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Higher returns, lower risk

Offshore investment is becoming more mainstream

While offshore investing used to be the exclusive preserve of the super-wealthy, it is increasingly becoming part of a diversified investment portfolio as investors look beyond SA's borders to realise better returns given the under-performing local market.

In fact, according to Glacier International MD Andrew Brotchie, offshore investing has become a lot more mainstream, particularly for SA investors looking to mitigate political and economic risk and currency volatility.

However, the poor performance of local markets is not the only reason investors typically look offshore, he says. Not only has the fragile state of the SA economy highlighted the importance of diversification, but the Covid-19 pandemic has created opportunities for some businesses – and not all of these opportunities can be accessed via local companies.

"In recent years investors have approached offshore investments with a different mindset, which has included a careful evaluation of their overall investment portfolio, where it is exposed and what its underlying assets are. Ultimately, investors are less concerned about getting money offshore than they are about where they can access different sources of return," says Brotchie.

Growth and diversification are the main reasons for investing offshore, agrees Chris Potgieter, MD of Old Mutual Wealth Private Client Securities. In the hunt for growth, investment diversification is critical.

However, according to the AfrAsia 2019 SA Wealth Report, high net worth individuals in SA hold less than 20% of their wealth offshore. Between about 65% and 80% of local investors' total wealth is directly exposed to the local economy.

Andrew Brotchie: Investors should consider moving a part of their retirement fund offshore

"What this means is that the majority of investors have too many eggs in one basket and have not diversified sufficiently," he says.

Offshore developed markets, says Potgieter, offer more depth and breadth relative to the local market, which allows investors to better diversify risk and access more investment opportunities for growth.

He advises that more liquid assets should be invested offshore for both capital growth and better protection and to supplement the limited offshore exposure achievable through pension funds.

Potgieter says offshore investments should be diversified across markets and geographies, including emerging markets.

"Broadly speaking, a typical equity portfolio would be heavily invested in US multinational companies together with selected UK and European multinationals, providing exposure to both developed and developing markets and a good balance between established businesses and growth businesses."

Many SA investors learnt the hard way not to react to disruptive events in an emotional way. After Nenegate in December 2015 when former president Jacob Zuma unceremoniously fired finance minister Nhlanhla Nene, some investors took their money offshore in a panic.

That's not the ideal way to invest offshore, says Brotchie, and savvy investors have realised that. "Instead of taking money offshore when the rand weakens, increasingly investors are taking money offshore when it strengthens, indicating that they're making more sensible, long-term decisions."

Timing can be critical, agrees Ninety One sales manager Paul Hutchinson.

"Offshore equities and the rand tend to move in opposite directions. Essentially, when offshore equity markets perform well, offshore bonds are the losers and the rand tends to strengthen, resulting in a currency loss on offshore portfolios.

However, when offshore equities perform poorly, offshore bonds gain and the rand weakens, resulting in a currency gain on the offshore portfolio.

Put differently, rand depreciation adds to the investor's return calculated in rands, while rand appreciation detracts from the overall return. This is why it's important to take a longer-term view and look past short-term currency movements.

NFB Private Wealth Management MD Andrew Duvenage agrees that offshore investing needs to be considered as a long-term, strategic investment.

He says a number of basic principles apply to successfully investing offshore including being sufficiently diversified; being cognisant of the risk and longer time horizons to deal with potential volatility; and being patient.

"Given the volatility of the rand, following a strategy of regularly exiting the rand may make sense as it could mitigate the risk of externalising at unfavourable rates – a so-called cost averaging approach. However, while tactical

What it means:

Local investors wanting growth and diversification are moving part of their portfolio offshore

Andrew Duvenage: Investment strategy must be long-term

Chris Potgieter: Offshore offers more depth and breadth

Radhesen Naidoo: Don't invest when the rand is weak

trading of currency movements may well produce results for some, it is a high-risk strategy," he says.

There are a number of variables that need to be considered when deciding on the right time to invest offshore, and the rand is only one of them, says Allan Gray business analyst Radhesen Naidoo.

"Just as important is to consider value in the market. Investing offshore at an extreme point – including when value is very high and the rand is weak – is not ideal. It's always the price you pay today that is the key determinant of future returns," he says, adding that the decision to invest offshore should not be a reactionary one but should rather match the investor's long-term investment goals.

"Treat the offshore component of your investment portfolio as part of a diversified investment strategy rather than flavour of the month. When offshore is part of your investment plan from the outset you have more options and more flexibility," he says.

Investing offshore without guidance can be a complex affair, resulting in investors inadvertently exposing themselves to unintended risks, including tax consequences, which is why Brotchie advises appointing a qualified financial adviser to design an investment portfolio that is tailored to the investor's needs and risk profile.

Furthermore, he advises investors to consider solutions and products that, administratively, enable investors to invest offshore with relative ease.

"Legal and tax implications need to be taken into account in the planning process when investments are being made in foreign currency," he says. "If they are not factored into the product or the planning, these implications could be costly."

Assets situated in the US or the UK, for example, can be liable to a 40% inheritance tax as opposed to the 20% inheritance tax imposed in SA. Similarly, winding up an offshore estate and getting offshore assets released can be time consuming and expensive.

The majority of investors have too many eggs in one basket and have not diversified sufficiently

However, structured correctly, these challenges can be reduced, he says.

For those who have opted for early retirement or have been retrenched, Brotchie suggests considering investing a portion of their retirement fund offshore. Up to a third of a retirement fund can be withdrawn as a lump sum on retirement or retrenchment. This allows for retirement funds to be diversified in foreign markets, industries and funds.

Given that the offshore fund universe is large, with many unfamiliar asset managers and funds, Brotchie advises choosing an investment partner with a proven track record locally and abroad.

"Reputation and research are of paramount importance," he says, adding that investment partners should be part of a reputable brand and have a track record that can be properly evaluated; have strong research capability and the skill to do deep-dive studies of funds and asset managers; and have a long-standing track record in the investment industry.

Finally, he advises looking for transparency in the investment proposal.

"Consider one that is well-researched; is offered by a provider with a good reputation and track record; has good levels of feedback reporting; and provides you with access to information. You don't want to have to work hard to get information about your portfolio or how it is doing."

Given the growing appetite for offshore investments locally, Glacier has launched the Glacier Offshore Investment Plan, which allows investors to diversify their investments across markets and currencies more simply and affordably.

The investment plan also allows for improved returns over the long term.

Glacier's Offshore Investment Plan, says Brotchie, offers investors liquidity, given that investments can be withdrawn at any time; access to global opportunities with lower minimums (the plan requires a minimum lump sum investment of R100,000) than traditional offshore options; a streamlined investment process with less requirements than traditional offshore options; and guided investment choices through risk-profiled model portfolios.

"The Offshore Investment Plan allows investors to invest in a range of risk-profiled portfolios managed by a dedicated team of research and investment specialists," he says.

"Alternatively, investors can construct their own portfolio in collaboration with their financial intermediary from a list of offshore funds carefully selected by our investment research specialists. Investors have the option of using their own offshore investment allowance, or they can invest via an asset swap provider. Reporting is available in euros, US dollars or British pounds."

The benefit of this plan, he says, is that it allows investors to diversify their portfolios across various countries, regions, sectors and economies, benefiting from a host of growth opportunities in a range of industries, companies, currencies and investment philosophies – ultimately improving returns over the long term. x

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