The impact of e-commerce on UK financial services product providers and their intermediary relationships

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Abstract The UK financial services sector is undergoing a period of profound change, including the advent of e-commerce, intermediary depolarisation, coupled with demographic changes and Government regulation. This paper explores the nature of these industry trends in relation to UK product-providers, mainly pensions and life assurance product-providers and their most important organisational stakeholder, the independent financial adviser (IFA). It discusses how this relationship has evolved to date and recommends how UK product providers might restructure their operations in light of the industry trends.

Keywords: *life insurance; pensions; distribution channels; independent financial advisors; stakehold pensions; 1% world; ageing population; advice; depolarisation; multi-channel distribution; e-commerce; Internet; business models*

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Introduction

The financial services sector has been revolutionised to become a more technologically driven, fiercely competitive service-oriented market.[1] Financial services are increasingly regarded as quasi-commodities that serve a complex market in which organisations of markedly differing business models use diverse marketing strategies and different technologies to service a multitude of consumer segments. Technology is now facilitating cost-effective mass customisation.[2] This is reflected in the customisation of the ideal product, the aggregation of services, the targeting of the right product for the right buyer, immediate transactions and the availability of progress information.[3]

The Internet has virtually eliminated the information arbitrage opportunities that many financial services firms have traditionally relied upon. The number of online users of financial services is increasing. In terms of the distribution of financial services business, IFAs and direct sales operations still handle the largest proportion of transactions but it is anticipated that the Internet has 17 per cent while ATMs/call centres and point-of-service venues will account for 12–13 per cent by 2003.[4] These statistics illustrate the importance of new technology to the future of global financial services and implies that in order to prosper, significant changes in strategic thinking, market organisation and consumer understanding are required.

In the New Economy, consumers have (for a price) the same access to the information sources as intermediaries (ie IFAs) and therefore need not rely on their 'expertise' to locate the best financial opportunities eg over 10 per cent of the UK population searched for financial products online.[5] This implies that consumers now want customised assistance in analysing requirements, the reassurance of strong brands, and the convenience of straight-through processing (which means that information is entered once and used throughout the decision-making, transaction and servicing process without human contact interfering with data integrity, leading to fewer mistakes, less duplication and efficiencies in data storage, sharing and processing).

Consumers also want better access to financial intermediaries and an all round more intuitive customer experience. However, Forrester research indicates a much larger percentage of online users are only browsing for life assurance or investment products than are actually purchasing online. Furthermore, 23 per cent of users have searched for financial services online, while only 2 per cent have purchased.[6] Accordingly, with regard to the three stages in the overall sales process — namely research the marketplace and provide generic information, understand clients' needs and offer advice, consummate the sale — only the information search process currently adds value despite being a commodity.

UK product providers in evolution

The evolution of business models

There is no doubt that e-commerce and e-business is changing the marketplace by transforming how firms conduct business, stakeholder relationships and market structures.[7] An organisational business model expanded to encompass the nature of e-business may be defined as 'a collaborative enterprise that establishes a close partnership amongst its stakeholders, employees, customers and suppliers, leveraging technology to minimise distance between its business and its partners and to automate transaction processing, strengthen relationships and reduce costs'.[8] This definition suggests that organisational boundaries are becoming less distinct and increasingly flexible to accommodate a wider network of strategic partnerships.[9] The advent of e-commerce allows companies to reorganise themselves in a virtual context. Many traditional business models have been successfully adapted to the online world eg the subscription-based content provider, direct marketing, free trial and a number of new models such as the freeware model, information barter, access provision or active service provider model.[10]

Product-provider business model design

UK product providers operate both business-to-business and business-to-consumer models. Thus, Scottish Amicable acts as the business-to-business division of the Prudential and so deals mainly with the independent financial adviser market. Other examples include Scottish Mutual as part of Abbey National plc or Scottish Equitable as part of the Dutch conglomerate Aegon. However, companies such as Standard Life or Fidelity Investments act as a single entity serving both consumers directly and professional intermediaries.

There are three main channels of distribution:

- Tied agents, who are contractually obliged to sell the products of the parent company.
- Direct channels such as telesales or direct selling has traditionally been a key distributional channel although use of sales forces is declining due to cost inefficiencies. For example, Prudential has recently significantly reduced its direct sales force.[11]
- The intermediaries ie independent financial advisers (IFAs) is a key distribution channel which is increasing relative to the others as the proportion of business transacted through IFAs has increased from 38 per cent to 54 per cent.[12]

These channels of distribution are serviced by several delivery mechanisms such as branch networks, call centres, internet portals or digital TV.

The impact of e-commerce and Internet technology

E-commerce and the Internet have had a significant impact on product providers' business. According to Datamonitor (2000)[13] online banking is the most popular financial service in the UK. Figures 1 and 2 illustrate online financial services behaviour.

This graph shows that there is still a big discrepancy in terms of the product category viewed via the Internet. This should come as no surprise as there remain significant differences between bank accounts/credit cards and personal pensions. This suggests that there is a clear need for research into the category of product most suitable to be viewed and transacted over the Internet. Indeed, the distinction between valuations and actual transactions is crucial because as the next graph demonstrates, consumers appear to currently use the Internet for viewing financial information and data etc as opposed to transactions. Figure 3 shows the factors that consumers value in financial services.

This figure controversially claims that consumers may be more interested in the provision of accurate information and prompt service than personal attention. However, the balance of personalisation and functionality is a complex issue that product providers have yet to resolve.

The independent financial adviser marketplace

IFAs represent a significant distribution channel in the UK financial services sector, as there has been a 33 per cent increase in new life and pensions premiums from £3.9bn to £5.1 during 1995–1999.[14] It is anticipated that the importance of the IFA as a key distribution channel will continue for several reasons. First, by 2005 over 5m people will have investible assets over £50,000 with aggregate wealth growing from £680bn to approximately £2 trillion.[15] Secondly, the increasing complexity of financial products implies a need for independent advice on a personal level, for example, there are now over 1,200 different ISA plans available to consumers. Thirdly, the increasing emphasis on personal financial responsibility, decreasing State provision and the increasing interest in share ownership further re-emphasise the need for advice. Finally, there is also an increasing recognition on the product-provider side that the use of a widespread direct salesforce is more cost-effectively utilised in conjunction with IFAs.[16] The IFA sector employs around 50,000 people with around 9,000

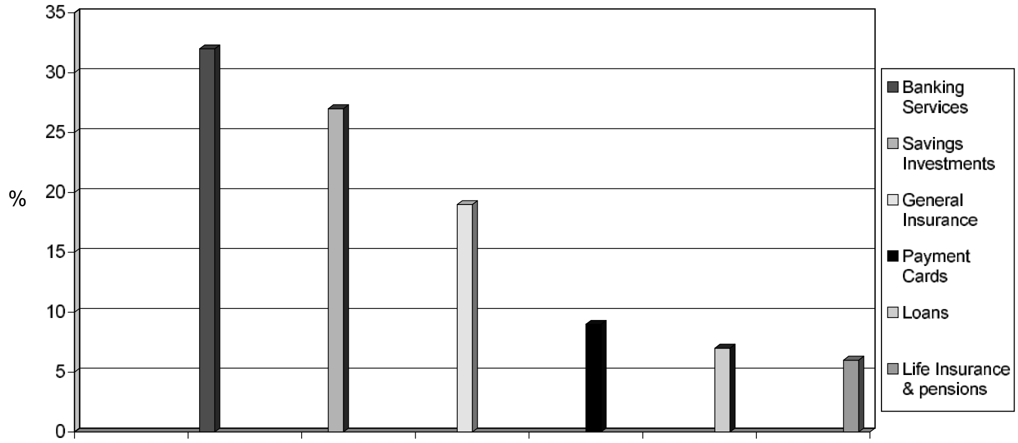


Figure 1: Financial Services browsing by Product Group — Datamonitor (2000)

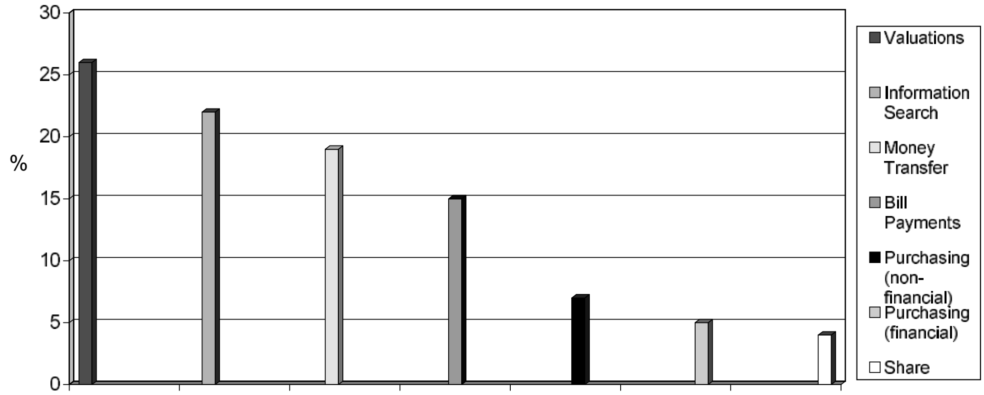


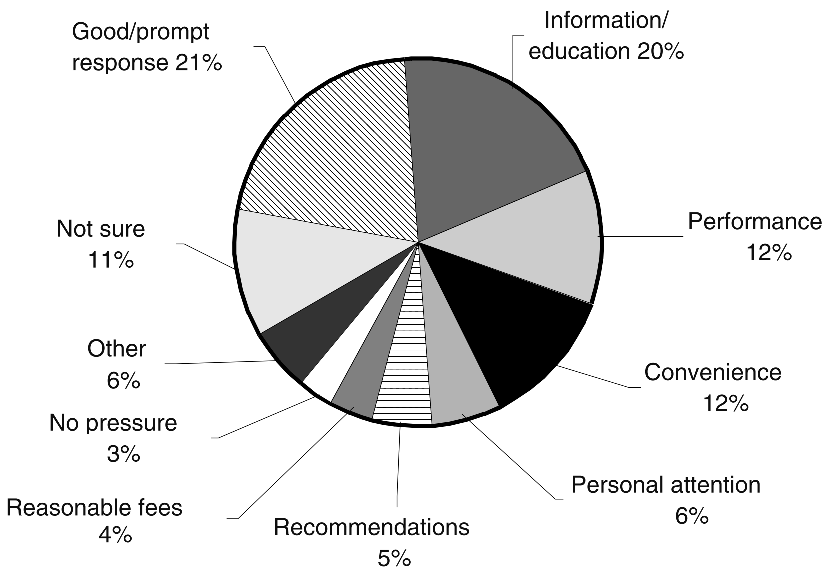
Figure 2: Popularity of banking services — Datamonitor (2000)

IFA organisations — the vast majority (in excess of 80 per cent) are SMEs. IFAs handled £25bn of new, medium and long-term savings business in 1998. It is estimated that by 2005 IFAs will account for over £2bn of GDP.[17] IFAs have become increasingly important in providing investors with impartial advice and are now responsible for approximately 60 per cent of the market in many business categories.

IFAs fall primarily into four main categories:

— National IFAs (eg Towry Law, Inter-Alliance)
— Networks (eg DBS & Burns Anderson)
— Large regional IFAs (eg Aitchison & Colegrave Group)
— Small IFA sector.

A constantly changing marketplace presents significant ongoing opportunities for IFAs able to adapt their marketing strategy quickly and efficiently. For example, consider the current UK political drive to make individuals responsible for their own financial arrangements.[18] This emphasis on financial independence coupled with demographic trends such as the



Source: IBM Consulting Group survey

Figure 3: What customers value in financial services — *The Economist*, 18th May, 2000

increasing elderly population, ie 'grey market', the increase in proportion of people pursuing professional and managerial careers, the increase in financial literacy plus associated increases in inherited wealth present significant opportunities for personal financial planning.[19]

The IFA sector growth has been higher than the national average for 15 years and is anticipated to grow faster than the economy for the foreseeable future.[20] Accelerating technological development, continuing changes in regulation, introduction of stakeholder pensions and an increasing emphasis on client servicing and retention together with a 1 per cent charging structure leading to lower profit margins for both product providers and IFAs are seen as the most important influences on future trading conditions.[21] The marketplace presents major opportunities for IFAs who can not only offer a comprehensive range of investment, tax shelter and financial planning services, with the emphasis on wealth management, client service and relationships but as importantly, are structured and managed on a professional basis.[22]

New virtual competitors and intermediaries

Although dot.coms are not replacing existing market players, the number of Internet trading firms has rocketed from 12 in 1996 to 170 in mid-2000.[23] Established companies such as Prudential (Scottish Amicable as IFA provider), Abbey National (Scottish Mutual as IFA provider) are using multi-distributional channels to emerge as formidable competitors in the financial services market eg companies such as American Express subsidising the cost of online dealing. UK players such as Motley Fool, IFAonline and FT.com are now offering free investment research and are consequently significantly altering traditional lucrative market positions. Traditional players are increasingly modifying business models in light of these pressures whilst barriers to entry are simultaneously declining. For example Inter-Alliance, a leading IFA is now transacting business online in conjunction to traditional face-to-face sales processes. A further example is an international product-provider that has just launched a new product-provider operation, which intends to deal with IFAs solely via the Internet.

The UK independent financial advisers perform an important role, though it is unclear how this role will change as market forces affect their business model design, remuneration models and intermediary functions. E-commerce, e-business and the Internet have led many industry commentators to suggest the demise of the intermediary.[24] It is suggested that the proliferation of information, the increasing sophistication of consumers and increasing direct communication between buyer/seller implies that the added value role of the future stereotypical intermediary is limited.[25]

The evolution of the intermediary

The traditional intermediary plays an important role in the function of contemporary markets, indeed according to Jallat[26] this role may be categorised into four separate functions.

- *Aggregation*: Intermediaries bring together a number of buyers and negotiate business on their behalf with seller(s). This achieves economies of scale, cuts costs and increases the bargaining power of buyers.
- *Trust*: Intermediaries introduce a middle ground that protects both sides. This creates a common, fair trading platform from which an intermediary may charge a premium.
- *Facilitation*: Information transfer across value chains may be complex and costly; therefore intermediaries can facilitate access to information and validate common standards. This is termed lowering coordination costs, and intermediaries may supplement this with added value services such as financing.
- *Matching*: Intermediaries may locate buyers or sellers and thus create a marketplace suitable for transaction. Here, intermediaries may actually create/stimulate demand thus pursuing a self-fulfilling role for product comparison etc.

Impact of e-commerce and Internet technology

While intermediaries have been historically recognised as performing an important role in markets requiring massive information flows between buyer and seller, some authors have suggested that intermediaries will become a relic of historically inefficient markets. The advent of Electronic Data Interchange (EDI) and the Internet has allowed more widespread inexpensive access to information and buyers to locate, communicate and transact directly with sellers.[27] Coupled with the creation of electronic markets, this has led to many (eg Kieft)[28] forecasting the demise of intermediaries. This disintermediation has been argued in the following way. First, radical operational efficiency improvements in the cost of obtaining, processing and storage of information have led to changes in market structures and organisational design.[29] This has led to the rise of the 'networked organisation' and carries the implication of improvements in an organisation's value chain and company interlinkages.[30]

Table 1: Categories of intermediary (Bailey and Bakos, 1997)

Role of market intermediaries	Physical-oriented intermediation service	Information-oriented intermediation service
Aggregation	Combination of customer orders in wholesale orders	Provision of one-stop shopping
Trust	Provide legal contracts to govern market participation	Provision of authentication and secure communications
Facilitation	Provision of market specific infrastructure	Exchange of messages between customers and suppliers
Matching	Provision of rich product information	Provision of marketing information to suppliers

As a result, manufacturers increasingly use IT to perform traditional intermediary functions themselves, making intermediaries redundant. Malone *at al*[31] suggest that electronic integration creates a cost advantage, which implies the disappearance of intermediaries. Following this logic to its natural conclusion, manufacturers will find it increasingly cheap to interact directly with consumers and consumers will utilise the ability to customise products/services directly with producers. Accordingly, Sarkar *et al*[32] question how far these improved electronic links between companies threaten the existence of intermediaries.

This logic has been criticised on the grounds that it assumes that companies and consumer are sufficiently sophisticated, have the necessary time/flexibility/attitude to risk to undertake lengthy comparisons and transact by themselves.[33] Some authors argue that this is not necessarily the case and that electronic markets create opportunities for the re-intermediation of electronic intermediaries. Reintermediation recognises that buyer/seller interests must, by definition, conflict and that roles such as needs analysis, product information dissemination or producer risk management require some form of intermediary body. Sarkar *et al*[34] note that these bodies may be termed 'cybermediaries' in that a network-based intermediary offers a range of functions such as product search or product distribution over the Internet. A useful example of this argument in practice is the existence of Auto-By-Tel.[35] Here, Auto-By-Tel acts as information broker matching vehicles with client preferences and matching buyers with suitable car dealers through access to a continually updated information base therefore creating a more efficient search and negotiation process.

With increasing Internet usage and an increase in awareness of and access to information, end users may continue to do their own information searching.[36] It seems equally likely that an element of disintermediation will occur. However, the advent of electronic markets and associated technologies does not necessarily imply the demise of the intermediary. Rather, the traditional form of intermediaries is liable to change giving rise to the likelihood of new intermediary models in the future.[37] Bailey and Bakos[38] note, 'new roles for intermediaries seem to outweigh any trend toward disintermediation'. Indeed, key functions of aggregation, matching and market facilitation seem to be critical to both buyers and sellers, albeit with varying importance in differing contexts. Bailey and Bakos[39] surveyed 13 markets and contrasted the role of electronic intermediaries with that of more traditional, physical intermediaries. Table

1 shows the differing roles attributed to the two categories of intermediary.

Bailey and Bakos[40] found that although the traditional role of intermediaries was in most cases reduced, there were new roles for new types of intermediary to fulfil. Thus, although the aggregator role was reduced, the reduced coordination costs produced by market infrastructure improvements created opportunities for mobilising consumer bargaining power. Another example is matching in the financial services sector. Here, although the plethora of information reduces search costs, this carries the concurrent importance of navigating, filtering and matching of financial products with individual requirements.

Strategic conclusions

As some consumers become more sophisticated and as the market for their products broadens, UK product providers must develop products/services more tailored to the end-user and distribution channels. Secondly, business models must be restructured to more closely reflect organisational core competences, distribution channel relationships, strategic alliances and outsourcing opportunities. Thirdly, the IFA/product-provider relationship will change greatly, affecting the delivery of financial product/services to consumers.

Strategies for UK product providers

As a result of dealing with an empowered and increasingly sophisticated and discerning customer, companies will become more focused on delivering tailored customer solutions. The coordination of products/services, systems infrastructure and strategy will be geared to conducting relationships with individual customers. Certainly, the existing product/technical focus is decreasing, but discussions with product providers such as Scottish Equitable, Scottish Amicable & Scottish Mutual reveal that all efforts are still focusing on value chain efficiencies rather than stakeholder management. Accordingly, the evolution of truly CRM-oriented financial services organisations may be still some distance away, perhaps three to five years in the future.

Further consolidation in the industry is likely as financial requirements (ie capital adequacy and free asset ratios), brand strength, access to global markets and customer trust are becoming difficult and expensive to establish/maintain. Traditional financial services company core capabilities such as technical skills and resources such as financial strength will allow larger players such Merrill Lynch, Prudential and Royal Bank of Scotland further merger/acquisition opportunities. Some companies will use their scale to become commodity or infrastructure providers, churning out products in volume (ie as commodities). Other companies will aim for niche positions as innovators or superior performers offering asset or risk management services.

Opportunities for outsourcing and strategic alliances in areas such technology, CRM and product delivery will be significant. *Business Week* speaks of 'technology on tap' in its annual report on technology and this example proves the synergy potential for the pooling of resources and capabilities. An example of distribution channel alliances is the partnership of Tesco with the Royal Bank of Scotland. This partnership allows Tesco to outsource the infrastructural (including technical expertise) aspects of their personal financial planning operation whilst the Royal Bank benefits from exposure in

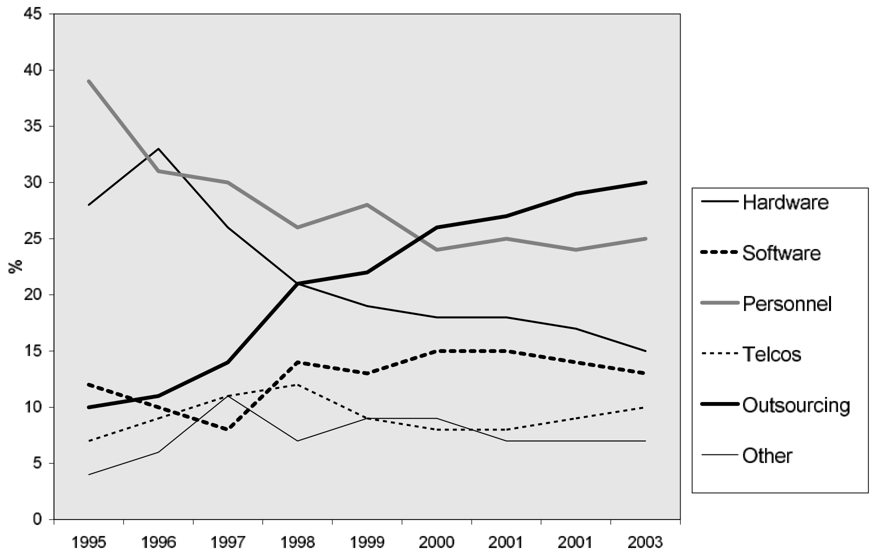


Figure 4: % of technology budget allocated to specific categories

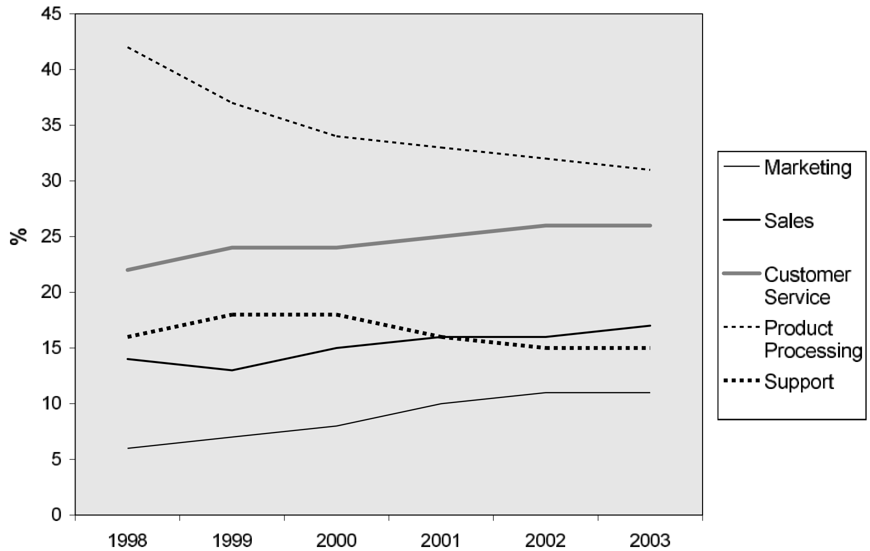


Figure 5: % of technology budget allocated to function

a separate but complementary area of its consumer market. The renewed emphasis on CRM, strategy and associated non-technical skills, the so-called 'soft skills' of the future, will place exhaustive demands on organisations. Traditional expertise in areas such as investment management, technical knowledge, deal-making and systems development may become less important with the resultant demand in favour of soft skills such as customer support — see Figures 4 and 5 for evidence of this. So, training, recruitment and associated consultancy will also be needed.

On the consumer side, increasing familiarity with technology and new concepts such as self-service financial planning (involving simple decision trees) look increasingly likely, particularly as the young people of today grow ever comfortable with technological innovation. As the industry is currently burdened by complex product specifications and ever increasing industry regulation, this however will not be easily achieved. A further extremely important trend for consumers is the increased prevalence of traditionally non-financial providers. For example, business-to-consumer financial portals coordinated by the likes of AOL-Time Warner, Yahoo and Tesco will bring financial services to a new tier of consumers that will combine to make products more simple to understand, more accessible, flexible and attractive to groups traditionally ignored by many financial services companies such as the retired population (the grey market) or lower income families in addition to the consumer segments who will readily embrace technology.

To date, UK product providers have justifiably been concerned with internal efficiencies (eg, new business processing) and continued profitability by focusing on areas such as increasing sales productivity and perhaps less interested in the provision of added value services and client retention. Product providers are prime candidates for a 'bricks and clicks' e-business strategy. Gulati and Garino (2000)[41] suggest that traditional companies combine their core competences with modern e-business skills to develop a hybrid business strategy thus servicing both established traditional markets together with electronic markets. However, the analysis above demonstrates a requirement for strategic thinking detailing how product providers may reorganise themselves to take advantage of the opportunities afforded by e-business.

Table 2: Transaction versus relationship approach

Transaction-based style	Relationship-based style
• One sale	• Many sales
• Commission bias	• Fees bias
• Low-service level	• High-service level
• Sales orientation	• Service orientation
• Product focus	• Solutions focus
• Product promotion	• Brand promotion

Product providers should consider the reorganisation of their value chain to encompass the efficiencies, cost savings, added value services and opportunities afforded by e-business. Indeed the notion of straight-through processing is similar to Rayport and Sviokla's (1995)[42] virtual value chain in that traditional business processes or market positions are circumnavigated by technology.

One option is that of relationship manager — a mediator between customer and product-provider. This model requires detailed understanding of consumer preferences and habits, while facilitating the possibility of premium pricing in return for customising the 'customer experience'. It is also expensive to implement, as sustained investment in systems, human resources and company culture is required. Further, this model requires a long-term horizon due to the difficulties associated with establishing/maintaining close customer ties. Table 2 summarises the main differences between the transaction and relationship approaches.

This model requires product providers to consider carefully their value chain activities and relationships with intermediaries. A key question is whether product providers wish to consider effectively transferring ownership of clients to themselves and away from IFAs. Product providers should assess whether it is more

Table 3: Life and Pensions Distribution, 2000–2004 (Datamonitor — eConsumers in Financial Services 2001)

£m	2000	2001	2002	2003	2004	CAGR 2000–4
IFAs	2992	3251	3545	3275	3961	7.3%
Direct sales force	1290	1291	1272	1279	1299	0.2%
Bancassurance	624	704	808	904	995	12.4%
Tied agents	258	277	295	301	309	4.6%
Other direct	209	227	249	273	301	9.5%
Affinity marketing	9	15	32	38	47	49.1%
Total	5382	5763	6200	6520	6912	6.5%
% Share	**2000**	**2001**	**2002**	**2003**	**2004**	**Change 2000–4**
IFAs	55.6	56.4	57.2	57.1	57.3	1.7
Direct sales force	24	22.4	20.5	19.6	18.8	−5.2
Bancassurance	11.6	12.2	13	13.9	14.4	2.8
Tied agents	4.8	4.8	4.8	4.6	4.5	−0.3
Other direct	3.9	3.9	4	4.2	4.3	0.5
Affinity marketing	0.2	0.3	0.5	0.6	0.7	0.5
Total	100%	100%	100%	100%	100%	

profitable to engage end-consumers more directly in the management and administration of their financial affairs or to maintain the manufacturer role and rely on distribution via intermediaries. Which choice they should make depends partly on the outcome of depolarisation and any resulting industry consolidation. If many IFAs evolve as multi-tied agents and commence contractual relationships with a limited panel of product providers, then this permits a greater degree of systems and service integration than is currently in existence. Accordingly, as product providers provide end consumers with greater access to their policies such as valuations/amendments/transactions/investment performance/general information, the possibility of product providers maintaining more direct relations with consumers appears increasingly likely. However, should the majority of IFAs remain truly independent then client relationships will continue to be considered their specific domain. This business model is further complicated by the fact that most product providers will have to operate both with multi-tied agents and IFAs and should therefore strive for the middle ground.

Indirect channels — IFA/product provider relationships

The existing preference by consumers for face-to-face contact will probably continue for the foreseeable future. IFAs will continue to play an important role in the distribution of investments, life assurance and pension products, despite the continued increase in direct channels such as telephone or new media ie the Internet and digital TV. Indeed, Datamonitor predicts that IFAs will increase their market share of the distribution of life/pension products to around 57.3 per cent by 2004.[43] Table 3 shows how product provider channels of distribution are expected to evolve. It is clear from these projections that the IFA/product provider relationship in terms of investments, life assurance and pension products will continue to form the most important role for product providers, with even a slight gain in share. Meanwhile, the once much-vaunted bancassurance model will grow but still only account for a small share. Finally, note that the distinction between IFAs and tied agents will need to be revisited with the introduction of depolarisation.

Depolarisation holds both opportunities and threats for product providers in that they must commence informal negotiations with 'candidate multi-tied' IFAs to gain access to the clients most suited to their products, but risk harming close ties with larger IFAs who intend to remain independent regardless of depolarisation. Accordingly, decisions must be made as to how UK product providers view multi-tied firms and truly independent financial advisers. We believe that both types of IFA should be accommodated, necessitating differing product/service offerings. Product providers should undertake extensive analysis of their entire product/service portfolio and cross-reference these results against a profile of the IFA that is most suited to these characteristics. This involves identifying key IFA accounts that require superior service levels compared to relatively low priority IFAs who simply require a telesales approach. This exercise should seek to establish each component's requirement for personal advice and specialist assistance and whether this form of advice/assistance is best administered via an IFA or multi-tied agent. Further, product providers should commit significant resources to the establishment/maintenance of closer electronic integration with selected IFAs. This will improve value chain efficiency and also provide a basic hygiene factors, ie proper customer service as required by IFAs.

The major source of innovation in the indirect channels of distribution is expected to lie with the introduction of information aggregators such as the Exchange, Yodlee and Fidelity's Fundsnetwork. This new form of intermediary will assist in the analysis, evaluation and purchase of relatively simple financial products and will act as medium accessible via the Internet to both consumer and corporate clients. UK product providers should view these new entrants as a major opportunity to dilute their historical reliance on IFAs and engage consumers more directly in the transaction process. Product providers should regard such intermediaries (portals, infomediaries etc) as the opportunity to match products with clients more efficiently. Product providers should undertake both product and profitability analyses to understand precisely which products are best suited to each distribution channel. For example, stakeholder pensions hold the possibility of being administered online using the technological capabilities offered by 4th Contact, for example, and their online project entitled 'Working Wealth' which offers the potential for viewing pensions, health insurance, stock options and other benefits schemes online.

We recommend that product providers should also consider greater product customisation in light of fast approaching depolarisation and dominance of national IFAs and networks. Here, more complex products such as self-administered pension schemes (SIPPs) or inheritance tax mitigation plans could be customised to more closely reflect the client base requirements of the larger, more profitable IFAs.

Direct channels

Many providers are using this approach, and although the share of business is low, it is growing. Success here implies use of the telephone to move from a purely execution-only to a more advice-driven basis. Growing consumer sophistication and the increasing ability for information search implies that product providers must offer consumers a range of products and services suitable for delivery over the telephone. At present Scottish Widows and Standard Life offer this service but use it as a method of backing up IFA business as consumers are encouraged to retain an IFA. Relatively simple products such as term assurance or ISAs should be available via the telephone due to the decreasing costs associated with maintaining a telesales operation. Accordingly, the telephone should be used as a direct channel of distribution supporting other channels but clearly has the capability for increasing transaction levels as Virgin has clearly demonstrated (although profitability has yet to emerge).

The Internet is perhaps the most important opportunity for direct consumer interaction with product providers as it offers the potential not only for increasing the frequency and quality of value chain communication, reducing cost and new marketing opportunities but also for transaction capability. However, product providers must engage in product analysis and, in essence, redesign products to become more streamlined and suitable for distribution via the Internet. An example of product providers establishing an alliance with a corporate client is Prudential's venture with Sports Fitness & Leisure Ltd, whereby Prudential provides an online education service with the intention of eventually launching a transaction-based operation. Since Government has already initiated price/charge transparency, product providers should seize this opportunity to refine their entire product range.

Depolarisation offers the opportunity of more closely aligning product providers across different product specialisms so the cost of this exercise could be shared across all partners. Indeed, the advent of depolarisation indicates that product providers will be selected on the basis of their systems/IT infrastructure. Therefore, although provider allegiances will prove cost-efficient, we believe that they will also prove to be a strategic necessity. An example of such partnership is Legal & General working with Standard Life and the Printing Industry Pension Scheme to deliver policy information account statement online. Industry initiatives such as ORIGO, will help the establishment of industry standards such as the widespread adoption of public/private key identification, standard proposal forms and new business processing.

Product providers should also increase efforts to transact online. This should be through relatively simple price-driven products to be delivered via the Internet effectively as commodities. The advent of Fundsnetwork & CoFunds further demonstrates the viability of using the Internet to transact online. There are significant opportunities for product providers to transact online to both corporate (eg in connection with stakeholder pensions) and consumer markets (eg ISA products).

Traditional product provider revenue models

UK product providers are under increasing pressure to provide products within a 1 per cent capped charge. They will need to find ways of radically reducing costs associated with processing and administering business. It increases pressure on IFAs to move from a primarily commission-based revenue structure to a more fee-based model. UK product providers may consider moving to a dual pricing structure, paying IFAs greater remuneration for operating electronic administration than that of traditional, labour intensive and paper-based methods. IFAs would probably experience declining margins in commission-oriented transaction-intensive activities such as fund switching and may be inclined to launch their own fee-based remuneration structure so that administration costs are reduced. Product providers must find ways to motivate IFAs to join in cost-cutting value chain efficiencies whilst adopting a more anticipative, proactive stance toward industry trends.

The functions of new business processing, client servicing, administration, communication and collaboration will need to be progressively migrated on to the web. New systems such as that offered by 1st Software, adopted by many leading IFAs, facilitate electronic reorganisation of systems, but there is a clear need to develop the notion of straight-through processing across the product-provider value chain. This will span both the internal departmental lines and across Intranet/Extranet with product providers or large corporate clients. This internal process integration will allow product providers to reorganise their organisational boundaries to follow a more flexible, semi-permeable membrane organisational model. The flow of communication between product providers and external stakeholders will become more frequent, structured and flexible to facilitate access to a variety of internal services.

Product providers need to recruit more customer-oriented staff with softer skills such as customer relationship management or alternatively outsource this requirement. A balance between the technical expertise, administration quality and the CRM oriented focus of the workforce is required, if product providers are to foster new and strengthen existing relationships with stakeholders. This implies that significant resources be devoted to the recruitment of new staff along with retraining of existing employees. Organisational culture is an important managerial challenge.

The financial services sector as a whole is contemplating the arrival of e-business related technology with considerable concern, as these issues do not rest easily with the traditional product oriented focus adopted by many companies. Product providers currently have strong cultures based on technical knowledge and expertise, investment performance and product-oriented sales norms as introduced and reinforced by legacy systems and industry trends spanning decades. How may this be changed to encompass the latest attitudes towards stakeholder relationships, technology etc required at Board level and at all levels throughout the organisation? Many product providers appear restricted to a relatively myopic view of e-business, believing it impossible to attempt anything more than value chain efficiencies for at least two years ahead. It is therefore up to progressive IFAs to spearhead developments in straight-through processing and business model design by exemplifying/pioneering innovations and aligning themselves more closely with similarly progressive product providers. So, current criteria for selecting a product-provider (namely, investment performance, charging structure, financial strength) should expand to include e-business capabilities.

One of the key external managerial challenges is concerned with strategic alliances and outsourcing of technological development, systems infrastructure and technical expertise eg IBM's links with the Bank of Scotland as a pioneering example, which proves the possibility of pooling resources while avoiding conflicting cultural problems, training costs and compensation disparities associated with the introduction of new system/business processes. Outsourcing and alliances increase the speed to market of in-house developments and allow the opportunity to expand the customer base at minimal cost. However, relationships with third parties require change management programmes coupled with information sharing and collaboration arrangements. These pose significant problems in an industry used to clear organisation boundaries and unambiguous market relationships underpinned by complex service level contractual obligations. Alliances will only offer work if undertaken with an open-minded, flexible managerial/entrepreneurial mindset.

A final managerial challenge is the myriad of technological innovations, which further hinder clear strategic thought. In addition to common development tools such as XML, communication/collaboration standards such as Rosettanet — there are a wide variety of access devices, which open the delivery of financial products and services to a new marketplace. The advent of mCommerce, iTV and wireless connectivity and broad bandwidth offer significant opportunities. The implications of this relate to the delivery of location non-specific services allied with more complex insights into consumer preferences. The development of the universal device (music, video, telephone, Internet access) also lends credence to the increasing diversity/dynamism of marketing as cross-selling opportunities and potential for individual customer relationships increase exponentially. For example, Natwest currently work with Orange and Woolwich with Nokia to deliver WAP services throughout the UK. It seems likely that consumers may soon become less concerned with technology and access devices and more concerned with seamless access to information and personalised transactions. So we recommend that product providers seriously consider the customisation of financial products and value added services to more closely reflect the idiosyncratic characteristics of distribution channels and, of course, the end consumer.

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