

INSIDE INFORMATION

The newsletter for serious financial advisors. (www.bobveres.com)

COMMUNICATING THE INVISIBLE

Our latest contest illustrates that many advisors can do a MUCH better job of helping consumers buy planning services.

by Bob Veres

Before we get too far into this publication, I want to congratulate the winners of our marketing materials contest: David Virt, Poteet, Virt & Associates in Indianapolis, and Jeff Davis, Falcon Financial Management, in Gainesville, FL. Each wins a complimentary registration at the FPA Retreat in Colorado Springs, May 13-16 of this year--along, of course, with the immense international publicity that comes from finishing at the top of such a prestigious event.

In all, we evaluated 30 entrants. The good news is that our judge, Brigid O'Connor--former PR director of the ICFP and FPA, now a communications strategist (and one of the more highly recommended speakers in our recent survey)--was able to evaluate how different financial planners are reaching out to prospective buyers of your services. As I had hoped, her evaluation, and our discussion of the materials, led to some groundbreaking insights into the way financial planners are--and could be--communicating their value to the investing public.

In fact, it is possible that we have started a dialogue which will lead to a transformation in the way planning services are marketed to people who may not realize that they need them.

Let's start with our winners, and look at what O'Connor found to be their strongest features. Falcon's primary brochure is surprisingly low-tech--a soft binder with a clear plastic cover which (I checked) you can buy at a local drug store for less than two dollars. Inside, the pages look like they might have been produced

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Client Services: *Introducing a new way to help clients change their lives for the better. ..*page 10

The Profession: *If you turn the Hurley Report upside down, you come away with some interesting insights.*page 12

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EARLY WARNING

- The FPA Retreat, May 13-16 in Colorado Springs, is about to fill up, with 200 of the roughly 250 slots already booked. So if you're interested in attending, get your name in before it's too late. You can find the registration information and schedule at: <http://www.fpanet.org/member/meetings/conferences/Retreat/index.cfm>.

It is interesting that the winners

of the marketing brochure contest will be granted registrations, because the expanded conference agenda will be, directly and indirectly, about what the financial planning profession offers to consumers, and how to communicate the value of what you do to the world at large.

I'll also be at the NAPFA national conference in Toronto April 21-25; http://www.napfa.org/index_full.html.

The Insider

How do you plan for estate taxes in this chaotic environment? It looks like those who said the estate tax repeal would not be permanent are correct. According to members of two different tax committees in Congress, there is slow bipartisan support building for a \$7 million unified exemption for couples (\$2.3 million individual), and a gradual lowering of the top rate from 50% to whatever ordinary income tax rates are at the time--or, perhaps (an alternative proposal) all the way down to capital gains rates.

Meanwhile, Forrester Research has finished its analysis of the Schwab Personal Choice initiative, and found that the company's credibility--long an issue with financial advisors--is eroding among individual consumers. In some areas, it seems to be well behind some larger brokerage firms that the company is always comparing its superior ethics with. For example? When asked whether they agree with the statement: "*My brokerage makes the rates and fees it charges crystal clear,*" only 55% of Schwab customers agreed, vs. 61% for customers of American Express Financial Advisors, 63% at A.G. Edwards and 64% at Merrill Lynch and Edward Jones. Only 56% of Schwab customers agreed with the statement: "*My brokerage always honors its promises and guarantees,*" compared with 65% of AMEX customers, 61% at Merrill, and 71% at A.G. Edwards and Edward Jones.

Communicating the Invisible

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on a color inkjet printer--but they are attractive enough and well-enough designed that O'Connor thinks the overall look and feel is not cheap.

Her first screen for each of the brochures is what she called the "open test," meaning, essentially, would a financial consumer have any reason to open the cover and look inside. Falcon passed this test with an intriguing cover line that made her want to find out more: "The Integrated Wealth Management Process," and subhead: "A holistic evolutionary strategic planning program, based on a conversation about your financial affairs for the rest of your life."

"Yes, it's a little wordy," says O'Connor. "But I wanted to find out what the process was, and how it might affect the rest of my life." She contrasts this with some of the entrants, who failed the "open test" by simply putting the name of the firm on the cover--or, in one case, nothing but the firm's logo.

My guess is that many readers of this publication are realizing that they, or their firm, are giving out company brochures with either the name of the company or a logo on the cover. What, exactly, is wrong with that?

The answer, in O'Connor's view, depends on what's going on in the mind of the person who receives this brochure. "If this is a really hot prospect, meaning that they know they want to work with a financial planner, and they think you might be the person they want to work with, then yes, they'll open anything you send them," she says. But she believes that most financial consumers haven't decided that they do, for certain, want to work with a financial planner; instead, they want to know

more about what financial planning is, how the process works, and what's in it for them. They may have asked for more information through one of the referral programs, or they may have been referred by a current client, but it's a very long leap of faith to think that means they're ready to buy into the financial planning process.

This was one of the three important insights of the project: that you, and most other financial planners, may be mistaking a casual inquiry with a readiness to buy your services. Instead of sending out a brochure that simply offers facts about your firm, O'Connor thinks that you need to start by imagining that your audience is a person who has heard about this financial planning thing but is not yet convinced that she really wants or needs it. Instead of telling this person that you're knowledgeable or better than other planners, you need to do something fundamentally different: communicate what you will do for that person, or why that person might want to buy your services.

Falcon's cover included four pictures: a youngish happy couple walking through fields; an older couple together on the beach, a high-tech computer shot and a picture depicting a bunch of disorganized paper. The pictures, in O'Connor's view, communicated the need for financial advice and guidance when you're young; the promise of retirement; the firm's ability to master the technology tools that are part of good financial planning; and the ability to untangle the confusion of financial paperwork. In other words, they implied (but never stated) what financial planning offers to the reader of this company literature.

Open up Falcon's brochure, and

you find that the words pass O'Connor's second test: a focus on the client, rather than the advisor--what she calls CLIENT-focused, as opposed to WE-focused. "A lot of these materials that I've seen over the years are all WE, WE, WE," she says. "WE offer tax planning. WE have these credentials. WE are one of the leading firms, bla, bla, bla. As the consumer, I want the focus to be on ME, not on the planner or the planning firm. I understand that a sales piece must speak about the service provider, but I think it ought to do that within the context of 'what's in it for the client.'"

In Falcon's case, the text of the brochure outlines the procedure that the advisor and client will go through together. Notice the "you/client" focus in the steps that it describes:

"The Unique Discovery Experience. At this state, we'll review your data and identify your goals and objectives."

Inside

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"The Interactive Drafting Session. During this meeting, we will review different scenarios. Together, we will develop a clear vision of your options and develop a draft of your plan."

The various steps are trademarked, so I won't offer all of them here, but O'Connor also likes the fact that the consumer is being shown, clearly, the process that she's going to be taken through. "Financial planning is kind of a mystery to people," she says. "Some of the other brochures say, basically, we offer tax planning, and retirement planning, and estate planning--but they don't tell you what that entails very clearly. Right up-front, Falcon's materials tell you the six steps you'll go through, and that you are going to be fine at the end. To me," she adds, "it says they're going to do the work and extract the information from me. If we follow these steps, and get my financial affairs cleaned up, then this will probably be painless."

The brochure also wins points for offering the company's core values ("The client is always right." "Appreciate everyone." "Communicate effectively." etc.). And it is more effective for being what O'Connor calls 'high touch,' meaning that you have to interact with it, run your fingers through it--which is becoming an important and trendy issue in today's marketing circles. The mechanical details are not superior, but they're fine, O'Connor says. The typeface is readable and the pictures on the front cover are used inside the brochure, so there is good consistency of message and appearance.

The other winning materials, submitted by Poteet, Virt & Associates,

is very different; it's a tri-fold brochure with a metallic gold border around every page, with a consistent picture of a bridge in the background. The front cover says (you've probably already guessed the first words) "Bridging the Gap Between Success and Significance."

"It passed my 'open test' because my first thought, as a consumer, is, hmmm; how do you do that?" says O'Connor. "I'm successful and, yes, I want to be significant. Let me open it and find out what they mean."

Inside, the focus is, once again, on THEM (clients) rather than WE (our firm):

"Financial planning is really about who you are."

"Planning for your future."

"Our mission is to help you realize your goals."

"Your financial plan should be based on what you truly want to do with your life, and who you really want to become."

There is an insert that talks about the firm, but once again, it is twisted from an ego piece to a declaration of how the firm helps the people who walk in its doors:

"Integrity: We understand the trust and confidence that you are placing in us, and we promise to live up to that through personal and professional integrity, honesty and candor."

"Objectivity: You can be assured that we will approach your financial needs and investment opportunities with objectivity, placing your best interests first."

I found it interesting that the two winners were not the most attractive brochures that O'Connor reviewed; if we had subdivided the contest and given out awards for an attractive-

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Trendspotter

Will anything really change in the fund industry?

The quick answer is: Yes, but slowly. The SEC is already requiring funds to post a summary of their 50 largest holdings on a quarterly basis (previous rules forced this disclosure twice a year)--with a 60-day lag. This may lead to more disclosure down the road, as some funds have been offering the same information monthly with no noticeable negative effects. Also: fund prospectuses must now list their expenses in dollar terms on a \$1,000 investment, and percentage terms based on a hypothetical 5% yearly return. A bill introduced in the Senate would require funds to disclose transaction costs as well--and also tell investors how, and how much, portfolio managers are paid.

On the horizon? The SEC is now looking at ending directed brokerage arrangements altogether, and new disclosure rules which would allow fund investors to see how much they pay in brokerage commissions. Further out, SEC officials are wondering whether the world would be a better place if 12(b)-1 fees were eliminated altogether, on the theory that they were originally permitted in order to help funds achieve greater economies of scale, which would lead to lower expenses passed on to fund shareholders. The evidence now is that the additional assets detract from fund performance, and there is little evidence of reduced costs due to larger portfolios.

Communicating the Invisible

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ness category, then the winners would have been the brochures that were designed, for different advisors, by Peter Montoya's organization. These included materials from Mike Harvey, in Winfield, KS that features, as a primary theme, wheat fields; Todd Washburn in Durham, NC ("Used a consistent color palette and the text was about the client, using "you" and "your" right out of the gate," says O'Connor); and David Stone ("Good tagline: Your Companion on the Financial Journey") in Pinkerton, OH.

With these and other materials, O'Connor found the eye-candy quotient high--and she thinks this is important to help consumers cut through the clutter. But while some were on target in terms of content too, others were not. And content--the actual message--is the most important thing to get right, in her view. "Sometimes advisors are taken though the process by somebody who is conversant in the visual area, but not necessarily in the other areas that are important," she says. "With some of the brochures, the story was: good logo, good pictures, good colors, no message. A lot of people think branding is the logo. A good graphic designer knows it is the logo, the font, the color palette, and the visual style. But the top professionals know it is about all that, and messaging also. It may be beautiful. But if I'm not interested in opening it, or reading through it, then ultimately it is not going to accomplish what you want it to."

Nor were the two winners the very best in terms of messaging. Perhaps the most creative--and most useful--messaging came from the

Grodman Financial Group, whose principal, Brian Grodman, works in Manchester, NH. "One heading--'A Profile of Our Successes'--is too planner-focused," she says. "But it goes on to offer several mini-case-studies that profile the firm's clients: how the firm helped the young family, the newly-retired, and other people who might have situations similar to prospective clients."

Others did a nice job of maintaining the "you/client" focus in their text. Deborah Abel, who practices in Menlo Park, CA, has a simple, probably desktop-published brochure, and the cover says, straightforwardly (and you-focusedly) "Helping people make wise decisions about their money and their lives." Inside, the subheadings are:

Your future is too important to leave to chance.

It is possible to simplify your finances.

Could you use some personal help right now?

"It is very much about the reader/prospective client, and not about her," says O'Connor. "She does have a bio on the back, and she has the list of all those services that everybody provides: cash flow analysis, investment analysis, insurance analysis. But all that stuff is on the back cover--appropriately behind the important messages that are centered on the client."

The fact that only a few of the brochures maintained this "you focus" was somewhat disturbing. This was, readers may recall, the topic of a recent column in *Investment Advisor* by Andy Gluck, whose Advisor Products firm also provides marketing services to financial planners.

Gluck found that financial planning web sites are often filled with 'WE-focused' text that may be doing more harm than good. As O'Connor was talking about this issue in discussing her finalists, she referenced the column, which suggests to her that the planning profession is still in its bare infancy in terms of understanding how to market its relatively new (historically) service. "Speaking about the client, instead of yourself, should be a foundational given," she says. "Clarifying what financial planning is, that should be in all of these."

This led to other insights which are extremely important to the planning profession--and which are literally never talked about; perhaps not even acknowledged:

1) What financial planners are utterly familiar with, the potential client or prospect is often clueless about. The brochure says that the planning firm offers retirement planning, estate planning, tax planning--as if the client already knows what they are and what kind of processes they entail. This is too big an assumption.

"If I am intelligent, I know that the goal of retirement planning is that I am supposed to have money to retire," says O'Connor. "But you have to figure that out for yourself. Nobody is saying that to me." One of the goals of every marketing piece should be to reduce, in some way, the intimidation factor; to help the client understand what they will be going through.

This leads to the other, even-more-important insight, which will be the subject of the next e-column we send out, and hopefully generate one of the most important debates of

the year.

2) Financial planners are not, ever, communicating the benefits of financial planning to their prospects. In fact (this is the really astounding part), they may not yet have ARTICULATED those benefits clearly to themselves, or have come to a profession-wide consensus on what they are.

"The most basic advice in the marketing arena," says O'Connor, "is to talk about benefits, not features." The winning materials in this contest, she said, made the leap from talking about themselves to talking about clients and the firm's features, but none of them made the leap all the way to benefits.

What ARE the benefits of working with a financial planner? When you buy hand cream, you don't see an advertisement that focuswes on the ingredients; the benefit is smoother skin. When you buy a car, the ad doesn't focus on the size of the engine or the steering system except in passing; it shows people enjoying a more pleasurable driving experience. When you hire a financial planner, what benefit is being offered?

"It's tough," says O'Connor, "because you can't guarantee a better life or a better investment return. "Peace of mind? Financial safety? I'm not sure anybody has really talked through what the tangible benefit is for somebody to work with a financial planner, and how to communicate it."

"I think you can talk about the fact that money is scary, that the lack of it or having it are both scary and complicated," O'Connor adds. "Is financial planning supposed to help me overcome those fears? To take

advantage of opportunities? To have money when I need it?"

The truth is, I don't think any of us knows exactly how to articulate this benefit--yet. It may be a moving target, different now than it was in the recent past. But if we can figure it out, then the planning profession can take a truly enormous step forward in marketing effectiveness--and, perhaps, in acceptance by the public as well.

In fact, as a byproduct of this little contest, we may have identified why, exactly, advertising has never worked in the planning profession. Until the planning profession has defined its deliverable, we probably won't be able to use traditional marketing tools with the effectiveness that is currently enjoyed by virtually every other industry and profession.

Meanwhile, my sense is that many of you could GREATLY improve the way you market yourself if you take a few minutes to recognize the insights that this little contest offered: that the person reading your brochure may not be convinced he or she needs financial planning services; that you need to demystify the planning process, that you need to direct your message to that person, rather than focusing on yourself and your own credentials and accomplishments.

If you do those small, basic things over the course of the next year, and participate in the greater dialogue about what financial planning's deliverable is, then you'll be among the few planners in the profession who are able to communicate effectively to the public--an unfair advantage that is exactly what this newsletter hopes to provide. ■

QUOTABLES

“As the name-calling escalates between commission and fee planners, each side focuses mostly on the scoundrels--rather than the professionals--on the other side.”

Mike Billingslea, Westminster, MD

“Honesty, ethics, and honor of the individual planner--these are the things that can never be trained. They are the wind that will forever make the strong stronger, and the weak topple. How many of our recent scandals would have not happened if these old fashioned values were the basis for making decisions and forming policies?”

Stephen C. Brody, Greenville, NC

“With the birth of new products like Morningstar's new asset allocation program--where they select the funds, charge a percentage of assets and pass it through the broker/dealer--the distinction between fee-only and fee-based planners is not as wide as the fee-only planners would hope, and it will get smaller.”

Stephen Hyde, Wilmington, DE

“Successful advisors see the business side as just as important as the practice side, and they are turned off by the idea that they should be on a “mission.” At the end of the day, it should be enough to offer a quality service for fair compensation, fully disclosed, and to earn a profit in so doing.”

Jim King, Walnut Creek, CA

Investing

QUADRANT MIGRATION

If Paul Gire is right, it's time to reevaluate everything we thought we knew about managing client portfolios.

by Bob Veres

A few years back, Roger Gibson offered a very simple matrix to help advisors determine what they believe about investing. The matrix was divided into four quadrants, and it looked a little bit like the chart at the top of the next page. Quadrant one--where you believe in the ability to beat the market through stock selection, and where you also believe that you (or a well-plugged-in professional) can navigate profitably between asset classes--tends to be where less sophisticated consumers reside. Quadrant two, where you believe in stock selection but not in your ability to shift profitably between asset classes, is the belief system territory where most fund managers live. Quadrant four, where you basically don't think anybody can add predictable value through either means, has been the dominant orthodoxy in the planning profession for at least the last 15 years. It is where Gibson himself resides, and his presentations (I saw him again in Charleston last month) make an excellent case for adding value in Quadrant IV by investing in non-correlated asset classes. The resultant smoothing of performance, over many years, leads to more actual dollars in the client's pocket.

The orphan stepchild of the matrix has been Quadrant III, which Lynn Hopewell, in one of his modern portfolio theory presentations, once called “the cold, dark place where market timers live.” But in the last couple of years, partially as a result of the bear market, there have been quiet discussions among advisors about taking a second look at this cold, dark quadrant. A few prominent investment theorists (Bill Jahnke, Robert Arnott) have openly suggested that we consider home-staying in this space. No, they aren't advocating market timing (however you define it). Instead, they argue that it's better to make educated forecasts about asset class returns than to default to a buy-and-hold orientation no matter what market or economic conditions prevail.

Among practicing financial planners, nobody has thought more deeply about our aversion to Quadrant III than Paul Gire, of Strategic Advisory Services in Orinda, CA. Over the past two years, he has been making presentations to planners in the San Francisco and Sacramento areas on what we've learned from the bull market, and from the bear market, and how that information might be applied to portfolio construction going forward. “I tell them, hey, I'm one of you guys, and have been man-

	Dynamic Asset allocation: Yes	Dynamic Asset allocation: No
Asset Class Selection: Yes	<p>Can you add value through stock selection? Yes. I</p> <p>Can you add value through overweighting or underweighting asset classes depending on their relative valuation? Yes.</p>	<p>Can you add value through stock selection? Yes. II</p> <p>Can you add value through overweighting or underweighting asset classes depending on their relative valuation? No.</p>
Asset Class Selection: No	<p>Can you add value through stock selection? No. III</p> <p>Can you add value through overweighting or underweighting asset classes depending on their relative valuation? Yes.</p>	<p>Can you add value through stock selection? No. IV</p> <p>Can you add value through overweighting or underweighting asset classes depending on their relative valuation? No.</p>

aging client money for more than 20 years,” he says. “And I now believe that most of what we learned in the 80s and 90s about money management--passive asset allocation--is incomplete.” He suggests that the lessons learned from the bull market--buy and hold, buy on the dips, overweight equities because they inevitably deliver the best long-term returns--are terrific strategies for periods when the bull is raging. But what happens if we enter a sustained period where stocks underperform--like, say, the 1970s in the U.S., or the 1990s in Japan?

In fact, Gire gives the buy-and-hold approach, which he calls “passive investing” (not to be confused with indexing, which he favors) a report card. It gets an A in bull market performance, an F in its attention to fundamental values, an F in its attention to investor psychology, and anywhere from a D to an F in protection against the kinds of secular bear

markets that all societies seem to experience periodically. “It has been good for the profession,” Gire admits, “but it does not give us the whole picture. It misses two primary things: valuation and human psychology.”

The two are, of course, related, nowhere more tightly than when the market enters into what Gire calls “manias.” The most recent mania, of course, led to the bursting of the tech bubble here in the U.S. Before that, there were the weird overvaluations in Japanese equities, preceded by the real estate mania, and the Nifty Fifty mania--going all the way back to the days when Dutch investors were trading expensive houses for particularly promising tulip bulbs.

In each case, the investing herd was cruelly punished, and the whole debacle was very clear in hindsight. “If you look back, you quickly see that manias are actually fairly common events,” says Gire. “We’ve had

roughly one every decade for the last four decades. And here’s the interesting thing: When we start talking about manias, we have implicitly agreed that there is some psychology in the markets, and that passive investing is not the whole story.”

So what about valuations today? Gire believes that the U.S. market has undergone some potentially treacherous shifts in its underlying dynamics. At present valuations, it is hard for people like Jahnke, Arnott and even Jeremy Siegel to see how the market as a whole is going to deliver double-digit returns over the next 10-20 years. At the same time, the S&P 500 has experienced a dramatic increase in volatility. Gire points out that there have been seven rapid swings of 20% or more over the last 24 months, compared with exactly one in the ten years from 1990 to 2000. “Basically, the evidence suggests that we’re in the early stages

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Quadrant Migration

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of another secular bear market in U.S. equities," he says. "If that assessment is correct, you'll see a lot of cyclical rallies that last about 24 months and go up 50%, and then it rolls over and declines again. If you look at the Japanese market for the last 15 years," he adds, "that could be a road map of what U.S. stocks are going to look like. Or you could look at the 1970s, which was the last secular bear market here in the U.S."

Gire is not suggesting that you put your money in a mattress and then hide there yourself for the next 20 years, although some who have attended his presentations have interpreted it as gloom and doom. Instead, he would like to see a profession-wide debate on whether advisors should be migrating from Quadrant IV to Quadrant III, and how that should be accomplished. The all-or-nothing, totally-in-or-totally out of stocks approach is not palatable or intellectually justifiable, but there are other regions within Quadrant III which are harder to ignore. Gire thinks there are opportunities in those cyclical rallies, if you can get a handle on when the investor psychology has turned (more on that in a minute). But a bigger opportunity comes if you look at the global markets and spot the next mania-in-the-making.

"Right now, I think it makes sense to look at equities in other markets that are cheap, which at this point boils down to Asia, and Japan in particular," he says. As evidence, Gire offers some contrasting graphs on the long-term trend of the U.S. and Japanese markets. On each, he draws bands that are two standard deviations above and below the long-

term trend. On one graph, the U.S. market has been bouncing around between the two bands since the late 1800s, occasionally popping outside on the top or the bottom, and always very quickly correcting back toward the center. What is interesting for today's investor is that the S&P 500 is now two standard deviations above the long-term trend, which suggests to Gire that there is a 95% probability that U.S. stocks will--sooner rather than later--move back into bear market mode.

Now for the truly interesting part. A similar graph of Japanese stocks offers exactly the opposite profile; you see the same bouncing back and forth, but at this moment, the Nikkei is trading just outside the bottom of the two-standard-deviation line. Looking at fundamentals, Gire believes that Japan currently represents an indirect way to invest in the growth of the Chinese economy--which, Gire says, is at the same place, economically, as the U.S. was in the 1800s. "Over the next 20-50 years, they are going to be creating wealth on a massive scale," he says.

Interestingly, China is also Gire's leading candidate to become the next investment mania, as other investors decide to jump onboard the economic growth train, and as more direct investment opportunities open up in the world's largest market. Over a 10-20 year period, he says, we will watch valuations move from very low to excessively high, and anybody who wants to ride that mania up to the point where the valuations look reasonable will generate attractive returns, even if the U.S. market is experiencing a long-term doldrums. After that, watch out. Gire thinks we could see the same situation that fu-

eled the tech boom: investors who are late to the game decide they want to get in on the next engine of growth at any price, and in the ensuing collapse they learn to their sorrow (and financial detriment) that price always matters.

I think it's important to stop here and distinguish what Gire is talking about from market timing. Gire is talking, first and foremost, about investing more broadly than most advisors are yet comfortable with. Instead of focusing exclusively on U.S. equities, he believes advisors should be willing to commit a significant amount of their client assets to non-traditional assets that are priced more attractively than the narrow band of U.S. stock and bond investments that most current advisor portfolios are confined to. Today, you can find those valuations in commodities--which are already seeing prices driven up by the Asian boom--and Japanese and (when they become more widely available) Chinese equities. Gire himself still holds U.S. stocks and he believes in the value of diversification--which Gibson has done such a good job of demonstrating.

And secondly, Gire is talking about identifying investment opportunities based on current prices and broad forecasts of future economic trends--which is similar to what Jahnke has advocated. That means you never just buy and hold anything; you are constantly evaluating every investment based on its current valuations. When somebody offers you a house for a tulip bulb, then it's time to liquidate your position and reposition your portfolio into assets that are less dearly priced and have more economic growth potential.

There may be another historical

trend going on here as well. If you look at the history of the planning profession, you discover that advisors are usually one or two steps ahead of the consumer in terms of their knowledge of portfolio design and market dynamics. But it isn't a constant lead; the process goes on in fits and starts: the consumer catches up to the idea of diversification and the investment pyramid, and then advisors learn modern portfolio theory and move ahead. We are now at another of those moments when the consumer has caught up, when it is possible to find well-diversified portfolios on the efficient frontier, implemented with passive funds, on a variety of consumer web sites. If history is any guide, the profession is about to learn something important that consumers will have to spend six years catching up on.

For Gire, learning how to incorporate valuations, investor psychology and top-down macro-forecasts is a work-in-progress. His own client portfolios offer a study in what might be described as fitful success: up 18% in 2000, up 4% in 2001 and 2002, down 7% last year when the market was in a rally. "If you take all the years combined, we did a great job of getting our clients through the worst bear market since the 1930s," says Gire. "But," he admits, "it was not a consistent, make-money-every-year kind of performance."

And that, of course, is the biggest problem with staking out your claim somewhere in Quadrant III: we still don't know a lot about it. The long bull market was an ideal time to explore and learn about Quadrant IV, and Gire says that shifting assets around doesn't work very well in a sustained bull market anyway. The



"By gadfrey, you're right! Limited partnerships are back."

current markets are going to provide a LOT of information about Quadrant III, and he thinks that even if they don't relocate their Quadrant loyalties, planners should get on this new learning curve, and begin to debate things that were once off-limits in the professional dialogue. They can dip their toes in the water or decide to swim.

Part of this debate will be about what has been described as the business risk of being too far from market performance: the idea that mirroring market performance is a safe harbor, that clients are less likely to leave if they are getting performance that is similar to what the market is doing to their friends in neighbors. Gire thinks that this argument is an artifact of the long bull market, where the question was not whether people were making money, but how much. And he points out that even in the best of times, advisors were losing clients because they were not aggressive enough during the tech mania. "Business

risk comes from both directions," he says. "In a low-return environment, the bottom line is liable to be, if you lose money, you are going to lose clients. But beyond that, the only really important question is: what is the best thing I can do for my clients? Even if I lose them, I have to do what I believe is the best thing for their long term welfare."

And so we may be entering an era when, suddenly, there is no clear consensus about things we thought we knew. "Once you allow that active management can add some value, then I think you get a continuum," says Gire, "ranging from those who are completely passive to those who are completely active. I don't know where the sweet spot is on that spectrum," he confesses. "I don't think we will have the answer until the end of the secular bear market. We're still developing our knowledge about how to invest, and there are a lot of discoveries that will be made in the next 10-20 years." ■

THE POWER OF PURPOSE

Here's a motivational speaker who offers more than just a temporary charge of excitement.

by Bob Veres

As many of you know, we're in the process of compiling a list of speakers recommended by readers of Inside Information, people who they have seen and enjoyed and--most importantly--learned something important from. The list, as you can imagine, has turned up a lot of recognizable names--some of the leading vote-getters included Dave Drucker and Joel Bruckenstein, Tracy Beckes, Ed Slott and Mark Tibergien.

meeting than a chapter luncheon. But his books ("Life By Design," "Closing the Gap," "Killing the Sale," "Wealth Strategies" and "The Power to be Your Best") and materials also have a lot to say about personal growth, and how (and where) to find the motivation to permanently change behavior. In fact, his perspective might be valuable to any advisor who wants to help clients overcome their personal hurdles, or who wants to offer a more personal version of the financial planning service.

If a person's success is not platformed on purpose, if it is simply platformed on action, then there will be a point in time where he or she stagnates.

But the process has also turned up some people you may not have heard of, whose presentations are off the beaten path in our profession. One speaker, recommended by Don James of the Kiplinger Group in Strongsville, Ohio, is Todd Duncan, of The Duncan Group in Duluth, GA (www.theduncan.com). Today, Duncan mostly focuses on helping sales professionals in the mortgage business, and his price (\$20,000) is more suited to a broker-dealer

The key concept here is what Duncan calls "on-purpose living." Duncan believes that all of us, if we want to make positive changes in our lives, need to identify what might be called "the point" of our existence, the thing that is most important to us. Once we have that, everything else can be organized around it.

You find your purpose by asking yourself some deep questions. What is the one thing that you want to present itself in all of your activities?

What is the most important thing for you to experience on a regular basis?

When you discover what that is, Duncan tells his audiences, everything else--decisions, motivations, goals--become clearer and more achievable. When you discover what purpose is, it becomes your main-spring, and you begin to order your life in a different way.

The opposite is also true. If you try to make changes without having them linked to an overarching purpose, Duncan maintains, then those changes are either hard or impossible to sustain. "If you don't know what's important to you in your life, if you don't know the why behind your efforts," he says, "then you will give up prematurely in almost every endeavor that you seek to accomplish in your life and in your business."

Take, for example, savings habits. Your clients know they should spend less than they make, and get ahead financially. At your prompting, they start to pay down their credit cards. But if they can't link that activity to some highly-personal purpose, something that is truly important to them, they'll revert back to the behavior that got them in trouble in the first place.

Duncan puts it a little bit differently: If a person's success is not platformed on purpose, if it is simply platformed on action, then there will be a point in time where he or she stagnates. "To discover one's purpose is the motive for endeavoring," he says. "If you don't know the motive, and if you don't know your purpose, then endeavor is more of a will-power issue than it is a natural motivation issue."

So where do you start? Duncan

invites people to start by doing a simple self-assessment. Are you (is your client) living life on-purpose or off-purpose? Are you living life intentionally or accidentally? Are you simply hoping for a different reality? Or are you expecting to experience a different reality based on a thought-through strategy and a plan?

“If you are not experiencing great levels of personal significance, if you are not succeeding the way that you want to succeed,” he says, “then you need to reorder how you are approaching your life, how you are approaching your business.”

Reorder how? Once you have your purpose, you need to define a goal. This, Duncan says, is very difficult for most people; it means they have to stop their lives long enough to decide what they want their future life to look like. He offers a terrific quote from a colleague: that people spend more time planning Christmas and holidays than they do planning their life.

As you go through the planning process, it is also important to give up on the idea that your future life is somehow burdened by the past. No, you can't change the past, he says, but you can make a decision today to start to create a brand new ending to your personal story. Duncan offers a terrific quote from Ralph Waldo Emerson: “One of the keys to total success and significance is to forget the yesterdays.” Later, Emerson says: “Finish every day and be done with it. You've done what you could. Some blunders and absurdities no doubt crept in. Forget them as fast as you can. Tomorrow is a new day. Begin it well, and serenely, and with too high a spirit to be encumbered



“If you’ll just have a seat, I’ll be happy to explain how we intend to phase out our commission revenues.”

with your old nonsense. This day is all that is good and fair. It is too dear with hopes and invitations to waste a moment on the yesterdays.”

He also quotes Henry David Thoreau: “If man advances confidently in the direction of his dreams, and he endeavors to live the life that he has imagined, he will meet with success unexpected in common hours. New and more liberal laws will dwell within him, and he will live with the licenses of a higher order of being.”

The point is that if you find the mainspring of your personal motivation, you will have found the key to accomplishing more than you ever dreamed possible. And if you then take the time to identify the direction you want to start accomplishing in, to

define how to make your life as nearly perfect as possible, then you've linked a source of virtually unlimited motivation with a goal that leads in the direction of happiness and fulfillment.

Duncan's personal growth concepts bring with them a set of ambitious objectives that few in the audience will have achieved. For the rest of your life you will never ever accomplish things accidentally again. You will never have to worry about where your motivation is coming from. Duncan cautions that this is not a quick fix; discovering your purpose and planning your future cannot be accomplished in an hour or a day. But what would be more important for you--or your clients--to spend your time on? ■

FUTURE, INVERTED

A second look at the Hurley report, with the benefit of hindsight.

by Bob Veres

You probably noticed that Undiscovered Managers--the Mark Hurley organization--has been purchased by J.P. Morgan Fleming, and that J.P. Morgan has, with the purchase, been named the investment advisor for Undiscovered Managers' Behavioral Growth Fund, Behavioral Value Fund, REIT Fund and the Small Cap Growth Fund.

This reminded me that it has been more than four years now since the organization released its Future of the Financial Advisory Business, Part I, which stated, forthrightly, "We believe that the financial advisory business will evolve in a similar fashion to the institutional money management business. From the fragmented ranks of the industry, a small group of 40 to 50 organizations will emerge as dominant competitors... Crafting comprehensive solutions for clients will become the critical function for all personal financial services companies such as brokerages, accounting firms, trust banks, financial planning organizations and insurance companies."

Four years later, it is fair to ask: how did these predictions fall so horribly off the mark? The answer, perhaps, lies with several built-in assumptions that, when corrected, offer a different view of the future.

Assumption 1: *Large financial services firms would be willing to forego profits while they sought to*

dominate the retail marketplace.

In retrospect, this sober prediction seems laughable. Short-term profits may not always be more important than market share in corporate board rooms, but there seems little inclination among the larger financial services firms to, as Hurley repeatedly said in his speeches, take short-term losses in order to screw up the pricing structure. Turn the assumption around and you get a more realistic picture: short-term profits matter, and those larger firms have to cover much higher built-in fixed costs than the average financial planner. If you look at the direction Schwab and Merrill are moving, the trend is toward higher, firmer prices, which could actually make it easier to charge a fair price for services in the future.

Assumption 2: *The public will be unable to distinguish between service providers who have conflicts of interest and those who do not.*

The Hurley Report came out two years before the research analyst scandals on Wall Street made those conflicts of interest--really at the beating heart of the Member Firm business model--visible to all. You could, of course, call this bad luck; who could have foreseen that these distinctions would suddenly become so clear? But if you turn the assumption around, the statement makes more sense. When has Wall Street ever been free of highly-publicized scandals, ranging from derivatives and Orange

County to selling life insurance as a retirement plan?

Assumption 3: *Larger firms can respond to changing market conditions more rapidly than smaller firms.*

The Hurley Report offers a lot of discussion relating to superior economies of scale and the ability to build legacy in-house software solutions. It seems to assume a degree of nimbleness that none of the rest of us are able to perceive in firms that have been routinely derided as dinosaurs. Yes, there are some excellent planners at each of these firms, and the very first thing they complain about is the legacy software they are stuck with when off-the-shelf solutions are evolving much more rapidly. They complain about fossilized sales staffers in their offices, about planning initiatives that are stalled because the branch manager is still paid based on sales quotas, and everywhere an inability to see past the quarterly numbers to the less-important well being of the customer.

Turn the assumption around and you get a clearer picture of what actually happened. If you want to see rapid response to changing conditions, look at the independent planning profession, which has consistently transitioned to more consumer-focused business models well ahead of its rivals.

Turning those assumptions around 180 degrees may offer a better picture of the future as well: smaller firms competing favorably with the larger firms, and consumers are increasingly figuring out that when a retail broker calls, there is a good chance he or she has a sales agenda. Fragmentation may not be a strength, but it is a better framework to respond with than bureaucracy. ■

THE PRACTITIONER FORUM

A COMPENDIUM OF THOUGHTS, IDEAS AND PRACTICE ISSUES FROM AROUND THE PROFESSION.

Tough Questions

When a group of us (Bob Veres, Bob Clark, Margie Welder) began working with Morningstar on its Advisor web site, one of the red flags that suggested that the relationship wouldn't work out as we expected came when we proposed that Morningstar create a standardized due diligence questionnaire, a kind of financial planning request for proposals (RFP) that each fund company would fill out once and make available at the booth and/or its web site, so that everybody could have the answers to some of the deeper due diligence questions that professionals like to know before they invest client money.

In the aftermath of the mutual fund scandals, this deeper-probing questionnaire looks truly prescient. Unfortunately, the executive team at Morningstar's advisor division wasn't thrilled with the idea of this qualitative evaluation process, and couldn't figure out how it added to their bottom line. So they decided that instead of using their clout to get the fund companies to fill out the form, they would instead offer funds a chance to pay to have their answers posted in the "Due Diligence Center" on its web site, as a handy way to market to advisors.

And, since the funds wouldn't be highly-motivated to pay for the privilege of answering tough questions, Morningstar cut back the questionnaire from roughly 70 detailed questions in five different categories to four softball questions that can be answered by the cheerful people in their marketing department. (You can find these four questions answered for a sample fund at: <http://advisor.morningstar.com/ddc/IndvFundQuestions.asp?selfundid=CHTAX&location=Investment+Philosophy&familyid=224>)

But, despite this discouraging setback, the dream of a consolidated RFP isn't dead. The goal is to allow each fund to answer these questions in one format, instead of in a thousand different ways in response to many different advisors--and therefore be able to justify the time and effort as a matter of consolidation. Instead of asking them to pay for the privilege, all we would ask in return

is honest, forthright answers.

The following is a list of questions that have been suggested by advisors over the years. Is there anything you would add to the list?

HYPOTHETICAL FUND RFP FOR ADVISORS

1. What is the fund's general investment philosophy? Are there any unique elements in your approach?
2. Since the fund's inception, has there been any change in the overall philosophy or approach?
3. Please define the universe of stocks, including the size, characteristics, and foreign securities, used by your mutual fund.
4. How is the universe of stocks constructed?
5. How many issues are typically in your portfolio? What criteria are used in selecting the issues for investing? Specifically, what do you look for?
6. What is your target market capitalization and what is the current market capitalization? What percentage of the portfolio is in the target market capitalization?
7. Do you expect these allocations to change?
8. Are there any secondary investment approaches used (i.e. technical analysis)?
9. Does your fund rely heavily on economic forecasts?
10. What is the fund's selling philosophy?
11. Using a specific investment, describe to us your entire investment process, from the idea's inception all the way through until liquidation of the specific security. Please include an investment that was implemented but was not successful.
12. What has been the portfolio turnover and where is it going to be trending over the next three (3) years?
13. How tax efficient is your fund? Do tax implications affect your investment decisions? What is the fund's effective tax turnover?
14. Does the fund have any tax-loss carry forwards that can be used to offset future gains? If so, how much

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Practitioner Forum

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in dollar amount or percentage of the funds NAV?

15. What is the average holding period for the fund?
16. How much money does this firm manage? How much is in equities? Are there any other businesses involved with the firm?
17. What is the size of your research staff? What role do they play in the research process?
18. What are some criteria for becoming a member of the research staff?
19. Please provide a list of key analysts/team members and their tenure with the firm.
20. How is research conducted in your firm? Where does this information come from? Please describe your process flow (top-down, bottom-up).
21. Where do you recruit your research staff? Inside the company, or outside?
22. How are you research staff/analysts compensated?
23. How are sector allocations determined? Are there specific policies regarding industry diversification?
24. Are there any restrictions on the top holding as a percentage of assets?
25. How many issues are currently in the fund? Please list the ten largest positions and their percentage of the fund?
26. If applicable, what is your exposure to Emerging Markets?
27. What is your smallest holding and why do you carry it?
28. Is there an investment time horizon or expected period in which an investment should reach your target price?
29. How do you control risk?
30. Do you sell short? If so, please explain your investment process and up to what percentage of the fund will you short securities?
31. Does the fund use leverage? If so, to what extent?
32. Does the fund purchase derivative securities? If so, to what extent and what types?
33. If applicable, what has been the currency hedging history of your fund? Do you foresee any change in hedging strategies?
34. What steps are in place to deter frequent trading

in and out of the fund?

35. What steps are in place to deter late trading, or buying mutual fund shares after the market close at that day's closing price; and timing which involves taking advantage of market-moving events after the close of the market?
36. Does the fund company give preferential treatment to hedge funds, allowing them the buy or sell fund shares at prices not available to the public?
37. What percentage of the portfolio manager's work time do non-portfolio responsibilities require? Break out marketing separately.
38. How long has the management firm been established? When was it founded?
39. Who is the head of the management firm? Please describe the length of this person's tenure with your firm and experience.
40. What percentage of the fund does the Fund manager or Team of Managers own?
41. What percentage of the manager's net worth does this number represent?
42. Please include a detailed biography of the manager(s). What is the length and degree of experience and responsibilities?
43. Have there been any philosophical changes in the management of the fund?
44. Is it possible to arrange for short phone interviews with the fund's portfolio manager once or twice a year? If so, who should we contact to arrange the call?
45. Is the portfolio manager(s) an owner(s) of the management firm? If so, what is the extent of ownership?
46. When was this fund founded? Please enclose ADV.
47. Does the fund manage any separate accounts, or have any privately managed money responsibilities?
48. What unique advantages does the fund have that would be of interest to prospective investors?
49. Please attach quarterly total returns for the fund either since inception or back to 1970. (Only include information for the period during which the current manager has been in charge).
50. What is the fund's expense ratio, and should we expect changes either up or down in the fund's expense ratio?

SURVIVING CHANGE

by **Bob Veres**

If you've read through this issue with any care at all, you will find a theme that is never stated but which breathes out from all the articles and really defines the challenge that faces the advisory profession going forward. Perhaps it is because financial planning is a new profession; perhaps it is because financial planning is, uniquely among professions, tied in with everything about a client's life--whatever the reason, the constant theme for planners is exploration. How do we define the "deliverable" of the planning service? How can we do a better and better job of helping people reach their human potential? What is there left to learn about investing, and are these lessons different in different market environments?

Of course, this constant change flies against the normal human tendency to look for a destination and ARRIVE. Think about how much easier it must be to practice as an eye surgeon, where you learn a technique and practice it over and over again, and perhaps once or twice in your career, a better procedure comes along and then you have to learn that. Or an attorney, who has to keep up with case law in his or her field, and may have to deal with a dozen seminal decisions which change the rules over the course of a career. In financial planning, it is not unusual to adjust to a dozen significant changes--spread out over practice management, the behavior of the markets, new regulatory initiatives, newly-introduced client services, new tax law changes, new software innovations, scandals that may or may not involve the investments you recommended, new investment alternatives etc.--every single year of your career.

Eventually, I think, the pace of change will slow down, and the profession will evolve certain standardized service and business models out of this current era of trial-and-error. But I suspect that planners will never experience less change per year or per career than any other profession, because what you do is tied up in so many areas of the ever-evolving world: money, taxes, investment markets, personal growth and achieving human potential.

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51. Are there lower expense ratios or institutional versions of this fund?

52. Does the fund use direct access with floor brokers/ ECN connectivity to control trading costs? If no, why not?

53. Do you expect to close the fund at a particular asset level?

54. What states is the fund not registered in?

55. Which mutual fund super-markets is/are your fund(s) distributed through?

56. Who does the fund use for its auditing?

57. When are income and capital gains distributions made?

58. How should the fund be used as part of a client's diversified portfolio? What type of client (i.e. conservative, moderate, or aggressive) should invest in your fund?

59. What have been the key factors in building the fund's performance?

60. What has been your biggest mistake in managing the fund?

61. What have you learned from this mistake?

62. List three things you believe have been your keys to success in managing the fund.

63. What are the fund manager's goals for the fund over the next 5 to 10 years?

64. What are the director's goals for the fund company over the same time period?

65. Do any fund managers have any plans of departing over the next 5 years (i.e. retirement)? If yes, who will be replacing them? (Please include a detailed bio of the replacement manager.) ■

Parting Thoughts

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So the important question becomes: how do you cope? What skillset does the successful advisor need in order to move to the top of this ever-evolving profession, and (much harder, I think) to stay there once that has been achieved? These are not, per se, planning skills, or practice management skills; they are, instead, personal coping skills that lie behind and beyond the churning foam of your daily existence.

I think there are three basic characteristics that everybody reading this publication should begin to cultivate.

The first is to have a strong core belief system that you can always go back to when making daily decisions. If you'll look around, you'll notice that many of the best and most successful financial planners have a kind of fanatical tinge around their gills. They give their loyalty to the consumer even if it means leaving occasional money on the table, and they have an unusually strong value system that sees right and wrong in black and white instead of the usual shaded nuances. You might think that these values are what attracts clients, but my experience is that clients have a hard time recognizing advisors with personal integrity from those who are selling riverfront property in the Sudan as tax-sheltered investments. It is not, as far as I can see, a huge marketing advantage, but it does help them in other ways. The strong value system is their rock in the storm, simplifying daily decisions, and also keeping them away from the areas of the business that are most susceptible to complicated, practice-harming scandals. Every ten years or so, when an unexpected tidal wave crashes through the profession, wiping away the opportunists who have built their houses near the shore, these people are largely unaffected.

The second is a healthy attitude about change. There isn't any way to sugar-coat this: changing things, every year, is a royal pain in the ass. It is disruptive, it is difficult, it requires you to learn new things and move yourself out of comfortable ruts. It takes energy, and many people begrudge that energy and do what they can to avoid these necessary adaptations until they become a crisis. The most successful advisors I talk with are deliberately uncomfortable with the status quo, and they budget time in their weekly schedule to figure out how to make positive changes, and more time to work on those changes. The least successful advisors are those who never seem to have a minute to sharpen their saw.

Finally, I think advisors need to spend time around other advisors in order to make the important adjustments incrementally, rather than all at once (or, as I sometimes call it, catastrophically). When you take the time, a minimum of twice a year, to compare notes with your peers and figure out where you're going and what they're doing differently, and where the trends are, then you accomplish two things. You recognize the changes that will need to be made before a crisis erupts, greatly lowering the psychic pain of change, and you also get a chance to see how others have coped with them, so you don't have to spend a lot of time reinventing various wheels.

Alas, in all the discussion about new IRA distribution rules and the conversion to a wealth management firm and life planning questions, these more basic prerequisites to success are hardly ever mentioned. They are the big picture behind the minutia, and if you can master them, the minutia, and the ever-present changes in the minutia, are a little less intimidating.