

## Financial advice: A substitute for financial literacy?

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### Abstract

A lack of financial literacy can hamper the ability of individuals to make well-informed financial decisions. For people who exhibit problems with financial decision making, financial advice has the potential to serve as a substitute for financial knowledge and capability. However, data from the 2009 FINRA Financial Capability Survey indicate that advice more often serves as a complement to, rather than a substitute for, financial capability: individuals with higher incomes, educational attainment, and levels of financial literacy are most likely to receive financial advice. © 2012 Academy of Financial Services. All rights reserved.

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### 1. Introduction

Recent studies of financial literacy demonstrate several common themes: First, individuals in the United States and other nations lack numeracy and financial literacy (for a review, see Lusardi and Mitchell, 2007a). Second, scores on financial knowledge measures tend to be lower for consumers with low incomes and low educational attainment (Agnew and Szykman, 2005; Bernheim, 1998; Lusardi and Mitchell, 2007b; Mandell, 2004). In addition, consumers' understanding of interest rates appears to be a particular area of weakness (Moore, 2003). Finally and importantly, people appear to engage in financial behaviors that might be construed as mistakes (Agarwal, Amromin, Ben-David, Chomsisengphet, and Evanoff, 2011; Campbell, 2006).

Studies of financial behavior often conclude that financial education, counseling, and

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advice might help individuals engage in financial practices that support longer-term financial security. Evidence of the effects of financial education programs on behavior is still emerging and remains inconclusive (for a review see Collins and O'Rourke, 2010). A separate line of inquiry concerns the extent to which individuals use financial advice and counseling to mitigate their incomplete knowledge—that is, whether or not people are sophisticated enough to turn to advice to ameliorate their own weaknesses with regard to financial capability. This study examines the ways that financial advice and counseling might serve as a substitute for consumers' inadequate financial knowledge.

There appears to be ongoing demand for financial advising services. The size of the financial advice industry is difficult to estimate, in large part because it is a diverse field. To gain a sense of the industry's scale, it is useful to examine figures on the number of individuals employed as financial advisers.<sup>1</sup> According to the U.S. Bureau of Labor Statistics (BLS), 208,400 individuals were employed as personal financial advisors in 2008. By comparison, the BLS estimated that 317,200 individuals were employed in the securities, commodities, and financial services field and 450,000 were employed as insurance sales agents (Bureau of Labor Statistics, 2010). These fields are somewhat different in that advice is often secondary to the sale of financial products, although most financial advisors also sell or broker financial products, making these distinctions subtle. BLS does not provide employment statistics for financial counselors, but because much of the financial counseling industry is based in non-profit agencies, tax filings offer a snapshot of the scale of the counseling field. Based on 2008 IRS tax form 990 records, about 2,100 nonprofit agencies across the United States are engaged in financial counseling (Collins, 2011). The average agency reported fewer than 10 staff, suggesting that approximately 21,000 people work as financial counselors nationally. Thus, personal financial advisors alone represent a significant set of service providers relative to related fields, and in prior decades the field has grown at a steady rate.

## **2. Prior studies of financial advice**

The literature indicates that personal financial advisors play five main roles: (1) offering information, (2) defusing biases that lead to common mistakes, (3) facilitating cognition, (4) overcoming affective issues, and (5) mediating joint decision making. Stigler's (1961) seminal article introduced the concept of returns to information search. Regardless of their experience and expertise, individuals will stop searching for information when the marginal cost equals the marginal benefit. Hiring an advisor may lower the marginal cost of searching for information relative to searching without assistance. An advisor may acquire expertise on a relatively technical topic and then spread the costs of acquiring that knowledge across multiple clients, each of whom may only need the information once in a lifetime.

Bluethgen, Gintschel, Hackethal, and Mueller (2008) published one of the only articles that provides an economic model of financial advice; they base this model on evidence that consumers often demonstrate significant cognitive errors when making financial decisions. The authors cite Shapira and Venezia's (2001) research on financial professionals, which indicates that financial professionals are less likely to fall prey to the disposition effect

(holding losing stocks too long) than the general public and therefore may help consumers avoid mistakes. In the model put forth by Bluethgen and colleagues, financial advisors add value by identifying and correcting their clients' cognitive errors.

Other studies support the idea that advice improves people's cognition and serves as a complement to low financial capability. Engelmann, Capra, Noussair, and Berns (2009) examine functional magnetic resonance image (MRI) of individuals' brains as they received financial advice. The MRI scans indicated that financial decisions were less taxing on the brain when participants received advice. Fischer and Gerhardt (2007) suggest that financial advisors can be particularly valuable for individuals who lack financial literacy.

A few studies examine how advice can support people as they make decisions in affective or emotional contexts. Haslem (2008) asserts that financial advisors can help clients overcome feelings of insecurity, help validate clients' past decisions, and serve as a neutral party in spousal disagreements. More recently, Haslem (2010) assessed the relationship between financial advisors and investors in light of the current financial crisis; he concludes that advisors can help clients avoid panicking and selling investments under distress.

Haslem (2008) provides one of the only studies to explore the role of advice for households in which spouses or partners may not be able to negotiate joint financial decisions. The advisor plays the role of a third-party mediator who can help couples make decisions collaboratively. In a field study Hung and Yoong (2010) conclude that being married increases an individual's propensity to seek financial advice, consistent with this rationale.

The literature is less clear about whether people who lack financial knowledge or sophistication are more likely to seek advice to make up for their shortfalls. One confounding factor is that knowledge of finance may be correlated with access to financial resources or wealth, and therefore low-resource consumers may be less likely to need or use an advisor. Even prior studies that have controlled for wealth and income, however, have found at best mixed evidence of advice serving as a substitute for knowledge. Hackethal, Haliassos, and Jappelli (2010) find that investors who are less financially sophisticated are least likely to use an advisor. Like other studies, the results revealed a strong positive correlation between advice and wealth levels. Bluethgen et al.'s (2008) analysis indicates that older individuals and women are more likely to access financial advice, which is perhaps a signal of using advice to shore up weaker or atrophying financial skills. Haslem (2008) finds similar patterns by age and gender, as do Gerhardt and Hackethal (2009). Richman, Barboza, Ghilarducci, and Sun (2008), as well as other studies that include race of the client as a control, find that Whites are much more likely use financial advice than other racial or ethnic groups, controlling for wealth and other factors.

Bhattacharya, Hackethal, Kaesler, Loos, and Meyer (2010) conducted an illuminating experiment with a European brokerage bank. Active bank customers were offered a new no-cost financial advice service they could either voluntarily enroll in or decline. The authors conclude that customers who participated in the financial advice service were among the bank's most financially sophisticated customers. However, many advisees did not utilize the advice they received. The authors also find that although returns did not improve for the average advisee, they did improve for the average advisee who followed the investment advice. Further, the authors show that the advice would have been most beneficial for

investors with the least financial sophistication at the start of the study. The authors conclude that investors who could benefit substantially from financial advice are the least likely to seek advice.

Calcagno and Monticone (2011) develop a useful economic model of the market for financial advice, including more and less financially sophisticated clients; their model predicts that advisors seek out and offer valuable information to only the sophisticated investors. Using European household data, the authors empirically show that people with low levels of financial literacy have the lowest demand for financial advice. The results are pessimistic about advisors ever being sufficient to address the needs of households with low financial literacy.

Chalmers and Reuter (2010) study the impact of financial advisors on retirement portfolio choices in the United States among public university employees in one state. Unlike other studies, the authors find that younger, less educated, and lower income individuals are *more* likely to choose to invest through a financial advisor. However, they also find that people using advisors pursue higher return, higher risk investments. The costs of the advice substantially erodes any gains to the investor from using an advisor, resulting in lower overall after-fee returns for clients. These results are similar to those found by Hackethal, Haliassos, and Jappelli (2010) using European data. Mullainathan, Noeth, and Schoar (2012) conducted a field audit of professional advisors in the United States, and found that advisers promote investment strategies with higher fee levels rather than lower-cost strategies, even if clients express a preference for lower-cost approaches. These studies suggest that financial advice might not prove to be a financial benefit in terms of investment returns. However, the widespread use of advisors suggests some revealed preference in the marketplace. It seems likely the impacts of advice extend beyond financial returns to include non-pecuniary factors, especially over longer time periods. Moreover, financial advice can cover a range of topics such as taxes, credit, insurance, and related topics not examined in these studies.

Fig. 1 shows the proportion of the U.S. population that has received some form of financial advice. Elmerick, Montalto, and Fox (2002) conducted a survey for the Certified Financial Planner board; they find that just over 20% of households use financial planners to obtain advice on credit and borrowing, saving, or investing. In the 2007 Survey on Consumer Finances, which asked respondents to identify where they obtain information on borrowing and investing, 29% of the respondents reported receiving advice (Bucks, Kennickell, Mach, and Moore, 2009). Hung and Yoong (2010) use data from the American Life Panel to estimate the take-up of financial advice related to investment and retirement, and found that 18% of respondents reported this type of activity. These estimates of the use of advice range from one-fifth to one-third of the population. Some of this variation is because of the fact that each survey uses a slightly different definition of financial advice, and the surveys were administered at different points in time and to different samples. Despite their differences, these studies all conclude that only a portion of the population uses financial advisors.

The primary focus of this study is analyzing what factors determine who uses various forms of financial advice, and to what extent characteristics associated with financial literacy or capability might be associated with receiving advice. The goal is to estimate the extent to which financial advice is a complement to or substitute for broader financial acumen.

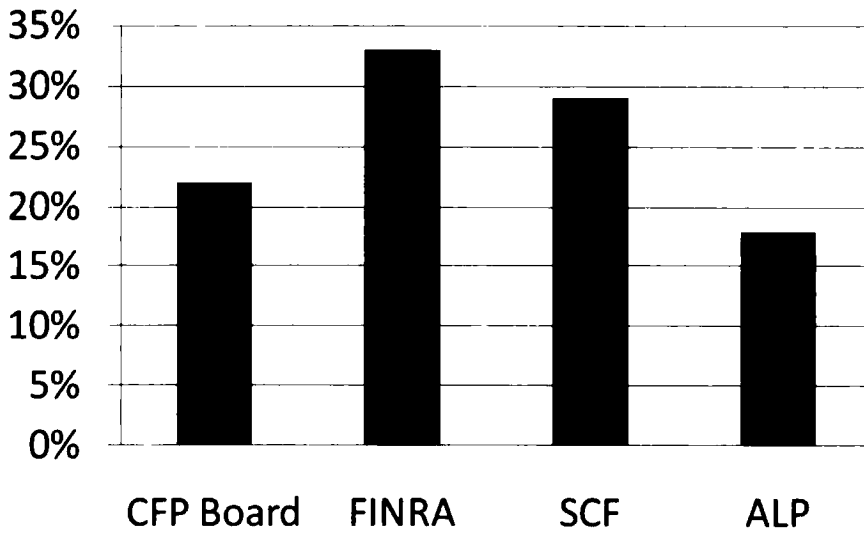


Fig. 1. Percent of respondents reporting use of investment/planning advice by survey source. *Sources:* CFP - Elmerick, Montalto and Fox. (2002). "Use of financial planners by US households." *Financial Services Review* 11(3): 217–231. FINRA - Applied Research & Consulting LLC. (2009). *Financial Capability in the United States: Initial Report of Research Findings from the 2009 National Survey*. 2009 National Financial Capability Study, FINRA Investor Education Foundation. SCF - Federal Reserve Board, 2007. ALP - Hung, A. and J. Yoong. (2010). *Asking For Help: Survey And Experimental Evidence On Financial Advice And Behavior Change*. RAND Working Paper Series WR-714-1.

### 3. Data

The data used to estimate the take-up of financial advice is from the National Financial Capability Study, which FINRA commissioned in 2009. The study included a national sample of 1,488 people, was conducted via a random-digit dialed telephone survey, and over-sampled on selected demographic variables. The dataset provides a reasonable cross section of people in the United States (for more detailed information see: <http://www.finrafoundation.org/>). One item in the survey asked: "In the LAST 5 YEARS, have you asked for any advice from a financial professional about any of the following: 1) Debt counseling, 2) Savings or investments, 3) Taking out a mortgage or a loan, 4) Insurance of any type, and 5) Tax planning?"

Each of the five types of advice was answered as a dichotomous "yes–no." The survey also included measures of three attitudes about financial advisors: (1) "I would trust financial professionals and accept what they recommend," (2) "Financial professionals are too expensive for me," and (3) "It is hard to find the right financial professional for me." Respondents could respond to each of these statements on a scale from 1 to 7, with 1 indicating "strongly disagree" and 7 indicating "strongly agree." The survey measured demographic characteristics, which allows for a general analysis of consumers' take-up of advice, and variation in attitudes toward advisors by gender, age, race, education, income, financial literacy, and negative financial experiences (see Appendix A for more information on variable construction).

#### 4. Empirical strategy

Using an ordinary least squares (OLS) linear probability specification with corrections for heteroskedastic errors, the following specification is used:

$$\begin{aligned}
 Y = & \alpha + \beta_1(\text{gender}) + \beta_2(\text{age group}) + \beta_3(\text{racial group}) \\
 & + \beta_4(\text{education level}) + \beta_5(\text{income level}) + \beta_6(\text{\# children}) \\
 & + \beta_7(\text{owner}) + \beta_8(\text{fin lit score}) + \beta_9(\text{fin lit perception}) \\
 & + \beta_{10}(\text{difficulty paying bills}) + \beta_{11}(\text{large drop in income}) \\
 & + \beta_{12}(\text{regional fixed effects}) + \varepsilon
 \end{aligned} \tag{1}$$

where  $Y$  is the take-up of advice about debt, savings or investment, mortgage or loans, insurance, or tax planning. An additional model defines  $Y$  as any form of advice, meaning that at least one of the prior dependent variables is positive. The three attitudinal measures of trust, perceived costs, and difficulty finding an advisor (each scaled 1–7) are modeled using a standard OLS regression with robust standard errors.<sup>2</sup> These models test for differences in the take-up of advice by demographic characteristics, financial literacy, and perceptions. All models use the representative population weights.

Variables are selected based on prior literature to serve as proxies for financial capability or because they are likely to explain differences in advice use. Gender is 1 for males and 0 otherwise. Prior studies have suggested that women might be more likely to use advice, as well as that women perform worse on financial literacy tests (Lusardi, 2007a). Age is included as a series of categorical variables with under 35 as the constant; based on prior literature, older people are predicted to be more likely to use advice. Race is included as a series of indicators of African American, Hispanic, and other race, with White as the constant. In prior studies non-White households have shown a greater tendency to exhibit negative financial behavior (Campbell, 2006) and perhaps benefit from advice. Likewise, education is included as a vector of indicator variables with high school dropouts as the constant. If advice is a substitute for financial capability, advice rates would be higher for less educated groups. Prior research suggests that advice use will likely increase with age. Income categories are also included as a proxy for economic resources available, with income under \$25,000 as the constant. Advice is likely to be more likely as income increases. Number of children and a homeowner status dummy are included primarily as controls that might explain the take-up of advice. A key variable of interest is financial literacy, measured as an index of a series of factual questions. Related to this measure is self-reported financial knowledge. Both of the variables will reveal the extent to which (actual or perceived) knowledge substitutes for or complements financial advice. Finally, two distress measures are included. Self-reported trouble paying bills and large reductions in income are included to test whether negative financial shocks might be associated with seeking financial advice. Fixed effects are also included for the census region of the respondent as a general control for economic context.

Table 1 Descriptive statistics from 2009 National Financial Capability Survey

	Mean	SD	N	Min	Max
<b>Dependent variables</b>					
Received any advice	0.567	0.496	1,488	0	1
Saw advisor: Debt (1 = yes)	0.080	0.272	1,485	0	1
Saw advisor: Investing (1 = yes)	0.333	0.472	1,485	0	1
Saw advisor: Loan (1 = yes)	0.235	0.424	1,486	0	1
Saw advisor: Insurance (1 = yes)	0.337	0.473	1,485	0	1
Saw advisor: Tax planning (1 = yes)	0.209	0.406	1,481	0	1
Trust advisor (1–7; 1 = strongly disagree)	3.95	1.769	1,468	1	7
Advisors too expensive (1–7; 1 = strongly disagree)	4.32	2.021	1,456	1	7
Difficult to find advisor (1–7; 1 = strongly disagree)	3.93	1.936	1,452	1	7
<b>Financial capability</b>					
Financial literacy score (0 = low, 5 = high)	2.783	1.398	1,488	0	5
Self-reported financial knowledge (1–7; 1 = low)	5.022	1.505	1,481	1	7
Difficult to pay bills and expenses (1 = yes)	0.467	0.499	1,485	0	1
Large drop in income (1 = yes)	0.324	0.468	1,481	0	1
<b>Demographic and related variables</b>					
Gender (male = 1)	0.484	0.500	1,488	0	1
Age 18–34 years (constant)	0.306	0.461	1,488	0	1
Age 35–54 years	0.374	0.484	1,488	0	1
Age 55+ yrs	0.320	0.467	1,488	0	1
White (constant)	0.640	0.480	1,488	0	1
African American	0.124	0.329	1,488	0	1
Hispanic	0.102	0.303	1,488	0	1
Asian	0.101	0.301	1,488	0	1
Other race	0.034	0.180	1,488	0	1
No high school diploma (constant)	0.102	0.303	1,488	0	1
High school	0.276	0.447	1,488	0	1
Some college	0.496	0.500	1,488	0	1
Graduate degree	0.126	0.332	1,488	0	1
Income under 25k (constant)	0.307	0.461	1,488	0	1
Income 25–50 k	0.241	0.428	1,488	0	1
Income 50–100 k	0.284	0.451	1,488	0	1
Income above 100 k	0.168	0.374	1,488	0	1
Number of children (0 = no children, 4 = 4 or more children)	0.962	1.194	1,488	0	4
Homeowner (1 = yes)	0.618	0.486	1,483	0	1

## 5. Findings

Table 1 displays the descriptive statistics from the analysis. Among the survey respondents, 56.7% report receiving some form of financial advice, 8% report obtaining advice on debt management, one-third report obtaining advice on investing, 23.5% report receiving advice about a loan, about one-third report obtaining advice on insurance, and just under 21% report working with a tax planning advisor. These rates of obtaining advice are consistent with estimates of seeking financial planning advice in prior studies (shown in Fig. 1). Ratings of perceptions of advisors are measured on a seven-point scale, where 7 is strongly disagree. There are three items including trust (mean of 3.95), too expensive (4.32), and difficulty in finding an advisor (1.93). Demographic and other factors appear consistent with tables published by FINRA when using population weights.

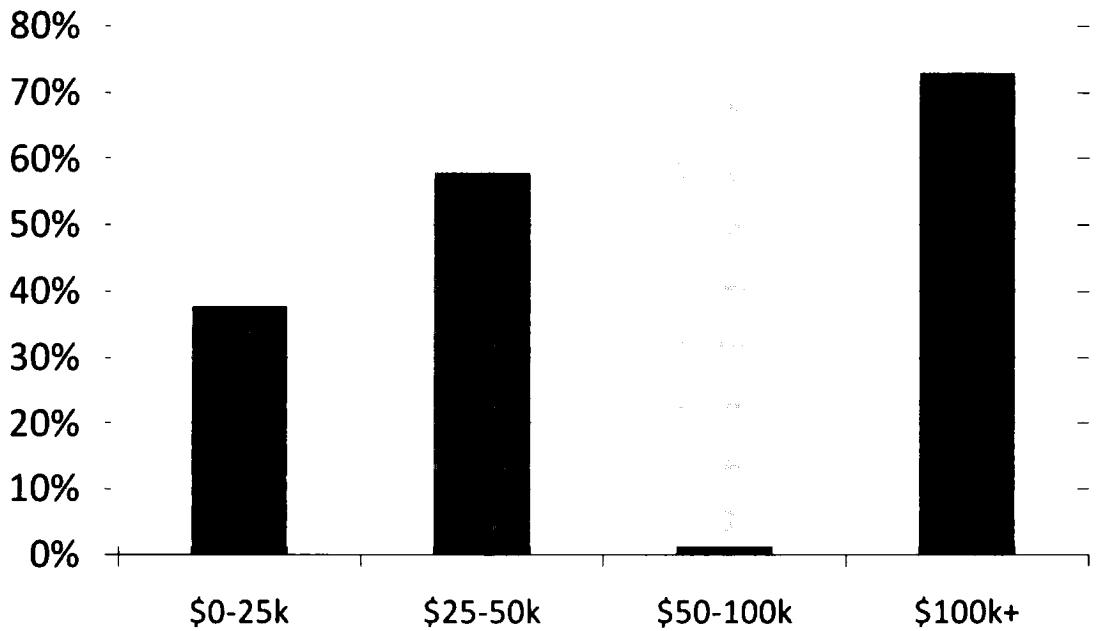


Fig. 2. Percent of respondents reporting use of any form of financial advice by income category. *Source:* Author's tabulations of FINRA National Financial Capability Survey.

Fig. 2 illustrates the differences in the take-up of any form of advice by income, and Fig. 3 shows the same distribution by education level. Overall, a predictable pattern emerges. Individuals with higher incomes and higher levels of educational attainment are more likely to take up advice of any kind. These results suggest that advice is largely a complement to higher levels of financial capability, although these trends do not account for differences in resources or other factors.

Of course, these simple comparisons might obscure the associations between other demographic factors and seeking financial advice. Table 2 shows the influence of various factors on the take-up of advice after controlling for the variables described in Eq. (1). The take-up of each form of advice varies across several demographic characteristics. The take-up of advice on savings and investing, loans, and insurance, and any form of advice (all forms combined) is less likely among males, which is consistent with prior studies. Males show no differences in take-up of debt or tax advice. Relative to those under 35, only people age 55 or older show differing take-up rates by age, and only in the form of lower rates of use of advice about loans. This pattern is likely because of the lower occurrence of debt among older households and therefore less need for such advice. Racial effects on the take-up of advice are modest. Relative to Whites (the constant), African Americans are more likely to use insurance advice, Hispanics are less likely to use tax or *any* form of advice, and Asians are less likely to use tax advice. Number of children is associated with insurance advice, perhaps consistent with parents' concerns about life insurance. Homeowners are less likely to seek debt advice but more likely to seek investment or loan advice. Performance on the financial literacy questions has a positive effect on investment, insurance, tax, and any form of advice. Self-reported financial literacy has similar effects.<sup>3</sup> As might be expected, self-



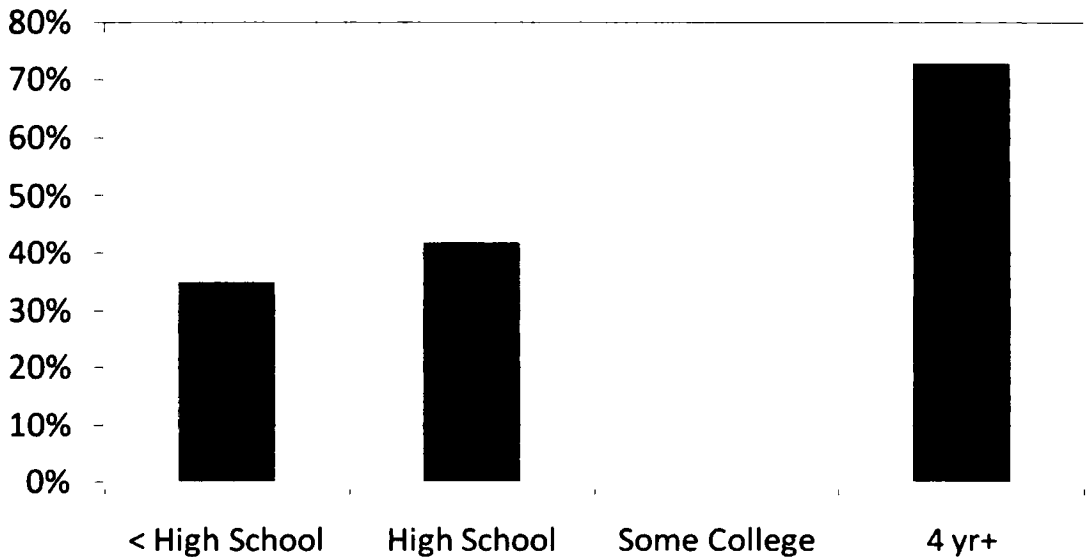


Fig. 3. Percent of respondents who reported using any form of financial advice by education attainment level.  
Source: Author's tabulations of FINRA National Financial Capability Survey.

reported difficulty paying bills is related to the take-up of debt advice, as well as loan advice. Experiencing a large reduction in income is associated with consulting all forms of financial advisors, with the exception of loan advice, which while not statistically significant is opposite in sign.

The take-up of most forms of advice increases with education (relative to no high school), especially investment and tax advice. The take-up of advice also increases significantly at higher income levels. Higher incomes and educational attainment are also generally associated with greater financial capability. This pattern is consistent with the most financially capable people being more likely to use investment advisors.

Few of these results run counter to the notion that financial advice is a complement to financial capacity and knowledge. Notably, African American respondents are more likely to use insurance advice, controlling for other factors, perhaps as a result of targeted insurance brokering and marketing aimed at this group. Homeowners are more likely to have received advice about loans, likely as a result of having to take out and repay mortgages. A drop in income is also associated with an increase in the use of financial advice across most types of advice services, perhaps signaling that advice is used during particularly difficult times. This pattern is consistent with advice serving a different role—not compensating for a lack of financial capability, but rather helping in periods when financial stresses are increasing.

Table 3 displays estimates of attitudes and behaviors surrounding financial advising, including perceived trust of advisors, agreement that advisors are “too expensive,” and agreement that advisors are difficult to find. These questions focus on the core reasons that individuals may not use an advisor: mistrust, cost, and accessibility. The questions were phrased as “I would trust financial professionals and accept what they recommend,” “Financial professionals are too expensive for me,” and “It is hard to find the right financial

Table 2 OLS results for financial advice obtained by form of advice

	Saw advisor: Debt (1 = yes)	Saw advisor: Investing (1 = yes)	Saw advisor: Loan (1 = yes)	Saw advisor: Insurance (1 = yes)	Saw advisor: Tax planning (1 = yes)	Received any advice (1 = yes)
Male	−0.0099 (0.0145)	−0.0486* (0.0237)	−0.0441* (0.0223)	−0.0680** (0.0246)	−0.0186 (0.0206)	−0.0495* (0.0246)
Age 35–54	0.0213 (0.0199)	−0.0175 (0.0307)	−0.0291 (0.0304)	0.0221 (0.0319)	−0.0188 (0.0265)	−0.0090 (0.0323)
Age 55+	0.0216 (0.0205)	0.0226 (0.0329)	−0.1492** (0.0318)	−0.0473 (0.0344)	−0.0089 (0.0293)	−0.0464 (0.0355)
African American	0.0292 (0.0252)	−0.0317 (0.0348)	−0.0281 (0.0312)	0.0862* (0.0383)	−0.0182 (0.0291)	0.0124 (0.0381)
Hispanic	0.0178 (0.0272)	−0.0357 (0.0390)	0.0109 (0.0385)	−0.0324 (0.0399)	−0.0599† (0.0322)	−0.0779† (0.0427)
Asian	0.0087 (0.0253)	−0.0982* (0.0434)	−0.0506 (0.0380)	−0.0589 (0.0429)	−0.0102 (0.0408)	−0.0720 (0.0449)
Other race	0.0110 (0.0425)	−0.0374 (0.0615)	0.0261 (0.0590)	0.0155 (0.0658)	0.0094 (0.0542)	0.0473 (0.0684)
Number of children	0.0015 (0.0070)	−0.0090 (0.0104)	0.0152 (0.0111)	0.0230* (0.0114)	0.0079 (0.0097)	0.0109 (0.0113)
Homeowner	−0.0398* (0.0197)	0.0510† (0.0284)	0.0752** (0.0273)	0.0254 (0.0296)	0.0227 (0.0238)	0.0600† (0.0312)
Financial literacy score	−0.0017 (0.0059)	0.0290** (0.0095)	0.0032 (0.0087)	0.0202* (0.0095)	0.0157† (0.0086)	0.0304** (0.0100)
Self-reported knowledge	0.0000 (0.0052)	0.0143* (0.0071)	0.0037 (0.0067)	0.0173* (0.0078)	0.0143* (0.0067)	0.0269** (0.0083)
Difficult to pay bills	0.0882** (0.0166)	−0.0378 (0.0270)	0.0440† (0.0252)	0.0441 (0.0276)	0.0069 (0.0224)	0.0226 (0.0280)
Large drop in income	0.0338* (0.0172)	0.0685** (0.0259)	−0.0240 (0.0238)	0.0752** (0.0272)	0.0804** (0.0234)	0.0859** (0.0268)
High school	0.0081 (0.0236)	0.0185 (0.0345)	−0.0183 (0.0349)	−0.0180 (0.0389)	−0.0070 (0.0284)	0.0204 (0.0451)
Some college	0.0461† (0.0254)	0.1210** (0.0362)	0.0303 (0.0363)	0.0868* (0.0405)	0.0386 (0.0299)	0.1386** (0.0452)
Graduate degree	0.0443 (0.0323)	0.2384** (0.0533)	0.0679 (0.0512)	0.1044† (0.0554)	0.1334** (0.0500)	0.1813** (0.0566)
Income 25–50 k	0.0585** (0.0226)	0.1118** (0.0315)	0.0785** (0.0274)	0.1322** (0.0332)	0.0237 (0.0244)	0.1629** (0.0374)
Income 50–100 k	0.0452† (0.0233)	0.2065** (0.0366)	0.1840** (0.0331)	0.2049** (0.0369)	0.1165** (0.0302)	0.2636** (0.0394)
Income above 100 k	0.0527† (0.0269)	0.1986** (0.0471)	0.1811** (0.0427)	0.2170** (0.0466)	0.2476** (0.0419)	0.2366** (0.0483)
Constant	−0.0505 (0.0402)	−0.0031 (0.0596)	0.0981† (0.0561)	−0.0789 (0.0616)	−0.0778 (0.0527)	0.0267 (0.0656)
Census region FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	1,468	1,467	1,468	1,466	1,464	1,469
R <sup>2</sup>	0.050	0.147	0.101	0.116	0.121	0.165

Notes: Standard errors in parentheses.

† $p < 0.10$ , \* $p < 0.05$ , \*\* $p < 0.01$ .

professional for me.” Answers were on a scale from 1 to 7, with 1 being strongly disagree and 7 being strongly agree.

Regarding clients’ trust in financial advisors, males, people age 35–54, homeowners, and

Table 3 OLS results for feelings toward advisors

	Trust advisor	Advisors too expensive	Difficult to find advisor
Gender (male = 1)	−0.2152* (0.0957)	−0.1546 (0.1081)	−0.0583 (0.1067)
Age 35–54 years	−0.2545* (0.1221)	0.0901 (0.1384)	−0.0363 (0.1318)
Age 55+ yrs	−0.1348 (0.1377)	−0.1247 (0.1518)	−0.2850† (0.1494)
African American	−0.0148 (0.1636)	−0.3432† (0.1860)	−0.1484 (0.1707)
Hispanic	0.0486 (0.1547)	0.1476 (0.1818)	0.0037 (0.1721)
Asian	0.0881 (0.1523)	0.6093** (0.1669)	0.3315+ (0.1764)
Other race	0.2673 (0.2758)	0.1733 (0.2780)	0.0337 (0.2858)
Number of children	0.0667 (0.0437)	0.0739 (0.0497)	−0.0482 (0.0484)
Homeowner dummy	−0.3248** (0.1243)	−0.0693 (0.1372)	0.0309 (0.1294)
Financial literacy score	0.0269 (0.0382)	−0.0138 (0.0447)	0.0112 (0.0447)
Self-reported financial knowledge (1 = low)	0.0535 (0.0369)	0.0083 (0.0406)	0.0337 (0.0384)
Difficult to pay bills and expenses dummy	−0.0235 (0.1090)	0.4081** (0.1224)	0.2783* (0.1204)
Large drop in income dummy	−0.2316* (0.1089)	0.0797 (0.1218)	0.1021 (0.1177)
High school	−0.0427 (0.1949)	0.2400 (0.2114)	−0.1392 (0.1997)
Some college	0.1159 (0.1922)	0.1615 (0.2077)	−0.1796 (0.2013)
Graduate degree	−0.0546 (0.2252)	−0.0494 (0.2501)	−0.3543 (0.2564)
Income 25–50 k	−0.1907 (0.1411)	−0.1433 (0.1585)	−0.2015 (0.1508)
Income 50–100 k	0.0234 (0.1531)	−0.2706 (0.1679)	−0.1885 (0.1642)
Income above 100 k	−0.0652 (0.1809)	−0.6912** (0.2087)	−0.1261 (0.2049)
Constant	4.1168**	4.3355**	4.2484**
Census FE	(0.2928)	(0.3250)	(0.3056)
Observations	YES	YES	YES
R <sup>2</sup>	1,451	1,439	1,435
	0.027	0.055	0.026

Notes: Standard errors in parentheses.

† $p < 0.10$ , \* $p < 0.05$ , \*\* $p < 0.01$ .

people who experienced a large drop in income were less likely to agree that they trust financial advisors. The finding regarding males is consistent with prior work showing that males may be more prone to overconfidence (Odean, 1999).

Regarding costs, there were few statistically significant findings. Asian respondents and

people who reported having difficulty paying bills were more likely to perceive advisors as too expensive. While the latter is predictable given tight budgets, the finding regarding Asians is somewhat surprising. As income increases, the agreement that advisors are too expensive declines, with the highest income group being significantly more likely to disagree with the statement that advisors are too expensive. There are few (weakly) statistically significant findings about difficulty finding advisors. Older people (age 55 or more) are less likely to agree that advisors are hard to find, and Asian respondents more likely (consistent with the view of costs above). Perhaps this result reflects an uneven distribution of advisors that target Asian clients. Individuals struggling to pay their bills are more likely to think advisors are hard to find, the only result in this column to achieve the 5% level of statistical significance. Overall these findings reveal variation in trust, perceived costs, and accessibility of advisors, but no relationship between these factors and financial literacy.

These results suggest that financial advice is primarily employed as a complement to financial capacity, rather than a substitute for financial knowledge. The findings reveal that as income, education, and financial literacy increase, the use of advice also increases. Of course, this pattern also suggests that consumers with lower functional financial literacy—those individuals who may be most likely to make financial mistakes without advice—are among the least likely to seek it. While researchers may hypothesize that advice is most valuable to people with lower education levels—both because they may face higher information acquisition and cognition costs and because they may be more likely to make errors—these results do not support this hypothesis. Rather, these data suggest that higher-income individuals consume more advice, perhaps because of the potential of larger perceived marginal benefits, a greater willingness or ability to pay, or the use of investment products that may be more closely tied to advisors' sales networks. As a whole, these findings suggest that the use of financial advice is more likely among individuals with higher incomes and higher educational attainment.<sup>4</sup> However, a recent drop in income is associated with higher take-up of some services, suggesting advice may play a key role in tough financial times.

Notably, debt advice as measured in this survey is likely more akin to credit counseling, which might differ from other types of financial advice for several reasons. First, debt counseling typically attempts to help clients resolve financial crises such as bankruptcy. Second, counseling also entails directing, instructing, and motivating clients (Kerkmann, 1998), especially because individuals faced with a financial crisis may not know what options are available or may have difficulties searching for and processing information. Third, counselors are typically not compensated via commissions or sales-related metrics. Counseling is often subsidized by public or private sources and provided by nonprofit or public organizations. While important, especially for those facing financial distress, debt advice should be considered separately from the other forms of advice discussed.

## **6. Conclusions**

People with higher levels of financial literacy or capacity are more likely to use investment, insurance, and tax-related financial advice, but not debt or loan-related advice. This

pattern likely reflects the prevalence of investable assets among more educated and financially capable groups, and also demonstrates that financial advice is a complement to, rather than a substitute for, financial literacy. As an individual's financial literacy and capacity increase, so does the likelihood of using financial advice, especially in the area of investing.

A majority of respondents (56.7%) reported using some form of financial advice, yet those with low levels of financial literacy were less likely to obtain any advice, and, in general, factors correlated with lower financial capability such as education and income were also related to lower take-up of financial advice. There is a strong correlation between advice seeking and financial literacy. If expanding the use of financial advice is a policy goal, increasing financial literacy levels may be an appealing approach to achieve this goal, but the notion that advice models can "make up for" lower levels of financial capability or knowledge among vulnerable populations is not well supported in these data.

Overall, more research is needed to better define, quantify, and measure the impact of each of the advice models presented. More robust evidence of the costs and benefits of various forms of financial advice can help inform policy decisions and guide consumers regarding the value of professional advice. The fact that some forms of advice are more widely used by people when they face a large drop in income is consistent with the notion that consumers turn to advice in response to major economic shocks or life changes. It is important for scholars and policy makers to understand and highlight the role of advice at such critical moments.

## Notes

- 1 Types of professional financial advice vary widely. For example, certified public accountants (CPAs) are not personal financial advisors in the same way that financial planners are. Other technical experts, including estate attorneys and bank trustees, may also provide financial advice. However, these fields are heterogeneous, and financial advice is generally a small part of overall services provided to clients.
- 2 Similar specifications using an ordered probit yielded similar results. OLS models are presented for parsimony.
- 3 The correlation between the financial literacy score and the self-reported score = 0.207.
- 4 Post-regression tests of coefficients reveal significantly different beta estimates at higher education and income levels relative to lower levels.

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**Appendix A: FINRA Financial Capability Survey: Variables used in the analysis**


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“In the LAST 5 YEARS have you asked for any advice from a financial professional about any of the following?”	
Saw advisor: Debt	K1 “Debt counseling”
Saw advisor: Investing	K2 “Savings or investments”
Saw advisor: Loan	K3 “Taking out a mortgage or a loan”
Saw advisor: Insurance	K4 “Insurance of any type”
Saw advisor: Tax planning	K5 “Tax planning”
Received any advice	Obtained by summing K15 and setting equal to 1 if sum was $\geq 1$
“How strongly do you agree or disagree with the following statements? Give your answer on a scale from 1 to 7, with 1 being ‘Strongly disagree’ and 7 being ‘Strongly agree’”	
Trust advisor	K8a_1 “I would trust financial professionals and accept what they recommend.”
Advisors too expensive	K8a_2 “Financial professionals are too expensive for me.”
Difficult to find advisor	K8a_3 “It is hard to find the right financial professional for me.”
Financial literacy and current financial status	
Homeowner	Ea_1 “Do you or your spouse/partner currently own your home?”
Financial literacy score	Created by taking the sum of 5 financial literacy quiz questions (M6–10), where the correct answer to the question was assigned a 1 and all others were assigned a value of 0.
Self-reported financial knowledge	M4 “On a scale from 1 to 7, where 1 means very low and 7 means very high, how would you assess your overall financial knowledge?”
Difficult to pay bills and expenses	J4 was recoded so “Not at all difficult” was 0 and “Somewhat difficult” and “Very difficult” were 1. “In a TYPICAL MONTH, how difficult is it for you to cover your expenses and pay all your bills?”
Large drop in income	J10 “In the PAST 12 MONTHS have you/your household experienced a large drop in income which you did not expect?”

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*Note:* All questions were coded so that “Don’t know” and “Refused” were changed to missing.