FLASH REPORT

WHEELER
Wealth Management

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How the Wealthy Navigate Stormy Weather

The past few years reminded all of us that financial markets not only don't always go up—a lesson we all likely know—but also that they can go down in surprising ways. We don't know the next curveball the markets will throw our way or when it will happen. But history suggests that at some point we'll once again be surprised by an unexpected path taken by the economy and various asset classes.

With that in mind, reacquaint yourself with some of the key action steps commonly used by very wealthy investors during trying times. By knowing what the affluent do in their efforts to safeguard and even grow their wealth during downturns, you can take a page from their playbook the next time things look bleak.

Eight Action Steps

Some of the moves—both large and small—that we see the wealthy making during downturns include the following.

Important: Not all of these strategies may be appropriate for you. The right decisions for you will, as always, depend on a broad range of factors.

1. Know the facts. Strange times can easily cause nervousness that leads to emotional financial decisions—which usually don't end well. You want to avoid panicking and instead find ways to stay the course (assuming that you have a plan in place and that plan still makes sense based on your objectives).

Look to shore up the rational part of your brain. Facts can be your best allies here. When you see evidence showing, for example, that bear markets are relatively rare events or that markets often stage recoveries from downturns at a rapid pace, it can help bring the thinking brain "back online." Ask professionals you work with for data that can help you see the bigger picture and historical trends.

2. Manage emotions. That said, facts aren't always powerful enough to stave off the fear that "this time it's different." One strategy recommended by behavioral experts is to assess whether you're engaging in so-called catastrophic thinking. It works a bit like this: Admit what you're thinking—yes, the entire financial system could potentially crumble because of recent event X. But ask yourself: Is that the most likely outcome? In fact, is that even 10% or 20% likely to happen? What scenario is much more likely to occur? This type of reality check can help shut down the leap in logic that the worst is bound to happen. That, in turn, can help prevent costly shortsighted moves.

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USING DOWNTURNS TO YOUR ADVANTAGE

3. Use gifting to shore up the future.
Gifting assets to one or more irrevocable trusts is a common strategy in estate planning, wealth protection planning and the like. A big downturn can enable you to gift higher amounts of money at a lower tax rate—and potentially enable more tax-deferred growth of the assets you gift. Ultimately, gifts of stocks at depressed prices can potentially help secure a better financial future for the person or people you want to benefit from your trust.

4. Alter foundational strategies. If you want to make significant, wholesale changes in your plan—shifting to an entirely different investment style or approach, for example—a market downturn can be an advantageous time to do it. The reason, of course, is that you may be in a position to clear out large swaths of your existing portfolio in a tax-efficient manner that ends up costing you less in capital gains taxes than you might have otherwise paid.

5. Identify assets that may be undervalued.
Rough economic times can present bargains in numerous financial categories, of course—but the affluent know to look beyond equities when it comes to “buying low, selling high.” Entrepreneurs might find other businesses to acquire. Collectors of art and artifacts may buy strategically. Real estate investors often expand their search criteria.

6. Convert an IRA. It’s become increasingly common for high-net-worth individuals to convert their traditional IRAs to Roth IRAs (which feature, among other benefits, tax-free withdrawals in retirement and continued tax-free growth). Converting when the market is down means paying a lower tax rate in comparison with the eventual growth of the account—although it can mean a large tax bill when the conversion occurs.

7. Take advantage of shifting trends.
Big economic and market surprises often are accompanied by changes in investment leaders and laggards. That’s why some affluent investors will look to position themselves in what they see as tactical, emerging opportunities arising from the changing dynamics of world economies and other factors.

8. Revisit financial goals and values.
The affluent tend to recognize that a period of turbulence is not the time to hide their head in the sand. Instead, they generally make a habit of being self-reflective—examining their existing financial goals and values for themselves and their loved ones, and assessing whether they need to revise them in any way. For example, some families’ philanthropic focus shifted toward health care-related charities due to the pandemic. Big or surprising changes often bring about shifts in our interests and deeper beliefs. For wealth to support our key goals, it needs to be aligned around what we care about most.

Ultimately, many of the “secrets” to how the affluent approach market downturns aren’t big mysteries. The affluent look to be prepared to weather storms, stay calm in the face of stress, be opportunistic if it makes sense and evaluate whether they need to make any significant changes. These are steps all of us can take in advance of and during periods of uncertainty. And of course, we can take steps to get the type of professional guidance that can potentially empower us to stay on track.