

The Investment Dilemma... What to do next?



By Mark Penston



With continuing uncertainty in world stock markets, many of our clients are asking for investment guidance in terms of should they sell, buy, hold or switch funds. It is a fair question, but one that is difficult to answer. As ever, economists, politicians and fund managers don't agree and it would seem reasonable to say that the media don't help portray a balanced view either. Bad news gets heard over good news.

The answer to our clients' question is not easy, and as ever starts with a discussion about investment objectives, and appetite for risk.

History has shown that staying 'in the market' has invariably been the right course of action for the investor who has no foreseeable need for the money.

The following table illustrates the effect of coming out of the market at the wrong time (based on the FTSE 100 Index) over a 20 year period from 31st March 1987 to 31st March 2007:

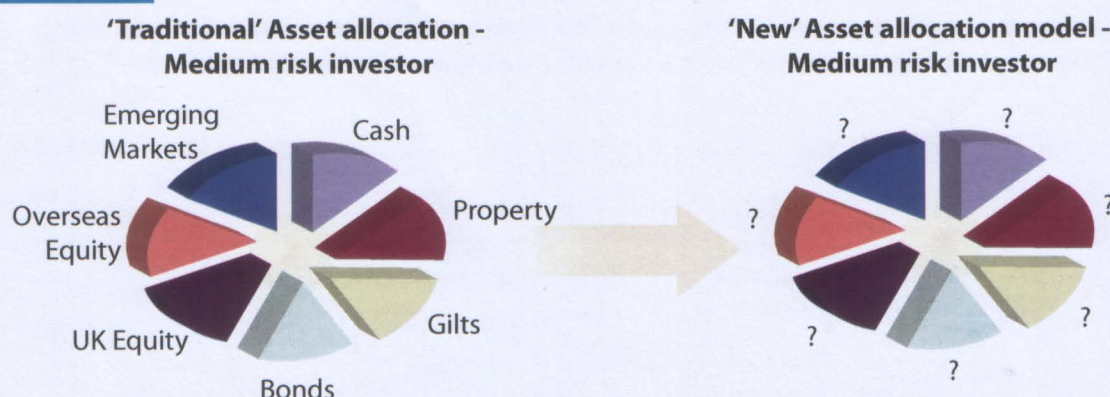
| Period of investment | Average annual total return (%) | Final value of initial £10,000 invested |
|-----------------------|---------------------------------|-----------------------------------------|
| Fully invested | 10.1 | £68,971 |
| Miss the 10 best days | 7.6 | £43,585 |
| Miss the 20 best days | 5.8 | £30,599 |
| Miss the 30 best days | 4.2 | £22,712 |
| Miss the 40 best days | 2.8 | £17,347 |
| Miss the 60 best days | 0.4 | £10,732 |

The table shows that trying to guess when to get in or out of the market is difficult and getting it right, unlikely.

It is however important to analyse what market to be in, and it is here that perhaps many investment advisers are rethinking strategies.

Traditional asset allocation models

In general most investors realise that investment diversification is important in order to add stability and reduce volatility. Full diversification will not just diversify within one market, but will diversify across global markets and other asset classes, such as bonds, gilts and property. A typical asset allocation model for a medium risk investor is shown below.



Historically, it has been the norm to see high elements of UK equity funds as the UK was felt to be a low risk, cost effective market to invest in and bonds and gilts would be present to add further stability through their 'guaranteed'

nature. Far East and emerging markets were generally held in lower proportions due to the economic, political and currency uncertainties that existed.

Without trying to be too dramatic, however, some of

the very fundamentals that have created traditional asset allocation models are perhaps in question and the answer to our clients questions about 'what to do next' is more to do with revisiting the asset allocation in their portfolio.

UK

UK and Eurozone debt levels continue to be a concern and evidence so far indicates that consumers are focused on debt repayment (deleveraging) and saving rather than spending. By the very nature of the level of debt, repayment will take many years and governments will also have to cut costs and increase tax revenues. Typically, many UK equity funds (which by definition have to stay invested largely in UK equities) are turning their attention to UK firms who derive a significant part of their revenue from other global markets in search of growth. Asset allocation models with high proportions of UK Equity should perhaps be viewed with caution.

Europe

It is easy to tar the whole of Europe with the debt brush, however Europe is a large area of many diverse economies, some of which have performed well. According to *Financial Express* the FTSE Emerging Europe index has outperformed the FTSE All-Share over a six month, one year and three year period. Focused funds may offer good growth potential.

Summary

The current global economic situation may be the start of significant changes to the relative strengths of world stock markets. It seems clear that even as matters stand now, traditional asset allocation models need to be reviewed and monitored in order to ensure that investments are diversified in correctly risk assessed funds and categories.

International/ Global markets

It is clear that not all economies have been as badly affected by the current debt crisis and fund managers of global equity funds have a good choice of markets in which to invest, particularly favouring those that also show good dividend yields. In fact the majority of companies with the longest track record of consistently increasing dividend yields are non-UK companies such as Nestlé and Procter & Gamble.

Property

The property market (commercial) was viewed as a safe environment, with upward only rent reviews and long tenancies. Coupled with the 'bricks and mortar' aspect to which so many investors were attracted, few foresaw the downturn due to economic pressures and oversupply. Prospects remain uncertain where the commercial property market is largely reliant on economic growth and latterly, Civil Service occupancy.

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