UBS Wealth Way - How can you invest to meet your objectives?

UBS Wealth Way

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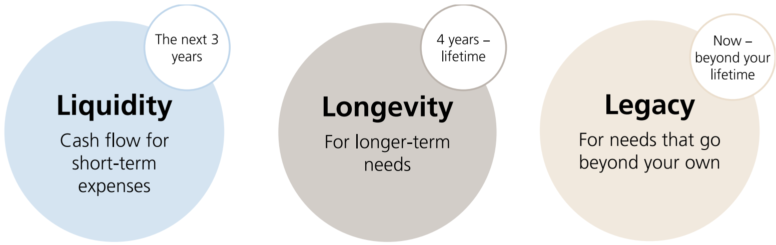
- UBS Wealth Way starts with questions and a discussion that helps focus on what's really important to you. The approach helps you organize your financial life into three key strategies: Liquidity—to help provide cash flow for short-term expenses, Longevity—for longer-term needs, and Legacy—for needs that go beyond your own.
- Together, these strategies can help to provide you with a clearer understanding of your objectives and the context that you need to stay the course during difficult markets.
- This report, will provide an overview of these strategies and address some of the factors to consider when deciding how to implement them to help you achieve your family's goals.

Introduction

This Liquidity. Longevity. Legacy. (3L) framework can help you to develop an investment strategy optimized for your goals and objectives. It can also help you understand clearly where your money is—and why. The clarity it provides enables you to stay focused on your long-term goals, no matter what the markets are doing. This is particularly beneficial during periods of high market volatility.

Disclaimer:
UBS Wealth Way is an approach incorporating Liquidity. Longevity. Legacy. strategies that UBS Advisors can use to assist clients in exploring and pursuing their wealth management needs and goals over different timeframes. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved. All investments involve the risk of loss, including the risk of loss of the entire investment.



To help **maintain** your lifestyle
- Entertainment and travel
- Taxes
- Purchasing a home

To help **improve** your lifestyle
- Retirement
- Healthcare and long-term care expenses
- Second home

To help **improve** the lives of others
- Giving to family
- Philanthropy
- Wealth transfer over generations

Source: UBS

Liquidity

Objective: The Liquidity strategy consists of resources that you need to meet your family's short-term cash flow needs, including regular income from employment or a pension, safe borrowing capacity, and investment assets earmarked for this purpose. The aim of the Liquidity strategy is to provide enough capital to give you the flexibility for greater risk-return potential in other portfolios. The strategy helps manage cash flow for near-term spending needs, usually for the next three years.

This approach should boost your confidence in maintaining your Longevity and Legacy strategies, regardless of what markets are doing. In other words, it should reduce the likelihood of making impulsive investment decisions with the remaining investment portfolio during periods of market volatility, which is important for maximizing long-term performance.

Strategy: To help you achieve your short-term goals, the assets in this strategy must be liquid with high price stability. The structure of the Liquidity strategy depends on two essential factors: 1) the ratio of regular income to regular expenses; and 2) the risk of not receiving the income or unforeseen expenses. The greater the uncertainty of your income or the risk of unforeseen expenses, the more you should set aside in your Liquidity strategy. The Liquidity strategy is also influenced by the risk profile of your Longevity strategy portfolio given the Liquidity strategy will typically be refilled by the Longevity strategy.

As a rule of thumb, around three years of expenses may be an appropriate amount to provide peace of mind during turbulent times that could entail periods of heightened volatility, potential interruptions of employment, or emergency expenses. Access to unemployment coverage, disability insurance, or other social coverage for unemployment further reduces the amount that must be readily available to cover recurring expenses. Furthermore, liquidity needs can also be met by taking a loan against a portfolio of securities and using the proceeds for external purposes.

In your Liquidity strategy, cash alternative solutions can be effective because they help to limit the potential for a mismatch between spending needs and the mark-to-market value of your Liquidity strategy. Such solutions consist of assets that typically yield more than cash deposits, but will necessarily involve a trade-off in terms of liquidity (the ability to withdraw money without any restrictions); market risk (the volatility of asset prices and the potential risk of capital loss); or counterparty risk (the potential risk of capital losses). (Read more: Cash Alternatives Liquidity Solutions, 2018, UBS). Particularly in Europe, where some cash rates are currently negative, investors need to give some thought to the risks and returns they are prepared to hazard in their Liquidity strategy. (Read more: Liquidity in a negative rates environment, 2020, UBS).

For instance, fixed-term deposits or money market certificates require investors to sacrifice liquidity in exchange for a higher yield. If you're willing to accept slightly lower liquidity, you may also receive higher yields in short-term corporate bonds from higher-rated issuers or select structured products, while still retaining some cash-like qualities. If you're willing to take on more credit or counterparty risk, investing in lower-rated short-term corporate bonds or depositing at lower-rated banks, for example, could potentially net higher returns.

To determine the optimal mix for your Liquidity strategy:

- First consider your short-term cash flow needs (i.e. the difference between your expected income and your expected expenses) and determine how much you need to set aside to provide peace of mind around risks to your Longevity strategy and fluctuations in your spending and income. In our experience, investors often need less than they expect in order to insulate themselves from these short-term risks.
- Second, pin down your risk appetite with regard to liquidity risk, market risk, and credit risk. Your ability and willingness to tolerate these risks will influence the choice of the most suitable Liquidity strategy solutions.
- Third, construct your Liquidity strategy bearing in mind your currency and country-risk exposure and applying the principle of diversification across different solutions, tenors, and issuers.
- Finally, since changing market circumstances may affect the attractiveness of different solutions, and as your income and expense patterns will likely change over time, you should regularly revisit your Liquidity strategy.

Benefit: The Liquidity strategy helps to provide confidence that your short-term needs can be met, even in volatile environments. It supports peace of mind, lowers the risk of panic selling, and allows the capital earmarked for your longer-term goals to grow regardless of short-term market conditions, empowering you to pursue your objectives with fewer disruptions.

Longevity

Objective: The Longevity strategy is focused on helping you meet your goals over your lifetime. Its aim is to ensure that you're invested in such a way that you have a high probability of meeting those objectives. The risk here is measured in terms of shortfall risk, in other words the possibility of not meeting one of your investment goals.

Strategy: "How should I invest? And how much risk should I take?" These are the most important questions you must ask when building your Longevity portfolio. The answers depend on your goals, the initial invested amount, and the expected cash flows. Your investment preferences and risk tolerance also affect the optimal asset allocation. You should select a Longevity strategy that maximizes the likelihood of meeting your objectives within these constraints.

Typical goals of the Longevity strategy often include securing early retirement, enabling relocation, or amassing funds to start new business ventures. Non-bankable assets can be incorporated into this strategy as long as they contribute toward achieving your goals. For example, if a residential home will eventually be used to finance a goal through rental income or a lump sum inflow from its sale, then it would be incorporated in the Longevity strategy. Assets that serve a consumption purpose should be omitted from the Longevity strategy. Human capital can also be incorporated by adding the expected salary income over the foreseeable future, and a sensitivity analysis can check how sensitive your plan is to employment fluctuations or interruptions. In general, a yearly review of your Longevity strategy is recommended in order to capture any changes in your circumstances or goals.

Example: Consider an investor with, say, two goals: funding their children's education and securing early retirement. The first step in defining a Longevity strategy would be to identify the appropriate amount that would be required to cover these expenses. It's important to take into account inflation expectations, potential currency mismatches, and the time horizon over which these cash outflows would take place. The second step would be to look at the likelihood of meeting these objectives with the selected investment strategy. Depending on the amount invested, the timing and magnitude of cash flows, and other factors mentioned, the optimal investment strategy may need to be more or less risky—or it may even be that available funds are not sufficient to achieve the goals within the boundaries of the investor's risk tolerance.

In our view, investors should err on the side of caution, but also bear in mind that they could adjust their spending along the way. We generally recommend targeting a probability of success above 85%. Investors with more spending flexibility could target a lower amount and those with less spending flexibility could fund their Longevity strategy to be more sure of success.

For entrepreneurs, we like to highlight the importance of assessing their Longevity strategies in combination with their business and its inherent risks. In our experience entrepreneurs tend to treat their business as a highly risky investment—and invest their liquid financial assets in a conservative strategy to offset this risk—or they ignore the business interest. Instead of these extreme approaches, we recommend a dynamic allocation, based on the ratio of liquid investable assets to annual spending. When this ratio is lower, more of the assets will need to be devoted to the Liquidity strategy, which naturally reduces the risk of shortfalls if the company needs to retain capital rather than distribute it as income. The higher the liquid assets/spending ratio, the more assets can be devoted to the Longevity strategy. In both cases, the Longevity strategy can be invested in a balanced or even equity-heavy allocation. Since most of the risk inherent in a private company is idiosyncratic, public equity market exposure actually diversifies the overall balance sheet, rather than adding more risk to the family's total wealth. (Read more: Uncommon success, wealth strategy for entrepreneurs and business owners, UBS 2019).

Lending may also be incorporated into the Longevity strategy. Taking a loan against the Longevity strategy and reinvesting the proceeds can help provide yield enhancement. In particular, in cases where higher returns are needed to meet goals, leverage could assist in meeting your objectives. Of course, leverage also changes not only the return but also the risk characteristics of your portfolio, so it’s important to identify the appropriate leverage ratio.

Benefit: By coordinating your Liquidity and Longevity strategies, your confidence in your long-term financial well-being should be secure even in times of financial market volatility and economic crisis.

Legacy

Objective: The aim of the *Legacy* strategy is to pass on assets that you do not need during your lifetime to the next generation, or to use them for other favored causes. So your Legacy strategy should focus on maximizing the value of transfers to future generations and to make a positive impact on society.

Structure: Once your Liquidity and Longevity strategies are adequately funded, you can invest the remaining wealth in your Legacy strategy. Traditional risk management considerations take on a different meaning for these assets than they do for the rest of the portfolio. For example, "sequence of return" risk is a largely irrelevant concept for a Legacy strategy that doesn't need to sustain withdrawals regardless of market conditions.

Such a horizon enables you to invest in a riskier portfolio with a high proportion of illiquid assets (where permissible by local jurisdiction) like illiquid hedge funds,private equity, infrastructure, and real estate. You may also want to incorporate long-term thematic investing funds to benefit from structural trends. Since the investment horizon extends beyond your lifetime, the daily ups and downs of financial markets should be less worrisome. Opportunistic views and tactical trade ideas may also be incorporated into the Legacy strategy given the objective of maximizing returns within an investor's risk boundaries. Life insurance offerings are worth considering given their role in liquidity and estate planning. Any assets intended for long-term consumption such as a holiday residence or an art collection may be included in the Legacy strategy. In addition to generating financial returns with your Legacy strategy assets, you may also be interested in deploying your capital to create positive impact on society and the environment. It should be noted that sustainable investing (SI) solutions may be incorporated in all strategies. In our experience, incorporating SI solutions can also be a great way to engage and bring in the next generation.

In the Legacy strategy, it's important to look at succession planning and the smooth transfer of assets. The aim should be to minimize family conflict, especially during challenging times such as divorce, sickness, or the movement of people or money across borders due to, for example, the migration to jurisdictions with a higher tax burden. Donations to charitable causes and contributions to foundations can also be incorporated in the Legacy strategy. Furthermore, the desire to expand a family business beyond a particular region may also drive a demand for Legacy plans to be based internationally.

Succession is a key topic for most families and one that deserves attention. Wealth succession is paramount for the preservation and stability of the family dynamics and fortune. Having such succession discussions early on is important. Involvement of heirs in investment decisions might also be beneficial in including—and educating—the next generation, as well.

Lending may also be incorporated to enhance the returns of your Legacy strategy. Taking a loan against the Legacy strategy and reinvesting the proceeds can help provide yield enhancement. In addition, lending can help provide diversification for a concentrated portfolio (e.g., single stock lending).

Benefit: A Legacy strategy helps you understand how much you can devote to goals that extend beyond your own lifetime. By separating these resources from the rest of your portfolio, you can confidently invest them to maximize growth for philanthropic causes and for future generations. Your Legacy strategy can also incorporate your passions and values, and helps to ensure that they will persist for generations to come.

Appendix

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