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ABAdvisorInstitute®

EXECUTION GUIDE

How to Present Your Capital Markets Perspective



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Any program that sets out to answer the question “How do I present my point of view on the capital markets?” must start with a more fundamental idea: “Why bother? The markets are far too complex to thoroughly understand, let alone explain to others.”

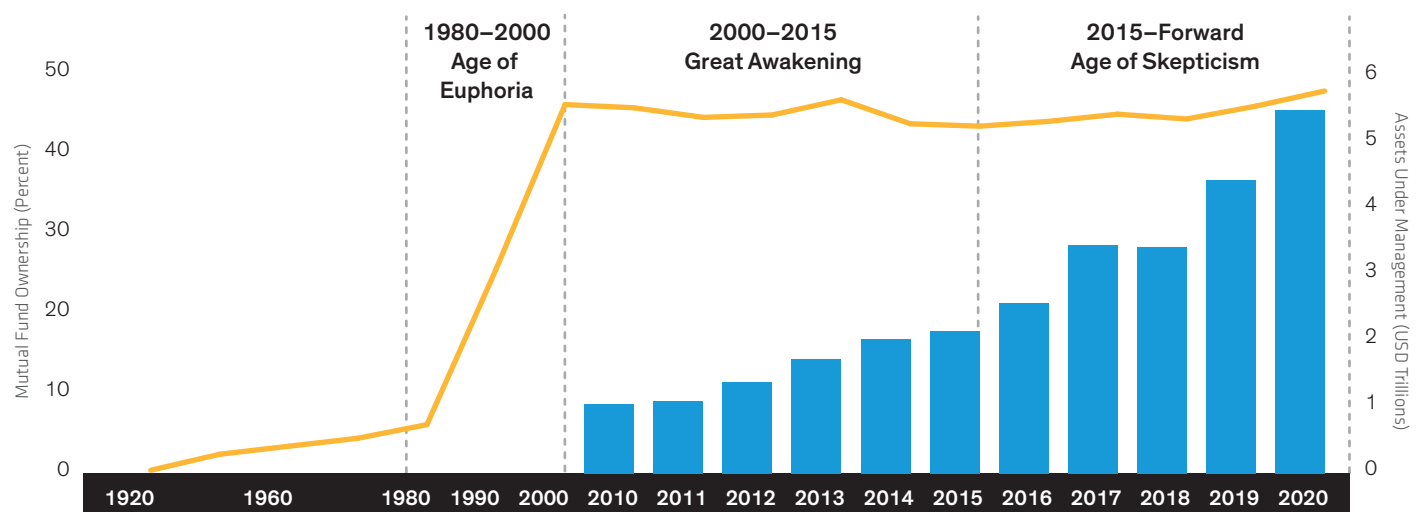
It's true that the dynamics within even a small slice of the markets are constantly changing and that predicting market behavior is impossible. A well-crafted point of view needs to be updated frequently to stay relevant. The task is large and onerous. However, a prudent Financial Advisor (FA) recognizes the importance of developing and maintaining a current point of view about the markets and being able to present it effectively to clients and prospects. This is partly because the financial-services industry is going through a profound transformation regarding what clients expect from their advisors.

The powerful forces that set client expectations over four decades ago have evolved significantly and are now redefining clients' emotions regarding their advisors. This program will help you understand these forces and will explain why an effective presentation of your Capital Markets Perspective is more important than ever before.

The Financial-Services Industry Is Going Through a Period of Disruption

The euphoria investors felt in the early 2000s has been replaced by skepticism about the value that professional advisors provide to their clients.

INVESTORS' EXPECTATIONS OF THEIR ADVISORS ARE CHANGING DRAMATICALLY



Historical analysis does not guarantee future results. For illustrative purposes only.

As of December 31, 2020 | Source: Investment Company Institute, 2021 Investment Company Fact Book

Let's start by looking at the trajectory of our industry over the past four decades. Mutual funds have been available since the 1920s, but by 1980 they had penetrated only a small percentage of the population. Suddenly and explosively—over a very short period—the culture embraced mutual fund ownership. A large reason for this was the advent of 401(k) plans. This change created a catalyst for engagement as millions of Baby Boomers began turning 35 years old. Mutual fund ownership exploded, maxed out at 46% of households in 2000 and then leveled off.¹

Another factor in the industry's growth was the enormous success of the US markets. We saw an unprecedented bull market in equities from 1975 to the early 2000s. This long period of strong returns led investors to expect great rewards. From 1981 to 2000, the S&P 500 Index rose almost 17.5% a year *every year*, with no emotionally significant corrections to cool off investor sentiment.

¹ Investment Company Institute, 2021 Investment Company Fact Book, as of December 31, 2020

By the early 2000s, the culture was awash in euphoria about the future. Anyone who invested expected to retire comfortably and early; wealthy people expected to see a magnificent expansion of their resources and established multigenerational legacies.

But several times in the 21st century, the environment changed when Boomers' expectations were shattered by big financial crises in 2000–2002, 2008 and 2020. While the markets delivered periods of euphoric returns after the Tech Wreck and the Great Correction, investors made back only what they had lost. Today we are still dealing with disruptions from the COVID-19 pandemic. The pervasive euphoria of the 1980s and 1990s was replaced by caution and then by an increasing skepticism about the original promise of investing and the role of the FA in delivering on that promise.

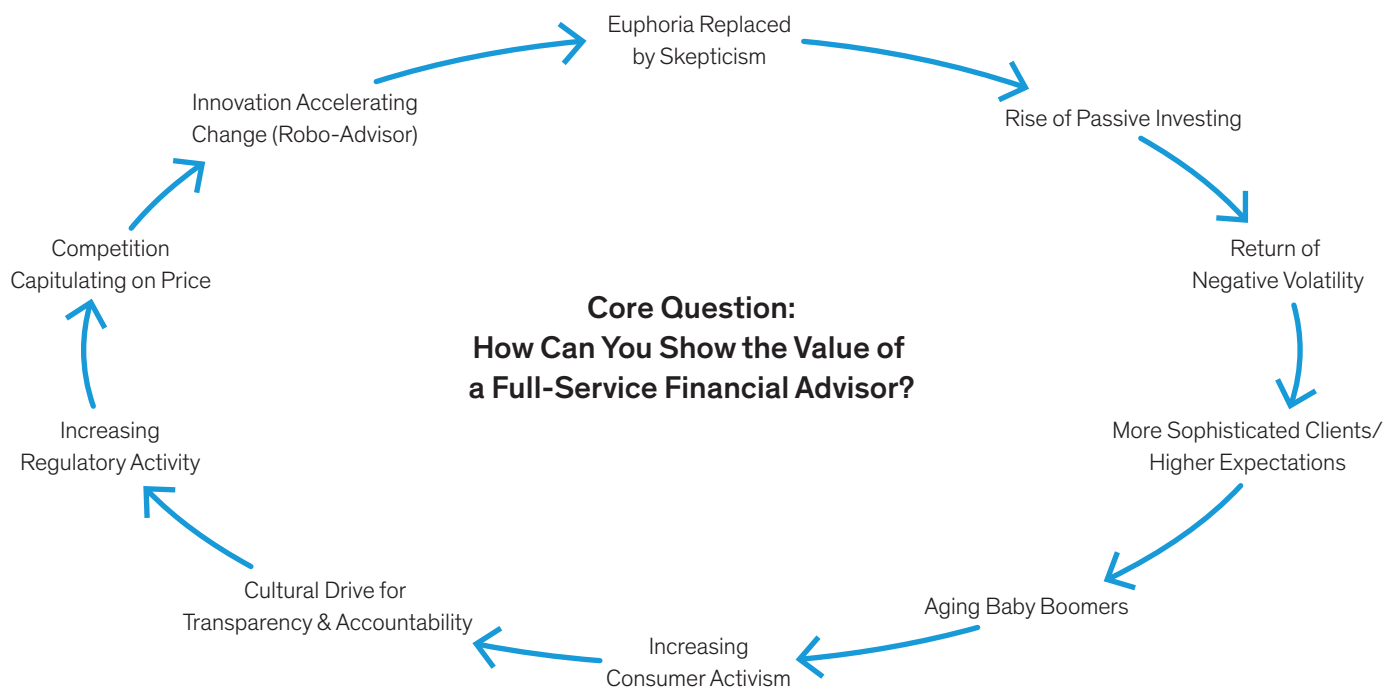
More than ever before, once-euphoric Baby Boomers are now acutely aware of their portfolios' and advisors' limits. Millions of experienced septuagenarian investors have been offered new approaches to investing—including discount providers and robo-advisors—and recognize that advisors can and will often disappoint.

The early 2000s were a period we call the Great Awakening, which was marked by growing sophistication. Today we are in the Age of Skepticism, when investors have increasing doubt about the value of working with a professional advisor.

The Trends That Are Reshaping How We Do Business

At least 10 major social trends emerged during the Great Awakening that have led to the Age of Skepticism.

FORCES THAT WILL DEFINE OUR FUTURE



For illustrative purposes only.

Euphoria Replaced by Skepticism

As we discussed, bull markets were replaced by financial crises, and investors began to be skeptical about the value of an advisor.

Rise of Passive Investing

Statistics show an accelerating rise of passive investing and a concurrent decline of active approaches. This represents a fundamental capitulation on the part of the investing public that the best an investor can hope for is marketlike returns in the various sleeves of a portfolio. Diversifying broadly, paying as low a fee as

possible and accepting the occasional down-trending market are seen as being as good as it gets.

Return of Negative Volatility

During the Age of Euphoria, and after each correction during the Great Awakening, the markets delivered highly attractive performance. Downside volatility was muted and returns were usually positive. In the Age of Skepticism, there is growing evidence that valuations are being stretched and the potential for downside volatility is increasing.

More Sophisticated Clients/Higher Expectations

As Baby Boomers became more experienced with investing and market returns remained positive, expectations about the value of investing grew.

Aging Baby Boomers

As the Baby Boomer generation moves through retirement, their needs and expectations have changed dramatically. No longer euphoric and naive, they know what to expect and how to demand a different type of service from advisors.

Increasing Consumer Activism

Consumers are being educated, inspired and provoked by organized consumer activism. For example, AARP and other consumer-focused groups question the practices of some advisors, thus raising doubts about the trustworthiness and value of the financial-services industry as a whole.

Cultural Drive for Transparency and Accountability

In the five decades since the Watergate scandal, there has been an evolution and acceleration in expectations regarding the transparency of information and the responsibility of those who abuse the trust of

others. Examples include WikiLeaks, Edward Snowden, the demand for greater accountability from teachers, and the requirement to hold business leaders responsible for the way they treat subordinates.

Increasing Regulatory Activity

The Department of Labor, the Municipal Securities Rulemaking Board, the US Securities and Exchange Commission, and the Financial Industry Regulatory Authority all embrace a responsibility of protecting investors, each from a slightly different perspective depending on its charter and those it assumes to be members of its primary constituency.

Competition Capitulating on Price

Some advisors are unwittingly disrupting the industry by dropping prices in response to questions about their value.

Innovation Accelerating Change (Robo-Advisor)

Another disruption of the traditional business model comes from the continuing evolution of technology through a digital intermediary, the robo-advisor.

Drivers of Client Satisfaction Change Through Time

Today's prudent FA needs a new set of assumptions about the advisor-client relationship.

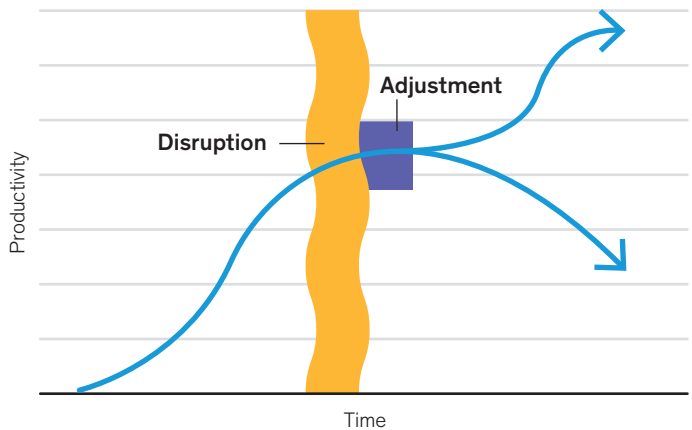
When disruptions occur, it becomes challenging to know how and whether or not to invest the time and energy needed to address the change. In and of itself, change isn't bad, especially if you're the originator of the next big, exciting thing in your industry. The problem is that disruptions are knowable only in retrospect. What we can know is that eventually, the future absolutely will not look similar to the past, and some type of change is required to help skeptical clients.

During the Age of Euphoria, the fundamental assumption was that the advisor significantly influenced investment returns and was therefore well worth the commissions or fees that she was paid. Importantly, the entire working relationship could be simplified down to the issue of performance: Does the number on the bottom of the paper make you feel good or bad? An entire generation of advisors operated on this set of assumptions—and many continue to run their business based on it.

In today's Age of Skepticism, investors' assumptions have changed; now clients are aware that the advisor has only limited impact on a portfolio's performance. The client is much more aware of price and is becoming increasingly skeptical about the value he is receiving from his full-service advisor. As we have seen, powerful forces are educating clients to question that value and are making it easier to hold advisors accountable for their behavior.

In an important way, the positive feelings of euphoria about investing and the role of the FA have been sucked out of the culture and are being replaced by questions and deeper feelings of skepticism. Today's advisors can no longer assume that positive performance will satisfy a client; they must establish a new set of assumptions about what clients value enough to pay a significant annual fee for.

ADAPT AND PROSPER— OR BECOME OBSOLETE



Source: Joel Arthur Barker, *Paradigms: The Business of Discovering the Future* (1993)

Fortunately, research from the behavioral sciences has revealed a new set of ideas that the advisor can use to inform his business model. Today's investors have a set of powerful but unspoken needs. When these needs are met, a strong bond is created that may sustain a relationship through periods of poor performance. This bond is the advisor-client relationship.

Advisor and Client: Trust as the Essential Currency

In an advisor-client relationship, the personal relationship is enhanced by a business dynamic that makes it more complex and more challenging to manage.

THE TRUST EQUATION

$$T = (C + E) (G + PC) TM$$

Trustworthiness = (Consistency + Experience) (Goodwill + Professional Competency) Time

The advisor-client relationship has both business and personal characteristics. In purely personal relationships, each party trusts the other to be consistent in his regard and care for the other; the positive quality of the relationship grows and is appreciated by the frequency of the exchange. If one party ignores the needs of the other, the relationship can sour quickly. In the advisor-client relationship, the personal dynamic is enriched but also complicated by the business dynamic: the advisor expects to receive a payment for services, and the client expects to receive meaningful value for the payment provided.

By looking at the advisor-client relationship as a combination of personal and business dynamics, we can develop a model for managing the client's appreciation of the advisor's value and learn how to proactively stimulate higher feelings of trust and interpersonal satisfaction. It begins with the advisor providing clients with the feelings of familiarity and consistency and developing the experience of trust.

Delivering performance was the priority during the Age of Euphoria. Going forward, the priority for the client-facing advisor will be to deliver the experience of trust.

Trust Cannot Be Caused—but It Can Be Managed

It's important to understand how trust works within relationships. The first essential element is that it cannot be controlled in the other person; you cannot cause another person to trust you. Trust is an experience and a label that the client gives to her advisor as a result of a series of experiences.

While you cannot cause a client to trust you, you can be trustworthy and work hard to earn each client's trust over time. Trustworthiness is expressed as a set of behaviors designed to stimulate positive feelings of confidence and reliability. You can influence the level of trust in the relationship by what you do from day to day.

The second essential element is that trust builds up over time through experiences. There's an enormous difference in the level of trust between a client and an advisor who have worked together for 20 years versus those who have worked together for less than a year. Let's look at the variables in the trust equation.

The experiences of honesty, fair pricing, transparent fees and putting the benefit of the client first must be unbroken over the entire length of the relationship. One episode of inconsistency may damage the relationship permanently. In this way, trustworthiness is highly fragile but can be managed if the positive qualities that define the relationship remain unchanged. The client must experience consistent evidence and reassurance of the advisor's goodwill and professional competency. When disruptions affect the trustworthiness of institutions and the transparency of pricing, the prudent advisor proactively provides compelling evidence to protect her trustworthiness. It's the accumulation of these experiences of evidence that builds up feelings of trust over time.

It's helpful to think of a relationship as building blocks stacked over time. When a client sees you providing goodwill and professional competency, another block falls into place. If the client doesn't feel goodwill or sees no professional competency, the buildup of trust can fall apart and the entire relationship can be called into question.

The Four Essential Experiences Clients Need from Their Advisors

To intentionally manage trust, you must understand the specific actions that will make you worthy of that trust.

Imagine that every client asks a set of questions that you must answer repeatedly. These four essential questions show your personal goodwill and professional competency.

1. Do I matter to you?

This is an essential question in any relationship. If we discover that the other person doesn't care, that we don't matter to them, we know that there is no relationship. We are, in fact, potentially in danger from that person. Having an emotional connection to someone inhibits behavior. If that inhibition is removed (i.e., the person doesn't care), then the uncaring person is liberated to serve only his own needs. This is especially problematic in the commercial advisor-client relationship. When a fee is paid, the client is aware that, to some degree, the advisor is acting out of self-interest. If the client believes his own emotional and financial interests are balanced with the advisor's self-interest, the advisor is deemed trustworthy.

This reinforces why you should provide evidence that every client matters. On a regular basis, check in and demonstrate to each client that she's important and that you keep track of the big events that impact her.

2. Do you get me?

Checking in regularly also helps you answer this question. Although it's more difficult to answer than the first question, it provides a greater benefit to the advisor who addresses it. By showing you truly understand the client, you fulfill his ultimate goal of being seen, known and appreciated. Most people report having only a handful of people who see them accurately and truly appreciate them. Taking these steps makes you hugely important to your client.

3. Are you great at what you do?

This question falls into the category of providing evidence of your professional competency. When a client is paying you a fee, sustaining positive feelings requires more than just warm feelings of care and being seen. The fee is being paid to receive a value, and that value must be connected to its associated cost. In this Age of Skepticism, the client is being actively educated to question that cost and to compare your fee to what other providers charge.

To continue valuing you, the client needs to understand that you're providing superior services compared to others and that your services are of great importance (and thus great value) to her well-being. Prudent advisors understand that to sustain the client's perception and appreciation of their value, they must provide evidence of superior skills. Fortunately, the work you do on your client's behalf most likely provides you with the opportunity to reveal your skills and superior professional competency.

4. Do I have reason to believe that the future I want is the future I will get?

The fourth question looks into the future. In the Age of Skepticism, you and your client must agree on what the desired outcomes are and that achieving those outcomes is what you're being hired to accomplish. Sometimes a client's desired outcomes don't require his investments to outperform their relative benchmarks. In fact, it isn't uncommon for a client with clearly defined goals to desire less risk and be satisfied with a more muted annual return.

Effective Messaging Starts with Understanding Motivation

To create highly effective messaging, we must first understand how the human brain—which will receive the information—is designed.

Our brain is a wonderfully complex network of specialized structures, each designed to accomplish a different task. With all its complexity, the brain's primary responsibility is to help us survive in a complicated and threatening environment. To do so, it must constantly cope with and sort through an incredible amount of information.

The brain exercises rational thinking by using the neo-cortex, located near the front of the skull. This is where analytic thought, calculations, planning and perceptions of time are processed. When presented with an advanced math problem, the neo-cortex activates, accesses and grinds through the proper protocols, then generates a solution. Such analytic processes can take minutes or hours—sometimes even days—of focused effort.

The words *focus* and *effort* are important for understanding the neo-cortex and its role in decision-making. When there's plenty of time to act, the brain can activate these skills and invest resources to process, analyze and solve problems. In many cases, the time involved and the effort required are worth it: humanity's greatest achievements have been generated through applying the scientific method, careful research, creative problem solving and the communication of ideas. These skills are controlled by the neo-cortex and are available for use if there's enough time to invest in the effort.

However, there are many situations when there isn't enough time to process all the information required to make a rational decision. In other cases, the amount of processing that would be required

to make a thoroughly considered decision is far too great to be accomplished. Because survival requires decisions to be made, often very quickly, the brain has a more primitive decision-making structure. This is located in the center of the brain and down toward the base and includes the cerebellum, the brain stem and the amygdala. This system relies on emotions and simplifications to make predictions about the world that inform how best to act for survival and success.

Both the neo-cortex and the primitive brain have roles in how the brain receives and processes a message. First, the brain tries to rationally understand what's being communicated by using the neo-cortex to decipher the message, then determines whether the information is personally relevant and decides what action to take. However, the second step in receiving a message—reacting by taking action—is controlled by the more primitive area of the brain.

This is why, for a message to have the optimum impact on the listener, it must activate the thinking part of the brain (so that the information is seen as relevant and is processed) as well as the more primitive feelings and automatic predictions that provoke motivation.

Additionally, research in behavioral finance tells us that the brain is automatically more motivated to avoid pain than to pursue pleasure or gain. So the structure of the message must activate concern about loss or a potential danger.

The Brain as a Predicting Machine

Research about how the brain works reveals that predicting patterns is potentially the most important function of the brain when it comes to survival and success.

Dr. Lisa Barrett tells us, “Through prediction, your brain constructs the world you experience. It combines bits and pieces of your past and estimates how likely each bit applies in your current situation... Prediction is such a fundamental activity of the human brain that some scientists consider it the brain’s primary mode of operation. Predictions not only anticipate sensory input from outside the skull but *explain* it... This efficient, predictive process is your brain’s default way of navigating the world and making sense of it. It generates predictions to perceive and explain everything you see, hear, taste, smell, and touch.”²

This idea of the brain as a predicting machine deserves much more attention, as it will inform virtually everything you do when creating an effective message. It’s the very process of using information from the past to accurately predict the future that makes a message impactful. The brain is hardwired to take in lots of information from the sensory channels, with visual and auditory stimuli being the most richly received and processed.

Making sense of the world starts with perceiving, processing and storing events. Importantly, events can be actual experiences or *they can be experiences described by another person*. If the description is rich enough to register as informative, the brain can use that material for the future. In this way, the brain is constantly updating the database from which it will make predictions.

The brain uses the same information-gathering process to take in new information about the present moment. Instantaneously, the brain filters all previous experiences to see which are similar to the current situation. These historic records are sorted out and a few relevant scenarios are retrieved that appear to “fit” the current situation most accurately.

Then, using the previous experiences that have been stored in its memory, the brain processes these scenarios into a prediction about how the current event is likely to unfold. Importantly, the brain typically approaches such predictions from a conservative perspective: the pattern of loss aversion means that the brain tends to assume the worst-case scenario when predicting the future for the purpose of being protective.

The final step is to generate a motivation to take action based on the prediction that was made. Unfortunately, new situations don’t always map accurately to past learning experiences, and prediction errors are common. As a simple example, think of the shortstop who fields thousands of ground balls and almost always accurately predicts the ball’s trajectory and makes the catch—except occasionally, the ball makes an unexpected hop and throws off his prediction about where to hold the glove. When it comes to investing, the number of possible “unexpected hops” is significantly greater than in baseball—and no investor has seen as many scenarios as the professional athlete. Therefore, when designing a Capital Markets Perspective, it’s important to provide descriptions of events that clients may never have seen or experienced so that those insights can inform the way their brains think about the future and decide on appropriate action.

2 Dr. Lisa Barrett, *How Emotions Are Made: The Secret Life of the Brain* (2017): 59–60

Stories Provide Learning Without the Pain of Experience

Since ancient times, storytelling has been a way for older people to share experiences with the next generation.

For thousands of years, our earliest ancestors gathered together and told stories. Most often, the older members of the group would use stories to teach important lessons to the younger members. Storytelling was a way of sharing experiences so that younger members of the clan could benefit from senior members' skills and experiences.

Storytelling is built in to many aspects of modern human experiences for the same reason. It takes children about two decades to learn enough from parents, teachers and peers to be able to function successfully in modern culture. New employees must learn from the stories told by their senior, more experienced colleagues. The drill sergeant shares his decades of practical experience with new recruits to help them avoid learning by trial and error. Over thousands of years, the human species has learned that trial and error pose an enormous risk, while learning from stories does not. This explains the popularity of novels, television shows, plays and movies. These are more advanced forms of storytelling that serve the same purpose: allowing the person watching to have a vicarious experience of learning without the risk of the actual experience.

Your Capital Markets Perspective fulfills the same role in the lives of your clients. By telling a well-formed story that provides insights about how the markets operate and then connecting those insights to guiding principles that inform decisions, your message provides the client's brain with painless learning that it can use to create predictions and to inform future behavior. In a sense, this type of message allows you to share your wisdom as a professional so that your clients don't have to learn the hard way. Another by-product of crafting an effective and impactful message is that it positions you as the wise sage who possesses powerful and valuable knowledge: i.e., "Are you great at what you do?"

In order for your message to fulfill this role, it must be structured as a story with a beginning, a middle and an end describing a series of events that are meaningfully linked together. Too often, advisors make their Capital Markets Perspective a series of lists, numbers or descriptions of key indicators. When this happens, clients have great difficulty understanding the meaning of the information and knowing how to apply it to their own situation. Such presentations are experienced as frustrating and boring, and have led to the widespread belief that clients aren't actually interested in understanding the capital markets.

In fact, nothing could be further from the truth. Clients who are deploying their hard-earned capital into the markets are very interested in understanding what they're doing and in being able to make some kind of prediction about the future. Getting a data dump of complicated and hard-to-understand information doesn't provide the right type of *experience*. A good story describes events in a way that is understandable and that links together over time: it's the links between events that equip the brain to make predictions from virtual experiences that connect to the real world.

This means that your Capital Markets Perspective should be crafted as a story that moves from explanation to explanation about events that connect to one another. Construct the story to allow you to explain how things work so that your clients can use the information to make better sense out of their world.

The experienced advisor knows that most investors are fascinated by stories about successful businesses and obsessed with the possibility of finding an investment in a company that is about to accelerate dramatically. These investments are understandable as a story that unfolds from the past to the present; they illustrate an exciting (and lucrative) possible outcome. When stock stories come alive, they're fascinating to the investor seeking a place to deploy assets.

A Picture Is Worth a Thousand Words

Another dimension of creating impactful messaging concerns the use of visuals. For the ancient storyteller, words and gestures had to suffice to make each element of the story come to life. Our primitive ancestors didn't have the benefit of television, movies or PowerPoint. The storyteller's words were sufficient to activate imaginations. And because there were few alternative entertainments after the sun went down, the stories shared around the campfire were the most compelling messages around.

For modern humans, entertainment options are numerous. Two or three generations ago, people were limited to reading a book or listening to the radio, which forced them to exercise their visual imaginations to bring the story they were listening to or reading to life. Today's listeners have grown up with all that work being done for them by talented visual artists, actors and animators. For messages to be optimally effective today, they must be constructed from meaningful visuals that tell key parts of the story.

This is another place where advisors make a mistake: a visual is not a list of numbers. Effective visuals tell their own story dynamically, by showing either a process unfolding over time or a comparison of

two objects that illustrates an important meaning. Even a graphic as simple as a single line on an XY plot can show an important part of a story. You can certainly include the source data for the graphic when necessary, but the primary purpose of a graphic is to activate the brain's visual processing, which increases retention of the information dramatically. As Dr. Lynell Burmark says, "Unless our words, concepts, and ideas are hooked onto an image, they will go in one ear, sail through the brain, and go out the other ear. Words are processed by our short-term memory, where we can only retain about seven bits of information... Images, on the other hand, go directly into long-term memory, where they are indelibly etched."³

Each step in the story that presents your message must function as an event that makes sense to the listener. It must be a piece of information that's useful for making predictions about the future. In addition, each event must connect to the events that precede and follow it, like a progression of steps that lead from one to the next. A good story has coherence throughout and takes the listener to a destination that's useful.

³ Dr. Lynell Burmark, *Visual Literacy: Learn to See, See to Learn* (2002): 17

Eight Guiding Principles for Effective Messaging

The human brain is not just collecting events as it processes experiences; it's creating meanings and building small maps of how the world works.

Our brains use visual maps because they include the information of each event and how events combine to create specific outcomes. In a sense, a client's brain is constantly looking for information to help it make sense of the world. An effective message makes the connections between events easy to decipher.

As you prepare to create your story, it's helpful to think of the capital markets as a big machine made up of interlocking parts that work together in understandable and predictable ways. As great investor and author Ray Dalio explains in his book *Principles*, "I believe that everything that happens comes about because of cause-effect relationships that repeat and evolve over time. At the big bang, all the laws and forces of the universe were created and propelled forward, interacting with each other over time like a complex series of machines that work together....All these machines are evolving together to produce the reality we encounter every day. Look to the patterns of those things that affect you in order to understand the cause-effect relationships that drive them and to learn principles for dealing with them effectively."⁴

With these observations in mind, we can now consider eight guiding principles that will ensure that your Capital Markets Perspective delivers the maximum desired impact on your audience.

1. Tell a Story

This is the most basic guidance: an effective message has a beginning, a middle and an end that connect each specific part of the message to the information that precedes it and follows it. Each step of the story must make sense, and the entire story must connect to create a larger, more comprehensive message. It's important to remember that the listener's brain will pay attention to the data you're providing only if the information can help the listener make sense of the world and guide future decisions.

2. Follow a Structure

To ensure that your story makes sense to the listener, organize the order in which you present the information. The order can change depending on what you're trying to accomplish, but a structure helps you sort out the data and decide what to include. In this way, a structure operates like a filter that allows only the most relevant information through to the final message.

3. Define Your Desired Outcome

The structure of your story and the specific content you include will be heavily influenced by what you want the story to accomplish. This is the desired outcome of the story you're telling: the reason you're going to the effort to tell a story.

The capital markets are dynamic and present your clients with a constant barrage of stimulation. Fortunately, there are usually only two basic responses that you want from your clients. Sometimes you want to provide reassurance, increase the client's sense of confidence in the future, and decrease his anxiety and emotional need to take action. This type of Capital Markets Perspective can be understood as a comforting presentation. In other circumstances, the situation in the capital markets may require that you take some type of action. In these conditions, the desired outcome of your message will be to stimulate an emotional response to *increase* motivation to take action.

The structure you use and the information you select will be very different depending on which of these desired outcomes you intend to achieve. Before you set out to create your message, determine which outcome you desire.

⁴ Ray Dalio, *Principles* (2017): 127

4. Make It Visual

As we explored earlier, the human brain is organized around processing visual information. Our primitive ancestors had limited tools at their disposal by which to stimulate visual images in the minds of their listeners. They had to rely on the quality of their voice, hand gestures, body movements and their listener's imagination to create the mental images that brought the story to life.

Today we have many tools that are designed to translate concepts and information into visual imagery. To the extent possible, your story should move from one visual to the next and should contain the fewest words needed to make those visuals understandable. Simple line drawings and bar charts can bring most stories fully to life, especially when you show the connections between events and reveal how past processes inform future circumstances.

5. Reveal the Mechanisms

It's helpful to follow Ray Dalio's advice: "I believe that everything that happens comes about because of cause-effect relationships that repeat and evolve over time... All these machines are evolving together to produce the reality we encounter every day." Of course, no one can fully understand and predict in detail the specific evolution of the capital markets; the complexity is just too great. However, the markets are understandable at least in general. Revealing the cause-effect mechanisms that are understood provides your clients with some of the insights they need in order to know more about the direction in which things are likely to go and what actions are best taken.

By explaining the cause-effect mechanisms that are operating within the markets, you stimulate the thinking part of the client's brain. It's helpful to remember that as you build your story, your client's brain is gathering information, attempting to make sense of the world and trying to make accurate predictions so it knows what to do. Your story should be designed to feed this process: information leads to a prediction that stimulates action.

6. Explain the Implications

Revealing the mechanisms of the capital markets isn't enough to satisfy the brain. You will also need to explain the implications of those mechanisms as they will likely unfold in the future. The difference between an amateur investor and a professional advisor has largely to do with how much detail about the mechanisms of the market each has mastered. Amateurs have a limited database because they have minimal personal experiences and inadequate time to process stories and explore the details of market behavior. By definition, a professional has a much larger database of experiences and dynamic understandings to draw from. This provides a richer source of ideas, cause-effect relationships and historical dynamics available to inform decisions.

One of the downsides to having a larger pool of information at your disposal has been called "the curse of knowledge" by Chip and Dan Heath in their book *Made to Stick: Why Some Ideas Survive and Others Die*. The brothers describe the tendency of highly knowledgeable storytellers to assume that their audience shares the same depth and breadth of knowledge and can make huge leaps of understanding based on a small amount of explanation. Unfortunately, if your client doesn't thoroughly understand the mechanisms that you're describing, she may be unable to comprehend the future implications of the message and will likely miss the point you are trying to make.

Avoid this breakdown by reviewing your story as you create it and ensure that the implications of each part of the story are clearly explained: what bad or good thing is likely to happen next because of this and how it will affect you if it happens. This fulfills your client's need to see how the information you're presenting helps him predict what will happen in the future and determine what to do about it.

7. Include the Timeless Principles of Investing

Your story should also include two or three guiding principles for investing. These principles will be determined by the current market conditions and the desired outcome of the message. Our ancestors used storytelling to provide survival guidance for younger tribe members. In the same way, your Capital Markets Perspective equips clients to become better investors by increasing their practical knowledge about investing.

The whole purpose of any meaningful story is to install a core insight or guiding principle into the mental toolbox of the listener. Story-based insights and actual experiences both provide the same raw material: information about the world designed to improve the brain's ability to predict. The most helpful insight is one that will apply to many different situations and provide reliable guidance for accurate predictions and behavior.

Examples of such principles are those that inform every investment decision a client may be faced with. The most beneficial principles reveal either market dynamics or human dynamics that impact investment decisions. Principles like "Regression to the mean is inevitable," "Bull markets are created on pessimism and die on euphoria" and "The human brain tends to inappropriately extrapolate patterns into the future" provide reliable insights that are applicable in many different market conditions.

8. KISS (Keep It Short and Simple)

Finally, your story must be kept manageable. The capital markets are far too large, complex and dynamically unstable to thoroughly understand, let alone try to explain in a 10-minute presentation. Define your desired outcome, select the mechanisms you want to reveal and the implications you want to explain, and choose two or three principles that you want to provide. That's plenty of material to weave into a short but meaningful story.

Focus Your Message on the Most Critical Issues

While it may seem daunting when you first attempt to craft a new Capital Markets Perspective, you have lots of resources to help you with the task.

When beginning to create your Capital Markets Perspective, look to your firm or partner firms for a regular articulation of the market issues that their strategists think are most important or their perspectives and insights. Popular media also help to sort out key issues and prime the attention span of your clients for certain topics. As behavioral economist Daniel Kahneman points out, the human brain is hardwired to elevate familiar topics to “most important” status on the basis of how frequently that topic has been presented. Kahneman calls this phenomenon availability bias, which will cause clients to be very interested in the themes that are most frequently mentioned by various media outlets.

Because of the dynamic nature of the capital markets, topics tend to rise and fall in terms of their value to your story. This short list can help

you sort out the relevant topics that most often provide insights into the markets. You can select three or four that are most helpful to the desired outcome that you have for your message.

Once you've selected the themes you will be illustrating and explaining, you can begin to consider how best to visualize the information the client needs to receive. Every picture in your presentation should tell a portion of the story, and the more you can show how a cause in one area of the markets produces an effect in another area, the more powerful your presentation will be. It's important to remember that the client's brain is constantly searching for information that helps predict what actions need to be taken. Powerful visuals show the relationship between various pieces of information.

KEY MARKET ISSUES

Monetary Policy/Inflation

Equity Valuations

Currency-Market Fluctuations

Value Investing Trends

Global Investment Dynamics

Oil and Other Commodities

Trends in Corporate Profitability

Major Political Events

Domestic/Global GDP

Fixed Income—Global Bond Markets

Growth Investing Trends

Large-, Mid- and Small-Cap Trends

Real Estate/Housing

Sector Dynamics

Consumer Sentiment

Natural Disasters with Global Impact

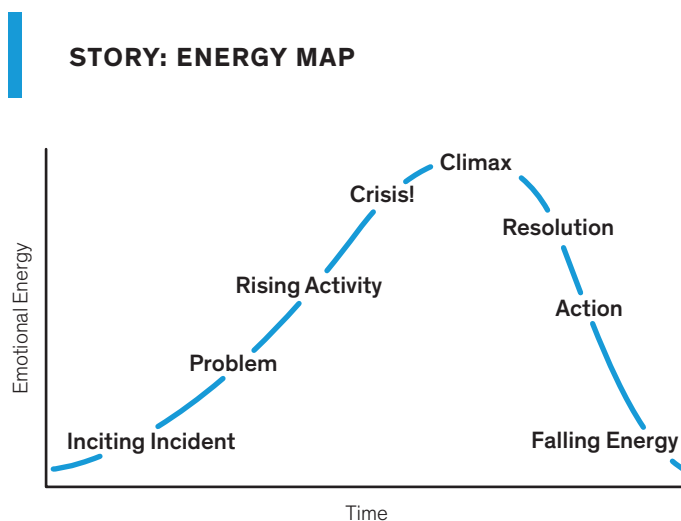
A Good Story Stimulates Thinking and Feeling

An effective message is not just an aggregate of information; it's a progression of ideas that link together.

The power of storytelling has advanced dramatically now that technology releases the reliance on the listener's imagination. The first step was catalyzed by the invention of printing technology. For the first time in the history of our species, the storyteller was liberated from writing multiple copies of his story by hand and instead could memorialize the structure and content in a book.

This meant that the storyteller could perfect the flow of ideas and the quality of the images being described. The emphasis moved from acting out the story with gestures and body positions to polishing the descriptions that the reader would later digest. The pace of the evolution of human culture accelerated dramatically once the quality of a memorialized story could be elevated by the hard work and artistry of the writer. More recently, the imagination of the writer has been liberated by film and television cameras and—over the last few decades—the emergence of high-quality computer-generated images. Now the storyteller can take full control of the visual images that the listener encounters.

Importantly, as the television and film industries have developed their own professional training discipline, the importance of story structure has been rediscovered and elevated to a significant degree. Donna Lichaw is an author and documentary filmmaker who helps writers understand the timeless principles that inform great storytelling: "Humans are sense-making creatures, and story is our most critical sense-making tool... Given how long we've lived with story, it's not surprising that Aristotle uncovered a working model for it long ago. Basically, he said that every story needs three things: characters, goals, and conflict. What weaves these elements together is a structure or a series of actions that have a shape to them... First, every story has a beginning, middle, and end—with the middle typically taking up a longer period of time than the beginning or end... Next, every story has a structure... typically called the *narrative arc* or *story arc*, which is a chronological series of events... [T]he story builds in excitement, the pace of its action increases over time until it hits a high point, and the story winds down before it ends."⁵



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Lichaw's concept of a narrative arc includes steps that appeal to the human brain. The inciting incident starts the story and represents the beginning. This is followed by rising action as the characters and dynamics of the story take shape. These elements weave together to create a crisis that captivates the thoughts and feelings of the listener. The result is the climax, where the meaning of the story is revealed and the conflicts are resolved. The hero of the story takes the right action to solve the problem, and the story winds down to its end.

The result is that the listeners are able to vicariously participate in the learning experience of the characters in the story, gain some new guiding principles for their survival toolbox and emerge from the story more able to predict how future dynamics will unfold so that they can take the right action. The implications for empowering your Capital Markets Perspective are clear: the more your clients can identify their situation within current market conditions, the more meaningful and relevant your story will be to them.

5 Donna Lichaw, *The User's Journey: Storymapping Products That People Love* (2016): 8–9

Two Structures for Storytelling

While your Capital Markets Perspective will not be as scintillating as a best-selling novel or award-winning movie, it can be highly impactful in achieving your desired outcome.

There are two basic desired outcomes that you are seeking to achieve: either you want to increase emotional motivation to stimulate action or you want to decrease emotional activation to provide comfort and reassurance. There are different structures for each of these outcomes.

A Structure for Stimulating Action

In order to increase the emotional reactivity of your clients and create more motivation to act, you will need to activate their loss aversion. Research in behavioral finance has uncovered that pain is more than two times as impactful on human decision-making as pleasure. Therefore, if you want to activate motivation, introduce the concept of pain or loss as the starting point of the presentation. Here's a six-step structure that will help organize your story:

1. Introduce a Problem

Start by framing the reason for the presentation as a potential problem that has implications for the investor. This galvanizes the brain's attention and desire to acquire more information so it can make a prediction and can take the right action.

2. Reveal the Mechanisms

A good story links together several cause-effect mechanisms as a way of making sense of the capital markets. Select a short list of the most relevant issues—those that most immediately inform the action that you want the client to take. Stimulate the client's rational thinking process by illustrating the key mechanisms that need to be understood to assist in predicting the future. This further engages the brain's desire to gather relevant information in its toolbox of concepts.

3. Explain the Implications

Avoid the mistake of assuming that the client will understand the likely future outcomes of the mechanisms within the markets; explain and illustrate each implication of the mechanisms you've revealed to ensure that the client makes an emotional connection to the issue. Consider saying, **"This has happened already; this is likely to happen next. If that happens, then this will be the impact on your investments. We don't want that to happen."**

Introducing the problem and revealing the mechanisms provide the brain with the information it needs to make useful predictions. Explaining the implications guides the client's brain to the predictions that are most likely to affect her well-being in the future. This brings the brain to the place where it wants to take action and is ready to receive guidance for what action to take.

4. Propose a Solution

In this structure, the climax of the story is reached when all the important implications have been explained and understood by the client. Ideally, this will activate strong emotions and a desire to take action.

5. Reveal the Mechanisms of the Solution

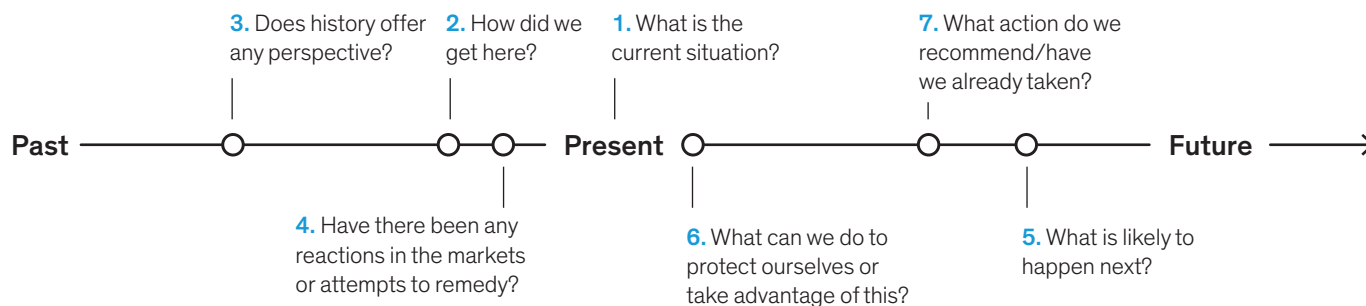
The climax of the story is resolved as the mechanisms of the proposal are explained. The first three steps increased the emotional energy within the client and created powerful feelings and the motivation to take action. By proposing a solution and then explaining the mechanisms that make up the solution, you direct the client's emotional energy toward the desired action that your Capital Markets Perspective was originally designed to stimulate.

6. Close for a Next Step

The client's emotional energy is channeled into the desired outcome of action. This is aided by the client's natural desire to predict the future to know what action to take now. Your message will be effective to the extent that it activates this process and then guides the "gather information/make a prediction/take action" instinct to the action that is correct according to your professional point of view.

Two or three timeless principles of investing can be included when you're explaining the implications and when you are proposing the solution. As you introduce a principle to clients, it's helpful if they can see how it connects to and informs the current situation. Ideally, you will want the proposed solution to be a great example of the principle you think best informs the current situation.

HOW TO CREATE COMFORT AND FEELINGS OF SECURITY



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When developing this type of story, there's always a tension between providing enough information to activate the emotions of the client and keeping it short and simple enough to present in 10 minutes or less. As a rule of thumb, the first three steps in the structure should take about two-thirds of the time you budget for telling the story, and the last three steps should take up one-third of the total time. It's much more important that you fully activate the client's emotions and desire to take action than it is to create a detailed argument of what action to take; the client's natural desire to predict the future and take action will automatically grab hold of your vision of what is in her best interest.

A Structure for Increasing Confidence

The second story structure is designed to decrease a client's emotional reactivity, provide reassurance and stimulate feelings of confidence. Anxiety is reduced by a story that reveals that the advisor has already gathered information, understood the mechanisms of the market, predicted the trajectory and taken appropriate action. Instead of the client having to figure out what to do to take care of a problem, the advisor reveals that the problem has already been taken care of.

This structure allows you to answer two questions—"Are you great at what you do?" and "Do I have reason to believe that the future I want is the future I will get?"—so that the client's emotional concerns can be satisfied.

There are seven steps to this story and a slightly different narrative arc:

1. What is the current situation?

The story starts with several observations of the current conditions of the market. This creates a shared agreement about the issues that exist in the present moment. It's helpful to look at materials provided by your firm, the media and select asset-management partners to choose the themes you will use to describe the current situation.

2. How did we get here?

The cause-effect mechanisms that led to the current situation are revealed and explained. This part of the story shows the client that you have a deep understanding of the markets and that you're paying attention to the processes that are unfolding.

3. Does history offer any perspective?

When it comes to investing, most clients don't have a thorough appreciation of the information available from the past; most investors have, at most, two or three decades of experience with investing and may have seen only two or three full market cycles unfold.

Using a longer sweep of history provides a richer framework of information for the client to use and allows you to provide better patterns of data that will inform the future. If left with an impoverished view of the world based on a limited set of information, the client may make inappropriate extrapolations

from bad data. By providing a larger perspective, you can find more accurate precedents to reflect upon. You also establish your stature as a capable professional with command of a much greater database of knowledge than the client (i.e., “Are you great at what you do?”).

4. Have there been any reactions in the markets or attempts to remedy?

Depending on the attributes of the current situation, various institutions (like the US Federal Reserve) may have reacted with strategies designed to affect the trajectory of the markets. There may also have been subtle (and not so subtle) reactions within various subsets of the markets that will impact outcomes. These forces are worth noting, especially if they inform the strategy that you have elected to use to navigate current market conditions.

5. What is likely to happen next?

This is the ultimate question for the client: What does the future hold and what action should I take? While market conditions are never simple and you will never be able to thoroughly explain what has happened or accurately predict what will happen, there are many processes in the markets that are understandable and that allow for a rough approximation of future outcomes.

Respect the impossibility of accurately predicting the markets, and don't provide highly detailed predictions that could be misunderstood as calling the market. Instead, make general observations of how the market is likely to behave that provide enough information upon which to decide on a course of action.

6. What can we do to protect ourselves or take advantage of this?

Depending on the current conditions and recent responses, there may be dangers or opportunities ahead that require appropriate action. This step will be determined by what you anticipate will happen next and the best course of action for the client to take: those actions may be protective or opportunistic depending on

the trajectory that you anticipate. It's helpful to use one or more timeless principles of investing here to support the strategy that you will pursue.

7. What action do we recommend/have we already taken?

The final step is designed to bring closure to the story and dissipate the emotions that have built up in the client. Many times, your investment strategy will already consider general market dynamics so no other action will be necessary. In these cases, the story is designed to reassure clients that, despite the events of the day, the investment process is sound and they can have confidence that the future they want is likely to be the future that they will get.

Sometimes, you may have already taken actions designed to protect the interests of the client or to take advantage of the opportunity. In these situations, the story is designed to reveal your strategy, confirm your wisdom, and reassure the client that all is well and that, despite market dynamics, the future is still bright.

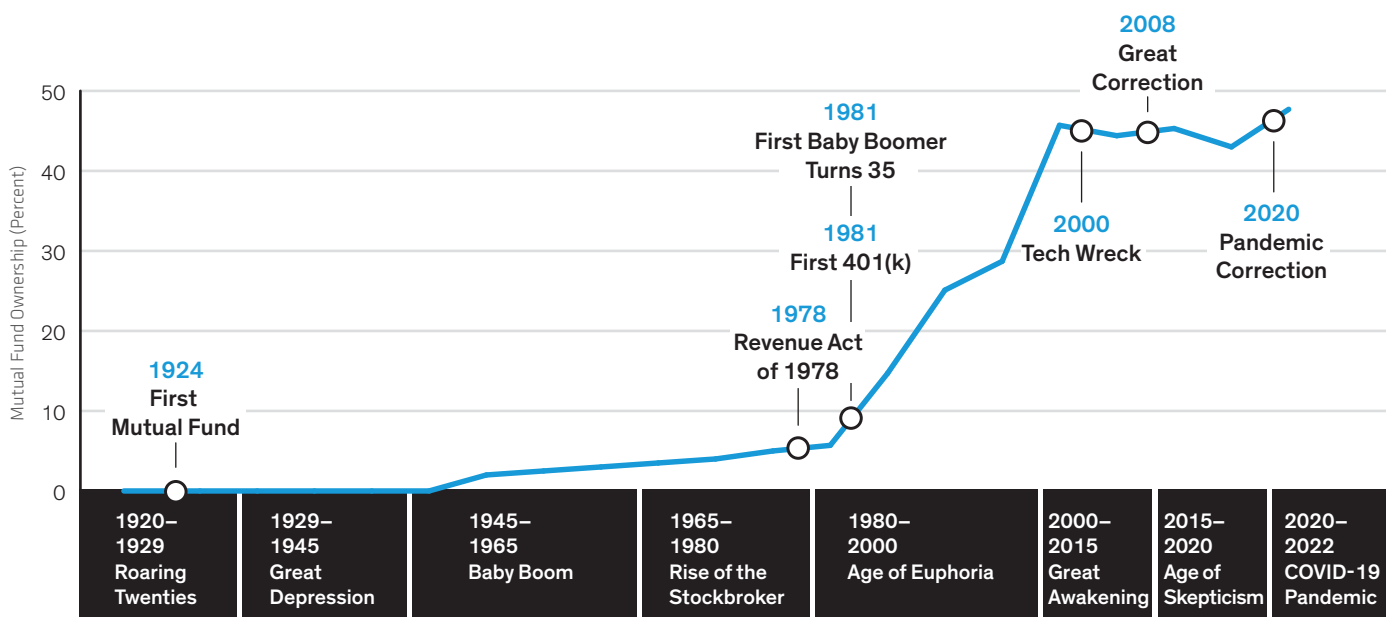
In other cases, you may be telling the story so that the client will agree with the strategy you're planning to use. In all three instances, the purpose of the story is to confirm your professional knowledge, reassure the client that the situation is being managed wisely and let him know that he can have confidence in the future.

To understand the power of story structure, we must recall that the brain's primary tasks are to take in information, make predictions about the future, and determine what actions (if any) need to be taken to ensure survival or success. These story structures are designed to show the client's brain that the advisor is paying attention to the events of the day, understands what the events mean and has appropriately addressed the situation. This tends to reduce client anxiety and eliminate the feeling that there is some need to take action. Over time and after hearing many similar stories that provide comfort and reassurance, the client will become better equipped to manage her own emotions.

Key Visual Strategies

Here are a few additional guiding principles about how to use visuals that will increase the impact of your Capital Markets Perspective.

KEY VISUAL STRATEGY: THE TIMELINE



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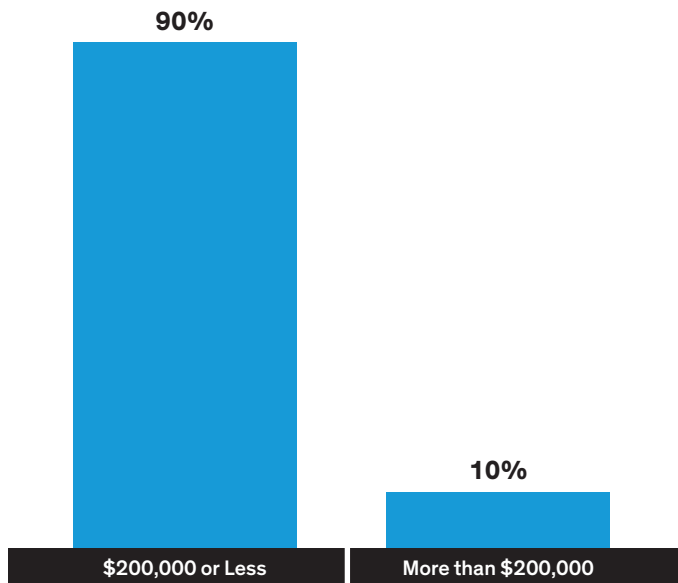
As of December 31, 2020 | Source: Investment Company Institute, 2021 Investment Company Fact Book

The Timeline

One of the most important types of visual images that you will use is the timeline, which represents a dynamic process unfolding over time, usually by tracking a single indicator from period to period. An example of this is how mutual fund ownership has evolved over time.

Timelines can be created by lines that show a smooth progression from point to point in time with a line chart or by rectangles that show discrete values next to one another. The purpose is to reveal dynamic processes that help to extrapolate likely outcomes in the future. Part of the power of a timeline is to show the progression of previous patterns so that the client can see that the current situation is “just another one of those.”

THE BRAIN RECEIVES AND UNDERSTANDS VISUAL COMPARISONS INSTANTLY



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The Bar Chart

Another key visual strategy is the use of vertical rectangles to show comparisons of value. Bar charts provide clear visual cues to the client's brain about how to distinguish the magnitude of one idea in comparison to another. When you want to indicate that "there is a big difference between these two values," it's helpful to use tall, skinny rectangles that look very different from each other. When you want to show that "there is very little difference between these two values," the brain will see two bars as similar if they are wider and with a scale that minimizes the differences.

In either case, the power of the rectangle is that it directly informs the brain of data that are more consistent with what the brain originally

| US Dollars (in 000s) | Percent |
|----------------------|---------|
| ≤\$10 | 41.4 |
| \$11-\$20 | 11.9 |
| \$21-\$30 | 7.3 |
| \$31-\$40 | 5.1 |
| \$41-\$50 | 3.9 |
| \$51-\$60 | 3.1 |
| \$61-\$70 | 2.5 |
| \$71-\$80 | 2.1 |
| \$81-\$90 | 1.8 |
| \$91-\$100 | 1.6 |
| \$101-\$200 | 9.1 |
| >\$200 | 10.2 |

had to work with in nature. Strings of numbers or lines of words are symbols of actual values; words and numbers don't exist in nature, so the brain must go through multiple steps of interpretation to understand the difference. For example, the difference between 100,000 and 190,000 is very small in terms of the actual visualization of the values: the two numbers have the same number of digits, and the visual difference between a 9 and a 0 is quite small. Contrast this with a pile of 100,000 rocks compared to 190,000 rocks, and the difference is enormous: 190,000 is almost twice as many rocks as 100,000. Because the brain is hardwired to use physical size as a key indicator, your message will be emphasized when you present data as close to the original types of information that the brain evolved to process.

The XY Plot with Multiple Variables

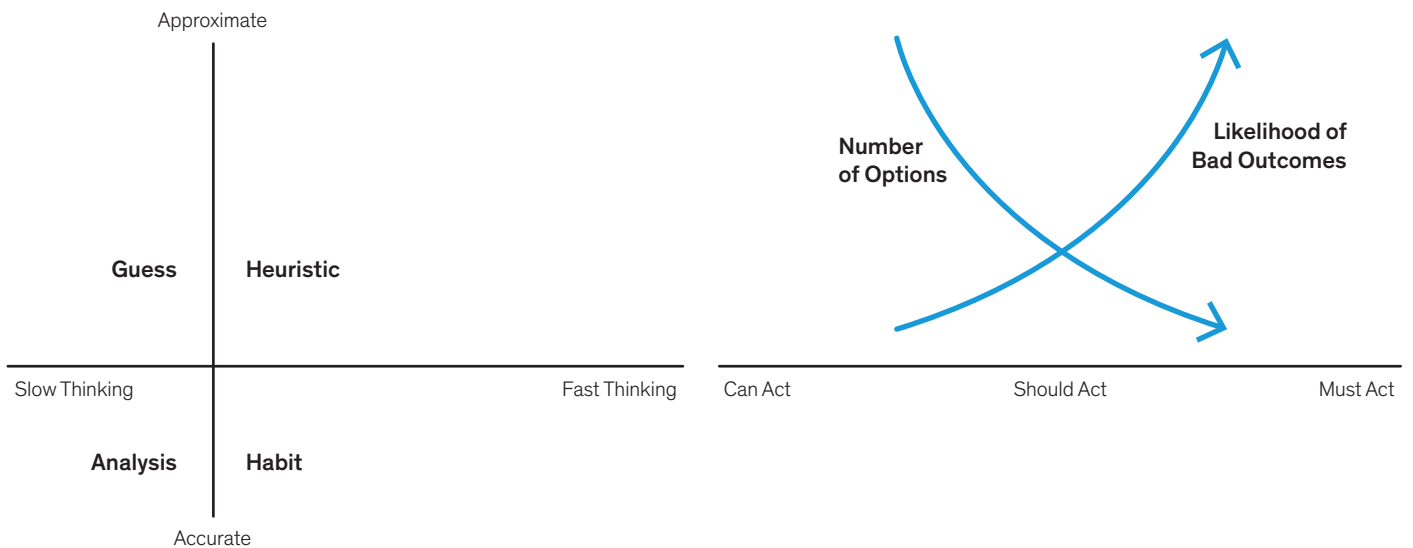
The physical nature of the way the brain prefers to use information shows how to best visualize dynamic cause-effect processes that represent multiple variables. Your message will carry greater meaning and be more impactful if the visuals you use make it easy for the brain to see the dynamic you are describing.

An XY plot comparing two or more dynamic processes that are related through some type of cause-effect relationship is a powerful storytelling aid. As an example, think of the relationship between the yield curve and the value of municipal bonds or between inflation and its effects on equity prices over time. There are many such relationships that inform investment decisions, and the more you can show how they relate and influence each other, the more you will activate another one of your client's built-in sense-making patterns.

Tens of thousands of years ago, humans used a simple rock in the hand to crush objects. Almost immediately, our early ancestors learned that they could throw the rock and affect the world at a distance. Importantly, to use a rock in hunting, the hunter's brain had to "predict" two trajectories: the motion of the running animal and the necessary motion of the rock to intercept it successfully. The hunter's brain would literally imagine two lines intersecting at a point in the future and use that information to aim the rock to hit the target.

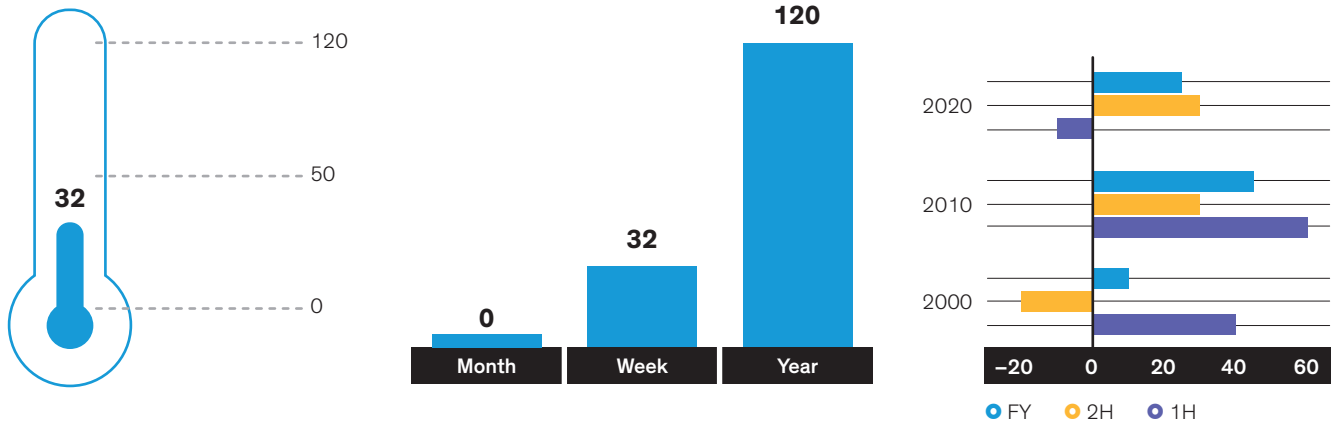
Because of this built-in capability, your client's brain will respond instantly to similar visual representations that show how a process at one point in time will affect a closely related process at a second point in time. In fact, virtually all of the brain's predicting activities are focused on these types of relationships; the more you illustrate dynamics in this way, the more your message will use the natural language of the brain's predicting processes.

SHOWING RELATIONSHIPS OVER TIME HELPS THE BRAIN PREDICT THE FUTURE



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KEY VISUAL STRATEGY: UP/DOWN ORIENTATION IS BETTER THAN SIDE-BY-SIDE



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Up/Down vs. Side-by-Side Orientation

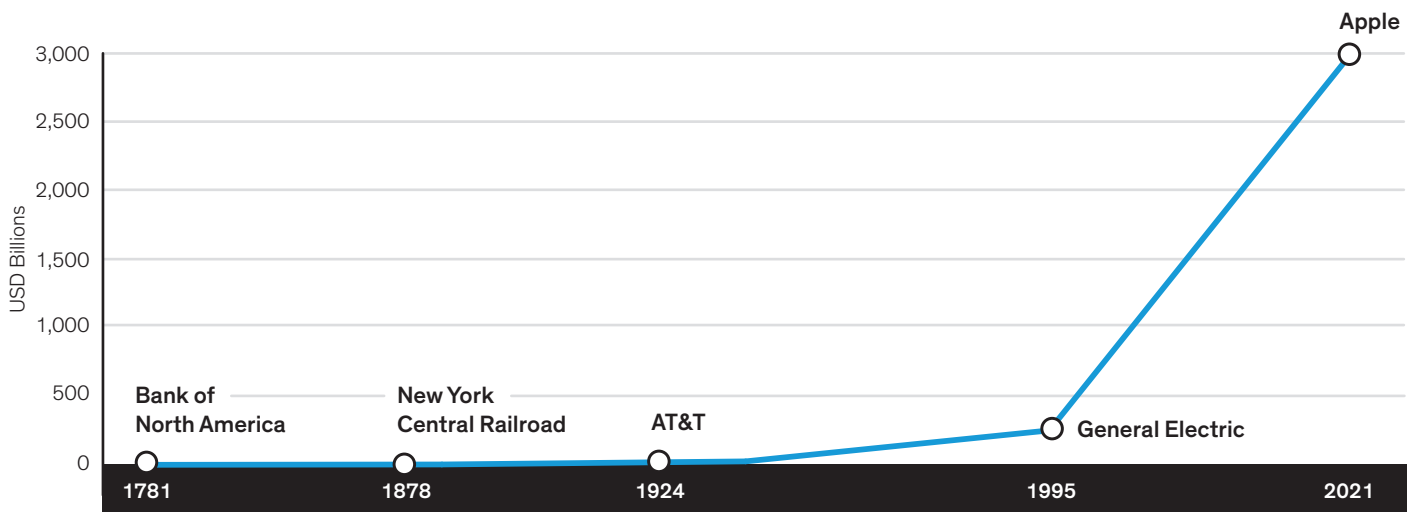
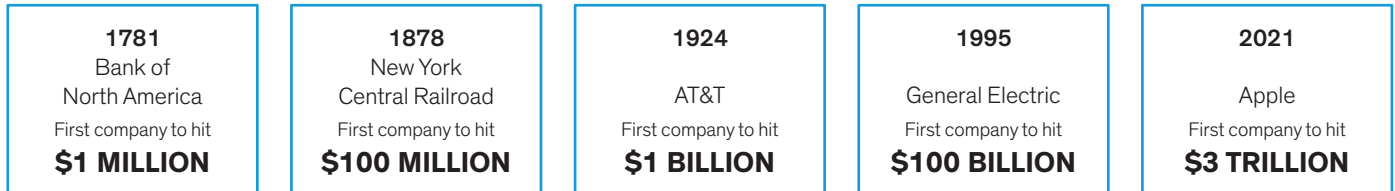
In a similar way to the linear movement of two objects or when comparing the physical size of two objects, the brain's natural style of orienting up and down influences how to represent quantities in visuals. In the natural world, going up is harder to sustain than going down: gravity is a one-way force. Making things hotter or colder than the ambient temperature is also a notable event: touching a burning log and falling into icy water are very important pieces of information.

As a result, the brain tends to find it easier to understand relationships that use up/down comparisons over those that use side-by-side

orientations. When it comes to PowerPoint graphics or even printed illustrations, orient quantities on scales that use vertical rather than horizontal orientation, like a thermometer with its gradients moving upward toward higher temperatures.

In some presentations, a visual may fit the slide or the page better if you orient the bars horizontally around a central tendency. The viewer will be able to make sense of this display, but it will require much more effort to sort out and understand the information than if it were oriented vertically.

STRATEGY FOR PRESENTING NUMBERS



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Avoid Visuals That Require the Brain to Interpret Words or Numbers

In our modern world, we have gotten used to a variety of images that don't reflect structures in the physical realm. Our daily diet of print media, television, movie and internet displays provides a vast variety of graphic images that serve different functions. As a result, we've lost our natural sense of how the brain processes information.

For example, in the display above, look at the square showing the value of \$1 million for the Bank of North America in 1781. This is followed by more squares showing the growth of what a big company is worth, culminating in Apple being valued at \$3 trillion in 2021. The viewer certainly knows the difference between \$1 million and \$3 trillion: the second value is a lot bigger than the first.

However, for a person to truly understand how big Apple is as a company, his brain needs to have a better sense of the difference

between the two numbers: How much bigger is Apple than the Bank of North America? In the display, the boxes that contain the numbers and words are all the same size; the only difference is in the symbolic value of the number in the display. In contrast, the timeline is a more effective way to show the magnitude of the difference.

For the client to truly get the difference in magnitude, you should show images the brain can recognize in terms of scale. For instance, instinctively we know that a thimble is in a different class of size from a house. Because there's no easy way to compare the sizes of these two extremely different values, it's hard to communicate the comparison visually and, for the purposes of your story, to find the graphic that best describes the scale in a visual way. The closer you can stay to making physical comparisons that reflect the way the brain instinctively processes information, the more powerful—and persuasive—your message will be.

Conclusion

It seems a bit ironic that as the financial-services industry goes through a new round of disruptions, the importance of the ancient art of storytelling is taking on a new level of significance. Even though changes are impacting every area of an advisor's practice, it remains true that the human central nervous system hasn't changed in any measurable way in more than 50,000 years. The way the brain learns, how it strives to predict the future and how it responds to negative information more forcefully than positive energy have been part of the

human experience since before we built our civilizations. In the same way, our modern conventions of television programs and movie scripts retain much the same structure and flow that the ancient Greeks used in their plays and epic stories. This is because the more things around us change, the more it's clear that we're operating with the same strengths and limitations that evolved over tens of thousands of years. The prudent advisor understands these patterns and takes advantage of a well-structured and clearly illustrated story to bring her advice and ideas to life for her clients.

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