Investors' Chronicle

Investing explained

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# I want to invest. What next?

*You've made the decision you're ready to start investing. How do you go about putting a portfolio together?*

One option is to use a robo-adviser and let it compile a portfolio for you.

But if you want to keep costs down and learn about markets along the way, you can put a portfolio together yourself pretty easily.

The first thing you might want to consider is how much exposure you have to different asset classes.

For someone with a long time horizon, you could consider putting all of your portfolio in equities, while keeping at least three months' worth of expenditure in cash.

But if you have a low risk tolerance, might need access to your investments in the medium term, or if you will struggle mentally with sharp swings in portfolio value, investing in assets that tend not to rise and fall at the same time can help smooth out returns.

In other words, investing in asset classes with a low or negative [correlation.]()

### Main asset classes

- Equities
- Bonds
- Alternatives:
  - Property
  - Commodities
  - Infrastructure
  - Private equity
  - Crypto
- Cash

## What's in this guide?



## More from this series



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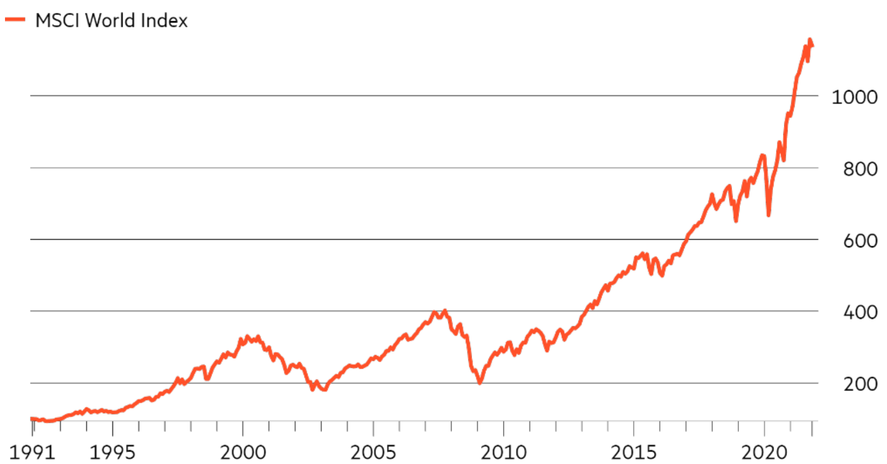
# Introduction to the main asset classes

## What are equities (shares)?

- A share is a fraction of ownership of a company. When you own a share in a Public Limited Company (PLC), you literally have a 'share' of the business.
- Shares have monetary value and are bought and sold on exchanges. When you have more people wanting to buy shares than sell, the price goes up.
- You can invest either directly in shares, or via a fund, which is a bundle of shares managed by a fund manager for a fee.
- Being a shareholder gives you certain rights and benefits; for example the right to vote on company matters at the Annual General Meeting and the potential benefit of receiving dividend payments.
- Equity market performance is measured via indices, which track a basket of shares, sometimes the entire market.
    - The S&P 500 is a popular barometer for large US companies, for example, while the FTSE 100 tracks large UK companies and the MSCI World Index tracks the global stock market.

**30-YEAR GLOBAL STOCK MARKET PERFORMANCE**

Rebased (%)




Source: Factset (performance includes dividends reinvested))



## What is fixed income (bonds)?

- Typically refers to sovereign bonds (money borrowed by countries) and corporate bonds (money borrowed by companies). The borrower pays regular payments to the bondholder.
- While the payments typically don't change over the lifetime of the bond, they are traded between investors after they've been issued, so part of the returns bond funds make is down to fluctuations in bond prices on the secondary market.
- Government bonds have been a haven when stock markets sell off, as the increase in the price of the safest government bonds has offset losses for the stock market.
- However, the correlation between equity and bond prices has increased in recent years partly owing to low interest rates. The diversification benefits of owning both may be less powerful than historically.

## Alternatives

Alternatives typically include assets that are difficult for private investors to access or buy and sell quickly – such as property, private equity, commodities and infrastructure.

However, there are funds (pooled investment vehicles) that enable you to access all of these asset classes. Investment trusts, which are listed on the London Stock Exchange, have sectors dedicated to property (via real estate investment trusts), infrastructure and private equity.

Returns linked to various commodity price movements can be accessed via exchange traded funds.

Read more about how to access alternatives in our funds guide.



# Asset class correlations

***Correlation: a statistical term describing the degree to which two variables move in coordination with each other.*** *A correlation of 1 means they move together by the same percentage. A negative correlation means that more often than not they move in opposite directions.*

The table below shows the correlation between a handful of global asset classes at the end of November 2021.

| | Global bonds | Global equities | Europe real estate | Global core infrastructure | Private equity | Bitcoin |
|---|---|---|---|---|---|---|
| Global bonds | 1.0 | | | | | |
| Global equities | 0.3 | 1.0 | | | | |
| Europe real estate | -0.2 | 0.3 | 1.0 | | | |
| Global core infrastructure | -0.1 | -0.1 | 0.0 | 1.0 | | |
| Private equity | 0.2 | 0.9 | 0.5 | 0.0 | 1.0 | |
| Bitcoin | 0.1 | 0.1 | -0.2 | 0.5 | 0.2 | 1.0 |

- Bonds and equities are mildly positively correlated, while infrastructure shows very gentle negative correlation with both equities and bonds.
- Private equity and listed equity have very high correlation
- The difficulty is, past performance is not a guide to the future.

Source: JP Morgan, December 2021

The best option for many investors getting started will be to drip money into a global equity tracker. But it is important to understand how equities sit within a wider investment universe.

Cryptocurrencies are a very new asset class, largely untested and unregulated. It is advised to only allocate money to crypto currencies that you can afford to lose.



# Putting a portfolio together

If you are investing for the first time, it is sensible to get core exposure by investing in a fund. Investing in shares is a much more hands-on approach and requires a significant amount of financial knowledge to be consistently successful.

When investing in funds, you can pick between actively managed (where an investment manager selects a pool of stocks for you) or a passive fund, which just gives you exposure to all of the holdings in a chosen index.

Passive funds are good for:

- Low costs
- broad market exposure
- Studies suggest on average passive funds perform better than active funds after fees

Active funds are good for:

- The possibility of outsize returns
- The possibility of greater owner engagement with investee companies
- Manager reports to help you learn

For many people, investing in a low-cost tracker fund will be the best option. You can choose between a straightforward index fund which is priced daily where you buy shares directly in the fund, or an exchange traded fund (ETF) – the increasingly popular option.

### Things to check

When picking an ETF, make sure you check the following things

- Fund size and set-up date (generally, the larger and more established, the better).
- Fund management fee (varies across sectors and geographies but large providers tend to be cheaper).
- Tracking error (the extent to which performance differs from the benchmark index).

If you are investing for the first time, a world index tracker – such as HSBC MSCI World UCITS ETF (HMWO) – might be a good starting point for core exposure.
Read the IC's Top 50 ETFs for more ideas.

When picking an active fund manager, you can choose between an open-ended mutual fund and a closed-ended investment trust (see funds guide for more detail).

When investing in an active fund, you need to check:

- Has the fund manager stuck to the investment process?
- Has the fund outperformed its benchmark over long timeframes?
- Is the management fee reasonable?
- How does the fund fit in the wider context of your portfolio?



If you hold too many active funds you can fall into the danger of effectively owning an expensive tracker. Experts say around 15 funds should be enough for a diversified portfolio, but if you are just getting started you may wish to buy fewer.

When picking a fund you can choose between an income share class or an accumulation share class – with the latter automatically reinvesting all dividends so you can automatically benefit from compounding interest.

For ETFs, you can choose between a 'distributing' or 'accumulating' ETF. For investment trusts, you can choose to automatically reinvest dividends via your platform.

## Picking a platform

There are dozens of platforms in the UK to pick between for investors. Here's an overview of some of the most popular for do-it-yourself investors.

IG:

- Low dealing costs of £3 for UK shares and no commission for US shares. Low exchange fee and access to a huge range of listed securities. Flat fee of £96 / year. Also permits derivatives trading. Enables you to hold foreign currencies in your account.

Hargreaves Lansdown:

- Largest DIY UK investor platform, easy-to-use website. UK share dealing fee £11.95 and foreign exchange charge 1 per cent. Custody charge 0.45 per cent for funds and capped £45 per annum of listed securities within an individual savings account.

interactive investor:

- Flat fee structure, basic plan costing £120 per year, which includes one free deal per month. Generally cost-effective for large portfolios. Same pricing structure for listed securities and mutual funds. Foreign exchange fee 1.5 per cent, can hold foreign currencies in account.

AJ Bell:

- Funds annual custody charge 0.25 per cent, capped at £42 per year for listed securities. Share dealing fee £9.95. Foreign exchange charge 1 per cent. Launching new app Dodl with no dealing fees, 0.1 per cent annual charge and a restricted product range.

Freetrade:

- Cheap option with no dealing fees. Isa customers pay annual custody fee of £36. Currently mobile only and has a limited product range of UK and US listed securities. No mutual funds.

For more information on platforms [see investors chronicle website](#)





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