The Journal *of*
Wealth Management

Editor's Letter

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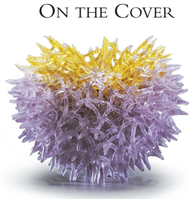
On the Cover



Glass, 2009
10 × 13 × 13 inches; 25.4 × 33.02 × 33.02 cm

Anja Isphording *(Born 1964) is a German glass artist living and working in Vancouver, Canada. The artist is known for her small-scale objects, with each holding their own unique form and saturated vibrant colors. Her glass pieces are reminiscent of basic molecular structures, honeycombs or environmental elements such as coral reefs, but their biological reference remains ambiguous. Inspired by nature, the artist is able to develop the illusion of forms in nature without directly reproducing it. Her work has been exhibited in both solo and group exhibitions across North America and Europe. This piece and others by this artist are available through Heller Gallery in New York, New York.*
Visit www.hellergallery.com to view more works by this artist.

A while back, we discussed a family's need to be both intellectually rigorous and honest to maximize the chances that it will be successful in managing its wealth. At that time, we were principally bemoaning the fact that the average sound bite had gone from 30 seconds to 6 seconds in the previous 20 years or so. We argued that this shortening made it incredibly difficult to argue anything with any degree of complexity, as 6 seconds is a pretty short time to go beyond mere platitudes. Little did we know then that we were only witnessing the early phases of a process that has gone considerably further! This exposes families to all kinds of pitfalls, whether dealing with issues related to financial markets or considering family education or more qualitative topics.

Recently, I had the opportunity to reflect on the good, but also on the bad, that comes with instant communication, under the generic header of social media. Stating the obvious, social media have played and are still playing a considerably constructive role in helping individuals in situations in which free speech is in any way limited. Clay Shirky, who wrote a book entitled "Here Comes Everybody," makes the case that the current environment substantially reduces the role of classical organizational structures and shows how a number of political events involving crowds would not have been possible without the ability to use social media to get the message around. This certainly sounds true, and one should therefore be careful not to throw the baby out with the bath water.

Yet, linking Shirky's notion of the role of social networks with two other phenomena that we have all observed in the last 50 years, one can begin to appreciate the nature of the new challenge. The increased superficiality of the press and the tendency for many to mix entertainment into serious endeavors is making it hard for many individuals to distinguish between reality and perceptions. More importantly, it is easier for many individuals to get caught in a game in which words take on a meaning that they were never meant to have. The example of the communist world before the fall of the U.S.S.R. has become a classic: Although most political systems in the countries behind the Iron Curtain surely did not allow for free elections, most of these countries' names still contained the term "democratic"! This allowed many a left-leaning politician in the West to argue that the Communist system was democratic. Now take that example and apply its principle to the present: Words have taken on a life of their own, whether they are true representations of reality or not; thus, no debate can be had without these words being brought to the fore, effectively reducing a reasonable question to a sophistic shadow of itself.

Imagine how this can play havoc in the everyday world of the wealthy, or even the mere affluent. Painfully slow economic growth is now presented as solid and a success. Without facts to place data in the appropriate perspective, the casual observer is not equipped to discriminate between statements or rationales that are sensible and those that are not. This affects a whole slew of family wealth management endeavors. How can one perform a reasonable analysis of financial asset prospects if one does not know how to conduct such an analysis or where to find the data that would allow one to prove or disprove a recommendation? How can one manage to shepherd family values from one generation to the next when the overall environment painfully excoriates anything that smacks of some degree of conservatism? Note that the point here is not to suggest that conservative values or positions are by definition superior; rather, it highlights the notion that these values or positions are not necessarily inferior either.

Families that we have seen deal with this successfully so far have adopted three simple approaches that others might want to emulate:

1. ***Make sure not to demonize the present, but ensure that intellectual honesty and rigor remain the key drivers of conversations within the family.*** This follows the principle that one should not antagonize others or make them feel inferior when one wishes them to become a part of a process. It requires them to develop sufficient internal resources to have all the facts—or at least as many of them as reasonably feasible—before launching into any conversations.
2. ***Encourage all participants to argue their views and coach them to find missing facts if they do not have them.*** This falls under the principle that it is always better to help people by replying to a question they ask rather than having them sit down and listen. It requires all family members to be taught to respect other people's views and yet to value supporting facts over mere opinions.
3. ***Make sure that the senior or more respected members of the family model the appropriate behavior.*** This follows the classical principle that it is always better to suggest that others should do as we do, rather than as we say. This is a more difficult feat as soon as one gets away from the creator(s) of the wealth; wealth creators indeed seem to enjoy a natural legitimacy that can allow them to take a few shortcuts—though they probably are better off not taking them.

It would be wonderful if our readers or members of the board of advisors would take on this topic and develop it further, as the novelty of the times in terms of the superficiality of many arguments and the absence of knowledge of many facts are two of the most dangerous obstacles that families face.

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The Summer 2016 issue of *The Journal of Wealth Management* remains well diversified, with articles covering quite a few aspects of the spectrum that have been of interest to our readers.

The first three articles cover three different topics, all of which revolve around the three main axes of wealth management: strategic asset allocation (investment planning), philanthropic planning, and wealth transfers (or dynastic planning). The first, by Peter Mladina, suggests that, as assets serve a lifetime of financial goals, optimal lifetime asset allocation should be goals-based and multi-period, requiring customization according to goals, human capital, and risk preference. The second, by Paul Schervish, Sean Davis, Richard Cosnotti, and Kirby Rosplock, notes the challenge experienced by very large donors and discusses the need for and offers an approach to, making a greater impact with that wealth. The third, by Robert Gordon, David Joulfaian, and James Poterba, looks at how estate executors managed the difficult choice that they had in 2010: either file an estate tax return and possibly pay a 35% estate tax on amounts above $5 million or instead choose to have assets pass without an estate tax but with a carryover in basis. They conclude that, on average, executors made the right decision in voluntarily filing an estate tax return but in the end paying little or no estate tax.

The next four articles cover the broad topic of equity investing. The first, by Gary Smith, revisits the classic question as to whether great companies do or do not make great investments, building on the findings of Anderson and Smith, who found that a portfolio of the 10 most admired stocks outperformed the overall market by a substantial and statistically significant margin over the first 22 years that the

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list was compiled. The second, by Steven Dym, proposes a consistent, fundamental approach to help investors summarize the salient characteristics of a company and relate them to stock market valuation. The third, by Keith Black and Edward Szado, observes that mutual fund managers may implement a variety of trading strategies using exchange-traded equity and equity index options. They note that the literature has previously documented superior risk-adjusted performance of mechanical index strategies and suggest that a large sample of listed funds provided strong risk-adjusted performance with returns similar to the S&P 500 Index from 2000 through 2014, with substantially less risk as measured by standard deviation or beta. Last but not least, the article by Kenneth Washer, Randy Jorgensen, and Robert Johnson focuses on the perception that stock market volatility has increased over time and provides a rigorous examination of historical stock price volatility over the period 1926 through 2014. The authors suggest that there has been no discernable change in return volatility except when volatility is measured based on daily data.

Our last three articles focus on different topics again, each effectively constituting something of a category of its own. The first, by Brian Henderson, Joshua Mallett, and Craig McCann, looks into nontraded real estate investment trusts (REITs)—registered investment companies formed for the purpose of investing in real estate and marketed to retail investors—suggests that they substantially underperformed traded REITs for a variety of reasons that are investigated and discussed. The next piece, by Daniele Lamponi, focuses on the important topic of currency exposure in minimum-variance equity portfolios and suggests that both typical approaches (fully hedged or fully unhedged) to currency management have their pitfalls, suggesting that a better constructed global minimum-variance portfolio has exposure to stocks and currencies that lies between fully hedged and fully unhedged solutions. Our last article, by Monica Singhania and Neha Saini, keeps to our tradition of looking at a typical challenge viewed from the perspective and in the environment of an emerging market: It examines the impact of foreign institutional investment on India's SENSEX returns and exchange rate and vice versa.

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Editor