



THE INVESTMENT FUNDS INSTITUTE OF CANADA

# THE VALUE OF ADVICE: REPORT

NOVEMBER 2011

**Featuring results from  
Ipsos Reid's 2011 research**

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## Preface

Canada has a competitive marketplace for financial services which provides Canadians broad access to savings and investment options for their individual needs and goals. Canadians can choose from a wide variety of financial products and services available from multiple suppliers.

There have been concerns that financial services in Canada are too costly. IFIC has conducted and commissioned research and produced several reports:

- Value of Advice Report, 2010;
- Understanding Management Expense Ratios, 2011; and
- Active and Passive Investing, 2011.

It is hoped that these reports will facilitate a fact-based discussion and will help to ensure that Canadians continue to benefit from a competitive financial services market.

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## 1. Introduction

The objective of the 2011 *Value of Advice Report* is to build on the Report released in 2010 with additional quantitative survey-based evidence, with a particular focus on the following areas: the causal link between receiving advice and wealth accumulation; the investment plan – how it pays off; and a more quantified look at the components of value that flow from the advisor-client relationship.

In 2010, The Investment Funds Institute of Canada (IFIC) published its first *Value of Advice Report*<sup>1</sup> which illustrated, using third party published data from Ipsos Reid, the strong and enduring values that financial advisors provide to their clients:

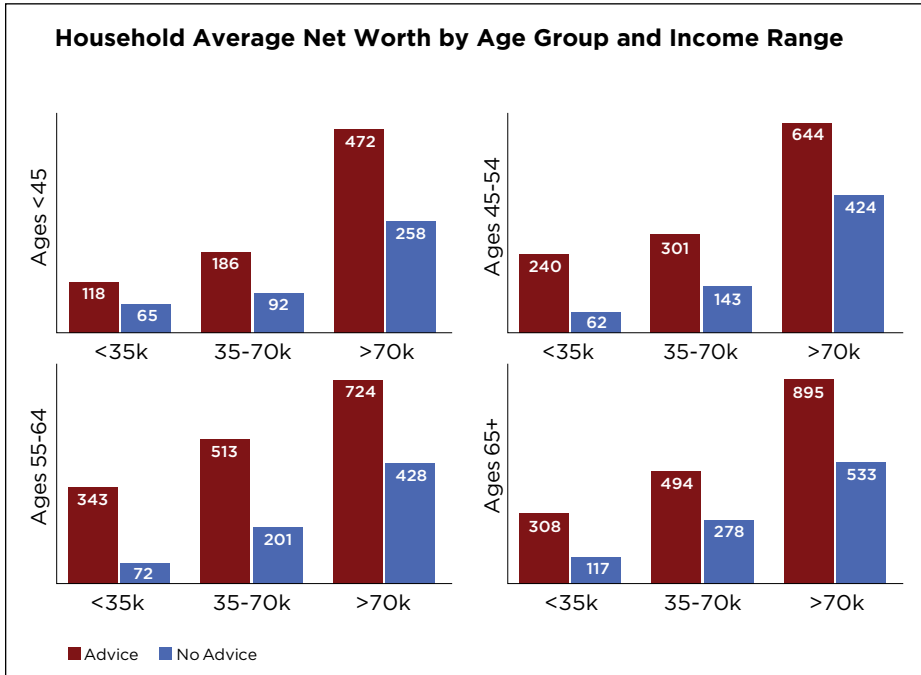
- Advisors provide durable values that benefit their clients throughout their investing lifetimes, such as the early adoption of a savings and investment culture, the avoidance of common behavioral investment errors, and the value of developing and following a financial plan.
- Advisors help individuals navigate through a wide array of financial products, vehicles and plans to arrive at solutions that fit their individual goals.
- Advisors help their clients build wealth through developing plans that are tax efficient and utilize the right asset mix for their circumstances and risk tolerance.
- Advisors contribute to the financial literacy of Canadians and have earned high levels of trust from their clients as sources of financial information for themselves and their children.
- Advisors operate in regulated channels which are proven to provide safety and soundness for the Canadian retail investor.

The 2011 *Value of Advice Report* highlights facts and research, which will help inform policy discussions about the costs of mutual funds and how and why Canadians access professional financial advice. The research will contribute positively to a better understanding of advice and its role in building wealth.

Featured in this study are new data released by Ipsos Reid in 2011 from its extensive *Canadian Financial Monitor* and *Canadians and Financial Advice* databases<sup>2</sup>. As highlighted previously, the new data confirm that, when controlling for age and income, the net worth of advised individuals is significantly greater than that of non-advised individuals (*Chart 1*).

“ Advisors provide durable values that benefit their clients throughout their investing lifetimes. ”

Chart 1



Source: Ipsos Reid Canadian Financial Monitor

## 2. Wealth or Advice – Which Comes First?

The research samples we have studied have consistently shown that investors who work with financial advisors (advised investors) have more wealth and investible assets on average than those who do not (non-advised investors). In the 2011 CFM database<sup>3</sup>, the sample of advised investors had an average net worth of \$555,447 in 2011 compared to \$191,743 for non-advised investors, nearly three times greater. In the same study, investible assets of advised investors were found to be four times greater than investible assets of non-advised investors.

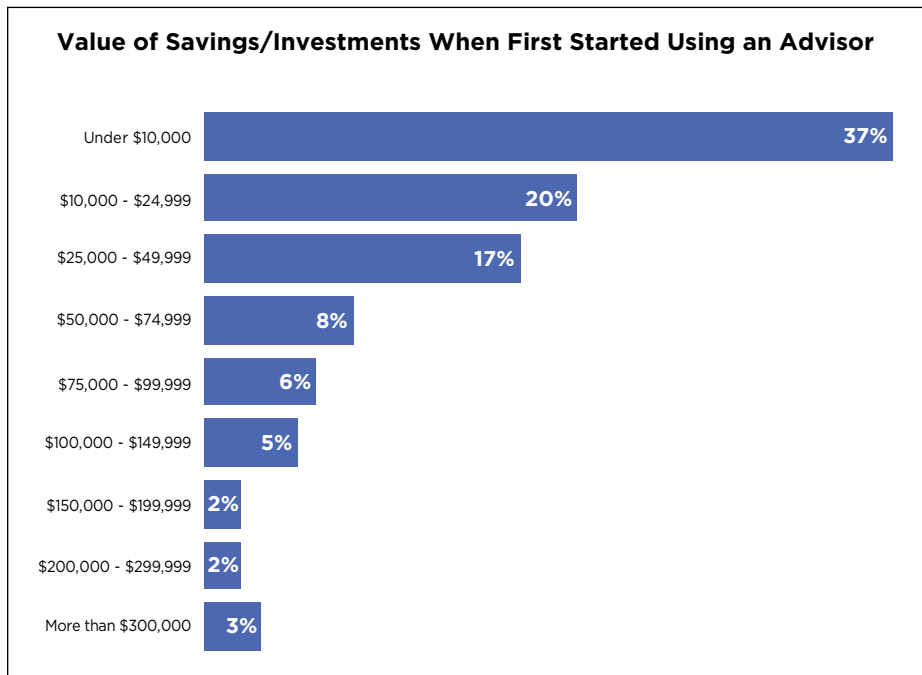
These large differentials were found to exist for net worth and investible assets across all age groups and income levels. This finding is independently corroborated by other studies, including the *Value of Financial Planning* study conducted by the Strategic Council for the Financial Standards Planning Council in 2010<sup>4</sup>, and in *The Future of Retirement: The Power of Planning*, published in 2011 by HSBC Insurance Holdings Limited, which concludes that “when controlling for age and income the advice advantage is still present”.<sup>5</sup>

However, some continue to pose the question: Are these investors wealthy because they have worked with advisors, or were they already wealthy before seeking out advice?

“ Investors who work with financial advisors (advised investors) have more wealth and investible assets, on average, than those who do not. ”

**In fact, research shows that most investors first begin to work with an advisor when they have only modest amounts of savings.** The 2011 Pollara Investors Survey<sup>6</sup> reports that 37% of mutual fund investors had less than \$10,000 in total household savings and investments excluding their primary residence when they first started using a financial advisor, and 57% had less than \$25,000.<sup>7</sup> (Chart 2)

Chart 2

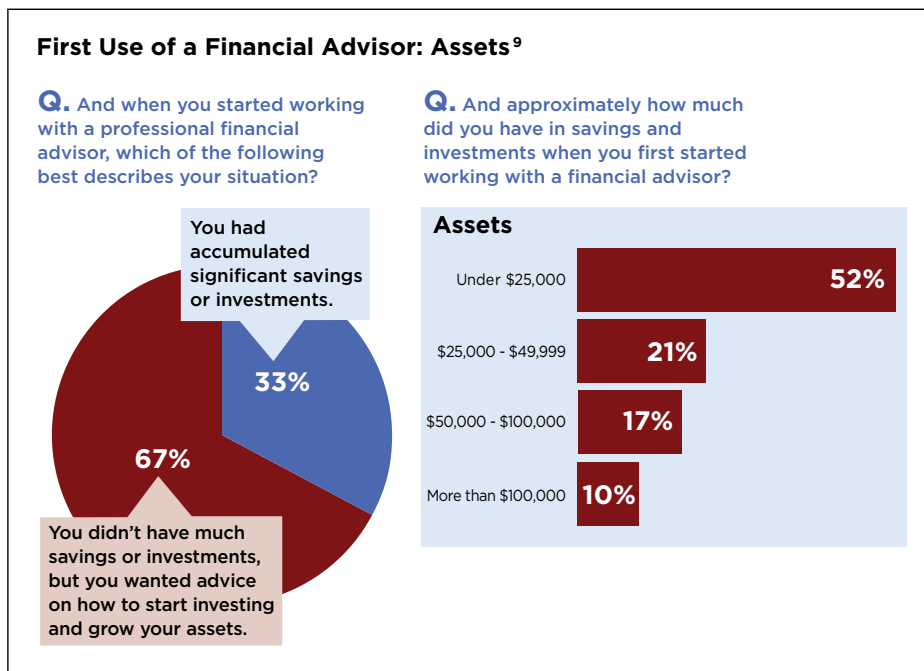


Source: Pollara Research 2011

In a completely different survey conducted by Ipsos Reid in 2011, the *Canadians and Financial Advice* (C&FA) study, Ipsos reports that 67% of advised investors with household assets of \$25,000 or more first consulted an advisor without much in savings or investments, but with a desire to start investing and to grow their assets. Similar to Pollara, Ipsos reports that most advised investors (52%) started working with an advisor with less than \$25,000, and 73% started with less than \$50,000.<sup>8</sup> (Chart 3)

“ 37% of mutual fund investors had less than \$10,000 in total household savings and investments excluding their primary residence when they first started using a financial advisor, and 57% had less than \$25,000. ”

Chart 3



Source: Ipsos, Canadians and Financial Advice

### Long term relationships between advisors and clients

One of the enduring values of the investor-advisor relationship is that it raises the financial literacy of the client through a continuing sequence of what the federal Task Force on Financial Literacy has termed “teachable moments”. In the words of the Task Force: “Those ‘teachable moments’ include decision points such as joining a pension plan or workplace retirement savings scheme, seeking financial advice or considering the purchase of a financial product, or determining one’s eligibility for benefits from a government program. Learners retain only some of what they are taught, particularly when the subject matter is outside their everyday experience. Thus, financial education needs to be reinforced through life.”<sup>10</sup>

The Pollara study shows that advisor relationships are long-lasting relationships that begin at an early age – i.e. when wealth is not well established for most people – and continue throughout life. Pollara (2011) shows that on average, investors under 35 first started using an advisor at just over 21 years of age and have been using an advisor for 8.4 years. Investors between 45 and 54 years of age first started using an advisor at just over 32 years of age and have been using an advisor for 17.1 years on average. (Table 1)

“ Advisor relationships are long-lasting relationships that begin at an early age – i.e. when wealth is not well established for most people – and continue throughout life. ”

Table 1

**Average Length of Advisor Relationship**

Age Group	Years Using Advisor (Average)
18 to 34	8.4
35 to 44	12.8
45 to 54	17.1
55 to 64	20.7
65 and older	23.0
All	18.0

Source: Pollara 2011

**3. The Investment Plan – How It Pays Off**

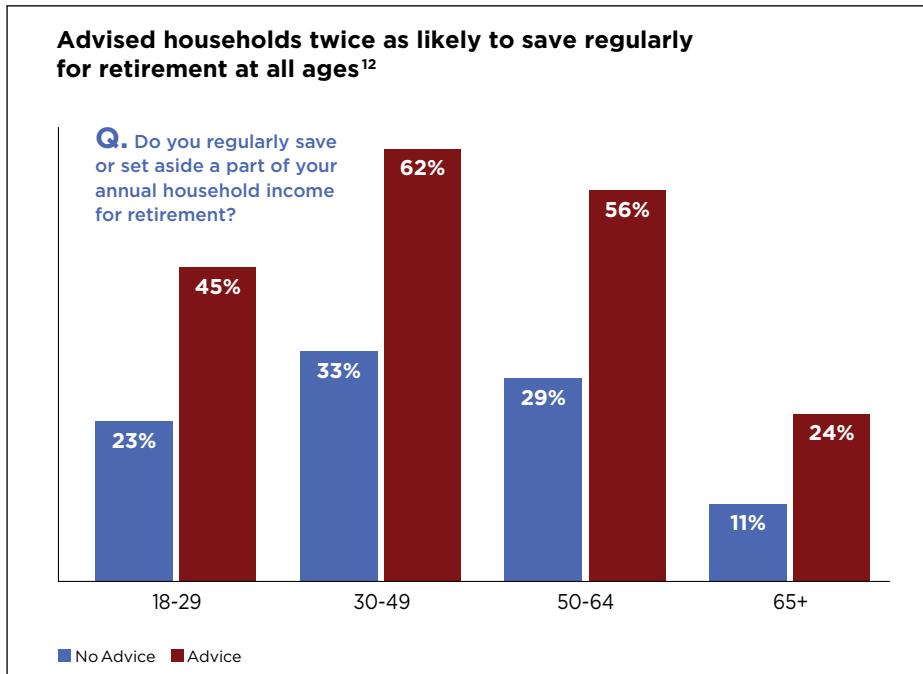
Great benefits arise from the discipline of developing and following a professional investment plan. Investors with a plan save more regularly and tend to avoid the common investment biases and errors that they would fall prey to if left to invest on their own.

According to results from HSBC's *The Future of Retirement: The Power of Planning*, 2011, those who have an advisor are more than twice as likely to have a financial plan<sup>11</sup>. Furthermore, “those who have a financial plan in place and seek professional financial advice are the best off financially. This group has the most retirement assets out of all our identified consumer types.” In fact, the group of individuals using an advisor for their financial planning had more than twice the retirement savings compared to those who did their own planning, and more than four times the savings compared to those who did not have a financial plan.

The regular reviews and updates of a financial plan by an investment professional serve as ongoing inducements to save. The Financial Standards Planning Council (FPSC) has published research that shows that advised households are twice as likely to save regularly for retirement across all age groups (*Chart 4*) and across all income levels (*Chart 5*).

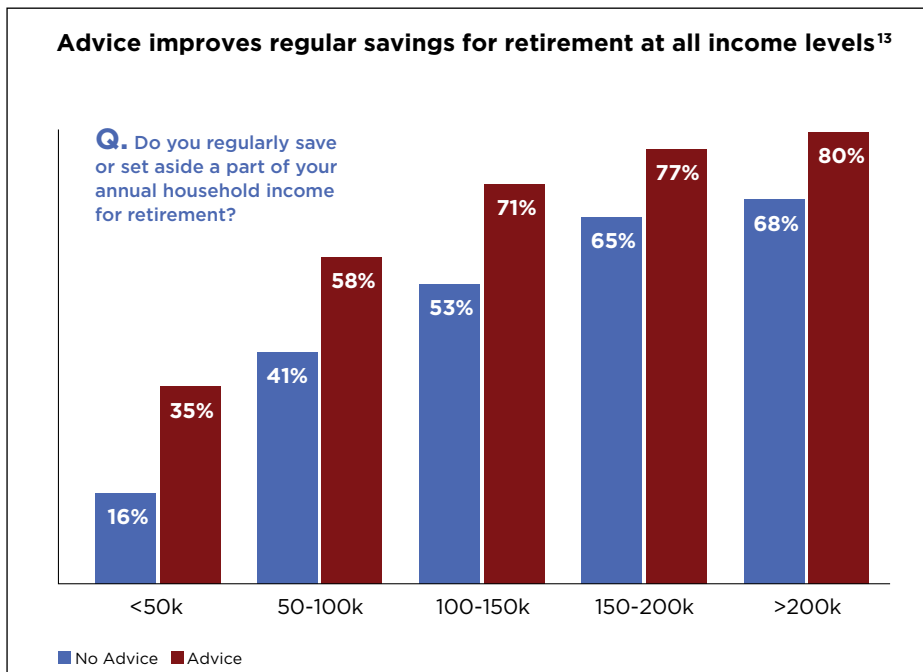
“ Investors with a plan save more regularly and tend to avoid the common investment biases and errors that they would fall prey to if left to invest on their own. ”

Chart 4



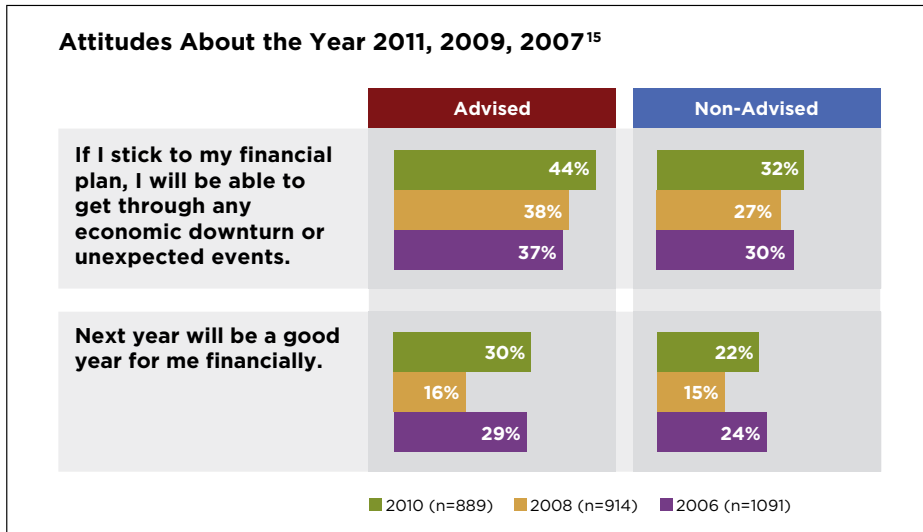
“ Advised households are twice as likely to save regularly for retirement at all ages. ”

Chart 5



A financial plan brings with it not only a more disciplined approach to savings, but also, once adopted, the greater confidence of investors in their financial affairs. The 2011 Ipsos Reid *Canadians and Financial Advice*<sup>14</sup> study (C&FA) reports that 44% of advised investors with \$25,000 or more strongly agree that if they stick to their financial plan, they will be able to get through any economic downturn or unexpected events. This represented an increase from 38% in 2008 despite the beginning that year of one of the most severe equity market corrections in recent memory. In contrast, only 32% of the non-advised group with \$25,000 or more believed in 2011 that their plan will get them through, following a dip in 2008 to 27%. (Chart 6)

Chart 6



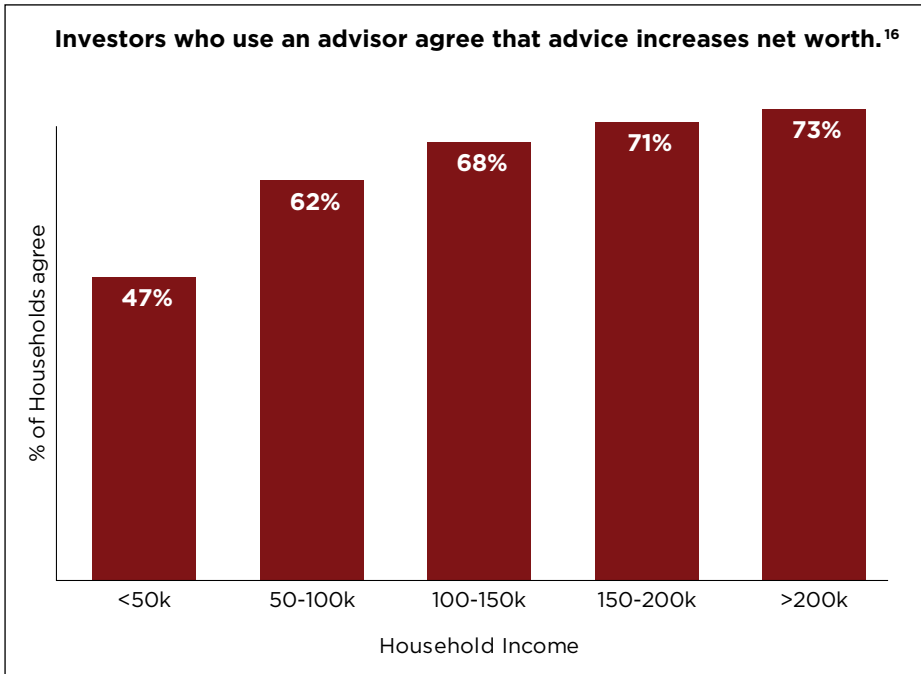
Source: Ipsos, Canadians and Financial Advice

It is also clear that planning has positive impacts on the value of investor portfolios over time. The 2011 C&FA data shows that the majority of advised investors believe that their advisor has had a positive impact on the value of their investments – 61% strongly agree that their advisor has helped them increase their net worth, and the same percentage (61%) strongly agree that their advisor has done a good job in helping them achieve investment returns.

“ A financial plan brings with it not only a more disciplined approach to savings, but also, once adopted, the greater confidence of investors in their financial affairs. ”

This finding also is confirmed by the 2010 FPSC research which shows that investors who use an advisor agree that advice increases net worth (*Chart 7*). In fact, the appreciation of the advisor although important at all income levels, is actually higher at higher income levels.

Chart 7



“ Investors who use an advisor agree that advice increases net worth. ”

#### 4. Investing Without Advice – the Pitfalls

While many Canadians want to work with a financial advisor, Canadians can choose to manage their own investments and save the costs associated with working with an advisor.

Do-it-yourself investors can also assess their own financial goals, develop and implement their own financial plan, select investment strategies and savings products to meet their objectives, monitor whether they are on track, and make adjustments as necessary.

There has been recent research about the behaviour and experience of these individuals. While some do-it-yourself investors have the ability to manage their own investments, some experience less than satisfactory outcomes.

### Making Non-rational Choices

In an August 2011 paper commissioned by l'Autorité des marchés financiers and the Ministry of Finance, Quebec, Cécile Carpentier and Jean-Marc Suret of CIRANO and the École de comptabilité, Université Laval shed some light on the experience of do-it-yourself investors<sup>17</sup>.

The results highlighted that many non-advised investors engaged in significant non-rational and biased investing behaviours. In particular, the authors show that individuals managing their own portfolios are overconfident when it comes to assessing their own ability to identify exceptional stocks. They also note that a large proportion of about 30% have a preference for stocks that have the characteristics of a “lottery ticket”, and a very large proportion show a bias of familiarity – when judging between an unknown large listed company, and a small listed company familiar to the investor, 58% indicated that the small listed company would be of equal or lesser risk as an investment.

### Inferior Investment Returns

In other recent research, U.S. firms Aon Hewitt and Financial Engines looked at eight large 401(k) plans representing more than 425,000 individual participants with \$25 billion in assets<sup>18</sup>. They compared the accounts of workers who received some form of financial help (Help Participants) with those who received no financial help (Non-help Participants) in the period from 2006 to 2010. When considering the difference in median returns across the different age groups, they found that Non-help Participants, on average, experienced returns nearly 3% (292 basis points) lower than Help Participants, **net of fees**. The performance difference ranged from 2.53% to 3.40% across the age groups.

The superior return for investors with financial help is attributed to the avoidance of common problems experienced by do-it-yourself investors, including: getting scared and pulling money out of stocks when the market tumbles; choosing an inappropriate level of risk for a worker's age and years to retirement; investing too much money in the employer's company stock; failure to periodically rebalance a portfolio; and complacency – the failure to do anything with the account for sometimes years at a time.

“ Non-advised investors engage in significant non-rational and biased investing behaviours. ”

## 5. What is the Role of Government?

Many Canadians choose to work with professional financial advisors. Our research shows these investors benefit from receiving advice. They save more, and feel more confident about retirement. In designing regulations, governments and policymakers should recognize the important role that advice plays in helping Canadians invest and save. Policies should be designed to make it easier for Canadians to access advice and use advice more effectively.

While a certain segment of the population has the expertise, time and dedication to manage their own investments, government policy should not, in general, encourage do-it-yourself investing or take measures that would limit the availability of advice.

Financial literacy initiatives should be designed to help investors understand when they should seek professional advice and how to work with an advisor. Carpentier and Suret (2011) suggest, for example, that there is a role for government in providing the tools to allow investors to measure their own knowledge about financial markets and investing.

## 6. Quantifying the Value of Advice

### Advisors add value by advising asset mixes that are right for the needs of their clients

It is generally accepted that it is prudent for individual investors to maintain long-term investment strategies that are based on the expected long-term relative yields of the major asset classes, as opposed to trying to time asset weightings to market movements. This is particularly true in times of volatility, such as we have been experiencing over the last few years.

While the right asset or product mix may be different for each investor, results show that on average advised investors have more growth-oriented asset mixes than non-advised investors. Ipsos (2011) reports that in 2011 advised households held 23% of their investible assets in chequing/savings accounts and GICs, 7% in bonds, 24% in stocks and 47% in mutual funds. The comparable percentages for non-advised investors were: 44% in chequing/savings accounts and GICs, 4% in bonds, 27% in stocks and 24% in mutual funds<sup>19</sup>. These results are broken down into the three asset classes of cash, fixed income, and equities for advised and non-advised investors in Table 2.

“ Government policy should not, in general, encourage do-it-yourself investing or take measures that would limit the availability of advice. ”

**Advisors add value by advising asset mixes that are right for the needs of their clients**

Table 2

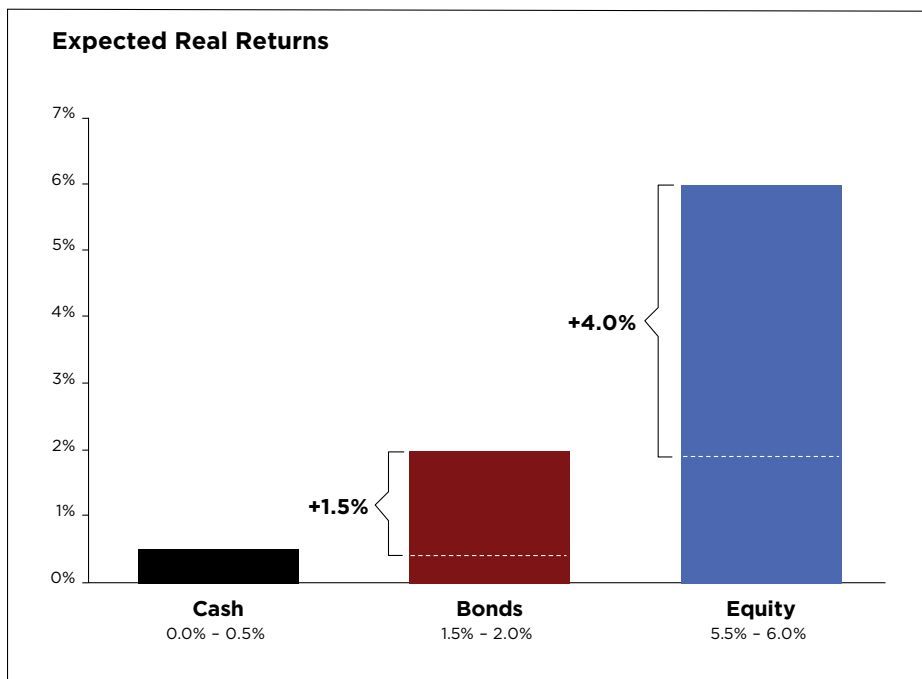
**Asset Allocation - % share of investible assets<sup>20</sup>**

Asset Class	Advised (%)	Non-Advised (%)
Cash	23	44
Fixed Income	24	13
Equities	54	42
Total	100	100

Source: Ipsos, IFIC 2011

What value does a higher equity exposure and a lower cash exposure have for a long-term investor? There has been much literature devoted to answering this question. One study, *Perspectives on the Equity Risk Premium* by Jeremy Siegel, published in the *Financial Analysts Journal*, assesses the real return risk premium for bonds at 1.5% and for equities at 4.0% respectively<sup>21</sup>. (Chart 8)

Chart 8



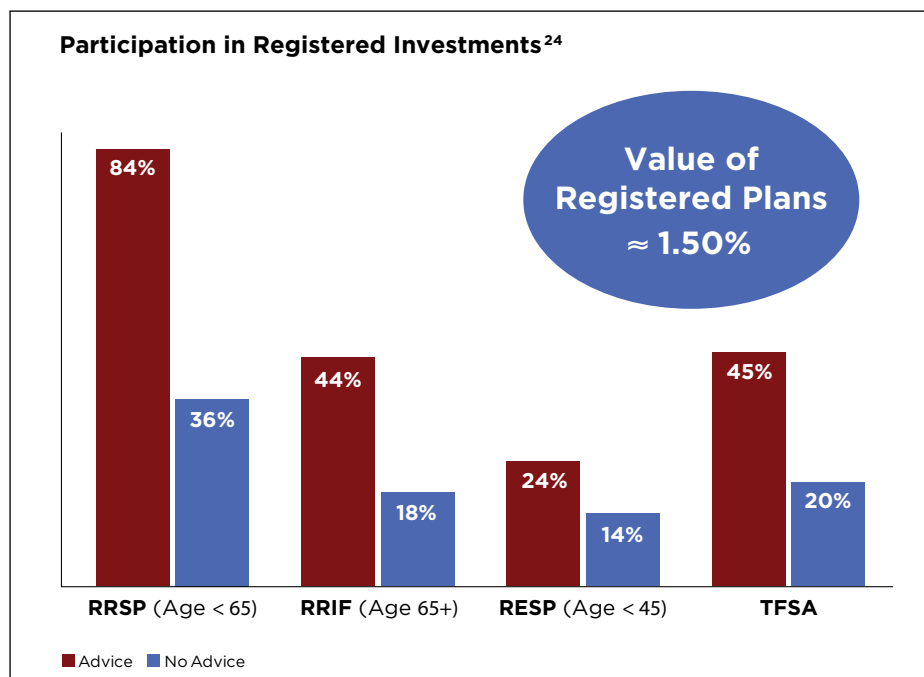
Based on the average asset mixes for advised and non-advised investors of Table 2, and the expected real returns of Chart 8, advised investors are calculated to have an expected net annual yield advantage of 0.83 percent over their non-advised counterparts due to this factor alone. Over time, with the larger balances generated in advised relative to non-advised accounts – four times larger according to Ipsos Reid’s CFM data<sup>22</sup> – advised investors will have increased capacity to increase their equity weightings, and thereby expected long-term returns, even further.

“ Advisors add value by advising asset mixes that are right for the needs of their clients. ”

### Advised households have higher participation in registered plans

Investors with advice are more likely to use tax efficient savings vehicles than investors without advice. The Ipsos Reid 2010 CFM study on Value of Advice reported that households with a financial advisor are twice as likely to be holding assets in registered plans as non-advised households. This result was re-confirmed in the 2011 Ipsos study which reports that in 2011, 84% of advised investors less than 65 years of age held RRSPs compared to only 36% of non-advised investors in the same age group. Similar results are found for other registered plans (*Chart 9*). Finance Canada estimates an after tax yield improvement of registered plans at approximately 1.5% – assets held in registered form earn 1.5% more after tax than the same assets in non-registered form.<sup>23</sup>

Chart 9



Sources: Ipsos 2011, Department of Finance, Canada

### Advisors add value by setting planning targets and adjusting targets

By setting planning targets, advisors influence better savings discipline over time, and help their clients avoid the costly investment biases and errors that non-advised investors are prone to. By adding the additional savings per year that arises from a more disciplined approach to savings, and compounding the positive yield advantages of advised portfolios over a lifetime, we can begin to understand why advice can produce significant improvements in financial health and retirement outcomes for individuals.

“ Investors with advice are more likely to use tax efficient savings vehicles than investors without advice. ”

## 7. Conclusions

The current study provides additional fact-based evidence on the value of advice. The objective was to further the 2010 Value of Advice Report by examining more closely the following topics: the causal link between having advice and wealth accumulation; the investment plan – how it pays off; and a more quantified look at the components of value that flow from the advisor-client relationship.

It is clear that the greater wealth and investible asset holdings of advised investors cannot be fully explained by the propensity of wealthy investors to seek out advice. In fact, research is presented from two independent studies which show that most investors first begin to work with an advisor when they have only modest amounts of savings, and advisor relationships are long-lasting relationships that begin at an early age when wealth is not well established for most people.

Research is presented which supports the value of an investment plan. Investors with investment plans tend to save more regularly and avoid the common investment biases and errors that they would fall prey to if left to invest on their own; and investment plans build the confidence of investors that they will be able to get through economic downturns or unexpected events.

One U.S. study looking at actual investment returns for 401-k plans over the period from 2006 to 2010 has shown a nearly 3% yield advantage for advised over non-advised accounts. These yield advantages when cumulated over a working lifetime produce substantially better retirement outcomes for advised relative to non-advised investors.

**Investing with advice yields higher returns than investing without advice because advisors provide asset mixes that are right for the long-term needs of their clients and encourage their participation in registered plans. When combined, these factors provide net return advantages that exceed the additional cost for advice that is contained within the mutual funds or other financial products used by the investor. This improved overall net yield applies to the four times greater investment balances shown to exist in advised relative non-advised accounts – largely a result of the joint setting of planning targets and the long-term view of investing that an investor gains through working with an advisor.**

“ Investing with advice yields higher returns than investing without advice because advisors provide asset mixes that are right for the long-term needs of their clients and encourage their participation in registered plans. ”

## Endnotes

- <sup>1</sup> IFIC, *Value of Advice Report*, 2010.
- <sup>2</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011. For the current study, Ipsos Reid constructed a static sample of individuals who responded in both the 2008 (12 months proceeding April 2008) and 2011 (12 months proceeding April 2011) CFM surveys. From this total sample of 3,568 respondents, Ipsos isolated sub-groups of investors who were: 1) advised in both years (N=1,047), 2) non-advised in both years (N=1,846), 3) transitioning to advice (N=296), and 4) transitioning away from advice (N=380). Groups 1 and 2 are referenced in this Report as the “Advised” and “Non-advised” groups respectively.
- <sup>3</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.
- <sup>4</sup> Financial Planning Standards Council, *The Value of Financial Planning*, May 2010.
- <sup>5</sup> HSBC Insurance Holdings Limited, *The Future of Retirement: The Power of Planning*, 2011.
- <sup>6</sup> Pollara, *Canadian Investors’ Perceptions of Mutual Funds and the Mutual Fund Industry*, 2011.
- <sup>7</sup> Pollara Research 2011. Q31: When you first started using a financial advisor, which of the following categories best represents the total value of your household’s savings and investments at that time, excluding your primary residence?
- <sup>8</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.
- <sup>9</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011. Q21c. And when you started working with a professional financial advisor, which of the following best describes your situation? Q21d. And approximately how much did you have in savings and investments when you first started working with a professional financial advisor? Base: Ever used a professional financial advisor (n=1370)
- <sup>10</sup> *Canadians and Their Money: Building a Brighter Financial Future*, Report of the Task Force on Financial Literacy, December 2010, p.7.
- <sup>11</sup> HSBC Insurance Holdings Limited, *The Future of Retirement: The Power of Planning*, 2011.
- <sup>12</sup> Financial Planning Standards Council, *The Value of Financial Planning*, May 2010. Q: Do you regularly save or set aside a part of your annual household income for any of the following: Retirement?
- <sup>13</sup> IBID.
- <sup>14</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.
- <sup>15</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.
- <sup>16</sup> Financial Planning Standards Council, *The Value of Financial Planning*, May 2010. Q: Indicate your level of agreement or disagreement with: Financial planning has helped me to increase my net worth. Top 4 of 9.
- <sup>17</sup> Cécile Carpentier et Jean-Marc Suret, *Connaissance financière et rationalité des investisseurs: une étude Canadienne*, CIRANO et École de comptabilité, Université Laval, 17 août 2011. The survey underlying their analysis, conducted by Vision Critical/Angus Reid in May and June 2011, was responded to by 1,814 investors with self-directed (non-advised) portfolios, roughly half from Ontario (901) and half from Quebec (913).
- <sup>18</sup> Aon Hewitt and Financial Engines, *Help in Defined Contribution Plans: 2006 Through 2010*, September 2011.
- <sup>19</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.
- <sup>20</sup> Numbers are derived from Ipsos Reid and IFIC. Ipsos Reid’s investible asset weightings in chequing/savings accounts and GICs, bonds, stocks and mutual funds provided on page 11 and described in *Value of Financial Advice*, prepared for IFIC, October 4, 2011, are modified as follows: weightings for mutual funds are divided into equities and fixed income according to IFIC estimates of 64% in equities and 36% in fixed income, and weightings for chequing savings accounts and GICs are allocated to cash.
- <sup>21</sup> Jeremy Siegel, *Perspectives on the Equity Risk Premium*, Financial Analysts Journal, 2005.
- <sup>22</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011. Advised households in the 12 months ending April 2011 held on average \$248,301 in investible assets compared to \$61,435 for non-advised households.
- <sup>23</sup> Department of Finance Canada, *Statistics on RPP/RRSP Participation and Savings*, March 31, 2010.
- <sup>24</sup> Ipsos Reid, *Value of Financial Advice*, prepared for IFIC, October 4, 2011.

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