DYNAMIC ASSET

YOUR GUIDE TO A THRIVING FINANCIAL ADVISORY BUSINESS

A TRANSFORMATIONAL APPROACH FOR AMBITIOUS ADVICE BUSINESSES

INTRODUCTION

The business of financial planning and advice is at a crossroads. Consumers, governments and regulators are demanding a higher level of delivery and performance from advice firms. A new standard of 'clients' best interest' is emerging.

The changing landscape is applying pressure to the traditional advice model, which needs to adjust to providing client-centric service delivery while accelerating business growth and improving efficiency.

This guide explores the most common goals of small- to medium-sized financial planning firms and the obstacles they face in achieving them. More importantly, we look at best-of-breed solutions that will help advisers to meet their primary business needs.

The barriers to growth in the existing advisor model are well known

WHAT A FINANCIAL ADVISORY BUSINESS NEEDS

Regardless of size, all financial planning business owners have certain fundamental requirements. These include:

- Profitable growth – grow revenue ahead of expenses
- Scalability – an ability to increase the number of clients serviced
- A differentiated value proposition – breaking free of the traditional model, which has been discredited in recent years
- Improved retention and referrals – deeper engagement and meaningful client relationships to reduce turnover and business risk
- Access to specialist knowledge and efficient systems that allow advisers to focus on their core skills to build their business
- Simplified compliance in an increasingly complex regulatory world
- To run a business that does good for clients and is enjoyable for advisers and staff.

However, the existing advisor model exhibits some common barriers to growth, including:

- Time constraints due to the diversity of work undertaken. The adviser has become a jack of all trades, working 'in' the business, rather than 'on' the business
- Client capacity limits; these, in turn, limit revenue and scale
- The absence of a differentiated value proposition to attract clients
- The tension between providing strategic versus investment advice, knowing it is difficult to do both without scale and adequate resources
- Passive portfolio management caused by typical review cycles, Statement of Advice requirements, existing platform offerings and administration workloads
- A dearth of adequate technology and tools to support effective Goals Based Advice
- Few true-to-label Goals Based Investment solutions to underpin the provision of Goals- Based Advice
- Inability to find quality service providers that deliver to the standards clients demand to alleviate business risk
- Developing processes and offerings that magnify the adviser's strengths and minimise weaknesses
- A lack of time and resources to develop ideas and keep up with industry developments to ensure best practice. .

Regardless of the size, every business will, from time-to-time, think about these goals and consider how to achieve them most effectively and efficiently.

Some advisory firms will successfully tackle these barriers, while others may take years to build and develop a satisfactory business. The vast majority find these challenges difficult to overcome, opting for the status quo due to a lack of alternatives.

However, recent developments have seen the advent of turn-key solutions that can help advice firms achieve greater profitability. The journey incorporates a number of elements, including selecting the right service offering, complying with evolving regulations and identifying appropriate technological solutions for service provision.

Highly successful businesses work to their core strengths and bring in or outsource the resources required to deliver in non-core areas

FINDING YOUR VALUE PROPOSITION

Developing a sustainable business requires owners to first assess their core competencies and the kind of service they wish to provide to their target clientele. In a financial planning context, there is an increasingly clear distinction between advisers that want to provide ‘strategic advice’ and those that chose to focus on ‘investment advice’; however, the delivery of strategic advice entails a distinct service offering and value proposition, resulting in a differentiated business plan and set-up.

This is because strategic advisers tend to be more holistic and require broad-based knowledge and versatile systems, while investment advisers have a narrower focus on markets, research, products and portfolio management.

Successful businesses focus on their core strengths and bring in or outsource the resources required to deliver in non-core areas. Planners have been doing this for years with accountants, lawyers, investment managers and other non-core services. While many are attracted to the idea of bringing services in-house to develop additional revenue streams and build business value, this can require scale and should be weighed against the value that is lost by dedicating time and resources to building new business lines. Advisors should also ensure that the vertical integration of new services does not introduce conflicts of interest.

Strategic financial planners often have insufficient time, resources or scale to compete with professional managers in the delivery of investment and portfolio management services to a standard that meets their client’s best interests. An adviser benchmark study conducted by Bloomberg found that an ‘elite’ strategic adviser works around 50 hours a week, spending at least half of their time in front of clients and prospects. The remaining time is spent on continuing education (6%), employee training and management (12%), practice management (8%) and office admin and back office (5%). This leaves little time for investment research, meeting managers, building portfolios or general portfolio management.

This has led advisers to search for managed portfolio solutions that can be implemented quickly and efficiently across a platform to remain competitive against dedicated professional managers, without having to spend the time or resources to do everything in-house. Research houses and asset consultants are increasingly offering such services, but advisers still need to narrow these down to find a solution that best reflects their investment philosophy, serves the best interests of clients and can be implemented or administered cost-effectively.

IT BEGINS WITH A CLEAR INVESTMENT PHILOSOPHY

Identifying the advice firm's investment philosophy is the ideal starting place for developing a sustainable and fulfilling business. It is important that the advice provided to clients is genuinely founded on the adviser's belief that it is in the clients' best interest.

Many of the world's leading investors say that nothing is more critical to long-term success than a clear philosophy that articulates the 'why' of their investment decisions to clients in times of market upheaval. Such a philosophy should enable clients to control their emotions, shut out market noise and focus on the long term.

An investment philosophy can usually be derived from two mainstream approaches.

RISK PROFILING OR STRATEGIC ASSET ALLOCATION (SAA) TYPICALLY BELIEVES:	GOALS BASED INVESTING OR DYNAMIC ASSET ALLOCATION (DAA) TYPICALLY BELIEVES:
Risk profiling is the most appropriate way to determine an investment strategy	Investors' needs and goals are the most appropriate way to determine an investment strategy. Investors have numerous goals, so there is no one strategy or profile that will suit all their needs
Markets are always efficient and repeatable. Modern Portfolio Theory can be used to build optimal portfolios based on historical data	The world is continually changing, so a flexible and broad-ranging asset allocation can best derive value or limit capital losses
Markets will always mean revert, suggesting there is little value in managing asset allocation	Markets are not always efficient, with risk-reward opportunities arising from time-to-time
History is the best guide to future outcomes	Forward-looking estimates and projections are more relevant than historical data
Investors are always adequately rewarded for risk, so a long-term strategic (or static) asset allocation is best	Protecting capital is of paramount importance
Risk means the volatility of capital	Risk means the probability of not meeting an investor's goals

Advisers have used risk profiling and the SAA approach for decades. However, there is a growing awareness that such an approach may not always work and therefore, not in the client's best interests. This is discussed by Dynamic Asset in their article "Why the Investment Profile Falls Short in Investment Advice" and shown by Schroders in their paper "Why SAA is Flawed."

Current market conditions are magnifying uncertainty over the suitability of SAA. Many in the industry are openly questioning whether a traditional SAA portfolio is likely to generate the returns needed by investors. This was well articulated by Graham Hand in the CuffeLinks newsletter in May 2020 in their article "The vibe of future returns: tell 'em they're dreaming."

Many of the world's leading investors will tell you that nothing is more critical to long-term investment success than a clear investment philosophy

A FOCUS ON CLIENT GOALS PROMOTES REGULATORY COMPLIANCE

A sustainable business that maximises resale value must enshrine compliance and corporate governance. Although all advice businesses aim to meet the needs of their clients, this focus intensified following the mandatory adoption of the Future of Financial Advice reforms in 2013. The need for advice to be in the client's best interest and meet stated goals is now enshrined in the Corporations Act and the Financial Adviser Standards and Ethics Authority (FASEA) Code of Ethics.

In addition, the Australian Securities and Investments Commission has released draft guidance on new consumer-centric financial product design and distribution obligations, which are to apply from April 2021. The draft guidance discusses "an increased responsibility to design products that are fit for purpose and deliver good consumer outcomes" and states that products must be appropriately sold and meet genuine client needs, with continual enhancements to ensure that outcomes are achieved. The obligations will apply to product distributors, including financial planners.

The new requirements provide astute financial advisers with an opportunity to get a head start in meeting the obligations and gain an edge by achieving superior client outcomes and improving their business practice. By ensuring their investment philosophy is aligned with clients' best interests, advisers can be confident in the sustainability of their business model within the changing regulatory environment.

TECHNOLOGY IS ENABLING BETTER BUSINESS

Technology can be a great enabler. Consumers and advice firms can access and utilise systems and services faster and more cost-effectively than ever before. Fast and effective access to a specialised service can often help evolve the service offering and value proposition far more effectively than building that solution from scratch.

This has seen the proliferation of cloud-based offerings available as apps that can plug-and-play into many businesses. A simple example of this in the financial planning industry is the evolution of manually administering assets to then using spreadsheets, platforms and now using administrative services like Managed Discretionary Accounts (MDA's). Likewise, with strategic planning software, client reporting, website, document management systems and client portals.

UNLOCKING EFFICIENCY GAINS WITH MANAGED DISCRETIONARY ACCOUNTS

Advisers are increasingly utilising Managed Discretionary Account (MDA) technology, which has dramatically improved in recent years. Research house, Investment Trends, reveals that 35% of financial advisers recommend a managed account solution to their clients.

Research by Business Health, Institute of Managed Account Professionals (IMAP), Colonial First State and BT on managed accounts found that:

- 87% of practices say they've reduced their administrative workload since investing in a managed account solution

- Managed accounts saved an advice business 14.4 hours a week overall giving the adviser an extra 4.8 hours a week to focus on new revenue-generating activities
- Advisers using managed accounts have on average 7.4 weekly client appointments compared with 6.0 industry-wide
- Firms that currently use managed accounts are generating an average of 32% more than their peers.

Other benefits of managed accounts to advice firms include:

- Improved efficiency, as there is no requirement to issue a Record of Advice when making changes to client portfolios

- A lower administrative burden for both clients and advisers, as advisers no longer need to chase clients for signatures

- Equity; all clients are treated equally when portfolio changes are made. This is an essential consideration under the FASEA Code of Ethics

- Cost savings achieved from the simultaneous implementation of portfolio changes across an adviser's client base.

- Modelling by Philo Capital Advisers showed that a one-week delay in implementing investment changes cost an average of 0.19% of portfolio returns over a year, or an average 0.90% a year when the delay was within a quarterly review cycle.

These are meaningful improvements for any business, attractive to any owner looking to get scale and improve profits and business value.

Not all advisers are aware of the available options, legal requirements or how to implement managed accounts without significant business disruption. However, the service has evolved, making the process easier than ever before. For example, IMAP (The Institute of Managed Account Professionals) put out a useful report on Alternative Diversified Portfolio Options and another on the Features, Benefits and Risks of Managed Accounts. The Financial Standard released a piece on Redefining your Value Proposition that talks through various considerations, which may be a useful reference.

CHANGING CLIENT EXPECTATIONS

Societal expectations are also changing dramatically. In a post-Hayne world where clients are increasingly discerning and have information available at their fingertips, advisers need to provide a value proposition that clients can both understand and identify with. In short, clients are more demanding of advisers to deliver strategies and solutions that match their specific needs. Advisers recognised as being more client-focused typically have more highly satisfied clients and receive the recognition and kudos they deserve.

As EY states in their Goals Based Planning paper; "... savvy financial advisors are using Goals Based Planning as a firm-wide strategy to attract clients, gain their trust and build long-term relationships".

Improved client satisfaction is linked directly to increased retention and referrals, which leads to higher business growth and profitability. Clients tend to have four main expectations of their investments:

1. Capital Protection – everyone likes making money, but they don't like losing it. So, keeping it safe is a priority, particularly for older clients;

2. Understanding – why were particular investments being made and how did they relate to the client's specific circumstances

3. Transparency – they wanted access to the detail. Not necessarily because they understood it all, but they just wanted to know they could if they wanted to.

4. Simplicity – they wanted to achieve their goals with the minimum amount of fuss.

BUILDING SCALE WHILE OFFERING BESPOKE SOLUTIONS

It is essential to offer customised solutions that meet each client's individual needs. Not only do advisers want to demonstrate the value of their services and meet the expectations of clients, they also need to keep up with the evolving regulatory environment. Customised solutions are undermined by the risk profile approach, as no one profile or portfolio will be suitable across differing clients' needs. Clients expect a nuanced approach, with fit-for-purpose investment portfolios that are designed to meet their investment goals.

However, it can be challenging to achieve scale while building, executing and managing discreet investment portfolios for each client, particularly when advisers only see clients periodically at a review. In the meantime, market conditions may change and recommendations become outdated.

This challenge can be overcome with access to a range of discreet portfolios that have various targeted mandates and can be matched to individual client goals or blended in such a way that the overall portfolio better aligns with each clients' needs. The right collection of portfolios across superannuation and non-superannuation can allow advice firms to efficiently achieve mass customisation while also meeting regulatory requirements.

At the same time, managed accounts offer clients full visibility of the underlying assets that make up their portfolios, delivering a deeper understanding of the basis for their investments. This helps to overcome the challenges associated with the behavioural psychology of retail investors, which often arise during market downturns. It is difficult for clients to see value and have buy-in if they do not understand their investments, either strategically or at the portfolio level, and advisers have limited time to discuss the specific details of each client's investments; over a year, it is usually measured in hours. This can leave clients feeling confused and underwhelmed.

In the Seven Steps to Goals Based Financial Planning, David Blanchett of Morningstar summarised it as follows: "Most individuals aren't financial experts. They don't speak in terms of alpha and beta, or even keep up with their accounts daily. However, when the time comes for them to accomplish one of their financial goals – whether it's funding a child's wedding or settling into retirement—they need to know the money will be there.

That's why the profession of financial planning must be built around helping people accomplish their goals. It's not only an opportunity for you to provide better advice to individuals; it's a way for you to speak their language and make closer, long-lasting connections with your clients".

David further suggests that "an optimal, goals-based strategy can add more than 15% in utility-adjusted wealth". That's a significant number that has a meaningful impact on a client in helping them achieve their goals and clearly in their best interests.

THE COMPLETE SOLUTION

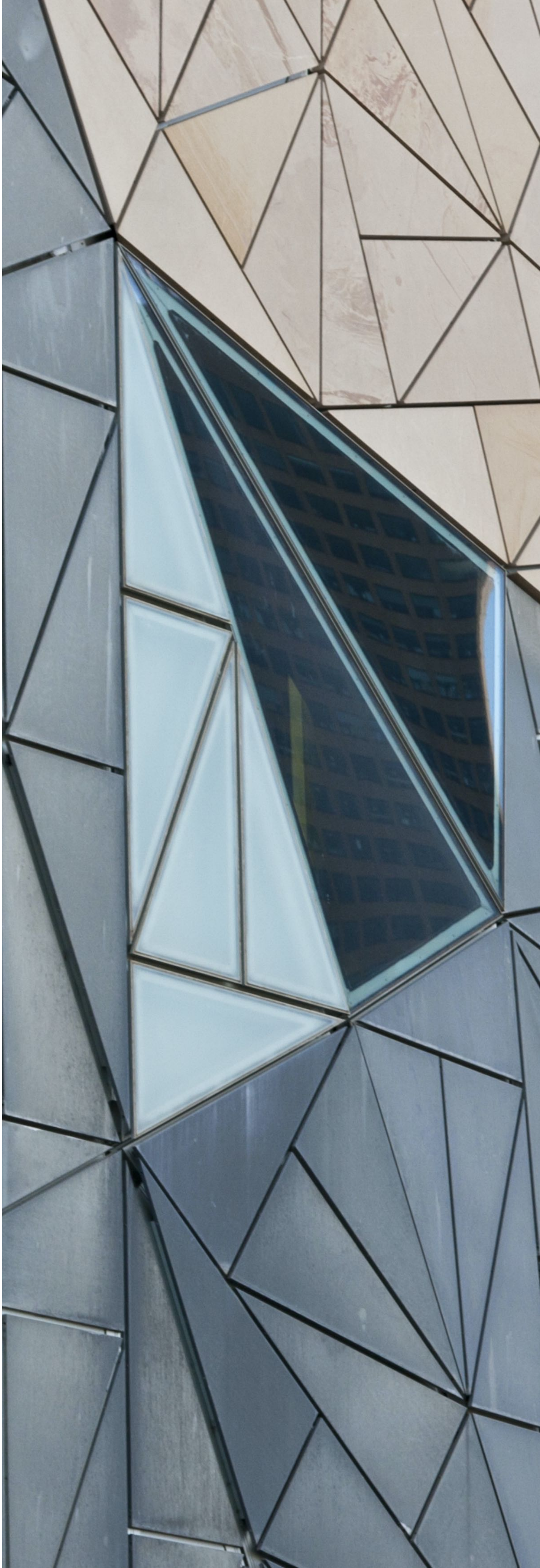
Advice firms that wish to maximise their business potential and meet clients' best interests would benefit from a whole of business solution that serves to overcome all the identified challenges. An effective solution should:

- Boost profits
- Deliver scalable execution
- Offer a differentiated value proposition
- Improve client understanding and engagement, leading to more referrals
- Provide access to specialised knowledge that complements and enhances core business skills
- Uncover technology and tools that help to deliver the advice that clients desire
- Allow for bespoke and scalable portfolio solutions that match client goals
- Reduce costs and offer back-office support
- Simplify and manage risk in an increasingly complex regulatory environment.

The breadth and complexity of significant developments in the advisory industry, regulatory environment, investment markets and consumer expectations can be daunting. How can advisers take advantage of these opportunities – and still manage the business on a day-to-day basis?

Dynamic Asset Consulting offers the only whole-of-business solution in Australia that helps advice firms overcome all of these common challenges, including providing multi-faceted portfolio management options within and outside of superannuation. The turn-key solution integrates seamlessly into the background of your advisory business. It was built by planners for planners and can provide everything you need to deliver a best-of-breed outcome for you and your clients.

There is a better way.



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