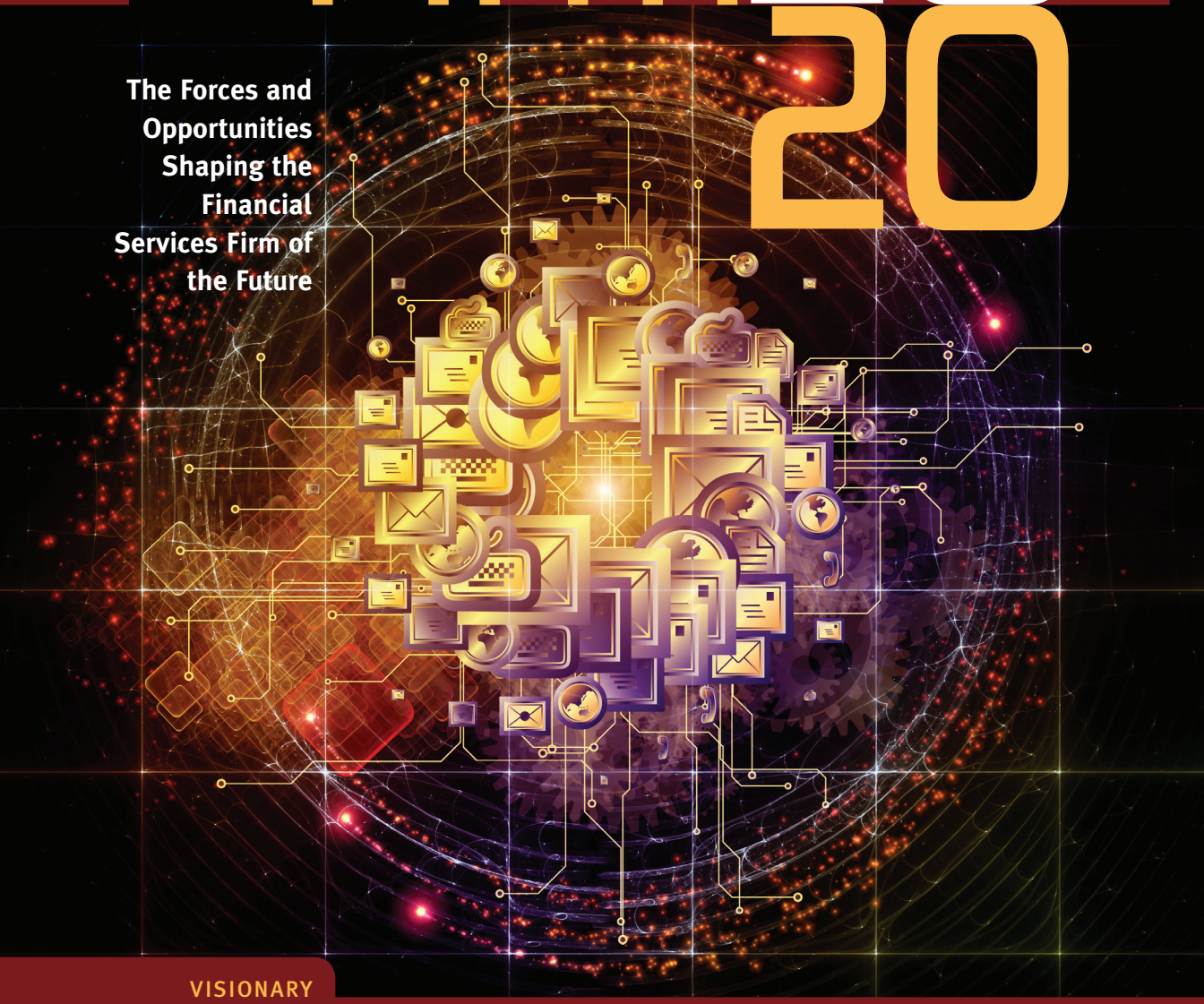
Firm 2020

The Forces and Opportunities Shaping the Financial Services Firm of the Future



VISIONARY LEADERSHIP SERIES

GAMA FOUNDATION
FOR EDUCATION + RESEARCH

Firm 2020

The Forces and Opportunities Shaping the Financial Services Firm of the Future

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Research funded by the GAMA Foundation for Education and Research
Conducted by Change Management Solutions, Signature i, LLC, and Trend Spot Consulting

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The GAMA Foundation and Its Contributors

The GAMA Foundation for Education and Research is a 501(c)3 nonprofit organization dedicated to conducting and promoting research and education to enhance the profitability and productivity of field leaders in the insurance and financial services industry. Since its creation in 1990, the GAMA Foundation has funded major studies on key leadership topics, including recruiting and selecting new associates, launching new associates, retaining successful associates, mentoring and coaching practices, effective local marketing, building successful advisor teams, developing high-performing leadership teams, and launching new frontline (sales) managers.

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Benefiting From Firm 2020

Successful businesses do not happen by accident. Visionary leadership, rigorous management, and daily execution are all key elements of the formula for success.

Most of us are consistently good at only two of the three, however, and it is our visionary leadership that often falls short. After all, creating plans that stretch for much more than a year can seem silly when unexpected changes so often render our ideas obsolete.

But what if you had a resource that made your firm's future easier to anticipate and plan for? That is exactly what you will find in the GAMA Foundation's *Firm 2020.* Our research findings open the door for you to work effectively *on* your business and not simply *in* it, and the insights and opportunities we present will give you confidence in addressing your business future.

Opportunity is the operative word for *Firm 2020,* and it is one we will use frequently throughout the book. We like it more than the word *risk*, which applies equally well (but less optimistically) to the research findings that follow. Entrepreneurs are optimistic and opportunistic by nature, and *Firm 2020* will not disappoint you. Its extensive range of trends and forecasts will help you clearly envision your business at the end of this decade.

Your answer to a single question now will largely determine how much opportunity versus risk you will experience in the pages that follow. That question is:

To what extent is your business purpose centered versus comfort centered?[1]

If your business is largely comfort centered, then as circumstances change — and they will change mightily — you will seek to return as much as possible to what you have known before, to what you're comfortable with.

But our culture and our economy are shifting in such profound ways that the comfortable choice will no longer be an option if you want your business to grow — or even to hold its own.

In today's evolving marketplace, people want a financial partner they can trust to help them achieve their goals — and their goals are *not* to buy products and services. The Great Recession has altered America's psyche, and people are focused more than ever on investing their dollars to achieve specific, meaningful outcomes in their lives. They want customized solutions that are simple, fast, and secure. Are you prepared to evolve into the fast, flexible, and value-laden firm that the world of 2020 will require?

[1] Ryan W. Quinn and Robert E. Quinn, *Lift: Becoming a Positive Force in Any Situation* (San Francisco: Berrett-Koehler Publishers, June 1, 2009).

If your business is comfort centered and you want to simply sell products and manage assets, you will have little to offer today's emerging markets. But if your business is purpose centered, there are real and growing needs for the expertise, and the outcomes, that your firm and its advisors can provide. To serve these growing markets, however, you will have to do business differently and offer more value than you have ever offered before.

Firm 2020 explores significant economic and cultural drivers that will greatly affect insurance agencies and financial services firms over the next five to seven years.

The GAMA Foundation invested in *two research studies* — conducted separately and simultaneously — to ensure that our *Firm 2020* results provide you with the richest and most comprehensive set of findings possible:

The first research study, *The Market of the Future,* examined the firm's challenges and opportunities based on economic, demographic, and sociological trends that will transform client demands. Conducted by Change Management Solutions, it *provides a bottom-up perspective* by examining changes in the needs of current and prospective clients that will greatly influence the types of products and services that competitive firms should offer. It then follows these impacts up the supply chain to the insurance and financial services industry. This research paid particular attention to where the money is in our society, where it's going, and where client opportunities and needs are either developing or not being met. It also identifies areas where strategic partnerships may allow field leaders to better address client needs. These research findings are based primarily on quantitative data and trends.

The icon above will the used throughout Study One to highlight the industry's evolving client *markets*, the products and services that will provide these markets *value*, and the types of *partnership* opportunities that emerged from this research.

The second research study, *The Firm of the Future,* examined the firm's challenges and opportunities from a cultural and environmental perspective. Conducted jointly by Signature i, LLC, and Trend Spot Consulting, it *provides an outside-in perspective* by examining major trends driving change in our environment and how these trends can impact our industry. This research paid particular attention to six significant change drivers that will require action on the part of field leaders, and it will open you up to major dimensions of the future that you as a leader can influence. These research findings are based primarily on qualitative data and trends.

The second icon above will be used throughout Study Two to highlight your opportunities for developing *people* (consumers and advisors), *capabilities* (technology and security), and business *strategies* (data analysis and business models) in building your firm of the future.

Understanding the economic and cultural forces examined in these two studies will inspire you to think about your business differently. The findings will very likely:

- Disturb you
- Spark new ideas about your business model
- Inspire creative thinking about the work you do and the value it provides
- Help you consider where your firm can best grow and excel in the coming years

Together these two studies provide a rich source of insights, trends, and provocative predictions. In addition, the simple planning questions and resources we have included with the research will start you down the path to your preferred business future. We hope, of course, that you won't stop at these first steps.

Firm 2020 was developed by the GAMA Foundation as a resource for your firm's growth and development. Ideally, you will want to share it with your team and incorporate its findings into your regular planning and implementation activities.

Firm 2020's highest value will not be found in its forecasts or even its exciting array of opportunities. It will instead be found in the new insights you gain into your own particular future, your greater ability to talk strategically with your team about that future, and the decisions you make to meet the future on your terms.

We hope, as you proceed down your unique path to the future, that you will be inspired and excited by the many changes and opportunities that will continue to appear on the horizon — and that you and your team will have a powerful and successful experience designing and building your own *Firm 2020*.

The Market of the Future

STUDY 01

Introduction to Study One

By understanding the market forces now under way in the U.S. economy, and the financial forces affecting consumers and their evolving needs, you as a field leader will be in the best position to consider — or reconsider — your firm's market focus.

Whether you decide to stay put, adjust course, or dramatically shift your business, this research will likely present opportunities you had not previously considered.

Study One includes the following:

- A brief overview of the *transformative changes* in household economics that occurred in the late 20th century and how the financial services industry must act soon to address even greater changes to come
- *Future business scenarios* for four different markets, giving you a chance to consider how our industry may come to look quite different in the years ahead
- Critical perspective on the three *market drivers* that provide the best opportunity for our industry to hold its own in the marketplace or, better yet, to grow; this section presents the forces in play behind the future scenarios
- A variety of *business opportunities* for each market driver, showing how changes already afoot in the marketplace could be harnessed by the insurance and financial services industry
- *Debrief and strategy questions* for each market driver to help you quickly identify the main takeaways for your firm
- Additional *drill-down* information for field leaders who want to delve more deeply into the background data and trends.

At the conclusion of Study One, you will be able to identify the market that is the likely sweet spot for your firm in the coming years, as well as the opportunities that are most appealing for where you would like to take your business.

You will then be well positioned to explore the six change drivers that will most dramatically impact your firm's structure and operations, as presented in Study Two.

But first, take a look at the following checklist of thought-provoking forecasts from Study One. Is your firm prepared to address these changes today?

CHECKLIST FOR

The Market of the Future

Below are 18 thought-provoking forecasts from *Firm 2020*'s Study One, *The Market of the Future*. Use this checklist to evaluate how well your firm is prepared today to address the business markets and clients of 2020.

18 Market and Client Forecasts	Is Your Firm Prepared?	
	NO	YES, Here's How
1. Industry professionals must offer a value proposition focused on a comprehensive and holistic quality-of-life outcome for clients.		
2. The commoditization of insurance products and their pricing will continue and accelerate.		
3. Regulations aside, the generational and economic changes under way in the United States will compel the industry to shift its compensation model from commissions to fees.		
4. To avoid shrinking, the financial services industry must follow the Baby Boomers into their retirement years and provide them with value in new and different ways.		
5. Entrepreneurial Boomers interested in creating encore careers represent an untapped market. They need products that offer transition income and start-up capital.		
6. Expertise is needed to manage the decumulation of assets over a 20- to 30-year retirement. The insurance and financial services industry must develop and provide this expertise or be supplanted by those who will.		
7. Affluent seniors will seek lifestyle planning and retirement management services, not simply asset management.		
8. The "skills gap" in the U.S. job market is severe and growing. Firms should adjust their business models to attract older professionals to their organizations.		

18 Market and Client Forecasts	Is Your Firm Prepared?	
	NO	YES, Here's How
9. Addressing the skills gap could mean looking abroad for talent or taking some activities offshore.		
10. Changes that will make the industry more attractive to older professionals are likely to also make it more attractive to women and younger generations.		
11. Unless the industry wishes to shrink to match the smaller size of the generation following the Baby Boom, it must significantly expand its presence in the middle market.		
12. Firms must become involved in financial education to reach new clients in small businesses and the middle market.		
13. Middle-market households may view savings as a reduction in current income rather than as deferred consumption.		
14. Middle-market providers should be prepared to sell products inside of tax-deferred savings plans available through the government or businesses, to compete against those plans, or to focus on households that do not currently receive employee benefits.		
15. Less financially savvy households are a prime target for fraud. An advisor with a personal interest in a financial transaction will likely be regarded as suspect.		
16. In evolving markets, firms should build partnerships with nonprofit organizations, community colleges, government-sponsored programs, and other organizations with compatible goals.		
17. Based on the industries driving the recovery, there will be greater opportunity to reach well-compensated professionals in small businesses who do not currently receive employee benefits.		
18. As employees increasingly define themselves more by what they do than for whom they do it, business associations and professional societies may become a significant channel for marketing financial services.		

Transformative Change — Past and Future

In less than a generation, the future of the insurance and financial services industry was transformed by three extraordinary forces that fundamentally changed the nation's approach to savings, wealth accumulation, and wealth management.

- **The rapid increase in women's participation in the workforce during the 1970s:** The rise of two-income households dramatically increased savings potential and decreased dependence on employer-sponsored retirement plans for long-term financial security.
- **The introduction of voluntary, self-managed retirement plans in the 1980s:** These plans allowed employers to migrate away from defined-benefit plans and the liabilities they were imposing on firms' balance sheets.
- **The rapid downsizing of large firms in the 1990s as they transitioned to just-in-time management practices, and the subsequent outsourcing of both support and core job functions:** This shifted most of job creation from large businesses to small ones, but the latter are much less likely to provide employer-sponsored pension plans and group life insurance policies.

These three forces combined to transfer the primary responsibility for saving for retirement from employers to households.

Previously, households depended on employers' pension plans for their long-term financial security, and most people gave little additional thought to preparing for retirement. Household savings typically had shorter-term goals: securing a down payment for a home or a car, financing vacations and home repairs, and saving for children's educations. Because of shorter life spans, retirements generally lasted only a few years, and ensuring there were sufficient funds to finance them was the responsibility of employers and, for a third of the workforce, unions.

But by the late 1990s all of that had changed. Individuals were now directly responsible for saving for their retirements, and they needed to become more deliberate and foresighted in their savings behaviors and financial planning. The tax advantages offered by a wide range of new pre-tax savings programs encouraged long-term savings.

Because people are process oriented and not product oriented, they focus on the outcomes they want and are willing to consider alternative ways to get there. They are not concerned about the product-oriented market segments — for example, life insurance versus equities — that defined financial product providers for decades.

In fact, the introduction of pre-tax savings programs encouraged greater risk taking by otherwise-cautious individuals and transformed households from savers to investors. Risk-averse consumers, who would normally choose a low-risk annuity like life insurance over stocks, have taken on greater risk in their

401(k)s because the tax deduction basically offset the increased risk of equities. Thus, even for the risk averse, mutual funds have become competitive with life insurance as a long-term investment.

In addition, because people are living into their 80s and 90s, they are far less likely to be concerned with one of the primary roles of insurance: the financial security of surviving children who are themselves in their 50s and 60s.

In response to these new roles and attitudes, life insurers have increasingly positioned their products as annuities that offer tax-free income for the policyholder in addition to providing for a surviving beneficiary.

Consumers now view all of the various financial products as alternative means of achieving their long-term goal: sustaining a defined quality of life into their later years. In today's world, life insurance must compete with voluntary programs like 401(k)s for households' savings dollars.

The Future of Financial Services

More significant changes are in store for the financial services industry.

By 2020, the Baby Boomers — the largest, most highly educated, and most affluent generation ever seen — will be well into retirement, and insurance agencies and financial services firms will face greater competition for the next generation's smaller pool of prospective clients.

It is clear that there simply will not be sufficient clients, as *they are currently defined,* to support all of the insurance and financial services providers. The industry must be willing to transform itself to serve new and evolving markets if it is to avoid significant downsizing. As in any evolving market, though, opportunities abound for entrepreneurs who are willing to provide value.

Throughout Study One, a consistent lesson appeared in every market trend examined. All indicators show that the industry must *redefine for the client* what its agents and advisors do. Advisors must shift from a focus on managing assets or mitigating risks to serving as partners who help clients *manage their lifestyles* and *reduce their risks.*

Services must be repositioned to reflect the value of the outcome of advisors' work — ensuring a sustained quality of life — rather than the tools they use to achieve it.

This transition is extremely important for a number of reasons:

- First, commission-based compensation is becoming increasingly unsustainable. The commoditization of insurance products, and the reduction of their profit margins, will accelerate as Baby Boomers begin to exit from the market and are replaced by smaller generations. This trend, in combination with other forces, will push the industry to fee-based compensation. (For multiline products, fees may be presented as levelized commissions.)
- Second, it is impossible for the average household to save enough money to cover all of the risks they will face during retirements that last 20 to 30 years. People recognize the impossibility of the task, and households have already begun shifting their focus. Rather than trying to save enough money to cover all of their risks, they are taking steps to reduce the risks in the first place. Reducing risks is an expanding market that will require services that cannot be reflected in a commission.

- Third, the financial literacy of prospective clients will be, in general, much lower in the future. Generation X is only two-thirds the size of the Baby Boom, and to avoid shrinking, the industry will need to expand into less financially educated households. These less-well-informed clients will require additional assistance in understanding, selecting, and managing the products and services that agents and advisors will offer.

Efforts are now under way to address the country's "savings gap" and shift a significant share of households' investments away from real estate — which should theoretically herald a significant rise in the demand for financial products and services. However, increased household savings will not automatically result in greater demand for what agencies and firms currently offer. Agencies and firms must shift what they actually do — redefining, even reinventing, what they provide for the client.

The client is the centerpiece of Study One because a business that wants a long and successful life must organize itself around consumer needs and desires. In the research that follows, consumer trends and their evolving needs are summarized and specific business opportunities are identified to capitalize on the economic forces in play.

In some cases, the research findings call for a radical reimagining of the industry, including new products and services, to help clients manage their lifestyles as well as their assets.

These offerings should not be viewed as ancillary services. Instead, they should be included in new service packages that would allow agents and advisors to charge fees for all of their activities — including those traditionally associated with asset management.

In considering these research findings and the new business endeavors recommended, it should be remembered that private, public, and nonprofit partners can and should be engaged to assist in many of them.

Future Business Scenarios

Market Shifts and Opportunities

To prevent contraction, cannibalization, and commoditization of our industry's services, agencies and firms will need to adopt new business models, expand into new products and services, and develop new partnerships that span the private, public, and nonprofit sectors. Otherwise, the sharp contraction in insurance agency employment witnessed during the 2007–09 recession will recur.

By 2020, much culling of the industry will have taken place, and several different business models will have emerged.

The four business scenarios that follow may be used separately, as described, or be put together in different combinations. Often such combinations will be through LEGO-like partnerships, through which firms snap together to attract certain market segments but remain separate for serving others.

As you read through the four scenarios, pay particular attention to where you see opportunity and where you feel concern. The information on the three market drivers, immediately following this chapter, will help you more fully appreciate the forces in play behind these scenarios.

SCENARIO ONE

Increased Competition for the Affluent Market

The traditional insurance agency and financial services firm will most likely continue to practice in the affluent market. But there will be fewer firms serving a much more targeted and, on average, wealthier clientele.

The conclusion of the *2012 World Wealth Report* observed, "A range of firm-specific and industry-wide trends are converging to undermine the profitability of wealth management operations today."[2] Using 2004 household wealth data, Chip Roame, founder of Tiburon Strategic Advisors, concluded, "There are far too many advisors for today's number of affluent households.

"If one includes brokers, independent reps, life insurance agents, private bankers, et al, there are 400,000 advisors and approximately 40 million households having $100,000 or more of investable assets, leaving a maximum of 100 clients per advisor."

The number of very wealthy individuals who are under 50 years old fell 21 percent between 2004 and 2007, from 504,000 to 398,000. Given the sharp decline in wealth among those under 50 years old during the 2008 financial crisis, that number has likely fallen even further. This decline in the younger affluent market will continue into 2020.

Roame further estimates that only 70 of those 100 households actually engage financial advisors, and only 12 of the 70 have assets in excess of $1 million.[3]

In addition to the above supply-and-demand problem, the market has fewer wealthy individuals under 50 years old. Thus, the number of new entrants into the "very wealthy" pool (investible assets of $2 million or more) will decline through 2020.

At the same time, more wealth is being concentrated at the very top of the very rich spectrum, and competition for these most affluent Americans will become increasingly fierce.

Fewer firms in the affluent market will survive, but as Roame points out "surviving is not prospering." To succeed, these firms will need to focus on "serving fewer, more wealthy clients with more comprehensive services." However, they will face steep competition for the very high end of the market from a growing number of institutional players. Four banks have entered this market since 2011: Wells Fargo with its Abbot Downing brand (2012), PNC Bank's Hawthorn Unit (2012), U.S. Bank's Ascent Private Capital Management (2011), and Fifth Third Bank's Mirador Family Wealth Advisors (2011).[4]

As wealthy Baby Boomers enter retirement and live longer, their concerns will transition from wealth accumulation to wealth *decumulation* and risk management, making them less likely prospects for traditional wealth-management products and services.

To retain these very wealthy clients, firms will need to greatly expand their product and service offerings. And with higher costs to service these clients, firms will need to instate fee-for-service pricing to offset the increasingly squeezed profit margins of commission-based compensation.

Decumulation will be essential to serving even the ultra-affluent households, and the range of services required will grow even as margins are squeezed. The *2012 World Wealth Report* noted that the cost-to-income ratio for assets under management for high-end clients had been climbing before the financial

crisis. As these clients live longer and become even more demanding, the cost-to-income ratios will continue to rise, making commissions on assets even more challenging. Many of the independent registered investment advisors (RIAs) serving these markets had already shifted from commission to fee-based compensation by 2010.

In addition to intergenerational wealth planning and risk management, ultra-wealthy clients will need to be protected from the variety of tax changes that will be put forward to address the growing deficit and for which they, the infamous "One Percent," will be targeted. To service these clients, firms will need deep benches with a broad array of talented professionals.

An axiom of economic development is that businesses consolidate in smaller markets and differentiate in expanding markets. As the industry faces a more affluent but shrinking number of high-end clients, expect the following changes by 2020:

- Insurance-based firms in the affluent market will become fewer in number and markedly larger.
- Banks in particular, with a broad range of resources and abilities to serve broad geographic areas, will have a natural advantage in this market, which explains why so many have started divisions to serve it.
- A growing number of financial advisors will be salaried employees working for large financial institutions.
- RIAs and small firms will be hard-pressed to compete for affluent retired Boomers, who have been labeled as "validators" and not "delegators" like previous generations. They will survive as niche players in narrowly defined markets.

SCENARIO TWO

Lifestyle Management for the Retiree Market

While many upper-market agencies and firms will not be able to compete for the ultra-affluent population, that doesn't mean they will simply go away. Many will transform themselves into lifestyle management firms and charge fees to help affluent households manage the complexities of retirements that are measured in decades instead of years. These would include helping clients on such matters as:

- Investing in aging-in-place renovations in their residences
- Choosing when to forgo maintaining a home and instead move into assisted living
- Managing finances and minimizing drawdowns following a catastrophic illness
- Negotiating the governmental and health insurance bureaucratic mazes to ensure they receive all of the benefits for which they are eligible
- Managing household finances when the "managing" spouse of a household dies or becomes cognitively impaired

According to a 2007 National Institute on Aging (NIA) study, one in seven Americans over 70 years old succumbs to dementia. NIA estimates that nearly 10 million Americans provide free care to dementia patients, including relatives and nonrelatives. The care is estimated at 8.5 billion hours valued at $94 billion.[5] In addition to this figure, one needs to consider the financial losses that dementia sufferers incur by not being able to manage their finances, making the return on investment for financial management services for the elderly very attractive.

In addition, one in four Americans over the age of 70 loses his or her driving privileges to medical conditions. Helping older clients anticipate and address the lifestyle changes associated with this loss of mobility — which could include relocating to a home closer to centralized shopping, moving in with adult children, or engaging shopping and delivery services to ensure access to fresh food and prescription medications — will become an important and lucrative business. And because a growing share of adult children live more than 100 miles from their parents, relocating closer to the children could require assistance in transferring a complicated array of records and services, including financial and tax, medical and dental, insurance, and numerous other complex components of life.

Large insurance agencies and financial services firms would be able to form nonprofit affiliates to provide these services while charging fees for managing retirement as opposed to managing assets.

Multiline firms could develop aging-in-place and lifestyle management specializations. This could also create new relationship opportunities with renovation contractors as well as insurance and financial services providers.

SCENARIO THREE

Financial Planning for the Middle Market

Financial literacy will become an increasingly important concern for the financial health of middle-class American households and for the fiscal health of the public sector.

Greater financial literacy and more deliberate household savings at all levels of income will be necessary to mitigate the effects of the "fiscal tsunami" the growing elderly population represents.

There will be an unavoidable shift in the financing of elderly services from government agencies to individual households. This will cause public officials and the financial community to realize that financial planning is not just an exercise for the affluent.

Although the emphasis in public debate is on federal entitlements, state and local governments provide the lion's share of public services for the elderly population and the "social safety net" for low-income households.

Any cuts in state and local social services that are made to balance their budgets[6] will directly affect the quality of life for retirees who depend on them, especially for those unable to offset public subsidies with out-of-pocket expenditures. And retirees with investible assets will experience much faster drawdowns than they had planned or will find their tax obligations increased, leaving them with less to begin with each year.

In addition, some combination of tax increases, tax deduction elimination, and benefit reductions at the federal level — including restrictions to Social Security benefits — will have happened by 2020 for the federal government to remain solvent.

These policy changes, combined with continued increases in the elderly population and growing health-care concerns, will make household financial planning both more complex and more essential to prevent a new "fiscal cliff" — a slashing of household spending — from occurring. Any sharp curtailment of spending by the nation's elderly population could throw the economy into an economic downturn that would be even worse than the "Great Recession" of 2007–09.

Anticipating that possibility, state and local governments will support efforts by both for-profit and not-for-profit organizations to improve financial literacy, especially among the adult population.

Community colleges with 50 Plus programs will provide train-the-trainer classes for financial literacy courses. Local financial services firms and insurance agencies will provide instructors for these courses. And nationally recognized academic institutions like Boston College's Retirement Research Center will provide credible, independent content for financial literacy training.

Credible content — content unaffiliated with a particular provider — will be key to the programs' success, particularly as the general population is not especially trusting of financial institutions, and memories of their role in causing the 2007–09 financial crisis will still be painfully fresh.

National insurance providers will support nonprofit research on financial literacy training. These product manufacturers will help stimulate the demand for life insurance policies by distributing independent, third-party financial education material and household workbooks through insurance-based firms. And by having their logos associated with the research, the companies will gain public credibility and distinguish themselves from the companies that contributed to the financial crisis a decade earlier.

Similarly, insurance agencies and financial services firms will use financial literacy programs as "social marketing" and community outreach opportunities.

Partnerships between local firms and nonprofit financial literacy training organizations will become common, with agencies and firms providing physical space and instructors for such training — assuming they do not try to turn financial literacy programs into direct sales opportunities.

By appealing directly to members of the Millennial generation, many of whom will be entering their early 30s in 2020, firms will be able to identify new clients much earlier in their financial development, and thus more effectively compete with the entrenched financial planner for future affluent households' trust and loyalty.

By providing community-based financial counseling services to individuals and helping them establish household budgets that ensure long-term wealth accumulation, insurance agencies and financial services firms will provide a valuable social service for tens of millions of households. As part of that process, firms will identify for themselves the potential 2 million households — newly married, 30- to 35-year old college-educated professionals considering purchasing their first home — who are most likely to eventually command investible assets of $2 million or more.

Large firms might consider creating nonprofit subsidiaries in an effort to capture these clients exclusively.

SCENARIO FOUR

Portable Benefits for the Professional Market

In 2020, the largest underserved population for insurance products and financial services will be the employees of small businesses and the part-time employees of larger ones.

While small businesses accounted for a disproportionate share of job losses at the outset of the recession, they have already begun to outpace larger firms in job creation. As the recovery gathers strength and credit markets loosen, small businesses should begin to expand at an even faster pace. By 2020, barring another recession, small businesses will again account for well over half of the jobs in the United States.

Since the 1990s, small businesses have largely transformed themselves from Main Street retailers to professional and technical businesses serving other businesses rather than final consumers. According to the Small Business Administration, small businesses hold more than 70 percent of all patents issued since 1997.

Small businesses will be most dominant in health care, private education, professional and management services, business administration and support, and personal services, especially those providing the growing number of retirees with leisure, health, and quality-of-life support services.

These sectors employ a disproportionate share of college-educated and credentialed professionals, making them attractive targets for financial services providers. All of these sectors will offer above-average incomes, making their employees more affluent than the average employee, and yet underserved in financial services. This will create a new market opportunity for many smaller RIAs, insurance agencies, and financial services firms now losing market share in the upscale agent and advisor markets.

Because many of these types of businesses do not require heavy capital investments to start up (with the notable exception of health care), market entry and exit are not difficult. Therefore, market turnover is much higher among these small businesses than among larger organizations.

It is among small-business payrolls that one will find the bulk of the 58 million households identified in a 2010 study on the underserved life insurance market. A common reason these households did not have any or adequate insurance is because they "did not know how much to buy,"[7] demonstrating a lack of professional guidance. It is estimated that these households could offer "a sales potential of a staggering $17.5 trillion worth of policies," a figure one and a half times greater than the combined net worth of the top wealth holders, those with assets in excess of $2 million, according the IRS.[8]

Because employees of small businesses are less likely to have retirement plans and life insurance, the employee may well view these products as competing for his or her savings.

For this reason, benefits firms will need to encourage employees to defer current consumption in favor of the long-term security that comes with enrolling in employer-sponsored benefits programs that include insurance and defined-contribution plans.

To this end, firms will need to offer employee training programs on topics such as household budgeting, managing credit, buying a home, and saving for children's college tuitions. These programs, offered periodically as an employee benefit, will be paid for by the employers. Employers will benefit from lower employee turnover rates that translate into lower recruiting costs and higher productivity. These training programs will be the major selling point for employers.

Educated professionals not only make good clients, they are also the most likely candidates to move into an encore career. Many of these individuals are not preparing for retirement — they are preparing for their second act. Simply offering them the traditional bundle of financial products and services will not be sufficient. Products that specifically meet their lifestyle and life planning needs and desires will be key.

As the country's skills shortage continues to tighten, small businesses will be unable to compete for the highly qualified workers they need without offering benefits. But given the volatility of the small-business market, firms will need to offer portable benefits to make them attractive to employees. This will make the small-business employer more of a gatekeeper or intermediary to individual households than the financial services firm's client.

The best opportunities to serve these markets will be through developing a sector-specific expertise to understand the kinds of individuals employed by a specific industry and their particular financial needs.

The one-size-fits-all approach offered to benefits managers of large companies will not suffice here. In fact, *the firm that is successful in this market will actually function as the benefits manager rather than a financial products salesperson.* This is not a market where one can make a sale and then move on to the next sales call.

Working with industry associations and professional societies will be extremely important to those serving this market. The role of associations could become especially important if legislation were passed to allow insurance agents to sell across state lines, or if a judicial decision strikes down such restrictions, as in the case of the 1978 *Marquette* decision that declared interstate banking regulations violations of the Interstate Commerce Act.

Such developments could allow for economies of scale among advisors functioning as voluntary employee benefit providers who could then operate nationally. It also would allow them to partner directly with financial literacy organizations to increase employees' voluntary participation in savings plans, and thereby increase individual enrollments in their various products.

NOTES

[2] William Sullivan, Karen Schneider, David Wilson, et al, *2012 World Wealth Report* (Capgemini and RBC Wealth Management), 37, http://www.capgemini.com/insights-and-resources/by-publication/world-wealth-report-2012/?ftcnt=10120.

[3] David J. Drucker, "Chasing The Wrong Clients?," *Financial Advisor* (November 2005), http://www.famag.com/component/content/article/1268.html?issue=62&magazineID=1&Itemid=73.

[4] Steve Watkins, "Mining the Heights," *Cincinnati Business Courier* (Apr. 6, 2012), http://www.hawthorn.pnc.com/assets/docs/Hawthorn_Cincinnati_announcement_0412.pdf.

[5] *Growing Older in America: The Health & Retirement Study* (Bethesda, Md.: National Institute on Aging, March 2007), http://www.nia.nih.gov/health/publication/growing-older-america-health-and-retirement-study/chapter-1-health.

[6] Vermont is the only state in the union that did not adopt a balance-budget amendment. The other 49 are all required by law to balance their budgets every year.

[7] Eric, T. Sondergeld, *The Facts of Life and Annuities* (Windsor, Conn.: LIMRA, 2009).

[8] Dave Lindorff, "Advisors Poised to Capitalize on Breakout Life Insurance Demand: LIMRA," *Financial Planning* (Sept. 7, 2011).

Market Drivers for 2020

Now that you have explored four future business scenarios, and seen some of our industry's risk and potential, it's time to drill into the three market drivers that underlie these scenarios. These three drivers will help you anticipate our industry's evolving client *markets*, the products and services that will provide these markets *value*, and the strategic *partners* who can increase your firm's market success.

By understanding how the industry's client marketplace is changing, you will be in the best position to plan now for your firm's mid- and long-term client focus and to put in place the value propositions and strategic partners that will best serve your clients' needs.

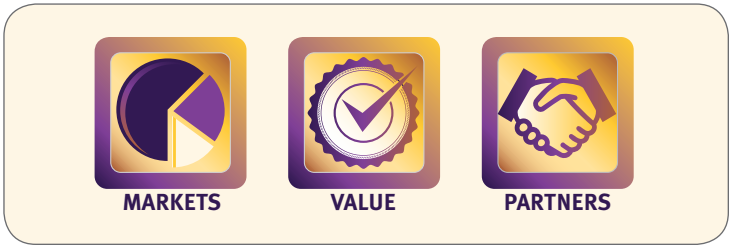
The three market drivers that will shape the firm in 2020 are:

- Baby Boomers and the new retirement culture
- New generations and the underserved middle market
- The changing business environment

For each market driver, our research presents:

- Forecasts for that market based on economic, demographic, and sociological trends
- Business opportunities emerging from the trends
- Questions to help you apply the findings and opportunities to your firm
- Drill-down information for those who want to explore the data and trends more deeply

You will find much to consider in the pages that follow as well as many exciting possibilities for your business. Enjoy!



MARKET DRIVER 1

Baby Boomers and the New Retirement Culture

For the firm in 2020, the market for insurance and financial services will be most influenced by how the Baby Boom generation adjusts to retirement.

Because of its size, wealth, and income, this generation will remain a powerful force in the job market and the economy for years to come.

The Boomers control more than half of the country's household wealth. How that wealth is managed will play a significant role in shaping the financial services industry — and the economic health of the nation itself — by the end of this decade.

In a case of fortuitous timing, Baby Boomers may also present a partial solution to the increasing challenge of attracting and retaining skilled talent to the financial services career. Field leaders should give serious consideration to when and how 59 million Americans, 40 percent of all workers, will leave the workforce — if, in fact, they will.

For these reasons and more, it is essential that financial services professionals understand Boomer expectations, desires, and concerns as Boomers enter their senior years.

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 41.*

Wealth and Income

The Baby Boomers are not simply the largest generation this country has ever produced; they also control a disproportionate share of its wealth and income.

When it comes to marketing products and services, field leaders ignore this generation at their peril. If financial services firms do not step up to meet Boomer needs and desires, other providers certainly will.

The numbers are impressive.

In 2009, the combined wealth of households headed by Baby Boomers, those between the ages of 45 and 64, accounted for 52 percent of all household wealth in the United States. (By comparison, the aggregate wealth of those under 35 years old accounted for less than 1 percent of all national household wealth.)

Boomer-headed households also accounted for 46 percent of all income in 2009.

Because of their longer life expectancies and their desire to stay economically active, Boomers will spend down their accumulated wealth much more slowly than did previous generations. Likewise, the income percentage for Boomers will shrink as more of them retire, but it will decline more slowly than for previous generations.

For these reasons — and others — Boomers will remain a powerful force in the economy for years to come.

Workforce Engagement

One of the primary distinctions of Baby Boomers as they enter their senior years is that they are in no hurry to leave the workforce.

Workforce participation among seniors has been increasing in recent years and is now doing so at an accelerating rate.

> According to BLS projections, by the year 2020, one in five Americans in the labor force will be 65 years old or older.

The Bureau of Labor Statistics (BLS) forecasts that by 2020, nearly 25 percent of seniors will still be working. For those aged 65 to 69, the workforce participation rate will be almost 30 percent. This level of senior workforce participation has not been seen since the mid-1960s.

Historically such participation had been the norm — it was only in the last few decades that earlier retirements became more common. Even before the financial crisis of 2007 to 2009, few Americans had the resources needed to support a retirement of 20 to 30 years.

Other factors contributing to today's later retirements include:

- Longer life spans that open the door to encore careers
- The attractive incomes that well-educated workers must give up upon retirement
- The increased investment in real estate associated with contemporary America's larger, nicer homes
- The very real concerns that older Americans have about access to health care

While the recent recession may have accelerated the trend of longer careers, it did not cause it. And for these reasons, even after household wealth returns to pre-recession levels, today's higher workforce participation rate by seniors is not expected to decline.

Encore Careers

For many seniors today, remaining in the workforce does not necessarily mean staying at the same job or even staying in the same occupation.

Encore careers — second careers started at age 50 or later — are increasingly attractive to those approaching retirement age.

A 20- to 30-year retirement presents an opportunity to craft a whole new career, one with purpose and meaning, without having to worry about fighting one's way up a career ladder or meeting the mortgage.

A third of those interested in encore careers, a potential 11 million workers, would prefer to transition into work that serves a "social purpose."[9] (See also sidebar on page 29.) Many will derive their new careers from past volunteer experience or a hobby.

Half of those interested in encore careers also note financial concerns — specifically health insurance coverage and possible reductions in Social Security or pension benefits — as motivations for staying active.

Starting a business later in life — essentially creating one's own encore career from scratch — is a related trend. A Kauffman Foundation study on trends in entrepreneurship found that Americans in their 50s and 60s are the fastest-growing segment of the new entrepreneur population. In 2011, Boomers accounted for approximately 52 percent of all self-employed persons and nearly 49 percent of all new entrepreneurs.[10]

Transitioning to an encore career typically requires an income bridge. Start-up capital will also be required for those desiring to launch their own businesses.

The widespread interest in encore careers by today's seniors presents a twofold opportunity for financial services firms:

- Offering products and services that will address the financial needs of seniors transitioning into encore careers
- Creating encore-career opportunities to attract talented seniors from other occupations to financial services

Why Work Past Age 65?
Survey respondents say it would:

- Allow them to stay active and productive
- Allow them greater control over their time, including the flexibility to take time off
- Allow them to keep learning, stay challenged, have new experiences, or develop new skills
- Provide them with an opportunity to help others
- Provide a sense of meaning and a feeling of accomplishment

The Skills Gap

One of the most important effects of Baby Boomers remaining in the workforce is that their encore careers can help to mitigate the skills shortage now hamstringing the U.S. economy.

At a time when the nation is facing chronically high unemployment, the United States, oddly enough, is also suffering from a serious skills shortage.

Unemployment has remained stubbornly high — but that is not because businesses are reluctant to hire. Businesses would gladly bring on new employees if they could find any who were qualified.

The vacancy rate — the number of firms reporting they were unable to fill positions for which they were actively recruiting — has been at pre-recession levels for more than a year as of the writing of this book.[11] Before the Great Recession, the last time vacancy rates for both the manufacturing and services sectors were this high, the unemployment rate was at 4.7 percent, well below what economists refer to as a "full employment" economy.

These data suggest that the unemployment problem is actually a "skills gap" between the skills employers seek and those the unemployed have to offer — it is not employer reluctance to bring on new workers.

This skills gap, which was already evident before the recession, is undermining economic growth in a number of industries, most notably professional services such as financial services.

In contrast to the high rate of unemployment generally, there is ongoing competition for college-educated workers.

Business Opportunities

OPPORTUNITY ONE
Encore Career Professionals

The desire to continue working is more common among the more educated. This means that the growing number of financial services workers in their 50s and 60s should be predisposed to continue working.

However, according to Civic Ventures, more than 70 percent of those considering encore careers — versus continuing in their current careers — are college graduates.[12] A desire for a career transition by large numbers of college-educated advisors will hit the financial services industry hard.

To keep senior producers engaged, and to attract encore career changers from other professions, field leaders must address the needs and desires of this population.

First, firms must more effectively define what they do in socially beneficial terms. They should not present themselves as sellers of financial services but as lifestyle advisors.

To attract encore career professionals, firms should position themselves by the value they bring (the outcomes of their services) rather than how they bring it (through their products and tools). This message will resonate with transitioning professionals — who are looking to do good and not just do well — and help attract them to the profession.

Changing the public's perception in this way is also essential to transitioning the profession from commissions to fees.

In addition, other priorities for encore careers — including part-time work and job-sharing arrangements — may not be readily compatible with traditional commission-based compensation.

While there is a broad-based desire to increase gender diversity in the industry, the need to attract and keep older financial advisors — with whom the growing number of senior clients can identify — might prove at least as important. And fortunately, focusing the career on the client's quality of life is a message that could prove just as effective with female professionals and younger generations as with seniors who want to stay engaged in the workforce.

VALUE

OPPORTUNITY TWO
Transitional Products and Services

The increasing numbers of encore career professionals, and the challenges of launching encore careers, will influence the types of products and services offered in the marketplace.

The Civic Ventures report recommended several methods to help an aging workforce retool and adopt new skills, technologies, and best practices, including:

- Savings programs and investment vehicles to assist people in financing their encore career transitions
- Policy changes that would make it easier to tap existing sources of funds
- Inexpensive and easily accessible training opportunities
- Expanded opportunities to earn a stipend while putting encore talent to work in areas of high need

Lifelong Learning Accounts (LiLAs) — employer-matched, portable accounts to finance workers' education and training — are an example of a product that makes education and training more accessible to workers.[13]

Today, seniors need help with the transition period between the first and second careers, a time when income drops off, often precipitately. Career transition planning represents a business opportunity for financial services providers.

New products are needed — to help finance a career change, create a new business, or form a nonprofit organization — that do not put the household's entire net wealth at risk.[14] By building access to start-up and operating capital into long-term planning and products, the industry can help senior entrepreneurs prepare for the costs associated with encore-career transitions.

In meeting this growing need, firms would benefit from partnering with organizations that help entrepreneurs launch new businesses. These include community colleges, state and local economic development agencies, the federal government-sponsored Senior Corp of Retired Executives (SCORE), AARP, and similar groups that focus on older career changers.

VALUE

OPPORTUNITY THREE

Holistic Value for the Client

Until now, retirement planning meant advising households on how to save enough money to cover the costs of catastrophic illnesses, relocation, or nursing-home care. Once retired, the client's plan was essentially put on autopilot. To help clients sustain their quality of life through 20 or 30 years, however, financial services professionals need to be more holistic in their approach.

As lifestyle advisors, industry professionals must have a better understanding of what happens between retirement and death. For example, clients who need their nest eggs to last three decades need to be advised differently — not on how to save for a catastrophic medical event, but on how to avoid such events in the first place.

Value-added services, such as aging-in-place strategies, and behavioral changes, such as personal health management, can ensure better long-term protection of wealth than can a savings plan.

In addition, a shift from retirement planning to lifestyle management creates new opportunities for financial services providers to transition from commissions to fees since the services related to lifestyle management are not related to the size of portfolio being managed.

Managing Decumulation

The greatest challenge facing current and future retirees will be managing the decumulation of their assets in a very uncertain future — especially when the chronic illnesses associated with aging begin to drain their savings.

Historically, the process has simply been a matter of saving for probable catastrophic events and using actuarial tables to estimate the total funds needed. But with retirements now stretching two to three decades, more comprehensive planning is required. People need to put as much planning into their retirements as they do into their careers and take a more active approach to managing, rather than responding to, life events.

Because extraordinary life events do not come in equal periodic installments, managing the *decumulation* of assets is not a simple exercise of dividing the total value of assets by life expectancy and setting up a payment schedule.

The skills and tools to manage asset decumulation will not be those of conventional financial management, but rather of lifestyle management, an area in which the financial services industry is not currently well equipped. According to Dr. Anthony Webb at the Center for Retirement Research, to date no one really knows how to manage decumulation.

Given longer life expectancies and the pervasive under-investment in retirement, saving enough money to pay for all anticipated risks is not possible in many cases. Managing asset decumulation means helping clients manage, and possibly develop strategies to avoid, unwanted events in the first place.

Consider:

Forty-three percent of Americans over age 65 will enter a nursing home at some point in their lives, with an average stay of 14 months and a median stay of five months.[15] Genworth Financial estimated

the cost of nursing home care at $222 per day in 2012, a 4.2 percent increase from 2011. In addition, Genworth estimates that the patient's out-of-pocket expenses for the typical nursing home stay will total an additional $14,000 and his or her primary care giver will spend another $8,000.[16]

The primary cause for a nursing home stay is an accident in the home, most frequently a fall in the bathroom.

Currently, agents and advisors help their clients save for the $55,000 or more needed to cover the costs of the nursing home stay. But the cost of renovations that would prevent a bathroom fall in the first place is only about $5,000.

Managing Lifestyles — Not Simply Assets

Helping households to manage the dispersal of wealth that needs to last 20 to 30 years requires a completely different set of knowledge, skills, and products than those currently at the disposal of insurance and financial services providers. Retirement management requires understanding clients' behaviors and managing their living environments in addition to their financial assets. The barriers that separate financial management from health management and property management are already beginning to blur as each one influences the other two.

To anticipate and mitigate risks to their clients' wealth, firms, rather than simply helping clients save for such contingencies, will need to develop relationships with home builders, health-care providers, and other community organizations that could influence the quality of their clients' lives. This suggests that larger firms with broader client bases would be more competitive in this environment.

Related changes are already taking place in the construction and health-care industries.

One of the fastest-growing areas in an otherwise-moribund construction industry is "aging in place" in residential design and remodeling.

The National Association of Home Builders (NAHB) created an aging-in-place certification to help seniors stay in their homes longer and with greater safely. For NAHB, aging in place is not just about renovating rooms; it is about understanding and managing a less mobile lifestyle.[17]

In the past, contractors and designers rarely took the health and aging of the resident into account when designing or renovating a room. Today that function has become a high-end, value-added service for which builders can charge a premium.

The health-care field is also becoming more engaged in lifestyle management.

The most expensive patient to treat is the older patient with multiple chronic conditions and reduced mobility. Thanks to the ubiquity of high-speed Internet access, health-care providers are beginning to install motion detectors in bedrooms, heat detectors in kitchens, and humidity sensors in bathrooms to monitor elderly residents' movements, cooking, and personal hygiene routines to ensure they are active and safe. Seniors are being taught to use Internet telephony such as Skype to speak with medical professionals and pharmacists without having to travel to a doctor's office or pharmacy.

Will those same seniors expect that kind of interactive communication and on-demand attention from those who are managing their life's savings? If the person on the other end of that email, tweet, blog, or Skype call is not a financial services professional, then who will that gatekeeper be?

The Multiline Connection

An emphasis on managing the living environment to reduce health-care costs provides an opening for the multiline insurance professional, which he or she could then share with other providers.

Tying health insurance rates to such accommodations would defray some of the costs to the policyholder, and provide new marketing relationship opportunities between multiline insurance agents, other insurance professionals, and renovation contractors.

Eventually this could lead to an aging-in-place specialization. The multiline agency could provide an integrated suite of products and services to help clients prepare for and finance lifestyle management investments that reduce risk, and then reward those who make the investments with more competitively priced products.

Likewise, financial services providers who include aging-in-place investments in their clients' plans could have the reduced risks associated with those renovations reflected in the client's premiums, making the investment more affordable to homeowners.

VALUE

OPPORTUNITY FOUR
Proactive Attention to Detail

Life insurance often serves as an investment vehicle and not just a survivor benefit. Thanks to several financially turbulent years, the cash value of a life insurance policy has become increasingly attractive, and its tax-free treatment has added to its appeal. In addition, while earnings from most equity accounts are subject to income or capital gains taxes, loans against the redeemable value of a life insurance policy are not.

As firms look to add value to their relationships with clients, attention to how life insurance policies are supported can make a tremendous difference in the client's experience. Consider several common policyholder events and how each could go devastatingly wrong for the client.

In today's low-interest-rate environment, policies have not performed as expected. If a policy was purchased for accumulation purposes, such as to fund a college education or to save for retirement, the policy may well be underperforming relative to how it was originally illustrated. However, unless someone reviews the policy's performance with the client, there would be no reason for her to think it isn't performing as originally discussed. The client could then find herself seriously underfunded at the exact moment the expected funds are needed most.

A similar need for proactive attention applies to using the growth of a policy's cash value to fund its premium. If the policy is underperforming, this approach will chew up the cash value until there is no money left, at which time a big premium will come due, and the policyholder will owe it all. In all likelihood, the client will not be expecting the bill, may not be able to pay it, and as a result, could be irreparably harmed or even die without coverage.

Finally, consider the risks that may be associated with policy loans that are not reviewed periodically with the client. These loans are, in a way, similar to home equity loans, which for years relied on the continued appreciation of the home to justify some nonproductive uses (such as hot tubs and vacations). It is important to recognize that when "nonproductive" uses of home equity loans eventually contributed to foreclosures, it was the lender — not the borrower — who was blamed for the product's misuse.

The same thing may be happening today with policy loans, and clients who assume that their policies continue to grow in value, negating the need to repay the loans, are facing a dangerous and unexpected outcome.

The critical question for each of these situations is the same: Is the advisor, or another properly licensed individual, going back to the client on a periodic basis to review the policy's performance against its purpose — and to recalibrate the planning process, if needed?

If that is not happening, then at some point clients may be shocked to discover that their financial plans have not achieved their purpose; that large and unexpected premium bills are due; that their life insurance coverage is at risk. In such cases, it is very likely that clients may hold their advisors and companies accountable, from both a financial and a reputation standpoint.

The Baby Boomers are entering their retirement years, and their expectations of their policies' performance will soon encounter reality. Turnover in the industry means that many Boomers are likely to be orphan policyholders and not receiving a periodic review. But even with an advisor, there's a good chance that any given client is not receiving annual attention.

What better opportunity exists for each advisor, each firm, each company, than to address the needs of their clients through regular reviews of the status of their policies? Proactive attention is key, because once a client discovers a problem on her own, it may well be too late to resolve it. And Boomers' individual and collective experience in situations such as these — as well as the attention they will draw to these issues — will strongly influence which firms and companies will earn policyholder and community loyalty.

PARTNERS

OPPORTUNITY FIVE
Partnerships for Lifestyle Management

America's community colleges are beginning to build some of the infrastructure needed to support senior lifestyle management.

In 2008, the American Association of Community Colleges launched a pilot project for its 50 Plus Initiative with 13 community colleges nationwide. The objective of 50 Plus is to "build the capacity to enable community colleges to respond to the workforce development and lifestyle needs of the population over 50 years old."

The program targeted four lifestyle areas:

- Workforce Training/Career Development
- Learning and Enrichment
- Volunteering
- Plus 50 Advising

Toward the end of 2008–12 grant period, 12 of the 13 colleges participating in the pilot announced that the demand for the courses and services was high enough for their 50 Plus programs to become self-sustaining. In the program's second phase, the 50 Plus Initiative has been expanded to include an additional 100 participating schools.

Incorporating a financial literacy component into these programs would be a natural fit, and one which the schools would welcome. (See pages 52–54 on the importance of financial literacy education.)

By including those who are still 15 years from retirement, the 50 Plus Initiative would provide financial service professionals with:

- Access to Boomers moving into retirement and encore careers
- A laboratory to develop the marketing and communications needed to expand middle-market penetration for products and services
- A communication channel to the next generation of clients

Insurance agencies and financial services firms should directly engage community colleges that have introduced the 50 Plus Initiative in their curricula. Larger firms might consider working directly with the American Association of Community Colleges[18] to identify the institutions involved.

By 2020, serving as an instructor for a course on financial literacy or a retirement-planning workshop may well have replaced the dinner or seminar invitations currently used by many financial planners to attract new clients.

Questions to Consider

One-Minute Debrief

1. Which Baby Boomer trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. How can your firm most effectively follow Baby Boomer clients into their retirement years?

2. Which of your available products could be repurposed immediately to support Baby Boomers who want to transition to encore careers?

3. How might encore career workers fill some of your firm's talent vacancies? How could you redefine the firm's work to make it more attractive to professionals transitioning in from other careers?

First Step

What *one thing* will you do this year to better position your firm to be successful in the expanding retiree market?

Additional copies of this worksheet can be found at gamafoundation.org.

Drill Down on Trends

Generational Size

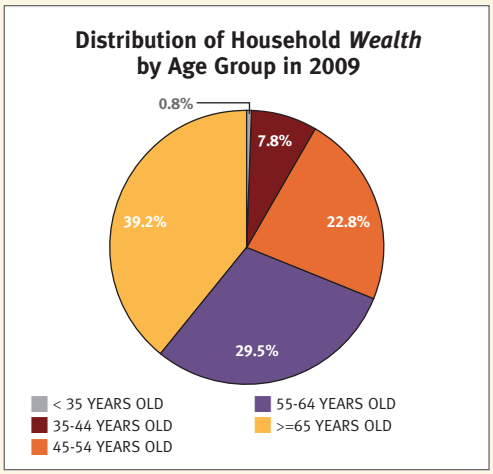
Population and Workforce Size by Generation				
Generation	**Birth Years**	**2010 Census**	**2010 Workforce**	**2020 Workforce Projection**
Silent Generation	Before 1946	40 million	5 million	2 million
Baby Boomers	1946–1964	81 million	59 million	39 million
Gen Xers	1965–1980	61 million	50 million	53 million
Workforce Millennials	1981–1995	85 million	38 million	51 million

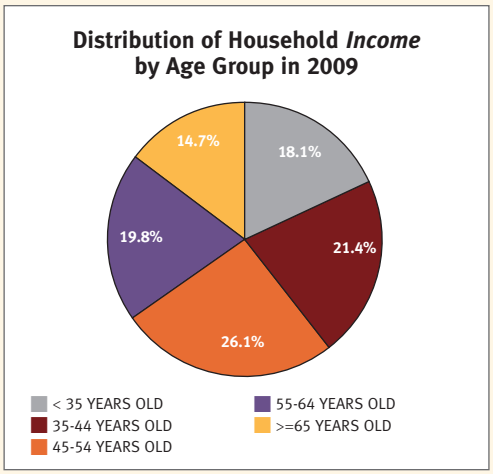
Study One uses U.S. population census counts, which include immigrants, when referring to the sizes of the different generations. There is no broad-based agreement on the birth years for the Millennial generation. The group we call Workforce Millennials are those who will be at least 24 years old in 2020.

Workforce numbers and projections are based on data from the Bureau of Labor Statistics, Office of Employment Projections (http://www.bls.gov/emp/ep_table_303.htm).

Generational Wealth and Income

Baby Boomers primarily fall into the age 45-64 sections of the following charts.





The Trend Toward Later Retirements

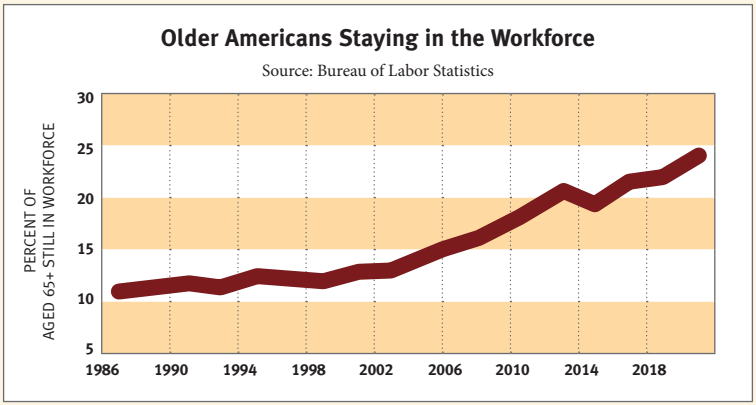
Life Expectancy

According to the Centers for Disease Control and Prevention, in 2009 life expectancy at age 65 in the United States reached 20 years. Those who make it to 75 can anticipate living for another 12 years.[19]

One reason for today's longer life expectancies was the country's shift to a service economy during the late 20th century. A service economy means that employment is less physically demanding — which contributes to longer life spans — and also means that today's workers are better able to stay in the workforce longer, if they so choose.

Early Retirements — A Trend Reverses

The trend toward earlier retirements in the late 20th century had reversed itself even before the 2007–09 financial crisis led many Americans to reassess their retirement plans.



After falling for most of the 1970s and 1980s, employment rates among those aged 65 and older began rising again in the 1990s. By 2010, the percentage of seniors (those age 65 and older) still in the workforce had nearly doubled from its 1986 trough.

The decline in retirement ages for men observed from the late 1970s until the 1990s was due in large part, ironically, to the surge in workforce participation by women. Female workforce participation rocketed from just 46 percent in 1960 to more than 70 percent by 1980, dramatically increasing household incomes and wealth. With much larger nest eggs than anticipated, two-income households were able to enjoy earlier retirements.

Dual Incomes and the Housing Bubble

Initially the growth in the number of two-income households fueled the rise in home ownership as well as allowing for earlier retirements. But then it led to spiraling housing prices as incomes rose faster than construction activity.

By the late 1990s, with Americans paying more money for ever larger and better-appointed homes, real estate investments had absorbed much of the second income,[20] helping to reverse the early retirement trend of the preceding decades. The percentage of total household spending devoted to housing expenditures increased by nearly a third, jumping from 15.5 percent in 1984 to 20.4 percent in 2010.[21]

Income Opportunity Cost

In addition to being the largest generation the nation has ever produced, the Baby Boomers are also its most educated. Because of draft deferments for college students adopted by the Nixon administration to defuse antiwar protests, record numbers of Boomers applied to graduate schools to avoid service in Vietnam.

Levels of education and income are closely related, meaning that the more educated an individual is, the higher the salary he or she must give up to retire. This higher opportunity cost associated with retirement has also contributed to extending careers. For many in the well-educated Boomer generation, retirement is simply too expensive a proposition to consider.

Retirement Readiness

With little time to recover from the financial crisis born of the 2007–09 recession, more than half of the 30 million households headed by someone aged 55 or older may be unable to maintain their pre-retirement standards of living after they stop working. A sharp drop in consumer spending of that magnitude by the nation's largest generation could trigger another severe recession in the not-too-distant future.

Health-Care Coverage

Medicare as currently defined and funded cannot sustain the demographic pressure of the Baby Boom generation. Some combination of cuts in coverage and increases in copayments and Medigap premiums are necessary to its survival.

Remaining in the workforce and being covered by employer-sponsored health care is among the more attractive options available to seniors.

In addition, long-term-care insurance, described by financial planners as the "greatest market opportunity that never was," failed to generate the interest anticipated when the products were first rolled out. Today, with the probability of long-term care now much closer, retirees find that long-term-care insurance is no longer affordable.

The Attraction and Challenge of Encore Careers

More Than the Money

According to author Marc Freedman, who coined the term *encore career*, there are already 9 million Americans engaged in second careers started at 50 or more years of age.[22]

In a 2011 survey of Americans 44 to 70 years old conducted by the MetLife Foundation and Civic Ventures, a nonprofit think tank founded by Freedman, 30 percent of those surveyed, representing a potential 31 million Americans, expressed an interest in launching a transitional career.[23]

The experience of those who had already transitioned into encore careers supports the emphasis on social priorities over income. Of the 9 million already in encore careers in 2011:

- 30 percent were working in education
- 25 percent were in health care
- 25 percent were in government
- 11 percent were working for nonprofit organizations

Financing the Transition

A 2008 Civic Ventures study found that the average time needed to transition into an encore career is 24 months. According to that study, "One of the biggest challenges of the transition is a financial one. Two-thirds say they experienced a significant drop in their income with nearly a quarter having no income at all during the transition period. And for a third, this decline in income extended over two or more years."[24]

According to the Civic Ventures survey, "Six in 10 (62 percent) of those interested in encore careers say they would consider working longer to establish an 'income bridge' that would enable them to postpone claiming Social Security and eventually claim a larger monthly check for life."

Entrepreneurship

Civic Ventures' *Encore Career Choices* research "found that as many as 25 million people — *one in four Americans ages 44 to 70* — are interested in starting their own businesses or nonprofit organizations."[25] This conclusion was confirmed in the Kauffman Foundation study on trends in entrepreneurship.

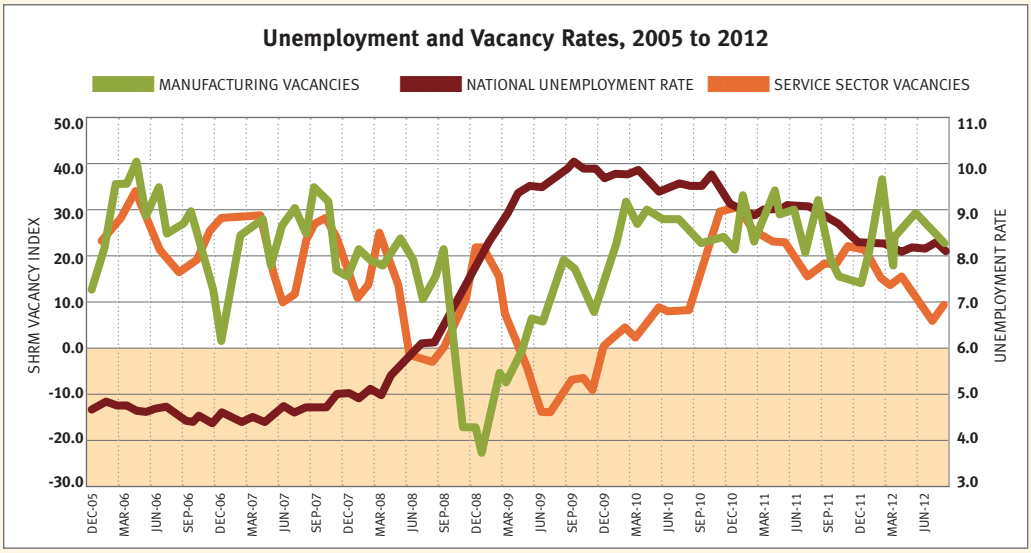
Many of those surveyed anticipate facing age discrimination as they transition to a new career, and a large number expect to have to strike out on their own to make the transition.

Share of New Entrepreneurs by Age Group

Age	1996	2011
Ages 20–34	34.8%	29.4%
Ages 35–44	27.0%	22.0%
Ages 45–54	23.9%	27.7%
Ages 55–64	14.3%	20.9%

Source: Robert W. Fairlie, University of California, Santa Cruz, using the *2010 Current Population Survey.*

The Continuing Skills Gap



College Graduate Employment Rate

In 2006, the unemployment rate for college graduates was only 1.8 percent. While the number of unemployed college graduates rose at the beginning of the recession, only recent graduates faced significant hurdles in finding employment. Even at its height, the unemployment rate for college graduates rose to just 5 percent. By 2012, it had fallen to 4.1 percent and has remained essentially unchanged since then.

Competition for Talent

The strong job market for college graduates is likely to grow even stronger. Lower birth rates in the mid-1990s point to a decline in the number of potential college graduates over the next eight years. This suggests that the competition for college-educated workers will grow more intense unless the country's immigration policies are liberalized.[26]

Professional services firms, including financial services providers, will be constrained by the growing skills gap in the job market, and they should evaluate how the current trend toward more restrictive immigration policies may affect their abilities to replace their advisor pools and grow their businesses.[27]

Competition for Career Changers

According to a University of Colorado study on financial planners, most are career changers. They spend an average of six years in another profession before entering the financial services field.

With today's skills gap and the increasing competition for talent, insurance agencies, financial planning firms, benefits advisors, and other financial services organizations may in the future face even greater difficulty in recruiting experienced talent away from other fields.

NOTES

[9] *Encore Career Choices: Purpose, Passion and a Paycheck in a Tough Economy* (Civic Ventures, 2011).

[10] Robert W. Fairlie, *Kauffman Index of Entrepreneurial Activity, 1996–2011* (Kansas City, Mo.: Ewing Marion Kauffman Foundation, March 2012), 11-12.

[11] Based on data from the Society for Human Resource Management (www.shrm.org), which conducts a monthly survey on hiring behaviors.

[12] *Encore Career Choices: Purpose, Passion and a Paycheck in a Tough Economy*, 9.

[13] LiLAs, enacted in 2011, allow for co-investment in worker education and training by the workers themselves, their employers, and even third parties such as local and state governments. Tax credits to either or both parties have been created to encourage investment in adult education for older workers.

[14] Several studies examined the outcomes for laid-off workers who used their severance packages to finance the start-up of a new business. Those who were successful started planning for their transition three to five years beforehand. Those who jumped into a new business venture spontaneously rarely succeeded.

[15] *Health Retirement Study* (Michigan: University of Michigan), http://hrsonline.isr.umich.edu.

[16] *2012 Cost of Care Survey*, Executive Summary (Genworth Financial, 2012), 3.

[17] NAHB's aging-in-place certification (CAP) focuses not only on the technical skills but also includes training in "emerging best practices in communicating and interacting with the evolving [senior] population." NAHB website: http://www.nahb.org/generic.aspx?sectionID=686&genericContentID=143173.

[18] The American Association of Community Colleges can be contacted at http://www.aacc.nche.edu.

[19] http://www.cdc.gov/nchs/hus/contents2011.htm#022.

[20] In fact, the square footage of just the garage in the average home built in 1995 was larger than the entire square footage of an average-size home built in the 1950s.

[21] *Consumer Expenditures Survey* (Bureau of Labor Statistics, multiple years), http://www.bls.gov/cex.

[22] Marc Freedman, *Encore: Finding Work that Matters in the Second Half of Life* (New York: Public Affairs, 2007).

[23] *Encore Career Choices: Purpose, Passion and a Paycheck in a Tough Economy*, 1.

[24] *Americans Seek Meaningful Work in the Second Half of Life: Encore Career Survey* (Civic Ventures, 2008).

[25] *Encore Career Choices: Purpose, Passion and a Paycheck in a Tough Economy*, 12.

[26] According to the Census Bureau's *2010 Current Population Survey,* immigrants entering the United States since 2000 are slightly more likely to have four-year degrees than native-born Americans (22.3 percent and 19.6 percent, respectively) and are significantly more likely to have advanced degrees (12.8 percent and 10.5 percent, respectively).

[27] *Current Population Survey, 2010 Annual Social and Economic Supplement* (Washington, D.C.: Census Bureau, 2010), http://www.census.gov/hhes/socdemo/education.

MARKET DRIVER 2

New Generations and the Underserved Middle Market

As the Baby Boomer generation moves into retirement, the financial services sector faces two major challenges.

One is how to continue to be compensated for serving the Boomers as they spend down their assets. The other is how to replace these older clients who will no longer be good candidates for traditional products and services.

Exhausting the supply of Baby Boomer home buyers was a principal trigger of the housing market meltdown, and that meltdown was the underlying cause of the 2007–09 recession. Financial services providers could face a similar fate if they cannot find new products and services to replace declining Baby Boomer demand.

For field leaders to maintain revenue and market share, the most obvious strategy is to expand the firm's market to a broader range of people — of different income and education levels — in the next generation. But this will not be easy.

The middle-market population is less motivated and less financially savvy than the upper-middle-class and affluent clients the industry has most recently targeted.[28] On the plus side, though, the middle market is quite large. The number of households with annual incomes between $35,000 and $100,000 is more than twice the number earning more than $100,000.[29]

The challenge for financial services professionals will be stimulating demand for greater savings within a more resistant population. Understanding this population and its financial mind-set will be key to middle-market success. Also, because prospective middle-market clients lack the motivation and sophistication of traditional clients, firms will need to adopt different techniques for prospecting.

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 63.*

MARKETS

Generation X

Generation X, the generation immediately following the Baby Boomers, is significantly smaller and less wealthy than its predecessor. At 61 million, Gen X is just two-thirds the size of the Baby Boom and suffered disproportionately from the financial crisis.

While the burst in the real estate bubble was a shocking blow to most households, it proved devastating for those in their 30s and 40s, whose net wealth at that time in their lifecycles was heavily concentrated in real estate.

A study by the Pew Research Center compared differences in net wealth by age group from 1984 to 2009. That research found a dramatically growing generational wealth gap. *According to the Pew Charitable Trust, in 2009 the net wealth of this age cohort was 44 percent lower than that of the same age group a generation earlier.*

While Gen X still has 20 to 30 years to make up the difference, the compounding effect of so substantial a loss in wealth suggests that senior workforce participation will remain high even when those now in their late 30s and early 40s reach retirement age.

Given their reduced resources, Gen Xers' motivation to rebuild should be quite high. By 2020, with more Boomers retired, Gen X should account for more than 40 percent of household income, making it the greatest wage-earning generation at that time.

The most traditional method for increasing wealth is through intergenerational wealth management — when senior parents and their adult children work together to manage the transfer of wealth from one generation to the next. But the Boomers' longevity means that they will substantially spend down their wealth. So replacing Boomer clients will take more than simply following their assets to their next of kin.

On the positive side, the homeownership rate for Gen X is quite high. Even after the bursting of the real estate bubble and losses from foreclosures, the Gen X homeownership rate was 65 percent in 2010, only slightly below the 68 percent national average.[30] This means that by 2020, compared with younger age groups, more of Gen Xers' discretionary savings from their income will be available to invest in assets other than real estate.

The Millennial Generation

Approximately 60 percent of the 85 million Millennials, those born since 1985, will be in the workforce by 2020.

Because of their youth, the Millennials were not overly exposed to real estate investment when the housing bubble burst. But they were also too late to build wealth from the run-up in home values in the 1980s and 1990s.

In addition to not benefiting from the housing boom, a large share of the Millennial generation went to college.[31] While in the long run beneficial to themselves and society, their advanced education also means that many of them postponed entering the workforce for at least four years, plus they acquired much higher college debt burdens — both of which have negatively affected their net worth.[32]

According to the Pew Charitable Trust, in 2009 those under 35 had a median net worth that was just a third of that of their counterparts from 25 years earlier.

While it is too early to make any claims about the Millennials' potential value as clients in 2020, there are two observations that lead one to question it.

First, nearly 30 million Millennials entered the workforce — or more accurately tried to enter the workforce — just before or during the Great Recession. The unemployment rate for this age group surged from 7.2 percent in 2007 to 17.1 percent in 2010.

The ripple effect on earnings and savings for those entering the workforce during a recession are quite profound. Many accept much lower salaries and enter suboptimal career paths that lower their wages for years and possibly their entire careers.

Second, the Millennial generation may face much higher social costs and tax rates than its predecessors.

By 2020 there will be only 1.5 workers for every person not in the workforce because they are either too young or too old. This ratio, called the dependency rate, stood at 1.7 in 2010 and is expected to fall to just 1.3 by 2030.

With fewer workers per retiree, either social entitlements will have to be cut or taxes will have to be raised. Those over 65 years old have much higher voter turnout rates than younger voters. Add in the size of the Baby Boom now entering retirement, and the senior voting block will be a powerful political force in 2020 that will be unlikely to vote for having its benefits cut. Taxes on those in the workforce will most likely rise.

One of the few striking features of the Millennial generation so far is its preference for renting just about anything. The percentage of 29- to 34 year-olds holding mortgages is only half of what it was just 10 years before. From Zip Cars to Rideshare bicycles, Millennials are mirroring the risk-averse strategies developed by manufacturers and retailers 30 years ago by taking a "just-in-time" approach to major personal needs.

If this pattern holds, it suggests that in time this generation will not divert as much of its savings to housing as did prior generations — which could make Millennials more open to investing their savings in other ways. However, that tempting possibility is beyond the horizon of this research.

Invisible Income Losses

In addition to the recession-driven losses in home equity and financial assets, younger generations and the middle-income groups have been hit especially hard by what are often referred to as "invisible income losses" from cuts in employer-sponsored voluntary benefits programs.

The most widely discussed of these have been cuts in employer-sponsored health-care coverage. An overwhelming majority of employers have shifted a significant share of health-care costs onto their employees.

These cost shifts are often unrecognized or underestimated by employees until a catastrophic medical event occurs. This is especially true when employers have switched to high-deductible catastrophic-care health plans, for which the deductibles can be thousands of dollars. Few households have augmented their savings patterns to ensure sufficient liquidity to cover a major medical expense. Unanticipated medical costs are the second major reason for home foreclosures behind loss of a job.

Another "invisible income loss" with a major impact on household savings has been the decline of traditional defined-benefit pension plans. According to David Wise, an economist specializing in the economics of aging, "Just two to three decades ago, employer-provided defined-benefit pension plans were the primary means of saving for retirement in the United States."[33] However, according to Boston College's Center for Retirement Research, the percentage of employees covered by defined-benefit plans fell from 62 percent in 1987 to only 17 percent by 2007.

Employees' participation in voluntary contribution plans like 401(k)s falls far short of the "forced savings" accomplished through defined-benefit plans. As a result, aggregate household savings rates have declined much further than is apparent.

Retirement (Un)Readiness

Due to misguided over-investments in real estate, lower overall savings rates, and the erosion of employer-provided benefits, the financial future for American households may prove to be even more daunting than the challenging years immediately behind us.

According to RetirementUSA, a think tank committed to reforming Social Security, the combined shortfall in retirement savings by all American households is $6.6 trillion, or $250,000 per household, assuming continued low inflation rates.

In 2010, McKinsey & Company introduced its Retirement Readiness Index (RRI) to demonstrate how broad a share of the population is vulnerable to underinvestment. The study's alarming conclusion was that average household income for retirees, based on 2009 numbers, was only 63 percent of the amount needed to maintain the household's pre-retirement lifestyle. While those closest to retirement age fare somewhat better, their RRIs still indicate that they would need to make substantial cuts in discretionary spending to get by.

This vulnerability included not just low-income but all middle-income groups as well. "While lower- and moderate-income households are least prepared, most Americans — even in middle- to higher-income households — will fall well short of their retirement expectations."[34] That kind of belt-tightening could throw the economy into recession, possibly before or around 2020.

Yet the McKinsey study concluded, "The good news … is that Americans are now acutely aware of their predicament and, with the right guidance, can act to fix it." Whoever provides that guidance will greatly shape future savings patterns, and, in turn, consumer demand for insurance and financial services. Industry professionals should not postpone addressing this issue. Time is not on our side.

Middle-Market Savings

For several decades, two outside forces have encouraged the American middle class to invest in financial products and services: tax incentives to encourage savings and mandatory employee benefit participation to compel savings by default.

The most common approach is the former. Consumers have been encouraged to increase their savings through a series of tax-deferred savings plans such as IRAs, 401(k)s, medical savings accounts, and, most recently, lifelong learning accounts.

The programs have been largely successful. But middle-market households have lower participation rates in voluntary savings programs than do more affluent households. For example, with defined-contribution plans such as 401(k)s, the core determinants of whether someone participates are income and education. Managers and professionals post a 79 percent participation rate, while only 50 percent of service sector employees participate.[35]Mandatory programs to encourage greater personal savings have proven very effective in expanding participation. Several studies have demonstrated that worker participation increases significantly in 401(k) programs in which employers apply an "opt out" versus "opt in" policy.[36]

Still, as more households take advantage of pre-tax savings incentives, less money is left in their paychecks for discretionary purchases. Savings rates outside of tax-deferred savings plans now trend consistently below 5 percent, suggesting that there is little discretionary income left for households to save even more. This creates challenges for the financial services professional, whose products may not be a priority in those households.

It is unlikely that expanded legislative or employment policies will provide enhanced access to middle-market households. With structural budget deficits at the federal and state levels, legislators are unlikely to support new or expanded tax-deferred savings plans that would further reduce income tax revenues. Likewise, employers are unlikely to expand mandatory participation in voluntary benefits. With rising health-care costs consuming an ever-growing share of total compensation, employers are reluctant to make workers' paychecks any smaller than they already are.

For these reasons, financial services providers who serve the middle market should be prepared to sell products inside of existing tax-deferred savings plans, to compete against those plans for households' long-term savings dollars, or to focus on workers who do not currently receive voluntary employee benefits.

Middle-Market Confidence

Savings patterns are not determined simply by income. The general consensus within the research literature is that there are three nonfinancial causes of lower savings participation rates for non-affluent households. To grow successfully in the middle market, firms must understand and address these issues:

- Lower levels of financial literacy
- Distrust of financial institutions
- Lack of access to professional advice

Financial Literacy

Financial literacy is closely correlated with education, socioeconomic status, and income.

The middle market, being generally less financially literate than the affluent market, is understandably less comfortable in selecting products for saving or investing its money. In general, a less financially literate prospect may do the following:

- Become paralyzed by too broad a range of choices
- Perceive retirement planning and saving to be much harder than it is
- Perceive defined-contribution withholdings as a reduction in current income rather than as deferred consumption

To better address the needs of this market, then, firms should do the following:

- Offer products that are simple rather than complex
- Offer products that are customized to the client's needs
- Offer access to financial education from a trustworthy source

Research conducted by the Employee Benefits Research Institute found that there is an inverse relationship between the number of options offered to an employee and his or her participation in any of them.[37]

As noted above, research has also found that employees with low levels of financial literacy may perceive retirement planning and saving to be much harder than it actually is. Indicative of this is a 2005 study of a representative cross section of the U.S. adult population conducted by the Consumer Federation of America and the Financial Planning Association. Their research found that:

- Only one in four respondents (26 percent) believed that they could ever save $200,000 over the course of their entire lifetimes.[38]
- Fifty-five percent of respondents agreed that "saving something each month for many years" was "the most practical way to accumulate over $100,000" — but 21 percent selected "playing the lottery."
- Nearly 40 percent of those making less than $25,000 per year viewed the lottery as the most practical approach.

Trust and Advice

Research has shown that distrust of financial institutions reduces employees' willingness to participate in defined-contribution plans such as 401(k)s. When employees with lower levels of trust do participate in these plans, they tend to choose the most risk-averse option, which often results in lower lifetime savings.

But the trust issue goes further than plan participation. A study by the National Bureau of Economic Research found that only a small fraction of households consult financial advisers, bankers, certified public accountants, or other professionals when making major financial decisions.

What sources of information does the broader public turn to instead of professionals?

To help make financial decisions, most households, and particularly those with lower education levels, rely on informal sources of advice such as family members, friends, and peers — people they know and trust. Yet those sources of advice are unlikely to be the most knowledgeable, further limiting the household's ability to plan and save effectively, the study noted.

"Insofar as there is a positive correlation between the education level of the individuals and the education level of the family or peers, low-education individuals may simply rely on crude sources of advice. Similarly, those with low financial literacy may be particularly disadvantaged in overcoming lack of knowledge."[39]

A reliance on secondary, and possibly uninformed, sources of advice increases the costs of prospecting among these households. Firms and advisors will need to appeal to prospective clients' families, friends, and peers through social networking, consumer education, and outreach to market influencers.

In addition, one likely reason for turning to family and friends for advice is that less financially savvy households are a prime target for financial fraud. This has made them wary of unsolicited offers to provide financial services and of promises of future riches — no matter how true such an offer might be. Advisors with a personal interest in a financial transaction will understandably be regarded as suspect.

According to the Federal Trade Commission, there were nearly one million cases of consumer fraud in 2011, a 62 percent increase in just the four years since the recession began. These are just the reported cases. Many more go unreported because victims often feel embarrassed, and many may not even be aware they have been scammed.

To sell effectively in the middle market, then, providing a credible source of information and advice is an issue that must be addressed.[40] In addition, firms themselves will need to be more fully engaged in educating potential clients.

Business Opportunities

OPPORTUNITY SIX

Reposition the Value Proposition

The industry must ensure that its messages, its actions, and its results are relevant to the financial needs and desires of the American consumer.

A significant change in the general public's perception of the industry will require involvement from major industry players on a national stage. But change can happen quickly and substantively at the local level when firms and their representatives decide to make it happen.

Financial products and asset management services are means of ensuring long-term financial security. They are part of *how* financial service providers do what they do, but not *what* they do.

Emphasizing the value of what industry professionals bring to their clients — the ability to sustain a quality of life throughout a lifetime — is a message that will resonate strongly with the public when backed up by appropriate actions, including outreach to the broader middle market.

A change in the general public's perception of the industry will be necessary if the industry is to successfully offer a broader range of services, transition compensation from commissions to fees, and attract more encore, female, and young professionals to the career.

Ultimately, financial product manufacturers, working with insurance industry organizations, professional societies, and other civic organizations, should develop a national public relations campaign to communicate and sustain these messages.

OPPORTUNITY SEVEN

Partnerships for Financial Literacy

Financial services professionals can and should help to solve the country's financial literacy problem. They, their firms, and their communities will benefit from this educational approach to social marketing.

And as noted when discussing the 50 Plus Initiative earlier, serving as an instructor for a course on financial literacy may well replace the dinners and seminars currently used by many financial planners to attract new clients.

That said, trust in institutions and third-party experts will be essential to increasing the demand for insurance and financial services in the broader marketplace. Partnering with reputable third parties to provide financial education will help firms insulate themselves and their representatives from the public fallout from the increase in financial fraud.

In addition, third parties with no vested interest in specific products or services have greater credibility in influencing consumers to take action. The more closely financial services firms associate with these groups, the more credibility they gain by association.

Firms will particularly benefit by working in partnership with employers' human resource departments, local schools and community groups, and nonprofit organizations such as the Financial Security Project as part of their middle-market initiatives.

Organizations such as the Center for Retirement Research, the National Endowment for Financial Education,[41] and even community colleges (see the 50 Plus Initiative on page 38) are eager to provide employers, insurance agents, and financial advisors with reference materials, easy-to-follow workbooks, and other educational tools that will not intimidate individuals who have low financial literacy.

The Center for Retirement Research launched the Financial Security Project (FSP) in 2010 to create educational tools to promote greater financial literacy.[42] The FSP provides employers, financial services providers, and employees with independent, unbiased materials that a person can trust to walk him or her through financial planning decisions, including evaluating the need to save and how best to do so.

When firms provide volunteers to participate in financial literacy courses, workshops, and other educational events — and use credible, independent third-party materials to help people make decisions — they can build the comfort level and confidence that middle-class Americans need to commit to a long-term financial plan.

In addition, the industry's product manufacturers have the resources to work with organizations such as the Financial Security Project and the 50 Plus Initiative to directly improve the country's financial literacy. These companies also have the clout to capture the attention of legislators at the state and federal levels to engage the public resources needed to address an issue that has the potential to undermine the viability of the economy.

VALUE

OPPORTUNITY EIGHT

Social Marketing Through Community Outreach

By working in partnership with independent third-party organizations, financial services firms can increase the market penetration of their products while helping to improve the financial literacy and financial confidence of a great many people.

Effective financial education will need to address barriers to financial literacy in the middle market by:

- Focusing on "can do" goals versus "should do" messages
- Demonstrating that retirement planning and saving are not hard to do
- Showing how savings products defer consumption rather than reduce income
- Demonstrating trustworthiness through credible, independent sources of information

Research conducted by Boston College's Center for Retirement Research on promoting financial literacy found that people were more likely to engage in financial planning in response to a positive goal such as "to sustain a quality of life," rather than a negative one such as avoiding financial disaster. Dr. Steven Sass, associate director for the Financial Security Project at the Center, explained, "The message that people need to save more is getting a bit tired."

For middle-market audiences, multiple education sessions[43] — and a multipronged communication strategy, through which financial education and information are provided by way of several venues — is recommended.

Research has also found higher savings participation rates when the financial training is closely followed by an opportunity to act on the training. This suggests that firms should include social media in their marketing programs to provide low-pressure opportunities for people to purchase products once they are predisposed to do so.

Given that households with lower levels of financial literacy depend on the opinions and recommendations of peers in making financial decisions, social media is an obvious tool through which to educate and nurture relationships with these households.

OPPORTUNITY NINE

Customized Products for New Markets

Middle-income clients, who are generally less financially literate than the more affluent, may become paralyzed by too broad a range of product choices. This speaks to the need for less complex products and more customized product offerings for the middle market.

As noted earlier, there is an inverse relationship between the number of benefits options offered an employee and his or her participation in any of them. Therefore, financial services providers should customize their product offering to suit the specific needs of the client or, if working with employers, the common characteristics of the workforce of the firm.

Customizing offerings to suit specific target populations adds to the cost of servicing them. But this flexibility should play to the advantage of agents and advisors over brokers.

MARKETS

OPPORTUNITY TEN

Set the Stage for the Next Generation

The Millennial generation will not yet be a major influencer of insurance and financial services in the year 2020. But they will be poised to become a force.

In 2020, many Millennials will be in their 30s, an age when insurance and financial services become more important.

This is the generation that mastered multitasking and information overload, and it may be that good managers of information will also prove to be good managers of money. In addition, that ability may make them more discerning in their financial decisions and their product selections.

Being a highly educated generation, Millennials will have the incomes to invest. And if trends hold and they prove to be less likely to commit to real estate investments than past generations, more of their income will be available for savings and investments.

Questions to Consider

One-Minute Debrief

1. Which middle-market trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. What organizations in your community could your firm partner with to improve financial education and planning for the middle market? How might you work with each partner to strengthen the finances of middle-market households?

2. Which of your available products could be repurposed immediately to support Baby Boomers who want to transition to encore careers?

3. Which of your available products and services address the basic needs of the middle market, including product simplicity and customization? How should your firm position its products and services to focus on the *outcomes* to be achieved rather than the savings or planning *activities* to be done?

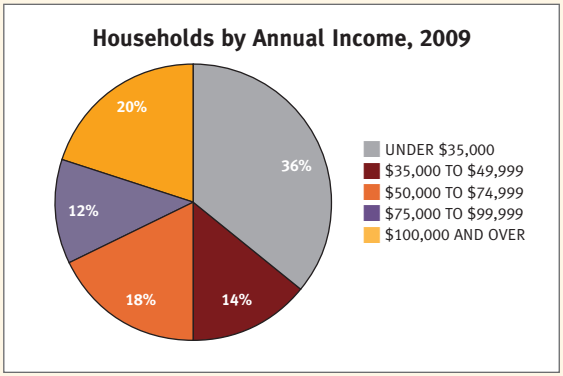
First Step

What *one thing* will you do this year to better position your firm for success in a broader cross section of the middle market?

Additional copies of this worksheet can be found at gamafoundation.org.

Drill Down on Trends

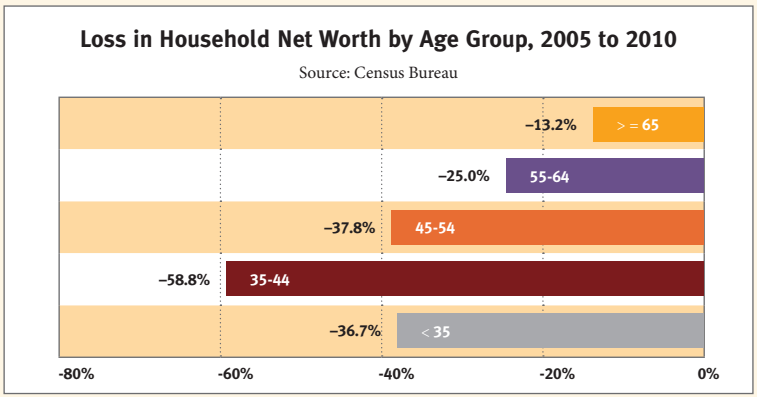
Households by Annual Income[44]



Gen X and the Millennials

Gen X

The Census Bureau estimates Americans 35 to 44 years old experienced a 59 percent decline in household wealth as a result of the 2007–09 recession. This is more than double the 24 percent decline reported by those aged 55 to 64, on the verge of retirement, and more than four times greater than the decline in household wealth reported by those already old enough to retire.



Using the Census Bureau's *Current Population Survey,* Change Management Solutions estimated that households headed by Gen Xers accounted for 26 percent of total household income in 2009, as compared with Boomers' share at 46 percent.

The Millennials

The following chart shows differences in household net worth, comparing current generations with those from 25 years before.

Median Net Worth by Age of Householder, 1984 and 2009 (In 2010 dollars)			
Age Group	**1984**	**2009**	**Change**
All	$65,293	$71,635	10%
Younger than 35	$11,521	$3,662	-68%
35-44	$71,118	$39,601	-44%
45-54[1]	$113,511	$101,651	-10%
55-64[1]	$147,236	$162,065	10%
65 and older	$120,457	$170,494	42%

[1]Baby Boom generation
Sources: Pew Research Center tabulations of *Survey of Income and Program Participation* data and Census Bureau, P-70, No. 7 (1984).

Real Estate

Facing higher housing prices and more years of schooling, the younger generations are postponing the purchase of their first home. According to Census Bureau housing statistics, the average age of the first-time home buyer rose steadily from 28 years old in the 1990s to 33 years old in 2009. In 2020, the oldest of the Millennials will be just 38.

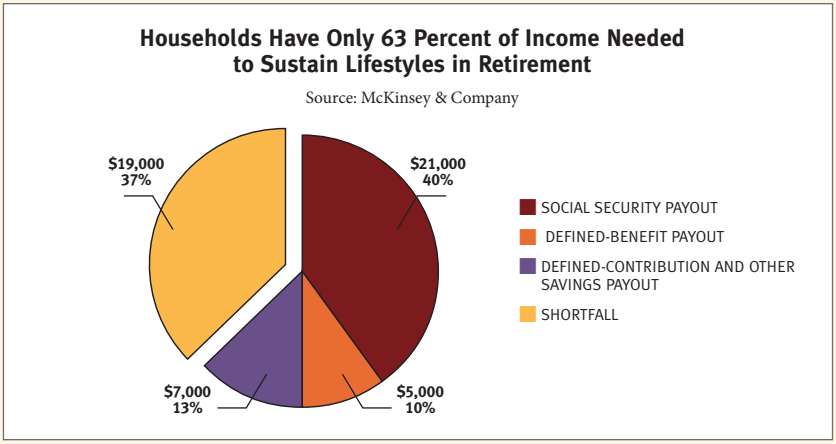
Retirement Readiness

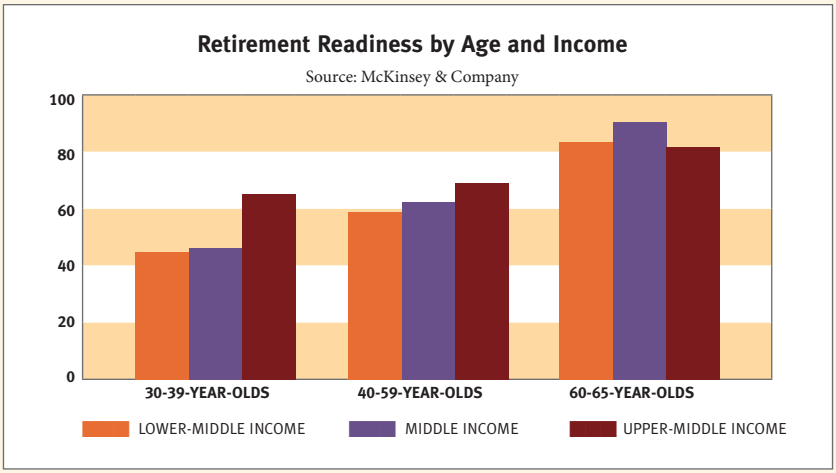
Calculating the Retirement Readiness Index (RRI)

The McKinsey & Company RRI is calculated by comparing all of the household's post-retirement income with the amount of money needed to maintain the household's pre-retirement lifestyle. Households with just enough savings to generate the income needed to maintain their pre-retirement lifestyle would be assigned an RRI of 100.

McKinsey estimated that the average household would need an annual retirement income of $52,000 to avoid cuts in discretionary spending. The researchers then combined all sources of income and all other savings and found that average household income for retirees would only total $33,000 (at current rates of return) or just 63 percent of the amount needed.

The McKinsey study concluded that households with RRIs between 80 and 100 would be able to survive, although at a lower standard of living through cuts in discretionary spending. But an RRI below 80 would mean sacrificing spending on essential needs such as housing, food, and health care. An average RRI of 63 is, to say the least, disquieting.



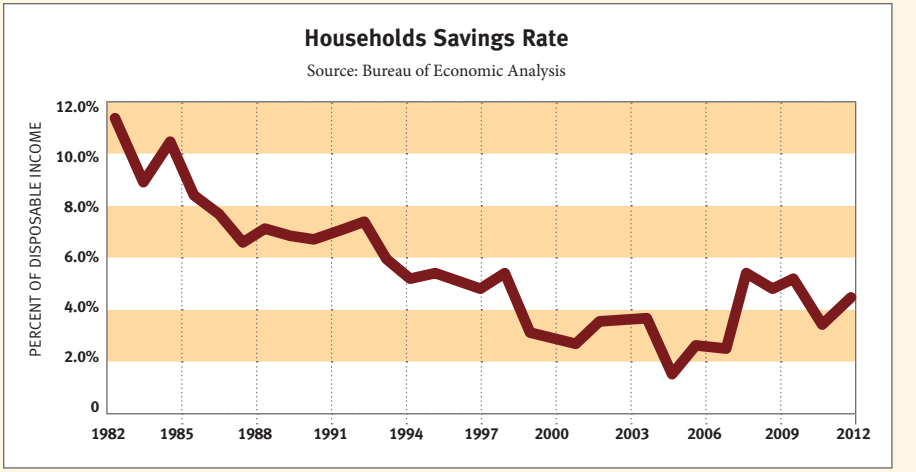


Savings Trends

Households Savings Rate

The national savings rate published monthly by the Bureau of Economic Analysis (BEA) is defined as that portion of disposable personal income, or "take home pay," that is not spent.

The savings rate, calculated as savings divided by disposable personal income, was an accurate measure of household savings until the 1980s. Then in 1983, individual retirement accounts were introduced, and since then the Congress has added a series of tax-deferred plans to encourage savings for retirement, education, and health care, and to lower tax obligations by reducing taxable income. Contributions to tax-deferred savings plans are not included in the BEA's calculation of the national savings rate.



A major reason why the savings rate fell from nearly 11 percent in 1982 to a low of 1.5 percent in 2005 was because of participation in pre-tax savings plans — contributions to those plans are not counted in the household savings rate. The increase in the saving rates from 2008 through 2010 reflected households' concern for greater liquidity during and after the Great Recession, leading them to contribute less to pre-tax savings plans. The slightly lower rates reported in 2011 and 2012 could suggest that more households are again putting more of their income into pre-tax savings.

Mandatory or "Opt-Out" Plans

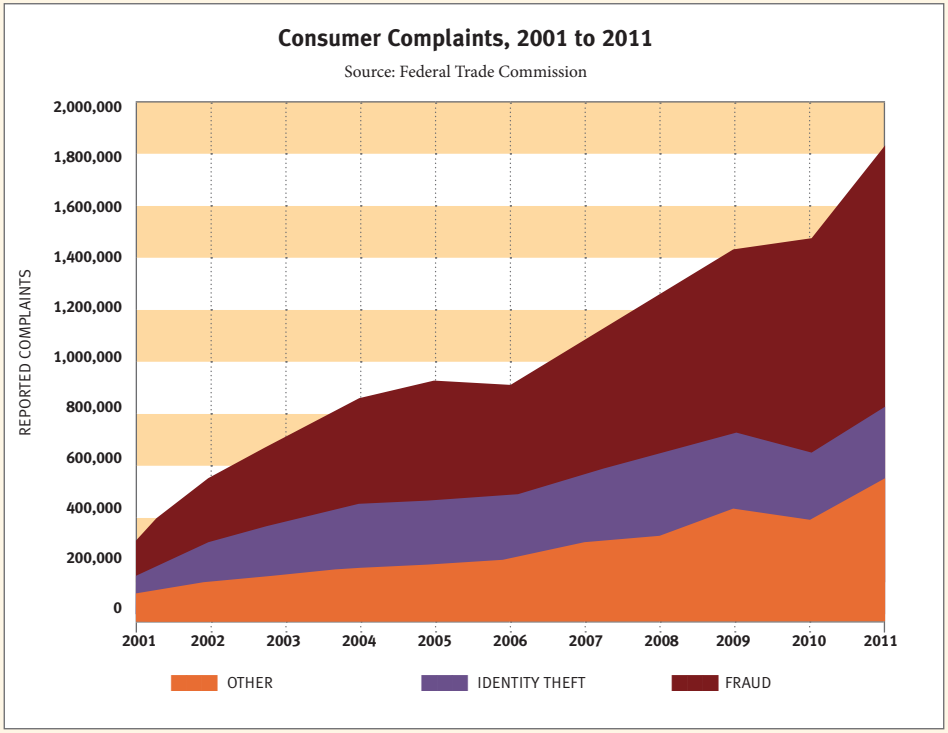
Some studies found that in opt-out plans, more employees leave their 401K contributions at the employer-set minimum in a low-risk plan rather than evaluating their choices and setting up their plans themselves. *As a consequence, while more employees are contributing to their retirements, more employees are also saving less than they would have if the initial decision had not been made for them.*

Financial Literacy and Confidence

Financial Literacy

The Center for Retirement Research at Boston College administered a study to evaluate respondents' financial literacy.[45] The researchers concluded that low levels of financial literacy result in a 30 percent lower participation rate in opt-in plans and a 13 percent lower participation rate in opt-out plans that could not be explained by changes in income or tenure with the firm.[46]

Interestingly, 67 percent of employees who chose not to participate in a voluntary program and 74 percent of those who deliberately opted out of an automatic enrollment plan reported that they were participating. This suggests that either they did not understand the forms they were signing when they started working or they do not distinguish between a defined-benefit pension plan, assuming the employer offers one, and a retirement savings plan.



Financial Fraud

Consumer reports of financial fraud have grown rapidly over the past decade (see chart), with the Internet being the primary vehicle for that growth. While the total number of consumer complaints against businesses has grown fivefold from 2001 to 2011, the number of consumer fraud charges has grown sevenfold over the same period, according to the Federal Trade Commission. Fraud accounted for 42 percent of all consumer complaints in 2001 and more than 55 percent a decade later.[47]

The Internet has made financial fraud more pervasive, and authorities fear that as Baby Boomers engage more in social media, opportunities for scams that can drain people's savings will become even more common.

NOTES

[28] Upper-middle-class and affluent clients are defined as those with household incomes above $100,000.

[29] *Income, Poverty and Health Insurance Coverage in the United States: 2009, Current Population Reports,* Series P60-238 and Detailed Tables (Washington, D.C.: Census Bureau, 2009).

[30] *Housing Vacancies and Home Ownership* (Washington, D.C.: Census Bureau), http://www.census.gov/housing/hvs/.

[31] By 2010 nearly 30 percent of the adult population held at least a bachelor's degree, compared with 20 percent in 1984. Most of these gains were enjoyed by minority populations, whose proportion of college graduates essentially doubled, jumping from 11 percent to 20 percent over the same period.

[32] The ratio of the average entry-level salary for a college graduate to the average cost of an undergraduate degree fell from 50 percent in 1980 to 25 percent in 2005.

[33] David A. Wise, James Poterba, and Steven Venti, *The Decline of Defined Benefit Retirement Plans and Asset Flows* (Washington, D.C.: National Bureau of Economic Research, August 2006).

[34] *Restoring Americans' Retirement Security A Shared Responsibility* (McKinsey & Company, 2010).

[35] The participation rates increase with company tenure and among married workers, regardless of education or income.

[36] Different studies have yielded a range of nonetheless impressive gains in participation from opt-out defined-contribution programs, with increases in participation ranging from just under a 50 percent increase in participation to nearly doubling the percentage of enrolled workers.

[37] Jodi DiCenzo, *Behavioral Finance and Retirement Plan Contributions: How Participants Behave, and Prescriptive Solutions,* Issue Brief 301 (Washington, D.C.: Employee Benefits Research Institute, January 2007), 11.

[38] The median household income in 2005 was $46,326 according to Census Bureau's *Current Population Survey* estimates. To save $200,000, a 30-year-old earning the median household income, need save only $217 per month until turning 65, assuming a 4 percent rate of return. The savings rate would only be 7.5 percent in post-tax dollars or 6.0 percent in pretax dollars.

[39] Annamaria Lusardi, *Household Savings Behavior: the Role of Financial Literacy, Information, and Financial Education Programs,* Working Paper 13824 (Washington, D.C.: National Bureau of Economic Research, February 2008), http://www.nber.org/papers/w13824.

[40] This finding suggests that for this population, truly independent agents and advisors, plus independent financial services firms, would be considered more credible than captive agents and advisors. But lower economies of scale and higher operating costs make independent agents less competitive. Unless clients are willing to pay the higher fees for the greater transparency they claim they want, these higher costs could lead to greater consolidation among independent agencies.

[41] http://www.nefe.org.

[42] http://fsp.bc.edu/.

[43] Lusardi, *Household Savings Behavior: The Role of Financial Literacy, Information, and Financial Education Programs,* Working Paper 13824, http://www.nber.org/papers/w13824.

[44] *Income, Poverty and Health Insurance Coverage in the United States: 2009, Current Population Reports*.

[45] Three questions in the study measured basic financial knowledge and five measured knowledge of the employers' financial benefits. They compared the results of the quiz to participation rates in defined-contribution plans. To see the entire list of questions see Appendix A.

[45] Julie R. Agnew, Lisa Szykman, Stephen P. Utkus, and Jean A. Young, *Literacy, Trust, and 401(k) Savings Behavior* (Newton, Mass.: Center for Retirement Research at Boston College, April 2009), http://www.bc.edu/crr.

[47] *Consumer Sentinel Network Data Book* (Washington, D.C.: Federal Trade Commission, multiple years).

MARKET DRIVER 3

The Changing Business Environment

Firms that provide voluntary benefits to employers will see fundamental changes in the kinds of businesses they serve in 2020.

The businesses driving the recovery today are health care, private adult education providers, manufacturers, and professional services such as management consulting, financial services, and administrative services. They are very different from construction, real estate, retail, and consumer finance — the industries that drove the economy before the 2007–09 recession.

The businesses emerging from the recovery are less likely to offer defined-benefit plans and other financial benefits to their employees, both because of their size and the economic sectors in which they operate.

Traditionally, defined-benefit plans — including pension plans, health insurance, and life insurance — were most likely to be offered by very large employers (500 or more employees) with unionized labor. Both of these characteristics are now in systemic decline.

The good news for financial services providers is that this business shift creates a growing underserved market of people who need insurance and other financial products. The bad news is that this market is dispersed, so the employer is still the best channel for reaching these potential clients.

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 79.*

Smaller Businesses Will Drive the Economy in 2020

It is an axiom in economics that consolidation takes place in contracting industries while specialization drives expanding ones. Therefore, as the economy expands around the new industries noted earlier, potential clients will be smaller firms with more individualized needs.

With the exception of health care, there is relatively low capital investment required for the types of businesses driving the recovery. That will make their entry into and exit from the market much easier.

For this reason, employee-benefits firms will find themselves facing a much more fluid market of small firms with relatively shorter life spans. That said, the people these firms will employ will be more highly educated and more highly compensated than the employees of the firms that dominated the economy before the recession.

Public Sector Retirement Plans

One way or another, the current dispute about public sector pensions and other benefits will be resolved by 2020. While the solution is far from clear, it is generally agreed that because both Republicans and Democrats see this battle as a wedge issue to rally their constituents, the fight will be protracted and messy.

In 2012, state and municipal workers accounted for 15 percent of the U.S. workforce, even after more than 500,000 positions nationwide were cut in response to budgetary shortfalls.

To add such a large population of workers to the underserved market could prove to be a huge opportunity for financial services providers. The market advantage could shift from large firms and product manufacturers selling directly to large bureaucracies to small firms providing customized individualized product offerings to individuals.

Alternatively, public employee unions could replace government agencies as large-volume providers of insurance and other financial products, which would keep the marketing advantage with larger organizations.

Telework and Compensation

According to World at Work, a human resources research organization, 2008 marked a milestone in telework. That year, full-time employees for the first time accounted for the majority of teleworkers.[48] Telework expert Kate Lister notes that "the typical telecommuter is a 49-year-old, college educated,

salaried, non-union employee in a management or professional role, earning $58,000 a year at a company with more than 100 employees."[49]

The benefits of telework to both the employer and the employee are too significant to be dismissed.

For employees facing $4-per-gallon gasoline prices, the opportunity to telework three days per week is equivalent to a $2,000 raise, given average commuting costs and tax brackets.

For employers, consider the following:

- The Building Owners and Managers Association estimates that firms with telework policies have reduced their commercial real estate costs by 20 percent.
- Employers have discovered that contrary to conventional wisdom, teleworkers have proven to be more productive than their nine-to-five on-site counterparts, not less.
- The growing skills shortage is already demanding that employers expand their talent searches beyond their immediate labor markets, making them open to accommodating talented candidates who are unable to relocate.

These factors make teleworker accommodations — including periodic long-distance travel to the physical job site — less expensive than relocating an entire family.

Some of the employers' savings are also finding their way into employee compensation, both in higher salaries and more generous benefits.

The rise of teleworkers, who will account for 15 percent of the workforce by 2020, could present a challenge for insurance agencies and financial services providers who define their markets regionally.

The Rise of the Nonprofit Workforce

Another major trend will be the growth of nonprofit organizations as employers. According to the Bureau of Labor Statistics, the nonprofit sector employed more than 9 million workers in 2007, one in every 15 American jobs.

Given the anticipated growth rates for health care and education, as well as encore workers' preference for socially valued work, one can reasonably expect the nonprofit sector to account for a much larger share of the workforce by 2020.[50]

It is widely expected that the benefits packages of nonprofit organizations need to be very different from those in the private sector. The reasons include:

- Somewhat higher turnover
- Bimodal age distribution — their workers tend to be disproportionately much younger and much older, with fewer middle-aged workers than in the private and public sectors
- Staffs who are motivated beyond simple financial incentives

Whether these factors will remain stable or change as the nonprofit sector accounts for a larger share of the total workforce is not yet clear.

Business Opportunities

OPPORTUNITY ELEVEN
Fee-Based Compensation

A combination of forces will drive the financial services industry to fee-based advisor compensation if it is to maintain market share. (Changes to advisor compensation will naturally have a material impact on managerial compensation as well, but that is outside the scope of this research.) The industry should proactively make the shift to fees for a variety of reasons, including:

- The accelerating rate of product commoditization
- The need to provide more customized and comprehensive services to help individuals and small groups, including retirees, mobile professionals, and the broad middle market
- The need to help Boomers decumulate rather than accumulate wealth
- The need to attract and retain encore talent, younger and female professionals, and part-time workers in a more competitive recruiting environment
- The need to take financial education and planning to the broader professional and middle markets to help more Americans maintain a quality of life for a lifetime

It is important to note that changing from commission-based to fee-based compensation will likely meet resistance from clients. Because commissions are often obscured, clients will likely perceive that they are now being charged for a service they once received for free. Therefore, industry professionals will have to reposition their services to reflect the value of the outcome of their work — ensuring a sustained quality of life — rather than the tools they use to achieve it.

OPPORTUNITY TWELVE
New Sources of Talent

Field leaders and their teams must prepare now to respond to the coming shortage of talented professionals available to transition into financial services.

The pool of mid-career, college-educated workers from which much of the industry draws its talent is shrinking rapidly. Fortunately, there are trends afoot that can help the industry respond.

First, with retirement lifestyle management becoming a growing concern at the same time that encore careers are becoming more common, the profession enjoys some lucky timing for the next few years. The Baby Boomers may provide at least a partial solution to the industry's talent needs (see pages 28-29).

But for some there may be another, more radical solution. Developing collaborative relationships with professionals or firms internationally could provide advantages to companies and larger firms that can leverage economies of scale.

Exporting Work

Addressing the skills gap could mean looking abroad for talent, to countries where college graduates have become more readily available. Other professions that have already had to respond to the skills shortage, especially health care, have found that they can either import workers or export work.

On the other hand, outsourcing back-office activities internationally could raise concerns about standardizing financial services practices across borders and cause some to question the current prohibitions on providing financial services outside of domestic markets. These are very legitimate concerns. Fortunately, they have already been addressed in the health-care sector, which has been laboring under a severe shortage of physicians and nurses for more than a decade. The medical profession has successfully increased its reliance on foreign providers through telemedicine in areas such as pathology, radiology, and health information management that do not require direct interaction with the patient.

Initially there was great resistance to allowing foreign medical providers to essentially export health services to the United States. But as health-care costs increased, technologies improved, and professional shortages became more severe, public resistance to cross-border medicine has abated. Concerns regarding foreign participation in personal financial services could follow a similar path.

Moving financial services offshore beyond simple back-office operations could also be possible. Identifying lessons from the medical profession's experiences in transnational service delivery could be of value to the industry as it faces a similar skills shortage in the years ahead.

For example, one of the initial challenges to cross-border health-care management was consensus on who owned the patient information. In the United States, patients' medical records belong to the medical practice, while in the European Union, medical records belong to the patient and cannot be given to anyone without the patient's permission. This significant difference in intellectual property ownership had to be resolved for cross-border health care to take place. Doing so resulted in the Health Information Portability and Protection Act (HIPPA) and the form that all American patients now sign when they come under any medical provider's care.

Similar concerns about information ownership, privacy, and conflicts of interest could emerge if financial services are managed offshore.

OPPORTUNITY THIRTEEN

Employers as Gatekeepers

The kinds of businesses that make up the market for employee benefits packages will change significantly by 2020.

An increasing share of the U.S. population already works for companies that do not offer retirement savings plans or employer-sponsored life insurance. This population will continue to grow as small, professional businesses become the primary engine that drives the country out of economic malaise.

This underserved market will provide financial services firms the opportunity to sell products and services directly to employees as well as to provide voluntary benefit packages to their employers. This is a market opportunity that should favor smaller, local financial services firms.

With the exception of manufacturing, the businesses driving the recovery will be more professional and service oriented than benefits clients of the past. These businesses will have much shorter life spans, and their employees will be more mobile. Their turnover will be much higher, so financial products will need to be more portable.

Because these businesses will employ the underserved, professional population that financial services firms want to attract, they should prove to be valuable gatekeepers.

The small-business employer is unlikely to take the time to personally educate their workers on the value of savings plans and insurance. So addressing this challenge will be fundamental to succeeding with these gatekeepers. In addition, to engage these firms effectively as partners, advisors will need to be sensitive to the specific needs of workers employed by the firm or its industry.

If specialized knowledge is required for specific market sectors, it could lead to greater concentration of firms around market niches, with a firm's identity more closely tied to its niche than to a geographic region. This would encourage more horizontal integration by firms across markets.

Nonprofit Firms

It is expected that a large share of the firms that will be created by 2020 will be not-for-profit businesses, which have different benefit needs than their for-profit counterparts.

With tighter budgets, employees who are both much younger and much older than the general workforce, and staffs motivated beyond simple financial incentives, nonprofit organizations are likely to need or desire customized solutions that are different than their for-profit counterparts.

OPPORTUNITY FOURTEEN

Industry or Profession Specialists

To provide benefits effectively in the small-business market, advisors will need to be sensitive to the specific needs of workers employed by the firm or its industry.

And as people increasingly define themselves more by what they do than for whom they do it, business associations and professional societies could become a more significant channel for marketing employee benefits such as insurance and other financial services. Indeed, given the more fluid environment for small-business entry and exit, firms might find that selling benefits through these types of industry groups would be a more stable strategy than selling directly through the businesses.

Such arrangements could play to the advantage of larger financial service providers and independents, as they could mix and match a broader range of products to meet the needs of a particular association's membership.

The trend toward telework could also play to the advantage of larger financial services firms that are able to serve broader regional markets, or to firms that define themselves as industry or profession specialists.

Questions to Consider

One-Minute Debrief

1. Which small-business trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. What would be the biggest challenge for your firm in shifting from commissions to fees? What would be the biggest opportunity?

2. How could your firm work more effectively with small businesses to bring financial education and services to their employees? To what extent can your firm address the desire for customized, portable products?

3. To what extent do your advisors specialize their practices by industry or profession? What clusters of small businesses in your marketplace could open doors to further specialization opportunities?

First Step

What *one thing* will you do this year to better position your firm for success in the small-business environment?

Additional copies of this worksheet can be found at gamafoundation.org.

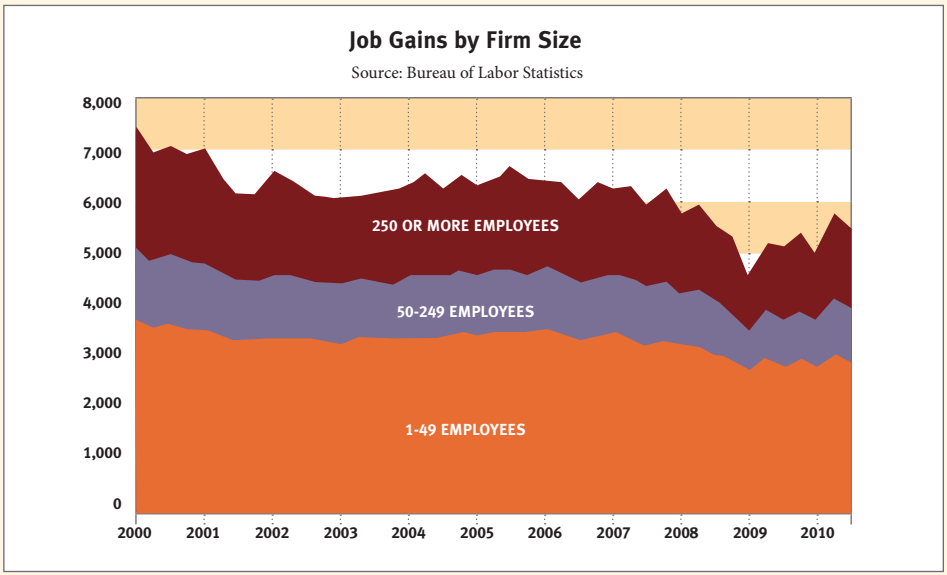
Drill Down on Trends

Smaller Businesses

Job Engine

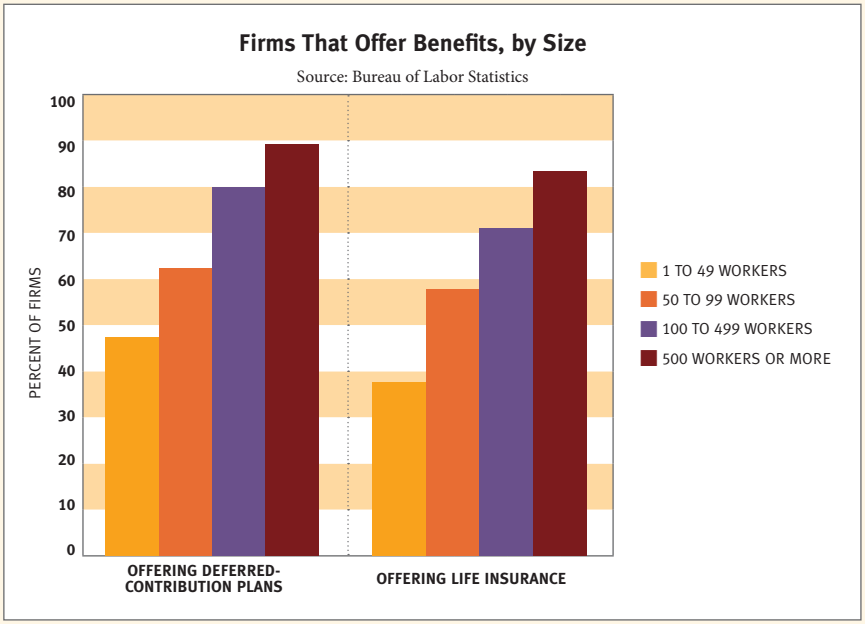
While small businesses played a significant role in job creation before the Great Recession, their importance as employers is expected to be even more significant in the years ahead.

As the credit crisis resolves and small businesses gain better access to credit, slow job growth among smaller businesses is expected to reverse itself. In fact, a look at the past decade of job creation shows that smaller firms have been a more dependable job engine than larger ones.



Why Size Matters

There is an inverse relationship between the size of the firm and the likelihood that employees will be offered retirement benefits and life insurance. According to the Small Business Administration, small businesses — those with fewer than 100 employees — accounted for 70 percent of all new jobs created from 1997 and 2007. According to the most recent Bureau of Labor Statistics' *Employee Benefits Survey,* small businesses are far less likely to offer defined-contribution plans and life insurance coverage.[51]



NOTES

[48] The number of teleworkers slipped in 2009 and 2010 when employees were reluctant to be invisible in times of rising unemployment.

[49] Kate Lister and Tom Harnish, *The State of Telework in the U.S., How Individuals, Business, and Government Benefit* (San Diego: Telework Research Network, June 2011), 7.

[50] Attempts to measure the size of the nonprofit sector labor force are relatively recent. Therefore, it is difficult to quantify a growth projection for 2020.

[51] *Employee Benefits Survey* (Washington, D.C.: Bureau of Labor Statistics, March 2012), http://www.bls.gov/ebs.

Action Items

The insurance and financial services industry is facing profound changes in its markets in the aftermath of the Great Recession and the migration of the Baby Boom generation into their encore career years.

But times of great change are also times of great opportunity for those who are willing to embrace the changes and provide value and service in ways that address the market's new realities.

This first study in *Firm 2020 — The Market of the Future* — has shown you many of the market's new realities, and it has identified a great many business opportunities for agencies and firms in our industry.

The market perspective you have gained from this research will be instrumental to your benefiting most fully from Study Two, *The Firm of the Future.*

Before proceeding to that study, please take a moment to consider your key takeaways from Study One, including the various client *markets*, the products and services that will provide these markets *value*, and your firm's potential *partners* in serving these markets. Then use the following table to capture your best ideas to share with your team.

Snapshot of Ideas

Briefly capture your best ideas and opportunities here. Remember to keep it simple. Once a first step is taken, subsequent steps are much easier.

Market	Best Opportunities	Value to Be Provided	First Steps	Potential Partners
Baby Boomers				
Middle Market				
Small Businesses				

Additional copies of this worksheet can be found at gamafoundation.org.

The Firm of the Future

STUDY 02

Introduction to Study Two

Study One presented a *bottom-up* look at our business future, using the client's economic future as its starting point and following those impacts up the supply chain to understand how they will affect our firms.

Now with Study Two, we take an *outside-in* look at our business future by examining the impact that major forces outside our industry will have on our firms. While not all of the changes forecast will affect your firm, many will, and it is important as you explore Study Two that you keep an open mind on how your firm can best benefit by embracing these changes.

Successful firms in 2020 will be highly networked, technology-empowered, and consumer-aware enterprises. In a world of diverse opportunities, they will be strategic in whom they recruit and train as advisors and whom they target as clients. They will deploy new sales tactics to identify and connect with customers, and many will adopt new business models. The leaders of these firms will harness the powers of imagination, innovation, and interaction among themselves and their advisors. You can be one of these leaders.

As you explore Study Two, *The Firm of the Future*, you may not be surprised by any one of the major drivers of change described in this study, especially if you frequently scan news and business reports. What could be unsettling is the sheer impact of these changes, taken together, and the volume of strategic choices you face.

Study Two includes the following:

- *An industry outlook,* providing a brief overview of major trends in the financial services environment and establishing the context for understanding specific changes that will affect your firm
- *Four future business models* that examine possible winning strategies for firms in 2020
- *Six change drivers* (which represent the heart of the study) to help you understand the cultural shifts behind the four business models, the significance of these changes, and their implications for field leaders
- *A set of opportunities to get started* as well as *debrief and strategy questions* to help your firm prepare for change

- *Additional drill-down information* for those field leaders who would like to delve more deeply into the change drivers
- And just to keep things interesting, *four potential game changers* at the end of the study to remind us all that surprises are certain to come

At the conclusion of Study Two, you will have a better understanding of how, in just a few years' time, the most successful firms in our industry will offer much greater value and convenience to their clients.

But the future arrives one step at a time. At the end of Study Two, you will have the opportunity to identify some steps for your own firm to begin down its unique path to 2020.

To that end, please turn to the following checklist of thought-provoking forecasts from Study Two. Is your firm prepared to address these changes today?

CHECKLIST FOR

The Firm of the Future

Below are 18 thought-provoking forecasts from *Firm 2020*'s Study Two, *The Firm of the Future*. Use this simple checklist to determine how well your firm is prepared today to address the business culture and climate of 2020.

18 Culture and Climate Forecasts	Is Your Firm Prepared?	
	NO	YES, Here's How
1. In 2020, first-line and frontline leaders will focus more on diversity outside the traditional census boxes when building effective teams.		
2. By 2020, the Baby Boom generation will redefine retirement, with many staying closely involved in their communities and former firms or launching encore careers.		
3. Firms in 2020 that want to attract the best talent from the Millennial generation will need to provide engaging, flexible work environments that align with this generation's values.		
4. The firm in 2020 will need to focus on a much more diverse array of family structures and their unique risks.		
5. In 2020, both advisors and clients will gravitate toward firms that they can trust and that share their values.		
6. The firm in 2020 will compete with others for the best advisors on the strength of collaboration and communication technologies.		
7. Advisors in 2020 will have direct access to client information, sales leads, social media profiles, and advanced modeling and simulation software anywhere and everywhere they need it.		
8. Producers in 2020 will begin offering self-learning products that proactively price risk based on a client's health and other characteristics.		
9. In 2020, firms will use virtual worlds and telepresence solutions to connect and build trust between advisors and their clients.		

18 Culture and Climate Forecasts	Is Your Firm Prepared?	
	NO	YES, Here's How
10. By 2020, firms will use a wide range of social technologies to participate in an increasingly networked culture.		
11. Privacy as a concept will undergo fluid changes over the next seven years, and firms will rely on younger workers to develop adaptable privacy policies.		
12. The threat of cybercrime will continue to rise in 2020 as the technology tools needed to sabotage, subvert, and disrupt businesses continue to evolve.		
13. Firms in 2020 will have a competitive edge when they can provide targeted intelligence systems that can turn large swathes of data into actionable insights for their advisors.		
14. Advisors in 2020 will need to add extra value through advising as more clients use data analytics software to analyze and purchase complex insurance products.		
15. Competition and consolidation over the next seven years will result in a barbell-shaped industry, with larger firms dominating the high end of the market.		
16. By 2020, the mid-market will emerge as a growth market for firms willing and able to capitalize on emerging trends.		
17. Over the next several years, the assets for high-net-worth individuals will recover and grow, but this market could face headwinds because of tax policy changes.		
18. Smaller firms in 2020 will have a competitive advantage by creating a virtuous circle of shared value between themselves and the communities they serve.		

Industry Outlook

Grim With Glimmers of Hard-Earned Hope

The 10,000-foot view of the next several years for the insurance and financial services industry, and the economy in general, is relatively grim. For the life insurance industry, the problem goes deeper than just the latest economic downturn.[1]

- Since 1980, the number of life insurance policies and inflation-adjusted premiums paid by customers has declined despite population growth.
- Agency revenues in 2010 saw flat to modest increases from a year earlier because of continued financial and regulatory uncertainty.[2,3]
- Economic uncertainty, choppy markets, and increasing regulation continue to challenge the financial advice industry.
- For consumers, unemployment remains high and income growth is anemic. Health insurance premiums, a more immediate concern, continue to rise.

The U.S. insurance and financial services industry is a challenged and mature industry where opportunities for growth are scarce and can come with risks. Even so, smart, entrepreneurial, and future-focused firms can spot opportunities that will elude their competitors. In any maturing industry, the segments in which a firm operates are much more important than the overall growth of the industry. The key is to focus time and resources on business segments where the firm has — or is willing to develop — the capabilities, assets, and market insights needed for growth.[4,5]

As noted in Study One, rebuilding consumer trust and understanding shifting consumer attitudes will be fundamental to the search for growth. Consumers are seeking greater financial security and risk management, but are skeptical of financial institutions and advisors. A 2009 study showed that less than 15 percent of the public reported trusting financial advisors and insurance agents.[6]

In addition to the loss of trust, a long-running recession and poor employment environment have changed consumer habits, especially among the Millennial generation (those born between 1982 and 2001). Consumers are refocusing their spending to prioritize sustainability, community, connection, quality, and creativity. They are looking for more than just the best price or the most features. They are spending their hard-earned, and often rare, discretionary income on high-quality goods and services that provide good value, reflect their own values, and support their communities.[7]

One reason consumers are seeking greater financial security is the increased amount of risk that employers are shifting to their employees. Defined-benefit retirement plans have declined dramatically in the private sector and are under significant pressure in the public sector.[8] (See also pages 50, 51, and 53.) By the same token, companies are cutting back or trimming many insurance benefits, including health[9] and disability[10] insurance, and may look to cut group life benefits in the near future. The shift of risk to

consumers is likely to drive them to well-positioned firms for insurance and retirement solutions that provide the stability and security that employers are no longer providing with their benefits packages.

These changes in consumer and business attitudes are likely to remain through 2020 as income and asset growth remains depressed. The global Baby Boomer generation is moving out of its productive years, drawing down personal savings, and placing greater burdens on social welfare programs.[11] At the same time, the global financial system is in a massive process of deleveraging as many countries have reached the end of sustainable growth in public and private sector debt.[12] This will put downward pressure on government programs and benefits, especially health care and pensions for government employees. Budget deficits will also imperil the preferential tax treatment for retirement investments and annuities.

The insurance and financial services industry is likely to face a number of new regulatory hurdles, from consumer protections to new taxes. The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act provides the framework for the most widespread changes for the financial industry since the Great Depression. The new law attempts to streamline oversight of financial institutions, reduce speculative trading by banks, increase transparency, reform credit rating agencies, and reduce risk in the financial system. The most influential changes will likely fall into the area of consumer protection with the establishment of the Consumer Financial Protection Bureau (CFPB) and Federal Insurance Office (FIO). Both of these new agencies will increase the oversight and reporting requirements of advisors and may intervene more directly in the market.[13]

There is also the risk of further regulatory changes in the United States. Many reformers believe the Dodd-Frank act didn't go far enough in protecting consumers or reducing systemic risk in the financial system. They want stronger federal oversight, limits on risky financial products, and the breakup of large financial institutions. While new laws and agencies have now been put into place to advance consumer protection, Congress and the administration face many other pressing priorities. Further instability in the financial system or large losses at financial institutions could spark further reform at the federal or state level.[14] Regulators will likely look abroad for new regulations to protect consumers, adding external impetus to a shift to fee-based compensation. This could be in conjunction with a shift toward a global standard that favors advisory fees over commissions. Another change could be further separation between producers and distributors of financial and insurance products in order to reduce potential conflicts of interest.

NOTES

[1] Tim Hill, Marc Slutzky, and Neil Cantle, *Emerging Risks in the Marketing & Distribution of Life Insurance & Annuities* (LIMRA and Milliman, Inc., Aug. 13, 2010).

[2] A survey conducted by *Best's Review* of 2,400 agents and brokers showed that four out of 10 respondents reported flat revenue or revenue growth under 10 percent. Roughly 37 percent of respondents had seen cuts in their commission rates.

Al Slavin, "Is Flat the New Normal?," *Best's Review* (April 2011), 48-52.

[3] The Patient Protection and Affordable Care Act will continue to create uncertainty for agencies that deal in health insurance. With some states electing to create their own insurance exchanges and others opting to participate in the federal exchange, and with the full consequences of many other changes yet to be fully understood, implementation may prove slower and more problematic.

Lyle Denniston, "Don't Call It a Mandate — Call it a Tax," SCOTUSblog (June 28, 2012), http://www.scotusblog.com/2012/06/dont-call-it-a-mandate-its-a-tax.

[4] Mehrdad Baghai, Sven Smit, and S. Patrick Viguerie, "The Granularity of Growth," *The McKinsey Quarterly* (2007), https://www.mckinsey-quarterly.com/The_granularity_of_growth_1993.

[5] By the same token, it is vital for firms to avoid diversifying into areas where they have little knowledge about future risks. The recent history of the financial and insurance industry is rife with companies diversifying into market segments where they had poor knowledge, such as AIG CEO Hank Greenburg's decision to secure credit default swaps in an attempt to boost growth outside of AIG's core insurance businesses.

Shah Gilani, "The Inside Story on the Collapse of AIG," *Money Morning*" (Sept. 23, 2008), http://moneymorning.com/2008/09/23/credit-default-swaps-3.

[6] Low consumer confidence is a huge barrier to sales for insurance advisors to overcome. Seven in 10 potential customers decide in the first meeting with an advisor whether they trust that person.

Hill, Slutzky, and Cantle, *Emerging Risks in the Marketing & Distribution of Life Insurance & Annuities*.

[7] John Gerzema and Michael D'Antonio, "The Power of the Post-Recession Consumer," *strategy+business* (Spring 2011), http://www.strategy-business.com/article/00054?gko=340d6.

[8] The recent market decline had a large negative impact on state pension funding levels, with a number of states in a very precarious position, including Illinois, Connecticut, Oklahoma, Louisiana, and Kentucky.

Karen Pierog and Tiziana Barghini, "Decline in U.S. State Pension Funding Slows: S&P," *Reuters* (June 21, 2012), http://www.reuters.com/article/2012/06/21/us-state-pensions-sp-idUSBRE85K1J420120621.

[9] Health-care spending has more than doubled in the last decade, and even employees covered at work are paying more out of pocket in premiums, co-pays, and deductibles.

Staff, *Healthcare Cost & Utilization Report: 2010 (Washington, D.C.:* Healthcare Cost Institute, May 2012), http://www.healthcostinstitute.org/2010report.

[10] Roughly 47 percent of employers offer long-term-disability coverage to their employees, and many are cutting back on premium payments and benefits.

Michelle Andrews, "Employers Increasingly Trimming or Cutting Disability Benefits," *Kaiser Health News* (Sept. 20, 2011), http://www.kaiserhealthnews.org.

[11] The aging population is a driving factor behind many recent problems, from rising health-care costs to the binge buying of collateralized debt obligations. A simple solution is to increase immigration of younger, preferably well-educated, workers. In the United States, immigration has become much more difficult, especially for highly educated workers, because of visa restrictions in place after the 9/11 terrorist attacks.

[12] John Mauldin, *Endgame: The End of the Debt Supercycle and How It Changes Everything* (Hoboken, N.J.: John Wiley & Sons, Inc., 2011).

[13] The Federal Insurance Office has almost no regulatory power and is set up to work primarily as an information-gathering shop designed to spot systemic risks or consumer abuse caused by gaps in state regulations. The Bureau of Consumer Financial Protections has greater regulatory power because of its broad authority to create and enforce consumer protection laws.

Greg MacSweeney, Phil Albinus, Katherine Burger, et al, "Dodd-Frank Cheat Sheet. *Bank Systems & Technology* (2012), http://www.bank-tech.com/dodd-frank.

Staff, "The Dodd-Frank Act: A Cheat Sheet," *Morrison & Foster* (2010), http://www.mofo.com/files/Uploads/Images/SummaryDoddFrankAct.pdf.

[14] The fate of the European Union could have profound impacts on future regulations. A breakup could stress global banking giants and reignite calls for a breakup of major financial institutions and the reintroduction of a Glass-Steagall–type separation between commercial and investment banking.

Future Business Models

Images and Ideas for the Future

The following scenarios illustrate four distinct business models that respond to the six major change drivers in our research. They were designed with one or more different types of firms and industry sectors in mind. Each describes a firm that chose a different strategy for success.

These are not predictions of the future; their purpose is to provoke your imagination, raise fundamental questions, and stretch your vision of what is possible and achievable. Each should offer something that will resonate with your situation and sense of the future.

As you choose your own strategies for success, you can use these models as a tool to apply creativity and imagination to your future. These four business model scenarios — and others you might imagine — will help you develop robust strategies for yourself, your teams, and your firm. Read all of them closely, even the ones that seem most unlike you. Understanding why you would not choose a particular path can help you choose the right path and equip you for a successful journey into the future.

The information on the six change drivers, immediately following this chapter, will help you more fully appreciate the forces in play behind these models.

MODEL ONE

Connected Entrepreneurs — Technology and Innovation Turnaround

It's the end of 2020 and Prawda Advisors can close the books on a successful year. Renewed global growth and a booming housing market in the United States lifted yields and market returns across the board. Its clients finally are putting memories of the volatile markets following the Great Recession behind them. Many firms did not survive this brutally volatile business cycle. Increasing costs and regulatory requirements forced many of Prawda's small and midsize competitors out of the market or into consolidation.

Firms and Sectors

- Large Managerial Firms
- Large General Agency Firms
- Traditional Life
- Financial Planning

To survive, Prawda Advisors had to make a serious investment in its long-term vision. Starting in 2017, the firm invested in a state-of-the-art customer relationship management system that connects every advisor across the company's 19 offices to the most sophisticated market intelligence and data analytics system in the industry. The company's new technology system makes each advisor a fully networked entrepreneur, able to drill down to the markets that matter to them, develop new leads from social media, and deliver highly customized products. Prawda Advisors anticipated and timed this move to take advantage of a federal regulatory overhaul that standardized consumer disclosure requirements.

Prawda Advisors is striving to be the most sophisticated firm in the business and can now attract the best leaders and advisors in the country. The company's first-line and frontline leaders use new social networking analytics to find promising new advisors and help them leverage their networks to increase sales, improve client management, and identify new markets for growth. The firm's best advisors are diving into this powerhouse of client data to structure highly customized products and services that the company's more affluent customers are demanding. These innovators are well rewarded for identifying new products and services, and their discoveries are spread firm-wide so all the firm's advisors can realize new opportunities.

THE OPPORTUNITIES AND DECISIONS UNDERLYING

Connected Entrepreneurs – Technology and Innovation Turnaround

Change Driver	Opportunity	Decision
Workforce Development and Talent Retention *(page 105)*	Attracting, retaining, and retraining a technology-savvy workforce	Recruit differently and create a team-oriented environment where technology-savvy advisors share best practices.
Consumer and Advisor Needs *(page 119)*	Leading the way with new products and services aimed at replacing traditional and vanishing forms of consumer financial security	Analyze customer needs and potential new consumer markets, and shift toward these opportunities.
Technologies for Sales and Service *(page 131)*	Increasing productivity and effectiveness to better integrate the business	Act as a fast follower, investing regularly in new technologies and training.
Privacy and Security *(page 145)*	Moving boldly into a networked culture with transparent privacy policies	Establish your comfort zone for firm and individual freedom and appropriate behavior in networks.
Market Intelligence and Data Analytics *(page 159)*	Maximizing the availability and capacity to use big data	Build your own systems modeling approach for mining data for big profits.
Shifting Business Models *(page 169)*	Adopting or creating a new business model with greater independence and resilience	Invest financial resources and the future of the firm in a higher-risk, potentially higher-reward situation.

MODEL TWO

Middle-Market Mavens — Empathy for the Masses

Managerial firm Daley, Brown & Root caught lightning in a bottle with its unique marketing of easy-to-understand insurance products in the middle market. As a proven innovator in the middle market with solid growth in the 1990s, the firm was acquired by a large insurance company. By the end of the Great Recession, this marriage of mutual advantage hit a rough patch. Many insurance companies decided to divest themselves of their distribution operations in the face of greater consumer regulations and a generally challenging business environment.

Firms and Sectors

- Large and Midsized Managerial Firms
- Large and Midsized General Agency Firms
- Traditional Life
- Multiline Insurance

Now that the middle classes are growing worldwide, Daley, Brown & Root is in a great position to help revitalize the middle market at home and abroad. The firm is investing in talent and training its growing cadre of advisors, many of whom are Millennials, with strong social networks and a desire to help clients through new digital distribution channels. The firm is working closely with its parent company to generate new low-cost products that appeal to this diverse and growing market. The firm now leads the industry in advisor retention and satisfaction thanks to its workforce development and retention model.

Business reporters now say the lightning has stayed in the bottle because Daley, Brown & Root mixes empathy across the company and for clients with its proven middle-market expertise. Its new, young advisors spend their first few years working on salary, providing excellent virtual customer service on the company's low-cost products. During this period, the company's mentoring program connects younger and older workers in ways that are mutually beneficial. By the time the new advisors are ready to go out and sell more complex and personalized insurance products, they have a strong sense of what people need, a sophisticated knowledge base, better sales techniques, and a more robust network. They retain their connections to this talent pool in training as they become the mentors and this cycle continues to renew the firm.

THE OPPORTUNITIES AND DECISIONS UNDERLYING

Middle-Market Mavens – Empathy for the Masses

Change Driver	Opportunity	Decision
Workforce Development and Talent Retention *(page 105)*	Embracing workers across generations	Develop mentorship programs where younger and older advisors gain valuable skills from each other.
Consumer and Advisor Needs *(page 119)*	Growing consumer demand for products that address the risks of diverse family structures	Keep connected with your customers, listen to their needs, and adjust your product portfolio regularly.
Technologies for Sales and Service *(page 131)*	Leveraging new virtual distribution channels	Learn best practices from your younger workers and leverage them across the firm.
Privacy and Security *(page 145)*	Creating a culture that respects privacy and security	Work with younger and older advisors to develop privacy and security policies.
Market Intelligence and Data Analytics *(page 159)*	Using social networks	Continually look for best practices and new technology for mapping social networks.
Shifting Business Models *(page 169)*	Expanding the market for simpler, lower-cost products	Look for new ways to structure your advisor workforce to lower costs and add value.

MODEL THREE

The Consumer-Centric Advisor — Capitalizing on Niche Relationships

Alvarez Advisors is wrapping up a good year in 2020, even as many of its more affluent clients struggle with rising tax rates. The federal government and states have been raising income taxes to cover increased health and pension costs from an aging population. Just last year Congress removed the tax breaks for municipal bonds and mortgages. Susan Alvarez and her brother Danny have capitalized on the changes by selling more life insurance products, which have thankfully kept their preferential tax treatment.

Firms and Sectors

- Independent Agents
- Small Firms
- Financial Planning
- Traditional Life
- Multiline Insurance

Alvarez Advisors is a leader in two of the fastest-growing markets over the last decade. Danny Alvarez is a national leader in financial planning for same-sex couples. He brought his sister Susan in to lead the family firm seven years ago to infuse new thinking after her successful tech career ended. She has built one of the highest trust and social influence scores on the social networks that matter for women executives in the tech industry. Her clients span the country, although she herself rarely leaves the grandkids in the Pittsburgh area. Thankfully, virtual worlds are robust enough that she can do almost all of her advising online.

Even with all the time-saving technology, she has so much business lately that she is now farming out a lot of it to her network of colleagues. Access to that technology has been her biggest headache for the last year. Alvarez Advisors has been partnering with a larger firm formed by one of their former mentees to access their back-end support system. So far the agreement has worked well for both parties, although Danny remains fearful that they're trying to get access to Alvarez Advisors' valuable social media networks. Susan is more sanguine. They've paid top dollar for a personalized data security system, and she doubts the clients they've cultivated over the last decade would suddenly jump ship to a new advisor. She sees everyone from her former mentees to her clients as part of a large extended family that is as important to her as Danny.

She tunes in to her social network feed before shutting down her personal mobile device for a couple of hours disconnected from the ever-present network. Fortunately there are no emerging trends or alerts from her client network. No clients or friends are showing public profiles in the immediate vicinity, just the usual collection of location-enabled personal posts, pictures, and i-videos. Susan is just about to disconnect when her digital assistant pops up in the corner of her fifth-generation Google Glasses with a video of the grandkids and their new puppy. Life is rich for Susan and Danny and their growing family of relationships.

THE OPPORTUNITIES AND DECISIONS UNDERLYING

The Consumer-Centric Advisor – Capitalizing on Niche Relationships

Change Driver	Opportunity	Decision
Workforce Development and Talent Retention *(page 105)*	Drawing on personal networks for skill development and assistance	Expand your business networks and look for win-wins with colleagues, mentors, and mentees.
Consumer and Advisor Needs *(page 119)*	Creating trust and value	Strengthen relationships with current and former clients.
Technologies for Sales and Service *(page 131)*	Using virtual worlds and telepresence	Experiment with new communication technologies as they emerge.
Privacy and Security *(page 145)*	Protecting valuable firm and client data	Invest in good security systems and robust policies.
Market Intelligence and Data Analytics *(page 159)*	Drilling down to the markets that matter	Use data analytics to identify overlooked niche markets.
Shifting Business Models *(page 169)*	Serving new segments of high-net-worth clients	Watch for regulatory or tax changes that could dramatically alter the value of financial or insurance products.

MODEL FOUR

A Shared-Values Business — Growing With Communities

Thomas Bowers sits in the executive office of Bowers & Sons quietly reflecting on the irony of history while four generations of Bowerses stare back at him from their oil and canvas perches. His great-grandfather founded the firm 120 years ago to provide insurance to African-Americans coming up from the South, and for decades it was one of the premier insurance firms serving the African-American community. They knew the community like no one else and were able to keep larger companies at bay by sharing the values of the community they served.

Firms and Sectors

- Small Firms
- Fraternal Firms
- Multiline Insurance
- Traditional Life

In the last decade, Thomas worked hard in the community building trust and connections. His firm regularly partnered with local institutions even as many younger people left older clubs, fraternal organizations, and the church. Still, the trust built from 120 years of service to the community helped see Bowers & Sons through some tough times as one insurance product after another became cheaper to buy online. However, the community has changed in ways Thomas's forbearers couldn't have imagined. For them the community was always defined by geography and culture. Data was gained by hitting the pavement, talking to your neighbors, and understanding their risks, needs, and desires. Now data is in the cloud and available to those on someone's "friend" list.

It wasn't until yesterday that the impact of the shift dawned on Thomas. A colleague at a fraternal firm shared with him the news of the first new fraternal insurance organization to be recognized by the state in years. It was for an online gaming guild with more than 3,000 members across the state. At first he laughed at the idea. Who would buy insurance from a gaming guild? Then he talked to his son. He had heard the news as well and had decided to do some analytics on the firm's client networks. More than 30 percent of its current clients' sons, daughters, nieces, and nephews were all members of the guild or another one like it.

It turns out there were all sorts of connections and communities that Bowers & Sons were missing. While Thomas may never truly understood the appeal of many of these virtual communities, he knows that Bowers & Sons' tradition of building shared value will be the guide his son needs to preserve the family's legacy wherever those communities might migrate.

THE OPPORTUNITIES AND DECISIONS UNDERLYING

A Shared-Values Business – Growing With Communities

Change Driver	Opportunity	Decision
Workforce Development and Talent Retention *(page 105)*	Developing cultural competency and emotional intelligence	Embrace an expanded form of diversity in your hiring and training programs.
Consumer and Advisor Needs *(page 119)*	Creating shared value	Closely monitor what matters to your community.
Technologies for Sales and Service *(page 131)*	Mapping social networks	Look for future generations of CRM systems that allow advisors to map their networks.
Privacy and Security *(page 145)*	Overcoming client concerns about privacy and security	Institute strong policies and educate advisors on how to talk to clients about privacy and security concerns.
Market Intelligence and Data Analytics *(page 159)*	Drilling down to the markets that matter	Use data analytics to identify overlooked niche markets.
Shifting Business Models *(page 169)*	Building trust through affinity marketing	Expand your firm affinity marketing programs and look for nonconventional partners.

Change Drivers for 2020

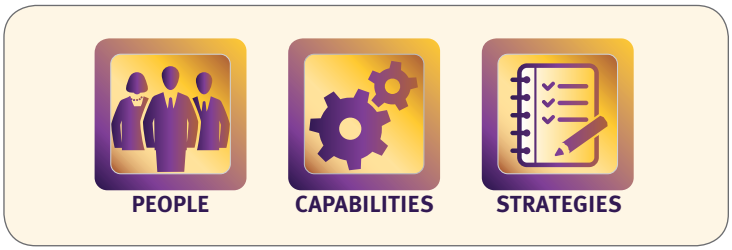
Now that you've explored four future business models and seen some of the industry's potential, it's time to drill into the six major change drivers that underlie these models. These change drivers will help you anticipate the *people* you will employ in your firm and serve as clients, the *capabilities* you will need to invest in, and possible business *strategies* for success.

You may not be able to do much to change the big picture of what the insurance and financial services industry will become; those forces of change need to be understood and monitored, but they are largely beyond the control of any single industry.

But you can do a great deal to anticipate and direct the impact of the six change drivers on your firm. That is why they are so critical to your business. They point to opportunities you cannot afford to overlook.

- Workforce Development and Talent Retention in a Dynamic Workplace
- The Shifting Needs of Consumers and Advisors
- Technologies for a Powerful Sales and Service Force
- Managing Privacy and Security in the Networked Age
- Advanced Data Analytics Empower Advisors and Consumers
- Shifting Business Models Shake Up the Industry

These change drivers are the heart of this study because they require action on your part. They open you up to the dimensions of the future that you can influence. The opportunities chart and the debrief and strategy questions included with each change driver will help you discover concrete steps that you can take right away to begin creating a competitive advantage for your firm.



CHANGE DRIVER 1

Workforce Development and Talent Retention in a Dynamic Workplace

Because of dramatic demographic changes, the firm in 2020 will be a very different workplace.

The Baby Boomers will be exiting the workplace and passing the torch to the Millennial generation.

Field leaders will be charged with developing new ways to retain these valuable workers and transfer institutional knowledge from one generation to the next.

The Millennials, with their high-tech upbringing, will bring to the workplace new ways to innovate and collaborate in an era where creativity is in high demand.

Top Trends to Watch and Manage

- New management methods for diverse teams
- Growth in flexible work methods and new forms of retirement
- Integration of digital workers into the workplace
- Growing demand for creative and connected workers

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 115.*

Beyond the Diversity Boxes

Now more than ever, first-line and frontline leaders need the social and emotional intelligence to communicate across the diversity of their advisors and ensure that they are reaching their full potential.

Embracing the wide array of diversity enriches an organization's ability to respond to its customers, identify problems, and create innovative solutions. But in the process, the firm needs to embrace a new paradigm of diversity.

In the old paradigm, leaders focused narrowly on the boxes people fall into, ignoring the broad range of diverse experience, thought, and opinion that drives successful teams. The old paradigm put the onus on potential employees to fit into the current workplace culture rather than embracing the true value of each employee.[15]

In 2020, firm leaders will focus on diversity outside the traditional census boxes when building effective teams. Firms can't afford to be narrow-minded in a rapidly changing and increasingly global marketplace that focuses on personalized service.

Increasingly, the business management literature is highlighting the broad spectrum of diversity found in the workplace and how to turn that diversity into a lasting competitive advantage.

The many forms of diversity that field leaders will need to manage and maximize include different personality types, experience with technology, generational cohorts, work experience, education background, religiosity, political affiliation, and sexual orientation.[16]

Managing the Graying of America

Fifty years ago, the Baby Boomers ushered in a new era of change focused on youth culture. The next 50 will be focused on a new definition of aging as this same generation moves into retirement.

In 2009, 21 percent of affiliated advisors and 28 percent of independent advisors were age 55 to 65.[17] And the number of workers over the age of 55 will grow nearly 45 percent (five times faster than the overall workforce) by 2016.[18] In the process the Boomers will once again fundamentally reshape how we view the workplace.

Every industry in every country of the developed world will struggle with how to transfer knowledge, experience, and wealth from the largest generation ever to enter retirement. The financial services and insurance industry will be no different.

As noted in Study One, many Boomers will want to remain engaged in the workforce long after they have passed retirement age. Firm leaders will need to develop programs that target the specific needs of older workers such as phased retirement programs, tailored benefit packages, mentoring and job sharing, wellness programs, and technology training. Restructuring the workplace to meet these needs creates a better workplace for workers of all age groups.

Digital Learners Become Digital Workers

The Millennial generation, also called Generation Y, Generation Next, and the Echo Boomers, just to name a few of their many monikers, will be coming into their own in 2020. Regardless of the name, the impact of this generation on the workforce will be the most profound since their parents entered the workforce in the 1960s.

By 2020, they will comprise 46 percent of the U.S. workforce, and will bring their own unique culture and viewpoints into the office with them.

These workers are much more likely to change jobs, and employers should strive for flexibility in order to keep them.[19]

As a group, the Millennials value much more than just a salary. They demand engaging, flexible work environments, loose social media policies that allow them to network with their colleagues, and jobs that have a high level of mobility.

In return, the Millennials bring a high level of technology sophistication, a dedication to lifelong learning, and sophisticated networking skills. They are natural networkers and self-promoters, which are key skills for new advisors.[20]

Recruiting Millennials

- Millennials expect employment instability, so make them a competitive offer up front.
- Highlight long-term benefits, as Millennials expect Medicare and Social Security to collapse before retirement.
- Millennials want to be engaged at work, so highlight job diversity, outlets for creativity, and lifelong learning.

Millennials are also the first generation of digital learners who naturally incorporate new ways of using technology into learning, working, and socializing. For digital learners, the web is an integral part of their lives, and they are much more comfortable working, networking, and sharing their lives through their web-enabled devices.[21]

Competing for Talent in the Creative Job Market

The most competitive environment for recruiting will be to fill jobs that require creativity and connectivity.

The twin forces of automation and globalization are rapidly removing repetitive jobs and jobs that can be done remotely. This includes even highly skilled white collar jobs in the financial services industry. To optimize their businesses, firm will automate lower-value processes and focus more on increasing customer value through high levels of creativity and personal interaction.[22]

Workers in high demand in the new economy will combine *imagination, innovation,* and *interaction.*

- Creative workers who are able to *imagine* new ideas, products, and solutions to problems will be in high demand in industries well beyond entertainment.
- Workers with the technical skills to *innovate* better processes, products, and technologies will have an advantage that cannot be easily replicated by technology.
- And in a highly networked world, there will be a lasting advantage for those workers who are naturals at *interacting* with others.[23]

The workers who combine these three skill sets are also the ones that the firm of 2020 will want to recruit. The likely outcome will be a much more challenging environment for firms as they compete for talent with some of the most dynamic organizations in the country.

Finally, as more jobs focus heavily on creativity and networking ability, we will see greater income inequality. Jobs that require these skills, such as commissioned sales, very often have a "power law" income distribution, where a few do phenomenally well in comparison to the majority of workers in the industry.

More organizations competing for a smaller pool of workers with these key skills will increase the problem of income inequality, which could lead to further unrest in society at large as well as inside the firm.[24]

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Developing Social and Emotional Intelligence	Acknowledge the diversity of your team and work on making diversity an advantage.	Support an open workplace that encourages diversity of thought and opinion.	Take a more thoughtful approach to your emotions and how they influence your work.
Managing Generational Transitions	Create more flexible work environments that appeal to both older and younger workers.	Develop mentorship opportunities where both young and old generations learn from each other.	Take the opportunity to learn from the different generations in your office.
Recruiting and Developing Creative Talent	Set personnel policies that attract, develop, and reward imagination, innovation, and interaction.	Look for ways to harness the talents of your most creative advisors.	Look for opportunities to develop and demonstrate your imagination, innovation, and interaction.
Leveraging Digital Learning	Provide digital learning portals inside the workplace grouped around key skills.	Stress the importance of lifelong learning to new advisors and help them find the best learning resources.	Search out new digital learning portals and continually update your skills.

Questions to Consider

One-Minute Debrief

1. Which workforce trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. What is the sometimes-overlooked diversity of your leadership team? Of your advisor teams? How can you better use the diversity you already have to strengthen your firm?

2. What strategies and policies do you have in place today to help you attract and retain the best advisors across all generations? What one change would make your workplace more attractive to multiple generations?

3. To what extent does your firm attract and retain people today who are skilled at *imagination*, *innovation*, and *interaction?* For which of your positions in the future will these skill sets be required?

First Step

What is the *one thing* you will do this year to better position your firm to be competitive as an employer of the changing workforce?

Additional copies of the worksheet can be found at gamafoundation.org.

Drill Down on Trends

Global Migration and Differing Birth Rates Reshaping America

In a little more than a generation, ethnic and racial minorities will outnumber non-Hispanic whites according to the Census Bureau.[25]

The pace of immigration has slowed down recently because of the bleak U.S. job market. Despite this slowdown, immigrant communities remain some of the fastest growing in the United States, and children of recent immigrants are the fastest-growing segment of the U.S. population.[26] These communities will become even more important as these children enter the workforce and build up their wealth.

The Diversity Advantage

America's firms, from large to small, depend on the growing immigrant communities here in the states and on an increasingly global market for talent.

Embracing diversity will be a key selling point for firms looking to attract the best talent and to access growing markets.

Diversity also improves team performance and makes it easier for teams to tackle tough challenges. For example, research has shown that diverse teams are more likely to elicit unique perspectives and critically review task-relevant information. This is true even when the people who are "different" don't express any unique perspectives themselves.[27]

Gender Diversity

Working women will be one of the most important and fastest-growing markets for financial services and life insurance.

Women bring in one third of the family's income, and the percentage of households where women are the primary or sole breadwinner is increasing.

Women are also more receptive to life insurance as a means to financially protect their families.[28]

According to the Bureau of Labor Statistics, women account for 31 percent of personal financial advisors and 47 percent of insurance sales agents.[29]

The Graying Workforce

The workforce, and the insurance and financial services firm, will be undergoing the most dramatic generational and technological changes since the 1960s.

The Baby Boomers, the cause of so much change 50 years ago, will be exiting the workforce in large numbers. The Census Bureau projects that the elderly population, those aged 65 and older, will grow by more than 36 percent between 2000 and 2020.[30]

The Boomers will not only be the largest generation to enter retirement; they will also be the most educated, wealthiest, healthiest, and most diverse generation to enter retirement.[31]

As noted in Study One, this diverse generation is widely expected to remain active in the workforce and their communities after retirement because of improvements in health care.

The Age Advantage

Older workers have lower absenteeism, well-developed professional networks, and greater motivation than younger workers. They also work well in teams, make excellent mentors, and offer a vast wealth of institutional knowledge.[32]

When given the opportunity, older workers are quite open to the flexible work arrangements and part-time assignments that are becoming more common in our highly networked economy.

Older workers may need more flexible work arrangements, and they often feel that their deep well of skills and knowledge isn't fully utilized. Not addressing these needs can lead to dissatisfaction and the potential loss of a valuable worker to retirement.[33]

It Isn't Easy Getting Old

Despite the growing number of older workers, and their many advantages, most have experienced discrimination in the workplace or in the hiring process. Nearly 60 percent of workers aged 45 to 74 experienced age discrimination, according to a 2007 AARP survey.[34]

Older workers who lose their jobs have been hit hard by the current jobless recovery. The Government Accountability Office reports that 55 percent of unemployed workers have been actively seeking a job for more than half a year.[35]

The growing number of long-term unemployed among older workers will likely have long-term impacts on their overall health and their ability to retire.

The High Cost of Being Young

High levels of student debt and youth unemployment have left many Millennials in a precarious situation. Roughly 40 percent of Millennials have more debt than savings, and they are much more likely to experience unemployment, pay cuts, or a reduction in hours.[36]

At least part of the rising debt levels can be attributed to the high cost of college. Cash-strapped state governments have cut funding for higher education, leading to increased tuition, and leaving more than 94 percent of college graduates with debt.[37]

High levels of debt, in turn, are holding back savings and putting Millennial families at greater risk of bankruptcy. Roughly 75 percent of Millennial households would only be able to cover everyday expenses for a few months if a primary wage earner passed away.[38]

Selling in a Post-Scarcity Economy

In the very long run, decades in the future, it is possible that new technologies will remove low-skilled work completely.

Some futurists and technologists, particularly those who study advances in nanotechnology, computing, and robotics, believe that the continuous automation of work could lead to the development of a "post-scarcity" economy where most goods and services are free or close to free.

Some of these economies already exist in virtual worlds and open-source communities. Here the economy runs on things other than money. It runs on trust, relationships, and perceived social influence. These currencies should only grow in importance, even if the development of a true post-scarcity economy doesn't occur in the time frame addressed in this report.

Crowd-Sourced Innovation

Leading organizations are increasingly tapping into open-source networks and using crowd-sourced methods for solving problems.

These include the use of social media platforms for design contests, marketing strategies, and structured problem-solving challenges.

Innovators will often take on these challenges with the promise of a monetary prize or funding for further research.

The technology backbone is increasingly run on open-source platforms such as the Linux operating system and the Apache web server. These technologies are created and maintained by thousands of programmers dedicated to free and easily modifiable products.

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CHANGE DRIVER 2

The Shifting Needs of Consumers and Advisors

The modern family faces new risks, and many of the traditional sources of financial security no longer exist.

Consumers in the future will be much more proactive in finding the right investment and insurance products to meet their needs.

By the same measure, advisors will be looking to their leadership team to provide them with the tools, technology, and products to meet their clients' needs.

Top Trends to Watch and Manage

- Women as primary breadwinners and financial decision makers
- Growth in new consumer markets such as LGBT (lesbian, gay, bisexual, and transgender) families
- Online avenues for information gathering and product sales

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 127.*

The New Risks to the Modern Family

Life insurance was developed in a time when the nuclear family was the norm and the family needed to be protected from a husband and father's untimely death. But in the 21st century, the nuclear family is no longer the norm.

In 2010, nuclear families with their own children made up just 20 percent of the population.[39] At the same time, the number of single-parent families, unmarried couples, and families formed by divorce and remarriage has been steadily growing.

The industry will also see increased growth in alternative family types, particularly in states that allow same-sex marriage and adoption.

Insurance and financial advisors will need to seek out products that fit the new risks of the modern family and sell to career women, single parents, LGBT (lesbian, gay, bisexual, and transgender) couples, and consumers concerned about protecting their extended families.

The changing family also presages changes to the firm's most important clients: their advisors. As the modern family changes, so does the future advisor workforce. They will want to work for firms that share their values and reflect their own diversity.

Firms that can reflect the diversity of the modern family in their own workplaces will have a distinct advantage in attracting the best young advisors. In turn, these advisors will bring with them valuable experience, cultural competency, and networks in growing markets.

Trust and Consumer Expectations for the Next Decade

By far the biggest challenge facing the industry in the near future is consumers' lack of trust in financial service professionals in the wake of the global financial crisis of 2007–2012.

At the macro level, consumers are looking to reduce risks and are turning to companies they feel share their values. At the same time, they are increasingly distrustful of the insurance and financial services industry.

Consumer trust in the industry, which had never been particularly high, hit an all-time low in 2008. This has a direct impact on sales, as seven out of 10 new consumers decide if they can trust an advisor during the first meeting, and that trust is vital to sales.[40]

Firms will need to develop new ways of developing affinity and shared values with their customers.

Future generations of advisors will also demand that their companies earn the trust of their clients and the public. Increasingly, younger workers are willing to trade autonomy and salary to work for a company that shares their values.

A recent survey found that 72 percent of students and 53 percent of workers listed "a job where I can make an impact" as very important or essential to their happiness. Comparatively, just 21 percent of workers and 36 percent of students rate "wealth" as very important or essential to their happiness.[41] This is a clear example of how addressing aspects of work that are important to encore workers (see page 31) will also make the work more attractive to the general population.

These trends in the workforce will likely be reinforced if fee-based advising grows, as it will better align the underlying values of new workers with their economic incentives.

Rebuilding trust with the public and advisors will require new products that address the real risks faced by the modern family. Companies are cutting back on benefits from defined-benefit pensions to health insurance. Most consumers have been left to invest for their own retirement, and health insurance costs are rising.

Related to the rising costs of care is the need for many families to arrange for long-term care for themselves and loved ones. Premature mortality is less of a concern for wealthier dual-income households who believe they can self-insure.

Combination products that provide life coverage with protection against the additional risks faced by the modern family will likely face higher future demand.[42]

New Demands for New Generations

Consumers are looking for new ways to educate themselves and interact with advisors outside of a face-to-face meeting. This is especially true of younger customers, who often use the Internet and social media to educate themselves before buying products.

Online tools such as quote generators and online purchasing will make it easier and cheaper to reach consumers, but further pressure commissions as products become increasingly commoditized.

The downward pressure on commissions will be felt most in simpler products aimed at the middle market since they will be easier for customers to compare online. Also, as technology empowers customers, they will find it easier to compare more complex plans and use modeling and simulation tools to find plans that are the right fit for them.

The drive for transparency and technology will be even more important as younger generations enter their prime earning years. Consumers in their 20s and 30s, used to shopping online, often compare products and services through websites that provide product reviews and compare prices. They are able to find out almost anything they want to about a product or service, and they reward those companies that are open and transparent.[43]

They may desire a face-to-face or virtual face-to-face meeting before making a purchase, especially for more complex products, but only after they have had the opportunity to educate themselves (rather than meeting with an advisor to be educated). Asking them to sit down for a meeting with sales representatives before they have the basic information is extremely off-putting.[44] As noted earlier, financial literacy education will be critical to the industry's health and reach, and firms must take into account the different ways that consumers want to gather information as they develop their financial literacy strategies.

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Serving the Modern Family	Seek a broader array of policies that meet different needs and risks.	Provide quality statistics and market information on alternative families.	Seek out opportunities to expand your customer networks.
Building Trust	Explore partnerships with trusted intermediaries in your community.	Educate and enforce strong consumer-protection policies among your teams.	Ask for referrals from satisfied customers, and work to educate new customers.
Selling to Younger Clients	Provide multiple channels for consumers to educate themselves.	Offer less complex, more affordable products.	Explore social media for networking opportunities.

Questions to Consider

One-Minute Debrief

1. Which consumer trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. To what extent does your firm provide resources online and other easy ways for consumers to educate themselves and contact your advisors? How might these methods also support financial literacy activities by your firm?

2. How can your advisors better meet the needs of the modern family? What better array of products might you offer to address some of the unique risks that modern families face?

3. How does the public gauge the trustworthiness of your firm today? What, if anything, is that reputation based on? What one step might you take this year to enhance the perceived trustworthiness of your firm?

First Step

What *one thing* will you do this year to make your firm easier to do business with for today's consumers?

Additional copies of the worksheet can be found at gamafoundation.org.

Drill Down on Trends

The Non-Nuclear Family

The traditional nuclear family with a primary breadwinner and 2.5 children, the basis of traditional life insurance, is rapidly becoming a thing of the past. Only 17 percent of households have a husband in the workforce and a wife who is not. Women now bring in one-third of the family's income on average, and many are now the primary or sole breadwinners.[45] Women are also much more likely to be raising the kids alone, as 41 percent of all babies are now born out of wedlock.[46] Young adults are frequently staying at home longer as they try to kick-start a career or pay down student debt. By the same token, unmarried households with both same-sex and different-sex couples have grown by 40 percent and 80 percent, respectively, since 2000.[47]

The Importance of Trust

A recent survey conducted during the height of the Occupy Wall Street movement found that 64 percent of consumers believe insurance advisors and brokers are more interested in fees and commissions than what is right for them. Less than 25 percent expressed trust in insurance advisors and brokers. Lack of trust directly affects the ability of advisors to sell the right investment and insurance products to their clients. Customers who trust their advisors buy three-fourths of the time; those who don't buy less than one-third of the time. [48]

Fee Transparency

One more sign of the increasing transparency across the financial services and insurance industry is the 401(k) fee disclosure that went into effect in 2012. The Department of Labor now requires plans to disclose the investment management, record keeping, administrative, and other fees being charged. Currently, the rules are unclear on their effect on annuities in a 401(k), but clearly leave outside their scope annuities outside of a 401(k) and other life insurance policies.[49] But similar disclosures for life insurance may be required in the future, particularly for annuities.

Affinity Marketing

The growing importance of trust and transparency for consumers could lead to a renaissance in affinity marketing. The best example is the growth of insurance plans and investment products offered under the umbrella of the AARP. The AARP acts as a trusted brand and intermediary and helps to counteract the current high levels of distrust in the insurance and financial services industry among a select group of consumers. The influence of consumer groups such as the Consumer Union is also likely to grow as more consumers go online to compare insurance and financial services products.

The Growing Income Gap

Income inequality is a large and growing concern in the United States and may soon affect even firms targeting high-income markets. The median income in the United States peaked in 1999 after adjusting for inflation, and much of the increase was fueled by greater participation by women in the workforce. Meanwhile, the wealth of the highest-income earners has been growing rapidly in the last decade. In 2004 and 2005, the top 1 percent of households took home the largest share of national income since 1928. The income gains increase dramatically even further up the high-earned income scale, which could prompt popular backlash and further calls for removal of tax breaks for products like annuities.

NOTES

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CHANGE DRIVER 3

Technologies for a Powerful Sales and Service Force

The future firm is poised on the cutting edge of technologies connecting advisors to their clients, colleagues, and leaders.

Advisors will have powerful customer relationship management (CRM) systems that integrate social media and other data to provide sales insights anytime, anywhere.

Both advisors and clients will have access to new products that use sophisticated modeling and simulation software to dynamically price and reduce risk.

The firm will also have a virtual presence where advisors can interact and build trust with clients from anywhere in the country.

Top Trends to Watch and Manage

- Social media as a powerful sales and customer relationship tool
- Mobile technologies connect data and analysis
- Modeling and simulations of new client markets
- Virtual worlds for collaboration and client communication
- Products featuring proactive risk management

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 141.*

CAPABILITIES

Technology Differentiates the Best From the Rest

The best financial advisors are entrepreneurial risk takers who look to partner with the best organizations for both themselves and their clients. They may be independent minded, but they also recognize the value of collaboration and teamwork inside a dynamic workplace.

New advances in collaboration and productivity technology will enable them to work at the highest level of their ability and will aid them in providing high-level service.

They will gravitate to organizations that successfully combine technology, independent thinking, and high-value teams because the results will show through in better outcomes and better compensation.

The firm will be operating in a competitive environment where resources for technology are scarce.

Many small agencies are delaying new technology projects to maintain compensation levels and deal with new regulatory requirements. Larger insurance companies are cutting back on spending now that business economics make it difficult to continue subsidizing their career distribution systems.

Technology adoption can also be extremely risky for small and large firms alike. The research shows that 65 to 80 percent of information technology projects fail to meet their objectives, overrun deadlines, or cost more than planned. The problem rarely lies with the technology itself. Often it is the people who determine the success or failure of a project.[50]

Field leaders must ensure that new technology leverages existing strengths and addresses the needs of the advisor workforce.

When money is tight, it is the frontline leaders who can make or break a critical investment in new technology. They have a better understanding of how their advisor teams collaborate and create value for themselves and the firm.[51] Much of this occurs along informal pathways that can be hard to replicate or enhance with technology.[52]

Client Data Everywhere and Anywhere You Need It

We used to be able to easily draw a line between home and office. Now we are constantly connected through our mobile devices, responding to emails, text messages, Facebook posts, and tweets.

Just when you are getting comfortable with the new world of *anytime* communication, the landscape is about to shift again to ubiquitous or pervasive computing, what is now called "everyware" technology.

In this brave new world of everyware technology, *everything* we use to communicate and store data will be connected. The only limits on what can be connected and what sorts of data will be collected

will be imposed by us through the privacy settings on our mobile devices and whom we invite into our "friend" networks.

Some of the things that are likely to be connected include health information, financial records, energy usage data, environmental sensors, and our more sophisticated household devices.[53]

The vast realms of data collected, often called "big data," will provide many opportunities for companies that have the modeling and simulation tools required to use it correctly.

Most importantly, wireless networks combined with GPS positioning will reveal everyone's and everything's location to those with the right access.

Technology companies are already linking detailed client information, from social media and other sources, to CRM systems. Soon it is likely they will integrate location services, so advisors who are linked as "friends" through social media could find out the location of potential clients.

For example, an advisor at a concert could be alerted by his mobile device when a potential client is at the same concert. The advisor could then pull up a wide variety of information on the prospect through his CRM application (everything from his Klout score to his latest musical preferences) and arrange an ad hoc encounter.

By the same token, first-line and frontline leaders will have greater access to a wide range of data on their advisors and clients. They'll have at their fingertips, among other functions, modeling and simulation tools that allow them to map out an agent's social networks, monitor client interactions, and improve worker productivity.

Used correctly, this technology could dramatically improve an advisor's ability to identify "influencers" in his or her network and increase sales through word-of-mouth advertising.[54]

On the other hand, first-line leaders could easily alienate important advisors by giving the impression that they are invading their personal privacy or trying to appropriate valuable personal contacts for the firm.[55]

Self-Learning Products Drive Advisors to Learn More About Their Clients

The era of big data will provide new ways to structure insurance products.

Auto and health insurers are already offering new plans that include sensors that monitor driving behavior and alter pricing based on the information. Health insurers (and employers) are increasingly offering incentives to members who enroll in health-improvement plans and share health-improvement data.

In the near future, it is likely that life insurance underwriters will be able to easily pull health information about a potential client from his or her personalized health record, allowing carriers to move from passively identifying and pricing risk based on demographics to proactively using information captured in the electronic health record and other databases.

The result will be highly customizable and self-learning products that adapt to a patient's unique risks and provide incentives for that person to pursue a healthier lifestyle.

Firms specializing in these products will need to devote more time and attention to clients throughout the life of the policy.

As their health changes, clients will naturally have questions about the effect on their life insurance coverage and premiums. The advisor could also take a more active role in providing incentives for their clients to improve their health.

Of course, this new model won't be attractive to every advisor or to every consumer. But it might be useful for advisors who want to develop a more interactive and trusting role with clients that crosses a wide range of products and services.

Tapping the Potential of the Virtual Firm

Over the next several years, we will see more customers going online to interact with their advisors and find out the latest information on products and services.

The number of consumers going online for product information has increased dramatically in recent years, but despite the growth of the Internet, most customers purchase life insurance and financial products through face-to-face meetings with a financial professional.[56]

Trust is the important differentiator. Customers value trust when making financial decisions, and nothing builds trust in the same way as a face-to-face meeting.

However, the value of the face-to-face meeting may recede in the near future as technology captures greater amounts of the non-verbal communication vital to building trust.

For example, new telepresence conference rooms re-create the intimacy of a face-to-face meeting with participants halfway around the globe. Adoption of this technology will accelerate as rising energy prices make corporate travel more expensive and the cost of installing the suites decreases because of technology improvements.[57]

Researchers are also building better avatars that capture non-verbal communication for virtual worlds like Second Life. Virtual worlds are three-dimensional, online landscapes that allow people from around the globe to interact with each other.

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Technology Adoption	Systematically monitor new technology trends and technology investment decisions.	Share knowledge of best practices with advisors. Communicate with advisor teams about their technology needs.	Leverage existing technology resources. Share needs and insights with leaders and colleagues.
Incorporating Social Media	Have a social media strategy that reinforces your brand identity.	Train advisors in the business uses of social media. Monitor level of adoption and appropriate use.	Create a sales identity in the social media environment. Experiment with different social media channels.
Leveraging Everyware Technology	Identify and adopt new tools that can leverage the growth of "big data." Develop robust privacy and security policies.	Communicate with advisors about creating personal time and space.	Experiment with new CRM functions. Listen closely to clients and avoid inadvertently invading their privacy.
Utilizing the Virtual Firm	Monitor other firms and industries for best practices.	Encourage younger advisors to experiment and share success stories.	Keep an eye out for clients who may be early adopters.

Questions to Consider

One-Minute Debrief

1. Which technology trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. Where will you invest in technology for your firm to get the best return on investment?

2. Who among your colleagues or competitors are early adopters of technology, and what investment and implementation lessons can you learn from them?

3. Who in your firm is at the leading edge of technology, and how might you use his or her knowledge to help your firm prepare for the future?

First Step

What *one thing* will you do this year to leverage the technology already in place (but perhaps underutilized) to provide greater value to your firm's clients and prospective clients?

Additional copies of the worksheet can be found at gamafoundation.org.

Drill Down on Trends

Portals for Learning and Collaboration

The current trend in operating systems and related applications is to create integrated portals that streamline work across multiple devices. Apple is currently leading the market with its focus on integrating user experiences across its many products through services such as iCloud. Microsoft is also moving in the same direction with its Windows 8 operating system. Windows 8 will enable users to seamlessly move between multiple devices with touch-screen capabilities. Business software providers will follow suit with applications that blur the line between devices.[58]

Evolution of Mobile Technology

By 2015, the global subscriber base for mobile devices is estimated to increase from 3.6 to 4.6 billion.[59] The ubiquitous presence of mobile devices, and the "always connected" nature of the latest services, will create vast amounts of useful data, including buying habits, social media usage, music preferences, location, and activities. Mobile devices linked through the cloud will also enable workers to collaborate or undergo training anytime and anywhere. Greater use of mobile collaboration technologies will hasten already-existing trends toward distributed, virtual workforces and distributed co-creation.

The Role of the ACA

The 2012 decision of the Supreme Court to uphold the Affordable Care Act (ACA) paves the way for fundamental reform in the health-care system. Individual and small-group health insurance will shift to online exchanges run by the states. Soon those very same states will be making decisions regarding broker access to the exchanges. The decision will also hasten the current push toward health data capture and collection. The locus of the new collection of health data will be the patient's electronic health record (EHR). The EHR will likely become an important source of information for underwriting and the development of new life insurance products.[60]

New Technologies for Non-Verbal Communication

Researchers are working hard to create new communication technologies that capture and analyze the 70 percent of non-verbal communication that is currently lost in video chats, phone calls, and emails. For example, sociometers, which analyze non-verbal cues, could be integrated into communications technologies to allow advisors and their leaders to analyze body language to tease out ways to improve client interactions, financial advising, and intra-office meetings.[61] The development of more lifelike virtual worlds and avatars should help fuel the adoption of virtual worlds for business applications such as increasing brand awareness, developing virtual prototypes, and conducting meetings at low cost.[62]

Integrating Social Media Into CRM Systems

Many CRM providers are working on integrating social media technology and metrics into sales software. The greater integration of social media will make the written and unwritten "rules" on who owns a social media account or even access to clients more complicated. Already companies are going to court over the control of Twitter or Facebook accounts. Likewise, many companies that require employees to post on their Twitter or Facebook accounts are instituting policies that give them access to followers and content control when an employee leaves.[63]

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CHANGE DRIVER 4

Managing Privacy and Security in the Networked Age

Advisors and leaders in the future will be increasingly networked, and they will have access to a wide variety of personal data on their customers.

Traditional definitions of privacy and security will shift as new technology blurs the line between the physical and virtual worlds.

Firms will need to use their best advisors to connect to a wide range of networks.

They will also be challenged to ensure that customer and advisor data are used appropriately and protected from increasing threats such as cybercrime.

Top Trends to Watch and Manage

- Shifting cultural norms regarding privacy between generations
- Greater prevalence and impact of cyberattacks
- Growing discontent by anti-corporate fringe groups

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 155.*

CAPABILITIES

Privacy in a Networked Culture

We are currently undergoing a subtle — but radical — cultural shift.

Public opinion is no longer being shaped by political or media elites alone, but in part from the bottom up by individual bloggers, interest communities, online forums, Twitter, and other virtual communities.

The creation of information no longer runs down from centralized creators of content, but from the interactions of many individuals in interconnected networks.

These networks also shape our opinions of the world, creating self-reinforcing mono-cultures of thought and opinion.[64]

Advisors, and the firms they represent, need to be part of these networks and create connections with potential customers, especially from younger generations.

Firm leaders will be faced with a number of new privacy challenges as social media networks grow more important for business.

The lines of privacy between these networks are not well defined, and they are easily shattered by companies involved in market intelligence and data analytics.

It falls on the first-line and frontline leaders to ensure their advisors are *appropriately* leveraging this knowledge to develop leads and manage clients.

Managing in a Networked Culture

Managing and monitoring social media in a networked culture will create some serious questions for firm leaders.

- Field leaders have an interest in monitoring the social media networks of advisors, but do they have the right to do so?
- Does the advisor or the firm own the social media accounts that advisors manage on a day-to-day basis?
- What happens when companies require their associates to have a social media presence and these associates leave?

Companies are only now beginning to wrestle with these questions. In the process they are realizing that the answers are not simple ones, and they are ones with potentially big impacts on brand reputation and trust between advisors, clients, and the firm.

Networked culture is currently a shifting landscape based on social norms, rather than clear rules of privacy, and it can be all too easy for the firm and its advisors to alienate potential customers.

Senior leaders, who are often older, see the potential threats posed by social media, and are much more comfortable with a linear model of marketing where the message is carefully crafted, sent out into the market, and carefully monitored for impact. In short, they are used to being in control of their own brands and firm image.

On the other hand, younger advisors and managers are much more likely to have a more relaxed and unrestrictive approach to social media.[65]

This is a significant challenge, especially in managerial firms where parent companies may be increasingly protective of potential damage to their brands.

Growing Cyber Threats

The last decade has highlighted the benefits of widespread interconnectivity, while the next could very well highlight the growing risks to our networked culture.

The 2012 World Economic Forum in Davos, Switzerland, highlighted the growing risk of cybercrime in its survey of economic and business leaders. The survey warned of the "impacts of crime, terrorism and war in the virtual world" that could eventually become as profound as their analogs in the physical world.

The report highlights some of the high-profile cyberattacks and viruses that hit the world in the last year, including the Stuxnet virus and the multiple attacks on businesses coordinated by the neo-anarchist activist group Anonymous.[66]

Our growing networked culture and its foundation of vast databases are uniquely vulnerable to attack in ways that could jeopardize firms and even the industry.

Businesses are increasingly interconnected and rely on massive amounts of data for client management, marketing, financing, and other everyday functions.

Customers and advisors rely on their mobile devices and cloud computing for storing and managing their personal networks, health information, financial records, and personal data. Increasingly customers, and by extension their advisors, rely on the firm to protect valuable financial and health-related information.

The costs of widespread technology failures for both consumers and the firm will continue to grow. As the cost grows, so will the need for cyber-insurance as a way to hedge against risk, and this could become a growth market for multiline firms.

The threat of cybercrime will continue to rise through 2020 as the technology tools needed to sabotage, subvert, and disrupt businesses continue to evolve. The threat could be accelerated by growing wealth inequality both inside the United States and abroad.

Field leaders will be at the forefront of protecting vital client data from black hat hackers, criminal networks, protest groups, competitors, and even foreign governments.

Frontline leaders will also need to ensure that their advisors keep client data secure by being smart about the use of their work computers, mobile devices, and network passwords.

Both the need for, and the cost of, securing proprietary databases will rise as cyberattacks continue to grow. Firms will need to invest in intrusion detection systems, vulnerability management tools, and identity management systems.

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Shifting Attitudes Regarding Digital Privacy	In firm policies, try to strike a balance between innovative use of social media and privacy protections.	Use younger advisors as guides to cultural norms regarding digital privacy.	Be sensitive to privacy concerns, and when in doubt, ask permission so you never have to ask for forgiveness.
Firm and Advisor Behavior in a Networked World	Develop strong and flexible policies on social media use. Talk regularly with advisors about social media use.	Provide latitude to advisors to experiment with new marketing and communication channels.	Follow the firm's policies about social media use and ownership.
Growing Cybercrime Attacks	Follow industry best practices for securing client data.	Conduct regular training on protecting client data.	Be prepared to share security policies with clients.
Securing Mission-Critical Systems	Conduct regular stress tests on mission-critical systems.	Keep lines of communication open with technical departments about data security.	Keep backup copies of vital information on a secure server.

Questions to Consider

One-Minute Debrief

1. Which privacy and security trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategic Questions

1. Whom do you know, personally or professionally, who has a good understanding of the risks associated with our networked culture? How might this person act as a guide, educator, or mentor for your firm?

2. What technologies and protocols is your firm using to secure valuable data from potential threats? To what extent are these measures stress-tested against attack?

3. What policies and practices does your firm have in place to protect client privacy? How well are they understood by your advisors? Are they easy to explain to clients and prospective clients?

First Step

What *one thing* will you do this year to strengthen your firm's procedures for continuing to conduct business following a technology failure or natural disaster?

Additional copies of the worksheet can be found at gamafoundation.org.

Drill Down on Trends

The Networked Self

The networks that we inhabit, both in the real and the virtual worlds, form the basis of our identity, which can shift in both subtle and profound ways.[67] This identity is created less as an individual prerogative than as a gestalt of connection with both humans and things. We are both the self that we show the world and increasingly the web of hyperlinks, tweets, blogposts, instant messages, friendlists, music preferences, buying patterns, and other connections we create through our various social media profiles. In the process of social networking, we validate the existence of others and have our own existence, both mundane and sublime, validated in return.[68] The Cartesian statement "I think therefore I am" is giving way to a new understanding of self. Increasingly people, especially younger people, are basing their concept of self around the networks they interact in. Increasingly, this simple statement of self needs to be rewritten to say, "I link therefore I am."

The Power-Law Distribution

One interesting phenomenon that has emerged in the study of technological and social networks is the prevalence of power law distributions. In these networks, each new link in a network is much more likely to attach itself to a node that already has a high number of links. For example, a new blogger is much more likely to follow, and link to, a well-known and respected blogger. Thus a very small minority of well-known bloggers attract the majority of readers and new links, and have the most overall social influence. In marketing, these highly linked nodes are often referred to as "influencers" because of their ability to sway public opinion and buying patterns. Networks and systems where the nodes are defined by power law distribution can be resistant to random failure, but are also vulnerable to carefully targeted attacks. In the social context, this can mean the best way to target a rival firm is by discrediting or co-opting an advisor or client who acts as a node in a given network.[69]

Business Use of Social Media

A recent survey of executives conducted by the Economist Intelligence Unit showed that less than half of companies used social media to communicate with customers in 2011 and only 11 percent did so over the previous three years. Firms that appoint a single individual to manage social media activity tend to be happier with the results than those that use a team approach. Most of these companies are investing in social media out of fear of customer criticism rather than to build positive customer opinions of a brand or company. Only 20 percent of companies are investing in the mobile applications that will drive the future of the networked culture.[70]

The Hyper-Connected World

Hyper-connectivity is rapidly becoming a reality across the globe. The sheer volume of connections and the huge amounts of data are nearly impossible to comprehend. More than 5 billion mobile phones now connect people across the world with interconnectivity and cloud-based computing.[71] Wireless signals now cover more of the globe than the electrical grid, and IBM estimates the number of connected devices will hit a staggering one trillion by 2015.[72] The number of interconnections, and the reliance on them for everyday life, makes our modern life increasingly vulnerable to cyberattacks and digital disruptions.

Increases in Cybercrime

Cybercrime is a notoriously difficult thing to quantify, but all signs point to a dramatic increase in attacks over the last three years.[73] Many firms are reluctant to release details on cybercrime attacks, but when such details are released, the monetary costs can be staggering. For example, in June 2012 the head of Britain's MI5 security service said in a speech that state-sponsored cybercrime cost a major British company more than £800 million in potential revenues.[74] Companies are seeing more malicious attacks by outside agents, but recent surveys report that it is attacks by insiders with authorized access that are the most costly to firms.[75]

NOTES

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MARKET DRIVER 5

Advanced Data Analytics Empower Advisors and Consumers

Successful firms in 2020 will be challenged to integrate the growing amounts of "big data" into actionable insights for their advisors.

They will be aided by better tools for market intelligence and data analytics. At the same time, the consumer will have access to better tools for analyzing complex investment and insurance products.

This will add pressure to commoditize many insurance products, forcing the firm and its advisors to bring additional value in other ways, such as through the advising process or related services.

It could also create a growing market for highly customized products.

Top Trends to Watch and Manage

- Better tools for analyzing data and turning it into usable knowledge
- Growth in targeted intelligence for micro-markets
- Commoditization of existing products
- Increased customization of new products

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 167.*

STRATEGIES

Targeted Intelligence Systems Drill Through Big Data

Data analytics is not a new concept. There are few successful businesses in the information age that don't use data to improve their business processes, manage employees, and analyze customer behavior.

Research shows that businesses that use data-driven decision making have higher levels of output and productivity.[76]

However, data-driven decision making is about more than investing in expensive technology systems. It is also about adapting firm management practices and organizational culture to maximize the use and potential of data.[77]

While the concept of data analytics is not new, the scale of big data available to firms and the tools needed to manage it are.

One of the hallmarks of this new flood of data is increased interoperability, which makes it easier to collect and share data and allows business software to create a more complete picture of ongoing trends.

Increasingly, companies are using advanced modeling and simulation tools to help turn big data into knowledgeable insights for business. This could provide opportunities for the firm to add value for their advisors by providing them with more leads, new sales ideas, and targeted marketing literature.[78]

Better data, modeling, and simulation software will also allow advisors to drill down to the local markets that matter.

For example, a Seattle-based firm could go beyond the generalities provided by sales guides of the buying patterns of the African-American marketplace. Instead they could use the growing amount of big data available to do precise modeling of an important subset of the community, such as second-generation East Africans in Seattle. In the process, they could find unique markets for potential growth.

The firm could then connect this model of the market to leads developed through better CRM systems and even run simulations on the long-term success rates of targeting that market.

Advanced Analytics for Advisors and Consumers

Over the next eight years, the U.S. economy will need to dramatically increase the supply of both data-savvy managers and advanced analytic software.

The growth of data, and the specialized knowledge required to interpret it, are quickly outpacing our ability to train workers to use it effectively.

Global consulting powerhouse McKinsey & Company estimates that the United States needs 1.5 million additional data-savvy managers just to cope with the current growth in big data.[79] The growth will likely increase as the amount of data grows to unimaginable heights.

In the process, the growing amount of data is leading to very specialized knowledge areas, which make it nearly impossible for any one individual to take a systems-based approach to analyzing and solving problems.[80]

Fortunately, the analytical systems designed to deal with the growth of big data are making it easier for users to turn large data sets into useful information and usable knowledge.

Some of these systems are already in wide use and familiar to many of us. For example, the credit scores that organizations use for everything from bank loans to job applications are an automated and processed form of thousands of individual purchases, credit card statements, and loan repayments.

These systems continue to improve and are now able to handle larger amounts of data, display it in ways that make sense to the average user, and support decision making through modeling and simulation. In the process, they are making all-encompassing, undynamic representations of complex data, such as the credit score, less useful in creating individualized and customized financial services.[81]

The widespread use of advanced analytics has the potential to dramatically change the insurance industry from top to bottom.

Consumers and advisors will have better tools for analyzing complex insurance products.

This will make it easier for advisors and consumers to find the right products at the right price. Advisors will be able to offer highly customized products that cover unique risks or a broad array of risks in a combination product.

For example, carriers could partner with firms to draw on the wealth of customer data to conduct long-range modeling and simulations to determine plan premiums. Also, underwriting would be largely automated, leading to faster approval and sales. Of course, these products would only be as good as the data used in the modeling and simulations, making it vital for the firm to create safe, secure, and interoperable streams of data.

However, there is one large potential downside to the greater use of advanced analytics. Better tools for analyzing products and adjusting them to fit a consumer will bring additional pressure to commoditize existing insurance products.

Consumers will feel more comfortable going online to purchase products, and insurers will be able to offer them more sophisticated technological distribution channels. This has already happened in areas like auto insurance, where the agent has been largely removed from the process.

Commoditization will force down compensation for many simpler products and force the firm and its advisors to add value to their client interactions through better advising, trust building, and services important to the client.

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Capitalizing on Market Intelligence	Look for market intelligence solutions that are targeted and linked to lead generation.	Identify the markets that matter in your community. Improve your ability to analyze complex data sets for emerging market trends.	Continually update your skills on the latest systems.
Managing Big Data	Strategically invest in data analytics.	Explore and share best practices for data analysis.	Look for ways to use data analytics to drill down to markets that matter.
Using Models and Simulations	Watch for emerging trends that might point to product commoditization or customization.	Understand how modeling and simulation software can aid in product analysis and sales.	Add value to the buying process beyond what can be found by consumers online.

Questions to Consider

One-Minute Debrief

1. Which data analytics trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. To what extent do you and your leadership team reward data-driven decision making versus intuitive or habitual decision making?

2. How can you improve your firm's data culture by making better use of market information available to you today to drive more leads and sales for your advisor teams?

3. How will your business be affected by consumer access to advanced tools for analyzing products? Which products will be most affected? Which advisors are best or worst positioned to provide client value in a more transparent business world?

First Step

What *one thing* will you do this year to increase the use of data (versus intuition or habit) in the decisions your advisors and managers make?

Additional copies of the worksheet can be found at gamafoundation.org.

Drill Down on Trends

The Big Data Flood

The volume of data available to companies has exploded in the past few years. Every year there is a 40 percent growth in global data generation, and companies with more than 1,000 employees store 235 terabytes of data on average. This is compared with a paltry 5 percent growth in global information technology spending. Much of the new data is generated by consumers or autonomous devices. Consumers on Facebook alone generate more than 30 billion pieces of content every month. The transportation, automotive, industrial, utilities, and retail sectors have more than 30 million networked sensors, and this number is growing by more than 30 percent a year.[82]

Modeling and Simulating Human Behavior

One of the most exciting areas of research is in the modeling and simulation of human behavior because of its wide applicability across industries. Researchers are developing intelligent user interfaces that improve the efficiency, effectiveness, and naturalness of human-machine interactions, systems that can map and analyze social network analysis and agent-based modeling.[83] Agent-based models, which refer to the autonomous agents used in a computational model, can be used to run simulations of complex human behaviors to predict behavior patterns and test new business strategies. These models are growing in sophistication because of advances in computing power and research on cognition and social systems. Models of human behavior can help business leaders understand how innovation occurs inside the workplace and among complex networks of companies.[84]

Analytic Systems Down the Cost Curve

As advanced analytic software continues to grow and mature, it will roll down the cost curve, making it available to smaller firms, advisors, and eventually customers. The financial services industry has already witnessed a similar process with financial tools. A decade ago, many sophisticated mapping and trend analysis softwares were only available on expensive Bloomberg terminals. Now they are nearly free for smaller investors through a cornucopia of investment websites and online brokerage services. This has opened up investing to a larger audience and allowed individual investors to operate in sophisticated markets such as foreign currencies and use more sophisticated hedging strategies such as stock options; it's also helped financial services companies to create new investment vehicles such as exchange-traded funds.

NOTES

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MARKET DRIVER 6

Shifting Business Models Shake Up the Industry

A tough market environment, combined with technology and regulatory changes, will force consolidation in the industry.

Private equity money will enter the market, and many insurance companies will sell or scale back their managerial firms.

The middle market will grow based on new products and distribution channels, and many smaller firms will thrive by embracing a culture of shared values.

Top Trends to Watch and Manage

- Consolidation among firms
- Investment by private equity
- Growth in middle-market products
- Consumer demand for products from companies that share their values

Forecasts

Find supporting information in the **Drill Down on Trends** *section that begins on page 179.*

STRATEGIES

Private Equity Pressures Smaller Firms

The last few years have been trying ones for firms in the investment and insurance industry.

Firms with a focus on financial advising have seen a raft of new regulations designed to protect consumers. At the same time, low yields and market returns have damaged much of their most consistent sources of revenue.

Large insurance companies are looking at the regulatory landscape and finding less reason to hold on to their own agencies. Increased government scrutiny, potential restrictions on offering incentives to sell their own products, and low yields have made these companies view managerial firms less as valuable channels for distribution and more as a distraction from their core business.[85]

Smaller general agencies, which have faced a constrained market for small-business lending, have been particularly hard-hit by new requirements. New regulations will further strain the capital budgets of firms, as they will need to invest in new compliance and technology systems.[86]

Consolidation and competition in the broker/dealer (BD) space will continue as private equity firms revitalize the industry and acquire smaller independents. Private equity sees long-term value in financial advising, particularly with demographics pointing toward a growing market for retirement products.

Many independent BDs also stand to gain should trading volumes increase and the extremely low interest rates return to normal. And private equity sees an opportunity to capture market share by attracting independent advisors and forcing out many small and midsize firms. They bring management expertise, strategic thought, scale, and capital to an industry struggling to invest in new technology and compliance systems.[87]

The end result in 2020 of consolidation and competition in the BD space will likely be a barbell-shaped industry, with larger firms dominating the high end of the market and many smaller firms growing organically in niche or local markets.

Independent BDs with a focus on investment planning may become potential targets for larger firms looking to achieve economies of scale, while managerial firms may see themselves spun off from the parent company or sold off to private equity investors.

Many smaller independents will feel the need to consolidate among themselves as costs increase and larger firms seek to attract the best advisors.

Markets and Products for Growth

New distribution channels that rely on disruptive technologies could dramatically reshape the firm by compressing compensation on products and forcing greater competition from overseas competitors.

Better technology allows customers to analyze complex plans online, and insurance companies could look to revitalize growth in this market by offering simpler products that can be sold online or through a noncommissioned sales force.

The advisor force, particularly in managerial firms, could see increased diversification, with a growing number of noncommissioned advisors interacting with clients rather than pounding the pavement selling products.

By 2020, firms could see increased demand and supply of products aimed at the middle market. On the supply side of the equation, increasing sales through online channels combined with the potential of virtual firms could lower costs.

Inexpensive analytical systems for consumer use could also lower expenses by allowing consumers to explore the cost and coverage of products before contacting an advisor. This fits with compensation recommendations in Study One, and may presage new roles for advisors that focus on noncommission sales.

On the demand side, consumers are looking for security and new products that address new risks for the family. As noted earlier, consumers will also be looking to the private market for increased security as companies cut benefits packages.

A revitalization of the middle-income market will create opportunities for firms well positioned to seize them. A growing middle- to low-income market creates new customers and a rare opportunity for organic growth in a mature industry.

As noted in Study One, simpler products that provide some protection against financial fluctuations and longevity risk are likely to do very well in this market. In particular, whole life plans have seen strong growth in the face of volatile markets and flat bond yields.

Trends for the Middle Market

- Growth in virtual sales
- Inexpensive analytical systems
- Cuts in company benefits
- Security demanded by consumers
- New risks for the consumer

Other products aimed at the middle market that could see growth include lifetime income annuities, longevity insurance, long-term-care insurance, and combination products.

As noted earlier, the rich will probably grow richer as the assets of high-net-worth clients likely recover and grow over the next several years. At the top end of the market, underlying trends including globalization and automation are fueling the wealth of the country's highest income earners and will likely continue to do so in the near term.

But future attempts to address the budget deficit could change the relative value of insurance products. The end of the Bush tax cuts on investments, removal of tax breaks for municipal bonds, and

higher marginal tax rates could fuel more growth in the affluent market as tax-advantaged products like annuities become more attractive.

On the other hand, politicians could also strip the preferential tax status of insurance products to raise revenue. This could have a devastating effect on the market for variable annuities, universal life, and certain categories of whole life products.

Small Firms Focus on Shared Values

As noted earlier, trust in financial institutions is at a low point. Many consumers are looking for companies that share their values and have strong ties to their local communities.

Corporations, for their part, are often trapped in a narrow approach to value creation that focuses on short-term financial performance at the expense of long-term strategic thinking. In the process, they ignore the well-being of their customers, suppliers, and the natural environment.[88]

The solution lies in creating shared value for both businesses and the communities they serve. Some of the leading businesses in the world, such as General Electric, Google, and Johnson and Johnson, realize the importance of shared values and are working with their internal leaders to create a deeper appreciation of societal needs, a greater understanding of the true bases of company productivity, and the ability to collaborate across profit/nonprofit boundaries.[89]

Smaller firms can create a virtuous circle by creating shared value between themselves and the communities they serve. This is especially true for firms with a strong presence in niche markets that may be overlooked by larger firms.

Shared value can be a differentiator for smaller firms and an advantage in competing against larger and better capitalized firms. Smaller firms are closer to the communities they work in or serve and can quickly respond to changes in their communities.

As the community prospers, so does the business, and the links between the two become stronger.

Opportunities to Get Started

Challenge	Field Leaders	Frontline Leaders	Advisors
Industry Consolidation	Explore industry partnerships or consolidation as long-term goals.	Explore alternative sources of training and technology.	Keep updating your skills to match your firm's evolving business priorities.
Lower-Cost Middle-Market Products	Diversify your client base to include multiple markets to help stabilize revenues and profits.	Explore new avenues and business models for the middle market with your advisors.	Explore efficient ways to sell in the middle market.
Creating Shared Value	Create a culture of shared value with the community among your key leaders.	Broaden training programs to cover key issues in your community.	Identify the most important groups inside your community and partner with them.

Questions to Consider

One-Minute Debrief

1. Which business model trends and opportunities are the most interesting for your firm's future?

2. Which cause you concern and why?

3. What is the most important thing you want to take away from this chapter?

Strategy Questions

1. To what extent is your firm a potential beneficiary or a potential loser in future industry consolidation — or in product manufacturers distancing themselves from their distributors?

2. To what extent will the clients you serve or the products you offer be affected by significant increases in regulations or taxes? How will you adjust your business model to accommodate such changes?

3. What relationships do you have in the local community, or in specific niche communities, that can form the basis for building shared value for your firm?

First Step

What *one thing* will you do this year to increase or enhance the professional services your firm provides to an underserved community in your local market?

Additional copies of this worksheet can be found at gamafoundation.org.

Drill Down on Trends

Consolidation in the Industry

The investments of private equity into BDs are part of a larger trend of consolidation and competition. The Compliance Department Inc., an industry consultant, forecasts that the BD universe will shrink from 4,555 firms today to 4,000 by 2015. Already the number of BD firms has declined to 88 percent of 2005 levels.[90] Profit margins have been down at many firms, and in response, many are scaling up to reduce overhead costs per advisor. Multiline agencies face additional challenges, which include increasing online sales and a generally constrained purchasing environment in the middle market for both group and individual insurance.

Large Players Exiting Annuities

Some of the largest names in the annuity business, such as the Hartford, have recently cut back on annuity sales or left the business altogether. An extremely low interest rate environment has pressured margins on existing books of business and forced many companies to raise reserves in a very capital constrained environment. Hardest hit have been suppliers of variable rate annuities with principal protection guarantees. During the boom years competition between insurance companies provided overgenerous guarantees, and the dynamic hedging strategies designed to protect insurers have been struggling in a volatile market.[91]

Consumers Looking for Security

The decision of many large providers to reduce their life insurance exposure is happening at the same time that permanent life insurance is becoming more attractive as an asset class for investors. The same trends that are hurting profitability for insurers — extremely high levels of market volatility and record low yields on treasuries — have many consumers looking for steady and predictable tax-free returns.[92] The trends are driving sales toward permanent life insurance policies such as whole life at the expense of universal and term life insurance (although variable universal life, which is purchased mainly by corporations for high-value employees, saw phenomenal growth in 2010).[93]

Demographic Trends Favor Lifetime Income Annuities, Long-Term Care, and Longevity Insurance

The case for lifetime income annuities, long-term care, and longevity insurance makes excellent economic sense for most consumers. People are living longer and racking up large bills for end-of-life care, which puts both themselves and their loved ones at increased risk.[94] Most are also losing access to the defined-benefit pensions provided by their employers that provided a cushion against these risks. A study by the consultancy Towers Watson showed that the number of Fortune 100 companies, the largest and most financially stable companies in the country, offering new hires a traditional

defined-benefit plan dropped from 67 in 1998 to 13 in 2011.[95] In addition, pension trust funds in both the public and private sector are underfunded. In this environment, the steady, guaranteed income of a lifetime income annuity looks extremely attractive, especially considering the economic research showing that most individual investors do not take advantage of 401(k) matching funds and generally underperform the market.

Tax Pressures

The fiscal challenge of fixing long-running problems with the U.S. national debt and recurring budget shortfalls will continue to generate uncertainty in financial and consumer markets. So far, markets have been sanguine about all the red ink and have kept borrowing costs low by investing heavily in treasuries. However, as seen in Europe in recent years, market sentiment can swing quickly, causing widespread financial turmoil. In 2011, the federal government ran into the red equal to roughly $42,054 per household, according to some accounting estimates. Everything, including preferential tax treatment for retirement products and life insurance, could be on the negotiating table as Congress searches for the right levers to get and keep the U.S. government on a more responsible financial course. Advisors helping clients manage their financial futures must be ready to respond with the right information as well as new strategies and products to meet their goals.

NOTES

[85] According to Morningstar data, roughly 62 percent of revenues at insurance-owned broker-dealers come from variable annuity sales and 90 percent of these sales are of proprietary products.

Diana Britton, "Breaking Out: A New Era in Insurance," *Wealth Management.com* (June 1, 2012), http://wealthmanagement.com/insurance/breaking-out-new-era-insurance.

[86] Broker-dealers with a heavy emphasis on securities are facing even more scrutiny than other firms at a time when low interest rates are hurting easier sources of revenue such as money market fees.

[87] Private equity firms are also looking for an excellent five-year return on their investments. They are consolidating struggling firms, integrating back-office functions, and competing for the best advisors by offering better management and technology.

Lisa Shidler, "Why Exactly Private Equity Firms Are Dumping Money Into IBDs at a Time When Many Are Going Bust," *RIABiz* (Sept. 2, 2011), http://www.riabiz.com/a/8143001.

[88] Michael E. Porter and Mark R. Kramer, "Creating Shared Value," *Harvard Business Review* (January 2011), http://hbr.org/2011/01/the-big-idea-creating-shared-value.

[89] Ibid.

[90] Diana Britton, "The Big Shrink: Independent Broker Dealer Report Card 2012," *WealthManagement.com* (Feb. 1, 2012), http://wealthmanagement.com/institutions/big-shrink-independent-broker-dealer-report-card-2012.

[91] Erik Holm, Leslie Scism, and Gina Chona, "Hartford Says Goodbye to Annuities," *The Wall Street Journal* (March 21, 2012), http://online.wsj.com/article/SB10001424052702304636404577294972124322432.html.

[92] Paul Essner, "Voices: Paul Essner, On Life Insurance as an Asset Class," *The Wall Street Journal* (June 20, 2012), http://blogs.wsj.com.

[93] Matthew Sturdevant, "Life Insurance Shows Growth in Fourth Quarter of 2011," *The Hartford Courant* (March 2, 2012), http://articles.courant.com.

[94] Michael J. Minton, "The Future of Long Term Care Planning," *LifeHealth Pro* (June 25, 2012), http://www.lifehealthpro.com.

[95] Brendan McFarland, "Prevalence of Retirement Plan Types in the Fortune 100 in 2011," *Towers-Watson* (July 21, 2011), http://www.towerswatson.com/united-states/newsletters/insider/5010.

Game Changers Can Challenge Future Assumptions

The Firm of the Future provides an overview of significant business and cultural drivers that are expected to affect the insurance and financial services firm over the next few years.

Yet not every significant change is a trend that can be monitored and predicted. An occasional low-probability, high-impact event can have a very large effect on your firm or even the entire economy. Examples of these kinds of events include the Lehman Brothers collapse and Hurricane Katrina.

Often it is not the event itself that causes the most damage. Instead, it may be the feed-on effects caused by organizations that are ill-prepared to deal with these game changers.

Below are four potential game changers that could have a profound and widespread impact on the insurance and financial services industry. These events may never happen, but if they did, they would be high-impact events.

Social Insurance

Widespread dissatisfaction with conventional insurance products and distrust of financial institutions spark the adoption of crowd-sourced insurance. The process starts with a number of online guilds providing virtual item insurance and gradually spreads to other products. The guilds use many of the same informational and marketing advantages that helped fraternal groups spark the boom in life insurance more than a century ago. The process soon spreads as innovators create crowd-sourced websites for pooling risk for people with similar interests.

What other surprising product and business model innovations might be ahead?

De-Globalization of Finance

Over the next several years, the global ties that brought together the global financial system unravel. The European Union breaks up as France and Germany are unable to agree on the terms of further integration. Global deleveraging of finance continues and leads to constrained capital conditions and increased risk aversion among investors. Protectionism sweeps across the globe, and the United States begins breaking up major financial institutions in an effort to reform the financial system and rebuild consumer confidence.

What twists and turns might alter the economy and rock the foundation of the insurance and financial services industry?

Catastrophic Technology Failure

Malfunctions of computer systems cause widespread data corruption. The first signs of a problem are spotted by major financial institutions as their automated trading systems cause wild fluctuations leading to a

multi-day stock market closure. The virus started as an isolated attack by a rogue state, but quickly spread because of an error in the virus's code. By the time the problem is discovered, the virus has already spread to hundreds of thousands of financial institutions and clients that did business with the bank. Hundreds of billions of dollars are lost as the financial system seizes up and financial records are hopelessly corrupted. Worse still is the prospect of a decade worth of lawsuits as clients and firms attempt to sort out the mess.

What are the risks to your systems, which are becoming so important to your business?

Go-Go Economy

Fiscal and market reforms finally stem the global financial crisis of 2007–2012 and set the stage for a prolonged period of global growth. The two U.S. political parties restructure taxes and entitlements to restore the fortunes of the middle class and incentivize the wealthy to invest in new economic opportunities. Globally, the European Union pulls together with an agenda for greater fiscal and monetary integration, while China stokes internal consumer demand and growth through market reforms. Businesses and consumers regain their confidence and begin investing in industries with the potential to propel global growth and stability for the next 20 years.

What are your expectations about the future, and have you considered both extraordinary successes and frightening failures as possibilities?

The list of low-probability, high-impact events can never be complete. The world will always hold surprises. But you should make it a practice to keep your own running list of potential game changers as a way to keep your expectations flexible and your mind open to unforeseen challenges and opportunities.

Action Items

In this second study of *Firm 2020 — The Firm of the Future* — the six major change drivers demonstrate how rapidly the world of business can shift and the dramatic impact that each shift can have.

If your firm is purpose centered rather than comfort centered, you have a distinct advantage over many of your competitors. That purpose will keep your eyes focused on your client market and the value your firm provides.

From that vantage point, you will be in the best position to evaluate opportunities and investments in *people* (consumers and advisors), *capabilities* (technology and security), and business *strategies* (data analysis and business models).

Take a moment now to synthesize your key takeaways from Study Two. Then use the following table to capture your best ideas to share with your team.

Snapshot of Ideas

Briefly capture your best ideas and opportunities here. Remember to keep it simple. Once a first step is taken, subsequent steps are much easier.

Change Driver	Best Opportunities	Value to Be Provided	First Steps	Potential Partners
Workforce Development and Talent Retention in a Dynamic Workplace				
The Shifting Needs of Consumers and Advisors				
Technologies for a Powerful Sales and Service Force				
Managing Privacy and Security in the Networked Age				
Advanced Data Analytics Empower Advisors and Consumers				
Shifting Business Models Shake Up the Industry				

Additional copies of this worksheet can be found at gamafoundation.org.

Moving Forward

Building the firm of the future begins with a few wise steps.

Lasting change is a process that requires hard work and patience. No firm can make all the changes needed to meet future challenges at once. *Firm 2020* is designed to help you recognize opportunities and initiate meaningful changes by focusing on the markets and change drivers most likely to affect your future.

A mature industry is a challenged industry. Add an uncertain business environment and a consumer base that questions the industry's value and trustworthiness, and you see that remaining with the status quo is not a compelling business plan.

In *Firm 2020*, you have been exposed to a great many insights, trends, and forecasts about the future. But most importantly, you've been asked to consider how you can use this information to make your firm stronger and more successful, beginning today.

This is not an idle exercise but a critical one. Not all of the forecasts in this book will come to fruition, of course, but many will. By building the *Firm 2020 process* into your planning sessions and team meetings, you will be in a position to choose your direction and business opportunities proactively in an unstable business environment. That is the best way to get ahead of your competition and stay ahead.

Don't stop with your team. Your colleagues in this industry are on the same journey. Talk to them, explore your insights about the future together, and share your strategic choices. If you are not competitors and can be collaborators, this is a way to test your thinking and strengthen each other's strategies. You may even find that you have clients and business partners who share your interest in how these changes and opportunities may affect the future of your business.

Never stop learning about the future and talking about its implications with your team. The two studies that comprise *Firm 2020* try to take a long view, but conditions do change. Monitor new trends and issues and keep your checklist for the future up-to-date and forward focused.

The environment is challenging, but the opportunities are real if yours is a purpose-centered firm. It's tough out there, and that fact will be enough to drive out the uncommitted. Set your sights and get going; 2020 is just around the corner.

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