BRENTHURST WEALTH MANAGEMENT

INVESTMENT REPORT

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SOUTH AFRICA'S LOVE-HATE RELATIONSHIP WITH OFFSHORE INVESTMENTS

By Magnus Heystek – Investment Strategist

SOUTH AFRICAN investors have had a love/hate relationship with offshore investments going back for more than 50 years.

Before the gradual relaxation of offshore investments for individuals was introduced in 1997 anyone who could attempted to smuggle money and assets out of the country.

Getting money and assets out of the country, especially after the Soweto riots in 1976, became a national pastime. Money was smuggled out in bras and in suitcases, in the form of notes, gold coins, rare paintings, diamonds and a host of elaborate schemes to build some kind of offshore nest-egg.

How do we know? According to National Treasury more than 54 000 South African taxpayers came forward during the General Offshore Tax Amnesty in 2004, declaring their offshore assets in excess of R60 billion.

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This is considered a conservative number as many more did not come forward in order to regularize their offshore investments, preferring to continue to hide their foreign assets.

Many wealthy SA families with substantial assets abroad have chosen to emigrate rather than declare their offshore assets to the local authorities, especially after the introduction of the residency-based system of taxation in 2001.

During the 1980's and 1990's investing money offshore was a no-brainer and hugely profitable. The rand was dropping at an annual average rate of about 15% against the US dollar while the US stock market in particular was busy with a multi-year boom market, ever since the correction of 1987.

Over the decade from 1990 to 2000 a SA investor would have made an approximate 1000% on any US equity investment, compared with an increase of only about 230% in the local market.

But for more most of that period SA investors could only look on as the US stock market boomed, especially in sectors like technology & media, as they were not allowed to invest offshore legally.

The introduction of a R200 000 foreign investment allowance in 1997 therefore came very late in the offshore equity boom. However, the sharp weakening of the rand in 2000/2001, coupled with a deteriorating political situation in Zimbabwe, led to a rush of now-eager SA investors wanting to move their allowance offshore.

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At the time it was widely expected that the rand would drop to R20 to the British pound and R14 to the US dollar over time. These projections were made by the SA government in terms of an agreement to purchase a fleet of Boeing jets at the time which lead to a massive hedging loss for national carrier SAA.

It was easy to convince investors to move money offshore. The previous ten years was a bull market for US and global equities, even more so in rands, and using the flawed practice of rear -view mirror-investing in order to extrapolate future returns, investors headed offshore in great numbers.

Over the following ten years investors would only consider offshore whenever there was a weakening of the currency or some kind of political upheaval.

With hindsight the ten years from 2000 to 2010 was great for emerging markets, boosted by the commodities boom which started in 2001 and has continued to this day.

At the same time global developed markets badly underperformed compared with emerging markets with annual returns of –1% versus the MSCI Emerging market index which returned 8.95% over the same period of time.

As far as opportunity costs were concerned, "local was lekker" and SA-based investments vastly outperformed offshore investments over this period of time.

Different investors will have different reasons for investing offshore. At the upper end of the market many individuals want to spread part or all of their R4 million offshore allowance worldwide. Such a move would improve global capital mobility, enhance diversification of assets & also be a precaution against political instability.

Another reason would be the fear of re-introduction of stricter exchange controls again or investors planning to emigrate some time in the future.

Others may want to invest offshore in the logical belief that sooner or later the rand will weaken, perhaps quite significantly. At the extreme end of the spectrum there are investors who react to the rantings of ANC Youth League-leader Julius Malema, whose threats about nationalization is unsettling many people.

THE BRENTHURST WEALTH-VIEW

Intelligent exposure to offshore asset classes offers true diversification.
This is the key to reducing volatility in overall investment performance.

During the recent turmoil in investment markets an investment portfolio with a 30% offshore holding produced substantially less volatility than a 100% SA portfolio.

Different economies in different parts of the world grow (or recede) at different rates and at different times.

The same goes for different industries and companies.

Other reasons for investing offshore include exposure to countries with higher growth rates, such as India and China. And lastly, by utilizing your offshore investment allowance you can invest in industries and companies that do not exist or operate in SA, such as biotechnology, computers, energy and many others.

Brenthurst Wealth has successfully been recommending offshore investments in specialist sectors such as gold & energy for our clients.

However, we cannot deny that our recommendation to invest in the Glanmore Property Fund, previously one of the most stable and rock-solid offshore investments, has been disastrous.

Globally, commercial property was hit very badly by the Credit Crunch with many companies going under, while others, such as the Morgan Stanley and Glanmore Property Funds, losing more than 70% of its value.

Following a successful rights issue completed late last year the latter fund the fund has started moving higher again on the back of a return of confidence to the UK commercial property market.

WHERE TO INVEST?

The issue of where and how to invest once the decision is made to remit some money offshore is a difficult one. The global investment market is vast and there are more than 35 000 registered funds to choose from.

Only a handful of these investment companies operate in the SA market as it is considered too small for the truly large firms to set up office here.

HOW TO INVEST?

The biggest problem for SA investors who choose to remit money offshore is where and how to invest?

Brenthurst Wealth uses the RMB-platform based in Guernsey to house offshore investments for its clients.
This platform provides a very efficient mechanism to gain entry to about 400 of the world's top funds and fund managers including Black Rock, Franklin Templeton, Aurum, GAM, Investec and Orbis, just to name a view.

Not only is it more convenient to invest using such a platform but is it considerably cheaper than going the retail route directly to the various fund managers.

HOW MUCH TO INVEST OFFSHORE?

There are no simple answers to this question. From a purely theoretical perspective SA investors should have 1% of their total portfolio in SA and 99% elsewhere. This recommendation is based on SA's relative contribution to world GDP (gross domestic product).

Naturally this has not always been possible and does not reflect the reality that most investors need to earn an income on their investments where they live.
However, several studies over the last number of years have shown that an exposure of about 30% to offshore assets (compared to local assets) has produced the optimal balance between risk & reward in order to create a truly global investment portfolio.

It's also prudent to match the currency of your assets with the currency of your future liabilities. In other words, if the bulk of your future expenses will be in SA then the bulk of your investments should be in rands.

Conversely, if you intend retiring offshore or emigrating in future then the bulk of your investments should be offshore.

Finally, many SA investors who received amnesty on their illegal offshore assets have preferred to leave these assets in foreign bank accounts. These funds are ideally placed to invest in long-term growth portfolios. Cash has not been an option for many years as interest rates have been so low or non-existent at all.

THE BRENTHURST INVESTMENT STRATEGY

The last number of years has again reinforced the need for a balanced and diversified approach to offshore investment portfolios.

At **Brenthurst Wealth** we have developed what we called the 80/20 principle when it comes to portfolio construction.

Depending on the individual's personal risk profile and tolerance to risk will we generally recommend an 80/20 breakdown of an investment portfolio based on the following rationale:

- **80% of the portfolio is allocated to four different global balanced funds with a flexible mandate. These four funds provide global diversification not only between asset classes and currencies but also between investment managers and styles. They form the CORE OF THE PORTFOLIO and adjustments are only made when a fund manager badly underperforms.**

- **20% of the portfolio is allocated to four specialist, cyclical funds, which are more volatile but can produce superior investment returns, depending on the short term movements of these sectors or asset classes. They are considered to be SATELLITE FUNDS and are changed more often than the core funds.**

THE CURRENT GLOBAL BALANCED PORTFOLIO CURRENTLY IS AS FOLLOWS:

CORE PORTFOLIOS:
- **Blackrock Global Balanced Fund.**
- **Franklin Templeton Global Balanced.**
- **RMB Global Balanced Fund.**
- **Orbis Global Equity**

SATELLITE PORTFOLIOS:
- **Investec Gold**
- **Investec Global Energy Fund.**
- **Ginsberg Global Real Estate Fund.**
- **Franklin Templeton BRIC fund.**

PLEASE SPEAK TO ANY ONE OF OUR FINANCIAL PLANNERS SHOULD YOU WISH TO DISCUSS OFFSHORE INVESTMENTS AS PART OF YOUR OVERALL INVESTMENT STRATEGY.

BRENTHURST INVITES YOU TO OUR NEXT SEMINAR

Presentation: Investing in a Recovering World?

2009 was a year of mixed emotions for investors. Fear and panic at the beginning of the year was reasonably quickly replaced by hope and optimism as green shoots sprouted and then grew and grew. Bear markets morphed into bear market rallies and ultimately talk of a resurgent bull market started to emerge. But the world is not fixed and talk of a correction is everywhere, as the economic recovery stumbles along, albeit in the right direction. Dubai has taught us that the ramifications of the worst economic crisis in 80 years lurk beneath the surface. The next couple of years are going to prove very tricky for investors as policymakers, companies, consumers and equity markets navigate their way through the risks associated with a wounded yet recovering world. In this environment, most investors are choosing to leave the asset allocation, sector allocation and general investment decision-making to the professionals.

SEMINARJOHANNESBURG

DATE: Wednesday, 5 May 2010
TIME: 15h30 for 16h00
VENUE: INVESTEC HEAD OFFICE: 100 GRAYSTON DRIVE | SANDTON
RSVP: JHB: +27 11 799 8100 or email reception@brenthurstwealth.co.za

SEMINARPRETORIA

DATE: Thursday, 6 May 2010
TIME: 15h30 FOR 16h00
VENUE: INVESTEC PTA OFFICE: CNR ATTERBURY & KLARINET STREETS | MENLO PARK | PTA
RSVP: PTA: +27 0861 799 8000 JHB: +27 11 799 8100 or email reception@brenthurstwealth.co.za

SEMINARCAPETOWN

DATE: Wednesday, 26 May 2010
TIME: 15h30 FOR 16h00
VENUE: INVESTEC CPT OFFICE: 36 HANS STRIJDOM AVENUE | FORESHORE | CPT
RSVP: CPT: +27 21 946 2095 email lesyl@brenthurstwealth.co.za or reception@brenthurstwealth.co.za

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PROGRAMME
15h30 –16h00 Registration
16h00 –17h30 Presentations
17h30 –18h00 Questions & Discussions
18h00 –20h00 Refreshments

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