

# Keep your options open to cash in on opportunities

**I**nvestment based on genuine long-term expectations is so difficult today as to be scarcely practicable". The wisdom of John Maynard Keynes is as relevant today as when it was uttered 80 years ago.

The US stock market has risen more than threefold in the past six years.

In the usually staid bond markets the Swiss managed to sell 10-year debt at a negative yield recently and Mexico issued a 100-year euro-denominated sovereign bond. Ireland sold 30-year debt in March at a yield of just 2%. In China the Shenzhen stock index more than doubled in value in 2015, with trading in May a multiple of that on the New York stock exchange.

Almost all asset prices across the globe have enjoyed a strong recovery from the lows reached in 2009. The "zest in making money quickly", as Keynes coined it, is alive and well.

Yet this is an uneasy time for those with an eye on fundamentals. With stock markets not cheap and bond markets at levels which require heroic assumptions to deliver a return, how should investors allocate their investments?

The investment legend Seth Klarman asks a rather interesting question: has the market tripled because things are better, or do things feel better because markets have tripled? Klarman wondered how everything would feel if the S&P 500 were suddenly cut by one-third or one-half? Would such a drop drive astonishing bargains, or would the festering problems such as unemployment, the federal, state and local deficits, the long-term fiscal situation, and the creditworthiness of most sovereigns suddenly seem ominous?

A recent survey from Schroders revealed more than

## GARY CONNOLLY COMMENT



half of investors globally say they are more confident about investment opportunities over the coming 12 months, with 91% expecting growth. The average investor anticipates returns of about 12% from their portfolio. Yes, 12%!

Notwithstanding such ambitious expectation, the average retail investor

the concern of any successful long-term investor. I'm more interested in the thought process that sees calm and complacency in a market at one price – usually a high one – followed by fear and caution at another – historically shown to be a low price.

My advice is to stay diversified and don't view cash with a jaundiced eye. To investors, cashing in a portfolio, earning next to zero, looks like a manager has run out of ideas.

At a recent investment lunch, a fund manager was asked about the level of cash in his fund, which was close to 50%. He replied: "I'd rather lose 50% of my clients, than lose 50% of my clients' money."

In truth, cash provides ballast and options in the event of a market decline.

It was Keynes who popularised the concept of the greater fool theory of investing: there will always be a "greater fool" to buy securities, even if you buy them when they are already overpriced.

In the short term, he who does not believe in the greater fool theory is the greatest fool. In the long term, I suspect fundamentals will reassert, providing our fund manager friend holding 50% cash with some buying opportunities.

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is looking to place only 21% of their portfolio in high risk/high return assets such as equities.

And to top it off, less than one in four investors will seek professional financial advice to change their investment strategy.

If this is an accurate view of investor expectations and behaviour, I'm concerned. Returning confidence is to be celebrated. Naïvety is not.

Klarman is clearly concerned about a market decline given the extent of this decade's rally. Knowing the "when" would be a great advantage and is far more difficult to predict than the "if". Market timing is not