L U L L A B Y

The Financial Markets Tease Us Back to Complacency

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Lullaby Part 1: We're Only Human

The year 2008 was a tremendous wake-up call for so many of us. For the normal business owner and C-Level executive, the economic downturn proved to be an event with permanent ramifications. "The New Normal" has brought an entirely new meaning to the idea of right-sizing and has cost many people their jobs simply so businesses could survive.

For the most part credit has evaporated, leaving business owners unable to stay the path previously traveled. For those who still have credit available, the valuation of the underlying asset has evaporated, along with the ability to reinvest in the business. What's worse is that human nature leads us to focus on only so many things at once, so retirement accounts and rainy-day funds are largely ignored, and for the most part, merely a shadow of what they once were. For those who actually paid attention to these accounts while still navigating the uncharted path ahead for their companies, the shock and uncertainty created situations where many simply reacted by changing their portfolios without thinking of the impact it would have.

As markets moved in a way that lead to the impression of recovery, those who made changes in the down-turn are again making changes with the hope that things will be okay; perhaps retirement goals will only be pushed back five years instead of ten. Today's stock market is creating a scenario where we are being lulled back into the basic instincts that cause investors to buy high and sell low. Make no mistake; there are still sizable dangers that lurk ahead. The question is at what point do we stop acting like it's the same old song and dance?

As investors, we want to believe that we can figure out where the market is headed at any given time. We are drawn to the flashing lights and bold promises of a "sure thing". Unfortunately we are not talking about a weekend in Vegas, but instead about the daily distractions we see all around us in the media. Whether it's the scrolling ticker on CNBC, the commercial touting the next great investment, or the blog our friends told us to subscribe to that's telling us "now is the time to…", we want all the financial successes we deserve, and we want to believe we can have them simply by paying attention to the information around us.

It's this behavior that lead to the findings in the study titled "The Cost of Active Investing" by Kenneth R. French, a finance professor at Dartmouth. In his study, Dr. French tells us that investors spend around $100 billion per year trying to beat the stock market. Even worse, those most prone to chase these returns are the very business owners and C-Level executives that are already suffering in this economy.

These are the people that are accustomed to making decisions in business that have a direct impact on the success of the enterprise itself. When they make a mistake, the good ones learn, adjust, and come out ahead of the pack. Instead, markets are not so kind and it seems the more we learn, the less we actually know. It is a nearly impossible change in mindset for the successful business owner or executive to make. So where does that leave us?

Lullaby Part 2: Pressure

Enter 2009. We experienced a classic example of how markets behave and why we can't figure them out. As the market began to recover losses from the credit crisis, nobody believed there was any reason for optimism. At the beginning of the year, stocks like General Electric were trading at unbelievable levels and economic news remained bleak. In a short time, we have seen the market make gains of over 35% from the lows, yet just before the rally the media was filled with comments such as:

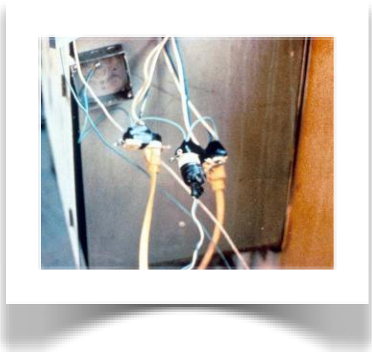
"The economy is still declining. Credit isn't coming back. Unemployment is rising, and we are seeing a much less robust consumer. I think the market at some point is going to give back a large portion of these gains." —E.S. Browing

"Is the Bull Run Pulling Up Lame?" Wall Street Journal, June 22, 2009 - Michael Farr, president of Farr, Miller & Washington.

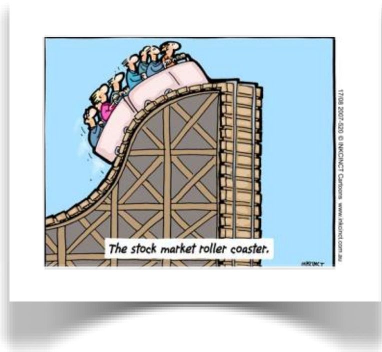
"The US economy appears doomed to enter an enduring episode of unimpressive growth." — David J. Lynch, "US May Face Years of Sluggish Growth," USA Today, May 8, 2009.

Unfortunately, herein lies the danger: Mr. Browning and Mr. Lynch were right.

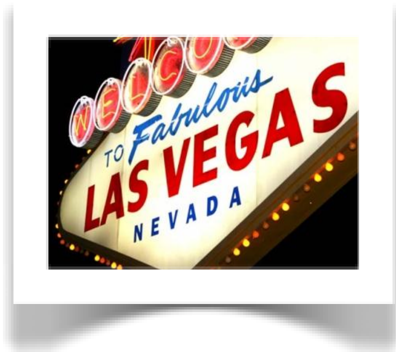
Going into the fourth quarter, many high-earning executives were subject to further lay-offs. The business owner, left with no other options, closed up shop and waved the white flag. When things are bad, we like to point a lot of fingers and yell at the top of our lungs: "Why didn't anybody see this coming?" Conversely when things have a sense of euphoria, even when we are waiting for the other shoe to drop, we don't think much of it. But why does this matter?



Successful Investor?



A bumpy and unpredictable ride



7 the hard way?

We are not wired correctly to be successful investors. We seem to thrive on buying and selling based on emotion rather than taking a prudent course of action. The problem is that the financial services industry is wired just as poorly as the investors it serves. Some of the most irresponsible people in these uncertain times are the same professionals we turn to for help. However you must understand that it is through no fault of their own.

In general, the industry has responded to investors' demands to know what's happening next. Some professionals make bets, hoping to make a career out of being right, without regard for the consumer should they be wrong. Other professionals are simply trying to recover their clients' (and their own) lost fortunes by taking on more risk than would otherwise be prudent. Many advisors have begun taking a more conservative approach in the face of the "new normal", however, this move came after the fact, and their clients will never have a chance of participating in the upside markets eventually provide. The pressure is as great on the advisor as it is on the investor.

With a temporarily good market lulling us back to complacency, the desire to make portfolio adjustments, or take the serious look at things most investors need, is once again being put on the back-burner as business owners and executives turn back to focusing 100% of their energy on the survival of the company. But what can one really do anyway?

<u>Lullaby Part 3: You May Be Right</u>

Most investors (especially business owners and executives) allow themselves to take advice based solely on returns, or at least the hope of those returns. But if one were to momentarily step back and evaluate what they are trying to accomplish, one could expect to see a misalignment in values. The mistake most advisors make is to never ask their clients what is important to them as a person.

When (if ever) has your advisor asked you what money means to you, and what it is that you hope to accomplish with it? Do you want to care for your family and transfer great wealth to the next generation? Do you want to use it to show your success? To become a mogul? Is it prestige? Power? Your answer will never be wrong, but the question does need to be asked. Looking at your future does not end with an asset allocation; that's merely the beginning.

If your advisor does not understand who you are, they cannot aid you in a direction that works for *you*. Financial success is a full time job. It requires a consultative team of experts constantly looking out for your specific goals. It requires staying awake at the wheel. It is not okay to ignore the issues in front of you; those will not go away. Complacency won't kill you; however it won't allow you to reach your personal financial goals either.

Business owners and executives need to understand that identifying what money means to them is just as important as identifying why they are in business in the first place. It cannot be stated strongly enough that a person *must* understand that they are successful because of what is known to them, and that it is *necessary* to delegate to others what is not. Successful Wealth Managers are just that, because they recognize the importance of setting their ego aside. We cannot know everything, which is why the only approach that should be acceptable to you is one where your advisor has a collaborative team of experts who are the best in their fields. Your team needs to include not only an investment consultant, but also highly regarded professionals in tax, estate, and insurance matters. Your Wealth Manager's job is to bring these minds together and work as a team to help you accomplish everything that is important to you.

Today's world will not allow you to close your eyes. Questions cannot be saved for another day. Our economy remains unstable and there are many, many hazards that still lie in front of us. Investors of all types need to have a game plan that is based on the values and goals held most dear to them. As we most likely face new lay-offs and challenges, we need to have a steady hand guiding our wealth and adjusting it accordingly. Portfolios should be built in such a way that market fluctuations do not necessitate hurried responses. Tax and estate issues must be constantly monitored, as the current environment can render the best of plans irrelevant. Insurance needs to be solidly in place and performing as designed.

Economies expand and contract. It's a simple fact of how they work. While this fire has already been burning long before we understood the significance of its impact, we *can* contain it and even work with it to turn our challenges into victories.