

Awareness of Investment Basics

There are some basic points that all investors need to be aware of when agreeing to a long term wealth management relationship. The most important things you need to have a **basic** understanding of are the following.

- Investors need to understand the **fundamental nature of assets** (cash, fixed interest investments and equities), their risks and how their risks change over time and, to make their decisions based on these facts. Otherwise they will not be able to make an accurate assessment of their attitudes to risk.
- They need to be aware of the **major differences** between the various investment styles and disciplines and the portfolio theories that may underpin their portfolios. A good manager or advisor will explain these major differences, albeit with a bias towards their own styles and preferences.
- They need to be aware of the risks of **long term depletion of capital** and how this risk can be managed within their portfolio. Most investors will end up depleting investment capital to some degree to meet their financial needs; the degree to which capital will be depleted will also be dependent on withdrawal rates and the maturity of the market and the economic cycle, so investors will also need to be aware of these risk factors.
- In order to safely manage risk and return, managers of your financial security will need to either manage or at least know the **disposition of all assets and financial needs** over time.
- **The impact of costs and fees** on investment risk and return over time: the cost of many products and services can invalidate their rationale for being. In many instances investors would be better off holding static allocations of low cost indexed based investment vehicles than taking high cost active alternatives.
- The impact of a portfolio **structure inappropriately aligned** to financial needs, in terms of ability to cope with significant market and economic risks, on investment risk and return over time.
- **Everybody wants more return to less return, more security of capital to less security of capital and more certainty of return to less certainty of return.** Unfortunately, if you want to out perform the market, or have less risk than the market, or have more income than the market, you need to accept the risks associated with these demands.
- There are in fact **three key risks** that an investor has to understand before they can make a decision about the portfolio structure and investment strategy most suited to them. The financial services industry tends to focus primarily on one risk when assessing an investor's aversion to risk.
- The industry has a poor record in personalising portfolios to meet financial needs over time and managing the risks to the ability of assets to meet needs irrespective of market and economic risks – even more so in the light of market performance since the late 1990s. This is a central issue in the financial services industry. TAMRIS calls this the portfolio problem.
- Conflicts of interest exist at every level of the wealth and asset management process. Some are obvious such as being remunerated by commission while others are subtle but no less important. Given this, not all communication from product providers, institutions or advisors is going to be fully transparent and wholly in the investor's interests.

- Investors also need to be aware of the regulatory climate; just what are the legal and regulatory responsibilities of their advisors, portfolio managers/investment counsellors with respect to the advice and portfolio management being provided and just what are the investors' responsibilities?
- Investors need to be aware of the full nature of the service being provided by their advisors, portfolio managers and investment counsellors.
- Investors also need to be aware of weaknesses in the regulatory structure of the financial services industry: weaknesses in regulation impact transparency of communications made to investors and may impact the integrity of services and products provided by the industry.

A good advisor will be able to provide you with explanation of these factors as well as access to more detailed explanation.