Perspective from
Franklin Templeton Industry Advisory Services

Embedded advisory and the direct-from-consumer model

New direct-from-consumer model embeds advisory upstream in the capital flow to direct its deployment

December 2024



This is the 10th article[1] in the Future of Investing series, drawing insights from our annual industry-wide survey, The Future of Investing.[2] The Overview summarizing the top 10 key findings can be found here along with a series of articles, each exploring a key finding in more depth.

The lower-touch advisory model of the future is likely to mimic the open banking approach, where data, activities and products are delivered and enabled via application programming interfaces (APIs). These APIs will be exported from today's proprietary platforms and distributed so that advisory can be embedded at the point where an individual receives capital, rather than managing the capital left over for investment after other spending demands have been met.

This would represent a fundamental shift of emphasis from episodic capital raising to placing continuous capital collection occurring wherever, and potentially whenever, the client receives funds. This would reposition advisory, and rather than measuring success by a banker's or advisor's ability to deploy lumps of capital into a commission or fee-generating product, the ability to advise on and influence the direction incoming capital moves the goal to shift toward optimizing the client's wealth and current living.

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> **People are underestimating how big the product strategy nexus to solutions and direct-to-consumer model using technology is going to change the industry in the next five+ years."**
>
> **Wealth Manager**
> >US$500 billion

Capital would be coming into the advisor's hands frequently, often daily, though in small and irregular amounts. The primary goal will be to understand the client's needs and determine the best ways to allocate and utilize incoming funds. The value lies in offering advice on how to optimize the allocation of the investor's money, across its many uses, e.g., spending, savings, philanthropy and investing. In this view, investing is just one of many potential uses for those funds.

Many wealth advisors are already targeting the workplace and looking to offer their services to those in high-potential professions much earlier in their careers before their net worth reaches traditional minimums. The potential to expand such advice to incorporate cash allocation and optimization would be especially well received by those still looking to build wealth and could help them meet their goals more quickly.

Yet, in today's modern society, the workplace is just one channel where individuals receive funds. A growing set of apps and "super-apps" are embedding wallets and facilitating the distribution of capital from payments, sales, subscriptions, promotions, donations, contests and rewards all on a single platform. Some of this is in the form of fiat currency, but some could be other forms of money—such as assets like loyalty points that can be directly exchanged for other assets–without the transfer being intermediated by fiat currency.

Embedding advisory services at the point where investors collect money and the need for advice comes into being places the wealth manager in a position to influence the direction of the flow of capital *upstream* rather than simply competing to manage the capital apportioned to investment well downstream.

> **There's a whole layer of someone's financial life that's untouched. Having real-time resources that can enable allocation and remove complexity. That's where there is exciting disruption."**
>
> **FinTech**
> Innovator

Beginning the journey at this point requires looking through a new lens at the individual's cash management. For lower-touch clientele, a new advisory service that might be called "robo-treasury" may be required. There are four functions that we would expect a robo-treasury service to deliver:

- **Budget and allocate incoming capital:** Monitoring an individual's transaction-level activities, tracking their liabilities and assessing these inputs against their stated goals and objectives should allow for the creation of a dynamic budget. This could inform what percentage of incoming funds would be required to cover operating expenses. It could also indicate how to best divide remaining capital between savings, giving, investing, etc., based on the individual's obligations, profile and behavior. Changes in monitored activity—rather than periodic verbalized aspirations and perceptions—could be used as triggers to reassess the budget and re-balance the investor's flow of money.
- **Optimize payments:** Unlocking and optimizing the value of an individual's entire array of money and money-like instruments would be the second focus of a new robo-treasury offering. Choices for what could be used as payment are expanding. Evaluating the available options and recommending or automatically applying the optimal form at point-of-payment would help extend client's wealth. Such advice could cover what form of money is best to use for specific types of transactions to minimize the impact on their retained buying power, how to earn the most potential rewards—apps already exist today to inform a user which credit cards to use in order to maximize the reward points—or achieve the most benefit from the individual's chosen form of payment, and how various choices may affect the individual's tax situation.

> **Everyone has rushed to get interest on cash, and now cash is an asset. … There needs to be more developed understanding [on the part of users] when it comes to yield, and what it can mean for their portfolio."**
>
> **FinTech**
> Innovator

- **Monitor spending and model impact on goals:** Analyzing transactions at the level of granularity required to optimize payments would also provide a personalized data stream about the investor and their activity. These patterns would not only inform the dynamic budgeting and allocation process but could also be used to provide notifications to the investor (if desired) to nudge their behavior, or at a minimum present them with information showing the impact of certain spending, giving or investing decisions against their stated goals so that they can take more deliberate actions.
- **Maximize buying power:** This final service that could be considered part of a robo-treasury suite is where the model crosses banking services and investing as both offer yield generating products that could be dynamically considered for optimal allocation purposes. This is where "money" as an asset class begins to impact the investor's overall portfolio of assets and tips the scales of required services toward robo-investing.

Survey participants viewed today's robo-investing algorithms as simplistic, limited to shifting allocations between different types of equity and bond exposures. Many saw this approach as insufficient and directed attention to upgrades needed to create a more modern and effective robo-investing solution. To meet shifting portfolio demands, more types of asset exposures need to be included. The increase in interest rates has turned "cash"—and alternate forms of money, money-like and directly exchangeable instruments—into an asset class requiring active investment decision-making. Today, cash is rarely treated as an asset class in robo-investing algorithms, with most advisory platforms simply sweeping any undeployed client balances into a brokerage account or money-market fund.

Growing interest in alternatives is also seen as requiring a more expansive view of what assets belong in the portfolio. Fundraising for alternative assets offered to retail investors reached US$47.6 billion in the first five months of 2024, more than half the US$76.2 billion allocated in the entirety of 2023—on pace to match or exceed 2022's total of US$104.8 billion.[3] Crypto exposures are also becoming more common in wealth portfolios.

> **An outcome has to be emotionally meaningful for it to be important. Asset managers have got to find a way to talk about and demonstrate what they do in terms of life goals."**
>
> **Asset Manager**
> >US$1 trillion

Other upgrades would also be required to enhance robo-investment offerings. Nearly all the portfolios being created today pursue a buy-and-hold asset accumulation strategy aimed at delivering compounding returns over time. Investors have shown their appetite for a broader set of outcomes, some of which may be non-financial. Whereas at one point, portfolios were only expected to deliver on two dimensions—risk and return—that formulation has since extended to three dimensions. Many investors look for their capital to help achieve both their financial goals and align to non-financial values-based outcomes, such as reducing greenhouse gas emissions, increasing board diversity or local issues. Alignment of the investor's portfolio to their everyday life and social identity was seen as another form of "value" that is beginning to take hold, particularly for younger investors.

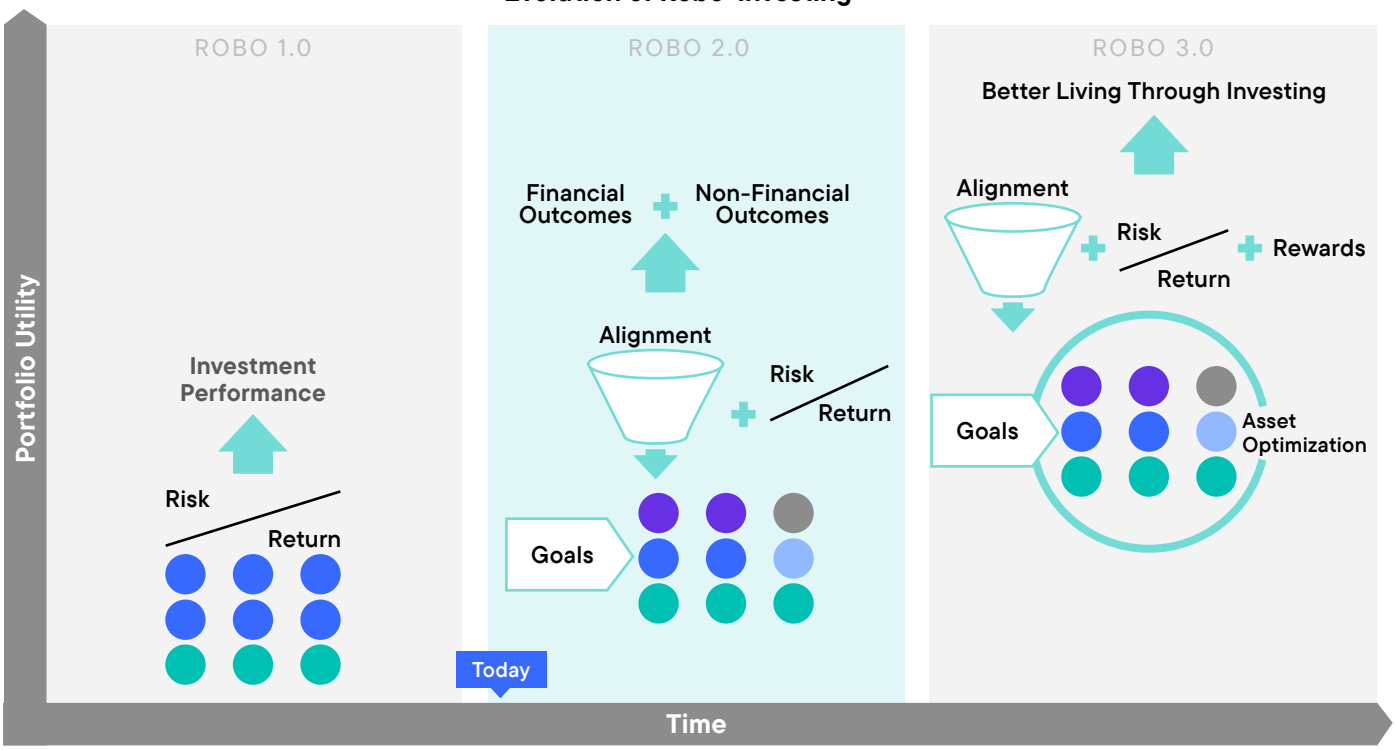
Next Gen's reliance on their mobile phones is extreme and instinctive—they use them not just for one-to-one communication, but as an extension of their identities and as gateways to the world. Connecting to the online communities where these users aggregate and understand their subcultures fosters trust and loyalty. It also helps explain certain investment behaviors that may perplex older investors, such as the "GameStop meme stock" phenomenon.[4] Bank of America found that 86% of investors between 21 and 43 years of age considered the "sentimental value of the investment" as a key consideration. This figure was more than three times higher than the 26% of investors aged 44 and above who considered this important.[5]

> **If intermediaries can structure portfolios to provide higher psychological enjoyment relative to something else, they have achieved a new variation of outperformance for their clients."**
>
> **Manager**
> >US$1 trillion

There is also a new dimension to non-financial outcomes: rewards. This concept of rewards is migrating from the credit card and consumer domains. Today, credit-card holders are already being given options to use their cash back rewards and have them automatically invested into a portfolio—or even a cryptocurrency. Increasingly, individuals are looking for their investments to issue rewards just like their credit cards. Some equity issuers already do this on their own, by treating shareholders like actual owners and offering discounts and rewards on common products and services. For example, investors holding 100 shares or more of Ford Motor Company for a minimum of six months qualify for the company's "Friends and Family" special vehicle pricing.[6]

Future robo-investing offerings may need to be able to automatically track the rewards being offered by portfolio constituents, alert investors about such opportunities, and administer such perks and benefits. In pockets of the world where this already occurs today it is manual and human based. As shown in this exhibit, algorithms can shape investment portfolios to favor investments that align with or offer benefits tailored to an investor's lifestyle, interests or profile.

Evolution of Robo-Investing



Source: Franklin Templeton Industry Advisory Services. For illustrative purposes only. Depictions are theoretical and may not come to pass.

Combining robo-treasury and an enhanced version of robo-investing broadens the scope of what falls under a wealth mandate, considering all aspects of an individual's life, adjusting course based on changing goals and actual behaviors, and informing decisions that individuals are left to determine on their own today without adequate training or insight. In essence, it delivers an algorithm-driven version of a chief financial officer (eCFO) that can focus on each person's activities and needs.

> **“The advisory industry shifted from leading with investing to leading with planning and today everyone is leading with planning, almost to the extreme of life coaching.”**
>
> **FinTech**
> Innovator

> **“The asset managers are becoming wealth managers because they realize that they already have everything they need.”**
>
> **Wealth Manager**
> Innovator

> **“If as an asset manager you’re not thinking about wealth and how to position for it, as well as leveraging the fact that the United States is the model on how everything else is going to be built, then it’s not going to end well.”**
>
> **Asset Manager**
> >US$1 trillion

Delivering these services through an “open advisory” framework would enable wealth service providers to leverage a broader set of third-party partners at the point where individuals receive wealth. Crucially, this approach would grant access to clients and relevant data about their behaviors and assets. Today, wealth managers build dedicated platforms for advisors and bankers. The cost and effort required to assemble the network and technology represents a significant barrier to entry. Shifting to a more “portable” provision of services that could be embedded in other providers’ offerings—and in conjunction with more “portable” portfolios held in cryptographically protected wallets—may on the one hand reduce this competitive moat, but on the other, open up new opportunities.

Existing leaders in the provision of traditional wealth management might be resistant to pursuing the “capital collection” approach and developing a suite of eCFO services. However, newcomers to wealth advisory may find this service-based, automated model appealing. It leverages existing communities and user-bases to lower client acquisition costs and provides a route to embedding relationships with a growing client base. Investment managers, industry consultants and tech platforms may be better situated to pursue this opportunity. Meanwhile, traditional wealth firms may look to deepen their high-touch approach by building a stronger network and more community-based strategy, at the opposite end of the advisory barbell.

Our next, and last, article in this current “Future of Investing” series expands on this and examines the final piece in the future of advisory puzzle: the role of networks and new forms of value generation.

For more information or to request a presentation on the 2024/25 Future of Investing findings, please contact your Franklin Templeton representative or reach us directly at *industryadvisoryservices@franklintempleton.com*.

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Endnotes

1. Discussions in this piece are theoretical in nature and may not come to pass.
2. On an annual basis, Franklin Templeton's Industry Advisory Services team conducts off-the-record, unscripted interviews of leaders across the financial services industry. This year, we were fortunate enough to hear from 85 leading thinkers controlling over US$50.1 trillion of assets under management across the financial services industry about their views on the future of investing between March and September of 2024. Input came from a broad cross-section of the industry—asset owners, private banks, wealth managers, consultants, investment managers, crypto firms, academics, industry leaders and fintech firms. Conversations took place formally as part of free-ranging, qualitative, off-the-record, survey interviews, and informally during one-on-one sessions where the implications and plans for each organization are discussed and explored. Each of these inputs added to an emerging picture of an industry that is changing rapidly and across multiple dimensions. Interviews were conducted globally with about two-thirds of discussions held with leaders of firms based in the United States, and the other third spread between Europe and Asia.
3. Source: Misonzhnik, Elaine. "Alternative Fundraising in the Retail Channel on Track to Top 2023 Volume." Wealth Management. June 24, 2024.
4. The "GameStop meme stock" phenomenon refers to the dramatic surge in GameStop's stock price in early 2021, driven by a coordinated effort among retail investors on social media platforms like Reddit, which led to significant market volatility and highlighted the power of collective investing.
5. Source: "2024 Study of Wealthy Americans." Bank of America. 2024.
6. Source: Farrington, Robert. "Companies That Give Shareholders Perks And Rewards." The College Investor. May 7, 2024.

Curated glossary of relevant terms

Cryptocurrency

Cryptocurrency is a form of digital or virtual currency that uses cryptographic techniques to ensure security, making it nearly impossible to counterfeit or double-spend. Most cryptocurrencies operate on decentralized networks powered by blockchain technology, which is a distributed ledger maintained by a network of computers. Cryptocurrencies typically not issued by any central authority, making them theoretically resistant to government interference or manipulation.

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal.

Companies in the **technology sector** have historically been volatile due to the rapid pace of product change and development within the sector. **Artificial Intelligence** is subject to various risks, including, potentially rapid product obsolescence, theft, loss or destruction of cryptographic keys, the possibility that digital asset technologies may never be fully implemented, cybersecurity risk, conflicting intellectual property claims, and inconsistent and changing regulations.

Blockchain and cryptocurrency investments are subject to various risks, including inability to develop digital asset applications or to capitalize on those applications, theft, loss or destruction of cryptographic keys, the possibility that digital asset technologies may never be fully implemented, cybersecurity risk, conflicting intellectual property claims, and inconsistent and changing regulations. Speculative trading in bitcoins and other forms of cryptocurrencies, many of which have exhibited extreme price volatility, carries significant risk; an investor can lose the entire amount of their investment. Blockchain technology is a new and relatively untested technology and may never be implemented to a scale that provides identifiable benefits. If a cryptocurrency is deemed a security, it may be deemed to violate federal securities laws. There may be a limited or no secondary market for cryptocurrencies.

Digital assets are subject to risks relating to immature and rapidly developing technology, security vulnerabilities of this technology (such as theft, loss, or destruction of cryptographic keys), conflicting intellectual property claims, credit risk of digital asset exchanges, regulatory uncertainty, high volatility in their value/price, unclear acceptance by users and global marketplaces, and manipulation or fraud. Portfolio managers, service providers to the portfolios and other market participants increasingly depend on complex information technology and communications systems to conduct business functions. These systems are subject to a number of different threats or risks that could adversely affect the portfolio and their investors, despite the efforts of the portfolio managers and service providers to adopt technologies, processes and practices intended to mitigate these risks and protect the security of their computer systems, software, networks and other technology assets, as well as the confidentiality, integrity and availability of information belonging to the portfolios and their investors.

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