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Is professional investment advice worth the fees?

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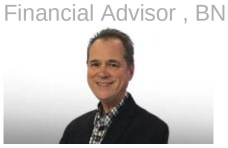

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Determining the value of professional investment advice is a catch-22. While professional guidance has proven to boost returns over time, the cost of paying for it also eats away at those returns over time.

The key is to get advice that boosts returns far in excess of the cost of that advice, and that's not easy when you try to navigate the maze of fees imposed by the Canadian investment industry.

Most Canadians investing for retirement wind up paying for advice whether they take it or not. Fees are baked into the most common investment vehicles – mutual funds – and crop up in various forms depending on the product, the vendor, or the relationship with a client. Despite numerous attempts at transparency the investment fee structure is as muddled as ever.

That tends to leave the average investor out in the cold and undermines the importance of professional management in an age when more Canadian retirement savings are exposed to the volatility of the broader market.

According to a 2015 study from the Montreal-based non-profit CIRANO Institute, investors who received professional advice were found to accumulate 3.9 times more assets after 15 years than comparable investors without advisors.

The most effective and common way of paying for investment advice is through a set percentage, charged annually based on the dollar value of assets invested. The advisor does well if the portfolio does well. Annual mutual fund fees could be as high as three per cent in Canada, which means the advice you receive from the advisor across the desk and the team managing the actual fund must generate an annual return of eight per cent to leave you with a five-per-cent gain.

When you factor in fees, it’s not hard to see why the average mutual fund underperforms the index it tracks, and why so many investors opt for passively-managed exchange-traded funds or robo-advisors, which charge much less.

But professional management is about more than returns. It’s about holding onto the wealth a client accumulates over time by managing risk as broader markets shift. A good advisor assesses a client’s risk tolerance and financial goals, and implements a comprehensive strategy to get them there over time. Good advisors have access to good research to find the best investments in the best sectors and geographic regions, and recommend selling them when they peak or as the client needs cash in retirement.

Good advisors also manage risk and boost returns by implementing tax saving strategies that effectively utilize registered accounts such as registered retirement savings plans (RRSP), tax-free savings accounts (TFSA), and, in some cases, non-registered investment accounts.

Good advisors also clarify how fees are generated and strive to keep them low. If their fees grow in dollar amounts as the portfolio grows, they have the opportunity to lower the percentage they charge. Wealthy clients often pay less than one per cent, which explains why the best advisors tend to focus on a few wealthy clients. There should come a time where any portfolio outgrows high-fee mutual funds in favour of direct investing.

Most important, good advisors deal with the human element. They keep their clients on track as markets fluctuate, and help them prepare and adjust to major changes in their lives such as the loss of a spouse.

Good advisors also require good clients. A recent Scotiabank investment poll found half of Canadians saving for retirement have not met with their advisors in the past 12 months.

Good clients do their homework, remain engaged, develop realistic expectations, and commit to saving.

Payback Time is a weekly column by personal finance columnist Dale Jackson about how to prepare your finances for retirement. Have a question you want answered? Email dalejackson.paybacktime@gmail.com.