



# YEAR IN REVIEW: HIGH-NET-WORTH-FAMILIES & FAMILY OFFICES

By **Patricia M. Soldano**

## Invest With Purpose

Create a foundation for a disciplined long-term strategy for a variety of market conditions

**A**s we know too well, the past few years have presented a challenge for investors.

The financial crisis and recession of late 2008/early 2009 have given way to a prolonged upward trend in the domestic equity markets and, along the way, significant volatility. This environment has led some investors toward behavioral temptations, for example, abandoning a diversified portfolio in exchange for greater risk with higher levels of equity exposure. Others, alarmed by the ever-rising stock market, are taking their chips off the table altogether.

A key element in avoiding these behavioral temptations in building a sustainable investment strategy is to “invest with purpose.” The first step? Know what you want to achieve with the wealth.

### Know the Goals

Setting clear objectives is central to a goals-based investing approach. This dynamic and ongoing process delivers immediate and tangible benefits. The process:

- Delivers greater potential to achieve goals versus just trying to beat an index or benchmark based on understanding your client’s specific personal, family, dynastic and philanthropic objectives.
- Provides a completely objective framework to help investors define what they hope to accomplish with their wealth.
- Promotes ongoing dialogue among investors and advisors to optimize their portfolios around circum-

stances that can change and evolve.

A customized portfolio asset allocation appropriately tailored to meet an investor’s prioritized goals can be a critical determinant of success.

### Goals-Based Investing

Investors often have more than one goal, with a range of views on how important each goal is. Traditional modern portfolio theory (MPT), while well-founded on historical information, doesn’t effectively connect portfolio success to the realization of one or more of an investor’s goals. The market-focused approach of MPT often leads investors to react emotionally to market movements. And, when short-term investment performance diminishes the connection between strategy and realized results, investor dissatisfaction grows—the very thing MPT was designed to prevent.

A better approach to mitigate emotional investing is to focus on the variables over which the investor can demonstrate some control. This tactic also demonstrates the direct connection between a steady investment hand and the achievement of measurable goals. Creating the link between an investor’s goals and the construction of her portfolio is the key differentiator of a goals-based approach and helps avoid the behavioral pitfalls of investing.

Goals-based investing provides a framework to ask each investor:

- What are your goals?
- How important are they—for each specific goal, is it a need or a want, and how much risk are you willing to take?
- Is this a short-term lifestyle goal or a longer term goal?



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### A More Logical Framework

This investing approach focuses investors on goals-based outcomes, moving the definition of portfolio risk from beating a benchmark or standard deviation to the probability of achieving one's goals. This helps investors remain disciplined in volatile times and avoid investment decisions that are driven by emotional reactions to portfolio performance.

Based on the goals that are set, risk can be budgeted specifically around each goal—such as meeting lifestyle spending or growing the body of wealth for future generations.

### Align Investments with Goals

Clearly defining goals can serve to mitigate instinctive negative reactions to, for instance, committing capital to an investment for a longer holding period. In this case, defining goals may potentially validate or disprove the need for short-term access. The goals-based approach has investors assign time and risk horizons to segments of their portfolio.

GenSpring's approach is to regularly discuss the client's progress toward achieving shorter term and longer term goals separately, so they're able to clearly see the benefits of using goals-based allocation strategies.

### Avoid the Benchmark Trap

Focusing on goals and defining risk as the possibility of not achieving goals can help investors avoid using benchmarks as the sole measure of investment success.

More effective accountability stems from measuring progress toward meeting defined short-term lifestyle and longer term goals measured in absolute dollars, as well as custom blended benchmarks designed around each client's asset allocation. This approach can help both advisors and investors avoid trying to time the market if portfolio performance doesn't exceed its benchmark in the short term. It can also help to appropriately allocate assets toward each goal. Goals-based investing provides a structure that helps investors resist "borrowing" from one goal to meet another without generating a discussion of trade-offs and understanding the implications of such decisions on the overall wealth enterprise and prioritized objectives.

### A Dynamic Process


Goals and the priorities investors assign them aren't static. An investor's circumstances, concerns, priorities and preferences can change over time. Goals-based investing encourages ongoing dialogue and conversation to help keep one's investment strategy aligned with

changing conditions.

### Goals Defined—An Example

A challenge that many investors face is developing an understanding of what they want to do with their money and what's most important to them. Often, clients state that they don't have any specific goals for their wealth. However, GenSpring has found that over the course of a goals-based investing discussion, it's possible to identify and prioritize multiple goals. As the rigorous process continues, our clients often begin to articulate very distinct risk tolerance parameters based on the overall importance and time horizon for each goal. With this information, an investor is able to structure a portfolio to address multiple goals, such as meeting short-term lifestyle needs, as well as longer term philanthropic objectives.

### Goals-Based Wealth Management

Goals-based investing provides investors with the foundation to build a disciplined long-term strategy that they can maintain under a variety of market conditions, thus delivering greater potential to meet one's goals. By measuring success with a yardstick of progress toward goals, investors can also minimize reactive behavior to shorter term market volatility and movements. Goals-based investing promotes a careful selection of investments that align with an investor's multiple needs. It creates a framework that allows investors to be more cautious with parts of their overall portfolio, while encouraging the selection of investments with more potential for return elsewhere. Goals-based wealth management, similar in concept to goals-based investing but applied to wealth planning, delivers additional benefits. It promotes the alignment of investment advice with effective tax and estate planning. Clearly quantifying and prioritizing client objectives can lead to multiple benefits for investors, both in pure investment management and in terms of wealth planning. 

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