THE SCANNER

MULTI-ACT
Built by investors for investors

Future-proofing wealth: **Constructing a portfolio for posterity.**

Creating a multi-generational diverse portfolio for posterity

Change is the only constant, and only those that can adapt to change will both survive and thrive. Nowhere is this more evident than in the investment ecosystem. The economic, political, and financial environments undergo periodic change. As economic cycles go through cycles of expansions and contraction, they engender opportunities for wealth creation while breeding risks that can have an adverse impact on portfolio resilience and growth. Thus, for families, institutions or individuals, keen on preserving their wealth for posterity while ensuring that the portfolio at minimum generates inflation-beating growth, it becomes essential to create a portfolio that can survive and thrive through these cycles. While it is challenging to have a view for the long-term, in this case at least 100 years investors can create a resilient portfolio that can harness the opportunities that present themselves during the boom period while remaining relatively unscathed during the bust periods.

Surprisingly, 100 year cycles with some rotational regularity between the investing "seasons" have been present for at least the last 4 centuries since financial records have been maintained.

Going beyond 60/40

Diversification is perhaps the main foundation for resilience. The most important risk in long horizon investment is tail risk and diverse asset allocation is the key to mitigating this type of risk. There is enough evidence to establish that the traditional 60/40 ratio does not protect your portfolio against tail risk in these long cycles. Multi-Act believes that a well-diversified portfolio, still primarily invested in equities, that is optimally distributed across both asset classes as well as geographies is well-positioned to weather market volatility, providing downside protection with an opportunity to harness the upside benefits of equity investing. Below is what we believe is one of the useful approaches to achieving optimal diversification.

Approach 1: Build a 25:25:25:25 portfolio

In such a portfolio, the following asset allocation is recommended:

25% in deep value equities to safeguard against "permanent loss of capital" during deflationary periods

25% in fixed income and /or utility stocks to ensure low downside and quasi fixed income like returns in securities such as ports, airports, toll roads and infrastructure assets

25% in monetary assets such as bullions and gold miners for credit risk free currency proxies

25% in commodities vital in the present but also of growing importance in the future such as clean "green" energy, uranium, and due to the EV revolution, copper, and nickel that are estimated to be the next big metals

Approach 2: Diversify across geographies, sectors, and stocks

70
60
50
40
30
20
10
0
100
200
300
400
500
600
700
800
10%
15%
20%
12%
10%

Alternatively, asset allocation can also be more nuanced as investors focus on selection across geographies, sectors, and individual line items of stocks. The range of line items can vary depending on personal preferences, however, selecting companies that will survive the timeline is imperative. Parameters for selecting line items should ideally be those that score highly on Quality & Value, but also that exhibit Momentum (fundamental or balance sheet improvement).

It is important to note that the 100-year portfolio can adopt an active or passive (ETFs) approach, depending on the family office's style of investment. The overarching philosophy behind building a 100-year portfolio is to ensure that your financial assets should perform relatively better during periods of financial and market distress. This means that while some of the investments might seem boring and provide low returns during periods of the boom, they must still be considered. A multigenerational portfolio should be built for difficult market conditions. History has shown that difficult market conditions often arise when least expected and just when market participants believe that good times are going to last forever.

Q&A

Prashant K. Trivedi, CFA

Founder & Non-Executive Chairman, Multi-Act

What is the premise behind creating a 100-year portfolio?

Families as well as wealthy individuals are tasked with preserving wealth for multi-generations while ensuring that they can optimize the return on their capital. This means that they need to embrace a long-term outlook and ensure that their portfolio can grow at inflation adjusted rates across market, economic, and geopolitical cycles. Thus, portfolio construction and assessment should be done through a long-term lens. A key tenet for creating a 100-year portfolio is to eschew the recency bias and accept that an investment portfolio needs to be positioned for change, i.e., it should be able to optimally navigate market cycles and changing environments while staying independent of the investment manager's ability to effectively time the appearance of economic and financial distress and the length and duration of market declines.

While diversifying globally, should investors focus on individual companies or should they evaluate the macro-economic environment as well?

Diversification is perhaps the main foundation for resilience. A well-diversified portfolio that is optimally distributed across both asset classes as well as geographies is well-positioned to weather market volatility, providing downside protection with an opportunity to harness the upside benefits of equity investing. To that extent, it is important to ensure that you are not just tethered to the domestic economy but are able to establish ideal exposure across global economies. Inarguably, macro-economic parameters will hold sway as you identify the countries to which you want to create exposure. However, sectoral as well as individual stock selection is equally important since the more nuanced opportunity stems from making the right selection. The choice of Quality, market leadership and attractive economics is higher the less geographic constraints that investors impose on themselves.

How can investors create an all-season portfolio?

To construct a portfolio that can survive and thrive through multiple economic and geopolitical cycles, one needs to combine assets that do well during the secular boom, i.e., risky assets, with assets that perform well during periods of instability, i.e., defensive assets. At the same time, investors need to ensure that the defensive assets do not exact too high a cost during any secular boom by undermining the portfolio's ability to optimally harness the benefits of the secular boom.

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