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New ecosystems in wealth management and how clients will benefit

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A PwC Wealth Management Centre of Excellence Point of View Discussion Paper

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Executive summary

The looming paradigm shift

Wealth management is hurtling towards a moment of paradigm shift. Changing client behaviour, advancing technology, new competitors, shifting demographics and falling profit margins are combining to pressurise both the traditional universal banks and the boutique banks. Taken together, these factors mean that the industry cannot stay as it is. If it does not evolve, it runs the risk of losing existing clients and not gaining new ones. In addition, there is a growing potential for disruption by FinTechs or the tech giants, both of which are studying opportunities in a sector that remains a technology laggard.

A vision of the future

Our vision is that these pressures will lead to a platform-driven wealth management ecosystem, with several hyper-specialised providers. They will serve clients through digital platforms – the Airbnbs and Ubers of the wealth management world if you like. Digital interaction, backed by artificial intelligence (AI), will become the norm for some clients and fee structures will have to be amended accordingly. Consequently, we see two overarching client segments challenge the assets under management (AuM)-based categories: Local Affluents and Global Actives. Incumbent banks have a one-off opportunity to transform themselves into these platforms, securing a place at the core of wealth management. Alternatively, they might act as niche service providers on others' platforms – part of a new ecosystem.

Gains for clients

Clients will benefit significantly from this future ecosystem, as their needs will become the industry's priority. Service providers will become more specialised and, consequently, offer better knowledge of suitable investments, favourable lending solutions and how to navigate specific logistical challenges. Greater digitisation through use of AI will also simplify and improve services. And clients with complex international affairs will gain from a consolidation of all their complex activities into one, simplified overview on the digital platform. Overall, clients will benefit from a better range of products and services.

Obstacles to evolution

Naturally, such extensive change will not come without its challenges. There is the difficulty of regulations and tax laws differing from one country to another, the question of who takes responsibility for integrating the different service providers' offerings, the danger that platforms favour related service providers and the problem of individuals failing to comprehend and self-assess their risk appetites correctly. Finally, it will be hard to win clients' trust in a platform so powerful that it can access all their financial assets at once.

Time to change

Banks and wealth management firms have a simple choice. They can stay as they are and see profitability continue to fall. Or they can capitalise on rising demand for wealth management by becoming innovators – either as platform businesses or as specialists on other platforms. Regardless, action is required; the end of universal banking is near, and incumbents should prepare to transform themselves. While the need to prepare for tomorrow is urgent, the journey towards it can and will be gradual. We realise that implementing new business and operating models overnight is unrealistic. But firms should acknowledge the shape of the future, design a strategy, set out a timeline and plan the steps toward organisational change.

Prologue

Imagine a world where wealth management services are accessible at your clients' fingertips at any given moment; as integrated into daily life as social media apps. Where, instead of meeting with your relationship managers a few times a year, you can message them digitally at any time, view your financial situation in real time, and make adjustments whenever you like. Where, instead of being confined by the offerings of your bank, you choose your own bundle of individualised services from a variety of providers, onboard with new services instantaneously, and have all of them consolidated in one place.

You won't have to imagine much longer; the wealth management industry has set a radical course towards making just such a digital world reality.

In this report, we examine the current state of wealth management, discuss the developing trends and innovations (and suggest short-term responses), envision the future landscape, and touch upon some of the future's challenges.

While the current trends, such as shrinking profit margins, evolving client preferences, and new competitors, are certainly of great significance, the crux of the report is our longer-term vision for the future. We foresee an ecosystem where several, specialised, niche entities interact to provide wealth management services via digital networks and platforms that are totally transparent and exchangeable in seconds. A far cry from today's 'universal bank'-dominated industry, but a concept that we believe is likely to become a reality.

What this conclusion demands is a reaction from incumbent firms – sooner rather than later. Wealth management is lagging far behind other industries in terms of digitisation and client-centricity. Just as ridesharing companies all but conquered the taxi industry, and online retailers virtually replaced book stores, wealth management is inevitably due for a reshape. It's time to come to terms with tomorrow's reality.

1. Today's environment

And a peek into tomorrow's…

Currently, the leading players in wealth management are the 'universal banks', which operate at every part of the value chain, providing the full range of financial services. Besides the universal banks, there is a group of smaller and mid-sized boutique banks, for example Switzerland has a strong and established private banking industry. In recent years, there has been a wave of mergers as these banks have consolidated in a quest to increase scale and cut costs. However, in our view, this is a short-term solution that is inadequate to handle the impending evolution of wealth management.

It is peculiar that the wealth management sector has such a low adoption of digital technology. Throughout the entire client life cycle, wealth managers and their clients tend mainly to interact face-to-face. Yet it is obvious today that, in the long-term, no industry will be able to avoid the digital age.

Furthermore, soon a new generation of clients will materialise. At present, wealth management clients are predominantly male, and mostly baby-boomers (the wealthiest generation). As stated earlier, these clients are conventionally segmented based on investable assets. But as new, younger clients start to comprise a larger portion of the market, new ways to segment them will become more effective.

Wealth management has historically been a rapidly growing, and highly profitable, industry. As the number of wealthy households has continually increased, so the wealth management industry has fed on a constant stream of new business. However, increasing competition, higher regulation and several other changes that will be discussed later mean that profits are no longer as high as they once were.

In the conventional wealth management model, advisors push financial products to the clients. Increasingly, though, firms are shifting towards a life event-based, holistic advisory model.

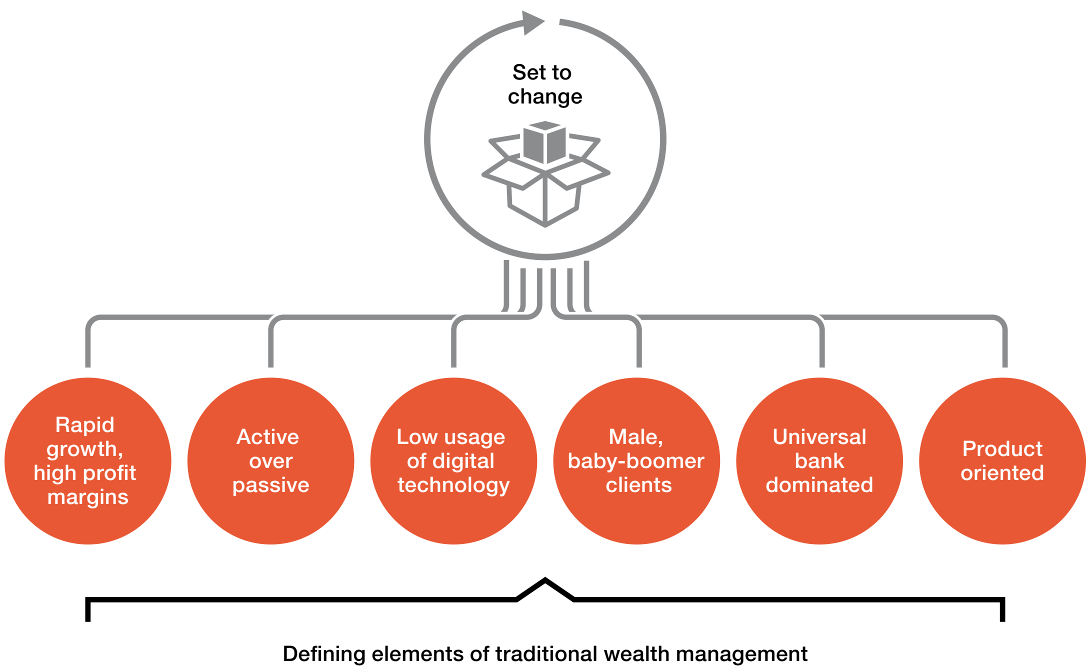
When it comes to asset allocation, wealth managers have commonly leaned towards active investments, rather than passive ones. However, a fundamental shift is under way. In 2017, active funds had 46 % more assets under management than passive funds.[1] Yet, in the same year, US ETFs and index mutual funds experienced an influx of $325 billion, whereas actively managed funds bled $124 billion in withdrawals.[2]

As depicted in the illustration below, each of the wealth management landscape's characteristic features are set to be transformed.

[1] Hunnicutt, Trevor. "Less than 18 Percent of Global Stocks Owned by Index Investors" Reuters. 3 October 2017. Ac-cessed August 2018.

[2] Ibid.

The changing elements of wealth management



Client life cycle

Here we have outlined the typical life cycle of a wealth management client, from the perspective of the firm/advisor. This can be expected to change significantly as the industry evolves, as we explain later in this document.

After onboarding, the advisor must assess and profile the client in order to be able to define a suitable strategy, taking care to ensure compliance with regulatory requirements. Long-term wealth objectives must be discussed, and, if applicable, the client's business strategy. Only after understanding all these elements can the advisor begin to present possible opportunities, solutions and services. Once assets are allocated, businesses are financed and any further services are provided. Regular reviews, adjustments and updates are essential in order to achieve optimal performance. While this is true for all client segments, it has particular importance for Global Actives, whose portfolios require continuous supervision across multiple dimensions. These include active management, and often additional activities such as philanthropy, long-term succession planning, family governance, etc.

It is important to note that the current life cycle is dictated by the operations of the bank, or wealth management firm. This is to be expected, as not all wealth managers have reached the point where their activities centre on the client. Of course, the activities are built around the client, as illustrated, but the process is still controlled by the bank. However, today's process is fairly inflexible and limits the client's freedom of action.

Time for two over-arching client segments

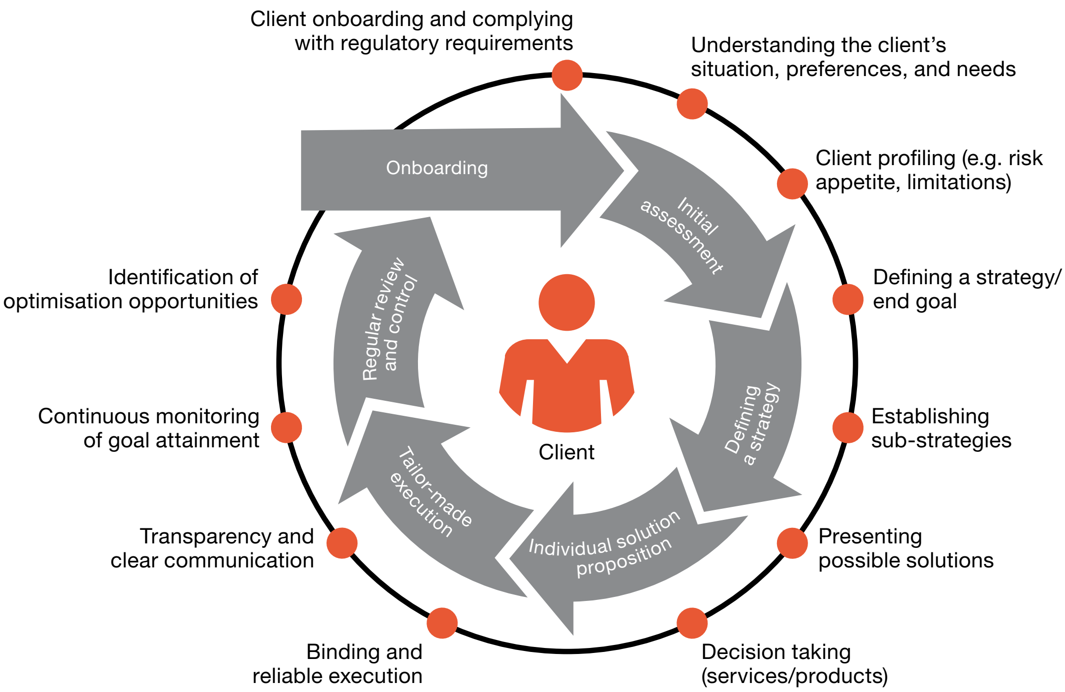
At the heart of the changes faced by wealth management lies the client's evolving behaviour. Technological advances have empowered clients, while the increasing flow of information has enabled them to make investment decisions in real time. Moreover, mounting regulation over the last few years has forced wealth managers to include clients in investment decision making. Finally, cost pressure has forced banks and wealth managers to focus on revenues and costs spent per client rather than just AuM. Consequently, individualised service offerings will only exist for those clients that have special needs, and are willing to pay direct or indirect fees for such a service.

This shifting client behaviour suggests that the old way of clustering clients by AuM is no longer appropriate – yet few banks have redefined them. In our view, there should be two over-arching client segments.

Local Affluents

These clients have a substantial level of wealth, but are conservative and passive in the way they invest. We call them Local Affluents because their families and businesses are situated in one region, rather than spread across the globe. Local Affluents require well-structured portfolios, with advice and guidance from a trusted bank that has a local presence (i.e. branches in the area where they live). Their main objective is normally wealth preservation (although their attitudes may change as they go through life); returns in line with their local market environment are usually sufficient. While these clients do not require highly-tailored services, they still demand digital access via multiple channels.

Today's client life cycle



Global Actives

Global Actives tend to be domiciled in different regions around the world, as do their families and businesses. Such itinerant existences create significant complexity, as wealth managers need to deal with differences in tax laws, federal regulations, trust structures and the complications that come with international cash flows.

Along with this logistical complexity, Global Actives typically favour more complex portfolios. They demand broad and thorough coverage of asset classes, as well as access to exclusive networks and alternative investments (such as private equity). They also expect their wealth managers to maintain a comprehensive understanding of their holistic situation (e.g. family wealth planning, personal ambitions, etc.), and to provide a highly-customised service, far beyond what traditional banks offer. The keys to meeting these expectations are global mobility and flexible access. Unlike Local Affluents, Global Actives do not worry about whether a bank is nearby; instead, they want wealth manager to organise deals globally, and to provide 24/7, unrestricted access, anywhere in the world.

Why does it matter?

If wealth management firms are still segmenting clients based solely on net worth, they are stuck in the past. We firmly believe that differentiating them by behaviour, preferences, and circumstances would allow a firm to position itself more distinctly and provide more suitable services to clients. We believe that this will become the necessary foundation for sustainable and profitable growth. In fact, the benefits of this were evident in the 2018 FA Insight Study by TD Ameritrade, which found that wealth management firms with a specific target market achieved 18 % higher median profit margins and 35 % higher median annual client growth than their peers.[3]

Putting revenue growth to one side, serving these two dissimilar client segments would require different operating and business models. Consequently, to achieve operational efficiency, it's vital that a wealth manager excels in its core segment. Doing so will boost the synergies within a firm.

Defining a clear target market benefits both clients and firms alike. Clients receive a specialised, high-quality service, while the wealth manager excels at a small set of core competencies, rather than attempting to do everything. Focusing on a target client is more important now than ever before, as the industry will soon be transformed, and client behaviour will continue to evolve. Firms need to be aware of which segment they are targeting to stay ahead of the curve. This is the first step towards being truly client centric; wealth managers should align their organisations and operations to the client's needs and behaviour. **This leads to the central message of this paper – that to succeed in the future, firms will need to focus on their niche, and provide outstanding service in that area.**

[3] "The 2018 FA Insight Study of Advisory Firms." TD Ameri-trade. Accessed August 2018.

Two overarching client segments

		Local affluent	Global active
Client	Customer traits	• Highly affluent in home country • Rather risk averse, focus on wealth preservation	• Global footprint and investment behaviour • Strongly and increasingly self-directed
Client	Complexity level	• Lower to medium, in terms of both direct services and number and complexity of investment vehicles	• Higher complexity, in terms of both direct services and the number of investment vehicles
Wealth manager	Business model	• Demand for holistic advice across the lifecycle and increasingly protected by regulators • Focus on plain vanilla investments products	• Broad, deep coverage of asset classes • Access to PE investments and networks • Increasing demand for very specific and individual services
Wealth manager	Operating model	• Gain high visibility in specific region; market penetration driven by distribution muscle • Local booking centre with strong retail capability and scalability	• Small number of branches in hotspot locations worldwide • Global booking centre footprint with strong offshore and multi-shoring capabilities

2. Emerging trends and innovations

Next, we identify and elaborate on the emerging trends that are likely to reshape the wealth management landscape.

Emerging trends and changes

Trend	Details	Implications on incumbents
Evolving Client preferences	• Demanding higher transparency, usability, personalised service and a strong digital offering • Changes in behaviour include a lack of trust and loyalty, as well as a desire to have more control	• Be first movers towards digitisation, allow it to help transform business model • Focus on the frontend, deliver outstanding user experience
Advancing Technology & innovation	• Robo-advisors uses algorithms to manage investment portfolios • Robos are quickly growing, with 14 % of surveyed HNWIs already using them • They present both an opportunity and a threat to incumbents	• Offer robo-advisory as separate service for different client segment • Or implement a hybrid model of advisory
New entrants	• FinTech firms offering services that cut out the traditional wealth manager • GAFA planning an entrance into finance • Both FinTechs and GAFA provide an excellent user experience	• Partner with FinTechs, allow them to handle advanced digitisation and user experience • GAFA not yet a concern
Shifting demographics	• Larger focus on the mass affluent segment, mainly through robo-services • Millennials and women are becoming wealthier, and have unique preferences • Specifically, they demand holistic, goal-oriented advisory	• Consider market opportunity of mass affluent • Adapt to preferences of millennials/women
Margin **pressure**	• Higher regulation and competition is decreasing profitability for incumbents • Reputation no longer as important as in the past, rising importance of performance and customer experience	• Rethink value proposition • Focus on niche

Shifting client preferences and behaviours

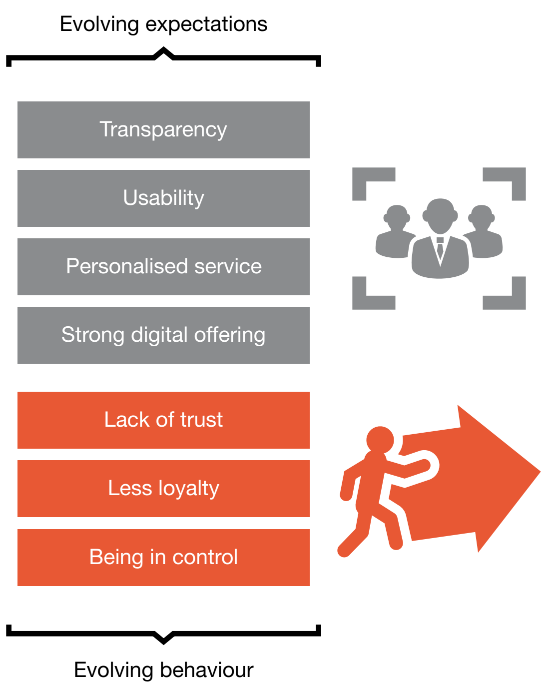
In a client-focused business such as wealth management, it is vital to pay close attention to clients' constantly changing preferences and behaviours. Today's clients are evolving in many ways: from thinking patterns, to standards, to expectations.

Firstly, they are more and more inclined to make financial decisions themselves, and want to keep control of their financial lives. They want to fully understand their wealth manager's advice – rather than simply take it as gospel. Clients are empowered through readily available information that allows them to conduct their own research, as well as take advice from peers. There's a lack of trust that likely stems from the 2008 financial crisis, where trusted figures of authority proved to be at fault.

Just as trust has fallen, so too has loyalty to the wealth manager. This is also caused by today's widespread accessibility to financial information, over which wealth managers used to have virtually exclusive access. So, clients are relying less on advisors for general information and analytics now that they can access this information themselves, thanks to the encyclopaedic knowledge of the internet. If advisors do not provide significant added value, clients no longer have an incentive to do business with them, and are likely to switch to another (or to a robo-advisor).

Clients also want transparent service and product offerings. This is interrelated with both factors mentioned above: the loss of trust, and desire to be in control. They want openness about performance and fees, as well as the logic behind portfolio decisions. In the digital age, and with the rise of social media, transparency has sharply increased across all industries; wealth managers need to catch up.

Evolving client preferences and behaviour



Being straightforward about fees is a major part of transparency. Next-generation clients do not want to be swamped with long, convoluted terms and conditions documentation, with the fee structure hidden somewhere inside. Transparency is key and fee structures might need to change.

Linked to transparency, clients want access to information and their contacts in real time –tailored to their needs. This relates to 'digital usability' and brings AI into play. Today's clients demand frequent touchpoints through various channels, and an intuitive, personalised customer experience. According to a survey conducted by PwC, "the world's wealthy are willing to give up personal data in exchange for highly personalised services"[4]. Wealth management firms will need to become better at leveraging data to deliver this, (as will be discussed in a later section).

In the 21st century, clients expect a strong digital offering that is intuitive. Digital services are perceived as table stakes, i.e. the bare minimum. But there is a wide gap between what clients expect and receive (69 % of HNWIs use online/mobile banking but only 25 % of wealth managers offer digital channels beyond email)[5]. Clients want information through multiple channels, a wish that relationship managers severely underestimate. Similarly, it is likely that relationship managers think the human touch irreplaceable when it's not, especially for HNW clients. While face-to-face interaction may continue to be necessary in many cases, administrative functions (e.g. portfolio review) should, in the view of clients, already be accessible through digital channels. With technical literacy advancing rapidly, it is also reasonable to assume that clients will eventually expect to receive advice through digital channels as well.

There is unusually low digital literacy throughout the wealth management sector, when compared to other industries and even other sectors within finance. According to PwC research, only 25 % of wealth management firms use digital channels beyond phone/ email, and only 10 % interact with clients through social media[6]. Additionally, some naively rate their business as digitally advanced when all they offer is a website. Very few firms have even introduced digitisation to back-office functions, let alone to the front-end. There is clearly a lag in the adoption of technology in the wealth management sector, and firms need to make an immediate effort to satisfy client expectations, if they wish to avoid losing business to robo-advisors and FinTechs that are more in touch with today's digital environment. In order to match up to expectations, incumbents should embrace digital technology as a transformational tool, rather than simply aligning tech with existing business strategy. (We will elaborate on this point in a later section.)

4 "Sink or Swim." PwC Strategy&. September 2016. Accessed August 2018.

5 Ibid.

6 Ibid.

Advancing technologies and innovation

Rapid advances in technology, and specifically the rise of AI, have enabled the digital automation of wealth management services. Dubbed the "robo-advisor", this software utilises algorithms to convert large amounts of data, including that illustrating market trends and individual risk tolerance, into suitable (usually passive) investments for clients. Robo-advisors build diversified portfolios (comprised largely of ETFs), and continuously adjust them, without any human assistance. They can also automate tax loss harvesting. Furthermore, fees tend to be significantly lower than the ones charged by traditional advisors.

Robo-advisory is rapidly accelerating in popularity. Business Insider Intelligence projects that robo-advisors will control around $4.6 trillion in assets under management by 2022,[7] from $402 billion today.[8] Interestingly, it is not only the mass-affluent client base that is attracted by the simplicity and price of robo-advisory services; 14 % of HNWIs (including 23 % of European HNWIs) are already using them.[9] Additionally, 47 % of HWNIs under 45 who don't already use a robo-advisor would consider using one.[10]

Innovative newcomers will likely expedite this rise in popularity. While some of the most well-known robo-advisory firms, such as Nutmeg and Betterment, already offer fees as low as 0.25 % of assets under management, new firms like WiseBanyan offer basic robo-advisory completely free of charge, and incur fees only for specialised services. Clients no longer need to give up a percentage of their assets before any returns are earned. This new model eliminates barriers to entry for clients, and encourages even those sceptical about robo-advisory to give it a chance. As new firms drive innovation, incumbents must quickly adapt.

Robo-advisory poses a threat – or presents an opportunity – to human advisors, depending on which perspective one takes. One thing is certain: it is sure to challenge the traditional model of wealth management.

In particular robo advisors will be used to help service the Local Affluent client segment mentioned in the previous chapter. It is too expensive to offer this segment personal and individual services. R obo advisors can meet this segment's needs for straightforward products and services.

New entrants to the field

Another emerging threat to wealth management comes in the form of the FinTech startups and tech giants.

FinTech firms commonly focus on the user experience. They are offering services that could potentially cut out the traditional wealth manager. For example, one 'social trading' app/website allows users to "copy" the investments of other users, including trusted, successful investors. This is essentially a basic form of wealth management, where the client pays no fees to the "advisor", and has access to perfectly transparent information about all investments, updated in real time.

Other FinTechs, like crowdfunding sites, allow investors to become creditors to small businesses, and achieve a fixed rate of return. It is easy to see how investment propositions like these could depreciate the value of, and pose a threat to, traditional wealth managers, through offering "do it yourself" solutions.

In addition, there is speculation that the powerful tech giants may be planning to enter the finance industry (in some cases, they are already in the process of entering). These firms benefit greatly from an extremely loyal and engaged customer base, as well as a firm grasp on what creates an excellent user experience. Their most uniquely advantageous asset, though, is the immense amount of user data at their disposal – data that can be leveraged to provide customers with highly personalised financial services. Furthermore, tech giants will likely aim to incorporate financial services into users' daily digital ecosystems. For example, Facebook has recently introduced the ability to send and receive payments through its Messenger app, and Apple now facilitates payments through its iPhones with ApplePay. This is almost certainly only the beginning of these firms' involvement in finance. David Marcus, VP of Messaging Products at Facebook, stated: "It is so much easier to do everything in one place that has the context of your last interactions, as well as your identity – no need to ever login – rather than downloading apps that you'll never use again and jumping around from one app to another."[11] This statement reveals the company's vision of eventually providing everything a user needs, presumably including wealth management, within one single interface. Additional evidence of the tech companies' entry into financial services is demonstrated by the forming of the coalition Financial Innovation Now by Paypal, Google, Amazon, Apple and Intuit. These tech companies have joined forces with the aim of promoting greater innovation in finance.

Note that, as far as wealth management is concerned, the tech giants' possible innovations are most likely to target the general population, and less so the wealthiest clients, i.e. HNWI and UHNWI, who will always require more specialised services. However, it is still worth noting how the landscape of financial services is evolving, to get an accurate sense of where the future is headed.

Shifting demographics

In the coming years, there will be a large transfer of wealth, often labelled the "Great Wealth Transfer". As the Baby Boomers (the wealthiest generation) become older, their assets will be passed down to their heirs, mainly Millennials. This transfer amounts to an estimated $30

7 "How Automated Investment Products Are Disrupting and Enhancing the Wealth Management Industry." Business Insider. July 2017. Accessed August 2018.

8 "Robo-Advisors – Worldwide | Market Forecast." Statista. 2018. Accessed August 2018.

9 "Sink or Swim." PwC Strategy&. September 2016. Accessed August 2018.

10 Ibid.

11 Marcus, David. "Here's to 2016 with Messenger." Facebook Newsroom. January 2016. Accessed August 2018.

12 "2016 Wealth Management Trends." PwC Strategy&. 2016. Accessed August 2018.

trillion or more, and is expected to have a substantial impact on the wealth management industry. In fact, recent PwC research revealed asset attrition rates of over 50 % in intergenerational transfers of wealth.[12] Therefore, incumbent wealth managers cannot rely on family loyalty. They will have to recapture the new generation to retain the assets they currently manage. Millennials are likely not only to exhibit the evolved client preferences discussed earlier, but also to carry traits unique to their generation. For example, two thirds of millennials view their investment decisions as a way to express social, political, or environmental values.[13] Additionally, they display a heightened interest in investments that are uncorrelated with the broad market; 63 % of millennials have either invested in, or are interested in, hedge funds, and this number rises to 75 % for private equity.[14]

Moreover, most millennials prefer to measure investment performance against their own personal goals or custom indexes[15], rather than against broad market benchmarks, which is the traditional practice. This is propelling another general trend in the landscape of wealth management: a shift from market-oriented, to goal-oriented investing. Goal-oriented investing emphasises the client's personal financial objectives, such as covering college tuition, growing a retirement fund to a specific amount, etc. Progress is then measured against the completion of these goals, largely ignoring the broad market. This strategy typically requires the advisor to take a proactive, personal, holistic approach, and be more involved in the client's life rather than only their finances. This type of wealth manager is labelled by some as a financial therapist.

This trend is understandable, given the higher desire for personalisation discussed earlier. Interestingly, the increasing popularity of this highly personal approach coincides with the rise of robo-advisory, which entails minimal human contact.

The rise of goal-oriented investing is already visible. Target-date funds are a common choice for goal-oriented investors, and these funds have grown significantly every single year since 2008.[16] Moreover, research by PwC found that 73 % of HNWIs under the age of 45 are likely to seek expert help for non-financial matters, such as career and family life, further signifying a growing demand for goal-oriented, holistic advisory.

This shift to goal-oriented investing could be linked with the rise of women as a proportion of the wealth management client base. As women comprise an increasingly large part of the workforce, and continue to inherit significant amounts, they are becoming wealthier. Additionally, they are becoming more involved with their family's finances; 84 % of HNW women across the US, UK, and Canada are now fully or partially responsible for their family investment portfolio.[17] Wealth management firms need to recognise that women have different preferences to men, and should begin to devise a new advisory model for this category of clients. Women tend to value holistic advice highly (goal-oriented investing), and assign less importance to purely financial advice. According to the former president of the wealth management division of Bank of America, women (like millennials) care less about their portfolio's performance against the market, and care more about questions like "can I send my kid to college?" Additionally, they often value wealth preservation over upside risk[18], which tends to be less true for men.

Lastly, an important demographic trend is the rise of wealth in the APAC (Asia-Pacific) region; particularly in China. PwC/UBS's 2017 Billionaires Insights report[19] found that, for the first time, there are now more billionaires in Asia than in the US. Additionally, based on current trends, the total wealth of APAC's billionaires will overtake that of the US within three years. This growing client base presents a significant opportunity for wealth managers.

Margin pressure

Profit margins in the wealth management industry are decreasing. The 2018 FA Insight Study, which surveyed nearly 400 established wealth management firms, revealed that average profit margins in 2017 were 19.7 %, down from 2016's margins of 24.4 %.[20] These decreasing margins can be attributed largely to greater regulation and fierce competition. The impact of more stringent regulation and compliance laws has been felt all over the finance industry, including wealth management, where increased investor protection has squeezed margins. Competition is also quickly increasing. Clients' new priorities have lowered barriers to entry as reputation has become relatively less important compared with high performance and an excellent customer experience. This has allowed FinTechs and robo-advisors to penetrate the market and achieve rapid growth in a short time. Their exceptionally low prices have put immense cost pressure on incumbents.

13 "Insights on Wealth and Worth." U.S. Trust. 2015. Ac-cessed August 2018.

14 Ibid.

15 Ibid.

16 "The $1 Trillion Target-Date Fund Landscape." Morn-ingstar. May 2018. Accessed August 2018.

17 "Women & Wealth Transfer." RBC Wealth Management. 2017. Accessed August 2018.

18 Ibid.

19 "Billionaires Insights Study." PwC and UBS. 2017. Ac-cessed August 2018.

20 "The 2018 FA Insight Study of Advisory Firms." TD Ameritrade. Accessed August 2018.

3. Tomorrow’s world

It is clear from the pace at which these emerging trends are progressing that a paradigm shift is looming. In this section, we illustrate what a platform-based wealth management industry might look like.

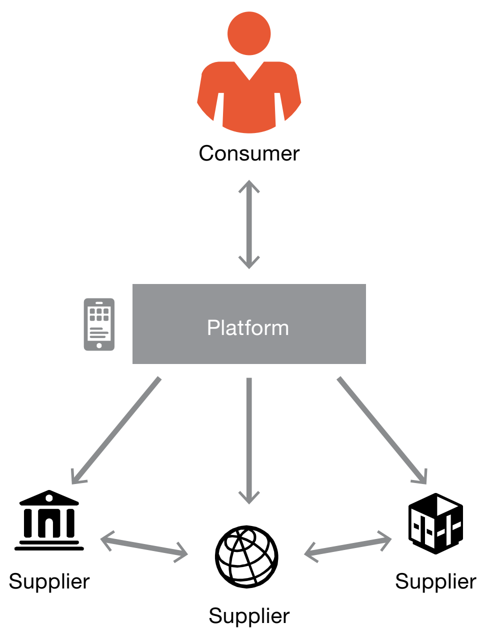
Platform-based economy

If we consider the digital economy, we notice a common element across various industries: business models built upon digital platforms. Whether it’s eBay for e-commerce, Uber for ride-sharing or Airbnb for lodging, numerous industries are gravitating towards a platform-based architecture. The unique feature of platforms is that, rather than handling production and distribution via a vertical supply chain, they simply facilitate connection between multiple parties – usually buyers and sellers. In other words, they efficiently connect supply with demand.

The recent economy-wide dominance of platform-based business models can be explained most simply by the fact that platforms are centred around demand, whereas traditional producers are, naturally, focused on supply. As the global economy becomes more consumer-centric across all industries, it is unsurprising that platforms have risen to great heights; they are able to provide consumers with better quality, more individualised service than ever before.

The recent rise of digital technology has taken cost-efficiency, scalability and reach to an entirely new level. Platforms also benefit from network effects, meaning that their value increases according to the number of users they have (because more users attract more producers, leading to better matches of supply and demand). Network effects often lead to a positive feedback loop, where more users increase the platform’s value, which consequently attracts more new users, and so on. This explains the recent exponential growth of platform businesses.

Motivation for niche focusing



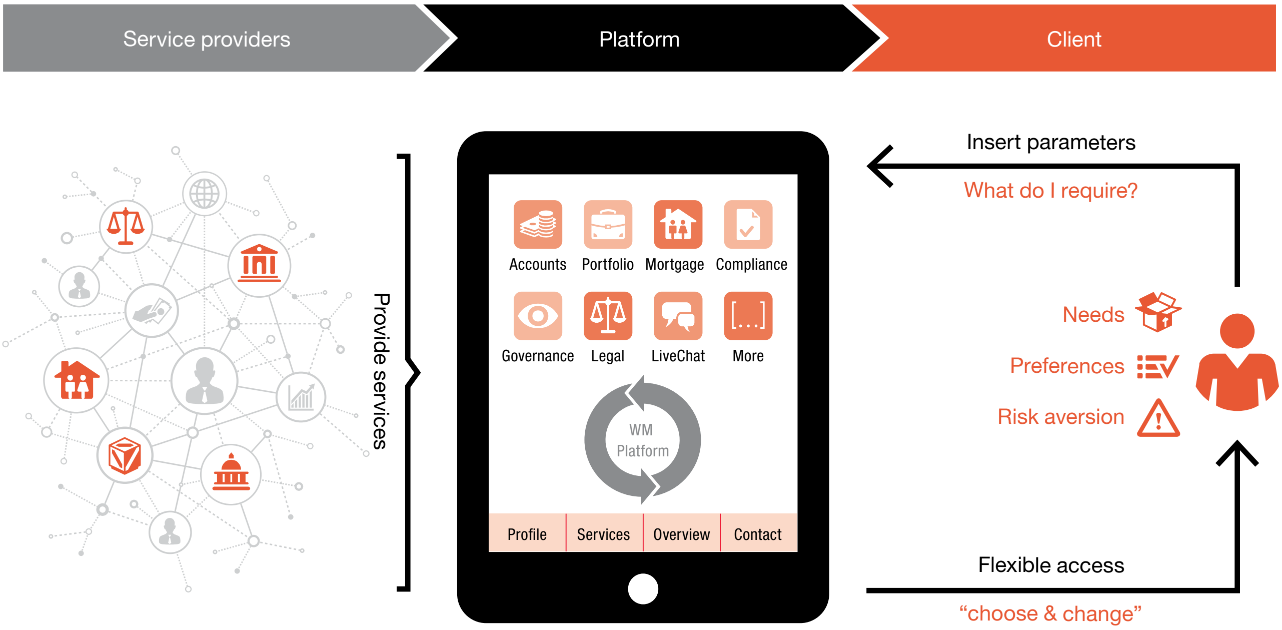
The ecosystem

We predict that the traditional model of wealth management will evolve into just such as platform-centric ecosystem, with several separate entities interacting with each other to provide wealth management services to clients.

We envisage a digital platform as the core of this ecosystem. Clients should be able to use a single interface, e.g. a smartphone app, to access all their wealth management services. This platform will allow clients to search for and compare service providers, using filters such as client objective, fee structure, area of specialization (niche), etc. There might also be a client survey asking questions about risk appetite, financial situation, etc., thus enabling the platform to recommend suitable service providers. Preferably, users would also be able to view reviews and feedback left by other clients for each provider. The platform, therefore, could be characterised as open architecture and not controlled by the platform owner. In this respect, it would be like a digital app store.

The process would start with the client’s requirements and expectations. A Local Affluent with locally-based wealth, for example, needs different services from an internationally minded Global Active with a complex portfolio of assets spread across several countries. Considering these differing needs, the platform can deliver various tailored solutions, supported by AI-based robo-advice (or similar). These might include administering different accounts, portfolio management, mortgage offerings, legal support, a 24/7 live chat etc. A different specialist firm would provide each service. After onboarding and selecting the desired services, a client would ideally use this digital platform as a dashboard. The dashboard would offer portfolio overviews, progress towards goals, live chats with advisors, and

Platform-based economy



instant updates and alerts. Advisors already use similar dashboards; however, the future is client-centric. That means clients should have a comprehensive overview of their wealth on one, easily accessible digital site.

It is possible that traditional banks will end up becoming platforms, essentially transforming themselves into vendors of third-party wealth management services, while still delivering a complete experience to the client. This outcome would make sense, as banks are proficient in authentication and security, and are trusted. These characteristics qualify them to conduct onboarding and KYC compliance on behalf of all the service providers. Additionally, they would vet each provider. Having banks playing such a central role would not only greatly increase the viability and appeal of the platform to clients, but also place banks at the core of the future ecosystem.

This is certainly one way for incumbents to partner with robo-advisors and FinTechs. Additionally, AI could play a major role in enabling such platforms, especially when it comes to delivering complex data-based solutions. AI-based services could support Local Affluents, who mostly require direct professional advice. Work originally carried out by human advisors could evolve into an AI-based robo-advice through industrialisation and automation. Therefore, AI could partly replace human advisors and transform the business of wealth management. The new world for Local Affluents would include both human and robotic advisors.

Turning to Global Actives, we predict that they will continue to be best served by trusted human advisors – but these advisors will leverage powerful algorithms to improve their advice. So, it seems inevitable that tomorrow's platforms will be based on open architecture, controlled by the client, regardless of whether that client is a Local Affluent or a Global Active.

If banks don't seize this opportunity, a FinTech or even a big tech firm could do so – therefore, we urge incumbents to act quickly. Converting to a platform-based business model would certainly require significant technical and organisational reorganisation, but most traditional banks have sufficient resources to do so. We believe that harnessing the full potential of digital technology means transforming the entire business. Simply adapting the back office to align with the existing business model is not a realistic option. Converting to a platform is an excellent way to achieve this result.

We view the platform-based model as a win-win situation for everyone. Clients gain more varied, individualised services; new service providers benefit from the reputable infrastructure of traditional banks; incumbent banks build a protected position at the centre of the future industry. When considering the network effects described earlier, it is easy to see how wealth management platforms could quickly become popular.

However, pricing would be affected by the change in product and service delivery. It would move towards a cost-based model, where individual services are priced higher than straightforward platform offerings. Pricing would no longer be based on AuM, but the cost per client. Therefore, Global Active clients would pay higher fees than Local Affluents.

Service providers

In tomorrow's ecosystem, service providers will be highly specialised, client-centric and completely integrated into platforms. Being a specialist provider to a platform-based ecosystem should foster economies of scale and, therefore, lead to a better quality of service, by implication improving performance across the whole ecosystem.

We predict that digital tools and solutions such as AI or robo-advice will become indispensable, in particular for the Local Affluent segment. They could significantly improve the solutions offered to clients, not just in investments but also more complex advisory areas including tax and estate planning.

Examples of ecosystem service providers could be mortgage lenders for small business owners, holistic wealth planners for retirees, robo investment advisors for Local Affluents, etc.

Traditional banks that do not take on the role of platform will also act as service providers, focusing on a niche and integrating into other platforms. Of course, there are also niche opportunities in B2B ecosystems, not only B2C – note the launch of ClearBank, the new UK clearing bank.

But regardless of whether a bank or another organisation takes the role of platform, the so-called B2B2C-Business, where several independent firms together add value for themselves (B2B) and for clients as a platform (B2C), will most likely become an important part in the future of wealth management.

Future client experience

Such an evolution to a platform-based ecosystem would have substantial benefits for clients. Imagine the client's future life cycle. Crucially, the client controls the process in tomorrow's platform-based ecosystem. This is fundamentally different from today's life cycle (see section 1).

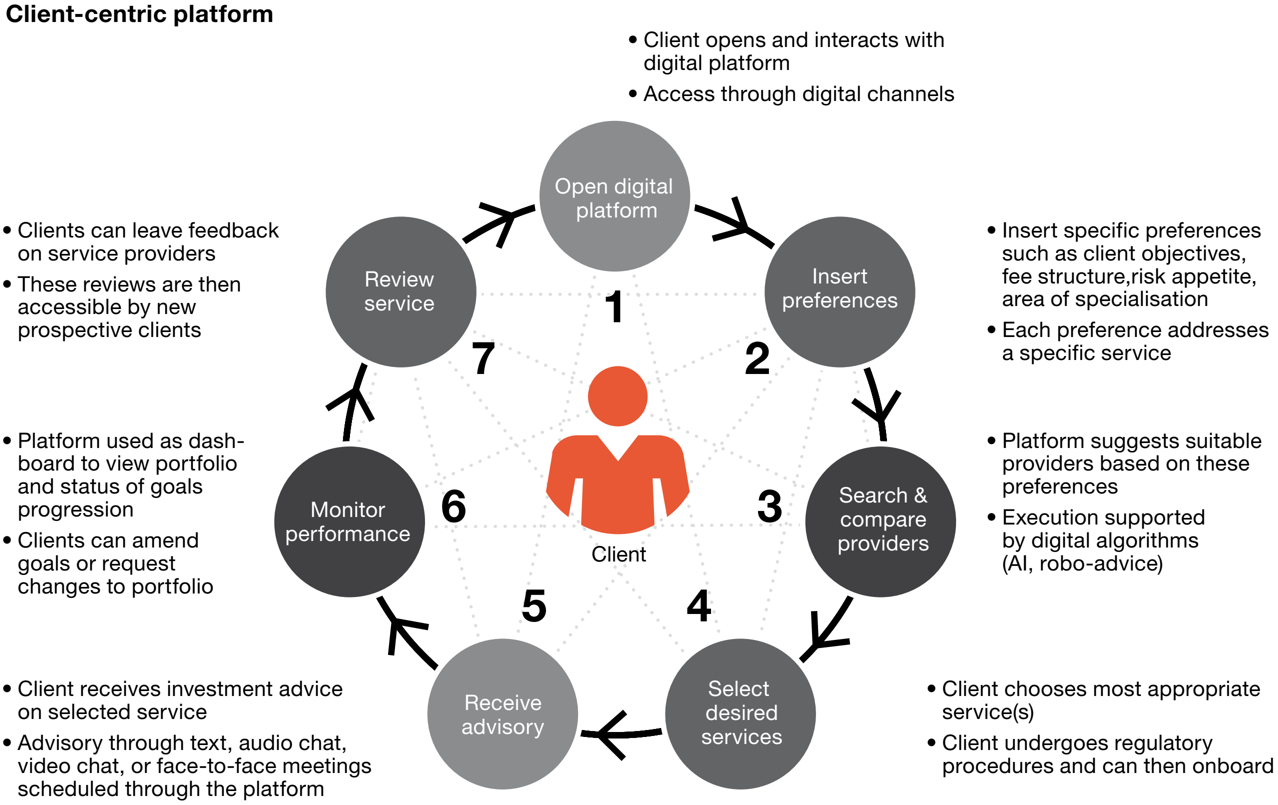
As already mentioned, clients first specify their parameters before searching and comparing service providers through a digital platform. Afterwards, clients can select their desired services and receive tailored advice.

Furthermore, they can choose new services or change existing ones at any time.

Powerful AI-based algorithms and further digital solutions provide tools to measure and monitor the performance of portfolios and progress towards goals.

The result? Tomorrow's clients will be freer to make decisions – such an outcome could fundamentally challenge existing wealth management business models.

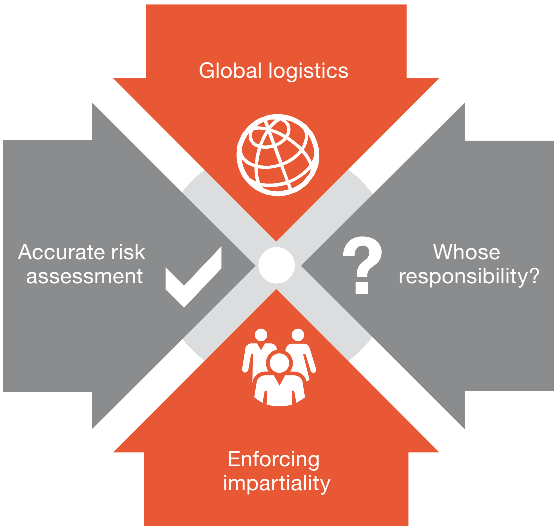
Client-centric platform



4. Future challenges and an outlook

Naturally, the future wealth management ecosystem will face challenges and limitations, just as the industry does today. Nonetheless, wealth management firms need to consider their positions within a platform-based industry sooner rather than later.

Future client life cycle



Future challenges

Global logistics

Firstly, and most obviously, implementing and managing this ecosystem will present logistical challenges. Notably, the differing tax laws and regulations of each country would present obstacles when integrating providers from across the world onto a single platform. Additionally, it's not clear which law should apply.

Responsibility?

Furthermore, the platform-based industry model raises the question of responsibility. Will platforms be responsible for integrating all their offered service providers? Or will each provider take responsibility for ensuring its software can easily be integrated? These are questions that will need to be answered as the industry's transformation moves into full swing.

Enforcing impartiality

Next, it is important to realise that as platforms gain popularity, they will hold a large amount of power in the ecosystem, as they control which providers are offered. If banks do indeed become the major platforms, the danger is that they push their own products rather than recommending those that are best for the client. Similarly, platforms could hold auctions, pushing the products of the highest bidding provider – just as Google does with sponsored search results. To guard against such an eventuality, there would need to be mechanisms to enforce platform impartiality.

Accurate risk assessment

Lastly, automated risk-assessment processes would have limitations. People tend to have trouble realistically assessing their appetite for risk. So, there could be problems using digital surveys alone as the basis for structuring appropriate asset allocation for clients. Some human input might be needed.

Need for action

Demand for wealth management services continues at a high level. But banks and wealth management firms must become the innovators of tomorrow's platform businesses.

In the long term, incumbents will need to decide whether to build their own network of specialised service providers, i.e. a platform, or join another network as a service provider. Regardless, action is required.

Many major players in wealth management already utilise external asset managers, for instance. Whether intentional or not, this is one step on the right track towards a platform-based business model. Similarly, some universal banks have begun to launch separate, specialized services.

How clients will be affected

Local Affluents

The concept of platforms perfectly fits the needs and preferences of Local Affluents. This model exemplifies simplicity, an overview is readily accessible and services can be added or replaced with others almost instantly. Personal contact will remain available but at a price.

We also predict a sharper focus on the lower end of the Local Affluent client segment. Digital technology's efficiency means that wealth managers can profitably extend their services to more clients – ensuring critical mass. The lower end of the Local Affluent segment comprises a large proportion of the population and wealth, and many of these people are receptive to digital services. Research by PwC found that 44 % of this segment "did not even consider their primary bank as a potential provider of household investment services"[21], either because it did not offer suitable products, or because it was not perceived as a qualified provider of investment advice. While the primary focus has traditionally been on the wealthy and ultra-wealthy, this finding reveals the huge opportunity that exists for wealth management firms to service a larger number of the somewhat less wealthy. FinTechs have been doing exactly this; we expect traditional financial institutions to catch up soon. In fact, some have already begun to do so.

Global Actives

With their complex finances, business interests and personal lives, Global Actives have much to gain from maintaining a continual summary of all activities in a single place. It is a convenient way for them to simplify their complex affairs. Whereas Local Affluents will have direct digital interactions with platforms, Global Actives are more likely to benefit from indirect use, which improves the performance of the client advisor.

The rise of hyper-specialised service providers will be of great advantage to Global Actives. Firms that focus specifically on one type of client (e.g. retired business owners) will have better knowledge of suitable investments and favourable lending solutions, as well as unique insights on how to navigate their unique logistical challenges.

[21] "How Banks Can Profitably Serve the Rising Mass Affluent." PwC Strategy&. October 2013. Accessed August 2018.

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