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Alternative paths to high performance of independent financial advisors: A fuzzy-set analysis☆

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ABSTRACT

This study performs a fuzzy-set Qualitative Comparative Analysis (fsQCA) to determine the conditions that lead to high performance of independent financial advisors. The study examines the performance of these companies in terms of their involvement in innovation activities, participation in business networks, and open innovation as a strategy to cope with difficult market conditions resulting from the recent economic downturn. This approach clarifies the relationship between combinations of conditions and high performance. The results suggest that involvement in innovation activities is the most relevant factor in financial advisors performance. Independent financial advisors may achieve higher sales thanks to engaging in innovation activities.

1. Introduction

Independent financial advisors (IFAs) offer customers personalized investment proposals that adapt at all times to the market environment. The work of the IFAs is independent and transparent, and aligns completely with customer interests.

The financial crisis has severely affected IFAs. Under poor economic conditions, small businesses are more vulnerable than large firms (Audretsch, 2012). The analysis of business performance during economic downturns shows that companies that engage in radical innovation are more likely to survive. Small businesses often depend on the effective use of their existing and newly acquired knowledge in order to remain competitive (Chaston, 2004). The participation of enterprise networking companies in the development of new products and production processes favors the acquisition of new knowledge. In fact, this collaborative approach is what Chesbrough (2003) calls open innovation. The purpose of this study is to examine the effect of innovation activities, participation in business networks, and involvement in open innovation on performance.

Regarding research methods, Armstrong (2012) recommends not estimating relationships for more than three variables in a regression. The use of algorithms is appropriate for crafting and testing theory (Woodside, 2013). In addition, any insightful combination of conditions usually has an asymmetrical relationship with an outcome condition and fuzzy-set Qualitative Comparative Analysis (fsQCA) allows for asymmetrical relationships of conditions.

Drawing on these remarks, this study revisits the theory, data, and analysis in Lassala, Momparler, and Carmona (2013). Through a fsQCA, this study performs a joint examination of different conditions leading to high performance of IFAs.

The structure of this study is as follows. Section 2 focuses on independent financial advice as a way to invest. Section 3 explores literature on involvement in innovation activities, knowledge, and networks and open innovation. Section 4 describes method and data, and discusses results. Section 5 presents conclusions, limitations, managerial implications, and future research.

2. Independent financial advisory

IFA provides, by law, a specific and individualized support. Before issuing the personalized recommendation, financial advisers give a suitability test to their customers to analyze their experience, knowledge, financial situation, and investment objectives. IFA informs their customers about IFA's responsibilities and the risks of a particular investment. Consumers do not perceive the same level of risk in all financial products (Renko, Shrader, & Simon, 2012), and some investments require a lot of involvement prior to the purchase decision (Beckett, 2000). Therefore, IFA's advice should be comprehensive for a given investment opportunity (Bourne, 2011) and take into account non-financial aspects.

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Although many consumers buy low-risk financial products without IFA's advice (Gough & Nurullah, 2009), some clients choose getting some counseling (Gill, 2008). Customers' knowledge of financial services and the availability of information determine their willingness to seek independent financial advice (Ennew, 1992).

In Spain, wealth management continues to rely mainly on financial institutions and potential conflicts of interests remain in commercial banks' advisory services. To overcome these problems, a new approach to investing based on independent, unbiased, and personalized financial advice is necessary.

IFAs' goal is to protect the interests of their clients. The Spanish IFAs still have a long way to go in order to achieve the level of recognition such entities enjoy in countries like the UK, Switzerland, or Germany. At the end of 2014, the number of IFAs registered with the CNMV is 143 and the assets IFAs managed are 21,391 million euros. In addition, IFAs signed 4639 contracts.

Montero and Fernandez-Avilés (2012) conclude that the use of some kind of financial advice is common in Spain, as well as the combination of several types of advice. As for independent financial advice, customers usually have a better understanding of financial matters and are aware of the cost of the service. Investors are willing to pay for a value-added service that is clearly independent and objective.

3. Literature review

3.1. Involvement in innovation activities

Sales revenues of IFAs have declined significantly over the recent financial crisis. Innovation and the focus upon creating new products and services help firms to emerge from an economic downturn in a much stronger position than competitors who choose to cut costs or improve internal efficiencies (Idris & Tey, 2011; Trott, 1998). Although price cuts assist a firm in sustaining an acceptable revenue flow during a recession (Bhasin, 2012), the strategy goes usually hand in hand with a reduction in profit margins. Such outcomes commonly occur in firms engaged in the provision of consumer services (Wener, McDermott, & Rotz, 2004).

Katz (2008) analyzes the importance of innovation in the development of new and improved services by IFAs during the economic downturn in the USA. In addition, Chiasson (2011) points out that computer-based Customer Relationship Management (CRM) systems offer an effective path to develop and launch new financial services. Small firms are aware of the need for a fully integrated range of services covering both their business operations and personal finance. Hence, these companies are an important market segment for IFAs.

3.2. Knowledge and networks

Knowledge management draws on the knowledge of the organization, creating new knowledge, and promoting innovation and exploitation of international collaboration to improve employees' skills (Bose & Sugumaran, 2003). Furthermore, Yaniv and Brock (2008) suggest that effective knowledge management requires combining tactics with explicit knowledge. To Carland and Carland (2000), business ideas are the result of knowledge, experience, and creative vision.

The efficiency in the use of new knowledge affects organizational performance. Jones and Crompton (2009) find a positive relationship between the use of new knowledge and obtaining a better performance in small businesses. Also, Merona, Lopez-Nicolas, and Sabater-Sanchez (2007) highlight the great importance new information acquires in knowledge-intensive firms. Companies in the service sector can collaborate with other firms to obtain competitive advantages in order to maintain their business performance (Shaw, Lam, & Carter, 2008). Elfring and Hulsink (2003) conclude network participation is a crucial factor in sustaining the performance of firms.

Because of resource limitations in small companies, their involvement in business networks is a key source of knowledge (Kosa & Lewin, 2000). The network promotes the exchange of ideas, knowledge, and technology among companies. Chatterjee (2004) also emphasizes the importance of business networks in innovation management. The success of small firm networks depends on the joint search for responses to changes in market conditions. Companies should accept higher levels of risk associated with the expansion of network members to access a larger pool of external knowledge (Presutti & Boari, 2008). Baker and Sinkula (2009) note the increasing importance of risk management in small businesses due to their reduced ability to use financial resources when a radical and new strategy fails.

3.3. Open innovation

In the current environment, users are increasingly demanding. The development of technology in many companies is becoming increasingly expensive (Chesbrough, 2012). Thus, companies that want to remain competitive rely on external sources of innovation. BarNir (2012) identifies the means available to businesses to implement open innovation paradigm, including research, collaboration, adoption of regulations, and exploitation of intellectual property.

Chesbrough (2003) introduces the concept of open innovation. Companies must look for ideas and ways to market both internally and externally by using the environment as a source of innovation. Implementing an open innovative approach requires establishing a strategy (Sandulli, Fernandez-Menendez, Rodriguez-Duarte, & Lopez-Sanchez, 2012) and defining the most appropriate tools, adapting the paradigm for each business case (Battistella, Biotto, & De Toni, 2012). Huang, Wang Yun, Tseng, and Lee (2010) emphasize that open innovation enhances the effectiveness in creating value by leveraging many ideas from a wide variety of external sources. Freel (2006) also concludes that involvement in open innovation is a key factor in the introduction of new production technologies and the development of new products.

However, not all companies have the same drive to innovation. Christensen, Olesen, and Kjaer (2005) argue that companies manage open innovation differently depending on (1) their position in the innovation system, (2) the stage of product/service maturity, and (3) the scale of the value proposition.

Elmquist, Fredberg, and Ollila (2009) point out the great importance of the number of partners in the business network and the adoption of an external focus versus an internal one on innovation. Companies very oriented to closed innovation can lose opportunities (Chesbrough, 2012). However, although open innovation allows access to external ideas, Birkinshaw, Bouquet, and Barsoux (2011) state that problems over intellectual property ownership and mistrust could frustrate the achievement of optimal project outcomes. Nevertheless, Moensted (2010) stresses the importance of participating in collaborative activities with other organizations to access new additional knowledge. Palacios, Gil, and Garrigos (2009) conclude that knowledge management is an especially critical factor influencing the level of innovative orientation of knowledge-intensive organizations.

Companies that focus on innovation are more likely to survive an economic downturn (Trott, 1998). Chesbrough (2012) indicates the importance of open innovation in order to benefit more effectively from existing and new knowledge for the exploitation of business opportunities to sustain business performance. With regard to the service sector, Chen, Duan, Edwards, and Lehaney (2006) prioritize the acquisition and exploitation of knowledge when organizations engage in open innovation. The knowledge management processes involve the acquisition of knowledge from external sources which, in turn, enhances service providers' ability to respond quickly to external environmental changes.