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Why Liquidity Matters: A Financial Planning and Investment Discussion for Plastic Surgeons

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Summary: Plastic surgeons should understand the importance of maintaining liquidity as part of a robust household financial planning and investment strategy. Although investors rightly focus on achieving solid long-term returns, our experience suggests that many plastic surgeons often pay too little attention to liquidity management in their outlook, and some may experience stress as a result. This article discusses why liquidity management matters both in terms of each surgeon's unique career and in the context of today's dynamic investment opportunities and risks. We also discuss how best to understand the trade-offs and costs associated with household debt. Finally, we present simple self-diagnostic questions to help surgeons assess whether their current financial planning addresses key liquidity risks. This article belongs to a series that introduces relevant wealth and investment subjects for practicing plastic surgeons, students in plastic surgery, and support function professionals. This discussion is not meant to be exhaustive nor constitutes investment advice regarding any asset class, strategy, or examples cited herein. *(Plast Reconstr Surg Glob Open 2024; 12:e5690; doi: 10.1097/GOX.0000000000005690; Published online 21 March 2024.)*

INTRODUCTION

A full understanding of the importance of liquidity related to investments and financial planning can help plastic surgeons cope with risks and better manage their careers in a variety of employment settings. Our view is that surgeons, like other individual investors, should maintain an appropriate percentage of net worth in liquid assets outside retirement plans, financial products, and insurance contracts, and in addition to other illiquid asset obligations. Maintaining sufficient liquidity is not only important during early career stages but also in mid- and late-career stages. Adequate liquidity becomes critical during life moments involving major decisions such as house purchases, job transitions, and salient family events. Higher liquidity provides greater optionality to manage financial variabilities, particularly if a life "shock" occurs during a period of higher overall economic and market stress. High salary incomes, broadly characteristic of the plastic surgery profession, do not necessarily address these key liquidity risks or reduce the importance of incorporating a liquidity lens in planning. Our experience is that this specific risk can be a blind spot for many in their planning outlook, in part because of a false assumption that high absolute income equates to good liquidity planning.

Solid liquidity planning is also more than just maintaining an "emergency fund." Holistic planning is important to clearly distinguish between building net worth and maintaining enough liquidity to pursue career changes, such as joining a private practice or controlling one's specific work-life balance through a host of dynamic economic and personal conditions.

WHAT ARE LIQUID ASSETS?

Addressing liquidity planning begins with a clear definitional understanding of liquidity as applied to underlying investment assets, common investment vehicles such as retirement accounts, and commercially available financial products such as annuities and life insurance contracts.

Cash, as a medium of exchange, or legal tender money, is the most liquid asset. An asset is also considered liquid if there is a functioning market in which buyers and sellers transact daily during market hours.

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Investments in publicly traded securities, mutual funds, exchange traded funds, and certain market-traded commodity assets such as gold and silver are all examples of liquid assets. Real estate, private businesses, and private equity funds are examples of illiquid investment. Although illiquid assets have willing buyers or sellers, transactions can require more time and involve much higher transaction costs, such as brokerage or auction fees. Illiquid investments can also involve strained or frozen transaction environments for extended periods and involve sellers taking steep discounts to achieve market-clearing (Fig. 1).

LIQUIDITY CONSIDERATIONS ON ACCOUNT TYPES AND FINANCIAL PRODUCTS

Although understanding the liquidity profile of underlying assets is key, sound liquidity management should also consider the constraints imposed by investment account types and common financial products.

RETIREMENT ACCOUNTS

Although retirement accounts typically hold liquid assets, retirement accounts, such as 401K plans, individual retirement accounts, and 403(b) plans, are not designed to address an individual's preretirement liquidity needs. According to internal revenue service (IRS) rules and with limited exception, individuals cannot access these funds penalty-free before a beneficiary reaches the age of 59 ½.[1] Tax benefits accrue because these vehicles are designed to serve household retirement needs later in life with stiff IRS penalties to deter accessing such accounts outside intended purposes, such as a 10% withdrawal penalty.

Takeaways

Question: How should plastic surgeons manage liquidity as part of their financial planning needs at each stage of their career?

Findings: Surgeons should understand the key aspects of liquidity plan, including underlying investment assets and commonly used financial products. Surgeons should also understand how debt plays a role in liquidity management at each stage of their career progression. Surgeons should understand risks and warning signs related to imbalances in their planning approaches, and take remediation action as necessary

Meaning: Liquidity planning is a key part of a robust financial plan and should be part of a robust approach to wealth and investment management.

WHOLE LIFE INSURANCE CONTRACTS AND ANNUITIES

Similarly, whole life insurance contracts typically involve committing capital up front to purchase life insurance benefits and build future surrender values associated with

Asset type	Liquidity rank
Cash, Bank deposits	Medium of exchange
Publicly traded securities, ETFs, traded commodities	Intraday liquidity
Mutual funds	Daily liquidity
Physical gold	Daily liquidity depending on physical delivery
Certificate of deposits	3 - to 12-month terms
Residential properties	Illiquid
Private business investments	Illiquid
Venture capital/Private equity	Illiquid

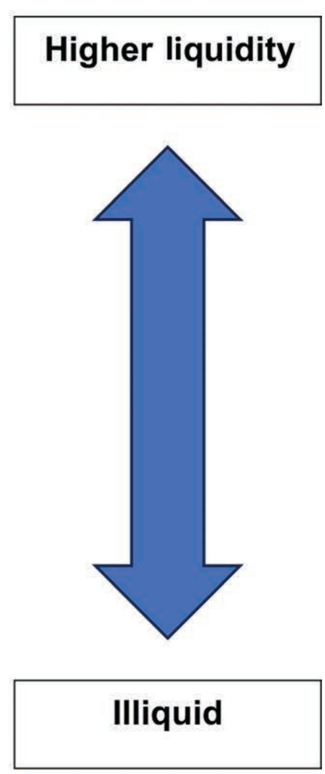

Fig. 1. Overview of asset-type liquidity. ETFs, exchange traded funds.

the contract. A whole life insurance contract can span multiple years and even decades, with specific age and other contract limits on withdrawals. Similarly, annuities typically require an initial capital outlay, with future annuity payments realized much later. Such products have the potential to reduce liquidity, and surgeons should precisely understand whether these trade-offs are acceptable. As an alternative, for example, term life insurance involves ongoing payments, but is not bundled with a savings component, and so may be more suitable depending on circumstances.

HEDGE FUNDS AND PRIVATE EQUITY

Individual investors can also participate in hedge funds that impose "lock-up" periods on redemptions. A lock-up period is a specified time, such as a year, during which investors cannot withdraw their capital. Likewise, a typical private equity or venture capital limited partnership normally has a commitment period of over 1–3 years, during which an investor is required to make contributions, followed by an investment realization phase with associated realized gains that can be as long as 5 years or more. A direct early-stage investment in venture capital is also illiquid, with investors monetizing investments via exits only after years of holding illiquid positions.

WHY LIQUIDITY MATTERS AS A RISK CONTROL

Maintaining liquid assets is a key risk control factor for two critical reasons, both of which relate to the inherent nature of uncertainty. First, liquid assets provide higher optionality regarding changing external market conditions, with daily price discovery being a way for investors to actively adjust to evolving economic conditions. Second, liquidity is important for dealing with changes in one's financial planning due to unexpected disruptions. Although good planning involves setting up long-term future goals and targets, strong liquidity management helps adjust to negative shocks, "course correct" during periods of stress, and potentially capture better uses of capital as impactful new circumstances emerge.

DEALING WITH UNCERTAIN MARKETS EXTERNAL ENVIRONMENT

Forecasting even major economic trends with high degrees of precision in today's complex, globalized financial markets is fraught with peril. Typically, a longer predictive time horizon is associated with a less accurate generalized forecast. One salient illustration of this is that, in 2019, before the onset of COVID-19 in early 2020, no major bank or government agency predicted a global pandemic; however, the pandemic reshaped multiple aspects of economic policy, market conditions, and daily life. Similarly, other disruptive events, such as wars, political regime changes, and natural disasters, are often modeled under risk scenarios but are not precisely predictable as future risks. The role of active investors and their financial advisors is to constantly adapt to emerging data, run stress tests on potential future conditions, and measure risk return trade-offs as new data emerge. Capital markets reflect the price discovery of buyers and sellers continuously. Surgeons should consider active investment management as a *continuous process* rather than a static set of decision points and assess whether working with qualified advisers can help navigate these issues or if they are comfortable adjusting their own portfolios in a self-directed manner.

ILLIQUIDITY PREMIUM

In this context, a key risk consideration for illiquid investments is that they potentially restrict the ability of any investor to quickly adapt to changing external conditions. Transaction costs for illiquid assets can also increase significantly in stressed environments. Modern financial theory recognizes this risk. For example, the term "illiquidity premium" is the incremental return that must compensate an investor for owning a less liquid asset. As investors assume higher liquidity risk, they should demand higher returns, although precisely measuring this premium is a controversial subject in this field.[2]

MANAGING YOUR OWN CAREER AND PLANNING

On an aggregate level, according to the US Federal Reserve, US households hold 67% of total assets in financial assets, including bank deposits, taxable and retirement accounts, and the remaining 33% in nonfinancial assets, including primary and secondary properties. We caveat that a plastic surgeon's specific liquidity plan must account for various constraints and considerations, such as age, household budget, and career stage (Fig. 2).[3]

LIQUIDITY MANAGEMENT SPECIFICALLY FOR PLASTIC SURGEONS

Our view is that surgeons, like other individual investors, should maintain an appropriate percentage of net worth in liquid assets outside retirement plans, financial products, and insurance contracts. These liquid investments are in addition to illiquid assets such as property,

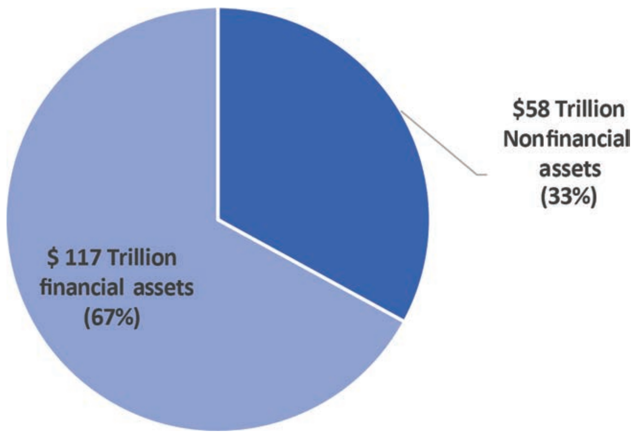

Fig. 2. Breakdown of aggregate household assets in the United States.

business ventures, equity in practices, and private equity. Our recommendation goes beyond just establishing an emergency fund and is focused on properly bucketing a fuller spectrum of liquid assets to achieve solid long-term investment outcomes.

Although our conceptual recommendation applies in principle to plastic surgeons in a variety of employment settings, we would highlight some common risk factors based on specific employment setting as described in Figure 3. For example, surgeons in private practice should recognize that private practice interests may be extremely valuable long-term assets, but these interests are typically illiquid. We also caution that other personal factors, such as family-specific events, can meaningfully impact individual circumstances beyond these general employment categories (Fig. 3).

DEBT AND LIQUIDITY MANAGEMENT

Why Use Debt at All?

Effective management of household debt is a key aspect of sound liquidity planning. Securing a loan is a common financial activity for most plastic surgeons, with high educational debt often required to enter the profession. Most surgeons typically leave residency with meaningful obligations and face major asset purchase decisions, such as property and auto purchases, whereas student debt is still outstanding. If properly structured, debt can support household liquidity at a reasonable cost. Borrowers receive financial resources and pay lenders an interest rate as the cost of this service. However, debt can become a source of risk if loan terms and amounts exceed a manageable servicing quantum. Failure to service debt negatively impacts credit profiles and introduces many other adverse impacts. Higher interest costs associated with floating-rate debt can also stress planning goals such as credit cards, and some floating-rate mortgages also adjust to higher market rates, a risk many households are experiencing in today's inflationary environment. Fixed-rate debt, such as most student debt and fixed-rate mortgages, are typically more favorable options from a liquidity-planning perspective, especially as repayment terms are usually more than 10 years. According to the Educational Initiative, for example, an average US student takes 20 years to pay off student debt.[4] For plastic surgeons, there are public service loan forgiveness programs, but the majority of plastic surgeons may not have access to these programs given that most surgeons work within a for-profit model. Thus, most need a strategy for direct loan repayment over time.

DOES SOUND LIQUIDITY MANAGEMENT SUPPORT ACHIEVING LONG-TERM RETURNS?

Maintaining appropriate liquidity does not need to conflict with achieving long-term wealth-building goals as measured by absolute return targets, but rather is a complementary approach. Consistent investing according to a

Surgeon Employment Categories	Common Liquidity Management Risks
Private Practice—Partnership Ownership	Obligations to support/buy—in to more illiquid partnership interests as a percentage of overall net worth
Employment—For profit healthcare providers	Potential risks related to external economic conditions impacting a for—profit health care providers such as unexpected layoffs, income inelasticity, pricing changes, and business combinations
Employment—Public healthcare providers	Changes in public sector policies and employment conditions (similar to private enterprises but generally less variable)
Residency/Early—stage physicians	Lower income, higher debt obligations, need to establish recurring income patterns, and lower overall net worth
Military employed physicians	Lower income, unforeseen conflict—related stresses, family commitments related to deployments
Academia	Untenured teaching roles that may have limited terms and lower paying roles

Fig. 3. Common risk factors by plastic surgeon employment categories.

long-term time horizon should not be conflated with the parallel need to adapt to evolving circumstances, both positive and negative. According to SIFMA, as of the year-end of 2022, the US households held 74% of their liquid assets in various marketable securities outside bank deposits and certificates of deposits (Fig. 4).[5]

Within this breakdown, equities have the largest percentage holding and the highest 30-year average returns. Capital market returns from publicly traded equity, as measured by the S&P500 from 1992 to 2023 were 9.6%.[6] In comparison, the US House Price Index YoY in the United States averaged 4.58% from 1992 to 2023.[7] This aggregate comparison, while subject to many caveats, suggests that, on a historical basis, liquid equities offer better long-run returns than illiquid property assets. One illustrative example of a widely held single-name equity asset with daily liquidity is Berkshire Hathaway, with 10-year returns of approximately 10% as of October 19, 2023.[8] Thus, an investor in Berkshire Hathaway enjoyed both long-term capital appreciation and the optionality to transact daily within their planning parameters at low transaction costs. Other liquid assets such as cash, bonds, and mutual funds have various return and risk profiles to consider.

AVOIDING KEY SELF-INFLICTED MISTAKES

In addition to earning returns on liquid assets, plastic surgeons should also avoid self-inflicted mistakes regarding their core household budgeting and planning choices. Controlling one's cost of living appropriate for one's career stage is a key discipline. Likewise, avoiding mistakes such as a large property purchase that constrains minimum threshold levels of free liquidity can help maintain a healthy profile. Surgeons should also consider whether their own circumstances warrant seeking qualified and trusted counsel from financing planning professionals as they navigate these constantly evolving challenges.

CONDUCT A SELF-DIAGNOSTIC

We compiled initial questions about liquidity to help plastic surgeons at any stage of their journey to assess their own profiles. Affirmative answers to one or more of the following questions can be warning signs, indicating the need to review liquidity risk more closely. The initial questions were only general warning signs. For additional details, we recommend consulting with trusted and qualified investment or planning professionals.

KEY QUESTIONS

- Are more than 60% of your total household assets invested in illiquid instruments such as fixed property, including your primary residence, business partnerships, and other illiquid asset types?
- Are your investment accounts more than 60% exclusively in retirement accounts, financial products, or insurance contracts versus in accounts that you can readily access without penalty before retirement?
- Are your liquid assets insufficient to cover at least 12 months of household expenses, assuming stressed parameters?
- Are your liquid assets insufficient to cover significant events such as a major career change, forced relocation, or the overall impact of a health-related event that may not be fully insured?

CONCLUSIONS

Dynamic economic conditions and the evolving state of the plastic surgery industry demand that plastic surgeons

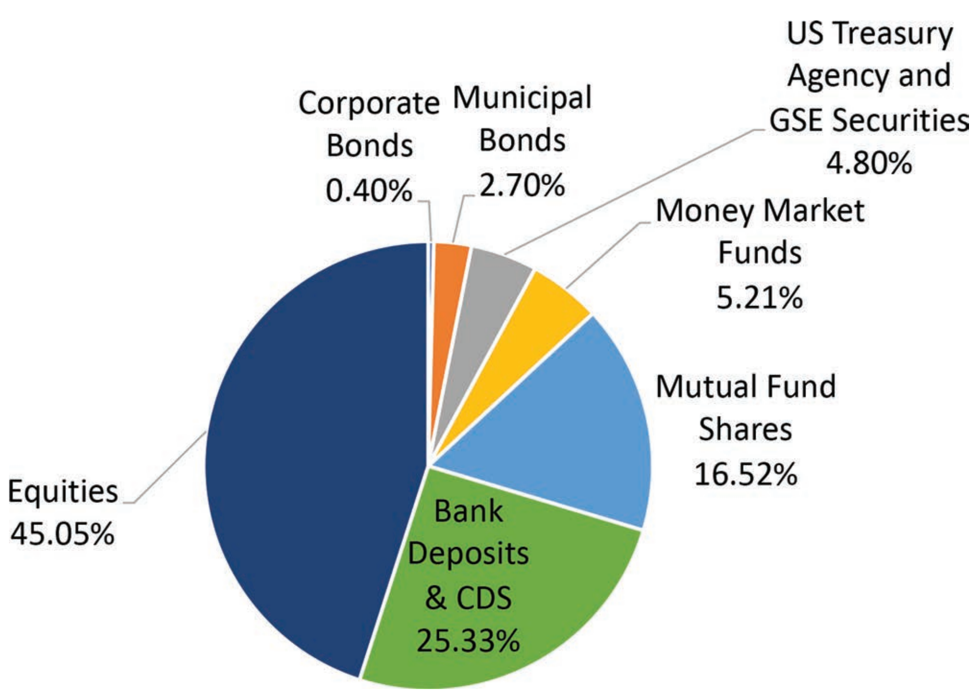

Fig. 4. US household liquid financial assets as of year-end 2022. CDs, certificates of deposits.

deepen their understanding of how liquidity management can help support sound investing and financial planning. The profession's overall high-income profile and perceived job stability is no substitute for managing liquidity in a robust manner. (**See appendix, Supplemental Digital Content 1** which displays practical tips on liquidity management for early-stage plastic surgeons, **http://links.lww.com/PRSGO/D125**.)

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DISCLOSURE

The authors have no financial interest to declare in relation to the content of this article.

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