

EXPECT THE UNEXPECTED

A chance occurrence might just be the opportunity for you to provide reassurance and insight for clients

Investment markets have provided a rollercoaster ride so far this year, and advisors are facing a renewed sense of urgency from rattled clients.

Reassurance, insight and guidance are in high demand in volatile markets. It's an excellent opportunity to provide value and secure client relationships. "Chance favors the prepared mind" is a quote attributed to the 19th century French scientist Louis Pasteur. He acknowledged that the universe, and thus life, is asymmetrical and that we are better off being ready for the unexpected. Indeed, scientific advancement has often been predicated upon chance events or observations. But, how does one "prepare"? And what is this "chance" for which we should all be prepared?

"Know Thy Client" is a popular mantra which also captures a core idea of having a prepared mind. Client knowledge is, of course, foundational, but it is particularly critical when "chance" comes knocking at the front door. The prepared mind is ready for chance because knowing a client thoroughly will help an advisor view life's inevitable chance events through a lens that is client specific. For example, clients may be tempted to seek the refuge of cash during market turbulence, and need the prepared mind of an advisor to refocus on their investment program and meeting obligations subject to inflation. Knowledge and perspective allow an advisor the invaluable opportunity to keep clients on course when chance appears to go against their interests.

In the world of investments, chance can be viewed as risk, which is client specific. For some, historical volatility numbers may appear acceptable in the context of a long-term horizon. But, the potential for periodic shortfalls can be masked by statistics

such as standard deviation that rely on mathematical averages. So, for a client with regular and unalterable cash flow needs, there may be little comfort in a favorable historical volatility number when obligations come due. Risk should also be thought of in an integrated fashion, where a diversified portfolio (or life) can change dramatically due to the unforeseen forces of chance. The unpredictable reach of the U.S. housing downturn, for example, has yet to fully unfold.

To date, we have seen the unexpected, including writedowns not only across Wall Street, but among regional banks in China and Germany, as well as the specter of some money market funds exposed to a weakening mortgage market. Regional economic weakness is stressing state budgets at a time when anxiety reigns over the municipal bond market due to the perilous condition of major bond insurers. Thus, advisors would be well served by keeping abreast of local economic issues, such as taxes and budget actions, which may affect client interests.

Also, global equity markets have long been moving in tandem, and global economies appear to be following suit. The great global decoupling story, in which emerging economies are less reliant on the U.S., may soon go the way of the late 1990s "new paradigm" or dotcom phenomenon. Qualitative insights may trump quantitative risk measures in the effective management of exposures in the current market environment.

A perceptive advisor will question assumptions and beliefs in an effort to properly define risk, and recognize that chance offers opportunity as well. Contingency planning and 'what if' scenario exercises can help set the stage for you and your clients to be favored by chance, or be prepared for it. ■



** Clients may be tempted to seek the refuge of cash during market turbulence. Help them refocus their investment programs.*

** Keep up on local economic issues like taxes and budgetary actions.*

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