

Money Wise UK

Growing Together With Integrity And Respect



**Independent Thinking:
The Power of Blending -
A Smarter Approach to
Investment and Research**

GROWING TOGETHER WITH
INTEGRITY AND RESPECT



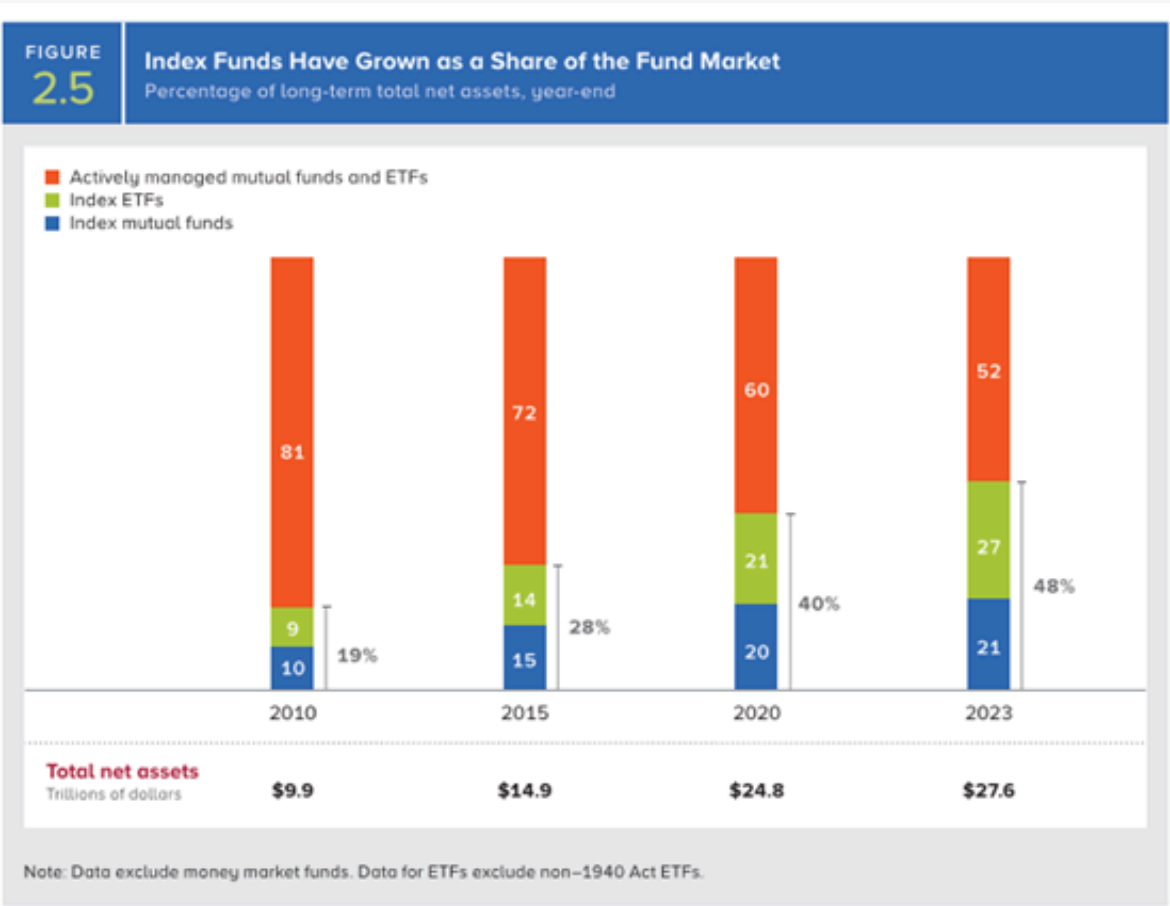
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Growing Together With Integrity And Respect

How Combining Strategies, Methodologies, and Expertise Drives Superior Outcomes

Investing has always been complex, yet the rise of index investing has led to a growing perception that it is becoming increasingly straightforward. The Investment Company Institute’s 2024 Fact Book highlights this trend, showing the substantial shift toward passive investing.



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How Combining Strategies, Methodologies, and Expertise Drives Superior Outcomes

The reasons behind the dominance of index investing are threefold:

- Cost-efficiency – Index funds typically offer lower fees than actively managed funds.
- Performance vs. Active Management – Studies such as SPIVA's long-term data challenge whether active management consistently delivers outperformance.
- Transparency – Passive strategies provide investors with a clear view of their holdings, thereby reducing concerns about hidden risks.

However, while index investing may seem to simplify decision-making, the reality is more nuanced. Rather than reducing complexity, the shift toward passive strategies has introduced new challenges, particularly in terms of concentration risk.

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How Combining Strategies, Methodologies, and Expertise Drives Superior Outcomes

For example, consider the MSCI World Index. Despite being labelled a "global" benchmark, it is heavily skewed, with 72.92% of its exposure in the US—effectively making it a US-dominated fund with limited diversification. Similarly, within the index, a handful of stocks hold an outsized influence. The top 10 constituents comprise a significant portion of the index, creating risks for investors who assume they are gaining broad market exposure but are highly concentrated in a few dominant names.

TOP 10 CONSTITUENTS			
	Float Adj Mkt Cap (USD Billions)	Index Wt. (%)	Sector
APPLE	3,676.97	5.13	Info Tech
NVIDIA	3,064.29	4.27	Info Tech
MICROSOFT CORP	2,803.30	3.91	Info Tech
AMAZON.COM	2,005.20	2.80	Cons Discr
META PLATFORMS A	1,460.33	2.04	Comm Svcs
ALPHABET A	997.67	1.39	Comm Svcs
BROADCOM	884.88	1.23	Info Tech
ALPHABET C	865.66	1.21	Comm Svcs
TESLA	842.37	1.17	Cons Discr
JPMORGAN CHASE & CO	752.97	1.05	Financials
Total	17,353.65	24.21	

This leads to a typical investor temptation: chasing past performance. Strategies that have recently outperformed often attract more capital, while those that have lagged are usually disregarded—without a thorough understanding of the factors driving their results.

This paper examines why adopting a more strategic approach to blending investment styles, asset classes, and methodologies can enhance long-term outcomes. By diversifying across multiple return drivers, investors can better balance risk and reward.

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The Giants

In March 2024, a new index, The Giants, was introduced, comprising 23 stocks spread across three regional and sector-based indices:

- Magnificent Seven (US technology giants)
- Roaring Dragons (Top UK stocks)
- Granolas (European defensive leaders)

Performance Comparison Over 5 Years:

- The Giants Index: 21.71% p.a. return, with volatility of 13.84%.
- Magnificent Seven (US): 39.88% p.a. return but with volatility of 28.53%.

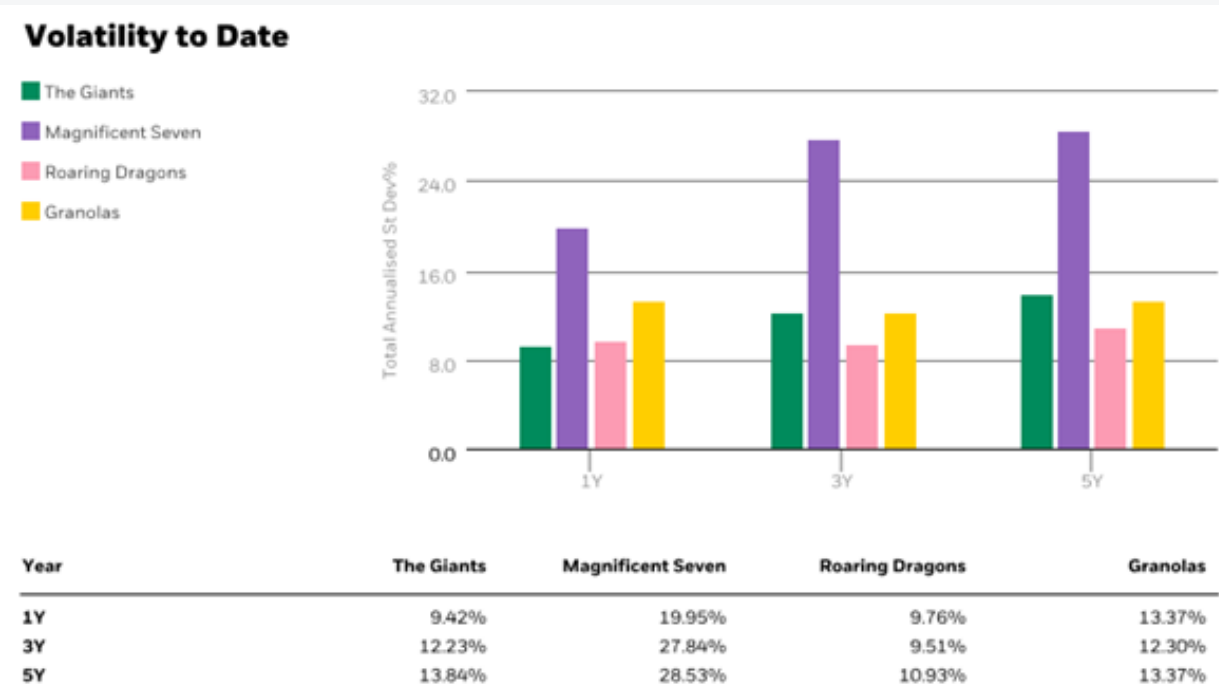
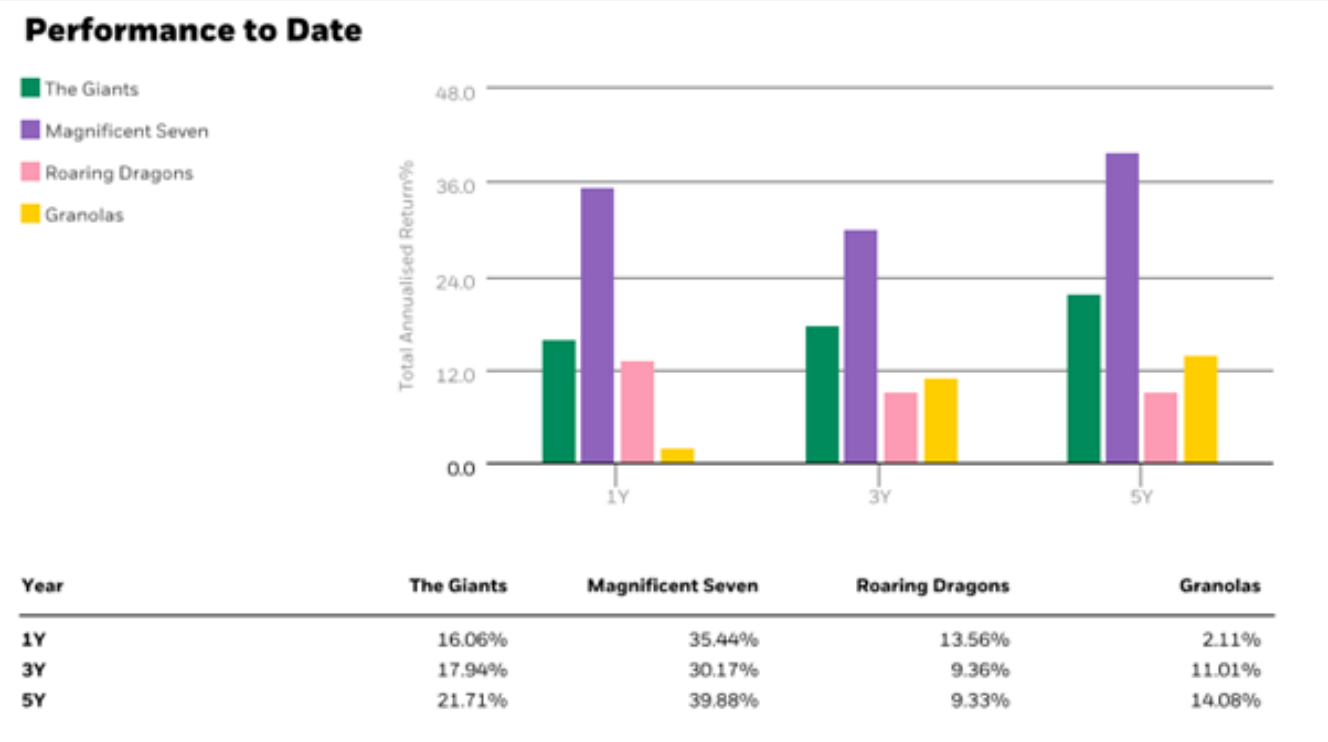
While the temptation might be to allocate purely to the highest-performing segment (the Magnificent Seven), doing so would expose investors to significantly higher volatility.

Instead, blending these three strategies yields a more balanced return profile, offering substantial long-term gains while mitigating downside risk.

A practical example of this approach can be seen in the multi-asset portfolios used by pension funds, where equity-heavy allocations are blended with defensive assets, such as bonds and alternatives, to create a more resilient portfolio.

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The Giants



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The Giants

Name	The Giants	Magnificent Seven	Roaring Dragons	Granolas
Equity	100.00%	100.00%	100.00%	100.00%
ALPHABET INC CLASS A A	4.40%	14.29%	-	-
AMAZON COM INC	4.40%	14.29%	-	-
APPLE INC	4.40%	14.29%	-	-
META PLATFORMS INC CLASS A A	4.40%	14.29%	-	-
MICROSOFT CORP	4.40%	14.28%	-	-
NVIDIA CORP	4.40%	14.28%	-	-
TESLA INC	4.40%	14.28%	-	-
DIAGEO PLC	4.30%	-	14.28%	-
BRITISH AMERICAN TOBACCO	4.30%	-	14.28%	-
ASTRAZENECA PLC	4.40%	-	14.28%	9.10%
LOREAL SA	4.30%	-	-	9.10%
LVMH	4.40%	-	-	9.10%
SAP	4.40%	-	-	9.10%
SANOFI SA	4.40%	-	-	9.10%
NOVARTIS AG N	4.30%	-	-	9.10%
ROCHE HOLDING AG	4.30%	-	-	9.10%
NESTLE SA N	4.30%	-	-	9.10%
LONDON STOCK EXCHANGE GROUP PLC	4.30%	-	14.29%	-
UNILEVER PLC	4.30%	-	14.29%	-
RELX PLC	4.30%	-	14.29%	-
ASML HOLDING NV	4.30%	-	-	9.10%
GLAXOSMITHKLINE	4.30%	-	14.29%	9.00%
NOVO NORDISK CLASS B B	4.30%	-	-	9.10%

The Power of Diversification

An equal-weighted allocation across these three strategies smooths returns, reducing extreme swings in performance. While no single approach will consistently outperform, combining multiple complementary strategies helps investors capture opportunities while managing risk more effectively.

A study by Morningstar (2023) found that portfolios blending US equities, European defensive stocks, and UK growth companies achieved a better Sharpe ratio than portfolios focused solely on high-growth equities. This highlights the benefits of blending different risk-return characteristics.

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What Is Blending in Investment and Research?

Blending goes beyond diversification across asset classes and regions –it involves integrating different investment styles and methodologies to enhance risk-adjusted returns.

For example:

- **Passive vs. Active Indexing** – While traditional passive strategies mechanically track an index, some systematic approaches, such as smart beta, adjust weightings based on factors like value, momentum, or quality.
- **Active-Passive Pairing** – A well-constructed portfolio might pair a broad global index fund, which has a high US weighting, with an actively managed global strategy that seeks opportunities in underrepresented regions or sectors to achieve better diversification.
- **Multi-Asset Investing** – Incorporating fixed income, alternative investments, and factor-based equity strategies can help smooth portfolio performance and improve resilience across different market environments.

The key takeaway: Successful investing isn't about picking a single "best" strategy but about thoughtfully combining different approaches to improve long-term results. A well-blended portfolio can adapt to changing market conditions while minimising unnecessary risks.

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Why Blending Works – Theoretical and Practical Foundations

Throughout history, financial markets have experienced speculative bubbles—phases in which asset prices rise sharply, often driven by investor optimism rather than fundamental factors. Time and again, many investors enter the market just as those who have profited are exiting. A crucial lesson from market history is that when asset managers are overly confident in a single strategy, it may be time to be cautious.

The Role of Behavioural Biases in Investment Decisions

Investors are naturally prone to behavioural biases. Confirmation bias leads us to seek evidence that supports our existing beliefs, while herd behaviour causes us to follow trends, sometimes to our detriment. For example, there is no shortage of voices on LinkedIn arguing that "active management is dead" and that passive investing is the only way forward. They present compelling data, yet markets are cyclical, and over-reliance on any single approach introduces risks.

One concern with passive investing is the sheer volume of money flowing into major indices. Since passive funds mechanically allocate capital based on market capitalisation, the largest stocks receive the most investment, which can distort price discovery. While passive investing has clear benefits, treating it as a foolproof strategy ignores potential vulnerabilities.

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Why Blending Works – Theoretical and Practical Foundations

For financial planners, investment management is just one component of the broader financial planning process. A key principle is avoiding unnecessary risks. If a client wishes to take speculative positions, they should do so consciously rather than as part of their core investment strategy.

Theoretical Foundations: Modern Portfolio Theory (MPT)

To construct resilient portfolios, we must go beyond trends and base decisions on sound investment principles. Modern Portfolio Theory (MPT), introduced by Harry Markowitz in 1952, provides a mathematical framework for maximising returns while minimising risk. A core insight of MPT is that diversification reduces risk without necessarily sacrificing return—a principle that supports blending different investment strategies.

Key MPT Concepts in Blended Investing

- **Efficient Frontier** – The optimal set of portfolios that offer the highest expected return for a given level of risk.
- **Risk vs. Return Trade-Off** – Adding assets with low correlation can reduce overall portfolio volatility while maintaining strong returns.
- **Correlation Matters** – Combining assets with different risk/return characteristics enhances risk-adjusted performance.

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Why Blending Works – Theoretical and Practical Foundations

Practical Example: Blending High-Growth and Defensive Strategies

Scenario

An investor is considering two distinct investment options:

- US Technology Stocks (Magnificent Seven) – High-growth but volatile.
- European Defensive Equities (Granolas) – Lower growth but stable returns.

(For context, "Granolas" refers to European companies in sectors like healthcare, consumer staples, and utilities—firms known for resilience in economic downturns.)

Analysis Using MPT

The Magnificent Seven stocks have historically delivered high returns (39.88% p.a.) but with substantial volatility (28.53%).

The Granolas offer lower returns (10.5% p.a.) but with reduced volatility (9%).

A low correlation between the two asset classes indicates that defensive European stocks tend to perform well during technology-driven sell-offs.

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Why Blending Works – Theoretical and Practical Foundations

Outcome

Instead of allocating 100% to the highest-return strategy, a blended approach smooths performance and reduces risk:

70% Magnificent Seven, 30% Granolas

This allocation captures higher returns than investing solely in defensive equities.

It significantly reduces risk compared to a purely tech-based portfolio.

The Sharpe ratio (risk-adjusted return) improves as diversification helps smooth out extreme market swings.

Conclusion

Blending investment strategies is not about choosing one approach over another—it is about constructing resilient portfolios that perform across different market environments. By integrating multiple investment styles and asset classes, investors can better navigate market cycles while mitigating unnecessary risks.

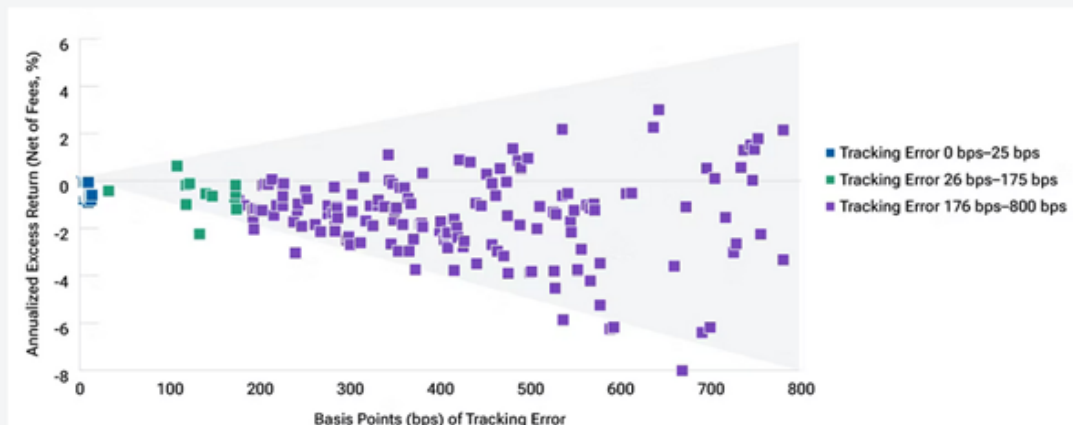
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The Benefits of Blending Investment Strategies

T. Rowe Price recently published an article on blending passive and active investment strategies, featuring a compelling chart that illustrated the wide dispersion of outcomes for U.S. large-cap equity strategies.

Wider dispersion in outcomes for U.S. large-cap equity strategies with higher tracking error

(Fig. 1) Average annualized excess returns, after fees, and tracking error vs. the S&P 500 Index



One particularly striking comment stood out:

“Popular indexes such as the S&P 500 and the MSCI All Country World were created to measure the performance of the broader market. Despite their strong performance over the past 10 years, they were not designed as investment portfolios.”

It's easy to assume that simply investing in these indices is a foolproof strategy. However, this approach inherently increases risk because we cannot predict future market shifts. If there is a rotation away from the U.S. or a change in investment style, investors concentrated in these indices may face significant drawdowns.

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The Benefits of Blending Investment Strategies

By blending different investment styles and strategies, investors can build a more resilient portfolio. The key benefits include:

- **Resilience to Market Conditions** – A well-diversified portfolio is better equipped to withstand economic downturns and market cycles.
- **Enhanced Risk Management** – Different investment styles respond uniquely to various market stresses, reducing the likelihood of concentrated losses.
- **Greater Opportunity Capture** – A multi-strategy approach enhances the ability to capitalise on inefficiencies across various asset classes and regions.
- **Better Client Outcomes** – A diversified investment approach aligns with long-term wealth creation, financial security, and client expectations.

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The Power of Blended Research Methodologies

In a recent analysis of three multi-asset investment strategies, performance alone highlighted a clear winner. However, examining the underlying methodologies revealed important insights:

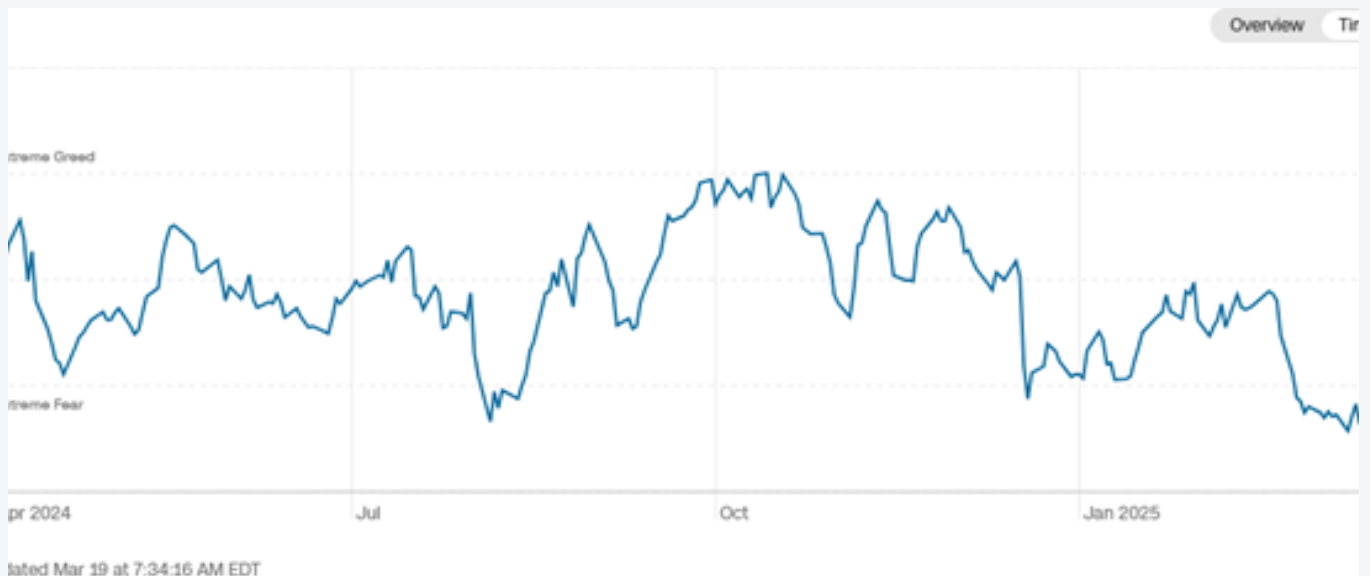
1. Strategic Asset Allocation Differences – The second strategy only slightly underperformed the best-performing strategy, but it employed a tactical asset allocation approach. By reducing U.S. exposure to 55% versus 70% in the first strategy, it positioned itself more defensively in case of a market shift.
2. The “Titanic Approach” – The first strategy invested purely in market-weighted indices, effectively assuming that, regardless of economic conditions, markets would recover. This approach carries risks, as it may continue sailing into potential downturns without adjustment.
3. Underperformance and Lower U.S. Exposure – The third strategy had less than 40% U.S. exposure and significantly underperformed, reinforcing the importance of understanding geographical allocation and timing.

While data-driven analysis is crucial, it does not tell the whole story. Gaining a deeper understanding of why specific strategies perform as they do enables investors to make more informed decisions when blending approaches.

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The Power of Blended Research Methodologies

The U.S. market has performed exceptionally well in recent years, but concerns remain. A look at market sentiment—such as the Fear and Greed Index from April 2024 to March 2025—can offer valuable insights into investor behaviour.



Proper investment discipline comes from integrating multiple perspectives, including sentiment analysis, valuations, and other key data points. This approach helps remove emotional biases from decision-making.

We are human, and no amount of data makes us infallible. However, by combining quantitative analysis with in-depth research and blending investment styles, we can mitigate behavioural blind spots and construct more robust portfolios.

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How to Implement a Blended Approach in Investment and Research

One of the biggest challenges in portfolio construction is accepting that, at any given time, some strategies will underperform others. The foundation of any effective blending strategy is understanding the individual strategies within the portfolio—how they function and why they are included.

A well-blended portfolio is not just about generating returns—it's about ensuring that when some assets decline, others hold steady or rise. The objective is to create a structure where not everything moves in the same direction simultaneously.

Technology and Portfolio Insights

Advanced research tools, such as BlackRock's Aladdin Research System, can help firms analyse and understand how different strategies interact within a portfolio. These insights allow investors to fine-tune allocations and assess risk exposures more effectively.

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How to Implement a Blended Approach in Investment and Research

Practical Implementation at the Firm Level

For firms and investment teams, a deep understanding of how and why different strategies are blended is crucial. This ensures that when clients ask questions about underperformance in specific areas, advisers can provide clear, well-reasoned explanations rather than reactive responses.

Although investments are only one part of the broader financial planning strategy, clients expect transparency and informed decision-making. Being able to articulate the rationale behind portfolio construction enhances trust and reinforces long-term investment discipline.

The Future of Blended Investment & Research Strategies

As financial markets evolve, blended investment and research strategies are becoming increasingly essential for achieving optimal risk-adjusted returns. A growing body of academic research, empirical data, and industry trends supports the case for combining passive and active strategies, diversifying across asset classes, and incorporating alternative investments.

Below is a summary of key evidence highlighting why the future of investing lies in blending strategies.

Empirical Evidence Supporting Blending Active & Passive Strategies

SPIVA Reports: Active vs. Passive Performance

- S&P Dow Jones Indices' SPIVA Scorecard (2024) shows that while many active funds underperform their benchmarks over the long term, certain categories (e.g., small-cap, emerging markets, and fixed income) provide opportunities for active managers to add value.
- The key takeaway: A fully passive approach may not be optimal—combining low-cost passive exposure with targeted active strategies can enhance returns.

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The Future of Blended Investment & Research Strategies

Research by BlackRock & Vanguard on Factor-Based Investing

- BlackRock's research (2023) finds that combining passive index exposure with factor-based strategies (e.g., momentum, value, quality) improves risk-adjusted returns.
- Vanguard (2024) highlights that investors can enhance portfolio diversification by including both traditional passive funds and factor-based active strategies.

Portfolio Diversification: The MPT & Multi-Asset Investing Case

Studies on Modern Portfolio Theory (MPT) & Diversification

- Harry Markowitz's Modern Portfolio Theory (1952) demonstrated that blending uncorrelated assets reduces risk without sacrificing return.
- The Yale Endowment Model (David Swensen) successfully applies blending by combining equities, fixed income, alternatives, and real assets, consistently outperforming traditional 60/40 portfolios.

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The Future of Blended Investment & Research Strategies

The Case for Multi-Asset Investing (2024 Data)

- JP Morgan Asset Management finds that multi-asset portfolios with a mix of equities, bonds, commodities, and alternatives outperform single-asset class portfolios in risk-adjusted terms.
- Bridgewater Associates' research shows that adding non-correlated assets (e.g., private equity, infrastructure, commodities) to traditional portfolios can reduce downside risk while maintaining returns.

Addressing Market Concentration & the Need for Regional Diversification

Evidence of Index Concentration Risks (MSCI World & S&P 500)

- The MSCI World Index is 72.92% weighted towards the US, exposing investors to regional concentration risk.
- The S&P 500's top 10 stocks account for 30% of the index, increasing systematic risk in downturns.
- Research by Robeco (2024) suggests that blending US, European, and Asian equity exposures lowers risk and provides more balanced global growth.

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The Future of Blended Investment & Research Strategies

Emerging Markets & Small Caps as a Blended Strategy

- MSCI Emerging Markets (EM) Index historically outperforms developed markets over longer time horizons but with higher volatility.
- Fidelity's research (2023) shows that blending small-cap and EM exposure with large-cap stocks enhances long-term portfolio performance.

Alternatives & Sustainable Investing: Expanding the Investment Universe

Rise of Alternative Investments in Portfolio Construction

- Preqin's 2024 Global Alternatives Report finds that institutional investors are increasing allocations to private equity, real estate, infrastructure, and hedge funds to improve risk-adjusted returns.
- Endowment Models (e.g., Harvard & Yale) have demonstrated how alternatives enhance diversification and protect against equity market downturns.

ESG & Sustainability as a Blended Strategy

- Morningstar's 2024 ESG Fund Performance Study finds that sustainability-focused funds outperform traditional funds over 10 years due to strong governance and risk management.
- Combining ESG-focused active strategies with broad market passive exposure provides both ethical and financial benefits.

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The Future of Blended Investment & Research Strategies

Future Trends: AI & Quantitative Research in Investment Strategies

- **AI-Driven Investment Models:** Hedge funds and asset managers are increasingly using AI for factor-based investing and real-time risk analysis, further blurring the lines between active and passive strategies.
- **Quantitative Research in Blended Strategies:** Firms such as Two Sigma, AQR, and Renaissance Technologies utilise quantitative models to identify market inefficiencies that can be incorporated into blended portfolios.

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Conclusion: The Evidence is Clear—Blending is the Future

The financial landscape is evolving, and the evidence overwhelmingly supports a blended investment and research approach. Investors who rely solely on passive investing may miss opportunities and take on hidden risks (such as market concentration), while those who invest only in active strategies risk higher costs and potential underperformance.

By integrating passive, active, alternative, and multi-asset strategies, investors can:

- Enhance risk-adjusted returns
- Mitigate downside risk
- Diversify across asset classes, geographies, and investment styles
- Leverage AI & quantitative research for smarter decision-making

In short, the future of investing lies in intelligent portfolio blending—combining the best of multiple strategies to optimise long-term outcomes.