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IN THIS ISSUE

While cash offers stability, liquidity and attractive short-term yields, the article explains why holding too much cash can limit long-term wealth creation, as inflation gradually erodes purchasing power and investment growth opportunities.

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CASH IS KING, BUT IS IT?

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Many investors tend to use a universal benchmark when gauging investment performance, and most default to money market rates and, to a lesser extent, cash rates that their banks provide in current accounts.

There are many different money market fund options available, of which performance is roughly equal because the underlying investment universe is relatively constrained.

In a world where the actual use of physical cash is declining, money market is still as popular as ever. But do money market funds have a place in modern investing, and should investors be using them in the long term?

Based on the chart below, a money market investment with Ninety One would have provided investors with an annualised return of 7.14% over the last 10 years.

FUND PERFORMANCE (ZAR)

Fund	Allocation %	6 mth	1 yr	3 yr	5 yr	10 yr
Ninety One Money Market Fund	100%	3.52%	7.46%	8.23%	7.15%	7.14%
Total weighted average		**3.52%**	**7.46%**	**8.23%**	**7.15%**	**7.14%**

The ZAR returns on money market has been pretty straightforward. Investors have had consistent returns over the last ten, five and three years. It would seem that having invested in a money market fund has been a good investment, but let us dive a bit deeper into the other factors that investors tend to overlook.

Let's assume an investor started with R1 million in a money market fund at the beginning of 2016 and has remained invested for 10 years.

At an annual return of 7.14%, the investment would be worth R1,992,100* after 10 years.

Year	Opening Balance	Interest @ 7.14%	Closing Balance
2016	R1,000,000.00	R71,400.00	R1,071,400.00
2017	R1,071,400.00	R76,497.96	R1,147,897.96
2018	R1,147,897.96	R81,960.91	R1,229,858.87
2019	R1,229,858.87	R87,813.92	R1,317,672.79
2020	R1,317,672.79	R94,084.84	R1,411,757.63
2021	R1,411,757.63	R100,803.49	R1,512,561.12
2022	R1,512,561.12	R108,001.87	R1,620,562.99
2023	R1,620,562.99	R115,714.20	R1,736,277.19
2024	R1,736,277.19	R123,977.19	R1,860,254.38
2025	**R1,860,254.38**	**R132,830.16**	**R1,993,084.54**

Sounds great, right? Yes, but in reality, a different picture emerges.

It's similar to a car manufacturer claiming impressive mileage on new models, when the car's outputs are measured in a controlled environment and driving at a constant speed - the best-case scenario. But unfortunately, this is never the case.

To quote Benjamin Franklin: ***"In this world, nothing can be said to be certain, except death and taxes."***

And taxes there will be.

Before we proceed to the next table, let us just make the following assumptions:

- The investor is below 65 years old at the end of the investment term
- Initial investment: **R1,000,000**
- Final gross value: **R1,992,100***
- Gross annualised return: **7.1349%**
- Annual interest exemption: **R23,800**
- Marginal tax rate: assume a **45% income tax rate** (currently the maximum tax rate)
- Fully taxable money market interest
- Tax paid annually

*** Inflation adjusted using official South African CPI figures**

Year	Opening Balance	Gross Interest	Taxable Interest	Tax @45%	Net Growth	Closing Balance After Tax	Inflation	Real Value in 2015 Rands
2016	R1,000,000	R71,35	R47,55	R21,40	R49,95	R1,049,952	6.60%	R984,95
2017	R1,049,952	R74,92	R51,12	R23,00	R51,91	R1,101,865	5.30%	R982,37
2018	R1,101,865	R78,62	R54,82	R24,67	R53,95	R1,155,815	4.60%	R983,23
2019	R1,155,815	R82,47	R58,67	R26,40	R56,07	R1,211,882	4.10%	R983,73
2020	R1,211,882	R86,47	R62,67	R28,20	R58,27	R1,270,152	3.20%	R991,61
2021	R1,270,152	R90,64	R66,84	R30,08	R60,56	R1,330,713	4.60%	R988,01
2022	R1,330,713	R94,97	R71,17	R32,03	R62,95	R1,393,659	7.00%	R966,35
2023	R1,393,659	R99,49	R75,69	R34,06	R65,43	R1,459,088	6.10%	R955,65
2024	R1,459,088	R104,16	R80,36	R36,16	R68,00	R1,527,085	4.40%	R960,68
2025	R1,527,085	R108,92	R85,12	R38,30	R70,61	R1,597,698	3.22%	R977,78

WHEN COMMITTING TO A MONEY MARKET FUND, INVESTORS TEND TO OVERLOOK TWO THINGS: INFLATION AND NET (AFTER-TAX) GROWTH.

We know that the R1m invested will be worth R1,992,000 after 10 years – there is no doubt about this. But as the table shows, the net return (after tax and exemptions) in the money market fund has effectively provided the investor with a 4.78% per annum return. Assuming the average inflation rate over the last 10 years was roughly 4.61%, the real return from money market is actually closer to 0.18% per annum.

Has this investment grown? Yes, technically it has, but this is before accounting for taxes and inflation. Has this investor made real capital growth? Not really.

THE REAL ANNUALISED RETURN AT DIFFERENT INCOME TAX BRACKETS

Marginal Tax Rate	Net Annualised Return	Real Return After Inflation
18%	6.18%	1.50%
26%	5.77%	1.10%
31%	5.51%	0.86%
36%	5.25%	0.61%
39%	5.10%	0.47%
41%	5.00%	0.37%
45%	4.80%	0.18%

Money market should be used for short-term cash savings. Investors are “saving themselves poor” when making use of money market. Nominal returns in money market funds can look attractive, but after inflation and tax, real wealth creation is often negligible over long periods.

When deciding on an investment strategy, regardless of age, there are alternatives to use, and investors need to be comfortable with increasing and adjusting their risk profiles. Investors have the ability to blend their portfolios with cash, bonds and equity, but purely relying on money market for long-term capital growth is just not effective.

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Mags is Head of the Sandton office and serves as the Key Individual for Johannesburg.

He has been active in the financial services industry for more than ten years and qualified as a CERTIFIED FINANCIAL PLANNER® professional in November 2012. In addition, he acts as a representative and Key Individual for Brenthurst Capital (Pty) Ltd and serves on the investment committee, where he contributes to investment and asset allocation decisions.

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