

Managing Investments in the 21st Century

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Investment Seminars
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How did we manage investments in the previous century?

- Law firms – trustees – fiduciary responsibility
- Establish cash flow first, invest surplus in “special interest shares”

“Don’t worry your pretty little head young lady.... we’ll take care of you”



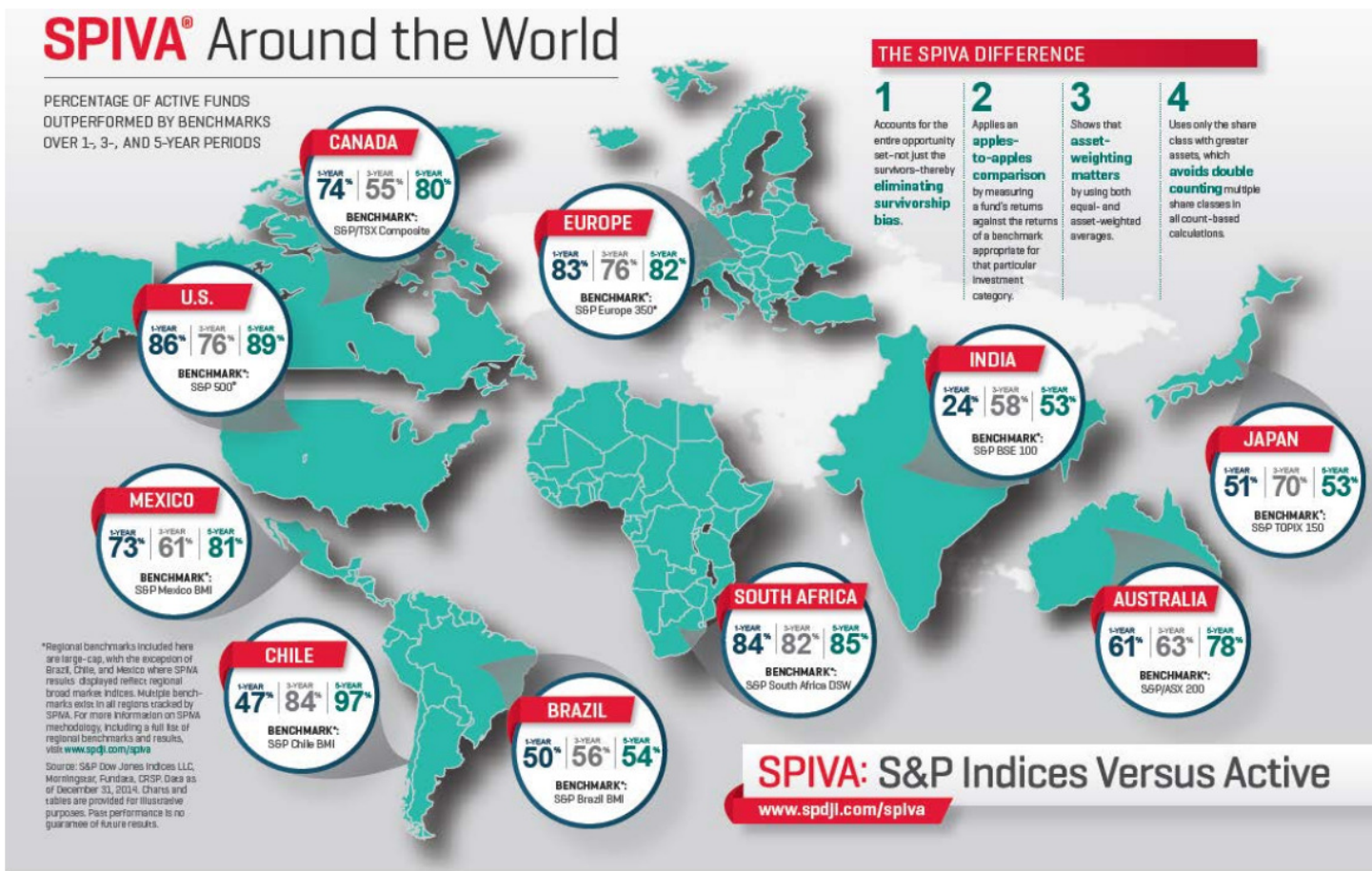
Investments products and processes from the previous century?

- Insurance companies were the first “asset managers”
- Introduction of specialist asset managers
- Occupational pension funds – move from defined benefit to defined contribution shifted responsibility to member
- Direct stock broking portfolios for wealthy investors
- Unit trusts opened up investment opportunities to a broader client base
- “Democratisation of capital” requires new investment opportunities for the 21st century

Unit trusts: launched in SA in 1965



What we now know to be true



±80% of active managers under-perform the general equity index

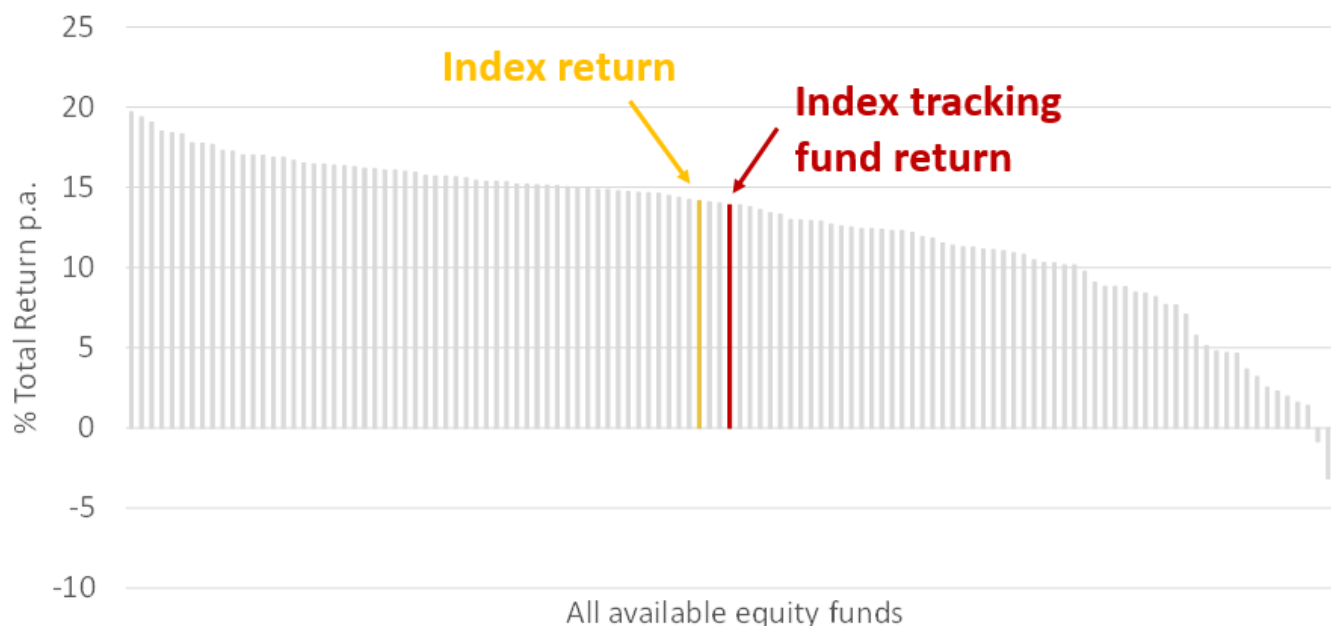
Source: S&P Dow Jones Indices, LLC. Chart is provided for illustrative purposes. Data is as of Dec. 31, 2014.

The Home of Exchange Traded Funds®



What we now know to be true

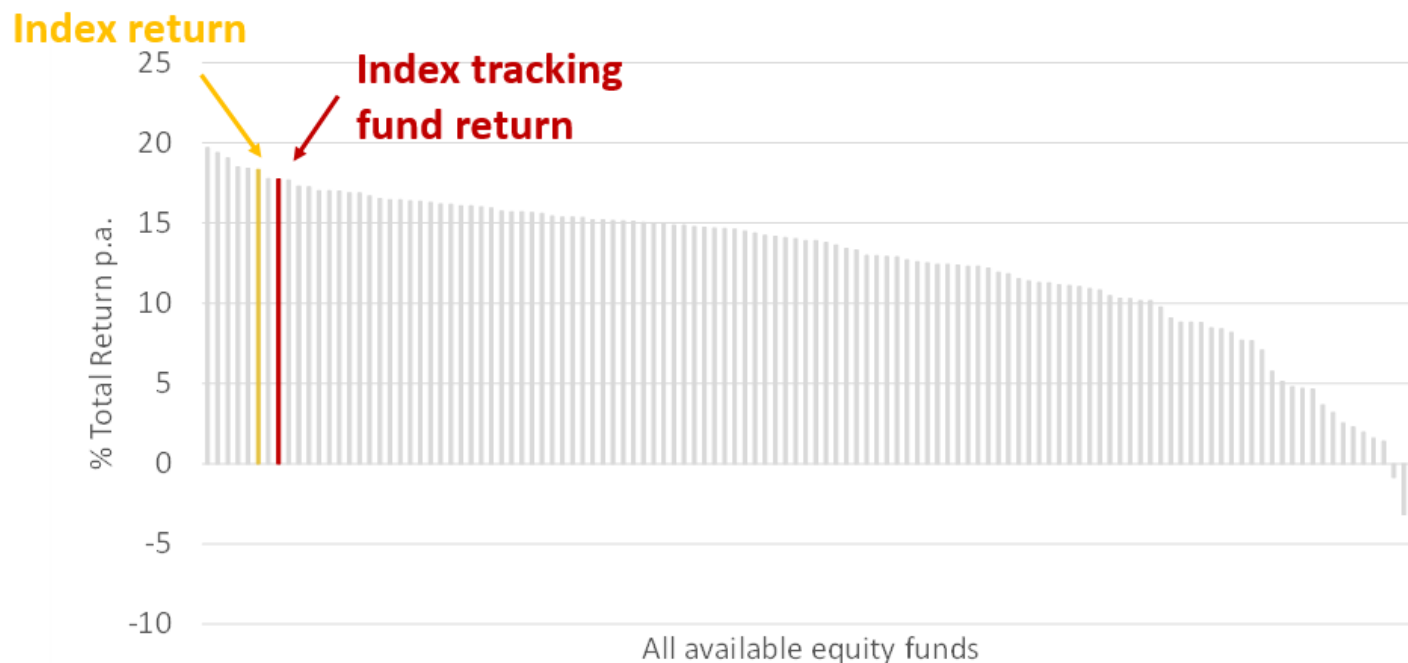
Perception of "average"



All index-tracking funds underperform the index it tracks 100% of the time

What we now know to be true

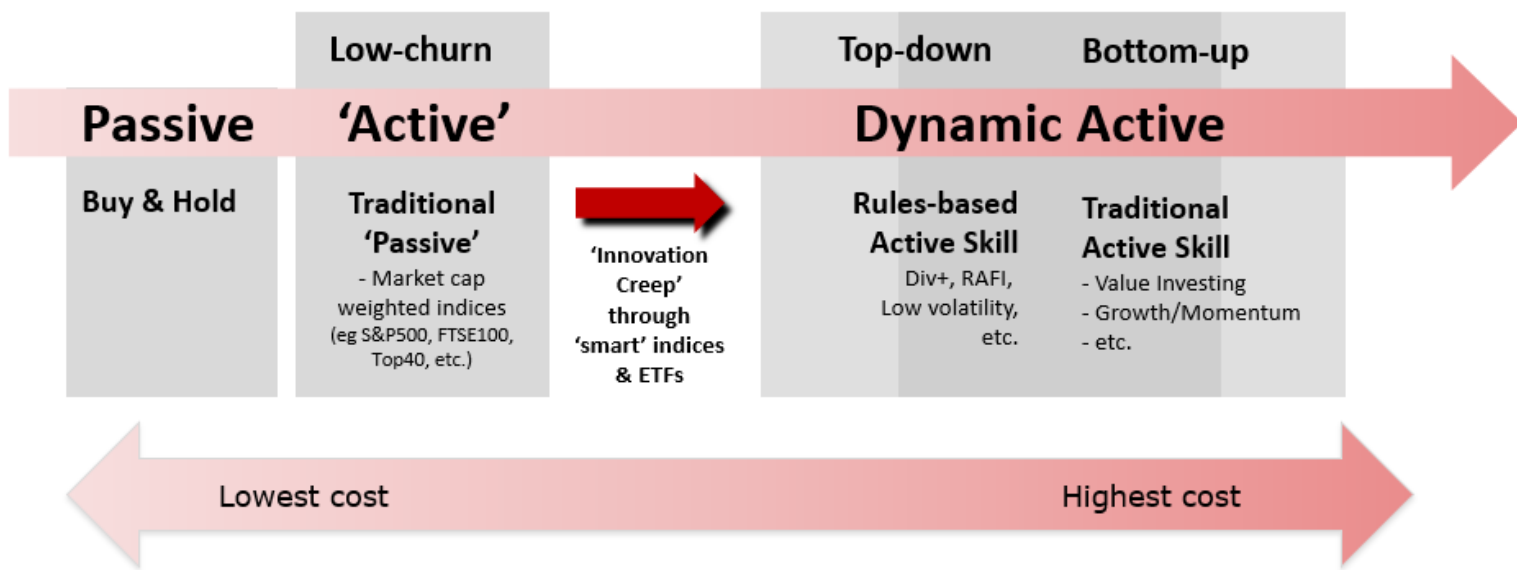
Reality of "average"



All index-tracking funds underperform the index it tracks 100% of the time

But that does not make it "below average"

What we now know to be true



All investing is active...

...it's just the level of activity that varies

What we now know to be true

Passive

costs less than

Active

What we now know to be true

Buy & Hold Passive

costs less than

So-called **Passive**

costs less than

Active

doesn't exist

What we now know to be true

Buy & Hold Passive
costs less than

So-called **Passive**
costs less than

Rules-based Active
costs less than

Traditional **Active**

doesn't exist

"smart" beta

Total Expense Ratio (TER) - what's in it?

- Fixed costs
 - Trustee fee; audit fee; regulatory charges; licensing fees, etc.
 - The smaller the fund, the bigger this is as a % of fund size
- Variable costs
 - Manco fee (issuing company) – relatively small, and standard
 - Asset management fee – varies significantly according to investment style, incl. active vs. index-tracking
 - Performance fee – can be significant, especially if the “hurdle” is inappropriate
 - Trading costs – varies significantly according to level of activity; usually excluded, will be incl. in Effective Annual Cost

Total Expense Ratio (TER)

- Average TER for actively managed unit trusts
1.52% per annum
- Average TER for Exchanged Traded Products (ETPs)
0.33% per annum

But we know that the TER does not include all the costs!

Unit trusts are much more expensive

Costs (all p.a.)	Unit Trusts	ETFs
Average TER	1.5%	0.3%
Portfolio construction fees	0.5% to 1%	Incl. in TER
Platform fees	0.25% to 0.75%	--
Stockbroker fees	--	0.25% to 0.5%
Wrap fees	0.5% to 1%	--
Investment plan fees	--	0.3% to 0.7%
Total costs	2.75% to 4.25%	0.85% to 1.5%

Stock Broking Portfolio Costs

- Direct costs incl. trading costs, incl. brokerage & statutory charges
- Buying & selling 40 individual shares rather than 1 ETF is a LOT more expensive...

	Basket of Top 40 shares	Top 40 ETF
Gross investment amount	R 100 000	R 100 000
Brokerage (0.5% + VAT)*	R 570	R 570
JSE fees & levies**	R 537	R 27
STT (only buy)	R 250	
Net investment amount	R 98 643	R 99 403
Total cost of investment	1.4%	0.6%

* *etfSA.co.za* brokerage is only 0.08%+VAT

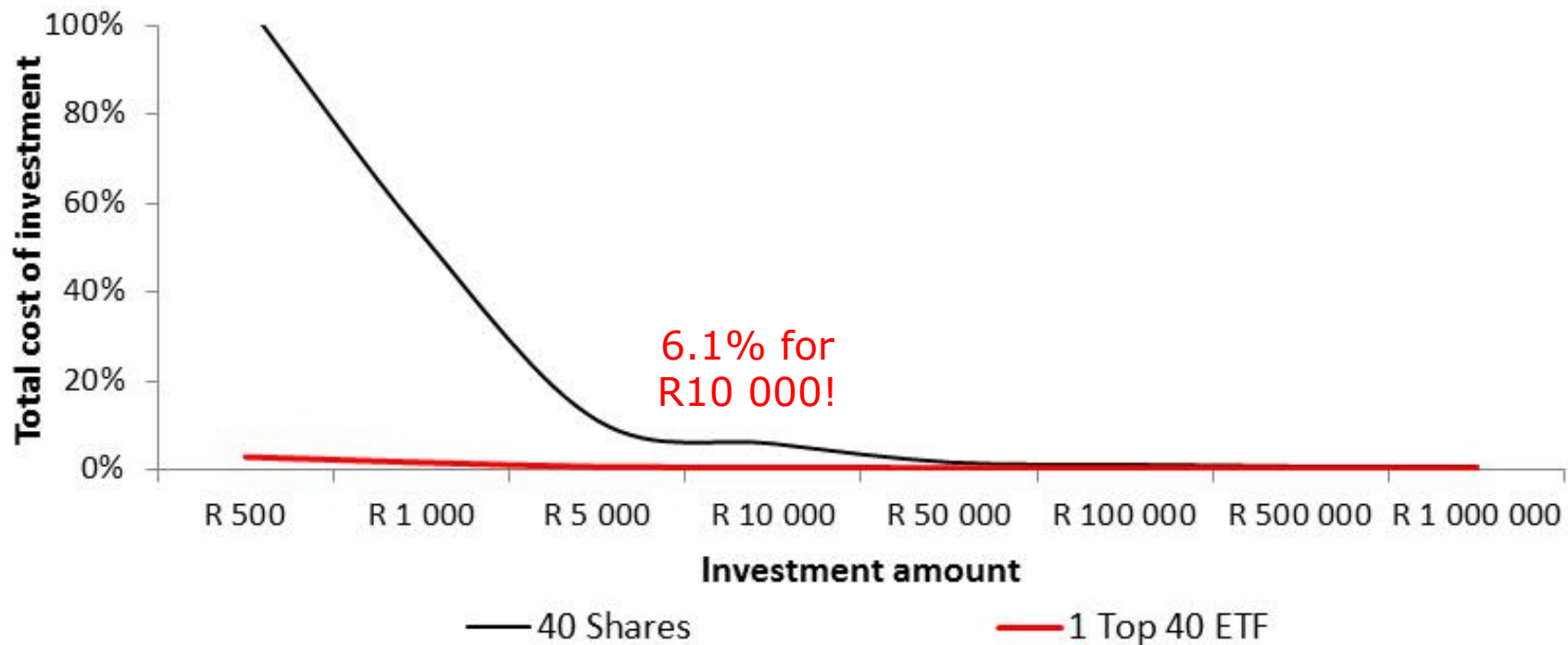
** *Statutory charges are shared amongst all investors on the day due to bulking*

The Home of Exchange Traded Funds®

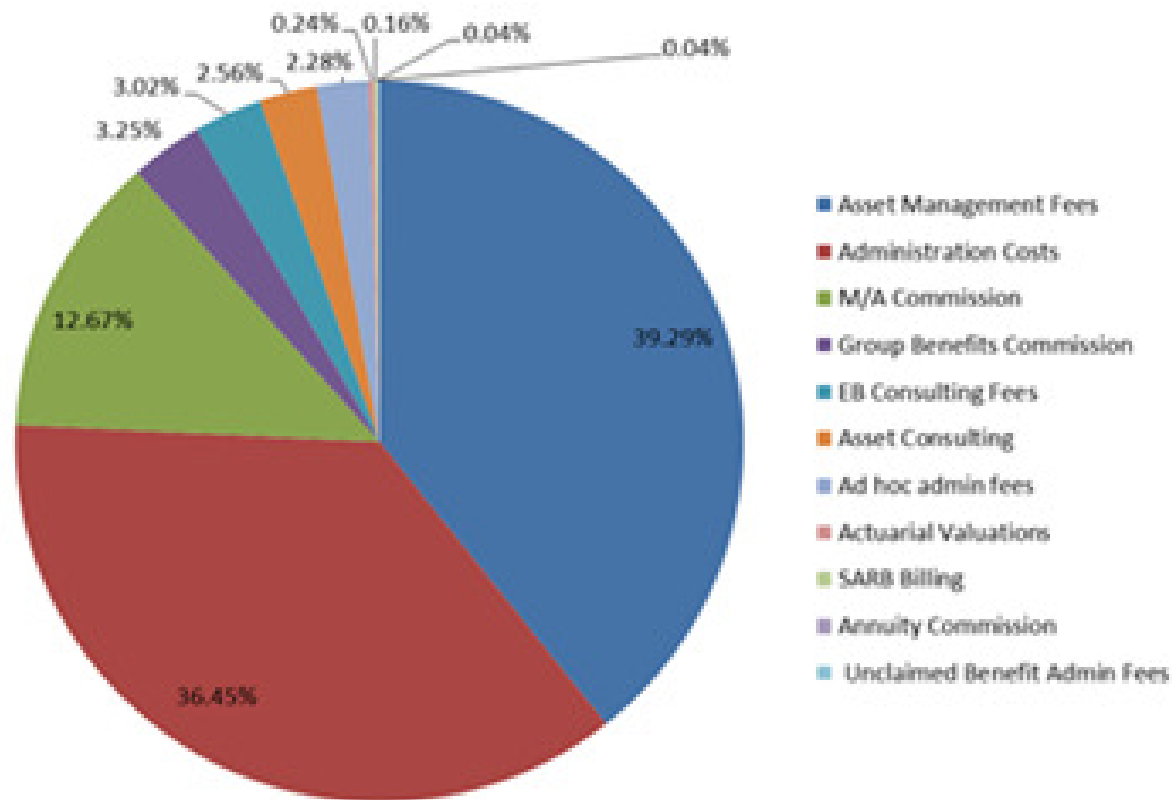


Stock Broking Portfolio Costs

- ...especially if your investment amount is relatively small (retail investors)



Cost Allocation of a Pension Fund



40%: Asset management

If TER = 1.5%
Total cost = 3.75%

If TER = 2.0%
Total cost = 5%

Source: Alexander Forbes

“ETFs are Low Risk Investments”

- **Absolute Risk**
 - An ETF carries just as much *absolute* risk as its underlying investments – can be very high, or very low
 - It’s the same as a unit trust in the same category
- **Relative Risk**
 - An ETF has negligible *relative* risk – SA regulations require full physical backing
 - The level of underperformance \equiv Cost to manage the fund (TER)
- **Regulatory Risk**
 - An ETF has the lowest *regulatory* risk – governed by FSB & JSE
 - An ETN has additional credit risk

Most Underrated Benefits of ETPs

Transparency

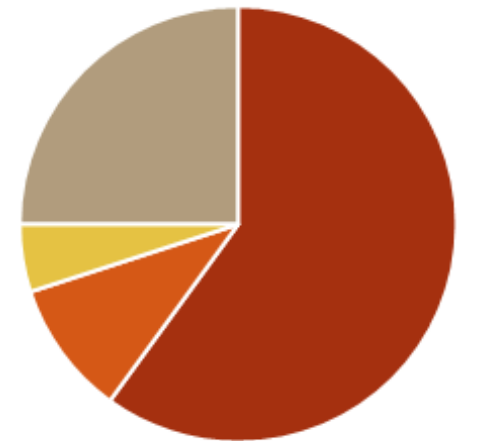


Consistency



Typical Balanced Fund

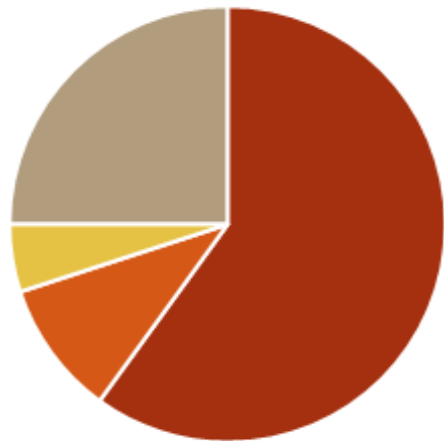
Unit trust / ETF portfolio



■ SA Equity ■ SA Bonds
■ SA Property ■ International

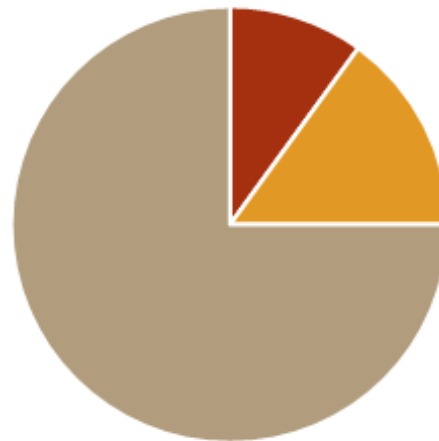
Pension fund limited to 25% offshore

Pension fund



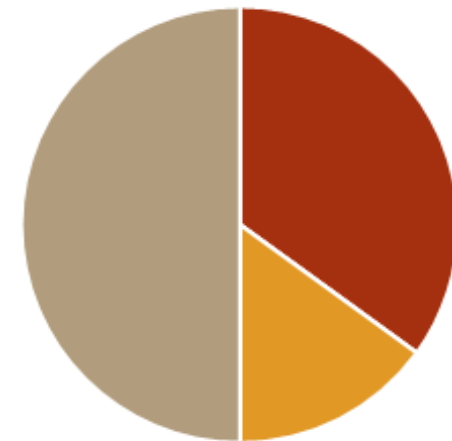
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ETF portfolio



■ SA Equity ■ SA Bonds
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Combined investments



■ SA Equity ■ SA Bonds
■ SA Property ■ International

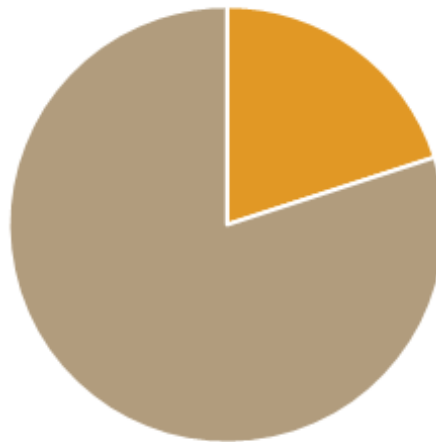
Stock broking portfolio – SA equities

Stock broking portfolio



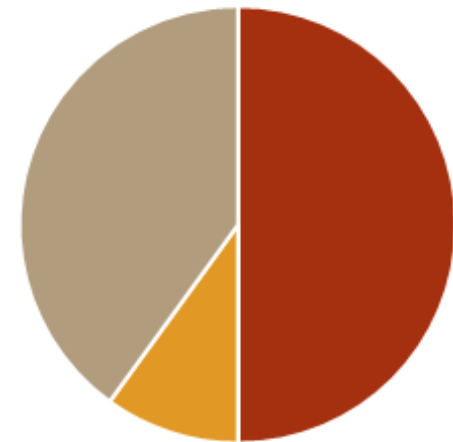
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ETF portfolio



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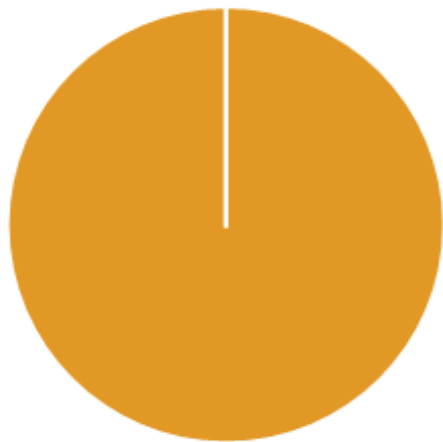
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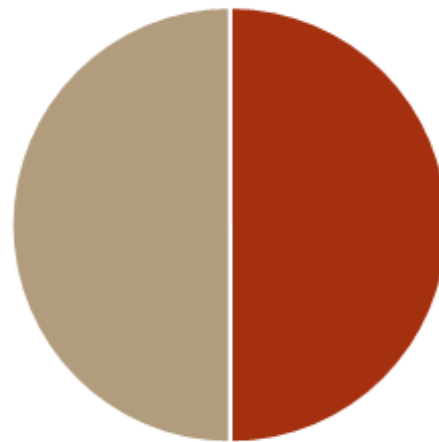
Rental income from properties

Investment properties



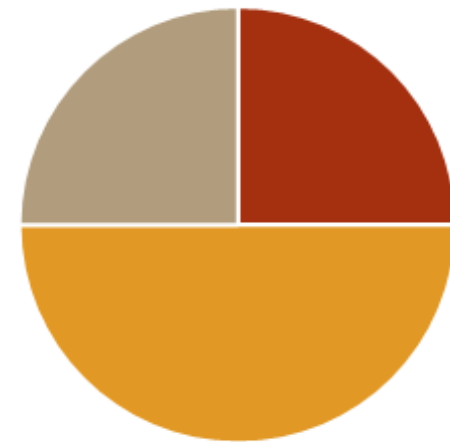
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ETF portfolio



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Combined investments



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How can you do this with your investment portfolio?

- **DIY investor**
 - Attend our seminars, do your own analysis, practise and learn
 - We can help you, but limited on etfsa.co.za – can't advise
- **Portfolio Management Service**
 - We offer a comprehensive service for portfolios > R1m
- **PIMMS – Passive Investment Management Mastery School**
 - Online training course in ETF investments & portfolio strategies
 - Learn how to do-it-yourself, or ask the right questions from advisers

Over to Mike