Financial Planning
INVESTED IN ADVISORS
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The Boom for Alts Training is Here

Advisor interest in alternative investment training is booming.

Case in point: During the past year, the nonprofit Chartered Alternative Investment Analyst Association, founded 13 years ago to help train advisors in alternative investing, began offering an online fundamentals program that requires only 20 hours of class time — a much shorter time commitment than CAIA's full-scale 400-hour program.

To date, more than 2,000 advisors have completed the program. The response to the alternatives training has surpassed all previous CAIA course registrations.

The sample quiz questions that CAIA offers on its website provide a glimpse into the course's sophistication. Concepts covered include internally advised REITs versus externally advised REITs, stock hedges with mandatory issues, basket hedges, synthetic worksheet hedges, dividend reduction convertible hedges and the consequences of asymmetry of information. "It never hurts, just knowing all the jargon they use," laughs advisor Charles Flowers about the training.

A LONGER DECISION TREE

Alternative investments require a "longer pro and con decision tree," than your typical stakes in stocks and bonds, says Flowers, a 14-year veteran analyst who heads the investment team at the Abacus Planning Group, an $836 million AUM wealth management firm in Columbia, S.C. Most of Flowers' clients are seeking assets that aren't correlated to stocks and bonds, so he plans to send some of his staff for alternatives training beyond the due diligence study groups they already participate in.

Interest in alternatives training is widespread among advisors. "The proliferation of more complex investment product strategies is challenging managers to efficiently educate clients and prospects as well as their own sales professionals and supporting cast," reports asset management researcher Cerulli Associates.

Cerulli is not alone in forecasting a surge of interest in alt investing and training. According to numerous studies, alternative mutual funds experienced the biggest growth of any fund group during the past two years.

This is reflected at San Diego–based Creative Capital Management, which has been adding alternatives to clients' portfolios since 2010. "Because these are not investments that most laypeople understand," says Margaret Eddy, president of the $260 million-plus AUM advisory, "it's important to explain to the client why we are using them."

Investment product wholesalers have also jumped on the alternatives-training bandwagon. Bob Kendall, head of retail distribution for the Americas at Deutsche Asset & Wealth Management in Kansas City, says his firm dispatched 150 of its advisors who sell to other advisors to get the 20 hours of CAIA training.

There is, however, the other side of the coin. Some advisors believe alts are too vaguely defined to constitute a true asset class and represent a potential risk to their clients. Instead of distracting themselves with alt-centric training, advisors need to recast their thinking and put the wide array of new products through basic due diligence, they say.

The definition of an alternative does have a fuzziness to it, says Ray Padrón, president of Brightworth, an Atlanta firm with more than $1 billion in AUM. He notes that different rating agencies and wholesalers have different definitions.

"We share the skepticism" about alternative investment products, says David Yeske of Yeske Buie, an advisory firm in San Francisco with about $600 million in AUM.

LITTLE IN COMMON

Among some of the so-called liquid alternatives, product wholesalers have lumped together assets that have little in common and don't make much sense as a category, Yeske says. The only trait they share is a common sensitivity to inflation, he says.

Yeske believes investments should be assembled in a fund or packaged as a strategy only if they share “a common economic driver at their core.” Too many fund options offered as alternatives include real estate or oil and other commodities. “If you lump them together,” he argues, “you lose the opportunity to ride the commodities’ cycle in a more nuanced manner.”

Advisors who are tempted to spend time on alternatives-training programs, should instead “take a graduate course in economics or finance theory,” recommends Yeske, who earned his doctoral degree from Golden Gate University’s Ageno School of Business.

With that kind of education, he says, advisors will grasp the basics that should underpin any evaluation of prospective investments, whether they are tagged as alternatives or not.

Advisor Dryden Pence believes in training to evaluate alternatives, but he conducts that training internally and rejects products that are overly complicated. “We stay away from anything that looks like a black box,” says Pence, who is chief investment officer at $1.3 billion Pence Wealth Management in Newport Beach, Calif.

Pence leads monthly training sessions for his advisors, during which his investment team engages in role playing based on actual case studies and develops scripts for working with clients. “We think it’s best to be able to articulate products in terms that clients understand,” Pence says. Typically, he adds, the firm uses alternatives as a way of generating income for clients in low-interest environments.

Brent Everett takes the middle ground on alternatives training. His firm uses alternatives for some of its clients’ portfolios but has strict rules for studying and evaluating the investments.

“We don’t talk to wholesalers; we do our own research,” says Everett, who is chief investment officer for $200 million Talis Advisors of Plano, Texas.

The products may sound complex at first, but “if you are willing to spend the time understanding them, it’s not that difficult,” he says. If, however, “you typically rely on wholesalers for training, you’re going to be in trouble.”

WHEN ALTS ARE USEFUL

Everett believes alts are a useful tool for controlling clients’ more impulsive behaviors. “They keep the clients in their seats,” he explains, since they are structured to have lower volatility at times when more traditional investments are heading south.

To choose the best alternatives for that purpose, Everett’s investment team puts a lot of time into reading the academic literature and cultivating a basic understanding of how markets work. This has implications above and beyond investing in alts.

To be able to devote the kinds of resources that this sort of advisor training demands, a firm’s management needs to relieve some staff members from client prospecting duties. “You have to assign different responsibilities,” Everett allows. “Someone has business development; someone has investment research.” The sales guy “is probably not the guy who should be picking liquid alternatives.” FP

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