

is the price right?

June 2010

Graham Bentley looks at consumer behaviour towards pricing and explains why flexibility in your investment proposition can help to ensure clients understand what they are paying for.



“The price of anything is the amount of life you exchange for it.”

Henry David Thoreau

Delivering great service post-RDR means offering the flexibility to fit with your clients' needs, not the needs of your business. But that doesn't mean your focus shouldn't be on profitability; of course it should. As David Burns's article attests, segmenting your client services within a fee-based model can provide the basis for a profitable business model which satisfies both TCF and RDR requirements.

While the move to a fee-based model places greater emphasis on client segmentation, it may also present some unexpected changes in the mindset of the consumer, ie your client. This change won't necessarily follow logic, but is likely to mean the client will pay greater attention to the services you provide in return for parting with their hard-earned cash. This is particularly significant in an industry faced with convincing an audience – one that for years has been taught that advice is free – that they now have to pay for it.

price psychology

So, how does a fee (or price) affect consumer behaviour? Take for example fuel prices in the US. Not too long ago American consumers were contentedly driving their gas guzzlers as prices steadily increased over time, from \$2.50 a gallon, to \$2.90 to \$3.30 and onwards. But it was when prices hit \$4 that consumer

behaviour changed radically in the form of a switch to smaller cars and hybrids.

Although the price had been steadily rising over time, it took the nice round figure of \$4 to trigger a reaction en masse. And later when the price had fallen, the trend to smaller vehicles continued.

Why does this happen? Well, it appears that people fixate on price 'anchors' to prompt a change in behaviour. Supermarkets recognise this; to 'encourage' shoppers to buy a more expensive item, they may quote 'was £10, now £8.50'. So £8.50 is deemed cheap *by comparison*. Another way of doing this is to place a more expensive version of the same item next to the one you want to sell.

We do seem to need these anchors, to the point where any comparator will do. In a famous experiment in Behavioural Finance, two psychologists asked subjects to estimate the percentage of UN member states that were African nations. The researchers spun a wheel of fortune, with numbers ranging from 1 to 100, in the presence of the subjects. Subjects were first asked to determine if the random value from the wheel was too high or too low an estimate, and then to actually estimate the percentage of African membership at the UN. The random, arbitrary numbers had an effect on subject responses – those who received 10 as the value, guessed 25% African membership, while those receiving 65 guessed 45%.

Your clients, therefore, are likely to create a perception of the services you provide and

decide whether the fee for those services represents value for money within the context of their own spending experience, even if they have no experience of financial services. Fortunately, successful fee-based advisers are adept at explaining the benefits of their services and what they mean to the client's current position. This brings us back to the importance of segmentation.

menu of services

We recently conducted research* with NMG which shows that many fee-based advisers are choosing to offer a menu of services. This in itself leads to segmentation, with each client paying only for the services they need. Key to that offering is an understanding of how to allocate your time to the different client requirements within the service level requested by the client.

Typically, the structure of investment services offered will differ according to client requirements to ensure the solutions provided are appropriate for a particular client or client segment. While client requirements can be wide and varied, NMG identified three broad sets of typical client requirements on a 100 point scale (see table).

The research also gave a picture of how advisers are adopting client-focused investment services to ensure time is spent on the agreed service areas. Some client segments will require the adviser to research and select funds themselves, but increasingly advisers are looking to focus



more on their client's financial planning needs and outsource elements of their investment service. While there are a number of different approaches employed, the research identified four broad investment strategies:

- Bespoke portfolio of funds
- Pre-defined portfolios selected by the adviser
- Asset-allocated portfolios using researched funds
- Fully outsourced solutions

In terms of the choice Skandia offers advisers, our existing Self Select fund range of 1,000 funds meets the demand for bespoke and pre-defined portfolios, while our Spectrum range of risk-rated funds meets the demand for fully outsourced solutions. And this month we are introducing the Skandia Signature funds to meet the growing demand from financial advisers for different approaches to portfolio construction and management.

The Signature funds meet the demand for asset-allocated portfolios and enable advisers to retain control over their client's asset allocation, while utilising the huge resources and expertise of Skandia Investment Group's (SIG) investment research team to identify the best fund managers in each asset class. SIG monitors the managers on a constant basis and replaces those that fail to perform.

NMG client service structures

How is the adviser's time/added value distributed across different elements of the advice process	Client A		Client B		Client C	
	Initial advice process	Ongoing advice process	Initial advice process	Ongoing advice process	Initial advice process	Ongoing advice process
Goal planning	25	10	50	20	40	25
Specialist advice (eg tax planning)	15	25	5	5	15	15
Wrapper selection	10	0	20	20	15	20
Investment research	35	45	5	5	20	15
Reviewing/reporting	15	20	20	50	10	5
	100	100	100	100	100	80

Of course, there is no definitive solution when it comes to creating an investment advice process. It will depend on what you are trying to achieve, what you can afford to do internally and where you want to focus your resources. Regular readers of this column will know the importance of a robust process in terms of your approach to strategic asset allocation. What the Signature range offers is another solution for the fund selection process – helping you to identify suitable funds to match the various asset classes you have selected, in the appropriate amounts. Rather than a way of selecting funds that relies on past performance figures or fund ratings agencies, it offers access to SIG's 40+ research team and their '4P' selection methodology to do the work for you.

The choice we give you with Spectrum, Signature and Self Select aims to offer flexibility in how you incorporate the different elements of our investment proposition into your own services and pricing. That way you can spend the time on the services that add value for your client. ●

*NMG conducted in-depth interviews with 14 financial adviser firms who have adapted or are actively adapting their businesses in line with the requirements of the Retail Distribution Review.

www.skandia.co.uk

Calls may be monitored and recorded for training purposes and to avoid misunderstandings.

Skandia provides you with access to its investment platform, known as Skandia Investment Solutions. Within this platform you can open an ISA and Collective Investment Account provided by Skandia MultiFUNDS Limited, a Collective Retirement Account and Collective Investment Bond provided by Skandia MultiFUNDS Assurance Limited and an Offshore Collective Investment Bond, distributed by Skandia MultiFUNDS Limited but provided by Old Mutual International (Guernsey) Limited.

Skandia Life Assurance Company Limited, Skandia MultiFUNDS Limited and Skandia MultiFUNDS Assurance Limited are registered in England & Wales under numbers 1363932, 1680071 and 4163431 respectively. Registered Office at Skandia House, Portland Terrace, Southampton SO14 7EJ, United Kingdom.

All companies are authorised and regulated by the Financial Services Authority with FSA register numbers 110462, 165359 and 207977. VAT number for all above companies is 386 1301 59.

Skandia Investment Group is a trading name of Skandia Investment Management Limited. Skandia Investment Management Limited is registered in England & Wales under number 4227837. Registered Office at Skandia House, Portland Terrace, Southampton SO14 7EJ, United Kingdom. Authorised and regulated by the Financial Services Authority with FSA register number 208543, VAT number 386 1301 59.

Old Mutual International (Guernsey) Limited is regulated by the Guernsey Financial Services Commission and is licensed to write long-term business under the Insurance Business (Bailiwick of Guernsey) Law 2002. Registered number 2424. Registered Office at The Beehive, PO Box 121, Collings Road, St Peter Port, Guernsey GY1 3HE, Channel Islands.