MOTSWEDI
Economic Transformation Specialists

Mark's musings

Passively changing the status quo

The South African asset management and investment consulting industry displays high levels of concentration. Looking specifically at the asset management industry, the level of concentration is scary, with 6 asset managers (out of well over 100), controlling about 60% of the entire pool of long term savings and investments. The implications of this are far reaching for an emerging economy, low flow of capital and coverage of small and mid cap stocks on the listed exchange for one. The concentration of decision makers over large sums of capital means poor democratisation of financing and bottle necks in new investment ideas which are implemented in retirement fund investment strategies.

The problem with concentration

One simply has to observe the low take up of organically grown black asset managers by retirement funds which make up only 8% of the entire long term savings and investment industry. Another place one can observe the bottle-neck of new ideas is the low take-up of passive investment strategies across the retirement fund industry in South Africa, which makes up about 3% of the entire pool – compared to the trend in global markets, like the USA where passive makes up roughly a quarter of the market.

The right debate

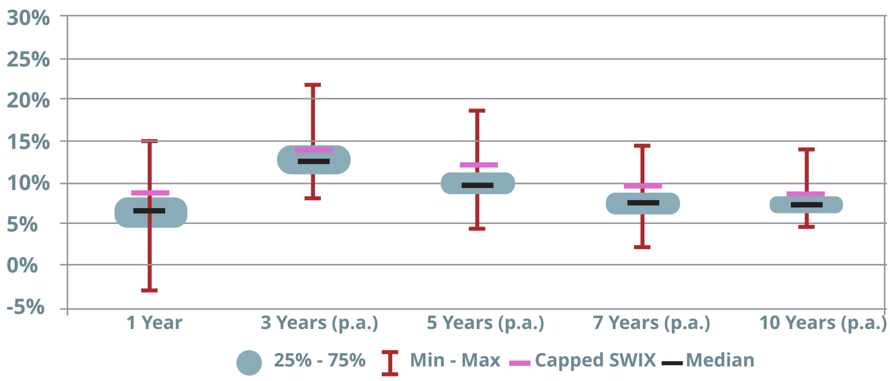
The debate in South Africa has always been active vs passive investing. Which in my view is the wrong way to look at the conversation – the discussion should rather be how can passive compliment active in a South African context and in that way create room for new ideas in the long term strategy. Many boards of trustees struggle with the idea of managing their risk budget to allocate meaningful assets to these new ideas and at the same time management of costs makes the discussion a challenge. For trustees the risk budget is made up of many aspects which they have to take account of, including their time, the total cost of management of the retirement fund and the ability to achieve the ultimate objective of long-term real returns for members.

What's in it for you

Looking at the performance of equity markets over time, both local and global, we see that the average active asset manager has found it difficult to outperform the index. In fact when looking at the global market over all time periods as described in Graph B, we see that the index has out-performed the average asset manager and if we take account of the higher fees in the global space, the index outperforms by an even greater margin.

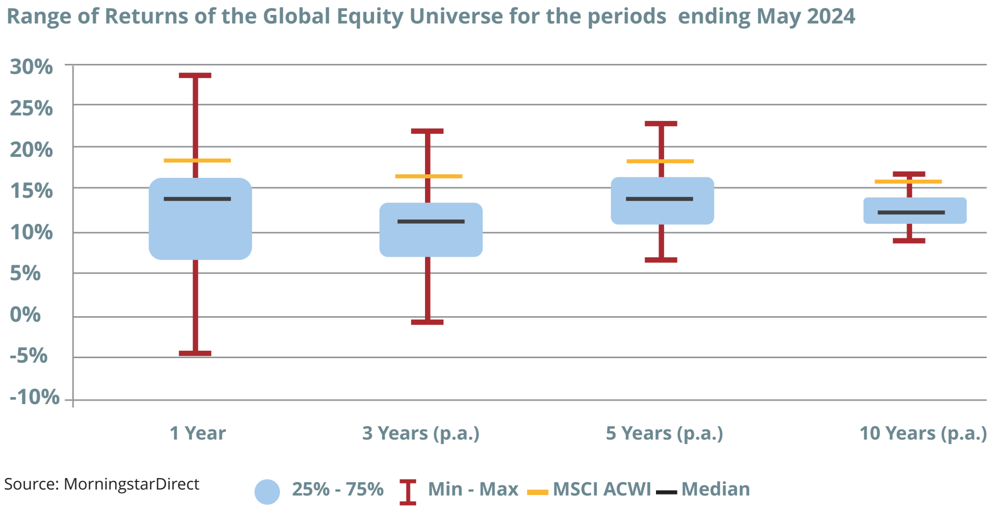
Graph A

Range of Returns of the SA Equity Total Investable Universe for the periods ending 31 December 2022



Source: Alexforbes Annual Manager Watch - 2023

Graph B



What these graphs are demonstrating is that by investing simply in the index, long term investors are able to achieve a better outcome than purely investing actively. Thus a combination of passive and active can add value to a long term investment strategy.

Trustees and their risk budgets

Juggling all these requirements means the demands on trustees are real and can be daunting. However, what we have observed is that with the inclusion of a low cost passive core as part of the retirement funds investment strategy we see the ability to create the space for trustees to actively engage these new ideas without increasing their overall costs and achieving improved diversification.

Doing things differently

We have to do things differently to achieve a different result to what we have achieved in the past 30 years. Problem solving for uniquely South African problems is how we will move the dial on Economic Transformation. Sometimes, the problem may not be that complex, but requires a new way of thinking to implement. Retirement funds hold the key to unlocking the transformative potential of the multiplier-effect that will empowering more black-owned businesses.