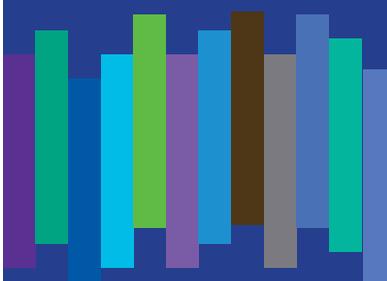


**INVESTMENT PRINCIPLES**  
INFORMATION SHEET FOR INVESTORS

# PUTTING IT ALL TOGETHER



12

## **IMPORTANT NOTICE**

The term "financial advisor" is used here in a general and generic way to refer to any duly authorized person who works in the field of financial services, including the following:

- Investment brokers
- Mutual fund brokers
- Scholarship plan dealers
- Exempt market dealers
- Portfolio managers
- Investment fund managers
- Life insurance agents
- Financial planners (F.Pl.)



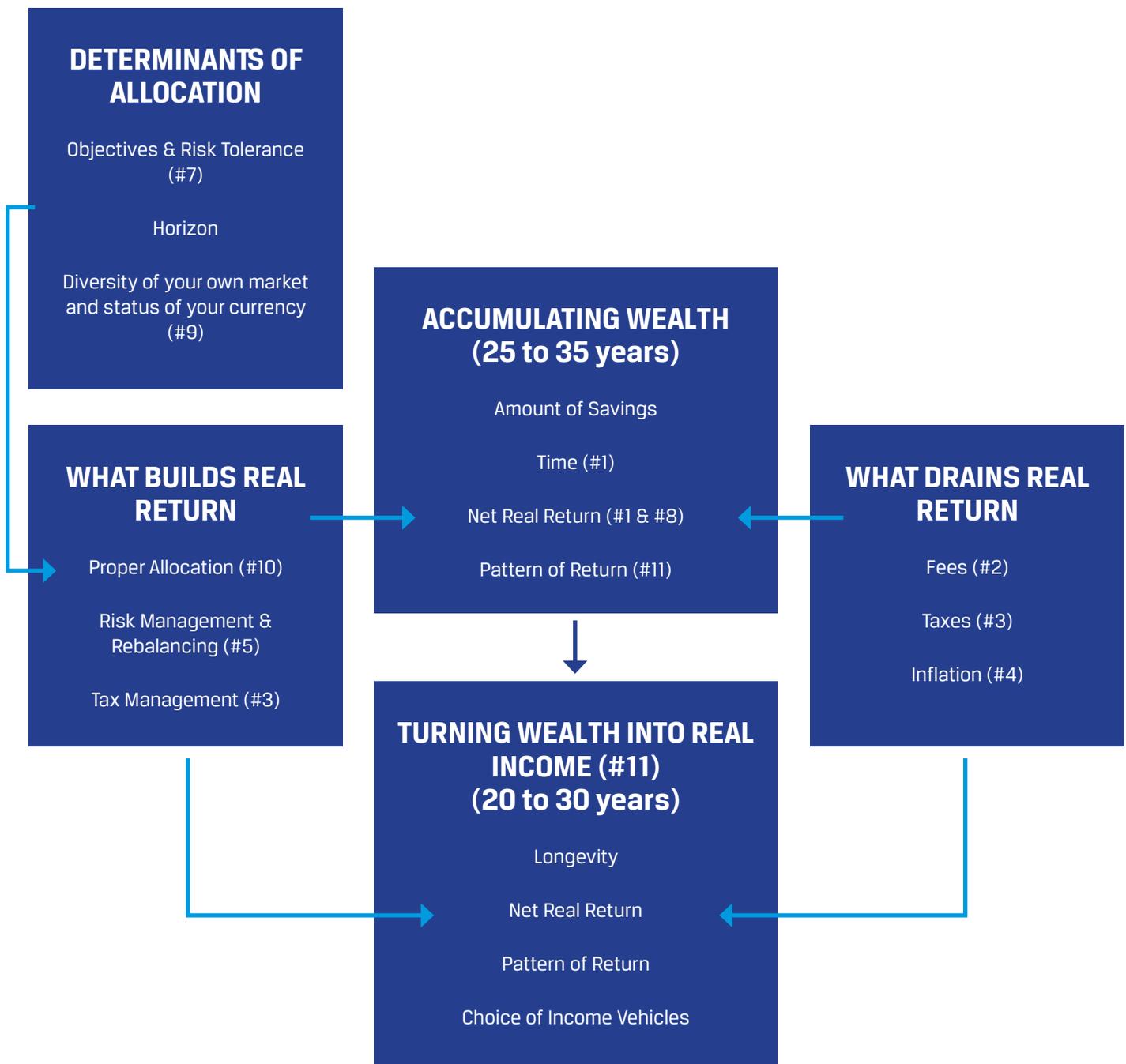
Copyright © 2016 CFA Montreal. All rights reserved.  
Reproduction in whole or in part without written permission of  
CFA Society Montreal is prohibited.

# PUTTING IT ALL TOGETHER

We have covered a significant amount of material in the previous documents. It may seem overwhelming, but the main dimensions of the retirement process can in fact be easily summarized. This last document in this educational series seeks to present the main dimensions of the investment process in a clear framework.

**THE RETIREMENT FRAMEWORK**  
**ADVISORY AND SUPPORT TOOL (#6)**

This chart summarizes the many dimensions of the retirement planning process. The number in parentheses refer to document that covers this aspect.



## WEALTH ACCUMULATION

There are four dimensions that will determine the amount of wealth accumulated from private savings at retirement. Obviously, there is how much you have saved over time, how long you have been saving (Document #1), what net real return you have obtained from your investment portfolio (Documents #1 and #8), and what pattern of return occurred during your savings period (Document #11). If you are lucky enough to benefit from a strong return environment after you had already accumulated a significant amount of savings (for example, in the last 10 years of your accumulation period), your overall wealth will significantly benefit.

## WHAT DRAINS REAL RETURN

Whatever real return you were hoping to realize, it will have been reduced by the amount of all-in fees that you paid (Document #2), by taxes in the case of your taxable account (Document #3), and by inflation if inflation was greater than you expected (Document #4). It is important to pay reasonable fees.

## WHAT BUILDS REAL RETURN

The real return you will achieve is, in a large part, a function of appropriate investment planning and consistency of execution. Document #10 discusses the process of building a diversified portfolio. As indicated, performance is strongly influenced by the rebalancing and risk management strategy (Document #5). An appropriate rebalancing strategy will help reduce the performance drain resulting from higher portfolio volatility. Finally, making full use of tax-exempt or tax-deferred accounts and properly allocating your asset classes between taxable and non-taxable accounts in order to minimize the total amount of taxes is essential to long-term performance (Document #3). While taxes drain wealth accumulation, their effect can be mitigated.

## DETERMINANTS OF ALLOCATION

Knowing how to build a diversified portfolio is essential, but which portfolio risk/structure is appropriate to each investor? Of course, how much risk we can take depends on our investment horizon (a longer horizon can support greater

risk), but in the end, it is a function of the objective and risk tolerance of the investor. Greater income at retirement justifies taking more risk, but the anxieties of some investors related to poor performance may justify taking less risk. It is a delicate balance and is discussed in Document #7. Finally, the structure of a portfolio (its allocation to different asset classes) is strongly influenced by the diversity offered by the home equity market of the investor and by the nature of its currency. Is it a currency that tends to appreciate in good times and depreciate in bad times or is it the reverse (Document #9)?

## TURNING WEALTH INTO REAL INCOME

Many factors relevant to the accumulation of wealth also apply during the decumulation process. However, return uncertainty can have greater consequences as we approach the decumulation phase, because the wealth we have accumulated becomes our main source of income. We can no longer expect a salary. There is uncertainty in terms of the net real return the investment portfolio may generate but also uncertainty related to the pattern of returns. Document #11 explains how much income can be expected from our savings and the impact on retirement income of unfavorable performance that occurs soon after retirement.

## ADVISORY AND SUPPORT TOOL

Finally, for most individuals, the complexity of the entire process requires the support of a trusted advisor (Document #6). There is also an added consideration that we did not address. Research shows that our ability to benefit from learned skills and knowledge declines in our 60s, while our ability to solve new problems starts declining even before, in our 20s. To the question: "If five people all have the winning numbers in the lottery and the prize is two million dollars, how much will each winner receive slightly more than 50% of individuals in their 50s had the right answer but less than 10% of individuals in their 90s did.<sup>1</sup> The level of cognitive impairment, excluding dementia, reaches nearly 30% for individuals in their 80s and 40% for those in their 90s. Cognitive changes explain why basic financial literacy skills decline, on average, in our 60s, and this process worsens gradually in our 70s, 80s and 90s. As we age, we are less likely to make rational and informed decisions and, unfortunately, we are more prone to be taken advantage of.

<sup>1</sup> Agarwal, Sumit; Driscoll, John C.; Gabaix, Xavier; and David Laibson (2009), The Age of Reason: Financial Decisions over the Life Cycle and Implications for Regulations, Brookings Papers on Economic Activity.

All of this makes the role of a trusted, accredited advisor and the need for proper planning even more important as we age.

Like in most human endeavor, the difficult part is to get going. These documents provide sufficient knowledge to get you started. The road to financial comfort is difficult, but you are now better equipped to reach your objectives.