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Why goals-based advice?

A profitable, client-centric model for progressive financial advisers

Matthew Walker

The purpose of any advice business is to help its clients to achieve what they want to achieve. So, why is talking about goals-based advice seen as being 'different' from what financial planners have always done?

We believe advisers are talking about goals-based advice more because it represents a paradigm shift in the industry away from selling products to focusing on each client's specific needs.

Client expectations are changing. Technology and interconnectivity mean clients have access to more information and choice than ever before.

Clients are more demanding of advisers to deliver strategies and solutions that match their specific needs.

The potential impact of the goals-based advice approach to improve the outcomes for clients and financial advice businesses are significant.

This paper focuses on the advice side of helping clients achieve their goals and looks at why taking a 'goals-based' approach is so vital for the future of any advice business. We have differentiated goals-based advice from goals-based investing, which is a separate topic.

How is it different from traditional advice?

Goals-based advice is an alternative to the traditional risk-profiling approach based on modern portfolio theory. Instead of starting with risk tolerance, goals-based advice focuses specifically on meeting clients' lifestyle objectives, including investment portfolios.

The first and most crucial task involves developing an understanding of all relevant client needs and issues in order to establish a suitable client-centric solution. Therefore, while understanding risk tolerances is a factor, the formation of goals is the starting point for developing strategies and portfolios.

The question for many advisers is how to implement goals-based advice.

Clients most satisfied with goals-based approach

An Investment Trends survey conducted in early 2018 provided some simple, logical and interesting observations about what goals-based advice meant for clients:

- Financial planners with the most satisfied clients "are often those who are successful in creating congruity between the client's investments and their goals".
- Many of the financial planners surveyed said they intend to become more goal-orientated in their approach.

- However, 87% cited challenges in the provision of goals-based advice as new models are in their infancy.
- Over half of the surveyed planners were unable to nominate any provider as 'best-in-class'.
- The adoption of managed accounts has seen strong growth as more planners choose them for the efficiency benefits offered over investing directly in shares and traditional managed funds.

In summary, clients were more satisfied with goals-based advice, and advisers are seeking such a solution for their business.

Communicating with clients

When using the goals-based approach, there is no fundamental change to the general nature of conversations that financial advisers have with clients. Advisers have always asked the question, 'What are your goals?'

What does change is the focus of the conversations. The conversation is focused more on the client and less on investments, markets and products—the technical aspects. It is focused on what clients want to achieve in their lives. This approach helps foster a deeper sense of understanding and empathy that, in turn, helps to develop trust and client engagement.

In a purely practical sense, advisers have a limited amount of time to meet face to face or talk with their clients. Over a year, it is usually measured in hours. This means there is literally not enough time to go through all the specific details of each product or investment. In reality, achieving a genuine understanding of technical matters is close to impossible. Clients can be left confused and underwhelmed.

If an adviser aligns strategies and investments with specific goals, it changes the focus from investments, markets and arbitrary benchmarks to a focus on goal completion. In the 'Seven steps to goals-based financial planning', Morningstar Investment Management's head of retirement research, David Blanchett, summarised it as follows:

"Most individuals aren't financial experts. They don't speak in terms of alpha and beta, or even keep up with their accounts on a daily basis. However, when the time comes for them to accomplish one of their financial goals—whether it's funding a child's wedding or settling into retirement—they need to know the money will be there.

"This is why the financial planning profession must be built around helping people accomplish their goals. It's not only an opportunity for you to provide better advice to individuals; it's a way for you to speak their language and make closer, long-lasting connections with your clients."

Investor behaviour and psychology

It is well documented and understood that investors often make irrational decisions when it comes to their finances and investments. Part of an adviser's role has always been to help educate and guide their clients through the process. However, the challenge has always been that the current approaches involve substantial quantitative input, whereas client input is highly qualitative around themselves and what they want. It can be difficult for clients to understand and engage because they are speaking a different language.

When a client does not fully understand what they are doing and why, either strategically or at the portfolio level, then it is very hard for them to see the value and buy into the solution. They are prone to base psychological influences of 'fear' and 'greed' and act accordingly—usually at the most inopportune times.

Example 1. Risk profiling and suboptimal decisions

If using a typical risk profiling approach to make investment decisions, what we find is that when markets are buoyant, investors typically feel euphoric and want to invest (at the top). However, when markets are correcting people become fearful and want to realise their investments (at the bottom). This is completely the opposite to what advisers know is the right thing to do.

EY summarised the challenge in its *Goals-based planning: a personalized service for strengthening client relationships* report:

"Since the global financial crisis and ensuing recession, the desires—and fears—of investors have changed dramatically. Investors seem less confident and more risk-averse than they were just a few years ago. They want more—and better—advice from financial advisors, yet they also want to wield more control over their financial lives."

Simply, aligning strategies and investments with specific goals to help clients with their mental accounting at a granular level changes the focus from investments, markets and arbitrary benchmarks to a focus on goal completion. The result is better understanding, continuity and control. In these circumstances, clients are less likely to be reactive to short-term market conditions and more focused on their goals.

Operational aspects

So how is goals-based advice delivered effectively and efficiently?

While the adviser's role and function does not change significantly, there are some operational and business issues to consider:

- How to communicate with clients (e.g. newsletters, seminars, one-on-one meetings, build into it through a review cycle)? There are many ways to get the message across to clients depending on the approach, but it should be carefully thought through before delivery.
- Will professional indemnity provide cover the model is

The quote

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changed from the more common risk profile approach to explicitly focusing on clients' goals?
- Can an adviser do what is necessary under their current Australian financial services licence?
- What alterations need to be made to the statement of advice and disclosure documents to reflect a consistent message across client conversations and reporting?
- How does one build investment portfolios that specifically match client goals?
- How does one find true-to-label goals-based investment managers that match clients' needs?
- How does one administer, measure and report on what is required?

All of these questions have established answers that are relatively simple to implement. Advice groups have and are moving down this path in increasing numbers because they know it is the right thing to do and because clients are increasingly demanding it.

True-to-label goals-based investment portfolios not only meet clients' needs across both investment and superannuation directly, but can also capture the benefits of technology, administration and reporting that allow advisers to increase profits.

The industry is also evolving behind the scenes to provide effective solutions for advisers—the use of improved technology such as planning software, platforms or managed accounts all increase operational efficiency.

Example 2. Leveraging business efficiencies through managed accounts

A 'Managed accounts research paper' issued by BT in 2017 found that using managed accounts saved an advice business 14.4 hours a week overall, giving the adviser an extra 4.8 hours a week to focus on new revenue-generating activities, thereby growing profits overall.

Each advice business needs to consider its identity, what their clients want, what they want to do and then find the best people to work with to 'plug any gaps'.

Better client outcomes

Morningstar Investment Management's head of retirement research, David Blanchett, argued that an optimal, goals-based strategy can add more than 15% in utility-adjusted wealth. That is a significant number that has a meaningful impact on a client in helping them achieve their goals.

In its goals-based planning report, EY found that focusing on meeting tangible short-, medium- and long-term financial needs on a lifetime basis helped give clients "a greater sense of clarity and control over their financial lives and increased "confidence in making investment-related decisions".

Advisers understand this. They know that by specifically focusing on the client and helping them to achieve their specific goals, they will have happier clients. It is an entirely logical outcome because the adviser has done precisely what clients have asked. Further, a happier and wealthier client base is both more satisfying and profitable.

Better business results

Today, more than ever, advisers and their businesses are under pressure. For instance:
- consumers are demanding more and better service at a lower cost
- public and press scrutiny are resulting in lower levels of trust
- there are increasing regulatory requirements and compliance burdens
- there are increasing training and education requirements.

Advisers must increasingly renew their value proposition and how they differentiate themselves from their competitors to become a 'provider of choice'. Goals-based advice plays very strongly to that theme.

As EY stated in its goals-based planning paper:

"Savvy financial advisors are using goals-based planning as a firm-wide strategy to attract clients, gain their trust and build long-term relationships".

Today's most progressive advisers are increasingly focused on building a more client-centric approach to doing business. They are finding that client relationships and strategic advice are central to the value they provide.

Further, to open up the capacity to service more clients, they are seeking outsourcing solutions to simplify the delivery of services that best meet their client and business needs.

As EY observed in its goals-based planning paper:

"Institutional investors, such as pension funds, endowments and insurance companies, have used goals-based planning for decades to make sure they have adequate funds available to meet future liabilities."

Advice businesses are now looking at how to bring that to the retail market to provide leading-edge solutions.

Completing the cycle: implementing goals based investing

The most critical question for an advice business to answer is how to deliver goals-based investing.

Goals-based investing provides the business with the complete capability to deliver transparent goals-based services that align with client needs.

Because goals-based investment portfolios are decoupled from a benchmark, managers have much more freedom in finding new opportunities that help the fund achieve real returns for clients.

It's time

The shift to true goals-based advice is now underway. It provides an opportunity for advice businesses to better meet the demands of today's clients.

Market leaders are providing the more holistic goals-based service through progressive service offerings, technologies and solutions. These will not only help them survive, but thrive in the current environment. **FS**