ETFs make their mark with wealth advisers and managers

By Beverly Chandler

June has seen two events in the ETF calendar organised by firms who have overcome their market competitiveness with each other in favour of educating investors.

The ETF Forum is an independent, UK-based partnership founded by ETF/ETP providers BMO Global Asset Management, ETF Securities, Source in association with Legal & General Investment Management and WisdomTree Europe.

The stated aim of The ETF Forum – which covers not only exchange traded funds (ETFs), but the entire ETP landscape – is to provide advisers and wealth managers with a better understanding of ETFs and how to use them as effective investment tools to build or enhance well-diversified portfolios.

"We have a common desire to increase ETF education among investors," says Marc Knowles, director of ETFs, at BMO.

ETF take-up across the world has seen assets under management overtake that other stalwart of the alternative field, hedge funds, as they have suffered loss of performance in recent years. The most recent figures from ETFGI show assets invested in ETFs/ETPs listed globally reached a new record high of USD3.143 trillion at the end of May 2016, with 6,374 ETFs/ETPs, with 12,200 listings, from 280 providers listed on 65 exchanges in 53 countries.

In terms of Europe, ETFs in Europe gathered USD2.68 billion in net new assets in May, marking 20 consecutive months of positive net inflows. At the end of May 2016, the European ETF/ETP industry had 2,219 ETFs/ETPs, with 6,927 listings, assets of USD530 billion, from 52 providers listed on 25 exchanges in 21 countries.

Passive investment in the form of ETFs is beating active, although original players in the ETF space might not recognise new entrants to the sector, whose ETFs are becoming increasingly smart through factor use or offering access to shorting and leveraging markets.

From a study published in early June, European ETF provider Source revealed that, on average, institutional investors – and, in a separate poll, financial advisers – predict the global ETF market will double in size over the next five years to account for 6 per cent of global investment fund assets under management. Source's findings were that just 2 per cent of respondents expect the market to shrink in terms of assets under management while 6 per cent believe that assets in ETPs will grow to between 11-15 per cent of the total investment fund market.

The research found that just 9 per cent of respondents expect to decrease their allocation to ETPs over the next 12 months. A third (33 per cent) expects to increase their allocation, with 7 per cent looking to increase this 'significantly'. On average, respondents said that passives/ index funds account for 8 per cent of their overall assets under management.

Lower costs were cited as the main benefit of ETPs over other investment funds (cited by 53 per cent of respondents), followed by more choice (18 per cent), better liquidity (18 per cent), and innovation (15 per cent).

The research also found a significant number of respondents (43 per cent) agree that ETPs are increasingly being used as long-term investments at the centre of portfolios as opposed to playing more tactical, short-term roles. A further 33 per cent said that this may be the case; less than a quarter (22 per cent) said they did not see ETFs/ ETPs being used as long-term investments at the centre of portfolios.

Interviews from the ETF Express Awards earlier this year, showed that ETFs are being used for all sorts of portfolio positioning and that there are new entrants to the field, coming from the more traditional brokerage and adviser sectors. Speaking at the etfexpress Awards 2016 in London, Townsend Lansing, Executive Director – Head of ETCs, ETF Securities (UK), commented on the exponential growth of ETFs. "They are here to stay," he said. "They are essential building blocks in a portfolio."

However, their growth has not gone unnoticed by regulators and a somewhat sceptical financial press. In his speech at the ETF Awards, Lansing commented on a recent letter, published in The Financial Times that sought to address the bad press the sector receives.

"Fears that ETFs are the next crisis are all misplaced," he said. "More active managers are looking to ETFs, and more retailers are continuing to move into the sector."

One of the big drivers of the ETF push into the traditional wealth management and IFA territory is fee pressure. ETFs offer cheap access to an index and earlier this year WisdomTree Europe's co-CEO Hector McNeil published a note on this very issue, predicting that the coming year will see a greater focus on performance in ETFs.

"The pricing of core ETFs has already arguably won the battle with mutual funds when it comes to the provision of passive trackers. Now we are seeing a shift in focus in terms of investor expectations as they become more aware of the opportunities and breadth of asset management benefits the ETF wrapper can deliver for them," McNeil said.

"We are yet to see this focus on performance after fees in the ETF space to the same extent as exists in the US, but as smart beta picks up momentum in Europe, we believe it to be the direction of travel over the next few years."

McNeil believed that rather than focusing on whether they can get US equity exposure for 4bps or 5bps from different providers, it will be the type of exposure investors are getting which will become more important.

In Europe, particularly again in the UK, ETFs face infrastructure issues with independent financial adviser platforms often designed to cater more for mutual funds or unit trusts. This is changing and the change was partly inspired by the UK's 2013 Retail Distribution Review which was designed to encourage transparency on the cost of investing by the investor, and to stop financial advisers being remunerated through commissions rather than fees.

If an IFA is being paid a fee for advice, rather than taking a commission, ETFs and mutual funds move onto a level playing field in the remuneration stakes, surely ensuring that the ETF industry will just continue to grow in popularity. ■