Glass Houses? An Open Letter to Bob Veres

By Clark M. Blackman II
March 31, 2009

Advisor Perspectives welcomes guest contributions. The views presented here do not necessarily represent those of Advisor Perspectives

Bob, you once again demonstrate a wisdom and insight that is too frequently lacking in the investment advisory industry. Thank you for cogently summarizing the realities of the challenges that advisors have faced in the onslaught of a truly unprecedented downward slide in world wide markets. Having said that, I do have a bone to pick with you regarding your article, "Casting No Stones," in Advisor Perspectives on March 10, 2009.

I have been in the financial planning and investment business in one form or another for 29 years. I have seen a lot and learned much along the way. You indicated in your article that the advisor who changed strategies as the market fell was more "sophisticated" than the advisor who stayed committed to their original strategy. I propose that your "more sophisticated" advisor, who succumbed to the fear of the day and made radical changes to client portfolios after steep drops in market prices, is the less sophisticated of the two major groups of advisors, not the other way around.

I believe the more sophisticated group consists of those who stayed calm and rational in the face of a stampeding herd spooked by fears that things could only get worse. This group understands that at the end of any given day, all the information available has been factored into the markets. Like water flowing downhill, information (most especially bad news) finds its way into pricing just as quickly as it possibly can. It doesn't take days or weeks for the market to reflect the latest news…it takes minutes.

Sophisticated advisors rightfully realize that, as long as their strategy allowed for a long term holding period (i.e. clients have plenty of liquidity or available cash flow to last a number of years in a down market), gambling on a continuing stream of new bad news could very well be in their clients' *worst* interest. A decision to stay with an investment strategy is as much an overt and assertive action (maybe more so) as is the decision to run for the hills along with the stampeding herd.

I save many articles, Wall Street Journals and other analyses as a matter of course, and during times like these I find it useful to go back to them to demonstrate how, at the time, things were not nearly as clear as they would seem to a Monday morning quarterback. Throughout this deteriorating economy and bear market there have been

© Copyright 2009, Advisor Perspectives, Inc. All rights reserved.

glimmers of hope and reasons for optimism throughout. This is typical of every bear market. A bear market will end, on average, three to six months before the economy turns, so it is virtually impossible to know when you have reached the market bottom. This of course is the next trick to pull off for advisors who fled the market.

Reading your article, I found it somewhat disconcerting that at least some of the advisors you talked to who had made radical changes are of a mind that those who did not see fit to do as they did are now somehow unfit to call themselves advisors. This demonstrates a certain hubris that these folks will likely regret. These advisors live in particularly fragile glass houses and their stone throwing is really not in their better long term interest.

Investors, and advisors, need to remember that for every genius selling, there is another genius buying! So a "rational" decision to make long term strategic changes that are not based on fear must be based on information that the market does not yet have (Dr. Nassim Taleb's *The Black Swan* is excellent foundational reading for all new advisors). Since the decision to sell in the face of potentially declining markets is based on events still to happen, the advisor is making a bet that there will be more negative news (more than one would otherwise expect given the news already in play) than positive news. And as Dr. Taleb so eloquently explains, it is necessarily the *unexpected* information that moves markets.

So the advisor who made radical changes is either willing to gamble on a strategic change *after* losses have already been incurred, or he truly believes he knows better than everyone else (i.e. "the market") what the information of the day means longer term. And let's not even broach the subject of what alternatives these advisors may have suggested to their clients (and we will save for another time certain fiduciary issues that might arise as a result if those potentially inadequately diversified alternatives don't turn out to be the absolute best place to be in the storm). Footnote here: a survey in Investment News this week indicates that two thirds of advisors believe inflation will characterize the market over the next 12 months, while the other one third believe it will be deflation. The difference between the two, in terms of *best* strategy, is huge. I'd hate to be the one guessing wrong on that prediction!

Market timing is a gamble, no matter how you cut it. And when one gambles and is correct, that doesn't make the gambler a genius. It makes him lucky! We all know the person who has taken an enormous gamble at one time or another and we shook our heads thinking "what a fool". Then luck smiled on them and their ignorance and chutzpah made them rich. Did fate make them a genius? Hardly.

To put this another way, today (March 24) a long time client of mine who predicted the market bottom on March 9 when he called to wish me a happy birthday, made the following statement as I kiddingly praised him for his prescience: "I learned a long time ago, if you shoot from the middle of the floor and make it, don't be fool enough to bet

© Copyright 2009, Advisor Perspectives, Inc. All rights reserved.

you can do it again". Anyone who plays basketball will understand the wisdom of that layman's comment.

I would not want to face the challenge ahead of that "prescient" advisor whose clients now believe his value is in his ability to forecast future economic and market turns. When even so august and venerable an economist as John Kenneth Galbraith believes "*the only function of economic forecasting is to make astrology look respectable*," these advisors might find themselves relegated to reading palms for a living when their clients discover that once lucky doesn't easily translate into forever smart.

Until the market once again makes fools of the market timers, I am afraid we are going to continue to hear a chorus of voices from the market timing, momentum following, gold buying, technical chartist believing crowd that a long term strategic policy no longer makes sense and that timing is the only intelligent, wise thing to do for clients. And Bob, I only hope you use your inestimable clout to be a voice of reason for those in the advice giving business struggling with this issue. Eventually, these new "market timers" will find that they are not nearly as good at the game as they say they are right now.

I close with one bit of advice for the advisor who "knew" things were only going to get worse – don't believe your own press. Consider yourself lucky for getting out before further damage was done. But if you believe you are going to call the bottom and get your clients back in at just the right time, remember that lightening isn't likely to strike the same spot twice. Be wise. Accept your good fortune, communicate the same to your clients and prospects, and perhaps when you get caught on the wrong side of fortune next time around they'll forgive you. And ask yourself this: Are we experiencing a "dead cat bounce" or did your clients just miss the first 22% run up in the market? I don't know and I suspect you don't either.

Clark M. Blackman II, MA, CFA, CPA/PFS, CIMA™, CFP™, AIF™ is President/CEO of Alpha Wealth Strategies, LLC, a Kingwood, TX-based advisory firm.

www.advisorperspectives.com

For a free subscription to the Advisor Perspectives newsletter, visit:
http://www.advisorperspectives.com/subscribers/subscribe.php

© Copyright 2009, Advisor Perspectives, Inc. All rights reserved.