# TABLE TALK

**Pieter Hugo**, MD of Prudential Unit Trusts, shares his insights into everyday investing issues.

**Q** **Because the performance of South African equities has been so poor in the past three years, I've been putting my savings into cash investments to avoid losses. Should I leave it there? I'm saving for longer-term goals like my children's university costs and retirement.**

**A** **You may be pleased with your decision to have** built up your cash holdings, since cash investments have returned around 2.3% per annum more than the local equity market over the three years to 30 September 2019. Investors have generally not been rewarded for holding riskier assets like equities.

Yet as a longer-term investor, you should be concerned about your current portfolio positioning and prospective returns. This is because cash returns are unlikely to beat inflation sufficiently in the long-term to give you enough capital growth over time. If you maintain a conservative approach going forward and stay in cash over the long term, you are unlikely to build up a large enough retirement pot to meet your needs. The reality is that at some point you will need to move back into SA equities and listed property, assets that have historically offered the requisite inflation-beating returns over time (averaging around 12% to 13% p.a.).

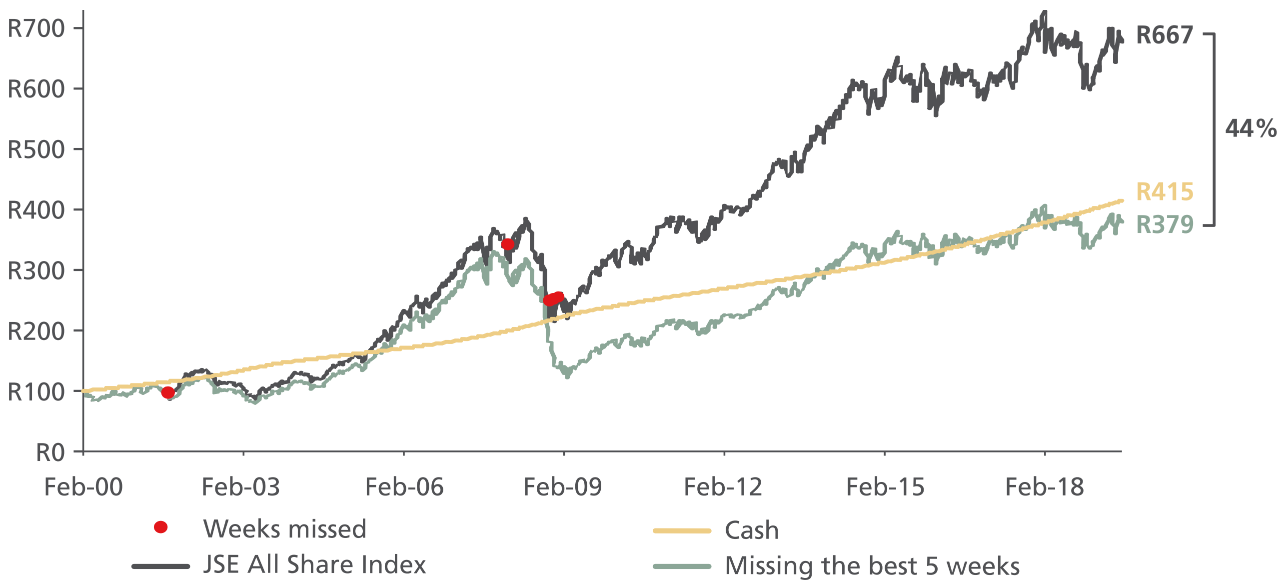
### MISSING BEST 5 WEEKS LEAVES YOU WITH 44% LESS

So when do you buy more equities? History has demonstrated that most people wait until it's too late. They don't want to invest in equities now because at this point historical equity returns have been poor – so they wait for the historical returns to improve first, and then move into equities. By definition, this means they miss out on a large part of the upside on offer.

Graph 1 shows the impact of missing out on the best five weeks of returns on the FTSE/JSE All Share Index (ALSI)

IMAGE: SUPPLIED

MISSING THE BEST 5 WEEKS ON THE JSE




Source: Morningstar, Prudential Investment Managers

since February 2000. During this 19-year period, investors who stayed consistently invested in the ALSI would have received R677 from their R100 investment (shown by the black line), but those who missed the best 5 weeks would have received only R379, an astounding 44% less (depicted by the grey/green line).

Meanwhile, those who were exposed to cash (represented by the gold line) over the entire period would have earned R415, which is 37% less than the equity investment.

## SA EQUITIES ARE CHEAP

After such a weak three-year performance, it should be no surprise that the SA equity market is valued at quite attractive levels representing a discount of around 20% to 25% compared to its own history. The market was last at such cheap levels in early 2009 as it was starting to recover from the Global Financial Crisis (GFC). Although many investors are arguing that "this time it's different", and that today's low equity valuations are merited, the current concerns over South Africa's low growth, corruption and divisive politics are certainly nowhere near as threatening as the GFC conditions were back in 2009. Should all things remain the same, with no change in valuations, we estimate that South African equities are priced to deliver a return of around 14% p.a. over the next three to five years. However, if valuations rise and company earnings growth doesn't disappoint, then they could offer an even higher return over the longer term.

## CONSIDER LIFTING YOUR EQUITY EXPOSURE

This makes it a good time for longer-term investors now sitting in cash to start getting back into the South African equity market, where they can benefit from the attractive valuations now on offer. Of course we don't know when these prospective returns will materialise, only that, based on its past performance over decades, the equity market typically delivers excellent returns over the long term from such attractive valuation levels.

Investors wanting to achieve longer-term returns of 4% to 5% above inflation should include around 40% equity exposure in their portfolios, typically found in more conservative balanced unit trusts like the Prudential Inflation Plus Fund. For those aiming for 6% to 7% returns above inflation, they would need up to 75% exposure to equities, which is offered by a typical balanced unit trust like the Prudential Balanced Fund.

Don't be dissuaded by the excessively pessimistic sentiment now prevailing that could lead to more equity downside in the short term; longer-term investors need to be in the market to capitalise on the upside.