



News from Louis Letourneau.

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Whether you want to play it safe or fancy yourself as a stock market demon, a financial strategy is a must.

I wrote last month about implementing a financial strategy. I know this sounds a bit daunting, so this month, I'm providing a step-by-step approach to help you get this important job right.

Step 1 Review your assets

Include all your savings and investments (ISAs, pensions, building society accounts etc.), but exclude the property you live in.

Sit down and work out how much you have and how it's divided between the main asset classes – cash, property, equities, fixed interest. At this point, if you haven't got an overall financial plan in place, it may be a bit of a hotchpotch. You've probably got a collection of ISAs and pension plans that you've acquired piecemeal over the years. But don't worry – this is just the starting point.

Step 2 Assessing your situation and objectives

Once you know what you have, you can start thinking about what you *should* have and draw up a plan.

The right investments for you will depend on a number of factors, the main ones being your objectives and expectations, your age, your attitude to risk and whether or not you need an income from your investments. These factors will dictate the strategy. The different factors affect each other, too. For example, if you're 57 and planning to retire at 60, you can't take too much risk with your investments if you need them to provide an income in a few years' time. Conversely, if you're 30 and expect to work until 60, you can invest the bulk of your resources in the equity markets for future growth.

Step 3 Your options

Asset allocation is the key to a successful investment strategy. All it means is that you (or your adviser) work out which types of asset you should invest in and in what proportions in order to achieve your objectives, and then construct an appropriate portfolio.

It's important to understand what the various asset classes are and what they actually mean. The main classes are:

Cash – Money on deposit. This is of course very low-risk. However, the problem with holding too much in cash is the inflation risk. Any rate of interest you can earn should be in excess of inflation so that the amount of your cash doesn't lose its future purchasing power in real terms.

Fixed interest is a low-risk investment consisting of gilts and corporate bonds. Gilts - (gilt-edged securities) are Government stocks and are effectively loans to the Government. Since it's highly unlikely that the British Government would ever default on its loans, they offer a high degree of security, although their prices do go up and down. The returns that they produce are closely linked to movements in interest rates. The gilts market has been negative recently. If you want a gilts element in your portfolio, you should look at index-linked gilts, as these protect against the risk of inflation.

Corporate bonds are similar in many ways to gilts, but are offered by limited companies and therefore carry a higher risk. There are varying degrees of quality of corporate bonds. Investment grade (i.e. good quality) bonds carry a lower risk than sub-investment grade bonds. As with gilts, the underlying capital value of corporate bonds is linked to movements in interest rates. Returns in the sector have been sluggish recently but they are an important component of a portfolio for someone who wants a lower risk investment.

Property funds normally invest only in commercial property, rarely residential. Returns from property funds have been excellent over the past few years and future prospects look good also. The commercial property sector doesn't correlate in any way to the residential property sector, so falling values aren't anticipated within this sector. Like fixed interest, this is an important lower-risk portfolio component.

Equities are quoted stocks and shares in different markets such as the UK, North America, Europe and the Far East. This is the most risky element of any portfolio but it's most likely to produce the highest returns; similarly, it could also produce the highest losses. Markets have been volatile over the past few years, but the present low-inflation environment is ideal for equities.

Step 4 Choosing appropriate funds

Once you decide on the overall asset allocation, it's a simple matter to choose funds (within a pension, ISA or other wrapper) which reflect this. The overriding factor of this planning is that your strategy should faithfully reflect your attitude to financial risk. Next month, I'll look at funds and risk in more detail. But, there's one final and very important step.

Step 5 Review

You should review your plan (with your adviser, if you wish) at regular intervals to make sure it's still appropriate to any changed circumstances or objectives. This also gives the opportunity to weed out any poorly-performing funds, but if the strategy is soundly established, and reflects your attitude to investment risk correctly, it shouldn't require more than the occasional 'tweak' to keep it on track.

Louis Letourneau, MA is an experienced independent financial adviser (IFA), specialist in financial planning and wealth management. He founded Rainbow Finance in 1995 and has consistently challenged financial companies and Government on their attitudes to gays, lesbians and same sex couples and was instrumental in the Inland Revenue to changing its guidance notes to recognise unmarried couples in pension benefits. His work has also resulted in life insurance companies starting to relax the discriminatory underwriting criteria toward gay men and people living with HIV. He was a founder of the Rainbow Research Project which surveys and educates private pension schemes in how they recognise unmarried couples on death benefits. He was also a founder member of the Stonewall Immigration Group (which campaigned for Immigration rights for same-sex couples, achieving a significant victory in April 1997) and helped set up the gaypartners.org initiative with gay.com in early 2001, campaigning for same-sex partnership rights. He speaks regularly on national and local radio.

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