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IN THIS ISSUE

Any spare cash should be used to create an offshore share portfolio, starting with the R1m annual investment allowance, which is the quickest and easiest way to externalize some capital from South Africa.

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THE FINANCIAL TSUNAMI HAS HIT

By Magnus Heystek, Investment Strategist and Director at Brenthurst Wealth

Ernest Hemingway's famous passage in his novella "The Sun Also Rises," "How did you get poor? Slowly at first and then suddenly," has become the most over-used quote to describe the situation in South Africa over the last couple of years. I even used it in one of my first articles many years ago, warning about the approaching financial calamity for almost everyone in SA.

I first read the book at university many years ago, but since then, my copy has probably ended up in a landfill or a second-hand bookshop, courtesy of a divorce or two in the interim years. A few months ago, I asked for a fresh copy of the book as a birthday gift and spent a recent afternoon, recovering from a total hip transplant, slowly reading it again, along with a number of other Hemingway books I received at the same time. And yes, the passage is very apt, describing the declining fortunes of one of the characters in the book in almost throw-away lines of writing.

After years of slowly becoming poorer as a country, we have now entered the "suddenly" phase. Everything is happening almost at once, and the outlook is unlikely to turn out well if we continue on the current trajectory under the leadership of the ANC. We haven't hit bottom yet…

SLOWLY, SLOWLY AT FIRST…

For years now, nearly every South African—almost EVERYONE, except the 1%-ers—has been experiencing a gradual decline in wealth, year after year, since around 2013.

THE SIGN-POSTS TO THE CURRENT COLLAPSE OF MIDDLE AND UPPER-CLASS WEALTH ARE AS FOLLOWS:

1. **Gross Domestic Growth per capita has been below 2% per annum, one of the slowest rates in the emerging world since about 2011.** Considering a population growing at more than 2% per annum over the same period, this has led to a decline in total wealth.

2. **SA's global credit rating started its downward spiral, from investment grade to its current level of junk status, at around the same time.** As a consequence, a lot of capital has flowed out of the country—slowly at first, but in recent years, it has turned into a torrent. This has impacted the growth in our capital and equity markets.

3. **The currency has been on a slow descending trend, declining by about 6% per annum against major currencies. However, over the past year, the ZAR has dropped from R14.40 in April last year to current levels around R19 to the USD.**

4. **The impact on local purchasing power of such a decline in the currency is often understated and overlooked. We live in a dollar-denominated world, and everything from grain (for the poor) to air class tickets, global holidays, and motor cars (for the middle-class rich) is priced in US dollars. The currency shock alone has pushed a lot of people into middle-class poverty. The price of new motor cars has become unaffordable for most but the rich.**

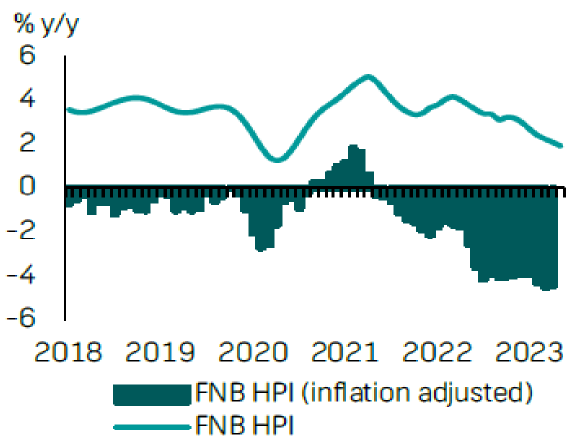
5. **Property prices—residential and commercial—have been a total disaster. Listed commercial property has shown no growth in 10 years, and over 5 years, it has lost you between 30-60% of its value**. Many, if not most, pension funds still stick to a 2-5% exposure to listed commercial properties, in many instances to protect their initial investment.

6. **SA's repo rate and hence prime overdraft rates have risen sharply as a result of the upsurge in global and local inflation.** This is having a major impact on the cash flow of the middle and upper middle class.

7. **The latest FNB Property barometer shows just how hard the middle to upper end of the residential property market has been hit**. In short, it has been a financial calamity, yet the media is too shy to ventilate this issue. The top end of the property market has bombed out, and real values have declined by between 10 and 30% over the past 5 years and more.

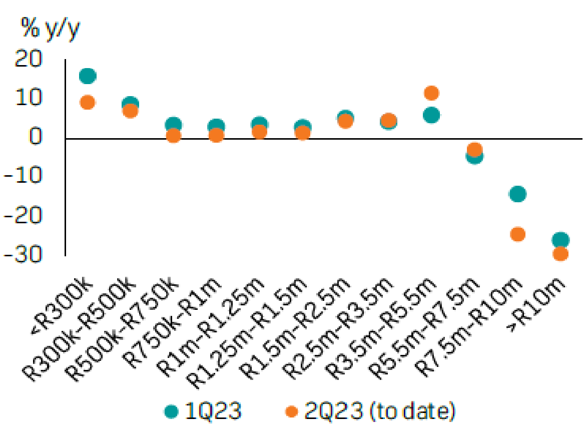
ANATOMY OF A PROPERTY PRICE COLLAPSE

Figure 1: FNB HPI



Source: FNB Economics

Figure 2: Price growth by price brackets



Source: SARB, FNB Economics

Top-end properties have experienced a substantial decline of about 20-30% in real value over the past 5 years, and selling them now takes almost 4 months, if at all. For numerous middle-class property owners nearing retirement, their once-sprawling mansions have turned into a capital trap, especially as municipalities impose ever-increasing taxes. I know this firsthand because I am one of those affected.

Surprisingly, the media provides little coverage of this ongoing bloodbath—yes, dear reader, it is indeed a bloodbath—whether due to design or shock at the unfolding situation. The only glimmer of hope can be found in the Western Cape, where a flood of people has driven prices well above national levels. However, when we remove the Western Cape effect, the overall picture becomes even more distressing.

In countless small to medium towns, there is virtually no effective residential property market left. The financial anarchy reigning in these areas has completely decimated any remaining property values. Several years ago, I advised a family from Bloemfontein to sell their local property portfolio, which they did, and wisely invested the proceeds offshore. Consequently, their offshore capital has doubled in value, while the property portfolio has suffered a loss of over 50% of its initial worth. Such decisions can significantly influence family fortunes, either protecting or jeopardizing them.

Over the past 10 years, SA's pension funds have largely failed to outperform the inflation rate. I have written numerous articles highlighting the poor performance of traditional retirement products. Since 2011, local pension funds were constrained by the rigid Reg28 regulations, contributing to their underperformance, in my opinion. To make matters worse, SA's placement on the so-called "Grey list" has dealt another blow, with capital slowly flowing out of the country while fresh investments remain scarce.

FINANCIAL TSUNAMI HAS HIT OUR SHORES

I have been closely monitoring these "wealth" indicators since around 2012/2013, and I began writing about them in 2014. These articles, however, didn't sit well with a sizeable and well-paid group of optimistic economists who made vigorous attempts to discredit my findings. Each time I published an article, it was met with several others aiming to refute my arguments. In short, my perspectives were considered nonsense, and the prevailing sentiment was that all was well with the Good Ship SA. Fortunately, the late Mike Schussler became my reliable source to verify my statistics, and he wholeheartedly agreed with my observations. He even provided me with additional facts that supported my contention of a slow-rolling avalanche heading down the mountain.

Even as recently as last year in July, we received confident reassurances from several economists—such as Johan Els from Old Mutual and JP Landman—that all was well, and a new era of growth had commenced. Old Mutual was optimistic about achieving a growth rate of 2.5% and possibly more in 2023.

However, the bad news is that major financial institutions like the IMF, World Bank, SA Reserve Bank, and other banks do not foresee any growth this year, indicating a possible marginal uplift of around 0.1% growth.

One may wonder how prominent financial institutions like OM can get their forecasts so wrong. To me, it seems apparent that they are grasping at any vaguely positive economic statistic to portray an imminent upturn.

Recently, numerous updates on this financial collapse surfaced almost simultaneously. The BER released statistics indicating that consumer confidence is at its lowest level since 1994. Bank impairments at nearly all major banks have increased significantly, and the SARB reports that foreign direct investment in the 1st quarter has dropped to nearly zero. Strangely, there is a scarcity of reports on these concerning developments in the mainstream media.

Certain media outlets have been using the word "surprise" in their commentary. However, one wonders where they have been over the past 5 to 10 years. This creeping financial collapse has been extensively documented and forewarned by many analysts, including Claude Baissac and myself. Despite the evidence, the media has tended to dismiss articles discussing these concerns as "too negative."

I can attest to this firsthand, as I have received numerous "too negative" rejection slips from finance editors over the past seven years or so. Instead of addressing the pressing issues, these media outlets often publish gloriously over-optimistic articles about South Africa's situation week after week.

The reality is that there is no escaping the severity of the situation, and pretending that all is well or that the downturn is merely temporary is futile. However, there has been one notable exception to this trend. Claire Bisseker of the Financial Mail has written several excellent front-page reports on this developing trend, with the most noteworthy one being "SA's Doomsday Clock," published in April of this year. Her willingness to address the serious challenges facing the country is commendable amid the prevailing optimistic narrative in the media.

South Africa and its people are broke. It's not due to one factor alone; rather, it's a combination of several ever-worsening financial trends that have all hit almost simultaneously.

- Over the past two years, **interest rates** have been raised a staggering 10 times during the upward phase of the interest rate cycle.
- According to SARS, there are merely **207,000 taxpayers who earn more than R1 million,** revealing the limited number of high-income earners contributing significantly to the country's revenue.
- **The number of dollar millionaires has significantly decreased, plummeting from 44,000 in 2018 to below 30,000 today.** Consequently, many affluent individuals are emigrating, raising concerns about the sustainability of South Africa's tax base and its ability to support the nation's financial needs.

Yet the ANC and its hangers-on keep on spending and planning large, as if we are a rich country. If it's not writing off Eskom loans (R400bn) or plans to introduce the National Health Service—which will cost an estimated R250bn or so per year—it's the fanciful idea that SA can afford a basic income grant for all.

WHAT TO DO, WHAT TO DO…?

1. **For many middle and upper-middle-class investors, it's almost too late to save the day. However, any spare cash should be used to create an offshore share portfolio, starting with the R1m annual investment allowance, which is the quickest and easiest way to externalize some capital from SA.**

2. **Secondly, any surplus property investments—the remnants from the Buy to Rent era—should be sold soonest. It's not going to get better, while the opportunity costs of alternative investments get bigger and bigger every year.**

3. **Consider cashing out your RA's and/or preservation funds, taking out your tax-free portion, and either converting your capital to a 100% offshore living annuity or paying the taxes and putting the cash into offshore asset swaps or moving it offshore using all or part of your R10m investment allowance.**

Obviously, this advice won't sit well with the country's asset managers, property developers, car manufacturers, etc., but I simply don't care. I think this is the best advice for ordinary investors and savers who have been offered biased and misguided "advice" for many years, but the end result is now clear for all to see.

Magnus Heystek is an investment strategist and director at Brenthurst Wealth. Brenthurst was once again voted one of the top 3 Boutique Managers in SA in the annual Intellidex Survey, published last week. This marks Brenthurst seventh consecutive inclusion in the top five companies in South Africa.

Brenthurst is proud to announce that we have been recognized as one of SOUTH AFRICA'S TOP WEALTH MANAGERS at the prestigious 2023 Intellidex Top Private Banks and Wealth Managers Awards.

This marks our seventh consecutive inclusion in the top five companies in South Africa, and we are thrilled to have been awarded the title of Top Boutique Wealth Manager in both 2020 and 2017.

This achievement fills us with immense pride and gratitude, and it serves as a testament to our unwavering commitment to excellence.

We are especially proud of our ranking in second place for the People's Choice Award category as client service is the cornerstone of our approach. The People's Choice award is a significant recognition, as it is solely determined by feedback from our valued clients.

We extend our appreciation to our valued clients and remain committed to providing the highest level of wealth management services, striving to exceed your expectations at every step.

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