



# Perspectives on the Future of the Wealth Management Industry

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# The wealth advisory industry is undergoing significant change

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The industry move to the highest fiduciary standards is here to stay

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2

Asset a shifting to fee-based and portfolio construction is becoming a critical element of an advisor's value proposition

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In a fee-based world, advisors demand investment strategies that offer quality and value

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Portfolios built with active and passive strategies are key to managing risk and fee budgets

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5

The emergence of digital wealth technologies offers advisors the opportunity to scale

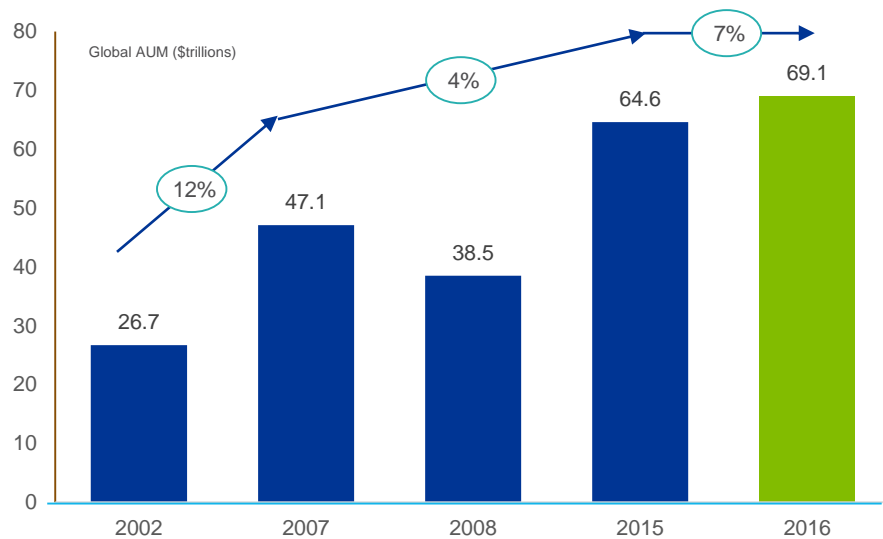
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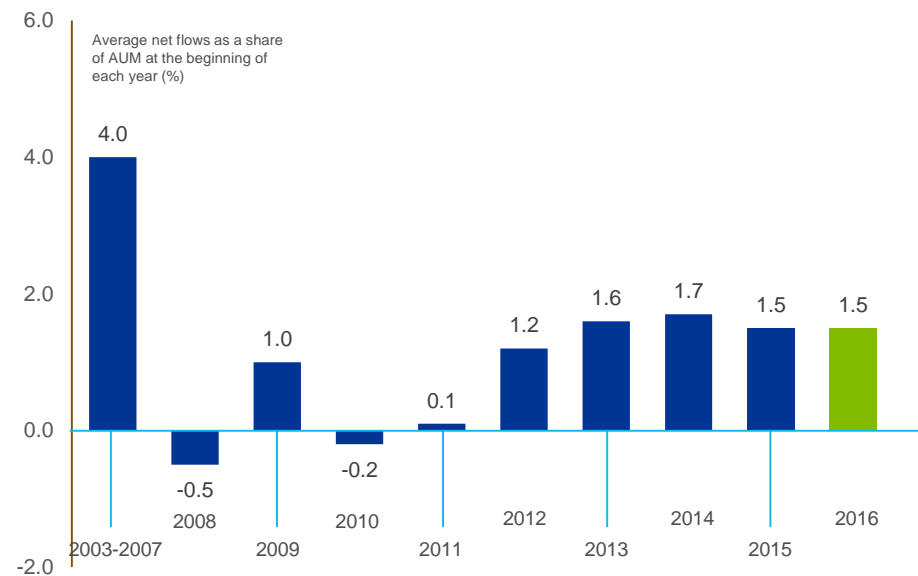
# Global Assets Under Management Growth

## Global AUM Grew 7%, mostly because of Rising Market Values

Global AUM rose 7%..



..while Net Flows were flat at 1.5%



Source: BCG Global Asset Management Market-Sizing Database, 2016

**In 2014, Wealth Managers major concerns were..**

**..and in 2017 the situation is the following:**

**Regulation**

The Industry paid closed attention to the changes required in US and Europe, but lack of clarity around the implementation phase

Still a burden for organizations, but they realize that forces put in place are not going to stop

**Technology**

Focus on the appearance of *"Robo-Advisors"*

Now in the age of digitization the focus is on 'front-end' client experience, risk management tools and hybrid advice

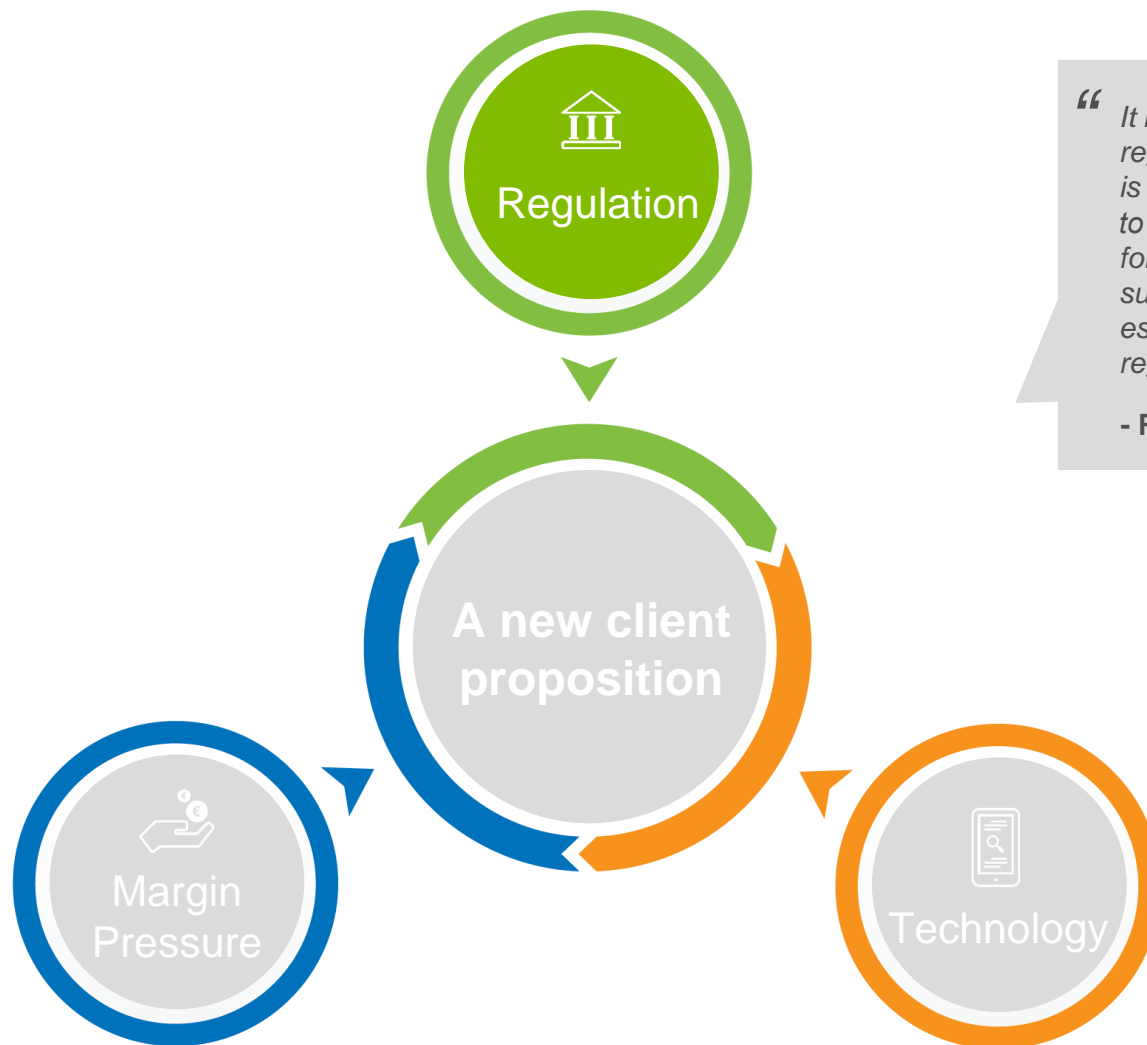
**Margin Compression**

Execution-only and traditional advisory challenged  
Fee-based advisory on the rise in Europe & US  
Product mix begins to change  
*'Barbellin'* acknowledged

Rapid growth of fee-based advisory  
Significant acceleration in indexed investing  
Rise of multi-asset/outcome oriented investing

Source: BlackRock Wealth Management Industry Surveys, 2014 and 2017

## Three forces are disrupting the value chain



“ It is an advantage to have all this regulation, because we see that it is more difficult for smaller players to keep up with it. It's more difficult for new entrants to become successful. So if you have an established operation, then regulation is also helpful ”

- Rabobank

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# Regulators are driving a shift to fiduciary standards & fee-based globally

## United States



- **Department of Labor (DoL) Fiduciary Rule** – Enforces best interest clause and fiduciary standards
- **Municipal Bonds and MSRB Rule Changes** – Requires brokerage firm pricing disclosure on bond trades

*Index and ETF; managed FI*

*Fee-based model*

## United Kingdom



- **Retail Distribution Review (RDR)**
- Ban on retrocessions (rebates from asset manager)
- Eliminate bias towards particular investment products and solutions
- Transparency

*Contraction in advisors & fees*

*Advice gap for smaller accounts*

## Europe



- **Markets in Financial Instruments Directive (MiFID II)**
- Ban on inducements
- Increased focus on investor protection
- Fee transparency and advisory model changing asset management

*Multi-asset outcomes*

*Guided architecture*

Source: BlackRock, as of August 2017

## Transparency: The focus is on pricing

### Cost given to the client by the financial institution

Investment 27,000 USD

Product cost (annual)	327 USD
Investment services costs (annual)	497 USD
Projected costs over 5 years	4,126 USD
Average cost per year	3%

**The investment seems expensive ...**

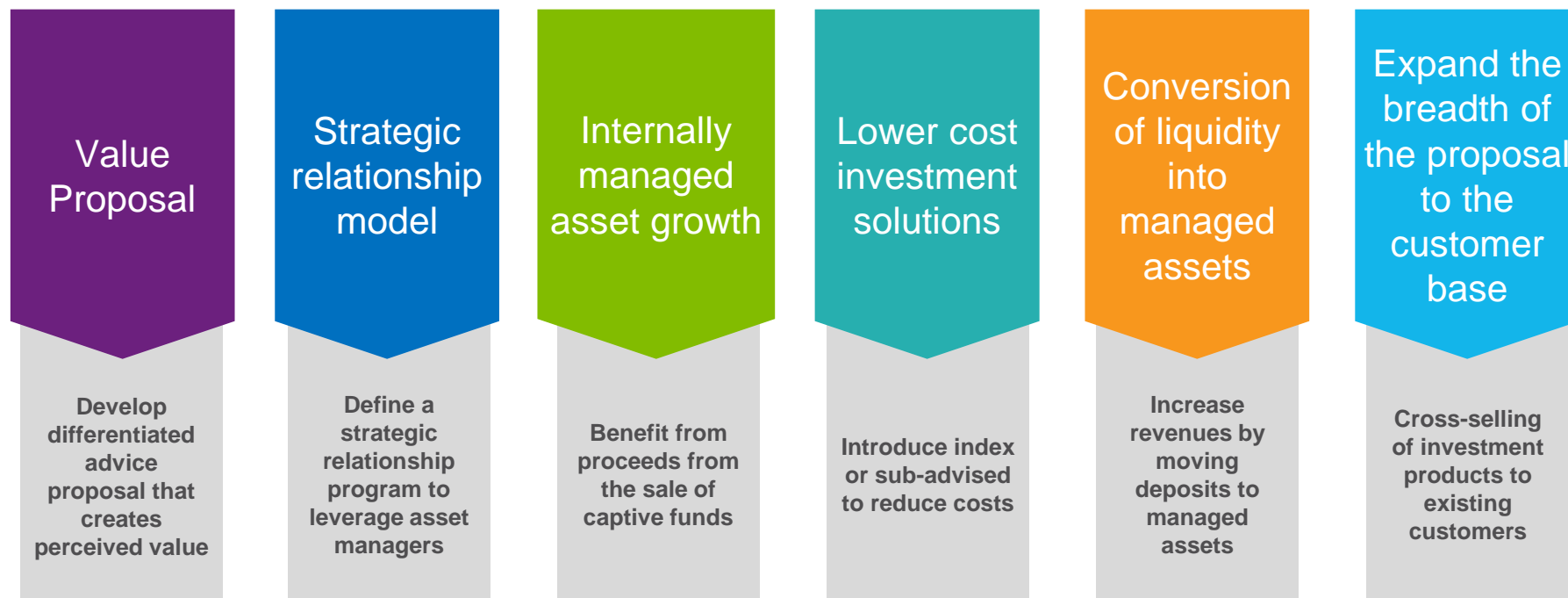
Wealth managers need to increase the real and perceived value they provide

Source: BlackRock, March 2017, For illustrative purposes only.

*“There is a strong interest on the part of the regulators worldwide to offer products in a transparent, efficient and clear way to the customers. It is in the interest of banks, regulators and clients to do so.”*

- Citi Consumer Bank, March 2017

# Challenge: Replacing income from lost retrocessions



Source: BlackRock. March 2017. For illustrative purposes only.



# Suitability: Aligning risk profiles with portfolio risk

Regulation puts suitability front and centre for Wealth Managers

The ability to monitor the suitability of investment recommendations over time is a core requirement:

- Match between risk profile and portfolio risk
- Understanding risk deviations in portfolios
- Justification for recommendation if questioned by regulator
- Wealth Managers wrestle with appropriate data to include in reporting

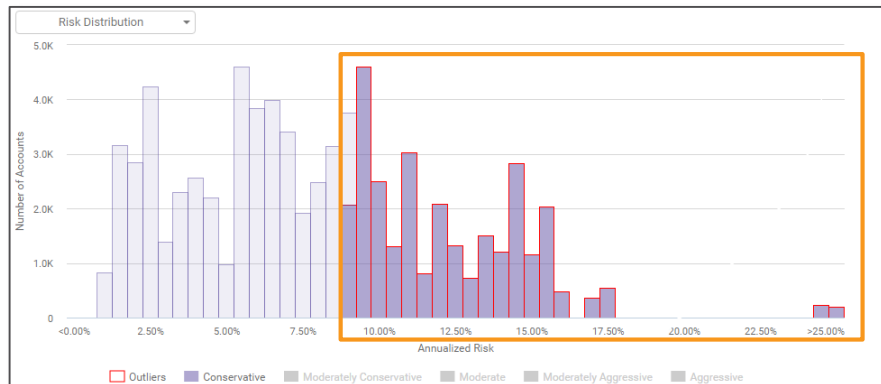
## The role of risk technology

- Identifying accounts which lie outside their risk profile bands
- Notification and remedial action

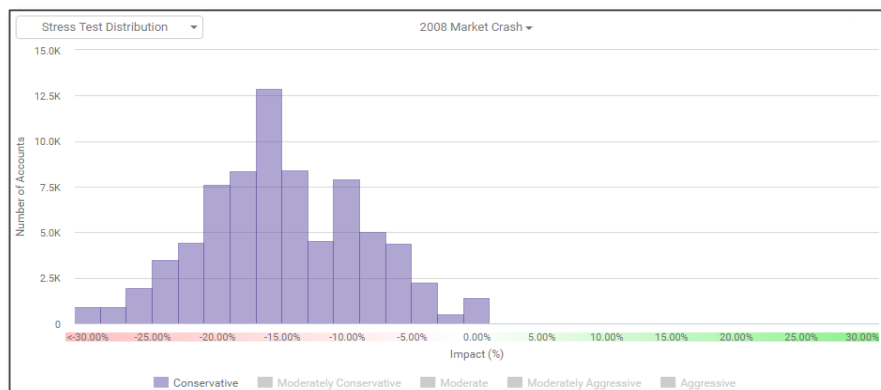
“Firms must obtain the following information from a client or a potential client before providing the above services: its **knowledge and experience** of the investment field in which the investment advice or portfolio management is to be offered; its **financial situation** including his **ability to bear losses**; and its **investment objectives** including the **risk tolerance**.”

NORTON ROSE FULBRIGHT, MIFID II ACADEMY:  
SUITABILITY AND APPROPRIATENESS, 2016

## Identifying portfolio outliers

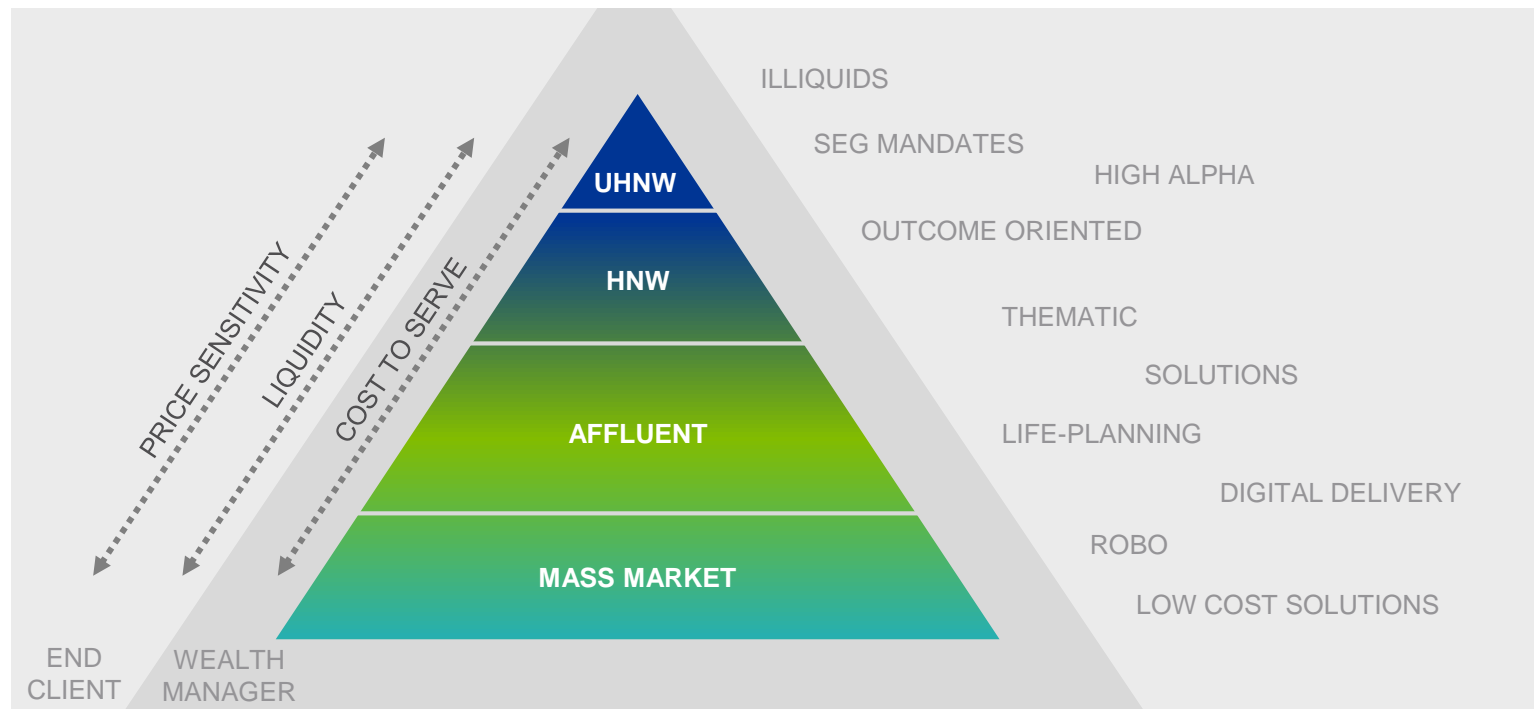


## Stress testing portfolios



Source: Aladdin Risk Monitor as of June 2017 (illustrative purposes only)

## Aligning the offering with the cost to serve

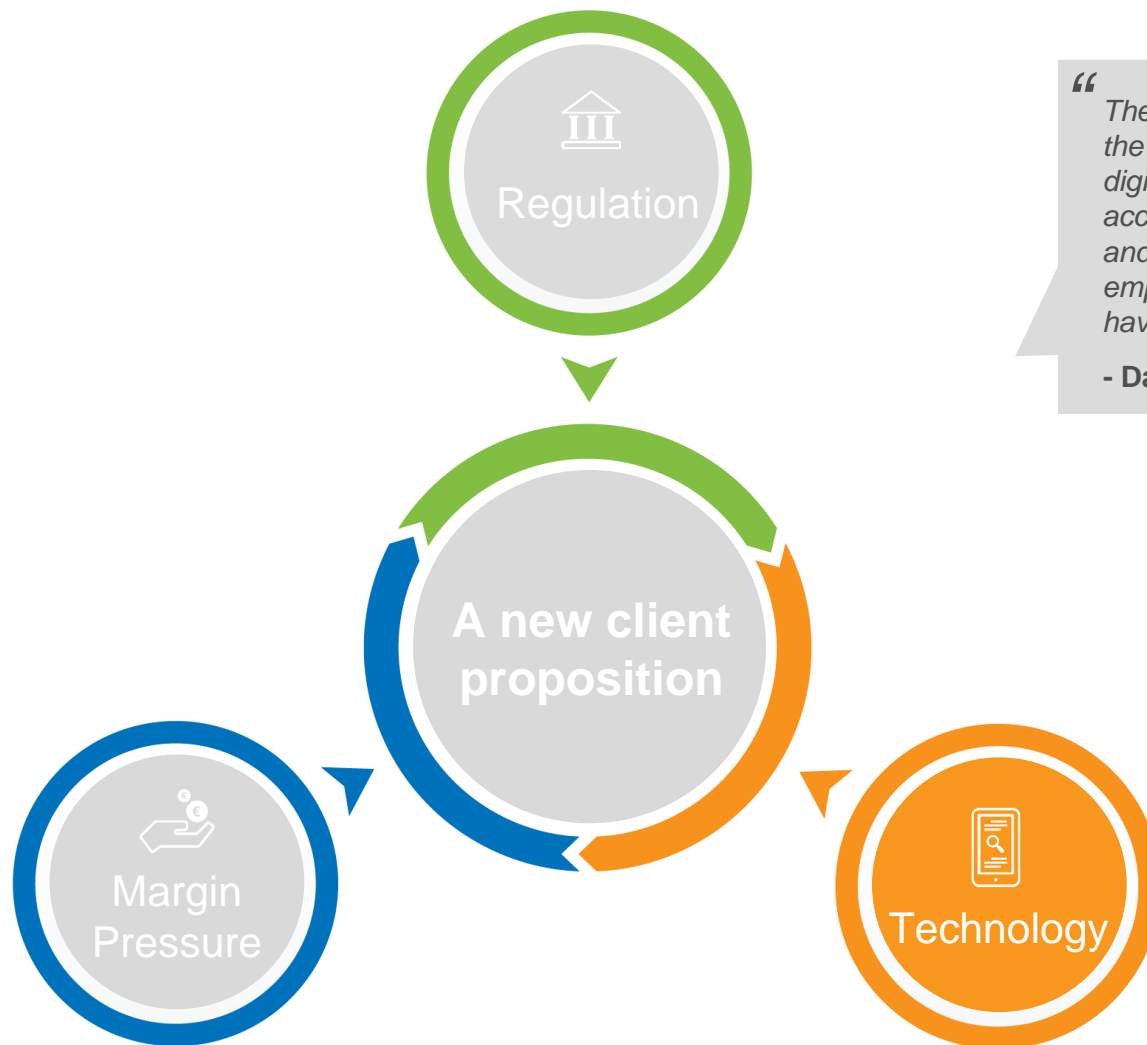


Source: BlackRock as of June 2017. For illustrative purposes only.

*“ You have to really look at your client base and have a very segment-specific offering, and then cater to the various segments in specific ways ”*

**- Deutsche Bank Wealth Management**

## Three forces are disrupting the value chain

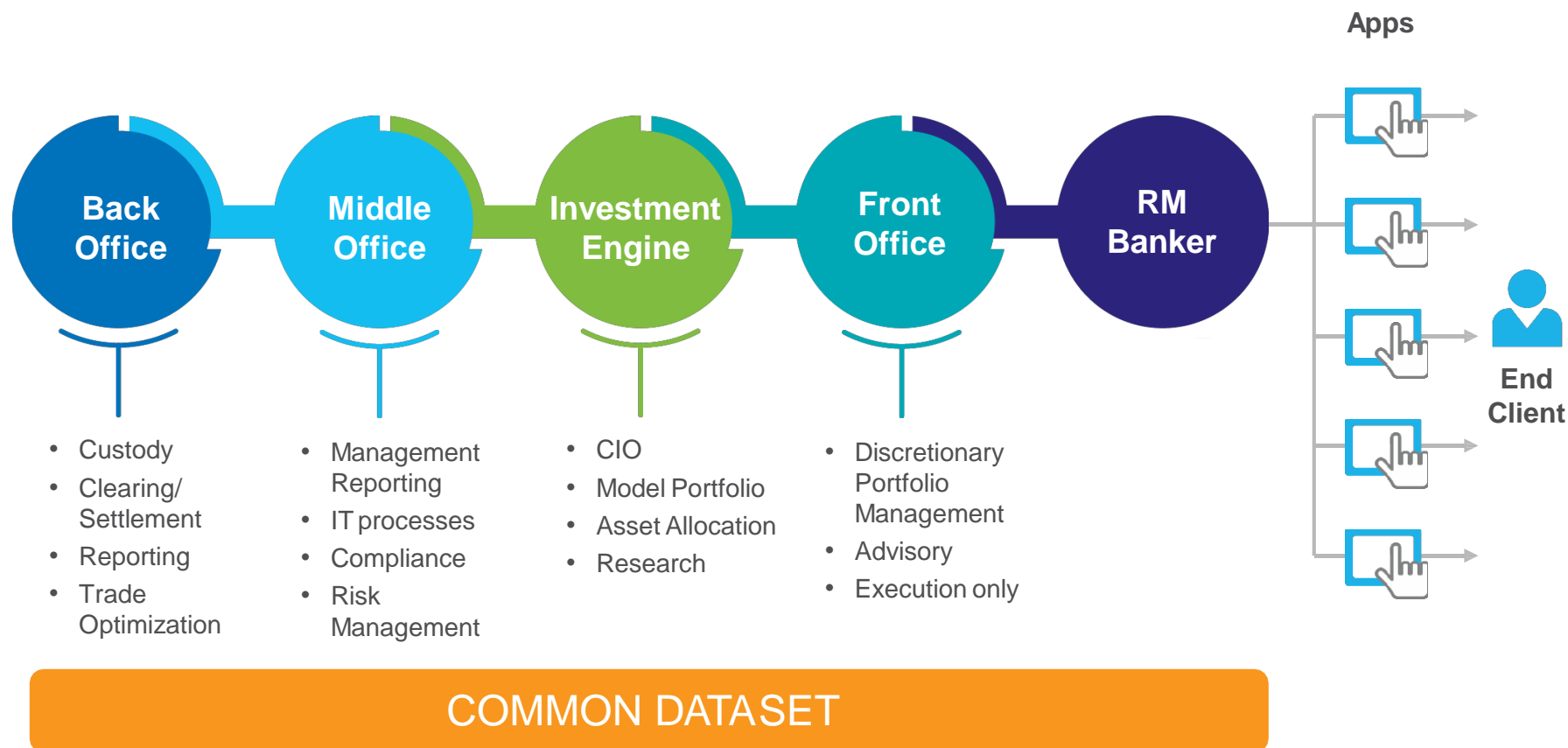


“ The big issue is how can we deliver the same kind of value through digitization that people used to accustom to their personal advisor, and how can we use digitization to empower the advisor so we still have a role to play. ”

- Danske

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# Digitalising The Bank Value Chain

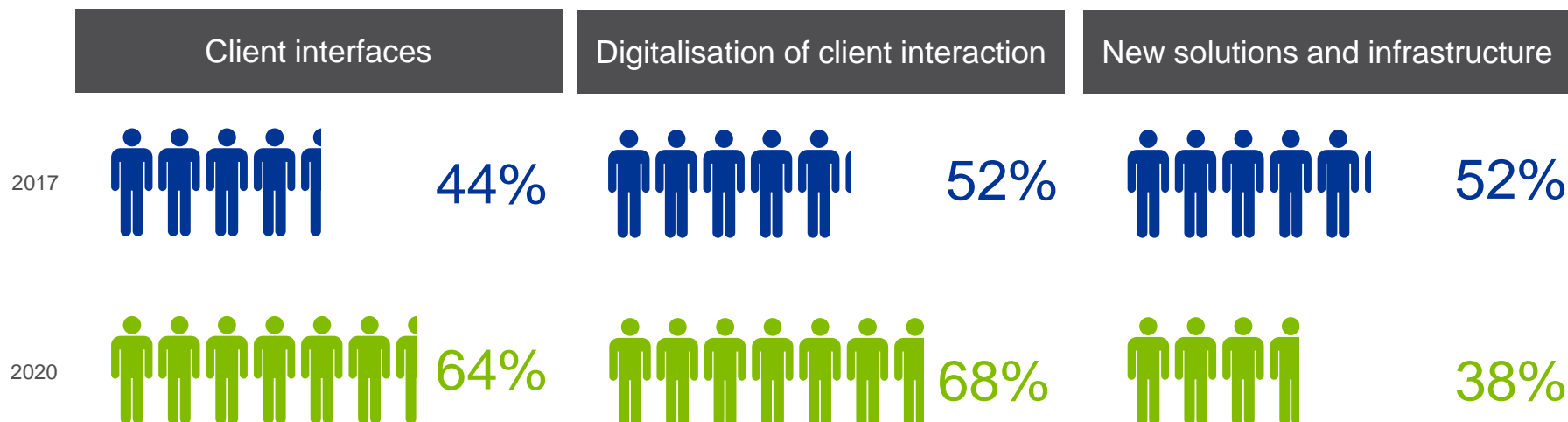


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# Client experience and relationship management are the next big industry focus

## Focus of technology investments

% respondents (selected all categories that apply, out of a total of 6)



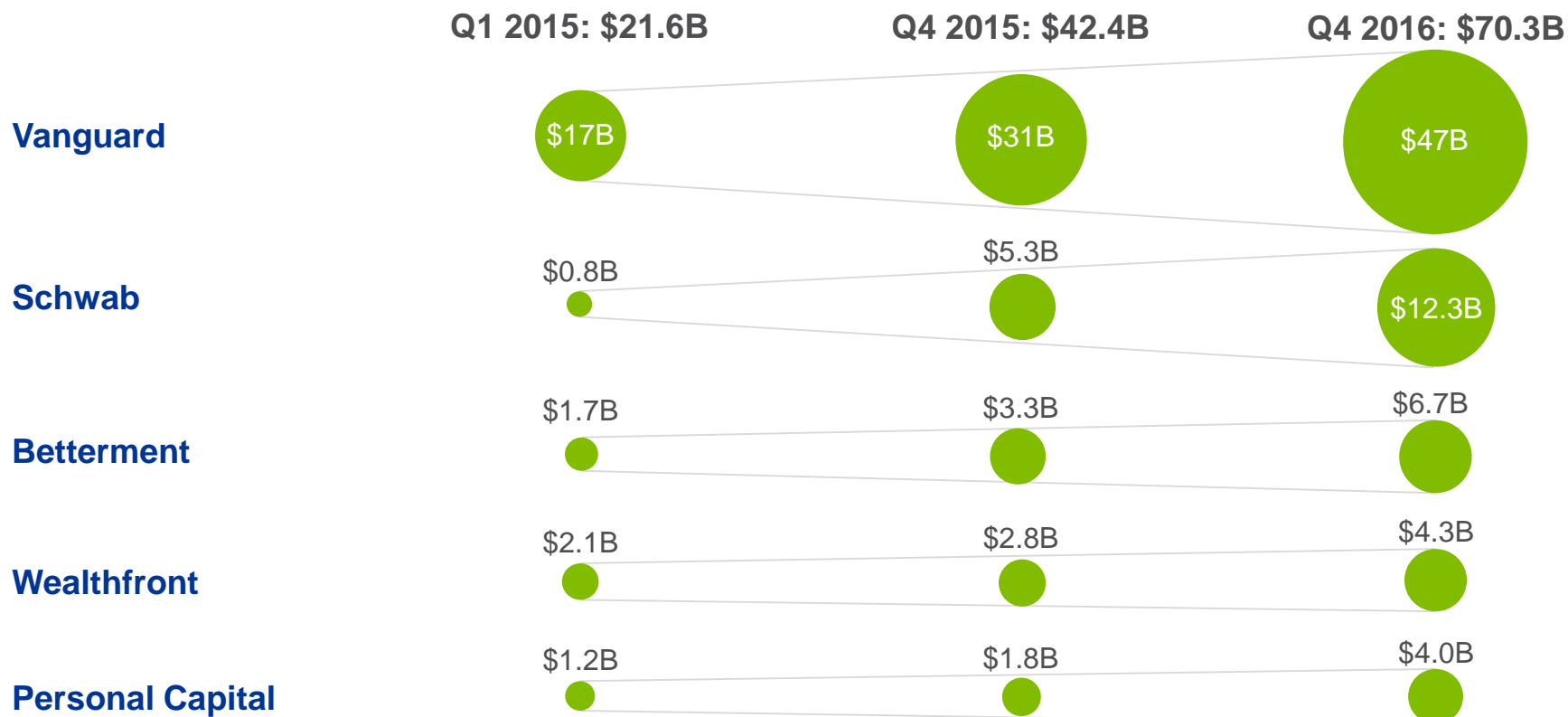
*“ We are investing in robo-advising to make it easier to offer the service to smaller clients, but also investing in apps to improve portfolio insight for all clients. So technology is important to make the offering cheaper, more profitable, or to keep it profitable ”*

**- Rabobank**

Source: Blackrock Wealth Management Industry Survey 2017

# The most successful robo-providers combine human and digital advice

## AUM for selected large robo-advisors



Factors for  
success

Brand

Existing  
Client Base

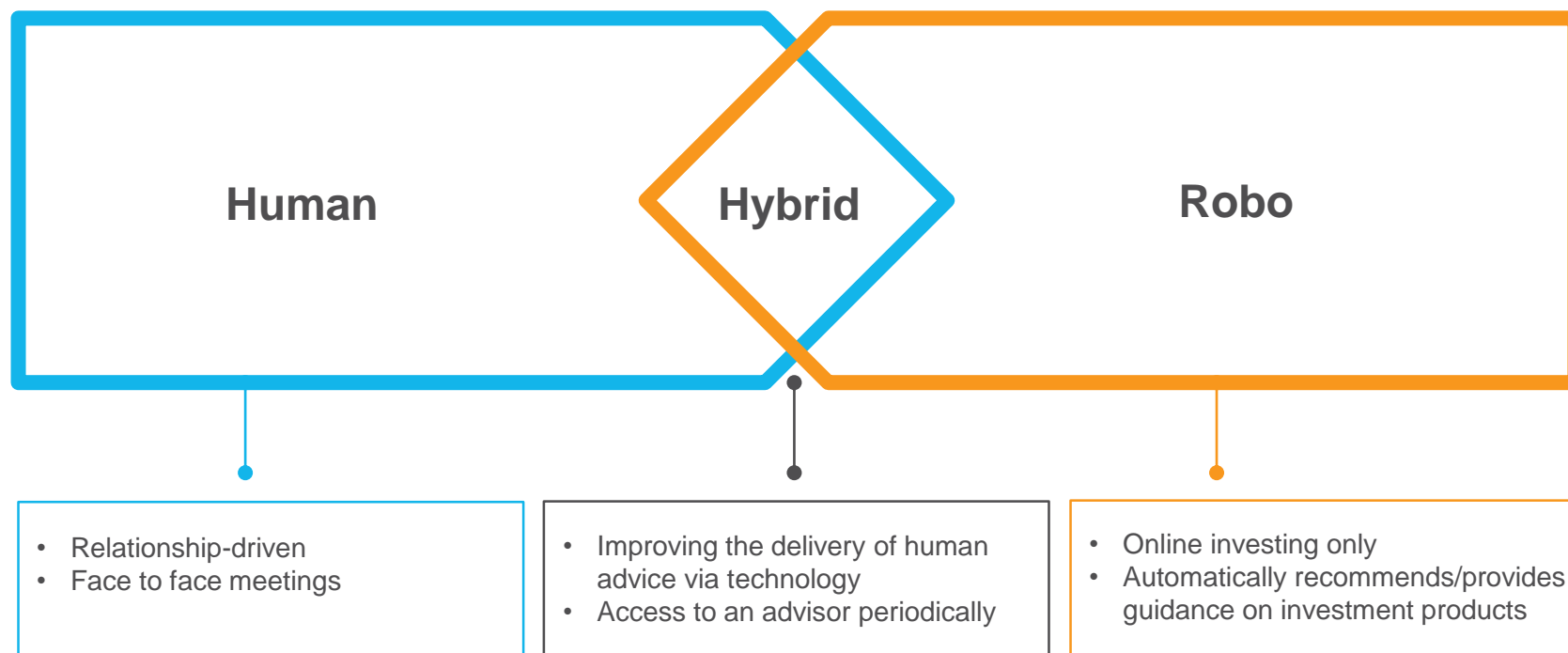
Existing  
Infrastructure

Regulatory  
Tolerance

Tech  
Innovation

Source: Company websites, "A Tour of the Top 10 Robos," January 24, 2017. <http://www.etf.com>

# Wealth Managers see Robo supporting, not displacing, human advisory



Source: BlackRock as of June 2017. For illustrative purposes only

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## Charles Schwab to combine robo-advice and financial advisers in new hybrid model

Financial giant targeting mass affluent clients with inexpensive planning services

Dec 13, 2016 @ 12:52 pm  
By Liz Skinner

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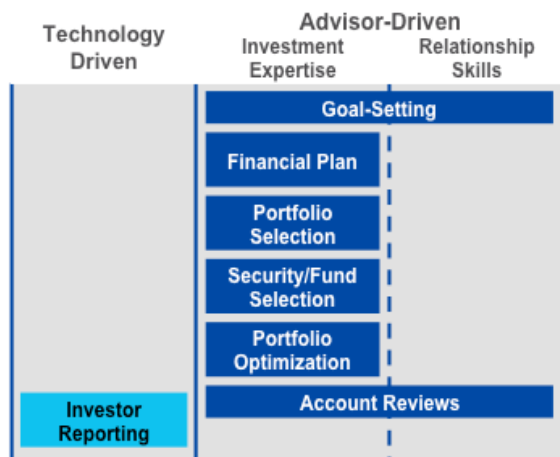
## Robo-Adviser Betterment Adds Human Option

Robo-adviser pioneer joins wealth-management industry's fast-growing trend of hybrid service

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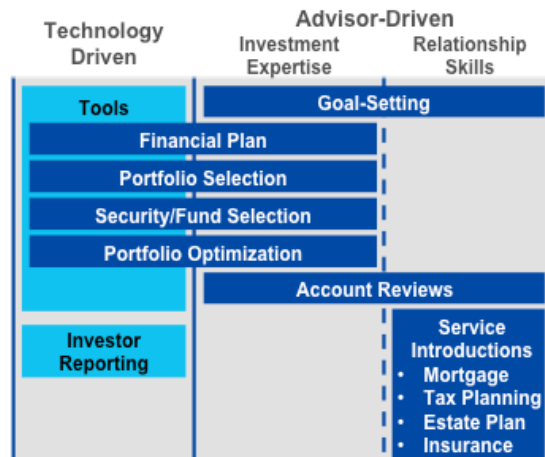
# Looking forward, wealth managers will automate what can be automated, and focus valuable FA time on high value activities like financial coaching

## Wealth Advisory Business Model: 1990's



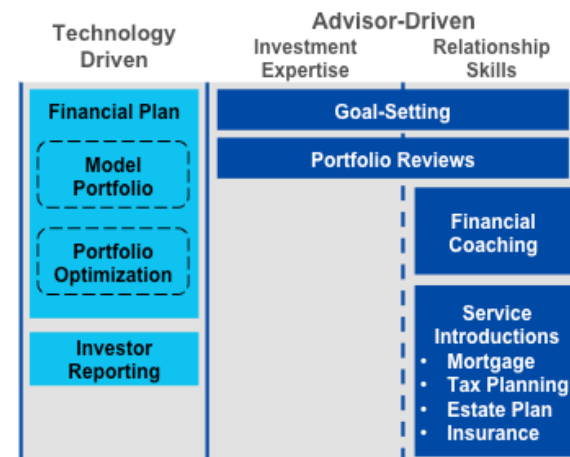
- Advisors valued for their individual investment expertise

## Wealth Advisory Business Model: Current



- More functions handled via the wealth platform
- Increasing focus on relationship services
- Decreasing importance of individual investment expertise

## Wealth Advisory Business Model: Future



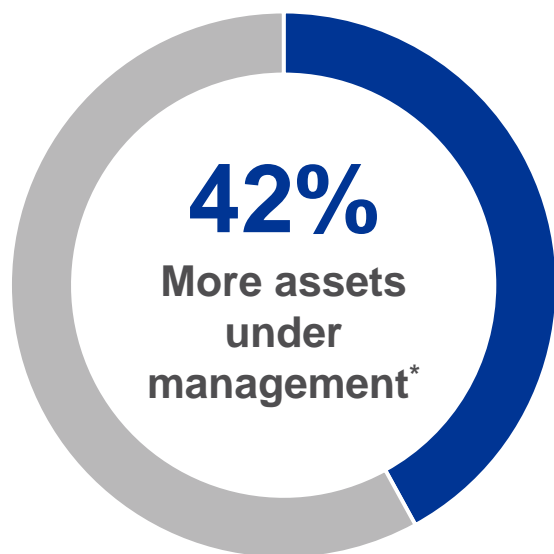
- Shift to more technology-driven wealth platform that performs key investment functions
- Advisors acts as private banker, providing life services and coaching clients

Source: Citi Business Advisory Services as of August 2017



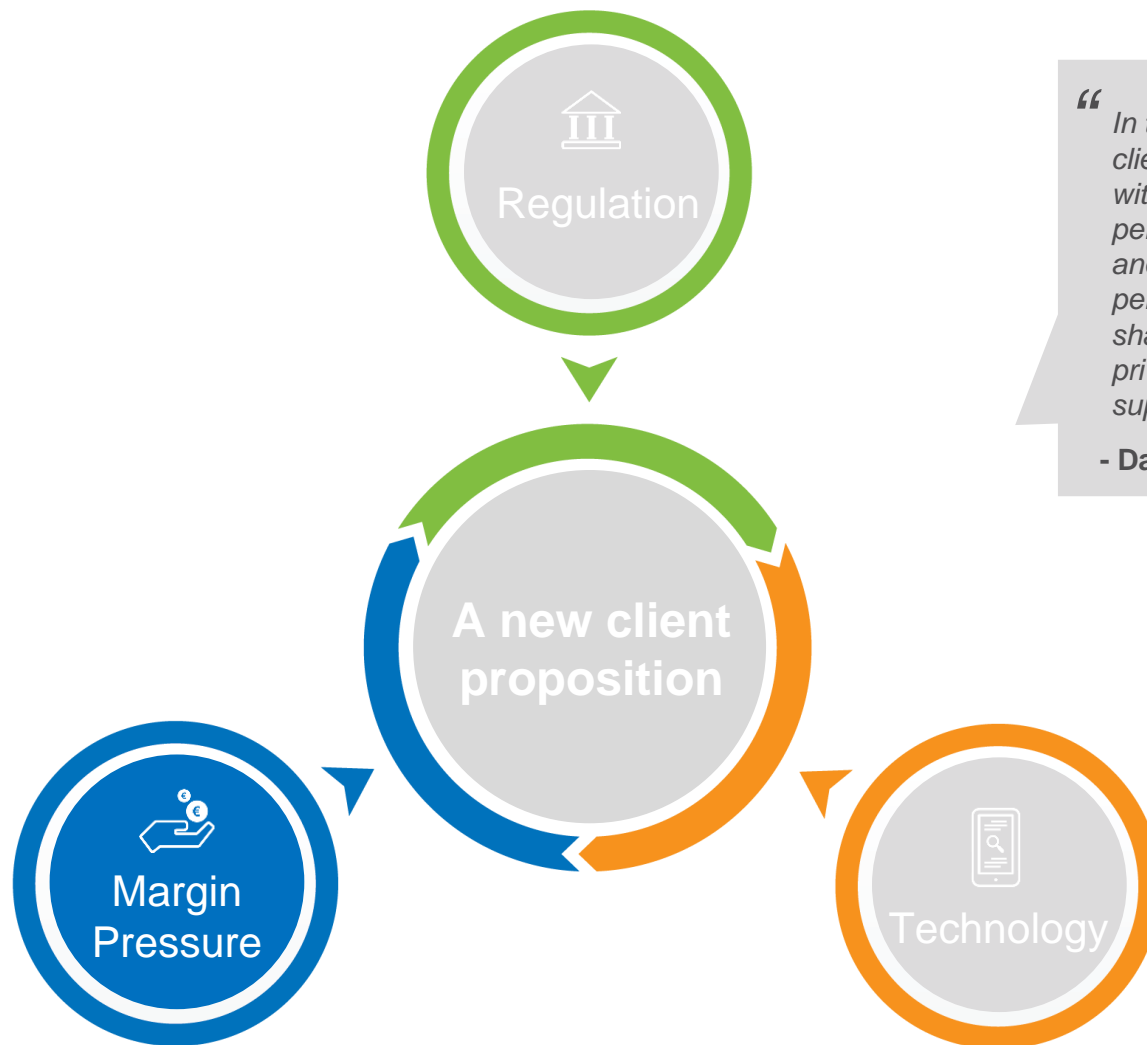
# Digital improves the experience for both the client and the advisor

Advisors who integrated technology into their practice saw:



Source: \*Fidelity, 2016. +McKinsey, 2016

## Three forces are disrupting the value chain



“ In the long term we cannot offer clients services, such as DPM, with a total ownership of 1.5 percent a year: that is too high and it will probably move to 1 percent. This 1 percent will be shared by asset managers, private banks, and other suppliers of services in the chain. ”

- Danske

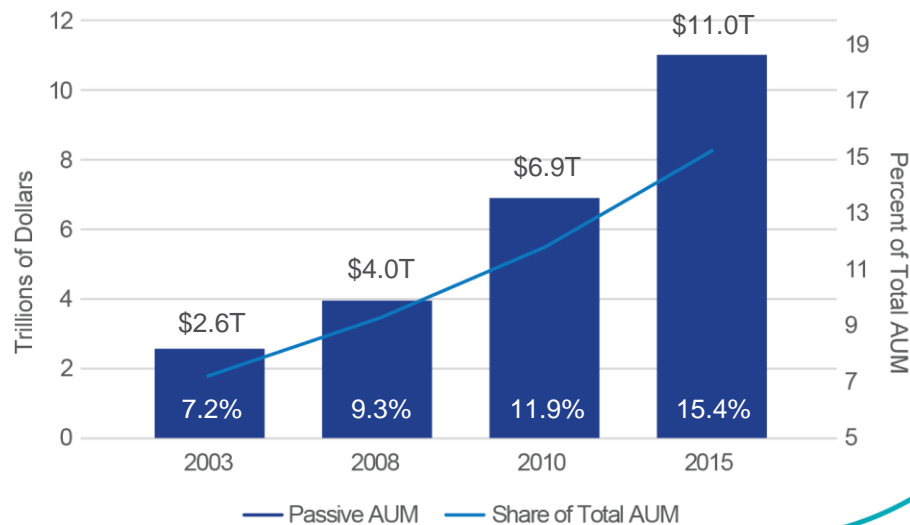
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# Index Investing Goes Mainstream

As technology and data improves, so does our ability to precisely capture and replicate exposures that allow access to a broader range of investment outcomes

## The growth of Passive

Growth in Passive AUM &  
Passive as Percent of Total Industry AUM



### Fixed Income

- >\$500B inflows in last 5 years
- Applications and user base expanding from deep retail through to Credit HFs and asset owners

### Smart Beta

- In 2016, \$1 in every \$3 invested into UCITS Equity ETFs was in smart beta
- Factor implementation becoming mainstream in portfolios

### Megatrends and Thematics

- >\$1.5B invested in Robotics and Automation ETFs (\$0 in 2012)
- New index innovation allows investors to capture economic impact of long-term trends (i.e. robotics, ageing populations, etc.)

### ESG and Impact

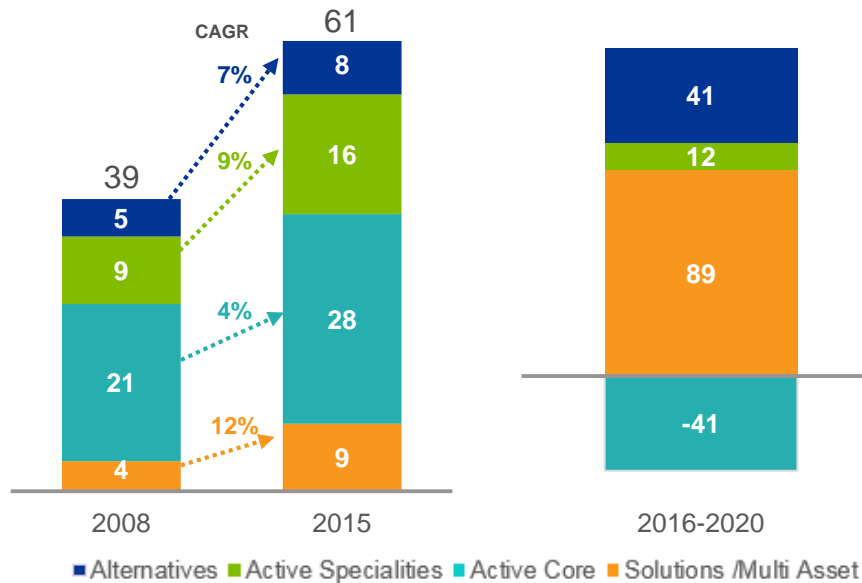
- Sustainable Investing ETFs >\$9B in 2016, up from \$3.3B in 2012
- From “nice to have” to an essential requirement of many investors across markets

Source: AUM Chart: Citi Business Advisory Services estimates based on Global Asset Management 2016: Doubling Down on Data, The Boston Consulting Group, Dic 2016

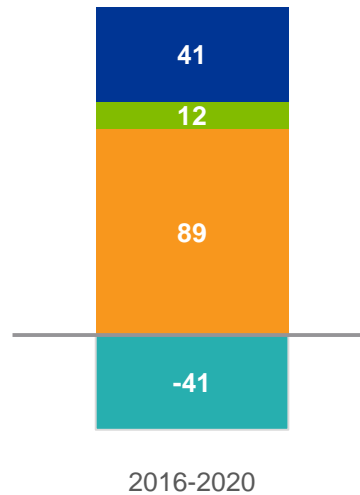
Source: Flows: Citi Business Advisory Services based on data from eVestment, Preqin, HFR, Strategic Insight, BlackRock ETP report, IMA, OECD, Towers Watson, P&I Lipper, Dic 2016

# The new Active opportunity

Global Active AUM, by product type, \$T



Estimated share of active net flows %



## Alternatives

- Global assets quadrupled from 2003-2015 (\$2T to \$8T)
- Hedge funds remain a key component of the universe, private asset classes are growing in prominence and Retail clients maintain strong appetite for UCITS alts

## Active Specialties

- Growth rate significantly faster than Active Core (2008-2015 CAGR 9% vs. 4%)
- Proven demand for alpha generation and exposures that are difficult to replicate
- Renewed desire to build satellites with high conviction strategies

## Solutions / Multi Asset

- In Developed Markets sub-advised AUM grew 17% pa since 2010
- Solutions on the rise, especially given high penetration rates in mass affluent and HNWI

## Active Core

- Challenged by ETF and index offering
- Forecast to account for -41% of global active asset management flows between 2016-2020
- Next innovation frontier in low cost / low tracking error, catalysed by technology

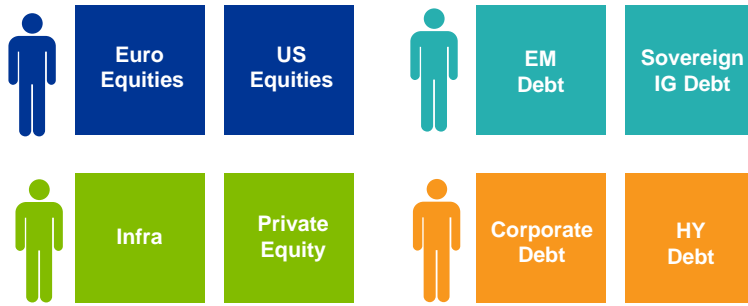
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# Moving from individual exposures to solutions

Putting the needs of the investor first is becoming mainstream

From a focus on single products and performance.. ..to a solution based on outcomes and goals



Illustrative purposes only

## Factors driving solutions adoption

1

From performance to outcome and goals

2

More scalable approach to client segments

3

Greater ability to explain outcomes to clients

4

Value for money

Source: BlackRock as of June 2016 For illustrative purposes only

## Three forces are disrupting the value chain



“ A quality counterpart [must] be able to share information, share risk knowledge, work in a value chain to provide a consumer product and to do that in an open, transparent, fiduciary way at the right price ”

- Embark

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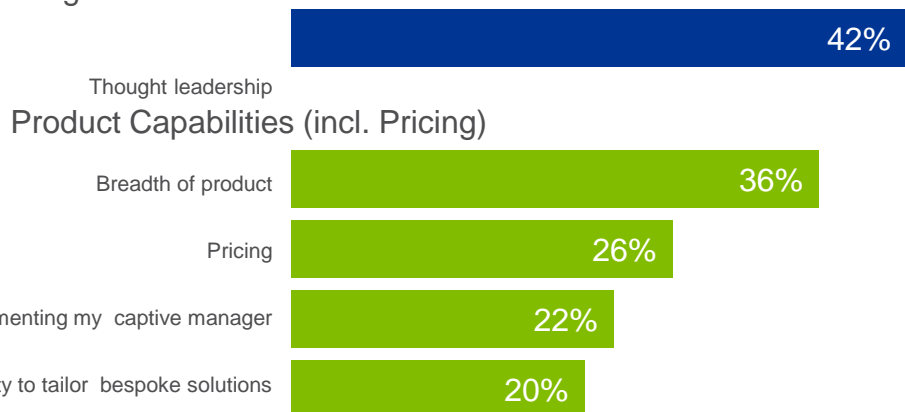
# Partnership Model: Wealth managers are asking for more from fewer asset manager partners

A new client Proposition

## Important attributes when partnering with Asset Managers

% respondents (select up to 3 categories out of a total of 11)

### Insights



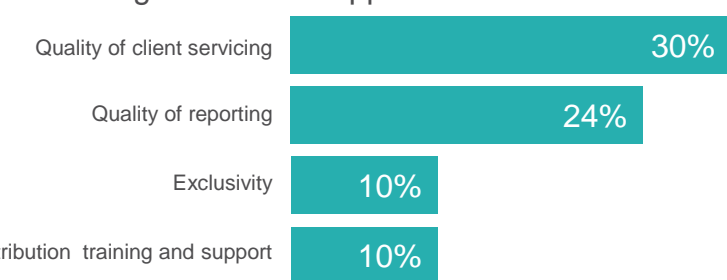
“Service providers differentiate themselves by understanding our business model, taking time to build the relationships with the people within our organization – by listening. Product will be the end result of a deep knowledge of an organization.”

- Citi Private Bank

“I expect a quality counterpart to be able to share information; share risk knowledge; work in a value chain to provide a consumer product; and to do that in an open, transparent, fiduciary way at the right price....The real shame is that the vast majority don't think like that and, even when they do, they can't deliver it.”

- Embark

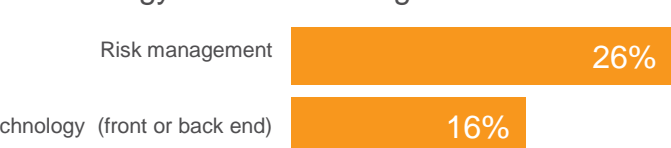
### Marketing and Sales Support



“I need vendors who try to understand my situation before they try to sell in. And that's where the '**partnering**' word is very important, that we could develop stuff together, and **grow stronger together.**”

- Danske

### Technology and Risk Management



“Performance matters, pricing matters, reputation matters, quality of managers matters. Increasingly, it's the service proposition and **the ability for the managers we work with to be aligned** in terms of what we're delivering and how we're delivering solutions to our clients.”

- Citi Consumer Bank

Source: Blackrock Wealth Management Industry Survey 2017

# A lot of ongoing industry changes are discussed... but these trends aren't new

What we've learned from regulation shifting our global clients to maintain higher fiduciary standards

Early adapters gain  
advantage

Shift from products  
to portfolios

Tech promises to fill  
the advice gap

Tremendous fee  
pressure surfaces



For illustrative purposes only



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