Executive Roundtable

Five financial services executives presented their views in a roundtable discussion following the Tiburon CEO Summit XXII in New York City, April 18, 2012.

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Context / Setting

Following the Tiburon CEO Summit XXII in New York City in April 2012, five financial services executives presented their views in a roundtable discussion. The 60-minute conversation was a spirited debate. This paper presents just a few of their important insights and observations.

Moderator: Evan Simonoff, Editor-in-Chief, *Financial Advisor* magazine

Roundtable Participants:

- Steve Atkinson, Executive Vice President and Head of Advisor Relations, Loring Ward, a strategist for broker/dealers and an outsourced money management solution for advisors
- James Carney, Chief Executive Officer, ByAllAccounts, a data solutions company
- Stephen Langlois, Chief Administrative Officer, National Financial, a Fidelity Investments company
- Matt Lynch, Principal, Tiburon Strategic Advisors, a strategy consulting firm
- Janine Wertheim, President, Securities America Advisors, the advisory division of Securities America

Publication Notes

An article based on the roundtable discussion were published in the June 2012 issue of *Financial Advisor* magazine (you can access that article at www.FA-Mag.com.) In addition, five video interviews (one with Evan Simonoff and each of the five roundtable participants, individually) are available as an "Online Extra" on www.FA-Mag.com.

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The Conversation Begins

Evan Simonoff: Most executives of financial services companies feel a sense of cautious optimism. They are starting to look at ways to deploy capital and start investing seriously. However, I think there continues to be a sense of unease beneath the surface and that's reflected among consumers. Even if their portfolios have come back, they often feel burned. Janine, is there a disconnect between the financial services businesses and their clients? Are financial services firms, in some cases, doing better than some of their clients?

Janine Wertheim: Reflecting on what we heard at the Tiburon CEO Summit and listening to feedback and insights from consumers as well as our executives at Securities America, we think we're doing a pretty good job of understanding the dynamics of the consumer. Many have been scarred and scared and have some skepticism about the financial services industry in general. However, most of our advisors stay very connected to their clients and take a holistic view to helping them navigate and focus on what they can control. I believe we're investing in the right things. I think our capital is being deployed in the right ways, such as newer technologies that make it easier for advisors to do business and identify the needs of their clients as well as comprehensive tools that help advisors better manage their clients' income distribution needs during retirement, taking their risk tolerance into consideration.

Simonoff: Maybe the issue should be reframed another way. Matt, even if a lot of clients' portfolios have recovered, is it possible that after two violent bear markets in ten years, their portfolios may be okay, but they may be permanently, psychologically scarred and more cautious and conservative? I mean, talk about kids today in their 30's and 40's and their 20's and 30's and they're talking about them like depression era kids.

Matt Lynch: I believe the consumer and the client (where the case is that the advisor is your firm's client) have both permanently changed expectations. As an industry I agree we are making

Matt Lynch

an effort to better meet client expectations, but I think we're way behind the curve. I think that most clients may be content to stay where they are, but they are not satisfied. If we look at the data, I don't think there is any greater degree of client turnover or asset loss among successful advisors than there was a decade ago. But I think it's not due to an overwhelming satisfaction level among their clients; rather it's a fear of the unknown. They don't know where to go. I don't think as an industry we're meeting their expectations yet, but I think there is a sensitivity and a recognition that we've got to change through innovation. In my view, one of the most important near term things we can all do, and I think Janine mentioned it, is providing the data in a way that the clients have access to it. Make the investments so that there's greater transparency and you start to rebuild that trust, right? But I don't think as an industry there's a full recognition yet of just how scarred the consumers are.

With regard to the next generation, they have a different set of expectations in part just because they are the next generation. But I think it's because of the era in which they grew up. They came into wealth during a period of time where it was just, "What do I do with it? Where would I put it?" And many of them, like the gentleman (on the Tiburon Summit Consumer Panel) who has the restaurant business, are betting on themselves, maybe too much. Maybe he should diversify a little bit at some point, but they are betting on themselves because they don't trust or have the knowledge to feel like they are making smart investment decisions. I think we owe it to those consumers to do a better job educating and providing greater transparency. As an industry I think to some extent, we're just playing catch up.

James Carney: I think there's a huge sea change that's going to happen and it's not due to technology — that's the easy part. It's a change that's needed in the advisor's behavior and type of relationship that they have with their client. That was borne out by the panel - and if you think they're unique people, they're not. We can throw all the technology at investors, whiz-bang reports etc., but real change that is needed is with the fundamental approach with how advisors communicate as well as the role they play with clients. It's a matter of understanding and embracing what an advisor should do beyond just the existing status quo. I think the advisors/technology firms that recast the client interaction model are going to be the big winners.

Cracking the Code

Simonoff: Do you know any advisors who are cracking the code?

Carney: Yes, we have a number of them as clients. They are RIAs — some of them are small and some quite large - that have taken an entirely different approach to the current client interaction model. As they said in the panel, consumers assume advisors have fiduciary responsibility and will provide the right level of information regardless of the legal requirement for a given type of advisor. Consumers expect that if your business card says “advisor,” you’re going to be looking out for their best interest as a fiduciary, versus if your card says “stock broker.” The advisor title is a big misnomer in some cases.

But what consumers expect is different and some of the more proactive firms have a completely different approach in that they look at not just the numbers and the long-term financial goals, but the relationship with the client. They are truly the quarterback. So if the client needs an estate plan, the advisor will bring in a good estate planner. If the client’s children are graduating or the kids are 18 years old, what do they do? They set up a Roth IRA when the children turn 18. The parents put $500 or a $1000 in to fund the IRA and the children have to contribute to it every Christmas with a portion of the Christmas money they receive. The advisors meet with the children once a year even though they have no substantial assets, but they will inherit assets at some point in time. But the most important benefit about meeting with the children is that they are teaching them about financial issues. So if a son or daughter wants to buy a car, they call the advisor (as well as discussing with their parents). If a son or daughter wants to rent an apartment, they ask the advisor, “What do you think I can afford?” It’s sort of a melding of financial advising with life coaching at a very high level, and it’s really a much broader relationship over time. It’s more akin to what’s done at a family office, but in a much more scalable way. To Matt’s point, the technology is there to make it scalable, but the technology isn’t the issue. It’s the change in behavior and paradigm shift and how advisors approach clients that is needed.

Simonoff: Stephen, you’ve got a viewpoint from, I don’t know if it’s 30,000 feet, but it’s the viewpoint from millions and millions of clients. Is there anything you’re seeing from that vantage point?

What Clients Want

Stephen Langlois: Well, I think what we heard on the panel is that consumers want to be more engaged in the activities of the advisor. It’s not “Do it for me,” anymore but it’s “Do it with me.” So that one panelist who will eventually engage an advisor, he is not going to just delegate to the advisor. He will require significant dialogue and interaction with the advisor he works with. We also saw somewhat of a generational change or difference on the panel. The older participants seemed to share a more traditional view of how to work with an advisor, right? Theirs was a perspective that the advisor is going to give me answers. But the younger generation is very comfortable with seeking and gathering information and leveraging technology to get that information, whether it’s about a restaurant or about their investments. This younger investor is going to be more involved with the advisor. We need to help advisors transition into that role and better enable it by making the tools we provide them easier to use.

Steve Atkinson: I think the biggest paradigm shift is that as an industry, we’re moving away from focusing on products. Something we learned a few years ago through our work with behavioral finance professors is that people make decisions with their emotional "right side brain," yet this is an analytical, "left brain" dominated industry. We want to throw out facts, figures, returns, and standard deviations all the time, and that's what clients are used to hearing even though most of them don't really understand those things. Clients make decisions primarily based on emotions. To help advisors deal with this shift, we're teaching them how to have a proper conversation to get to know the client and how to keep the focus on goals, needs, desires, etc. That's what clients want to talk about.

When consumers panicked in 2008, or last August when the market fell, the real question the advisors needed to ask their clients was, "So let me get this straight; you're concerned that the plan we put together is no longer on track?" This takes the focus off of the Dow Jones dropping 19% and on to "Am I on track?" Who cares what the Dow Jones is doing? If you planned properly and you had short-term cash put aside, does it really matter what the market did last month or the next month? It all comes down to planning, listening to the client and really getting to know how we all make decisions. That's the big shock wave I think that's going through the industry right now.

Wertheim: I would agree with the panelist who said, "Advice is dependent upon where I am in my life stage." I think that's why you got different answers from the women who were more accomplished, further along in their careers with larger asset levels, with affluent husbands compared to the younger men. The way consumers view advice and advisors has a lot to do with their experience. I believe you can still have young consumers from the Gen X and Gen Y that want to totally delegate to an advisor at some particular time in their life. I don't think they're in this box because of what generation they are. It's the experiences that they have along the way that determine whether or not they are willing to trust that advisor or not.

Janine Wertheim

Simonoff: Are any of you seeing a difference in people who are at or near retirement and have been through the last ten years and those who are in their 30s and 40s? For many of them in their 30s and 40s, investing in the last ten years might be like the 1970s - it was a great time to invest, but nobody wanted to do it. Are you seeing any of that?

Wertheim: Our advisors generally serve the pre-retirees and retirees. That's the lion's share of whom they serve. We don't have a large share of advisors that are marketing to 30 and 40 year olds but they are definitely interested in building relationships with their clients' adult children. We are developing more and more resources around helping advisors retain assets of the client's next generation. Understanding the whole family dynamic and discovering the best practices for retaining assets when clients pass on is a key initiative at Securities America.

Investment Outlook

Atkinson: There's so much noise out there, and people don't know what's good information and what's bad information. Like the comment that the last ten years is like the '70s; when people talk about the lost decade, they're talking about the S&P 500 or the U.S. large cap stock market. The U.S. is just one of 45 countries tracked by MSCI. We were one of the worst performing of the last ten years. Most international markets actually had positive, if not double digit, rates of return. So a well-diversified, well-advised portfolio during the lost decade probably had a return of maybe 5% or 6%. You know the compounding rule of 72, you almost doubled your money during the last decade, but I think a lot of people were poorly allocated and they were heavily allocated in U.S. large cap stocks. It's what happened during the tech wreck; it affected mostly U.S. large cap.

Simonoff: Yes — the banking sector is a huge percentage of the S & P.

Atkinson: The first quarter of this year was the best first quarter since 1997 for the S & P and the Dow and the best first quarter for the Nasdaq since 1991. Where's the party? I mean of the 45 countries where do you think that best first quarter in 15 years ranks? 28. Turkey had a 41% rate of return, but you don't see people overrating Turkey. You don't chase returns. You diversify like crazy and you educate the client because you don't know where lightening is going to strike next. So own it all and by doing that you're going to get the return of capitalism around the world. And capitalism over time has been the greatest rate of wealth. It's not just U.S.; it's everywhere now.

Behavioral Change


Stephen Langlois

Langlois: Near-retirees are anxious. We've done some work with consumers and they're anxious because they've seen how fast the world can change. And many of these folks, maybe half of them if you look at the data, have some form of Defined Benefits plan. I recently heard a consumer say, "You know I don't know whether my advisor is going to do much better than I, because given what I just went through, we didn't seem to be doing so well." So I think there is a lot of anxiety out there among folks who are getting close to retirement. What we saw with the younger two people on the panel was a sense that they have a longer runway, right? They had an attitude of, "I'm not really going to worry about this now. I'm going to get my business going. I want to find financing for my business because that's where I'm going to make the money. I'm not going to be as concerned with my investments right now." It's a matter of priorities. But their time horizon is so much longer than the older consumers.

Lynch: I think generally what we see is the fear and I think someone mentioned the fear of running out of money was greater than the fear of death. The behavioral change we are observing is that people are putting off retirement, as they're not sure that the nest egg they built up is adequate.

There's a flight toward more conservative investments. There's a desire for yield income that the industry is trying to keep up with that through new products. But there's less of a willingness to take risk with the retirement assets and a recognition that that the nest egg needs to be a whole lot larger if it's going to last 20 years into retirement. And for the below 50 group, there's an additional concern about underfunded pensions or the loss of pensions — we're seeing that happen in the airline industry and other places.

And so everybody knows somebody who's lost their pension through some bankruptcy or some default; such as the airline bankruptcies, or General Motors and others and those events do impact how consumers think. Is my Union pension fund really going to be there and is Social Security going to be there? So the retiring boomers are facing a lot of uncertainty. They are making different types of investment decisions and life decisions about how long to work or retiring into a different type of job. Not just working because they want something to do, but because they don't want to tap into that nest egg. If they can put it off five years and go ahead and retire and just work for another five years and generate enough income to pay the bills, that might give them another ten years in retirement. So I think we are seeing behavioral changes and concerns on the part of consumers. I don't think they've figured it out yet though in terms of what's the right mix, working longer, adjusting the allocation, or just not retiring. I think we're going to see a significant percentage of this generation choose not to retire because of the fear of running out of money.

Atkinson: Almost every retiree works in retirement. We have to have a purpose whether we're getting paid for it or not, you just do it. It isn't a 30,year vacation, right? But very few clients have ever actually thought about what retirement means. That's another key area advisors are going to have to address. Let's have those softer conversations that are uncomfortable to have and let's make them comfortable because that's what the clients are worried about. I met with a client a couple of weeks ago that's been retired 10 years, and he's worked almost every day. And I said, "Did you think you would work when you were retired?" and he said, "No, I thought it was like play time."

Simonoff: What sort of work was he doing?

Atkinson: Golf Pro, teaching people to golf. He's a really good golfer and he taught lessons at a local club. He loves it, but he doesn't view it as work. He loves to golf. He loves to teach. So he gets paid for doing something he loves and if he didn't want to do it, he wouldn't have to, but that's the beauty. So it's important to have the conversation with clients.

Simonoff: He's also got something to do every day as opposed to a place to go.

Carney: Yes; that was what I was referring to, a behavioral change. It's not just about the numbers, it's about advising them. It's not just about the financial piece, and it doesn't mean you are going to be a psychologist, but it's the basic things that anybody will go through when they're going to think about retirement. And to your point, Steve, discussing the client's vision of retirement is important. What do you want to do? Do you have hobbies? Do you want to spend 40 hours a week on that hobby? And at that level as well as around family, and all the other factors. That's what people will expect because it's high value.

Generating Lifetime Income in Retirement

Wertheim: Our feedback from advisors is that when they tell their clients about their process for generating income during retirement and lay out a plan for the client, it alleviates a lot of fears. We have been educating our advisors about using a time segmented income distribution strategy and we've been really focused on this since 2009. We have a comprehensive platform that includes education and coaching, marketing, an integrated platform for managing retirement income streams with an internal retirement income desk for support. When you talk to advisors that have clients that they've discussed our NextPhase® strategy with and presented the income distribution plan to them, they just seem to be able to ride out the storms better than those who don't. When the advisor educates the client on how the plan works in which funds needed for the first five years are guaranteed, funds needed in the medium term are invested somewhat conservatively, while funds needed later are invested for the long term, the client focuses on the plan instead of the volatility of the market. Clients want to know how they are going to get there and what do they need to do to generate a lifetime income check during retirement.

Atkinson: I've seen that firsthand with some of your advisors and their clients. I think the secret to that success is you're able to telegraph in advance to the client where their money is coming from. And they don't have to worry about where their money is coming from, with the time segmentation and the way you've allocated it, brilliant right? And it works in real life with clients.

Simonoff: One thing you may have seen as a result of the financial crisis is a growing interest in alternative investments - they're going mainstream now. Some people, traditionalists, question this. There are products out there that seem to be trying to separate alpha and beta and a lot more people are using tactical asset allocation strategy. There's a firm up in Boston, an RIA firm that Schwab bought, Windward, that they immediately took and started marketing both to RIAs and directly to their clients. Do you see that as a long-term viable trend? There's also AQR that raised $7 or 8 billion in two years. It's attracting money just because it's different and it's supposed to be uncorrelated.

Atkinson: I'll give you the unpopular answer of course. Do I think it's going to be a success? I think people are going to sell the heck out of it. It's a sexy story. Do I think most clients need it in their portfolios? No, probably not. A few of them will. If you have a diversified portfolio and you plan properly, you don't need to add speculative alternatives. You're not really buying investments there. You know they are adding this asset class, but we want to stick to our knitting for clients and educate them about investing. The issue I have with alternatives and managed futures is that you really can't predict what the return is going to be because there is no income. Take bars of gold, for example; they don't create income. There are no earnings so you can't calculate an expected return. You're simply speculating on price. My Mark McGuire rookie card, which was worth $500 at one time, is worth about a nickel. That's what happens with those things and I just don't think they belong in the average person's investment portfolio.

Steve Atkinson

Mainstreaming Alternatives

Lynch: To your point, I think we are seeing the mainstreaming of alternatives and the demand is coming down market, driven in part by advisor knowledge and more importantly lack of knowledge. So the broker/dealers generally, and other industry partners that advisors have, are not equipped to meet advisor demand currently with respect to alternatives, whether it's managed futures or REITS or whatever. There's not sufficient knowledge at the product due diligence level among distribution organizations in our industry to meet this emerging advisor demand. We've done some studies that show that two thirds of advisors indicate they are going to use/sell more alternatives in their recommendations this coming year, right? But I was at a conference recently with 40 broker/dealers represented and they really didn't have a plan to address that; in part, because it hasn't been part of a standard allocation strategy for that emerging affluent or middle market that many of them are serving, but also that there's a disconnect in that the perceived risk associated with alternatives at the broker/dealer level is very significant. The E&O carriers are really not eager to cover it. There's not adequate knowledge at the local office level, so there's a mismatch in terms of market demand and part of it is that they can't get their arms around the data like they can a mutual fund. The aggregation, the data, standardized reporting, standardized evaluation methodologies need to be resolved so that it can show up on a statement and not be some held away asset.

So the clients think they want it, but there's an education gap. The advisors think they want to deliver it, but the industry, both in terms of knowledge at most firms, the risk, the E&O coverage limitations or exclusions. And I think most importantly the data has not kept up. So I think we're going to see creative products come out. I think to your point we're going to see sales, but I'm not sure that they are being sold the right way. I'm not sure there are thoughtful processes in place in terms of saying, "Should I allocate this in my client's portfolio?" I'm not sure that the industry, in terms of the advisor and their broker/dealer partner, are as informed as they need to be to really meet the demand that's out there and yet they'll still try to meet it, right? So there's some risk there. I mean as an industry there needs to be an answer to the data. Once they've become accessible, on statements like every other asset, like a mutual fund or TAMP programs or whatever, then I think we'll break through and they will probably truly become mainstream.

Simonoff: Well you're talking about a small pool. Most advisors who are using the AQR are plugging their products hard, but they are a pretty small part of the portfolio. I am thinking of two advisors I know with advanced degrees in engineering who are very smart and when they came out with these risk parity funds, both these advisors said, "I followed these guys for about 50% of the presentation, then I lost it and then I decided that if I couldn't follow it I wasn't going to invest in it." These are advisors who have given some of their other, easier-to-understand products 2%, 3% or 4% for each of their portfolio. What are you seeing on your platforms, James?

Evan Simonoff

Carney: We have data and it's based on RIAs, wealth managers, private banks, and family offices. Our client base consists of well over 1500 firms, some large and some small. The alternative investments are growing at a 30% increase over last year. The difference may be due to the fact that RIAs understand what they are investing in because they do their own due diligence. Often it's a very specific need for the allocation - for example, REITs for meeting a real estate allocation need. Some REITs now have offerings with a daily NAV.

James Carney

Simonoff: Are these private REITs?

Carney: Yes, most are private but we see an increase in traded REITS. One thing in common regardless of whether the REITS are traded or private is that the REITS themselves are not highly leveraged. Advisors are clearly increasing the use of REITs as part of their strategic allocation.

Wertheim: That's traded or non-traded REITs?

Carney: Non-traded.

Simonoff: Stephen, what are you seeing in terms of alternatives?

Langlois: There's a lot of interest. But I also think that end-investors don't quite know what to do with them. The interest comes more from the advisor than from the consumer. For advisors registered with broker/dealers, probably it is dependent on the position the broker/dealer takes with regard to whether they allow their registered reps to have access to alternatives. I think probably the biggest area of interest is REITs because of the yields.

Carney: And as you said, it's different for an RIA than for a broker/dealer because there is much more you have to go through to put it on your platform in terms of due diligence. An RIA, family office, private bank can do their due diligence on their own and make that decision. So that's why it works for them.

Growth of Hybrid Firms

Lynch: And of course the growth of the hybrid firms, where they're having to deal with both the broker/dealer compliance and regulatory structure and the RIA, I think we're seeing a desire for growth there in terms of alternatives and they are trying to keep up with that demand, in part, relying on the due diligence often of the broker/dealer. And so they're still trying to catch up.

Atkinson: I'd like to clarify, I mean, actually real estate is an asset class. It's an investment. That's the trouble because the alternatives are so big and vague. I'm talking about commodities.

Simonoff: You were talking earlier that you still think a diversified portfolio is going to offer protection in some ways unless you give the Six Sigma - the 2008 scenario. A lot of people are saying "buy and hold"' is kind of dead or passé.

Atkinson: I've heard that. (laughter)

Simonoff: I'm sure you have. Do you think that's valid?

Modern Portfolio Theory

Atkinson: No. It depends what you're buying and holding, right? Just buying a mutual fund that owns like 30 securities and hoping those are the right 30 is not a good strategy? When I think of buy and hold, I go back to MPT and Dr. Markowitz's thesis that you have to have a balanced allocation between equities, fixed income and cash. And you think about that allocation mix, even in 2008, fixed income and cash were flat or positive. Now, most people's fixed income was negative because their managers were chasing yield or mortgage backed security type stuff and went out on the risk curve and got clobbered. But short-term fixed income, high quality fixed income was positive; it was like 5% or 6% that year, and it all goes back to what are you putting into the client's portfolio?


Steve Atkinson

It's like building a house made of straw versus brick. The brick house is going to withstand more storms than the straw house, so you've really got to know what's in there. So I definitely believe in a globally diversified portfolio, properly weighted based on a client's pain threshold. And that's really the key — the risk tolerance questionnaire — at what point are you going to bail? There's really only one question you have to ask: How big a drop in the value of the portfolio a year from now would prompt the client to bail? And the client will tell you and you kind of reverse engineer this in the stock-to-bond ratio based on the downside percentage level. There is no evidence that buying and holding a globally diversified portfolio didn't work over the last 10 years or for that matter, the last 80 years. The data is overwhelmingly positive that a diversified portfolio of equities, fixed income and cash in free markets is arguably one of the greatest creators of wealth in our lifetime.

Simonoff: Okay, you spoke in slightly disparaging terms about commodities which seem in your view that they are not appropriate or that if you buy into countries like Brazil or Russia, resource rich countries, the Middle East, your portfolio will end up with Canada; you'll end up with significant exposure to commodities and you don't need to buy the actual physical asset itself.

Atkinson: Exactly, you buy mining companies and the companies that actually are getting profits from the higher commodity prices, you're getting a lot of exposure right there. I've got commodities — I've got a wedding ring on. But I'm getting other value for the use of the commodities. I'm just arguing that something that doesn't have any earnings can't be called an investment because there's no expected rate of return. It's just the difference between investing and speculating. I'm not saying you shouldn't own commodities or art collections or things like that. I just wouldn't call them part of your investment portfolio. But like what James' company does—I'm sure clients are asking advisors to aggregate all of their assets to show their net worth, but it's very important to inform a client that they shouldn't think of that as an investment because there's no expected rate of return. Because the day that price drops the clients are going to ask, "What happened?" And what happened was people had a new price tag. Think of the phenomenon with the Dutch tulip craze. There are so many examples of that, like the real estate bubble. It's only worth what people are willing to pay for it and when people reassess risk, price can drop immediately.

Defining Transparency

Simonoff: Janine, I'm sure you have advisors who have clients calling them up saying, "Buy gold, buy gold." What's your view on that? It's the client's money.

Wertheim: On the consumer panel today, when asked "how would you define transparency", they said "transparency to them means simplicity". If the advisor doesn't understand the investment inside out it's hard for that advisor to invest the client's money in it. And, you have to ensure the client understands the investment. We aren't hearing from our advisors that their clients are begging for gold. We're a pretty conservative shop, from an advisor perspective. While some advisors may utilize a more tactical approach to money management, the majority uses a more strategic core with some tactical overlay. Steve's comments reflect a large share of what many of our advisors are implementing.

Janine Wertheim

Simonoff: Stephen and James, from the big picture across a lot of accounts, do you see rising interest in gold, copper, oil, manganese?

Langlois: I don't really have a point of view on that from our perspective.

Carney: So we have over $500 billion of account data we aggregate every night and when you look at alternatives, REITs, hedge funds and private equity are the vast majority in dollar volume as well as units. Commodities are not even a fraction of a percent.

Simonoff: Really? It's not even 5%?

Carney: No it doesn't even show up, but the real estate does show up and hedge funds show up, but not the other kinds of more speculative things and even the REITs that show up, it's really interesting, they are all based on cash flow and return, regardless if there is any value in the property, whether there is any appreciation at all. That's not the basis of why people invest in them. They expect zero appreciation and anything they get is gravy. So they are very conservative. Some of the hedge funds are more speculative, but those that do hold hedge funds are fairly sophisticated and have a sophisticated clientele.

Retirement Income

Simonoff: Okay, let's turn the questions back to something we touched on earlier — retirement income. Looks like most people, even people who saved a lot of money and fairly high net worth individuals are not in a position to earn a significant amount of income off of cash today. I mean what is it? $20 million to get $50,000 in income. It's not a great proposition and that's really affected a generation of retirees who thought they had done everything right. How are your advisors, Janine, I mean there are places you can go; floating ripe bond funds, emerging market bonds, there are places where you can get more than a percent or two as everybody learned with bank stocks in 2008 for a favored source of income. They're not always risk free. Are there any particular options your clients are favoring right now?

Wertheim: Based on feedback from our advisors, they are mostly using a diversified group of fixed income mutual funds including some high yield bonds and variable annuities. In a recent survey of our advisors, there was considerable interest in exploring publicly traded REITs, ETF's and structured products. They want more research and we're fortunate to have our parent company, Ladenburg Thalmann coming to the table, providing some of that research — it's a benefit for our advisors. With interest rates so low in the fixed annuity space, the most used yield generators our advisors are using are diversified portfolios of bond funds.

Atkinson: From the beginning of our company we never viewed fixed income as the way to actually generate your income stream. It's just a dangerous game to allocate so much into fixed income just to live off the yield, so we've always professed a total return strategy. Dr. Meir Statman, who is a behavioral finance professor at Santa Clara, is on our investment committee and he talks about how all people engage in mental accounting and it fits into your segmentation strategy. We segment portfolios according to different needs.

The corn flakes money is for what I need today. When I wake up I want to be able to eat, right? So what we've done from a total return portfolio strategy is establish a dedicated cash allocation in the portfolio, which is going to be in any of their portfolios, but from a reporting standpoint we help the advisor educate the client on its proper function: "Okay, this 25% of your overall portfolio, in cash and high quality, short-term fixed income, is where we're going to draw from when you need cash over the next five years. Your equity component is your next ten years. The intermediate fixed income to short fixed income, that's maybe the five to ten year gap, even if it's one big portfolio."

So really nothing has changed from a portfolio construction perspective. What's changed is the reporting, the transparency; so now you are educating the client on how it fits into the mental accounting that they are already doing.

Better Conversations with Clients

Langlois: Providing clients — whether they are broker dealers or RIAs — with tools that enable an advisor to have that conversation is really important. We have a product called myStreetscape, which is the consumer portal of our platform, which helps the advisor have the dialogue with her clients, maintain transparency and see the same data at the same time. I mean we heard today, I thought it was interesting, of the conversation about statements — "I don't know what it is and I don't understand the data," and I think that consumers want to understand what's going on in their accounts. It's in their interest and the advisor's to be able to easily have that discussion and look at the same stuff and do it efficiently. Because otherwise, if the rep spends all day long explaining all the different lines on the statement, it's just not a good for anybody — they'll end up missing the forest for the trees.

Simonoff: A question for James and Stephen, because you can see this. You probably know your clients' age, right? Are you seeing in this slow yield environment, I would think, maybe I'm wrong because stocks have done pretty well, but are you seeing balances? Any declining balances noticeable among people over 65 – 70? They certainly are not living off the — well maybe they have high yield or emerging market bonds or something.


Stephen Langlois

Langlois: They work more and delay their retirement. If you talk to advisors about what in the past five years people have done, they change the time horizon they have for when they retire as much as try to pull money out of the portfolio because they can control that. I think the profound impact that the market crisis brought with consumers is that they realized that they couldn't control things. They can control, but for health issues, how long they work and those sorts of things and that's how they have been generating incremental income – but working more or finding, as we talked about, other forms of employment to get the health insurance, to get your income to cover your costs. I think people have had to be more self reliant on their own capability as opposed to reliant on their portfolios. And advisors can encourage that.

Wertheim: They are classifying the new boomers and the old boomers now. Thank goodness I'm a new boomer, but you know one of the things advisors say is really the biggest problem with clients is their spending behaviors; overspending. And so I think you're exactly right, they would rather delay retirement than reduce spending and that's just kind of unbelievable. We just did a white paper on this - talking to clients about overspending and retirement. I think advisors are coming up with some pretty good ways to kind of zero in on this, but it's a hard behavior to modify. I think that we still have to crack the nut; client's spending behaviors.

Simonoff: Janine, you think that even after 2009? Because one thing that I heard from some advisors is you don't have to lecture clients nearly as much about overspending.

Wertheim: I think they lasted for a little while. Unfortunately, many people have gone back to their ways. At least, that is what we hear from advisors. They are still struggling with it. In fact, a recent survey of our advisors indicated that a top concern during their clients' retirements is overspending. The number one concern was managing healthcare expenses closely followed by overspending.

Closing the Gap

Lynch: Some of the data that I've seen suggests that for a certain segment of the population, let's call this maybe it's below half a million of investable assets that are within 5 years or 10 years of retirement, the challenge they face is that there's not an opportunity to fix it. Even if they reduce their spending, discretionary spending by 25%, it's not going to close the gap. So the option is, "Well, I'm going to go ahead and keep working. I can't fix this." Just as our national debt, at over $14 trillion, we can't fix it by raising taxes on one small segment of the population. There's got to be a broader fix; reduce spending, increase revenue. For clients, first of all there's not sufficient education around what it takes to get there, but if you're within 5 years of what was your planned retirement and because of the market performance in what was to be your final working years, you can't close that gap. It's unlikely you're going to tweak your behavior. You'll keep working. You'll more likely put off retirement a few years. But there's just not enough room to close that gap through reduced spending along, so they choose not to change that behavior.

Carney: I can't tell age by our data. But a couple of things I can see; one, there has not been a tremendous shift in allocation other than; the big shift is the increase in real estate investments. But the one thing I hear in talking to a number of our advisors is that what they've started doing is, applying more focus on goal based planning. In addition, there is more focus with regard to performance analysis against goals by portfolio allocation.

Margin Compression

James Carney

Simonoff: Okay, one last question. I'll start with Matt. Chip (Roame) mentioned that Tiburon Strategic Advisors has seen a pretty big increase in clients looking to the Schwabs, the Fidelitys, the people that help self-directed investors. But when you look at the earnings out of a Schwab or TD, it doesn't seem like, if they're getting the business it's really dry — are they giving the services away? Is a lot of it going into money market funds where they're earning nothing?

Lynch: I think one, throughout the industry whether it's the broker/dealers or custodians are experiencing significant margin compression. I mean there is virtually no margin when we compare to just a few years ago, right? So even if you are accumulating more assets as a custodian or a broker/dealer, it's really tough with no margin on the money market assets. There are very few places to make that up, but they are gaining market share and the do-it-yourselfers, maybe the assets are moving from one bucket to the other so maybe it's advisor directed to do-it-yourselfers, but the net assets aren't producing increased margins. But I think what we are seeing is this share of wallet changing, where I don't know that consumers fit neatly into one bucket or the other. I don't know that they're putting all their assets into self-directed — we're seeing them kind of do a little bit of both. We're seeing a client have an advisor and will put maybe 20% investable assets or 50% and they'll manage the other half themselves. They might have multiple accounts, they might deal with a Schwab or TD and their advisor might be as well.

Simonoff: What do you think is driving it, is it the lower cost?

Erosion of Trust


Matt Lynch

Lynch: I think it's the trust gap. It's the perception that was mentioned at the conference, that's there's a significant population of consumers who believe that the entire industry looks like Bernie Madoff — that they hear about, the Goldman issues and other things and they just believe that the table is tilted against them. The odds are not in their favor. Take the argument over the fiduciary standard; I think that there is a certain segment of clients who believe, "Look, I'm not sure I'm getting the best advice. I'm not sure I'm getting the best deal." And they might even say, "I trust my advisor, but I'm not sure I trust the institutions behind him and the lack of transparency." That's why I think we're going down a path, whether it's driven by regulatory change or not, as an industry we have to educate the clients, be more transparent with them, demonstrate that we're great firms, it's a great industry that really provides a lot of value to the clients that we all serve. But I think we've got a long way to go to win back that trust. Meanwhile, the clients, more of them are going to tend to do it on their own because they don't perceive the value or they don't believe that we're all operating in their best interest.

Simonoff: I was going to ask Janine. I talk to fairly sophisticated people who have an advisor. It's not an issue of trust as much as it is an issue of, "He's a nice guy. He's intelligent. Or a nice woman, but how much more does he really know than anybody else?" I mean the only person who, there are only 5 people who saw the 2008 meltdown coming. John Paulson was down 50% last year. He was kind of a one hit wonder. So there's a general — I don't know disrespect is the wrong word, but…

Wertheim: We're just not hearing that our advisors are having difficulty retaining clients nor does the data show that they are losing clients to the self serve market. We definitely watch our transfers out. We certainly don't want to drop this from the radar and we want to continue to equip our advisors with great tools so that they can provide great value to their clients. We believe that advice has never been needed more. That means our advisors need to ensure their clients are fully aware of the value they are providing and it means our firm needs to continue to offer tools that help our advisors stand out.

Langlois: The value they deliver is not just the returns. We heard that today. It's the communication, it's keeping clients informed, it's understanding their needs and listening, it is not all about the numbers. As an industry, we need to enable advisors to do more of that and make them aware. It's broader.

Simonoff: At Fidelity, you probably have clients who have money with an advisor and self directed money, both of them at Fidelity, do you see movement going one way or the other?

Langlois: Yes, but we wouldn't then see the other side of these clients' money that might be at Fidelity.com as we segregate those accounts and maintain a wall between those different businesses.

Wertheim: We use National Financial, which is a different platform than Fidelity, and they don't have a way to match that up.

Langlois: We don't match that up.

Simonoff: James, do you see any?

Carney: I don't see any of that because I don't see what the consumer has on their own. I only see what they have through the advisors as well, so I don't have any insight. But my sense is that the advisors that we work with are advising on the majority of their clients assets, that's why they're using us. We're getting their client's Fidelity account, we're getting the other accounts, and we're getting the 401Ks.

Simonoff: Is there a typical number of accounts per client?

Carney: It ranges and there's an average number of held-away accounts per client of 4 and it can go as high as 10 or 12.

Simonoff: Well is there anything that you can think of to add; any burning issues that we haven't touched upon here?

Industry Innovation

Langlois: Whenever I come to these Tiburon conferences I come away with the fact that we forget sometimes how much positive intent there is in our industry. And whether it's through the innovation that was featured with David Booth and what they've done at DFA, or Bob Reynolds the work he did building the retirement business at Fidelity and now the turnaround at Putnam, there is phenomenal positive intent in this industry across all elements in the value chain. Somehow that message doesn't get out in the mainstream media? Back in the crisis, Bernie Madoff, those sorts of catastrophic things then cast a lot of negative aspersions on the industry, but there is just incredible energy and positive intent about doing the right things for consumers and enabling advisors to do the right things for their consumers. That's just really refreshing. You know we live in this every single day and then you get to come to a conference like this and the innovation and positive intent is all there in many different ways whether it's a Bright Scope – kind of a Yelp! for financial advisors or whatever that's going to be. It's very refreshing, I think, in many ways to remember that.

Simonoff: Are there any things, any new initiatives - you just mentioned Bright Scope - any new initiatives that you think could be very positive for clients?

Atkinson: I think a big initiative that is already happening, and it's only going to get bigger, is the changing landscape in the 401(k) marketplace. The increasing transparency and fiduciary standard are a major, major change that will put RIA advisors in a good spot. Full transparency type advisors are going to thrive when this goes mainstream. That's a major thing happening.

Lynch: I think one of the other drivers that we're seeing, we've had a number of conversations and a number of the panelists mentioned how they are investing in and leveraging technology and particularly with focusing on client facing technology where it's coupled with the behind the scenes data that the advisor has and bringing that information and delivering that to clients in new and different ways. To Stephen's point, it's that positive intent. There's a lot of capital that's being deployed, a lot of resources; new entrance into the industry, new sources of capital. They are excited about the future and about delivering value. And part of it is delivering value through access to data, educating the clients, recognizing that they need more information to make better-informed decisions. One of the exciting things that I took away from the conference is there is a desire to really add value and to demonstrate the value to close the trust gap.


Janine Wertheim

Wertheim: One of the most talked about tools at Securities America is our NextPhase® program and we just keep evolving it over time. The platform has a number of client facing tools to help advisors establish solid retirement plans for their clients. The platform includes a special website, educational videos, commercials, a proposal system, a monitoring system and a host of other educational tools. Our goal is to help our advisors serve their clients with the best advice and that involves considerable investment in technology to present the data in an easy to understand way so that their clients feel good about the advice and service they are receiving from their advisor. There is something to be said for some type of semi-serve advice based on the feedback and technology proficiency of the younger consumer who is in the earlier stages of accumulation. The younger participants on the consumer panel certainly touched on that and indicated they need the right amount of advice at this stage of their life. We continue to listen to our advisors through our various advisory councils to determine the needs of their clients. I can see where helping advisors create turnkey advice models for the younger generation might be something of interest to them. As I think about what we've done on the NextPhase platform, we have built a great foundation for helping advisors deliver exceptional advice, and it would make sense to consider using that same foundation for different life stages of the client's need for different levels of advice.

Simonoff: Well, thank you all very much. I'm happy to have done this.

-- More --

Roundtable Participants

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Steve Atkinson is the executive vice president in charge of the Advisor Relations Group at Loring Ward, a leading provider of investment strategies and business development support for independent financial advisors. He oversees a team dedicated to helping the independent advisors grow their businesses through ongoing support, coaching and partnership.

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James Carney is the president and CEO of ByAllAccounts, a provider of account aggregation software for investment professionals. He and his teams have had a proven track record of effectively building, marketing and selling highly scalable, complex solutions on time and within budget.

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Stephen Langlois is Chief Administrative Officer for National Financial, a Fidelity Investments company. Prior to joining National Financial, he was Executive Vice President at LPL Financial, and had also served as Director of Strategy and Business Development at Columbia Management.

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Evan Simonoff is Editor-in-Chief and Editorial Director of *Financial Advisor* magazine, as well as Editorial Director of *Private Wealth* magazine. He has spent more than 15 years as an editor and reporter covering the financial services industry. Evan is a widely recognized expert on personal finance and investments.

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Janine Wertheim is President of Securities America Advisors and Chief Marketing Officer for Securities America, Inc. She began her career with Securities America at its inception in 1984 and plays a key leadership role in ongoing technology and quality initiatives.

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