HOW WEALTH MANAGEMENT CAN SURVIVE A 40 BASIS POINT FUTURE

The world of wealth management is barely recognizable today in comparison to just a few years ago – and the pace of change is accelerating. We now live in a highly regulated, technology enabled world with a customer/investor base that's experiencing a major demographic shift. It's a perfect storm of disruption.

All these changes are putting substantial pressure on revenues and margins and profitability has taken a beating, putting many firms' very survival into question.

The advice industry is now under immense pressure to find new ways to make money. It's no longer sufficient to add some additional products here or change your pricing approach there or allocate more capital to recruiting front line staff. These kinds of business tweaks have had little impact on margin expansion.

THE 40 BASIS POINT FUTURE

Speaking at the TD Ameritrade LINC advisor conference earlier this year, Don Bennyhoff, senior investment strategist for Vanguard, famously predicted: "The future is 40 basis points."

Whether or not you agree with the number 40, it's hard to deny the pressures that are moving us in that direction. There are pricing pressures on many of the services advisors provide their customers today. Technology has commoditized many of these services and this trend is increasing. In a technology-enabled wealth management industry, the value of your service as an advisor does not lie in access to and management of investments. Long gone are the days that investors needed a highly compensated advisor to call in an order to a trading floor. Decently-designed portfolios of low-cost investments are merely a click away. The alpha of advisors is increasingly not associated to investment portfolio management. All of this is a scary proposition for many advisors and wealth management firms today.

The question all firms should be asking themselves now is this: How will we adapt to a business environment in which investment advice is priced at (or moving in the direction of) 40 basis points?

As I see it, there are really three options for advisory firms:

1. Cut costs massively;
2. Scale your business significantly;
3. Reinvent your business model.

With respect to the first two of these options, they are well underway. Firms have been cutting costs continuously for much of the past two decades and cost management continues to be a focus. And consolidation to achieve scale is already occurring.

CHALLENGES AND OPPORTUNITIES

The real opportunity facing many financial services businesses, and in particular the wealth management industry, is the reinvention of the entire business model of delivering advice.

So, how do you reinvent your wealth management business model and ensure you won't become a casualty of this new reality? How do you create stickier clients, boost growth, and earn a premium by delivering increased value? And how can you do that amidst these five massive shifts underway in wealth management?

Despite the multitude of challenges facing our industry, the opportunities are abundant:

- There is significant wealth in the market (see State of US Wealth).
- There are massive pockets of underserved potential clients, including executive women (see Harnessing the power of women investors in wealth management).
- There are 10,000 new retirees per day (see Pew Research).
- Over $30 trillion of intergenerational wealth transfer is estimated over the coming decades (see CNBC.)

The challenge for advisory firms face is the need to create more value for their investor clients. But how?

THE FUTURE OF FINANCIAL ADVICE

The future for many wealth management firms depends on formulating and executing a multi-pronged strategy that re-envisions financial advice business model and leverages digital technology throughout the enterprise.

Here are a few ways financial services firms can do this:

- ***Digitize the Enterprise*** – As digital technology disintermediates and commoditizes many of the core transactions in financial services, firms need to be at the leading edge of integrating these technologies and services into their offering. Portfolio management can be automated. Customer data can be intelligently mined for business insights. While robo-advisors haven't won a significant market share yet, they have moved the yardsticks with regard to user value and customer expectations. State-of-the-art digital technology and business processes are less about competitive advantage and increasingly table stakes.
- ***Unbundle the Value*** – Fintech innovations are often based on unbundling financial services and delivering them better, faster and/or cheaper. Advisory businesses can no longer thrive by bundling advice along with

product transactions and expect customers to be able to tell the difference. A shift needs to be made to an advice and knowledge centered business model.

- ***Broaden the Offering*** – Advice providers need to move up the value chain to address their clients' core needs around life planning. This means focusing less on transactional services like securities trading and portfolio management and more on relationship-based advisory services to help clients define and achieve not only their financial, but their life goals. Holistic financial and estate planning offerings are emerging and some advisors are recognizing the emotional issues surrounding money, particularly during liquidity events and life transitions, and offering counselling support through these changes. Yet, there are many unexplored potential ways for financial, accounting, legal, business and life advisory services to be bundled into niche market offerings.
- ***Embrace the Humanity*** – Even as firms are digitizing, they need to put the humanity back into the business. Customers want it. The growth of the independents has been driven by a belief by those advisors that they needed to flee firms that were systematically taking the humanity (not the humans) out of the equation. Stop removing the emotion from the customer relationships. Embrace it. Focus on it. Deal with it. Invest in advisors by supporting them with the right tools, enabling them to refocus on relationships and efficiency so they can maximize their productivity.

Advisors can also do many things to help themselves in the future of wealth management. Read more about this in our article 10 Ways advisors can prosper in the new wealth management.