ADVISOR PERSPECTIVES

The $100 Million Nightmare

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About 20 years ago, the financial advisory industry began a mass exodus to what it believed was a promised land. Thousands of advisors from coast to coast switched from commissions to fee-based planning, aiming to gain $100 million of assets under management. With such aspirations in mind, abiding advisors set forth what was to be a fail-safe plan to bring them freedom, fat pockets and absolute leverage over their lives and their businesses.

Offering fee-based planning had visible advantages, and this supposed fail-safe plan had many professionals believing that with fee-based planning they stand apart from the advisor down the street. Planners grew confident this would grow their book of business by attracting affluent clients – who were tired of the sales approach – and increase profit margins.

Unfortunately, this was not an exclusive club, and thousands of advisors fled to this strategy only to find all of their competitors were now in the same boat. Commoditization began to weaken business models in the financial advisory business, turning this stately plan into an endless nightmare. Every shop in town was a commodity – offering the same "perks" as the next – and the $100 million plateau was now even further away. Soon, downward pressure lowered management fees and plagued businesses attempting to compete with the rest of the financial advisory world. Like a small crack in a dam, this problem became a disaster soon enough.

This downward pressure showed up in many studies. A 2009 study performed by Moss Adams, which evaluated advisor staffing, compensation and costs, highlighted the operating profit margins for wealth management firms. It indicated that the operating profit margin – or take-home pay on average – was only 14.7 percent of a $1.3 million advisor's revenue, totaling a miserable $955 per client. While wealth management practices fled to fee-based planning, advisors soon learned it wasn't greener on this pasture.

Advisors' workloads quickly snowballed out of control. Regrettably, there was no disclaimer that every new wealthy client brought an unmanageable amount of caring and handholding. In essence, million-dollar clients turned out to be more work than they were worth. Advisors fortunate enough to actually have $100 million of assets under management fell into the category of "most time spent per $1 million of assets under management," according to the 2009 RIA Benchmarking Study from Charles Schwab.

The cost of that time: a whopping $3,000!

The turning point

The expectation of individual counsel challenges an advisor's ability to leverage themselves and their practice. Coupled with suffocating commoditization, the need for individual attention means advisors are now bringing in less money per client – profits were once 1.5 percent of total assets under management, but they are now well under one percent.

When assets under management grow, a company must also. More overhead becomes necessary, and the staffing and costs associated (i.e. health care, technology) increase. As the staff and their benefits grow, the appeal of chasing a $100 million plan recedes. The aforementioned Moss Adams study concluded that 40.1 percent of expenses are overhead costs, with 10.1 percent coming from the salaries of technical, support and administrative staff. As a result, overhead and new costs are now suffocating profit margins.

After the financial crisis and the recession, many wealth management firms' assets under management shrunk has along with their percentage of take-home pay. Problems are now coming one-after-another faster than the average advisor can even begin to recognize and square to face them. The current system has proved itself to be unrewarding and draining.

Advisors have become exhausted from burn-out, long hours and lack of relief. The plan that was supposed to ease advisors' lives and businesses has done the opposite. And on top of the toll taken by demanding clients and commoditization, advisors must also combat the lack of trust brought on by the Madoff and Stanford scandals.

The solution

It is time for a strategy to jolt business back to life. The keystone that will save advisors from the $100 million nightmare is client coaching. Business growth and leverage are compromised by the hours that are spent planning and preparing reports for hundreds hellacious client meetings. Sitting one-on-one with each client – each quarter – is a daunting and time-consuming task. Are there even enough hours in a year?

By coaching clients in groups, advisors will have more time in their business to take on more clients, particularly smaller ones with more potential. Using this group-consultation model, advisors can free up 20 weeks per year of valuable time.

In order to begin a coaching program, your clients must understand that they are emotionally and intellectually unable to manage their own money because they, like all of us, are prone to experience panic, loss aversion, or unnecessary risk-taking. This is where an investor inventory comes into play. An investor inventory consists of in-depth questions (e.g., Do you know how to measure diversification? Has anyone ever calculated the hidden internal costs in your investment portfolio? Do you have an Investment Policy Statement?) for the advisor to fully comprehend and identify their clients' financial behaviors.

Once these behaviors are established, the second step for an advisor is to actively engage clients in prudent investment behavior through "homework" assignments, books, audio tapes, etc. Finally, the clients participate in monthly group coaching sessions to share their experience and reinforce critical investing concepts.

Unlike the plan to which advisors flocked 20 years ago, client coaching has not yet become appealing to many advisors yet. Wealth management firms that differentiate themselves by coaching will ultimately have the leverage in their life and business that fee-based planning once promised. Potential clients will be attracted to the low fees that advisors will soon be able to offer, in part by their capacity to differentiate their practice through coaching.

By employing coaching tools, advisors can break free from the mold of the $100 million nightmare and take home their desired $1 million a year. Those currently adhering to a coaching model are finding that true leverage in life and business is attainable – but the route to the promised land looks different than we once thought.

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