Inflight advice

How to beat the fear of investing

The airline and investment industries have much in common, argues AMP Capital's Anthony Edmonds – they both aim to safely deliver their customers to their chosen destination, while negotiating a series of mostly known risks. You may encounter some turbulence, but buckle up (and note the exits) as Edmonds pilots the analogy to a smooth landing

By Anthony Edmonds

Like Marge Simpson, I have a fear of flying. The idea of plane travel fills me with dread and given I have to travel for work, it is a fear that I have to confront on a regular basis.

My fears were certainly not alleviated when I read about the missing Air France flight recently. And as I was thinking about planes and crashes, I realised there are some parallels between the investment industry and the airline business.

Both industries need to set goals and manage risks for their clients, both have to travel with their clients through the ups and downs and both need to focus on providing a good service to ensure the journey meets their clients' expectations. Then I found myself thinking that if there was a battle between which industry does these things better, who would win?

Setting goals and managing risks

The airline industry sets goals and manages risks for their clients well. Admittedly, it is easier for an airline to set goals with their passengers than it is for the investment industry – passengers usually know where they want to go.

Airlines also make the risks of flying clear to their passengers and put checks in place to try and minimise them: the tagged bag (yes it can get lost); departure updates (yes it might be delayed); and the safety briefing (yes planes do crash). Sure it won't necessarily ensure you get your bag back, get there on time or that you survive "in the unlikely event of an emergency", but it does help to control expectations.

Passengers on US Airways Flight 1549 described how calm everyone was in the final moments before crashing into the

Hudson River. Perhaps this was because, before they took off, they understood that there was always that possibility.

On the other hand, often when clients contact us they haven't really thought about their objectives. And does the investment industry really have the appropriate checks and warnings in place to minimise the screaming and panic from clients if things do go pear-shaped?

Determining a client's investment objectives is essential in helping them understand what the journey will be like, the risks involved and to avoid a lot of problems later if things don't go to plan. You only need to point to the collapse of the finance companies and CDO funds to see that some investors were not aware of just how risky the investments were and that this is an area that our industry needs to fine tune.

The experience and returns your clients get should not be markedly different from the one they expected. For example, while your client might be happy if they get a return that is much higher than expected – it's a bit like landing in Vomo Island when you thought you were heading to your in-laws in Palmerston North – in reality, they should be just as alarmed as if they had lost more money than expected.

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A good goal-setting and risk management tool used by many is creating a written statement of investment policies and objectives, or a SIPO.

The process involved in writing a SIPO means that clients are forced to clearly articulate their objectives and understand the risks they are taking. It also requires the investment provider to clearly state expected returns and the potential variance of these returns, taking into account market fluctuations.

Focus on what you can control

Imagine an airline that promoted itself on having the smoothest flights. Inevitably this airline's passengers would have a bad flying experience because there are a massive range of external factors that the airline can't control, including turbulence.

I see this as being similar to an investment manager or adviser saying they generate superior returns. Chasing high, short-term returns usually results in crashing. The bottom line is that everything goes in cycles and if your portfolio is well diversified, components of your portfolio will be weaker and stronger during different parts of the cycle.

The best strategy is to clearly identify these investment objectives and long-term strategy through a tool like a SIPO and to stick with it.

A large part of the experience you have on the plane is driven by the in-flight service, as opposed to the quality of the flying itself.

Rather than trying to focus on beefing up returns, I think good advisers put their efforts into the key thing they control – the service they provide. And people do value better service and greater comfort along the way – what about all of those passengers in business class, paying up to three times as much as the ones riding in economy?

The truth is all the passengers travel on the same flights, get to the destination at the same time, and run the same risks of being delayed or, heaven forbid, not even making it.

Good investment advice is about so much more than just investment performance. Good advice covers a huge range factors like establishing the client's investment objectives; determining a client's tolerance for risk; providing tax advice; recommending appropriate ownership structures (like family trusts); ensuring a client's investments are securely held; educating clients about investment-related issues; communication and reassuring them when things are a bit bumpy.

Conclusion

Preparing a document such as a SIPO as part of the standard advice process is something every adviser should spend lots of time on. This helps everyone to understand the objectives, how these are best achieved and the risks involved. Those in the industry who are client-facing need to focus on providing quality service to their clients not generating investment performance.

And here is where we return to Marge. Her fear of flying came from the fact she was too embarrassed to admit that her father was an apron-wearing flight attendant, not a pilot. This sounds familiar to me. When asked, I often say that I am an 'investment manager'. Maybe I need to man-up and admit that, like Marge's Dad, in reality I am in charge of service and in-flight entertainment, not flying the plane. A