



Last weekend was a pretty dreadful one for world financial markets. First of all, XL Airways went bust, leaving tens of thousands of holidaymakers out of pocket and without their long-awaited holiday; in many cases without even a flight home. Then on Monday morning Lehman Brothers, a large US bank, went bust (filed for Chapter 11, as it is technically called). Financial markets around the world have, understandably, reacted by plunging downwards, and investors, equally understandably, become nervous at such times.

Once again, I find myself writing to explain events totally beyond the control of any of us, and to try to reassure clients that the world is not about to end. It would be foolish and disingenuous of me to try to pretend that all is well and that everything is rosy in the world of investing, but it is vitally important to persuade you that the very worst thing you could do now is panic.

What difference will it make to you, now and in the long run?

Right now, I would contend that the current situation makes not a lot of difference, in practical terms, to you. As long as you are still in receipt of income, whether from a job or a pension, you can pay the bills: food will still be on the table, you can still clothe yourselves and your children, and there is still a roof over your head. You can still put fuel in your car; if you feel like it, you can have a meal out next weekend. Ask yourself: is there anything in your daily life which you were able to do before last weekend that you can no longer do?

Your financial plan was constructed taking account of your short-term needs, whether this was to be provided by cash deposits or income, so – barring the unexpected – you should not have to dip into your long-term financial planning funds. Ergo, the current crisis has little or no immediate, practical effect.

There are exceptions to this, of course. If anyone has lost their job as a direct consequence, this will, obviously, have an immediate, direct, negative impact. If this has happened to you, please contact me so we can discuss what action needs to be taken.

Also, if you are trying to move home, it is much more difficult to secure mortgage finance than it was a year ago, and the current problems are not helping this. Rather than looking at this as a problem, I would encourage you to think about it as an opportunity. The so-called credit crunch is going hand-in-hand with falling house prices (it is hard to differentiate between cause and effect) and so if you can wait a while – and it might be a year or more – the house you are looking at now, or one very like it, may very well be available at a significantly cheaper price than today. Even if you are moving home and are worried about the value of your house falling, consider that there may be a relative fall in the price of the new house, but your income is unlikely to fall in pro-

**Figure 1: House affordability**

	Today	If prices fall 20%
Existing house value	£ 250,000	£ 200,000
Existing mortgage	-£ 100,000	-£ 100,000
Equity	£ 150,000	£ 100,000
New property	£ 350,000	£ 280,000
<b>New mortgage</b>	£ 200,000	£ 180,000
<b>Joint income</b>	£ 50,000	£ 50,000
<b>Income multiple</b>	4	3.6

portion, and your mortgage will be same or maybe smaller, so the whole operation is likely to be more affordable – Figure 1 gives an example.

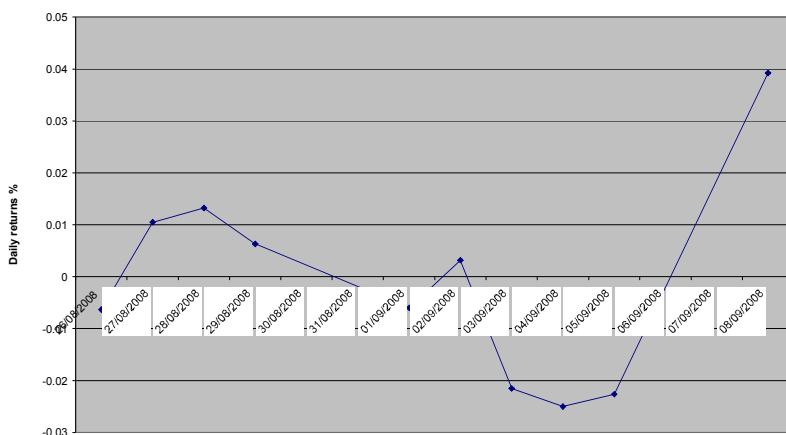
Your financial plan was built with the long run in mind. By “long run”, we mean five years or more. A certain level of volatility is assumed, because a decent level of long-term return requires that a level of risk be taken. If you are worried about the safety of your capital, you could put your money in the bank, where it would be guaranteed at least to the level of 100% of the first £35,000, but please consider two things.

1. You would be locking in a loss from which you could never recover. By staying in the market, you will benefit from any future recovery, whenever it happens.
2. You will be removing any realistic chance of achieving your financial objectives, as inflation will almost certainly increase the cost of living faster than after-tax growth of your savings.

Two questions spring to mind: could we have done anything to predict what happened and taken avoiding action, and, is there anything we can do now.

Cast your mind back a couple of weeks, to the date that the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), the two big US loan underwriters, were taken into US Government ownership. On the run-up to that, there were mutterings about the inability of those two huge institutions to continue, much the same as there have been rumours about Lehman Brothers over recent days, both that they were in trouble and that they would be bailed out. Figure 2 is a chart of the UK stockmarket over that period. Would we have been right to recommend clients

Figure 2: Chart of FTSE 100 Returns



to sell the equity part of their portfolio on the Friday in that period? With hindsight, clearly not, as that would have meant losing out on the steep upsurge when Fannie & Freddie were semi-nationalised. With hindsight, it would have been better to be out of the market from last Friday night, but what if Lehman Brothers had agreed a rescue package? The effect would have been much less, and possibly even positive, as with Fannie & Freddie, and investors would have lost out.

History offers abundant evidence that market economies are resilient. The world will find a way to manage its financial affairs without the advice of Lehman Brothers, and Merrill Lynch. The key issue for investors is to make sure their financial future does not get derailed by events at a handful of firms, and that their portfolios are properly positioned to capture all the rewards the markets have to offer when the next recovery begins. Recent events have provided an unusually harsh lesson of the importance of diversification. In a matter of days, shareholders of three financial giants—Fannie Mae, Freddie Mac, and Lehman

Brothers Holdings—have seen their shares plunge into the penny-share category. A fourth, AIG, is scrambling for survival, although it appears to have done so, as seems to be the case at HBOS. For well-diversified investors, the financial damage associated with these firms has been minor. Four or five years from now, these investors may have a difficult time remembering what happened and when.

However, for those with investments concentrated on a few companies or even one or two asset classes, these events are a financial tornado inflicting potentially irreparable damage. When times are good, the risk of a concentrated portfolio often appears extremely remote.

What now? Is there anything we can do? Yes! Sit tight, stay disciplined, rebalance your portfolio to stay within your risk tolerances. The evidence is that investors and their advisors do much more harm than good by attempting to time markets. Investing is for the long term, five years plus. We build your financial plan to give you confidence that your finances are on track, we ensure that you have sufficient cash in the bank to see you through difficult investment conditions, and the very worst thing to do right now would be to jeopardise long-term financial plans by taking short-term emotional decisions.

The events of 2008 demonstrate the importance of getting a few big issues right: financial planning for the long term, matching asset allocation to risk profile, and diversifying as widely as possible.

The Navigator name was chosen for a reason. My job is to find out where you want to go and to help you get there, avoiding the rocks & shoals in the way. I cannot prevent hurricanes, but I can encourage you to ride them out and take as many precautions as possible towards seeing that you come out the other side in good shape to take you to your financial destination.

