Monthly Newsletter – October 2017

Bitcoin fever: A note from Theo and Warren

Bitcoin mania is in full swing and investors around the world are getting caught up in the hype. Unfortunately, investor frenzy is never a great predictor of future returns, especially for those who are late to the party. The lure of investment gold at the end of the proverbial rainbow is so powerful that many speculators do not apply rational investment principles when making investment decisions about bubbles.

While we think there is huge merit to the technology behind Bitcoin and all similar currencies (blockchain) we are not convinced about Bitcoin as a long-term investment. It currently looks more like a speculative bubble than a new investment asset class.

Some early bubbles

Tulip mania

The tulip bubble began in 1633 and burst in 1637. At the peak of the bubble, a single tulip could be traded for an entire farming estate; in one month, the price of tulip bulbs rose 2 000%. Once the bubble burst, a tulip was the same price as a common onion.

Ostrich feather bubble

The ostrich feather boom took place between 1890 and 1914. This was driven by fashion, as the feathers were primarily used to decorate hats. At one point, you could get more money for 1kg of feathers than 1kg of gold. The boom ended in 1914 and was blamed on Henry Ford and the arrival of the first motor car. Ladies were not able to wear their elaborate feathered hats in cars that had roofs, and so the demand for feathers collapsed.

What does Bitcoin have to do with tulips and ostrich feathers?

There is no doubt that blockchain technology and cryptocurrencies could have a massive impact on all forms of business, especially financial services. However, this does not guarantee that Bitcoin will be the first choice as a store of value. It is very difficult for proper investors to consider an asset that can appreciate by 180% in six months.

Similarly, Bitcoin has lost more than 80% on a few occasions, causing serious investors to allocate very small amounts of money to Bitcoin and only as a form of speculation.

“We learn from history that we do not learn from history” (George Hegel)

One of Warren Buffet's pearls of wisdom is to only invest in what you know. How many investors in Bitcoin understand what Bitcoin is and how it really works? Apparently, there are only a few hundred people in the world with such skills, and for many, Bitcoin continues to remain a mystery.

If you don't understand your investment and you are buying when there is a state of euphoria, tread very carefully: you might be the last buyer at the highest price. Our advice to people considering investments in Bitcoin is to avoid it unless you have done your research and understand the market dynamics. If you do take the leap into Bitcoin, be sure to only allocate capital that you can afford to lose.

- Theo and Warren

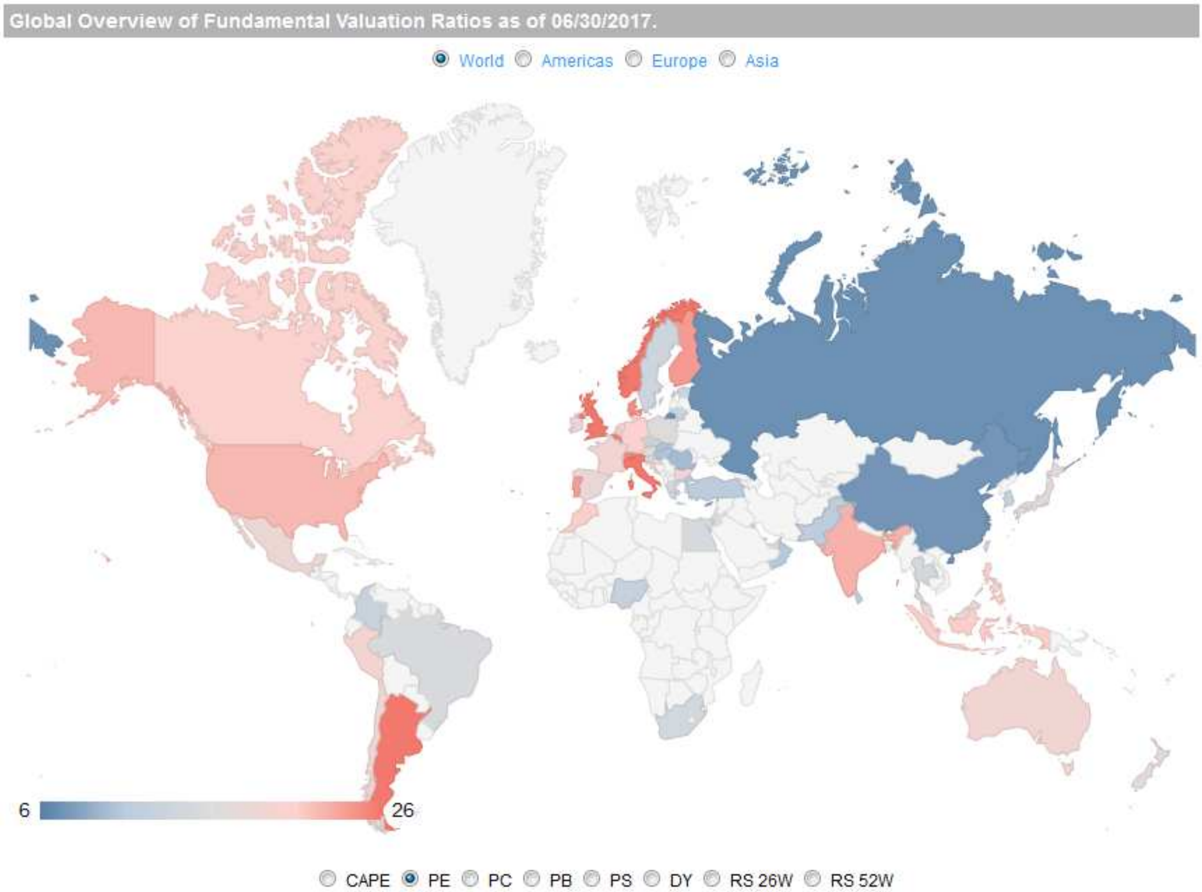
What – in the world – are we doing?

One of the benefits of having a global investment platform at our disposal is the stunning array of choices it offers. There are approximately 70 000 shares, 40 000 ETFs and 14 000 unit trusts listed on the primary offshore platform we use. Sure, quite a number are multiple listings across markets, but that's still a lot!

We use ETFs that are targeted to what we want to achieve. We are predominantly a value manager, as we believe this style offers enhanced risk-return characteristics, but we are by no means dogmatic in our approach. Our value bias should be expected to outperform the index in weak and normal market conditions, and underperform in strong bull markets. Our average goal is to match the performance of the relevant market index over the long term, with lower risk.

We believe that stock markets offer the best inflation-beating returns over the long term. We consider equity markets to be fairly efficient, but not always rational. It is our view that only the purchase of attractively priced and well-managed quality businesses will provide sustained capital growth with increasing dividend income. We generally avoid (with some rare exceptions) the practice of timing the market, as long-term investments in quality businesses are the best risk management strategy of all!

A second consideration is geography. Some countries are loved and over-invested, and others are hated and discounted irrationally. So while we don't time markets, we'll look at good value markets over more beloved ones. The following graphic of global price earnings (PE's) gives some perspective:



The range of global PE's extends from 7x-30x. We note a lot of 'penny dreadful' writers are currently jumping up and down and calling the next crash. Some of them have consistently done so since 2009! We also note that the track record of such writers is – when aggregated – worse than the market as a whole.

It's true that global PE's are higher than average – but PE's are very blunt instruments – after all, global inflation is ridiculously low. A PE in 2017 is not the same as a PE in the 1980s. It is no more reasonable to compare PE's across time, than across geography. Different inflation rates will mean different real returns.

A much more constructive angle is to look at measures called Equity Risk Premiums, which categorise market valuations against the inflation rates and bond rates prevailing across different markets. By the measures we have at our disposal, the most attractive valuations are to be had in Europe and emerging markets. Next would be Japan (but don't forget Japan's rock solid corporate balance sheets) and the tail is brought up by North America. This doesn't mean that we disregard North America, it just means we tend to be allocated elsewhere – by choice.

Market timing is generally an exercise in frustration. There is a mass of deflation keeping a lid on inflation in most of the world. Central Banks may have expanded their balance sheets, but the private sector pulling in their horns has created a tide the other way. Share buybacks still make sense for many companies. And the global savings glut is a demographic baby boom phenomenon that isn't going away in a hurry.

The point of global investing is not to run away from South Africa. It is to run towards the sea of opportunity out there. Clients of Galileo Asset Managers can access targeted country funds through their SwissQuote platform accounts.

- Warwick Lucas, Chief Investment Officer, Galileo Asset Managers

Avoiding burnout in the final quarter

It's the final quarter, and everything is building up towards the summer holidays. Here are some practical tips to get you through the last stretch of the year without burning out.

1. Exercise regularly and try to take a daily stroll somewhere pleasant.
2. Eat healthily – remember your food is your fuel.
3. Drink enough fluids, especially plain water.
4. Get enough sleep and try to go to bed at the same time and get up at the same time seven days a week.
5. Avoid too much alcohol and caffeine – they do more harm than good.
6. Focus properly at work, with the goal of leaving your work at work.
7. Stick to regular working hours as far as possible – keep your days to nine hours maximum.
8. Take a lunch break – it gives body and mind a rest and will make your afternoons more productive.
9. Ensure you stay connected with family and friends.
10. Take time to rest and relax.
11. Set boundaries with colleagues, family and friends.
12. Approach the festive season with realistic expectations when it comes to both finances and family responsibilities.