A E Thomson Ltd

Independent Financial Advisers

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GUIDE TO

SETTING INVESTMENT GOALS

SECURING YOUR FINANCIAL FUTURE – SOLUTIONS TO HELP YOU MEET YOUR INVESTMENT GOALS

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Securing your financial future – solutions to help you meet your investment goals

Creating and maintaining the right investment strategy plays a vital role in securing your financial future. How much control do you want over your investments? Do you prefer to be in charge, or do you want someone to invest for you? Volatile markets can test your nerves. We can advise you on solutions to help you meet your investment goals so that you weather the markets by keeping your portfolio diverse. So what do you need to consider?

Timescale

Probably the first question you should ask in setting your investment goals is, 'What is my time horizon?' In other words, when will you need the money? Are you investing for your young child's school or university education, or for your retirement 30 years in the future? Or do you hope to achieve your goal in a shorter time frame? For example, do you want to buy a property in three years, or start your own business in five years? Your timescale for a particular financial goal will have a significant impact on the type of investments you choose to try to achieve it.

The general rule is: the longer your time horizon, the riskier (and potentially more lucrative) investments you can make. The longer the timescale, the more opportunity you have to ride out any fluctuations in your investments. On the other hand, if your timescale is very short, you may want to concentrate on investments that may offer a lower return but also greater reassurance about whether the money will be there when you need it, because a shorter time frame may not give you enough time to try to recoup any losses.

Investment risk

Another factor to consider is your individual investment risk profile. How comfortable are you with the possibility of investment loss, or seeing the value of your investment fluctuate? Some investors may forgo the possibility of a large gain if they knew there was also the possibility of a large loss (these investors are known as 'risk averse'). Other investors, or risk seekers, are more willing to take the chance of a large loss if there was also the possibility of a large gain.

It's not always easy to determine where you stand on the spectrum of risk aversion versus risk-seeking, but it's important to try to get an accurate assessment. Risk aversion isn't an either-or proposition; many investors consider themselves risk-seekers until they actually experience a loss that gets too painful. Before making any investment, you should try to get a sense of just what circumstances might cause you to sell an investment if it began to experience a loss. After all, an investing game plan only works if you're able to stick to it, and having an accurate sense of your true risk tolerance will help you develop a plan you can stay with.

Keep in mind that, as noted above, your timescale can affect your approach and attitude to risk. For example, if you're investing for retirement 30 years from now, you may be more willing to face greater risk in exchange for the potential for a higher return than if you're saving to send your child to university in four years.

Liquidity needs

Another question you should ask when setting your investment goals is, 'What are my liquidity needs?' Liquidity refers to how quickly an investment can be converted into cash (or the equivalent of cash). Property, for example, tends not to be very liquid; it can take a very long time to sell either residential or commercial property. Publicly traded stock, on the other hand, tends to be relatively liquid, though you might suffer a loss if you need to sell when the market is down. Cash and cash alternatives are extremely liquid (though even here, some types of cash alternatives may be more liquid than others).

Your liquidity needs will affect the types of investment you might choose to meet your goals. For example, if you don't have short-term liquidity needs, you can probably afford to invest in less liquid investments where the potential for gain is much higher than for more liquid investments. However, if you have two children going to college in the next couple of years, you probably don't want all of their tuition money invested in less liquid assets. Like your risk tolerance, your liquidity needs are also related to your time horizon.

When considering your liquidity needs, don't forget to think not just about your liquidity needs for a given financial goal, but your overall liquidity needs. If you have a stable income, excellent job prospects, an emergency cash reserve and no pressing financial obligations, you may have fewer concerns about liquidity than someone with a family and no emergency fund who works in an industry that's experiencing layoffs.

Investment goals

Once you've determined your financial goals and how your timescale, attitude to risk and liquidity needs affect them, it's time to think about how your investments might help you achieve those goals. When considering any investment, you'll need to think about what it offers in terms of three key investment goals:

Growth: in investing terms, growth (also known as 'capital appreciation') is an increase in the value of an investment; in other words, you can sell it for more than you paid for it. Your capital is the money you put into an investment initially.

Income: some investments make periodic payments of interest or dividends. Those payments represent investment income, which can be spent or reinvested. For retirees, income obviously is a key investment goal, but it can be important for other reasons as well. For example, income payments can help offset the impact of the ups and downs of a growth-oriented investment.

Stability: this is sometimes known as 'capital preservation' or 'protection of principal'. An investment that focuses on stability concentrates less on increasing the value of that investment and more on trying to ensure that it doesn't lose value. If you plan to spend a certain amount of money soon and want to make sure the money is there when you need it, stability might be your primary investment goal.

With each individual investment, there is a relationship between growth, income and stability. The more an investment offers in one of those areas, the more you may have to trade off in terms of the other two. The key to setting investment goals is to tailor each investment to what you want it to do for you.

You may choose to have a single investment goal for a given financial goal, as in the example of making stability a priority for short-term money. Or you may prefer to combine several investments to achieve a balance among stability, income and growth so that you maximise your overall returns at a level of risk that you're comfortable with and that suits your financial goal or goals.

Be clear about what you're investing for. Putting all your money in one type of investment can be a risky strategy. You can help reduce that risk by spreading your money across a mix of investment types and countries. Different investments are affected by different factors: economics, interest rates, politics, conflicts, even weather events. What's positive for one investment can be negative for another, meaning when one rises, another may fall.

Make time to regularly review your investments to check they're on track to meet your goals. When you start investing, or even if you are a sophisticated investor, one of the most important tools available is diversification. Whether the market is bullish or bearish, maintaining a diversified portfolio is essential to any long-term investment strategy.

Diversification allows you to spread risk among different kinds of investments (called 'asset classes') to potentially improve investment returns. This helps reduce the risk of the overall investments (referred to as a 'portfolio') under-performing or losing money.

With some careful investment planning and an understanding of how various asset classes work together, a properly diversified portfolio provides an effective tool for reducing risk and volatility without necessarily giving up returns.

If you have a lot of cash – more than six months' worth of living expenses – you might consider putting some of that excess into investments like shares and fixed interest securities, especially if you're looking to invest your money for at least five years and are unlikely to require access to your capital during that time.

If you're heavily invested in a single company's shares – perhaps your employer – start looking for ways to add diversification.

Diversifying within an asset class

There are many opportunities for diversification, even within a single kind of investment.

For example, with shares, you could spread your investments between:

- Large and small companies
- The UK and overseas markets
- Different sectors (industrial, financial, oil, etc.)

VISION, A LONG-TERM COMMITMENT AND THE HELP OF PROFESSIONAL EXPERTS

Achieving your investment goals doesn't happen by chance. It needs vision, a long-term commitment and the help of professional experts to create and execute your strategy. Investors are facing unprecedented challenges in today's global markets. Finding answers can be hard. We can help you to meet your investment challenges – please contact us for more information.

Main four asset classes

ASSET CLASS	OVERVIEW	RISK PROFILE
Cash[1]	Savings and current account balances, savings bonds, premium bonds and other NS&I products, Cash ISAs and any cash you have.	Low, but your money's buying power is eroded over time if inflation is higher than the interest rates paid. Cash you put into authorised UK banks or building societies is protected by the Financial Services Compensation Scheme up to £85,000.
Fixed Interest Securities – also called 'bonds'. Essentially a loan to a company or government for a fixed period.	Gilts (government bonds), overseas bonds, local authority bonds and corporate bonds (loans to companies).	Relatively low and returns predictable if held to maturity. However, traded prices can be volatile. Your money's buying power can still be eroded over time if inflation is higher than the interest rate paid on the bond.
Shares – also known as 'equities'. A stake in a company.	You can hold shares directly or through an investment fund where you pool your money with other people's, like with a unit trust, OEIC (open-ended investment company) or life fund.	Investing in a single company is high risk. Investing in a fund provides more diversification, but risk levels will depend on the type of shares in the fund.
Property	Includes residential or commercial property and buy-to-lets, and investments in property companies or funds.	Price can vary and be more volatile than with bonds. Potential for gains but also losses. You might not be able to access your capital quickly if you have invested into property directly. Access to capital might also be restricted through property funds if closed to redemptions, meaning you will not have access until the redemption restriction has been lifted.

[1] Cash you put into UK banks or building societies (that are authorised by the Prudential Regulation Authority) is protected by the Financial Services Compensation Scheme (FSCS). The FSCS savings protection limit is £85,000 (or £170,000 for joint accounts) per authorised firm.

TIME TO REVIEW YOUR SITUATION AND THE INVESTMENT OPTIONS AVAILABLE?

Investing is not just about what you know but also who you are. Whether a seasoned investor or just starting out, if you would like to review your situation or discuss the options available, please contact us for further information – we look forward to hearing from you.

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