



What's Driving Investment Management Outsourcing?

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Why do investors hire financial advisors? Why do clients fire financial advisors? And what bearing does the advisor's role in investment management have on client satisfaction?

Taken together, these three questions go to the heart of the advisor's understanding of his or her value proposition, especially in the aftermath of the economic and market crisis.

In April 2010, Northern Trust Investments conducted research aimed at understanding advisors' views on the outsourcing of investment management. Data collected in a blind survey to *Advisor Perspectives* subscribers is the basis for our [white paper](#) on advisors who choose not to fully outsource or partner their investment capability.

The trend toward outsourcing investment research has been driven by several market dynamics.

A heightened understanding of what clients value. Investment performance is no doubt part of what a client expects from working with an advisor. But investors have been surveyed exhaustively over the last two years and the feedback is unambiguous in terms of what clients value most. According to a June 2009 report by Cerulli Associates, client satisfaction is driven more by advisors' service and knowledge than performance. "Many best-practice advisors have found that time with clients and prospects remains their most valuable activity," Bing Waldert, Cerulli Associate Director, wrote in IMCA's Quarter I 2009 *Research Quarterly*.

The time required to perform essential investment management tasks competes with time that might otherwise be spent with clients. As shown in the accompanying data reported in the College for Financial Planning's *2009 Survey of Trends in the Financial Planning*, more than 50% of advisors' time is spent on client-facing activities.

Investment management activities represent the second largest (18.5%) demand on an advisor's time.



How Financial Advisors Spend Their Time

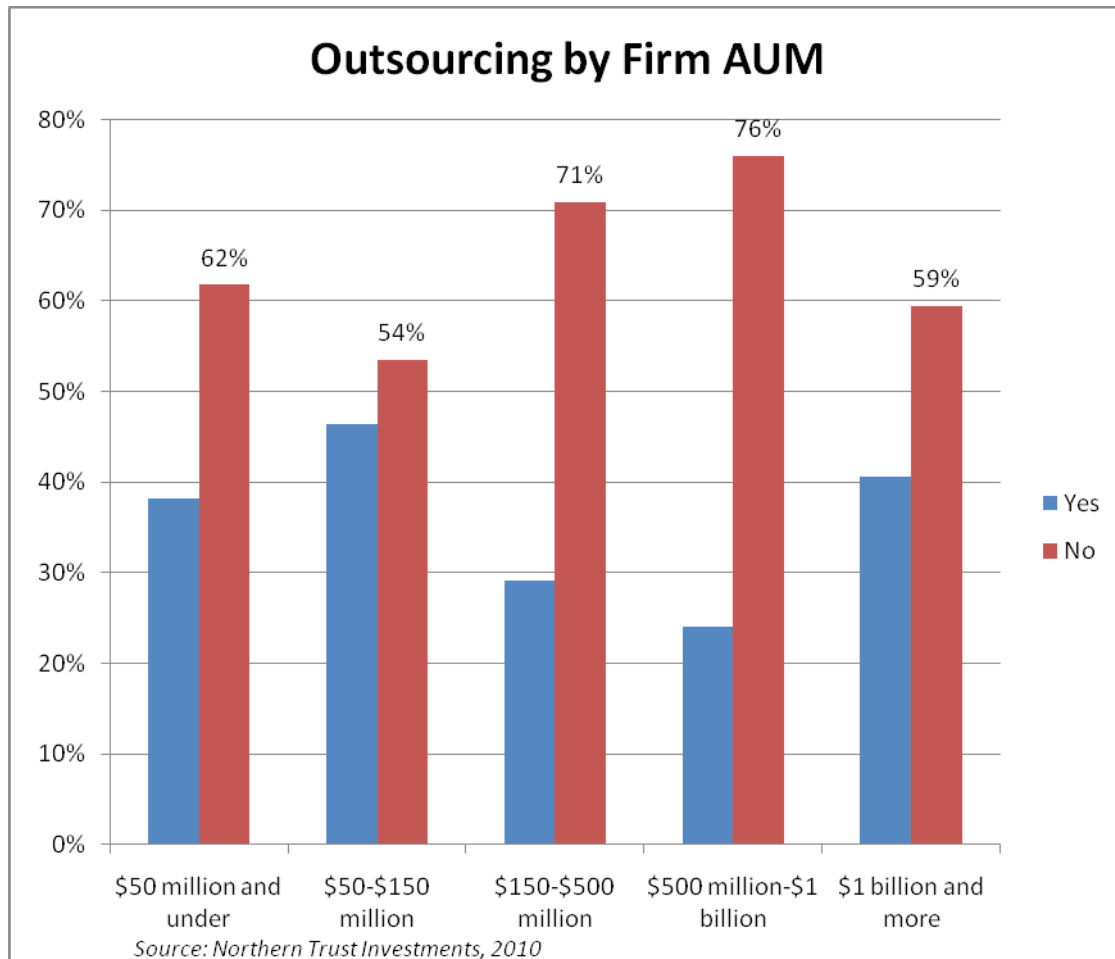
Client-facing activities	53.0%
<i>Meeting with current clients</i>	26.3%
<i>New client acquisition</i>	15.1%
<i>Client service problems</i>	11.6%
Investment activities	18.5%
<i>Research/due diligence</i>	9.3%
<i>Trading and asset management</i>	9.2%
Operational activities	11.8%
<i>Office administration and management</i>	7.6%
<i>Dealing with operations/back office</i>	4.3%
Training/professional development	7.3%
Compliance	6.6%
Other	2.8%

Source: College for Financial Planning's 2009 Survey of Trends in the Financial Planning Industry

Practice management recommendations. As we elaborate on in Northern Trust Investments' Building A Signature Practice program, advisors need to consider the efficiency and effectiveness of what they do. The trend toward outsourcing investment research represents an acknowledgement that an in-house operation can't do it all.

In general, larger firms typically offer more services, and that drives overhead expenses. According to the *2009 FA Insight Study of Financial Advisory Firms: People and Pay*, larger firms tend to rely more on in-house staff to produce and support services while small firms outsource services more often.

The Northern Trust Investments research found that firms with assets under management of \$150 million and \$1 billion were least likely to be outsourcing or partnering for their investment management capability. Elsewhere in the research is a consequence of their decision. As the firm grows in AUM, advisors spend increasingly more time on investment research-related tasks—up to as much as two workdays per week at the largest firms.



Others question the effectiveness of in-house investment management, particularly at firms whose capabilities have developed over time and in an ad hoc fashion. Relatively few firms have the capital base and people and technology infrastructure to take an open architecture-type approach to asset management. The inadvertent result: investment strategy decisions that favor familiar or easy-to-implement solutions.

Expanded “outsourcing” options. The investment industry has created multiple iterations for how to approach the management of the investment portfolio. Best known is the full outsourcing of all investment responsibilities to a third-party asset management program (TAMP). Firms that choose this option optimize their time for working with clients.

But full outsourcing isn’t for all advisors, as survey respondents expressed loud and clear. Asked for the primary reason they are not outsourcing, 37% of RIAs said they consider investment research part of their value proposition, and 19% said the in-house capability was a competitive advantage.



While these advisors appear resolute, options that stop short of full outsourcing exist for them, too. Many seek investment management-related help today in the form of investment product analysis, asset allocation models and multi-manager mutual funds. Multi-manager funds, in particular, offer a means of “outsourcing” the manager research and due diligence, the portfolio-construction and ongoing monitoring, including balancing.

As advisors focus on growing their businesses and serving their clients, there is no reason to believe that investors’ post-crisis desire for communication and education will ebb. Small and high net worth investors alike are seeking more information, and particularly about the risk exposure of their portfolios. The good news is that even advisors uncomfortable with fully outsourcing have options for fulfilling their investment management role in-house while freeing the time to be responsive.

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