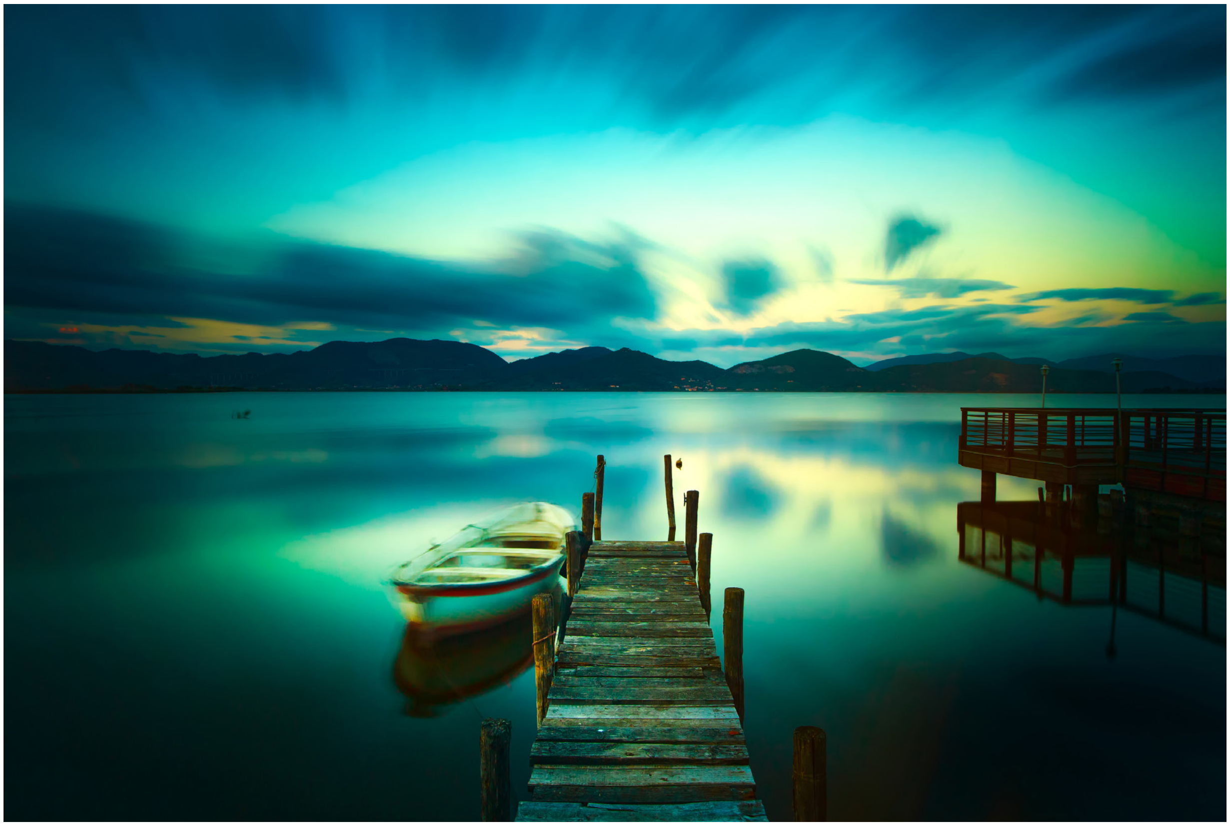
ClarkCapital MANAGEMENT GROUP

NavigatorInsights



Delivering Anxiety-Adjusted Returns with a Time Segmented Approach

Time and time again, advisors say their largest challenge is managing client emotions. If clients are unhappy or anxious about their investments, they run the risk of making impulsive or emotionally fueled decisions. Since one of the most important things clients want from their financial advisor is help making better decisions, let's explore what makes clients anxious in the first place.

People get anxious when they spend too much time worrying about the bad things that might happen in the future or rumi-nating about what happened in the past. Unfortunately, as an industry, we repeatedly highlight past performance in order to help us make recommendations for the future. By encouraging clients to shift their attention away from past mistakes and future worries, you can help them stay focused on the current steps they need to take to grow and maintain their wealth. It's important to create an environment where investment decisions are customized to the client's individual goals and aspirations. This tailored approach is designed help investors think objectively about what they want their money to do for them.

In this article, we'll review three ways to help mitigate the effects of emotional investing.

Divide and Conquer

Break the investment plan into segments, or buckets, designed to meet short, medium and long-term needs. Segmenting allows you to vary the risk exposure across an investor's long-term time horizon. The investor's immediate anxiety can be eased with short-term investments that focus on safer asset classes including fixed income and cash.

Time diversification creates a comfortable distance from assets reserved for long-term goals. *Stocks for the Long Run* author Jeremy Siegel advocates for substantial equity exposure over decades. He acknowledges that, "In the short run…stock returns are very volatile, driven by changes in earnings, interest rates, risk, and uncertainty, as well as psychological factors, such as optimism and pessimism as well as fear and greed."

We believe investing for the long term can help clients withstand the inevitable volatility of the equity market. CFA and MIT professor Mark Kritzman quantified this concept in his article "What Practitioners Need to Know…About Time Diversification." His analysis illustrates the diminished probability of loss over greater periods. He advocates that a long-term investment "reflects the tendency of above-average returns to cancel out below-average returns." In short, stick it out, and you'll win in the end.

Spell It Out

Success is a relative term. To measure success, you must understand and commit to the client's definition of the word. You are likely to find that the client has numerous desired milestones, yet original intent can become obscure as distractions from the media loom large in the psyche of the investor. So, what can we do about it?

Psychology professor Dr. Gail Matthews conducted a study on the success rate of various goal pursuit methods. Some participants were instructed to retain specific targets only in their head. Another group declared their goals in writing. A third group embraced a more robust plan, writing their goals, ranking them and attributing action commands to each.

Those who engaged in the most intensive recording of plans and progress experienced the greatest success. Dr. Matthews remarked, "My study provides empirical evidence for the effectiveness of three coaching tools: accountability, commitment, and writing down one's goals." Put the results of this study to use with your client by creating a personalized financial playbook.

Build It Together

Make the process collaborative. The key players in collaborative portfolio construction are the client, the investment advisor and the asset manager. Each party needs to take the time to ask questions and listen. First, the conversation must begin with the client. Understand their goals and engage them in a granular-level conversation. In many cases, the client will come prepared not only with goals but with ideas on how to accomplish them. Clients want to be involved, and this process helps ensure they are heard.

Use your understanding of the goals and risk tolerance of the client to begin a case design process. More on adopting the case design process here. Case design helps advisors create a balanced and cohesive plan alongside the asset manager.

Involving the investment manager at an early stage in the planning process can help you take advantage of their insights and the full breadth of their investment capabilities. Managers are often able to identify areas for improvement, such as tax optimization and overlap analysis. Such opportunities might not be taken advantage of if they are brought in later in the planning process. Involving these three players can help create a lasting relationship where each person understands their role and communication is clear. In the long-term, a trusting and rewarding relationship is a strong advantage in a competitive industry.

Ultimately, investors' success rests upon the combination of the right investments and the right investing mindset. By using these three methods to help clients achieve their financial goals, advisors may be able to keep clients in their risk comfort zone and on track to achieve their life goals.

Sources:

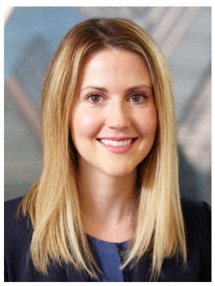
Kritzman, Mark, "What Practitioners Need to Know…About Time Diversification." Financial Analysts Journal, January/February, 1994, pp.14-18.

Siegel, Jeremy J., Stocks for the Long Run. New York: McGraw-Hill,1994, p.29.

Goedhart, Marc and Mehta, Darshit. "The Long and the Short of Stock Market Volatility." McKinsey & Company. May 2016.

Locke, Edwin A., and Latham, Gary P. "New Directions in Goal Setting Theory." Association for Psychological Science 15(5). 2006, pp 265-268.

Matthews, Gail, "Study Focuses on Strategies for Achieving Goals, Resolutions." Dominican University of California.



Author: Patty Quinn McAuley

Patty Quinn McAuley, CFP®, is the Director of Marketing for Clark Capital Management Group. On the blog, she writes about helping clients achieve successful investment outcomes and about communicating effectively with clients.