Russell Investments

2023
VALUE OF AN ADVISER

YOUR VALUE IS IN THE NUMBERS

EMBRACE THE POSS/BLE™

EXECUTIVE SUMMARY

In a complex world that keeps posing challenges to investors, advisers continue to add value that enables their clients to attain their long-term financial goals.

The spectre of a global recession and rising inflation have created an environment of extreme caution in 2023, just three years after a global pandemic swept through markets to test investors' fortitude.

In this environment, Australians have relied on their advisers heavily to navigate both the practical and emotional aspects of investing. It is a relationship that proved fruitful not just in periods when markets fell, but also when assets rose to buoy portfolio gains.

Of course, financial advice encompasses much more than investing. It requires in-depth knowledge of taxation and social security, plus the understanding of human behaviour that's necessary to support people making life decisions.

Advisers proved more than up to the task over the past year.

Russell Investments' annual analysis shows the value of an adviser in Australia is approximately 5.9% in 2023.

This is substantially higher than the typical adviser fee paid by clients and a validation of the holistic service that advisers provide to clients. It is a function of their ability to help clients adapt as markets, regulations, and their own circumstances change.

Our 2023 Value of Adviser formula is:

A + B + C + E + T

Appropriate asset allocation

Behavioural coaching

Choices and tradeoffs

Expertise

Tax savvy planning and investing

A IS FOR APPROPRIATE ASSET ALLOCATION

Asset allocation is at the heart of every investment strategy, determining more than 85% of the outcome for an individual ahead of the selection of the actual assets within a portfolio.[1]

This known investment truth is becoming even more apparent as the range of investment opportunities increases, encompassing asset classes that didn't exist until recently and remain difficult for retail investors to access.

It is also, though, perhaps the most underestimated element of financial advice by the general public. Retail investors are more inclined to remember the returns of individual stocks – such as this year's gains from the so-called magnificent seven AI stocks – than how asset allocation laid the foundation for overall risk-adjusted returns.

Russell Investments' analysis shows that carefully considered asset allocation which takes into account the needs of an individual can add value of up to **1.2% per annum**.

Asset allocation: who benefits most

There are generally two types of non-advised superannuation investor. The first category is disengaged investors who either consciously or unconsciously opt for the one-sized-fits-many default options offered by their funds. By definition, these default options take limited – if any – account of personal circumstance or needs.

The second category are engaged investors who build their own portfolios but can sometimes find themselves falling foul of risks which they have not considered when allocating capital to different assets.

In both cases, professional advice can help prevent investors from falling behind in their retirement planning.

The disengaged super member

More than 63% of the $996 billion in MySuper investments is allocated to single strategy options.[2] This means members – no matter their age, super balance, or retirement goals – are invested in the same way as everyone else.

Let's take Jane as an example. Her adviser recommended an allocation of 80% to growth assets after conducting an analysis which considered her age, investment goals, superannuation balance and other preferences.

Her hypothetical portfolio could deliver an annualised return of 7.8% over a 10-year period, versus the 6.6% gain from a default superannuation fund with a 70% allocation to growth assets.

Her potential extra gain of 1.2% means her retirement savings could be worth $210,947 after 10 years – or $21,818 more than if she invested in a default portfolio.

Advised portfolio	Alternative: default portfolio
80% growth assets	70% growth assets
7.8% p.a.	6.6% p.a.
$210,947	$189,129
Jane's advised portfolio delivers 1.2% p.a. higher return from an appropriate asset allocation; nearly $22,000 over a 10 year period	

This example is provided for illustrative purposes only.

[1] Russell Investments Making Super Personal White Paper 2020
[2] APRA, Quarterly MySuper Statistics Report, 30 June 2023

The DIY asset allocator

There are inherent risks in a DIY approach to asset allocation that can limit investment returns – ranging from a lack of investment know-how, to ill-discipline that prevents an individual from implementing a strategy and reweighting it as required.

The increasingly complex world of investing requires an in-depth knowledge of markets, economics and geopolitics that is difficult for individuals to both attain and maintain. Advisers can fill this gap by offering an insight into alternative assets which make up a larger part of institutional-grade portfolios than previously, such as private debt and infrastructure.

The above factors are reflected in Australian Taxation Office statistics which consistently show self-managed super funds (SMSFs) have a relatively high allocation to cash. The latest figures show SMSFs had a 16% allocation to cash at March 2023.[3]

Such conservative asset allocations can hold investors back if they require capital growth to meet their retirement goals.

For example, Lee has a SMSF he manages on his own. It holds over 70% in cash and other defensive assets, even though an adviser may recommend that over half his portfolio should be in growth assets given his circumstances and objectives.

Indeed, Lee's portfolio could deliver a hypothetical return of 4.3% over 10 years versus a return of 5.7% from a portfolio split equally between growth and investment assets. The significant difference of 1.4% could be reduced if Lee sought assistance from a financial adviser to determine the asset allocation best suited to his needs.

Lee's option for advised or DIY asset allocation:

DIY portfolio	Alternative: Advised portfolio
30% Growth assets	50% Growth assets
4.3% p.a.	5.7%
$152,936	$174,575
Lee's DIY portfolio delivers a 1.4% lower return, which leaves him almost $22,000 worse off over a 10 year period	

Based on an initial $100,000 balance, after 10 years Lee might have $152,936 in the more conservative portfolio versus a balance of $174,575 for the advised portfolio.

By investing in a DIY portfolio, Lee could be $22,000 worse off after a decade.

In periods of steadily rising markets, it can be easy for people to underestimate the value of a professionally-run portfolio . The danger, however, is that a DIY allocation will drift away from its initial position.

A more disciplined approach to portfolio management by advisers can ensure the original intent is maintained and the asset allocation remains appropriate for an investor's stated needs.

This example is provided for illustrative purposes only.

TAKE A SHARPER LOOK AT COMMUNICATING THE VALUE OF YOUR ADVICE

Actions you can take

- ☐ Spend time articulating why getting the right asset allocation can be a key driver of achieving goals and the consequences of getting it wrong.
- ☐ Remind clients of the art and science of understanding true risk preferences.
- ☐ Use your investment philosophy to demonstrate how you select and implement an appropriate asset allocation to achieve their goals.

[3] ATO, SMSF quarterly statistical report March 2023

B IS FOR BEHAVIOURAL COACHING

More than ever, advisers are helping clients navigate the emotional side of their financial affairs as much as the technical aspects.

A series of unexpected events over the past five years – including COVID-19, the Ukraine war, US banking crisis and surging interest rates – have tested nerves time and again as market volatility pushed the values of portfolios temporarily lower.

After all, it is less than 20 years since the global financial crisis (GFC) rocked markets and its impact remains etched in the memories of many people.

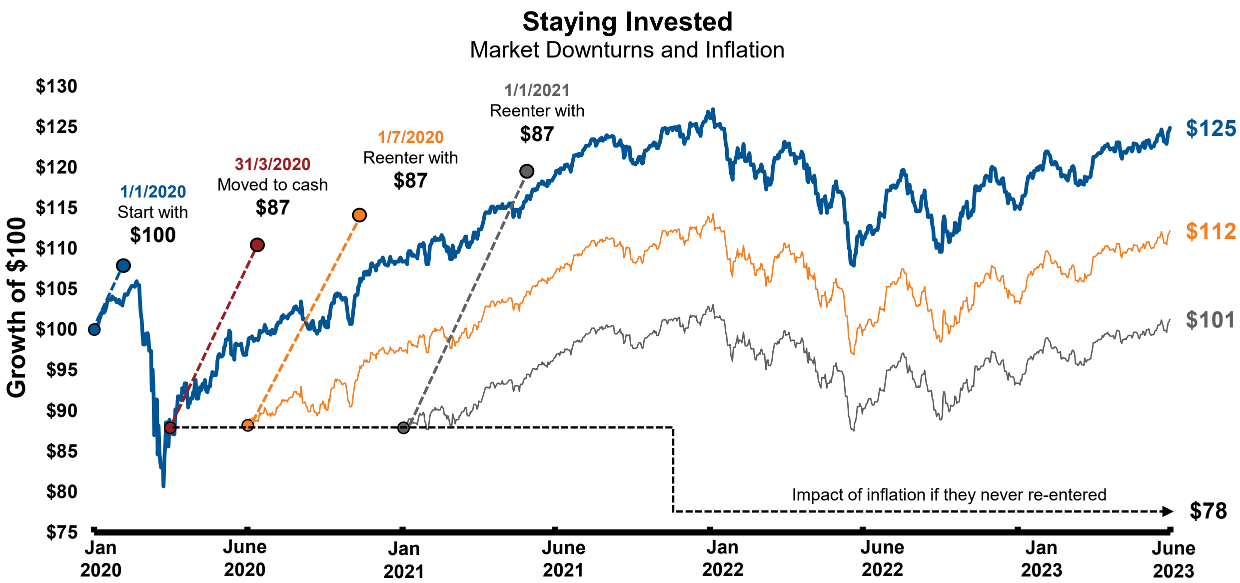
Advisers, however, have played a crucial role in ensuring people understand that both the GFC and COVID-19 proved the adage that an investor with a properly constructed portfolio can weather such extreme periods of volatility.

It's a lesson that has proved crucial even in a period during which official rates have risen from emergency lows to today's 11-year high. Many investors are learning for the first time that high inflation erodes gains from cash investments to push real returns lower.

Inflation magnifies indecision

Consider the journey of four hypothetical investors who each invested $100 in January 2020 but reacted differently to the market downturn triggered by COVID-19 in March that year.

- **Fiona** remained in the market and witnessed her $100 investment rise to $125 by June 2023 (blue line in the chart below).
- **Muhammad** instead moved to cash in March 2020 after his $100 fell to $87, re-entering the market three months later. His ultimate investment was worth $112 in June 2023 (orange line in the chart below).
- **Paloma** also moved to cash in March 2020 but waited until the following New Year to re-enter the market. Her investment was worth $101 in June this year (grey line in the chart below).
- **Craig** was worse off still – he also bailed into cash in March 2020 and has never re-entered it. The $87 he initially moved to cash is now worth just $78 in real terms due to the impact of inflation.



Source: Bloomberg. Balanced Portfolio: 35% ASX300 TR Index, 35% S&P 500 TR Index (Half Hedged), 15% Bloomberg AusBond Composite 0+ Yr Index & 15% Bloomberg Aggregate Bond Index.
As of 30 June 2023.

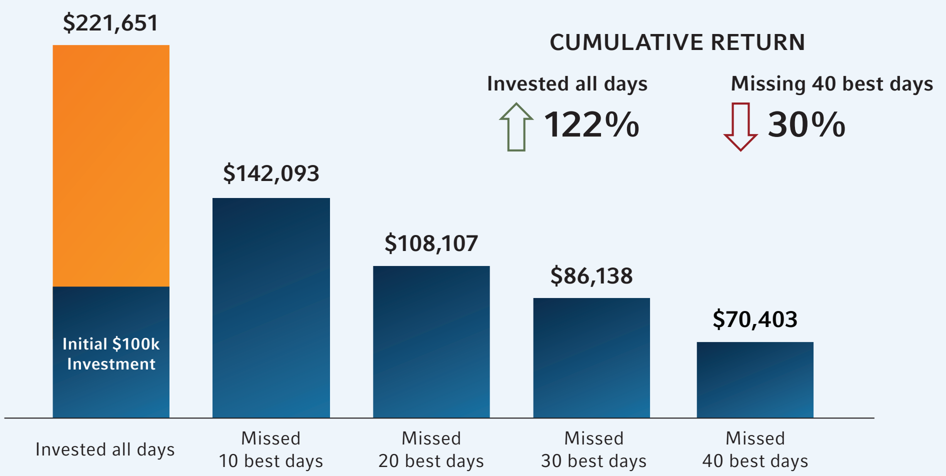
As the graph below shows, missing out on even a handful of the market's best days can have a real impact on the amount of capital that someone can accumulate over time. This counterintuitive result occurs because markets, while unpredictable, have a history of rising over the long term.[4]

In fact, investors who remained invested in the S&P/ASX300 Total Return Index throughout the past 10 years built significantly more capital than those who missed just the 10 best days' performance of the index in that period.

And those who missed the best 20 days wound up more than 50% worse off than if they had remained invested for the full decade.

THE INVESTMENT IMPACT OF MISSING BEST MARKET DAYS

10 years ending 31 August, 2023



Source: Morningstar. Returns based on S&P/ASX 300 Index, for 10-year period ending August 31, 2023. For illustrative purposes only. Index returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment. Indexes are unmanaged and cannot be invested in directly.

[4] https://russellinvestments.com/us/blog/bulls-vs-bears-2

A = 1.2% | B = 3.4% | C | E | T

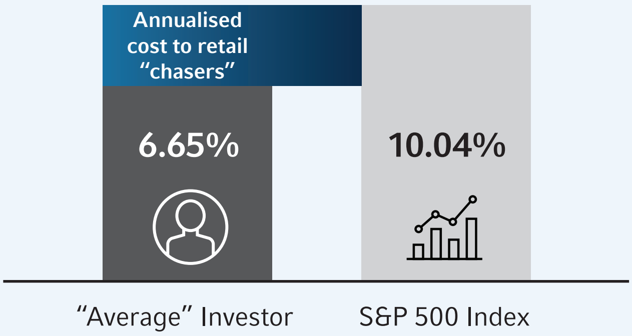
Without the guidance of advisers, investors can fall into the trap of buying when markets are bullish and selling when sentiment turns bearish. There is real value in the ability of advisers to help clients maintain their long-term strategies in the face of unnerving volatility.

In another example, calculations show that regularly increasing or decreasing exposure to the US S&P500 Index might have cost investors as much as 3.39% in returns in the 20 years to June 2023.

Advisers who forge solid relationships with clients are best placed to convince them of the merits of maintaining the positions that underpin the financial strategies they formulate on their behalf.

ANNUALISED RETURN

20 years ending June 2023



Source: "Average" Investor - Russell Investment Group, Refinitiv DataStream. Return was calculated by deriving the internal rate of return (IRR) based on ICI monthly fund flow data which was compared to the rate of return if invested in the S&P 500 Index and held without alteration from 1 July 2003 to 30 June 2023. This seeks to illustrate how regularly increasing or decreasing equity exposure based on the current market trends can sacrifice even market-like returns. Indexes and/or benchmarks are unmanaged and cannot be invested in directly. Example provided for illustrative purposes only. Returns represent past performance, and are not a guarantee of future performance, and are not indicative of any specific investment.

TAKE A SHARPER LOOK AT COMMUNICATING THE VALUE OF YOUR ADVICE

Actions you can take

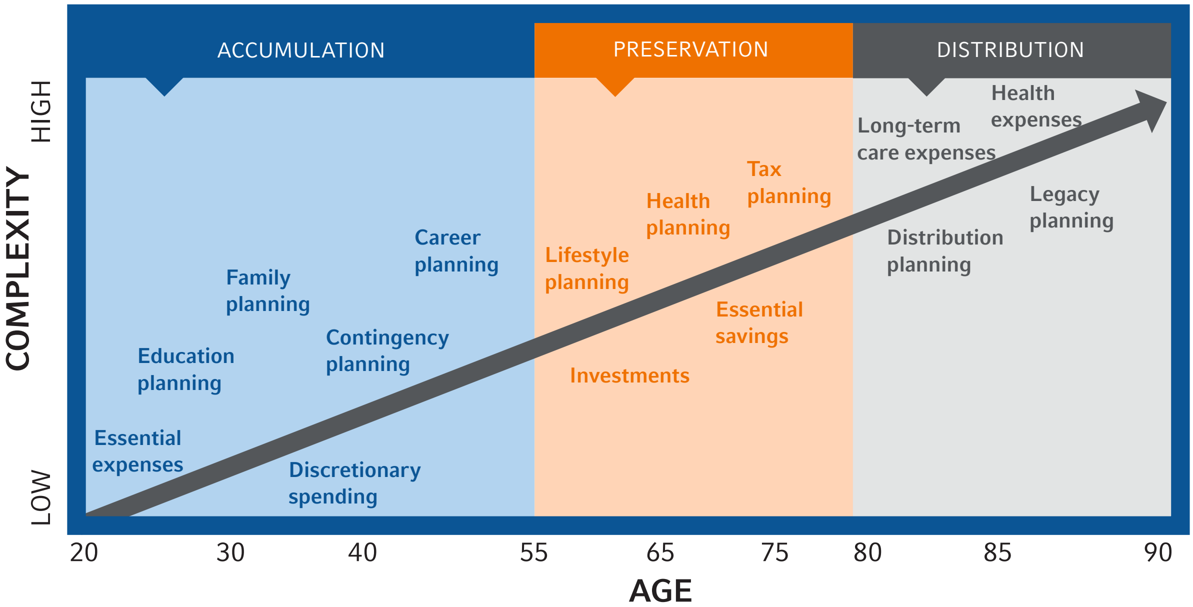
- ☐ Use a consistent framework for review meetings around when to and when not to make changes to a client portfolio.
- ☐ Develop a proactive client engagement plan for different client types and different scenarios.

C IS FOR CHOICES AND TRADEOFFS

The role of advisers as financial coaches whose work extends beyond the selection of investments to holistic wealth management is not always understood. However, the growing complexity of regulation, family situations and social security means it is increasingly invaluable.

The inputs into this advice changes as clients age and go through typical life stages, from early adulthood when they are accumulating assets to late middle age when other considerations come into play and, finally to older age when their affairs take on an added dimension.

More people will fall into the latter category over next 40 years, with the 2023 Intergenerational Report forecasting the number of Australians aged 65 and over will more than double. Those aged at least 85 are forecast to more than triple and the number of centenarians is expected to increase six-fold.[5]



Source: https://russellinvestments.com/us/blog/customized-experience

All this means the financial affairs of a broad cross section of the community encompass many choices and trade-offs that previous generations didn't always face. For example:

- The so-called "bank of mum and dad" has grown rapidly as adult children ask parents to fund mortgage deposits
- Grandparents are more often funding school fees as the cost of private education extends beyond the reach of parents
- Second marriages can add an extra layer to estate planning, particularly to provide for two sets of children
- The so-called sandwich generation must juggle the financial and emotional needs of ageing parents with those of their own children
- Older parents are sometimes asked to provide an early inheritance to adult children or grandchildren to supplement their income
- Older singles have a broader range of retirement funding options to consider, including downsizer contributions to superannuation.

Each of these scenarios can require detailed arrangements to make sure no party is at a disadvantage that could derail their financial future or fracture family relationships. Advisers are an important link in this planning by offering, for example, assistance in striking loan agreements for parents providing mortgage deposits to adult children. By working closely with other specialists such as lawyers and accountants, they can develop solutions which protect the interests of clients.

This process includes explaining implications which a lay person may not contemplate, helping to avoid situations in which important decisions are put aside or made incorrectly.

Even if the above scenarios are not applicable, each client has their own unique **circumstances**, **preferences** and **considerations** which require innumerable decisions over a lifetime.

PERSONAL CIRCUMSTANCES

In the accumulation phase, individuals tend to plan for major life events like establishing a career, buying a home, or raising a family. These priorities change as they enter the preservation stage before retirement and their own health or elderly parents become a bigger consideration. Finally, the distribution phase can involve decisions related to long-term care or creating a legacy.

PERSONAL PREFERENCES

Each individual has personal preferences that must be integrated into financial decisions. These may include a preference for lower or higher investment risk, for low-cost investments or for ESG products. Advisers can suggest appropriate options and also explain any trade-offs required to implement those decisions. For example, they can help price-conscious investors understand that passive investments may be in conflict with ESG principles as a result of the make-up of an underlying index – and, of course, suggest alternative strategies which may achieve their underlying objectives.

EXTERNAL CONSIDERATIONS

External considerations can impact a wealth strategy as much as personal preferences. In 2023, this is clearly seen in the rising interest rates and high inflation that is forcing people to reconsider their financial situations. It is also evident in the ageing population – in terms of both social security for the elderly and inheritance events for younger generations. For the former, advisers can ensure elderly clients take advantage of available benefits such as the Commonwealth Seniors Health Card. And for those who inherit assets, an adviser's role is to help manage those assets and minimise any tax impacts that arise.

TAKE A SHARPER LOOK AT COMMUNICATING THE VALUE OF YOUR ADVICE

Actions you can take

- ☐ Can you articulate your Unique Value Proposition and the services you provide?
- ☐ Do you provide clients with a roadmap of how you will work with them to address their specific needs?

[5] Intergenerational Report Factsheet

E IS FOR EXPERTISE

Advisers are more than financial technicians. They are also specialists in human behaviour who build trusted relationships with clients that allow them to deliver on their recommendations.

In the best of times, advisers help clients achieve life-long goals and celebrate personal milestones along the way. But they also support people in challenging times – through trauma, illness, financial crises, job loss and death.

The unique combination of technical skill and emotional expertise demonstrated by advisers provides a priceless form of value to their clients.

In terms of technical expertise, regulatory change and product innovation are constants in the Australian financial system. Advisers are at the frontline of interpreting change to determine both the impact and, of course, opportunities for clients.

This is a real responsibility due to the level of financial literacy among Australians. A 2021 survey conducted as part of the federal government's Financial Capability Strategy found Australians scored 68 out of 100 in terms of financial literacy[6]. There is an obvious need for improvement and advisers can help bridge the gap.

Retirement planning

Retirement planning is one example where professional advice adds considerable value. Legislative change and product innovation are quickly broadening the decisions both pre-retirees and retirees must consider as they age. The impending retirement of the majority of the Baby Boomer generation means more people than ever must establish income streams, make aged care decisions, and undertake robust estate planning.

But each of these decisions is not just financial – it involves a multitude of emotions as people leave the workforce and plan their final decades.

The empathetic adviser

The same applies to Australia's complex social security system. The benefits available provide not just financial support but also the emotional security drawn from a government safety net. By ensuring clients access legitimate entitlements such as childcare rebates and the age pension, advisers are helping people when they are most vulnerable.

As a result, technical skills only get part of the job done – the ability to engage with and gain the trust of a client is critical to a successful relationship and achieving the best outcomes. This is where advisers draw on their essential interpersonal skills like empathy, caring and genuine curiosity.

17%

of Australians are not very confident or not confident at all about their ability to hit a financial goal

45.3%

Less than half of Australians agree or strongly agree they have a financial plan for retirement

33%

of Australians find dealing with money stressful or overwhelming

Source: Australian government national financial capability survey 2021

[6] Australian government national financial capability survey 2021

Problem-solving practitioners

Elsewhere, understanding financial markets and portfolio construction is key to advisers' training and experience. Advice teams are consistently researching investment solutions by decoding technical terminology to determine what is appropriate for different clients.

The value of working with an experienced adviser is about tapping into the accumulated expertise they've developed over their career. Together with ongoing education, this insight grants them problem-solving skills that can be leveraged by clients at all stages of their lives.

The adviser's role

Through the best and worst times of a client's life, as their needs evolve, an adviser can act in many different roles.

Guide

A trusted adviser can help manage both the practical and emotional burden of decision-making to clients who may overwhelmed by their financial affairs. For other clients who opt for control, advisers can act as a coach, or sounding board, who provides support to the person and their family.

Guru

In many circumstances, an adviser is both an expert and voice of reason. This includes disseminating knowledge that can improve a client's understanding – and also imparting the objective wisdom gathered during a career.

Gladiator

If needed, an adviser can be an advocate on a client's behalf. This could mean challenging a refused insurance claim, chasing beneficiary payments, or managing administration of finances. In all instances, it allows a client and their family to focus on what is important to them.

TAKE A SHARPER LOOK AT COMMUNICATING THE VALUE OF YOUR ADVICE

Actions you can take

- ☐ Have a clear value proposition, advice philosophy and service model that helps illustrate.
- ☐ Have existing client case studies that highlight how elements of your expertise helped them and the outcome you delivered. Share these with new clients to understand some of the intangible value you deliver.
- ☐ Understand the different motivations for seeking advice and have examples to use with new clients on how you deliver sometimes intangible yet appreciated value.

T IS FOR TAX SAVVY PLANNING AND INVESTING

Tax knowledge is as much part of an adviser's role as a grasp of markets or estate planning. In fact, the importance of tax know-how becomes more critical every year.

This is perhaps most obvious in superannuation due to the continued introduction of caps designed to limit the amount of capital that people can hold in tax-effective retirement funds. But it is equally important outside superannuation, in both investing and social security.

Russell Investments believes the value of tax savvy advice is at the least the sum of:

- **Asset allocation**
  optimising assets across superannuation, investment bonds and other tax structures.
- **Asset implementation**
  delivering tax-effective investment strategies and maximising tax benefits.

According to our calculations, the total tax benefit that advisers can deliver is around **1.3% per annum.**

Super-charged retirement

Salary sacrifice is one of the most potent tax-effective investment strategies advisers can implement across a majority of their working-age client base.

Consider Natasha as an example. Her salary is $85,000 and if she sacrifices $5,000 to super, she will pay $750 in contributions tax instead of $1,725 in income tax.

This means an additional $975 is invested in her superannuation fund, providing an initial boost that will increase the power of compounding too.

For older clients, transition to retirement strategies can deliver real benefits by allowing people to add extra to super without reducing their take-home pay. But such strategies can prove complicated for individuals to arrange without the help of an adviser who has a working knowledge of all the requirements.

And, for those with a higher super balance, alternative vehicles such as investment bonds and company structures are an option worth considering as the proposed implementation of an additional tax on earnings on super balances above $3 million draws closer.

Advisers can walk clients through these sometimes complicated alternatives – explaining both the pros and cons – and undertake any implementation on their behalf to ensure it is completed in an optimal fashion.

This example is provided for illustrative purposes and is based on 2023-24 income tax rates.

Beyond Super

Outside this planning, advisers can provide expert guidance on a range of tax-related matters such as:

- Investment solutions which use low turnover strategies, tax minimisation overlays or centralised portfolio management
- Insurance strategies which allow clients to hold polices in super, thereby providing tax benefits that can be reinvested
- Entitlement to social security payments such as the Child Care Subsidy, Family Tax Benefit and Parental Leave Pay
- Eligibility for seniors' benefits such as the Age Pension, Commonwealth Seniors Health Card and Home Equity Access Scheme
- Small business grants and incentive payments.

Getting it right

Individuals can easily be wrong-footed by tax rules and face penalties for decisions that advisers would foresee – and prevent.

The fact that only 12% of people consider overall tax effectiveness as among the top three considerations when making investments[7] further highlights the crucial role advisers can play in guiding clients to better wealth outcomes.

Indeed, tax is not just the realm of the accounting profession and not limited to the items included in an individual's tax returns.

By reinforcing these key points to clients, advisers have a significant opportunity to establish their credentials as invaluable service providers over the entire lives of customers.

TAKE A SHARPER LOOK AT COMMUNICATING THE VALUE OF YOUR ADVICE

Actions you can take

- ☐ Know each client's marginal tax rate, tax sensitivities and opportunities.
- ☐ Provide access to solutions that have tax-savvy strategies for your clients.
- ☐ Explain the different tax-smart decisions you include in your advice and ongoing implementation.

[7] ASX Australian Investor Study 2023

COMMUNICATE YOUR VALUE

Continued economic uncertainty and geopolitical tension provide an ideal time for advisers to reassess the full value they offer to their clients – and to articulate it to them clearly.

This is the premise behind Russell Investments' simple Value of an Adviser formula. It was developed to allow the industry to demonstrate the many facets of the services it offers in an at-a-glance format for the lay person.

Many advisers have worked with clients during recent market volatility to help them stick to planned investment strategies and navigate other areas of their financial affairs. The Value of an Adviser formula shows that even if advisers were only able to help people avoid common behavioural mistakes, they have likely provided value above and beyond their fees.

But once their other services are included – asset allocation, expertise, and tax planning – the total value of advice is clearly significant.

Russell Investments' easy-to-understand equation is calculated as follows:

A is for appropriate asset allocation: **1.2%**

\+

B is for behavioural coaching: **3.4%**

\+

C is for choices and trade-offs: **Variable**

\+

E is for expertise: **Priceless**

\+

T is for tax savvy planning and investing: **1.3%**

= at least **5.9%** — the value of your advice in 2023

FOCUS ON THE VALUE YOU PROVIDE

At Russell Investments, we believe in the value of advisers. And the numbers back up our belief. We see the potential advantages you create for your clients. We know the commitment you bring to your relationships. This annual Value of an Adviser Report quantifies that dedication and the resulting benefit.

Visit our website to see our range of tools and resources designed to help you engage and build trust with your clients, including a client version of this report.

Scan the QR code or visit russellinvestments.com.au/clientresources

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ADDITIONAL DISCLOSURES

The value of Appropriate Asset allocation is based on 5 portfolios with average asset allocations across Conservative, Diversified 50, Balanced, Growth and High Growth risk profiles. The value takes the difference of 10 year annualised performance of each adjacent risk profile, and calculates the average overall. These portfolios use index values as asset class exposures, including Australian equities: S&P/ASX 300 TR Index AUD, International Equities: MSCI AC World TR Index AUD, MSCI AC World ex Australia NR Index (AUD Hedged). International Bonds: Bloomberg Barclays Global Aggregate TR Index. Australian Bond: Bloomberg AusBond Composite 0 Year Index AUD. Example is provided for illustrative purposes only. Real returns may vary. Past performance is not a reliable indicator of future performance.

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