CAPCO

WEALTH MANAGEMENT TRENDS 2020

INTRODUCTION

Against a backdrop of global economic uncertainty, the potential end to the US equity bull market, continued industry fee compression and regulatory scrutiny, wealth managers are faced with significant headwinds that could destabilize their core business in 2020.

Coupled with the continual rise and disruption of the independent channel, primarily registered investment advisors (RIAs) and independent broker-dealers (IBDs), and consolidated discount broker landscape, incumbents should consider a recalibration of strategic initiatives to prioritize new revenue streams and drive cost efficiency.

Firms would be well-suited to focus on the following strategies to capitalize on trends set to accelerate:

- **Engage the underserved**
- **Provide holistic solution offerings**
- **Monetize data capabilities**
- **Evolve business and operating models**

ENGAGE THE UNDERSERVED

Access Retail Investors via Alternative Investments

The democratization of alternative investments provides wealth managers with an opportunity to improve their offering to retail clients at a time when demand for uncorrelated returns to traditional equity and bond markets will proliferate.

The retail market represents a largely untapped pool of capital for the alternative investments industry. Traditionally associated with institutional and ultra-high net worth investors, the landscape is evolving, whereby the broader adoption of alternatives downmarket within retail client channels is ready to accelerate due to favorable tailwinds – improved accessibility and lower fees enabled by fintech platform providers, proven long-term investment performance and positive sentiment of private market growth potential.

Ahead of an anticipated market pullback, retail investors should consider increasing alternative investment exposure to provide downside risk protection and potential alpha generation. According to Preqin[1], global alternative assets was approximately $9 trillion as of year-end 2017, forecasted to surpass $14 trillion by 2023. As AUM continues to grow steadily and asset managers prioritize retail client channels, wealth managers must ensure their offerings are suitable to meet an uptick in client demand.

1. https://docs.preqin.com/press/Future-of-Alts-Oct-18.pdf

ENGAGE THE UNDERSERVED (CONTINUED)

Women in Wealth

Wealth managers should prioritize efforts to better engage with women, who are largely underserved, particularly as a client segment and within the advisor field.

Despite making up more than half of the US population, having longer life expectancies and earning the majority of undergraduate and master's degrees, women are viewed as a niche client segment and represent only 16 percent of financial advisor roles[2]. Firms that are seeking to increase focus on this demographic need to understand the unique challenges women face including the wage gap, career breaks and investment preferences.

Women are increasingly controlling more wealth in the US and taking more of an active role in family financial planning. As a result, there is a growing demand from clients wanting to work with female FAs. Deepening relationships with existing clients through products and platforms targeted to female investors and financial education tailored to the evolving needs of women will differentiate firms in the industry.

Pricing Model Redesign

The traditional AUM-based fee model is being disrupted by new pricing strategies, such as the fee-for-service model, which is seeing increased adoption.

Once viewed as an ancillary service, financial planning has become the cornerstone of wealth management. As a result, the unbundling of investment fees and financial planning is being driven by client demand for greater fee transparency and a more holistic goal-based planning approach.

Although the challenge of re-configuring a long-served pricing strategy is in its early stages, firms need to sharpen their focus on an approach ahead of expected regulatory focus. The opportunity for firms to bridge the gap between fees charged and tangible value-added cannot be understated. Aside from fee-for-service, a subscription-based pricing model is gaining traction as it is both scalable and draws recurring revenue.

Furthermore, many clients seeking standalone financial planning services are broadly underserved as their investable assets typically do not meet minimums that would trigger the attention of an advisor. Tapping into the growing mass affluent client segment can serve as a longer-term growth driver.

2. Cerulli Associates: https://investmentsandwealth.org/getattachment/199f4b97-37a5-44fb-80f4-91ebae9a39a5/2019-1-InvestmentsWealthResearch.pdf

PROVIDE HOLISTIC SOLUTION OFFERINGS

Financial Wellness

Financial wellness presents an opportunity for employers to better serve their employees via reducing stress and improving engagement and retention while creating a new source of potential clients.

The increased attention of financial wellness in recent years reflects a broader industry shift toward workplace benefits services. However, firms have struggled to increase revenue and grow market share in an increasingly competitive landscape. The current challenge related to financial wellness programs is the disconnect between employer solutions and the custom needs of employees that are not being addressed. Targeted offerings to particular segments, including millennials and women, can help to bridge the discrepancy gaps.

Despite these headwinds, wealth managers such as Morgan Stanley believe there is an opportunity for growth. Their recent acquisition of Solium Capital provides the wealth manager with a direct channel to plan participants and a natural transition to serve them early in their wealth accumulation years via their financial advisor model as their needs become more complex. Firms that demonstrate market leadership by improving employee retention and providing financial benefits beyond retirement plans will be well-positioned to successfully navigate the ‘war for talent’ while tapping into a newly established B2B distribution channel.

Convergence of Offerings/Services

The ability to successfully weave together wealth management with banking, retirement and insurance services will set the stage for an ecosystem battleground.

A firm’s ability to offer a comprehensive financial picture that enables clients to seamlessly navigate across investments, savings and lending is proliferating. The increased focus on providing a broader range of customer-centric solutions has naturally led to the intersection of wealth management with banking, retirement, insurance and potentially healthcare.

Insurance and benefits firms are increasingly pursuing retirement practices, as evidenced by Hub International’s recent acquisition of Sheridan Road Financial, a large retirement advisory firm. Employers see growth potential in providing a full suite of capabilities to their workforce and further value when comparing to peers that are ignoring the emerging trend.

The complexity associated with transformation on this scale is significant but addressing this gap in the market represents a substantial opportunity for forward thinking firms to provide an omnichannel solution that will revolutionize the industry.

MONETIZE DATA CAPABILITIES

Data-Driven Portfolio Construction

Wealth managers are increasingly investing in technology such as sophisticated portfolio risk analytics to provide actionable insights and differentiate their capabilities among competitors.

In response to a limited understanding of risk exposure by financial advisors and clients, firms are solving for the deficiency by developing a comprehensive portfolio analytics strategy. By leveraging big data and AI technologies, wealth managers are producing a more robust portfolio construction process that positively impacts the firm, advisors and clients alike.

The most impactful outcomes include firms attracting and retaining advisors, FAs increasing client engagement and AUM and clients optimizing risk/return outcomes in their investment portfolios. Firms would be well-suited to capitalize on this opportunity to distinguish themselves in the near-term.

Automation via Big Data

AI, ML and RPA continue to drive increased productivity and efficiency, improving cost reduction and unlocking new revenue streams through scalable and tailored solutions.

Automation via artificial intelligence (AI) and machine learning (ML) is transforming the client experience and extending the reach of wealth managers. Additionally, robotics process automation (RPA) is streamlining back-office processes via scalable rules-based work.

Firms are increasingly leveraging big data to improve compliance amid an evolving regulatory landscape and are utilizing predictive analytics to collect new assets better. For example, identifying mass affluent clients that are likely to move up the value chain to HNW will enable firms to enhance the customization of products and services. While wealth managers are focused on developing these deep customer insights, cybersecurity remains a top priority. Firms continue to invest in AI and ML infrastructure to manage cyber threats and build better outcomes.

EVOLVE BUSINESS AND OPERATING MODELS

Succession Planning

Wealth managers are grappling with attracting and retaining talent and AUM as the primarily baby boomer financial advisor population approaches retirement.

According to Cerulli, approximately 37 percent of the advisor force will retire over the course of the next decade[3]. Furthermore, it's estimated that only 13 percent of adult children, primarily millennials, would use their parents' advisor. The multi-generational wealth transfer, combined with the disruption of long-standing relationships, poses a significant challenge for wealth managers.

Viewing the impending disruption through this lens, firms need to stand up business succession programs in the near-term while developing career paths to attract younger talent, in the long-term. Increasing recruiting and training efforts, targeted explicitly to Generation Z as they begin to enter the workforce, will be critical to mitigating the risk of losing assets.

Engagement and Adoption

To offset low content utilization related to technology investments, firms should consider recalibrating their engagement and adoption strategy to drive improved ROI.

In recent years, wealth managers have invested significantly in proprietary and third-party technology applications via open API to equip FAs with the tools to automate manual processes and thus enabling them to focus on business development.

Despite the substantial investment in technology, user adoption has been muted, likely due to the focus on additional features rather than the user experience.

As we move into an uncertain economic environment, it will become increasingly critical for users to adopt existing technology as firms decrease technology spend and shift focus to streamlining fragmented data. The intersection of clients and advisors with best in class technology will chart the path for future success in wealth management. Firms should formulate a straightforward approach that educates their advisor field on the significant insights at their fingertips.

Reg BI

Although the DoL Fiduciary Rule was removed in 2018, there continues to be a consistent regulatory focus on conflicts of interest aimed at protecting retail clients.

Similar to the Fiduciary Rule, the SECs Regulation Best Interest (Reg BI) seeks to mitigate conflicts of interest in client recommendations and financial incentives. In response, wealth managers need to review their current state business model to assess operational readiness adequately. However, due to the recent response related to DOL, wealth managers are better prepared to comply.

As clients continue to seek greater transparency, firms have an opportunity to simplify their approach to revenue models and compensation.

3. Cerulli Associates: https://www.cerulli.com/about-us/press/2019-october-us-brokerdealer-marketplace-2019/

CONCLUSION

Due to the structural changes occurring in the industry, primarily digital transformation and changing client demands driven by technology, wealth managers are faced with constant disruption. Firms that increase client engagement via a service model that can address all levels of wealth and reframe their value proposition via the use of data and automation will be well-positioned to grow wallet share and differentiate their offering in a challenging market environment.

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ABOUT CAPCO

Capco is a global technology and management consultancy dedicated to the financial services industry. Our professionals combine innovative thinking with unrivalled industry knowledge to offer our clients consulting expertise, complex technology and package integration, transformation delivery, and managed services, to move their organizations forward.

Through our collaborative and efficient approach, we help our clients successfully innovate, increase revenue, manage risk and regulatory change, reduce costs, and enhance controls. We specialize primarily in banking, capital markets, wealth and asset management and insurance. We also have an energy consulting practice in the US. We serve our clients from offices in leading financial centers across the Americas, Europe, and Asia Pacific.

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