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For Many Financial Advisers, Stocks Become a Hard Sell

By JONATHAN CHENG

WILMETTE, Ill.—Financial adviser Jeffrey Smith recently watched a once-confident client scrawl his fears across a legal pad during a discussion of stock investments: "Congressional stalemate," "unemployment," "European crisis," "corruption."

The client, retiree Nicholas Zerebny, later recalled how his thoughts strayed to Edvard Munch's "Scream" paintings. In the middle of the page, Mr. Zerebny drew a crude version of the iconic screaming face. "That's how I feel right now," he told Mr. Smith. For Mr. Smith and other U.S. financial advisers, that anguished cry—real and metaphoric—has become a familiar part of the job.

Peter Hoffman for The Wall Street Journal
Financial adviser Jeffrey Smith meets in his Wilmette, Ill., office last month with his client Nicholas Zerebny.

Since hitting a recession-driven low in March 2009, the Dow Jones Industrial Average has doubled in value. But many ordinary investors remain too fearful to join in the gains.

After two stock collapses in one decade—2000-2002 and 2007-2009—along with scandals, the rise of high-frequency trading and worries over Washington's ability to rein in debt, Americans are pulling out of the market. Individual investors yanked a net $900 billion from U.S. equity funds since January 2000, according to fund flow tracker EPFR Global. Stocks and stock mutual funds now make up 37.9% of the average U.S. household's financial assets, down from 50.5% during the height of the tech-stock boom in 2000, according to the U.S. Federal Reserve.

"Is it me or does it seem like a calamity could be just around the corner?" Mr. Zerebny asked during the meeting. "I accept that there are cycles in the market, but it's the trust in the system that concerns me."

Mr. Smith, a 47-year-old former bond trader with a trim runner's build, tries to be a rock of stability for his clients, especially those who seem one headline away from bolting the market. He pointed to a hanging chart, showing stock market performance since 1926. With a few bumps, the market's chartline sloped up over time, from bottom left to the top right.

Mr. Smith belongs to the National Association of Personal Financial Advisors, a group of about 2,100 advisers that has doubled in the past seven years as more and more individual investors seek professional guidance.

"Changes in the economy have been a tipping point for a larger number of consumers to reach out for help," said Nancy Hradsky, an executive at NAPFA, based in Arlington Heights, Ill.

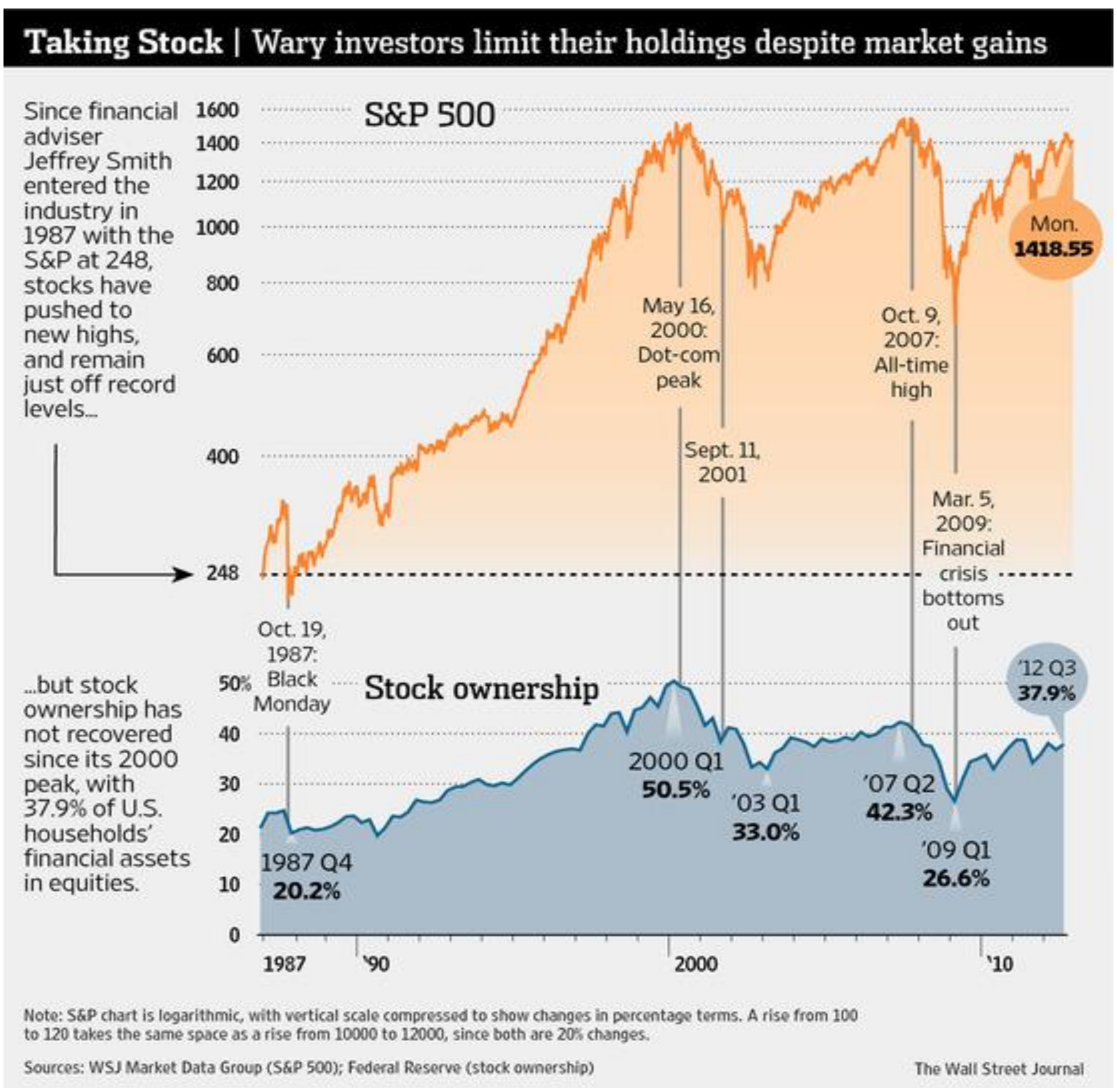
Mr. Smith and many of his peers don't take commission on transactions, but instead charge clients a fee to provide retirement and investment advice. Mr. Smith, for instance, charges an annual fee of 0.9% on the first million dollars of client assets.

In the late 1980s, Mr. Smith began his career trading bonds and stocks for a securities firm, before managing a portfolio for a not-for-profit group. For much of the 1990s, he recalled fondly, stock gains were taken for granted and the appetite for stocks among ordinary investors was insatiable.

Since starting his North Shore Investment Consulting LLC 11 years ago, Mr. Smith said, he has spent more of his time trying to keep his 140 clients in stocks. Most would like Mr. Smith to reduce their exposure to stocks without jeopardizing decent returns on their nest egg. But such safe alternatives as bonds or money market accounts offer only paltry returns.

"There's a fear and a phobia that's out there," he said. "Many investors haven't accepted that the financial crisis is in the rear view mirror. They think we're still living through the events of four years ago."

Mr. Smith usually fills his workdays with quarterly client meetings to discuss family finances and retirement goals. But he also keeps a close eye on the stock ticker. If stocks fall or rally for no clear reasons, he jumps on his computer to send a calming email to clients, trying to explain the market moves.



During a flare-up in Europe's debt crisis in June, he blasted emails from his hotel room in St. Kitts and Nevis during a vacation with his wife to celebrate their 20th anniversary. He returned to work the next week with the delicate task of soothing the nerves of a wealthy client family thinking of pulling out of stocks.

"I never expected that it would be this hands-on, with this frequency of interaction. But I understand why it's necessary," said Mr. Smith, a Chicago native and M.B.A. graduate of DePaul University, who dreamed of a life in finance while in high school.

A little more than half of Americans in a Gallup poll this spring said their households owned stocks, either individual shares, mutual funds or 401(k) retirement accounts. The proportion, 53%, is down from 65% in a 2007 poll and is the lowest since 1998, when Gallup began tracking stock ownership among U.S. households.

Many predicted Facebook's FB +0.50% initial public offering this year would lure back retail investors after a decade of retreat, triggered by the bursting of the technology stock bubble in 2000 and worsened during the financial crisis.

Instead, the Facebook IPO may have soured even more people after investment banks fed closely held information to favored clients and technical glitches marred the opening. Worse, many lost money.

For Mr. Smith, the IPO trouble didn't land close to home; it was a direct hit.

His wife, Darlene, an accountant by training, has long handled her own stock investments, separate from the couple's savings that Mr. Smith manages. Like many investors, she wanted a piece of Facebook's IPO and put in an order for shares at $38 on the open market the day Facebook went public.

Ms. Smith at first was told the transaction didn't go through. But over the weekend, she learned the trade, in fact, had cleared. She tried to sell the shares as the stock slid to $32. After many panicked calls and complaints to her online broker, she got her entire Facebook transaction canceled. Since then, Facebook lost as much of half its value before rebounding to close on Monday at $27.99 a share.

Ms. Smith has since vowed to stop picking stocks. "My individual stock days are over," Ms. Smith recalled telling her husband at the time.

"After all my concerns about high-frequency traders, Facebook was that final moment where I said, 'OK, if they can't get this right, with such a big IPO, then there are just too many things out there that can decimate my individual stocks,' " she said.

Around the time Mr. Zerebny sketched his "Scream" picture, Mr. Smith helped reduce Mr. Zerebny's stockholdings to a bit more than one-third of his savings from nearly 60%. The 63-year-old retired high school social worker now worries lower returns might stress his retirement. He collects a state pension from Illinois but fears government budget troubles could jeopardize his benefits.

"There's a duty on my part to make sure that my clients are properly invested for retirement, and that means holding stocks," Mr. Smith said. But with the market swings fraying investors' nerves, he said, he doesn't have the final word. "Ultimately, it's the client's money," he said.

Even some of Mr. Smith's clients who have stayed firmly in stocks are poised to pull out at the first sign of trouble.

Lawrence Zachary, a 59-year-old plastic and reconstructive surgeon at the University of Chicago, socks away money in mutual funds at Mr. Smith's urging. Between surgeries, he said, he consults his iPad a dozen times a day to check the stock market. Any sign of a big downturn, he said, would drive him out.

Lately, Dr. Zachary frets over Europe's debt woes and partisan rancor in Washington. When the market slips, he peppers Mr. Smith with emails, such as this recent missive: "I can't look, I'm getting sick, I'm in this rut, America is stuck."

Despite the stress, Dr. Zachary said, he must hang tough. "For ordinary Americans, the stock market is just about the only way to make money," he said. "You have to play."

Mr. Zerebny, who lives in nearby Deerfield, Ill., is "wise enough" to continue holding stocks but relies on Mr. Smith for reassurance, he said: "I want to be able to sleep at night."

Early in his career, Mr. Zerebny managed his own money. In the late 1990s, he bought tech stocks on the recommendation of a newspaper columnist.

"The article was saying, 'If you're not in on the tech ride, you're really missing out and you really should have half of your money in the market,' " Mr. Zerebny recalled. He called his stockbroker: "I told him, 'Get me in there.' "

His timing proved disastrous, coming near the peak of the tech stock bubble. "I rode that puppy down," he said. He returned to stocks and watched his portfolio swell during the rally that lasted from 2005 to 2007. "Those were good times," he said.

These days, Mr. Zerebny gets nervous even when the market goes up, fearful the rally will end. Just as surging home prices during the early part of the 2000s proved "too good to be true," he said, he is worried the stock market is being artificially buoyed more by Federal Reserve and government policies than sturdy economic growth.

In recent months, he has shared his concerns about dwindling natural resources and more-frequent droughts and hurricanes. In response, Mr. Smith helped him buy shares of agricultural and clean-water companies, not because he wants more stocks, but to protect him from a natural-resource calamity. In the event of a disaster, these stocks are likely to rise.

That move nudged Mr. Zerebny's total stockholdings to just under half his savings, up from their lows but still well below their highest level. He remains uncomfortable with the stock market.

"I react more on an emotional basis, and I'm very nervous," he said. "I remember the last time the Dow was in this range, housing prices were sky-high, we were all just sailing along and then, Bam!…The air's getting thinner, and I wonder, 'Can I trust this, or is this going to lead to another sharp reversal?' "

Mr. Smith again pointed to the historic stock chart hanging on the wall of his office.

"Volatility is going to be a companion on this entire ride," he said. "It hasn't been a great companion, but the long-term benefits of the equity market—we have to keep that in context in the face of the shorter-term noise."