IBF Financial Planning Connect[1]

"The Financial Planning Narrative and the Role of Financial Advisors"

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Synopsis

The theme of my talk is how financial planners or advisors can move up the value chain and the standards of competency this requires. I start with the claim that financial planning needs are underserved in Singapore and discuss the reasons for this state of affairs. I argue that a large pool of underserved individuals provides a unique opportunity for financial advisors to expand their role to help clients fill important gaps in financial planning. At the same time, I show evidence that lack of "trust" has been and still is a key barrier to people approaching financial advisors for financial advice. I suggest that to win client confidence, the common perception that financial advisors are mainly product sales driven must be corrected, that financial advisors must demonstrate not only salesmanship but also mentorship, that this evolution of roles requires enhanced standards of knowledge, competency and professionalism at the level of advisors *and* institutions (examples given), and that advisors should be remunerated not only for meeting sales targets, but also competency in delivering valued advice.

[1] Supported by Association of Financial Advisers (AFA), Financial Planning Association Singapore(FPAS), Insurance and Financial Practitioners Association of Singapore(IFPAS) and Life Insurance Association Singapore(LIA), IBF is organizing this event to launch the Financial Planning standards and showcase the industry collaborative efforts to raise the bar of financial advisers in Singapore.

Financial planning needs are underserved in Singapore. Singaporeans spend much of their busy lives working, paying off hefty mortgages, and raising children. Time is a scarce resource. So, the average Singaporean has little bandwidth for many critical aspects of personal financial planning such as investment and retirement planning. To many people, planning for long-term goals like retirement or wealth accumulation takes a back seat to more immediate daily needs. This has got to change, as people are living longer, and CPF funds cater only to a basic standard of living post-retirement.

Financial advisors (and I will use this term generically to encompass independent financial advisors, relationship managers of banks, and insurance advisors and their agent managers) can play an important role in improving the financial literacy of the clients you come into contact with. This is not just a matter of altruism. It makes business sense. If you are able to change people's mindset and provide them with a compelling narrative of the rewards of continual financial planning, you increase your chances of cementing a relationship with them as long-term clients.

What are the key elements of this narrative? How do you arouse in your clients the passion for lifelong planning? How do you equip yourself with the knowledge and professionalism to sustain a long-term client relationship?

In my mind, the planning narrative has four key elements: (1) starting early; (2) a commitment to save, (c) wealth accumulation through investments and (4) wealth protection and distribution. This is a narrative because it has got a time dimension to it.

Lifecycle theory in economics teaches us that people save during their working years in order to provide the means to spend during their retirement years. They would know to figure out their retirement goals and put in place investment plans to achieve their goals.

Reality is very different. The HSBC Future of Retirement Survey 2015 shows that for 82% of Singaporeans, saving for retirement is *not* a priority. About 2 in 5 retirees underestimate the amount they need. And working age people are more comfortable holding cash and insurance policies than investing for higher returns.

There is also a poor understanding of the basic concepts of risk and return in the population. According to a 2015 investment survey of 1,000 Singaporeans by Black Rock Asset Management, the average target return by respondents is over 8% per annum, but across all age groups, respondents hold 46% of their money in cash. Equities comprise less than 20% of the average investor's portfolio.

The mismatch between desired returns and asset allocation is also evident from a May 2015 survey of investor expectations by Schroders Asset Management: the average investor wants to hold just 21% of their wealth in equities, yet most expect a return of at least 10% over the next 12 months.

For most people, the concept of retirement planning is complicated and confusing. Being loss-averse and unfamiliar with managing investment risks, people choose the easy route of holding sizeable amounts in low-return assets which will only diminish their chances of enjoying a comfortable retirement.

Richard Thaler, noted behavioral economist and co-author of *Nudge*, a book on how to coax people into making better financial decisions summarizes the state of financial planning very well:

"Most people have difficulty understanding how numbers like savings rates, expected rates of return, and volatility translate into changes in their lifestyles when they are old. Forming and managing an investment portfolio over a long period of years is difficult. The end result is similar to what you might expect if most of us try to cut our own hair: a mess"

Obviously, this is an unsatisfactory state of affairs for both individuals and society. On the bright side, as a financial advisor, you can make a difference if you expand your role from one that is product-centric to one that provides your clients with valued advice which will ultimately help improve their financial literacy. The challenge is to internalize the planning narrative (which by the way, is pretty similar for most people), and parlay this into a long-term relationship with your clients.

The key to building this long-term relationship is trust. If people do not trust financial advisors, they will seek advice elsewhere such as family and friends, many of whom need financial guidance themselves!

What is the state of trust in the financial planning industry? Being a young nation, the financial literacy movement in Singapore has a relatively short history compared to countries like the US, where public financial education goes back to the 1930s. In Singapore, the setting up of MoneySENSE by the Monetary Authority of Singapore (MAS) in 2003 was a milestone. MoneySENSE was launched in 2003 by then Deputy Prime Minister Lee Hsien Loong and Chairman of MAS, to help Singaporeans "become more self-reliant in their financial affairs" so as to "manage their day-to-day finances, make prudent investments and plan for their long-term needs". An inter-ministerial Financial Education Steering Committee (FESC) and a MoneySENSE Working Group (MSWG) were formed to spearhead a host of educational outreach initiatives. Among these was Singapore's first National Financial Literacy Survey, which collected questionnaire responses from a total of 2,023 Singaporeans aged 18 to 60. The results of the survey were published in July 2005 in a 100-page report entitled, "Quantitative Research on Financial Literacy Levels in Singapore".

It is interesting to note that the survey covered three broad areas of financial literacy which closely overlaps with the planning narrative I mentioned earlier. The three aspects are (a) basic money management (covering savings, liquid asset management, and credit management); (b) investment and (c) insurance and retirement planning.

A striking finding from the MONEYSENSE survey was that 72% of respondents do not approach financial advisors for advice. About half of those who do (48%) did so because the advisor was a friend / relative, or that they had been approached (17%) by the adviser. Only 33% had sought professional advice because they felt that they would be getting advice from an expert. One way to interpret these results is that people do not feel that financial advisors' can help them improve their financial outcomes in a big way.

Things have not changed much since. A survey conducted by the Financial Planning Standards Board (FPSB) in 2015 found that 7 in 10 respondents said they did not know who to trust for financial planning. As in the MoneySENSE survey, more than half of the Singaporean participants (53%) said they rely primarily on their friends and family for financial matters and planning. Only 45% rely on financial planners for advice.

The FPSB survey was actually carried out across 19 markets on more than 19,000 adults. The Singapore sample comprised 1,001 participants who had primary or shared responsibility for household financial decisions. And despite being a premier financial center in Asia, Singapore ranked in the bottom three on confidence in the financial strategy and know-how of financial advisors. In short, while people clearly need help in financial planning, financial advisors are not their main source of advice.

In a Business Times piece I wrote in February, 2009 (entitled, "Restoring Trust in Bankers"), I said that many relationship managers practise more salesmanship than guardianship, but that this is understandable given the incentives for meeting sales targets and the penalties for not. So it is not surprising that the financial planning industry is still perceived by the public as one that is product sales driven, rather than advice driven. Fee-based advisors do offer more in-depth financial advice, but the fact is, people are generally averse to paying fees for advice.

The theme for this forum is raising standards. One key indicator of standards being raised would be when more and more people entrust their most important financial goals to the counsel of financial advisors. This is not possible unless clients believe that advisors have their best interest at heart and possess the competence to make a difference.

With an increasingly educated client pool, advisors must upgrade their technical skills which will be called upon when clients require advice in diverse areas such as building financial roadmaps, quantifying goals, developing savings, liquidity and insurance plans, articulating investment goals through investment policy statements, designing investment glide paths, understanding/simulating short and long-term risks, incorporating investment styles into asset allocations, portfolio rebalancing, tax and estate planning, insurance and business succession planning. As a financial advisor, you may also be your client's first port of call for advice in times of market turbulence.

So, to advice clients well, financial advisors themselves must be trained and constantly re-tooled to keep abreast of regulations, market trends, and indeed, even academic research that have important bearing on financial planning.

I can give a personal example on the latter. Brandes Investment Partner is a leading investment advisory firm with over $26 billion of assets under management. Its clients comprise mainly institutions that invest with a focus on long-term returns based on value principles. I am on the Board of Advisors for its research unit, the Brandes Institute, which generates a stream of interesting and highly relevant investment research that constitutes implementable investment ideas. I invite you to visit their website - you will find readable papers on topics such as strategic asset allocation, low-volatility investing, smart betas and of course, value-investing. The point is: here is one institution which is clearly commercial but through its research, adds credibility and intellectual gravitas to what it does.

The process I have described above does not diminish the importance of product or sales. In fact, well-designed products will always be a key component of financial planning, whether these are savings products such as high-yield, liquid savings accounts, target-date (lifecycle) funds, or insurance and annuity products with innovative features.

In dispensing product solutions to clients, financial advisors must always inspire trust. This can only happen if advisors perform their duties with care and integrity. Care means that products should only be recommended to clients if they are "fit for purpose". Examples of the contrary is when a product is recommended even though the client does not understand the product well enough to make an informed choice, does not have the appropriate risk tolerance, or already has purchased products with similar risks, since adding more products of the same risk class would go against the principle of diversification.

Ethical leadership begins at the highest level of an institution. Codes of ethics should be adopted by senior management, the board of directors and oversight units of the organization, thus sending a strong message that everyone in the organization are to serve their clients with duty of care. This message should be enforced by clear remuneration/promotion policies as well as internal audits. Financial advisors should not be evaluated purely on sales but also on whether he has looked after a clients' best interest in actions such as advising clients to diversify, limit "risk-on, risk-off" trades, which are a sideshow to the larger scheme of meeting long-term goals, invest in cost-effective investment and insurance products and so on.

Senior management should also institute checks to minimize product mis-selling. In my contribution to the December 2009 issue of the CFA magazine shortly after the global financial crisis, I suggested that to rebuild trust with customers, financial institutions should adopt a multi-layer process of checks before products recommended by an advisor can be sold to a client. I am encouraged to hear that many banks now have such processes in place. They should also be beneficial to non-bank financial service providers.

In closing, this year's budget has focused on the need for a greater pace of innovation, especially in manufacturing. Perhaps it is time for the financial planning industry to ask how it too can be more innovative in upgrading its standards of service. Financial institutions should deploy technology to create web-portals and apps to arouse the public's interest in financial planning. As mentioned, people find investment and retirement planning complex and confusing. Technology is a great simplification tool. Imagine your app or web users interacting with a highly intuitive interface. Imagine delighting them with interesting visuals such as simulated wealth paths that literally gives them a picture of wealth outcomes to expect for a particular planning narrative. Untidy calculations are hidden in the background seen by no one except the programmers. The complexity of financial planning is reduced, if not gone.

This is an exciting time to be a financial advisor. Thank you.