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global investment management

The art and science of investment: Why process matters

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In the world of fund selection, picking funds is a blend of science and art. Every investor prioritises their research differently, but the most common framework involves the 4 P's: philosophy, process, people, and performance. Unlike the marketing mix of product, price, place, and promotion, this framework helps in assessing funds comprehensively. People and performance often weigh heavily in an investor's decision-making process.

A high-profile manager with a strong track record is an easy sell for any asset management company. Philosophy reveals the manager's fundamental beliefs guiding their decisions and helps investors distinguish between different investment styles. However, the investment process, which is sometimes overlooked, is crucial. We have invested a lot of time in developing our own process and analysing those of investment managers worldwide.

An established investment process is vital for mitigating emotional biases that often affect investment decisions. Behavioural finance has shown that emotions like fear and greed can lead to irrational decisions. A structured process helps investors remain disciplined and avoid impulsive choices based on short-term market movements. By sticking to a well-defined process, fund managers can ensure their decisions are based on analysis and strategy rather than emotional reactions.

Consider the 2008 financial crisis. Many investors, driven by fear, sold their investments at significant losses. In contrast, those who adhered to a disciplined investment process, such as Warren Buffett, who famously advised to "be fearful when others are greedy and greedy when others are fearful," made rational decisions that ultimately led to long-term gains. Buffett's commitment to his investment principles allowed him to spot undervalued opportunities during the downturn, demonstrating the importance of a solid investment process in countering emotional biases.

A robust investment process also promotes consistency and objectivity. Behavioural biases such as overconfidence, herd behaviour, and loss aversion can cloud judgement and lead to erratic decision-making. A systematic approach enables fund managers to apply the same criteria and methodologies to each decision, thereby reducing the influence of personal biases. This objectivity is essential for achieving long-term investment goals and maintaining investor trust.

Clear and transparent investment processes enhance accountability. When fund managers follow a documented process, it is easier to review and evaluate their decisions. This accountability ensures that each investment choice is based on sound reasoning and predefined criteria. Transparency builds investor confidence, as they can see that their money is being managed systematically, rather than being subject to whimsical or emotionally driven decisions.

Market volatility often triggers strong emotional responses, leading to decisions that may not align with long-term strategies. A disciplined process helps fund managers navigate volatility by sticking to their investment principles and strategies. This steadiness is crucial during downturns, as it prevents panic selling and encourages a focus on long-term value rather than short-term losses. Managing volatility with a structured approach enables fund managers to better protect investor capital and achieve more stable returns.

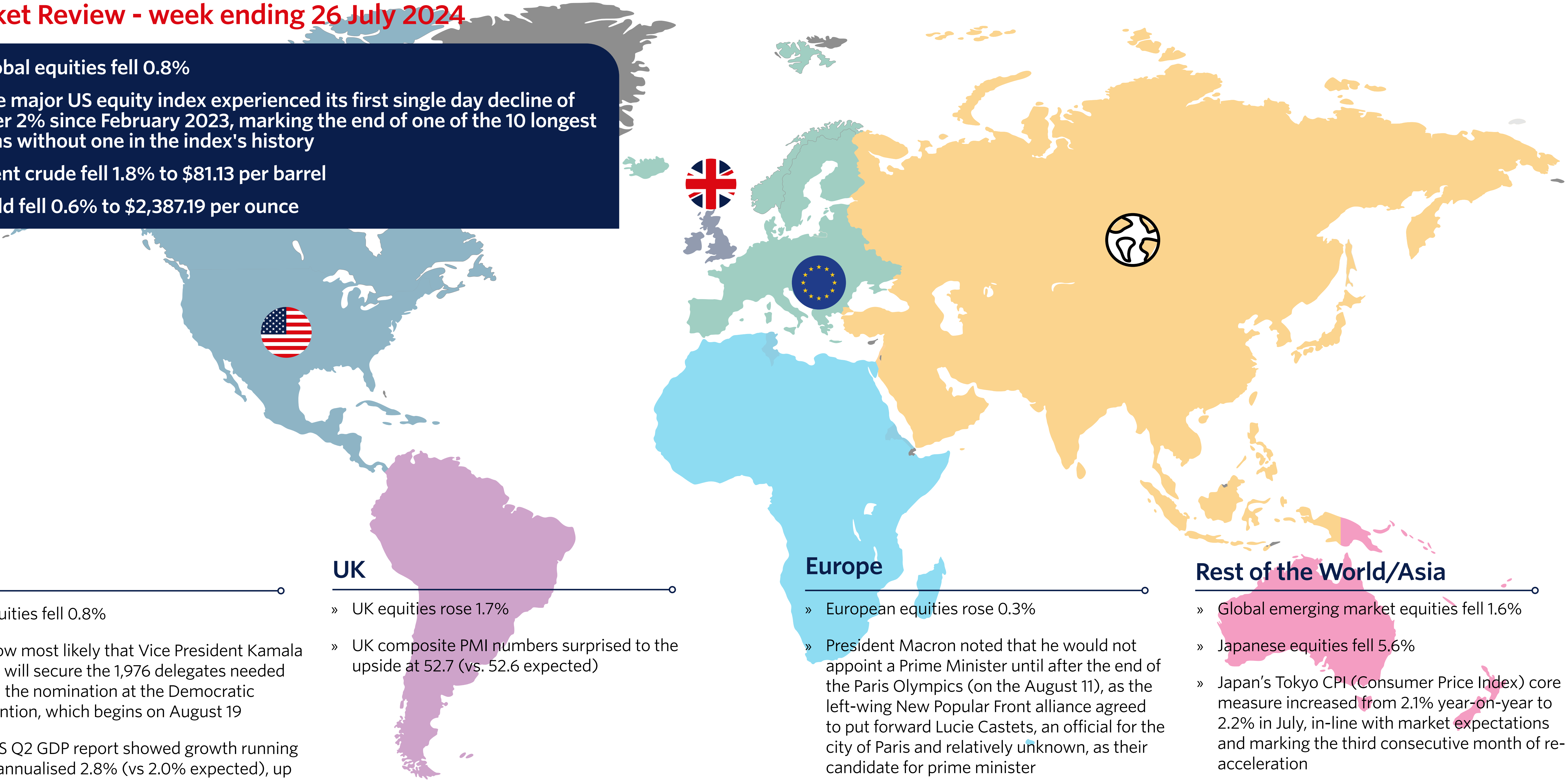
The impact of the COVID-19 pandemic on markets in 2020 underscored the importance of managing volatility through a disciplined process. Fund managers who maintained their investment processes avoided panic selling and instead focused on rebalancing portfolios and identifying opportunities in undervalued sectors. This approach helped protect investors from permanent loss of capital and positioned funds for recovery as markets stabilised.

The quality of investment decisions improves significantly with a well-defined process. Behavioural investing highlights how cognitive biases like anchoring, confirmation bias, and hindsight bias can distort perception and analysis. A systematic process involves rigorous research, data analysis, and adherence to investment criteria, leading to more informed and rational decisions. This disciplined approach ensures that each investment is thoroughly evaluated, reducing the likelihood of errors caused by cognitive biases.

In conclusion, a well-defined investment process is crucial for managing the behavioural aspects of investing. It should allow the portfolio manager sufficient freedom to implement their judgement, but it must also be robust enough to mitigate emotional biases, ensure consistency and objectivity, enhance accountability and transparency, manage market volatility, and improve decision-making quality. By focusing on a structured process, fund managers can achieve better investment outcomes and maintain long-term investor confidence.

Market Review - week ending 26 July 2024

- Global equities fell 0.8%
- The major US equity index experienced its first single day decline of over 2% since February 2023, marking the end of one of the 10 longest runs without one in the index's history
- Brent crude fell 1.8% to $81.13 per barrel
- Gold fell 0.6% to $2,387.19 per ounce



US

- US equities fell 0.8%
- It is now most likely that Vice President Kamala Harris will secure the 1,976 delegates needed to win the nomination at the Democratic convention, which begins on August 19
- The US Q2 GDP report showed growth running at an annualised 2.8% (vs 2.0% expected), up from 1.4% in Q1
- The US core PCE (Personal Consumption Expenditure) index for June rose 0.2% month-on-month in line with expectations
- The Richmond Fed's manufacturing index was down to -17 in July (vs -7 expected), its lowest level since May 2020 during COVID-19 lockdowns

UK

- UK equities rose 1.7%
- UK composite PMI numbers surprised to the upside at 52.7 (vs. 52.6 expected)

Europe

- European equities rose 0.3%
- President Macron noted that he would not appoint a Prime Minister until after the end of the Paris Olympics (on the August 11), as the left-wing New Popular Front alliance agreed to put forward Lucie Castets, an official for the city of Paris and relatively unknown, as their candidate for prime minister
- The Euro Area composite PMI (Purchasing Managers Index) fell to 50.1 (vs 50.9 expected), with the German figures particularly disappointing at 48.7 (vs 50.6 expected)
- The IFO's Business Climate indicator from Germany fell to 87.0 (vs 89.0 expected), its third consecutive monthly decline
- In France, The INSEE Business Confidence index fell to 94 (vs 99 expected), its lowest level since February 2021

Rest of the World/Asia

- Global emerging market equities fell 1.6%
- Japanese equities fell 5.6%
- Japan's Tokyo CPI (Consumer Price Index) core measure increased from 2.1% year-on-year to 2.2% in July, in-line with market expectations and marking the third consecutive month of re-acceleration
- Chinese equities fell 2.3%
- The Chinese central bank unexpectedly cut their seven-day reverse repo rate for the first time in almost a year, lowering it by 10bps to 1.7%
- The Bank of Canada delivered a 25bp interest rate cut to 4.5%, the second consecutive meeting where they've cut rates

Market Performance - week ending 26 July 2024

		Cumulative returns			
Asset Class / Region	**Currency**	**Week ending 26 July**	**Month to date**	**YTD 2024**	**12 months**
Developed Markets Equities					
United States	USD	-0.8%	0.0%	15.1%	20.8%
United Kingdom	GBP	1.7%	1.6%	9.5%	12.6%
Continental Europe	EUR	0.3%	-0.4%	8.3%	12.7%
Japan	JPY	-5.6%	-3.9%	15.4%	21.0%
Asia Pacific (ex Japan)	USD	-1.8%	-1.1%	7.3%	7.4%
Australia	AUD	-0.6%	2.0%	6.3%	11.3%
Global	USD	-0.8%	0.4%	12.2%	17.5%
Emerging Markets Equities					
Emerging Europe	USD	-2.0%	0.8%	16.3%	24.5%
Emerging Asia	USD	-1.7%	-1.5%	9.4%	8.7%
Emerging Latin America	USD	-2.7%	0.9%	-14.9%	-9.7%
BRICs	USD	-0.6%	-0.2%	6.1%	3.5%
China	USD	-2.3%	-2.9%	1.7%	-9.7%
MENA countries	USD	-0.3%	2.8%	-0.7%	-1.7%
South Africa	USD	1.4%	1.7%	6.4%	3.3%
*India	USD	0.0%	2.2%	13.6%	23.5%
Global emerging markets	USD	-1.6%	-0.9%	6.5%	6.6%
Bonds					
US Treasuries	USD	0.3%	1.4%	0.5%	2.7%
US Treasuries (inflation protected)	USD	0.0%	1.0%	1.7%	3.1%
US Corporate (investment grade)	USD	0.2%	1.5%	1.6%	6.0%
US High Yield	USD	0.3%	1.7%	4.4%	11.1%
UK Gilts	GBP	0.1%	0.8%	-1.9%	4.5%
UK Corporate (investment grade)	GBP	0.1%	1.3%	1.2%	10.0%
Euro Government Bonds	EUR	0.2%	1.5%	-0.5%	4.2%
Euro Corporate (investment grade)	EUR	0.4%	1.3%	1.8%	7.1%
Euro High Yield	EUR	0.1%	1.0%	4.1%	11.0%
Global Government Bonds	USD	0.4%	2.1%	-2.2%	-0.2%
Global Bonds	USD	0.2%	2.0%	-0.9%	2.2%
Global Convertible Bonds	USD	-0.4%	1.5%	0.3%	1.5%
Emerging Market Bonds	USD	0.2%	1.3%	2.7%	8.0%

		Cumulative returns			
Asset Class / Region	**Currency**	**Week ending 26 July**	**Month to date**	**YTD 2024**	**12 months**
Property					
US Property Securities	USD	0.1%	5.5%	4.7%	7.2%
Australian Property Securities	AUD	-2.8%	3.7%	12.2%	21.6%
Asia Property Securities	USD	-1.4%	3.5%	-8.4%	-9.0%
Global Property Securities	USD	-0.5%	4.9%	2.4%	6.4%
Currencies					
Euro	USD	-0.2%	1.4%	-1.8%	-1.9%
UK Pound Sterling	USD	-0.3%	1.8%	0.9%	-0.3%
Japanese Yen	USD	2.4%	4.6%	-8.4%	-8.6%
Australian Dollar	USD	-1.8%	-1.6%	-4.0%	-2.8%
South African Rand	USD	0.0%	-0.3%	-0.1%	-3.4%
Swiss Franc	USD	0.6%	1.7%	-5.0%	-2.3%
Chinese Yuan	USD	0.3%	0.2%	-2.1%	-1.4%
Commodities & Alternatives					
Commodities	USD	-1.7%	-4.7%	2.6%	-2.4%
Agricultural Commodities	USD	-0.9%	-2.3%	-2.1%	-9.3%
Oil	USD	-1.8%	-6.1%	5.3%	-2.2%
Gold	USD	-0.6%	2.6%	15.7%	21.2%

Source: Bloomberg Finance L.P. Past performance is not indicative of future returns.

*Data as at 15 July 2024 due to Bank Holidays in India

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