Bold Moves Are Needed to Thrive in a New Era of Asset and Wealth Management

By Michael Andrews, CFA®, Julia Binder, and Matthew Fronczke
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Innovative technology developments, societal changes, and economic trends are shaking up the asset management and wealth industries. A few firms are responding by radically reimagining their organizations and business strategies, making big changes to remain viable in a new era. We’ve seen firms:

- Introduce zero-fee index funds
- Replace stock portfolio managers with robots
- Integrate digital advice as a standard operation where products are maintained that are not products.
- Explore the capital markets (e.g., debt or equity issuance, mergers and acquisitions activity) to build sustainable competitive advantages
- Determine what you want to be when you grow up.
- Introduce robots to your firm and discard some of the structural holdovers that may be getting in your way. Does any of the following sound familiar?

These audacious moves are just a few that firms are taking to position themselves for leadership in the rapidly transforming global asset and wealth management industries. We expect new leaders to emerge worldwide with innovative solutions, new business models, and modern approaches to growing assets and increasing customer lifetime value—as old stalwarts fade away.

A TIME FOR CHANGE

The pressure on asset and wealth managers has never been greater. Innovative technologies, changing consumer behaviors, and fee compression have forced the global asset and wealth management industry to face some of the biggest disruptions since John Bogle launched the First Index Investment Trust in 1975, the U.S. Congress passed the Revenue Act of 1978,¹ and State Street launched SPY in 1993.

Every single firm must deliver a clearly articulated and differentiated value proposition, deploy company resources efficiently, and build mutually rewarding partnerships across distribution channels. That means taking a hard look at your firm and discarding some of the structural holdovers that may be getting in your way. Does any of the following sound familiar?

- Your revenue is concentrated in and primarily driven from one country, one channel, one dealer firm, or one product (or a very small number of each).
- Your sales team is well-compensated yet potentially focused on the wrong relationships (and the incentives driving them are not aligned with their customers’ needs or broader goals of the business).
- Your marketing and distribution teams struggle to measure return on investment and evaluate profitability across various channels and markets.
- You have large and expensive portfolio management teams managing sub-par products.
- Products are maintained that are not core to your firm’s value proposition.
- Your firm’s culture does not support rapid or nimble change (or there is a lack of appetite for major change).

Not all asset and wealth managers struggle with these challenges, but many do. More often than not, major changes to firm operations, marketing, distribution, and product strategy need to be made to ensure long-term business sustainability. Non-core business activities and processes outside the main value proposition of your firm should be streamlined and outsourced to leaders in their fields—not just across back- and middle-office functions, but even for front-office operations where appropriate. Capital market options and strategic acquisitions and mergers need to be explored to further investments in technology, increase asset and operational scale, open access to new markets, and expand investment capabilities.

In short, it’s time for leadership to make difficult but important firm-wide changes in operations, channel, and geographical distribution; the role of marketing, products, and pricing; and investment management capabilities. Complacency will exacerbate the current challenges and increase the likelihood that firms fall victim to disruption, increased competition, and industry consolidation.

There are tremendous opportunities in this environment, but seizing them requires transformative leadership rooted in modern, scalable, data-driven strategies. Identifying technology partners and vendors, as well as carrying out significant internal investments in technology infrastructure and data, are at the heart of this transformation. All options should be explored. This is essential to uncovering previously hidden business opportunities, developing...
new business models, or achieving essential efficiencies in product management, prospecting, business development, and client servicing.

**PICK YOUR LANE**

Don’t try to be everything to everyone. Typically, that just leads firms to try too many things at once, all in a mediocre way. A few large global players are more capable of providing an array of quality products to a broad consumer base. However, even at their best, most firms will be good at only one thing in particular, or their value proposition is centered on a core capability. Make sure you truly understand what that is and focus on excelling in that area.

An increasingly competitive environment has no room for asset managers with a wealth of underperforming products, inadequate customer service, and no distinct competitive advantage. Professional buyers, financial advisors, and retail customers need to have clear, compelling reasons to do business with your organization. So pick a lane and own it. Only a few firms are going to thrive in the long run, and they are the ones that really stand out.

Technology, rising customer expectations, and market pressures, including fee compression and amplified distribution costs, will continue to drive consolidation across the industry. Asset managers that have achieved scale (in operations or assets), technological advantages (in their products, services, partners, or affiliates), product leadership positions, or vertical channel integration (direct access to the end customer)—are more likely to be around for the long haul. Firms that don’t will find it hard to differentiate themselves and will be at greater risk of shutting down or being on the acquired-end of mergers and acquisitions activity.

Our analysis of the industry indicates that leading asset and wealth managers exhibit some common characteristics. Firms without these advantages need at least one of them for continued growth and success. We encourage firms with none of these characteristics to pick a lane by placing focus and purpose in one of these areas; trying to build advantages in all areas at once puts a firm at risk of missing the mark and lagging market leaders.

**Operational, asset-scale, and technology advantages.** These firms have large asset bases—typically more than $1 trillion in global assets—across multiple channels of global distribution, and a diversified product line across asset classes and investment vehicles. They also have integrated technology and data into their core business processes and have invested in financial technology, which broadens their distribution and marketing capabilities or creates new revenue opportunities through product development and innovation, opening up markets, and finding new customers.

**Direct link to customer with vertical integration.** These firms have a direct link to the customer, either through a wealth management organization or an established direct retail consumer platform. This includes owning or partnering with technology-driven wealth management platforms (robo-advisors, turnkey asset management programs), fund supermarkets, and wealth management organizations.

**Product leadership position.** Strong investment management capabilities, a unique value proposition, or a history of innovative product development give these firms distinct competitive advantages. Pricing advantages (e.g., low-cost option), performance excellence in a niche area (e.g., alternatives, fixed income), or recognition as an innovative firm that is excellent at creating new investment solutions are common attributes of these firms. Technology plays a critical role for these organizations, both in reducing operational and investment management costs and in improving investment outcomes.

For a subset of asset management organizations, another option is to be private, small, and focused. Obviously, being private is not limited to small firms—take Fidelity, for example. But large, private organizations with multiple business lines or a global presence must exhibit the advantages discussed above to remain competitive in the modern asset and wealth ecosystem.

Small, privately owned firms that benefit from distinctive investment management capabilities and a loyal customer base can coexist in a world of behemoths. As small privately held organizations, these firms are not as concerned with operational margins or aggressive asset expansion, given their current levels of profitability. They are under less pressure to alter their business models because of their special expertise or unique place with a loyal customer base. Owners are typically happy to be small, local, and domestic, and are in no hurry to drastically alter their businesses, because there is no intention of competing outside their unique marketplace.

All other asset managers—or those who do not clearly fit into the profiles stated above—are operating without distinct advantages. And, to be clear, this is true for a majority of the asset management industry. These firms have not achieved the operational and asset scale of their counterparts, nor do they hold product leadership positions or technology advantages. They typically have large asset concentrations in a small number of products, and their lack of investment in modern technology and sole focus on the intermediary retail channel of distribution compromises their futures in the industry. This is not a viable lane, so product improvements, technology improvements (for efficiency, revenue generation, or both), competitive scale, or access to the end customer must become a priority for these firms.

The use of technology and data is clearly separating the leaders from the laggards. And regardless of whether a firm’s
competitive advantages lie in scale, product, or service, no firm can expect to thrive in the future without data-driven, technology-supported strategies. No organization, no matter its size or current business model, can be complacent about its present-day market position. Competitors will adapt and grow, and new entrants always will be a looming threat. Building and retaining a leadership position is critical to future success and longevity.

**EMBRACE DISRUPTION**

Asset and wealth management organizations that see disruption as an opportunity rather than a threat will be able to avoid the inevitable shakeout. Firms must seriously consider the following:

**Technology is core to the entirety of the asset and wealth management business.** Technology and data—no longer a novelty—have become table stakes for firms competing in the asset and wealth management industry. Firms focused on garnering competitive advantages from the use of technology and data services can’t be complacent with their systems and tools. Those that make aggressive investments in marrying advanced technology with a comprehensive data strategy will continue to have a competitive edge over firms that hesitate and stick with traditional business operations.

**Personalized investment solutions are the future of wealth management.** Digital financial advice providers and evolving consumer expectations have fueled a few industry players to develop platforms for delivering personalized portfolios and even family-office services at scale. Thus far, most of the industry has failed to address market needs for personalized investment solutions. The increased attention to the individual and seamless customer experience is forcing great changes across marketing, distribution, and product functions. Asset managers must adapt the delivery of their investment products (or intellectual capital) to fit into the modern world of wealth management.

Various forms of artificial intelligence (AI) are upending all aspects of the asset and wealth management business, and they are a source of both inspiration and concern. From redesigning operational processes and workflow automation to micro-targeting marketing campaigns and stock-picking, there is seemingly no area of the business that will remain untouched by artificial intelligence.

AI-powered engines can enable more consumers to invest and receive advice once reserved for only high-net-worth clientele (think digital family office or private client services for the mass affluent). They can create personalized investment portfolios that are tax-efficient, low-cost, and aligned with investors’ preferences and values. AI also will drive efficiencies that investors don’t realize, from the back to the front office, greatly reducing the need for current staffing levels. Unfortunately for the asset management industry, in a technology-driven environment there are few winners and many losers (e.g., Amazon for consumer retail, Google for search). So, firms must take their investments in technology seriously and avoid thinking of them as beneficial add-ons. To the contrary, they must be an integral part of the business strategy.

**CHANGE GEARS TO INCREASE CUSTOMER LIFETIME VALUE**

Distribution and marketing traditionally have been fixated on the short term, with organizations and strategies built to acquire new customers and bring in new assets. Campaigns primarily designed to generate leads, metrics focused on lead conversion rates, and compensation based largely on gross sales reinforce the premise that new sales drive growth.

But in this era of shrinking margins, changing dynamics, and net outflows, it is imperative that firms shift their focus to the long term by increasing customer lifetime value (CLV). In essence, the longer the customer continues to purchase and retain assets, the more CLV can increase. Yet our research finds that only 3 percent of firms currently calculate CLV when determining their marketing effectiveness. Computing CLV enables firms to predict the total profit a customer will generate over the course of the business relationship, helping them to build their organizations and plans accordingly. To do this, modern marketing and distribution teams are organizing around the following:

- Prioritizing relationships based on strategic alignment and high-growth opportunity
- Structuring teams and optimizing strategies to retain and increase existing business
- Amplifying customer experience with critical data and technology investments

This outcome-based approach has implications across every aspect of the firm. It embeds efficiency in delivering service and accountability for maximizing the profitability and potential of every relationship.

Making it easy for professional buyers, advisors, and investors to do business with your firm entails providing the right information, at the right time, in the way the recipient expects and prefers. That means embedding individualized recommendations throughout the digital ecosystem via dashboards for sales-team members on the phone or online chat, chatbots and digital assistants for website users, and alerts on mobile phones. It isn’t possible to do this manually at scale. But ignoring the need to deliver the individualized recommendations and next steps that are hallmarks of superior customer experience isn’t an option either. In fact, it’s a tipping factor for three out of four advisors evaluating asset managers with comparable products.

That’s why distribution and marketing executives need to embrace AI as a de facto organizational competency.
AI enables marketing and distribution teams to obtain insights to accelerate decision-making, automate rote work to gain efficiency, integrate predictive recommendations to increase relevance, and embed digital assistants to create opportunity. Investments in sophisticated technology and data reflect an intention to enhance the efficiency of the workforce, enable agility in anticipating and managing opportunities, and optimize outcomes that increase CLV.

**SECURE A PRODUCT LEADERSHIP POSITION**

With fierce competition among asset managers of all types and sizes, an increased focus on fees almost everywhere in the world, and the seemingly relentless rise of passive investing, investment managers are facing a challenging environment—especially now that market volatility has returned. Unfortunately, the share price of many publicly traded managers reflects this reality, with most managers down between 20 percent and 50 percent in 2018.

The same forces of transformation and consolidation that have erupted across the asset management landscape recently also have brought relatively rapid and widespread change to many wealth management organizations. In turn, the many changes going on inside these wealth platforms have had a direct impact on product development and distribution efforts at a time of increasing costs and steady downward pressure on manager profitability.

For example, how many wealth managers will have the resources to maintain teams of analysts to review third-party offerings and construct model portfolios? Many will choose to outsource this function, which likely will accelerate the institutionalization of the investment management industry.

Asset managers have had to work harder and more strategically to avert platform consolidations, reduce expenses, and consciously alter their businesses to manage lost revenues and declining operating margins. Accordingly, whether firms are global giants or small boutiques, they must all do the following with regard to products:

1. Be ruthless in analyzing your products. Create a plan to rationalize (i.e., cut) anything that isn’t competitive or best-of-breed. This will lower operating expenses by aggressively trimming unprofitable product lines that your firm is not committed to.

2. Be aggressive in filling product gaps. Some firms—though not most—should develop or acquire new products to better meet the needs of their investors. Rationalizing capabilities in higher-value specialized asset classes or customizable solutions that command large fees may demand the development or acquisition of new products.

3. Evaluate investment management expenses and portfolio manager compensation. In light of declining margins, we believe senior management must give careful consideration to the question of how portfolio managers and analysts are paid relative to the value they create. Now may be the time for some firms to attack a culture in which the chief executive officer seemingly works for the investment management teams, not the other way around.

4. Invest in technology and alternative data sources to reduce costs and improve investment outcomes. We believe the impact of technological change on product will continue to increase. Specifically, we see AI and machine learning applications helping managers overcome some of the pressures they face in terms of fees, performance, operations, and revenue, as well as offering a means to optimize their investment analytics and potentially better their performance results.

5. Have a global perspective on product development and partnerships. As competition for investors and assets has intensified—and technology and cross-border regulation have extended the reach of all parties in the financial value chain—asset managers increasingly have been forced to look outside their domestic footprints to sell their products and gather assets.

Many asset managers seem to think it is important to offer a range of styles—across the full spectrum of active to completely passive—to be competitive. We caution that this likely is beyond the reach of all but the biggest and best capitalized firms. In fact, we would argue that unless this range of styles is accompanied by a distinct product or brand advantage, it most likely will result in diminished value.

Also, most investors want help putting their disparate investments together; they do not think in terms of purchasing individual products. Accordingly, we want to remind managers that selling in the new era requires going beyond being just a product provider. Understanding your prospect’s structure, procedures, goals, and challenges is essential intelligence that managers must begin to centralize and utilize to develop concrete and targeted product solutions. Being a trusted advisor—rather than simply a product manufacturer—will build deeper loyalty, enhance manager opportunities, and minimize the risks of rationalization as distributors look to reduce the number of available funds on their platforms. The firms with the ability to provide assistance with an array of services, such as portfolio construction or portfolio planning tools, will be beneficiaries of this investor need.

Simply put, whether you are a U.S. wealth manager, a European bank with an investment manager subsidiary, or a Japanese asset manager with captive distribution, you will not be immune to the forces rocking the industry.

Regardless of geographical location, whether you are a traditional active or

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passive manager, or an alternatives manager with an institutional focus, fees will continue to compress and technology spending will increase. People are living longer, the world is becoming richer, and markets are increasingly interconnected. For those global players able to provide best-of-breed products and solutions at an appropriate price, tremendous opportunities exist today and into the future.

THRIVING IN THE FUTURE

The massive changes pending for the asset management industry make this an exciting time for firms that are positioning themselves to seize opportunity with deep investments in technology and data. Those investments enable business leaders to develop innovative products, forge powerful strategic partnerships, and deepen customer intimacy to increase lifetime value. Asset managers that hesitate during this critical time will increasingly be sidelined and may not survive.

Investments in data and technology are supported by cultural changes, first and foremost in shifting the focus from portfolio managers to customers. We’ve observed important signs of this change with investments in digital advice, sales enablement and marketing automation technologies, and the restructuring of distribution and marketing organizations around their most significant customer opportunities. At the same time, firms have been more aggressive about outsourcing non-core business activities to take advantage of expertise and reduce long-term costs.

Ultimately, however, the ability of firms to deliver benchmark-beating performance at a reasonable price will determine future success. To accomplish this, senior management will need to make tough strategic decisions around their product offerings, staffing, and compensation. Unfortunately, these decisions will not be easy and not everyone will get it right. But standing still is not an option. Today’s changing environment demands rapid action.


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ENDNOTE

1. The Act added section 401(k) to the Internal Revenue Code. This provision, intended to limit executive compensation, was used later to develop one of the primary tax-advantaged retirement savings vehicles in use in the United States and thus was a catalyst for defined contribution market growth.