

FREQUENTLY

QUESTIONS

ASKED

from our clients

If you have a question about any aspect of financial planning then our FAQs should help to make things clear.

If not please feel free to call Polestar on **01252 626200** or email **Office@PolestarFP.com** to speak with your adviser or to talk to us about your financial plans if you are not currently a client.

Contents

PART 1 –

The basics of Bonds, Equities and Property

1. What is investing?	3
2. What does good investing look like?	3
3. What does bad investing look like?	3
4. What is an equity (or stock)?	3
5. Are all equities the same?	4
6. What is a 'small cap' stock?	4
7. What is a 'value' stock?	4
8. Are the higher returns from value and size stocks guaranteed?	5
9. What is the difference between a 'developed' and an 'emerging' market? . .	5
10. What is a bond?	5
11. Are all bonds the same?	6
12. What are REITs?	6
13. Is buy-to-let property as an alternative to an investment portfolio?	6
14. What is liquidity?	6

PART 2 –

What is systematic investing and advice?

15. What is your process for providing quality advice?	7
16. What is 'systematic' investing?	8
17. What is 'judgmental' (active) investing? . .	8
18. How did you arrive at the structure of my portfolio?	9
19. Why is diversification so important? . . .	9

Portfolio building and what is risk?

20. Why do I own bonds that do not pay me much?	10
21. Do I have to be invested in complex investments to earn a decent return? . .	10
22. Why do you pay so much attention to product costs?	10
23. How do you select individual funds? . .	10
24. What do you mean when you talk about 'risk'?	11
25. Is taking risk a bad thing?	11
26. How much risk should I take on in my portfolio?	12
27. Should I worry when markets fall? . . .	13
28. Will my returns be similar to that of the UK FTSE 100?	13

PART 3 –

Living with your portfolio

29. How will I judge whether my investment program is successful?	14
30. How often should I look at my portfolio? .	14
31. Why does my portfolio not change much?	14
32. What regular 'maintenance' do you do on my portfolio?	14
33. What is rebalancing and why is it important?	15
34. How safe is my money – and where does it go – when I invest?	15
Notes and references	16

PART 1 –

The basics of Bonds, Equities and Property

1. What is investing?

That may seem an obvious question with an obvious answer. In some ways it is. We believe investing to be the process of building and preserving purchasing power that helps to fund lifestyle and personal choices, now (if retired) or in the future (if accumulating wealth). It is a slow, emotional, and sometimes painful process that requires a well-thought-out plan, executed over many years with discipline and patience. Anyone hoping to get rich quick is a gambler and is playing the wrong game. Likewise, anyone unwilling to take on at least some risk is a saver.

2. What does good investing look like?

To us 'good investing' is about being able to sleep well at night knowing that your portfolio has a good chance of delivering you with the growth in wealth that you need. We think this is best achieved by being guided by the academic theory and empirical evidence available to us. It turns out that focusing on broad diversification (across asset types, markets, sectors, and companies) to capture broad market returns makes sense. Not trying to time when to be in or out of equity markets or picking individual companies to invest in, keeping investing costs low and sticking with the plan, all really improve the odds of a successful outcome. The one thing that no-one can control, though, is what the markets do, particularly in the shorter term. Time,

patience, and discipline are your allies in the three-steps-forward-and-one-step-back, world that investing inhabits.

3. What does bad investing look like?

Low-odds-of-success activities like jumping in and out of equity markets, trying to pick the next Amazon or Apple, owning only a handful of stocks, chasing markets (or themes and sectors or 'star' fund managers) by looking in the rear-view mirror are likely – over the longer term – to lead to disappointment and a narrowing of future lifestyle and personal choices. Thinking that three to five years is long term, or that you or a fund manager have special insight that others do not, or acting on a hunch, are all likely to result in disappointment, unless you simply get lucky. Luck is not a strategy to base your financial future on!

4. What is an equity (or stock)?

An equity (or share) represents the partial ownership in a company and the rights that this conveys upon the owner including your share of any dividends paid and a claim on the company's assets. Returns from equities come from changes in the price of the shares and cash dividends received (if and when they are paid). The sale of shares may result in a capital gain or loss, which may be taxable, depending on which type of investment account they are held in.



5. Are all equities the same?

No, they are not, as one company may have very different characteristics to another. A company's size, sector and firm-specific strategy will vary, as will the markets in which they operate. Whether a company's shares are cheap or expensive relative to some fundamental metric, such as book assets, sales or cashflows will also result in different risk and return characteristics. Broadly, smaller stocks behave differently to larger companies; relatively cheap stocks – scaled by a fundamental metric – behave differently to relatively expensive companies. Likewise, developed market companies face different challenges and risks compared to companies domiciled and operating in emerging economies. Some of these groups of stocks provide the opportunity for higher expected returns on account of the higher risks they exhibit (as a group). These differences in characteristics also provide the opportunity to diversify a portfolio more fully and to position it along these axes of difference, either to reduce risk or enhance returns (or preferably both).

6. What is a 'small cap' stock?

A 'small cap' (smaller company) stock is a company whose size, as defined by market capitalisation – the price of each share times the number of shares – is smaller than other stocks in the market. A commonly used definition of 'small cap' is the bottom 10% of stocks by

market capitalisation. Empirical research suggest that globally, smaller companies have offered a premium, on average over time (but certainly not every year), relative to larger companies. Assuming that markets work pretty well – which we do – this premium must be in return for taking on a higher level of risk associated with owning smaller companies.

7. What is a 'value' stock?

A 'value' stock is a company whose price is cheap relative to some metric – or 'fundamental' – that relates to the firm. This 'fundamental' could be its book value, earnings, sales, dividends, cash flow or some other measure. The opposite of value is 'growth' where the price is high relative to the metric chosen. For example, stocks may be sorted by price-to-book i.e. the multiple of book value that an investor is willing to pay to own the shares: the bottom 30%, being those with low price-to-book ratios, may be referred to as value stocks and the top 30% may be described as growth stocks. Empirical research suggests that value stocks across global markets have offered a premium, on average, relative to growth stocks, in return for taking on a higher level of financial risk associated with them. An alternative behavioural explanation for the premium is that investors often get too excited about companies with great stories and overpay for them; anything that you have not overpaid for – being the more boring value stocks – will therefore outperform down the line.

8. Are the higher returns from value and size stocks guaranteed?

Unfortunately not. As with every decision in investing, there are no guarantees, but we can stack the odds in our favour. If you think about it logically, premia must be volatile; sometimes they will deliver a positive return relative to the market and sometimes they will not. If these extra premia were certain, everyone would simply own value stocks and smaller companies and capture extra returns on offer for no risk. Yet, if there was no risk to owning exposure to these companies, there would be no premium! Time is your friend in investing and the longer you can hold for, the greater the chance that you will be rewarded for taking on diversified risks. It is worth remembering the equity premium for holding company shares relative to placing bank deposits is not guaranteed either, but again, time is your friend.

9. What is the difference between a 'developed' and an 'emerging' market?

That is a good question and a bit of a grey area. Generally, emerging markets have lower levels of gross national income per head than developed markets. Other factors, such as corruption levels, political stability, or capital market development and liquidity, may also be used to distinguish between the two. A few countries sit on the cusp, like South Korea, which is considered as being a developed nation by the index provider FTSE, but an emerging market by the index provider MSCI. Remember that many multi-national companies operate in both developed and emerging markets e.g., Microsoft, HSBC, and Samsung. In general, emerging markets are deemed to be riskier than developed markets and should, on average over time, attract a premium above developed markets. Again there are no guarantees.



10. What is a bond?

A bond is an IOU provided in return for a loan made to a government or company with an agreed rate of interest and a promise to repay the loan at a specific date in the future. Bonds are also referred to as 'fixed interest' securities, for this reason. Once issued, bond prices move in response to changes in the market rate of interest (yields). Yields may move due to general economic conditions such as rising inflation, which tends to push up all bond yields (interest rate risk) and due to company-specific reasons which may affect a company's ability to meet its interest and debt repayment obligations (credit risk). When bond interest rates (yields) rise, bond prices fall, and vice versa.

11. Are all bonds the same?

Absolutely not. In fact, bonds range from risk-free deposits (e.g. bank deposits under £85,000 in the UK which are backed by the government if the bank goes bust) to equity-like 'high-yield' bonds. How long you lend for, and who you lend to, matters. The longer you lend for i.e. the further out the maturity date of the bond is, the more a bond's price will move when yields change. The lower the

quality of the borrower, the higher the interest you receive. Unfortunately, when times are hard these borrowers are less likely to be able to pay you back and investors tend to sell their bonds or demand higher yields, driving prices down. As a consequence, they are poor diversifiers of equity risk, which is the primary reason for owning bonds for most long-term investors in the first place. The lower the quality of the borrower, the more equity-like the characteristics of the bonds they issue (and investors own). Our general rule is that if you want equity-like risk, own equities.

12. What are REITs?

REITs (Real Estate Investment Trusts) are companies that invest in commercial property assets that are owned primarily for rental income. Provided that a major proportion of the rental income is passed through to end investors (note these rules differ slightly by tax regime) then the REIT itself avoids paying corporation tax. REITs listed on global stock exchanges provide investors with liquid access to underlying illiquid commercial property assets through the secondary stock market (i.e. buying and selling shares).

This is in stark contrast to 'bricks-and-mortar' property funds that must sell buildings to meet the liquidity demands of fund investors. You may have read in the papers that many such funds have been suspended in recent times as they offer to provide daily liquidity, yet the property assets that need to be sold to raise cash could take many weeks if not months or occasionally years to sell.

That is why we prefer REITS. Several hundred REITs exist around the world, providing diversified access to commercial property by geography, property sector, manager strategy

and tens of thousands of individual properties in aggregate. Each REIT can, in essence, be thought of as an individual property fund, thereby providing broad diversification when owned as part of a broadly global REIT (index) fund.

13. Is buy-to-let property as an alternative to an investment portfolio?

There is no doubt that buy-to-let residential property has been a profitable investment for some over the past few decades. However, it is not without considerable general and specific risks, not least an increasingly unfavourable tax regime, the risk of rent arrears (e.g. Covid-related), voids, dilapidations, and the need to run a hands-on portfolio and, in effect, a small business. There is also the erroneous assumption that residential property only ever goes up in value. The easy access to mortgages to leverage investor capital is the main attraction of buy-to-let, rather than the underlying dynamics and return characteristics of the UK property market. Buy-to-let properties may in some cases sit sensibly alongside an investment portfolio, but rarely replace one entirely, or even in the main.

14. What is liquidity?

Simply put, a liquid asset is one that allows you to dispose of in a timely manner with little price impact. That is different to be able to sell an asset at any price. We prefer liquid assets because they reduce the chance of any unwelcome surprises. This is one of the reasons we tend to avoid investments such as private equity, hedge funds, and brick-and-mortar property schemes within your portfolio.



PART 2 – What is systematic investing and advice?

15. What is your process for providing quality advice?

Stage 1.1) Discovery or Review Meeting

Your financial planner will start by listening carefully to your objectives, needs and priorities, in the context of your short, medium and long term financial aspirations.

By gathering information from you, they begin to understand your current situation and what provisions you have in place already.

Then, by exploring your hopes and aspirations, they can construct a picture of what you want to achieve, taking into account your knowledge, experience and attitude to risk and return. This stage also allows you to understand what to expect from us and how you will benefit from using our services.

Stage 1.2) Research to Build Client Plan

We'll explore and research various scenarios and options and start to put together a road map to help you move towards achieving your objectives.

We will assess the suitability of your current plans and make recommendations to help you achieve your current and future objectives. This stage is fee based.



Stage 1.3) Present Plan & Recommendations

Your financial planner will sit down with you and go through your plan and recommendations answering any questions you may have. This stage is fee based.

Stage 2) Implement Plan & Recommendations

Here's where your plans start to take shape. Most of our clients prefer us to complete, check and manage the documentation required for them to put 'Their Plan' into action. This saves them a lot of time and energy, and helps ensure that plans are set up in line with expectations. The cost of this service will be included in the fee structure that has been agreed.

Alternatively you may decide you wish to implement our recommendations yourself, and so can simply pay a fee for our time and expertise up to this point.

Should you choose to implement your plan and your choice of recommendations, your fee in 1.2 and 1.3 may be discounted against your stage 2 implementation fee.

Stage 3) Ongoing Support, Your Choice

We believe that most clients will benefit from a review of their circumstances and we offer a range of options. This may depend on which stage of life you are in as well as your relative level of wealth.

Many clients like to meet up regularly to take advantage of valuable allowances, or understand the impact of UK Government Budget announcements.

You will also hear from us at other times during the year when we feel something may be of interest to you, or you may wish to get in touch yourself, if your circumstances or objectives have changed.

16. What is 'systematic' investing?

We often refer to the way we invest as being a 'systematic' approach. What we mean by this is that we adopt a disciplined, rules-based, and as unemotional approach to investing as we can. We structure portfolios around long-term strategic allocations to different types of investments, rather than trying to second guess short-term market and company movements and adjust the portfolio accordingly. The latter might seem like the sensible thing to do, but the evidence suggests

that outguessing the market is exceptionally hard to do persistently. Our aim is to pick up the broad market returns on offer in compensation for market risks taken on, and rebalancing portfolios back to their original structure on a regular basis as they stray from the original plan.

Funds used to implement the strategy are always highly diversified, transparent and lower cost and structured to capture exposure to broad market risks. For example, if we want to access smaller companies to capture the higher returns potentially on offer, we will seek out funds that have a very broad exposure to the small cap universe – in order to effectively capture these characteristics – rather than choosing a fund where the fund manager owns a few hand-picked companies that they hope will be stand-out winners. In a systematic approach, returns come predominantly from markets, not from fund manager skill.

17. What is 'judgmental' (active) investing?

Judgmental – or 'active' – management differs from systematic investing because the underlying premise is that a fund manager, using his or her judgment, will position a portfolio to take advantage of short-term forecasts of market or company valuation levels in an attempt to beat the market. Unfortunately for them, trading in the markets is a zero-sum game i.e. for every winner there has to be a loser. Markets also work pretty well, which means they incorporate new information reasonably efficiently into prices. Active management costs also tend to be much higher than systematic approaches both by way of higher manager fees and the costs associated with buying and selling stocks or bonds. The consequence of these hurdles is that the vast majority of active managers fail to deliver on their market-beating promise. Even for those that do, it is hard to distinguish between skill and luck and even harder to identify skilled managers for the future. This is another low-chance-of-success strategy, which we avoid.



18. How did you arrive at the structure of my portfolio?

Building an investment portfolio requires a combination of investment science and a good dose of common sense. The evidence suggests that timing when to be in and out of markets (or sectors, or companies) is extremely difficult and persistent market-beating skill is very rare and hard to identify in advance.

The emphasis in constructing portfolios therefore lies in making long-term 'strategic' allocation decisions that seek to capture broad, favourable characteristics offered by different investment assets, such as equities and bonds, over the medium to longer term. Placing an emphasis on diversification avoids the consequences of specific companies, sectors or markets doing poorly and also ensures that you always own the rare companies that grow from nowhere into behemoths, such as Amazon or Apple.

Avoiding too much in the UK makes sense, given its small size (a little over 5% of global markets), sector biases and stock concentration levels, owning some emerging markets and taking small above market-weight positions to smaller companies and value stocks can also make good sense for disciplined longer-term investors, seeking to improve returns.

Balancing the potentially large – but hopefully shorter-lived – falls in equity markets, with higher quality bonds that hold up well at these times is a sensible strategy. In bonds, as in equities, being

globally diversified – with the caveat that foreign currency risk is hedged out when owning bonds – is a good starting point.

19. Why is diversification so important?

Diversification matters because we have very little idea how companies, market sectors, geographic markets and asset types will fare in the short term, despite increasing confidence with how they might – but are not guaranteed to – perform in the longer term. Making concentrated bets on a few companies in the UK has a far higher chance of pain than a broadly diversified global portfolio of equities, counted in thousands of companies across all sectors, markets and company size. Being well-diversified is, primarily about not losing money permanently.

Second, it is about avoiding being stuck in a few companies, a sector or a country that performs poorly over an extended period of time and takes a long time to recover.

Third, it is about capturing the areas of the market that – at a particular moment in time – are driving returns. Recently, it may have been all about US technology firms, but tomorrow it will be something else entirely.

Diversification helps smooth returns. Inevitably there will also be parts of the portfolio that will be doing better or worse than others in your portfolio, but that is the nature of the game. Try not to look on enviously at recent winners, but just be glad that you already own tomorrow's winners.

20. Why do I own bonds that do not pay me much?

It is quite simple really. Most longer-term investors own bonds in a portfolio to protect against large equity market falls that might halve the value of their equity assets, or worse, in the short term. High quality bonds provide the best defence at these times as investors get nervous and scared money moves into 'safer' bond assets driving prices up.

These tend to be bonds issued by strong governments and companies whose cost of borrowing is low and whose bonds are liquid. In today's markets, bond yields are exceptionally low in general and those of high-quality bonds are the lowest. You should think of them as being an insurance policy with a high premium. Investors can either pay the premium by owning bonds or self-insure, by riding out an equity market storm. Every investor has a balance that makes sense for them.

Trying to reduce the premium by holding bonds that have higher yields (i.e. weaker borrowers) significantly reduces the pay-out terms of the insurance policy as they exhibit equity-like characteristics just when you do not want them to. Holding low quality bonds is like picking up pennies in front of a steam roller; it pays off until you trip over! If you want to take on more risk to increase your returns, simply own more equities instead.

21. Do I have to be invested in complex investments to earn a decent return?

One of the largest myths in investing is that there is some relationship between complexity and better outcomes. That simply is not true. By and large, complexity hides risks and costs. If it is difficult to understand how returns are generated in an investment, then it is usually difficult to identify the underlying risks that you will be taking on. If an investment looks too good to be true, it probably is. We allocate to transparent, rules-based strategies. This risk-focussed

approach to investing helps to mitigate the risk of unwanted surprises. We find 'Occam's razor' to be a useful tool, where the simplest solution is often the best solution.

22. Why do you pay so much attention to product costs?

The reality is that over the long term, equity and bond returns probably sit in the region of 4% or so above inflation for equities and 1% for bonds. Shorter-term expected returns may be even lower than this. That does not give much room to play with. Product costs come in two main forms: the Ongoing Charges Figure (OCF) of the fund and portfolio transaction costs incurred when a fund manager trades the underlying portfolio, which are both deducted from fund performance. Low OCFs and low levels of transactions leave as much of the market return available to investors as possible. Money kept in the portfolio compounds over time – in a non-trivial manner – to the benefit of the investor.

23. How do you select individual funds?

Our focus on diversification, low cost and a rules-based approach to capturing market risks helps us to identify funds with these characteristics from an extremely extensive universe of products available for sale to retail investors. We screen against a range of 'systematic' criteria to narrow down this broad market universe into a 'long list', which is refined with further work down into a tight 'watch list' of the best funds that meet our criteria. We then undertake due diligence on a number of funds in each asset class and finally identify our recommended funds. Each fund must be approved as suitable for use by clients by the firm's Investment Committee and your advisor will ensure that funds recommended are suitable for your individual circumstances. Regular screening and due diligence are undertaken to make sure the existing choices are doing their job properly and that any strong, new products are identified and reviewed.



24. What do you mean when you talk about 'risk'?

That is one of the trickiest questions to answer in investing. There are many different kinds of risk that investors face and different measures of these risks. For investors planning for the future, the ultimate risk is that they fail to meet their goals. That is very different to what is often referred to as 'risk' which is the volatility of, say, monthly or annual returns.

Goal risk is most critical to you and is addressed through a combination of owning a soundly structured portfolio and good financial planning. Market volatility, on the other hand, manifests itself more in the emotional pressure that comes with seeing the value of your assets fall, despite the fact that you do not need to – or have any intention of – cashing them in.

In a volatility-oriented definition of risk, equities are risky, and cash is not risky. During the Global Financial Crisis of 2008-9, equities fell heavily whilst cash held its value. Yet since then, cash deposits have lost around one fifth of their purchasing power once inflation is considered whereas global developed equities have doubled in value, even if you invested at the height of the market in late 2007. Which is riskier to your long-term financial goals? Cash or equities?

25. Is taking risk a bad thing?

That depends on what risk you take. Everyone knows that risk and return are the opposite sides of the same coin, so if you take on more risk then you should expect more return. By and large, good risks are those for which adequate compensation is likely to be received, with a high degree of confidence, over a sensible period of time. The uncertainty about what returns equities will deliver tomorrow, next month or next year is the very source of their higher returns. Bank deposits on the other hand offer great certainty, but consequently deliver poor returns.

Owning a material allocation to globally diversified equity investment in thousands of companies – if you have a 20 year plus horizon – is potentially a good risk to take, as it is probable that you will earn a reasonable return above inflation, on average, over time, despite the sometimes-material equity market falls along the way. On the other hand, owning shares in one or a small, concentrated pool of companies is far riskier as you have all your eggs in one basket as some of the companies may perform poorly or fail altogether.

Permanent loss of capital is to be avoided at all

costs. On the other hand you may just get lucky (but don't bank on it!).

'Bad' risks are those that you are inadequately compensated for. Academic research and empirical evidence help us to separate good and bad risks. For most investors, bad risks include: those that can be diversified away; a lack of liquidity; trying to pick a winning fund; jumping in and out of markets; paying costs that are too high; and ultimately fraud. These all place your long-term wealth at risk and although a few may get lucky over specific periods, the odds of success will be stacked against you.

Even owning good equity risk can, for example, be bad if there is a mismatch between the time horizon that makes the risk acceptable (e.g., 15-20 years plus) and the amount of time you intend to invest for (e.g., 5 years).

In general, we take on broad global equity market risk, avoiding concentration and liquidity risk. In bonds we tend to take on low levels of interest rate and credit risk but avoid material equity-like credit risk and foreign currency risk. Judgmental – or active – manager risk is largely avoided, as the evidence suggests that it is largely uncompensated and true skill is hard to identify in advance.

26. How much risk should I take on in my portfolio?

A suitable level of risk to take in a portfolio is a balance between your need to take on risk to achieve your goals and the falls in the value of your portfolio that you will experience from time to time that will impact you both emotionally and financially.

Every investor has a point at which the upside returns no longer compensate for the worry and pain of seeing a portfolio fall, even if there is plenty of time for the portfolio to recover. This is often referred to as an investor's risk tolerance or willingness to take risk. There may also be a minimum value of your portfolio that if permanent losses were to be incurred, you would jeopardise even your essential planning goals. This is known as your financial capacity to suffer losses.

One of the most important ongoing areas of discussion is ensuring that we identify the portfolio that provides the best trade-off between these elements for you. Changes in your circumstances may result in a change in the overall level of risk that is most suitable for you. Identifying a suitable level of risk to take in a portfolio is the primary investment decision that any investor makes and this needs to be revisited on a regular basis.



PART 3 – Living with your portfolio

27. Should I worry when markets fall?

The rational answer is, of course, 'no'! Yet we all know how difficult it is not to. Let us assume that in the cold light of day you have discussed with your adviser the question of how much equity risk is suitable to take on in your portfolio, and you agreed on 60% equity exposure with 40% in bonds. If the equity markets fall by 50% – which they have done several times in the past – and your high-quality bonds hold their value, your portfolio would be down around 30%.

So, a £1 million portfolio would now be worth £700,000, down £300,000. The mind starts racing, the heart starts pumping and all the news is doom and gloom. But do you need the money today or even in 5 years' time? The answer is probably no, as otherwise you would not be invested in equities.

Even if you are drawing an income, you still have £400,000 sitting in high quality bonds that can meet your expenditure needs. These bonds could support £40,000 p.a. of income for 10 years, which would allow for a very slow and unusual equity market recovery, in an extreme case.

It never feels pleasant, but understanding that you do not need the money, that falls are not losses unless you sell, and that a highly diversified approach greatly reduces the risk of permanent loss of capital that can arise in

concentrated portfolios, should help to see you through. One day – if you have not already – you will experience a tough time in the markets. Lean heavily on your adviser if you need to at these tough times for reassurance.

28. Will my returns be similar to that of the UK FTSE 100?

The short answer is 'no' for two main reasons. The first is that few investors are invested 100% in the equity markets, as that takes a very strong stomach and iron-clad discipline. It is likely that your portfolio will be a combination of equities and higher quality bonds.

The second is that the equity portion of the portfolio will be diversified across a wide range of global markets avoiding the risk of the UK market performing poorly. So, when you hear on the news that the UK's FTSE 100 is down, say, 20% in a year, it is unlikely that this will be the same as your portfolio's outcome.

Sometimes a specific market, such as the UK, may do exceptionally well in a year and your portfolio will be below the FTSE 100, but remember you don't own 100% equity and you own a more diversified pool of equities that is potentially a better option – on balance – over the long term. Try not to anchor on this somewhat meaningless measure that the news outlets use!

29. How will I judge whether my investment program is successful?

Over the longer term, being on track to meet your financial goals is the true definition of success. The first target is to be growing – or at least maintaining your portfolio in real (after inflation) terms over the medium term. It may not happen on a year-by-year basis, but over a five-year term or more you would hope that to be the case.

The one thing you should not do is to judge your portfolio on its outcome compared to other assets or portfolio structures that have done better identified with benefit of hindsight! These envied outcomes probably occurred simply by chance and as part of loud market noise of the recent past.

You should judge your portfolio strategy on the quality of the decisions that were made when it was put together, and their ongoing validity today. Be comfortable in the knowledge that you have stripped out as much of the uncompensated risk as possible and paid out the minimum possible in costs.

Sometimes your returns will be disappointing, but unfortunately that is the way of markets from time to time. Be confident in your long-term strategy and dig deep to find the conviction and fortitude to soldier on at these times. That is not always easy, but to do anything else would be to pretend that you (or we, or anyone else for that matter) could see into the future. Unfortunately, we cannot.

30. How often should I look at my portfolio?

Preferably not too often! As the old saying goes, you can look at your cash daily, your bonds every 2-3 years and your equities every 10 years. Given that in one in every three years or so equities are expected to deliver negative returns, there is plenty of scope to be disappointed in the short run. However, the persistent ability of equities to deliver the opportunity for strong inflation-plus returns over the longer-term needs to provide a sense of balance when your portfolio is down in

value, as it will be from time to time. Remember that a fall in value is not a loss unless you sell out, which in the shorter-term most investors have absolutely no need to do.

31. Why does my portfolio not change much?

One of the great misconceptions about investing is that you have to be busy anticipating and reacting to market events and opportunities. That is not what we do, based on where the evidence suggests that success lies. In fact not doing something is often far harder than doing something.

Sometimes investors get tempted to look through a hindsight lens at other 'better' performing investments or forward at 'obvious' future events. This can manifest itself in either blaming an advisor or putting pressure on them to act. A topical case is Tesla – best known for its electric cars – whose shares rose almost eight-fold in 2020. No-one knew this was going to happen either in timing or magnitude and no-one knows what happens next. But everyone wishes they had owned more Tesla or a fund that (probably luckily) did! That is not a reason to act or change course and overweight Tesla and tech stocks.

Our portfolios are structured for the long-term and have identified best-in-class funds to capture the risk exposures we wish to take. Holding firm – unless the evidence changes – is hard, but the right thing to do. A significant amount of ongoing portfolio tyre-kicking and maintenance goes on behind the scenes in the Investment Committee which sits in May and November each year.

32. What regular 'maintenance' do you do on my portfolio?

There are a number of levels on which maintenance occurs. At the portfolio level, the latest research and evidence is reviewed in the Investment Committee to see if it points to issues that need deeper discussion and

possible portfolio strategy changes. This is quite a slow-burn process and changes tend to be evolutionary over time, rather than revolutionary. Remember, we are not talking about shorter-term market outlooks and forecasts here and moving the portfolio around tactically, but long-term understanding of market risks and their expected compensation over the longer term and how this might impact long-term strategy.

At the product level, funds are regularly reviewed to make sure they are doing the job asked of them and regular screening for new, strong products ensures that the best products are always available to investors.

Finally, portfolios are rebalanced back to their original structure on a regular basis to ensure that the level of risk being taken on remains suitable. Tax consequences of portfolio changes are always part of the issues we consider and discuss with you.

33. What is rebalancing and why is it important?

Rebalancing takes a portfolio back to its original structure. For example, if the equity markets have performed well, then a portfolio with a target weight of 60% in equities may end up with, say, 70% in equities. Without being rebalanced, the equity content (being, in general, the higher return asset in a portfolio, over time) tends to drift upwards and the swings in portfolio values may become alarming.

Likewise, when equity markets fall, the portfolio now has too little risk in it and it makes sense to sell safe bonds and buy equities. No-one feels like doing this when markets are down. Yet you will be buying more units in equities at a cheaper price, which lowers the price recovery needed to get back to where you started – that is simply maths.

Having a systematic, disciplined approach to rebalancing allows us to overcome the emotional inertia that often creeps in when markets fall. Rebalancing is a contrarian process, selling out of assets that have done well and buying into assets

that have performed less well. It requires no forecasts of market valuation levels, but simply sells a proportion of better performing markets, banking the profits, and buying into assets that have performed less well. Whilst this process has the possibility – but not the guarantee – of a rebalancing return bonus, its true value lies in maintaining an appropriate level of risk in your portfolio.

34. How safe is my money – and where does it go – when I invest?

That is a good question. It may help if we follow the trail of advice and money through from investing to disinvesting. First, your adviser provides advice and product recommendations as a regulated person employed by a regulated firm which is overseen by the UK's Financial Conduct Authority (FCA) and they must abide by the regulations in place. You can look up a firm in the register on the FCA's website. In the event that you are not happy with the advice you receive you have the right to complain to us and then, if the situation is not resolved to your satisfaction, to the Financial Ombudsman Service, who will take over the complaint.

So where does your money go? The first thing to note is that, as an adviser, we never handle any of your money. You will have a third-party investment 'wrap' platform account where your assets are administered. Your assets, including any cash, are completely segregated from the assets of the platform company in accordance with the FCA's Client Assets rule. This means that if the platform goes into administration, your assets are ring-fenced and protected from its creditors. This separation is usually achieved through all client assets being held via a nominee company, separate to the operating platform company, with you recorded as the beneficial owner.

When you invest in a fund, cash is either already in your account with the platform or you send it directly to your account with them, or it is raised from the sale of some of your existing assets held on the platform. The order for fund units is

sent by the platform to the fund administrator and the cash is sent to the fund's segregated client cash account held with the fund's third-party custodian. To avoid fraud the fund manager and the custodian should always be independent third parties. Your beneficial ownership in units in the fund is recorded. The fund manager simply has the authority to pass trading instructions to brokers that are then settled with the custodian.

In the event that the fund manager fails, they can simply be replaced by the fund's trustees (otherwise known as the ACD) with another manager. In the event of the failure of the custodian, the fund's assets are ring-fenced from the balance sheet of the custodian. The fund can appoint an alternative custodian. Records of the ownership of the funds are held by the fund administrator (at the nominee company level) and by the platform at the client level. When you ask for cash from your platform, it will only be paid out to a bank account of your choosing. The final layer of protection is the Financial Services Compensation Scheme (FSCS), which protects – to varying degrees – against corporate failure. Products domiciled outside the remit of the UK will fall under other regulatory regimes. Rest assured that your money is as safe as it can be, over and above the market risks that you take on in your portfolio.

Notes and references

This is a purely educational document to discuss some general investment related issues. It does not in any way constitute investment advice or arranging investments. It is for information purposes only; any information contained within them is the opinion of the authors, which can change without notice. All information is based on sources that Polestar in conjunction with Albion Strategic Consulting (Albion) believes to be reliable. No responsibility can be accepted for actions taken as a result of reading this document.

Past performance is not indicative of future results and no representation is made that the stated results will be replicated.

Errors and omissions excepted.

Polestar is an Appointed Representative of Quilter Financial Planning Solutions Limited, which is authorised and regulated by the Financial Conduct Authority. Financial Conduct Authority does not regulate advice on trusts. Principal Ian Russell DipPFS. Polestar is part of Polestar Holdings Ltd. Incorporated in England and Wales Number 11882633.

Do you have a question about any aspect of financial planning?

Our FAQs should help to make things clear.

Call Polestar on 01252 626200 or email Office@PolestarFP.co.uk if you have any more questions, or to talk to us about your financial plans.

CLIENT RESOURCES

Key Guides

Polestar produce a series of Key Guides to address complex issues in a way that is simple and easy to understand. They are regularly updated, highly informative and free to download from our website.

polestarfp.co.uk/resources/key-guides

They cover the following areas (click to view):

- ▶ [Investment planning and asset allocation](#)
- ▶ [You and yours – estate planning](#)
- ▶ [The financial planning journey](#)
- ▶ [Taxation of property](#)
- ▶ [Saving for retirement](#)
- ▶ [Investing for Children](#)
- ▶ [Business succession planning](#)
- ▶ [Investing tax-efficiently](#)
- ▶ [Pensions and tax planning for high earners](#)
- ▶ [Financial protection – for you and your family](#)
- ▶ [Making the most of ISAs](#)
- ▶ [Taking income at retirement](#)



Website

As well as the Key Guides our website contains other useful client resources such as calculators, videos and blog.

polestarfp.co.uk

Social Media

You can also find us on the following social media channels:



[@PolestarFP](https://twitter.com/PolestarFP)



facebook.com/PolestarFP



linkedin.com/company/Polestar-FP