THAMESIDE FINANCIAL PLANNING

OUR INVESTMENT APPROACH

UNDERSTANDING INVESTMENT RISK

An overview

Thameside Financial Planning recognises the importance of working with you to understand, achieve and maintain your desired lifestyle. In order to do this it is important for us to understand your attitude towards investment risks and the potential variance on risk versus return.

Throughout our discussions with you we will recommend an investment solution based on the following:

• Your attitude to risk tolerance.

• Your investment objectives.

The portfolio that we recommend will consider these factors and will seek to achieve your objectives while controlling the investment risk within it. This will be reviewed with you on an agreed time-scale to ensure your financial objectives remain realistic based on your circumstances at that time.

We believe that diversification within a portfolio is one of the most effective ways of maximising opportunities while minimising risk. The main principle of diversification is to smooth out the fluctuations that can occur within a portfolio by broadening the exposure across a range of different asset classes. The balance of different asset classes can therefore reduce the overall volatility without significantly reducing the returns.

Following our beliefs, we use a volatility based approach to investing which ensures that you are never taking on more risk in your investment portfolio than you would be comfortable with.

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Getting to know you

The logical starting point of the investment process is for us to get to know you and determine what you are looking to achieve. A wide-ranging 'discovery' meeting will ensure our subsequent advice is soundly based. As well as taking account of your personal and financial circumstances, it will cover your broader attitude and the level of experience and knowledge you have about investing.

It is important for us to understand what your objectives are for investing. For example:

- Are you looking for capital appreciation or capital protection over the short/medium/long term?
- What are your current income requirements?
- What will be your income requirements in the future?
- How much money do you have to invest?

We must also consider the timescale for investment and we may recommend more than one solution based on different financial objectives for different events. For example, you may wish to invest in the short term for a specific requirement such as school fees, but want to ensure you have enough money to fund your lifestyle in retirement and leave a legacy for your chosen heirs.

We will ask you about your existing investments as it will be important that we analyse and evaluate their continued relevance and suitability in the light of your current circumstances and objectives

Understanding your tax position will help us ensure the investment recommendations we make are as tax-efficient as possible.

Selection of 'tax wrappers' – ways to hold your investments

A tax wrapper is a financial product, such as a pension, collective investment, ISA or bond, within which your investments can be held and which usually has certain tax benefits.

Once we have established your financial goals we can begin to determine the most appropriate tax wrapper(s) to meet your needs and instigate them when you are ready to invest.

Establishing your attitude to investment risk

The investment strategy we recommend for you needs to be in line with your attitude to investment risk, which means taking account of several factors such as:

- The anticipated length of time before you want to use the capital you accumulate – its ‘term’.
- Cash to meet unexpected circumstances.
- How you think your earnings might grow.
- Whether you have any debts.
- Your overall view on investing.
- The impact of short-term falls in the value of your investments.
- The importance of protecting your investment from the effects of inflation.
- The question of ‘liquidity’– how easy will it be to get your hands on your money?

Using a specially designed questionnaire, we will ask you a series of questions. Each answer produces a score and these are then aggregated to calculate your specific level of tolerance for risk, from 1 (low) to 10 (high). We call this your risk profile score.

The risk profiling questionnaire we use has been developed in conjunction with Oxford Risk Research and Analysis (ORRA). ORRA Ltd is an independent company, linked to the University of Oxford, who are acknowledged experts in risk profiling. Their risk analysis expertise and tools are used by a wide range of financial services companies. (From Standard Life – 2011)

Many of the terms commonly used to describe attitudes to investment, such as ‘cautious’, ‘balanced’ or ‘aggressive’ can mean different things to different people. We aim to make our assessment of your attitude to risk as objective as possible. That’s why the next stage of the process is a discussion about what your risk profile score means.

Discussing your risk profile score and understanding capacity and tolerance to loss

Your resulting risk profile score, or risk-rating, is an indication of the extent to which you are prepared to accept a short-term fall in the value of your investments as markets experience ups and downs. These fluctuations in the value of investments are also known as their volatility.

If your score is 1, then low volatility investments such as cash or bank deposits could be the resulting investment recommendation. If your score is 10, then we might recommend a portfolio which includes investments in asset classes such as emerging markets, whose higher expected volatility is matched by greater growth potential.

Before making recommendations we will discuss your ‘score’ with you. We want to be sure you understand what that score implies for the design of your investment strategy and whether this reflects your true attitude to risk.

Our recommendation will be based on the belief that clients should accept a level of risk no higher than that appropriate to the achievement of their objectives – in other words, take no more risk than is necessary and feels comfortable.

We offer ongoing service options which include reviews of your risk profile to ensure that your investment strategy remains aligned to your investment risk profile.

Risk category descriptions

Higher risk – Aggressive

People in this category are very comfortable with investment risk. They aim for high long-term investment returns and do not overly worry about periods of poorer performance in the short to medium term. Ordinarily these portfolios can be subject to the full extent and frequency of stock market fluctuations.

Medium to higher risk – Assertive

People in this category are relatively comfortable with investment risk. They aim for higher long-term returns and understand that this can also mean some sustained periods of poorer performance. They are prepared to accept significant fluctuation in value to try and achieve better long-term returns.

Medium risk – Balanced

People in this category are balanced in their attitude towards risk. They don’t seek risky investments but don’t avoid them either. They are prepared to accept fluctuations in the value of their investments to try and achieve better long-term returns. These portfolios will be subject to frequent and at times significant fluctuations in value.

Lower to medium risk – Cautious

People in this category are relatively cautious with their investments. They want to try to achieve a reasonable return, and are prepared to accept some risk in doing so. Typically these portfolios will exhibit relatively modest yet frequent fluctuations in value.

Lower risk – Conservative

People in this category are conservative with their investments. They prefer taking a small amount of risk to achieve modest or relatively stable returns. They accept that there may be some short term periods of fluctuation in value.

Creating an 'asset allocation blueprint' to match your risk profile

'Asset allocation' involves designing the right balance of assets in your portfolio. Investment funds are categorised under different asset classes depending on their particular focus. These asset classes include cash or money market investments, UK fixed interest, international fixed interest, property, UK equity and international equity. Each category can respond differently to the same circumstances – asset classes expected to respond very similarly to each other are said to be highly 'correlated'.

Diversification across assets that tend to behave in different ways can help protect a portfolio against market fluctuations, while providing the potential for rewarding returns. Little real diversification is achieved through the combination of asset classes whose expected performance shows high correlation to each other. It is far better to blend asset classes which have:

- Appealing long term risk/return characteristics.
- Relatively low correlation with each other.

That way, if one asset class falls at any point, there is a reasonable chance that the other may not, thus providing some protection and reducing volatility of returns for the portfolio.

Price volatility can be unsettling and reducing that volatility gives a greater likelihood that investors can stick to their long term strategy and realise their goals.

Asset allocation expertise

Instead of relying purely on historic investment returns, our forecasts are calculated using a stochastic investment model, developed by Barrie & Hibbert (a global leading provider of financial risk modelling solutions) and projection engine provided by eValueFE Ltd (an associated company of Financial Express). Stochastic models are generally considered more reliable than historic returns alone as they explicitly allow for:

- Economic drivers underlying investment returns, such as inflation or economic growth.
- Day to day variability inherent in investment returns and equity market shocks.

Stochastic models project hundreds of different possible future investment scenarios to give a better indication of the level and spread of future returns.

Nobody can guarantee that the volatility range of a particular asset allocation will not be breached occasionally. There is always the possibility of exceptional market conditions, due to unanticipated external events.

Investment strategy

Once the asset allocation stage is complete, we need to choose appropriate investments within the various asset classes specified in your 'blueprint'.

One of the decisions to make is whether to take an 'active', 'passive' or 'blended' approach to investment management.

An active approach is where the fund manager uses their skill to select stocks they think will perform better than average or better than the benchmark in a particular sector.

The passive approach is where fund managers don't try to beat the index; they aim to match it (sometimes called 'tracking') as closely as possible.

The strategy Thameside Financial Planning adopts

Our approach to working with clients is flexible when it comes to determining the strategy most appropriate to their needs and preferences. However, we also feel it is important that we state our starting position on this aspect.

Blend of Passive and Active

We recognise that a passive approach to fund management gives our clients access to the markets at a competitive price and that active management, while more expensive, can add value because of the opportunities it can seize. Adopting a blend of both strategies (passive and active) gives our clients the best of both worlds; exposure to market opportunities and at lower cost than with a completely active approach.

Selecting investments to match your asset allocation blueprint

Once the asset allocation stage is completed, we need to choose appropriate investments to reflect the various asset classes in the right proportions. There are thousands of investment options to choose from, including Unit Trusts and OEICs, Investment Trusts, Exchange Traded Funds (ETFs) and Hedge Funds.

Selecting funds for investment presents many challenges including:

- **The sheer number of fund choices available.**
- **Finding sufficient information to feel confident about a fund choice.** It is important to have reliable sources of information on different funds. Each fund promotes its performance but how can the cause of that performance be confirmed?
- **Making the time to do the right level of research into all the options.**
- **Keeping track of all the manager changes that take place.** Fund managers are joining and leaving fund groups all the time and it's important to keep track of all the movements and work out who was, and who will be, truly responsible for performance.
- **Creating a well diversified blend of managers.** Without information on each manager's investment style and the type of investment they're making, it's very difficult to know how much diversification is on offer or whether several managers selected are in fact investing in similar things.
- **Keeping it up to date.** This is the hardest challenge of all – getting access to meaningful information to judge whether change is needed and having the necessary objectivity to make changes.

Robust method of portfolio construction

Creating well diversified portfolios of investment funds (both passive and actively managed) to match a range of client risk profiles requires significant research expertise and resource. Monitoring the blend of funds selected requires detailed analysis and review. Our assessment of the multi-manager market led us to select two managers:

- **Architas Multi-Manager Ltd.** Architas is a specialist, dedicated investment company resourced with the right people, tools and robust investment process. They are part of the AXA global insurance group.
- **Standard Life MyFolio.** Managed by Standard Life Investment, MyFolio Funds are a family of carefully-constructed portfolios that offer our clients the choice of 15 fully-diversified active and passive investment strategies across five risk levels. They can also be blended to create bespoke investments. Standard Life plc is listed on the London Stock Exchange.

The investment process of both companies is designed to identify consistent, good managers who are specialists in their field and then bring them together in a properly diversified portfolio.

Architas and Standard Life have built a wide range of investment solutions giving flexibility in meeting client needs.

The key features that differentiate Architas and Standard Life as specialists in their field include:

- Comfort from knowing that each investment is backed by deep and thorough research. Architas and Standard Life take an in-depth look 'under the bonnet' before selecting a manager.
- Peace of mind that the mix of managers in each portfolio is properly diversified and that each portfolio has been designed with the aim of giving more consistent returns and avoiding some of the 'roller coaster' of share markets.
- Reassurance that a dedicated team of investment professionals is constantly watching over the investments. It is checking that the managers are on track and that the portfolio stays in balance. It is always looking for new and better options and will make changes when needed.

Where we believe it appropriate, and to help further diversify a portfolio, we may recommend the selection of individual fund managers and/or funds from another multi-manager.

Discretionary Fund Management

If a Discretionary Fund Manager is appointed to manage your investments, that manager will be responsible for establishing the risk level that is most appropriate for you and for recommending an appropriate strategy. Thameside will also work alongside the Discretionary Fund Manager to ensure that the correct risk level is established.

On-going review and management

The ongoing management of an investment portfolio should reflect the strategy that was intended and agreed at the outset.

Reviews carried out by multi-managers

On a day to day basis the multi manager institutions will adhere to their processes for monitoring the underlying fund managers and funds, and portfolios will be rebalanced as appropriate to the intended strategy. This means that a portfolio designed to meet a specific asset allocation will be rebalanced to ensure that asset allocation is maintained, and a portfolio that is designed to satisfy a target volatility level will be managed to achieve that target.

Monitoring conducted

We monitor the multi manager institutions we have selected for our clients and undertake due diligence to ensure that they are adhering to their stated processes, and managing client portfolios to their intended strategy. Where we believe that a multi manager is failing to meet expectations we will investigate, discuss with our clients and take action as appropriate.

Reviews with clients

Unless agreed otherwise, we provide our clients with the reassurance of a regular review of their investment strategy. The frequency of that review will be based upon the specific ongoing service and review agreement confirmed when an investor becomes a client.

An investment review will appraise the performance of your portfolio and assess levels of volatility and return. It will also take into account your current circumstances, investment attitude and any changes to your investment objectives and timescales.

The outcome of a review may involve agreed adjustments or changes to your strategy or your holdings or may well be an agreement that no changes are required at that time.

Investment control – your client account

We are able to offer greater control, simplicity and confidence to our clients in managing and reviewing their investments through a client 'wrap account' we open on their behalf.

In the same way that you might access your bank account online, a client wrap account provides a 24/7 secure and confidential online view of your investment holdings at any time convenient to you. In essence a 'wrap account' provides a cost effective and modern way of holding investments.

Because client access to the account is on a view only basis, it means you won't be able to accidentally trigger any fund trading or switches affecting your holdings.

The account also enables us to electronically administer any changes required to your holdings with your consent but without the traditional paperwork and postal delays.

Conclusion

Our purpose is to maximise the probability of our clients achieving everything that is important in their financial lives. In order to do this we apply the skills of leadership and guidance, and employ the benefits of teamwork and technology.

We trust you have found this document informative and relevant.

We would be delighted to discuss any aspect of the way we help our clients achieve the peace of mind that comes from having a sense of being financially well organised.

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