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Recently, Institutional Investor Events organized the Second Annual Integrated Wealth Management Forum in New York. *The Journal of Wealth Management* is an integral part of the event, as we work to select those speakers who should be invited to present their research and findings. We would like to help make the forum the central annual event for the wealth management industry, serving, like a medical symposium, as the venue where all relevant new material is presented once a year in front of clients of the industry and peers. Last year, we did publish a few of the most thought-provoking presentations and are planning on doing so again this year. In fact, we believe that combining in-person presentation with appropriately peer-reviewed articles best serves the development of our industry. We therefore invite all our readers to let us know what topic they feel most needs to be covered and we will undertake to work with potential researchers in the field to try and make these presentations happen.

The Forum, which was particularly well attended, really offered a number of interesting insights, among which three key issues seem to dominate.

The first relates to the importance of soft issues. The wealth management industry, influenced as it often and rightly is by its institutional counterpart, has made much progress dealing with the quantitative and objective aspects of the problem. Yet we are only beginning to scratch the surface of a number of soft issues whose successful handling will likely make the difference between real success and failure.

- This starts with the need for clients to learn to understand themselves, as a very first step by being aware of the fact that they are subject to a number of biases, preferences, and related needs to live with the consequences of their decisions.
- Equally important is the need for all service providers to make a determined effort to understand the needs of their clients. While numerous organizations will argue that this very effort is what makes them different, the reality is that the conflict is real between the economic need to find solutions that are scalable and can thus be leveraged across a large client base and the requirement for each investor to feel that his or her portfolio is appropriately tailored. The focus on tax-efficiency was a first challenge in that direction and technology has helped many managers provide what effectively amounts to mass-customization.

THE JOURNAL OF WEALTH MANAGEMENT

• The next such challenge may well be the need to develop more flexible and sensible strategic asset allocation processes as well as investment approaches that recognize the importance of "traveling on the road to optimality." This is needed to address the frequent lack of "sustainability" that characterizes many current approaches to strategic asset allocation. This requires integrating the quantitative framework of modern portfolio theory and the qualitative makeup of our own behavioral biases.

• Client education is the last, but not the least critical need. Clients of our industry are understandably leery when they see service providers provide so-called education that, seemingly coincidentally, tends to reinforce whatever selling proposition is on the table. Though quite a number of organizations truly attempt to provide objective education, it is often hard for clients and prospects to discern between those who really have their interests at heart and those who are more interested in their bottom line. The need is clear for industry participants and client organizations to work even harder on this crucial issue.

The second major takeaway from the Forum is that the industry has in fact grown substantially over the last 10 years and is further maturing. This is both heartwarming in that it demonstrates that the needs that a few pioneers identified many years ago have finally been recognized and that successful businesses can be built serving those needs.

• This forces us to recognize that what was pioneering work as recently as 10 years ago is now pretty much common practice. Consider the focus on tax-efficiency, the increasing use of non-traditional strategies in portfolios and even the growth of both family and multi-family offices. Yet one cannot rest. Indeed, we need to keep asking ourselves how we can improve further. The example of so-called hedge funds is a useful, but not unique illustration. Many of these strategies started with a few very gifted managers identifying inefficiencies in the market place and seeking to take advantage of them. Often, these inefficiencies rested on incomplete analysis of information and high transaction costs. The substantial flows of new monies in these strategies, together with the increased effectiveness and availability of computing techniques and information flows may well have served to arbitrage these spreads away. Yet, there are new inefficiencies that should be investigated. Consider the disintermediation of many parts of the banking sector, the lack of appropriate evaluation of the value of liquidity, the arbitrary investment universe segmentations that provide useful discontinuities …

• This maturation of the industry is naturally leading to increased complexity. The first obvious indicator is in the complexity of the array of products offered. Yet this is only a beginning, as, barring a sudden (and from a number of perspectives welcome) change in the tax code, the use of derivative instruments is bound to increase, in part to enhance tax-efficiency. There is also considerably more information and thus insight on the very end markets that the industry is serving. This presents a much needed set of guideposts both to service providers who can segment their markets and thus more effectively align clients and services and to clients themselves who should find that work useful in forming rational expectations of the products and services that the industry may offer to them, given their own financial, demographic, and even geographic circumstances. A common element of these maturation trends is the ever-growing need for more flexible and reliable technological solutions. Consider how many master custodians offered on-line access 10 years ago and how much of an industry standard that electronic interface has become!

The last takeaway seems to be that research should be prioritized on three principal areas, in order to be as effective as possible.

• If it is true that a critical first effort for our industry was the focus on tax-efficiency (as one of the major distinguishing factors between institutional and individual investors), it should be true that the next crucially needed piece of this puzzle is the development of a more effective policy formulation process. The seminal work of behavioral finance specialists has provided us with a solid theoretical framework, within which it is now important to build a process combining soft issues and technology. Strategic asset allocation that ignores the major need for investors to "stay with the program through thick and thin" is bound to fail. Finding ways to make the process real and thus understandable to individual investors is essential, failing which we will continue to have a broadly dissatisfied client base that reacts to market movements rather than anticipates them. And a belief that individuals will simply have to learn the

THE JOURNAL OF
WEALTH
MANAGEMENT

mean-reversion properties of capital markets may well prove accurate over the very long term, but will unlikely be rewarded in a more realistic intermediate-term horizon.

• An equally important focus must be on the portfolio construction process. With strategies that are increasingly complex and the need for a taxable individual to consider simultaneous—rather than sequential—optimization, processes that integrated the various strategies with and alongside one another are key to solving the problems of our clients. Some way to help manage the mix between market and manager risk on a continuing basis, to help understand the various interactions across different strategies from an after-tax standpoint, and to combine a variety of approaches or tools to achieve one set of goals are just three of the most immediate needs one can identify.

• The final research focus should be on the perennial topic of client and provider education. Note that we do expect both clients and providers to need to learn to deal in and with that market. Developing relatively simple and yet powerful education tools could very well be another of these areas where technology can play a major role. As individuals, we are indeed more likely to respond favorably to processes that involve some practicality, rather than relying on the old tested theoretical jargon! Service providers also need to be taught how to work with individuals in need of wealth management services and in particular how to develop a team that bridges the multiple specialized disciplines that are involved.

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This Winter 2004 issue of *The Journal of Wealth Management* comprises articles covering three broad disciplines. Our regular readers will no doubt notice that the articles in this issue of the Journal tend to be somewhat more quantitatively oriented than is usual here. This is not a change in editorial policy. We continue to seek articles that are as relatively easy to read as possible, to cater to the wide diversity in our audience. Yet the topics covered in this issues often require the use of more advanced mathematics and we felt that intellectual honesty and plain integrity made it necessary to bend our rules when needed to make sure that our readers have access to the most current insights. I would also add that we are gratified by the significantly greater interest many members of the academic community seem to show in our Journal and welcome them.

We start with three important pieces related to the issue of strategic asset allocation. William Reichenstein offers an interesting perspective on the question of the definition of risk, showing that after-tax risk actually has some path dependency to it. Cris Lewis and Frank Caliendo revisit the issue of asset location, from the point of view of seeking to maximize the value of one's estate. Then, Moshe Milevsky considers the important issue of portfolio rebalancing, from the point of view of the risks associated with breaking desired weights with illiquid assets.

The next three articles continue to contribute to the debate on so-called hedge funds. Jean Brunel starts with a review of the role of hedge funds in portfolio allocation, discussing the lack of homogeneity in that universe, illustrating the puzzling features of many hedge fund strategies, and recommending the use of a model different from the standard mean-variance. Claus Huber and Helmut Kaiser then evaluate and discuss the option-like structures of several hedge fund strategies. Finally, Greg Gregoriou investigates whether hedge funds of funds show significant market timing skills.

Our last two articles cover specific investment areas. First, Vincent A. van Antwerpen, Janwillem P. Engel, Harry M. Kat, and Theo P. Kocken offer thoughts on bond duration management in a potentially rising interest rate environment. Finally, Mark Anson presents an interesting review of the current state of the private equity industry, drawing important implications for the prospects for and pitfalls in that asset class.

With this issue, we are fortunate to have two eminent members of the academic community join our advisory Board, both of whom have already made significant contributions in the form of articles or peer reviews. Harry M. Kat is professor of risk management and director of the Alternative Investment Research Centre at the Cass Business School, City University in London. William Reichenstein is the Pat and Thomas R. Powers Chair in Investment Management at the Hankamer School of Business at Baylor University. We welcome them, thank them for their continuing support, and are looking forward to an even closer working relationship.

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Editor