



RLS Financial Services investment philosophy and approach:

Creating a measure of certainty where uncertainty reigns.....

Some investment Fundamentals:

Risk versus Volatility

'Risk' and 'volatility' are not the same thing. Think of risk as the potential of permanent loss of capital, whereas volatility is essentially the fluctuation in an investment's value. Different types of investments carry different levels of fluctuation, and also deliver different returns. Asset classes with the potential for greater returns are associated with increased short- to medium-term volatility. Although the dips and troughs in value from a volatile investment should be on paper only, they result in permanent capital loss if you disinvest at the wrong time. You should avoid volatile asset classes if you know you will need to access your money in the short term. However, just because an investment is more volatile does not necessarily mean that it more risky in the long term. The real risk is permanent capital loss, not how smooth the ride is.

Consider your time horizon:

Your time horizon has an important impact on your choice of savings vehicle and how much you need to contribute. Saving for short term goals provides the foundation for financial security. Short term goals can include putting money away for an emergency fund to cover unexpected expenses and to act as a buffer for potential short-falls. Your medium- and longer-term objectives could vary, from saving for your child's education or wedding, for example, to saving for your retirement. Since different types of investments behave differently over time, knowing how long you have to invest, and thinking about when you might need access to your money, can help you decide how much short-term volatility you can afford.

It is important to put a plan in place and to pick the investments, or combination of investments, that are appropriate for each objective and time horizon. A longer time horizon usually means you can afford to take some risk with your money to achieve growth that contributes meaningfully towards your goals. If you are going to choose more risky investments, however, you need to be comfortable with market fluctuations.



Returns do not come in a straight line.

If you decide to draw money early from a long-term investment – either because you need it or because you lose your nerve – you run the risk of locking in losses if the market is going through a down period. On the other hand, choosing to save in a bank account, or with a very stable investment product, presents you with **another risk: inflation**. Over time, inflation erodes the value of your money, leaving you able to buy less with the same amount of Rands. Unfortunately, even if you save consistently, if the money you put away doesn't grow enough to at least have the same amount of purchasing power at some point in the future, then you are not being rewarded for your discipline and sacrifice and you are in fact losing money.

Bringing it all together:

RLS Financial Services applies a time weighted investment philosophy that has been formulated by MI-PLAN and we utilise MI-PLAN's propriety software to construct your individual investment plan and maintain the plan over its lifetime.

MI-PLAN offers a unique approach to financial planning that matches your future income needs to the key decision of how best to allocate your assets all the way through your life.

During your life you will save and spend. The choices you make in each phase will define your retirement. Most service providers describe your retirement plan as either a "lifestyle" choice or choice that tries to address your attitude to risk.

MI-PLAN has developed an approach that moves beyond either. The approach encapsulates two key components - **income and portfolio allocation**. In developing this approach MI-PLAN has integrated the latest thinking in the field of portfolio management with the principles of sound financial planning.

MI-PLAN's approach does not seek to create an investment strategy based on your attitude to risk or even your desired lifestyle as we have found the investment logic behind these approaches too subjective and often lacking in foundation. In order to resolve this problem MI-PLAN has developed an approach to financial planning that matches your future cash flow needs to the key decision of how best to allocate your assets. The optimal deployment of this decision has a material impact on your financial plan.



Planning: the essence of surety:

MI-PLAN's approach incorporates a few simple yet important principles and observations:

- Your financial needs span a number of time horizons.
- Risk is a function of time and not some subjective measure based on an assessment of desired lifestyle or attitude to risk.
- Risk needs to be modelled over different time horizons.
- Based on the assessment of how risky asset classes behave over different time periods, MI-PLAN is able to model how best to deploy your assets to optimise the growth that can be achieved vs the risk taken.
- Meeting future cash flows with a high level of certainty is based on the same principle. MI-PLAN's approach explicitly models how asset class risk changes as time periods shorten - thereby accurately matching your cash flow requirements to the asset deployment decision.
- Market volatility is a fact of life for every investor. Many financial planning programs base their final recommendations on the unlikely premise that you'll receive a set rate of return on your assets year after year. Failure to take into account varying annual returns can have a substantial impact on your retirement assets.

Wealth creation - Savings : the intelligence of foresight:

There are a few common premises when considering creating wealth, and more specifically retirement security. If risk is considered, too often the cost of taking insufficient risk is not evaluated in the equation.

Another common fallacy is that most investors only think of wealth creation as being important before one retires. All the focus after the retirement date then generally focuses to protecting the wealth that has been accumulated at that point. This results in portfolios being shifted in their entirety to short term risk averse funds.

However, research shows that the proportion of retirement funding financed by contributions to savings vehicles (e.g. retirement annuity funds etc.) comprises only 20% of your total consumption requirement. Investment returns comprise over 80% of your retirement funding.

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Put differently, of the R1 that you will consume during retirement, 19c comes from the money you saved, 40c from the investment returns on these savings and an astounding 41c from investment returns generated **after** retirement.

	CONTRIBUTIONS	RETURNS	TOTAL
PRE-RETIREMENT	19c	40c	59c
POST-RETIREMENT	-	41c	41c
	19c	81c	100c

Source: Russell Research - A modal for pension fund growth

Retirement - Spending: the knowledge to do so wisely:

The problem

As a retiree you face the problem of how best to construct an appropriate portfolio of investments in order to both continue to build wealth and to ensure sufficient cash flow (income) during retirement. Most approaches use the concept of risk profiling. A number of problems exist within the risk profiling framework that, if not clearly understood, could have negative consequences for clients.

- The use of a single fund to meet both present and future cash flow or income requirements limits the effectiveness of meeting both objectives.
- Taking too little risk and the low return could result in you outliving your capital.

For example, you are 60 and have accumulated R 5 million in retirement funding. You want to be able to draw R 500 000 every year. In order to fund this, you would need to draw 7% of your capital each year for the rest of your life. However, you are likely to run out of capital by the time you are 72. The common approach to resolving this problem is to increase the level of estimated or targeted return achieved on the assets from say 3% p.a. to 5% a year. If you experience a market collapse in your early years, paying your income out of this more risky fund will erode your capital base and you run the risk that your income does not last for your lifetime!



The Solution:

The **MI-PLAN** solutions incorporate the ability to model the impacts of changes to your income withdrawal rates with the consequent changes to your investment strategy. The MI-PLAN software assesses these variables based on the time limitations of your portfolio and accurately determines how long your capital will last.

Time diversification and the significance of investment time horizons

As time horizons shorten, the opportunities for investment in higher risk assets decrease. The volatility of risky assets tends to decrease over longer investment time horizons and conversely increase over shorter periods. This, known as time diversification, is essential in understanding why you need to be holding risky assets while your time horizons are still long i.e. at the beginning of your retirement.

How it works in practice:

1. An annuity is a defined series of future cash flows (your annual income requirements).
2. Each cash flow therefore defines the investment time horizon for a small portion of the fund.
3. By structuring and managing the portfolio correctly it is possible to ensure that each year's income requirement is drawn from a part of the portfolio that has a very low volatility (i.e. cash). This process protects the income draw-down from market risk.
4. Asset class risk, and consequently portfolio risk, increases as the investment time horizon shortens. It is important to have exposure to volatile assets, such as equities, in order to achieve real capital growth over the longer term.
5. A rigorous and robust cash flow matching process, through time based evaluation of risk, allows you to maximize the real growth of your portfolio and achieve a degree of certainty with respect to your annual income requirements.

And the implications for your portfolio construction?

1. A range of building block funds that span the risk spectrum is then selected by MI-PLAN software. These funds are managed according to real return targets and investment time horizon.



2. MI-PLAN software sets out your annual investment allocation between these funds taking into account the income requirements as well the changing requirements on building your capital.
3. You will need to switch annually between these funds based on your future capital withdrawal requirements.

The partnership - Our unique approach:

Retirement Partnership

We adopt a partner for life approach in our financial planning model. We assist and partner selected financial planners in the construct of your plan, setting a sustainable path for your life. Importantly, we continue to partner you along this journey. Each year the performance of your portfolio is compared to the original advice, to ensure that the plan is still on track. Where necessary, changes to the portfolio and / or income levels are made as soon as the need arises to ensure the long term sustainability of your assets.

Which introduces financial intelligence and emotional maturity

Research has shown that greed and fear present the greatest danger to the implementation of a sound financial plan. They also interfere when trying to establish a client's appetite for risk on a subjective basis.

The MI-PLAN approach of matching your cash flow with the key decision of how to allocate your assets based on time diversification introduces a mathematical or quantitative intelligence and removes emotional bias. The complex math behind achieving the primary objective of providing a sustainable income for life is elegantly captured in the MI-PLAN software.

Through the use of time based risk management

Asset liability matching or time based risk management are the technical names given to our unique process of selecting funds or asset classes based on the investment time horizon. This process is based on quantitative research which indicates that the time to maturity has the most significant impact on risk and in turn the attainment of any income goal. While a riskier asset class such as equity provides for the best returns it also introduces the most risk. However time diversification, or holding equity for an appropriate longer time horizon, reduces this risk to a manageable level. Your portfolio is allocated by matching your cash



flows (or income needs) based on your time horizon, providing cash when you need it from a low risk low return portfolio and growth when you don't need the cash.

To deliver an objective based investment approach

At the heart of it, we only save to allow us to consume later, whether in our lifetime or our heirs. Therefore the MI-PLAN approach focuses solely on the achievement of the goal of providing sustainability of income for life. Trying to time the market or buy the best fund seldom produces the correct result and is doomed to fail in the long term. More significantly it does not have any relevance to the reason for our decision to save.

Unique product range and philosophy - Objective Based Investing

Risk taken without reference to your time horizon decreases the probability of achieving the required investment return. Add the complexity of the types of funds available for selection, (asset, sector, or geographic class) to the mix and choosing the right fund, or funds, becomes more a matter of luck than the application of investment intelligence.

The MI-PLAN range of funds span the risk spectrum and have been set up to target a specific outcome, based on an investment time horizon. Each fund is managed according to a real return target (or outcome) and specified investment time horizon:



The essence of Investment Management is the management of Risks, not the management of returns – Benjamin Graham

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Conclusion:

Utilizing the above approach I look forward to advising and assisting you to construct the optimum portfolio to maximize and achieve your investment objectives.

Ryan Smith

Client Signature

Client Name:

Date:

Date: