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Wrap-focus on distribution

A very personal view

Agenda

- The customer proposition
  - Selling product or buying services? (or none of these)
  - Use of analytic tools-helpful or Ferraris for adolescents?
- Distribution structural issues-customer segmentation, branding, consolidation / fragmentation
- Logical value chain impact

The customer

- Incumbent industry wants to sell product:
  - Insurance companies = bonds / Sipps etc
  - Fund managers = funds
  - Government = keeps inventing new ones - Pep / Isa,VCT, ASP??! etc
  - Regulator - polarisation is a foundation, but polarisation is by definition product based
  - Institute and Faculty - “of interest to those developing wrap PRODUCTS”
- I am very unsure this is meaningful to the customer

Tools and analysis

- Clearly sophisticated risk and performance tools are the ‘coming thing’
- Many wrap platforms provide these as part of the offering
- Personally unclear that they have anything directly to do with wrap - much more that wrap data makes their utilisation practical
- Some are very sophisticated and big training job for IFAs - dangerous to use with clients unless you understand the limitations

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Lets just think about distribution

- Historic soft differentiation:
  - Tied sales people
  - IFAs
  - Private client stockbroker
  - Private banks
- Different regulation, different branding, different service- but the same customer need
- Wrap is bound to blur these differences
  - maybe IFAs today want to become private bankers and private bankers want to go down market

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So my personal wrap definition

- A technology based risk and wealth management service enabling customer and advisor to understand and MANAGE risk at all levels.
- A direct challenge to the historic product based regulations
- Logically the market is ALL forms of distribution- banks,tied,IFA,retail stockbrokers and private bankers. Service proposition then is more about wrap platform than historic demarcations

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Thinking about the structural issues

- Obvious differentiators going forward:
  - The revenue model. IFAs are very variable in ability to move to renewal earnings. Many though do have renewal>fixed costs. Most recognise that business value tied to trail
  - Self evidently much easier to support trail from richer clients. Support costs have some linkage with size, but certainly not linear
  - Further reinforces recent IFA drift up market
- Some services (notably mortgages) though will always be transaction based.

Switching investments

- Much industry concern over replacements
  - Polly put kettle on etc
- Wrap platform
  - Provides much more accessible client information
  - Generates renewal earnings as priority
- As a CUSTOMER I think replacement in this model thoroughly good
  - if funds change / deteriorate I want my adviser to recommend exit. I don't buy shares and hold until retirement - why should investment managers be different?

Knowledge is power

- Wrap market likely to polarise between historic providers and independent/intermediary led
- Providers have advantages of scale and capital
- The distribution dilemma is "In 5 years time the provider has all the clients and their assets"
  - what then is the IFA value and independence?

The IFA market - historic M&A

- Industry is fragmented, subscale, capital poor and generally poorly managed
- I can think of no other industry where value doesn't sit with the customer interface (think Tesco and farmers)
- Attempts at consolidation have generally destroyed shareholder value
- There is no real mass market or even HNW distributor brand

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Wrap impact?

- My favorite brand definition is CAT
  - Consistency, Attitude and Targeting
- IFAs do very well on Attitude, OK on targeting but the legacy product focus destroys consistency
- Wrap does force a much more coherent customer experience.
- So, in theory brands can be developed via wrap and maybe that leads to better M&A
- That is an obvious issue for provider wrap

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Lets move to value

- Transparency is variable
  - sharp distinction between those disclosing unit trust rebates and those not
- Clearly provider margin is maximised by aggregating holdings, limiting choice in order to guarantee volume and thus rebate
- It is my personal view that at least up market full transparency will win

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The value tensions

- Control of customer. There is pretty much a cartel on 50bp trail commission
- Fund management. A more professional distribution system forces better management but NOT lower costs (think hedge funds and private equity at 200bps plus 20% of the gain)
- Platform - a personal view is that will settle at 25-40 bp
- Tax wrapper (or life company) is logically a commodity

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So some final thoughts

- Wrap is fundamental - it challenges all aspects of the current model
- By enhancing knowledge it creates a superior customer experience and has the potential to enable a much more valuable and well managed IFA sector
- Transparency is part of that, and that in turn is a challenge to life companies
- They must find new utilisation for their capital and resources - but that is for another day

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