Morgan Stanley

PRIVATE WEALTH MANAGEMENT

Andrew Schultz |My Thoughts - Ballast, Dislocation, Disputation

There are many investment styles, with many names, that may mean different things to different investors. In this article, I will discuss three investment styles and how I may or may not recommend employing them based on an investor's goals, needs, risk tolerance, and time parameters. Let me be clear, there are many ways to skin the cat and these are my opinions and not necessarily those of Morgan Stanley or other seasoned investment advisors. I call these three investment styles Ballast, Dislocation, and Disruption.

The idea behind ballast investing is to try to create a portfolio of investments that have minimal volatility, maximum diversification, that attempt to go slow and steady down the middle with hopefully consistent single-digit returns. A portfolio that rarely beats any stock indexes but rarely declines as much as stock indexes might in drawdowns and that still may be able to provide returns when stocks or bonds may not. This may be achieved through what I define as proper diversification across many asset classes and many investments that are tailored to the investor's needs, goals, risk tolerance, and time parameters. For many investors, this is typically how I would advise investing the bulk if not all of their capital. Slow and steady, as far as I am concerned, for most investors may be the best way to "win the race."

Given that the bulk of a portfolio is invested in the ballast style, there are investors that like to take a portion of their portfolio and be more aggressive. Most investors as of late have been handsomely rewarded by just adding that capital into a few mega-cap technology names and riding the momentum wave. I am not sure if that can continue and I instead advocate two other types of aggressive investment styles that I believe can have the potential of long-term upside returns that may outpace many indexes and mega-cap tech names going forward. I call these two styles Disruption and Dislocation.

Disruption, to me, means finding businesses whose product or service will be a game-changer and if the stars align will potentially see huge growth in revenue and demand that will then reflect in a rising share price. Past and present examples may be electric vehicles, smartphones, 5G, AI, fintech, or renewable energy. Investments into disruptive technologies can be highly volatile and are best to be done, in my opinion, in diversified portfolios into these various spaces. Within these spaces, I believe there can be clear winners and losers which is why I tend to like individually managed portfolios that are concentrated and not ETF's. If and when an investor gets bets right in this space large returns, to the tune of 5x to 10X can potentially be achieved. On the flip side, when investors get bets wrong in this space or sentiments change, large drops in value, sometimes better than 50% or even losing everything, can happen.

Dislocation, to me, means investing in businesses that have had their share price decimated by either external factors or some bad decisions within the business that has caused major short-term share price reduction. Examples could be the major drop in energy prices at the beginning of the pandemic, Financial stocks coming out of the 2008 crisis, Asian e-commerce, and technology names now. The key thing to note when bottom fishing is just because something is cheap does not mean it cannot get cheaper and just because something went way down does not mean it just turns around and goes way up. A lot of homework must be done before making dislocation investments and many times one has to hold their nose and buy-in when things seem at their worst. If a business is solid, has strong growth prospects, and may be temporarily down due to external reasons, and there is a feeling those external reasons may improve in the future, it may make a good investment. These investments may have a large upside with potentially more limited downside than an overvalued momentum play. But let's be very clear that this space can be highly volatile and if you get your bets wrong further pain can ensue.

As I had stated earlier, I believe most investors should have the bulk of their capital invested in the ballast style. There are times though, where I believe for some, it makes sense to take full advantage of disruptive and dislocated investment opportunities. In my opinion, the best way to learn what to allocate to where is with a well-experienced investment advisor.

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Principal value and return of an investment will fluctuate with changes in market conditions.