Manage your Investments as you do your Business

Managing risk is the key to financial security

KEY POINTS

• Concentration is the greatest way to build financial security—and destroy it

• Asset preservation requires management of concentration, tax, market, and longevity risk

• Each stage of your business brings distinct financial risks
Does it feel like yesterday that you launched your business? Like many entrepreneurs, you probably started with little more than energy, confidence, and a good idea.

Life has changed a lot since then. Your financial picture is considerably brighter and you may be thinking about stepping away from your business, or perhaps you already have. In either case, you need to examine your financial life—and your investments, in particular—from a new perspective, to ensure the next stage is as rewarding as the last.

Depending on where you are on your journey, you might be focusing on building your business capital, managing your personal capital, or transferring the business and personal capital you have built.

Here are some tips to help prepare you for the financial risks you may face at each stage of your business’ life:

**Rapid growth phase**

Lay the foundation for a financially secure future.

Consider establishing a 401(k), an IRA, and a taxable account for stocks and bonds. These vehicles are important tools for combatting concentration risk, or the danger that your fortunes are too tightly tied to a single investment, in this case the equity in your business.

**Maturity phase**

If your business has reached a more stable phase, it is time to focus on both concentration and tax risk.

Diversify away from your company and industry.

To manage growing concentration risk, you will want to consider taking even more cash out of your business. If you own a significant amount of commercial real estate as part of your operations, you can also use your personal portfolio to reduce the risks associated with the cyclical commercial real estate market.

Have an asset allocation strategy that seeks to maximize after-tax returns.

For example, you want to be sure tax-advantaged investments, such as municipal bonds, are in your taxable accounts.

If you don’t already have a trusted investment advisor, now is an ideal time to identify and build a relationship with one, possibly as part of your estate planning. This will give you time to confirm that you have found the right person to help you when you transition away from your business—and cannot afford a misstep.

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Late stage
Are you currently deciding whether to maintain or transfer ownership of your business? Don’t count on a single liquidity event, such as an outright sale, for funding your later years. What if your business or sector faces a rough patch just as you’re planning to move on?

Focus on transitioning your business in a tax-efficient way
This will likely include sophisticated transfer and investment planning, with the goal of ensuring sufficient cash flow for your transition plan and desired lifestyle.

Life after your business
Those who have already left their businesses need to carefully manage two competing and very real risks: market risk and longevity risk.

Develop an Investment Policy Statement that balances your need for safety and returns
A clear asset allocation plan can help you mitigate market risk and avoid emotional decision-making—and the significant losses that frequently accompany it—when markets become volatile.

Plan for a longer retirement than you think
While you want a sizable slice devoted to stable investments, safety is a double-edged sword. Currently, the 10-year Treasury bond has a real return of essentially zero, and your retirement could last much longer than the 30 years for which many people plan. As a result, you will need to look at a range of investments, some growth-oriented, such as dividend paying stocks, diversified bonds, and even liquid alternatives to meet your needs over a longer time horizon.

Of course, knowing you need a plan to match your stage of life and creating one are two very different things. Why do so many successful business owners put off personal planning? Many enjoy being in control or haven’t identified an obvious successor for their business. Others can’t imagine what they might do after retirement. Despite such valid concerns, it is unlikely you will lead your business for your entire life so it is crucial to lay the groundwork for the life you want after you give up its reigns.