RETIREMENT INCOME INSTITUTE
Alliance for Lifetime Income

Who Should Read This Insight:
Retirement investors, financial professionals (especially financial planners and advisors), employer-sponsored retirement plan advisors who work with individual investors, employer-sponsored retirement plan participants, employer retirement plan sponsors

Institute Research Agenda Topic:
Understanding differences in consumer behavior and decision-making

Insight: USING A FINANCIAL PLANNER AND PORTFOLIO PERFORMANCE

Definitions of **bold key terms** are at the end of this article.

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Authors, Titles and Publication Dates of the Articles Addressed in the Insight
Yao, Rui, and Shan Lei. 2018. "Source of Information and Projected Household Investment Portfolio Performance." Family and Consumer Sciences Research Journal *46 (3): 219–37.*

IDEAS IN THE INSIGHT YOU CAN PUT INTO ACTION

When talking with their kids about financial topics, parents should avoid traditionally defined gender roles that may influence saving and investing behaviors over the long term. Until the time that these gender differences dissipate, **financial professionals** can encourage consumers, especially women, to include protected lifetime income plans when planning for retirement. Protected lifetime income plans fit with women's lower risk tolerance and can decrease the chance that women will outlive their retirement assets. Finally, given the importance of parents' role in socializing their kids about financial literacy, policymakers can design programs that encourage parental participation in financial education at home.

PRINCIPAL INSIGHTS

Using national data that collect information on family finances, this study explored the relationship between investors' entire household investment portfolio's performance and the primary source where they obtain information when making retirement investment decisions. The primary information sources that individuals reported were either using a **financial planner** or being "self-directed." Self-directed refers to using information sources with little or no monetary cost, such as consulting with friends/relatives and/or a spouse/partner, conducting personal research or calling around, belonging to investment clubs, or accessing media.

Among the investors surveyed, 78 percent did not seek professional assistance when making saving and investment decisions while 22 percent used financial planners. Investors who used financial planners achieved significantly higher returns than self-directed investors for the same level of investment risks they took in their investment portfolio.

The two groups had significantly different socioeconomic characteristics. Compared to self-directed investors, those who used financial planners were older, wealthier, and had higher education. Among investors who used financial planners, 69 percent were 45 years of age or older. On the other hand, only 58 percent of self-directed investors were 45 or older. Non-Hispanic white investors accounted for 81 percent of those who used financial planners and 71 percent of self-directed investors. The majority of investors (53 percent) who consulted with financial planners had at least a bachelor's degree. However, only 38 percent of self-directed investors had similar education. Investors who used financial planners as their information source reported higher household incomes (average of $135,269) than self-directed investors (average of $87,602).

In addition, users of financial planners are more willing to withstand financial risks and are investing for longer-term financial goals than self-directed investors. Three-fourths of investors

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who consulted with financial planners reported at least an average level of risk tolerance, while only 58 percent of self-directed investors reported similar levels of risk tolerance. A higher percentage of investors who used financial planners (42 percent) than self-directed investors (33 percent) were long-term investors, reporting an investment horizon of at least five years.

Among investors with the same socioeconomic characteristics (such as age, gender, education level, and income) and expectations (such as how willing they are to withstand financial risks and whether they are long-term investors), the use of a financial planner was significantly positively related to their investment portfolio performance. Results showed that, compared with self-directed investors, investors who used financial planners as an information source when making saving and investment decisions were 116 percent as likely to achieve better returns for the same level of financial risks they undertook.

Among self-directed investors, those in the highest income group were over 300 times as likely as those in the lowest income group to achieve better portfolio returns for taking the same level of financial risks. On the other hand, among investors who used financial planners, those in the highest income quartile were 151.1 percent as likely. Similarly, compared to self-directed male investors, self-directed female investors were 124 percent as likely to achieve better investment portfolio performance. In addition, among investors who used financial planners, females were 18.9 percent less likely than (i.e., 81.1 percent as likely as) males to achieve better portfolio performance.

In summary, results of this study revealed evidence that portfolio performance, as measured by the amount of return for the same level of financial risks, was better for investors who used financial planners than for self-directed investors. In addition, the relationship between information source and portfolio performance was partially differed by respondents' income and gender. With their experience and expertise, financial planners should be able to identify useful and relevant information more efficiently than average investors. In contrast, investors who, whether unwilling or unable, do not regularly search for information are less efficient in such searches. Consequently, some investors are not fully informed at the point of decision-making, and the service of financial planners can help them fill the information void. The findings of this study have confirmed that the service of financial planners is positively related to a client's financial life.

One result that is of concern is that females who used financial planners were less likely to achieve better returns with the same amount of financial risks taken in the portfolio than males who used financial planners. It is established in the literature that females are less risk tolerant than males. Investors with low risk tolerance reasonably limit themselves to products with low risks. Although low portfolio performance may be due to a lack of attention on the part of financial planners who helped construct the portfolios, another possible reason for the low performance could be lack of selection of higher-return investment products among people with low risk tolerance. This, in turn, would lead to under-diversified portfolios that are more likely to have a higher risk, which reduces the amount of return that the portfolios can achieve for the same level of financial risks taken.

Retirement investors and employer-sponsored retirement plan participants, if they manage their own investments without consulting with professionals, need to consider not only the amount of return for the level of financial risks taken in the portfolio, but also their total portfolio including all investment assets. If they work with a financial planner or **advisor**, they should ask their financial professional to consider the performance of their entire investment portfolio. Doing this requires investors and their planners or advisors to have adequate knowledge of all of their assets. One area that is often overlooked in these discussions is the correlation between these assets (i.e. how closely these assets' returns go up and down together), which can increase or decrease the risks the investors are exposed to. Employers who sponsor retirement plans should provide investor education to help their plan participants understand not only the performance of assets held within the retirement plan, but also that the retirement plan asset is a part of their total investment portfolio.

To learn more, visit the Retirement Income Institute at
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KEY TERMS ARE SOURCED FROM THE ALLIANCE FOR LIFETIME INCOME'S ANNUITIES LANGUAGE GLOSSARY AND INVESTOPEDIA

Financial advisor: *A qualified person who can help you understand your options and make financial decisions to work toward your financial goals.*

Financial planner: *A qualified investment professional who helps individuals and corporations meet their long-term financial objectives.*

Financial professional: *A qualified person who can help you understand your options and make financial decisions to work toward your financial goals.*

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