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The Wilson Group at Morgan Stanley
Eric S. Wilson, CIMC®, Family Wealth Director

"How can I assure my portfolio is performing as it should be, based on the risk I'm taking?"

By Eric S. Wilson

(Re-visiting a previous essay.) In light of the U.S. equity market's robust performance in 2013, many clients are looking at the percentage gains and dollars generated in their portfolios as good things. . . which they are. As a famous investor once said, no one ever went broke taking a profit. However, many times, positive equity returns mask the inequality between risk and reward. Perhaps now is a good time to try to understand the risk taken to generate the rewards of a higher portfolio balance and decide if the two are acceptable to you.

First, you need to know what benchmark your portfolio is currently measured against and if that benchmark is an appropriate comparison to the composition of your portfolio. Many investors set their performance expectations to that of the S&P 500 index. With this view in mind, how would you account for bonds or gold or small/mid-cap stocks, or international stocks, or emerging market stocks, etc., in setting your own performance expectations for your portfolio?

And how would you deal with cash in the portfolio? What about illiquid investments, like hedge funds and private equity? And to simply say "bonds," rather than Treasury bonds, municipal bonds or corporate bonds, for example, is also getting further away from the answer you seek.

Consider this: What if your advisor was using the S&P 500 price return and the three-month Treasury bill return as your portfolio's benchmark? "What's wrong with that?" you'd ask. Well, first, your portfolio's performance calculation had the benefit of the dividends paid from your stocks, but because your advisor was using the price return, not the total return for the S&P 500, your benchmark did not. Second, because most investors have a diversified portfolio of bonds, it is arguable that the three-month T-bill return would not be the appropriate benchmark. The result: Your benchmark would give you a false sense of reality by overstating your own portfolio's returns to that of the actual benchmark.

Another gauge of performance measurement is to take a more granular view and compare each of your investments' (ETFs, mutual funds, and/or private account) performances with those of their index and peer groups. (The peer group comparison is important because you need to know whether you're investing in/with the dud or the dynamo.)

The final part of the question references the risk you are taking. When my clients use the term "risk," they're usually referring to volatility relative to the S&P 500. Again, we have to go back to the composition of the portfolio and ask a series of questions. For example, if the S&P 500 were to drop 10 percent over a period of time, how much of that loss would be acceptable for the portion of your portfolio exposed to the S&P 500? If you're using the S&P 500 as a risk benchmark and you have a substantial allocation to small cap or emerging market stocks, be prepared for potentially more downside capture than you're currently expecting.

Peter Drucker is credited with saying that, "Long range planning does not deal with future decisions, but with the future of present decisions." Similarly, you can make better present decisions by taking the time to understand the composition of your portfolio, develop a custom benchmark to help measure it against and monitor your performance relative to that custom benchmark.

Eric S. Wilson is a Wealth Advisor with the Wealth Management division of Morgan Stanley in Macon, GA. The views expressed herein are those of the author and may not necessarily reflect the views of Morgan Stanley Smith Barney LLC, member, SIPC (www.sipc.org). Morgan Stanley Financial Advisors engaged Worth *to feature this profile. Eric Wilson may only transact business in states where he is registered or excluded or exempted from registration, www.morganstanleyfa.com/ericwilson. Transacting business, follow-up and individualized responses involving either effecting or attempting to effect transactions in securities, or the rendering of personalized investment advice for compensation, will not be made to persons in states where Eric Wilson is not registered or excluded or exempt from registration. The strategies and/or investments referenced may not be suitable for all investors.*

S&P 500 Index is an unmanaged, market value-weighted index of 500 stocks generally representative of the broad stock market. An investment cannot be made directly in a market index.

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—Eric S. Wilson

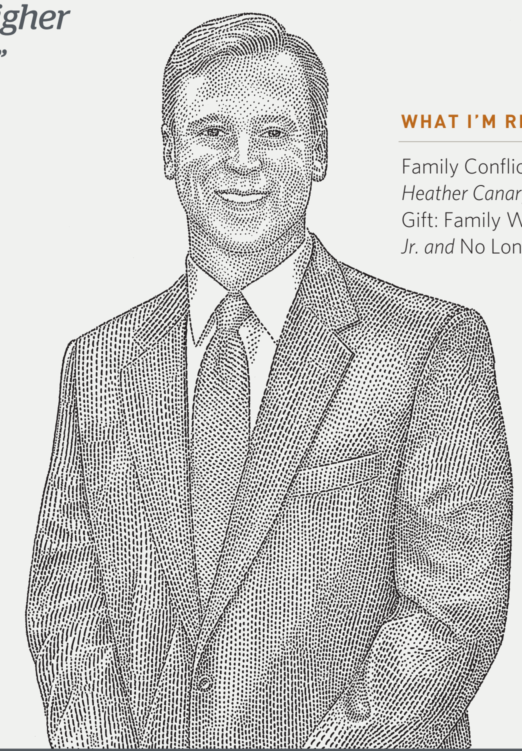

ILLUSTRATION BY KEVIN SPROULS

How to reach Eric S. Wilson

Families may reach me with questions or with interest at 877.442.5445 *or* eric.s.wilson@morganstanley.com.

WHAT I'M READING NOW…

Family Conflict: Managing the Unexpected, *by Heather Canary and Daniel Canary;* The Cycle of the Gift: Family Wealth and Wisdom, *by James E. Hughes Jr. and* No Longer Awkward, *by Amy Florian*

WHAT MAKES A GOOD CLIENT…

A first or second generation family of wealth that desires to improve the odds of the successful transition of their wealth to subsequent generations

MY HOBBIES ARE…

Being a husband and a father, playing tennis, upland hunting and reading

About Eric S. Wilson

Eric S. Wilson is a wealth advisor and senior vice president at Morgan Stanley, and for the past 19 years he has served the varied needs of families whose wealth has the potential to change the essential nature of their descendants' lives. Mr. Wilson began his career at Merrill Lynch in 1994, where he served until joining Morgan Stanley in 2010. For his work with affluent and high net worth families throughout the southeastern United States, he has been specially designated at Morgan Stanley as a family wealth director. Achieving this prestigious designation meant adhering to stringent quantitative and qualitative requirements set forth by Morgan Stanley and now provides him with specialized and dedicated resources from around the firm, which benefits his clients by providing them with many of the same services offered by family offices. Mr. Wilson is a Certified Investment Management Consultant℠ (CIMC®) and an Accredited Investment Fiduciary Analyst (AIFA®). He proudly serves on the advisory boards of the Community Foundation of Central Georgia and Children's Hospital of Central Georgia and is a member of the Macon Estate Planning Council. He and his wife, Cindy, are proud parents of four sons, ages 12, 12, 12 and 5.

Assets Under Management
$1.8 trillion (Morgan Stanley Wealth Management, as of 3/31/13)

Minimum Fee for Initial Meeting
None required

Minimum Net Worth Requirement
$5 million (planning services); $2 million in investable assets (investment services)

Largest Client Net Worth
$25 million+ (as of 12/31/12)

Financial Services Experience
19 years

Compensation Method
Asset-based fees and commissions (investment and insurance products)

Primary Custodian for Investor Assets
Morgan Stanley Smith Barney LLC

Professional Services Provided
Planning, investment advisory and money management services, advanced wealth transfer planning and liability management

Association Memberships
IMCA, Fiduciary 360 (www.fi360.com)

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