Schroders

Schroders 2022 UK Financial Adviser Annual Survey

Adviser Report

Marketing material for professional clients only

Welcome

Our UK Financial Adviser Annual Survey series aims to deliver a range of insights that can help advisers with their planning.

It covers a wide variety of issues from the current challenges facing financial advisers, to the way their strategic thinking is developing and the direction of travel for the industry.

This report sets out the key findings from the November 2022 Adviser Survey.

This was completed by over 400 advisers from more than 350 different firms, providing a broad survey of views from across the financial advisory community.

We hope that you find the report informative and useful.

Doug Abbott
Head of UK Intermediary

Gillian Hepburn
Head of UK Intermediary Solutions

Contents

How are clients feeling about investing?

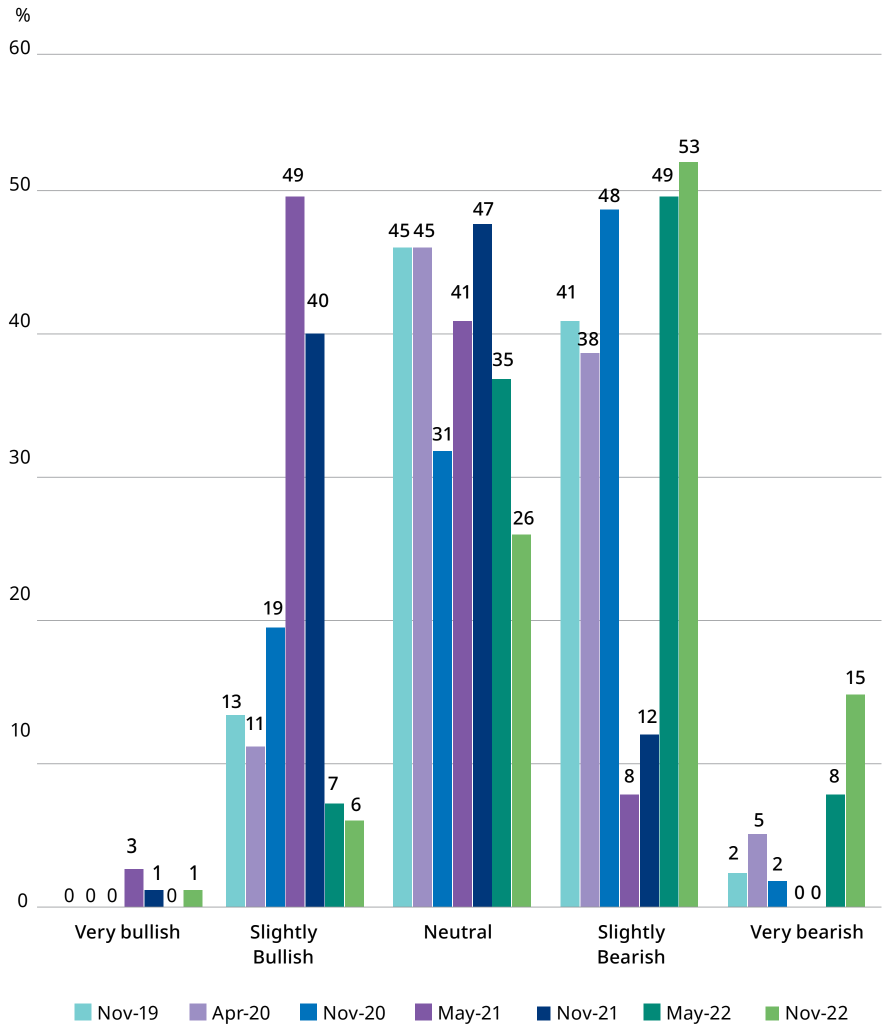
7%
of advisers' clients are bullish

68%
of advisers' clients are bearish

It comes as no real surprise that the sentiment of advisers' clients has worsened since our last survey in May 2022 and is now more bearish than at the height of the Covid crisis. 68% of clients are now bearish, up from 57% in May this year.

There has been a massive swing in sentiment since this time last year when 41% of advisers' clients were bullish and only 12% were bearish. This reflects a marked deterioration in the economic and market landscape. Slowing growth, soaring inflation, increasing energy prices, sharply higher interest rates, and heighted geopolitical tensions following Russia's invasion of Ukraine, have all taken their toll.

Figure 1: How would you describe the sentiment among most of your clients?



The impact of the cost of living crisis

53%

of advisers reported that some of their clients had adjusted their plans due to the cost of living crisis

63%

of advisers ranked capital loss as the greatest concern for clients

The survey suggests that the cost of living crisis is having an impact on many people's savings and investment plans. In May 2022, 69% of advisers told us that they expected that some of their clients would have to adjust their plans as a result of the cost of living crisis. In November, 53% of advisers reported that some of their clients have now adjusted their plans and we would expect this to continue to trend higher as winter bites, mortgage rate increases are felt and Christmas comes at a cost for many.

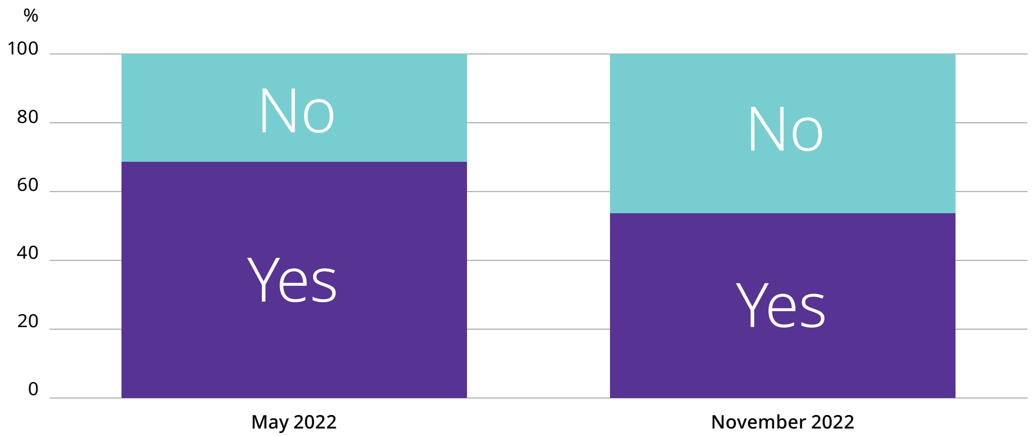
We asked advisers what their clients were currently most concerned about - capital loss, inflation, generating sufficient income or rising interest rates.

63% of advisers ranked capital loss as the greatest concern for clients from this list, with an additional 15% ranking this in second place.

As most advised clients are at the stage of life where they have built up assets which they are relying on to fund their retirement, this is perhaps unsurprising. Falling capital values at this stage of life can jeopardise plans and have long-reaching knock-on effects, particularly when a drawdown strategy is in place to provide retirement income. Inflation, which erodes the purchasing power of accumulated assets was generally ranked next as a concern, followed by generating sufficient income.

Rising interest rates were generally seen as less of a concern. This may be because many advised clients are at the stage of life when they will have paid off much or all of their mortgage and in addition to investments may have built up cash savings, which will benefit from higher rates.

Figure 2: Have some of your clients adjusted their investment plans as a result of the cost of living?



Market trends

46%
of advisers have increased client holdings in cash

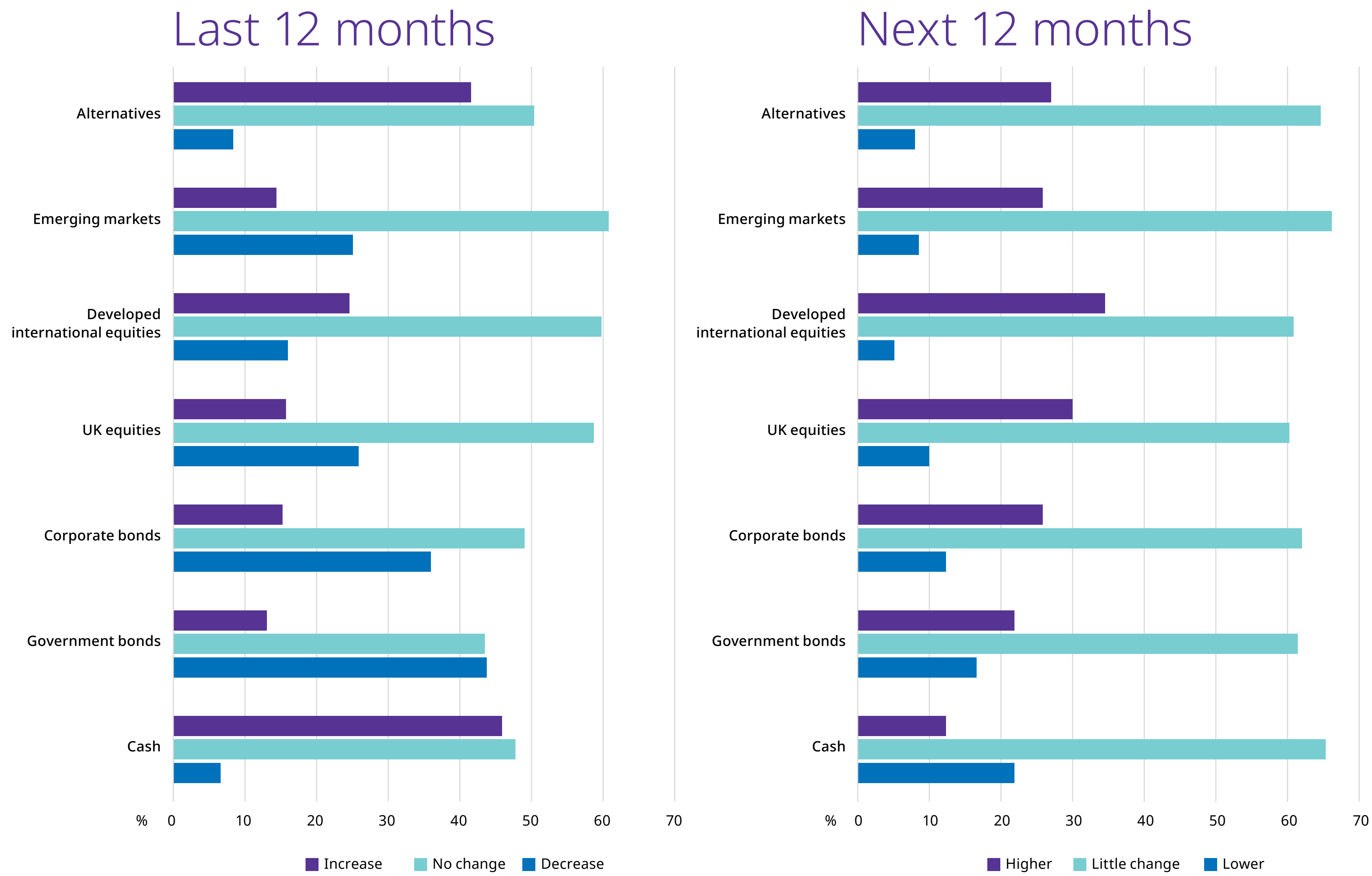
41%
of advisers have increased client exposure to alternatives

Against a background of poor sentiment and falling values across both equity and bond markets, advisers with a tactical asset allocation approach have positioned client portfolios more defensively over the past twelve months. Most notably, 46% of advisers say that they have increased client holdings in cash, while only 6% have reduced cash exposure. Advisers, on balance, have significantly cut holdings in government bonds and corporate bonds and have also reduced exposure to UK equities and emerging market equities.

This year's tandem fall in equity and bond markets has focused attention on whether a traditional portfolio structure, relying on diversification between equities and bonds to reduce risk across the market cycle, is still fit for purpose. The search for diversifying assets that can provide investors with some additional protection in challenging market conditions has led to increasing appetite for alternative investments with 41% of advisers increasing exposure to the asset class compared to 9% reducing exposure.

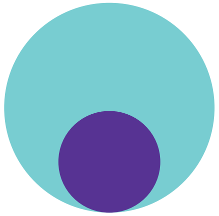
Forward looking asset allocation intentions suggest advisers think that markets may stage something of a recovery over the next 12 months. Advisers, on balance, expect to reduce cash holdings slightly and increase exposure to risk assets across the board, with the greatest increase in developed international equities. However, many see little change, reflecting the many uncertainties that remain.

Figure 3: Change in client asset allocation over the last 12 months and expectations for the next 12 months

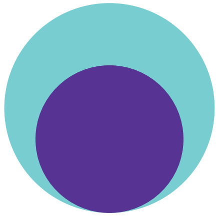


Longer term expectations

20%
of advisers expect equity and bond markets to be higher than historical averages over the next 5 years



57%
of advisers expect higher levels of disruption related to changes in the environment, including climate change, over the next 5 years



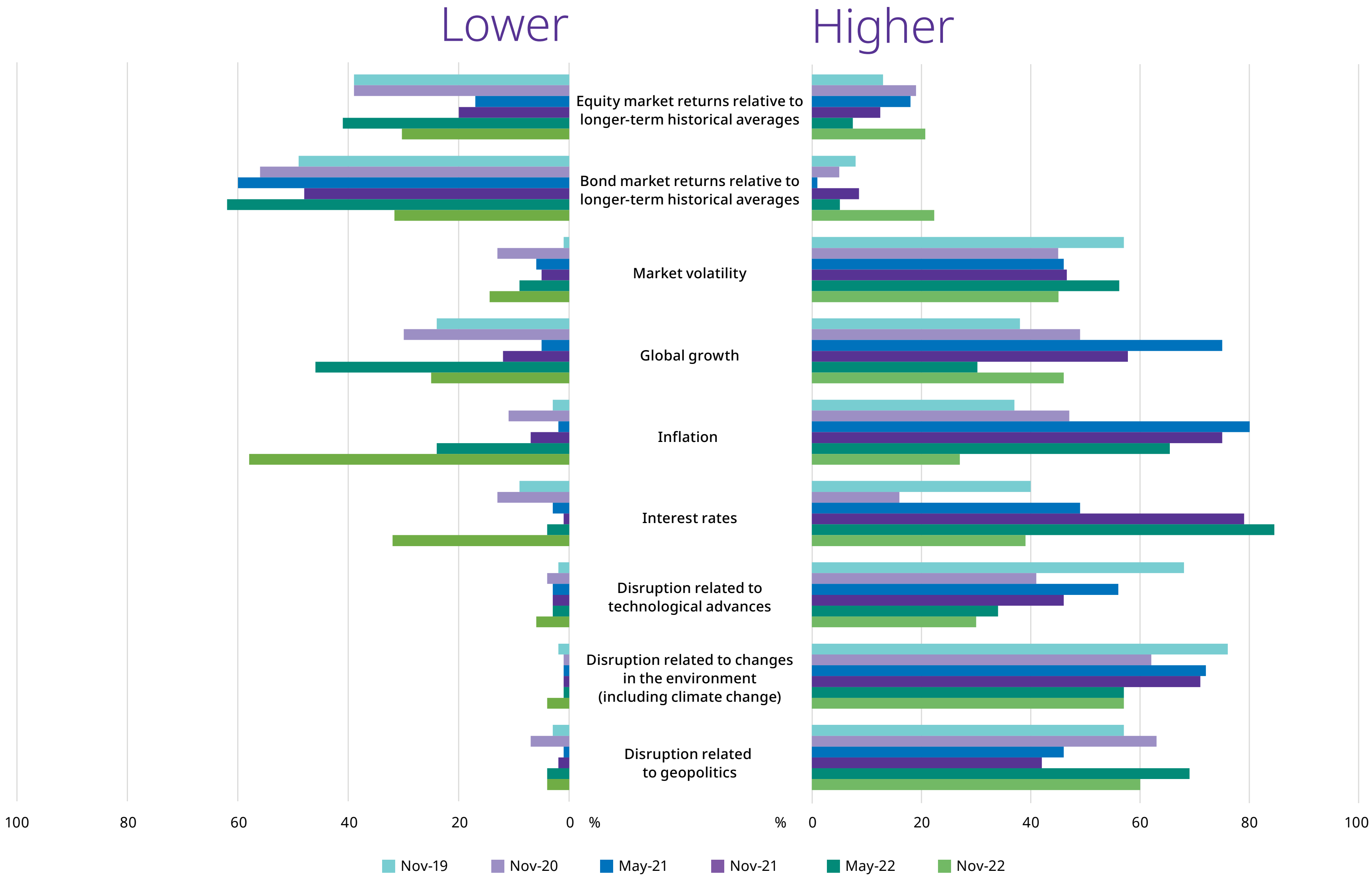
Looking further ahead, advisers' sentiment on prospects for equity and bond market returns over the next five years has improved since May.

Overall, sentiment on equities and bonds is still far from bullish, with more advisers still expecting returns to be lower rather than higher than historical averages. However the percentage of advisers with this view has fallen, and for bonds by a significant margin, down to 32% from 62%.

Over 20% of advisers now expect equity and bond market returns to be higher than historical averages over the next five years, the highest figures since November 2019.

Advisers on balance continue to expect that markets will remain volatile, although the percentage expecting higher volatility has dropped back to 45% from 56% in May.

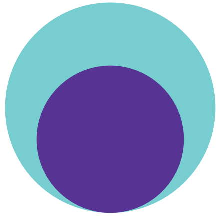
Figure 4: How would you expect the following to trend over the next 5 years?



Longer term expectations

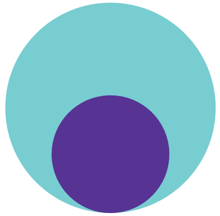
58%

of advisers expect inflation to come down over the next five years



32%

of advisers expect interest rates to trend lower over the next five years



On balance, advisers expectations for growth over the next five years have turned positive. 46% of advisers expect higher global growth while 26% expect lower growth, a reversal of their expectations in May when 46% expected lower growth and 30% higher growth.

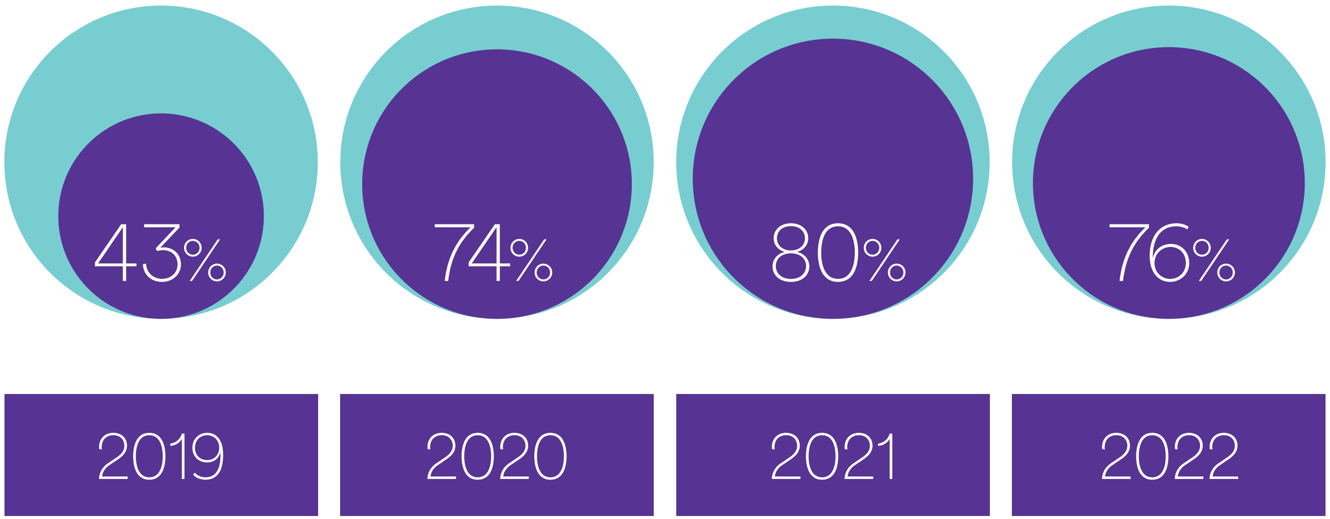
Expectations for inflation going forward have also reversed. 58% of advisers now expect inflation to come down over the next five years while in May, 65% of advisers expected higher inflation. Perhaps we could be close to reaching peak inflation?

Expectations for the path of interest rates over the next five years have also shifted. In May, 85% of advisers expected interest rates to trend higher. Now only 39% expect this, while 32% expect rates to trend lower. Could we also now be close to reaching peak interest rates?

Advisers expect that disruption will remain a major theme in markets. Given events of this year it's no surprise that 60% of advisers expect a higher level of disruption related to geopolitics. With extreme weather events a regular fixture in the headlines, it's also unsurprising that 57% expect higher levels of disruption related to changes in the environment, including climate change. These appear to have become dominant areas of concern, with the percentage of advisers expecting higher disruption related to technological advances now standing at 30%, down from 68% in November 2019 which is a significant shift.

Sustainability

Percentage of advisers specifically considering sustainability and ESG factors as part of their fund selection process:



The survey provides evidence that advisers and their clients are becoming ever more aware of the link between sustainability and investing and are increasingly looking to ensure that their views on sustainability are reflected in portfolios.

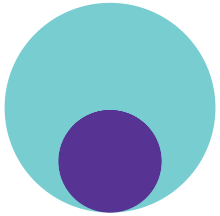
76% of advisers now specifically consider sustainability and ESG factors as part of their fund selection process, compared to 43% in 2019.

When asked about their organisation's views on investing, 56% of advisers expect an investment manager to consider sustainability/ESG factors as part of investment decision making, to minimise risk and maximise returns. This compares to only 8% who say they prioritise maximising returns and minimising risks entirely over the sustainability of investments.

Client demand for sustainable investment options

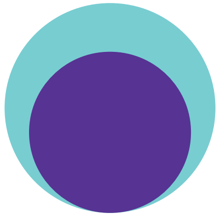
24%

of advisers report that more than a quarter of clients now ask to incorporate ESG factors when investing



50%+

of advisers report that clients have discussed their views on investing in fossil fuels and the transition to renewable energy sources in light of the war in Ukraine



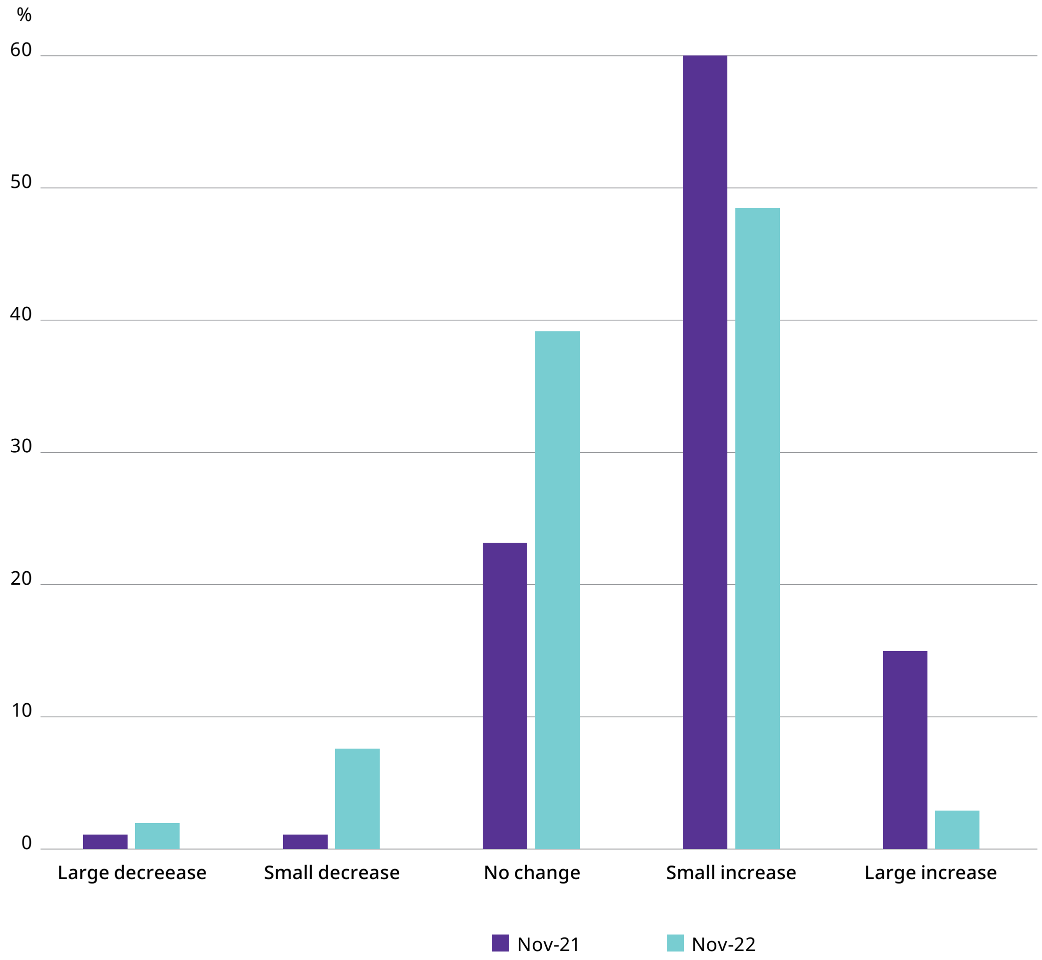
Advisers' clients have begun to explicitly specify that their investments should reflect ESG factors in some way. However, the survey suggests that this trend may have slowed slightly.

51% of advisers have seen an increase in the number of clients asking for sustainable investment options over the past 12 months. This is down from 75% in November 2021. 24% of advisers report that more than a quarter of their clients now ask to incorporate ESG factors when investing. This is up sharply from 14% in 2020 and 9% in 2019. However it is again below the 29% figure reported this time last year.

It's possible that a combination of difficult market conditions and the increasing strain on household finances may have pushed sustainability back a little in the list of the concerns that clients have relating to their investments.

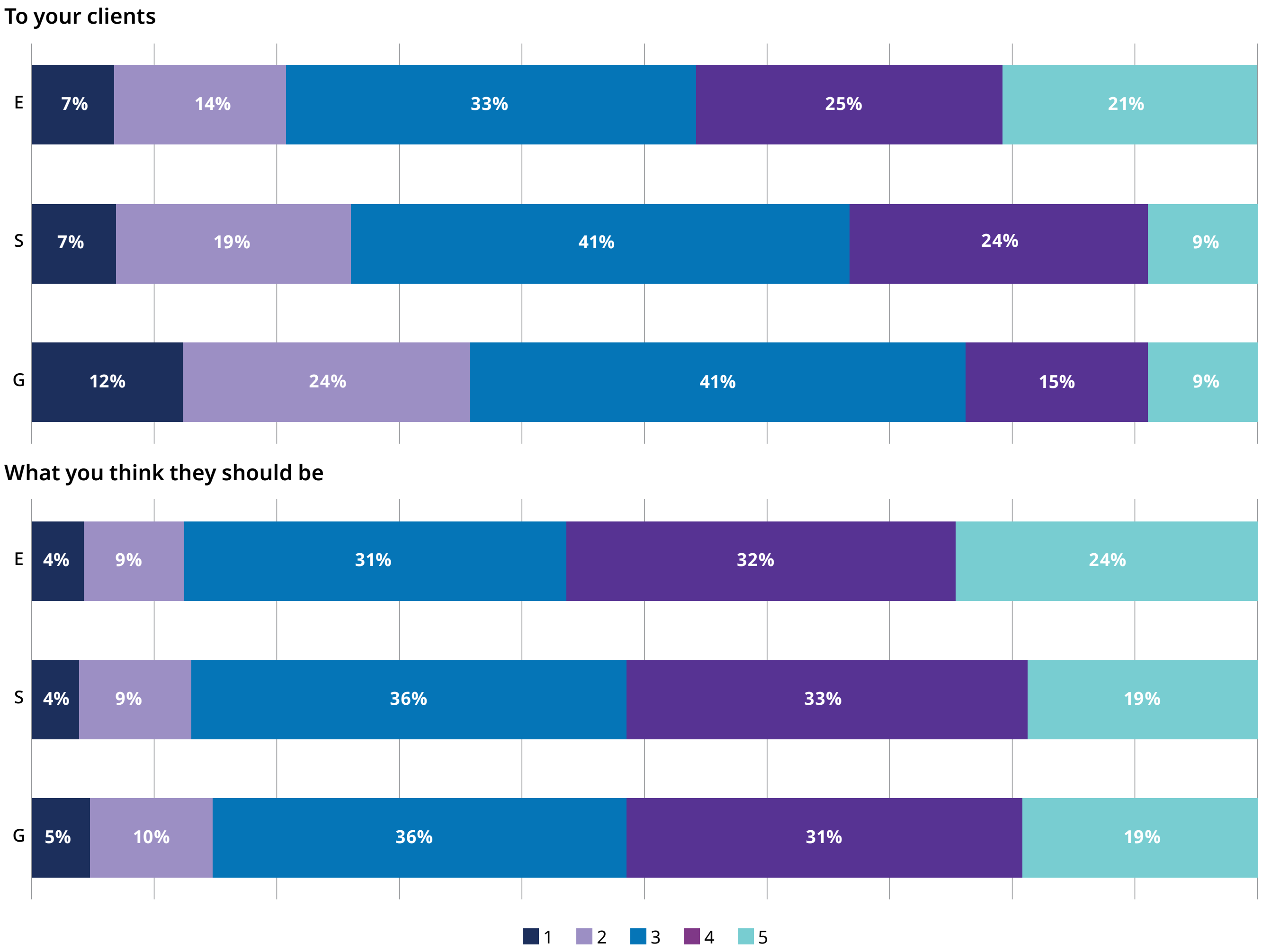
However the survey suggests that many are keenly aware of the sustainability related issues linked to recent headline events and the tension between these issues and their sustainability beliefs. More than half of advisers report that clients have discussed their views on investing in fossil fuels and the transition to renewable energy sources in light of the war in Ukraine, and 43% say that clients have discussed the inclusion of armaments' related investments in their portfolios.

Figure 5: How has the number of clients asking for sustainable investing changed over the past 12 months?



Relative importance of E, S and G when investing

Figure 6: On a scale of 1 to 5 (with 1 being least important, 5 being most important), how important are the E, S and G factors of ESG when selecting an investment?



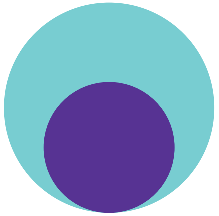
Advisers report that environmental factors are still rated as the most important of the ESG factors by their clients when selecting an investment.

Advisers themselves maintain a fairly balanced view of the importance of each of the ESG factors.

Educating clients about sustainability

40%

of advisers would like more educational support on sustainable investing

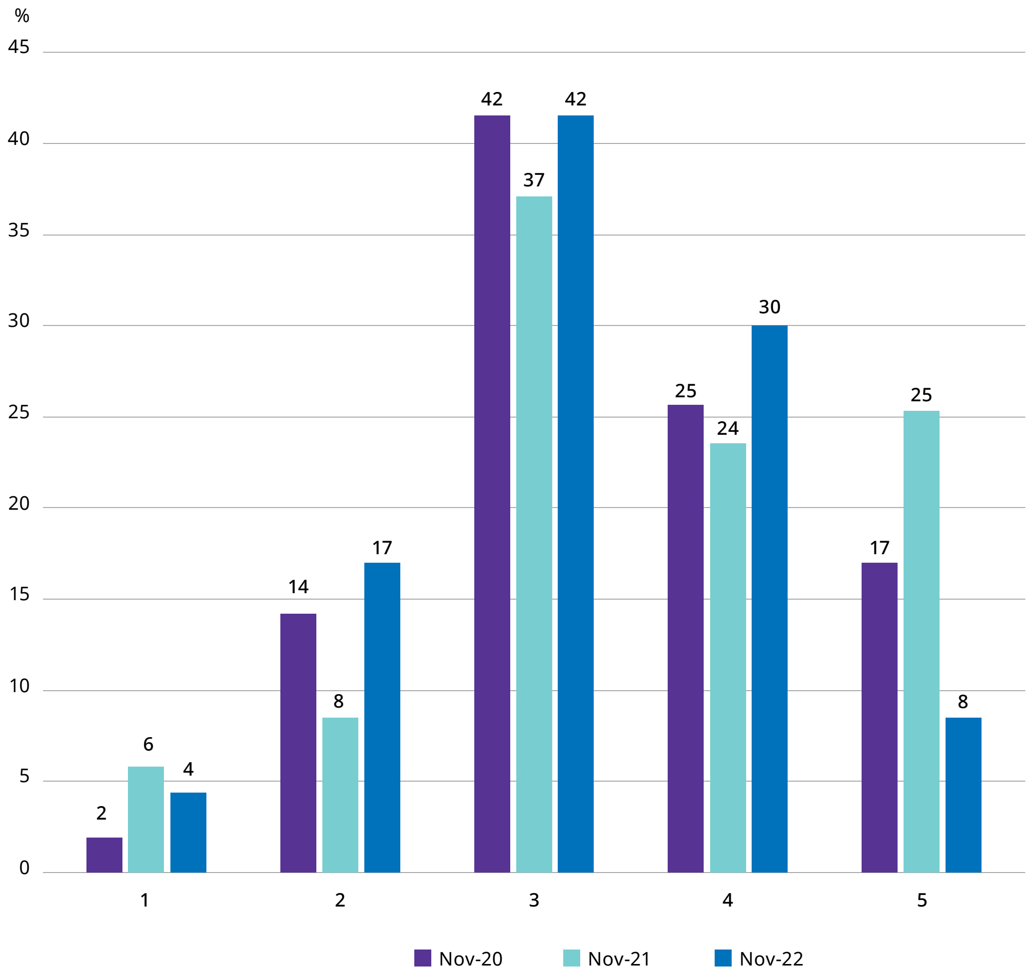


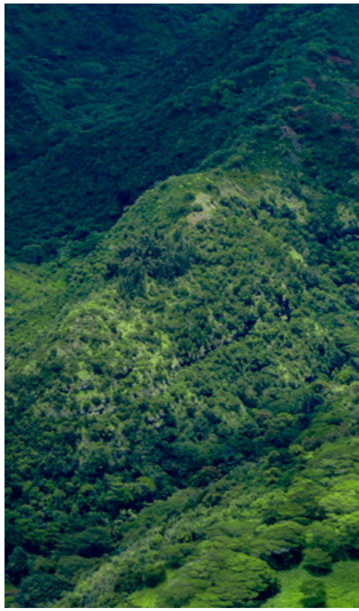
Confidence in talking to clients about sustainable investing has dropped back, with 63% of advisers rating this as middling or below on a scale of 1-5 compared to 51% in 2021. The percentage of advisers who are very confident talking about sustainable investing has fallen from 25% to 8%.

Advisers have increasingly come to view sustainability as a crucial factor in investment decision making and sought education from investment managers with 40% saying that they would like more support.

However with a range of data providers and lack of consistent terminology, this can often be a challenge. At the time of the survey, the FCA had issued the consultation paper on labelling which will require significant change for investment managers and client suitability which may have been reflected in the responses.

Figure 7: Rate your level of confidence about talking to clients with consistency about the terminology, regulation, integration and behavioural implications of sustainable investing on a scale of 1 (very low) to 5 (very high)

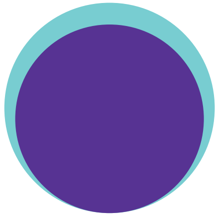




Active engagement on sustainability

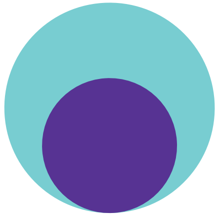
89%

of advisers think that the last two years has reinforced the importance of active management



37%

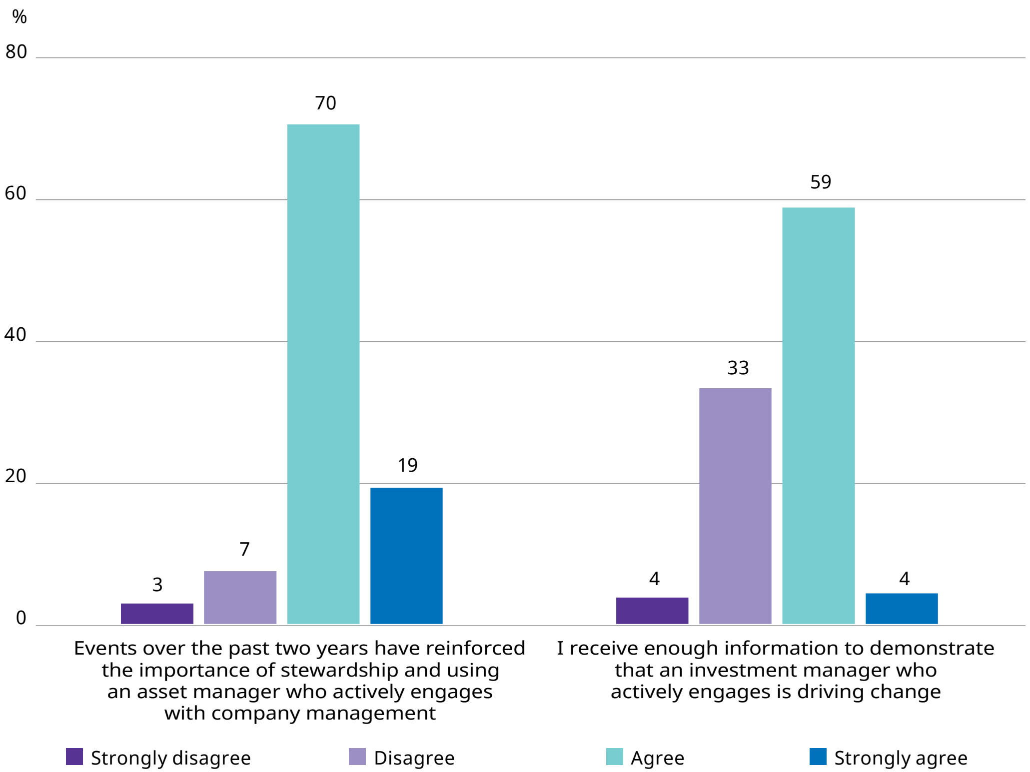
of advisers do not think they receive enough information to demonstrate that an investment manager actively engages is driving change



89% of advisers think that events over the past two years have reinforced the importance of stewardship and using an asset manager who actively engages with company management.

However, 37% of advisers do not think they receive enough information to demonstrate that an investment manager who actively engages is driving change. This is a crucial point and investment managers not only need to report on the number of engagements but also the outcome of these.

Figure 8: To what extent do you agree with the following statements:



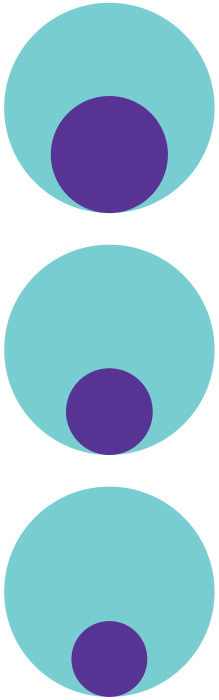
Adviser business challenges

Top three adviser concerns:

32%
Regulation

17%
Succession planning and/or exit strategy

14%
Servicing existing clients

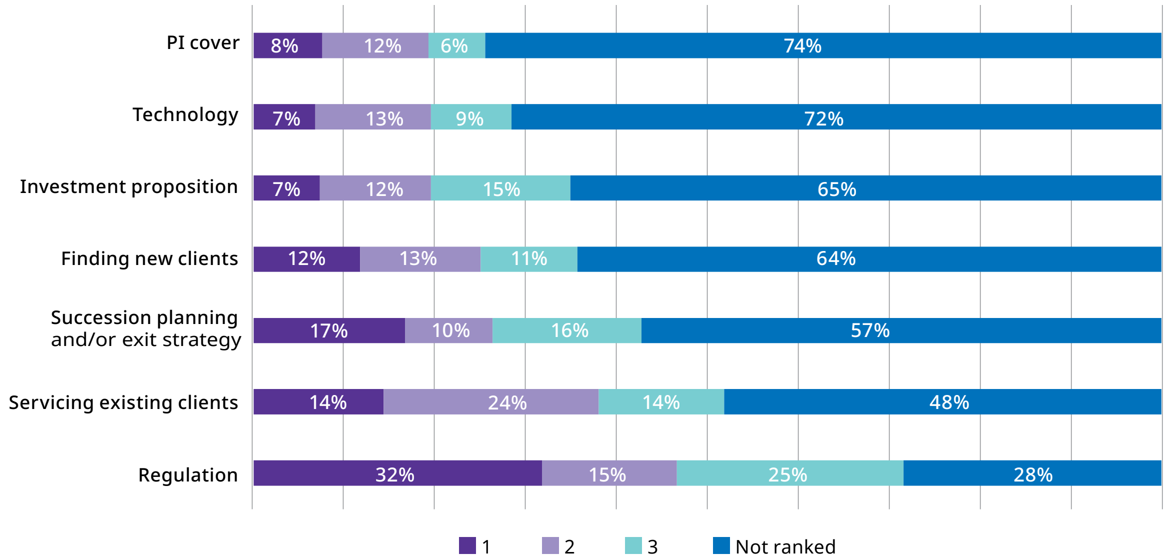


As with previous surveys, regulation is the key concern for advisers. This is hardly surprising given the current focus on planning for The Consumer Duty and the ongoing consultation on labelling for sustainable products.

Servicing existing clients is also high on the list. It's likely than advisers will be keen to spend more time with clients explaining the market challenges identified earlier in this report and encouraging them where possible to remain invested. Succession planning or finding an exit strategy also continue to feature against a backdrop of significant M&A activity in the market and the plethora of Private Equity (PE) companies looking to acquire advisory businesses.

Over the last few years, PI cover featured near the top of a list of advisers' concerns and is now at the bottom We believe that this continues to be a concern for advisers but the relative importance of this has simply shifted.

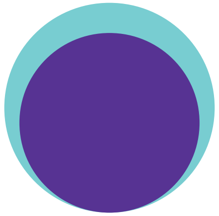
Figure 9: From the following list, rank the 3 areas you are currently most concerned about relating to your business (1 is greatest concern)



The Consumer Duty and client segmentation

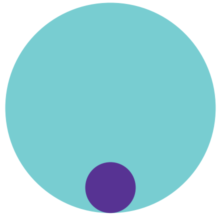
82%

of advisers are not yet fully prepared for The Consumer Duty regulation



6%

of advisers have not started to look at The Consumer Duty regulation



Firms have 12 months from July 2022 to implement the new rules under The Consumer Duty.

At this stage, only 18% of advisers say they are fully prepared for this so 82% have more to do. Worryingly 6% have not started to look at it yet, despite plans having to be finalised by October 2022.

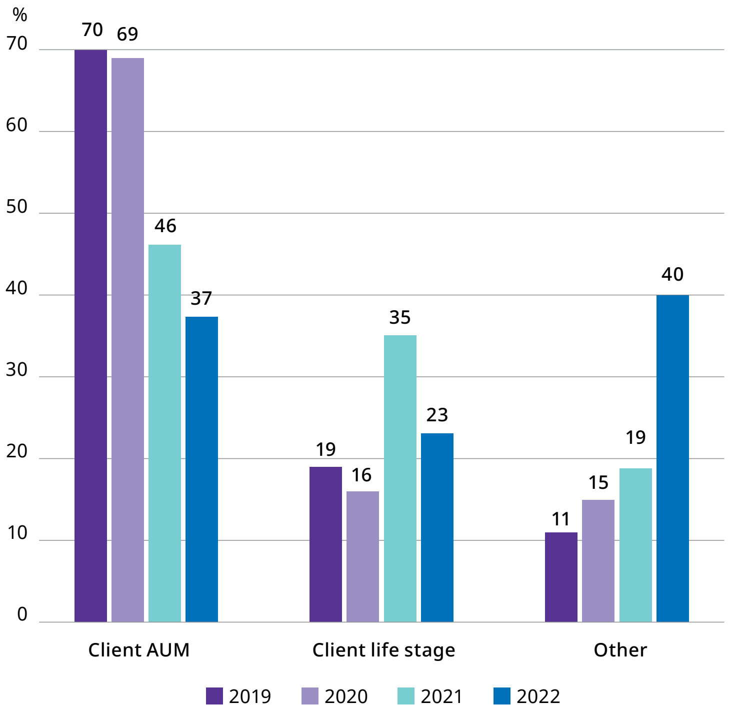
One of the client outcomes is 'Products and Services' where these need to meet the needs of the target market. With this in mind, it is interesting that 42% of advisers say that they do not currently segment their client base.

What is of more interest is that there has been a marked change in the way advisers segment their client base over the last year.

The proportion of advisers segmenting their client base by AUM has fallen from 70% in 2019 to 37% in 2022. Whilst we had been observing a rise in segmentation by life stage, 40% now segment their client base on a basis other than AUM or life stage.

This may suggest that advisers are starting to segment clients at a more granular level and we will use future surveys to understand this trend better.

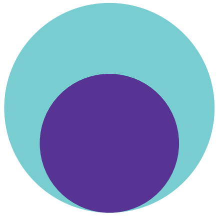
Figure 10: If you segment your client base, what basis do you principally use?



Fees

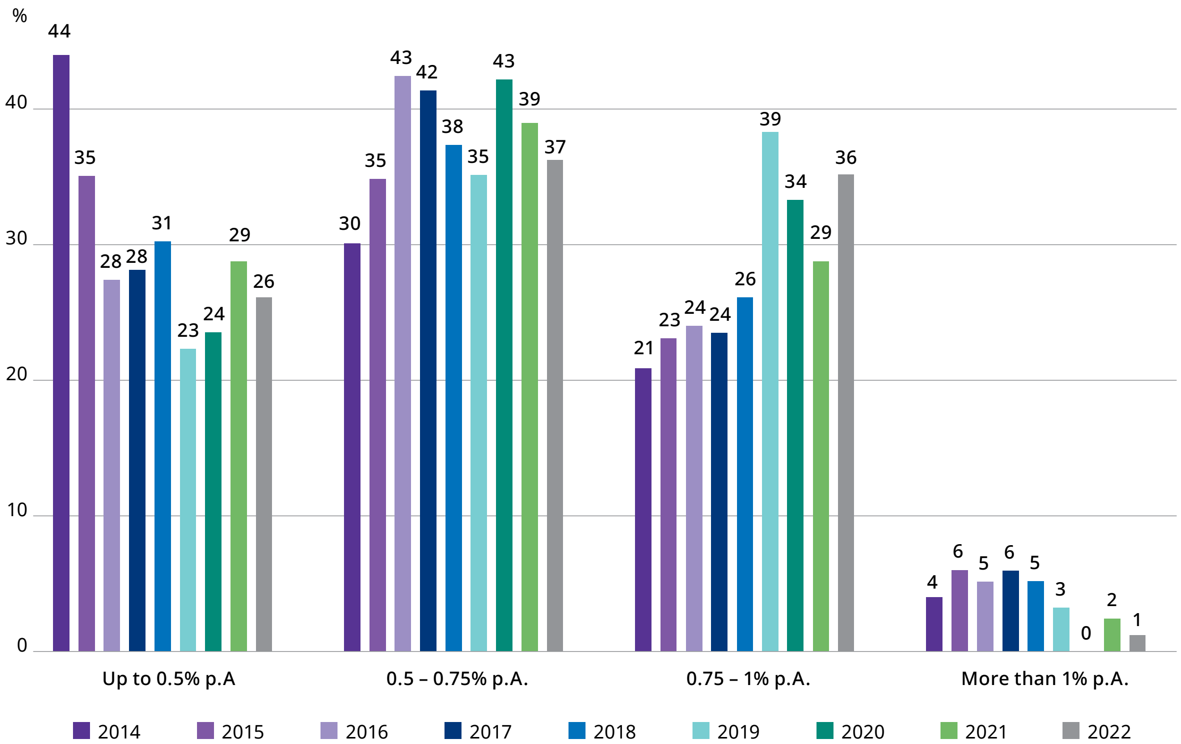
42%

of advisers feel there is a downward pressure on their advice charge



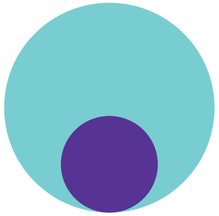
73% of advisers surveyed now have an average percentage fee based on assets of between 0.5% and 1% but 42% feel that there is a downward pressure on their advice charge. Contrary to this, there is a marked increase in those charging between 0.75% and 1.00%. As advisers start to implement the Consumer Duty regulations in 2023, we may see further movement in this area.

Figure 11: What is your average % fee based on assets (approximately)?

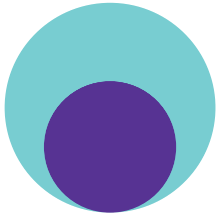


Outsourcing trends

20%
of advisers have increased their use of outsourced solutions in the last year



43%
of advisers outsource over a quarter of their clients' assets under management



Overall, advisers are continuing to increase their use of outsourced solutions and the pace of this appears to have accelerated a little during this year's challenging market conditions. This is perhaps unsurprising, as the main reason why advisers outsource portfolio management is the access to investment expertise and resources it provides. 20% of advisers reported that they have increased their use of outsourced solutions in the last year.

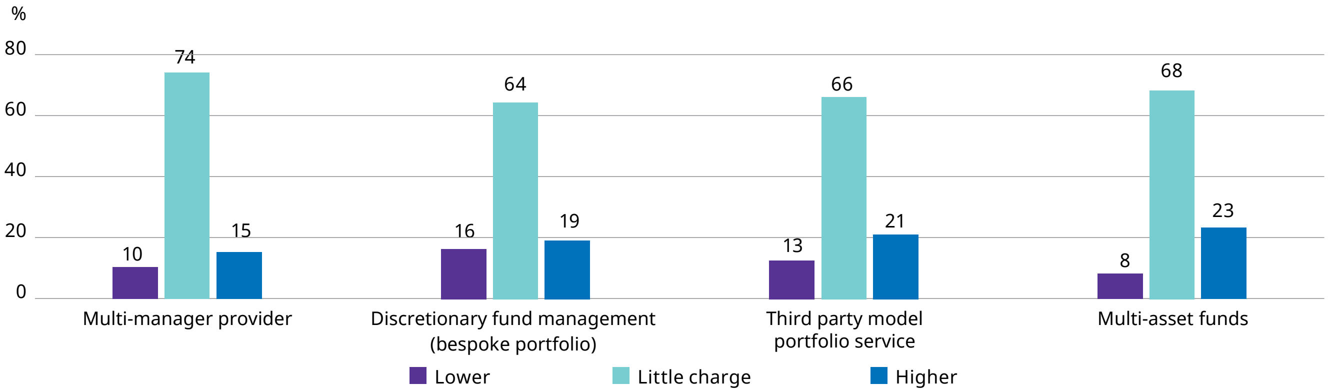
Similarly, we have seen the number of advisers who don't outsource any of their clients' assets reduce to 22% which is a significant shift from 33% last year.

Advisers are also using outsourced solutions to help manage an increasing proportion of their clients' assets.

43% of advisers now report that they outsource over a quarter of their clients' assets under management compared to 27% in November 2021.

When asked where clients' assets will be allocated next year, the greatest increases are towards multi-asset funds and third party model portfolio services.

Figure 12: If you outsource portfolio management, how do you expect your allocation to the following services to change in the next 12 months?



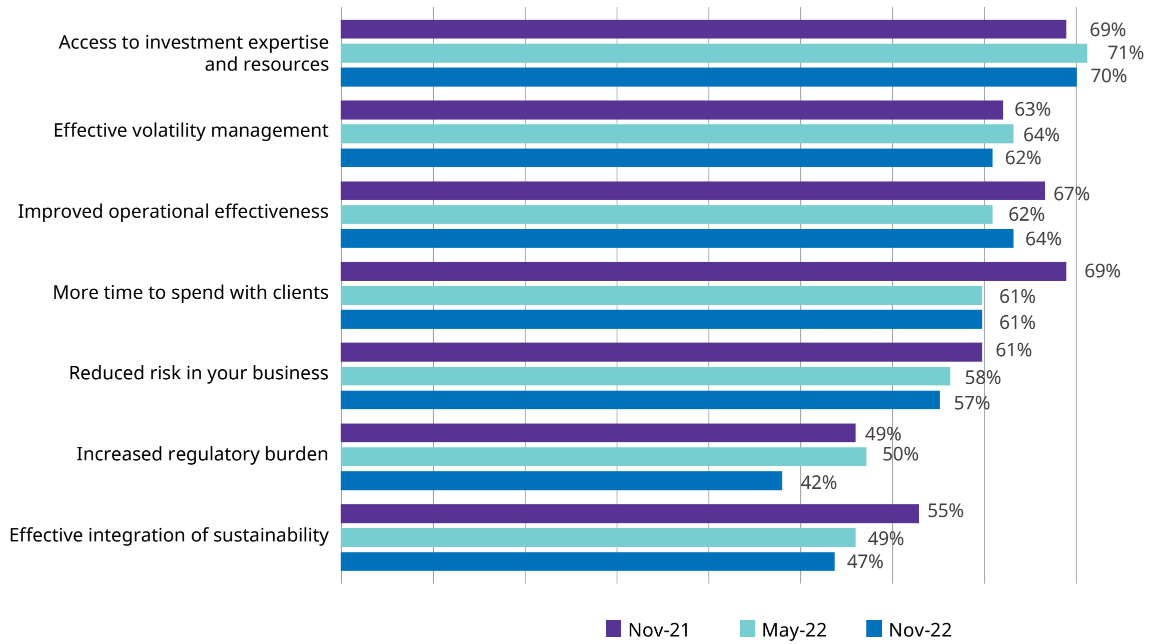
Reasons for outsourcing

The main reasons for outsourcing remain predominantly the same as in previous surveys. Access to investment expertise was rated important or very important by 70% of advisers.

Improved operational effectiveness, effective volatility management, more time to spend with clients and reduced risk to their business, also continue to be rated as important or very important by more than half of advisers.

Our conversations with advisers indicate that many of the factors influencing a decision to outsource are inter-related. As an example, the increasing burden from regulation such as MiFID II reporting on charges and portfolio depreciation can be linked to operational effectiveness. For some advisers, access to investment expertise and resources is very much related to the requirement to offer a sustainable solution and integrate sustainability into their investment processes. Many are still on a journey with this and therefore feel more comfortable using an investment partner for their sustainability offering to clients.

Figure 13: How would you rate the following in reaching a decision to outsource portfolio management?



Selecting an outsourced solution

Top three factors when selecting an outsourced solution

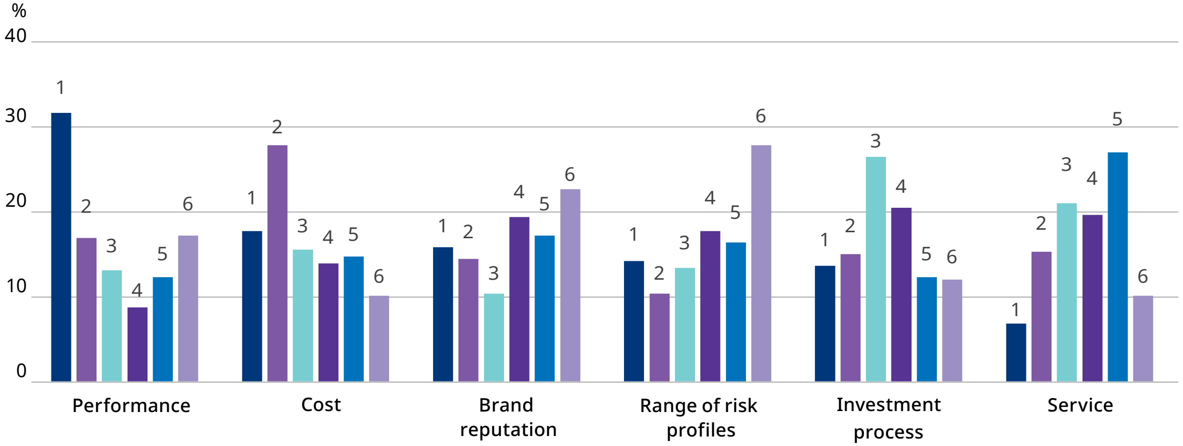
Performance

Cost

Brand reputation

Figure 14: Rank the importance of the following 6 factors in selecting a model portfolio service or multi-asset fund solution for your clients from 1 (most important) to 6 (least important)

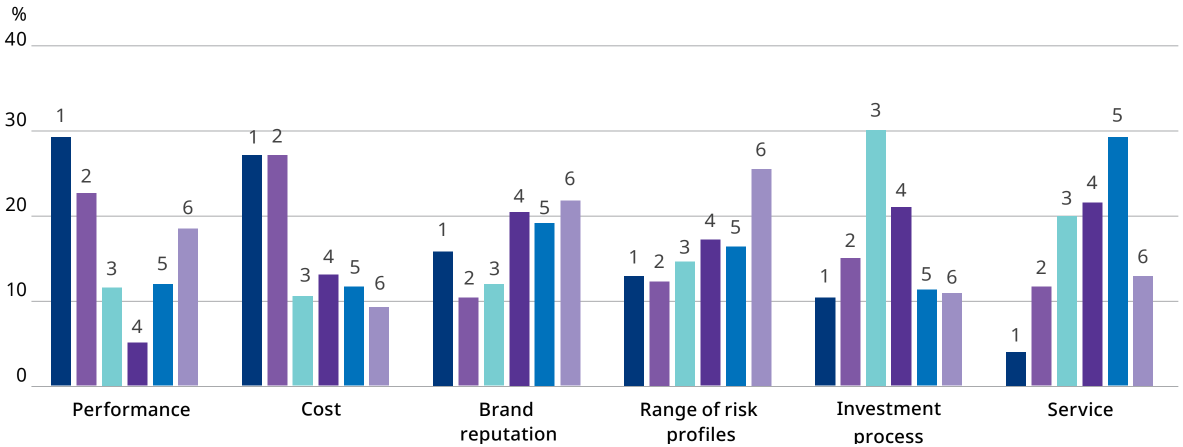
Model Portfolio Service (MPS)



Performance and cost remain the most important factors when selecting an MPS or multi-asset solution.

In previous surveys, brand reputation has regularly been cited as the least important factor in the selection process. Could its position higher up the ranking reflect a recognition of the value of a reputable, trusted name in providing reassurance to clients in uncertain times?

Multi-Asset Fund



Wealth transfer

Advisers are increasingly concerned about the impact that wealth transferring between generations could have on their businesses. 59% are now concerned that they could lose business as wealth transfers between generations.

In our previous surveys, nearly 80% of advisers indicated that wealth transfer provides a significant opportunity, yet clearly the challenge of retaining assets within a business when it transfers is now more broadly recognised. Perhaps we should be reframing this important issue as 'the great wealth retention challenge'.

Are you concerned that your business could lose assets as wealth transfers between generations?

59% Yes

41% No

Do you have a specific proposition for targeting the transfer of family wealth to the next generation?

26% Yes

74% No

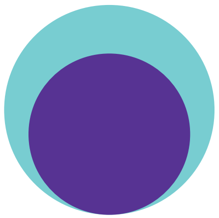
An ageing client bank

Attracting younger clients does not appear to be a priority for most advisers. This is reflected in the ageing profile of their client bases and the declining number of advisers prepared to advise clients with less than £50,000 to invest.

This has reduced dramatically over the last few years from 53% in 2019 to only 32% this year. The proportion of advisers with a differentiated strategy for younger investors has also reduced.

68%

of advisers surveyed have clients with an average age of 51-64



26%

of advisers surveyed have clients with an average age of 65+

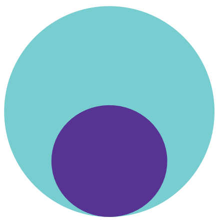
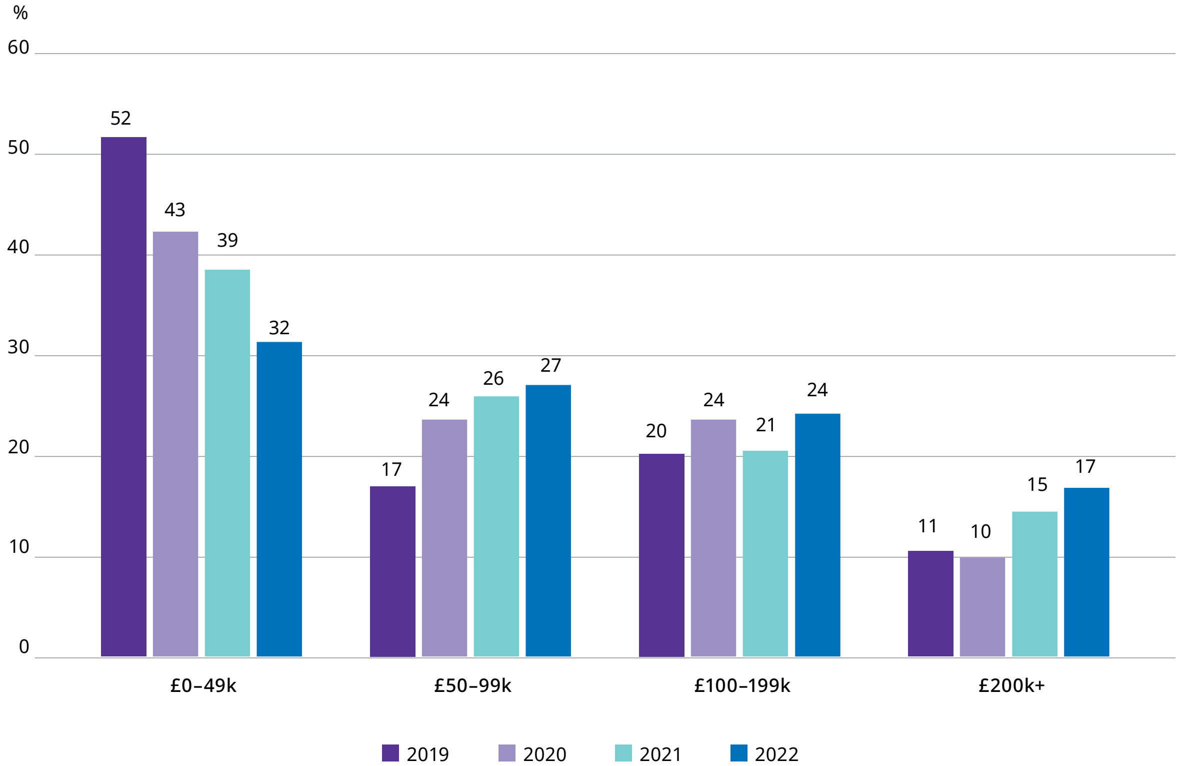
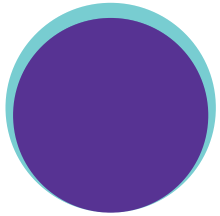


Figure 15: What is your minimum asset size for new clients?

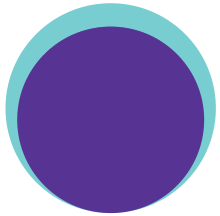


The next generation of investors

95%
of advisers don't have a differentiated sales and marketing strategy for female investors



86%
of advisers don't of advisers don't have a differentiated sales and marketing strategy for younger investors



The wealth within the baby-boomer generation is typically transferring to female partners with predictions that 60% of wealth will be in female hands by 2025. However, the number of advisers with a strategy for retaining, attracting and advising women has fallen since our last survey in May. Those with a specific proposition may be well placed to pick up these female clients.

Advisers might therefore be wise to consider offering services to the partners and younger family members of clients, even if these may not immediately be profitable. Establishing relationships with those who may inherit assets from clients well before the point of inheritance can be very helpful in efforts to retain those assets within a business.

Advisers ignoring the wealth transfer opportunities might also find that when negotiating business valuations for an exit strategy that the potential loss of assets could be challenging.

Key takeaways

As ever, our UK Financial Adviser Annual Survey delivers lots for us to consider and highlights some interesting trends.

Advisers continue to face a range of challenges not just from the current market and economic environment but also from the added burden of running a business with regulatory changes to manage, pressure on fees, and decisions on their investment proposition and wealth transfer to consider.

With The Consumer Duty firmly on the radar, it is important to recognise their value to clients in providing peace of mind and keeping long-term investment plans on course against a backdrop of the cost of living crisis, rising taxes, inflation and interest rates.

Hopefully financial advisers can evidence the intangible!

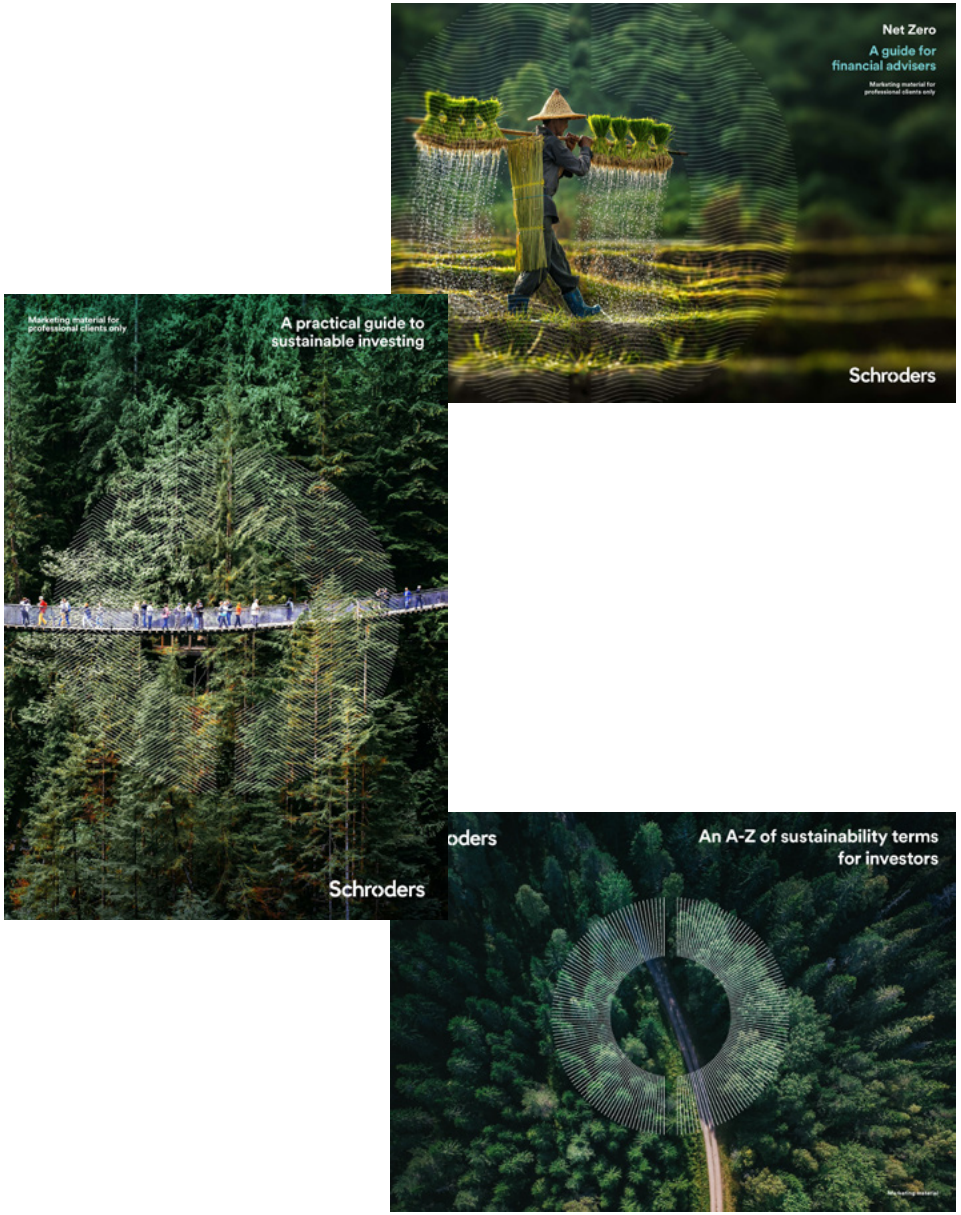
Adviser toolkit

Schroders have a range of support available, including our recent:

- A-Z of sustainable investment terms
- Net Zero guide
- Transfer of wealth guides
- A guide to Schroder Investment Solutions

Our team are also always happy to have conversations about succession planning.

To find out more about these topics run-on and our investment solutions, visit **schroders.com/investment-solutions**, contact your usual Schroders representative or call our **Business Development Desk on 0207 658 3894**.



EST. 1804

Schroder Investment Management Limited
1 London Wall Place, London EC2Y 5AU, United Kingdom
T +44 (0) 20 7658 6000

schroders.com/investment-solutions
@Schroders_UK
Schroders

Issued in December 2022 by Schroder Investment Management Limited, 1 London Wall Place, London EC2Y 5AU. Registration No. 1893220 England. Authorised and regulated by the Financial Conduct Authority. UK005407. 606092