FINANCIAL ADVISER SURVEY 2021

THRIVING THROUGH TURMOIL

How financial advisers navigated a year of unprecedented change

FE fundinfo

Contents

About this research

This FE fundinfo research was conducted throughout November and December 2020 and January 2021. It consisted of 45 questions and was completed by 250 financial advisers over this period.

It spanned a broad range of subjects including the impact of the Covid 19 pandemic, business drivers, revenues, new business opportunities and overheads for firms, regulatory changes, trends in investing, outsourcing and this year with a particular focus on retirement propositions and ESG investing.

This is the sixth annual financial adviser survey conducted by FE fundinfo.

Executive summary

- 91% of advisers feel more positive about their business outlook than 12 months ago
- Regulation still tops the charts as being the largest business concern, followed by cost pressures, exacerbated by rising PI premiums
- Covid-19 has prompted greater remote working and investment in technology to serve clients, potentially bringing in more efficient ways of working
- 65% of advisers now actively incorporate ESG factors into their investment propositions, or plan to do so imminently
- Two thirds of advisers report an increase in the amount of client money invested in ESG over the past 12 months
- Advisers still feel their clients lack a full understanding of what ESG investing entails and some of the contradictions that may exist
- The implementation of centralised retirement propositions has increased during 2020
- There remains a shortage of products and solutions to support retirement advice and there is a growing need to help clients stretch smaller pots over longer life expectancies


2020
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Introduction

There is no doubt that 2020 was a year unlike any other in living memory.

With the coronavirus pandemic hitting global economies, the culmination of the UK's final departure from the EU at the end of the year barely registered, barring the inevitable 'deal or no-deal' negotiations, that with hindsight was always likely to happen.

While the ramifications for many sectors has been dramatic, for the adviser community the impact of Covid-19 has fortunately been less seismic and with some intelligent technological and behavioural application, the client adviser relationship moved online.

Some advisers think that this is the way forward and there are a great deal of efficiencies to be had by going virtual, possibly meaning that an adviser could serve more clients and start to close up the ever-widening advice gap (more of that later).

One of the unexpected consequences of quarantining the country has been the big increase in people attempting to sort out their personal finances as financial wellbeing became a priority. For some, lockdown enhanced their finances as people saved money on travel, commuting, holidays and instead started saving and investing. This is evidenced by execution-only platforms seeing big spikes in new business and so too have advisers with inbound enquiries. 60% of advisers reported an increase in the number of clients advised in 2020 while only 5% reported a decrease.

ESG investing has grown and matured throughout 2020 and is now a major factor in global investing, attracting new and existing clients who are increasingly aware of the impacts of their investments.

The pandemic certainly provided the tailwinds to show that ESG-friendly investments could perform as the carbon-based economy slowed and sustainable businesses flew. Indeed, in FE fundinfo's recent Crown rebalance, ethical and sustainable funds demonstrably outperformed traditional funds, with one in five now having the highest 5-Crown rating. While last year was unique, it is clear their underlying strength is not diminishing.

The full enormity of the challenges of retirement planning continued to be in focus last year, for advisers and their clients, as people wrestle with the stark realities of an ever-increasing reliance on Defined Contribution pensions and having to make less money last longer.

With the regulator delaying its planned regulatory programme of implementations during the pandemic, there has been some relief from the FCA that has typified adviser concerns in recent years.

Even when the country starts the long road to normality post-pandemic and we've all been vaccinated, the damage has been severe in terms of lost jobs and output, and the tail of this crisis is likely to be long and difficult.

On the other hand, these kinds of economic challenges often call for the services of a financial adviser and that's good for business.

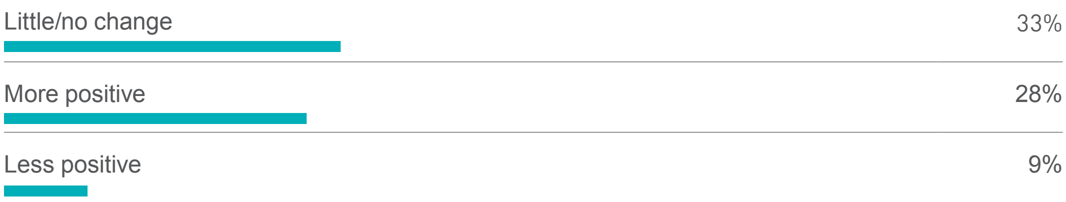
Chapter 1

Adapting to a post-covid world

There's a resilience to financial advisers rarely seen in any other sector of the UK economy. And 2020 has been no different, insofar as the pandemic seemed to create the time for clients to pay closer attention to their finances and do something about them. With nothing else to spend money on, due to the series of lockdowns and restrictions, people started investing or ploughing cash into other assets.

With additional surges from people looking to boost their retirement provision and a broader interest in ESG investing, advisers are feeling pretty positive about their business outlook, with just 9% of respondents feeling less positive about their prospects in 2020. This is a continuing trend, with advisers having felt more positive year-on-year for a third year in a row. Compared to the previous year, 54% felt more positive in 2019 and only 41% felt more positive in 2018.

How do you feel about the outlook for your business compared to 12 months ago?



When it comes to what keeps advisers awake at night, then our perennial favourites are still leading the pack of concerns.

74% of advisers cite the burden of regulation as their main worry followed by the cost pressures of running their business, primarily the ever-increasing cost of PI cover.

> *"PI costs and excess have gone up and Lloyds of London pulled out of the market a year ago which has led to large insurers like Liberty and Collegiate following suit. Also ever increasing FCA fees and FSCS levy are causing SME IFAs to really struggle with balancing the books; we really require the regulator to step in and do something about this as it is not sustainable."*
>
> ***Lloyd French, Financial Planning Consultant, Delauny Wealth***

Other than these, there are the specific issues of Brexit and Covid-19, both gradually resolving, then a plethora of smaller concerns, such as recruitment/ succession planning and finding the right types of client.

Which of the following would you say are the top 3 areas of concern currently facing your buisness?

Burden of regulation	74%
Cost pressures of running your business	52%
Uncertain economic conditions caused by Brexit	35%
Market conditions in the wake of the Covid-19 pandemic	34%
Recruitment/succession planning	28%
Finding the right type of client	27%
Clients turning away from regulated financial advice	15%
Lack of appropiate software solutions within the market	10%
Growth in direct-to-consumer platforms	10%
Lack of diversity within the industry’s workforce	6%
Consolidation/increasing M&A within the advice market	6%
Other	2%

After the cost of PI cover, there’s a broad spread of cost concerns, primarily focused around regulatory issues and operational costs.

What has been the biggest cost your business has faced over the past 12 months?

Increasing PI Insurance	41%
FSCS Levy	15%
Operational costs	15%
FCA fees	11%
Investment in/maintenance of technology/software solutions	6%
Loss of income/losing clients	5%
Recruitment	4%
Other	3%

Over the past year, we've witnessed a significant reinvention of the advice process, with much client consultation and even prospecting moving online.

The big revelation has been the rapid adoption of remote working and on-screen client servicing, driven by the Covid rules, but having a really positive impact on working practices. 77% of respondents said that this was the biggest opportunity for their business, presumably due to the increased efficiencies of servicing a client bank and the avoidance of commuting and travel time.

With the new demand for ESG investing and an ever-evolving product offering, there is a very rosy picture to paint for the future of financial advice.

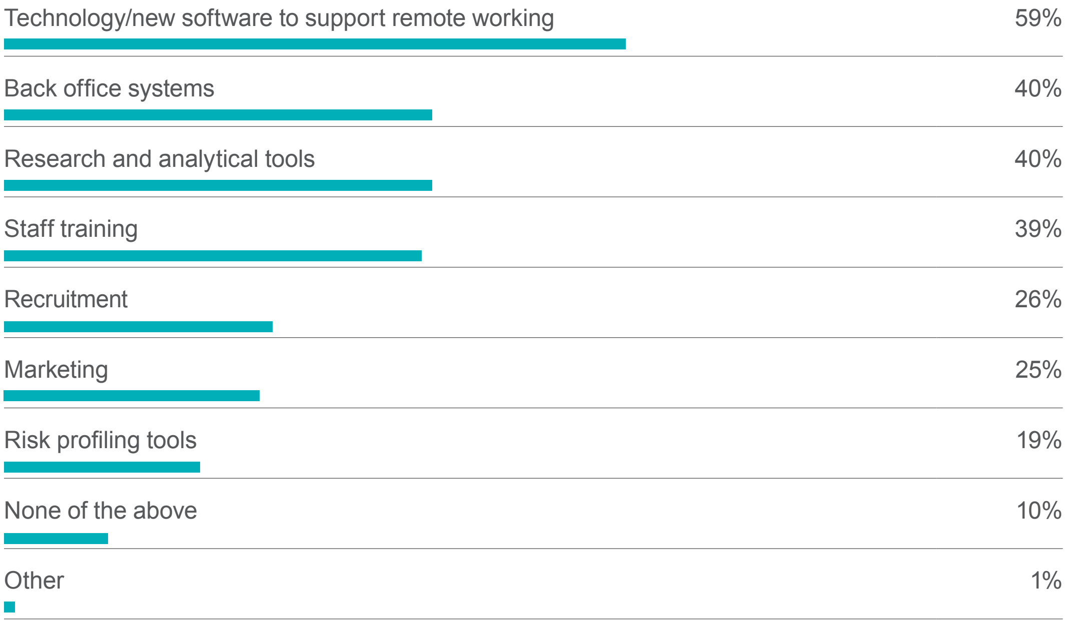
It suggests that this might form a template for future working practices for adviser firms not only as a better way of servicing and attracting new clients, but also for the cost saving benefits of remote working.

Which of the following would you say are the top 3 opportunities for your business in the year ahead?

There's also optimism surrounding the efficiencies of new technology and software beginning to improve efficiencies and reduce costs as well as a raft of new sales opportunities being generated by ESG investment coming of age.

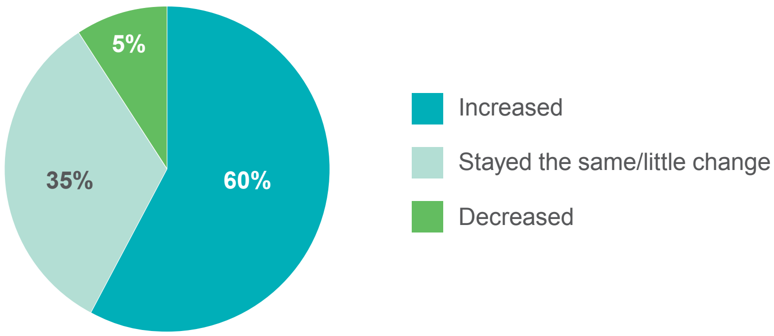
And to reinforce the point, more firms are investing in technology than ever before: four of the seven biggest investments made by adviser businesses are in technology (remote working, back-office systems, research & analytics tools and risk profiling tools) and they dominate the business expenditure charts.

Which of the following have you/your business invested in over the past 12 months?



Although advisers have found that servicing existing clients (and indeed finding new ones) has worked well using new screen-based technologies, it was expected that client numbers would have remained relatively static throughout 2020. So, it's a big surprise that 60% of advisers reported an increase in clients and only 5% reported a fall. Again, this might be attributable to inbound enquiries from people taking the opportunity to sort out their finances during lockdown periods. Although it should be pointed out, this is not as dramatic as 2019, where 78% of advisers reported an increase in clients, it's impressive given the circumstances.

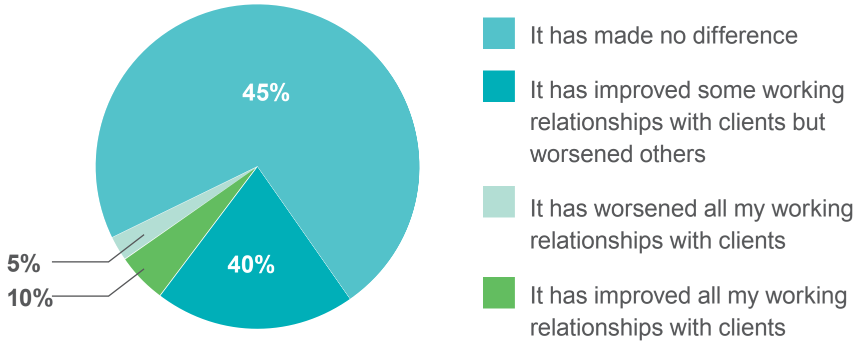
How has the number of clients you advise changed over the past 12 months?



In terms of utilising new technology to service clients, there is only a small minority of advisers that have found a worsening of relationships with their clients. Although the 'Zoom Culture' seems to have been a success with advisers, there are clearly some clients that don't like using the technology. This is reflected in the responses with 40% reporting mixed feedback from clients, whereas the biggest response of all (45%) have reported that it has made no difference to client relationships.

Surely a strong sign that increased use of remote client servicing will stick around post-pandemic.

How has the lack of face-to-face time with your clients during the 2020 lockdown affected your relationships with them?

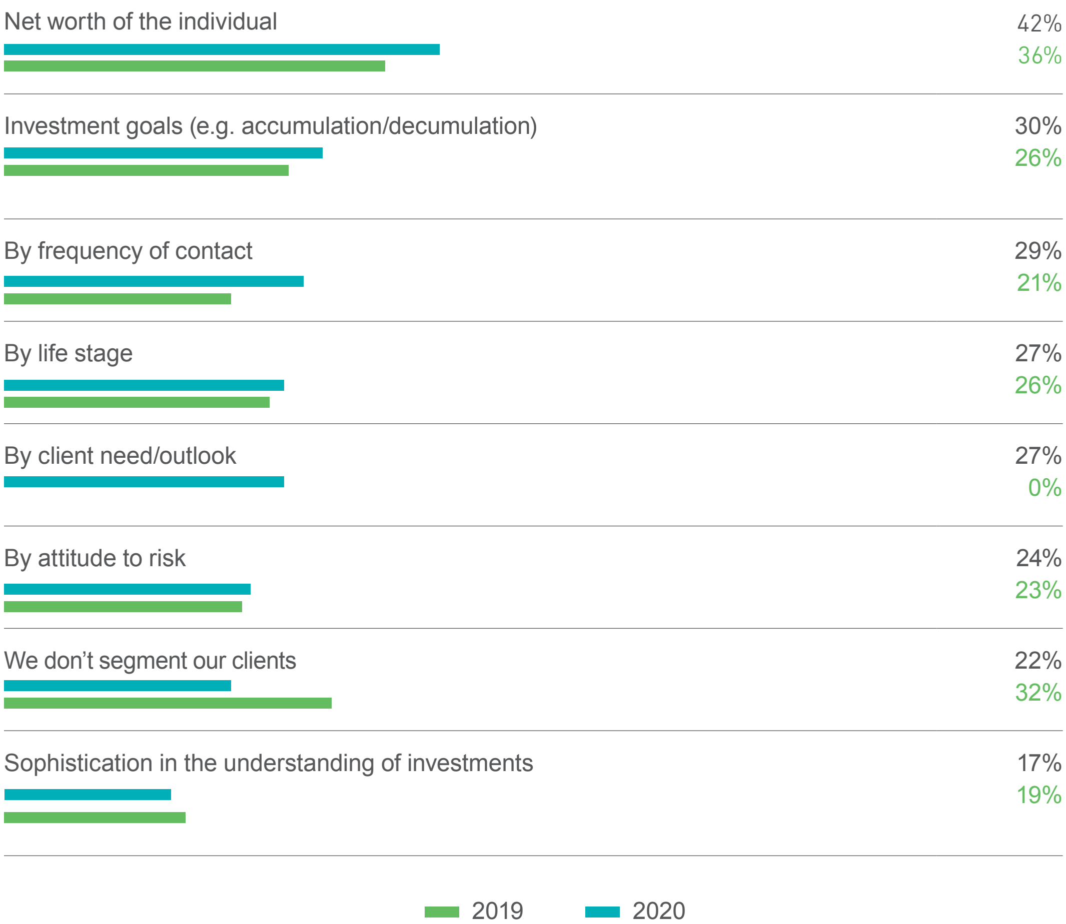


Segmentation

Last year we observed that only 19% of advisers seemed to be segmenting their clients as per the requirements of the recently introduced PROD rules.

In 2020, this method of segmentation fell further to just 17% with the primary segmentation method being based on net-worth, which has increased in popularity. Nearly one fifth (23%) meanwhile do not use any form of segmentation techniques.

Do you/does your firm segment your clients by any of the following?



It may be that, given the chaos of last year, any improvements to client segmentation in terms of sophistication were put on the back-burner.

Indeed, almost three quarters of respondents said that they had not changed their segmentation techniques, so this is one to watch as normality returns.

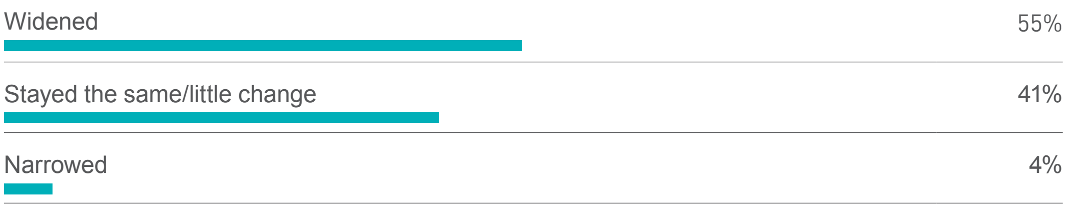
Have your segmentation techniques changed over the past 12 months?

The advice gap is always interesting in terms of how advisers perceive it as they are at the coal face of understanding the demand for advice and their ability to satisfy that demand.

More than half of advisers have responded saying that the gap has widened (further) with just 4% reporting that it had narrowed.

This might be in connection with the ground swell of people seeking to sort out their finances during the pandemic and having to turn business away in some cases or noting the rapid growth in DIY investor numbers on retail platforms.

Over the past 12 months would you say the advice gap has?



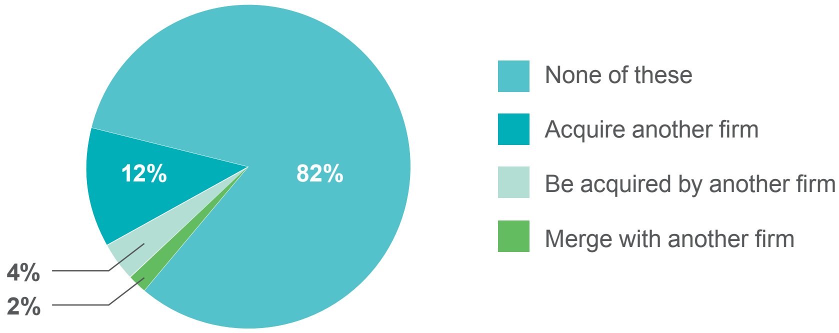
Either way, there isn't much evidence of anything happening in the market to suggest the advice gap should be closing, so it's an interesting observation – and opportunity – for financial advisers.

And talking of opportunity, there has been a tidal wave of corporate activity throughout 2020 continuing from the previous year, with a move towards consolidation and older practitioners looking to cash in their chips to hungry acquirers with pots of Private Equity cash.

Although 82% of firms reckon there will be no M&A activity on the menu for them in the coming year, it is hard to know.

The fact is that 18% of the industry is expecting (or hoping for) some form of merger or acquisition activity, with 12% of firms on the hunt to buy another firm.

In the coming 12 months do you expect your business to?



Summary

Despite predictions and expectations of a catastrophe – or even a flat year of business – advisers seem to have done exceptionally well to adapt to the new environment through deft application of technology to not only service existing clients but actually win new ones.

In addition, advisers have capitalised on three things in 2020:

- A revitalised interest in people sorting their finances out and investing unspent cash
- An increased interest and rise in demand for ESG investments
- Retirement planning rising to the top of the agenda for baby-boomers with DC pensions

It does look like, in a year that polarised fortunes, financial advisers not only got lucky but made their own luck during the pandemic.

Firms are demonstrating a long-term commitment to their practices by making significant investments in new technology to continue to drive further efficiencies and profitability.

Once the Covid restrictions ease there is every reason to believe advisers will continue to flourish, boost efficiencies and offer a wider product range.

Chapter 2

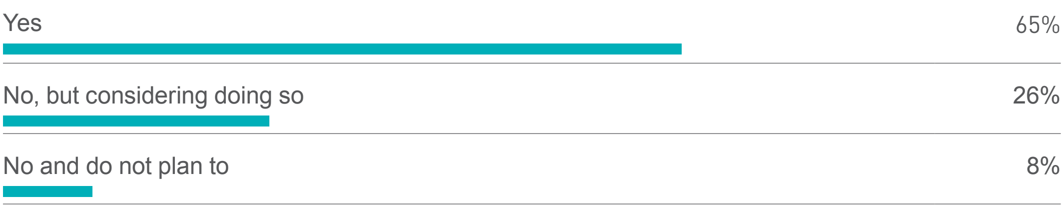
ESG starts to professionalise

ESG has been a rare good news story during the pandemic as reports of ESG focused funds outperforming their traditional cousins suddenly made people think that it is possible to invest sustainably and make money.

And so new clients and new types of clients came to advisers, as well as existing ones looking to rebalance towards a more responsible, ethical or environmental asset allocation.

It is surprising then, given the surge in demand, that there are still 8% of advisers who have no plans to incorporate ESG factors into their investment proposition at all.

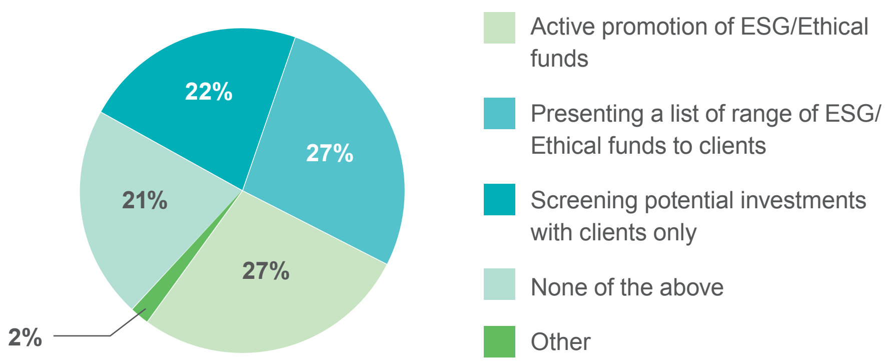
Do you currently incorporate ESG factors into your investment proposition?



What isn't such a surprise is that the sector is still trying to find its feet in terms of common standards, taxonomy, data and most of all proper consumer understanding.

The way that advisers offer up their ESG proposition is still rather disparate and scattered across 4 broad categories, with the most popular being presenting a list of ESG funds to clients.

Which of the following best describes your ESG offering?



This might be because most advisers have yet to firm up a specific ESG proposition. Just over half of advisers have already implemented a custom-built ESG proposition or outsourced this to a 3rd party.

> *"Screening of investments in the ESG space is notoriously hard to do. Firstly, you are trying to align an investor's subjective decisions with information which is naturally hard to come by. Most funds will not have the level of detail that many investors would like to see regarding their underlying holdings, so often an adviser has no choice but to accept the fund's mandate at face value."*
>
> ***Rob Gleeson, Chief Investment Officer, FE Investments***

Prior to the conclusion of Brexit, many advisers were preparing for the implementation of SFDR and 21% said their ESG offering matched these basic requirements, whereas just under a third of advisers have no specific proposition at all.

Do you currently have a specific ESG proposition in place?

> *"Now that the government has confirmed SFDR will no longer apply to UK firms, many advisers are now at an impasse over their ESG obligations. Undoubtedly demand for ethical investment products is increasing at client level, but there is no underpinning regulation or best practice readily available. The government wants the UK to align firms to the Task Force on Climate-related Financial Disclosures (TCFD), but this is at institutional level, rather than at advice level. There is no requirement for advisers to include it in their propositions, or even talk about it. For the time being then, advisers are caught in the middle of investors wanting sustainable portfolios, but without a clear set of standards in the UK in which to work towards."*
>
> ***Mikkel Bates, Regulations Manager, FE fundinfo***

So, who is driving the surge in ESG investments? Is it advisers pushing their marketing buttons and generating interest with their clients, clients themselves wanting to invest and coming to their adviser for help, or the fund managers and media whipping up demand?

Last year's survey showed over a third of advisers reported that it was their clients that were the biggest driver in ESG demand followed by institutional pressure (which we assume to be an ever-growing supply of ESG funds and associated publicity) and a small dose of regulatory pressure.

Has Covid given more people the time to sort out their finances but with an ESG focus? Or is it that in a year where the oil price has collapsed to an historic low and international travel is practically non-existent, ESG investments have taken the place of more cyclical assets?

When we asked advisers if their clients' interest in ESG investing had changed, they responded that almost 40% of clients were more engaged with 16% of them significantly more interested.

Just 25% of clients were apparently unconvinced by ESG or hadn't changed their investing behaviour.

Would you say your clients' interest in ESG investing has changed over the last 12 months?

Yes, to a limited extent	23%
Yes, but only for certain types of client	20%
There has been no noticeable change	16%
Yes, significantly	16%
Yes, when ESG investing is explained to them	14%
No, most clients remain unconvinced	11%

The telling statistic is the fact that 66% of advisers reported an increase in ESG investing over the last 12 months and just a 1% decrease.

This supports the notion that ESG is dragging in a lot of capital even before the sector has matured fully and standards are yet to be fully put in place.

This is likely to be because of the reported performance gains against traditional investments during the pandemic, coupled with more people with time on their hands to invest.

How has the amount of client money you have invested in ESG Investments changed over the past 12 months?

Increased	66%
Stayed the same/little change	33%
Decreased	1%

The lack of a single set of standards and taxonomy, data and general immaturity in the ESG market has created a spread of approaches to the due diligence advisers undertake when reviewing investments.

"ESG as a term is not particularly helpful and has broadly been spoken about from an institutional point of view as a catch-all solution to a complex problem. Retail investors and adviser clients don't tend to think along the lines of whether their portfolios are 'ESG portfolios', but rather that their investments are not doing any harm and that they align with their own values. These are subjective decisions which advisers will have to get to the heart of and understand the range of suitable services within the market to meet their clients' needs."

Rob Gleeson, Chief Investments Officer at FE Investments

The two most popular methods of due diligence are using a fund filtering tool such as FE Analytics (62%) followed by the more traditional reliance on fund fact sheets. This is validated by Nextwealth's 2021 ESG Tracker Survey, which revealed FE fundinfo was the leading ESG influencer among financial advisers.

Some of the emerging ESG research tools have yet to make it into mainstream use and there is a broad spread of research techniques additionally used, to ensure that the ESG recommendation being made sticks to core principles and avoids any "greenwashing".

"The issue of greenwashing and its associated ESG scoring is complex, as much of the thinking around it is qualitative. Does, for example, Phillip Morris' commitment to move away from tobacco products suddenly make them ethical? BP meanwhile has committed to making its energy sustainable, but how can end investors tell that action has been taken? When, too? At what point are they judged to have reached this commitment?

"Things can change quickly as well. Kingspan, the building company for instance might previously have had a good ESG score, but when their role in the cladding scandal in the UK became apparent, their ESG rating would have changed significantly, almost overnight."

Mikkel Bates, Regulations Manager, FE fundinfo

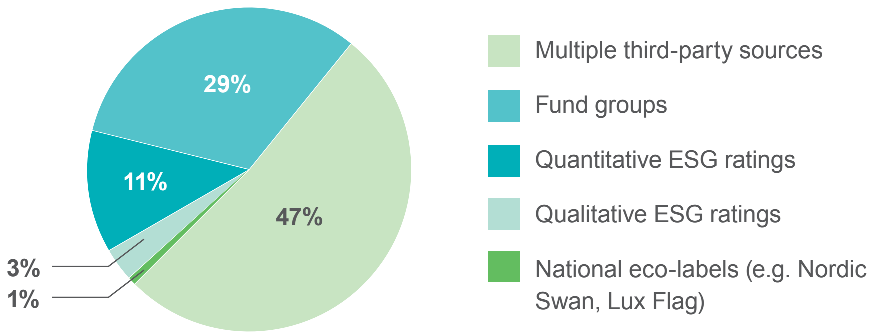
What due diligence do you currently undertake to review an investment's ESG credentials?

Filtering via research tool (e.g. FE Analytics)	62%
Review fund documents/factsheets	51%
Comparing a variety of fund ratings/multiple sources	39%
Conduct your own independent research into an investment without client instruction	32%
Review a fund's rating by agency/ecolabel	29%
Review fund holdings at base level	29%
Conduct your own independent research into an investment based on client instruction	19%
None	8%
Other	9%

When we asked what the main source of information was when checking out ESG funds, some degree of nervousness seems to be in evidence with the majority of advisers (47%) using multiple third-party sources in their research.

Just under a third of advisers trusted the fund manager's information and there are early signs of some advisers using new quant/qual ESG ratings and even national eco-labels, such as Nordic Swan.

What is your main source of information on a fund's ESG credentials?

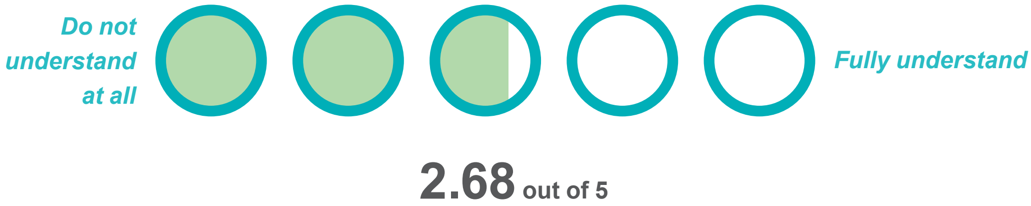


There is still a good deal of scepticism as to whether clients themselves really understand the overall concept and spread of environmental social and governance funds. It's a confusing label as a catch-all, and the industry has a habit of creating acronyms for its products, but three different issues are rather uncomfortably lumped together – sometimes contradictorily so – under a single umbrella.

"ESG screening and labels are still in their infancy and will not capture the whole performance of a particular business. By their nature most start-ups do not have good governance as they concentrate on growth and cashflow management, but that doesn't mean they are not ethical for instance, so what would a low ESG score mean in this case? Putting an ESG label based on a pre-determined list of criteria which doesn't align with their own values on a business or investment is unlikely to tell the end investor much."

Rob Gleeson, Chief Investment Officer, FE Investments

How much do you think your clients understand what ESG investing involves?



If you dig a little deeper the primary desire for clients is to make a positive environmental impact followed by fostering social impact. Strong governance within the companies in which clients invest comes third.

"Governance – the 'G' in 'ESG' investing – is very much the least understood concept within the term. Nonetheless, it is the most important as it underpins every aspect of investing. Good governance should be a basic tenet and the absolute minimum requirement of all investments. That a company doesn't break the law, doesn't commit fraud and treats its customers and staff fairly should naturally be a given. Good governance should not be considered as a separate entity in its own right, but considered simply as 'investing'."

Oliver Clarke-Williams, Portfolio Manager, FE Investments

Please rank in importance the reasons for your clients to choose ESG investments?

To make a positive impact on the environment	1.52 avg
To make a positive social impact	1.81 avg
To seek strong governance in the companies in which they invest	2.67 avg

So, what do advisers think about the future of ESG investing, now it seems it's here to stay?

The majority (76%) believe that clients will have more than a quarter of their portfolio invested in ESG funds over the next 5 years.

Just 24% of advisers think clients will hold less than 25% of ESG funds by then.

Thinking ahead, what proportion of investments do you think will incorporate ESG factors into their make-up within five years?

76-100%	8%
51-75%	29%
26-50%	38%
0-25%	24%

Many of the barriers identified by advisers are set to come down over the next couple of years – partly driven by regulation, but spurred on by better data, taxonomy and a common set of standards.

The three most cited barriers are the lack of a clear set of standards, shortage of underlying data and the risk of greenwashing.

A familiar problem of investors not wanting to sacrifice returns for doing good has dwindled as a concern to the fifth biggest concern, as evidence emerges to contradict this theory, alongside a lack of ESG propositions.

Last year, advisers reported that there was a clear correlation between buying into ESG and clients expecting a reduction in returns. 85% of advisers felt that less than 25% of their clients were prepared to suffer loss of return in order to invest in ESG. That's a significant turnaround in 12 months.

What do you think are the main 3 barriers currently preventing financial advisers promoting ESG investing further?

Lack of a clear set of standards and definitions	63%
Lack of data solutions/comparable data on ESG investments/funds	52%
Potential for “greenwashing”	52%
Adviser understanding of what ESG investing entails	37%
Lack of ESG propositions	30%
Investors reluctant to jeopardise returns	30%
Volatility of ESG investments	5%
Other	4%

Summary

ESG investing has flown out of the blocks in 2020.

Last year’s survey showed signs that the sector was coming of age, but this year has seen ESG grow fast and mature in many ways as a sector.

Looking back, the sector was a little “Wild West”, without much structure, standard practice, data or definition.

Now, there is a clear idea as to what the framework of a mature sector looks like and these improvements are being made at pace, either through commercial imperative or regulatory changes.

There is no doubt now that, once the pandemic has been dealt with, then the climate emergency will be at the top of the agenda and that can only boost the most pressing part of the ESG agenda.

Excitingly, it feels like ESG investing is bringing new and younger investors into advisory firms, which can only be good news.

1 in 5

ethical/sustainable funds has been awarded FE fundinfo’s highest 5-Crown rating

8.44%

of all funds with a 5-Crown rating are ethical or sustainable

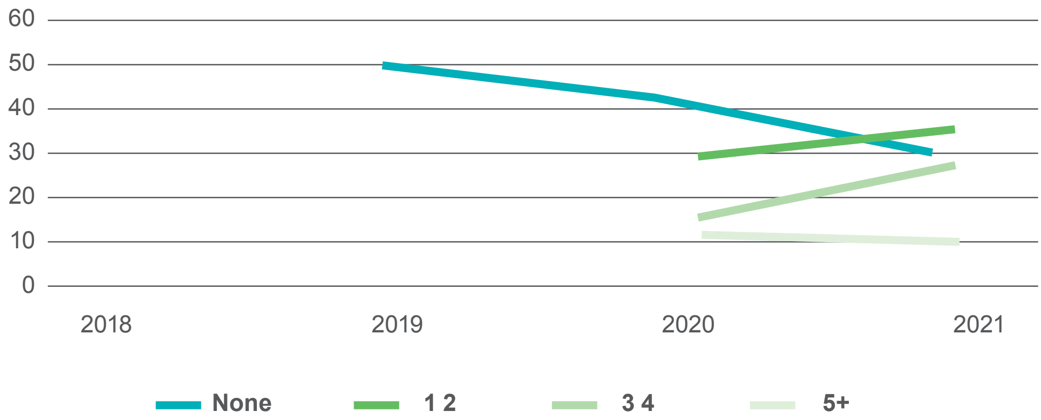
Chapter 3
Investment strategies in 2020

Model portfolio adoption

With all the other challenges faced by adviser firms, it is not surprising to see any behaviours that didn't involve trying to maintain a state of 'business as usual' being lower down the priority list.

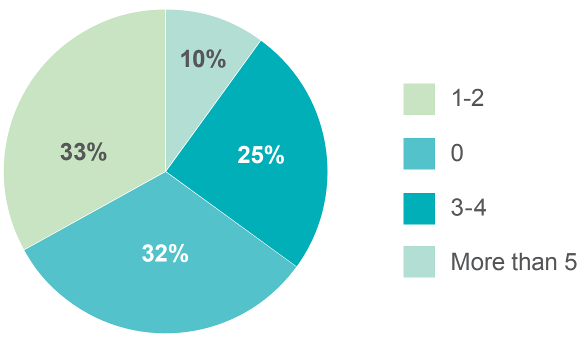
And so it was with the 3rd party model portfolio relationships with advisers. The trend towards outsourcing continued with just under a third of advisers still not using 3rd party models or managed portfolio services, down from 42% in the previous year.

Trends in using 3rd party model portfolios



In terms of how many providers advisers partner with, these numbers have remained relatively static year-on-year.

How many 3rd party model/managed portfolio providers do you use?



This is borne out by the fact that 72% of advisers have not changed providers during the last year.

Have you changed providers over the past year?

> *"We don't tend to see much churn in advisers changing their third party solutions, so the fact more than a quarter have changed providers could be a reflection of the market turmoil that many investors faced from March onwards last year. Additionally, with new ESG solutions available, many might be adding to their providers, rather than replacing them outright."*
>
> ***Rob Gleeson, Chief Investment Officer, FE Investments***

As the adoption of outsourced portfolio services continued to increase, so the amounts of money invested in them has grown further with 46% of advisers reporting growth. Only 8% report that they are putting less money into 3rd party investment solutions in the last 12 months.

However, in last year's survey 58% of advisers say that they increased the amount they invested into 3rd party solutions, so the rate of increase is falling away, possibly diverting into ESG offerings.

How has the amount you/your firm invested on behalf of your clients in third party investment solutions changed over the past 12 months?

Increased	46%
Stayed the same/little change	46%
Decreased	8%

Asset allocation

Given the Covid-driven crash at the beginning of the year, the US elections, Brexit uncertainty and a general Global malaise, it's interesting to observe how asset allocation changed throughout 2020.

Here's a quick review of the highlights of the 12 key asset classes and how they fared:

Property	46% decrease	(45% net)	▼
UK equities	36% decrease	(22% net)	▼
Absolute return	21% decrease	(15% net)	▼
Emerging markets	33% increase	(29% net)	▲
ESG/ethical funds	61% increase	(59% net)	▲
Emerging markets	33% increase	(29% net)	▲
US equities	28% increase	(17% net)	▲
Alternatives	16% increase	(8% net)	▲
Mixed investment (40-85%)	13% increase	(8% net)	▲
European equities	no change		—
Corporate bonds	no change		—
Mixed investment (0-35%)	no change		—
Mixed investment (20-60%)	no change		—

Net figure represents number of increases minus decreases in asset allocation

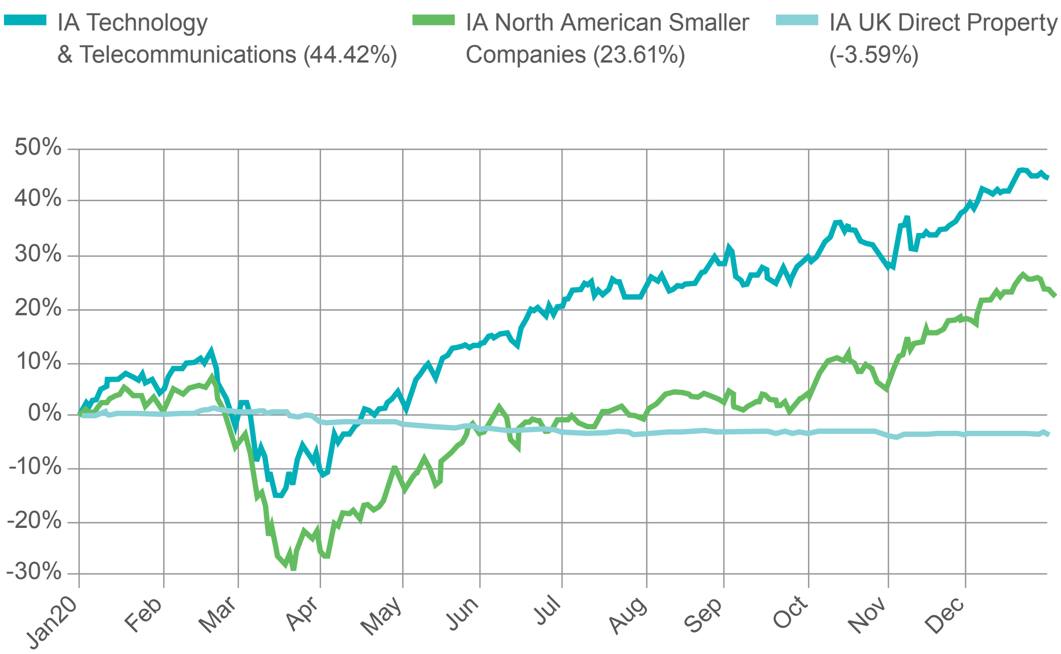
Data from FE Analytics however presents a more mixed picture from general investors. Of the ten funds which attracted the most inflows last year, equities, bonds and property are all represented.

"After what has been a difficult year for investors, the allocations advisers are making are broadly in line with what we would expect and mirror in our own portfolio allocations. Throughout 2020 there were clear 'winners' and 'losers' of the pandemic, with US equities – dominated by big tech stocks – performing well, while more traditional markets such as energy and financial services performed poorly. If inflation were to rise in 2021 we might see a turnaround in these sectors, but there is no clear sign that this is going to happen.

"The restrictions of 2020 will last well into 2021 so some of the trends we have become familiar with will most likely stay. Property for instance was affected badly by the move to home working, with commercial and retail falling sharply; indeed, datacentres and warehousing offered the only glimmers of hope for the struggling sector."

Charles Younes, Research Manager, FE Investments

Data from FE Analytics over the past year shows US Smaller Companies have generated the largest returns, followed by the IA Technology & Telecommunications sectors. As the chart shows, IA UK Direct Property has seen the lowest returns, supporting adviser scepticism about growth within the sector.



Summary

Last year, advisers reported some pretty big swings in asset allocation, with property falling strongly out of favour, primarily due to fund suspensions and the effects of Covid on likely demand for commercial property/office space if home working takes hold.

The big winner was ESG and ethical funds with advisers reporting a massive 61% increase in asset allocation against a 2% decrease in client portfolios.

This is clearly an exceptional performance in such a short space of time and some advisers have even commented that they'd like even more diverse ranges of products from fund managers to meet demand.

Other changes are more measured and logical with a move out of UK equities and into US and emerging markets as investors seek growth and stability through the Brexit transition period. The US tech-stock behemoths have also performed well through the pandemic, again dragging money into that market.

Chapter 4

Trends in retirement planning

Retirement planning is gradually moving towards centre stage as increasing numbers of the population – particularly baby-boomers – approach retirement without DB pensions. And the lucky people who do have DB schemes are keen to take advice as schemes attempt to transfer them out with tempting pots of cash.

Not only is pre-retirement advice in demand, but the word decumulation (hardly mentioned as recently as 5 years ago) is now well used within the industry.

Whereas advice used to be simple during the progression from accumulation to decumulation, save some cashflow planning and general de-risking and “wealth preservation”, nowadays there’s new thinking permeating the pensions industry and adviser community. Simply put, sustainability of income can only be achieved with some element of risk.

Pension freedoms may have done a lot of good, but they have also created a number of issues that the industry needs to tackle. Helping people to maximise their pension pots by retirement and then squeezing every ounce of value from it post retirement has become a challenge for providers, advisers and even the government, who want less pressure heaped upon the state pension.

And with defined contribution pensions becoming the norm and life expectancy continuing to grow, the whole nation is struggling with trying to make less money last longer.

Essentially, the post-retirement journey has now been acknowledged as a very different journey to the pre-retirement journey and consequently a new suite of products, tools, approaches and advice needs to brought to bear in order to solve the unique challenges a retiring client faces.

“Since the introduction of pensions freedoms several years ago, many decumulation offerings have emerged in the market, but it remains to be seen how effective they will be. The effectiveness of drawdown strategies are only able to be evaluated after a significant period of time. What is clear however is that attitudes to risk around retirement need to be reframed. With longer life expectancy, a yearly drawdown rate of 4% – which is highly unlikely to be achieved in any case – is not sustainable. The risk in retirement therefore is not about investments performing badly, but running out of cash; the only way to improve dividend payments or capital growth is through taking on more risk. There needs to be a conversation – at both client and adviser level – about long-term risk and what it means.”

Rob Gleeson, Chief Investments Officer, FE Investments

Just as advisory firms have developed centralised investment propositions (CIPs), they are now building centralised retirement propositions (CRPs) with sets of products, tools and solutions designed for different client needs.

This ensures consistency of offering and generates efficiencies in the advice process.

In the previous survey, 48% of advisers said they had or were planning to develop a centralised retirement proposition whereas this year that number has risen to 62%.

Do you/does your firm have a centralised retirement proposition? (CRP)

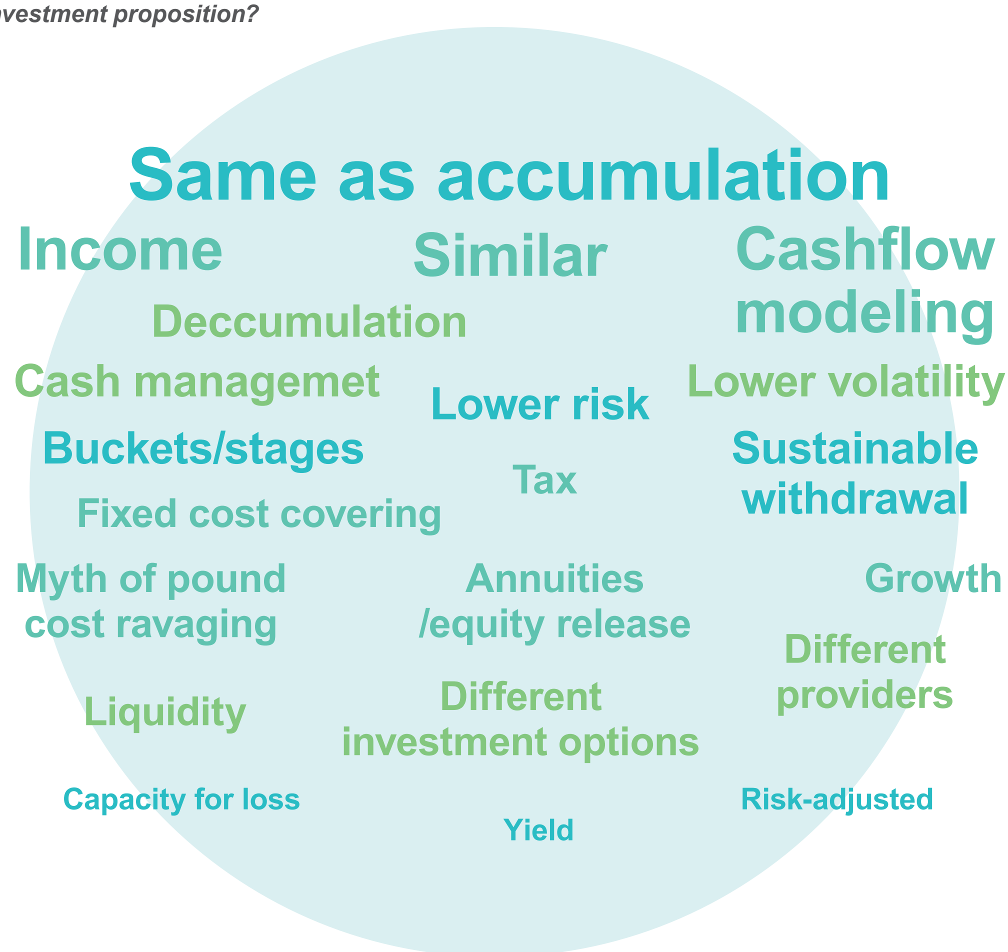
Yes	38%
No and I/we have no plans to develop one	38%
No, but I/we are developing one	24%

There are still a proportion of advisers that don't subscribe to the notion of a CRP, with many citing the fact that they employ the same techniques and personal service to their retired clients as they do with other clients.

This may account for this rather stubborn 38% of the market that feel a CRP has no place in their armoury.

When asked about their CRP and how it differs from their CIP, some interesting themes arise and are highlighted by the concerns below.

How does/how will your centralised retirement proposition differ to your centralised investment proposition?



Specific quotes from advisers when describing the differences between their CIP and CRP include a heavy bias towards income and cash:

"It has a separate fact-finding process and integrates cashflow planning more deeply"

"[It] focuses on three income solutions, cascade, natural income and growth"

Others were more interested in client risk during retirement:

"We focus on explicit capacity for loss in decumulating, along with a cash strategy to support retirement objectives"

"[We use] increased allocation of to low risk equities or fixed income instruments and larger holdings of cash"

Other advisers were also talking up some new approaches:

"[Our solution is] much broader covering everything from Annuities to Equity Release and everything in between; the CIP is just that, a set of investment solutions"

"[Our retirement proposition] incorporates more about life stages, ages, decumulation as opposed to accumulation, investment strategy may change, but underlying funds don't change substantially"

What we see is strong representation from the "retirement is no different" camp but some emerging themes such as income, cashflow modelling, decumulation (strategies), volatility and "buckets, pots and stages" used quite often.

The vexing subject of sustainable withdrawal rates also is mentioned fairly often, mainly in conjunction with cashflow modelling as advisers try to help clients draw down the right amount of money each year.

Some advisers also highlighted themes such as annuities, equity release and tax as all having a unique bearing on the retirement journey as well as mentioning different retirement-related terms that suggest that retirement has been carved out as an entirely separate subject with different solutions.

The two thirds one third split in advisers appears again when we asked if they used specific retirement investment solutions for their clients, with 33% saying they deployed their usual preferred non-retirement investment solution.

Do you use specific retirement investment solutions for your clients who are in retirement, or do you use your usual preferred investment solutions?

A mixture depending on the client	56%
Usual preferred non-retirement specific investment solution	33%
Specific retirement investment solution	11%

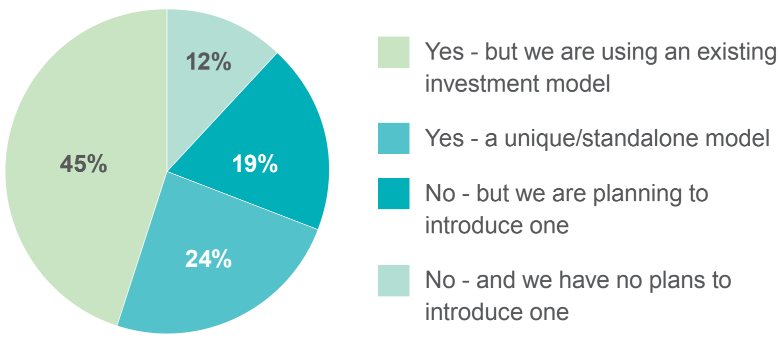
There's a less clear pattern when we asked advisers how they manage their retirement proposition, with the majority saying the service was bespoke or through their internal investment committee. There's some evidence of emerging 3rd party solutions for clients in retirement.

How do you currently manage your retirement proposition?

Bespoke for each client	43%
Through an internal investment committee	28%
A mixture of outsourcing and centralisation	17%
Outsource to a third party	11%
Other	2%

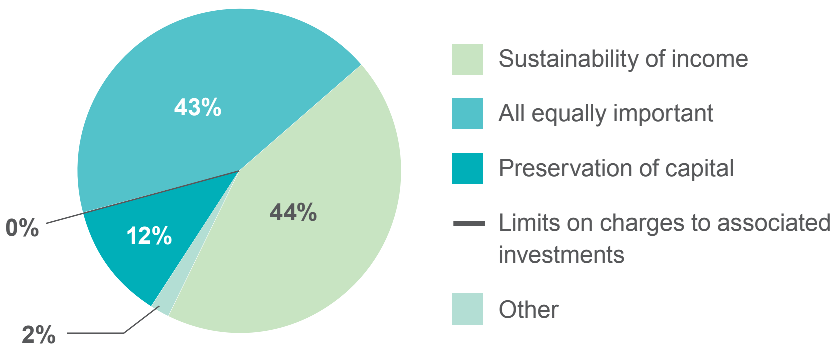
On the subject of drawdown, there seems no preferred way of provision with a tendency to adapt existing models, but this is understandable given the very early stage that the "decumulation industry" is at.

Do you have a drawdown strategy in place?



In terms of the importance of factors to clients, sustainability of income is clearly the most important, but advisers point out that all factors are important.

Which of the following is the most important to your clients in your retirement proposition?

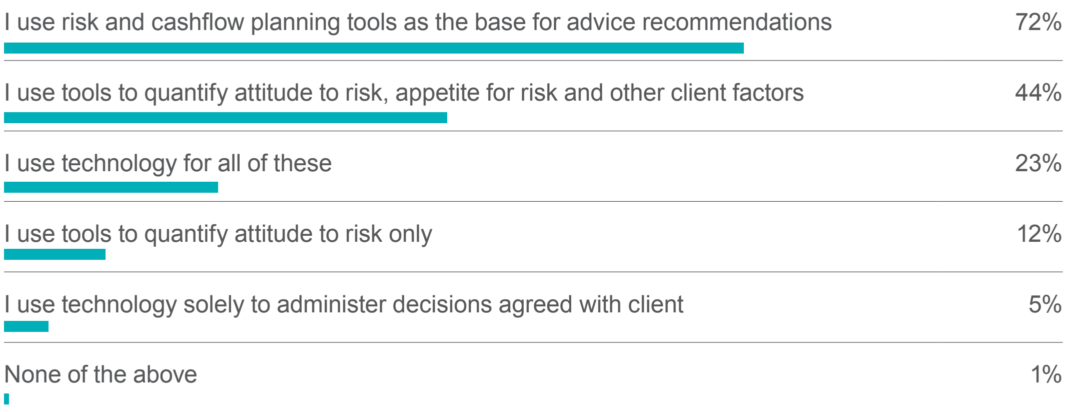


There are a number of new tools emerging, as well as some tried and tested cashflow modelling tools that are useful to help model retirement outcomes.

It is unsurprising that almost three quarters of advisers rely on cashflow planning and risk tools together and a significant number of advisers use other risk measurement tools, which is telling as in the new era of retirement planning risk is the key lever to pull when trying to make a finite pot last longer.

There are very few advisers that don't rely on some kind of software-based planning tool.

How do you use technology (other than as a platform for holding assets) in providing advice to retiring/retired clients?



There seem to be two schools of thought when advisers are asked about their stance on decumulation for their clients.

The bigger party (40%) tend to create a seamless journey through the period of retiring with no sudden change of strategy, maintaining a client's risk profile.

The second party (29%) deploy their CRP for retiring clients that incorporates a whole new set of products (and strategy).

This trend will be interesting to follow as the market becomes more refined.

Which of the following statements best reflects your stance on advising clients in retirement?

We tailor our advice but maintain a client's risk profile post-retirement	40%
We have a centralised retirement proposition using different investment products and tools than those used in accumulation	29%
We adjust a client's portfolio to generate more income/natural yield and have less risk exposure in retirement	12%
We adjust a client's portfolio to have less risk exposure in retirement	10%
None of the above	9%

It's a tough question to answer objectively, but it seems that advisers think that specific decumulation solutions available in the market are average and more needs to be done in this space.

When asked more specifically about which areas advisers would like more assistance with, the picture becomes clearer. As stated earlier, decumulation is in its infancy as a proposition, but when you offer up specific issues it becomes clear that advisers are looking for help on a number of fronts.

Sequencing risk solutions top the charts either as strategies or actual investment portfolios, followed by an assortment of planners, calculators, tools and delayed annuity strategies.

What product gaps do you think exist in the retirement advice market?

Sequencing risk tolerant investment strategies	52%
Specific funds or decumulation portfolios	45%
Cashflow forecasting/sustainable income calculators	35%
Delayed annuity strategies	33%
Variable drawdown	30%
Other	7%

When given the chance to comment, advisers are not short of an opinion or two on the subject of platforms and additional features they would like to see added.

The fact that these features aren't generally available on platforms again supports the fact that the decumulation sector is indeed in its infancy but that potential solutions are being talked about and in some instances actually being built.

Are there any features you would like to see platforms developing around retirement pathways?

Cashflow tools	Tax planners
Sustainable income calculators	Improved decumulation strategies
Income portfolios	Income strategy tools
Annuity purchase on platform	Volatility tools
Easier withdrawal	Sustainability warnings
Sequence risk assistance	UFPLS assistance
Multiple MPS	More MI/Reporting tools
Stress testing tools	Volatility tools
Visual aids	Forecasting tools

Specifically, advisers made the following points regarding desired platform features to cater for retirement pathways.

The main theme revolved around cashflow modelling and sustainable income tools:

"Adding cash flow analysis of the client portfolio based on performance and charges"

"[We would like to see] a mixture of low volatility investments and growth, so clients can draw an income without too much worry of being in a downturn, but not be penalised over the long term for growth"

Advisers were keen that platform functionality kept up with their new retirement strategies:

"[We would like] more visual aids and graphical reports with real life experiences based upon previous portfolio uses"

"Annuity purchase on a platform within a SIPP is very interesting, providing for security & flexibility, but I would like to see OMO within this product type"

It is absolutely to be expected that cashflow planners and sustainable withdrawal rate calculators feature large on adviser wish-lists for platforms to implement, along with a host of other planners.

As well as tools, specific products were highly valued, with a better range of income portfolios, more retirement biased MPS, sequencing risk-mitigating portfolios and annuities available on-platform were also requested.

Some advisers were keen to point out that these tools were available off-platform but it is interesting to note how much trust advisers are putting in platforms as a potential one-stop shop for their administration and technology requirements.

Risk in retirement

As noted earlier, risk is becoming increasingly more relevant in a modern retirement plan. In previous years, it was seen as essential to take clients on a glidepath from higher risk, lower risk and then income/natural yield strategies as they approached and then entered retirement.

Even today, that journey is still relevant to clients with large portfolios where wealth preservation is the priority.

But many clients are now approaching retirement with a finite DC pot and potentially 25-30 years of life expectancy to budget for.

Therefore, sweating that portfolio to drive more growth out of this extended time horizon means taking on more potential risk.

Given that backdrop, we were keen to see if advisers are talking to clients about taking on more risk.

Respondents indicated that in general, no more than 30% of advisers' clients are likely to want to take on more risk in retirement.

This makes a great deal of sense if you assume that adviser clients tend to be wealthier and may still be benefitting from DB pensions at this point. What is interesting is that although this is the first time we have asked this question, there is clear evidence of additional risk being discussed and taken on and we have to assume that this is in an attempt to stretch smaller pots over longer lifetimes.

What proportion of your clients would be willing to take on greater investment risk when in retirement?

0-10%	32%
11-20%	25%
21-30%	24%
31-40%	8%
41-50%	6%
51-75%	2%
76-100%	2%

Generating a sustainable withdrawal rate is still more of an art than a science. Reliance on cashflow modelling techniques are flawed insomuch as it models cash rather than investments.

Historically, planners have often used the ‘4% rule’ but this is a risky strategy.

We were compelled to ask if there is some persistence in the use of the 4% rule and asked what a sustainable withdrawal rate might be.

The top answer was indeed 4%, with 44% of advisers plumping for this option. What was telling was the bell-curve of responses show more advisers believing that the sustainable annual withdrawal rate is actually less than 4% and only 11% of advisers suggesting that you could withdraw more than 4%.

New technology on sustainable withdrawal rates is being developed now and can help advisers forecast a more bespoke output for clients, dependent of their investment portfolio and early signs are that higher percentages of withdrawal can be achieved for clients on a sustainable basis.

While on the subject of sustainability, there are a series of risks that can alter client outcomes, the most obvious one being longevity.

We asked advisers which risks had the greatest impact on planning a sustainable retirement income and were unsurprised to see sequencing risk come top. Major market movements, corrections and crashes, like the one we say in March 2020 can play havoc with client outcomes at, and during, retirement and is the most difficult risk to mitigate against.

Longevity risk is increasingly difficult to manage, as for the most part, we live much longer than the traditional ‘three score and ten’ that the state pension was set up to handle.

Failure risk (i.e. the risk of running out of money), volatility risk and inflation risk completed the responses with broadly similar impacts.

Please rank the following risks in terms of highest to lowest (where 1=highest and 5=lowest) of their impact on sustainability of income retirement

Sequencing risk (i.e. market falls early in retirement, reducing the length that a portfolio will last)	2.14 avg
Longevity risk (i.e. the risk of a client outliving their retirement portfolio)	2.18 avg
Failure risk (i.e. the risk that the client spent more than they had available)	3.29 avg
Volatility risk (the need to access a fixed income when the portfolio value has fallen)	3.53 avg
Inflation risk (i.e. understimating the long-term effect of inflation)	3.86 avg

Summary

The survey results show a much greater awareness of retirement planning as a separate specialism than we might have expected.

There seem to be two camps of respondents – one group that is starting to embrace new ideas, systems, products and tools – to enhance the retirement and decumulation journey.

The second believes that traditional tailored adviser techniques applied in accumulation can equally be applied to the retirement journey with an equal measure of success.

We are not judging whether one strategy is better than another, simply measuring the number of advisers who are adopting these strategies.

Given the fact that the decumulation market is in an early development stage, (in terms of services and products), we have a stake in the ground and can measure to see if there are further developments and usage by advisers in future surveys.

Chapter 5

A lull in regulation

f there’s one good thing the regulator has done in the eyes of advisers, then it was the prompt acknowledgement that the last thing firms wanted to deal with was a raft of regulatory change during the Covid pandemic.

The burden of regulation was cited as the top concern for 43% of advisers in last year’s survey, whereas in this year’s survey it has soared to 74%.

Whether the respite in relentless regulatory pressure was acknowledged and even welcomed by advisers allowing them to focus on their clients is unclear.

We were interested in finding out where advisers thought the regulator should be aiming their attention in future and it’s interesting to report that more than two thirds of advisers believe the FCA should be trying to address the widening advice gap.

In tandem with this is that the second highest priority (49% of advisers) was to provide some form of financial education to consumers. Advisers have been really consistent in their views here as these were the key findings from last year’s survey too.

There are also calls for better frameworks to be established for both ESG investing and the post-Brexit market. Both are currently viewed as unclear.

One third of advisers feel that the regulator needs to tackle the rise of vertical integration and consolidation in the market, although one wonders how this might be achieved, given it is an issue that arises year after year.

There are several other calls for the FCA to focus on, but an interesting point is the use of AI and robo advice and how they might be incorporated into advisers’ investment propositions.

Is this the first signs of adviser firms looking to use technology in a bid to address the advice gap?

Although delayed, the FCA will be reviewing how successful the Retail Distribution Review (RDR) and the Financial Advice Market Review (FAMR) have been in achieving their objectives. What themes/aspects of the industry would you like to see the FCA looking at?

Addressing the advice gap	67%
Improving the provision of financial education among consumers	49%
Developing a common framework for ESG investing	42%
Developing a regulatory framework for a post-Brexit market	35%
Tackling the increase in vertical integration and consolidation of the market	33%
Further increasing transparency in relation to the cost of advice	25%
How AI/robo advice can be integrated into an investment proposition	22%
Reviewing levels of professional qualifications for advisers	21%
Further investigation into contingent charging in the pensions transfer	15%
Investors reluctant to jeopardise returns	13%
Was unaware that RDR and FAMR are to be reviewed	3%
Other	5%

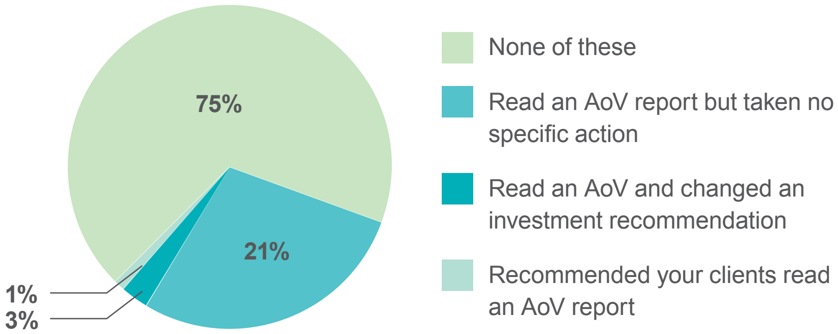
One of the new pieces of regulation introduced in September 2019 was the Assessment of Value statements that asset managers were required to produce on each of their funds. These were supposed to be of use to advisers in their assessment of suitability for clients, but our survey showed that they are being largely ignored. Just 3% of advisers have read an AoV report and changed an investment recommendation while three quarters of advisers just don’t read them.

It will be interesting to see, post-pandemic, whether the uptake of AoVs increases from a very low base.

“Given that most of those who read Assessment of Values reports are either fund groups’ competitors, or the press, it is not surprising that many advisers are not paying them much attention. In any case, they were not primarily designed for adviser use, so the impact they have had on the advice industry has been negligible.”

Mikkel Bates, Regulations Manager, FE fundinfo

In 2020 fund groups had to produce Assessment of Value (AoV) Reports. Which of the following have you done since their introduction?



Another piece of regulation that came into force just before the start of 2020 was the Senior Managers and Certification regime (SMCR), designed to make individuals within firms more responsible for their actions in order to boost accountability and integrity.

83% of advisers believe this legislation has made no difference, with just 10% saying that this has improved the health of the industry.

A year on from the Senior Manager Certification Regime (SMCR) coming into place, how would you say that it has improved the health of the industry?

"For most advisory firms, roles and responsibilities are usually clearly defined. In most small businesses, it is quite clear who is in overall charge, so SMCR regulations are not likely at all to impact on adviser thinking."

Mikkel Bates, Regulations Manager, FE fundinfo

Summary

Although regulatory pressure and regulatory costs are never far from the top of the list of concerns for advisers, there seemed to be some perspective gained from a more measured regime throughout the pandemic.

What is interesting is that, despite the introduction of new regulatory measures, these are not only going largely unappreciated by advisers, but more importantly by their clients.

If the people that are supposed to be the beneficiaries of regulation are not seeing the benefits, surely the FCA should turn their attention to some of the bigger market failures, primarily the advice gap and consumer education, which seems to be a consistent area of concern.

By contrast, recent regulation, such as AoVs and the SMCR are viewed as offering little benefit to end consumers and another area of cost and frustration for advisers, who have tended to take a more relaxed view to their obligations in respect to these implementations.

"Moving forward, we can expect greater divergence from Europe in regulations. The long-awaited Brexit deal made no mention of financial services and equivalence remains unlikely. The FCA in any case works differently from EU regulators, in that it is principles-based and less prescriptive. This approach is likely to lead to a different set of regulations for UK advisers in the longer term."

Mikkel Bates, Regulations Manager, FE fundinfo

Final thoughts

How do you frame the year that was 2020?

Many have marked 2020 down as the worst year ever, but for financial advisers it was defining.

Not only did the industry demonstrate remarkable fleet of foot to adapt to the lockdown economy, but by almost every measure, the industry actually grew.

There are many factors at work here that have led to a coming of age of modern financial advice as a profession and the pandemic may have given evolution a shove in the back to get to a remote working and servicing model that dramatically boosts efficiency and reduces costs.

With the FCA shelving many initiatives during the pandemic, advisers could just get on with their businesses without having to spend time boning up on the latest new rules and regulations. Did this contribute to the success seen over the year?

There were several major tailwinds that put advisers on the right side of the fence as the UK saw industry and commerce polarise into winners and losers.

- Heightened client engagement
- Efficiencies from new technology
- Video technology helped to facilitate servicing of more clients more often
- Some reduction in costs through remote working
- Two booming sectors – ESG and retirement planning
- Huge demand for adviser services

It's difficult to fully assess the status of the industry given the pandemic, but there definitely seems to be real evidence of progress made in terms of efficiencies through the use of technology, which further builds the credibility and professionalism of advice firms.

There are also strong signs of major leaps forward in developing stronger and more sustainable retirement propositions, with firms investing and interested in finding new ways to deal with the challenges for clients in a pension freedoms and DC world.

The star of 2020 has been ESG, which is developing rapidly into a mature, credible and professional sector to keep pace with high consumer demand. The appeal of ESG investing to a different audience, coupled with low interest rates and existing client needs has presented a huge opportunity.

But, in the minds of advisers it seems the constant “Sword of Damocles” of the amount of energy firms might have to divert to continue meeting the pent-up demands of the regulator remains a worry. Will a steady stream of new regulation come back and ruin the momentum built up in 2020?

Overall, 2020 has been a positive year overall for advisers.

The market demonstrated that ESG funds are the place to put additional disposable income bringing new investors flocking, whilst lockdown and Covid restrictions gave people the time to sort out their finances and invest unspent cash.

While these conditions undoubtedly helped to create demand for advice, the industry showed remarkable ability to adapt and capitalise on this demand, in a year that has tested us all.

FE fundinfo