The Real Value of Advice

In the investment world, where results are measured in percentage terms, it is very easy to lose track of the real value of advice. Of all the participants in the 'investment value chain', historically it has been the financial adviser who has most keenly felt the pressure to reduce their fees. Being people centric at heart, quite often they oblige. As it turns out, quite unfairly, as we will explain below.

Consider the illustration showing investor returns:

Comparison	Return % per annum
Stock market (eg JSE, S&P, Dow Jones)	10.0%
Managed Equity Fund (a fund manager)	12.0%
Excess Investor Return (Difference between stock market and the Fund	2.0%
Less: fund manager fees (cost of accessing the fund)	*1.25%*
Net return received	**10.75%**

At a glance this shows the investor receiving a net 10.75% return from the fund manager for a fee of 1.25%. Seemingly a good deal.

Take then a financial advice fee of 0.75% p.a over and above the fund manager's fee, and we are back to square one: the stock market return of 10.00%. Many investors do this simple comparison and start to question the value of advice, with the fund manager receiving substantially more gratitude for the returns delivered.

The reality could not be more different. This comparison, while simple, illustrates how the value of advice can get lost in the numbers.

To start with, we have assumed above that the fictitious investor in this case knew exactly which investment strategy to invest in. In practice, we find this is rarely the case, and only in quite exceptional circumstances do home-grown investment plans reflect the investment objectives of the investor. The difference can be significant, for instance, a low risk compared to a high risk portfolio can mean a 20 year compounded difference of 72% in value, or an extra R4m return on a R1m investment! Unknowingly investing in the wrong strategy can have severe consequences. The role of the adviser in this case is to ensure you are invested in the correct strategy to suit your needs, and to maximise your ability to achieve your long term savings objectives. Very few fund managers can compete with that magnitude of value add: the ability to fit an individual's requirements to a specific investment plan.

A second example of the real value of advice is the ability to plan around tax, estate and other fiduciary needs. We recently came across a client example where the adviser had saved the investor 30% of their portfolio value through tax efficiency based on a single meeting. The 0.75% fee is starting to seem like good value.

A third source of real value is the behavioural management role of the adviser – that which protects investors from themselves. The so called 'behavioural gap' is well documented, essentially referring to the human bias we have to be greedy and fearful, which leads us into making investment mistakes: buying high and selling low. Numerous studies document this cost to the investor of between 1.5% and 4.0% per year. Through managing the investor's emotions, it is possible to add significant value merely by being disciplined around decision making.

The behaviour management responsibility extends to the general benefit of being disciplined and taking action, the fact that the investor is accountable to someone means that they tend to be more responsible with their financial affairs.

There are a number of other sources of value: the unquantifiable comfort of knowing a good adviser is looking after your interests; the fact they are shopping around for better costs; that they are keeping abreast of investment risks to best position your investment plan; that they are there for your family when you are not.

To put this back into numbers then: the real value of advice:

Adviser Role	Adviser Value Add %
Matching investors to the correct plan	Up to 7% or 8% per annum in returns
Managing the 'behaviour gap'	1.5% to 4% per annum
Tax, Fiduciary, Estate	Varies but can be up to your annual tax rate, ongoing and at death
Relationship value	Priceless

What the table above highlights is that financial planning is not operating in the investment value chain, but rather the personal financial value chain, which has significantly more moving parts, and significantly more opportunities to add value. In this context the real value of advice is clear to see, and can far outweigh the potential value add of a fund manager.

A word of caution though: not all advice is created equal. Advice is often dressed up in a product sales dress where the incentive is the management of your assets, rather than the advice on your assets. In this case, the many sources of value illustrated above are largely null and void. The correct phrase is therefore: "the real value of ***independent*** advice".

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REDFIN WEALTH

INVESTMENT AND FINANCIAL CLARITY

30 June 2017

data provided by Profile Data Analytics, Reuters and Datastream

		3m	YTD	1yr	3yr pa	5yr pa	10yr pa	5yr Vol[1]	10yr Vol[1]
LOCAL MARKET INDICES									
FTSE/JSE All Share Index (ALSI)	ZAR	-0.4%	3.4%	1.7%	3.4%	12.2%	9.3%	10.5%	15.1%
FTSE/JSE SA Listed Property	ZAR	0.9%	2.3%	2.8%	13.2%	13.8%	14.3%	14.1%	15.2%
SA All Bond Index (ALBI)	ZAR	1.5%	4.0%	7.9%	7.1%	6.6%	8.4%	7.8%	7.5%
SA Cash Index (SteFI)	ZAR	1.9%	3.7%	7.7%	6.9%	6.3%	7.3%	0.3%	0.6%
Balanced Benchmark [2]	ZAR	0.4%	3.5%	2.5%	6.4%	12.4%	10.2%	6.4%	6.4%
SA Inflation (1 month lag)	ZAR	1.0%	2.7%	5.5%	5.4%	5.7%	6.1%	1.4%	1.4%
GLOBAL MARKET INDICES									
Global Equity (MSCI World)	USD	3.4%	9.3%	15.9%	3.2%	9.2%	1.8%	10.0%	16.5%
Emerging Markets Equity (MSCI EM)	USD	6.3%	18.4%	23.7%	1.1%	4.0%	1.9%	14.4%	23.4%
Global Bonds (Barclays Global Bond Index)	USD	2.6%	4.4%	-2.2%	-0.4%	0.8%	3.7%	4.6%	5.9%
Global Cash	USD	0.3%	0.5%	0.8%	0.4%	0.3%	0.9%	0.1%	0.4%
MAJOR INDICES BASED TO RANDS									
FTSE/JSE All Share Index (ALSI)	ZAR	-0.4%	3.4%	1.7%	3.4%	12.2%	9.3%	10.5%	15.1%
Global Equity (MSCI World)	ZAR	1.7%	6.0%	5.7%	12.8%	22.4%	10.6%	13.3%	13.8%
Emerging Markets Equity (MSCI EM)	ZAR	3.8%	13.5%	10.7%	8.3%	14.2%	8.4%	12.0%	15.7%
SA All Bond Index (ALBI)	ZAR	1.5%	4.0%	7.9%	7.1%	6.6%	8.4%	7.8%	7.5%
Global Bonds (Barclays Global Bond Index)	ZAR	0.3%	0.0%	-12.5%	6.8%	10.7%	10.3%	11.7%	14.6%
COMMODITIES									
Gold (US Dollars)	USD	-0.2%	8.4%	-5.9%	-0.5%	-0.3%	-0.1%	10.5%	7.4%
Gold (Rands)	ZAR	-2.5%	4.1%	-15.9%	3.6%	2.1%	1.1%	10.8%	7.6%
CURRENCIES									
Rand / Dollar	ZAR	2.7%	5.2%	13.0%	-6.6%	-8.9%	-6.0%	13.0%	15.9%
Rand / GBP Pound	ZAR	-1.0%	5.0%	15.3%	2.3%	-5.4%	-1.8%	14.4%	15.5%
Rand / Euro	ZAR	-3.9%	-2.8%	9.6%	-0.8%	-7.0%	-4.4%	12.5%	13.6%
LOCAL UNIT TRUST SECTORS									
SA Equity - General	ZAR	-1.9%	0.6%	-0.9%	2.1%	9.6%	7.5%	9.0%	12.3%
SA Multi Asset - High Equity	ZAR	-0.2%	2.3%	1.5%	4.6%	9.7%	7.8%	6.0%	7.1%
SA Multi Asset - Low equity	ZAR	0.8%	2.9%	3.7%	5.9%	8.4%	7.8%	3.4%	3.6%
SA Real Estate - General	ZAR	0.6%	2.4%	2.7%	12.2%	12.9%	12.8%	12.3%	13.2%
Global Equity - General	USD	4.1%	10.4%	17.9%	3.1%	9.1%	1.5%	10.1%	16.3%
Global Multi Asset - High equity	USD	4.5%	8.4%	13.5%	2.5%	7.1%	2.9%	7.8%	12.4%
Global Real Estate - General	USD	4.2%	5.9%	-0.7%	1.3%	5.3%	0.5%	11.0%	21.4%

Spot Rates		3-Jul-17	Latest Quarter	1 Year Ago	5 Years Ago	10 Years Ago	20 Years Ago
CURRENCIES							
Rand/US$	Rand	13.2	13.1	14.6	8.2	7.1	4.5
Rand/GBP	Rand	17.1	17.0	19.7	12.8	14.2	7.5
Rand/EUR	Rand	15.0	14.9	16.3	10.4	9.5	NA
RATES							
Libor 6m $	US$	1.5	1.4	0.9	0.7	5.4	5.9
Repo Rate	Rand	7.0	7.0	7.0	5.5	9.5	NA
Prime	Rand	10.5	10.5	10.5	9.0	12.5	20.3
All Bond Index Yield	Rand	9.5	9.5	9.3	7.6	NA	NA
COMMODITIES							
Gold ($/oz)	US$	1,222.7	1,243.5	1,321.1	1,597.4	649.7	334.6
Platinum	US$	911.0	922.0	999.0	1,428.0	1,279.0	430.0
Oil (Brent Crude) $	US$	49.6	47.8	49.6	95.4	71.0	18.6
INFLATION							
SA Inflation	%	NA	6.2	6.3	5.5	5.8	9.4

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