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& PARTNERS

Why the choice between advisors and robo-advisors is more obvious in times of volatility

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THE GLOBE AND MAIL
PUBLISHED JANUARY 9, 2023

See the column on The Globe and Mail's website here. (Subscription required)

Robo-advisors automatic rebalancing can take advantage of buying opportunities in changing markets. That is unless investors panic and sell at the wrong time.

The rise of robo-advisors over the past decade may have some investors questioning whether they still need to seek out a wealth advisor. While robo-advisors are cost-effective and easy to use, can these services meet all of an investor's needs? And where does it leave human advisors?

For many young investors or those who are just starting their investment journey, robo-advisors can be an affordable way of managing their savings. They're automated algorithms that provide investment services with little to no human interaction. They build and adjust a portfolio of investments automatically based on questionnaires clients have completed.

While robo-advisors can have the advantage of lower costs, they fall short when an investor's needs become more complex. As investors grow and age, they typically seek out more holistic advice.

They may question what proportion of their after-tax cash flow should go toward saving or debt repayment. How their children will have access to and funding for their education? How to prepare for unexpected events like health scares and how incorporate philanthropy, tax and estate planning into their goals, and plan for a comfortable retirement?

Robo-advisors can be useful for the basics, but as investors' financial needs evolve, they may need to turn to an experienced advisor to provide a comprehensive perspective on their financial situation and guide them on how to achieve their goals.

Holistic, goals-based advice

Robo-advisors use a one-size-fits-many approach, while advisors can take a highly personalized, holistic goals-based approach.

Advisors determine risk tolerance and investment style, often incorporating values and interests into portfolios, advising on property ownership and financing, optimizing businesses for income splitting and retirement planning, providing needs analysis, insurance, and personalized benefits plans.

By analyzing this information, an advisor can discuss the client's overall financial situation and give insight into specific goals they may have, tracking their progress actively and adjusting for changes in circumstances.

While robo-advisors focus solely on investments and rebalancing, advisors can structure a personalized plan to put their clients on the right path.

For example, many business owners wonder if they should withdraw cash from their company to pay off debt, incurring a larger tax bill to lower their interest and mortgage payments. An advisor can analyze whether the taxes paid on withdrawing capital from their company will offset the increase in interest payable on the mortgage or not.

Expertise in times of uncertainty

Even for professionals, navigating through market cycles can be challenging. The past year has been a difficult investment climate for almost all investors as rising interest rates, inflation, and global uncertainty have affected almost all asset classes negatively. During these difficult times, when many individuals are staring at significant drawdowns, it can be daunting for them to make the right financial decisions.

Robo-advisors' automatic rebalancing can take advantage of buying opportunities in changing markets. That is unless investors panic and sell at the wrong time. A recent report from Vanda Research Ltd. shows the average active amateur investor's portfolio is down about 30 per cent this year as big bets, which paid off handsomely in the past, began to backfire.

Working with an advisor can take the emotional toll out of making difficult investment decisions during times of uncertainty. They can also avoid the peer pressure and adrenaline some investors feel about chasing momentum and speculative fad investments.

Instead, advisors will re-focus on investing like a rational business owner thinking about buying a business. In times of uncertainty, advisors can re-orient clients by reviewing their progress toward their goals, preparing for contingencies, and providing a reassuring voice among the market noise.

Who takes accountability?

Robo-advisors rely heavily on clients' self-discipline, but they lack accountability. For the strong, hands-off investor, they can be a good resource. However, for clients who struggle to stick to a savings plan, suffer from "paralysis by analysis," or tend to sell when markets become challenging, robo-advisors don't provide the confidence or expertise to question investment decisions or talk through investors' concerns.

Advisors can take a disciplined, personalized, and relationship-focused approach. Much like how a person may choose to hire a fitness trainer or train by themselves, investors can also choose to hire an advisor or manage their own finances.

While one option may appear more costly in the short run, it's much more likely to deliver the desired results in the long run. Regular training sessions, like wealth management progress reviews, encourage both parties to be present, outline goals and trade-offs, work toward them, and review progress together with accountability on both sides.

Robo-advisors occupy an important space in wealth management and have been an innovative tool to democratize investing. While they may be here to stay, they will not be able to replace the value a trusted advisor can offer clients.