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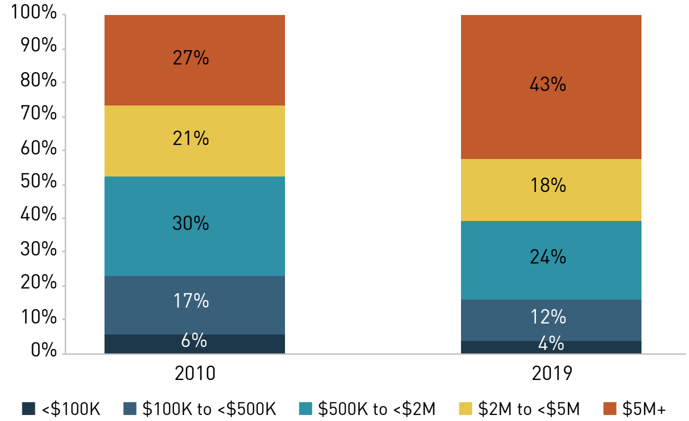
THE EVOLVING NEEDS OF AFFLUENT AND AGING CLIENT SETS

By Ed Louis, Associate Director, Wealth Management, Cerulli Associates

In this edition of *Investments & Wealth Research*, Cerulli Associates examines key trends shaping the future of wealth management. Affluent investors ($2 million to $5 million in investable assets), high-net-worth (HNW) investors ($5 million to $20 million), and ultra-high-net-worth (UHNW) households ($20 million or more) have grown their share of investor assets steadily over the past decade. Simultaneously, the industry is being forced to evolve as large shares of both its client base and advisors are aging. Advisors seeking to address the challenges and opportunities that come with these developments must exercise self-awareness and thoughtful long-term planning. Fortunately, these are fundamental skills advisors already leverage in their best client relationships.

FIGURE 1

ASSET DISTRIBUTION BY INVESTABLE ASSET TIER, 2010–2019



Sources: Federal Reserve, U.S. Census Bureau, Cerulli Associates

FIGURE 1 HIGHLIGHTS: Households with $500,000 to $2 million saw their share of household assets drop from 30 percent in 2010 to 24 percent in 2019.

KEY IMPLICATIONS: According to the most recently available data from the Survey of Consumer Finances, financial assets in the hands of HNW and UHNW investors grew to nearly $20 trillion in 2019, increasing nearly $13 trillion (or 11 percent annualized) over the previous decade. In contrast, the annual growth for households under the $5-million threshold was 3 percent. Despite accounting for only a small fraction (1.3 percent) of all U.S households, HNW and UHNW investors accounted for more than 43 percent of all U.S. investable assets, up from just 27 percent in 2010. This is driving many firms to try to move upmarket. However, advisors attempting to do so must assess whether they have the necessary capabilities and resources.

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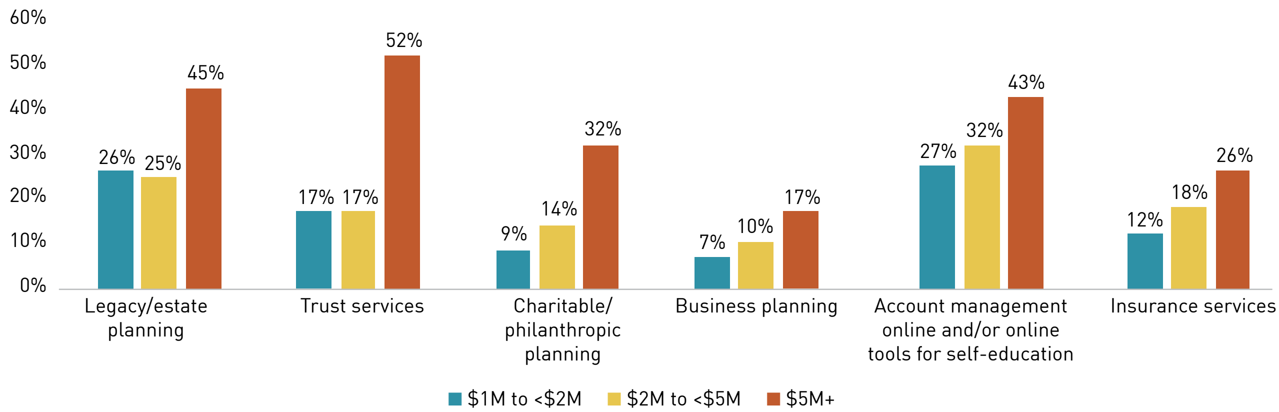
FIGURE 2

SERVICES USED WITH FINANCIAL ADVISORS BY INVESTABLE ASSETS, Q2 2020



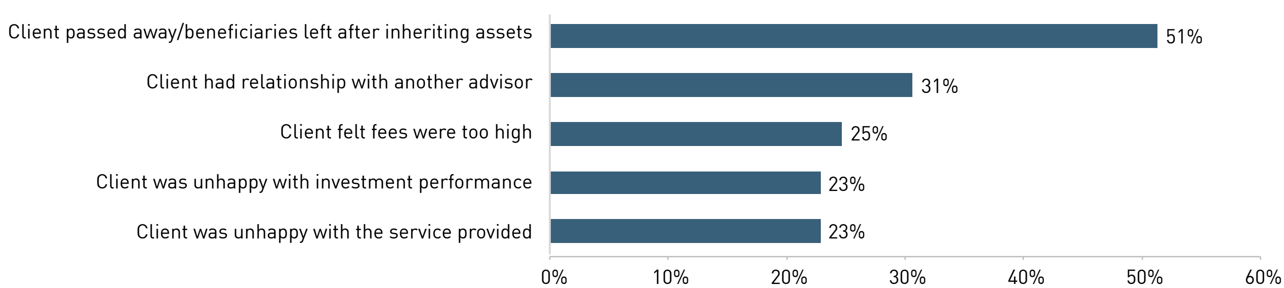
Sources: Phoenix Marketing International, Cerulli Associates

FIGURE 2 HIGHLIGHTS: More than two-fifths (43 percent) of HNW and UHNW investors use online offerings provided by their financial advisors.

KEY IMPLICATIONS: Serving HNW clients requires that firms expand their offerings beyond investment management to support a broader scope of services. HNW investors are almost twice as likely to use trust services (52 percent), estate/legacy planning (45 percent), and charitable/philanthropic giving services (32 percent) compared with less-affluent households. Cerulli Associates notes that the demand for these services likely will accelerate in the coming years as more investors begin to transfer wealth to the next generation. Advisory firms looking to cater to the higher end of the market must ensure that they have a well-diversified expertise and service offering to align with client expectations—and can place greater emphasis on customized wealth, investment, and banking solutions.

FIGURE 3

HNW PRACTICES: PRIMARY REASONS INVESTORS LEAVE THE PRACTICE, 2020



Analyst Note: Respondents were allowed to select more than one choice.

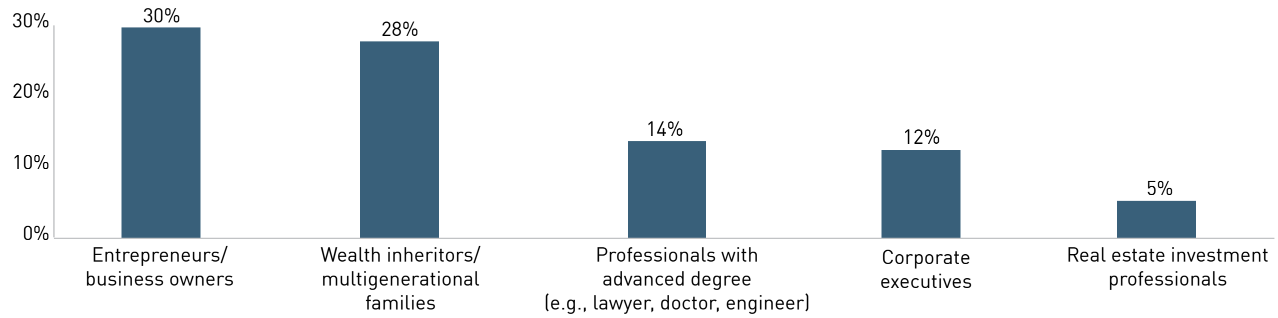
Sources: Cerulli Associates

FIGURE 3 HIGHLIGHTS: More than half (51 percent) of HNW practices consider clients passing away and the inheritors seeking another advisor as a primary reason why they lose clients.

KEY IMPLICATIONS: As baby boomers retire and a significant portion of their wealth is transferred to younger generations, HNW practices will be presented with both a major opportunity and a significant threat. Even though HNW practices are well aware of the risks that attrition can have on their businesses, many fail to take the appropriate steps to overcome the loss of clients across generations. Although creating an estate plan and executing trust vehicles may satisfy the needs of current clients, those who neglect relationships with a client's spouse and heirs dramatically risk losing those assets once the client passes away.

FIGURE 4

HNW PRACTICES: LARGEST SEGMENTS OF CURRENT CLIENT BASE, 2020



Source: Cerulli Associates

FIGURE 4 HIGHLIGHTS: Entrepreneurs/ business owners (30 percent) and wealth inheritors/multigenerational families (28 percent) make up the majority of clients among HNW practices surveyed by Cerulli Associates.

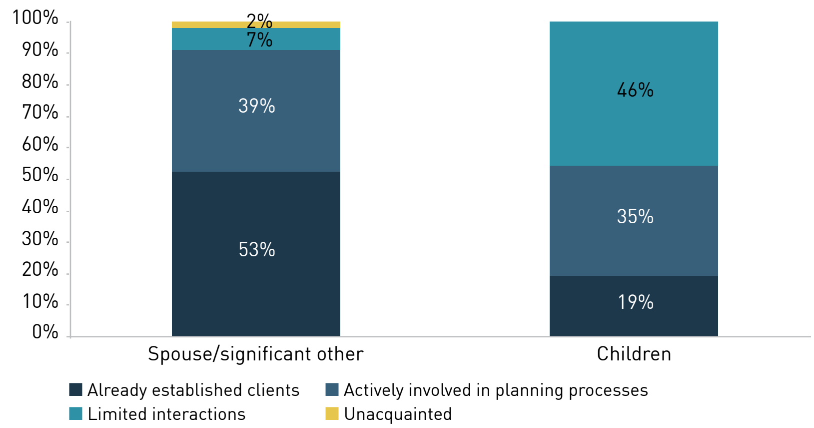
KEY IMPLICATIONS: Though entrepreneurs and business owners continue to make up the plurality of client relationships at HNW and UHNW practices, wealth inheritors and multigenerational families are very close to becoming the top client demographic in this space. Cerulli Associates projects that nearly $70 trillion in wealth will be transferred to heirs and charities during the next 25 years, creating a vast shift in the nature of HNW client relationships, practice management, and business development strategies. Rather than relying primarily on referrals and generating business with new wealth creators, a large share of future wealth owners are the children of today's wealth owners and represent key, already identifiable future clients.

FIGURE 5

HNW PRACTICES: RELATIONSHIPS WITH CLIENTS' POTENTIAL INHERITORS, 2020

FIGURE 5 HIGHLIGHTS: The vast majority (92 percent) of surveyed HNW practices report having actively involved planning relationships with current clients' spouses/ significant others.

KEY IMPLICATIONS: Roughly half (46 percent) of all surveyed practices have only limited interactions or are completely unacquainted with their clients' children. Cerulli Associates has found that practices that make a concerted effort to either involve clients' children from the outset, or at least open a line of communication at some point between themselves and potential future inheritors, experience significantly greater retention over time. In the best cases, effective communication should be practiced regularly between the advisor and family members well before any major transition or event occurs to ensure expectations are understood.



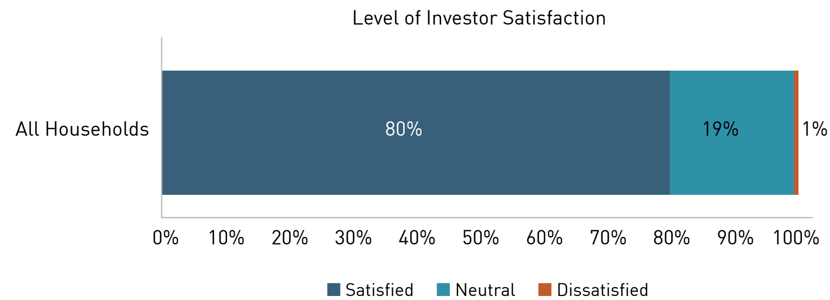
Analyst Note: Other potential inheritors not shown include grandchildren, extended family members, friends, foundations, and business partners.

Source: Cerulli Associate

FIGURE 6

INVESTOR SATISFACTION DASHBOARD, Q2 2020

FIGURE 6 HIGHLIGHTS: The majority (80 percent) of investors are satisfied with their primary advisors.



Sources: Phoenix Marketing International, Cerulli Associates

KEY IMPLICATIONS: A prolonged bull market buoyed investor satisfaction over the past decade and, despite market volatility, satisfaction levels remained high in early 2020. This is a positive indicator for advisors, given that it suggests they were able to effectively demonstrate the value of their services amid widespread uncertainty. Especially in turbulent times, investors are more apt to ask for advice, check in on their portfolios, and seek reassurance that their finances have not deviated from the long-term plan. Ultimately, an investor's perception of the advisor's trustworthiness, honesty, and dependability supersedes all other factors (i.e., investment performance, service quality) and drives satisfaction.

TABLE 1

PRIMARY REASON FOR NOT HAVING AN INVESTMENT ADVISOR, Q2 2020

TABLE 1 HIGHLIGHTS: Costs/fees are a primary reason nearly one-third (31 percent) of self-directed investors choose not to work with an advisor.

Primary Reason for Not Having an Investment Advisor	All Households
Confidence in my own investment decisions/strategies	38%
Costs/fees	31%
Not relevant to my personal financial situation	12%
I don't currently have enough information to choose an advisor	9%
Lack of useful advice/information	6%
Other	4%

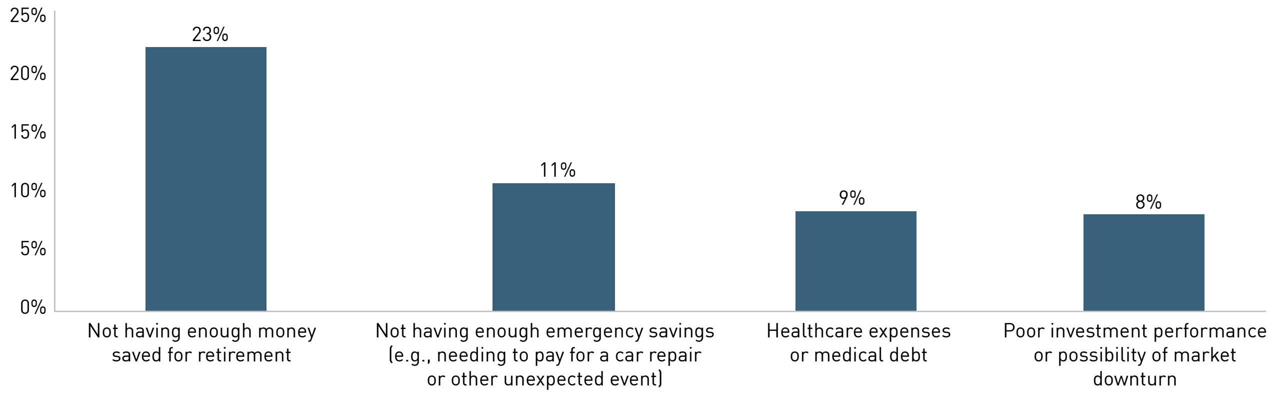
Analyst Note: This question was only asked of respondents who indicated, "I do not discuss my finances or investment decision-making with an investment professional/advisor at all."

Sources: Phoenix Marketing International, Cerulli Associates

KEY IMPLICATIONS: Although some investors may have the skills to competently run their own portfolios and make long-term plans, more are likely to overrate their own skills and fail to recognize their deficiencies. Without objective measurement, investors end up trapped in a web of behavioral biases, including selective memory, loss aversion, and anchoring, to justify their actions no matter how suboptimal or illogical. Essentially, those with the most need for help are least likely to ask for it. Unfortunately, investors in this category also are generally highly resistant to change, though they may choose to seek help when faced with excessive volatility.

FIGURE 7

TOP SOURCES OF STRESS FOR ACTIVE WORKERS, 2021



Analyst Note: Respondents were asked to select the top-two factors that cause the most financial stress.

Source: Cerulli Associates

FIGURE 7 HIGHLIGHTS: Not having enough saved for retirement (23 percent) ranks as the most common source of financial stress for active workers.

KEY IMPLICATIONS: Lack of sufficient retirement savings is a leading cause of financial stress for retirement investors of all ages. Given that retirement savings is the broadest financial concern, Cerulli Associates views this as an effective starting point from which to partner with employers to build a holistic financial wellness program. In the past, it may have been challenging to bring in various subject-matter experts from a practice, but remote work environments could make this tailored approach easier to deliver. For example, some retirement plan sponsors have begun to host a retirement benefits seminar for all participants followed by breakout sessions that cover specific topics in more depth.

TABLE 2

PRACTICE MANAGEMENT PROFESSIONALS: MOST EFFECTIVE STRATEGIC ALLIANCES, 2020

	Practice Management Professionals		
Top-Five Most Effective Activities	Not effective	Somewhat effective	Very effective
Keeping other professionals up to date about joint client status	0%	26%	74%
Joint client events	3%	34%	63%
Joint meetings with clients or prospects	3%	37%	61%
Socializing with other professionals	3%	42%	55%
Starting out with a long-term organic relationship	3%	45%	53%

Analyst Note: Responses are from practice management professionals.

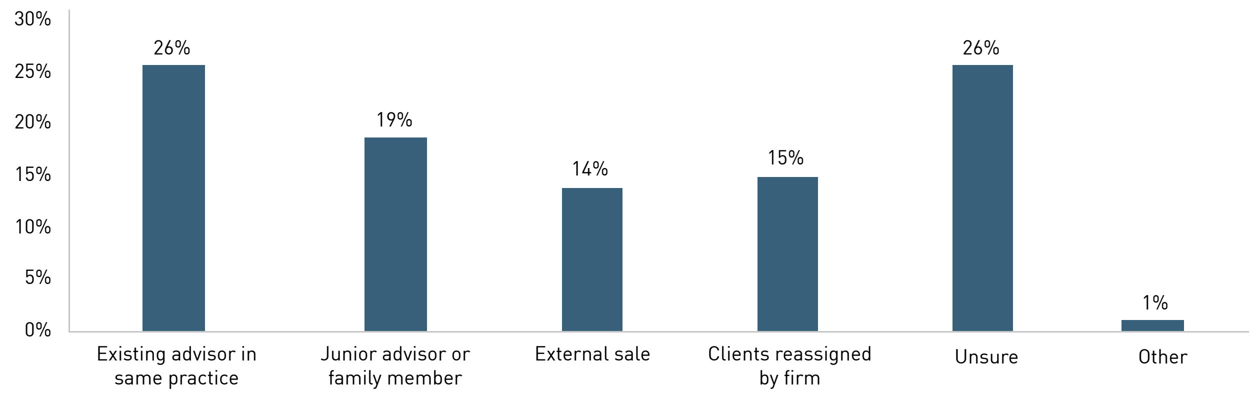
Sources: Cerulli Associates, in partnership with Investments & Wealth Institute® and the Financial Planning Association®

TABLE 2 HIGHLIGHTS: Among practice management consultants, 74 percent consider keeping other professionals up to date about joint client status to be a very effective strategy for advisors to build strategic alliances with centers of influence.

KEY IMPLICATIONS: Partnerships with other professionals—attorneys, accountants, real estate agents—can be a boon for practice growth, if thoughtfully cultivated. New advisors often underestimate the time and care required to foster strategic alliances that consistently result in new business. A common misstep is to view the relationship as a transactional referral network instead of a collaborative partnership that allows both sides to enhance the value proposition. Other professionals will be unwilling to make referrals to an advisor whom they are not confident can deliver quality outcomes for their clients. Therefore, advisors should move slowly to breed trust and leverage mutual connections through industry associations or other networks.

FIGURE 8

CURRENT SUCCESSION PLAN, 2020



Sources: Cerulli Associates, Meridian IQ, Investment Company Institute, Insured Retirement Institute, VARDS, Strategic Insight/SIMFUND, InvestmentNews, *Judy Diamond, Department of Labor, PLANSPONSOR, S&P Capital IQ, Financial Planning,* Financial Advisor Magazine, Investment Advisor Magazine, *and Cerulli Associates, in partnership with the Investments & Wealth Institute, WealthManagement.com, and the Financial Planning Association*

FIGURE 8 HIGHLIGHTS: An equal percentage of advisors (26 percent) are either transitioning their clients to another advisor in the practice or are unsure of their succession plans.

KEY IMPLICATIONS: Although advisors successfully support clients through various life stages and transitions, they often fail to plan for themselves. However, those who ignore the inevitable and delay retirement often face more-difficult issues when they are forced to retire rather than allowed to dictate their own terms. More than 26,000 advisors are retiring in the next 10 years and do not currently have succession plans.* As one succession specialist with whom Cerulli Associates spoke stressed, "Succession planning does not have to be retirement, but if an advisor waits too long, it becomes retirement."

** Datapoint not shown in figure 8.*

TABLE 3

SUCCESSION PREPARATION CHALLENGES, 2020

	Practice Management Professionals		
Challenge	Not a Challenge	Moderate Challenge	Major Challenge
Emotional aspects of transferring clients to a new advisor	8%	26%	66%
Finding a qualified buyer	16%	26%	58%
Transferring clients to the buyer	3%	47%	50%
Valuing a practice accurately and fairly	11%	42%	47%
Negotiating with prospective buyer(s)	16%	43%	41%
Structuring deal terms (e.g., earnouts, promissory notes)	13%	47%	39%

Sources: Cerulli Associates, in partnership with Investments & Wealth Institute and the Financial Planning Association

TABLE 3 HIGHLIGHTS: The emotional aspects of transferring clients to a new advisor pose the greatest challenge as advisors prepare for succession.

KEY IMPLICATIONS: Although advisors may prefer an internal succession to an external sale, it is often easier said than done. Successful advisors typically have built practices from the ground up and worn multiple hats to grow their businesses. These advisors want successors who can do the same. In conversations with practice management professionals, Cerulli Associates has found that an internal succession usually will require more than one successor to adequately replace an owner-advisor. Advisors should look within their practices for team members who can be groomed to take over aspects of the retiring advisor's role when it's time to transition to retirement.

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