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IN THIS ISSUE

Building a well-balanced investment portfolio requires diversifying across various stock sectors to mitigate risk and enhance returns. Understanding the roles of different sectors—such as cyclical, defensive, growth and value stocks—helps investors align their choices with their financial goals and risk tolerance.

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STOCK SECTORS EXPLAINED:

HOW TO BUILD A WELL-BALANCED PORTFOLIO

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Investing isn't just about picking stocks, it's about understanding how different sectors respond to economic conditions.

Some industries thrive when economies boom, but struggle in recessions, while others provide steady returns no matter what.

By diversifying across sectors, investors can reduce risk and improve long-term performance. Numerous academic studies have consistently shown that asset allocation, rather than investment selection, is responsible for approximately 90% of a portfolio's returns.

This guide breaks down key stock sectors, their role in a portfolio, and who they're best suited for.

1. CYCLICAL STOCKS – RIDING ECONOMIC WAVES

What they are:

Cyclical stocks perform well in economic upswings, but decline during downturns. These include companies in luxury goods, travel, retail and automotive industries.

Role in a portfolio:

Offers high growth potential during strong economies, but requires tolerance for volatility.

Suitable for:

- Investors with a higher risk tolerance; and
- Those looking to capitalise on economic recoveries.

Examples of cyclical stocks:

- JSE: Richemont (CFR) – Luxury goods giant (Cartier, Montblanc) benefiting from rising wealth.
- JSE: Naspers (NPN) – Tech-driven holding company with a stake in Tencent.
- Global: Tesla (Nasdaq: TSLA) – A leader in electric vehicles; sensitive to economic conditions.
- Global: Nike (NYSE: NKE) – Sportswear brand dependent on consumer spending.

2. DEFENSIVE STOCKS – STABILITY IN UNCERTAIN TIMES

What they are:

Defensive stocks belong to industries that stay resilient regardless of economic conditions, such as healthcare, consumer staples and utilities.

Role in a portfolio:

Provides stability and downside protection during market downturns.

Suitable for:

- Conservative investors seeking stability; and
- Retirees or those prioritising dividends.

Examples of defensive stocks:

- JSE: Shoprite (SHP) – Leading grocery retailer with steady demand.
- JSE: Aspen Pharmacare (APN) – Pharmaceutical company producing essential medicines.
- Global: Johnson & Johnson (NYSE: JNJ) – A healthcare giant with consistent earnings.
- Global: Procter & Gamble (NYSE: PG) – Consumer goods leader with essential products (e.g., Pampers, Gillette).

3. GROWTH STOCKS – INVESTING IN FUTURE LEADERS

What they are:

Growth stocks are companies focused on high revenue expansion, often reinvesting profits into their businesses instead of paying dividends.

Role in a portfolio:

Provides long-term capital appreciation, but can be volatile.

Suitable for:

- Investors with a long-term horizon; and
- Those comfortable with higher risk for high potential returns.

Examples of growth stocks:

- JSE: Prosus (PRX) – Major global tech investor (stake in Tencent, e-commerce holdings).
- JSE: Purple Group (PPE) – Owner of EasyEquities, benefiting from digital investment trends.
- Global: Amazon (Nasdaq: AMZN) – A leader in e-commerce and cloud computing.
- Global: NVIDIA (Nasdaq: NVDA) – A top AI and semiconductor company.

4. VALUE STOCKS – BUYING UNDERVALUED COMPANIES

What they are:

Value stocks trade below their intrinsic worth, often due to temporary market mispricing. They're usually well-established companies with strong fundamentals.

Role in a portfolio:

Provides steady returns and less volatile than growth stocks.

Suitable for:

- Long-term investors looking for undervalued opportunities; and
- Those preferring a lower-risk approach.

Examples of value stocks:

- JSE: Absa Group (ABG) – A major banking institution trading at attractive valuations.
- JSE: British American Tobacco (BTI) – A stable dividend payer with global exposure.
- Global: Berkshire Hathaway (NYSE: BRK.B) – Warren Buffett's investment company, focused on value investing.
- Global: Unilever (LSE: ULVR) – A multinational consumer goods company.

5. INCOME STOCKS – GENERATING PASSIVE CASH FLOW

What they are:

Income stocks pay consistent dividends, making them attractive for investors seeking passive income. These include real estate investment trusts (Reits), telecoms and financial services.

Role in a portfolio:

Provides steady income and lower volatility.

Suitable for:

- Retirees and income-focused investors; and
- Those looking for dividend-paying stocks.

Examples of income stocks:

- JSE: Growthpoint Properties (GRT) – A major Reit offering stable dividends.
- JSE: MTN Group (MTN) – A leading telecom provider with regular dividend payments.
- Global: Coca-Cola (NYSE: KO) – A dividend aristocrat with a history of steady payouts.
- Global: JPMorgan Chase (NYSE: JPM) – A top global bank with strong dividend performance.

6. SPECULATIVE STOCKS – HIGH RISK, HIGH REWARD

What they are:

These stocks belong to emerging industries or startups with huge upside potential, but significant risks.

Role in a portfolio:

Can provide massive growth, but should only be a small portion of a diversified portfolio.

Suitable for:

- Experienced investors willing to take calculated risks; and
- Those comfortable with potential losses for high reward.

Examples of speculative stocks:

- JSE: Karooooo (KRO) – A vehicle-tracking tech company with global expansion potential.
- JSE: Thungela Resources (TGA) – A coal mining company with volatile commodity exposure.
- Global: Tesla (Nasdaq: TSLA) – While also a cyclical stock, its high valuation makes it speculative.
- Global: Coinbase (Nasdaq: COIN) – A cryptocurrency exchange tied to digital asset volatility.

CONCLUSION

A well-diversified portfolio should include exposure to multiple stock sectors. While cyclical stocks provide high returns during economic booms, defensive stocks offer protection during downturns. Growth stocks fuel long-term gains, while value stocks provide stability. Income stocks generate passive cash flow, and speculative stocks add excitement, but come with high risk.

The key is to balance these sectors based on your investment goals and risk tolerance. Whether you're a conservative investor seeking stability or a high-risk investor chasing returns, sector diversification is essential for long-term success.

Before making investment decisions, consult a financial advisor to ensure your sector allocation aligns with your financial strategy.

CHARIZE BEUKES | CERTIFIED FINANCIAL PLANNER®, BRENTHURST PRETORIA

Phone: +27 (0) 12 347 8240 | **Email:** charize@brenthurstwealth.co.za