Why the future of advice starts with educating kids

Proper financial education at an early age will not only instill a need to seek advice when it comes to financial affairs. It will also positively influence financial advisers to embrace training in pursuit of higher professional standards, says Paul Smith of CFA Institute.

PAUL SMITH, CFA
CFA Institute

The investment and wealth management industries continue to find themselves in a Catch 22: most end-customers are not aware of – or might not even think about – the need for financial advice, in turn forcing wealth managers to push product.

And an immediate – and damaging – upshot is the seemingly insurmountable hurdle in convincing most practitioners to pursue higher professional standards and more ethical practices.

Yet the business model should, in reality, be far from one where products get 'sold'. Instead, it is the services which should be 'bought'. "The industry continues to be sold to people rather than them going looking for what may or may not be appropriate," explains Paul Smith, president and chief executive officer of CFA Institute.

The impact of such a conflict of interest is further exacerbated as a result of fees being embedded in products, rather than the service.

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This further fuels the perception among many would-be consumers of financial advice and products to steer clear of wealth managers to address financial concerns or needs. Indeed, a trust-related study from CFA Institute, released in February 2016, highlighted that pro-

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fessional investors expect higher levels of transparency than ever before, including regular and clear communications about fees and upfront conversations about conflicts of interest. They hold their investment managers to the highest ethical standards, plus are laser-focused on returns.

"The bar for investment management professionals has never been higher," explains Smith.

"Retail and institutional investors, as always, crave strong performance, however both groups also demand enhanced communication and guidance from their money managers. Building trust requires truly demonstrating your commitment to clients' well-being, not empty performance promises or tick-the-box compliance exercises," he adds.

"Effectively doing so will help advance the investment management profession at a time when the public questions its worth and relevance."

READY-MADE REMEDY

Some of the results of the study by CFA Institute are reflected in other surveys.

In the 2016 Edelman Trust Barometer, for example, financial services ranked 8th in terms of the trust that the public places in it as an industry sector. At 51%, this lags the leader, technology, at 74%, as well as others including telecoms, energy, and pharmaceuticals.

"Other professions have an inbuilt advantage," says Smith. "They are the sort of people you know from an early age in your life. For instance, if you are sick, you know you need to go to a doctor."

By contrast, he adds, few people ever get told they need a financial adviser until they are well into their 20s. This builds an apathy and lack of interest when it comes to the services on offer.

It also highlights the urgent need for proper financial education to be given at as young an age as possible.

This would also help to overcome the never-ending debate over whether the advisory industry's problem stems from the lack of public awareness or a lack of training and professionalism.

"The answer has to be more fundamental financial literacy, meaning starting this education sooner," says Smith.

"We have to teach people at an earlier age that seeking financial help is something they are going to require, and the individuals within the industry need to be readily identifiable as professionals from which the public can get that advice as they go through their lives."

CHANGING THE INPUTS

Yet while the end-customers have responsibility for changing the rules of the game by being better informed, financial services institutions must do a lot more to drive better practices.

Inevitably, training has a big role to play. And CFA Institute has seen signs of more appetite too.

Its December 2015 exam, for example, saw a record number of candidates (52,315) tested for Level I, an increase of 11% from the previous year. There was a 43% pass rate.

And in June and December 2015 combined, the highest total number of more than 103,000 candidates sat for Level I, representing nearly a 10% increase on 2014.

In pursuit of transparency, ethics, performance

Key findings from the CFA Institute study on trust include:

- *Since 2013, retail investors show a significant increase in trust of the financial services industry – rising from 50% to 61%. About half the gain is thanks to strong increases in the US, UK and Australia. The other half is due to higher absolute trust levels in markets not included in the 2013 study, notably China, India and Singapore.*
- *Both retail and institutional investors share the view that financial professionals are falling short on issues of fees, transparency and performance.*
- *More than half (53%) of retail investors cited "underperformance" as the biggest factor that would lead them to switch firms. This was followed by "increases in fees", "data/ confidentiality breach", and "lack of communication/ responsiveness".*
- *Forty-three percent of retail investors would leave an investment firm if data security were to be compromised.*
- *The study found that once an issue has triggered an investor to re-evaluate their relationship with an investment manager, the majority (76%) of retail investors are likely to leave within six months.*

Pinpointing CFA Institute priorities

After just over 12 months in his global role at CFA Institute, Smith says the priority remains to maintain the relevance of the curriculum.

Practically, this involves making sure newer topics get covered, such as ESG (environmental, social and governance), Islamic finance, and private wealth management.

The latter is a segment in which Smith sees significant growth potential – evidenced by the fact that 30% of the membership now in the US is on the private wealth management side.

"The world's middle class is getting bigger and bigger, as are the assets they control, so there is going to be a greater need for people to help others understand what to do with their wealth."

Another key goal for CFA Institute in general, Smith adds, is to try to improve the overall health of the industry, via thought-leadership and advocacy, as well as making members as good as they can be.

"The prime way we can influence the market is by having more CFAs who are better at their jobs on a day-to-day basis," he explains.

Also increasingly important to creating the right culture and mind-set towards higher professional standards is the ability to ensure more diversity in the investment and wealth management industries – by gender, by ethnicity and by background.

"If we want to change the outputs, we must first change the inputs," says Smith. "This is vital if we are to improve the quality of the decision-making."

Some of these issues are especially acute within the banking segment targeting the mass affluent.

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THE ALL-ROUND CHALLENGE

The organisation which Smith presides over is one which has such a vision to promote professionalism and ethics in investment management, for instance, to be able to drive a positive influence in the market.

"If we can spread the CFA story and impact enough investment communities around the world, then we will produce some positive returns because we are trying to produce investment professionals who put their clients' interest first and behave in a professional manner," he explains.

The more of these types of individuals who are around, and the more important they become, the more this all builds to create a healthier industry, adds Smith.

An important aspect to this, however, is the relevance of what people learn and how they portray it to their clients.

This exposes a shortfall in the majority of industry training – too much of a focus on technical knowledge and less on the softer side that facilitates the conversation with the client.

It is these types of human skills, or the 'bedside manner', in the case of a doctor, that differentiates practitioners working in medicine, for example. But they are found wanting among many financial professionals today.

Smith says this is largely due to the fact that it is possible to test an individual's technical knowledge, but difficult to do so with bedside manner.

"This is the challenge of the whole industry, though, which can leave clients feeling cold." ■