The 4 Criteria to Evaluate Financial Advice

Announcer: Welcome to the Empowered Investor Podcast. Have you ever felt overwhelmed by the sheer volume of choices and voices telling you how to plan or invest for your future? With this straightforward approach, host Keith Matthews of Tulett, Matthews & Associates cuts through the noise to help you create a winning action plan for you and your family. The decision-making framework discussed in this show can transform you and your investment experiences and will increase your odds of becoming financially secure. Learn more and subscribe today at TMA-invest.com.

Keith: Welcome to the Empowered Investor. My name is Keith Matthews and I'm joined by my co-host, Marcelo Taboada. Marcelo, how are you today?

Marcelo: Keith, as you can see, I'm smiling because I'm super excited about this show, first of all. I am beyond excited also that we're all back in the office and it's just an amazing feeling. I never thought I'd be so excited to have everybody here, but it's been a great two weeks.

Keith: Oh, you're right. You're absolutely right, Marcelo. So we have a combination of three and four-day-a-week sessions with most of the team members. Advisors are back in four days a week, with a day working from home, and operations and client service are in three days a week with two days working from home with some flex time around a variety of things. But it is absolutely incredible to have everybody back, and clients want to come back too, and individuals we meet in general, whether they're potential clients or we just had a conference. In fact, Marcelo, we had 11 leaders from international advisory firms come into the office last Friday from an association called Gaia, which is the Global Association of Independent Advisors.

Marcelo: That was amazing.

Keith: Yeah. And it ties into today's theme, which is the value of advice. One of the things that we picked up, of course, is that the issues that we deal with in the Canadian advisory channels are often very similar to those that individuals in the UK, New Zealand, Australia, or the States have to deal with.

Marcelo: Absolutely. Money is universal, right? So people have the same stresses about money everywhere.

Keith: Yeah, whether you're a client, investor, or an advisor. So in today's show, we're going to be really focusing on the concept of the value of financial advice. In particular, we're going to cover a few subject matters on that, starting with why individuals should gauge the value of any service provider, followed by historical ways in which investors have reviewed the value of advice. We'll discuss the evolution of advice, right? Most importantly, we're going to present a framework for our listeners and investors at large to review when they think about advice. So Marcelo, why this topic? Why this topic of trying to value advice?

Marcelo: It is a fair question because at the end of the day, Keith, we all use professionals, and we all at some point in our lives will have to hire somebody to help us with many different things, whether that's a dentist, a lawyer, or a financial advisor. So we have to have a way of gauging and sensing how value is important when we hire a professional. It is just part of life.

Keith: Absolutely. In our subject matter today, some of it is intangible. So how do you actually value that? What's your quote from Warren Buffett that you were talking about offline as we were preparing for today's show?

Marcelo: I love that quote because it goes like this. It says, "Price is what you pay. Value is what you get." I think that quote is amazing because it really represents that a lot of the times, yeah, you're paying for a service and you're getting in exchange something, but what is the actual value that you're getting out of that exchange of money for a service, right? So I think that's a question that we sometimes forget that, yeah, we're paying for a service, but what is the actual value that we're getting? What is it?

Keith: Yep. Absolutely. So today we're going to try to discuss and provide a framework around that. Why don't we start with historically? So here we are today, 2022. But how was advice gauged in the last 10, 15, 20 years, historically speaking, when you said, "Wow, I got good advice." What did people sometimes refer to?

Marcelo: I think there's three things really that come to mind. I think the first one would be the value associated with financial advisors in the past was always picking winning stocks, beating the market. Can this person help me pick the best stocks to beat the market overall? It's like you're getting that impression or that value or perception of value, I would say, because it's been proven it doesn't work, but we'll get into that later. Then you have picking winning managers. So, okay, you don't want to do stocks. Let's look at mutual funds. So the value that advisors would provide, quote-unquote, is they would be able to select which portfolio managers would do better and build you a portfolio with those winning managers. And then the third thing is timing the market, the value perception or the perception of value. There was that an advisor could help you get out of the market at the right time and get back in at the right time. And we also know that's been proven to be incorrect or at least the statistics don't show it.

Keith: Yeah. So you're referring to three general concepts that for many years, individuals would assume that financial advisors somehow had the inside track. They somehow had this ability to see the future and know where things were going. Of course, the industry positioned themselves as having that ability. So, of course, it's not the fault of the investor. This is what was being pushed and promoted, and this was a narrative that was being built. What I find fascinating now, and I would say in the last two decades, there's been this push. The data is showing, the evidence is showing that it is very hard for financial advisors to actually consistently add value in any one of those three categories. That's essentially how we've built our firm for the last 25 years. We call it evidence-based investing.

Marcelo: I know that's a mouthful and we can't get into the weeds here because we're just talking about something different, but we have the SPIVA reports. We have tons of reports that are research and statistically significant when it comes to looking at whether advisors could add value in those three things that we just discussed.

Keith: Hang on, Marcelo. You're talking about SPIVA. Remind the listeners, what is SPIVA?

Marcelo: Yeah. So it's a report that's put out by Standard & Poor's, which is the company that builds the S&P 500 index and the S&P TSX. They do this very extensive research about answering a very simple question: Do portfolio managers beat the market over long periods of time? They look at the U.S. market, they look at the Canadian market, international markets, emerging markets, small-cap funds, value funds, you name it. The evidence is clear that over long periods of time, a very large amount of mutual funds don't end up beating the market. So you're not getting what you're paying for.

Keith: And so it's the same with picking managers. Evidence shows that identifying winning managers, there's no science, it's very hard to do. Because you're a winner today. It doesn't mean you're a winner in three years from now. This was historically considered the value. You went to an advisor because he or she knew how to advance in one of these three areas. So what I would say, looking at the evolution of advice, I'd say in the last 10 or 15 years, advice has changed. It has become more holistic within the industry. I think that's an amazing thing for end investors.

Marcelo: A hundred percent.

Keith: You're seeing more planning. You're seeing people moving away from trying to beat the market. Exchange-traded funds have really been a revolution. Systematic investing strategies have added to this whole process. So advisors are offering perhaps more value because they're delivering a suite of services. So that's the good news. As we move forward in this conversation, we're now going to get into the nuts and bolts of what we think is the way to create a framework around the value of advice. Now, Marcelo, you, Ruben, Jackson, Lawrence, you went to a conference a few weeks ago, and you saw this framework, and we're going to discuss this framework because this is how we conduct ourselves. Talk a little bit about the conference you went to, and in particular, the session.

Marcelo: So we went to the Dimensional Fund Advisors Conference down in Austin, Texas. It was an amazing conference. We got to see the strategies, how they put them together, what type of research they're doing. They've mentioned over the years they've been really good at giving us better tools on how to communicate with clients because that's such a big part of our job, to communicate complex concepts in very simple terms that people can understand, right? People who are not in the industry. The conference was amazing, but they had this really interesting day at the end of the conference called the communications workshop. It's really just about giving us better tools on how to communicate difficult concepts, how to articulate our value, how to answer really tough questions that clients may have regarding certain issues in the market. One of the things that they talked about is this framework called the four C's, and it all stemmed from the basic questions that a client may have, such as, "I'm paying you a fee for a service. What am I getting out of it? What is the value that you provide? How do you make my life easier?" So they developed this framework called the four C's, which is what we're going to discuss today.

Keith: Yeah, it's an amazing framework because it's, we would suggest that all listeners look at this framework as a way of evaluating, "Am I getting value from the services that I receive?" All right, Marcelo, let's jump into this. Let's review the four C's together. The first C is competence. Tell us what that means exactly.

Marcelo: Sure. So competence basically means hiring an expert that can do the work. So in other words, making sure that the individual that you're hiring can actually do the work. In our world, that means doing the work on the investment front, doing the work on the planning front, doing the work on the tax front if you need that.

Keith: Exactly. Okay. So let's go into a little bit more detail here. In terms of the investment front, you would want to hire somebody who can do what exactly?

Marcelo: Yeah. You want somebody that invests for you, right? So that's going to put together a portfolio for you. Then you want the advisor to help you choose an asset allocation. Asset allocation is basically whether you put 50 percent in stocks and 50 percent in fixed income or bonds, or 60 percent in equities and 40 percent in bonds. So those discussions have to be had. The advisor has to help you decide what's the proper asset allocation for you. Then he has to help you rebalance that and maintain that allocation throughout the year.

Keith: I'd go as far as even at the forefront, the advisory firm has to make sure they present an investment philosophy, a process, and they have to be able to adhere to it. So that's part of being competent. The last thing you want to deal with is an advisory group that changes investment philosophies every three years.

Marcelo: Yeah. We had that whole episode on the importance of choosing an investment philosophy and why that's important, like the early episodes, but yeah, a hundred percent, that's crucial.

Keith: Okay. So you have to have an expert in the investing part. The next group is an expert in planning. What exactly does that mean?

Marcelo: Yeah. The financial planning aspect is you want somebody to help you do retirement projections that give you a better idea if you are on track to reach your goals and if your saving rates are okay. So for example, if a person comes in and says, "I have a million dollars, and they want to retire at 55 and spend 100,000 a year," then a discussion needs to be had. How do we help you get there? How much do you need to be saving every year? Are the saving rates you have appropriate? Maybe the person needs to be saving 25 percent of his gross income and is only saving 10 percent, and he thinks he's saving a lot, right? So without the proper analysis, you'll never know if you're on the right track. So that's the other thing that we do for clients.

Keith: I think competence in planning is more than just simply looking at a software projection system, plugging in a dozen or so numbers. There's a dialogue that has to occur with the client or the investor. The dialogue has to include questions that they haven't thought about their lifestyle, about things that might pop up that advisors see in other people's lives. It's important that the end client sees those questions and responds to them, and then there's a lot of nuances around that planning. That's part of the competence. Same for retirees in terms of drawdowns. Can they afford to have a certain spend rate? What's the sustainable spend rate? Part of competence. The last part would be tax and estate planning. You want to hire an expert that can help you either do tax returns or do estate planning. We've lumped them together. It's a fairly large area, but any final comments on that, Marcelo?

Marcelo: We do taxes in-house, but even if that advisor doesn't do taxes in-house, you still have to look at the big picture because if you're going to be planning around the portfolio and investing, there are tax consequences sometimes that need to be discussed. Even if the firm that you're working with doesn't do taxes, you still have to be able to understand what the impact is on the decisions you're making on a year-to-year basis on the portfolio.

Keith: Fair enough. It's great. So we've just covered off competence, which is the first C. The second C is coaching. What does that mean exactly?

Marcelo: Yeah. Coaching is basically the behavioral aspect, right? It's the, for lack of a better term, the hand-holding that goes around when you hire an advisor. The education process is teaching you what the philosophy is and why we're choosing it, educating the client on the different options on the portfolio and why certain things are chosen before others, right? For example, if you're choosing a certain asset allocation, you've got to be able to educate the client throughout and explain to him why. Then the biggest one is we have a lot of behavioral biases, and investing is extremely emotional. If you're dealing with a machine here at a robot, it's easier because you can set up the plan and just let it go, but we're human beings. It's been proven that the emotions associated with the market are tough, especially when we're in a down market and we're losing money. So that's where we come in, and we add that behavioral coaching and adding the guardrails to the client. The client may call and say, "Look, the market's going down. We should be doing something." That's where we come in and say, "This is what we should be doing based on evidence. Let's keep it cool and keep our calm here." That's the behavioral aspect that we add to the table.

Keith: Very well put. I'd also like to add a good coach has perspective.

Marcelo: Yes.

Keith: Perspective about historical moments, perspective about how things really do work. Investing is a tricky one because markets tend to be forward-thinking, and there's a disconnect between a market that's forward-thinking and how investors feel at large today. That needs to be coached. That needs to be discussed, and that's done through perspective. So coaching is a pretty big part of the value, and coaching can come in personal meetings. It can come in newsletters. It can come in a podcast. It can come in a variety of different mediums and ways.

Marcelo: One of the things that I'm most proud about with the clients that we work with, and this is also a result of the investment philosophy that we follow, right? We spend a ton of time on education when we onboard the client on the investment philosophy, how we invest, how we manage money through turbulent times. I have a lot of people ask me, "Oh, when I tell them I'm a financial advisor, this is what I do for a living." A lot of them ask me, "Do you have a lot of clients calling you or panicking when the market goes down?" My answer is always no, actually clients add money. Of course, you always have those discussions, "What does this mean for my portfolio?" But that's a different conversation than someone panicking when the market's going down. I think that's a result of proper education and behavioral coaching from the start. That's where you should set the bar.

Keith: You're absolutely right. If I look back in time, the vast majority of our clients have added money, if they can. Again, a retiree can't add money, so there's rebalancing going on, but the vast amount of accumulators are trying to add money during those downturns as opposed to taking money off the table. So that's the perspective part. So we've now covered off two of the four C's: competence and coaching. The third C is convenience. What does that mean exactly, Marcelo?

Marcelo: Yeah. Convenience can mean different things to different people, but I think we've identified a few here. The first one would be the time savings. You're delegating to your advisor and spending your free time doing the things that you love doing. Instead of worrying about your portfolio on Saturday morning, you can go out and play golf or go for brunch with your friends, just to give you very basic examples. Then you have a personalized service. It adds convenience to the person. So when you have a firm that adds a holistic approach, integrating the things that we talked about, the investment, the planning, the taxes, that adds convenience to your life because you have everything in one place, and every component of your plan is talking to each other. Then it's the service. When you need it, you have an unforeseen event in your life or something unexpected, you get an unexpected bonus, you change jobs, somebody dies in your family, these things. You have an advisor that's there for you with one call to help you deal with the situation. So in terms of time convenience, that's the things that an advisor could add value.

Keith: An advisory firm that does all of the things that you just mentioned will provide convenience for end investors, period. That's one of the C's. In our world, not only would we want to do these things, we also build a service and a portfolio service and a planning service that has elegance to it. It's simple. It's straightforward. It's clear to understand. That clarity, I feel, and have always felt, provides not only peace of mind, which we'll talk about a little bit later, but really does provide a convenient way for individuals to receive advice. So let's move forward, Marcelo. Let's go to the last C.

Marcelo: The last C is continuity. So that is the one where we add a framework there to encourage spouses to work together. Just like we discussed in the last podcast, a lot of divorces, I think one in four divorces in Canada named financial stress as their main culprit of a divorce or conflict. So we encourage spouses to work together, to unify, work under the same environment. We encourage family meetings with every member of the family to make sure everybody's on the same page as to how things are going to be managed. Then there's multi-generational planning, like you have a larger estate and you want to pass it down to your beneficiaries in a tax-efficient way. We're looking at that. So all that stuff adds to the continuity.

Keith: What I would also mention on continuity, and we've seen this before, is individuals might come in and say, "Listen, I've been working with our family's affairs for many years. I do it myself." But as things progress, I would like to include my spouse. They feel that when they do it on their own, it's harder to include their spouse. So they like the fact that a firm that embraces these spouse meetings together, they like that. They're like, "I want to get my spouse. I want to get my partner involved in our finances, just in case something happens to me." But also, as time evolves, that person might want to relinquish the responsibility of overseeing their overall finances. So continuity is huge. I would also add one other element. Continuity works both ways. If the client is being served by a firm, the firm offers support and additional members that know the client. That is continuity. So there's continuity in terms of should something ever happen to an advisor, because life gets in the way too. Should something ever happen to a team member, if you're working with a firm or a larger team, you have continuity, and that is a huge value add.

Marcelo: Yes, absolutely.

Keith: Marcelo, those are the four C's, right? You went to a conference, and you came back. We discussed this amongst our advisory meeting, our advisory group meeting three weeks ago, and we said, "This is brilliant. This really lays out a roadmap that we want to share with our clients. We want to share with listeners." So that's really what we tried to do today, share this framework.

Marcelo: Yeah, it's the gold standard, pretty much. If somebody asks, "How does an advisor add value?" Or we're dealing with a prospect, and they say, "Okay, I'm going to pay you this fee. How will you add value to my situation?" That's it. It's the four C's.

Keith: So I love the way you're confident in the process, as am I. Now, I'm going to ask you a question. What are the outcomes? We're going to talk about if a client can get these four C's and the value of advice, what are typically the outcomes that we've seen anyway for either our clients or investors at large?

Marcelo: There's a few, but of course, it's better results because you're following a structure, you'll have a plan that's well-crafted, you'll have better results because you're staying in your seat, and that's the behavioral aspect. If you have somebody who's jumping out of the market and coming back into the market or moving all these parts when markets are turbulent, then we have evidence that doesn't work. So that's number one: you get better results because you're following a plan and a structure. Two: you're getting better behavior, so you're getting better investment returns long term. Then you have more confidence and peace of mind because you know that you have a plan and things are well taken care of, and you can trust the person that's taking care of that. So I think that should be the outcome. A lot of people will say, "Oh, you guys are doing this show. It's self-serving because you are financial advisors." But I've said this before, I wouldn't do this if I didn't think this adds value to people's lives. I wouldn't dedicate my life to this if I didn't think this adds value to people's lives. So I think that's what the ideal outcome should be if you're dealing with the proper advisory firm.

Keith: A hundred percent. Marcelo, I couldn't agree with you more. I've always felt super confident that a process like the four C's, and that's how you evaluate advice. At the end of the day, investors will get two main things. They will get better results. They will get better results because of the plan, the commitment, the process, and the right behaviors: adding money when the market's down, better results with less stress. We've spoken about this in the book, The Empowered Investor, for the last 20 years. That is an incredible outcome. That is the winning outcome. Ultimately, what we're trying to do in today's episode is share this way of evaluating advice so that individuals, whether they're clients or not clients, are able to review their service provider, their advice provider, and say, "Am I getting good value?" So what are your takeaways? Let's wrap the show up with takeaways. I will say one thing, Marcelo. Our next show that we're going to do, we discussed, is going to be how to select a financial advisor, a whole series of steps, guidelines. So that will be the next show. It will be part of our two-part series about financial advice. What are our takeaways for today's show?

Marcelo: My takeaway is that it's your money. It's your future. The bar should be super high. This is the gold standard. If you're getting it, you're going to get those good results. But if you're not, it begs asking the question, "Am I getting the value for what I'm paying for?" So for me, it's don't be shy to ask questions. Make sure that you're being tough in the services that you demand, and make sure you're getting that value add for your money's worth.

Keith: Excellent. Thank you so much, Marcelo. I'll just add a short piece that says essentially today we presented a framework, a way to evaluate advice to all our listeners. Please use it. The four C's, please embrace it. Feel free to ask any questions you have. Thank you so much for tuning in, and we'll see you in the next episode.

Marcelo: Thank you.

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