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Advisors in Sync With Clients, But May Overestimate Risk Tolerance

By Bing Waldert, Cerulli Associates

In Cerulli Associates' survey of IMCA membership in late 2009, respondents named additional financial planning services in their practices as the primary planned change because of the bear market. This planned change reflected a greater need to tie financial advice delivery to client needs and to de-emphasize mere investment performance. A similar process of evaluation occurred at asset managers, where firms experienced massive flows out of equities into more conservative vehicles such as cash and fixed income. Constituents throughout the industry were reminded of the importance of client needs and opinions.

This is perhaps best illustrated by looking at the personal and economic concerns of retail investors. Rarely does one see massive shifts in consumer opinion—financial or otherwise. However, economic concerns of investors will change quickly to reflect the current economic climate. For example, 18 months ago, investors were chiefly concerned with energy prices, whereas today investors' primary concerns are the real estate market and the cost of health care. On the other hand, clients' personal financial concerns remain relatively static. Retirement preparedness, wealth preservation, and cash flow consistently rank as investors' greatest personal concerns. The relative importance of these various elements can change greatly based on a client's underlying wealth. The least-wealthy investors are most concerned about cash flow and the most-wealthy investors are most concerned about wealth preservation. Regardless, advisors can benefit from focusing client conversations on the client's goals and how the client is progressing toward those goals—rather than on economic headlines.


For the most part, financial advisors are in tune with the needs of clients. IMCA respondents ranked the same three

factors—retirement planning, wealth preservation, and cash flow—as their three primary concerns for clients. Some mismatches exist between advisor perception and client opinion, however.

First, advisors are likely to overestimate the number of clients who consider themselves to be aggressive investors. Advisors must be careful not to overestimate clients' risk tolerance. When asked about which products clients were asking about, some of the most common responses were conservative products, such as municipal bonds and certificates of deposit (CDs). Nowhere is this more true than with the wealthiest investors; as noted above, the richest investors are also the most concerned with wealth preservation. Regardless of client wealth, advisors should re-evaluate how they manage risk in client portfolios and how this is communicated to clients.

Second, investors are likely to be more concerned about taxes than advisors perceive. If anything, the industry has discouraged advisors from thinking of themselves as tax experts. While advisors don't need to completely understand clients' tax returns, advisors may benefit from paying closer attention to taxes when considering the services they provide and products they recommend. Better tax sensitivity may improve client satisfaction.

Finally, attitudes of retail investors do shape the financial advisory industry. Advisors are in tune with clients, and clients' needs shape the services and products provided. Understanding client needs also has implications for broker-dealers, product manufacturers, and service providers, who support advisors.

Table 1 defines the wealth tiers used by Cerulli Associates in evaluating the survey data. 

Methodology: In January 2010, IMCA distributed a survey link to more than 7,500 current IMCA members providing access to a proprietary Cerulli Associates online survey instrument. The total respondent base of 126 is a sample of the investment advisor and broker-dealer membership of Investment Management Consultants Association.



TABLE 1: CERULLI WEALTH TIERS, 2009

Wealth Tier	Name of Tier	Investable Asset Range	Net Worth Range	Client Needs/Description	
Ultra-High-Net-Worth	Tier I	Ultra-high-wealth market	>\$20m	>\$50m	Family office services
	Tier II	High-wealth market	>\$10m–\$20m	>\$25m–\$50m	Increasingly complex product set (e.g., direct hedge fund investment), wealth preservation, estate planning
High-Net-Worth	Tier III	Wealth market	>\$5m–\$10m	>\$10m–\$25m	Increasingly complex product set (e.g., direct hedge fund investment), wealth preservation, estate planning
	Tier IV	Affluent market	>\$2m–\$5m	>\$5m–\$10m	Increasingly complex product set (e.g., funds of hedge funds), needs shift to preservation
	Tier V	Mass-affluent market	>\$500k–\$2m	>\$1m–\$5m	Accumulation, holistic distribution, more complex product set (e.g., separate accounts)
	Tier VI	Middle market	>\$100k–\$500k	>\$250k–\$1m	Advice, accumulation, holistic distribution
	Tier VII	Mass market	<\$100k	<\$250k	Accumulation, maximize income

Sources: Federal Reserve, Cerulli Associates

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5619 DTC Parkway, Suite 500
 Greenwood Village, CO 80111
www.IMCA.org
 303.770.3377 (p) 303.770.1812 (f)

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