MONTHLY INVESTOR

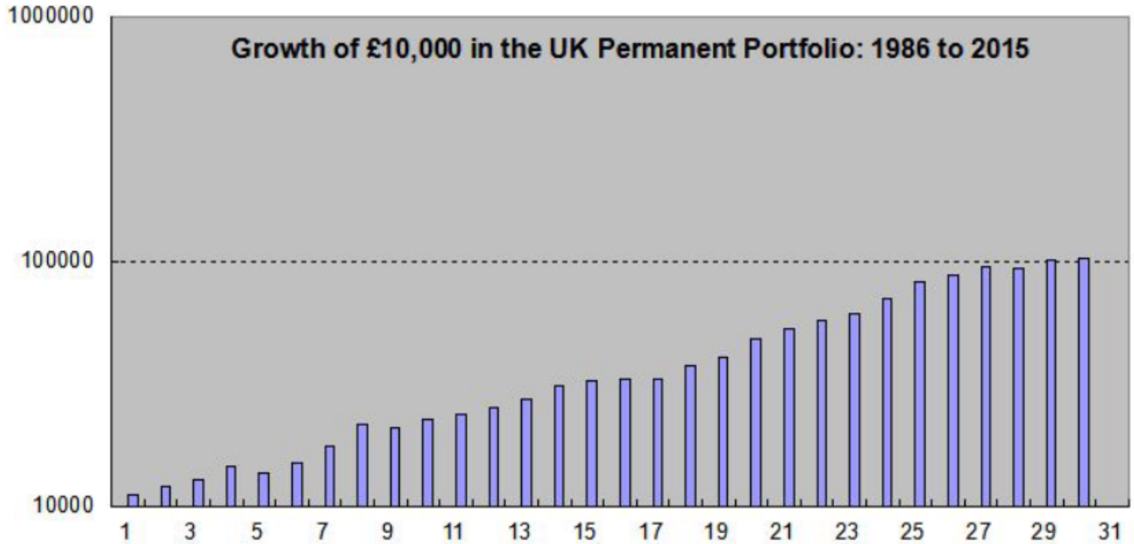
Permanent Portfolio UK

The “Permanent Portfolio” was devised originally by Harry Browne for US investors based on his own experience as an investment advisor. He realised that complexity in portfolio design was unnecessary and that frequent trading damaged returns. He intended it to be a 'set-and-forget' portfolio requiring minimum work yet capable of providing long-term returns similar to the overall market with much lower volatility. The holy grail of investing!

The actual performance of the Permanent Portfolio over several decades is consistent with his objectives. From 1970 - 2015, the annual average USA return was 8.35% which is similar to that of the S&P500. The impressive thing is the lack of volatility compared with the stock market. Only a few years have seen losses, and those were low single digits. What about 2008? Authors differ on the figures, some quoting a gain of about 2% and others quoting a loss of about 2%: but either way that beats the market by a very wide margin. (N.B. Figures quoted may differ slightly in published articles due to differences in methods used in the calculations, but the overall picture is consistent.)

These are returns for the USA market where the PP is relatively well-known and reported. It is much less well-known in the UK yet the results have been just as good for our market and currency. A few authors have published returns for the UK market showing similar results. Further papers are available under the pull-down menu 'free material'. We have calculated returns for a UK version using the FTSE250 in place of the FTSE100, which most commentators use. We use FTSE250 at Monthly Investor because it has massively out-performed the FTSE100 in recent decades. During the 30 years 1986 to 2015 the UK Permanent Portfolio based on the FTSE250 returned a Cumulative Annual Growth Rate (CAGR) of 8.1% and a worst year loss of -3.7%. The real return above inflation averaged over 5%. Since 1996 the worst annual loss has been -0.7%.

Years	**CAGR**	**Worst year**	**Real return (gain above inflation)**
1986-2015 Only 3 losing years in 30 (-3.7%, -2.2%, -0.7%)	**8.1%**	**-3.7% (1990)**	**5.1%**
2006-2015	**6.8%**	**-0.7% (2013)**	**5.0%**
2011-2015	**3.2%**	**-0.7% (2013)**	**1.9%**



The Permanent Portfolio is amazingly simple, consisting of just four equal holdings of gold, bonds, stocks and cash. Harry Browne's idea was that one or two of the holdings would out-perform whatever the economic and market conditions. The out-performing asset(s) would compensate for any losing holdings. The performance over decades seems to support his view. Most importantly for investors saving for retirement, or already in retirement, the gains have been 'real' – i.e. they have been greater than the increase in the cost of living.

Browne designed the portfolio to cope with four recurring economic scenarios:

• Inflation - Gold and precious metals outperform
• Deflation - Bonds outperform
• Prosperity - Stocks outperform
• Recession - Cash outperforms

25% is allocated to each of these asset classes using just four instruments. Once invested the portfolio is rebalanced once a year, reducing the assets that have climbed well-above 25% back to that number, and buying any well below 25% to bring them back to that number. This has the merit of 'buying low and selling high', the obvious route to investment gains but one which few investors manage to achieve.

Permanent Portfolio compared with the 60/40 portfolio?

You may be wondering about the well-known 60:40 portfolio, comprising 60% allocated to a stock market index tracker and 40% to bonds – no cash or gold. How does the performance of the Permanent Portfolio compare? William J. Bernstein wrote an article in 2010 titled 'Wild about Harry', in which he compared the two using US market data back to1964. The portfolio of 60% stock index, 20% long-term bonds and 20% T-Bills would have returned 8.8% per year with volatility of 11.3%. Over those 45 years, the Permanent Portfolio, rebalanced annually, yielded an average of 8.5% per year, with volatility of 7.7%. The 60/40 gave very slightly greater gain than the Permanent Portfolio though at the cost of 46% higher volatility. Therefore, the inclusion of gold in the Permanent Portfolio led to only a slightly lower overall return but gave the advantage of significantly less annual volatility. Our figures for a UK Permanent Portfolio show a similar outcome.

What about the devastating effect of inflation on retirees in the 1970s? Inflation is the big financial fear of all retirees. Bernstein reported that the Permanent Portfolio performed well during the high inflation years 1973-1981. In fact, over the past 30 years the PP returned about 9.9%, while inflation has averaged 4.5%. How many fund managers or index trackers have achieved that? His article is well-worth reading. It is available under the 'free materials' tab

Too conservative?

Despite all this, some authors have stated that the Permanent Portfolio is too conservative for long-term investors trying to build wealth for their retirement. This criticism ignores the fact that few private investors or indeed fund managers achieve comparable returns long term. They almost certainly do not achieve the low volatility that the Permanent Portfolio has historically shown. But if you want to try for higher returns, we also offer subscribers our proprietary Seasonal Portfolio methods and our Trend Following methods.

Another criticism made by US writers is that the income stream from the PP may be inadequate for retired investors. UK-based investors are better placed due to the higher dividends generally made in this country, with payments available from two of the four components - the FTSE250 share tracker and long term gilts. We also offer to subscribers our proprietary 40:40:20 portfolio which exhibits similar performance with higher income stream.