Problems with Today's Wealth Management Industry

Christopher Casey of WindRock Wealth Management was interviewed concerning the state of the wealth management industry as well as WindRock's investment philosophy and its current view of the financial markets.

Question: Although WindRock Wealth Management is a US-based Registered Investment Advisor which manages money for wealthy individuals, you certainly seem different from other firms out there. One of those differences is your adherence to the Austrian school of economics. Why is that important to WindRock?

WindRock: We think it's a tremendous advantage. And you're right – as far as I can tell, **no other wealth advisory firm** utilizes Austrian economics as a tool. We think it's *vitally* important in designing portfolios. Austrian economists, unlike the mainstream Keynesian economists, understand what truly causes inflation and recessions – the artificial expansion of the money supply by central banks. Since these are the two greatest threats to anyone's investment portfolio, this understanding is critical. This is why other wealth advisory firms herded their clients right over the cliff with the crash in technology stocks and later with all equities in 2008. They could not foresee these events, along with the collapse in housing prices, because they don't comport to their flawed models and theories. For the same reason, they do not foresee any danger with today's overvalued US equity markets. By using Austrian economics, we have a time-tested tool to guide our decisions.

I should make one more point about economics and other wealth management firms. As I said, many adhere to Keynesian economics - they basically parrot what the Federal Reserve and other mainstream organizations predict. And the Federal Reserve in particular has a horrific track record in this regard – having completely missed the 2008 recession, the housing crisis, and the collapse in tech stocks. But perhaps just as amazing, many wealth advisory firms have no view on the economy! I cannot tell you how many times I have asked a Chief Investment Officer of a major wealth advisory firm what causes recessions, and their response is either "**we don't know**" or "**we're agnostic as to the economy**" – whatever that means.

Question: Recessions pop asset valuations, and are thus a threat to anyone's portfolio, but what about inflation? What do you see going forward and how do you position clients accordingly?

WindRock: The actions of the Federal Reserve since August 2008 – and shockingly all central banks in the developed world – are truly unprecedented. Depending on how you measure it, the US money supply has more than quadrupled since the Great Recession. Increasing the money supply to this degree will inevitably cause significant price inflation. It may not show up in 2015, it may even be preceded by an asset deflation, but it will develop. When this happens, stocks will, *at best*, be flat in real terms. And bonds will be decimated. The only way to protect one's wealth is to invest in precious metals and certain types of real estate – mainly farmland and rental real estate. Positioning one's portfolio as such will not only offer protection, but great profit. And this isn't just based in theory, but in experience. The historical performance of these investments in the 1970's in America offers great guidance – while the price index more than doubled in 10 years, farmland and gold provided tremendous appreciation.

Question: So how do you use Austrian economics in designing your portfolios?

WindRock: Our clients' risk profiles and liquidity needs are integrated with our projections of real economic growth and price levels over the next twelve months. We then combine this with our judgment as to overall asset valuations in the equity and debt markets to determine the allocation between stocks, bonds, and hard assets such as real estate and precious metals. After determining these broad allocations, those same assessments dictate the constituent parts of each allocation. For example, if we are in equities, how much is in emerging markets versus the developed world? How much is defensive versus aggressive, etc.?

One additional item I should note about portfolio construction, we do not believe in "putting all of your chips on red" and waiting for the big payoff. By that I mean we select investments we expect to do very well when the economy plays out the way we expect, but they will also do well in the interim due to the compelling risk and return profile the investment itself offers. As an example, we believe multi-family rental real estate will do quite well in the US when a housing decline unfolds due to rising interest rates. The multi-family rental real estate vehicle we utilize is projected to almost double a client's money in three years – even without a housing market decline. We did not go out and buy a publicly traded rental real estate vehicle (they are currently overvalued) which may do well in a housing decline – we found an investment which will do well regardless since it is building a new type of multi-family housing community.

Question: What else differentiates WindRock from other wealth advisory firms?

WindRock: It's not just about having a different view on how economies work. It's about what you do with that knowledge. It's about having an entrepreneurial mindset to act on these opportunities - to seek out and vet investment vehicles which the mainstream wealth advisory industry won't touch. I think we describe this well on our website where we wrote:

> *Conventional wisdom associates the word "entrepreneur" with the assumption of risk. While risk can never be fully avoided, what actually makes entrepreneurs unique is their understanding of risk. Our unique insight of the risks posed by governmental interference in the economy serves to protect our clients' wealth. As entrepreneurial-minded advisors, we emphasize independent and creative thought to boldly seize opportunities while minimizing key risks.*

Farmland is a great example. There are very few public farmland vehicles – Real Estate Investment Trusts – or REITs, in the US. Accordingly, there are no investment benchmarks for farmland to be considered by mainstream wealth advisors (because the sample size is too small). Therefore, mainstream wealth advisory firms will not consider an investment in farmland. Mind you, it's not because the investment opportunity isn't there, but because they cannot be viewed as performing out of sync with the commonly used real estate investment benchmarks. To do otherwise will entail risking their careers. This is a real problem in the wealth advisory industry – **advisors are worried about losing clients, not with losing clients' money**. The mainstream wealth advisors are happy tracking what everyone else is doing – because in so doing, they believe they are preventing their clients from switching to another firm. This "career risk" syndrome forces wealth advisors into short-term outlooks with a herd-like mentality.

Question: Besides the lack of an economic viewpoint (or an incorrect one), besides the "career risk" mentality, what other problems exist within the wealth advisory industry?

WindRock: Misaligned incentives. Many firms lack independence, meaning they create and market their own investment vehicles. So oftentimes they're not just advising clients to own a particular type of investment – they're advising clients to own their investment. Which certainly means additional fees and probably a sub-performing investment vehicle. I cannot tell you how many times I have reviewed a prospective client's investments only to find they are heavily invested in their advisor's funds. **Is it really that likely that the best emerging market equity fund just happens to be owned and run by the advisor's firm**? That the very same advisory firm has the top currency fund? What are the odds?

Question: So the XYZ Wealth Management Firm owns the XYZ funds . . .

WindRock: I think common sense and anecdotal evidence suggests that if you examined client statements from all wealth advisory firms, you will not find the ownership dispersion you would expect if wealth advisors truly provided independent advice. This Wall Street sales culture permeates many firms. Unfortunately, **the more wealth advisors serve as salesmen, the less they act as a trusted advisor**.

Question: With all of these problems in the industry, why should investors even consider using a wealth advisor?

WindRock: Doing it yourself can be an option. And perhaps a fairly viable one when compared to the alternative of using many of these firms. But there are still compelling reasons to use a wealth advisory firm. For example, since wealth advisors possess buying power by representing numerous clients, we can have access to certain investment vehicles which may simply be unavailable to the individual investor. In addition, we can negotiate lower fees and minimum investments with the funds we utilize. Specifically, with our main farmland fund, we negotiated a 50% reduction in management fees and reduced minimum investments. But in a greater context, maximizing returns and minimizing risks for any investment portfolio requires time, research, money, judgment, and knowledge. It's a full-time job, especially in today's world of massive government intervention in the economy and the financial markets, to manage a portfolio. This is why we created WindRock, because wealth advisory has its place – it just needs a different economic viewpoint, a unique investing mindset, and greater independence.

Question: How can anyone interested contact you to learn more about WindRock's services?

WindRock: Of far greater importance than what we do is what we believe. All of our marketing is driven by thought-leadership, so I encourage any interested parties to visit our webpage at www.windrockwealth.com to read about our philosophy as well as our regularly posted research and analysis. I also suggest interested parties to sign up for our mailing list.

About the Interviewee

Christopher P. Casey, CFA® is a Managing Director at WindRock Wealth Management (www.windrockwealth.com).

Combining a degree in economics from the University of Illinois with a specialty in the Austrian School of Economics, Mr. Casey designs investment portfolios to maximize returns and minimize risk in today's world of significant government intervention. Mr. Casey can be reached at 312-650-9602 or at chris.casey@windrockwealth.com.