Maintenance

Airplanes don't fly around long without maintenance. That varies from a quick inspection every night to completely stripping the aircraft to the bones, inspecting and rebuilding. Keeping several million moving parts perfectly airworthy for a projected useful life of 50 years takes a little TLC. Parts wear out and must be replaced. Other parts need to be upgraded to take advantage of improved design and efficiency.

By the way, aircraft mechanics are professionals certified by the FAA. You expect before you put your family on an airplane that the person signing it off as airworthy has the training, testing, certifications and experience to care for your precious cargo.

Your investment portfolio needs continuous maintenance, too. Clearly you would like to avoid catastrophic failures. But avoiding crashes is only part of the problem. Keeping it running at optimum efficiency will greatly enhance your future security.

- Rebalancing to keep the original risk profile. Left to it's own devices a very well designed portfolio will morph over time as asset classes diverge to grow or fall at different rates. It's counterintuitive to sell assets that have appreciated in value in order to buy underperforming asset classes. But, rebalancing enforces a discipline of buying low and selling high at the margin that adds considerable value over time.

- Addition of new desirable asset classes. Thousands of new investment products are introduced each year. Most are clones of existing products, or a bad idea recycled under a new brand name. However, a very few offer valuable diversification benefits that over time will enhance performance while reducing risk. We prefer to incorporate new products after they have stood the test of time. I'd much rather be late adopting a new asset class than jump on to something that I didn't fully understand and have it bite my clients.

- Substitution of cheaper funds. The market has vastly improved pricing for exposure to asset classes through the mutual funds and ETFs that offer them. The internal expenses and trading costs today are a very small fraction of what they were when I entered the security business. If there are no tax consequences and low trading costs it's always better to own a low cost portfolio than an expensive one. Costs matter and small incremental cost reductions add up to large differences in performance over the long haul.

- Dividend avoidance. ETFs and Mutual Funds announce their estimated dividends in advance. Those dividends will come with a tax cost. If selling the fund in a taxable portfolio just before the dividend is declared has a smaller cost than recognizing the dividend, that will clearly save capital that can live to grow for you. It takes a few calculations to net out the costs and benefits, but because taxes are the greatest expense investors face, it's well worth the effort. Keeping dollars in play that would otherwise get taxed away pays huge dividends.

- Tax loss harvesting. Occasionally investments go down in value. It's annoying when that happens. But, it gives the investor an opportunity to recognize a taxable loss that she can deduct against gains otherwise in her portfolio. If she doesn't have gains, she can store them against future gains. Again, it takes a few calculations to sort out long term gains, and short term gains, but it's a very positive thing for long term performance. Think of it as turning lemons into lemonade.

- Conversion of short term gains to long term gains. Whenever you must sell a security you should look at the tax implications. If that security has a short-term gain, the tax will be approximately twice as high as if you waited to sell it when it qualified for long term gain. Perhaps you should sell another security at less tax cost, or simply wait until it qualifies for the lower taxation.

Tax aware investing is complicated and tedious unless you have sophisticated software to track your portfolio on a daily basis. But, every dollar that marches away to the tax man is never coming back. It can't be reinvested or spent. So, your yardstick for measuring performance must be after tax returns.

There is nothing magic about portfolio maintenance. It's just the basic TLC that keeps a portfolio tuned up and performing optimally for the long haul.

Every decision to buy or sell a security involves multiple tradeoffs. Many investors can't or won't take the time and effort incorporate it into their long-term strategy. If not, they might be well advised to hire a professional to do it for them. Protecting that precious cargo must be mission number one. After all, your investments are your future.

Have a good trip

When aircrews meet each other anyplace in the world, they often end their conversations with: "Have a good trip". It's a metaphor for life. If you plan, follow a few basic rules, exercise judgement and discipline, your life and investment experience can be a good trip.

So, let me wish you all: Have a good trip!

Excerpted from "A 30,000 Foot View", Frank Armstrong's contribution to *The New Book of Investing Rules*, which will be published by Harriman House in Autumn 2017.