On Course Financial Planning

Facing the Future with Optimism and Courage

July 2019 Vectors

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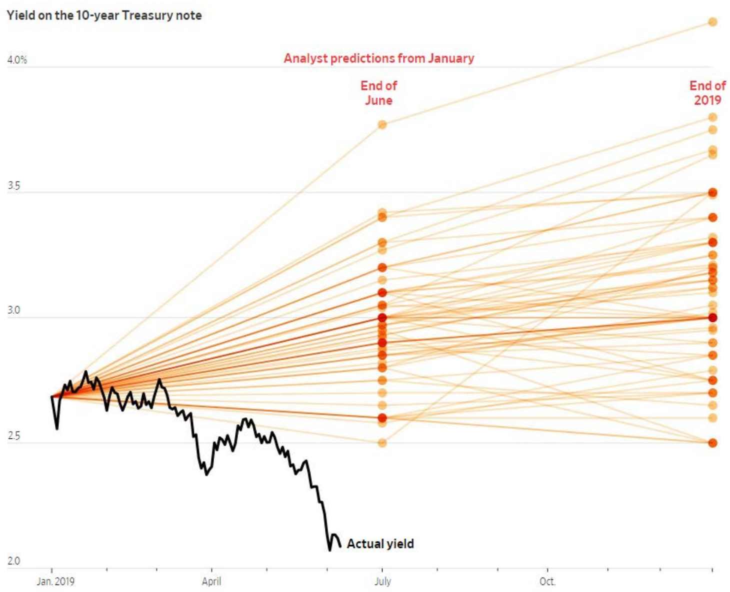
69 Busted Forecasts

Last November, the yield on the 10-year US Treasury note stood at 3.2%. This chart from the *Wall Street Journal* shows the January 2019 forecasts of 69 economists for the yield of the 10-year note at the end of June and the end of 2019. The average forecast for the end of June was about 3.0%. The actual yield was 2.0% - a 50% miss. The *Wall Street Journal* noted –*"In the U.S., a fresh scramble for U.S. government debt has driven the benchmark 10-year Treasury yield down to 2% for the first time since 2016, a situation few economists or investors foresaw a few months ago…The decline has caught nearly everyone by surprise. In January, none of the 69 economists surveyed by The Wall Street Journal predicted yields would fall below 2.5% by June."* These folks are not dumb, so how could they all have missed it by so much? It's because predicting interest rates is no easier than predicting the stock market. This is the latest, soon to be forgotten example of the folly of attempting to predict short-term price changes of any long-term financial asset. It also shows why it's foolish to base investment decisions on consensus forecasts. You can't outsmart the capital markets and they regularly extract money from investors too proud or too foolish to admit this truth. But the forecasts will continue because if any one of these economists correctly predicted the sharp decline in yield, they'd be the financial media's newest shining star. The lunacy of trying to predict the future to two decimal places never ends –*"The Journal's most recent survey of economists, published earlier this month, on average forecast 10-year yields would finish the year at 2.34%."*



Sources: WSJ Survey of Economists (predictions); Tullett Prebon (actual)

How to Be a Successful Financial Advisor

The three most important numbers in a financial advisor's life are blood pressure, cholesterol level and assets under management (AUM) - not necessarily in that order. The only way to increase AUM is to acquire new clients, especially affluent clients. So, it's not surprising that there are numerous articles in trade publications advising financial advisors how to attract affluent clients. I recently came across an article by the president of Prospective Business Solutions, a company that provides high net worth client acquisition training for financial advisors. He sets the stage by proving to his readers that he knows their secret shame – *"You attend the right events and drink in the right places. You're getting in with a wealthy crowd. But there's a problem. You feel like you don't belong (and you think they know it.) How can you send out the right signals that you are wealthy and successful?"*

He then presents ten ways to make an impression on wealthy prospective clients –

- **Always dress well.**
- **Accessories get noticed** – *"many people have great brand awareness and can spot a Rolex watch or a Montblanc pen across the room."*
- **Don't be selling**. You'll come across as desperate. *"They know what you do for a living. If you aren't pushing business, they'll conclude you must be successful."*
- **Treat everyone with respect.**
- **Always be upbeat**. *"Always smile. Find positive things to talk about."*

So far, no great revelations. However, the next five are a bit more interesting.

- **You need a favorite restaurant**. *"You will want to entertain people outside your home. Rich people do it all the time...Become a regular…The staff know you and treat you like royalty…Rich people expect the royal treatment. You were given it. Therefore, you must be rich."*
- **Pick a competition category**. It could be wine collecting or restoring classic cars. Others will see it as "your thing" and assume that your expertise in your hobby means you are also an expert at investing.
- **Choose a favorite champagne.** *"It should be a big-name French brand. You bring it to other people's houses. You order it at bars and restaurants. You bring it on picnics. People associate it with you…You are piggybacking on their branding."*
- **Own a nice car in perfect conditio**n. *"A late-model used BMW, Mercedes or Audi will probably look like your rich friends' cars."*
- **Get a country or shore house.** *"This is expensive, but it gets you out of the "world travel" expenses. You spend weekends. You commute to work from there during the summer. You become a two-house family… Many rich people do the same. People never see the place; they just hear about it."*

In summary, *"Coming across as rich isn't as tough as it sounds. It isn't cheap, but that's a barrier to entry for many of your competitors."*

Soon thereafter, I read an article proclaiming the marketing benefits of hosting a rosé wine tasting for clients that contained recommendations for the type of glasses to use and the appropriate bread, crackers and cheeses to serve. It concluded with a reminder to serve coffee to finish the evening because *"You want everyone to get home safely."* Another article noted: *"You may consider identifying the clients who are interested in out-of-the-box adventures…For example, you can host a hike with an introduction to sustainable investing…or a scuba diving lesson with a presentation on weathering market volatility. This type of event can both reinforce your authority on investing topics as well as provide unique opportunities clients will want to share with their friends."* I must admit that I fail to see the connection between scuba diving and stock prices.

In short, act rich and affluent prospects will assume that you're an investing expert. If you're just starting out on your career as a financial advisor, my recommendations of how to increase AUM would be significantly different –

- Always act in your clients' best interest. If you're an employee of a firm, putting your clients' interest ahead of your boss' demands may be the most difficult part of your job. This is a big reason behind the recent trend of advisors leaving large firms and going independent.
- Never lie by pretending to know more than you do or by presenting your opinions as facts. *"I'll have to research that and get back to you."* is a legitimate response to many questions.
- Few financial organizations find any benefit in educating financial consumers. Never take advantage of the knowledge gap that exists between yourself and your clients. The language of investing is often used to confuse more than clarify. Billions of investor dollars have been lost because financial advisors leveraged the knowledge gap for their own benefit.
- Never pretend to know what tomorrow will bring and you'll never have to apologize for being wrong.
- Be scrupulously ethical. Your ethical standards must go beyond the industry standard of "good enough". You might lose the opportunity to add AUM by taking the morally correct stance, but only temporarily.
- Never stop learning about your profession. I have sympathy for new advisers who give poor advice because they're still learning their trade. But you have a duty to your clients to know what you're talking about; not just repeating a marketing spiel.
- Study the history of markets. The world is constantly changing but people don't change. Individually and collectively we oscillate between greed and fear on an ongoing basis. There will always be booms, busts, and new companies replacing old companies that have outlived their usefulness.
- Have a long-term investment philosophy that is based on sound academic research, not forecasts. Your clients need historical perspective, not a viewpoint or an outlook. Your job is to allocate client assets so that they have the highest probability of achieving their financial goals, no matter what the future holds.
- You can't prove anything. Explain, but never argue.
- Have more interest in your clients than in their financial assets. Financial planning is more personal than financial. You must know people, their unique needs, goals, risk tolerance and time horizon before you offer them financial advice. Good financial advice is not a commodity. Never pretend that a portfolio allocation is a substitute for a financial plan. If you put AUM ahead of people, you will have a short tenure in this business.
- Never base your value proposition on investment performance because outperformance is not a financial goal. All promises or intimations of outperformance are lies. Once you've set a client's portfolio allocation, performance is beyond anyone's control, including your firm's economists and marketing department. Until you come to this realization, you're just a rookie playing with other peoples' money.
- You can make a nice living as a financial advisor by being good to people.

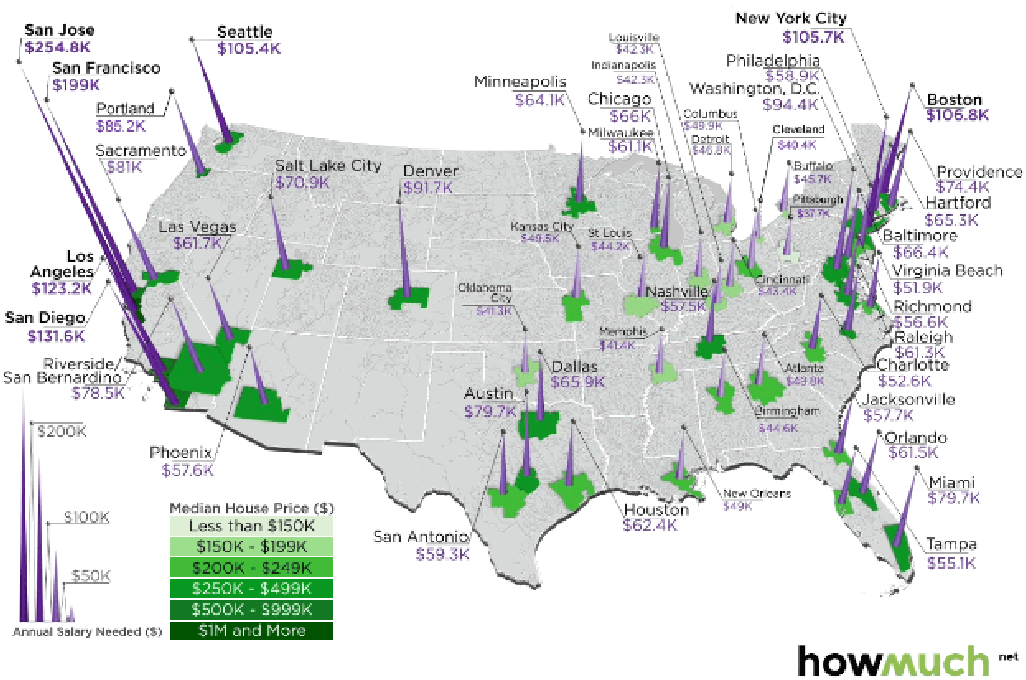
If you're seeking the services of a financial advisor, I offer this piece of advice - character counts. Advisors who present a false image of themselves have a severe character flaw, one that should eliminate them from your consideration. Unfortunately, for every advisor who pretends to be rich, there are ten who pretend to know more than they do; and believe me, I've met plenty of them. It's easy to think well of an advisor who seems successful, it's natural to think that maybe he's the smartest guy in the room. But the history of the investment business is replete with characters whose smarts exceeded their honesty, to the detriment of their clients. Keep your guard up – avoid any advisor who seems more interested in your AUM than your financial goals.

In the News

This month's useless market commentary is from Justin Wiggs, managing director of equity trading at Stifel Nicolaus - "*People are struggling to figure out where to put their money in the midst of so many unknowns.*" Note to Justin – The number of unknowns never changes because the future is unknowable - all day, every day. Too many investors fall under the influence of this type of investobabble and make portfolio changes based on someone's prediction of the unknowable.

According to the National Bureau of Economic Research, the official record keeper of recessions and economic expansions, the USA is officially in its longest economic expansion, which began in June 2009, breaking the record of 120 months of economic growth from March 1991 to March 2001. Pessimists note that this record-setting run saw GDP grow at a slower rate than previous expansions. But that might be a key to its longevity. The drumbeat of negativity — forecasts of impending recessions, market crashes and the end of the financial system as we know it — has been unrelenting the past ten years. Pessimism attracts more eyeballs, ears and clicks than optimism because we have such an aversion to losses. The ongoing negativity of the financial media might have prevented speculative excesses from building up in the economy. A study by the San Francisco Federal Reserve Bank noted that the age of an expansion has virtually no influence on the probability of entering a recession. The *Wall Street Journal* reported in June that *"Australia is enjoying its 28th straight year of growth. Canada, the U.K., Spain and Sweden had expansions that reached 15 years and beyond between the early 1990s and 2008. Without the Sept. 11, 2001 terrorist attacks, the U.S. might have, too."* My advice is to ignore forecasts about how long the current economic expansion will last, because nobody knows. It's hard to appreciate the good times when you're in the midst of them, which is why studying history is a prerequisite to gaining perspective.

As the S&P 500 reached new all-time highs this month, the reaction of most pessimistic investors wasn't pleasure, it was the latest evidence for their tortured minds that the stock market is getting ready for a big fall. After all, what goes up must come down – often quite suddenly. How common are new market highs? Even optimistic investors might be surprised to learn that in 323 of the 1,113 months from January 1926 through September 2018, the S&P 500 closed the month at a new high - 29% of the time.



This map from HowMuch.net, shows the annual salary needed to buy the median (half cost more, half cost less) home in the 50 largest U.S. metro areas. The median price for a home in the United States is about $258,000, according to the National Association of Realtors. Assuming a 20% down payment and a 4.9% 30-year fixed rate mortgage, it takes a $62,000 salary to qualify for the mortgage – including principal, interest, taxes, and insurance. The cheapest metro area is Pittsburgh. It requires a salary of $38,000 to afford the median Pittsburgh metro area home price of $142,000. The most expensive metro area is San Jose. It requires an annual salary of $255,000 to afford the median home price of $1,250,000.