



February 10, 2020

Harvesting Strategy

3 Investment Rules of Thumb Updated for Today's Markets

Investing and the markets have evolved dramatically over the years. Humans no longer crowd the trading exchanges, waving papers and yelling orders. Indexing, barely in existence 40 years ago, now [has more AUM than actively managed funds](#). With the new dominance of indexing and [the growing awareness of the value of Tax Benefit Capture \(TBC\)](#), some old Wall Street rules of thumb may sorely need a revisit. Here are three:

1. *Alpha is shrinking and/or getting harder to find.* If you're reading this article (from an indexing focused asset manager), you are almost certainly familiar with the common refrain that alpha is increasingly hard to find – i.e. competition for market inefficiencies is as fierce as ever. Relatedly, investor money is flowing to “cheap beta”, i.e. low-cost passive strategies that seemingly ignore opportunities for generating alpha.

In our TBC world, however, tax alpha can be abundant. The same forces, such as ever-improving portfolio management and trading technology, and availability of low-cost beta, may be enabling *more* alpha, perhaps just not in the form investors are familiar with. We would argue that, more prevalent than ever, are structural forms of alpha such as reductions in fees and taxes. Unlike traditional alpha opportunities (which are uncertain and require continuously seeking out new market mis-pricings) reducing fees and tax costs can be more consistently applied with proper strategic planning and a disciplined process.

2. *Turnover is bad.*¹ In the old, alpha-seeking world of picking stocks or mutual funds that in turn pick stocks, turnover was a rough proxy for some of the transaction related costs you might pay when chasing traditional alpha. Higher turnover would typically be associated with higher trading costs and tax inefficiency. Less turnover seemed preferable, all things being equal.

In our TBC world, however, turnover can be an opportunity to capture tax benefits. With the advent of zero commissions and efficiently traded ETF's, transaction costs have been on the decline. This allows for an increase in trading and turnover for more tax benefit opportunities to be captured.

3. *Never sell in a down market* (or its cousin: Buy Low, Sell High). It's often said that investors may be slower to adopt “Tax Loss Harvesting” [simply because of the word “loss”](#). Investors do not want to lose money, they want to make it.

In our TBC world, however, a loss can be a gain. Losses are recognized as an inevitable component of investing. So, how do we make the most of them? Harvest the losses so as to capture tax benefits. This may offset gains realized elsewhere in portfolios, such as from mutual funds, hedge funds, private equity or from portfolio rebalancing.

¹ Referring to the measure of the total amount of exposure traded as a % of a portfolio over a period of time

Thanks to indexing's rise, improvements in technology, and lower trading costs among other factors, [Tax Benefit Capture \(TBC\) is gaining in prominence and sophistication](#). What used to be [once-a-year *ad hoc* activity](#) is evolving into a streamlined, fully integrated, optimized strategy. Advisors and investors may want to revisit their assumptions and [consider incorporating tax alpha strategies](#) into their portfolios.

Solomon G. Teller, CFA
Chief Investment Strategist
Green Harvest Asset Management

Market Data Summary for week of February 3 – February 7, 2020:

	Sectors/Regions with GHAM Tax Benefit Capture	Total Return (%)	Weekly Max Drawdown	
Market Exposure			(%)	Day of Low
S&P500		3.3%	-0.7%	Friday
Materials	X	4.3%	-1.8%	Friday
Energy		1.0%	-2.2%	Friday
Financials		3.2%	-0.9%	Friday
Industrials		3.1%	-1.0%	Wednesday
Consumer Staples		1.7%	-0.6%	Wednesday
Utilities		-0.6%	-1.4%	Wednesday
Health Care		3.9%	-1.4%	Wednesday
Real Estate		1.8%	-1.1%	Tuesday
Info Tech		4.6%	-1.3%	Monday
Consumer Discretionary		2.4%	-1.1%	Friday
Communication Services		3.6%	-1.4%	Tuesday
MSCI ACWI Ex-US		2.4%	-1.1%	Friday
Asia Ex-Japan		3.5%	-1.3%	Friday
Japan		3.0%	-1.1%	Friday
Australia		2.1%	-0.9%	Friday
Switzerland		0.0%	-1.5%	Friday
EuroZone		3.1%	-0.8%	Friday
United Kingdom		0.1%	-1.4%	Friday
Lat America		1.3%	-2.5%	Friday
Canada		1.8%	-0.5%	Friday
Areas with Tax Benefit Captures (TBCs) indicates where individual tax-loss harvest trades were executed in each market exposure across all eligible accounts for period specified.				
Max Drawdown calculated as max decline from interim peak to Intra-Day Low.				
Market Data Source: Bloomberg				
Market statistics calculated using representative ETFs.				



Disclaimers:

Performance quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate, so you may have a gain or loss when the portfolio is liquidated. Current performance may be higher or lower than that quoted. Performance of an index is not illustrative of any particular investment. It is not possible to invest directly in an index.

GHAM does not provide tax advice. Although GHAM does not employ a Certified Public Accountant on its staff, we have, and continue to work with outside accounting firms and outside tax counsel that provide ongoing guidance and updates on all relevant tax law. Federal, state and local tax laws are subject to change. GHAM is not responsible for providing clients updates on any changes in tax laws, rules or statutes.

Reasons to harvest capital losses, sources of capital gains and the suggestion that mutual funds distribute capital gains are for example purposes only and not meant to be tax, estate planning or investment advice in any form or for any specific client.

All performance and estimates of strategy performance, after tax alpha, after tax alpha opportunities and other performance figures are derived from data provided from multiple third-party sources. All estimates were created with the benefit of hindsight and may not be achieved in a live account. The data received by GHAM is unaudited and its reliability and accuracy is not guaranteed.

The availability of tax alpha is highly dependent upon the initial date and time of investment as well as market direction and security volatility during the investment period. Tax loss harvesting outcomes may vary greatly for clients who invest on different days, weeks, months and all other time periods.

All estimates of past returns of broad, narrow, sector, country, regional or other indices do not include the impact of advisor fees, unless specifically indicated. Past performance and volatility figures should not be relied upon as an indicator of future performance or volatility.

This material is not intended to be relied upon as legal, investment or tax advice in any form or for any specific client. The information provided does not take into account the specific objectives, financial situation or particular needs of any specific person. All investments carry a certain degree of risk, and there is no assurance that an investment will perform as expected over any period of time.

As a convenience to our readers, this document may contain links to information created and maintained by third party sites. Please note that we do not endorse any linked sites or their content, and we are not responsible for the accuracy, timeliness or even the continued availability or existence of this outside information. While we endeavor to provide links only to those sites that are reputable and safe, we cannot be held responsible for the information, products or services obtained from such other sites and will not be liable for any damages arising from your access to such sites.