EPISODE TRANSCRIPT

The Banking Crisis: Its Impact on Advisor Movement and the Wealth Management Landscape – A Special Industry Update

A conversation with Louis Diamond.

Mindy Diamond:

Welcome to the latest episode of our podcast series for financial advisors. Today's episode is The Banking Crisis: Its Impact on Advisor Movement and the Wealth Management Landscape - A Special Industry Update with my partner Louis Diamond. I'm Mindy Diamond, and this is Mindy Diamond on Independence.

This podcast is available on our website diamond-consultants.com, as well as Apple Podcasts and other major podcast platforms. If you are not already a subscriber and want to be notified of new show releases, please subscribe right on your favorite podcast platform or on the episode page on our website. For Apple Podcast users, I'd be grateful if you'd give the show a review. Your input helps us to make the series better and alerts other advisors like you, who may find the content to be relevant. And while you're at it, if you know others who are considering change, or simply looking to learn more about the industry landscape, please feel free to share this episode or the series widely.

From all that's happened in the world over the last several years, there have been few events since the financial crisis of '08 that rocked the financial services world in ways which we've experienced over the last several weeks. No doubt, the fall of Silicon Valley Bank and those banks that tumbled after sent shockwaves through the system, reverberating down to wealth management firms of all sizes, their advisors and the clients they serve. So in this episode, we thought it was important to share some perspectives from our vantage point, along with thoughts on how this may impact advisors, movement and the wealth management industry at large. So I've asked my partner, Louis Diamond to join me and there's a lot to discuss, so let's get to it. Louis, thank you for joining me once again.

Louis Diamond:

Yes, of course. Happy to be here.

Mindy Diamond:

So let's jump in. Let's talk about a quick update on why we're having this conversation. What's the relevance of what happened with Silicon Valley Bank and Signature Bank, First Republic Bank and even Schwab?

Louis Diamond:

Yeah, so we're talking about March of 2023, Silicon Valley Bank tumbled unexpectedly, and then Signature Bank over the weekend did the same thing, and then there was shockwaves sent through really all regional banks. First Republic certainly got swept up in it as well, where there is a flight toward larger banks where deposits left, and it was definitely a period of uncertainty. Over that time period too, we saw the stocks of Charles Schwab and LPL Financial and many other firms take a hit. Since then, the stocks have somewhat rebounded, but we're still in a period of uncertainty and flux right now and can

even lump into this somewhat unrelated but somewhat related, UBS buying Credit Suisse in an emergency rescue by the Swiss government.

So lots of changes across the industry, and I think that's why we're talking about this. It's what's the impact on advisor movement and how it might have changed advisor sentiment overall?

Mindy Diamond:

Yeah. Let's back up the train a little and talk first about the evolution of advisor mindset or advisor thinking, and how the pendulum has swung over the years. Two big firms, two independents, back to big firms and back to independents again. So if we rewind to pre-financial crisis, so pre-2008, if we rewind to pre-2008, what we had was a time where advisors believed that they needed the big brand names, the Merrills, the Morgans, the UBSs, the Wells Fargos of the world in order to really satisfy clients' concerns about safety and stability.

So it was rare to find an advisor pre-2008 who went independent because the belief was that independent firms couldn't service and support especially high net worth clients, and independents just didn't provide the safety and stability that clients wanted. Well, enter 2008 and the entire wealth management landscapes get shaken by the fact that if firms like Merrill Lynch could be on the brink of going under and Lehman Brothers can crash and Bear Stearns can go out, what's left?

So all of a sudden, the pendulum swung from advisors believing they needed the biggest brands and the biggest firms to feeling like the notion of the separation of church and state, which is what independents stood for, that assets were custodied at a third party institutional custodian like Schwab or Fidelity or Pershing, and that advisors could really shop the street and leverage best-in-class products and services from anywhere.

So independence has been all the rage for the last decade or more, and it even not only independence, but it really gave rise or created an opening for firms like Raymond James and Stifel and the regional firms who had always been after, or also-rans in the race for top talent really found an opening where even mega-million dollar teams were joining them because it was anything to get away from the bad big firms.

So where we're at today, or pre-March of '23 was an industry landscape where top advisors were as likely if they were to move to go independent as they were to move to just about any employee model. So plenty going to the likes of Morgan Stanley and UBS and Wells Fargo, plenty going to regional firms and plenty going independent. So let me ask you a question as a follow-up to that. We're talking about this Louis, because do we think that the recent news, the recent bank crisis will in any way slow advisor movement overall? So maybe let's talk a little bit about the pace of advisor movement of late and do we think it'll slow?

Louis Diamond:

Yeah, certainly. We just published our transition report for 2022, and one of the main takeaways was that despite everything going on in the world and what the stock market was doing, advisory movement was very, very strong. So we won't know for some time if the events of the last couple of weeks will impact the velocity and direction of advisor movement. We can however use past events to make some predictions and the most notable, you mentioned it earlier, was of course, the Great Financial Crisis of 2008 and 2009.

We actually saw more advisors change firms during that time period than really any time we can remember. Sure, some firms went under or almost went under, but it was a period of dislocation in the markets and that caused a lot of advisor movement. And then even amid one of the worst recessions in US history, advisors really continued to move with record velocity. And why was that the case? It was largely because when an advisor feels frustrated or limited or vulnerable or motivated by a better option that's out there, no amount of market turmoil will change that. We also saw it again during the COVID-19 pandemic where there was a period of just pause because no one knew what was happening in the world, but then things really rebounded and because of this uncertainty and the change in the way the world was operating, advisors moved again with record velocity. So who knows what can happen here, but we do not predict an overall slowdown.

I would say the one thing that this might do, similar to COVID or the Great Recession is those that maybe were on the fence, were a little bit lukewarm about moving, maybe use it as an excuse to stay because anytime there's change, it's hard. So I would say those still motivated and are unhappy enough are still going to move forward with the same velocity or even more, but those that are on the fence and maybe looking for a reason not to do something will use this as comfort to stay put.

Mindy Diamond:

Yeah, I completely agree with that. I think if you think about the most typical drivers that advisors cite for wanting to consider change, those drivers are things like too much bureaucracy or don't like the fact that compliance is managed to the lowest common denominator or don't like the fact that big firms change payouts at will, and whether there's a recession or a banking crisis or anything going on in the markets, that doesn't change the fact that an advisor who's running a successful business and serving a quality group of clients is feeling limited in some way.

What it might do is change where advisors move to, what firms will be the winner in the next year and what firms won't? How do you think advisors will think about custody of assets moving forward?

Louis Diamond:

Yeah, it's an important question. So I think the first thing is the third party custody story worked. In the case of Silicon Valley Bank with assets with Schwab and Fidelity and Pershing, and Signature Bank with Fidelity and First Republic with Pershing as well. Even when these banks had their darkest days, the client assets were safe and that's what's kept a lot of advisors comfortable and also has prevented I

think a lot of clients from leaving, is that the separation of the platform, the advice and the custody actually worked. So even though bank deposits might be secured or unsecured and FDIC and receivership, the investment assets, which is the really important thing, those are safe. So I think this is a live case study that safe asset custody works, especially when you separated from the firm.

The other thing I'll say is clients are certainly more concerned than ever, and rightfully so, about the safety and security of their assets. So that in turn means advisors need to be mindful of how their firm safeguards client money and how clients might perceive that risk. So as we know, many firms' custody assets with one of the major third party custodians like Schwab or Fidelity or Pershing or even are self-clearing, but that doesn't automatically translate into client confidence. Every advisor knows their clients and every client has different sensibilities around safe asset custody and the overall business model.

This much is true though, safety and security means different things to different people. For some, it'll mean establishing an independent firm where the assets are separate from the broker dealer, which is separate from the platform, which is separate from the advice. For others, it means being at a big brand name firm with a rock solid balance sheet, and that hasn't really changed. Ultimately, there's no right answer and we do expect advisor movement to still reflect this dichotomy of choice.

Mindy Diamond:

Yeah, I agree with that totally. As you're talking, I'm really thinking about the fact that in this situation, if you queried 10 advisors that were thinking about making a move, 50% of them would say, "This makes me only want to go to a major firm," and 50% would say, "This would only make me want to go independent." So let's talk about why that would be. Why somebody would only want to go to a big firm is concerned that clients would have a problem swallowing an unknown name. They would want a big brand name, they would want a firm with the big solid balance sheet, and that as deposits in these last couple of weeks have flowed from these regional banks to the big banks, it shores up the notion that big is better.

Why might an advisor prefer an independent or a firm that custodied with a third party custodian? Because they want more freedom and control. They may have come from a big bank like a Merrill Lynch or a UBS or a Morgan Stanley and they move to a bank like a First Republic, for example. And so they watched Merrill Lynch almost fail and get swallowed by a big bank. Then they went to a mid-sized bank and that almost failed. So I think the only logical choice for many of these folks is to move to a model that really gives them total and complete control, as long as their assets are safe, and in any of these models they are, it's just a different way of keeping them safe. So that leads us to the question, so what about the wirehouse firms? What do we think about that?

Louis Diamond:

Yeah, so I think the logical question is will this make all advisors only consider wirehouse firms? I think while this is probably a positive on net for wirehouse firms, there are many advisors and clients that prefer the safety and stability and familiarity of big brands in the wirehouse world, but there's plenty of advisors that we know felt that way even before these recent events. When advisors change firms, data shows they're more likely than not to stay in channel. So that narrative still holds true.

Wirehouses, like I said, certainly look better after this, but the frustrations and limitations that many advisors in the wirehouse world described initially do not magically disappear as a result of this noise. So I think there's probably some that this tips towards the wirehouse world, but certainly doesn't destroy the recruiting ability of regionals and independents. I'll give you a live example of how this plays out.

There's is a story that many of the Silicon Valley Bank advisors joined Serenity Partners, which is an RIA, multi-family office, that custody's third party. At the same time, we've seen now a number of First Republic teams have joined Morgan Stanley. So this is a live example of how advisors impacted by something very, very similar are motivated by different things and go to two firms on the opposite ends of the spectrum, one in RIA and one a bulge bracket wirehouse.

Mindy Diamond:

Tell us a little bit about Cerity? What would make advisors that were worried about safety and stability to the max as Silicon Valley Bank was imploding? What would make them choose a firm with an unknown name that wasn't a bulge bracket firm?

Louis Diamond:

Yeah, I think in the case of the Silicon Valley Bank advisors, many had been operating on an RIA platform for their whole careers. Silicon Valley Bank acquired Boston Private, which had acquired a number of RIAs over the years. So there were advisors that were culturally comfortable with the RIA model, and with third party asset custody. So Cerity serves the ultra-high net worth and investor and is a very well-run private equity backed RIA firm. That custody is with Schwab and Fidelity and Pershing, amongst others. So that's a little bit about them.

So I think in this case, it was where the advisors that were at Silicon Valley Bank mostly came from and also where their assets were custodied. Since their assets were with mostly Schwab is our understanding, it was an easier transition for them to join an RIA that already had Schwab custody.

Mindy Diamond:

And then on the flip side, as you just alluded to, we're recording this on April 5th and as of April 5th, I just read this morning that eight advisors, eight teams I should say, have left First Republic in the last, I don't know, week or two, as their stock has tanked and as they seem looking to find a buyer. And seven of the eight teams have left to go to wirehouses, six to Morgan Stanley, one to UBS, and then one to Rockefeller. So let's talk about that. Let's unpack that for a second. What is it that we think has made

these advisors, so seven of the eight, opt for wirehouses as opposed to going to a firm like a Cerity or any other RIA or even Rockefeller?

Louis Diamond:

Yeah, so I can't speak directly about the intentions or motivations of any of these teams, but my guess is there were teams that were very comfortable operating within a bank. They believed that they needed a big brand behind them, that because of the way assets were custodied at First Republic, they would have to repaper the business anyway, so may as well go to a firm that provided the maximum amount of safety and stability and comfort for their clients.

And in the case of these teams, different from the advisors from Silicon Valley Bank, they all largely came from the wirehouse world. So it was back to a model that they were successful in, that they knew would resonate with their clients. So I think in many ways it was the safe choice is for these teams to go to the largest firms in the industry.

Mindy Diamond:

But I think what remains to be seen is will these folks be happy back at these big firms? Many of them left the big firms to go to a model like a First Republic because it represented the best of both worlds. It gave them more freedom and control than they had at the big firms, and now they're going back to, so it makes sense that they were going back to the place that they believed provided safety and stability for now, whether that works in the long-term remains to be seen.

And I think the other thing is that it creates the question about whether or not this crisis emboldens the wirehouses to be even more strident and less flexible, if you will, because I think one of the things that was really good for advisors was the threat that independence or models like a First Republic, which were so prolific in recruiting, caused them. So if wirehouses swung too far one way and took enough control or freedoms away from the advisors, there were always models like a First Republic or independents for them to go to.

Do you think, Louis, that this banking crisis and the fact that many advisors as a result of this crisis will run from these models back to the wirehouses, will it embolden them further to become even more dug in and less flexible? And how might that affect advisors?

Louis Diamond:

Yeah, it's a great question. So like we were saying, I don't think it's going to necessarily push everyone toward the wirehouses, but it is an interesting point. Do the firm's view alternative models with less skepticism or with less fear and does it make it so that they can push through their agendas and cost-cutting measures with more freedom? I think that remains to be seen.

Mindy Diamond:

Yeah, I would agree totally. I also think that this pendulum swing toward the wirehouses seems to me limited for now to advisors that were impacted or swept up in this banking crisis. I'm not sure that it's going to affect advisor movement or advisors as a whole all that much. Do you?

Louis Diamond:

I agree with you.

Mindy Diamond:

Yeah. So let me ask you another question. What do you think about movement to non-wirehouse firms like Raymond James and RBC and William Blair? Will they continue to be winners or will they get caught up in this change in thought as well?

Louis Diamond:

Yeah, so the firms you mentioned haven't had any headline risk or exposure during the banking crisis. So we still see them as remaining attractive homes for these advisors, similar to those who are considering independents. Maybe it gives those who are still inclined to join a wirehouse who are on the fence about joining these firms, an extra nudge in that direction. But those who still want a full service firm with additional autonomy in a more advisor friendly culture will likely still go the direction of the firms that you mentioned.

I think another outsized winner in all of this, two other boutique firms you didn't mention are Rockefeller and JP Morgan. Both firms have impeccable brands and reputations and advisors that still value the high-end boutique model are going to covet these types of firms, that are still perceived to be safe and I think are still going to be very impactful homes for advisors.

Mindy Diamond:

Yeah. So talk to me for a second about Rockefeller, because Rockefeller actually is the firm with culture most akin to let's say, a First Republic, more of a boutique culture offering advisors more freedom and flexibility. They were already having a whole lot of success. I think I read they recruited one of the First Republic teams, and the thing that I read is that what's attractive is that there is no balance sheet risk. What does that mean to advisors or what could that mean to advisors?

Louis Diamond:

Yeah, so again, depending upon how an advisor views things, the fact that Rockefeller isn't a bank is either an extreme positive or it's a negative. So First Republic obviously is a bank just like UBS and Merrill and Morgan Stanley are banks. Many advisors believe they need to be affiliated with the bank in order to serve clients on both sides of the balance sheet. While others will look at this First Republic and other regional banking crisis and say, "I want to get away from a bank. I like that I can help my clients

with banking. So in the case of Rockefeller, work with a multitude of different lenders but not be exposed to interest rate risk and the balance sheets of a major bank."

So again, it's a matter of perspective as to whether a model like a Rockefeller that isn't attached to a bank is going to win or for some it's going to lose.

Mindy Diamond:

And how does Rockefeller handle deposits, client deposits?

Louis Diamond:

They don't. They custody assets with fidelity, and that's where clients can keep their money. So again, third party asset custody. And then if a client has a lending need, they're able to shop the street and have multiple bank partners and lending partners they can turn to, to serve a client's needs. So instead of being captive or beholden to one institution, they can go to many different institutions as a buy site advocate for clients.

Mindy Diamond:

As we're talking about this, I think the real lesson or the real takeaway from all of this is that the greatly expanded industry landscape is a really, really, really good thing for advisors. It means that if an advisor pokes his head up and is at a place where they believe that they're becoming curious or concerned about whether or not their firm is the best place to service clients or grow their business for the long-term, that they've got choice, that they aren't stuck and that it is as valid to practice, run any size business at a wirehouse as it is at a regional firm, as it is at a boutique firm, as it is at any number of versions of independents. That choice is what keeps every firm from being too empowered and becoming too monopolistic, if you will. And it also keeps everybody in check, I think.

Louis Diamond:

Free market at work.

Mindy Diamond:

Free market at work. I love it. Okay, so let me ask you a closing question, the $64 million question. If we look at things a year from now, who do you think will be the big winners and losers?

Louis Diamond:

Yeah, it's a great question. I think too, a couple of just quick lessons learned from this crisis that advisors will be left with. One of the lessons is do your homework before joining a firm. Ask the tough questions about asset custody, about risk management policies, about balance sheet risk, study the financial statements for those publicly traded companies. Ask to see financials if possible for the privately held ones and just really understand how the business works.

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I think another thing is walk in your client's shoes. Think about what they will be most concerned about. I think now for anyone who moves in the next little while, it's going to be safe asset custody is front and center, similar to what it was a number of years ago. Another one is forgivable notes, while they're a great thing and it de-risks a move for an advisor, in many cases too, it can also remove optionality in time of crisis. And if you're tied into a note and owe back a lot of money, it does sometimes limit where you can go to.

So a nod for those who run their own business that they're not beholden to anyone else and they can make decisions that are best for them and their clients, and I think the last lesson learned is that there's always going to be a reason that the big banks are central to the wealth management industry. Regardless of asset flows and advisor movement and overall sentiment, there's always going to be a place for the major banks, especially within the wealth management industry. So I would say those are the lessons learned, but if we look a year from now, who are going to be the winners and losers? I think it's still rapidly unfolding.

But our guess right now, I'll give you a couple winners, a couple losers. I think the winners like we mentioned, are certainly the wirehouses and the big name banks. They picked up a ton of deposits from Silicon Valley and other banks, and I think they'll continue to be really impactful homes for client assets, but also for advisors. And given what we've seen so far, they will continue to capture the attention of many advisory teams who are at institutions that were impacted by this banking crisis. I think that's one group of winners.

Other group of winners, it's going to be the Rockefellers and multi-family offices who don't have balance sheet risk as we were talking about. These were firms that decided to not be banks and that decision, while maybe it hurts them sometimes with some recruits, I think it's going to serve them really well, that it's clean and that it's separate.

Mindy Diamond:

JP Morgan Securities is an interesting one. While I think largely there is a real separation between the private bank and the JP Morgan Securities or the old Bear Stearns unit with the private bank being the crown jewel of JP Morgan, that JP Morgan name, that JP Morgan Imprimatur is really powerful, and an advisor who works for JP Morgan still holds a JP Morgan business card and I think it's powerful. And with JP Morgan being a firm that wants so much of the deposits that swept over from the banking crisis, a lot of the mid-size bank clients moving to firms like JP Morgan, I think it makes sense. They may be a large winner in this as well. And JP Morgan is really trying to grow that old Bear Stearns unit anyway. This may be just the impetus for them to do so.

Louis Diamond:

Yeah, I think that's right. And then I'll say the losers or the firms that are going to be impacted the most, I would put it into two different categories. So one are smaller self-clearing firms who can't project the

same stability as far as asset custody as the larger ones, and maybe don't have the big name custodians behind them. And unfortunately, the non-bulge bracket banks, the regional banks that have wealth management units, that will certainly take some time to recover. There's scar tissue that will continue to be there and for a very long time, I think advisors are going to have a long memory about what could have happened if they were at a regional bank.

I think the last one, this one is yet to be seen, but I don't think we're done as far as headlines about consolidation. So with more dislocation in the market, there's no doubt going to be more consolidation and M&A between firms. So I think some of the advisors that are at firms that have buyout risk or may be impacted by something that we're not yet seeing, may be put into a situation where they're forced to evaluate alternatives and be put on defense when they have to evaluate a new acquirer or a new platform.

So to me, those are the potential losers. It's the advisors at regional banks or the regional banks themselves. It's smaller self-clearing firms, and it's the next shoe to drop with another wave of consolidation. I think that pretty much covers it. I think we really talked at length about how the landscape is going to be shaken up, how independence is going to be impacted, how regionals and boutiques are shaping up, certainly the strength that the wirehouses have, and then some of the winners and losers.

Mindy Diamond:

As we said, the free market works, and we've had enough proof of concept now to show that I think it's an exciting time to be an advisor. Advisors have choice, that's a good thing. I think it's a good thing for clients. I think it's a good thing for the wealth management industry as a whole. So I thank you once again for joining me, Louis. This was a fun episode, fun quickie, impromptu episode to do, but I think it was an important topic.

Louis Diamond:

Yes, hopefully next time something a little bit more positive as far as the topic, but everything like this is an opportunity.

Mindy Diamond:

I thank you for listening, and I encourage you to visit our website, diamond-consultants.com and click on the tools and resources link for valuable content. You'll also find a link to subscribe for regular updates to the series, and if you're not a recipient of our weekly email, Perspectives For Advisors, click on the articles link to browse recent topics. These written pieces are an ideal way of staying informed about what's going on in the wealth management space without expending the energy that full on exploration requires.

You can feel free to email or call me if you have specific questions. I can be reached at 973-476-8578, which is my cell, or my email, mdiamond@diamond-consultants.com. Please note that all requests are handled with complete discretion and confidentiality, and keep in mind that our services are available without cost to the advisor. You can see our website for more information. And again, if you enjoyed this episode, please feel free to share it with a colleague who might benefit from its content. If you're listening on the Apple Podcast app, I'd be grateful if you gave it a star rating and a review. It will let other advisors know it's a show worth their time to listen to. This is Mindy Diamond on Independence.