Did U Know?

How to create a ‘wealth efficient’

Investment Portfolio

Goldsmith Financial Solutions

400 Thames Valley Park Drive

Thames Valley Park

Reading Berkshire,

RG6 1PT

Tel: 0800 152 2505

Web: www.goldsmithfs.co.uk

A few words by author Hannah Goldsmith:

I have been working in the business of financial investment for over 30 years. During this time cultures have changed, economies have changed and technologies have changed in ways that were inconceivable 30 years ago. So why has the landscape of investing in the UK financial services industry barely changed at all over this period?

It has been well documented that investors and institutions in many countries around the world, such as the United States, Australia and parts of Europe, have begun to move heavily away from the traditional financial services model, provided by the Banks and Wealth management companies. This traditional model uses your money to identify and purchase individual stocks (or place 'bets') in the market. As expectations and predictions don't always materialise, these stocks are continuously traded creating additional fees for these companies at your expense.

With the development of new technologies, new models of investing have emerged, which provides the investor with an opportunity to buy the 'market' or 'Index' at a very low fee. These new models help create financial efficiency for the investor, but at the expense of the traditional financial services industry. This dilemma raises a question. Why would these companies want to inform you that alternative 'more profitable' ways to invest are available?

That is why my book 'The Black Hole' has been written. I explain how the traditional system of wealth management works and how this model is slanted (like casinos) in favour of the financial services industry, making you aware of how the industry transfers wealth from you to them. I will also offer you alternative investment models to consider, which are slanted in favour of the investor. You will then be in a much stronger position to decide which model best suits your investment objectives. The hard back book is currently being edited and will be listed and available for purchase on Amazon very shortly.

This eBook has been created from the final chapter of my book which summaries ‘How to create a wealth efficient portfolio’. The following pages list 10 easy referable rules that should serve as a useful 'aide memoire' for the seasoned investor and a valuable route map for the inexperienced investor looking to learn more about the 'dark arts' of investing.

Financial decisions that you have made in the past have bought you to where you are today. Financial decisions that you make from today, will determine the lifestyle that you wish to enjoy in the future. I hope this eBook will provide you with the knowledge to make those considered decisions wisely and help you achieve those first steps to financial efficiency.

Hannah Goldsmith.

GoldSmith financial solutions

1. Let Markets Work For You

World Equity Trading in 2014

	Number of Trades	Sterling Volume
Daily Average	60 million	£194 billion

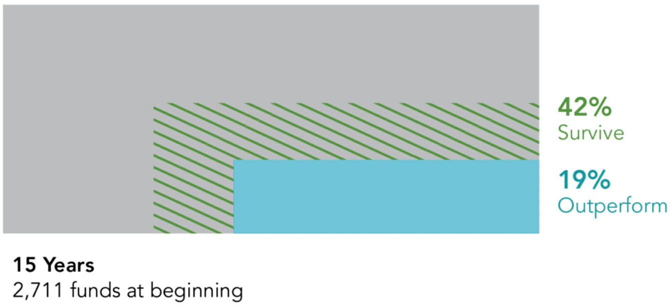
The market is an effective information-processing machine. Millions of participants buy and sell securities in the world markets every day, and the real-time information they bring helps set prices.

Rule 1: The financial market is an effective information processing machine and with all the millions of trades around the globe each and every day, the real time information sets the price. So using the famous 'Jelly Bean' analogy described in earlier chapters, with 60 million trades a day, the probability of finding a favourable discrepancy in price is going to be very minimal.

Let the markets work for you. Buy into the concept of holding a wide basket of stocks from around the world and let the markets do the work. Stop trying to outguess the markets or pay somebody to outguess the markets, as that's the quickest route to burning cash outside of a box of matches. Remember nobody has yet been awarded a Nobel Prize for the world's best fund picker and if you could predict the future (or this year's best performing funds) would you be working for a monthly salary cheque, because that exactly what investment fund managers do.

2. Investment Is Not Speculation

US Equity Mutual Fund Performance



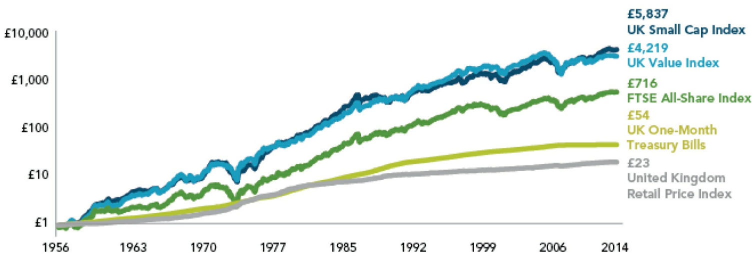
The market's pricing power works against fund managers who try to outsmart other market participants through stock picking or market timing. As evidence, only 19% of US equity mutual funds have survived and outperformed their benchmarks over the past 15 years. In addition, very few managers that do perform well repeat their performance in subsequent time periods. Studies of the European fund market find similar results.

Rule 2: The research has shown over a myriad of time sequences that fund managers will not outperform the markets after fees, costs and taxes. The above research looked a 2,711 US equity funds over a 15 year period and only 19% survived and outperformed their benchmarks.

The European fund managers fair no better. The problem is how do you predict which horses to back? So buy the market and leave the speculation to the gamblers.

3. Take a Long-Term Approach

Growth of a Pound, 1956–2014
(Compounded monthly)



The financial markets have rewarded long-term investors. People expect a positive return on the capital they invest and, historically, the equity and bond markets have provided growth of wealth that has more than offset inflation.

Rule 3: If you cannot accept that you will lose money at some stage on the investment cycle then don't invest at all. However it's important to remember that you will also lose money in value terms by putting it under the bed or in a current low interest bank account due to inflation.

Therefore invest dependent on your capacity for loss, don't try to out-think the market and don't believe anyone who says that 'they' can out-think the market. Just invest in a portfolio that suits your risk profile and stay invested for the longer term.

4. Consider the Drivers of Returns

Dimensions of Expected Returns

EQUITIES

Market
Equity premium—stocks vs. bonds

Company Size
Small cap premium—small vs. large companies

Relative Price
Value premium—value vs. growth companies

Profitability
Profitability premium—high vs. low profitability companies

FIXED INCOME

Term
Term premium—longer vs. shorter maturity bonds

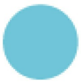
Credit
Credit premium—lower vs. higher credit quality bonds

Academic research has identified these equity and fixed income dimensions, which point to differences in expected returns. These robust dimensions are pervasive across different markets and persistent across different time periods. They can also be pursued in cost-effective portfolios.

Rule 4: When buying a portfolio of stocks please bear in mind that academics for over 50 years since access to computers have become available, have been studying returns in the financial market place. These clever Nobel award winning Laureates have determined that the drivers of returns come from these 6 key areas. So have your portfolio created with these tilts in mind. If you do not have access to this information, consider using an independent financial adviser who does understand these concepts and who will help you create a low cost efficient portfolio.

5. Practice Smart Diversification

FTSE All-Share Index (1988–2014)
FTSE All-Share Index (gross of fees, GBP)



Annualised Return (%)	9.23
Annualised Standard Deviation (%)	14.42

Globally Diversified Portfolio (1988–2014)
100% Equity Model Portfolio (gross of fees, GBP)

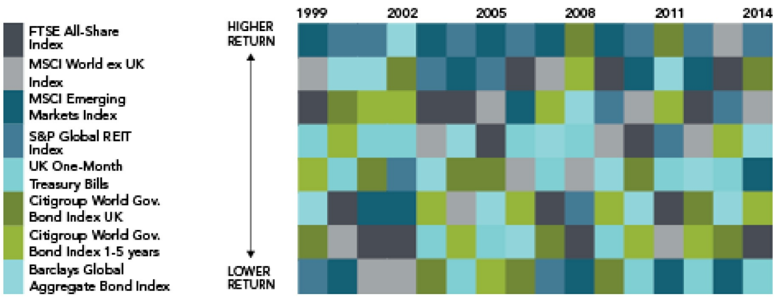
Annualised Return (%)	10.37
Annualised Standard Deviation (%)	16.12

Diversification helps reduce risks that have no return, but diversifying within your home markets is not enough. You should also use diversification to broaden your investment universe.

Rule 5: Investing your money into a portfolio with a heavy UK market bias may suit your wealth managers comfort zone, but this course of action may not necessarily work to your advantage over the longer term. Taking the roulette wheel scenario (described in earlier chapters), investing only in the UK market means you will be putting all your money into only 7% of global capitalisation. There is a large global world out their full of opportunities and yes there are risks of currency exchange and political upheaval, but we are talking about established global markets and there is life and positive investment returns outside of the UK.

6. Avoid Market Timing

Annual Returns by Market Index

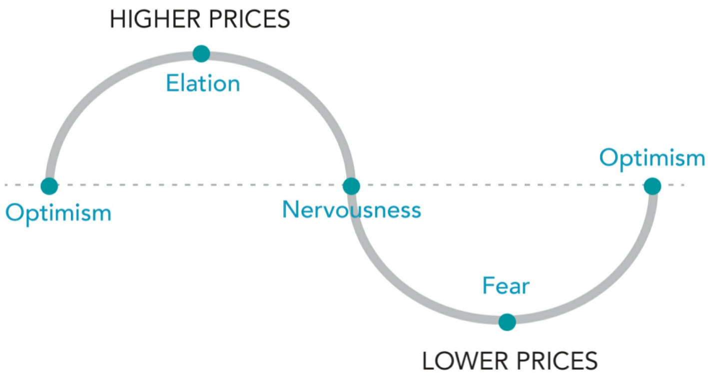


You never know which market segments will outperform from year to year. By holding a globally diversified portfolio, investors are well positioned to capture returns wherever they occur.

Rule 6: Do not try and guess which countries or regions of the world will outperform another or try and guess whether bonds will outperform equities or if large stocks will outperform small stocks. What makes anyone without super powers able to predict the future? All you will get by playing this game is sleepless nights, an ulcer or a heart attack. How many times have you won at the races or greyhounds only to have lost most of it by the time you go home? How many times have you won on the one arm bandit only to put all the winnings back in because you think you are on a lucky streak? As we have seen throughout the book, you will only make your money in short bursts and if you're not in the market when those short bursts happen you lose. Avoid market timing at all costs. Just stay invested or not at all.

7. Manage Your Emotions

Reactive Investing in a Market Cycle



Many people struggle to separate their emotions from investing. Markets go up and down. Reacting to current market conditions may lead to making poor investment decisions at the worst times.

Rule 7: My job as an independent financial adviser is to manage people's expectations and help steer them to achieve their long term lifestyle objectives without fear of ever running out of money. Anyone can make money when the markets are moving favourably. Those that have cost effective portfolios will of course earn even more profit during this stage of the financial cycle and investors are full of optimism finding more money to invest to maximise their wealth. The biggest concern for investors, is when markets are volatile and big losses are incurred over longer periods of time. Investors (prompted by the media) are then tempted to jump ship and wait for the markets to recover before they jump back in. The problem is market timing cannot be predicted. If you take money out in falling markets you will lose 'real' money because of fear. Therefore you will not reinvest until you get your optimism back which is often too late, because all the gains have been recovered and you still have your losses to make up. The value of your portfolio is just a number which changes daily until you cash it in. Only then does it become a reality. So if you invest for the longer term, just stay invested and don't be influenced by the media.

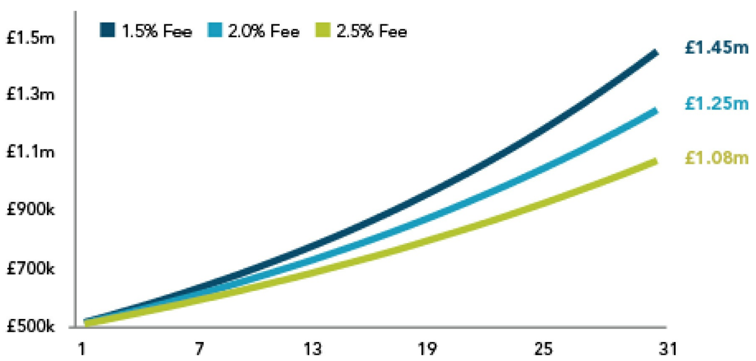
8. Look Beyond the Headlines

Daily market news and commentary can challenge your investment discipline. Some messages stir anxiety about the future while others tempt you with the promise of easy profits. If you are tempted, consider the source and learn to spot the difference between entertainment and real advice.

Rule 8: Manage your emotions by investing in a risk portfolio correlated to your capacity for loss and remember investing is for the longer term. History says that you will be rewarded for your bravery, but during negative markets, the media will try to convince you otherwise. It is important to note that the media is not in business just to provide factual information. The Media is a business in its own right and there to entertain and offer an opinion which it does extremely too well at times. They are also in existence to make a profit and if they don't sell their program or publication, they go out of business. Therefore, they sell stories and without interesting stories, they have no viewers or readers, so don't expect anything from the media other than rhetoric to cause anxiety or must have information. If you have to follow the media dialogue, ask yourself why are they are saying this? Consider the source and again, ask yourself if they have any more information than anyone else? Remember our stories from earlier chapters in the book about financial predictions. Listen by all means, but act very carefully.

9. Keep Costs Low

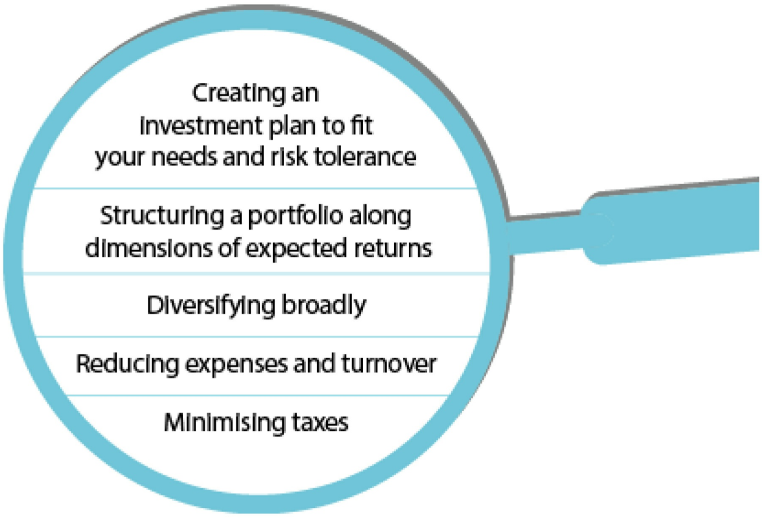
Net Growth of £500,000



Over long time periods, high costs such as management fees, fund expenses and taxes can drag on wealth accumulation in a portfolio. You should strive to incur only those costs that are unavoidable and those that add value to your investments.

Rule 9: For a wealth efficient portfolio it is really important to ensure that your portfolio costs are kept to the bare minimum. The fee you pay your financial adviser (even if paid directly from the portfolio), is not part of the cost review as long as you are getting value for your money. It's the hidden fees and costs that are taken from your portfolio fund value, in the name of service costs, annual management charges and discretionary management fees that are often unnecessary. Try and keep these costs to less than 1% in total. The industry average with traditional financial service companies is in the region of 2.5%. Refer to the chapter in the book which highlights that a saving of just 1% a year, will enable you to make a substantial amount of money utilising compounding interest over the life of your portfolio. Enough to perhaps buy a holiday home, finance exotic holidays, contribute towards education costs for grandchildren or an additional nest egg for care in later life. Money that you can use for you and your family, rather than just giving it away to an industry that feeds the fat cats.

10. Focus On What You Can Control



A financial adviser can create a plan tailored to your personal financial needs while helping you focus on actions that add value. This can lead to a better investment experience.

Rule 10: Use your financial adviser to create a wealth efficient portfolio that's in line with your capacity for loss. Do not focus on how much you want to make (nobody knows), but more on how much are you prepared to lose without causing financial hardship. Let them help you prepare a cash flow analysis and build a lifelong cash flow plan to help you achieve all the things you have on your to–do list before you leave this earth. Don't let your financial adviser come round each year moving and changing your funds to justify their existence and their fees. They are wasting your money. If they were that good they wouldn't have to change funds every year. If they got the fund choice wrong last year what makes you think they will get it right this year? Ask them what their investment philosophy is? If they don't have one in print for you to read, why would you let them manage your money?

In Conclusion

So in summary, create a portfolio to suit your capacity for loss, build the portfolio along the lines of academic study and dimension of returns, diversify globally and buy the market, reduce turnover of stock and minimise fund management fees, costs and taxes.

I wish you well in your investment journey and hope this book has enlightened you to take action and maximise your investment returns. I said at the beginning of this eBook that ‘financial decisions that you have made in the past have bought you to this moment in time. Financial decisions that you make from today, will lead you to your future lifestyle’.

Please choose wisely...

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