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Goals-Based Investing: Managing the Stability-Focused Experience

DECEMBER 2017

Snapshot

- Goals-based investing helps investors prioritize financial objectives, along with the time horizon for their goals.
- SEI utilizes a framework that distinguishes between growth-focused and stability-focused approaches.
- Stability-focused portfolios may be more appropriate for investors who prefer to specify such a target and optimize return against the drawdowns we might reasonably expect in a less favorable market environment.

Goals-based investing helps investors pursue different financial objectives with a distinct focus on each specific need and allows an individual to separate investments according to purpose and timeframe. We believe these defined goals make it more reasonable that each objective will be achieved and can help an individual optimize their allocation to risk based on the time horizon.

SEI utilizes a framework that distinguishes between growth-focused and stability-focused approaches.

Growth-focused portfolios are optimized on a traditional risk-return framework. These portfolios tend to be appropriate for longer time horizons, non-critical or aspirational goals and other situations where an investor is willing and able to assume a risk of capital loss without specifying a maximum loss target in advance.

Stability-focused portfolios may be more appropriate for investors who prefer to specify such a target and optimize return against the drawdowns we might reasonably expect in a less favorable market environment.

The resulting portfolios have maximum drawdown targets specified in advance. However, realized drawdowns may exceed these levels. We monitor the portfolios and employ a dynamic risk-mitigation process when actual drawdowns begin to approach those target maximums.

There are four key metrics we use to measure and monitor portfolio performance:

- **Drawdown budget:** the maximum drawdown target specified for each portfolio
- **Current drawdown:** the percentage difference between the portfolio's historic peak and current values
- **Drawdown cushion:** the percentage difference between current drawdown and maximum drawdown budget
- **Current drawdown risk:** the most up-to-date drawdown risk estimates for each portfolio under especially poor market conditions

The portfolios are monitored on an ongoing basis. Qualitative discussions begin once a portfolio has consumed 30%-to-50% of its drawdown risk budget. From there, we:

- Review current capital market assumptions (CMAs) for the underlying asset classes; if appropriate, CMAs are adjusted and the portfolio allocation is recalibrated.
- Adjust current allocations to bring current drawdown risk in line with the current drawdown cushion.
- Add risk back to the portfolio until the drawdown cushion fully recovers, at which point the strategy would once again be fully invested and rebalanced to its targeted allocations.

Current Status

The steady overall behavior of financial markets since the global financial crisis has kept stability-focused drawdown cushions fairly wide. Historically, this hasn't always been the case. Monitoring stability-focused drawdowns and standing ready to mitigate the risk of future losses is just one more way that SEI can help investors stay on course to pursue their investing goals.

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