



A Guide To Portfolio Construction: Balancing Risks and Rewards

Statistics Last Updated January 2010

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Balancing Risks and Rewards

This guide is intended to provide an overview of the wide range of investment portfolios that we can construct for our clients.

In order to provide an indication of how these various portfolios may perform over the longer term, we have chosen to show the average yearly returns that have been produced since the mid-80s. And, since clients will no doubts want to have a better idea of the risks that are associated with their investments, we have also shown the highest level of profit and loss that was seen in any one year during the same period.

It is our hope that these figures will allow you to hold a more informed discussion with us in regards the type of investment portfolio that best suits your needs.

However, it is important to note that these figures stretch back to the mid-80's when the returns on most asset classes were exaggerated as a result of inflation, and where 'real' returns would have appeared lower were inflation accounted for.

To this end, in the current low-inflation environment, we would suggest that it is unlikely that similar annualised returns will be produced going forward.

We should also add that, as prices in the financial markets move so rapidly, it would be imprudent of us to offer more specific opinions about the current state of the markets within such a generic document.

However, it would be fair to say that at the current time we are hoping for expected returns to be within the following territory over the longer-term (say 5-10 years):

Instant Access Cash deposits	3.0%
Index Linked Government Bonds	4.5%
UK Government bonds	5.0%
Investment-Grade Company Bonds	6.5%
Non Investment-Grade Company bonds	7.5%
Commercial Property	8.0%
UK, European & US Shares	10.0%
Emerging Market Shares	15.0%

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No-Risk Portfolio:

The only way to guarantee that your capital remains entirely safe is to keep your money invested in cash.

However, please bear in mind that, whilst this approach might keep your capital safe, consideration must be given to the erosive effects of inflation.



Cash 100%

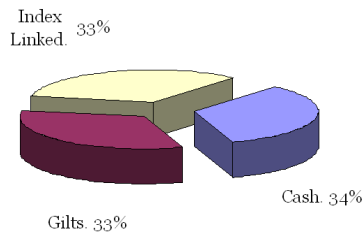
Asset	Average	Best	Worst
Cash	4.28%	6.23%	1.71%

Very Low-Risk Portfolio:

Whilst one can't guarantee that government bonds won't fall in value, the British Government has always honoured its commitment to repay money that it has been loaned.

To this end, since the rate of return offered through government bonds is slightly higher than cash, one can consider a government bond to be one-step up the risk ladder, and a great way to provide a little extra income without taking undue risks.

Here National Savings products also fit the bill nicely.



Asset	Average	Best	Worst
Cash	4.28%	6.23%	1.71%
Govt Bond	9.73%	34.18%	-12.06%

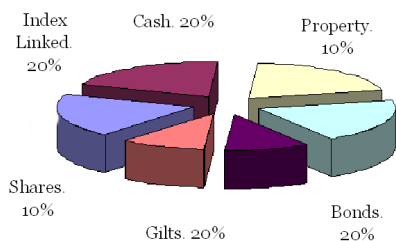
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Low Risk Portfolio:

As an alternative to lending the government money through the purchase of their bonds, it is also possible to lend money to companies in much the same way.

Suffice to say that company bonds are similar in nature, but could be considered more risky.

You might now also consider adding an element of 'commercial property' to your portfolio, as the income yields on this type of investment have been sound for some years.



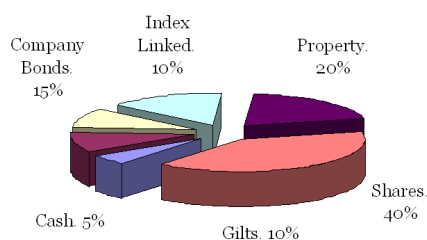
Asset	Average	Best	Worst
Cash	4.28%	6.23%	1.71%
Govt Bond	9.73%	34.18%	-12.06%
Co Bonds	9.52%	34.25%	-11.08%
Property	9.76%	30.00%	-26.30%
UK Shares	10.93%	59.45%	-20.51%

Balanced Portfolio:

The client that wishes to produce a slightly higher overall return might opt to increase share holdings to around 40%.

However, if you are still looking to take an income then it might be prudent to keep some property holdings, as this asset class tends to produce a mix of capital gains and income over the longer term.

And to further underpin your income requirements we would suggest that you consider keeping around 40-50% of your money in lower-risk bonds

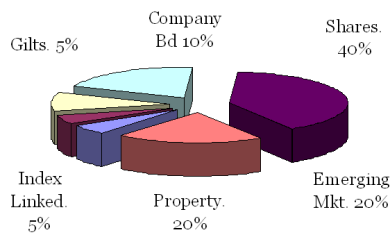


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Aggressive Portfolio:

If you are looking to produce a higher level of growth, and you are prepared to see the value of your capital fluctuate, then you might opt to hold a slightly higher percentage of shares and property in the hope that returns are boosted over the longer term.



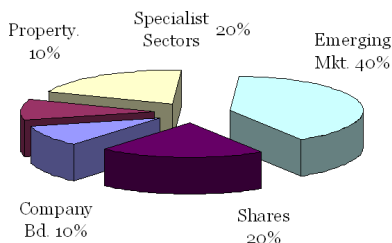
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Emerging Mkt	8.31%	64.42%	-48.71%

Speculative Portfolio:

For the more aggressive investor who is attempting to produce above average returns, shares tend to form a larger component of the portfolio.

The risks to your capital are clearly increased; however holding foreign shares can help to mitigate risks by improving diversification.

We would suggest that portfolios holding a larger percentage of shares are managed more closely.



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Property	9.76%	30.00%	-26.30%
UK Shares	10.93%	59.45%	-20.51%
Euro Share	5.34%	33.09%	-47.48%
US Shares	7.48%	33.65%	-39.24%
Emerging Mkt	8.31%	64.42%	-48.71%

Source of statistical information:

Short-term cash returns are calculated from the LIBID 7-day notice rate. In all instances the 'real' return has been indicated. We have used the 'real' return as we feel that this better reflects the day to day life – in other words returns have been adjusted to remove the effects of high inflation, which would otherwise distort the figures and imply an unreasonably high return on cash during the 80's.

Government bonds returns are taken from the FTA Actuaries British Government Securities All Stock index. Here nominal returns (i.e. they have not been adjusted for inflation) have been provided, as we feel that this better reflects the actual gains and losses that would have been made by holding bonds. Figures date back to 1985.

Corporate bonds returns are taken from UBS Warburg & IBOXX 10-year indexes for AA rated bonds. AA rated bonds have been chosen as we typically use higher-grade issues. Lower grade bonds can of course be used and we will highlight this when a substantial percentage of the bonds recommended have a 'non-investment grade. Nominal returns (i.e. not adjusted for inflation) have been used and go back to 1990.

Property returns are provided by the Jones Lang LaSalle index, which values returns net of expenses and also shows the re-investment of rental income. Suffice to say that due to the volumes of cash involved, one can consider the index to reflect returns on the commercial property market as opposed to the private houses. Nominal returns (i.e. not adjusted for inflation). Here the figures go back to 1985.

The UK Ordinary Share returns that are indicated include net dividend yields as received from pension funds. Nominal returns (i.e. not adjusted for inflation) have been provided. Again the figures used go back to Sept 1984.

We have decided to use the MSCI Euro Index for our European Share figures. Figures go back to 1997. It is worth noting that due to the shorter time scale, the average returns have been significantly reduced by recent events.

US Share returns are based on the MSCI North American Standard Core Index since 1980 and reflect actual returns.

Emerging Market returns are based on the MSCI index of the same name back to 1987. This is designed to measure equity market performance in the global emerging markets. As of July 2007 the index consisted of the following 25 emerging market country indices.

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