Insights, Tacit Thought | Weekly Investment Insights

Aligning your investments with your objectives

Published on: 21 February, 2025 | Author: Investment Team

Benjamin Graham's views on asset allocation have significantly influenced Tacit's approach to investment, emphasising a balanced and disciplined approach to portfolio management. His principles, first published in the book *The Intelligent Investor* in 1949, continue to shape how we think about risk management and long-term wealth accumulation in a world where short-term investment trading and new investment products are frequently promoted as asset types—and often represented as having qualities which, equally frequently, do not stand up when markets come under stress.

The Tacit approach, at its core, is based on the concept that there are two primary asset classes into which most investment assets should be allocated: Growth and Stabilisers. This can sometimes be mistakenly viewed as an approach that only invests in equities and government bonds, but this is a misunderstanding of what we mean and of what we do in practice. Our investment universe is as wide as that available to any investor, but the primary difference in our approach is to allocate any investment into one of our two buckets. This is actually no different from the core teachings of Benjamin Graham from nearly a century ago.

Key aspects of Graham's asset allocation thoughts are worth restating at this time, as anxieties around geopolitics are at generational highs and can lead to bad investment decisions.

Firstly, Graham advocated for a balanced portfolio that includes a mix of equities, bonds, and other asset classes. This diversification strategy aims to spread risk and potentially achieve more stable returns over time. He recommended distributing one's portfolio evenly between equities and bonds as a way to preserve capital during market downturns while still achieving growth.

Secondly, Graham suggested a flexible approach to asset allocation. This adaptive strategy allows investors to respond to changing market dynamics while maintaining a long-term perspective. One point that UK investors need to remember here is that your home should be included in this mix, not just your investments.

Graham's philosophy prioritised capital preservation first, followed by growth. This approach has influenced modern risk management practices, encouraging investors to consider downside protection alongside potential returns. At Tacit, our focus on the risk of permanent impairment of capital—the risk of total loss—is our secondary line of defence when constructing portfolios across the two asset classes of Growth and Stabilisers. What this means in practice is that, within either high-level asset class, there will be investments that have a greater propensity for impairment than others—a company with a fragile balance sheet or a bond with weak covenants being practical examples.

Although the next new investment idea is very exciting and captures people's attention, numerous studies show that asset allocation is a primary driver of investment returns, often outweighing the impact of individual stock picks. A well-diversified asset allocation strategy can provide more consistent and predictable returns over the long term, while one successful individual idea can lull investors into a false sense of competence. A body of academic studies shows that it is very difficult to consistently beat the broader investment markets through narrow selection.

Asset allocation ensures that the investment portfolio is aligned with the investor's financial goals and time horizon. For instance, an investor saving for retirement many years away should allocate a larger portion of their portfolio to Growth assets (primarily equities), while someone saving for a short-term goal should consider more conservative investments.

During periods of volatile news flow and polarised political views, we feel it is important to remind investors of the importance of balanced portfolio construction, as your investment objective should remain the primary driver of any decisions you take—not the latest social media post or news story. This is becoming more difficult in the modern world, but not impossible with a structured investment approach grounded in historic empirical evidence.