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Investing for a
world of change

If it sounds too good to be true, it usually is



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I have learnt the hard way that there are no shortcuts to building wealth. Every time I tried, I lost. Over time, I have come to realise that there are three ways to build wealth.

- 1 Inherit it. For most, me included, this is not an option. I have also explained to my children that this is not an option for them either; there will be little left for them to inherit.
- 2 Steal it. Again, not an option.
- 3 Which leaves us with three: work hard and then let that money work even harder over the long term.

Unfortunately, the unscrupulous among us play on our emotions, our biases, and often our desperation. The hook and the narrative they present are compelling because we so desperately want them to be true.

It's impossible to cover every way people are scammed; the last time I Googled 'Ponzi scheme', for example, nearly ten million results appeared! However, I can highlight some important warning signs and what to look out for.

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The Ponzi scheme

For the uninitiated, a Ponzi scheme is when a con artist offers investments that promise exceedingly high returns, with little or no risk to investors. The scheme is named after Charles Ponzi, who in the 1920s convinced thousands of clients to invest with him. He lured them with higher-than-market returns for investing over a specific period, and then used money raised from later investors to pay back earlier ones. All was well until new investors dried up. And then the scheme collapsed, as a Ponzi scheme can only continue to offer profits for as long as the number of investors keeps increasing. Sound familiar?

In this example, two clear warning signs stand out:

The promise of high returns. Be wary of anyone claiming that you'll earn returns substantially higher than those from traditional investments, especially if the return is promised over a relatively short period.

Any reference to 'little to no risk.' At its simplest level, an investment's return largely depends on its level of risk – the greater the risk, the greater the potential (and required) return. Put another way, the greater the required return, the greater the level of risk that must be borne by the investor.

Alarm bells should ring when someone promises you high returns at minimal risk.

Legitimate investments are regulated, and managers and financial advisors are licensed by the South African Financial Sector Conduct Authority (FSCA), which maintains a list of regulated entities on its website. Always verify credentials on the [FSCA website](#).

Be concerned if you **do not receive regular or quarterly statements** of your investment, and/or you **do not receive any payments** that you have been promised.

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Another major warning signal became clear when reflecting on the most famous Ponzi scheme in recent history – perpetuated by Bernie Madoff, where investors lost an estimated US\$65 billion. Madoff's firm Bernard L. Madoff Investment Securities LLC calculated its own investment returns, which were incredibly consistent over the long term. Investment managers should not be able to 'mark their own homework,' but rather **performance should be independently verified**, and returns should align broadly with the asset class in which the fund invests.

The pyramid scheme

A pyramid scheme is like a Ponzi scheme in that the proponent of the scheme is also looking to take advantage of unsuspecting people by promising them extraordinary returns, if only they invest, and often with a sense of urgency "invest now before the opportunity disappears". Yes, you guessed it, **being forced to commit immediately** is yet another warning sign.

The difference is in execution. A pyramid scheme relies on recruiting new participants, who then recruit others, and so on. Essentially, then, the new investors pay those who recruited them for the right to participate in or sell a certain product. The initial investors who are at the top of the pyramid profit the most. And as more people join, more money gets funneled up the pyramid. But eventually the music stops when those people at the bottom of the pyramid cannot find new participants to join the scheme, and the scheme collapses.

Be suspicious of a scheme if it:

- Requires you to recruit others to earn money,
- Demands an upfront fee to join, or
- Fails to provide financial documents or statements.

A more recent South African example of a pyramid scheme is Mirror Trading International (MTI). MTI was started in South Africa and quickly expanded globally by promising to grow members' cryptocurrency Bitcoin with yields averaging 10% monthly, and substantial bonuses to members for recruiting more people into the scheme. When MTI collapsed in December 2020, it had become the largest pyramid scheme in South Africa's history. It proved to be unlawful and unsustainable, with returns paid to earlier investors from investments made by later investors. A classic pyramid scheme simply updated with a new, compelling narrative – an artificial intelligence foreign exchange trading bot was (falsely) generating the remarkable returns.

And to rub salt into the proverbial wounds, new websites have since emerged claiming to help victims recover refunds. Yet another scam targeting the desperate.

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Other scams to be aware of:

419 scams: Those that promise a significant share of a hefty sum of money in return for a small upfront payment; the classic email 419 scam, where the scammer will often claim to be a foreign dignitary or wealthy individual who needs help transferring money out of their country. Once you pay the fee, the scammer disappears, and the promised money (obviously) never materialises.

Pump-and-dump schemes: Fraudsters inflate the price of a share they own by spreading false or misleading information. Once the share price has been driven up, they sell their shares at an inflated price, whereafter the share price typically collapses. This type of scheme is particularly prevalent in the world penny shares and seldom-traded shares.

Cryptocurrency scams: With the rise of cryptocurrency, new types of scams have emerged. These include fake initial coin offerings where fraudsters create a new cryptocurrency and solicit investments, then disappear with the funds.

Romance scams: Con artists create fake online profiles on dating websites or social media to institute romantic relationships with victims. Once they have established trust, they fabricate a story about needing money for an emergency or some other heart-tugging reason. The victim, believing they are helping a loved one, sends the money, never to see it again.

Employment scams: Fraudsters post fake job listings to collect personal information or money from job seekers. Often, they may ask for a “processing fee” to conduct a background check or to provide “training material.” Once the fee is paid, the job offer disappears, with the victim now also out of pocket.

Charity scams: Con artists exploit people’s goodwill by pretending to be a legitimate charitable organisation. Often, they will create a fake website or use social media to solicit donations for causes such as disaster relief or medical expenses. The donated money never reaches its intended cause.

Lottery and prize scams: Victims are informed that they have won a considerable sum of money or a valuable prize. Again, to claim their winnings, they are asked to pay a fee for taxes, processing, or shipping to claim it. And then, once the fee is paid, the prize does not arrive.

To conclude by stating the obvious, “If it sounds too good to be true, it usually is.”

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Because when it comes to building real wealth, good advice is never a scam.

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