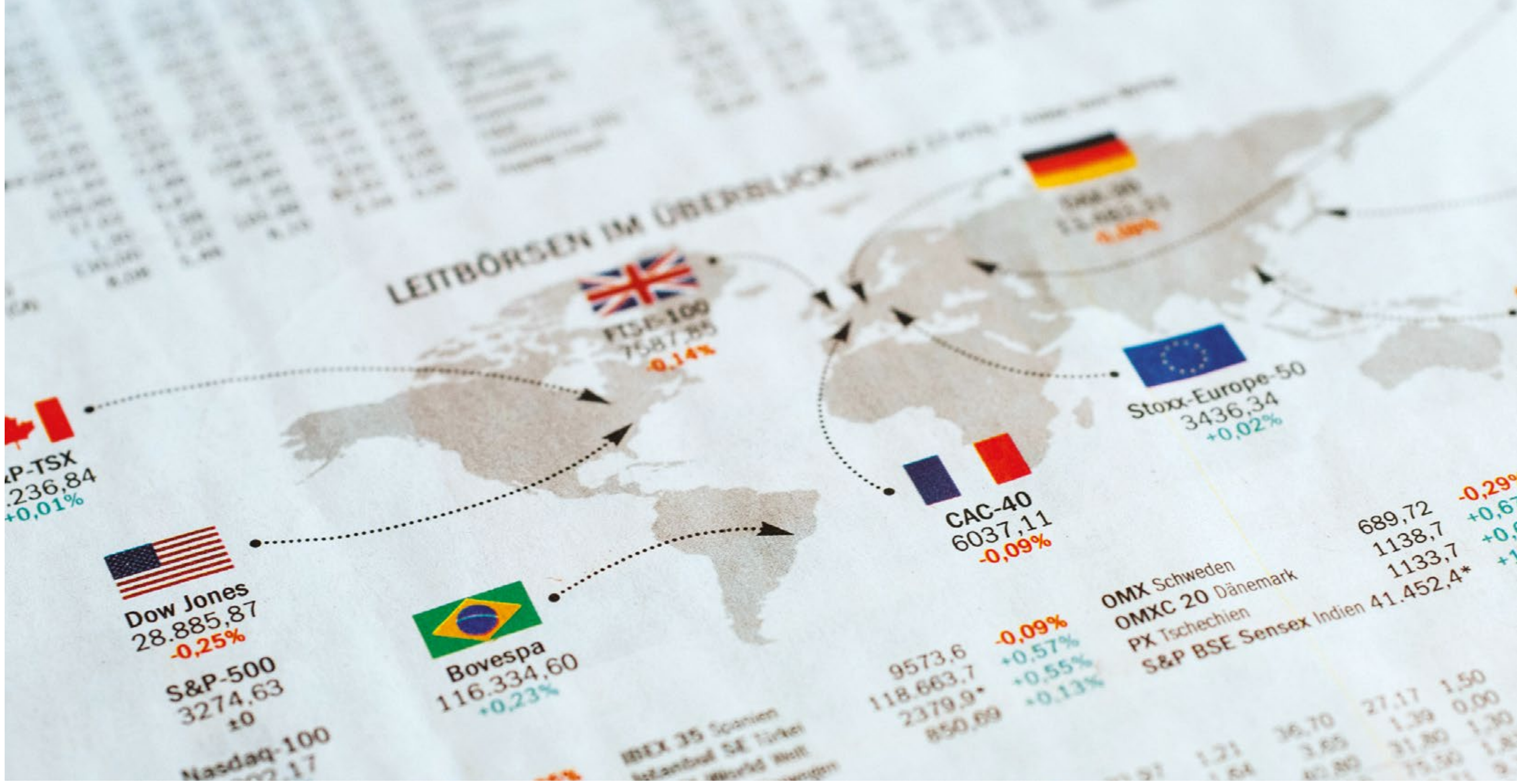
The importance of diversification



The pandemic has highlighted the value of holding a well-diversified portfolio of investments.

The Covid-19 pandemic has already taught us a great deal, from government ministers to trapped-at-home office workers. Some people have been faced with relearning old lessons they may have forgotten.

Global stock market performance has changed radically since February when the world first began to pay attention to Covid-19. While nearly all markets took a sharp downturn in February and the first three weeks of March, there has been a marked divergence in behaviour since then. The table below shows how differently the various main markets have performed.

Market	Index	31/12/19–23/3/20*	23/3/20– 30/10/20	Year to 30/10/20
UK	FTSE 100	-33.79%	11.68%	-26.05%
US	S&P 500	-30.75%	46.15%	1.21%
Europe	Euro Stoxx 50	-33.63%	19.02%	-21.01%
Japan	Nikkei 225	-28.61%	36.06%	-2.87%
China	Shanghai Composite	-12.78%	+21.22%	+5.72%

** 2020 year-to-date low point for UK, US and China markets*

Best returns outside the UK

A UK-based investor who only invested in UK-focused equity funds would have paid a heavy price for staying with their home country and not diversifying internationally. The 2020 performance of the two main UK equity sectors, UK All Companies and UK Equity Income, has been such that at 30 October they occupied the bottom two year-to-date slots of the 39 sectors monitored by the Investment Association. The best performing UK sector over the period was UK Index Linked Gilts, with an average return of 12.9% – a reminder of the diversification benefits of bonds.

The relatively strong performance of the US has much to do with the dominance of the US technology sector – the five largest companies in the S&P 500 index are Apple, Microsoft, Amazon, Facebook and Alphabet (the holding company for Google). The pandemic has given a massive boost to this sector, from online shopping in all its forms to video conferencing. The UK has no companies that come near to competing – in September the value of Apple exceeded the total worth of the companies of the FTSE 100.

Diversification between markets is not only about capital performance; it can also help on the dividend front. For example, in the second quarter of 2020, global dividend payments were 22% lower than in the corresponding period of 2019, according to one major investment house. However, the bald figure hid some enormous regional differences: in the UK, the fall in dividends was a brutal 54.2% while in Japan it was just 4.2%. In the USA, dividends rose by 0.1%.

The turbulence of 2020 has been a reminder that investment diversification can help smooth both capital and income performance in challenging times. For a review of your existing investment holdings and advice on your diversification strategy, please talk to us.

The value of your investment, and the income from it, can go down as well as up, and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.