**7 LESSONS THAT WILL RESHAPE YOUR FUTURE**

You’ve heard it before: sticking to your long-term savings plan is one of the surest paths to a more comfortable retirement. The fear of losing money often drives investors to sell out of the market and opt, instead, for the perceived safety (see lesson 2) of a bank account.

This was particularly relevant in 2017, as local political turbulence appeared to reach fresh highs – making it extremely easy to get caught up in the negativity. In fact, seldom has a year highlighted the importance of keeping a long-term focus in mind better than 2017. In the first half, equity markets continued tracking sideways and made “risk-free” bank accounts look attractive. However, the strong rally later in the year meant SA equity delivered 21% in 2017 – its best annual return since 2013.

Old Mutual Investment Group’s multi-asset class boutique, MacroSolutions, invests across a wide range of local and global asset classes. To do this, the fund managers require an in-depth knowledge of what drives each of these asset classes, especially over the long term. In scrutinising the performance and behaviour of asset classes over the past 88 or more years, they identified valuable lessons to help build a resilient investment plan.

These lessons shape the key principles of MacroSolutions’ investment philosophy and have contributed to the success of its multi-asset class funds.

**LESSON TO SHAPE YOUR [LONG-TERM] THINKING**

**REALITY:** Many investors suffer from “inflation illusion” as they don’t notice how destructive inflation can be over time.

**LESSON:** We need to look at long-term investment returns in “real” terms, stripping out the impact of inflation.

“Inflation is as violent as a mugger, as frightening as an armed robber and as deadly as a hit man.” Ronald Reagan

**LESSON 1 – INFLATION IS YOUR ENEMY**

**INFLATION ERODES SPENDING POWER**

Take a look at what a 6% inflation rate effectively does to your money

<table>
<thead>
<tr>
<th>TODAY</th>
<th>10 YEARS LATER</th>
<th>20 YEARS LATER</th>
</tr>
</thead>
<tbody>
<tr>
<td>R10 000</td>
<td>R5 584</td>
<td>R3 118</td>
</tr>
</tbody>
</table>

**REALITY:** A bank deposit exposes you to minimal risk, but there’s a price to be paid for that security.

**LESSON:** Cash does not significantly increase your real wealth over time. Over 88 years, cash has an after-inflation return of just 0.7% a year. It is better to own shares in the bank than to leave your money there.

**LESSON 2 – CASH IS TRASH**

**TIME NEEDED TO DOUBLE YOUR MONEY**

Using each asset class’s long-term average returns, this is how long it will take to double your REAL investment value...

<table>
<thead>
<tr>
<th>SA EQUITIES</th>
<th>SA BONDS</th>
<th>SA CASH</th>
</tr>
</thead>
<tbody>
<tr>
<td>10 years</td>
<td>41 years</td>
<td>90 years</td>
</tr>
</tbody>
</table>
REALITY: Many investors will not retire with enough money.

LESSON: We need the higher long-term returns from equities to grow our wealth. This is particularly important in a world where people are living longer.

**PERFORMANCE OVER 88 YEARS (nominal returns)**

<table>
<thead>
<tr>
<th>Investment</th>
<th>14% a year</th>
</tr>
</thead>
<tbody>
<tr>
<td>SA Equity</td>
<td></td>
</tr>
<tr>
<td>SA Bonds</td>
<td>7.8% a year</td>
</tr>
<tr>
<td>SA Cash</td>
<td>6.9% a year</td>
</tr>
</tbody>
</table>

Inflation: 6.2% a year

LESSON 3 – YOU NEED EQUITIES

REALITY: The main reason investors prefer cash to equities is the fear of losing money.

LESSON: The best way to manage the risk of losing money is to remain invested in equities for longer. As soon as you extend your holding period to more than three years, past performance shows that the chance of losing money become negligible.

**PROBABILITY OF NEGATIVE RETURNS OVER DIFFERENT TIME PERIODS**

- 1 day and 1 week: Rolling total returns, June 1995 – December 2017
- 1 month to 10 years: Rolling returns, January 1960 – December 2017

<table>
<thead>
<tr>
<th>Time Period</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Day</td>
<td>44%</td>
</tr>
<tr>
<td>1 Week</td>
<td>42%</td>
</tr>
<tr>
<td>1 Month</td>
<td>38%</td>
</tr>
<tr>
<td>1 Quarter</td>
<td>30%</td>
</tr>
<tr>
<td>1 Year</td>
<td>20%</td>
</tr>
<tr>
<td>3 Years</td>
<td>6%</td>
</tr>
<tr>
<td>5 Years</td>
<td>0%</td>
</tr>
<tr>
<td>10 Years</td>
<td>0%</td>
</tr>
</tbody>
</table>

LESSON 4 – TIME IS YOUR FRIEND

REALITY: Money needs time to benefit from the full potential of compounding growth.

LESSON: Start saving as soon as you can, leave it for as long as you can, and let compounding do the work for you. And tick the dividend reinvest box on your investment application form to maximise your growth.

Compounding simply means making money on your original investment as well as on the gains made in previous years (i.e. growth on growth over time).

**GROWING YOUR WEALTH OVER TIME**

Using the long-term nominal average return of 14% a year, look at what happens when your money is invested in SA equities over time:

- **TODAY:** R1 000
- **10 YEARS LATER:** R3 712
- **20 YEARS LATER:** R13 780

LESSON 5 – COMPOUNDING IS A POWERFUL WEALTH GENERATOR

THE OLD ADAGE HOLDS TRUE: “TIME IN THE MARKET, NOT TIMING THE MARKET.”
REALITY: Equities may have been the best performing asset class since 1929, but cash was the best performer for 11 of those years and listed property for 9 years…

LESSON: Diversification is the one free lunch in investments; use it. That is because it pays to invest across different asset classes.

LESSON 6 – DON’T PUT ALL YOUR EGGS IN ONE BASKET


- SA Equity – 48%
- SA Gold – 16%*
- SA Cash – 13%
- SA Bonds – 14%
- SA Property – 10%**

* since 1967
** since 1980

REALITY: Asset classes have distinct secular or long-term periods of under- and outperformance.

LESSON: Active asset allocation is a vital tool in delivering superior returns.

LESSON 7 – ASSET ALLOCATION ADDS VALUE

UNDERSTAND THAT MARKETS MOVE IN CYCLES

SA BONDS, for instance, gave a negative real return for 40 years, before delivering a great return over the last 30 years.

LISTED PROPERTY went nowhere for 15 years, before becoming the best performing asset class for the next 20.

If any of these lessons resonated with you and you’d like to find out more about the long-term history of local and global asset classes, go to www.oldmutualinvest.com to read MacroSolutions’ LONG-TERM PERSPECTIVES 2018 yearbook.

Sources: FactSet and Old Mutual Investment Group.
Using annualised returns from December 1929 to December 2017.