Ensure fiduciary duty

Retirement Years

By David Mayes

FIDUCIARY duty basically means that an agent is meant to act in the best interest of his client, and not his own. It is a very simple concept, yet not surprisingly the real world all too often does not work this way.

When it comes down to it, human beings very often fall victim to greed. If I told most people how many times I have been blatantly lied to by fund managers and their promoters, most people would stay away from the financial markets all together.

Unfortunately, they would then fall victim to inflation which may have a far worse impact on their long term financial well-being.

You would also have had to have spent the last decade in a vacuum to believe that a publicly traded company's financial statements aren't easily manipulated to hide an imminent bankruptcy. Do a quick search on Bear Stearns, Lehman Brothers or Enron if you need a refresher.

You don't need to despair though, as there are in fact ways to align a money manager's interests with those of yourself. This ensures fiduciary duty is followed without relying on the moral fiber of those entrusted with your money. Unfortunately, it doesn't eliminate human error, but sadly there are no guarantees in life. You could get hit by a bus tomorrow, especially if you venture out onto Phuket's roads. Diversification can help with this.

There have been many structures and regulations tried over the years and decades to try and solve what is called the principal agent problem. Unfortunately, attempting to regulate morality has never worked very well, but it has managed to make fraudsters get much more creative. The most common historical breach of fiduciary duty on Wall Street has been churning accounts, where brokers made per-trade commissions and thus overtraded at the clients' expense, to pad their own pockets. Fixed annual management charges as a percentage of an account's value, have reduced the practice of churning, but have opened the door for a separate problem.

Since the manager can continue to make money even if the client gets a negative return, many will make opposite calls for separate accounts since they are guaranteed to keep some happy clients. I think this practice is absolutely despicable, and the most famous cases of this involved investment letters.

LIMITED TRUST: There are ways to ensure your financial advisors act in your best interest. Photo: Dave Dugdale

Firms would fax out recommendations for highly volatile stocks to a large database with opposite recommendations (think of telling half to put their money on red and the other half on black at roulette), and since each time they would be right on 50%, eventually they would widdle their list of prospects down to a small amount of people but they would have an amazingly impressive 100% track record with these few. I remember my father getting these faxed to him all the time when I was growing up and him checking up on them, luckily we always seemed to be in the loser group and he never became a victim of the ploy.

Incentive fees attempt to fix this problem, since a manager who charges an incentive fee (usually 10-20% of profits) will earn a lot more by making you positive returns. This is great in theory and I generally only like to use funds where the manager earns an incentive fee and also for another reason. It proves that the manager believes in himself. If you believed you could make positive returns and were setting up a fund, would you not set it up in a way to earn yourself the most money? A fund manager who does not have an incentive fee in my opinion does not believe in his ability and will thus only take a fixed management fee.

Staying in touch with Facebook

Island Investor

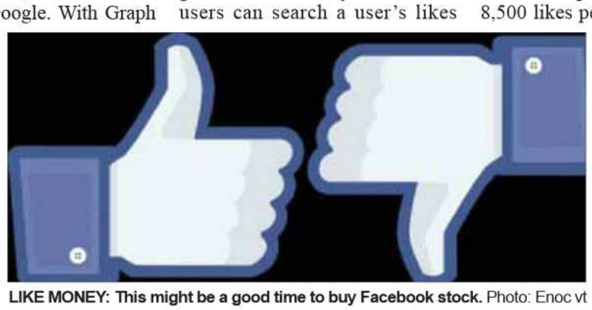
By Don Freeman

ONE of the main things I like about Facebook is that I can stay in touch with my family and friends all via one platform. Before I had to keep emailing, making phone calls and writing the occasional letter to and from the US. Now with Facebook, I don't have to do that anymore. I'm able to share my life here in Thailand and be able to see the events in the lives of those closest to me. All of this has led me to wonder if now is the time to buy Facebook stock since I use it every day.

Last year when the company went public, I had clients calling me asking if they should buy. I told them that I never buy stock on the IPO because there's too much risk. Boy was I right. The stock came public at US$38, popped to $45 and then started a gradual decline to a low of $17.55. The stock is currently trading around $26 and my investment radar is on high alert.

Facebook has the largest database of user's personal data in the world. Users have shared with Facebook data that no other site has. How many sites have the user's birthday, employment, likes, employment and education? The company is an aggregator of user information. The question that has been on investor minds is how can the company capitalize on all that information and justify a huge market cap.

To capitalize on all this information, the company has launched Graph Search, Facebook's challenge to Google. With Graph Search, users can search and find anything that's been shared on the site within one's own network. You can find people, places, photos and the likes of your friends.



LIKE MONEY: This might be a good time to buy Facebook stock. Photo: Enoc vt

Facebook's strategy is have the user search Facebook before they turn to Google.

With Graph Search, businesses can pay to have their rankings higher than competitors the same way they do with Google search. Since the user's information is localized, businesses can target the user and provide the nearest location for the customer to purchase. In comparing the two companies, Google last year had $50 billion in revenues versus Facebook's $5bn. If Facebook can capture just 5% of Google's search business, revenue will increase by 50%.

One of the ways Facebook is seeking to monetize this data is through the use of the Facebook Gift Card. This is a potential game changer in the growing gift card industry. Facebook users can search a user's likes and then purchase a gift card tailored to their interests. This eliminates the hassle of figuring out what to get someone for their birthday or an occasion. So far the program is only available for the Olive Garden, Jamba Juice, Target and Sephora. Look for many more companies to join the program as Facebook grows the business.

One of the key acquisitions that Facebook has made is Instagram. Instagram has been a growth phenomenon. When Facebook purchased Instagram for $1bn, Instagram had 27 million users. Almost one year later, Instagram has over 100mn users. Instagram has 90mn active monthly users that upload 40mn photos per day. Users make more than 1000 comments per second and over 8,500 likes per second.

If you compare the growth of Instagram to that of Facebook, you'll find that Instagram is growing at a much faster rate than Facebook did.

It took Facebook four and a half years to reach 100mn users. Instagram reached this milestone in only two and a half years.

Making this feat even more impressive is the fact that the photo-sharing application is limited to iPhone and Android devices.

The immense popularity of Instagram is being led by teenagers. Teenagers are typically at the forefront of the latest and greatest. They were the first ones to get on Facebook and then their parents and grandparents followed.

Now they're spending more time on Instagram and their parents and grandparents are likely to follow as well.

Some of the smartest investors in the world have been recently buying Facebook stock. Among those buying are former Fidelity Magellan star manager, Jeffrey Vinik and billionaire Leon Cooperman. Last quarter the number of funds owning Facebook stock increased from 48 to 67. The buying interest in the stock by the big funds is a positive sign for long-term holders of Facebook stock.

I have been watching the stock since the company went public 10 months ago. The stock got a little ahead of itself when it hit $32 last month but now Facebook has consolidated nicely and technically looks very good. This pullback appears to be a good spot for long-term buyers to get in the stock.

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