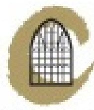

CATHEDRAL
Financial Consultants Limited

26 April 2016

Feature Article

Welcome to our Company Newsletter

Welcome to this, the first edition of our newsletter!

In our first article, we set out a few thoughts about the importance of the health and welfare of your business partners and how ultimately these factors can affect your business success. Then we take a look at how our own behaviours can sometimes get in the way of investment success!

Finally, there is a mix of content that we found on the web that we think will be of interest to you.

Best wishes!
Barry Oliver

Main Articles

How Well Are You Looking After Your Business Partner?

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The health and welfare of your business partner is a really important factor in your financial planning. After all, they have probably been working alongside you since you came up with the idea for your business, and also have shared the highs and lows as your business survived those difficult early years and has hopefully grown as time went on. Your partner has toiled alongside you, shared the stresses and hopefully you've built a business you're both proud of. It wouldn't have been the same, or indeed may not have happened without them.

Now I want to tell you a story about a situation we came across recently. Two business partners (let's call them Tom and Gerry) built a great manufacturing business in the Southwest of the country. They built a great business that supported them nicely and indeed also a small team of dedicated staff. Unfortunately Gerry developed a very serious medical condition and passed away after a very short period of time. Tom was of course devastated; the 2 men had been a great team working together, very reliant on one another and sharing everything down the middle. And that included having an equal share of the value of the business. They had never felt the need to formalise the situation, they were very trusted friends to each as well as partners.

After Gerry's death, his son who had just finished college decided that he would (with his mother's blessing) take his father's place in the business, minding what was an important financial asset to them. Tom was not 100% happy with this as he now had an equal business partner again, but not the one he had built the business with. The 2 partners tried hard to make it work, however they just had very different visions for the business. In the end, after real slippage in the business and quite a bit of bad feeling creeping in between Tom and Gerry's family, Tom managed to secure a sizeable bank loan and bought out Gerry's family.

Tom now owns all of the (smaller business), under pressure to pay off the loan and without his friend alongside him. And all of the angst and financial pain could have been avoided… Unfortunately, such

situations are repeated frequently each year around the country.

Business Protection

There is a range of business protection solutions available to help businesses survive the death or indeed the serious illness of someone that would result in a financial loss for a business. These solutions provide a number of benefits for businesses;

- They offer real peace of mind benefits to the directors or partners, as they remove the financial worries associated with the death or serious illness of a colleague.
- They remove the need for businesses or surviving partners to borrow money to buy out their partner's share of the business.
- They remove the need for a surviving family member to take the deceased's place in the business.

In the situation mentioned earlier, if Tom and Gerry had co-director's insurance to the value of their shares in the business on each other's lives, all the stress would have been avoided. When Gerry died, Tom's insurance policy would have paid out, and he would have been in a position to immediately buy out Gerry's share of the business for a fair price and keep control of it – which could have been agreed as a right for each of them when effecting the policies.

There are a number of different types of business protection solutions available to suit the different types of business structures.

Co-director's insurance

This would have been the answer to Tom & Gerry's issue! Each director insures themselves against the death of their partner, enabling them to buy out the partner's shares on death and/or serious illness. As an alternative, the insurance can be effected by the company itself.

Partnership insurance

Similar to the above, a partnership takes out insurance, protecting itself against the death or serious illness of an individual partner, enabling them to compensate the deceased partner's estate for their share of the partnership.

Key person insurance

This helps a business to minimise the impact of the death or serious illness of a key employee. The insurance can be used to quickly attract a replacement employee or indeed to pay off loans of the company that may have been guaranteed by the deceased.

So the good news is that Tom & Gerry's situation can be avoided. The key to finding the right solution is getting the right advice. And that's where we come in! If protecting the future of your business is a concern to you, please give us a call and we can walk you through your options.

Are You Leaving Over Half of the Returns on the Table?

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"We have met the enemy, and he is us", is a quote attributed to Pogo, a comic strip character created by American cartoonist Walter Kelly. Pogo may well have been referring to investors, whom it would seem are their own worst enemies when it comes to making investment decisions.

According to a study carried out by DALBAR, a leading financial services research firm, the average stock market investor over the twenty years to end 2011 earned a return of 3.5% p.a. versus the average fund return of 7.8% p.a. Less than 50%! Are you leaving more than half the stock markets' return on the table?

People make poor investment decisions because they are human. We all come with mental software that tends to encourage us to buy after

results have been good and to sell after results have been poor. Exactly the opposite of what we are told to do, i.e. buy low and sell high.

So why does this happen? To explain, I'll introduce two investment terms - time-weighted returns & money-weighted returns for funds.

- **The time-weighted return** which is the return typically reported, is simply the return for the fund over time.
- **The money-weighted return** on the other hand calculates the return on each of the Euros invested. These two calculations can yield very different results for the same fund.

So let's look at an example to explain the difference between the two.

Say, a fund starts with €100 and goes up 20% in year 1. It's now worth €120. The next year however, let's assume it loses 10% (-€12). So the €100 invested at the beginning is worth €108 after two years and the time-weighted return is 3.9% p.a.

Now let's say we start again with the same €100 and the same first year results of a 20% return. Investors see this very good result, and because they assume the good returns will continue (remember we're human!), they pour an additional €200 into the fund. So now they have €320 at the end of year 1 — the original €120 plus the additional €200 invested. The fund then goes down 10% in year 2, now causing €32 of losses.

The fund will still have the same time-weighted return, 3.9% as this is calculated on the fund's performance over two years (an increase of 20% in year 1, a drop of 10% in year 2).

But now the fund will be worth only €288, which means that in total, investors put in €300 — the original €100 plus €200 after year one — and lost €12.

So the fund has positive time-weighted returns but negative money-weighted returns. Investors' tendencies for buying high and selling low means that investors earn, on average, a money-weighted return that is less than 50% of the market's return (as per above). The results of our decisions with respect to timing are simply appalling.

The DALBAR study also identified something even more startling. An investor committing money on a regular basis to the stock market fared even worse than the lump sum investor, with a return of just 3.2%. So what are we to make of this?

Patterns of stock market returns are important to the regular investor. Investment strategy cannot be simply ignored if an investor is committing money on a regular basis. You can't just throw money blindly at the market.

To investors that commit lump sums to the stock market, you're pre-disposed to undermining your return through your own actions. Emotions, like hair growth or your heartbeat can't be controlled. You need to take the emotion out of the investment decision making. To do this, at a very minimum, have a proper plan when investing and seek external validation of your plan. Or better still, employ an expert who won't get caught up in the emotion of the investment decisions to invest the money on your behalf.

Where do you find and get access to such an expert? Well this is where we come in. It's our job to show you the range of investment options available to you, to talk you through the different funds and fund managers available and to help you find the one that best suits your needs. We're on your side and again, will be able to leave the emotion out of the decision making!

If you have any comments or queries in relation to this article, we look forward to hearing from you!

Around the Web

How Safe Is Your State Pension? Five Ways The Benefit May Be Cut

The number of +65s in Ireland is projected to increase by nearly 300,000 in the coming decade. The pension time bomb is ticking

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How Pro Golf Explains the Stock Market Panic

Can professional golf help explain what is now happening with the stock market? I think that it can.

Warren Buffett's Investing Dos and Don'ts

Here is a review of “What Buffett wouldn't do” for Investing and Management

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Learning to Take Responsibility When Things Go Wrong

What good does it do to blame other people? The answer, of course, is nothing.

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9 Financial Mistakes Retirees Can’t Afford to Make

Avoid these 9 mistakes so that you can live more comfortably in your retirement.

Quiz: How much should you be panicking about your finances?

A light-hearted quiz about the potential for financial misery that perpetually threatens to devour us all

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