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WHITE PAPER

Five Ways to Provide More Value for Your Clients

Access to the Internet has become nearly ubiquitous in the United States, and Internet-based data analytics are increasingly being used by investors to support their financial decisions and to complete investment transactions. Technological advances have enabled the rise of the "robo-advisor," emerging software tools that offer many do-it-yourself options for investors. Meanwhile, globalization is increasing the correlation of many markets and asset classes, making effective portfolio diversification more challenging.

In today's environment of rapid change, savvy financial advisors must ensure that they remain relevant in the financial lives of investors. To do this, advisors must sharpen their focus on providing value for their clients that can't be readily obtained through other sources, such as automated tools. In this way, advisors can position themselves not only to survive, but also to thrive. The following suggests five ways advisors like you can enhance client perceptions of the value they deliver. Those who succeed will move closer toward becoming an indispensable resource for their clients.

1. Construct well-diversified portfolios that reduce volatility and promote more rational investor behaviors.

One of the most common errors in allocating capital is insufficient portfolio diversification. You can enhance your value to clients by helping them avoid this common error. You can provide the expert advice necessary to promote a more thorough understanding and application of portfolio diversification. Encouraging your clients to capture all the relative risks in the global financial system positions them to own the available hedges. By capturing and managing risk, you unlock the potential rewards clients can receive, befitting their investment time horizons, risk tolerance and need for liquidity.

Help your clients counterbalance the potentially destructive effects of fear and greed by constructing portfolios that manage volatility more effectively.

Help your clients counterbalance the potentially destructive effects of fear and greed by constructing portfolios that manage volatility more effectively. This can be accomplished by taking full advantage of a marketplace that is now providing individual investors with a wider range of opportunities to invest in both public and private debt and equity.

Where appropriate, also consider adding allocations to directional strategies like long/short, arbitrage and spread investing concepts, and the balanced use of leverage in certain instances. Clients should also think two-dimensionally in the investing process, recognizing that it is not just what they own, but also what they denominate in that ownership, that could provide a significant difference in performance. Increased diversification can help to stabilize client portfolios and reduce the volatility that often prompts fear-based selling during a downturn. Your goal should be to manage volatility without sacrificing real rates of return.

Beyond these tactics, continue to monitor the plans your clients have in place and provide the perspective and context required to adjust them as needed. Setting risk-and-return benchmarks consistent with client goals, and rejecting the premise that beating the S&P 500 is the only standard of performance when it comes to those goals, can set you apart from commoditized advice tools. By helping clients fine-tune their plans to meet individual needs and changing circumstances, you provide value that goes beyond what can be accessed through standardized tools and market-based index comparisons alone. Robo-advisors simply are not capable of providing this kind of personalized service in scale. Only financial experts can provide the sophisticated counsel that can help their clients consider all of the pertinent investment options available to them while making adjustments that accommodate personal circumstances as they evolve over time.

Provide customized counsel and sophisticated expertise that automated advisors can't match.

2. Help clients change self-defeating investment behaviors by communicating clear, consistent messages and repeating them frequently.

Most investors will usually do the wrong thing at the wrong time, especially when stressed and acting on instinct alone. The unfortunate reality is that investors frequently flood money into the top-performing asset classes without considering that investing after these asset classes have become top performers is equivalent to investing too late. Investors also frequently sell assets during a downturn, which only serves to lock in the resulting loss before the markets have sufficient time to recover.

You can increase your value to clients by helping them avoid these self-defeating, but all too common behaviors. Get started by studying the circumstances that usually provoke investors to make decisions based on the powerful emotions of fear or greed, rather than rational analysis. Then seek to change established patterns of investor behavior by modifying the rituals and repetitive narratives that established them in the first place.

Harness the power of messaging that is clear, consistent and repeated frequently. Take advantage of the myriad communication options now available. Remind clients, as frequently as on a weekly basis, about the fundamental principles of investing. Anticipate the fluid nature of your clients' tolerance for risk and provide additional support that encourages them to "stay the course" during downturns. Do not assume that clients "get it," and do not assume that they cannot be easily distracted by market movements. Frequent reinforcement is especially important for retired clients, and those approaching retirement, because they have less time and opportunity to recover from the effects of impulsive investment choices and any resulting losses.

Most importantly, in spite of attempts to educate, motivate and communicate, the evidence is abundantly clear that these efforts are not always effective. Evidence suggests that, while the greed impulse is powerful, it is the fear impulse that is ultimately destructive. Smart portfolio construction that focuses on reducing volatility and increasing diversification through low or noncorrelated assets can make a meaningful difference in overall portfolio value. Simply stated, 30% drawdowns in

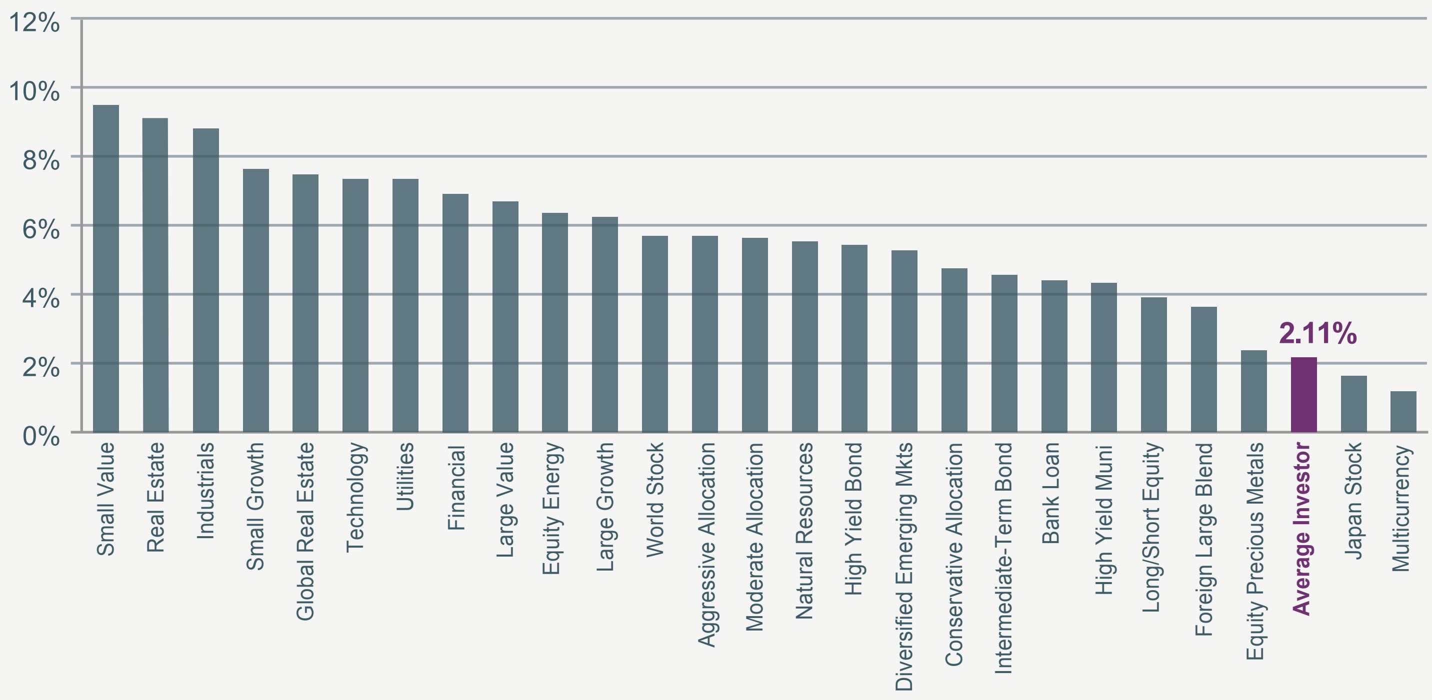
2008 led to massive outflows, redemptions, and locked-in losses.

You can build portfolios that still meet the real return requirements while working to reduce drawdowns. The inclusion of alternative investments, like structured credit, precious metals, long/short, infrastructure and other asset classes, can enhance investor portfolios in difficult times.

Education and communication are important. Portfolio construction is vital. There is a direct relationship between successful advisors and their portfolio construction techniques; the most successful advisors construct portfolios that reduce drawdowns without sacrificing real rates of return.

Are self-defeating behaviors causing poor investor performance?

20 Years Annualized (12/31/1996–12/31/2016): Morningstar category averages vs. the average investor.



Past performance is not indicative of future results.

Returns are Morningstar Category averages for open-end mutual funds. Morningstar classifies open-end mutual funds into categories based on their actual holdings, and a Morningstar Category average returns include all funds classified by Morningstar in a particular category. Return data for all Morningstar categories is available upon request.

Source: Morningstar Direct/*DALBAR 2016 Quantitative Analysis of Investor Behavior.* 'Average investor' is represented by Dalbar's average asset allocation investor return for the twenty year period ending 12/31/2015, which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior.

3. Serve as a resource for credible and reliable information about the topics your clients care about most.

Develop unsurpassed expertise in managing risk in ways that are consistent with what you know about human nature. Proactively communicate to share your expertise in multiple ways. Make it clear that you are more focused on building a relationship with your clients than on selling a product. Be approachable, trustworthy, intelligent and well-informed, and promote these impressions consistently with current and potential clients. If you do these things effectively, you will be more likely to land and retain any account.

Realize that each client is unique, and no single communication medium has the capacity to resonate powerfully with all clients. Some will be more responsive to a specific form of communication than others. To have maximum impact with as many clients as possible, vary your methods of communicating with them. Better yet, eliminate the guesswork by allowing each client to choose the ways they prefer to hear from you.

Most investors still prefer to have expert advice when investing, and that propensity is higher with investors that have investible assets of $100,000 or more, according to a WellsFargo/Gallup survey.[1] Some trail-blazing broker-dealers are positioning their organizations to provide their clients with the best of both worlds: a combination of convenient automated tools and access to people with the expertise to accurately interpret data and the flexibility necessary to develop customized solutions.

We must use caution when attempting to commoditize advice or construct portfolios based on static, returns-based models. Given the tenets of behavioral finance, this type of advice has limited value for clients when the market collapses. Focus on assisting individual clients with financial planning for special circumstances and requirements, because this is a service that standardized software cannot deliver. In addition, discuss with your clients of all ages how to generate and manage income for retirement through risk management and portfolio construction.

Be consistently approachable, trustworthy and well-informed.

[1]Younger investors often are more skeptical about accepting advice, and you may need to work harder to demonstrate your credibility and reliability to them. Younger investors also tend to be more comfortable with using online financial advice tools. Approximately 66% of non-retirees have at least some level of comfort with using online financial advice tools, compared with 35% of retirees, and men generally have a higher comfort level than women.

SOURCE: WellsFargo/Gallup *Investor and Retirement Optimism Index Survey,* June 27 – July 9, 2014.

Although generating retirement income is a traditional goal for advisors, today's low-yield environment demands more creative solutions for income-oriented investors than any other time in recent decades. The large cohort of Baby Boomers is creating increased demand for retirement income solutions that have the potential to provide higher risk-adjusted returns than those currently delivered by traditional stocks and bonds. If you are willing to recommend allocations to alternative asset classes, you can better position yourself for competitive advantage. By providing your clients with access to alternative income solutions, you can help suitable investors participate in investment strategies, often pursued by institutions, which have not been readily available to individual investors. These same institutions (many of which are charged with providing monthly checks to pensioners) provide us with real-world and real-time examples of progressive portfolio construction that focuses on real returns and drawdown reduction.

4. Remember that communication is still done best by humans.

In spite of all the automated tools at our disposal, people still do the best job of communicating with other people. Technologies are powerful resources that serve some communication roles well, but they can't entirely replace personal interactions. Nothing can replace the dynamics involved when two people meet or speak directly. Additional meaning can be conveyed or overlaid when verbal cues and other unspoken signals help to make understanding more complete. No other form of communication is as effective in building relationships as personal interaction.

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How can you put these principles into practice? Pick up the phone occasionally and find other ways to be personable and approachable. Think creatively about how you can stay personally connected with your clients, and strive to demonstrate that you are an individual capable of making unique contributions to their financial success.

How can you differentiate yourself from others in your field to provide compelling value for your clients? Evaluate your talents and areas of greatest expertise, and then use these strengths to further differentiate your services for established clients. The same strengths can be used to attract new clients that represent an ideal fit with the unique combination of experience and expertise only you can offer.

It is vital that you work with clients in a forthright manner to promote both their intellectual understanding of sound investment principles and their emotional relationship to investing. But in the end, it will be the quality of the portfolios you build and the expectations you manage that define your twenty-first century client/advisor relationships.

5. Guide your actions with a self-directed moral compass that takes into account instinctive financial behaviors and the emotions that drive them.

As individuals and as a society, we all stand to benefit when profit-driven intermediaries temper their drive for profits with a professional code of ethics that makes appropriate disclosure and education an integral part of their interactions.

In a separate white paper, we will explore in depth why smart portfolio construction, rather than education alone, is more effective in counterbalancing the often irrational and self-defeating investment decisions prompted by fear or greed. However, appropriate disclosure and education about available investment options will always be integral components in the ethical business practices of financial advisors. Trust must be earned, and these activities are essential in developing the trust you want your clients to feel when receiving counsel from you.

Develop your own moral compass that tempers your drive for profits with a personal commitment to the professional ethics from which you will never waver. Focus on sound strategies for promoting a more rational approach to investing by managing risks and reducing portfolio volatility through enhanced diversification. A well-diversified portfolio can be expected to be less volatile and your clients should experience fewer disruptive events likely to trigger the fear or greed that often leads to irrational investment decisions.

As a component of your moral compass, include a commitment to providing an accurate assessment of the potential benefits and risks associated with any action you recommend to your clients. Openly address risks with your client and construct portfolios that hedge for known risks in proportional ways. In addition, provide value that can apply to many aspects of your clients' lives. Help them understand how economic systems and markets function, as well as sound investment principles based on these realities, such as diversification and proportionality. Encourage development of the skills necessary to evaluate the quality of the counsel they receive from you or from other sources.

Make a real difference for the real people you serve by communicating with them frequently and by counseling them as individuals. Provide more vigilant support during times of personal financial crisis or economic disruption. In addition, periodically re-evaluate and adjust investment strategies to account for the fact that the aging process gradually reduces your clients' tolerance for risk over time.

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Conclusion

By following these suggestions and similar approaches, you can maintain and enhance your relevance in the financial lives of your clients, and even expand your book of business. Strive to be among the best financial advisors; focus on developing creative and innovative ways to increase the perceived value of the services you provide for your clients. Despite the inevitable advances in technology and the rapid evolution of global markets, financial advisors who pursue these goals most effectively will be positioned to thrive during any market cycle for years to come.

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CAPITAL PARTNERS

14675 Dallas Parkway, Suite 600
Dallas, Texas 75254
866.655.3600
provasicapital.com

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