

# What We Know Now: Planners Reflect on 2009

by Shelley A. Lee



**T**heir comments are raw—“anguish, insomnia, weight gain, panic”—and contradictory—“After almost three decades in practice, I never could have imagined this,” and, “No, it wasn’t really a shock.” They’re also pragmatic—“It’s cyclical, relax!”—and painfully wry: “We now have a lower minimum balance for a new client account, since \$500,000 accounts are down to \$300,000.” There’s the optimistic—“Good people continue to do good things”—and the snide:

“CNBC is a joke.” There are more than a few who acknowledge their disappointment—“The experts really don’t know any more than I do”—and the obvious: “We now know that annual losses of 40 to 50 percent in the stock market are not just theoretical.” And there are almost too many to count who mention risk, and the lack of in-depth understanding of the concept by clients and planners. They say they’re re-evaluating the asset allocation strategy they typically recommend and are spending more time and money on client

communication. And they refer often to the cultural and business touchstones that helped them then, and still do: colleagues, Black Swans, and Nick Murray.

Every good crisis deserves, and usually gets, a post-mortem. The crisis/debacle/meltdown of late 2008 and 2009 is no exception. And like any group coming together after a seismic event, the post-mortem on the past 12 months in the world of financial planners is equal parts therapy, confession, and “told ’em so.” Three hundred twenty of them took the

time to answer a 44-question FPA survey in September 2009; 10 were interviewed at length, describing their stumbles, their victories, their emotions, and their outlook. But the clarity of hindsight is one thing; the ability to adapt and shape future behavior—their own and that of others, such as clients—is another. What have financial planners really learned?

Ask almost any actuary about using models to manage risk and you're likely to get this answer: models are often subject to their greatest limitations precisely when they are needed the most. Now ask Google if asset allocation or modern portfolio theory failed and you'll get 446,000 and 2,560,000 hits, respectively. Articles examining what went wrong in 2008 and 2009 appear everywhere from the industry publications—"Financial Planners Need Better Answers" for clients with shorter-term horizons was the opinion of a *Registered Rep* article—to top-tier business and consumer publications: the *Wall Street Journal* called asset allocation the "failure of a fail-safe strategy" and the *Financial Times* likened it to the wisdom of crowds becoming "the madness of mobs." Ask a group of financial planners the same question about whether the bedrock principle of asset allocation failed and you'll get mixed results. While 50 percent of planners in the FPA survey said that modern portfolio theory did not fail, the other half said yes or that they weren't sure.

The recent financial crisis and bear market have reminded us of risk's supremacy, says Jamie Lapin, CFP®, of Risk Management Group Inc., in Rockville, Maryland, who notes that when she named her firm in the mid-1980s, having "risk" in it "wasn't very exciting—now it's pretty popular."

Lapin began her career as an options trader, so she's not particularly averse to risk. But despite an extraordinary amount of time educating her clients on the risks inherent in ... well, taking too much risk, some of her clients didn't quite buy it. In 2007 and 2008, she began using more conservative investments for client portfolios,

including annuities with income guarantees, not wanting older clients to have to depend on a portfolio that needed a lot of time to heal. "I felt sort of ridiculous positioning people out of harm's way when they were saying, 'What harm? Everything's going straight up.' Clients, and some planners, were pointing to the dotcom implosion of 2000 and saying you could see that coming because many of those companies had no business plan or revenue, but that this subsequent 'up' period was very different," says Lapin. "But there were plenty of signs for everybody that we were in for a bad downturn. If the sky appears to be falling for two years, it's likely that it's not falling gently."

As for whether the "failures" of typical portfolio construction will change how planners practice, "It certainly will for some," says Lapin. "That's a given. Clients are highly risk-tolerant—until

they're not." Adds Bedda D'Angelo, CFP®, of Fiduciary Solutions in Chapel Hill, North Carolina, "People *always* overestimate their appetite for risk. I distinctly remember a 61-year-old client telling me that surely she shouldn't have as much as



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—Jamie Lapin, CFP®

40 percent of her portfolio in conservative fixed-income investments, should she?”

The tolerance for risk must be meaningful, says Michael Mazzilli, CFP®, an

## Lessons Learned from the Economic Downturn

- Although the media have suggested that the need for better tools and processes to address and determine risk tolerance is one of the major lessons learned, our evidence suggests that planners are largely satisfied with the effectiveness of their existing products and processes, and are looking only for incremental improvements in this area.
- The evidence suggests that planners were more prepared than they give themselves credit for. This could be the reason that other recent research has indicated that planners are enjoying a rise in market share, relative to brokers.
- Among people who think that modern portfolio theory didn't fail, the percentage has remained steady over multiple studies, suggesting a core of believers.
- Among people who said they were reevaluating their asset allocation strategy, the percentage had remained consistent over multiple studies, suggesting that reevaluating asset allocation is an ongoing process, not necessarily dependent on crisis conditions.

For more information about the study, see the results at:

[www.FPAnet.org/Learn/ResearchCenter/ForPlanners/AYearAftertheMarketCrash](http://www.FPAnet.org/Learn/ResearchCenter/ForPlanners/AYearAftertheMarketCrash)



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—Bill Russo, CFP®

adviser with Ameriprise Financial in Mamaroneck, New York. It’s always a struggle to identify it in a way that can be both measured and understood. He thinks that most typical risk tolerance questionnaires failed planners and clients, although it’s fair to say that even a loss tolerance

Russo, CFP®, of Securus Financial Strategies in Solon, Ohio, is committed. “We’re going to be much firmer in our discussions about the nature of risk and about how much our clients are taking,” he says. “We’ve recalibrated portfolios because we now know that many clients just can’t take

figure may have been too low for 2008’s losses.

“Too many are theoretical,” Mazzilli says. “It’s hard to relate terms like ‘moderately conservative’ to having a million dollar portfolio and losing \$250,000. We probably all need to get better at that conversation.” It’s a conversation to which planner Bill

the risk they thought they could—even though they’re calling and saying, ‘Now that the market is going up, aren’t we going to get a little more aggressive?’”

Despite planners’ best efforts, the diversification-through-asset-allocation strategy is still misunderstood—it’s intended to minimize risk, volatility, and harm, but not to *eliminate* all those things. Asset allocation is not magic—it was never intended to mean that a portfolio wouldn’t go down in value. This, says Rick Mayo, CFP®, a branch manager with Raymond James Financial Services in Virginia Beach, will be the ultimate education lesson for clients going forward.

“Intuitively, they know that we’ll never avoid the ups and downs of the markets in the long term,” says Mayo. “Emotionally, though, it’s hard for them not to wonder if they’ll be wiped out in the short term. The bottom line with any re-evaluation of asset allocation is to avoid the train wreck.”

As with many planners, Mayo experienced

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real, gut-twisting fear during the downturn, the most acute being early March. “I was frightened—I didn’t know where down was, and the negative press about the Dow Jones going to 4,000 begins to work on even professionals with many years of experience,” says Mayo. “What saved me was the support of my clients and some tactical allocation changes I had made earlier.” In early 2008, Mayo began adding more alternative investments to clients’ portfolios, primarily short ETFs (for their negative correlation), commodities, and natural resources. “I was on to something before the big drop without really knowing how much it would help,” Mayo says. “I wanted something tactical to smooth the ride, and in fact I ended up with an asset class that actually went up during the fourth quarter of 2008. Now I wish I’d done more.”

Tactical adjustments are the basis for much of the debate about whether “old” notions of static, strategic asset allocation

are flawed. Unlike in years and decades past, global financial markets now move more *in tandem with*, than in opposition to, each other, reducing the benefit of diversification. A *Wall Street Journal* analysis showed that by early 2008, almost all asset classes were moving more significantly in sync with the S&P 500. Commodities were the rare bright spot, with a strong rally in early and mid-2008. By early 2009, though, the disciplined, mathematics-based strategy of diversifying with asset allocation had broken down, at least temporarily. In fact, even the chief economist of Ibbotson Associates told the *Wall Street Journal* that diversification’s recent performance has been “humbling.” An Ibbotson analysis of the



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past 35 years showed that European stocks rose, on average, three-quarters as much as U.S. stocks did in months of gains more than six percent. Conversely, when the U.S. market fell by more than 4.5 percent in one month, European stocks largely tracked the decline, falling equal to 86 percent of the U.S. stocks’ drop. This challenging, difficult-to-explain, and even harder to absorb technical analysis is why some planners no longer even bother with the “math.”

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## “What Do I Show the Clients Now?”

For Alan Landay, CFP®, a sole practitioner since 1981 in Severna Park, Maryland, the great bear market and recession of 2009 is less about lessons learned than a philosophy confirmed. Landay is opposed to the typical goal-setting that many advisers fall

back on—“save these tens-of-thousands of dollars a year because you need \$2 million by the time you retire. *Terribly frustrating to clients.*” He refuses to use historical charts—“They’re worthless and too many advisers don’t explain all the ramifications of the small print.” And he wouldn’t touch a Monte Carlo simulation—“I don’t care

how many you ran, it never assumed that [General Motors] would go bankrupt. Nor would it have helped a client prepare for this year.” Oh, and he doesn’t offer his clients an “outlook.”

“We just set up a program and go. The only goal is to save and accumulate as much as possible and to reduce their tax exposure,” says Landay. “I work with my clients on the practical, not the theoretical. Forget the charts, the graphs, the history lessons, the mathematical models. I’ve factored out everything out of my control. This past year is proof that more than we thought is out of our control.”

“Go for it” may be oversimplifying; Landay does use an investing model based on the client’s risk tolerance, but it’s simple too: save 15 percent a year—7 percent in a qualified plan and 8 outside—until a client has 50 percent of one year’s income in conservative investments. The 8 percent in non-qualified investments goes into muni-bond funds and other tax-advantaged funds. “If we’re able to get the client a 5 percent return with little tax to pay, they’ll be okay,” Landay says. “I will not put a client in an investment with more risk just because they have a shorter time to retirement—or because the market is going back up.” As for the drumbeat of “modern portfolio theory failed,” Landay believes that too many planners are just all tied up in a knot about it. “Smart, left-brained people are agonizing over the Sharpe Ratio and the efficient market frontier and asking, ‘What do I show the client now?’ You don’t really have to show them anything.”

For some planners, “conservative” doesn’t adequately describe their strategy, either now or in the past. Porter Landreth, CFP®, holds firmly the conviction that a focus on bonds is a lesson that many advisers need to learn. He’s been managing a bond portfolio for his 300 clients at Asset One in Aurora, Colorado, for 28 years and says he has “dramatically” outperformed the S&P 500 for many years (and that he has the audited results to prove it).

“Every planner should be looking for the safest opportunity to make money for their

## Cross, Cautious, and Confused: What Have Consumers Learned?

The attitudes of consumers—clients or would-be clients—may reveal just some of what financial advisers have been going through. According to a study done by the Sales Quality Research Group (SQRG), client dissatisfaction with advisers is up—somewhat perversely because advisers are spending more time with clients. SQRG says that once the crisis and recession hit, the average length of a client meeting shrank by 10 minutes due to the sheer volume of clients that needed reaching out to. On the good-news front, a J.D. Power & Associates study found that 30 percent of investors consider finding a good financial adviser their paramount concern, while the percentage of investors saying that getting strong financial returns was the most important factor dropped from 24 percent to 15 percent between 2009 and 2008.

Rational or not, many investors feel as though they misplaced their trust and are not likely to return to either advisers or active participation. They are “cross, cautious, and confused,” says Clarence Hahn, the co-leader of the financial services practice at AlixPartners, a consulting firm. An AlixPartners survey found a staggering 49 percent of people who identified themselves as “previous investors” have either stopped or reduced investing; 26 percent said they had no intention of investing in the next three years. “The irony, of course, is that lost wealth can

only be rebuilt through participation in the markets,” says Hahn.

The September 2009 FPA study, *A Year After the Market Crash: How Financial Planners Are Adapting to a New World*, by contrast, indicated a high percentage of clients who’d gotten out of the market, but 85 percent of planner respondents indicated they had recently recommended that clients get back into the market or dedicate additional money to the market to take advantage of the upswing.

These three “Cs” may be reflected in other reports of consumers’ moods and attitudes. A September 2009 investor survey on investing, the capital markets, and investor confidence done by the Center for Audit Quality, which is affiliated with the American Institute of CPAs, isn’t exactly a rousing endorsement of advisers or institutions. Investors say they, themselves, do the best job of protecting their interests. Twenty-two percent believe the recession will last another two years and 25 percent feel it will last more than two years. And an August survey of 11,400 people in 16 countries, by Synovate, found 26 percent saying they would not invest in the stock market in the future. Fifty-one percent said their trust in financial institutions had declined dramatically. While a majority of planners in the FPA study agreed that there would be long-term business implications, they also reported consistent increases to their client bases.

clients going forward,” Landreth says. “I’ve made a career out of getting people out of the stock market—I usually call it nitroglycerin in a bottle—and into *managed* bonds of all stripes: corporate, munis, international, floating rates. The bond market is huge, very deep, and liquid. It’s just not sexy.” Landreth isn’t surprised that



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—William Pitney, CFP®

half the planners in the FPA survey couldn’t say “no” to whether modern portfolio theory failed: “It *has* failed. Diversification magnified clients’ losses in 2008 and 2009. And buy and hold is a disaster. Advisers need to develop disciplined and robust sell strategies. Hiding behind MPT and ‘it will get better’ is a poor service to your clients.”

### An Annual Review—Every Week

Service to clients was an inescapable fact of life in 2009—at least for planners who wanted to survive. Sixty-five percent of planners who responded to the FPA survey are spending more time and money on client communication; 45 percent are spending 10 to 19 hours per week communicating or meeting with clients, and 15 percent are spending 20 to 24 hours per week. During the worst parts of the crisis, so many clients wanted so much time from Bedda D’Angelo that it was “like an annual review with them—every week.” Serving clients—including preserving a relation-

ship or reducing their stress—also included getting a client completely out of the market against planners’ better judgment.

Alyson Ross, CFP®, J.D., relented on one client who wanted out. “I had to respect his anguish,” she says. “You can advise, but you can’t force. Interestingly, he was one of my younger clients. He eventually did a *mea culpa* and we moved on.”

Ross, a senior financial adviser with Ameriprise Financial in Richmond, Virginia, and her partners have increased the firm’s market update communications from quarterly to monthly. Mayo meets with clients in other states in person, and more frequently than in the past. Delmar Gillette, a planner in Newport News, Virginia, also was consumed with a lot of hand-holding calls, sometimes to the same clients repeatedly. He uses

“real life” anecdotes to help his clients put things in perspective about the markets and the economy: this winter won’t be like last year’s; next year’s may not resemble either of them—but spring always follows winter. “That may sound corny to some, but human beings relate to that better than they do to us saying our models failed, even those of the financial institutions.” Gillette also had to respect a client’s wishes to get out of the market—and on March 9 no less, the day before the recent big upswing began. “She was at the end of her rope,” he says.

Sometimes planners were, too.

Every planner has a test case or two, says William Pitney, CFP®, of Santa Rosa, California. His largely highly educated client base of analytical engineers, some of whom actually read every word in a prospectus, challenge him regularly in a healthy way. But it was a client whose early indications that she would be problematic—after a portfolio drop of \$100—who convinced Pitney she could no longer be a client and

that he could better use his nine years of undergraduate and graduate education in sociology and family studies to get better “fits” with his clients. He disengaged from another client because of her mistrust and complete inability to listen to and act on his recommendations.

“She wanted to outsmart me, but I’m not in competition with my clients,” Pitney says. “It was taking its toll and I didn’t want to keep taking emotional baggage home to my family.”

Pitney began using more behavioral finance tools to connect better with his clients, even asking new and existing clients to take Kolbe personality tests. The biggest benefit, says Pitney, is using what he learns for one purpose: “How can I help clients make better decisions?”

Pitney and other planners have used the troubles of the past 12 months to re-energize clients to get focused on elements of financial planning that have little to do with the market. In 2008, Pitney accelerated development of a standard “topic” planning cycle so that clients will have specific expectations each quarter: updating the plan, rebalancing portfolios, and re-examining risk tolerance in the first quarter; estate planning and beneficiary review in the second; insurance in the third; and taxes and year-end portfolio opportunities in the fourth. Bedda D’Angelo appreciates the opportunity to finish what is needed for the depth of the client engagement.

“For every client that was slow on giving me all their information and files, boy, I have it now,” D’Angelo says. “All of a sudden, they realize how important it is.” For Michael Mazzilli, it also was a great year to cover all the basics—again—such as legal documents clients need to update.

Some planners are focused on maintaining or improving the simplicity of their business model. Mayo works from a shared executive suite and needs only a laptop and a cell phone to run his business. Pitney has outsourced most portfolio management to third-party asset management programs and has pared down his universe of preferred insurance companies

to just a handful. Jamie Lapin plans to pass along to a younger planner her stack of magazines with articles about signs of the coming downturn a full 18 months before it happened—“They’ll pay more attention to that now,” she says. She also plans to re-read *The Black Swan*, a favorite book that both comforts and illuminates with its premise of highly improbable events.

### Hangin’ On to Points of Reference

Human beings are a hopeful lot; we’re also inclined to turn to our support systems to bolster our hope. Financial planners turned to colleagues down the hall or across the city; in FPA chapter meetings they commiserated, debated, and listened to guest speakers. Some fell back on past experience with financial products companies and their words of wisdom. Delmar Gillette still remembers well his first encounter with a market meltdown, on Black Monday in 1987, when the Dow Jones dropped 22.6 percent. American Funds, he says, did something simple but powerful, a lesson that sticks today: “They answered their phones and talked to us.”

Several financial planners interviewed are grateful for the support of their broker-dealer. A sometimes-contentious relationship that often involves the word “compliance,” broker-dealers stepped up to the plate with planner support. Lapin’s broker-dealer, H. Beck, has a wonderful due diligence department, she says, and she’s called on them every step of the way during the downturn for guidance on how to analyze specific investments. Lincoln Financial Group, the broker-dealer with whom Pitney is affiliated, offered weekly sessions by investment and economic specialists. Ross is impressed with the perspectives on history and patterns offered by Ted Truscott, the chief investment officer of Ameriprise Financial, her broker-dealer. “When I hit low points, his writings helped me stay calm and keep my head,” she says.

Gillette and Russo draw from the writings of Nick Murray, a long-time financial services guru, for historical lessons that

have contemporary truths. It’s the consistency of Murray’s message that serves as their touchstone—patient, disciplined, long-term equity investing in the great companies in the United States and the world, with the understanding that a bear market is always just a temporary interruption of a permanent uptrend. Murray himself has plenty of opinion to offer on the lessons that financial advisers have—or should have—learned.

“If there’s one primary lesson for advisers, it should be that a value proposition based on the illusion that you can predict the economy, forecast the markets, and select for consistently superior relative performance is a delusion at best and a lie at worst,” Murray says. “The great mistake advisers made—and that these astonishing couple of years exposed—was confusing an outlook with a philosophy. An outlook is always going to be wrong. All of life, for good and ill, is a ‘black swan’ event.”

Those with the perspective of age and experience feel comparatively lucky. For one, they’ve been here before and *believe* it when they say: the more things change the more they stay the same. They’ve been through quite a few “new normals” and “it’s different this times.” Newer, less experienced planners, on the other hand, get D’Angelo’s sympathy.

“Those not in business in 1982, a truly horrible recession, even not in 2000 when the first bear market of this century started—for them, this has to have been devastating,” D’Angelo says. “On the bright side, and this may sound strange, the chances are really good that within the next 10 years the newer planners will have the privilege of experiencing this again. Myself? I hope I’m retired before that happens. I don’t know how much more of it I can take.”



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