You can drown in water averaging 30 cm deep

There is a saying that you can drown in water averaging 30 cm deep. The principle behind the saying is that an average, is simply that, and a water mass averaging 30 cm deep can at some places be 3 meters deep. If you find yourself in a situation where you can't swim, the knowledge that the water depth only averages knee height, will have no value to you at all.

Unfortunately, this is a common human error when it comes to the average growth on your investment, and could prove especially costly for those close to retirement or recently retired. Let me illustrate what I am trying to say by using an example. Below you will see the average annual return achieved by one of the best fund managers over a period of 20 years from 4/10/94 – 30/09/14 in a balanced fund.

Average growth per year since inception (4/10/94 – 30/09/14)	9,93%
Average growth per year over the first 10 years (1994-2004)	8,42%
Average growth per year over the next 10 years (2004-2014)	11,91%

The fund fact sheet shows an average return of 10.3% per annum over the last 10 years. This period includes the market crash of 2008. People will comfortably invest their long-term retirement savings in a fund with such return figures, especially considering that most quality fund managers had similar performance. Consider the table above, and notice that the difference in the average return between the first and second decade is nearly 3.5% per annum for the exact same fund. It is important to consider what the impact would be on your investments if your first 10 years of retirement experience similar returns to that in 1994 – 2004 compared to the more favourable returns between 2004 – 2014. The graph below will illustrate the difference:

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In the above projection, I assumed the retired individual makes an income withdrawal of 6% per annum (gross) of his capital, escalating at 7% annually to keep up with inflation. Assuming this fund will achieve the same return over the next 30 years compared to the last 20 years (very dangerous assumption to begin with), we will see that the funds will last until age 90 before it is completely depleted. If his retirement years start off with a period achieving meagre returns (as in 1994-2004), his capital will be depleted 2 years earlier. If it was the other way around and he had the peak years first (like people who retired 5 years ago) his capital would probably last until age 93. The order in which growth phases occur (high-growth vs low-growth) makes a 6-year difference (or 72 pay-outs) in terms of how long the funds will last.

Am I implying that you should time the market and only invest in funds following a period of low growth? Not at all, but here are some aspects that you need to consider from the above.

· Predictions are of no use to man or beast, but if someone holds a gun to my head insisting on a prediction of how the next term of growth on our investments would be like, considering similar funds like a balanced fund with 75% exposure to SA assets, I would have to say we are going to experience a lower growth period.

· If this was the case, it would be prudent to ignore the past 10 years' performance on these types of funds and adjust your expectations to roughly 70% of those performances. Provided you incorporate these expectations into your planning, and your planning still adds up, it shouldn't result in sleepless nights. If you are currently achieving long-term average growth of 10%, ensure that your capital will still achieve its goal if it only grows with 7% per annum.

· Diversification and sensible asset-allocation is going to be more important than ever. It is very important to avoid expensive assets, but still have enough growth assets in your portfolio to outperform inflation in the long run.

· If you barely have enough funds to retire, and your portfolio mainly consist of shares, then you are playing a very dangerous game because performance on pure growth assets could be a lot weaker for longer than illustrated above. It can ruin your retirement planning if the markets would fall shortly after your retirement date and you need to survive on those funds. Remember, you can't fix your shortfall before retirement with higher than normal returns (and per implication higher risk).

· Dismiss any idea of 'timing the market'. Only on very few occasions does a strategy of timing the market fit into an individual's personal financial planning. If you are a balanced investor, your portfolio would relatively withstand dramatic market collapses relatively well, where if you are an aggressive investor you should have time on your side to rectify the collapse (even if it was a big one).

· Be very careful to change your strategy after retirement on a reaction to the market. Too many people changed their strategy during or after the 2008 crash to a more conservative portfolio. This had a huge impact on the long-term outcome, since it exaggerated a sluggish recovery instead of simply leaving the asset allocation unchanged until it rectifies itself.

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