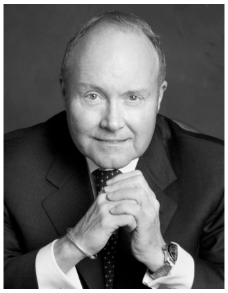

A New Kind of Relationship with Clients: Perspectives on the U.S. Wealth Management World

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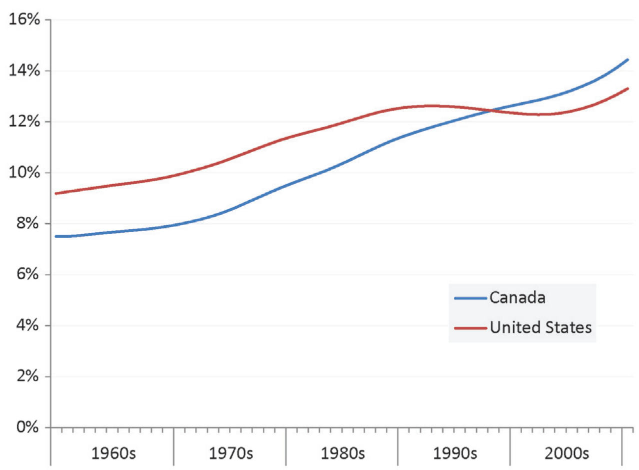
In the past five years the U.S. wealth management business has made great strides in improving its effectiveness in meeting client financial needs. There have been three principal catalysts driving change: an aging demographic that has pressed for new products and services to meet retirement goals and the inter-generational transfer of assets; increased client sophistication creating demand for better service; and shaken trust and confidence triggered by the 2008 financial crisis, prompting pressures for a new approach to doing business.

Aging Demographic
Percent of population aged 65 and above



Source: World Bank

These changes can be grouped into two broad categories – emphasis on creating a new kind of dialogue with clients, and new strategic approaches to carrying out business with clients. The new approach to dialogue increasingly involves a focus on more frequent and deeper conversations with clients. More than ever before, Investment Advisors (Financial Advisors in the United States) listen carefully to the objectives and goals of their clients, and to their investment perspectives. A conscious effort is made to keep jargon out of the conversation, and speak in terms the client can understand. As an example, the advisor assesses the client's portfolio performance, not against financial benchmarks, but against the client's specific goals. Specifically, does recent portfolio performance move the client closer or further away from his or her objectives, such as attaining adequate savings for retirement, or funding the education of children or grandchildren?

Needed: Across-the-Board Financial Experts

The effective Investment Advisor is no longer viewed as simply an expert providing expertise on investment decisions. The advisor is now considered an expert across all aspects of financial decision-making, offering a wide suite of financial products and services related to tax, estate planning, insurance, and retirement and education savings objectives. The advisor becomes the "go to" professional. And if the advisor doesn't have the technical expertise in a particular area, he or she knows where to find it, and then integrate the information in a financial plan.

Leveraging Technology

Advisors increasingly take advantage of advances in technology to facilitate a dynamic and interactive dialogue with the client. For example, interactive technology now enables the client to "visualize" a financial plan, monitoring progress towards defined goals.

Financial planning technology can simulate shocks to the client portfolio that are helpful in identifying client risk tolerance. For example, simulating market losses on the client portfolio for different allocations of equity securities, for a pre-determined market decline, can identify how much the client is prepared to lose, an effective way of measuring risk tolerance. These programs can simulate cuts to social security payments, and the portfolio savings that will be needed to compensate. All of this information is integrated into the financial plan of the client.

Technology has transformed the financial planning exercise. At one time it was an obligatory formal procedure, yielding little client benefit. The plan was completed, paid for, put on a shelf and often ignored. New planning technology, adapted by many

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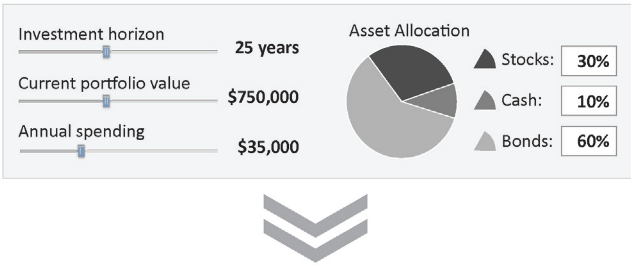
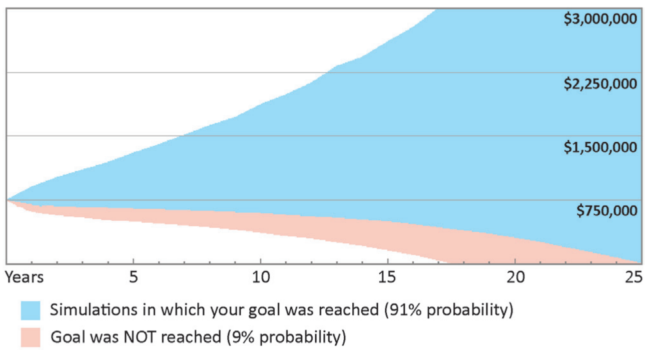
firms in the industry, has brought the plan to life, and made it a dynamic and evolving planning tool, rather than a static, point-in-time document. This allows the plan to become the epicenter of investor decision-making, and facilitates ongoing client-advisor dialogue to monitor portfolio performance against goals.

Scenario Analysis

- Specify investment goals and asset allocation



- Range of projected portfolio balances



Source: Vanguard

This interactive client-advisor dialogue, together with a broadening suite of offered financial services, allows the advisor to build a deeper relationship with the client, strengthening trust and confidence, and encouraging client referrals.

Firms are cautiously embracing social media tools to improve communication with clients, and to prospect for new clients. The industry has adopted a two-pronged approach. Many firms have aggressively adopted LinkedIn and Facebook for corporate marketing. However, concerns about monitoring advisor communication for compliance purposes have made some firms cautious in permitting advisors to use these social networks. Some firms have initiated "pilot projects" with advisors to determine the effectiveness of social media in building the client book. Anecdotal evidence suggests that LinkedIn and Facebook can markedly extend the reach of the advisor to a wide range of prospective clients.

Training and Retention: More Important Than Ever

Firms have invested considerable money and other resources into their business. That includes extensive training programs and continuing education of advisors, providing a full range of products and financial expertise to meet the broadening client needs for financial services, and implementing sophisticated and complex technology, both to facilitate client interface and improve back-office efficiencies.

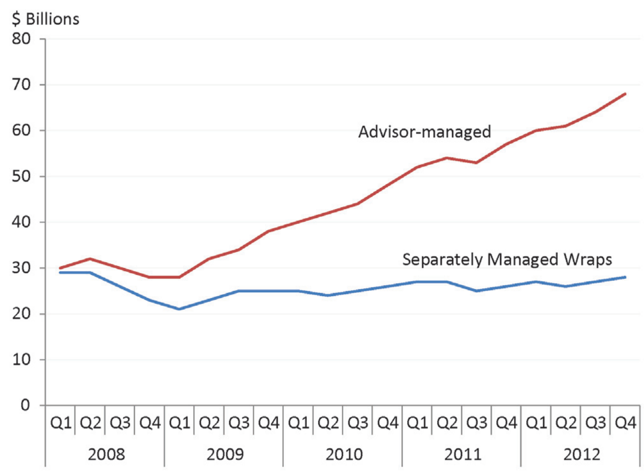
One of the greatest challenges faced by the securities industry is the retention of the experienced advisor and the client book. The evidence suggests good advisors are approached by competitors almost on a weekly basis. The massive restructuring of the wealth management business and resulting migration of many advisors has made advisors more responsive to overtures from competing firms. Over the past decade there has been a significant migration of advisors from the large wire-houses to the smaller broker-dealers and RIA firms, a trend that accelerated in the aftermath of the 2008 financial crisis.

With competition for qualified experienced advisors intense, an important element in the optimal retention strategy, aside from providing the requisite products and services and technology, is effective communication on firm strategy and direction between senior management and the advisor. Firms have also put considerable thought into succession planning. Firms recognize that the likelihood of success for a newly-trained advisor building a book from scratch are slim, given the sophistication of the business and restrictions from the "Do Not Call" lists. Few new advisors can meet the required minimum client asset thresholds to compensate for allocated fixed and variable costs. The majority of new advisors, after completing an extensive training program, are typically inserted into teams. Firms have developed different types of succession plans to transfer client assets to a new advisor as a retiring colleague scales back business involvement.

A Challenge: Responding to Client Demand for Discretionary Management

One of the notable developments in the U.S. wealth management business has been the qualification of advisors as portfolio managers. These discretionary accounts have become popular because of the higher fees on separately managed wrap accounts and the close relationship between the advisor and the client. A similar development has occurred in Canada, with advisor-managed accounts doubling in size in four years and accounting for nearly two-thirds of discretionary managed assets.

Growth in Advisor-managed Discretionary Assets
Canada



Source: Investor Economics

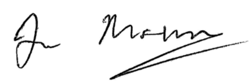
The phenomenon has brought its share of challenges to the firms. First, the focus on discretionary management comes at the expense of the advisor having less time to offer the increasingly demanded more holistic approach to financial services that builds a deeper relationship with the client.

Second, discretionary management at the advisor level raises potential risks of client portfolio losses, as well as the ability to provide a consistent standard of discretionary management to all clients across the firm. In response to these concerns, firms have set high proficiency standards, above the statutory requirements for advisors, in offering discretionary management services. They have restricted allowable investments (notably prohibiting derivatives, and illiquid assets like private placements), and introduced continual monitoring of portfolio performance. The practice of permitting advisors to manage money on a discretionary basis is still permitted at most firms, but in all cases is subject to tight controls and oversight. However, there is a consensus around the view that the practice will be limited as the more successful advisors will be those who provide a holistic approach to serving the financial needs of their clients.

Conclusion: A Big Step to Rebuilding Client Confidence

The investments made in restructuring the wealth management business in the United States, at both large and small broker-dealers, has been extensive. The focus has been on training and continuing education of advisors, new management practices, and new products and services. Firms have also taken advantage of advances in technology that have facilitated the delivery of financial advice and products. These structural changes have probably done more to rebuild investor trust and confidence, and engage investors in the market than the ongoing efforts at regulatory reform. Firms have been well positioned to help their clients benefit from the recent turnaround in U.S. equity markets.

Yours sincerely,



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