Risk Disclosures

MoneyFarm wants to help you to make informed investment decisions, bearing in mind that investing is typically a long term decision. The concept of risk and how it affects the value of investments is one of the most important aspects any potential investor needs to understand.

Please read this document, and any other information we hereby give you, carefully.

Investment Risk

Investments are exposed to different kinds and degrees of risk. MoneyFarm wants to help you understand the complex subject of investment risk and how we seek to manage this when you receive our Advisory Service or Discretionary Management Service. For further information about the services MoneyFarm offers clients, please click here.

This document describes the types of risks that are relevant to the investments (Exchange Traded Funds and Exchange Traded Commodities) used by MoneyFarm, but it cannot be an exhaustive list. Unless otherwise stated, the information provided below applies to both our Advisory Service and our Discretionary Management Service.

If you are in any doubt about the risks involved in investing, the services we provide or whether to invest with MoneyFarm, ask us or seek independent financial advice.

The value of your investments can go down as well as up, so you may get less than your initial investment

When investing, there is always the risk that your investment could fall in value as well as rise.

If you save cash in an account with a reputable bank or building society, your savings are normally guaranteed by the Financial Services Compensation Scheme up to the value of £75,000 per institution. This means that if the bank were to fail, you will get back up to £75,000 of your money; if the bank remains solvent, there is no danger that you will get back less than you put in.

Although this seems a relatively 'safe' option, there is the risk that the real values of your savings are reduced by the effects of inflation. The interest rate you earn on your savings account must at least equal the prevailing rate of inflation, or you will lose money in real terms.

When investing in things that are not cash, there are no guarantees. Share prices fall as well as rise. Companies can run into financial difficulty, although in this sense, the Financial Services Compensation Scheme also protects eligible investors for up to £50,000. Even governments sometimes struggle to repay their loans. Property can also be subject to large fluctuations in value. Everyone looking to make an investment does so for the opportunity to make positive returns but in doing so, they must accept the possibility that they may end up with less money than they originally put in.

Risk vs. Return

The potential returns from an investment are, to some degree, linked to the risk an individual investor is willing to accept. In general, the higher the risk, the higher the potential return you (as investor) could potentially receive, but this is not always the case.

Unfortunately, by taking on more risk in the hope of achieving a greater return, the chance of losing money increases as well. None of the investments provided by MoneyFarm are risk-free, and you may therefore get back less than you initially invest. While MoneyFarm's objective is to select investments with the potential to achieve the optimum level of return for your accepted level of risk, there can be no guarantees that the investment strategy will succeed.

What are the Risks?

There are many risks affecting the type of investments MoneyFarm provides. They range from high level socio-economic concerns such as war or political turmoil to more company specific risks like bankruptcy, or effects caused by the actions of a rogue trader.

Social/Political Risk

Government policy and wider political, social and environmental issues have the potential to significantly affect the value of investments. For example, regulation can constrict industry, just as favourable tax breaks can benefit it.

Political decisions, instability and changes to public sentiment create uncertainties for business and therefore represent a risk to the profitability of investments.

Interest Rate Risk

This is the risk that the prevailing interest rates can harm the value of your investments. Rising interest rates can cause the value of fixed interest investments to fall as the fixed interest rate they offer is no longer competitive compared to, for example, bank deposits.

Currency risk

This is the risk that the value of an investment held in a foreign currency falls as a result of a change in the exchange rate. For example, the value of shares in an American company held by a UK investor may grow in dollar terms but if the Dollar/UK sterling exchange rate moves adversely, the value of that investment in UK sterling could fall overall. If your MoneyFarm investments' underlying holdings are in a currency which is different to the denominated currency of your MoneyFarm account, you will face currency risk.

Liquidity risk

This is the risk that the value of an investment cannot be realised quickly because there are insufficient buyers in the market. This can be caused by a number of factors, including but not limited to insolvency, market conditions or selling restrictions. Losses may be substantial in a falling market, as an investor is unable to sell quickly without accepting a much reduced price. Although relevant to all investments, liquidity risk may typically be higher with investments in property or in shares of unlisted companies, because these assets do not have the high volumes of trading activity that FTSE 100 companies might have. MoneyFarm only invests in ETFs or ETCs trading on the London Stock Exchange. Liquidity risk should be lower for such investments than for, for example, investments in the shares of unlisted securities, though it cannot be excluded that particular events or circumstances could cause the ETF or ETC trading market to become illiquid.

Investment Manager Risks

This is the risk of insolvency or poor performance of MoneyFarm in the management of your portfolio (Discretionary Management Service) or the investment advice given (Advisory Service). In the unlikely event of an insolvency situation, your investments may be liquidated without your consent, and potentially at a loss.

Exchange Traded Fund/Exchange Traded Commodities

MoneyFarm invests exclusively in Exchange Traded Funds ("ETFs") and Exchange Traded Commodities ("ETCs"). ETFs are investment funds, traded like shares, which hold investment assets such as shares, commodities or bonds. ETFs normally closely track the performance of a financial index, and as such their value can go down as well as up (and you may get back less than you invested). Some ETFs rely on complex investment techniques, or hold riskier underlying assets to achieve their objectives. MoneyFarm also invests in Exchange Traded Commodities ("ETCs"). ETCs are similar although not identical to ETFs and are traded and settled exactly like normal shares; ETCs allow investors to gain exposure to commodities such as Crude Oil or Gold. The following are risks specifically associated with these types of investments.

Index Risk

ETFs and ETCs are designed to match an index, and are passive investments. Because an ETF or ETC is not actively managed, it will not sell a security if the security's issuer is in financial trouble—unless the security is removed from the index. This means that the ETF or ETC will move up and down with the index and the ETF/ETC manager will not take defensive positions, or sell losing positions, in a market downturn. This also means that the manager won't increase exposure to positions that it anticipates increasing in value, either. This lack of management means that investors are placing their money with an index, not a manager, and their fortunes are related to the performance of the index. The best way for an investor to deal with index risk is to understand what is in the index and the rules governing what goes into, or out of the index, as covered in the ETF's or ETC's documentation which we will provide to you on your request.

Tracking Error

In addition to the risk of their investment being exposed to the movements of the index, investors also are at risk when the ETF or ETC does not match the performance of the index, a situation known as tracking error.

Tracking error represents the difference between the performance, or return, of the ETF's or ETC's portfolio and the underlying index. Tracking error occurs for a number of reasons. The first is that an ETF or ETC has expenses that an index does not have, because it incurs costs when it buys and sells securities. The frequency of these transactions, such as how often an ETF or ETC rebalances its portfolio, can increase the costs that increase tracking error and diminish an ETF's or ETC's performance.

Another reason for tracking error occurs when an ETF or ETC holds cash, which will earn a different rate of return than ETFs or ETCs invested in the portfolio and cause a deviation in returns between the index and the ETF or ETC (at some times the cash may perform better than the ETF). With ETFs and ETCs, however, the amount of cash held tends to be small.

Certain ETFs or ETCs may exhibit tracking error because the weights of the securities in their portfolios do not match those in the ETF or ETC. When the weights are based on market capitalisation, this will not be much of a problem, because the weights are tied to the capitalisation of the stocks, and if a stock moves up in price in the index, that will be captured in the ETF or ETC. The difficulty arises when an ETF or ETC assigns weights by another means, such as equal weighting or some arbitrary method of weighting. In these cases, changes in the values of the securities in the index may not show up in the ETF or ETC until the it is rebalanced, where the ETF's or ETC's securities are adjusted to match those in the index. This lag can induce tracking error.

Another source of tracking error comes from the fact that many ETFs or ETCs do not hold all the securities that make up the index. There are two ways for an ETF or ETC to track an index. The first is replication, whereby the ETF or ETC holds all the securities in an index in the same proportions as in the index. The second is by representative sampling, whereby the ETF or ETC uses a sampling methodology to select securities that it believes will provide the same performance as the entire portfolio. This methodology usually produces larger tracking errors than if the ETF or ETC bought the whole index. The amount varies depending on the quality of the sampling process.

Counterparty risk

ETFs and ETCs do not always hold the physical assets. If the investment bank providing the future/option fails, the ETF or ETC will lose part or all of the money it has invested.

Volatility

The value of all your MoneyFarm investments depends on market fluctuations outside our control. ETCs generally have higher volatility risk than other investments because the value of the underlying assets of an ETC (commodities) can move by more than 10% in a single day. Movements of this order are unusual, but they do occur, and are further magnified by leveraged or geared exchange traded investments.

Trading within foreign market closures

ETFs and ETCs traded on a particular exchange can be bought or sold between normal market opening hours, typically 8am to 4.30pm. However, many of the indices an ETF or ETC might track might be open outside the exchange on which the ETF or ETC is listed. This means the ETF or ETC is trading during periods when the underlying index is closed. This can result in a disparity between the daily performance of the ETF or ETC and the index being tracked.

Tax

The tax treatment of an exchange traded investment is subject to change, which could affect your investment in the future. In some cases, the returns from trading ETFs and ETCs may potentially be subject to income tax rather than capital gains tax. The ongoing tax liabilities are determined by both your individual circumstances and the continued status of the exchange traded investment. If you are unsure of your tax liabilities you should consult a qualified tax advisor.

Other risks

Other risks include, but are not limited to, the following:

Investors may not benefit from the same entitlements as if they held the shares directly (e.g. voting rights).

Investors cannot control the investments that are made within the ETF or ETC. This discretion is held by the Investment Manager appointed by the third-party investment ETF or ETC provider.

Although an ETF or ETC may be denominated in a particular currency, underlying investments may be held in other currencies and thus the ETF or ETC may be subject to currency moves. ETF or ETC prices can be volatile. The overall market may fall, or the ETFs or ETCs that you invest in may perform badly. The value of your investment may go down as well as up, and past performance is no indication of future performance. Counterparty risk should be considered when acquiring ETCs in particular, as ETFs' investments are generally held with a counterparty. While funds invested in ETF may also be held with a counterparty, they are generally invested in securities.

Collective Investment Schemes (or "funds")

A fund is a term that covers different types of structure, such as Open Ended Investment Companies (OEICs) or Unit Trusts (UTs). Each fund will typically already have its own preferred structure, so you will not normally be given a choice. Most funds can be held in tax-efficient wrappers, such as ISAs and pensions. Funds allow investors to pool their money in order to gain access to professional fund managers. Funds typically hold investment assets including gilts, bonds and quoted equities. Depending on the scheme, they may hold 'riskier' assets such as property, derivatives, unquoted securities or other complex products. The value of the fund (and the income derived from it) can go up as well as down (and you may get back less than you invested). Funds bear investment management risks, insolvency risks and liquidity risks, as well as sector/asset specific risks (see above).

Investment Trusts

Investment trusts are similar to funds in that they are a means of investors pooling money. Investment trusts are publicly listed companies, whose shares are traded on the London Stock Exchange. The prices of shares in an investment trust will depend on market fluctuations and also the value of their underlying assets. The value of the investment trust (and the income derived from it) can go up as well as down (and you may get back less than you invested). They will be subject to a combination of the risks associated with shares, bonds and funds in which they are invested.

Managing Risk

Some of these risks can be anticipated and will occur regularly. Other risks are completely unpredictable. Unprecedented world events occur all the time and it is impossible to predict them.

It may not be possible to predict what is going to happen but it is possible to manage exposure to potential problems. Past performance is not a guide to future performance. MoneyFarm's objective is to design portfolios that can withstand unexpected shocks, while at the same time offering the opportunity for growth, whatever your individual risk appetite. Nevertheless, the risk factors set out in this document will apply to investments recommended to you by MoneyFarm Advisory Service or made by MoneyFarm Discretionary Management Service on your behalf.

Where you select the Advisory Service, MoneyFarm will build a portfolio and recommend investments for you. MoneyFarm will take reasonable steps to ensure that the investments we recommend are suitable for you, taking into account your knowledge and experience in the relevant investment field, your financial situation and your investment and risk objectives. If the information which you provide to MoneyFarm is incomplete or inaccurate then this may impair our ability to assess the suitability of a transaction for you.

When you select the Discretionary Management Service, MoneyFarm will build a portfolio that meets your stated investment and risk objectives, achieving this in a number of ways – from appropriate asset allocation to ensuring adequate diversification in your portfolio.

For both the Advisory Service and Discretionary Management Service, risk is managed because different classes of assets are affected to different degrees by the risks detailed above.

By changing the allocation to different kinds of assets, the risk profile of a portfolio can be adjusted. Striking the right balance across all these different asset classes and ensuring that this investment mix is right for you is what good investment management is all about.

Risk and our Services

For our Advisory and Discretionary Services, MoneyFarm runs a series of different model portfolios which are kept within the defined risk parameters at all times. MoneyFarm will then either suggest investments to you that match these portfolios (Advisory Service) or create a portfolio for you (Discretionary Service). Each portfolio is run with set risk-focused strategy ranging from very cautious through to very adventurous.

The level of risk each portfolio is exposed to is designed to be kept constant at all times. This means that MoneyFarm will not materially change the exposure to risk assets just because they happen to be doing well at a certain point in time.

Through this commitment to fundamentals MoneyFarm can manage the level of risk you, as an investor, are exposed to. If you decide that your circumstances have changed and you would like to take on more or less risk with your investments, then you can simply let us know and we will link your holdings to a more or less adventurous strategy. We will not however do this without your prior consent.

Investing is not a short-term option

We want to help you to fully understand the risks involved in investing with MoneyFarm. However, investing may not be for everyone and you should seek independent financial advice if you are unsure.