Robert Cowen Investments

Growing families' wealth since 1982

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Newsletter

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The Family Office

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

"Wisely and slow. They stumble that run fast." ~ *William Shakespeare*

Visit our website: www.rcinv.co.za for back copies of the newsletter, background information, etc.

In August, the rand continued its weakening pattern of the past few months. Why? The threat of the Trade War escalating from President Trump has caused American Investors to sell some of their foreign shares and repatriate some of their funds, causing the dollar to rise against most currencies. Then, the Turkish Lira collapsed, putting pressure on other emerging currencies such as the rand. There is also the risk that South Africa's mineral exports might be under threat.

Over the first three or four months of 2018, the rand had been surprisingly strong and the 'Ramaphoria' had been high. Now things came back to earth and the outlook for South Africa is tough. Our long-term strategy of expecting a tough economy for the next decade or so, and pressure on the rand appears to be correct.

One cannot change long term investment strategies too frequently. Why not? Firstly, it will change the investor's tax profile from long-term capital gains (with a lower tax rate) to a speculator with a higher tax rate. Secondly, because it is impossible to consistently call, with specific accuracy, the geo-political and economic effects of policy changes such as Trade Wars or how long it will take investors to react to such changes. A day, a week, a month? These guesses must be made to enable successful speculation.

You do not have to react quickly to these changes to be a successful investor (as opposed to speculator) for which you need a good plan and steadfast execution. We believe that mainly investing in companies with a high ROCE (Return on Capital Employed) is the most logical starting point.

Seven traits of highly successful fund managers

RCI BCI Flexible Fund had a great month and closed August above 400c after paying a 1.2c dividend on 31st August – it is almost at an all-time high. It rose 6.93% for the month. It ranked 6th out of 78 funds in its category for 2018.

RCI BCI Worldwide Flex closed August at an all-time high of 129.3c and is up to 132c by 5 September. It is flying - as one should expect with a weakening rand. It rose 14.05% for the month! See graphs later in this letter. Ranked 1st out of 71 funds in its category for 2018. As we always say, being in the top quartile takes skill – being first takes luck.

The Trade War between the USA and China

The percentage of American trade with the rest of the world is quite low. America is largely self-sufficient while China exports much of its production. "Chinese exports account for 12% of American goods consumption, which translates into 2.3% of the US CPI basket." The danger is the Chinese exports fall in consequence of which resources importation reduce. This could lead to a drop in demand for resources. This would cause South Africa's exports to further reduce. The trade war is causing emerging markets to fall, aggravated by contagion effect from the declining Turkish market and currency. Many overseas investors tend to tar South Africa with the same brush as other emerging markets. Just as they over-rated us in March, they are probably being too pessimistic on the South African Rand in the short term.

South Africa's perilous economic position

Our country has entered into a recession. The demand for goods and services is consequently suffering. The uncertainty resulting from the threat of land appropriation without compensation and the difficult economic circumstances is causing the country's economy to falter. The rand has collapsed and has dropped further in the first few days of September. When will this turn around? It is difficult to see the silver lining that eventually will come. Just as in April people thought the economy was in recovery and the rand was strong, this difficulty will also pass. South African shares are generally not cheap and we need to drop a further 10 to 20% to restore attractive value. Hence our liking for offshore investments at this time. Sadly, we have warned of this ominous situation for a number of years but take no pleasure in it finally occurring.

Will we have another drought in South Africa in 2018?

We hate to be the bearers of further bad tidings but Business Day's headline of 4 September warns:

That the drought in Cape Town may be over but Johannesburg and the hinterland might face a poor summer rainfall.

"Some experts say there is a 60% - 70% chance that an El Nino effect will hit SA by the summer."

Largest Industries in South Africa

Largest Industries in South Africa	
Finance	20%
Government	18%
Trade	15%
Manufacturing	13%
Transport	9%
Mining	7%
Personal Services	6%
Electricity	4%
Construction	4%
Agriculture	4%
	100%

Stats SA: Sept. 2018

The direct importance of mining to South Africa has dropped right down to 7%, although the indirect importance is substantially higher.

Seven Traits of highly successful investors

Extracted from an article by Michael Pireu in Business Day, mainly quoting Mark Sellers

https://www.businesslive.co.za/bd/opinion/columnists/2018-08-28-michel-pireu-rule-number-one-for-becoming-an-investor-man-know-thyself/

1. Ability to buy shares when others are panicking and selling, plus the ability to sell shares when others are euphoric.
2. Obsession with playing the game. "You can't learn to be obsessive -you are, or you aren't"
3. Willingness to learn from mistakes. "Most of us would rather just move on and ignore the dumb things we have done in the past"
4. Inherent sense of risk.
5. Strong belief in one's convictions
6. Having both sides of your brain working
7. The most important and rarest of all: The ability to live through volatility without changing investment thought strategy. "It is almost impossible for most people to do."

"By the time you reach adulthood, your potential to be an outstanding investor has already been determined – by the way your brain is wired and the experiences you had as a child. That doesn't mean financial education and investing experience aren't important. Those are essential to get you into the game and to just keep playing But, unlike the seven traits, they can be copied."

So, is your fund manager obsessive, opinionated and had an unusual childhood?

We May Be Facing a Textbook Emerging-Market Crisis

This article by Satyajit Das for Bloomberg was quoted in FullerTreacy Money on 4 September 2018.

Total emerging-market borrowing increased from $21 trillion (or 145 percent of GDP) in 2007 to $63 trillion (210 percent of GDP) in 2017. Borrowings by non-financial corporations and households have jumped. Since 2007, the foreign-currency debt – in dollars, euros and yen – of these countries doubled to around $9 trillion. China, India, Indonesia, Malaysia, South Africa, Mexico, Chile, Brazil and some Eastern European countries have foreign-currency debt between 20 percent and 50 percent of GDP.

In all, EM borrowers need to repay or refinance around $1.5 trillion in debt in 2019 and again in 2020. Many are not earning enough to meet these commitments.

Turkey and Argentina have twin deficits (combined budget and current-account gaps as a percentage of GDP) of 8.7 percent and 10.4 percent, respectively, that require financing. Pakistan has a twin deficit well above 10 percent. Brazil, India, Indonesia, South Africa and Ukraine are at or above 5 percent on that basis. In India, if state governments are included the number approaches double figures. Those gauges are rising in China, Malaysia, Mexico, Colombia, Chile and Poland.

Then look at reserve coverage – foreign-exchange holdings divided by 12-month funding needs for the current account, short-term debt maturities and amortization of long-term debt – which measures the capacity to meet immediate foreign-currency obligations. Turkey and Argentina score 0.4 and 0.6 respectively, meaning they can't cover their needs without new borrowings. Pakistan, Ecuador, Poland, Indonesia, Malaysia and South Africa have reserve coverage of less than 1. Chile, Hungary, Colombia, Mexico and India have coverage of less than 2. Brazil and China come in at 2.5 and 3.1 times, respectively.

Even where reserve coverage appears adequate, caution is warranted. Long-term debt becomes short term with the passage of time or an acceleration event. Forex holdings may not be readily accessible. Much of China's $3 trillion of reserves is committed to the Belt and Road infrastructure initiative. The ability to turn U.S. Treasury bonds and other foreign assets into cash is limited by liquidity, price and currency effects. Reserve positions are notoriously opaque: In 1997, the Bank of Thailand was found to have grossly overstated available currency holdings.

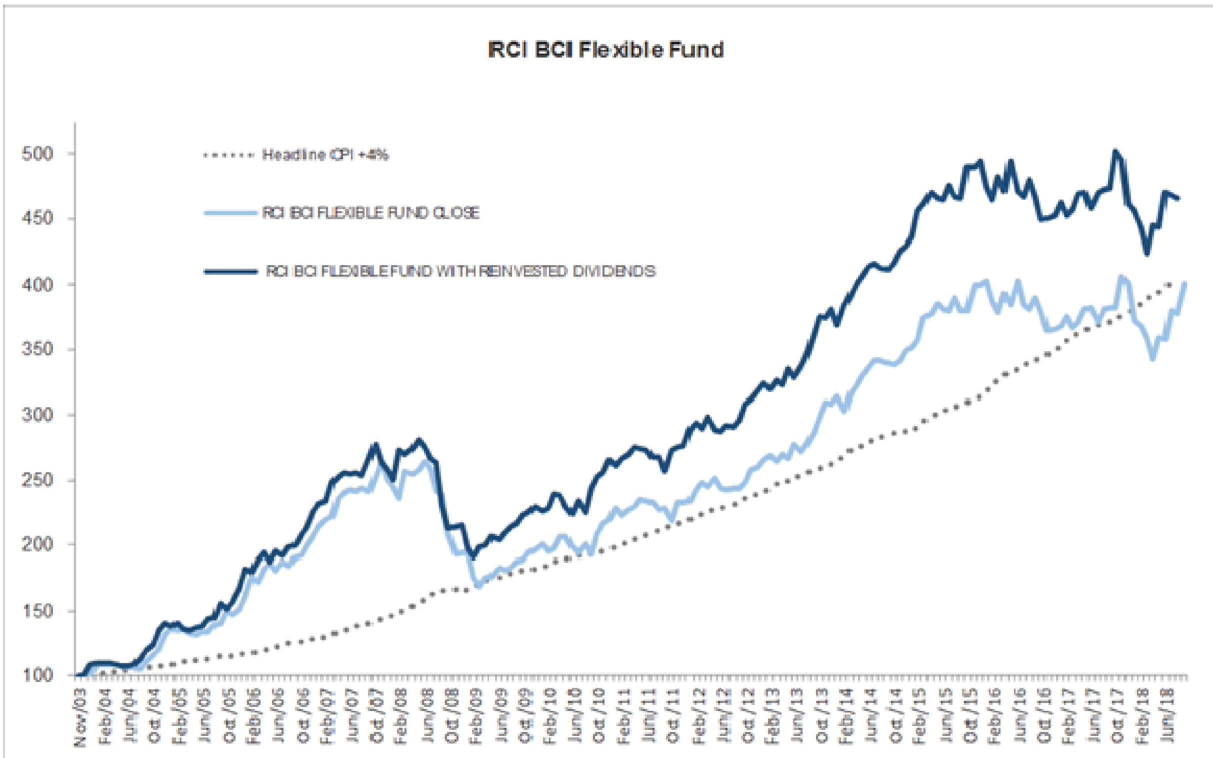
Eoin Treacy's view: Capital is both global and mobile. Quantitative easing programs did not just help to inflate asset prices in the regions the funds originated, but globally. When yields drop in region yield hungry investors are forced to look further afield for returns and emerging markets were a logical choice. That looked like a genius move until the Federal Reserve embarked on quantitative tightening which has reduced the supply of Dollars used to repay that debt.

Editor's Comment: Emerging Markets are normally all tarred by the same brush, irrespective of merit. When the outlook as perceived by the markets changes, things can get ugly! Over the past few years, Emerging Markets were lent too much money. It reminds one of the saying about a banker lending one an umbrella until it starts to rain!

RCI Unit Trusts

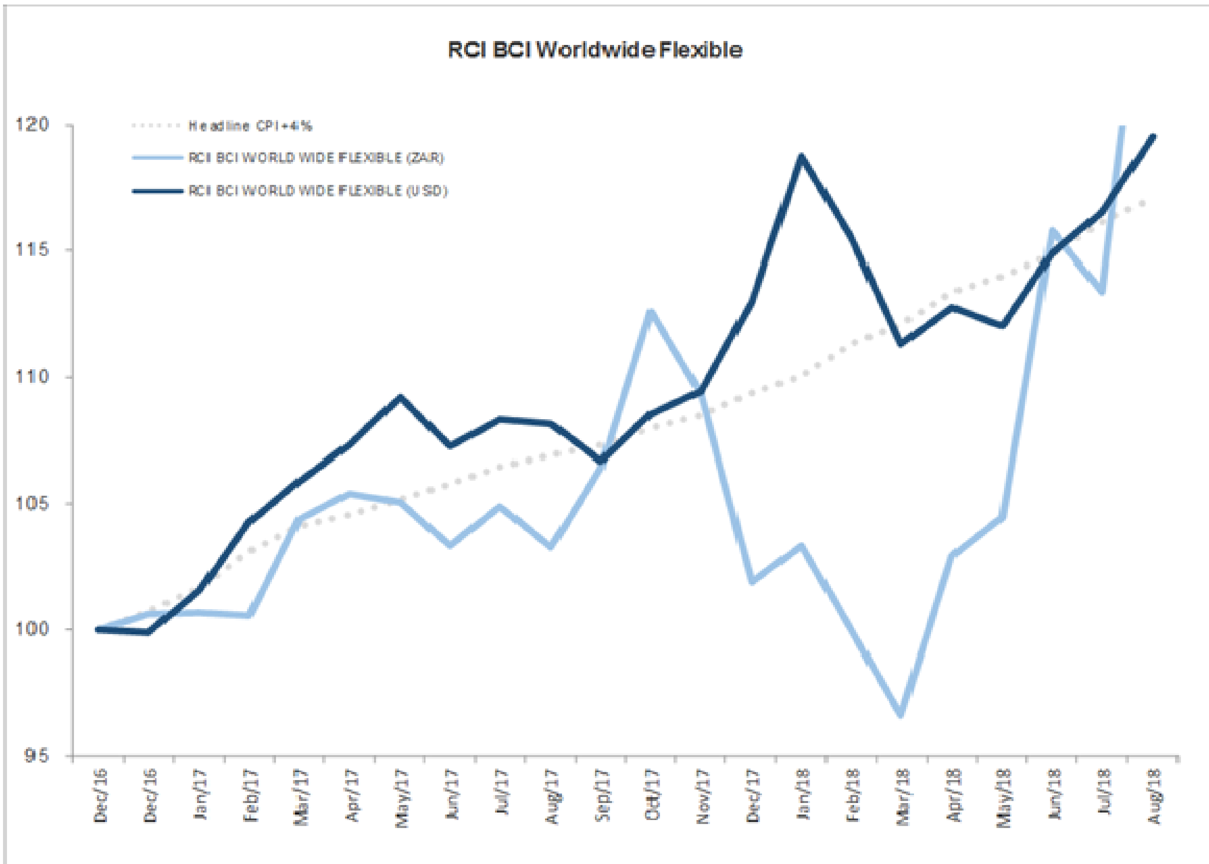
Please contact Maggie on 011 591 0578 for any help on your unit trusts.

RCI BCI Flexible Fund closed August at 400.8c, up 6.93% for the month as it paid a dividend of 1.02c on 31st August. It ranked 6th out of 78 funds in its category for 2018.



We have almost gone back to an all-time high (see the graph below) sadly because, as we had expected, the "Ramaphoria" has worn off and we remain fully invested in the maximum amount of off-shore shares in which we are allowed in this fund. As we have been advising clients, "Live in the sun but invest in the shade." One cannot change a long-term investment strategy from month to month for two main reasons: the tax consequence of the change and, secondly, it is impossible to forecast changes to politics and economics with such precision, let alone the investment public's reaction to such changes. When American share maven Warren Buffett was quizzed why everyone did not follow his "simple" method of investing, he replied that most people wanted to get rich quickly but his method, although so successful, took years so most investors would not follow this strategy.

RCI BCI Worldwide Flex closed August at 129.30c, up 14.05% for the month. This is a substantial all-time high (late note: this unit trusts closed at 132c on the 5th of September. In contrast, the JSE Top 40 was only up by 2.2% during August. The investments in the fund is mainly in foreign companies with very high ROCE (return on capital employed) which has normally resulted in very good long-term returns with low risk. This fund is now 1st in its category of 71 funds for 2018. It has risen 26.93% for the year while the average fund in its category is up 10.76%. As we always say, being in the top quartile takes skill – being first takes luck!



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.

To conclude

August has been a very rewarding month for our clients. It is sad to recognize that this has been achieved because of the drop in the rand. As South Africans we have lived through many trials and tribulations (very few which have come true) and we expect these unpleasant circumstances to continue for a while. However, the sun always rises in the morning and this too will pass. We have invested a lot of our clients' money in offshore shares which are currently performing very well in dollars, and even better in rands. We assure you of the best of our attention.

We hope to be the best family office in the country!

Best regards

Di, Alan and Mike