

Not all logic is persuasive

WORDS PETER BELSEY

IFAs have to find ways to work with clients even in difficult times

The independent inquiry led by Sir Richard Sykes into the investment industry has certainly pulled no punches. The report, just published, calls for the industry to sign up to a new code of conduct - what Sir Richard himself has likened to a 'Hippocratic oath' - in order to restore the public's trust and "sort out the crisis of confidence in investing." In demanding more openness and honesty, he draws a direct comparison with the medical profession and points to 'enormous disconnects' between fund managers for example and the actual owners of shares - often ordinary individuals saving for their pensions.

In what is in many ways a devastating critique of recent industry practice, the report points the finger at the many aspects which need to change if, in the longer term, the general public are to view investment in a more favourable light. Summing up, Sykes believes that, "the issues are about trust, confidence, transparency, standards and principle.

At the end of the day, we need to bring confidence back so that people are willing to invest in equities rather than rushing headlong into bricks and mortar."

INVESTOR EDUCATION

So how should IFAs respond and ensure that the service they provide is in line with what the Sykes Report is calling for?

The key here, I believe, lies in what the report describes as 'a gulf in investor education' - IFAs have a critical role to play in improving clients' understanding, so that they are well placed to make better quality investment decisions.

Of course, many IFAs will passionately believe, quite rightly, that they have always tried to do this. Yet, at a time when confidence needs to be rebuilt, there are a number of traps into which the unwary can fall, with the result that they fail to be persuasive and so take advantage of the upturn in the current investment market.

The problem they face is that there has been an overall loss of faith on the part of the general public in investment vehicles. The main reason for this of course has been the fall in the value of the stock market, but the result has been that people have seen a significant, if as yet unrealised, decline in the value of their pensions and other savings instruments which they have worked hard to build up over many years.

Not surprisingly, they have thus become more wary about where to put their money and for many this has meant putting it into property. The challenge for the IFA therefore is at what stage do they attempt to persuade such clients to 'dip their toes back into the water' in the area of high yield investments.

The good news is that, at the top end of the private investor market, there is also already some momentum in this direction. According to a recent survey by Capgemini and Merrill Lynch, the world's richest people saw their wealth rise by 7.7% in 2003,

driven in large part by, 'a shift...back into higher yielding investments, including equities, specialised products and alternative investments, including hedge funds.'

This move by ultra high net worth individuals contrasts strongly with the continuing caution of the average private investor and reinforces what IFAs and other financial advisors see as the logic - both in terms of direction and timing - for the saver community to reassess the options available.

Two obvious questions emerge from this: when should the IFA seek to persuade a client to do something different and how can this be achieved?

The 'when' will to a large degree depend on how risk averse an individual client is and how hard IFAs feel they can push a recommendation for change in each case. (There is evidence for example to suggest that some wealthier investors have already dispensed with the services of wealth managers as a result of what they saw as poor advice.)

Yet IFAs and other advisors cannot simply disengage from their client base and revert to straightforward order taking. Regulatory imperatives concerning 'best advice' and Sykes' call for investor education require IFAs to act positively in ensuring the investment solution meets the client's objectives. This means that, where the client wishes to pursue a course of action which will not achieve the desired outcome, the IFA has a responsibility to dissuade the client from going down that route and to consider alternative options. However, at a time when private savers are still smarting from having their fingers burned in making higher risk investments, the real issue is how to get them to take a fresh look at such savings mechanisms.

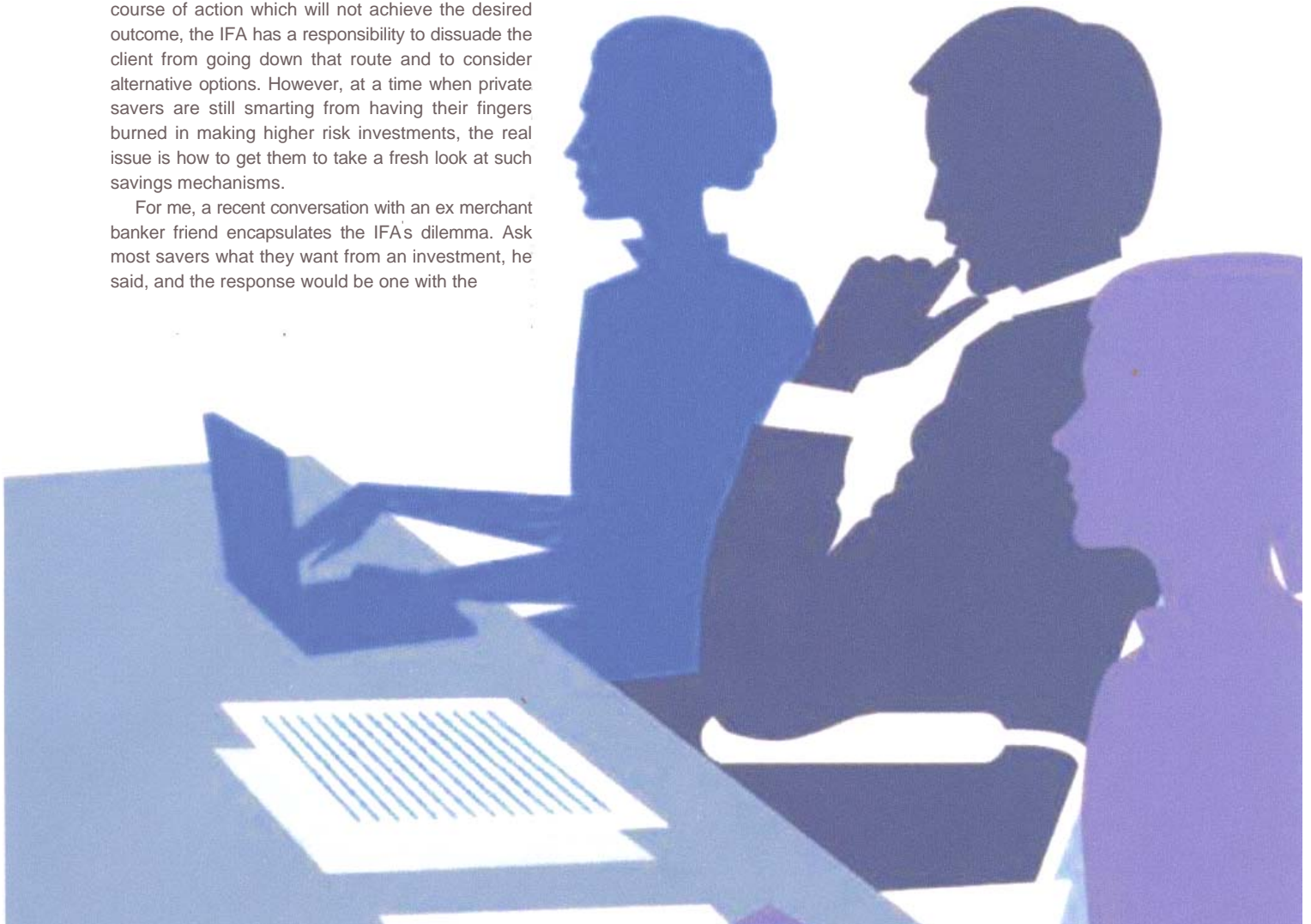
For me, a recent conversation with an ex merchant banker friend encapsulates the IFA's dilemma. Ask most savers what they want from an investment, he said, and the response would be one with the

lowest risk and highest return. Not the real world of course, where the trick is to achieve the best balance between risk and reward.

As a result however, many investors have got caught out through investing in fashion stocks including many technology funds or split capital funds - superficially attractive perhaps, but where the fundamentals just weren't there. He likened this to a car purchase: in choosing between the latest high tech design sports car and a classic 40 year old Jaguar, say, though the value of both may go down in the short term, financially there is absolutely no doubt which is likely to prove the better ultimate purchase.

So with investments, he argued, where one should look to the quality end of the market. Even in the toughest times there have been many shares which have continued to yield good dividends - and so provide an attractive revenue return - even though the value of those equities has suffered in the past two years or so.

My response was that this was a strong and totally logical argument - but not in the least bit persuasive! Providing a sound argument is all very well, but the critical question is, who is seeing the need to do something different here? The IFA ▶



clearly does, yet for the average investor the risk of switching back into equities still outweighs the potential value longer-term of doing so.

A QUESTIONING APPROACH

So how does the IFA tackle this? The key is to adopt an approach principally based on questioning, rather than giving information.

Firstly, explore with the client where they are now in terms of existing investments and then compare that with where they want to be. The purpose of this is to establish a gap, as the current investment strategy will almost certainly fail to produce the desired outcome. The goal is not to get the client to accept that change is OK, but rather to see that continuing as they are is untenable. This is because it is essential to create doubt in the current strategy before you can hope to build value in an alternative.

To be successful, the IFA's role here is to help the client come to this conclusion themselves and not force it on them. One obvious focus is the changing

typically complex sales environment.

The 'right' questions are neither 'open' nor 'closed'. Rather, the skilled seller will phrase their questions so that each has a clear purpose, whether to uncover, clarify or extend implied or explicit needs. By being client-centric, they will enable the client to form insights that will help them recognise differing needs.

In the context of an IFA helping savers recognise the value of moving back into higher yielding investments for example, what is appropriate will depend on the client's individual circumstances and goals. Yet common to all will be the need to help each identify the level of return they will need to achieve in order to realise their objectives and the appropriate level of attendant risk. The IFA is then - and only then - in a position to provide advice in a way which will truly connect with the client, rather than dumping information and recommendations at a point where the response is likely to be negative.

The stock market may have lost half its value in the wake of September 11, yet recent months have

THE ISSUES ARE OUR TRUST, CONFIDENCE, TRANSPARENCY, STANDARDS AND PRINCIPLE. AT THE END OF THE DAY, WE NEED TO BRING CONFIDENCE BACK

climate of interest rates: in a recent speech, the governor of the Bank of England for example clearly endorsed the view that property prices - and thus, by implication, the value of bricks and mortar based investments - are unlikely to continue their upward spiral. The result is a greater level of risk in staying with a property only investment strategy, just as staying with cash is similarly unlikely to produce the level of return required to meet the client's aspirations.

Having enabled the client to see the limitations of their current strategy - and so appreciate the need for change - the IFA can then explore with them the value of investing again, at a time when the rewards for so doing have once again started to increase. The questioning technique needed - asking the right questions in the right way - is very much in line with the consultative approach adopted by most successful salespeople in today's

seen a strong recovery. This will have come as no surprise to most IFAs, many of whom have been in the business for many years and understand the long term nature of equity investment. Yet it is easy to forget what it is like to be a client, who does not have 30 years' experience, has not seen markets going up and down and is terrified of seeing their plans for a comfortable old age disappear. The trap is to move at too fast a pace and, with insufficient inherent trust today in accepting the advice of a financial 'expert', the IFA will fail to take the client with them.

It is important to recognise that any investment, be it property, cash, or the latest exciting investment product, should come with a health warning. It may be at a time when the stock market is rising and the value of alternative investments is being brought into increasing question, the opportunities for the IFA to encourage clients back into insurance products are now greater than for some time.

Just remember, there are times when logic on its own just isn't enough. ISFSI

