PRACTICE MANAGEMENT INSIGHTS

A Primer for Financial Advisors Seeking to Differentiate Their Practice

Adding Value to Black Parents

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Two important aspects of successful financial management: a working knowledge of managing and multiplying assets, and the ability to pass those assets and that knowledge down to future generations.

What comes to mind when you hear the word marathon? Some of us feel the excitement and rush of the potential to conquer a grueling, challenging activity. Others of us simply respond with the word "no." Well imagine it's a beautiful day for a spring marathon and you've mustered up the courage to participate. While others don light tank tops, runner's shorts and specially crafted sneakers, you arrive in a light winter jacket, bulky sweat pants, and basketball shoes — after all 45 degrees is cold. Furthermore, you learn the other runners have been training exclusively for this race for the past four months. Your "training" consisted of running a few miles here and there on the treadmill over the last month or so — and a pick-up basketball game last week.

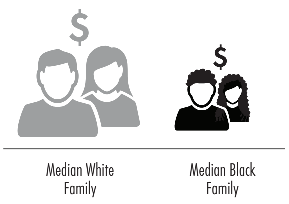
The probability of dramatically different marathon outcomes is very high.

The concept of wealth creation is a lot like hearing the word marathon for most people. It can be especially daunting for many black families across a broad spectrum of income earning levels. A typical response to such a claim is to say train properly or harder and wear the right clothes. But what if you did not have access to a proper training schedule? What if you could not procure an appropriate running outfit? To add value to these runners, as it were, one would do well to acknowledge the access aspect of the dilemma before moving on to prescriptive solutions.

We believe that Black Americans have a great deal of desire for growth when it comes to financial management and investing, especially conveying key financial lessons to their children. Collectively, this segment represents over $1 trillion in buying power[1]. The opportunity for advisors to help translate those resources into unprecedented wealth creation while also providing opportunities to be supportive partners in this process, may provide advisors with an opportunity to differentiate their practice.

[1] Boschma, Janie. The Atlantic. "Black Consumers Have 'Unprecedented Impact' in 2015." 2Feb2016. https://www.theatlantic.com/politics/archive/2016/02/black-consumers-have-unprecedented-impact-in-2015/433725/

The cumulative, generational effect of these practices has helped lead to the median white family having 12 times the wealth of the median Black family.



AMERICA'S WEALTH GAP PRIMER

Before advisors can credibly and effectively add value to this underserviced segment they must understand some factual impediments to Black family wealth accumulation, forces that prevent the willing marathon runner from being fully prepared. Much of the challenge for Black communities stems from discriminatory practices — both historic and contemporary — such as redlining,[2] general housing discrimination,[3] and inflated interest rates.[4] The cumulative, generational effect of these practices has helped lead to the median white family having 12 times the wealth of the median Black family.[5] In fact, one in four Black households have *zero or negative* net worth.[6] Even in families where one or more members has a professional degree, Black families have, on average, $200,000 less in wealth than their white counterparts.[7]

With dramatically lower generational assets, two important aspects of successful financial management have historically been unavailable to generations of Black Americans: (1) a working knowledge of managing and multiplying assets, and (2) the ability to pass those assets and that knowledge down to future generations.

Even today, Black Americans who report being well-educated in finances, tend to emphasize saving over investing. Consequently, Black Americans tend to participate in "safe" low-return investments[8] while black youth tend to score lower on financial literacy assessments.[9]

America's wealth gap is largely structural in nature and, while that gap may ebb and flow, astute advisors can help Black families translate their income earnings into wealth accumulation. It is important, however, for advisors to embrace a paradigm shift in thinking, which is that while poor financial choices contribute to the aforementioned gap, it is not a leading factor. When working with Black clients, financial advisors should consider acknowledging this reality and also championing the idea that personal efforts, such as promoting financial literacy within one's family, may help to improve wealth acquisition outcomes.

Here are some actionable strategies you can use in partnership with your clients for teaching key financial management lessons to their children.

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[2] Gross, Terry. National Public Radio. "A Forgotten History of How the U.S. Government Segregated America."- 3May2017. http://www.npr.org/2017/05/03/526655831/a-forgotten-history-of-how-the-u-s-government-segregated-america.

[3] National Association for the Advancement of Colored People (NAACP). "History of Housing Discrimination Against African Americans in Detroit." January 2017. http://www.naacpldf.org/files/our-work/Detroit%20Housing%20Discrimination.pdf.

[4] Desilver, Drew & Kristen Bialik. Pew Research Center. "Blacks and Hispanics Face Extra Challenges in Getting Home Loans." 10January2017. http://www.pewresearch.org/fact-tank/2017/01/10/blacks-and-hispanics-face-extra-challenges-in-getting-home-loans/.

[5] Jones, Janelle. Economic Policy Institute. "The Racial Wealth Gap: How African-Americans Have Been Shortchanged Out of the Materials to Build Wealth." 13February2017. http://www.epi.org/blog/the-racial-wealth-gap-how-african-americans-have-been-shortchanged-out-of-the-materials-to-build-wealth/.

[6] Ibid.

[7] Ibid.

[8] Natella, Stefano, Tatjana Meschede & Laura Sullivan. Institute on Assets and Social Policy. "Wealth Patterns Among the Top 5% of African-Americans." November 2014. http://iasp.brandeis.edu/pdfs/2014/Top5.pdf.

[9] Mottola, Gary. FINRA Investor Education Foundation. "The Financial Capability of Young Adults – A Generational View." March 2014. http://www.finrafoundation.org/web/groups/sai/@sai/documents/sai_original_content/p457507.pdf.

Teach saving at an early age

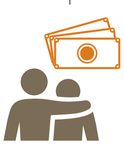
Physically walk them into a bank

CHILDHOOD PHASE: **Teach the importance of saving**

It's never too early to teach the value of saving. Your clients may want to consider purchasing a piggy bank or a clear mason jar when their child is around five or six years old, so that the child can watch actual savings in action. This allows them to become familiar with watching their funds "grow in reserve." Once they have accumulated a reasonable amount in their personal piggy bank, parents can take their child to open a savings account. By physically taking them into a bank, parents provide children with a tangible learning experience regarding financial institutions.

All parents should encourage a consistent savings habit while teaching the differences between needs and wants. As children age, they will continue to learn the value of saving by adding money to their account that is either earned from chores or received as holiday gifts. As they enter the pre-teen and adolescent years, parents should begin talking with their child about savings goals: "How much do you want to save and for what purpose? What will it take to achieve your goals?"

The elementary years are also a great time for lemonade stands or other child-generated ideas for raising money. Whether it's making and selling ice cream sandwiches or homemade crafts, children can earn additional money to add to their savings accounts by appealing to adults who appreciate their entrepreneurial spirit.



Continue talking about financial "next steps"

Teach them how to make small investments

TWEENS AND TEENS PHASE: **Educate about investing**

Parents with teens have a lot on their plate — myriad activities, biological and cognitive changes with their children, and navigating increasing peer pressure. Consequently, the immediate challenges of the adolescent years may result in financial education taking a back seat. During this period, however, financial advisors can be a particularly important support, further encouraging parents to maintain and build upon the foundation they laid earlier while offering specific tips and strategies.

In fact, suggesting to your clients that continuing to talk to their children about "next steps" when it comes to financial matters might actually help bridge the potential growing relational gulf that may have opened up between teens and their parents during adolescence. While it may sometimes seem they're not the most rational human beings, it is important to continue to hone those critical thinking skills and may be the perfect time to introduce basic concepts of investing.

Teens love hands-on experiences that don't feel like learning, and, of course, many of them love money, too. Explain to parents this creates an opportunity to provide children with direct exposure to investing. They can set aside time each month to discuss current investing trends, encouraging their child to do research and select a few companies they believe will increase in value over the next quarter. Next, they can have their child "put their money where their mouth is," by even making small investments. Having the child pick companies they care about and which reflect their values can make investing fun while providing practical grounding for the future. At the same time, the opportunity to gain and lose money will provide a realistic idea of the risks associated with investing.

Once parents are confident in their teen's knowledge, they may want to introduce them to mutual funds and exchange-traded funds (ETFs) as a way of investing in a professionally managed basket of securities. Additionally, this is the age when parents might want to introduce children to their own process for preparing for long-term financial commitments, such as saving for college, and to key members of their financial planning team, such as a banker or to you, their advisor.

Work with them concerning budgeting and navigating the credit card landscape

Teach how to minimize student loan debt

YOUNG ADULT PHASE: **Handle the present, keep building for the future**

By emerging adulthood, this type of consistent investment training may provide a child with both a foundation for how to save and invest, and if done correctly, potentially have at least a little money set aside from their previous years of research and practice. The lemonade stands of their formative years may have morphed into budding entrepreneurship and the beginnings of wealth creation. Now, as young adults they may be learning about financial topics like working with a limited budget, navigating the credit card landscape, and minimizing student loan commitments. This is also an important time to drive home the concept of the time value of money.

The fact that a child may be about to move away from home for college, work, or a gap year doesn't mean your role as the advisor is complete with respect to providing support to your clients who are parents. In fact, your advice can be more important than ever, as you outline for parents the key lessons they need to convey to their young adult children.

Talk with parents about student loans and how to involve their young adults in responsible planning and management so their debt burden is minimized over time. If the family is fortunate enough to not need student loans for college, invite parents to consider encouraging their child to seek a part-time job so they can develop a steady work history. The moment when the child begins generating consistent income, however modest it might be, may provide a parent with the opportunity to discuss opening a Roth IRA with a discussion around retirement.[10] And reinforce the message that retirement may seem ages away, but early contributions make big differences in the future.

Remind parents, this is also a great time for their children to develop connections with individuals who have business ventures. Many billion-dollar companies today started as concepts during college. Emerging adulthood provides diversity and experiences that can lead to either potential career opportunities or building relationships that can prove to be profitable business ventures later in life. Internships, apprenticeships, and other mentor-type relationships, whether formal or informal, can yield great fruit in the years ahead.

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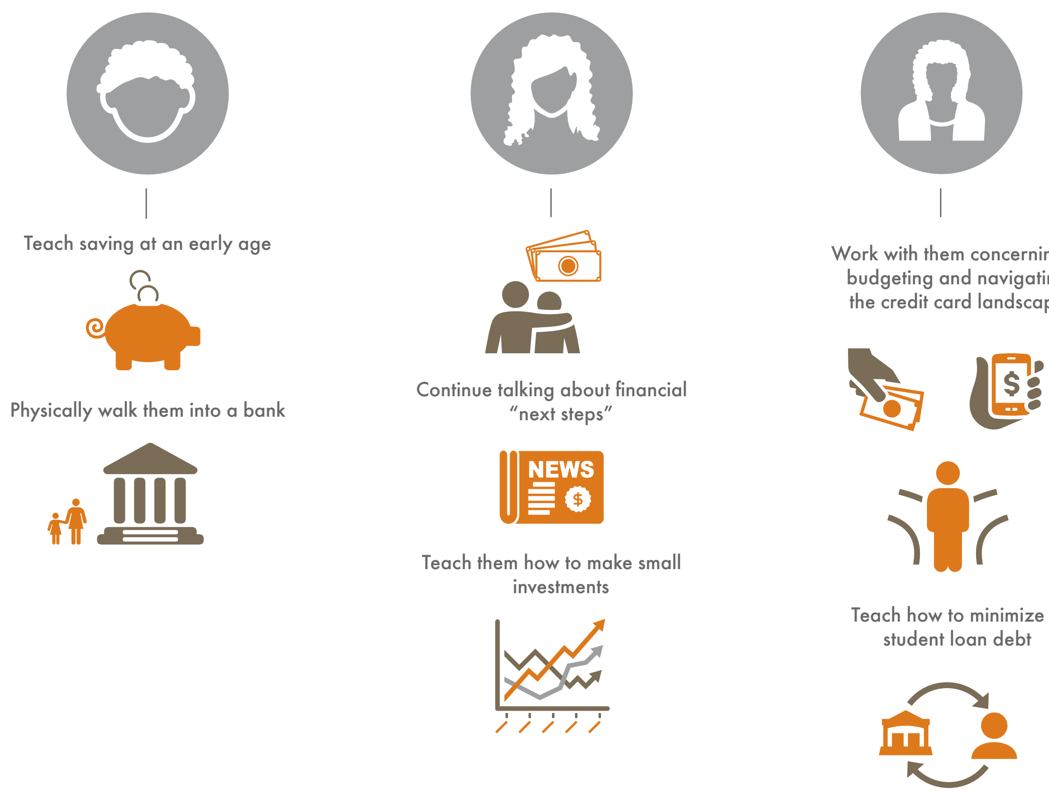
[10] Malone, Matthew. RothIRA.com. "What is a Roth IRA?" January 2017. http://www.rothira.com/what-is-a-roth-ira.

CONCLUSION

Financial growth requires planning and research indicates investing is a key area of opportunity in the Black community. According to Morningstar, the number of Black investors has increased from 57% to 67% over the last 17 years.[11] While that's certainly an improvement, this demographic has greater growth potential, and advisors can play a key role in helping close the significant investment rate gap.

Starting young is a primary key to begin to dismantle structural obstacles that have prevented past generations of Black Americans from accumulating and fostering wealth. Teaching children the importance of financial literacy, and emphasizing the importance of planning to achieve both short- and long-term goals, can make a significant difference in their lives. Advisors, who are well-positioned to add robust value to clients with children, can offer those who have historically been left out of wealth development with ideas and tools to help them create wealth.

THE MARATHON RUNNERS OF THE FUTURE ARE COUNTNG ON YOU



[11] Glaser, Jeremy. Morningstar Advisor. "Black Investor Making Gains; More Work to be Done." 6February2016. http://www.morningstar.com/advisor/v/113036249/hobson-black-investors-making-gains-more-work-to-be-done.htm.

ABOUT THE AUTHORS

Cliff Goins IV is a senior executive at FlexShares with prior work experience in asset management and private equity, and a passion for helping people improve personal finance outcomes. He's experienced firsthand the effects of structural obstacles, low investment rates, and conservative financial choices on Black families. He's presently doing his part to help close the wealth gap.

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