

# standing up to the challenge

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**Joe Le Jehan** explains why multi-asset investing is critical to success in a rapidly changing market.



Financial markets are more schizophrenic than ever. They seamlessly lurch from pricing one extreme scenario to another. Over the last 18 months we've moved back and forth between hyperinflation, deflation, stagflation, recession, depression, reflation, recovery and expansion – and each of these distinct scenarios potentially warrants a different asset mix. This is why multi-asset investing makes sense. The ability to draw upon different asset classes has been critical to investment success in recent times. We see no reason for this to change in the future. Add in sufficient flexibility to be nimble, but provide a structure that builds an appropriate expectation amongst clients, and you've gone a long way to supplying a compelling solution in what are quite extraordinary times. This is the demand which the Cazenove Diversity range of funds seeks to satisfy.

## easier access

Regulation changes in recent years have made access to multi-asset investing easier for advisers, prompting a range of alternatives to appear in the retail market. At Cazenove we utilise a multi-manager approach, providing access to 'best-of-breed' funds across a multi-asset portfolio. There are, though, a wide variety of different approaches.

There is little point in denying that the last year made achieving positive returns a Herculean task for most investors. The near

collapse of the financial system and the downturn that followed impacted every asset class and caused widespread turmoil across global markets. But diversification across asset classes should provide consistent and low volatile returns through any economic scenario.

If the last year has shown us anything though, it is that successful multi-asset investing requires more than this. Diversification for diversification's sake, in fact, proved to be pretty ineffective, as anyone exposed to private equity or property would probably agree! These were areas to avoid as the global deleveraging process saw liquidity withdrawn from the system at an unprecedented rate and valuations adjust downwards accordingly.

## strategic allocation

The increased correlations between asset classes due to the global unwind is only part of the story. The key to multi-asset investing last year was to find those areas with tailwinds and, crucially, steering clear of those with structural difficulties. It is this strategic approach to diversification that should continue to work in the future.

There were, after all, areas to make money last year and at least provide some respite from the wider problems. Certain structured products, for instance, provided downside capital protection against falling equity markets, whilst providing a stable yield.

Of course, even here the issues of many financial institutions meant counterparty risk was a troublesome concern in choosing the right product. Elsewhere, selected hedge fund and fixed interest holdings may also have helped performance.

This willingness to strategically allocate between asset classes therefore remains critical to successful multi-asset investing. But is it enough? We think not. The last 18 months highlight how it is just as important to find a manager willing to rotate exposure within asset classes.

For instance, to provide a consistent return through 2008 you needed completely different equity portfolios from one period to the next. In the early months industries related to China such as miners and commodities led the market as inflation remained a concern and oil spiked up above \$140 in mid July. Holding onto such a portfolio in the second half of the year would have been disastrous as thoughts turned to an impending recession and many of these same areas were savaged.

Unfortunately, history has shown that many investors get caught out at these turning points – having 'followed the herd' to these popular areas only to find themselves overweight as markets reverse. We only need to look back at the end of the property boom and the losses that those late to the party suffered to remind ourselves.



## importance of flexibility

Last year it was those tactically nimble managers able to transition to more defensive sectors (eg pharmaceuticals, utilities, tobacco) that provided some respite in the later months. This flexibility and willingness to tactically rotate holdings again proved crucial to provide consistency of returns through the year.

Allocating capital to macro-led managers in late 2008 for instance was preferable to holding bottom-up orientated stock pickers – many of whom suffered as company specifics provided little differentiation in relative performance.

It is not just in equities either. In fixed interest, the post-Lehman Brothers freefall left many overexposed to illiquid bank debt as riskier assets struggled and deleveraging gathered pace. In the hedge fund world market-neutral products provided more protection than directional vehicles – the latter more geared into the performance of their particular asset class. The list goes on – and continues to highlight the need for a flexible approach to asset allocation and diversification.

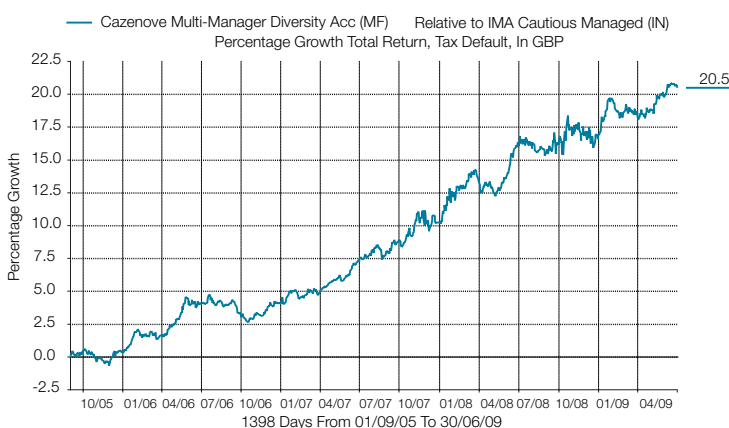
## looking ahead

If we continue to lurch from one extreme to another in markets then the need to find an acceptable asset mix becomes ever more important. What if inflation concerns reappear, for example? Perhaps broader exposure to real assets (direct property, commodities et al) or inflation linked bonds may provide some upside. Or deflation –

# risk and return

A difficulty for advisers remains the degree of freedom to give a multi-asset manager. At Cazenove, our Multi-Manager Diversity range provides a spread of funds across the risk spectrum offering both tactical and strategic allocation within and across asset classes. We believe that investing in this manner can provide the consistent return advisers require. As such, for us, multi-asset investing continues to offer a compelling investment case.

## Cazenove Multi-manager Diversity Fund performance relative to IMA Cautious managed Sector



Source: Lipper. Percentage growth total return, GBP, Net income reinvested 1 September 2005 to 30 June 2009. Past performance is not a guide to future performance.

where cash, government bonds and perhaps even gold may make interesting investment options.

Ultimately, managers who can offer a tactical approach to diversification in a flexible framework should prosper in any scenario. ●

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