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Prudential Investment Managers

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Remembering the fundamentals of investing

The rate at which the COVID-19 virus has spread globally has left many investors feeling understandably nervous. Equities have fallen dramatically since the start of the outbreak, with the FTSE/JSE ALSI falling 33% in the past 30 days (as at 19 March 2020). Bonds haven't fared much better either, with the yield on the SA 10-year government bond increasing roughly 31% over the same period. All of which begs the question: What action, if any, should investors take?

In times like these it's important to remember the fundamentals of investing. While this may seem like an oversimplification of a fairly complex situation, its often the case that by going "back to basics" you will avoid making rash investment decisions, which could end up have detrimental long-term implications on your investment outcomes. To help you navigate these uncharted waters, we've listed three investment fundamentals which we strongly encourage you to consider before transacting on your investment.

1. Don't act out of emotion

Research has shown that poor investor behaviour can have a significant impact on your investment returns. This is largely down to poor timing, where you either buy or sell at the wrong time. These decisions are

typically driven by a heightened sense of emotion (such as a fear or greed), instead of being based on intrinsic data or your long-term investment objectives. When looking at this phenomenon within the context of today's investment environment, it's clear that the fear of losing money has become one of the primary drivers behind the market sell-off. This course of action is somewhat ironic given that the risk of locking in losses (and actually losing money) becomes significantly higher when selling during a market downturn. Often, the most appropriate course of action in times like these is to mitigate the additional risk of poor investor behaviour and simply do nothing. If history has taught us anything, it's that at some point in time markets are likely to recover.

2. Stick to your investment objective

There's a saying that goes: unless your investment objective has changed, neither should your investment. The premise of this statement is twofold – that investors select the most appropriate asset classes to achieve their investment objectives, and that they have a good understanding of the characteristics of their chosen assets. Understanding your chosen asset class can go a long way in helping you avoid overreacting during periods of volatility. Equities for example are typically volatile investments over the short term, with an upward-sloping performance trend line over the long-term. Put different, while equities are expected to go up and down over the short term, over the long-term (7 years plus), they are expected to outperform most other asset classes. Granted, the COVID-19 market sell-off is somewhat of an anomaly, but investors who understand this asset class should expect some degree of volatility – and when it happens – they are less likely to act out of fear of losing money, thereby mitigating the risk of diverging from their investment objective.

3. Look for opportunities

There is another saying that goes: just because it's cheap, doesn't necessarily mean you should buy it. However, if an asset class that forms part of your long-term objective is trading as a significant discount, you may want to consider taking advantage of the low price. Something to consider is that by doing so you may create an imbalance within your target asset allocation. For example, if your total portfolio consists of a mix of 25% bonds and 75% equities, buying more equities may very well push your bond exposure within your portfolio lower. Similarly, if your portfolio is relatively low-risk with a higher proportion of bonds relative to equites, increasing your equity exposure will increase the risk profile of your portfolio. When buying more of a discounted asset class, the decision

to do so shouldn’t be made in isolation, but rather with the view of how it will affect the broader asset weighting of your total portfolio and the impact that this might have in reaching your investment objective. It’s usually the case that most personal portfolios have some degree of flexibility to account for market movement. We strongly encourage talking to your financial adviser first before making any decisions relating to your investments.

In conclusion, the market sell-off has been a trying time for many investors. But to echo the thoughts of our president, now is not the time to panic. Chaos often presents opportunity, and it’s important to fight the urge to act out of emotion and to look for those moments where you can capitalise on the irrational actions of others. That said, in times like these it’s worth remembering the fundamentals of investing and sticking to your investment objectives. After all, time in the market is typically always better than trying to time the market.

For more information, please contact your financial adviser or feel free to call our client services team on 0860 105 775 or email us at query@prudential.co.za.