How platforms are evolving

Moore's law is named for Gordon Moore, a co-founder of Intel. In the mid 1960s he predicted that transistor computing power would double every 24 months. This has meant that the temperature-controlled room full of IBM valves of yesteryear has very rapidly turned into a device we can carry around and use not simply for data processing but to watch films, retrieve music and talk to our friends.

Fund platforms are also evolving at great speed, but since they are software rather than hardware the difference is not always so apparent. However, they are evolving faster than many realize and they are starting to redefine the structure of the financial services market.

In 2000, two entirely different types of platform emerged to meet two unrelated needs at opposite ends of the adviser market. Early "fund supermarkets" were initially simply used to set up ISA products that contained funds from a wide number of managers. They were built around the demands of commission based advisers and made no additional charge for use.

At the same time, "wraps" appeared, which were essentially web-based portfolio administration systems which met the needs of fee-based discretionary managers.

Initially there was some confusion about which service did what, but the distinction outlined above has come to be generally understood. However, the picture is becoming muddied as competitors enrich and upgrade their functionality.

First, we have seen various models launched - or at least trailed - by insurance companies. A cynic might be describe some of these principally as attempts to sell the company's life and pension products on-line, allied to web-based fund administration. Or to increase controls and reduce costs for a tied sales force.

Second, the major "fund supermarkets" have announced that they will be launching fee-based services in the new year. To do this effectively, they will have to introduce cash management products and the other elements of what has so far been the preserve of "wrap providers". So the old definition will no longer work.

How will advisers decide which provider to use in this new circumstance? We believe this will be a function of 3 elements – price, service and, most importantly, choice.

Price might seem simple. However, currently price comparison in the wrap space is difficult because discretionary managers typically have a whole menu of charges for each element of their service. Product producers have historically favoured complex charging models for this very reason. However, the FSA is pressing on the issue of disclosure and is using MIFID to demand that the whole of the value chain is clarified so all the various financial arrangements inherent in agreements between insurers, fund managers and advisers are transparent.

However, the FSA must be well aware that rebates, subsidies and “marketing support” have been a feature of UK financial services since long before platforms arrived and we can anticipate that TCF will start to bite across the industry. So transparency and simplicity are, the FSA hopes, going to be the end result. And if this is the case, then prices will be under pressure across the board.

Service is the next key element. This is partly what we may term “positive service” – how helpful the person you get on the phone turns out to be. However, even more important is “negative service” – not making a mess of things. Platforms, whatever the financial model, are essentially just internet based administrators. You never think about your water company until you turn on the tap and nothing comes out.

It is important to note that if prices are under pressure then margins will fall. The only way to cope in the long run will therefore be to increase volumes. But the greater the volume of transactions, the worse the effects of any glitch will be. Successful providers will have to be able to cope with a massive scale of client records and transactions. At present, 3 providers, Cofunds, Fidelity FundsNetwork and Skandia/Selestia have, we believe about 75% or more of the total platform assets. High volumes and low margins will mean that only a handful of competitors can succeed in the long run.

The final element in our equation is choice. This is perhaps the most significant area of future change. Platforms started doing a few things like providing open architecture ISAs more effectively than they could be done on paper with a range of product providers. In the first year or two, choice meant having more funds on the platform than anyone else. Now all platforms carry links of one sort or another to more funds than anyone could rationally want.

Then choice meant having tax wraps other than an ISA available. This was offered in two possible ways. The integrated form meant deep system links between a life and pensions company and a platform to allow for a seamless process from on-line quotes, through to fund choice and portfolio analysis across all the clients assets regardless of tax wraps. The other form is just a price link which allows for portfolio valuations but not a lot more.

Now we are starting to see platforms providing a menu of business support options which an adviser can use flexibly to support their individual corporate models. Some of this is in the area of management information which allow IFAs to interrogate their business data in a flexible way through Excel tools to help understand client profitability, branch activity and to keep an eye on compliance risk. Some of it lies in the way a dynamic platform can integrate with a range of industry software providers such as 1st Software, Intelliflo and others so that an advsisory firm can get a unified picture of on and off platform business through whichever supplier they choose to use.

We have already mentioned that a firm will be able to use fee based and commission based or execution only models from a single platform. We are also starting to see independent platforms starting to provide access in a meaningful way to more than one life and pension provider. Moreover, major distributors are now working with platforms to set up white label platforms where they are involved in defining functionality and choice.

It is critical that advisers realize that at this point they are carrying out a major outsourcing exercise and will be dependent on the continued strength and capability of their platform partner. Equally, platforms must understand the full weight of their responsibilities in providing long-term support to the adviser. Like the marriage ceremony says, these relationships should not be entered into "lightly or inadvisably".

The end result of all these rapidly developing options is that, for successful IFAs, the market is moving from product push to demand pull. It is the financial services equivalent of building playlists on your iPod rather than buying a CD.

The challenge for life and pensions companies is to consider that if simple and transparent products will be the result of the FSA's pressure on the one hand and of the optimal use of the technology on the other, how they will be able to differentiate in the world of open architecture that IFAs now demand. They will equally face a dilemma if their platform is not independent and is limited to ties only to the owner's products.

So IFA firms have been on a journey. It began with a flirtation, trying out the various platforms for a bit of business. Then they started to go steady deciding on one main provider for new business to simplify and streamline administration. After that, they got engaged, shifting their old book of business on to their preferred platform and using that as an outsource solution for client records. Now they are starting to walk up the aisle and getting married. This means fully integrating their business, using all the tools for analysis, reconciliation and client communication and defining in conjunction with the platform the nature of the choices it feels its advisers should offer.

Historically financial services companies launched the products they wanted to sell. The evolution of platforms will finish with advisers defining the funds and tax wraps they want to use to build the business they want to have.

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Notes To Editors

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