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SENIOR CONSULTANT

The Voice of the Investment Management Consultant

Building Your Practice Around A Plan

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The investment management consulting industry is growing almost exponentially as thousands of brokers are beginning to evolve their books toward consulting. All too often, brokers in moving their business into investment consulting neglect to do what they always advise their clients to do: have a plan. Whether you are new to consulting or have an established practice, it never hurts to have a framework around which to build your business. Consulting is a business, a service business, where the end product is valuable investment advice provided to long-term investment clients. Like all businesses, it has costs. In a brokerage firm, most of the operating costs are covered by the firm in exchange for the firm's portion of the fee; while with independent contractors, many of the costs must be borne by the consultant. Needless to say, it is essential for the independent consultant to understand what those costs are and to keep tight control over them.

The biggest "cost" in a consulting practice is the primary resource for that practice: you and your time. Unfortunately, while your energy, knowledge and expertise may be truly unlimited, your time is not. There are so many hours in a day, a month or a year, and it is critically important that, to achieve your goals, you have a plan as to how you are going to use those hours.

THE BIGGEST "COST" IN A CONSULTING PRACTICE IS THE PRIMARY RESOURCE FOR THAT PRACTICE: YOU AND YOUR TIME

In order to build a plan, you must do the math. Start with the basic questions: What is my income goal? How should I price my services? How many hours per quarter does a client need? How many clients can l serve effectively? Let's start with some basic assumptions. In round numbers, there are about 250 working days in a year. Given eight working hours per day, that totals 2,000 working hours a year. Assuming that half of those hours are devoted to activities other than client service, most importantly, to acquiring new clients and assets, then 1,000 hours per year or 250 hours per quarter are available to serve your existing clients.

Let's also assume that you want to earn a minimum, before taxes, of $200,000 per year from your consulting activities. That's easy: $200,000 divided by 1,000 hours is $200 per hour. The problem is you don't charge by the hour for your services, the way a lawyer or accountant does. You have to look at it a different way.

In order to get your $200 per hour, or $200,000, you need to gross $500,000 per client, assuming a 40% pay-out. Let's also assume, for discussion purposes, that after all expenses, the independent consultant will also keep 40% of the $500,000.

You now arrive at a pricing issue. What are you worth to your clients? You don't have total independence there, because the competition will impose constraints on your pricing ability, but within a reasonable range, you need to decide what a client should pay for your services. Current practice indicates that the average $500,000 client pays a fee of approximately 2.4% and the average $1 million client pays approximately 1.9%. From those numbers you must subtract the manager's fee (assume 50 basis points) and the "program" fee, internal or eternal (assume 40 basis points). That means the average $500,000 client is going to pay you 1.5% gross, and the average $1 million client is going to pay you 1.0% gross.

Going back to our assumed 40% pay-out or retention, that means you will receive 60 basis points from the $500,000 client and 40 basis points from the $1 million client. That translates into pretax income of $3,000 and $4,000, respectively. If, indeed, you need to earn $200 per hour to achieve your income goals, then that means you have available 15 hours per year (3.75 hours per quarter) for the $500,000 client and 20 hours per year for the $1 million client. Is that enough? Can you provide sufficient, effective consulting advice to your clients within those timeframes? Leaving aside the first year, which always requires more of your time in order to establish the client's investment plan and select the managers, will the client feel he or she is receiving value in return for fees paid?

Continuing with the math, if your average client is $500,000 and is paying you $3,000, you need to have 67 clients to achieve an income of $200,000. If the average size of your client is $1 million, then you only need 50 clients and can afford to devote more time to each of them. This can go on and on, but that is not the intention. What is important is for every consultant to develop a business plan and, once developed, execute that plan. Only you can divide how many clients you can appropriately service, how many hours you are willing to devote to being a consultant, how many dollars of client assets you need to achieve your goals, what your target average client size should be, and finally but most importantly, what your minimum acceptable income is in context of all these questions.

But one closing thought is perhaps more important than all the others. With the average broker at a major wirehouse having $50 million under management, there are tens of thousands of brokers who already have more than enough qualified clients to make the transition to investment management consulting. Remember, whether you target $200,000 or $1 million of income, this recurring fee revenue comes in year after year, if you serve your clients well. The difference in consulting is that you provide a much higher level of service, investment counsel and value in managing all of your client's assets than in trading a small portion of it. You also have more time for your clients as the number of accounts you manage is a small fraction of that required in commission brokerage.

Investment consulting is an excellent profession. It will be even more rewarding if it is approached, like investing itself, in a logical, objective and well-thought out manner. So, make a plan. ■

About the Author

John Daly is director of marketing of Spears, Benzak, Salomon and Farrell and is agilely involved with the leading investment management consulting initiatives within the industry For more information, call 212-903-1230.

Business Plan Model

How To Earn $200,000 A Year in Building An Investment Management COnsulting Practice

Managed Account Investment Strategy

Gross Revenue	$ 500,000	$ 500,000
Less: Firm Retention at 60% or		
Operating Expenses at 60%	$ 300,000	$ 300,000
Targeted Earnings	$ 200,000	$ 200,000
Fee Structure:		
$500,000 Average Account	2.40%	N/A
$1 Million Average Account	N/A	1.90%
Net Fee Earned:		
Average Fee Charaged	2.40%	1.90%
Less: Manager's Fee at 50 Basis Points	0.50%	0.50%
Less: Program Fee at 40 Basis Points	0.40%	0.40%
Adjusted Fee Charged	1.50%	1.00%
Less: Firm Retention at 60% or		
Operating Expenses at 60%	0.90%	0.60%
Net Fee Earned	0.60%	0.40%
Average Revenue per Client:		
Average Account Size	$ 500,000	$1,000,000
Times Net Fee Earned	x 0.60%	x 0.40%
Average Revenue per Client	$ 3,000	$ 4,000
Number of Clients Required:		
Targeted Earnings	$ 200,000	$ 200,000
Divided by Average Revenue per Client	÷ 3,000	÷ 4,000
Number of Clients Required	66.6	50.0
Assets Required:		
Target Earnings	$ 200,000	$ 200,000
Divided by Net Fee Earnings	÷ 0.60%	÷ 0.40%
Assets Required	$ 33,000,000	$ 50,000,000
Number of Existing Clients	______	______
Number of Qualified Clients		
With Investable Assets of $500,000 or More	______	______
With Investable Assets of $1 Million or More	______	______
Number of Qualified Accounts	______	______
Number of New Accounts Required	______	______
Number of Clients Required	______	______
Less Qualified Accounts	–______	–______
New Accounts Required	______	______

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