Ep #347: XYPN's 2022 Benchmarking Study Highlights: A Review with Alan Moore and Michael Kitces

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XYPN Radio with Maddy Roche

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Narrator: [00:00:05] Welcome to your community of fee-for-service financial advisors who are successfully building profitable firms that serve the next generation of clients. You'll learn from innovative advisors whose unique stories will inspire you to dream big and take action on your goals. Are you ready to live your great life and help clients live theirs? Then you're in the right place.

Alan Moore: [00:00:32] Hello and welcome to this episode of XYPN Radio. I am your host, Alan Moore, and I've invited XYPN co-founder Michael Kitces on the show today to talk about our Annual Member Benchmarking Study that we've just released. Every year we survey our members to understand how their businesses are doing and slice the data to show a number of different angles so you can get an accurate picture of how these advisors really are doing and growing their businesses. We focused on a handful of graphs that we felt really tell the story, looking at things like average gross revenue by year, average fees per client over time, how XYPN member firms are growing, and how having a niche impacts that and ending with a discussion on the revenue expenses and net profit that advisors are earning based on the type of business they're building. And candidly, some concerns we have for firms that are trying to build a more boutique style practice. This is a conversation you don't want to miss. Without further ado, here's my conversation on the data with Michael.

Alan Moore: [00:01:30] We hear it every day: compliance is overwhelming for independent financial advisors. That's why XY Planning Network offers three compliance services to get you the support you need. Let our experts become your experts through our Initial Registration Service, designed to help you navigate your initial state or SEC registration. Get your firm up and running with our Ongoing Compliance Coaching to hone your compliance program so that it grows with you. Want both? Our First Year Compliance Foundations service helps you build a custom-tailored compliance program while you get your firm registered. Go to xyplanningnetwork.com/compliance101 to get the compliance support you need and let us take the guesswork out of the process.

Alan Moore: [00:02:12] Michael, welcome back to the show man. It's been a year.

Michael Kitces: [00:02:15] It's good to be back. It is. This is now like an annual tradition for us. Like, a year has gone by. There's new data. We got a talk.

Alan Moore: [00:02:25] So now we have to review the data. So very excited that we now have our final-final version of our XYPN Annual Benchmarking Study. So for those of you who have not listened to one of these episodes before. Every year we survey our members and gather a whole bunch of data related to their business. How fast or how much they grew, how many new clients, revenue per client, fees per client. What are their expenses in the business? Do they have a niche or not? Do they have the CFP®? Just to really develop an understanding of our member firms. Because our member firms are really unique. So Michael, can you kind of compare like the XYPN Benchmarking Survey and study to sort of industry benchmarking studies that are done?

Michael Kitces: [00:03:11] Yeah, I mean, there are a couple of things to me that are really unique around just what's going on with the industry, with the industry benchmarking studies in general versus what we do at XYPN. The the first thing I mean, just to reflect, like for a lot of the industry studies, you're literally not included unless you have at least $100 million under management, just they start at $100 million firms and then they do hundreds of millions and then a billion and then several billion and all the way up. And so your practices under 100 million are literally excluded from a number of the studies. And even for the subset that that include them, they're not as deep in that realm. And frankly part of it just because you, the metrics of an advisory firm when you just I'm putting just in here, like when you just have a couple of hundred thousand of revenue looks different because at the most basic level, from a business benchmarking perspective, when firms have one or several hundred million dollars under management, really in a revenue sense, when you've got millions of revenue, your your business accounting starts to standardize like you tend to have multiple owners. So like everybody actually has to get paid a salary or compensation. And so what you make off as an advisor in the business starts to separate from what you get as the profits from the business. And frankly, it makes it a little bit easier to benchmark because the numbers are normalized. In-in the realm of advisors who are still on their path to, we'll call it $1,000,000 of revenue. Just the whole nature of benchmarking looks a little bit different because most businesses of that size are essentially the revenue minus the expenses I pay equals mine. As it is, the advisor is the founder as the owner. And so we don't necessarily make the same separations of like what do you earn in the business versus what do you generate as profits from the business. And and so does a lot of industry benchmarking studies don't even do the best job of being able to measure those numbers because businesses under a million account for themselves a little bit differently than the larger ones. And the just additional complicating factor in practice is the industry is mostly AUM by numbers and headcount. So most industry studies are basically benchmarking of AUM firms, not benchmarking of firms that charge fee-for-service. And so between those two, our focus on fee-for-service and the fact that we live in a realm of advisors who by and large are under

$1,000,000 of revenue, gives us a lot more perspective on what's really happening with individual advisors running individual firms.

Alan Moore: [00:05:42] And I do want to call out that we hire a third party agency that-that does surveys and studies like this to come in and operate this independently from us. We are not making up the data, cherry picking the data, anything like that. I mean, we're bringing someone in to really develop an understanding of our member firms. So that really one of the reasons we started this was because we wanted to be sure we were giving realistic expectations to our new members of what-what is expected revenue over time. You know, you're not.

Michael Kitces: [00:06:11] Yeah, the -

Alan Moore: [00:06:12] -if you're starting from scratch, you're not going to earn 100 grand your first year. We wanted the data to be able to show that. And also be sure we weren't telling people you could get you'll make 100 grand in your first year just because one person said they did it.

Michael Kitces: [00:06:23] Yeah, our-our study gets run by the folks at Ensemble Practice, Philip Palaveev and his team. And Philip was one of the original guys that was running the what were known as the Moss Adams Benchmarking Studies literally-literally more than 20 years ago. Like for anybody who's heard the industry label out there Ensemble Practice, like he coined that 22 years ago when he started doing these studies. And so it was very deliberate for us when we decided we want to start doing these benchmarking studies for XYPN to go to the people who had the most depth and the most experience on this to make sure that we are doing this well and properly, to really get a good, accurate understanding of what's-what's going on with XYPN member firms.

Alan Moore: [00:07:06] So if you haven't listened to one of these episodes, we're going to go through some of the highlights of this study. Now, this study, I think, in total is 39 pages. Members do get free access to it, but we're going to go through some highlights. I think we've got seven or eight charts that that we'll talk about just in the course of this, which means we understand the medium through which you are listening to this. So I'm going to draw the graphs with my hands in the air and try to paint the picture for you. But if you go to XYPlanningNetwork.com/347, we will pull these charts out and make them available there so that with the other resources associated with the podcast episode, just so you can see them, because I understand it's a little frustrating, like what was that number again? But we will do our best. So kicking things off, there are a few charts in here that talk about revenue growth over time. And really one of the first charts actually shows this on a cohorted basis, which is starting to get very confusing because there's a lot of lines, a lot of little numbers. And so I think this is the first year we've had what I'll call figure 15, which is sort of this consolidated look at basically how what is the revenue per year for a new firm who is joining XYPN with almost no clients. I think we define this as today you have few fewer than 10% of your clients today were with you when you joined XYPN, which means if you have 50 clients today and you're answering these questions, that means five or fewer of those 50 were with you when you started the firm, which basically separates out anyone who started with revenue.

Michael Kitces: [00:08:44] Yeah, I mean, the goal was just we didn't-we didn't want to talk like, hey, the average member has $200,000 of revenue in the first year because they brought $17 million with them from the old firm and then added three clients. We wanted to really make sure that when we were talking about realistic expectations for the growth of a-of a member firm, that this is like the people who either start with nothing or very close to nothing. Some advisors, if they break out from a firm they were at and have to start clean, start from scratch. So they've got non competes, non solicits like okay, I started from scratch but like my mom and dad came with me and my cousin and like my best friend from a long time that was also working with these, like these were my three clients, but it was, I was basically starting over. So we really wanted to focus this around advisors who were starting from scratch or pretty darn close to starting from scratch. And that also includes just those who are career changers and getting started from literally zero.

Alan Moore: [00:09:45] And what we learned is the same story that we have to tell every year, which is the first two years, are awful. It looks like year three, sometimes it gets better, sometimes it gets worse depending on the date of year. But like year one, according to our data, on average in their first 12 months. Right, Michael? Is it 12 months or-or what if they join in the middle of the year? Do we ask for trailing 12? Is that right?

Michael Kitces: [00:10:09] We asked them for calendar year, but if they started at the very late end of the year, we don't include them. So this is-this is for first year or very close to first full year that you are actually operating.

Alan Moore: [00:10:21] So average first year revenue, 13,449 rounded up 13,500 bucks. That is.

Michael Kitces: [00:10:29] For the year.

Alan Moore: [00:10:30] For the year.

Michael Kitces: [00:10:31] Gross, not net, not after expenses. Gross.

Alan Moore: [00:10:35] So we've said for a long time, first year is hard. It is a grind no matter who you are. But it's.

Michael Kitces: [00:10:41] A little depressing, to be fair, like.

Alan Moore: [00:10:44] Because you're working hard, you're bringing in clients. I think said average was by the end of year one you've brought on four clients. So you're starting to get a little bit of traction. But-but the first year is really tough and-and it's tough for everyone, whether you have a niche or not, whether really the only people who skate by year one or the folks who start with a couple hundred thousand dollars of revenue because they broke away with a book of business. And so if you have the option to go do it that way, I highly recommend it because year one is tough, but year two is when you start to see things get a little better. That's when on average, firms are earning about 62,000 gross.

Michael Kitces: [00:11:20] So you go from 13 to 62.

Alan Moore: [00:11:24] Probably haven't replaced your income from your last advisory practice, but you're-but you're taking some money out of the business. You're making a little bit, you're now getting a paycheck. It's starting to feel like a real business. And year three is really when things open up and that's when we're seeing firms hit 140,000 of average revenue. So 13000 to 62000 to 140000 in their third year.

Michael Kitces: [00:11:49] Another thing to note that these are gross revenue numbers. But realistically, what that means is by year three, almost 140 gross, you're going to have some expense at that point, like, well, you've got XYPN membership with us, but you've got-you've got some technology costs, you're maintaining your website. Maybe you're getting to the point where, like you've outsourced your books, maybe you've got a couple hours of contract or work. If someone like helping you with your website or helping you with some tasks. So these are-these are-are firms that are probably netting right around 100,000. And so just that-that starts to be this crossover of depending on what you were doing previously as a career changer or breaking out from a-from an existing firm like you may or may not be fully back to where you were previously. Like, the numbers are moving. There's material dollars coming out of the business now, if you're-if you're drawing some out to maintain your lifestyle. As I find for a lot of advisors, like just by this point, you're breathing a sigh of relief, like momentum is building. You now have enough clients that they actually refer you like that whole growth through referrals of existing clients. Like now you have existing clients so you can start getting referred and you've been around for three years. So people who are like, Yeah, I've been following your stuff for a while. I, you know, seems like you're here to stay. I'd like to work with you now, like they start appearing. And in part that's what just makes it kind of catapult from there. Like to me, there's this interesting progression that firms-firms get to 62 grand on average in year two, 140 grand in year three. So like you grow more in year three than the first two combined. Depressing but true. Year four the averages goes from 140 to 255. So you almost grow as much in year four as the first three years combined. And it's that kind of hockey stick of growth that begins to come with revenue for most advisors by year four. It's like, okay, I'm now making more than I was before and I own my business. I got my client base and now like people are referring me and stuff's flowing. I'm thinking about hiring a team member to help out with this and the business really starts cranking. But just that journey, that kind of phenomenon of income or not even income, gross revenue, right? You got to be fair. Income will be lower than these numbers because you have expenses, gross income, gross revenue, 13 grand in year one, 62 in year two, 140 in year three, 255 in year four. And it's notable to me that, I mean, well, these numbers literally are the averages of what we've drawn from these studies over the years. But truly, like these numbers have been stunningly consistent as we do them from year to year, they almost never wobble by more than about 10% plus or minus each and each and every year like these have been very consistent.

Alan Moore: [00:14:45] And so this is really why if you're thinking about starting a firm, you're going to be starting from scratch. It's why we say have at least either two years of runway or be able to pay your bills with some other stream of income, whether that's your partners or savings or whatnot, because it really does take till the third year. And remember, it's an average, which means there's a bell curve, which means some people are on the top end of the bell curve and some folks are on the lower end of the bell curve. And so don't don't say like, Oh, well, Alan promised me I'd make 140,000 in year three. That's not how it works. So we're going to talk here throughout this episode of some things that you can do to help. Be sure you're at the mid-level or top end of that bell curve.

Michael Kitces: [00:15:22] Although I would note as well, like, yes, it may take three plus years into the fourth year for a lot of folks to get back to where they were. Depending on quite what your earnings were, where you where you left, but it's not like you're 0000 on that income and then suddenly you're four pops up like you're starting to draw some dollars out. By year two, you're drawing more by year three. It may not be enough to cover your your old salary or your lifestyle by your three, depending on what what that looks like in your cost of living in your area. But it is at least starting to make a dent in it. So I've talked to a lot of members that were going through this transitions. Like at the end of the day, they drew down something in the neighborhood of like one and one half to two years worth of expenses, like they had almost all of their expenses in year one. They had to support like half their expenses in year two and then just a little bit in year three. And then they're really like positive cash flowing as a household, not just as a business, but they can cover their own bills and still have some money left over to start saving as they get latter part of year three and into year four.

Alan Moore: [00:16:29] It's also worth noting that in this chart you start getting out into year five and in year six, XYPN has been around for eight and a half years now, so we're starting to see some of these longer term advisors that are growing. But year five is making 375,000 a year, year six 511,000 on average. And I do want to sort of call this out because XYPN has this reputation in the marketplace for-for a variety of reasons. Welcome to marketing and branding. And that is we're just a bunch of 22 year olds running around who are charged, everybody's charge at 100 bucks a month, which are actually right here in a second and not really making any money. And I was trying to pull up sort of industry studies or industry benchmarks on what the sort of typical registered rep makes. And-and that is per firm. There's just a couple that have that are exceptionally high. But I'm pretty sure, Michael, that like most independent broker-dealers, their reps are making less than six figures on average. Is that accurate?

Michael Kitces: [00:17:26] Well, varies a lot by rep by-by rep and firm for where they are about whether they get to six figures. Most of them they're grossing higher than six figures. Just broker-dealers have a lot of overhead, but you see a lot of broker-dealers where if you look at their broad based numbers of like average rep, average production, average GDC across the whole firm in the IBD realm, there's a lot of folks that are in the 250, 350,000 gross range. Now your-your IBD may be taking 8 to 12% of that off the top, another 10% program fees, like there's a bunch of stuff that starts taking that down. That's before you get to staff, although again, you've got to pay your expenses as an-as an RIA as well. But but by the numbers that we're seeing now for growth of a member, I mean, that's the average across IBD's who have people that have been doing this five, ten, 15, 20 plus years, like we're seeing members on average getting that 250, 250 to 350000 range in 4 to 5-in 4 to 5 years, and then continuing to compound from there. So you've got some firms that like Commonwealth, that's well known for being a much, much higher average rep and wirehouses, where a lot of that is like literally more than $1,000,000 per advisor. But they're working in an ultra high net worth space that just looks different overall when you get to the mass of advisors, it's much more in this realm of two, three, 400,000 gross and you net down from there, which we're seeing members getting to in four or five years on average.

Alan Moore: [00:18:59] Yeah. And and it's almost all recurring revenue, not one off revenue which many of the IBD advisors are-are earning. So if they take a break from their practice for three months, things go to zero. When our advisors take break, things continue, which is, you know.

Michael Kitces: [00:19:15] I mean that's part of the trade off. Like it makes that early. You're much more of a grind. You can move revenue a lot faster when you're selling mutual fund shares out of the gate, which is how a lot of advisors that are experienced today got started ten and 20 years ago. But the flip side of what happens with the compounding is the business gains traction is what we see so clearly in the numbers here.

Alan Moore: [00:19:36] So I'm going to jump to another graph here. So we're going to go to figure two, which is client profitability over the last five years, actually six years. If I'm looking at this from 2016 through 2021 and what this graph shows, it has three numbers associated with. Again, I'll do my best to paint the picture for it year over year, but it shows revenue per client. So just gross fees being charged to the client on average the operating profit of each client. So you may charge 1000, but your profit is 200. And then the sort of profit margin over time. And so what this chart is showing us, just without getting too mired in the numbers, is that back in the day in 2016, our members were effectively charging a little less than 100 bucks a month. They were charging like $900 a year. And we can talk more about why that is. I'll take some of the credit and the fault for-for having too many advisors charging way too little. But some of you may be listening, thinking like, oh, yeah, I was the person who was charging basically 1000 a year for a plan. And then we've seen this slowly increase over time to where in from 2016 to 2019, it was up closer to 15, just over 1500 a year. So it went from 900 to 1500.

Michael Kitces: [00:20:56] So now you're at about $125 a month if you want context.

Alan Moore: [00:21:00] $125 and then 2020, it suddenly went to over $200 a month. In this last year it was almost $300 a month. And so this is a huge increase from over the last five years to go from basically an average planning fee of not or average revenue per client from $912 to $3426. I mean, that's is that 4x, almost 4x the revenue and operating profit margins growing from 21% to 46%, which is just astronomical. So, Michael, you want to talk about sort of what how you're seeing this in the marketplace and what's impacting this.

Michael Kitces: [00:21:40] Yeah, I think the core driver that we're-that we're seeing play out here is-is sort of twofold happening at the same time. On the one end, look, just the reality we've seen in our benchmarking studies since forever, since we first did them, that the overwhelming majority of members raise their fees in the first several years for-for many years, when we did the study, it was literally pegged at 100% of members raised their fees in the first three years. Now we're down to the point that members who join more recently are pricing a little bit higher. So only I think 85% of experienced members now raise their fees in the first three years. So a few of them priced a little higher at the beginning. Almost everybody is-is raising fees and so on. The one end like industry-industry chatter, fee compression, yadda, yadda, yadda, like, like no evidence here. Like it's the opposite here, is what we're seeing in practice. Members are raising fees left and right now, to be fair, again, in some cases, that's because they were charging a little bit lower than they probably should have. In some cases, it's just because they're building their experience and skill set and capabilities to say like, I literally give better advice than I used to. I can charge more for this. For some of them, we're seeing them. They're getting deeper into niches and specializations and just literally able to command higher fees because they've got a more specialized offering as they refine it and iterate on it. I think the other effect, though, frankly, that's starting to crop up and I'm seeing this come up more in-in just conversations with members, there is such a shortage of advisors providing advice in this market, right? Just like 95% ish of advisors are still on some version of commissions or AUM and not doing fee-for-service, but there's literally tens of millions of households who might be willing to pay for financial advice, but they don't want to buy a product, they don't have a portfolio, and so they can't engage a traditional advisor. There's so much demand and so few advisors that I'm seeing a lot of members that essentially are they're getting bid up market. They didn't necessarily set out to say, I want to work with really high income folks, but they're putting their services out in the marketplace. High income folks are showing up and saying like you only charge 300 a month, like I'd pay 400 or $500 a month probably. I don't say that blatantly, but like, oh, $300 a month. What a deal. Like, I'll sign up for that instantly. And when you get enough clients who like, sign up for your $300 a month service without blinking, you start charging 400 and you start charging 500. And so now we're seeing just across the whole network, this average has moved up so dramatically from $75 a month to $125 a month to $200 a month to $300 a month as an average. Right. Again, bell curve around that, some low or some higher that. I think what we're seeing play out is this twin effect of as members get more established, they get more confident in their fees, charge more, create more specialized offerings that command a higher fee in the marketplace and the rising popularity of the model. Means more affluent folks who want to pay a fixed or subscription fee are finding their way to our members, and they're-they're engaging members so quickly. The members are realizing, like, I could charge more for this, like it's selling a little too fast and easily. And so that combination of rising fee confidence and more express demand just is-is leading to this huge increase in what members are managing to charge in the marketplace for their services.

Alan Moore: [00:25:13] Yeah, and I imagine AUM, does play a component here. Again, people think of XYPN is as being anti AUM we are not. We are just anti AUM only because that's a business model that really excludes the vast majority of Americans and the clients that Michael is talking about right now. But the overwhelming majority of our members do manage investments in some capacity on an AUM fee. And in general, when you start working with those clients over several years of saving and sort of charging what you're worth, you get a few rollovers like the assets under management start to increase as well. And you do have that sort of natural fee lift. And later on we're, I don't think we were planning on talking about this, but later on we did talk about raising of retainer fees. So we are seeing advisors both raising their retainer fees, fixed fees, flat fees going from 200 to 225 or 200 to 250 a month in addition to sort of a natural rise of-of AUM as markets go up. This study concluded at the end of 2022 or 2021. So 2022's market is not included in these in these studies. So it'll be interesting to see what what comes out of this next year. But that natural lift as well exists.

Michael Kitces: [00:26:25] And it is a good highlight where AUM fees naturally move with markets. Markets grow over time. Just the raw dollar amount of fees you're getting.

Alan Moore: [00:26:34] Is that guaranteed? Can you guarantee that too?

Michael Kitces: [00:26:37] I will not guarantee that, but it is highly probable according to a lot of historical charts, that technically can't be relied upon. But we all do. The interesting effect that comes from that, though, is while AUM like the literal fee rises naturally, even at a set percentage, your retainer fees only move up if you step forth and say like, I'm increasing my fees because I create more value or costs are up or inflation or some combination thereof. And so it's striking to me, even when we look at fee schedule like changes in fees for scaling members, which are the folks who've been doing this for many years, at least 75 clients, a critical mass of revenue. We look at those numbers like eight over 85% of members of scaling members have raised their retainer fees. Only 23% have raised their AUM fees. And so not seeing a lot of shifts in AUM fees aside from my clients grow with the markets, but I'll have to change my rate. But there is a lift that's happening retainer fees. And part of that is, frankly, you need to and you should be planning to. I mean, especially in an environment like this with inflation, like, look, everybody's raising fees right now in pretty much everything across the board because that's what happens in inflation environments. So I would-I would hope and expect this percentage of members raising fees to go up even higher next year because if you're not looking at raising fees in this inflationary environment, just you're going to have a squeeze in your business. It's going to get hard when you want to hire team or outsource services or buy more tech or whatever it is, because that stuff's going to get more expensive. You have to move your fees in line.

Alan Moore: [00:28:15] Absolutely. All right. I want to jump to figure five. So this is one I have to say, I am like maybe most excited about. I actually presented on a few of these charts to the to the XYPN team yesterday from this recording. And this was one that really highlighted because what this chart shows is the growth of client households. So the number of new clients that our members are serving and it's been a couple of years ago now that at XYPN LIVE we-we sort of said our-our long term vision for the company, our ten year goal, we call it a core target. If you follow EOS, our core target was to have 5000 advisors and to be able to bring real financial planning to half a million consumers, right? You can 5000 advisors serving 100 clients each, half a million consumers. And-and it's very you know, we're not an RIA so we don't, I can't just go run an Orion report that says exactly how many clients are our members serving because they're all attached to sort of one RIA. So it's not very often it's once a year that we get some of these numbers to be able to say like how big of an impact is XYPN having in the marketplace? How faster we growing relative to some of the other other large RIAs that are out there that have hundreds or thousands of advisors and what are their growth rates and that sort of thing. And what makes XYPN advisors unique, and especially the aggregate, is that all of our growth almost exclusively is organic growth. It is not by acquisition. We do have a few who maybe have acquired member or other advisors or have merged firms, but in general the growth rates are natural, are organic. New clients, many times new clients to financial advising in general. But these are really these are not trading one client for another. This is these are all new clients. And so if you look at sort of this this figure, figure five, again, we break this out into sort of three phases of business implementing, building and scaling. So implementing is basically 0 to 20 clients. You're just getting started.

Michael Kitces: [00:30:23] Just getting started. Like how does all this work? I launched my firm. I told some people about it. I hope they pay my services. I'm not quite sure what my pitch is because it changes every week along with my financial plan and my software. Just it's that you're figuring it out phase. You know we all go through.

Alan Moore: [00:30:40] Year one and year two because let's just say you're charging 3000 per client, 20 clients, 60 grand. That's what we're seeing through year two. So this early stage is sort of the first two years. Building is when you cross that mark, you hit your 21st client all the way up to 75 clients. And again, we've historically sort of thought of that as like the 150 to 200000 in revenue is sort of when you hit when you sort of move out of building phase. But that's as you're building the business and then you hit scaling, which we'll talk a little bit later about sort of different-the different elements of scaling. But scaling is when you have 75 clients, you have now grown to a point to where it is you're either not taking new clients or you're hiring staff and you're building out a business and you're making a couple of hundred thousand revenue. So implementing those early days, average growth rates are much higher because the denominator is smaller. When you go from two clients to four clients, you have 100% growth rate. When you go from 100 to 102, it's 2% growth rate. So growth rates are much higher in the early days because the denominator is smaller. But on average, our-our early phase, our implementing members are adding 8.2, say eight clients per year when you move to the building phase. So now we talked about how you add more revenue in year four than you made in your first three years and you added more in year three than your first two years. When you hit the building phase, you're adding 11 and one half clients on average and scaling, which is when you start to see these practices get larger and it does get harder to grow as you get larger, are adding 22 clients on average. So that brings an average across all practices to 13.6 clients per advisor per year. Michael, how do you -

Michael Kitces: [00:32:25] New clients

Alan Moore: [00:32:26] - relate new clients? Absolutely new clients to the practice. So how does that compare to the industry, sort of industry at large that that you see with the other data that's out there?

Michael Kitces: [00:32:37] So these, these numbers are frankly are huge. I mean, if you look just anecdotally at a lot of advisory firms, what you see is individual.

Most individual advisors just struggle to add half a dozen, 5 to 10 new clients a year and the average member is at 13 plus doing basically 1 a month ongoing and in practice scaling firms or averaging almost two a month. Now some of that can get distorted by like, tell me how many clients you've got because firms grow relative to where they are, particularly in a referrals context. So to me this is more powerful to look at on a percentage basis. So average member within the firm is growing client households at 36%. Like that was-that was the numbers in the aggregate. Scaling members who are because that percentage is going to be high if you're like really new and you went from one client to three clients, you're like, ooh, 200% growth because you went from 1 to 3. Even if you look out to scaling members, we're seeing scaling members growing at 28% in growth of new client households. That's how we get to this 36% average for-for across all of XYPN. And just to me, like I've got to put into context how ridiculously large these numbers are, particularly since like this is-this is XYPN wide. So Schwab did a recent benchmarking study of how advisory firms are growing in their overall ecosystem. So if you look at five year compound growth rates out of the Schwab data, average advisory firm is growing at 14% a year over the past five years. Now, the caveat is that in terms of their assets under management, your revenue grows more slowly because some of that growth is just growth in markets and growth and markets comes at the top of your fee schedule at the lowest rate. So firms are growing 14% on assets, but only 11% on revenue. And revenue still grows in part because the lift of markets. So when you look across Schwab's entire like massive benchmarking study because they-they-they study like a bajillion advisors that are in the Schwab ecosystem. The average annual compound growth rate of advisory firms in terms of new client households is 5.1% and XYPN's growth is 36%. I mean, these numbers are just astronomically, ridiculously far apart from each other, even in the Schwab data. Like even if you get down to the smaller firms in in Schwab's data, you know, it was still 14% on asset growth amongst 100 million firms. And our scaling members are doing 28% in households which by Schwab data correlates to about 5 to 6% organic growth rates in households. So just what we're seeing across membership overall. Again, this is part of the sheer demand around fee-for-service because there are just so many clients that can't be served by AUM products and members that are growing like we're seeing 36% growth rates when the rest of the industry is struggling to literally struggling to get to one sixth of that growth rate like XYPN is growing at 36 in fee-for-service models when Schwab's brought advisor based can't get to six in client household growth. These are just enormous, enormous numbers in client household growth.

Alan Moore: [00:36:22] So do you really think. Just the fact that our advisors are serving non AUM clients. I can't get that. This is really just on the demand side. Is it that they just can't get access to an AUM advisor? Do you think it's also the niche focus of these advisors and just providing a much higher level of service and value to these clients? Is it that the clients are out there looking for retainer or advice only type fee structures that just don't have AUM or is it really just a combination of all the above at this point?

Michael Kitces: [00:36:57] I mean functionally I think it's a combination of all of the above. I think the reality is just look in part, members who have niches are growing well and members who don't have niches are growing well, which frankly just reinforces like, no, they're just like a demand issue here. Think again. The-the look, I'm not trying to knock the AUM model like it's very profitable. I'm part firm that does it like it's a good economic deal but it is very-very limiting about who can be worked with because they have to have enough assets liquid available, able to move and transfer them and willing to delegate them. And just we publish about this a bit on the Kitces site as well. Like you get down to 120 million households, only a third of them have at least 100,000 investable assets. Only about half of those have it liquid outside of 401k plan. Only about a third of those are actually willing to delegate. You go all the way through that math. You're in something like 7 to 10 million households that can do this and there's 300,000 advisors. So you go through that math and you're like 20 to 30 clients per advisor in the AUM model. Now most AUM firms have more than that because not everybody is doing AUM and some are still selling products. But this ongoing convergence, the AUM model, there really aren't enough clients, which is why you see across Schwab's entire giant base, only 5% client growth rates. And the irony for that, I mean, XYPN members are at Schwab and we're a non-trivial percentage of their members. So the irony to me, like if XYPN's own members weren't in the Schwab data, like their growth rate wouldn't even be 5%. It would be-it would be a little bit lower than that. We're bringing up the average, but there-there just aren't that many AUM households. There are even fewer left that are not attached to some advisor at some point because this has been going on for a long time. But there's literally tens of millions of households that show a willingness to pay for advice that have some financial wherewithal to pay for advice but don't want a product and don't want to delegate a portfolio or don't have a portfolio that's liquid and available to delegate. And so it's tens of millions of household potential and almost 1700 XYPN members. There just aren't enough. So as we may touch on in some of the later data in the benchmarking study, we do see the members that are more niche oriented, just running better businesses like they're growing faster. The non niche advisors are growing well, but the niche ones, they're growing faster, they're commanding higher fees, which lets them have better profitability and better practice economics. There's a lot of other dynamics around if you're going to go build this firm and you want to scale it up and run it profitably, the niche firms are outperforming the non niche firms, but there's such a demand relative to the availability that everybody's growing at just astronomically high rates compared to where the rest of the industry is. The only question comes down to are you going to run this particularly efficiently into a niche focus? And again, asterisk to all of it. Yes, there's a lot of demand. No, that doesn't mean when you hang your shingle on year one, a bajillion clients are going to come to you. It still takes a while to get known and trusted and liked and establish the marketplace, which is why we still see it. It takes five years for members to get to 375,000 of revenue, not two.

Alan Moore: [00:40:20] Yeah, that's why we started with that chart. We started with a bad -

Michael Kitces: [00:40:23] It still still takes time. It's still, good growth, still takes time to establish yourself.

Alan Moore: [00:40:29] And what I was alluding to earlier was this goal of 5000 advisors serving 500,000 consumers. If we take this data and sort of extrapolate it over the XYPN membership, I mean, this means in aggregate, XYPN members added something around 20,000 clients that are now being served by real financial planners that weren't being served 12 months ago, which is just awesome. That's just a cool feeling, especially. I mean, this is 2021 data. I guess we should have said that earlier. Like this is Jan 1 to December 31, 2021. No COIVD

Michael Kitces: [00:41:00] Yeah, not the best for a lot of firms from a growth environment. Yeah, this is in the middle of COVID.

Alan Moore: [00:41:05] And just to see that 20,000 client households now got to have access to real financial planning, that's-that's why we do what we do, right? I mean, we're here to help support the advisor starting, running, growing their business so that they can reach these clients. And it's just really amazing to see that in the data. We're going to jump forward to a couple of figures that we're going to talk about sort of at same time, figure ten and figure 11. But what these -

Michael Kitces: [00:41:32] Oh it's niche time.

Alan Moore: [00:41:33] It's niche time, which piggybacks on it was a good segway that you had there around just sort of how niche firms are doing. And so what figure ten shows is a two year growth rate for members that-that are joining with basically no clients, starting from scratch and whether or not they have a niche or not and how fast they're growing in each phase of the business. So what this shows is sort of if you're in the implementing phase niche versus non niche, how fast have you how much have you grown in the last two years if you're the building phase and then if you're in the scaling phase. And later figure 11 then breaks this down to actual revenue and operating margin. But it's really interesting because for the longest time our data showed that niche firms really did, do, I would say, less well, they did poorly in the early years, but it wasn't until years like four and five that the niche started really working. And then we've seen data, particularly last year, that showed really at all phases, niche firms were sort of winning in terms of growth rates. What we saw this year is that niche firms are sort of even, especially in the middle is sort of in that middle or built building phase and they really take off in the scaling phase. So Michael, do you want to talk about this?

Michael Kitces: [00:42:51] Yeah. So we have a couple of charts here that looks at sort of two core metrics. One is two year compound growth rates, which essentially was COVID. This was 2021 data, so year compound growth rates is like how you grew in 2020 and 2021. So non niche scaling firms through that two year

COVID window, we're growing, it grew cumulatively at 38%. Scaling firms that had a niche grew at 56%. So 38% growth versus 56% growth cumulatively over two years. You want to do that on an annual basis. You're talking about about 19 versus 28% growth rates. Now, again, at the at the size of the firms that we're talking about, like this is a half a dozen to a dozen additional clients who are paying thousands of dollars a year like this is tens of thousands of dollars of difference in each year's new revenue growth, which then adds and compounds as you-as you maintain the clients. The second thing that we saw going along with this and sort of the subsequent chart 11 if you're following along in the study, is we look at the average revenue per client of firms in the scaling phase that have niches versus not. And the difference becomes even more stark between the two. Firms that focused into in the niches are averaging 48000 per client, so about $400 a month. The firms that did not focus in the niches are at only 32000 per client. So a $1600 difference in revenue per client. Now, bear in mind, by the time you're in the you're in the scaling phase, you've got, by definition of how we do it, at least 75 clients. So you're talking about 100 plus thousand difference in revenue. Between scaling firms that are that have niches and the ones that don't, by the time they get out into the scaling phase, while they're also growing at 10% plus higher growth rates annually compounding. These make enormous differences in the efficiency of the business. And because just we have some level of overhead as a business, particularly by scaling phase, you're either ramping up your outsourcing or you're starting to hire internally. So there's a big cost difference as well to support these clients. And when you look at this on a profitability perspective, it's even more drastically different. The scaling firms that are focused in the niches are averaging 1900 dollars of profit per client. The firms that are not niche are averaging a little under $600 per client. So on a profitability basis, the firms with niches are literally 3x the profits per client as the ones-as the ones that don't have niches. I mean, these this is just an enormous profitability difference. And again, when you write when this is writ large across across the whole firm, like you're literally talking about $100,000 of difference in profits between the scaled up firms that picked a niche and the scaled up firms that didn't. And the challenge is the ones that didn't pick a niche and then say they want to go into the niche later. They can't because they don't have any room, because their client seats are all full of their non niche generalists, not efficient clients.

Alan Moore: [00:46:16] They can. It's just harder. But yeah, it's a challenge to make that pivot later on. And that's what we're seeing is really, I would say more industry, I guess more similar to industry surveys out there. But yet when you're- when you're looking at that no niche client or that advisor without a niche as they're getting larger, the profit margins are really getting compressed and we're going to talk about that here in a bit and sort of why we what's going on here in particular the types of firms and where they're at in their business. But I think this is a compounded impact of not having a niche, not being willing to-to charge what you're worth, not will not be willing to raise fees over time because you don't have the confidence in the value, because you don't have a clearly defined niche.

Michael Kitces: [00:47:02] It's harder to charge what you're-what you're worth. I mean, one of the data points that we've seen in the study, I mean, literally every year we've ever run the study is that firms with niches are much more likely to be able to charge retainer fees and charge significantly higher retainer fees when they do. And I think it just comes back to look, if you're a generalist that's operating on the AUM basis I mean, as long as the clients have dollars to manage, that's one of the services you provide. You can do that and it's reasonably profitable. But if you want to go out there and say like, I charge 200, 300 and $400 a month or more, like I charge five grand, seven grand, ten grand, like you want to say that number with a straight face and get clients to do business with you. You got to have a pretty compelling value proposition. I think just it's hard to do that as a generalist. You get back to like, well, I'm really smart and likable and I'm a good person. Let's build relationships together. And all those ways that we've tried to grind out new business growth over time versus a firm that says, well, you know, we specialize in tech employees that work in the New York City area. We're experts in their options. There are RSUs. We have an in-house tax service that prepares all the return and helps you navigate through it. And we built our own tools to be able to do the options analysis really, really efficiently and show you how to maximize your dollars, like clients picking that firm over a generalist. And that's anonymous, properly anonymous. That's one of our more successful members who literally has that offering that I just described.

Alan Moore: [00:48:33] Yeah, I always think it's interesting. Our fastest growing firms on the AdvicePay side and when we look at the data, they're most of the fastest growing firms have the name of their niche in the name of their business. Like they're just so, like, so niche.

Michael Kitces: [00:48:46] They name doctors, doctor, doctor wealth, techie wealth.

Alan Moore: [00:48:49] Yeah. Like it's amazing to-to see. I'm curious what your take on when you look at this data in the building phase. It's fairly even in terms of gross revenue and profit not non niche is just a little bit higher in that building phase of 20 to 75 clients. What do you make of it there? Is this just the-the niche firms haven't really raised their fees to be commensurate with their value because they're it.

Michael Kitces: [00:49:16] It takes a while to build into a niche you I'd-I'd written this article on the site years ago that basically it takes at least three years to build a niche just and I mean I've done this with now many different businesses that I built and I mean even across different parts of the industry. And it is disturbing how consistent it is that it takes three plus years for any kind of niche specialization to get going. It takes a while to iterate your offering just to really make it tight. It takes a while to iterate your marketing to really figure out your messaging. It just takes a while to get known in your space and actually have people trust like you're legit and you're here to stay and you're not just like the random person showed up one meeting and then who knows if the person's going to even stay around. I think it just takes several years and until you get there, I mean, the reality is, look, a member who starts and I mean, I think this is a common misperception, like members who start in a niche in day one don't exactly walk around saying like, oh, you're a doctor, screw you. And I'm walking away because, like, I only work with doctors. And if you don't have doctor in your in your name or on your business card, like I'm giving you the cold shoulder.

Alan Moore: [00:50:26] We encourage it. But yes, people don't always listen.

Michael Kitces: [00:50:30] You know, you take whatever you can get early on. I mean, just that's what most advisors end up doing. The question is, is not like if a client who will pay you great fees whacks you upside the head, will you take it like, okay, go for it. You want to get some revenue going because you're struggling. The question is, where do you put all your marketing energy and where do you put your focus? And in a world where it's still going to take you three years of like being immersed into the Architects Association and getting involved in the architect committees and sponsoring architect events and building relationships, the partners at architect firms before you can really like get your niche for architects thing going when you're in the early years, there's just not a big difference in what happens in-in firms in terms of their client growth, because the reality is niche firms are marketing more into their niche, but they're getting what they can get. And non niche firms are marketing all over the place and getting what they can get. So everybody gets what they can get early on. The question is like when your marketing starts getting going, when your firm gets traction, when you begin to get known for what you do and you start trying to increase your fees commensurate with that value, do you build marketing momentum and can you get higher fees commensurate with your value? And to me, that's ultimately what we're seeing in the scaling firm phase is the ones that have been niching all along start just like drastically pulling ahead by six figure levels of revenue and profitability because of the seeds that they were setting in the early years. While they basically had no material difference in the early years, like they weren't drastically better in the building phase, they weren't any worse. But once those seeds have been laid, you know, it's kind of like the farmer that plant seeds. Like you can't tell who's done a good job of planting seeds and those who have not done a good job planting seeds before the seeds begin to break through the surface. It's when they start growing and breaking the surface. You can tell really quickly who is doing a good job in farming.

Alan Moore: [00:52:30] No, it's a great point because our data does not differentiate those who are 100% niche versus those who are 50% niche. Have the marketing but still take clients that are outside of it versus those who don't have a niche. We're not-we're not able to gather that level of granularity. So it is a fair point that when we say niche versus non niche, it doesn't necessarily mean 100% of your clients are inside of a niche. And if you're at 99%, you're a non niche firm. It just it really points to the marketing. And you know what, what is many of our members are building, leveraging content strategies and just like what is that content strategy and that has a very long tail. And are you focused on the next should I open a Roth IRA article or are you focused on the next Here's what to do with those stock options at this particular company, kind of-kind of content?

Michael Kitces: [00:53:19] Well-well, notably our benchmarking study this year, we did actually have a couple of questions, just trying to understand like how-how-how niche are niche advisors. And so in-in the typical niche practice, seven out of ten clients are actually from the advisor's niche. So even amongst niche-niche advisors, almost a third of the clients were outside. Either you get an opportunity you don't want to say no to, or for many of them, like I said, yes to anybody early on I marketed to my niche, but I said yes to what I could get. And so they accumulate some base of non niche clients early on. But the niche focus is what creates the the acceleration in the growth by the time you get established. And-and we see that again in terms of both growth rates and the fees you can charge. And when you're growing faster and charge more like that's when you start getting six figure differences in profitability because the niche firms spent 3 to 4 years laying the groundwork and the non niche firms didn't.

Alan Moore: [00:54:20] Absolutely. So it sort of ties in with a conversation coming from Figure 12, which is sort of prospective conversion rates. So this is conversion rates of new prospects coming to advisors that are niche versus non niche firms. And we looked at what-what was the percentage of the new prospective clients that were qualified. So you get on the phone with someone, what are the chances that they're qualified? And what we found was that non niche firms, it was about 50%-about 50%. So you had a coin flip. When you get on the phone with a prospect or you're meeting with them, you're spending your time and energy with them. Half of them are qualified. Half of them were not qualified for your firm. When we look at the niche focused firms, that goes up to 64%, almost two thirds of prospects were qualified. Now, I think it's kind of obvious what that means and why that is, because they're going to your website, they're seeing themselves in the stories. They can see themselves in your niche, and therefore they're reaching out in order to engage with you. I think it'd be interesting to actually overlay whether or not people have their pricing on their website by niche or non niche, because.

Michael Kitces: [00:55:33] Yeah, we would love to know we didn't ask that question in the study this year.

Alan Moore: [00:55:38] Anecdotally, I think niche firms to have their pricing on their website because they're so clear on who they serve, they can get it specific enough and they can show the value proposition on the website the way non niche firms can cannot. But anyway, that's an aside, that's a guess. So just quality of-just quality of prospect coming in is significantly higher. But then we also looked at percentage of those clients that ultimately converted to either a monthly retainer, sort of an ongoing service or AUM and again, these numbers are a lot higher for non niche firms, 25% of prospects converted to a monthly retainer for niche firms, 34%. So almost 10% higher, 28% converted to AUM for non niche firms, 41%. So almost 14 points higher converted to AUM so we're getting higher quality prospects that are much more likely to convert, which again starts to speak to this long tail benefit of having a niche in Y in the later years. These niche firms are really starting to grow a lot faster.

Michael Kitces: [00:56:40] Yeah, I mean, just when you run this across month after month, year after year, clients after clients, these-these differences of like niche focused firms have 15% higher rate of-of being qualified prospects, 10% higher rate, 9% higher rate on closing monthly retainers, 14% higher rate on closing AUM client. When you start adding that up over time where you're getting as, as you get more established, dozens of new prospects a year, hundreds of prospects that you talk to cumulatively over 5 to 10 years. Like these differences again like these are six figure differences in the growth and momentum of an advisory firm. When you look at how this adds up over time, I mean, these are- these are really, really big differences when at the end of the day, there is just there is a grind to the business, there is a volume of prospects we're going to talk to. There's a volume of-of sales means we're going to have to try to get people to come on board. 10 to 15% differences writ large over time are kind of life changing for the trajectory of the business.

Alan Moore: [00:57:51] Yeah, those are big numbers. It's like, oh, it's only 10%. It's like 10% compounded is a really big number.

Michael Kitces: [00:57:57] Yes, Yes.

Alan Moore: [00:57:59] As we tend to cover

Michael Kitces: [00:58:00] As our clients live when we talk to them about the benefits of of markets like you, you tack on. Well heck, I mean we show clients the difference in what happens if you invest in a a moderate growth portfolio that gets seven conservative portfolio that grows at five, like try tagging on a 10% higher growth rate and watch how that compounds over a 5 to 10 year period.

Alan Moore: [00:58:22] Especially. It depends on the type of business that you're building, particularly if you're going to. I want to grow massive. Those compound rates matter, but also the when you're having much higher quality prospects who are paying you a higher fee per year, if you want to stay solo and you want to stop taking new clients at 40, 60, 80 clients, whatever that is, 50 clients paying you 4000 a year versus 50 clients paying you 10,000 a year, that is a drastically different income level for you, sort of as as the firm owner. So let's talk about that, because anyone who is at XYPN LIVE 2021 probably saw your keynote where and this is a topic we've talked about many times, which is really defining the different types of businesses you can build in our space and-and being really intentional about building the right business. I see too often I made this mistake myself where you think you're going to build a business one way and you end up building it the other way. And do you really like your business when it's built the other way? And so really helping people cement, sort of-sort of cement, what kind of business are they building. But we break the businesses out into sort of three groups we have solo, boutique, and enterprise. Solo is by definition solo. There is one advisor that is you. Technically, you could have a support staff, but for the most part, folks don't want to manage anybody. They might have a part time person. They probably outsource to a lot of different vendors because they just really want they want it to be themselves. They do not want to grow beyond themselves. On the flip side, you have the enterprise. These are the folks who want to grow big. They want a billion under management. They want hundreds of employees. They want to grow big. I think by definition, what I think it's 20 employees or I can't remember how we defined. Do you remember how we defined enterprise? Here was it was.

Michael Kitces: [01:00:14] It's not employee count. It's just a vision of what you're trying to build and scale towards.

Alan Moore: [01:00:19] So it's what you want to grow to, not necessarily, the data isn't showing necessarily where they're at today with those 20 employees.

Michael Kitces: [01:00:25] But it matters because you make very different staffing decisions if your plan is to grow huge versus not. And as we'll probably talk about a few minutes so we can see that very clearly in the numbers of solopreneur was run very different style practices and how they staff up then enterprises or boutiques do.

Alan Moore: [01:00:48] Yeah. So the enterprise, they want to grow really big and boutique sits in the middle where they don't want it to be by themselves. They do want to grow. We see a lot of these. Michael you talked in your keynote about these tend to be very mission driven advisors who many times just can't help themselves. They can't stop because they just want to spread their mission.

Michael Kitces: [01:01:05] It's-it's an interesting split. Like I almost find it's-it's sort of more straightforward to-to define the solopreneur Those of us who are solopreneur is this is much more of a like I make sure I say this the right way. I-I don't live to work. I work to live like I built my practice to serve me to generate a certain level of income so that I can enjoy a certain lifestyle and engage with a small subset of clients the way I want to engage with them to do the work that I want to do that's meaningful for me and to make the money so I can do other stuff. Most solopreneur members we see have a very limited number of clients. They might have 30, 40, 50 clients. Often it's not a lot higher than that because if you go a lot higher than that, you at least have to start hiring some support staff to build around you. Although from our definitions, like if it's you with support staff but no other advisors, you do still count as a-as a solopreneur in our model. But the key to, defining treat is if you're going to be a solopreneur or at some point you just hit capacity. I literally can't take any more clients because if I did, I'd have to hire another advisor and I don't want to do that. And so solopreneurs stop. At least by client count. Your income can grow because you can get new clients who pay higher fees and then wind down or lose some clients that pay lower fees. So your revenue and profits may go, but client count stops, boutiques don't stop, can't stop. It's that subset of us like I do this good thing in the marketplace and people pay me and they're referring me around. And more than want to want to come work with me and like I couldn't say no to them, solopreneur is like, Yeah, my life's good. I don't need to add more complexity by adding more clients. Boutique folks tend to have that mindset. Like, I couldn't say no, like I couldn't I couldn't stop here. Like I can't send them out. No one else will serve them the way that I do. Like I have to keep taking them, not doing it because I want to make like the big next big giant thing and be like the next Joe Duran or Ron Carson or whatever. Like just I can't stop. I can't say no to them. So I guess I'm going to continue building and hire some more advisors to try to make sure there are more people that can do this for the ongoing number of clients. And so those are the boutique firms. They kind of live between. I can't just stop at a certain number of clients, but I'm not trying to like grow the bejesus out of this to become the next mega firm because that's a whole other kind of roller coaster and investment.

Alan Moore: [01:03:30] I mean, said another way, I don't think we've ever really framed it this way, but really the solo is building a job for themselves. The boutique is really building.

Michael Kitces: [01:03:38] Really, really, really sweet, high income.

Alan Moore: [01:03:40] Great high income, flexible job. But it's a job. The boutique is really building a mission and the enterprise is really building a business. And that person, the folks who are building enterprises, they may or may not care about financial planning, candidly, they just they are building they care about building businesses. Now they're in the industry. They probably had some sort of connection to it. But like and their passion is building business.

Michael Kitces: [01:04:03] And you see it in the trade offs that start showing up. Right. And an enterprise builder will say, well, you know, we're having a little trouble scaling up the pace that we want. I think we're going to bring down our advisor standards a little. We're going to start hiring some people with a little less experience and less credentials. You know, we may take a little bit of a hit and in slightly lower growth rates and lower client satisfaction rates, but that's what we got to do to get through this growth cycle. Boutique firm is like, we can't compromise our standards. That's blasphemy. Like just you can't do that. It violates who we are. And again, I'm like, I'm not trying to knock enterprise firms as though it's all about like having low standards or sacrificing your standards. But like, if you're trying to scale up an enterprise, you may have to make those decisions sometimes. And just that's one of the levers you pull when you make business compromises to make business decisions, boutiques when you're built around a mission like you don't compromise that stuff. And that's part of the distinction that just it's a-it's a mindset and mentality difference around how you approach the business.

Alan Moore: [01:05:06] So it's really important that we differentiate because with these next charts, what we're going to talk about are for our scaling members. There's going to be a lot of terminology or for our scaling members. You have hit 75 clients, you have grown to that point. We then bucket into solo, boutique, and enterprise, and what we're looking at is productivity numbers, which are which are really great measures to sort of be able to compare across advisory firms to see how are you doing from a staff productivity, from just an overall revenue per advisor, revenue per staff. And then we'll talk about the cost here in a second. There is this misnomer, and we have said this for years and people I don't think people believe us, but people think, Well, when I go from solo to boutique, I'm going to make so much more money. That's how you get that's how you get wealthy is you start to hire. And what the data says is that is the absolute wrong answer because our advisors solo advisors, revenue per advisor, which by definition there's only one, is on average $700,000 of gross revenue for solo practices that are at scale. Boutique is 300,000, less than half, and then enterprise crops back up to 430,000. So just the revenue by advisor. What this means is you've hired a bunch of advisors, right? You're hiring more advisors, but your revenue is not scaling as fast.

Michael Kitces: [01:06:32] You're hiring advisors ahead of the revenue because you have to do that, right? Like if I'm look at my ideal world is like I've got 80 clients, two staff members that support me and like we just crush on those 80 clients. I'm good, like I got my 80 clients to do my thing. If I'm a growing scaling boutique, like I-I can't have one advisor serving 80 clients because then if I get the next 10, 20 clients, they're going to quit because they're going to be drowning. Like, I've got to have two or three advisors that I've got enough capacity and more people out there doing business development and then more people taking on new clients and distributing the new client load, which means if I've got the same number of total clients in revenue, I've got to have two or three advisors instead of one, which basically chops my economics in half or worse.

Alan Moore: [01:07:18] And your take home really goes down with it. Now, that may be the business you want to build. We're going to talk a little bit more about this, but as the enterprise, as folks are starting to build enterprise firms, we are seeing them have about, almost 50% higher revenue per advisor versus the boutique. So not as high as the-as the solo, but it's just a really interesting it's a really interesting number. And the same thing shows up in revenue per staff. So this includes employed as well as outsourced because the solos are hiring sometimes or are outsourcing to various providers. And basically the numbers reflect the same, which is revenue per staff is 230,000 in the solo practice, 115,000 in the boutique at 130,000 in the enterprise. And so -

Michael Kitces: [01:08:08] And so, that's good to frame just in context. So if if an advisory firm has 700000 dollars of revenue. So we got whatever, 125, 250 clients are charging four or five grand apiece. If we're supporting $700,000 of revenue, a solo firm is typically three people. That's usually the founder and one or two support. And the typical boutique or enterprise is six or seven people to support the same amount of revenues, like same amount of money coming in. Twice as many staff members just to support the same amount of-of revenue. And part of that is depth of service. And I've got, not even depth of service, like depth of room to scale and grow. I need more infrastructure, I need more capacity. Now of course, if you add more people for infrastructure and capacity, then you also have to hire people to manage people because now there's too many people for all of them to report to you. So you have to start adding in the-the overhead infrastructure that comes when you begin to grow and scale a business. And so all of that is showing up very clearly here in the metrics of these firms. But per your point earlier, Alan, around like the economics and profitability, like the boutique firms are not on a path to making more money any time soon. To put it mildly.

Alan Moore: [01:09:37] Yeah. You make a good point there that if you just look at sort of what it's taking to service the revenue is that the enterprise firms are making the decision to hire more support staff, fewer advisors, boutique firms are hiring more advisors and fewer support staff because in the end the revenue per total team member is fairly level, which means they are making very different hiring decisions in preparation for growth.

Michael Kitces: [01:10:01] And boutique firms tend to start hiring up advisors. Enterprise firms, because if you're really focused on scaling up, you're focused almost out of the gate into how do we maximize our value, the value of our advisors, how do we maximize their time and productivity? So we tend to staff more around the advisors instead of just putting more high touch advisors the way boutiques tend to.

Alan Moore: [01:10:24] So I'm not sure if I said, but that was that was figure 29. Tied to figure 29 is figure 35, which is average profitability per client in these different business types. And so what this graph looks at is revenue per client, which we'll talk about. So we got revenue per client, expenses per client netted out, you get operating profit per active client. Now the revenue numbers are not drastically different. They are a little bit different. But we are seeing solo practices commanding a higher fee than boutique, which is commanding a higher fee than enterprise. So your solo, about $5,700 per client of fees boutique is 5200, about $500 less or 10, 9% less. Enterprises are about 4200 of revenue per client, so about 1000 less than a boutique, about 15 to 1600 dollars less than your-than your-than your solo. But there's some variability, but not huge. But that might speak to what you're talking about earlier.

Michael Kitces: [01:11:24] No, I think this is notable because to me, there's a perception, because I've heard it from advisors when the the biggest practices with the most team and resources attract the most affluent clients. And so -

Alan Moore: [01:11:39] This is true.

Michael Kitces: [01:11:39] You know, big enterprises should attract bigger clients. And like those, those tiny solopreneurs, they're only going to get little clients. And so to me, like it's striking when we look at the actual data, it's the reverse. It's upside down of that. It's the solopreneurs that actually have the highest average revenue per client, and it's the enterprises that have the lowest. And now, to be fair. Part of this is about which clients you can attract. Part of this is about which clients you accept. Right. Solopreneurs have to be focused. They have the most limited capacity and they're not adding capacity. So the only way you grow as a solopreneur is you have to focus on getting very, very high quality clients because there's only a couple of seats on that bus. And that's exactly what we're seeing here. When you're an enterprise and you're focused on scaling up and you want to achieve certain fast growth targets in order to scale up over that time horizon, you can't wait for the best fit clients. You've got to pretty much take anybody that's reasonably close to the neighborhood. And so you end up being forced to compromise on client standards to some extent, and that starts to drag down average revenue per client. And just that's part of the nature of this trade off. Solopreneur is, can-can just focus on my subset of really high quality clients that pay a great fee to work with me. Enterprises are focused much more on taking in a wider range of clients to maintain their growth pace. Because you've got you've hired all these people for capacity. You're staffed twice as many people as the solopreneur for the same amount of revenue. You better be growing faster to make up for that. But in order to do that, you may not be able to get the strongest clients. You've got to start compromising client standards and taking anybody in that you can or not anybody, but having looser standards than solopreneurs that manage their capacity more delicately.

Alan Moore: [01:13:31] And then that shows up where revenue is higher in the solo down to the enterprise. But it's about a 1500 dollars difference per of revenue per client per year. When you look at expenses, though, it is upside down when it comes to the boutique firms in particular, solo practices spend in total expenses per client about 8000 hundred dollars per year. Remember, they earned 5700, they spend 1800. The boutiques are earning 5200, but spending 4000 enterprises are at 4200 revenue spending 2500 in revenue or I'm sorry, 2500 expenses. So when you look at operating profit per active client solos are at $3,900, boutiques are at 1100 dollars, enterprises are at almost 8500. So solos are net income. When you look at operating profit, net income to the business owner, solos are earning three times, over three times the net revenue as boutiques.

Michael Kitces: [01:14:37] Yeah, and just worth just putting this into dollar terms again, scaling firms by definition have at least 75 clients. So if you want to put these in the dollar terms, the average solopreneur in the scaling phase or like even average, solopreneurs in the scaling phase are making a minimum of 292,000 of profit and at the same 75 clients, the boutiques are not even clearing 100,000 of profit. They may have 700 plus thousand of revenue, but they've got $600,000 of costs associated with it. And so they're-they're clearing a third of the profits in actual dollars on a similar amount or per similar revenue unit per client unit. I mean, these are these are just drastic differences. And to me I think is particularly highlights. What I would almost venture to say is kind of an emerging concern to me around the benchmarking study here. Look, I would expect solopreneurs to have the highest revenue per client and the highest profit per client. Just you're very lean, you're built up around yourself. You don't have to staff a lot of other, frankly, relatively expensive advisors. You don't have to staff for additional capacity because once you get to mature practice, just you got your ideal clients. You don't have to staff room for more. And so high income, high profit makes a lot of sense. And just we're seeing huge like hundreds of thousands of dollars of income advisors in this model. Enterprises, lower average revenue, higher costs, lower profit. No surprise, like you want to scale up as an enterprise, you're going to take out less and you're going to put more in and you're going to push the growth pedal a little bit harder. And so those metrics shift. The concerning thing to me looking at these numbers is boutique practices. Boutique practices, ostensibly by any kind of classic business measure, really should fall somewhere between the solopreneur and the enterprises. They're not trying to grow as fast, so they shouldn't need to invest as heavily, but they are trying to grow and scale up a little further so they shouldn't be as profitable as solopreneur. What we see is very different, though. What we see is boutique practices have drastically higher costs, even then scaling even then enterprise firms. And we can see where it's coming from. It's not because their total staff count is different, it's that their revenue per advisor is much lower, which essentially means that the, what we're seeing in the data here is boutiques are hiring advisors too fast. I mean, they're to say the least, they're high in the room very fast. But the implication here is they're hiring them too fast. The firms that want to grow huge in enterprises are still not hiring advisors as fast as boutiques. And I think just the what this really raises is sort of a question and concern is it really looks like boutique firms are frankly focusing too much on hiring the next advisor and not enough on the-the admin and operational support staff to leverage the advisors that they've got. Or in other words, basically they're-they're hiring very expensive advisors to do operations and administrative tasks that other firms are figuring out how to staff with much lower cost staff that don't cost what an advisor costs.

Alan Moore: [01:18:04] I'm really interested to see this data over a couple of years because, I mean, I can tell the story that, Hey, I'm a boutique, I'm going to get to three advisors. That's my vision, and then I'm going to build out all of the support staff infrastructure. I'm going to see those numbers change and that's fine. If that's your long term vision and you've got to and you've got a path there. But I think it's really telling that the folks who are building businesses for the-for the more of the core purpose of building a great business are hiring advisors at a much slower rate. And again, I can tell a story. You're at a conference, you meet someone who has a passion for your niche. They have experience in your niche, whatever. They bring something unique to the business. You just you can't not hire them. I mean, it's your mission. This is what you want to do. You found somebody else who's your kindred spirit. You have to bring them in now, but you got to be able to afford them. And maybe you're going to build out that infrastructure. Maybe you're planning on leveraging virtual assistants or outsource support or whatnot to be able to start scaling up. But I agree with you that it is concerning that I'm interested to see this over time whether or not boutiques hire a couple and then stop or do they stay in this perpetual cycle of over hiring advisors.

Michael Kitces: [01:19:14] But if you're-if you're a boutique and you feel like the firm is growing pretty well, but geez, there's just not a lot of dollars coming out of the business yet. We recognize that this may be maybe why. Just the nature. It is an interesting distinction. Solopreneurs don't hire up a lot of staff. So frankly, the staffing decisions are relatively straightforward. It either leverages me and I want to manage it or I don't. Enterprises tend to build with a very long term hiring roadmap in mind, and so they are very focused on systematizing and scaling from the start. Boutiques, I find just in practice, knowing a lot of our boutique members over the years, like we're not looking at it as a business. I didn't get into this to build-build a big business and scale it up into enterprise like I'm doing because I've got a mission of serving certain people and I want to see people serve a certain way and maybe I want to create opportunities back to the industry as well. But it's still really important to make sure you're making good decisions for your business. And to me, like the concern that crops up when I see numbers like this is. Whether some members that are running boutique firms are you know, they're so caught up in their mission, they're literally sacrificing their own business, economics and profitability in order to do it. And look, it's your business and your mission. So if you want to do that, you can do that. But if if your big focus is creating opportunities for young advisors, like maybe instead of running a marginally profitable firm, you can run a more regularly staffed firm and like donate a $50,000 scholarship somewhere, it'll actually be cheaper than hiring advisors to create capacity you don't actually need and effectively over staffing and air quotes over staffing the firm because that's really the implication of what we're seeing in the-in the data here is that boutique firms appear to be starting over staff on advisors. They're hiring advisors sooner than they really need advisors when what they really might need is just some admin operational support.

Alan Moore: [01:21:22] So good thing for us to keep an eye on. Interested to talk to some advisors who are in this position. This-this recording comes out after #XYPN LIVE in Denver here at the beginning of October, but we'll be at the conference sharing, talking about a lot of the same data and we'll be great to have some conversations with advisors to hear if this is their experience. Is this what they're dealing with? How do they think they're over hiring? What's the story they're telling themselves? What are they seeing in the marketplace. In terms of why are they making some of these decisions? And again, over the course of 2 to 3 years, I can see these numbers normalizing. I can also see these numbers staying this way and becoming a real pain point for folks who are just working their tails off, doing way more work because they actually grew a business and now they have employees and staff and HR issues and all those things and not making any more money or making way less money than if they had just stayed solo. And and again, that's the story I mainly hear. I don't generally meet people who accidentally built a 100 employee business. I do hear the well, it was just me and I was doing really well. And then I brought on a couple of advisors and now I hate my company. And so that's generally.

Michael Kitces: [01:22:32] I don't serve clients anymore. I just manage people. And I actually did this to work with clients, not manage people.

Alan Moore: [01:22:38] Yeah. And I make way less money and I do the, I'm not doing the work I love as much. So it's something for-for everyone to be really aware of. Again, building the business that-that works for you and really where you're at in your life so. Well Michael, thank you for coming on. I know you just can't resist coming on and talking about data, but yeah.

Michael Kitces: [01:22:59] You lured me with data as you do every year.

Alan Moore: [01:23:01] I love-love being able to go through this to really give a fair and accurate, independent, objective opinion and picture, I should say, of where our members are at, how they're growing their businesses, decisions they're making. Members do have access to the benchmarking study. They'll be able to see all of this data and sort of compare. Now, it's not just about being the best, just because some of these numbers are higher than where you're at, that's okay. Again, there's a bell curve that we-we don't want this to be a 300 page report showing every percentile for every single thing. Candidly, we don't have enough data sometimes to be able to show that. But hopefully it gives you an idea. It gives you something to benchmark of and off of and be able to make good decisions about your business. And if you're thinking about getting started, hopefully this you've taken-you've heard us sorry, we're not here. We are in the business of helping people start their firms and we are trying to talk you out of starting them too soon. All right. So listen to us. Let us know

Michael Kitces: [01:23:58] Apparently, we're-we're trying to talk you out of hiring new advisors.

Alan Moore: [01:24:02] Yes. And I apologize for those who are looking for jobs. We are as conflicted as it comes when it when it comes to convincing you to start a business. And we really do want you to have a realistic picture because I'd much rather you join in two years and be successful because you've gotten yourself where you needed to be then join today and ultimately not make it because you weren't quite ready. So again, Michael, thank you for taking the time to come on the show.

Michael Kitces: [01:24:25] Absolutely. My pleasure. Thank you, Alan.

Alan Moore: [01:24:30] We hear it every day: compliance is overwhelming for independent financial advisors. That's why XY Planning Network offers three compliance services to get you the support you need. Let our experts become your experts through our Initial Registration Service, designed to help you navigate your initial state or SEC registration. Get your firm up and running with our Ongoing Compliance Coaching to hone your compliance program so that it grows with you. Want both? Our First Year Compliance Foundations service helps you build a custom-tailored compliance program while you get your firm registered. Go to xyplanningnetwork.com/compliance101 to get the compliance support you need and let us take the guesswork out of the process.

Alan Moore: [01:25:12] Also, be sure to go to XYPlanningNetwork.com/VIP to join our private Facebook group for fee-for-service advisors. It's the community you've been looking for that's there to support you no matter where you are in your journey—best of all, it's free. Again, that's XYPlanningNetwork.com/VIP.

Narrator: [01:25:31] Thanks for listening to XYPN Radio. If you enjoyed the show, please be sure to leave a review that will help grow the movement of fee-for-service advisors, serving next gen clients and building the firms of their dreams. That's all for today's episode, until next time.