WINNING AGAINST THE RACE TO ZERO

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This article is relevant to financial professionals who are considering offering model portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios, please inquire with your financial professional. Not all financial professionals have access to these Model Portfolios.

Maybe someday, saved by zero
I'll be more together
Stretched by fewer thoughts that leave me
Chasing after my dreams, disown me, loaded with danger
So maybe I'll win (saved by zero)
Maybe I'll win (saved by zero)

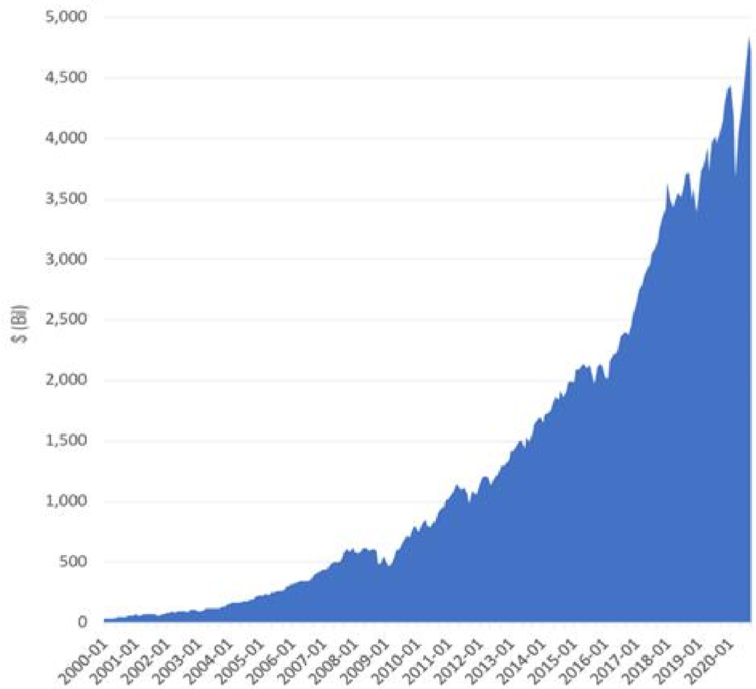
Holding onto words that teach me
I will conquer space around me
So maybe I'll win (saved by zero)…

(From "Saved by Zero" by The Fixx, 1982)

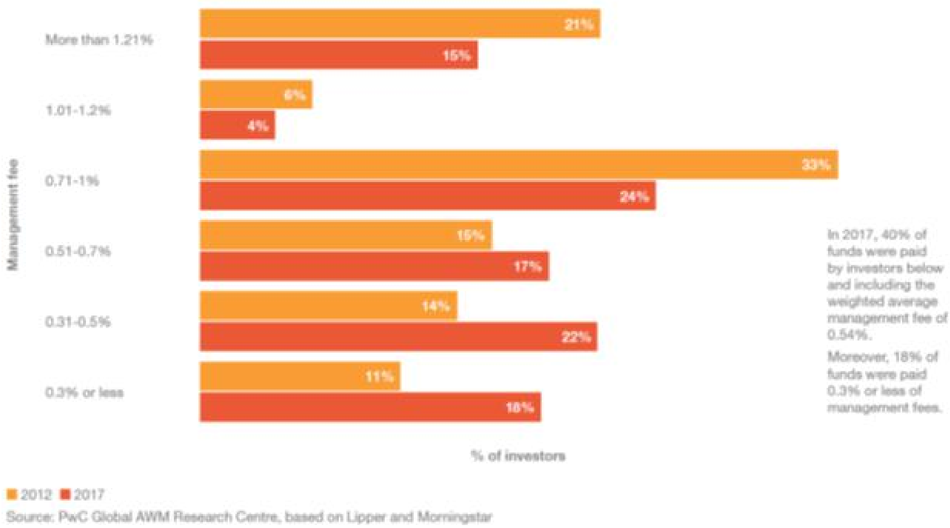
Few would disagree that the wealth management industry is becoming increasingly competitive. Many refer to the current state of the industry as "a race to zero." This is true on both the asset management side and the advisory side.

On the asset management side, the explosive growth of ETFs has put significant pressure on active management fees:

The Exponential Growth of ETFs Since 2000



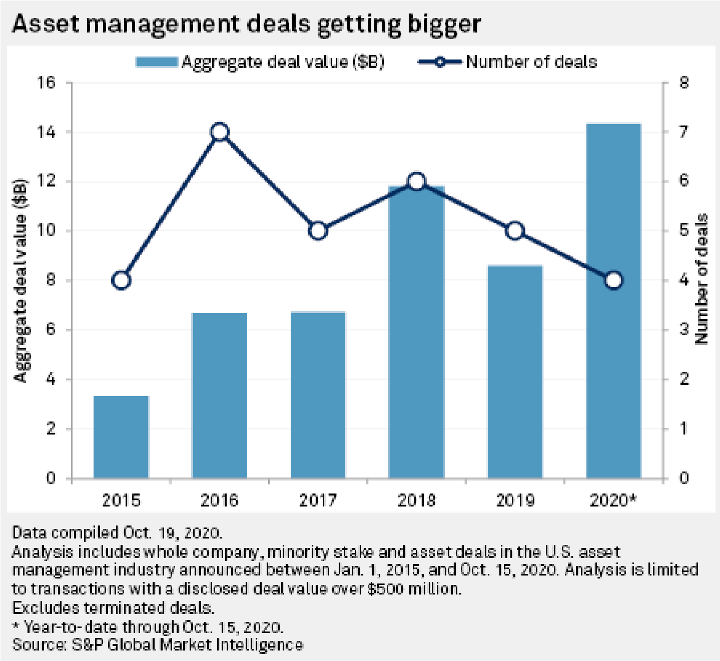
Source: Morningstar, data as of September 30, 2020. The data above represents Assets Under Management and not investment performance.



Source: PWC, "Asset & Wealth Management Revolution: Pressure on Profitability," 10/18.

Even within the ETF space itself, we see continued downward pressure on the expense ratios for passive market beta products, up to and including zero fees, rebates on fees and even paying investors to invest.[1]

This fee pressure and the movement by both institutional and retail investors toward ETFs led to dramatic consolidation within the industry in 2020:



Source: S&P Global Market Intelligence, 10/20

Distribution Analysis of Management Fees: Active Mutual Funds, 2012 vs. 2017

Advisors are facing similar competitive pressures. While fees have not felt the same level of downward pressure as in the asset management industry, it is happening. Clients want either lower fees or higher levels of service for the fees they pay.

One result is that there has been a distinct shift toward financial planning and holistic advice, and away from investment management as an advisor's primary value proposition.

In 2020, Envestnet MoneyGuide published the results of a survey of financial advisors.[2] Some of the key highlights of this survey include:

- **Demand for financial plans is growing:** The number of clients with a financial plan has been increasing since 2015. More than half (55%) of advisors' clients have a financial plan in 2020, up from 48% in 2015. In addition, advisors providing comprehensive planning grew 39% from 2017.

- **3 out of 4 advisors charge some type of planning fee:** Advisors charging a fee, commission or via AUM for financial planning has jumped to 72%, up 8% from 2017. Of the 38% of advisors who charge a separate fee for a financial plan, almost two-thirds (65%) charge a flat fee and almost one in five (18%) charge an hourly fee. Interestingly, 8% charge a subscription fee. Additionally, 29% of advisors who charge some type of fee are considering implementing a different fee model in the future. For example, of those advisors, 44% are now considering implementing a subscription model in the next 12 months.

- **Financial planning fees are on the rise:** Since 2015, we have seen an increase in fees charged. Flat fees went up by almost 50%, averaging $2,482, and hourly fees went up almost 25%, to $257. On the other hand, those who charge as a part of AUM have maintained a fee rate steady around 1% since 2015.

Another aspect of this evolving industry business model is that to successfully grow enterprise value, scale and efficiency are paramount. One way to accomplish this is consolidation, and 2020 was a banner year for mergers and acquisitions in the wealth management industry, despite (or perhaps because of) the Covid-19 pandemic:

Source: Mark Bruno, The State Of M&A Activity In The Wealth Management Industry, Forbes Magazine, 10/08/20.

Another way to drive scale and efficiency in an enterprise is through the use of outsourcing. There is no shortage of outsource providers in almost every aspect of running a wealth management practice—accounting, legal, marketing, compliance, performance reporting and so forth.

In the WisdomTree context, this means the use of [WisdomTree Model Portfolios]. We have written extensively about our models solution, including how the use of [models can help drive scale and efficiency in a practice].

We have also done extensive research on how both advisors and [clients view the use of model portfolios]. The bottom line is that most clients have little to no reservations about advisors using third-party model portfolios if it helps them achieve their long-term investment objectives. In fact, many of them view the use of models as a distinct positive, and a majority indicate they would consider switching advisors if they knew the advisor used model portfolios.

Despite these survey results, we recognize that many advisors still view investment and portfolio management as a primary value proposition of their practice, which is why we are happy to work with advisors to build customized model portfolios tailored to their specific practices and investment objectives.

We want to be viewed as an extension of already in-house investment expertise, helping advisors deliver institutional-quality portfolios to their clients and, oh, by the way, helping those advisors drive scale and efficiency in their practices.

In addition to assisting with investment management, WisdomTree has also developed an award-winning [Advisor Solutions Program] that retains professional experts to help advisors with other aspects of running their practice—optimizing their online presence, recruiting and retaining appropriate professionals, retirement planning, improving communication and persuasion skills, and business transition and succession planning.

The race to zero is tough, and some will not finish. But the advisors who have the best opportunity to survive and thrive in this increasingly competitive marketplace will be those who

1. Focus on their core competencies
2. Enhance their retirement and financial planning offering
3. Understand that their clients are objectives-based and not benchmark-based
4. Optimize their online presence
5. Access professional outsourcing solutions

WisdomTree created our Model Portfolios and our Advisor Solutions Program to do just that—help advisors maximize their potential to deliver a successful, profitable and differentiated client experience.

[1]See https://www.cnbc.com/2019/10/10/who-won-the-zero-fee-etf-war-it-looks-like-no-one.html. It should be noted that these somewhat exotic fee structures have, to date, not been sufficient to drive significant asset flows into those products. It appears the phrase "there is no such thing as a free lunch" still resonates with many investors.

[2]Envestnet MoneyGuide, "State of Financial Planning and Fees: The Bigger Picture," https://www.envestnet.com/press/envestnet-moneyguides-latest-advisor-survey-finds-financial-planning-services-fees-rise.

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Expense ratio : The annual fee that all funds or exchange-traded funds charge their shareholders

Passive : Indexes that take a rules-based approach with regular rebalancing schedules that are not changed due to market conditions.

Beta : A measure of the volatility of a security or a portfolio in comparison to a benchmark. In general, a beta less than 1 indicates that the investment is less volatile than the benchmark, while a beta more than 1 indicates that the investment is more volatile than the benchmark.