INVESTMENT PLANNING

Practical Guidelines for Managing Portfolios (and Clients) Through Volatile Investment Markets

By S. Timothy Kochis

Aspiriant serves hundreds of clients in eight offices throughout the United States. Our clients are entrepreneurs, corporate executives, and accomplished professionals. We often serve as a complete "family office" and provide comprehensive planning and implementation services to all of our clients and the wealth transfer and philanthropic entities we help them create. The strategy setting and ongoing management of substantial investment portfolios is usually the central feature of our suite of services, but thoroughly coordinated with all other relevant financial planning dimensions of accomplishing our clients' goals.

Through the market downturns of 2008-2009 and again this year, we have learned some important lessons that we believe will be valuable to all client advisors.

The market devastation of a few years ago was driven heavily by the over-leverage and over-valuation of residential real estate. While leverage is at the core of the current malaise, this time, the great surprise factor is missing. For quite a long time now, all market observers have been aware of the significant sovereign debt problems in Europe and their follow-on effects for the European and domestic banking system. At home, the persistent weakness in the housing market, very high and unabating unemployment, large current deficits and very large cumulative national debt, and severe disappointment with our elected officials' inability to come together to address these concerns gives investors significant pause; many even fear a renewed actual decline in economic activity, the "double dip." Finally, as the third leg of this ugly stool, some developing markets are significantly slowing their rates of growth, withdrawing what had been the only really robust element of global growth. It is indeed very difficult to be optimistic about the near term future of investing. Why bother? Well, because of the long term.

When the global financial crisis of 2008-early 2009 occurred, clients often felt unprepared for the depth and speed of declines in investment markets that reached levels of 30 percent, or even much more. We responded, by general email communications, webinars, individual phone calls, and our routinely scheduled quarterly communications, to provide information and confirmation of our strong belief that the downturn was temporary and that strong recoveries were very likely to occur; we just could not say when. Still, the psychological shock was so great to many, even very wealthy and sophisticated clients, that we learned that we could not over-communicate. Our clients wanted to hear from us quickly, even if we did not have much new to say. They simply wanted us to reach out and contact them to assure them that we were carefully considering what we could do to help. They looked to us to be calm, aware, and still devoted to their welfare. Later, after markets had begun to recover, we convened small client conferences to learn from them what they appreciated about our responses and how we could have improved. They were very frank with us about what they liked and did not like. Their main

Mr. Kochis is President, International Ventures, Aspiriant, San Francisco, California, and is a member of the CCH Financial and Estate Planning Advisory Board.

message was that we needed to communicate as frequently and as much on a one-on-one basis as possible. Private letters or emails were much better than general communications; phone calls or meetings were much better than email.

The key messages in all of our outbound communications focused on the individual client's actual ability to withstand the losses that they had suffered. No one, of course, likes to lose any significant amount of money, but if those losses do not really jeopardize accomplishing important goals, a client's ability to be optimistic about recovery is much greater. Many had feared that their situation was much worse than it actually was. But, after our re-evaluating those objectives and the ability of even reduced resources to fulfill them, they came away, not happy, but relieved that things were not really so bad. Some even took advantage of reduced market values and added new money to their investment portfolios or even increased their risk postures. Some decided that the market volatility was too uncomfortable and either reduced their future expectations or scaled back their goals to adopt a less risky portfolio strategy. Most, however, stayed with the strategy that they had in place. And *everyone* took that opportunity to reassess their capacity for, and their comfort with, actual risk. A number concluded that their tolerance was less than they had believed it would be. And a few decided that the pain was just too great and abandoned the commitment to invest altogether. We lost more existing clients during that era than is normal for us, but we still retained over 95 percent of our client base. We also gained a larger number of even wealthier new clients. Our efforts were focused on serving those new and remaining clients well; we could not dwell on the regret over losing those few.

Communicate, frequently and in as many ways as possible, to assure clients that you remain committed to their welfare, that you are paying close attention, and that you remain confident in the wisdom of the investment strategies you have helped them to adopt.

The current market declines and frightening volatility in 2011 seem to be a betrayal of the "good behavior" that most clients undertook barely two years earlier: that is, they carefully recalibrated their portfolio strategies or remained perseverant with the strategies already in place. This was initially rewarded by significant and mostly steady recoveries in values. But, since early this year, steep declines once again threaten clients' actual financial resources and sharp volatility assaults their peace of mind. For many, the psychological wounds had not yet healed and they have now been painfully reopened. Still, most clients learned from that earlier experience and are now reasonably relaxed, both in their belief in eventually good results and in our commitment and ability to help them achieve that. Nevertheless, some clients complain that we're not doing enough to protect them from losses or that we aren't able to foresee trouble in order to step aside when it seems so obviously right to do so (after the fact).

So, the most important responses, again this time, are to:

- Communicate, frequently and in as many ways as possible, to assure clients that you remain committed to their welfare, that you are paying close attention, and that you remain confident in the wisdom of the investment strategies you have helped them to adopt;
- Demonstrate that you are eager to help them thoroughly re-evaluate the adequacy of their resources for their desired objectives at levels of risk that they are willing to accept. That re-evaluation process has value in other ways as well. The act of recalibrating the long range match-up of resources and goals responds

to the client's perceived need to "do SOMETHING!"; and, finally,

- Elucidate, that, though painful, remaining committed to the current strategy may be essential to accomplishing important objectives; abandoning the strategy now may seriously jeopardize long range success.

Importantly, these messages cannot be just about the need for psychological comfort. While that is a deeply essential component, the central message must be founded on the logic of how investment markets must behave over time, that is, to reward risk and to reflect the actual performance of the underlying world economy. If your clients will accept a fundamental belief that humans will continue to create value, and if they are prepared to be broadly diversified, and if they have the benefit of time, they must reach the conclusion that they will be rewarded for taking short- term risk. History is also an important guide. Despite the apparently rapid return of a deeply negative investment experience, longer term history shows that investment markets do, ultimately, outperform the alternative of not being invested. It is not really that different this time.

So, how can we, as advisors, better prepare for these short-term threats. First, we should not pretend that we can foresee the near term future; we cannot. Attempts at "timing" investment markets are almost certain to be expensive and are very likely to fail. Some, very few, may be lucky (for a while), but there is no predictive value in that initial good fortune. So, we are left with a reliance on matching the necessary logic and the consistently demonstrated history of investment markets with the desires, goals, tolerances, and time-frames of our individual clients. Carefully guiding them through those choices and thoroughly educating them about the opportunities and risks is the fundamental responsibility of the advisory professions. That fundamental service also provides the best assurances both that the client actually achieves desired objectives and perseveres when the process gets very uncomfortable.

Is there opportunity here? We think so. There are many current investors who are now struggling with poor guidance or no guidance at all. Moreover, quite a few are too frightened to even begin to invest. We, as caring and well-informed advisors, have the necessary expertise to identify wise choices, and we provide the understanding and motivation to help clients actually implement and then remain committed to those wise choices. There are many people looking for what you have to offer, either directly or through related, qualified advisors. So, as "untimely" as it may now seem, this is a very appropriate time to ask your current clients for referrals. Likewise, it is the time to refer clients to those other professionals with the investment skills, experience and wisdom to genuinely assist where your skills are not on point. Or, if your skills are on point, it would be appropriate for you to ask related professional service providers to send you their frustrated or "lost" investors.