
WILL COVID-19 CAUSE SMALL, INDEPENDENT ADVISORS TO BECOME EXTINCT?

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This article is relevant to financial professionals who are considering offering model portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios, please inquire with your financial professional. Not all financial professionals have direct access to these Model Portfolios.

“Robo-advisors will make human financial advisors obsolete.”

Remember that narrative years ago?

It was aimed particularly at smaller advisory firms. These advisors were believed to stand no chance against a robot’s ability to scale at razor-thin margins.

Did the pundits get this right?

Over the last decade, the total number of state-registered investment advisor firms (RIAs) with less than \$100 million in regulatory assets under management has not declined in a single year.¹

Furthermore, a recent study conducted by WisdomTree after the March-April pandemic-related market volatility found that 82% of investors prefer to get their financial advice through human interactions.²

Do human advisors get the win? I would say so.

But do not get too comfortable; there is a new narrative gaining momentum...

It goes like this: *COVID-19 will likely cause small, independent advisors to become extinct.*

It’s painful to hear on a personal level. I started my career employed as a research analyst for an RIA. But I must admit that some of the narrative holds merit. Advisors need to rethink aspects of their business to survive in the long run.

What Goes Up Must Come Down?

Many small, independent advisors were already vulnerable before the pandemic. Many advisors were operating expensive business models measured by cost-to-income ratios, which is not sustainable for the long term.

Dorothy Hinchcliff highlights a study conducted by the Boston Consulting Group (BCG) regarding wealth managers today (my accompanying opinions are in bold)³:

- Asset-based fees, which are more vulnerable to market declines, make up a substantially higher percentage of many advisors' incomes than in the past. Prolonged [bear markets](#) will directly cut into a firm's top-line revenues and disproportionately affect high-net-worth individuals, who are popular audiences amongst advisors.
- Nearly double the number of wealth managers were operating in the red in the beginning of 2020 versus those that were in 2007 and many have higher cost-to-income ratios than during the 2008 financial crisis. This is staggering, considering advisors experienced a 10-year [bull market](#) while there were significant advances in financial technology that added gains in productivity and profit margins.
- Regulatory and compliance burdens have ballooned; meanwhile, many advisors "kept adding more people to cope with these burdens instead of finding efficient ways to deal with them." Burdens are likely to increase during a work-from-home operating environment.

BCG adds that "the environment has been way too favorable" for wealth managers over the past decade and many advisors have under-invested in their businesses to ensure relevancy in the future. In fact, BCG predicts that "most services that differentiate wealth managers today will, in the next few years, become commodities."

When a House of Cards Meets a Tornado

So far, COVID-19's impact has been the harshest on small, independent advisors with a concentrated list of clients. These advisors structurally lack the resources and economic foundation of their larger peers that aids a transition into a remote work environment.

This transition has not been easy for many. AdvisorStream recently conducted a study of 1,000 advisors, in which Drew Voros of ETF.com highlights the bigger-picture worries for advisors during this pandemic⁴:

- Nearly 50% of advisors still struggle with digital know-how.
- Almost 75% are frustrated about sales generation and standing out among peers without the benefit of digital tools.
- 48% are concerned about losing clients in 2020.
- Digital solutions are the number one focus for advisors.

I expect digital solutions to remain the primary focus, especially when considering the results of a study conducted by Oranj in which nearly half of the participating advisors said they did not offer a digital client experience⁵.

The question that remains is whether it is too late.

Better Late Than Never

It is not too late.

As I wrote about in a prior post, it is precisely in these times of [crisis that financial advisors earn their stripes](#).

Trusted personal relationships with clients are not going away. Smaller, independent firms can stand out amongst their peers, provided they have the right technology and tools in place. Retaining clients and reaching prospects with a personalized and differentiated message is critical during these times.

Where Do Advisors Go from Here?

There are many ways WisdomTree can potentially help advisors of all sizes:

Optimizing Online Presence. Our online credibility offering, Growth Solutions, provides the tools needed to help an advisor's online presence, engage audiences and build credibility—helping ensure that advisor becomes a prospect's first call.

Engaging Clients with Behavioral Finance. In conjunction with Professor Shlomo Benartzi, PhD, co-founder of the Behavioral Decision-Making Group at UCLA, we can help [a](#)

[advisors apply the latest behavioral economics research](#) to deliver personalized strategies that can help their clients more successfully make important financial decisions.

Leveraging Our Deep Investment Expertise. Through our [Model Portfolio offerings](#) and interconnectivity with more than a dozen platforms, advisors can lean on WisdomTree's deep bench of investment professionals to provide their clients with institutionally managed Model Portfolios in a cost-effective manner. We can be seen as an extension of the advisor's already-thin research capabilities and leveraged to provide tailored solutions to their clients' unique situations and goals.

Entrepreneurs Will Live On

COVID-19 has wreaked havoc across the world. Unfortunately, some portion of advisors, and small, independent advisors specifically, will fall victim to its disruption. But I do not believe the pandemic will crush the entrepreneurial spirit of independent financial advisors—the very foundation many practices are built upon.

As with the threat of robo-advisors, small, independent advisors can beat this narrative too. Many will just need to rethink their business model if they want to survive long-term, and the first step is to consider the resources at hand.

¹King, GJ. "Are Smaller RIA Firms Facing Extinction? Maybe Not." Financial Planning, Financial Planning, 23 Jan. 2019, www.financial-planning.com/opinion/two-thirds-of-rias-registered-with-the-sec-have-less-than-1-million-in-aum.

²2020 WisdomTree Model Portfolio Study

³Hinchcliff, Dorothy. "BCG: Small Advisors Face Big Challenges." Advisorperspectives.com, 24 June 2020. Quoting: Boston Consulting Group's Global Wealth 2020 Report. www.advisorperspectives.com/articles/2020/06/24/bcg-small-advisors-face-big-challenges?bt_ee=VGJs0EFtcYbbt2/JEBfKCCIEYU9wKATSWUFY6N/UPSw0FBz1Aoh9Jt5Qxf2nZV25

⁴Voros, Drew. The Slings & Arrows Facing Advisors, 1 Sept. 2020, Quoting: AdvisorStream Survey. <https://www.etf.com/publications/etfr/slings-arrows-facing-advisors>

⁵An Advisors Guide to Understanding Investors' Digital DNA, Oranj and InvestmentNews, 2017

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Bear market: A sustained downturn in market prices, increasing the chances of negative portfolio returns.

Bullish: a position that benefits when asset prices rise.