Chapter 5

How Does This Affect Me?

"You did what you knew how to do, and when you knew better, you did better."

—Maya Angelou, poet and educator

Regardless of whom you've worked with in the past, you know that market movements change and mutate over time. Investment strategies once considered conservative may now seem aggressive, and vice versa. It may seem ironic that, as a revolutionary investor, your best bet when it comes to investing is to stick to a discipline with well-thought-out rules. It's important to have a dynamic rules-based investment process that adapts to different market environments and proves that sticking to the game plan, in all actuality, is the best game plan. It's up to each individual investor, however, to discover which plan is right for them.

My goal as a portfolio manager and educator is to inspire confidence in investors by teaching them to focus on the process and the achievement of lifelong results. You already know that short-term performance, as pushed by Wall Street firms, is more about sales than achieving lifelong results. The markets and portfolio-management strategies are ever changing, and thus no single investment style works in all market environments.

I was having lunch with a client, a woman who was passionate about charitable giving. In the past, she had a bad experience with the standardized investment approaches typical of Wall Street.

She was used to living on an emotional rollercoaster, watching the market swing up and down, and worrying that she wouldn't have enough money for her expenses, let alone her giving. After lunch, we reviewed her portfolio. During the prior quarter the market had fallen about 7 percent. Her portfolio was down about 4 percent. Free from fear and focused on the long term, she looked at the dip in the market and simply said, "It's just a fluctuation."

I knew how significant a step that was for her because of her previous experience. With some financial education, she knew that her portfolio-management parameters were being followed. The peace of mind that could only come from understanding her investment process gave her the confidence to continue to make a difference in the world through her giving. Now she can focus on living her purpose and passion, confident that her customized portfolio will serve her well in the long run.

Today we focus on the most efficient investment *process*. It's a way of adhering to a disciplined approach. The key to leading a prosperous life in every sense is finding the right approach that works for you, one that's custom-built with your vision of an optimal tomorrow in mind. With the myriad of "investment professionals" out there and the old practices of Wall Street still highly commercialized, finding the right approach can seem like the modern version of the needle in the haystack. Taking ownership of your financial decisions is up to you, but as you begin to understand and embrace the investor revolution, you may find the time is right to explore options beyond the traditional Wall Street methods.

Financial Planning: A Step in the Right Direction

One day in 1979, my monthly copy of *Registered Representative* magazine arrived in the mail. The cover showed a man in a business suit, his open shirt revealing a Superman-type outfit with the letters CFP® emblazoned across the chest. Inside, an article described a brand-new kind of advisor: a Certified Financial Planner™. This highly trained professional helps clients tackle their most important issues—areas like estate planning, insurance needs, retirement goals, investment planning, and more. Intrigued, I became a CFP and changed jobs to work for a major Wall Street firm as a regional financial planning director, handling financial planning for some of the firm's clients with the highest net worth—for a very high fee. The process was exhaustive for both parties. It was mostly a left-brain activity with lots of numbers and projections. The financial plan was more than 200 pages long. The counseling was good, but the process was much more about the reports and investment products than about coaching and getting ongoing results. As a few years passed, I learned that although financial planning has many benefits, it doesn't always achieve its intended results. The model contains three inherent flaws:

1. *Most financial planners give investment advice, but very few have investment credentials.* This means that few of them have professional designations in security analysis or portfolio management. Although there are some excellent planners who provide high-quality service, most focus on gathering financial data and producing a one-time, written plan containing future projections.

2. *The fee structure tends to put more emphasis on the plan and less on the counseling.* Planners generally charge a flat fee, a fee based on net worth, or an hourly fee. In most cases, planners put more emphasis on the planning process and less on financial coaching, client education, or counseling; this is partly due to the one-time, fee-for-plan business model. Some planners are fee- and commission-based, a model that causes them to focus more on implementing the part of the plan that requires buying products and less on non-commission-generating activities. Once the plan is done, there's no incentive to help you to stick to it.

3. *Financial planners typically refer portfolio-management duties to an investment-management firm or mutual fund.* The planner often charges a quarterly fee to "manage the managers," which means the client ends

up paying layers of fees—often to other divisions of the same large company. In many cases, the planner doesn't have the expertise or specialized designations to justify the additional costs. With rare exceptions, the referred investment-management firm or fund manager isn't apprised of the client's personal objectives, tax concerns, or financial plan, resulting in a lack of coordination between the plan and the actual investment management.

Financial planner: A generalist who helps individuals and corporations meet their long-term financial objectives by analyzing the client's status and setting a program to achieve those goals.

Certified Financial Planner™ (CFP®): A financial advisor who takes extensive exams in the areas of financial planning, taxes, insurance, estate planning, and retirement and also completes continuing education programs each year to maintain certification status.

Furthermore, any financial advisor can call himself or herself a financial planner. Two certifications are available: Certified Financial Planner and Chartered Financial Consultant. The former is the more rigorous program. However, there are no parameters guiding the requirements to provide certain services or charge certain fees.

One client, Jim, described an experience that illustrates some of the drawbacks inherent in financial planning. When Jim's wife decided to accept an early retirement offer, the couple had some decisions to make about the severance package she received. They consulted a financial planner who recommended that they invest in mutual funds.

Jim described the process this way: "Basically, it forced us to gather all our information in one location, and it forced us to look at our income, expenses, and tax liabilities, but that was something we could have done on our own. We never saw it as any kind of strategy. There was no real direction about what we should do to maximize income or minimize taxes. We had several accounts in several different places, but there was never any coordinated review of all our assets. It was more of an organizational tool for information gathering.

"With the financial planners," Jim continued, "we really didn't have any education. They picked certain mutual funds, but I had to ask for information about the stocks that the mutual funds invested in. They would have been perfectly comfortable just telling me what mutual funds they were going to invest in, and then I was supposed to sit back and watch what happened."

As Jim discovered, a typical financial planner attempts to predict whether you'll reach your investment objectives at a certain age, based on projected rates of return and inflation. "Of course, none of those things panned out," Jim observed, "because the rate of return didn't follow their projections, and there was no follow-up."

What Jim didn't get was any sort of meaningful counseling on how to create a plan based on his and his wife's life goals. They didn't strategically match their plan to where they wanted to be, and without that connection, they didn't stay on track. The planner was constrained by a business model—a one-time, fee-for-plan with no counseling on anything to do with Jim's life—which was more to blame for the planner's lack of follow-up than the planner's skills. Jim's poor investment results were also partly due to the fact that the planner wasn't a portfolio manager.

Investors with serious money—those with good savings plans or good retirement packages and those who have been smart about growing their nest eggs—have tried financial planning and ended up with nicely bound plans that were only partially implemented and, in many ways due to our dynamic lives, were obsolete shortly after delivery. Or they dealt with salespeople whose primary objective was to sell them more products. Jim and his wife even tried managing their investments themselves through discount brokerages that cost less but lacked the extensive high-level advice required by individuals with high net worth.

Chartered Financial Consultant (ChFC): A financial professional who has completed a course which includes the courses for CFP certification and builds on that knowledge with classes in estate, retirement, and in-depth financial planning applications. Certification requires three years of full-time business experience and continuing education.

The Magic Number Myth

A lot of people sit down with financial planners and hear about a number. This number is supposed to be the amount of money you need to retire on and be secure in your future. The financial planners work through a complicated formula to help you figure out your own number based on income, age, and when you want to retire, but they fail to take into account the fact that retirement looks different for everyone. No one number works for any and all investors.

Some years ago, a couple I know—Ken and Janet—walked into an office with a sign above the door that promoted the professionals inside as brokers and financial planners. Ken and Janet sat down to speak with a financial planner who immediately asked what their objective was. The couple, who were both successful professionals, had always been the types to plan, and they said they'd like to retire in 10 years.

"That's interesting," said the planner. "How much money do you spend now?"

The couple replied that their typical spending was around $10,000 a month. The planner used this information to begin calculating the amount of assets Ken and Janet would need to accumulate before they could retire. Then, the planner started running through projections, figuring in how many assets Ken and Janet had already accumulated, which tax bracket they were in, the inflation rate, and numerous other variables, until he came up with a solid figure. The planner's approach involved many calculations, numbers, and projections.

"The bottom line," said the planner, "is you're going to have to save $5,000 a month in addition to your existing portfolio to be able to retire in 10 years."

Ken and Janet took the advice and followed it for a while, tucking away exactly $5,000 each month. That figure started to cause some discomfort, so gradually they strayed from saving exactly that much. Eventually, they stopped saving all together and became frustrated.

They began to look elsewhere for advice, eventually contacting a personal wealth coach to help counsel them through the process. "We want to retire in 10 years," said Ken to the personal wealth coach, "and we were told we have to save $5,000 a month to get there. It's binding us financially, and we can't motivate ourselves to do it any longer."

The personal wealth coach asked the frustrated couple, "What does retirement look like to you?" They thought about it and replied that retirement involved lying in a lounge chair on the beach, listening to crashing waves. Not discounting the couple's retirement vision, the personal wealth coach asked if that was what they wanted to do for the rest of their lives. They said no. The coach asked if perhaps they should focus on their passions, which could lead to even greater fulfillment.

Personal wealth coach: A financial professional who helps people envision, monitor, and achieve maximum fulfillment from both their tangible and intangible wealth. The coach accomplishes these important goals by focusing on two key components: financial/investment services and personal life issues.

Ken responded that his passion was woodworking. Janet was interested in buying and selling antiques. Before long, they began the process of figuring out how Ken and Janet could do more than retire; they drafted a plan that allowed them the financial capability to graduate from their professional lives into work that involved their true passions—in this case, a small woodworking shop built onto their home and consignment space in a local antiques shop. They worked through the process based on their vision of what would follow their working lives and left the experience with a far more alluring outlook on their future than endless months of tucking money away.

Ken and Janet were urged not to focus on building a retirement nest egg, but to think of ways in which their passions might become a profitable goal to aim toward. The techniques and approaches of a personal wealth coach usually leave clients surprised with themselves and not frustrated by their impending circumstances.

Most investors are curious to know the exact number it will take so that they can consider themselves financially independent. Later in this book, as we begin to investigate probabilities of returns, you'll learn that the number question is extremely difficult to answer. As we revolutionary boomers begin to consider retirement, we find that we're dealing with a different time than our parents experienced; their income was predictable, and they were more likely to bank their livelihoods on pension funds, profit-sharing plans, and Social Security. They were also more likely to retire to leisure and live a shorter life. Finding their number was a much easier process, but for us there are so many different variables that it's hard to define an exact number that will financially cushion us as we age. In the case of Ken and Janet, their financial planner saw their options as saving money and growing it by investing. The financial planner never looked at other potential sources of income in addition to their investment portfolio. A financial planner couldn't look toward the future to see Ken's love of woodworking translating to a small shop where he repairs and refinishes antiques that Janet resells in her profitable antiques business.

Investment Management Consultants: Not Quite Right Either

You've now begun to understand the need for a creative or revolutionary model and to see that many traditional approaches may not be the best solution to help you reach your future goals.

As you explore your options, you'll most likely encounter investment management consultants. These advisors combine several style-specific investment managers or mutual funds of certain styles for each of their clients. Consultants have limited interaction and contact with these style-specific investment managers, and over time, they switch style-specific managers to maintain what they hope is an optimal blend of different styles. Investment management consulting puts the financial advisor in more of a counseling role after the process has begun. The investment management consultant may be able to give objective advice and protect the investor from the psychological risk of circumventing the process.

Investment management consultant: A financial advisor who typically structures a client's portfolio using outside money managers/brokers or mutual funds. Such a person is sometimes called a "manager of the managers" or the manager of a broker consults program.

Stockbroker or broker: An agent (typically a registered representative of a NYSE firm) who charges a commission for executing buy and sell orders submitted by an investor. A broker is prohibited from charging a fee for advice while trading.

There are some benefits to combining different investment management styles and managers. However, investment management consulting isn't without its flaws. These simple bullet points are a good summary of investment management consultant flaws you should keep in mind:

- *Few investment management consultants have ever acted as portfolio managers,* so they're making recommendations about a discipline they've never practiced. Their process generally isn't dynamic enough to adjust standardized managers to market conditions. They also don't address changing market volatility over time.

- *They typically base their recommendations on past performance* and correlation among the managers over too short of a period. Unfortunately, today's best-performing style-specific managers are often the worst-performing managers in the future (because their specific styles go in and out of favor). It takes many years to generate risk and performance data that has any meaningful statistical significance.
- *They choose style-specific institutional money managers who tend to carry many stocks.* The result: The client ends up with hundreds (or, in the case of mutual funds, thousands) of individual stock positions. Because the money managers don't communicate with each other, the client gets cross-ownership (for example, three different managers buying IBM) and uncoordinated changes in asset allocation and weighting.
- *They put a great deal of emphasis on measuring the various managers against market indices.* Most of their reporting is on a quarterly basis. Measuring performance over short-term periods, as anywhere from one quarter to a few years, has no statistical significance and creates a great deal of emotional or psychological risk for the client/investor, which may be the biggest risk of all.
- *Because the money managers own so many stocks, their stock-picking ability is watered down.* Their performance tends to be highly correlated with the style or index they use as a benchmark (such as large-cap growth, mid-cap value, contrarian, and so on).
- *When a consultant changes investment managers, it's usually due to underperformance,* which normally results less from the manager's decision-making process than his style going out of favor. Many times, by the time the manager is changed, the style comes back into favor.

- *Hiring and firing style-specific managers can be expensive.* Liquidating your entire portfolio and buying new securities from a new manager can lead to significant tax consequences and shifts in allocation. When you add all the transaction costs, the impact costs of trades in the market, the consultant's fee, and the manager's fee, you can see why it becomes difficult to receive financial value. Often an investment management consultant's program can cost twice what it would cost to utilize a portfolio manager.

Certified Investment Management Consultant (CIMC): An investment professional who has completed extensive course work and passed NASD-proctored examinations for Levels I and II of the Institute for Certified Investment Management Consultants' course. The CIMC must also meet requirements related to experience in consulting and managed accounts, adhere to a code of ethics, and meet continuing education requirements.

Style-specific investment manager: A manager who invests in just one style of investments, such as growth stocks, value stocks, contrarian stocks, and so on, or mutual funds with a very specific investment focus.

As a result of these considerations, investment management consulting isn't the best model available.

Portfolio Management: A Better Approach

Now we come to yet another category of investment advising—portfolio management. What makes it different than the other approaches? Institutional portfolio-management firms manage money in a standardized, style-specific manner. Often, investment-management consultants hire institutional portfolio managers to manage their clients' portfolios. Institutional portfolio managers rarely communicate directly with their clients and generally don't customize portfolios to meet the client's individual objectives. Given that revolutionary investors want to meet their specific goals and that customization is now possible, what if we took the concept of portfolio management one step further? What if we found a revolutionary portfolio manager?

Institutional portfolio manager: The person with the discretion to buy and sell securities on behalf of a client in the implementation of the client's investment strategy. The manager is generally paid a fee based on the dollar value of the assets managed.

Revolutionary portfolio manager: A financial professional who plays an educational and consultative role, teaching clients about the fundamentals of investing, customizing and managing the portfolio based on the clients' specific objectives and risk parameters, and counseling them through difficult periods in the market.

The first step we'd take is to use a fee-based portfolio-management system. This business model encourages portfolio managers to educate clients and take a customized approach. The fee-based system, unlike the commission-based model, dramatically reduces the potential for conflicts of interest. However, in a traditional Wall Street investment firm, this fee-based system can be a problem. The fee structure is sometimes prohibitively high because of all the layers that needed to be paid—the investment firm itself, the portfolio manager, the brokers, and the mutual fund companies and managers. That leads us to step two.

The second step in creating a process that reflects what today's investor really needs is working in an environment flexible and small enough to provide expert advice but also keep fees at a reasonable level. Combined with an element of coaching so both the portfolio manager and client understand the strategy, we have the basic elements of the investor revolution process. As with any revolution, this one will come from dissatisfaction with the current regime among the masses.

Two keys distinguish a revolutionary portfolio manager: discretionary authority to select securities for clients and a personal relationship with clients. If you have a financial advisor who recommends a product or service that is managed by someone other than herself, she is product-centered, or a distributor of standardized investment products. (Keep in mind that some portfolio managers use specific index funds within their portfolios as risk-management tools; that isn't the same thing as selecting other managers to choose funds for the portfolio.) On the other hand, an advisor who makes the investment decisions on a discretionary basis is a portfolio manager. On a fee-only basis, portfolio managers don't benefit from individual transactions. A broker—the person making the trades directed by the portfolio manager—receives a commission on the transactions. This separates the person making investment decisions from the person selling investment products.

Traditionally, institutional portfolio management has taken a hands-off approach when it comes to client interaction. For the most part, these people are securities analysts who manage portfolios in a standardized way, and rarely is a client relationship ever established. This results in an inability for these managers to coach their clients through difficult periods in the market, which can create significant psychological risk.

Investors who are leading the revolution will work with independent, regionally-based portfolio managers who focus more on high-net-worth individuals and smaller- to medium-sized companies. Most cities have several independent portfolio-management firms offering regionally-based management and a personalized touch. At these firms, you meet the people who are making the decisions that relate to your money and who thereby become familiar with you and your investment goals. These firms have a process for managing portfolios using a rules-based system.

Some portfolio managers are obviously better than others. To be able to justify an expense for their services, portfolio managers must show that they have a process to add reasonable value over and above what investing in an index fund would do. These managers have different styles, but if they have the credentials and experience we'll discuss in the next section, as well as an investment discipline they can articulate, and you are able to make a personal connection with them, then they should be worth considering for managing your portfolio.

What Is a Portfolio Manager?

It's important to make an informed decision when selecting a portfolio manager. As you begin to pay attention to roles, titles, and credentials, it's imperative that you know and can speak directly to the person who manages your portfolio so he can customize it to your specific needs.

Independent portfolio managers generally have training or designations in fundamental and/or technical analysis and modern portfolio theory. The two top designations for portfolio managers are Chartered Market Technician (CMT) and Chartered Financial Analyst® (CFA®). Both designations require at least three years of study and testing. Both certifications also carry requirements for work experience. As confusing as they may seem, the right acronyms are invaluable finds when it comes to picking the portfolio manager who's best for your money. Portfolio-management firms sometimes have their own in-house programs to teach their portfolio managers the fundamentals of portfolio management.

Although credentials don't necessarily guarantee you're getting a great portfolio manager, they provide a starting point and show that the portfolio manager has gone through training, taken a certification exam, and focused on investment analysis for a certain period. Anyone can call herself a portfolio manager; you must look deeper to make sure you're getting what you want. Portfolio-management experience and process are most important.

Following are a few of the financial areas I feel investors should keep in mind when researching portfolio managers. To be successful at managing portfolios, a manager needs to be skilled in five disciplines:

1. *Fundamentals of portfolio management and construction of efficient portfolios:* The most efficient portfolio is the one with the highest return and least risk. Rational investors want the highest return possible within their personal risk-comfort range.
2. *Stock and bond selection:* The manager must have a clear understanding of the psychology of markets. Technical market analysis is based on the irrefutable law of supply and demand. Supply and demand causes stocks and markets to go up and down. The law of supply and demand is the result of changes in human behavior, which are somewhat predictable.
3. *Volatility management:* The manager must utilize a method to measure and identify the changing volatility in markets, securities, and portfolios, and then use a process to make adjustments in the asset allocation and securities based on that. The key to obtaining the highest risk-adjusted return is to maintain a consistent level of volatility in the portfolio.
4. *Investor education:* The manager must possess an understanding of and have the ability to communicate common myths and psychological stumbling blocks that cause individual investors to make wrong decisions. Client coaching is crucial to helping investors avoid one of the biggest risks in investing: psychological risk. Psychological risk causes people to abandon their investment discipline during difficult times and to be too optimistic at the top of the market and too pessimistic at the bottom of the market.
5. *Investment Policy Statement (IPS)*: The manager must establish written investment objectives and make every attempt to follow an investment process that quantifies and encompasses the investment objectives of the investor. An IPS should also address quality-of-life issues involving the role and purpose of money for the investor.

Manage Your Own Portfolio, or Seek the Help of a Professional?

You may have begun to realize that managing a substantial portfolio is a complex and time-consuming endeavor. You have just begun to scratch the surface of the knowledge you need to have lifelong success at investing. So, the question arises: Should you try to manage your own portfolio or let a trained professional do it for you? Like Jim in our earlier example, you may be looking for the answer to that question but may not know who can answer it for you.

You may think I have only one answer because I make a living in the field of investment management. But in reality, I can't answer this question for you. Before you make the first phone call or surf the first Web site, you should ask yourself what you really want.

There's no right or wrong answer. Your answer depends on your personal style: Are you a hands-on type who likes to personally oversee every aspect of your life? Are you fascinated with the financial markets? Do you consider portfolio management an enjoyable and productive activity or hobby? If so, then you'll probably be willing to manage your portfolio on your own.

On the other hand, do you consider the management of investments a burden? Do you want to understand the nuances of investing but not necessarily handle the day-to-day maintenance? Are you comfortable delegating important tasks to others? If so, you may want to consider working with a portfolio manager.

Which Financial Advisor Option Is Right for You?

Questions to ask yourself:

- Do I want to manage my own portfolio?
- What am I looking for—assistance with buying/selling securities, investment advice, or both?
- How do I want to pay a financial advisor? Fees? Commissions?

- How important is it that my financial advisor have a fiduciary responsibility to put my interests first?

Questions to ask a potential advisor:

- Do you manage portfolios on a discretionary basis?
- Are you compensated by management fees, commissions, or both?
- Do you recommend or utilize mutual funds or outside money managers or products?
- Are you compensated by commissions on trades?
- What are your credentials?
- Can you articulate your investment process in a way that I can understand?
- How much experience do you have?

Locating the Right Portfolio Manager

Trust is a huge factor in investment management. It goes without saying that you need to trust the person in charge of your assets. When trust is established, often through a personal connection with the portfolio manager, the investor typically experiences peace of mind regarding how her money is being handled. The real task on the investor's part is to perform the due diligence to find the right portfolio manager, which is more important than understanding all the complexities of the products currently available in the market. Here are some keys to locating the right portfolio manager:

1. *It's impossible to get a customized result if you don't know the portfolio manager.* A customized investment program is more than just the portfolio itself. It should include individualized investor education, coaching through investment objectives, and the creation of an Investment Policy Statement, which connects the client's specific objectives to the investment process. Ongoing counseling is important to protect the investor from the psychological risk of circumventing the investment process.

2. *There is no substitute for experience.* Be sure your portfolio manager has been around long enough to have experienced many different market environments. In 2000, many portfolio managers with the best short-term track records had never experienced a bear market. They didn't recognize the need to practice risk management. A a result, they lost billions of investor dollars as well as, in many cases, their jobs.
3. *Make sure you generally understand the portfolio manager's investment process and that you're comfortable with it.* The manager should discuss things like his buy and sell discipline, how he defines and manages various kinds of risk, the kinds of securities he considers, and how he diversifies his portfolios. Does he manage the portfolio with consideration given to tax implications? You should jointly define expectations for communication. You may require quarterly meetings or may want to meet on an as-needed basis.
4. *Portfolio management is primarily a left-brain (analytical) activity.* Find out if the portfolio-management firm offers some right-brain services that are included in the management fee, such as financial planning, personal wealth management, or coaching.

One benefit of the Information Age coupled with the growing wealth of individual investors is that there are more and more regionally-based portfolio management firms. Most of these firms specialize in working with investors with minimum assets generally ranging from around $500,000 to $1,000,000. You can find these firms by asking for referrals from friends or doing an Internet search for investment-management firms coupled with the name of your closest major city. Looking at a portfolio-management firm's Web site is a great way to gather information and to get a first impression prior to narrowing your choices for firms to interview.

Most portfolio managers like to meet with potential clients several times to be sure of a fit. There is rarely a charge for the introductory process. You should feel comfortable bringing your statements with you for the manager to analyze. Expect discussions about what you want and your investment experiences—both good and bad. The portfolio manager will probably want to provide you with some investment education, which is important to help get you and the manager speaking the same language for better communication.

You should be able to sever your relationship at any time with no penalties. For that reason, it's as important to the manager as it is to you that everyone feels at ease. The last thing the manager wants is for you to change your mind after a year or two. The manager has a lot of time and effort invested in setting up your accounts and creating your portfolio. You should fully expect and feel comfortable with the idea of having a long-term relationship with your portfolio-management firm. If you have any second thoughts, then you should probably keep looking.

When I met Larry and Lindsay, a couple in their 50s, they had already met with several potential financial advisors, none of whom had presented a logical investment strategy they felt fit them. By the time I met them, they were loaded with questions.

We talked about what they wanted in an advisory relationship and the types of clients with whom I'd successfully worked in the past. After a series of meetings over the next few weeks, we decided to work together. As an added benefit, we've also become good friends.

Larry and Lindsay used an intelligent approach to finding an investment advisor. "You have to educate yourself," Larry suggested. "You have to know what you're going after, and the only way to do that is to talk with people, find out what their philosophy is, and find out if you agree with that philosophy. We discounted certain people right away because their personalities didn't mesh with ours."

Lean Toward a Fee-Based System

Although there is no perfect way for an advisor to charge for services, some methods are better than others. A fee-only portfolio manager is more likely to give objective advice than someone who's commission-based. Portfolio managers have the discretion to trade securities in your portfolio; they should not be compensated by commissions, because they're then paid for trading. Fee-only portfolio managers make more money when the portfolio goes up and less when it goes down, and they get their management fee only as long as they're managing the portfolio. Therefore it's important for them to keep the client happy. Their fee-based system presents more of a win-win dynamic—the advisor can earn more only if the value of the portfolio increases, which is also a win for the investor. It's a better incentive system.

Working with a portfolio-management firm is entirely different than working with a brokerage firm. Keep in mind that as of July 2005, the SEC requires that brokerage firms offering fee-based advice make this disclosure (verbatim):

"Your account is a brokerage account and not an advisory account. Our interests may not always be the same as yours. Please ask us questions to make sure you understand your rights and our obligations to you, including the extent of our obligations to disclose conflicts of interest and to act in your best interest. We are paid both by you and, sometimes, by people who compensate us based on what you buy. Therefore, our profits and our salespersons' compensation may vary by product and over time."

In a study commissioned by TD Ameritrade in 2006, of 1,000 U.S. investors, 79 percent of respondents said they would be less likely to go to a brokerage firm for financial advice after reading the disclosure. However, 43 percent were unaware that brokers and independent portfolio managers are held to different standards by the SEC—and that of the two, only independent portfolio managers are required to act in the best interests of their client in all aspects of their relationship, and only independent portfolio managers are required to disclose all conflicts of interest. It's not always easy to find advice you can trust.

Securities and Exchange Commission (SEC): The agency charged with administering federal securities laws in the U.S. The SEC oversees the key participants in the securities world, including securities exchanges, securities brokers and dealers, investment advisors, and mutual funds. The SEC is concerned primarily with promoting the disclosure of important market-related information, maintaining fair dealing, and protecting against fraud.

Customizing the Investment Industry

The investment industry isn't alone in its gravitation toward client-centered, customized approaches. Retailers latched on to this idea some time ago, and many have found it to reap lucrative results and more satisfied customers. Drugstore giant Walgreens is a prime example. In the 1960s, Walgreens' patrons could expect to find a diner and soda fountain in most locations, along with the standard pharmacy products. Back then, the retailer was more focused on maximizing its profit margin per store, not per customer. In time, Walgreens' executives learned that in order for their good company to become a great company, adjustments were needed, which in effect would change their entire business model. So, Walgreens began to axe its expenses. The diners and soda fountains were done away with to help pay for amenities like drive-up windows and photography studios. The sacrifice was the loss of a sheer volume of customers, but the gain came in persuading each pharmacy customer to spend more by offering more. Walgreens changed its model to be more client-focused and, in effect, blew much of its competition from the 1960s out of the water.

Harry Dent, Jr., the S-curve specialist from earlier chapters, noticed a trend in the early 1990s that showed successful companies moving from standardized retail products to value discount goods and finally to customized premium products. In *The Great Boom Ahead* (Hyperion, 1993), Dent noted how the future economy would "provide enough growth markets for both emerging and maturing companies that can appeal to the growing quality and customized segments of the marketplace." Dent whittled down the three basic market segments in all industries, and labeled companies with one of the following three classifications: yellow-chip, red-chip, or blue-chip.

Yellow-chip: "…The old standard-quality, mass-market sector in the economy. These shrinking companies in mature industries grew up in the assembly-line standardized economy."

Red-chip: "This is the value/discount segment…have made substantial incremental improvements over standard-quality yellow firms, bringing high value into their industries with discount prices, often accompanied by improved quality and service…"

Blue-chip: "The blue-chip is the premium sector of an industry, specializing in high quality, customization, and personalized service with fast response and quick delivery."
(From *The Great Boom Ahead*, Harry S. Dent, Jr. [Hyperion, 1993].)

The yellow-chip companies of Dent's economic outlook were the old, standard-quality companies, or the mass-market sector of a particular industry. In the early 1990s, according to Dent, these included household names like Sears in the retail business, Pizza Hut in food delivery, Ford and GM in the automobile industry, and Merrill Lynch in the investment world.

Next were the red-chip companies, or the value/discount segment, which Dent called "a hotspot in the past, but only warm in the future." Included in this group were maturing retail giants like Wal-Mart, clothiers such as Levis, and, in the investment world, Wall Street discount brokers like Charles Schwab. Dent noticed the trend of red-chip companies making "substantial incremental improvements over standard-quality yellow firms, bringing generally standardized value into their industries with discount prices and improved quality and service." However streamlined the approach of red-chip companies may have seemed, there was still much ground between them and the superior blue-chip sector.

Blue-chip companies represent the premium sector of all industries. Dent's blue-chip term denotes the highest-quality companies, which specialize in customization and personal high-tech service with fast response and quick delivery. Representing this echelon, according to Dent, were automobile manufacturers such as BMW and Lexus, clothiers like Giorgio Armani, delivery services like Federal Express, and, in the investment world, local financial firms. "The future in the coming boom," wrote Dent, "will belong to the companies that fit my definition of blue-chip." Advancements in technology and access to information will allow highly mobile creative firms to revolutionize business models and overtake the giants of the past.

Similar to the successful companies in each economy that tended to focus more on the individual, the ultimate evolution of the investment industry will be to adjust the standard commission-based model to a more personalized fee-based approach. The fee-based model promotes more objectivity and client-centered treatment, representing the blue-chip processes of investing. The number-one incentive for advocates of the fee-based model is to keep clients content with the direction of their portfolio, because the more the portfolio swings in a positive direction, the greater the compensation for the portfolio manager. The fee-based approach tends to eliminate the conflict of interest that's inherent in the sales-based model and thereby ensures that all decisions made within the portfolio are being made in the client's best interest. Customized portfolio management coupled with personal wealth coaching, or personal wealth management, is the investment industry's answer to the need for a blue-chip investment company.

Personal wealth management: A unique process for helping people achieve and manage total wealth and abundance in all forms. It can be broken down into two critical areas: personal wealth coaching and customized portfolio management.

Looking at the Big Picture

Revolutionary portfolio managers need to be good educators who are able to teach revolutionary concepts and explain them in a way that resonates with clients. Investing is counterintuitive: You always feel good at the top and dismal at the bottom. The true risk that investors primarily deal with lies within themselves. Individuals have done more than their fair share of blowing themselves up financially, and it's not always Wall Street's fault. Time and time again, investors have dumped hundreds of thousands of dollars into investments that they haven't begun to understand, which shows an extreme lack of diligence on their part. Time and time again, those steps have resulted in sharp losses, which signal that investors need to better inform themselves about who's right for the job of handling their money.

Not only do investors need to select the right financial advisor, but they need to be sure to use the right tools. One tool is the Investment Policy Statement, which helps investors adhere to more rational objectives. Developed with a portfolio manager, the IPS outlines and prescribes a prudent and acceptable investment philosophy while defining the investment-management procedures and long-term goals for the investor. Creating an IPS compels investors to put their investment strategy in writing and commit to a disciplined investment plan. An IPS is like a blueprint and a report card combined, and it's just one example of a tool that revolutionary investors are utilizing in crafting their futures.

A written IPS helps an investor maintain a long-term focus when short-term market events create distress and perhaps cause you to question your policy. With the objective, predetermined plan outlined in the IPS, an investor avoids emotional decision-making and concentrates on rules-based decision-making. Basically, you become a more disciplined investor. The outcome is a more predictable investment strategy focused on consistency and long-term results.

To realize your potential as a revolutionary investor, you need not only a dynamic investment-management process, but also the right-brain processes that can help add color to your financial objectives. Personal wealth management represents a new approach in the way we invest in our lives. The investor revolution will help us get there.

Funny as it may sound, investing can be an exhilarating and interesting experience. Are investors afraid to change? Of course. Do they want to be safe? Sure. But there are ways to be safe that can also add value. Anyone can cash out and go bury their money in the backyard. Sure, when it's buried, the money is somewhat safe and is always where you put it. If you're going to bury your money, however, why not move it to a savings account, another option for safekeeping? In a savings account, your money may actually make you more money, kicking back about 4 percent interest per year. That's a better deal, but is it the best you can do?

If you want to do better than that, you need to select the best investment process for you. Throughout my professional experience, I know I added value for my clients as a broker, a financial planner, an investment-management consultant, and a portfolio manager. I have many friends who are highly competent advisors, and they too add value for their clients. However, many of today's investors are looking for something more. That "something more" is a revolutionary portfolio manager who practices personal wealth management and is paid a fee to maximize the investor's entire portfolio and structure it in a way that best suits the investor's specific life and goals.

Aaron is a 56-year-old physician. When he became responsible for managing his family's $18 million fortune, he sought guidance from a tax attorney and a broker. "My lawyer emphasized estate tax planning," he recalled. "He set up two charitable remainder unit trusts and a charitable lead trust. With a family limited partnership—another idea of the tax lawyer's—I found myself making choices so that the avoidance of estate taxes seemed to make my life worse instead of better. The broker showed a personal interest in me but not in any way toward furthering my goals or helping me use the money to have a better life. The money seemed like the only goal. He'd say, 'Buy bonds' but never made any suggestions about balancing my total portfolio."

Aaron knew he wanted a comprehensive approach to coordinating his life issues with his personal finances. He also wanted a fee-based service, free from conflicts of interest. Working with a personal wealth manager has met those needs.

Challenge yourself to join the revolution! Challenge yourself to move to the next level, beyond standardized solutions for complex issues, and to work with an advisor who integrates your future life vision and goals with personal wealth coaching and portfolio management customized to meet your changing needs. What revolutionary investors are looking for can only be found in personal wealth management—the blue-chip answer to an evolving environment. Individual investors must decide what's best for them. Making an informed choice is the first step in producing the best results for the future.