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ASK THE **ADVISERS**

The views and opinions expressed in “Ask the Advisers” are solely those of Keith Singer.

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Defined Outcome ETF’s

For investors in or near retirement, one of the most important characteristics of a portfolio is reliability. A high expected return is wonderful, but any portfolio with a wide range of potential outcomes makes planning for the future much more difficult.

There have been decades where the S&P averaged over 14% per year and there also have been decades where the stock market lost a lot of money. Most of our clients do not ask us to give them a portfolio that makes them the most money possible. They ask us to create a plan to ensure they can potentially maintain their lifestyle without worrying if they will run out of money, even if they live a long time and the stock market has a bad decade.

In order to achieve their objectives, they need more predictable investments than the typical 60/40 portfolios. One of the tools we use to reduce the variance of our client portfolios is Defined Outcome ETFs. These funds track a major index like the S&P 500 however the fund uses derivatives to create downside protection.

In exchange for that protection there is a limit on the upside. For instance, if you want 15% downside protection, there may be an upside limit of approximately 18%. In a year that the index is down 16%, investors would only lose one percent. A $100,000 investment would be worth $99,000 before fees after a year. Conversely if the index ended the year up 20% the ETF would only appreciate by the cap of 18%. If you are comfortable with a 10% downside buffer, your cap could be higher, perhaps 23%.

Typically, when you take less you risk you get less potential reward but since the year 2000 an ETF with a 15% buffer and 18% cap would have not only had much less risk than the S&P 500 index, it would have returned more than the index as well since the big down years would have been eliminated or substantially mitigated.

To receive the weekly email version of Mr. Singer’s column, email the word Column to Caitlin@Singerwealth.com.

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