Australian Wealth Management at the Crossroads

WHERE TO FROM HERE?

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From our Sponsors

Andrew Varlamos, Co-Founder & CEO/MD OpenInvest Limited

"My centre is giving way, my right is retreating...situation excellent, I am attacking" - Message sent by French General, Ferdinand Foch in the early stages of WW1.

I've always liked the wisdom and clarity inherent in that famous quote because it accurately reflects that amidst the challenges, disappointments and setbacks (also known as Life), within us all there is the capacity for decisiveness. For Action.

And the General also reminds us that taking bold action is never more valuable and important than when a situation looks particularly difficult.

Is there an industry in Australia whose struggles are so publicly documented as the wealth management and financial advice sector?

Industry veterans Harry Chemay and Brett Ebedes canvas these challenges in this white paper, but more importantly they also propose ideas and themes designed to help industry participants to look for and craft solutions. Now - rather than all of us waiting until the various policy reviews currently underway release their final recommendations, such recommendations make their way through the political process and the regulatory framework is then possibly changed.

Solutions that will help the 90% of Australians currently not receiving professional help with their financial lives to find that help, in a way that suits them, for a fee they can afford, and from a source they trust.

More than anything, they propose Action, imploring industry participants to work together to try new business models, new technologies and new approaches to address the "advice gap". As a new technology business successfully working with a range of well-established industry participants actively addressing this broad need, OpenInvest is proud to co-sponsor this paper.

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Stephen Handley, Founder & CEO, Fin365 Pty Ltd

In 2008, after a decade of working in the fast paced, high energy USA tech industry, I decided to try something new and joined the family financial planning business.

Little did I know that the "something new" was an industry destined to endure a GFC, FoFA, LIF Reforms, FASEA, FDS, DDO and now QAR. Am I missing anything?

The outcome of the above? A significant drop in adviser numbers means less Australians have access to quality advice, which has become so costly it is unattainable for all those who could most benefit.

With all that in mind, "At The Crossroads" seems a gentle euphemism. After countless conversations with advisers over the past few years, I've heard many more colourful descriptions.

So what to do under such circumstances? Like good financial advice, the first step is to assess the current situation accurately and honestly, so that practical strategies can be put in place to move toward the desired outcome … access to quality financial advice for more Australians.

This white paper encourages the reader to take that first step, while also providing valuable food for thought about the future we should be aiming for and how we might get there.

And in the spirit of making a small contribution, I found the following quote quite apt …

"Everyone feels depressed, angry or frustrated at times; it's a crossroads not a dead end." – Sam Owen

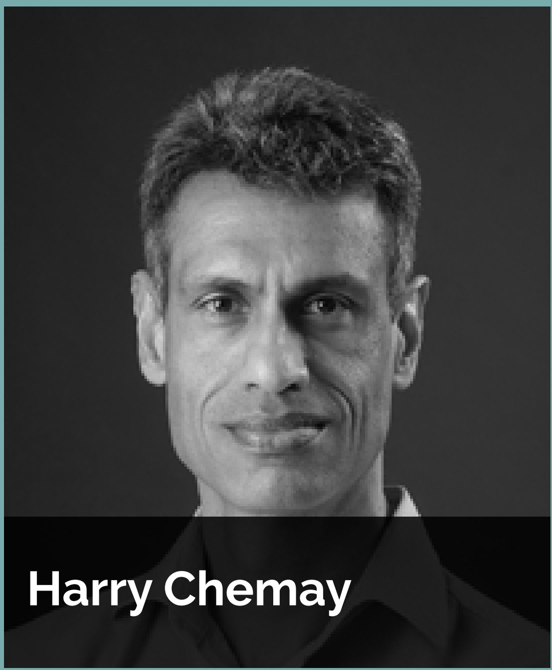
About Fin365

Fin365's innovative software solutions enable high quality financial services to be delivered more affordably, through multiple channels, providing consumers flexibility with how they engage/access services, depending upon the complexity of their needs at any given time.

Leveraging the power of Microsoft 365 enterprise technologies, Fin365 has added the necessary data management, connectivity and functionality required to turn these powerful tools into instantly useful solutions that deliver tangible benefits for financial services businesses and their customers.

Fin365

About the Authors



Harry Chemay has more than two decades of experience across both wealth management and institutional asset consulting. A Certified Financial Planner by his early 30s, Harry practised in the High Net Worth/SMSF space for a decade before switching to institutional investment consulting. He was also a co-founder in Clover.com.au, one of Australia's earliest digital advice services (now owned by SuperEd) where he was a Responsible Manager and Key Person (advice) for the company's AFSL until December 2020.

An active participant within the wealth and superannuation space, Harry is a regular contributor to investment websites in Australia and overseas, writing on investing and financial planning.

He has also been appointed an Australian ambassador to the Transparency Task Force, a UK-led initiative to bring greater transparency and accountability to financial services.

Harry's qualifications include a Bachelor of Business (Banking & Finance major), a Grad. Dip in Applied Finance and Investments – Financial Services Institute of Australasia (former Fellow member) and a Grad Cert in Self-Managed Superannuation Funds. He has previously held the Certified Financial Planner and Certified Investment Management Analyst (CIMA) designations.

About the Authors

Brett Ebedes is a financial services industry consultant who specialises in working with and solving the business problems of financial services participants including licensees, advice practices, platform providers, asset managers and other industry service providers. He also works as a specialist consultant to other management consultancies, offering domain expertise, thought leadership and specialist insights at the intersection of technology, advice and platform.

Brett has more than 20 years' experience in advice and financial technology including having worked at Iress for 12 years where he held the roles of General Manager, National Manager of Australia and State Manager. Brett's remit focused on leading the business unit responsible for product distribution and client service with respect to delivering advice production, regulatory and practice management capability to a large, diverse client base, including some of the largest licensees in Australia through to IFA practices.

Prior to his time at Iress, Brett was Director of Wealth Management for the Major Client Group at NAB / MLC, where he led a team of business development and client success specialists, providing wealth management solutions, with an emphasis on group superannuation and employee benefit programs, to NAB's Corporate Bank clients.

His previous roles include private client adviser, financial planner and paraplanner where he was responsible for providing financial advice as well as assisting with the running of a small AFSL.

Brett's qualifications include a Bachelor of Commerce, Bachelor of Economics, Advanced Diploma in Financial Planning and an Executive MBA from the Australian Graduate School of Management.

Executive Summary

It is indisputable that Australia's Wealth Management sector has not fared well in the past few years. The evidence is as abundant as it is concerning, with industry research house Adviser Ratings recently reporting the number of advisers falling below 16,000 for the first time, having peaked at almost 28,000 in 2019.

Meanwhile the CFA Institute has found that Australians are less trusting of financial advisers than global peers, with only 42 per cent of Australians expressing trust in financial advisers, versus 56 per cent of the global investors surveyed.

The reasons for this decline in trust are many and complex. The GFC-era advice failures; particularly those of Storm Financial and Opes Prime, paved the way for the Future of Financial Advice (FoFA) reforms of 2012-13, and in many ways the advice sector has faced a rolling series of challenges since.

The revelations stemming from the 2018 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Hayne RC) have only added to the sector's woes.

Yet amidst all these demand-side challenges, it is clear that Australians want guidance, direction and advice in what is a challenging financial landscape to navigate unassisted. After all, some 20,000 Australians move into the retirement zone each month, facing a multitude of retirement planning choices in relation to their existing debt, superannuation assets and, for two in every three, the potential of an on-going interaction with the social security system.

Beyond the traditional pre-retirement advice market, the need for advice across differing life cohorts is only growing, with Investment Trends finding in 2018 that almost half of adult Australians were failing to have their financial advice needs met.

One consequence of advice inaccessibility has played out right before our eyes this year, with the unfolding carnage within the cryptocurrency sector highlighting the problems that can arise when individuals attempt to make complex financial decisions without the aid of competent financial advice.

While some of those unfortunately impacted by the crash of several hitherto high-flying crypto tokens (such as Luna and its stablecoin twin TerraUSD) may have had the capacity to seek qualified financial advice, yet choose not to do so, there would have been very many others that might have made different choices - and had vastly different outcomes - had advice been more readily attainable.

The lesson of the 2022 cryptocrash, echoing in a way the Dot Com crash of 2000, is that a lack of accessible and affordable financial advice, whether that be one-off, episodic, scaled or comprehensive, sets people up for outcomes that can be hugely binary; lottery-like payoffs or potential financial decimation.

The challenge the entire Australian financial services sector has, therefore, is to bring the sector's talent, capability and drive together with new and emerging wealth technologies to broaden the reach of quality advice to more Australians earlier in their wealth journeys.

The regulatory landscape will have to move with this zeitgeist, evolving from a 'pre-web' 1990s during which the current laws were first conceived, into a future where the methods of engagement, advice delivery and investment management will be shaped as much by technology as it will by legislative fiat.

Perhaps now, in the wake of the federal election and the recent change of government, is the time to take stock of the decade just past; from FoFA to FASEA to the Hayne RC to Your Future, Your Super and ask: 'have consumer outcomes been enhanced, in aggregate, by the changes since 2012-13?'

If not, and there is certainly ample evidence that it hasn't across very many areas, what then needs to now be done to bring more financial advice to more Australians in a manner of their choosing, at a price that encourages engagement and of a quality that helps rebuild trust in the sector, so that more Australians make better financial decisions, and ultimately, achieve greater long-term levels of financial wellbeing.

That is a question that may be too hard for any one vertical within the wealth management ecosystem to answer; be it funds management, platforms/tech or financial advice.

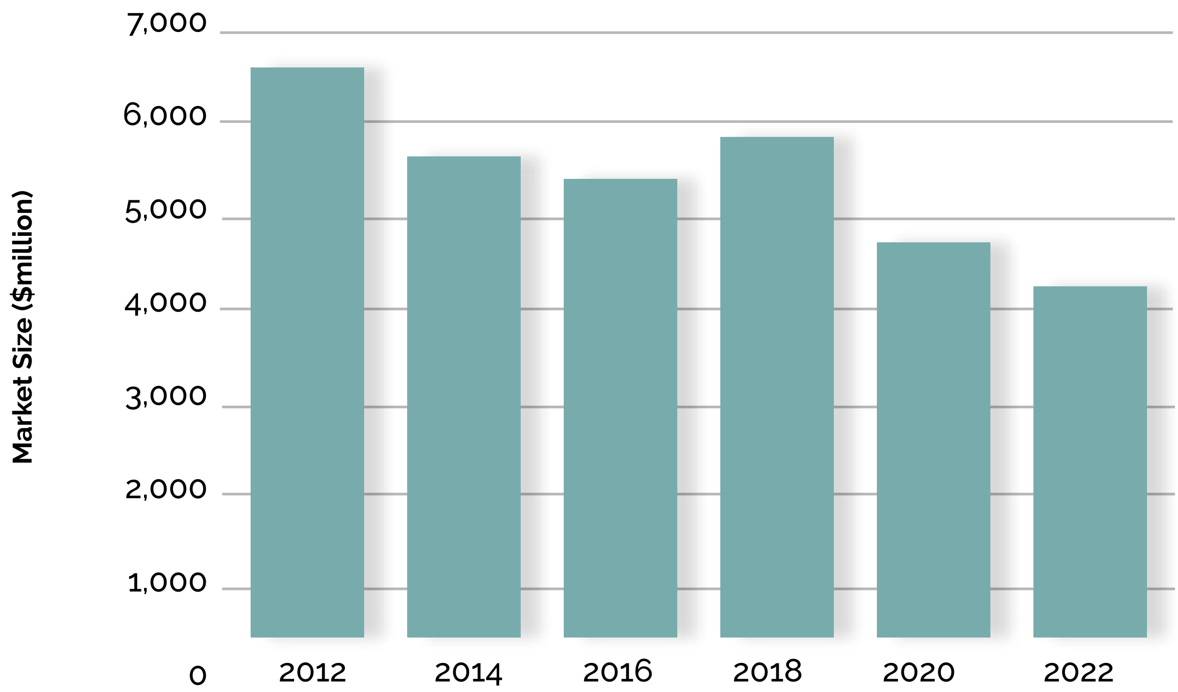
This then is a collective challenge; a challenge that if successfully met will deliver tangible benefits to millions of consumers while simultaneously advancing the wealth management sector into a brighter tomorrow.

The Development of Financial Services in Australia

The financial services sector is a success story with few parallels in the Australian economy. According to data collated by the Financial Services Council [1] (FSC), the sector was worth in excess of $160 billion to the economy in 2019, making it the industry with the largest share of gross value-add in the economy at that time.

In addition, the sector employs over 450,000 individuals, accounting for some 3.5% of total employment, according to the FSC data.

It is also an industry more likely to provide full-time employment than most other industries, spread across the key pillars of funds (asset) management, superannuation, insurance and financial advice.



[1] Financial Services Council, State of the industry, 2019

The Wealth Management Sector

In undertaking any exposition of the Wealth Management sector, it is helpful to first have a clear set of definitions as to its key components.

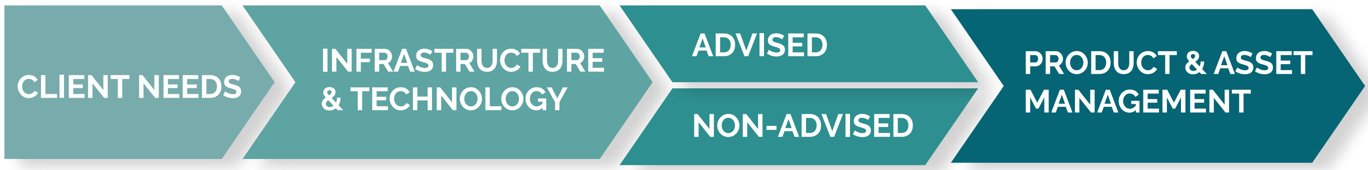
The below definition attempts to do so, such that the content to follow remains consistent in terminology and shared understanding:

'Wealth Management', as used in Australia, is a catch-all term that encompasses those elements of the financial services sector primarily dedicated to the intermediation process that allows individuals to save, insure, invest, build and protect their wealth to meet their personal financial goals and objectives through time.

It therefore can be said that Wealth Management is a term within which resides the key functions of investing, insurance and financial advice. Between those foundational functions sit an enabling infrastructure of service providers including:

- Custodial services
- Unit pricing/registry services
- (Non-super) unitholder / (super) member administration
- Exchanges (securities, forex, commodities, crypto)
- Brokers providing access to exchanges
- Investment platforms
- Insurance companies (both life and general)
- Asset consultants, ratings agencies and investment research houses
- Financial advice technology services, including the following:
    - Client Relationship Management (CRM) systems
    - Financial modelling, product research & Statement of Advice (SOA)/Record of Advice (ROA) generation
    - Client engagement systems such as online fact finds & client portals
    - Revenue management
    - Compliance and practice management services

Taken together, the value chain of Wealth Management can simply be depicted as:



The Financial Advice Sub-sector

The nexus between the giving of advice and the acquisition, disposal or transfer of financial products (or interests therein) is readily apparent insofar as the definition of 'financial advice' in the Corporations Act 2001 makes specific reference to financial products.

Thus, the Corporations Act refers to 'financial product advice' [2], and defines the elements that would lead to an act or action being classified as such.

An alternative definition of financial advice can be found in frameworks established by various financial planning professional associations. One that is commonly quoted is the Six Step process adhered to by members of the Financial Planning Association (FPA) as follows:

1. Defining the scope of engagement
2. Identifying client goals
3. Assessing the client's financial situation
4. Preparing the financial plan
5. Implementing the recommendations
6. Reviewing the plan

While the above is a useful guide to the process of financial planning, it does not provide a clear explanation of what financial advice actually is.

For the purposes of this White Paper, reference to 'financial advice' will be taken to be reference to 'financial product advice' as contained in the Corporations Act, broadly being a recommendation or a statement of opinion, or a report of either of those things, that is intended to influence a person in making a decision in relation to a financial product (or class of product), or could be seen as intending to influence said person.

[2] Corporations Act 2001, Section 766B

What is (and is not) advice?

One of the key distinctions in the legislative framework as it applies to financial advice is between 'general' and 'personal' financial advice.

Personal financial product advice, as defined above, it is taken to be advice provided with consideration to one or more of an individual's objectives, financial situation and needs [3]. Where advice is provided without such consideration, it may be considered to be general advice.

Both personal and general advice are distinct from the provision of factual information, generally the provision of objectively ascertainable information, the truth or accuracy of which cannot reasonably be questioned.

As the provision of factual information is not considered to be advice, the regulatory obligations are significantly different, however it is incumbent on the provider of said information not to stray into the making of a recommendation, or the expressing of a statement of opinion, in respect of a financial product without the appropriate licensing and authorisations in place.

The reality of the financial landscape in Australia today is that those who offer financial advice are likely, in the course of interacting with advice seekers, to be given personal information that could be taken to form the objectives, financial situation or needs of the advice seeker.

Once in possession, any advice that takes into account one or more of these is 'personal advice', the compliance bar for which has lifted substantially post-FoFA. The existence of a 'Best Interests Duty' (BID) compels the advice provider to acts in the best interests of the client in relation to the advice provided [4] .

Perhaps the greatest area of contention since the introduction of the BID revolves around the 'safe harbour' provisions of Section 961B(2), which involves a series of highly prescriptive steps needed to be undertaken for a provider to establish, prima facie, that advice was provided in the best interests of the client.

The final step, a so-called 'catch all' provision has proven highly divisive within the financial advice sector, leading many to take a highly cautious approach to advice provision in order to stay within the letter of the law.

[3] Corporations Act 2001, Section 766B(3)(a)
[4] Corporations Act 2001, Section 961B(1)

Comprehensive versus scaled advice

One unintended consequence of this cautionary mindset since the introduction of BID has been the reluctance by many advice businesses to provide anything other than comprehensive financial advice.

Such advice seeks to take into account a client's total financial affairs; typically covering insurances, superannuation and non-superannuation assets, retirement planning/post-retirement pension strategies, and very possibly estate planning all within one comprehensive Statement of Advice.

This response to BID, while perfectly rational from a risk mitigation perspective, has resulted in advisers seeking to provide comprehensive personal advice as the surest way to be in compliance with BID. This despite guidance from ASIC that robust, high quality personal advice need not only be comprehensive in nature.

ASIC holds that advice can be 'scaled' according to a client's requirements, and its views are articulated in Regulatory Guide 244 on the matter [5]. The guide makes clear that all advice is either less or more comprehensive in scope along a continuous spectrum, and goes as far as to indicate that once an adviser has identified the subject matter of the advice sought, it is possible to limit the scope of advice within this subject matter to a single issue [6].

The current tendency to preference comprehensive personal advice over scaled personal advice, with all the cost/complexity it entails, speaks more of a widespread misplaced perception within the advice sector of ASIC's 'expectations', possibly hardened by the events of the Hayne RC and its aftermath.

This view must shift if advice is to be made genuinely accessible to more Australians.

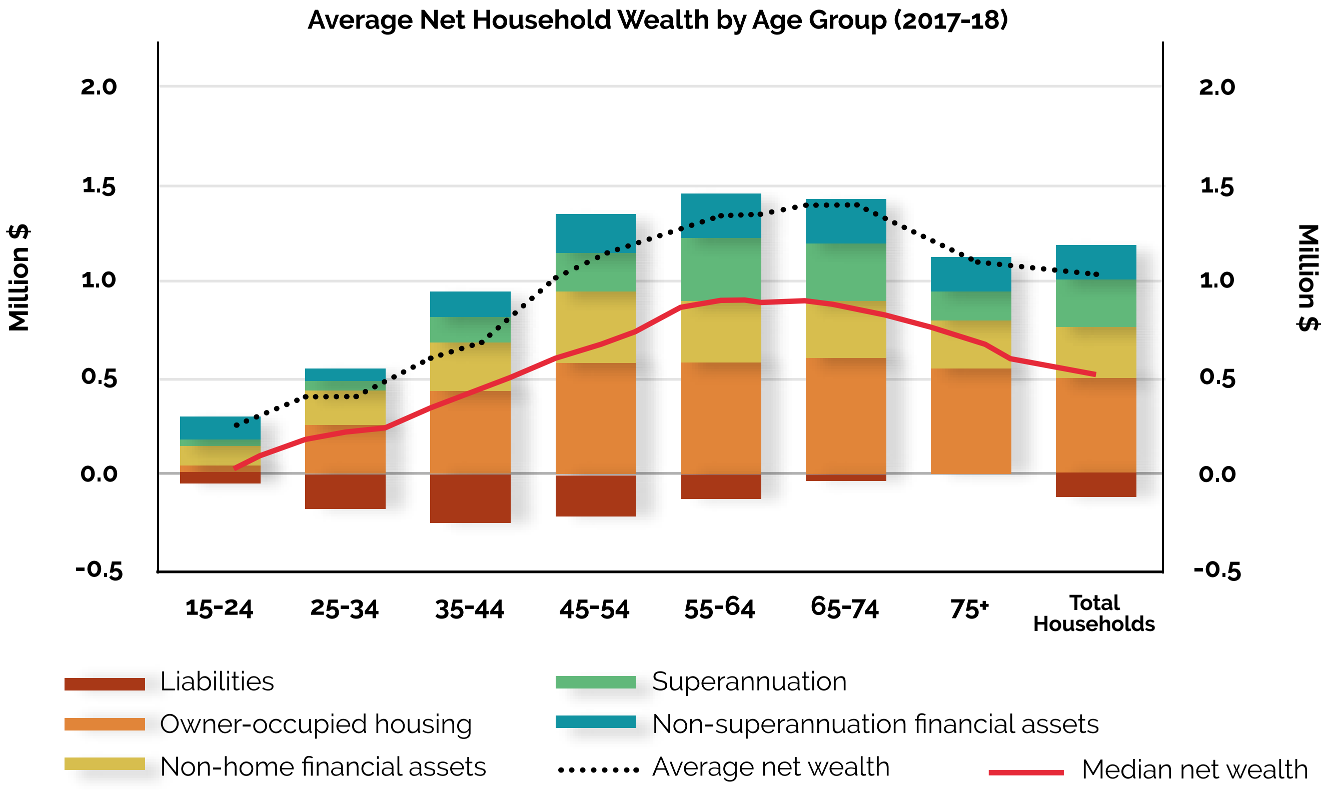
[5] ASIC, Regulatory Guide 244, 'Giving information, general advice and scaled advice', December 2012
[6] Ibid, RG 244.65

The Economics of Retail Wealth Management

Advice in Australia

Australians are amongst the wealthiest citizens in the world today. Research by global banking giant Credit Suisse[7] ranks Australia as the country with the highest median wealth, at USD $273,900 per adult, ahead of other highly developed nations such as Belgium, Hong Kong, New Zealand and Denmark.

Much of this household wealth is concentrated in residential property, the value of which now is close to $10 trillion. In addition, the nation's superannuation system, now almost 30 years in its modern conception, broadly adds a further $3.5 trillion to household wealth. Together with direct holdings of managed funds, equities and other securities, as well as other forms of wealth, the average household net wealth by decile is outlined per the chart below:



7 Credit Suisse Research Institute, Global Wealth Report, 2022

The Australian financial system is also somewhat unique amongst global comparators in that the architecture of the defined contribution-centric superannuation system places a high burden on the individual to make decisions and execute choices in respect of their own retirement.

Thus, in addition to a range of financial decisions Australians have to make in respect of banking and credit products, insurances and mortgage products, the need to interact with one's superannuation throughout one's working life should underpin demand for financial advice in Australia.

Given the above, it is therefore concerning that the obtaining of financial advice has reduced rather than grown in recent years. According to financial services research house Investment Trends[8] the number of active financial planning clients declined from 3 million in 2007 to 2.3 million in 2016. As a percentage of the then adult population, this would suggest a decline in the demand for advice from around 20 per cent to 15 per cent during this period.

A more recent attempt to quantify the demand for financial advice in Australia was undertaken by ASIC[9] during 2018-19 via a survey of over 2,500 Australians. Somewhat consistent with the Investment Trends data, ASIC's 'Financial Advice Report' found that 27 per cent of respondents had received financial advice in the past. Crucially however, only 12 per cent had received advice in the preceding 12 months.

The survey also found that while 41 per cent of respondents intended to get advice at some point in the future, 20 per cent had considered getting advice in the preceding 12 months, but had declined to do so.

Cost and Trust – The Key Barriers to Accessible Advice

ASIC's Financial Advice Report also provides a degree of insight into other barriers constraining the demand for advice. Two of the most problematic, from the perspective of the Australian wealth management sector, are cost and trust.

High Cost of Accessing Advice

The ASIC report notes that of the top 10 barriers to getting advice, "too expensive" was cited as a reason not to engage with an adviser by 37 per cent of respondents.

Overall, 64 per cent of all the survey participants felt that financial advisers were too expensive.

That is supported by the 18 per cent who couldn't see the value in consulting a financial adviser, and 29 per cent who felt that their financial circumstances were too small to warrant advice.

A recent financial advice consumer survey conducted by Adviser Ratings found that 65 per cent of prospective clients would only pay $500 per year for advice.

[8 & 9] ASIC Report 627 Financial advice: what consumers really think, August 2019

By contrast, the research house found the median annual ongoing fee for providing financial advice has risen to $3,529, a 41 per cent increase from the previous corresponding period.

When combined with a recent KPMG research[10] report finding that the cost of comprehensive personal advice production is broadly $5,330 at present, it becomes abundantly clear that the 'total addressable market' for financial advice in its current format shrinks dramatically, as prospective clients either with lower investible assets or simpler financial needs are effectively priced out of the advice market.

Trust Issues

Trust is the other key factor in determining access to advice. There is little doubt that trust continues to be a significant concern for Australians in engaging with the advice sector, particularly since the revelations that surfaced during the Hayne Royal Commission.

The ASIC Financial Advice Report found that, when asked about their level of trust in advisers, only 14 per cent of participants responded that they had "a great deal" of trust in advisers, while 15 per cent responded "none at all" and 34 per cent "a little".

That is gravely concerning, given the amount of remediation effort underway, some of which precedes the royal commission. It also, in a way, speaks to the lack of 'cut through' the advice sector has had in communicating its message of reform since the Hayne RC's findings, or that the key transgressors uncovered during the hearings, the major banks, have since substantially reduced the provision of financial advice, mostly through divestment of their financial planning dealer groups.

The post-Hayne RC advice landscape of 2022 bears less resemblance to the industry to which Commissioner Kenneth Hayne cast his forensic eye, and more to the pre-2000 era preceding the 'bancassurance' merger frenzy as each of the four major banks aggressively expanded into superannuation and investment management, and by extension, financial advice as a distribution channel for both.

This issue, whilst prevalent across the major banks, was not unique within the industry, with several other major players distributing product in a vertically integrated manner under the auspices of advice.

The paradox of the four major banks ceasing to be significant participants in financial advice is that the power attached to their brands also ceases. This creates a dilemma for the advice sector in rebuilding trust, insofar as none of the non-institutionally owned dealer groups has, on its own, a presence that can be amplified through brand awareness, or the marketing budget to build such a presence.

The following breakout box outlines some of the issues this lack of brand power surfaces.

[10] KPMG Research Paper, 'Cost Profile of Australia's Financial Advice Industry', August 2021

The Importance of Branding in Wealth Management

Modern financial decision-making is replete with complexity, and the cost of error can be significant, both at the individual level and in aggregate at the societal level.

Receiving professional advice therefore can make sense for the very many individuals who are daunted by the prospect of 'owning the decision'. However, a challenge in any industry, never mind one dealing with consumers potentially 'handing over' a high proportion of their hard-earned savings, is the value a consumer places in a brand.

Whether conscious or otherwise, brands underpin consumer trust. The 2021 Edelman Report , surveying 14,000 consumers in 14 countries, confirms that 'highly trusted brands are seven times more likely to be purchased'. Brands signal trust and confidence and underpin a set of expectations a consumer should be able to access by selecting one brand over another. Whether conscious or otherwise, branding plays a significant role in consumer decision making and organisations across all industries spend a tremendous amount of resources positioning and promoting their brand accordingly.

The challenge here, however, is advice remains largely a brandless industry, which has been compounded by the departure of the banks. Consumers have also grown more wary of the association of a financial brand and its related distribution channels i.e. vertical integration, which was also placed under the microscope, albeit for full public view, during the Hayne Royal Commission.

Advice as an industry has not sought to address the brand awareness issue, be at a firm level or professional body association. Rather the industry operates on the basis of a client to adviser relationship as the medium of trust. This may work when a client meets with an adviser and gets to know them, but it does not get the client in the door, especially when a given client does not know where to get advice.

Moreover, professional bodies have not extolled the virtues of their associated branding (eg CFP) in the consumer domain as effectively as they might have. The 'brand' of advice should ideally be tied to one or more professional associations, as this is far more tangible to a consumer than a license under one of many AFSLs.

The Supply of Financial Advice

The ascent of financial advice in Australia has broadly paralleled the growth of superannuation over the past 30 years, as the complexity inherent in Australia's retirement system lends itself to the seeking of professional counsel.

At their zenith (prior to the Hayne RC), the five largest advice entities (the big four banks plus AMP) accounted for over 40 per cent of the sector, measured by advisers operating under a AFSL they controlled. The 10 largest entities had close to 60 per cent of authorised representatives. In June 2017 ASIC had some 25,000 individuals listed on its Financial Adviser Register.

The supply dynamics for financial advice has seen a drastic reversal since the findings of the Hayne RC and the legislation passed in its wake, with the next section outlining in greater detail the subsequent decline in numbers to the current 16,000-odd individual advisers.

A struggling advice sector impacts not only advice dealer groups and practitioners - and ultimately consumers who would almost invariably be better off by seeking advice - but the entire supporting service ecosystem including platforms, technology solution providers and compliance/CPD providers.

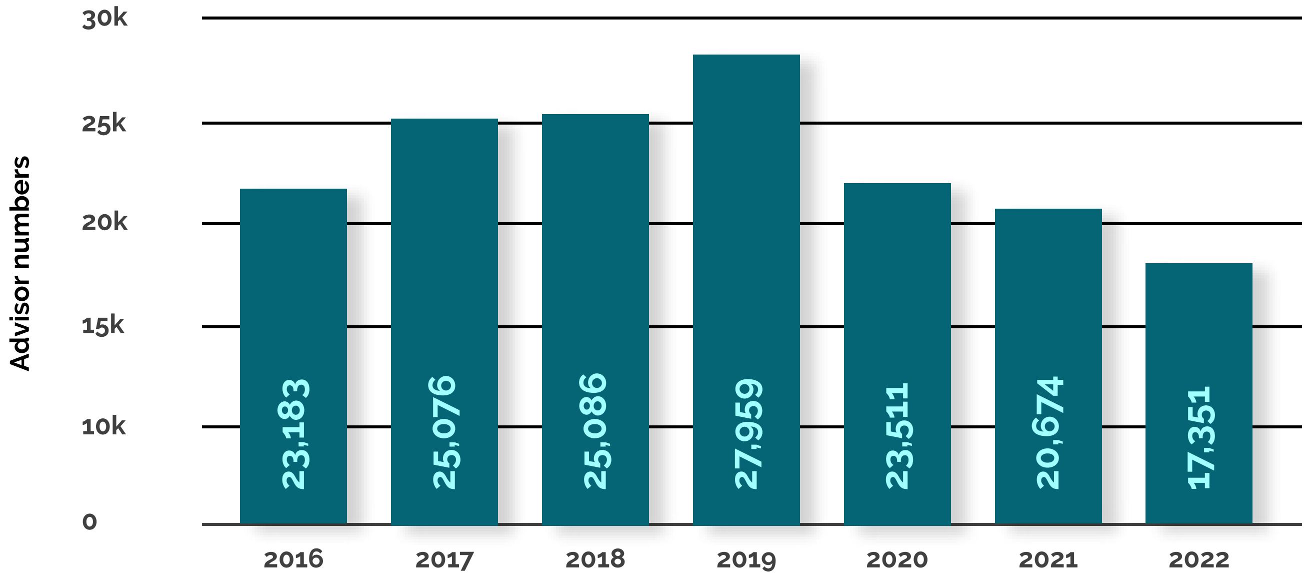
The majority of managed investment flows in Australia are still intermediated via the financial advice sector. Some 86 per cent of the $2.5 trillion dollar domestic fund management industry is currently invested at the direction of financial advisers [11] .

Given the dominance of advice intermediation, wealth management service providers and participants have a vested interest in the success of the advice sector.

It is thus unfortunate that, despite a thriving advice sector being beneficial to the entire wealth management sector, the advice problem is seen in isolation: if consumers don't seek advice, it's seen as a problem for the advice side of the wealth management industry.

As adviser numbers continue to fall there will be less demand for all supporting services to the advice sector, fewer recipients of advice and potentially increased cost for the supply of all of these services including advice itself, a trend already underway.

[11] Source: Professional Planner September 28, 2021; Report 702 Competition in funds management presents findings from independent research by Deloitte Access Economics, September 2021



The Australian financial advice headcount, which at one stage boasted approximately 28,000[12] practitioners in various forms, is today in steady decline, with less than 16,000 licensed advisers at present.

Of these, there are in the vicinity of 11,000 full-service practitioners and it would appear those leaving the industry are doing so at a faster rate than new entrants are joining, with a recent Adviser Ratings report noting that at present there are six advisers leaving the advice industry for every new entrant.

[12] Adviser Ratings, 'Adviser Musical Chairs Report', Quarter 4, 2021

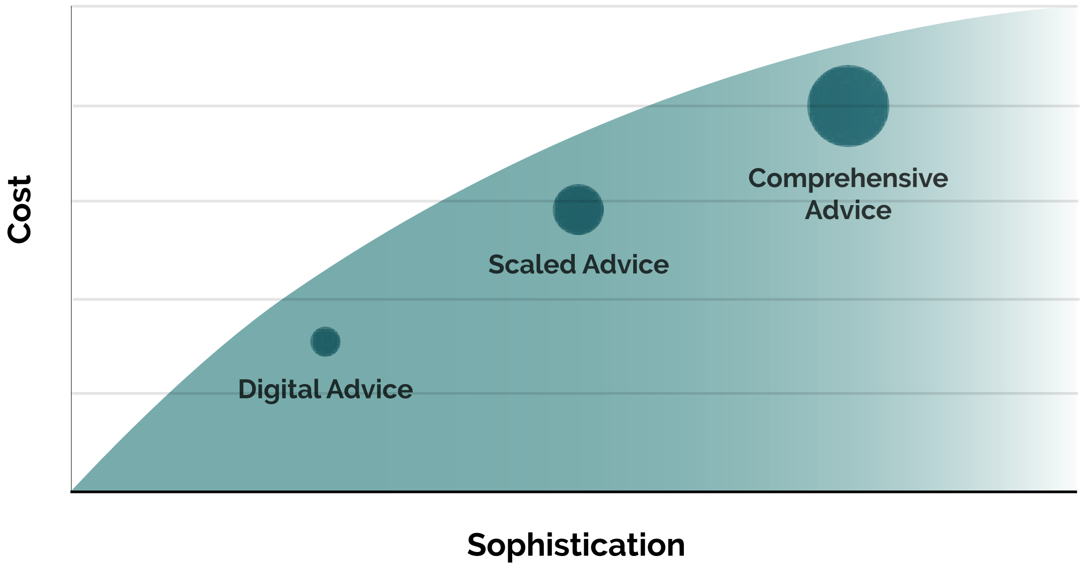
Enabling Infrastructure and Technology – The Critical Data Piping

Advice can mean different things to different people. Whilst it is clear that many people do not understand what a financial adviser does, seeing one is not the only way to receive some level of guidance. With industry cost pressures and supply side factors making advice less attainable for certain cohorts of potential consumers there are alternatives that fall within the advice spectrum, including digital advice.

Technology plays a pervasive role in our lives and its implications for finance have been building for many years, disrupting the way consumers engage with financial services.

From online banking to stockbroking, which had its genesis in Australia in the mid 1990s, digital finance has become a way of life and this is set to continue as solutions become increasingly more sophisticated and cost effective. The concept of digital financial advice is not new, the earliest iterations of which in the US date back to the 1990s.

The introduction into Australia circa 2015 of the first iteration of digital advice concerned licensed advisers, who questioned whether in time they might be replaced by a 'machine'. However, there is increasing appreciation that advice operates along a spectrum of solutions, catering to different cohorts of consumers along a continuum of cost and sophistication.



This can be shown, as depicted in the above graphic, as a series of alternatives for receiving advice, rather than a mutually exclusive set of solutions.

The consumer who starts with a digital channel may skip to comprehensive advice or first have a scaled interaction or vice versa. That is, advice needs to be delivered flexibly and there is no reason why each channel or type needs to be seen in isolation.

The important part is the advice journey has started and consumers should be able to move in either direction along this advice continuum, at different points in time, depending on personal circumstance.

The high levels of online trading and interest Australian investors have shown for share ownership and more recently cryptocurrency, indicates there is demand for investment solutions. And while these may be a far cry from a comprehensive financial planning engagement, which goes well beyond an investment service, consumers clearly want to increase their wealth. This is not a surprise. There is however a significant difference between speculating - be it taking positions in equities with little foundational understanding or a punt on a cryptocurrency.

The improbability of getting lucky with a speculative position aside, the advised scenario, even via a digital channel, has the advantage of research and diversification. Unfortunately, despite the proliferation of technology in our lives, digital advice solutions are yet to have the anticipated consumer take-up (or human advice replacement capability) given how technology has rapidly developed in other facets of our lives.

With technology permeating virtually all aspects of our lives, it is safe to assume that digitalisation will filter even more deeply into finance and investing. Whilst it is arguable that robo-advice or digital investing is a natural starting point for seeking advice by creating consumer awareness, it has not had the desired take-up rate, with the correlation between starting with digital advice and going on to receive scaled or comprehensive advice as yet unproven.

The possible reasons for the low adoption rate of digital financial advice include:

Trust: many people are reticent to trust their wealth to a 'machine'. They may be curious enough to start the "robo" journey, however the drop-off rate at the final screen (commitment) stage is inexorably high. This may in part be due to brand and trust issue mentioned previously.

Apathy: even in superannuation, where the money is already invested and the choice is to select a fund option with more relevant (to the superannuant) risk-return outcomes, there is tremendous apathy and most superannuants stick with the default option. Ironically, there is still significant use of online trading exchanges, be it, equities or crypto, which are less about advice and more oriented towards speculation.

Fairly or otherwise, roboadvisors have up until now been seen as "lite advice" options – with algorithms performing a risk profiling function to map a client's risk parameters to an aligned portfolio such as a model portfolio via a managed account or ETF.

The salvation of robo advice, however, may come in the form of high-profile brands moving into this space, overcoming the aforementioned trust and brand issues. This certainly appears to be the case in other jurisdictions where, unshackled by the need to generate SOAs that take into account a user's personal circumstances, roboadvisors have gained greater traction.

If we look to the US market, every major wealth manager / stockbroker is growing their presence in the digital investment market. The intent is to reach a different demographic, investors who are tech-savvy, comfortable engaging without human contact, and are looking for professional investing help. What is most significant in contrasting this US experience with the current situation in Australia is the nature of the entities – and their associated brand equity – who have entered this market, names that include JPMorgan, Merrill Lynch, UBS, Morgan Stanley, and Goldman Sachs.

The brand awareness these organisations enjoy are amongst the highest in finance, and they are keen to expand their geographical reach beyond their home markets. The very nature of their offerings is highly scalable and able to be exported and customised as required.

US roboadvisors have also helped lower the bar for minimum viable 'funds under advice' client thresholds, with some offering access to investors with as little as $1,000 in investable funds. This has the potential to be a game-changer for Australian investors but it may not, in and of itself, solve the broader under-advised problem or be the magic pill the advice sector might hope it to be when used in a hybrid context.

The ability for digital financial advice to play a role in closing the advice gap is thus real but nascent, given the inherent limits to complexity any algo can reasonably be expected to address, and the regulatory environment that makes Australia one of the hardest markets into which to launch a robo-advice offering.

The Dominant Business Model. Is it Sustainable?

Australian advisers have had to endure years of unprecedented regulatory change from FSR to FOFA to the Hayne Royal Commission and consequently FASEA. The intention was to improve consumer outcomes and therefore confidence by ensuring advisers are better educated and trained; act in the best interests of consumers; restrict their ability receive conflicted commercial incentives including product commissions; and transition from an industry to a profession.

These reforms have been deleterious to both revenue and cost, with Business Health[13] revealing a reduction in advice business profitability from 27 per cent in 2017 to 24 per cent in 2021. The removal of conflicted remuneration, particularly commissions, was significant, however most businesses simply replaced commissions with alternate charging methodologies with much the same effect.

Whilst it would be expected a fee for advice or service model would prevail, for many advice firms the removal of commissions became a 'lift and shift' approach to asset based fees within a platform, which have many of the same hallmarks of a commission.

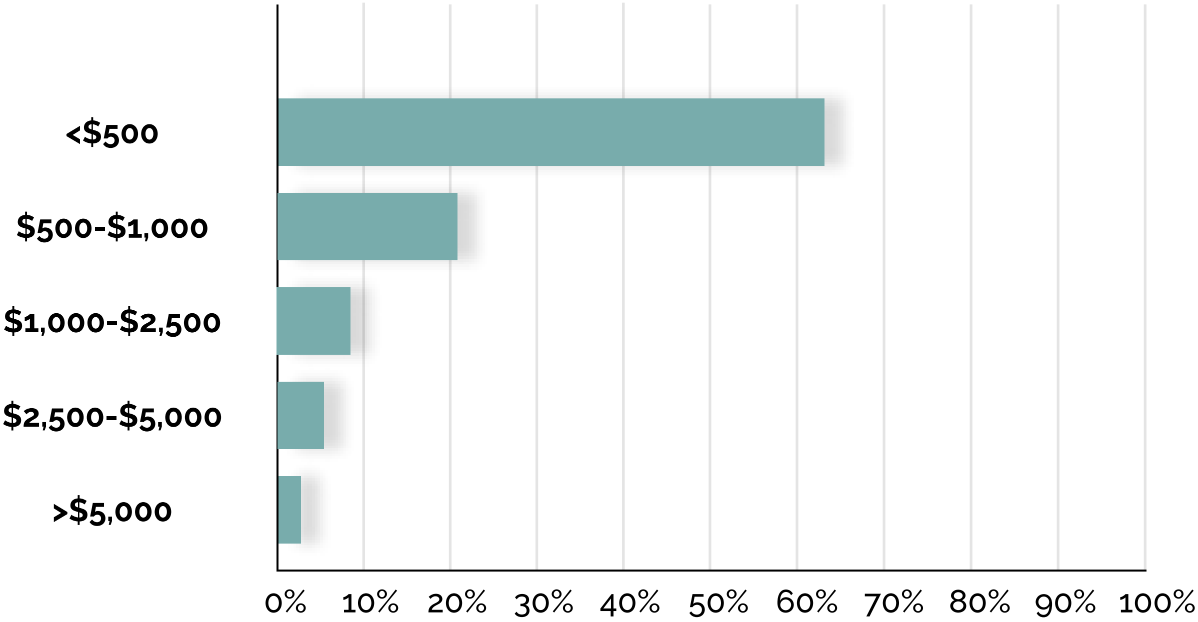
In adjacent professions a fee is rendered for a piece of work. Most, other professional services do not have a perpetual subscription fee. More progressive firms have realised this may not be what their clients want, and have instead offered some clients episodic fees for specific pieces of work or time based services. This makes sense in cases where consumers essentially

[13] Business Health 'FutureReady IX Report',January 2022

have a set and forget strategy in place, particularly in the retirement stage, and find it hard to justify paying subscription fees.

One of the barriers to consumers seeking advice is cost and this has been highlighted as a preventative factor in consumers seeking advice. Adviser Ratings[14] highlights the willingness to pay problem,

There is no doubt that the long tail of repeated regulation has increased cost for advice firms. Statements of Advice are complex and voluminous and as such take time to produce. In this context, the Levy Review draft proposal 9, to remove the requirement for SOAs in favour of written records of advice provided available on request, will be keenly followed.



with 61 per cent of surveyed consumers believing advice should cost under $500pa. 22 per cent said they'd pay up to $1,000 annually, while less than 10 per cent said they would pay up to $2,500 a year.

Only 5 per cent said they would pay between $2,500 and $5,000 pa, while just one in 40 said they would pay more than $5,000.

With the average cost of delivering comprehensive advice estimated to cost between $3,000 and $5,000, there is a significant disconnect between cost of provision and willingness to pay.

The aforementioned Business Health reports supports this, whereby advice firm average revenue has increased very slightly, yet profitability has fallen as costs have risen whereby average "notional expenditure of each business is now $813,247 [in 2021] up from $758,261 in 2019".

Whilst advice firms have responded in different ways to business pressures, from increasing fees (where possible) to squeezing suppliers, there still remains an opportunity for improved practice management to enable better business efficiency.

[14] Adviser Research data consumer survey of 1500 Australians, 2022.

Driving efficiency and reducing cost via technology

Few would argue with the assertion that technology is the key to improving business efficiency and driving down the cost of advice. Historically, however, financial services businesses have failed to derive maximum benefit from technology, likely due to one, or more, of the following:

- The broad and complex nature of the data required for the delivery of financial advice and practice management;
- Different business needs between dealer groups (who often controlled technology decisions) and advice firms;
- A lack of integration between their software systems; and
- A belief/desire that an all-encompassing "silver bullet" software solution will come along to fix everything.

Predicated on driving business efficiency through practice management is the effective use of industry specific software or customised generic solutions, generally structured around advice CRMs.

The better options within these offerings enable business management capability. Yet, most advice firms fail to capitalise on the depth of capability available.

The above issues have led most firms to lack a cohesive technology strategy and are therefore not optimising technology, which ultimately leads to a reduction in customer experience, business efficiency and quality assurance. Referring again to data from Business Health:

- 9% of businesses are now using more than one CRM system
- 5% of businesses only update their CRM system on a monthly basis and 9% process changes to their client data when they have time to do so
- 77% of businesses store the names and details of prospective or potential clients on their core system
- Only 4% are holding 20 or more individual pieces of information on each of their key clients. 35% still store fewer than 15 data points and quite often it is the more personal, key relationship building information that is missing
- Only 55% of businesses use workflow management.

The technology industry has not been a lighthouse beacon in helping advisers better navigate the complexities of technology. Rather it has often added to the confusion and frustration by frequent overpromising and underdelivering. In Oct 2021, KPMG reported there were 718 active Australian fintech companies[15] . Despite this plethora of choice,

[15] Australian fintech landscape 2021 - KPMG Australia (home.kpmg)
[16] Adviser Ratings – Financial Adviser Landscape 2022

the 2022 Adviser Ratings Landscape report[16] showed ongoing dissatisfaction with the most commonly used software solutions.

Technology underutilisation makes a business more prone to error, reduces enterprise value and task efficiency, including the time-cost in producing written advice, the main tangible 'product' provided to a prospective client.

Business inefficiency thus perpetuates the cost problem, borne by consumers who in the main have rejected 'the value of advice'.

Achieving advice delivery efficiency is multifaceted. Utilising advice technology for back-office and middle-office capability is important, but having a clear data strategy and multifaceted value proposition also make a significant difference.

There are next-generation CRM and SOA preparation systems available now at little incremental cost. It is thus possible for an advice business to offer an omni-channel solution to existing and prospective clients even with existing technologies, provided they are fully utilised.

Targeting a new type of client

Many advice businesses have a website onto which suppliers can embed a basic robo solution at an attractive price point. Prospective clients can start their advice journey with a less intimidating digital experience. For more complex needs, a scaled or episodic advice scenario may suffice, which may be delivered efficiently by using digital data solutions, either an electronic fact find or by leveraging data already obtained should the client have started with digital advice. The technology that underpins this is available now.

If advisers don't take advantage of this, others such as superannuation funds will, as they already hold extensive member data in registry systems.

The age of advice is no longer about a one size fits all model. By leveraging technology, a multi-faceted omni-channel advice solution can be accessible cost effectively, helping transform advice businesses to reach more clients at different stage of the advice journey and in a cost-effective manner.

Wealth Management Reimagined

Much of this paper thus far has dealt with identifying the factors involved in the current difficulties being experienced within wealth management more broadly, and financial advice specifically.

To recap, the financial advice sector is experiencing what can be described as a form of market failure, insofar as market demand for the type of advice now favoured by the industry, comprehensive personal retirement planning advice, is severely limited by the cost of supplying it, now often exceeding $5,000 for an initial engagement and $3,000 in annual service fees thereafter.

In short, it is only in wealthy pre-retirees with complex retirement planning needs where the service that the financial advice sector offers currently intersects with a willingness and capacity to pay. If one were to assume this cohort represents 20 per cent of those approaching retirement each month, this equates to only 4,000-odd prospective clients for the nation's 16,000-odd advisers to engage with and compete for on a monthly basis.

It should be apparent that the entire financial advice sector chasing this same small addressable market is not a recipe for sustainability, let alone organic growth.

So what might an alternative future for Australian wealth management look like? And what are the conditions precedent in order to facilitate it? The following are suggestions that we believe will assist the financial advice sector to regain lost ground and, more importantly, create the foundations for sustained growth into the future.

Applying the Tinbergen Principle to Financial Advice

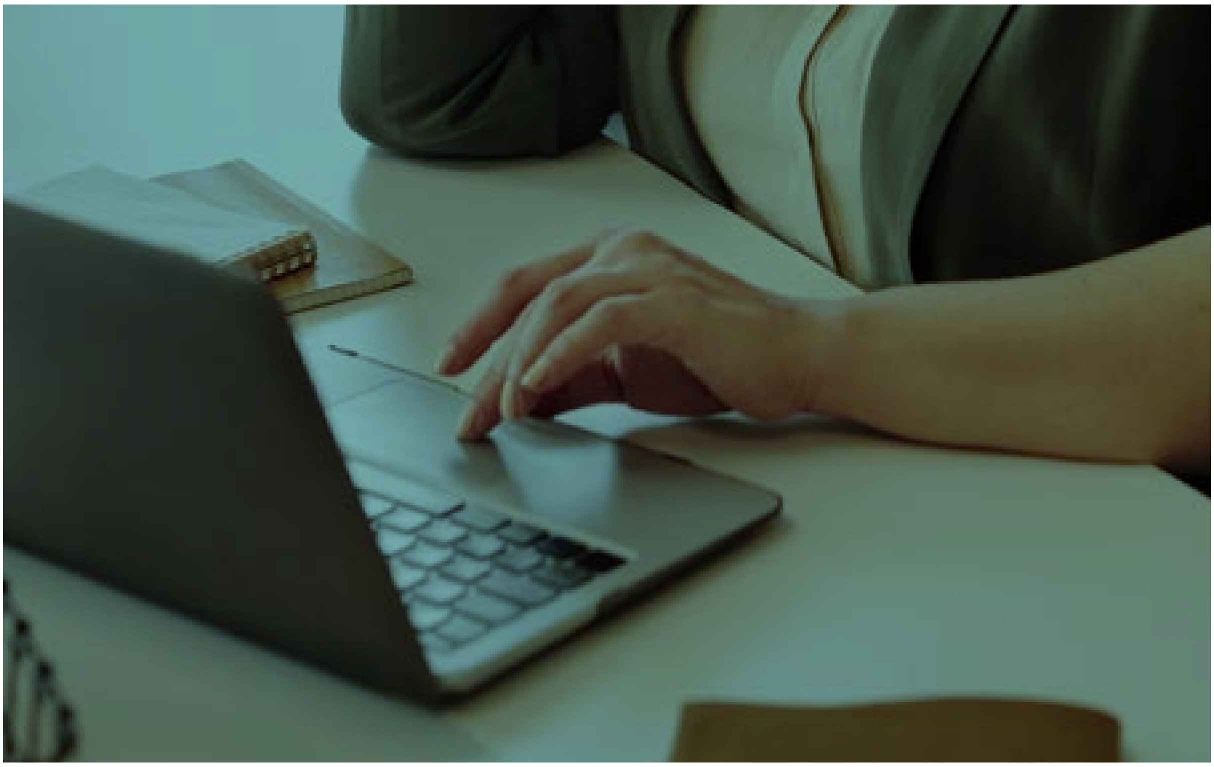
The Tinbergen Principle is named after Dutch economist Jan Tinbergen, the first economist to be awarded the Nobel Prize in Economics. In essence the principle states that in addressing complex economic dilemmas, sustainable solutions require as many instruments as there are policy objectives.

Which is a very fancy way of saying “one size does not fit all”.

In relation to financial advice, there is one dominant ‘instrument’ being bluntly applied to the varied advice needs of Australians of varying demographics, socio-economic circumstances, financial literacy, engagement preferences and price point sensitivities.

This instrument is comprehensive pre-retirement personal advice encapsulated in an unwieldy SOA, implemented via an adviser-directed investment/super solution with ongoing fee arrangements still dominated by the percentage of ‘Funds Under Advice’ (FUA) model.

The advice sector could continue with this approach, and it would almost certainly perpetuate the issues currently constraining advice accessibility, as well as its own growth prospects. Or it can choose a different path.



Matching Advice Models to Consumer Needs

There needs to be a recognition that Australians engage with the financial services sector across multiple decades in ways that shift over that time-span. Their needs differ according to their life-stage, and forward-thinking advice models ought to be able to cater for these life-stage cohort preferences.

In addition, research into engagement preferences suggests that consumers have varied preferences as to how they choose to engage with their finances, and a 'traditional' financial advice relationship with a financial adviser is now but one such option.

The ASIC Financial Advice Report of 2019 found 31 per cent of those surveyed said that they had received financial advice or guidance from family, friends or colleagues, while 23 per cent had done so from information found online.

Similarly, even when consumers become engaged with their finances, there are a range of preferences that extend beyond receiving financial advice and/or outsourcing complex financial decisions to an adviser.

At the High Net Worth end of the market, CBA research into SMSFs[17] found that only 22 per cent of survey respondents were 'Coach Seekers' and 13 per cent 'Outsourcers', those more likely to engage with financial advice on an ongoing basis.

Quite remarkably, 30 per cent described themselves as 'Self-Directed Investors' with a preference for a DIY approach toward financial decision making, while 35 per cent were 'Controllers', eager to do things themselves, but open to some advice to support their decision-making. For these individuals an online SMSF admin solution, coupled with a next-gen investment platform and some episodic advice from a Financial Adviser may be all that is required to meet their needs.

Thus, right across the age and wealth spectrum, from Gen Z commencing their wealth journeys to wealthy Baby Boomers with sizable assets in their SMSF, the notion of 'one-size-fits-all' is readily disabused.

What therefore is needed is a breath of ways to engage with the varying advice needs of consumers across life-stage and wealth cohorts.

The proposals outlined in the draft Quality of Advice Review report notwithstanding, changes to the legislative framework, in particular the way many licensees have chosen to implement a particularly rigid interpretation of the Best Interest Duty and scaled advice, technology presents the best opportunity to close the advice gap in the short term.

[17] Commonwealth Bank, 'The SMSF Report' Edition 1, 2017


BTC / USDT

Technology to the Fore

The rapid adoption of all things digital in daily life, since the initial COVID lockdown of March 2020 points to the possibilities for advice productivity that is still very much untapped within the sector.

Workarounds to lockdown, such as online virtual advisor/client meetings, the rise of electronic signatures over 'wet ink' and the improvement of adviser/client interactivity within leading-edge investment platforms allow advisers to better leverage their time and resources.

These developments will not regress in a post-COVID world.

Rather, forward-thinking licensees and advice practices need to revisit the entirety of the FinTech and AdviceTech landscape to look for ongoing opportunities to increase prospect engagement and reduce the cost of advice provision.

One such example is the CRM, often considered the heart of any financial advice operation. Advice CRMs have been a slow work-in-progress since the 1990s, with the rise of server technology and the ubiquity of the internet leading to advances in CRM capabilities in the years since.

Yet the seamless integration of all the aspects of running an efficient financial advice practice, from prospect engagement to financial modelling to advice provision to the implementation of recommendations (possibly incorporating investment/platform account opening) to ongoing servicing and advice remains elusive.

Part of the reason is that advisers may not currently be utilising existing advice CRMs to their fullest capabilities. In addition, the lack of integration between disparate advice technology systems means that data captured in one system may not flow freely into another to be leveraged for productivity gains.

The advancements in API usage, led by a host of FinTech start-ups over the past several years, represents a large and as yet underappreciated opportunity for advisory groups to drive productivity upward while restraining, and possibly lowering, the cost of advice provision.

A host of novel FinTech applications, from robo-advice to next-gen investment platforms, have conclusively demonstrated that many aspects of traditional advice workflow can be automated to a large degree. AML/CTF client identification and compliance via API calls to relevant databases being only one such example. Automated account opening being another.

Legislative/ Policy Interventions

While technology can assist in increasing productivity within the existing landscape, the opportunity to improve financial advice affordability and accessibility rests even more so with appropriate amendments to the legislative framework surrounding advice provision.

It is clear that there is a reticence to sail outside the 'safe harbour' enshrined in the definition of best interest duty, with the 'catch-all' provision of Section 961B(2)(g) proving particularly problematic.

While this remains the case for personal financial product advice, risk averse compliance committees will continue to enforce advice workflows that preference costly comprehensive advice over less expensive, lighter-touch scaled advice.

It is therefore hoped that the current inquiry by the Australian Law Reform Commission into Australia's financial services legislation[18] , including a review of key definitions such as 'Financial Product Advice' and 'Retail' v 'Wholesale' client definitions definitions will yield recommendations for pragmatic changes to Chapter 7.7 of the Corporations Act 2001

The final ALRC report, due in late 2023, may in turn incorporate elements of the final Quality of Advice Review report, due to the Treasurer by mid December this year.

The proposals put forward in its August consultation paper would see a significant change in the current 'personal v general advice' distinction, where the existing Best Interest Duty in respect of personal advice would be replaced with a duty to provide 'quality advice'. [19]

Alternative Models – Guidance and Assistance

Finally, in respect of the Tinbergen Principle, there has to be an acceptance that even with legislative relief, an abundant adaptation of AdviceTech and FinTech and all the goodwill the advice

[18] ALRC 2021, Financial Services Legislation: Interim Report A, p 463, https://www.alrc.gov.au/wp-content/uploads/2021/11/ALRC-FSL-Interim-Report-A.pdf (ALRC Interim Report)

sector can muster, there will be a cohort of Australians who will still face barriers to accessing financial advice.

This may be due to a lack of financial literacy and proficiency in dealing with advisory professionals. It may be due to financial circumstances, with price inevitably being a barrier for some even were advice costs to fall over time. Or price may not be a barrier, it may simply be an individual preference to remain a 'Controller' or to continue with a 'DIY' strategy.

Whatever the reason, a well-rounded financial services sector would have a range of viable alternatives to attaining financial advice from a 'traditional' provider.

In a way the market already caters for such needs, with a variety of online financial information sites, finance and investment magazines/online sites, government initiatives such as ASIC's 'MoneySmart' website, investment blog sites and what can only be described as a deluge of investment content on sites such as YouTube.

Thus, it is possible for those of more modest means, or who have the capacity to engage professional financial advice but chose not to, to find content either for free or at a relatively low cost.

The issue that arises is one of quality, motivation and, by extension, potential adverse consumer outcomes.

Traditional financial advice is costly in part because of the layers of 'assurance' built into the system, from the AFSL licensing process to the requirement for appropriate professional indemnity insurance to the internal and external dispute resolution schemes required in the event of complaint.

Content, information, service and investment product providers who sit outside the AFSL regime tend not to operate pursuant to the same rigorous requirements, and thus the potential adverse consequences of their actions can be immense.

There is possibly no more salient case of unregulated 'advice' impacting consumers than the recent crash of several high-profile cryptocurrencies that were promoted by a range of 'FinFluencers', crypto shills and bad actors in schemes most kindly described as "pump-n-dump" operations.

With the likes of the algorithmic stablecoin USDTerra and its crypto twin Luna effectively going to zero recently, and generating investor losses estimated at over USD $60 billion, the dangers of an unregulated investment advice ecosystem have been shown to be all too real.

In total it is estimated that worldwide losses in crypto alone this year now exceeds USD 1 trillion.

Yet this year's crypto/NFT crash is precisely the reason why the development of non-traditional methods of providing appropriate 'guard-rails' to Australians who can't or won't engage traditional advice is so critical.

[19] The Australian Government Treasury, Quality of Advice Review, Issues Paper, March 2022, p 9

This applies not just to Gen Z or Gen Y getting lured into the next big 'rugpull'; it applies just as much to Gen X and Baby Boomers of more modest means who want to organise their financial affairs, perhaps plan for retirement, but don't feel an ongoing engagement with a traditional adviser is warranted.

To that end, the benefits of a wide range of robust, engaging, appropriately regulated and inexpensive alternatives to traditional advice would be highly beneficial.

Robo-advice, while it has not had anywhere near the penetration of the US or Asia, is one such example where consumers with more modest requirements can 'self-serve' within the confines of a regulated environment where the choice architecture has been deliberately constrained so as to avoid consumer choice overload.

Next-generation investor-directed portfolio services (IDPS) where consumers can choose either a DIY experience or to have some guidance from a Financial Adviser are another such example.

These solutions point to a hybrid advice future, where the interaction between consumer and adviser might evolve along a spectrum over time, starting with a highly digital, near self-serve model and evolving toward a human-centric relationship as retirement approaches.

Beyond the constraints of the current legislative edifice, the concepts of 'Guidance' and 'Assistance' should be brought in from the cold to sit in between General/Personal Advice on the one hand and Factual Information on the other.

The recent Budget submission by Super Consumers Australia, in calling for a government-funded retirement guidance service in-line with the UK's Money and Pension Service where consumers can gain access to impartial guidance on a range of retirement planning issues, points to a possibility.

The Melbourne University 'FinFuture' white paper of 2019 proceeded in much the same direction, calling for the establishment of a National Financial Wellbeing Agency that would be tasked with improving the financial wellbeing of the nation in aggregate.

These and other ideas need to sit alongside the push toward appropriate legislative relief and amendments spearheaded by the Levy Review and the ACLR Review, and the continued advancement of AdviceTech and FinTech into the fabric of the Australian financial advice sector.

Conclusion

In order for consumers to want to seek advice, they need to understand what it is. There are too many misnomers, misconceptions (e.g. its only for the rich, it's for retirees etc) and trust issues blighting financial advice at present. Effort needs to be directed to educating potential consumers in order to help them understand what advice is, where they can get it, what are the hallmarks or badges of a good adviser / advice firm in what is largely a brandless industry. This is what will help facilitate trust.

To an extent, the trusted 'brand' becomes the licensed advice profession with associated professional membership as branding.

Control Your Own Destiny

The government drive to ensure practitioners of advice complete a minimum threshold of ethical and educational qualification makes sense in that it was intended to 'clean up' the industry and make it more professional. A healthy advice and wealth management industry is ultimately beneficial to all. Keeping in mind, the vast majority of advisers were already capable and had good intentions. Yet here we are with an advice sector at the crossroads.

At a time when the government has not helped consumers and industry professional bodies arguably could have done more to support their practitioner member base. With the industry essentially having been kicked to the curb over the last 20 years, the only remaining chance is for the private sector of participants to help itself, and in so doing, help the millions of Australians currently priced out of accessing advice.

The call to action is for fund managers, platform providers, insurance companies, advice technology providers and other significant industry suppliers to unite with advisers to create awareness. To band together and promote what advice is, where to get it and how it is beneficial. There is a clear problem and an opportunity to do something about it. Stakeholders who have a vested interest in their own success, and equally importantly helping end consumers through their products and services, need to work together and do so now.

The industry is too fragmented, and key stakeholders need to be united in working towards a guiding vision: advice is valuable and consumers who obtain it are by and large better off. Alas, there remains a lack of voice and a lack of unification to tackle this issue and advocate on behalf of the wealth management industry, extolling the virtues of advice.

Without action, the advice industry will continue to shrink, other wealth management participants will be worse off, and so will the average consumer of financial advice. Despite the Hayne Royal Commission and the egregious behaviour it uncovered, there are hundreds of thousands of advice recipients who are far better off for having received advice. This second side of the story, has unfortunately never been well told. Consequently, the wealth management industry, particularly the advice sector, persists in a state of decline.

It's time for all wealth management participants to act, to control their own destiny! Because clearly the past 20+ years have shown no one is going to do it for them and this is an important industry and part of society, especially in such a wealthy country. The industry funds carved out their stake, became a clear choice for a significant number of cohorts, and the remainder of the wealth management industry needs to do the same. This needs to be achieved via an advice led ethos, to grow the size (and share) of the pie for all and all wealth management stakeholders have a vested role to play in achieving this important outcome.

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