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Ellwood Viewpoint

Goals-Based Investing: Unlocking Value for Investors and Advisors

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In recent years, goals-based investing has emerged as an attractive alternative to traditional investing. Indeed, many wealth advisors and financial advisors have found that employing this approach can help recruit and retain clients, add value to a practice, and build a more sustainable and scalable business.

That's not to say that traditional financial planning has lost its relevance. Rather, goals-based investing presents a different approach to investing that may help advisors tap into a new market of young investors. Here, we explain what goals-based investing is, who it's for and how it can benefit both investors and advisors.

Defining goals-based investing

Goals-based investing is focused on achieving specific, short-term goals as defined by individual investors. As such, asset allocation is based on meeting these goals, rather than on generating long-term returns or beating the market. Greater emphasis is placed on specific investments to provide an expected outcome in the near-term. In goals-based investing, the goals set by the investor typically fall into the category of "wants" versus "needs." Ideally, these goals are attainable in five years or less. For example, an investor might set the goal of taking a European vacation in two years or buying a new car in four years.

With a new generation of investors entering the marketplace, advisors should begin the process of rethinking their approach to investing and managing client relationships.

By contrast, longer-term goals, such as saving for retirement, are better met via traditional approaches to investing.

When a client sets a short-term goal, an advisor should try to provide some oversight, guiding the client towards goals that make good financial sense or course-correcting as needed. For example, if an investor wants to buy a luxury car but hasn't saved much for retirement, an advisor might encourage them to select a more modestly priced car and educate them on the value of saving for retirement early and often.

Target clientele

In theory, advisors can use goals-based investing with any type of investor. However, this approach is usually most appealing and applicable to a younger segment of investors—specifically clients in their 20s or 30s.

That's mainly due to a difference in mindset. Younger investors tend to be more interested in financially preparing for smaller, short-term purchases versus larger, long-term purchases. This is especially true for younger Millennials who are getting married later, forgoing home ownership and choosing not to have children. Broadly speaking, the spending habits of these young professionals divert from that of their parents; they'd rather, for instance, save for a high-priced vacation than save for a down payment on a home.

Therefore, goals-based investing can serve as a valuable tool for advisors that want to convert young professionals into clients while their liquid assets are relatively small (e.g., $50,000–$150,000).

Advantages for investors and advisors

Goals-based investing can serve the interests of both investors and advisors. Among its many benefits, this approach can change investors' behavior in positive ways improve an advisor's service offering, and create a more valuable, long-lasting relationship between an investor and advisor. Additional benefits include the following:

- Creates a sense of accomplishment for investors. With goals-based investing, investors can experience the satisfaction that comes with achieving savings goals—and experience it earlier in life than retirement age. This, in turn, can motivate an investor to work toward other financial goals and establish lifelong saving habits.

- Enables the advisor to customize service offerings. With traditional financial planning, clients often receive investment advice based on quantitative information or long-term goals. By contrast, with goals-based investing, clients receive advice that's tailored to their specific needs and goals. Advisors work to understand their clients on an individual level and then design a game plan, which leads to a more valuable service offering.

- Increases frequency of interactions. Goals-based investing creates more opportunities for advisors and investors to communicate and interact. Advisors have a good reason to reach out to their clients on a more frequent basis to review savings goals, check on their progress or talk through decisions.

- Strengthens the advisor-investor relationship. These benefits add up to one important outcome: They strengthen the relationship between an advisor and investor. This primarily stems from a behavioral change. When an investor is able to recognize the value provided by their advisor, they are more likely to stick with them and commit to an asset allocation despite fluctuations in the market.

With a new generation of investors entering the marketplace, advisors should begin the process of rethinking their approach to investing and managing client relationships. The burning question is this: What's the best way to take advantage of the growth opportunities that young investors present? Goals-based investing may just be the answer. E

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