

## Contact us:

Alan McConnochie

+27 11 591 0551

083 378 3463

alan@rcinv.co.za

Di Haiden

+27 11 591 0572

083 308 7928

di@rcinv.co.za



You are welcome to pass this newsletter on to friends who may wish to learn more about investment.

To be added to our email, contact alan@rcinv.co.za

The only way to keep your health is to eat what you don't want, drink what you don't like and do what you would rather not. ~ Mark Twain

**RCI MET Flexible Fund** – closed May at 382.12, up 0.27% for the month, compared to the JSE Top 40 which was up 0.17%. The RCI BCI Flexible Fund is up 3.94% year to date whereas the JSE Top 40 is up 7.41% year to date. Excluding dividends, over five years our fund is up 59% and the JSE Top 40 is up 60%. We outperformed strongly until 2016 when our expectations of a weak rand and poor mining were derailed. However, we believe that a weak rand will resume and that mining will take many years to be boosted by a long-term turn in metal prices.

**RCI BCI World Wide Flex** closed at 105.05c. It is up 5.05% since its launch in December 2016.

**Visit our website:** [www.rcinv.co.za](http://www.rcinv.co.za) for back copies of the newsletter, background information, etc.

The newsletter is very short this month as Alan is desperate to get his foot on the aeroplane as he is going barging in France to celebrate his wife's birthday – so, if you hear a big splash, he has probably fallen off the gang plank.

**Gold** - South Africa no longer glistens and gold is now largely irrelevant.

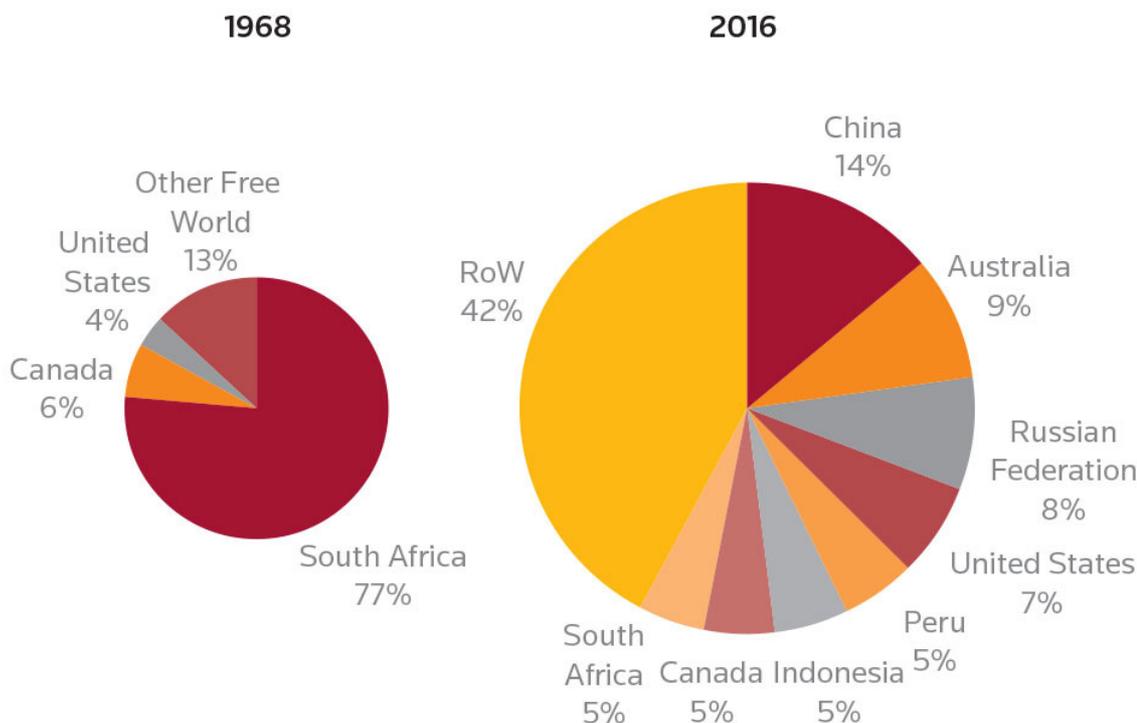
Last month we warned that the **Moody's final downgrade** could take months not weeks and this was confirmed as the rating came through one notch down but still investment grade. Downgrade to sub-investment grade, triggering a big sell off in Government bonds and a drop in the rand is probably a year away.

**Tax ducks turn into turkeys.**

**Why is the rand so strong?** Despite the collapse in the iron ore price (SA's largest export) over the past two months, the rand is virtually unchanged. This is mainly because of the big flow of investment money into Emerging Markets. South Africa then attracts its fair share and the rand remains strong.

### How South Africa has fallen in importance in gold mining

In 1968, South Africa produced 77% of the 'Free World's' gold. Since then, SA's gold has been mined out. Most of the surviving gold is now very deep and very expensive to extract. This has resulted in SA's gold output falling to 5% of the World's total in 2016 – and it should continue to get worse.



### What counts in SA?

What are our biggest exports or sources of foreign exchange?

1. Iron Ore
2. Coal
3. Platinum
4. Cars (but for every car we export there is almost an equal import on the components)
5. Tourism (doing well for us)
6. Diamonds (very erratic)
7. Agricultural exports (suffered due to the drought)
8. Gold

Over the past month we have seen the iron ore price plummet to under \$60. Bear in mind that when Mr. Gordhan got fired it was at \$92. Thus, is it surprising that the rand is not weaker? It is being held up by good inflows from Americans into Emerging Markets. Fortunately, South Africa picks up its share of these flows.

### Moody's downgrades South Africa

Last Friday Moody's dropped our credit rating. It remains one notch above junk but is on a downward watch. This is as we had expected. The bottom line is that they are only likely to downgrade us to junk in a year's time. Then many bond managers will be forced to sell about R150bn of government debt which should cause the rand to fall.

We have been expecting the downgrade for many years. One could see the country moving inexorably towards the cliff for a long time. A few years ago, the government could have taken steps to avoid the problem but did nothing. Now we are afraid that it is almost too late to panic – we are likely to go over the cliff but with the rand currently holding below \$13 we consider it a fine time to invest more offshore.

The South African economy is likely to remain under much pressure. Metal prices should be weak (they were much stronger than we expected in 2016) and the economy (with the exceptions of tourism and agriculture) should remain weak. The government is unlikely to collect as much tax as expected and the country's deficits should remain problematic.

This will result in everybody but the government, getting the blame!

We shall see if President Zuma remains in power after December but we would point out that no one can hold back the tide of the metal prices going out. Times should remain tough for the country for years so please be careful where you invest! Some sectors will suffer further as they are still overpriced!

### Tax ducks turn into turkeys

Some years ago, in a bulletin for clients, PWC wrote: "The moral of the story is – it may look like a duck, it may quack like a duck, it may swim like a duck, but if the Income Tax Act says it's a turkey, then it's a turkey."

### Why is the rand so strong?

We have pointed out that the biggest fundamental influence on the rand is probably the iron ore price.

When President Zuma fired Mr Gordhan, the price of iron ore was about \$92 and the rand was about R12.98. Now the iron price has plunged 30% to below \$60 yet the rand is at R12.84. Why has the rand not fallen?



The first factor is that Emerging Markets, of which South Africa is one, have been attracting massive investment flows. US investors think the dollar and the US markets are peaking so have been diversifying a small part of their portfolios into Europe and Emerging Markets. Bizarrely, the outlook for SA is largely irrelevant (at least in the short term). If SA is 20% of the value of emerging markets, SA attracts 20% of the inflow into Emerging Markets.

Many of these funds are invested into Index funds, which then causes an inflow into SA irrespective of any fundamentals.

This strengthens the rand and improves our local share prices, irrespective of the fundamental outlook for the country (at least in the short-term). Of course, we keep our eyes on the horizon and our investment policy covers the long-term!

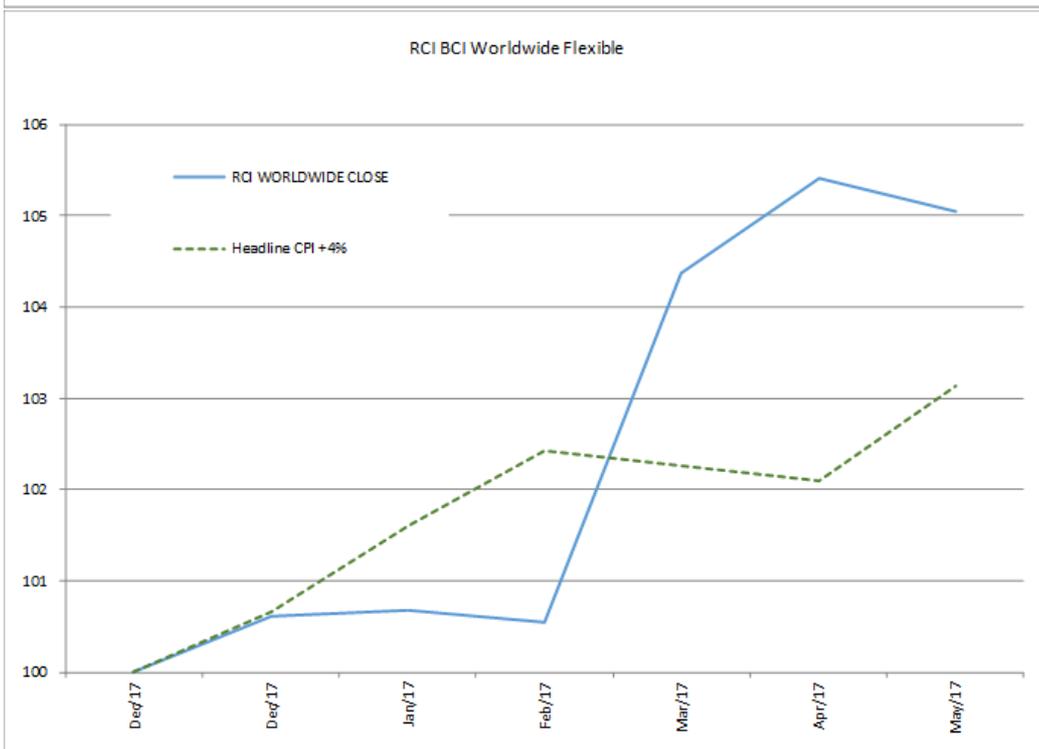
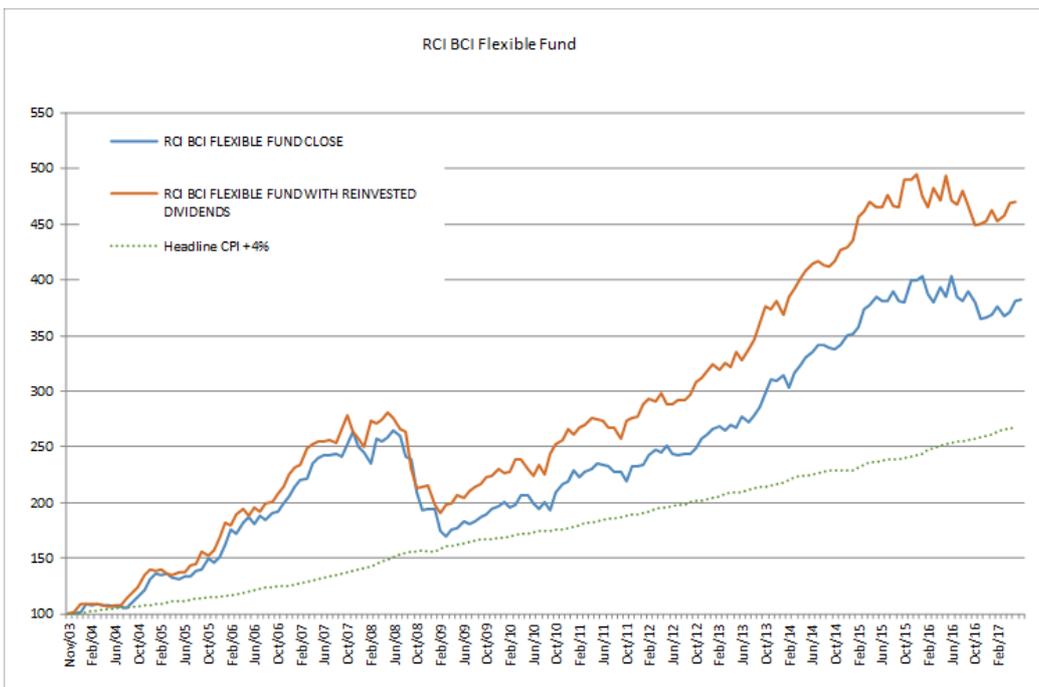
### RCI BCI Flexible Fund

Please contact Maggie on 011 591 0578 for any help on your unit trusts.

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**RCI BCI World Wide Flex** closed May at 105.05c. It is up 5.05% since its launch in December 2016. Much of the short-term performance will be dependent on the outlook for the rand.

We are investing for the long-term in companies that should enjoy reliable growth in earnings and dividends. Sooner or later, this should be translated into good share price growth.



### Unit trust has flexibility – happy to take small amounts

The unit trust has the flexibility to buy and sell shares and to change weightings more frequently than in an individual portfolio. We are happy to take small amounts into the unit trust (from R1 000 per month or lump sums of R25 000). As you will not pay commission to any agents there is no cost to get in and out of our fund. On selling, the amount you receive back will depend on our performance.

Collective Investment Schemes in Securities (Unit Trusts) are generally medium to long term investments. The value of participatory interests (units) may go down as well as up and past performance is not necessarily a guide to the future. Unit trusts are traded at ruling prices and can engage in borrowing and scrip lending. A schedule of fees and charges and maximum commissions is available on request from the company/scheme. Commission and incentives may be paid and if so, would be included in the overall costs. The portfolio is registered under the license of Boutique Collective Investments, a member of the Association for Savings & Investment SA. Forward pricing is used. More details are contained in a fact sheet that is available on request.

### To conclude

Unlike April, May was not a great month for our client's portfolios as the rand strengthened and the numerous rand hedges in which we have invested declined slightly in value.

Naas Botha famously said, "The Currie cup is not won in May." The outlook for the rand remains precarious but this is not a short-term view as anything might happen over a few weeks. Economic fundamentals often take months or years to unwind. We remain steadfastly resolute to invest clients' money with the long-term in mind; to buy great and growing companies that can deliver a steady and growing stream of dividends that will provide the income you require to fund your old age.

We know of no better way than to invest the bulk of your portfolios in companies with high ROCE's (return on capital employed) and then let them compound over several years. Over time, we expect the rand to weaken as the next metal boom is about 15 years away still and South Africa has plenty of political trouble to work through.

We aim to be the best family office in South Africa.

Thank you for being our clients.

Best regards

*Di and Alan*