Insurance: Better to buy ten years too early than one minute too late

As stock markets move off a very successful 2024, it is fair to say everyone is daring to hope 2025 will be another great year. Whilst we share that sentiment and are invested to capitalise on another positive year, history reminds us that it pays to be cautious when sentiment is riding high. Given that, the core tenet of this note is something simple - insurance. You wouldn't countenance the idea of driving a car without insurance, mainly because it's illegal. Why? Perhaps because at its core, events which we need insurance to cover can be destructive enough that, without financial assistance from a 3rd party, people wouldn't be able to put their lives back together. Ergo, it's important to cover oneself. It's largely the same when it comes to someone's portfolio. Usually protection is called "hedging" as in hedging one's bets. More's the pity, much of this hedging world sits behind the exorbitantly expensive curtain of the "hedge fund" industry and doesn't find its way into the portfolios of the classic investor. But for those who know where to look, there are some investments, which we can all buy, that focus on going up in value when the stock market has a wobble or even crashes. Amundi's Volatility fund is one such investment. It seeks to, through the use of derivatives, to react positively to stock market volatility. Simply speaking, the fund makes its money when the stock market isn't delivering. In fact, the best performance periods for this fund are when the stock market is selling off quite hard. Over the first three months of

2020, when COVID hit our shores, investors in the UK's FTSE All-Share Index saw their portfolios drop 26%. The Amundi Volatility fund in that same period went up 36%. Despite being an extreme scenario, it does illustrate my point quite nicely about the resemblance to an insurance product. Considering TAM's entire investment message oscillates around creating "sleep safe at night" portfolios of high quality, low volatility investments, it makes sense that these types of insurance investments are things we put a lot of stock in, at certain times. I add this caveat because when the market is rallying, which it tends to do a lot, these investments work against you. Therefore, there is an art to establishing the right time to buy. So, now we have postulated on the idea of investments as insurance policies, against the probability of other investments going wrong. Is now a good time to take out a market policy? Well first thing's first, with the market doing so well in 2024, volatility was subdued, and as such, it was cheap to buy volatility strategies as we went into 2025. Recently, headlines around the new AI contender "DeepSeek" sent Nvidia stock into one of the largest sell-offs in stock market history. This created the exact market volatility to which this fund needs to perform. Whilst TAM didn't see this headline coming, we had agreed that there was an increased likelihood of something happening. This saw us put an investment into the fund earlier in January for a bit of client cover. The talk of market volatility all sounds a little morose, so I want to remind readers that talking about insuring a portfolio does not mean that we expect a bad market ahead. Afterall, taking out car insurance doesn't mean you intend to go and have a crash. The world remains on a growth footing with improving earnings margins, better outlooks and stable economic growth. The way we see it, buying investment insurance allows us, on the other side of a portfolio, to remain fully invested into the things that have the potential to go up. However, with a market which did so well in 2024 - largely off the back of just 7 huge tech companies alongside two global conflicts, inflation not quite yet beaten, governments taking on more and more debt and now an unashamedly mercurial US president - it feels like a prudent time for a modicum of insurance. After all, making these types of investment decisions on your behalf is exactly what any good discretionary fund manager should be evaluating as we continue into 2025

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