WealthManagement.com

Is it Time to Outsource Investment Management?

Potential benefits include more time for clients and growth in AUM

Adhesion wealth®

Investment management was once considered a core component of an advisor's relationship with their clients. These days, however, there is a strong case to be made for outsourcing the task of managing clients' investment portfolios. RIAs who outsource stand to benefit from more time to work directly with clients and more opportunities to grow revenues and assets under management (AUM). These are just some of the findings of a January 2021 WealthManagement.com survey commissioned by Adhesion Wealth Advisor Solutions and involving more than 330 RIA firms.

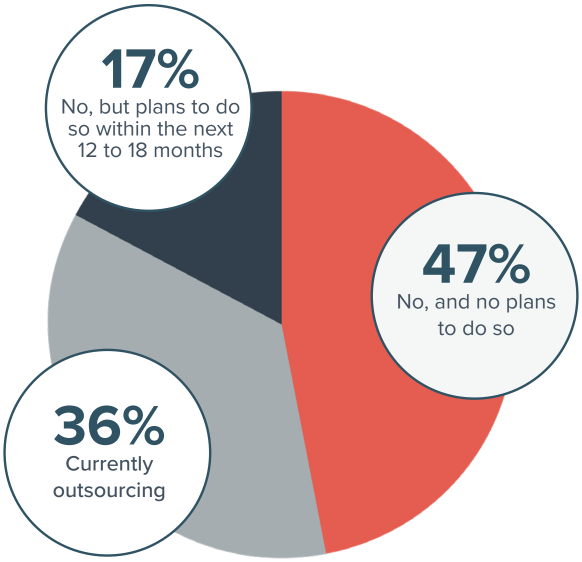
The survey's other key findings include:

- Outsourcing investment management is already widely adopted among RIAs.
- The main drivers for outsourcing are generally tied to improving client relationships.
- Advisors who currently outsource also link the strategy to growth in client numbers, in addition to the growth seen in AUM and revenues.
- Most advisor see a decrease in operating costs in conjunction with outsourcing investment management.

Outsourcing is already here

As a practice, outsourcing investment management is already an established model in the industry. More than half of advisors surveyed are currently outsourcing investment management or plan on doing so in the next 12 to 18 months. It is a strategy adopted by a range of firm sizes, in terms of either AUM or number of clients, as well as firms that offer a range of services.

Percent of Firms That Outsource Investment Management



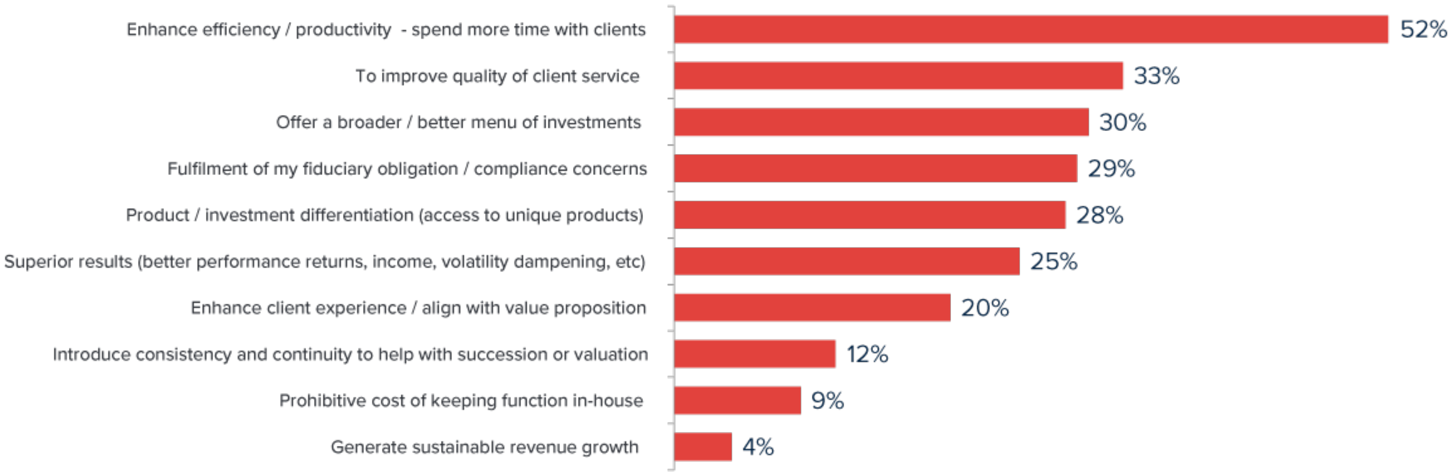
Outsourcing tends to be more common among RIAs working alone versus those already working as part of a team. Meanwhile, smaller firms with AUM of less than $100 million are more likely to outsource than to have no plans of doing so (45% versus 37%), while larger firms with AUM of $500 million or more show the opposite: 36% of larger firms report no outsourcing plans while 25% are currently engaged in the strategy. This trend is perhaps not surprising, as smaller firms may feel the pressure to outsource more than their larger peers to facilitate growth and expansion, and they may also lack the resources that larger firms have at their disposal to handle these services in-house.

This trend toward outsourcing investment management is not new. **More than 9 in 10 firms currently outsourcing their investment management services have been doing so for at least two years,** with 81% of advisors saying they have three or more years of experience to draw from. Based on this experience, nearly nine in 10 (87%) of advisors who currently outsource say the practice has had a positive economic impact on their firm, with 58% claiming the impact has been "very positive."

Outsourcing benefits clients...

Most advisors look to outsourcing so they can focus more time and resources on clients. In fact, more than half (52%) of advisors cite a desire to spend more time with clients as the main driver of their decision to outsource, while one-third (33%) cite improving quality of client service and 30% pursued the strategy to offer better investment options to clients.

Main Drivers of Outsourcing Investment Management

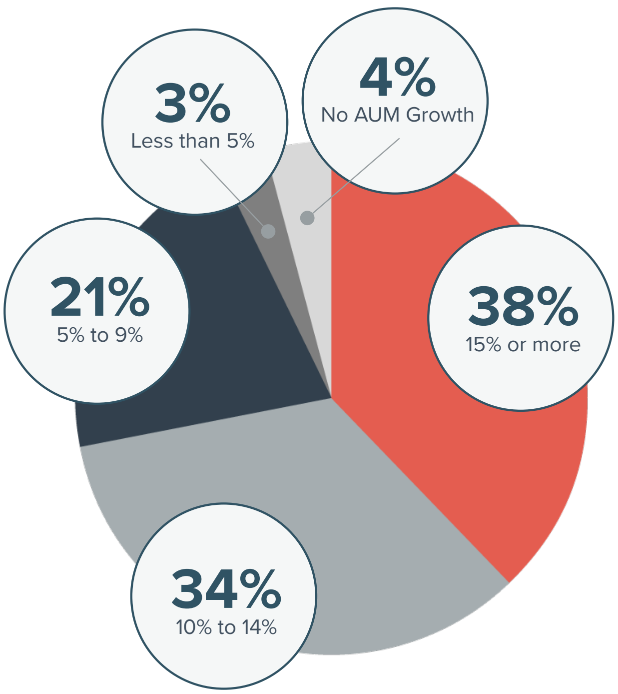


These drivers largely align with the benefits advisors are actually seeing from the strategy. For instance, **more than two-thirds of advisors (69%) report the primary benefit of their decision to outsource has been more time to spend on other services, on client relationships and on business development**. Meanwhile, 88% of advisors who outsource report their decision "definitely" or "probably" contributed to an ability to spend more time client prospecting. Clients also benefit in the performance arena, as more than one-third of advisors (38%) cite better overall investment performance as a primary benefit of outsourcing—the third-most cited benefit.

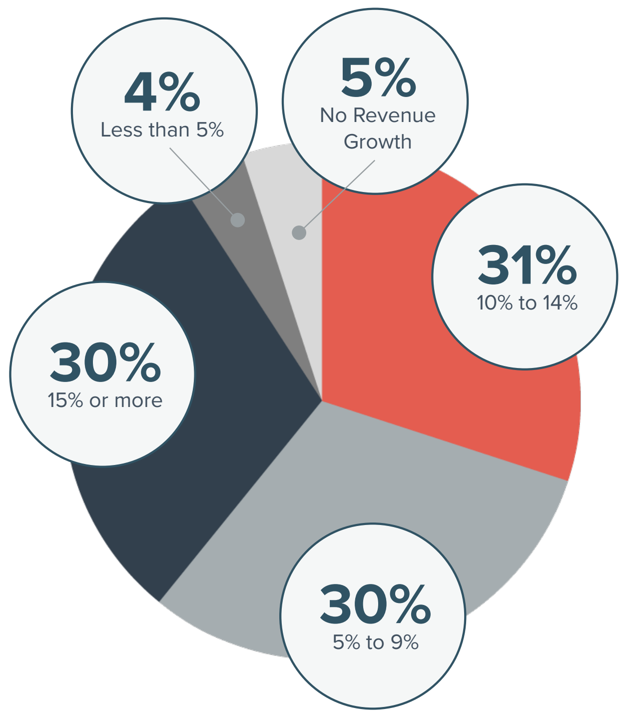
...and offers financial benefits for advisors

Outsourcing gives advisors more time to build stronger relationships with clients, develop new relationships with clients and focus more on growing their business. These qualitative benefits have an impact on real performance metrics for RIA firms. For instance, AUM growth is a primary benefit of outsourcing according to more than half (53%) of advisors engaged in the strategy. In fact, 72% of advisors report annual AUM growth of 10% or more since they decided to outsource investment management, which puts them above the 6% to 9% growth measured by industry benchmarks.[1,2] And 87% of the advisors who report AUM growth point to outsourcing investment management as a direct contributor.

Annual Growth in AUM Since Outsourcing



Annual Growth in Revenue Since Outsourcing



Revenue growth is also high on the list of outsourcing benefits, according to one in three advisors. Of those advisors reporting growth, more than half (61%) report growth of 10% or more, which represents a growth rate 30% higher than the median revenue growth benchmark of 7.3% cited by Schwab's benchmarking study. As with AUM growth, 88% of those advisors who reported growth in revenues say the decision to outsource had an impact on that growth. What's more, freeing up more time to spend on developing client relationships has also paid off in measurable growth in client rosters, with 86% of advisors reporting more than 5% growth in their number of clients since outsourcing, and more than half (51%) reporting growth in excess of 10%—both above Schwab's benchmark of 4.7% growth.[1]

[1] Schwab 2020 RIA Benchmarking Study (9.2% median annual growth in AUM)

[2] Fidelity 2020 RIA Benchmarking Study (6% median organic growth in AUM)

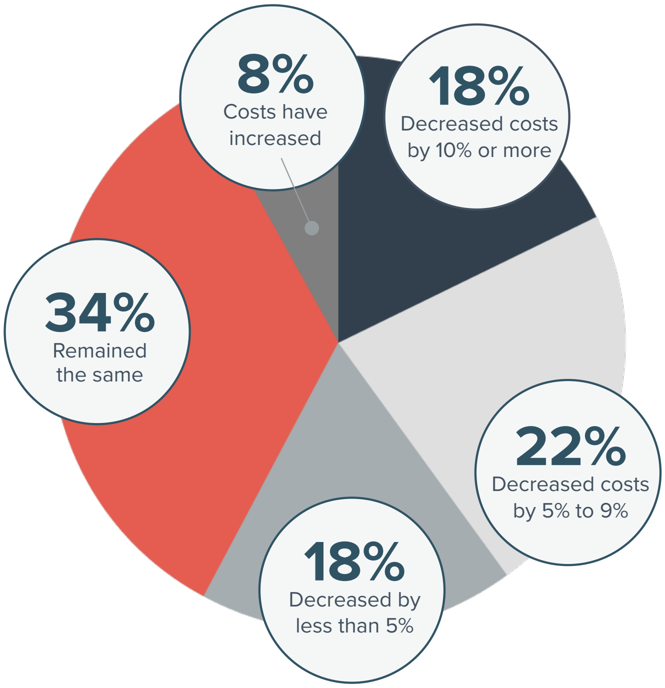
Costs and other barriers to outsourcing

Not all advisors have embraced outsourcing investment management, and costs are viewed as one of the top obstacles. Of those advisors with no current plans to outsource, 43% say costs were a primary deterrent, while more than half of advisors (55%) planning on outsourcing soon cite costs as a primary deterrent (the most frequently cited factor). And yet, for most advisors, outsourcing actually reduces costs.

More than half (58%) of advisors who currently outsource their investment management report their operating costs have declined since they began outsourcing, with 40% seeing declines in costs of 5% or more. By comparison, less than 1 in 10 advisors say their operating costs have increased since outsourcing. Further underscoring the positive relationship between costs and outsourcing, more than a quarter (28%) of advisors cite cost reductions as a primary benefit to outsourcing—on par with higher revenue growth and better performance of investments.

In addition to costs, more than half of advisors not currently outsourcing their investment management cite reduced control and the inability to customize or personalize solutions as top deterrents. As with costs, however, these concerns are most likely based on a misperception of what outsourcing means. There are outsourcing options available that address these concerns.

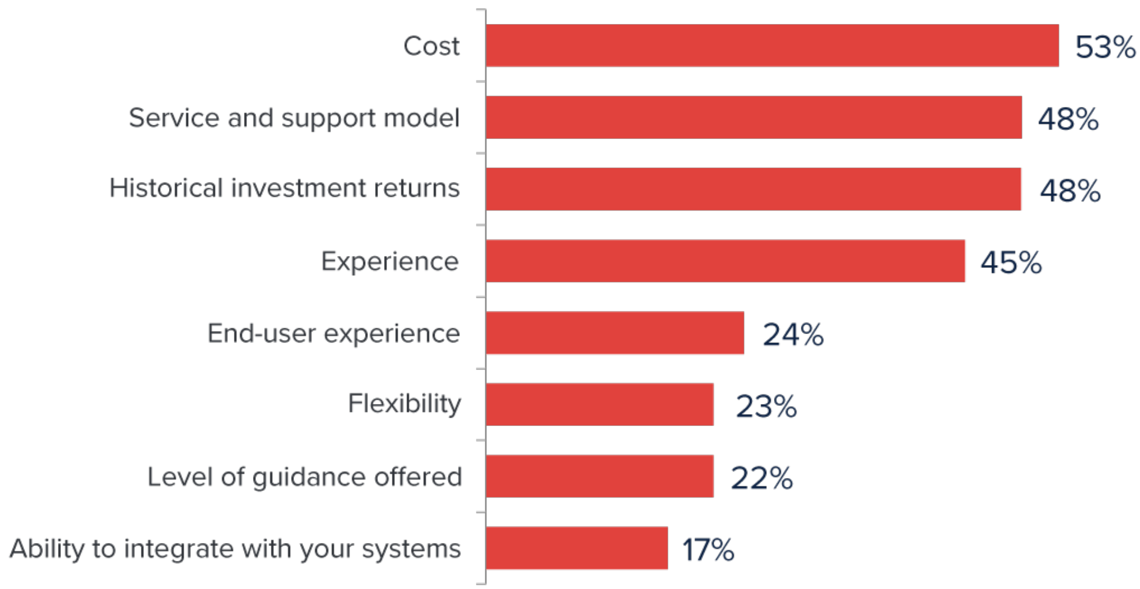
Annual Change in Operating Costs Since Outsourcing



What outsourcing can look like

When selecting a potential outsourcing partner, most advisors (53%) focus on cost as a consideration, while just under half view historical investment returns (48%) and service and support model (48%) as top concerns. Experience also matters: 45% of advisors said experience was a key consideration in choosing a potential outsourcing partner. It is perhaps not surprising that these considerations largely overlap with the deterrents listed in the previous section—particularly costs and the service and support model.

Key Considerations When Choosing an Outsourcing Partner



The most popular outsourcing partners are managed accounts/UMA platforms and TAMPs (Turnkey Asset Management Provider), with 1 in 4 advisors citing these two types of partners. But outsourcing can take many forms, including models that allow advisors to maintain a higher degree of control. **The survey data has shown that most advisors were able to find an outsourcing partner that reduces their costs**. Customization and personalization are just as available, depending on the partner involved.

Some outsourcing models allow advisors to decide what they want to do in terms of their investment objectives and goals, and then build the relationship around those goals rather than limiting advisors to specific investment options. In particular, open architecture models allow for the flexibility that advisors appear to be concerned they will lose if they opt to outsource. There are even outsourcing models that offer advisors access to the full suite of investments they may want—in essence, partnerships that are agnostic to an advisor's investment solutions. In fact, it is possible that with the right outsourcing partner, concerns about all three top deterrents to outsourcing (namely cost, control, and customizability) can be addressed.

Ultimately, outsourcing investment management offers advisors the opportunity to free up their time and energy to focus on areas of their practice where they can add the most value. Based on the responses of advisors in the current survey, that choice has helped generate positive economic impacts for their firm.

Disclosure

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Contact Adhesion Wealth:
(888) 295-8351
www.adhesionwealth.com

5925 Carnegie Blvd,
Suite 500 | Charlotte, NC 28209