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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	-6.00%	-1.03%
CMEFS Flexible Fund	+0.96%	+1.23%

What to do, what to do?

Yes, the markets are volatile, and yes, today you are making a profit, and tomorrow you are making a loss. Or the other way around.

But with interest rates globally being at or near zero and in some instances below zero, as a retiree, or as a young person wanting to build retirement capital, just where do you put your money?

If you do not receive some sort of interest or capital growth (known as "yield" in the industry) on your capital invested, then as a retiree you start spending your capital on day one of your retirement, and we all know that longevity is the name of the game right now post-retirement.

So if you are likely to live to age ninety-five or even beyond, spending your capital from day one is not going to seem very appealing to you.

Similarly, if you are trying to build retirement capital and you receive zero yield on your capital invested, after bringing inflation to account, what is in fact happening is your savings are going backward in value from the first amount saved, as you will be receiving a negative return in real terms on your investment.

This is the dilemma facing almost every investor in the developed economies, and they are growing ever more desperate.

So desperate in fact that they are now willing to take on even greater and greater risk with their capital, in the hopes that when the music stops it is not they who will find themselves without a chair to sit on, but the ubiquitous "someone else."

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You might at this point ask what this has to do with our experience in SA as we can still get a fairly "decent" rate of return on money invested.

Well, if interest rates remain at these depressed levels in the developed economies for any continued length of time, much like the virus, we will soon find ourselves having to deal with the same problem they are having to deal with.

Just in case you did not notice, the average money market rate in SA in 2016 was 7.74%

In 2017 the average rose to 7.99%

In 2018 it dropped to 7.61%

In 2019 it rose back to 7.67%

The average for this year is now 5.93% with the current BEST rate offering 3.99%

Yes, the virus has had a direct influence on the current rate offered, but it is not only the influence of the virus we are battling with, it is also the influence of these depressed rates in these more developed economies.

And should "the Fed" start printing money again (virtually guaranteed under Biden), there will be a great incentive for international investors to adopt what is known in the industry as a "risk-on" approach.

When this happens, they start investing aggressively in developing economies such as ours in the hopes of picking up a few scraps of yield here and there, hoping all the while that the mousetrap won't close on them whilst they nibble at the cheese.

Right now the yields we are offering on some of our bonds are still sitting at a mouth-watering 7% or so.

Very, very tempting.

Consider this excerpt from a bit of research done recently by the Financial Times. (*My comments in italics*)

"The hunt for yield is getting harder for fixed income investors. Roughly 86% of the US$60 trillion global bond market, that's US$51.6 trillion, traded with yields no higher than 2%.

This is a record proportion, with 60% of these SAME investors earning LESS than 1% on capital invested.

Keep in mind that the bond market is not risk-free, although it is often touted as such.

Not only can you lose capital if interest rates go against you, but you can also lose capital should the bondholder default, sometimes some of it, sometimes all of it.

For example, right now you do not want to be holding Argentinian debt (Bonds)

Argentina owes a fortune - US$323 billion as of the end of 2019 — which it cannot pay back.

Incidentally, this amounts to 0.5% of the US$ 60 trillion total mentioned above.

The solution?

This is what was put on the table.

Roll the debt over with existing creditors but reducing the debt to 55 cents for every US$ owed – and investors are accepting this.

This is a loss of 45% for every US$ held. Ouch!

To recover from this loss, the investor would have to get 81% growth on the capital remaining to get back to their original US$1 they invested. Ouch indeed.

And now back to the excerpt.

This has pushed investors into riskier segments of the market in search of yield, compelling them to lend to lower quality companies and countries.

End of excerpt.

That last sentence is easy to read but needs to be re-read several times to fully absorb the import of what is being said here.

“Lending to lower quality companies” would include lending to companies that would have long ago been declared insolvent (zombie companies – the walking dead) were it not for the cheap money thrown directly at them by the Fed through providing the world’s largest asset manager Black Rock, with a mandate to do so.

This is not even nuts, it is completely insane. “Ga Ga” insane. And yet the people making these decisions are otherwise considered to be ‘rational” in that they are “preventing job losses”.

If you think otherwise than this then you are in complete agreement with Pravin Gordan in so far as throwing more money at SAA is concerned.

It is no different.

“Lending to lower quality countries” would include loans to Argentina and the like and, dare I say it following on from our sovereign risk rating downgrade by the various rating agencies, South Africa.

These continued low or no interest loans to these kinds of entities do much more harm than the simple loss of capital to the investors themselves (which is bad enough in and of itself) but it creates a very real disincentive to “get one’s house sorted out”, so to speak.

This applies equally to governments and businesses.

As long as the money keeps flowing, the parties can continue, and to hell with the hangover and the consequences that will inevitably follow.

This is precisely what has happened in Eskom's case as with most of our state-owned enterprises, and this phenomenon is NOT unique to SA.

It is becoming a global pandemic of its own.

No one wants to take the pain that will come along with "getting one's house sorted out" whilst at the same time no one wants to take the blame when it inevitably goes pear-shaped at some point in the future.

It is of course always someone else's fault.

It is the popular view that people, for example, have died en masse of the Coronavirus because the amorphous "government" has not done its job properly, as "it is the job of government to take care of all social ills", even when we do everything we can to make it impossible for them to do so.

For example for example. How many people have not yet downloaded the Covid-19 SA app onto their smart-phones whilst at the same time pointing a finger at the government saying they are "allowing people to die unnecessarily". Really?

I have just visited the play store and as of 15th October 2020, only 500 000 people had downloaded the app.

With SA's adult population sitting at somewhere around 43 million, this represents less than 1.16% of the total adult population.

Yes, many cannot afford smart-phones, but certainly, more than 1.16% of the total population can.

And maybe it is this same phenomenon playing itself out unconsciously in people's minds when it comes to the subject of money.

Should the proverbial hits the fan, the unconscious thought is don't worry, "the government" will come to the rescue, forgetting that 'the government" has no money of its own. It simply takes from Peter to pay Paul.

Let's hope Peter has very deep pockets, or that globally we start taking more responsibility for our own affairs than we currently seem to be.

I hope you enjoyed the read. Until next time then, do take good care of yourselves. Kind regards, Nine, Charles, and the rest of the team at CMEFS.