Effective Asset Allocation is Fluid

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Today's CPAs should be prepared to discuss investment strategies with their clients. Because clients regard their CPAs as trusted business advisors, it is not a surprise that many look to their CPAs for advice or tips on investing.

Good investing generally requires all portfolios have a strategy. The strategy is ideally constructed from the stated goals of the portfolio owner(s) incorporating their risk tolerance(s) and current market conditions. Surprisingly, some investors think that a strategy can be created at the beginning of the creation of a portfolio, and then followed until the end of the portfolio. This, however, does not make any sense.

When embarking on a long journey, which investing should be, the investor should expect to encounter many different conditions. A single asset allocation should not be expected to optimize portfolio performance over a wide range of economic, market, and personal conditions.

Given the above discussion, consider the term "long-term investing (LTI)." LTI usually comes up when investments are losing money. Then, the advisor calls up LTI as a way of maintaining the support of clients and others when a particular strategy is not working. In other words, he knows more than the market does, so if you'll just "ride out" this "bad spot" by using LTI, you'll again become convinced of his brilliance.

People often hate to admit they're wrong. If the reasons for buying an investment are incorrect or change, people still hate to admit they made a mistake. So, suddenly, a short-term trade becomes a long-term investment. However, continuing to lose money under the rationalization of LTI will eventually make one a "non-investor."

Finally, a client often brings up LTI when he really doesn't want to take the time to evaluate new allocations. Such a client would want the time and energy spent making up the initial asset allocation to last forever.

Strategic and tactical allocations of an investment portfolio must be fluid in order to optimize the stated goals of the owner(s) and be consistent with their risk tolerances. The goals of the portfolio must be paramount when designing the portfolio strategy. Nevertheless, even portfolios with different goals and strategies should react to changing market conditions in similar ways. When the portfolio strategy becomes less effective due to changing market conditions, it only makes sense to tactically change market segment allocations.

In conclusion, investors and those who advise investors should keep the following points in mind. First, don't be hamstrung by "sound bites" that sound like good advice but aren't. Second, changing market conditions force the strategy and tactics of a good portfolio manager to change. The key point is that in order to meet client goals for any portfolio and be consistent with his risk tolerance, the strategy and tactics used must be fluid and market-condition appropriate.