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Wealth Management's Major Sea Change

Kelly L. Castleberry III, Senior Vice President
Graystone Consulting

Kelly L. Castleberry III is a financial advisor and senior vice president with Graystone Consulting in Charleston, West Virginia. He carries the additional titles of family wealth director and senior investment management consultant. Graystone is a business of Morgan Stanley specializing in institutional and family wealth consulting.

He has been with Graystone and its predecessor firms for 26 years. He joined with three colleagues in 2006 to form one of the founding teams for Citi Institutional Consulting, which under the Graystone name has grown to 46 teams across the United States.

Mr. Castleberry is a graduate of Marshall University. He is a Certified Investment Management Analyst℠ (CIMA®), a designation offered through IMCA℠ and developed by the faculty of the Wharton School of Business. In addition, he sits on a variety of charitable boards.

It is often said that the only constant in the world is change, but only recently has this maxim rung true for the wealth management industry.

After a tsunami of regulatory changes in the 1930s and 1940s in response to the Great Depression, the wealth management business changed very little for generations. Stockbrokers pitched individual stocks and bonds and clients measured their progress only monthly when the mailman delivered a paper statement. Now, however, the wealth management industry is going through its most profound change in decades. This change is being driven by three distinct, yet interrelated forces – **Demographics**, **Technology** and **Regulation**.

Demographic pressures are both internal and external. Over the next 10 years, it is estimated that nearly one-third of all advisors will retire, leaving firms scrambling to retain and shepherd the assets they manage.[1] A recent study indicated that the average age of a financial advisor in the U.S. is 51, and fewer than six percent of advisors are younger than the age of 30. In addition, according to Cerulli Industry reports, only 13 percent of advisors are women, and fewer than two percent are African-American. As a result, firms are retooling how they attract and retain talent, including making major changes to their training programs and hiring procedures so that their advisors are demographically representative of their client base. Firms are also embracing the formation of teams, which permit advisors to specialize and which allow retiring advisors to transition their books seamlessly from one generation to the next. The old vision of a sole practitioner tackling trading, research, financial planning and relationship management is a model that is clearly destined for mothballs.

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This all comes at a time when wealth management firms are all trying to attract a younger, more diverse clientele. Although millennials dwarf the baby boomers by four million people, they have been largely ignored by the wealth management industry. It has been estimated that more than $30 trillion will be transferred to millennials over the next generation.[2] This leaves the industry scrambling to gain a foothold with younger clients now, even if it will be 20 or 30 years before they amass significant wealth. Reaching the next generation will require firms to both dramatically improve **technology** and to convince them that while information has been commoditized, no smartphone can deliver sage and experienced advice. It will be incumbent upon firms to attract young people by building a "digital lobby" that leads directly to the advisor's office.

And, while technological innovation will be a critical factor in reaching younger investors, it also provides the potential for disruption in the form of the "robo-advisor." Robo-advisors offer algorithm-based portfolio management with little or no human interaction. The benefits to this approach are low cost and minimum investment. And yet, algorithms cannot compete with seasoned professionals in addressing critical life issues such as retirement planning and wealth transference, nor can the robo-advisor help clients avoid the multitude of critical errors that can derail investors throughout the wealth accumulation and distribution phases of life.

Advisors can compete only if they bring advanced competencies to the table, often in the form of additional education and bona fide professional designations. Product pushers with minimal expertise save sales acumen may find themselves increasingly irrelevant.

The third concentric circle imposing change on the wealth management industry today is **regulation**. Increasing regulatory burdens and demands for transparency pose daunting new challenges to wealth management companies. For decades, stockbrokers were merely charged with obtaining the best execution for their client's trades. Now, financial advisors are being held to the much higher fiduciary standard to help ensure that the customer's interests are placed ahead of the interests of the firm, and that advisors are acting in the best interest of the client. FINRA, the SEC and DOL are working to accelerate the transition to this standard. Although this effort is necessary and well-intentioned, transparency may not necessarily translate into improved performance. If it succeeds only in leveling the playing field to the benefit of the client, it should be deemed a success.

From changing demographics to improved technology and heightened regulation, the wealth management industry is undergoing a major sea change in the way business is conducted. What will not change is the investor's desire to receive conflict-free, unbiased advice from an advisor they both know and trust. To remain relevant in the 21st century, wealth management firms must develop new ways to build the client-advisor bond. To fail in this endeavor could not only spell the end of the industry as we know it, but also leave boomer wealth prey to rudderless models and mass-market technology.

[1]*Source: Investment News, February 3, 2014*
[2]*Source: Morgan Stanley, April 28, 2015*