IN THE NEWS

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Sound Portfolio Strategy

For many years now, my family has taken an annual trip to the beach. North Carolina's Outer Banks region has been the popular destination of choice for some time. Each year, my father takes time to map out a road route. His strategy is to get from point A to point B without getting lost. The family also discusses the best departure time based on past experience. Their strategy? To avoid as much traffic as possible.

In the same vein, a retailer such as Wal-Mart almost certainly strategizes each year about its inventory for the Christmas season. They want to stock in appropriate amounts and carry what they believe will be the hottest-selling items. These decisions (and many more to be sure) help to create maximum profitability during the strongest retail season.

Shouldn't investors also have a sound strategy for managing their investment portfolios? The decisions made in this regard can have lasting impacts on an individual's future financial well-being and his or her ability to attain financial goals and objectives. All too often, individual investors lack a well-crafted portfolio strategy, and if you ask them what they own or why they own it, you're liable to be answered with silence. Individual investors can also be prone to taking advice, whether from friends or family members or the media, without context. I'd like to suggest an approach, summarized below, that is multi-level and designed to reduce unintended risk.

Macro Strategy

By now, most folks who follow the world of finance know about the significant crisis facing the Eurozone, from sovereign debt to failing banks. For months now, the stock market's direction has hinged not on the fundamental financial positions of corporations, which largely impact the market's long-term direction, but on every macro headline, including those emanating from Europe and other sovereign nations who are facing severe debt and deficit issues. Given the impact these event risks can have on the market in the short term, investors may consider a portfolio strategy that begins by taking these macro indicators and trends into account. In this way, tactical investors can implement portfolio changes that may reduce risk during times of heightened uncertainty. Macro themes to monitor may include, for example, monetary and fiscal policy decisions, trends related to consumer confidence or technical indicators.

Asset Class & Sector Strategy

Having reasoned through a "big picture" strategy, investors may then consider asset classes and sectors they find most attractive. In early phases of economic recovery and expansion, more cyclically sensitive investment themes have historically delivered strong returns. In these instances, investors

may favor stocks over bonds or, from a sector perspective, industrial and materials investments. During periods of economic contraction, such as the one we recently experienced, an investor may seek to reduce portfolio risk by allocating more of his or her portfolio to fixed income investments or more defensively-oriented economic sectors such as consumer staples or utilities. If an investor believes in strong future growth from emerging economies, emerging market investments may be considered. Each asset class and sector decision, it can be reasoned, should be derived from the investor's macro perspective.

Investment Level Strategy

The final level of portfolio strategy would then be selecting the individual investments to construct the portfolio. Investors sometimes fall victim to making the investment level decision the first step in their process. If Jim Cramer likes a particular stock, for instance, an investor can fall prey to buying the stock without considering if he or she favors equities or that specific sector. Here again, the dispensation of financial advice must be taken in context. If purchasing equities, does the investor choose stocks, exchange-traded funds (ETFs), mutual funds or another vehicle? And what of fixed income – buy ETFs, mutual funds or individual bond positions, and what type(s) of bonds? These are among the final decisions to be made, and the advantages and disadvantages of each investment should be thoroughly reviewed, as well as consideration given to how investment types may complement one another. Investment level decisions should only be made after satisfactory due diligence and the deliberation of an exit strategy if the investment does not perform as expected.

The strategies described here do not suggest that investors can prosper by making changes that significantly alter the strategic design of their portfolios, because market risk cannot be wholly diversified away. As well, each investor should always maintain a diversified portfolio and a perspective on his or risk tolerance. Rather, this approach may allow investors to work from a macro to a micro level to help assist in investment decisions rather than the reverse. Investing in today's environment can be complex, where changes are swift. For those so inclined, seeking the advice of a professional may be instrumental in helping to develop a sound portfolio strategy that takes multiple variables into account but that is not swayed by the day-to-day machinations of a stock market that bends to no one.

Investing in fixed income securities involves certain risks such as market risk if sold prior to maturity and credit risk, especially if investing in high yield bonds, which have lower ratings and are subject to greater volatility. All fixed income investments may be worth less than original cost upon redemption or maturity.

Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Stocks offer long-term growth potential but may fluctuate more and provide less current income than other investments. An investment in the stock market should be made with an understanding of the risks associated with common stocks, including market fluctuations.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. These risks are heightened in emerging markets.

This article was written by Shawn Berwager, Portfolio Consultant with Econ Wealth Management, and provided courtesy of Steve Economopoulos, CFP®, ChFC®, Managing Principal and PIM Portfolio Manager with Econ Wealth Management. Investment products and services are offered through Wells Fargo Advisors Financial Network, LLC (WFAFN), Member SIPC. Econ Wealth Management is a separate entity from WFAFN.

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