Embracing the Digital Revolution

How to Empower Digital Advice to Create Scale

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That Was Then, This is Now

Barely a week goes by without an announcement of a new and better robo advice solution—with bells and whistles designed to capture the interest of mainstream and tech-savvy investors alike. The challenge is that despite the rise of cool, consumer-friendly apps, the back-office hasn't gotten the memo. Compliance, custody, and trading are still beset with regulations and money movement grounded in the traditional regime.

Focusing on the consumer—engaging them, building trust, and providing value in a just-in-time manner—is the winning formula. Ultimately, the consumers don't care what goes on behind the curtain; they want to know that they are safe, secure, and can manage their financial lives. As wealth managers, we're caught in a quandary: aware of the complexity of operational functions, and balancing the requirement to be fully compliant with the need to evolve the client experience to one that is educational, user-friendly, and interactive.

Digital advice is still in the early innings. Advisors who embrace the new landscape will be able to seize the opportunities out there. The time is now.

Baby Boomers approaching retirement are discovering that they actually need professional advice. The mass affluent may deem the traditional, one-on-one advisor relationship to be too expensive. Gen X and Millennials have different needs—they are digital natives, and expect to use their smart phone to manage their finances, too.

Although the traditional advice model will still play an important role, the advisor landscape is being transformed into a three-pronged approach: (1) human advisors who will continue to service mainstream investors; (2) a hybrid, advisor-assisted solution to meet the needs of consumers who crave on-line tools, but when a complex situation arises, want to connect to a human; and (3) a digital-only solution to give Gen X and Millennials the experience they prefer in a cost-effective way.

At the same time, advisors are embracing technology as a tool to evolve their businesses: defining and segmenting their clients, and devising new and better ways to serve them. Their overarching goal is to grow their practice, keep assets sticky, manage costs, and improve value for an ultimate succession plan.

Advisors who adopt a digital strategy will add data aggregation, financial planning, FinApps, and straight-through processing technology to the traditional platform—proposals, investments, reporting, and Compliance. This new, interactive model—computers and humans working together to power the delivery of engaging advice—is the ideal solution.

The digital revolution underway is approaching a new phase. Robo advisors have struck a chord with Millennials, who seek an interactive experience. Their technology platforms were designed to create a simple, streamlined experience. Robo advisors then morphed into a B2B next generation of advice, extending that core functionality to enable advisors to broaden their service offering and achieve cost efficiencies in the process. We now have advanced to the next stage: combining the simplicity of a robo advisor with established players who have reputable, navigable toolsets to automate the entire process, from the consumers on their tablet or smart phone to the custodian who provides safe keeping of assets.

Assessing the Challenges

Challenge: Online Research is the Consumer's First Step

In today's fast-paced environment, in which few have either the desire or the time to make an appointment to meet with an advisor, a digital model makes it easy for individuals to begin the journey when it's convenient. They can use interactive tools to ask easy questions and obtain quick answers before determining whether they want or need to take the next step and meet with an advisor.

Investors are willing to take the first steps to do research to educate themselves about their financial wellness. However, when they need more in-depth advice or their financial circumstances become complex, they want to push the help button. For example, a Baby Boomer approaching retirement seeks answers to questions such as: How soon can I retire? What will my lifestyle cost when I do? When should I start claiming Social Security? Finding answers to these questions can be involved and time consuming, so the investor can use on-line resources to create what-if scenarios before committing to assembling mounds of paperwork to prepare for an advisor meeting.

66% of children fire their parents' financial advisers after they receive an inheritance. *

* "The great wealth transfer is coming, putting advisers at risk," InvestmentNews, July 13, 2015

Gen X and Millennials have grown up with technology from the time they were toddlers, and they are much more proficient with (and prefer) digital connectivity, be it mobile phones, iPads, social media, or websites. Their goals are different: They want an engaging experience and tailored services from an advisor they can trust. More often than not, that means a robo one, rather than a person, but they won't know whether they can extend their trust until they do their research—something they will likely do online and via social media.

Challenge: Wealth Transfer

We are in the throes of a generational shift. In terms of population, Millennials now outnumber baby boomers. Today's investment landscape will undergo the greatest wealth transfer seen in decades, as Baby Boomers hand down $30 Trillion to succeeding generations[1]. Over the next 4 years, $4 Trillion in assets are projected to be transferred[2]. Gen X and Millennials already comprise more than 20% of the wealth market over $1 Million, and many are high earners in their own right. In fact, Millennials recently outpaced Baby Boomers as the largest demographic group working today[3]. Each of these groups needs to connect to advice that addresses their needs in a way that is convenient for them[4].

1 Wall Street Journal, April 27, 2016 "Preparing Millennials for a $30 Trillion Wealth Transfer"
2 WealthManagement.com, April 20, 2016 "Where's the Money Going in 2020? Six Trends Driving Wealth Flows"
3 http://www.valuewalk.com/wp-content/uploads/2016/04/16_US_FSI_Executive_Summary.pdf
4 After a wealth transfer, around 66% of children do not stay with the same advisor their parents used, and up to 70% of widows do the same once they inherit wealth. Source: InvestmentNews, July 13, 2015: "The Great Wealth Transfer is Coming, Putting Advisers at Risk"; CNBC October 11, 2014, "For Some Widows, Breaking Up with an Advisor is Easy to Do".

This challenge—wealth transfer—is a huge opportunity for advisors as money is in motion. And a digital offering can be the perfect bridge to building a relationship to the clients of the future.

Given today's advisor backdrop, only 8% of advisory clients are 40 years or younger[5], and merely 20% of advisors are targeting younger family members of their existing clients[6]. To sustain and grow their practices, advisors must reposition their firms to meet the next generation's expectations for high-level digital experiences that deliver the training, education, and comprehensive services they want and need. This includes hiring the next generation advisors to attract and serve a younger clientele.

Technology powered advice—every step of the way—fits these client segments.

Challenge: Pre-Retirees

As clients approach retirement, they want engaging, intuitive, and interactive technology to inform their decision making and provide immediate answers to what-if scenarios. And that includes access to guaranteed products, income generating investments, and health care management options. Yet, there are more than 30 million households approaching retirement with insufficient assets to merit personal advice based on advisors' asset minimums, which may be $250,000 or more[7].

Challenge: It's a Three-Tiered Approach

The three-tiered approach—traditional, hybrid, digital only—really amounts to a segmenting strategy. Some clients, who may not be as adept at using digital tools, will still avail themselves of the traditional, one-on-one advisor relationship despite the higher cost. The mass affluent may embrace a combination of an advisor and digital solution because they prefer not to commit time, energy, and fees associated with an advisory relationship. Gen X and Millennials may prefer only a digital experience, because they gather and curate information that way. Advisors who think this group can be swayed by lunches and golf outings are missing the boat.

Advisors who strategically meet this group's needs for a compelling digital experience may be rewarded with a long-term advisory relationship.

[5] Cerulli Advisor Metrics 2015
[6] InvestmentNews, July, 13, 2015: "The Great Wealth Transfer is Coming, Putting Advisers at Risk"
[7] Cerulli 2015 U.S. Retail Investor Advice Relationships

Challenge: Millennials Want a Digital Experience

Millennials were weaned on technology and social media, and they want nothing less when it comes to their financial lives. They prize ease of use and convenience over more traditional advisory options. They operate 24/7 from their mobile phone, expect accessibility on their terms—when it suits them, from whatever device they choose, and in a way that makes sense to them—rather than being dependent on an advisor's office hours. And they trust technology more than humans. They are accustomed to using Yelp to find the perfect places to eat, and you can be sure they will be looking at on-line resources to uncover the best advice providers and how their peers evaluate them.

Millennial investors feel closer to their financial advisors when connected through **social media***

* GlobalEdge, 2015

Number one on the list of demands is a holistic view of their financial life, and data aggregation is the solution to that requirement. Second, the experience must be engaging—with personal data, compelling education, peer comparisons, and content that is simple to understand. They learn through gamification.

Challenge: The Influence of the DOL Fiduciary Rule

It is technology that will pave the way for meeting requirements under the DOL Fiduciary Rule, as solutions will be incorporated all along the investment and reporting process.

Technology will help firms to service small accounts that would otherwise be "orphaned."

A digital solution can help advisors readily facilitate these accounts with an on-line technology process that standardizes the way they work and interact with clients. The digital portal's appeal is its structure that generates proposals, documents activity, computes fees, and satisfies compliance requirements. It also can capture, execute, track, and store service requests.

A digitally empowered wealth management platform provides the ability to capture and record data so that when a need arises, such as a SEC audit, the information is there.

Implementing a Plan

Advisory firms rethinking their approach to consumer-centric digital solutions will want to gravitate toward highly-engaging tools that meet the demands of different client segments. A successful transition includes the following eight steps that comprise a path toward embracing digital.

Step 1:

Understand the technology resources

Research shows that firms with technology integration tend to have nearly twice the level of client assets as firms without it, and its affiliated advisors earn higher levels of compensation[8]. If they aren't already, advisors must first become comfortable with technology, and then learn how to apply it to their practices. They can begin by asking their platform provider for a demo of current and pending technology enhancements. Fintech firms are developing new techniques to drive client engagement, and they are eager to show their applications.

What Are the Different Market Segments?

- **Baby Boomers**—The generation born during the post-World War II period, with birth dates between 1946 - 1964
- **Gen X**—The generation born between 1965 through the early 1980s
- **Millennials**—The generation born between 1982 and 2002
- **Silent Generation**—The generation born between 1928 and 1945
- **Mass Affluent**—A group defined by assets and income, rather than birth year, which typically range from $100,000 to $1,000,000 of liquid financial assets, or an annual household income over $75,000

Advisors need to become familiar with the definitions of basic terms the digital industry uses. Here are some standard terms:

- **Fintech**—The segment of technology that is disrupting sectors such as mobile payments, money transfers, loans, fundraising, and asset management
- **Digital disruption**—Changes in the competitive environment that result from the use of digital technology or established competitors that were never actually competitors before
- **SSO**—Single sign on. A method to move from one website to another without signing in again.
- **E-signatures**—A coded message that uses Public Key Infrastructure (PKI) to securely associate a signer with a document in a recorded transaction
- **FinApps**—Financial applications that often appear on mobile devices

[8] Aite. Whitepaper (April 2013): RIA Productivity and Profitability: Integration Pays. Page 3.

- **Consumer permissioned data aggregation**—Information gathered to target the selling of goods and services based on the consumer's granting consent in advance to receive the marketing information
- **Blockchain**—A data structure based on cryptography to create and share a secure, digital ledger of financial transactions without the need for a central authority
- **Smart learning**—The use of technology to gather data providers can use to better identify both opportunities and threats, determine strategic direction, develop tactical plans, and communicate and collaborate with clients [9]
- **Straight-through processing**—(STP) An initiative used by financial institutions to conduct capital markets and payment transactions electronically without the need for re-keying or manual intervention
- **Robo advisor**—An on-line wealth management service that provides automated, algorithm-based financial advice without the use of human planners or portfolio managers.
- **Document vault**—An electronic document management system that creates digital replicas of all documentation and then indexes, archives, retrieves, and sends the images electronically as needed
- **Predictive analytics**—The ability to employ techniques such as data mining, statistics, modeling, machine learning, and artificial intelligence to analyze current data and make predictions about the future

Step 2:

Segment the business

Advisors need to examine their business, with a view toward building a process to systemize and craft solutions to address the challenges of each segment. It begins with defining the firm's strengths and articulating its value proposition. It also consists of a thorough understanding of their client base: What are my client's needs? How satisfied are they? How do they define excellent service? Are they making referrals? If not, why? Which ones are most profitable?

Segmenting makes it easier for advisors to understand clients in a deeper way, and use the right technology tools, investment strategies, and marketing tactics to engage with them.

Not only will advisors need to know what clients want today, the savvy advisor will know how to predict what a consumer wants before the consumer does (i.e. predictive analytics and smart learning).

- **Baby Boomers:** Research shows that Baby Boomers are projected to move nearly $500 Billion in self-directed assets to wire houses and broker dealers, independent consultants, and registered investment advisors.[10] Many of them are considered Mass Affluent, with close

9 http://denovati.com/smart-learning
10 WealthManagement.com and A.T. Kearney April 20, 2016, "Where's the Money Going in 2020? Six Trends driving Wealth Flows"

to $9 Trillion in assets and an average age of 56. With household income around $118,000 annually, a digital option is a cost-effective vehicle to give them the answers they need to the issues they face in their pre-retirement years.[11]

- **Gen X:** Gen Xers are entering their most productive years in which their personal savings and portfolio returns will add substantially to their balance sheet. Yet, they are not saving as much as they should, so they will benefit from guidance on 401K and catchup contributions. They represent a significant opportunity set for advisors to provide solutions and build lasting relationships.
- **Millennials:** Millennials are not comfortable with their parents' advisors. Advisors who want a relationship with them must approach them in an engaging and digitally savvy way. It's critical to understand what their goals are. Are they paying off school loans or saving for a house? Advisors need to help them solve their immediate budgeting needs versus saving for retirement. In fact, focusing on retirement would be a disconnect with this group vis-a-vis their most pressing needs. It's an automatic "swipe left" for Millennials.

Step 3:

Use the Digital Tool Set

By 2020, digital advice providers are expected to gain $800 billion in new assets from investors with no current advisor solution, and about $500 billion in assets transferred from traditional advisors, highlighting the growing demand for digital advice tools[12]. The client experience should be based on simple financial planning logic and ask a series of questions to tease out an investor's fears and thoughts about risk and return. Ideally, the tool will generate a goals-based plan to chart the course for investors. This plan becomes the guidepost that helps investors stay the course and not make hasty decisions during periods of market volatility.

Creating the right client experience is paramount to success. So much so that many platforms are looking to incorporate theories from behavioral finance within their investor portals, to be sure they provide a compelling environment.

The Digital Tool Set:

- Marketing and engagement techniques
- Budgeting, cash flow, net worth applications
- Data aggregation
- Goals-based planning
- Quick portfolio view
- Self-serve investing
- Simplified portfolio selection Online help tools
- Document vault
- E-signature for account opening
- ACH transfer
- Tax-efficiency solutions

[11] http://www.ixicorp.com/wp-content/uploads/2014/06/June-2014-DYK-Graphic-for-Web.jpg
http://www.ixicorp.com/wp-content/uploads/2013/08/Pie-Chart-August-Financial-DYK-Web-Version1.jpg
[12] WealthManagement.com and A.T. Kearney, April 20, 2016, "Where's the Money Going in 2020? Six Trends Driving Wealth Flows"

Data aggregation capabilities foster a view of the client's complete financial picture, including those assets and liabilities held elsewhere. This is arguably the best way to provide advice—a holistic view of a client's wealth picture which lays the proper groundwork to start the process. It is the first step to becoming the trusted advisor and potentially consolidating all those assets under one roof. Using data analytics to better understand and direct targeted services to their clients can help advisors forge deeper client relationships by moving up the curve from a transactional, information-management orientation to one that anticipates their needs and wants, and delivers customized, actionable, and timely solutions.

A digital marketing presence can incorporate newsletters, market updates, automated email alerts, social media, and educational messaging to keep clients informed. But digital marketing can be so much more, with functionality to easily tailor all kinds of news and videos that resonate with specific clients' touchpoints. It gives advisors flexibility to customize information that is relevant to clients and germane to their current financial needs. The key is to engage and convert the prospect to a client and keep them coming back for more.

Step 4:

Define an operating model

It is important that advisors understand their core competency and the value proposition they bring to clients so they can focus on areas that are most productive, like spending more time on client-facing activities, and less time devoted to operational aspects of the business. This is mission critical: Today's advisor spends about 40% of the day in non-client-facing activities[13].

Having an integrated technology platform is the way around this challenge. The back office tasks are covered, and even middle-office tasks are streamlined. The wealth management platform provides a structure, be it fee-based or a hybrid commission/fee framework, to create standardized processes to drive scale and efficiency and free up advisor time to spend with clients.

Advisors who add a digital advice component can broaden their services to offer the best of both worlds—hands on and digital—to satisfy today's digitally savvy customers who seek answers and solutions from an advisor who can help them. It's an effective way to extend the advisor's reach and services.

Empower your wealth management platform with a digital engine, but make sure it is integrated.

[13] Cerulli Advisor Metrics 2015

Step 5:

Outline advice options—Traditional, Advisor-Assisted, Digital Only

Three advice models will give advisors the flexibility to manage clients across generations and wealth tiers.

- **Traditional:** The traditional model equals a more personalized solution customized for the individual. Clients have varied needs, and advisors can tailor their advice accordingly, and decide how best to allocate the time they spend with each type of client. For example, retirees are most concerned about how much income they will require when they stop working. A more involved client situation may dictate whether a comprehensive financial plan is warranted that includes a combination of retirement income solutions, or a healthcare and wellness option, and the costs associated with each.
- **Advisor-Assisted:** Uses digital predominantly, but when a customized need arises that requires human advice, the advisor steps in. The ideal wealth management platform integrates tools for both the traditional and the digital model. That way, an advisor can drop in at any point in the client's journey and create optionality for the client.
- **Digital:** Younger clients, or those with fewer assets, are ideal for a lower-cost digital option with portfolios pre-constructed by risk tolerance, as it is not cost effective for advisors to spend time engaging with them through telephone calls or meetings. With a digital offering, advisors can schedule less-frequent personal contact and opt instead for an annual review. Tools can be programmed to initiate a pop up reminder when asset levels reach a higher threshold, signaling personal contact with the advisor may be warranted. Note: Although this segment does not require hands-on time, the digital experience must be engaging, thoughtful, and designed to anticipate and respond to the client's needs.

Step 6:

Prepare for fee transparency

Building trust means full disclosure. Millennials require it to engage, and the DOL Fiduciary Rule is mandating it in retirement accounts. Transparency in fees is a big selling point for digital advice platforms. Advisors should not be afraid to discuss their fees and the value they provide to clients in return. Clients need to know the fees and other expenses to expect, and this information must be concrete and specific.

The fee discussion should start at the beginning of a relationship. Advisors should conduct a needs analysis to see what services their clients want. The goal is for clients to feel that what they are paying for is fair, reasonable, and commensurate with the value provided by an advisor. When advisors are not forthcoming about fees, client satisfaction is likely to suffer.

Some digital advice providers are confusing the consumer, because they focus the discussion on cost instead of value. Consumers and advisors need to be clear about what costs are being paid for what menu of services. Fee compression is not happening because of robos—fee compression occurs at firms that have not provided value to consumers.

Step 7:

Know the economics

Every business needs to know what it costs to serve a client, but unfortunately, it is not always readily apparent to advisors. It depends on the advisor’s model –independent broker dealer, registered investment advisor, bank broker dealer, or other.

The operational eco-system required to manage a digital offering will have costs associated with it. However, an investment in this structure will pay dividends, as advisors will be able to manage more clients. The objective is to grow and achieve scale. The enhanced operational efficiencies of an investor portal include: automated workflows for administrative tasks, risk monitoring and compliance tools, and client engagement features. Other features that can streamline processes include eSignature capabilities, cloud-based portfolio management, and rebalancing software.

Time spent within each segment should be estimated, so that the costs for each group can be measured. For example, the digital model calls for tech savvy staff, whereas the traditional advisor model will likely have more experienced, higher-cost professionals. It is important to understand the inflection points, such as when an advisor-assisted client will need human interaction. Track and plan for these points, and assign a cost to them. Customized solutions for more complex clients, for example tax planning, charitable giving, and estate planning, may be billed at a professional services rate. Once the business has been segmented, and the service components defined, then the costs to serve each group can be projected.

Step 8:

Create a timeline to transform the business

In the rush to become all things digital, advisors should be realistic about the time it takes to implement a digital strategy. Set aside time to think through a growth strategy, define a vision, establish goals for the business, and develop an execution plan to segment clients and map their planning and investment needs. Building an engaging and interactive digital experience, based on behavioral finance characteristics, is vital to retaining existing clients and attracting new ones from the next generation.

Doing so also makes sense from a succession planning standpoint, because segmenting is the first step in keeping the client base "evergreen." Unless advisors can attract younger clients, they may see the value of their practice decline in the eyes of potential buyers. A book of business heavily skewed to 60- or 70-somethings decreases the practice multiple. This is why it's imperative to have a client base that is well distributed across generations.

Get Started

Advisors need to:

- Understand the landscape ahead and embrace digital as an opportunity to grow.
- Focus on clients' needs and add technology depth to the team to provide new services.
- Focus on client acquisition strategies to ensure growth.
- Identify partners to provide the digital and operational backbone.
- Make commitments with partners and technology that offer flexibility.

The financial industry has been behind the curve in addressing consumers' needs. It took a digital revolution to provide the pathway for advisors to engage with their clients in a new way. Advisors now have a route forward to create a digital advice solution for their firms. Huge decisions aren't required—they can start by making small ones. But they must GET STARTED—they cannot sit on the sidelines. The advisor's future and profitability hinge on embracing this wealth management opportunity.

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