THE CASE FOR CHANGE

Toward a New Frontier in Team Productivity

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A LETTER FROM SEI

Change is inevitable. It is happening in every industry at unprecedented rates. Those that embrace change are disrupting their industries before the hesitant can even utter the words "too risky". Uber. Amazon. Starbucks. Their names conjure thoughts of innovation, disruption, and sustainable growth. These are companies that didn't focus on widgets or feature/function to get ahead. They took a close look at their business model and re-invented the entire value chain. They did this with customer experience and convenience at the center of their strategy, and they built a business model that blended vision with operational integration and capital allocation. They embraced disruption and used it as a chance to reinvent their industries, their businesses and their associated profitability. The result didn't just drive unprecedented change, but also unprecedented growth.

And now it's time for the wealth management industry to do the same.

Wealth management used to be simpler, but regulation, globalization and increasingly demanding customer expectations are pressurizing this business like never before. Cracks are appearing. Infrastructures have become more and more complex. In order to keep pace, firms have added plug and play solutions to legacy infrastructure. Bolted on technology has created a mess of disparate systems causing a seismic increase in vendor oversight, due diligence and operational nightmares. It has put a serious strain on risk management, as disconnected technology is error prone and ultimately leads to a disconnected client experience. Right now the cracks are growing and without radical transformation, wealth management "cracks" can quickly turn into wealth management "breakdowns".

And at the heart of any wealth management business is the advisor. The advisor should be focused on understanding their customers' life goals, building and sustaining their wealth and proving advisor value through differentiated service. Instead, they are impaired by administrative tasks, have clunky, disconnected workflows and are far less productive than they could be, largely because their organizations are choosing feature/function over enabling customer connection. Too often technology is judged on discrete bells and whistles, not efficiency and effectiveness of the value chain. The portfolio manager has what he or she wants, the operation has what they want, but it is all at the expense of a seamless customer experience. Did that bell or whistle actually create value for the client or, more to the point, value the client cared about? It's time to repair this value chain and the associated wealth management profitability.

Wealth management reinvention is possible, but there is no silver bullet. It is a journey. It starts with re-examining your profitability structure. You need to re-think your value proposition with a focus on the client experience. But have you considered what it takes to deliver that value? Have you done a thorough analysis on how you are organized, how technology enables and integrates operations and the capital required to execute that value proposition? Have you thought systemically from the client back, and not from the discrete functions out?

At SEI, we believe it is time for wealth managers to take a lesson from Uber, Amazon and Starbucks. It's time for wealth managers to do an honest assessment of their entire value chain and reinvent their profitability structure. Where are you spending money today? You need a flexible business model that can respond to the changing needs of the market and increasing pressures on cost. You need to be open to automation and partnership.

There is a paradigm shift underway in wealth management and day-to-day tactics need to support long-term strategic vision. We are so proud to partner with leading research provider, WISE Gateway. Their research will take a closer look at the pressures facing wealth managers today and more deeply examine the relationship between customer value, growth and profitability. What separates visionary leaders in wealth management from those allowing themselves to be disrupted? We believe it's two things: a vision and a commitment to change.

We truly thank WISE for allowing SEI to be a part of this study. Their insights are compelling – the case for change isn't coming. The case for change is here.

Al Chiaradonna
Senior Vice President, SEI Private Banking

SEI New ways. New answers.®

METHODOLOGY

Research Participants and Data

The information in this research is from bank wealth managers and trust organizations that serve high net worth individuals. Participants run the gamut in terms of size and geography.

Data about these firms are principally drawn from three sources:

- **A paper-based survey of bank and trust company financials**
  In the summer of 2015, approximately 75 firms provided data about their wealth management operations, including revenue, expense, productivity, and related information.
- **A Web-based survey of bank and trust company operations**
  In the summer and early fall of 2015, approximately 40 firms provided data about their service processes and teams.
- **Qualitative research interviews**
  In fall 2015 WISE staff conducted numerous research interviews with industry executives about their efforts to improve productivity and efficiency.

Segment Definitions

This research looks at business performance from three perspectives: wealth management (all services), investment management and trust services only, and private banking services only. The primary focus of this research is high net worth individuals. Where possible, data pertaining to mass affluent and institutional clients have been excluded.

In detail:

- **Wealth Management**
  Data that are labeled Wealth Management describe businesses that provide a wide array of products and services to high net worth consumers, including investment management, trust, credit, and deposit services. These data are typically from larger, diversified financial services firms that have highly integrated operations.
- **Investment Management and Trust**
  Investment Management and Trust refers to trust, fiduciary, and investment services provided to high net worth individuals, including services such as personal trust, investment management, irrevocable and revocable trusts, individual retirement accounts, etc.
- **Private Banking**
  Private Banking data pertain to the business of providing credit and deposit services to high net worth individuals, as well as to the employees that manage related accounts and relationships. "Private Banking", therefore, is primarily a product or line of business distinction; it is not a client wealth segment distinction.

In a few instances, where data are drawn from the Web survey on operations, the following segments are also used:

- **Small Firm**: Assets under management (AUM) of $5 billion or less
- **Mid-Size Firm**: Assets under management between $5 billion and $10 billion
- **Large Firm**: Assets under management of $10 billion or more

The Case for Change

At a time when client service preferences are evolving and their financials are challenged, firms need to do more to improve productivity and to support their client-facing teams.

EXECUTIVE SUMMARY

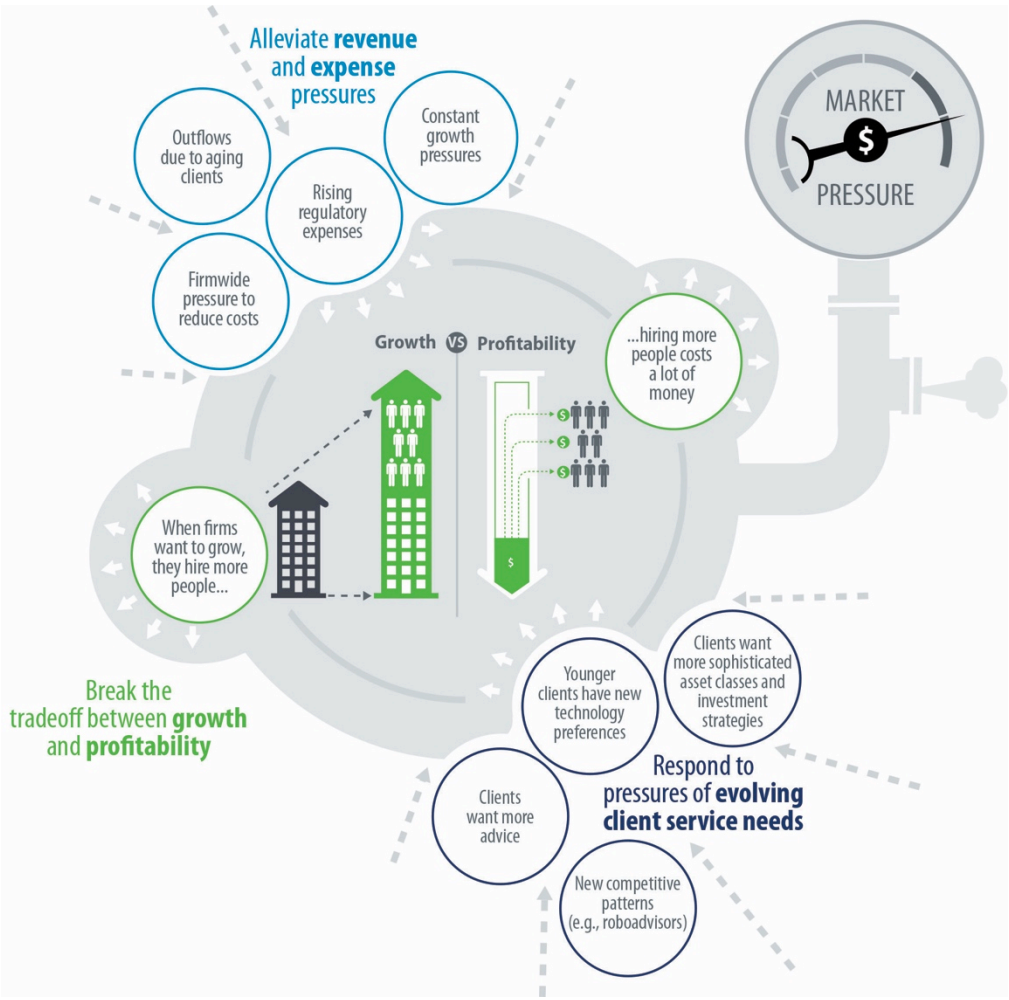
Are you ready? Wealth managers must respond to emerging trends and familiar challenges.

Wealth managers are under pressure. For starters, firms must keep pace with evolving client expectations, including demands for advice and for access to more sophisticated asset classes and investment strategies. Service models are also flexing to accommodate the technology and delivery preferences of younger consumers, and to respond to the emergence of roboadvisors. On balance, these changes are probably good news. For clients, service model shifts are likely to bring better service outcomes. For wealth managers, they open the door to deeper, stickier client relationships. Implementation, however, places new demands on firms, their teams, and their profits.

The timing of service model changes is inopportune, as firms are under significant financial pressure. Revenues are adversely impacted by a challenging investment environment and by asset outflows from aging clients. Demands from senior management for growth are ever-present, yet firms are loath to spend; hiring new advisors and sales officers to spur growth is unpalatable. In the near-term, firms need to keep a close eye on spending to compensate for reduced banking spreads, escalating regulatory costs, and economic uncertainty. Operationally, firms must contend with longstanding tradeoffs between growth and profitability. In simple terms, growth is expensive: firms can have high growth rates or high margins but rarely both. Achieving sustainable topline growth seems to require continuous investment in people and other resources.

In many respects, today's manager's mandate almost seems unfair. It's to do more—improve the service and grow—while not spending a lot of money. And in some cases, it's to do more with less.

WEALTH MANAGERS UNDER PRESSURE



We believe that firms should undertake a wholesale review of the processes and infrastructure that support their client-facing advisors.

Ultimately, firms need to design flexible business models capable of responding to the ever-changing realities of the market.

THE CASE FOR CHANGE

Under pressure, the 'release valve' is to improve productivity—and especially advisor productivity.

At a time when client service preferences are evolving, when firms' financials are under pressure, and in the midst of demographic shifts, the client advisor is becoming even more critical to the client service experience and to financial success.

Our view, therefore, is that firms need to do more—significantly more—to support their advisors and to improve the productivity of their client-facing teams. Attracting top talent is paramount, yet providing that talent with adequate support and infrastructure often falls by the wayside. Saddling talented, high-cost employees with administrative work and old technology exacerbates longstanding tensions between growth (which is expensive) and profitability. Our recommendation is that firms undertake a wholesale review of the processes and infrastructure that support their client-facing advisors. Ultimately, firms need to design flexible business models capable of responding to the ever-changing realities of the market.

The case for change is compelling:

Client advisors are often burdened with low-value tasks and constrained by inefficiency.

Profitable firms are those that deploy their key people most effectively. That's both truism and empirical fact: productivity and profitability are highly correlated. Nonetheless, it is an open secret that advisors are encumbered with administrative work, manual processes, and inadequate technology. Given the margin implications, the case for investing in productivity is strong; buffeted by a variety of new and familiar pressures, the need for firms to act is stronger still.

Advisors will be tasked with delivering the new and improved client service experience.

As the liaison between client and institution, between important life goals and the means to achieve them, the client advisor has always been integral to the service experience. As service models more commonly feature advice at the core, the advisor's role becomes even more critical. Navigating a successful shift will require giving advisors additional capacity for high-value client servicing activities.

By empowering their advisors to drive growth, firms can alleviate revenue and expense pressures.

In a world of limited budgets and hiring constraints, adding more people to fuel growth isn't an option. Longer-term, age and retirement will drain the talent pool. Even today, searches for sales officers and other key positions can drag on for months at a time, if not longer. Increased efficiency, therefore, is the best of a limited set of options; firms need to find ways to give their existing advisors more time for sales.

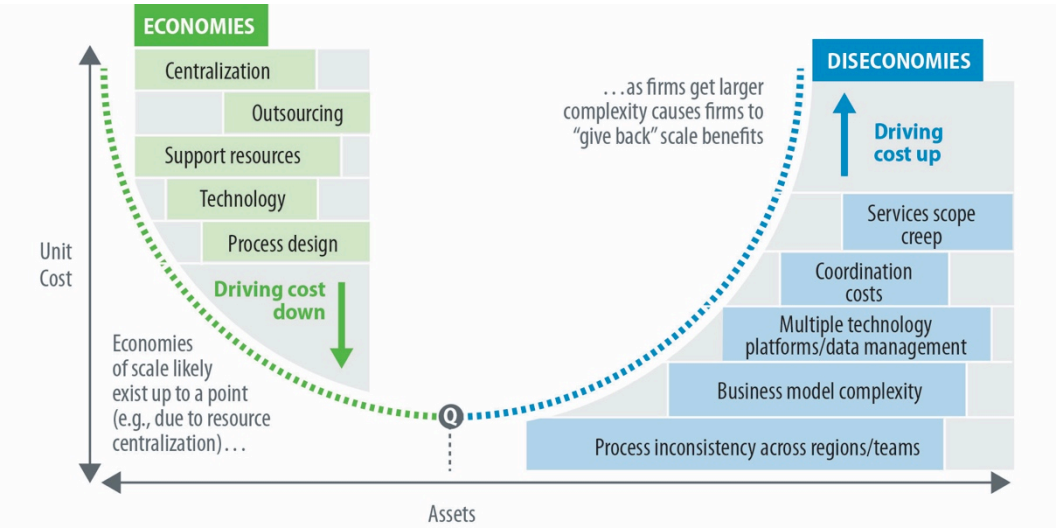
Productivity improvements can weaken the tension between growth and profitability.

Growth in wealth management is expensive; revenues and expenses are very strongly correlated. There's evidence, however, of at least modest economies of scale, especially as firms grow from small to mid-size. There's also evidence of diseconomies of scale, especially among large and super-sized wealth managers.

Our view is that productivity (or lack thereof) underlies evidence of economies and diseconomies of scale. As firms climb the scale curve, centralized and specialized labor, as well as investments in technology, reduce per unit costs (e.g., managing an extra dollar of AUM gets cheaper). In other words, growth becomes a little less expensive. Past a certain size threshold, however, escalating business model complexity causes firms to "give back" scale benefits. Complexity arises from myriad causes, ranging from business acquisitions to incompatible technology platforms, to rising coordination costs.

One implication is that firms need to heavily leverage resources that drive productivity. Support resources such as administrative support and outsourcing partners have a quantifiable, positive impact on productivity. A second is that firms need to assiduously root out productivity-destroying complexity by streamlining sales and service processes, striving for process consistency across teams, and improving technology connectivity.

SIGNS OF ECONOMIES AND DISECONOMIES



FIVE THINGS FIRMS NEED TO DO TODAY

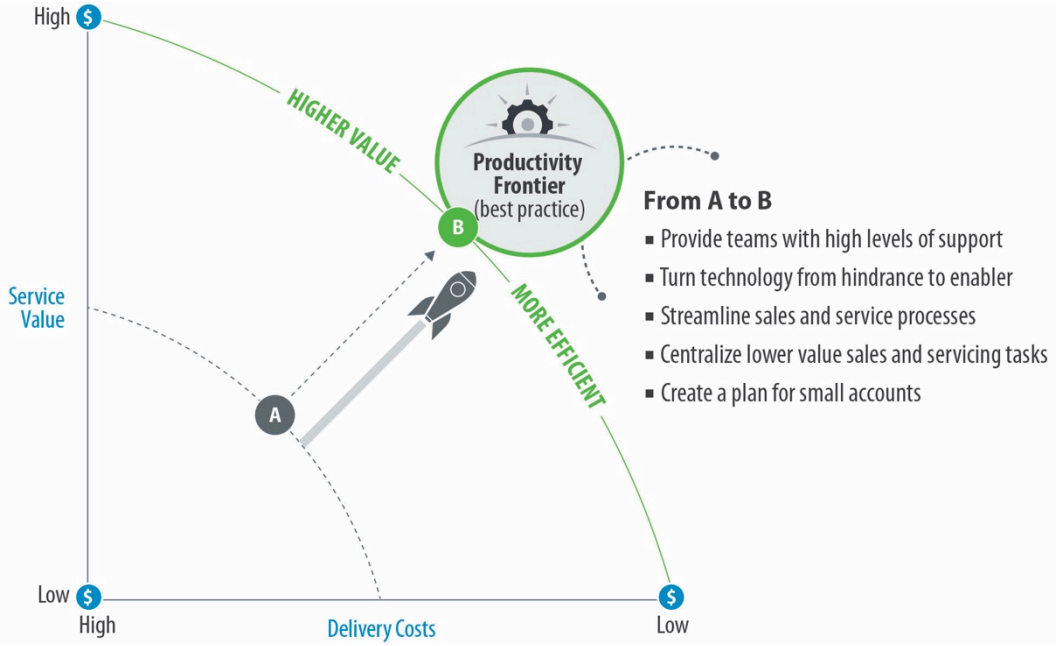
For many firms, significant productivity gains are well within reach.

Even adjusting for business model differences, some wealth managers are much more efficient than their peers. Within size-based cohorts, for example, we observe a lot of variance in the productivity of client advisors, as well as in all employees. We observe similar variability in the performance of client-facing teams.

Productivity differences have a host of tactical explanations: the ease with which teams coordinate; the extent to which key sales and service processes are standardized and streamlined; the number of manual processes and amount of administrative work; the way in which firms support advisors with teams and support resources. Most of these activities are enhanced by effective technology deployment, which is likely one of the biggest differentiators in the performance of client-facing teams.

The benefits that accrue to productive firms aren't just financial, they also impact the client service experience. For example, by enabling proactive servicing and by minimizing errors, firms can increase service value. Our research reimagines these dual benefits as dimensions of a Productivity Frontier, and proposes five steps for attaining a new, higher frontier.

THE PRODUCTIVITY FRONTIER



OUR RESEARCH REIMAGINES THE FINANCIAL AND SERVICING BENEFITS AS DIMENSIONS OF A PRODUCTIVITY FRONTIER, and proposes five steps for attaining a higher frontier.

1. Provide client-facing teams with higher levels of support and better infrastructure.

Our analysis of common service team models finds examples of exemplary performance in each. Our research found no evidence that a particular service team structure was demonstrably better at improving productivity than another. Looking at performance variations *within* categories of service team models, however, hints at the characteristics of profitable firms and productive teams:

- Firms with proportionately fewer client-facing employees and proportionately more support staff tend to have better financial outcomes. These firms are offloading administrative and lower-value tasks to less expensive employees—and incentivizing client-facing staff to use freed time for servicing and sales.
- Productive teams serve larger client relationships and account sizes. Large account sizes, high share of wallet and profitability go together—building teams that can deliver deep and broad relationships drives profitability.
- Larger teams, broader service offers, and team-based sales go together; firms desiring deeper, advice-based relationships with clients need to develop competencies in team sales and cultivate good sales talent.

2. Turn technology from hindrance to enabler.

As it relates to technology, the industry divides into two camps: invest and invest not. The latter category includes those that have old technology, lots of workaround solutions, and manual processes. It is likely that the "invest nots" are essentially pushing the costs of old technology to their service teams or elsewhere in their business models. Frustrations relating to the lack of interconnectivity between platforms are particularly palpable. In the "invest" camp, firms with newer technology are doing the exact opposite: displacing labor costs by automating formerly manual processes.

3. Streamline sales and service processes.

By developing more consistent sales and service approaches, firms are improving both the client service experience as well as staff productivity. Through process redesign and by leveraging technology, these initiatives share the goals of consistent execution across teams, promotion of 'best practice' sales and servicing strategies, error and risk reduction, and elimination of redundancies.

4. Centralize lower value sales and servicing tasks.

As firms get larger, their employees generally get more productive, and task centralization and role specialization are key reasons why. If the quintessential small firm advisor does a bit of everything, as firms grow, administrative tasks, small accounts, labor-intensive processes, and specialty expertise are commonly centralized in support resources. These support resources—from administrative assistants, to client service officers, to outsourcing partners—are almost always lower-cost and can pay big productivity dividends.

5. Create a plan for managing small accounts and single-service relationships.

Rivaling old technology, small accounts and single-service relationships are arguably one of the biggest drains on front office productivity. Conversely, larger accounts and larger relationships generally have salutary effects. For most firms, a "small account" solution begins by differentiating the always-small, productivity-sapping relationships from those with future growth potential. From a sales perspective, a way to grow these relationships via more disciplined pricing and cross-sales is a must. Further, from a servicing perspective, firms must strive to serve small accounts with lower-cost labor or, better, to develop standardized and automated service approaches.

Staying still is a decision—and it's a poor one.

Many firms will choose to stay the course in 2016: to maintain tight control of expenses and to hope that an improving economy, financial markets or business liquidity will fuel revenue growth.

Even setting aside recent declines in the equity markets, the status quo has significant limitations. At the very least, firms need to find a way to offset the rising costs of regulatory, technology, and service demands. Cutting other costs is an unlikely solve, as most are already working off of lean cost structures. Alleviating expense pressures, therefore, will require growth, but growth net of market effects has been difficult to come by. Unfortunately, the traditional model of growth—hire more advisors—is both costly and likely to become more so.

The Case for Change

- Minimize widespread inefficiencies
- Respond to evolving client service needs
- Alleviate revenue and expense pressures
- Weaken the tension between growth and profitability

For reasons both new and familiar, our view is that most firms need to prioritize improving the productivity of their client-facing teams.

A compelling case can be made for investing in support resources, process improvements, and infrastructure.

THE CASE FOR IMPROVING PRODUCTIVITY

Client advisors disproportionately impact both the client service experience and firms' financial outcomes, yet advisors are saddled with administrative work, imperfect technology solutions, and inefficient sales and service processes. One key culprit: investment dollars tend to favor hiring new people over enhancing the productivity of existing teams. Whereas hiring a new relationship manager has an obvious impact on sales and service capacity, the benefits of productivity investments—increased sales capacity, happier clients, fewer errors, and reduced risk—are less easily measured.

> **Everybody** wants to spend money on adding advisors, yet **nobody** wants to spend money on operations. It's a long-term money saver but trying to convince people to invest is hard. People think that more headcount will solve their problems.
>
> PRESIDENT AND CEO, PRIVATE TRUST COMPANY

For reasons both new and familiar, our view is that most firms need to prioritize improving the productivity of their existing client-facing teams. Aside from the obvious—productivity and profitability go hand-in-hand—a compelling case for investing in support resources, process improvements, and infrastructure has three main components:

Evolving Client Service Needs
Firms need their advisors to help implement new service approaches, respond to changing client needs, and deliver superlative client service.

+

Revenue & Expense Pressures
Alleviating revenue and expense pressures requires growth; freeing up sales capacity in client-facing teams is a must-do.

+

Growth & Profitability Tradeoffs
Lessening the tension between growth and profitability requires greater efficiency from client-facing teams.

We first assess the status quo, then explore each in detail.

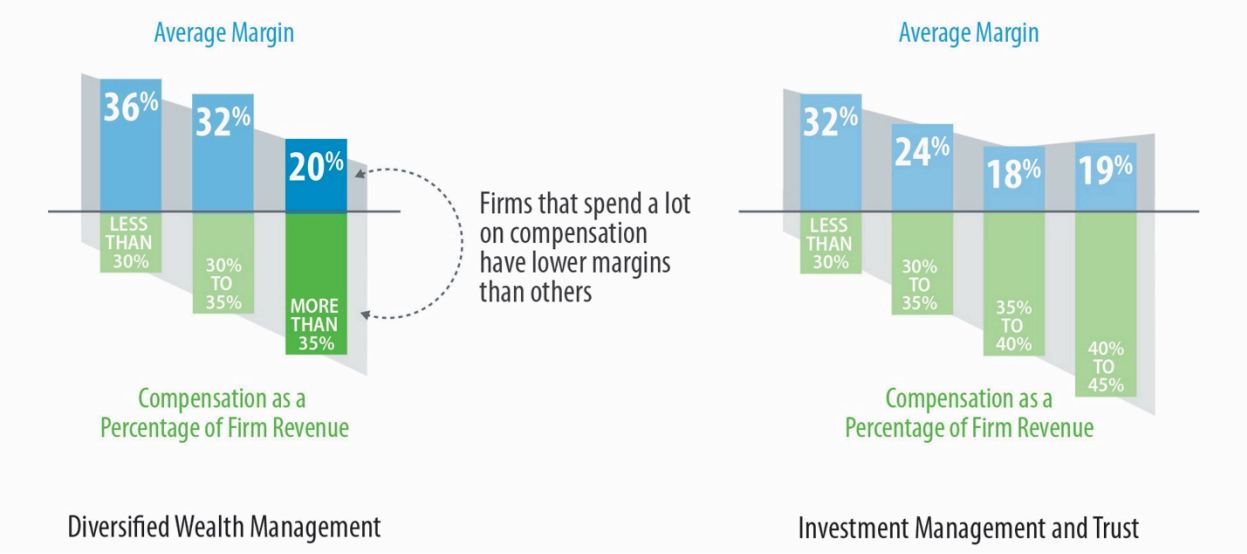
Productivity and profitability go hand-in-hand...

…yet nearly one-third of firms use a core accounting platform that is older than the first iPhone, and advisors spend almost 40% of their time on administrative work.

THE STATUS QUO: BURDENED BY INEFFICIENCY

In terms of both the client experience and profitability, it's hard to overstate the importance of sales and service personnel. Firms with the most productive employees usually have the best financial outcomes. Fundamental measures of staff productivity, such as compensation as a percentage of revenue and net income per full-time employee, are strongly correlated with operating margin. In our sample of diversified wealth managers, as well as in our sample of investment management and trust businesses, firms that spent less than $0.30 of each revenue dollar on compensation were, as a group, considerably more profitable than all other firms.

PRE-TAX OPERATING MARGIN, BY COMPENSATION AS A % OF REVENUE

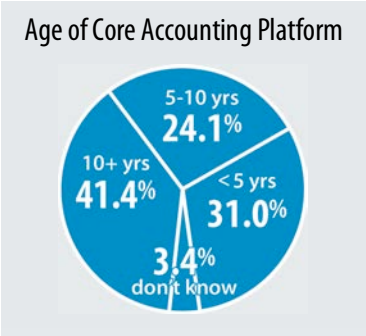


IN OUR SAMPLE, FIRMS THAT SPENT LESS THAN $0.30 OF EACH REVENUE DOLLAR ON COMPENSATION WERE, as a group, considerably more profitable than others.

Given the financial implications, it is surprising to find that advisors at many firms are weighed down by aging infrastructure, administrative work, and manual processes.

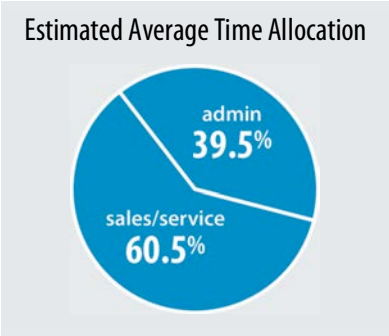
Aging Infrastructure

The industry's technology issues run the gamut from old technology to lack of connectivity between technology platforms to poor data management. Lack of spending is a key contributor to technology issues. Firms' direct expenses—what they spend on their core sales and service operations—have barely budged over the past four years (or more) and many firms spend relatively little on technology. Underinvestment means that industry technology platforms are often very old. The core accounting platform at nearly 25% of firms is 5-10 years old; another 40% are using a core accounting platform from 2005 or earlier. (For perspective, Apple released the first iPhone in mid-2007).



Process Inefficiencies

Process inefficiencies have numerous causes and old technology is certainly one. It is commonly the case that incompatible platforms—such as a firm's CRM and trust systems—require manual and often redundant data entry or other workarounds. Growth via acquisition is another source of inefficiency. Business combinations saddle firms with multiple systems, as well as inconsistent ways of servicing clients and selling to prospects.



Unsurprisingly, advisors are saddled with low-value administrative work. Managers estimate that about 40% of their advisors' time is consumed by administrative tasks (ranging from about 30 to 50 percent). Some amount of administrative work, of course, is unavoidable. However, industry veterans estimate that current levels are about twice what is necessary. In other words, they estimate that through greater efficiency firms can free up an additional 1.5 hours of time per day per advisor.

Manual Processes

Our view is that the cost of legacy technology and inefficiency is felt most acutely in the front office. Although many firms have invested in upgrading their back office processes or in establishing a middle office, many critical front office sales and service processes are still performed manually.

On a seven-point scale, where seven represents full automation, few managers describe sales and service processes as very automated. On average, not a single process garners a top three score (i.e., a 5, 6, or 7 score indicating "highly automated"). Services that are highly visible to a prospect or a client are also the most manual, including sales proposals, new client enrollment, client meetings and client reporting.

SALES & SERVICE ACTIVITIES BY DEGREE OF AUTOMATION

SEVEN POINT SCALE WHERE 1 = COMPLETELY MANUAL AND 7 = COMPLETELY AUTOMATED | ■ = HIGHLY VISIBLE PROCESSES

3.1 Sales proposal generation
3.1 New client enrollment
3.8 Client meeting preparation & reports
4.2 Investment policy statement generation
4.6 Investment compliance
4.7 Portfolio rebalancing
4.8 Administrative & investment reviews

On a seven-point scale, where seven represents full automation, few managers describe their processes as very automated.

On average, not a single one garners a top three score.

LEAST AUTOMATED	Small Firms	Mid-Size Firms	Large Firms
1	Sales proposal generation	Sales proposal generation	New client enrollment
2	New client enrollment	New client enrollment	Sales proposal generation
3	Client meeting preparation & reports	Investment policy statement generation	Client meeting preparation & reports
4	Investment compliance	Portfolio rebalancing	Investment policy statement generation
5	Investment policy statement generation	Client meeting preparation & reports	Administrative & investment reviews
6	Portfolio rebalancing	Administrative & investment reviews	Investment compliance
7	Administrative & investment reviews	Investment compliance	Portfolio rebalancing
MOST AUTOMATED			

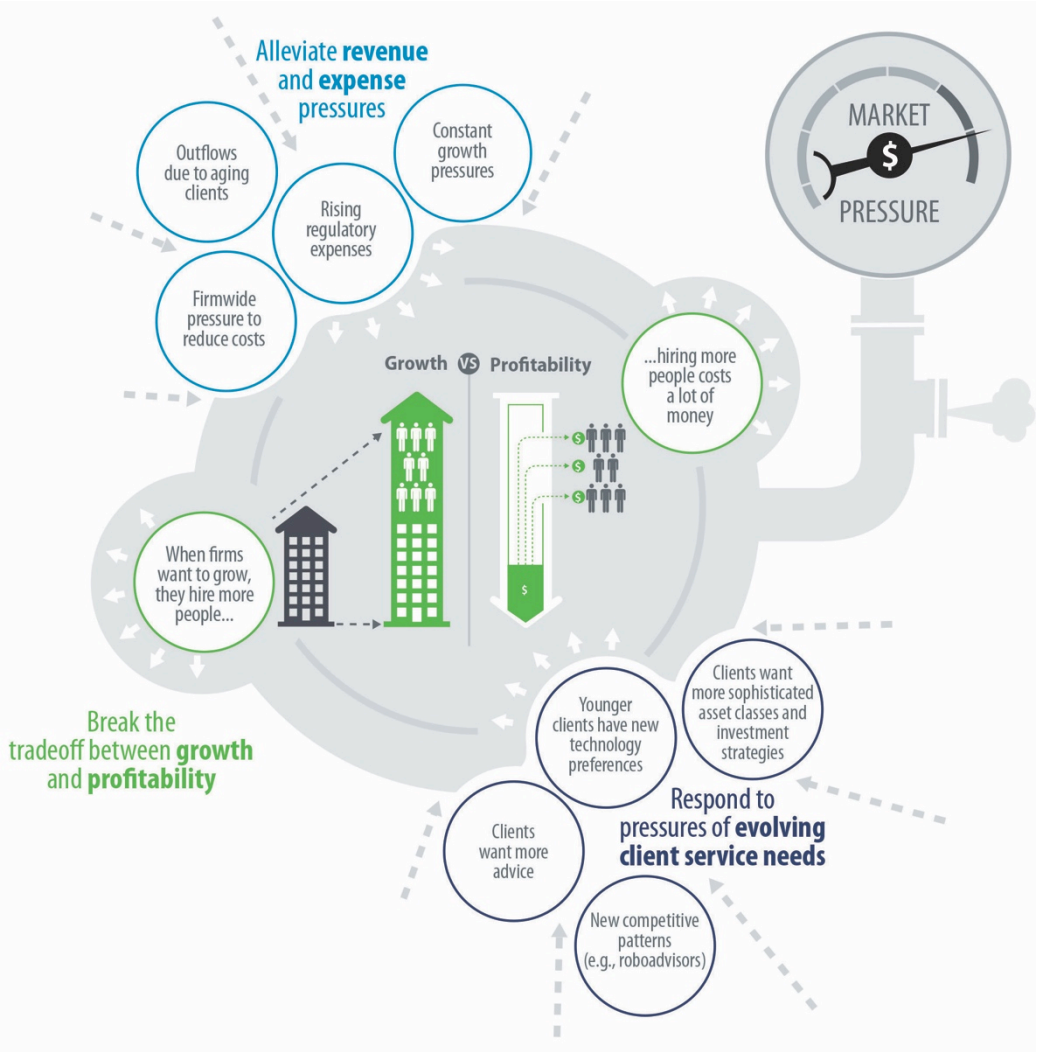
THE RANKING OF VARIOUS PROCESSES IN TERMS OF AUTOMATION IS ABOUT THE SAME FOR FIRMS OF ALL SIZES: smaller firms tend to have less automated processes across the board.

Industry service models are evolving in ways that are likely to create a better service experience for clients.

Navigating a successful shift will require giving client advisors time for higher-value servicing activities, as well as new sales and service processes.

Given the importance of the advisor, defending the status quo is difficult enough. If anything, however, the advisor's role is becoming even more critical to a firms' success. Firms are buffeted by a variety of pressures: from the market and their clients, to competitors and their managers. Increasing sales and service capacity by improving the productivity of client advisors is arguably the only lever that provides relief from each.

WEALTH MANAGERS UNDER PRESSURE



An environment that demands effective expense management and desires organic (non-market) growth is one that rewards efficiency and productive teams.

RESPOND TO EVOLVING CLIENT SERVICE NEEDS

Industry service models are evolving in ways that are likely to create a better service experience for clients. The biggest change, of course, is the continued expansion of advice-led service models. In addition, firms are exploring ways to deliver more sophisticated investment strategies and to satisfy the technology and delivery preference of both younger consumers and younger advisors.

For wealth managers, service model changes offer both retention and growth benefits. In ultra-wealthy segments, where advice-led offers are more common, advice leads to stickier relationships and amplifies the benefits of annuity economics. In terms of growth, advice opens the door to broader service relationships. For example, whereas most firms have found ways to grow their investment advisory revenues over the past few years, faster growers are growing the personal trust business, or tapping new opportunities in business advisory, oil and gas, insurance, or charitable giving. In short, they are growing from both breadth and depth.

Service model changes portend good things for both clients and their advisors, but they also bring transition costs. In particular, they place new demands on client-facing teams who have to contend with greater complexity and higher coordination costs, such as a greater need for team-based sales. Navigating a successful shift will require giving client advisors time for higher-value servicing activities, as well as new sales and service processes.

EVOLVING SERVICE PREFERENCES & MODELS

- Delivering on the promise of holistic advice
- Providing clients access to UHNW or institutional-caliber investment strategies and asset classes
- Meeting the service and delivery expectations of tech-savvy Millennials and younger clients (e.g., digital, mobile technology)
- Hiring or training the next generation of advisors
- Developing new service models for the emerging affluent (e.g., roboadvisors)

Source: Deloitte Consulting; WISE Research

ALLEVIATE REVENUE AND EXPENSE PRESSURES

Despite working off of lean costs bases, managers are likely to face continued pressure to reduce (or at least maintain) their expenses. At the same time, challenging financial markets and demographics are creating growth headwinds.

Productivity improvements may not fully break the tradeoff between growth and profitability, but they can chart a path towards more efficient growth at a time when one is sorely needed.

Rising Expenses

On the expense side, firms can expect continued increases in regulatory and compliance costs. For many, aging technology platforms require an upgrade and for most, keeping pace with the demands of the Millennial generation will prompt new spending on digital, mobile, and other forms of remote delivery. Wealth managers that are part of larger financial services firms (especially banks) are being asked by senior management to do more with less. Given profit pressures from reduced spreads across the banking industry, wealth managers are being held more accountable for managing expenses while also delivering higher growth rates.

Revenue Pressures

There are ample reasons to believe that growth may be hard to come by. The same demographic trends that are pushing younger consumers' preferences to the forefront also have critical revenue implications. Firms with older clients and large, legacy personal trust businesses are reporting an increase in the "ATM effect" of distributions and death—outflows are likely to have a meaningful impact on growth rates. An aging advisor workforce, meanwhile, will make the tried-and-true strategy of growth via hiring more challenging; business development officers, for example, already seem to be in short supply. Weakness in the financial markets rounds out a daunting list of reasons why near-term growth rates may be atypically low.

An environment that demands both effective expense management and also organic (non-market) growth is one that rewards efficiency and productive teams.

MAJOR FINANCIAL PRESSURES

- Regulatory costs
- New client service demands
- Executive mandates to cut costs and grow in order to compensate for underperformance in non-wealth businesses
- A challenging market environment
- Asset outflows from aging clients and distributions
- Reduced banking spreads

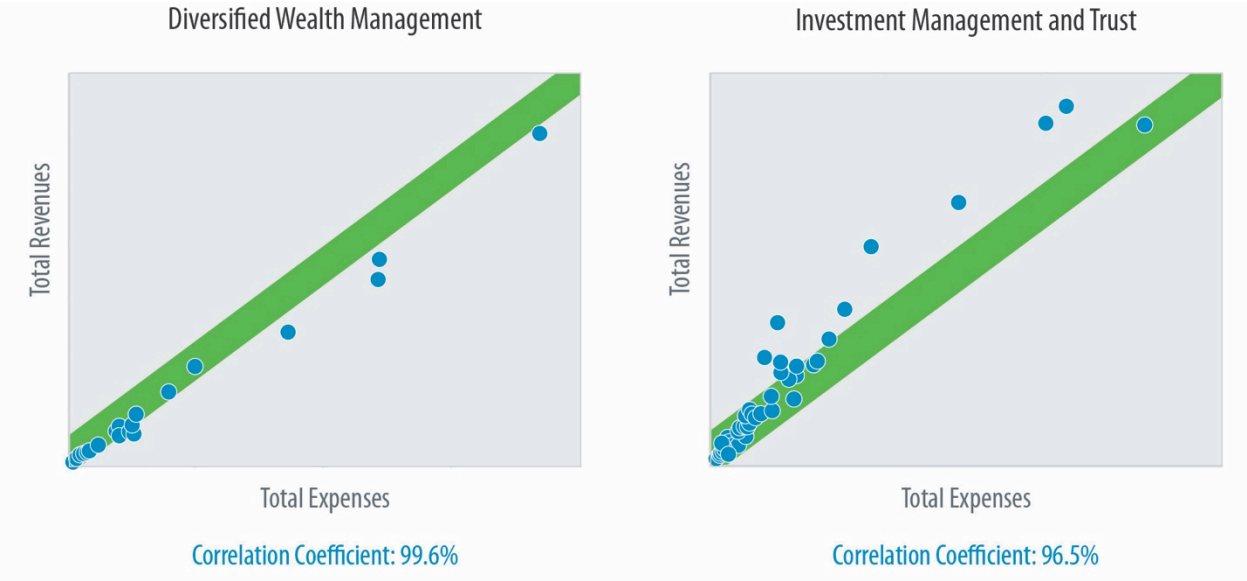
WEAKEN THE TENSION BETWEEN GROWTH AND PROFITABILITY

Growth is Expensive

For integrated wealth managers, as well as for just the investment management and trust business, expenses and revenues move in lockstep. In simple terms, growth in wealth management is expensive: firms can have high growth rates or high margins, but rarely both. Achieving sustainable topline growth seems to require continuous investment in people and other resources.

The relationship between expenses and revenues (below) suggests that scale benefits are relatively weak. If the scale benefits were stronger, the graphics below would show stronger evidence of an upward curve; each additional dollar in spending would produce incrementally more revenue.

TOTAL EXPENSES VS TOTAL REVENUES



THE RELATIONSHIP BETWEEN EXPENSES AND REVENUES (ABOVE) SUGGESTS THAT SCALE BENEFITS ARE RELATIVELY WEAK: If the scale benefits were stronger, the graphics would show a stronger upward curve; each additional dollar in spending would produce incrementally more revenue.

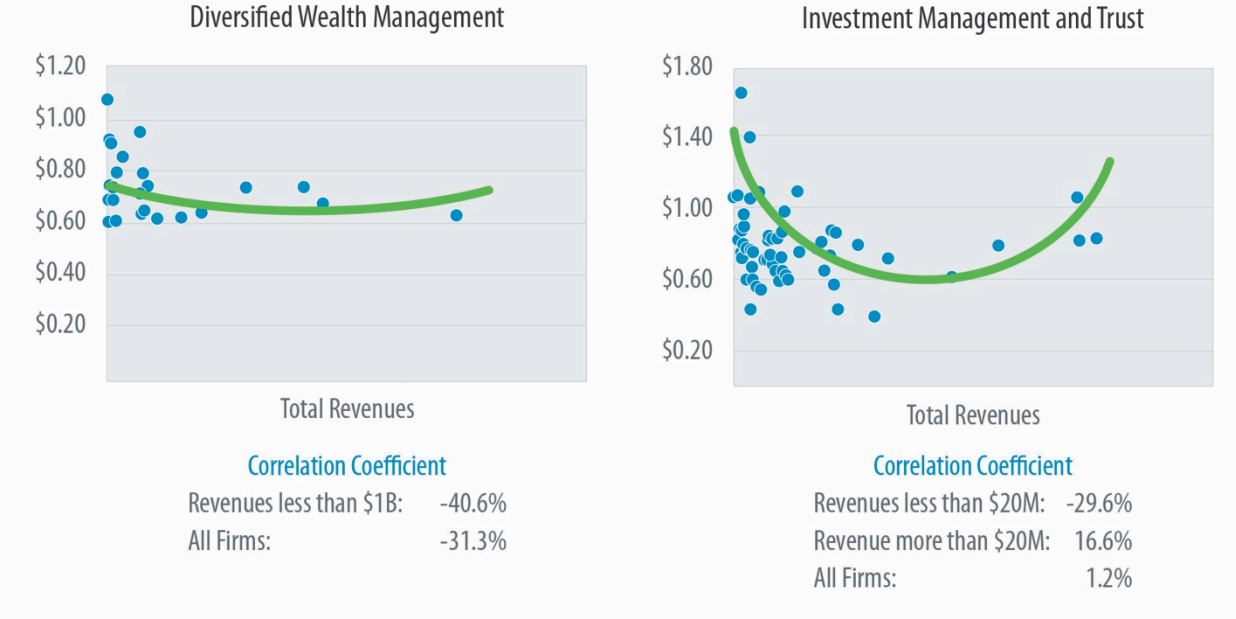
Signs of Scale Economies and Diseconomies

Further exploration of scale suggests that there are at least modest scale economics in both the diversified wealth management business as well as in the investment management and trust business.

For *all* firms, from very small to very large, the relationship between a firm's unit costs and its size is weak or nearly nonexistent. However, as firms grow from small to midsize, or from midsize to large, the relationship is more nuanced.

For example, up until a point, the costs per revenue dollar decrease as firms increase in size (i.e., they are negatively correlated). In other words, up to a point, there is evidence of modest scale benefits that likely reflect the benefits of resource centralization, specialized labor, and investments in technology.

COST PER REVENUE DOLLAR



FOR ALL FIRMS, FROM VERY SMALL TO VERY LARGE, THE RELATIONSHIP BETWEEN A FIRM'S UNIT COSTS AND ITS SIZE IS WEAK OR NEARLY NONEXISTENT. As firms go from small to midsize, or from midsize to large, however, the relationship is more nuanced.

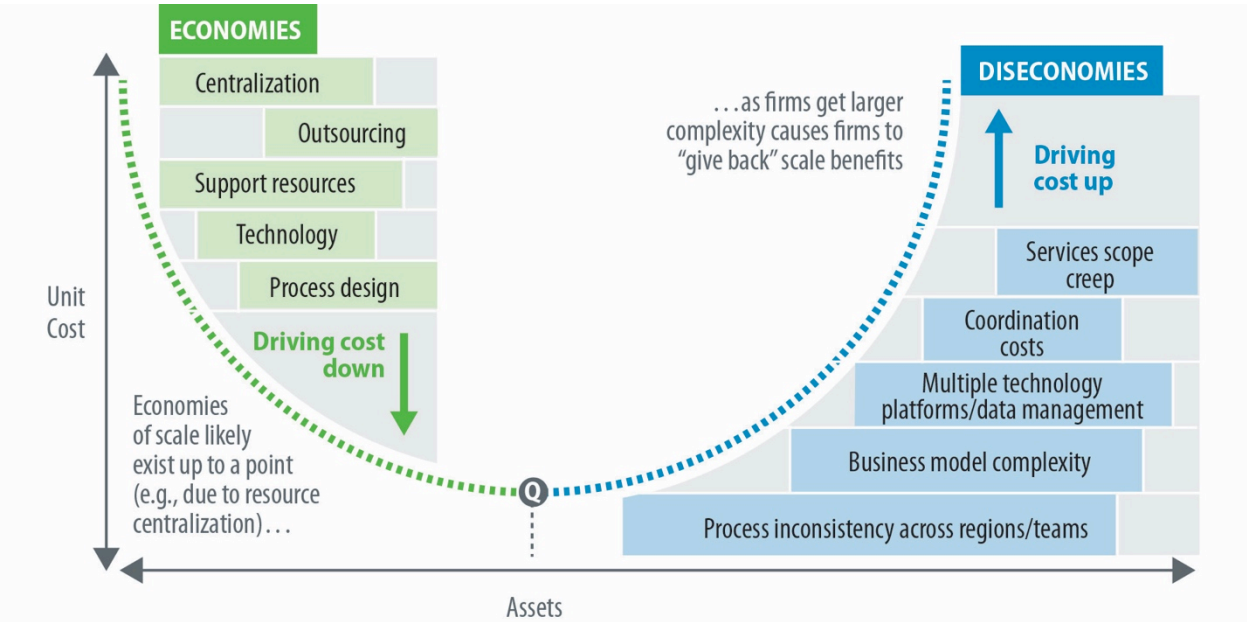
A similar pattern is observed in the cost per dollar of assets under management (AUM). Up until a point, as firms get bigger, the cost per dollar of AUM tends to go down. Beyond that point, the benefits of getting bigger seem to degrade or weaken. In fact, the data hint at diseconomies of scale for large and very large firms.

COST PER DOLLAR OF ASSETS UNDER MANAGEMENT

THE NEGATIVE CORRELATION BETWEEN THE UNIT COST OF A DOLLAR OF AUM AND SIZE STARTS TO DEGRADE AROUND $20 MILLION IN REVENUES. In other words, there appears to be at least modest scale benefits for firms beneath this threshold. Including larger firms significantly weakens the observed scale benefits.

In the stylized graphic below, unit costs go down up until point Q. Beyond point Q, unit costs start to increase again (or at the very least, to flatten).

SIGNS OF ECONOMIES AND DISECONOMIES



UNIT COSTS GO DOWN UP UNTIL POINT Q. Beyond point Q, unit costs start to increase again (or at the very least, to flatten).

The relationship between unit cost and firm size has key implications for wealth managers of all sizes.

Resource centralization, specialized labor, and investments in technology provide significant benefits.

Firms follow a predictable path as they grow: they centralize various processes, job functions, and types of expertise; they outsource; they invest in technology. These changes provide concrete returns in the form of more productive advisors and lower per unit costs.

Unmanaged complexity causes firms to 'give back' some of the benefits of scale.

As firms grow from midsize to large (to very large) they also introduce a lot of complexity into their service and sales operations. As firms grow, service breadth, team size, and number of teams go up. Having more people and more services increases firms' coordination costs; having more teams increases the risks of inconsistent process and execution. Acquisitions of other wealth management businesses adds to this complexity. For these and other reasons, larger firms are often working off of multiple technology platforms. Lack of interconnectivity—from planning to brokerage systems—renders fundamental tasks such as effective client data management more complex.

In short, growth is expensive, and the tension between growth and profitability is real. In particular, a growth strategy powered primarily by hiring more relationship managers and more sales officers will likely add commensurate expense. Rather than simply hire more advisors to drive growth, firms would first do well to take more low-value tasks off of their existing advisors' desks to free up time for sales. In other words, they would do well to invest in their advisors' productivity.

What is clear from the "small" to "midsize" growth trajectory is that investments in improving productivity have strong financial benefits. Similar benefits likely accrue to those that are able to establish a bulwark against the encroachment of complexity as they grow. All signs seemingly point in the same direction: productivity improvements may not fully break the tradeoff between growth and profitability, but they can chart a path towards more efficient growth at a time when one is sorely needed.

STAYING STILL IS A DECISION—AND IT'S A POOR ONE

Our view is that firms need to do more to improve the productivity of client-facing teams. To be sure, however, many firms will choose to stay the course in 2016: to maintain tight control of expenses and to hope for an improving economy, strong equity markets or business liquidity to fuel revenue growth. While the status quo might work in the short-term, it has limits. At the very least, firms need to find a way to offset the rising costs of regulation, technology, and service demands. Cutting other costs is an unlikely salve, as most are already working off of lean cost structures. Alleviating expense pressures, therefore, will require growth, but growth net of market effects has been difficult to come by.

Unfortunately, the traditional model of growth—hire more advisors—is both costly and likely to become more so.

Responding to Advisor Scarcity

Longer-term, demographic changes threaten to shrink the talent pool and make "staying still" an even less palatable option. Replacing relationship managers and business development officers is already challenging. BDO openings in particular can languish unfilled for months. A retirement wave is likely to exacerbate hiring difficulties. Development and coaching programs may provide relief, but not immediately: firms that plan to "grow their own" advisors typically plan for a 5-7 year development time horizon from new hire to full productivity. Improving productivity will provide an essential source of service and sales capacity that firms require to grow.

Five Things Firms Need to Do Today

For many firms, significant productivity gains are within reach.

INTRODUCTION: TOWARDS A NEW FRONTIER

For a bank with a history dating to the late 19th century—to the Second Industrial Revolution, the development of railroads and the steel industry—Hay Adams Bank* could be forgiven for falling victim to its own traditions. Following numerous business consolidations, however, the leadership in the bank's wealth management business realized that its productivity lagged far behind its potential. In essence, the "consolidated" business wasn't: legacy technology and inconsistent servicing practices led to inefficiency and unacceptable risk. Enlisting a third-party for a complete review of its sales and service processes, the bank made significant investments in standardizing its service approaches and providing enhanced support to its advisors. The outcome? A 40 percent increase in the bank's sales and service capacity.

CASE STUDY: PROCESS REVIEW, HAY ADAMS BANK

ACTIONS:

#1: Standardized Approaches

Aiming for greater process consistency and less risk, the bank added managerial oversight for operations, service delivery, and compliance; introduced new quality control processes; and created a codified desk version of the firm's policies and procedures. Advisors are less reliant on their managers for guidance.

#2: Enhanced Support for Client Advisors:

A Centralized Administration Team staffed by Client Service Managers (a new role) was created to provide centralized service support for the following:

- Small accounts: Less than $1 million in assets
- Complex or specialized products: Custody, IRAs, life insurance trusts
- Administrative processes: Account openings and closings

OUTCOMES:

40% increase in front office capacity

30% average increase in 2016 sales goals

HOW IT WORKS:

Account openings shift from the front office to Client Service Managers (CSM).

The CSM is responsible for client setup, asset transfers, initial reviews, fees and setting up files; once complete, the lead RM gets the account back for ongoing service.

KEY INSIGHT:

"We estimate that we will reduce the front office workload by 40%. Importantly though, [our advisors] have to fill the 40% with sales and service. We estimate the average sales goal per advisor will increase by 30% next year."

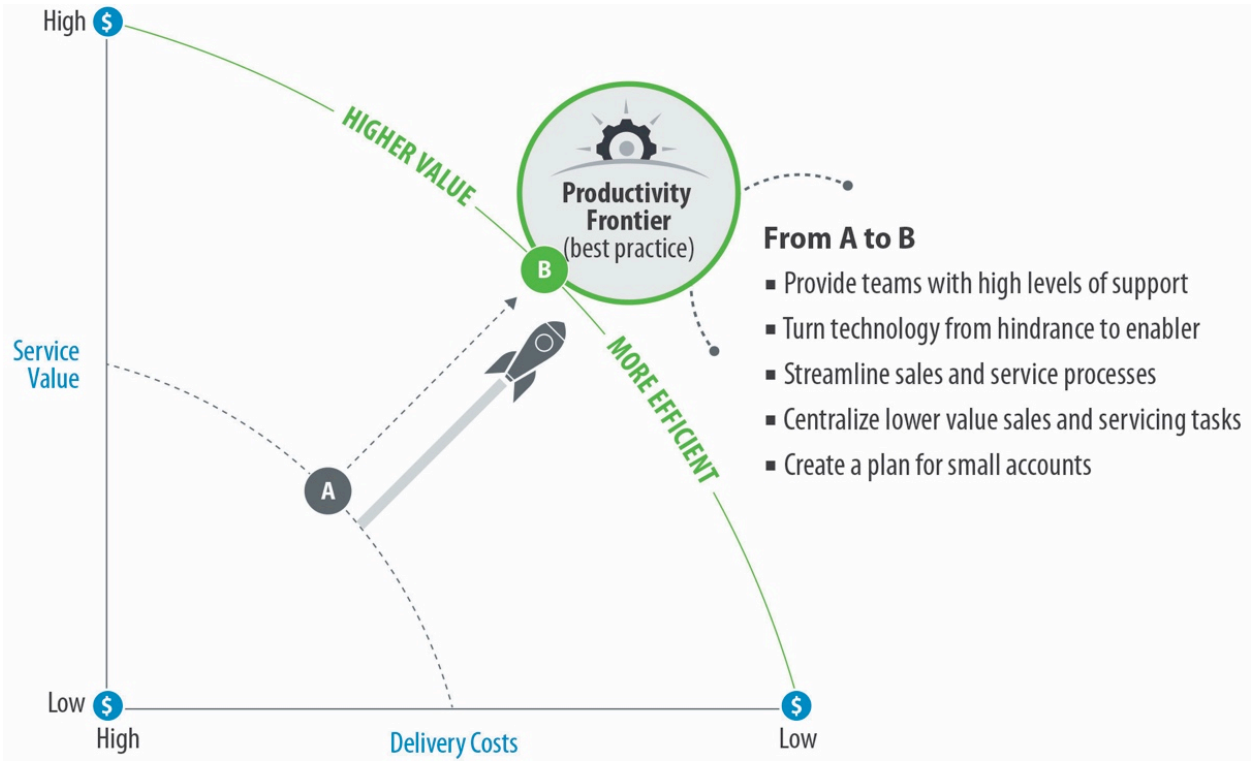
ENLISTING A THIRD-PARTY FOR A COMPLETE REVIEW OF ITS SALES AND SERVICE PROCESSES, the bank made significant investments in standardization and advisor support.

* Pseudonym

Standardization and support are the hallmarks of the Hay Adams Bank case example, and show that productivity improvement initiatives can have extremely high returns. In our view, those returns are measured in better service quality and lower costs.

Imagining these dual benefits—better service, lower costs—as the dimensions of a productivity frontier, our research seeks to understand whether firms have the opportunity to improve. In other words, can they move from point A to point B (below)? The answer is a resounding "yes".

THE PRODUCTIVITY FRONTIER



AT THE HIGHER FRONTIER, DELIVERY COSTS ARE LOWER (e.g., per-unit costs are lower, risks and errors are reduced. Service value goes up as advisors have more time for proactive servicing, communications, needs identification, etc.

For many firms, significant productivity gains are within reach.

There is a lot of qualitative evidence that firms fall short of the optimal frontier†. There's also a quantitative case: fundamental productivity metrics such as revenue per employee show huge variations between high and low performers (e.g., of 50% or more). These variations persist even within cohorts of firms that are a similar size and have similar service team structures. Some firms, it appears, are simply a lot more productive than others.

† See Section 1, "The Case for Change"

We believe a set of five characteristics differentiate firms that are less productive (point A) from their more productive peers (point B).

In the following pages, we explore each of these characteristics in detail.

1. Provide client-facing teams with higher levels of support and infrastructure.

SUMMARY OBSERVATIONS

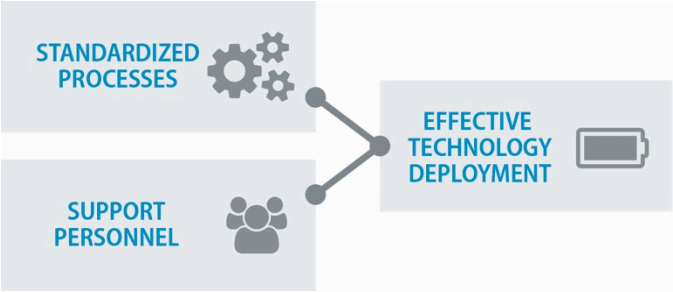
Our analysis of common team structures anchors our productivity recommendations. A few observations rise to the fore:

Some firms get a lot more production out of their teams than do others.

There is a lot of variability in the productivity of similarly-structured teams at similarly-sized institutions. In other words, implementing a specific type of service team model won't necessarily yield better results than another. Management quality matters, of course, as do support resources.

How firms support their teams affects productivity more than team structure.

"Support" is broadly defined here as the resources and processes firms use to minimize coordination costs and to leverage key client-facing personnel. More so than team structure, success hinges on how firms deploy support personnel to handle lower-value servicing and administrative tasks, and the extent to which sales and service processes are standardized. Most of these activities are enhanced by effective technology deployment, which is likely one of the biggest differentiators in the performance of client-facing teams.



DIFFERENCES IN PRODUCTIVITY HAVE LESS TO DO WITH TEAM STRUCTURE and more to do with service processes and support personnel (administration, client service officers, middle office, and third-party). All are enhanced by effective technology deployment, which is a big performance differentiator.

Account size, revenue mix, and pricing matter too.

Fairly or not, some teams' productivity measures receive a revenue "lift" from factors that they may not directly impact. Having large average account sizes has a particularly strong positive impact on profitability.

Larger teams generate more revenue per person, but also have higher coordination costs.

Larger teams generate more revenue per capita, but they are also more expensive by definition and have higher coordination costs. For example, as teams get bigger, more than one person is likely to serve as the main point of contact and team sales become a lot more common (multiple people have sales responsibilities).

To the extent that bigger teams, broader service offers, and higher-revenue relationships go together (and they do), the need to effectively manage complexity escalates as well.

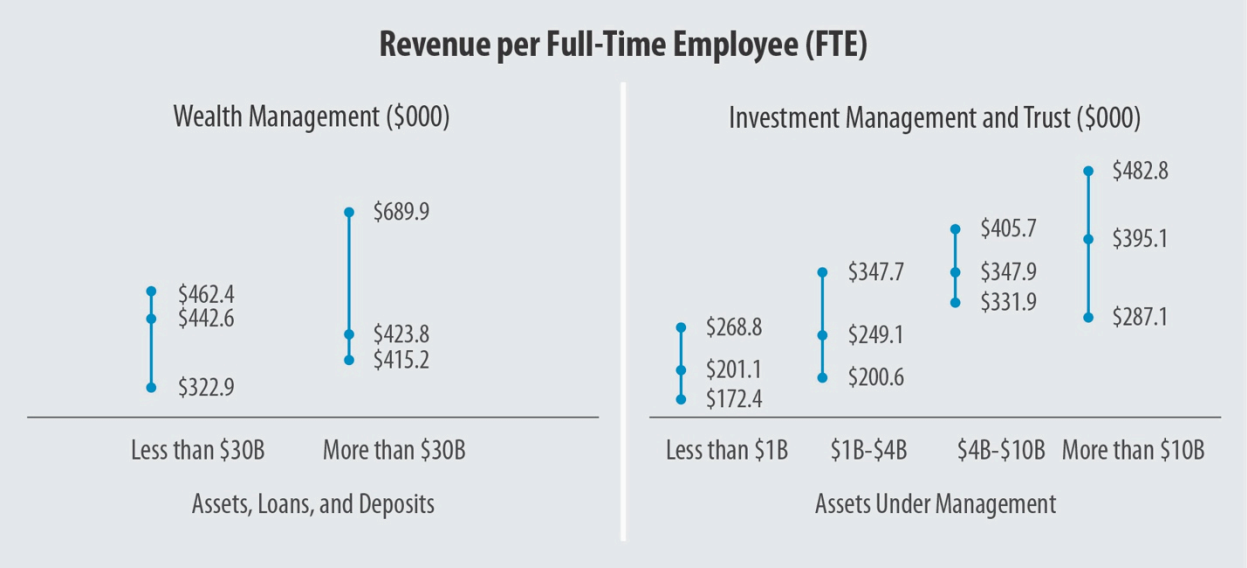
Our analysis of team structure is organized around three main questions:

- What does "productive" mean?
- How are teams structured?
- What explains variations in team performance?

Each of these questions is explored in turn.

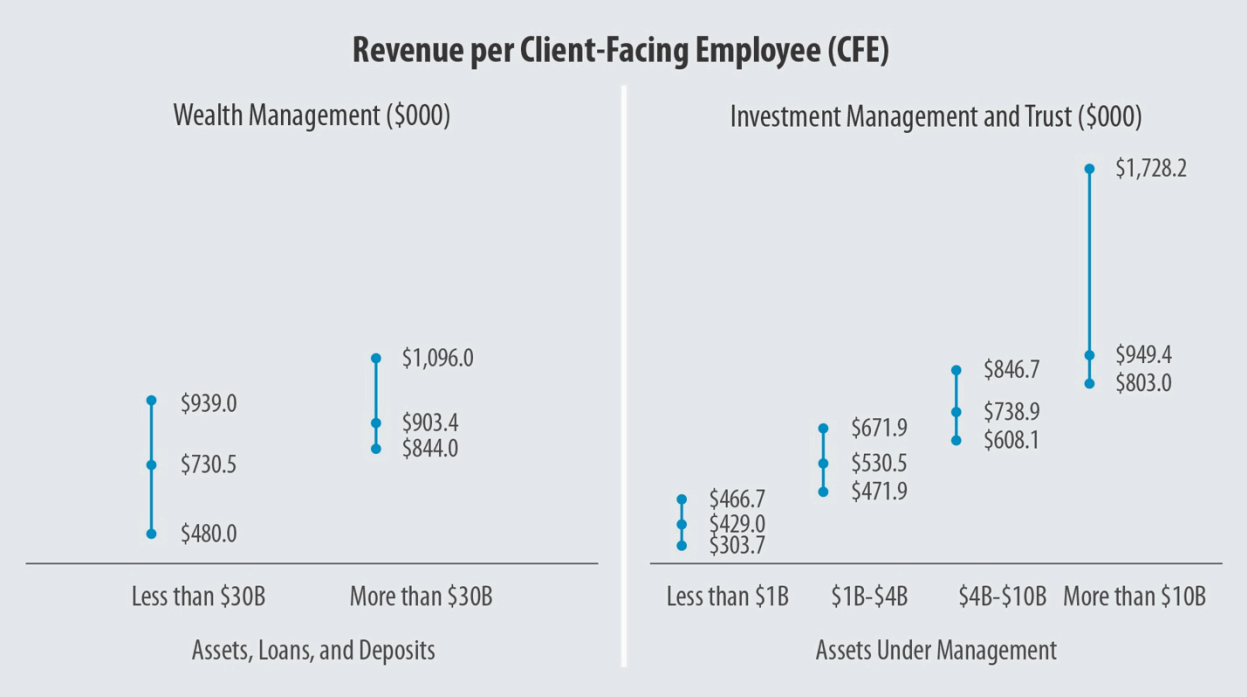
WHAT DOES "PRODUCTIVE" MEAN?

To the extent that there are scale benefits in wealth management, they likely come from having more productive client advisors.



Productivity—defined here as revenue per full-time employee—increases with firm size. In simple terms, the most productive advisors work for larger firms. Size is only part of the story, however, and, even within size cohorts, productivity is extremely varied.

Revenue per client-facing employee measures—defined here to include all of a firm's client-facing service and sales exclusive of support roles—show similar patterns. Client-facing employees at larger firms manage more revenue, although production levels are again highly varied within size cohorts.



THE LANDSCAPE: OBSERVATIONS ON TEAM STRUCTURE

We analyzed four common team structures using team size as an organizing framework:

- Model A: Investment Management and Trust, Small Team (three employees)
- Model B: Investment Management and Trust, Large Team (four employees)
- Model C: Wealth Management, Small Team/Small Firm (five employees)
- Model D: Wealth Management, Large Team/Large Firm (six employees or more)

With the exception of Model D—which is the largest of our four teams and common to many very large firms—Models A, B, and C are found in firms of varying size (for a detailed overview of each model, see the end of this section). We similarly use team size to identify patterns in the industry landscape and, specifically, key differences between small and large team service models. Going from small teams to large:

Bigger teams deliver broader service offerings.

As the service offering gets broader and service delivery more integrated, the size of the team goes up, and in many cases considerably.

Team sales become more important.

The number of people per team with relationship expansion or new client acquisition responsibilities goes up. Common relationship manager roles—trust officers, bankers, wealth advisors—are more likely to be responsible for sales to both new and existing clients.‡

More than one person serves as the relationship manager.

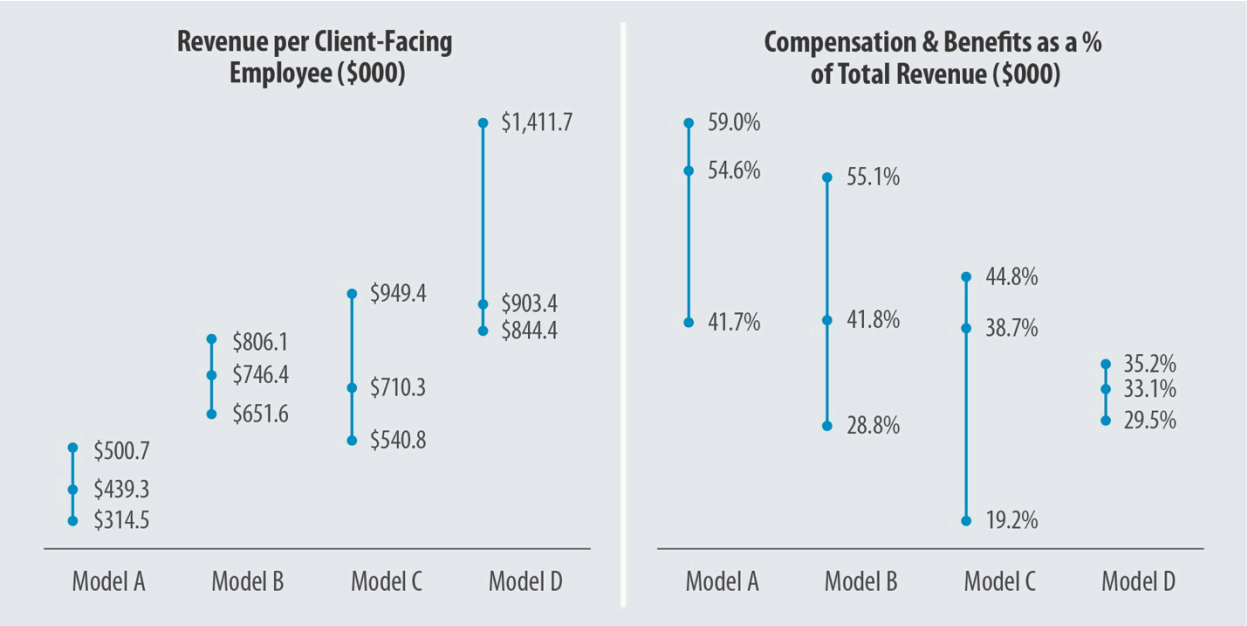
On bigger teams, the lead relationship manager can be filled by more than one role, depending on the lead product, client preferences, etc.

The average relationship and account size increases.

Average relationships are bigger in terms of depth (e.g., assets per account) and also in breadth of services.

Core productivity metrics go up.

Notably, revenue per client-facing employee goes up and firms spend less on compensation as a percentage of revenues.



The proportions of relationship manager to investment professional to support staff are fairly consistent.

Except for the three-person team, the ratios of RMs to investment professionals to support staff is roughly 3 to 1.5 to 1.

‡ The Portfolio Manager role is an exception to this trend. As team size increases, the Portfolio Manager's sales responsibilities decline, and the Portfolio Manager's role is much more likely to be a pure investment role.

EXPLAINING VARIATIONS IN TEAM PERFORMANCE

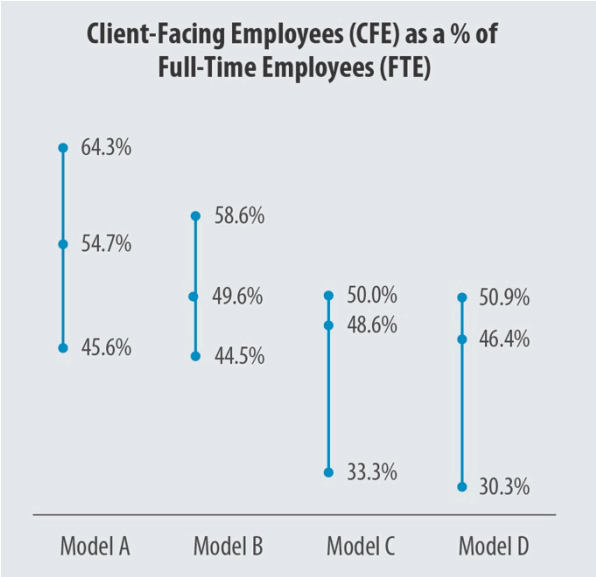
Variations in performance at firms that deploy similar service team models provide clues about what characteristics matter more than others.

More profitable firms have more productive teams.

This is true for multiple definitions of "productive", including net income-, compensation-, and revenue-related productivity metrics.

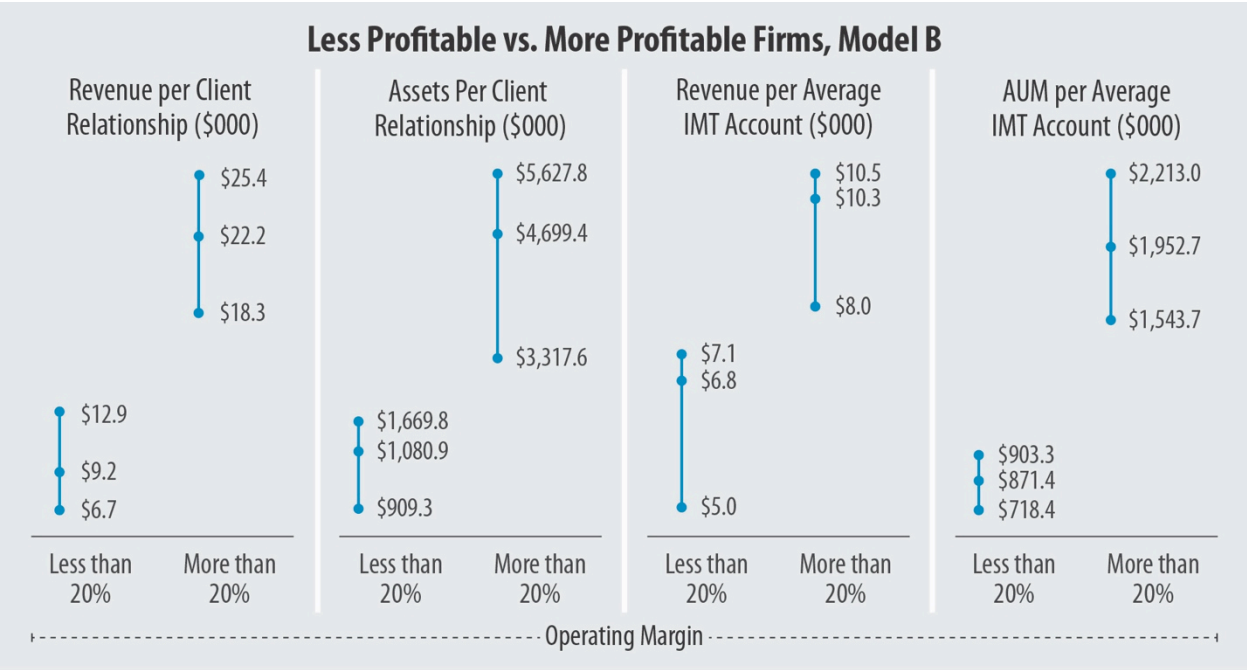
Firms with fewer client-facing employees as a percentage of all employees tend to have better financial outcomes.

In other words, providing advisors with high levels of support has a salutary impact on financial outcomes (support can include better tools and technology). From a financial perspective, at many higher margin firms, the overall staffing mix proportionately favors lower cost labor. For example, in Model D (large firms, diversified wealth management services), key "all FTE" productivity metrics are similar across the board. At more profitable Model D firms, however, the productivity of high cost, client-facing staff is much higher, and they are proportionately fewer in number.



Relationship and account sizes matter a lot.

There are big swings in average investment management and trust account sizes within our four models. Teams at more profitable firms tend to have larger accounts and larger client relationships, as shown below for firms that use team model 'B'.



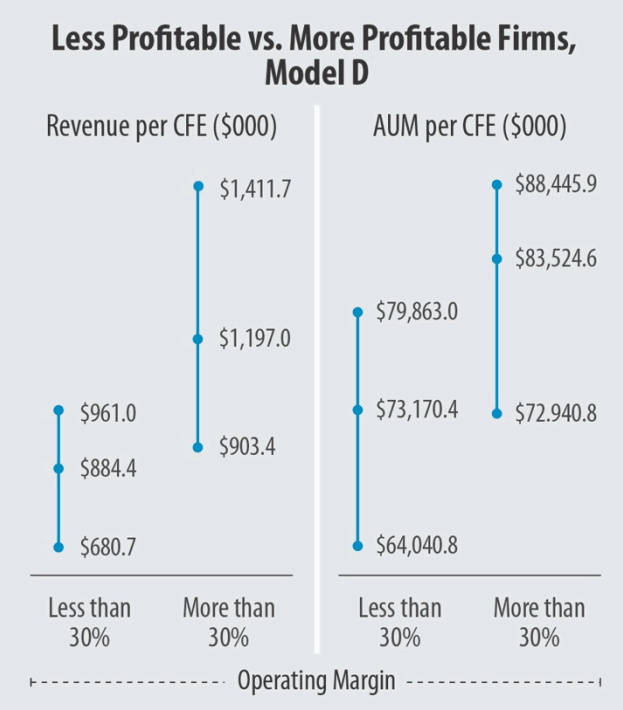
Teams at lower margin firms serve more client relationships.

This observation is a corollary to the notion that bigger relationships and accounts are beneficial. As a group, lower margin firms have smaller average relationship and account sizes.

Revenue mix and pricing effectiveness probably make certain teams look a lot more productive than others.

For example, in Model D (large firms, diversified revenues), teams at higher-performing firms are more productive on a *revenue* basis, but are about the same as others on an *asset* basis. These teams are probably the beneficiaries of a more favorable revenue mix (e.g., more banking revenue) or better pricing. Neither the team nor team design may deserve "credit" for this outcome, but, nonetheless, their productivity numbers are favorably impacted by these characteristics.

For firms that are have a higher-proportion of non-interest income (in our parlance, Models A and B) the same is true: higher performing teams tend to work at firms with a greater emphasis on investment management, and derive proportionately less revenue from personal trust.



IMPLICATIONS FOR MANAGERS

Especially as firms embark on a shift to broader-based client relationships (under the banner of providing holistic advice), variations in team design and performance carry important implications. In their strategic plans and communications, numerous firms aspire to bring "the full breadth of their organizations" to bear on client needs; in team performance, however, it is likely the case that lower-performers have the additional headcount, but have an unfavorable revenue mix and/or lack relationship depth.

Our team structure analysis suggests that gaining "scale" in client relationships is especially important, both depth and breadth. Phrased in the negative, as teams get bigger (and more expensive), the costs of saddling them with small and single-service relationships seems even more risky. An effective small account strategy seems essential.

It is also likely that service model trends are likely to introduce greater complexity in the form of larger teams (e.g., more bodies, more products, more services). Firms' ability to manage complexity and coordination costs—through support resources and technology—as well as their ability to develop strong competencies in team-based sales and source good sales talent are likely to be key performance differentiators

MODEL A — INVESTMENT MANAGEMENT AND TRUST — SMALL TEAM — 3 PEOPLE

Who is on a typical team?

- Trust Officer
- Admin Assistant
- Portfolio Manager

What is the average division of labor?

Relationship Management/Sales	42%
Investments	33%
Support/Administration	24%

Who is the lead relationship manager?

Trust Officer	62%

Who is the investment lead?

Portfolio Manager	85%

% of advisor time spent on admin work	47%
% of assets managed by firm	92%
% of assets managed by a third-party	8%

Sales Model

Number of BDOs per client-facing team	0.75
BDOs per relationship manager	0.5
Dedicated sales support per relationship manager and BDO	0.1
Percent of prospects that become clients	52%
Typical length of sales cycle	3 mos.

MODEL B — INVESTMENT MANAGEMENT AND TRUST — LARGE TEAM — 4 PEOPLE

Who is on a typical team?

- Trust Officer
- Financial Planner or Wealth Advisor
- Portfolio Manager
- Admin Assistant

What is the average division of labor?

Relationship Management/Sales	56%
Investments	26%
Support/Administration	17%

Who is the lead relationship manager?

More than one position	63%	Trust Officer	50%

Who is the investment lead?

Portfolio Manager	88%

% of advisor time spent on admin work	47%
% of assets managed by firm	91%
% of assets managed by a third-party	9%

Sales Model

Number of BDOs per client-facing team	0.28
BDOs per relationship manager	0.1
Dedicated sales support per relationship manager and BDO	0.2
Percent of prospects that become clients	53%
Typical length of sales cycle	4 mos.

MODEL C — DIVERSIFIED WEALTH MANAGEMENT SMALL TEAM 5 PEOPLE

Who is on a typical team?

- Trust Officer
- Portfolio Manager
- Private Banker
- Admin Assistant
- Financial Planner or Wealth Advisor

What is the average division of labor?

Relationship Management/Sales	58%
Investments	24%
Support/Administration	18%

Who is the lead relationship manager?

Private Banker	>1 position
50%	38%

Who is the investment lead?

Portfolio Manager	75%

% of advisor time spent on admin work	35%
% of assets managed by firm	90%
% of assets managed by a third-party	10%

Sales Model

Number of BDOs per client-facing team	0.33
BDOs per relationship manager	0.1
Dedicated sales support per relationship manager and BDO	0.1
Percent of prospects that become clients	41%
Typical length of sales cycle	4 mos.

MODEL D — DIVERSIFIED WEALTH MANAGEMENT LARGE TEAM 6+ PEOPLE

Who is on a typical team?

- Trust Officer
- Portfolio Manager
- Private Banker
- Client Service Officer
- Wealth Advisor
- Admin Assistant

LESS COMMON ROLES

- Financial Planner
- Investment Analyst

What is the average division of labor?

Relationship Management/Sales	56%
Investments	20%
Support/Administration	24%

Who is the lead relationship manager?

Wealth Advisor	Private Banker	>1 position
63%	40%	40%

Who is the investment lead?

Portfolio Manager	89%

% of advisor time spent on admin work	37%
% of assets managed by firm	94%
% of assets managed by a third-party	6%

Sales Model

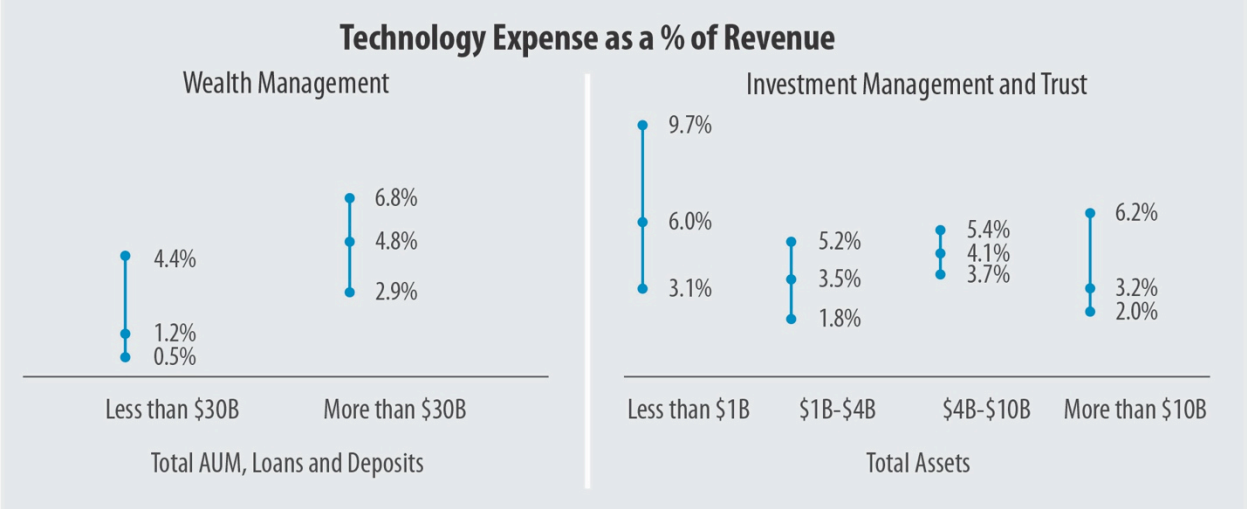
Number of BDOs per client-facing team	0.35
BDOs per relationship manager	0.1
Dedicated sales support per relationship manager and BDO	0.1
Percent of prospects that become clients	44%
Typical length of sales cycle	4 mos.

2. Turn technology from hindrance to enabler.

The manner in which firms deploy technology almost certainly contributes to differences in productivity and other performance outcomes. For many firms, the hidden costs of legacy technology are a hindrance. Firms that have upgraded their technology platform are realizing much greater productivity gains by streamlining and automating formerly manual processes. The following are our key observations on technology:

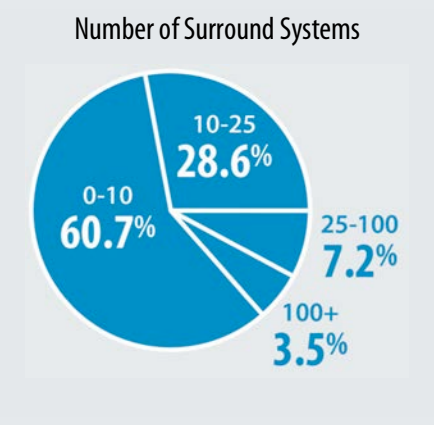
Spending levels vary considerably by firm.

Larger firms tend to spend more on technology (as a percentage of revenues) but, as with many expenses, solid minorities in all size cohorts spend very little. For large diversified wealth managers, a typical firm spends between 2.9% and 6.8% of revenue on technology. Technology spending at large investment management and trust business shows a similarly wide range, from 2.0% to 6.2%.



Low spenders are probably redistributing costs rather than saving money.

The cost of underperforming technology solutions is heard most acutely in anecdote—for example, in the difficulties of changing a client address, or in figuring out if "Mr. Jones" in the trust and banking systems is the same person. Other costs are more easily quantified, such as the number of surround systems. As the age of the core accounting platform goes up, so too does the number of surround systems, and often dramatically (i.e., systems that firms have to layer on top of their core platform to get it to work).

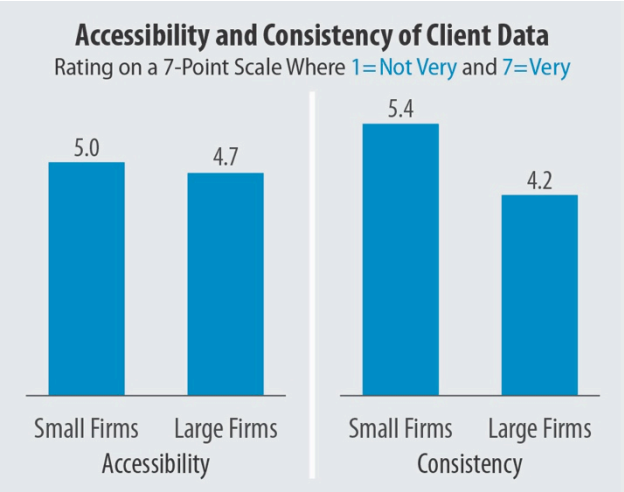


Similarly, firms with older, legacy technology, spend a larger percentage of their budgets on maintenance rather than new investment.

Effectively managing client data is a big challenge, especially for larger firms.

Many firms feel that they could do more to make client data accessible to their teams, and to make the data itself more consistent.

Effective data management generally gets more challenging as firms get bigger and have to contend with more clients and technology platforms. On average, firms do an adequate job making client data available to their teams, rating themselves roughly a five on a seven-point scale. Maintaining consistent data is a bigger challenge. Large firms barely eke out a 4 out of 7 rating.



> [Until recently], all of our wealth businesses were distinct business units. That means that the systems that service them, such as the brokerage system, are all separate and distinct from other platforms, such as banking and trust. Each of those legacy business units has its own way of measuring revenue associated with relationships. We don't have good reporting. We don't know how many new clients we bring to the table every year. We are still establishing a firm hold on our customer base. We've been segmenting our clients and developing a household strategy.
>
> COO, LARGE WEALTH MANAGER

New technology can displace manual processes and labor costs.

A sizable chunk of firms' technology budgets is earmarked for fixing problems: for upgrading old accounting platforms and for improving interconnectivity and data management.

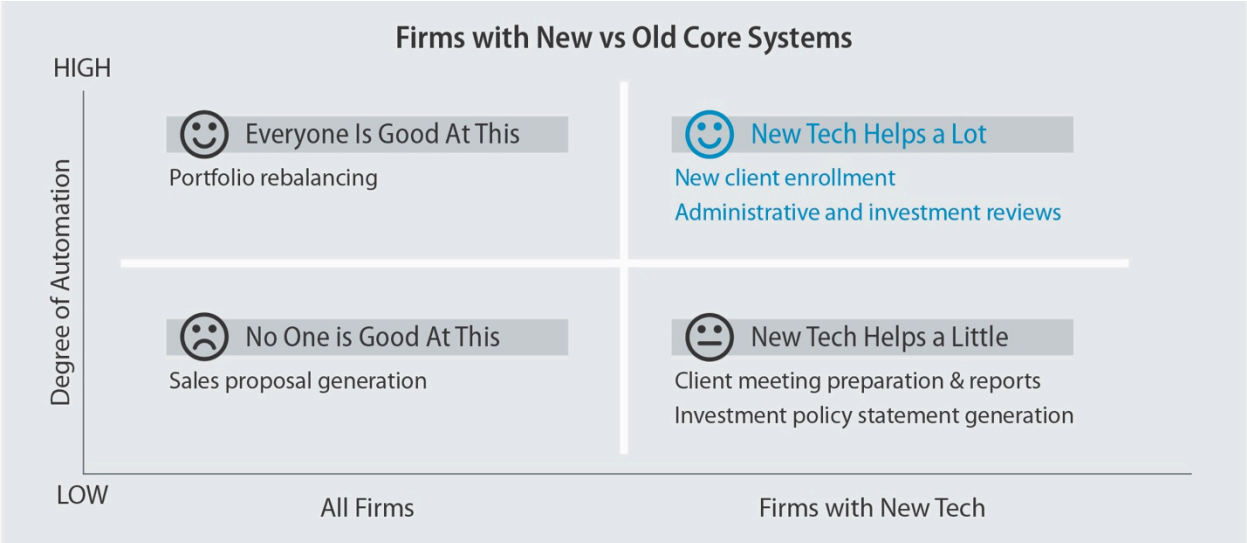
A second set of spending priorities—including CRM, financial management and planning tools, and mobile—aim to directly impact the client service experience.

SURROUND SYSTEMS & TECHNOLOGY SPENDING PATTERNS

Firms where core accounting system is:

	NEWER THAN 5 YRS	OLDER THAN 5 YRS
% of firms with >25 surround systems	0%	17%
% of tech budget spent on maintenance	79%	85%

Although difficult to quantify, technology initiatives potentially yield significant productivity gains through the automation of formerly manual processes.



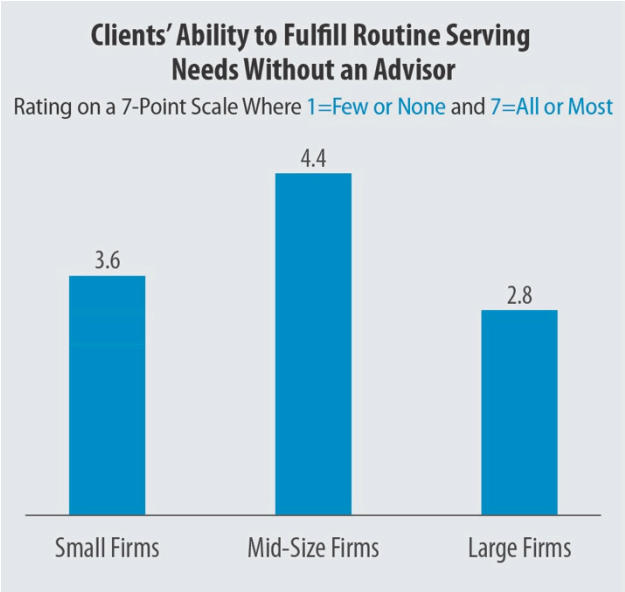
Firms with newer technology are somewhat more likely to automate the processes supporting investment policy statements, client reporting and meeting preparation. They are much more likely to describe the "problem areas" that are common in firms with older technology as automated, such as new client enrollment processes and administrative and investment reviews.

New technology is displacing routine client service interactions and labor costs (but there's more work to do).

For the do-it-yourself set, which likely includes a lot of younger clients, the options in wealth management are a mixed bag. Firms commonly give themselves a 3 or 4 rating for "self-service" on a seven-point scale.

Despite being the big spenders in technology, large firms rate themselves the lowest. Our expectation is that self-service options are likely to improve in the near term.

Managers are keenly interested in realizing potential service and efficiency gains by providing automated or self-service options for routine service interactions and lower wealth tiers.



3. Streamline sales and service processes.

While not as exciting as a new investment strategy, consistent execution is arguably more important to the success of wealth managers. By developing more consistent sales and service processes, firms improve both the client service experience as well as staff productivity. Process improvement initiatives are often low-cost but potentially high-return. Success typically requires the ability to affect change in employee behavior rather than large capital expenditures. While many might believe that process improvement initiatives only apply to the middle or back office (e.g., centralizing account opening processes; concentrating tasks in a middle office to reduce errors) they also apply to the front office. For example, firms are providing their advisors with coaching, tools, and templates to conduct better client meetings and to expand client relationships.

Efforts to implement more consistent, streamlined service approaches share many of the same characteristics:

GOALS

- Consistently execute across teams
- Promote the adoption of "best practice" sales and service strategies
- Reduce errors and risk
- Eliminate multiple-touch processes and similar redundancies
- Manage the risks of localized knowledge (i.e., held by a small number of people)

ACTIONS

- Standardize team structures across offices and region
- Articulate a clear vision for the client service experience
- Document and analyze existing sales and service processes; identify redundancies and best practices; identify highest return process improvements/triage according to risk, client impact
- Create new service standards, guidelines, activities lists, and success metrics for implementing best practices
- Provide staff training
- Automate workflows for consistency across the supply chain

Success typically hinges on two types of accountability. First, firms are making a person or team accountable for identifying efficiencies (many managers believe process redesigns require different skillsets than those possessed by sales and servicing personnel). A second, more challenging form of accountability is in affecting behavioral change in team members. Compelling managers and their teams to comply with new guidelines is a common but insufficient tactic. Most believe that providing "positive" incentives is vital (e.g., providing staff with an evidence-based case), as well as iterative training and regular, ongoing communication initiatives.

CASE STUDY: SERVICE PROCESS REVIEW, WILLARD BANK

SITUATION

Seeking to eliminate numerous inefficiencies in its trust organization, Willard Bank hired a process engineer, mapped out every single service process, evaluated the impact of each on its client experience, then set out to selectively eliminate redundant processes.

ACTIONS:

Willard Bank's account opening and account review processes were identified as having the greatest potential for improvement.

#1: Account Openings

In certain cases, the bank was asking for the same information three different times (due to lack of connectivity between the bank's trust, CRM, and other wealth management systems). The bank made improvements by changing its account opening documents, tailoring the process to account type, and by integrating data from different systems more effectively.

#2: Account Reviews

Administrative reviews were formerly one-size-fits-all. Post re-design, the review process is designed around specific account types (e.g., the frequency of these reviews and the types of questions they ask).

OUTCOMES:

Improved account review process

	Account Type		
	A	B	C
Review Frequency	2x per year	1x per year	0.5x per year
Question Types			

KEY INSIGHT:

Many efficiency gains are also low cost. The bank is adamant that many firms can improve by more thoughtfully structuring service process and leveraging existing technology resources more fully (rather than investing in new technology).

> "We were asking unnecessary questions during the review process and reviewing more frequently than was needed. For account openings, we were drawing data from multiple systems manually. Not only did we gain efficiency from better managing our account review and opening processes, we reduced risks associated with inconsistent, manual processes."

4. Centralize lower value sales and servicing tasks.

Task centralization and role specialization are good for business. As firms get larger, their employees also get more productive—task centralization and role specialization almost certainly drive the transformation of firms' business processes as they scale. One way to free up advisor capacity, for example, is to centralize various tasks.

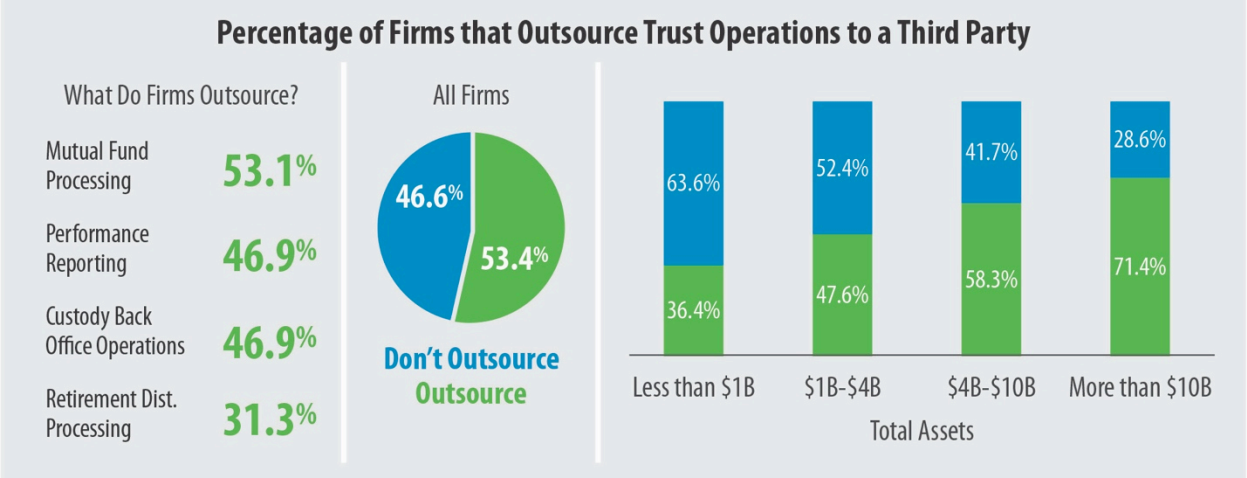
Centralization efforts commonly fall into one of the following categories:

- Administrative tasks
- Small accounts
- Labor-intensive processes (account openings)
- Specialty planning and product expertise (e.g., tax planning and IRAs)
- Investment analysts/research
- Reporting

We look at two examples—outsourcing and administrative associates—to help quantify the impact of centralization efforts on staff productivity. Both examples suggest that centralization initiatives can have a significant, positive impact on productivity.

Example #1: The Impact of Outsourcing

When it comes to outsourcing, theory and practice converge: firms that outsource their operations generally report higher per-employee productivity. This convergence likely explains why the practice is so widespread. As such, the appetite for outsourcing has significantly grown. What was once limited to smaller organizations now includes firms of all sizes; organizations across the size spectrum outsource at least a piece of their business, if not their entire back office. In fact, across firm size cohorts, typically about half of firms outsource their trust operations, with mutual fund processing, performance reporting and custody topping the list of outsourced services.



The empirical case that outsourcing displaces labor costs is strong. Compared to firms that don't outsource, those that do report considerably higher productivity per full-time employee. Assets, revenue, clients, accounts, and key sales metrics are each higher per capita for firms that outsource.

For certain metrics, the gap is considerable: assets per full-time employee are more than 25% higher per employee for firms that outsource.

The difference almost certainly is in the denominator: firms that outsource employ fewer people.

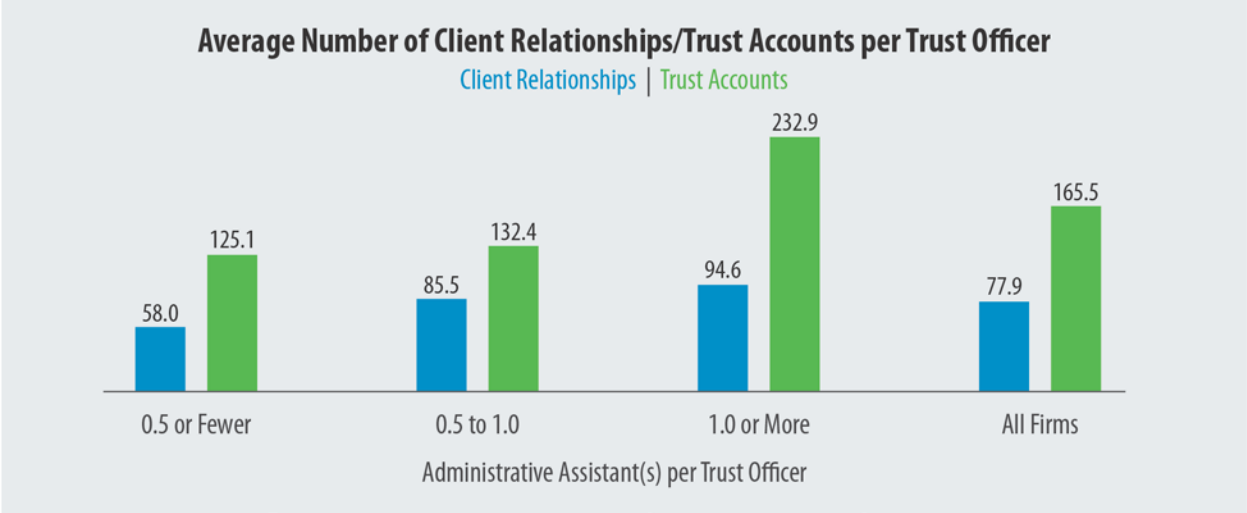
PRODUCTIVITY PER FULL-TIME EMPLOYEE

	Don't Outsource	Outsource
AUM ($000s)	$38,950	$49,063
Revenue ($000s)	$282	$319
Clients	20	23
Accounts	37	50
Revenue from Sales ($000s)	$39	$40
Assets from Sales ($000s)	$4,911	$5,645

THE DATA SHOWN are for investment and management and trust businesses managing less than $10 billion in assets.

Example #2: The Powerful Impact of Administrative Associates

Whereas outsourcing largely displaces labor in the back office, administrative assistants more directly impact the front office. Advisors with relatively high levels of administrative support can handle more clients and accounts (and, often, significantly more). This is especially good news considering that adding clients and accounts also adds incremental servicing costs (versus adding a dollar to an existing account, which carries very little cost). In other words, well supported advisors can manage a more "costly" book of business than others.



In the trust business, these differences can be substantial. For example, trust officers with only a little administrative support—half an administrative associate or less—manage about 60 clients and 125 accounts on average. Trust officers at a merely average firm manage 30% more of each (about 77 and 165), and at well-supported firms, even more.

5. Develop a plan for small accounts and single-service relationships.

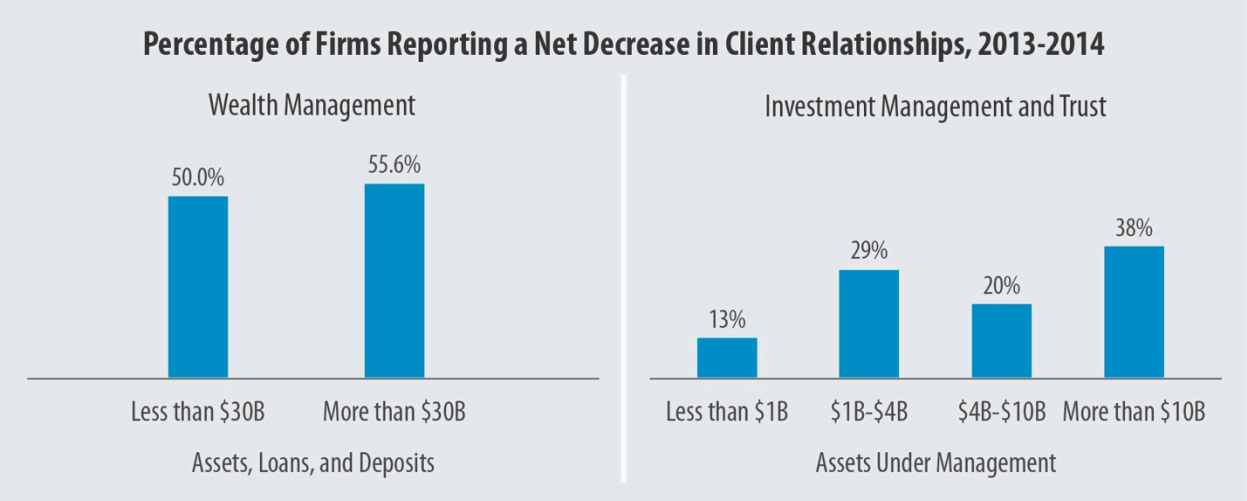
Rivaling old technology, small accounts and single-service relationships are arguably one of the biggest drains on front office productivity. At small firms and large, they contribute to cross-subsidies between clients and crowd out sales activities. Small accounts and single-service relationships have even been blamed for higher cost allocations, staff burnout and poor service. In centralization initiatives, small accounts are one of the first things to move.

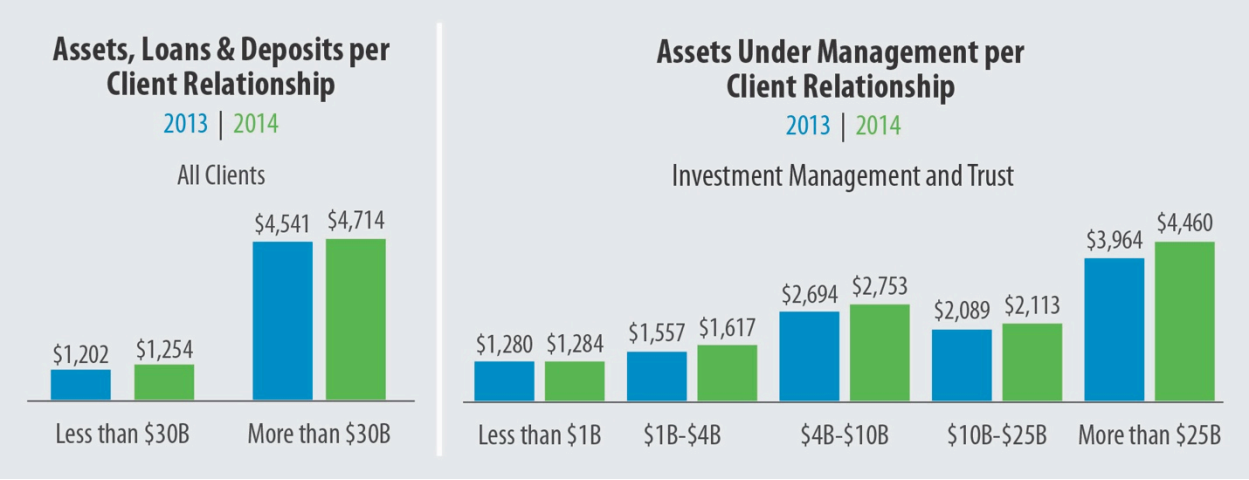
> **"50% of our accounts represent just 10% of our income."**

> **"We're stuck with all of these clients that just have a home equity line of credit from back when our firm was trying to acquire new relationships. I don't know what to do with them!"**

It's no surprise, therefore, that while most industry growth metrics have gone up at least modestly over the past few years, client counts have been going down as firms work to improve the quality of their books of business.

In fact, roughly half of diversified wealth managers reported a net decrease in client relationships from 2013-2014. Sizable minorities reported the same in their investment management and trust businesses. Paired with modest increases in assets, loans, and deposits, the average client relationship size has been growing year-on-year (next page).





IMPLEMENTING A SMALL ACCOUNT STRATEGY

One Giant Caveat

Although larger client relationships generally have a beneficial effect on profitability, small account initiatives are tricky to implement. The biggest challenge is in differentiating between a productivity-sapping small relationship and a future growth opportunity. A small account can be either. A lesser-voiced concern is that external referral sources are less likely to refer valued client relationships to firms that will serve that client using a small accounts team, call center or equivalent resource. Firms typically address the former concern one of two ways. Some assign a sales resource to mine small accounts for relationship expansion opportunities. Others segment their accounts—by tenure and current-period revenue contribution, for example—to identify high and low-potential opportunities. Tenured, low-revenue accounts are candidates for reassignment to a lower-cost servicing resource.

Approach #1: Serve Small Accounts with a Lower-cost Resource

A straightforward approach is to move small accounts from the desks of senior client-facing advisors to lower-cost personnel. A centralized trust administration team, for example, might be staffed by a lower-cost client service manager/officer role (or equivalent). These roles are something less than a senior client advisor and something more than a purely administrative role. Client service managers often support cumbersome or labor-intensive services such as account openings.

Approach #2: Serve Small Accounts with a Standardized Service Approach

If the first approach involves swapping higher-cost and lower-cost labor, the second is essentially the same, except higher-cost labor is displaced by standardization and automation. The investment advisory services at Lombardy Bank[§] are characteristic of this approach.

§ Pseudonym

CASE STUDY: STANDARDIZING THE SMALL ACCOUNT, LOMBARDY BANK

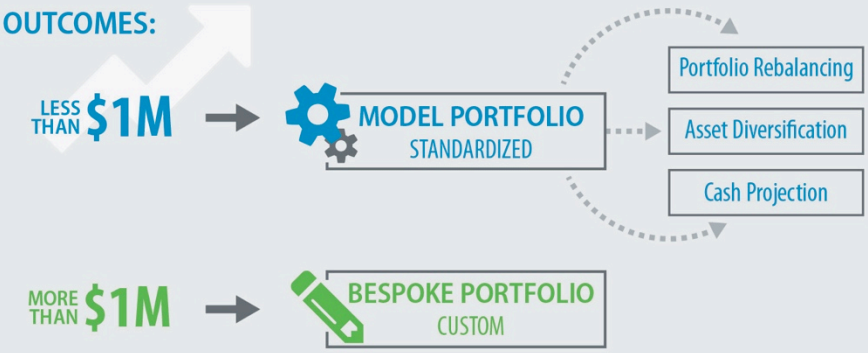
ACTIONS:

Lombardy Bank designed a more efficient investment process by building standardized models for smaller accounts (less than $1 million in assets).

Automation replaced processes that were formerly completely manual.

The bank continues to provide customized/bespoke portfolio management for accounts larger than $1 million in assets.

OUTCOMES:



HOW IT WORKS:

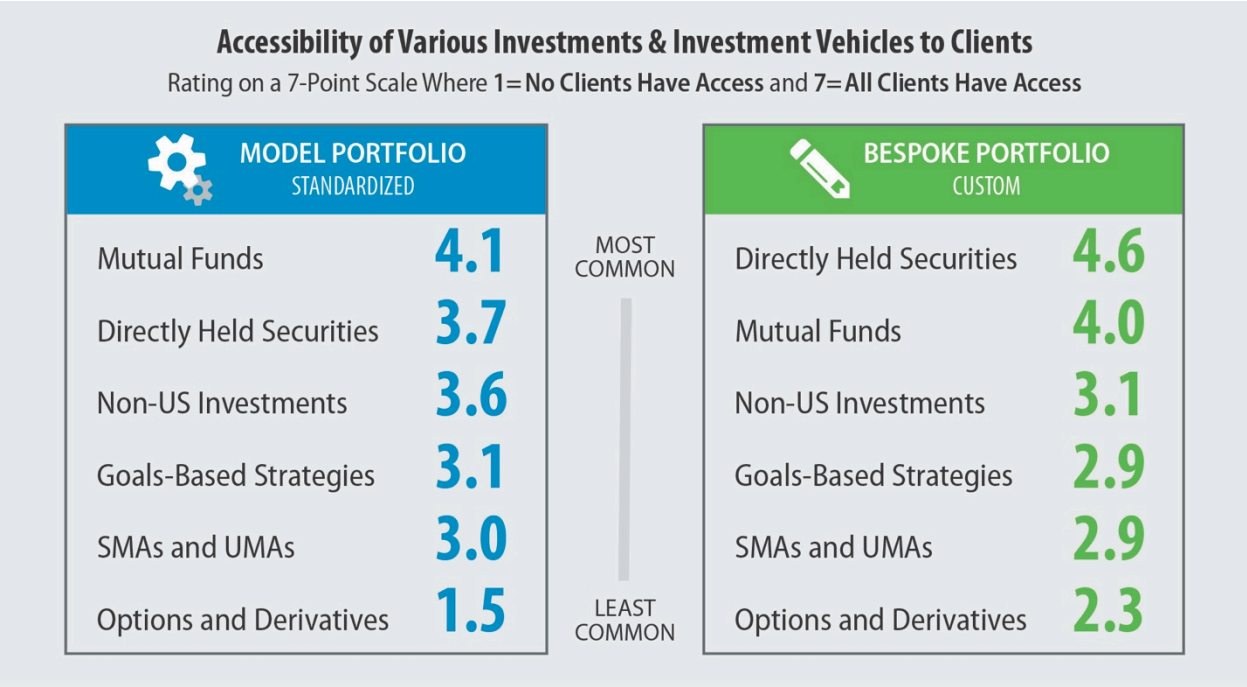
The bank's investment models are fully automated, including asset allocation and diversification.

The models can also auto-rebalance and raise cash in anticipation of distributions and overdrafts.

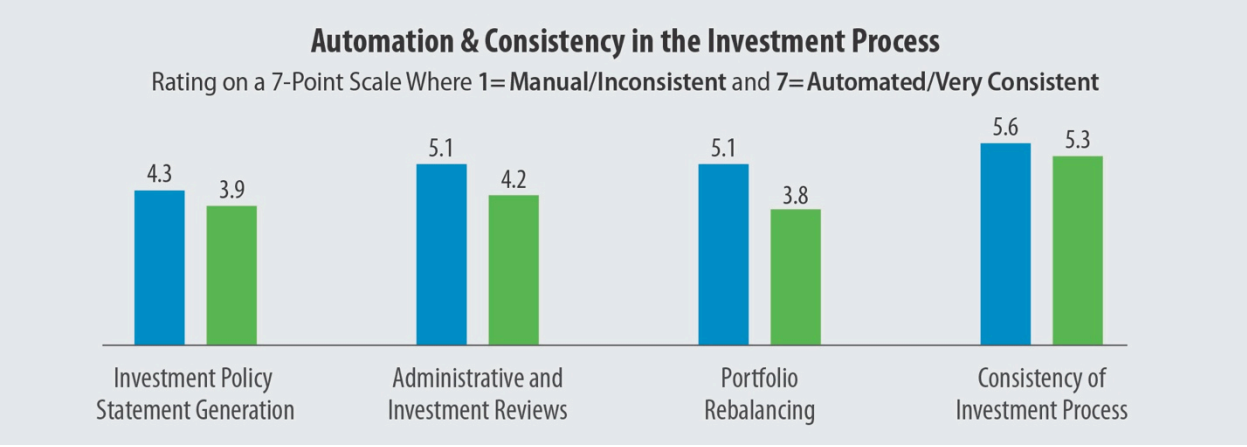
The approach implemented by Lombardy Bank mirrors industry wide patterns. Standard models and automation are much more likely to characterize the service approach for smaller clients. Firms that primarily use standard models in their investment process serve clients that, on average, are nearly one-third smaller than those of firms that deliver customized portfolio management.

	MODEL PORTFOLIO STANDARDIZED	BESPOKE PORTFOLIO CUSTOM
Average Client Relationship Size ($000s)	$2,657	$4,686
Average Investment Mgmt. Account Size ($000s)	$1,353	$1,660
Average Personal Trust Account Size ($000s)	$877	$1,136
Percent of Assets Managed Internally	92.5%	99.5%

The use of models supports higher levels of automation and greater service consistency, one of the paramount shared goals in client service and efficiency initiatives.



By at least a small margin, firms that primarily deploy standard models report higher degrees of automation in the way they generate investment policy statements, conduct administrative and investment reviews, and rebalance portfolios. They are similarly more likely to describe their investment approach as consistent across client relationships.



If anything, the use of models is likely to become more commonplace, especially since the benefits—cost and standardization—don't necessarily imply lower quality. It is already the case that newer technologies are able to automate more sophisticated and complex models, and deliver increased capabilities beyond what's typical of traditional mutual fund models.

Conclusion

Faced with seemingly irreconcilable demands, “fight” or “flight” seem like perfectly reasonable coping mechanisms. Our vote, however, is in favor of a third option, one congruent with the idea of ‘building the new’.

"The secret of change is to focus all of your energy, not on fighting the old, but on building the new."

CONCLUSION

In wealth management these days, there seems like an awful lot of old foes to fight against: a challenging investment environment, rising regulatory costs, aging clients, and ever-evolving service expectations.

Inside their own firms, managers must find ways to grow revenues without spending a lot of money. They must grow efficiently, even though growth—so often fueled and supported by hiring—is expensive. Faced with seemingly irreconcilable demands, "fight" or "flight" seem like perfectly reasonable coping mechanisms.

Our vote, however, is in favor of a third option, one congruent with the idea of 'building the new'; one that reconciles the irreconcilable. That option is to invest anew in supporting the industry's most valuable resources: its relationship managers and sales officers. In practical terms, this means investing in their productivity, in cutting back administrative work, eliminating manual processes, reducing coordination costs, upgrading old technol-ogy, and giving them time back in their days—and then holding them accountable for better service and sales outcomes.

Attaining higher levels of productivity—attaining a new frontier—involves a variety of tactical and foundational changes: streamlining sales and service processes; centralizing lower-value sales and servicing tasks; developing a plan for small accounts; adding administrative and client service support resources. Each of these changes, of course, is enhanced by effective deployment of technology. In so doing, firms are "building the new": stronger, more flexible business models well-suited to competing demands of the market.

1 Millman, Dan. "Way of the Peaceful Warrior: A Book That Changes Lives", HJ Kramer, April 2006

WISE is a Washington, DC-based research and advisory services firm that uses high-quality data and research to provide wealth managers with affordable, customized insight about their business. Our team believes that wealth managers and trust companies deserve the type of high-quality data and insight that are increasingly common elsewhere in the economy—especially regarding growth, sales, pricing, staff productivity, and profitability. WISE's member community is comprised of industry-leading firms, ranging in size from large national banks to super-regional and community banks.

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