Charles Merrington
Executive Financial Services (Pty) Ltd

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CMEFS WEEKLY INVESTMENT NEWS

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Hello and welcome to this week's edition of Investment News.

Before we go into this week's discussion, let's see how the CMEFS Flexible fund has done for the year thus far as compared to the All Share Index (ALSI)

Fund	Last week Thursday	This week Thursday
ALSI	-5.15%	-1.99%
CMEFS Flexible Fund	-0.43%	-0.32%

I would like you to take a close look at the table below, which was current as of last week.

10-Year Bond Yields			
	YIELD%	1D bps	1Y bps
Germany	-0,42	5	-21
United States	0,62	-2	....
South Africa (10-year)	**9,45**	**-5**	**141**

The table shows you the interest (Yield%) you would receive on your money if you loaned your money for 10 years to the German, United States, or South African Government.

Let's look at what the yield in Germany is telling us.

Before going into any sort of detail, bear in mind that in all instances, you are parting with your money for 10 years.

Also bear in mind that as a rule, the longer the period you are prepared to loan your money for, the greater the reward you would seek for the additional risk taken on.

For example, we all have a pretty good idea that tomorrow will closely resemble today, barring some unforeseen disaster.

We all kind of have a pretty good idea that next week will closely resemble this week, although not quite given the constancy of change, again barring some unforeseen disaster.

As for next month, well, one kind of has the hope that whatever change will take place will not be so radical that next month will be so very much different from this month.

Now when we talk of a year from now, we almost silently agree with ourselves not to make any rash predictions about how things will be a year from now, as a LOT can happen in a year.

If we now look five years into the future, well, that's another ball game entirely. There is just no way one can predict with any degree of accuracy what the world will look like then.

And finally, because we are talking about a 10-year loan, when we try and think 10 years into the future, well, don't even try.

What we have done here is step through the increased risk of not knowing what is going to happen with interest rates (and for that matter everything else) in the future.

Are interest rates going to go up, are they going to go down? Are they going to remain the same? And the further into the future we look, the greater the uncertainty, which is why we would want to be paid more interest when investing for 10 years than we would when investing for 1 year.

This dynamic would hold in any "normally" functioning economy, and if you look at the table below showing German Bond Yields over varying periods, you will see that you are punished less the longer you invest for. In fact, if you were prepared to lend your money to the German Government right now for 30 years, they would "only" take -0.03% of your money every year for the privilege of allowing you to do so.

Bund Yields

Name	**Coupon**	**Yield**
GTDEM2Y:GOV **Germany** Bund **2 Year Yield**	0.00	-0.70%
GTDEM5Y:GOV **Germany** Bund 5 **Year Yield**	0.00	-0.67%
GTDEM10Y:GOV **Germany** Bund 10 **Year Yield**	0.00	-0.47%
GTDEM30Y:GOV **Germany** Bund 30 **Year Yield**	0.00	-0.03%

As an aside, I note that 80 German Banks are now paying negative interest rates to their customers, most of them of the order of -0.5%

Although you are punished less (as opposed to rewarded more) the longer you invest, this is not indicative of a normally functioning economy by any stretch of the imagination.

So we have a “normal” but “abnormal” economic situation by way of the creation of negative interest rates.

In essence, people are being ***punished*** for saving and ***rewarded*** for spending.

Borrowed money in Germany right now only attracts around 1.8% pa in interest charges.

Another determinant of interest rates is the certainty of getting your original capital back.

The less certain, the higher the rate you would charge, the more certain the lower the rate you would charge.

Negative interest rates can only be charged where there is ***great*** certainty.

And this great certainty arises out of the fact that Germany posts trade surpluses year after year with its economy being responsible for 1/3 of the economic output of the European Union.

This is politically problematic for Germany and economically problematic for the other countries of the European Union.

This is because the value of the Euro factors in the weaknesses of all of the other economies of the European Union, which results in an unfair trade advantage to Germany in that it is trading out of a weaker currency than would otherwise be the case.

If Germany still had the Deutsche Mark, as it’s economy strengthened so too would the value of the Deutsche Mark, which would act as a counter-balance, making it less competitive price-wise thus giving other countries of the European Union a fighting chance to compete with it.

Little wonder then that, from a purely economic point of view, Germany will fight tooth and nail to keep the European Union intact. It’s really good for business!

Another determinant of interest rates is inflation.

Again as a rule, the higher the rate of inflation, the higher the interest rate earned, and visa versa.

In a normally functioning economy, the interest rate earned on savings should always be higher than the prevailing inflation rate for obvious reasons.

There is no reward to be had by investing at 2% or less when the prevailing inflation rate is 2%.

In the above scenario, you would either be earning 0% or less than 0% on your money.

Germany’s inflation rate right now is 1.18%.

A -0.42% yield against a current inflation rate of 1.18%, gives a net real return on investment of -1.6%pa

That is to say, if you were going to invest your money for 10 years in German Government Bonds right now, your R1 000 000 invested today would be worth R851 041 in 10 years' time – with “interest”!

And that is without drawing an income.

Now imagine that you are a pensioner and you are investing for income? Desperate times indeed!

Again just as an aside, if you are borrowing at 1.8% interest against an inflation rate of 1.18%, your actual cost of borrowing is 0.62% pa.

This is akin to giving money away.

And now we have Covid-19 thrown into the mix and the promise of yet more money printing to come from the European Union, amounting to €1 350 billion.

This will have the effect of holding interest rates down for even longer as the European Central Bank buys up debt with this newly printed money.

As can be seen, a similar dynamic is playing itself out in the US, and one can extend this to all of the developed nations of the world. In fact, there is a push going on right now for interest rates to go negative in the US too.

It seems these developed economies are getting themselves deeper and deeper into debt to keep the illusion of normalcy going for as long as they can, in the hopes (I believe) that “something” is going to happen “somehow”, “somewhere” in the future that will make the problem go away.

And this money that is being printed needs to find a home.

With yields being extremely low to negative in most of the developed world, pensioners and savers in the developed economies are becoming increasingly desperate to obtain some sort of yield on their money, which is why most of it is finding its way into already extremely over-valued stock-markets as well as into developing economies such as our own, where you can still get 9.45% pa on your money, despite the currency and sovereign risks this poses.

And it seems this situation will persist for as long as people think that the money that is being printed by central banks across the developed economies is worth what they say it is.

Be reminded that ***all*** currencies in circulation today are fiat currencies, and are what they are worth simply because we have “Faith in the Issuing Authority”

I trust you enjoyed the read.

Until next time then, do take good care of yourselves.

Kind regards, Nine, Charles, and all of us at CMEFS.