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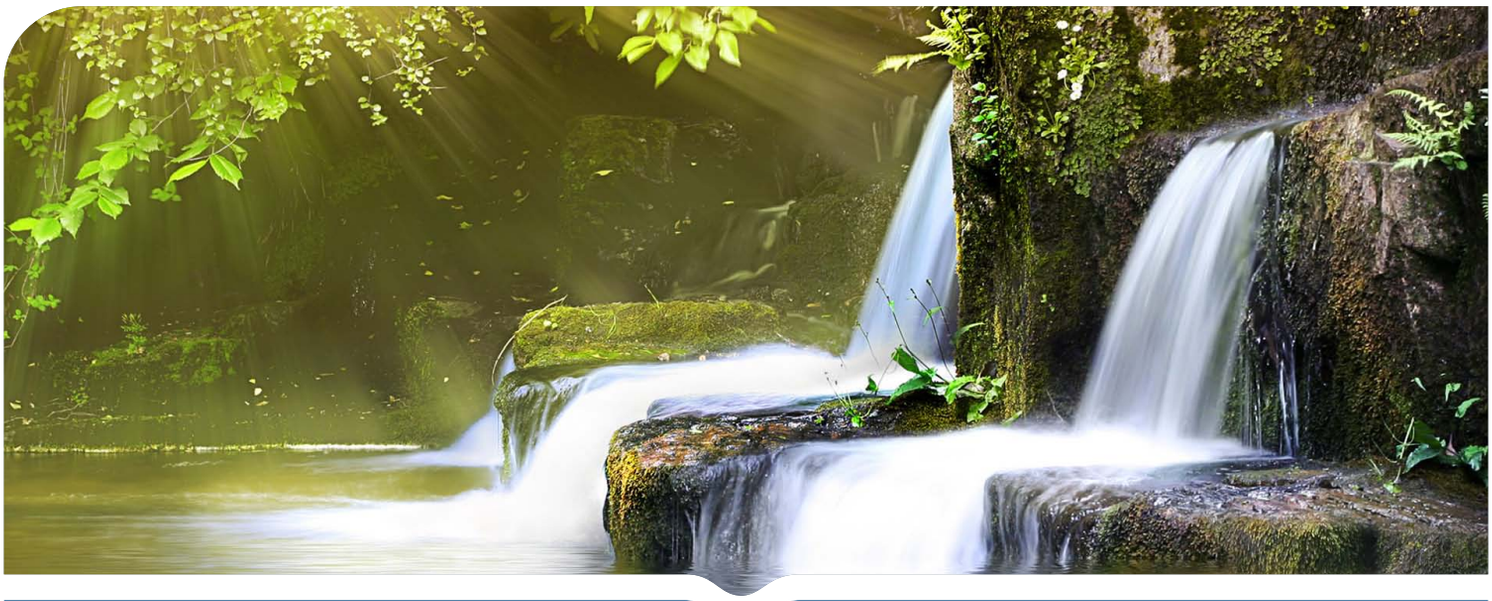
PCH INSIGHT

PRIVATE CLIENT HOLDINGS



Active versus Passive investment strategies – which is best?

With the investment mantra remaining "the maximisation of performance" and with the quest being for long term outperformance, one witnesses the ongoing debate between active and passive investment strategies.

Passive management is an investment style based on investing in the same securities, and in the same proportions, as an index such the Dow Jones or the ALSI40. It is called passive investing because portfolio managers don't make decisions about what to buy and sell; they merely follow the same tactic of constructing a portfolio as the selected index uses. Passive managers invest in broad sectors of the market, called asset classes or indexes, and are willing to accept the average returns produced – they do not try to beat the market, but only to match its performance.

Active investing, which attempts to outperform the market and to beat a particular benchmark, involves analysing market trends and the economy and constantly searching out information and gathering insights to help make investment decisions about companies with the ultimate goal of outperforming the market. Active investment managers use fundamental, technical, quantitative and macroeconomic analysis to consistently identify enough high-performing investments to ultimately achieve better than average results.

Passive or Active Management?

According to **Pieter Koekemoer, head of Coronations Personal Investments**, who spoke at the recent Private Client Holdings seminar, in the great debate between advocates of active versus passive investment strategies, there is in fact some middle ground.

Whilst the main advantage of active management is that skilled managers will be able to outperform the index by making informed investment decisions, passive investing holds benefits in that it closely matches the performance of the index at lower costs.

By construction passive investment will under perform because of costs involved. Koekemoer says that in South Africa instead of accepting this guaranteed underperformance, investors prefer to pick active managers who are likely to beat the index. Unlike the US, the SA market is not as efficient, and opportunities arise through indiscriminate selling by certain large institutions and foreign investors. This leads to valuation gaps that play to the strengths of opportunistic stock pickers.

A common misconception is that passive investments are considered to be less risky than active portfolios. It is interesting to note that many good funds, including the Coronation Top 20, which forms part of the equity block in the PCH multi-manager portfolio, in fact has lower volatility than the passive investments tracking the ALSI40 and by that measure are less risky. Ultimately, it may make sense for you to use passively managed funds as a complement to the actively managed funds in your portfolio.

> "A common misconception is that passive investments are considered to be less risky than active portfolios."

A blended portfolio will provide the benefits of active management, such as the potential to perform differently from the index. But it will also have some of the benefits of passive management, such as lower fees and taxes.

Active and passive management styles offer distinct benefits and the good news is that you don't have to pick one style over the other. At Private Client Holdings we apply both approaches, albeit with a strong bias to active management. In our offshore segregated portfolios, we use Exchange Traded Funds (ETF's) to gain exposure to certain sectors or themes, although the portfolio is dominated by stock picked direct equities.

Your Private Client Holdings Wealth Manager will be able to offer you the best advice on active or passive investment strategies, or if you should adopt a blended approach. It is this key relationship with an expert who understands your goals and needs that will guide you and ultimately maximise your investment.

THE DIRECTOR'S DESK

CURRENT TREND: WEALTH PRESERVATION NOT WEALTH CREATION

Recently, I attended a conference in New York City, where leading gatekeepers to wealth in the Family Office industry gathered to share international perspectives and trends in wealth management for high net worth individuals.

One of the presenters was Michael Connor of the Consolidated Investment Group who ran a single Family Office for Paul Allen, co-founder of Microsoft. Many of the high net worth clients have substantial Private Equity interests and Paul Allen was no exception. Connor spent much of his time on due diligence for new acquisitions or mergers and had to run teams of staff members related to sports teams, commercial spaceships, mega yachts and global property portfolios. With a personal fortune eclipsing the market capitalisation of Old Mutual it is understandable that managing Allen's wealth is a little more complicated than the norm!

WE ARE IN THE STAY RICH BUSINESS

The overriding message from presenters and participants was around the importance of preservation of capital and that it is far more important for high net worth clients to limit losses rather than generate outstanding returns. Paul Tramontano of Constellation Wealth Advisors distilled this message when he said that he tells his clients "You have been in the get rich business and we are in the stay rich business".

Jonathan Bergman of TAG Associates, a top 30 multifamily office, cautioned about concentrated share or sector bets and said "when you are 50% down you have to double to get back to where you started – it's simple maths!".

This cautious approach is illustrated in the latest World Wealth Report produced by Capgemini, where more high net worth individuals claimed to be focused on preserving wealth than those focused on growing wealth.

The asset allocation breakdown during the first quarter of 2013 indicates the extent of the aversion to risk with a mere 26.1% of portfolios exposed to equities.

DISCIPLINE, DEVELOPING A STRATEGIC PLAN, APPROPRIATE ASSET ALLOCATION AND DIVERSIFICATION

Notwithstanding the fact that many Family Office clients produce more than the GDP of some small countries, the common sense principles which inform normal asset management practices are still relevant – discipline, developing a strategic plan, appropriate asset allocation and diversification.

The importance of structuring a strategic plan during calm times cannot be emphasised enough as it removes emotion and paves the way to make tactical decisions without emotions of fear and greed.

It is interesting to note the apparent disconnect between the advice of professional firms and the reality of the underlying asset allocation. It seems that the asset allocation decisions are not set in calm times, but have been hastily adjusted during the financial crisis.

High net worth investors, like the man in the street, have succumbed to fear and have adjusted their portfolios inappropriately by rushing to stable investments and underweighting equities. In the process they have forgone substantial equity returns.

It was a very informative convention that provided in-depth insight into the habits of high net worth individuals and it will be interesting to report to you on what trends unfold in next year's Capgemini World Wealth Report.

Grant Alexander

HAVE YOU HEARD?

PCH Customer Service Referral Initiative

In early September at a beautiful breakfast held at Highlands House in Kenilworth, PCH successfully launched our customer service referral initiative with all of the PCH wealth managers and wealth manager assistants in attendance.

This initiative provides another avenue of communication with our valued clients, so don't be surprised if you get an extra call from one of our wealth manager assistants to check that our database details are up to date and to check if the services you are receiving from PCH are up to scratch.

Planting trees with Greenpop

In line with our CSI initiatives and to show our continued support for the amazing work the team at Greenpop do, (visit www.greenpop.org.za for more information) the entire PCH staff went tree planting at the St Monica's home for the elderly in Bo Kaap.

Not only are we trying, in small ways, to offset our carbon footprint, but we are also delighted that the 30 trees planted with Greenpop will provide a valuable windbreak for the flourishing and necessary vegetable garden at St Monica's.

Coronation Double Century Cycle Challenge

For the first time ever, PCH will be entering a mixed team into the Coronation Double Century Cycle Challenge, taking place in November. We wish the guys and girls taking part in this race all the best and if you are on the road please keep an eye out for the team in our PCH cycling kit.

6 Down Rugby

Sadly this will be PCH's last year of supporting our committed 6 Down rugby team. Most of the team will be heading off to remote locations in the new year to finish their medical internships. We wish them all the very best of luck for this final season!

The value of good advice is measurable

There has been much debate and criticism on the cost of financial advice in South Africa and a strong regulatory driven focus exposing any hidden costs. The question of what financial advice is really worth has come to the fore recently with the introduction of the Retail Distribution Review (RDR).

South Africans are often reluctant to pay for financial advice because it is hard to establish the link between its value and the fees they have to pay for this advice. As a result of this some investors approach Fund Houses directly as they believe they can get a better deal by cutting out the "middle man", namely the wealth manager. Enter Clean Pricing - which enables investors to know exactly how much expert investment advice will cost; what they are paying for (independent or restricted advice), and to improve professional standards.

Susan Vermaak, member of the Private Client Holdings Investment Committee, explains that investors will now move from paying opaque fees and commissions, which has long been criticised as unclear and overly lucrative for advisers and administrators, to clearly defined service fees. Private Client Holdings has already implemented unbundled pricing and have teamed up with investment services groups like Investec IMS that are at the forefront of these developments in South Africa.

And now there is Gamma

Recently a group from Morningstar, who provide independent investment research, came up with what they call **the theory of "Gamma"**.

Beta is regarded as the exact return of the market - effectively what is produced by a passive investment strategy. Alpha is regarded as the additional return produced by an active manager.

Gamma is a term used to describe the value that making the soundest financial decisions over a long period can provide for investors – i.e. the value that advisers and wealth managers add to the investment process.

Gamma represents the variance between DIY investing versus using a wealth manager.

In a recent Sunday Times Personal Finance article written by Bruce Cameron, he states that research executives David Blanchett and Paul Kaplan at Morningstar have deduced that financial planners can add the equivalent of a 1.82% annual arithmetic return to clients through Gamma.

> "Over time, that can translate to nearly 29 percent more money to spend in retirement"

This is a significant percentage for anyone's retirement fund and clearly shows the value of good investment advice – which our clients experience with their Private Client Holdings Wealth Manager.

As stated at a recent PCH Seminar by Pieter Koekemoer of Coronation, good advice essentially costs good money. Partnering with the right financial adviser is the most important decision in your wealth management decision making.

Meet the Private Client Holdings Wealth Management Team

From left to right are: Alan Ferguson, Bryan Leach, Gareth Lange, Janine Horn, Mark MacSymon and Mark Robson, the highly qualified and experienced Private Client Holdings Wealth Management team who manage all of the assets, investments and wealth management needs of our clients, both locally and internationally.

Have you practised dying recently?

Have you considered what would happen if you met your demise on the way home from work this evening?

Would your family know where your will is kept? Would they know where your assets are held? Or would there be chaos? You may know exactly where assets are invested but does your spouse or your investment adviser know?

According to David Knott, Director of PC Trust, most people are methodical and precise in their business lives but often pretty haphazard with their personal affairs. Documents of title and investment confirmations could be scattered anywhere in the study, the office and all points in between.

After death, your executor needs to take charge of all assets, investigate and settle all claims against the estate and give transfer of the residue of your estate which could include fixed properties, vehicles and investments to the rightful heirs in terms of your will.

Try to imagine the wasted time if the executor cannot easily ascertain where all these details may be.

With many investors now also having funds abroad, the search for assets becomes more complex unless you have kept reasonable, accessible records. Obviously, having your investments and tax affairs managed under one "roof" by a company such as Private Client Holdings helps to keep everything together and allow for a seamless transmission of information to the executor who can then leap into action without delay.

Details of your assets and investments, along with other important documents, such as ante nuptial contracts, title deeds, motor vehicle registration certificates, orders of divorce, lease agreements and the like must be kept together. And your spouse and executor must know where to find these documents in the event of something unforeseen happening to you.

The sooner your executor can confirm investments and settle taxes and other liabilities the sooner they can distribute your estate to your heirs and allow them to gain finality and get on with their lives.

Speak to our Private Client Trust experts about your Will and Estate and let them advise and address any of your concerns.

WHO TO TALK TO

Our Private Client Holdings experts are available to field your questions. Don't hesitate to contact us for expert wealth management advice.

Portfolio Management
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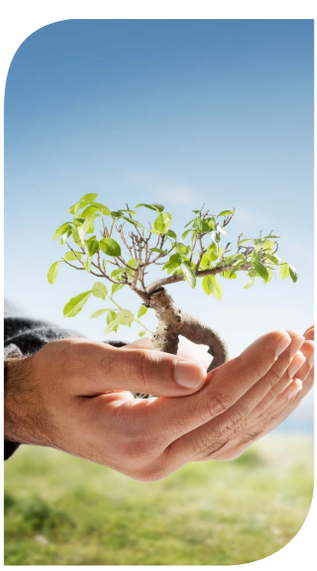
We are growing...

Private Client Holdings is growing in size and capacity in response to our clients' needs, and the Private Client Trust division - under the guidance of director, David Knott, and our Forex and Cash Management divisions, have moved into our new Private Client Trust building.

The PC Trust building entrance is directly across Niekerk Lane opposite the entrance to the Private Client Holdings building.

You are welcome to pop in for coffee and a tour of our new offices any time – David and his team are on hand to welcome you.



TEST YOUR SUDUKO SKILL!

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