



# **NaviPlan Standard Online/Offline**

## **Asset Allocation Self-Study Guide**

**USA version 11.0**

EISI, Winnipeg

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# Asset allocation

The NaviPlan Standard Asset Allocation Self-Study Guide was created using NaviPlan Standard Offline with the Ibbotson Asset Allocation option. This option allows you to use actual Ibbotson return rates in NaviPlan's calculations.

**Note:** If you are using a version of NaviPlan without the Ibbotson Asset Allocation option, or if you are using NaviPlan Online, there will be some differences between the guide and your version of NaviPlan.

NaviPlan Standard, with the Ibbotson Asset Allocation option, provides you with a questionnaire to determine your clients' investor profile. You can override the questionnaire results and select an investor profile directly (but you must fill out the questionnaire first).

In either case, NaviPlan suggests an asset mix appropriate for clients with that profile. In Level 2 and Level 3 Plans, you can modify the suggested asset mix. This suggested asset mix is used as an asset allocation target (a model to achieve) throughout the plan.

The exercises in this module are based on a version of NaviPlan Standard Offline that includes the Ibbotson Asset Allocation option, which means that the asset allocation settings (asset classes, investor profiles) are set up for you. If your version of NaviPlan Standard Offline does not include the Ibbotson Asset Allocation option, you can modify the data.

## Learning objectives

This module will enable you to

- Use the Asset Allocation analysis
- Interpret the *Asset Allocation* client report
- Reallocate assets in a plan

## Learning tools

This module includes some practice exercises. We recommend that you use the Nick and Lisa Brown (Brown, Nick and Lisa.nps) client file in the data folder of your installation of NaviPlan Standard Offline (the default path is C:\Program Files\EISI\Data, but you may have installed it elsewhere). It will be available when you run NaviPlan Standard Offline, as well as on the central server if you prefer to work in the online application.

**Hint:** In NaviPlan Standard Offline, to find the location of your data directory, go to the **User Preferences** menu – **System Settings** selection – **User Preferences - System Settings** dialog box – **File Locations** tab.

## Use the Asset Allocation analysis

Two levels of detail are available in the Asset Allocation analysis: simple and detailed. If you use the simple Asset Allocation analysis, you can promote it to a Level 1, 2, or 3 Plan. The detailed Asset Allocation analysis can be promoted to a Level 2 or 3 Plan, but not a Level 1 Plan. Promoting an analysis to a plan enables you to create a more advanced analysis without having to re-enter the client information already gathered.

## Create an Asset Allocation analysis

You can create and use the Asset Allocation analysis to review your clients' current asset allocation, establish their risk tolerance, and create a proposed allocation. You can use the *Asset Allocation* client report to compare the clients' current allocation to the proposed allocation.

### To create a new Asset Allocation analysis

1. Go to the **Plan Management** section – **Plan List** category – **Plans** page, and then click the **New** button. The *Plan Creation* dialog box opens to the *Plan Selection* tab.

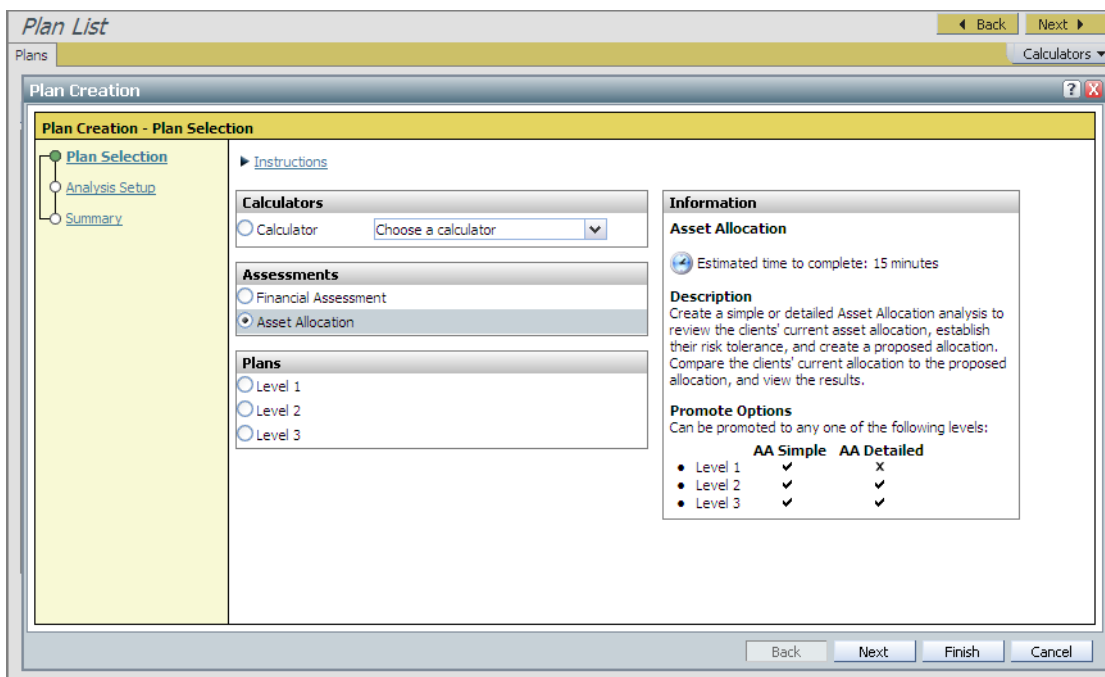


Figure 1: Plan Management section – Plan List category – Plans page – New button – Plan Creation dialog box

2. Under *Assessments*, select **Asset Allocation**, and then click **Next**. The *Analysis Setup* tab opens.

3. Enter a unique name for your Asset Allocation analysis in the *Assessment Name* field, and the start year for the plan in the *Plan Year* field, and then click **Next**. The *Summary* tab opens.
4. Verify the information on the *Summary* tab, and then click **Finish**. The *Plan Creation* dialog box closes, and NaviPlan opens to the *Asset Allocation* section – *Asset Allocation* category – *General* page.

## Enter general information

Once you have created the Asset Allocation analysis, you can enter the clients' data.

Figure 2: Asset Allocation section – Asset Allocation category – General page

You can enter or modify the *Assessment Name* and *Assessment Analysis Date* on the *Asset Allocation* section – *Asset Allocation* category – *General* page. When you select the *Use today's date* check box, the *Assessment Analysis Date* updates each time you open the *Asset Allocation* analysis.

## Enter simple or detailed accounts

The *Accounts* page in the *Asset Allocation* analysis offers two modes of account data entry:

- Simple account entry mode
- Detailed account entry mode

To switch from simple account mode to detailed account mode, click the **Detailed Accounts** button on the *Asset Allocation* section – *Asset Allocation* category – *Accounts* page.

You can enter the following information in both simple and detailed account modes:

- *Market Value* – Enter the account market value based on the *Assessment Analysis Date* (assumed valuation date)
- *Asset Class Weightings* – Classify the account based on specific asset classes or manual classification, and then the return rates populate automatically
- *Return Rates* – Override return rates for pre-retirement and retirement periods by clicking the *Return Rates* link

In the detailed account entry mode you can also

- Enter holdings within an account
- Search for and classify holdings using the holding's ticker symbol, type, or asset class

The screenshot shows the 'Asset Allocation' section of the NaviPlan software. It features a navigation bar with tabs for 'General', 'Accounts', 'Questionnaire', 'Profile', 'Summary', and 'Client Report'. Below the navigation bar, there are buttons for 'Back' and 'Next'. The main content area is titled 'Detailed Accounts' and includes a 'Hide Instructions' link. A note states: 'Use the "Add" button to create an account. If client data is contained in the central database, Import Accounts will retrieve the available information.' Below this note is a table titled 'Qualified and Non-Qualified Accounts'.

Description*	Plan Type*	Annuity	Additional Settings	Owner*	Market Value*	Basis*	Asset Class Weightings	Return Rates	Delete
Joint Savings Accou	Non-Qualified	<input type="checkbox"/>	Details	Joint	\$50,000	\$50,000	45% Large Cap Equ...	7.05%	X
Lisa's Brokerage Acco	Non-Qualified	<input type="checkbox"/>	Details	Joint	\$55,000	\$46,000	80% Large Cap Equ...	5.63%	X
Nick's Brokerage Ac	Non-Qualified	<input type="checkbox"/>	Details	Joint	\$61,000	\$47,500	67% Large Cap Equ...	11.88%	X
Nick's 403(b)	403(b)	<input type="checkbox"/>	Details	Nick	\$25,000	\$0	50% Large Cap Equ...	8.02%	X
Lisa's Roth 401(k)	Roth 401(k)	<input type="checkbox"/>	Details	Lisa	\$50,000	\$0	50% Large Cap Equ...	6.89%	X
Kevin's 529	529 Plan	<input type="checkbox"/>	529 Plan	Nick	\$12,000	\$0	25% Large Cap Equ...	5.81%	X

At the bottom of the table is an 'Add Account' button.

Figure 3: Asset Allocation section – Asset Allocation category – Accounts page (simple account entry mode)

There are several other distinguishing differences between simple and detailed account entry modes:

- In the simple account mode, you can promote the Asset Allocation analysis to a Level 1, 2, or 3 Plan
- In the detailed account mode, you can only promote the analysis to a Level 2 or 3 Plan
- Once you have selected the detailed account mode you cannot return to a simple account mode, but you can add simple accounts by clicking *Add Account – Simple Account*

#### To enter an account

1. Click the **Add Account** button to create an account. If client data is contained in the central database, clicking *Import Accounts* will retrieve the available information.
2. To enter more detailed account or annuity information, click **Detailed Accounts**.

### Complete the asset allocation questionnaire

With the Ibbotson Asset Allocation option, a questionnaire is provided to determine the clients' risk tolerance. NaviPlan determines the selection of the appropriate investor profile.

Use the *Questionnaire* portion of the *Asset Allocation Fact Finder* to gather information, and then answer the questions on the *Asset Allocation section – Asset Allocation category – Questionnaire* page.

A score is calculated when every question in the questionnaire has been answered. Each possible score is associated with an investor profile, which in turn is associated with a suggested asset mix. This suggested asset mix is used as an asset allocation target.

Blank *Asset Allocation Fact Finder* forms are available on the EISI Support Site: [http://support.eisi.com/support\\_us/nps\\_offline/v11/tips\\_and\\_tools/data\\_collection\\_forms.htm](http://support.eisi.com/support_us/nps_offline/v11/tips_and_tools/data_collection_forms.htm)

## View the suggested asset mix

The *Asset Allocation* section – *Asset Allocation* category – *Profile* page displays the breakdown of the suggested asset mix that was determined by your answers to the questionnaire.

The *Profile* page also displays a summary of your clients' investment profile containing the following:

- the proposed investor profile
- the proposed time horizon
- the expected rate of return
- the expected standard deviation

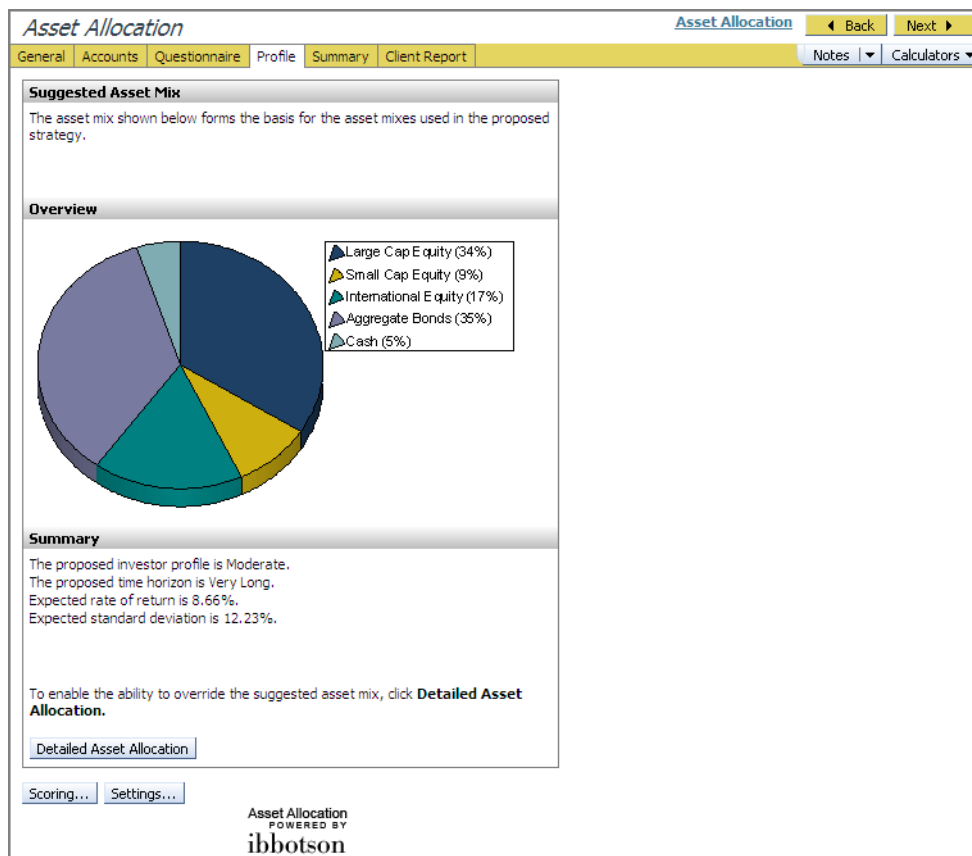


Figure 4: Asset Allocation section – Asset Allocation category – Profile page (simple asset allocation)

If you are using the simple asset allocation mode of the asset allocation analysis, you need to promote it to a plan level in order to edit the suggested asset mix.

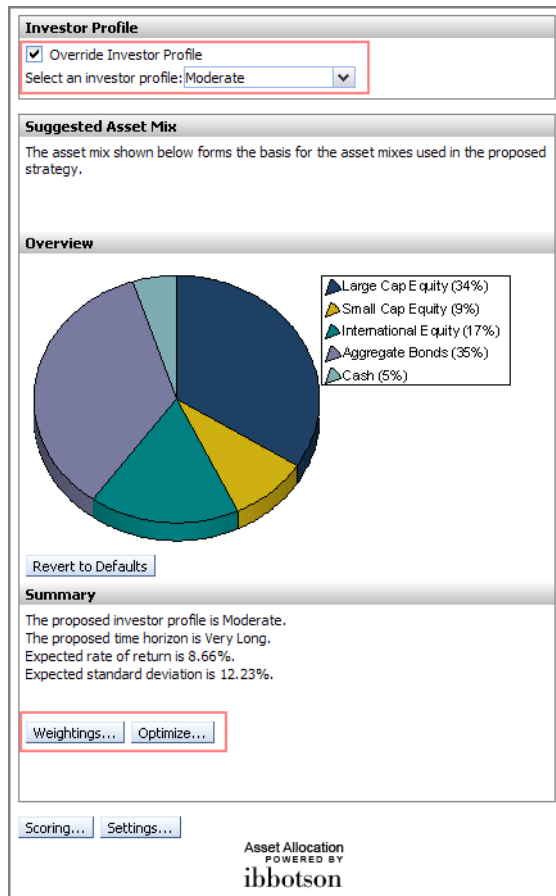


Figure 5: Asset Allocation section – Asset Allocation category – Profile page (detailed asset allocation)

Clicking the *Detailed Asset Allocation* button changes the simple asset allocation to detailed asset allocation, and gives you more control over the investor profile, time horizon, etc.

In detailed asset allocation mode you can override the investor profile by selecting *Override Investor Profile*, and then selecting a new profile from the *Select an investor profile* list. Selecting a different investor profile changes the suggested asset mix.

Two new buttons appear when you change from simple to detailed asset allocation:

- *Weightings* allows you to override the default asset class weightings of the suggested asset mix
- *Optimize* allows you to enter a minimum and maximum percentage range for the asset class

**Note:** Analyses in detailed asset allocation mode can be promoted to Level 2 and Level 3 Plans, but not to Level 1 Plans.

## View the asset allocation comparison

The *Asset Allocation* section – *Asset Allocation* category – *Summary* page displays a comparison of the current asset mix with the suggested asset mix.

This summary view displays the differences in the rate of return, standard deviation, and the asset mix.

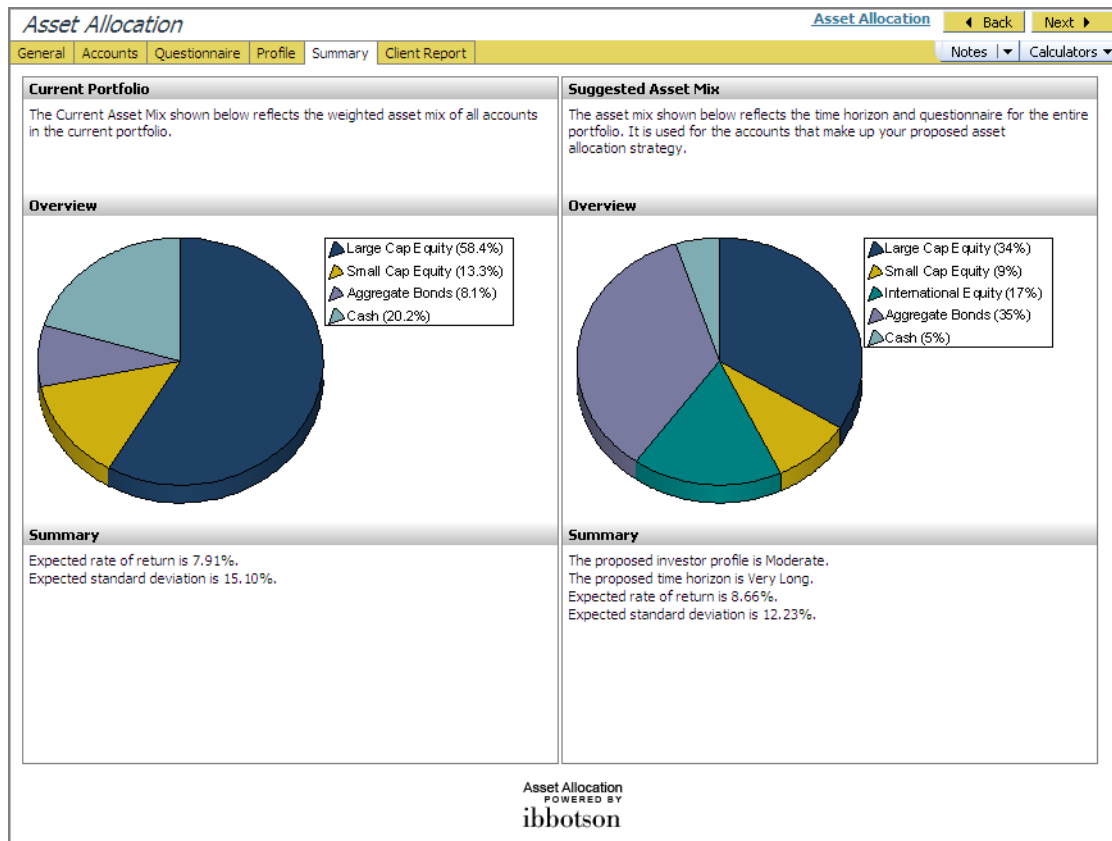


Figure 6: Asset Allocation section – Asset Allocation category – Summary page

## Interpret the Asset Allocation client report

The *Asset Allocation Analysis* report is a large report composed of many different sections. It combines text and graphs to give you an overview of your clients' current assets, risk tolerance, current asset mix, portfolio breakdown, and suggested asset mix.

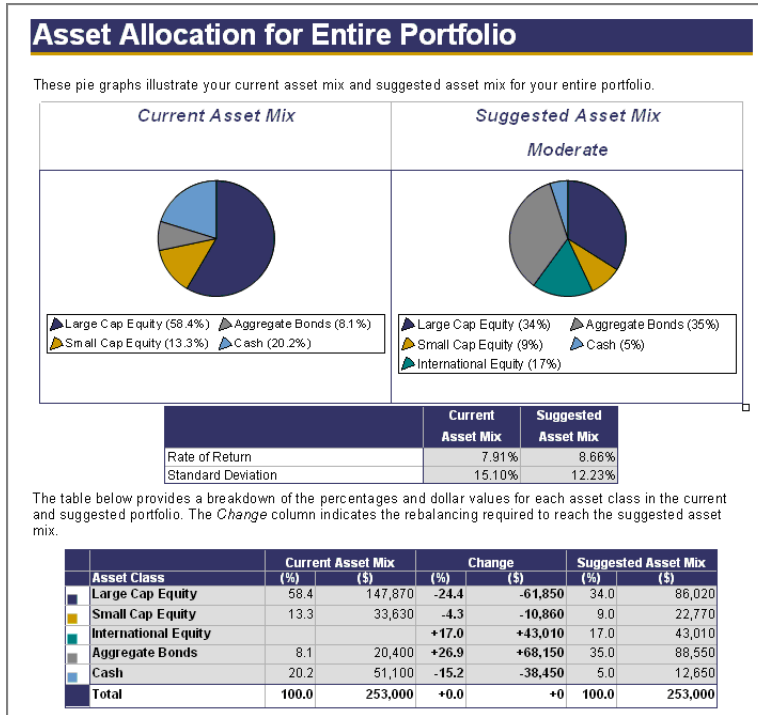


Figure 7: Asset Allocation section – Asset Allocation category – Client Report page – Generate button – Asset Allocation for Entire Portfolio report

This report is available in the Asset Allocation analysis as well as in all three planning levels.

## Generate the report

To generate and view the *Asset Allocation* client report

1. Go to the **Asset Allocation** section – **Asset Allocation** category – **Client Report** page, and then select **Default Template** from the *Template* list.
2. Click the **Select Document Sections** button to open the *Select Document Sections* dialog box.

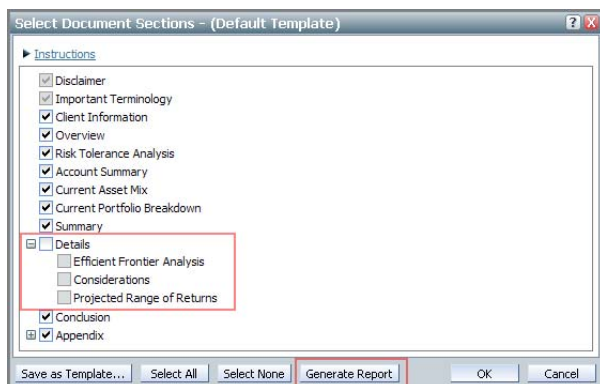


Figure 8: *Select Document Sections* dialog box

3. Clear the **Details** check box to reduce the size of the report, and then click the **Generate Report** button. The *Asset Allocation* client report opens.

## View the report

The report includes two mandatory sections (*Disclaimer* and *Important Terminology*), plus the sections that remained selected in the *Select Document Sections* dialog box.

Let's look at several sections of the report:

- *Client Information* – Displays a recap of the client information entered in the assessment
- *Asset Allocation Overview* – Discusses the basic principles behind asset allocation
- *Risk Tolerance Analysis* – Displays the answers to the questionnaire
- *Account Summary* – Shows the assets used in the asset allocation
- *Current Asset Mix* – Displays the current asset mix in a table format
- *Asset Allocation for Entire Portfolio* – Displays a side-by-side comparison of the current asset mix and the suggested asset mix, and displays recommendations on how to achieve the suggested asset mix

If further planning is needed, promote the Asset Allocation analysis to a Level 2 or 3 Plan.

## Reallocate assets in a plan

Reallocating assets in a plan allows you to modify the clients' current asset allocation mix and asset returns based on the clients' risk tolerance.

### Promote an Asset Allocation analysis to a Level 3 Plan

To reallocate assets, you must first promote the Asset Allocation analysis to a Level 3 Plan.

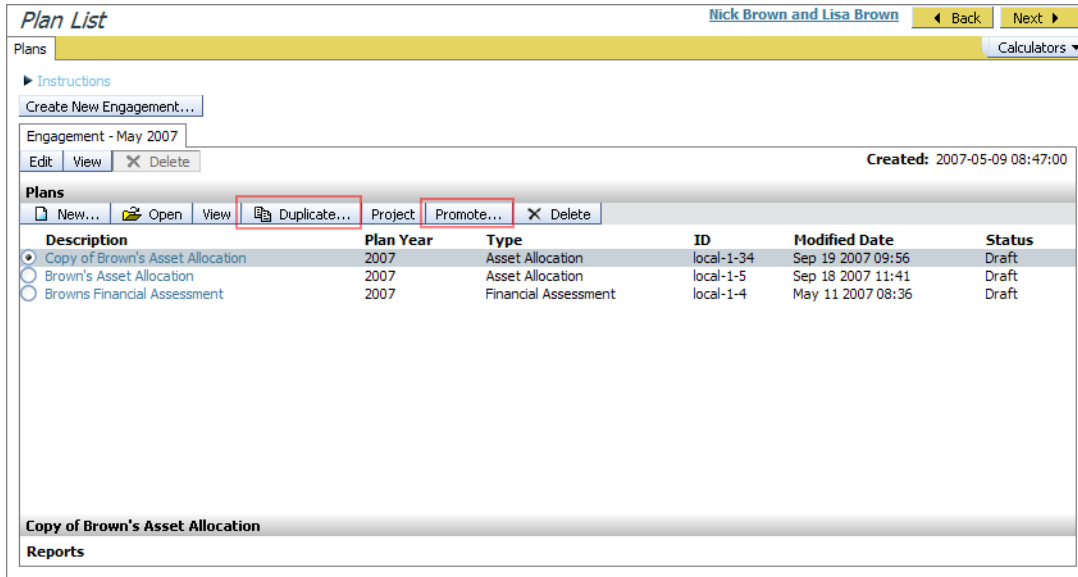


Figure 9: Plan Management section – Plan List category – Plans page

### To promote the analysis to a Level 3 Plan

1. Go to the **Plan Management** section – **Plan List** category – **Plans** page, select the **Brown's Asset Allocation** plan, and then click the **Promote** button. The *Promote Plan* dialog box opens.

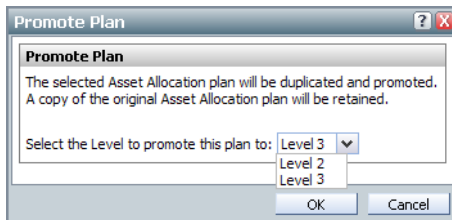


Figure 10: Plan Management section – Plan List category – Plans page – Promote Plan button – Promote Plan dialog box

2. Select **Level 3** from the *Select the Level to promote this plan to* list, and then click **OK**.

A Level 3 Plan, based on the Asset Allocation analysis, has been created, and can be used to apply asset reallocation strategies.

## Modify asset allocation in a Level 3 Plan

The asset allocation in a Level 3 Plan is very similar to an Asset Allocation analysis. After opening the Level 3 Plan you just created, go to the **Plan Management** section – **Asset Allocation** category – **Profile** page to view and modify the investor profile.

In a Level 3 Plan, you can

- override the investor profile and asset class weightings
- optimize holdings based on the *Efficient Frontier* graph

The screenshot shows the 'Asset Allocation' software interface. The main window is titled 'Asset Allocation' and has a 'Level 3' tab. The 'Profile' page is active, showing an 'Investor Profile' section with a checked 'Override Investor Profile' box and a dropdown menu set to 'Conservative'. Below this is a 'Suggested Asset Mix' section with a pie chart and a legend. The legend lists: Small Cap Equity (12.7%), International Equity (11.9%), Aggregate Bonds (45.7%), and Cash (29.7%). A 'Revert to Defaults' button is below the chart. A 'Summary' section provides details about the investment profile and asset mix. At the bottom left, a 'Weightings...' button is highlighted with a red box. A red arrow points from this button to an 'Asset Class Weightings' dialog box that is open. The dialog box contains a table with columns for 'Class Name' and 'Class Percentage'.

Class Name	Class Percentage	Class Name	Class Percentage
Large Cap Equity	0.00%	Aggregate Bonds	45.72%
Small Cap Equity	12.66%	Cash	29.73%
International Equity	11.89%		
		<b>Total</b>	100.00%

Figure 11: Plan Management section – Asset Allocation category – Profile page – Weightings button – Asset Class Weightings dialog box (Level 3 Plan)

### To modify the asset class weightings for a given investor profile

1. Go to the **Plan Management** section – **Asset Allocation** category – **Profile** page, and then click the **Weightings** button. The *Asset Class Weightings* dialog box opens.
2. Modify the **Class Percentage** for any or all of the asset classes, and then click **OK**.

These modifications will be noted in client reports.

## Modify standard deviation

The *Efficient Frontier* graph shows you the most efficient asset mix with the maximum expected return for a given level of risk. Standard deviation is a measure of how much the rate of return fluctuates around its historical average. The higher the standard deviation, the greater the degree of risk. Modifying the suggested standard deviation gives you some control over the risk factor in an investment.

If the *Efficient Frontier* graph displays the clients' current asset mix below the efficient frontier line then the clients' returns are low for the amount of risk, or the return is suitable but the level of risk is too high.

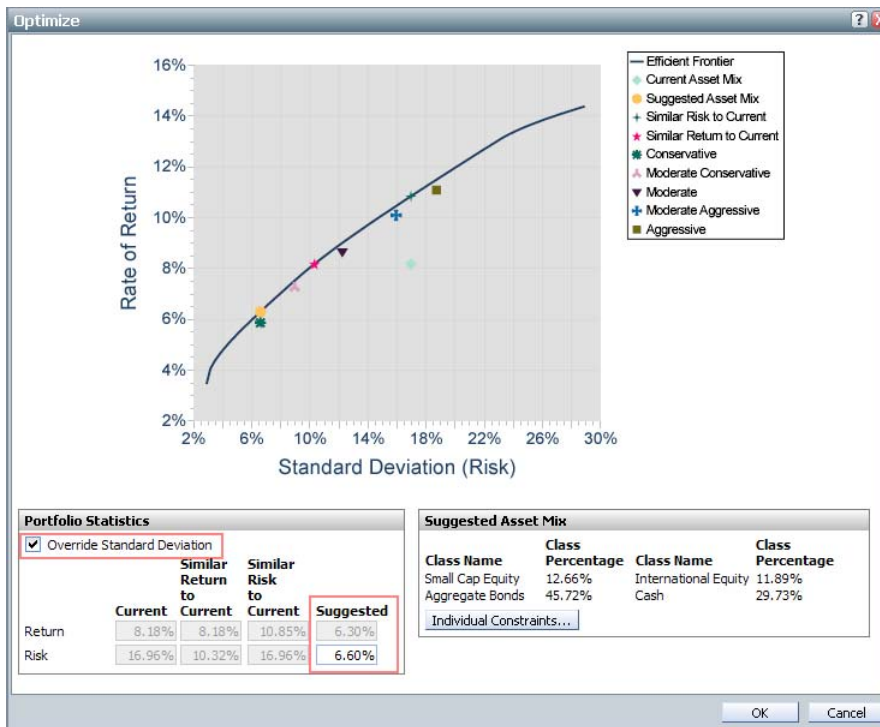


Figure 12: Plan Management section – Asset Allocation category – Profile page – Optimize button – Optimize dialog box

Clicking the *Optimize* button opens the *Optimize* dialog box and displays the *Efficient Frontier* graph. The graph plots overall return rates and standard deviation. The solid line in the graph represents the efficient frontier which is the set of portfolios that provides the highest expected returns for their respective risk levels.

### To override the standard deviation

1. Select the **Override Standard Deviation** check box to manually enter a new standard deviation. The *Risk* field under *Suggested* becomes editable.
2. Enter the standard deviation in this field. Once a new standard deviation is entered, the graph updates to show the manually entered standard deviation.

- Click **OK** to close the *Optimize* dialog box. The *Suggested Asset Mix* graph on the *Profile* page updates to display the optimization.

**Note:** Click a point on the *Efficient Frontier* graph to show the return rate and standard deviation of that point. Double-click a point on the line of the *Efficient Frontier* graph to use that point as the new suggested asset mix. Use this process as an alternative to manually override the standard deviation.

## Modify individual constraints

Constraints are used to prevent assets with favorable inputs from dominating a portfolio. This helps maintain diversity in a portfolio.

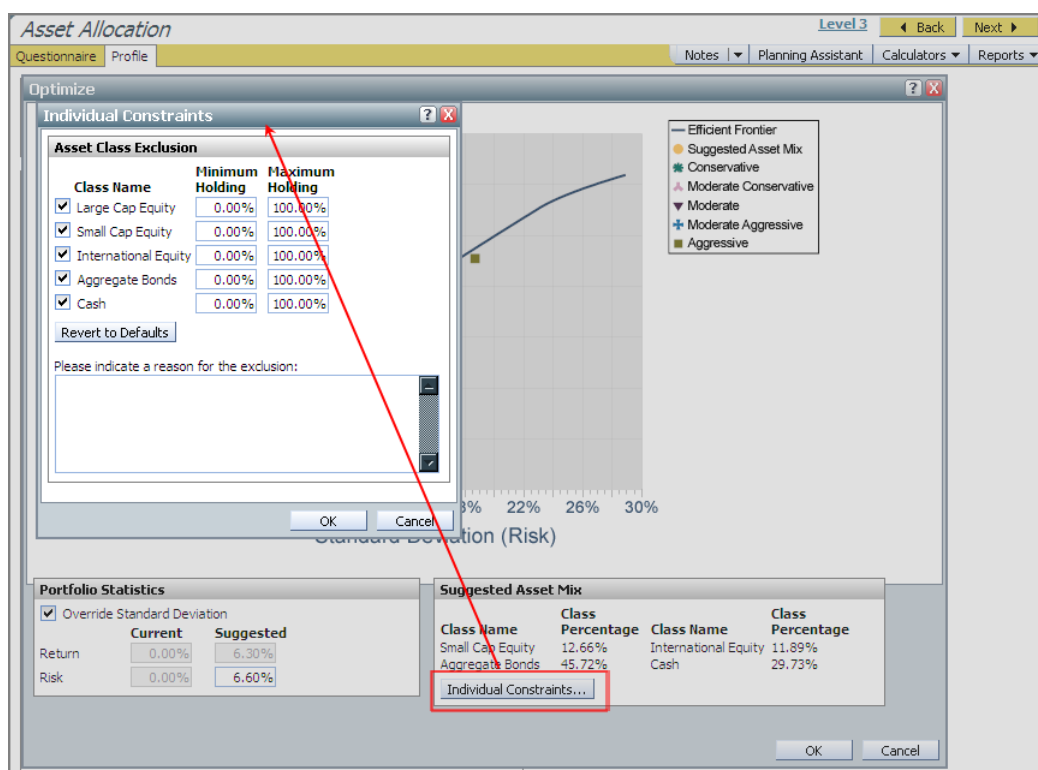


Figure 13: Plan Management section – Asset Allocation category – Profile page – Optimize button – Optimize dialog box Individual Constraints button – Individual Constraints dialog box

### To modify the individual constraints

- Click the **Optimize** button on the **Plan Management** section – **Asset Allocation** category – **Profile** page. The *Optimize* dialog box opens.
- Click the **Individual Constraints** button to open the *Individual Constraints* dialog box, and then set the maximum or minimum allocation for a single asset or group of assets.

## View retirement asset allocation

You can access the *Asset Allocation Details* dialog box by clicking the *Goals* section – *Retirement* category – *Objectives* page – *Asset Allocation* button. It shows the current portfolio and the suggested asset mix based on the questionnaire results. Clicking the *Questionnaire* button allows you to modify the questionnaire for the retirement goal, and then compare the clients' current portfolio to the suggested asset mix.

The fields under *Override Profile* allow you to override the investment profile for the *Pre-Retirement* and *Retirement* periods.

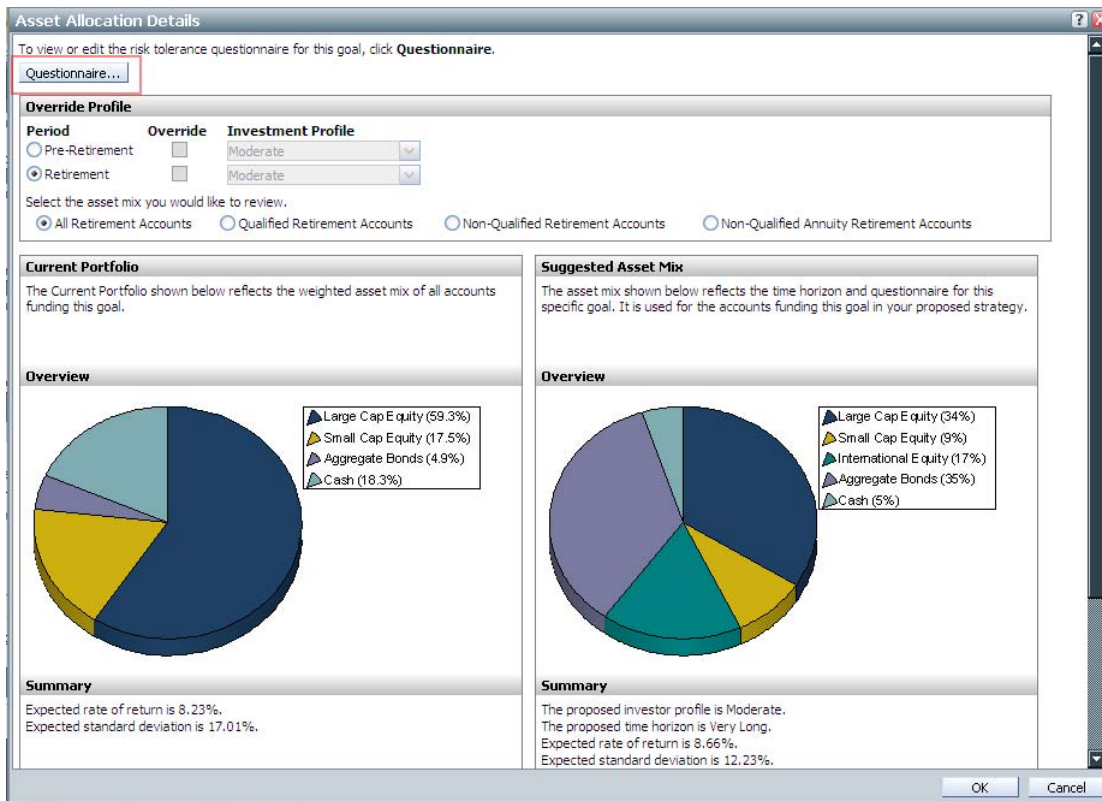


Figure 14: Goals section – Retirement category – Objectives page – Asset Allocation button (Level 3 Plan) – Asset Allocation Details dialog box

## Reallocate assets

To compare the effects of asset reallocation on the clients' plan, go to the **Goals** section – **Retirement** category – **Scenarios** page – **Objectives** tab. By default the *Current Plan* scenario is displayed on the left side and the *Recommended* scenario is displayed on the right side.

The *Recommended* scenario represents the clients' current plan with the reallocation to include the suggested asset mix. You can modify the *Return Rate* or the *Investment Profile*, as needed, in the *Recommended scenario* and the *Goal Coverage* updates accordingly.

The screenshot shows the 'Retirement' section with the 'Objectives' tab selected. It compares two scenarios: 'Current Plan' and 'Recommended'. The 'Recommended' scenario has a higher return rate (11.09% vs 8.43%) and a more aggressive investment profile (Moderate vs Current Asset Mix). The 'Goal Coverage' for the 'Recommended' scenario is 100%, while the 'Current Plan' is at 74%.

Scenario	Current Plan	Recommended
Scenario Name	Current Plan	Recommended
Nick's Retirement Age	62	62 +/- 0 = 62
Lisa's Retirement Age	62	62 +/- 0 = 62
Life Expectancy	Nick: 90, Lisa: 90	Nick: 90, Lisa: 90
Inflation Rate for Plan	3.00%	3.00%
Investment Objective	Pre-retirement: Current Asset Mix (8.23%); Retirement: Current Asset Mix (8.43%)	Pre-retirement: Moderate (11.09%); Retirement: Moderate (11.09%)
Annual Retirement Expenses	Fixed: 100%, Discretionary: 100%	Fixed: 100%, Discretionary: 100%
Goal Coverage	74%	100%
Other Goal Coverage	Education: Kevin's Education (52%); Emergency Fund: Emergency Fund (0%); Estate Planning: Estate Planning	Education: Kevin's Education (75%); Emergency Fund: Emergency Fund (0%); Estate Planning: Estate Planning

Figure 15: Goals section – Retirement category – Scenarios page – Objectives tab

**Note:** It might be a good idea to use different profiles or asset mixes for different asset types, since asset mixes generate returns that are taxed differently.

## Exercises

The exercises have been designed specifically for this module and assume that you are working with the original data in the *Brown Asset Allocation* analysis. Before starting the exercises, duplicate the **Brown Asset Allocation** analysis, rename the duplicate with a meaningful name (e.g., *Asset Allocation Assessment training*), and then use it to complete the following exercises.

**Hint:** All copies of plans are managed in the *Plan Management* section – *Plan List* category.

### Exercise 1: Use the Asset Allocation analysis

To find the answers, see “Answers to asset allocation exercises” on page 19.

1. What is the purpose of the Asset Allocation analysis?
  - a) Reallocate assets contained within a plan to a more aggressive mix
  - b) Create an Asset Allocation analysis to review the clients’ current asset allocation, establish their risk tolerance, create a proposed allocation, compare the clients’ current allocation to the proposed allocation, and then view the results
  - c) Create custom asset classes and investor profiles
2. When using the detailed account entry mode in the Asset Allocation analysis on the *Accounts* page, what can you do that you could not do using the simple account entry mode?

**Hint:** Click **Detailed Accounts** to see what is different.

- a) Have access to more asset types
  - b) Classify your assets
  - c) Add multiple holdings to accounts
3. If you click *Detailed Accounts* on the *Accounts* page or *Detailed Asset Allocation* on the *Profile* page, what are you no longer able to do?

**Hint:** Try clicking either button, and then read the message that appears.

- a) Promote to a Level 1 Plan
- b) Promote to a Level 2 Plan
- c) Promote to a Level 3 Plan

4. The *Asset Allocation* category – *Questionnaire* page allows you to establish a suggested asset mix based on your clients' risk tolerance. Is this statement true or false?
  - a) True
  - b) False

### Exercise 2: Interpret the Asset Allocation client report

To find the answers, see "Answers to asset allocation exercises" on page 19.

1. The *Asset Allocation* client report is available in an Asset Allocation analysis, as well as in Level 1, Level 2, and Level 3 Plans. Is this statement true or false?
  - a) True
  - b) False
2. The *Asset Allocation for Entire Portfolio* section of the client report looks at the current asset mix and the suggested asset mix side by side, and displays the changes needed in the current mix to model the suggested asset mix. Is this statement true or false?
  - a) True
  - b) False
3. The *Efficient Frontier* graph displays the clients' current asset mix below the efficient frontier line. What does this mean?
  - a) The rate of return is much too high
  - b) The current asset mix is perfect for the clients' risk tolerance
  - c) The clients' returns are low for the amount of risk, or the return is suitable but the level of risk is too high

### Exercise 3: Reallocate assets in a plan

To find the answers, see “Answers to asset allocation exercises” on page 19.

In the following questions, you will learn to reallocate assets in a Level 3 Plan. Before starting this last exercise, duplicate the **Brown Base Details** plan, rename the duplicate with a meaningful name (e.g., *Asset Allocation training*), and then use it to complete the following exercise.

**Hint:** All copies of plans are managed in the *Plan Management* section – *Plan List* category.

1. In the *Goals* section – *Retirement* category – *Objectives* page – *Asset Allocation Details* dialog box, how many account types can you reallocate?
  - a) 4
  - b) 3
  - c) 2
  - d) 1
2. *Pre-Retirement* (based on the *Plan Analysis Date*) and *Retirement* are the only two time periods for which you can have NaviPlan automatically reallocate assets. Is this statement true or false?
  - a) True
  - b) False
3. When reallocating assets, NaviPlan Standard will calculate the taxes due as a result of the reallocation. Is this statement true or false?
  - a) True
  - b) False
4. Review the *Goal Coverage* success rate on the *Goals* section – *Retirement* category – *Scenarios* page, and then reallocate assets to try to improve the success rate of the goal.

## Conclusion

This module has enabled you to

- Use the Asset Allocation analysis
- Interpret the *Asset Allocation* client report
- Reallocate assets in a plan

## Answers to asset allocation exercises

### Exercise 1: Use the Asset Allocation analysis

1. b) The purpose of the Asset Allocation analysis is to review the clients' current asset allocation, establish their risk tolerance, create a proposed allocation, compare the clients' current allocation to the proposed allocation, and then view the results.
2. c) Add multiple holdings to accounts – When using the detailed accounts entry mode in the Asset Allocation analysis on the *Accounts* page, you can add multiple holdings to accounts.
3. a) Promote to a Level 1 Plan – If you click *Detailed Accounts* on the *Accounts* page or *Detailed Asset Allocation* on the *Profile* page, you can no longer promote the Asset Allocation analysis to a Level 1 Plan.
4. a) True – The *Asset Allocation* category – *Questionnaire* page allows you to establish a suggested asset mix based on your clients' risk tolerance.

### Exercise 2: Interpret the Asset Allocation client report

1. a) True – The *Asset Allocation* client report is available in an Asset Allocation analysis, as well as in Level 1, Level 2, and Level 3 Plans.
2. a) True – The *Asset Allocation for Entire Portfolio* section of the client report looks at the current asset mix and the suggested asset mix side by side, and displays the changes needed in the current mix to model the suggested asset mix.
3. c) The clients' returns are low for the amount of risk, or the return is suitable but the level of risk is too high – When the *Efficient Frontier* graph displays the clients' current asset mix below the efficient frontier line, it means that the clients' returns are low for the amount of risk, or the return is suitable but the level of risk is too high.

### Exercise 3: Reallocate assets in a plan

1. b) 3 – In the *Goals* section – *Retirement* category – *Objectives* page – *Asset Allocation Details* dialog box, you can reallocate three account types.
2. a) True – *Pre-Retirement* (based on the *Plan Analysis Date*) and *Retirement* are the only two time periods for which you can have NaviPlan automatically reallocate assets.
3. b) False – When reallocating assets, NaviPlan Standard will **not** calculate the taxes due as a result of the reallocation.

