



THE POWER
OF INDEPENDENT ADVICE

IN THIS ISSUE

"As financial advisors our focus is on the importance of generating consistent and reliable returns under different market scenarios while 'protecting clients' investments from the downside, aligned to their respective risk profile."

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FOMO COULD LEAD TO BAD INVESTMENT DECISIONS

By Brian Butchart, CFP® and Managing Director of Brenthurst Wealth

Investors like to compare their portfolios with others and not just those of friends and family. No investors like to compare their portfolio performance to those who achieved the best possible returns. It is only natural and if you start looking at what you 'could've made' (even if it is that 1 in a 1,000 chance), the fear of missing out (FOMO) is a sly devil that could lead to bad investment decisions. It's not a new phenomenon, even if the term 'FOMO' only recently got popularised.

Let's take **smartphones** as an example. When **Apple** released its first iPhone in June 2007, the company's share price gained 37.20% in the following year. Investors knew that smartphones were the next big thing, but Apple wasn't the company everyone was chasing. No, that mantle belonged to Blackberry, which returned 75.36% over the same period, more than double Apple's performance. **Blackberry** made great smartphones and was dominating the market at one point, but there is a reason why investments carry a disclaimer of 'past performance is not necessarily an indicator of future performance'. From July 2008 to where we are now in 2021, Apple's share price gained an astonishing 2,383%. In comparison, Blackberry's share price is down 92%.

Chasing something that delivered a good return the previous year, may not provide the same fortune the next year. The same thing can be said about sectors, asset classes, and funds.

SECTORS RANK DIFFERENTLY IN PERFORMANCE EACH YEAR

The below table ranks the sector performance over each year. On closer inspection, you will often find a top performing sector in one year, fall down the rankings the very next year. To illustrate this, we followed Health Care's performance each year. If you stood at the start of 2016 and looked at the performance of Health Care in 2014 and 2015, you would've felt some FOMO if you missed out, but switching your portfolio to this sector would have had disastrous consequences as Health Care was the only sector to record a negative return in 2016.

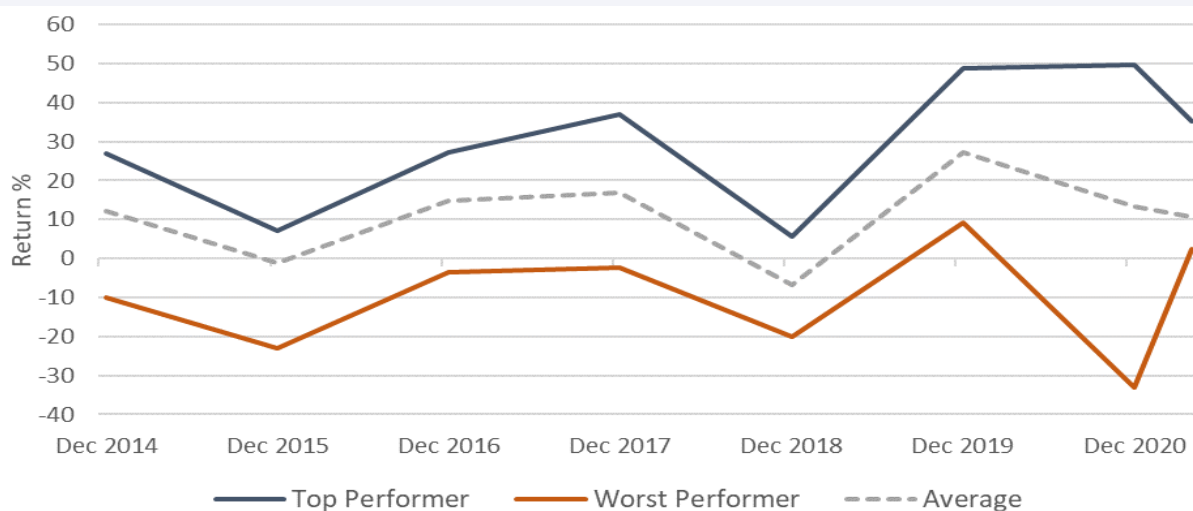
	2014	2015	2016	2017	2018	2019	2020	YTD	
Best ↓	26.94	7.07	27.11	36.83	5.53	48.93	49.53	35.32	Fidelity® MSCI Communication ServicesETF
	25.07	6.31	24.88	23.50	4.34	31.59	45.87	17.90	Fidelity® MSCI Consumer Discret ETF
	18.34	5.84	23.04	23.34	-0.37	30.62	28.35	11.90	Fidelity® MSCI Energy ETF
	15.82	4.98	21.06	22.96	-0.87	28.79	19.62	11.79	Fidelity® MSCI Health Care ETF
	0.00	3.30	20.53	22.21	-4.51	27.44	18.16	11.07	Fidelity® MSCI Industrials ETF
	14.01	0.00	17.13	19.98	-5.35	26.83	13.76	10.61	Fidelity® MSCI Materials ETF
	9.39	-0.73	13.92	12.71	-8.49	26.69	11.02	7.93	Fidelity® MSCI Financials ETF
	6.67	-3.63	7.86	12.51	-13.43	24.88	-0.67	3.63	Fidelity® MSCI Real Estate ETF
	6.34	-4.72	6.59	8.85	-13.84	23.35	-2.14	2.95	Fidelity® MSCI Consumer Staples ETF
	5.74	-9.95	5.65	3.65	-17.39	21.93	-4.87	2.64	Fidelity® MSCI Information Tech ETF
Worst	-9.89	-23.12	-3.41	-2.31	-19.98	9.07	-33.15	2.41	Fidelity® MSCI Utilities ETF

Source: Morningstar, Sharenet Investments

DIVERSIFICATION REDUCES RISK OF PICKING THE WORST PERFORMING SECTOR

Picking the top-performing sector each year is a super power yet to be discovered in any investor, no matter how good or legendary. Diversifying portfolios by allocating across sectors is the best strategy. The difference between the best and worst-performing sector in the market is usually around 30% and could even be as big as 83%, like we saw in 2020 (table below).

PERFORMANCE DISPERSION



Source: Morningstar, Sharenet Investments

LARGE RETURNS CONCENTRATED IN CERTAIN SECTORS FUEL FOMO

Investors who were not invested in global equities over the past few years and in particular, Mega Cap Technology and Biotechnology sectors, lost out on stellar growth and one of the fastest and strongest recoveries in market history, post the Covid-19 volatility of March last year. Technology, Communication Services, and Health Care led the recovery as lockdowns, unprecedented stimulus, dovish monetary policy, and historical low interest rates pushed valuations in these sectors to highs never experienced before. The staggering difference in returns is even more apparent when compared to other asset classes like bonds and property.

Investors often ask their wealth advisors about switching into growth-style sectors, like technology, as these have delivered superior returns compared to multi-asset funds and value-style stocks. I caution against making this comparison as these all serve as important components of a long-term portfolio, rather than stand-alone investments.

Investors must remember that bonds, property, and cash all serve a purpose when included alongside equity in a portfolio. In my experience, these asset classes hold up better than equity during times of economic crises, which happens to be the most likely time investors need to dip into their funds. Being forced to sell when the market is at a low must be avoided. Including value-style stocks within the equity portion of a portfolio adds another layer of protection in the event of a downturn and it is one factor that has started to play out in 2021.

A VALUE REVIVAL

Value stocks are recovering following years of underperformance that was magnified during the Covid-19 crash. This comes off the back of extremely high valuations in growth sectors, in part due to record low interest rates that investors no longer find palatable. **The top three best performing sectors in 2020 all find themselves in the bottom half in the first quarter of 2021. Active fund managers with a value bias benefitted from this.**

The sector rotation from growth into value has happened spectacularly fast. By March 2021, value regained the ground it lost during the pandemic.



Emerging markets should be the next focus point, currently offering substantial value relative to their developed market counterparts in the same sectors and hence the rotational swing to China and other emerging markets.

BEWARE OF CONCENTRATION RISK

The value style and multi-asset funds were never intended to necessarily beat growth-orientated funds. Instead, they offer diversification and serve a purpose in the construction of the overall portfolio to benefit from lower valuations and protect and preserve against risks when markets start gyrating, as they inevitably do. These funds offer alternative asset classes with the objective of beating money market and inflation and at the same time preserving capital.

As financial advisors, our focus is on the importance of generating consistent and reliable returns under different market scenarios while protecting clients' investments from the downside, aligned to their respective risk profile. Right now, rising inflation poses a risk to central banks, which may prompt interest rate hikes. Should this risk materialise, we should see equity valuations pull back as rates go higher and that is when a flexible fund or equity with a value bias becomes a welcome sight for the investor.

For more than 10 years now, Brenthurst has constructed multi-themed international portfolios for clients across multiple unit trust funds and solutions, successfully incorporating the above philosophy and delivering stellar performance to clients.

More recently, **Brenthurst partnered with Sharenet Investments** to construct personal share portfolios both internationally and locally, making use of investment tools like sector diversification to spread the risk across personal share portfolios and improve long-term objectives. It is also important to keep a finger on the pulse of growing industries like eSports, 5G, and renewable energy. We identify these trends and analyse thousands of stocks and ETFs, resulting in a low-cost portfolio that manages the risk while also giving our clients exposure to high growth sectors and geographic regions with access to a world class Trading Platform to monitor in real-time.

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2021 CHECKLIST FOR THE SMART INVESTOR

- ✓ There are going to be headwinds, new Covid-19 'waves', potentially higher yields, a buoyant US dollar, and heaps of uncertainty. These are all ingredients for a potentially bumpy ride in the markets.
- ✓ Volatility is the price you pay for participating in the returns so do not exit the market after a large correction – it is normal market behaviour.
- ✓ Understand what risk tolerance is and how this applies to you. Everybody wants a 30% (or higher) return; few can stomach a 30% decline in portfolio values.
- ✓ Diversification, sometimes referred to as the 'only free lunch' in investments, is an integral factor in the construction of an investment portfolio.
- ✓ Take the time to set personal investment goals and objectives suited to individual needs. No person's requirements are exactly the same as that of another.
- ✓ Failing to plan, is planning to fail... Stick to your financial plan. Historical returns are no guarantee for future success.
- ✓ Be clear on the investment's objective. Is it for retirement, leaving a legacy, protecting the future financial security and money requirements of children or a spouse/partner, or perhaps for an entrepreneurial venture sometime in years ahead?
- ✓ Investing is one component of an overall financial plan. A comprehensive plan also covers estate planning (always have a will that is up to date with current personal circumstances), risk planning, and tax efficiency.

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