J.D. Power and Associates

2009 Canadian Investor Satisfaction Study℠

Canadian Investment Channel Diversification—A Changing Landscape

Amid the continuous bad news in the market, Canadian investment service firms are witnessing a dynamic change in channel diversification that is reshaping the landscape of the industry. Following its half-billion-dollar acquisition of E*Trade Canada in the fall of 2008, Scotiabank reported more than 60% growth in its new online brokerage account openings for the first quarter this year. Other major online brokerages have reported similar growth patterns. Shouldn't investors be seeking advice from experienced investment advisors to get them through the market turmoil instead? Common sense would say yes. However, these reports seem to suggest otherwise.

Have investors fled their advisors to self-direct their investments with the cheaper online or discount brokers, or have they diversified their investment channel use to maximize the benefits from each? To answer these questions, J.D. Power and Associates surveyed 65,000 investors in Canada earlier this year as part of the *2009 Canadian Investor Satisfaction Study*, which provides information about the needs and experience of investors who use both full service brokerages and/or discount brokerages or private banking and wealth management firms.

Overlap vs. Bimodal Channel Use

Currently 40% of investors in Canada either do not have investable assets other than employer pensions and stock plans, or do not use investment advisory firms. One in five investors uses a full service brokerage firm to manage their investment, while one in four uses a bank or credit union. The remaining investors use either Insurance-Based advisors or advisors from financial planning or wealth management firms.

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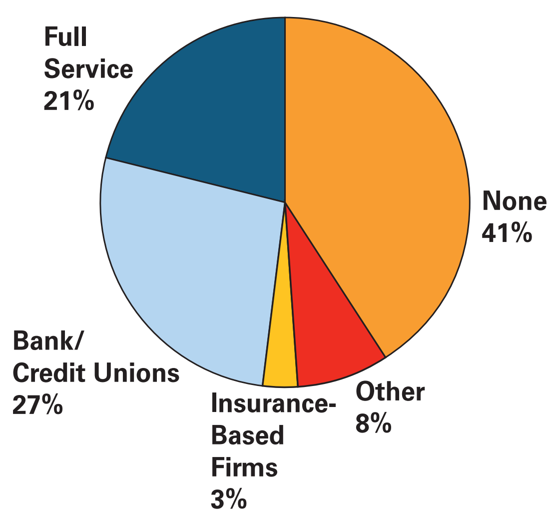
Investment Advisory Services Used by Investors in Canada



Source: J.D. Power and Associates 2009 Canadian Investor Satisfaction Study℠

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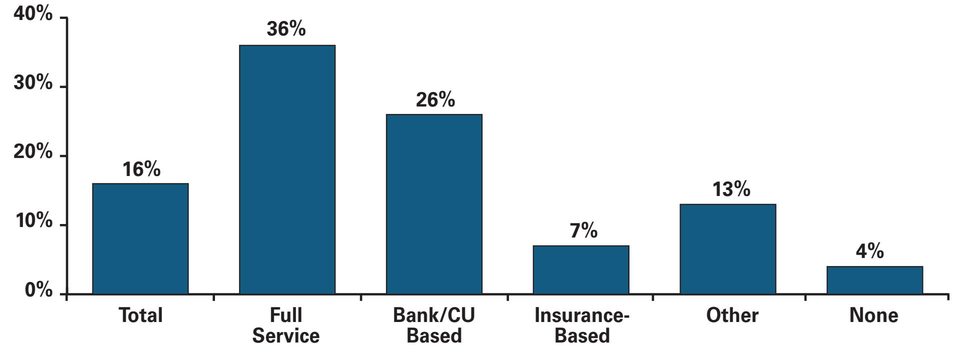
In comparison, discount brokerage usage is still low in Canada, 16%. However, the choice between seeking advice or self-directing investments is not a discrete bimodal pattern in which investors using the advisory firms differ from those using discount brokerage firms. Instead, the two channels overlap, with the discount brokerage penetration highest among investors who also use advisory services.

"...with the market going through a meltdown, full service investors using an online brokerage firm in 2009 grew by almost half over the previous year to 36%."

Usage of Discount Brokerage by Segment



Source: J.D. Power and Associates 2009 Canadian Investor Satisfaction Study[SM]

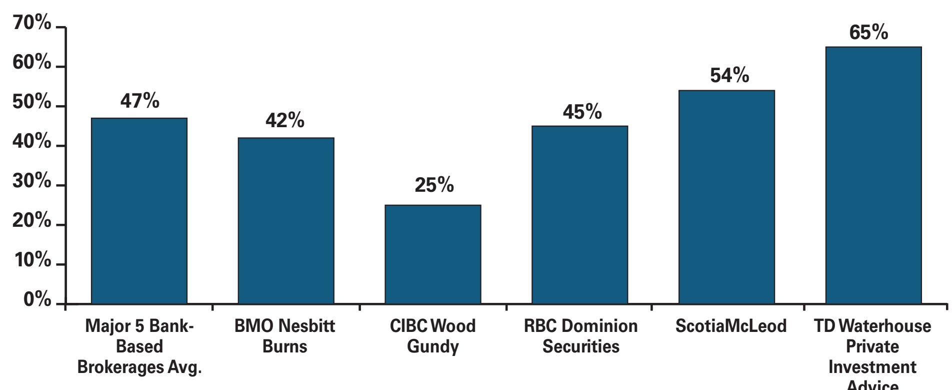
This may suggest that the growth of the discount brokerage channel is not propelled by new investors coming into the market or by those who have fired their advisors. Instead, it is driven by increasingly sophisticated investors who are diversifying their investment channels to benefit from both the guidance of their advisors and the low cost of trading online themselves. In the *2008 Canadian Investor Satisfaction Study*, 25% of full service investors reported using an online brokerage firm. In contrast, with the market going through a meltdown, full service investors using an online brokerage firm in 2009 grew by almost half over the previous year to 36%.

Driving the Trend

The first driver of this trend is the increasing integration of the wealth management industry in Canada. All major Canadian banks have a separate full service brokerage firm, a discount or online brokerage, and branch-based private banking or financial advisor services. To retain their clients, these banks cross-refer them within the investment firm's different channels, based on their asset levels and investment style.

The chart below shows the percentage of discount brokerage usage among investors who use one of the five major bank-affiliated full service brokerage firms. Except for CIBC Wood Gundy, all have discount brokerage penetration higher than the full service industry average. TD Waterhouse PIA has the highest cross-channel penetration, with nearly all of their investors staying within the company's own discount channel.

Usage of Discount Brokerage among Bank-Owned Brokerage Investors



Source: J.D. Power and Associates 2009 Canadian Investor Satisfaction Study[SM]

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Another factor driving the trend is the increasing sophistication of investors. They understand the value of each channel and know how to maximize their own benefits by diversifying channel usage, while also diversifying their investment portfolio.

As investment vehicles become more complicated, investors with substantial assets and the need to manage them will require professional assistance from advisors. At the same time, investors are finding online investment information accessible, and online trading secure, easy to use, and cost-effective. This has created a new frugality, a situation in which an investor might call their advisor to get recommendations on portfolio mix and stock selection, but then turn around and place their order online for $9 or $7 per trade rather than spending $250—or 2% of total transaction value—by trading through an advisor.

In a bull market, investors might not mind spending a few extra dollars to have everything done in a one-stop shop. But when their assets are losing value, that extra trading charge could become painful enough to force them to change investment behaviour. The banks' integrated channels have also made this an attractive and viable option.

The net result: J.D. Power and Associates believes investors in Canada are seizing control of their own financial destiny and putting the investment service firms on high alert they want a custom mix of products, services, and reasonable pricing for both advice and do-it-yourself transactions to match their comfort level and investment styles.

Navigating the Crisis and the Road Ahead

Looking ahead, J.D. Power and Associates believes the Canadian channel diversification will continue in the foreseeable future, with each channel playing a unique and critical role. Investors will still need to consult an advisor on complicated products or portfolio strategy. At the same time, they will become more willing to take a do-it-yourself approach and self-direct their routine trading transactions. The current economic crisis and market volatility will accelerate this trend.

Financial institutions offering an integrated full service and discount brokerage channel are better positioned to take advantage of this changing trend. Those that do not integrate channel offerings need to look for alternatives to protect and grow their business. Some full service firms have partnered with online brokerages to deliver better value to their clients, while others have segmented their client base to target investors who have a more complex portfolio or those who are less inclined to be self-directed investors.

Another factor that investment service firms need to consider for their long-term business model or planning is the changing demographics of investors in Canada. In another decade or so, the youngest Baby Boomers will be retiring, while consumers in both Gen X and Gen Y will mature and start investing. These younger generations of investors have grown up with computers and interactive games. Their world exists online and on-the-go, fueled by immediate gratification via texting, Twitter, and Facebook, among others. Their investment needs and channel preferences will likely differ from those of their parents. To attract Gen X and Gen Y investors and stay competitive, investment firms need to rethink their business model, including their product, pricing, and channel strategies. Staying close to the voice of the clients, including future clients, will be a step in the right direction.

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About J.D. Power and Associates

For four decades, J.D. Power and Associates has been measuring the Voice of the Customer and providing key performance indicators for various industries in many parts of the world.

Since its inception in 2006, the *Canadian Investor Satisfaction Study* has provided unbiased information about investment firms so investors can make informed choices. The study also provides information to the investment industry to help firms improve their products and services.

J.D. Power and Associates currently conducts six syndicated benchmark studies that serve the Canadian financial service and insurance industries:

- *Full Service Investor Satisfaction*
- *Discount Brokerage Investor Satisfaction*
- *Retail Banking Customer Satisfaction*
- *Auto Insurance Customer Satisfaction*
- *Home Insurance Customer Satisfaction*
- *Auto Dealer Financing Satisfaction*

For a more detailed briefing about the results of this study and how your organization can use this information to improve your performance and outperform your competitors, please contact Lubo Li, Senior Director and Financial Service Practice Leader, 416-499-3033 ext. 142 at lubo.li@jdpa.com; or Adrian Chung, Research Manager, 416-499-3033 ext. 117 at adrian.chung@jdpa.com.

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