Church House Investment Management

The Ten Principles of Successful Investing

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A tried-and-tested framework

With today's ever-changing market conditions, knowing how and where to invest your money can feel overwhelming. Coupled with an endless supply of investment advice online, investing can seem complex.

However, once we cut through the noise, we find that the same tried-and-tested principles apply when it comes to making good investment decisions. Whether you're a seasoned investor or a novice, the ten principles we outline in this guide will provide you with a solid overview and a reminder of what it means to invest successfully.

Committing to a principled, repeatable investing plan can put you on the path to building wealth. Investors who plan for the future and stay true to their principles are more likely to take the steps necessary to achieve their financial goals.

Inflation is a silent killer

Inflation refers to a decrease in your money's purchasing power over time. When the costs of goods and services rise, your investment returns become diluted.

This is particularly topical at the moment, given that the Consumer Prices Index (CPI) rose by 9% in the 12 months to April 2022[1] – the highest CPI 12-month inflation rate since the National Statistic series began in January 1997. For cash savers, the problem is exacerbated when inflation rates exceed interest rates on cash savings, meaning the real value of your money is falling.

The reason that inflation is a silent killer is that it can leave you with a false sense of understanding about how much money you'll need in the future.

For example, you might have a planned expenditure in 10 years – let's say for a world cruise. The cost for that today is £15,000, and you have £10,000 to invest. So you calculate that in order to achieve this, you'll need an annual return of approximately 4.2% per annum. This does not take into account any associated charges.

Unfortunately, this ignores the likelihood of the same cruise being more expensive in 10 years' time. Therefore, for the plan to be realistic, you need to account for inflation in your projections and arrive at a required 'real return' for your investment, i.e.– a figure that has been adjusted for inflation.

It's easy to overlook inflation from year to year. However, over time, the compounding effect will catch up with you, making your money even less valuable.

[1]https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/april2022

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Compound interest – the eighth wonder of the world

Compound interest enables money to grow exponentially over time. As such, it can turn small investments into large returns and unpaid bills into large debts. It is often quoted as: “The eighth wonder of the world. Those who understand it, earn it; those who don’t, pay it”.

If you’re making an investment, compound interest will increase the amount your money grows by every year. This is because every year, there will be a larger sum of money on which to earn returns.

For example, if an investment of £10,000 is made, and the return is 5% a year, the growth in year one is £500. The 5% growth in the second year is then on a sum of £10,500, equating to £525, leaving a total of £11,025. And the cycle continues.

Because of the way that compound interest ‘snowballs’, an investment can yield impressive returns if the money is left for long enough. The longer the money is invested, the more interest it will generate. Prospective investors can divide 72 by an anticipated annual return for a rough estimate of how long it will take to double their money. For example, an annual return of 7% would be just over 10-years.

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It's all about effective risk management

The value of investments can fall as well as rise, so it's important to know how comfortable you are taking risks. An investor's risk tolerance is usually determined by the following three factors:

- **Risk capacity** – How much you can afford to lose without it affecting your financial security.
- **Need** – How much your investments need to earn for you to achieve your financial goals.
- **Emotions** – To what extent do your emotions impact your investment decisions?

A successful investor will choose investments that are aligned with their risk tolerance. In turn, this increases the chance that both their investment returns and the volatility of their portfolio will be in line with their expectations. With this approach, investors are more likely to stay invested for a longer period.

Investing consistently, rather than looking for quick returns, can also reduce your risk over the long term. Playing the long game, so to speak, can help keep your emotions out of your investments. This strategy is based on the general assumption that markets rise over time.

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All that glitters is not gold

In recent years, internet and social media advertising have seen an increase in companies and individuals promoting investments that claim to be easy money. However, it's important to remember that if an investment looks too good to be true, it probably is.

These types of investments are usually based on rising market prices rather than basic fundamentals and tend to encourage herding behaviour. This type of investing is what leads to market bubbles, where the price of a financial asset exceeds its value by a large margin.

A recent example of this is cryptocurrencies such as Bitcoin. Constant marketing and word-of-mouth recommendations have created an increase in demand despite many investors not fully understanding how they work. They are highly volatile and subject to market crashes. And because the future of digital currencies remains uncertain, they're considered a risky investment.

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A little knowledge can be dangerous

According to recent research from Business Insider[2], "half of millennials go to a friend, family member, or partner for money advice" – regardless of how much they earn. While this can be useful in some contexts, when it comes to investing, no one knows your personal finances like you do.

Investment tips from friends and family should be treated with caution. Just because an investment has paid off for one person doesn't mean it will pay off for you. Money matters are very personal, and investment tips can often do more harm than good.

When it comes to investing, one size doesn't fit all. Your friends and family are probably unaware of your exact financial situation, and they're unlikely to be qualified investment professionals. How many have taken the time to assess your risk profile before offering you free advice? As such, your investment decisions should be based on your own personal finances, tolerance for risk, values, and goals.

[2]https://www.businessinsider.com/half-of-millennials-ask-friends-family-for-money-advice-2020-9?r=US&IR=T

Maximise opportunities for tax-free returns

Tax can eat into your investment returns, so finding opportunities to minimise its impact is a key strategy. Perhaps the best known investment method to minimise tax is Individual Savings Accounts, or ISAs. With an ISA, you can deposit up to £20,000 a year without paying tax on the investment's return[3]. Since the original ISA was introduced, the Government now offers several types of ISAs, including Cash ISAs, Stocks and Shares ISAs, Lifetime ISAs and Innovative Finance ISAs (IFISAs).

Private pensions also offer tax-free returns while your money is invested. In addition, you can receive tax relief[4] on contributions up to the annual allowance of £40,000, or 100% of your income if lower. In some cases, it's also possible to carry over any annual allowance you didn't use from the previous three tax years[5].

[3]https://www.gov.uk/individual-savings-accounts
[4]https://www.gov.uk/tax-on-your-private-pension/annual-allowance
[5]https://www.gov.uk/guidance/check-if-you-have-unused-annual-allowances-on-your-pension-savings

Diversification is key

Placing all your investments in only one type of asset is a higher risk strategy than diversifying your investments across a variety of assets. Diversification aims to maximise your returns by investing in areas that react differently to the same event. For example, a diversified portfolio might include investments in different asset classes, such as bonds, shares and property.

Similarly, diversifying across different sectors and industries can help reduce your risk exposure, as a downturn in one market won't necessarily impact another. An event that takes place in one country may not impact others so spreading your investments across different countries can also reduce risk. It is also beneficial to diversify your investments in several companies, rather than in just one. If one company goes bust, the performance of the others will help mitigate your risk exposure.

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Time in the market, not market timing

To secure an immediate return, it can be tempting to try and invest when the market is falling. However, research suggests that those who stay invested over the long term will generally see better returns.

'Market timing' refers to buying a security at a low price in the hope of selling it a higher price shortly after. By contrast 'time in the market' is based on the strategy that the fundamentals are more important than the timing.

As legendary investor Warren Buffett has explained, we humans are by nature irrational, so can find ourselves being tempted to sell when we think the market is acting against us. He has been quoted in saying "The most important quality for an investor is temperament, not intellect[6]" with the message being market fluctuations are normal and patience pays off.

[6]https://www.sarwa.co/blog/warren-buffett-quotes

Keep things liquid

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Liquidity is defined as the ease with which an investment can be bought or sold. Investments that can be sold easily are referred to as ‘liquid’ while those that are difficult to sell are ‘illiquid’.

It is essential for investors to have liquid investments in order to have access to cash. During times of market turmoil, some investments can become subject to restrictions, which can impact your access to cash and investments.

It is important to make liquid investments part of your overall portfolio to ensure you’re prepared for changes in circumstance. With near-immediate access to capital, you won’t need to take on extra debt if disaster strikes.

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Make sure you are protected

In the UK, regulated investments are controlled by the Financial Conduct Authority (FCA) and covered by the Financial Services Compensation Scheme (FSCS). If something goes wrong with your investment, such as a provider going into liquidation, you may be compensated by the FSCS.

Regulation is in place to protect consumer interests. However, not all investment providers are subject to regulation, and it can take various forms. Unregulated investments are not covered by the rules of the FCA, and thus carry a higher risk of loss of capital.

Unregulated investments are on the rise in the UK and, unfortunately, many are outright scams. It is therefore important to be extra vigilant when investing in any opportunities advertised as low-risk. Successful investors are able to look beyond the glossy brochures and see claims of high returns (with today's low interest rates) as potentially risky investments.

Important Information

The contents of this document are for information purposes only and do not constitute advice or a personal recommendation. Investors are advised to seek professional advice before entering into any investment decisions.

At Church House Investment Management, we only make recommendations from our range of investment portfolio services and associated accounts. Full details of the nature of our services can be found at www.ch-investments.co.uk/important-information or can be provided on request.

Please also note the value of investments and the income you get from them may fall as well as rise, and there is no certainty that you will get back the amount of your original investment. You should also be aware that past performance may not be a reliable guide to future performance.

Church House Investment Management is a trading name of Church House Investments Limited, which is authorised and regulated by the Financial Conduct Authority.

About Church House Investment Management

Church House is a private limited company, majority-owned by its directors. We provide investment advice and management to individuals, families, trusts and charities.

Established in 1999, our company now manages approximately £1.5 billion of assets, employing around 30 people at work across our offices in London and Dorset.

We offer a choice of investment portfolio services, the 'building blocks' of which are our range of investment funds, and, in some cases, other securities. Our investment philosophy is that successful investing is about effective risk management, and so the focus begins with the preservation of capital.

Find out more about how Church House can manage your investments. Call us on **01935 382620**, or email **enquiries@church-house.co.uk.**

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