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Keep calm and carry on investing: As study reveals investors are sticking to cash, what's the best approach in stormy markets?

- A quarter of wealthy investors hold more than 50% of their portfolio in cash
- Cash savings offer a great deal of peace of mind amid volatile markets
- But history has shown that investing can yield better results over the long term

A quarter of high-net-worth investors currently hold more than 50 per cent of their wealth in cash savings, according to new research.

The study, by Rathbone Investment Management, found that a further 35 per cent of wealthy individuals in a sample of over 1,500 UK adults said they keep between 26 and 50 per cent of their money in cash savings.

Robert Szechenyi, investment director at the asset manager, said the move to cash is largely down to the economic and political uncertainty currently at play as a result of Brexit and the US/China trade war.

Cash offers a great deal of peace of mind in volatile markets as its value doesn't fluctuate, something that is particularly important to those approaching retirement.

But over the long term, the buying power of cash is usually eroded by rising price inflation, so it's only truly suited as a short-term home for your money.

History has shown that investing can yield better results than cash savings over the long term.

For example, an investor who bought in before the market peaked at the start of 2007 would have suffered the worst of the financial crisis' nosedive in share prices.

Had they ridden out the storm they would now have turned £10,000 into £20,197 - a 101.97 per cent return to September 2018, according to Click & Invest analysis.

By contrast, someone who stayed in the safety of cash savings over the past decade would have earned 17 per cent in total over that period.

Getting a return on your cash

If you're committed to keeping a significant proportion of your wealth in cash then there are a few golden rules.

First things first, keep cash short-term otherwise inflation will erode its value.

Secondly, be aware of how much cash you hold in each banking institution and ensure it doesn't go over the Financial Services Compensation Scheme limit of £85,000.

Thirdly, don't let cash languish in accounts that pay desultory rates. Savings rates may not be great at the moment - in fact they're pretty dreadful - but there is increasing competition and you can find the odd inflation-beating rate if you're prepared to lock up cash for a few years.

ICICI Bank is currently offering the best buy easy-access savings account paying 1.55 per cent, topping the Marcus by Goldman Sachs account by 0.01 per cent.

The best five-year fixed rate is from Sharia-compliant challenger bank Gatehouse at 2.68 per cent available through Raisin UK. Gatehouse Bank adheres to a strict ethical code of Sharia, meaning they won't invest in gambling, alcohol, tobacco or arms.

An alternative to a straightforward savings account is to invest in Premium Bonds from NS&I.

Every month more than a million prize-winning Premium Bond numbers are chosen at random and two bond-holders pocket £1million each. Other prizes range from £25 to £100,000.

More than £75billion is invested in Premium Bonds, which typically have a return of 1.45 per cent although there's no guarantee that you'll win.

Your capital is protected as it's a Government-backed provider but the amount you can invest in Premium Bonds is now capped at £50,000.

How to invest in stormy markets

Ideally, even when markets are rough it is still worth keeping your money invested.

But how should nervous investors broach moving their money from cash saving into invested assets amid stormy markets?

We asked three wealth managers to outline what they think could be the best approach to take.

Patrick Connolly of Chase de Vere said:

Many investors like to think that they can time markets so that they invest in shares when stock markets are rising and then move into cash as markets peak and start to fall.

However, the reality is that very few - if any - people can consistently get these calls right and those who try often lose money.

Everybody should hold some money in cash, at the very least to cater for any short-term emergencies, and they should hold more if they are nervous about investing or simply don't need to take risks to achieve their financial goals.

However, too many people have too much money in cash and as a result they are unlikely to generate strong long-term returns.

The problem is that with volatile stock markets, it's difficult for them to know how and when to invest.
Investing should be about achieving returns that are consistently better than cash and not about taking excessive levels of risk.

A sensible approach is to drip feed cash into your investments, rather than investing everything at once. This helps to mitigate the risk of market timing and means that if markets fall you simply buy at a cheaper price next time, thus reducing your average buying cost.

Also, for many investors, a good strategy is to hold other investments, such as fixed interest and property, alongside shares.

This helps to spread risk and means that you have some protection in your portfolio if stock markets fall further.

Ben Yearsley of Shore Financial planning said:
The first thing I would do is decide how much of my cash I was comfortable investing and then what sort of return I wanted from it.

The second step is to decide what to invest in – be it bonds, equities or property.

It is better to phase your cash into your chosen investments over a period of time, say between six and 12 months, to reduce the timing risk of entering the market.

However you have to be disciplined with phasing and ensure you buy when markets go up and down. This approach ensures you shield your investments from short-term market movements.

Remember, it isn't just the return that's important but also the capacity for loss. In other words, how much are you prepared to see your investment go down in the short term.

Are you comfortable with your portfolio falling 10 per cent in value in the short term? What would you do if it did? Likewise, if it rises 10 per cent in the short term what would you do?

If you can't bear this kind of short-term movement then equities aren't for you and bonds and property may be more appropriate or even managed funds.

When deciding a portfolio, always ensure you have a spread of investments. In the equity world this could be ensuring that you have small and large companies as well as, say, UK and overseas holdings.
In the bond world, this could be ensuring you have investment grade alongside some government bonds.
The reason for having a spread as to ensure you aren't over exposed to one specific risk.

Martin Bamford of Informed Choice said:
Moving from cash to invested assets is a big leap, especially for more cautious investors.

The best place to start is understanding whether you need to invest the money in order to achieve your financial goals, and if so what level of investment return is needed to meet those goals.

When we work through the financial planning process with clients, we often find there is no financial need to invest their cash reserves; they can keep the money safely in cash and still achieve their goals in life.

Nervous investors need to have clear goals and a framework in place before they start investing. This framework can be documented in an investment policy statement.

It's also important to take the long-term view of any investment you decide to make, riding out short-term volatility rather than trying to sell before markets fall.

A first-time investor should have a well diversified portfolio, invested across a variety of mainstream investment types including equities, bonds and property.

They should absolutely avoid any fad investments, including cryptocurrency.

Simon Lambert, This is Money editor and author of the Minor Investor column, says:
As an investor I understand that investing is a lifetime game and that there is truth to the old adage that it's time spent in the market that matters, not timing the market.

I recently wrote about the interesting words Fundsmith manager Terry Smith had on this in his letter to investors.

Nonetheless, concerns that the market may take a big dip will always nag investors, so what can we do if this kind of thing worries us?

One option is to adopt the Buffett mantra of being greedy when others are fearful and buy more while the stock market is on sale.

Understandably, if your worry is that shares will suffer a 30 per cent fall and we’re only down 10 per cent now, this may not be your chosen course of action.

Instead, you could look at shifting your investing style to adapt to a more volatile world.

Traditionally, the way of doing this would be to up your bond exposure - a cheap easy passive option for that would be a Vanguard Lifestrategy fund further up the bonds to shares scale.

But the bond market is a dangerous place to tread, thanks to mass purchases through quantitative easing warping prices, so I'd prefer an active approach.

Working on the basis that I'd still want to be holding shares for their better chance of a higher total return, my thoughts are that it's best to hunt in two areas:

Managers backing things that are cheaper, with a value or contrarian stance, thus providing some insulation against the disappointment that can send highly-rated growth stocks crashing.

Funds or investment trusts with a defensive outlook are the other option. Among these, on my list to consider are Personal Assets, which I bought earlier this year and we look at here, and Ruffer, whose co-manager I interviewed for the Investing Show, other names include Capital Gearing and RIT Capital Partners investment trusts, while on the fund side, those such as Baillie Gifford's Managed Fund, Premier's Multi-Asset Growth & Income, or similar, may be worth a look.

All of these trusts and funds adopt a cautious approach, balancing their investment in shares around the world with bonds and other assets that should bolster performance when the going gets tough.

None are likely to match the stock market's performance over recent years, when conditions have been benign, but they do tend to have enviable records when markets fall.

Capital Gearing, for example, made money in 2008 at the height of the financial crisis, while Personal Assets fell just 3.4 per cent that year before rising 19.4 per cent in 2009 and says, 'its investment policy is to protect and increase (in that order) the value of shareholders' funds per share over the long term'.

Ruffer managed to position itself to not only dodge the stock market falls of 2008 but rise 23 per cent that year, by holding a large amount of the portfolio in index-linked bonds.