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A Risk-Focused Approach to Investing

Our Investment Approach - In Summary - In Quotes

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Our Investment Philosophy – In Quotes

Our investment philosophy is simple and different. We believe that investment decisions should be guided by the wealth of academic and empirical evidence available to us. On review, it provides a number of clear pointers to where we should focus our energies to deliver our clients with a successful investment experience. We define a successful experience as one where our clients can sleep soundly at night, have a strong chance of achieving their future lifestyle goals, and both understand and believe in the investment journey they are taking. It is probably quite different to investment approaches that many clients have experienced in the past. In essence, our philosophy comprises three core beliefs and three important practical principles.

Our approach can be summarised by the quotes taken from leading academics and investment practitioners, who inform and share our thinking.

"Successful investors operate with a coherent investment philosophy that they apply consistently to all aspects of the portfolio management process. Philosophical principles represent time-tested insights into investment matters that rise to a level of enduring professional convictions."

David Swenson, CIO, Yale University Endowment – a highly respected investment practitioner

Belief 1: Capitalism and markets work effectively

We believe that capitalism works.

"It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest."

Adam Smith, The Wealth of Nations (1776).

We believe that markets work well.

"I remain sceptical that markets are systematically irrational and that knowledge of such irrationalities can lead to profitable trading strategies. Indeed, the more potentially profitable a discoverable pattern is, the less likely it is to survive. This is the logical reason one should be cautious not to overemphasize the apparent departures from efficiency"

Professor Burton Malkiel, author of 'A Random Walk Down Wall Street'

"Every market determined price is an equilibrium price that should take account of all information available at the time the price is set. (This is the definition of market efficiency.) But things inevitably change, and equilibrium prices change along with them. All we can say about the recent market turmoil is that the volatility of information and its implications for forecasts of profitability must be quite high."

Eugene Fama – a leading academic who established the Efficient Markets Hypothesis.

"The idea that a bell rings to signal when investors should get into or out of the stock market is simply not credible. After nearly fifty years in this business, I do not know of anybody who has done it successfully and consistently. I don't even know anybody who knows anybody who has done it successfully and consistently. Yet market timing appears to be increasingly embraced by mutual fund investors and the professional managers of fund portfolios alike."

John Bogle, Founder, Vanguard Group and author of several important investment books

"The lack of risk-adjusted excess returns and the absence of persistence support the efficient market hypothesis. Therefore one policy prescription might be that plan sponsors should engage entirely in passive asset management".

Busse et al. Academics who conducted research into the performance record of institutional investors.

Belief 2: Risk and reward go hand in hand

There are few free lunches in investing.

"If you want to earn high returns, be prepared to suffer grievous losses from time to time. And if you want perfect safety, resign yourself to low returns."

William Bernstein, author of 'The Intelligent Asset Allocator" and other investment books

Belief 3: Diversification is a useful tool

Not putting all of your eggs in one basket is an intuitive and valuable concept.

"Sensible investors prepare for a future that differs from the past, with diversification representing the most powerful protection against errors in forecasts of expected asset class attributes."

David Swenson, CIO, Yale University Endowment – a highly respected investment practitioner

"Asset allocation [the mix of your investments] is not a panacea. It is a reasoned – if imperfect – approach to the inevitable uncertainty of the financial markets."

John Bogle

"You can eliminate non-systematic portfolio risk, as defined by Modern Portfolio Theory, with a relatively few stocks. It's just that non-systematic risk is only a small part of the puzzle. Fifteen stocks is not enough. Thirty is not enough. Even 200 is not enough. The only way to truly minimize the risks of stock ownership is by owning the whole market."

William Bernstein

Principle 1: Focus on the structuring of a client's portfolio

A client's long-term portfolio structure will dominate their investment journey.

"For the individual investor, the asset allocation decision is by far the most important factor in determining returns."

Sandler Review: Medium and Long-Term Retail Savings in the UK (2002) – commissioned by the UK govt.

"By understanding and articulating the role played by each asset class, investors avoid making allocations based on the fashion of the day."

David Swenson, CIO, Yale University Endowment

"Since the future cannot be predicted, it is impossible to specify in advance what the best asset allocation will be. Rather, our job is to find an allocation that will do reasonably well over a wide range of circumstances."

William Bernstein, author of 'The Intelligent Asset Allocator"

A portfolio must be suitable for the client and their circumstances.

"A firm [must] take reasonable steps to ensure that a personal recommendation, or decision to trade, is suitable for its customer...[and] to take account of a customer's preferences regarding risk taking, their risk profile and ensure they are able financially to bear any related investment risks consistent with their investment objectives. We use the expression 'the risk a customer is willing and able to take' in this report as a shorthand description of these elements."

The Financial Services Authority

Principle 2: Manage costs effectively

Costs are insidious.

"In investing, you get what you don't pay for"

John Bogle

From a financial perspective:

"By a continuing process of inflation, government can confiscate, secretly and unobserved, an important part of the wealth of their citizens."

John Maynard Keynes, economist.

"When the dumb investor realises how dumb he is and invests in an index fund, he becomes smarter than the smartest investor…most investors, both institutional and individual, will find the best way to own common stocks is through an index fund that charges minimal fees."

Warren Buffett, Chairman, Berkshire Hathaway and legendary investor.

"The significance of the evidence is not that passive investing will always outperform active investing, but that when an investor has to make a decision about which way to invest, the probability of success always lies in favour of passive investment."

Professor Simon Keane, Glasgow University

From an emotional perspective:

"The investor's chief problem – even his worst enemy – is likely to be himself"

Benjamin Graham, author of 'The Intelligent Investor' and the grandfather of modern investing.

"If I have learned anything from my 52 years in this marvellous field, it is that, for a given individual or institution, the emotions of investing have destroyed far more potential investment returns than the economics of investing have ever dreamed of destroying."

John Bogle

"Success in investing doesn't correlate with IQ once you're above the level of 100. Once you have ordinary intelligence, what you need is the temperament to control the urges that get other people into trouble in investing."

Warren Buffett

Principal 3: Manage risk tightly

"Risk surrounds us and envelops us. Without understanding it, we risk everything and without capitalising on it, we gain nothing."

Glynis Breakwell, author of 'The psychology or risk'

Rebalancing:

"The fundamental purpose of rebalancing lies in controlling risk, not enhancing return. Rebalancing trades keep portfolios at long-term policy targets by reversing deviations resulting from asset class performance differentials. Disciplined rebalancing activity requires a strong stomach and serious staying power."

David Swenson, CIO, Yale University Endowment

Product due diligence:

"In evaluating people, you look for three qualities: integrity, intelligence and energy. And if you don't have the first, the other two will kill you"

'Risk comes from not knowing what you`re doing.'

Warren Buffett, Chairman, Berkshire Hathaway and legendary investor.

'Sometimes your best investments are the ones you don't make.'

Donald Trump, real estate entrepreneur.

Ongoing governance:

"It is not the responsibility of the fiduciary to follow every tic in the stock market, but it is his or her duty to understand everything in the Investment Policy Statement; if one doesn't understand it, it shouldn't be there."

Trone, Allbright, and Taylor (1996)

In conclusion

Our approach to investing is elegantly simple, yet highly effective. We cannot control the returns that the markets deliver, but we can select and manage closely the risks that our clients take in their portfolios. We can help them to obtain the bulk of the returns delivered by the markets, by minimising both financial and emotional costs, and helping them to stay the course. Belief, patience and discipline are the key to a successful investment experience.

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