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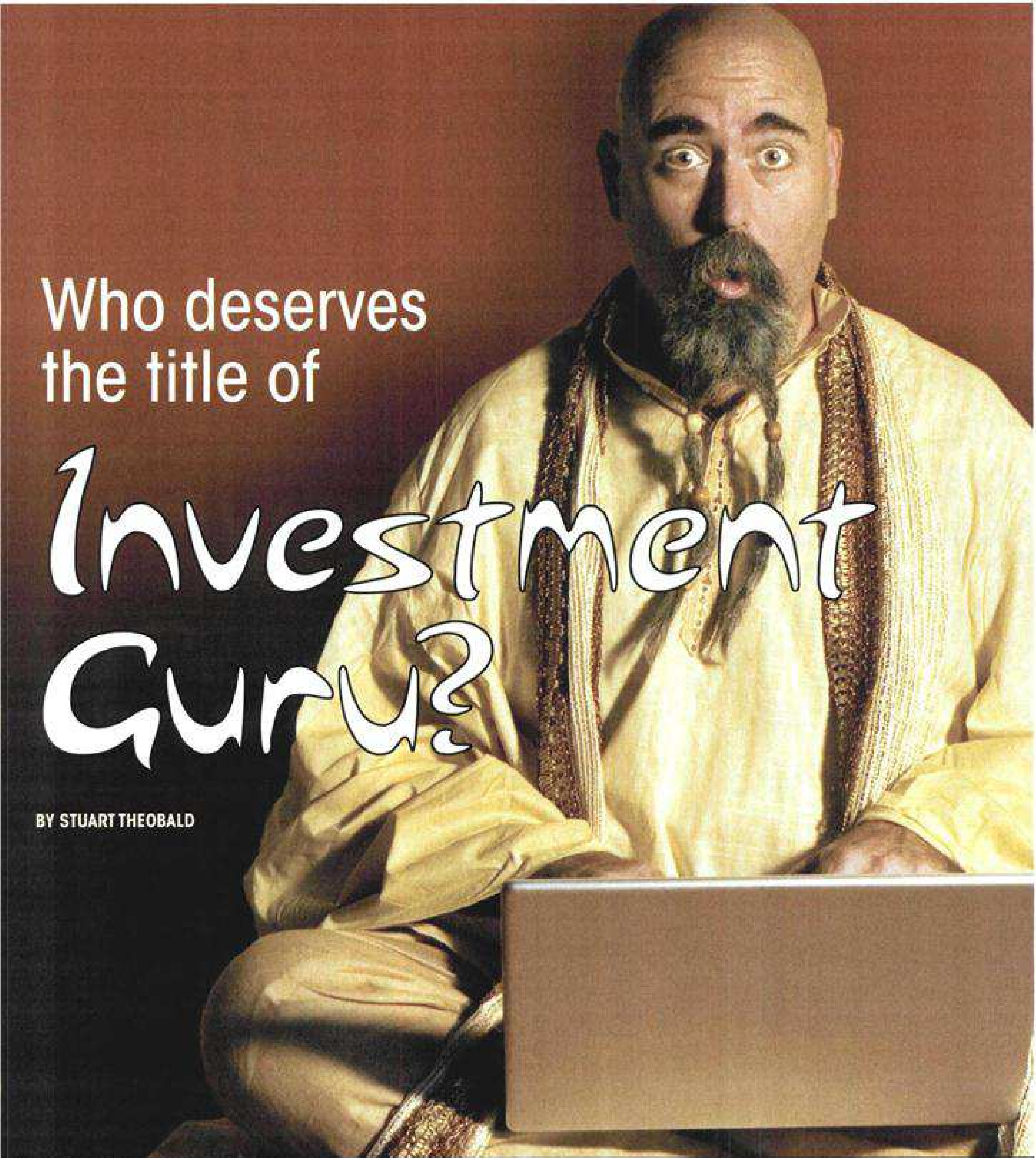

Who deserves the title of Investment Guru?

BY STUART THEOBALD

Sifting through mandates, separating the individual contribution from the asset class's movements, balancing risk and returns – many factors are at play in assessing long-term performance

YOU'D THINK IT would be a simple case of seeing who boasts the best returns. If all we were talking about was stockpicking, that might be the whole story. But there's far more to investment decisions than picking stocks. Every fund manager has a mandate to follow, a specification of which asset classes or investment targets they are allowed to invest in, and by how much. Risk is also important – the less volatility experienced by a portfolio, the better.

Investment success comes from choosing asset classes (shares, bonds, property and cash mainly) then choosing a sector within each asset class, and only then choosing the specific instruments. A lot of fund managers are only given the last leg in that decision tree. And generally, most returns come from the asset class, not the instruments.

To identify who deserves to be considered a guru of South African investing, we've looked at both a house view and at individuals. Some decision processes are about the team and it's impossible to select specific individuals. Others are more clearly about stockpicking and individuals stand out. As we describe, selecting top performers is a deeply difficult task.

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The guru houses

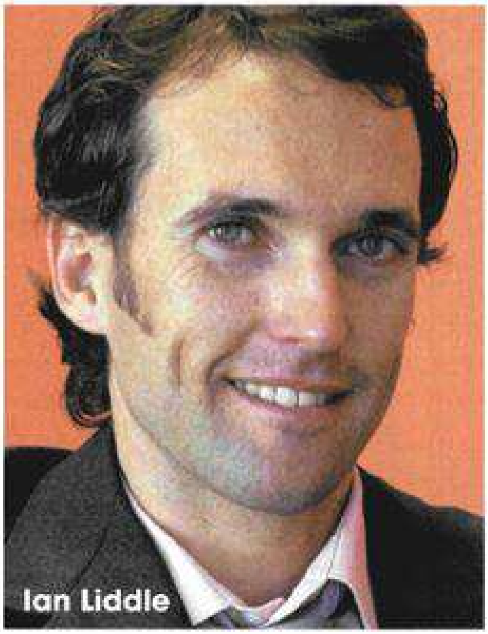
There is one fund type where the fund managers get to make all the decisions – from the asset class through to which instruments to invest in. That's the balanced funds. It's not quite total freedom – under South African rules the fund manager is still restricted to some limits (the main one is no more than 75% equity or 25% foreign assets, but these are changing, see page 34).

Balanced funds have become the flagship of most investment houses. They have also become increasingly popular as the realisation has taken hold that asset class allocation is usually responsible for more returns than within-class picks. As a result pension fund advisers and trustees have tended to hand this responsibility over to the fund manager rather than carry it themselves. That means funds have shifted from typical equity, bond and property funds into asset allocation funds.

Specific equity sector funds that allowed investors to choose between industries (industrial, financial and resources), size (large cap and small cap) or style (growth or value) have become even less popular. But, it is largely the risk that is controlled in balanced funds, not the returns – pure equity funds will have higher returns on a 10-year view. In the long run, equities outperform the other asset classes.

So if the balanced fund is the gold standard of fund management, is choosing the best fund managers not simply a case of seeing which funds give the best returns? Again, this is not the whole story. For one thing, performance differs quite strongly from year to year. We've examined the top five balanced funds on a 10-year view (see graphs). While **Allan Gray** and **Coronation** had the top two funds over the past 10 years (the figures are compounded annualised returns), their ranking varies dramatically in other time periods. The graphs show the rankings for five-, three- and one-year performances too and neither house holds on to the top two places in shorter time periods.

Plus, it's not clear that returns are all that matter – many investors would rather see less risk as well. The graphs reveal consistency in the top three funds – Allan Gray, Coronation and **Sanlam Investment Management** have returns that rank in the top 25 of the funds for all periods

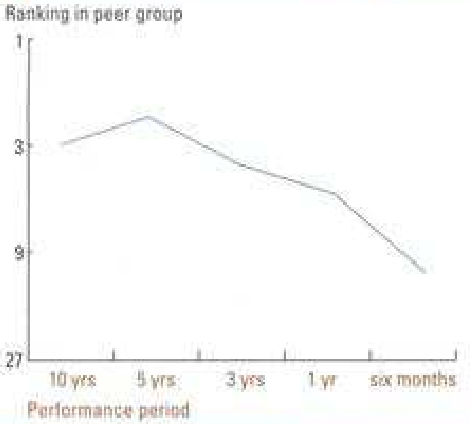

Ian Liddle

we examined. Allan Gray's worst relative performance has been over the past year when it's comparatively light weight in equities hurt. But it has stepped back up in the past six months. Coronation has stayed remarkably consistent – in the top three over 10, five and three years. **Stanlib**, which hit a rough patch three years ago, has recovered to take top spot on a one-year view.

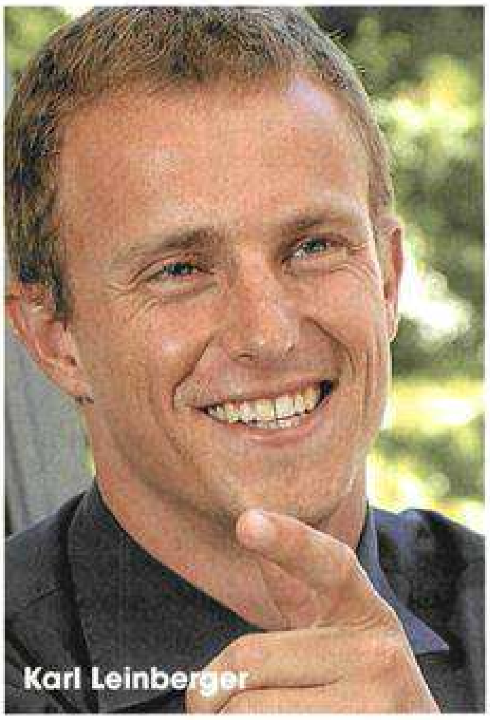
The far tougher step is to attribute performance to individuals. Allan Gray will insist that it's well-developed investment strategies are key to its success, rather than the flair of any individual fund managers. The balanced fund, for example, draws on a wide range of fund managers, each of whom manages a slice of the assets. Allan Gray's process sees portfolio managers lobby for particular fund positions, but the actual picks are made by the group. The asset allocation decision, while ultimately the responsibility of chief investment officer Ian Liddle, is made through a complex process of value assessment by the entire team. If any individual has to be named, it is surely the one responsible for designing the process, and that would be founder Allan Gray himself. But he plays no active day-to-day role in picking investments. For houses such as Allan Gray and Coronation, led by chief investment

THE RANKINGS SHAKEDOWN

CORONATION BALANCED PLUS



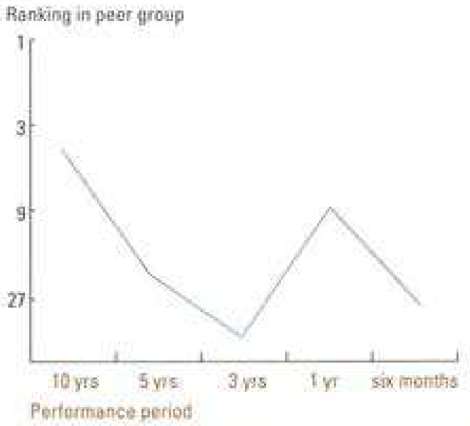
Source: Morningstar



ALLAN GRAY BALANCED

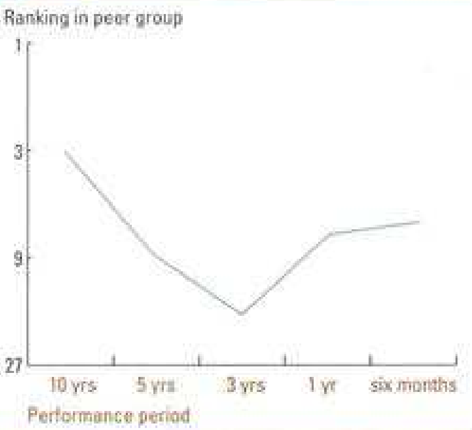
Source: Morningstar

INVESTEC MANAGED



Source: Morningstar

SIM BALANCED



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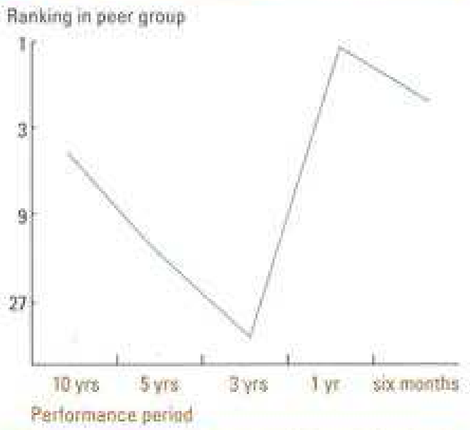
STANLIB BALANCED



Source: Morningstar

officer Karl Leinberger, where process and teamwork is emphasised, it makes no sense to select individuals. The gurus are the houses themselves.

We graph the performance of the top five asset managers based on returns over the past 10 years. There are only 14 balanced funds that have been around for the past 10 years (compared with 65 in existence now).

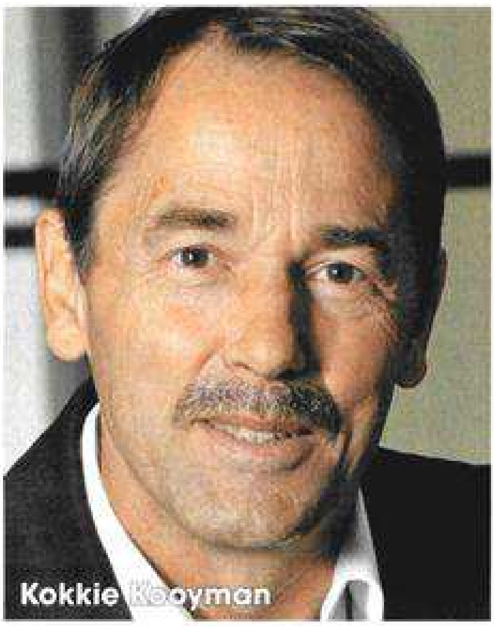
The best has returned just more than 18% a year compounded, while the worst has done just more than 8% (**Metropolitan's Absolute Provider**).

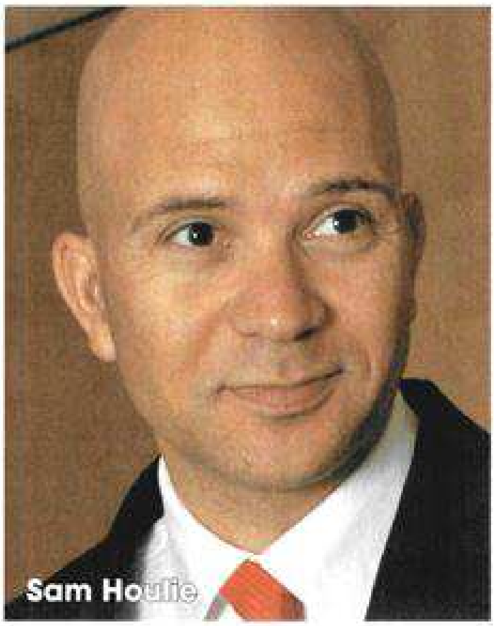
Top fund managers

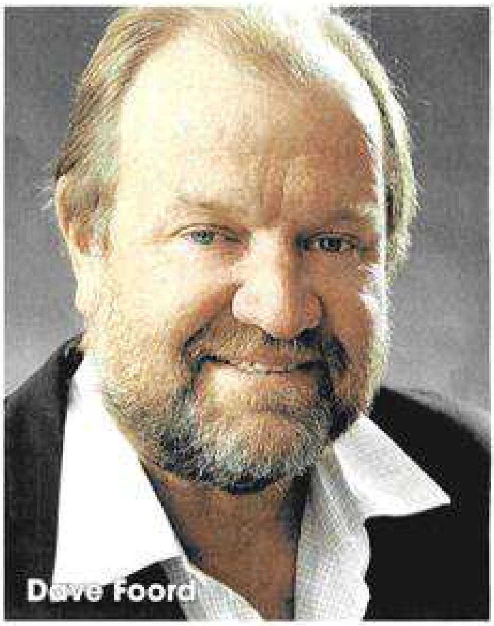
When it comes down to narrow funds in which an individual is making the specific investment calls, individual influence can be the critical factor. These tend to be specialist funds, following particular equity or bond investment styles or mandates. We've examined the performances in some of these sectors to look for stand-out managers and focused on equity funds where variation in performance can be significant. Some of the sector styles are arbitrary – there happen to be three worldwide specialist technology funds, but no specialist worldwide mining funds. Other sectors have a universe of just one fund.

There's one further source of confusion in assessing performance: fund managers change. If you consider the **Stanlib Worldwide Technology Fund**, the performance is impressive, with a consistent top place of the three funds on one-, three- and five-year performances. Yet the fund was managed until early 2008 by Stanlib's head of research, David Gibb. It is now run by Theo Botha. Who should take the credit for the strong performance? The answer is probably both. Indeed, the fund management industry has more than its fair share of staff turnover. A manager can establish a strong track record for a few years, then use that as the basis to move into a more senior role or set up their own shop.

We've dug through the universe of funds to select some gurus who stand out.







That's chiefly because of performance, but also usually because they've been around the block a few times and developed a strong following. Here's our list of SA's top individual gurus.

Kokkie Kooyman – financials guru

Kooyman has attracted worldwide attention for his management of **SIM Global's International Emerging Markets Financial Fund**. But Kooyman has kept his hand in the local waters, also managing the **Nedgroup Investments Financial Fund** on an outsourced basis, and has proven he has not lost his local touch. The fund is the best of the six specialist financials funds on a five- and one-year view, and comes third by just a few basis points on a three-year view. Kooyman has always stood out as being on top of the banks, insurers and other financials, and the performance figures prove it. That's largely a function of a long history of managing financials funds, starting with Coronation in 1999.

Sam Houlie – general equity funds guru

Houlie is head of equities at Investec Asset Management, so has a hand in all of IAM's equities management. He's an old hand who began his career at Allan Gray in 1997, then moved on to various shops before settling at IAM in 2006. He manages the low-risk **Investec Cautious Managed Fund** that's delivered middling returns but at very low risk. He shows his stockpicking skills with the **Discovery Equity** fund that he manages on an outsourced basis. It has thumped its benchmark, and ranks second on both a one-year and three-year view in the highly competitive general equity fund group (coming second to PSG equity on one year, and Marriott on three years).

Dave Foord – general equity and foreign guru

Foord is not one for the limelight, but has quietly built a strong equity-based boutique, Foord Asset Management. Well known in the industry for his strident investment views, his general equity fund is within the top five on most period reviews. He's also proven his stripes in international markets, with his foreign asset allocation fund ranking second on a five-year view, and in the top five on other time periods, in a highly competitive space.

Piet Viljoen – general equity and foreign guru

Viljoen left Investec to set up RE:CM as his own investment boutique, which has now grown to 18 analysts. While there have been some performance lulls when Viljoen has moved into conservative cash before the rest of the market, he's generally proven right eventually. That's clearest in the **Nedgroup Investments Managed Fund**, which he manages on an outsourced basis. It's top of its 82-fund universe on a three-year view, fifth in five years and 11th on one year. Viljoen is building a track record for RE:CM's international funds. While not shooting the performance lights out yet, they are ones to watch.

FOOLED BY RANDOMNESS

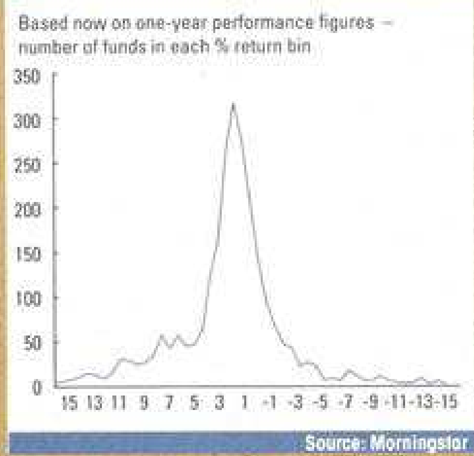
THERE IS ONE major conceptual challenge in measuring fund manager performance – separating random market returns from returns actually attributable to the manager's skills. Most investors approach assessing investment performance by looking at who's above average. That average is usually specified through a benchmark – equity funds, for example, often follow the all share or the Swix top 40 indices.

The assumption is that investors who beat the benchmark (add alpha, in the industry parlance) must be doing something right. Those who are under the benchmark must be doing something wrong. The difficulty is that this is a mathematical truism – half of investors are above average, and half are below. Even if they had exactly the same skills and it was just random luck that led to the differences in their portfolios, half would still be above average. So just looking at the averages doesn't tell you who is getting there through skill or who is getting there through luck.

In fact, the distribution of returns, if it were random, would follow a predictable pattern – a lot near the average, with fewer outperformers and underperformers as you go out to the extremes. Just to illustrate the idea, we created a histogram (as such depictions of statistics is known) of all 2 337 South African-registered funds for their performance over the past year (see graph alongside). This shows how many funds are in each performance "bin" of returns. The average return was 1,96% (pretty sad, we know) and the funds tend to cluster around this return figure (Who "won" I hear you ask? **Stanlib's Global Equity** Fund of Funds).

This distribution is not far off the standard "normal" distribution used by statisticians to indicate complete

SA FUNDS: DISTRIBUTION OF RETURNS

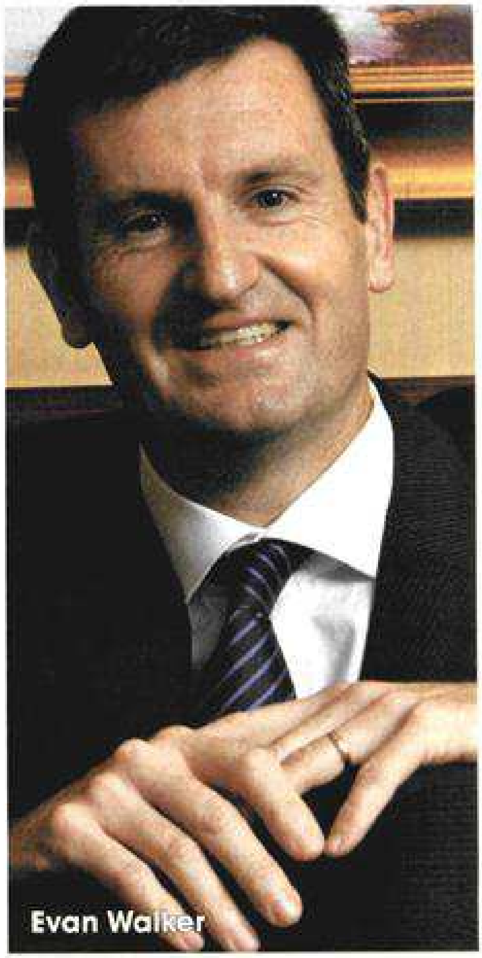


Peter Major – mining guru

Major is a large personality in the fund management industry, having worked his way through various mining roles before joining the fund management industry with Allan Gray. He's since moved around, including a stint managing Mark Shuttleworth's assets and starting his own mining company. He joined Cadiz in 2006, where he is part of the corporate solutions team, and manages **Nedgroup Investment's mining fund** on an outsourced basis. That's been the best performer of the eight-strong group on a three-year view, and third on five- and one-year views. He also manages **Nedgroup's growth fund**, which is middle of its peer group.

Evan Walker – smaller companies guru

It's not often that a fund can come top of its group on one-, three- and five-year views. But the **RMB Small/Mid-Cap Fund**, managed by Walker, does it. Walker joined RMB in 2007 from Credit Suisse Standard Securities and has pulled the fund's performance into good shape. The small-cap segment has seen some disasters over the years but Walker has proven he can deliver consistently. He is a value seeker, choosing quality, dividend-paying companies outside the top 40.



randomness. For example, people's height in a population follows a normal distribution, as do rainfall measures. (Whether markets do follow a normal distribution is a matter of fierce academic debate – that's why we've been careful to say it's "not far off" so we avoid a pack of statisticians baying for our blood.)

Some argue that this is all there is to investment returns. In any normal (like) distribution, you are going to have some brilliant outliers, some dreadful laggers, and a lot in between. Even Warren Buffett, considered by many to be the world's best investor, may just be an outlier that would naturally emerge from a random distribution – just far out at one tail-end.

The sceptics hold that the media and our own psychologies do make this all appear as if there is a real outperformance going on. We focus on those who are above average and attribute all sorts of skills to them. Magazines put them on front pages and people write books about their investment strategies, building a narrative that translates blind dumb luck into investment genius. Psychologists put this down to an innate need humans have to attribute cause to events – we just don't like seeing things as random. Perhaps we are completely fooled into thinking the randomness is a real skill.

But the sceptical view takes things too far. Yes there is a lot of dumb luck in investing. But that's not all there is to it. Some simple thought experiments reveal why. Imagine we all agreed with the sceptical view that market returns were random and all we could hope for was the average. By that logic, we'd all just invest in the market as a whole, say by buying index trackers. But if everyone did that, there would never be any movement in prices as no one would change their view on what a particular stock is worth. That would be irrational – over time some stocks would perform better than others, and it would become obvious that you could improve your returns simply by switching to the relatively better performers (think of it in terms of those who increase dividend payments faster than others). Even if the distribution of outperformers was random, you could still switch to the outperformer and that would not be random.

But it's safe to go a step further and argue that some companies can be anticipated to be outperformers. Businesses are not created equal. Some have better quality products, others have better people, some have both. The question is whether a fund manager is able to tell which is which. IM


John Biccard

John Biccard – value guru

Value investing is viewed by many as the dominant investment style, and Biccard has proven over the years that he applies it best. He manages **Investec's Value Fund**, which comes out top of its 16-member peer group on a one- and three-year view, and third on a five-year view. Biccard has been at it for more than a decade, making him one of the longest serving, and most consistent, fund managers around. While the big houses have designed value-seeking strategies, Biccard shows how to do it at the stockpicking level.

Gavin Joubert – emerging markets guru

Coronation's Joubert started its emerging markets fund four years ago and manages to rank top of the foreign funds flexible asset allocation category on one- and three-year views. He took on the international role after managing various local equity and balanced funds at Coronation, which he joined in 1999. It's a 39-fund universe that also includes Piet Viljoen's global fund. IM


Gavin Joubert