The Financial Services Industry in 2030

By Matt Lynch

The new millennium entered quietly, the Y2K crisis averted. The market was optimistic and pleased with the AOL and Time Warner merger, and NASDAQ hit an all-time high in 2000. But that was before the dot-com bubble burst. Ensuing years brought the record-setting bankruptcies of Enron and then WorldCom, and conviction of some of the executives. The Enron scandal also brought down accounting giant Arthur Andersen. The Dow Jones closed at a record high on October 9, 2007, but was soon followed by the bursting of the housing bubble, the demise of Lehman Brothers, and the Bernie Madoff scandal, among many others. In 2009 the Dow Jones marked the low of the recession closing at 6,547—not more than 50 percent from its high. While the market has recovered and in fact achieved new all-time highs, the twin wounds of the great recession and continued Wall Street scandals have left consumers feeling less than fulfilled.

At a recent industry meeting Chip Roame, managing partner of Tiburon Strategic Advisors, addressed the resulting consumer attitudinal and behavioral changes, including those driven by the widening wealth gap. “Consumer confidence and sentiment are both trending up but are extremely low,” he said. “A substantial trust gap has arisen, represented by the Harris Reputation Quotient that lists only tobacco and government lower than financial services. There is a major consumer self-serve movement due, in part, to the lack of trust in the financial services industry.”

According to Tiburon’s research there were 8.6 million millionaires in 2012 versus 9.2 million in 2007, so the size of the market for many financial services firms has not grown in the past six years. Yes, the stock market has hit new highs and the bond market has done relatively well, but consumers do not feel rich or happy because their homes and small businesses are still down in value from the peak. The numerous scandals affecting all segments of the financial services industry have contributed to consumer skepticism, and on a personal level most consumers have not achieved their financial objectives. What does the future hold?

It is difficult to overestimate demographic shifts and what they mean to the financial services industry. However, it is also important to look at two very different scenarios on how the industry may choose to address—or avoid—these trends.

As the demographic data in table 1 show, although population growth rates are slowing, the United States is changing in terms of age, diversity, and gender. Population trends also reinforce women’s longer life expectancies.

Industry Trends

These data illustrate several key trends with major implications for the financial services industry in these demographics.

Consumer Expectations vs. Industry Standards

In terms of their relationships with financial advisors, consumers are beginning to expect a fiduciary standard, even if they are not familiar with the terminology. More than 75 percent of investors expect all financial profession-
Women also are expected to inherit about 70 percent of the estimated $41 trillion in intergenerational wealth transfers by about 2050 (Havens and Schervish 2003). Additionally, women tend to live six to eight years longer than men and will need ongoing financial advice. However, about 70 percent of widows change financial advisors within a year of their husbands’ deaths. Women advisors make up only 30 percent of the industry and only 25 percent of CFP professionals (Kutler and Simon 2009).

Women as a Major Market
Contrary to some industry articles, women are not a niche market. Women currently control the majority of personal wealth (51.3 percent). These assets are estimated at $14 trillion and are expected to increase to $22 trillion by 2020 (InvestmentNews 2012). Women also are expected to inherit about 70 percent of the estimated $41 trillion in intergenerational wealth transfers by about 2050 (Havens and Schervish 2003). Additionally, women tend to live six to eight years longer than men and will need ongoing financial advice. However, about 70 percent of widows change financial advisors within a year of their husbands’ deaths. Women advisors make up only 30 percent of the industry and only 25 percent of CFP professionals (Kutler and Simon 2009).

TABLE 1: POPULATION TRENDS BY AGE, RACE, AND SEX

<table>
<thead>
<tr>
<th>Age Range</th>
<th>2010 Population</th>
<th>2010 % of Total</th>
<th>2030 Population</th>
<th>2030 % of Total</th>
<th>2050 Population</th>
<th>2050 % of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 20</td>
<td>84,150,000</td>
<td>27.1%</td>
<td>97,682,000</td>
<td>26.2%</td>
<td>112,940,000</td>
<td>25.7%</td>
</tr>
<tr>
<td>20–64</td>
<td>185,854,000</td>
<td>59.9%</td>
<td>203,729,000</td>
<td>54.5%</td>
<td>237,523,000</td>
<td>54.1%</td>
</tr>
<tr>
<td>65 and Older</td>
<td>40,229,000</td>
<td>13.0%</td>
<td>72,092,000</td>
<td>19.3%</td>
<td>88,547,000</td>
<td>20.2%</td>
</tr>
<tr>
<td>Total</td>
<td>310,233,000</td>
<td>100.0%</td>
<td>373,504,000</td>
<td>100.0%</td>
<td>439,010,000</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Source: U.S. Census Bureau

**TABLE 1: POPULATION TRENDS BY AGE, RACE, AND SEX**

<table>
<thead>
<tr>
<th>Race</th>
<th>2010 % of Total</th>
<th>2030 % of Total</th>
<th>2050 % of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Whites alone</td>
<td>79.5%</td>
<td>76.6%</td>
<td>74.0%</td>
</tr>
<tr>
<td>Blacks alone</td>
<td>12.9%</td>
<td>13.0%</td>
<td>13.0%</td>
</tr>
<tr>
<td>Asians alone</td>
<td>4.6%</td>
<td>6.3%</td>
<td>7.8%</td>
</tr>
<tr>
<td>All other races*</td>
<td>3.0%</td>
<td>4.0%</td>
<td>5.2%</td>
</tr>
</tbody>
</table>

*“All other races” includes American Indian, Alaska Native, Native Hawaiian, and other Pacific Islanders.

The most common race given for reporting Hispanics was "white." In 2010 49.7 million people or ~16% of the U.S. population identified themselves as Hispanic. If current demographic trends continue, this is expected to increase to 85.9 million in 2030 (~23%) and 132.6 million in 2050 (~30%).

Source: U.S. Census Bureau; Please note: data based on rounding.

<table>
<thead>
<tr>
<th>Age Range</th>
<th>2010 Population</th>
<th>2010 % of Total</th>
<th>2030 Population</th>
<th>2030 % of Total</th>
<th>2050 Population</th>
<th>2050 % of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Males — Total</td>
<td>152,753,000</td>
<td>49.24%</td>
<td>183,870,000</td>
<td>49.23%</td>
<td>215,825,000</td>
<td>49.16%</td>
</tr>
<tr>
<td>Under 18</td>
<td>38,437,000</td>
<td>12.39%</td>
<td>44,808,000</td>
<td>12.00%</td>
<td>51,789,000</td>
<td>11.80%</td>
</tr>
<tr>
<td>18–64</td>
<td>97,024,000</td>
<td>31.27%</td>
<td>106,768,000</td>
<td>28.59%</td>
<td>124,120,000</td>
<td>28.28%</td>
</tr>
<tr>
<td>65 and Older</td>
<td>17,292,000</td>
<td>5.57%</td>
<td>32,294,000</td>
<td>8.65%</td>
<td>39,917,000</td>
<td>9.09%</td>
</tr>
<tr>
<td>100 and Older</td>
<td>15,000</td>
<td>-0.01%</td>
<td>51,000</td>
<td>-0.01%</td>
<td>172,000</td>
<td>-0.04%</td>
</tr>
<tr>
<td>Females — Total</td>
<td>157,479,000</td>
<td>50.76%</td>
<td>189,634,000</td>
<td>50.77%</td>
<td>223,185,000</td>
<td>50.84%</td>
</tr>
<tr>
<td>Under 18</td>
<td>36,780,000</td>
<td>11.85%</td>
<td>43,007,000</td>
<td>11.51%</td>
<td>49,785,000</td>
<td>11.34%</td>
</tr>
<tr>
<td>18–64</td>
<td>97,763,000</td>
<td>31.51%</td>
<td>106,829,000</td>
<td>28.60%</td>
<td>124,769,000</td>
<td>28.42%</td>
</tr>
<tr>
<td>65 and Older</td>
<td>22,937,000</td>
<td>7.39%</td>
<td>39,789,000</td>
<td>10.66%</td>
<td>48,630,000</td>
<td>11.10%</td>
</tr>
<tr>
<td>100 and Older</td>
<td>65,000</td>
<td>0.02%</td>
<td>156,000</td>
<td>-0.04%</td>
<td>429,000</td>
<td>-0.10%</td>
</tr>
<tr>
<td>Total — ALL</td>
<td>310,233,000</td>
<td>100.0%</td>
<td>373,504,000</td>
<td>100.0%</td>
<td>439,010,000</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Source: U.S. Census Bureau; Please note: data based on rounding.
Diversity and Cultural Changes

Demographic data indicate that the U.S. population is becoming increasingly diverse racially, with the Hispanic population estimated to be about 23 percent of the total by 2030 and 30 percent by 2050. Younger generations are increasingly diverse. As of 2008, 58 percent of millennials considered themselves white or Caucasian and 42 percent were a minority. Social diversity is increasing as well, with a growing number of single heads of households as well as gay and lesbian couples who can benefit from financial advice. Same-sex couples need specialized financial planning to ensure they receive the same legal benefits that heterosexual couples receive automatically.

Additional Trends

According to Tiburon research, other trends also will impact the industry in the future:

Technology

The Internet will continue to fuel the technology revolution and online investor options will continue to grow in importance.
- More than half of wealthy consumers believe that engagement with the Internet and digital technology contributed to their ability to create wealth and more than three-quarters believe that these will contribute to their future success five years into the future.
- Almost two-thirds of wealthy investors believe that collaborating with others online will be important to their continued wealth creation.
- Offering innovative technological solutions will be an increasing need—and expense—in all segments of the financial services industry in the decades to come, to streamline efficiencies and to serve and retain clients.
- Technology will continue to allow more consumers to design their own product offerings, lessening dependency on banks or large institutions. This à la carte approach allowing investors to select features in an annuity or subadvisors in a customized separate account will become the norm in product design.

Future Products

Product development will be influenced by consumers’ focus on increasing fiscal conservatism and deleveraging, and a growing population in retirement. Despite a prolonged low-interest-rate environment, and even with rising rates, consumer behavior will be altered for a generation in terms of how investors think about lower risk or cash-equivalency investing. This will result in the following:
- Need for guaranteed return and income-generating products
- Continued and accelerating innovation of fee-based accounts
- Accelerating product shifts toward lower-total-cost investment vehicles, which will ultimately influence total cost of ownership, including for actively managed accounts
- Growth of indexing and exchange-traded funds
- Continued growth in popularity of unbundled products (separation of advice from product)

Other Trends

- Demand for transparency on fees and charges
- Full implementation of Dodd-Frank and/or other financial services reforms
- Settlement in some form of the common fiduciary standard for delivery of retail advice
- Higher percentage of participants in self-directed retirement plans and continued expansion of auto enrollment; likelihood of mandated participation in the United States by 2030
- International markets and consumers will have an increasing impact on the U.S. and world economies

2030 Scenario #1

Continued growth in the wealth management business is driven by independent advisors, online tools and advice companies, and emerging international markets. The financial services industry has consolidated through mergers and acquisitions to enable economies of scale and allow success despite shrinking margins. Venture capital opportunities are plentiful. Focus intensifies on retirement income with accelerated growth in investable assets due to retirement account rollovers. The independent channel continues to grow and fee-based advisors increasingly dominate the market. However, the role of financial advice has evolved so that the value exchange is more transparent.

The industry has evolved, realizing what can be commoditized and what cannot. Recognizing that money is a means to an end, financial advisors now provide a more comprehensive spectrum of services that demand customization, including help with life-planning decisions. Trusted advisors become stewards of their clients’ goals as well as their wealth. Transparency is essential regarding fees and other charges, as well as explanations of risk/reward trade-offs. A fiduciary standard is the norm and consumers are more active participants in the planning and investment process. Financial advisors and the aided do-it-yourself channel reach collaborative leverage, ultimately benefitting the client.

The most-successful advisors have a well-thought-out succession plan, implemented over a minimum of several years to allow for smooth transition with their intergenerational clients. Their successors are well-educated, and through association with other professionals are able to provide expertise in the areas of investments, insurance, tax planning, retirement strategies, and estate planning. They are likely to be part of a team of advisors where members develop areas of specialization, allowing the firm to demonstrate effectiveness in terms of
Without professional input and encouragement, fewer investors take action to develop and implement long-term plans; others make poor decisions. Either situation jeopardizes long-term financial security.

Conclusions

With either scenario, the prolonged slow economic recovery coupled with prior financial services stumbles will result in a generation of more risk-averse consumers. Regulatory initiatives will continue, but are unlikely to be successful in legislation aimed at breaking up “too big to fail” institutions.

Demographic trends will produce continued focus on retirement income: accelerated growth in investable assets, insurance in force, and expansion of broadly defined wealth management services. The growth in these services likely will be driven by independent advisors, online tools and advice companies, and emerging international markets.

- Leading fee-based financial advisors increasingly will dominate the market.
- Retail banks will continue to lose power.
- Wirehouses will embrace the fee-based channel and direct resources into acquisition and organic growth of registered investment advisors.
- Direct distribution models are also likely to grow as consumers continue to embrace technology to help them meet their financial services needs.

Successful investment management firms will embrace international markets. China, India, and other areas in Asia are likely to become good markets for gathering assets in the coming decades. The emergence of a new

Continued on page 14
Lynch
Continued from page 9

sumer class in China will change the balance of economic power.

Some would suggest demographics alone should generate a multi-decade boom for financial services firms. At some level the demographic shift certainly will benefit the industry; to what extent this will occur depends largely on the decisions current and future leaders make. Where those strategic decisions are focused on innovation and the consumer, we believe the future can represent the best of times. Where those decisions focus more inwardly on the status quo and what is perceived to be solely best for the industry, we believe the future is uncertain at best.

Matt Lynch is a principal at Tiburon Strategic Advisors, where he has led numerous corporate strategy engagements for a wide range of financial services firms. His book, with Tiburon Managing Partner Chip Roame, Building Innovative and Ethical Financial Services Businesses—Insights from Tiburon CEO Summit Award Winners, will be published by Wiley in 2014. Contact him at mlynch@tiburonadvisors.com.

Endnotes
4 Veena A. Kutler and Annette F. Simon of Garnet Group LLC are involved with the Women’s Initiative of the National Association of Personal Financial Advisors (NAPFA). See Kutler and Simon (2009).

References

Continued from page 13

and serves on the editorial boards of Investments & Wealth Monitor and the Journal of Investment Consulting.