

Valuable advice, or not?

Issue 71: August 2015

This issue explores financial advice, its perceived or potential value and what a person [seeking financial advice] perhaps should look for. The service level for example of any type of consultation rendered (lawyers, doctors etc.) is often difficult to quantify. How good, or of what quality, was the **service** rendered? Isn't it often based on an experience rather than a measured result? How do you measure a good outcome compared to the perceived value of a **product** (a tangible item), e.g. a smart phone, piece of art or antique furniture? Are we more prone to look at what it costs? As the saying goes: *"Nowadays we know the price of everything, and the value of nothing"*.

Merits of seeking independent advice

We laud anyone who makes the effort to get involved in their personal planning – it empowers you. What we would like to highlight, is an awareness of shortcomings by doing something without experienced input or professional counsel.

Most sportsmen and women have a coach – someone who helps them prepare physically and mentally in order to remain at the top of their game. Even the Springboks have many individuals (in addition to the coach and most recently unions) that help them prepare for each match – tactically and strategically. In a similar way we support our clients.

Several of our clients are savvy investors in their own right. Hence, we would rather see our role as that of a coach. These individuals are determined to get their financial affairs in order, but don't have the time, inclination or knowledge to do so. Our service is tailored to our clients' level of interaction, or needs. In simple terms, our responsibility is to make sure clients are continually on track and that the investment strategy ties in with their lifestyle goals. We regularly review these personalised financial plans – a process that is often underestimated, because legislation changes and markets move quickly. When the circumstances change, we need to adjust our approach and implementation.

Pitfalls we need to heed against:

- Underestimating risk. As a result, not enough attention is given to the likelihood of being wrong.
- Failure to pick a strategy and stick to it. Often the frequency of changes could be detrimental to the desired outcome, e.g. it is important to stay invested and not to try a time market movements.
- The lack of diversification. The future is unpredictable and the disproportional exposure to a given investment theme often means that an external (or unexpected) event may materially impact your portfolio.
- Over-confidence. Harvard research confirmed that as confidence increases, effective financial decision-making declines. Not surprisingly age is an important factor.

There is no question that investing your own money is becoming easier – thanks to the Internet, online platforms tout their low costs and ease of use. However, the important question is whether handling a portfolio and planning could make you more successful?

Is there a measure of value?

For many, the cost savings of not using an advisor may seem attractive. However, research by Morningstar in 2012 showed that using sound advice improves results.

The study found that investors, who worked with a qualified financial advisor, increased their retirement income by roughly 1.8% per annum (approximately 30% in total if compounded over your expected life). It may come as a surprise, but superior outcomes are often based upon good planning and decision-making rather than simply picking investments that outperform. Research also confirmed that the particular investments are generally less of a success factor, but rather the decisions [good or bad] we make. At Afrafin we identified tangible benefits within these key areas:

1. Goal formation. Experience showed that individual investors often struggle to establish appropriate, realistic and manageable goals.
2. Integrating other expertise: E.g. fiduciary services.
3. Effective asset allocation: When required, balancing volatility and reward, e.g. how much to invest offshore?
4. Designing a withdrawal strategy: Deciding when and how to take distributions from your portfolio.
5. Tax efficiency: Investing and withdrawing to minimize the tax impact on assets (your retirement versus discretionary funds).
6. Product and administration mix: Negotiating bulk fees on behalf of clients and "family groups" (husband, spouse plus trust); and using the optimal investment products with lower fee structures.
7. Goal-based investing: Investing to meet specific objectives within defined time frames (calculate the saving for a child's tuition).
8. Behavioural management. We are all prone to behavioural and cognitive biases that impede our progress and inhibit success. An advisor should mitigate these tendencies.

Using a planning process and implementing a sound strategy creates a tangible performance advantage. A financial plan with the right "coaching" elements supports clients to remain steadfast during volatile markets and ultimately protects you against self-defeating behaviour.

Are there any criteria to go by?

This is certainly not an exhaustive list, but consider:

- **Personal trust**: based on what? Look for substantiated credentials and regulatory compliance.
- Relevant **qualifications** with background and experience, e.g. is the particular person qualified as a CFP® (CERTIFIED FINANCIAL PLANNER)?
- **A process**: is there a clear planning and investment process?

Could we attach a "price tag", or value to advice? It may be a case of... *"Beauty is in the eye of the beholder"*. Ultimately, an advisor could, or should influence and encourage good investor behaviour (by the way, a significant success factor). Personal financial issues have become increasingly and unnecessarily complex. An effective advisor may help figure out what is true and what isn't, what works, what matters, what is useful, and what can, or could potentially go wrong.

In these financial volatile times (with Greece etc. in the headlines) I want to close with a quote from a famous American investor, Peter Lynch: *"Far more money has been lost by investors preparing for corrections or trying to anticipate corrections than has been lost in the corrections themselves"*. Stick to a solid plan and a diversified investment portfolio!