Volume 16 No. 12
December 2020

# Benchmark Retirement Fund

## MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 DECEMBER 2020

By T H Friedrich – Retirement Fund Solutions Namibia (Pty) Ltd

The monthly review of portfolio performance, as set out in this issue, is also available on our website at www.rfsol.com.na.

### 1. Review of Portfolio Performance

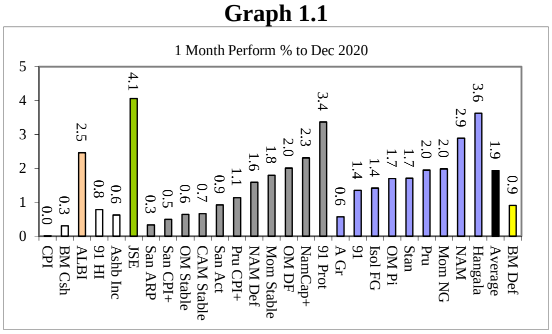
In December 2020 the average prudential balanced portfolio returned 1.9% (November 2020: 5.7%). Top performer is Hangala Prescient Absolute Balanced Fund with 3.6%, while Allan Gray Balanced Fund with 0.6% takes the bottom spot. For the 3-month period, NAM Coronation Balanced Plus Fund takes the top spot, outperforming the 'average' by roughly 3.4%. On the other end of the scale Stanlib Managed Fund underperformed the 'average' by 2.0%. Note that these returns are before (gross of) asset management fees.

**Graphs 1.1 to 1.10** reflect the performance for periods from 1 month to 20 years of a number of the most prominent prudential balanced portfolios (blue bars), 'special mandate portfolios' with lower volatility risk (grey bars), fixed interest portfolios (no color bars), the average of prudential balanced portfolios (black bar), the JSE Allshare Index (green bar), and the CPI (red bar). Benchmark investors should take note of the performance of the default portfolio (yellow bar), which represents a combination of Prudential Namibia Inflation Plus, Sanlam Inflation Linked and Allan Gray Namibia Balanced Funds. **Take note that we have added a new graph 3.5.3 which reflects the returns of the low risk special mandate funds**.

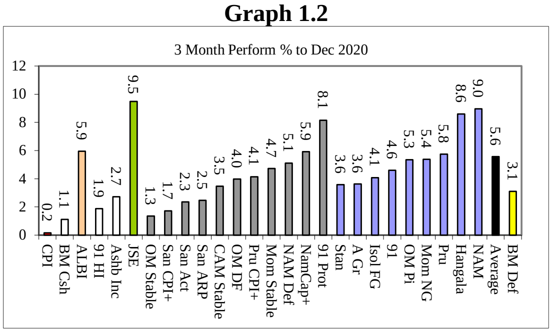
Below is the legend to the abbreviations reflected on the graphs:

| | |
|---|---|
| **Benchmarks** | |
| Namibian Consumer Price Index | CPI (red) |
| All Bond Index | ALBI (orange) |
| JSE Allshare Index | JSE Cum (green) |
| Benchmark Default Portfolio | BM Def (yellow) |
| Average Portfolio (prudential, balanced) | Average (black) |
| **Special Mandate Portfolios** | |
| Money market | BM Csh (no color) |
| NinetyOne High Income (interest bearing assets) | 91 HI (no color) |
| Ashburton Namibia Income Fund | Ashb Inc (no color) |
| Capricorn Stable | CAM Stable (grey) |
| Momentum Nam Stable Growth | Mom Stable (grey) |
| NAM Capital Plus | NamCap+ (grey) |
| NAM Coronation Balanced Def | NAM Def (grey) |
| NinetyOne Protector Balanced Fund | 91 Prot (grey) |
| Old Mutual Dynamic Floor | OM DF (grey) |
| Prudential Inflation Plus | Pru CPI+ (grey) |
| Sanlam Active | San Act (grey) |
| Sanlam Inflation Linked | San CPI+ (grey) |
| **Smooth bonus portfolios** | |
| Old Mutual AGP Stable | OM Stable (grey) |
| Sanlam Absolute Return Plus | San ARP (grey) |
| **Market related portfolios** | |
| Allan Gray Balanced | A Gr (blue) |
| Hangala Prescient Absolute Balanced | Hangala (blue) |
| NinetyOne Managed | 91 (blue) |
| Investment Solutions Bal Growth (multimanager) | Isol FG (blue) |
| Momentum Namibia Growth | Mom NG (blue) |
| NAM Coronation Balanced Plus | NAM (blue) |
| Old Mutual Pinnacle Profile Growth | OM Pi (blue) |
| Prudential Managed | Pru (blue) |
| Stanlib Managed | Stan (blue) |

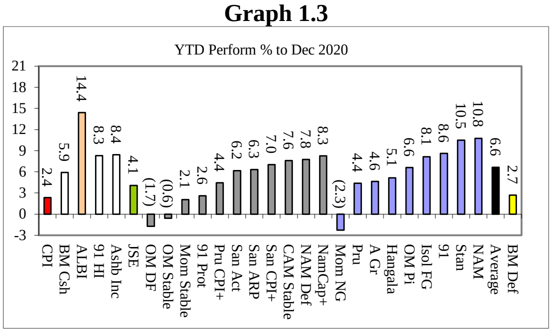
**Graph 1.1**



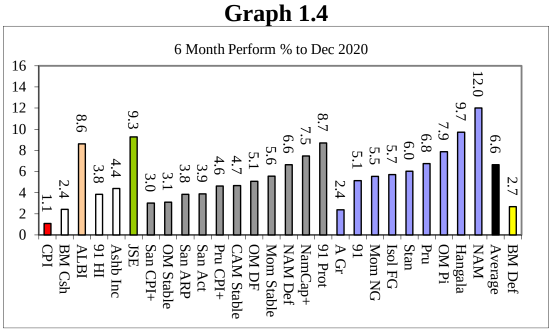

**Graph 1.2**




**Graph 1.3**




**Graph 1.4**



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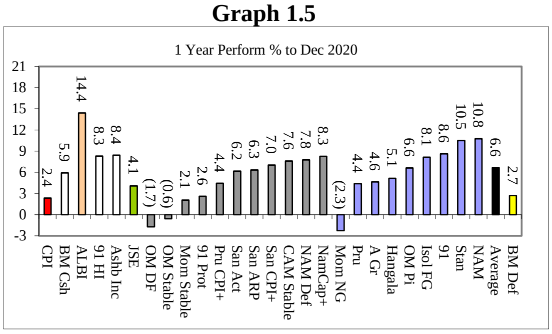
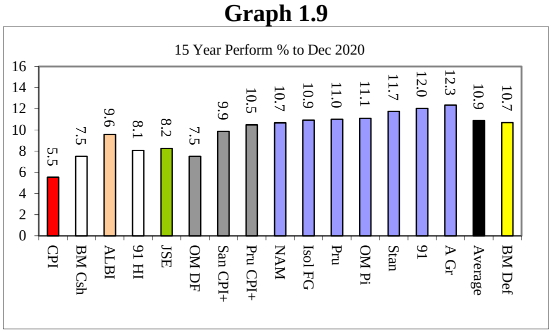
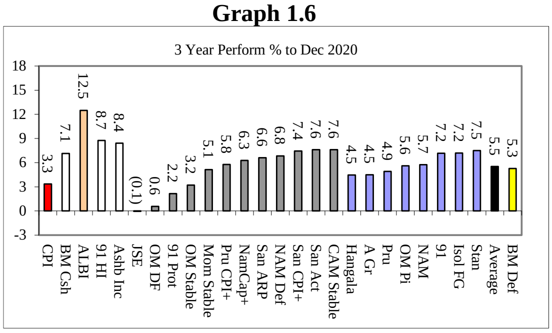
### Graph 1.5



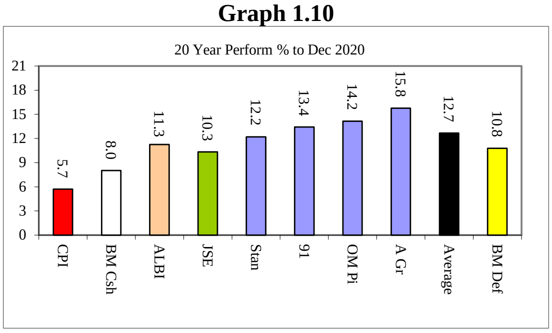

### Graph 1.9



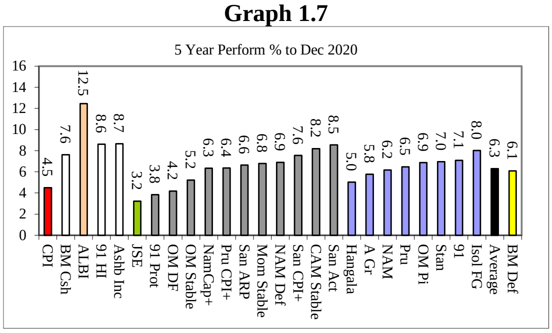

### Graph 1.6



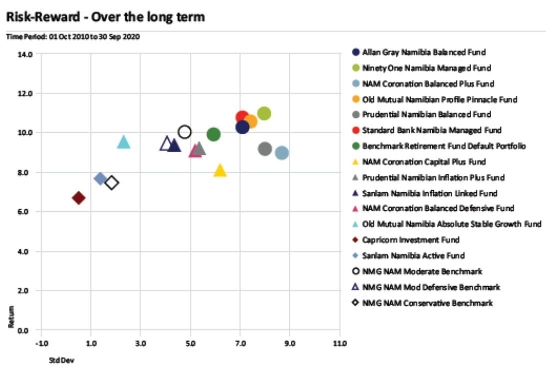

### Graph 1.10



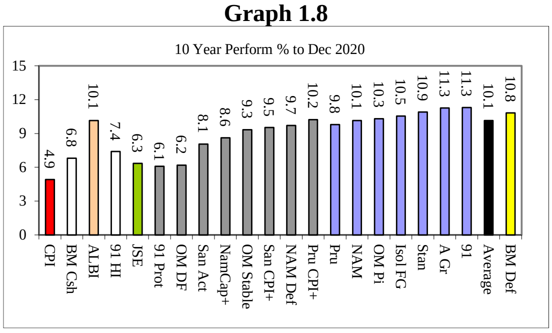

### Graph 1.7

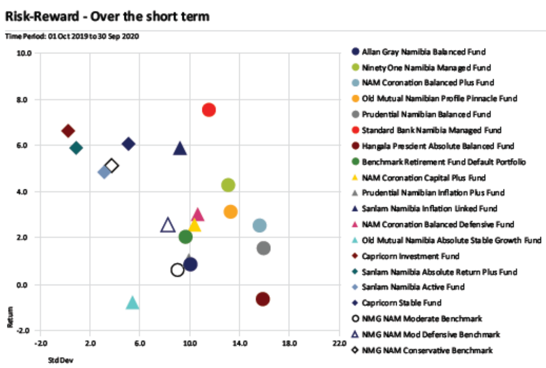



### Risk/ Return




### Graph 1.8



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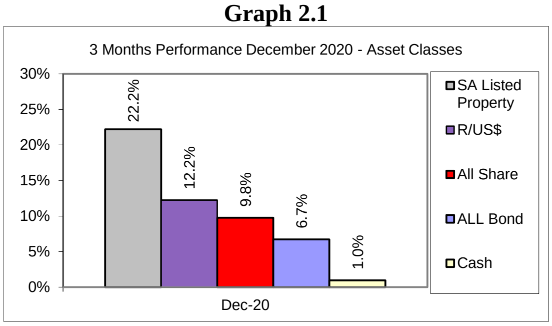
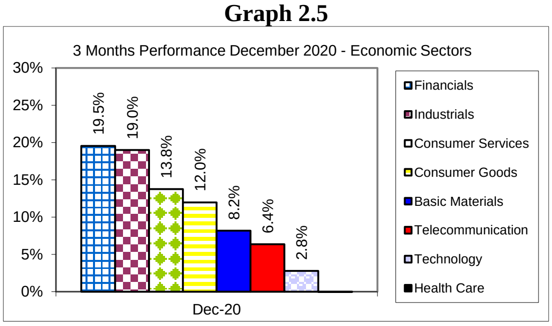
## 2. Performance of Key Indices (index performance by courtesy of IJG/Deutsche Securities)

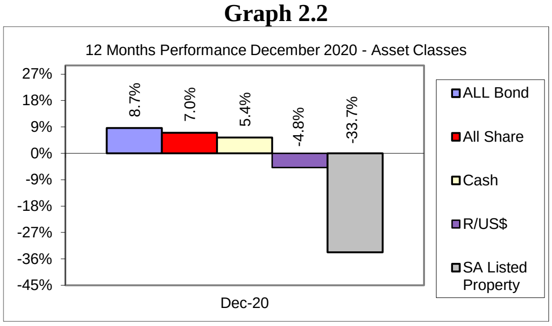
**Graph 2.1**



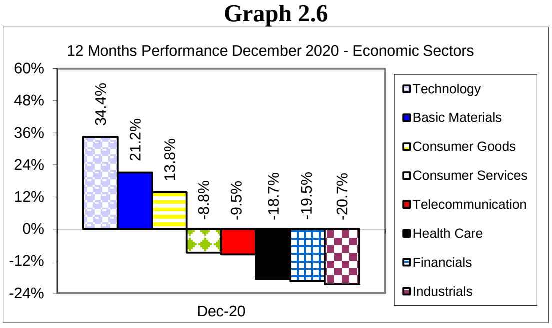

**Graph 2.5**



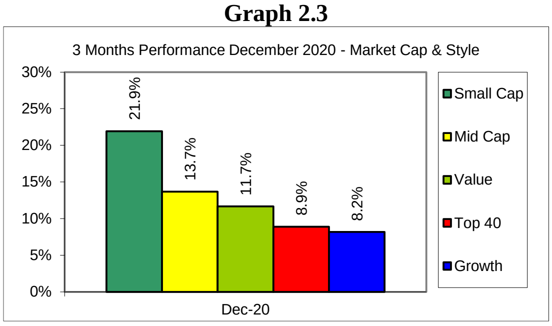

**Graph 2.2**



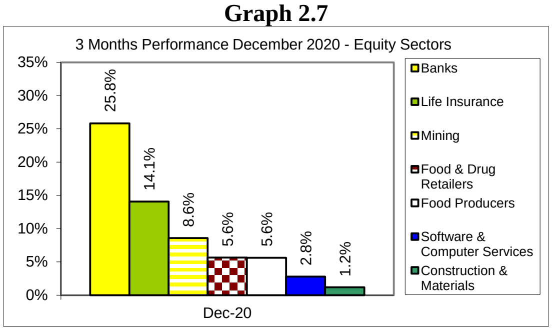

**Graph 2.6**



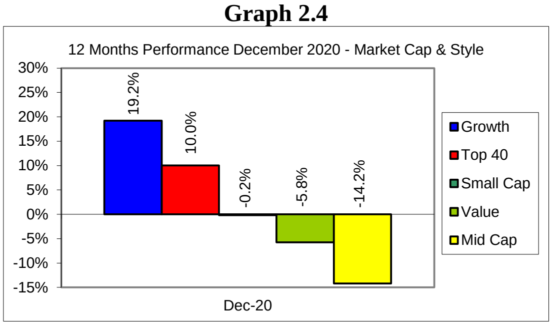

**Graph 2.3**



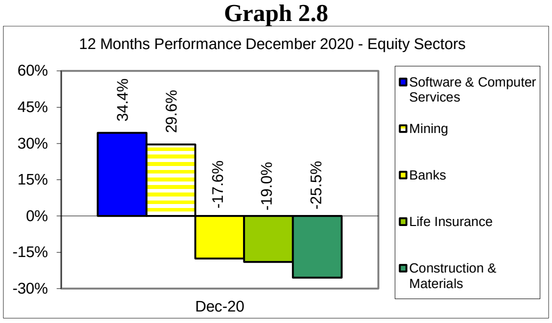

**Graph 2.7**




**Graph 2.4**




**Graph 2.8**



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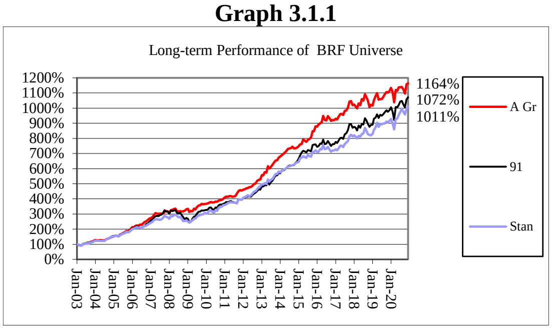
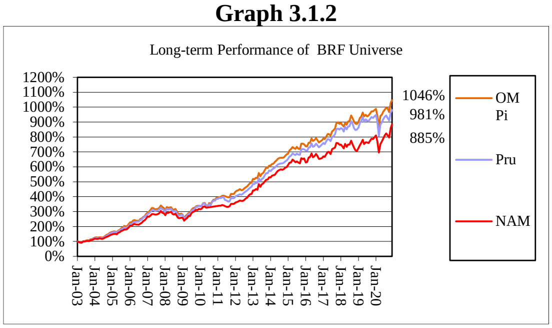
## 3. Portfolio Performance Analysis

### 3.1 Cumulative performance of prudential balanced portfolios

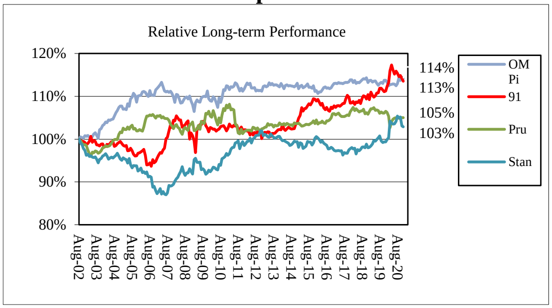
**Graph 3.1.1**



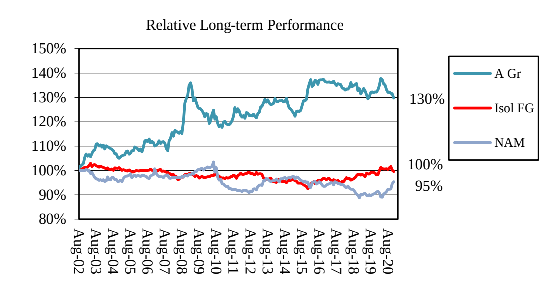

**Graph 3.1.2**



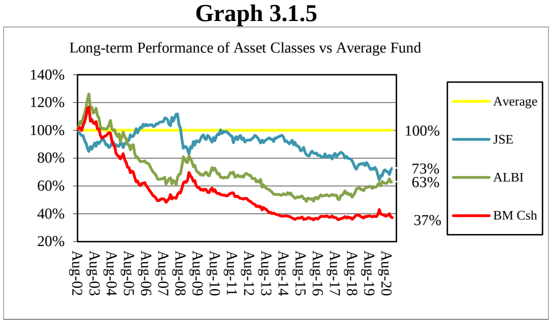

**Graph 3.1.3**




**Graph 3.1.4**

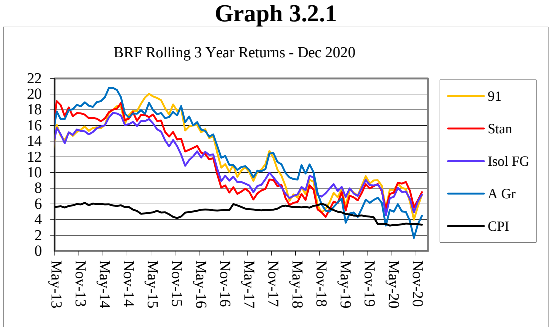



**Graph 3.1.5**

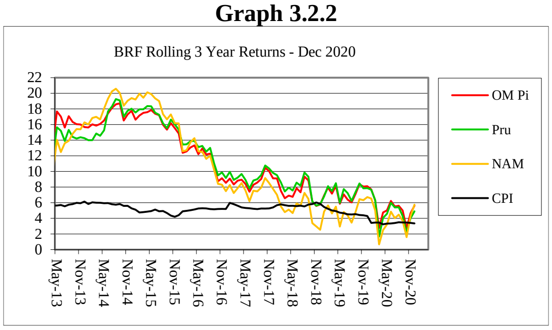



### 3.2 3-year rolling performance of prudential balanced portfolios relative to CPI

**Graph 3.2.1**

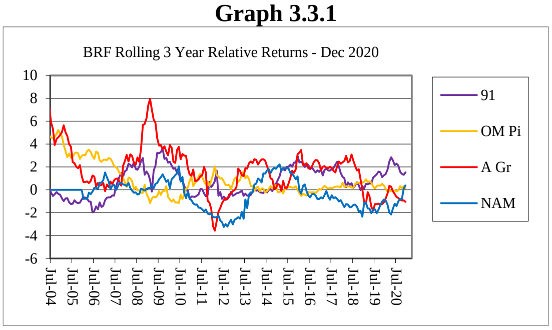



**Graph 3.2.2**




### 3.3 3-year rolling performance of prudential balanced portfolios relative to average prudential balanced portfolio on zero

**Graph 3.3.1**



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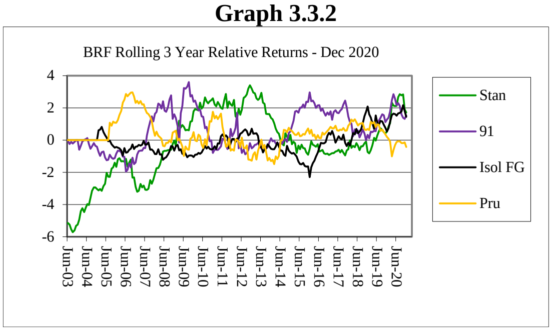
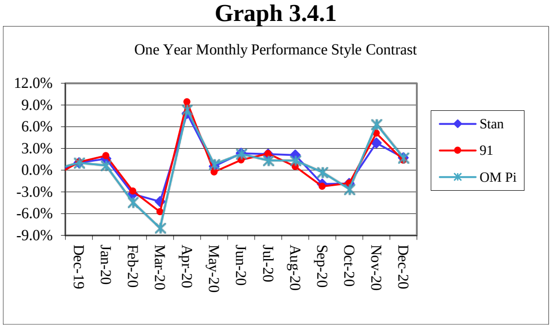
**Graph 3.3.2**

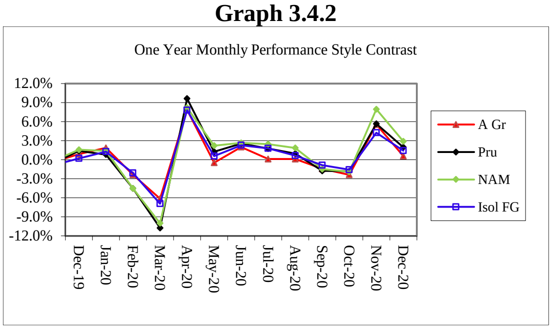



### 3.4 Monthly performance of prudential balanced portfolios

**Graph 3.4.1**

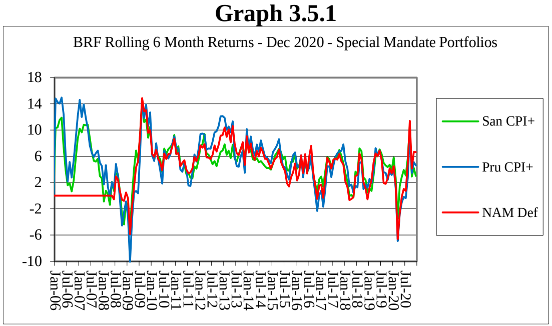



**Graph 3.4.2**

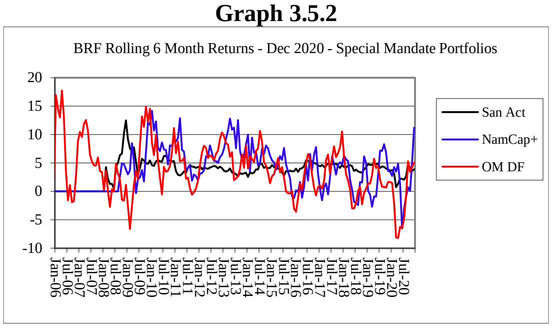



### 3.5. 6-month rolling and cumulative returns of 'special mandate' portfolios

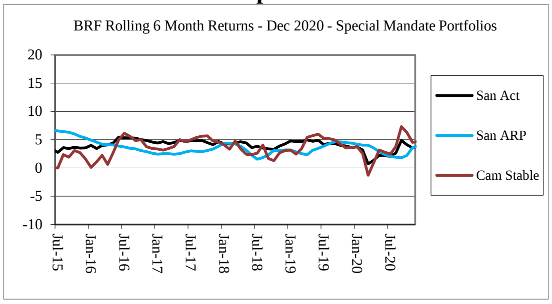
**Graph 3.5.1**



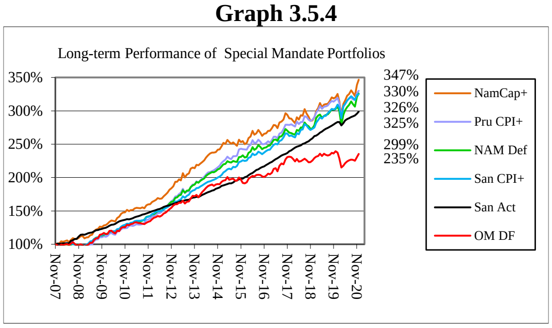

**Graph 3.5.2**




**Graph 3.5.3**

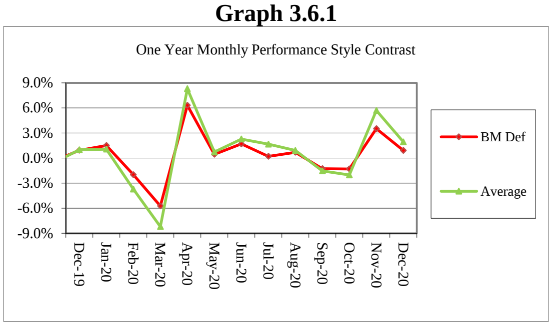



**Graph 3.5.4**




### 3.6 Monthly and cumulative performance of 'Benchmark Default' portfolio relative to average prudential balanced portfolio

**Graph 3.6.1**



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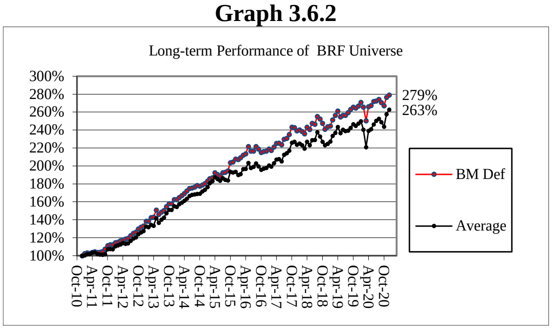
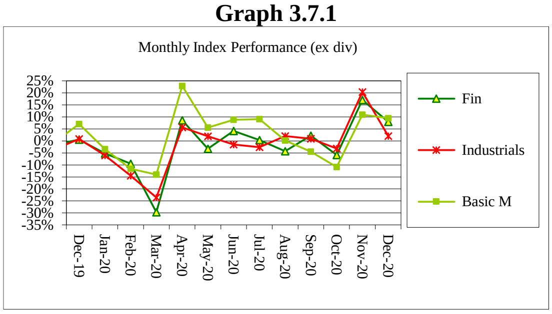
**Graph 3.6.2**

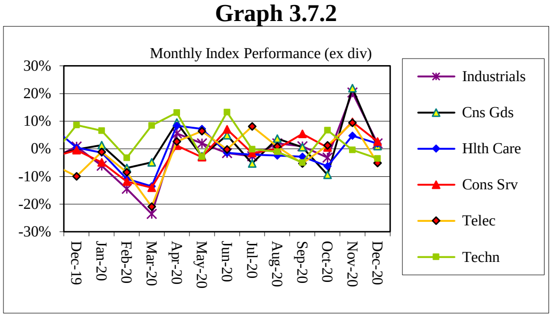



### 3.7 One-year monthly performance of key indices (excluding dividends)

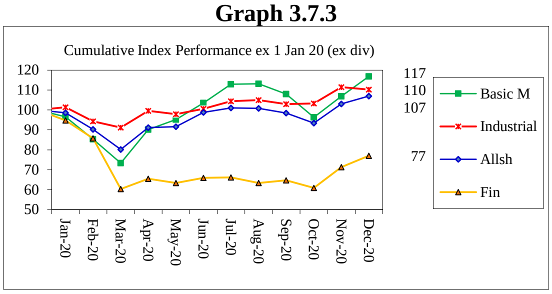
**Graph 3.7.1**



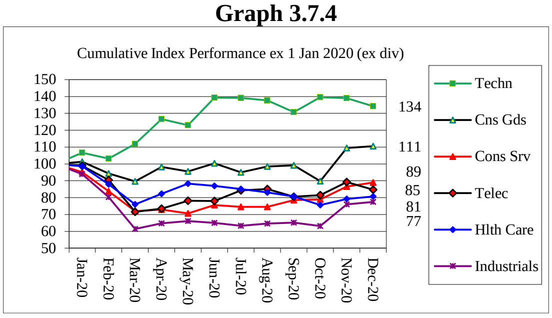

**Graph 3.7.2**




**Graph 3.7.3**




**Graph 3.7.4**




## 4. The Benchmark Default Portfolio – Facts in figures

**Table 4.1**

| Portfolio | Default portfolio | Average Prud Bal |
|---|---|---|
| 5-year nominal return - % p.a. | 6.1 | 6.3 |
| 5-year real return - % p.a. | 1.6 | 1.8 |
| Equity exposure - % of portfolio (qtr end September 2020) | 45.1 | 63.3 |
| Cumulative return ex Jan 2011 | 179.2 | 162.8 |
| 5-year gross real return target - % p.a. | 5 | 6 |
| Target income replacement ratio p.a. - % of income per year of membership | 2 | 2.4 |
| Required net retirement contribution - % of salary | 13.0 | 11.6 |

The above table reflects the actual returns of the Default Portfolio versus target returns required to produce an income replacement ratio of 2% of salary per year of fund membership that should secure a comfortable retirement income. It is to be noted that the default portfolio of late under-performed the average prudential balanced portfolio, although still ahead since January 2011, when it was restructured to its present structure. This is the result of its significantly more conservative structure with an equity exposure of only 45% compared to the average prudential balanced portfolio's exposure of 63%. When equities significantly out-perform the other main asset classes, the default portfolio will under-perform the average prudential balanced portfolio. Over the past 6 months and as the result of the further significant increase in central banks' bond buying activities, equities have indeed outperformed the other asset classes significantly. This intervention of course distorts financial markets and causes significant volatility and artificially increased valuations of equities, in particular.

The default portfolio's long-term return must be read in the context of it initially having been managed with a low risk profile that was only changed from the beginning of 2011 when the Metropolitan Absolute Return fund was replaced with the Allan Gray balanced portfolio.

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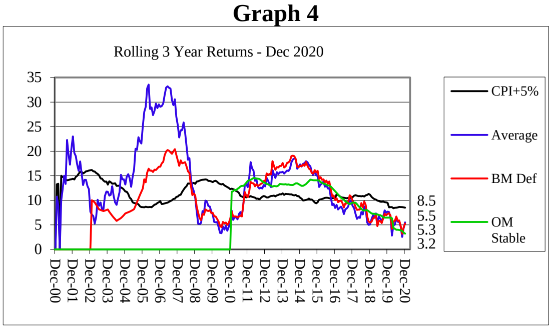
**Table 4.2**

| Measure | Money Market | Default Portf | Average Prud Bal |
|---|---|---|---|
| Worst annual performance | 7.2% | 3.1% | 2.5% |
| Best annual performance | 8.2% | 9.8% | 8.8% |
| No of negative 1-year periods | n/a | 0 | 0 |
| Average of negative 1-year periods | n/a | n/a | n/a |
| Average of positive 1-year periods | 8.0% | 6.6% | 6.2% |

The table above presents one-year performance statistics. It highlights the performance differences between the 3 portfolios over the 3 years January 2017 to December 2020. This gives an indication of volatility of the performance of these 3 risk profiles.

**Graph 4**

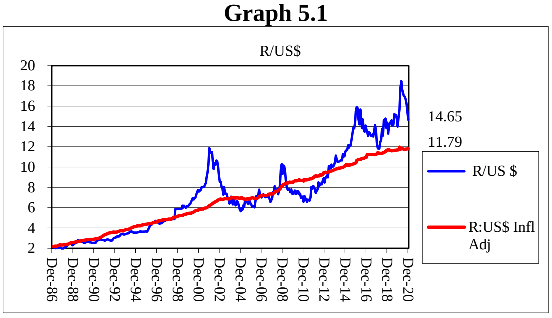



**Graph 4** measures the success of the Benchmark Default portfolio in achieving its long-term gross investment return objective of inflation plus 5%, on a rolling 3-year basis. It also shows rolling 3-year returns of the average prudential balanced portfolio and rolling 3-year CPI. The Benchmark default portfolio 3-year return to end December was 5.3%, the average was 5.5% vs CPI plus 5% currently on 8.5%.

### 5. Review of Foreign Portfolio Flows and the Rand How is the Rand doing?

**Graph 5.1** indicates that the Rand by our measure is at fair value at 11.79 to the US Dollar while it actually stood at 14.65 at the end of December. Our measure is based on adjusting the two currencies by the respective domestic inflation rates.

**Graph 5.1**

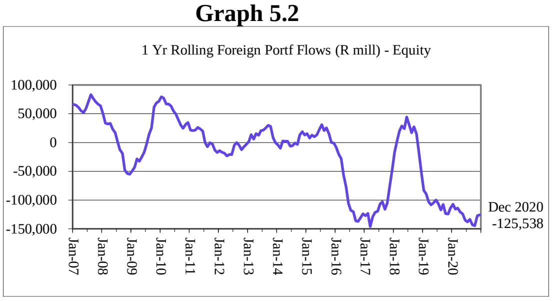



The Rand strengthened by 5.04% in December with net foreign investment inflows into bonds and equities of R16.2 bn. Over the past 12 months the Rand weakened by 4.84%. Net outflows of foreign capital from equity and fixed interest securities over the past 12 months amounted to R 173.8 bn (outflow of R 184.7 bn to end of November 2020).

Since the beginning of 2006, total net foreign portfolio outflows amounted to R 86.90 bn (November R 103.1 bn outflows).

**Graph 5.2** reflects a net outflow of capital from South African equities on a rolling one-year basis, of R 125.5 bn at the end of December (outflow of R 127.4 bn year-on-year to end November). The month of December experienced a net outflow of R 0.1 bn. Since the beginning of 2006, foreign net investment outflows from equities amounts to R 283.6 bn (end November net investment outflow of 283.5 bn). This represents roughly 1.6% of the market capitalization of the JSE.

**Graph 5.2**




**Graph 5.3** on a rolling one-year basis reflects foreign portfolio outflows in respect of SA bonds of R 48.3 bn over the past 12 months to end of December (outflow of 57.3 bn over the 12 months to end of November). The month of December experienced a net inflow of R 16.3 bn. Since the beginning of 2006, foreign net investment in bonds amounts to R 196.7bn (to November R 180.4 bn).

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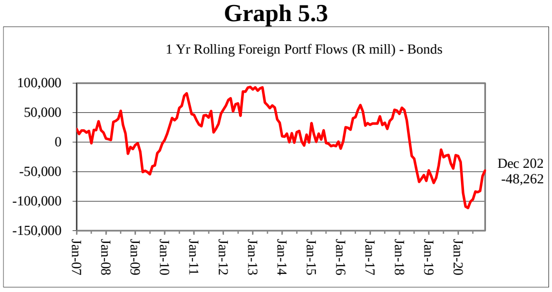
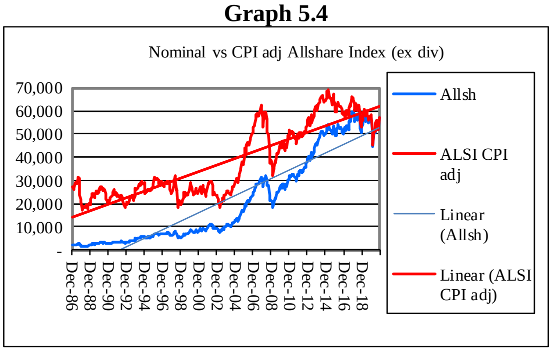
**Graph 5.3**



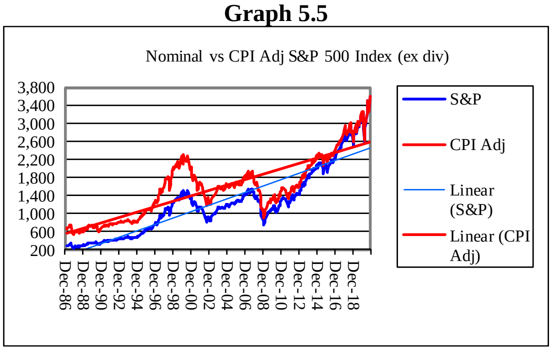

**Graphs 5.4** reflects the movement of the JSE since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. In nominal terms, the JSE grew by 10.5% per year since January 1987, and this excludes dividends of 3.1%. Namibian inflation over this period of 33 years was 7.8% per year. This is equivalent to a growth in real terms of 2.7% p.a. over this period, excluding dividends, or around 5.8% including dividends.

**Graph 5.4**



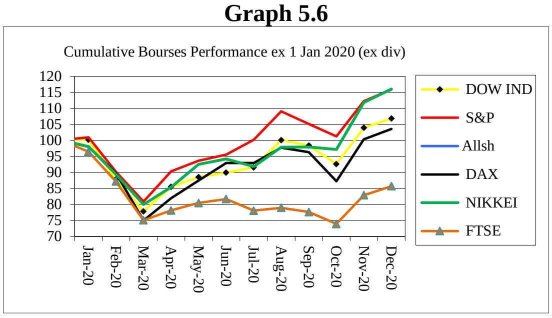

**Graph 5.5** reflects the movement of the S&P500 Index since January 1987 in nominal and in inflation adjusted terms, with trend lines for these. Since January 1987 the S&P500 Index has grown by 8.0% per annum, over this period of 33 years. US inflation over this period was 2.5%. This is equivalent to a growth in real terms of 5.5% p.a. over this period, excluding dividends or around 7.7% including dividends.

**Graph 5.5**



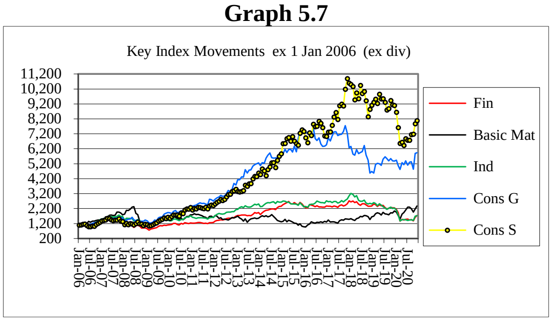

**Graph 5.6** provides an interesting overview of some of the major global share indices, showing up the S&P as the top performing index since the start of 2020.

**Graph 5.6**




**Graph 5.7** provides an overview of relative movement of the key equity sectors on the FTSE/JSE since December 2005 when these indices were first introduced. From this the investor should be able to deduce which sectors offer greater value and which one's offer less value on the basis of fundamentals. Annualised returns for these indices since the beginning of 2006 were: Consumer Services: 14.9%; Consumer Goods: 12.5%; Basic Materials: 5.9%; Industrials: 3.7% and Financials: 3.7%.

**Graph 5.7**




## 6. The 2020s are going to be about rifle shots, not the shotgun approach of index funds!

By Tilman Friedrich

In his newsletter 'Thoughts from the Frontline' of 23 January 2021, John Mauldin presents a number of US market metrics that should make an investor think.

Consider the so-called 'Buffet Indicator' as per **graph 6.1** (Source: Adviser Perspectives), that measures US equities as a percentage of nominal US GDP. It is at an all-time high and about as far above the 'Eponential Regression' line as it was at the end of 2000 when the S&P 500 dropped from its peak of 1,518 at the end of July 2000 to 815 by end of August 2002. That was a drop of 87%! It took the S&P 500 5 years to get back to the July 2000 level, i.e. by 2007, only to drop back to 735 at the end of January 2009 through the global financial crisis. That was a drop of 108% from the peak it reached at the end of April 2007. As we speak, the S&P 500 is testing the 4,000 level, evidently driven by quantitative easing that we have referred to repeatedly in earlier newsletters.

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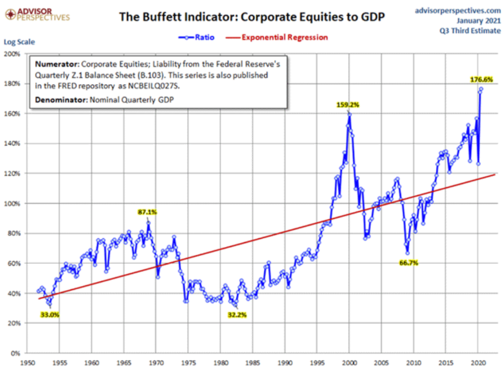
# Benchmark Retirement Fund

## MONTHLY REVIEW OF PORTFOLIO PERFORMANCE TO 31 DECEMBER 2020

By T H Friedrich – Retirement Fund Solutions Namibia (Pty) Ltd

The monthly review of portfolio performance, as set out in this issue, is also available on our website at www.rfsol.com.na.

**Graph 6.1**




Similarly **graph 6.2** (Source: Doug Kass) reflects a list of 15 S&P 500 metrics that are at historical highs of somewhere in the 90th to 100th percentile.

**Graph 6.2**

S&P 500 Valuations

| Model Factors | Most Recent Value | Historical Percentile |
|---|---|---|
| Median EV to Sales (Ex-Financials) | 4.0 | 100% |
| US Total Market Cap to GDP | 170% | 100% |
| EV to Free Cash Flow Margin-Adjusted (Ex-Financials) | 48.8 | 100% |
| Median Price to Sales | 2.8 | 100% |
| Median Price to Book | 3.9 | 100% |
| Median EV to EBITDA (Ex-Financials) | 15.0 | 100% |
| Aggregate EV To Sales | 3.0 | 100% |
| Aggregate EV to Trailing 12M EBITDA | 17.5 | 100% |
| Aggregate EV to 2021 EBITDA Estimate | 15.9 | 100% |
| Aggregate Price to 2021 Book Value Estimate | 3.8 | 100% |
| Aggregate Price to Tangible Book Value | 12.8 | 100% |
| Aggregate Price to Earnings | 27.9 | 98% |
| Cyclically Adjusted P/E (CAPE) | 32.9 | 97% |
| Aggregate Price to 2021 Earnings Estimate | 25.6 | 97% |
| Aggregate Price to Book | 3.9 | 91% |

Source: Bloomberg, Yale/Robert Shiller, John Hussman *Numbers as of November of 2020 ©2020 Crescat Capital LLC

The message clearly is that the US market is in extreme territory, or as John Mauldin put it 'valuations are at nosebleed levels' in the US. In last month's column, we had a table that presented a few key metrics of Europe, the UK, Japan and emerging markets (also covering the SA market), many of which similarly lead to the conclusion that all these markets are also not exactly cheap in historic context. Equities thus present a significant investment risk

Looking at other asset classes, treasury bills currently yield only around 4% which is not even 2% above inflation. Namibian government bonds in contrast, yield between just over 5% (GC21) and just over 13% (GC50). That may sound like a wonderful return on long-term bonds. The problem with bonds is that these yields can only be realised if one holds the bond to maturity and ignores the risk of capital loss in the event of a forced sale before maturity, should interest rates increase, as they should do, considering their extremely low levels currently. Just looking at current yields to maturity is about the same as saying, don't worry about the share price, let's just look at the dividend yield of a share. Very few investors, if any, can afford to hold an asset to maturity. There are always situations, e.g. retirement, unemployment or death of an individual, or the dissolution or liquidation of a fund or the employer, when one may be forced to sell the asset and the yield to maturity was then only a pie in the sky.

When we look at share indices, we need to realise that we are looking at a wood consisting of many different trees, some of which grow faster, others slower, some producing an exceptional crop, others a poor crop and some never make it at all. Last year the S&P 500 was up 18.4%, and an equally weighted portfolio of FAAAM (Facebook, Alphabet, Amazon, Apple, Microsoft) plus Netflix was up 55%! The contribution of that latter group to the S&P 500's growth was 14.35%. The "S&P 494", i.e. excluding these 6 out-performers, gained only 4.05%. By far the biggest investment risk is thus posed by those 6 shares while the balance of the index is probably at fair valuations. Currently 60 of the S&P 500 shares trade at over 10 times there annual sales compared to just under 50 just before the bubble burst in the early 2000's. Take Tesla that currently trades at 30 times annual sales. While the average tree in the wood grew nicely, there were a handful that delivered stellar growth, the rest delivering rather mediocre growth.

But even in a market that is generally expensive, there are always shares that are cheap, that are solid businesses generating great profits and paying high dividends. As John Mauldin put it in his 'Thoughts from the Frontline' newsletter of 23 January 2021: "The 2020s are going to be about rifle shots, not the shotgun approach of index funds." If one does not overpay for a good company, the company and its share price should grow in line with its sector in the economy and in addition, it will pay dividends. If you need to sell it, you should be able to sell it without having to incur a loss, having bought it at a fair or cheap price. Contrast this with property as another potential asset for investment. When the economy is in the doldrums, so the property market is and it will not matter what property you hold. The difference here is that shares are highly liquid and can be traded easily, making it much easier to realise the true value of the share, as opposed to owning property and being forced to sell it when the market is in the doldrums.

**Conclusion**

Considering the state of the global economy and financial markets, it is difficult to achieve the investment returns that are implicit in typical pension fund structures, of around 6% in real terms. This is the result of the disruption of financial markets by the intervention of reserve banks after the global financial crisis and now again in response to the COVID crisis. However, there is an end to what reserve banks can do and they are at this stage left with very little 'fire power' to stimulate the economy. Once inflation sets in with all the easy money floating around, interest rates will start increasing while equities as an asset class will start declining. Hiding your money under your mattress bears its own risks as does speculation with investments and the investment in less

Benchmark Retirement Fund

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common assets where it is difficult to determine a price because of the absence of an active market.

The good old fashioned investment principle still applies. Do not put all your eggs in one basket but diversify your risk by spreading it across assets and asset classes as widely as possible. Equities are a mirror of the real economy and remain the asset class that should generate superior returns in the long run. Economic fundamentals should improve as the COVID-19 hysteria subsides going forward. The time we find ourselves in, however, requires stock picking skills rather than the shot gun approach of index management and the focus should be on good quality, fairly valued or cheap companies with high dividend yields. The investor should thus be able to expect a real dividend yield in excess of 3%. This may be low in relation to what we have seen in years gone by, however it is still a respectable return on any equity investment. The investor should thus be able to expect a real dividend yield in excess of 3%. This may be low in relation to what we have seen in years gone by, however it is still a respectable return on any equity investment and an investment in a typical balanced portfolio should be able to generate a real return of around 5%, or around 7% in the prevailing inflationary environment. Offshore diversification is essential and the strengthening of the Rand once again creates the opportunity for doing so. It is this principle one needs to focus on more than the timing though, as the Rand tends to rise when offshore markets also rise, and vise-versa, often negating the effect of its strengthening or weakening.