VAN LIEW TRUST COMPANY

as we see it

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THOUGHTS FROM OUR CHAIRMAN

During difficult economic times the music is often significantly different from country to country. It appears this time, at least on first impression, that we may be dancing to the same tune as our European brethren. We both seem to be moving in slow foxtrots, trying to cobble together programs to elevate our constituents out of a vicious circle of economic weakness, mounting debt and crippling social programs. Although we are suffering some of the same ailments, at least our economy seems to be growing at a decent pace. Elsewhere in the world, in places like Brazil, Malaysia, India, and yes, China, economic improvement is strong and investors have been dancing the Twist. In this issue of As We See It, Charlotte Yeomans explores one of many investment strategies that can help an investor improve their dance moves - asset allocation.

Alfred B. Van Liew

Let's Waltz, Rumba and maybe Jitterbug

Charlotte A. Yeomans

In the world of investing there are many investments and investing styles just as there are many dances from which to choose. The glue that ties them all together is asset allocation. Asset allocation is an investment strategy used to construct a diversified investment portfolio. This strategy seeks to minimize investment risk while achieving the highest investment return. Asset allocation isn't about picking individual securities. Instead, it focuses on broad classes or categories of investments then combines them together in the right proportion to match the investor's financial goals, time horizon, tax impact and risk tolerance which makes the process highly individual. Some research studies show that asset allocation is the single most important factor in the investment process.

The asset allocation process spreads investments over a number of asset classes in an attempt to protect the portfolio from swings in the market. Different classes of assets carry varying levels of risk and potential for return and typically do not respond to market forces in the same way at the same time. Asset allocation doesn't guarantee a profit or ensure against a loss. However, if you diversify by owning a variety of assets, a downturn in a single holding or asset class won't necessarily damage your entire portfolio. Asset allocation involves identifying the asset classes that are appropriate to meet the investor's goals and determining the suitable percentages that should be allocated to each class. The asset classes to choose from are varied and wide ranging and may include cash or cash equivalents, bonds or fixed income, stocks or equities, real estate, precious metals, other commodities, and even venture capital and private equity, if you are up for a jitterbug.

The four major classes of assets that I will take a closer look at are cash or cash equivalents, bonds, stocks and real estate.

<u>Cash or cash equivalents</u> such as bank savings accounts, certificates of deposit, treasury bills or money market accounts are considered low risk and provide lesser returns. They are subject to inflation risk, the chance exists that their returns will not keep pace with rising prices. Cash provides easier access to funds making it appropriate for investment goals that are short-term.

<u>Bonds</u> are generally less volatile than stocks but offer more modest returns with less opportunity for growth than stocks. Bonds are classified by type of issuer, geography, risk and time factor. The type of issuer categories are government, municipal and corporate. The geographic categories are domestic (U.S.) and international which includes emerging markets. The risk categories are investment grade and high yield. The time factor categories are short, intermediate and long term. Bonds are sensitive to interest rate changes. Because bonds offer fixed interest payments at regular intervals, they may be appropriate for investors seeking a predictable cash flow from a relatively safe investment.

<u>Stocks</u> have historically, over time, provided higher total returns but are more volatile than other asset classes. Stocks are classified by company size, geography and style. The company size categories are large cap, mid cap, smallcap and micro cap. The geographic categories are domestic

(U.S.) and international which includes emerging markets. The style categories are aggressive growth, growth, value and income. Investing in stocks may be appropriate if your investment goals are longer term. Obviously picking companies and issuers with sound financial fundamentals is important.

Cash and Bonds are a bit like a Waltz. On the other hand Stocks are a bit more like a Rumba. Stepping on toes and stumbling happens to the best dancers and investors. The key is to minimize the stumbles.

Real Estate is a class that contains one's home, a vacation home, undeveloped land, investment property and Real Estate Investment Trusts (REITs). The majority of real estate categories are illiquid, an exception being publicly traded REITs. Some categories of real estate can generate regular income and offer a partial protection against inflation. Except for one's home or vacation home, many investors would prefer not to dance.

The objective in executing an asset allocation strategy is to construct a portfolio that provides the investor with a return on their investment without exposing them to more risk than they feel comfortable with. How long you have to invest is also important, because the longer you have to invest, the more time you have to ride out market ups and downs. For instance, if your investment goal is to save for retirement over the next 20 years and you can tolerate a relatively high degree of market volatility, you might put a large percentage of your investment dollars in stocks, and allocate a smaller percentage to bonds and cash alternatives.

There is no such thing as a standardized solution to an asset allocation plan. Successful asset allocation depends on personal variables such as your age, risk tolerance, goals, etc. thus making this process a very individual one, one that is right for you. At Van Liew, we work with our clients to accomplish just that.

Once the investor has chosen an initial allocation, it should be revisited at least twice a year or more frequently in turbulent markets. One reason to do this is to see if the portfolio needs to be rebalanced. Rebalancing is necessary because over time some of your investments may become out of alignment due to market conditions. The investment portfolio may no longer reflect the initial allocation balance that was chosen. For instance, if the stock market has been performing well, eventually you'll end up with a higher percentage of investments in stocks than was initially intended. To rebalance, you might shift funds from one asset class to another. In some cases, you may want to rethink your entire allocation strategy if your financial goals have changed due to a change in your circumstances.

Finding the appropriate asset allocation can be a challenge for many investors. Most investors need the help of a professional advisor to guide them through this process. If you have an investment portfolio of more than $250,000 and are not currently working with an investment advisor, we would be pleased to review your portfolio through a free consultation to assist in providing an asset allocation that meets your financial goals. ⚓