Seed Weekly

Income Investing in the Current Environment

Most investors – whether wealthy or poor, young or old – should allocate a component of their investment portfolio to a low-risk bucket. This low-risk bucket is there to cover a variety of needs. A monthly income for investors that have retired, or emergency savings for a young couple that has just bought a house and started a family, are just two of the potential needs for this pool of low-risk assets. Each investor's individual requirements will dictate how much they should have stashed in this low-risk bucket, and a good financial advisor will be able to assist with this calculation.

Most advisors recommend setting aside 3 – 12 months (depending on how secure your monthly income stream/salary is) of your net salary into an emergency fund. For those investors at or near retirement, the recommendation is usually a bit higher, where your low-risk bucket might be required to cover up to 3 years of income needs. In short, it is likely that between 3 months and 3 years of your monthly expenses should be in an investment that is readily available, and not overly exposed to the vagrancies of market volatility.

While this could constitute a small component of a client's net worth, it makes sense that it is looked after with the same care as their other assets. All too often we see excess savings sitting idle in a bank or savings account, and a good advisor would be remiss not to try and optimise this component of a client's portfolio. While it does makes sense to have a buffer in your bank account, leaving it all there (a) leaves money on the table as the interest rates in bank account aren't usually competitive with other options, and (b) could tempt you to spend it in a way that wasn't planned (i.e. spending 'emergency savings' on an overseas holiday, or spending 'October's income' on a fancy new bicycle in August).

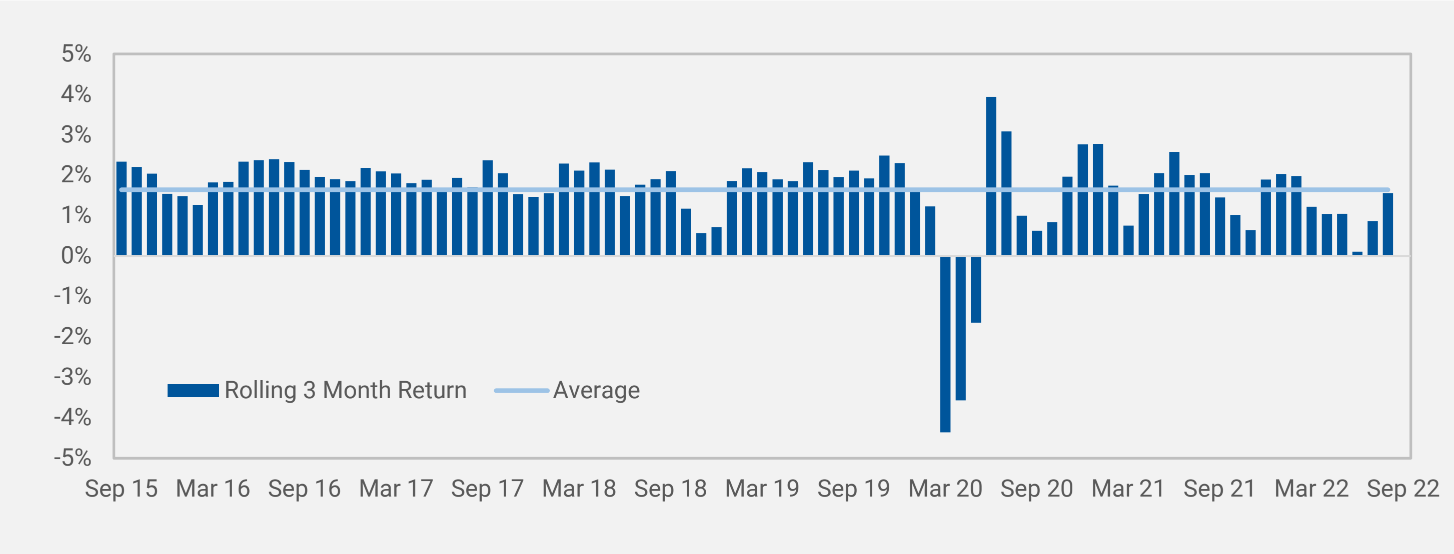
Money market unit trusts have historically been an excellent place to park short term / low-risk savings. Over most of the past two plus decades, they have generally been able to generate returns above inflation and thus, maintain purchasing power. This has all changed with yields currently sitting well below inflation. It is difficult to see when money market assets will deliver healthy positive real yields again.

Government bonds offer investors double digit yields for those willing to invest for 10 years, but the downside is that bonds can be very volatile when compared to money market. They typically experience at least one 5% drawdown per year, and during the Covid sell down fell nearly 20%.

Our view is that funds in the Multi Asset Income category offer investors the best of both worlds. Money market / cash linked investments typically constitute the bulk of the assets, and managers are also able to allocate a portion of assets to bonds and other income assets when value is on offer. This is all done within a risk-controlled framework that should satisfy most investors' low-risk bucket.

The Seed Income Prescient Fund falls into this category. It has a track record of over 7 years and has experienced 2 major market dislocations – Nenegate at the end of 2015, as well as Covid in the first half of 2020. Over its full history, it has delivered positive monthly returns 96% of the time (i.e. only 3 negative months) and when measured over rolling 3 month periods, has only delivered negative returns for a brief period during Covid.

The chart below shows the Fund's rolling 3 month returns since inception –



Over the long term, Multi Asset Income funds have been able to outperform Money Market funds by around 1% pa with a little extra volatility. There are times when they are more attractive – and other times when they won't add much value – but the benefit for the Investor / Advisor is that the portfolio managers are making the decisions to shift between the various income asset classes.

The Seed Income Prescient Fund's current gross yield is approximately 9.25% and is more than 3% higher than the typical money market fund, as it has a reasonable allocation to government bonds and other higher yielding assets. While they do bring their own risks, we constantly ensure that risk taken at the fund level is appropriate for those investors that either require monthly income from their holdings, or those who park their emergency savings into the Fund.

For any questions around Income Investing, please reach out to your Financial Advisor or contact our Investment Team on investmentteam@seedinvestments.co.za. We would love to hear from you!

Take care,

Mike Browne *CFA*
Portfolio Manager

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Past performance is not necessarily a guide to future performance. Performance has been calculated using net NAV to NAV numbers with income reinvested. The performance for each period shown reflects the return for investors who have been fully invested for that period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestments and dividend withholding tax. Full performance calculations are available from the manager upon request.

Prescient Management Company (RF) (Pty) Ltd are registered and approved under the Collective Investment Schemes Control Act (No.45 of 2002). Collective Investment Schemes in Securities (CIS) should be considered as medium to long-term investments. There is no guarantee in respect of capital or returns in a portfolio. CIS's are traded at the ruling price and can engage in scrip lending and borrowing. The CIS may borrow up to 10% of the market value of the portfolio to bridge insufficient liquidity. A CIS may be closed to new investors in order for it to be managed more efficiently in accordance with its mandate. CIS prices are calculated on a net asset basis, which is the total value of all the assets in the portfolio including any income accruals and less any permissible deductions (brokerage, STT, VAT, auditor's fees, bank charges, trustee and custodian fees and the annual management fee) from the portfolio divided by the number of participatory interests (units) in issue. Forward pricing is used. In the event that specific CIS in securities are mentioned please refer to the relevant Minimum Disclosure Document in order to obtain all the necessary information in regard to that unit trust. In rare instances redemption transactions may be subject to a redemption fee. The applicable Prospectus and Key Investor Information Document will be made available upon request.

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