

In association with



  
owenjames

The logo for Owen James, consisting of a stylized 'O' symbol made of two overlapping circles (one white, one yellow) above the text "owenjames" in a white, lowercase, sans-serif font.

# IFA performance benchmark 2008

## Executive summary

Part one

# Background

- A pilot study was put together in November 2006 in an attempt to better understand the key performance indicators within advisers' businesses and to identify areas where streamlined processes could aid efficiency and increase profitability.
- The idea sprung out of an event called A Meeting of Minds organised by Owen James whose intention was to promote a more united industry, identifying common ground and working together to make progress.
- The need for better business modelling was identified as a priority and in response to this, Owen James, working with a leading professional services firm, devised the Advisory Distribution Performance Benchmarking Questionnaire.
- Scope - 102 IFAs completed the questionnaire, but only 60 of the 102 were fully completed. This is a marked increase on the 18 IFAs that completed the pilot study back in 2006.
- All data has been treated totally confidentially and these findings have been published in aggregated form for the whole sample and per category of business model. All participants who supplied full data will have an opportunity to benchmark themselves against similar models using the online reportal.

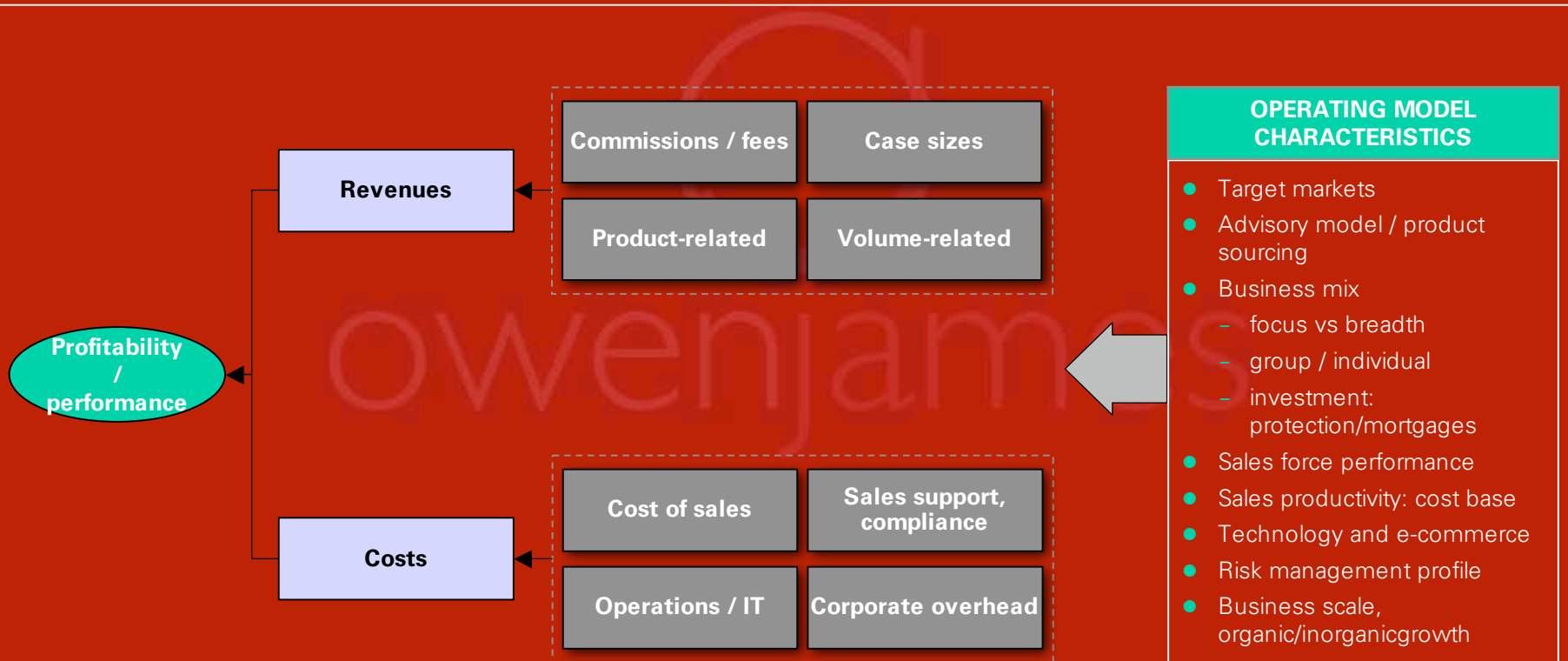
# Objectives

- Identify the productivity pressure points within the IFA firms by analysing data on business practices and performance.
- Formulate actions to reduce costs and improve profitability.
- Highlight examples of best practice - what does a profitable business model look like?
- Understand the true value of IFA businesses.
- Answer the following:
  - How many appointments should an adviser be able to manage in a day?
  - What is the average income by adviser?
  - What proportion of a successful company's income is invested in IT?
  - The mix of fees and commission - is a move to fees the answer? What sort of fees are people charging?
  - How many firms are using wraps? What the effect on business performance?
  - What is the recruitment market like? And just what is the average age of the adviser?
  - Average income per client ie cost of time spent on client vs yield?
- Provide an opportunity for IFAs to benchmark themselves against similar business models.
- Create business learning opportunities.
- Build a collective voice to respond to the FSA - to answer some of the criticisms being levelled at it that it is not commercially viable.

# Findings from the pilot study (2006)

- The analysis from the pilot study found that the characteristics of higher margin businesses included:
  - greater proportion of earnings from existing rather than new clients
  - greater proportion of earnings from recurrent rather than initial commissions
  - less commission given to advisers
  - greater use of electronic trading
  - lower turnover of advisers
  - more equally spread distribution of business among advisers
- Key stats:
  - most of the sample did not declare profits: average cost income ratio was over 100%
  - top performers earned over 85% revenues from existing clients but had a lower proportion of revenue from fees
  - top performers used e-commerce more than four times as much as poor performing firms

# Overview of performance benchmarking process



# Some important definitions

- Gross Margin (GM) = This is an indication of how profitable a company is and how much a company earns taking into account the costs it incurs to produce its products and services. eg a GM of 35% indicates that £0.35 is retained from every £1 of revenue generated to put towards paying off selling, general and administrative expenses, indirect expenses and distributions to shareholders.

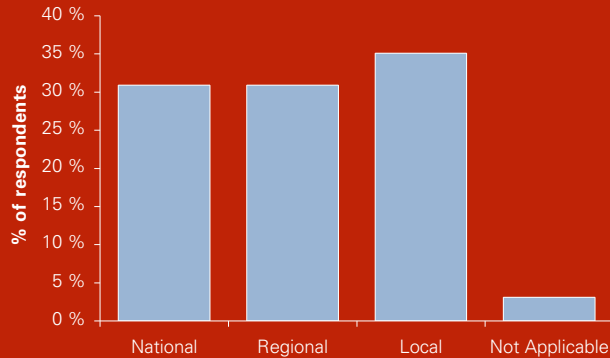
$$\text{Gross margin} = \frac{\text{Gross income (total sales revenue - cost of goods sold)}}{\text{Net sales}}$$

- Cost Income (CI) = The cost/income ratio is an efficiency measure similar to operating margin. Unlike the operating margin, lower is better. The cost income ratio is most commonly used in the financial sector. It is useful to measure how costs are changing compared to income.

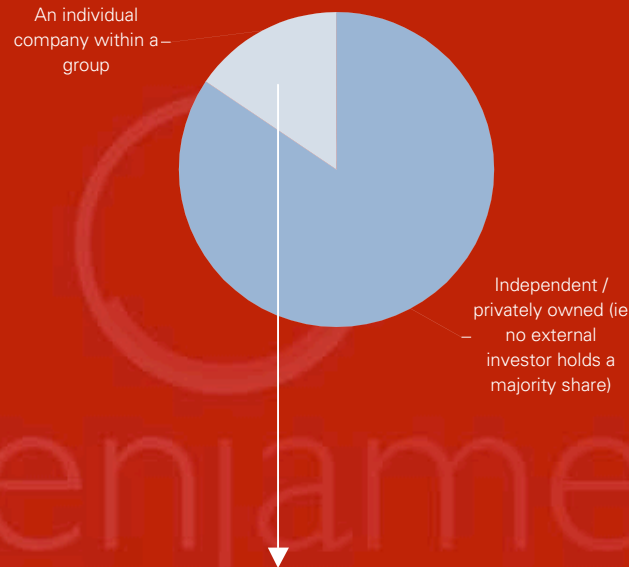
$$\text{Cost index} = \frac{\text{Operating expenses}}{\text{Operating income}}$$

# Overview of sample

**Business structure**

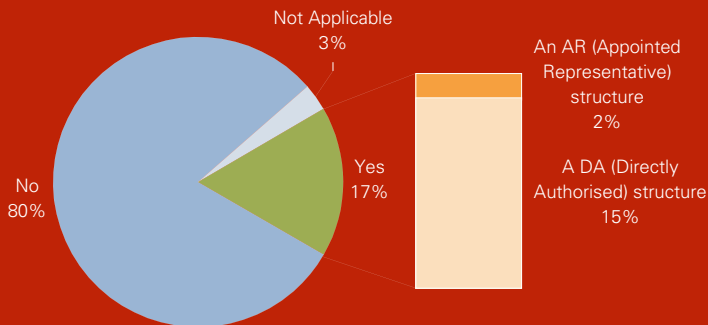


**IFA ownership**

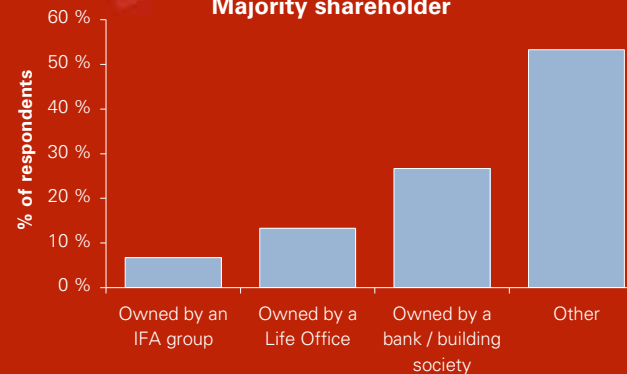


- This year's sample consisted of 102 responses
  - But only 60 out of 102 were fully complete.
  - For the purposes of the analysis, the responses were filtered, as there was a number of respondees who answered only few of the questions asked

**Member of a network**

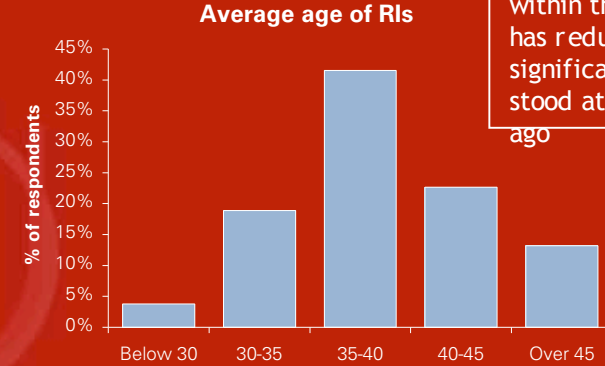
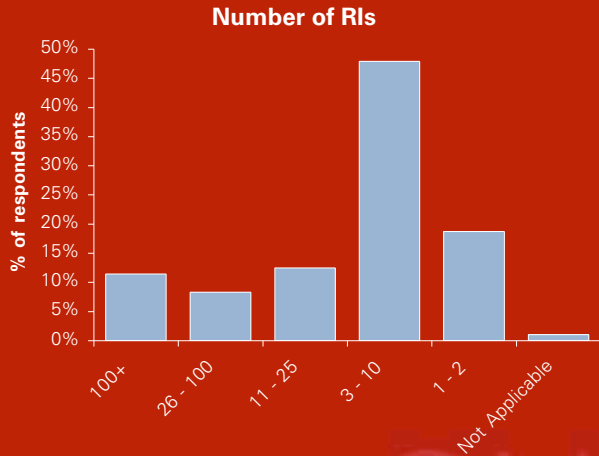


**Majority shareholder**

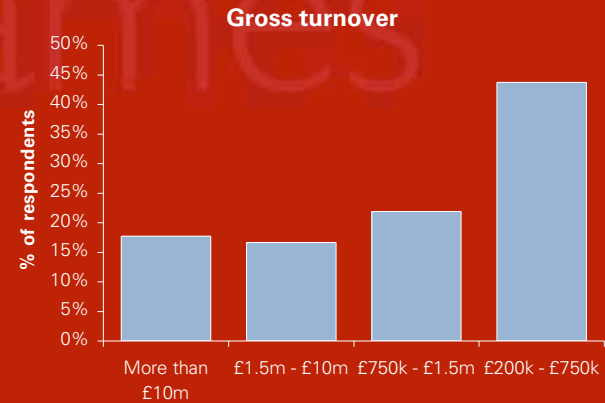
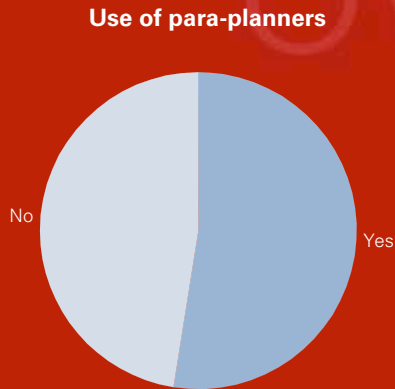


- The sample represents a good spread of different business models across the industry

# Overview of sample (cont.)



The average RI age within the industry has reduced significantly, which stood at 56 four years ago



# Survey results

## Average profitability

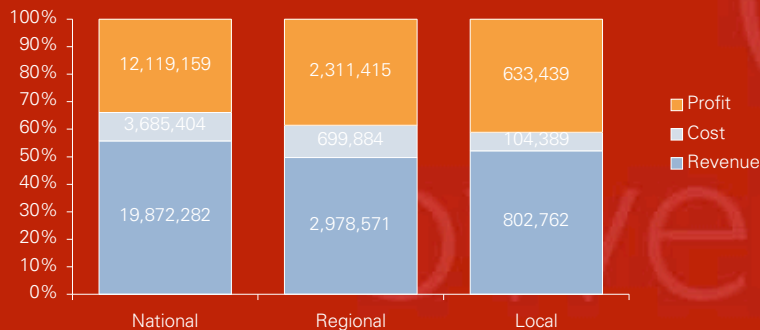


Despite a strong increase in revenues, profitability has risen slightly over the past four years due to strong cost increases.

# Survey results

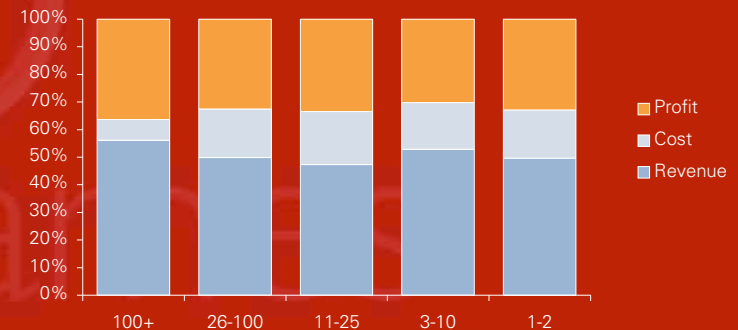
## Average profitability by business structure and RI number

Average profitability by business structure



Local business models are able to generate greater profitability due to lower cost pressures.

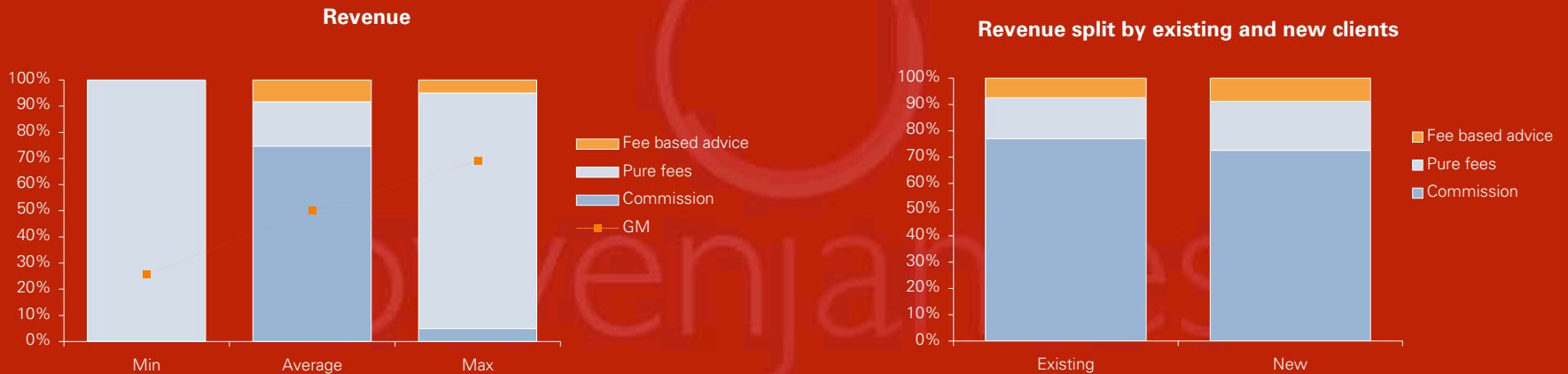
Average profitability by number of RIs



However, cost efficiencies begin to be realised with IFA practises employing over 100 RIs, and as a result these firms also enjoy greater profitability.

# Survey results

## Revenue mix

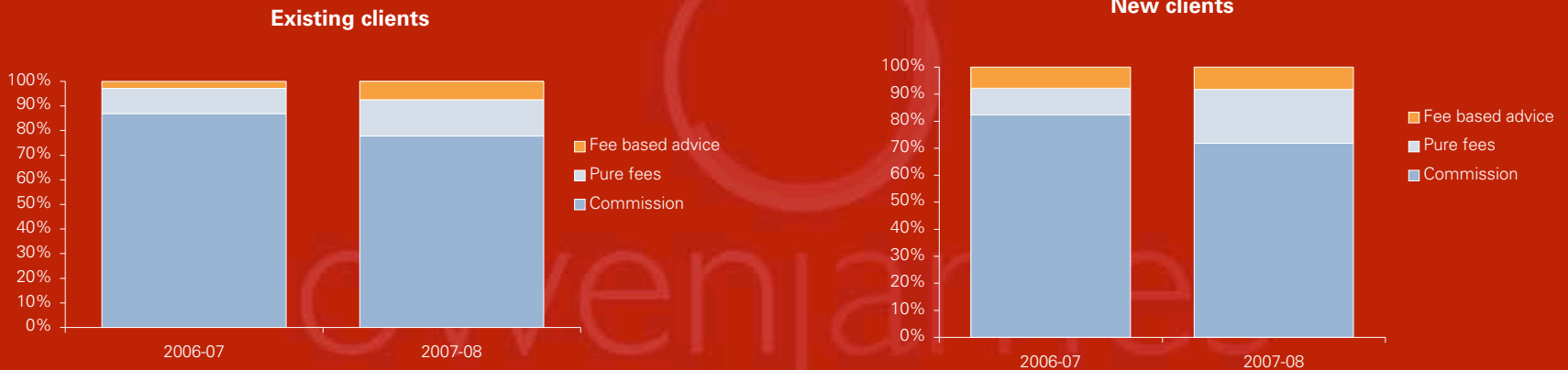


Fee-based models are generating greater gross margins, rather than the traditional revenue models. The pure fee model on the left is a slight red herring as it is suspected they have only just changed their business model.

New clients are more readily open to pay fees rather than commission.

# Survey results

## Revenue mix - comparative results

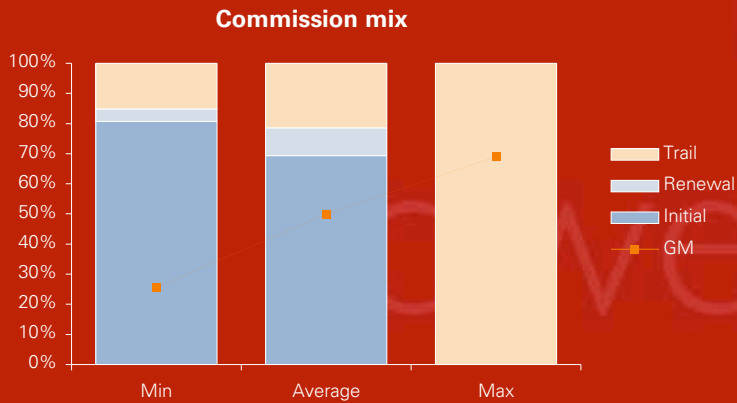


Increasingly existing clients are moving to fee based advice (an overall increase of circa 10%)

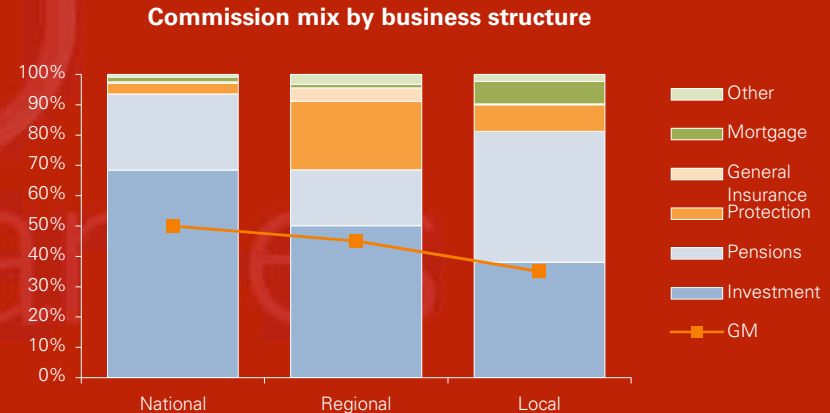
Increasingly new clients are moving to fee based advice (an overall increase of circa 12%)

# Survey results

## Business and commission mix



Trail is king - a clear indication that trail commission is generating higher gross margins, and initial commission is having an opposite effect on profitability.



Investment commission and focus is key - national firms are writing higher volumes of commission through investment business and do not have such a diverse spread (by commission generated) of product mix. As a result are generating higher gross margins.

Note: (a) For min and max columns, two IFAs with below and above average gross margin ratios respectively have been chosen, excluding outliers  
 (b) Where the chosen min & max IFAs have incomplete answers, an appropriate alternative IFA is used  
 (c) A filtered sample of 60 responses was used

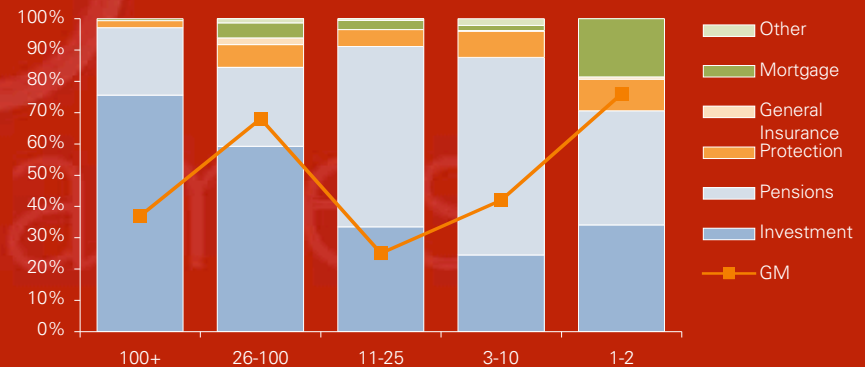
# Survey results

## Business and commission mix

Commission mix by gross turnover



Commission mix by number of RIs

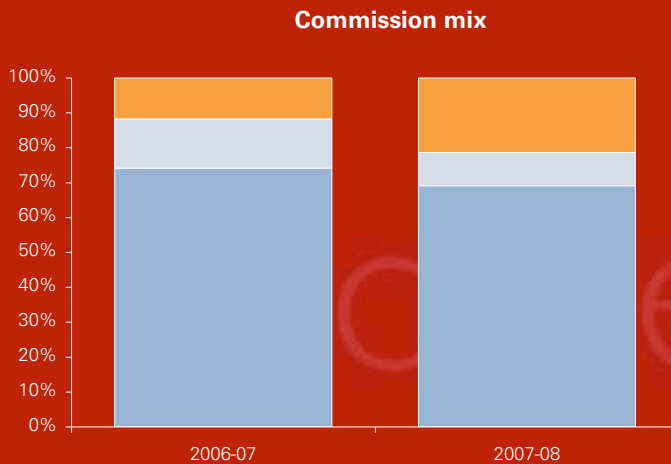


Larger firms with higher turnover and greater numbers of RIs tend to have a far greater focus on writing investment business.

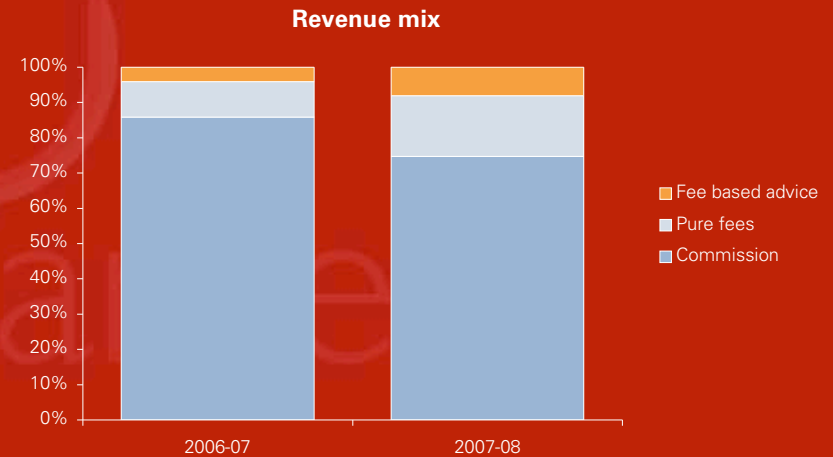
The spike gross margin for IFAs employing 26-100 RIs, can be explained by the fact that these IFAs are investing far less in training their RIs up to IFP level. As a result the revenue generated per RI for these firms is much higher in the short term (please see pg 24-25 for more details).

# Survey results

## Commission and revenues mix - comparative results



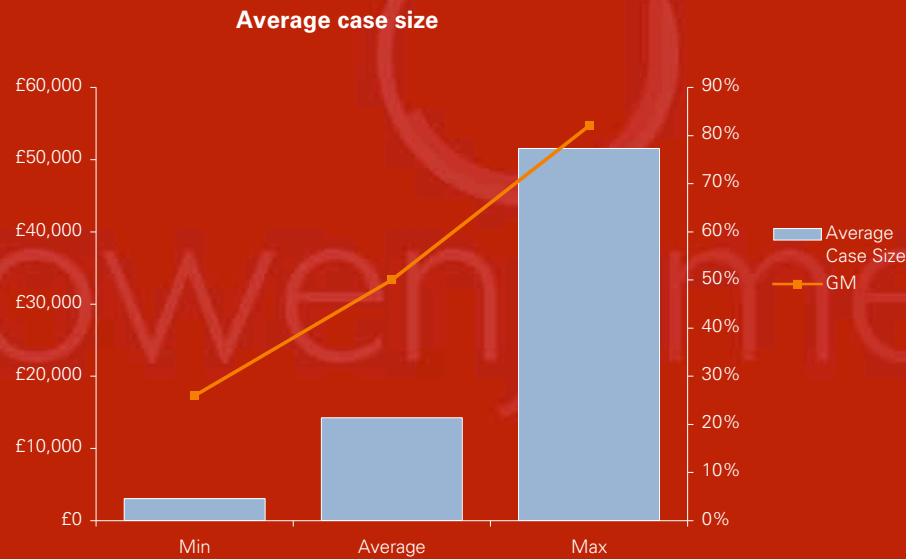
Trail is king - increasingly business models are moving from renewal and initial to trail (an increase of circa 43%).



Fees breakthrough - increasingly business models are moving from charging commission to charging fees (an increase of circa 46%).

# Survey results

## Contribution average case size



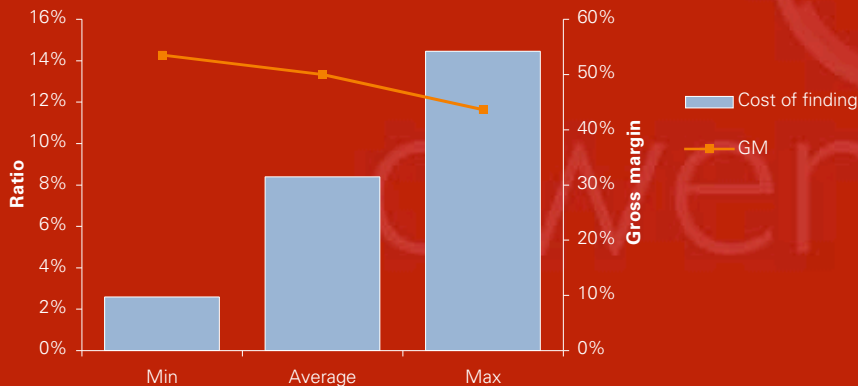
Predictably, the larger the average case size for a firm, the higher the gross margin.

Note: (a) For min and max columns, two IFAs with below and above average gross margin ratios respectively have been chosen, excluding outliers  
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(c) A filtered sample of 60 responses was used

# Survey results

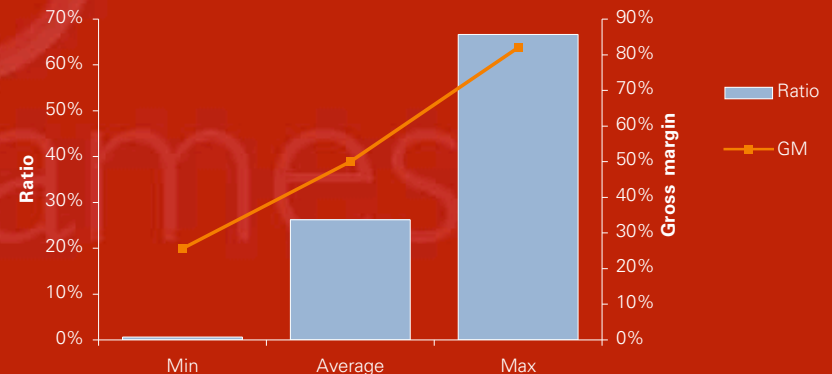
## Cost of finding customers and administration costs

Cost of finding customers as % of total costs



Beware the cost of sourcing new clients - the greater your cost of finding new clients as a percentage of total costs, the lower your gross margin.

Administration cost as a % of RI costs

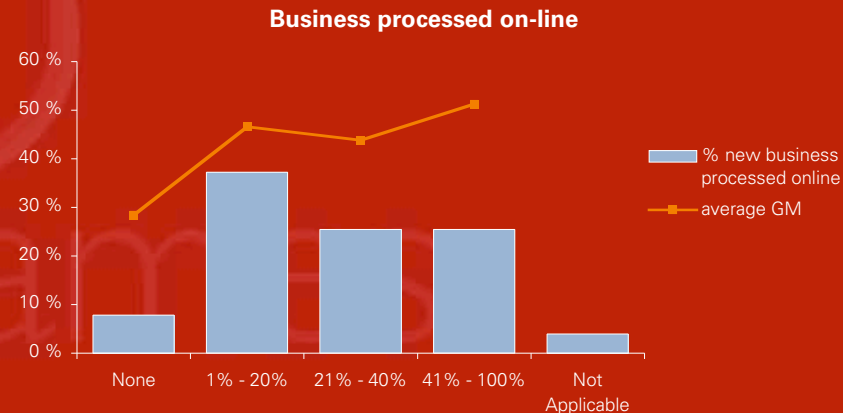
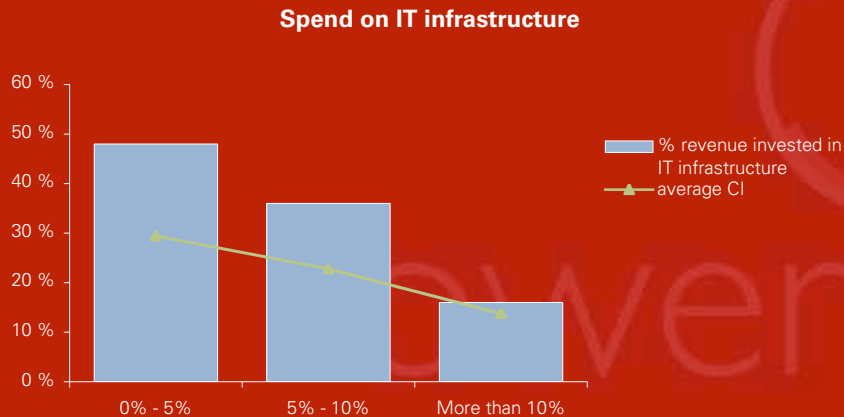


Investing in administration for your RIs pays off - the greater your administration costs per RI, the higher your gross margin.

Note: (a) For min and max columns, two IFAs with below and above average gross margin ratios respectively have been chosen, excluding outliers  
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# Survey results

## Spend on IT infrastructure and on-line processing

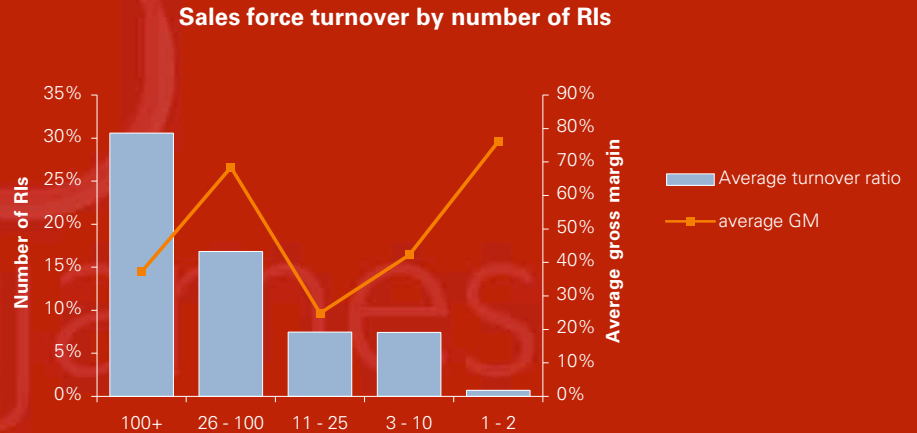
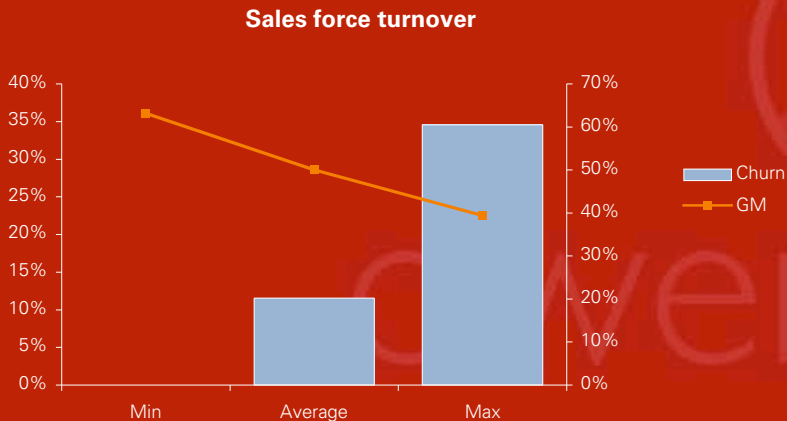


Investing in IT infrastructure drives efficiency (ie a lower cost/income ratio).

On-line growth - the more business processed on-line, the higher the gross margins.

# Survey results

## Sales force turnover



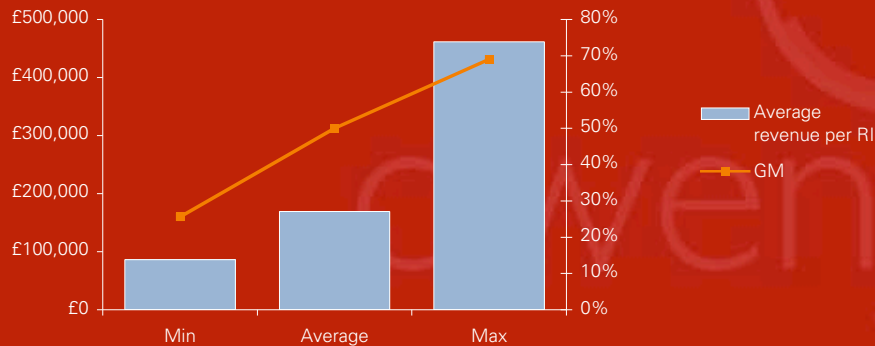
Staff retention is key - increased churn of staff leads to reduced gross margins.

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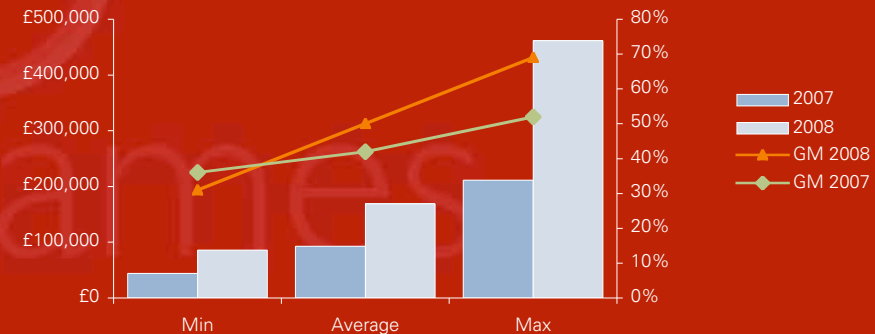
# Survey results

## Average revenue per RI

Average revenue per RI



Average revenue per RI, comparative



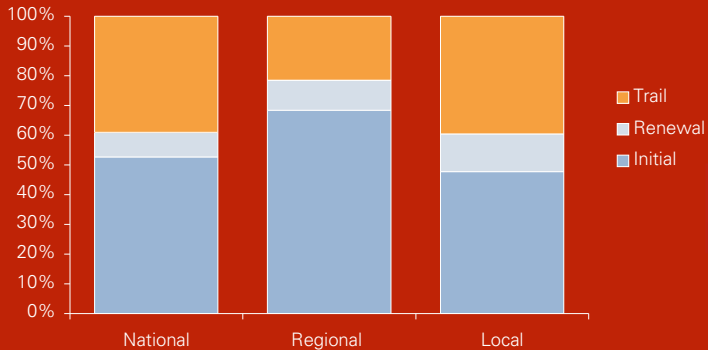
On average an RI is typically generating a revenue of circa £160K, with the highest generating a revenue of £460K. The greater the productivity of the RI, the higher the company's gross margin

Productivity on the increase - Over the past year, RIs have typically doubled the revenue they generate on average, and as a result increased gross margins.

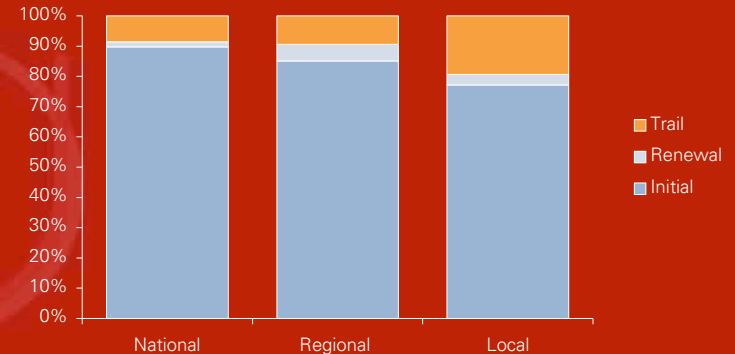
# Survey results

## Revenue split by clients

Revenue from existing clients by business structure



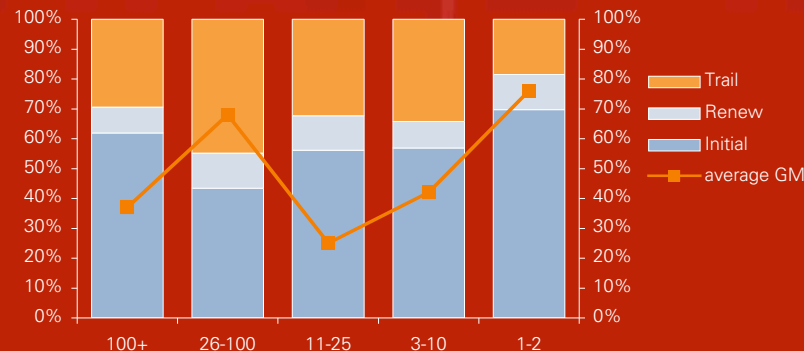
Revenue from new clients by business structure



Overall, IFAs have experienced 43% increase in trail within their commission mix over the last year. Nationals and Locals are currently the 'trail' blazers generating circa 40% from of their commission mix from trail (from existing clients).

Surprisingly, Nationals (closely followed by Regionals) generate least revenue through trail from new clients (only 8%), with local generating 20% of their commission mix through trail.

Revenue from existing clients by number of RIs



# Survey results

## RI costs by business structure and gross turnover

RI costs by business structure



RI costs by gross turnover

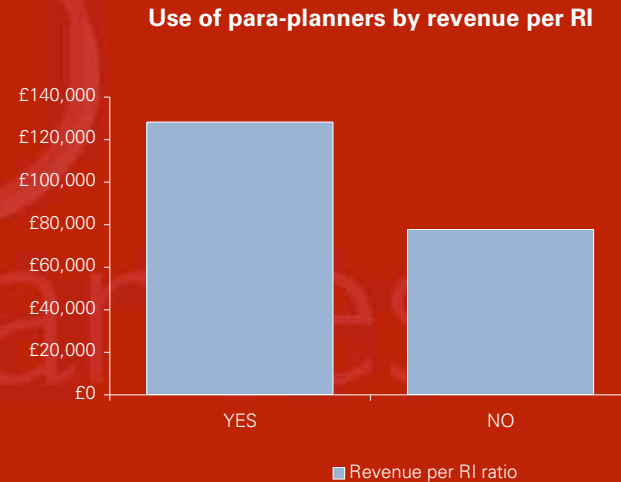
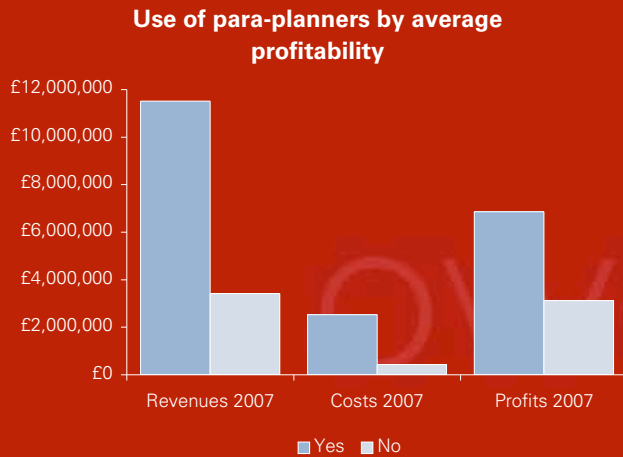


It pays to be employed by a Regional IFA - Typically those models which pay a higher % as base salary rather than commission, incur much higher RI costs. The average cost per RI is almost double at a Regional (£125K) as apposed to a local or national.

Victims of their own success - those firms which generate higher turnovers, typically incur much higher RI costs. Much of this is undoubtedly through commission.

# Survey results

## Use of para-planners

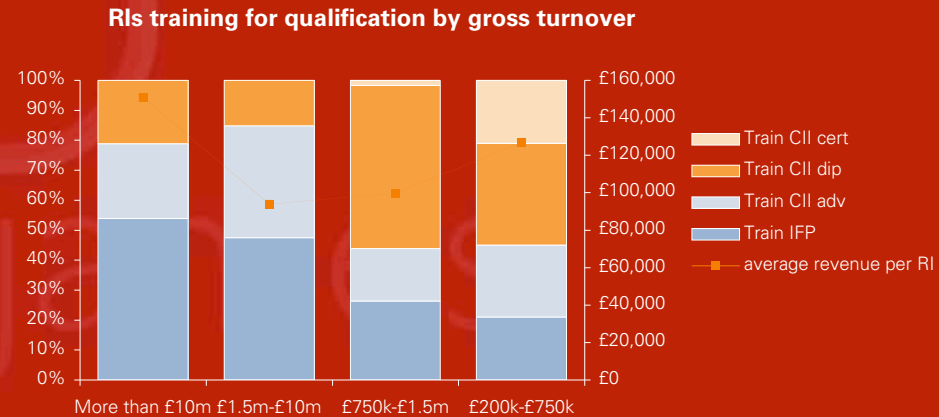
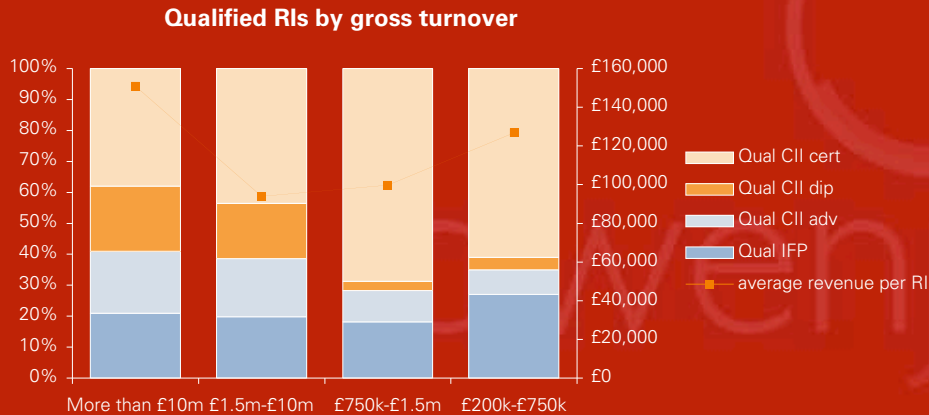


Para-planner... it's a no brainer - the cost of using para-planners is far outweighed by the increase in revenue generated and ultimately profitability (an increase of 100%)

The use of para-planners increase the revenue generated per RI by almost 40%

# Survey results

## Qualification by gross turnover



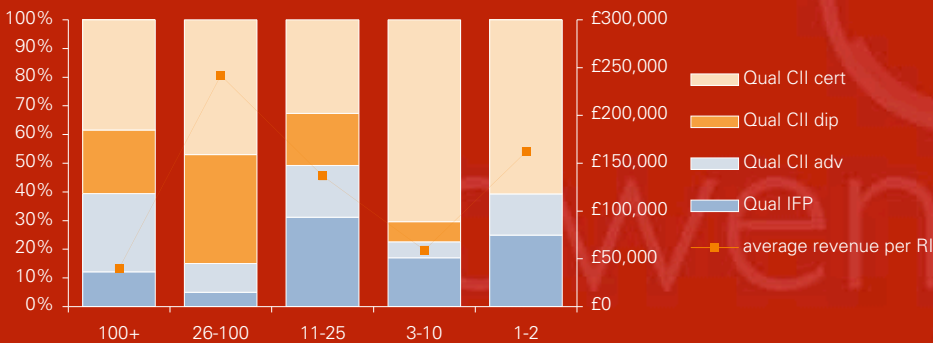
Training pays - those RIs that have been trained up to a higher level will generate higher revenues.

There is clearly a move from the firms generating the greatest turnovers, to train their staff up to the highest level as quickly as possible.

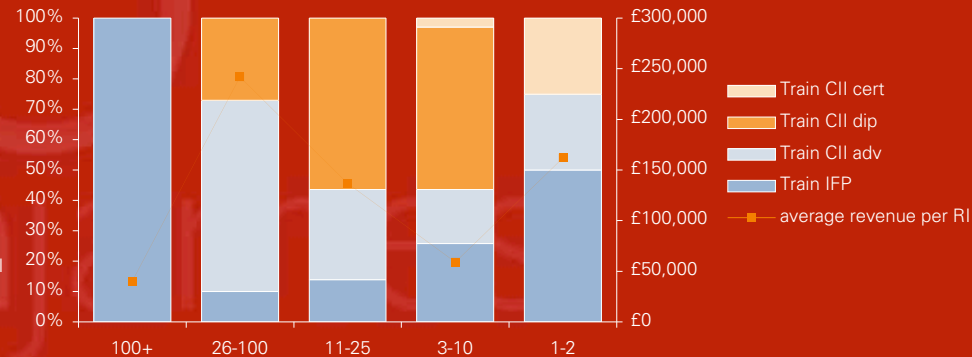
# Survey results

## Qualification by number of RIs

Qualified RIs by number of RIs



RIs training for a qualification by number of RIs



A short term loss for a long term gain – clearly training RIs up to IFP level has a negative effect on productivity in the short term (ie average revenue generated per RI). This is undoubtedly due to the time spent investing in their future.

There is a strong focus amongst the large national firms with over 100 RIs to train all their RIs up to IFP level

# Conclusions



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- **What are the value drivers for IFA business models:**
  - **recurrent income / fees (pg 11-13, 15 and 21)**
  - **investments / pensions mix (pg 13-14)**
  - **higher case size (pg 16)**
  - **use of technology (pg 17-18)**
  - **Investment in administration for RIs (pg 17)**
  - **low cost client acquisition (pg 17)**
  - **RI productivity / churn (pg 19-20)**
  - **use of para-planner (pg 23)**
  - **higher qualifications (pg 24-25)**

# Consolidation and value in the UK IFA Market

Part two

# Does increased profitability increase the value of an IFA?

- Profitability is arguably the most important but not the only valuation metric for IFAs.
- IFA businesses with the largest profit and the highest profit margins generally command premium value.

	Value £m	Revenue £m <sup>(4)</sup>	Profit before tax £m <sup>(4)</sup>	Profit margin %	Revenue multiple
Hargreaves Lansdown	£681m <sup>(1)</sup>	£98.8m	£54.0m <sup>(a)</sup>	55%	6.9x <sup>(b)</sup>
Bestinvest sale to 3i	£165m <sup>(2)</sup>	£21.2m	£9.2m	43%	7.8x
Pantheon Financial sale to Friends Provident	£30m <sup>(3)</sup>	£11.3m	£3.5m	31%	2.7x
Cavanagh	£17m <sup>(1)</sup>	£16.6m	£1.6m	10%	1.0x

Sources: (1) Bloomberg dated 24 June 2008, (2) Press release, (3) Press, (4) Latest annual audited statutory accounts  
 Notes: (a) excludes £29.6m of exceptional expenses for the year ended 30 June 2007, (b) on IPO, market capitalisation of £759m giving an implicit revenue multiple of 10.3 times

# IFA pricing factors

## Current

- Profitability
- Scalable business model
- High proportion of recurring income
- Growth potential
- Strength and ambition of management
- High adviser productivity
- Synergy potential

## Future?

- Level of debt
- Brand
- Demonstrable assets under influence
- Salary / bonus model
- Level of adviser qualification / training
- Proportion of fee income
- Track record of consolidation
- Client base - portfolio size
- Proportion of on-line business

# Is there an active M&A market?

## Buyers of IFAs in 2008

AXA/Thinc - SBJ  
Focus Financial - Greystone  
Intrinsic - Mint  
Lighthouse - Sumus  
Money Portal - Burns Anderson  
Origen (Aegon) - Thackray Williams  
Sanlam - Buckles  
Scott-Moncrieff - William Lawler  
Skipton - Torquil Clark  
Towergate - Albannach Financial  
Towry Law - Hazlems, MLP

## Listed IFAs (Market Cap)

Cavanagh (£17m)  
Clarkson Hill (£3m)  
IFG (€134m)  
Jelf (£124m)  
Lighthouse (£31m)  
Mattioli Woods (£48m)

## IFAs with 'interesting' ownership

AWD (Swiss Life)  
Bankhall (Old Mutual)  
Bestinvest (3i)  
In-Partnership (Private individuals)  
Intrinsic (Sanlam)  
LEBC (BP Marsh)  
Pantheon Financial (Friends Provident)  
Personal Touch (Lloyds Development Capital)  
Positive Solutions (Aegon)  
Simply Biz (Standard Life/minority stake)  
Tenet (four product providers)  
Three Sixty (Standard Life/minority stake)  
Towry Law (Palamon)

# Further consolidation?

- Overly fragmented market.
  - Only need £3 million turnover to get into the top 100 IFAs and £10 million to get into the top 50.
- Bolt-on acquisitions make sense to generate synergies, are relatively easy to integrate and can be funded.
- Larger deals are more difficult and there are few high quality, profitable large scale independent players.
- Need to maintain high standard of compliance to attract purchasers, especially in a market downturn.

# Conclusion



In association with

- There will be further consolidation
- Funding large acquisitions is harder in credit crunched markets.
- Profits, proven scalability, high levels of recurring income and strong management are critical to attracting premium value.
- Improved industry disclosure will facilitate comparability of IFAs which will impact on pricing.

# Owen James - who are we?

- Owen James is a change agent for the financial services industry.
- Owen James organise A Meeting of Minds - a strategic forum bringing together the key influencers from the IFA industry to work through the strategic issues facing the industry and put together an action plan for change.
- If you have any questions please do contact:
  - James Goad, Director
    - T: 01483 861 334
    - E: [jamesgoad@owenjamesevents.com](mailto:jamesgoad@owenjamesevents.com)
    - W: [www.owenjamesevents.com](http://www.owenjamesevents.com)