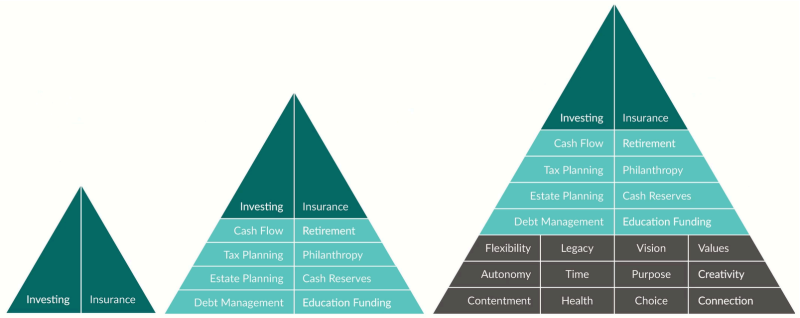
Wealth Management

Financial Professionals

Working In and On The Practice

Evolution of Wealth Management



What is Wealth?

- Time Capital
- Social Capital
- Intellectual Capital
- Financial Capital
- Physical Capital

Types of Financial Professionals

- Certified Financial Planner
- Wealth Manager
- Portfolio Manager
- Robo-Advisor
- Financial Consultant/Coach
- Insurance Agent

Terminology Spotlight: "Basis Points"

In finance, a basis point (bps) is an unit of measure used to describe the percentage change in the value of financial instruments or the difference between two interest rates.

- 1 Basis Point (bps) = 0.01%
- 100 Basis Points = 1.00%

The Wealth Management Process

- Holistic Wealth Management: The industry is moving beyond just "investing and insurance" to include legacy, vision, values, and even "financial therapy".
- Robo-Advisors and AI: While technology has commoditized technical skills and lowered fees (e.g., 25–50 basis points), human advisors remain essential for managing relationships during market downturns.
- The Seven-Step Financial Planning Process: A core takeaway from the lecture is that modern wealth management is inseparable from financial planning. This systematic process ensures that technical advice aligns with the client's life circumstances.
    - Understand Personal and Financial Circumstances: This involves "fact-finding" and gathering qualitative data (e.g., family dynamics) and quantitative data (e.g., assets/liabilities).
    - Identify and Select Goals: Distinguishing between what the client wants and what they need.
    - Analyze Current Course of Action: Evaluating if the client's current strategy will meet their identified goals.
    - Develop Recommendations: Creating a strategy that addresses gaps in the current plan.
    - Present Recommendations: Communicating the plan clearly to the client.
    - Implement Recommendations: Taking action on the agreed-upon strategies (e.g., opening accounts, purchasing insurance).
    - Monitor and Update: Regularly reviewing the plan to account for market shifts or life changes (e.g., a "health scare" or "inheritance").

Working with Clients

Model	Old	New
Focus	Product Selection	Process & Behavior
Standard	Suitability	Fiduciary
Role	Money Manager	Behavioral Architect
Value Driver	Market Access	Customization & Coaching

Investments in Practice

Traditional Investments

Active vs. Passive Strategy: The "Efficiency" Paradox

Core Concept: The transition of the U.S. sector market toward semi-strong form efficiency, making "alpha" (excess return) increasingly difficult to capture after fees.

- The "Fee Hurdle": In sector funds, the "quality" of active management is often negated by the expense ratio. Research (Fan & Lin, 2020) shows that even top-tier families like Fidelity have seen historical outperformance fade in the last decade.
- Professional Application (Fiduciary Duty):
    - Core-Satellite Model: Use passive ETFs for broad market beta (low cost) and reserve active management for inefficient "satellites" (e.g., emerging markets or small-cap value).
    - The Concentration Risk Factor: Passive indexing can lead to unintended over-exposure (e.g., the "Magnificent 7" dominating the S&P 500). Active management acts as a "risk-mitigation" tool here, even if it doesn't always beat the benchmark on price.

Fixed Income: Bond Funds vs. Individual Ladders

Core Concept: The choice between these two is a choice between Total Return (Funds) and Liability Matching (Ladders).

Bond Funds (The "Evergreen" Asset):

- Pros: Instant diversification, professional duration management, and high liquidity.
- Cons: Interest rate risk is perpetual. There is no "maturity date" where you are guaranteed your principal back.

Bond Ladders (The "Cash Flow" Asset):

- Pros: Eliminates "Sequence of Return Risk." By holding to maturity, the investor ignores market price fluctuations and focuses on the contractual par value.
- Cons: Higher transaction costs for small investors; "reinvestment risk" if rates fall when a rung of the ladder matures.

Behavioral Finance: The Risk Tolerance Correlation

Core Concept: Risk tolerance is not a static trait; it is a "pro-cyclical" variable heavily influenced by recent market performance.

- The $r = 0.70$ Correlation: Guillemette & Finke (2014) identified that measured risk tolerance moves in tandem with the S&P 500.
- The Valuations Paradox:
    - Market Peak: High P/E ratios (expensive) = High Risk Tolerance (Investors want to buy).Market Trough: Low P/E ratios (cheap) = Low Risk Tolerance (Investors want to sell).
    - Fiduciary Challenge: The advisor must act as a "Psychological Anchor." Rebalancing is technically a "contrarian" act; it requires selling what is performing well to buy what is "hurting."

Alternative Investments

The RIA Channel and Advisor Skepticism

A key theme discussed was the evolution of the *Registered Investment Advisor (RIA)* channel:

- The "Skeptical Advisor": Modern RIAs are "highly skeptical" and have a "just the facts" attitude toward fund selection.
- Thought Leadership: Wholesalers must provide real value in the investment domain rather than just practice management.
- Vehicle Selection: Advisors are moving away from traditional mutual funds in favor of more efficient or specialized vehicles like **ETFs** and **CITs**.

Market Realities & Alternative Investments

Why "traditional" planning is changing:

- Shrinking Public Markets: The number of public companies has plummeted since the mid-90s (from ~8,000 to ~4,000).
- The Private Shift: Companies are staying private longer to avoid the "rigors of quarterly reporting" and market scrutiny.
- Democratization: Access to Private Equity and Private Credit is moving down-market to the "mass affluent" level.

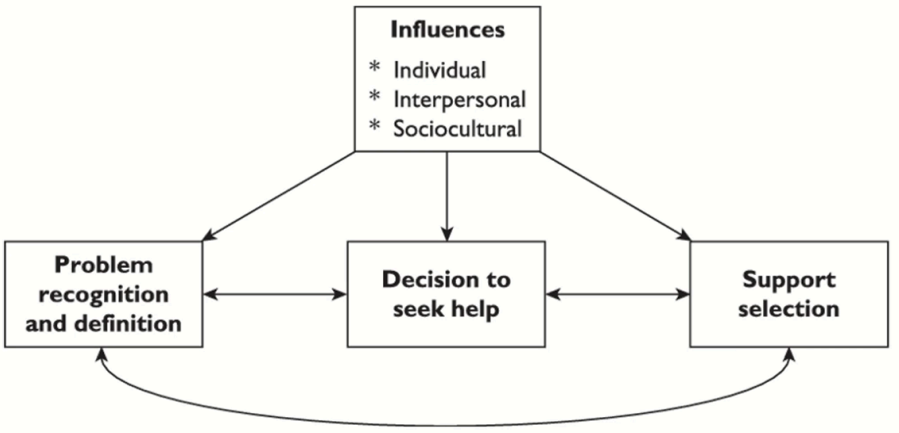
Behavioral Finance Application

The importance of managing client psychology during periods of market volatility.

- Defined Outcomes: Using structured notes or buffered strategies to keep clients from panic-selling.
- Planner Bias: The need for advisors to recognize their own biases (e.g., being "asleep at the wheel" regarding digital assets/crypto).

The Business

Client Service Model



- Asset Allocation: What you own
- Asset Location: Where you own it

Growing the Business

Advanced Asset Location & Retirement Accounts

Roth vs. Pre-Tax Matrix:

- Young/Lower Income: Favor Roth 401(k) or Roth IRA contributions due to lower current tax brackets.
- Mid-Career: Often agnostic; tax brackets are typically in the 20% range.
- High Income: Favor pre-tax options if in the 30% tax bracket or higher.

The "One Arrangement" Rule: To the IRS, you have only one IRA "arrangement," regardless of how many separate accounts you hold.

Employer-Sponsored IRAs:

- SEP IRA: Employer-funded only; allows contributions up to 25% of earnings (max $72,000).
- Simple IRA: Requires employee contributions with an employer match; easier to administer but has a lower limit ($17,000) and a "weird" two-year rule.
- 529 Plans: These offer state tax deductions (in Utah) and tax-free growth. New rules allow converting up to $35,000 to a Roth IRA, provided the account has been open for 15 years.

Strategic Charitable Giving

Charitable giving is a tool for both legacy building and tax efficiency.

- Appreciated Securities: Donating stocks directly avoids capital gains taxes while providing a deduction for the full market value.
- Donor-Advised Funds (DAF): Allows a donor to get an upfront tax deduction, invest the funds, and then "advise" grants to charities over time.

Split Interest Trusts:

- Charitable Remainder Trust (CRT): Pays income to the donor for life; the remainder goes to charity.
- Charitable Lead Trust (CLT): Pays income to the charity first; the remainder goes to heirs (ideal for permanent assets like real estate).

Estate Planning & Transfer Taxes

The goal of the U.S. transfer tax system is to prevent the creation of "permanent nobility" by taxing the transfer of wealth.

- Federal Exemptions: Current limits are approximately $15 million per person (30 million per couple).
- Gift Tax Exclusion: You can give $19,000 per year per person without reporting it to the IRS or affecting your lifetime exemption.
- Generation-Skipping Transfer Tax (GST): A tax applied when wealth bypasses children to go directly to grandchildren, ensuring the government doesn't lose out on a generation of transfer taxes.

Longevity & Retirement Phases

Retirement is statistically about 8,000 days and moves through four distinct behavioral phases:

- Honeymoon Phase: High excitement and freedom.
- Big Decision Phase: Novelty wears off; focus shifts to purpose and long-term housing.
- Longevity Phase: Increased focus on medical expenses and caregiving.
- Solo Phase: Managing life after the loss of a partner.

Managing the Business

Trust is defined as a "confident reliance on someone when you are in a position of vulnerability". In financial planning, trust is often high for individual advisors but low for the industry as a whole.

Key Drivers of Complete Trust

Research identifies five specific beliefs that separate "moderate" trust from "complete" trust. An advisor must ensure the client believes they:

- Understand their specific financial needs and concerns.
- Fully grasp their future goals.
- Provide genuine peace of mind.
- Explain difficult concepts clearly.
- Prioritize the client's family needs first when making recommendations.

Hurley's 10 Factors of Trust

Trust is a decision-making process influenced by 10 factors:

- Individual Factors (3): Result from the client's own personality, culture, and risk tolerance.
- Situational/Relational Factors (7): Include the advisor's perceived capability and "benevolent concern".
- Real-World Application: An advisor might be technically brilliant, but if they are unpredictable (e.g., missing deadlines), trust will erode because consistency is a primary driver of predictability.