

One Size Doesn't Fit All — The Advantages of SMAs

By Chuck Carlson, CFA
CEO, Horizon Investment Services, LLC

“One size fits all” is not an idea that usually sits well with consumers.

Just visit any grocery store. There's a reason you see more than 17 different mustards, over 100 different beverage brands, and at least 10 different toothpaste flavors.

Consumers want choices.

Consumers want customized solutions.

Consumers want bespoke.

Unfortunately, some of the most heavily-promoted investment products have adopted a “one-size-fits-all” approach.

Take target-date mutual funds. Target-date funds, usually offered in five-year increments, gradually adjust the mix of stock and bonds to become more conservative as an investor ages and approaches retirement. Investors typically buy target-date funds based on the year they plan to retire. It's a simple approach that has been marketed exceptionally well — target-date funds have captured more than \$3 trillion in 401(k) and other retirement portfolios, for example. But target-date funds basically key off one data point — expected retirement date. If you are 55 years old with three kids, still-massive student debt, no savings, and hopes of retiring in 10 years, you will receive the exact same investment as a 55-year-old who plans to retire in 10 years but who has no kids, no debt, a six-figure salary, and a seven-figure savings account.

Aside from the obvious — these two investors, despite sharing the same age and retirement date, could hardly be more different — fiduciary issues come into play when trying to ram a “one-size-fits-all” solution into the investment process.

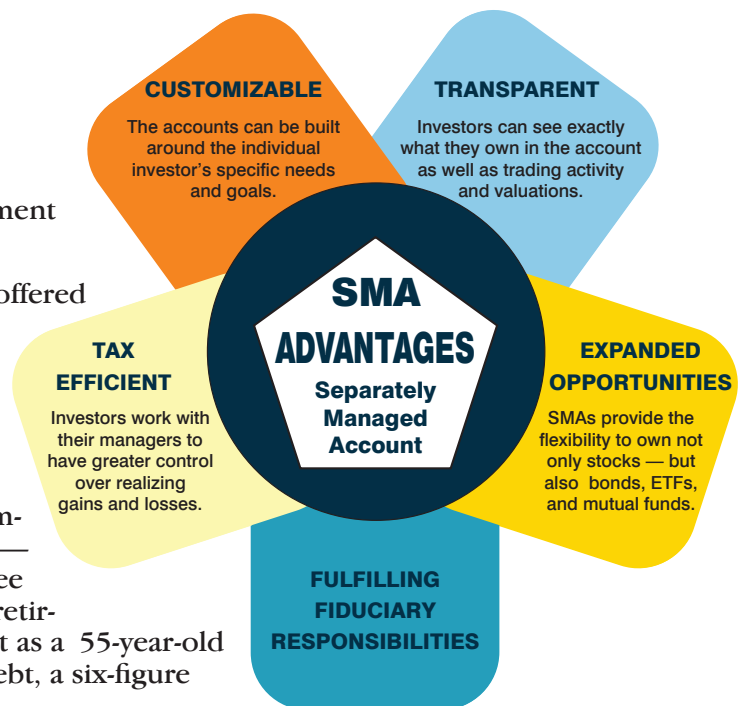
The good news is that the investment landscape continues to evolve, bringing more choices to individuals who want customized solutions.

Leading the charge are Separately Managed Accounts (SMAs).

SMAs are portfolios owned by an investor and typically managed by an investment firm, such as a registered investment advisor (RIA). Separately managed accounts are not “pooled” accounts, like a mutual fund. Rather, the account is set up and managed for the individual, with the individual owning directly each of the securities in the account.

SMAs offer a variety of advantages:

- ▶ ***The accounts can be built around the individual's specific needs and goals.*** Let's say an investor wants the specific portfolio to generate cash flow. An SMA can be constructed to produce the cash flow at the appropriate risk level. The ability to create customized portfolios is especially attractive for affluent investors who may have unique investment requirements.



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- ***SMA*** offer a certain tax efficiency not available in mutual funds. SMA holders can work with their managers to have greater control over realizing capital gains, for example. Also, the ability to “tax harvest” in SMAs — selling losers to offset winners — is a big advantage over mutual funds, which can lock unwanted capital gains on shareholders, even in years when the value of the fund has declined.
- ***The ability to mix and match investments in an SMA provides a high level of flexibility.*** Within a single SMA it is possible to own individual stocks, individual bonds, exchange-traded funds, and even mutual funds, thus expanding the opportunity set for the SMA manager to meet the investor’s goals.
- ***An underappreciated aspect of SMAs is the transparency they bring to the investment relationship.*** Investors can see exactly what they own, unlike in a fund. Knowing what is owned can be especially relevant for investors interested in socially-responsible or faith-based investing practices. Thus, for those investors, SMAs offer perhaps the best investment vehicle for achieving those goals.

Transparency. Tax efficiency. Customization. Expanding the opportunity set. Fulfilling fiduciary responsibilities. All of these benefits make SMAs an attractive alternative for investors.

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7412 Calumet Ave
Hammond, IN 46324-2692

1-800-711-7969

www.HorizonInvestment.com