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Crisis Investment 101 – 5 Steps to Take Before Your Clients Invest

Dear Valued Members of IFPAS,

I've written this article as a consultant, for consultants – in the hope that it will encourage you during this particular crisis. Most of us have experienced changes to our business in a manner like never before.

The Investment Business is particularly tricky because it is full of contraries. Covid-19 is unlike the Global Financial Crisis and previous epidemic-related crises. Food, which would typically be considered an essential and defensive sector (and by extension a theoretically great place to invest) has given a mixed bag of results due to retail failure, while places like Domino's have thrived.

As financial practitioners, we have a responsibility to our clients to give them the highest assurance to do business with us during a time where everyone is tightening their belts, trust may be at an all time low, whilst fear being possibly at an all time high for some. By taking these 5 steps before your clients invest, I believe that you can continue to run a sustainable business even in the now and especially in the future.

Step 1: Additional Safety - Having Reserves

As a consultant, you need to ensure that your clients can uphold the budget that they intend to set for investing or a specific investment.

Most of us are familiar with the '6-month expenses as an emergency fund' rule of thumb. If we're considering a Regular Savings Plan (RSP) as an investment, its obviously an asset but one that shouldn't be used for an emergency.

This requires us to file it under 'Expenses', where if the client decides to commit to $1000 per month, whilst their expenses prior to that were $1500 per month, their total then should be $2500 per month.

Thus, their 6-month expense should be calculated as $2500 x 6, instead of $1500 x 6, prior to investing. Furthermore, we have to realize the rationale behind the rule of thumb and remember that Financial Planning is a very personalized and customizable experience.

Factors that can change this rule of thumb are:

a) Lack of Job Security: Not all jobs are equal. It's partly why the government gauges our income as 70% of what we made the previous year when we go through credit underwriting. Similarly, your client's job may not be as stable – perhaps as an employee, franchisee, entrepreneur or otherwise, and they may require a few more months of emergency funds.

b) Upcoming Short-Term Expenses: This is in relation to postponed plans and expenses, such as trips. There tends to be enormous consumer kickback and forced delayed gratification (such as the inability to travel as a prominent example) that could result in higher anticipated expenditure.

c) Upcoming Large Expenses: This may relate to postponed MAJOR short-term plans, such as marriage, housing, etc. There may have been perhaps a lack of financial prudence during this period which results in unpreparedness or additional liabilities that have been largely overlooked. It helps them when this is raised to their attention so that their long term plans isn't compromised with short term ones.

d) Wear and Tear Sudden Expenses: This is something people tend to overlook but is especially prevalent in Covid-19. For example, my computer and air con has been working much harder than usual. Due to more time as well as work from home, it is likely some of your things will wear and tear more, which may result in additional unanticipated expenses.

Step 2: Purpose - with Intelligence, Versatility and Commitment

Clients need to set goals because investing is not a consistent process of making money. You can go 3 years without making money at all before you suddenly double that amount in a year.

Identify and help client set goals as well as time horizons so that they can look forward to them, based upon projections and reviews of investment performance during that period.

For example, in relation to tertiary planning, the client may say, 'I want to plan for my daughter's education. She is 2 years old and when she gets to her first year in university, she'll be 18, so I want to invest in something for 16 years only.'

However, over the course of time, his daughter gets into university at age 22 or 23 via the ITE and Polytechnic routes respectively.

Should the investment period be extended and risk profiles be relooked? What happens if she wants to get a Master's or a PhD after that?

On the other hand, she isn't inclined to go to university and prefers to start a business. How would you approach this change of circumstances, given she may want to have access to the money? Will the market conditions be favourable, at the time of request to withdraw?

So that's a problem as well, which needs to be discussed so goals are set clearly and concisely as well as reviewed every year.

These actions will help to ensure :

- You add value as an advisor, not just an instrument offering
- Showcase credibility and experience
- Increase service quality

Step 3: Anticipating and Explaining What Could Happen

People have varying views over what could happen with the stock market. There are a lot of theories by many institutions and analysts. However, when the dust blows over, like every crisis that has come along in history, most of them may not be as accurate as presumed in the beginning.

A problem is that Covid-19 has almost all the characteristics of previous financial crashes.

In a disease-oriented crash, which is similar to SARS, H1N1, or even the Spanish flu, what has typically happened is that after a sharper surge of losses in the stock market and the general economy, the market exhibits a V-shaped bounce where it recovers extremely quickly.

Humans are both quick and adaptable to the situation. This is not too dissimilar from, when there is an adverse impact on people, for example, in a very cold country. Of course, there are initial difficulties for sure, but people learn eventually to adjust and create methods of survival for themselves.

You may notice that in using this analogy, the winter is not solved.

There is no cure, if there is no vaccine. What happens is that the market rebounds when optimism and adaptation arrive. Based on that logic, the stock market could go up and improve or exceed on that past performance.

Of course, it could also go down. For example, if you look at the Global Financial Crisis or any other critical period where there was severe unemployment loss, the correlation is pretty high and there are typically a couple of false starts where we assumed the market would recover before it simply plunged even lower.

That's a serious and distinct possibility as well, in that it could just go even further down.

The last possibility is in relation to a general sideways movement. This just means that it goes up and down, but it tends to stay fairly stagnant like corrections in 2014. The market will constantly try to recover, and there will be people who contribute both from the government and the private sectors. Not a lot can be done until it experiences actual recovery in relation to an actual boost in return, whether political or consumption-wise. And the lesson in there is it isn't useful to theorize or border on any conclusion about what could happen.

Nevertheless, by going through these things with your clients, they will understand that there is a range of possibilities of how their monies could be affected in the short term, so that they can relate better to those issues and keep trusting you in the long term.

Step 4: Understand Where You Come In

How we come in as advisors is by following some time-tested and good advice based on statistical facts. Regardless of how the market goes, advisors still have to do risk profiling, which is the ability and willingness to take risks. This does not and should not change in the face of a crisis.

We are not just instrument providers. We are advisors. We also have to do proper portfolio construction, and it has to be statistical analysis at the very least or as a point of reference. We have to review regularly, and very importantly, we have to do some major strategic shifts in the event that our fundamental understanding or assumption is challenged.

What that last part means can be best illustrated if we look at case studies such as Nokia, which was largely considered a blue-chip stock, or local case studies such as Singapore Press Holdings. You may notice that most of these companies, while they remain fairly large companies with capitalisation, are no longer considered a solid investment even though they were considered a decent investment for several decades.

This would be an example of a fundamental shift in relation to types of stocks. Also, if you look at it on the sectors as a whole, media or print has been completely affected since technology disrupted them. A clear example of this is the impact on stand-alone cameras as a sub-sector of IT.

If your clients had mindlessly bet on their preferences or their beliefs on what would succeed in the long term, they would bleed a tremendous amount of losses over time.

That is where the expertise of advisors can make a difference. We need to continually be abreast of the market and doing the job our clients should not have to do. Most importantly, we need to be confident in our execution of buying and selling when the time is right according to the goals they have set and the decision they have made based upon those reviews. As there may be varied emotions a client may be go through, such as fear or even a sense of over-indulgence like greed, these can emerge and be MOST PREVALENT during a crisis like the current one. Therefore, it is critical to help them navigate those moments with clarity as well as based on the due diligences conducted in those reviews.

Step 5: Put Your House in Order

The best thing you can really do for your clients, perhaps even before Step 1, is to ensure that your business is steady. And this requires being part of the adaptability that I talked about in Step 3.

Despite the range of experience, it is safe to say many financial practitioners who have done this business for a long time, may have never experienced anything on the scale of this magnitude. This is unprecedented and without parallel, even if this is compared to those severe crises such as Asian Financial Crisis (1997), Dot Com (2000) and GFC (2008).

Based on the presumption most financial practitioners are financially secure, I venture with a suggestion to you which is, to try adaptations to the ongoing situation based on available resources and financial comfort. Seeing there are alternative ways of operating in the face of Covid-19, it may present a more appreciable understanding of those adaptations, as discussed in the paragraphs prior, as well as with an implementation of some.

After all, the easiest and perhaps most effective way to show your clients as well as future prospects a good financial consultant, is to lead by example and experience.

If your expertise cover investments or savings plans, since you are doing this for yourself, this will provide you a great vantage point in your financial practice and advice to clients. Specifically, it may help you relate ideas better on how they can adapt, how they can keep an active income and what they can do if they potentially lose it.

This will accomplish the following:

1) Show your clients, demonstrating your expertise as an advisor and your knowledge, as a consumer

2) Add value to your client on the basis of your experience

While there are limitations and challenges to our business, I remain confident that we will breakthrough as a profession.

In this time of crisis, more than at any other time, it maybe a positive and telling moment where financial practitioners can bring a wealth of value to the country and its citizens by encouraging and reinforcing good financial habits and practice, that may help promote their sense of well-being and possibly even prevent, a financial ruin for years on end.

I wish you all well.

About the Writer

Luke Ho is a licensed financial practitioner and an active IFPAS member. He is also an Associate Financial Consultant. In 2019, he qualified for the prestigious MDRT award and has confirmed his placement for 2020.

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