk
 - It is undermining job growth, raising dependency ratios
 - It is pressuring government's fiscal situation
 - It is risking worsening socio-economic unrest
 - It risks a vicious circle: little saving = little growth = less saving = less growth = less saving...
 - It will force companies to externalize their savings (i.e. seek opportunities abroad)
 - It risks losing investment grade rating
- **Some of our growth problems are beyond our control:**
 - But there are sufficient things we can do to make a meaningful, positive difference
 - Failing to make *correct* policy interventions *will make matters worse*
 - Making *wrong* policy interventions *risk a crisis*



THE MACRO-ECONOMIC PAIN FINALLY ARRIVES...

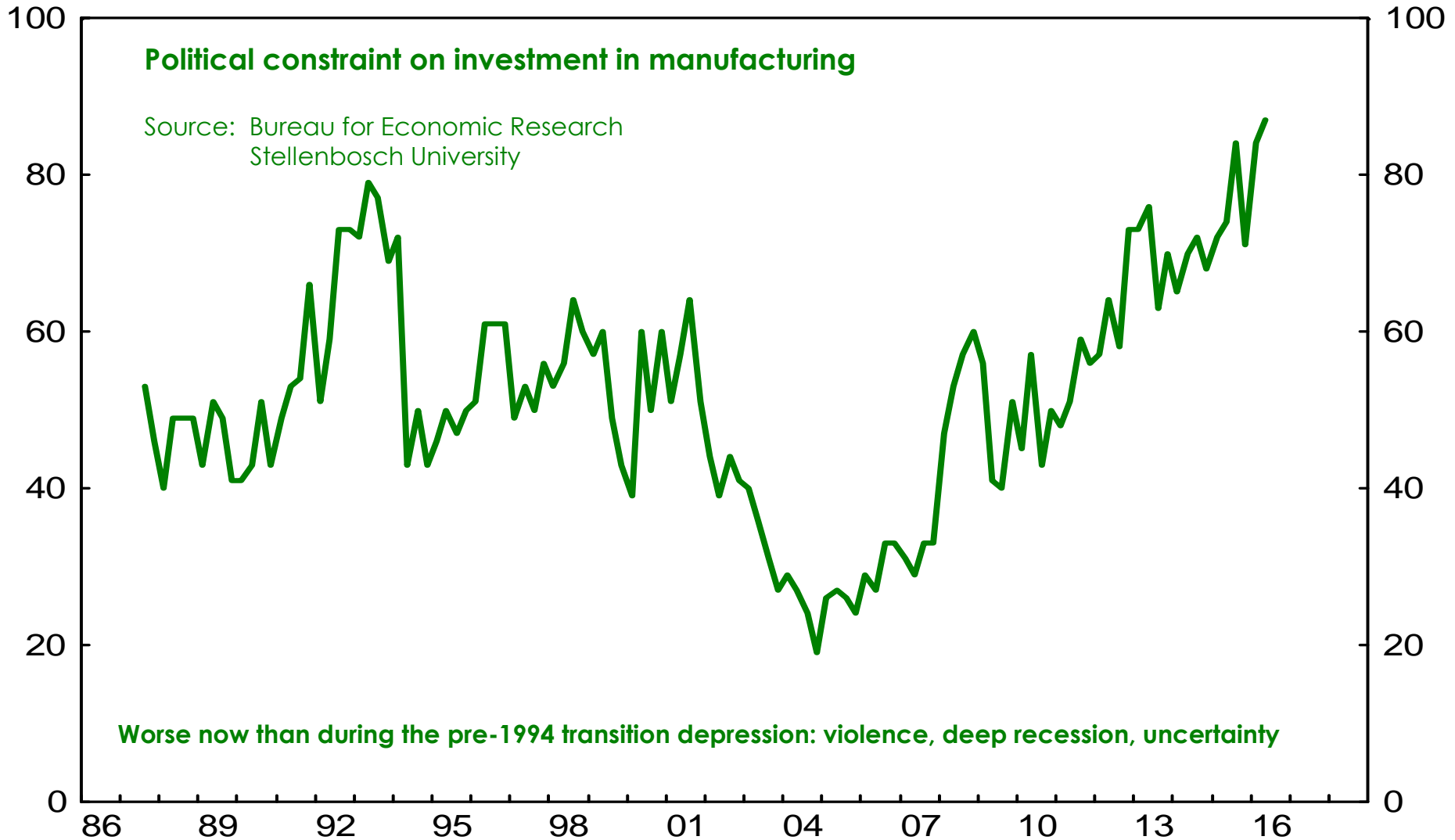
AND THERE ARE VARIOUS TRANSMISSION MECHANISMS



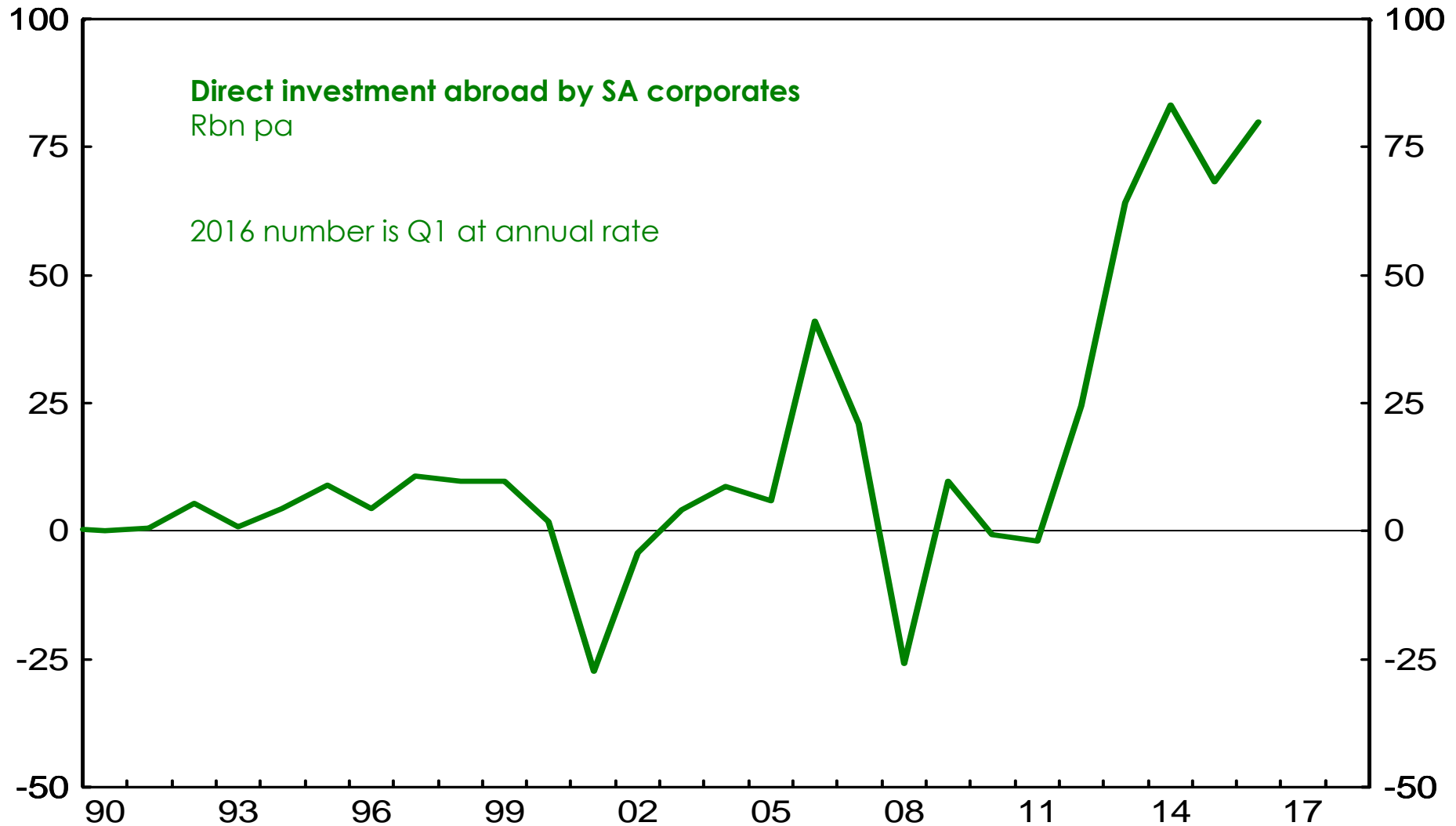
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POLITICS IS A MAJOR CONCERN

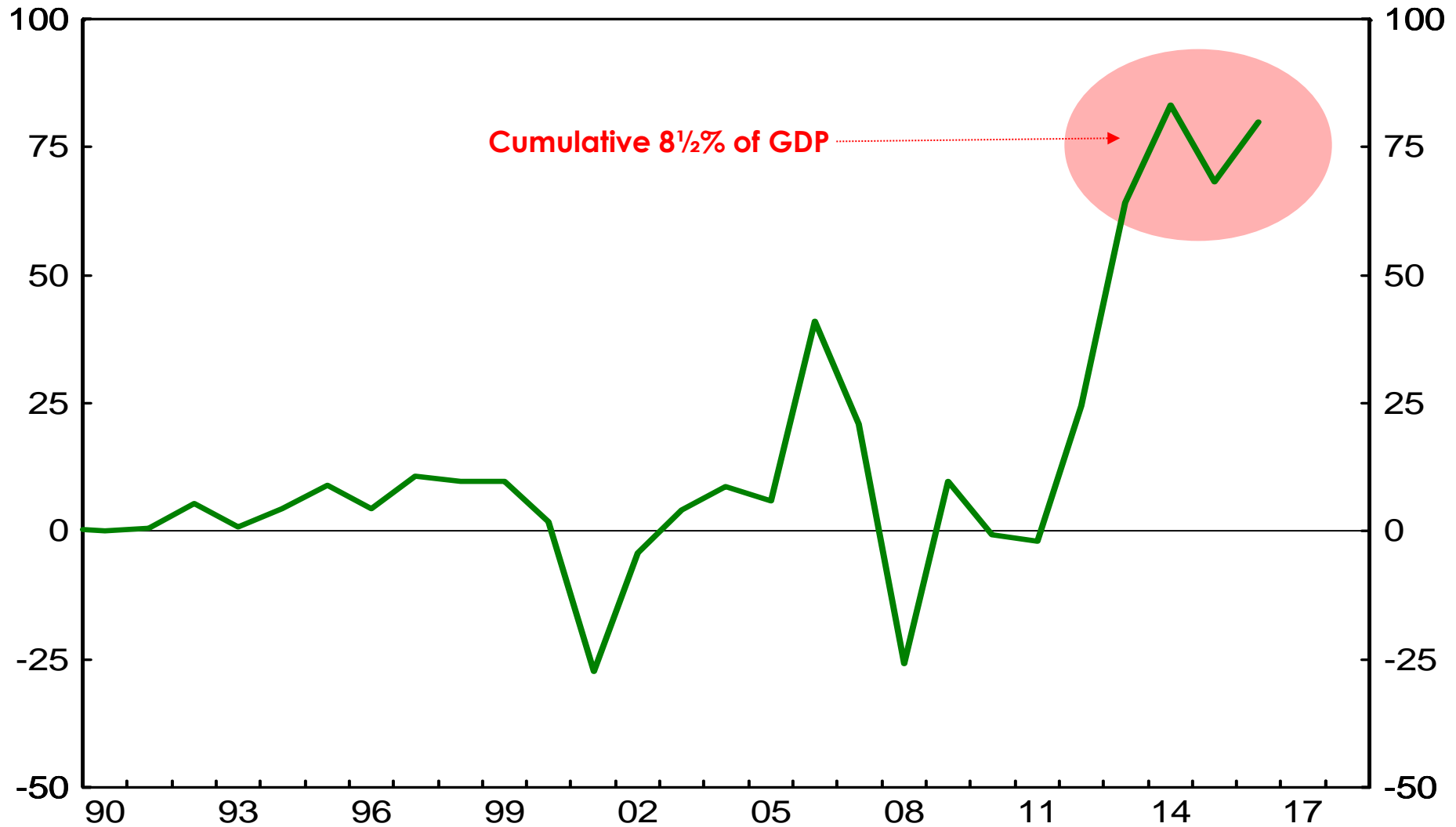
IT IS ALL ABOUT CONCERNS OVER A BUSINESS-FRIENDLY ENVIRONMENT, RISK OF POPULISM AND SOCIAL UNREST



...AS PREDICTED, BUSINESSES INCREASINGLY SEEK OPPORTUNITIES ABROAD...

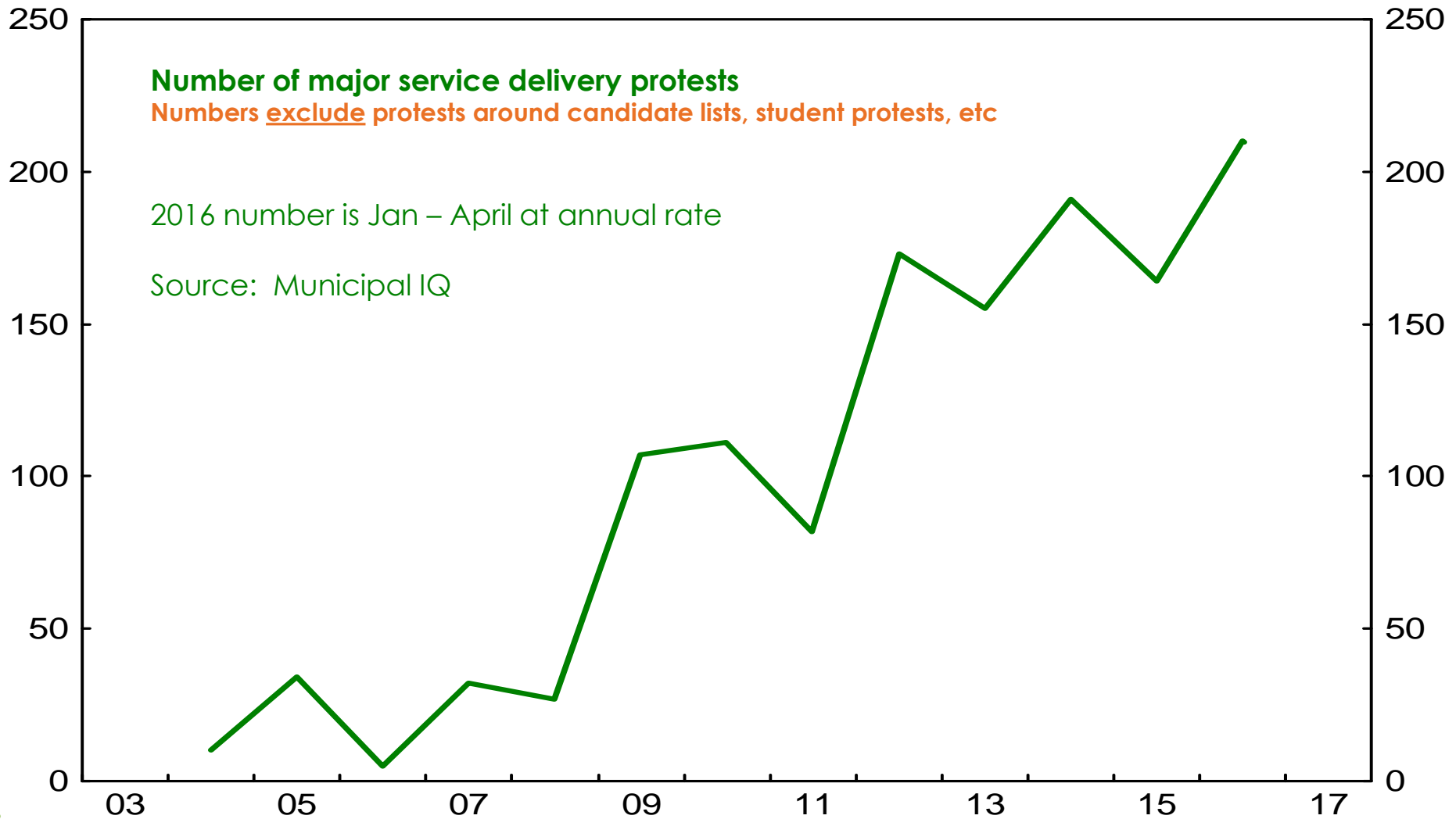


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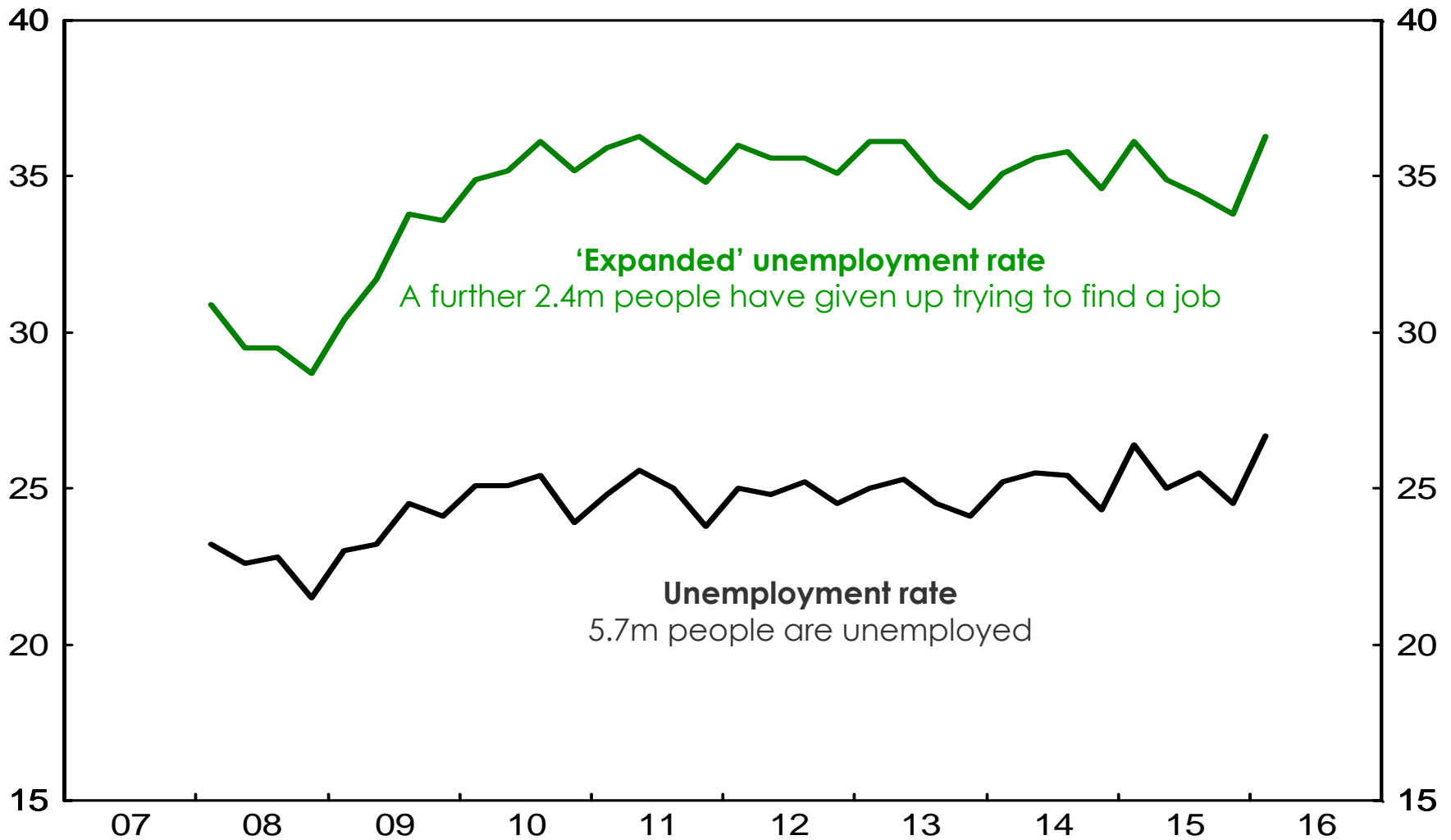
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...STREET TROUBLES ARE MOUNTING... AND SEEMINGLY MORE VIOLENT TOO



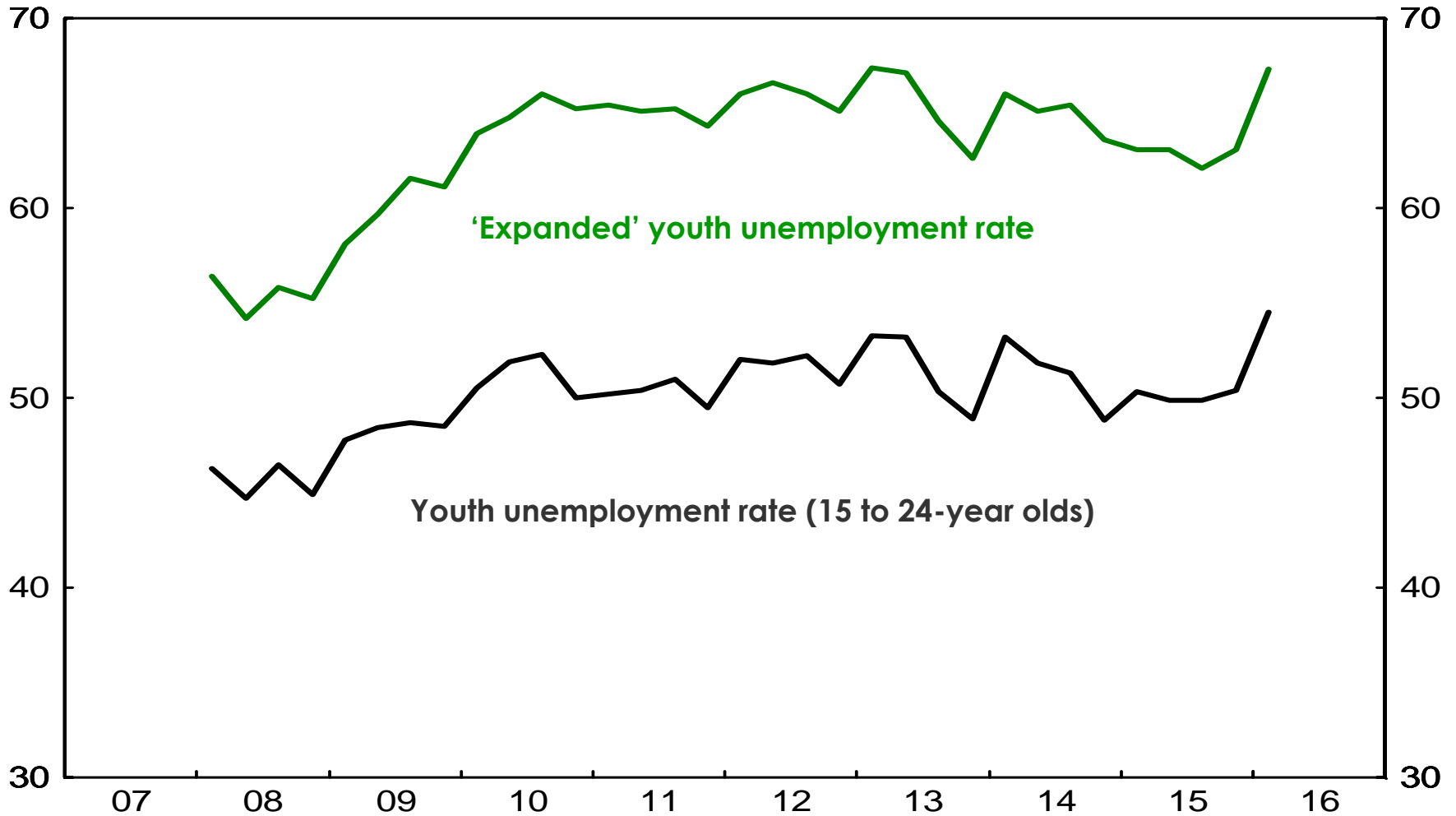
...AND WE'VE MADE NO PROGRESS WITH UNEMPLOYMENT...

IN FACT, IT'S GOTTEN WORSE

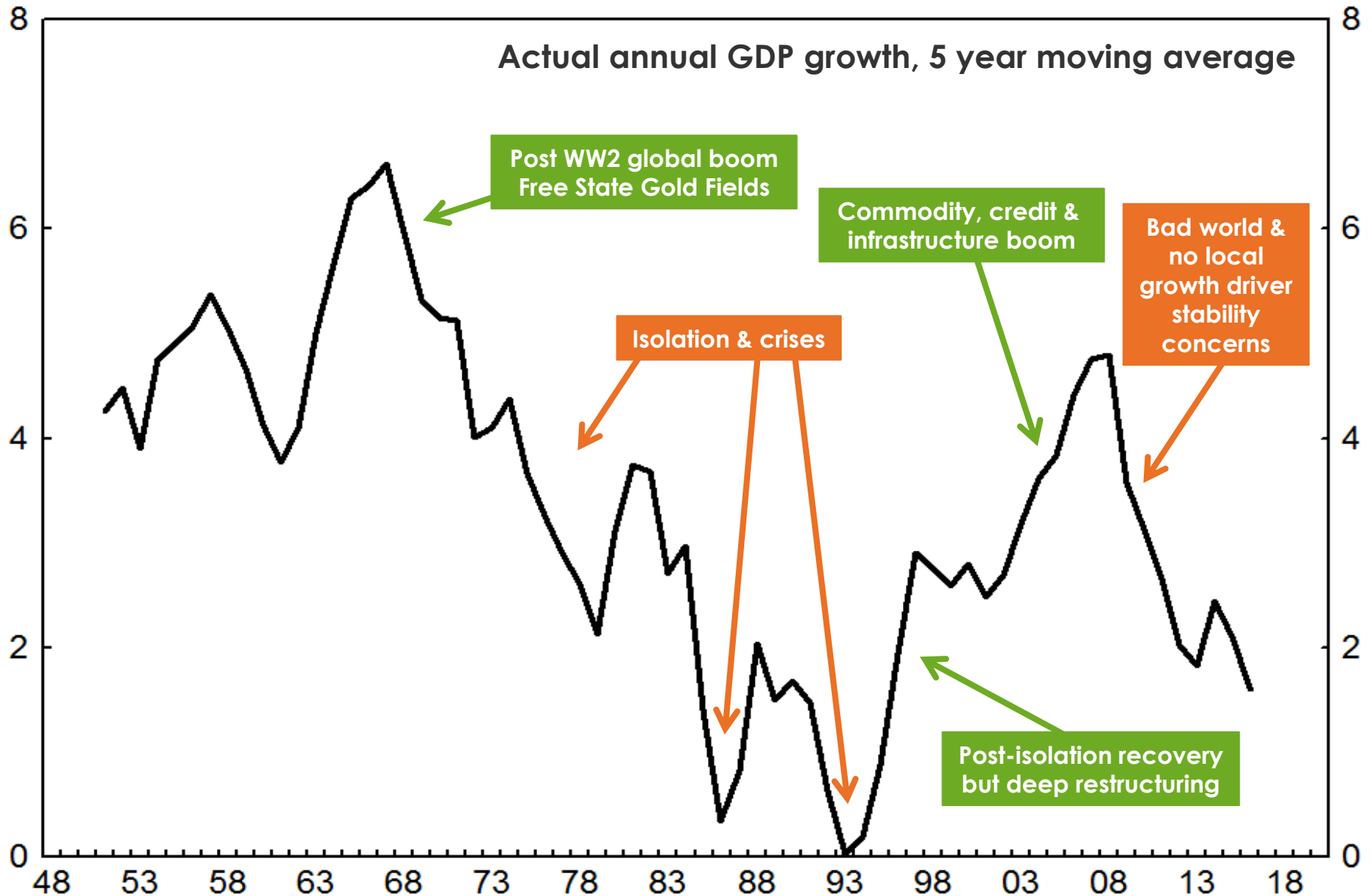


...ESPECIALLY YOUTH UNEMPLOYMENT

BETTER MATRIC PASS RATES HAVE DONE ZERO FOR THE YOUTH UNEMPLOYMENT RATE



SO, RAISING THE GROWTH RATE HAS NOW BECOME CRITICAL



WHAT IS THE TROUBLE...?

- **Weak global growth:**
depressed commodity prices & weak export demand
- **No sector boom:**
a la mining in the 1950/60's, stimulating other forms of activity
- **No infrastructure boom:**
big numbers yes, but no *net growth*
- **No strong consumer spending support:**
rates, taxes & inflation rising, employment falling
- **SA lacks strong global competitiveness:**
remains a major issue
- **Electricity bind:**
as availability constraints ease, price becomes a constraint on competitiveness
- **Policy uncertainty and a rising regulatory burden**
- **Messy politics and a rising risk of a drift into populism**
- **A deep and intensifying confidence crisis**



WHAT NEEDS TO BE DONE...?

- Address cyclical problems: C/A & fiscal deficits & inflation pressures
- Address the deep distrust between Govt, Labour and Business
- Create greater policy certainty, both on a macro and sectoral level
- Address SA's highly problematic labour relations
- Speed up social & economic infrastructure spend
- Aggressively address underperforming public institutions
- Ensure the more competitive ZAR is not undermined by higher inflation
- Finish those power stations!



WHAT NEEDS TO BE DONE...?

DO I DETECT PROGRESS, EVEN PROMISING IN SOME CASES?

- **Address cyclical problems: C/A & fiscal deficits & inflation pressures**
Progress, lots of risks
- **Address the deep distrust between Govt, Labour and Business**
Promising Progress
- **Create greater policy certainty, both on a macro and sectoral level**
Some hope
- **Address SA's highly problematic labour relations**
Progress under way?
- **Speed up social & economic infrastructure spend**
Strong drive to contain current spend
- **Aggressively address underperforming public institutions**
Much talk, little evidence
- **Ensure the more competitive ZAR is not undermined by higher inflation**
SARB acting
- **Finish those power stations!!!!**
Definite progress



WHAT NEEDS TO BE DONE...?

DO I DETECT PROGRESS, EVEN PROMISING IN SOME CASES?

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Progress, lots of risks

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Promising Progress

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BUT:

- **Address SA's high unemployment, Acute concerns over politics, populism, corruption & patronage, undermining of Treasury and Finance Minister, unaffordable projects, rising unrest & destruction**
Progress under way?

- **Speed up social & economic infrastructure spend**
Strong drive to contain current spend

- **Aggressively address underperforming public institutions**
Much talk, little evidence

- **Ensure the more competitive ZAR is not undermined by higher inflation**
SARB acting

- **Finish those power stations!!!!**
Definite progress



REVISITING MY MESSAGES ON HOUSEHOLD SAVINGS OVER THE PAST FEW YEARS

People that can save, save too little (many can't save)

- Often because they do not realise they need to save more
- Few people bother to fully understand their retirement provision status
- *So, many experience a painful living standard drop in retirement*
- *Saving more is a conscious decision that requires spending less today: tough for most*
- Many end up having to care for parents or being cared for by children
- People often claim they cannot save; *actually they just prefer not to*

Things are going to get tougher

- It is already hard for many people to save; it is going to get even harder
- Investment returns will be lower in future
- *So, just as it becomes more difficult to save, it becomes necessary to do just that*

People often make poor investment decisions

- They often fall for the *promise* of a higher investment return – forgetting about the risk, *they then often lose 100% of their capital*
- Too fixated with short term market volatility: this leads to poor long term investment decisions (MM funds!)
- As people have no savings goal, they have nothing to tailor their investment decisions on

My advice: be clever and safe

- **Clever:** start saving early (*when you are born*), have a goal and a plan
- **Safe:** beware of promises, stick to reputable institutions, consult a registered financial adviser

A LITTLE REMINDER...

ASSUME A WORLD OF NO INFLATION AND NO INVESTMENT RETURNS

SO, ALL YOU WILL NEED IN RETIREMENT MUST BE SAVED WHILE WORKING

ZERO INVESTMENT RETURNS, BUT ALSO ZERO INFLATION, SO PRICES ARE CONSTANT

YOU EARN THE SAME FOR 35 YEARS OF WORKING (25 – 60)

YOU RETIRE AT 60 AND LIVE ANOTHER 25 YEARS

WHAT PERCENTAGE OF YOUR MONTHLY INCOME MUST YOU SAVE TO HAVE 75% OF YOUR WORKING LIFE MONTHLY SALARY AVAILABLE IN RETIREMENT?

54%

It highlights the implicit reliance on obtaining high real returns on retirement savings over one's entire working life

HIGH RETURNS IS EXACTLY WHAT WE HAD, BUT, SADLY, NO LONGER

1960 – May 2016

Sector	10 years 60-69 (%)	10 years 70-79 (%)	10 years 80-89 (%)	10 years 90-99 (%)	17 years 00-16 (%)	57 years 60-16 (%)	What we expect* (%)
Shares	15.8	21.3	26.7	16.6	16.7	19.1	10.0
LT Gilts	4.5	6.8	11.8	19.5	13.2	11.4	9.0
Cash	4.4	8.2	14.8	16.2	8.3	10.1	6.5
Inflation	2.5	10.3	14.7	9.4	6.1	8.3	5.5

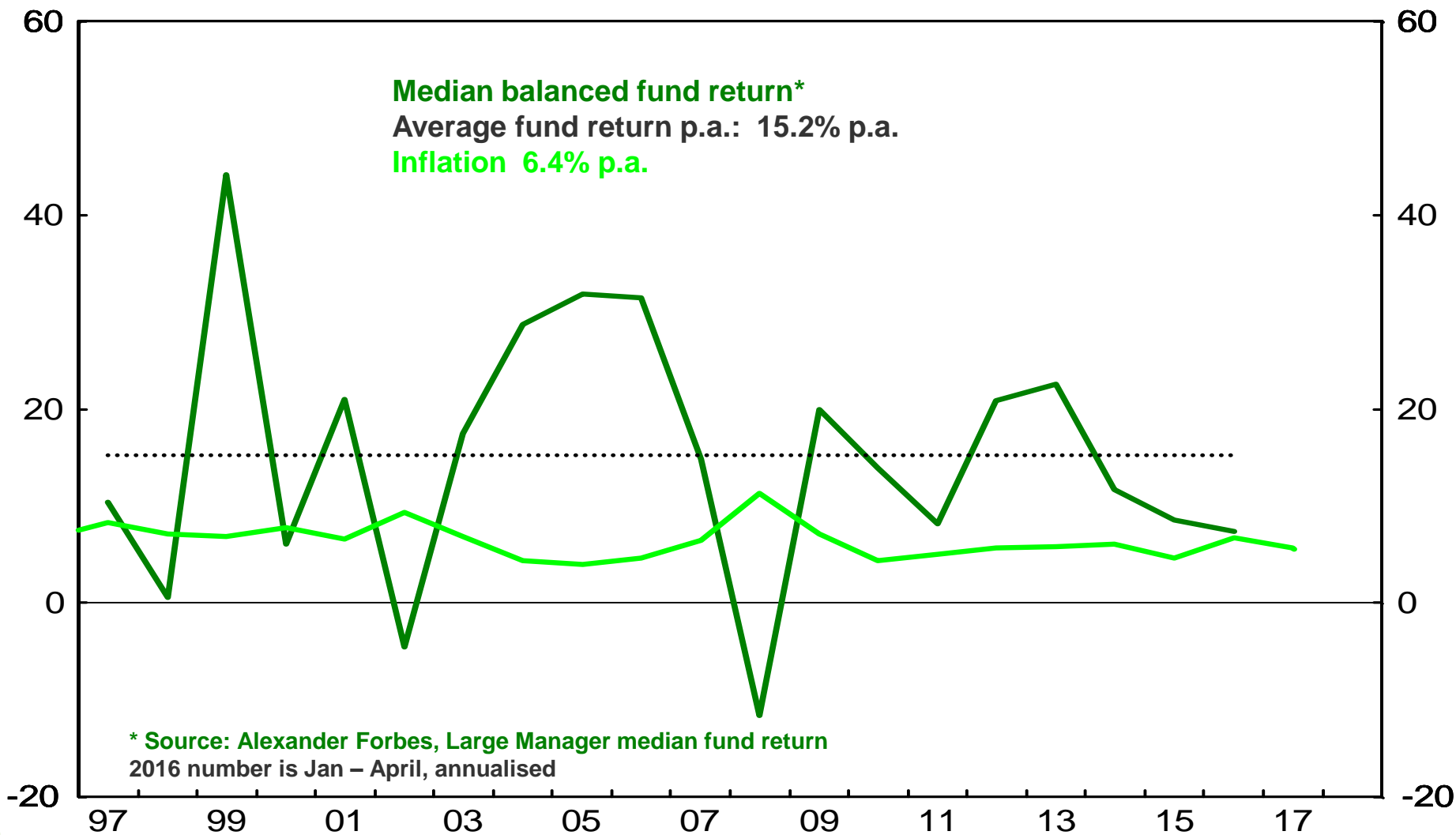
* Our estimates

Balanced Fund of 60:30:10

Over 57 years: 15.9% vs 8.3% inflation = 7.6% real
 Going forward: 9.4% vs 5½% inflation = 3.9% real

LOTS OF LESSONS FROM INVESTMENT RETURNS

THEY ARE SLOWING (AS PREDICTED); DON'T BE FIXATED WITH SHORT TERM VOLATILITY; A LONG TERM VISION REMAINS THE BEST STRATEGY, DIVERSIFICATION IS VITAL; LOWER RETURNS REQUIRE MUCH HIGHER SAVINGS



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HOW MUCH MUST YOU SAVE? – A GUIDE

35 years worked			
% saved	Inv. Return	% of pension taken	Pension as % of last salary
13	9.0	6.5	32
30	9.0	6.5	75
13	13.5	6.5	75
13	9.0	15.0	75

- All examples above assume 9% p.a. salary gain & 6% p.a. inflation
- Realistic overall Investment Returns going forward \pm 8% - 10% p.a. (vs \pm 15% p.a. past 15 years) – local assets

MESSAGE? Can't rely on high investment returns to build your capital, people will have to save far more

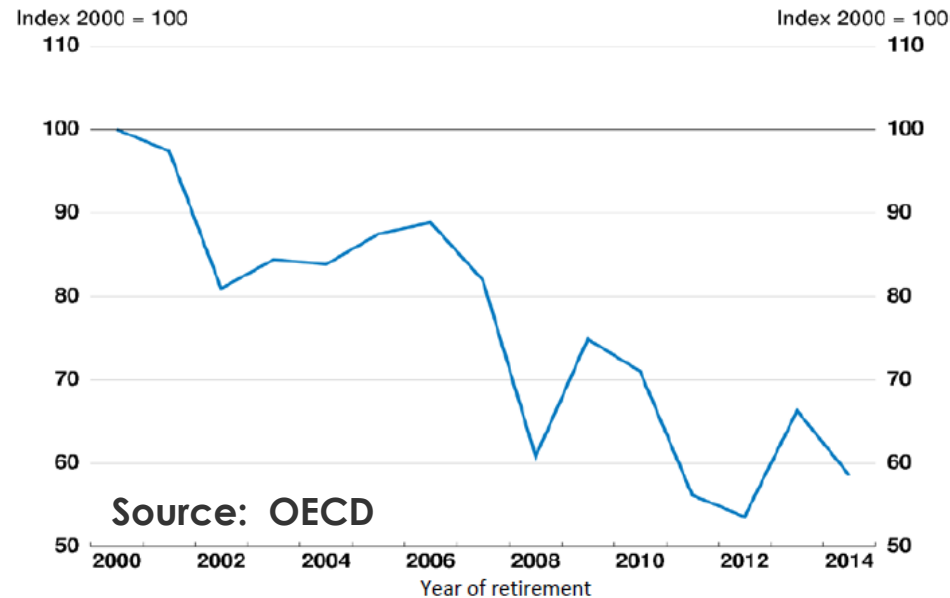
A STARK LESSON FROM THE OECD ON PENSION INCOMES



Keeping promises to older people is more difficult with low returns and low growth

Policy reforms become more urgent, including extending working lives

Falling retirement income for a given contribution



Source: OECD

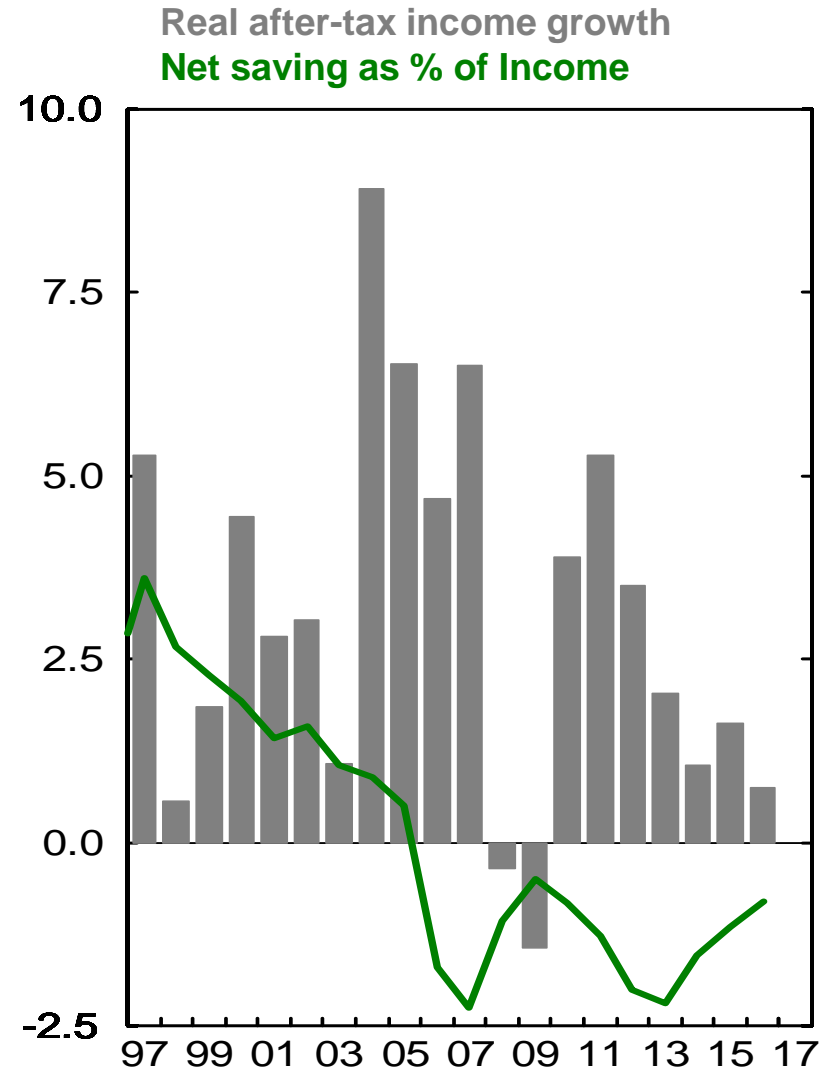
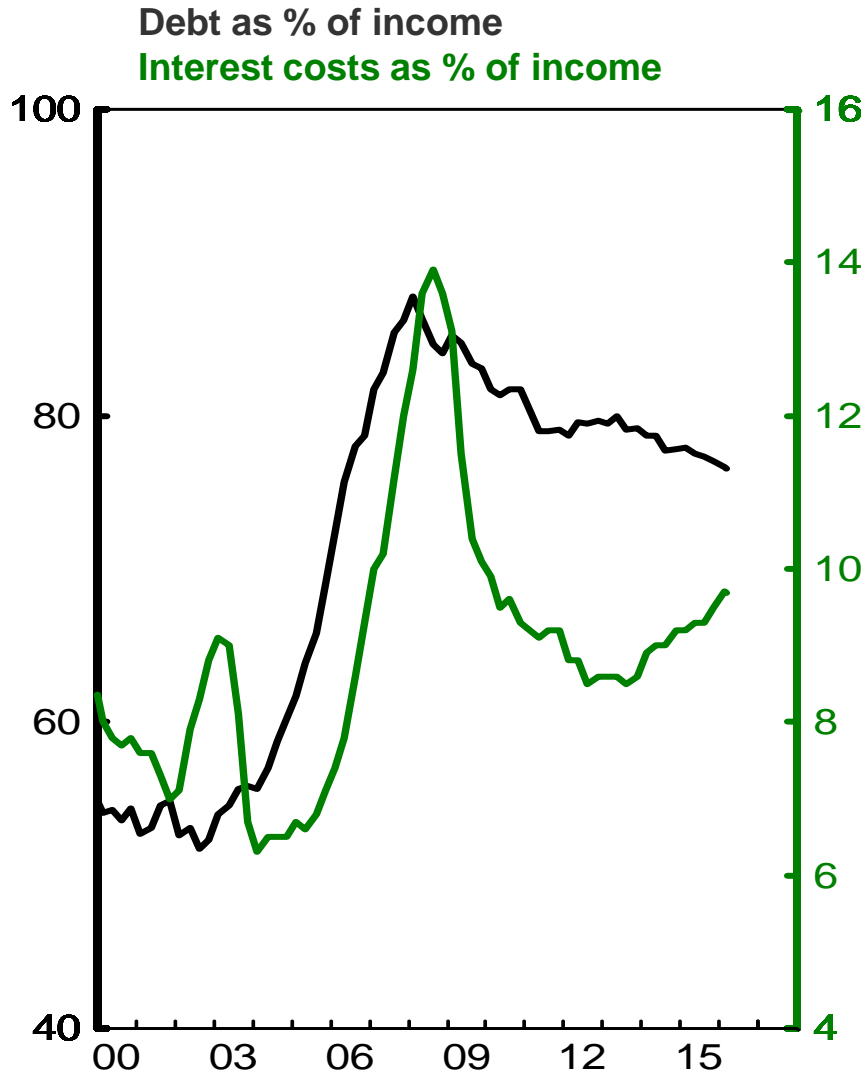
Note: The chart shows the impact of falling interest rates on real incomes in retirement for a defined contribution scheme. Annuity payments calculated for the same hypothetical individual contributing 10% of wages over a 40 year period. The assets are invested in a portfolio comprising 60% of variable income (fixed return of 4.5%) and 40% of fixed income (historical 10 year government bonds yields, kept to maturity) and used at retirement to buy an annuity with a life expectancy of 20 years at age 65 using actual government bond yields for calculating the annuity premium. Constant annual inflation of 2 per cent and productivity growth of 1.5 per cent are assumed.

Source: OECD Business and Finance Outlook 2016 (forthcoming).



HH'S UNDER PRESSURE: SAVING BECOMES A VERY CONSCIOUS DECISION

SAVING MORE BECOMES MORE IMPORTANT, JUST AS IT GETS MORE DIFFICULT



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THE MESSAGE IS LOUD AND CLEAR

PEOPLE NEED TO SAVE MORE!



TO 'GET IT RIGHT' EACH OF THESE HAVE CERTAIN REQUIREMENTS...

How long, and consistently, you save for

- Start at as early as possible – in investments, **time and discipline** are your best friends
- Advice for young parents: Save for the **children from birth**, make it contractual, increase it annually



How much you save

- This is really the only variable you can control
- For most people this is very hard as it requires spending discipline
- Keep a budget – and stick to it
- Teach your children, and yourself, the miracle of **compound returns**
- Teach your children, and yourself, the benefits of **proper budgeting**

Investment returns

- Beware of promises – 1% extra promised return, can cost you 100% of your capital
- The 'safest' investments (cash) mostly yields poor long term returns and rarely build real capital
- Tailor your investment decisions to your risk profile and time horizon
- Speak to a registered financial consultant

INVESTMENT REWARDS OF TIME AND CONSISTENCY

R150pm invested over 21.5 years to 30/5/2016, income reinvested

- Amount invested: R38 700
- Capital value at 31/5/2016:
 - **Balanced Fund: R195 798**
 - **Investors Fund: R270 236**

R150pm invested over 21.5 years to 30/5/2016, increased by inflation every year, income reinvested

- Amount invested: R76 326
- Capital value at 31/5/2016:
 - **Balanced Fund: R295 744**
 - **Investors Fund: R400 112**

If you do this for your children from birth, what a head start they have on their peers at 21!

SOME TRUTHS WORTH REMEMBERING

“A budget tells us what we can't afford, but it doesn't keep most people from buying it.”

“Good spending decisions are made when we know we're spending money, not fooled into thinking we're saving money.”

“Seek your happiness by limiting your desires, rather than in attempting to satisfy them.”

“He who will not economize will have to agonize.”

“Even if you have the money to buy something, it does not mean you can afford it.”

“There is no dignity quite so impressive, and no independence quite so gratifying, as living within your means.”

“We must consult our means rather than our wishes.”

“Budgeting has only one rule: Do not go over budget.”

“A certain way to have financial security in life is not enough savings, but enough ability.”



AND SOME HARD FACTS TOO...

The biggest present you can give **your children** is to never become dependent on them
(retirement provision)



The biggest present you can give **yourself** is to make your children independent of you
(education)



WHAT SHOULD PEOPLE DO NOW?



REMEMBER: Time is your best friend when it comes to capital building

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