Innovate Software Consulting Inc

AMERICAN ACADEMY OF FINANCIAL MANAGEMENT

Wealth Management

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What is Wealth Management?

Wealth Management is a discipline that incorporates financial planning, Investment portfolio management and a number of financial services. It is a professional service it can also encompass all parts of a person's financial life. Wealth management is done by wealth managers. Wealth managers can be MBAs, CFAs, certified financial planners or any credentialed professional money manager who works to enhance the growth and income. Investors must have already accumulated a proper amount of wealth for wealth management strategies to be efficient and effective. It can be provided by large company entities, independent financial advisers or multi-licensed portfolio managers. Their services are designed to focus on high-net worth customers. Wealth Managers use their experience in estate planning, risk management and legal specialists, to manage the holdings of high net worth client. Wealth managers must contain a current profile of client holdings. Wealth management is integrated processes for helping clients manage their wealth. It involves huge a wide range of services and the services depend upon each investor but the condition is that services should include investment management, financial planning, retirement, Estate planning, tax planning, debt management and cash flow. It is based on the long term relationship with the customer. It results in deeper customer relationship which leads to increased profitability and more client referrals. Wealth management offers wealth managers the opportunity to cross-sell a huge range of services and products to each customer as appropriate. Wealth management is an emerging sector.

Wealthy people come from all walks of life and make their money all sorts of ways. Some are doctors or lawyers, and others are small business owners operating roofing businesses or a chain of dry cleaners. Some inherited their wealth, and others are corporate middle-level executives who've saved and invested, making millions in the process until they became rich. And yet others are high school dropouts who started their own companies, eventually selling them for handsome sums. No matter what their background, though, the wealthy have various asset management issues that are different than the average employee with a basic compensation package and a few hundred stock options in the firm he works for. To address these more complex asset management issues, the financial services industry has created private wealth management departments that offer a host of products and services for the very wealthy. Private wealth management, also called private banking, is a specialized branch of the investment community that provides one-stop shopping for a whole host of products and services needed by wealthy folks—typically defined as those who have liquid assets of more than over $1 million.

Features / Functions of Wealth Management

- **Creating Income**

  It is the first job of private wealth managers to help create, from among various investment strategies, income or growth sufficient for the everyday needs of their clients. Because the wealthy often need to live solely off of their investments, today private wealth managers must use a variety of investment techniques to help clients create enough income to live off of every year. The wealth managers must ensure that their clients get enough income from their portfolios that the clients are able to meet up to their expenses and also be able to fulfill their Dear-to-Life Objectives.

- **Paying Taxes**

  Another problem wealthy clients often encounter is taxes. No one likes paying taxes. While managing large pools of assets, small differences in tax rates can translate into big changes in after-tax returns. Various types of investments used are treated and taxed differently. The private wealth manager must balance assorted types of investments to create the most tax efficient combination for the client. The clients might also be subjected to inheritance taxes. Accordingly, private wealth managers must help their clients select from a number of products or legal entities, such as trusts or insurance, to preserve their estates after their death.

- **Asset Protection**

  In today's society, people with money are sometimes targeted with lawsuits just because they happen to have money. So, an increasingly popular area of practice for private wealth managers is called "asset protection," which helps the wealthy guard against losing money in civil lawsuits. There are several techniques used to protect assets, including trusts laws and foreign, offshore banks. Advocates of asset protection methods contend that making their clients impervious to lawsuits doesn't just protect assets, but also prevents lawsuits from even happening.

- **Risk Management**

  There is risk involved in everything we do. Risk is nothing but the potential of a loss. It is the duty of wealth managers to ensure that their clients face as minimum risk as possible. The risk can be in various forms. It can be market risk, business risk, liquidity risk, credibility risk, fortune hunters risk, interest sensitivity risk, estate risk, etc. The private wealth managers must keep in mind all risks while giving solutions to their clients regarding management of the wealth. The wealth manager should try to minimize risk as much as possible and in turn increase safety of the portfolio.

- **Estate Planning**

  The wealth managers must also plan as to how the will be created in order to match the transfer wishes of the client. Confidentiality is the main concern in this function of the wealth managers. The wealth managers must evaluate the need for power of attorney, health care declaration, and living will. They should ensure proper titling of assets and set up appropriate beneficiary designations so that it meets the client's needs. The necessary funds must be established and appropriately funded.

- **Miscellaneous**

  The above provides a glimpse of the more common types of services that private wealth management firms offer their clients. But some firms also offer other unique services, which vary from firm to firm. Some of these might include:

- ✓ **Philanthropic Services:** Giving to charities in a planned way.
- ✓ **Agricultural Services:** The transfer and or management of farms or ranches for families.
- ✓ **Auction And Art Services:** Providing services allowing clients to purchase, value, sell and manage collections of fine art.
- ✓ **Appraisal Services:** Valuing and managing unique assets like intellectual property.
- ✓ **Securitization Services:** Providing ways to monetize any assets that provide a stream of cash flow, like movie or book royalties.

Segments for Wealth Management

- Stocks.
- Stock Options.
- Bonds.
- Funds.
- Insurance.
- Cash flows.
- Education Planning.
- Tax Planning.
- Estate Planning

Benefits of Wealth Management

It is possible to revise risk profiles multiple times.

- Safe, Reliable and scalable for clients.
- Online access to returns.
- Consolidated view of cash flows.
- Online proposal generation.
- Keeping accounts up to date.
- Monitoring changes in client's portfolio.
- Multiple account reservations.
- Multiple investment scenario analysis and
- Allocation of Assets

Key Market Trends

On a broader level, trends witnessed across the wealth management industry can be classified into two categories, namely, HNWI-specific and firm-specific trends.

HNWI-specific Trends

a) Client trust in advisors and wealth management firms has been improving during the post-crisis period.
b) Growth in HNWI wealth and population over last three years has been higher in emerging markets as compared to that in developed markets.
c) The proportion of young HNWIs (< 45 years) has been gradually increasing across regions mainly due to the rise in number of young entrepreneurs and also due to the increase in wealth transfers towards younger generations.
d) HNWI's demand for philanthropic planning and products is rising steadily.

Firm-specific Trends

a) Wealth management firms are struggling to create scalable business models while facing rapid changes in the financial markets.
b) The wealth management division is becoming central to universal banks' operating models.
c) Regulatory oversight on the wealth management industry is increasing across the globe.
d) Emerging markets (especially Singapore and Hong Kong) are emerging as new offshore centers for wealth management.
e) Behavioral finance is going main-stream as wealth management firms leverage it to better serve their clients.

IPI Model of Asset Allocation

IPI is the Institute of Private Investors, which is a consortium of top 200 richest families in the US and their wealth managers. It is a very simple model which follows the basic principle that money should be invested with respect to the projected needs of the client. This model takes into account the need and "fitment" of almost all types of Asset Classes, namely, Fixed Income; Equity; Real Estate; Commodities; Precious Metals and Jewels; Art, Antiques and Collectibles; and Private Equity.

Wealth Management Process

- **Personal Details**

  This is the first step involved in the process of Private Wealth Management. The client is asked personal details about him and his family, which will help in knowing about the client and also influence the investment strategies to some extent.

- **Current Asset Allocation**

  The next step that follows procurement for personal details is the procurement of details regarding current investment. This is important as the wealth managers need to know where the client has invested its assets currently in, as this investment will be re-structured in order to optimize the performance of the portfolio so that the needs of the client can be fulfilled.

❖ **Need Analysis & Goal Setting**

The client is then asked about his needs in life. This refers to the goals/dreams he wishes to achieve in life with the money he earns up to retirement. The aspiration of clients may vary with their lifestyle. The client is required so specify the amount of money that he would like to spend on the particular aspiration and what is the expected time by which he wants to fulfill the particular aspiration. The time plays a very important role here as the Wealth Manager needs to ensure that the client has the required amount of money at the appropriate time.

❖ **Assumption & Expectation**

Every Wealth Manager needs to take certain assumptions and expectations in his mind before preparing a financial plan. These assumptions play a very crucial role as they help in devising the strategies for re-structuring the investment of the client in order to achieve better results. These assumptions form the basis on which the entire financial plan is made. They may vary from one Wealth Manager to another as it is very subjective in nature. The assumptions are made for:

- Life expectancy
- Return on different investment mix
- Rise in income
- Expectation from capital markets
- Expected inflation rate

❖ **Quantifying your aspiration**

The next step is to allocate the amount required to fulfill the aspirations of the client. The client needs to tell his Wealth Manager as to how much money he wants to keep aside for the particular aspiration if that aspiration was to be fulfilled as on the current date. On the basis of this amount the Wealth Manager will calculate the future value of this amount keeping the time and inflation rate in mind. This is the amount that the client will require to fulfill his aspiration on a future date. But since the Wealth Manager need to keep a sum of money aside from the current date, he needs to find out the present value of this future value if he expects a fixed rate of return from his income and investments. This is important in order to find out the SIP amount for the particular aspiration.

❖ **Mapping Corpus Required**

The Wealth Manager then takes into account the corpus required in total by the client. The point of focus in this step is to see if the current state of the income of the client is enough to match upto his expenses. This is done by making a Balance Sheet for the client. The assets side includes all investments made by the client and also the present value of the net future income of the client upto retirement. The liabilities side consists of the present value of all the aspirations he wishes to achieve, the present value of household expenses upto retirement, and current mortgages (if any). Also, a Distress Balance Sheet is prepared. This Balance Sheet is used to see if the current net income and investments is enough to match the expected expenses of the client, IF anything happens to the client at the current date and is unable to earn. The Distress Balance Sheet is similar to the Current Balance Sheet, with the only difference that Present Value of Future Income is replaced with the Life Insurance that is available for the client. It helps in checking the security of the client's family in a situation wherein he is not there. Also, it is seen if both the Balance Sheets are Positive/Negative. A Positive Balance Sheet is one in which the total of Assets is more than the total of Liabilities.

- **What are limitations in the Balance Sheet?**

The Wealth Manager needs to check the limitations in the Balance Sheet. He needs to see if the current income is enough to take care of the future needs and aspirations. A SWOT Analysis of the Balance Sheet is done in order to see the limitations in the Balance Sheet. It also helps in checking if there is a need to restructure the asset allocation in order to enhance the returns of the investment. It is also important to see the amount locked in debt/ insurance as debt instruments are generally not liquid. The next step is the investment strategies that the Wealth Manager suggests to his client which would help them in increasing the performance of the portfolio. The suggestion must be made keeping in mind the returns and risks involved with each type of asset.

- **Implementation of strategies**

The suggested strategies are decided by the Wealth Manager and communicated to the client. The client then reviews the strategies and recommends changes in accordance to his needs. A joint strategy is then implemented by the Wealth Manager. It involves investing in the decided instruments and fulfilling the formalities in order to optimize portfolio performance. A regular review of the portfolio and client needs is important in order to make the financial plan more effective. The Wealth Manager must check if any of the objectives of the client has changed. He must also review the income and expenditure details regularly as such changes will have an effect on the Balance Sheet and hence the entire Financial Plan. Also, it is important to see if the securities invested in are giving the desired results. If the performance of securities is below expectation and/or there is a security whose performance is better, then the investment must be changed accordingly so that the performance of the portfolio can improve.

Process of Wealth Management includes:

- **i.** Step1: Finding Facts
- **ii.** Step2: Investment Strategy
- **iii.** Step3: Allocation of Assets
- **iv.** Step4: Structuring Accounts
- **v.** Step5: Structuring Implementation.
- **vi.** Step6: Communication
- **vii.** Step7: Annual review & Monitoring.
- **viii.** Step8: Refine Strategy.

First step to be considered is to create a profile of customer in which personal details, current financial situation and family circumstances. In personal details they involve income, savings, investments, retirement, tax status, Family. In step2 investment objectives and risk tolerance is to be undertaken. Then assets are allocated and it’s all about getting the balance right. After this wealth management need to consider the account structure that best suits the client. To be highly communicative is quite necessary because it is an important aspect of client-wealth manager relationship. They organize regular face-to-face meetings. Then after monitoring, it is essential to refine the strategies.

Conclusion & Summary

Investors prefer to invest in portfolios having low risk along with high returns. Based on a client's needs, it is important to construct a viable portfolio keeping in mind all Dear-to-Life Objectives" so that a client is satisfied with the returns that a private wealth manager can ensure keeping in mind the value of investment and expected returns. The general misconception is that people believe that it is more important to choose the correct form of security, but it is more important to choose the correct form of asset class rather than choosing the right security. Thus it becomes vital to invest funds in a manner that it diversifies risk. High net worth individuals, today are slowly moving towards investment through private wealth management companies so that their money multiplies efficiently rather than investing it themselves in conventional forms of investment.