SurreyLawyer

THE OFFICIAL JOURNAL OF THE SURREY LAW SOCIETY | **SUMMER 2020**

Why put all your eggs in one basket?

The benefits of a diversified approach to investment

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Why put all your eggs in one basket?

The benefits of a diversified approach to investment

"Whilst the risks associated with investing funds cannot be avoided, when managed collectively as part of a diversified portfolio, they can certainly be diluted," says Iain Halket, Chair of the HFS Milbourne Investment Committee.

By investing in a wide range of funds across different asset classes and industry sectors, we can reduce the impact of market volatility and thereby limit the risk of capital loss, whilst generating more consistent returns over the medium to long term.

In addition to spreading and minimising risk, global diversification has other benefits such as offering a way to preserve capital in order to protect savings, which could be a priority for clients approaching retirement. Plus, not 'putting all your eggs in one basket,' means that there is scope to generate income from several sources.

Diversification works because assets, which may be any mix of shares, cash, property, commodities, bonds etc, can react differently to the same economic event.

Take for example, the current COVID crisis which has seen the UK market perform poorly versus other global markets.

Investors often prefer their 'local' market and therefore many UK managed funds tend to be overweight UK equities. But our view is that if better returns can be had by investing in the US or Asian markets why settle for overweight UK? A wider global diversification is key in our opinion.

If we look at the US Nasdaq, we can see that it is currently at an all-time high. However, during the severe market falls which took place between 19 Feb and 23 March 2020 the Nasdaq dropped by -18.66%; but since 23 March this market is currently +26.99% and +17.76%. on a year to date basis.

There is a logical explanation for this fluctuation in values. After an initial period of panic came the realisation that tech stocks such as Amazon, Netflix, Alphabet (Google) Microsoft etc were in even higher demand than usual.

HFS Milbourne Strategic Portfolio Service 5 year performance.

Our recommended approach is certainly borne out by the results: HFS Milbourne's managed Strategic Portfolio Service (SPS) 10, which consists primarily of global equities has given a return of +50.54% over the last 5 years whilst the FTSE100 is showing +15.86% as at 10 July 2020

Hold your nerve

The basic rule of investing will always hold true. Keep your nerve and do not panic when markets fall as they will bounce back at some point.

We have seen this time and again following periods of severe volatility including the two Gulf Wars, the Credit Crunch and the Euro Crisis. And the data suggests that the same pattern is emerging with the COVID-19 pandemic: between 13 Feb – 23 March 2020 the FTSE100 fell by -32.41%; from 23 March to 1st June 2020 this market is up +22.09%.

Of course, we can expect to see continued market volatility before we return to the 'new normal', whatever shape that ends up taking. But you must be in the market to benefit from the likely spoils of the recovery.

It is encouraging to see the level of volatility in markets has come back down to more normal levels since the panic sell off in March. The VIX index is often described as the 'fear' index with elevated levels indicating excessive trading as investors escape markets and dash to cash.

The Vix index measures the expectation of stock market volatility over the next 30 days implied by the S&P 500 index options.

There was a disheartening article recently in the Wall Street Journal reporting on data from Fidelity which showed that nearly a third of investors aged 65+ sold ALL of their equity holdings between February and May, implying those that did have missed out on the equally sharp recovery as market strength continued in to June.

As it stands right now, global markets are recovering well on the back of sustained government fiscal stimulus; death rates from COVID 19 are falling and businesses are starting to reopen which will kickstart economic activity.

Looking ahead
A burning question as the economy starts to recover relates to the government coffers and how the unprecedented level of spending will be paid for.

Although we are seeing record government borrowing in the UK (currently standing at £190bn and projected to rise to £350bn by the end of the year), the Chancellor will take some solace from the fact that the cost of that debt to the government is at an all-time low with, for example a 10 year Gilt now paying 0.2% (as opposed to 4% prior to 2008).

It will be interesting to see how the Chancellor tackles this thorny area, given the election promise of no tax rises. But then these are exceptional times which require exceptional solutions.

There is talk of a predicted V shaped recovery, with some commentators suggesting the economy will bounce back once lockdown measures start to ease, although we believe this will give way to a shallower rise in economic output as structural impairments from COVID-19 will weigh on potential growth.

The Government support will undoubtedly help ease the burden, but with the possibility of a second wave of COVID, combined with the end to the furlough scheme in October, there are some uncertain times ahead. And, of course, we can expect to see Brexit rear its head again before the end of the year, to add further to the unrest.

A priority will be to revive the COVID stricken economy, to encourage people to spend more and to support the high street, with the resulting demand for goods and services encouraging a lift in employment levels. To that end, the Chancellor continued the theme of 'splashing the cash' in the summer statement, with additional measures including VAT cuts, stamp duty holidays, green investment and job creation schemes, aimed at stimulating the economy and protecting jobs and this has been widely applauded within the business community. Mr Sunak will surely be remembered as the most popular Chancellor in history!

Interest rates are the lowest they have been for three centuries and although there has also been speculation about the use of negative interest rates as a further stimulus, in my view this is highly unlikely to materialise. Such an approach, which would see customers charged for banking services, is unprofitable for banks and unpopular with clients. And what is more, as we have seen in parts of Europe and Japan, it is not an effective way to solve the problem.

It is worth mentioning commercial property here as this sector will be under pressure for some time to come as the effects of COVID related home working and social distancing take effect. We picked up on a slowing of some areas of the commercial property sector in 2019 and very prudently, sold out of related funds mid-way through last year. This decision has had an incredibly positive impact on our overall performance which I am delighted to report.

Ethical investment
Socially responsible or ethical investing has gained remarkable traction over recent years and in the post COVID era it is set to become even more popular.

As global governments and the public increase their focus on the need to protect the environment, accountability, corporate governance and socially responsible business activities, we are pleased to report that we are in the final stages of developing a new Socially Responsible Strategic Portfolio Service.

As the name suggests, this service will allow us to hand pick appropriate investment opportunities, in line with a client's principles, be they ethical, moral, social or environmental and very much reflects a more socially aware mindset amongst our customers which we are very keen to support. Further details will follow in due course.

HFS Milbourne Financial Services is authorised and regulated by the Financial Conduct Authority (FCA) and specialises in wealth management, pensions, finance on divorce, mortgages, employee benefits and corporate financial planning.

For further information visit **www.hfsmilbourne.co.uk** or telephone 01483 468888. ■

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