



Pushing Investment Responsibility Elsewhere!

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In one of the most revelatory events I could ever have imagined, I recently spent three days in Philadelphia at the Schwab Impact 2004 Convention for investment professionals who have a business relationship with Schwab. This was the first of these meetings I have attended since our firm began to use Schwab as the custodian for the assets of our investment management clients in 2000. One woman with whom I spoke told me she had been at all 14 such Schwab conferences and had watched them grow from a few hundred people to the cast of thousands attending this year.

Money Talks

As a person who has been in the investment business for decades, what hit me like a ton of bricks was the degree to which this gathering was a veritable bazaar of competing mutual fund companies paying Schwab large sums of money to garner the attention of those gathered. There were exhibitor booths, sponsored meals, polar fleece vests, hats, bags and briefcases, all embroidered with the name of one fund company or maybe three. Don't get me wrong. The educational programs offered were excellent and highly useful lectures. Topics included the myriad changes in Government rules and regulations, new SEC record keeping requirements, how to better attract more clients, how to sell them annuities, bonds, hedge funds, or life insurance, how to use U.S. Trust (which Schwab owns) for your clients, and how to better manage your business using the latest technology platforms (available from Schwab at added fees).

I was thrilled to be a part of the standing ovation for President Bill Clinton when he took the stage to expansively discuss the issues of the day and a post mortem on the recent elections. Before Bill was introduced, the president of a mutual fund complex, who reportedly paid \$100,000 to precede the President (but not introduce him), spent five minutes thanking the overflow crowd for recommending his funds to their clients over the years!

Ring out the Old, Ring in the New

The dramatic changes in the investment management industry in recent years were unmistakable at this conference. I have spent my investment lifetime first as an analyst and then as a portfolio manager. My idea of an "investment conference" is meeting with managements and analyzing companies; listening for trends and finding interesting new investment ideas. This conference had nothing to do with that old paradigm. This was a reflection of the new reality. Today many people in the investment business in their thirties and forties don't know the first thing about constructing a portfolio, analyzing a security, or knowing that the Enron business plan or that of MCI didn't make sense; forgetting the culture of fraud and deception that plagued both of them .

Passing the Buck, Chuck

Account executives have been trained by Merrill Lynch, Smith Barney, Morgan Stanley or whatever firm you use to sell you comfort, their brand name and perhaps a financial plan to make the whole thing sound convincing. You hope that they know more about investing than you do. What they know a lot more about than you do is sales, not investments. They are acutely aware of that and, more importantly, so are their bosses. This construct is deliberate. The people at the top of these firms don't want to be sued because a broker bought you a stock that was not appropriate for your investment goals. Nor do they want to be sued because a research analyst wrote a glowing report on a stock for retail customers while telling his friends in emails that the company was a dog, which is what Henry Blodgett did. He was fired from Merrill Lynch with a several million dollar exit package. Quite a punishment for a breach of ethics, don't you think?

We've Got a New Plan, Stan

By design, the new model is to avoid selling you a stock or a bond unless you specifically ask for one and they can't convince you otherwise. The new model is to sell you one or more mutual funds or a managed account from an investment advisor that might be part of a "Wrap Account Program." Fees change hands for the referral of your business by the broker. When Schwab tells you it has a select group of funds or Investment Advisors from whom you can pick, rest assured Schwab is being paid a fee by the group of firms it is referring. Those fees must be disclosed to you but you might not notice if you don't read the small print. Their key idea is that the investment decision maker is somebody other than your broker. Like any good salesman, they want to sell you the products that generate the highest commissions. Nothing pays the broker a higher commission than selling you an annuity or a mutual fund with a big upfront load!

Being on the Top Shelf

Consider this. There are now many thousands of mutual funds offered for sale. Do you honestly believe there are thousands of excellent managers out there? Believe me, there aren't. That's why picking one is a chore beyond belief. It's just like going to the supermarket where the consumer products companies pay for shelf space. You are more likely to buy the cleanser at eye level than the brand on the bottom shelf. You are more likely to select a mutual fund for your clients (if you are an asset gatherer, not a manager) from a company that has wined you and dined you or that has spent a lot of money on advertising so your customer has heard of it. Decades ago, the SEC allowed fund companies to charge a "12b5 Marketing Fee" to existing clients to promote the fund to new prospects. Mario Gabelli once said to me that you had to be brain dead not to use this perfectly legal method of having your clients pay for you to promote your business to new prospects. A major lobbying effort got this accomplished. Remember that when you read in coming months about the new move to privatize Social Security. What would be more of a bonanza for the big investment houses than that torrent of newly investable money?

The Moral to this Story:

Pay very close attention to what you are buying and from whom you are buying it. Ask about their experience level. Have they lived through many market cycles? Are they Chartered Financial Analysts (the industry gold standard of training)? Understand how

they are compensated? Ask to speak to some other clients? Are they going to invest your money themselves or farm your funds out to others with added layers of fees? Do they really understand about investments and your needs? Do they care? Feel comfortable with the answers to all these questions before you proceed. If you're not, keep looking elsewhere.

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