Insights, Tacit Thought | Weekly Investment Insights

Stay focused on your goals

Published on: 19 May, 2017 | Author: Investment Team

With the UK equity market hitting new all time highs this week, we believe it is important that investors remember their personal objective and time horizon. Rising markets are a good thing, however, chasing markets and not remembering your longer term objective will ultimately lead to disappointment.

It is vital to understand behaviour and not let emotions drive decision making.

To illustrate this point, consider this factual scenario which was published in the Financial Times this week. In 1972, the UK stock market had a total return of 17.9%, so £100,000 invested at the beginning of that year would have grown to £117,900 before costs. In 1973 the market fell 27%, meaning that the same portfolio would have fallen to £86,000. The following year saw the market fall by 50%, reducing the portfolio value to £42,700. Many (irrational) investors, driven by the pain of seeing their portfolio lose so much money, would encash their holdings and put them in a savings account. As a result, you would then miss the market rise of 145% that happened in 1975, the 2.6% rise in 1976 and the 48.7% in 1977. By the end of 1977 your cash deposit would be worth about £54,000 with compound interest, compared to the portfolio which would be worth nearly £160,000. The £104,000 differential would ultimately be the difference between achieving your objective and not.

This example is extreme but it does remind us all that equity investment comes with risks. At Tacit, our focus is on managing these risks within each of our four strategies whilst meeting their stated objective. For the first time in many years, the returns achieved by our four strategies have diverged as positioning of a lower risk strategy needs to be ***materially*** different to a higher risk strategy invested predominantly in equities.

Our high risk Total Return strategy, which can be invested wholly in equities, is designed for investors that have a long time horizon, are in the accumulation phase of their investment planning and have a high capacity for loss due to either their earnings power or other assets they own. In the longer term, this strategy is rewarded for embracing risk through potentially higher returns.

Our more cautious Real Return strategy on the other hand, aims to preserve and grow the ‘real’ value of client investments which means that we are as worried about large, short term market falls as we are about growing the value during periods such as 2017 when equity valuations are generally high. We do not know when a market downturn will come, but historic analysis illustrates clearly that when this downturn does come, high equity valuations can make it more severe than if valuations were cheap. Hence the more cautious positioning of this strategy since late in 2016.

We remind our readers that returns are only one side of the investment coin, your ultimate objective and appetite for risk are just as important.

Download Tacit Thought here

Opinions constitute our judgment as of this date and are subject to change without warning. Past performance is not a reliable indicator of future results.

sourced from information we believe to be reliable, we make no guarantee as to accuracy or completeness. Past performance is not a guide to future results, and the value of investments can go down as well as up.