

WHY USE AN ADVISOR?

STERKFORTEIN: I recently received an email from an irate reader wanting to know why anyone would use an advisor when making financial decisions. There are many who feel the same as he does however there are millions of people worldwide who make extensive use of advisors. He compared the financial industry with the medical profession and asked why advisors charge annual fees while doctors don't. In my view, there would be far more healthy people in the world if medical professionals started charging annual fees to keep us healthy.

THE QUESTION

Hi Warren

Can you please shed some light on my little puzzle?

When I go to the Doctor, he treats me and I pay him. When I go to the Dentist he treats me and I pay him. But if I went to a Financial Advisor, he gives me advice but then expects monthly payments. But for what?

Talking to a number of people on this subject, they are all complaining that they get once-off advice but are expected to pay the advisor an on-going monthly fee. This happened to me with my Financial Advisor (really an Estate Planner – very well-known in the industry). He was advising about where to invest my accumulated pension monies. I wanted to be in equities, he wanted me to place my funds in Stable and Balanced funds. Out of loyalty I continued paying him but I moved the funds myself to equities and caught a couple of years of the last major bull run.

My friend's father, many years ago acquired 3500 ABSA shares. An advisor offered to "look after them" for him. I suspect the advisor then "churned" these shares and, over time, the 3500 ABSA shares or their equivalent in money were no longer! I guess this one depends on the mandate you give to an advisor!

So I guess the question is "why don't advisors charge a once-off fee", same as the doctor or the dentist?

Kind regards

N

MY ANSWER

Hi N,

I think you are asking the wrong questions here.

Why are there so many obese, unhealthy people who do not exercise, stick to a healthy eating plan or take care of themselves? Is it because the health professionals involved only get paid when something is wrong and the patient comes to see them as a result? Proper healthcare is all about behaviour management, so people need to control their actions and manage themselves correctly to live their healthiest life.

If health professionals agreed a mandate with a patient where the health professional would assist the patient with a health plan and then helped the patient implement and stick to the plan, (in exchange for the monthly fee) don't you think there would be many more healthy people in the world?

Financial planning is no different, people CAN read up enough to manage their money and they CAN make the time and put in the effort to manage their investments. However, just as people don't spend time and effort on their health; many people also don't spend time and effort on their finances. There are so many sources of bad financial information telling us to do the wrong thing that many people become irrational. This results in bad decisions which are compounded by a lack of knowledge and experience in financial matters.

That is why there are so many people who are in a bad financial position and why there are so many obese, unhealthy people - behaviour management is very difficult for the majority of people. It is not difficult to find a healthy eating and exercise plan BUT it is very difficult to stick to it. Similarly it is not difficult to develop a budget BUT it is very tough to stick to it.

In essence, most people need someone to guide and cajole them to be the best they can be - that is why you pay a good advisor a monthly fee and that is why the medical profession is structurally flawed!

As a matter of interest, you CAN pay advisors a once-off fee. There are two ways to do this, either an upfront commission in exchange for a product or you can pay a good advisor for a proper financial plan that enables you to manage your own investments. However, just as in matters of health, it is very difficult to implement and then stick to the plan which is the most important part.

That is why annual fees are the right incentive and why transaction fees are wrong, advisors should be paid to keep you financially "healthy" over the long term.

Regards,
Warren

CONCLUSION

You can get a training plan to run the Comrades Marathon on the internet for free. You can even get a good eating plan and some good tips on how to start running; however this information will not automatically enable you to complete the Comrades. You have to spend hundreds of hours every month training, usually with a buddy or running group to make it. Managing your own investments is exactly the same, it is possible to do it yourself but unless you have the time and inclination to do so, you will not do a good job of it. That is where a good advisor can play a role because your advisor is your "training buddy" and is heavily invested in your success or failure. For most investors the decision to use an advisor could be the most critical financial decision they make.