How asset managers can transform distribution

The traditional distribution model for asset managers—selling "wholesale" to financial advisors who sell investment products to their clients—needs to evolve. Because of fee compression, it needs to be more efficient. And because of changing expectations of advisors and investors, it needs to deliver new levels of service.

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Introduction

An array of market forces are conspiring to compress fees and margins in the asset management industry. At the same time, the financial advisors that asset managers count on to sell their products are under pressure to provide higher levels of service to their customers.

As a result, the wholesale model needs to be updated. In this paper we show top asset-management leaders how data-driven approaches to marketing, sales, and service can bring distribution into the 21st century and help them compete in a challenging environment.

The complex B2B2C dance of wholesaling continues, with asset managers marketing mutual funds and other vehicles to financial advisors, who then sell products to investors. But distribution can no longer be regarded simply as a means to get products to the market, but rather an essential channel to support the financial advisors who are the gateway to end investors.

There are four main catalysts driving this change:

1. Shelf space continues to shrink at wirehouses and other wealth management firms
2. Investor demands are changing the advisor's value proposition, reducing the role of product selection
3. Both financial advisors and investors want simpler, on-demand guidance and education
4. Demographic shifts—aging and the rise of millennials—are challenging the advisor business

In addition to these forces, downward pressure on fees mandates increased operational efficiency across the value chain, including wholesale distribution. We believe that, rather than making incremental changes, winners will transform their distribution model with data and technology. They will use data-driven processes to make wholesaling more efficient and provide a higher level of service to financial advisors and their customers.

The new data-driven distribution model will be built on three major improvements:

1. Optimized marketing using multi channel experiences and data-driven campaign recommendations
2. Optimized sales that prioritize customers by value through micro-segmentation
3. Optimized advisor services to deepen relationships with both advisors and investors

Finally, the shift to this data-driven approach also has implications for asset-management organizations.

Companies will need to:

1. Develop a clear vision for an operating model to deliver data-driven marketing, sales, and support
2. Develop a talent management strategy that doubles down on data and technological capabilities
3. Build agility to rapidly prototype new solutions and bring them to market

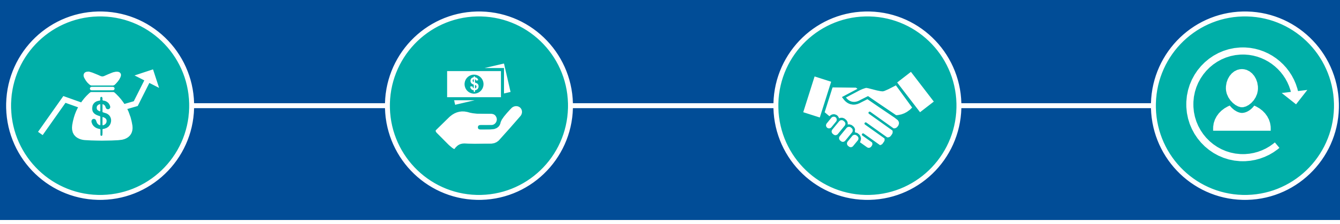
[1] In this paper, we focus on the distribution challenges relating to selling investment products via registered representatives, registered investment advisors (RIAs) and other financial advisors who serve retail investors, and not on distribution challenges in selling to institutions, defined-benefit plans, chief investment officers, family offices, etc.

[2] According to the SEC, "There are approximately 7,600 investment advisors registered with the SEC that serve retail investors, with over $12 trillion in retail client assets under management, and approximately 34 million clients.

The case for change

Changes to the distribution model are rooted in the trends that are shaping the new wealth manager and rewired investor of the future. New distribution models should focus on addressing the needs of a new world.

Funds struggle for shelf space	Shifting financial advisor value proposition	Changing expectations of financial advisors and investors	Demographic shifts among financial advisors and investors



Fund's struggle for shelf space

Wirehouses and other wealth management firms are constantly rationalizing investment catalogs in an effort to reduce the number of funds advisors offer to investors.[3] They are motivated to eliminate funds or share classes that may charge high fees but offer limited returns, as well as to increase their leverage over the asset managers on their platforms. Nearly one-third of broker-dealers have cut the number of funds available to advisors by at least 10 percent.[4]

In addition, large wealth managers are increasing their focus on centralized fund due diligence to remove fund managers with limited track records or those deemed to be underperforming benchmarks and/or peer groups.

Morgan Stanley, for example, reduced the number of mutual funds available on its platform from about 3,000 in December 2016 to approximately 2,300 in May 2017. The firm also encourages its advisors to use about 650 "focus" funds across a variety of strategies. Merrill and Ameriprise have recently taken similar actions.[5] We expect this trend to continue as firms prepare for Regulation Best Interest, which requires advisors to show that they are recommending investments that are in the client's best interest.[6] This puts additional pressure on firms to make sure that advisors do not recommend underperforming funds that could trigger legal action under the new standard.

Shifting financial advisor value proposition

Wealth management clients are demanding more comprehensive financial advice that goes beyond traditional asset appreciation into topics such as goals-based investing or cash-flow planning, estate planning, charitable giving strategies, and tax minimization. Many financial advisors are also utilizing behavioral economics to better help clients achieve financial goals.

This move from selling investments to providing financial advice has helped accelerate use of managed accounts. Instead of paying commissions and sales fees, clients are typically charged a wrap fee based on assets under management (AUM). These vehicles, which are often managed by the home office or a third party, have grown by 280 percent over the past ten years.[7] Managed accounts tend to limit the advisor's discretion to recommend specific funds; this has altered customer interactions from being transactional in nature—selling a fund—to more relationship-based. And because compensation is tied to growing client assets, the advisor is incented to retain clients and increase the value of their portfolios.

[3] Alex Steger, "Morgan Stanley kicks off next phase of fund cuts, ups gatekeeper coverage," Professional Buyer CityWire, January 26, 2018.

[4] Ignites Research, The Responsive Sales Staff, December 2018.

[5] Alex Steger, "Morgan Stanley kicks off next phase of fund cuts, ups gatekeeper coverage," Professional Buyer CityWire, January 26, 2018.

[6] SEC Regulation Best Interest (Reg BI)

[7] Sandler O'Neill + Partners, 2018 Asset Manager Transaction Review & 2019 Forecast, January 29, 2019.

Changing expectations of financial advisors and investors

Similar to the fee compression seen in the asset management industry, financial advisors are also experiencing secular downward pressure on fees and margins. Yet, with more internal functions to perform (such as providing Reg. BI forms to clients) and leaner support staffs, advisors have little bandwidth for building portfolios and selecting specific funds. As a result, many financial advisors are simplifying their lives by using a small list of funds to recommend to clients. This changes the relationship with wholesalers—increasingly, advisors look to wholesalers they deal with to be consultative experts who can explain how a particular fund can help clients achieve investment objectives.

Retail investors, meanwhile, have become more focused on outcomes than benchmarks, rewarding managers for helping them to achieve personal financial goals rather than just asset appreciation. As a result, there is increased pressure on asset managers to provide insights into how specific fund recommendations impact the balance of risk and return best suited for achieving a client's financial goals. Asset managers that effectively impart cogent advice via the wholesale channel on topics such as expected return, volatility and diversification stand to gain market share.

Demographic shifts among financial advisors and investors

The average age of a financial advisor is 55 and approximately one-fifth of advisors are 65 or older.[8] Nearly 40 percent of advisors plan to retire in the next 10 years, potentially putting $8 trillion of client assets in motion and disrupting longstanding relationships between asset managers and financial advisors.[9] As millennials displace baby boomers as the largest age demographic in the US, with the oldest members of the cohort entering their prime earning years, it will be critical for both asset managers and advisors and to understand and respond to their needs and preferences.[10]

More than other cohorts, millennial investors show interest in impact investing and funds that meet environmental, social, and governance (ESG) or socially responsible investing (SRI) criteria. According to Morgan Stanley, 86 percent of high-net-worth millennials are interested in sustainable investing.[11] Therefore, providing fund lineups that cater to the new generation and using the financial advisor channel to convey the merits of these funds are critical to remaining relevant and capturing money in motion.

Furthermore, investors increasingly expect access to private equity, private credit, commercial real estate, hedge funds and other asset classes traditionally reserved for ultra-high-net-worth or institutional investors. The explosion in non-traded alternative funds has democratized access to these historically inaccessible asset classes. Distributors must be able to articulate the value of these alternative strategies within the context of a diversified portfolio for financial advisors.

[8] "Firms try to attract and retain tomorrow's advisors," cnbc.com, June 25, 2019.

[9] Richard Frye, "Millennials projected to overtake Baby Boomers as America's largest generation," Pew Research Center, March 2018.

[10] The Managed Account industry now represents almost $2 trillion in assets under management (AUM) in the United States, a 280% increase over the past 10 years. Emily Gamble Bush-Brown, "The Separately Managed Account Opportunity for ADR Issuers," bnymellon.com, August 2019.

[11] Sustainable Signals: New Data from the Individual Investor, Morgan Stanley Institute for Sustainable Investing, 2017

The way forward: data-driven distribution

Data analytics is central to innovation in distribution, helping improve performance, minimize operational costs, and enable tailored marketing and better-targeted sales. The ability to quickly extract insights from a variety of structured and unstructured data has opened new opportunities for asset managers to engage with advisors and offer increasingly personalized service. While most asset managers already recognize that data analytics can sharpen decision making and streamline tasks and processes across the business, few firms have committed to the transformational changes necessary to use analytics on the scale required to significantly boost performance in distribution.

The transformation of wholesale distribution requires three initiatives to build data-driven marketing, sales, and service. It also requires organizational changes, including an updated operating model and new talent and capabilities.

Use multiple contact channels

Rely more on direct-response systems

Use data-driven campaign recommendations

Optimize marketing: use digital channels to customize messaging and adopt data-driven campaign recommendations

Marketing optimization starts with obtaining insight into the best ways to approach potential customers, then creates tailored journeys to reach them. Through channel optimization, direct-response systems and data-driven campaign recommendations, this approach improves both cost-to-distribute and cost-to-serve, increasing marketing effectiveness for asset managers and financial advisors.

Use multiple contact channels

Traditionally, asset managers have used a single-channel approach to target particular advisors. In the new data-driven world that no longer suffices: financial advisors move across channels searching for products and information. Financial advisors expect to interact digitally, though a contact center, or in-person with wholesalers and receive a consistent and insightful experience regardless of channel. An integrated multichannel strategy can help manage customer interactions across the distribution journey and tailor interactions for each financial advisor, according to behavior and channel preferences.

Rely more on direct-response systems

Asset managers should build digital self-service experiences that provide quick and thorough answers to financial advisor questions and requests, via computer and smartphone. This has the dual benefit of improving financial advisor satisfaction through faster response time and lowering costs for asset managers through call avoidance. In addition, online direct-response systems collect valuable data, including the profiles of clients that financial advisors serve and asset class or vehicle preferences. Insights from such data can be used to generate highly personalized recommendations and marketing messages to drive adoption. Using analytical capabilities, asset managers can routinely reach out to advisors with information and content they know the advisors will find useful, leading to the development of new prospects and deepening existing relationships.

Use data-driven campaign recommendations

By analyzing historical data, asset managers can develop campaigns that match the needs of advisors with product features. Predictive analytics can enable asset managers to optimize campaigns for specific types of advisors, based on the types of practices they run, their purchasing history, and behavior. To measure the performance of these campaigns, analytics can identify which channels or touchpoints should be credited with sales or conversions. Outputs of analytics engines allow distributors to segment, analyze, and mine additional client data. This can enable rapid adjustments to campaigns in order to optimize spending through the most effective mix of media channels, and advisor segments. Data analytics can also help gauge the impact of creative material.

Optimize sales: prioritize customers by value through micro-segmentation

Wholesaling can be costly and inefficient because of the way sales resources are deployed—or, all too often, mis-deployed. Using a data-driven approach, asset managers can make informed decisions about which advisors warrant dedicated face time and which can be served through lower cost interactions.

Use micro-segmentation when targeting advisors

Traditionally, asset managers have segmented their target advisor populations by sales, AUM, channel, territory or some combination of these criteria. Micro-segmentation uses advanced analytical techniques to comb through a broad range of attributes from a wide variety of sources, such as CRM systems, meeting notes, and external demographic or geographic data. This enables asset managers to segment advisors by business models, investment approaches, and clients. Financial advisors will typically share overall book sizes, but not details about investors. This means that managers must rely heavily on external data sources to develop insights about the needs and preferences of the advisors' clients to drive impactful segmentation techniques. Micro-segmentation helps asset managers identify those most likely—and least likely—to buy particular products so that marketing and sales resources can focus their energies on the pursuits that can be best monetized.

Prioritize advisors to drive revenue opportunities

By combining internal and external data sources to develop micro-segmented views of their financial advisor clients, asset managers can develop ranking methodologies to prioritize the advisors most likely to drive revenue opportunities. Using historical data, analytics systems can recommend up-to-date talking points for a meeting and give prompts on next steps and channel preference. This yields a cost-effective "tiered" coverage model that prioritizes financial advisors based on potential to generate revenue. Then, through desired contact method (from in-person to remote to digital), product preference or geographic location, with higher-touch services dedicated to the most impactful revenue opportunities.

Sales management can also determine the overall level of outreach needed for each financial advisor based on customer value, type of practice and book, and preferences. Through smart use of data analytics, we believe wholesalers can dramatically improve call planning for wholesale reps and arm them with a list of follow-up activities to help close. Data-driven planning will also yield cost savings and margin improvements by focusing expensive face-to-face interactions on the advisors who have the greatest revenue potential.

Making the mobile connection

To digitize and hyper-personalize interactions with its financial advisors, an asset manager developed a mobile platform to offer free value-added services and increase digital engagement. By capturing data about interactions with the mobile app, the asset manager achieved a higher level of understanding of its customers and was able to craft personalized and highly-targeted marketing campaigns. Data from the app also gave the sales team insights about the customer and highlighted opportunity areas to target for further engagement and potential sales.

In the first months of deployment, the company measured success through adoption rates and engagement:

- The app was adopted by 100 percent of the pilot group
- The app was adopted by 70 percent of the initial release group
- Engagement was up 60 percent among app users and sales by the most highly engaged reps jumped 350 percent

Optimize service

Data-driven approaches can deepen relationships with advisors and investors through personalized services and interactions. By providing relevant, personalized content online, asset managers can provide targeted guidance and insights into the products that each financial advisor is apt to utilize. The result: responsiveness and quality of customer service go up, while distribution costs go down.

Personalize service

Asset managers can develop a personalized approach to customer service, based on the advisor's previous interactions, products the advisor handles, assets under management and types of investors served. Data analytics can be used in both online and offline channels to impart product-specific insights to financial advisors quickly and effectively. Personalized interactions can better drive adoption and facilitate understanding of how investment products can help the client achieve stated and unstated goals of returns, volatility and diversification. They can also better address the needs of financial advisors who are increasingly focusing their energies on planning rather than portfolio management. Personalization extends to the call center as well, where intelligent systems – offering tailored rather than canned responses – empower call center agents to be far more productive and provide better service.

Make content available on demand

Intelligent direct-response systems can handle routine questions and service requests efficiently and effectively, saving the financial advisor time and improving responsiveness. Armed with data about the financial advisor visiting the website, the system can proactively offer relevant content based on the products the advisor is selling and the profile of the advisor's clients, rather than solely offering content reactively.

Interactive platform increases coverage and wins

A top global asset manager wanted to enhance salesforce effectiveness and invested in the development of an interactive, guided selling platform. The platform directed wholesalers to financial advisors who were most likely to use its various products and also provided insights about how and when to approach them.

Drawing on a database of more than 3,000 attributes, the data analytics team broke the sales cycle into three stages--pre-meeting, during-meeting, and post-meeting--and developed a solution for each stage. It built a recommendation engine that provided wholesalers with specific product recommendations to discuss with each financial advisor contacted. The system also fed real-time sales insights to wholesalers to use when discussing products with financial advisors.

To deploy the platform, the company used a test-and-learn approach, measuring performance against a control group and making refinements as needed. The platform also captured meeting notes and tracked the effectiveness of recommendations, helping refine future recommendations for that advisor and similar advisors.

In the first months of deployment, the company saw the following concrete improvements:

- The average number of meetings per advisor rose to 5.2 per week compared with 3.5 in the control group
- The test group marked four to five opportunities as won per week, compared with two to four for the control group
- The average number of days for opportunities outstanding declined for the test group
- The number of advisors covered in the test group's territories was 25 percent higher than the control group

Get ready: Organizational changes to enable data-driven distribution

Initiatives to optimize marketing, sales and customer service using data will require investment and changes in how asset managers structure and operate their distribution teams and overall business. While incremental investments in a modernized distribution business can yield benefits, we believe that organizational transformation is necessary to fully realize the benefits of the new data-centric model. Enabling this transformation journey requires asset managers to develop a clear vision of the future state operating model. This includes a talent strategy that doubles-down on data-centricity and the agility to rapidly prototype new solutions and bring them to market.

Develop a clear vision of the new operating model

Developing a new distribution model requires the breaking down of functional barriers. Cross-functional teams – representing product, sales, service, marketing, data management, analytics, and technology – will need to operate in unison to develop a clear vision of a modernized distribution model. Refocusing from channel-centric journeys to client-centric journeys, asset managers will organize teams to focus on specific client needs. To develop an operating model that supports a data-centric distribution model will require collaborative cross-functional teams to address issues ranging from customer segmentation and persona mapping to specialist vs. generalist models.

Assemble talent with data and technology expertise

It will require new kinds of talent for asset management distribution to move quickly to data-driven approaches to marketing, sales, and service. While asset managers typically have advanced technology expertise in their investment functions, most lack capabilities in specialties needed for the new advisor-distribution model, such as behavioral analytics and cross-channel interaction models. Almost all asset managers have begun to add personnel with a software development background, but they also need talent in data analytics and data science, as well as digital marketers who can optimize distribution. This model also requires new cost and compensation structures, and asset managers will face trade-offs between investment costs and scale benefits.

Build the ability to rapidly prototype new solutions and bring them to market

It's not enough to have big plans for data-driven processes and invest in the people to design the systems. To transform the distribution system and remain competitive, asset managers will need to become agile innovators. This means creating an environment that fosters experimentation and continuous improvement, using the iterative model of agile development: rapid piloting, test-and-learn, and revise. Using iterative, incremental releases, asset managers can turn analytical insights into reliable distribution journeys. This change in approach is not easy and requires management buy-in. Agile development organizes work around collaborative, cross-functional teams. And traditional metrics, such as hitting project milestones, are replaced with KPIs that focus on outcomes, such as customer engagement, time-to-market, and adaptability.

How KPMG can help

KPMG's Wealth and Asset Management Strategy practice helps asset managers increase the agility, efficiency and effectiveness of their wholesale distribution models. We work with managers, wirehouses, bank broker-dealers, top independent wealth managers, insurance wealth managers and wealth tech firms. Our professionals bring deep wealth management experience and a hands-on understanding of the asset management ecosystem. Our engagement teams include strategists, data analysts, and quantitative/agile developers dedicated to helping clients digitally transform their businesses.

We can assist your organization in creating a data-driven distribution function through the following services:

Assess the performance of your current distribution approach in articulating value propositions, choosing channels, driving engagement, attracting and retaining customers, and obtaining platform representation of products

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Assess the current state of the organization and establish a target state distribution model; define requirements for functional team structures, skills development, and compensation structures

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Advise on an execution strategy that includes refining your distribution channel approach, building a cost-effective coverage model, and providing analytics-based product recommendations to advisors

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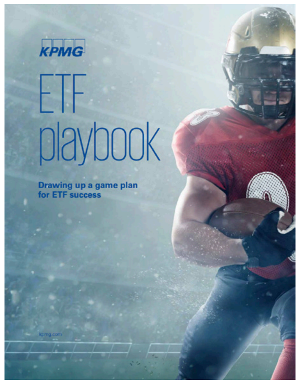

ETF playbook

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