Personal Investment Portfolio

Introduction

It is not surprising to see young men spend their money arbitrary because they perceive a long future hence no need to plan for life after retirement. Conversely, old workers about to retire are mindful about their 'sunset' years hence the need to plan accordingly. Thus, a carefully managed personal investment portfolio is requisite to ensure financial assets are well put into use. Having been rewarded with severance pay, retirement benefits, and other statutory funds, retirees would like to know the best way to make use this cash in the presence of economic risks associated with market volatility. This calls for a personal investment portfolio that is well managed. Kayapoor (2014) underscores the essence of portfolio management by stating that portfolio management involves inputs such as the financial capital and critical analysis of financial and economic effects such as risks associated, return on investments, and inflation before deciding on which investment to undertake. A critical analysis pertaining personal investment portfolio is created herein based on short and long-term perceptions. In addition to that, scenarios of financial crisis such as the 2007-2008 cash crunch are considered as a way to guide in decision making on risk(s) aversion.

Financial position/capital available

Presently, a substantial severance payment has been offered which after tax leaves a net sum of 1.5 million GBP to invest. Other than the severance pay, other financial assets available include long-dated gilts with a current market value of 65,000 GBP, ordinary shares of the previous company worthy 135,000 GBP, and individual savings cash worthy 48,000 GBP. The potential disposable fund for investment is estimated to be 1.748 million GBP. This is summarised in table 1 below.

Type of financial asset	Value in GBP
Severance net payment	1.5 million
Long dated gilts	65,000

Ordinary shares (previous company)	135,000
Individual Savings Accounts cash	48,000
Total	1.748 million
High-risk investments (70%)	1.2236 million
Low Risk ventures (30%)	0.5244 million

With this financial background, there are some factors to consider. First, the investment portfolio covers not less than 10 years though financial decisions can be made on short term basis depending on financial market and economic dynamics. Taking corrective action in case of a financial crisis is wise. At least 70% of the portfolio will be in the low or medium risk investment category. This means that investments in low-grade bonds and shares of small, vulnerable firms are not an option. Considering a 70% allocation, the potential fund for low-risk investment is approximately 1.2236 million GPB leaving a balance of 0.5244 million for high-risk ventures.

Types of investments

At any one time, investments are made based on the performance of the financial markets and other economic sectors. Investors are bound to experience risk provided they take a 'risk' of investing in short or long term. An investment portfolio has to consider the possibility of shortfalls where short or long term goals are not achieved. It is not advisable to undertake may high-risk investments since the portfolio may "lose value at the wrong time" (Byrne and Blake, 2012). Political and economic factors influence the performance of an investment portfolio citing variants such as economic growth, inflation, interest rates, regime change, international conflicts, and political uncertainty.

Considering the timeline provided (10 years and more), this portfolio would ideally take a balanced approach. The main goal of a balanced oriented model is to minimise possible volatility by encompassing investments that are income generating accompanied by a moderated growth of seed capital. Investors are prone and willing to experience price-fluctuations that are short lived. In such a case, bonds and stocks are worth investing in. However, high-risk investments such low-grade corporate bonds are not advisable because such companies cannot withstand shock that comes with financial crisis. A growth-oriented investor would rather tolerate large short term price fluctuations while investing in long term projects.

It is important to note that investing in stocks attracts a certain degree risk considering financial crisis are unprecedented. However, investment for future generation such a legacy would require a stock portfolio. In this case, an investment in government bonds is ideal because of guaranteed security. Long term investments are driven by amassing equities compared to fixed income since more wealth is likely to be generated 10 or more years to come. For this particular case, 33 percent of the potential fund can be invested in stocks. However, deciding to go the way of stock requires that an investor gets fully on board without any incidence(s) of cash out of stocks the moment the financial market tumbles (Kymin, 2015).

Alternative investments

This is another form of investment that is not listed as a conventional investment such as stocks, bonds, or cash; rather, they are not liquidated, and examples include property, hedge funds, commodities, trust funds, and private equity (Skully, 2007). Notably, this category of investments such as land and trust funds are resilient to financial market dynamics. Real estate is prone to effects of financial crisis and economic dynamics such as pricing fluctuation and inflation. This particular portfolio also emphasizes on alternative investments on property or land. Stocks are further divided into sub-assets namely large cap, mid cap, small cap, and international stocks. On the bond side, municipal and foreign bonds are considered. Each of this is broken below in a table and pie chart form. The bottom line of spreading the investment is to spread the risk, which is, not ‘putting the eggs in one basket’ (Kymin, 2015).

Allocation decision

With the categories of investments identified above, it is possible to perform asset allocation. The assumption in this undertaking is that no taxes are charged on the portfolio similar to a tax-deferred account (Levisauskaite, K. (2010). Another assumption is that the portfolio will adopt an aggressive approach of 80/20 implying an investment of 80 percent on stock and 20% on bond. This means that 80 percent of the 70 percent share of the potential fund (1.784 million GBP) is allocated to stocks whereas 20 percent goes to bonds. Socks are further subdivided to total local and international stock market. Essentially, these subgroups can be allocated differently to have an impact on portfolio growth mitigated risk over time. Consider the scenario illustrated in Table 2 below.

Type of stock investments	The growth of 1.2236 million	Cumulative % return in 10 years	The loss of value in %
Conservative – 40/60	**Low**	**low**	**lowest**
Aggressive – 80/20	**High**	**high**	**highest**

The table above shows two interesting scenarios. Investing in stocks and bonds conservatively minimises the risk of loss in value of the invested capital. Interestingly, this does not guarantee an increased return on investments after the investment period. Conversely, an aggressive approach implies a higher risk of loss of value but with a high return on investments. Thus, this portfolio adopts the aggressive model of 80/20 split into three categories; 60% total stock market, 20% total international stock market, and 20% total bond market. Table 3 shows the subgroups in sterling pounds.

Investment category	The amount in millions GBP

Total stock market (60%)	0.73416
Total international stock (20%)	0.24472
Total bond (20%)	0.24472

The first category can be divided further into large, mid, and small cap stocks as shown in chart below.

Stock category	Amount (% of 0.73416m GBP)
Large Cap (21%)	154,173
Mid Cap (25%)	183,540
Small Cap (14%)	102,782

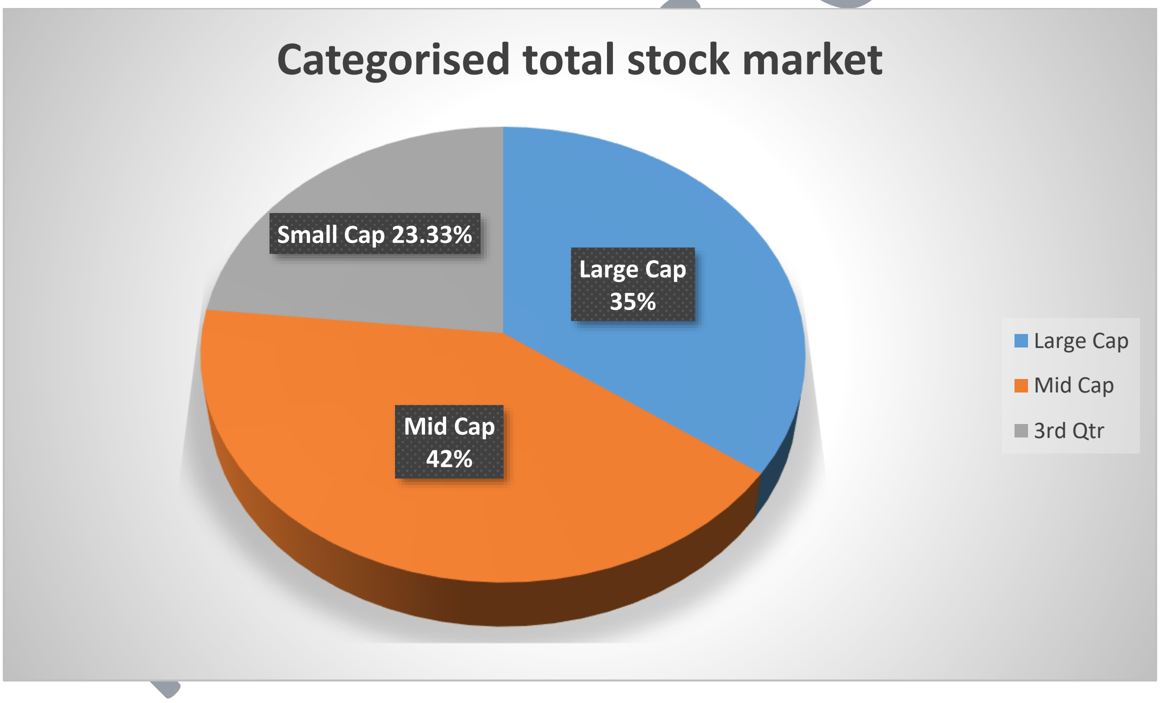

Fig 1. Shows categorisation of total stock market

Unless a portfolio diversification is undertaken, putting money in a single investment is dangerous as it happened in 2007-2008. According to Kymin (2015), shareholders in the UK banking sector in 2006 were rewarded impressively some of them deciding to purchase more shares in other banks only to face a credit crunch in 2007-200 hence a global banking crisis. It means the value of shares in that sector tumbled leading to big losses.

On the other hand, an investment in bonds and property is more vulnerable to interest rates (Levisauskaite, K. (2010). Investment in bonds is characterised by a lower risk of losses accompanied by lower returns. Another key factor considered in this portfolio concerning bond investment is the prospect of inflation. A rise in inflation (sometimes triggered by low interest rates from lenders) is detrimental to bond returns since income is fixed. Surprisingly, this is a contrast with the performance of stock markets when inflation soars.

Geographical area

Care should be taken when investing in different regions since different countries have economic conditions that affect stock markets variable. There is no strong correlation between the markets of different countries. For instance, a stock market that is performing poorly in South East Asia may not necessarily have a negative effect on West Europe's market. Despite the economic conditions being different in various countries and having less impact on local stock markets, care should be taken when investing in international stocks since it is an extra risk. In this particular portfolio, two countries have been chosen for international stocks, that is, Germany and the U.S. Though international investment helps in diversification, the levels of risk in these countries are tolerable. Markets in these countries are less volatile (Levisauskaite, K. (2010) in additional to a stable political environment. This portfolio recommends that bonds be invested in local government and international bonds. Concisely, 15% to be invested locally and 5%. Therefore, a total of 36,708 GBP and 12,236 GBP should be put into local and international bonds respectively. Since portfolio diversification is encouraged to spread risk, investing the bonds in a number of companies is necessary. In this case, about 5-10 companies will be identified for this purpose. Unit trust funds are important for alternative investments such as property. Land, being a form of property has been considered in this portfolio because of its appreciating characteristics. Since this investment has long term goals, land investment is ideal because of guaranteed increased returns in the future.

Personal cash and private equity

Having dealt with 70% of the potential fund for high-risk investment, the remaining amount requires an allocation. A portion of the remaining 30% ought to be put to a unit trust fund or acquisition of a fixed asset, for example, land. In numerical terms, the two categories of investment can be divided as follows; 15% (property funds), and 5% (trust fund). After considering allocations for unit trust and property fund, the 10% remainder can be saved as liquid cash in an interest-earning account. Table 4 shows the allocation below.

Investment category	Amount (% of 0.5244 million m GBP)
Property (15%)	78,600
Unit trust (5%)	26,220
Cash saved (10%)	52,440

Conclusion

Coming up with a personal investment portfolio is no easy task but worthwhile. There are many factors to consider especially economic and political factors. With help from a professional financial advisor, investors can put their cash in good use both in short and long term periods. Most importantly is having a portfolio that is diversified to share or spread risk. It is good to invest using an aggressive model where the return on investments are high though loss on capital is high. When investing in international bonds, countries with less volatile markets are better than new emerging markets and those that are not politically stable. Some factors that affect the performance of conventional assessment include interest rates, fluctuation of prices, and inflation. Therefore, bonds can be invested well by putting in unit trusts and many companies. Property investors speculate on increased prices of properties such as land because it keeps appreciating gradually hence a sound investment.

Reference

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