

## COMMENT

# In defence of investment advisors

*Many retail clients lost significantly less than did institutions and stock market indices*

■ BY IAN RUSSELL

**T**HE RECENT FINANCIAL crisis has resulted in a sharp and sudden drop in financial asset prices. Equities' prices, as measured by the S&P/TSX composite index, fell by an average of 45% from last August to early March before financial and economic conditions improved and markets rebounded in April and May. Investors did not anticipate the scale of this market collapse. Their shock at the size of the market decline has been palpable.

Despite the sudden drop in share values, individual Canadians have, on balance, been well served by their financial advisors, who have guided their clients through unprecedented conditions. The typical losses in individual portfolios, from September 2008 through March, were on average less than the 45% drop in the composite index. Many individual portfolios performed better than the managed portfolios of large pension funds last year, mainly because of sound portfolio diversification and less exposure to exotic financial instruments.

Although most investment advisors didn't see this crisis coming, neither did most investment managers, regulators and central

bankers. Those who did had been warning of the consequences of excessive leverage and derivative risk for several years; the timing of the crash, however, was predicted by few. Moreover, investors who followed the naysayers' advice and moved into cash earlier in the decade would have missed out on the substantial rise in Canadian equities markets in 2005-07. Although most clients have not blamed their advisors for failing to predict the crash of 2008, advisors are responsible to advise their clients through the financial crisis and its aftermath and, for the most part, have discharged these responsibilities effectively.

Individual Canadians advised by advisors registered with the **Investment Industry Regulatory Organization of Canada** have generally avoided the worst of last year's losses and are now well positioned to benefit from a significant market rebound. This reflects the conservative approach taken by IIROC advisors, who understand their client's financial position and investment goals.

Most clients have been invested in diversified portfolios, with appropriate allocations to cash and conventional debt securities. Equities portfolios have been properly balanced,

with significant holdings in liquid, dividend-paying large-cap stocks and modest amounts of less liquid, speculative securities, depending on the client's risk tolerance. Unlike the institutional investment funds that suffered substantial market losses, individual portfolios held minimal amounts of unconventional and illiquid financial assets. As well, many investors were counselled by their advisors not to sell severely undervalued securities late last year, as their portfolios were defined with long-term investment horizons. In the past two months, as equities markets rebounded and the composite index rose by 32% from the March lows, many investors have recouped a significant portion of recent portfolio losses.

Brokers are held to a high professional standard. They must ensure their clients are fairly and properly treated, particularly in terms of disclosure and recommending investments suitable to their clients' investment goals and risk tolerance. These advisors must also meet stringent proficiency requirements involving formal and extensive training programs and ongoing continuing education. Every client complaint must be examined for possible investigation, and every client can seek redress and restitu-

tion for market losses through his or her brokerage firm and also through the Ombudsman for Banking and Securities Investments, whose office reviews and judges the merits of such complaints.

The small number of serious client complaints relative to the number of transactions substantiates the reasonably good performance of most individual portfolios advised by advisors. The number of client complaints last year totalled about 2,000. While client complaints were up by roughly 40% from 2007, and early signs indicate a higher number this year, complaints are relatively few compared with the eight million retail accounts at investment dealers and the total volume of some 70 million transactions last year alone.

The reputation of the majority of advisors that do a good job catering to the interests of their clients will inevitably be tarnished by a few "bad apples." However, IIROC moves quickly to investigate and punish brokers who have contravened the principles, rules or regulations governing professional financial advice. The regulatory infractions of each and every advisor are published on the IIROC website and accessible to all investors.

Clients also have responsibility in

the investment process. They must understand the professional relationship with their advisor, provide and update all relevant information affecting their investment objectives and risk tolerance, and review their accounts on a regular basis. Clients need to feel comfortable with their advisor, in terms of investment style, communication, service and fees, and should be prepared to move to the advisor best suited to their needs. Clients who fail to take these responsibilities seriously, or who furnish inaccurate or incomplete information, risk getting advice that is not appropriate to their needs and requirements. Clients who override their advisor's advice are also responsible for such investment decisions.

Unlike south of the border, Canadian institutions have overall been well managed and individual investors well served. As the financial position of Canadians improves, investors will recognize the positive contribution of their advisors in shepherding them through this unprecedented financial crisis.

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