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Our Investment Philosophy

Our Approach: Our aim is to help you achieve good long-term results from your investment by establishing and adhering to an appropriate investment strategy. Our philosophy is based upon several key beliefs about financial markets. These beliefs lead us to construct carefully structured investment portfolios that are designed to meet the investment needs of our clients.

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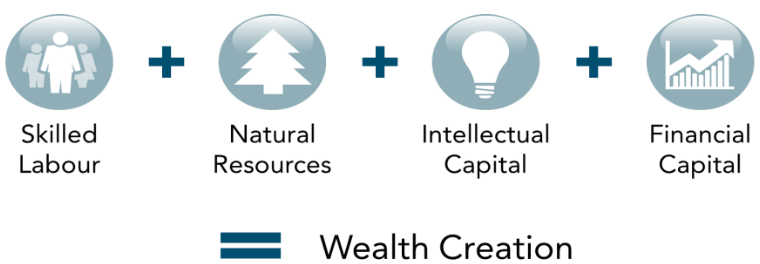
Capitalism works: Capitalism is what underpins the world's economy and is overwhelmingly the most successful economic model that mankind has devised. The free market is a simple mechanism that brings together ideas for products and services, and the finance required to produce them. People who invest in an enterprise are taking a risk with their capital and are therefore entitled to share any financial rewards - just as they would have to accept any losses.



Markets work: Capital markets are the best mechanism there is to calculate the value of an asset. Some investors believe they can price assets more accurately than the market. They perform research and analysis to arrive at a price for an asset. If the market price is below their calculated price, they might buy that asset to make a profit when it rises.

But however carefully they make their calculation; it is never more than an estimate upon which they base a prediction. Some estimates will be right, but many will be wrong. Very few people can make consistently accurate estimates over a reasonable period, so we do not use predictions about markets or prices in our portfolios. This principle applies across our investment philosophy which means we do not buy funds we think will outperform the market; or weight investments towards countries or regions we expect to do well in the short term. Instead we use investment funds with broad exposure to the whole market.

We therefore accept that the market, powered by the wealth-generating capability of capitalism, provides an adequate rate of return. We do not try to beat the market with predictions; instead we harness the returns of the market through discipline and structure.

Risk and Return are related: We believe it is impossible to improve your investment return without taking more risk. In other words, the potential for financial loss you expose yourself to in taking a risk is also the reason you earn a return. Risk is the premium investors pay for the expectation of a greater return. Our role as an adviser is first to identify which risks offer consistently higher expected returns and which do not, and then to provide you with exposure to those risks in a structured, disciplined and cost-effective way.

Diversification is essential: Diversification is the principle of spreading your investment risk around. Our investment portfolios therefore hold the shares and bonds of many companies and governments in many countries around the world. This means the negative and positive influence of each individual investment is reduced, producing, on aggregate, less risk in our portfolios.

Table: Key bond and equity index returns (%), ranked by performance

2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
23.58	20.31	17.43	28.30	19.59	8.78	35.43	21.06	0.78	25.70
21.26	16.68	15.54	23.97	18.77	5.48	34.11	17.18	0.50	21.64
19.07	6.52	12.76	21.03	14.64	5.35	29.56	16.86	0.10	20.18
16.74	5.80	12.30	20.81	12.51	4.04	25.48	13.84	-0.39	19.17
14.51	2.14	11.99	13.59	11.30	2.53	25.41	13.10	-2.24	15.48
12.73	1.21	11.18	11.13	9.36	1.39	21.17	11.27	-3.10	15.24
8.85	-3.46	10.72	1.64	7.92	0.98	18.27	8.59	-3.44	13.68
8.75	-6.57	9.29	0.56	7.87	0.70	16.75	4.86	-7.64	9.34
7.54	-12.58	5.93	0.04	2.81	0.49	12.27	2.45	-8.03	7.62
6.57	-15.01	2.91	-4.22	1.18	-1.08	10.73	1.95	-9.08	6.85
4.82	-18.36	0.56	-5.29	-1.35	-10.31	3.66	1.93	-9.47	6.33

Top-performing asset class
Bottom-performing asset class

Global equities	UK government bonds
North American equities	UK index-linked gilts
Emerging market equities	UK investment grade corporate bonds
Developed Asia equities	Hedged global bonds
European equities	LifeStrategy 60% Equity Fund
UK equities	

Investment Styles: Active vs. Passive: Investment styles are often categorised as active or passive. An active investor is one who makes decisions about holding one investment over another. Passive investors are willing to accept the market rate of return and enjoy paying smaller fees than active investors.

Our investment process targets market-beating performance through structured exposure to dimensions of higher expected return and uses methods of portfolio construction and implementation that enhance performance relative to the average investor. We believe that the average active investor will do worse than the market because they are paying the highest fees; whereas the average index investor will perform better than that because their fees are lower than the active investor.

We make extensive use of index-based investments to implement exposures in different classes and regions. We only use the more 'actively managed' funds and investment trust when looking to specific asset classes such as smaller companies and geographical areas where a suitable index-tracker type fund may not currently be available.

Sources of Investment Return: In this section, we will identify the broad asset classes which we believe provide positive returns for investment over long periods of time. We will look at the risk characteristics of these asset classes, as well as their expected return characteristics. We believe that an investor should only take risks that will produce a positive expected return on their investment.

Asset Classes: the variety of instruments an investor can use is vast. The most conventional are shares, bonds and cash. These are the most liquid and transparent asset classes which, in many cases, offer investors a real stream of income now or in the future. This quality gives them a tangible and genuine value.

Portfolios should be built around Structure, Discipline and Diversification: we do not use predictions, estimates or judgements to construct investment portfolios; instead, we look to world-renowned academic financial theory as a basis for our portfolio construction. We believe markets works and we are prepared to accept the average rate of return from the market for our core holdings.

Following the whole market or sections of it through index-tracking funds is a low-cost way to gain exposure to markets for the core aspects of the portfolio. In addition, we help our clients remain disciplined. Staying invested through thick and thin is usually the best strategy for investors as timing exit and entry points is as unreliable as any other prediction of market movement. We help investors remain in the market all the time it remains appropriate to do so.

Equities: both in the UK and across the world tend to be volatile, with rises and falls and may lose value over any given period rather than provide a smooth upward progression. In general, the more equity a portfolio contains the higher the returns albeit with higher risk. In order to get the best possible equity market return, we focus clients' exposure where possible on dimensions of higher expected return that various academics have identified. Their research suggests that smaller companies and low-priced companies (that is companies whose book value of assets is high relative to their market price) perform better than the market average over time.

Because risk and return are related, the higher expected return comes at a price and, therefore, investing in these companies is riskier than investing in the whole market. There are periods when these groups of shares underperform the market, but over time, the academic research indicates that these risk premiums have been worth paying.

We therefore tilt our clients' portfolios towards small and where possible to value companies to an extent that is appropriate to the investor and their long-term goals. Small cap stocks are considered riskier than large cap stocks, and low relative price stocks are deemed riskier than high relative price stocks. These higher returns reflect compensation for bearing higher risk.

Fixed Income: e.g. gilts, corporate bonds and index-linked gilts, are less prone to extremes on both the upside and the downside. The closer you are to needing access to the capital, the more bonds and cash you should hold. Short duration bonds are bonds with a short time to maturity, typically less than five years. They can be a useful tool in mitigating the risks of both rising yields and market volatility.

As a result of short duration bonds having less time to maturity, they are less sensitive to rising yields. For a similar reason, Short Duration bonds are also less affected by changes in interest rates, making them less volatile in general than longer duration instruments.

Other Asset Classes: We have also identified two other sources of investment return which we believe should be considered in an overall portfolio.

- **Commercial Property:** is uncorrelated to either equities or bonds. It provides investors with a stable, diversified total return comprising elements of both capital and income growth and has performed very well when compared to equities or bonds. In addition, the returns from commercial property tend to be delivered with much lower volatility than equities or bonds.

  Including UK commercial property within a multi-asset portfolio can help to reduce overall risk as the sector has a low or even negative correlation to other asset classes.

- **Global Listed Infrastructure:** are funds that invest global infrastructure such as toll roads, hospitals, prisons, schools etc. It has market risk but offers liquidity, diversification and healthy rising income flows.

Correlation and Diversification: Understanding the correlation between returns from different assets helps us to diversify risk in a portfolio efficiently and effectively. There is very little diversification achieved if we combine two assets whose expected returns have a high degree of correlation to one another. It is far better to combine assets which have attractive long-term risk and return characteristics as well as relatively low correlation to each other i.e. assets that behave differently at any point in the economic cycle. That way if one asset falls in value there is a reasonable chance that the other may not and thereby provide some protection and lower volatility for the whole portfolio.

Adding a risky or even a low-return investment to a portfolio can make the portfolio more efficient if the new investment has a very low or negative correlation with the rest of the portfolio. For example, assets like 'index-linked gilts' which can appear relatively unattractive when compared based on risk versus reward may justify a place in most portfolios due to their low correlations with equities and conventional bonds.

The positive result of combining assets with relatively low correlations into an efficient portfolio should be that, for any level of risk, a well-diversified portfolio should have the potential for a higher rate of return. Equally, for any desired level of return, a well-diversified portfolio should be able to achieve it with lower risk and less volatility.

The benefit of diversification in your portfolio should be clear and significant over the longer term. Sometimes it is not so apparent over shorter periods of time as in any given year, narrowly based portfolios may produce dramatically better or worse returns than more diverse and therefore theoretically less volatile portfolios. Investors need to weigh the expectations of higher long-term risk adjusted return against the potential regret of underperforming certain benchmarks over shorter time periods.

Geographical and Sector Diversification: The principle of diversification also applies across different countries and markets. This underpins our belief that portfolios should have a significant allocation to overseas opportunities in the global marketplace. There are risks to investing in overseas markets as currency fluctuations can have an impact in both positive and negative ways. Experience shows that allocation to international markets can be beneficial in the long run providing scope for more efficient portfolio construction due to wider diversification.

Risk Tolerance: Our aim is to help you achieve good long-term results from your investment by establishing and then adhering to an appropriate investment strategy. We need to agree what sort of risk you are willing and able to take. The process of risk profiling is invaluable in deciding which portfolio is most appropriate for your specific needs and goals.

We use the FinaMetrica Risk Questionnaire to help us build a suitable portfolio where your investment is allocated across the different asset classes with the objective of obtaining the highest potential return in line with your risk profile. It also helps ensure you are not put into a portfolio that would expose you to unnecessary or unwanted levels of risk.

Risk and return are related to the extent that it is not possible to achieve a higher investment return without taking more investment risk. Many people invest with a level of risk that is guided by their "risk tolerance" – that is how much investment risk they are prepared to tolerate. But taking too little investment risk is risky in itself – the danger being that your assets will not grow enough to meet your investment goals. So, a trade-off is necessary to achieve a balance between taking enough risk to achieve your goals, while not being reckless. We build bespoke investment portfolios for our clients with various degrees of risk and expected returns and express these variables in simple terms that we hope you understand.

Here are some of the other things you might consider when deciding upon your risk tolerance:

- **Time Horizon and Liquidity Needs:** How soon might you need to withdraw money from your investments? The longer an investor holds onto a risky asset the lower the chance there is of obtaining poor cumulative returns. It is important to note the importance of time in the investment process. Our view is to evolve change in the asset allocation over time wherever possible rather than make any immediate change to reduce the possibility of adverse timing implications.

- **Attitude to Risk:** What is your aversion or attraction to risk when risk is defined as "the possibility of loss"?

- **Net Worth:** Generally speaking, the more assets an investor has in reserve, the higher their capacity for risk.

- **Investment Knowledge:** How good is your understanding of the investment you are making and how it behaves over time.

Monitoring Fund Performance vs. Benchmark Performance: We believe it is important for us to keep a close eye on the funds within our clients' portfolios to make sure that they are capturing the risk and return characteristics of the asset class(es) that they are targeting. Part of this process involves us reviewing the funds on a regular basis.

The different asset classes in your portfolio are unlikely to perform well or badly at the same time. The different timings of their types of performance is useful to the portfolio because it means that you are diversified. Equities, for example, might perform better over a given time period than bonds. This would mean that the proportion of the total portfolio that is made up of equities increases from the initial proportion. At the same time, the proportion of bonds in the portfolio would, in this example, have reduced.

This is perfectly natural as the capital markets move up and down in relation to each other. However, the danger is that the portfolio may 'drift' so far away from the initial proportions of asset classes that the portfolio is exposed to more risk than we initially designated it to. However, if new money is being invested into the portfolio, we will direct this towards the asset appropriate classes that will move the overall asset allocation closer to the proposed target.