

# SA investors incurred a 3.5% behaviour tax in 2021, says Momentum report

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In a year where movement restrictions and lockdowns have resulted in increased savings rates around the world, with South Africa's savings rate having escalated by nearly 22% from levels of less than 15% of gross domestic product (GDP) in 2019 to more than 18% in June 2021, rising levels of uncertainty have pushed investors to seek more control of their savings.

According to Momentum Investments' latest Sci-Fi report, this shows that the behavioural patterns of South African investors became more palpable in 2021 as a record number of investment switches were processed.

The report measured investor behavioural patterns on the Momentum Wealth platform for the 2021 period. By analysing the behaviour of over 9 000 investors during this period, it was found that active investors (defined as investors performing switch transactions) increased by 80% and the number of switches by 50% to a record-high level of 27 994.

On average, investors were chasing past performance and up-risking their investment portfolios from October 2020 to April 2021. This reversed dramatically as the South African volatility index spiked and investors switched to worse-

performing funds, down-risking their investments. This resulted in an annualised behaviour tax of 3.5% for investors in 2021, amounting to over R90m.

The report also found that the high number of switches in September 2020 and November 2020 correlate strongly with high market volatility as per the South African Volatility Index (Savi). Head of Behavioural Finances at Momentum Investments, Paul Nixon, says, "As the Savi stabilises at lower levels, switch activity seems to reduce as well. Sudden spikes in the Savi, as seen occurring in March and June 2021, does not seem to influence switching activity as much as prolonged periods of high volatility."

"Clearly, we all struggle to bridge our intentions and our actions. It is clear that investors have become more engaged with their investments and, in doing so, incurred an annualised behaviour tax of 3.5% for 2021," he adds.

Shifting investments around during market volatility usually results in a behaviour tax. Behaviour tax is

calculated as the difference in future performance between the funds switched from and the funds switched to. Overall, the rand value lost over the 2021 period analysed in this report was over R90m, which equated to an annualised behavioural tax of 3.5%.

"This essentially explains why following our gut instincts when investing does not always serve us well," says Nixon.

The 2021 Sci-Fi report goes on to unpack the complexities of the 2020/2021 investment shifting behaviour. Momentum Investments Research Analyst Prof. Evan Gilbert says, "The findings support the need for effective short-term risk management among investors.

"This initial study shows that the switching decision of South African investors is not a simple, linear response to poor investment returns. There are several potentially rich alternatives to explore. To do so properly will require a model that includes all of these in an integrated fashion."

The final section of the report deals with the investor behavioural archetypes that Momentum Investments observed in a previous white paper titled *Understanding the great forces that rule the world: A study on South African investor behaviour*.

By categorising switches based on the level of past relative performance, changes in the risk profile of the switched funds, and switching frequency and average asset allocation, Momentum Investments was able to identify groups of investors with similar switching behaviour. With further investigation into the general behaviour exhibited by each of these clusters, four investor archetypes were identified, which include: the avoider, the anxious, the assertive, and the market timer.

As expected, market timers (those who always try to beat the market) were the most active archetype during the period of analysis. Even though they made up the smallest portion of active investors, they made the most switch transactions. Market Timers realised the largest

behaviour tax with an average of 5% per year of the switch amount lost.

As part of its conclusion, the report said the year 2021 was a period that saw increased engagement between investors and their portfolios. This was reflected by the 80% increase in the number of active investors and a 50% increase in the number of switch transactions. On closer investigation, there was overall an increase in the risk appetite of investors as investment flows climbed the risk spectrum from cash to more stable and balanced strategies. Another trend was the flow of funds offshore, which correlated particularly well with the extremely strong rand performance earlier in 2021.

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"This report sets the scene for using psychometric data (the development of a South African financial personality assessment) in hyper-personalised nudging strategies as Momentum Investments enhances our capability to focus on target behaviours," says Nixon. Nudging or positive reinforcement and indirect suggestions are ways to influence groups or individuals' behaviour and decision-making.

"Momentum Investments, however, is most certainly aiming to use nudging techniques to communicate with the different segments with the right message at the right time to deliver better client outcomes and to help investors on their journey to success. This is the next level in making investments truly personal," concludes Nixon.

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