What the Smart Money Knows

Six investment practices
that lead to steadier results.

We take a different perspective.
Yours.

NEWPORT
PRIVATE WEALTH

ABOUT NEWPORT PRIVATE WEALTH

Newport Private Wealth is among Canada's largest independent wealth management firms for high-net-worth individuals.

The firm offers professional investment management and full-service wealth management delivered through a team of multi-disciplined investment professionals averaging 25 years of experience. Based in Toronto, Newport Private Wealth is privately owned and managed by its professionals who, to ensure alignment of interests, have their own money invested alongside clients.

Newport Private Wealth's investment approach is purpose built for individuals who want to earn steady income to fund their lifestyle now or in the future, grow their wealth ahead of inflation and protect their capital from significant or permanent loss.

To achieve these objectives, Newport Private Wealth offers its clients the best of both worlds: the preferred access of an institutional investor with the personal service of a boutique.

Using its size and capabilities, Newport Private Wealth sources hard-to-access private investments, such as real estate, infrastructure, etc. to complement traditional stock and bond asset classes, so client portfolios are less dependent on the ups and downs of the stock market. For specialized expertise in these asset classes, it retains independent money managers – many of whom are unavailable to individual investors.

At the same time, the firm's style of personalized service, low turnover and high levels of client satisfaction* evoke a boutique experience for the families it serves.

Newport Private Wealth's services are best suited to individuals with a minimum of $1 million to invest. Individuals with less than $1 million can access Newport Private Wealth's investment management capabilities through its division, Lonsdale Portfolios.

* 97% client satisfaction rating as measured in a 2013 third-party survey conducted by Advisor Impact.

YOU DON'T HAVE TO BE A BILLIONAIRE TO INVEST LIKE ONE.

Welcome to the world of ultra-high-net-worth investing, where large investors, such as family offices, elite money managers and pension funds, enjoy certain advantages over the investing public.

They also, by and large, enjoy higher investment returns, over the long term, at lower levels of risk – while the average investor struggles to earn portfolio returns that barely exceed the rate of inflation and generally underperforms most asset classes.[1]

How to explain the difference?

Certainly, a large asset base and network of relationships can open up access to unique investment opportunities and money managers not available to retail investors. But as this white paper makes clear, there are also defining beliefs and practices that the smart money employs to drive results.

It is not so much *what* elite investors do that is markedly different from ordinary investors – it's *how* they do it. They approach investing with an uncommon degree of rigour, discipline and passion. To use a sporting analogy, there are weekend golfers; there are the players on the PGA Tour; and then good players that don't get there. Each group may get around the course in the same way, but with vastly different outcomes and levels of consistency.

In this white paper, we examine the common investor experience compared to the beliefs and practices of ultra-high-net-worth and top institutional investors. We distill their methods into six key factors that contribute to better investment results and are instructive for individual investors.

1. http://www.forbes.com/sites/advisor/2014/04/24/why-the-average-investors-investment-return-is-so-low/

1

The best offense is good defense.

The smart money is relentless in measuring risk against return.

In our experience, the smart money has a different approach to investing altogether.

Generally, they believe that good performance is the byproduct of sound risk management. They do everything they can to quantify and manage risk. To be clear, this does not suggest they are putting money under the mattress or in T-bills and GICs: they know these strategies represent significant risk to the long-term protection of their wealth.

Rather, they believe that the straightest path to higher returns is through *steadier* returns – avoiding large or permanent losses and dramatic declines in value.

To understand this viewpoint, it is helpful to understand how volatility impacts wealth.

For example, we can show that an average annual return of 7% over many years will result in a different outcome depending on the volatility of the return. (Volatility being the degree of dispersion in returns from the average or expected return.) Let's compare the experience of two individuals who each start with a $2.0 million portfolio and withdraw $80,000 from it every year.

Each portfolio delivers an average annual return of 7% over 25 years. But the portfolio of Investor A, who is striving for the highest return possible, has a volatility measure of 20%[2], reflecting more dramatic ups and downs. Meanwhile, Investor B, who is seeking the steadiest return possible, has a much lower volatility measure of 5%.

At the end of 25 years, because of the volatility, Investor A has a 27% chance of running out of money, whereas Investor B has virtually no probability of outliving his capital. Even though they both earned an average of 7% over the time period.[3]

2. Approximately equal to the historical volatility of the S&P 500 in CDN dollar terms.

3. Results assume a normal return distribution and have been calculated based on 5,000 simulations. Results also assume 2% inflation.

Again, the smart money places greater value on steady performance, satisfied that this will lead to greater wealth long term. This is the opposite of what we see a lot of individual investors – and their advisors – doing. That is, they move in and out of investments all too frequently and usually at just the wrong time. Predictably, their portfolio returns suffer.

Over the past 20 years, the average investor's portfolio has underperformed every asset category except two (Asian fixed income and Japanese equities), even underperforming cash.[4]

In summary, the good news is that you don't have to have a nine-figure portfolio to generate steady returns. But you do have to have a good process that applies the practices outlined in this whitepaper.

4. http://www.rbadvisors.com/images/pdfs/toward_the_sounds_of_chaos.pdf

2 More heads are better than one.

The smart money assembles a diverse team to implement a process.

Just as it is common for retail investors to hire a professional advisor or money manager, large pension funds and family offices also employ advisors to oversee the management of their capital. But once again, there are some key differences as to how they do this.

A best practice is to establish an investment committee – a purpose-built team of professionals with one goal, to be a steward of the client's investment experience, acting in the client's best interests.

The investment committee defines and governs the overall objectives, including risk parameters, asset mix and the process for selecting and terminating managers, etc.

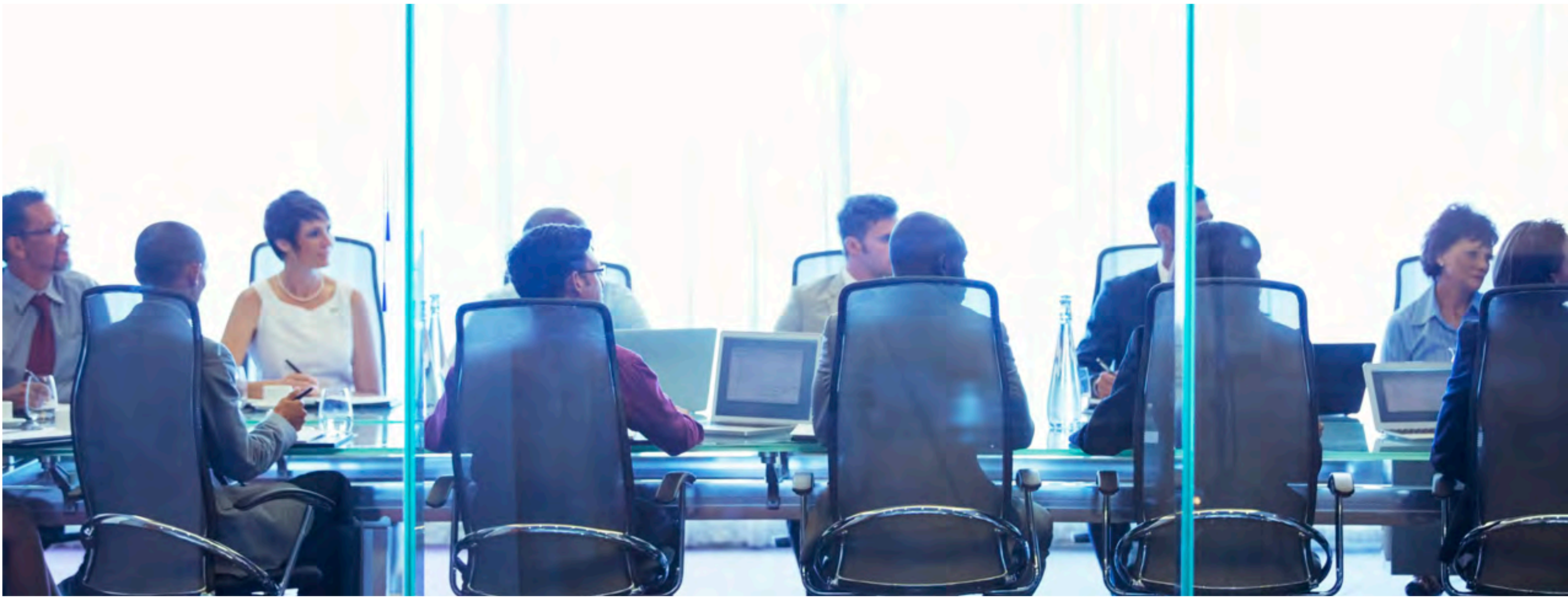
There are several advantages to this approach.

MORE HEADS ARE BETTER THAN ONE

Typically, investment committee members are highly-skilled professionals with different areas of expertise (i.e. investments, law, accounting, business). While one member's strength may be real estate investments, another's may be taxation or legal issues, resulting in a rich treasure trove of expertise and experience that can't be matched by a single individual advisor.

BETTER DECISION MAKING FROM DELIBERATION

By definition, an investment committee is a forum where ideas are presented, debated and, ultimately, voted on. In theory, only the best ideas survive the scrutinizing process. The most successful investment committees engage in a respectful, objective exchange of diverse viewpoints, while remaining united around the common cause of serving the client's interests.



THE INDIVIDUAL INVESTOR EXPERIENCE

Contrast this with the common experience of working with a single financial advisor and it is easy to understand why the average individual's task is more difficult. A single advisor faces time constraints in both looking after clients and overseeing the investments in potentially hundreds of different client portfolios. By definition, the advisor must try to stay current on a multitude of different holdings – or rely solely on in-house research and analyst recommendations.

With an investment committee, the job of analyzing money managers and investments is shared by a group with wide-ranging backgrounds and expertise. Each member contributes to the process and, therefore, has conviction and accountability for decision making.

An investment committee is accountable for:

- ***Establishing and governing the overall investment objectives***
- ***Assessing and managing investment risks and ensuring controls are in place to mitigate them***
- ***Approving the engagement and monitoring of external money managers***
- ***Monitoring performance***
- ***Rebalancing asset mix in accordance with the overall objectives***

3 Public markets aren't the only place to invest.

The smart money diversifies their holdings with alternative assets.

For most investors, 'diversification' means owning a mix of stocks and bonds (or ETFs/ mutual funds of underlying stocks and bonds) to spread risk and enhance returns. This strategy works well in years when stocks are up and bonds are down, or vice versa.

However, over the past ten years, the direction of stocks and bonds has been remarkably similar: the correlation of returns between a traditional '60/40' balanced portfolio (60% stocks, 40% bonds) and a 100% stock portfolio was 0.98. Even a less risky 30% stock, 70% bond portfolio had a 0.84 correlation. See Figure 1.

What this data makes clear is that during some periods, stocks and bonds will move in the same direction, offering less downside protection than some investors may think.

As a rule, sophisticated and large investors lean toward alternative investments (e.g. non-market-traded investments such as real estate, private equity) to diversify their portfolios.

Alternative investments are compelling for their low correlation to public markets, unique income streams, capital preservation and inflation protection, and different risk-reward profiles.

A sampling of family offices found that high-net-worth investors have more than 20% of their portfolios in alternative investments.[5]

At the same time, investing in alternatives is a more complex process with a different set of risks requiring specialized skill sets and due diligence capabilities. They are also generally illiquid, have high investment minimums and higher fees to participate. As a result, investment committees need to have specialized expertise.

In a survey by RBC, smaller pension funds cited "lack of expertise" and "insufficient scale" as hurdles to investing in alternatives.[6]

Individuals who want to participate in alternative investing, and can meet certain investment criteria, are able to do so through exempt market dealers, who take on the role of sourcing, vetting and marketing the investments. Investors should take care to

5. Atherton Consulting Alternative Assets - A Current Perspective from RIAs and Family Offices - July 2014.

6. Reported in Globe & Mail by Janet McFarland on September 9, 2012 Pension plans see investing opportunities in alternative assets.

CORRELATION OF RETURNS RELATIVE TO ASSET MIX:

STOCK %	BOND %	CORRELATION TO A 100% STOCK PORTFOLIO
20	80	0.64
30	70	0.84
40	60	0.93
50	50	0.97
60	40	0.98
70	30	0.99
80	20	1.00

FIGURE 1

ASSUMPTIONS:

- Stocks represented by the S&P 500 Index (SPY ETF) U.S. dollar returns between October 31, 2005 and December 31, 2015
- Bonds represented by the S&P U.S. Aggregate Bond Index (AGG ETF) U.S. dollar returns between October 31, 2005 and December 31, 2015
- All data sourced from Thomson Reuters

align themselves with a high-quality provider that has stringent investment criteria and due diligence capabilities.

WHEN ARE ALTERNATIVES NOT ALTERNATIVES?

In recent years, traditional mutual fund companies and investment firms have also gotten into the game. A review of these offerings raises questions about whether some really are 'alternatives'. Often, what is billed as a 'real estate alternative' is really a portfolio of public REITs (real estate investment trusts) – subject to daily trading and market volatility just as stocks and bonds are. In our view, this doesn't meet the test of alternative investing. Contrast this with the ultra-high-net-worth investor's portfolio of real estate investments, held directly or through a private fund, which does not trade on an index and is not subject to daily volatility.

While the benefits of alternative investing are many, investors of all sizes should proceed with prudence, understand the risks and invest with specialists that have the resources, capabilities and track record in the space.

Alternative investments are compelling for their low correlation to public markets, unique income streams, capital preservation and inflation protection, and different risk-reward profiles.

4

Seeking and retaining experts globally is a critical skill set.

The smart money has a rigorous process for manager selection.

The smart money is prepared to admit that they are not experts at everything. Their expertise is in surrounding themselves with the right people with the right skill sets.

This is needed because the field of investing has become increasingly specialized.

No one money manager, regardless of how large or how legendary, can be exceptional in every asset class.

It is also true that the majority of professional money managers do not outperform the benchmarks for their asset class.

The fact is, even the best managers may underperform in any given year or two. However, over the long term, there are some that have proven to produce superior results consistently. The trick is to separate the wheat from the chaff – and then monitor them closely.

The process of investment manager selection is another area in which the practices of the smart money differ from those of the average investor or financial advisor.

First, large investors use their scale and networks to source and retain specialists from around the world – some of whom may not even be available to individual investors.

Second, the selection process is typically more rigorous and applied across multiple criteria such as the manager's investment acumen, risk profile, clarity and repeatability of investment process, organizational structure and resources, fees and incentives, etc. For some investment committees, it's an exhaustive process of research and analysis, due diligence and reference checks. And that's just the hiring process. Once the manager is retained there is the process of oversight to ensure they are executing and perfroming as expected.

5 Relationships and scale create opportunities.

The smart money uses their size and networks to access special investment opportunities not generally available to retail investors.

The smart money enjoys privileges when it comes to accessing unique investment opportunities, often limited to a small cadre of investors. Examples include:

- Pre-IPO private equities
- 'Institutional-only' funds
- Real estate limited partnerships with investment minimums of >$1 million

Even among the high-net-worth segment, many of these types of opportunities tend to be out-of-reach and are reserved for the ultra-high-net-worth and institutional class of investor.

An example is the Brookfield Infrastructure Group of Brookfield Asset Management, a global alternative asset manager. The Brookfield Infrastructure Group invests in large-scale projects such as toll roads, bridges, ports and hydroelectric power plants that underpin the global economy. These types of assets are long-term, stable and highly desirable to own because of their secure and growing cash flows and diversification away from public markets. Unfortunately, they're only available to a restricted group of institutional investors such as pension funds and money management firms, like Newport Private Wealth.

It's easy to understand why.

From a regulatory, time and financial standpoint, it is more efficient for institutional players to deal with a small group of sophisticated investors, than to service a mass market of retail investors and their advisors.

Infrastructure assets, such as toll roads, bridges, ports and hydroelectric power plants, etc. are long-term, stable and highly desirable to own because of their secure and growing cash flows and diversification away from public markets. They are typically reserved for large institutional and family office investors.

"In addition to size and scale, you need a network of relationships to turn up the sorts of private opportunities the retail investor never even sees," says Mark Kinney, Chief Investment Officer of Newport Private Wealth.

"After that, you still have to apply your process of review. In reality, most of the opportunities we are shown, we reject, either because they don't meet our investment criteria or they just aren't the right fit for the risk tolerance of our clients and ourselves."

While individual investors may not be able to access these special opportunities directly, working with an investment firm that does could open up opportunities to diversify, to mitigate market volatility and improve the overall quality of holdings in your portfolio, which, as the smart money knows, can lead to better returns with less risk.

6 ‘Setting and forgetting’ doesn’t work.

The smart money rebalances portfolios as part of the process.

Portfolio rebalancing is a very simple yet powerful strategy that every investor, regardless of portfolio size, can apply to better their results. There are two ways to approach it.

STRATEGIC REBALANCING

Let’s assume you have a formal IPS that states a target asset mix for your portfolio, within ranges. With the passage of time, market forces cause your asset mix to fall outside your target ranges. For example, in a rising stock market environment, your equity weighting will grow as a percentage of your overall portfolio. Higher stock prices could mean higher risk as valuations become inflated. Portfolio rebalancing is the process of selling those assets that have risen (and buying those that have fallen in price) to restore your overall asset mix to its stated target range. It is a way of protecting capital and taking the guesswork out of investing. Sounds easy?

Unfortunately, the opportunity to rebalance is too often overlooked and feels unnatural for some investors and their advisors. After all, why sell your best performers? What the smart money knows is that the practice has proven to improve returns over time.

Given their disciplined approach, institutional money managers and family offices are well set up to rebalance their portfolios. It’s just part of their process. Many of them also employ a process of tactical rebalancing, which is different from strategic rebalancing. It’s less automatic and requires greater investment acumen.

TACTICAL REBALANCING

To understand tactical rebalancing, we refer to our earlier example. When an investor’s equity weighting grows beyond its target allocation due to a rising stock market, the investment committee may appraise the overall economic and market conditions, determine that the environment remains favourable for equities and, subsequently, decide to temporarily increase the target equity allocation. This is tactical rebalancing. Obviously, this approach is dependent upon accurate forecasting and it allows a skilled investment committee to add value to the portfolio.

Newport Private Wealth.

Putting it all together for the individual investor.

The Newport Private Wealth Investment Committee is able to draw from a large universe of traditional and alternative asset categories in managing client portfolios.

WHILE IT MAY BE TRUE THAT IN THE HIERARCHY, BILLIONAIRE AND INSTITUTIONAL INVESTORS ENJOY A PREFERRED STATUS OVER THE INVESTING PUBLIC, A SOLUTION EXISTS FOR HIGH-NET-WORTH INVESTORS:

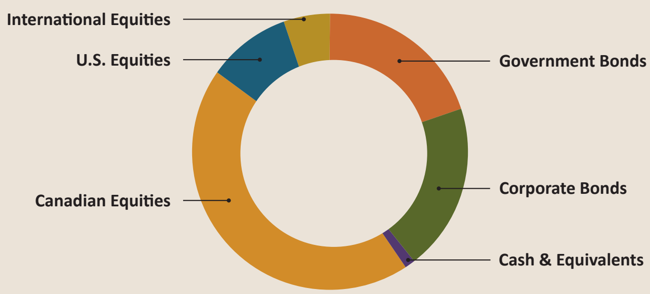
Newport Private Wealth is a Toronto-based wealth management firm founded by a group of investment executives who had their own capital to invest and wanted to create the best of both worlds: the privileges of an institutional investor coupled with the personal service and integrated wealth management of a boutique. The firm's investment program employs the best practices outlined in this whitepaper.

1. A FORMAL PROCESS AND TEAM TO MANAGE YOUR MONEY

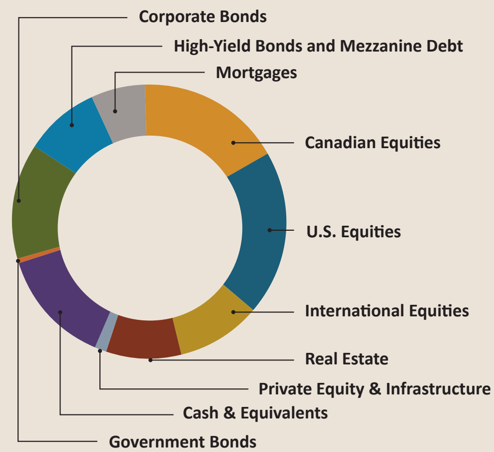
Newport Private Wealth has a long-established Investment Committee for the management and oversight of client portfolios, not just one or two individuals. Investment Committee members

FIGURE 2

TYPICAL PORTFOLIO



NEWPORT PRIVATE WEALTH PORTFOLIO



are senior professionals, having, on average, 25 years of experience, with successful backgrounds in finance, accounting, law and business. The Committee has knowledge on diverse subjects ranging from mortgage lending to corporate finance to tax and legal issues, to name just a few.

This is a figurative illustration of asset mix for a Newport Private Wealth balanced portfolio, compared to a typical investor's portfolio. Asset allocations are made through proprietary Newport Funds and will change due to market conditions, our investment strategy at any given time and the unique situation of every client.

The Committee meets formally on a weekly basis – informal consultations occur day-to-day – to deal with the business of stress-testing various risk/return scenarios, setting asset mix and portfolio rebalancing, selecting and reviewing managers and direct investments, etc.

It has, among its storehouse of intelligence resources, a highly-respected independent economist and a network of contacts in various industries that are called on for specialized knowledge and perspective, as needed. Prior to finalizing any decisions, in-depth investment memos are prepared and committee members review, discuss and debate the merits and hazards of each proposal, carefully weighing the trade-offs between risk and return.

Finally, committee members also invest their own money alongside clients, which ensures that interests are aligned and decisions are taken from the perspective of a client. This fact, together with the rich diversity of perspectives and uncommon discipline, makes the investment process better and more robust. The benefit for clients is that a better process leads to better investment results.

2. TRUE DIVERSIFICATION

Newport Private Wealth's investment approach combines traditional and alternative investments in a professionally-managed, liquid portfolio. Specifically, the Investment Committee has 10 different asset categories to draw on for portfolio construction. See Figure 2.




Newport client portfolios benefit from the firm's access to unique private opportunities, from investments in retirement homes to apartment buildings, to infrastructure assets throughout the world.

It is perhaps the Committee's greatest strength that it is able to find and invest successfully in alternative asset classes that require specialized knowledge. As a result, portfolios are far more diversified than the traditional '60/40 stocks and bonds' model, thus diminishing dependence on public markets, reducing risk and evening out returns.

This is ideal for clients who don't like the volatility of stock market investing, but still need and want their money to grow ahead of inflation, taxes, etc.

3. SPECIALISTS FOR EVERY ASSET CLASS

The Newport Investment Committee sources and retains independent money managers from around the world – some of whom are not available to individual investors.

The Committee's independence from its stable of external managers (known in the industry as 'open architecture') provides the flexibility for changes at any time, for any reason.

That's because the Committee's process of selection is extraordinarily rigorous and comprehensive. Specialist managers are selected, not only for proven expertise in a particular asset class, but also for their fit for the risk profile and expectations of Newport's high-net-worth clients.

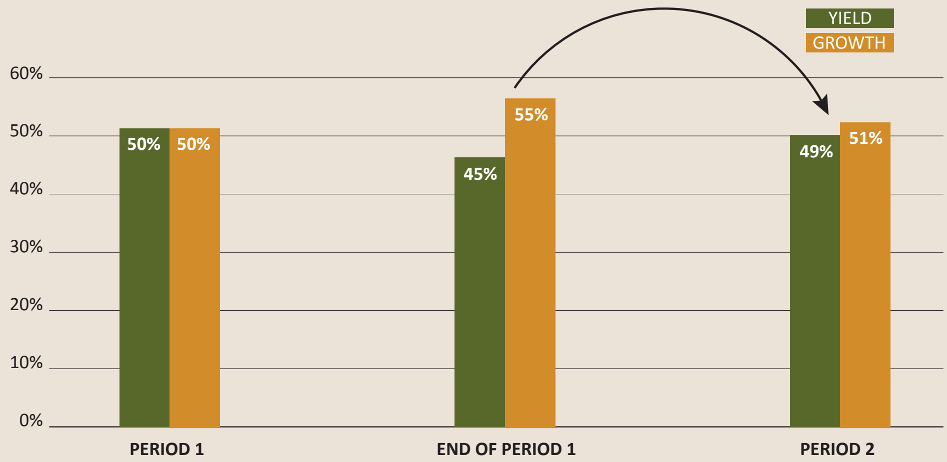
Due diligence efforts include everything from volatility measurement and predictability of returns, to correlation with other managers in the portfolio, to the depth of the resources and infrastructure supporting the manager.

The Committee has been known to spend two to three years following a money manager before it actually invests.

"Even then, we'll frequently start with a smaller investment and build on it as our confidence grows that the strategy is being implemented as advertised," says Kinney.

TACTICAL PORTFOLIO REBALANCING

FIGURE 3



This is a theoretical illustration of how the Newport Investment Committee rebalances portfolios. In period one, the Investment Committee sets asset mix based on target ranges and its outlook for each asset class. Market performance changes the asset mix during the period. So at the start of period two, the Investment Committee rebalances tactically based on target ranges and a revised outlook for each asset class.

"It takes more time but, overall, we think it's a better process and another way we manage risk in pursuit of returns."

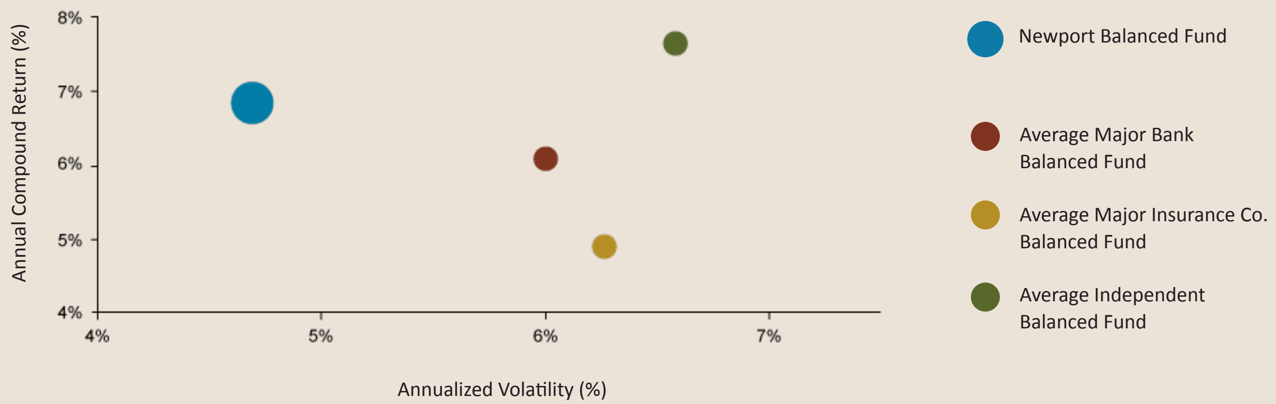
4. ACCESS TO UNIQUE OPPORTUNITIES

A hallmark feature of Newport Private Wealth's investment approach is its ability to unearth and invest in unique private opportunities, generally only available to a narrow universe of investors.

Examples include direct investment in well-located apartment buildings in the U.S. and Canada, private investments, private mortgages, infrastructure and private mezzanine debt. These alternatives have long been popular with the ultra-high-net worth and pension fund investors because they have different risk profiles – helping to lower the overall risk in the portfolio and earn steadier returns.

The Newport Investment Committee is regularly shown opportunities derived from the members' extensive networks, experience in alternative investing and reputation as 'tough but reliable' capital partners. Only a few are selected, given the Committee's stringent standards of selectivity. "For every investment we make, we probably look at forty or fifty," explains Kinney.

FIGURE 4 AVERAGE ANNUAL COMPOUND RETURNS/RISK FOR BALANCED MUTUAL FUNDS



The average returns are represented by the quarterly performance of fifteen representative mutual funds between January 1, 2011 and December 31, 2015. The universe is made up of the balanced funds of five major banks, five large independent fund companies and five major insurance companies. Fund returns were obtained from public filings found on www.sedar.com. Included in this universe are: RBC Select Balanced Fund, BMO Fund Select Balanced Portfolio, TD Comfort Balanced Portfolio, Scotia Balanced Opportunities, CIBC Managed Balanced Portfolio Sr B, AGF Elements Balanced Portfolio, Mawer Blanced A, CI Portfolio Series Balanced, Beutel Goodman Balanced Cl D, Manulife Simplicity Balanced, Great West Life Balanced Portfolio, Sun Life Balanced Portfolio, Canada Life Balanced, and Standard Life Ideal Balanced. Volatility was calculated as the annualized standard deviation of quarterly returns for each fund between January 1, 2011 and December 31, 2015.

5. PORTFOLIO RE-BALANCING OCCURS QUARTERLY

The Newport Investment Committee rebalances asset mix – both strategically and tactically. It meets weekly to discuss developments in the economy and capital markets and undertakes a formal rebalancing exercise quarterly. By managing asset mix within stated ranges, adjusting the allocation of capital to specialist managers, and seizing undervalued areas of investment, the Investment Committee adds value to client portfolios. See Figure 3.

6. STEADY RETURNS

Many investors own exchange-traded funds (ETFs) or mutual funds whose performance closely mirrors the performance of an index. By definition, this demands a high tolerance for volatility that most high-net-worth investors would prefer to avoid if they could. Newport Private Wealth's investment platform was built to deliver more predictable returns. Figure 4 compares the performance of the Newport Balanced Fund against the average risk/returns of a universe of fifteen balanced mutual funds. What it shows is that the Newport Balanced Fund had significantly lower volatility, while nearly matching the highest average rate of return among the peer group. The investment platform is built to deliver a smoother ride and, as this chart shows, it achieves that.

	TYPICAL APPROACH	NEWPORT PRIVATE WEALTH
DIRECT CONTACT	Licensed Advisor/Salesperson/Mutual Fund Representative	Licensed Portfolio Manager
ASSET MIX AND INVESTMENT UNIVERSE	Asset mix set by Advisor, Mutual Fund Rep, or 'roboadvisor' Cash & Equivalents; Government Bonds; Corporate Bonds; Canadian Equity; U.S. Equity; International Equity	10-member Investment Committee (CFAs, CPA/CAs, LL.B.s, MBAs) sets asset mix; average 24 years of investment experience Cash & Equivalents; Government Bonds; Corporate Bonds; High-Yield Bonds; Mortgages; Canadian Equity; U.S. Equity; International Equity; Real Estate; Private Equity & Infrastructure
ASSET CATEGORY MANAGERS	Mutual fund managers may be internal or external	A global universe of independent specialized managers in traditional and alternative asset classes, objectively selected and monitored by the Investment Committee
REBALANCING	Variable	Quarterly and as needed by the Investment Committee
PORTFOLIO	A collection of mutual funds, public securities, ETFs, etc. Portfolios are often over-diversified with index-like characteristics.[7]	A cohesive and liquid, professionally-managed portfolio

The illustration compares the service model of a typical advisor with that of Newport Private Wealth, where clients enjoy the benefit of the intellectual capital of the entire senior management team.

INVESTMENT MANAGEMENT INTEGRATED WITH OVERALL WEALTH MANAGEMENT

A popular maxim around Newport Private Wealth is, "if you're just managing your investments, you're not truly managing your wealth." High-net-worth investors typically have complicated corporate and personal financial affairs. Newport Private Wealth's professionals help clients better manage their entire balance sheet. Drawing on their diverse professional skill sets and decades of experience serving some of Canada's wealthiest families, and working collaboratively with a client's external advisors, the team is able to add value to any situation a high-net-worth individual may encounter.

If you've been expecting more,
we've been expecting you.

For more information visit newportprivatewealth.ca

7. Based on our sampling of portfolio analyses for prospective clients.

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