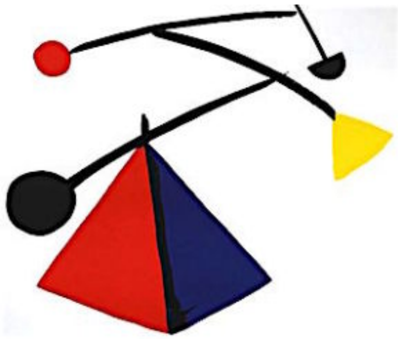
Curve, Triangle or Rectangle: What Kind of Advisor Are You?

By Kerry Pechter *Thu, Jul 27, 2017*

At the Retirement Income Industry Association's 2017 Summer Conference, founder Francois Gadenne asserted that advisors can protect themselves from automation, regulation and commoditization by advising in three dimensions.

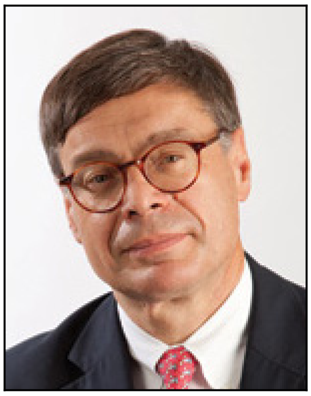


Retirement advisors can be either "curves," "triangles," and/or "rectangles," but it's best to corral all three symbols inside a holistic circle and use them as a framework for serving the best interests of the retirement client, said Francois Gadenne at the July 17-18 meeting of the Retirement Income Industry Association (RIIA).

Quick definitions: A "curve" advisor focuses on investment management. A "triangle" advisor helps facilitate a client's goals and aspirations. A "rectangular" advisor considers a client's entire household balance sheet, including all assets and liabilities, along with investments.

Advisors who master this entire model—by obtaining RIIA's Retirement Management Analyst designation, as a start—will survive and prosper in the Ice Age of commoditization, automation, regulation and fee compression now chilling the wealth management industry, said Gadenne: "You can demonstrate compliance just by checking off the boxes of RIIA."

"The advice industry faces its most disruption ever," Gadenne (right) told a group of 40 or 50 at RIIA's 2017 Summer Conference on the campus of Salem State University in Salem, Mass, where he released a workbook, written by Gadenne and investment analyst, educator and author Patrick Collins, Ph.D. He founded RIIA in the Boston area over a decade ago and remains its chief executive.



RIIA's 148-page workbook describes the Curve-Triangle-Rectangle-Circle concept, which Gadenne says advisors can use as a framework for professional education and client communication. It builds on RIIA's "View Across the Silos" (a cross-sectional map of the retirement industry and market), its "Floor and Upside" strategy (of dedicating assets to a combination of safe income and risky investments in retirement) and its "RMA Procedural Prudence Map," a process for serving retirement clients.

The shape of things to come

Here's an attempt to defined the most important elements of the Gadenne-Collins paper that was introduced in Salem:

The Curve. Advisors who are curves limit themselves to portfolio management. The curve is a reference to Modern Portfolio Theory and the efficient frontier. Those two models, along with each client's answers to questions about risk tolerance and time horizons and the risk-free interest rate, provide the bases for many advisors' asset allocation recommendations. This type of advisor focuses on risk/return optimization.

The Triangle. Advisors who are triangles practice so-called goal-based planning. Clients describe their essential, desirable and aspirational goals and the advisor helps them finance the achievement of those goals. The image of a triangle refers to Abraham Maslow's 1943 hierarchy of human needs, a five-level pyramid including, in order of pure necessity: physiological requirements, safety, love/belonging, esteem and self-actualization. This type of advisor focuses on portfolio sustainability.

The Rectangle. Advisors who are rectangles create plans that consider all of the assets and liabilities of the client's household. The rectangle refers to the Household Balance Sheet (HHBS), use of which is a central to the RMA training. The HHBS includes a family's real property, social wealth (e.g., the present value of Social Security benefits), human capital (earning power), debts and future liabilities—such as retirement expenses. This type of advisor focuses on portfolio feasibility.

The Circle. The circle signifies a holistic, comprehensive retirement advisory model that encompasses the rectangle, the triangle and the curve. To put it another way, the advisor who uses this model operates not just in one dimension (asset allocation) or two dimensions (asset allocation plus goal-based planning) but all three dimensions (asset allocation, goal-based planning and the HHBS). The entire model is described in RIIA's aforementioned Procedural Prudence Map.

Advisors who follow the map can't help but serve the best interests of the client and thereby comply with the spirit and the letter of the DOL fiduciary rule, RIIA believes. The RIIA process is fundamentally client-centric.

"Procedural Prudence starts with the client and circles back to the client," write Collins and Gadenne in their paper. "The advisor helps the client organize facts and priorities in order to translate them into actions and outcomes. The fact-patterns originate with client-specific data.

"The decisions are the client's to make, not the quant's or the psychologist's. Who makes the decision (governance) is as important as what is decided (policy) because a decision becomes successful, in large measure, only when it is willed into existence on a daily basis, by the client."

Gadenne's perspective

Will this model help advisors and broker-dealers survive the current crisis and make more money? Presumably yes, because multi-dimensional advisors are less likely to be replaceable with robots and more likely to capture a bigger share of the client's so-called wallet. But RIIA and Gadenne—the two are nearly synonymous—are at heart more concerned with the client's well-being than with the advice industry's.

That's because Gadenne had first encountered the retail financial services industry from the outside, as a client. After co-creating and selling a kind of robo-advisor during the dot-com boom of the late 1990s, he became, by definition, a high net worth prospect for Boston-area advisors.

An intellectually rigorous, French-born MBA-holder from Northwestern's Kellogg School of Management, Gadenne was surprised by the conflicting messages he received from advice providers. "Becoming a client myself, with agents and advisors coming at me, I realized that I was getting contradictory prescriptions, sometimes even in the same meetings," he said in Salem.

On the one hand, he heard that stocks were safe if your time-horizon was long enough. On the other hand, he heard from Zvi Bodie that stocks were not safe in the long run. He was told to trust in bell curves and Monte Carlo simulations, but he knew that averages and normal distributions have little value for individuals. He heard that investors are rational and that they are irrational.

Gadenne decided to start RIIA to make sense out of what he was hearing. The messages were contradictory, he found, because they came from different parts of a fragmented financial services industry, and because they were often merely ad hoc formulations designed for marketing purposes. Many of these contradictions vanished, in fact, when the financial plans began with the needs of the client rather than the needs of the sellers of investments or insurance products.

As evidenced at the conference, RIIA now believes that what's good for clients will be good for advisors, at least in the long run. It's trying to take advantage of the current disruption by positioning its educational materials and its RMA designation as a solution for advisors and broker dealers who are trying to stay compliant in a post-fiduciary rule world, trying to make themselves automation-proof in a world of increasingly sophisticated artificial intelligence tools, and how to differentiate themselves and justify their profit margins in a world where financial advice and products have become commodities.