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## Wealth Firms Tackle Shift to Goals-Based Mode

By Tom Stabile June 15, 2010

Wealth management firms adapting to goals-based planning for high-net-worth clients face a tall order to properly plan the effort, train advisors, and discuss changes with clients, according to executives who have led such efforts.

The budding movement away from a traditional asset allocation vocabulary – such as equities, fixed income, and cash – doesn’t necessarily mean big portfolio changes. But shifting the planning and dialogue to a more personal view of client objectives still demands that all participants understand the new approach. And it could lead some investors to new product sets as they fine-tune the “purpose” of different parts of their portfolios.

The changes are more than simply new talking points, because they push advisors and clients to more thoughtfully assess and allocate risk, says **Brent Fykes**, senior investment partner at **GenSpring Family Offices**, the multi-family office affiliate of **SunTrust Banks**. GenSpring, which has \$20 billion in client assets, introduced its own version of this investing approach to clients over the past year.

“We’re trying to meet our clients’ goals and objectives, not just target a return or measure standard deviation,” Fykes says.

A big underpinning for the goals-based planning concept is research by **Ashvin Chhabra**, CIO of the **Institute for Advanced Study** in Princeton, N.J., and his 2005 article, “Beyond Markowitz: A Comprehensive Wealth Allocation Framework for Individual Investors.” Another influence is the liability-driven investing (LDI) focus that a growing number of institutional investors have adopted, which aligns investment moves to match future obligations.

Firms moving to a goals-based approach have to muster the resources and willingness to delve deeply into client financial affairs, says **Ronald Florance**, director of investment strategy and asset allocation in Charlotte, N.C., for **Wells Fargo Wealth Management Group**, which oversees \$121 billion in assets.

“Not everybody wants to be a full balance sheet manger for their clients,” he says. “This is a very complicated approach.”

The former Wachovia Wealth Management, which Wells acquired in 2008, started implementing goals-based investing about four years ago, Florance says. “It’s all very customized,” he adds. “It’s not as if you’re only picking an investment risk tolerance.”

GenSpring began to establish its new process in 2008, and its advisors introduced it to clients last year, starting with detailed goal-setting and crafting of a family balance sheet, then structuring the allocation across risk capital budget categories matched to client goals, Fykes says.

Clients have generally been receptive to the change, he adds. “It allowed us to re-focus clients on goals-based investing and not simply return percentages, relative performance, and manager fodder,” Fykes says.

The mechanics of shifting the basic advisor-client discussion is “no small feat” for bigger firms, says **Jamie McLaughlin**, a wealth management industry veteran of firms such as **Mellon Financial** and **Convergent Wealth Advisors**.

“It’s one thing to say you’re making the change philosophically,” McLaughlin says. “It’s another to say you’ll do it with the next new client. But to bring it to all of your clients – if you’ve got 1,000 clients with different characteristics, each with their own liquidity considerations, their own closely held businesses – it’s another level.”

And he says a firm has to make critical calls on the terminology and discussion framework advisors use to speak with clients.

McLaughlin says the changes aren’t merely cosmetic, because objectives-based planning can differ significantly from the traditional modern portfolio theory approach built around mean variance optimization and diversification principles. He says Chhabra’s work underscores the “art” behind a goals-based process, more so than LDI, which he calls more “science-based,” built on calculations of how to fulfill specific numeric liabilities.

Many wealth firms echo Chhabra’s core recommendation to divvy client assets and liabilities into “distinct buckets.” Chhabra suggests a set of three: a low-risk bucket meant to preserve the standard of living and basic expenses, allocating, for instance, to cash, annuities, or insurance; a second for market growth through investments such as equities, fixed income or commodities; and an “aspirational” slice through which the client shoots for returns through alternatives, concentrated positions or other riskier holdings.

Clients also assign personal objectives into each bucket, so assets meant to pay for children’s college tuition might skew toward the less risky or market growth categories, depending on how soon bills are due, while a further-off retirement might lean toward higher risk.

That apportioning of client assets could open opportunities for specific investment types.

“The product sets don’t need to change,” Florance says. “But a single client could have more than one investment tolerance, and they would understand, for instance, that their legacy assets for a future generation that might not be distributed for 30 years would have a very different time horizon and risk tolerance than the money for food and clothing and shelter. So it is possible to look at more aggressive investing for a long-term horizon. It’s a bit of an institutional approach.”

Alternatives may fare well particularly because they more clearly fit into discussions about investment purpose rather than drier talk about asset classes, says **Jane Abitanta**, principal of **Perceval Associates**, a wealth management business consultant.

Fykes says GenSpring has found newer clients going through the process to be more open to alternatives, particularly managed futures and long-short equity strategies. He notes, however, that goals-based discussions are meant to be strategic, not geared toward specific investment lineup changes.

Fykes says the new process required refocusing GenSpring’s “family investment officers” away from the “old nomenclature” of bond risk capital and equity risk capital over to four new categories of cash, “defensive,” growth, and private investment. In the changeover, some asset classes and strategies moved around, requiring the firm to explain the new logic to advisors.

The advisors also began using new client assessment tools and had to “fully revisit the wealth diagnostic for all of our clients as if they were walking through GenSpring’s door for the first time,” he adds.

Wells similarly uses purpose-driven language, such as a “liquidity pool” meant for living expenses, Florance says. Interestingly, Florance says the definition of liquidity changed for many clients in 2008, transcending the “credit line” for basic needs to become a buffer in case things got worse.

Fykes says that adopting a goals-based approach has other ramifications, including demanding more staff time and resulting in a higher cost of delivery for the firm, as well as the need for “a more intense effort” from clients, who have to share more data and input. He says executing the process requires a lower client-to-staff ratio and adds, “Technology must be your friend.”

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