Robert Cowen Investments

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Newsletter

end May 2018

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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

"You become an expert through repeated exposure to similar patterns."
~ Carl Richards

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

In May, the rand fell 2%. It was down by 7.4% from 31 March to the end of May as the realities of the political and economic realities began to sink in.

The RCI Flexible unit trusts rose again this month and is up some 7% from its bottom on 4 April. The portfolios have risen a similar amount.

The RCI BCI World Wide Fund is up 9.5% from its bottom as the strong dollar performance has been complimented by the weaker rand and it is back to 106c. It rose by 2.48% (in rands) for the month and is up 3.58% for the year-to-date.

On the 1st of June, our new Chief Investment Officer, Mike Gresty, joined us. Give him a week or two to settle in and we will introduce him to you.

Why is the rand weakening?"

"An algorithm could really do better than humans." Daniel Kahneman.

Ramaphosa's New Dawn by JP Landman.

What happens in an internet minute?

Argentina: A warning for South Africa: 9 May 2018 - RW Johnston

Unit trust details.

Conclusion.

Why is the rand weakening?

Why has the rand weakened?

- The dollar is stronger.
- Most Emerging Markets and their currencies are weak. South Africa usually moves in line with these other markets, warranted or not, over the short-term.
- Commodity prices are mostly lower (except for oil, of which South Africa, has none). South Africa's largest export, iron ore, is down from about $76 to $65.
- The threat of a trade war between the USA and China remains.

Where Humans Meet Machines

Daniel Kahneman - "An algorithm could really do better than humans, because it filters out noise. If you present an algorithm the same problem twice, you'll get the same output. That's just not true of people. You can combine humans and machines, provided the machine has the last word! Humans have a lot of valuable inputs; they have impressions, they have judgments."

https://medium.com/mit-initiative-on-the-digital-economy/where-humans-meet-machines-intuition-expertise-and-learning-be639f00bade

Ramaphosa's New Dawn

15 May 2018 by JP Landman for Nedbank Private Wealth. Reprinted with permission

Cyril Ramaphosa was elected President of South Africa on Thursday 15 February. He delivered his first State of the Nation Address (SONA) on 16 February where he declared 'a new dawn'. How much of that new dawn is visible so far? Two caveats are in order:

1 Ministers' budget votes are only now being discussed in Parliament, and that is where most information is divulged. The President pronounces, ministers execute. We thus cannot compile a final tally yet.

2 Also, not all the actions are of equal importance. Fixing state-owned enterprise (SOE) boards or SARS is arguably more important than organising a summit. Even so, we find the preliminary results instructive.

We counted 53 promised actions in the SONA. Of these 11 (21%) have been done, 19 (36%) are in progress, 9 (17%) have not been done yet, and we don't have information on 14 (26%) of them.

THE PRESIDENT'S GOAL WAS TO 'SET THE COUNTRY ON A NEW PATH OF GROWTH, EMPLOYMENT AND TRANSFORMATION'

He explained that 'This will be done by getting social partners in our country to collaborate in building a **social compact** on which we will create drivers of economic recovery.'

The idea of a social compact is a key recommendation of the National Development Plan. It was also a specific undertaking in Ramaphosa's election manifesto. This is a hard and arduous initiative, but in this fractured country a necessary one. It will take a while to tick this one. Progress is unknown.

He stated that **confidence** had to be restored and an investment **downgrade prevented**. Both have been done.

The President also recognised that tough decisions would have to be made to close the **fiscal gap** and stabilise debt. In the National Budget following the SONA, VAT was increased – a tough call indeed. Done.

A major push for the year would be to encourage significant new investment and to this end an **investment summit** would be organised within three months. Four investment ambassadors have been appointed ahead of the summit, which is now expected in the third quarter. In progress.

A **job summit** would be held with the focus on how to grow the economy and make it more productive. Not done.

Government aims to promote investment in key **manufacturing industries** with incentives like special economic zones and a localisation programme where textile, clothing, furniture, rail rolling stock and water meters are designated for local procurement. R57 billion will be spent on local goods. In progress.

Transformation would be pursued through **preferential procurement**, support for **black professionals** and **industrialists**, **competition policy** that opens markets for black entrants, investment in **businesses in townships and rural areas,** and by **dealing decisively** with companies that resist transformation. In progress.

On youth unemployment, the President promised to launch the **Youth Unemployment Service Initiative** that places unemployed youth in paid internships with companies. Together with the participating businesses, the aim is to create one million internships over three years. Done – launched in March, 100 companies signed up. The President also undertook to establish a **youth working group** so that the voices of the youth can be heard. Not done.

On infrastructure, he wanted to **assemble a team** to speed up implementation, with a focus on budgets and monitoring systems. Progress is unknown.

On mining, the President promised that engagements on the **mining charter** would be 'intensified'. Done. He noted an indication by Parliament that the **Minerals Amendment Bill** would be finalised during the first quarter of 2018. Not done.

On small business, four commitments were made: to build (with social partners) a **support ecosystem,** to honour government's undertaking of a **30% set-aside** for small business and co-operatives, to establish a small business and innovation **fund to help start-ups**, and to reduce the **regulatory barrier** for small business. In progress.

The Small Enterprise Finance Agency has launched a programme to help entrepreneurs with **disabilities.** Done.

On tourism, the President undertook to enhance support for **destination marketing** and to take further steps to **reduce regulatory barriers** and **develop emerging businesses**. Progress is unknown.

Regarding science, technology and innovation, he undertook to appoint a **Digital Industrial Revolution Commission** to help position the country, and to finalise the **allocation of spectrum** to build efficient networks. Not done.

The President also signalled that he wanted to appoint a **Presidential Economic Advisory Council**. Not done.

AGRICULTURE, LAND AND EXPROPRIATION

The President undertook to accelerate land reform to bring more producers into the agricultural sector. This accelerated approach will include expropriation without compensation done in a way that increases agricultural production and food security and ensures that the land is returned to those from whom it was taken. He committed government to undertake a process of consultation on how to achieve this. In progress.

TRADE AGREEMENTS

The President noted that negotiations on a **continental free trade agreement** were progressing briskly and he expected an agreement would be concluded soon. The agreement was concluded in March, but government has committed itself to more consultation before tabling it in Parliament. Cabinet has endorsed the Tripartite Free Trade Agreement that covers 26 countries in Eastern and Southern Africa for parliamentary approval. Done.

LABOUR MARKET

The President wanted to introduce a **national minimum wage** on 1 May. Parliament has not concluded its legislative work on this. Not done.

EDUCATION

The President promised details on the financing of fully subsidised **free higher education**. That was done in the subsequent budget speech. Efforts would continue to improve the **outcomes** of public schools. He promised that all outstanding **school infrastructure** projects would be completed by the end of the next fiscal year. Both in progress.

SOCIAL GRANTS

He gave his personal undertaking that there would be **no interruptions in the payment of social grants** on 1 April. Done. The **public sector-led hybrid model** would be developed to pay social grants. In progress.

Recognising the importance of NGOs and community-based organisations in tackling poverty, inequality and related social problems, a **social sector summit** would be convened this year. Progress is unknown.

HEALTH

An additional two million people would be on **antiretroviral treatment** by December 2020 (in progress) and a **cancer campaign** would be launched in three months (not yet done). Certain **NHI projects** would commence in April (unknown) and the **NHI Bill** would be processed through government and submitted to Parliament. In progress.

CRIME

The **Community Policing Strategy** to restore trust in the police as well as the **Youth Crime Prevention Strategy** to involve young people in crime fighting would be launched. A key focus for this year would be the **distribution of personnel and other resources** at police station level. Progress is unknown.

BUILDING A STRONG AND CAPABLE STATE

A process would be initiated to review the **configuration, number and size** of national government departments. Progress is unknown.

A lot of attention was given to **SOEs**, with the promise to intervene decisively to stabilise and revitalise them, saying that action at Eskom was just the beginning. Done.

Steps would be taken to **remove board members from procurement** and work with the Auditor-General to strengthen **external audit** processes. Progress is unknown. The funding model of SOEs would be re-visited. Progress is unknown.

The tide of **corruption** in public institutions would be reversed, promising that the State Capture Commission would commence its work soon. In progress.

Steps would be taken to **stabilise SARS** (done) and a **commission of enquiry** into SARS governance would be established. Not done.

The President promised to **visit every department** to engage with senior leadership and ensure that the work of government is effectively aligned. Progress is unknown.

SO WHAT?

• The most dominant theme in the SONA was the economy, jobs and transformation. More than half of the President's actions fell into that category.

• Building a capable state has the second largest number of actions. There the focus is clearly on turning SOEs and the tide of corruption around.

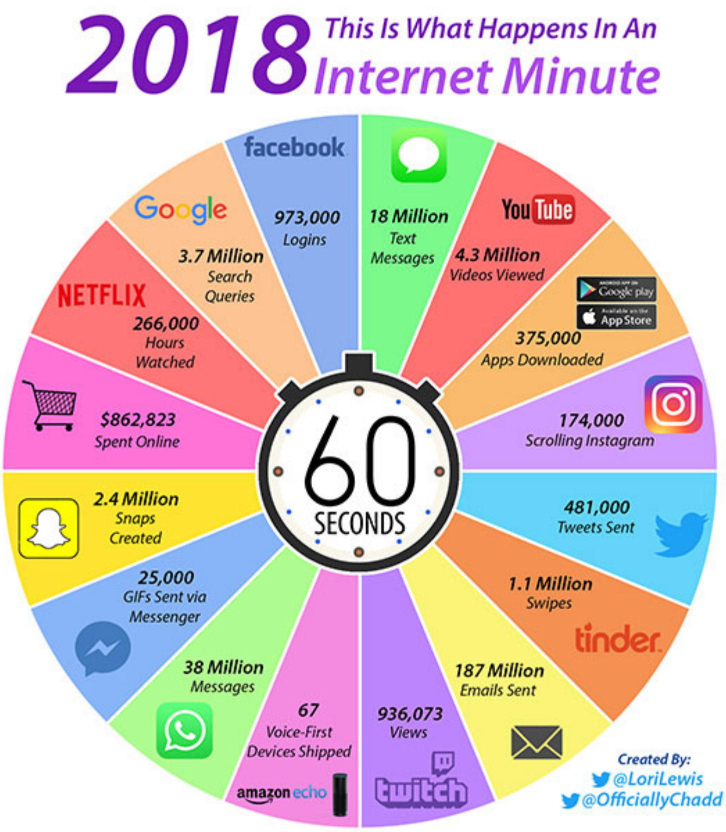
• Education, health and social support make up the balance of his programme.

• A scorecard of 21% 'done' within the first 90 days and 36% 'in progress' is, in my opinion, not bad at all. Even some of the 17% 'not done' will be realised over the coming year, as will many of the 26% on which we do not have information. A solid beginning.

• With clear priorities (which he has spelt out), a strong team (which he has in the critical area of the economy), and decisive action to build a capable state, the scorecard should improve considerably over the remaining 275 days of the year.

• The elephant in the room is of course land and the issue of expropriation without compensation. How he finesses this issue will determine his presidency. The stakes could not be higher.

JP Landman, Political Analyst



Argentina: A warning for South Africa : 9 May 2018

RW Johnston in Politicsweb

How many South Africans are paying much attention to events in Argentina? I can think only of Tony Leon, our former ambassador there. But Argentina could be all our futures and it would be as well to sit up, pay attention and think hard.

Under Presidents Nestor Kirchner and then his widow, Cristina Fernandez de Kirchner, Argentina went on a protracted populist spree with runaway corruption from the top down – very much like our own Zuma period. During that period the government flouted international financial opinion, refused to have anything to do with the World Bank or IMF, paid no attention to its credit downgrades by the ratings agencies and insisted on such financial follies as keeping the national airline, Aerolineas Argentinas, running on non-economic lines.

The government simply refused to face up to the economic damage this was causing, rather like the insouciance of our own rulers as the number of unemployed rose to 9.4 million. (Which ANC leader is willing to remember that in 1994, when the ANC posters read "Jobs,jobs,jobs", unemployment stood at 3.7 million ?) In the Argentinian case the government carried out such pirouettes as banning all imports in some months and systematically falsifying the inflation rate. (In the end international publications like The Economist simply refused to publish the figures provided by the Argentine government.) When it felt like it the Kirchner government would simply expropriate even huge foreign companies like Spain's Repsol (oil) company, with precious little compensation. Nothing was safe.

All good things have to come to an end, as did the rule of Cristina de Kirchner in 2015 when she was defeated by Mauricio Macri, who espoused far more conventional pro-market solutions. He paid off Argentina's bad debts, attempted to throttle back the runaway inflation of the Kirchner era – and published the truth about it. He also attempted to curb wasteful expenditure, to reduce the budget deficit and to bring down the trade deficit. International opinion was ecstatic, just as it has been at the emergence of the Ramaphosa government here. Suddenly it was much easier to sell Argentinian (or South African) bonds and bond rates fell back a bit from the horrific levels of the earlier period. As for Cristina, the only question, as with Zuma, was whether she would go to jail.

At this point, however, the fairy story rather tailed off. Macri's reforms had been based on the hopeful assumption that once Buenos Aires showed that it was a market-rational, indeed market-friendly place, foreign investment would flood in, lifting all boats and inaugurating a happy new period of economic growth. After all, Argentina is the world's eighth biggest country and has enormous natural resources. That would have been just the happy ending that we all like. However, it left one or two things out of account. First, investors had been badly bitten and were not twice but many times shy. They were willing to risk investment in Argentinian bonds and shares (which they could sell the next week) but they were hardly willing to invest any long term money into factories, farms or even real estate. Investors hadn't forgotten Repsol and things like that took a lot of getting over. And, after all, there were lots of investment opportunities in markets where such risks were unthinkable.

Secondly, developing countries like South Africa and Argentina had benefited enormously from the "quantitative easing" (QE) policies of the US and EU central banks since the 2007/8 crisis. This inaugurated ten years of very low interest rates, enabling debtor countries like South Africa to fund their deficits far more cheaply than would normally have been the case. But now that QE policies were ending at last, US and EU interest rates were rising with dramatic results for emerging market currencies and interest rates. There was no point bemoaning this. Like the weather, it was beyond anyone's control.

The unhappy result in Argentina was a sharp drop in the peso, a rise in interest rates to 40% and finally a desperate plea to the IMF to shore things up with a $30bn. loan.

This is the context within which we should view the warning by the Treasury's Director-General, Dondo Magajane that SA is still at risk of becoming a failed state and the accompanying warning by Deputy Finance Minister Mondli Gungubele that "we dare not relax and allow the things that took our country to the precipice to prevail". For the truth is that we are facing a situation every bit as difficult as Argentina – and just as likely to end in a desperate appeal to the IMF.

At present publications like Business Day are happily congratulating President Ramaphosa on having made a few board changes at Eskom and suggesting that with a bit of luck we should now see some recovery. This is grossly irresponsible. The Eskom board still includes some obviously ridiculous figures and in any case the real question is when will that board face up to the urgent necessity for it to lay off some Eskom staff, decree a pay freeze for the rest, and sell off at least some of its power stations? For Eskom owes $35 bn. which it cannot possibly pay and which the government can't afford to pay either. If the DA was truly a responsible Opposition it would be speaking out loudly now about what this implies.

Similarly, we currently see debate as to whether public servants should get an increase equal to inflation (as the government would like) or inflation +++, as the unions are demanding. This simply disregards the repeated IMF finding that our public service is enormously overpaid and over-large in comparison to all our peers. The truth is that we need to impose a multi-year wage freeze, as was done in developed countries like the UK after the financial crisis. Not just the unions but the government too is living in fairyland. And the Opposition says nothing.

However, the biggest sortie into fairyland is Ramaphosa's absurd crusade for $100bn. of foreign investment. This appears to be based on the same happy assumption as in Argentina that since we have all sorts of resources the rest of the world is just yearning to pour money in once we tell them that we're "open for business" again. This despite a years-long investment strike, the huge capital flight from South Africa, the abrogation of all the investment -protection treaties and the latest mantra of expropriation without compensation. To believe that one can really expect a flood of foreign (or even domestic) investment under such conditions one has to believe not just in fairies at the bottom of the garden but that Father Christmas is shipping them in in flying saucers. Yet this ridiculous initiative is treated with grave respect by the Opposition and the media. Apparently everyone believes in fairies, Father Christmas and flying saucers.

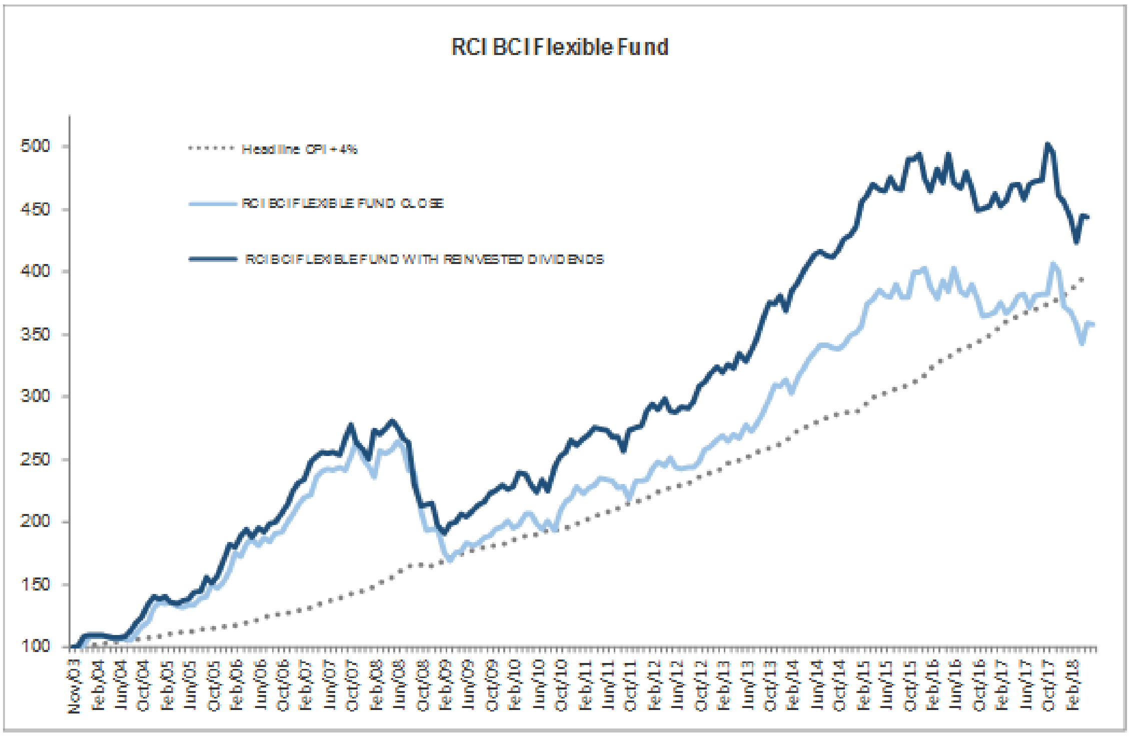
One understands why Ramaphosa wants the country to live a little longer in Dreamland before the next election (though that is no excuse for the likes of Business Day or the DA to be also so fast asleep). The reality, as with Argentina, is that all this desperate wishfulness ends, inevitably, with a humiliating recognition of reality – and a desperate rush to the IMF.

RW Johnson

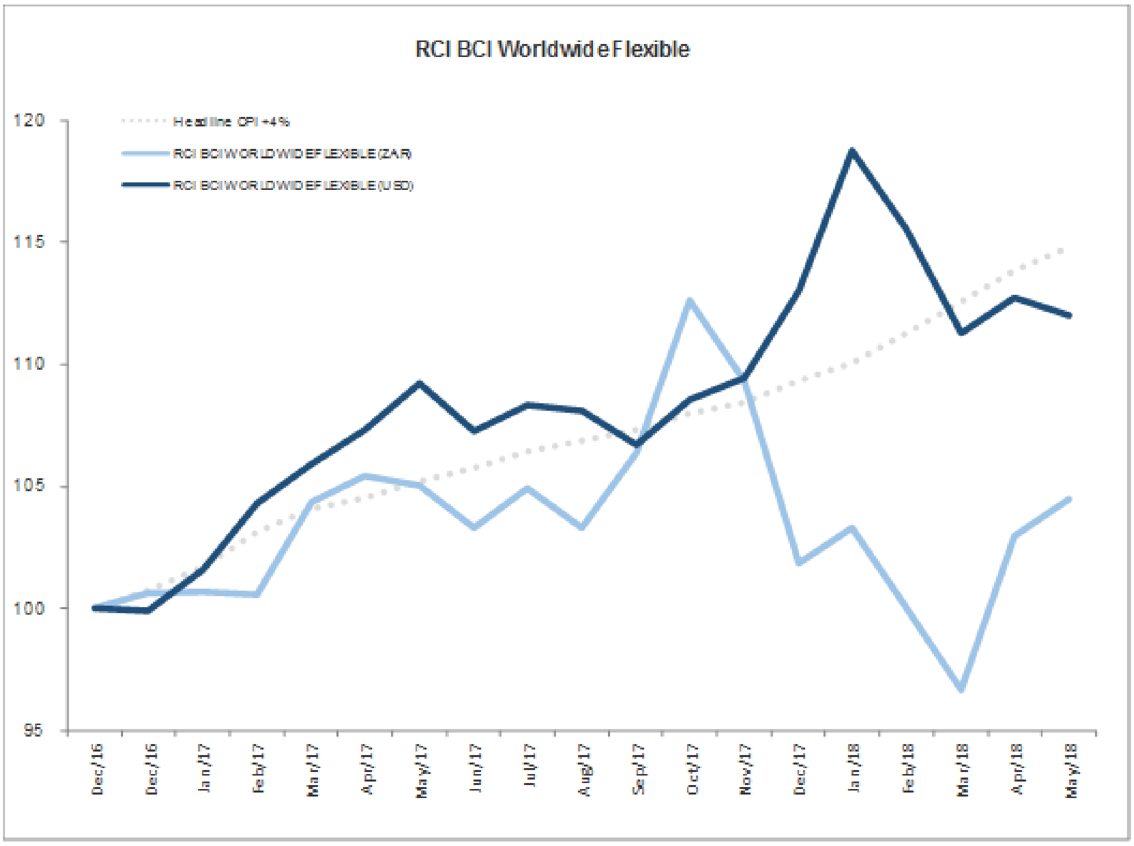
RCI Unit Trusts

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

RCI BCI Flexible Fund closed May at 358.32c, down 0.37% for the month. The JSE Top 40 was down by 3.2% for the month.



RCI BCI Worldwide Flex closed May at 104.46c, up 1.4% for the month. In contrast, the JSE Top 40 fell by 3.2% during May. The investments in the fund are mainly in foreign companies with very high ROCE (return on capital employed) which has normally resulted in fantastic returns with low risk investments. The performance in dollars remains good (which is what we focus on) so the weaker rand has resulted in good growth when measured in rands.



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

Some of your children or grandchildren probably watch “Game of Thrones” on DSTV. In this imaginary world, the summer and winter seasons are each seven years long! On the Highveld, winter has definitely arrived and our thoughts turn to cuddling up snuggly!

As the winter will surely pass, (and it will last only another 2.5 months, not seven years) so too, will this investment cycle. We are concentrating on holding or buying great long- term companies with growing dividend streams. If most of your drawings are funded by reliable dividend streams, share price fluctuations become largely irrelevant. Already, over the past two months, we have seen the over-reaction to the election of President Ramaphosa start to abate.

The appointment of Mike Gresty to RCI, ensures good long-term continuity to both our business and, more importantly, to your portfolios. We expect Mike to make a huge contribution over many years.

Thank you for being our clients.

Best regards

Di and Alan