Sterling Times

December 2022 Edition

In this edition

MERCHANT WEST

STERLING PRIVATE WEALTH

Introductory message from our Managing Director

By Graydon Morris, Managing Director, Sterling Private Wealth

Dear valued clients and friends

We are nearly at the end of 2022. It's been quite a year. Again.

What lies in store for 2023? The view of US Business and banking leaders is that we are in a for a trying time, still. More volatility and uncertainty are expected.

To some extent, when this environment is expected, as it is, it lessens the risk of complacency and speculation, a key feature of the last decade of excessive liquidity.

What can be said, without question, is that global market equity valuations, and indeed capital market valuations, have normalised materially in the year. This is healthy and sets a base for improved returns and conditions in future.

Our clients have weathered the storm very well during the year. US and Global markets are down -18% in US$, as I write. The Emerging Market index is down -20% and the Rand has weakened against the US$ by -7% or so, alongside the GBP and the Euro. Dollar strength has prevailed.

Many of our global investors have been protected by the stellar alpha added by select value managers in the global context, who have performed very well, with low single digit declines in US$.

As a ZAR investor, of course, one has been shielded somewhat against this global correction and portfolios are very robust. The SA equity market has been very resilient in this context, up nearly 5%. Diversity is key. The proverbial free lunch. Those in balanced portfolios with reasonable SA allocations have fared very well, under the circumstances.

Global inflation is a headache, though, and we have shared a Visual Capitalist Slide in this Report, showing global inflation by Country, that will be very revealing and fascinating.

We have also shared a piece, again, by Joe Wiggins, discussing the importance of carefully considering one's view when selecting active managers. There are a few boxes one needs to tick to ensure an optimal outcome, and Joe hones in on these brilliantly.

Our old friend Sean Peche also shares a note on the dangers of the Crypto world and the recent implosion of FTX. Don't say we never warned you!

As South Africans we are being battered by the continuing electricity crisis and political showdowns. Its unnerving and disheartening but us "Saffer's" are made of stern stuff. Cool investment heads, and a belief that the future can be better, are needed.

As advisors, we take on the frustrations, concerns, and anxiety our clients feel. We are here to make sense of the investment world in this context and map out a path that keeps investors safe against longevity risk and a focus on the preservation of real capital.

We have a shared a few thoughts and pieces here that we think will resonate with you.

We wish to all a safe and blessed and happy holiday season and cannot wait to connect in the New Year with you, after a good break. We are eternally grateful that each and everyone one of you chose to deal with us. It is our privilege and a role we take very seriously.

We hope you enjoy the read.

Graydon Morris

Managing Director

Three Questions to Answer Before Investing in an Active Fund

BY JOE WIGGINS

There are still too many people investing in active funds. Not because they are unnecessary, but because owning them comes with a unique set of behavioural challenges that we are often unprepared for. If we are to have any hope of benefitting from holding them, we must accept and embrace these. The worst – and all too common – scenario is investing in active funds whilst holding entirely unrealistic expectations about the realities of doing so. This dooms us to almost inevitable failure and disappointment. Before investing in active funds there are three questions we need to answer:

– Am I willing to own a fund for the long-term?

– Can I discount short-term performance?

– Can I withstand long periods of underperformance?

Let's take these in turn:

Am I investing for the long-term?

As the investment industry has become increasingly myopic, I have had to moderate my view on what the long-term is because it seems too outlandish. I have heard people discuss the long-term as three years or more, but this is far too short – it is much closer to 10 years. The longer our time horizon, the greater the odds of investment success. Why is an extended time horizon so important? Because the shorter it is, the more our results are beholden to randomness and fickle swings in market sentiment. If we believe there is a strategy with an edge, we must give it time to play out, for fundamentals to exert themselves over noise. This does not mean that we must persist with an active fund whatever happens or that simply increasing our time horizon guarantees better results, but it at least gives us a fighting chance.

Can I discount short-term performance?

It is one thing to say that we are willing to own a fund for the long-term, doing it is another thing entirely. The biggest impediment to long-term investing is obsessing over short-term performance. Not only is it an entirely fruitless activity that sees us attempt to read patterns in the chaotic fluctuations of financial markets, but we persistently make poor decisions based on such fleeting observations. Each time we check performance, write a report or hold a meeting we are creating a decision point; another opportunity to make a near-sighted judgment. We need to be realistic about our situation – if the short-term matters (whether we want it to or not) active funds really should not be for us – it will simply mean constant anxiety and frequently poor choices.

Can I withstand long periods of underperformance?

Although incredibly damaging, the hardest part of active fund investing is not the senseless fascination with short-term performance, but the prolonged and painful periods of underperformance that are an inevitable feature of any active strategy. All skilful (and unskilful) active fund managers will go through years of underperformance – this is inescapable. Living though this on a day-by-day basis is exhausting and exacting. The doubts about the strategy – whether the manager has lost her edge, whether the process is broken or the market environment irrecoverably changed – will often be overwhelming. Yet if we want to successfully invest in active funds then we need to find a way to withstand them. The alternative is believing that we can time our investment into active funds so that we capture the good times and avoid the bad (we can't).

The problem with this required fortitude is that it is music to the ears of the unskilled active fund manager who will be delighted if we persist in investing with them despite their lack of ability, but this is the job of the active fund investor – to identify skill without relying on past performance. If we cannot tolerate lengthy spells of poor relative returns, we should not be investing in active funds.

If we answer these three questions in the affirmative, it does not mean that we should invest in active funds; these are simply the minimum entry requirements before we even consider attempting it. If we answer any of them negatively, we really should not be doing it at all. None of these features are easy to deal with or manage, in fact the behavioural aspects of active fund investing are just as tough as finding a manager or strategy with an edge. Far too many investors neglect this and leave themselves in a position where the odds of success become vanishingly small.

Understanding the Generational View

BY JOUBERT STRYDOM, DIRECTOR STERLING PRIVATE WEALTH

“I spent an hour in the bank with my dad, as he had to transfer some money. I couldn't resist myself and asked...

"Dad, why don't we activate your internet banking?"

"Why would I do that?" He asked...

"Well, then you wont have to spend an hour here for things like transfer.

You can even do your shopping online. Everything will be so easy!"

I was so excited about initiating him into the world of Net banking.

He asked "If I do that, I wont have to step out of the house?

"Yes, yes"! I said. I told him how even groceries can be delivered at the door now and how Amazon delivers everything!

His answer left me tongue-tied.

He said "Since I entered this bank today, I have met four of my friends, I have chatted a while with the staff who know me very well by now.

You know I am alone...this is the company that I need. I like to get ready and come to the bank. I have enough time, it is the physical touch that I crave.

Two years back I got sick, The store owner from whom I buy fruits, came to see me and sat by my bedside and cried.

When your Mom fell down a few days back while on her morning walk. Our local grocer saw her and immediately got his car to rush her home as he knows where I live.

Would I have that 'human' touch if everything became online?

Why would I want everything delivered to me and force me to interact with just my computer?

I like to know the person that I'm dealing with and not just the 'seller'. It creates bonds of relationships.

Does Amazon deliver all this as well?'"

Technology isn't life.

Spend time with people ... Not with devices."

16 MONEY RULES EVERYONE SHOULD LEARN BY 25

1. **Pay yourself first**

   As soon as you get paid, put money into savings. Automating this is even better.

2. **Keep a 6-month Emergency Fund**

   If you have multiple streams of income, you can go as low as 3 months.
   If starting out on your own, you could need as much as 12 months.

3. **Budget using the 50/30/20 Rule**

   - 50% for needs
   - 30% for wants
   - 20% towards saving/investing

4. **Divide your bonus into thirds**

   - 1/3rd for fun
   - 1/3rd for retirement
   - 1/3rd for debt paydown (add to retirement if only low-interest debt)

5. **Put all, or a large percentage, of your raises into saving and investing**

   This helps avoid lifestyle inflation and moves up your retirement date.

6. **Avoid high-interest debt**

   It's a wealth destroyer, pay off all debt as fast as possible.

7. **Your home payment**

   (Mortgage, Interest, insurance) should cost less than 25% of your monthly income.

8. **When buying a car use the 20/4/10 Rule if you must**

   - 20% down
   - 4-year loan
   - < 10% of your monthly income

9. **You should save at least 15%** of your income for retirement, **from when you start working!**

10. **Your age subtracted from 100** represents the percentage of stocks you should have in your portfolio. Some are now using the number 120.

11. **The local stock market** has a long-term average real return of 7%. (100 years historic, not the last 5 years!)
    To calculate your returns, it's common to use 12% to capture the effect of inflation.

12. **The rule of 72** tells you how long it will take your investment to double.
    Example: The stock market returns 10%, so 72/10 = 7.2 years to double your money.

13. **The 4-percent rule** says you can reasonably safely withdraw 4% of your starting investment balance each year (adjust for inflation in subsequent years) and not run out of money.

14. **Your Net Worth** should be equal to your age x Pre-Tax Income /10.
    Example: if you are 35 years old and R 500 000 in annual income, then your net worth should be R 1 750 000 (35 x 500000 / 10)

15. **Have at least five times** your gross salary in life insurance or group life insurance. This is very NAV dependant, you may need more.

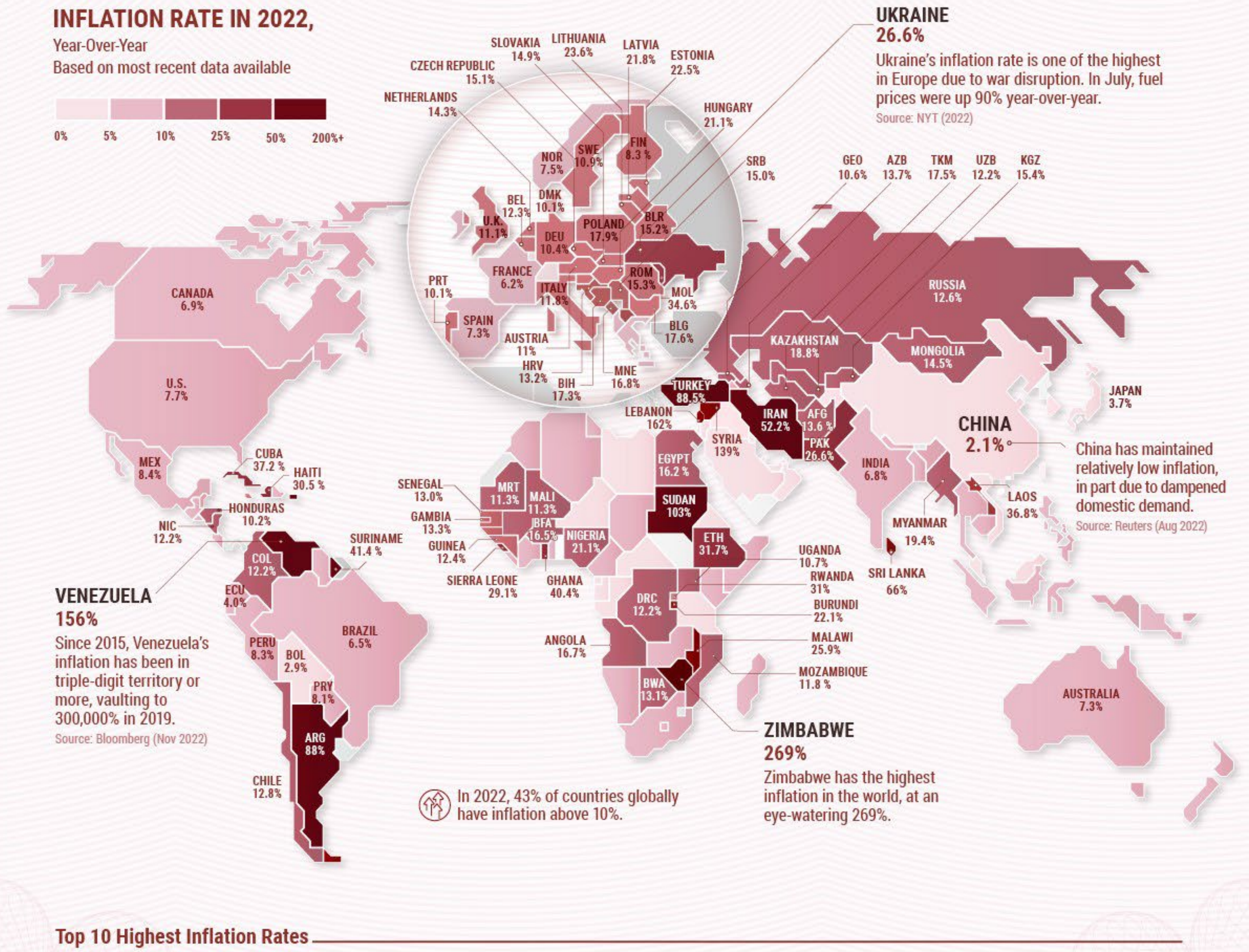
16. **Before spending money,** wait 24 hours and ask: do I still want it? If you do, go ahead, and buy it. This will save you from a lot of impulse purchases.

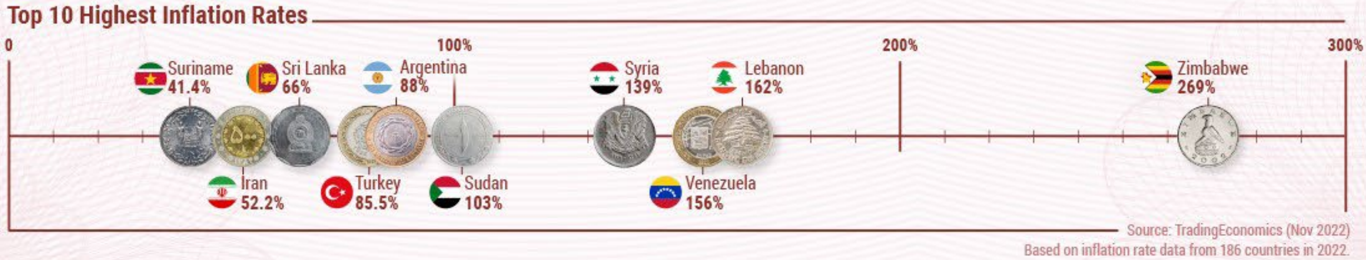
DOUBLE-DIGIT INFLATION

IN ALMOST HALF THE WORLD

Today, many countries around the world are experiencing double—or even triple—digit inflation.

Here are the countries with the highest inflation rates globally as soaring energy prices are driving up the cost of living.





The Slide below from Coronation shows just how cheap the SA equity market may well be. Does it remind you of 2001-2002? From 1 January 2002 until 31 December 2007 the JSE returned 338%! In six years.

It had returned 77% in the previous six years.

Ranking table of valuations and divis

Counter	Market Cap (Rm)	Spot	Divi Yield (f)	5YR divis as a % of Mcap
TGA	36,473	26,757	60.4%	143.4%
IMP	162,215	19,024	15.9%	71.0%
SOL	180,786	28,500	11.6%	70.5%
RBP	42,943	14,791	15.7%	66.8%
HMN	19,024	413	8.2%	64.0%
KIO	117,329	36,428	16.1%	59.2%
EXX	71,831	20,564	14.3%	58.0%
LEW	2,886	4,861	8.6%	57.6%
GLN	1,405,431	10,849	11.0%	53.3%
SUR	1,884	2,070	8.6%	52.5%
PAN	6,765	353	5.5%	51.2%
AFE	9,732	9,223	7.2%	50.4%
ARL	7,679	17,890	7.8%	50.0%
OMU	48,545	1,031	7.6%	48.5%
SSW	122,238	4,319	8.8%	48.5%
AMS	388,258	146,351	10.0%	47.6%
TSG	12,077	1,150	4.3%	46.6%
NED	110,546	21,612	6.8%	45.1%
SBK	286,447	17,069	6.5%	45.1%
N91	27,302	4,385	6.2%	44.5%
JSE	9,071	10,441	7.9%	43.2%
TRU	21,491	5,261	8.2%	42.3%
SLM	118,230	5,309	6.5%	41.3%
AVI	25,045	7,442	6.9%	41.0%

By Sean Peche, Ranmore Fund Managers

“Bitcoin got fried”, a title in today’s FT, would have gone over my head 24 hrs ago

I’d never heard of Sam Bankman-Fried & might have guessed "FTX" was a sports car brand extension

My 2022 surprise list a year ago was for Bitcoin to fall 50% to $25k so the collapse doesn’t surprise me (see link in comments)

What DOES surprise me, is the spreadsheets of once reputable investors - SoftBank, Sequoia, Ontario Teachers' Pension Plan Board, & Tiger Global thought 300 employees in the Bahamas was worth $32bn, only 10 mths ago

But they’re “disruptors”

Yes, "disrupting" those poor teachers' retirement plans..

Even the editor of, The Block, thought it impressive – tweeting “FTX…nabs $32bn valuation, worth more than Credit Suisse, Deutchebank & Nasdaq”

“Nab" – "verb / informal / take, grab or steal”

FTX proudly tweeted: "They may have 47,000 employees, but we have 1 Gary"

Who’s Gary? I wondered

Maybe "About Us" would tell me

An “All-Star team” – "built by traders for traders”

Not built for investors, that’s for sure - except short sellers…

and seemingly more of a Supernova

But while up in space, in what galaxy did these spreadsheets kick out a $32bn valuation?

even with “1 Gary”

Who was too busy staring at monitors for any photo shoots but studied at MIT & worked at Google aggregating flight prices - well he should definitely cancel any flights to the US until they find that $8bn..

Those “investors” can’t have used a DCF model - there was none!

Clue? They’d raised cash only 4 months earlier!

And who answered the Finance questions during their fundraisings because their “All-Star” team doesn’t list a CFO?

Show me a charismatic CEO & a weak/absent CFO, and I’ll show you a short-selling candidate because there’s only one person driving any journal entries, and it’s not the CFO

Not that I find Sam very charismatic, but what do I know?

other than he's the “Son of two Stanford Professors”?

How does anyone know that & who cares what anyone's parents do for a living?

It can’t be COO, Constance, because her LinkedIn profile reads, “primarily responsible for global user growth, PR & marketing, institutional clients servicing and operational procedure” (sp)

well, that "procedure" clearly wasn't focused on liquidity!

Perhaps there was no CFO because my search revealed you can get a Digital Asset Business license in Antigua within 3-4 months for $100k of capital. And you don’t even need an audit…

Ah ha!

The “millennial portfolio” of 50% Tesla + 50% bitcoin is down 57% this year

But I fear there's lots more pain ahead for tech as this BTC & VC fallout plays out

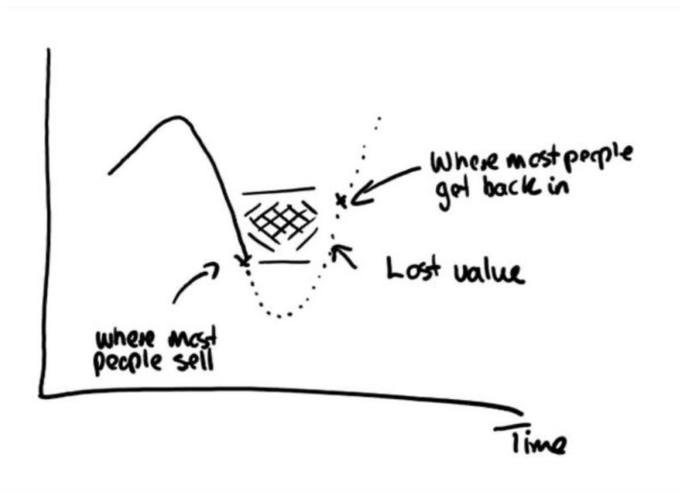
Ranmore has created wealth by buying decent businesses at decent valuations with sensible management who are on our side. Our margin of safety requirement means we focus on the downside - very important these days!

And we don't do FOMO

You can try catch the (All) stars

but please remember…

some stars explode.

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