How Financial Advisors Buy ETFs

With nearly 3,000 ETFs in the U.S. market and ongoing pressures on fees, ETF Advisors are changing how they work with ETF issuers.

Executive Summary

Context

The past 20 years has seen unprecedented change in how people buy nearly everything in their day-to-day lives. Mass customization and online-intermediation are part of every transaction, from a Starbucks coffee, to watching a movie on Amazon Prime. So too, has the way Financial Advisors research and buy ETFs.

2019 saw near-record inflows into Exchange Traded Funds, the passage of the ETF Rule at the SEC, equity markets that topped 30%, and the approval of new, non-transparent active ETF structures. At the same time, the ETF industry has been in a brutal fee-war, with a fully diversified ETF portfolio now available for less than 0.05% in annual expenses. Most brokerages and custodial platforms dropped commissions on ETFs to zero in 2019, and the financial media is peppered with ads for ETFs in a way few financial products have been promoted before.

The Research

Advisors spend significant time focussed on investing, but how they want to consume information is radically changing.

- Only 10% of advisors want to meet with issuers one-on-one, most preferring webcasts and other digital education efforts.
- Advisors are more tech-savvy than most might expect, and want their ETF education digitally.
- Home office “approved lists” have little uptake, while 81% use model portfolios of some sort.

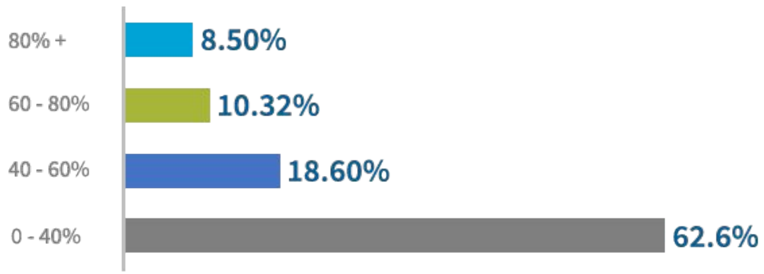
ETFs Have Made A Real Impact . . .
But There's Lots Of Room To Grow

The Research

The ETF Super Users group -- those that allocate nearly all their clients assets to ETFs, is a relatively small 8.5% of the advisors surveyed. But the ETF Dabbler group -- where ETFs represent under 40% of client assets -- represent over half.

Projected across the entirety of advised assets, this implies there are still Trillions of dollars in addressable assets for ETF issuers to pursue.

What Percent of your clients portfolios are in ETFs?



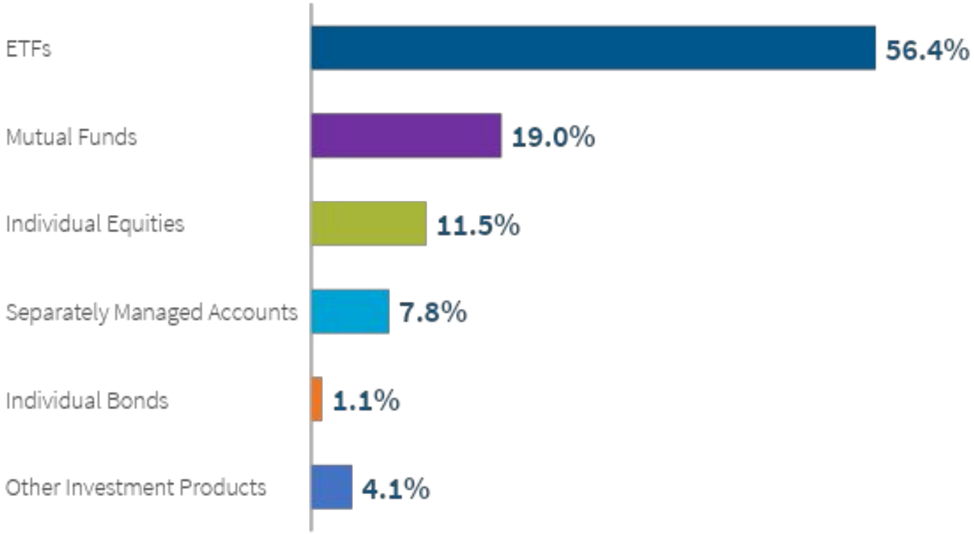
Source: 2019 ETF Trends/ETF Database Advisor Survey

Context

ETFs have been one of the fastest growing financial products in history. Since the Global Financial Crisis, U.S. listed ETFs have pulled in $2.6 Trillion in net new money, while the traditional mutual fund industry (including index mutual funds) has lost $186 billion. Financial advisors were a huge source of that growth, and yet, penetration remains modest.

ETFs Are Dominating New Asset Allocations

What are you most likely to allocate into in the next year?



Source: 2019 ETF Trends/ETF Database Advisor Survey

The Research

Whether super-users or not, Advisors overwhelmingly expect to use ETFs in allocations over the next year, at a rate three times that of traditional mutual funds.

We actually expect this number will turn out to be much higher: with an increasing focus on smart beta strategies, environmental-social-governance related ETFs and a coming wave of new active managers taking advantage of the recently approved structures, it seems inevitable that 2020 will be a banner year for the industry.

Context

As the ETF market has evolved, advisors have gone from using ETFs just for low-cost beta exposure to implementing complete portfolios. In 2019, flows into ETFs were evenly split between equity and fixed income products for the first time. Thematic, smart beta, ESG, defined outcome and tactical products continue to flourish, and there’s no slice of the investment pie-chart where there’s not at least a few ETFs competing for attention.

Advisors Are Hanging Up On ETF Issuer Reps

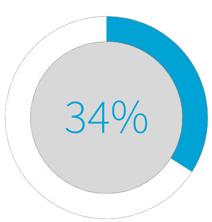
The Research

Advisors rarely speak with the ETF issuer representatives, with only a third of surveyed advisors saying they spoke to a rep in the past month. The amount of time they spend talking with the ETF issuers is in sharp contrast with the amount of time they spend researching ETFs – once a quarter on average versus one day a week.

However, very few actually show interest in speaking with a rep (10%). Instead, advisors are looking for digital educational content as well as more digital contact with their ETF issuer representative.

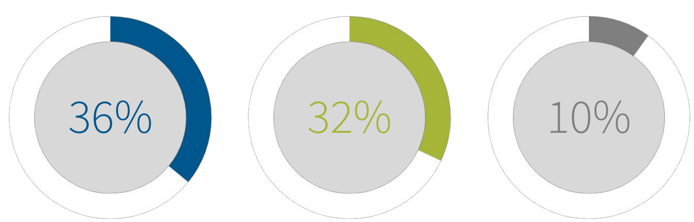
Only one-third of advisors have talked to an ETF rep in the past month. Advisors prefer digital communication.

When was the last time you spoke to an ETF issuer representative?



Within past month

How would you like most ETF issuer representatives to communicate with you in the future?



Educational / Strategy Webcasts | Email / Newsletters | One-On-One Meetings

Source: 2019 ETF Trends/ETF Database Advisor Survey

Context

Historically, the manufacturers of financial products, including ETFs, have used in-house employees - wholesalers - to go out into the field and talk to advisors. Ten years ago, meeting requests from wholesalers were almost a daily occurrence in many larger RIAs. Our research suggests those days are long gone.

The ROI on Wholesalers Continues to Decline

Context

The old wholesaling model is expensive, but increasing headcount has not translated into higher profits.

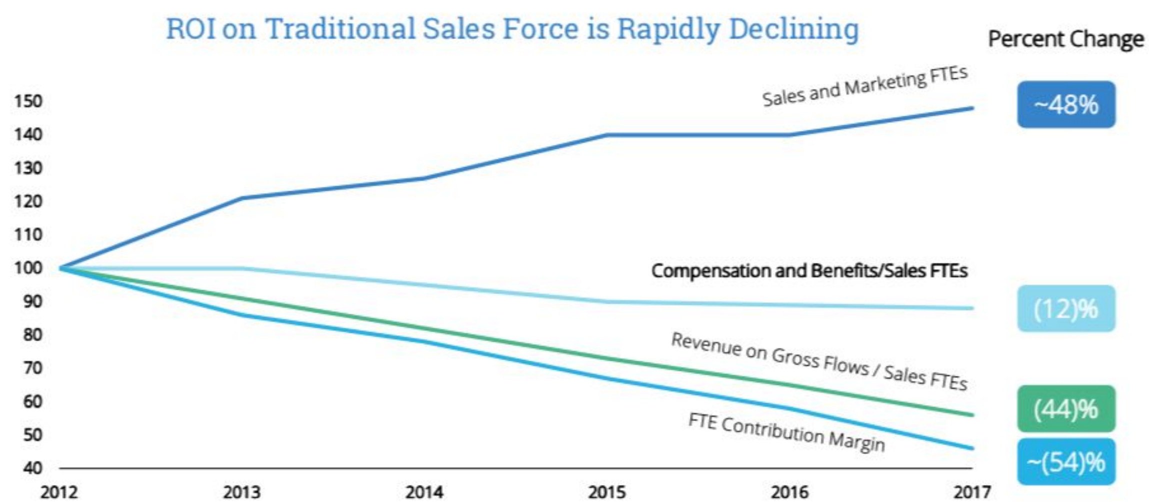
Successful ETF issuers provide their sales representatives with digital content geared both to the advisor, and the advisor's client. For many this will mean investment in new technology, system improvements, and cross-functional coordination to deliver meaningful and insightful, easily searched content to advisors to help them grow their business.

The good news for smaller issuers is that digital distribution is much more scalable than is hiring wholesalers. Quality matters.

The Research

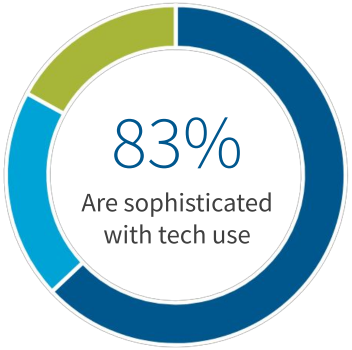
The results from our study show that advisors' needs have evolved, and the industry has not followed. ETF issuers still offer the same traditional approach to distribution, pushing upstream against the trend.

This finding meshes nicely with work done last year by Ben Phillips and his colleagues at Casey Quirk, which suggests that despite continually increasing spending, the old model of throwing more bodies into the field simply isn't working. They coin this shift 'Distribution 2.0."



Source: Casey Quirk, "Distribution 2.0: How Technology will redefine relationships with asset management clients", 2019

ETF-Centric Advisors Are More Tech Savvy



When it comes to the use of technology, you consider yourself…

- Sophisticated: **63%**
- Highly Sophisticated: **20%**
- Not Sophisticated: **17%**

Source: 2019 ETF Trends/ETF Database Advisor Survey

The Research

The overwhelming majority (83%) of advisors say they are sophisticated or highly sophisticated in their use of technology, especially those from larger firms (90% vs. 80%). This has an important implications for how advisors research investments, particularly ETFs. As advisors become more sophisticated and more informed, they spend more time on researching and developing their investment strategy—and they're using technology to do it.

Context

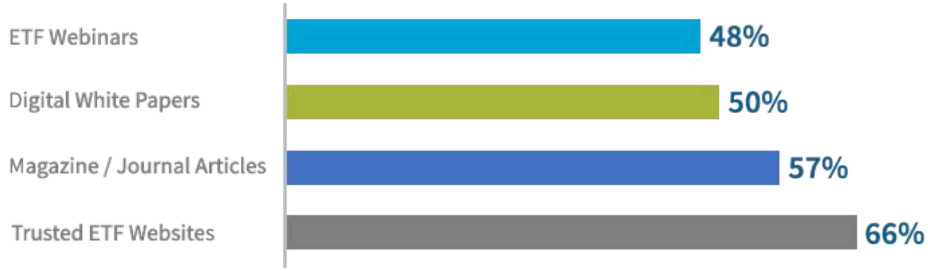
It wasn't too long ago that financial advisors were considered stodgy in their tech-savviness. After all, according to Cerulli Associates, the average age of a financial advisor is now over 50, with a shallow pipeline of younger advisors taking the place of retirees.

The results here tie to another industry trend: consolidation. Successful advisory practices invest substantially in technology platforms to enable all aspects of their business from prospecting to statements. Those investments benefit from economies of scale, helping fuel M&A activity.

Trusted ETF Research Sources Are Essential. Approved Lists? Not So Much.

Advisors use technology for industry news & research

When you are conducting ETF investing research, which sources do you use?



Source: 2019 ETF Trends/ETF Database Advisor Survey

The Research

Education plays a very important role in ETF investment decisions. Advisors have limited time to dedicate to researching ETFs, and with so much information available, they currently prefer going to trusted (mostly online) sources for their information. ETF research websites, articles from industry journals, digital white papers, and ETF webinars are the most commonly used and preferred sources for information.

According to survey respondents, less than a fifth of advisors (18%) use the custodial ETF Approved Lists they have access to, which raises questions about the value of these internal research tools.

Context

ETF issuers have invested millions into developing their own websites but they are rarely visited by their advisor clients. Issuers who make their content and research more readily searchable will be rewarded many times over. But all that work in creating “approved” lists seems to be falling on deaf ears.

Advisors Spend A Day A Week On Research

The Research

On average, advisors spend just over six hours per week on industry and investment-related news and research. Financial advisors who define themselves as "portfolio managers" clock even more time each week on research, spending an average of one day per week of their time on research. They conduct this research mainly online, in the office.

Advisors spend a significant amount of time per week on industry news and research.

How much time do you typically spend per week on industry and investment-related news and research?

Portfolio Managers

All Advisors

Source: 2019 ETF Trends/ETF Database Advisor Survey

Context

Growing a financial advisor practice is incredibly labor intensive. At a small firm, the lead advisors are meeting clients, prospecting, running the firm, managing a back office … in addition to managing clients' investment portfolios.

Into that busy schedule, ETF issuers vie for advisors' attention. Their best opportunity is likely to help advisors save their most critical resource: time.

Information needs to be in easy-to-find and easy-to-digest packages, and advanced tool offerings from issuers that make the research process more efficient will find traction.

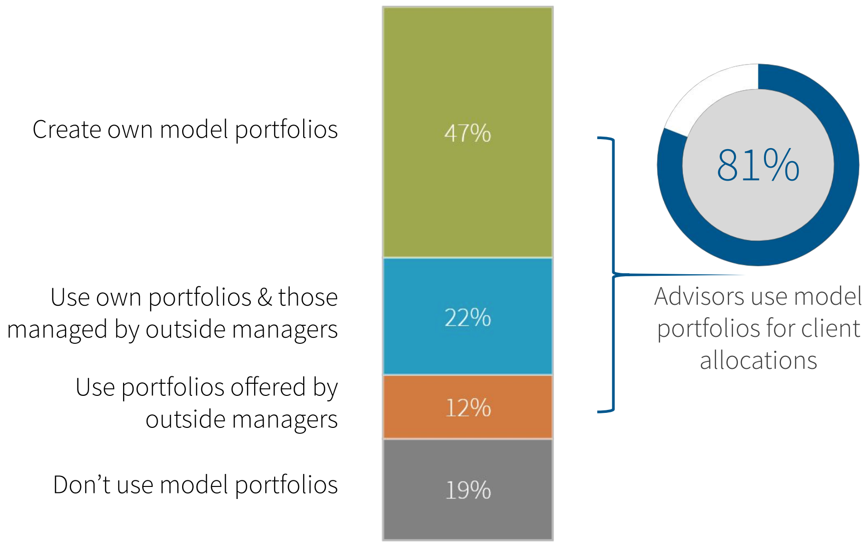
Models Helps Sustain ETF Growth

The Research

Model portfolios are popular among advisors, and continue to gain popularity, with 81% of advisors using some sort of model portfolio in their practice. This reliance on models is a positive for ETF issuers, as it helps build a long-term structure for portfolios and creates a greater commitment to hold ETFs.

More than four out of five advisors implement model portfolios in their client portfolio construction today. Most advisors (47%) are using their own models for their clients while only 12% of advisors use only outside manager models.

Do you use model portfolios for your client allocations?



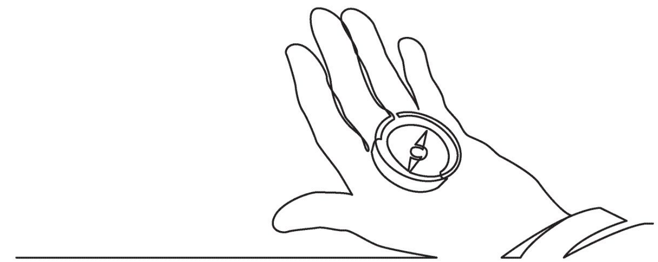
Source: 2019 ETF Trends/ETF Database Advisor Survey

Context

One of the early "objections" from advisors in previous decades had been that they didn't know how to make ETFs work in a full-portfolio context. This led to the rise of ETF Strategists and model portfolios. Models, in any form, provide a critical time-saving tool in the daily management of the business, streamlining the onboarding of clients, reporting of results, and management of rebalances.

In the past few years, most large ETF issuers have started providing model portfolios at no charge to advisors, and virtually all larger financial advisor groups produce in-house models.

Conclusion



Today's financial advisor has been forced to become more sophisticated and tech savvy in order to compete. This evolution has affected everything from the products they use, the technology they adopt, the way they perform their due diligence and the way they communicate today.

ETF issuers need to adapt too. Traditional distribution systems, dependent on headcount, won't be replaced overnight, but successful firms will marry the human element with technology, providing tools and content when and where advisors want them. These changes have to come from the top, however. Smaller firms will have to balance maximizing reach with budgets constrained by the ongoing fee war. Larger players with established distribution efforts will need to plan for this shift, collaborating internally on issues from Technology & Machine Learning, to Marketing, PR and Social Media.

The face of the financial advisory business is changing. It's up to the investment community to keep up.

Context

Across all aspects of our lives, buyer behavior has evolved as the digital tool suite expands, the modern financial advisor is no different. More and more asset managers need to embrace this change and look to alter their distribution model to educate and aid their clients and customers on how, when and where they want to consume information along their research journey.

PROFILE OF RESPONDENTS

- $100M or less — 58.4%
- $100 Million - $1 Billion — 23.7%
- $1 Billion - $50 Billion — 8.3%
- Over $50 Billion — 3.7%
- Unknown/Does Not Apply — 5.9%

- Asset Gatherer — 28.7%
- Portfolio Manager — 30.4%
- Firm Management — 17.9%
- Other — 23%

STUDY METHODOLOGY

This survey was conducted by ETF Flows LLC using a quantitative online survey methodology in third quarter of 2019.

Participants included 675 financial advisors.

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