# Each client should have a distinct, customized portfolio of their own

The fourth 'D' of the investment strategy involves the creation of a distinct portfolio that is consistent with the risk profile and other objectives of the investor. Of these, the most important factor is the investor's risk tolerance.

In order not to treat all investors with different risk profiles the same way, the model utilizes three broad risk profiles. An investor's risk profile is based on the minimum and maximum exposure to stocks and bonds, as well as on the general characteristics of mutual funds to be selected from any one-asset class.

## Risk Tolerance

• **Conservative/Cautious Investor.** For a conservative investor, minimum and maximum allowable percentages are specified, respectively, for stock and bond funds. That is, at all times an investor of conservative risk profile is expected to invest a minimum percentage of the total assets in bond funds; simultaneously, it is not recommended that this investor invest more than a certain percentage of the total assets in stock funds. In addition, this investor may be advised not to invest in, say, global bond funds or emerging market stock funds that represent riskier investments.

• **Assertive/Aggressive Investor.** An assertive investor is expected to hold at all times no less than a minimum percentage in bond funds and no more than a maximum percentage in stock funds. In addition, an assertive investor is expected to invest in those categories of stock and bond mutual funds that carry higher degree of risk. For example, such an investor may hold small cap mutual funds and high yield or global bond funds, which might be out of bounds for a conservative investor.

• **Moderate/Balanced Investor.** A moderate investor has a risk profile that lies midway between a conservative investor and an assertive investor. Such an investor is advised to maintain a range which is no less than a minimum percentage of the total assets in bond funds and no more than a maximum percentage in stock funds that fall between the relative percentage specifications of the two groups described above. Again, there are some restrictions that might be placed on the nature of mutual funds that can be selected for a moderate investor.

## Other Objectives

In addition to risk tolerance, the portfolio must also satisfy other objectives of the investor. These objectives (including risk tolerance) can be articulated by using the acronym, SMART:

**S**hort-/long-term financial objectives
**M**onetary needs - short-/long-term
**A**ttitude toward life's values
**R**isk tolerance
**T**ime horizon

## Investment Policy Statement

For achieving best long-term results, for each client an Investment Policy Statement is developed, which spells out in detail the client's objectives covered under the acronym, SMART. These objectives are periodically updated, and the investment portfolio is revised to accommodate these changes.

## Dynamic One: Kaleidoscope

Dynamic One begins with an analysis of the economy as well as the individual segments of the financial markets and, ultimately, selects those stock, bond, and money market mutual funds, and individual securities, that are appropriate for each investor with a specific risk profile.

Over the long run, the ultimate objective of a Dynamic One is both to enhance the investment return of a portfolio and reduce its risk level through:

• Allocations based on changes in the economic and financial environment
• Diversification among different asset classes
• Diversification between domestic and foreign assets
• Diversification among stocks of different market capitalizations
• Selection of mutual fund managers with impressive track records
• Determination of the risk tolerance of every investor
• Construction and management of an investment portfolio especially designed for each individual investor
• Development of an Investment Policy Statement

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teria include:

- Performance during rough years (such as 1987, 1990, and 1994); the extent of risk assumed by the fund manager as measured by standard deviation and beta;manager's tenure; manager's style (such as value, growth, top down or bottom up, specialization, etc.) and alpha.

The final choices are made from among two or three top-rated fund managers identified under each of the sub-categories. This is accomplished on the basis of subtle – and sometimes not so subtle – differences that may exist among the finalists. For example, if a manager has a topdown approach that concentrates on macro-economic variables whereas another manager has a bottom-up approach that begins with an analysis of individual stocks, then both managers could conceivably be selected.

• **Performance Test for Bond Funds.** With suitable modifications, procedures followed for selecting stock mutual fund managers are applied to the selection of bond mutual fund managers.

• **Performance Test for Money Market Funds.** Money market funds are selected purely on the basis of short-term returns.