Advice Gap Analysis: Report to FCA

5 December 2014

TOWERS WATSON

Contents

Executive summary: Introduction

- The purpose of this document is to set out the results of analysis carried out by Towers Watson into the possible existence and size of an advice gap in the UK retail investments market.

- This analysis was commissioned by the FCA as part of its post-implementation review (PIR) of the Retail Distribution Review (RDR). In this PIR the FCA is seeking to explore, among other issues, the impact of the RDR on financial adviser capacity and whether and if so how, changes in adviser capacity arising from the RDR may have resulted in or contributed to a so-called 'advice gap'.

- The FCA engaged Towers Watson to assist the FCA in estimating the extent of the following three elements: (1) demand for retail investment financial advice, (2) the amount of adviser capacity required to meet that demand and, (3) possible gaps in advice provision (the advice gap) in the UK retail investments market.

Executive summary: Scope limitations

- The scope of our work, as agreed with the FCA, was limited in three important respects as follows:

  - Our brief was to develop an estimate of one year's demand and supply as of early 2014 based on recent market data. Our brief did not include developing estimates at other dates, trend analysis over time or any prospective analysis of the future evolution of supply and demand for advice. The modelling therefore did not take account of any potential future build up of demand for ongoing advice, which might be expected to increase the absorption of adviser capacity over time. Nor did it consider any increase in demand which might arise from developments such as the increased choice and flexibility in the retirement income market following the 2014 Budget reforms. Over time, such factors might be expected to increase demand for financial advice and guidance. In theory, this might put existing advisory capacity under more pressure, unless more efficient operating models can be developed or more advisers brought into the market. However, pension reforms are not connected with the RDR and therefore have been excluded from advice analysis relating to the RDR.

  - We modelled demand for "full" regulated financial advice – using separate assumptions about "transactional" advice (e.g. how to invest a given sum of money at a point in time), and "holistic" advice (relationship-based financial planning). We did not model demand for, and supply of, services relating to "simplified" or "streamlined" advice or guidance services which are either available today or which might become available in the future.

  - The scope did not include primary research into important drivers of demand and supply. These drivers could include the length of advisory processes, whether advisers focus on specific consumer segments and how any such focus affects adviser productivity and capacity utilisation, the amount of adviser time available to deliver advice, and consumer propensity to seek advice and to utilise ongoing advice services. In the absence of such primary research we therefore relied to a high degree on publicly available data, together with our insights and experience of the operation of the advice market. Public data is limited and generally predates the implementation of the RDR and therefore may not be reflective of changes in adviser business models which have occurred following RDR implementation. A high degree of estimation and judgement was therefore required to assess current practice and variations in different parts of the advice market. Generally, in applying such judgements, we sought to adopt a conservative approach to assumption-setting, such that if anything, advice demand is likely to be overstated and the likelihood and size of any advice gap increased.

- Attention is drawn to the Reliances and Limitations section later in this report.

Executive summary: Approach (1)

- **Total demand** for advice in the current year (assumed to be 2014) is the sum of modelled initial advice demand in that year and modelled ongoing advice demand which follows from initial advice cycles in previous years (referred to in this document as "Legacy Ongoing Advice"). Advice demand is expressed as the number of initial and legacy ongoing advice transactions. The capacity consumption implications of these transactions are arrived at by assuming standard advice process times for transactional or holistic advice, applied to the number of advice transactions modelled as described below.

  - **Demand for initial advice** in the 12 month period is modelled by estimating the probability of consumers seeking initial advice and multiplying by the number of people. A segmental approach is taken (using data from the FCA 'Consumer Spotlight' segmentation model), thus enabling different probabilities to be assigned to different customer segments. The segmental probabilities of seeking advice are arrived at by judgementally scoring segment characteristics judged likely to be consistent with higher or lower usage of (or demand for) initial advice and using these judgemental scores to place the segments on a hypothesised probability distribution of advice seeking for the market as a whole.

  - **Demand for legacy ongoing advice** is calculated by estimating the probability of the current holders of investment products having (a) sought initial advice in any of the prior ten years (b) opted for ongoing advice at the time and then (c) continued to use ongoing advice until the current period. The approach is similar to that used for initial advice in that it is based upon judgemental scoring of segment characteristics in order to place the segments within an estimated probability range for taking up ongoing advice to which other assumptions regarding historic advice seeking and lapsation are added. Given that the concept of ongoing advice did not exist as clearly pre-RDR as it now does, judgement was used to assess ongoing advice usage based on historical product holdings.

  - **The adviser capacity implications of the demand for advice** are calculated by multiplying the modelled number of initial and ongoing advice cases by the assumed number of adviser hours per case. This is based on assumptions as to the proportion of initial and ongoing advice demanded by each segment and by an assumed mix of "holistic" advice (higher capacity absorption) or "transactional" advice (lower capacity absorption). Assumptions are then made as to the number of adviser hours available for delivering investment advice per adviser. Dividing the total number of advice hours required by the number of hours available for advice per adviser yields the number of advisers required.

Executive summary: Approach (2)

- **Supply of advice** is expressed as the estimated number of financial advisers available to deliver advice on an individual basis (as opposed to a full time equivalent basis).
- The demand for and supply of advice, both expressed in adviser numbers, can be compared and any **gap** (surplus or shortfall) calculated.

Executive summary: Data and key assumptions

- As noted on the previous pages, in applying the approach described, considerable judgement and approximation were required, in particular in relation to:
  - The allocation of judgemental scores to segmental characteristics deemed likely to be consistent with higher advice demand.
  - The estimation of the number of advised retail investment purchases in the market (especially in relation to the average case size of intermediated investment sales reported by the IMA).
  - The estimation of the proportion of advice cases that consume advice capacity but do not result in a retail investment product sale.
  - The estimation of the highest and lowest probabilities to seek advice either side of the observed advised retail investment product purchase rate once inflated for advice not resulting in a product sale.
  - The scaling of the number of married/cohabiting individuals in each customer segment to take account of the financial advice being taken at a household level.
  - The historic conversion rate of initial advice to ongoing advice in previous years and the historic annual lapse rate of such ongoing advice.
  - The adviser hours required on average to effect holistic and transactional advice cycles.
  - The hours available per adviser for the purposes of delivering advice.
  - The proportion of advisers who work less than full time and the proportion of full time hours worked by those individuals.

Executive summary: Results (1)

No advice gap resulting from an overall shortage of advisers

- The results do not point to an obvious or substantial gap in advisory provision, when considering demand for “full” regulated financial advice. The central view of our analysis indicates demand for around 25,000 individual advisers, compared with estimates of around 30,000 financial advisers currently active in the market.

- These results therefore indicate excess capacity (or a negative advice gap) based on the productivity and time allocation assumptions used, of around 17% of the adviser base, or about 5,000 advisers. Over time, any such excess capacity may be absorbed if demand for ongoing advice increases and if demand for pre-, at- and in-retirement financial planning increases.

However, adviser capacity may not be optimally aligned at customer segment level

- A different picture is likely to emerge in considering individual consumer segments, as opposed to the total market. Although it has been possible to estimate demand by consumer segment, it has not been possible to analyse supply by segment. This is because data on the customer segment focus and other key business model attributes (eg what types of consumer specific firms sell to) is not available and cannot be surmised from other data sources. However, anecdotal evidence of developments in the market post RDR suggests that advice capacity serving less affluent segments is likely to have reduced and there may therefore be reduced provision. These anecdotally-supported developments include:

    - Advisers focussing on customer segments that are most likely to be able to afford such an offering, or where the benefits of taking advice are most cost-effective.
    - The increased adoption of holistic financial planning models that are likely to be more capacity-intensive.
    - New large-scale services focussed on the needs of less affluent customers are yet to develop to a significant extent.

Executive summary: Results (2)

There may therefore be a gap in the provision other forms of financial advice or guidance to less affluent segments

- A further consideration is therefore whether there is a gap in the nature of the advice or guidance available to less affluent consumers (or consumers generally who do not seek or require full financial advice). This is a potential concern in segments where modelled demand levels for holistic and transactional advice are substantially lower or close to zero. Segments with a lower likelihood of seeking advice (segments 6, 7 and 8 as described in the following section) are at potentially higher risk of such mis-matches given their generally lower demand levels and lower wealth stock and income. Whilst not modelled as part of this work, these segments may potentially display higher propensities to seek and utilise other forms of guidance not currently offered or widely available in the market.

Approach

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Overview of modelling approach

Consumer segmentation	Advice demand		Advice capacity required		- Actual capacity available	= Advice "gap"
Total number of customers per segment *Uses the FCA 'Consumer Spotlight' segmentation model to provide the number of individuals in each segment and data on the characteristics of those segments.*	**Initial advice demand in current year:** *Estimate probability range for seeking initial advice for the market as a whole (ie highest, lowest and average).* *Use judgemental scoring of segment characteristics to place segments in the probability range.* *Multiply derived probability for each segment by number in the segment to yield modelled number of expected initial advice cases.*	+ **Ongoing advice based on activity in previous years**: *Estimate probability range for taking up ongoing advice for market as a whole.* *Use judgemental segment characteristic scores to place segments in the probability range.* *Calculate segmental probabilities of having taken initial advice in any of the previous 10 years, taken up ongoing advice, and not lapsed usage of ongoing advice.* *Apply resulting probability to current number of investment owners in each segment to yield ongoing advice cases.*	**Advice capacity required to meet initial advice demand** *Estimate the proportion of initial advice cases that consume higher and lower adviser capacity (reflecting holistic and transactional advice respectively).* *Hypothesise the number of adviser hours required to service each type.* *Multiply the number of 'high' and 'low' cases by respective hours required to give total advice hours required.* *Divide total hours required by hours available per adviser to give the number of advisers required to service initial advice demand.*	+ **Advice capacity required to meet legacy ongoing advice demand** *Estimate the proportion of ongoing advice cases that consume high and low adviser capacity.* *Hypothesise the number of adviser hours required to service a high case and a low case.* *Multiply the number of 'high' and 'low' cases by respective hours required to give total advice hours required.* *Divide total hours required by hours available per adviser to give number of advisers required to service legacy ongoing advice demand.*	Approximate total number of retail investment advisers in the market	Surplus or shortage of advisers in the market to meet modelled investment advice demand.
Page 12-13	*Page 14-17*	*Pages 18-21*	*Pages 22-27*	*Pages 28-31*	*Page 32*	*Page 39*

The demand modelling is underpinned by the 'FCA Consumer Spotlight' segmentation model using the ten segments and their underlying detail

- Based on data supplied by the FCA and subsequent enhanced detail tables, a master index was created by collating approximately 100 data types common to all of the segments. Three of the data points (percentage of the total population, the number in the segment and a summary description) for all ten segments are outlined for illustrative purposes below:

Segment Number	1	2	3	4	5	6	7	8	9	10
Segment Name	Retired with resources	Retired on a budget	Affluent and ambitious	Mature and savvy	Living for now	Striving and supporting	Starting out	Hard pressed	Stretched but resourceful	Busy achievers
% of population	14%	7%	11%	7%	14%	8%	9%	10%	14%	7%
Seg count (million)	6.8	3.6	5.5	3.3	6.7	4.0	4.4	4.7	6.9	3.4
Summary description	Retired people, living comfortably on income from pensions and savings, very rarely going overdrawn or needing to take on debt. The majority have the resources to deal with an income or expenses shock. Some use expert financial advice but they are also well informed. An optimistic and confident group	Retired elderly people, living on low incomes, often alone. Organised and careful with money, they avoid debt and tend to be very loyal to a small number of financial service providers. Many with access challenges due to poor health or disabilities, they are likely to rely on cash and cheques to make payments.	An affluent working age segment more likely to be men, many are married with children living at home. Financially secure, confident and optimistic, they are likely to own a large number of financial products, including savings and mainstream credit. They enjoy shopping around for the best deals, often online.	An affluent, middle aged segment, more likely to be male. Working and usually home owners, most have some form of savings and investments. They are very confident money managers and generally find it easy to keep up with their financial commitments. A secure and optimistic group.	A relatively low income group, more often younger and male. The majority work and keep on top of bills but they tend to be less organised with money than others and can be prone to risk taking. Although internet savvy, they lack confidence in financial decision making, often relying on friends or family for advice.	A low income segment, mostly female and the majority with dependent children. Most work but although risk averse, money management is a struggle. They may fall behind on payments, find it difficult to meet an unexpected expense, and rarely switch providers. A busy and pressured group.	A young segment of men and women, with more than half from minority ethnic groups. Despite many having higher level qualifications with some still studying, incomes are relatively low. They may struggle to make ends meet, often relying on credit to get by, but they have a strong support network and are confident and optimistic about the future.	A low income segment of men and women, most are single but many live with dependent children. The majority are out of work and keeping up with bills is a struggle. With low financial confidence and limited access to mainstream credit, this segment finds it hard to make ends meet.	A family segment of men and women with children, almost all in work. Incomes are relatively high and more than half own their home with a mortgage. Although generally able to keep up with bills, credit use is high. Confident but time poor, many would struggle to cope with an income or expense shock.	Mainly female and married, most have children living at home. The majority work and household incomes tend to be high. Most have savings as well as loans and credit cards and although often overdrawn, they are able to keep up with household bills. Very time poor, but optimistic and confident about the future.

Segmental characteristics were assumed to influence demand for initial advice

The master index data for the segments were used to develop a summary list of five characteristics believed to be consistent with higher levels of demand for investment advice. Data types illustrative of the characteristics were therefore grouped together to provide a ‘picture’ of each segment’s characteristics to enable judgemental scoring to be applied. The five characteristics are outlined below:

Characteristic	Description	Basis for inclusion of characteristic	Key underlying segmental data
Life stage	The likely life stage of those in the segment.	Certain life events frequently trigger advice seeking – eg retirement or change of family circumstances.	Age distribution within the segment.
Wealth flow	The likely annual income of those in the segment.	Larger annual income is likely to translate into higher disposable income which, in turn, is more likely to result in choices about where and how to save as well as providing the means to do so.	Household income distribution in each segment and qualitative indications of disposable income.
Wealth stock	The likely level of wealth stock for those in the segment.	A larger stock of wealth is more likely to result in the need to make saving and investment choices and to keep them under review.	Percentage of outright home ownership, percentage incidence of investment/savings total value, having received inheritance, and employment status.
Wealth complexity	The complexity of the wealth of those in the segment.	The more products owned, the more complex the customer’s arrangements are likely to be and hence they are more likely to warrant advice – eg how to withdraw income optimally from a combination of pensions, ISAs and other investments.	Percentage ownership rates for multiple financial product types.
Disposition	Psychological disposition to seek financial advice.	More educated and/or financially informed segments are more likely to understand the benefit of advice and hence seek it.	Education level, internet availability, segment profile description.

Adjustment was also made to the number of married/cohabiting individuals in each customer segment in order to take account of financial advice and planning taking place at a household level.

The characteristics assumed to be consistent with higher initial advice demand were judgementally scored for each segment

- Based on the data underlying the characteristics, each segment was rated on a 1 – 10 scale relative to the other segments for each of the characteristics.

A score of 10	*Data underlying the characteristic implies the strongest relative likelihood of seeking advice*
A score of 1	*Data underlying the characteristic implies the weakest relative likelihood of seeking advice.*

- The characteristic scores for each segment are then summed to give a total characteristic score as illustrated below:

Segment Number	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
Segment Name	Retired with resources	Retired on a budget	Affluent and ambitious	Mature and savvy	Living for now	Striving and supporting	Starting out	Hard pressed	Stretched but resourceful	Busy achievers
Life Stage	10*	7*	8	9	2	7	1	3	8	8
Wealth Flow	2	2	10	9	5	5	4	1	8	10
Wealth Stock	10	5	7	8	5	3	5	1	7	6
Wealth Complexity	10	4	8	9	4	2	1	1	8	8
Disposition	7	6	9	9	3	2	2	1	8	9
Total characteristic score	**39**	**24**	**42**	**44**	**19**	**19**	**13**	**7**	**39**	**41**

* Whilst both segments are ‘retired’ segment 1 has a materially higher proportion of those in/at retirement, whilst segment 2 has a higher proportion of those in later old age.

The distribution of the segment characteristic scores was then calculated above and below the overall average

- The characteristics are assumed to be equally important and are not weighted as no data was available to enable testing of their explanatory power and such testing was outside the scope of our work.

- The characteristic scores for each segment were summed to yield a total score for each segment (see previous page). The average score across all segments was then calculated, together with the dispersal above and below the average figure (ie the difference between the highest scoring segment versus the average, and the difference between the lowest scoring segment and the average):

Average characteristic score	28.7
Upper tail dispersal (ie highest minus average)	15.3
Lower tail dispersal (ie average minus lowest)	21.7

- Where a segment has an above average characteristic score, the model calculates the percentage by which the segmental score is above the average. Similarly, where a segment has a below average score, the model calculates the percentage below the average.

- The percentage above or below the average characteristic score for each segment is used to place that segment within an overall market-level hypothesised probability range for seeking advice. This is done on the basis that the segment with the highest characteristic score will have the highest probability of seeking advice (and by extension, the segment with the lowest characteristic score will have the lowest probability of seeking advice).

  - The segment with the highest characteristic score will therefore have a score of 100% (of the upper tail dispersal)
  - The segment with the lowest characteristic score will therefore have a score of 100% (of the lower tail dispersal)

(See next slide for illustration)

A probability distribution for advice seeking was then hypothesised for the whole market based on observed product purchase rates

- The calculation of characteristic score distributions can be illustrated as follows:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Above average (1=Yes)	1	-	1	1	-	-	-	-	1	1
Distance above average	10.3	-	13.3	15.3	-	-	-	-	10.3	12.3
Distance as % upper dispersal	67%	0%	87%	100%	0%	0%	0%	0%	67%	80%
Below Average (1 = Yes)	-	1	-	-	1	1	1	1	-	-
Distance below average	-	4.7	-	-	9.7	9.7	15.7	21.7	-	-
Distance as % of lower dispersal	0%	22%	0%	0%	45%	45%	72%	100%	0%	0%

- In order to derive the overall market-level probability range for seeking advice, an average ‘advice seeking’ probability is required, together with the upper and lower bounds of the probability range.

- Based upon ABI data for insurer-provided intermediated retail investment sales in 2013, together with IMA data for intermediated gross retail investment sales in 2013, the model estimates the average purchase rate for the population as a whole as being approximately 6.5% (taking into account the judgementally applied scaling factor for married/cohabiting couples where planning may be joint). This 6.5% is therefore based on the number of intermediated retail investment sales divided by the number of individuals in the population as represented by the FCA ‘Consumer Spotlight’ segmentation model.

- An assumption is then made in order to allow for advice cases that do not result in an investment product sale in order to scale up from average ‘purchase rate’ to average ‘advice rate’. This ‘advice to purchase drop out rate’ assumption is set at 30% in the absence of supporting data and is based on judgement regarding the level likely to be reasonable. This therefore yields an average advice rate of 9.5% for the population represented by the FCA ‘Consumer Spotlight’ segmentation model.

- The upper and lower bounds of the probability range for seeking advice either side of the average advice rate are judgementally applied in the absence of supporting data, with 0% as the lower bound and 15% as the higher bound.

Finally, the distribution of the characteristic scores was used to position each segment on the probability distribution for advice seeking

- The penultimate stage of the demand model uses the distribution of the characteristic scores to map the segments onto the range of potential advice seeking probabilities. This is achieved by calculating the percentage of the above or below average dispersal for the characteristic scores (see earlier) and applying the same percentage to the above or below average dispersal for the probability range.

- This yields a calculated segmental probability of seeking initial advice as illustrated below:

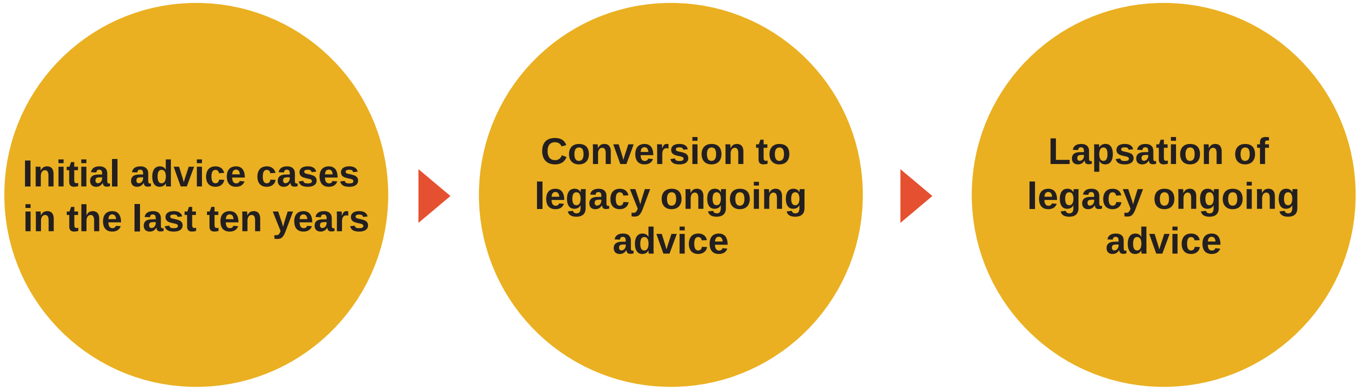
Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Weighted Total Score	39	24	42	44	19	19	13	7	39	41
Distance as % upper dispersal	**67%**	**0%**	**87%**	**100%**	**0%**	**0%**	**0%**	**0%**	**67%**	**80%**
Distance as % of lower dispersal	**0%**	**22%**	**0%**	**0%**	**45%**	**45%**	**72%**	**100%**	**0%**	**0%**

High Probability of Advice seeking	15%		
Average probability of advice seek	9.5%	Dispersal (upper tail)	5.5%
Low probability of advice seeking	0%	Dispersal (lower tail)	9.5%

	1	2	3	4	5	6	7	8	9	10
Probability (upper dispersal)	3.7%	0.0%	4.8%	5.5%	0.0%	0.0%	0.0%	0.0%	3.7%	4.4%
If Zero (for sum below)	1	-	1	1	-	-	-	-	1	1
Probability (lower dispersal)	0.0%	2.1%	0.0%	0.0%	4.3%	4.3%	6.9%	9.5%	0.0%	0.0%
If Zero (for sum below)	-	1	-	-	1	1	1	1	-	-
Probability of advice seeking	13.2%	7.5%	14.3%	15.0%	5.3%	5.3%	2.6%	0.0%	13.2%	13.9%

- The probability of seeking initial advice can then be multiplied by the number of ‘decision units’ in each segment to yield a calculated number of initial advice cases demanded by that segment (see results). Summing the number of initial advice cases across all of the segments therefore yields a total market number of initial advice cases for the 12 month period.

Legacy ongoing advice demand is estimated based on the conversion of historical initial advice to ongoing advice



The number of initial advice cases in the last ten years was estimated using current product holdings data

- Using the data from the master index created from the FCA 'Consumer Spotlight' segmentation model, we can infer the number of individuals in each segment that own investment products.

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Segment count	6,800,000	3,600,000	5,500,000	3,300,000	6,700,000	4,000,000	4,400,000	4,700,000	6,900,000	3,400,000
Investment ownership	52%	22%	46%	42%	19%	17%	16%	5%	43%	38%
Investment ownership count	3,536,000	792,000	2,530,000	1,386,000	1,273,000	680,000	704,000	235,000	2,967,000	1,292,000

- The initial advice modelling yields a percentage likelihood for each segment to seek initial advice in a given year (see earlier)
- The modelling approach therefore builds on these two pieces of information to estimate the probability of having taken initial advice within the last ten years (conditional upon not having taken advice in any of the earlier years). The resulting probability can then be applied to the number of investment holders in each segment to yield an estimate of the number of individuals who are likely to have taken initial advice in the last 10 years.

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Probability of initial advice in any given year	13.2%	7.5%	14.3%	15.0%	5.3%	5.3%	2.6%	0.0%	13.2%	13.9%
Probability of having taken initial advice in the last 10 years	75.7%	53.9%	78.6%	80.3%	41.7%	41.7%	23.4%	0.0%	75.7%	77.7%
Estimated count of initial advice in last 10 years	2,678,227	426,925	1,988,242	1,113,132	531,447	283,884	164,720	-	2,247,257	1,003,543

The probability that those initial advice cases became subject to ongoing advice was estimated

- The conversion rate for historic initial advice to ongoing advice was estimated on the basis of:
  - Allowance for initial advice cases where the product sold did not warrant ongoing advice (judgementally set at 50%)
  - Allowance for ongoing advice being available and offered by the adviser (judgementally set at 60%)
  - Judgemental scoring of segmental characteristics deemed likely to be consistent with higher levels of conversion to ongoing advice (the methodology for scoring these and translating them to a probability of conversion is identical to that used for initial advice).
  - An assumed probability range of converting to ongoing advice:

High take up	60%
Average take up	40%
Low take up	0%

- The approach to arriving at the probability of converting initial advice into ongoing advice for each segment is the same, in principle, as that outlined for initial advice (ie using the dispersal of each segment's characteristic scores to place the segments in a hypothesised probability range) and yields probabilities as follows:

Segment Number Segment Name	**1** Retired with resources	**2** Retired on a budget	**3** Affluent and ambitious	**4** Mature and savvy	**5** Living for now	**6** Striving and supporting	**7** Starting out	**8** Hard pressed	**9** Stretched but resourceful	**10** Busy achievers
Probability of having taken ongoing advice as a result of initial advice taken in the last 10 years.	60%	40%	60%	52%	14%	9%	6%	0%	58%	60%

- This therefore enables the number of people who potentially took initial advice in the last ten years to be scaled down for the likelihood of them having taken ongoing advice at the time. This yields an estimated number of legacy ongoing advice cases (before lapsed advice is taken then into account – see next page):

Segment Number Segment Name	**1** Retired with resources	**2** Retired on a budget	**3** Affluent and ambitious	**4** Mature and savvy	**5** Living for now	**6** Striving and supporting	**7** Starting out	**8** Hard pressed	**9** Stretched but resourceful	**10** Busy achievers
Potential ongoing advice universe (pre lapsation)	1,606,936.45	171,615.47	1,192,945.07	579,710.37	76,467.24	24,507.96	9,480.27	-	1,303,854.06	602,125.83

Lapsation of ongoing advice usage was then factored in to estimate the current number of active legacy ongoing advice cases

- The annual lapsation assumption is judgementally set at 10% - ie each year, 10% lapse their ongoing advice. This lapsation assumption is based on judgement without empirical support but is believed to be conservative and therefore, if anything, will overstate advice demand and therefore increase the size of any advice gap.

- Factoring in this lapsation assumption into the earlier probability calculations therefore generates a modelled count of currently active ongoing advice cases as follows:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Current ongoing advice count (net of lapses)	798,892	57,822	620,872	310,164	19,580	6,275	1,330	-	648,214	308,820
Total (all segments)	2,771,969									

- As noted in the results and sensitivities section, this figure is sensitive to the annual lapse rate assumption which, together with the general absence of empirical data in this area makes this figure potentially subject to a fairly wide margin of error.

Estimation of initial advice capacity required: approach overview

Hours of advisory time required

Based on the segmental demand for initial advice, hypothesise the proportion of advice cases seeking holistic and transactional advice.

Hypothesise the capacity consumption assumptions for each of the proposition types.

Apply the number of advice cases for each proposition type to the hypothesised capacity consumption for the relevant proposition type to yield a total number of adviser hours required to meet the modelled initial advice demand.

Number of advisers required

Formulate assumptions for the average number of hours available to advisers for the purposes of giving advice.

Divide the number of advice hours demanded by the number of advice hours available per adviser to yield a capacity requirement in FTE.

Apply a part time proportion assumption to the FTE capacity requirement to yield the number of actual advisers required to meet initial advice demand.

The capacity modelling approach builds on the demand modelling

- The demand modelling work yielded a projected count of initial advice cases broken down by customer segments as illustrated below:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Seg count	6,800,000	3,600,000	5,500,000	3,300,000	6,700,000	4,000,000	4,400,000	4,700,000	6,900,000	3,400,000
Decision units (scaled for couples)	5,107,556	3,072,000	4,173,889	2,449,333	5,657,778	3,288,889	4,224,000	4,151,667	4,814,667	2,266,667
Projected advice count	674,542	228,934	596,144	367,400	297,624	173,010	111,101	-	635,861	315,612
Total Advice count (all segments)	3,400,227									

- The total projected initial advice count for each segment was then segmented further into advisory propositions which are based on expected advice capacity consumption.

Advice Proposition	Definition
Holistic advice	Holistic regulated financial planning and advice that takes account of the totality of the client's financial position and goals in providing advice in respect of retail investments.
Transactional advice	Regulated financial advice and planning focused on a client-specified goal in respect of retail investments (such as how to invest a given sum of money at a point in time).

Total projected initial advice capacity for each customer segment is then segmented further by advisory proposition

- Assumptions are made as to the proportions of each segment's demand that are likely to seek holistic and transactional advice.
- These assumptions are judgementally applied on the basis of underlying segment profile data. This application of judgement considers characteristics such as wealth stock and wealth complexity on the basis that increased levels of wealth and wealth complexity will correspond with a greater need and likelihood of seeking holistic financial advice.

- The base case assumptions about advice proposition mix by segment are as follows:

Segment Number	1	2	3	4	5	6	7	8	9	10	Weighted average
Segment Name	Retired with resources	Retired on a budget	Affluent and ambitious	Mature and savvy	Living for now	Striving and supporting	Starting out	Hard pressed	Stretched but resourceful	Busy achievers	
Projected initial advice count	674,542	228,934	596,144	367,400	297,624	173,010	111,101	-	635,861	315,612	
% Holistic advice	25%	20%	25%	25%	0%	10%	5%	0%	25%	25%	**21%**
% Transactional advice	75%	80%	75%	75%	100%	90%	95%	100%	75%	75%	**79%**

- In the absence of data, assumptions are defined judgementally for the expected advisory capacity consumption based on experience of what is likely to be reasonable:

Advice Proposition	Adviser hours required per case
Holistic advice	8 hours per case
Transactional	4 hours per case

- The capacity consumption assumptions do not include apportionment of 'overhead time' – such as time spent on business administration as this is factored in later when considering adviser time available for advice.

Applying the number of projected cases by advisory proposition to the capacity consumption assumptions yields advice hours required

- Multiplication of the number of cases by the capacity required to service them yields the number of adviser hours required to service each advisory proposition type for each segment as illustrated below:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Projected initial advice count	674,542	228,934	596,144	367,400	297,624	173,010	111,101	-	635,861	315,612
% Holistic advice	25%	20%	25%	25%	0%	10%	5%	0%	25%	25%
% Transactional advice	75%	80%	75%	75%	100%	90%	95%	100%	75%	75%
Holistic advice count	168,635	45,787	149,036	91,850	-	17,301	5,555	-	158,965	78,903
Transactional advice count	505,906	183,148	447,108	275,550	297,624	155,709	105,545	-	476,895	236,709
Holistic advice hours assumption	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
Transactional advice hours assumption	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Holistic advice cap consumption (hrs)	1,349,083	366,295	1,192,288	734,800	-	138,408	44,440	-	1,271,721	631,223
Transactional advice cap consumption (hrs)	2,023,625	732,590	1,788,432	1,102,200	1,190,496	622,836	422,182	-	1,907,582	946,835
Capacity requirement implied by demand/service usage	3,372,708	1,098,885	2,980,719	1,837,000	1,190,496	761,244	466,622	-	3,179,303	1,578,058

Total capacity required (Hrs) (all segments)	16,465,037

Translating initial advice hours into the number of 'full time equivalent' (FTE) advisers requires assumptions regarding the number of hours available per adviser for giving advice

- In order to translate the advice hours demanded into a measure of individuals required to provide advice to meet initial advice demand, further judgemental assumptions are needed to determine the number of hours that an adviser has available for the purposes of giving advice.
- On the basis of a 35 hour working week, 5 weeks' holiday and 8 bank holidays, we calculate that there are 1,589 working hours per annum available to each adviser.
- We assume that approximately 60% of this time is available for the purposes of giving advice, with the remaining 40% being accounted for by a combination of marketing and prospecting activity, business administration, un-remunerated client servicing, and 'other' including continuing professional development and regulatory compliance. We arrive at this assumption on the basis of expert judgement applied to update previous Deloitte assumptions cited in their report to the FSA 'Costing Intermediary Services' (November 2008).
- We therefore assume that of 1,589 working hours available per annum, each adviser has, on average, 906 hours available for the purposes of giving advice. Dividing the total hours of initial advice demanded by the hours available yields an estimate of the number of 'Full Time Equivalent' advisers required to service the initial advice demand:

Segment Number	1	2	3	4	5	6	7	8	9	10
Segment Name	Retired with resources	Retired on a budget	Affluent and ambitious	Mature and savvy	Living for now	Striving and supporting	Starting out	Hard pressed	Stretched but resourceful	Busy achievers
Capacity requirement implied by demand	3,372,708	1,098,885	2,980,719	1,837,000	1,190,496	761,244	466,622	-	3,179,303	1,578,058
Total Capacity required (FTE)	3,724	1,213	3,291	2,028	1,314	840	515	-	3,510	1,742

Total capacity required (FTE) (all segments)	18,179

Converting the number of full time equivalent advisers into the number of actual advisers requires allowance for part time advisers

- Finally, an allowance is made for the existence of part time advisers. The base case assumption for this is that 10% of advisers work half time. This assumption is arrived at on the basis of subjective judgement and without the benefit of primary research validation.

- The practical implication of this assumption is that the model calculates the number of advisers required to meet initial investment advice demand as being 10% higher than the number of 'full time equivalent' advisers required*:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Total persons required/segment	4,096	1,335	3,620	2,231	1,446	925	567	-	3,861	1,917
Total persons required (all segments)	19,997									

* Expressed in an alternate manner: the 10% of the advisory capacity that works half time performs half of the workload that they would if they were full time. Therefore the 10% of the workload that would, ordinarily, have been performed by these advisers had they been full time requires double the number of advisers to complete – ie an additional 10%.

Legacy ongoing advice capacity required: approach overview

Hours of advisory time required

Based on the segmental demand for ongoing advice, estimate the proportion of cases demanded by each segment that will seek holistic or transactional ongoing advice.

Apply the capacity consumption assumptions for each advisory proposition type to the relevant number of cases in each segment to yield hours of advisory time demanded for legacy ongoing advice.

Number of advisers required

Utilise the same assumptions for the average number of hours available to advisers for the purposes of giving advice as for the initial advice capacity required modelling (see earlier).

Divide the number of advice hours demanded by the number of advice hours available per adviser to yield the capacity requirement in FTE.

Apply a part time proportion assumption to the FTE capacity requirement to yield number of advisers required to meet demand for legacy ongoing advice.

The legacy ongoing advice capacity modelling approach follows very similar principles to initial advice

- The demand modelling work output yielded a projected count of legacy ongoing advice cases broken down by customer segments as illustrated below:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Legacy ongoing advice cases	798,892	57,822	620,872	310,164	19,580	6,275	1,330	-	648,214	308,820

- The total projected legacy ongoing advice count for each customer segment is then broken down further into advisory propositions using the same proposition typologies and proportion assumptions for each segment as for the initial advice modelling. The base case assumptions are therefore as follows:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
% Holistic capacity consumption	25%	20%	25%	25%	0%	10%	5%	0%	25%	25%
% Transactional capacity consumption	75%	80%	75%	75%	100%	90%	95%	100%	75%	75%

- The rationale underlying the use of the same proportions is that it is considered likely that the level of service between the initial and the resulting ongoing advice will be consistent.

Applying the number of projected legacy ongoing advice cases to the capacity consumption assumptions yields advice hours required

- Assumptions are then judgementally defined for the expected advisory capacity consumption of legacy ongoing advice per advice case as follows:

Advice Proposition	Adviser hours required per case
Holistic advice	3 hours per case
Transactional advice	1 hour per case

- The capacity consumption assumptions do not include apportionment of 'overhead time' – such as time spent on business administration as this is factored in later when considering adviser time available for advice.

- Multiplication of the number of cases and the capacity required to service them yields the number of adviser hours required:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Holistic advice cap consumption (hrs)	599,169	34,693	465,654	232,623	-	1,883	199	-	486,160	231,615
Transactional advice cap consumption (hrs)	599,169	46,258	465,654	232,623	19,580	5,648	1,263	-	486,160	231,615
Total capacity required (hours)	1,198,338	80,951	931,309	465,246	19,580	7,530	1,463	-	972,321	463,230

Total capacity required (hrs) (all segments)	4,139,967

Note:

The total hours of capacity required for legacy ongoing holistic and transactional advice is the same in each of segments 1, 3, 4, 9 and 10. This results from the interaction of the ratio of holistic to transactional advice and the ratio of the hours required for each of the proposition types. Essentially, in these segments, there are three times as many transactional cases as holistic cases but they take a third of the capacity per case – hence the number of hours required is, coincidentally, the same for both holistic and transactional.

The number of advisers needed to service legacy ongoing advice is calculated by dividing the total number of hours required by hours available per adviser

- To translate the advice hours required into a measure of individuals providing advice, the same assumptions as used for initial advice are applied to determine the number of hours that an adviser has available for the purposes of giving advice (ie just over 900 hours). Dividing the hours of advice demanded by the available time per adviser therefore yields a number of full time equivalent (FTE) advisers required in order to serve the legacy ongoing advice demand:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Total capacity required (FTE)	1,323	89	1,028	514	22	8	2	-	1,074	511

Total capacity required (FTE) (all segments)	4,571

- Finally, an allowance is made for the existence of part time advisers. The base case assumption for this is the same as for the initial advice demand capacity modelling – ie that 10% of advisers work half time. Once applied, this assumption translates full time equivalent advisers into actual individuals required:

Segment Number Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers
Total persons required/segment	1,455	98	1,131	565	24	9	2	-	1,181	563

Total persons required (all segments)	**5,028**

The number of retail investment advisers currently active in the market is estimated at around 30,000

- The number of regulated financial advisers active in the market at any one time is subject to some data uncertainty.
- Based on the FCA press release of 13 January 2014, the total number of advisers active in the market was cited as being 31,220.
- More recent publically available data from Matrix solutions as at September 2014 cites the number of CF30 individuals in their ‘investment intermediary universe’ as being 28,199.
- For the purposes of considering the advice gap, we therefore make an estimate that there are in the region of 30,000 retail investment advisers active in the UK market.

Results, sensitivities and discussion - demand

Demand modelling results indicate approximately 3.4 million initial advice cases and 2.8 million legacy ongoing advice cases in the 12 month period

Segment Number	1	2	3	4	5	6	7	8	9	10
Segment Name	Retired with resources	Retired on a budget	Affluent and ambitious	Mature and savvy	Living for now	Striving and supporting	Starting out	Hard pressed	Stretched but resourceful	Busy achievers
Estimated initial advice count	674,542	228,934	596,144	367,400	297,624	173,010	111,101	-	635,861	315,612
Total estimated initial advice count (all segments)	**3,400,227**									
Estimated ongoing advice count (net of lapses)	798,892	57,822	620,872	310,164	19,580	6,275	1,330	-	648,214	308,820
Total estimated legacy ongoing advice count (all segments)	**2,771,969**									

Initial advice demand – sensitivity to a 10% change in key assumptions

- The following table outlines the percentage impact on the total initial advice cases demanded that results from changing each of the key assumptions by 10% of their base-case value.

Assumption	Base Value	Basis	% change in initial advice cases resulting from a 10% change in assumption
'Decision unit' scaling for married/cohabiting	1.8	TW Estimate	3.6%
Advice to purchase drop out rate	30%	TW Estimate	1.6%
Lowest probability of seeking advice*	0%	TW Estimate	5.2%
Highest probability of seeking advice	15%	TW Estimate	6.4%

*Increased by 1.5% percentage points as a 10% increase from zero is zero

Legacy ongoing advice demand – sensitivity to a 10% change in key assumptions

- The following table outlines the percentage impact on the legacy ongoing advice cases that results from changing each of the key assumptions by 10% of their base-case value.

Note The historic take up of legacy ongoing advice is based on the modelling for initial advice take up, hence the legacy ongoing advice model shares some key assumptions with the initial advice model (as outlined on the previous page). The table below illustrates the impact on the number of legacy ongoing advice cases from changing the shared assumptions as well as the further assumptions dedicated to legacy ongoing advice.

Assumption	Base Value	Basis	% change in legacy ongoing advice cases resulting from a 10% change in assumption
‘Decision unit’ scaling for married/cohabiting	1.8	TW Estimate	0.9%
Initial advice to purchase drop out rate	30%	TW Estimate	1.0%
Lowest probability of seeking initial advice*	0%	TW Estimate	0.4%
Highest probability of seeking initial advice	15%	TW Estimate	8.3%
Probability of maintaining ongoing advice in any one year	90%	TW Estimate	70.5%
High probability of ongoing advice take up	60%	TW Estimate	9.2%
Average probability of ongoing advice take up	40%	TW Estimate	0.8%
Low probability of ongoing advice take up*	0%	TW Estimate	0.1%

*Increased by 1.5% percentage points as a 10% increase from zero is zero

Discussion of results and implications

- The results of the modelling imply about 3.4 million instances of initial retail investment advice per annum in the UK. In addition to this, the modelling suggests that there are approximately 2.8 million instances of legacy ongoing advice resulting from initial advice in prior years.

- Three segments account for over 55% of the initial advice demand, this being underpinned by the higher incomes of the '*affluent and ambitious*' and '*stretched but resourceful*' segments, and the wealth complexity of the '*retired with resources*' segment.

- The model suggests that the '*hard pressed'* segment accounts for almost zero initial and legacy ongoing advice demand which broadly reconciles with intuition given their limited disposable income and straightforward asset bases where such assets exist.

- A potential concern, however, may be the 17% of initial advice demand that the model implies should emanate from segments that are also, intuitively, least likely to be financially attractive to service. '*Living for now'* and '*Striving and supporting'* and '*Starting out'* may therefore, between them, represent a source of advice demand that is difficult to fulfil economically using traditional financial planning models.

- The stock of legacy ongoing advice, at 2.8 million cases, is very sensitive to the annual lapse rate assumption from both product and, since the RDR, ongoing advice itself (as discussed in the methodology section). The transparency of ongoing advice pricing and the ease with which the offering can be cancelled under the RDR may possibly therefore lend itself to a step increase in the lapse rates of legacy ongoing advice with a commensurate fall in the demand for legacy ongoing advice.

- Finally, the modelling, as previously discussed in the methodology section, is grounded in assumed segmental characteristics and the estimated market-wide purchase rate and therefore there is a potential disconnect between the demand for advice modelled by this work, and what demand for advice *ought* to be if (a) its value were better understood by the general population and (b) the advice was provided in a suitably efficient and cost effective manner.

Results, sensitivities and discussion - supply

The results suggest that approximately 25,000 advisers are required to meet demand

Segment No / Segment Name	1 Retired with resources	2 Retired on a budget	3 Affluent and ambitious	4 Mature and savvy	5 Living for now	6 Striving and supporting	7 Starting out	8 Hard pressed	9 Stretched but resourceful	10 Busy achievers	Total Advisers Requried
INITIAL ADVICE – ADVISERS REQUIRED											
Holistic advice	1,638	445	1,448	892	-	168	54	-	1,544	767	**6,957**
Transactional advice	2,458	890	2,172	1,339	1,446	756	513	-	2,317	1,150	**13,040**
LEGACY ONGOING ADVICE – ADVISERS REQUIRED											
Holistic advice	728	42	566	283	-	2	0	-	590	281	**2,492**
Transactional advice	728	56	566	283	24	7	2	-	590	281	**2,536**
INITIAL AND LEGACY ONGOING ADVICE – ADVISERS REQUIRED											
Holistic advice	2,366	487	2,014	1,175	-	170	54	-	2,135	1,048	**9,449**
Transactional advice	3,185	946	2,738	1,621	1,470	763	514	-	2,907	1,431	**15,576**
TOTAL ADVISERS	**5,551**	**1,433**	**4,751**	**2,796**	**1,470**	**934**	**568**	**-**	**5,042**	**2,479**	**25,025**

Note:

- The hours of capacity required for legacy ongoing holistic and transactional advice is the same in each of segments 1, 3, 4, 9 and 10. This results from the interaction of the ratio of holistic to transactional advice and the ratio of the hours required for each of the proposition types.
- Essentially, in these segments, there are three times as many transactional cases as holistic cases but they take a third of the capacity per case – hence the number of hours required is, coincidentally, the same for both holistic and transactional.

Total advice capacity required – sensitivity to key assumptions

- The following table outlines the percentage impact on the total number of advisers required to meet investment demand that results from changing each of the key capacity consumption assumptions by 10% of their base-case value.

- The key assumptions relating to the underlying number of cases of initial advice and legacy ongoing advice were sensitised earlier on page 35 and 36 and are therefore not included in the table below which considers only those assumptions required to translate number of cases into the adviser capacity that they might be expected to consume.

Assumption	Base Value	Basis	% change in number of advisers resulting from a 10% change in assumption
% of individuals taking holistic advice*	Varies by segment	TW Estimate	9.3%
Holistic advice hours/case (initial)	8.0	TW Estimate	2.8%
Transactional advice hours/case (initial)	4.0	TW Estimate	5.2%
Holistic advice hours/case (ongoing)	3.0	TW Estimate	1.0%
Transactional advice hours/case (ongoing)	1.0	TW Estimate	1.0%
% of adviser time available to advise	57%	TW Estimate	9.5%
% of advisers working half time	10%	TW Estimate	1.8%

*Increased by 10 percentage points for all segments (ie if 25% of a segment was previously assumed to take holistic advice this would be increased to 35% for the sensitivity)

Discussion of results and implications

- The results of the modelling indicate that the number of retail investment advisers required to meet the modelled demand for retail investment advice is in the region of 25,000.

- Comparison of this figure of 25,000 to the approximate number of advisers currently active in the market of 30,000 suggests that based on the modelling assumptions there is sufficient advisory capacity. At a market level the results of the modelling therefore imply that any advice gap that may exist is not resulting from a shortage of advisory capacity.

- As noted in the methodology section and illustrated in the sensitivities, the model is sensitive to the assumptions used, many of which require the application of experience and judgement owing to the absence of robust data that is generally accepted to be reliable.

- The sensitivity analyses conducted on the model suggest that the assumption changes that would be required to return an output implying an advice capacity shortage (ie a requirement for more than 30,000 advisers in order to meet the modelled demand for investment advice) would be substantial and, we believe, would take them beyond levels that would be deemed reasonable.

- In isolation, no single assumption change would be capable of producing an advice capacity shortage without placing the assumption at such a level as to be intuitively very unlikely to be correct.

- An illustrative sensitivity scenario conducted to yield a requirement for approximately 37,000 advisers (ie a requirement for an additional 7,000 advisers in the market over and above existing numbers, and an additional 12,000 over and above the base model result) would require simultaneously:
  - Increasing the proportion of initial advice that is holistic by 10 percentage points for every customer segment
  - Increasing the probability distribution of initial investment advice seeking for the entire market. For this assumption change to still reconcile with observed intermediated investment sales in the market however would require either (a) 50% of advice cases failing to result in an investment product sale (as opposed to the 30% assumed in the base model result) or (b) the average investment case size for data reported through the IMA to be almost half that witnessed for investment cases reported by the ABI.
  - A 10% increase in the average advisory cycle time for both holistic and transactional advice from 8 and 4 hours respectively in the base model.

Discussion of results and implications (2)

- Although the results of the modelling do not illustrate an advice gap resulting from outright adviser capacity shortage, adviser capacity may not be optimally aligned at customer segment level.

- Whilst it has been possible to estimate demand by consumer segment, it has not been possible to analyse supply by segment. This is because data on the customer segment focus and other key business model attributes (eg what types of consumer specific firms sell to) is not available and cannot be surmised from other data sources. However, anecdotal evidence of developments in the market post RDR suggests that advice capacity serving less affluent segments is likely to have reduced.

- These anecdotally-supported developments include:
  - Advisers focussing on customer segments that are most likely to be able to afford such an offering, or where the benefits of taking advice are most cost-effective.
  - The increased adoption of holistic financial planning models that are likely to be more capacity-intensive.
  - New large-scale services focussed on the needs of less affluent customers are yet to develop to a significant extent.

- Based on our modelling, we estimate that over 60% of demand for retail investment advice is likely to be transactional rather than holistic in nature. It is therefore quite possible that the initial strategic response of advisory businesses to the RDR to move towards holistic financial advice would lend itself to a capacity application mis-match and a shortage of advice capacity – especially at the lower end of the mass market.

- There may therefore be a gap for other forms of financial guidance to less affluent segments A further consideration is therefore whether there is a gap in the nature of the advice or guidance available to less affluent consumers (or consumers generally who do not seek or require full financial advice). This is a potential concern in segments where modelled demand levels for holistic and transactional advice are substantially lower or close to zero. Segments with a lower likelihood of seeking advice (segments 6, 7 and 8) are at potentially higher risk of such mis-matches given their generally lower demand levels and lower wealth stock and income. Whilst not modelled as part of this work, these segments may potentially display higher propensities to seek and utilise other forms of guidance not currently offered by the market.

Reliances and Limitations

Reliances and Limitations

This report is provided subject to the following and the terms set out in our engagement letter of 20 February 2014 and any accompanying or referenced terms and conditions.

Reliances

In preparing this report, Towers Watson has relied on information and data from various publicly- available sources without independent verification. The information and data on which we have relied was, in some instances, limited or indicative in nature. Any additional information becoming available subsequent to this report could lead to different conclusions being reached.

In producing this report we have also relied without independent verification upon the accuracy and completeness of the data and information provided to us, both in written and oral form, by the FCA.

In particular, reliance has been placed upon, but not limited to, the following information:

- FCA 'Consumer Spotlight' segmentation model and segment profiles as supplied by the FCA
- ABI and IMA new business statistics in relation to calendar year 2013

Limitations

This report has been prepared by Towers Watson on an agreed basis to meet the specific purposes of the FCA, and must not be relied upon for any other purpose. Except with the written consent of Towers Watson, the report and any written or oral information or advice provided by Towers Watson must not be reproduced, distributed or communicated in whole or in part to any other person, or be relied upon by any other person. Any reference to Towers Watson in any report or other published documents is not authorised without our prior written consent.

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This report was based on data available to Towers Watson at, or prior to, 21 October 2014 and takes no account of developments after that date. Towers Watson is under no obligation to update or correct inaccuracies which may become apparent in this report.

Towers Watson does not assume any responsibility, or accept any duty of care or liability to any third party and any reliance placed by such third party on this report is entirely at their own risk.

Appendix 1: The FCA 'Consumer Spotlight' segmentation model

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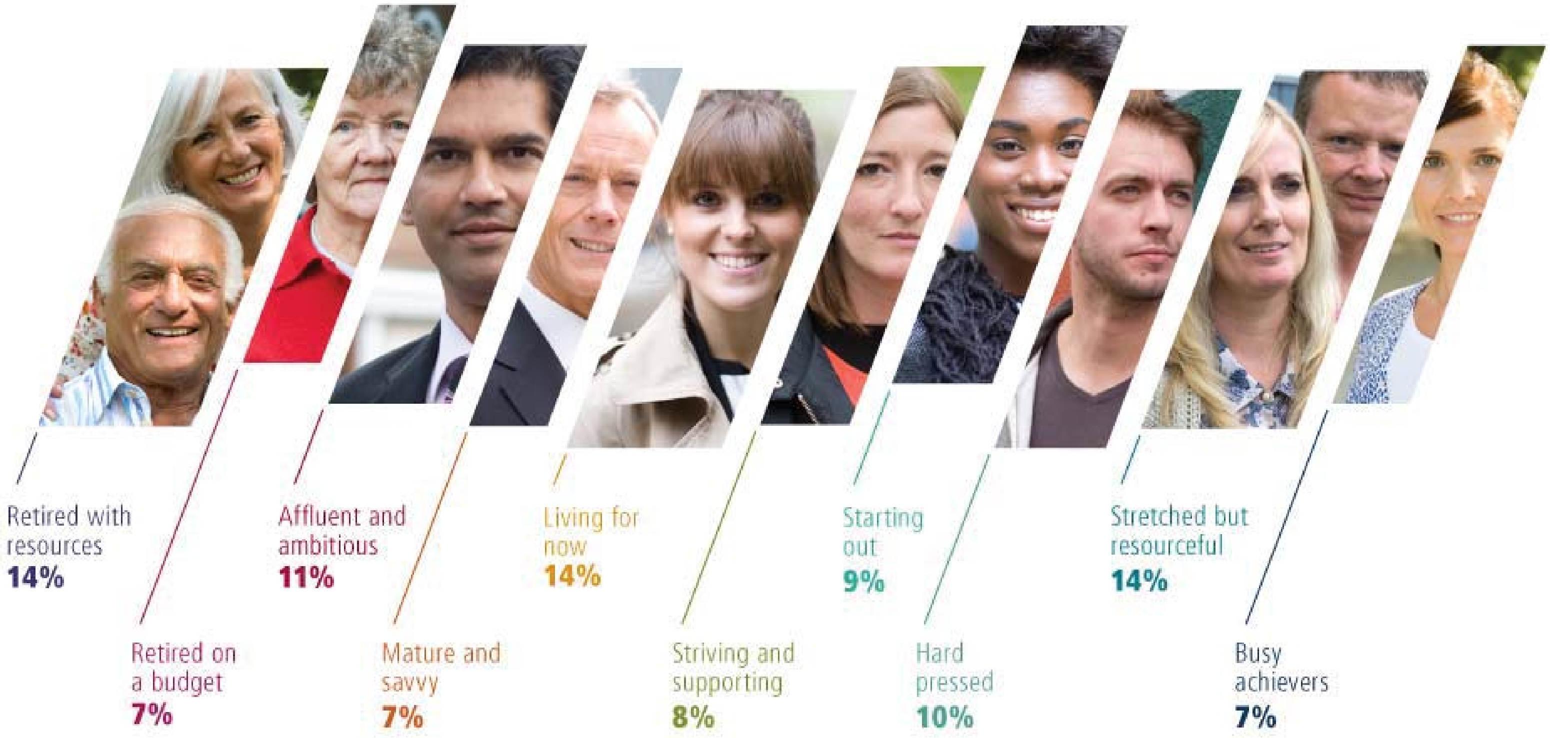
FCA ‘Consumer Spotlight’ segmentation model overview



FCA 'Consumer Spotlight' segmentation model segment descriptions

Retired with resources 14%
Retired people, living comfortably on income from pensions and savings, very rarely going overdrawn or needing to take on debt. The majority have the resources to deal with an income or expenses shock. Some use expert financial advice but they are also well informed. An optimistic and confident group.

Retired on a budget 7%
Retired elderly people, living on low incomes, often alone. Organised and careful with money, they avoid debt and tend to be very loyal to a small number of financial service providers. Many with access challenges due to poor health or disabilities, they are likely to rely on cash and cheques to make payments.

Affluent and ambitious 11%
An affluent working age segment more likely to be men, many are married with children living at home. Financially secure, confident and optimistic, they are likely to own a large number of financial products, including savings and mainstream credit. They enjoy shopping around for the best deals, often online.

Mature and Savvy 7%
An affluent, middle aged segment, more likely to be male. Working and usually home owners, most have some form of savings and investments. They are very confident money managers and generally find it easy to keep up with their financial commitments. A secure and optimistic group.

Living for now 14%
A relatively low income group, more often younger and male. The majority work and keep on top of bills but they tend to be less organised with money than others and can be prone to risk taking. Although internet savvy, they lack confidence in financial decision making, often relying on friends or family for advice.

Striving and supporting 8%
A low income segment, mostly female and the majority with dependent children. Most work but although risk averse, money management is a struggle. They may fall behind on payments, find it difficult to meet an unexpected expense, and rarely switch providers. A busy and pressured group.

Starting out 9%
A young segment of men and women, with more than half from minority ethnic groups. Despite many having higher level qualifications with some still studying, incomes are relatively low. They may struggle to make ends meet, often relying on credit to get by, but they have a strong support network and are confident and optimistic about the future.

Hard pressed 10%
A low income segment of men and women, most are single but many live with dependent children. The majority are out of work and keeping up with bills is a struggle. With low financial confidence and limited access to mainstream credit, this segment finds it hard to make ends meet.

Stretched but resourceful 14%
A family segment of men and women with children, almost all in work. Incomes are relatively high and more than half own their home with a mortgage. Although generally able to keep up with bills, credit use is high. Confident but time poor, many would struggle to cope with an income or expense shock.

Busy achievers 7%
Mainly female and married, most have children living at home. The majority work and household incomes tend to be high. Most have savings as well as loans and credit cards and although often overdrawn, they are able to keep up with household bills. Very time poor, but optimistic and confident about the future.

Appendix 2: Glossary

Glossary

Term	Definition
Advisory proposition	The nature of the regulated retail investment financial advice offered by advisers which is considered to be either 'Holistic' or 'Transactional' in nature.
Capacity consumption	The amount of advisory time 'consumed' by an advice case. This includes time spent directly advising the client, together with preparation, and subsequent administration in relation to that advice. It does not include wider overhead apportionment (for example training, CPD, holidays, etc).
Customer segment	A group of consumers with identifiable common or similar characteristics useful for the purposes of identifying likely behaviours.
Decision unit	The number of 'units' that could possibly seek financial advice in each segment that results from applying the 'family situation' factor to the number of individuals in the segment.
Disposition	Other factors taken into account based on the FCA 'Consumer Spotlight' segmentation model that collectively imply a disposition to seek financial advice, for example more highly educated and/or financially informed segments are assumed to be more likely to understand the benefit of advice and hence seek it.
Family situation	A factor applied to the number of individuals in each segment to take account of those who are married or cohabiting in order to take account of financial advice being taken at a household level.
FCA 'Consumer Spotlight' segmentation model	The FCA 'Consumer Spotlight' segmentation model that segments the adult population of the UK into ten distinct segments on the basis of underlying survey data.
Financial advice	Regulated financial advice given in respect of retail investments in the current twelve month period, including 'initial', and 'legacy ongoing' advice.
Full Time Equivalent	The number of hours that one person would work on a full time basis in a given period.
Holistic advice	Full holistic regulated financial planning and advice that takes account of the totality of the client's financial position and goals in providing advice in respect of retail investments.
Initial advice	The first and subsequent fact finding meetings with a retail client leading to a recommendation to invest in a retail investment product.
Legacy ongoing advice	Ongoing servicing and regulated advice in respect of retail investments that has resulted from initial advice in a period prior to the current twelve months.
Life stage	The likely phase of life (eg, dependent, student, cohabiting, married with children, etc) for those in each segment based on the FCA 'Consumer Spotlight' segmentation model. This is used to infer the likelihood of specific events (eg retirement) that would encourage the seeking of financial advice.
Ongoing advice	Ongoing servicing and regulated advice in respect of retail investments that has resulted from initial advice in the present twelve month period.
Retail investment product	As defined by the FSA handbook at http://fshandbook.info/FS/html/FCA/Glossary/R
Transactional advice	Regulated financial advice and planning focused on a client-specified goal in respect of retail investments (such as how to invest a given sum of money at a point in time).
Wealth complexity	The likely degree of complexity of the wealth stock for those in each segment as implied by the levels of multiple financial product type ownership based on the FCA 'Consumer Spotlight' segmentation Model. This is used to infer the potential for advice seeking on the basis that a more complex financial situation is more likely to require financial advice.
Wealth flow	The likely income level of those in each segment based on the FCA 'Consumer Spotlight' segmentation model. This is used to infer the likelihood of disposable income that would require investment and hence the potential for seeking advice.
Wealth stock	The likely amount of wealth of those in each segment based on the FCA 'Consumer Spotlight' segmentation model. This is used to infer the likelihood of a stock of assets large enough to require investment and hence the potential for seeking advice.

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