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Strategy & Marketing Consultants

Pricing for Growth in Wealth Management

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The wealth management industry is on the cusp of a big change. How quickly it happens depends on those prepared to innovate.

This has implications for the proposition and how it is structured, how we charge for value, and how we persuade clients that the value is worth the price.

In this document, we cover all three topics using insights we have gained from other industries facing disruption, increased competition and pricing pressure.

Given technology, regulation and changing client behavior, the need for innovation is likely to be ongoing. Those who move first are likely to remain ahead of the curve.

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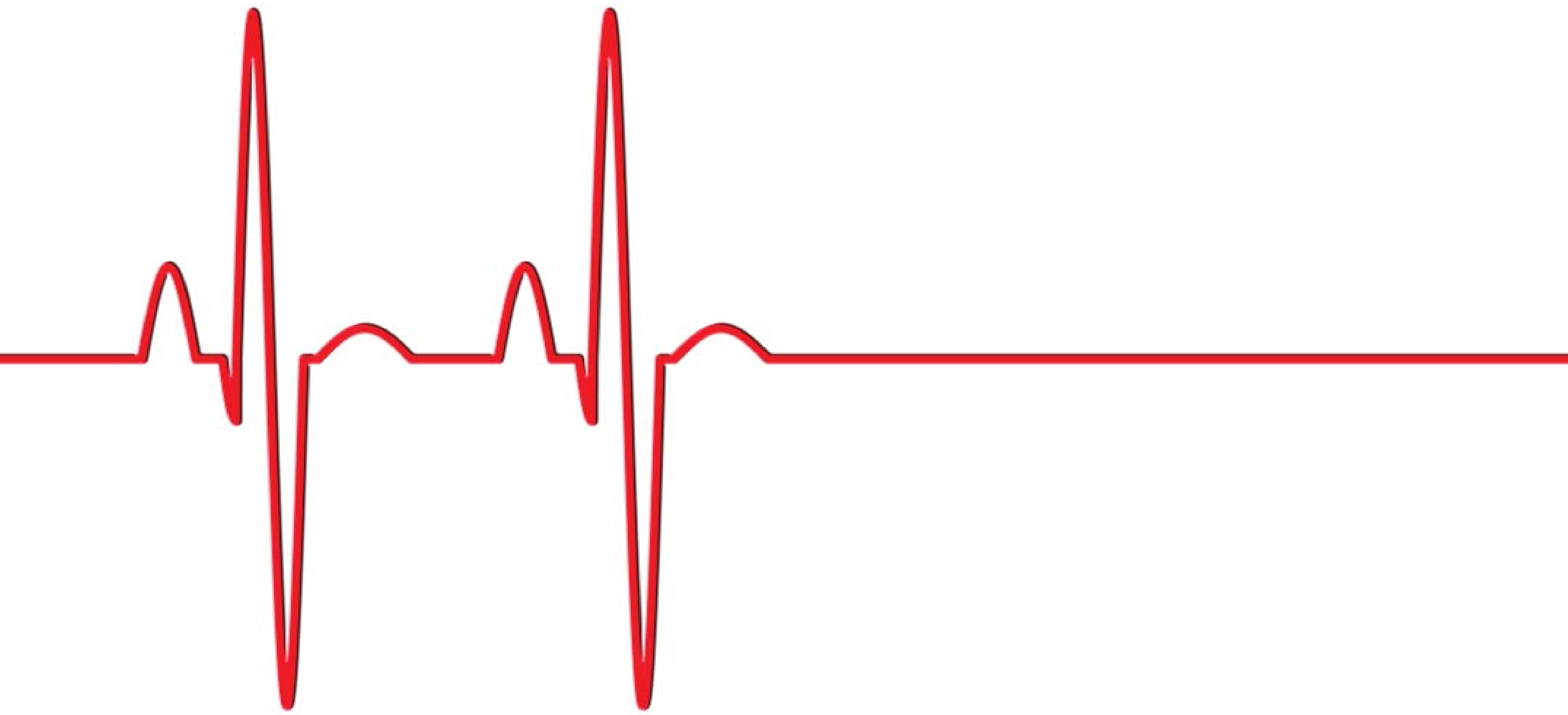
Chapter 1

What Future for Wealth Advisory? The Choice Is Yours



There is a fundamental problem facing wealth advisors - be they fee-only, commission-based, hybrid or banks.

Happily - there is one common solution.

We are all familiar with this solution, because other industries have been doing it successfully for many years.

Take the car industry as an example. It does not market 'a car', but different models and different prices.

What if wealth managers sold cars?

Welcome

Here at XYZ Motors, we take your automotive conveyance needs seriously. Our expert staff are pleased to offer a holistic value-based proposition that is tailored to your personal transportation journey. Today, we know our clients expect to travel to a wide variety of destinations: some close by, some far away. We want to be your partner in achieving this goal.

Our offering

- Velocity Modulation Capability
- Internal / External Atmospheric Regulation
- Ignition Fulfilment Mechanism
- Motion Curtailment Enablers
- Illumination Intensifiers & Reductors
- Sendentary Comfort Enhancement
- Horizontal Movement Empowerment Facility
- ...

If the Wealth Management industry sold cars...

A differentiated line-up implicitly recognizes that customers have 1) different needs (e.g. young and cash-strapped vs. married with kids vs. mid-life crisis) 2) different abilities to pay.

Don't we recognize this in wealth management? The answer, to quote Nick Murray, is an unequivocal yes and no.

In practice, we do tailor services to customers as all are unique. The key difference, however, is the lack of choice.

Let the customer choose

Going back to cars: I can be a billionaire and drive a Tata Nano. Theoretically also, I can have modest savings and choose to divert all my resources into acquiring a Bentley.

But if a billionaire goes to a wealth manager, she will by and large, be assigned the maximum level of service that the wealth manager believes is affordable. The person with lower assets will in all likelihood be told to come back when he has more assets saved.

The problem here is that one customer is receiving service which incurs cost to the advisor but may not reflect her needs, while the other customer is receiving no service of any kind, despite being prepared to pay for it (one can have zero assets and a high monthly salary).

This is not capitalism at its efficient best.

Can’t we do the same thing?

		CLASSIC	ELEGANCE	AVANTGARDE
Mercedes	**C-class**			

What is getting in our way?

The problem is that the proposition is currently supply-side driven.

The advisor is thinking:

1: “What can I do?”

2: “What can I afford to give away?”

The important questions remain unasked and unanswered, namely

1: What does the customer want?

2: What is the customer willing to pay?

Of course, the ubiquitous all-in AuM fee goes part way to addressing them.

Most AuM clients have more complex needs; and most will pay more, which is why they are sought after.

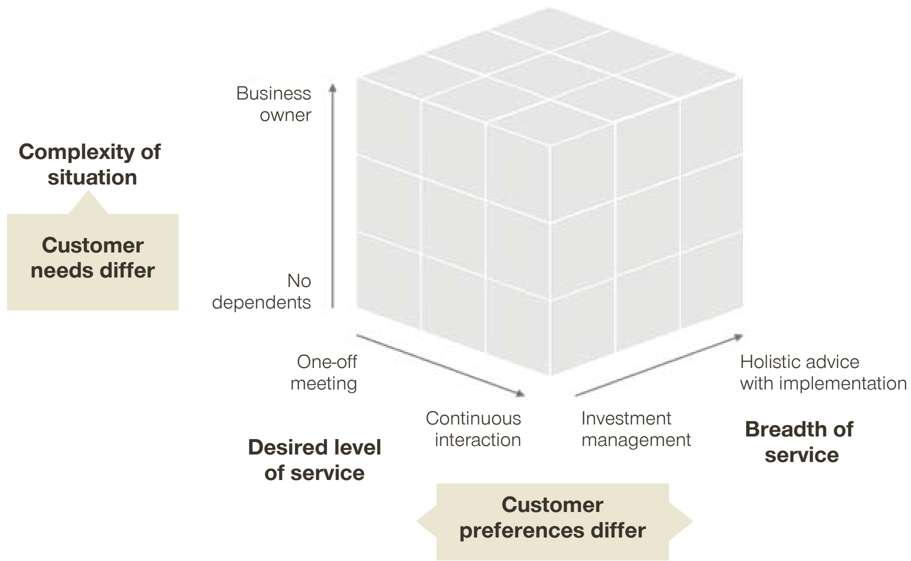
From a customer perspective, there are big problems in using AuM as a substitute for choice and substitute for willingness to pay.

We’ll address the second problem (and the shape of the solution), in the next article.

But first we should address the issue of choice, which comes down to needs and preferences.

Segmenting by needs and preference

For a segmentation that translates into a customer-centric offer, we need to look beyond age and assets. Below is an example framework.



Complexity

Customers differ along lines of **complexity** e.g. a) single person with no dependents versus b) business owner with two ex-spouses, a parent requiring ongoing medical treatment, and three children aged two, twelve and nineteen respectively.

The single person could be young **or** old, and have **more** assets than the business owner. Age and wealth are not reliable guides to complexity, in other words.

Level of service

Another way in which customers differ is in their **preference for interaction** with their advisor (level of service). Some may prefer minimal interaction, some frequent. Some may want to have phone access, some face to face, some may be content with email.

Once again, this is not dependent on AuM. Wealthy people are often too busy to attend face-to-face meetings. Gen X-ers are wealthier than Millennials, but have less time. As a result, they are equally likely to interact digitally, albeit through different channels, at different intervals and for longer durations.

Breadth of service

Finally, as we all know, customers differ in terms of their **requirements for advice** (breadth of service). The Wealthy Validator may require only financial planning help, preferring (at least initially) to hold assets elsewhere. Others will seek the full nine yards – holistic advice with implementation – from day one, while others require investment management only. People should have the choice.

So now what?

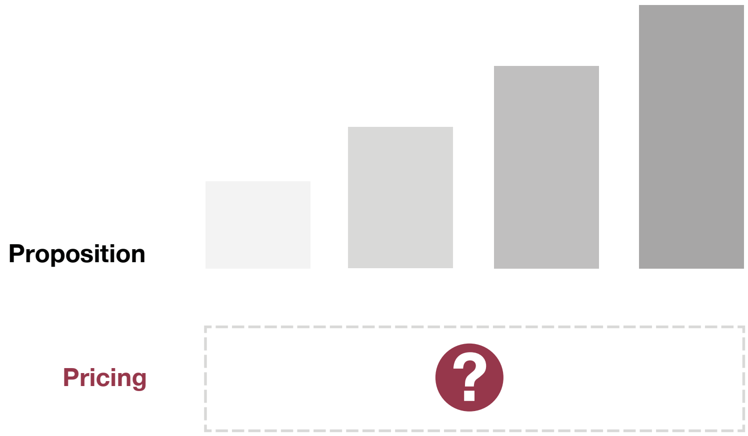
It is up to the advisor what to offer, but there should be an offer that meets the needs of each of their target segments. This will make it easier for a client to relate to the proposition in the first place, amid the sea of 'holistic solutions' - to say nothing of ending up with the service that they want.

Just as car manufacturers have different catalogs - some serving many segments (Honda / Infiniti) whereas others are niche-focused (Maserati) - the final line-up will differ from advisor to advisor.

There are some universal principles ('Leader + Filler - Killer') in designing effective packages which we have found can be reliably applied in any market.

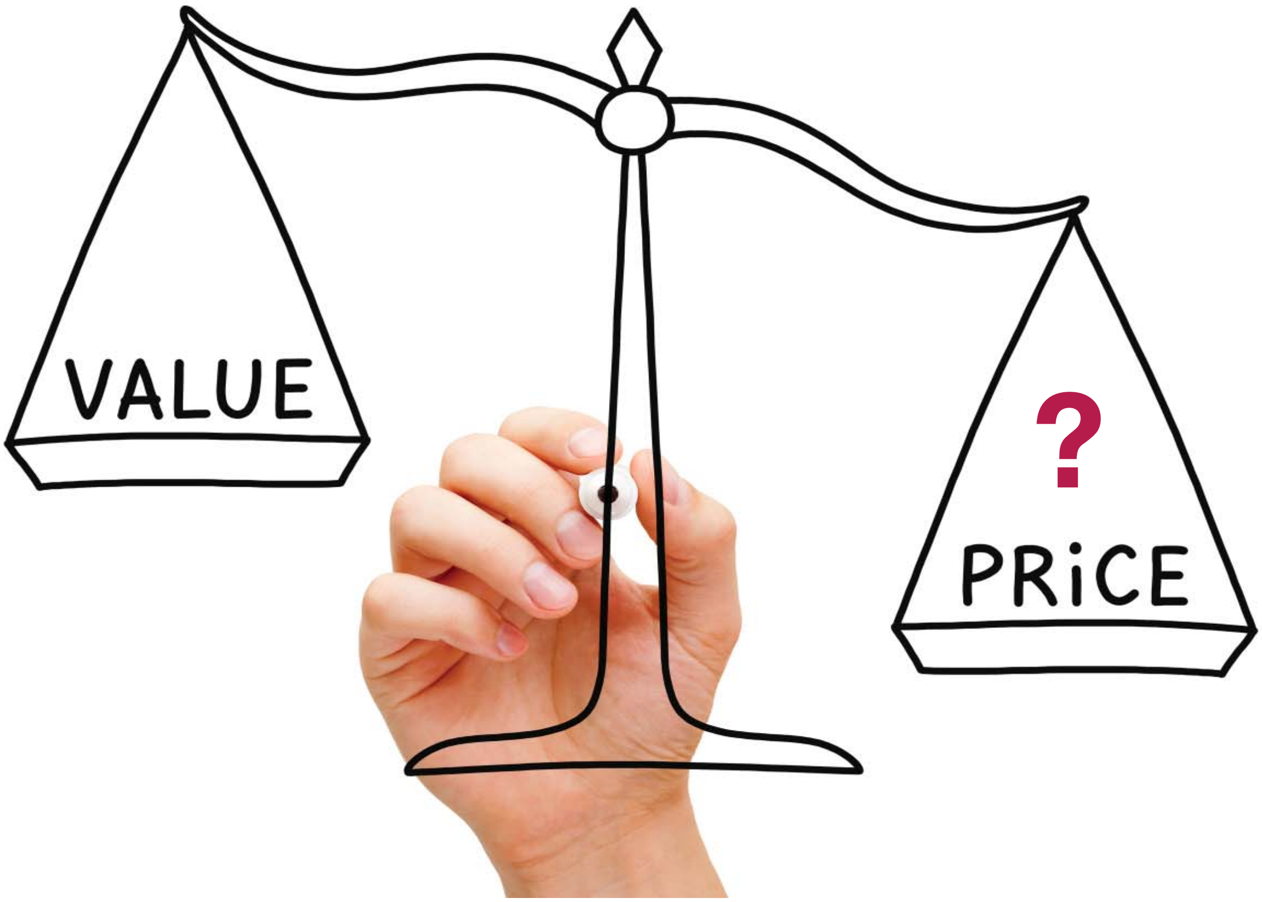
Most importantly, we have found that the success of any initiative will depend on starting with an analysis of customer needs - whether through surveys, focus groups or internal data.

Once you have designed the right offering (create value) the next step is to price it correctly (extract value), and finally to communicate it (defend value). These will be covered in chapters two and three.



Chapter 2

The Price is Wrong.
What Next for Wealth Advisory Fees?



Pricing is one of the hottest topics in wealth management at the moment. This has a lot to do with regulation, proposed or enacted (in both the US and Canada).

But regulation is only the catalyst for a change that is long overdue.

The 2016 Financial Performance Study released by IN Research revealed that only 2% of investment advisory firms employ 'value-based pricing', and 46% of firms do not charge additional fees for specific services.

By not charging fees, advisors (counter-intuitively) are locking out the very customers they need in order to grow, as well as sacrificing profitable growth that is available today.

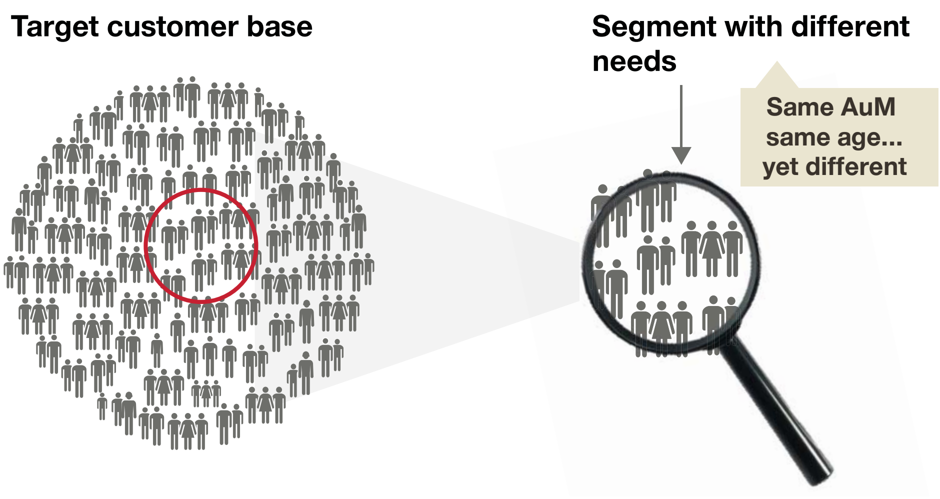
Smart pricing represents a big opportunity for firms who do it right. This article is the second in a series about how it can be done.

The need for Value-Based Pricing

As we saw in part one, the beginning of any new proposition and pricing change should be a detailed analysis of customer needs and preferences - i.e. what customers value.

Why? Because when you analyze 'the customer', you realize that there is no such person. Different customer groups come into focus, with different needs and willingness to pay.

The value proposition should reflect this diversity, and so should the pricing model.

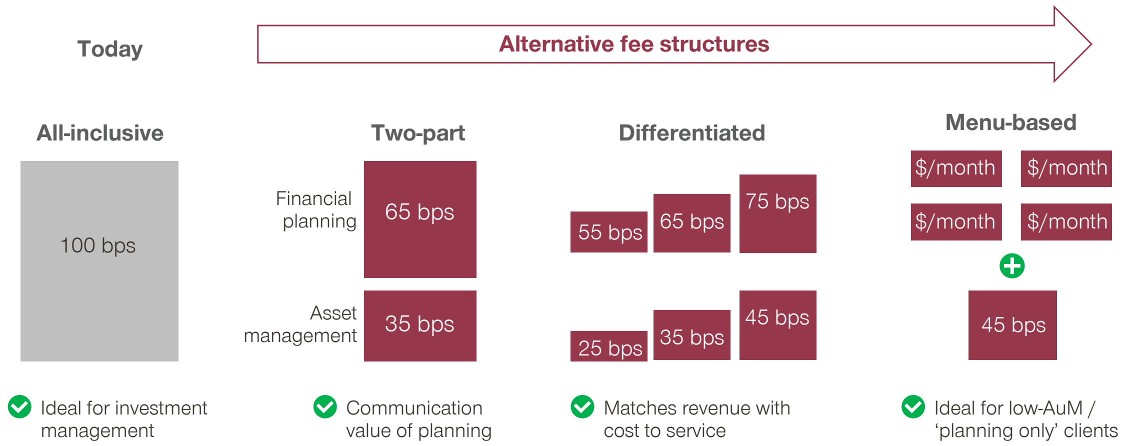


So what's on the menu?

In the ground-breaking report 'Fees at a Crossroads', SEI Advisors and Bob Veres make an eloquent case for evolving away from the trusty All-In AuM model, as well as setting out the alternatives.

The alternatives include **one-off fixed fees, periodic fixed fees**, and **hourly fees** (we exclude commissions and ticket-based fees – a can of worms for another day).

These building blocks can be mixed and matched to form a potentially limitless number of combinations.



There is no 'right' pricing model for the industry as a whole, but it should be possible to determine the 'right' pricing model for a given advisor.

Choosing your price model

As with everything, there are some general principles.

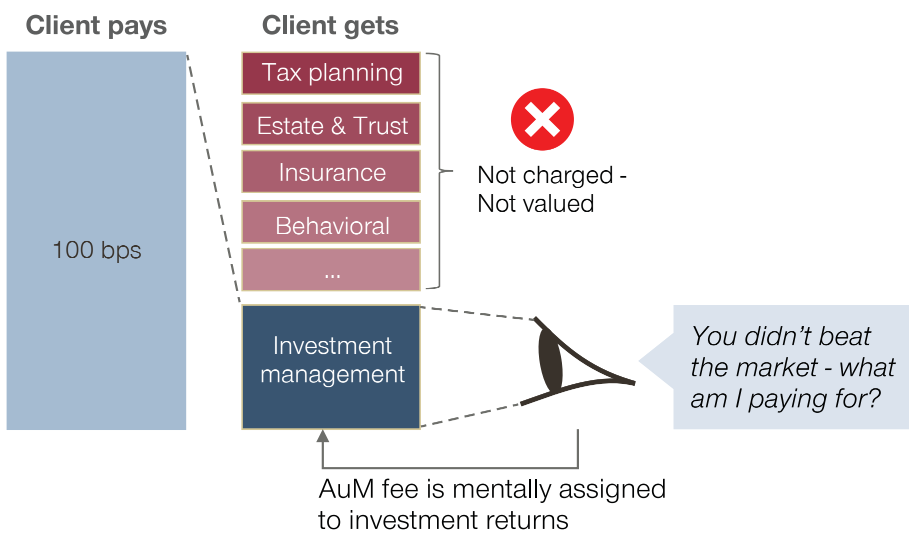
Before getting to these, we must again stress that the ultimate proof of any pudding is testing with customers.

We have learned from many years experience that this step is necessary whenever an organization is contemplating a pricing change, or any change to its offering. In fact the process never ends, as the customer base has an inconvenient way of changing its needs and preferences over time.

With this caveat in mind, we can make a first pass by thinking through the psychology of pricing.

Price metrics have different mental associations, meaning that they work well for some services but not others.

The AuM % fee, for example, is a psychologically frictionless way of charging and paying for investment management. But it is a very poor way to charge for up-front planning work.



Because up-front planning is – by nature – up-front, it is hard to justify charging the same amount in the second year, when the financial plan is unlikely to require the same amount of work.

How about ongoing planning advice, or the ability to contact the advisor with ad hoc inquiries? Surely this justifies a boost to the AuM fee?

Problem: clients will pay more according the amount of assets they have with the firm, not the amount of ongoing planning they require. As we saw in the last article, this is not a 1:1 correlation.

Clients would be, in effect, punished for bringing assets to the firm. Put another way, clients have a incentive to move assets to a lower-cost investment manager while still receiving the full benefits of ongoing planning advice.

What is the solution? Simply: link price to value.

Linking price to value: an example

One solution is the three-part fee – which reflects the three-part nature of the value offering.

Investment management = AuM % fee

Up-front planning = one-off fixed dollar fee

Ongoing advice = monthly or quarterly fixed fee

Just breaking out the value into three parts is valuable in itself. It communicates how the proposition differs from a lower cost provider.

Furthermore, clients who do not wish to receive a given service can deselect it.

This way the customer avoids the fee, and the advisor avoids the cost to serve for that particular service – a win-win that is not possible within the murky, ambiguous confines of the all-in fee.

Protect your existing base and build your future

But I don't want to nickel-and-dime my most profitable clients!" you might say.

Not a problem. Higher AuM clients can (if they wish) continue with their existing model. But - and here is the good part - you can now let them know that the fixed fees have been waived thanks to their loyalty and valued status.

Loss aversion (=dislike of fees) is a deep human instinct. We have seen in other cases that waiving fees turns the table on loss aversion and reinforces the client relationship.

Waiving fixed fees for high-AuM clients will have a minimal effect on profitability, but a powerful effect on customer loyalty. Apart from anything else, it provides an incentive for them to keep their AuM balances high.

As well as being a **retention** measure, fixed fees are also an important **acquisition** measure.

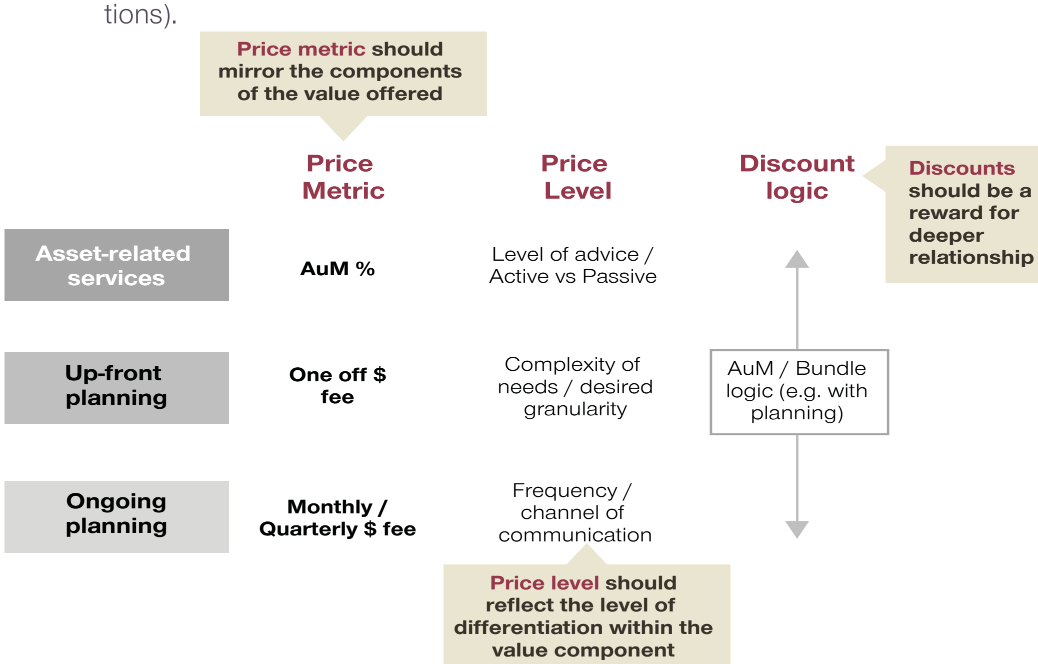
For wealth managers looking to grow outside the traditional target market of older asset-rich clients, introducing fixed fees creates the possibility of accepting clients with low assets who would previously have been unprofitable.

The asset-poor customers of today will be the asset-rich clients of the future – and they will likely belong to the first advisor who will accept them.

Pricing structure is only the first step

The **price metric** is not the end of the story. Within a fee category, there can and should be different **price levels**, corresponding to the quantum of value delivered.

Discounts as well - if left to the individual advisor's discretion - can turn into a free-for-all with differing rules applied and little effect other than to deplete margins. Done correctly, discounts should have a **consistent** tit-for-tat logic, based on a deepening of the client relationship (e.g. commitment to higher contributions).



Is getting all of the above right a difficult procedure and fraught with risk?

You bet it is – particularly for larger institutions. In our experience, it can take anywhere from months to years, and as noted above, the process never ends once and for all.

With cumulative pressures of regulation, technology and competition, the choice is not whether to change, but when.

Viewed more positively, the return on all efforts in this direction will be profitable, sustainable growth.

Where next?

One of the great advantages of the all-in AuM fee was its simplicity. This simplicity is not reflective of the variegated nature of client needs and willingness to pay – and its day is over.

Which raises the next question: if the value proposition of the future involves choice for the customer and more nuanced pricing, how will advisors – let alone the customers themselves – cope with the additional complexity? Aren't things difficult enough to understand already?

They certainly are, and that is why **Presentment** is the final component in any proposition and pricing initiative.

More details in the next chapter.

Chapter 3

Wealth Advice that Sells Itself – Why Presentment Matters

Needs-based proposition: ✔ check.

Customer-tested pricing structure: ✔ check.

Mission accomplished? Not quite.

In fact, the final mile is typically where it all goes wrong.

The Problem

Introducing differentiated propositions with smart pricing models is the first step to profitable growth.

But: introducing differentiation (and choice) means potentially more complexity for customers.

Customers are confused enough already by *what* we offer, let alone the differences between offers. Isn't more choice going to make things worse?

Confusion leads many customers to default to the lowest price option. Cheap is a concept everyone understands.

What is not always understood is that lower price = lower value in the long run. Knowing this is the starting point for the solution.

What is our job in the 'final mile'?

There are ultimately 3 things the customer wants to know in an initial interaction:

1. What are the options?
2. Is there an option that meets my needs?
3. Is this option worth the money?

Go to your website or pull out your marketing materials, and imagine you are one of your target clients.

Can you answer the above questions in under 45 seconds? If not, you are in good company. So what can be done?

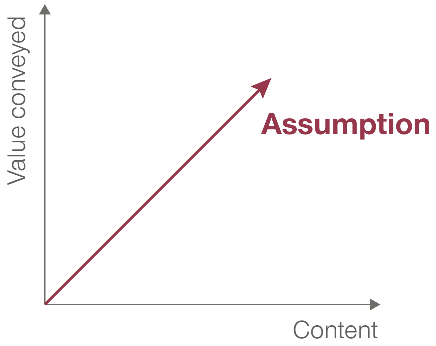
Here are three principles to address the three questions above.

Principle 1: Clarity – What are the options?

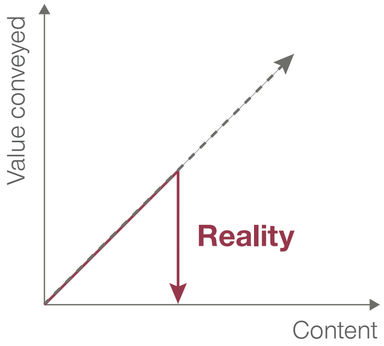
Clarity is primarily a question of visuals, or rather the *absence* of visuals.

Beyond a certain amount of information or visual content, the customer's understanding of a given page or screen does not decelerate or plateau - it goes to **zero**.

The implicit assumption...



But after crossing a certain cognitive threshold, more content = no value



Almost all visual communication materials today are to the **right** of the cliff edge.

Our current approach assumes that our customers have the time and energy to read through every paragraph carefully, with the tireless rigor of an academic researcher.

In this fantasy, the customer pieces together a picture of our entire offering, pausing occasionally to look up words and phrases such as 'cash flow modeling'.

After performing a similar analysis of our competitors, respective utilities are computed and our offer selected in the final step of a careful cost-benefit exercise.

Do such customers exist? In economic textbooks, you will find them on every page. But not in a whole lot of other places.

What we are writing on our websites is not only not being read by the majority of our customers, it is actually **preventing them** from making an informed decision.

Yes I know, I know. We are trying, with pictures and motifs and large fonts – but this is not good enough.

Not only are we still to the right of the cognitive cliff edge, but for younger consumers, the tipping point is moving further to the left.

What does cognitive ease look like?

That's what cognitive ease looks like. Why can't we be like this?

Obviously there are good reasons why we *aren't* like this. Visual noise tends to correlate positively with the number of stakeholders involved, which depends on the size of the organization.

Other than stakeholder politics, there is a perfectly good reason for the anxious parade of content: a valid fear that we may miss something important.

Google Search is differentiated by the quality of its algorithm. Surely, we might think as marketers, this message should be front and center? A simple explanation, perhaps, or some dramatic visual of an earnest group of scientists around a chalkboard?

We intuitively know this is wrong. Most google users neither appreciate nor care about the nuances of algorithm design. But they do know that when they use Google they tend to find stuff they want.

Google.com is devoted purely to facilitating that end. Period.

How can you be sure what customers care about? The only answer is to take the time to get to know the customer, design the page around the customer, and then test the results with the customer.

Principle 2: Coherence – Is there an option that meets my needs?

Let's assume that we have eliminated all visual noise, and clients can figure out basically what we are offering, in about 15 seconds.

Next question – is the offering right for them? If there are choices, which option is the right one?

If Clarity relates to how we display things (visuals), Coherence relates to how we describe things (words).

Feature rich, but value poor

Instant comprehension

"I need to optimize my risk management strategy" is a phrase that no potential client has said ever.

Why not do our clients a favor, and eliminate this and all similar expressions from client-facing materials.

No client is going to leave us because we are too easy to understand.

Not just plain English

A digital environment enables us to go one step further than this.

Discovery tools allow customers to narrow down or – better yet – tailor the offering that is right for them.

This is an alternative to presenting a comparison table with 15 different parameters, in order to explain how the 'Premium' differs from the 'Value Plus' package.

To avoid, rather than add, complexity in such a system, we must select the 1-3 trade-offs that really matter.

For example:

1. Services required: investment advice only, holistic planning
2. Frequency of interaction: yearly, quarterly, on-demand
3. Preferred channel: Email, Phone, Face-to-Face

If a customer indicates that she 1) wants planning advice only but has 2) limited needs and is 3) happy with remote channels, we can guide her instantly to a digital package with remote support from a junior planner at 150 dollars per month.

(This assumes the package in question is available and the price is right. See articles one and two for how to do this).

The transparency of a properly designed discovery process will not only delight the customer. It will also please the regulator, as the sales logic is recordable and clear to everyone involved.

Principle 3: Calibration – Is this option worth the money?

Interactive discovery tools or "navigators" also help with the final phase – price communication.

To get customers to buy-in, we need to give an indication of fees. Being coy on this topic is not a re-assuring sign.

Because price is a sensitive issue, we need to control how it is communicated. This is the reason fees have traditionally been communicated face to face.

But there is a better way.

We know this because, in literally hundreds of pricing and proposition transformation projects we have carried out, we have found that digital navigators are the best way to ensure that the price is communicated consistently and optimally. This applies in face-to-face and remote interactions.

What is the secret sauce?

Price discussions *only* go wrong when value drops out of the picture.

You can't decide whether 1 million dollars is too high or too low a price to pay for a painting, if all you know is the price. You first need to know who painted it.

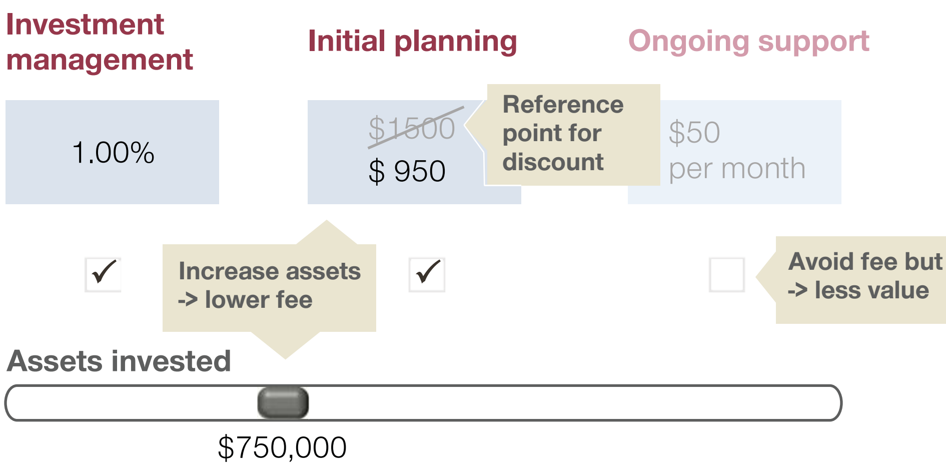
The failure to communicate value can happen in a face-to-face conversation if the advisor is having a bad day.

It can happen online if the price communication is mishandled.

It can happen in *any* context if the link between value and price is poorly conveyed.

It need never happen if the conversation is guided by digital architecture that is properly designed.

Here is a sketch of how a three-part model could be communicated to calibrate price with value.



The reality is that the process of design is slow and iterative, and requires the embedding of behavioral principles such as anchoring, loss aversion, endowment effect, priming and framing.

Finally, testing is required with the all-important stakeholders – the front-line advisor and the end-consumer.

Wrapping up

There are very few examples of presentment in wealth management that meet the demanding standards of the 3 principles outlined above. If you believe you know of any, or want to build one – we should talk.

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