Talking Points
Elections and Investments

Morningstar Investment Management South Africa
May 2019

Victoria Reuvers
Senior Portfolio Manager, Morningstar Investment Management South Africa

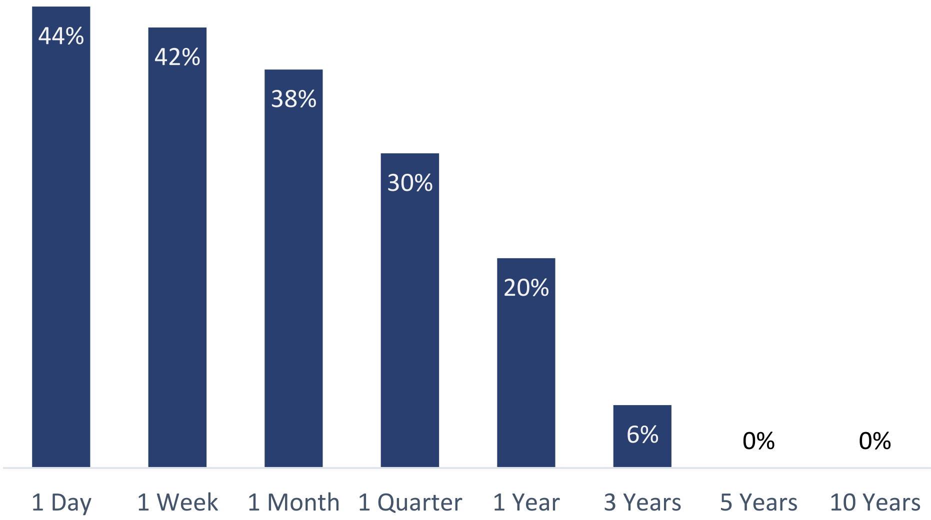
For Financial Advisors and their Clients

As we draw close to election day, there is a palpable sense of anxiety due to the many iterations of how things will be post 8 May 2019. While we process these thoughts and possible outcomes, the one question that is front of mind for many investors, is when will confidence return?

Confidence and optimism are both necessary in order to promote a belief that tomorrow will be better than today. Confidence is the much-needed missing ingredient that can breathe life into our ailing economy. In addition to this, positive economics is what will create jobs, tax revenue and ultimately wealth. But what about our investments? It is easy and tempting to translate fear and anxiety around possible outcomes of events into something within our reach - our investments. When we invest for our future, we often forget that the returns we achieve by staying in the market will almost never occur in a straight line. It can be a bumpy and uncomfortable ride over the short term. There are so many things to worry about and so much that could go wrong, but this is part of the journey. Every year holds unknowns and uncertainties - it is our behaviour that defines our investment outcomes.

If we look back at the SA equity market's daily performance over the past 20 years, which is represented in the graph below, we can see that the daily market return was negative just over 40% of the time. That makes sense – there has been a lot of bad news and negative headlines over the past 20 years on a day to day basis.

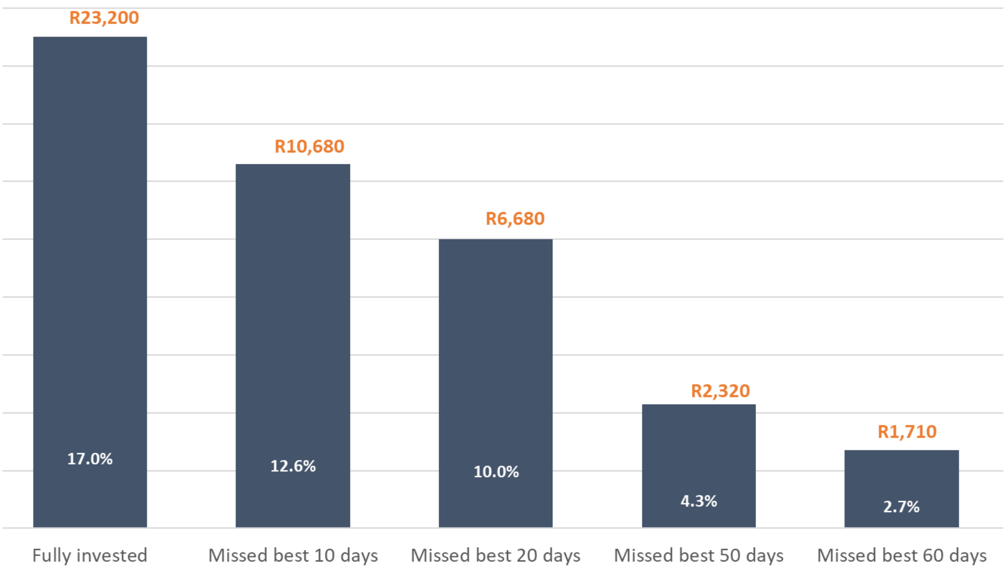
Probability of negative returns from equities over various time periods



Source: Morningstar Direct

If you had been invested in the market for the past 20 years and ignored the headlines – and withstood the temptation to withdraw money - you would have made a return of 17% per annum, translating into a return of around 11% per annum above inflation! However, if you tried to time your entry point and exit point based on news flow and you missed the best 50 days of the past 5852 days (20 years) you could have been invested, your return drops to 4.3% per annum – this is a negative real return of roughly 3% per annum.

Risk of missing the best days in the market 1997-2018 (initial investment of R1,000)



Source: Morningstar Direct

There is an entirely understandable temptation to take control and make changes when faced with negative headlines. The belief that there is an ability to time entry and exit points is one of the fastest and easiest ways to destroy wealth over time.

As with all matters to do with long-term investing, patience is key. So too, is the knowledge that all the concerns and uncertainties surrounding an uncertain future - currently the national election outcome - is most likely already in the prices of associated assets. For example, South African-focused companies have endured a torrid time over the past decade and as a result, their share prices have fallen dramatically. At this point in the cycle, there is an enormous amount of pessimism incorporated into their current share prices and therefore, select shares are looking particularly attractive for long-term investors.

While we cannot predict the outcome of what will transpire following the election, the best we can do is to remain disciplined investors focused on valuations and generating long-term real returns for investors. In this context, volatility in market prices should be welcomed. A drop in price can create opportunities for our managers who hold cash to buy assets that are significantly underpriced relative to their long-term fair values, thereby sowing the seeds for future returns. The key is to remain patient and to assess the developments with a rational framework that avoids behavioural impulses and political biases. This remains the most optimal way to create long-term value and is one of many areas where we can add value, by maintaining a long-term view when others won't.

.

Risk Warnings

This commentary does not constitute advice and is supplied for information purposes only. Morningstar Investment Management South Africa cannot guarantee positive results from our investment decisions, and we cannot guarantee that our portfolios will meet your objectives or that losses will be avoided in any of the portfolios. Any investment's future performance could differ greatly from its past results, and this difference includes a potential for losses, which may cause portfolio values to drop.

Morningstar Investment Management South Africa Disclosure

The Morningstar Investment Management group comprises Morningstar Inc.'s registered entities worldwide, including South Africa. Morningstar Investment Management South Africa (Pty) is an authorised financial services provider (FSP 45679) and is the entity providing the advisory/discretionary services.