SPONSORED BY
bdb
Your Personal Finance Director

Risky business

When predicting the future at home gets trickier, the temptation to run to safety with your investments rises. But what assets can offer both safety and a return? Karl Tomusk looks at how wealth managers are making money work harder

The word 'uncertainty' could well be the most overused in recent years. Political and economic unknowns in the UK have driven the story for investors as they look for clarity on the future. But a "wait and see" approach isn't particularly helpful when the unknown drags on for years. As a result, wealth managers and their clients have had to put together strategies that work within – and maybe even benefit from – heightened uncertainty.

"Money is still going into all asset classes, but people are perhaps dropping down on the risk scale a little," says Chris Harrington, director at Cowgills Wealth. For example, he has a client who is "normally quite adventurous", but a year or 18 months ago, they moved his investments from high to more moderate risk.

Another shift, says Harrington, is toward investors "dripping" capital into investments. Where previously someone with £100,000 to invest might have allocated that in a relatively short space of time, that client might now take six to 12 months to minimise the risk of volatility.

Step 1: Diversify

"Those who follow investment trends are setting themselves up for failure," says Matt Kiddle, operations director at wealth management firm BDB. He says the firm is guided by scientific evidence when constructing investment advice so short term trends "do not factor" – it would be a "fool's errand" to try to position a portfolio tactically to take advantage of short-term economic conditions. Instead, he encourages a long-term, balanced approach.

He points to global equities markets, which have rallied in 2019. "UK investors who adopt a genuinely diversified approach from a geographical perspective in their stock portfolios will have experienced improved valuations over the last three years," Kiddle says.

Outside of equities, he says bonds have a role to play as a diversifier and risk dampener in any "sensible long-term portfolio".

As a result of that long-term view, Kiddle adds: "We have not had a single enquiry from clients worried about the impact of Brexit on their portfolios."

Having that diversity in your portfolio does mean you have to be wary of how Brexit plays out. "It is an irony to think that a 'good' Brexit can be a problem for some investors," says Michael Craven, head of office at Brewin Dolphin.

He says that in the event of a 'good' Brexit – where the UK leaves the EU with a deal – the point at which the Bank of England's Monetary Policy Committee raises interest rates is likely to be brought forward. "This is usually bad news for fixed interest and equity markets," he says.

With an estimated three quarters of the FTSE 100's revenues coming from outside the UK, values increase as Sterling falls, which means international equities have been more attractive than local ones in recent years. Between 2014 and the start of 2019, Brewin Dolphin calculated the FTSE Local Index delivered a return of -3.6 per cent, whereas the FTSE All-Share index returned 18.7 per cent.

> "Money is still going into all asset classes, but people are perhaps dropping down on the risk scale a little"
> **Chris Harrington**
> Cowgills Wealth

The value of investing in global equities as a UK investor becomes even clearer when comparing different currencies. The FTSE All-World Index has, at the time of writing, risen 15.7 per cent in the year to date (after sharp falls at the end of 2018) in US dollars but 18.2 per cent in pounds.

Investors worried about potential negative impacts of Brexit would have taken steps to hedge against it by positioning their portfolios to take advantage of the fall in sterling. If the Brexit process is nearing any kind of clarity, it might be time to reassess one way or the other.

Step 2: Target income

A combination of a slowing economy and low interest rates means investors are moving toward income-yielding assets.

This includes investing in property or equity funds that target dividend income yield.

"The idea is if we can use funds that have yields of three or four per cent, even if we find over a period of 12 months that markets generally are flat and we're not seeing much in terms of capital growth at all, at least we're generating some return by way of yield," says Harrington.

If markets dip, these funds still pay out on a monthly or quarterly basis, at which point investors can automatically re-invest by buying more units in the fund at a discount. When the markets recover, prices will go up again, ultimately generating growth in a more roundabout way.

One recent trend Harrington has seen is younger clients taking this approach. Traditionally, retired investors would favour income-driven funds because they would

SPONSORED BY
bdb
Your Personal Finance Director

generate cash they could live on, while younger investors would focus on capital growth funds. But Harrington says younger clients, while still looking for long-term capital growth, are more likely to want to accompany that with income-driven funds.

"Having some funds that generate income and some that generate capital growth will hopefully give clients a bit more diversification," Harrington says. Since funds that generate income and those that generate capital growth invest in different asset classes, risk is spread further.

Diversification and exposure to a range of asset classes is the idea that underpins much of Harrington's advice, particularly at times of heightened risk. "Even where a particular market looks positive, one should be very careful in terms of the level of exposure one has to it," he says.

Step 3: Indulge a little bit

Despite that advice, there has always been demand for luxury goods: things that do not produce an income and that, as Kiddle says, is reliant on "greater fool theory", the idea that in order to get a return you are reliant on someone else buying it from you at a greater price.

These investments tend to come from people who are collectors or have an interest and understanding of the asset class they are investing in. Those investments, Harrington says, tend to sit alongside their core portfolios.

Knight Frank's annual Wealth Report tracks some of these markets, including art, wine and classic cars. "There has been an increasing focus on tangible assets since the global financial crisis," says Andrew Shirley, the report's editor.

But recent activity in classic cars, for example, shows how much these markets can shift. Following a bull run from 2012 to 2015, interest has cooled. The HAGI Top Index, which tracks rare classic car sales, rose 2.5 per cent last year (by comparison, returns for the last decade sit at 258 per cent) and has now fallen 2.1 per cent to date this year. Shirley says speculative investors are exiting the market, which means it's once more dominated by genuine collectors.

The biggest outperformer in this year's Wealth Report was rare whisky with a 40 per cent rise in asset value over 12 months.

The fall in sterling has also benefited some asset classes, such as wine, that are traded in the UK, Shirley says. Political uncertainty, "doesn't seem to be having a profound effect on most markets," but he does say there is some concern about the ability to move collections around the EU after Brexit.

After all, there is no escaping volatility right now. The best you can do is balance your portfolio and ride the storm. ■

Asset class return and volatility expectations (5 years)

	Return (%)	Volatility (%)
UK large cap equities	4	14.6
Global large cap equities (ex-UK)	4.7	14.8
Europe large cap equities	4.6	15.8
US large cap equities	4.4	16
Global small cap equities	4.6	17.1
Emerging large cap equities	4.4	20.7
UK government bonds (15+ years)	-3.4	12.1
UK corporate bonds (10+ years)	-1.6	10.3
Global aggregate bonds	0.4	3.3
Global high yield bonds	2.7	7.7
Cash	0.8	0
Global core real estate	2.4	13.4
Real estate mezzanine debt	3.8	10.5

Source: BlackRock Investment Institute, 30 June 2019

Knight Frank Luxury Investment Index (Q4 2018)

	Change in asset value (12 months) (%)	Change in asset value (10-years) (%)
Rare whisky	40	582
Coins	12	193
Wine	9	147
Art	9	158
Average	9	161
Watches	5	73
Cars	2	258
Furniture	1	-32
Coloured diamonds	0	122
Stamps	0	189
Jewellery	-5	112

Source: Knight Frank Research

Macallan Valerio Adami whisky sold for £848,750 at auction in Edinburgh