

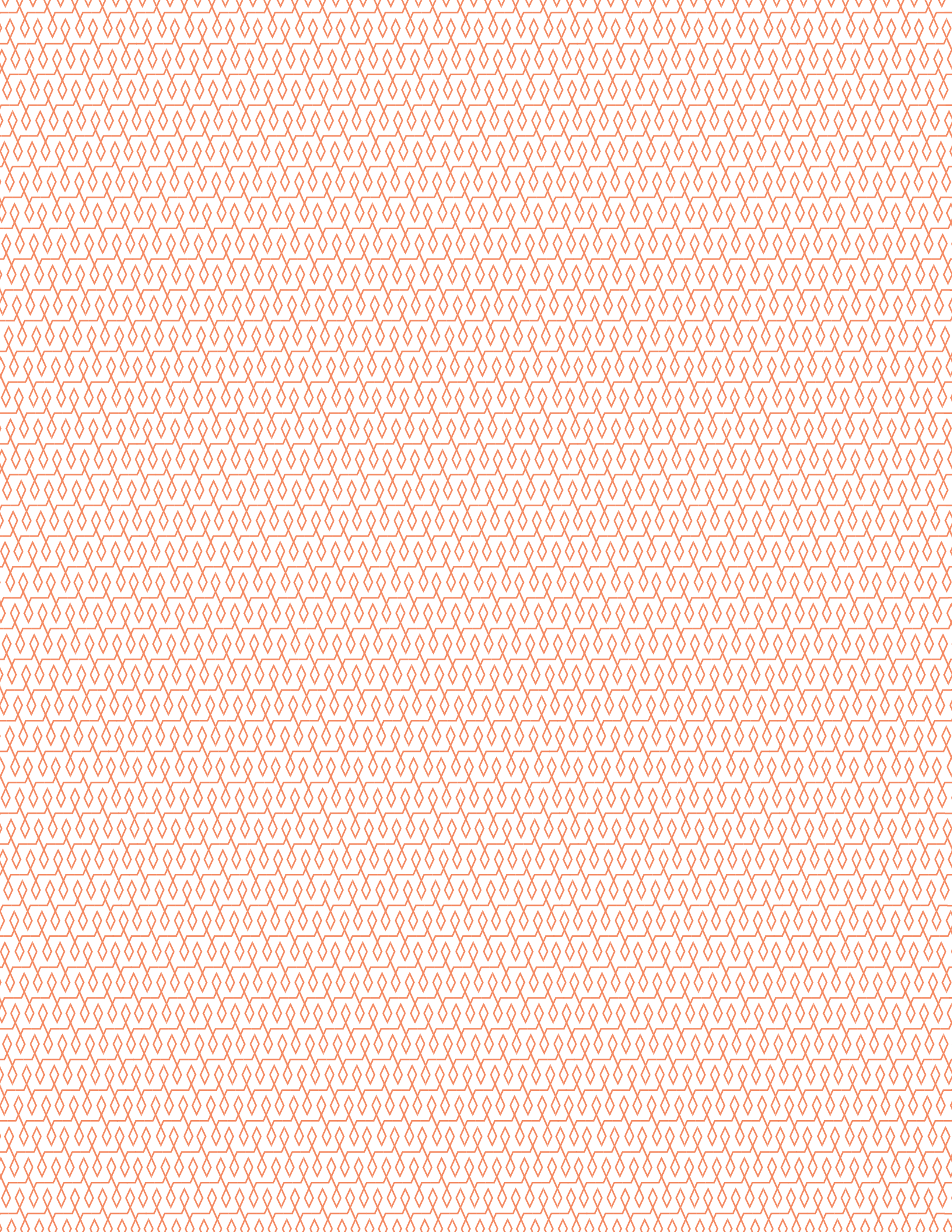


ADVISOR CONSULTING

Building Financial Advisory Business Value Amid the Great Wealth Transfer



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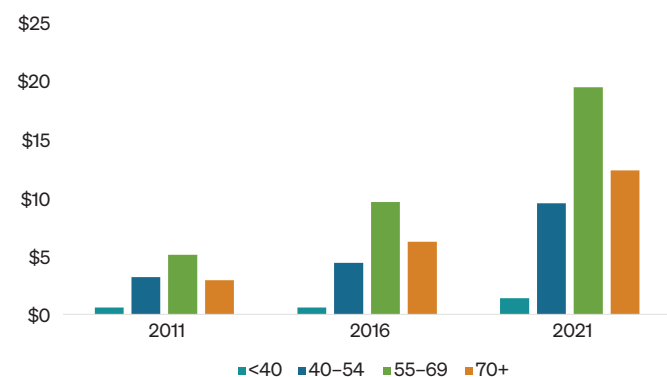


The Changing Landscape

The financial advice industry is beginning to experience the Great Wealth Transfer as an estimated \$70 trillion in assets shifts from older generations (i.e., the Silent Generation and Baby Boomers) to younger generations (Gen X and Gen Y). However, this shift is often portrayed as a momentous event at which point who possesses the assets and who manages them will win. The transition has already begun and will gradually accelerate, requiring financial advisors to adjust their business models to attract and serve a more diverse clientele.

Baby Boomers were the first generation to accumulate wealth and rely less on public (i.e., Social Security) and private (i.e., defined benefit plans) safety nets. With 40+ years of asset gathering and compounding in their rear-view mirror, this generation possesses the most significant percentage of financial wealth. Consequently, the Baby Boomer generation is where financial advisors have focused most of their practice growth over the last several years. As illustrated, in the previous ten years, the long bull market grew the assets of each age group. However, it benefited older investors the most, as the wealth of those aged 55 and older grew at a compound annual growth rate of 15%, compared to 11% for younger investors.

Exhibit 1: Assets by Age Group (\$ Trillions)

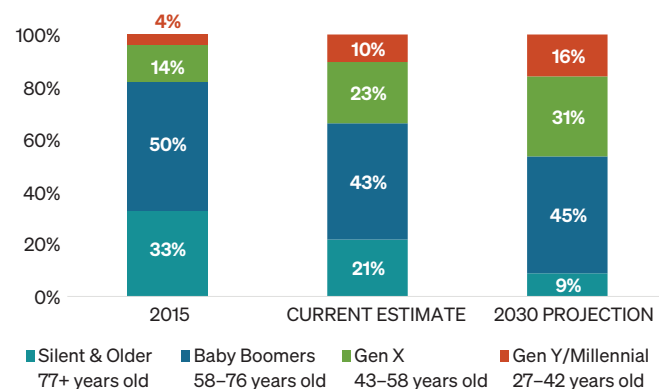


Source: Federal Reserve

The sheer size of the Baby Boomer generation and their higher average assets per client continue to make them an attractive market segment for financial advisors. Concentrating on older investors almost exclusively is a strategy that offers diminishing returns for business growth and value. First, many of these investors have begun, or will soon start, drawing down their assets, while Gen X and Gen Y are still firmly rooted in the accumulation phase. Second, they are invested more conservatively than their younger counterparts and could become even more risk-averse given the recent increase in market volatility. Therefore, they will participate in less upside once the market turns more bullish.

Finally, the passage of time has prompted shifting assets among the generations. Research conducted by Deloitte in 2015 showed that the Baby Boomer and older generations owned 83% of net household wealth; however, the firm projected that by 2030 that proportion would decline to 54%, while Gen X and Gen Y would control 46%.¹ In 2022, halfway through the forecast period, this shift is gradually changing the financial advisory landscape.

Exhibit 2: Share of Household Wealth by Generation



Source: The Future of Wealth in the United States, Deloitte, 2015

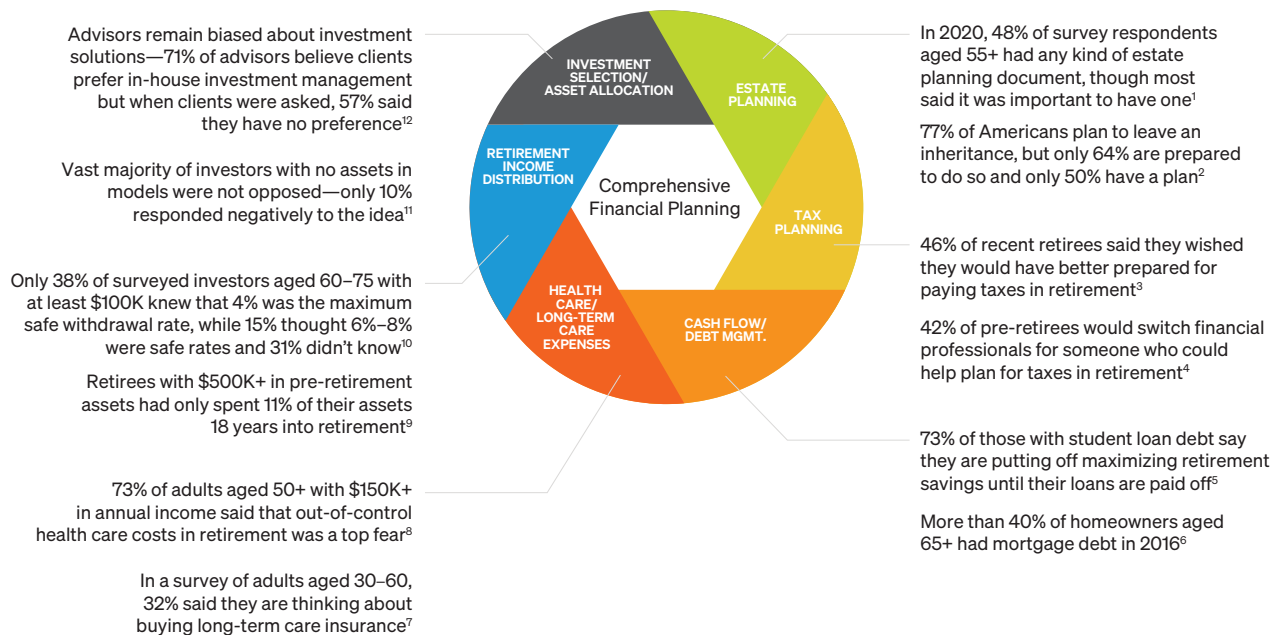
THIS SHIFT IS ALSO CHANGING ADVISOR DEMOGRAPHICS

The financial advisor community mirrors the population in terms of who manages assets. Between 2020 and 2030, more than one-third of financial advisors, who manage 40% of assets, are expected to retire.² The combination of an aging advisor and an aging client, who will bequeath a large percentage of their assets to a younger generation, means that advisory models must evolve to address the changing needs and preferences of younger clients and advisors.

CLIENT NEEDS ARE CHANGING

As illustrated in Exhibit 3, there is growing recognition of the need for tax planning, with a large proportion of retirees saying they wished they had prepared more for taxes in retirement. A similar percentage of pre-retirees indicate that tax planning help is sought-after when choosing a financial advisor. In addition, current and future healthcare costs are weighing on the minds of investors in different generations—as rising healthcare expenses concern those in or approaching retirement. In contrast, younger investors are interested in whether long-term care insurance is worthwhile. Finally, there is a clear, unmet need for estate planning, as many investors do not have a plan in place, even though they intend to leave an inheritance. This is where financial advisors have an opportunity to bridge the needs of existing clients with their beneficiaries by addressing how and when the assets will be passed down and achieving the financial goals of the next generation.

Exhibit 3: The Advisor Role Must Expand to Meet Growing Investor Needs



¹ 2020 Estate Planning and Wills Study, Caring.com

² The Family Wealth Check-up Study, Ameriprise Financial, 2017

³ 2019 Tax-Efficient Retirement Income Survey, The Nationwide Retirement Institute

⁴ Retirement Income and Tax Planning Consumer Survey, National Association of Plan Advisors, 2018

⁵ Student Loan Debt: The Multigenerational Effects on Relationships and Retirement, TIAA and MIT AgeLab, 2019

⁶ Joint Center for Housing Studies at Harvard University

⁷ MassMutual Chronic Care Research Study, 2020

⁸ 2018 Nationwide Health Care and Long-Term Care Consumer Survey, The Nationwide Retirement Institute

⁹ "Spending Patterns in Retirement: Retirees Are Slow to Exhaust Their Assets," EBRI, April 3, 2018

¹⁰ Retirement Income Literacy Survey, The American College of Financial Services, 2017

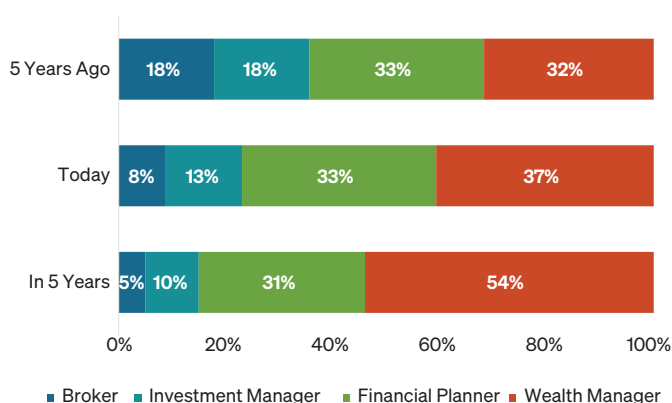
¹¹ Model Portfolio Solutions and the Client Experience, SSgA, 2022

¹² FA Insight Study, TD Ameritrade, 2019

What Advisors Can Do

Financial advisors are beginning to evolve their business models to offer the additional services that clients, notably Gen X and Gen Y clients, want, which can be seen in the changing labels financial advisors place on themselves. Research from FUSE Research Network and [WealthManagement.com](https://www.wealthmanagement.com) shows that advisors are moving away from calling themselves brokers or investment managers and toward labeling themselves, wealth managers.³ The evolving business model of many financial advisors is also evident in the fact that advisors are serving fewer clients but have a higher number of accounts per client, suggesting deeper relationships. However, while broadening the client relationship beyond investing helps with retention—especially when markets decline—advisors have limited capacity. This means the added time spent serving multiple accounts per client poses an opportunity cost—and often that cost is a limited ability to pursue new client relationships.

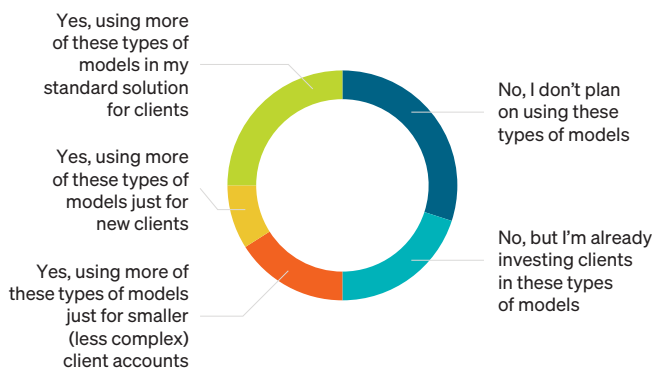
Exhibit 4: How Advisors Define Themselves: Past, Present & Future



Source: Advisor Trend Monitor: Advisor Top Trends for 2021, FUSE Research, [WealthManagement.com](https://www.wealthmanagement.com), March 2021

Exhibit 5: Model Usage

Changes in Home Office and Third-Party Model Use



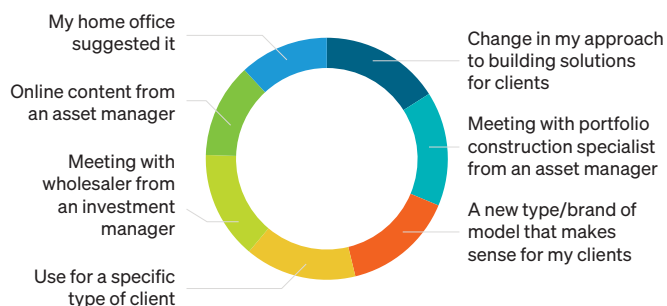
Source: Advisor Trend Monitor: Advisor Top Trends for 2022, FUSE Research, [WealthManagement.com](https://www.wealthmanagement.com), March 2022

PURSUING PRACTICE EFFICIENCY

With so many demands on their time, financial advisors must look for and adopt efficiencies allowing adequate time for servicing existing relationships and growing the business. One area where advisors are gaining efficiency is investment management, as the proliferation of home office and third-party solutions allow them to provide professional management with increasing customization—reducing the need to allocate the lion's share of their time to this function. A recent report from FUSE Research Network and [WealthManagement.com](https://www.wealthmanagement.com) shows the majority of financial advisors in each channel are already using model portfolios to some extent and are self-forecasting that their use will grow. When advisors were asked to indicate how they foresaw their model use changing, of those who anticipate increasing their use, the largest percentage indicated they intend to make models a greater part of their standard client solution.

Following this question, the survey also asked about the factors which are driving increased adoption of models. As shown, advisors gave multiple reasons for their growing use of models. Interestingly, the least chosen response was, “my home office suggested it.” Instead, advisors were more likely to say that asset manager efforts to explain their models through specialists, wholesalers, and content were having an impact.⁴ This implies that while model adoption may have started with a top-down push from home offices, advisors are increasingly seeing the benefits of applying models within their practices and are interested in learning how the models emerging from third parties could fit with serving their clients' needs.

Drivers of Model Use in the Last 3 Years



While the trend of outsourcing investment management continues to grow, there is still a segment of financial advisors who are reluctant to shift responsibility to another party. First, there appears to be a discrepancy between how much advisors think clients want them to handle investment management and how much clients say they do. According to the 2019 FA Insight Study, 71% of financial advisors believe clients prefer in-house investment management, but when clients were asked the same question, 57% said they have no preference.⁵ This is supported by research data from SSgA, which indicates that investors who do not have their investable assets in a model portfolio are not opposed, as only 10% responded negatively to the idea.⁶ The implication is that most advisors feel that providing investment management is still a primary component of the value they bring to a relationship. However, most clients do not see this as a motivating factor when establishing or maintaining an advisory relationship.

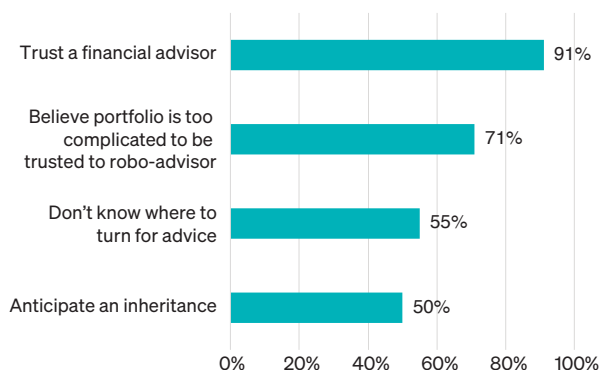
Second, a proportion of advisors think that model portfolios will underperform the portfolios they develop and manage themselves. However, as model portfolios build performance track records, advisors are finding that they can provide better returns for clients and help mitigate risk. Finally, some advisors are concerned that outsourced investment options are too costly. In fact, according to a report by FlexShares, among advisors who could be persuaded to use outsourced solutions, the largest percentage (28%) said they would reconsider if there were more affordable options available.⁷ While model portfolio fees vary, research from Morningstar shows, on average, the expense ratio of an allocation model portfolio comprised of Separately Managed Accounts (SMAs) is lower than a similar portfolio of unbundled mutual funds using the lowest-cost share class.⁸ Though some models also overlay a strategist fee, as competition increases and model management becomes more efficient, costs are coming down.

PERSONALIZING THE CLIENT EXPERIENCE

Younger generations have multiple competing financial priorities, requiring financial advice that considers them all. A 2021 survey by RBC Wealth Management of high-net-worth and high-earning millennials showed that while the majority (75%) of Millennials, like their parents, still have a goal of investing and saving for their long-term security, they also have other shorter-term goals. For instance, 27% said one of their top financial goals was starting a company.

Given the complexity of their financial lives, most younger investors understand that their needs cannot be met through digital solutions alone, as 71% of surveyed Millennials say their portfolios are too complicated to be trusted to a robo-advisor. Additionally, 72% said that after paying off debt, saving for an emergency fund, and maxing out their 401(k), they are unsure what to do next financially.⁹

Exhibit 6: Perspectives of Millennials

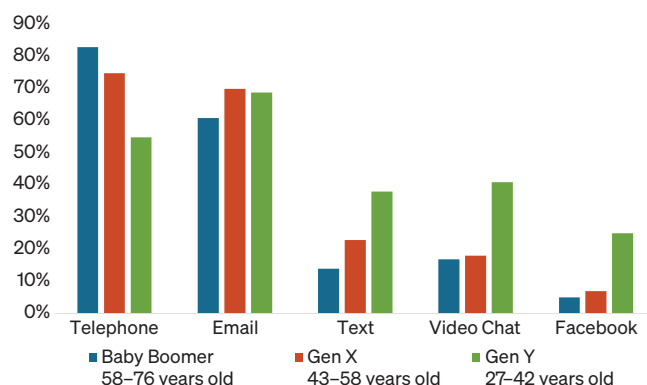


Source: "The millennial mindset: Insights into the next generation's needs, wants, preferences and their relationship with money management," Wealth Insights, RBC Wealth Management, 2022

This underscores the fact that younger investors need financial advice that addresses personal, intermediate investment goals versus managing to a pre-determined retirement date. However, it also highlights that most Millennials began their financial planning journeys through digital platforms, and though they are comfortable using digital planning tools, they now require advice that goes beyond the capabilities offered by these solutions.

For financial advisors who plan to court Gen Y, finding a way to incorporate digital tools into their planning models and how they communicate with clients is imperative to attracting and retaining the next generations of investors. A 2021 study by Spectrem Group shows that Gen Y is much more likely to communicate with their advisor through text, video chat, and social media than their older counterparts. A greater percentage of Gen Y also communicates with their advisor via email than by telephone.¹⁰ Combined, these findings imply that the financial advisors who are successful at attracting younger investors will be those who can demonstrate how technology plays a role in the planning process and show that they are open to communicating with clients in whatever way they prefer.

Exhibit 7: Ways Clients Communicate with Their Financial Advisors by Generation




Source: Spectrem Group, 2021

CONNECTING WITH HEIRS EARLY AND OFTEN

Establishing regular and persistent contact with clients' family members is just one step in retaining assets. Financial advisors must also align their service models with the needs and preferences of all generations, which is perhaps the most challenging aspect in the evolution of the financial advisory landscape. For financial advisors who have been in the industry for several years, investment management has served as the core, and sometimes the only, component of the client relationship. However, changing circumstances—economic, political, and societal—are altering the way Americans view and manage their finances. Those in or nearing retirement are concerned with more than just the value of their portfolios. Meanwhile, younger investors are trying to balance their short-term financial needs with long-term retirement planning. Comprehensive financial and wealth management advisory must prescribe solutions aligned with complex needs across all these life phases.

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Exhibit 8: Will They Stay or Will They Go? Willingness of Younger Investors to Meet with Advisors Can Overcome the High Attrition Rate of Heirs

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- » 46% of benefactors had not had a discussion about inheritance plans with their children¹
 - » 61% of investors say they have not or are not sure they have ever had a family wealth management discussion with their advisor²
 - » Of heirs that inherited \$2M+ and fired their parents' financial advisor, nearly three-fifths didn't know their parents' financial advisor³

- » 49% of Gen X/Y millionaires are likely or very likely to meet with their parents' advisor, if asked⁴
- » 57% of Millennials said in 2016 that they plan to use the services of a financial advisor linked to a branded institution within the next 5 years⁵
- » 91% of HNW Millennials trust a financial advisor⁶

¹ UBS Investor Watch: Begin before the end, 2014

² Three-Step Guide to the Family Wealth Conversation, MFS, 2016

³ "Why Inheritors Fire Their Parents' Financial Advisors," Forbes, June 2016

⁴ Millionaire Outlook Study, Fidelity Investments, 2017

⁵ Targeting the Digital Generation, Broadridge, 2016

⁶ The millennial mindset, RBC Wealth Management, 2022

PURSUING GROWTH IN BUSINESS VALUATION

The financial advisory business is on the cusp of a major transition, during which one in three advisors is expected to retire. As many advisors approach this milestone, they seek to optimize their businesses' value. While focusing on the needs of the Baby Boomers has served most advisors well in building assets under management and revenue, moving forward, this segment of the population will no longer deliver the same level of growth. To prepare their businesses for the future, advisors must alter their business models to attract younger clients, who are beginning to increase their wealth faster through higher earnings and inheritances from older generations. Our analysis of the current and future advisory landscape points to several actions that advisors can take to attract and retain the assets of younger investors and increase the value of their businesses.

To prepare for the shift in clientele from older to younger investors, advisors must look for efficiencies that will allow them to service more clients through deeper relationships. This requires sharing the workload with other resources in a way that adds value to the overall relationship by considering these moves:

- » **Outsource investment management** – Research shows that advisors who choose to outsource investment management gain efficiency without sacrificing performance. It also supports the premise that few clients and prospects perceive an advisor's decision to use models and other outsourced solutions as diminishing the value of their service.
- » **Partner with other service providers** – As the industry continues to evolve to offer more comprehensive financial planning, financial advisors need to carefully analyze which functions they should perform themselves and which are more suited to a dedicated service provider, such as a tax or estate planning specialist. Similar to outsourcing investment management, clients are more apt to view the value of an advisory relationship based on whether it addresses all their financial needs, regardless of who performs each function.
- » **Work in teams** – Like outsourcing, working in teams is shown to improve efficiency and growth. Teams not only help to spread the workload but also make the value of the whole more than the sum of its parts by creating larger and deeper relationships with clients and retaining their business for a longer period of time.

Understanding the needs and perspectives of younger investors and how they differ from current clients, will allow advisors to earn a larger share of these relationships, which will become growth accelerators for the advisory business going forward. Some recommended steps are to:

- » **Make advice more approachable and accessible** – Waiting to pursue younger investors until after they have acquired significant wealth means advisors will face more competition for those clients. By initiating communication now, whether by being introduced to the children of current clients or appealing to high earners, advisors will already have relationships for when younger investors need to make decisions about managing their wealth. However, to do this, advisors will need to overcome the perception among younger investors that they do not own sufficient assets to warrant the attention of an advisor.
- » **Prioritize prospecting** – During the long bull market, advisors could continue growing their asset-based revenue without allocating significant time prospecting for new clients. The result has been a gradual decline in the median number of new client relationships per advisor. Falling markets and the ongoing wealth transfer to younger generations means that advisors must refocus their efforts on business development via prospecting to continue growing their businesses.
- » **Add younger advisors** – While qualifications for hiring new advisors are typically based on years of experience and the size of their books, younger advisors are often better equipped to attract the business of younger investors—and the difference may be surprising. According to research from FUSE Research Network and WealthManagement.com, among advisors aged 30 to 39, the average client age is 49.7 but rises to 57.7 for advisors aged 60 to 69. The time between these average ages represents the peak earning years when clients are accumulating wealth at the fastest pace.

Many seasoned advisors spent their careers building a large book of loyal clients; however, inertia threatens to deplete the assets and reduce the value of their businesses. To retain the assets, advisors must adapt their practices to appeal to younger investors using these strategies:

- » **Initiate wealth planning discussions with clients and their families** – Talking about money within the family has traditionally been a taboo subject, leaving a lot unsaid about who will inherit a client's assets. The result is that many beneficiaries suddenly receive a large inheritance but face a steep learning curve in determining how to deal with it. As an outside service provider, financial advisors can help facilitate these family discussions so that clients do not have to handle them alone, and beneficiaries are better prepared when they inherit the assets. Knowing and understanding the needs of both parties also makes it much more likely that the advisor will retain the assets over the long run.
- » **Diversify the communication strategy** – When most financial advisors began their careers the only ways to communicate with clients was in-person or by telephone, so many have grown accustomed to managing their client relationships by picking up the phone. While many younger investors want to engage with an advisor and see value in having occasional face-to-face meetings, they want most communication to be convenient through technology, using text, email, and video communications.
- » **Take a personal approach** – In addition to a wider breadth of financial services, investors increasingly demand a more customized planning approach. Most Baby Boomers had an investment horizon of three to four decades of accumulating assets followed by two to three decades of drawing them down in retirement. Now, younger investors are more likely to have intermediate investing goals—such as starting a business, buying a home, or planning for a child's education. Additionally, many see themselves experiencing a longer but less traditional retirement. These investors want an advisor who will adapt their planning approach to address multiple, sometimes shifting goals.

Exhibit 9: Keys to Building Value Amid the Great Wealth Transfer

BECOME EFFICIENT

- » Outsource investment management
- » Partner with other service providers
- » Work in teams

GROW THE BUSINESS

- » Make advice more approachable and accessible
- » Prioritize prospecting
- » Add younger advisors

RETAIN THE ASSETS

- » Initiate family wealth planning discussions
- » Diversify communication
- » Take a personal approach

Source: FUSE Research Network

¹ The Future of Wealth in the United States, Deloitte, 2015

² Cerulli Associates, 2022

³ Advisor Trend Monitor: Advisor Top Trends for 2021, FUSE Research, [WealthManagement.com](https://www.fusewealth.com/research/advisor-top-trends-2021), March 2021

⁴ Advisor Trend Monitor: Advisor Top Trends for 2022, FUSE Research, [WealthManagement.com](https://www.fusewealth.com/research/advisor-top-trends-2022), March 2022

⁵ FA Insight Study, TD Ameritrade, 2019

⁶ Model Portfolio Solutions and the Client Experience, SSgA, 2022

⁷ The Race to Scalability 2022, FlexShares, 2022

⁸ 2022 Model Portfolio Landscape, Morningstar, 2022

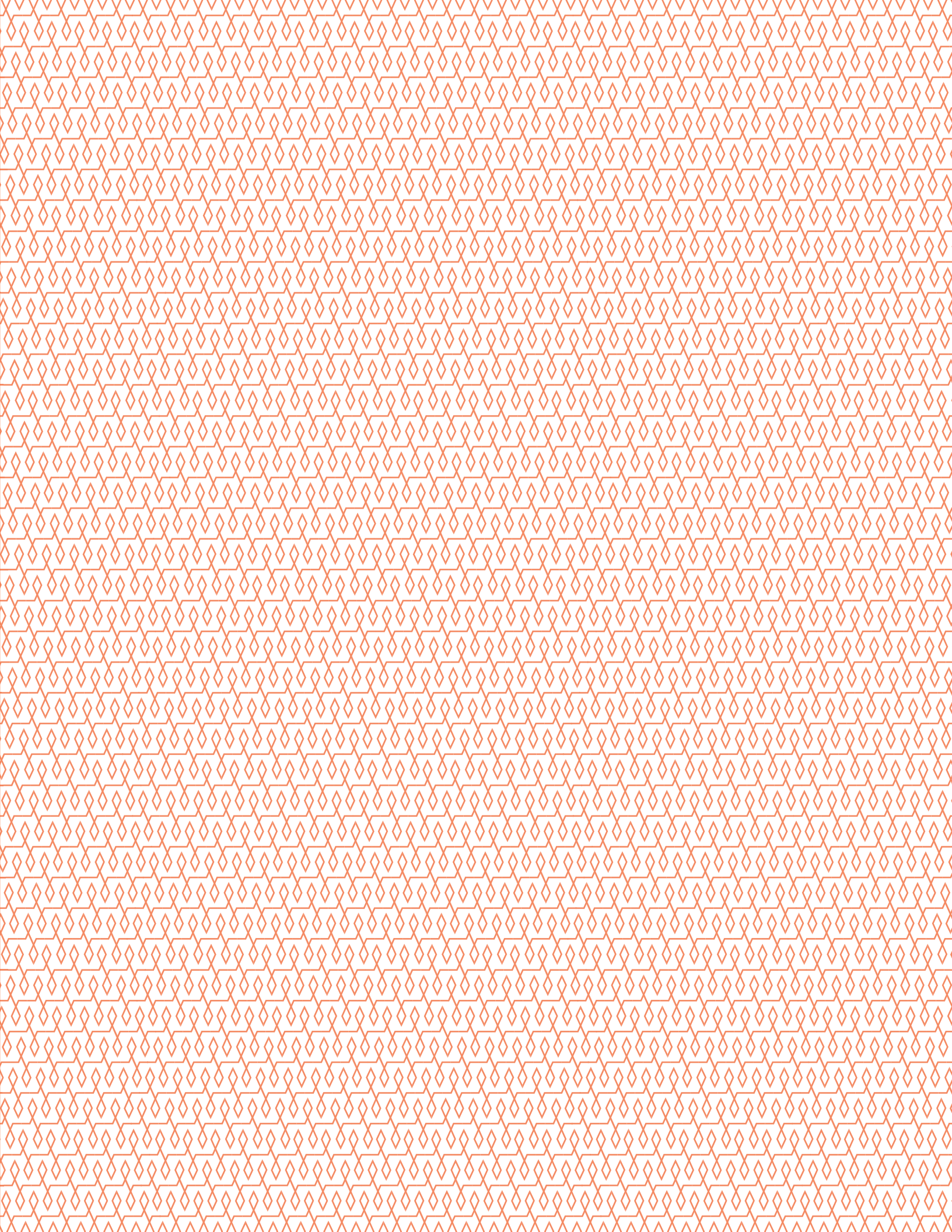
⁹ "The millennial mindset: Insights into the next generation's needs, wants, preferences and their relationship with money management," Wealth Insights, RBC Wealth Management, 2022

¹⁰ "Communication Preferences of 2021," The Voice of the Investor, Spectrem Group, 2021

A massive intergenerational wealth transfer—an estimated \$70 trillion in the U.S. alone—is occurring. Building ever-stronger client relationships to address the needs and concerns across generations is business critical for sustaining and expanding a successful practice.

As wealth changes hands from Boomers and the Silent Generation to Millennials and even Gen Z, new strategies, including wealth transfer planning, are imperative. Introducing new strategies into the practice can help drive financial advisors' expertise and nurture broad and deep relationships with families. Customizing the delivery of advice and communication with clients will be critical. Intergenerational strategies will not only help ensure client asset retention and growth during this unprecedented economic event—but also create opportunities to forge new connections and win new clients.







6125 Memorial Drive, Dublin, Ohio 43017 | meederadvisorconsulting.com