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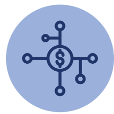
# Implementing Lessons Learned From 2022

As we complete the first quarter of 2023, it's a great time to reflect on the market turbulence of last year, and not just what we learned from it, but how we can incorporate those lessons into planning for the future.

Below are a few key takeaways from last year, and some insights into what they could mean for individuals and families this year.



## LESSON #1: CELEBRATE DIVERSITY…OF ASSET CLASSES

How did your portfolio perform in 2022? The typical 60/40 portfolio was down 15-20% last year. While there was no escaping the downturn with publicly traded stocks and bonds, a more diversified portfolio may have produced better results. In fact, many alternative investments showed positive returns for the year. Access to desirable alternative investments, including institutional real estate, venture capital, private equity and private debt funds can help investors to diversify and balance "swings" in the market.

**TRY THIS** Meet with your wealth advisor and have them review their investment selection, providing examples of how they can help you diversify your portfolio. Don't have an advisor? It may be the right time to find or change advisors. Bordeaux's guide to interviewing wealth advisors is a great resource for asking the right questions for the best fit.

## LESSON #1 COROLLARY: GET UN-CONCENTRATED

If your wealth is heavily concentrated in a single stock, take immediate action to diversify. With last year's market volatility, many investors saw their wealth reduced substantially because it was tied to an individual stock that declined sharply. Remember: A good company does not necessarily equal a good stock. Even if you love your job (and we hope you do!), that is not a guarantee of the company's stock performance. If you have significant equity compensation, review your situation carefully with a qualified wealth advisor.

## LESSON #2: SAVING / BUDGETING IS VITAL – HAVE AN EMERGENCY FUND

According to Crunchbase news, more than 140,000 jobs were slashed from public and private tech companies last year as they were forced to confront a slowing economy and rising inflation. And they report that layoffs are continuing into 2023. For individuals suddenly unemployed, an emergency fund offers financial protection from this type of worst-case scenario. The standard advice is for families is to have 3 to 6 months' worth of expenses set

## LESSON #2 COROLLARY: GO WITH THE (CASH) FLOW

As a follow up to lesson #1 above, we want to underscore the importance of planning for cash flow. Ensuring that you have sufficient funds to meet expenses means you won't end up in a "forced seller" position, where

*continued* ⇨

## LESSON #2 *continued*

aside to provide the time needed to find another job without the stress of missing payments, or falling behind financially. For high-net-worth individuals, the "runway" might be even longer, for example 2-3 years.

Experts operating in the private equity space suggest that technology companies increase their runway to 24 months minimum, mostly by slashing expenses. We suggest taking a similar approach, but with the additional flexibility of raising cash balances and diversifying out of concentrated risk assets. In the interim, many short-term cash equivalents with low risk are paying 4-5% income and will benefit from further interest rate hikes.

## LESSON #2 COROLLARY *continued*

you have to sell assets at a market low. Make sure you have investments in place that can be easily liquidated should something happen. If a significant portion of your wealth is tied up in illiquid investments, you may need to make adjustments to your portfolio. In essence, you want easy access to liquidity that can sustain you for 1-2 years.

**TRY THIS**

Build an emergency fund appropriate to your level of wealth and expenses. Small, regular contributions can help you save without significantly disrupting your current cash flow. For families with two income earners, consider increasing cash balances to 1.5x your baseline amount (6 months of expenses as a baseline is common). Families with income largely tied to one earner should consider increasing cash balances more – maybe 2-2.5x the baseline, depending on occupation and industry.

## LESSON #3: TAKE ADVANTAGE OF A (TEMPORARILY) LOWER TAX BRACKET

A down market can present a good opportunity for a Roth conversion (convert your traditional IRA to a Roth IRA). While you will have to pay taxes on the converted IRA, you'll be doing it when the assets are at a lower value. Then, when you're ready to use your Roth funds, you'll be able to access them tax-free. Additionally, you may be able to minimize your capital gains from a lower tax bracket.

**TRY THIS**

Take inventory of your projected income this year, including items such as compensation, dividends, interest, and Required Minimum Distributions. Some wealth management firms, such as Bordeaux Wealth Advisors, will maintain up-to-date income tax projections for clients. With a more specific tax bracket in mind, you can calculate a maximum amount for Roth IRA conversions, capital gains taxes to realize, and other income realization techniques. While in lower income years, there is a likely greater benefit to realizing ordinary income tax items as opposed to long-term capital gains, as the vast majority of long-term capital gains are taxed at 15%.

## LESSON #3 COROLLARY: TAXES, TAXES, TAXES!

Remember that taxes are still the greatest source of leakage to your wealth. Always be aware of tax implications and ensure your advisor is qualified and has the credentials to consult on taxes.

Maintaining projections of your own, or having an advisor maintain them for you, can help you to make ongoing technical improvements to your after-tax situation, and having a tangible context to operate in is always preferred to guesswork or using your gut to understand when making Roth conversions or other opportunistic planning might be advantageous. We recommend individuals develop that planning and revisit it at least quarterly.