

## - TWP Core Investment Strategy -

### Overview:

TWP is passionate about investment and has a view that is primarily different from the majority of Financial Advisers. We have a perspective of what is going on in the economy and the markets. More importantly we actually invest our clients' money in accordance with that view. At the heart of our investment offering is wealth preservation. Both our chosen investment partners and we use diversified, low correlated, multi asset and absolute return investments to control risk.

In our view, strong returns can be achieved consistently over time by using a risk focused process. We believe that the vast majority of investors prefer a smoother journey where returns are steadily compounded over time by trying to avoid the major losses of market corrections and then participating in a good proportion of the market rises. This means we may go through extensive periods where we protect capital, rather than grow capital. We believe that this smooth and consistent investment approach where volatility is targeted and managed rather than ignored is the more effective way of protecting and increasing wealth over the longer term.

TWP's Investment Strategy centres on a using a series of Risk Related Managed Portfolios; each portfolio has a 'core holding' that looks to protect capital in challenging investment conditions, using a variety of alternative low volatile investment funds which have a low correlation to both Bonds and Equities. Portfolios are managed on a Strategic and Tactical level. A Strategic asset allocation is agreed, whilst the Tactical allocation enables the portfolios to be altered to reflect changing economic and investment conditions. The portfolios are mandated to hold 100% cash at times of great uncertainty. The higher risk portfolios will have an increasing exposure to volatility, aiming to deliver superior growth over the longer term.

For clients with smaller investments, or who have less investment experience, we have a set of lower cost and more simplistic managed portfolio solutions.

### Background & Economic Perspective:

Our strategy is based on our belief in two key respects:

- Ongoing poor economic conditions will lead to continuing volatility in the Stock Markets and a broadly sideways movement in stock prices over the next few years.
- The Investment industry is outdated in looking to persuade the investor that they have to hold shares in the long term.

### The History of the Stock Market in the 20<sup>th</sup> Century

The 20<sup>th</sup> Century and the first decade of this Century have been characterised by very long periods of either substantial growth ("Bull Markets") or market falls, with no growth:

<u>Years</u>	<u>Duration (Yrs)</u>	<u>Market Type</u>
1905 – 1919	14	Bear
1919 – 1929	10	Bull
1929 – 1948	19	Bear
1948 – 1965	17	Bull
1965 – 1982	17	Bear
1982 – 1999	17	Bull
1999 -	?	Bear

What is interesting is the length of these Bull & Bear phases. For example during Bull phases, the markets tend to make substantial gains, which is why the Investment Industry claim that in the longer term Equities out perform any other asset class. However, during Bear Markets, Equities make little or no long term growth: Following the Wall St Crash in 1929, it took 19 years for the Stock Market to recover. During these Bear market phases, there is great volatility characterised by significant market corrections. These can be seen by the graph on the following page showing the Stock Market from 1965- 81.



It is our belief that an investment strategy needs to be adapted to reflect the economic environment and whether the Equity Market is in a Long Term Secular Bull Market or a Long Term Secular Bear Market? It is our strong belief we are presently 12 years into a Bear market, which could last at least a further 4-5 years, maybe as many as 7-8. As highlighted above, a 15-20 year Bear market is not unusual.

Moreover in the last hundred years stock markets have seen major falls in 1929, 1972, 1990 and in 2008. Each occasion was preceded by huge levels of excessive leverage. In 1929 the US market fell 90%; in 1972 there was a fall of 75% in UK markets; in 1990 Japanese markets fell by 80% & they are still down 75%, some 20 years later. Finally by March 2009 global Western markets fell by 50% from their peak in late 2007. Although each occasion witnessed massive debt levels before the market falls, by far the most extreme levels of debt have been witnessed in the most recent crisis. And the market was 'only' down by 50%! We believe the markets will remain highly volatile & the market will fall further from these levels and we will see new lows being tested.

#### **Outdated Traditional Investment Methods:**

Any investment process, however well thought out, will ultimately fail unless the Management is prepared to change. The Financial Services industry is renowned for this inability to react to change. Why is this? Quite simply, it is our view that the vast majority of fund managers fear losing their jobs more than they fear losing investors' money. If they deviate from their benchmark and they lose money when all other fund managers make money, then they lose their jobs. If they do not deviate from the benchmark and they lose client money as do other fund managers, then they keep their jobs. Most investment managers are more concerned at preserving their employment rather than not losing client money.

It is for this reason the investment industry is outdated and they have a vested interest to persuade the investor they have to hold shares in the long term. Well educated professionals and investment management companies will be trying to persuade the Public the stock market has found a bottom. In our view the bottom of the market has not been reached and fundamental investment returns will not be delivered by long term investing in the stock market. In essence, we believe traditional investment strategies are not relevant for a long term Bear market. These traditional methods are:

- Based on a lack of diversification between different asset classes
- Hold mostly equity based investments with a smaller proportion of fixed interest investments, and perhaps a very small element of property.
- Based on "Long Only" investing, where assets are held for the long term and suffer volatility and capital losses when markets fall.
- This volatility has been huge in recent years; for example the market falling 31% in 2008 and rising by c50% from its low in March 2009 to the end of December 2009.
- The danger to the investor of this approach is much higher volatility and a strong probability that any short term gains will be reversed.
- After a 30 year 'Bull' market in Fixed Interest investments, there is a real danger of significant capital losses in the future.

## **TWP Economic Outlook:**

Global economies are precariously positioned: Whilst Emerging markets are facing rising inflation and higher interest rates, the Developed world is saddled with unprecedented levels of debt. The threat of a downgrade in the US AAA rating materialised in the summer of 2011. Also the continuing crisis in the eurozone economies is only now starting to be addressed. The authorities are finally accepting the enormity of the situation. If Italy needs bailing out, the European Financial Stability Facility will not be able to cope. Meanwhile market pressure continues to build on France with her bond yields rising to record spreads over Germany's. At best we face GDP growth making modest headway and at worst we face stagflation and further recession.

In 2010 we wrote of our concerns of an imminent Sovereign debt crisis- Dubai and Greece were merely a taste of what is to come. We said: "The euro 750 Billion 'rescue package' announced in May (2010) is no more than sticking plaster and delaying the inevitable." More than 12 months later, Greece was back asking for another bailout of similar proportions. We believe a Sovereign default will occur, European banks will face further crisis, but unlike 2008/9, no Government will be able to bail them out. This will impact severely on all global equity markets which are likely to face a major correction in the coming months, and therefore we are fearful that a traditional investment strategy will lead to a reversal of any gains achieved since March 2009.

What of Fixed Interest? We believe this has been over bought and if the values start to fall, there could be significant liquidity problems, with investors unable to get their money out of the funds. Fixed Interest investments do well when inflation and interest rates are low. However it is probable the next movement is up, which will lead to capital losses for Fixed Interest Bonds. Whilst inflation itself might not be a problem for some time, & rates are likely to remain low in historical terms, we believe it is important to invest with fund managers who are able to keep liquidity and the ability to actively manage the sector with the widest mandate allowing them to short the markets, thus benefitting from market falls. The other destabilising factor is if there is a Sovereign debt crisis it will severely impact on the fixed interest market, with yields rising and capital values falling.

UK commercial property had a strong 3-4 years to mid 2007, delivering annual returns in the region of 16%. However, the outlook is poor; many UK funds have fallen by up to 40%. Likewise the residential sector is unattractive as well. Over the last few months the market has made a small recovery, however we are very cautious of the sector as any "Double Dip" recession will have an adverse affect on property. The UK's biggest banks still have huge exposure to property where the covenant has been broken and the values are less than the outstanding loan. The Bank of England has recently announced its concern over the banks' practice of 'loan forbearance', whereby they waive breaches of loan terms and avoid foreclosure; this means there is a higher proportion of prospective bad loans on their books. Hence TWP will avoid main stream commercial property funds. The property funds we recommend tend to be either specialist niche funds, broadly uncorrelated to UK property or overseas investments, & are a mix of residential & commercial.

## **The Alternative: TWP's Investment Strategy**

As argued above, a wholly different strategy needs to be employed during the Long Term Secular Bear market we currently face. This involves using a much wider range of asset classes than traditional investment methods employ. This wider diversification allows for reduced volatility risk. The portfolios both our chosen investment partners and we use have a low correlation to equities and bonds; they also have lower volatility characteristics. Our objective for our more cautious clients is Wealth Preservation, delivering an absolute positive return whatever the economic & investment conditions. This means we should outperform traditional equity investment methods at times of uncertainty, but under perform in the event of strong stock market growth. However we believe that in the prevailing long term Bear market, our Clients would rather see steady capital preservation and appreciation year on year rather than large gains one year only to face significant losses the next.

Of course, when a long term Bull market is confirmed, TWP will adapt its strategy to accommodate the economic conditions.

For clients with larger sums for investment, or who may be experienced investors one of TWP's investment partners runs 10 risk-based portfolios each with a mandate for capital preservation by using multi asset investments and having the ability to invest 100% into cash.

For less experienced clients, or for those with smaller investments, we use five lower cost simplified portfolios managed by a different investment partner. These portfolios are mandated with the same investment philosophy as those used for more experienced investors.

We believe that blending different assets gives our clients three important benefits:

1. Access to a significantly diversified portfolio which reduces risk
2. Reduced volatility which means they can plan their financial future
3. The potential for higher returns than other funds with comparable risk

By investing in fewer asset classes, other funds can leave themselves more exposed to greater volatility and increased risk.

TWP Wealth Ltd November 2011

***Please Note: Past performance is only a guide and may not be replicated in future. Some of the Funds TWP use are for more experienced investors only.***