The Neglected Generation

Cerulli White Paper | March 2019

Summary

Due to the aging population of the industry's most heavily targeted clients, developing relationships with the next generations of potential investors is paramount. This is not only important when recruiting new clients, but also to ensure firms will retain assets during existing clients' wealth transfers. For good reason, firms are hyper-focused on the Millennial generation, but many are overlooking Generation X.

Key Points

- The collective investable asset base of Generation X ($7.6 trillion) is currently more than four times larger than that of Millennials ($1.8 trillion).
- Gen X and Baby Boomers (*i.e.*, children of the Silent Generation) stand to inherit the most significant share of wealth transferred in the coming decades.
- Placing greater emphasis on Generation X is a relatively easy process as it dovetails with existing initiatives created for Baby Boomers or Millennials.
- Young Gen-Xers appreciate the potential benefits of professional advice, but they remain hesitant to fully engage financial advisors.

Lost in the Fray

Strong segmentation strategies are healthy for the industry and are a characteristic of successful wealth managers. Virtually every organization includes the Baby Boomer, Silent, and Greatest Generations among their most heavily targeted clientele. Focusing on older generations is prudent; however, too many firms are succumbing to the impulse that they must rush to immediately meet the perceived demands of Millennials.

Cerulli is not implying that building relationships with the next generations or developing services associated with Millennials (*e.g.*, digital capabilities) are a waste of resources. On the contrary, these initiatives are so critical that they may determine future market leaders. That being said, while Millennials can't be ignored, the hype is compelling much of the industry to overlook the similar demands and much larger opportunity presented by Generation X—a group commonly referred to as the Neglected Generation.

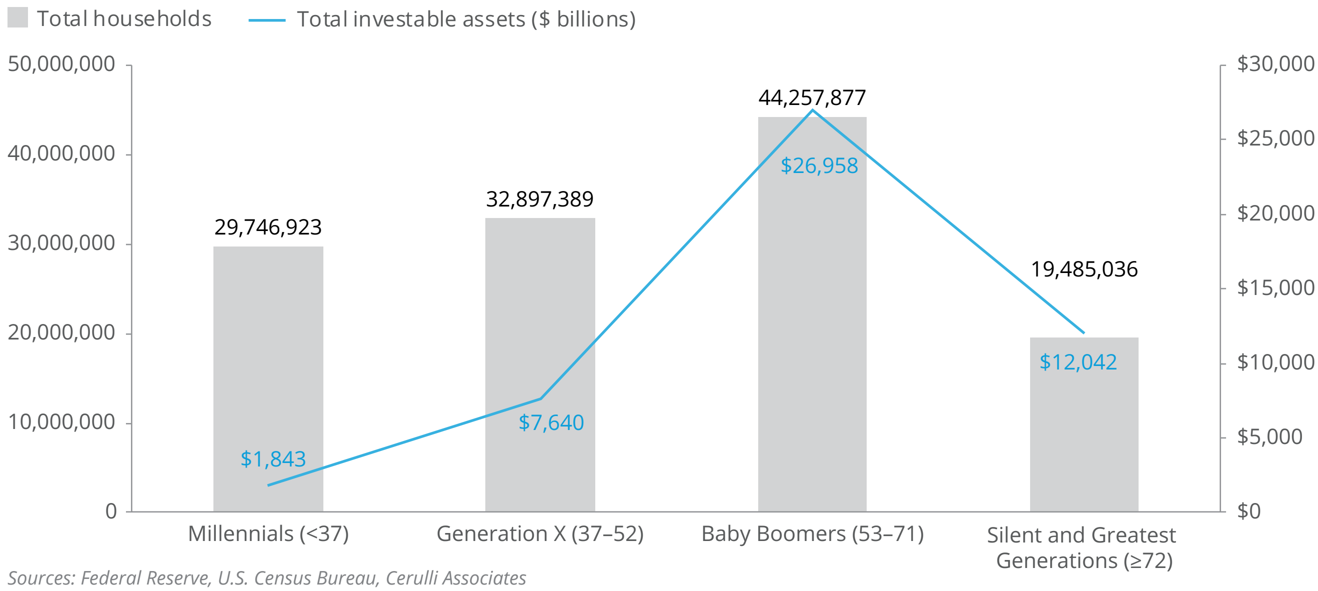
Millennial Focus

In recent years, two trends have accelerated firms' scrambling to react to Millennials—population size and the inevitable impact of wealth transfers. Cerulli can debate both of these in favor of Gen X.

Per the U.S. Census Bureau, the Millennial population has exceeded that of Baby Boomers. This has fueled an urgency to adapt. However, when viewed through Cerulli's lens, there are approximately 30 million addressable Millennial households, compared to 33 million and 44 million households led by Generation X and Baby Boomers, respectively. Moreover, the total addressable investable asset base of Gen X ($7.6 trillion) is more than four times larger than that of Millennials ($1.8 trillion).

EXHIBIT 1

Distribution of Households and Average Investable Assets by Generation, 2017E



Sources: Federal Reserve, U.S. Census Bureau, Cerulli Associates

Analyst Note: Cerulli's investor sizing is derived from the Federal Reserve's Survey of Consumer Finances (SCF), a tri-annual survey. The Federal Reserve releases the Survey of Consumer Finances data two years after survey data collection, meaning 2016 data was released in 2018. To make estimates for the current year, Cerulli projects assets by applying the growth or decline of values for each individual asset and debt category for each household within the survey. In addition, Cerulli adjusts the number of households to reflect the growth of the U.S. population and new household creation.

The enthusiasm surrounding Millennials and the influence that they already have on services and delivery mediums is real, but for wealth managers specifically, there is a massive difference between total population and addressable households in terms of assets.

More important is the impact of wealth transfers. Many industry executives acknowledge this is the central motive for such a strong focus on Millennials. However, this is another area where Gen X is being significantly overlooked.

Firms cannot lose sight of the fact that households led by investors age 60 or older control 57% of all investable assets. Conceptually, these are the wealth benefactors, but average investable assets total approximately $640,000. It's not surprising that their major concerns are protecting current levels of wealth, planning for retirement, and the cost of healthcare. At this level of assets, many may struggle to fund their own retirements, while leaving behind a monetary legacy is unlikely.

The most impactful inheritances will be concentrated among upmarket investors who rely on estate planning services. Nearly two-thirds (61%) of all families with investable assets greater than $5 million are led by investors age 60 or older.

The industry needs to reconsider an important element: How many members of the three oldest generations—Greatest, Silent, and older Baby Boomers—have Millennial children? A reasonable number of these investors will have Millennial heirs, including grandchildren, that will benefit. However, based on age alone, it is Gen X and younger Baby Boomers (*i.e.*, children of the Silent Generation) that stand to inherit the most significant share of wealth transferred in the coming decades.

EXHIBIT 2

Household Advice Orientation by Generation, YE 2018

	Generation				
Advice Orientation	**Millennials**	**Generation X**	**Baby Boomers**	**Silent and Greatest Generations**	**All Households**
Self-directed	46%	42%	30%	29%	34%
Advice for special events	31%	28%	23%	17%	24%
Advisor-assisted	12%	15%	20%	20%	18%
Advisor-directed	10%	15%	28%	34%	24%
Total advisor-reliant	**22%**	**30%**	**47%**	**54%**	**42%**

Sources: Phoenix Marketing International, Cerulli Associates

From a practical perspective, Cerulli advises firms to analyze their client base. Cerulli trusts that most children of affluent, aging clients will be in their late 30s or 40s, if not older. Unfortunately, this information is often outdated or unavailable. This highlights the need to engage clients' family members immediately or there will be little hope of retaining the assets. Many high-net-worth (HNW)-focused practices are overestimating their chances of retaining families' assets simply because they work with the current wealth owners.

Use of Existing Resources

For segmentation purposes, Generation X is a unique group, especially if viewed in two distinct segments. Placing greater emphasis on the generation can be a natural use of existing resources. For many firms, these investors can fit within existing initiatives created for Baby Boomers or in reaction to the demands of Millennials.

Gen X and Baby Boomers

Baby Boomers (53 to 71 years old as of year-end 2017) control nearly $27 trillion in investable assets and have nearly the highest percentage allocated across retirement accounts and mutual funds. Preserving wealth and assuring a comfortable retirement are consistently their most important financial goals. Caring for the health and financial well-being of their children (often adult children) and elderly parents are also major aspirations.

It's not surprising that these investors are considered prime candidates for income-oriented products, such as annuities, as they approach retirement. Nor is it surprising that they are among the most likely to be advisor-reliant investors, as these objectives require disciplined saving and investing habits and goals-based financial planning.

However, the lines become blurred among the youngest of the Baby Boomers (*i.e.*, ages 53 to 60). Like a younger Baby Boomer, the older half of Gen X (*i.e.*, ages 43 to 52) is not only approaching prime wealth accumulation years, but its economic concerns and trust in firms are essentially identical. These investors have accumulated significant assets and are primed to inherit more. They may also be facing significant life events such as caring for multiple generations, college planning, and large purchases (*e.g.*, second homes).

Financial planning services that address Baby Boomers' core goals may translate seamlessly to older Gen-Xers, including cash flow, insurance, and retirement services. Approximately one in five Gen-Xers and Baby Boomers took a 401(k) loan in the last three years. "Funding basic spending needs" and "because it appeared as the best option" were common motives. In most cases, this indicates a lack of non-retirement savings and professional guidance. Without better preparation, meeting goals will be challenging.

EXHIBIT 3

Households That Feel They Need More Investment Advice by Generation, YE 2018

	Generation				
Household Needs More Advice	Millennials	Generation X	Baby Boomers	Silent and Greatest Generations	All Households
Agree	52.7%	42.1%	30.4%	19.4%	33.8%
Neutral	29.7%	29.9%	32.5%	35.7%	32.1%
Disagree	17.5%	28.0%	37.1%	44.9%	34.0%

Sources: Phoenix Marketing International, Cerulli Associates

Analyst Note: Households were asked how much they agreed or disagreed with the following statement: "I find that I need more financial and investment advice than I have in the past."

Fortunately, older Gen-Xers are 47% more likely than Millennials to identify themselves as advisor-directed. Their willingness to work with an advisor removes an immediate hurdle for firms because direct-to-consumer and digital solutions continue to gain traction among younger Gen-Xers and Millennials.

When choosing an advisor, Gen-Xers in their 40s emphasize the importance of transparent interactions, prompt replies, and advisors taking the time to fully understand their needs. However, they represent an inflection point for the industry—41% say they need more investment advice, but this rate declines at age 50 (38%) and plummets to 22% by age 70.

This reaffirms that, while the industry's focus on older investors is understandable, the space has become somewhat saturated. Takeover opportunities always exist for advisors, but the key is to develop relationships with these approachable investors before other advisors do.

Gen-Xers also continue to express a willingness to consolidate financial providers and relationships, especially as wealth increases. Nearly two-thirds of HNW Gen X investors recognize the potential value in doing so, but there is a disconnect between their willingness and taking action. Cerulli recommends that firms continue to round out their digital capabilities without sacrificing active and passive solutions, impact investing, charitable giving services, and at least consider relationship- or enterprise-based pricing. The value in consolidating needs and assets must be clear.

Gen X and Millennials

In contrast, younger Gen-Xers (*i.e.*, late 30s) tend to resemble Millennials, but with more assets. Several firms have deemed this population as being "too young and too broke to bother." Others have taken more strategic steps to address their preferences, such as launching direct investing and/or digital advice platforms. Although encouraging, these digital solutions are typically designed in response to the trendy needs of Millennials, not Gen X. While it is true Millennials were born into the digital environment, many Gen-Xers were young during the digital transition phase. They are generally considered just as tech-savvy, if not tech-dependent, as Millennials.

Interestingly, these younger investors in their 30s are the most likely group to say they need more investment advice, but just 13% report being advisor-directed. Nearly half (44%) define themselves as being strictly self-directed. However, much like Millennials, they seemingly recognize the potential benefits of professional guidance, but their hesitance to engage advisors is a substantial obstacle. Overcoming this is critical. As noted, by the time investors reach age 40, the chances of having an advisor relationship soars. Financial planning becomes more complex as new needs, debt, and goals arise and add to the challenges of saving for retirement.

Although younger investors express retirement planning concerns, their longer time horizons translate to concerns that tend to differ from their elders. For example, they are at least twice as likely to worry about rising interest rates, real estate, inflation, and taxes. These issues offer opportunities for advisors because managing these anxieties and risks are not nearly as commoditized as researching passive or active investments and executing the trade on a discount brokerage platform has become.

Attempting to increase walletshare among young clients is always smart, but firms should prepare for those that prefer a more hands-on approach. More than half of all investors under age 40 say they need more investment advice; however, a similar portion plans to be actively involved in managing their money.

Rather than approaching these households with asset allocation services, the initial strategy may be cash flow management and goals-based planning. They comprehend the value of getting, and remaining, on track. Given their general reluctance to hand over control to advisors, there may also be opportunities to explore alternative pricing models, such as hourly fees or fee-for-planning structures.

In addition, a popular strategy today—comprehensive, bundled services—may fail among many young clients. Like other industries, comfort in technology and fee awareness may mean they will attempt to piece together “comprehensive services” through an unbundled, multi-firm approach. A fair comparison would be the trend of “cutting the cord” with entertainment services. The wealth management industry can try to reject this idea; however, many executives rejected the idea of direct-to-consumer platforms in the ‘90s. Firm leaders must plan ahead.

Time will tell whether these trends remain true as situations become increasingly complex. Many investors may lose interest or aptitude in managing their own wealth. Others may choose to manage investment sleeves that are easily researched, want to test their own investing ideas, or simply not want to consolidate everything with one firm. In the end, they could prove to be time-consuming clients that limit opportunities (*e.g.*, investment discretion). That is, if the industry can convince them to work with advisors.

Preparing for Wealth Transfers

Enriching relationships with clients’ spouses and heirs should be considered as important as recruiting new clients, which most firms admit is their top growth strategy. Gen X and Baby Boomer relatives are high-priority clients. They continue to accumulate their own assets and stand to capitalize on the wealth transfer phenomenon.

Although this is challenging, attracting these family members away from other advisors later will be even more difficult. Again, Cerulli’s data reveals that the older and wealthy a client is, the more likely they have a pre-established advisor relationship. Therefore, the real threat is that Gen X and Baby Boomer heirs will have their own trusted advisors who proactively prepared them for receiving their inheritances.

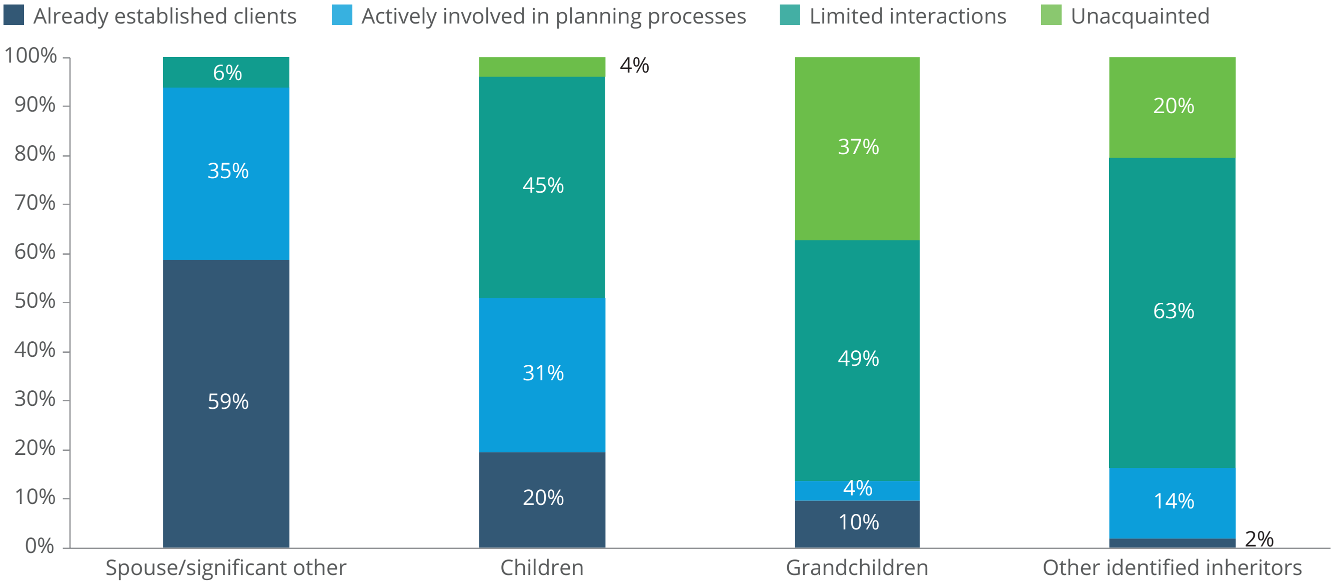
Data from Cerulli’s most recent HNW-focused report displays the huge effect that wealth transfer will have in the coming decades. Sizing the amount of wealth that will be transferred in the next 25 years at $68 trillion, Cerulli concluded that Gen X will surpass Baby Boomers near the end of this period in terms of overall worth as they stand to inherit a greater share of wealth than any other generation.

The Cerulli Report—U.S. High-Net-Worth and Ultra-High-Net-Worth Markets 2018 elaborates on the importance of shifting advisory relationships from the more popular one-to-one model to a one-to-many model in which the advisor is the financial consultant to the whole family and not simply the primary wealth creator.

As this report notes, HNW practices are presented with both a major opportunity and a significant threat as Baby Boomers retire and a significant portion of their wealth is transferred to younger generations. Firms must respond by building multigenerational relationships with their clients and adapt to the new expectations and preferences of the next generation. In order to build greater cohesion across generations, HNW practices will need to encourage greater collaboration between family members, provide better financial education, instill family values, and prepare future generations to manage the families’ business affairs.

EXHIBIT 4

HNW Practices: Relationships with Clients' Potential Inheritors, 2018



Sources: Cerulli Associates, in partnership with the Investments & Wealth Institute (formerly IMCA) and the Financial Planning Association® (FPA®)

Analyst Note: Examples of "Other identified inheritors" include extended family members, friends, foundations, and business partners.

Believing advisors will retain the assets because they worked with parents is a dangerous assumption. In 2016, the two most-cited reasons for clients leaving HNW-focused practices were due to client deaths and beneficiaries opting to leave after their inheritances.

Digital options are a great start to overcoming some of these issues; however, they should not be considered fail-safe solutions to attracting either new, younger investors or clients' heirs. Cerulli truly believes digital capabilities are an increasingly necessary complement to well-rounded offerings, but they are not in and of themselves a "wealth transfer strategy." Although younger investors may lean heavily on these capabilities, the value of human interactions will not cease. This is particularly important on the higher end of the wealth spectrum, where nonfinancial services are typically the differentiator.

Lastly, full blame cannot be placed on practices. Many investors procrastinate including their families in difficult, but important, financial and nonfinancial discussions. Firms must equip their advisors to help coordinate, even mediate, meetings that include as many generations and potential inheritors as possible. This level of service exemplifies goals-based planning, strengthens rapports, and increases the likelihood of retaining assets in the future.

About Cerulli's U.S. High-Net-Worth Research

Cerulli's high-net-worth research focuses on the distribution of retail asset management products and services to the high-net-worth and ultra-high-net-worth segments in the United States. Areas of coverage include market sizing, vehicle use, fees, and services provided at family offices, wirehouses, RIAs, and private banks.

Contact us to learn more:

info@cerulli.com | www.cerulli.com