

Monthly Newsletter – February 2018

TIMES ARE A CHANGIN' ... AGAIN!

A message from Theo and Warren

It appears the world is in a state of flux. This time last year, SA investors were worried about the future of the country. The economy seemed to be on a continuous slide and ratings agencies were telling us what we already knew: we were becoming a 'junk' country for international investors.

In the space of a year, many South Africans are much more positive, business confidence is gradually recovering, and our currency is looking much healthier. In contrast, international markets are struggling while the global economy grows.

The next few months are very important to South Africa's mid-term future as we wait for the new budget, a new president and hopefully a clean-up of Cabinet and the state-owned enterprises.

On the business front, Steinhoff and speculation about Capitec has caused massive volatility in our markets, much of it unwarranted. There have been many corporate scandals around the world and investors tend to overreact by judging all companies against the most recent disaster. We feel the Steinhoff scandal has given the asset management industry a bloody nose and has reminded investors that investing is a hugely difficult and complex job.

Over extended periods, the best asset managers have been proven to be correct about 51% to 60% of their decisions, and often the best decisions by asset managers are those made when they avoid big mistakes.

We would caution investors against becoming too optimistic about SA, too pessimistic about international markets (they are correcting from being too expensive) and we urge you to avoid Bitcoin and other cryptocurrencies unless you are happy to speculate with money you can afford to lose.

The investment markets are going to be rather wild for a while, so we suggest you ignore some of the hype in the media and ensure that you have the correct allocation to cash, bonds, property and shares, both in local and international markets. Proper rational diversification is the best antidote to wild markets.

- Theo and Warren

A new video for you

For some months, we have been asked to provide short videos with updates on current issues for our clients. With some reluctance (mostly because Warren does not like being filmed) we have finally recorded our first video for you. It explains our views on the rand and what we think you should do with offshore investments.

We would love to receive your feedback so that we know if this is something we should continue to do. You'll find us on YouTube at <https://youtu.be/fGeLfZjINw4>.

How loss aversion skews your thinking over Capital Gains Tax

At the end of February, the new tax year rolls around. I'd like to share with you an example of how behavioural bias from prospecting theory (specifically loss aversion) sneaks up and messes with people at tax time – in any tax year.

Humans hate to lose: the pain of losing is psychologically about twice as strong as the pleasure of making profit. Fear of losing has an unquestionable impact on investment decisions.

Imagine you must choose one of the following options:

- Option A: A sure gain of R10 000.
- Option B: Playing a lottery with an 80% chance of winning R12 500 and a 20% chance of winning nothing.

Most people prefer Option A. From a purely rational perspective, the two options have an identical expected gain, but Option B is clearly riskier. The chance of winning an extra R2 500, compared to the safe option, is not worth the risk of winning nothing. This reflects risk aversion, and it means that investors are only willing to take on additional risks if they are adequately compensated for it in the form of higher returns.

Now imagine that you must choose one of these two options:

- Option A: A sure loss of R10 000.
- Option B: A lottery with an 80% chance of losing R12 500 and a 20% chance of losing nothing.

If you are like most people, this time you will prefer option B. However, a risk averse investor should choose Option A over Option B, which is riskier while offering the same expected return. Yet, by just switching from a potential gain to a potential loss, most investors switch from being risk averse to being risk seeking. So, what is going on here?

These two examples demonstrate 'loss aversion', which is a natural tendency to avoid losses whenever possible. Instead of accepting a loss, we try to avoid them if possible, even if this means risking an even bigger loss.

Let's apply this to tax. People are much more likely to make the effort to earn extra money they don't have (a certain or uncertain win that means extra tax) than to sell a share and incur capital gains tax (a

certain loss). Part of this relates to loss aversion and part of this relates to the natural antipathy people have towards tax.

A 2011 study from the University of Chicago showed that people can get so focused on avoiding tax, that they will sacrifice higher potential net-of-tax returns. In addition, people will pay more time or money for a tax-related discount than any other discount.

Loss aversion affects everybody and is not always harmful. But there are circumstances when loss aversion can lead to investment mistakes. Don't allow your natural loss aversion to prevent you from locking in (and enjoying) a well-earned capital gain this tax year end!

- Warwick Lucas, Chief Investment Officer, Galileo Asset Managers

Getting your work resolutions back on track

January can be a bit of a strange month, with most people trying to get back into the swing of things after the summer holidays. Once February arrives, it feels like the year has started properly. And it's a good time to review all those professional resolutions you made – to be more productive and assertive, manage your finances better, or work smarter rather than harder.

Like your personal resolutions, many of them might already have fallen back on the wayside, especially if you hit the ground running when the holidays were over. Here are some ways to get back on track.

1. **Narrow things down to one goal.** You can only focus on one thing at a time, so get that right and then move onto the next one.
2. Use your imagination. Envision your success, and think about how you'll celebrate when you reach your goal.
3. **Manage your stress positively.** Stress is a willpower killer – you can't focus on making changes if your mind and body are working overtime to deal with your stress.
4. **Plan every step.** Setting a goal is just step one – plan how you're going to get there, step by step.
5. **Use the domino effect to your advantage.** Start with small actions that lead to larger changes. Success is sequential, and it's about lining up your priorities correctly, and then setting off that first domino.

How to keep burnout at bay

Burnout is becoming something of an epidemic, so it's worth putting some strategies in place to keep it away. Prevention, as they say, is better than cure.

Burnout is the mental and physical exhaustion you experience when the demands of your work consistently exceed the amount of energy you have available. We live in an always-on culture, and it is leaving more of us feeling lethargic, stressed, and depleted. Here are some ways to protect yourself.

- **Take breaks during the workday** – many people see the need for rest as a sign of weakness, but to perform at your best you need regular opportunities for restocking your mental energy, and that means time away from your desk, computer and devices.
- **Leave your work at work** – and that means putting away your digital devices. Actively limit your use of smartphones, tablets and laptops after hours. Most things really can wait until the following day.
- **Schedule fun** – make plans to play squash with a friend or cook a meal with your spouse so that you focus on doing something pleasurable and have that to look forward to, rather than making an avoidance goal like not checking email.
- **Take long weekends** – regular three or four-day weekends can be enough of a rest. Just don't call the office or check your email while you're gone.
- **Focus on meaning** – remind yourself of why the work matters to you. A sense of purpose can change your approach, and give you the energy you need to complete tasks.