

Digital Wealth Management Report

Introduction

The wealth management industry is facing a period of unprecedented change. Economic turmoil, regulatory variation, customer experience demands, and digital transformation are all shaking the foundations of how firms operate. Wealth managers stand on the edge of a fundamental change in the way they do business, serve their customers, and adopt technology.

The way that wealth managers operate in 2020 and beyond is sure to be a far cry from models which succeeded just a few years ago. High-net-worth individuals (HNWIs) are getting younger by the year, and as their median age dips, their expectations rise. New customers are demanding better personalisation, niche portfolios tailored to their interests, sustainable investing, and an ability to be able to invest from anywhere at any time.

While the wealth manager has perhaps broken free from the image of a middle-aged man in a tan suit stuck behind his desk, challenges remain when trying to move technologically. As firms begin to prioritise interaction with customers and better managed experiences, their legacy technology remains a challenge to be dealt with.

Wholesale replacement has extraordinary risk in both costs and time, though it may remain a strategic target for many years. The scaling technological capability can be achieved through application programming interfaces (APIs), the introduction of third-party services and the oft-quoted marketplace model.

Yet an increased digitalisation of services also creates a larger attack surface for cybercriminals. Information security has become paramount in the digital era, and the risks of a breach can tarnish a firm for decades. Regulatory scrutiny following

the implementation of legislation such as the EU's General Data Protection Regulation (GDPR) and authentication procedures mandated via the second Payment Services Directive (PSD2) have also played their part in pressuring firms to prioritise cybersecurity, especially when it comes to onboarding services.

Experts predicted as 2019 moved into 2020 that a long-running bull market would succumb to emerging economic pressures. Wealth managers were faced with the task of future-proofing their business models if challenging economic pressures became a stunning reality. Now with unprecedented market volatility shaking corporations, financial institutions, and individuals alike, an examination of technological strategy shifts to a necessity if wealth managers are to survive and thrive in a new 2020 paradigm.

“ We believe that technology does not replace the value-adding role of an advisor but complements it by giving the wealth managers of the future new tools to support and inform their advisory function. It is also contributing to a further professionalisation of the wealth management function, allowing the performance of wider tasks with the added benefit of giving a more bespoke feel.



Victor Allende, executive director of CaixaBank Private Banking

Decade-Defining Changes and Challenges

Sustainable Investing

An increasing number of investors have started focusing on the impact of their assets. The nature of the companies, bonds, and shares they are investing in are becoming a greater priority in a time when environmental and civil concerns are gaining greater public consciousness. More than half of all asset holders are now thinking about environmental, social, and corporate governance (ESG) factors in the strategies¹.

Additionally, 52% of the general population and 67% of millennials take part in at least one sustainable investing activity, such as investing in companies or funds that target specific environmental or social outcomes².

Sustainable investing (SI) portfolios have traditionally been kept separate from core offerings by wealth management firms. Yet as demand grows from clients SI options are beginning to be offered and integrated into core offerings with greater regularity.

The late quarters of 2019 saw major wealth management firms shift and assimilate ESG strategies by signing partnerships with decision-support providers, or by conducting thorough exclusionary screening. A survey from the US Forum for Sustainable and Responsible Investment (US SIF) found that \$2.6 trillion in ESG assets was being actively moved into core portfolios, by 75% of the market³.

A Shift in Demographics

The shift of wealth among HNWIs has been a key trend for many years, but its longevity doesn't make it any less important as we enter a new decade. The rise in numbers of millennial and generation Z members of the HNW group, as well as the increasing representation of women, means that wealth managers will have to continue to reinvent their offerings and relationship strategies.

Young HNWIs don't invest like their parents. They care about social impact, transparency, security and privacy. To service these digital natives, wealth management advisors need to adapt. This becomes increasingly important as HNW clients plan to transfer as much as \$68 trillion to their younger heirs within the next 25 years, of which 80% plan to change financial advisor as soon as they inherit.⁴



¹ FTSE Russell, "Smart beta: 2018 global survey findings from asset holders", <https://investmentnews.co.nz/wp-content/uploads/Smartbeta18.pdf>

² Morgan Stanley, "Sustainable Signals", <https://www.morganstanley.com/ideas/sustainable-investing-growing-interest-and-adoption.html>

³ US SIF, "Report on US Sustainable, Responsible and Impact Investing Trends", <https://www.ussif.org/trends>

⁴ CNBC, "What the \$68 trillion Great Wealth Transfer means for financial advisors," <https://www.cnbc.com/2019/10/21/what-the-68-trillion-great-wealth-transfer-means-for-advisors.html>

“The biggest challenge for wealth management firms is to stay relevant to their clients. In fact, in a fast-paced world where challenges and opportunities can arise from both technology and the speed of innovation, staying ahead in those areas and anticipating changes in client behaviour will be key.

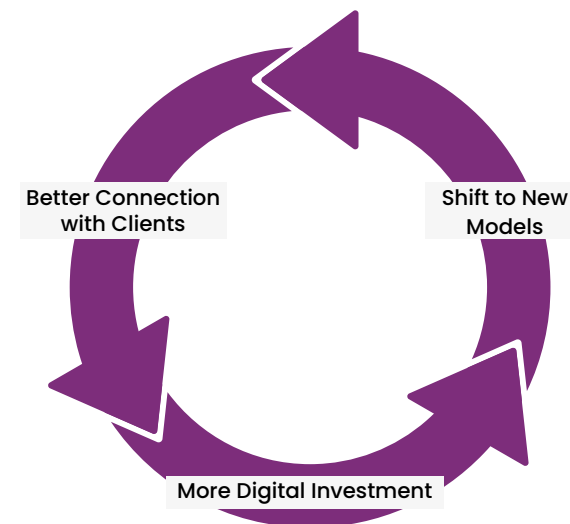
Most of the new breeds of clients expect the same convenience from their wealth managers as they have in other areas of life – for some wealth managers this will require a complete overhaul of their culture and how they operate. In a world where information is at the client’s fingertips, transparency and accountability will also be key.



Philip Frijs, commercial owner, investor segment, Saxo Bank

The attitudes of HNW women can also be markedly different than their male counterparts. By the end of 2020, women are expected to control US\$72 trillion, 32% of all wealth and up from US\$51 trillion in 2015⁵. A greater emphasis on representation is reflected by the investment choices of women, 45% of whom say they want to be better represented by client-facing staff. 36% want to feel less patronised by their managers, and 28% simply want less jargon⁶.

An initial high cost of technological change, compliance requirements surrounding a shift in strategy, and personnel changes may make catering to the demands of younger and female HNWIs seem like a short-term challenge. But the service element of client relationships remains a key success factor in successful differentiation.



⁵ Boston Consulting Group, “Financial Institutions Consumer Insight”, <https://www.bcg.com/publications/2016/financial-institutions-consumer-insight-global-wealth-2016.aspx>

⁶ Wealthiher, “The Wealthiher Report 2019: Understanding the Diversity of Women’s Wealth”, <https://www.wealthihernetwork.com/reportall>

Cybersecurity and Information Security

The financial services sector has always been a major target for criminals, and in 2019 the industry was among the top three affected by cyberattacks and phishing attempts. As wealth management firms undergo digital transformations, a widening of their customer-facing options, and a greater surface of interaction, they must be wary of the implications when it comes to data security.

While 78% of small businesses and 92% of mid-sized business say that cybersecurity is a top priority for them, only 60% of wealth management firm say the same. On top of this, just 43% of wealth managers are concerned about the effect a data breach may have on their brand⁷.

While data leaks and security breaches can erode away consumer and client trust, it will also gain the attention of regulators. The EU's GDPR legislation aims to create an industry of strict data compliance, with violators liable to pay €20 million or up to 4% of global revenue, whichever is greater.

Strategic security decisions need to be made to improve stakeholder trust, while the reskilling of employees in cybersecurity protocols can promote awareness within firms and foster a culture of data security.

Regulation and Compliance

Regulatory reporting in wealth management has come under the spotlight following the publication of the second Markets in Financial Instruments Directive (MiFID II). Under it, firms must provide their advisory clients with a suitability report. The report drills down on how each piece of advice that is given meets the client's circumstances.

These reports are required whether a transaction is made on the back of a client discussion or not. This stipulation means that it is becoming more time-consuming and expensive for firms to offer investment advisory. MiFID II also stipulates that firms must disclose all ex-post costs and charges to clients, requiring firms to plough through multiple layers of flows and accounts.

Research shows that as many as two thirds of wealth managers feel burdened by the regulation and that it has increased their workload. This has likewise had an adverse effect on minimum portfolio sizes, with a third saying they have considered raising them⁸.

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A great challenge facing the sector has been directly linked to the introduction of MiFID II. In this sense, future customers will demand, amongst other factors, greater cost transparency, which will create significant differences between those with value-added advisory services and those without. Transparency is one of the key demands among our clients.

Victor Allende, CaixaBank

⁷ GlobalData, "Trends to Watch in Global Wealth Management", <https://store.globaldata.com/report/fs0178ja--2019-trends-to-watch-in-global-wealth-management/>

⁸ NetWealth, "MiFID II Implementation – A Work in Progress", <https://www.netwealth.com/mifidiireport>

COVID-19

The full impact of the coronavirus pandemic has yet to be felt. Despite this the virus has caused an enormous change in the reality of the industry. Financial markets have gone into a freefall not seen since the 2008 financial crisis, with trading blocked no less than four times across the S&P 500, Dow and Nasdaq in the wake of the virus as all experienced drops in the market of between 10% and 15%. A global recession seems likely.

UK chancellor Rishi Sunak told the country's parliament that an economic fight of this nature has never been experienced in peacetime. The unprecedented market volatility and unease created a waterfall effect, with assets stripped and investments pulled in huge quantities across the globe.

With timelines still unclear, it remains important for wealth managers to diversify their investments, and to avoid correlation. Clients have become naturally concerned for the short-term outlook of their investments, and at this junction wealth managers must do their utmost to assure their customers of their ability to ride the storm. Now more than ever, adaptive and responsive technology is key to informing users of day-to-day activity and keeping communication consistent across all levels of the business.

Future-Securing Strategies

Omnichannel Offerings and APIs

The HNWI of 2020 owns multiple bank accounts and has investments spread across multiple products, likely managed by more than one advisor. There is a strong business case for the providing of unified services, bringing together disparate data sources across multiple platforms.

For wealth managers to retain investment and continue growing their assets under management, all boxes need to be ticked when it comes to the desires of the customer. While a third of new HNWIs may regularly manage their investments over mobile or online channels, that still leaves a significant number who prefer the personal touch.

Yet decades of legacy technology build-up and complex historical processes are slowing the adoption of systems which can offer a cross-channel service. While an evaluation of back office technology is underway, and while the years-long process of replacement, reinforcement, and rebuilding is underway, partnerships with third party services can help lighten the digital load.

The potential of open banking isn't limited to the retail space. While collaboration is not a dirty word to most wealth managers, who already augment their services with the support of execution brokers, custodian banks, and more, it is the speed at which API-enabled third parties operate that can add real value.

APIs can open additional integration and customisation possibilities for wealth managers. The way they can be implemented and added onto existing systems to enhance an offering are potentially transformational.

APIs unlock an easily integrated and adaptable interface, which can be shaped to suit the needs of different channels. APIs mean wealth managers can choose whether they want an entire front-to-back proposition or whether they just want to use certain parts in tandem with their own systems.

More than just papering over the cracks, adding an API layer to the client-facing aspect of wealth management can enable a firm to transform how they interact with their clients in a short turnaround time, enabling agile mobile, online interactions while the wealth manager undergoes crucial future-proofing technology change in the back end.

Personalised Services and Data Analytics

Nearly two thirds of wealth managers (64%) are segmenting their clients and creating unique profile for personalisation, while a third are still lagging⁹. HNWI and mass affluent are calling for better results from active portfolio management and greater predictive analytics and forecasting when it comes to riding peaks and troughs in the market.

Wealth managers need to assess their assets under management, account growth, inflows and outflows across multiple time frames, accounts, sponsors, and managers. Not only are clients looking to pull reports from data, but also to use it to make impactful investment decisions. The bottom line is making the data actionable and meaningful, rather than a spreadsheet of numbers which are tough to draw conclusions from.

Just 40% of HNWI are happy with the personalised offerings from their firms¹⁰. This can be where firms focus their omnichannel efforts to drive engagement while producing personalised offerings that require the advanced technology enabled by APIs.

Open API architecture enables wealth management firms and private banks to integrate and distribute third party offerings in addition to their products to offer greater personalisation and product innovation.

Yet advanced analytics is also being used to improve productivity in the wealth management middle and back offices to improve efficiency and productivity in the engine room.

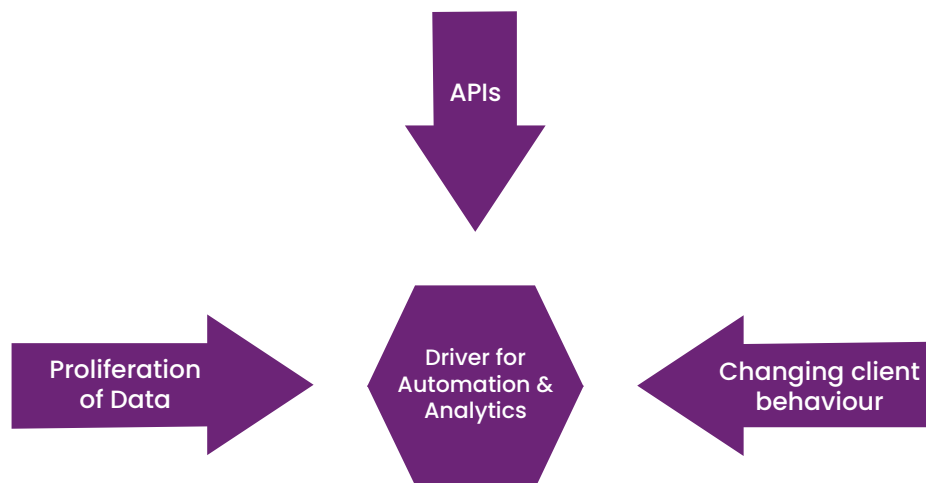
⁹ Forbes, "The Next-Generation Wealth Managers: Advancing Services and Personalization with Technology", <https://www.forbes.com/forbes-insights/our-work/next-gen-wealth-manager/>

¹⁰ Capgemini, "World Wealth Report 2019", <https://www.capgemini.com/es-es/wp-content/uploads/sites/16/2019/07/World-Wealth-Report-WWR-2019.pdf>

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Data and artificial intelligence will continue to play a key role in wealth management innovation, with sophisticated algorithms and modelling allowing for greater service customisation. Today this is being used in tailoring investment solutions to match clients' risk appetite, but its biggest future potential lies in the delivery of more traditional services that rely on a deep understanding of individual circumstances and needs, such as inter-generational wealth transfers, succession planning, and other life events.

Victor Allende, CaixaBank



Automation and AI in the Right Places

While the wealth management space has traditionally been led by, and focused on, the emotional and empathetic abilities of fund managers, the leveraging of technology can be a key method of empowering their decisions.

Wealth management is a sector rich in data whether about markets or – as seen above – data about clients. Combining the two in an intelligent way and communicating that combination to clients can be a differentiator in the market.

Yet AI applications are only as good as the data they use, and the quality of data held by wealth managers is often less than optimal, and rarely resides in a single repository for ease of analysis. Wealth management firms should therefore create a culture of data capture, storage and management across the business.

Automated analysis of data for the sake of it won't yield the right results. To properly utilise the potential of AI, firms need to combine their proprietary data with external information. This comes with its own technological challenges, but the results from such cross-referencing can be substantial.

A front-to-back culture of data analysis needs to be implemented to ensure that the right data is captured and utilised. A lot of automation systems can be lodged in the back office, rarely glimpsed by relationship managers facing clients. Collaboration between relationship managers capturing usable client data and back office analysts collecting external references will drive greater insights and better results across the business.

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There are many buzzwords in the technology space and we are certainly leveraging machine learning and artificial intelligence to improve how we service our clients. Technology itself is an enabler but you need to combine that with intellectual capital and relationships.

We combined our technological prowess with our relationships with liquidity providers to revolutionise how retail investors trade corporate and government bonds, something which was previously a very manual process. This couldn't have been done by technology alone, but it was achieved thanks to our drive and determination to open up access to investment opportunities for our clients

Philip Frijs, Saxo Bank

Conclusions

Between 2018 and 2019, HNWI's trust and confidence in their primary wealth manager and wealth management firm remained at a steady level, at 79% and 82% respectively¹¹. With the industry facing one of its greatest challenges in recent times investment in technology – particularly the right technology – has never been a greater challenge and opportunity.

The wealth management industry can exploit the rise of innovative technology through faster client acquisition, onboarding and servicing. These goals completed will create more time and resources for bespoke and personalised client advisory services, and discretionary wealth management. Eventually, this all lead to a virtuous cycle of client service efficiency and high-quality advice – the cornerstones of a successful wealth management business.

¹¹ Capgemini, "World Wealth Report 2019", <https://www.capgemini.com/es-es/wp-content/uploads/sites/16/2019/07/World-Wealth-Report-WWR-2019.pdf>

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