

Investment Fundamentals No. 1

Simple investment rules (can be hard to follow)

There are three investment rules we think investors should always abide by. Very simply, they are:



1

Diversify sensibly, but not gratuitously



2

Be opportunistic, but only at the margin



3

Have a plan – and stick to it (give your strategy the time it needs to work)

Nobody wants investment markets to fall. However, financial pain aside, a fall can be a useful experience for investors because it provides a real-world test of your investment strategy, your expectations and fortitude. When people invest in shares, for example, they often expect them to go up 10% a year or some similar figure. However, what is often conveniently forgotten is that even if they do that on average, they rarely do it year in and year out.

This is why you need to stick to the plan. Typically 90% of the movement in the value of a standard 70/30¹ balanced fund comes from one asset class: shares. As your portfolio becomes more defensive, your sensitivity to the movements of growth assets like shares diminishes. This is why conservative funds are less volatile than growth funds, but it is also why their expected return is lower. The amount of diversification you employ should be consistent with your tolerance for risk and appetite for return. ‘Over-diversifying’ may save you in the short run, but will cost you over the long run.

“In volatile times there is a natural, human temptation to *just do something*”.

In volatile times there is a natural, human temptation to just do something. Our view is that if your investment strategy was correctly matched to your risk tolerance to begin with, then market gyrations (down and up) should just be part of your long-term investment journey. So does that mean we don’t advocate short-term adjustments to the strategic asset allocation? Not quite. If you believe you (or your adviser or investment manager) have skill in short-term investing, by all means give it a go... but only at the margin, ie in small sizes.

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Our tactical asset allocation process relies on being right on average on many small investments held over the long-term, rather than taking a few large bets over short periods – as is often the temptation. Savvy investors can still take advantage of opportunities when they arise, but they should continue to rely on the main game plan to deliver the vast majority of their investment outcomes.

¹ 70/30 refers to a multi-asset balanced fund with 70% growth assets and 30% defensive assets. Defensive assets are generally fixed interest securities and cash. Growth assets are everything else.

It may be instructive to consider the effects of prior sharp selloffs. Driven by specific events, fear can feed on fear to produce an oversold situation. For example, the so-called 'taper tantrum' of 2013 took the Australian share market from above 5,100 to 4,600. As it turns out, it was the start of a significant market rally.

“Use the past and the present to clarify your future expectations by all means, but stick to your plan”.

Use the past and the present to clarify your future expectations by all means, but stick to your plan. Let's say you have decided to take 5% of your portfolio to chase tactical opportunities. Plan ahead so you know what your reaction will be should it go against you. Therefore, before making the tactical trade, ask yourself the question: 'what loss can I take before I have to pull up stumps?' and write it down. As required, reconstruct your portfolio on the basis of your findings.

About Pental

Pental Group Limited (Pental), known as BT Investment Management until May 2018, is ASX-listed (ASX:PDL) with \$99.0 billion in funds under management as at 31 March 2018.

The philosophy and success of the BT investment management business since the 1970s led us to link our new name and brand to our heritage: Back in 1971, Ord-BT established Pental Nominees to hold assets on behalf of its first prospective client the Dalgety Pension Fund, being a reversal of Dal(gety) Pen(sion).

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Pental is a diversified global investment manager with offices in Sydney, London, New York, Boston and Singapore.

Pental offers over 50 investment strategies including equities, diversified, property, cash and fixed income products. At 31 March 2018 Pental employees were the largest single shareholder group, holding ~14% of total PDL shares on issue, providing strong alignment between employees and the company's growth and success.

For more information, speak to your adviser
or visit **pentalgroup.com**

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