M&G Investments

The M&G guide to

Multi-asset investing

Contents

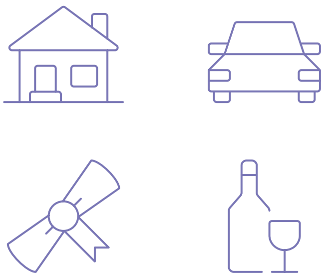
What are assets? 3
The case for diversification 5
Diversifying your investments 6
What are multi-asset funds? 7
Are all multi-asset funds the same? 8
The advantages and disadvantages of multi-asset funds 9
Glossary 10
The M&G guides 11

Please refer to the glossary found on page 10 for an explanation of the words highlighted in **bold** throughout this guide.

What are assets?

An **asset** can be anything that has value – from bonds to buildings and even bottles of wine. When an asset can be traded, it can be owned as an investment.

There are many different types of investment assets, each with their own qualities and characteristics. Two of the most common are bonds and equities.



Bonds

When you buy a bond, you are basically loaning money to a government or company. This loan lasts for a set period of time and you'll receive regular interest payments (known as **coupons**), as well as the original value of the loan when the bond finishes (or matures). The interest payments are usually for a fixed amount, which is why bonds are also called fixed income investments.

If you're investing in bonds, the main risk to keep in mind is the possibility that the borrower might fail to keep up with their interest payments – or, in rare cases, default completely, so you might not get anything back. This means that the level of safety, or risk, in a bond largely depends on who the borrower is. For example, German government bonds are seen as lower risk than Argentinian government bonds, because Germany has a stronger economy and a better record of repaying its debts.

Bonds can also be bought or sold before they mature. If you do this, the level of income you receive (known as the **yield**), will depend on the amount of interest you get and the price you pay or receive.

The value of your investments can go down as well as up so you might not get back the amount you put in. When you take money out, this will reduce the value of your investment.

Equities

When you buy a share of equity, you become a part-owner of a company. This means you share in its successes or failures and may receive a portion of its profits in the form of **dividends**.

'Listed' companies have shares that are bought and sold on a stock exchange. A company's share price can go up or down, depending on how much demand there is for its shares.

For example, if the company's performance exceeds expectations, demand is likely to grow and the share price will increase. Equity investments can rise and fall in value quite dramatically, depending on company performance and perceptions of future prospects as well as on the general economic conditions and on actions taken by policymakers such as central banks.

The value of your investments can go down as well as up so you might not get back the amount you put in.

- An asset can be anything that has value
- Bonds are basically loans taken out by governments and companies
- When you buy an equity share you become a part owner of a company

The case for diversification

All investments involve a degree of **risk**. In exchange for potentially higher returns, you must accept a greater level of risk (or, in other words, a higher chance of losing some or even all of your initial investment).

However, investment risks can potentially be managed by spreading money across a range of assets. This is known as **diversification** and it aims to limit the impact of any individual failures. It can also reduce the volatility of an investment portfolio, as one asset may rise in certain market conditions when another may fall.

Diversification is possible because asset classes have different risk and return profiles, so they can perform differently in different economic situations. Effective diversification involves picking the right blend of assets to actively manage the ups and downs of the markets.

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Key words

If two assets tend to perform similarly across a range of economic conditions, they are said to be 'correlated'. On the other hand, if their performance is very different throughout these conditions, they are 'uncorrelated'.

Diversifying your investments

You can, of course, build your own diversified portfolio by picking a collection of uncorrelated assets. However, many people find that they don't have the resources to achieve effective diversification or manage a portfolio in a cost-effective way. They may also lack the time or expertise to choose a combination of assets that suits their attitude towards risk and return.

- A pre-existing investment fund will pool your money with many other people
- A 'multi-manager' fund contains a combination of different investment funds

One alternative is to use a pre-existing investment fund – which will pool your money with many other people – as this can allow you to hold many more investments than you might be able to buy on your own. You also get access to economies of scale and professional expertise.

For even more diversification, you could look at a 'multi-manager' fund, otherwise known as a fund-of-funds. This will contain a combination of different investment funds, each of which holds assets directly and is run by a fund manager. This means your returns don't rely on the skill of a single fund manager and risk is spread across many investments.

However, the fund-of-funds approach can mean you end up paying two layers of manager fees. As well as fees directly charged by the manager of the fund-of-funds, investors may indirectly shoulder the charges levied on the underlying funds by their respective managers. Investors need to be sure that they're getting the extra performance potential to justify the higher cost where this approach proves more expensive. It might also be harder to work out exactly where your money is invested, given the number of fund managers and companies involved.

Alternatively, there is an option that has become increasingly popular in recent years – an all-in-one product known as a multi-asset fund.

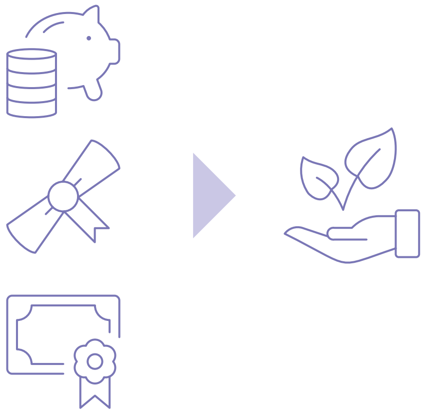
What are multi-asset funds?

When you choose a multi-asset fund, you get a diversified blend of assets in a single investment.

The mix of holdings can typically include equities, bonds and cash, but the key point is that the allocation to each asset isn't necessarily fixed. Instead, some multi-asset funds have the flexibility to respond to changing market conditions.

For actively managed, flexible multi-asset funds, the managers can adjust the blend of assets, increasing or reducing the fund's exposure to certain markets and sectors, with the aim of benefiting from opportunities or managing particular risks.

As a result, multi-asset funds broadly aim to provide investors with less volatile returns in the 'good' times and to reduce the impact of losses during downturns. The goal is to offer lower risks than a pure equity fund, while having greater growth prospects than a pure bond fund.



Are all multi-asset funds the same?

Multi-asset funds are not all the same. They each have different investment goals and approaches to risk. Some focus on achieving an income for their investors, so they may invest more in bonds. Others will be more focused on achieving long-term growth, which normally means they'll have a greater weighting towards equities.

Many multi-asset funds choose to add more diversification by investing in what we call 'alternative assets', which are typically uncorrelated with equities and bonds. This may reduce the fund's overall volatility, even if the individual assets have very variable returns.

Some common types of alternative investments that are held within some multi-asset funds include:

Commodities

Basic goods, such as oil and iron, often used in industrial processes

Currencies

Globally traded cash from different countries

Derivatives

Financial 'contracts' whose price is derived from an underlying asset, such as a commodity or currency

Hedge funds

Unrestricted investment portfolios that are typically used to seek to maximise returns for investors

Private equity

Company investments that are not publicly traded

Property

Commercial premises that seek to offer rental income and capital growth from the value of the property increasing over time

The advantages and disadvantages of multi-asset funds

On the upside

Accessibility

You need much less money to create a diversified portfolio with a multi-asset fund than you do to put together your own diversified fund portfolio or to build a portfolio by investing directly in assets.

Convenience

Multi-asset funds give you an 'off-the-shelf' way to get professional diversification.

Economies of scale

With a multi-asset fund, investment costs can be spread across large numbers of investors, so everyone may pay less.

Flexibility

Active, multi-asset managers have the flexibility to adjust the blend of assets in their portfolio, so they can respond to, or anticipate, changing market conditions.

On the downside

Benchmarking

Multi-asset funds often target a specific rate of return, rather than aiming to outperform a specific benchmark index. This can make it much harder to compare their performance.

Suitability

Each multi-asset fund has different aims and objectives, based on its underlying investments. Some target higher returns in exchange for higher risk. Before you invest, you need to check what is 'under the bonnet' to help make sure a fund matches your attitude towards risk and return.

The value of your investments can go down as well as up so you might not get back the amount you put in. □

Glossary of investment terms

The following are explanations of some of the terms you would have come across in this guide.

Asset Anything having commercial or exchange value that is owned by a business, institution or individual.

Bond A loan in the form of a security, usually issued by a government or company, which normally pays a fixed rate of interest over a given time period, at the end of which the initial amount borrowed is repaid.

Coupon The interest paid by the government or company that has raised a loan by selling bonds.

Derivatives Financial instruments whose value, and price, are dependent on one or more underlying assets. Derivatives can be used to gain exposure to, or to help protect against, expected changes in the value of the underlying investments. Derivatives may be traded on a regulated exchange or traded over the counter.

Diversification The practice of investing in a variety of assets. This is a risk management technique where, in a well-diversified portfolio, any loss from an individual holding should be offset by gains in other holdings, thereby lessening the impact on the overall portfolio.

Dividend Dividends represent a share in the profits of a company and are paid out to the company's shareholders at set times of the year.

Risk The chance that an investment's return will be different to what is expected. Risk includes the possibility of losing some or all of the original investment.

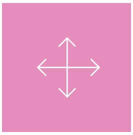
Yield This refers to either the interest received from a fixed income security or to the dividends received from a share. It is usually expressed as a percentage based on the investment's costs, its current market value or its face value. Dividends represent a share in the profits of a company and are paid out to the company's shareholders at set times of the year.

The M&G guides

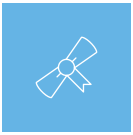
The M&G guides aim to give you the basics about investing, to help you make informed decisions about your financial goals and how to reach them.

We're unable to give financial advice. If you're unsure about the suitability of your investment, speak to a financial adviser. The views expressed in this document should not be taken as a recommendation, advice or forecast.

This brochure is part of our range of M&G guides:



Investing



Bonds

Equities

Risk

Multi-asset investing

Income

M&G Investments

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