

# CHAPTER 1

## The Evolution of Financial Advice

*You can't connect the dots looking forward; you can only connect them looking backwards. So you have to trust that the dots will somehow connect in your future.*

—Steve Jobs

Advice is essential for people to reach their financial goals and dreams. Technology has made it so much easier for consumers to access information, and it is important for advisors to recognize how this impacts their role—for better and for worse. As consumers think about their changing demands, and as advisors position themselves for the future, both groups must understand how drastically the financial system has evolved. It's easy to forget that not long ago the financial landscape was very different. For example, we take for granted the number of transactions we can handle on our phones. Even 10 years ago the thought of moving money with the swipe of a finger or depositing a check by taking a picture seemed crazy.

In the broad history of our industry, the 1950s wasn't that long ago. During that time, when consumers had a few dollars to put away, they opened a savings account. At some savings and loans (S&Ls), the teller wrote down the amount of the deposit in the saver's bankbook along with any interest that had accrued. In time, computers took over

many of these tasks, and the economy started to become more global. In the 1980s and 1990s, banks focused on geographic expansion, entering new markets and building more—and larger—branches. Less than a decade later, the amount of traffic into most retail branches declined sharply. Today, few people visit a brick-and-mortar branch to do their banking. Many banks, especially those with a regional focus, are trying to shutter as many locations as possible, a trend driven largely by the rise of ATM transactions.

The first ATM in the United States appeared sometime in the late 1960s. By 1980, the number of monthly ATM transactions was nearly 100 million. Within 10 years that number grew to almost 500 million transactions per month.<sup>1</sup> This accelerated a strategic change for banking executives. In 20 years, banks went from adding real estate to decreasing real estate—an amazing transformation in a sector that remains the heart of the financial services industry. In the remaining branches, there is also a tighter focus on generating revenue through the sale of specialized products and services that often have higher margins. There are also far fewer tellers than in the past, and it is not uncommon for them to encourage customers to bank online and through mobile channels.

This short trip down memory lane was intentional. Banking is the largest portion of the financial services industry and these rapid changes impacted its employees and clients. In the wake of such significant change to the industry's biggest sector, it's reasonable to believe that the wealth management and advisory businesses will face similar disruption in the very near future. Those opportunities and challenges exist today and will accelerate for advisors.

## THE ROOTS OF MODERN INVESTING

The majority of this book is about the future. Our goal is to present a roadmap for increased success in a period of immense change. In order to do so, we believe it is crucial to examine the past. After all, these events have set up where we are today and represent the building blocks

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<sup>1</sup> Michael Quint. "Citibank Joins Teller Network," *New York Times*, February 16, 1991, [www.nytimes.com/1991/02/16/business/company-news-citibank-joins-teller-network.html](http://www.nytimes.com/1991/02/16/business/company-news-citibank-joins-teller-network.html).

of the future. In the 1950s, most people in the United States shunned investing. Many of them had lived through the Great Depression and wanted no part of the stock market. A number of Americans subscribed to the notion that the stock market was for rich people, and this perception had become a reality. Buying and selling securities was costly, in large part because most brokerage firms charged fixed commissions, which were quite high and typically nonnegotiable. These rates could be 10 percent or more of the transaction amount. In 1952, only 6.5 million Americans, which was about 4.2 percent of the U.S. population, owned stock.<sup>2</sup>

In the 1970s and 1980s, consumers typically looked to brokers for what they deemed to be financial “advice.” Madison Avenue helped broker-dealers convey that message to consumers through advertising. One of the most famous commercials of all time was for the brokerage firm, E. F. Hutton. In one commercial, wealthy people were filmed as they lounged around a swimming pool at what appears to be a country club or a fancy hotel. A man turns to a woman and asks about her broker’s advice. She answers casually, “Well my broker is E. F. Hutton, and E. F. Hutton says . . .” Everyone around the pool stops talking, purportedly because they want to hear E. F. Hutton’s financial advice.

Advertising campaigns like E. F. Hutton’s were built on the premise that a brokerage firm could give investors tips on what securities products to buy. Since that campaign, the firm has disappeared through a series of acquisitions involving Smith Barney, Morgan Stanley, and Citigroup. (E. F. Hutton’s grandson has launched a new, unrelated company under the old name.) But many people remember the slogan that made E. F. Hutton famous, “When E. F. Hutton talks, people listen.” *Money* magazine describes, on its website, how effective the campaign was during the bull market that began in 1982:

This was a powerful image during the bull market that started in 1982. After the lost decade of the 1970s, investors were getting excited about stocks again. The

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<sup>2</sup> “Stocks Then And Now: 1950s And 1970s,” Investopedia, October 1, 2008, [www.investopedia.com/articles/stocks/09/stocks-1950s-1970s.asp?layout=orig](http://www.investopedia.com/articles/stocks/09/stocks-1950s-1970s.asp?layout=orig).

Hutton ad suggested that only through a broker could you gain an investing edge.

In some ways, the suggestion was ironic—coming just ahead of the massive insider trading scandals of the late 1980s, when dozens of Wall Street players, including Ivan Boesky and Michael Milken, were found to have skirted the rules for their own advantage. So much for the broker edge, which in those cases anyway was about illegal stock tips sometimes in exchange for suitcases full of cash.<sup>3</sup>

During that same era, Smith Barney launched an equally memorable ad campaign. Distinguished actor John Houseman voiced the immortal slogan: “Smith Barney. They make money the old-fashioned way: They earn it.” It’s worth revisiting these advertisements because they capture what the world of financial advice was like in the 1970s and 1980s. And they also reflect how consumers perceived it. These campaigns strongly tied financial advisors to the wealthy classes, and perpetuated the mystique of investment firms. That approach was quite different from what you see today in television commercials for established firms, and in taxi-cab ads for new players like Wealthfront and Betterment.

Firms also operate much differently now. Up until the late 1980s, if you were a broker, you attended a daily research call where stock ideas were discussed. These research calls gave brokers ideas for how to help their clients buy and sell securities. Brokers were allowed to promote only those stocks on which there was research coverage. There’s a debate as to why this happened. Some would argue it was to manage risk, as recommended securities should be tracked, but others with a more jaded view argue it was to push the securities with higher commissions or with companies with financial ties to the brokerage firm. The investment business was largely product focused. It was an era when brokers pushed stocks touted by research analysts.

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<sup>3</sup> “Shhh . . . E.F. Hutton Is Talking Again,” *Money*, March 19, 2015, <http://time.com/money/3751675/ef-hutton-gateway/>.

## REGULATORY AND TAX CHANGES SPUR EVOLUTION

In 1975, the Securities and Exchange Commission (SEC) made an important decision that laid the path for the financial world as we know it today. Fixed commissions were abolished. Up until what is known as “May Day,” brokerage firms charged commissions based on a schedule published by the New York Stock Exchange. The commission was calculated off a grid based on the number of shares traded. Brokerage firms, therefore, could not compete with each other on price. The new regulations created a situation where commissions could now be negotiated. This decision opened the way for discount brokers, and eventually led to the online trading craze of the 1990s. Fueled by enhanced technology, online trading allowed people to cheaply buy their favorite stocks on their own, without a broker, for the first time.

The next change came in 1978, three years after fixed commissions were abolished. A major change to the tax code opened the door to an entirely new financial services sector. Congress added Section 401, under which Item K allowed companies to offer their employees an additional benefit, now known as the 401(k) retirement savings plan. 401(k)s and similar defined contribution plans helped turn employees from spenders into savers—and investors.

401(k) retirement savings plans took off in the 1980s around the same time that companies began to sunset traditional pensions. The vast majority of defined contribution plans were offered by larger companies as one of the benefits to retain employees and also encourage saving. A key inducement was the employer match, a 401(k) contribution made by the employer at no cost to the employee.

Despite the potential benefits of 401(k) plans, they also presented employers with new challenges. Most companies had no idea how to determine which investments should go into these plans, so they turned to 401(k) record-keeping firms to administer their plans. Most of these firms were units of large mutual fund companies so, not surprisingly, the investment menu consisted of a good range of mutual funds. (The default option was the money market fund, much like today’s default option would be a target date fund.) This represented a key building block for the future because the 401(k) business supported the enormous growth of the mutual fund industry.

Meanwhile, wirehouse firms began to more clearly separate business development from managing money. During the 1980s, firms encouraged their account executives to gather new business and increase clients' investments, while professional money managers tended to client portfolios. This shift emerged from the belief that individuals would benefit from the investment professionals' expertise, and that client-facing advisors could better serve customers by focusing more time on their existing clients. Without the burden of managing every client portfolio, advisors could also work on business development.

So marked the beginning of fee-based management and managed accounts. On the heels of the existence of managed accounts came professional gatekeepers who decided which asset managers qualified to be on a securities firm's platform. The good gatekeepers protected clients because the decision to put an asset manager on or off the platform was based on performance. One could argue there were also bad gatekeepers who selected asset managers onto the platform based more on revenue share agreements than what was good for the clients. The debate on good versus bad gatekeepers remains to this day and the managed accounts business has blossomed into a \$4 trillion industry.

## A SMALL SHIFT TO ADVICE

As we will discuss in depth later in the book, we believe financial planning and coaching will be a key building block of advisor value in the future. When we speak at conferences and industry events, it seems like some people think this is a fundamental change that happened overnight. It's not. The industry has actually been shifting this way for decades. For comparison, consider a musician who has been writing songs and playing in clubs for years. When she finally gets a hit song, she is viewed as an overnight sensation. In reality, however, the musician is being noticed for the first time after years of playing the same kind of music.

Financial planning as a value proposition is nothing new for thousands of advisors. Although in its infancy the idea of *planning* was very different than it is today, it did exist. Back then, the financial planning process focused mostly on asset allocation advice and was often driven

by Morningstar-style boxes. The idea of planning gained some attention when the College for Financial Planning opened in 1972. The College has graduated more than 64,000 individuals into the financial planning industry. Can you imagine what it must have been like to graduate in some of those earlier classes? The economic and political factors a planner dealt with in the mid to late 1970s represented uncharted territory. Planners were required to deal with double-digit inflation and a sustained bear market. It was actually a bad time to be in the “advice” business, because the bear market had soured consumers and there were few who wanted to invest. For many consumers, paying close to 18 percent interest on their home mortgages left them with little disposable income. This situation left advisors with fewer potential clients because people were not investing in the market. Consumers with assets were likely keeping their money in certificates of deposit (CDs) or treasuries with longer-term yields above 12 percent.

The 1980s brought a major shift. Faced with making investment selections for their own 401(k) retirement plans, which provided no guidance, people’s investment lives started to become more complex. On top of that, the stock market began to recover in 1982 and the tax code was changed in 1986, two changes that made people more interested in the investment potential of the markets. However, the advice business as we think of it today still didn’t exist. More money entered the market, but stocks and bonds continued to dominate.

The concepts of holistic advice and account aggregation were not in the lexicon of the day. It was not until the late 1980s that the advice business began to change, and these changes started setting up many of the advice models that exist today. *Fee-only* firms, as they are known today, started popping up around the country. Fee-only firms were built on the idea that the way advisors were paid in the past created conflicts because advisors were paid differently based on the investment products they recommended. Fee-only firms don’t collect commissions and don’t collect fees from the fund companies for putting their clients in certain securities. The client fees for advice are the only source of revenue for these firms. The argument is since the client is the only one paying the advisory firm, potential conflicts of interest are removed from the relationship. We will drill deeper into this argument later in the book when we discuss how advisors are

paid and how consumers should think about fees. Ric Edelman started his firm in 1991, right around the time fee-only advising was going mainstream. When we asked Ric why he decided to start his firm, his answer was simple:

We went looking for a place where people could get good financial advice and we couldn't find a place like that anywhere. We believed consumers needed people that were focused more on the outcomes they needed in their lives, than the products they needed in their portfolios. The only advice people got was from people focused more on selling them something in their portfolios than bringing better outcomes to their lives.

In the early 1990s, technology use in the industry was exploding and so was the stock market. A trading frenzy enabled by online trading came onto the scene. Charles Schwab was the major disrupter during this time. For the first time, trades were far less expensive than at the major brokerage firms, but the major brokerage firms countered by starting their own online divisions. This intersected with the rise of technology companies nobody had ever heard of—commonly referred to as *dot-coms*. These companies had no real business models, but they became the most talked-about companies in America—and people wanted to feel like they were part of the game. Investing presented them with a way to become directly involved in the action. Regardless of age or wealth tier, people had online accounts to play the market, and they were winning because technology stocks seemed to go in one direction, *up!* Research analysts covering these tech upstarts were measuring them in part by the amount of traffic their websites were getting, which often took precedence over the companies' financials. Later, this time period was famously referred to by Federal Reserve Chairman Alan Greenspan as the period of "irrational exuberance." The dot-com bubble started to burst in 2000, and the stock market slide continued for three years. What is interesting about the market collapse of 2000, and even back to 1987 and 1989, is that consumers seemed to accept that market cycles existed, so unstable periods didn't increase the number of consumers seeking financial advice. We believe this changed with the market turmoil of 2008 and 2009, which we will discuss later in the chapter.

After the technology bubble burst in 2000, many consumers headed for the sidelines, but around 2005 a number of online trading tools emerged, offering people a do-it-yourself approach and luring some people back to the markets. During the peak of this trend, you couldn't go to a party without someone talking about their brother, sister, cousin, or unemployed friend who was day trading. Few were day trading full time, but many who were quickly realized they should have kept their day jobs. It's not easy to win against the professionals who dominate market trading. Even more discouraging was the devastating market correction that occurred during the 2008 economic meltdown. Anyone involved in the financial services industry back in 2008—advisor, trader, investor—can't help but be scarred from what occurred during the *Great Recession*. People inside the industry and outside of it enjoy debating the merits of quantitative easing or the government bailouts during this time period, but one thing everyone can agree on is how awful late 2008 and 2009 were for those in the financial services industry—especially for all the clients who lost big. It was like a financial Armageddon. It seems nobody was immune. As we mentioned earlier in the chapter, consumers who survived prior market corrections seemed to disconnect their effects from financial advice or Wall Street anger. Markets go up. Markets go down. That seemed to be the prevailing view of previous corrections. We aren't saying clients weren't frustrated or worried, but given that many of the previous market corrections were at a time when pensions and Social Security were the key retirement vehicles for most Americans, the Great Recession was the first major market correction where everyday investors felt their retirement savings and overall financial health were in jeopardy. The anger, confusion, and growing need for advice triggered an interesting journey for both individual investors and advisors since 2009.

## **A NEW ADVICE MODEL**

In 2008 and 2009, client portfolios were destroyed. When talking to consumers during that time period, many told us they couldn't even open their account statements because they were too anxious to look at them. However, that market cycle, which started in March of 2009, brought about a new approach that correlated with the consumer's

perception that investing is easy. The do-it-yourself, day-trading frenzy that took place just before the financial meltdown was replaced by a hybrid model of simplistic, cost-conscious investments packaged in a digital advice model, the so-called *robo advisor*. The robo-advisor movement really began in early 2013 and accelerated throughout that year. As the stock market recovery began to take hold in 2009, the annual returns for the S&P were as follows:

2009: 26 percent

2010: 15 percent

2011: 2 percent

2012: 16 percent

2013: 32 percent

Consumers began to forget about the carnage that occurred in their accounts in 2009. Although consumers were still scared, it certainly started to feel like the markets would go up forever. Despite this, today's complex markets mean individual investors need even more reliable advice than they did in the past.

## Too Much Noise

Financial advice is needed now more than ever. Ironically, what makes it more difficult for advisors today is the fact that far more resources are at their disposal. Today's individual investors can obtain financial information from a variety of sources, not just their broker, insurance agent, or financial advisor. Many of these consumers watch CNBC and Fox Business; they read research reports. Financial information (good and bad) is available everywhere. The question for a consumer remains the same: Am I receiving objective and disinterested advice?

Jay was in an airport working on this book, and a guy sitting next to him on the plane asked him what he was writing. Jay explained the premise of the book, and it turned out the man was a financial advisor. The guy laughed and said, "I knew consumers had too much free advice at their disposal when I got a call from my 78-year-old mother. She was calling to ask me why we weren't shorting a stock in her account because she heard it discussed on Jim Cramer's *Mad Money*

television program.” It really is an ironic twist. Consumers have gone from getting little or no financial data to suffering from information overload but, with this change, the consumer is no better off. Many people would argue that investors should put that information to good use and do more research before making investment decisions, but when you spend time with the people, you quickly realize few have the time or the interest to sift through the information available to them. With apologies to Jim Cramer and E. F. Hutton, investment advice today should encompass much more than hot stock tips.

## Changes in Investment Products

Just as the advice model has changed for consumers over the past five decades, so have the investment products and solutions in their portfolios. In the 1950s and 1960s, most portfolios consisted of stocks and bonds. That was it. There were no mutual funds or exchange-traded funds (ETFs) or any of the other, more sophisticated investment products that exist today. If you were one of the 4.6 percent of Americans during that time period with investments in the market, you probably owned blue-chip stocks like IBM and corporate bonds like those offered by General Electric. In the 1970s, investors graduated into partnerships; commonly oil and gas limited partnerships driven by the oil boom. In the 1980s, some investors began to move toward fee-based brokerage accounts, but it wasn't a large movement.

The setup for many of today's investment vehicle trends occurred in the 1990s with mutual fund superstars like Peter Lynch of Magellan. Lynch claimed that during his time at the firm, one out of every 100 Americans with investable assets put them in the Magellan mutual fund.

Mutual funds were touted as a way for small investors to diversify their nest egg. Initially, most mutual funds were actively managed by a fund manager who selected which stocks to include. Later, mutual funds tied to market indexes like the S&P 500 became popular.

The separately managed account (SMA) was also on the rise in the 1990s. Separately managed accounts were touted as highly personalized accounts, managed to meet the specific needs of a single investor. For all the talk around these new products, SMAs were not customized

as many consumers believed. Instead they were just packaged strategies. The manager actively traded stocks with the goal of using a particular strategy to outpace the overall market.

In 1991, the first consumer ETF was launched, but it took some time for these new products to gain momentum. Today, many financial advisors' strategies are built around ETFs, and they are the building blocks of many robo-advisor or digital portfolios. The rapid growth of ETF utilization has surprised many, including us. Chip Roame, managing partner of Tiburon Strategic Advisors, is similarly amazed:

I wrote off ETFs initially because I didn't think they were attractive in the way they were being sold. Originally the differentiation salespeople discussed was that, unlike mutual funds, ETFs could be traded and valued throughout the day. I remember thinking, "Who cares?" What I and so many others missed was the appeal investors saw in passive indexing at much lower product costs.

The ETF marketplace now represents \$4.1 trillion in assets or 15 percent of the overall mutual fund universe. ETFs have many advantages for end investors. Even the SEC commissioner has taken notice of the benefits of the vehicles for investors. ETFs, according to SEC Commissioner Kara M. Stein in a speech at Harvard Law School on November 9, 2015, have been in some ways a "positive, competitive innovation in the markets. They have opened up an array of investment options for investors and are often more tax efficient." Her continued comments on ETF behavior could be signaling an interesting focus as the SEC and other regulatory agencies deal with their growing utilization in digital portfolios. According to Stein, ETFs behave very differently than mutual funds—*very* differently.

On August 24, 2015, many stocks opened extremely and unexpectedly low. Certain stocks dropped almost 50 percent and then quickly recovered for no apparent reason. Trading was halted 1,200 times that day. But that rocky day demonstrated that ETFs may act quite unusually in stressed market conditions. ETFs should trade relatively closely to the overall fair value of the underlying stocks in the ETF. Throughout the day there were a number of times where this did

not occur, where wide variances existed between certain ETFs' traded values and the value of the underlying securities. This has an impact on the liquidity of the ETF. Liquidity and interday valuations/trading, on paper, are supposed to be key benefits of ETF vehicles.

Stein expressed concern for everyday investors who submitted stop loss orders on August 24. There were numerous reports of investors who found that their shares were sold at a price well below their stop loss orders, which defeated the purpose of the stop loss orders, which is to cut an investor's losses when a security is dropping in price. In the end, ETFs, in many advisors' and investors' eyes, have brought some key benefits to the end investor. The key benefit being the ability to access diversified investments at a much lower cost. Regardless of these recent comments from the SEC, it is clear that ETFs are not only here to stay, but also a continued growth segment of the investment product universe.

## Changing Technology

As an industry, we tend to look at today's technology as if it's extremely disruptive. Although this is true, the technology revolution didn't just arrive; it's been incrementally impacting the business for over eight decades. As we were finalizing this chapter, someone correctly pointed out that we didn't go far enough back in talking about technology's impact. The technology impact on the securities industry goes all the way back to the universal ownership of the automobile. Up until the 1940s, most people with financial assets lived in cities. The ownership of the automobile caused geographic dispersion. Suddenly firms wishing to do business with the wealthy opened branches outside the cities. Charlie Merrill was the leader, with his campaign: "Bring Wall Street to Main Street." Technology was so expensive, only the largest firms could afford it and do business with it. The biggest firms on Wall Street had the advantage because they were the only ones with certain information.

A look back at personal finance articles through the decades has to make you laugh given where we are today as advisors and investors. In a December 1983 article in *Changing Times* magazine, the predecessor of *Kiplinger*, the author took note of the computer blitz:

As in so many other fields, the computers have taken over in financial planning. The odds are that the information you give the planner will be fed into a computer and massaged into impressive arrays of figures. The more sophisticated programs can perform marvels such as calculating taxes in various ways to find the lowest-cost method.<sup>4</sup>

At a time when Elon Musk was warning the United Nations to ban work on artificial intelligence robots because of his concern they might take over the planet, tax-calculating computer software hardly seems groundbreaking.

As the United States and other countries struggle to keep ahead of hackers and terrorists, what is often overlooked is the regulatory change necessary to deal with the advancing technology landscape. These regulatory changes are particularly challenging in the financial services industry. Although this seems like a small issue, it's relevant to firms trying to build their value proposition for small accounts using digital technologies. Commissioner Stein observed that the SEC is now thinking about what it means to regulate a robo advisor, a concept that did not exist when most of the laws governing investment advisors were drafted. Stein stated:

What does a fiduciary duty even look like or mean for a robo advisor? The idea of a robotic entity that automatically generates investment advice certainly bumps up against what we would traditionally think of as a fiduciary. As this innovation gains more market share (as it seems poised to do), we should be asking whether these new robo advisors can be neatly placed within our existing laws. Or, do we need certain tweaks and revisions? Do investors using robo advisors appreciate that, for all their benefits, robo advisors will not be on the phone providing counsel if there is a market crash?<sup>5</sup>

Keep in mind that the Investment Advisers Act became effective in 1940.

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<sup>4</sup> "Financial Planners—How to Find the Right One," *Changing Times* (December 1983), p. 30.

<sup>5</sup> Commissioner Kara M. Stein, "Surfing the Wave: Technology, Innovation, and Competition—Remarks at Harvard Law School's Fidelity Guest Lecture Series," November 9, 2015, [www.sec.gov/news/speech/stein-2015-remarks-harvard-law-school.html](http://www.sec.gov/news/speech/stein-2015-remarks-harvard-law-school.html).

We believe that robo technology that offers investors a 100 percent do-it-yourself approach will present challenges to most consumers. We believe it's analogous to the pursuit of driverless cars. In 1989, the movie *Back to the Future 2* predicted we would have flying cars by 2015. This seems just as unbelievable and futuristic today as it did then. However, it seems certain we will have driverless cars someday, likely before flying cars are possible. Although prototypes are in the works, we still don't have driverless cars, let alone flying automobiles. Will we get there one day as a society? It's likely. However, the pursuit of the goal has been much more expensive and much more difficult than those inventing them believed it would be.

This isn't some off-the-wall tangent. In researching the pursuit of driverless cars, we found the pursuit parallels the emergence of do-it-yourself financial advice technologies. It isn't the mechanics of driverless cars that is impeding their adoption. The technology is currently failing when things don't go as planned: a human driver doesn't follow the rules at a stop sign, or there's rapid lane change by a driver texting and drinking coffee while driving. These anomalies require quick assessment and reaction that computers have yet to figure out. Sound familiar? Like driverless cars, the markets work most of the time, under typical conditions. It's when the markets are volatile that consumers need advice. Assessing the do-it-yourself capabilities during the majority of the time or in periods of normalcy may lead investors to very different conclusions on the need for human financial advice. When the market swings like a crazy driver switching lanes, the true role of professional advice needs to be assessed.

The financial services industry has come a long way over the past five decades. It continues to move from being product centered to being advice centered, and technology and regulations continue to push advisors to do things differently, hopefully for the better.

Our journey through the past in this chapter was designed to set up the realities of where we are going in the industry. We interviewed a wide variety of industry leaders, practitioners, and consultants. One of the questions we asked everyone was, "How disruptive do you see the current forces being on the future of the financial services industry?" The answers were across the board, with some people saying it's a consumer revolution, not an evolution, and others believing that every

10 years something disrupts the industry, but good advisors can help their clients weather the storm. We will sort through these differing opinions in the coming chapters. In the end, clients need advice and we as an industry are here to deliver it.

## THE CONSUMER PERSPECTIVE

Pam Krueger believes consumers should have realized that up until the mid-1980s, people invested for only two reasons: (1) they were well off and wanted to continue building their wealth, or (2) they wanted to play in the market. The average American didn't feel as compelled to invest because Social Security and a company pension was enough to fund retirement; investments weren't necessary. Average investors still kept their money in bank accounts and CDs. They trusted their employers and the government, and they had secure futures. Most Americans didn't have to make investment choices, because their pension plans did the investing for them. As the 401(k) came online, it democratized the investment process. The financial services industry saw this as a positive change because it put the investor in charge. On balance, it has been a good thing. However, as people are forced to make more decisions on their own, it has caused consumers to become frightened. This fear has led to inertia, which causes investors to do nothing. To give themselves the opportunity to achieve their financial goals, it is imperative that investors be proactive.

When consumers were less dependent upon investing to fund their retirement and other long-term goals, dabbling in the stock market was viewed as a hobby. If they invested in a company that lost money or went bankrupt, it was upsetting, but not dream crushing. But today's investors are in an entirely different situation. On the one hand, they are far less likely to have pensions and, with interest rates near zero, today's consumers must become active investors if they hope to retire and achieve other life goals. On the other hand, a negative investment outcome could be devastating.

### Digitizing

The financial industry is really proud of itself for coming up with all kinds of great tools. However, these tools might give the consumer vertigo. In some cases, these tools have driven assets to places like Schwab and Vanguard, brands that have successfully communicated the value of automated advice. The digital tools that the industry is so proud of have only caused bigger problems for consumers. For

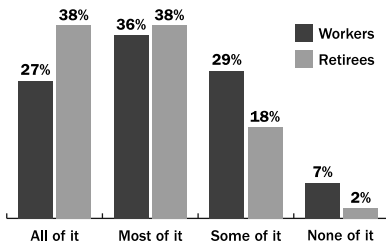
those who are already apprehensive about making investment choices—and suffering the consequences—alone, digital tools can seem even more daunting and lonely.

### The Trust Gap

A trust gap remains where even consumers that do seek advice are hesitant to follow it. See Figure 1.1. In 2013, one in four consumers who paid for advice implemented 100 percent of the advice. The number one reason cited for not following that advice was lack of trust. Given the scandals of the 1980s and 1990s along with this heightened need for the returns on investments, it's easy to see why a trust gap exists between the investing public and the industry.

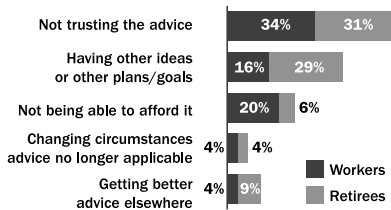
**How Much of the Investment Advice Did You Follow?**

Receiving advice in 2014: Workers N=239, Retirees N=152



**Reasons for not Following All of the Advice**

Receiving advice in 2014: Workers N=239, Retirees N=152



**Figure 1.1** The Trust Gap

### KEY TAKEAWAYS

- Although the pace of change is picking up in the financial services industry, reacting to changes has always been the hallmark of successful advisors. Consumers feel either empowered or frightened and overwhelmed into inertia. By failing to do anything with their money, it loses value and fails to keep pace with inflation. To overcome inertia, consumers want someone to drive the car for them.
- The push and pull between technology and regulations are going to be a major driver of future industry change.

- While the industry moves from product centered to advice centered, the investment products in client portfolios have changed and will continue to do so.
- The pressure has mounted on clients to achieve positive investment outcomes to reach their goals. It is unlikely they will have a pension to plug the gap between their Social Security income and what it will take to live a comfortable retirement.
- The trust gap that exists between the industry and the investor will continue to be a problem that advisors need to overcome.