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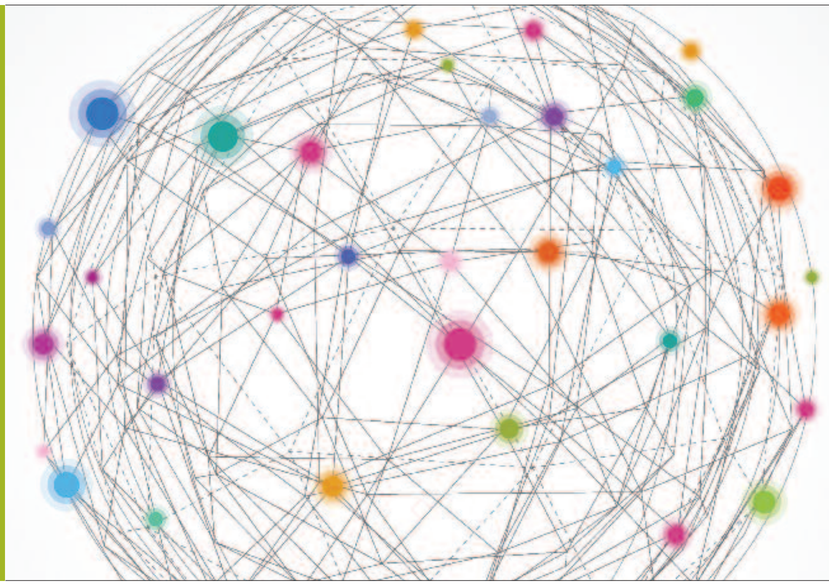

The Virtual Financial Advisor: Delivering Personalized Advice in the Digital Age

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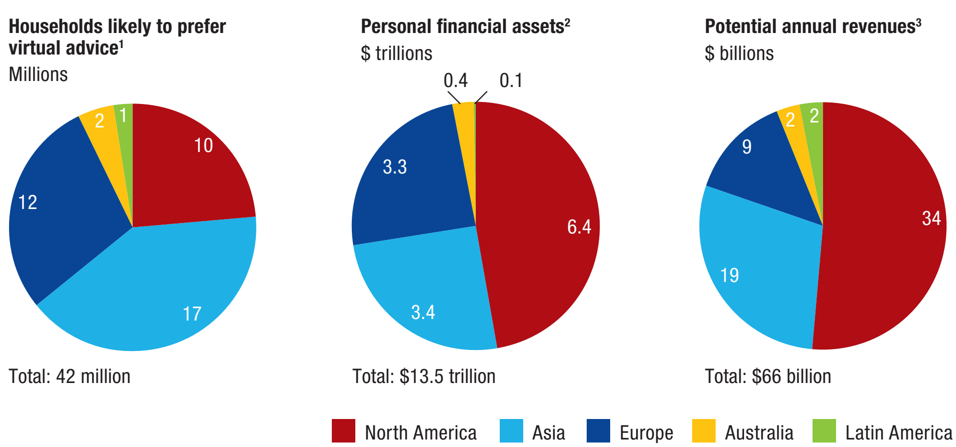
Consumers increasingly use Skype or FaceTime to discuss personal matters and connect with friends and family globally. It is only a small leap to imagine a couple using the same tools on a Saturday morning to receive personalized financial advice without leaving the comfort of their living room. This scenario is indeed coming to pass. The rapid advance of digital technology is allowing financial advisors to be remote and face-to-face at the same time.

Pioneering banks and wealth management firms around the world are taking a novel, centralized approach that offers high-quality personal financial advice for clients without a local advisor or relationship manager. The "Virtual Advisor" retains tailored service from qualified advisors, but replaces networks of branch offices with a central hub, from which advisors cover a dedicated set of clients via telephone, video conference and digital tools. This model allows firms to afford a superior proposition for offering financial advice, particularly for consumers with assets between $100,000 and $1 million (the "mass affluent"), who have been historically difficult to serve in a cost-effective manner.

As clients in these segments grow increasingly comfortable using "virtual" channels, they will inevitably form a profitable core of customers for those financial services providers that can deliver high-quality advice digitally. In fact, McKinsey estimates that approximately 42 million households worldwide, representing $66 billion in annual revenues across banking, borrowing and investing, are already prime candidates for a "virtual advice" model (Exhibit 1). Moreover, consumer behaviors are shifting rapidly within all age groups. In the United

Exhibit 1

McKinsey estimates that 42 million households, representing $66 billion in annual revenues, are prime candidates for virtual advice



[1] Assumes that 25% of affluent households ($100,000 to $1M in financial assets) and 10% of high-net-worth households ($1M to $30M) are prime candidates for virtual advice.

[2] Includes deposits and investments and insurance.

[3] Includes revenues for mortgages, consumer loans, deposit products, investments and insurance. Excludes payments revenues.

Source: McKinsey Panorama; McKinsey Global Wealth Pools

States, for example, 40 to 45 percent of affluent consumers who switched their primary wealth management firm in the past 24 months moved to a direct, digitally-led firm—in many cases choosing to work with a phone-based advisor at those firms. For banks, virtual advice is particularly critical, because customers are quickly adopting online and mobile channels for service interactions, but continue to prefer human contact for important sales. In a world with fewer branches, virtual advice will be a critical component in attracting and serving banking clients.

A number of banks and wealth management firms around the world are already building execution expertise in delivering remote advice, attracting new clients and reaping significant cost advantages.

In addition to growth, a successful virtual model can deliver reductions in cost to serve of as much as 40 to 50 percent, lead to customer satisfaction scores that exceed those of a firm's in-person models, and enable stronger compliance and control—two critical institutional priorities for nearly all financial firms.

A number of banks and wealth management firms around the world are already building execution expertise in delivering remote advice, attracting new clients and reaping significant cost advantages. This paper examines the trends that are making virtual advice an imperative for forward-looking banks and wealth managers, describes emerging virtual advice models, and lays out a set of key operational elements that will demand critical attention from senior leaders.

A new approach to personal advice

In most markets, the distribution of advice-based financial products looks much the same today as it did 20 years ago, when the commercial Internet was launched: thousands of advisors serving local clienteles, from a geographically widespread network of wealth management offices, bank branches and insurance agencies.

Of course, advisors and the firms they represent have not ignored the digital era. Many advisors use digital tools to connect with clients and to improve their own productivity. Financial firms, for their part, have invested heavily in providing these tools to their advisors and encouraging their use. However, the structure of the financial advisory network remains fundamentally rooted in a physical branch network. This is the element that is now changing.

In the past 12 months, firms such as WealthFront and Betterment, along with offerings such as Schwab Intelligent Portfolios, have gained attention by offering one alternative to the traditional advisor-branch model. These so-called "RoboAdvisors" replace advisors' judgment with automated low-fee investment platforms offering asset allocation and portfolio rebalancing. Ultimately, fully automated advice algorithms may come to play an important role in the financial advice landscape for many products, both as standalone models and as tools for advisors. But so far it is not clear whether these firms can move beyond simple investment solutions, capture non-millennial investors at scale, or replicate the trust and intimacy of a human advisor. The potential exists, but the jury is still out.

In parallel, a less-heralded trend is quickly reshaping the distribution of a broad swath of financial products. The new model—"virtual advice"—retains the high level of personal service that most consumers value from their financial advisor, but leverages the connective power of digital communication (e.g., videoconferencing, co-browsing) to deliver this service from a distance. Advisors in this model often work with digital platforms (such as those being created by robo advisors) to simplify parts of the advice process, but they continue to offer the personalized services that customers demand. In other words, the digitization of advice does not mean the automation of advice.

Virtual advice should also not be confused with a high-end call center or a service center for low-value clients. It is not a digital add-on that allows in-branch advisors to communicate virtually with their clients. Rather, it is an end-to-end delivery model for financial advice that replaces an in-person advisor – and offers a different (and frequently better) value proposition for a segment of consumers.

Virtual advice would not be making strides today unless a substantial number of mass affluent and high-net-worth clients were already comfortable handling their finances at a distance. McKinsey estimates that in most markets at least 20 to 30 percent of these clients are likely to subscribe to the virtual model, with an even higher percentage in Northern Europe and parts of Asia where digital usage is more advanced.

The virtual financial advisor model has been deployed successfully by banks and wealth managers in both mature markets and growth markets. European banks including Santander, ABN AMRO and Nordea have pioneered the model alongside their traditional branch-based advisory networks. In the U.S., Fidelity, E*Trade and Charles Schwab are consolidating clients' investment assets by adding personal financial advice to their existing direct distribution platforms. ChinaTrust's "Air Financial Advisor" in Taiwan and Itau's "Personalite" service in Brazil are testing the power of the model in maturing markets. In addition to large incumbents, a number of firms without established branch models are also making the leap to virtual advisors. These include large asset managers like Vanguard, digital banks such as mBank in Poland and startups such as Personal Capital in the U.S. (Exhibit 2).

A distinct and novel channel

Three core features define the virtual advisor channel and distinguish it from other advisory channels:

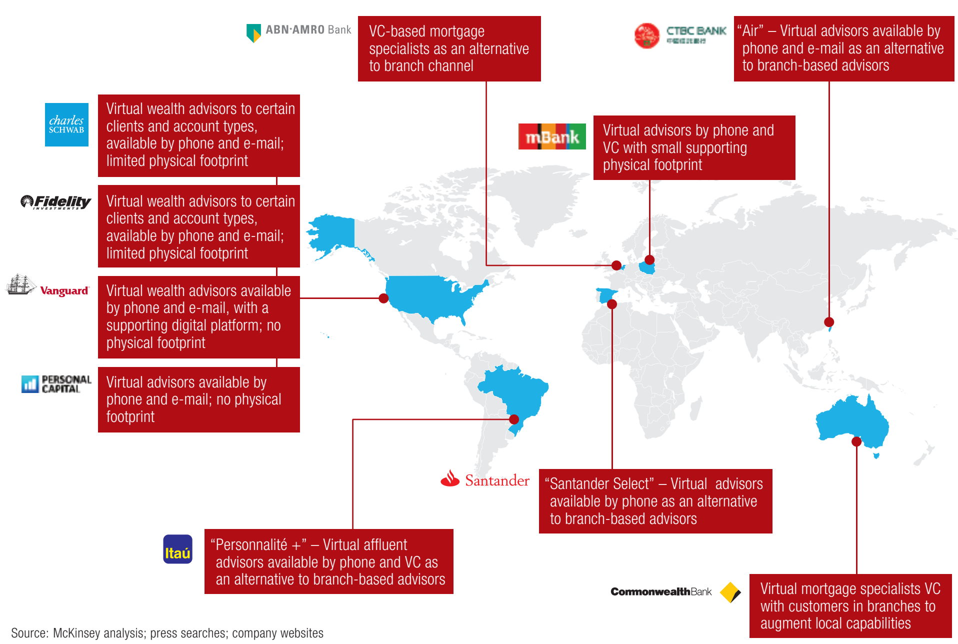
- **Dedicated advice at a distance:** As opposed to the classic call center, the centralized hub of the virtual advice center delivers a high level of personal service from high-caliber advisors. Licensed professional advisors work with a named book of clients individually, or in small teams. As with an advisor located in a physical branch, every client has a "real person"—a specific advisor (or small group of advisors)—to call if they need help.
- **Central locations:** Rather than meet face-to-face or reach out from a branch network, advisors operate from one or more "main branch" locations that support interaction with clients by phone, video chat and e-mail. Centralizing operations removes many of the constraints of geographically widespread networks.
- **Seamless digital fulfilment:** Nearly all transactions are completed digitally and seamlessly. The hub is not a lead generator for in-person advisors— rather it must be able to fully execute on the advice and recommendations advisors deliver to clients.

Three archetypes

Globally, firms have deployed virtual advisors in several configurations. Three primary archetypes have emerged,

Exhibit 2

Leading financial firms around the globe are launching virtual financial advisors



Source: McKinsey analysis; press searches; company websites distinguished primarily by their product focus:

- The **virtual affluent banker** provides holistic advice across investment, lending and banking products. The type of advice can lean more towards the transactional (i.e., focused on specific product needs of clients) or can be holistic (leading with a financial plan, and uncovering specific needs). This model is most prevalent in markets where it is the norm to provide integrated advice to mass affluent consumers.
- The **virtual wealth advisor** replaces the traditional financial advisor, and provides investment- and financial-planning-led advice. For many clients the focus is retirement saving, but this model also covers other financial goals and activities (e.g., budgeting). Firms deploying this model, such as Vanguard and Personal Capital, often roll out a side-by-side digital tool to support the financial planning process.
- The **virtual mortgage advisor** is a standalone offering which focuses on mortgages and home equity. Advisors in this model help clients with end-to-end management of the mortgage process—from initial conversations to closing—but typically do not emphasize a long-term relationship (because of the nature of the product sale).

In each of these archetypes, virtual advisors are typically launched side-by-side with existing in-person advisors, and often rely heavily on in-person channels to build initial scale. In most cases, the advice center is offered as an integrated alternative for the segment of consumers who are comfortable with a remote relationship. In others, the advice center can work in tandem with an in-person network– providing end-to-end specialist support for a specific type of product, or supplementing in-person teams.

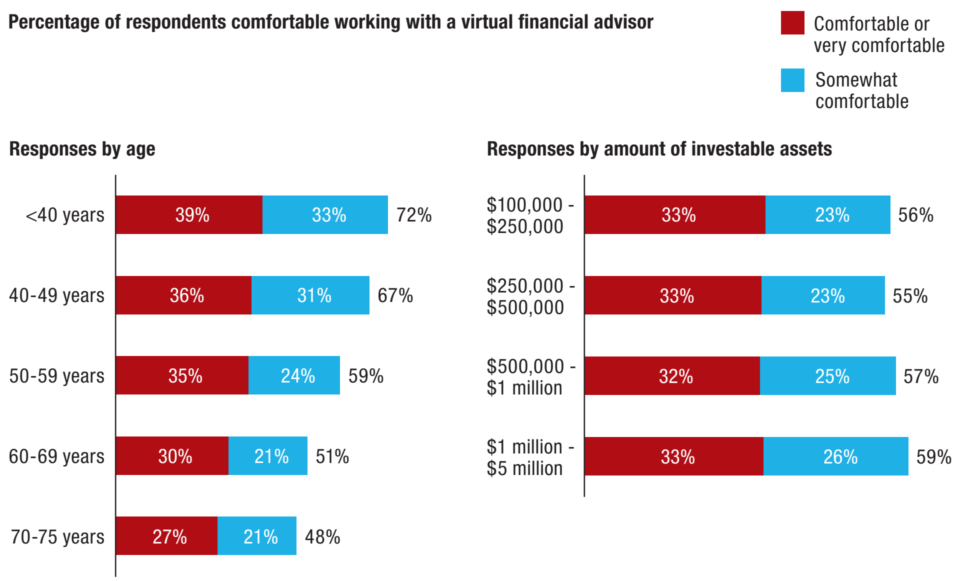
Why Now?

The virtual financial advisor dovetails with four fundamental trends currently reshaping the distribution of personal financial products:

- *A critical mass of consumers is now open to receiving financial advice from someone who does not live or work near them.* Consumer surveys across mature markets show that at least 20 to 30 percent of mass affluent and affluent consumers would use a dedicated financial advisor based outside their local area, and a larger share are open to the concept. While many early efforts have targeted clients in the mass affluent range, research shows that wealthier consumers are just as likely to prefer this service model (Exhibit 3).
- *The number of clients is growing at a faster rate than distributed advice networks can sustain.* In mature and emerging markets alike, the number of households with sufficient assets to need some form of financial advice is growing significantly faster than GDP (Exhibit 4,). Banks and wealth firms will struggle to grow in-person advice capacity at the same pace. In mature

Exhibit 3

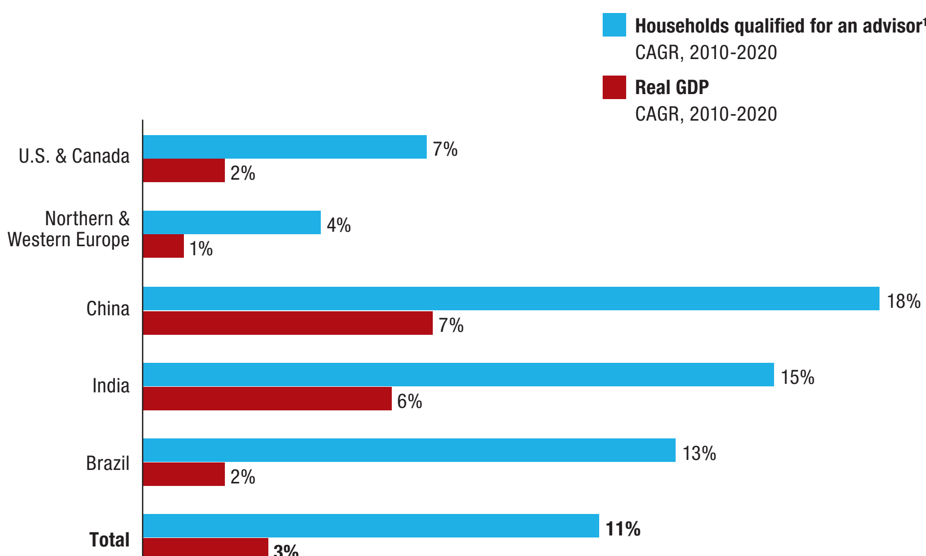
Significant numbers of customers – regardless of wealth level or age – are comfortable with virtual financial advisors



Note: n=10,865, respondents with $100,000 to $5 million in investable assets, aged 30-75 years old in the U.S.
Source: McKinsey Affluent Consumer Insight Survey 2014

Exhibit 4

The number of households with enough investable assets to require advice is growing significantly faster than GDP



[1] Qualified defined as investable assets >$100,000 in U.S. & Canada; >€100,000 in Europe; and >$50,000 in China, India and Brazil.
Source: McKinsey Global Wealth Pools; The Economist Intelligence Unit

markets branch foot traffic is declining, making it difficult to justify expansion of the physical network, and important to find new ways of delivering advice. In emerging markets where the growth of the advised segment is most robust, there is a significant shortage of advisory talent. In this context, the rapid capability-building that is possible in advice centers is especially valuable.

- *Digital technologies and capabilities are moving mainstream.* Three groups of technologies that underpin the virtual financial advisor have grown more common and more stable in recent years: connective technologies (e.g., video conferencing, chat and co-browsing) that allow the advisor and client to build a trusted relationship despite the lack of a physical presence; security tools (e.g., secure e-mail, e-Signature and voice identification); and digitized processes that enable streamlined and paperless completion of transactions.
- *Regulators in many markets have turned their focus to the quality of financial advice, and the fees charged to retail consumers.* These shifts have made the cost of advice more transparent, and increased the importance of consistent and compliant sales practices— thereby creating advantages for a lower-cost, more controlled model.

The Value Proposition

The virtual financial advisor offers substantial value to clients and financial firms. For advisory clients in certain behavioral segments, the center can be a more convenient experience, and offer advice and service that is equal or superior to traditional accounts, and potentially with lower fees. For the bank or wealth manager, the advice center delivers substantial cost savings and productivity gains over the scattered distribution network.

Client value proposition

- *High-quality advice, on the client's terms.* Virtual advice centers offer hours and weekend coverage beyond the working hours of the conventional branch, enabling consumers to engage with their advisors on their own terms. This is often accomplished by creating early morning and late evening advisor cohorts, and alternating "off days" to allow more continuous coverage. Consumers particularly value the ability to interact on nights and weekends, when they have time to discuss their finances. In addition, the ability to receive consistent high-quality advice from any location appeals to professionals who travel frequently, retirees who relocate for part of the year, or any clients who value the convenience of a digital interaction to a face-to-face meeting.
- *Client-segment specialists.* Because it concentrates a large group of advisors in a single pool, the advice center allows for efficient matching of clients with advisors who are uniquely suited to serving them, whether for a preferred language, profession (e.g., doctors, small business owners, corporate man-

agers, freelancers) or other characteristics (e.g., retirees). Top-performing advisors in physical networks often develop specialties organically, but the hub allows firms to plan for and build in such expertise at necessary scale, and deploy it across the client base.

- *"Industrial-strength" client experience and contact cadence.* Embedding a common gold standard customer experience across hundreds of branch locations is a frequent challenge for distributed advisory networks. With virtual advisors, firms can more effectively develop a consistent model of service, while maintaining individual entrepreneurship and personalization. Additionally, on-site hub leaders spend 60 to 70 percent of their time directly observing client-advisor interactions, and providing immediate feedback. The centralized structure also simplifies the adoption of sophisticated CRM systems and predictive models to support advisors in meeting needs at key moments of truth for clients.

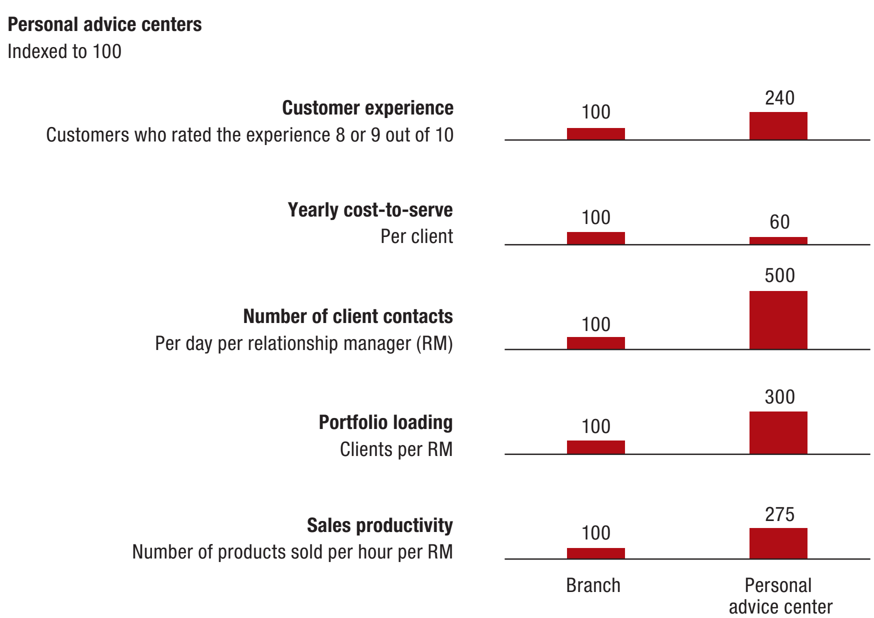
Firm value proposition and value at stake

The unit economics of the virtual financial advisor are superior to the traditional in-person advisor (Exhibit 5). The most obvious benefit is the scale economies from reducing real estate and operational costs through centralization, but the center enjoys four other advantages:

- *Higher advisor efficiency and productivity.* The hub advisor can achieve loading

Exhibit 5

Institutions launching virtual financial advisors have seen improvements in both economics and customer experience



Source: McKinsey & Company

ratios that are 70 to 90 percent higher than traditional advisors, while often increasing the frequency of contact for each client. Generalist hub advisors working with mass affluent clients, for example, can work with 500 to 600 clients, far above the typical book of 300 clients in in-person networks. One bank's hub advisors were able to complete four times more client meetings per day than in-person advisors, doubling both the loading ratio and contact frequency. Several factors make hub advisors more efficient: centralized administrative and operational support; on-boarding specialists to support new client introductions; less travel time; and fewer distractions in the branch en- vironment. Moreover, clients who choose to work with a hub advisor tend to prefer shorter conversations, further enhancing advisor efficiency.

> The hub environment is especially conducive to building advisor capabilities at scale.

- *More consistent and cost-effective use of specialists.* The coaching and co-location tactics that enable the "industrial strength" client experience in the centralized hub can also upgrade the efficiency of specialists. In the centralized environment, specialists are co-located within pods of advisors to build informal relationships, and are actively promoted by leaders as part of their day-to-day coaching. Moreover, the reduction of specialist travel affords many more client conversations, and their presence in the central branch makes specialists part of the natural rhythm of the business.
- *Opportunity to rapidly build advisor capability, especially for early tenure advisors.* The hub environment is especially conducive to building advisor capabilities at scale. In distributed networks, the hands-on coaching and role modeling that is core to adult learning is expensive to execute. Field coaches travel across a distributed network to work with advisors one-on-one, while branch advisors have to leave their offices to attend group forums. In the centralized hub, however, a regular pattern of short training sessions can more efficiently build advisor capabilities, with lessons reinforced by coaches listening to their live calls to clients. Advisors also benefit from informal exposure to the best practices of successful peers.
- *Reduce the risk of advisor and client attrition.* Lastly, the centralized hub can reduce the frontline attrition that erodes the profitability of many advisory sales forces. The deep integration of the advisor and client with a custom digital platform curtail advisors' opportunities to poach clients. In addition, departing advisors can be replaced more quickly by dividing their books among the large

base of advisors, instead of having to wait for a local replacement.

The improved economics of the virtual financial advisor can be shared with clients (through lower fees) or advisors (through higher compensation), or reinvested by the firm. The savings can also be applied to deliver higher quality advice to mass affluent segments that the firm often cannot otherwise afford to serve. Delivering equivalent advice at lower cost is particularly critical in countries such as the UK, where new regulations dictate that advisory fees be explicitly disclosed.

Advice centers share common elements, but design decisions made at the outset can yield a wide range of value propositions.

Operational imperatives for setting up the advice center

Capturing the full potential of the virtual financial advisor requires a fundamental reengineering of a firm's distribution model. Ten areas in particular demand critical attention:

- *Crafting a distinctive value proposition and coverage model:* Advice centers share common elements, but design decisions made at the outset can yield a wide range of value propositions. For example, firms must decide on whether advisors will be generalists or product-specialists; on the mix of outbound product offers versus inbound servicing; and on the extent to which clients will have access to a bespoke digital platform. There are important trade-offs to be made—for example, between creating highly specialized teams that focus on specific client segments, and aligning those teams with local geographies. Firms must also decide the degree to which clients will have access to their advisor. One U.S. firm, as an example, provides four advisor meetings to clients below a certain asset threshold. And, of course, the value proposition must be appropriate to the target wealth segment, and positioned to compete against alternatives in the market.
- *Identifying, cultivating and on-boarding new clients:* The design of the acquisition pathway for new clients is the most important operational element for a successful advisor hub. Large financial firms already have a substantial base of mass affluent and affluent clients who are strong candidates to embrace the hub model, but initiating a relationship over digital channels is a more challenging task. New processes must be created to prioritize lead sources, funnel leads to the hub, predict which clients are most open to remote advice, and develop marketing materials that emphasize the advisor hub proposition. Inside the hub, a specialized role is often created to reach out to prospects, explain the proposition and schedule meetings with advisors. Advisors then need to develop tactics to

quickly build trust and demonstrate value with new clients. Each acquisition pathway has its nuances—particularly in cases where new leads are referrals from advisors in other channels (who must be compensated), or completely "new to firm" (where basic KYC and account opening processes have not been completed).

Firms must find creative ways to develop a distinct sub-brand for the virtual advice model.

- *Marketing the new value proposition in a compelling way, without cannibalizing existing channels:* As with any new service, a distinctive marketing strategy is critical to attracting clients into the virtual advice model. Unlike traditional face-to-face advice, virtual advice must rely heavily on centralized marketing to describe the value proposition to new clients. While virtual advisors still play a key role in acquisition, the more substantial marketing effort is often required to entice clients to have the first conversation. Firms must find creative ways to develop a distinct sub-brand for the new model, clearly define the value proposition and create offers to attract new clients. Importantly, incumbent firms must accomplish these goals while managing the risks of "de-marketing" existing face-to-face models.
- *Designing and embedding a "gold standard" client experience (without undercutting individual entrepreneurship):* To achieve an industrial-strength client experience and higher advisor efficiency and productivity it is critical to define and embed a single "gold standard" approach. Depending on the focus of the center there are typically 5 to 10 client journeys that require an explicit standard. For a mortgage center these might include new client on-boarding, product selection and initial approval, and separate standards for primary home purchase, secondary home purchase and refinancing. The standard should be granular enough to establish a common way of working, without becoming too prescriptive. In order to maintain individual ownership among advisors, firms can use an approach that borrows heavily from lean management, incorporating proactive problem-solving by teams in daily huddles, and a collaborative design process in which individual advisors suggest improvements to the standards. Advisors in the hub should be actively engaged in the initial design and continuous refinement of talking points, customer engagement standards, contact and financial planning expectations, and frontline managers should support the cultural changes.
- *Re-engineering operational processes to work seamlessly and securely in a virtual environment:* Operational processes designed for branches need

to be re-engineered for a virtual environment. For example, one North American firm systematically re-engineered the personal lending process to combine the advisor empowerments embedded in their branch-based process with the streamlined processing of their traditional call-center workflow. Often, completely new solutions need to be developed, particularly with regard to confirming the identity of a client over phone or VC. A cross-functional team including representatives from regulatory/compliance, legal, back office and product groups must overcome challenges such as the requirement for "wet signatures" on applications, enable the secure exchange of documents, and create workflow approaches that ensure a seamless client experience.

- *Establishing a management rhythm and culture that drives sales performance through capability building:* In distributed networks, many sales managers take a "hands off" leadership approach, pushing targets and providing support and coaching in a mostly reactive way. Hub managers need to adopt a different approach to coaching and sales management, one that establishes a daily and weekly operating cadence with one-on-one and team-based capability- building, and off-loads administrative tasks to central resources in the center. Given the scarcity of advisory talent in many markets, the ability to quickly build capabilities can be a significant differentiator. Leaders should help new advisors manage their activity levels on a daily basis, and provide more extensive hands-on coaching and feedback through call listening sessions. In order to accomplish this, administrative and operational leadership tasks must be centralized. In a successful hub, leaders spend up to 70 percent of their time on direct coaching activities, compared to 30 percent or less in traditional physical networks.
- *Identifying high-potential talent:* The hub advisor is, first and foremost, an advisor. However the mix of skills and mindsets required is different to that of the typical advisory population. There is a premium on the ability to communicate effectively over phone and digital channels, to learn quickly from peers and leaders and to efficiently operate with co-located specialists and support staff. Commercial independence remains extremely valuable, but must also fit within the hub environment. Identifying successful profiles and finding rich veins of talent is critical to successfully scaling the model. There are also often opportunities to tap into traditionally underrepresented populations— for example, working parents who prefer to work from 7 am to 3 pm.
- *Creating an integrated digital platform at the heart of the advisor-client interaction:* Building a trust-based relationship, discussing new financial concepts, and reviewing illustrations or results can all be done remotely—but are only effective if the right platform or tools are there in support. The ability to video-conference and co-browse are key strengths of the

hub value proposition. Most firms will need to revamp their existing tools for digital interaction; for example, they will need to pare back lengthy paper-based financial plans and replace them with dynamic visualizations. A distinctive digital experience can also be a client acquisition tool; Personal Capital, as an example, is tracking over $120 billion in AUM on its free financial planning and tracking software.

- *Integrating the hub with existing channels and managing change within the physical network:* Most banks set up the virtual advisor center as a complimentary (not competing) channel; thoughtfully designing the interfaces with other channels and managing communications and change is critical to success. In particular, aligning incentives to ensure the branch and call center channels support the migration of clients into the hub is critical.
- *Using advanced analytics to optimize performance:* Successful virtual advice models rely heavily on the use of advanced analytics to improve lead generation and optimize client outreach. A

Five lessons learned from creating advice centers

Five lessons

1. The leader of the virtual advice business should have an advisory background, rather than a call-center operations background. Their two most important responsibilities are to develop the vision for the advisor experience and to hire and inspire great advisors. Surround this leader with a team that has experience in operational centers and digital capabilities.
2. Successful virtual advisors have a different talent profile than in-person advisors. They build trust quickly over the phone, are operationally (and personally) efficient, and highly comfortable with digital tools. Skills in lead generation and building a book can be relatively de-emphasized..
3. At the outset, don't hesitate to double count revenue in the physical "branch of origin" to motivate branch managers to refer appropriate clients to the virtual center. However, avoid assigning a "back-up" in-branch advisor in order not to duplicate costs.
4. Create strict guardrails (e.g., explicit consent) to prevent onboarding clients who actually prefer to work face to face. This may slow the pace of growth, but it avoids building a book of remote clients who refuse to engage.
5. For most clients, co-browsing is more important than video-conferencing in driving virtual advisor productivity and client experience. That said, knowing that VC is available helps build customer trust.

well-structured virtual advice center enables the deployment of these tools in a powerful way and becomes highly reliant on them. Three analytical models in particular are a seamless fit in the more controlled hub environment: prioritizing leads based on client propensity to favor remote service; pinpointing when clients are going through life events or moments (first child, wedding) that make them more open to particular products; and analyzing transactions and online interactions to give advisors insights into how they can help their clients in real time. It is important to build these models early, so that they can be refined as operational data is gathered.

Solving these operational challenges requires a live operating environment where the firm can test, learn and refine the execution of the hub model. Successful deployments invariably feature an "at-scale laboratory," initially staffed with between 30 and 50 advisors. Firms building a virtual advice model should avoid the tendency to "over design" through a central team. The initial focus should be on determining the core value proposition, designing a "minimal viable product" and setting up the laboratory. With this approach, it is possible to refine the operating model, and build a track record that justifies investment within 12-18 months.

To reach scale, virtual advice models ultimately require between 100 and 200 advisors – although some banks are already in the process of scaling to more than 500 advisors. The size of the opportunity and the results of early laboratory efforts also guide the pacing of four types of large capital investments: building front-end digital capabilities, re-engineering back-end technology and operations processes, outfitting new physical space and launching the new brand at scale in the open market. The initial laboratory is often launched with an investment of less than $10 million and heavily leverages the institution's existing capabilities; delivering the full client value proposition typically requires a total capital investment of between $25 and $40 million.

■ ■ ■

For the foreseeable future, virtual financial advisors and incumbent in-person advisors will operate in parallel. The time for innovation, however, is now. Pioneering firms are quickly building execution expertise in delivering remote advice, starting to attract new clients and reaping cost-advantages through the use of advice centers. There is an opportunity for forward-leaning banks and wealth managers to join them and to transform how consumers' financial service needs are met.

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