Effectively transitioning to a FEE-BASED BUSINESS

Advisors who quickly transition to a fee-based business are realizing faster growth in revenue and are increasing the per-client value of their book

This shouldn't come as too much of a surprise, but we're in the midst of a steady and deliberate shift to a fee-based model. While many investment firms have encouraged advisors to transition their accounts and households to a fee-based approach to pricing, financial advisors tend to lack guidance as to what the best approach is in making the transition, and what the financial impact might be.

By analyzing and researching our exclusive aggregated retail brokerage database of 40,000 advisor books of business, 7 million investors and over $3.5 trillion in investment assets, we have found that advisors who aggressively move a significant portion of their assets under management into fee-based accounts benefit from an increase in assets, a higher return on assets and ultimately greater revenues.

From 2009 to 2012, assets in fee and managed programs have risen from 21 per cent to 28 per cent, though not all advisors are making the transition, and those that are,range significantly in their pace of transition. Still, 70 per cent of advisors have increased their percentage of fee assets over this period, and 21 per cent have increased by at least 10 per cent.

Today, 91 per cent of advisors have at least one fee account in their book of business. Interestingly only 1 per cent of advisors have 90 per cent or more of their client assets solely in fee accounts. So-called hybrid households, in which a household has at least one fee-based account and one transactional account, are also growing quickly and are up 41 per cent since 2009.

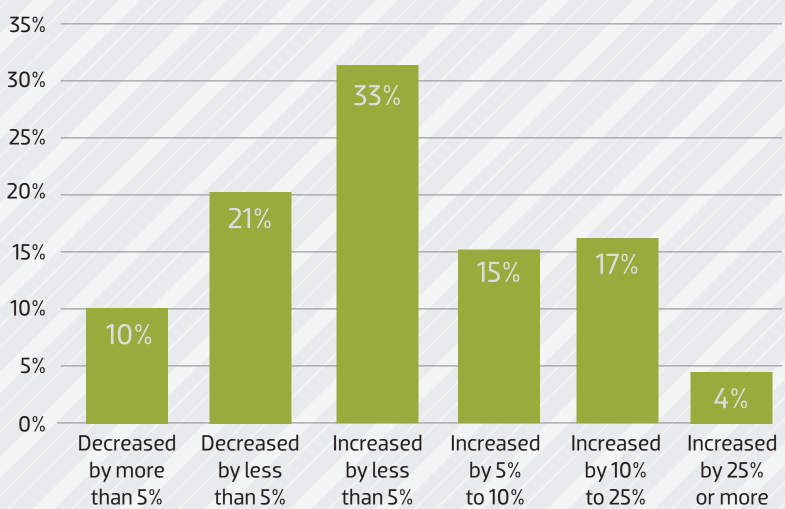
Although advisors often think of themselves as either "fee-based" or "transactional," the reality is that most advisors are a little of both. While the trend towards fee-based business is clear, as the market matures, both clients and wealth management firms are demanding that advisors offer a variety of products and services to satisfy a wide range of client needs.

Our analysis indicates that fee-based accounts are more attractive for advisors almost across the board. The average fee-based account is 46 per cent larger than the average transactional account. It also generates more than three times the revenue, an average $2,900 per fee-based account compared to $870 for a transactional-based one. Households with at least one fee-based account generate a return on assets that is 40 to 70 basis points higher than households that are purely transactional.

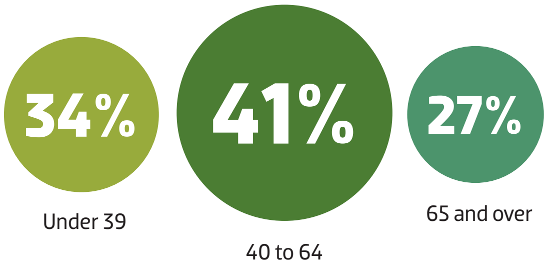
Interestingly, both the age of the client and the advisor appear to play a role in the degree of interest in fee-based accounts. Clients between the ages of 40 and 64 have exhibited the greatest propensity to use fee-based accounts.

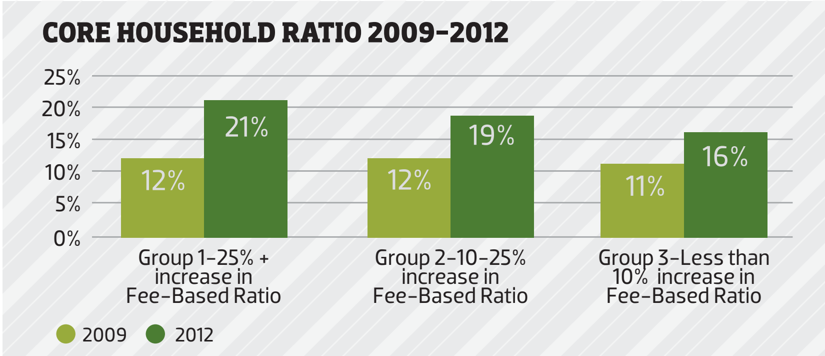
At the same time, however, less experienced

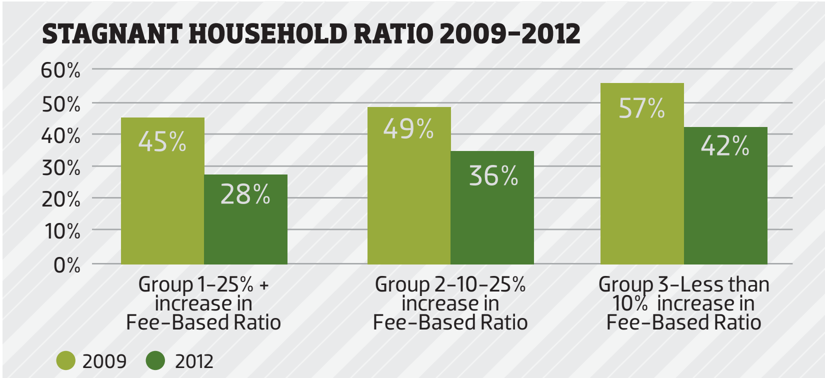
DISTRIBUTION OF ADVISORS BY PERCENTAGE CHANGE IN FEE-BASED ASSET RATIO 2009-2012



PERCENTAGE OF HOUSEHOLDS, WITH $250,000 TO 500,000 IN ASSETS, WITH FEE-BASED ACCOUNTS BY HOUSEHOLD AGE 2012







advisors seem to be much more eager to embrace fee-based business than more senior advisors. The majority of advisors with less than ten years experience have at least 25 per cent of their assets in fee-based accounts, while two-thirds of advisors with more than 20 years of experience have less than 25 per cent of their assets on the fee side.

We also found much of the increase in fee-based assets has come from new accounts – 70 per cent of new fee accounts are from brand new client-advisor relationships, while the remaining one third of new fee-based accounts was opened with existing clients.

Our research clearly shows advisors who most aggressively moved more of their books into fee-based business outperformed their counterparts. Advisors who increased their fee-based ratio of business by at least 25 per cent over the last three years improved the quality of their household mix (the proportion of clients above a certain asset size), their return on assets, and transformed their revenue stream to be more than two thirds recurring. The average advisor in this group saw a 49 per cent increase in assets under management and a 41 per cent increase in recurring revenue. These advisors also almost doubled the percentage of households in their books generating $5,000 or more in annual revenue, while significantly reducing the number of households generating less than $500.

Our data has shown that an aggressive shift in an advisor's business model is an excellent opportunity to assess their client base and align clients with the type of service model they intend to provide.

Advisors have a decision to make – they can "go with the flow" and see their book slowly evolve, relying on investors to demonstrate their interest in a fee-based model before adapting their offerings to serve their clientele; or they can be more aggressive in transitioning their book. Advisors who are more aggressive and move a significant percentage of their assets into fee-based accounts benefit more quickly from higher RoA, revenue, and assets. They also use the opportunity to part ways with small households and reawaken dormant ones.

ADDRESS THE CHANGING CLIENT NEEDS

- Learn to service both fee-based and transactional accounts. Be able to define the features and benefits of both and explain the differences in pricing models;
- Many clients want to have both types of accounts. Learn to spot and capitalize on those opportunities;
- Find the right business mix for your book and plot your course as you transition your book from non-fee to fee;
- An aggressive shift in business model is an excellent opportunity to prune your book of non-strategic clients. Review your client roster and determine which clients might be better suited for a different business model;
- Understand the demographics of your book: young and very old investors may find less appeal in fee products.

And remember, results will be less dramatic and materialize more slowly for advisors who take a reactionary approach. WP

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