Independent Financial Planning
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Pensioneer Trustee

STEP Presentation 2012

Financial Planning Process - Not Products !

- Financial Management
- **Asset Management**
- **Risk Management**
- Tax Planning
- Estate Planning
  – Whether investing in Cash, Directly Holding Shares, using ETFs, REITS or Bonds the process is the same and explained at a high level on the following slides.

You <u>Can</u> have a successful Investment experience!

- You need to make 5 informed decisions:

1. The Do-It-Yourself Decision:
   - Should you try to invest on your own or seek help from an investment professional? And if so, which type of advisor is best?
2. The Asset Allocation Decision
   - How should you allocate your investments among stocks (equities), bonds (fixed Income), cash (money market funds) and Property (Directly or by REIT)

You Can have a successful Investment experience!

3 The Diversification Decision

- Which specific asset classes within these broad categories should you include in your portfolio, and in what proportions?

4 The Active versus Passive Decision

- Should you favour an actively managed approach to investing that seeks to outsmart the market, or a more passive approach that delivers market-like returns?

5 The Rebalancing Decision

- When should you sell certain assets in your portfolio and when should you buy more?

1. The Do-It Yourself Decision

- The DIY approach is increasingly popular but the odds are stacked against you!
- I believe you should take care of your financial health the same way you take care of your physical health – with the appropriate professionals by your side!
- The average stock market investor earned a paltry **3.2%** annually over the last 20 years versus **8.2%** for the S&P 500 Index ..Why?

1. The Do-It Yourself Decision

- The average bond fund investor earned only **1%** annually over the last 20 years versus the Barclays US Aggregate Bond Index return of **7%**.... Why?
- The Average Stock Fund Investor barely beat inflation and the average bond fund investor barely grew his money at all…..Why?
- The Simple Answer is: We Buy When Markets are at or near their highs, and selling at or near market lows !!

1. The Do-It Yourself Decision

- Do any of the following sound familiar:
  - **Overconfidence** : Success in one walk of life does not automatically translate to success in investing
  - **Attraction to rising prices**: Past performance is not indicative of future results
  - **Herd Mentality**: The comfort of being part of a group! Recent property speculation in Ireland....
  - **Fear of Regret**: Have you ever left money un-invested due to fear of the market? My view is that the right time to invest is when you have the money and the right time to sell is when you need the money.

Model Portfolio | Tailored Selection | Full Screen

Model Portfolio

- Model Portfolio 2 - Cautious
- Model Portfolio 3 - Balanced
- Model Portfolio 4 - Adventurous
- Model Portfolio 5 - High Risk

Cumulative Performance to month ending May 2012

AXA Financial Model Portfolio 2 - Cautious

In general terms, a cautious investor is looking for an investment where the return should be slightly better than that available from a high street deposit account and accept that the value of the investment could fall as well as rise. They would feel uncomfortable however if their investments were to rise and fall in value very rapidly.

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Portfolio/Fund Name	Cumulative Performance to month ending May 2012 6 months	1 Year	3 Year	5 Year	Weighting
AXA Financial Model Portfolio 2 - Cautious	9.28	6.19	29.05	15.12	100%
Allianz RCM Euroland Equity Growth	13.48	-0.52	61.03	3.69	7%
BlackRock Euro Bond	8.48	7.12	19.80	30.46	14%
BlackRock Euro Government Bond Index	8.74	7.79	14.15	28.65	23%
BlackRock Euro Markets Fund	4.59	-17.29	15.82	-27.82	6%
BlackRock UK Index	5.16	0.68	46.47	-18.30	10%
BlackRock US Index	15.58	15.61	73.16	2.91	15%
Newton BNY Mellon Global Bond	8.25	19.22	37.41	46.12	10%

1. The Do-It Yourself Decision

- **Affinity Traps** (Bernie Madoff!) Instead of doing our own research, we make a decision based on mutual ties to an organisation
- Charles Kindleberger, Author of Manias, Panics and Crashes: “ **There is nothing so disturbing to one’s well-being and judgement as to see a friend get rich**”..
- The Key here is discipline and clarity, with the right professional in your corner you can meet your investment goals.

1. The Do-It Yourself Decision

- Retail Brokers
  - Despite the titles they put on their cards, they should not be confused with independent, fee only advisors.
- Stockbrokers are:
  - Better compensated for generating more trades
  - Better compensated for selling certain investment products over others and
  - Limited to selling the investment products approved by their firm

1. The Do-It Yourself Decision

- In contrast to brokers, independent fee only advisors are legally required to act as *fiduciaries* to their clients. This means they must put their clients needs first
- Always use an advisor who uses a 3rd party custody account to hold your assets during the investment process.
- **A broker is working for his firm. An independent fee only advisor is working with you.**

1. The Do-It Yourself Decision

- How to select an independent fee based advisor:
  - Investment Philosophy – Make sure they have one!
  - Personal Connection and Trust – You need to have trust in your advisors ability to help you reach your financial goals
  - Professional Qualifications – Certified Financial Planner (CFP) make sure they are proficient in their field

2. The Asset Allocation Decision

- An understanding of Risk and the relationship between risk and return is necessary for any prudent long-term investor to make smart investment decisions
- For long term investors there are two general types of investments that make up a portfolio:
  - Equities (or Stocks) – are an ownership or interest in a company. If the company does well you reap the reward through dividends and the price may rise. If the company does poorly, its stock may fall in value

2. The Asset Allocation Decision

- **Fixed Income (or bonds) –** are an I.O.U or a loan to an entity such as the U.S government, a state, or company. Bonds are contractual obligations that usually involve interest payments paid by the borrower at regular intervals and ultimately, the return of your initial investment at maturity date.
- **Bonds** are considered to be lower risk/ lower expected return investments (especially high quality, short term bonds).

2. The Asset Allocation Decision

- Investment Risk in Bond investments include:
  - Credit Risk
  - Inflation Risk
  - Maturity Risk
  - Market Risk
- **The common denominator in all measures of risk is the uncertainty of future returns.**

Year	Growth of €100K	Annual Return		Growth of €100K	Annual Return
1	€110,000	10%		€134,000	34%
2	€115,500	5%		€121,940	-9%
3	€131,670	14%		€153,644	26%
4	€143,520	9%		€129,061	-16%
5	€162,178	13%		€169,070	31%
6	€165,421	2%		€167,380	-1%
7	€185,272	12%		€197,508	18%
8	€214,916	16%		€173,807	-12%
9	€227,811	6%		€210,306	21%
10	€257,426	13%		€227,313	8%
Ave Return		**10%**			**10%**
Compound Return		**9.9%**			**8.5%**
Standard Deviation		**4.5%**			**18.6%**

2. The Asset Allocation Decision

- **It is important to understand that the primary driver of investment returns is <u>Risk</u>, <u>and not:</u>**
  - – Timing the Market
  - – Picking stocks
  - – Finding the next guru fund manager
  - – Or all of the above !

2. The Asset Allocation Decision

- **Fixed Income Assets Classes**
  - Cash Equivalents
  - Short Term U.S or German Government Bonds
  - Short Term Municipal Bonds
  - High-Quality, Short-Term Corporate Bonds
  - High-Quality, Short-Term Global Bonds

2. The Asset Allocation Decision

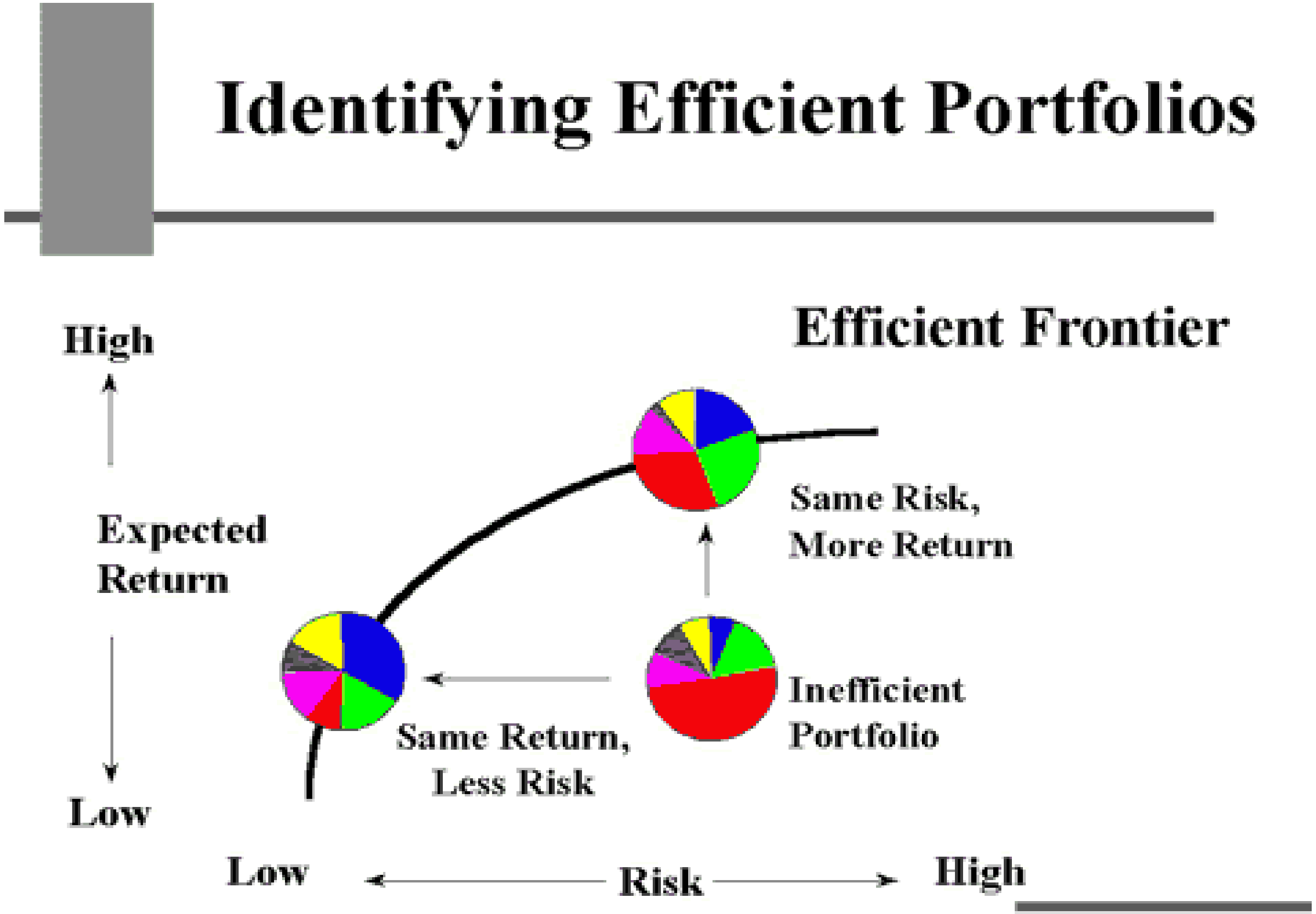
- **Equity Asset Classes**
  - U.S Large Cap Stocks
  - U.S Large Value Stocks
  - U.S Small Stocks
  - U.S Small Value Stocks
  - International Large Stocks
  - International Large Value Stocks
  - International Small Stocks
  - International Small Value Stocks
  - Emerging Market Stocks (Large, Small and Value)
  - Real Estate Stocks or REITS (Real Estate Investment Trusts)

The Asset Allocation Decision

- Hypothetical Portfolios

	100%	80/20	60/40	40/60	20/80	100
Equity	0%	20%	40%	60%	80%	100%
Fixed Income	100%	80%	60%	40%	20%	0%
Annualised Return % 1973-2009	7.2	8.8	10.2	11.5	12.5	13.3
Annualised Standard Deviation% 19793-2009	2.5	3.9	6.6	9.7	12.8	16.1
Growth of $1	$12.99	$22.73	$36.96	$55.95	$78.72	$102.46

3. Diversification Decision



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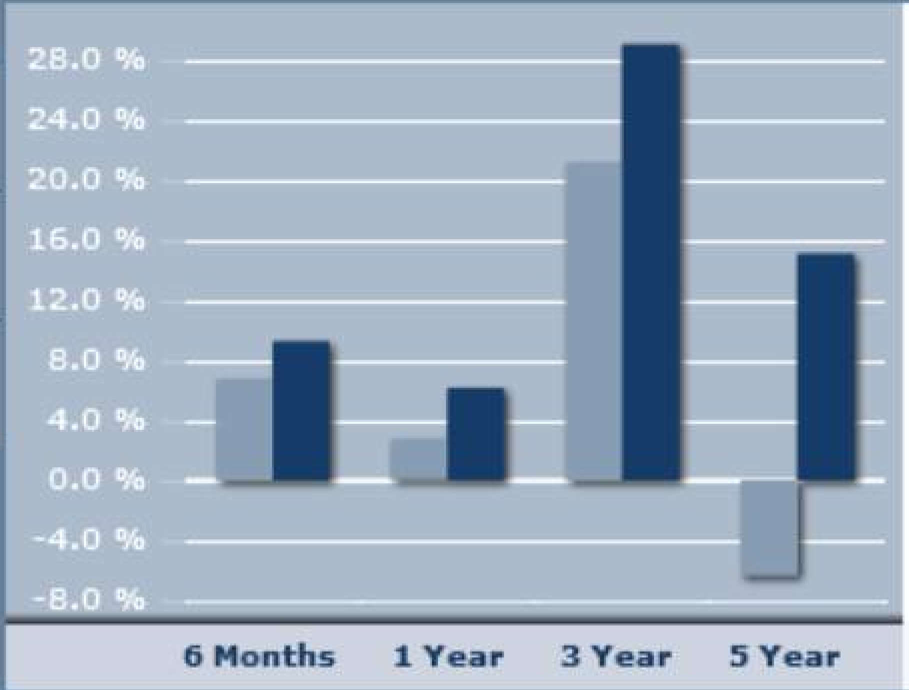
Cumulative Performance to month ending May 2012

AXA Financial Model Portfolio 2 - Cautious



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Sector average ■ AXA Financial Model Portfolio 2 - Cautious

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4. The Active Versus Passive Decision

- Active Managers attempt to beat the market by using:
  - Stock picking - 50% Chance of being right after charges.
  - Market timing – No one can reliably predict the future, it should come as no surprise that the overwhelming evidence suggests market timing is a losing proposition
  - Markets tend to have bursts of large gains (or losses) that are concentrated in a relatively small number of trading days

4. The Active Versus Passive Decision

Fees Matter - Nobel Laureate William Sharpe

- "As a group Active managers must always underperform passive managers".
- This is because investors as a whole can earn no more than the total return of the market (there is only so much juice in an orange).
- Since active managers' costs are higher it follows that the return after costs from active managers as a group must be lower than that of passive managers.

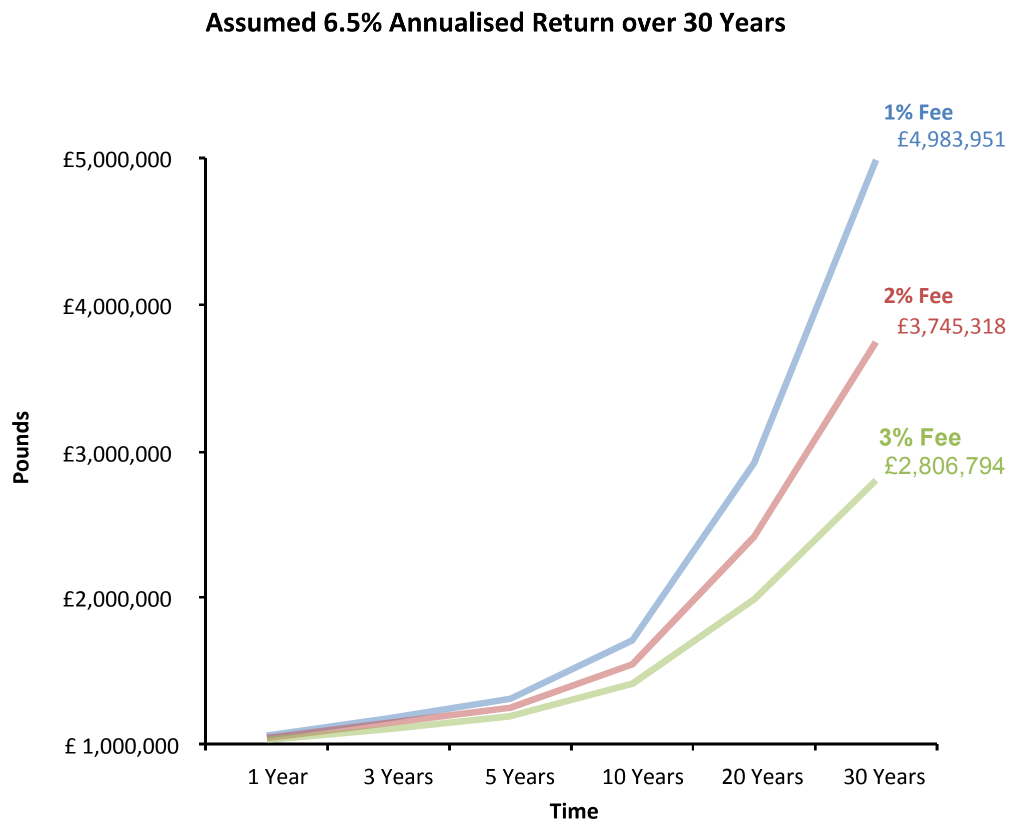
4. The Active Versus Passive Decision

- The Higher Costs of Active Managers can be broken down into three categories:

1. Higher Manager Expenses due to higher research and front loaded commissions
2. Increased turnover they tend to over trade which means more brokerage commissions
3. Greater Tax Exposure – e.g. Holding Direct Bonds in an after tax portfolio can lead income tax on income and CGT on gains.

Fees Matter

- Fees matter.
- Over long time periods, high management fees and related expenses can be a significant drag on wealth creation.
- Passive investments generally maintain lower fees than the average actively managed investment by minimising trading costs and eliminating the costs of researching stocks.



For illustrative purposes only.

4. The Active Versus Passive Decision

- A Passive Approach to investing is more sensible, this is based on the belief that markets are efficient and extremely difficult to beat.
- One method of passive investing is called indexing, which involves the manager purchasing all of the securities in a benchmark index in the exact proportions as the index.

4. The Active Versus Passive Decision

- The manager then replicated the results of that benchmark, index less any operating costs.
- The most popular benchmark index is the S&P 500, which is comprised of 500 US large cap stocks that currently make up about 70% of the US market capitalisation of the US stock market

5. The Rebalancing Decision

- If equity markets enjoy a period of strong return, it is possible that a 60/40 stock/bond portfolio could drift to a 70/30 mix.
- Left alone your portfolio will have a higher risk level at what could turn out to be a market high point
- By rebalancing back to the 60/40 mix you started with you can maintain your desired level of risk and expected return

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Cumulative Performance to month ending May 2012

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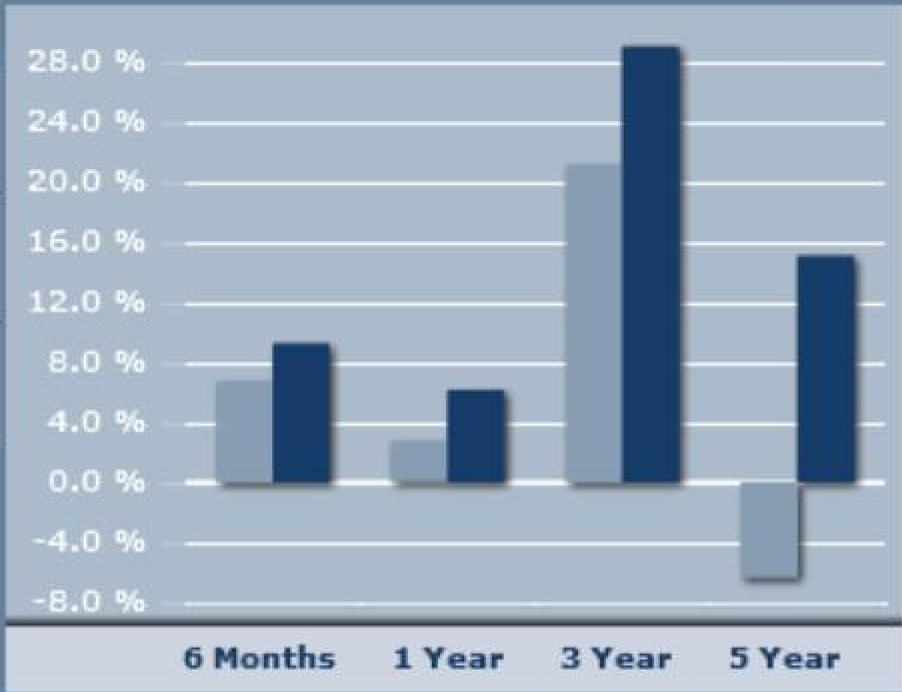

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5. The Rebalancing Decision

- Rebalancing is an automatic way to buy low and sell high, without your emotions getting in your way.
- Rebalancing can be accomplished by either adding new money to your portfolio and investing in Fixed Income or by selling some equities and reinvesting the proceeds into fixed income to bring the mix back to 60/40
- Rebalancing in After Tax portfolios may trigger a taxable event.

Investing in Ireland

Product	DIRT	CGT	Income Tax	Div With Tax	Pension / Life Levy
SSAP (Penison)	No	No	No	No	Yes 0.6%
Life Co. Pension	No	No	No	No	Yes 0.6%
Life Co. Investment Bond	No	Yes	No	No	Yes 1%
Directly Held Bonds	No	Yes	Yes	No	No
Directly Held Equities	No	Yes	Yes	Yes	No
Approved Retirement Fund	No	No	Yes	No	No

Disclaimer

- The contents of this presentation does not in any way constitute investment advice.
- Please consult with an Certified Financial Planner before making any investment decision.
- Further Reading:
  - – The Investment Answer – Dan Goldie CFA, CFP
  - – A Random Walk Down Wall treet – Burton Malkiel

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