SPEAKING

'Investornese' & you

ATOM CAPITAL

#2 OF 6

When first entering the investment world, it seems as if everyone is speaking a different language. Here is a simple guide to help you navigate the terminology and investment jargon you may encounter.

Saving vs Investing:

Although they may appear to be the same and both are essential, they have 2 distinct differences.

1 The first differentiator is time:

Saving is when you put money aside until you need it, while investing is putting your money into something you believe will go up in value in the future. An important distinction between the two is the time horizon; saving is for shorter term needs such as saving for a holiday or to buy something specific and investing is for medium to long term needs, such as retirement or building wealth over a long time period.

2 The second differentiator is risk:

Saving generally has a fairly steady, constant uptick in value, with the increase mainly driven from contributions made by you. Often savings vehicles are lower risk, but with lower expected returns.

With investing, you can expect ups and downs in line with the volatility of the type of assets you are invested in. The total gain is driven by investment returns and contributions. Generally speaking, investment vehicles have a higher risk profile than savings, but with the potential of higher returns.

What is...

A Linked Investment Service Provider (LISP)?

A LISP acts as a platform that facilitates investment transactions on behalf of investors. They are like a supermarket for various investment vehicles, where you can access various funds and other investment vehicles all in one place. They typically offer investment services such as administration, reporting, and monitoring of investments.

Risk profile?

Risk profiles are the measure of the risk that you need to take to achieve your investment goals, given your financial needs, time horizon and willingness to accept those risks.

Risk can be broken down into three factors:

Need: The level of risk needed in order to meet your financial goal.

Ability: The investment risk you can afford to take.

Willingness: This is your comfort level with the possibility of losing some or all of your investment. In essence, it is your willingness to take on risk. If you prefer little or no risk, your risk tolerance will be low. If you accept the risk of losing some or all of your investment because you want the potential for higher returns, your risk tolerance will more than likely be moderate to high.

Your risk profile is specific to you and your financial situation. Your financial advisor is best suited to help you determine what your preferred risk profile is - this will further help you meet your short-term and long-term financial goals. It's important to note that different investment goals have different risk profiles.

An investment horizon?

An investment horizon refers to the length of time an investor expects to or is able to hold an investment before selling it. It is the time frame within which you aim to achieve your financial goals through the returns on your investment. Investment horizons can vary depending on the type of investment, the risk involved, and your financial goals.

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An MDD?

Unit trust funds are required to produce a Minimum Disclosure Document (MDD), previously known as a fund fact sheet, at least quarterly. MDD’s are governed by regulations and contain key information about the fund to help investors decide on the suitability of the investment. This includes information such as the asset allocation, the fund size, the total cost, the top 10 holdings as well as historic performance and income distributions. However, it is good to remember that past performance is not an indicator of future performance.

An asset?

In the investment world, an asset is something investors can buy (and invest in) that has a value or some kind of future benefit. Often this future benefit is investment return, which can differ depending on the asset. Common asset classes include stocks (also referred to as equities or shares), bonds (also referred to as gilts), cash, and property, each with their own potential return and risk characteristics.

Asset allocation?

This involves balancing risk and reward by optimising the mix of assets (e.g. local or global - equities, bonds, property, cash) of a fund to best meet the investor’s goals.

Rebalancing?

The process of realigning the mix of assets in a fund to their original/optimal weights. This is often required when certain assets appreciate or depreciate in value over a certain time period and throw the overall fund off its optimal mix of assets.

Standard deviation and is it different to volatility?

Standard deviation is used to measure the volatility of the fund:
the higher the figure, the more widely dispersed the returns of a fund will be. Volatility is the fluctuation of the returns of a fund.

A drawdown and why does it matter?

The drawdown of a fund shows the negative return of a fund over a specific period, which is measured from its highest point (peak) to its lowest point (trough). It is important to keep the investment horizon and risk profile of the fund in mind when looking at the drawdown of the fund. Funds with a higher risk profile can be expected to have a larger drawdown and vice versa.

A Sharpe ratio?

The Sharpe ratio measures the risk adjusted performance of a fund. It shows the potential additional return (measured by fund return less the risk-free rate) per unit of increase in total risk. The easiest way to interpret the Sharpe ratio is the higher the ratio the better (the more return you get for the risk you take). The risk-free rate is, in theory, what return an investor would earn with zero risk. In reality, no investment has completely zero risk, but a bank deposit rate or an appropriate government bond yield is commonly used as a proxy.

The difference between Passive and Active funds?

A passive investing style is where a fund aims to track the performance of a certain market index. The composition of stocks in the passive fund will look the same as the market index it is tracking and the difference in return should only be the fee paid. An active investing style is where the portfolio manager believes they are skilled enough to outperform the market index and will build their own portfolio of stocks which aim to outperform the market. It can therefore underperform or outperform the market at different points in time.

Tracking error?

The tracking error is the difference between a fund’s actual return versus the return of the benchmark. For a passive fund, an investor generally wants to minimize this as the goal with the passive fund is to match the return of the index. For an active fund, tracking error may be less of a concern.

Liquidity?

This represents how easy it is to turn assets of a fund into cash. It is important to remember that different investments have different liquidity characteristics due to the nature of the underlying asset classes.

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Styles of investing

Growth investing:

This is an investment style whereby the focus is **buying assets that are rapidly growing with higher-than-average growth** with the expectation that they will continue to do so over the long-term.

Value investing:

Value investing is an investment style whereby the **focus is buying assets at a discount to their estimated fair value and selling them when they reach this fair value.** Often these types of assets are unloved or less favoured by the market, hence their undervaluation.

Thematic investing:

Thematic Investing is an investment style whereby the focus is **finding and investing in assets that relate to a specific long-term trend or theme**, such as renewable energy, artificial intelligence, fintech innovation, and so on.

Quality investing:

Quality investing is where the focus is on **buying assets that rate highly on certain fundamental metrics that are deemed 'quality.'** Often these are companies that are profitable, financially stable, have low debt and strong management which are expected to grow in value over time. There can be a wide interpretation of 'quality' and investors may be willing to 'pay up' for this quality.

We hope this has helped to simplify some of our jargon.
However, if it is all still sounds like a different language to you, please don't hesitate to contact us.

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