

advantage life stage plus

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Executive summary

The Advantage Life Stage Plus portfolio provides investors with a unique life stage product that can address both the pre-retirement and post-retirement requirements of fund members.

During the pre-retirement accumulation phase, this product provides members with an actively managed multi-manager solution that targets inflation-beating returns within a robust, risk-controlled framework.

As members move closer to retirement, Life Stage Plus automatically begins to underpin a member's accumulated savings with a capital preservation and interest rate sensitive strategy, providing members with liability matching features.

- Structuring the pre-retirement solutions entails using variable exposures to two core building blocks: a high equity portfolio as well as a capital preservation portfolio (both on Advantage's platform).
- The pre-retirement solution can be fine-tuned with respect to required funding targets (inflation targets between CPI+2% and CPI+6%, capital growth, capital protection and liquidity needs). This is achieved by combining different allocations to the two building blocks.
- Pre-retirement has four stages using four different combinations of the two building blocks (100% High Equity, 75% High Equity + 25% Real Return, 25% High Equity + 75% Real Return and finally 100% Real Return).

Life staging starts with the highest exposure to equities (per Regulation 28) in the most aggressive stage and gradually moves to a more conservative strategy, just prior to retirement. Different funds might need different combinations of the two building blocks to meet their specific members' requirement.

- Retirement funds should appoint their choice of a broker and/or financial advisory service. This financial advisory service should be available as soon as the fund is functional and needs to be a continuous facility for members who have the option to review their status, especially as they start to approach retirement.

Three years before retirement, members then have the opportunity to determine their ultimate pre-retirement portfolio that best aligns with their post-retirement plans. The options provided to members are:

1. A blended solution of the fund's High Equity portfolio with the Real Return portfolio, suitable for members wishing to ultimately purchase living annuities with variable income draw downs.
2. The Real Return portfolio, suitable for members wishing to purchase a living annuity on retirement.
3. The Advantage Multi-Manager Bond Fund, suitable for members wishing to purchase life annuities
4. The Advantage Multi-Manager Cash Fund, suitable for members wishing to take a portion of the retirement fund savings in cash.

The key advantage of Life Stage Plus is that, at the point when members actually do retire, they have the benefit of options that range from providing partial liability matching for the purchase of a life annuity through to maintaining a level of exposure to equities (to ensure that inflation-beating growth is maintained into retirement). All of these options also have capital preservation as an inherent feature in the portfolio construction.

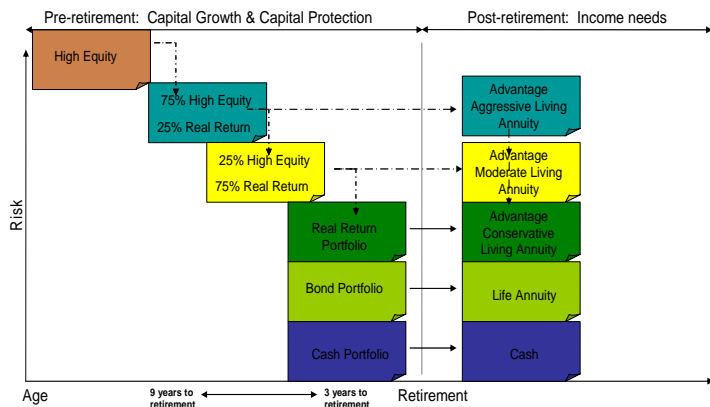
In addition, should the Fund elect to, it could provide members with access to living annuities with the same investment building blocks that can address the full spectrum of post-retirement requirements. The living annuity portfolios have been constructed to give returns from interest type income as well as the potential of growth from capital gains.



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asset managers

The dynamics of Life Stage Plus can best be understood from the diagram below:



While the default option for Life Stage Plus employs the above progression through the Life Stage portfolios, the timing of the portfolio switches could potentially change should the fund and its members wish to reflect a different risk profile or range of terminal portfolios.

Guiding principles of the Advantage Life Stage Plus portfolio

The design of the Advantage Life Stage Plus Portfolio is predicated on the following principles:

Principle 1

Maximum capital growth should be provided for members with a long term to retirement. This is termed the accumulation phase.

Principle 2

A member's investment horizon does not end at retirement; it can extend for decades thereafter. This is termed the retirement phase.

Principle 3

Members should maintain asset growth at least in line with inflation, especially when close to retirement.

Principle 4

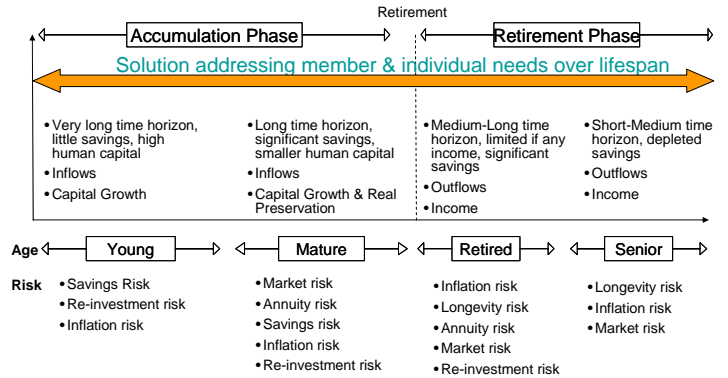
A member's exposure to growth assets should be maintained. Members do actually have time to recover from small market fluctuations. Members close to retirement have a higher savings base on which to generate additional wealth.

Principle 5

Although exposure to growth assets should be maintained, a degree of capital protection is necessary for members with a shorter accumulation horizon.

Principle 6

Risk profiles for each stage should fall within the risk budget of the members of the Fund.



While the default option for Life Stage Plus employs the above progression through the Life Stage portfolios, the timing of the portfolio switches could potentially change should the Fund and its members wish to reflect a different risk profile or range of terminal portfolios.

Guiding principles of the Advantage Life Stage Plus post-retirement offerings

If the trustees and their advisors elect to include a range of post-retirement living annuity offerings to their members, the principles we apply to our post-retirement living annuity products are as follows:

Principle 1

Smooth and cost effective transition from pre- to post-retirement portfolios.

Principle 2

Solutions should be flexible and cost sensitive to cater for different retirement needs.

Principle 3

A range of optimised asset allocations should provide for members' flexible income requirements.

Understanding the underlying investment building blocks

We believe there are two viable options that could be considered for the High Equity building block:





Option 1: A High Equity portfolio that incorporates a high beta equity blend, managed to the FTSE/JSE All-Share Index.

Our proposal for this option addresses the following considerations:

- How to derive the maximum international exposure for members in an environment where nearly half of consumer expenditures (future liabilities) entail consumption of products that have been manufactured or sourced offshore. Realising that effective optimal international blends are constrained within current legislation that restricts offshore investments to 20% of assets.

Portfolio implementation: Equity exposure in the portfolio is benchmarked against the FTSE/JSE All-Share Index which holds the maximum exposure to rand hedge stocks of all the domestic listed benchmarks. This indirectly exposes members to the international markets in which these rand hedge stocks operate.

- How to maintain a high beta exposure, ensuring that the equity exposure over the long term is properly matched to meet members' inflation-related liabilities.

Portfolio implementation: Design a multi-manager equity blend that maintains a relatively high beta (above 0.90) to the benchmark.

- While introducing alpha (excess return potential) that does not dilute this required beta exposure.

Portfolio implementation: Introduce low risk, alpha enhancing strategies such as a 130/30 portfolio in the portfolio blend.

- How to capture diversified alpha in the international arena that isn't simply a function of the volatility of the Rand.

Portfolio implementation: Integrate into the solution range of uncorrelated alpha Funds for the international equity exposure and hedged global bonds for the international bond exposure.

Option 2: A High Equity portfolio that attempts to approximate the best of traditional balanced manager performance by incorporating an equity blend managed to the SWIX benchmark and a Tactical Asset Allocation overlay strategy.

Our proposal of this option addresses the following considerations:

- How to ensure that members don't become concerned that the High Equity portfolio might veer too dramatically from the performances of other traditional balanced portfolios while still benefiting from the robustness provided by a multi-manager investment strategy.

Portfolio implementation: Benchmark the equity blend against the SWIX benchmark, the benchmark more commonly used by South African equity managers. Introduce a Tactical Asset Allocation overlay strategy for the bulk of the accumulation phase to ensure that the asset allocation on the fund, even during this early period, is responsive to changing market dynamics.

- How to maintain a high beta exposure, ensuring that the equity exposure over the long term is properly matched to meet members' inflation-related liabilities.

Portfolio implementation: Design a multi-manager equity blend that maintains a relatively high beta (above 0.90) to the benchmark.

- While introducing alpha (excess return potential) that does not dilute this required beta exposure.

Portfolio implementation: Introduce low risk, alpha enhancing strategies such as the Portable Alpha portfolio into the portfolio blend.

- How to capture diversified alpha in the international space that isn't simply a function of the volatility in the rand.

Portfolio implementation: Integrate into the solution a range of uncorrelated alpha funds for the international equity exposure and hedged global bonds for the international bond exposure.

Discussion of the Real Return portfolio—combined with the High Equity portfolio

The Real Return portfolio is a conservative market linked portfolio that gives inflation targeted performance while protecting capital over rolling 12-month periods. The primary objective is to give sustainable positive real returns while protecting investment from downside risk.

Below is a short discussion of the main features of this product:

Investment philosophy

The investment philosophy of the portfolio aims to add value through: enhancement strategies per asset class (equities, bonds, cash) that gives incremental performance over time, the use of an objective asset allocation process determined by relative pricing and risk targets, and where opportunities exist, locking in returns and raising the return profile through hedging and the use of derivatives.

Asset allocation

Asset allocation is actively managed to adapt to changing financial markets. The fund will invest in equities, bonds, cash and protection strategies.





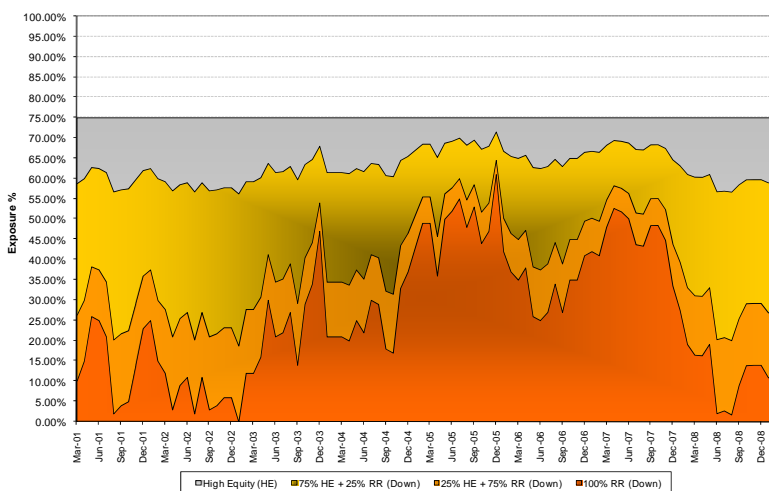
Benchmark

This fund aims to deliver positive returns and to beat inflation +3% over the medium to longer term. The benchmark therefore is headline inflation plus 3%(CPI+3%).

Understanding how the portfolio structure impacts asset allocation over time

To appreciate the power of the design in the Life Stage Plus product, the chart below provides an insight into the variability of the asset allocation that the combination of the High Equity Portfolio and the Real Return portfolio provides to members over time.

Effective Local Equity Exposure in Negative Markets



Note the two critical periods of equity decline towards the end of 2002 and the 2nd quarter of 2008. During both of those periods, the effective equity exposure in the Real Return portfolio went to nearly zero or around 5%. Over those same periods the effective equity exposure of the 25/75 blend went to around 20% (inclusive of international equity exposure) and in the 75/25 blend, the effective equity exposure went to 55% (inclusive of international).

In essence the Advantage Life Stage Plus portfolio provides members with that critical flexibility in asset allocation just as the time diversification benefit starts to wane.

Note: The portfolio complies with the prudent investment guidelines set out in Regulation 28 of the Pension Funds Act. This fact sheet does not purport to offer advice or make any recommendation. Always consult with your professional advisor before making any investment related decision.

- Authorised as a financial services provider (FSP) under the Financial Advisory and Intermediary Services Act, 2002 number 19840
- Registered as an administrator in terms of Sec 13B of the Pension Funds Act, number 24/401 E&OE

Advantage Asset Managers Registration Number 2004/023064/07

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