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## NEW EVIDENCE ON THE VALUE OF FINANCIAL ADVICE

By Dr. Jon Cockerline, Ph.D.

A Guide to the Research Paper:  
“Econometric Models on the Value of Advice of a  
Financial Advisor” by the Center for Interuniversity  
Research and Analysis on Organizations



Center for Interuniversity Research and Analysis on Organizations

New Evidence on the Value of Financial Advice  
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## Is having a financial advisor really worth the cost?

Unfortunately, scientific literature on the topic has been scarce. The absence of confirming scientific evidence from a recognized academic source has allowed doubts to persist.

This has all changed with the recent release by the Center for Interuniversity Research and Analysis on Organizations (CIRANO) of the research paper “Econometric Models on the Value of Advice of a Financial Advisor” by researchers Professor Claude Montmarquette and Nathalie Viennot-Briot. The research paper uses econometric modelling and a robust sample of Canadian households to demonstrate convincingly that having a financial advisor contributes positively and significantly to the accumulation of financial wealth. It provides important insights on how the process of advised wealth accumulation actually works.

In particular, the research paper provides new evidence that:

1. Advice has a positive and significant impact on financial assets after factoring out the influence of close to 50 socio-economic, demographic and attitudinal variables that also affect individual financial assets;
2. The positive effect of advice on wealth accumulation cannot be explained by asset performance alone: the greater savings discipline acquired through advice plays an important role;
3. Advice positively impacts retirement readiness, even after factoring out the impact of a myriad of other variables; and
4. Having advice is an important contributor to levels of trust, satisfaction and confidence in financial advisors—a strong indicator of value.

The CIRANO research paper is written for experts with a deep understanding of econometric models, and it is complex. *New Evidence on the Value of Financial Advice* is a guide to understanding the research paper, including its methodology and findings, and highlights the important contributions of the research paper to our understanding of advice and how it benefits investors.

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**Is having a financial advisor really worth the cost? Not an easy question: the impact on an individual's assets from having a financial advisor relative to not having one is not directly observable, and the role of advice in wealth accumulation is not well understood.**

One place to look for an answer is in the substantial body of evidence that has been collected over the last two years by independent market research firms.<sup>1</sup> These studies demonstrate that financial advisors add value in a number of ways: by recommending asset mixes that are right for the needs of their clients; by advising on vehicles for optimization and tax efficiency; and by encouraging savings through programs and planning targets.

The first Canadian quantitative studies that demonstrate significant advantages for advised relative to non-advised households were released by the Investment Funds Institute of Canada (IFIC) in 2010 and 2011 using data from Ipsos Reid's Canadian Financial Monitor.<sup>2</sup>

The studies show dramatically higher investible assets and net worth of advised relative to non-advised individuals after accounting for age and income level. Average net worth for advised investors is nearly three to four times greater than that of non-advised investors, and wide differentials are observed across all age and income levels. These results are reinforced in separate research conducted by The Strategic Counsel for the Financial Standards Planning Counsel in 2010 and by Pollara Research for IFIC in 2011.<sup>3</sup>

These studies give rise to a number of questions: Are the conclusions reliable? Are there other variables besides age, income, and advice which might explain the wide differentials? Do the findings accurately reflect the impact of advice on wealth accumulation or are they impacted by other variables, such as potential bias arising from the prevalence of wealthy clients seeking advice?

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<sup>1</sup>Ipsos Reid, Value of Financial Advice, prepared for The Investment Funds Institute of Canada (IFIC), October 4, 2011; Pollara Research, Canadian Investors' Perceptions of Mutual Funds and the Mutual Funds Industry, 2011; Strategic Counsel for the Financial Planning Standards Council (FPSC), The Value of Financial Planning, May 2010.

<sup>2</sup>IFIC, *The Value of Advice: Report 2010 and The Value of Advice: Report 2011*.

<sup>3</sup>See footnote 1.

Unfortunately, scientific literature on the topic has been scarce. The absence of confirming scientific evidence from a recognized academic source has allowed doubts to persist.

This has all changed with the recent release by the Center for Interuniversity Research and Analysis on Organizations<sup>4</sup> (CIRANO) of the research paper “Econometric Models on the Value of Advice of a Financial Advisor” by researchers Professor Claude Montmarquette and Nathalie Viennot-Briot.

The research paper is the first academic study on this topic to apply scientific methods that address these questions directly.

The research paper uses econometric modelling<sup>5</sup> and a robust sample of Canadian households to demonstrate convincingly that having a financial advisor contributes positively and significantly to the accumulation of financial wealth. It provides important insights on how the process of advised wealth accumulation actually works.

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<sup>4</sup>CIRANO ([www.cirano.qc.ca](http://www.cirano.qc.ca)) brings together over 180 professor-researchers active in a variety of disciplines, including economics, finance, management, information systems, computer science and operational research, psychology, sociology, political science, law, history, and medicine. These researchers belong to eight Québec academic institutions and more than 10 institutions from other parts of Canada, the United States and Europe. More than 20 of them hold research chairs. Recognized internationally, these experts produce high-calibre scientific work and publish in leading international journals.

<sup>5</sup>Econometric modelling studies the statistical relationship between different variables, including causal relationships. It aims to isolate the impact of a specific variable when all others have been taken into account.

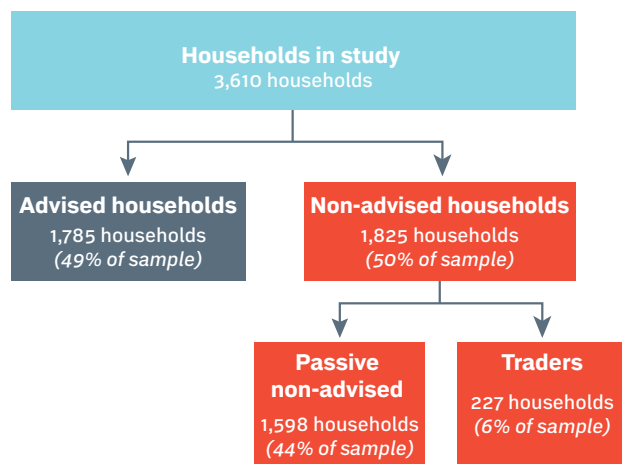
A significant feature of the research paper is the depth and quality of its underlying data—the largest and most extensive database yet developed in Canada for this purpose.

The initial research, conducted by Ipsos Reid in December 2010, consists of a 45-question internet survey, to which 18,333 Canadian households responded.<sup>6</sup> The initial sample has been reduced to 10,505 households through filters removing retired households, households with annual incomes greater than \$250,000 or less than \$10,000, households reporting above-average incomes and no financial assets, households with pension contribution rates above 30%, and those with savings rates greater than 90%.

In a follow-up survey of the same 10,505 households between June 24, 2011 and August 2, 2011, Ipsos Reid received 4,978 responses to a survey containing similar questions to the original survey plus new questions about the respondents' financial situation, investment behaviour and attitudes towards savings and advice. Filters were applied to remove households that responded inconsistently to the two surveys, misinterpreted investment questions, completed the survey in less than 10 minutes, had investments of less than \$1,000, expected to retire at an age less than 45 years, or had investment-to-income ratios greater than 50%. This produced a high-quality final sample of 3,610 households.

# 3,610

households in  
research study



CIRANO researchers, Professor Montmarquette and Ms. Viennot-Briot have now taken this research to a new level by applying scientific methods to analyze the data. Their first step was to segment the households into two groups: those who indicate that they have received financial advice (termed “**Advised**” in the research paper) and those who indicate that they have not received financial advice (termed “**Non-Advised**”).<sup>7</sup> The researchers then distinguish between two types of Non-Advised participants—those who do not receive advice because they consider themselves capable of managing their own investments (termed “**Traders**”)<sup>8</sup>, and the remainder (termed “**Passive Non-Advised**”). The study sample contains 1,785 **Advised** households (49% of the sample), 1,598 **Passive Non-Advised** households (44% of the sample) and 227 **Traders** (6% of the sample).

<sup>6</sup> Ipsos Reid was commissioned by Power Financial to conduct a broad survey about the use of financial services in December 2010. Professor Claude Montmarquette and Ms. Viennot-Briot designed a follow-up survey specifically targeted to studying the value of advice. The combined dataset has been provided to CIRANO to work with and publish.

<sup>7</sup> Households were classified as **Advised** or **Non-Advised** according to their response to the question: “Does anyone in your household currently deal with a financial advisor?”

<sup>8</sup> The **Traders** were **Non-Advised** respondents who agreed with the statements: “I do my own financial planning” and “I am capable of doing my own finances”.

In general, those in the Traders group are older with higher incomes, more education and a higher level of financial literacy than Passive Non-Advised households. Since they are a small group in numbers, large in assets, and motivated differently with regard to savings and attitudes toward advice than the other two groups, the researchers have studied them separately.

A second distinguishing feature of the research paper is to the richness of the data. A host of socio-economic, demographic and attitudinal information was collected on each of the respondents (as presented in the following chart) so that asset levels could be compared for households that were effectively identical in all respects except for their use of advice.

Demographic characteristics	Economic situation	Advice categories
<ul style="list-style-type: none"> <li>• Sex</li> <li>• Age</li> <li>• Post-secondary diploma</li> <li>• Financial literacy</li> <li>• Risk aversion</li> <li>• Preference for investing or receiving cash today</li> <li>• Number of income earners</li> <li>• Marital status</li> <li>• Region</li> </ul>	<ul style="list-style-type: none"> <li>• Household's annual income</li> <li>• Annual savings</li> <li>• Source of income</li> <li>• Employment sector</li> <li>• Minimum living needs at retirement</li> <li>• Willingness to save for retirement</li> </ul>	<ul style="list-style-type: none"> <li>• Level of financial assets required to seek advice</li> <li>• Tenure of advice</li> </ul>

**Table 1: A selection of the variables studied in the CIRANO Research paper**

With this rich database, the researchers were able to single out the effects of advice on asset accumulation after accounting for more than 50 other variables that also influence wealth accumulation.



This section reviews the findings in the research paper, beginning with the raw data and then outlining the analysis and conclusions drawn from the econometric analysis.

### 1. ADVICE HAS A POSITIVE AND SIGNIFICANT IMPACT ON WEALTH ACCUMULATION

Median and mean asset levels for Non-Advised households (including Passive Non-Advised and Traders) and Advised households are provided in Table 2. Consistent with previous research, analysis of the raw data shows us that those in the Advised group have significantly larger asset balances than the Non-Advised.

	Non-Advised <sup>9</sup>	Advised
Number of respondents	1,825	1,785
Median financial assets	\$24,000	\$101,000
Mean financial assets	\$93,384	\$193,772

Table 2: Financial assets held by Advised and Non-Advised Households

Chart 1 displays median asset levels for the Advised and Non-Advised groups. As the chart illustrates, Advised households have 4.2 times the median assets of Non-Advised households.



Chart 1: Financial assets held by Advised and Non-Advised households

<sup>9</sup>Includes all Non-Advised households, including Passive Non-Advised and Traders.

The large difference in assets that is observed may be the result of other variables besides advice. For example, it is easy to argue that a household's rate of asset accumulation could also depend on demographic, economic and other variables such as age, education, marital status, annual income, gender of the head of the household, the number of income earners in the household, savings rates, sources of income (whether salaried, pensioned, self-employed, full- or part-time), perceived living needs in retirement, preferences for consumption and investment, financial literacy and the region of Canada in which the household is located.

One way to separate out the effects of advice from these other potentially important variables is to incorporate all variables, including whether or not the household has advice, in a single regression model. The importance of each variable on the level of assets can then be determined statistically from the estimated coefficients.<sup>10</sup> In such an analysis, the influence of advice on assets is interpreted as the impact of advice *after correcting for all of the other variables*.

Unfortunately, when the variables in regression models are not truly independent, inferences drawn about the connections between variables can be incorrect. For example, imagine a two-way relationship between the variables of wealth and advice, which could look something like this: having a financial advisor contributes to the wealth of a household, while at the same time, a household's wealth may trigger the need for advice, or make the household more attractive as a prospective client. In such cases, advice is not truly an independent determinant of the level of wealth. This problem is addressed in the research paper by creating a new variable—*the probability of having a financial advisor*—for each of the respondents, and then using this as an “instrumental variable”<sup>11</sup> in an equation explaining the level of assets.

### **The probability of having a financial advisor**

The researchers find that the probability of having a financial advisor is affected primarily by income levels, the capacity of the household to save, and the age of the respondent. Respondents who declare that they will never save for retirement are less likely to have a financial advisor, and couples with no children are more likely to have a financial advisor.

**“The influence of advice on assets is interpreted as the impact of advice after correcting for all of the other variables.”**

<sup>10</sup> An “estimated coefficient” measures the variability in a data set. It provides a measure of how well future outcomes are likely to be predicted by the model.

<sup>11</sup> The “Instrumental Variable” technique is standard econometric practice for correcting for inconsistency of estimates caused by explanatory variables that are not independent.

An additional variable called the “Advice Threshold”<sup>12</sup> is also found to have a significant impact. Advised households report that they began working with a financial advisor when they had very modest levels of assets. (The median initial investment is \$11K.) Passive Non-Advised households report that they believe they would need higher balances: 44% of Passive Non-Advised believe they need assets of \$50K or more to engage an advisor, and 65% of Traders believe that they need \$100K or more.

Category	Respondents with the following characteristics were significantly more likely <sup>13</sup> to have a financial advisor
Advice threshold	Those who do not believe that a relatively high asset level is required to seek advice.
Income	Those with household income of \$90,000 or more.
Savings rate	Positive savings rate: those with higher savings are more likely to have an advisor.
Willingness to save for retirement	Those saving for retirement.
Household composition	Couple with no children.
Age	45-65

**Table 3: Lists variables that are key in explaining whether those studied have a financial advisor**

The probability that a given household has a financial advisor is used as an “Instrumental Variable” in explaining the level of financial assets.<sup>14</sup>

### The level of financial assets

The most important variables explaining the level of assets of Advised and Non-Advised households are shown in Table 4 on page 12. The presence of a financial advisor, when engaged for periods of four to six years, seven to 14 years, and 15 or more years, contributes positively and significantly to the level of assets when the impact of all other variables have been factored out. Moreover, the impact on the level of assets is more pronounced the longer the tenure of the advice relationship.

<sup>12</sup> The “Advice Threshold” is the actual level of assets that Advised Households had when they first started working with a financial advisor, and the level of assets that Passive Non-Advised Households and Traders perceive they would need to engage an advisor.

<sup>13</sup> These variables had estimated coefficients that are significant at the 99% level ( $p < 0.01$ ). For a detailed list of coefficients, see Appendix A.

<sup>14</sup> A similar analysis was applied to the sample of 1,825 Non-Advised and Trader respondents to predict the “Probability of Being a Trader”. Again, “Advice Threshold” is found to be a significant determinant of the “Probability of Being a Trader” – this time significantly positive. The higher the perceived level of assets needed to engage an advisor, the more likely the respondent is to be a Trader. These results, reported fully in the research paper, illustrate the different characteristics of the Trader group among the sample of Non-Advised respondents.

Many of the variables in the regression model have significant impacts on wealth accumulation. For example, significantly higher asset levels are found in households with income levels above \$35,000, ages over 45, those who are financially literate, males, and those residing in Alberta, Ontario, and British Columbia. Significantly lower asset levels are found in households with the intention of never saving for retirement, those that are risk averse, and those with two or more income earners.

Category	The following characteristics were significant factors <sup>15</sup> in predicting the level of assets held by respondents
Tenure of financial advice	At least 4 years. (Longer tenure is predictive of higher level of assets.)
Income	Over \$35,000. (Higher income is predictive of higher level of assets.)
Financial literacy	Demonstrated financial literacy is predictive of higher assets.
Gender	Being male is predictive of higher assets.
Age	Being between ages 45-65 is predictive of higher assets. Higher age is predictive of higher assets.
Household composition	Households with two or more income earners are predictive of lower assets.
Province	Residing in Ontario, Alberta or British Columbia is predictive of higher assets.

**Table 4: Sample variables explaining the level of assets**

Based on these results, the researchers conclude that:

- Having a financial advisor has a significantly positive relationship on the level of household financial assets, and
- The longer the advice relationship, the greater the impact. These impacts exist after accounting for the broad range of variables described in Table 1.

What can be said about the magnitude of the impact of advice? The researchers estimate these impacts using the estimated coefficients on the tenure of advice.<sup>16</sup>

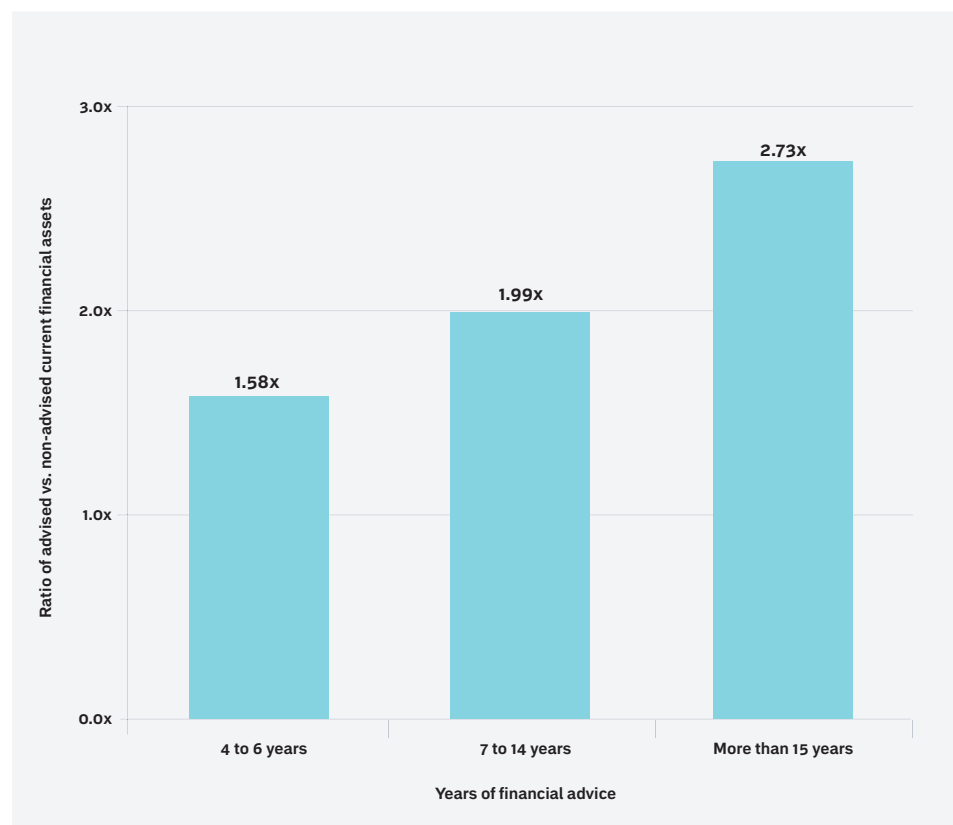
<sup>15</sup> These variables had estimated coefficients that are significant at the 99% level ( $p < 0.01$ ). For a detailed list of coefficients, see Appendix B.

<sup>16</sup> The detailed methodology is provided in the research paper, footnote 24, p.17. The variables can be found in Table III.2. of the research paper.

Chart 2<sup>17</sup> shows financial assets for households that received advice over various time periods, as a multiple of the financial assets of households that did not receive advice. This data removes the influence of all other variables, so that the difference is attributable only to receiving financial advice.

The data show that an Advised household that has worked with a financial advisor for four to six years accumulates 58% (1.58 times) more assets than a Passive Non-Advised household that is identical in all other respects. Similarly, a household with a financial advisor for seven to 14 years accumulates 99% (1.99 times) more assets than an otherwise identical Passive Non-Advised household. After 15 years or more with a financial advisor, the Advised household accumulates 173% (2.73 times) more assets than an otherwise identical Passive Non-Advised household.

**“...an advised household that has worked with a financial advisor for 15 or more years has 2.73 times more assets.”**



**Chart 2: Comparison of financial assets between households that received advice and those that did not receive advice depending on the length of the advice relationship**

<sup>17</sup> This chart has been adapted from the original chart in the CIRANO research paper. The CIRANO chart included raw data (before removing the influence of other factors). This chart shows only the econometric data, in which the influence of other factors has been removed.

## 2. ADVICE IMPROVES SAVINGS BEHAVIOUR

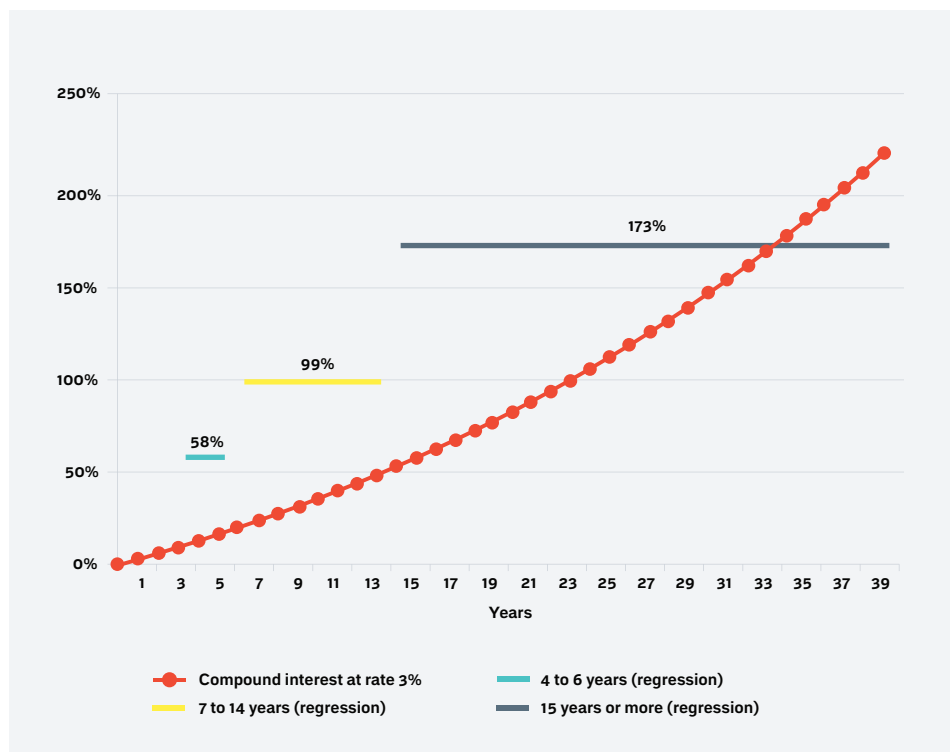
What could explain why Advised households have more assets than Passive Non-Advised households over the same time period, after all other observable differences are controlled? For example, as Chart 2 illustrates, households that receive financial advice over 15+ years have 2.73 times more assets than Passive non-Advised households over the same period. One suggestion might be that financial advisors are able to improve the investment returns of their clients through asset selection and portfolio optimization. In other words, better assets and better asset mixes translate into improved returns and higher asset levels over time. Is this a plausible explanation of the significant differences in asset levels shown in Chart 2?

Efficient market theorists would argue that return advantages derived from advice are not much greater than zero, if at all. On the other hand, empirical research documents investment returns, net of fees, on advised accounts that are as much as 3% higher than on non-advised accounts.<sup>18</sup> While this debate continues, it might be reasonable to conclude that a financial advisor could produce a yield advantage for clients of between 0 and 3% annually relative to what clients could earn on their own.

In order to determine if this yield advantage can explain the difference in asset levels between advised and non-advised households reflected in Chart 2, the researchers take the upper end of this range—3% net of fees—and examine the impact of this additional yield on financial assets over time. Their analysis shows that the impact of a compound 3% annual rate of return advantage on assets falls substantially short of asset levels observed for the households that received advice, for all three tenures of financial advice. For example, it would take over 15 years for a 3% yield advantage to increase assets by 58%; the advised households achieve this differential in 4 to 6 years. Clearly, the increase in assets of Advised households relative to Non-Advised households cannot be explained by asset selection alone.

**“...the increase in assets of Advised households relative to Non-Advised households cannot be explained by asset selection alone.”**

<sup>18</sup> Aon Hewitt and Financial Engines *Help in Defined Contribution Plans: 2006 Through 2010, September 2011* compared the accounts of workers who received some form of financial help with those who received no financial help in the period from 2006 to 2010. For median returns, the advised participants received on average returns net of fees about 3% higher than non-advised participants.



**Chart 3: Percentage increase in the net worth of advised participants over non-advised participants with the same level of initial assets**

**“Advised households save at twice the rate of Passive Non-Advised households.”**

To investigate this further, the researchers look at other variables that might help to explain the higher levels of assets acquired by Advised households. They note important differences in the savings rates of Advised and Passive Non-Advised participants. Table 5 shows that Advised households save at twice the rate of Passive Non-Advised households excluding Traders (8.6% compared to 4.3%). Traders save at the highest rate of 10.4%.

The researchers note that other studies report that advised investors hold higher proportions of non-cash investments, and participate more in tax sheltered plans, in comparison to non-advised investors.<sup>19</sup> Could any of these variables—the savings rate, the ratio of non-cash over total investments, and the ratio of RRSP investments over total investments—play a role in the higher asset levels achieved by Advised, as compared to Non-Advised households?

<sup>19</sup> IFIC, *The Value of Advice: Report 2010 and The Value of Advice: Report 2011*.

Advised	8.6%
Passive Non-Advised (excluding Traders)	4.3%
Traders	10.4%

**Table 5: Savings rates for Advised, Passive Non-Advised, and Traders**

To answer this question, the researchers develop predictive models<sup>20</sup> for each of these ratios. Since the ratios display classic features of “censored data”,<sup>21</sup> the analysis requires conditional estimation techniques. For example, in the case of the savings rate, the researchers develop a predictive model to explain the savings rate among those who save. The savings rate model consists of two equations: one explaining the probability that the respondent will save, and the second explaining the rate, given that they are savers.

**“... financial advice increases the probability that a respondent saves, and among those who do save, it increases the rate of saving.”**

The results from the savings rate model demonstrate that financial advice increases the probability that a respondent saves, and among those who do save, it increases the rate of saving.

Similar models are designed for the “ratio of non-cash to total investments” and the “ratio of RRSP to total investments”. The predictive values of the three ratios are then added as explanatory variables in a model explaining the level of assets. This analysis found statistically significant positive effects for the “savings rate” and the “non-cash to total investments ratio”. According to these findings, a 1% increase in the “savings rate” increases the level of assets by 8.7% and a 1% increase in the “ratio of non-cash assets to total investments” increases the asset level by 8.5%.

The effect of having a financial advisor on the level of financial assets can be isolated through the predictive values of the ratios described above. The researchers conclude that if you compare two otherwise identical individuals, the one with a financial advisor will have 106% more financial assets or 2.06x the level of financial assets of the passive non-advised respondent. This value is comparable to the previous analysis.

<sup>20</sup> “Predictive models” use the estimated coefficients and observed data for the determining variables to predict the value of the variable being explained – in this case the Savings Rate.

<sup>21</sup> With censored data, where the relationship being examined is only valid for non-zero or non-negative points, ordinary estimation techniques produce biased coefficients. For the savings rate, allocation to non-cash assets, and ratio of RRSP investments, the researchers adjusted for this by applying a Tobin Type 2 methodology to estimate the determinants of the dependent variable conditional on it being non-negative. For each ratio, the technique consisted of estimating two equations—a Probit Model to explain the probability of a non-negative ratio, and a regression model to explain the ratio, conditional on it being positive.



To sum up, the researchers show that:

- The higher level of assets acquired by Advised households in comparison to Passive Non-Advised households cannot be explained by asset selection alone;
- Having advice is an important contributor to the rate at which households save; and
- Higher savings rates contribute to higher levels of assets.

All evidence points to **improved savings behaviour** as the key to the relative success that Advised households have in accumulating assets, and the important role of the financial advisor in encouraging this behaviour.

### 3. ADVICE POSITIVELY IMPACTS RETIREMENT READINESS

Survey respondents exhibit strong differences with regard to retirement readiness. On a scale of one to 10, a total of 56.4% of Advised households indicate with a score of six or higher that they feel confident they will have enough money to retire comfortably. Only 40.8% of Passive Non-Advised households feel the same way. Traders again differentiate themselves with 71.4% declaring this level of confidence.<sup>22</sup>

To test whether or not these differences can be attributed to the presence of advice or better explained by other variables, the researchers develop a model for retirement readiness as explained by financial advice plus all external variables (such as those described in Table 1).<sup>23</sup>

Having a financial advisor is found to have a strong and significantly positive effect on the level of retirement readiness. Controlling for all other explanatory variables, the researchers show that having a financial advisor increases the probability of a respondent declaring confidence in achieving a comfortable retirement by more than 13% relative to a Passive Non-Advised respondent.<sup>24</sup>

Other important characteristics promoting high levels of confidence include: high incomes, availability of workplace pensions, and employment in the public sector. Respondents who are older, and thereby closer to retirement, are less likely to feel confident that they will have enough money to retire comfortably.

**“Survey respondents exhibit strong differences with regard to retirement readiness.”**

<sup>22</sup> Respondents were asked: “To what extent do you either agree or disagree with the following statement: ‘I am confident that I will have enough money to retire comfortably?’”

<sup>23</sup> The researchers use a Simultaneous Probit Model with the first equation explaining the probability of being ready for retirement and the second equation the probability of having a financial advisor, as defined on page 10.

<sup>24</sup> To compute this, the researchers calculate the marginal effect for each individual. The mean of these marginal effects is the value reported in the text.

## 4. ADVICE POSITIVELY IMPACTS LEVELS OF TRUST, SATISFACTION AND CONFIDENCE IN FINANCIAL ADVISORS

### Trust in financial advisors

A person's declared trust in financial advisors is an important indicator of the value that the person attaches to financial advice in general. The research study examined this by asking all respondents the following questions:

- From the initial survey: "Do you trust financial advisors?"
- From the follow-up survey: "Do you associate 'trustworthy' or 'trusted' with the term 'Financial Advisor'?"

For both sets of responses, the researchers estimate equations similar to the above analysis of retirement readiness.<sup>25</sup> While there are some differences between the two sets of results, both provide strong confirmation that having a financial advisor increases the probability of declaring trust in financial advisors. Controlling for all other explanatory variables, the research study identifies that an Advised respondent has a 28% higher probability of declaring trust in financial advisors than to a similar Passive Non-Advised respondent for the initial survey question, and a 32 percentage point higher probability for the follow-up question.<sup>26</sup>

### Satisfaction with financial advice

When a client is satisfied with a service, s/he is likely to continue with that service in the future.

The researchers measured satisfaction with financial advice by asking people with advisors: "Thinking about your primary financial advisor, how would you rate your household level of satisfaction with the following items?" The items explored in this question were:

- Value for money/cost,
- Product offering,
- Service offering (e.g., financial planning, tax advice, insurance advice, asset allocation),
- Knowledge level,
- Financial outcome/performance,
- Personal attention and understanding of my situation,
- Accessibility, and
- Independence.

The researchers found the levels of satisfaction for these measures to be stable and very high, ranging from 74.7% (value for money/cost) up to 86.3% (knowledge level).

<sup>25</sup> For both, the researchers use a Simultaneous Probit Model with the first equation explaining the probability of trusting a financial advisor and the second equation the probability of having a financial advisor, as defined on page 10.

<sup>26</sup> The estimated impacts are derived according to the methodology supplied in the research paper, footnote 31, p. 26.

### **Confidence in financial advice**

To examine respondents' level of confidence in financial advice, the follow-up survey asked: "Which of the following words do you associate with the term 'financial advisor'?" Respondents were asked to select all words that apply.

Some of the words are clearly negative (e.g., confusing, detached, dull) and others are clearly positive (e.g., competent, friendly, trustworthy). The researchers compute a general scale from the responses from 0 (the lowest) to 1 (the highest). Respondents with scores of from 0.8 to 1.0 are counted as having "high confidence" in financial advisors. Respondents with scores of from 0 to 0.2 are counted as having "low confidence" in financial advisors.

Applying a similar methodology for satisfaction levels, the researchers test the probability of having a high level of confidence in financial advisors. The same treatment is then applied for the probability of having a low level of confidence in financial advisors.

The results indicate strongly that respondents who have a financial advisor are more likely to have a high level of confidence in financial advisors, and less likely to have a low level of confidence in financial advisors.

**"The results indicate strongly that respondents who have a financial advisor are more likely to have a high level of confidence in financial advisors."**

New evidence is brought to bear on the value of financial advice with the release by CIRANO of the research paper *“Econometric Models on the Value of Advice of a Financial Advisor”* by Professor Claude Montmarquette and Nathalie Viennot-Briot.

Through scientific data analysis of a robust sample of Canadian households, the researchers convincingly demonstrate that having a financial advisor contributes positively and significantly to the accumulation of wealth, and provides important insights on how advice contributes to asset growth.

The research paper provides new evidence that:

- 1. Advice has a positive and significant impact on financial assets after factoring out the impact of close to 50 socio-economic, demographic and attitudinal variables that also affect individual financial assets;**
- 2. The positive effect of advice on wealth accumulation cannot be explained by asset performance alone: the greater savings discipline acquired through advice plays an important role;**
- 3. Advice positively impacts retirement readiness, even after factoring out the impact of a myriad of other variables; and**
- 4. Having advice is an important contributor to levels of trust, satisfaction and confidence in financial advisors—a strong indicator of value.**

Financial advisors instill in their clients the importance of saving regularly and maintaining a savings discipline through the execution of a plan. The research paper confirms that this fundamental behavioural change is likely to be at the root of the higher asset growth of Advised relative to Passive Non-Advised investors. Advice is found to contribute significantly to the rate at which households save. The longer the advice relationship, the greater the impact on wealth. Individuals receiving advice are more confident that they will have enough to retire comfortably, and they exhibit higher levels of trust, satisfaction and confidence in financial advice. These are all important indicators that advice creates lasting and measurable value for those who receive it.

## ESTIMATED COEFFICIENTS FOR VARIABLES EXPLAINING THE PROBABILITY OF HAVING A FINANCIAL ADVISOR

Estimated coefficients for variables listed in Table 3.

Significant Variables Explaining the Probability of Having a Financial Advisor	Estimated Coefficient <sup>27</sup>
Advice Threshold	-1.62e-06
Income before taxes >=90,000	0.416
Savings > 0 and <= 3,000	0.255
Savings >3,000 and <= 10,000	0.444
Savings > 10,000	0.673
Never save for retirement	-0.578
Couple with no children	0.260
45<= age<54	0.294
54<=age<65	0.535

All coefficients shown are significant at the 99% level ( $p < 0.01$ ).

Table 3: Determinants of having a financial advisor

<sup>27</sup> Coefficients extracted from the research paper, Table I.1, p.11. Only coefficients with the highest level of significance ( $p < 0.01$ ) are listed in this appendix.

## ESTIMATED COEFFICIENTS FOR SIGNIFICANT VARIABLES EXPLAINING THE LEVEL OF ASSETS

Estimated coefficients for variables listed in Table 4.

Significant Variables Explaining the Level of Assets	Estimated Coefficient <sup>28</sup>
Tenure of Financial Advice: 4 to 6 years	0.456
Tenure of Financial Advice: 7 to 14 years	0.687
Tenure of Financial Advice: 15 or more years	1.006
35000<= income before taxes <60000	0.482
60000<= income before taxes <90000	1.081
Income before taxes >=90000	1.682
Fully retired	0.387
Minimum living needs at retirement: More than 80%	0.388
Never save for retirement	0.926
Financial literacy	0.288
Male	0.196
45<= age<54	0.586
54<=age<65	0.950
Two income earners	-0.216
Three or more income earners	-0.379
Ontario	0.295
Alberta	0.424
British Columbia	0.395
Constant	8.947

Table 4: Determinants of the level of assets

All coefficients shown are significant at the 99% level ( $p < 0.01$ ).

<sup>28</sup> Coefficients extracted from the research paper, Table II 1.2, p.15. Only the coefficients of variables with the highest level of significance are listed in this appendix.

### About this Publication

New Evidence on the Value of Financial Advice is a guide to understanding the research paper *Econometric Models on the Value of Advice of a Financial Advisor*. For more information about the research paper, refer to the box on the right.

The research paper was written for experts with a deep understanding of econometric models. New Evidence on the Value of Financial Advice provides a plain language overview of CIRANO's methodology and findings, and highlights the important contributions of the research paper to our understanding of advice and how it benefits investors.

### About the Author

New Evidence on the Value of Financial Advice was written by Dr. Jon Cockerline, Ph.D., Director, Policy and Research, The Investment Funds Institute of Canada. Prior to his present position Dr. Cockerline was Director, Capital Markets at the Investment Dealers Association of Canada, and before that, he was Director of Research at the Toronto Stock Exchange. Dr. Cockerline began his career as an economist at the Bank of Canada. He subsequently held various positions with the federal Department of Finance including Chief, Debt Policy and Markets, where he was responsible for management and policy development for Canada's debt and foreign exchange reserves. Dr. Cockerline has a Ph.D. in Economics from McGill University and was awarded the CFA Charter in September 2003.

### About The Investment Funds Institute of Canada

The Investment Funds Institute of Canada ([www.ific.ca](http://www.ific.ca)) is the voice of Canada's investment funds industry. IFIC brings together 150 organizations, including fund managers and distributors, to foster a strong, stable investment sector where investors can realize their financial goals. The organization is proud to have served Canada's mutual fund industry and its investors for 50 years.

For more information about New Evidence on the Value of Financial Advice, contact: Dr. Jon Cockerline, [jcockerline@ific.ca](mailto:jcockerline@ific.ca), 416-309-2327

### About the Research Paper

The research paper *Econometric Models on the Value of Advice of a Financial Advisor* was released in July 2012 by the prestigious Center for Interuniversity Research and Analysis on Organizations (CIRANO). It can be viewed online at: <http://www.cirano.qc.ca/pdf/publication/2012RP-17.pdf>

The lead researcher was Dr. Claude Montmarquette, Ph.D., President and Chief Executive Officer and Vice-President Public Policies at CIRANO. Dr. Montmarquette has a Ph.D. in economics from the University of Chicago, and is full professor in the Department of Economics at the University of Montreal. He is well known as a specialist in the economics and econometrics of education and labour, and in the economics of public choice.



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