Small is beautiful

A portfolio biased towards smaller companies has done well for Paul, but he's looking for some help with managing his investments

Paul has constructed his portfolio with growth in mind, not income. 'I have never taken income from the portfolio,' he confides. 'Growth is my priority right now: I will move more towards income assets in the future.'

The 51-year-old, who works in the food industry, has been investing for almost 30 years. His largest holding is the JP Morgan European Smaller Companies investment trust, winner of our award this year for Best Overseas Investment Trust (see June issue, page 45). About a third of his portfolio (or half if you don't count the cash holding) is invested in smaller company funds specialising in various parts of the world: Baillie Gifford Shin Nippon, North Atlantic Smaller Companies, Aberdeen Asian Smaller Companies and – just in case he'd left anywhere out – F&C Global Smaller Companies.

Canny move

Paul also owns the open-ended First State Latin America fund, which he likes because of the favourable demographics of the region. He was able to bag something of a bargain for himself when the trust offered to buy back shares from investors in an attempt to narrow its discount to net asset value. The price offered was higher than the market price at the time, so Paul sold some of his existing shares back to the trust only to buy them back again at the lower, market price. 'That was one of the better investments I have made, certainly!' he says.

Paul has also been a long-term investor in the Invesco Perpetual UK High Income fund, which was managed by Neil Woodford until earlier this year. He comments that he sold down some of his holding in this fund a short time before Woodford announced his departure, but the two events were not linked. 'It was simply the case that too much of my exposure was to that fund, and as *What Investment* frequently hammers home, diversification and rebalancing of holdings is very important.'

As for the new Woodford fund (see New Offers, page 38), Paul is somewhat reluctant to invest on the basis that he already has a fair exposure to UK equities through funds like Nick Train's Finsbury Growth & Income, Lowland (see page 37) and Unicorn UK Income (see page 31).

On the defensive

Paul's fairly racy asset allocation strategy is counterbalanced by a hefty cash holding, over a third of the portfolio, and a small allocation to physical gold. He is planning to reduce the cash weighting by investing some of it but, interestingly, he won't be doing this himself. Instead, he has decided to entrust half of his cash holdings to a wealth management firm.

'I am doing this in order to see how they perform, and whether they can manage the money better than I have,' he explains, adding that the task of managing his portfolio has become 'more onerous' as it has grown in size. 'I have spent a very long time looking for the right firm.'

If the experiment proves successful, he will add more to the externally managed portfolio. 'My investment mantra is centered on growth, but also on the idea that I invest in riskier asset classes in the most cautious way that I can. I am hoping that the wealth management firm can do that better than me, but I want to compare their performance with mine before I make a decision.'

If you would like to see your portfolio featured in this section, please call Carly O'Donoghue on 020 7250 7055.

Paul's portfolio

Holding	% weight in portfolio
Investment trusts:	
JP Morgan European Smaller Comps	7.8%
Baillie Gifford Shin Nippon	4.4%
North Atlantic Smaller Companies	3.6%
Finsbury Growth & Income	3.3%
F&C Global Smaller Companies	2.9%
Others	15.4%
Total	**37.4%**
Unit trusts:	
Jupiter European Income	4.2%
Unicorn UK Income	3.9%
Invesco Perpetual High Income	3.5%
Others	2.7%
Total	**14.3%**
Exchange-traded funds:	
ETFS Metal Secure Physical Gold	2.7%
iShares FTSE MIB UCITS ETF	0.8%
Total	**3.5%**
VCTs:	
Proven VCT	7.5%
Cash:	37.3%

What the experts say...

Richard Troue is head of investment analysis at Hargreaves Lansdown

Richard Troue says:
This is a higher-risk portfolio, with a lot of exposure to small and medium-sized companies globally.

Generally speaking, this is an area that has performed exceptionally well over the past five years. During the past three months, however, small- and mid-cap shares have been hit as investors started taking profits from any area that had performed well and reinvesting in areas that had lagged: larger companies and more defensive sectors, for example.

There is also a lot of exposure to higher-risk emerging markets – an area that has performed less well over the past couple of years as investors have been concerned about slowing growth, among other things. We continue to believe that emerging markets have tremendous long-term potential.

> 'I'd consider increasing exposure to quality equity income funds'

Paul's choice of investment trusts and unit trusts is good, with an attractive mix of highly rated managers. However, his allocation to the gold ETF is probably too small to offer any real hedge against another crisis, if that is why it's held. And other than as a short-term trading opportunity, I'd question the need for the FTSE MIB ETF, which tracks the Italian stock market. ProVen is a solid VCT manager, but we generally suggest holding a diversified portfolio of VCTs, so in the coming years I'd aim to build on this allocation by adding other VCTs such as those from Northern, Mobeus, Maven and British Smaller Companies.

Simply looking at the investments held, I would suggest that this is a portfolio for someone in their thirties and forties. The cash provides some balance, but seems high when compared with the risk profile of the investments. As a general rule, keeping the equivalent of three to six months' outgoings in cash is sensible: with any remainder, I'd consider increasing exposure to quality equity income funds and larger companies.

Jonathan Davis is an economist and wealth manager

Jonathan Davis says:
Paul's portfolio is largely equities and cash. The equities have performed superbly for the past five years, since the start of the current bull market. However, that is itself an issue.

Nothing goes in a straight line forever, and five years and three months is long in the tooth for an equity bull market. I am uncomfortable with Western shares at these prices, and Paul may consider reducing his exposure to lock in some of the wonderful gains he must have made. I am more attracted to emerging market equities, the prices of which have been battered – especially those of Russia, Brazil and India.

Paul has a small allocation to Japanese shares through the Baillie Gifford Shin Nippon and JP Morgan Japanese investment trusts. Japan's stock market is down 5 to 10 per cent so far this year and could still have further to slide, as could Western shares.

> 'Five years is long in the tooth for an equity bull market'

However, in the long term I'm very bullish on Japanese shares – more so than Western shares. They fell for 23 years to 2012, and I believe a multi-year bull market is commencing.

There is no allocation to bonds. I am uncomfortable with high-yield bonds for the same reason as equities: there has been a prolonged period of gains. However, as risk aversion appears to be rearing its head, I remain attracted to government bonds.

Paul has a small allocation to commodities in the form of a gold ETF. The prices of gold and gold shares have fallen to a level where they are becoming tempting, but gains are far from assured. Other commodities offer a better risk-reward profile in the long run, for example US natural gas.

He can continue to invest for growth rather than income for now, but could look at increasing his allocation to equity income as he moves towards retirement. The compounding of dividends can work wonders. ◆