



THE POWER
OF INDEPENDENT ADVICE

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“ *Choosing the most appropriate asset mix for your investment is critical: too much risk and you’re vulnerable to volatility and losing money; too little risk could result in lost gains.* ”

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FACTS & FALLACIES OF INVESTMENT

By Sonia du Plessis, Certified Financial Planner®, Brenthurst Wealth Management

We have all been there, it is a Saturday afternoon and the fire is lit. You are standing around the braai chatting with your friends and one of them pipes up with “You need to get in on this fund. I am getting 20% returns; don’t waste your time with your provider”. Sound familiar? Well, as a financial advisor, I must stress that moving to the fund with 20% returns, based on a conversation you had around a braai, is one of the most dangerous things you can do.

Investments are very tricky to get right and when you do get it right, it is often not that way for long. The process around selecting the right investment is a critical component in the long-term success of an investment.

An investment return does not happen overnight. One of the most important considerations is something called the investment horizon: essentially how long you need to hold an investment for.

Risk is good for high returns, but only in the long term. In the short term, risk can be very dangerous because it is volatile. A long investment horizon allows for the compounding effect to really take effect.

For example, if you were to invest R100 every year for ten years, and each year your return was 10%, after year one you would have R110. After year two you would have R231, and so on. By the end of ten years you would have R1753. Now, if you took that R100 payment and each year took the 10% return as cash, you would have effectively received R1100 (10 x R110).

The difference of R653 is due to the compounding nature of the investment. By keeping your money invested you are not getting a 10% return on the R100 you are investing – you are getting a 10% return on all the money you have in the investment.

Asset managers refer to ‘timing the market’ versus ‘time in the market’. What this means is that it is almost impossible to tell when exactly the markets will rally and when is the optimal time to invest, so in order to give yourself the best opportunity you should make sure you are invested before the rally. This is termed ‘time in the market’.

One of the most important decisions to make when choosing what investment is most appropriate is asset allocation. The main asset classes are equities, property, bonds, and cash. The highest risk is normally equities and the lowest risk is cash. Risk and return are linked, over time. The fund with the highest risk will have potentially the highest potential return.

It is not reasonable to expect a cash investment to provide you a return on 15%, while at the same time it is not reasonable to expect an equities investment to have no volatility.

When you take out an investment, there are three entities that charge fees: the asset manager, the administrator and the financial advisor. Altogether these fees are known as the effective annual cost (EAC). Depending on the type of investment and the amount being invested, the EAC can be anywhere from 1.5% to 5%. There are certain circumstances when the EAC could be outside that range, but as a financial advisor, an EAC of between 2% and 3% is normally appropriate. If your EAC is greater than 3% that is not say you are being ripped off, it might just mean that your investment requires a more hands-on approach and consequently the asset manager is charging more.

Investing offshore has a romance about it – it makes one sound like a savvy investor. The merits of investing offshore versus investing locally makes for a lively debate.

When people are looking to invest money offshore they are more often than not looking to protect their capital. For example, investing in a German bond is perceived to be a much safer investment than a start up on the JSE.

South Africa is a developing country with a liquid currency. This means that asset managers in New York, Zurich, or London will invest in South Africa and divest too, based on the mandate of their funds. If the mandate says that 10% of their assets must be invested in emerging markets, then the asset manager will find the best available emerging market asset to invest in.

Making money through investments is an exercise you need to go through with a qualified financial advisor. Ask questions, but also understand that investing is not an exact science.

However, there are some concepts that you should keep in mind. The investment horizon is very important: a longer horizon allows for more time to generate a greater return and thus allows for investing in riskier asset classes.

Staying invested for the entire investment horizon also opens up the potential for compound interest to work in your favour. Choosing the most appropriate asset mix for your investment is critical: too much risk and you open yourself up to volatility and losing money, but too little risk could result in lost gains. Evaluating the fees being charged and questioning your financial advisor if your EAC is above 3% is a conversation you should be having.

Your investment needs to be suited to your specific needs, and what your risk appetite is. Do not chop and change your investments based on what a friend says around a braai. Rather get a financial advisor to investigate options best suited to your needs and give you a professional opinion.

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INTRODUCING: SONIA DU PLESSIS, CERTIFIED FINANCIAL PLANNER®



SONIA heads up the Stellenbosch office. She has been in the financial services industry since 2001. She previously worked for Magnus Heystek International as well as Absa Private Bank where she gained valuable experience in investment and life insurance matters.

She obtained a B.Com degree in 2001 from the University of the Free State and was awarded the CERTIFIED FINANCIAL PLANNER® designation in 2004.

Sonia is a CERTIFIED FINANCIAL PLANNER® professional, a member of the Financial Planning Institute of South Africa and is fully qualified to give advice on all investment matters.

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