Vartan Ravenscroft

Risk Investment Guide

What is this guide for?

We ask all of our clients to read this guide before they complete the Know Your Client document (KYC Application Form). Before you select your attitude to risk we wish to ensure that you fully understand what that particular level of risk means and how this will impact your investment selection. Within our KYC document are some risk related questions which will enable us to review your attitude to risk in the context of the wider information which you detail.

It is vital that we do this as your attitude to risk will impact what investments are contained within your portfolio and your potential losses or gains.

We call this process Assessing Suitability.

What does Assessing Suitability mean?

To ensure that we treat all of our clients fairly and select your investments appropriately we want to ensure that we have gathered all relevant information about you and your attitude to risk, to reach a suitable decision.

There are three stages to this process, first, KYC. KYC is an information gathering exercise. We are required to collect financial and investment information from our clients. This would involve asking such questions as, your occupation, salary, general investment and financial objectives, attitude to risk, investment restrictions, time scales for investment etc. Asking these type of questions enables us to gain a full picture about you and your circumstances and therefore make a suitable recommendation. Whilst completing the KYC you would also read this guide and answer the questions within.

The second stage of the process now takes place. We complete a Suitability Assessment document. This is an internal document that enables us to review all of the collated information and check that the level of risk selected is appropriate and reflects what we know about you and your circumstances. We therefore will look at the investment objectives, investment preferences, knowledge and experience of each client, the amount to invest and capacity for loss amongst other things.

Once the Suitability Assessment has been completed and the level of risk established, we can then make the investment selection, this is the third and final stage of this process.

The investment selection involves four key factors, the customer's objectives, financial situation, level of risk and diversification. Once we have completed the investment selection we will write to you informing you of the outcome of the suitability assessment and the initial investment selection we have made.

Risk

Investment risk can be defined as the deviation of the expected returns from an investment over time. We tend to think of risk in predominantly negative terms, as something to be avoided or a threat that we hope won't materialise. In the investment world, however, risk is inseparable from performance and, rather than being desirable or undesirable, is simply necessary. A common definition for investment risk is deviation from an expected outcome. That deviation can be positive or negative, and relates to the idea of "no pain, no gain" - to achieve higher returns in the long run you have to accept more short-term volatility. How much volatility depends on your risk tolerance - an expression of the capacity to assume volatility based on specific financial circumstances and the propensity to do so, taking into account your psychological comfort with uncertainty and the possibility of incurring large short-term losses.

With certain investments we can quantify specific types of risk. For example, with overseas investments there is currency risk because the currency in which the investment is priced may fluctuate in value against Sterling in the foreign exchange markets.

Liquidity risk is the risk that arises from the difficulty of selling an asset. An investment may sometimes need to be sold quickly and there may be an insufficient secondary market which may prevent the investment being sold or limit the proceeds that can be generated by the sale. Illiquid assets include shares in unlisted companies, unlisted hedge funds, Permanent Interest Bearing Shares (PIBS) and direct property investments.

Introducing Risk Categories

1. No risk

In general, very cautious investors prefer knowing that their capital is safe rather than seeking high returns. They are not comfortable with the thought of investing in the stockmarket and would rather have the piece of mind of their money being on deposit with for example a bank. Very low risk investors may be dependent on their capital and cannot afford to sustain a capital loss.

From a suitability perspective Vartan Ravenscroft does not provide a service for individuals who fall into this category. We would actively encourage individuals who fall into this "profile" to speak with their bank or building society about cash based deposits.

2. Cautious – lower medium risk

A cautious investor is typically looking for an element of safety in their investment strategy with the potential for modest returns over the medium to long term to help counter the effects of inflation. In exchange for this you would be willing to accept that the capital value of your investment is not guaranteed and that the value may fall over the period you are invested.

A fall in the capital may be less than a category which has increased risk such as medium risk. A cautious portfolio would typically hold a higher percentage weighting towards fixed-interest securities and this may be more than half of the portfolio's value. The income yield from these securities are generally more predictable than capital appreciation from equity markets. It is important to note though that any income generated by the portfolio as a whole is not guaranteed. To provide the potential for capital growth the remainder of the portfolio may be invested in equity markets (both domestically and overseas) and alternative assets such as commercial property and infrastructure. A cautious portfolio may have exposure to investments which we regard as being of a medium risk but it would have no direct exposure to higher risk investments.

3. Income – medium risk

Under an income approach an investor is seeking higher potential returns with an emphasis on this return coming from income. In exchange for this you would be willing to accept that the capital value of your investments is not guaranteed and that the value may fall over the period you are invested. A fall in the capital value of your portfolio may be less than a portfolio which has an increased risk category such as higher. An income portfolio would typically hold a higher weighting towards fixed-interest securities complemented by exposure towards equity markets (both domestically and overseas) and alternative assets such as commercial property and infrastructure. The emphasis on income generation may come at the expense of capital growth generated by the portfolio. If a higher income has been stipulated the impact on capital growth may be far more pronounced and this may also mean that the portfolio has a higher risk category. It is important to note though that any income generated by the portfolio as a whole is not guaranteed. An income portfolio may contain exposure to investments which we regard as being of a higher risk.

4. Balanced – medium risk

Under a balanced approach an investor is seeking higher potential returns from a combination of capital appreciation and income. In exchange for this you would be willing to accept that the capital value of your investments is not guaranteed and that the value may fall over the period you are invested. A fall in the capital value of your portfolio may be less than a portfolio which has an increased risk category such as higher medium risk. A balanced portfolio would typically hold a diversified range of assets with a higher weighting towards equity markets (both domestically and overseas). This would be complemented by exposure to fixed interest securities and alternative assets such as commercial property and infrastructure. Due to the higher weighting towards equity markets your portfolio may experience times of greater volatility in terms of its capital value. A balanced portfolio may contain exposure to investments which we regard as being of a higher risk.

5. Growth - higher medium risk

Under a growth approach an investor is seeking higher potential returns with a focus on capital growth. In exchange for this you would be willing to accept that the capital value of your investments is not guaranteed and that the value may fall over the period you are invested. A growth strategy is for investors who understand that a heightened level of risk may not necessarily translate into higher rewards. A growth portfolio would typically hold a more concentrated range of assets with the majority of exposure towards equity markets (both domestically and overseas). This may be supplemented by a low weighting towards fixed interest securities and alternative assets such as commercial property and infrastructure. Due to the high weighting towards equity markets and greater concentration your portfolio may experience more times of greater volatility which could translate into a significant fluctuation in the capital value of the investment. A growth portfolio will contain exposure to investments which we regard as being higher risk. For clients who have signed a High Net Worth Form exposure to investments which fall under this category can be obtained.

6. Growth – high Risk

Under this growth approach you would view yourself as being a High Net Worth Individual **(HNW*)** who has signed the appropriate documentation to this effect. You would be prepared to accept a high level of risk to the value of your investments if this would give you the potential for high capital growth over the medium to long term and you are willing to accept that the capital value of your investments is not guaranteed. Whereas a growth portfolio would typically hold a more concentrated range of assets with the majority of exposure towards equity markets (both domestically and overseas), your portfolio may have a bias towards smaller companies, special situations and more specialist investments permitted to be held by high net worth individuals. This may be supplemented by a low weighting towards fixed interest securities and alternative assets such as commercial property and infrastructure. Due to the high weighting towards equity markets, greater concentration and exposure to more specialist investments your portfolio may experience a greater frequency of volatility which could translate into a significant fluctuation in the capital value of the investment. For this client category we would agree with you a guideline figure of the exposure to high risk investments and this would be detailed in your client application form in the investment preferences section.

*** High Net Worth Individuals who have signed the appropriate HNW form may place themselves in earlier risk categories overall but have individual assets in their portfolios facilitated by the HNW categorisation.**

The risks of investing in different asset classes

As a continuing development prompted by changes related to MiFID II we are required to provide an explanation of the risks associated with investing in different asset classes. These asset classes could form the components of your portfolio and your Investment Manager is able to talk you through the risks associated with them to help you determine your risk category in conjunction with our investment process.

The following tables are of a "generic" nature and it should be noted that they may not cover all of the investments which may form your portfolio. Portfolios will from time to time contain an element of cash which we would look to form a "working balance" for future investment. We do not however formally view cash as an investment and it is therefore not detailed in these tables. We would view cash as low risk if it is being held on a short to medium term basis.

These are bonds issued by companies to raise money for business

Direct asset class	Investment description	General risk profile of asset class/historic volatility	Returns are generated from
Fixed Interest	Fixed interest, or bond investments generally pay a set rate of interest over a defined period of time and then upon maturity return the face value. Bonds have the potential to provide a more predictable overall return than shares as the return is fixed. However, with the exception of index linked bonds they provide little protection against inflation. The return from a conventional bond is dependent upon the rate of interest paid and the purchase price of that bond.		
(i) UK Government Bonds & Supranational Bonds	UK Government Bonds are issued by the UK Government and are sometimes referred to as Gilts. They are perceived to have a lower medium risk profile and high credit rating as the UK government can raise tax or print money to fulfil its commitments. Supranational Bonds refers to bonds issued by an international organisation or quasi-government organisations such as the European Investment Bank and World Bank. As they are backed by multiple countries they enjoy a high credit rating and a lower medium risk profile.	Lower medium risk Historically lower levels of volatility	Income
(ii) Corporate Bonds (Investment Grade)	These are bonds issued by companies to raise money for business purposes. They usually pay higher rates of interest than government bonds because they tend to be riskier reflecting the fact that the underlying company could go out of business and default on payment. We typically look to invest in "investment grade" corporate bonds which generally have an overall higher credit rating depending on valuation.	Lower medium risk Historically lower levels of volatility	Income
(iii) High Yield & Emerging Market Debt	High Yield Bonds are issued by lower quality corporates and therefore have higher yields to compensate for the additional risk that the company defaults. Also, this encompasses Emerging Market Bonds issued by governments and companies in developing markets such as Latin America, the Middle East and Asia (excluding Japan). Emerging Market Bonds offer more attractive yields but these reflect additional risks such as political instability and currency volatility.	Generally medium risk depending on the issuer Historically higher levels of volatility	Primarily income & potential for some capital growth
(iv) Inflation Linked Bonds	These are bonds which have their interest rate adjusted on a regular basis to reflect changes in the rate of inflation. They are primarily issued by governments but can also be issued by corporates. In a deflationary environment the inflation adjusted principle could decline below its par value.	Lower medium risk Historically lower levels of volatility	Capital growth and income
Equities	Shares (also known as equities) represent the part ownership of a listed company. Equities are a real asset and offer protection against moderate inflation. Long term returns can come in the form of dividends and capital growth which are not fixed and are not guaranteed. As compensation for this, returns can be typically higher. However, the downside is that as part owner of a company your original capital is at risk should things not go according to plan. Equities when held on an individual basis are volatile and sensitive to a wide range of unpredictable factors such as changes in economic sentiment, political shocks and company specific issues. By holding a diverse range of companies either directly or through a collective this risk can be balanced but not eliminated.		

Direct asset class	Investment description	General risk profile of asset class/historic volatility	Returns are generated from
(i) UK	Fully listed UK companies are subject to high levels of corporate governance and accounting standards. The UK stock market contains a wide range of companies ranging from internationally focused Blue Chip Companies found in the FTSE-100 index to more domestically focused names in the FTSE-250 index. Outside of these indices are a diverse range of smaller companies which are fully listed. The less regulated AIM market (Alternative Investment Market) also contains an extensive range of firms. The risk profile of UK equities can vary enormously across the sizes of companies however, the size of a business is no guarantee over its viability. There have been many instances of FTSE-100 companies which have fallen from grace leaving little or no value for shareholders. Larger UK companies tend to have good liquidity which is the degree to how quickly an asset can be bought or sold without impacting its price.	Medium risk for FTSE 100 and FTSE 250 indexes as a whole Historically higher levels of volatility Usually for a higher risk for the majority of UK smaller companies and AIM If held via a "Collective" is of a higher medium to higher risk depending on the level of diversification Historically higher levels of volatility	Capital growth and income
(ii) Global developed markets	Overseas developed markets benefit from good levels of corporate governance and internationally recognised accounting standards. These markets are typically highly regulated. However sterling based investors are exposed to currency movements which can impact returns and are of course exposed to the same company specific risk as investing in UK shares. Overseas developed markets generally benefit from good liquidity when focusing on the larger names and provide diversification.	Medium risk for large capitalisation companies Historically higher levels of volatility	Capital growth and income
(iii) Emerging markets	Emerging markets have fast-growing economies and may be going through the process of industrialisation or urbanisation. They are often characterised by high levels of economic growth. Although they offer investors the higher potential for returns this comes with increased risk. Risk can come in the form of poor corporate governance, low regulation, poor liquidity, political instability and currency volatility.	Usually of a higher risk Historically higher levels of volatility	Capital growth and income
(iv) Sector specialist	Sector specialist covers investment in equities derived from one economic sector such as commodities, financials, technology, healthcare, biotechnology. We would typically use an Investment Trust to gain exposure to these specialist areas to benefit from diversification and the specialist skills of an external asset manager. As exposure is to only one sector risks are considerably increased. This risk can be increased if the Investment Trust "gears" its portfolio by borrowing money.	Medium to higher risk depending on the sector and level of diversification Historically higher levels of volatility	Capital growth and income

Direct asset class	Investment description	General risk profile of asset class/historic volatility	Returns are generated from
Commercial property	We only invest into commercial property via stock exchange Listed REITs (Real Estate Investment Trusts) and conventional Investments Trusts, or for high net worth clients looking for specialist exposure, their overseas equivalent. These are referred to as being closed-ended property funds. We do not invest in open ended funds such as a Unit Trust as we feel that these are not the best way to access this asset class as they tend to suffer from poor levels of underlying liquidity. Commercial property can act as a diversifier and has been less correlated with the performance of equity markets. Commercial Property can represent investment into offices, retail premises, industrial units and residential property. A higher return is generally offered to investors as the risks of investing in commercial property are higher than that offered by fixed interest securities. Commercial property is more economically sensitive and leverage (through borrowing) can increase this risk. Closed-ended property funds can trade at a discount or premium to their net asset value which can effect investment returns. The income generated by property funds is not guaranteed but can offer protection against inflation. Conventional Investment Trusts that invest in property typically do so via investing in the shares of listed property companies and as such can be more linked to the performance of equity markets.	Medium risk for UK REITs and London listed investment trusts Historically lower levels of volatility Higher risk for overseas "specialist vehicles" Historically higher levels of volatility	Primarily income and the possibility of some capital growth
Alternatives	These are formed from investments outside of the traditional asset classes of equities, bonds and cash. We may use alternative investments such as infrastructure and private equity in a portfolio. This can also include investments for which clients have signed High Net Worth		
(i) Infrastructure	Infrastructure investment involves investing in investment vehicles which have paid for the right to construct and manage long term infrastructure projects such as hospitals and roads. We only invest in closed-ended infrastructure companies. In many countries it has become more challenging for public authorities to meet funding requirements from traditional sources, such as banks, with private capital helping to bridge the gap. Investors in the sector receive an income stream which can be inflation linked and ultimately backed by public authorities. The income yield on offer is typically higher than the one derived from investment grade corporate bonds, reflecting volatility in the political environment and the risks with the underlying projects. It also reflects the fact that the income stream is not guaranteed. Closed-ended infrastructure companies can trade at a discount or premium to their net asset value which can affect investment returns. Infrastructure companies tend to be less correlated to the performance of equity markets. Closed-ended infrastructure companies can borrow money which has the potential to increase risk.	Medium risk Historically lower levels of volatility	Primarily income and the potential for some capital growth
(ii) Private equity	Private equity involves investing in private companies i.e. those whose shares are not quoted on a public exchange. The managers of private equity companies often use high levels of debt to enhance returns and the private equity firm can be directly involved in running those investee companies. The returns on offer from this sector are likely to be higher than those from listed equities, reflecting the complexity and highly illiquid nature of private equity.	Medium to higher risk depending on level of diversification Historically higher levels of volatility	Capital growth (although this may also come via income returns)

Notes

Disclaimer

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