

29th December 2021

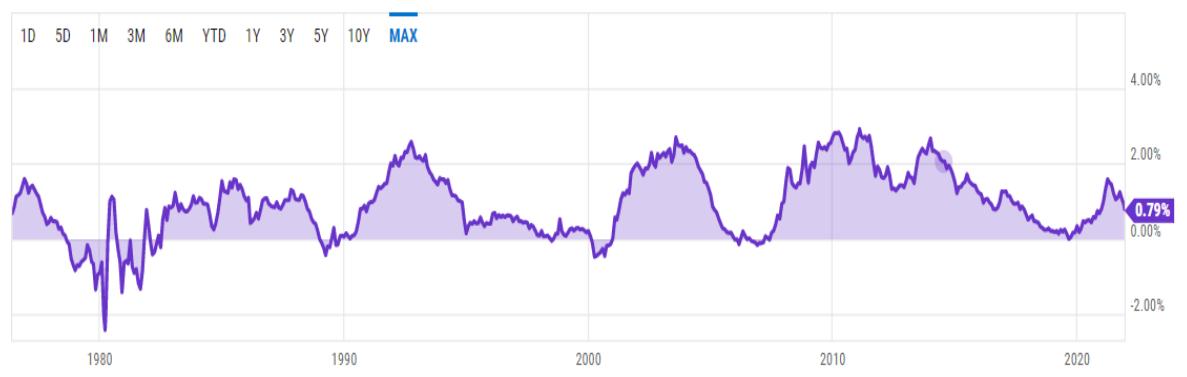
When the music stops

Is the market expensive?

The average S&P 500 price-earnings (*P/E*) ratio is 29,61 versus its mean of 15,95 and median of 14,87. This highlights the stretched valuations of US stocks, especially the top 50 companies within the S&P 500 index. It is significant to note, that over the past 44 years, such high price multiples have never endured for a sustained period.



The US Federal Reserve (*the Fed*) has recently indicated the end their ongoing bond buying program (quantitative easing) and their intent to begin raising interest rates. This is in response to inflation running above its long-term average (The current inflation in the US is 6,2%). Owing to the Fed's policy change, treasury yields (espically the short duration bonds) have increased. The current 10-year Treasury Yield is 1,51% and the 2-year Treasury Yield is 0,70%. The treasury yield spread tightening (the difference between the 10 and 2 year treasurey yields – refer to graph below). Historically, the crossing of the spread has indicated an upcoming market recession.



In considering the following factors:

- Continued elevated inflation,
- Ongoing shut-downs due to various COVID variants,
- Stretched valuations,
- S&P 500 trading above long-term indicators, and
- The change in Fed monetary policies;

We anticipate a market rotation.

As a house, we have:

- Reduced client portfolio exposures to high beta, growth equities and property stocks.
- Increased exposures to consumer durable, defensive stocks.

We continue to remain underweight in fixed income and Treasuries in the short-term

Situs Tax

The standard route to structure South African and offshore investment portfolios, has been via a local or offshore trust. The benefit of a trust was the avoidance of estate duty, as the value of an estate is pegged whilst capital growth occurs within the trust.

However, with the introduction of SITUS taxation in the United Kingdom and United States, tax is levied on property (including physical and non-physical property, such as shares) where it is located for legal purposes.

The effects and considerations with regards to structuring investment, are numerous. The table below, lists a comparison for estate duty and situs tax, as levied in South Africa, the UK, and the USA, on persons holding assets from these jurisdictions, at the time of their death. This comparison includes the effect for a person who was a South African resident at the time of his/her death and who had utilized his/her permissible foreign capital allowance during his/her lifetime.

Country	South Africa (SA)	United Kingdom (UK)	United States of America (USA)
Name	Estate Duty (ED)	Inheritance Tax (IHT)	Estate Tax (ET)
Rate	20%	40%	40% (maximum)
Threshold	R3,5 million	£325,000	US\$60,000
Roll-over relief between spouses	Yes, therefore R7 million upon death of surviving spouse	Yes, therefore £650,000 upon death of surviving spouse	The surviving spouse may make use of a unified credit of up to \$13,000. Property passing to a qualified domestic trust (QDOT) is also excluded.
Immovable Property	Subject to ED in SA	Subject to IHT in UK	Subject to ET in USA
Equities	Subject to ED in SA if Company issuing the Shares was incorporated in SA	Subject to IHT in UK if Company issuing the shares was incorporated in UK	Subject to ET in USA if Company issuing the shares was incorporated in USA

Unit Trusts	Subject to ED in SA if register of unit holders kept in SA	Subject to IHT in UK if register of unit holders kept in UK	Subject to ET in USA if incorporated in the USA
Foreign Collective Investment Schemes	N/A	Generally excluded from IHT in UK	Generally excluded from ET in USA
Assets held by a trust	South African Registered Trust: The assets are generally excluded from the founder's estate. The value of assets settled on the trust by way of loan account is generally pegged	Offshore Registered Trust: 10-year charge on UK situs assets. This is usually overcome by incorporating an offshore company (the shares of which are owned by the offshore trust) to acquire the UK situs assets	Offshore Registered Trust: Generally excluded from ET in USA, provided there are no US resident beneficiaries
Assets held by an offshore company	N/A	Excluded from IHT in UK	Generally excluded from ET in USA
Assets held in an offshore life policy (life wrapper)	N/A	Excluded from IHT in UK	Excluded from ET in USA

In determining the right investment structure, it is important to note the transparency of the structure. As a house, Rockman Capital advises on the structure that gives clients the most flexibility, having regard to the individual's specific risk tolerances.