OUR TWO CENTS

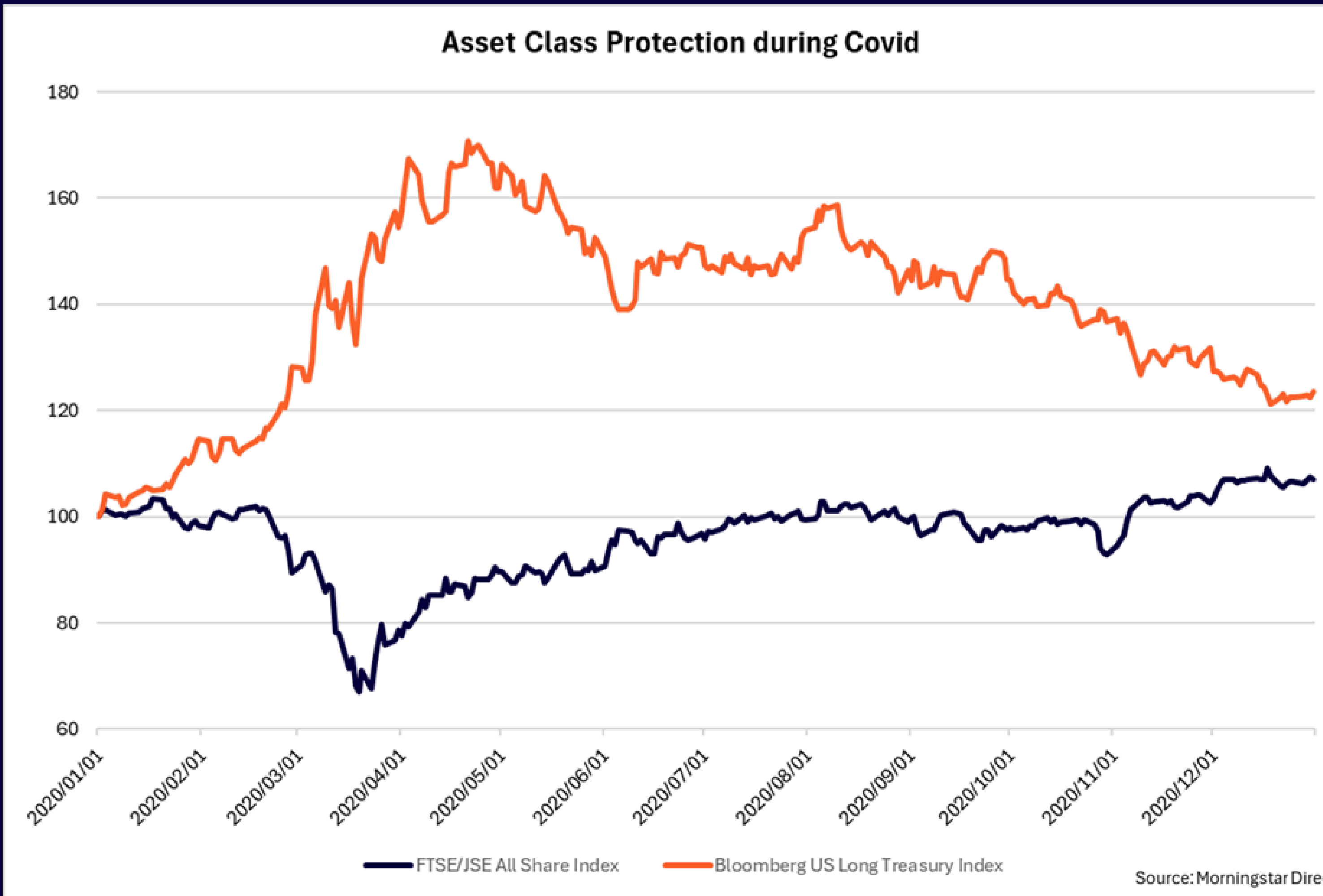
January 2026

NEW ROAD CAPITAL
INVESTMENT MANAGEMENT

Asset Classes & Position Sizing: Important Risk Management Tools

Investors often think of risk management primarily in terms of security selection, yet this perspective overlooks two of the most powerful tools available to portfolio managers: asset class diversification and position sizing.

In equity markets, it is common to hear references to “defensive equities” when concerns about market risk begin to rise. While the label may sound reassuring, it can be misleading. Periods of market stress tend to affect all equities, albeit to varying degrees, and the extent of the impact depends heavily on the underlying cause of the stress. Rather than attempting to rotate within equities, a more robust approach is to diversify across asset classes. Assets such as US government Treasuries have historically performed well during many risk-off environments and therefore offer South African investors an effective hedge against equity drawdowns. This is illustrated in the chart below, which highlights the benefits of US Treasuries during Covid relative to the FTSE/JSE All Share index. From this, the protection power of the asset class as a whole dominates the protection gained from “defensive equities”.



The second important tool of risk management is position sizing. While asset class diversification helps protect portfolios against broad market moves, position sizing plays a critical role in managing risk within an asset class. Fund X provides a useful example of this principle in practice. The fund invests across more than 300 individual debt instruments globally, with each position sized conservatively. As a result, defaults at the individual security level have no material impact on overall fund performance. For example, there were three defaults in the fund during 2025 yet despite this, the fund still returned 10.85% while having a maximum drawdown of 1.05% during the year.

This framework can be applied across all asset classes. By constructing portfolios around a stable core and allocating appropriately sized positions to higher-conviction ideas, investors can capture return opportunities while keeping risk well controlled. When combined with the diversification benefits offered by multiple asset classes, this approach helps create portfolios that are both resilient and consistent. Over time, investors who stick to such a strategy and allow it the time to work are more likely to be rewarded.

Michael Caroline

Investment Analyst

BCom (Hons) Investment Management (UP) | MPhil in Finance (UP) | CFA Charterholder

Michael is an Investment Analyst at New Road Capital, where he contributes to the investment process and focuses on quantitative modelling for asset allocation and fixed income. He holds an MPhil in Financial Management Sciences (cum laude) from the University of Pretoria, where he specialised in economic psychology, and is a CFA Charterholder. Before joining New Road Capital, he worked as assistant lecturer at the University of Pretoria assisting with quantitative investment analysis. Outside of the office, he enjoys the freedom of flight, sailing, and the peacefulness of the bush.