

# VALUE OF AN ADVISOR

## ADVICE MATTERS.

According to a study done by Vanguard, using an advisor who utilizes wealth management best practices can add about 3% in net returns over time.<sup>1</sup>

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When we make big decisions in life, most of us look for a source of expertise and guidance to help us make thoughtful choices. That's what professional financial advice is all about. Several pillars of advisor created value can be quantified. **The following are 4 areas where a professional financial advisors can add value and help improve investment returns.**

### 1 BEHAVIORAL COACHING

*Most people act like humans, not investors. But when it comes to investing, acting like a human may actually cost you money.*

Today's modern advisor is now also a behavioral scientist and coach. Someone who helps their clients avoid bad decision making, weather market volatility, and stay on track with their financial plan. A strong behavioral coach understands an investors goals and fears and is able to help steer their financial behavior.

It's common for investors to become overly optimistic when markets are rising, or overly pessimistic when markets are declining. Left to their own devices, many investors buy high and sell low. An advisor can help an investor remain objective and disciplined through the cycle of market emotions. Avoiding behavioral mistakes is a significant contributor to the overall value of a financial advisor.

#### THE BASICS OF BEHAVIORAL FINANCE

##### FAMILIARITY BIAS

We prefer outcomes and patterns we have observed previously. Investors in the midst of a long bull market run may not feel a need to rebalance, as they have become familiar with the direction of the market and forget about corrections and consequences.

##### OVERCONFIDENCE

We tend to overestimate the accuracy of our predictions. For an investor this could mean believing their knowledge of an investment is greater than it actually is.

##### HERDING

The concept of herding refers to individual investors finding comfort in following the crowd, or "herd". This behavioral phenomenon can easily cause an investor to abandon their personal financial goals for fear of missing out on opportunity or making mistakes.

##### INFORMATION OVERLOAD

Well-rounded financial plans require an advisor's process and decision making, not cognitive "short cuts". Too many choices or too much information can actually cause an investor to withdraw, delay decision making, or take no necessary action at all towards achieving their goals.

#### VALUE OF BEHAVIORAL COACHING

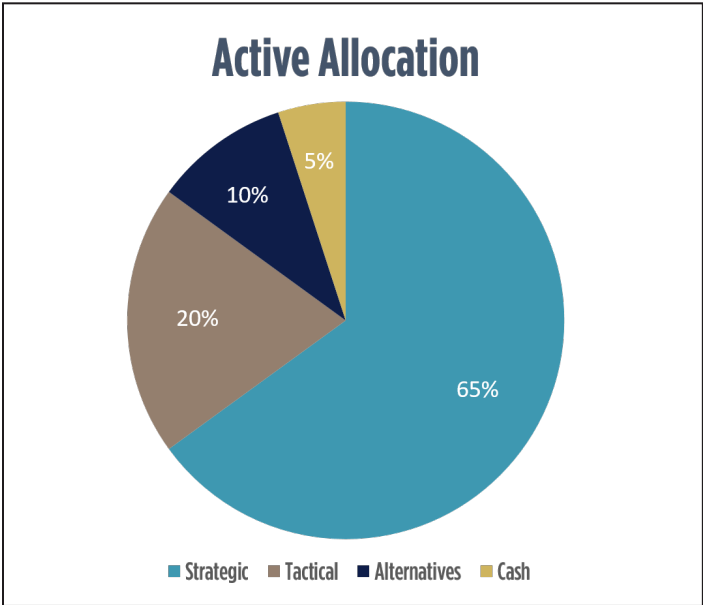
According to Vanguard's Advisor's Alpha®, behavioral coaching alone can add **1.5%** to net returns.<sup>1</sup>

<sup>1</sup>According to Vanguard's study based on their Alpha framework. Putting a value on your value: Quantifying Vanguard Advisor's Alpha, Vanguard Research, 2016.

## 2 ASSET ALLOCATION

Advisors are trained and licensed to do what is in their client’s best interest. A big part of this obligation is to really “know the investor”. Knowing an investor includes revealing the investor’s willingness and ability to tolerate risk. Advisors have a fiduciary responsibility to make sure their clients understand investment risks. This understanding allows advisors to use specific mandates and strategies to allocate client portfolios properly. Allocation models are managed professionally with close attention to many possible market variables. For example, asset allocations are no longer just a simple 60/40 split of fixed income and equities.

The modern advisor may now include asset allocation models with strategic and tactical styles holding underlying active and passive securities with several non-correlating asset classes for a truly diversified allocation.



For illustrative purposes only. Allocation will vary in each of our models.

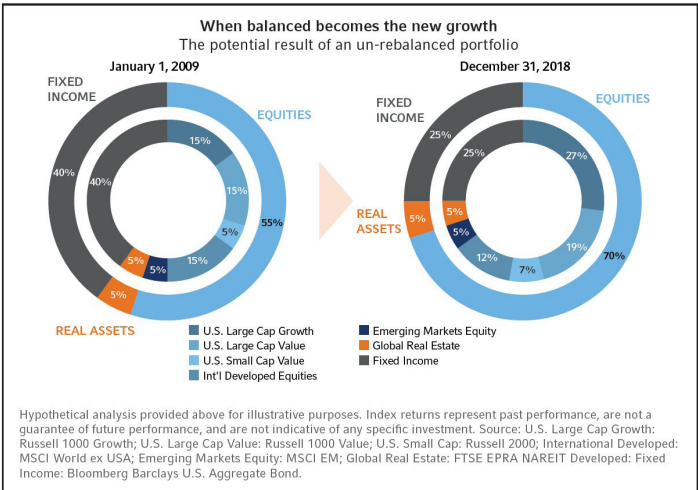
### VALUE OF ASSET ALLOCATION

A thoughtfully developed asset allocation that is both diversified and consistent with the client's risk profile and investment objectives can add **0.52%** of value annually.<sup>3</sup>

## 3 ACTIVE REBALANCING

Often when advisors recommend changes to client portfolios, the number one reason is rebalancing. Rebalancing a portfolio regularly can help an investor stay within a risk tolerance zone and prevent an overreaction to market movements, benefits that outweigh rebalancing costs.

Regular systematic rebalancing has the potential to generate higher returns when taking market momentum into account. Vanguard research estimates that annual systematic rebalancing can increase the expected portfolio return by up to 0.35% annually<sup>1</sup>, while Russell<sup>2</sup> and Investnet<sup>3</sup> estimate this annual return improvement to be 0.30% and 0.44%, respectively.



<sup>2</sup>According to Russell Investments annual study. Why Advisors Have Never Been So Valuable, 2017 Value of an Advisor Study.

### VALUE OF ACTIVE REBALANCING

Investnet reports the process of systematically rebalancing a diversified portfolio annually can add **0.30%** of value each year, compared with a naïve strategy of rebalancing once every three years.<sup>3</sup>

<sup>1</sup>According to Vanguard’s study based on their Alpha framework. Putting a value on your value: Quantifying Vanguard Advisor’s Alpha, Vanguard Research, 2016.

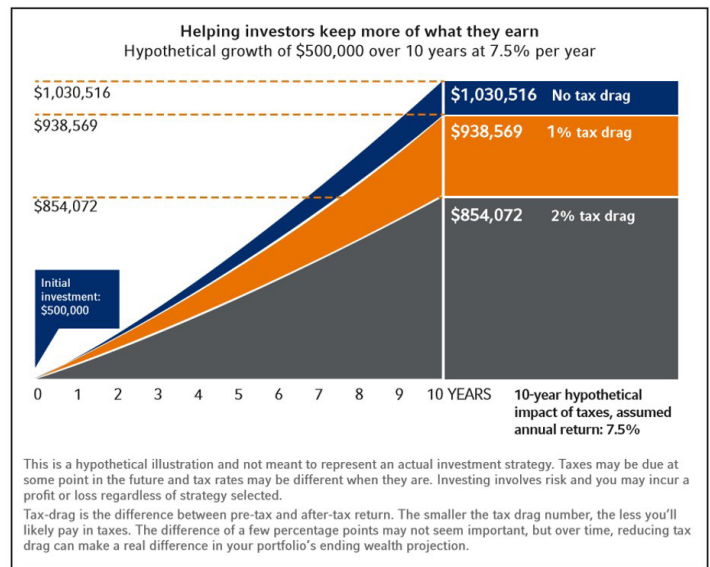
<sup>2</sup>According to Russell Investments annual study. Why Advisors Have Never Been So Valuable, 2017 Value of an Advisor Study.

<sup>3</sup>According to the Investnet/PMC research brief, Capital Sigma: the Sources of Advisor-Created Value, 2019.

## 4 TAX MANAGEMENT

When it comes to investing, it's not what you make that counts. It's what you get to keep. Advisors, working with accountants and attorneys, implement strategies for tax shelters, and smart withdrawal strategies.

Advisors know it's not just asset allocation that is important, but asset location is just as important. A good advisor will holistically manage all of your assets, placing less tax efficient investments into sheltered, or qualified accounts, and more tax efficient securities into taxable, or nonqualified accounts.



<sup>2</sup> According to Russell Investments annual study, Why Advisors Have Never Been So Valuable, 2017 Value of an Advisor Study.

### VALUE OF TAX MANAGEMENT

Investnet concludes that managing an all equity portfolio for tax optimization can add approximately **1.0%** of annual value when compared with an investment strategy that is not actively tax managed.<sup>3</sup>

## TOTAL VALUE QUANTIFIED

What is a relationship with a financial advisor worth to an investor? A 2019 Vanguard study estimates that an advisor adds about 3% of "advisor alpha" annually.

*A 2019 popular study estimates that an advisor can add about 3% in net returns over time if utilizing wealth management best practices.<sup>1</sup>*

The biggest opportunity to add value was found to be in behavioral coaching, which was estimated to be worth about 1.5% in additional return.

SOURCE	ANNUAL VALUE-ADD
BEHAVIORAL COACHING	1.5%
ASSET ALLOCATION	0.52%
ACTIVE REBALANCING	0.30%
TAX MANAGEMENT	1.0%
<b>TOTAL</b>	<b>3.32%</b>

Source: Investnet<sup>2</sup>; Morningstar; Vanguard

AROUND <sup>1</sup>  
**3%**

Keep in mind, the estimated 3.32% doesn't even account for the fact that many investments cannot be bought by the general public. Many investments must be bought and managed by a properly licensed advisor.

<sup>1</sup> According to Vanguard's study based on their Alpha framework. Putting a value on your value: Quantifying Vanguard Advisor's Alpha, Vanguard Research, 2016.

<sup>2</sup> According to Russell Investments annual study, Why Advisors Have Never Been So Valuable, 2017 Value of an Advisor Study.

<sup>3</sup> According to the Investnet/PMC research brief, Capital Sigma: the Sources of Advisor-Created Value, 2019.

Using an asset allocation methodology does not guarantee greater or more consistent returns, or against loss; it is risk management method. The market indexes discussed are unmanaged and generally considered representative of their respective markets. Individuals cannot directly invest in unmanaged indexes. Past performance does not guarantee future results. The return and principal value of investments will fluctuate as market conditions change. When sold, investments may be worth more or less than their original cost. No investment strategy can guarantee a profit or protect against loss. Independent Financial Group (IFG) does not give tax advice. IFG Registered Representatives (RR) do not give tax advice while acting as an RR. These matters should be discussed with your tax professional.

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Bring to Consultation:

- \_\_\_\_ Copies of Retirement Investment Statements
- \_\_\_\_ Pension & SS Income [SSA.GOV] Estimates
- \_\_\_\_ Estimated Monthly Retirement Income Needs