



The Truth about Investment

As a recruitment specialist in private banking (which largely means asset management), the Somers Partnership has to keep abreast of developments in investment thinking. Conversations with investment academia have revealed some worrying home truths which cut across much of the received wisdom of the asset management industry. First economic forecasting is impossible, as proclaimed by Mervyn King, the Governor of the Bank of England, who admitted he had no idea what was going to happen the following day let alone the following month. The vast resources of the IMF, OECD, Bank of England or the Federal Reserve Board have evidenced no ability to forecast macro-economic developments. But the good news is that this does not matter because there is only the most tenuous link between financial markets and macro-economic developments. The supposed correlation between positive stock market performance and positive economic growth is based on no empirical evidence, though this is the core supposition of every investment committee in the City. There are two further disturbing conclusions. There is no evidence that asset managers can market time. Nor can they find alpha, that elusive contributor to stock market returns divorced from market returns overall. The sad conclusion is that much of the asset management industry is built on sand. It is assumed that diligent, well-educated and inspirational strategists, economists, analysts and fund managers can predict the future course of financial markets. All the evidence suggests that ninety-nine per cent of them cannot.

At the Somers Partnership we discuss such matters at our advisory board, of which the Chairman is Roderick Collins, a founding partner of Hasley Investment Management. Hasley is modest about what an asset manager can achieve, eschewing the impossible market directional bets, while favouring reversion to mean (i.e. the assumption of inter and intra asset class relativities reverting to their normal historic level) and trend following, the phenomenon that persistent trends develop in most financial markets, which are sufficiently evident to provide a formulaic alternative to the discredited judgemental approach to asset management. Indeed during the Spring the Somers Partnership will host a seminar, delivered by two Professors of Finance, and a drinks party, at which some of these iconoclastic ideas will be discussed. We very much hope that our friends will be able to attend. Indeed it might prompt some private banks to reassess their investment proposition.

Roderick Collins, Co-Founder, Hasley Investment Management
roderick.collins@hasley.co.uk www.hasley.co.uk

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