Regions Wealth Podcast

Episode 17: Digital Advisor or Human Advisor: Which is the Right Option for You?

With the rise of self-directed investing platforms, it can be tempting to take portfolio management into your own hands. But are robo-advisors an effective stand-in for human advisors? And how do you know which option is the right one for you? Chief Investment Officer Alan McKnight joins us to discuss the pros and cons of digital advisors vs. investment advisors, and how to determine which one is right for your goals and portfolio.

Episode Transcript

Sarah Fister Gale:

Welcome to Regions Wealth Podcast, the podcast that tackles life's challenges with financial experience. I'm your host, Sarah Fister Gale. With the rise of self-directed investing platforms, it can be tempting to take portfolio management into your own hands. But are robo-advisors an effective stand-in for human advisors? And how do you know which option is the right one for you? Joining me remotely is Alan McKnight. He's the Chief Investment Officer for Regions Wealth Management. Alan, thanks for joining us today.

Alan McKnight:

Thank you for having me.

Sarah:

In this episode of Regions Wealth Podcast, we're discussing robo-advisors and *human* advisors, and how to determine which option is right for your investment goals. We've taken some taken frequently asked questions and developed a character who needs your help. Let's listen.

Johann:
"Hey. My name is Johan and I'm an internet entrepreneur. I got into investing in college and I guess I've done pretty well for myself. I started off reading all of these investing forums and basically taught myself how to trade. I did better when I had more time on my hands, but, you know… when I launched my business a few years ago, things just got too busy, so I switched over to this robo-advisor my friend recommended."

Sarah:

So Alan, let's talk about robo-advisors — which are sometimes referred to as "digital advisors". For those who may be unfamiliar, what are they and how do they work?

Alan:

So a digital advisor attempts to replicate what you would see in an in- person advisor or wealth advisor, whereby the digital advisor will ask questions regarding your risk tolerance, objectives, and goals, how you feel about draw-downs and volatility. And the best analogies is one of a travel site, such as Expedia whereby you have a comprehensive set of questions around hotel, plane, rental car, all those various pieces. And they try to tie that all together to better understand you. And that really is the delivery mechanism for the digital advisor: taking much of what you would have in person and via a real life or in-person discussion and applying it online.

Sarah:

I love that analogy. So if using a robo-advisor is akin to using an online booking site like Expedia which makes recommendations based on your travel needs, how would traditional self-directed investing fit into this travel analogy?

Alan:

To extend the idea of the travel experience, conversely you can go out and build it yourself. Or as I like to describe, the “build your own adventure”. So on self-directed investing, you would go out and you would decide whether you needed a bond fund or a stock fund, how much risk do you want to take? How much are you going to pay? And so the difference is really threefold. One, you have discovery, which is understanding the investment profile, your risk tolerance and objectives. Two is on transparency. On a digital advisor, you know exactly what you're paying versus in the self-directed program. It may take more time and understanding to find out, what are my costs and fees?

And then finally on frequency. With a digital advisor, you'll have the opportunity to have your portfolio rebalanced. You'll have a common set of questions and concerns as you go along that you're able to interface with versus self-directed, again in the “build your own adventure” model where you're just picking up each piece of it. It really is on you to determine that rather than on any of your self-directed investments.

Sarah:

So you’re saying that traditional self-directed investing is sort of like travel planning pre-internet? You’re going out and gathering travel guides, doing the research, figuring out where you want to stay, and booking the hotel yourself. That’s a great comparison. Now, let’s talk about what it’s like to work with an advisor. What are the benefits? And what aspect of the investing process would they manage for you?

Alan:

If you are looking to deliver a plan over time, and you are looking to ensure that you will meet your goals over that time period, there may be different levers depending on if you own a business, or if you are a caregiver to elderly family members, or if you're in the middle of retirement. All of those things are critical to understand and what that may mean for your cash flows, your risk tolerance. And by having an advisor, you can develop a comprehensive plan that meets those needs.

Sarah:

So the advisor might know things about you and offer more custom advice than a robo-advisor who you haven't given that information to?

Alan:

That's exactly right. So the robo-advisor can only ask so many questions, and they're great questions. And they provide as much information as possible in a limited amount of time with a limited set of user interfaces. So if you go through 10 or 12 or 15 questions, it will get a lot of information from you. But the reality is, even with quite a bit of technology, you're never going to catch all of the nuances of, "Oh, you hadn't mentioned before that you're the caregiver to your elderly father. Are you going to have to fund that at some point? Is he funding it today? What do you think about having to pay for your children's college? Is that something you definitely want to do? Is it a possibility? May that change if you decided to no longer work in the future?" So those are the types of nuanced questions that really build off of the dialogue initially. And the digital advisor just isn't set up for that. It delivers transparency, it delivers discovery, but it's going to be in a much less extensive way.

Sarah:

That’s a helpful way to differentiate it! So, let’s go back to Johann and learn a bit more about his individual situation.

Johann:

“...I check my investment account every month or so, but I really don’t have the time to devote to managing it. Right now, things are OK with my portfolio, but I’d like them to be better. I’ve got a pretty aggressive retirement goal — I want to retire at 50. I’m 36 now, so ya know, if I wanna hit that goal, I need to make sure things are on track.”

Sarah:

So Alan, when someone has a very clear — and in Johann's case, fairly aggressive goal that they'd like to reach, should they be working with an advisor? And if so, why?

Alan:

Working with an advisor is really about preference and the ability to meet your long term goals. It comes down to the ability to discern, what are you hoping to achieve? Is it reasonable to meet your goals in the time period that you have ascribed? And understanding what the trade-offs are. Because everything in investing is about trade offs. If you'd like to retire in 14 years, then you need to have a very sharp focus on how much do I need to save? What do I need to cut in terms of expenses? And what does it look like at age 50 when I do retire? Do I have the same standard of living? Do I have a different standard of living? And that really comes back to this. Working with an advisor can hopefully flesh that out because over time and as you age, the trade offs you have today may look different than the trade offs you have tomorrow. The more you can catalog all of those and have them available to you and have that discussion, even if it's more challenging and quite honestly, that can be one of the best benefits of working with an advisor is having someone to challenge you on what you've envisioned as your goal and how you arrive at that goal.

Sarah:

So can you get the same kind of guidance and challenge from a robo-advisor?

Alan:

You can certainly get the initial stages of that, certainly versus self-directed whereby you're going to have to go out and do the research on your own. But as it relates to a full service advisor, you may lose a bit in translation as it relates to the nuances of your life and the critical elements of how you look at this money and how you want that money invested. Having a dialogue about it can really provide more information. If you have a primary physician, they're just going to know more over time about you. It doesn't mean that there's not still value for the earache that you experienced after being in the pool for the day and you need to go to urgent care. But you're just never going to get the same level of engagement, but there's still value there. And it's really about that preference because you may not want any more than that.

Sarah:

Great! Let's take a listen to the final portion of Johann's story.

Johann:

"...My dad's constantly bugging me to get an advisor, but I'm not sure if that's the right move. No offense or anything, but I don't want to deal with some old-school type coming in and trying to tell me what's what. I know that's probably a bad stereotype, but it's still my concern. Also, aren't advisors just for super wealthy people? My portfolio is in the mid six-figures so, you know, it's pretty decent, but I don't want to get assigned to some guy who's going to just give me the brushoff because I'm not a millionaire. Doing the robo-advisor thing has been ok, but I guess I could do better. I'm just not sure if an advisor is right for me."

Sarah:

So Johann has this notion that you have to be ultra wealthy to have an advisor. Is this true?

Alan:

Definitely not. Although it's a common misperception because folks see the advertisements, they hear about the folks who have advisors, who are a part of that ultra wealthy contingent.

The reality is that everyone can utilize an advisor and it's just a matter of what that interaction looks like. And it may mean that that interaction is on a very limited basis, whereby you're trying to get a first blush at financial planning. You want to understand what could this look like over the next five or 10 years? And the day to day interaction is much less so. And I think over time, what most investors will find is that you may require a different type of advisor over time, depending on your current lifestyle and life cycle of where you are in life. If you're young and you're single and you're just starting the savings and retirement planning process, that's going to look different than the individual who is close to retirement and has a very different set of needs and a very different set of levers to pull around ensuring success over the longterm. And what we would advise to all investors is do the work upfront, understand what that looks for you. And even down to the point of what type of advisor, what type of interface.

Sarah:

Johann is concerned about getting the brush off. How can he know that his advisor has his best interests in mind?

Alan:

The first way to know is that the advisor is acting as a fiduciary, which just means from a legal or regulatory basis, that that advisor is practicing the highest standard of care, that they are sitting on the same side of the table as the client to ensure that they meet their needs and solutions. Number two is that that advisor is proactive and the advisor is going out and reaching out to provide new information, to ask questions, to understand, have things changed in the portfolio or on a life basis or life events that are occurring along the way.

Sarah:

Terrific. And so at a high level, can you run us through all the things that advisors should be doing for their client?

Alan:

Certainly. So it starts with the foundational element of knowledge and understanding what their balance sheet looks like, the assets and the liabilities, to ensure it's a holistic plan. The advisor should then better understand what the goals of the client would be, how much risk can they take on to ensure they're going to meet those goals. And probably most importantly, that they're challenging the client on the way in which that will occur: what levers need to be pulled, and if that client wants to start a business or buy a home, or needs to provide care to an elderly family member, what things need to be modified in that portfolio. If the advisor's doing their job well and acting as a fiduciary and providing that, you'll have a great relationship and you'll build longterm success.

Sarah:

Excellent. So Johann touches on a fairly important point here: the importance of choosing the right advisor. Obviously he's someone that likes to have an active role and wants to work with someone who will respect that. What questions should individuals ask when choosing their own advisors?

Alan:

The critical component for choosing an advisor comes down to those questions upfront, like selecting so many service providers. It's really understanding how you want to be treated, what that looks like for you. And some of the questions you can ask are one, how many clients do you have? How much time do you spend with those clients on a regular basis? Is that more phone call? Is it in person? Understanding and envisioning the working relationship — so if he has a preference for a dialogue every week, does that meet with the advisors expectation? Is it email form? Is it a blast? What does that really look like? And finally and probably the most important of all the questions is around, “what do you see as challenges to my goals and objectives?” So if he wants to retire in 14 years, having a real difficult conversation up front will be critical. And you'd rather have that advisor lay those out. What could go wrong? How could this not work out? It's very easy to see the positives and the silver linings and to say, of course, you're going to make this work. Of course, you're going to reach your goal. But you’re really doing a disservice and so the more he can ask those questions up front to really glean what the relationship will look like, will he have the most success.

Sarah:

So Alan, how important is it for investors to build a relationship with their advisors, so they feel comfortable sharing some of those personal details about their life?

Alan:

We think it's critical because it builds that confidence level to understand what's important to the investor. How can they ensure that they will meet their goals over time, if they're going to find success in their investment program? And that is a multi-part, multi-year environment, whereby both sides of the table are working together in concert to ensure that those needs are being met and in a way that is viable, realistic for both sides. And what I mean by that is someone may be able to take on an undue level of risk, but realistically and psychologically, they're not comfortable doing that. You'll find that out over time, as that confidence is built, as the relationship is built. And it truly becomes a team orientation, both on the same side of the table, and as advocates rather than solely with the focus of going from point A to point B.

Sarah:

That’s an important reminder: your advisor should be someone who’s sitting on the same side of the table with you. So Alan, at the end of each episode, we like to ask for a few key takeaways for our listeners. What would you like to share with them?

Alan:

Number one, we believe it's critical to stay the course and we recognize and appreciate, acknowledge that that's not easy to do. We know that in difficult times and difficult market environments like we saw during the tech bubble, the global financial crisis, and most recently with the pandemic sell-off, it's very difficult to stay the course in a plan when you're watching assets drop. When you have additional stresses, as it relates to health, your financial wellbeing, or even your job, those things all come together to make it very difficult, to focus on the longterm and on your plan. But that's exactly why it's so critical to do so. And if you don't have a plan, it's virtually impossible to reach your longterm goals. You may get lucky and it happens, but we want to remove as much luck from the equation as possible, and staying the course is the critical component to that.

The second component, and this is really getting more to communication, engagement, and relationship, is really what Tolstoy talks about at the beginning of Anna Karenina, when he says that, "Happy families are all alike, every unhappy family is unhappy in its own way." And what I believe that means is that happy families, AKA happy relationships, investors working with advisors, have a foundation of communication and dialogue and understanding of what goals are available and achievable and where there need to be challenges. Unhappy relationships at the core don't have that foundational element whereby there's information that's missing, there hasn't been enough work or discovery by the advisor or conversely the investor doesn't feel comfortable in the relationship to provide the full view of the balance sheet, concerns, risk, and thereby there's an unhappiness either on one side or the other that doesn't allow for the highest degree of success. So we think those two are really the key takeaways for all investors, regardless of having $5 or having $5 million or $50 million, those flow through.

Sarah:

Thank you so much, Alan McKnight, Chief Investment Officer at Regions Bank. As always, we appreciate your insights.

Alan:

It was a pleasure to join you today. Thank you.

Sarah:

And thank *you* for joining us today. Each episode of Regions Wealth Podcast covers a different financial challenge, so be sure to check back — and maybe introduce us to a friend you think might benefit from these insights. For more, visit www.regions.com/wealthpodcast.

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