



## **The Information Risk Premium: A New Danger to Client Portfolios**

By Bob Veres  
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When you step back and look at the investment landscape, it is helpful to ask yourself if anything really *is* different this time, to try to determine what has changed.

The usual answers point to recent return gyrations: the tech bubble's spectacular burst ten years ago, the near-death experience of global capitalism in 2008-2009. But the truth is, we've seen all this before in one form or another.

Michael Aronstein, who manages the Marketfield Fund, offers an interestingly different take on what is fundamentally different today. In his presentation at the NAPFA Practice Management & Investments (PMI) Conference in San Diego, he connected two dots that most of us are aware of intuitively, but may not have consciously considered. He says that the primary challenge for investment advisors, financial planners and money managers today, which is different from the challenges you faced in the past, is the sheer amount of attention that investors are now able to pay to the ups and downs in their portfolios.

"In the last 15 years," he said, "we have moved from an era where people who were not in the business would check stock quotes, if at all, in the morning when they got their newspaper. Sometimes, you would listen to a radio program on your way home from work, and it might tell you where the Dow Jones Industrial Average closed."

Compare that with today, when an investment client might have a running ticker at the bottom of his or her computer screen, or a portrait of the investment portfolio continuously updating its various components and arriving at new values every 15 minutes. At the same time, news, information and even fundamental analysis might be flowing into the client's brain through various sources. "Regarding the economy and its various indicators, there are probably ten thousand data points that we could be looking at in real time," Aronstein continued. "Combine that with hundreds and hundreds of opinions being thrown around as important every day, and it is a formula for driving everybody insane – and I think that really is what is happening to the retail investing public."

Put in its simplest terms, your clients are being driven to an unbalanced mental state by the sheer amount of information and opinions that are piling into their awareness at



increasing speed, and nobody has a vested interest in telling them that paying attention is highly unlikely to improve their investing lives, and may well be sabotaging their returns.

In fact, the incentives are exactly the reverse. Aronstein pointed out that it has become a pretty good business to give out doomsday information and frighten investors, and a lot of people have become pretty good at it. "It is rare to spend a day watching CNBC or any of the other financial reality programs," he said, "and not hear somebody come out with the most disastrous, frightening, extreme forecast about what is going on in the world and in peoples' portfolios."

That, in itself, helps us get a better handle on this new era of persistent client anxiety. It may also help explain why so many *advisors* are so anxious about their clients' financial well-being even as the global economy continues its slow recovery. In passing, Aronstein noted that professional portfolio managers, who spend their lives reading the financial tea leaves, are becoming increasingly overwhelmed trying to identify the signal buried in the increasingly deafening noise.

This trend toward more (and less helpful) information also helps explain two other, related phenomena. First, risk assets like stocks, which tend to be liquid and priced every second, become increasingly unattractive in an environment where there is a negative or confusing spin on their every movement. Who wants to own something which increasingly gives you heartburn and insomnia? Aronstein speculates that this confusion/heartburn factor might make risk assets more attractively priced than their fundamentals would justify, raising future returns the same way value stocks enjoy return advantages over sexier growth companies: they are less attractive to the average investor.

On a related note, Aronstein noted that the PMI conference exhibit hall has undergone a little-noticed shift in terms of its exhibitors. In the past, you saw booths with traditional mutual fund organizations that take a buy-and-hold philosophy, hewing closely to Morningstar style boxes. Today, more than half of the exhibitors were offering less liquid investment opportunities: long/short vehicles like Aronstein's Marketfield fund, real estate, direct participation in mortgages, and various investments involving bonds, either directly or indirectly.

What do the products of these new exhibitors have in common? They aren't traded every day, which means there is no way to watch them change in value in real time, and the market commentators aren't talking about them or offering doomsday scenarios before the commercial break. Look for these products to proliferate, and for many advisors to offer them to their clients, not necessarily because they believe the new less-liquid products offer better returns, but because they provide a way of reducing stress in the advisor/client relationship.



It would be easy to say that market reality shows (a wonderful term) or financial pornography represent a scourge on the investing world. Of *course* they are unhelpful. Of *course* the moment-by-moment market movements and most of the data and opinions are of less than zero value to your investing clients.

But the important thing here is for you, the advisor and professional, to recognize that a new risk factor has emerged in the investment marketplace, and to help counteract it with your clients. Just as you might help clients live with the decision to overweight value and small cap stocks in their portfolios, now that you're aware of an emerging "information risk premium," you have another issue to help clients address and live with. To the extent that you can help them tolerate these increasingly anxiety-producing assets while others cannot, you will probably tend to get better returns for your clients' ultimate retirement.

And you might even help them get their lives back.

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