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The Guidance Gap

An investigation of the UK's post-RDR savings and investment landscape

Fidelity Worldwide Investment report in association with Cass Business School

Professor Andrew Clare
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Executive summary

Arguably sound finances are as important to our well-being as sound health. In 2006 the Financial Services Authority (FSA) launched the Retail Distribution Review (RDR) to reconsider the way in which financial advice is provided to retail investors and savers. One of the main goals of this review was to identify ways of improving the quality of this advice which, if successful, would in turn help to improve the quality of our personal finances.

An important conclusion of the RDR was that professional independent advisers should no longer be paid for their advice by product providers via commission arrangements. Instead they would need to charge their clients an explicit fee for their advice. The FSA's intention in moving independent financial advice away from the commission-based model was to make clear not only the cost of financial advice but also its value. This new, fee-based framework for the provision of financial advice began on 1st January 2013.

The move to a fee-based remuneration model raises an important question: will UK retail savers and investors be willing to pay a fee for financial advice?

Based on a survey[1] of 2,060 people, representative of the UK's adult population, our survey indicates that only just over 7 million[2] people are 'likely' to be willing to pay a fee for financial advice. Although of course, many people did not make use of financial advice prior to the RDR changes, we nonetheless find that **26.5 million[3] people across the country, say that they are 'unlikely' to pay for financial advice**.

Given that there is likely to be a large number of people that will not be serviced by professional financial advisers in the RDR world, we explored the possible role that **'financial guidance'** could play. By guidance we mean **a resource that would provide people with all of the information they would need to make investment and savings decisions on their own**. Such guidance could be provided by, for example, large employers for their employees, by the finance industry, by independent web-based companies, or indeed by financial advisers.

In the course of this research we have identified a financial 'guidance gap'. This gap comprises those people that will be without professional financial advice in the RDR world and that will not have the confidence to make their own decisions in the absence of professional advice but who, nevertheless, will be in need of financial guidance in order to maintain the health of their personal finances.

In aggregate we estimate that the total investible wealth of the 43 million[4] of the UK's adult population that will fall into the guidance gap is approximately £440 billion. We also estimate that people in the guidance gap currently save a total of £54 billion every year.

Of course the RDR revolution has only just begun and the full impact of the changes that took place at the start of this year have yet to be felt. We believe that it is very possible that more people could fall into the **guidance gap** over time. This is because up to a half of those people that say that they would be likely to pay for financial advice in the future will probably either be unwilling to pay the likely fees that an financial adviser will need to charge or will not have sufficient assets to make them attractive to professional financial advisers.

Furthermore, a number of senior industry figures believe that the requirements of RDR, with regard to adviser qualifications, and the end of the commission-based remuneration arrangements, may lead to a substantial fall in IFA numbers, which may in turn make it harder for people to find a financial adviser.

The FSA's goal may have been to improve the average quality of financial advice, and the RDR may well achieve this aim, but at the same time it seems likely to us that both the demand for and the supply of financial advice are likely to shrink as a consequence of this new regulatory regime. Without a commensurate increase in the supply of high-quality guidance, the quality of personal finances in the UK is unlikely to improve.

About Cass Consulting

Cass Consulting is a research-led consultancy service provided by Cass Business School in the fields of finance, insurance, actuarial science and business.

Cass Consultant

Andrew Clare
Professor of Asset Management, Cass Business School
Professor Clare was formerly a Senior Research Manager in the Monetary Analysis wing of the Bank of England, which supported the Monetary Policy Committee. He has published many papers in academic and practitioner journals, and a 2007 survey ranked him the world's ninth most prolific finance author of the past 50 years. He serves on the investment committee of the £4 billion GEC Marconi pension plan, and is a trustee and Chairman of the Investment Committee of the £2 billion Magnox Electric Group Pension scheme.

1 This survey formed part of YouGov's Omnibus survey. The fieldwork for this survey was undertaken between 11th and 13th December 2012. The survey was carried out online. The figures from the omnibus survey have been weighted and are representative of all UK adults (aged 18+).
2 14% of the survey are likely to pay for financial advice – 14% x 49.97 million is 7 million.
3 53% of the survey did not make use of financial advice – 53% x 49.97 million is 26.5 million.
4 See Appendix 1.

Key findings

1. 43 million people fall into a guidance gap as they are unwilling or unable to access financial advice.

2. Just 14% or 7 million UK adults say they are likely to pay a fee for advice.

3. People demonstrate a strong appetite for alternatives with 50% saying they would use a guidance service instead of advice.

4. Our survey suggests that the average level of investible assets needed to make a consumer commercially viable to an adviser is approximately £61,000. We find that around 75% of the UK's adult population did not have current investible assets above this level, while a further 19% preferred not to reveal the size of these assets.

5. The investors who said they would not pay a fee for financial advice in the future have average investible savings of £43,000.

6. Only 31% of advisers expected to keep most of their clients, meaning of course that 69% expect not to retain at least some. 39% of advisers indicated that they would keep in infrequent contact with these clients.

7. Half of investors and 37% of non-investors would be likely to use a guidance service that was available in an easy to use and jargon-free website.

8. Only 21% of investors believe they have a good understanding of investment and savings products.

9. 41% said they could not afford to invest in the stock market or equities. Nearly a third (30%) told us they don't know where to start, while 20% are not confident making their own investment decisions.

10. All these factors create a guidance gap comprised of those people who will be without professional financial advice in the post-RDR world but who will not have the confidence to make their own decisions.

Background

The Retail Distribution Review (RDR) was established by the Financial Services Authority (FSA) in 2006 to review how financial advice is provided to retail savers and investors. On 1st January 2013 the recommendations of this review came into force. The implementation of RDR will usher in three important changes to the financial advice landscape.

- First, depending upon the client and the type of advice sought, professional financial advisers will either charge their clients: a one-off fixed fee for advice; a fee based upon an hourly rate; a fee based upon the assets under management or under advisory; or a combination of these.

- Second, advisers will have to make it clear to their clients whether they are able to advise on financial products from any providers, or whether they are only able to advise on those from one provider. In the former case, the adviser will be providing 'independent' advice and, in the latter case, they will be giving 'restricted' advice.

- Finally, with the RDR the FSA hopes to improve the quality of financial advice by increasing the qualifications necessary to practise as a financial adviser.

Financial advisers have been preparing for the RDR revolution for some time. However, it would be fair to say that most UK consumers are probably unaware that this revolution has taken place.

1. The Guidance Gap

The most important result of the detailed research summarised in this report is that there will be a substantial number of people in the UK that will not consult professional financial advisers in the RDR world. We find that many people will simply not be willing to pay for financial advice at all; others that might be willing to pay will not be willing to pay the level of fee that professional advisers will need to charge; and finally, some that may be willing to pay will simply not have sufficient investible assets to make it economical for financial advisers to provide them with the advice that they need.

Given that sound personal finances are probably as important to our well-being as good health, how will these consumers make their financial decisions in the future?

We explored the role that **'financial guidance'** could play for these people. By guidance we mean **directing an individual towards resources that will provide them with all of the information that they would need to make investment and savings decisions on their own**.

We believe that there will be a role for product providers, employers, adviser firms and other trusted sources to provide the financial guidance that will be needed in the future. It will be needed for two main reasons: first, only a very small proportion of the UK's adult population will be both willing to pay for financial advice and attractive as a client to a professional financial adviser; second, even among current investors the required knowledge to make investment decisions is limited – for example, only 21% of current investors told us that they had a 'good' understanding of saving and investment products.

In order to maintain the health of their personal finances, those people that will be without professional financial advice but lack the confidence to make their own decisions, will require some form of financial guidance. Together they comprise what we refer to as the financial guidance gap.

Using this survey, we have been able to identify both the number of people that will fall in to the guidance gap and also their financial position. In aggregate we estimate that the total investible wealth of the 43 million of the UK's adult population that will fall in to the guidance gap is approximately £440 billion. We also estimate that the people in the gap currently save a total of £54 billion every year.

The sheer scale of the guidance gap is worrying. Indeed, without wishing to be too melodramatic about the problem, we would suggest that a deficit in medical advice on the same scale would trigger a national outcry. On the positive side, understanding and recognising a problem is at least part way to resolving it. The guidance gap represents both a challenge and an opportunity for the financial services industry to provide a level of financial guidance that could help mitigate both the reduction in demand for financial advice and the possible decline in its supply.

2. Focusing on current "investors"

"The current investor"
The typical investor in our survey has at least one investment product. 45% of investors had direct holdings of equities, 44% had a stocks and shares ISA, 55% had a personal pension, while 9% had a SIPP. 66% of the respondents were male; 9% were under the aged between 18 and 40, 57% were aged between 40 and 64 and the remainder were aged 65 or older; 53% were working, while 42% were retired; 39% of respondents lived in London and the South, 13% lived in Scotland, Wales or Northern Ireland, 24% lived in the North, 15% in the Midlands and 9% in the East of the country; finally, the average gross household income of the respondents was £45,700. We also found that 53% of male investors would be confident making their own investment decisions without taking any advice compared with only 36% of women investors.

The total amount of money that investors had in bank accounts, ISAs and other investments, averaged £88,748. In addition, these investors saved an annual amount (excluding personal pension contributions) of £2,811. And of the 35% of investors that contributed to a personal pension, their average annual pension contribution was £2,641.

Today's current investors are likely to be the first to experience the impact of RDR. We surveyed 521 UK adults that were already engaged in the challenging process of investing . So, for example, 45% had stocks and shares, 44% had a stocks and shares ISA, 55% had a personal pension, while 9% had a SIPP. Just under 92% of this sample of individuals were owner-occupiers, with a median household income of £37,500. Finally, 14% of the sample had children in their household under the age of 18.

Overall, the total amount of money that this sample had in bank accounts, ISAs and other investments, averaged £88,748. In addition, this sample of individuals saved an annual amount (excluding personal pension contributions) of £2,811. And of the 35% of this sample that contributed to a personal pension, their average annual pension contribution was £2,641.

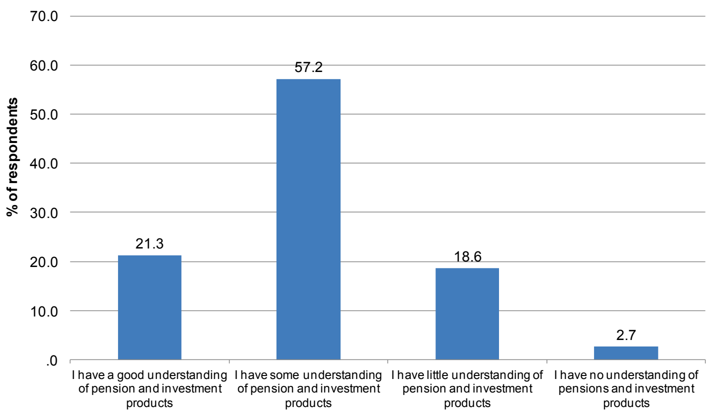
So how did these investors make their investment decisions before the introduction of RDR?

Financial decisions pre-RDR
Figure 1 presents a picture of investors' assessment of their own knowledge of investment and pension products:

- Only 21% believed that they had a good understanding of these products while, at the other end of the scale, approximately the same proportion said they had little or no understanding
- Just over 57% claimed to have some understanding.

These results suggest that even among those people who are already well engaged with the investment industry, and with relatively large sums of average wealth, there is a significant need for appropriate help.

Figure 1 How would you decide your knowledge and understanding of pension and investment products?



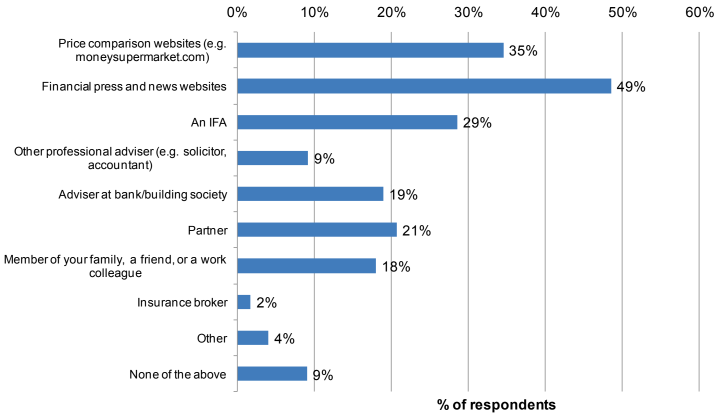
In Figure 2 we can see where UK retail investors go for advice about their personal finances. The results show what a significant role the media and internet play today in the decisions that investors make about their personal finances. But we can also see that investors do make use of professional financial advisers too, for example, 29% say that they tend to seek advice from IFAs. Furthermore, it would seem reasonable to assume that some of the advice that is derived from partners, family, friends and/or work colleagues will in turn have come from professional financial advisers.

Taken together these results suggest two things:

- First, that retail investors in the UK obtain financial advice from a mixture of sources
- Second, that within this fusion of information sources, professional financial advisers have played an important role.

5 This was a bespoke survey of UK adults that was carried out by YouGov. The fieldwork for this survey was undertaken between 30th November and 5th December 2012. The survey was carried out online.

Figure 2 **When it comes to your personal finances, which of the following sources do you tend to use to seek information and advice?**

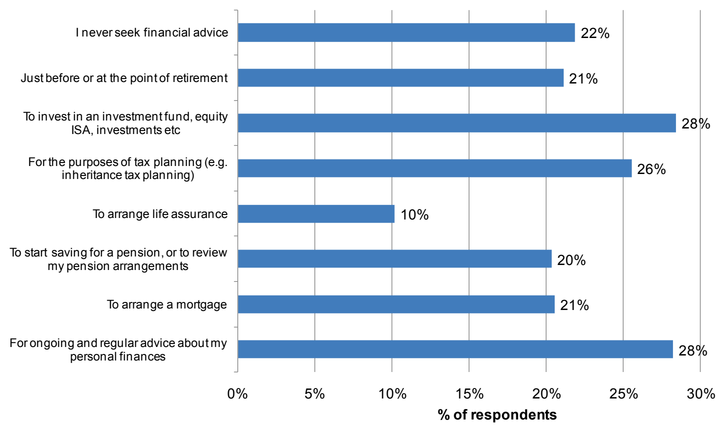


NB: percentages sum to more than 100% because respondents were encouraged to choose more than one option where appropriate.

Given the eclectic mix of advice and information that investors use, we also asked the sample which financial products they would be more likely to seek professional advice on (Figure 3). 22% of the sample, said that they never sought professional financial advice. Interestingly, at the other end of the scale, 28% of the sample said that they would seek professional advice for ongoing, or regular, advice about their finances. It would seem reasonable to assume that investors that seek ongoing financial advice have the closest relationship of all with a professional financial adviser.

Perhaps unsurprisingly, the financial product for which respondents would be most likely to seek professional advice was an investment fund (unit trust) or equity ISA (28%). The volatility of equity markets probably explains why individuals would prefer to seek professional advice when thinking about investing in the equity markets. At the other end of the scale, the product for which they would be least likely to seek professional advice is life assurance, presumably because it is perceived to be a simpler product.

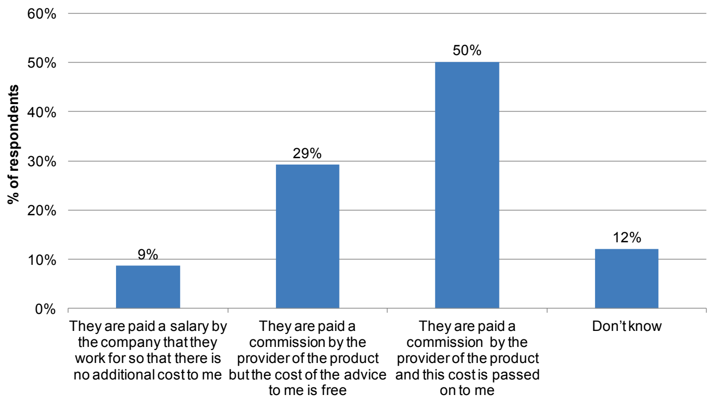
Figure 3 **For which of the following reasons, if any, would you seek professional financial advice?**



NB: Percentages sum to more than 100% because respondents were encouraged to choose more than one option where appropriate.

The majority of the UK's retail investor community tends to make at least occasional use of professional financial advice and a substantial number seek advice on an ongoing basis about their personal finances. Since RDR will change the way in which financial advisers will be paid, we asked how they believed that professional financial advisers were paid for their advice (Figure 4). The vast majority, 79%, were aware that their advisers were usually paid on a commission basis. However, we also found that 29% of investors thought that the pre-RDR commission-based remuneration framework meant that the cost to them of financial advice was free.

Figure 4 **Please imagine a financial adviser seleted an investment product for you on your behalf, which of the following ways, if any, do you think best describes how financial advisers are paid?**



One of the FSA's goals for the RDR was to make advisers' remuneration structures clearer. In other words, to make clear to consumers the 'true' cost of advice that, to some at least, appeared to have been free in the pre-RDR world. However, in doing so the FSA introduced the distinct possibility that investors will not be willing to make an explicit payment for financial advice in the future, particularly if they felt that the advice they were receiving in the past was 'free'. **As such, they could find themselves falling into the guidance gap**.

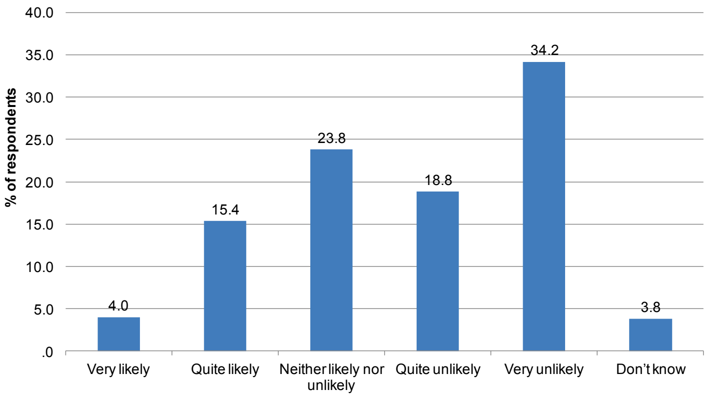
Investors' financial decision-making post-RDR

We asked the sample how likely they would be to seek financial advice if, in the future, they were charged an hourly fee for this advice commensurate with the fees that other professionals, like an accountant or a solicitor, might charge for their advice (Figure 5). Just under 20% of investors indicated that they would be 'likely' to pay for financial advice in the future.

Arguably, those investors willing to pay for financial advice would be least likely to be affected by RDR. We estimate that this group of investors, have:

- Just over £22,739 of current investible savings and
- Regularly save around £846 per year.

Figure 5 **How likely or unlikely would you be to seek financial advice in the future if you were charged a fee or hourly rate by the adviser, equivalent to the sort of fees you might expect to pay to an accountant or solicitor?**



However, the price of financial advice will clearly be key in determining whether investors will actually pay for it or not. When we asked those currently seeking financial advice what hourly fee they might be willing to pay, **58% said that they would be willing to pay 'less than £50 per hour', while 16% said that they would be willing to pay 'between £50 and £75 per hour'**.

In section 4 of this report we focus on the RDR-related views of financial advisers. As part of that survey we asked what hourly fee they were planning to charge once the RDR comes into effect. **The proposed mean hourly fee of the advisers surveyed was £165 per hour**. This average suggests the very real possibility that there will be a significant number of people in the UK who will be unwilling to pay the fees that the IFA community will need to charge to make their businesses viable in the future. We return to this issue in Section 4.

Aside from the apparent misalignment between what some investors might be willing to pay for advice and the fee that might be charged for that advice, perhaps the most concerning aspect of the responses to this question is that over half of our sample 53% indicated that they would be 'unlikely' to pay fees for financial advice in the future. We also estimate that those investors unwilling to pay for advice currently have:

- An average of £43,000 in a combination of bank accounts, ISAs etc and
- Save, on average, £1,729 every year including contributions to personal pensions.

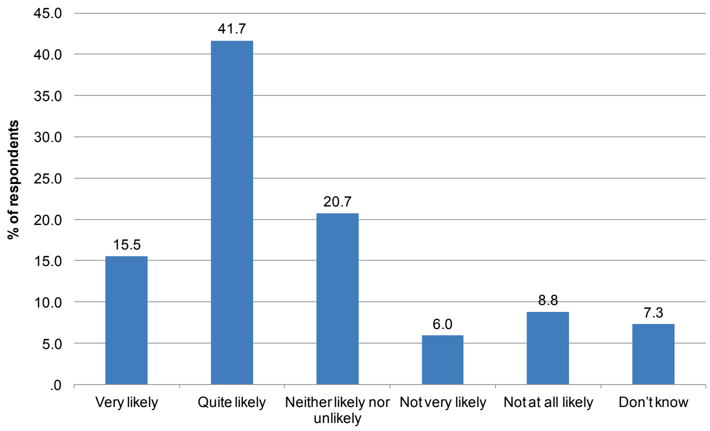
The results of our survey show that one of the unintended consequences of RDR might be that a significant number of current investors will be discouraged from seeking professional financial advice in the future. Indeed, in the post-RDR world these investors are likely to find themselves falling into the **'financial guidance gap'**.

The need for financial guidance

If there exists the possibility that a large number of current investors will not be willing to pay for financial advice or, alternatively, will not be willing to pay the equivalent of more than £50 per hour for that advice, **is it nevertheless possible for the personal finance industry to help these individuals make better-informed decisions in the future?** To ascertain the possibility of an alternative to direct financial advice, we explored the appetite for **'financial guidance'**.

We explained to our survey respondents what we meant by **'financial guidance'**, which was that it could involve pointing individuals in the right direction by providing them with all of the information that they would need to make their own investment and savings decisions. We asked them how likely they would be to use a service that provided guidance of this kind. Just under 15% of investors said that they would be 'unlikely' to make use of such a service. **However, by contrast, just over 57% of the sample said that they would be 'likely' to use such a service (Figure 6)**.

Figure 6 **How likely or unlikely would you be to use a 'guidance' service instead of paying for 'advice'?**



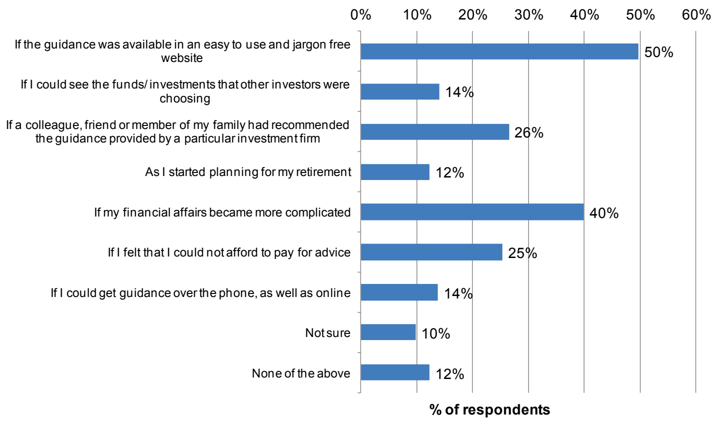
NB: Percentages sum to more than 100% because respondents were encouraged to choose more than one option where appropriate.

But what form would they like this service to take? We listed a few possible forms of **'financial guidance'**, shown in Figure 7:

- 50% of investors said that they would be willing to use a guidance service that was available in an 'easy to use and jargon-free website'
- 40% said that they would use such a service if their 'financial affairs became more complicated'
- 26% said that they would use the service if it were recommended to them by someone they knew, and
- 25% said that they would consider using the service if they felt that they could not afford to pay for advice.

Overall, these results show that there is an appetite for 'financial guidance', possibly influenced by the fact that fees for professional financial advice in the future will be more visible and will no longer appear to be 'free', as it may have seemed in the past to some people. Our survey indicates that around 80% of current investors will fall in to the guidance gap.

Figure 7 Which of the following, if any, would encourage you to seek guidance? Please select all that apply



We also asked whether there would be particular instances when they would be more likely to seek guidance (Figure 8). Although 15% said that they did not seek financial advice or did not know if they would seek guidance:

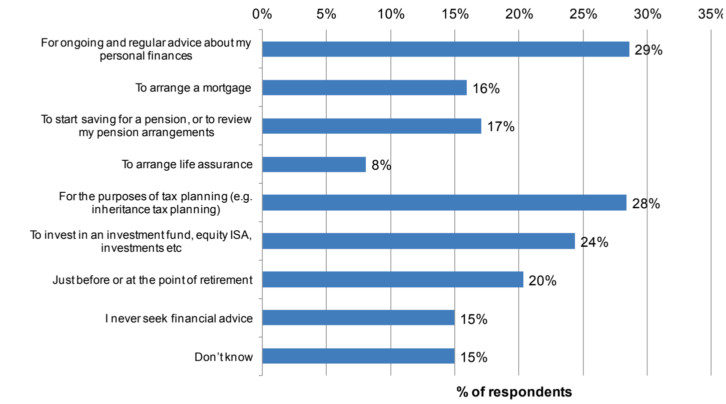
- 29% said that they would seek guidance for 'ongoing or regular advice' about their finances

- 28% said that they would seek guidance for tax planning purposes

- While 24% indicated that they would be interested in seeking guidance before, for example, buying an equity ISA.

Arguably the financial decisions required in these circumstances are more complex than those involved in the purchase of life assurance, for which only 8% of our sample said that they might seek financial guidance.

Figure 8 For which of the following reasons, if any, would you be most likely to seek guidance?



Investor summary

Overall, our survey of UK investors provides strong evidence to suggest that a significant proportion of those people in the UK that are already engaged in the process of investing, and that have significant amounts of investible wealth, will find themselves in the guidance gap. **We estimate that those UK investors that would be 'likely' to make use of financial guidance have, on average, £51,000 of investible savings and save an average of £2,081 every year.**

These results present a worrying picture of the likely immediate impact of the RDR. After all, these are people that have tended to make use of financial advice in the past, and yet less than one in five of them say that they would be likely to pay for advice in the future. Even among this group, a not insubstantial number will either not be willing to pay the likely fee for financial advice in the future, or will not have sufficient investible assets to make them attractive to an adviser.

If RDR is going to leave around 80% of current investors in the guidance gap, what impact will it have on those people that have yet to begin their investment journey? In the next section of the report we focus on these people, and consider whether RDR will be conducive to the fostering of a wider saving and investing habit.

3. RDR and the development of a wider savings habit

"The non-investor, regular saver"

A number of "non-investors" in our survey, describe themselves as saving every month. This group of individuals represents 10% of all our non-investors. We estimate that there are around 2.5 million people in the UK that fall into this category. 70% of this group are owner occupiers. 17% of these people have a gross household income of less than £25,000 per year, while 27% have a gross income between 25,000 and 50,000 per year. 66% live outside London and the South East, and 77% of them are in full time employment.

The average total savings of these regular savers is just under £6,000 and we estimate that they save an average of around £750 per year. Our survey suggests that a minimum of 86% of this group of regular savers will fall into the guidance gap, while 54% indicated that they would be likely to make use of financial guidance.

"The non-investor, non-saver"

One of the major challenges for the UK's government must be to encourage more of a savings culture in the UK population. 44% of the "non-investors" in our sample said that they did not put aside savings regular at the moment. We estimate that just over 12 million people in the UK fall into this category. 40% of this group of people live in rented accommodation or in a house owned by a Housing Association. 41% live in a household with a gross annual income of less that £25,000 and 65% live outside London and the South East. Only 51% of these individuals are in full time employment, 14% are retired from work.

Despite not being regular savers we estimate that the non-investors in this group have average, total savings of just under £2,000. We estimate that a minimum of 93% of these people will fall into the guidance gap, but encouragingly 54% of these "non-investors" said that would be likely to use a financial guidance service.

Current investors will clearly be the first to feel the impact of RDR changes. Our results show that these people will be severely impacted by the move away from a commission-based remuneration framework for financial advisers. However, the availability and nature of financial advice will also affect the wider UK population. In an attempt to understand what impact RDR will have on the savings habits of, for the want of a better term, "non-investors", we undertook a second survey of 2,060 people which was representative of the UK's entire adult population[6].

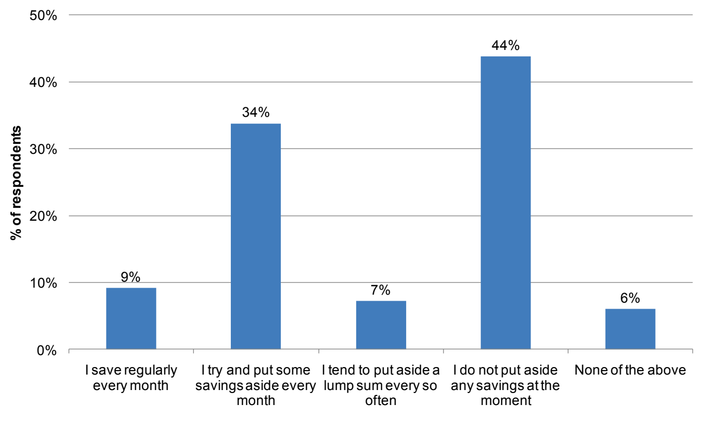
We identified this group of "non-investors" as those people that did not currently have:

- Any direct equity holdings
- A stocks and shares ISA
- A unit or investment trust
- A capital-guaranteed product
- A personal pension or SIPP
- Or another product that would indicate that they were currently engaged with the finance industry or the process of investing.

The survey indicated that "non-investors" make up around 56% of the UK's adult population, or just under 28 million[7] people.

Although these people are not currently engaged with the demanding process of investing, many do nevertheless try to save for their futures. Figure 9 shows how this large section of the UK's population tends to save. Only 9% of them describe themselves as regular savers but 34% do try to save regularly, while 7% tend to put a lump sum aside every so often. The largest single group is those people that do not put aside savings at the moment. We asked the 44% of the sample that made up this group why they did not currently save. 84% said that they did not do so because they could not afford to. It would be fair to say that the RDR would have the smallest impact on this group of people which makes up around 12 million[8] of the UK's population.

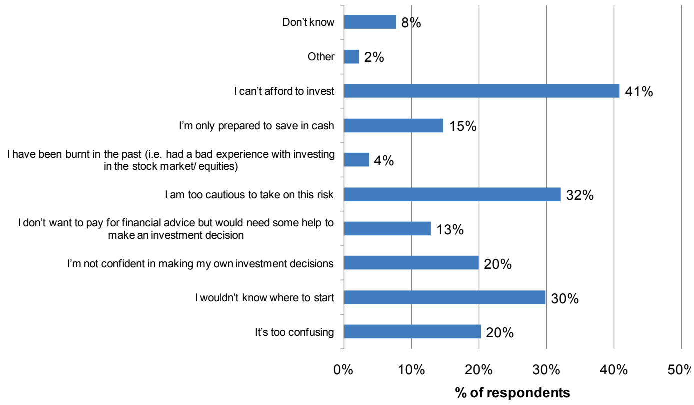
Figure 9 Which one of the following statements, if any, best describes how you tend to save?



6 This survey formed part of YouGov's Omnibus survey. The fieldwork for this survey was undertaken between 11th and 13th December 2012. The survey was carried out online. The figures from the omnibus survey have been weighted and are representative of all UK adults (aged 18+).
7 56% of the omnibus survey are non-investors – 56% x 49.97 million = 28 million.
8 44% of non-investors make up this group – 44% x 28 million = 12 million.

Those “non-investors” that do save, save an average amount every year of £962, and the total amount of average investible savings of all non-investors is £3,221. These are substantial sums of money that are not currently finding their way into investment products. We asked these “non-investors” why they did not currently invest in equity-related products (Figure 10). In keeping with the results shown in Figure 9, a large proportion said that they did not invest because: they felt that they could not afford to; 32% viewed themselves as being too risk-averse to invest; while 30% said that they ‘wouldn’t know where to start’.

Figure 10 Which, if any, of the following reasons describe why you do not currently invest in the stock/ market/equities?



NB: Percentages sum to more than 100% because respondents were encouraged to choose more than one option where appropriate.

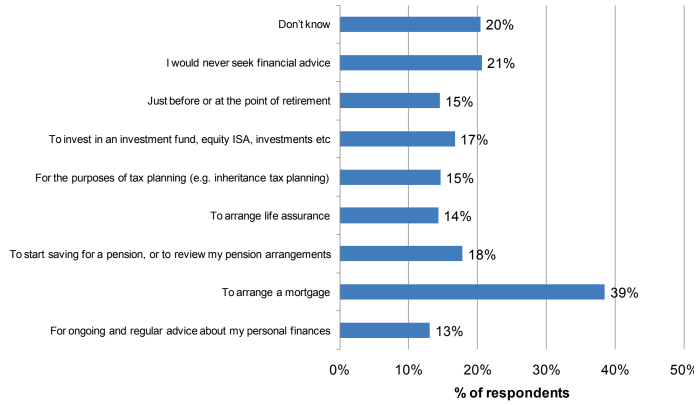
Clearly, one of the main reasons why a significant proportion of people in the UK do not currently invest in the stock market is because of the perceived complexity. However, putting this aside for a moment, we asked the “non-investors” how much they could afford to invest in equity-related products. **Of the approximate 60% of respondents that said that they could spare money to invest in such products, the average amount that they could afford to invest every year was £709**. Again given that these people are not currently investors, it seems unlikely that these potential sums for investment will find their way into investment products without advice or guidance of some kind.

Given the level of caution with regard to investing, but also the not insubstantial potential demand for investment, we asked these “non-investors” when they might consider seeking professional financial advice (Figure 11):

- 39% said that they would do so to arrange a mortgage
- 21% said that they would never seek financial advice
- 15% said that they would do so at or just before the point of retirement
- While 18% said that they would do so to either start saving for a pension or to review their pension arrangements.

Perhaps surprisingly only 17% said that they would do so before investing in an equity-linked product, though this may reflect a general unwillingness to invest in equities, rather than being an indication that they would invest in equities without advice or guidance.

Figure 11 For which of the following reasons, if any, would you seek professional financial advice?

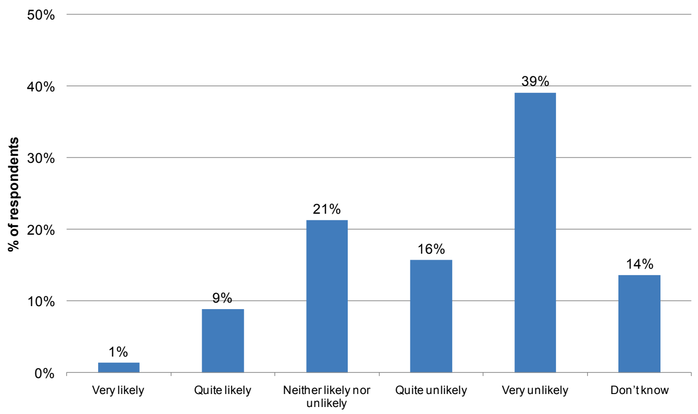


NB: Percentages sum to greater that 100% because respondents were encouraged to choose more than one option where appropriate.

Our results clearly suggest that there is a demand for financial advice amongst “non-investors”, and in particular amongst the 13% that said they would like ‘ongoing financial advice‘. Given that the implementation of RDR will now require financial advisers to charge a fee for their work, we asked “non-investors” if they would be willing to pay for financial advice in the future. **Only 10% of non-investors said that they would be ‘likely’ to do so, whereas a substantial number 55%, said that they would be ‘unlikely’ to pay**. Furthermore, when asked what hourly rate they might be willing to pay, of those non-investors that were willing to consider paying a fee, almost three out of five, 58%, said they might be willing to pay less than £50 per hour.

It is therefore clear that the vast majority of the UK’s population that are not currently engaged in the process of investing would be unwilling to pay for financial advice in the future. In the absence of professional advice or some sort of financial guidance it is difficult to conceive how these people will begin their investment journey, or indeed how they will make more of their current savings.

Figure 12 **How likely or unlikely would you be to seek financial advice in the future if you were charged a fee or hourly rate by the adviser?**



The potential for financial guidance for "non-investors"

To address this point we again asked whether people would be willing to consider using the sort of financial guidance service (Figure 13) described earlier. **Over half of non-investors said that they would be 'likely' to use such a service, compared with 19% that said that they would be 'unlikely' to**. Interestingly, we also found that 61% of 18 to 34 year old "non-investors" would be willing to use a financial guidance service, compared with only 30% of those aged 55 and over. Indeed, we find that 36% of "non-investors" aged 55 and over would be unlikely to use such a service; by contrast only 9% under the age of 34 said they would be unlikely to use a financial guidance service. It would appear then that the concept of financial guidance appeals more to the younger "non-investors" than to older generations of "non-investors". Finally, Figure 14 shows that 37% of "non-investors" would consider using a guidance service if it were on a 'jargon-free website'; while 28% said that they would use a financial guidance service if their 'financial affairs became more complicated'.

These results show that there is substantial demand for financial guidance among the UK's population of "non-investors", the majority of whom will find themselves in the guidance gap.

Figure 13 **How likely or unlikely would you be to use 'guidance' service instead of paying for'advice'?**

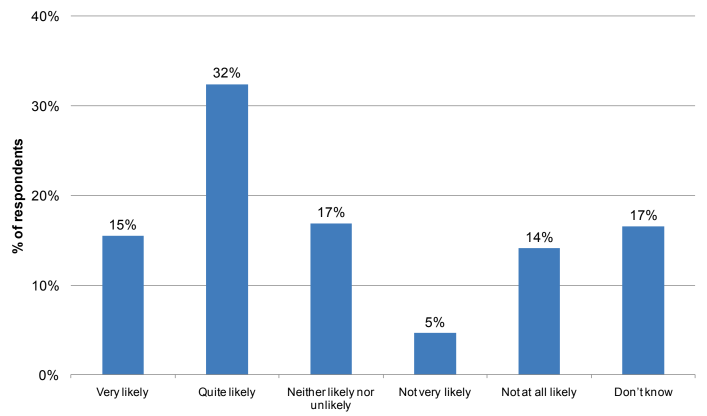
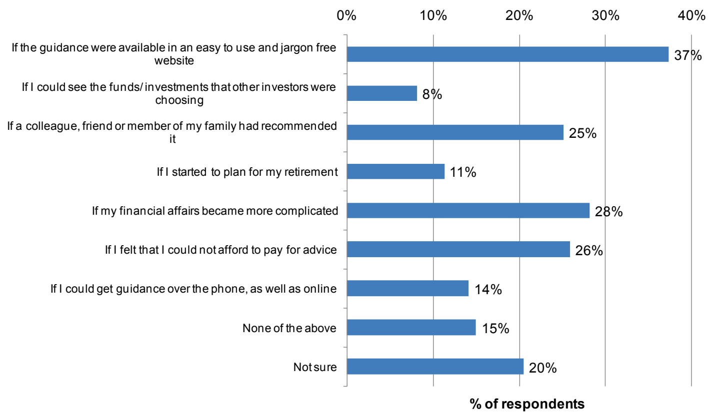


Figure 14 **Which of the following, if any, would encourage you to seek guidance?**



NB: Percentages sum to more than 100% because respondents were encouraged to choose more than one option where appropriate.

"Non-investor" summary

Unsurprisingly 12 million[9] or so people in the UK today are not currently investors and do not save regularly because they cannot currently afford to save. The RDR revolution is unlikely to have an immediate impact on these people. **However, a significant number of "non-investors", around 15.5 million[10] do save, either regularly, every month, or less regularly and have both the capacity to save more and to become investors. But the vast majority of all "non-investors" will fall into the guidance gap.**

Among "non-investors" we do find clear evidence of demand for financial guidance. Of those that would be 'likely' to make use of financial guidance, their average total savings is approximately £2,420.38 and they currently save an average of £562.88 every year.

9 44% of the 28 million "non-investors" make up this group – 44% x 27.75 million = 12 million.
10 56% of the 28 million "non-investors" make up this group – 56% x 28 million = 15.5 million.

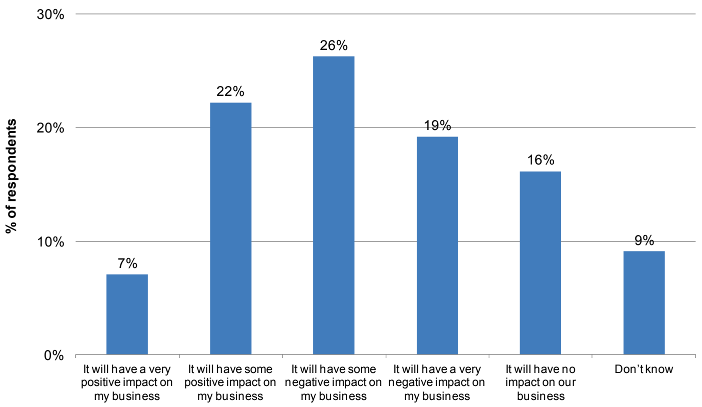
For “non-investors”, making the decision to embark on a meaningful investment journey would, prior to the advent of the RDR, have been a big decision, and one that some would probably not have started without at least occasional professional financial advice. It seems entirely possible to us that starting this journey in a post-RDR world will be an even more difficult process if those “non-investors” that wish to begin it feel that financial advice is either too expensive or not available to them. **As such in the absence of a suitable alternative – high-quality financial guidance – there exists the real risk that fewer people in the future will make the transition from “non-investor” to “investor”. Indeed, in the absence of such guidance, the RDR could turn out to be a major impediment to the development of a wider saving and investment habit in the UK.**

4. The impact of the RDR on financial advisers and their clients

In order to determine whether the expectations of professional financial advisers are aligned with those of their clients, we conducted a survey of 99 UK-based financial advisers[11]. We began by asking the survey participants what impact they thought the RDR would have on their business (Figure 15). 29% of those surveyed suggested that it would have at least some positive impact on their business, though 45% felt that it would have at least some negative impact on their business.

On balance it would seem that the RDR is expected to have a negative impact on the financial advice industry. Further investigation of the responses revealed that this view was not influenced by the size of the firm; that is, some big and some small firms felt that it would have a positive effect on their business, while some large and some small firms thought that it would have a negative impact.

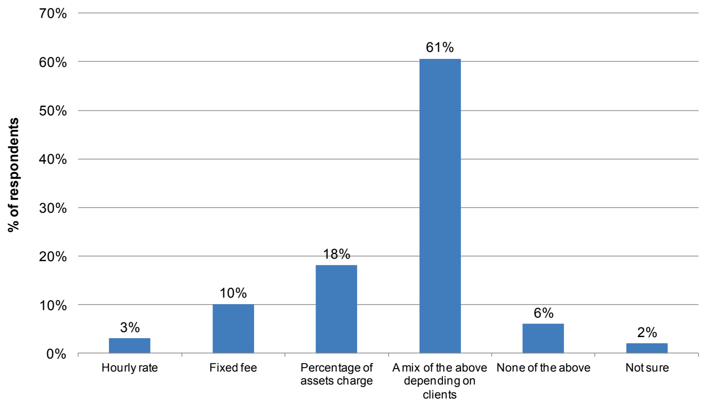
Figure 15 How do you think the Retail Distribution Review will affect your business?



The RDR will mean that a professional adviser's clients will pay a more explicit fee for the advice they receive. But this fee could be determined in a number of ways. We asked which fee model they were proposing to use in the RDR world (Figure 16). 61% said that they would be using a mixture of a percentage charge on assets under advisory, a fixed fee and an hourly fee.

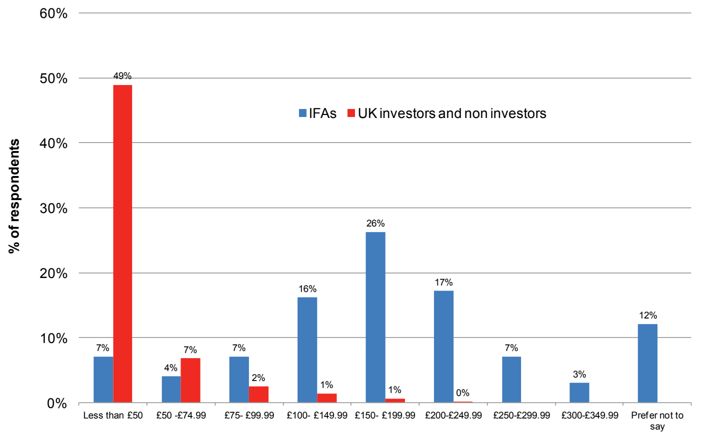
It is likely that the nature of the fee will depend very much upon the nature of the relationship between the adviser and their client. Discussions with senior figures in the financial advice industry revealed that for one-off pieces of advice a fixed fee or an hourly rate might be charged while for clients with more significant assets on which they wished to receive regular advice the fee would more likely be a percentage of the portfolio under advice. This latter arrangement is of course the most common approach to management fees paid by institutional investors to their fund managers.

Figure 16 Which of the following methods of charging do you expect to offer clients post-RDR?



However, most advisers in our sample, when asked the likely hourly charge for their services, indicated a level higher than people expected to pay. This result suggests that in this post-RDR world advisers will need to demonstrate the value and benefit of their advice. The blue bars in Figure 17 show the hourly fees that the financial advisers in our survey plan to charge in a post-RDR world. We estimate that the average hourly fee that IFAs plan to charge is just under £165 per hour. The red bars show the fees that investors and "non-investors" would be willing to pay per hour for financial advice; 49% would be willing to pay less than £50 per hour, but only 7% of the advisers we surveyed are planning to charge a fee of less than £50 per hour.

Figure 17 Hourly fees for financial advice in an RDR world

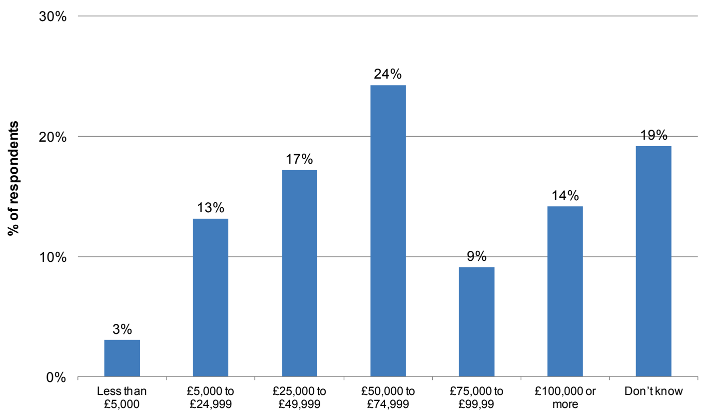


We also asked the advisers what level of investible assets a client would need to have in order for them to be attractive as a client (Figure 18). First, a significant proportion of advisers 19% did not know what this level would be, a result that perhaps reflects some of the uncertainty that the RDR has created about viable advisory business models. 24% of the sample estimated that clients would need between £50,000 and £75,000 in investible assets. We estimate that just over 55% of the UK's adult population have less than £5,000 of investible assets, and only 14% have between £5,000 and

11 This was a bespoke survey of UK IFAs that was carried out by YouGov. The fieldwork for this survey was undertaken between 30th November and 5th December 2012. The survey was carried out online.

£25,000 of investible assets. **This should serve as wake up call to the industry and to regulators because over half of the adult population will only be of commercial interest to just 3% of the adviser community. It would seem very implausible that such a small proportion of the financial adviser community would be capable of servicing such a large proportion of the UK's population.**

Figure 18 **What minimum level of investible assets will a client need to have for you to continue to service them?**



The orphan issue

As we explained in Sections 2 and 3 of this report, a large proportion of both current investors and the UK population more generally would be 'unlikely' to be willing to pay for financial advice. In a post-RDR world then they may choose to make financial decisions without advice from a professional adviser. But as well as there being a large proportion of people that may choose not to seek professional advice on a fee-paying basis, there is another group that may also find themselves 'adviceless' in the post-RDR world despite their desire to access advice.

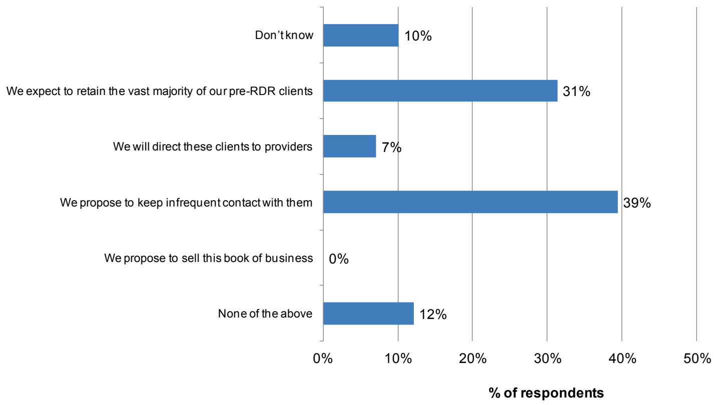
We find that among those in the UK population that would be 'likely' to pay for financial advice, only 46% have sufficient assets to make them commercially viable to, at most, 3% of the adviser community, because they have less than £5,000 in current investible assets (Figure 19).

But there are clearly many financial advisers who may no longer find it viable to service the needs of some of their clients, even where they have investible assets well in excess of, say, £5,000. Our survey suggests that the average level of investible assets needed to make a consumer commercially viable to an adviser is approximately £61,000. We find that 69% of the UK's population does not have current investible assets above this level. Those clients that fall below the required investible assets threshold of their current adviser may also find themselves looking for a new one.

One of the unintended consequences of RDR may well be the creation of a pool of willing investors, who sought and received advice in the past, and that will still seek such advice in the future, but who may not be able to find an adviser willing to provide the service they need. These individuals may find themselves becoming financial advice orphans.

We asked the advisers what they intended to do with those clients that would not be commercially viable to them in the light of the RDR changes (Figure 20). Only 31% expected to keep most of their clients, meaning of course that 69% expect not to retain at least some. 39% of advisers indicated that they would keep in infrequent contact with these clients, in effect withdrawing as their financial adviser, but staying on the sidelines just in case the client was willing to pay for advice in the future, either directly or because the size of their investible assets had risen sufficiently to make them commercially viable for the adviser's business. Interestingly, 7% indicated that they would direct them towards a product provider for their financial needs. Finally, none of the advisers sampled here said that they would sell this book of business. **However, once the RDR changes begin to have an impact on adviser businesses, those that plan to keep in infrequent contact with their clients may consider selling this portion of their client base to maximise their revenue from their pre-RDR book of business.**

Figure 19 **Where it is commercially viable for you to retain a client, what does your firm intend to do?**



Looking further ahead

As well as surveying a large sample of UK-based advisers we also conducted a number of in-depth interviews with senior industry figures. The purpose of the interviews was to try to elicit views from experienced professionals about the possible longer-term impact of RDR on the financial advice industry.

Financial adviser numbers

Most of those questioned suggested that one of the most likely consequences of RDR would be a fall in adviser numbers. It was suggested that this decline in numbers could come from two possible sources. First, the unwillingness or inability of some pre-RDR advisers to pass the necessary qualifications to remain as an adviser in the post-RDR world. Second, those advisers that relied entirely on commission-based remuneration, may find that enough of their pre-RDR clients would be unwilling to pay for financial advice in the future making their businesses uneconomic, thereby forcing them to withdraw from the industry. Some of the interviewees suggested that within two to three years there could be as few as 15,000 professional financial advisers in the UK.

From an adviser perspective the possible decline in adviser numbers could be an opportunity for those that remain in the industry which would arguably be those that are best prepared for RDR or those that have been operating an RDR-compliant model prior to its imposition. Such a contraction in numbers, were it to happen, would mean that these remaining advisers could concentrate even more on those people with higher levels of investible assets. From a client perspective, a decline in adviser numbers should mean that the better-qualified advisers would provide, on average, better-quality advice in the future. Of course, the flip side of this is that this contraction could also leave an increasing proportion of the UK population without advice, or as financial advice orphans.

The re-emergence of direct sales forces

Another issue raised by interviewees, and which is related to the possible decline in adviser numbers, was the prospect of a re-emergence of direct sales forces. It was suggested that large providers, with equally large numbers of clients, will need to service the needs of these consumers somehow. Interviewees suggested that one way of doing this would be via the 'restricted advice' route, where large providers might put together teams to service the holders of their products, possibly over the phone, advising on these existing products and also talking to these clients about their own restricted range of products - that is, not those of other providers. It was generally felt that in order to comply with RDR these direct 'sales teams' would have to be remunerated on a fixed-salary basis, and not as some proportion of 'sales'. They would also need to make it clear to their clients that they could only advise on their provider's range of products, and on the possible benefits of speaking to an independent financial adviser. Such a service might at least meet some of the financial needs of those consumers with relatively small investments, or who were making only very low levels of regular contributions to, for example, an equity ISA.

Technology

Finally, a common theme was the role that technology was expected to play in the RDR world. For those individuals that either did not want to pay for advice, could not afford to pay for it, or who found themselves becoming financial advice orphans, technology was seen as one possible way of providing for their financial needs. In particular, web-based services that would allow individuals to keep track of all of their finances from their salary, pension contributions and financial products, through to their bills and other outgoings, were likely to develop, making them more and more attractive to use on tablets, and via internet TV, for example. Indeed, Figure 2 shows how much use current investors make of web-based information sources already. Interviewees saw a number of possible providers of such websites. First, large employers may develop existing workplace savings platforms for their employees. Second, the providers of financial products could make their services more widely available. Third, websites designed by third parties, perhaps developed from existing 'financial supermarket' and 'financial comparison' websites could emerge. And, finally, it was suggested that some financial advisers, or groups of advisers, might be able to provide such a service. They could, in effect, offer advice for those current and future clients that would be willing to pay for it on the one hand while, on the other, direct those that do not wish to pay for it, including current clients, towards a financial guidance equivalent of their direct advisory service.

Throughout this report we have highlighted the crushing need and demand for financial guidance. A combination of all of these could provide people with the financial guidance that our survey says a huge number will need in a post-RDR world.

5. Conclusions

One of the presumably unintended consequences of the RDR will be the creation of an enormous guidance gap, comprising millions of the UK's current investors, and millions more potential investors that have not yet begun their investment journey. These people will almost certainly not seek professional financial advice in the future, despite their clear need for it. And if the worst fears of some of the industry's senior figures are realised, and the population of professional financial advisers shrinks as a consequence of the RDR, then it will be harder and harder to find such financial advice anyway, as the remaining population of advisers focuses more and more on wealthier, more profitable clients.

In the absence of financial advice, trusted sources will need to provide help for those in the guidance gap as they either continue their investing journey or as they look for ways to begin it. In aggregate we estimate that the total investible wealth of those in the guidance gap is approximately £440 billion. We also estimate that those people in the guidance gap currently save a total of £54 billion every year. **The challenge for the finance industry in coming years will be to find ways of guiding this wealth for the long-term benefit of its owners**.

Appendices

Appendix 1: Calculating the guidance gap

- To calculate the size of the guidance gap, we identified all those respondents in YouGov's omnibus survey that did not tell us that they would be likely to pay for advice.
- This group of people represented 85.7% of the omnibus sample, therefore representing 42.8 million UK adults (currently 49.97 UK adults according to ONS).
- We then calculated the sample average of 'investible savings' of this group of people which came to £10,271.
- Our estimate of the total investible savings of those in the guidance gap was then calculated as the product of this average and the number of people in the guidance gap, a value of £440 billion.
- We used the same methodology to calculate the average annual savings of those in the guidance gap, including pension contributions which came to £1,259, giving a value of approximately £54 billion for the regular flow of savings in the guidance gap.

Appendix 2: The surveys

The results in this report were based upon three surveys that were each conducted by YouGov.

- The results in Section 1 of this report are derived from the YouGov omnibus survey, which is designed to be representative of the UK's adult population. The total number of respondents to the survey was 2060. 48% of the respondents were male; 37% were under the aged between 18 and 40, 47% were aged between 40 and 64 and the remainder were aged 65 or older; 62% were working, just over 20% were retired; just under 35% of respondents lived in London and the South, 16% lived in Scotland, Wales or Northern Ireland, 24% lived in the North, 16% in the Midlands and just over 9% in the East of the country; finally, the average gross household income of the respondents was just over £38,000 per year. From this survey we were able to calculate the size of the Guidance Gap and the number of people that fell into it.
- The analysis in Section 2 of this report is based upon a bespoke YouGov survey of 521 UK adults that already held an ISA, a unit or investment trust, a capital guaranteed product, a SIPP or other products that would indicate that they were already engaged with the finance industry and in the challenging process of investing. 45% of this sample had direct holdings of equities, 44% had a stocks and shares ISA, 55% had a personal pension, while 9% had a SIPP. 66% of the respondents were male; 9% were under the aged between 18 and 40, 57% were aged between 40 and 64 and the remainder were aged 65 or older; 53% were working, while 42% were retired; 39% of respondents lived in London and the South, 13% lived in Scotland, Wales or Northern Ireland, 24% lived in the North, 15% in the Midlands and 9% in the East of the country; finally, the average gross household income of the respondents was £45,700.
- Section 3 of this report was based upon a subset of the respondents to the omnibus survey, which we refer to throughout the report as "non-investors". We identified this group as those respondents to the omnibus survey people that did not currently have: any direct equity holdings; a stocks and shares ISA; a unit or investment trust; a capital-guaranteed product; a personal pension or SIPP; or another product that would indicate that they were currently engaged with the finance industry or the process of investing. The omnibus survey indicated that "non-investors" make up around 56% of the UK's adult population, or just under 28 million people. 43% of "non-investors" were male; 42% were under the aged between 18 and 40, 46% were aged between 40 and 64 and the remainder were aged 65 or older; 63% were working, 17% were retired; 37% of respondents lived in London and the South, 13% lived in Scotland, Wales or Northern Ireland, 27% lived in the North, 14% in the Midlands and just over 9% in the East of the country; finally, the average gross household income of the respondents was just over £33,000 per year.
- Finally, Section 4 of the report was based largely upon a survey of 99 UK-based IFAs. This survey was also carried out by YouGov. 46% of the IFAs surveyed were based in London and the South, 18% in the North of England, 22% in the Midlands and the East; 11% in Scotland and 4% in Wales. 51% of those surveyed worked in a firm with between 2 and 9 professional financial advisers; 27% worked alone, while over 10% of the IFA respondents worked for firms with 50 or more advisers.

Cass Consulting
Cass Business School
106 Bunhill Row
London EC1Y 8TZ
T: +44 (0)20 7040 3273
E: christina.makris.1@city.ac.uk
www.cassknowledge.com/cass-consulting

Cass Business School
In 2002, City University's Business School was renamed Sir John Cass Business School following a generous donation towards the development of its new building in Bunhill Row. The School's name is usually abbreviated to Cass Business School.

Sir John Cass's Foundation
Sir John Cass's Foundation has supported education in London since the 18th century and takes its name from its founder, Sir John Cass, who established a school in Aldgate in 1710. Born in the City of London in 1661, Sir John served as an MP for the City and was knighted in 1713.