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Are Cottage Advisors Going the Way of the Family Farm?

By Ed Drake

Growing up on a small hundred-acre hog and cash crop farm in Wisconsin, I always thought I would continue on in farming. Fortunately, I recognized the harsh economic realities early. That, coupled with a love for business and a tremendous curiosity for financial planning lead me to pursue the education and career that I did.

Do I miss the farm? Yes. I miss the work and the open spaces. What I don't miss, however, is the stress of the constant financial threat, volatile commodity prices, ever increasing equipment costs, and continual surprises from Mother Nature; factors that have driven many a family farm out of business. Those that didn't cave realized early on that they needed to bet bigger, by acquisition or by partnering with other farmers to gain economic advantages.

The investment advisory industry is very much the same and is going through a similar metamorphosis that the farming industry experienced, namely, due to brutal market conditions. You either grow or die out. Just as commoditization, regulation and technology dramatically changed and continue to change the face of farming; the same forces are impacting cottage advisors.

When the cottage advisory practice emerged and took off, we were competing against the low service, limited or non-existent planning, often sales focused brokerage and insurance world. Independent cottage advisors offering just basic planning and objective investment management services, by today's standards, could command a great hourly fee or asset management based fee. Today, you could not only argue those fee levels have come down, but also that the level of service expected for those fees has jumped significantly, and continues to do so every year.

Today's Advisor and Challenges to Growth

Currently, you are expected to provide integrated ongoing planning, websites, on-demand performance reporting, social media contacts, a complete and complex array of investments, and tax and other planning solutions to meet the ever growing competitive demands of serving clients. Throw in dynamic marketing needs, growing compliance duties, business responsibilities, and technological advances, you'll begin to see why the complexity of running a cottage practice has grown exponentially. As you might expect, fee competition and the growing service expectations have taxed the time and profits of many advisors, especially the cottage advisor.

Technology may help you provide more services to your clients at a lower cost and faster rate. However, that is a double-edged sword. It means that more and more advisors are offering greater and greater services to their clients. After all, what's the shelf life of any technological advantage we invest in today? One or two years? The technology race in our industry is one of the factors punishing the cottage advisor.

So what do you do? Deny it? Pretend it doesn't exist? The march of market realities makes maintaining the status quo anything but a wise plan. Just ask all those family farmers that I watched fold or sell out growing up.

The bottom-line is, recognizing impending market changes is necessary, and something all of us should plan for accordingly. What does that mean to you and me? It can mean a lot of different things. It just doesn't mean maintaining the status quo, unless you are heading into retirement.

Possible Solutions

You could sell your practice to a larger firm and join them. Bigger firms can offer greater business efficiencies. This may be perfect for some. However, much like the family farmer, maintaining your independence is one of the most attractive benefits of being autonomous.

You could merge with other cottage firms struggling with the same needs as you. Ideally, they would have a similar business approach and culture. Otherwise, a merger of convenience could be a marriage of disaster.

You could outsource one or more of your business functions, like your investment management, financial planning, marketing, human resources, etc. There are Turnkey Asset Management Programs (TAMPs), financial planning teams and the like that can help free up your time and focus. This liberated time could be invested in what you do best—growing and expanding your practice. The trade-off is that many of these functions are crucial to your business. They often help to define your brand. TAMPs and other providers tend to feature their own brands. That dilution of your identity may be a minor or major factor, depending on your practice.

Strategic Partnering

A relatively new approach has been emerging, called strategic partnering. It is something that Hewins Financial Advisors has been doing for years. We are a larger firm that has partnered behind the scenes with cottage advisors or smaller firms to help them grow and expand by utilizing our back-stage and front-stage resources. This allows us to gain greater leverage on the dramatic technology and infrastructure investments we make, while the firms that we partner with gain access to tools, people and infrastructure they may not be able to afford on their own and all while maintaining their brand. In other words, you are aiming to get the advantages of outsourcing while trying to maintain the advantages of being an independent entity. The disadvantage is that this is a newer concept, and few firms are publicly making this offer. So, you may have to approach a lot of other advisors to find those interested in such a partnering.

My intention for this article wasn't to paint a bleak future of the cottage advisor. On the contrary, I think the great features of being a cottage advisor can be preserved. Of course, this can only be accomplished if we recognize the changes that are occurring all around us and take action to create greater efficiency in each of our practices.

About the Author

Ed Drake is a Principal and Regional Director at Hewins Financial Advisors, LLC, a subsidiary of Wipfli LLP. Hewins Financial serves the needs of over 900 clients and manages over $3 billion of investment assets. Ed leads a practice serving about 170 clients and manages over $290 million investment assets.

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