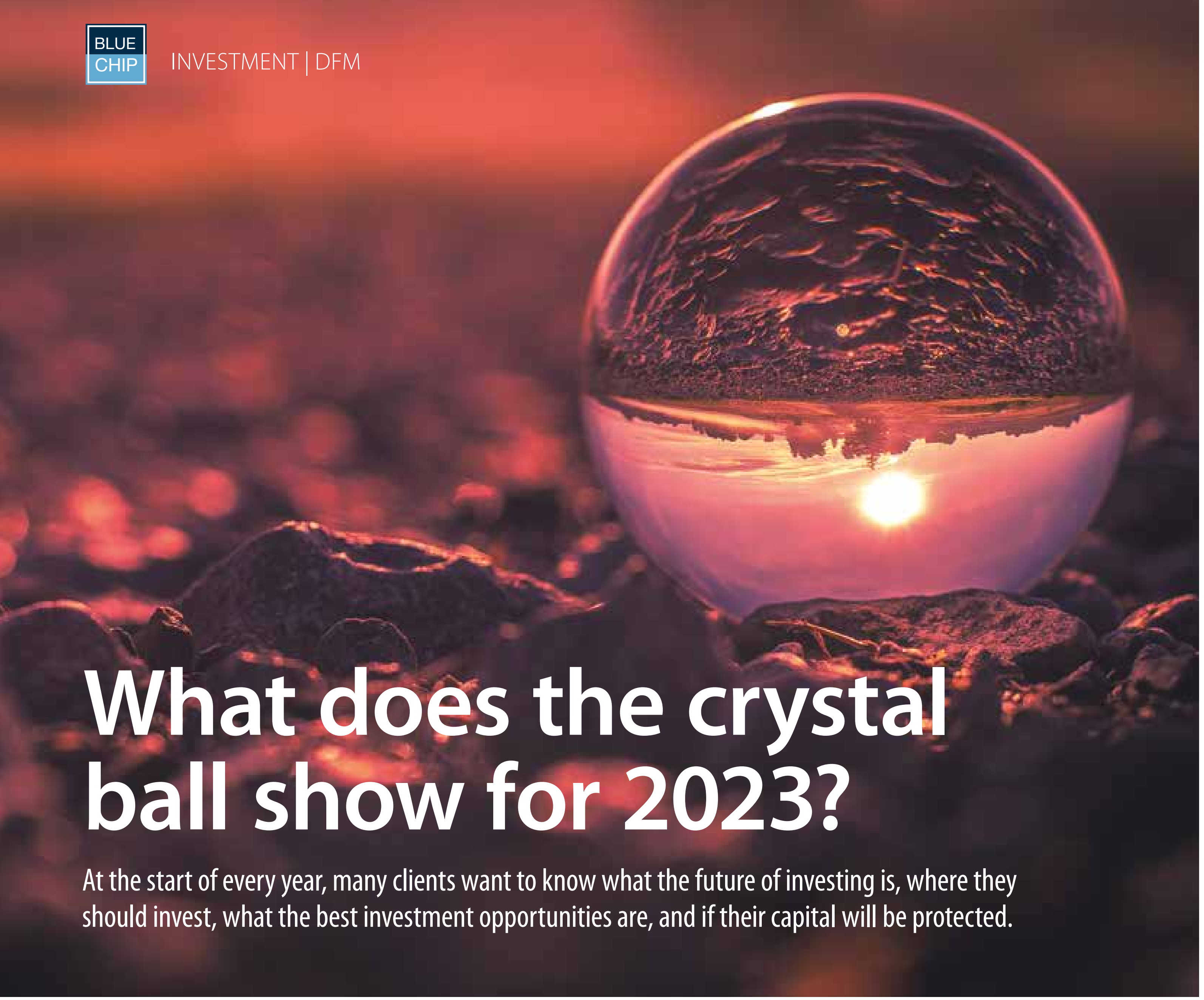

What does the crystal ball show for 2023?

At the start of every year, many clients want to know what the future of investing is, where they should invest, what the best investment opportunities are, and if their capital will be protected.

The first question is easy to answer. The basic definition of investing is where one party is providing capital to another in exchange for some sort of return on the capital provided. Based on this definition, the essence of investing will be no different in the future than in the past.

However, it would be naive to assume that investment opportunities and market dynamics will remain the same in the future. In the last decade, for example, we had growth in technology shares, growth in infrastructure investing and the emergence of cryptocurrencies. Certain investment opportunities may also fall out of favour. A recent example is mortgage-backed securities, which all but disappeared after the 2008 global financial crisis. Market conditions will definitely not stay the same and we can already see the shift from the last decade's ultra-accommodating monetary policies toward a normalisation of global interest rates.

The way we invest will most likely also change. The shift from the open outcry system on trading floors to electronic trading to online trading over the last 30 years has not only drastically impacted the way we invest, but also who can invest. Today almost anybody can trade from anywhere in the world, which has drastically changed the demographics of market participants.

As we move to the more difficult question of where to invest, we first need to look to the past for some lessons. Going only a year back and assuming we have no knowledge about 2022, we were all sitting with a Covid hangover, but we were mostly optimistic about the future given that most lockdowns were lifted, and global economic activity was almost back at full capacity. We were told the structural reforms in China were necessary and most of it was priced in the market. Inflation was starting to rise, but we were also told not to fear since it should be temporary given that supply chain disruptions and pent-up demand would be resolved soon.

How wrong were we?

The first blow to our optimism was the discovery of the new Omicron variant by South African scientists in November 2021. We were looking forward to the first festive season with no Covid restrictions since 2019, but unfortunately global governments "punished" South Africa by re-enforcing travel restrictions on us.

The year 2022 continued to deliver hits with a dramatic fall in the "untouchable" global tech share prices in January, the Russian invasion of Ukraine, exacerbating the already elevated global inflation risk, the persistent higher than expected global inflation and commensurate normalisation of global interest rates. At the time of writing (early November), we saw a spectacular sell-off in global equities and property. Not even the traditional safe haven asset classes were spared. US treasuries saw a record-breaking sell-off on the back of inflation fears and higher bond yields.

Initially, South African asset classes were spared the brunt of the global turmoil, with gold and resource shares supporting our market. South African bonds, already trading at very attractive yields as we went into 2022, were not spared the volatility in global fixed interest instruments, but at the time of writing, were still one of the safer asset classes to invest in.

The strengthening dollar did cushion South African investors against the worst of the storm raging in the global markets.

Why partner with a DFM?

It is understandable that clients expect some guidance on which markets, and maybe specific shares, would provide the best or safest returns for 2023. I always get nervous when financial advisors ask me what the "best" place to invest their clients' money would be. At Equilibrium, we believe that the "best" investment for a client is the one that best matches their financial needs and goals, allowing for their unique time horizon, return requirements and risk objectives.

We recognise that each person's financial needs are unique. More importantly, we recognise that most of the time these financial needs are independent of the performance of markets and state of the economy.

Partnering with a discretionary fund manager (DFM), like Equilibrium, will ensure that the appropriate risk/return profile for an investor's unique financial needs is achieved on the underlying investments. Equilibrium does this by blending different asset classes, investment strategies and fund managers in proportions that speak to the investors' unique time horizon and risk tolerances to achieve the optimal return.

South Africa has world class investment managers who are specialists. However, this specialisation seldomly speaks to the investors' unique financial needs. Certain asset classes and/or investment strategies perform differently in various market and economic conditions. Where advisors partner with a DFM, the DFM bridges the gap between investors' unique financial needs and the specialist skills of investment managers.

What lies ahead for 2023?

Many of our clients ask me what my crystal ball shows as the best place to invest their money. Strange how clear that crystal ball is when we are optimistic about economic growth and markets, and how dull and uninspiring it is when there are concerns about markets. The year 2022 might have been different to what we expected. And I am sure 2023 will be no different. Global economic recovery seems to be at risk on the back of interest rate normalisation, inflation remains stubbornly high and the Russia/Ukraine conflict is continuing for much longer than expected. Volatility in global and local markets persists with markets taking guidance from press releases.

After the significant sell-off in most global asset classes, these asset classes are starting to look attractive, but the main drivers behind global markets for the foreseeable future are going to be whether inflation will be reined in, the interest rate decisions of central banks and the impact on economic growth. The rand remains a big risk for foreign investments, particularly if it strengthens. Most commentators on the local currency are of the view that it is oversold and strengthening could erode the potential returns of global asset classes.

On the local side we see value everywhere. Our bonds are some of the most attractively priced bonds in the world while our equity market is very profitable at the moment. This makes these two asset classes very attractive on a relative basis. Unfortunately, we do foresee economic growth, which typically supports the equity market, to remain subdued for 2023.

Our economists and strategists believe that global inflation should start to taper off towards the middle of 2023 with a commensurate easing of interest rates. This should support global economic growth and markets to be more optimistic. South African markets (especially bonds) stand to be big winners when this shift happens and foreigners return to riskier markets.

This year may bring us as many surprises as 2022 did. At this stage it is important to remind your clients to stick with their financial plan tailored to their needs. Your clients' financial needs are unique and more importantly, not dependent on the performance of markets and economies. Changing an investment strategy based on hope and fears is very dangerous and may move your portfolio away from sound financial planning principles to speculation. ■

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