DIGITAL DNA 2.0

How advisers can maximize trends in advisory technology

ORANJ

IN RESEARCH

FOREWORD

Uncovering the Latest Adviser Technology Trends

The financial advice industry has seen seismic shifts over the past decade that have changed the very fabric of what it means to invest. Technology has been, and continues to be, a major driver of change in the industry. Every type of business - from wirehouses to independent broker-dealers to registered investment advisers - has integrated technology into the foundation of their services and processes.

However, all technology is not created equal - and neither are the benefits it can bring to advisers, institutions, and the investors they serve.

Oranj has partnered with *InvestmentNews* for this study to seek out the answers to three fundamental questions:

- What does the future of technology investments at both institutions and independent advisory firms look like?
- What are the differences in perceived value of technology when comparing institutions and independent advisers?
- How are major institutions evaluating technology at a large scale, and what are the institutions' findings that can be applied by independent advisers?

Many large institutions in the advisory business have teams and budgets dedicated solely to evaluating the technology that's made available to their affiliated advisers. With these types of resources, they are able to make data-driven determinations that ultimately dictate their technology implementation decisions and budgets.

Yet many RIA's do not have the time, resources, or scale to conduct that type of detailed technology assessment. Through this study, Oranj sought to uncover the outcomes of in-depth technology evaluations, produced by large institutions, that can easily be applied by the broader market of advisory firms.

On behalf of Oranj and *InvestmentNews*, we hope you find tangible value in some of the findings covered in this study. We believe that with world-class service, expertise, and the right technology, financial advisers and institutions today can solve critical problems and help evolve the industry for the better.

David Lyon
Founder and CEO
Oranj

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Executive summary

Since 2016, the operating environment for advisers and their firms has been extremely supportive. While all firms have tended to do well, the firms showing the greatest growth were those that made a commitment to technology — specifically in areas that improve outcomes for clients and improve firm efficiencies and internal processes.

With digital tools becoming ubiquitous in all aspects of everyday life, and with investors of all ages increasing their reliance on these tools, their use in the advisory business must keep pace. Firms that are in the forefront of developing, adopting and promoting user-friendly digital interfaces and services will be the ones who gain market share and prosper in the years ahead. Advisers seeking to do the same should seek out the firms that provide such tools and those which use them.

Advisory firm technology: Driving growth

Facing regulatory headwinds and market uncertainty in 2016, advisory firms and many of the financial institutions that support advisers, have experienced a turnaround and are now enjoying a period of robust growth. Revenues have rebounded and the future is full of promise.

Independent advisory firms saw double-digit revenue increases in 2017, after two consecutive years of declining top-line growth, as illustrated in Figure 1. The independent broker-dealer channel also saw a resurgence: The group's top 25 institutions generated a combined $23.2 billion in revenue in 2017, a 13.1% annual increase and the best revenue performance in the 14 years that InvestmentNews has collected financial data from the largest IBDs (Figure 2).

FIGURE 2: REVENUE OF THE TOP 25 INDEPENDENT BROKER-DEALERS

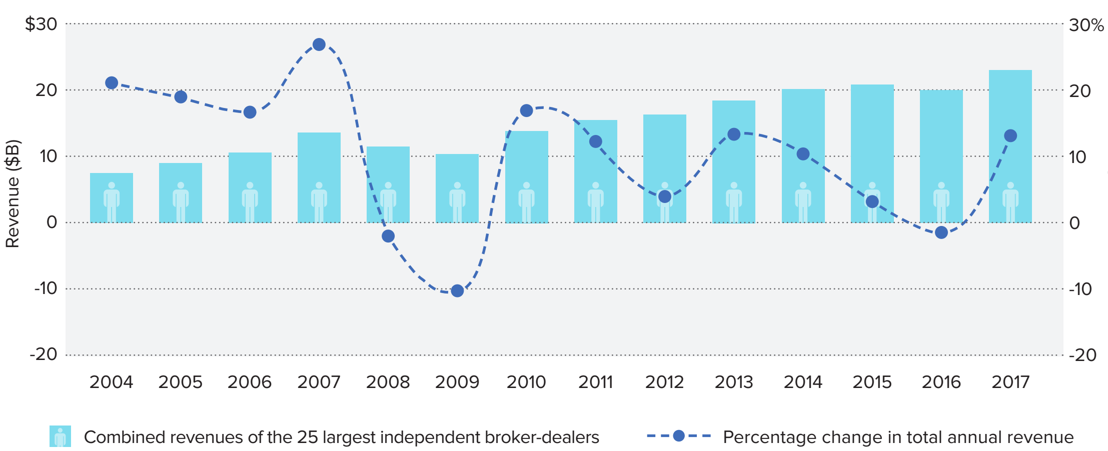
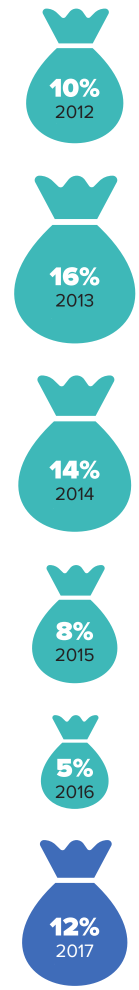


FIGURE 1: MEDIAN REVENUE GROWTH RATE (INDEPENDENT ADVISORY FIRMS)



Based on our research, we believe that recent performance will provide a unique opportunity for firms to re-invest in their businesses, especially in the area of technology, and make adjustments that could fuel future growth.

Technology is so important because our research found a direct correlation between technology investments and growth rates. The top-performing independent advisory firms – those in the top-quartile of growth in revenues, assets and profitability – had technology budgets that were 21% greater than all other firms, on average. This contributed to average revenue growth of roughly 14.6% for top-performers, vs. 10.5% for the remainder of the field.

Since it is clear that technology increasingly will drive success for advisers and their firms, this paper will detail and explore:

- Areas of recent and future technology investments
- How a new mindset surrounding technology investments and strategies will re-shape the advice industry
- What the new technology environment means for advisers

Technology spending and growth

At the core of our findings is a near consensus statement from advisers about their individual growth opportunities: Nearly nine out of ten advisers who participated in the 2018 InvestmentNews Pricing & Profitability Study indicated that their revenues will increase over the next three years – with 50% of advisers anticipating revenues to grow by at least 5%. In line with these expected revenue upticks, both operating profits and adviser compensation are anticipated to increase by 81% and 76% of advisers, respectively, in three years:

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IMPACT: There is a direct correlation between technology and growth – and top-performers are already reinvesting in the next generation of tools to improve clients' digital experiences.

FIGURE 3: ANTICIPATED INCREASES IN REVENUE, SPENDING OVER THE NEXT THREE YEARS

[1] 2018 *InvestmentNews* Pricing & Profitability Study. Advisory firms reported 19.9% average AUM growth in 2017 Markets contributed 8.7%, or 44% of the 19.9% net increase

Growth will not come only from the rising value of assets under management. While market appreciation has fueled 44% of the recent increase in advisory firm assets in 2017 , many advisers – and institutions – are looking to make new investments in technology to help improve their internal operations, as well as the digital experience delivered to clients and prospects.

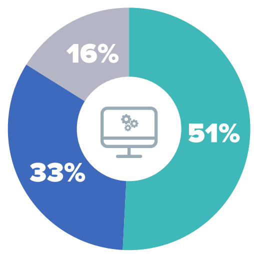
Seven in ten advisory firms anticipate that they will increase their technology budgets and investments over the next three years, with roughly one-third of those firms increasing their spending by at least 5%.

Technology tops the list of areas for strategic investment, slightly outpacing marketing, business development and compliance over the next three years. Reinforcing the emphasis on technology, 84% of advisers noted that technology will play a critical role in achieving their firms' future growth goals.

At the advisory firm level, the industry's largest firms will be driving the increased investments in technology – with the $1 million in annual revenue level serving as the industry's equator. Nearly 80% of firms with more than $1 million in annual revenue, for example, reported that they will invest more in technology over the next three years, whereas only 60% to 70% of firms with revenue under $1 million will increase their technology spending.

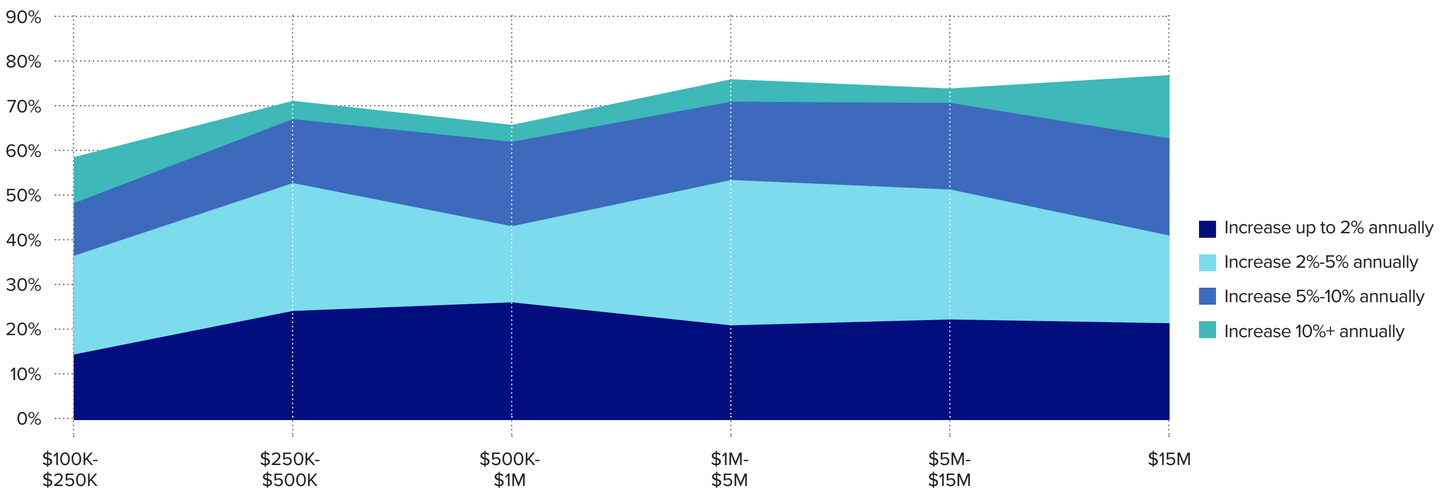
It is also worth noting that the industry's largest RIA firms, or those with more than $15 million in annual revenue, are the most likely to increase their technology spending by at least 10% over the next three years, as noted in Figure 4:

FIGURE 4: THE ROLE OF TECHNOLOGY IN FIRM GROWTH



- Fully utilizing my firm's current technology
- Investing and new and emerging technology
- Technology will not play a significant role in my firm's ability to grow

FIGURE 5: ANTICIPATED TECHNOLOGY SPENDING CHANGE OVER THE NEXT THREE YEARS, BY FIRM REVENUE



The largest firms are expected to make the largest investments in tech – potentially distancing themselves further from the pack, while also re-shaping client's digital expectations

On a relative basis, a similar set of strategic investments in technology are expected in the independent broker-dealer channel as well, where 88% of firms said they would be increasing their technology spending in 2018, with a median projected growth rate of 12.6% and an average of 15.7%. In 2017, the typical IBD spent $2.3 million on median, or $7.2 million on average, on technology.

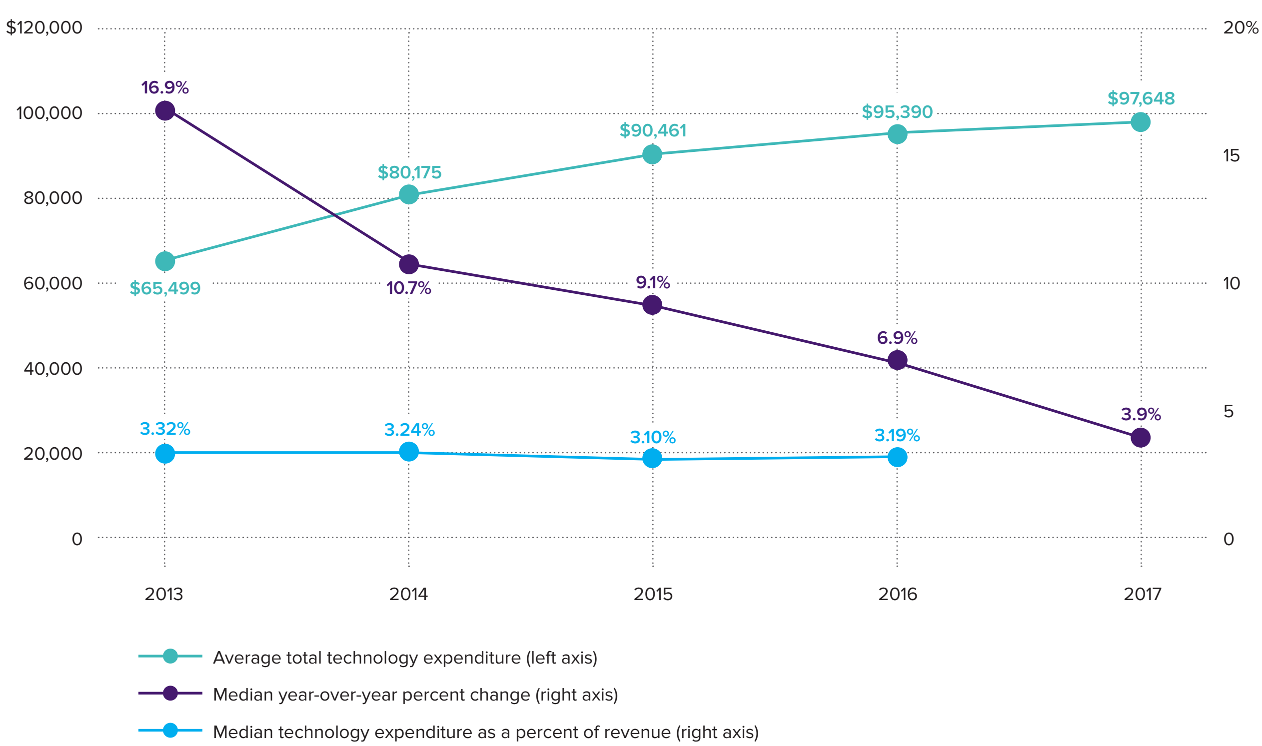
The focus of new technology spending

Future technology investments likely will continue the recent build out of platforms. Over the last several years, advisers and institutions have focused on leveraging technology that is "purpose built," or specifically tailored to support the back office and data management needs of a financial advisory firm's core business functions and workflows.

Overall, the pace of this core technology spending is cooling, despite the overall increase in tech investments. From 10.7% in 2014, the median year-over-year increase in total technology spending dropped to 9.1% in 2015, 6.9% in 2016, and 3.9% in 2017, according to the InvestmentNews study. Figure 6 below details both the rate of technology spending, as well as average spending at independent advisory firms:

While the technology stack at most independent firms has matured, many firms have identified themselves as "second-movers" – and are waiting to see what frontend and client-facing applications will provide the most return.

FIGURE 6: TECHNOLOGY SPEND LEVELS AND GROWTH RATES (2013-2017)



For most firms, the anticipated acceleration in spending over the next three years will be focused in two key areas: Optimizing the existing technology stack and identifying new and emerging technologies that improve productivity, as well as client and prospect interactions.

The vast majority of advisory firms are already leveraging and managing multiple technology applications, with customer relationship management and financial planning software at the core of their technology platforms, as outlined in Figure 7. At the other end of the spectrum, while few firms reported that they are currently using digital account opening, video chat or digital advice applications, each of these tools are now readily available and present advisory firms with easily employed ways to enhance the client experience.

The technology offered by broker-dealers shows a similar alignment and prioritization of core advisory firm technologies. Notably, however, broker-dealers have made significant investments in compliance and document management technology relative to spending at registered investment advisory firms. At the same time, while a vast majority of broker-dealers are offering client portals, electronic signature solutions and fully digital account opening solutions, the broad advisory industry lags in their usage rate.

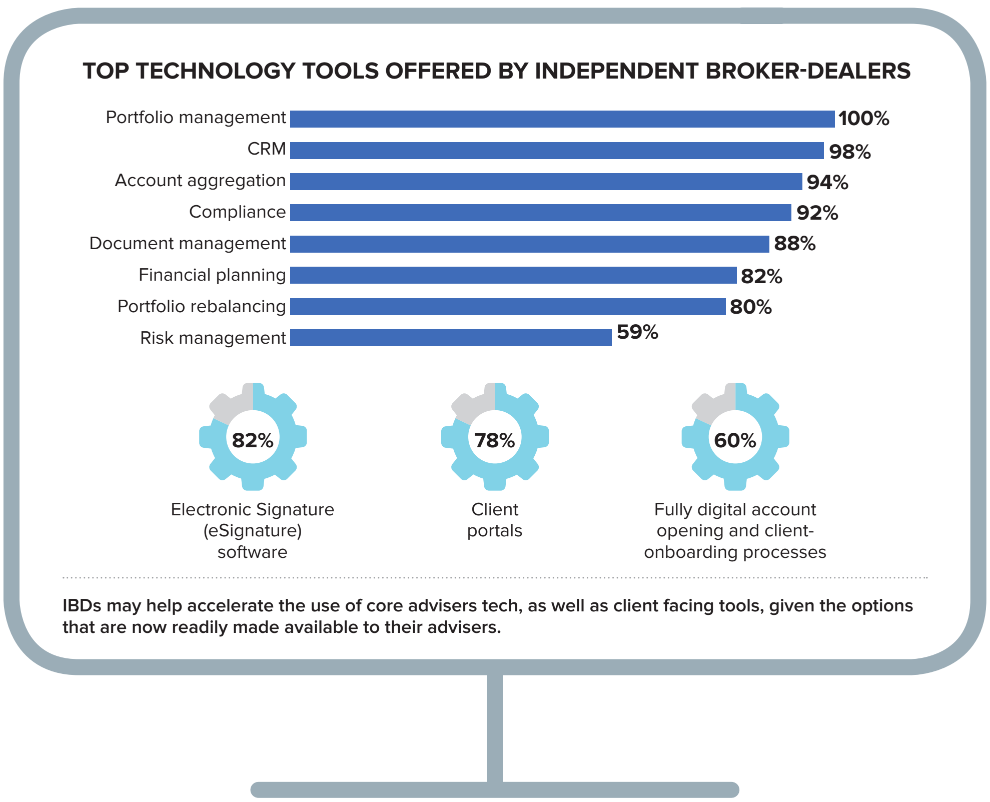
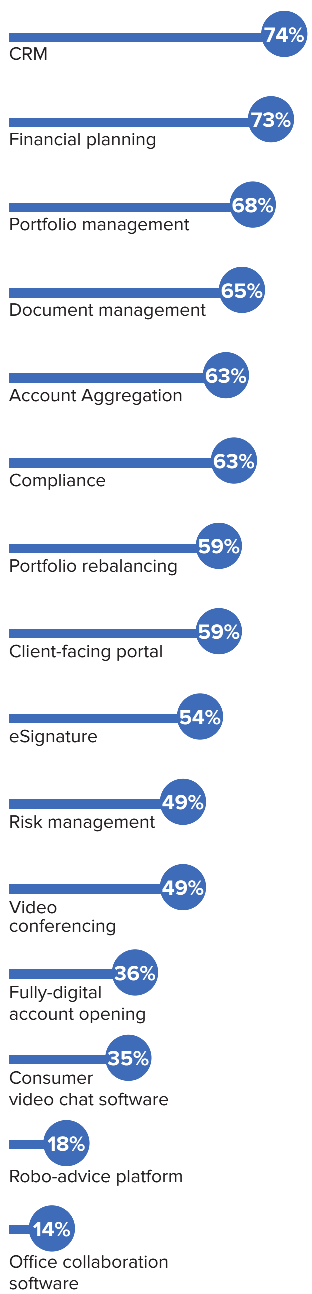


FIGURE 7:
ADVISORY FIRM TECH STACK – SOFTWARE AND APPLICATION USAGE RATES



These technologies have been at the heart of many broker-dealers' recent investments, ***as well as their focus on providing advisers with tools that provide improved investor-facing – and essentially more digitally relevant – experiences.*** The gaps in adviser adoption actually foreshadow, we believe, what will likely be a significant increase in adviser adoption rates over the next 12 to 18 months.

What advisers and firms want from new technology

As noted, RIA firms are placing greater emphasis on productivity when investing in technology. Specifically, advisers ranked "improve workflows and create efficiencies" as their top consideration when evaluating technology, followed closely by cost, improved client outcomes and integration, as detailed in Figure 9:

For broker-dealers, the primary consideration in evaluating a technology solution is its ability to integrate with existing applications (65%), as outlined in Figure 10 below, followed by adviser satisfaction (50%) and alignment with the broker-dealer's service model (43%):

FIGURE 9: INDEPENDENT BROKER-DEALERS' TOP CONSIDERATIONS WHEN EVALUATING TECHNOLOGY

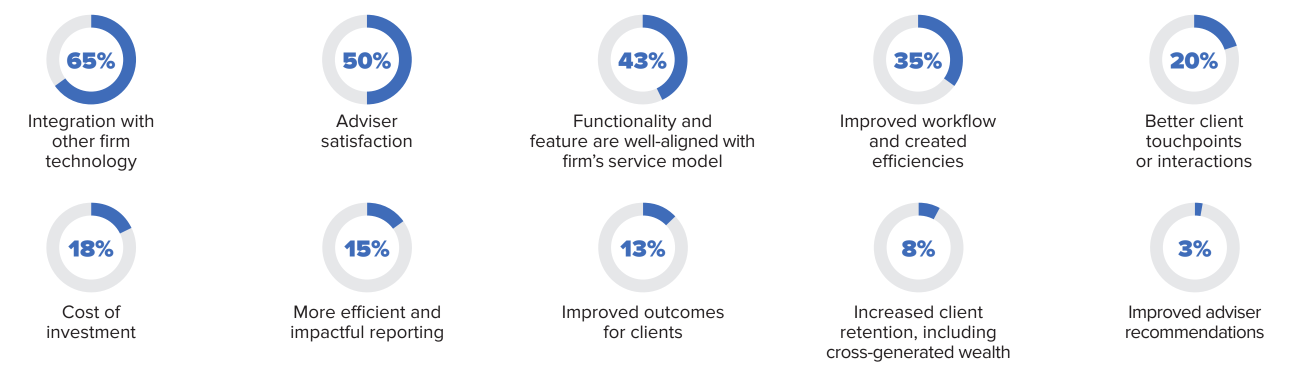
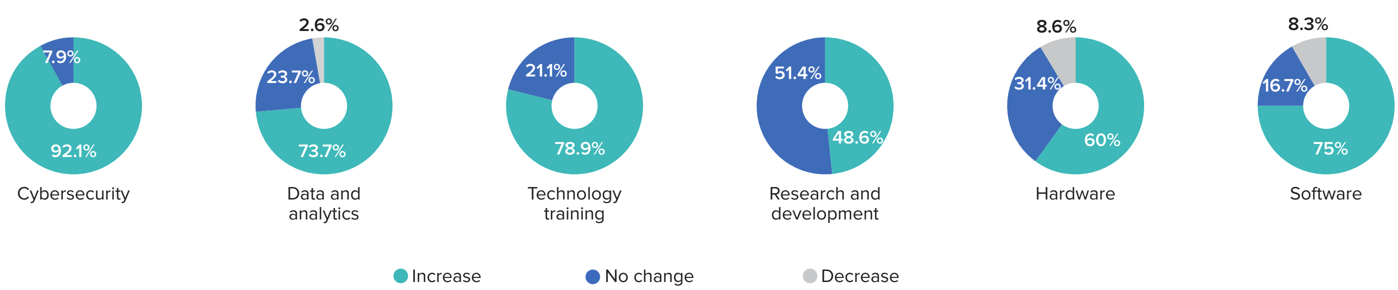


FIGURE 10: 2018 PROJECTED INDEPENDENT BROKER-DEALER SPENDING



Looking ahead, broker-dealers will target their technology investments consistently at important, but utility-like, functions. For the full year of 2018, cybersecurity and technology training rank as the top two areas for increased technology investments for independent broker-dealers, as Figure 11 illustrates.

On the surface, while these interests might appear to indicate a divergence in the technology agendas of advisers and firms, we view them as more complementary than conflicting. Combined, these priorities and areas of emphasis can power both the proactive and defensive strategies of a financial advisory firm. By focusing on protecting client and firm accounts, accelerating technology adoption and its execution, and improving overall productivity, broker-dealers are enabling advisers to explore ways they can improve their own productivity and organic growth, while also leveraging technology to deliver more customized services and advice.

Where 'Tech Accelerators' are directing technology spending

To better understand how technology investments might affect advisers and the advisory business in the future, we decided to analyze the behaviors of those firms currently in the forefront of technology investment. These firms, which we have dubbed "Tech Accelerators," are increasing their technology investments by at least 10% over the next three years, and also are the most likely to be early adopters of new technology.

Accelerators also are more likely to increase technology spending over the next three years in all categories, including spending on software and hardware, as well as technology training. They also, notably, are more likely to have employees who specialize in technology (46% of Accelerators have such employees, compared with 29% of all other firms) and business development (52% vs. 38%) – indicating that they have assigned a clear value to both the management of technology, as well as their firm's ability to grow organically.

Like other firms, Tech Accelerators are striving to improve their overall productivity. But more than other firms, they are paying particular attention to ways they can improve the client experience through an enhanced technology platform. Their primary objective, by far, is improving outcomes for clients, with 44% of Accelerators indicating this as their top consideration. By comparison, all other firms ranked the cost of technology and improved workflows (27% for both) as their main consideration when evaluating and investing in technology, as outlined in Figure 11.

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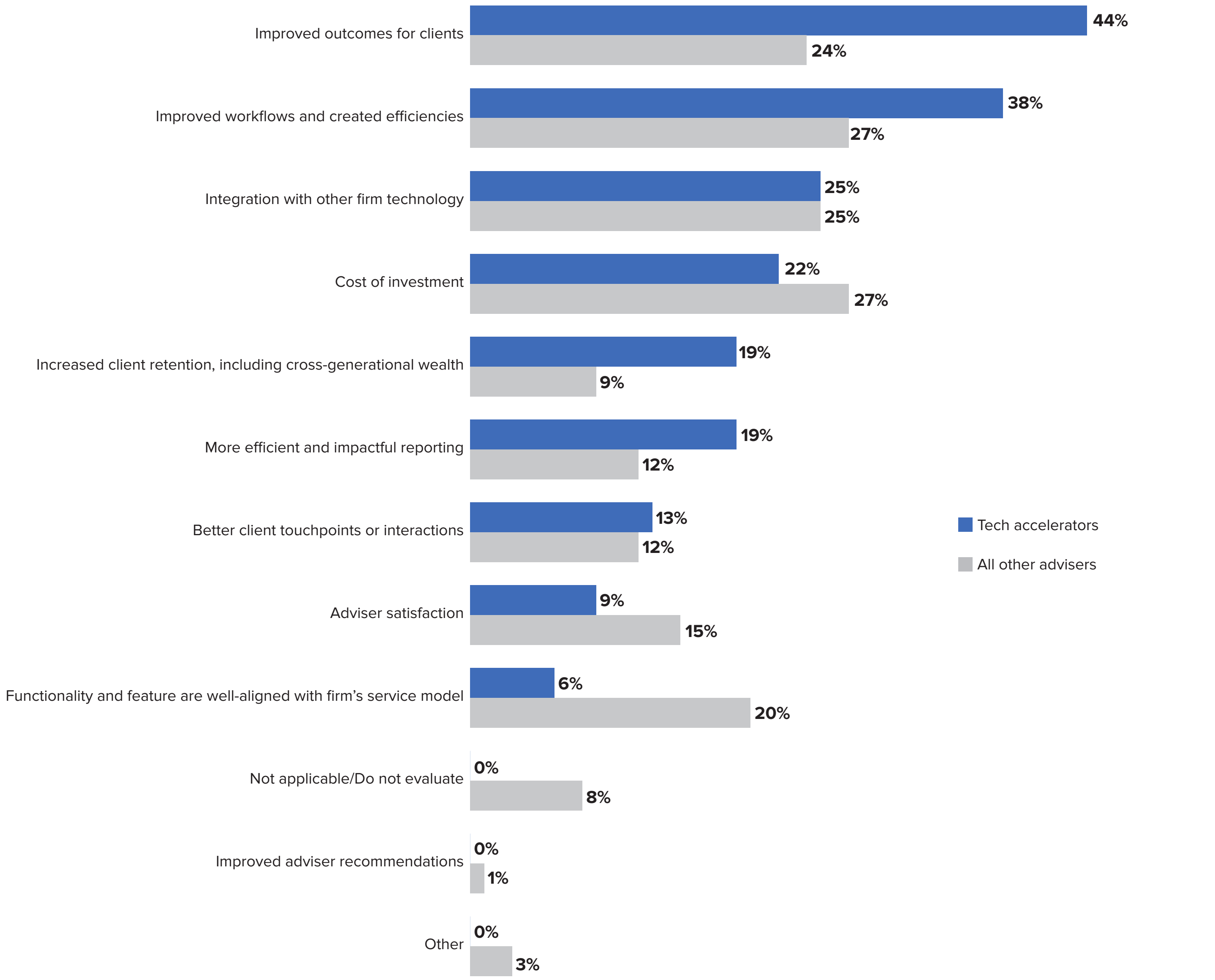
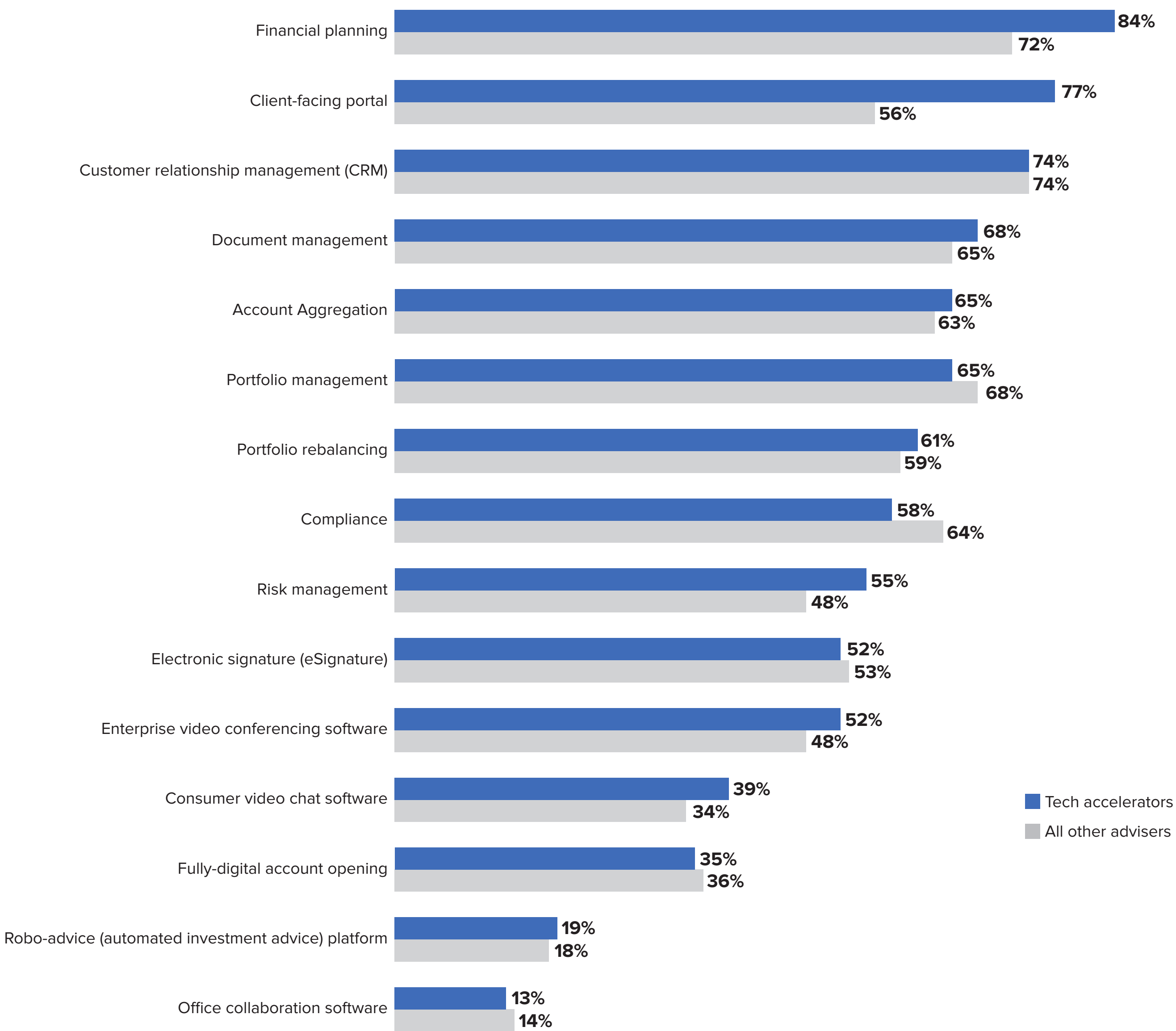
Accelerators, by a nearly two-to-one margin, will be emphasizing improved client outcomes as they look to make their double-digit increases in spending over the next three years. Additionally, Accelerators are putting a premium on improved workflows and efficiency, with 38% indicating that it is a top priority, compared with 27% of all other advisers.

FIGURE 11: TOP CONSIDERATIONS WHEN EVALUATING TECHNOLOGY INVESTMENTS – TECH ACCELERATORS VS. AVERAGE ADVISORY FIRM



The Accelerators have already committed, specifically, to leveraging more client-facing and consumer technology tools to provide improved services and delivery of advice to their clients. When examining the technology stacks of Accelerators compared with other advisers, there is a clear separation in the use of client portals – 77% vs 56% -- risk management, enterprise video conferencing tools, and consumer video conferring tools, as noted in Figure 12.

FIGURE 12: TECHNOLOGY APPLICATIONS AND SOLUTIONS USED, TECH ACCELERATORS VS. AVERAGE ADVISORY FIRM



Conclusions and takeaways for advisers

Technology has evolved from an advisory business expense into a strategic investment that enables firms and advisers to meet the expectations of current and future clients. For principals of advisory firms of all sizes, as well as for advisers themselves, the key implications of this change — and the takeaways for action — are the following:

Technology drives growth. Among the largest advisory firms — those with more than $1 million in revenue — nearly 80% plan to increase their technology spending over the next three years. This is in contrast to smaller firms, where only 60% to 70% of firms plan to spend more. While all firms have tended to do well over the past two years, the firms anticipating the greatest growth have been those that are spending more on technology -- specifically in areas that improve outcomes for clients. **The bottom line:** Advisory firms that are growing the fastest believe that technology investments pay off.

Technology solves real problems. Increased investments in technology and improved adoption rates over the last several years have directly translated to better workflows and proven efficiencies throughout the advice industry. Tools such as customer relationship management (CRM), used by 74% of firms, financial planning software (73%) and portfolio management tools (68%) have allowed scores of firms to experience how purpose-built technology can solve real business issues within a firm.

However, many firms have indicated that when it comes to investing in emerging technology, a lack of track record or proof point can be a deterrent from making a new investment. Look no further than our Accelerators: These firms at the forefront are more likely to employ lesser-used tools, such as a client-facing portal (59%), fully-digital account opening tools (36%) and client video-chat software (39%). These solutions are being leveraged specifically to solve for more client-facing problems and will directly address common challenges advisers face in proving an improved client experience. **The bottom line:** Firms want to emulate the leaders should adopt these newer and lesser used tools.

Technology spending should be focused. Among firms we have dubbed Tech Accelerators — those in the forefront of tech investment — 55% say they will grow revenue by 10% or more on an annualized basis over the next three to five years (vs. just 17% of all others) and 46% say they will grow operating profits by 10% or more over that time period. This compares to just 17% and 13%, respectively, of all other firms that share those expectations. This difference between accelerators and other firms is, like their motivation to invest in tech for improved client outcomes, statistically significant. What's significant too are the areas in which the accelerators are focusing their tech investments to a degree greater than other firms: technology that improves outcomes for clients (44% vs. 24% for other firms) and improved workflows and created efficiencies (38% vs. 27%). **The bottom line:** Follow the leaders and invest in the areas where they believe they can capture a competitive advantage.

Technology has become democratized. Fortunately for smaller advisory firms and individual advisers, the marketplace for specialized advisory technology and tools has grown. A firm of any size now has access to the technology that once was only available at the largest firms, and the latest and most useful tools effectively can be employed with guidance from leading vendors instead of being developed in-house.

More than anything, what's needed for success is a commitment putting clients' needs first and aligning advisory operations and service to meet those needs. For advisers and firms willing to make the commitment, technology provides the road to a very bright future.