

## INTRODUCTION

I have recently returned from a two week Easter break and whilst I was away the worldwide markets were going through a fresh period of turmoil.

Over this period the UK market has fallen in one day by around 3.5%, risen on another day by 3.5% and we have seen a major investment bank collapse. Those of you who have had meetings with me over the last few months will be aware that my concerns were relating to further terrorist attacks or another banking crisis. We have now seen the demise of Bear Sterns with the share price falling by more than 90% from its 12 month high.

### Asset Allocation Strategy

On one occasion during the holiday I got chatting to someone who asked me what I did for a living. When I explained he instantly assumed that I would be on the phone to the office every hour.

I was able to explain that all of our clients had a strategy that was specifically designed to ensure that their **portfolios survived during times of turmoil** and, if anything, were positioned to be able to take advantage of it. I specifically explained that:

- Our most adventurous recommended portfolio only had 50% in equities and therefore even if markets were to fall by 25% this would be a 12½% drop of their total assets. We would then have the ability, and the funds, to *switch into markets at a low* and therefore take advantage of the fall rather than being a victim to it.
- The majority of clients were holding *unprecedented levels* of cash within their portfolios and that this could be used to buy into markets if necessary.
- We had recently been recommending that clients increase their fixed interest holdings within portfolios. The turmoil in equity markets is likely to lead to lower interest rates which should support fixed interest markets, and therefore to a large extent what is bad for equities is likely to be good for fixed interest creating balance within the portfolios.
- For many of my clients, my staff, in my absence would be following through with recommendations that had already been made should the markets hit certain levels. These would all be recommendations to increase holdings in the equity market.

### Market Levels

I have believed for some time that the market is trading between the 5500 and 6500 levels, and that 5500 is a strong buying opportunity and represents value for money and that 6500 may be an opportunity to reduce equities if a client is currently overweight.

I have therefore agreed trigger points with many clients so that, for example, if the market closed below 5600 for three consecutive days, then we would use this as an opportunity to buy in, and as we were holding pre signed switch forms on this basis, we were able to do so promptly. Therefore, I was comfortable that whilst I was away many of my clients would be taking advantage of the market volatility to increase their equity weightings.

### Emotion versus Logic

I appreciate that buying into markets during periods of volatility and underperformance is a brave thing to do, and I also appreciate that selling equities when the markets are riding high is equally difficult.

However, this is where the strategy should override our emotions. The strategy is designed to provide us with a track to run on and to keep us on the straight and narrow. When we know exactly where we are going we don't need a map to get us there, however when we start to feel slightly lost a map is essential.

I believe that the clients whose portfolios will come through this turmoil with the best results will be those that follow an agreed strategy.

### Not According to Plan

Having reviewed some notes of late that strategy isn't always followed. I had a number of clients where we agreed to reduce equities once the market got passed 6500. This it did for the first time in May 2007 and we therefore contacted these clients to see if they wanted to reduce their equities. Whilst a number of people did, there were others who felt that the market still had "*further to go*". This is similar to my briefing of May 2006 ("*Where are all the orders?*") when we had similar discussions with clients.

As I said earlier, I was pleased that we had buying instructions for a number of clients and when I returned it was great to see that a number of these had, indeed, taken place. However, we are not discretionary managers and these still had to be on the agreement of the clients and some declined. An interesting trait is that a couple of clients who I had recommended sell at 6500 but didn't, then recently contacted the office asking whether or not they should sell at 5500!

The level of the index itself **does not apply to everybody** as a buy or sell opportunity, it should be relative to the amount of equities the client has in their portfolio. If I have a client who has 60% in equities which is above our adventurous portfolio, then I would not be recommending they sell right now, but I would certainly be recommending that they reduce this down perhaps to our balanced level of 40% once the market hits 6500, for instance.

It follows that if I have client who has 40% in equities who is balanced I would not be recommending that they buy into the market at 5500, but if I have somebody who is balanced and only has 30% currently then I would definitely be recommending that they buy in.

### Market Summary

I am confident that if you are buying into equities when the index is at a level between 5500 to 5700, then in five years time this **should represent an excellent investment** relative to other asset classes. I am equally confident that the market will continue to be very volatile over the next six months and is **likely to test previous highs and lows**.

The market is moving very quickly in both directions which means that some quarterly reviews will show fantastic returns and others poor returns. It is important that we **do not get distracted** by these peaks and troughs.

As investment guru Warren Buffett says:

*"To invest successfully over a lifetime does not require a stratospheric IQ, unusual business insight, or inside information. What is needed is a **sound intellectual framework** for making decisions and the ability to keep **emotions** from corroding that framework"*

### CONCLUSION

**We can't predict what will happen in stockmarkets**, which is why having a plan is so important. The strategy has always remained the same. If we stick to the strategy, have confidence in the fact that we have a plan and that it does deliver consistent returns on a rolling five year basis then we need not fear short term volatility.

If you feel that your portfolio has either too much or too little in equities and you would like to set target index levels for either buying or selling, then please contact your usual adviser who would be delighted to discuss your strategy with you.