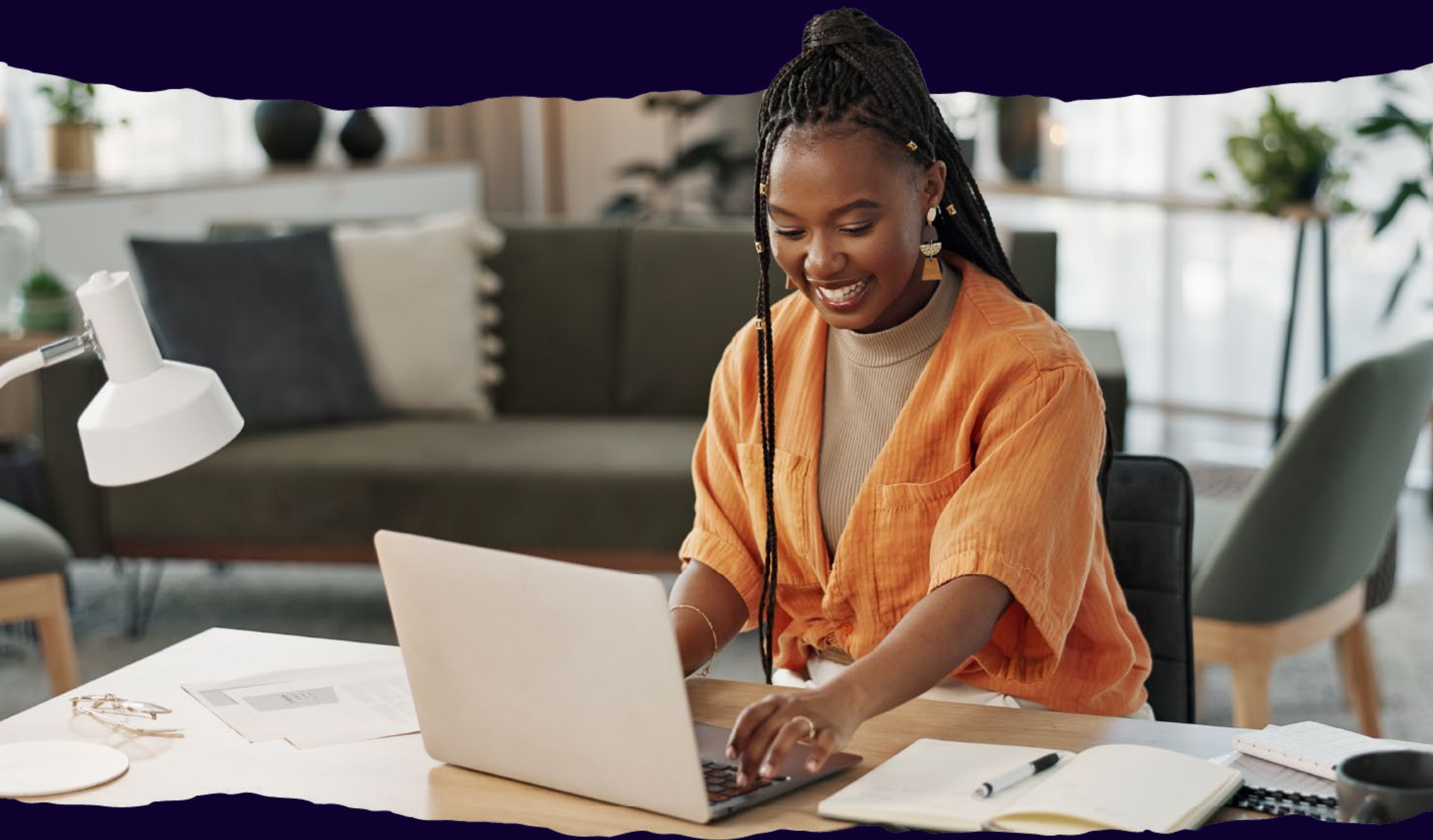
WHITE PAPER

Unlock your firm's potential

Two simple changes that could add millions to the value of your business



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octopusmoney.com

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Are there hidden costs lurking in your client book?

Take a look at the table below.

Assets under advice	Number of clients	% of clients	Assets under advice (£)	Ongoing advice fee
0-50k	173	29.42%	£3,784,084	£70,710
50-100k	117	19.90%	£8,658,709	£108,014
100-250k	152	25.85%	£24,361,186	£261,381
250-500k	76	12.93%	£26,037,249	£239,453
500k-1m	56	9.52%	£36,718,355	£326,325
1m+	14	2.38%	£35,566,180	£238,187
Total	**588**	**100%**	**£135,125,763**	**£1,244,070**

This anonymised data was shared with us by Catalyst Partners, M&A experts in the financial services arena. The table above reflects a real firm they are advising. The firm's owners are looking to sell and want to get the best deal they can. There is, however, a bit of an issue. Can you spot it?

A revealing tale

Every set of numbers like this tells a story. Two of the key strands are:

- Around half of its clients (those with assets up to £100,000) account for only 14% of ongoing advice fees.
- That same cohort accounts for just 9% of assets under advice.

On top of that, another quarter of the firm's clients (the £100k-£250k bracket) account for 21% of ongoing advice fees and 18% of assets under advice.

To put it another way, just under 25% of this firm's clients represent over 70% of assets under advice and more than 60% of ongoing advice fees.

It turns out this is a challenge many firms face when it comes time to consider selling. What story does your data tell?

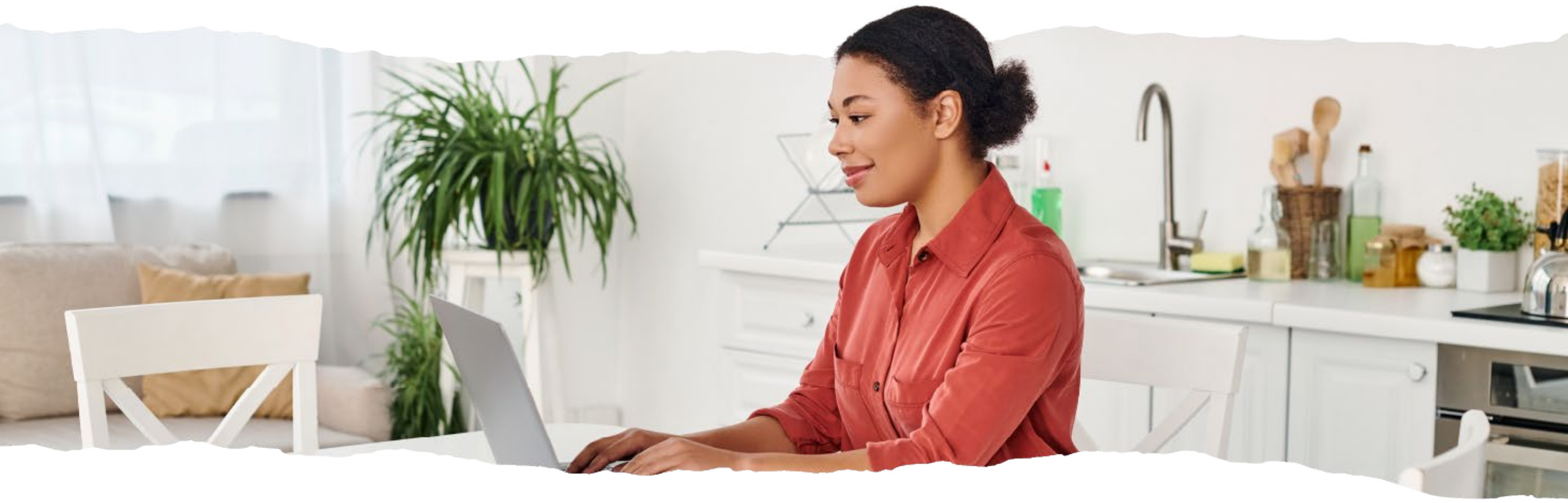
The hidden cost lurking in this client book

Of the firm's 588 clients, 442 have assets below £250,000. The time spent servicing those clients could represent a significant opportunity cost. The numbers suggest this firm is set up to serve those clients with more complex needs, who tend to be those in the higher assets-under-advice brackets. Adviser resources are finite, and it may make more sense to use those scarce resources where they deliver the most value..

These points matter to potential buyers too. As we discuss in Part 2, a tail of lower-asset clients can make a substantial difference to the earnings multiple an acquirer is willing to pay.

There's a potential hidden cost for clients here too. The advice fee generated by clients with lower asset values may not cover the cost to deliver advice. With heightened regulatory obligations to evidence ongoing advice, in some cases a firm might decide to turn off ongoing advice fees for such clients, putting them at risk of falling into the advice gap.

There are two changes the firm could look at making. One is to find a different way to service these clients. Another is to find them a new home specifically set up for this type of client. We'll return to this topic in Part 3.



ACTION POINT

What do the numbers look like for your firm?

1. Start by mapping out what proportions of your firm's revenue comes from which cohorts of clients.

2. Then understand your cost to serve. How much does it really cost to deliver initial and ongoing advice, including all of the general reassurance around political and economic factors and servicing?

This exercise can help identify the types of client you want to focus on. It can also be a catalyst for finding a better solution for those who don't fit that target client profile.

02

How your client book affects the sale of your business

While advisers are amazing at helping clients plan, it can be hard to dedicate the time to do the same for your own business. If you expect to sell your business at some point in the future, it pays to start thinking about it sooner rather than later. Ideally, you shouldn't wait any later than five years before you plan to exit. That gives you time to identify changes you should make to maximise the value of the sale and implement them.

Even if you have no immediate plans to cash out, it's still worth taking the time to look at your business the way an acquirer would. You will probably find a number of areas where you can tighten up, leaving you with a more efficient, more profitable operation.

In this chapter we'll look at the landscape of acquirers, what they tend to look for, and what actions you can take to make a deal as attractive as possible.

Why private equity likes the UK financial advice market

Most acquirers active in the market over the past few years have been backed by private equity. PE-backed acquirers typically follow similar strategies: they buy a 'hub' business in a major town or city and then grow by adding smaller 'spoke' businesses. The aim has been to buy firms at a low multiple of earnings (between around 8 and 10) and sell at higher multiples (between around 16 and 20).

Some PE firms have had success doing this, which is why others are keen to get into the market. Some of the reasons PE firms like the UK financial advice market are:

- It's a fragmented market with lots of room for consolidation
- The market has shown steady growth
- Income streams are regular
- The UK has an ageing population, which supports the need for retirement planning
- The regulator is very receptive to consolidation

As well as PE-backed acquirers, there are also larger regional advice firms looking to add client books of smaller firms. Asset managers are also looking at ways they can get into the advice market by acquiring firms.

What acquirers tend to look for

Broadly speaking, acquirers want to buy a clean, well-run business with scale. They also want to reduce risk as much as they can, with a low number of complaints, and will review your back book for things like defined benefit transfers. In a perfect world you won't have any, but most acquirers are okay with a small percentage of your book being DB transfers.

Most acquirers also prefer firms to have employed advisers, to protect the retention of clients and their advice fees. They want to see a robust operating model that makes good use of your back office system, with clean and accurate data.

Geography can also be decisive if an acquirer really wants to build up their footprint in a particular region.

Other factors that can make a big difference

Of course, some of these factors will be out of your hands. But there is still a lot you can do to make your firm more attractive to a potential buyer.

That's because what matters most is the overall picture. So even if one aspect of the business is not ideal in a potential acquirer's eyes, others may more than offset it.

A big consideration for all acquirers is your clients' average holding. "If this is above £250,000 per client then you put yourself in a much better position," says John Chapman of Catalyst Partners.

How Consumer Duty has changed the landscape

The Consumer Duty was first introduced by the FCA in July 2023, to promote higher standards of consumer protection. Initially it slowed down M&A activity in the financial advice market. Acquirers turned their focus to integrating firms they had already bought to achieve a common proposition across all their businesses. But since most buyers are backed by PE investors looking for growth, they're motivated to stay active in the market.

The Consumer Duty has also encouraged advice firms to look at the cost of serving clients, including how much it costs to do an annual review, the paraplanning, and the administration, as well as the margin they need to build on this base cost. Firms that work through this exercise get a better idea of the type of client they need to target to run a profitable business that will attract potential buyers.

Our research[1] finds that the overwhelming majority (98%) of advisers say the Consumer Duty has made serving smaller clients harder. Over a third (35%) of advisers told us that additional reporting requirements have increased the administrative time spent per client. As a result, advisers indicated to us that the time required to deliver a single case has more than doubled.

Our findings also lay bare the issue of servicing clients with lower asset values, with 74% saying it is increasingly challenging. The solution for both parties is to find a better way to service these clients or a better home for them.

The ability to evidence the delivery of the ongoing advice service you charge for is a critical new requirement of acquirer's due diligence.

[1] Octopus Money Consumer Duty Advice Gap Research July 2024

ACTION POINT

Study your business the way an acquirer would

Looking at your firm through an acquirer's eyes could be the most valuable business development exercise you do this year. Some useful questions to ask include:

- Is it a clean, easy-to-understand business when viewed from the outside? What can you change to make it so?
- Do you accurately know your cost to serve?
- Can you evidence the delivery of your obligations under Consumer Duty? Can you do this for every client?
- Is your average client holding attractive to potential buyers?
- Do you have a clear target client?
- Do you have a strategy for serving clients who don't fit your target profile, especially where you want to maintain goodwill?
- Is your data management as good as it could be?

A couple of companies that can help you answer these questions are:

Catalyst Partners can work with you to identify and address areas of your business that will increase its embedded value. They can also help you decide if an offer to buy your business is the right one to take. John Chapman at Catalyst explains "We work hand in hand with financial services business owners to understand their ideal exit, and ensure the best cultural and commercial outcome through our 35 years experience understanding the acquirer landscape." You can find out more at thecatalysts.uk

Woven Advice specialises in taking your data and putting it into easy-to-understand dashboards so you can see exactly what's going on in your business. This helps you to ensure client outcomes are being met and to evidence that process. Nicky Sevel, Director at Woven Advice says, "We are passionate about data, and the story it tells. By segmenting clients and assets using their integrated back-office data, firms are able to paint a picture of the risks and opportunities in their business. By using a firms real time client data it's easy to see the commercial challenge that clients with lower levels of assets present to advice firms, with many not realising the extent of the loss they are making." You can find out more at wovenadvice.com

These firms often partner with other experts who can meet your needs, so please do reach out.

03

How to add more value for smaller clients

(And what to do if you can't)

Finding the right solution for smaller clients can not only make a material difference to the multiple you'll be offered when it comes to selling an advice firm. You may also have an opportunity to make more revenue by redirecting your time to your target clients. Addressing this issue could unlock millions of pounds for firms like the one we looked at in Part 1.

The alternative is a lose-lose situation: advisers spend time and resources that could be better used on clients with complex needs, while smaller clients end up in an advice model that doesn't fit their situation.

The best of humanity, the best of technology

At Octopus Money we have solved this conundrum by reimagining the regulated advice model. We combine automated advice technology with financial coaches. By doing so we provide a service for those clients who have simpler needs at a lower cost than traditional advice models, which tend to be geared towards clients with more assets and more complex needs.

This is not the kind of robo advice that leaves clients to do all their own financial planning without any guidance. Our accredited financial coaches work with clients to understand their goals, build their cashflow model, and create a financial plan. The regulated advice is then supported by our technology platform based on that financial plan.

Who we work with

The firms we work with cover a variety of different advice models.

We work with advice firms who want to de-risk their business and focus on clients with more complex needs. We can help them do this by acquiring the book of clients that would benefit from our coaching and digital advice model. We pay a multiple of the ongoing advice fee, and migrate clients into a holistic advice model with a TER of c. 1.15%.

We are also a home for advice enquiries, where the clients are outside their target market. These referrals might come from existing client banks, or they could be prospective clients for whom our proposition is a better fit. It's a way for advisers to help those clients they can't take on themselves by signposting them to us.

You can find out more about how referrals work and how much we pay for them here.

We also work with some firms to create a business where growth is not constrained by adviser capacity, every client has their cashflow model refreshed every year, and they never have to turn a customer away. By embedding our methodology into their business we can reduce their cost to serve. By using a combination of coaching and technology, they can create an 'incubator' for future clients, such as those who expect to inherit wealth in future.

Whether using our technology within their business or referring clients to us, the big advantage for firms is we help them free up time to focus on their target clients who have more complex needs. This is where their advisers can add the most value, which also helps firms address Consumer Duty risk.

What our clients say

Our accredited financial coaches do the job because they enjoy working with and helping people. And this shines through in the feedback we get from our customers because we're set up for exactly this type of client.

Our customers like the fact that they can talk to their coach on a video call, meaning they can fit it into their schedule without having to go to their office or stay in for their adviser to visit them at home. Many have not done cash flow modelling before and find it eye opening, and really brings to life the steps they can take to deliver the financial future they want. We also have coaches from a wide variety of backgrounds, making it easier to match a customer with someone they really connect with. We believe this service will help open up a new demographic of investors.

ACTION POINT

Develop a strategy for clients who fall outside your target market

One of the reasons firms end up with a lot of clients who don't fit their target profile is because they don't realise the implications of not taking action. We understand that desire to help. It's hard to say 'No' if, say, an existing client refers a friend, or if your current model makes it challenging to serve those who historically you were able to serve.

But as we've discussed in this chapter, there is a way to achieve a better outcome both for your firm and for those smaller clients.

04

What to do next

In this report we've looked at two simple changes advice firms can make to ensure a better-fit service for lower-asset-value clients. One is to sell that part of the client book to a firm like Octopus Money that specialises in serving those clients, and refer on would-be new clients who also fit this profile. For some firms there may also be the option to reduce their own cost to serve by embedding our technology in their business.

If you're expecting to sell your business at some point in the future, it's worth having a chat with Catalyst Partners. You'll find them at thecatalysts.uk

Woven Advice can help you to make the most of your firm's data, highlighting risks and opportunities. For example, it can identify which clients it may actually be costing the firm to serve each year. You can find out more at wovenadvice.com

If you want to free up your firm's time to focus on those clients with more complex needs, get in touch with us at Octopus Money. We'd love to have a chat about how we can help you find a better way to serve your smaller clients:

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Notes to editors:

About the research
The research was conducted by Censuswide, among a sample of 203 Financial Advisors (aged 18+). The data was collected between 04.07.2024 - 11.07.2024. Censuswide abides by and employs members of the Market Research Society and follows the MRS code of conduct and ESOMAR principles. Censuswide is also a member of the British Polling Council.

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