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On the cusp of change: North American wealth management in 2030

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On the cusp of change: North American wealth management in 2030

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On the cusp of change: North American wealth management in 2030

Recent decades have witnessed meaningful changes to North America's wealth management industry's structure and dynamics. The first decade of the 2000s saw the further democratization of trading due to increased access through technology, and the current decade has seen the convergence of banking and investing and the rise of fee-based managed accounts. These seismic shifts raise the question of what the next decade will bring—and how we might describe the 2020s from the perspective of 2030.

First a glance backward: According to McKinsey research, in 2000, the North American wealth management industry totaled US$13 trillion in client assets. In the next ten years, client assets grew approximately 45 percent, reaching $19 trillion, with a profit margin of 16 bps in 2010. There were about 420,000 advisors in the US and Canada in 2010. By 2018, client assets rose 64 percent compared to 2010, reaching about $30.5 trillion, and margins improved to 18 bps. While the total number of advisors remained largely unchanged, the advisor workforce aged materially; in the US, only 25 percent were under the age of 44, compared to 33 percent in 2010.

This evolution occurred against a backdrop of more fundamental changes in the economy. In the last ten years, global data volume also skyrocketed—from 2 zettabytes in 2010 to 41 zettabytes in 2019 (a zettabyte is 1 sextillion bytes). Internet users globally doubled to roughly 4 billion, and monthly active Facebook users grew from 370 million in 2010 to about 1.6 billion in 2019.

Now, looking ahead, we expect the wealth management industry to evolve again, along the following lines:

— The "face" of the consumer is changing as: women control more assets; Millennials and Gen Xers gain control of more assets—and their preferences and comfort with digital tools have a profound impact on other age groups; and participants in the expanding gig economy are increasingly in need of new approaches to protection and retirement planning

— Customer needs are shifting away from risk-based portfolio construction to outcome-based planning across multiple dimensions (e.g., investments, banking, health, protection, taxes, estate)

— Client expectations are rising rapidly—for things like virtual engagement, seamless apps experience, omnichannel support, instant payments—at a pace set by industries outside of financial services

— Rapid technological progress—robotic process automation (RPA), smart workflows, machine learning, advanced analytics, natural-language processing, and cognitive agents—enabled by the proliferation of data is reshaping value chains across industries, bringing more automation and efficiency and, in turn, changing the nature of work performed by humans

These trends and others will lead to a meaningfully different wealth management industry by 2030.

What will happen to advice?

In the next ten years, the nature of advice and the way it is delivered and consumed will fundamentally change.

The "Netflixing" of advice

In 2030, up to 80 percent of new wealth management clients will want to access advice in a Netflix-style model—that is, data-driven, hyper-personalized, continuous, and, potentially, by subscription.

The emergence of a tailored and personalized model underpinned by data can be observed across industries, but is perhaps most prevalent in entertainment—in the shift from physical music recordings to unlimited streaming of digital music, or from seeing films in movie theatres to streaming them from home—or from anywhere. The "streaming giants" are using customer data to continuously and deeply understand preferences and develop hyper-personalized recommendations.

For wealth managers, continuous access and automatic hyper-personalization could change the terms of success. Advisors can embark on the journey now by using data and technology on a more frequent and consistent basis.

The "fit-nance" tracking of advice

Advice will also be refocused. By 2030, at least 80 percent of advisors will offer goal-based advice, and about half of clients will actively pursue and track bite-sized goals (e.g., saving for three college credits a month)—and this granular goal-tracking will span customers' investment, protection, education, retirement, and broader wellness.

Despite the recent progress made by goals-based advice, only 39 percent of affluent consumers have a written financial plan. Furthermore, success in goals-based advice will also require a dedicated approach to modifying client behaviors and mindsets to help them achieve their goals. To bring goals-based advice to life, and make it practical, intuitive, and actionable, advisors need to leverage behavioral economics techniques such as gamification and community-based competitive measures.

Outside of wealth management, the success of goals-based methodologies can be seen in the skyrocketing growth of fitness tracking devices, which first showcased the psychological power of breaking down large goals, subsequent daily monitoring and tracking, and the importance of validation and feedback. Discovery, a South African financial services provider, launched a behavioral-change program called Vitality. The program incentivizes customers to set goals, make healthier choices, track their progress, and gain "status" in the community, and dynamically rewards them for reducing their risk through insurance premium reductions and other benefits such as discounts on cars and flights.

By 2030, we believe that all successful wealth managers will develop services that help their clients dynamically monitor, adjust, and achieve their goals.

The "big tech effect" on advice

Leading big tech ecosystem players have emerged as the core infrastructure providers of the wealth management industry, accruing significant economics through their analytics and cloud services offerings. The clout of the big tech infrastructure providers will only grow over time. Furthermore, barring regulatory hurdles, they could become direct competitors, and ultimately vastly increase pricing transparency and ease of access.

So far, big tech firms have participated in the wealth management industry largely through the provision of cloud-computing services, which have become a core part of the infrastructure of many wealth management firms. For example, auto-scaling capabilities offered by cloud-computing service providers ensure website stability during days of market turbulence and peak traffic by "spinning up" additional capacity. This is one example of how big tech firms are quickly becoming leading "infrastructure" providers for the wealth management industry and, in the process, extracting a greater share of the industry's profit pool. In the next ten years, the wealth management value chain will likely consolidate around a set of infrastructure providers who will capture a significantly larger portion of the industry's economics. In this future state, wealth managers will rent larger portions of their value chain from third parties and their ability to manage these relationships will be strategically differentiating.

It remains to be seen whether "ecosystem" big tech firms—which own end-customer relationships and offer an interconnected set of services—have ambitions to enter the advice space itself or whether they are content to remain service providers to the industry. If they do enter, they have customer, technological, and capital advantages that could meaningfully distinguish them from incumbents. Amazon, for example, has more than 100 million Prime households in the US (roughly 82 percent penetration)–that is a lot of touchpoints.

One potential "future" can be seen in China, where Tencent, which offers a host of financial services, including lending and payments, acquired a license to sell mutual funds through their chat app WeChat in January 2018. Previously they had only been able to act as a platform through which third-party fund companies could sell their products. Currently, the regulatory environment in the US may be a barrier to entry for big tech firms seeking to get deeper into advice. Over time, however, this could change.

What will happen to advisors?

As the nature of advice and the way it is accessed and consumed shift, advisors will need keep up with the changes.

The "face" of the advisor will fundamentally change

Imagine a world where half of advisors across channels in 2030 are women, up from about 33 percent today, according to McKinsey research (in private banks the figure is closer to 45 percent today); 40 percent are minorities, up from roughly 20 percent today; and 50 percent are mid-career in tenure (30 to 40 years old), up from about 25 percent today. The approach to recruiting and talent sources will need to fundamentally change to realize a different mix in our advisor forces.

As women, minorities, Gen Xers, and Millennials become a higher share of the client base, wealth management will see the rise of advisors who speak their clients' "language," who know how to garner their trust, and are more digitally savvy.

While women will soon control the majority of the assets in the US, no wealth manager is known to have cracked the code on serving women through new and differentiated value propositions thus far. In the coming decade, it is likely that an incumbent or newcomer will figure out how to appeal to this segment and meet their needs and preferences and, in turn, achieve disproportionate organic growth.

More broadly, it is clear that firms will need to reflect the communities they serve.

Advisors will continue to expand their remit
By 2030, as advice becomes increasingly analytics-driven and automated, advisors will shift their focus to comprehensive planning beyond the portfolio. As a result, the number of advisors will drop by up to a fifth. This will also be in part driven by the natural retirement of advisors—Cerulli forecasts, for example, that over the next five years about 7,000 "traditional" advisors will retire.

Today, many advisors offer some kind of financial planning (the percentage of clients who actually use the service varies greatly by advisor and by firm). In fact, there are about 80,000 Certified Financial Planners in the US, some of whom are part of a larger financial advisor's team. We believe advisors in the next decade will require a different set of skills tailored to client needs. This shift will also be fueled by the proliferation of the hyper-personalized advice model and the emphasis on bite-sized goals.

In the next ten years, advisors will gradually shed their role as investment managers and become more like "integrated life/wealth coaches" who advise clients on investments, banking, healthcare, protection, taxes, estate, and financial wellness needs more broadly. As the industry undergoes this shift, wealth managers will need to fundamentally rethink their recruiting strategies and training programs.

Transparency will become ubiquitous with a focus on user ratings
By 2030, clients will join community forums to rate and review advisors, especially as advice becomes more "democratized."

To date, an advisor's reputation has been largely shaped by word of mouth; no systematic, transparent form of advisor ratings or reviews exists. This is bound to change as the bar for customer experience is set by industries outside of financial services, information availability increases, and data-sharing continues to grow in relevance.

Transparent, community-based ratings and reviews are common in other industries. Ride-sharing drivers have ratings and reviews, coupled with highlights of their track record (e.g., number of rides they have given, percent of five-star rides). Doctors are rated and reviewed on platforms such as ZocDoc and Opencare—which are particularly influential given that patients increasingly choose doctors and make appointments online. The transparency and community-based nature of these reviews tend to encourage superior performance and customer outcomes in these industries—as they will in wealth management.

The emergence of transparency and user ratings on advisor performance may lead to a decline in client stickiness; as information and "alternatives" abound, clients may more readily switch between advisors—although these same trends could encourage better advisor performance that helps retain clients.

What will wealth management firms do?

As customer preferences shift and as advisors adapt, wealth management firms will need to make strategic choices and determine where and how they will play in the next ten years.

Wealth tech and platforms will demand new talent
By 2030, wealth managers will leverage data and advanced analytics in every aspect of their business, both client-facing and non-client facing, and this shift will change the type of talent they will need to succeed.

A compelling example from China is Lufax, the Ping An-backed online wealth management platform that engages customers purely through its mobile app. Lufax leverages its wealth of behavioral data in every aspect of its business—from deploying advanced analytics to understand customers' needs and risk appetite and projecting their future investment paths, to leveraging big data to create dynamic and detailed "profiles" of each of its 5,000 investment products, including information on underlying assets, fund manager identity, skills, and style, and using artificial intelligence to "match" these products with individual customers based on their shifting needs.

As data increasingly becomes the "raw material" for success, financial services providers need to behave and function like tech firms. In recent years, banks have been competing with the likes of Google and Facebook for tech talent. The same will be true for wealth managers as they seek to meet customers' digital demands, make data-driven, AI-enabled investment decisions, and improve operational effectiveness.

Wealth managers as aggressive cost managers

In the coming decade, the number of clients served by wealth managers will grow at unprecedented rates as lower-cost solutions penetrate historically underserved segments. To serve these clients profitably in an evolving environment in which entire revenue pools can disappear (e.g., online trading commissions), wealth managers will need to turbocharge their operational excellence to defend their profit pools.

We anticipate that in order to profitably serve new customers, firms will need to be radically leaner than they are today and set a rising bar for operational excellence. They will need to use technologies like AI and robotics to reshape economics and reduce more than half of administrative work, allowing them to remain profitable in an era of greater fee transparency and lower fees.

Most US and Canadian wealth managers have struggled to fully deploy some of the recent milestone developments in technology—RPA, smart workflows, machine learning, advanced analytics, natural-language processing, and cognitive agents. Front-end digitization in wealth management has been lagging many other consumer-facing industries, and playing catch up with constantly rising customer expectations. At the same time, tech and operations platforms are in dire need of modernization. Across the industry, firms remain saddled with tech debt, manually intensive processes, and complex servicing arrangements, leading to stubbornly high operating costs, reduced (and sometimes negative) operating leverage, and unrelenting margin pressure.

However, some firms have started to capitalize on these technologies. For example, chatbots are now regularly deployed in online customer support, creating efficiency gains.

Despite North American wealth management firms' slow progress in the application of robotics and AI, the future is promising. The technology is rapidly maturing, and domain expertise is developing among both wealth managers and vendors, many of which are moving away from the one-solution-fits-all approach and toward more specialized solutions. Firms are also learning critical lessons about workflow; for example, how to more effectively manage handoffs between man and machine, and where typical process redesign/reengineering can be put off or even skipped in favor of automation—particularly where systems are likely to be replaced. In addition, the technological instrumentation of processes will enable the extensive measurement and collection of data, which will support innovation and the ability to make the technologies smarter and self-adjusting.

A handful of at-scale wealth managers will attempt to serve "everyone" while the rest will remain "exclusive"

We expect two winning models to emerge over the next decade: the first will be a handful of at-scale wealth managers offering the full spectrum of advice and engagement models for all client segments; the second model will comprise more exclusive, U/HNW-focused institutions that provide white-glove, specialized capabilities and services (e.g., access to private markets, estate and legacy planning services). While the latter group will be largely comprised of wirehouses, private banks, and RIAs that already specialize in the U/HNW segment, the former will be made up of a wider set of institutions, from direct firms to full-service firms and private banks. Two sets of dynamics are at work here:

— Over the last several years wealth managers of all sizes and types, from robo-advisor start-ups to private banks, have raced to offer a broader spectrum of advice models to appeal to the mass affluent segment. To be competitive and economically viable over the longer term, a firm will likely need to serve a few million households. Given that there are only about 30 million households in the US with $100,000 to $1,000,000 in investable assets, we believe only a select few will emerge as winners in this segment.

— Direct players have been gaining share in the HNW market traditionally controlled by wirehouses and private banks and now account for 13 percent of AUM, up from 11 percent five years ago. We expect direct firms to seek to deepen their relationships with HNW households—which currently use them mostly for low-cost services and products—by enhancing their HNW-focused capabilities and value proposition, especially as this segment accounts for more than 60 percent of the industry's revenue pool.

Over the next decade, we expect the continuation of consolidation in the industry, especially among direct firms that fail to "crack" the HNW segment and struggle to differentiate "upward." In addition, we expect that many traditional firms will fail to integrate "downward" and will remain completely upmarket, with a family-office/private bank model serving only the wealthiest clients and continuing to charge premium fees justified by highly bespoke products and services.

Integrated banking-wealth management "ecosystems" will emerge with a unique competitive advantage

The convergence of banking and wealth management is beginning, as evidenced by major banks building new wealth management offerings and, in turn, wealth managers building out their banking capabilities. These dynamics will continue, as customers increasingly demand integrated financial advice across their investments and cash management needs (i.e., checking, savings) and as wealth managers seek to tap into banking profit pools.

This convergence is a "win-win" situation for institutions that currently have both a wealth manager and a more traditional bank—the wealth manager can expand the isolated "investment relationship" it maintains with clients to one that addresses their primary financial services needs. Retail banking relationships help increase stickiness and are a prime source of low-cost deposits for funding needs.

In the coming decade, banking-wealth management ecosystems will become more commonplace and begin to accrue advantages that will multiply over time (e.g., more customer data, stickier relationships, cross-sell opportunities), putting competitive pressure on those wealth managers who remain "stand-alone."

What can wealth managers do in light of the "new age"?

Wealth managers must act today to prepare for the new age in wealth management.

— Drastically clean-sheet advice and engagement model and deploy more hyper-personalized, data-driven, and engaging approaches

— Heavily invest in and build customer insights engines, developing a comprehensive view of clients at the home-office level, including leveraging third-party data

— Rapidly launch recruiting and upskilling programs and develop a talent pool geared towards the future

— Radically transform mid and back office leveraging advanced technologies to achieve operational excellence

— Vigilantly monitor for consolidation on the horizon, and be prepared to join forces with competitors to harness synergies

The North American wealth management industry will undergo meaningful shifts in the next ten years, influenced by evolving customer segments and rules of engagement, rapid technological advances, and shifting competitive dynamics. These trends will have profound implications for both the nature of advice and for advisors' and wealth management firms' broader talent strategy, operating model, and sources of competitive differentiation. There are challenges and opportunities on the horizon—those wealth management firms that rise to the occasion and embrace the change will be in a position to thrive.