



# ASSETS

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› Unraveling the Recession:  
Regaining Trust

# FEATURE

The ongoing recession continues to take its toll on almost everyone, and working toward a recovery remains uppermost on the agenda of business and government. In this context, we examine a few different perspectives from UCLA Anderson alumni involved in some key areas related to the recession. Along with so many others, they are engaged in the wide-ranging effort to understand the underlying causes and determine how best to respond.

With the severity of the impact, there has been some loss of faith in our financial system, especially as contributing factors that are particularly troubling have been revealed. An honest assessment of the mistakes that were made and solutions aimed at preventing their repetition can go a long way toward reestablishing trust in our institutions. Learning the lessons is essential to having the confidence to determine the appropriate next steps for moving forward again and to identifying opportunities available in the current situation.

UCLA Anderson is also responding to the recession with events and expert speakers, addressing various aspects of the issues involved. Members of the school's faculty continue to contribute their expertise to media analysis of the details of the recession as well. In addition, the ramifications are considered in classrooms (including the new Master of Financial Engineering program), in fundraising efforts and in career support services at the school, among other areas.

# Unraveling the Recession: Regaining Trust

By Paul Feinberg

The current recession has lasted so long – 15 months and counting at press time – that it already has its own history. The recession hasn't run its course but there certainly are lessons to be learned from it already. The impacts of the recession are as numerous as its victims, and even if your name is Gates or Buffett, we've all been victimized to some extent by current economic conditions.

In the pages that follow, *Assets* looks at the recession through the eyes of a few of UCLA Anderson's alumni. We'll get the perspective of a pair of financial advisors and learn how they're helping their clients and what their advice is for the rest of us. We meet an award-winning public relations expert, who describes ways in which we can creatively and effectively use communications to our advantage in this environment. Finally, we'll hear from a marketing executive whose seat at the boardroom table at one of the nation's leading mortgage companies gave him an up close and personal view of the bursting of the housing bubble.

## Managing Money with Confidence in Any Environment

As partners, certified financial planners and principals at Quantum Wealth Management ([www.quantumwm.com](http://www.quantumwm.com)) David DeWolf (EMBA '05) and Darius Gagne (EMBA '05) are making it a point to study the aforementioned lessons.

"I think definitely the surprise is the magnitude of the recession," DeWolf said. "In past recessions, clearly some people lost a lot

of wealth, but there weren't so many people wondering 'Wow, do we have to cut back on our lifestyle?'"

"It seems to be everyone's recession this time," Gagne added. "You can probably say that in past recessions, post World War II, some areas of the economy were affected worse than others, whether geographically, industry-wise and so on. But this one is just hitting everyone."

The pair traversed divergent paths before coming to UCLA Anderson, ending up as partners sharing a common vision on how best to manage wealth. DeWolf received his undergraduate degree at UCLA, and then earned his C.P.A. while at Price Waterhouse. He then took a few different jobs in finance before deciding to enter Anderson's Executive MBA (EMBA) program. His goal was to improve his finance skills and parlay his MBA into a chief financial officer position.



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Gagne (who also holds a UCLA undergraduate degree) studied science, eventually receiving his doctorate in physics from UCLA. He then headed straight for Wall Street, joining a cadre of quantitative specialists with advanced degrees in subjects like math and engineering, to create models for products like interest rate options, mortgage-backed securities and collateralized debt obligations. After five years, he returned to California to work at PIMCO in Newport Beach. He entered the EMBA program, because he considered himself “a finance guy who knew very little about business.”

While still at Anderson, Gagne approached DeWolf with the idea of becoming partners – and the opportunity struck a chord. They spent their second year consulting with faculty and leveraging the experience and expertise of classmates while formulating their final business plan. They opened the doors of Quantum Wealth Management – the name derives from Gagne’s background as a physicist – immediately upon graduation without a single client. Within a few months, their client list had grown to more than a dozen.

The Quantum moniker connotes more than just Gagne’s physicist-turned-financier history. It is a firm whose management approach and philosophy is grounded and guided by research. For example, DeWolf noted that they have found that it is asset allocation – not stock selection – that accounts for the vast majority of returns. Therefore, the focus on research informs the company’s philosophy, which has been trademarked as Total Market Portfolio™.

“We believe that value migrates from business to business, industry to industry, nation to nation,” DeWolf said. “Predicting the flow is usually impossible, but fortunately, entirely unnecessary, because we also believe that the global productive capacity for creating value is immense. Although we do not know where the bubbles will be in a pot of boiling water – i.e., where value will migrate to – we know overall that the heat will rise. There is no shortage of objective research supporting these beliefs. Therefore, the most rational thing one can do from an investment perspective, in order to maximize returns while minimizing downside, is to own a share of each of the global capital markets. That is the Total Market Portfolio, which includes over 10,000 stocks, 10,000 bonds and hundreds of real estate investments around the globe.”

In today’s economic climate, Gagne thinks the first and foremost key is not to panic. The most common mistake a lot of investors make is panicking, he said. DeWolf added that their clients have an investment strategy, which is developed at the beginning of the relationship. It serves as an anchor to ground them if they start getting anxious. The plan is actually built on the possibility of a bear market, so clients can be reminded that their portfolio still has a lot of safety built into it. Then they leave with “a weight off their shoulders,” feeling a lot better, DeWolf said.

One way not to panic is to understand one’s risk. Gagne believes that another of the big lessons being taught by the current recession is a heightened awareness of what is meant by risk. “This crisis has reminded us of how important it is to have the right risk exposure at any time, especially heading into a crisis,” said Gagne. “The common strategy out there is to say, ‘Hey, things look great; let’s be close to 100 percent in stocks’ or ‘Hey, things look bad; we should be 100 percent out of stocks.’”



“We don’t buy that, because the market timing thing never seems to work,” added DeWolf. “What we say is, ‘You should have the right amount of risk at any time.’ Safe doesn’t mean cash either. There are a lot of good opportunities in the bond market right now, which we’ve seen develop in the last six months.”

It’s tempting to try and pin down exactly what the ideal portfolio should look like. But the truth is, every situation is unique, and there is no ideal portfolio that covers everyone. But, there are some general principles that DeWolf and Gagne adhere to. For example, they believe

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that a portfolio should have seven to 10 years of fixed income cash flow. That way, when there are massive losses on the equity side, investors have time to let them come back. During this recession, what then should investors who’ve suffered large losses do? Is it possible to convert a “damaged” portfolio into one with more acceptable fixed-equity ratios?

“Unfortunately, no,” DeWolf said. “If somebody had \$2 million – and we’ve run into these people – then suddenly they have \$1.2 million, they might not have the bandwidth to have 10 years of protection at this point, because they’ve lost so much. Markets are going to go up and down, and it is the disciplined investor who prospers at the end of the day. However, it’s very challenging to maintain that discipline.”

“The category of folks that we’re talking about suffer from a behavior bias called ‘recency effect,’” said Gagne. “What they should be doing is looking at this \$1.2 million as if they just got it, as if they just inherited it. And then they should ask, ‘What’s the most rational thing I can do with it?’ Instead, they look at it as ‘Darn, it was \$2 million,’ and that obscures smart decision-making regarding what they have left.”

Helping their clients make smart decisions is what DeWolf (who specializes in serving executives in transition) and Gagne (who specializes in serving entertainment industry professionals) do. DeWolf has recently authored a white paper offering five key concepts for financial success. They include: (1) leverage diversification to reduce risk, (2) seek lower volatility to enhance returns, (3) use global diversification to enhance returns and reduce risk, (4) employ asset class investing and (5) design efficient portfolios.

When talking with the Quantum pair, it’s the globally-related third item that is emphasized. It’s a complex issue, but ultimately, DeWolf and Gagne make the case for a global stock portfolio. They explain that there is so much that gets ignored through a home-country bias, because U.S. market capitalization only represents about 40 percent of the total in the world.

## Communicating Effectively Even in an Economic Downturn

Peter Marino (FTMBA '02) founded Chicago-based Dig Communications ([www.digcommunications.com](http://www.digcommunications.com)) five years ago with just one client. Recently named PR Week's Small Agency of the Year, the full-service public relations agency now represents high-profile clients such as MillerCoors, The Wm. Wrigley Jr. Company and Solo. Marino has more than 14 years experience in public relations and strategic consulting, beginning his career at Cramer-Krasselt working on Master Lock's famous "shot lock" Super Bowl ad campaign, among others. He was also at Ketchum Communications, working with the Miller Brewing Company (now MillerCoors) and with then travel startup Orbitz. After UCLA Anderson, Marino joined the Los Angeles office of the Boston Consulting Group, before moving to Chicago to become chief executive officer of Dig Communications.

Like many others, Marino and his clients are feeling the effects of the recession. He said that his company has been perfectly fine when you consider that "flat is the new up." However, he acknowledged that Dig has felt the impact of the down economy, as clients cut back on spending and funding decisions take longer to make. He said a lot of his clients are delaying these decisions as long as possible, trying to see what the potential pitfalls may be before committing.

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— Peter Marino (FTMBA '02)

Of course, it helps when your two biggest clients are MillerCoors and Wrigley. With just a touch of humor, Marino explained that beer is fairly recession resistant and chewing gum is an affordable luxury. However, not every industry is recession proof or easily affordable. For the rest, Marino believes public relations can be both an effective tool and an efficient use of marketing funds, particularly in a rough economy.

Public relations campaigns are an excellent way to set one's company apart from the competition. As an example, Marino describes Miller High Life's recent Super Bowl campaign. Miller, it seems, can't actually buy a commercial during the game, as a rival brewery holds an exclusive. So, this year, the company launched a guerrilla campaign to get attention by taking a swipe at everyone who paid \$3 million for a minute of commercial time by creating a "one-second commercial." Along with the commercial, a website was created, and Miller High Life's "delivery man" spokesperson ended up on the late night talk show circuit. The public relations campaign netted coverage in USA Today, Advertising Age, countless column inches and blog activity. The result: Miller High Life sales were up 8.6 percent, and the entire campaign created buzz proclaiming the beverage as the right brand for the economic times. As Marino pointed out, all marketing ultimately needs to deliver sales.

Social media – blogs, Facebook, Twitter and the like – is a growing area of opportunity where Marino sees great potential. He said that there is a gray area surrounding such new media, with advertising agencies, public relations companies and marketers all playing in the space. His company is using a lot of social media these days, he said, since it is relatively affordable and easy to track.

“I think you need to be diligent about differentiation,” Marino said. “Consumers are looking for unique products that offer enjoyment and functionality, and providing such things is one way to survive the recession. Companies also need to be topical and find ways to get into news stories, particularly in ways that show your products and services can be a benefit.”

What about companies in more dire circumstances? How up front does a company need to be with its customers? Here, Marino also emphasizes honesty, believing that consumers and clients can sense when a company is being disingenuous.

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## Bearing Witness to the Collapse in Housing

“The Foreclosure of America” is the first book written by Adam Michaelson (EMBA ’04). It is in one sense an autobiography – an insider’s look at the mortgage crisis that fanned the original flames of the recession – but it is also a meditation on the marriage of marketing and finance in the economy.

Michaelson spent a decade and a half working at ad agencies, such as Ogilvy & Mather and Grey Worldwide, before joining Countrywide Financial as senior vice president. In the book’s opening chapter, he describes a meeting in the mortgage giant’s semi-legendary “vault,” a conference room that was specifically designed to be part bomb shelter, part panic room. (The vault was left over from when it was used for top secret meetings when the building was the Cold War headquarters of Lockheed Corporation.) The meeting was to discuss the introduction of pay option loans, mortgages where buyers had the option to pay less than a standard mortgage payment every month. (Michaelson noted that Countrywide did not invent the pay option concept; other financial institutions, like Wachovia, had similar products.)

Michaelson explained that the products were predicated on the notion that real estate



prices would rise for the foreseeable future or “in perpetuity.” While everyone at the meeting alternated between gloating about the new product and discussing how to market them, Michaelson raised questions, wondering what would happen if real estate prices did not continue to rise. Five years later, Michaelson runs his own company, Michaelson Marketing Group ([www.MichaelsonMarketing.com](http://www.MichaelsonMarketing.com)), and it is almost difficult to believe that these were once the thoughts of very smart, very successful people. They had crunched all the right numbers and created all the right spreadsheets, coming to the conclusion that loan products built on the notion of always rising real estate prices were well worth the risk.

Michaelson reflected not only on these past events but also on his emotions at the time. “At that moment, I had actually spent an entire career selling things to people that they maybe didn’t necessarily need,” he recalled. “But making them feel like they needed it, which is fine when it comes to toys or technology or things that are sort on a lesser scale. However, when you’re selling home ownership – the American dream – I took that responsibility very seriously. At that time, I became concerned over whether what we were doing was responsible.”

Michaelson’s concern, other than the projections regarding future real estate prices, was that under pay option plans, home owners could actually end up owing more on their house each month than they did the month before. A drop in home prices could leave homeowners upside down, and the rest, as they say, has been history. He makes it clear that he was not the only person who was worried about the negative

potential of pay option mortgages, though he said he may be the first to write about it. So, it is legitimate to ask why banks and mortgage lenders created and sold the products.

“I liken it to a space launch, where they run the numbers, they do risk assessment and they freely admit that it’s possible that ‘this thing could explode,’ but we believe it’s worth the risk,” Michaelson said. “That’s the nature of any business decision. The first thing they teach you at Anderson is that you’ll never have all the information you need, and you need to make an educated best guess, based on all available data, intuition, history and what’s best for your shareholders. And at the time, what was best for our shareholders was to increase value by increasing loan volumes and by getting more people into homes.”

The collapse of the real estate economy is well documented (see the summer 2008 edition of *Assets*). Michaelson, like the rest of us, is left to consider the lessons learned. From his perspective, there are several. First, he believes that not everyone in America was ready for home ownership. Home ownership, he suggested, used to be a privilege that was earned by saving for a 20 percent down payment, creating good credit and establishing character in one’s community. That’s how you got a loan.

“Somehow, it morphed into ‘everyone has the right of home ownership.’ Clearly, not everyone was ready for the responsibility,” Michaelson said. “The saddest truth of this crisis is that, in this nation, subprime used to mean ‘second chance,’ and everybody deserved a second chance. Now, subprime has become a dirty word, and because of this crisis, it’s going to be even harder for someone with a minor credit ding to get a loan.”



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