How RIAs can stay ahead of the competition: Cerulli

By Editorial Staff *Thu, Mar 3, 2022*

Broker-dealers 'are impinging on what has historically been viewed as largely unique to the RIA channels—an independent, fee-based business centered on financial planning,' a new Cerulli Associates report says.

A confluence of competitive threats is eroding the registered investment adviser (RIA) channels' key differentiating factors, according to the latest report from consulting firm Cerulli Associates: *US RIA Marketplace 2021: Meeting the Demand for Advice*.

The threats to RIAs include an industry-wide shift away from brokerage, broader adoption of financial planning, and the popularity of independent business models. In response, more RIAs are considering whether to extend their service offerings to deepen their impact with existing and prospective clients.

"To unlock the RIA channels' success formula and protect against adviser movement to independence, broker/dealers (B/Ds) are increasingly developing independent affiliation options, promoting financial planning, and creating more opportunities for advisers to conduct fee-based or fee-only business," a Cerull release said.

By 2023, 93% of advisers across all channels expect to generate at least 50% of their revenue from advisory fees. Likewise, over the past five years, the number of financial planning practices across all channels grew at a 5.3% compound annual growth rate (CAGR). As a result, B/Ds are impinging on what has historically been viewed as largely unique to the RIA channels—an independent, fee-based business centered on financial planning.

In addition to this convergence of business models, investor influence, democratization of services, and client acquisition challenges are encouraging RIAs to reevaluate their position in the marketplace. For some, this means expanding their service offerings to combat value differentiation concerns and capture emerging opportunities.

According to the research, trust services (19%), digital advice platforms (17%), and concierge/lifestyle services (16%) rank as the top-three areas of anticipated service expansion for RIAs within the next two years.

"While implementing these additional services may help RIA firms move upmarket and generate greater revenue, RIAs will need to reinvest in the business by hiring more staff, adding technology tools, producing marketing materials, or paying a third-party provider for outsourced support," said Marina Shtyrkov, associate director, in a release. "These expenses typically lower the firm's profit margins, so by expanding their purview, RIAs find themselves at risk of profit margin compression unless they are able to offset expenses with higher fees, new client acquisition, or additional revenue streams."

To preserve profitability levels as they add services, advisers can either adjust their fees upward or implement alternative pricing structures. These nontraditional fees (e.g., fixed financial planning fees, monthly subscription fees) are not correlated to portfolio performance and can help RIAs offset the increased costs of delivering additional services, thereby reducing profit margin pressure.

For RIAs that offer financial planning, nontraditional fees also ensure that the firm's pricing is more closely aligned with its value proposition.

Ultimately, value differentiation challenges will become a question of firm economics—one that RIAs must be ready to answer. While Cerulli does not believe that all RIAs must expand their service set to remain competitive, under the right circumstances, additional offerings can help firms capture new opportunities and tackle competitive challenges.

"Like any business decision, the addition of a service should allow advisers to better address their target market and achieve stronger alignment between that segment's needs and the firm's offerings," wrote Shtyrkov. "RIAs will need to consult their strategic partners (e.g., RIA custodians, asset managers, service providers) to help them navigate these choices, weigh the tradeoffs of service expansion, and mitigate the risks of thinning profit margins."