ARK ROYAL
WEALTH MANAGEMENT

Helping Successful People Make Smart Decisions About Money

SPRING 2017

BUYING MUNI BONDS? CAVEAT EMPTOR!

Prospective clients sometimes come to us with municipal bonds in their portfolio. These bonds can vary dramatically in terms of size, maturity and credit quality. In contrast to the equity markets, the bond market largely remains quote driven. It relies on dealers or principals to make the market, and most trades still require considerable human contact, judgment, and a degree of old-school negotiation.

In a typical trade, a seller of a bond requests a bid from a group of dealers and stipulates a time limit—for example, 20 minutes. This "request for quote" (RFQ) identifies the bond, the quantity offered for sale, and the time allowed for dealers to provide a quote. There is no obligation for dealers to respond, and when the time frame has elapsed, the seller decides which, if any, quote to accept.

If the dealer cannot generate buyer interest in this short period of time, the dealer may choose to bid on the bond at a price that would justify holding it in inventory while taking more time to find a buyer. This is one role of the market maker: to provide liquidity by assuming the risk of carrying securities in inventory.

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Individual investors own about 42% of municipal bonds (more than 6 times the level of ownership of Treasury bonds), making it an area of the market where more sophisticated traders can take advantage of mom and pop investors. A study last year by S&P found that investors in muni bonds in lots of $100,000 paid 1.73% in mark ups on average. Mark ups are fees, but are embedded in the price of the bond. The S&P study found mark ups were most significant in "odd lot" denominations, i.e. bonds less than $100,000. For example, customer Joe Smith buys a $30,000 NC muni for 106, but 10 minutes earlier the bond dealer bought the same bond for 101. In this example, the bond dealer made $1,500 profit or about 5% in mark up!

Most individual investors would do well to tread cautiously in trading individual muni bonds, and endeavor to make their minimum lot size $100,000.

OVER THE MOON

My hope is that as a financial advisor, I am able to translate somewhat complicated concepts into easy to follow terms. One of the best story telling techniques I know is to use parallels from other disciplines.

For over two decades I've favored an investment philosophy that abstains from try to identify only the "best" stocks for one that embraces asset class returns. Only in the last few years has that message gained more widespread acceptance. Even today, a majority of investor dollars are directed towards investment strategies that attempt to pick only winning stocks, an approach that scores of academic research suggests reduces the odds of a successful investment experience. Alas, perhaps Samuel Johnson was unknowingly describing the average investor with his famous quote about the triumph of hope over experience.

To understand how a misguided belief can become so widely accepted let us turn to the heavens. Throughout myriad cultures dating back over 20,000 years, man believed Earth to be the center of the universe. Roman scholar Claudius Ptolemy (100 AD) refined early Greek astronomy findings to produce the Ptolemaic model, which put the Earth at the center of the solar system. The Ptolemaic model was readily accepted because it fairly accurately predicted the movement of planets and the moon.

It took nearly 1,400 years before Nicolaus Copernicus put forth the heliocentric model, which placed the sun at the center of the solar system. The heliocentric model wasn't embraced with open arms by leading scholars of the day or even other astronomers. In this regard, it shares much with index investing. When John Bogle started the first index mutual fund in 1976 he raised a mere $11 million, so far short of the $150 million target that investment bankers underwriting the capital raise wanted to cancel it.

It took nearly 250 years (and the inquisition of Galileo) before heliocentrism gained official acceptance.

Today, it's hard to believe any educated person would argue the Earth is the center of the solar system. It hasn't taken two centuries, but the acceptance of an evidence based investment strategy has been slow to take hold. In fact, one might contend the difference between a stock picking investment strategy and an evidence based investment strategy is like the difference between astrology and astronomy—which would you rather bet your financial journey on?

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IN THE NEWS

Look for Mike Palmer's three-part series on behavioral finance in upcoming issues of *Medical Economics* magazine.

MARK YOUR CALENDARS

Ark Royal is offering our 2-hour retirement planning workshop "Ready, Set, Retire!" on Saturday, May 6 from 9:15–11:15 am.

Seating is limited, call Lisa Shirley at 919-710-8665 for more information.

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ROLE REVERSAL

I had the opportunity to speak to two different groups last month, and as is often the case, I came away from the sessions feeling like they taught me more than I taught them.

The first group was a class of UNC undergraduates taking a personal finance course. Ironically, I'd had a class in the very same Carroll Hall classroom some thirty years ago, so it was an odd feeling being the one at the front of the room.

MY FIRST TAKEAWAY was how pervasive technology is in the educational environment. As a student at UNC in the mid-80s, computer access was scarce and required signing up (limited to an hour at a time) in the computer lab on a Compaq 386 (complete with amber screen). Every student attending my recent lecture had a laptop, and one student videoed my presentation on her cell phone.

MY SECOND TAKEAWAY from the UNC class was how thirsty the students seemed to be for personal finance insight. I fielded a wide-range of questions after my talk, topics from college funding to how to find a fee-only financial planner. Professor Carol Wolf shared that her class has skyrocketed to over 50 students in just the second semester it has been offered.

My second speaking engagement was to a group at the opposite end of the age spectrum at the *Wake Tech Plus 50 Expo*. This presentation focused on evidence-based investment strategies and the importance of working with a fiduciary financial advisor. There was no less thirst for financial education from this group. However, from talking with attendees this demographic is far more focused on the personal nature of an advisory relationship. They place greater importance on working with an advisor who is held to a fiduciary standard that puts the interest of the client first.

I suspect these two dynamics—how technology impacts personal commercial interaction and the fiduciary standard—will have major implications for how the financial advisory business evolves going forward.

WHY A "HOME DEPOT" APPROACH TO YOUR WEALTH MAY FALL SHORT

As March gives way to April, we come out of hibernation, get outdoors and start home improvement projects. The advertisements from Home Depot and Lowe's promote the do-it-yourself ethos, after all they exist to help the DIYer make his home his castle.

That same DIY mentality is a staple of advertising from Charles Schwab and Fidelity, brokerage firms that cater to do-it-yourself investors. However, far too many people mistakenly associate managing investments with managing wealth. Over the course of two decades in the financial advisory profession, I've come to appreciate the distinction.

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As my wife will attest, my home improvement talents are limited. Installing deck lights may take me an afternoon (and a dose of frustration), but it is something I can do. And, the downside to any shortcomings I may have in doing so doesn't impact the structural integrity of my home. However, repairing the roof or replacing bath fixtures, those are jobs beyond my pay grade.

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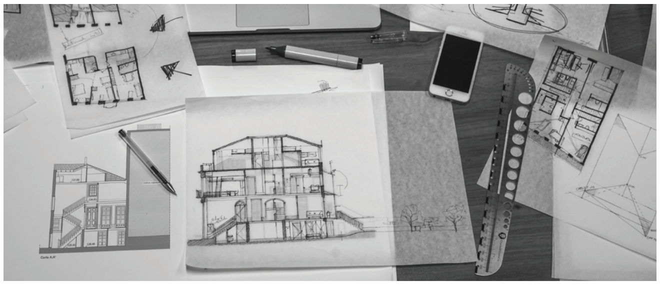
Managing one's investment portfolio is a little like installing deck lighting; someone with the time, discipline and discernment may be able to do-it-themselves at a reasonably competent level. But managing one's wealth is another matter altogether. Few, if any, DIYers have the expertise, experience and knowledge of all the various components of wealth management (insurance, estate planning, retirement planning, etc.). It's not something that one can learn by watching a YouTube video or Googling "wealth management." Comprehensive financial planning is far beyond most people's ability. It's like building a house, not something one can do with the help of Home Depot.

Our clients share that what gives them the most comfort and reassurance in working with us is that we bring coordination to all the aspects of their wealth. We monitor their progress, anticipate issues and recommend solutions. **We provide a blueprint for a secure and independent financial future that insures an enduring legacy.** Or as the Home Depot advertisement might say, we keep their financial house in tiptop shape.



"The inherent vice of capitalism is the unequal sharing of blessings; the inherent virtue of socialism is the equal sharing of miseries."

WINSTON CHURCHILL

The CORNERSTONES *of* ARK ROYAL WEALTH MANAGEMENT

To nurture a culture that puts our client's interest first—always

To be truthful at all times, to be intellectually honest with ourselves and with our clients, even if it isn't what they want to hear

A commitment to lifelong learning, and a passion for applying our wisdom efficiently and effectively every single day

Align what you say, what you do and what you think to honor yourself, your family and our firm