Global fund services made simple

- Alternative investment administration
- Compliance
- Custody and lending
- Distribution and marketing
- Exchange-traded products
- Fund accounting and administration
- Mutual fund administration
- Transfer agent and shareholder services

Get to know us at **usbank.com/globalfundservices**

usbank

U.S. Bank Global Fund Services is a wholly owned subsidiary of U.S. Bank, N. A. Custody and lending services are offered by U.S. Bank, N.A.

U.S. Bank Global Fund Services (Ireland) Limited is registered in Ireland with the Companies Registration Office Reg. No. 413707 and Registered Office: 24-26 City Quay, Dublin 2, Ireland. U.S. Bank Global Fund Services (Ireland) Limited is authorised and regulated by the Central Bank of Ireland under the Investment Intermediaries Act, 1995

U.S. Bank Global Fund Services (Guernsey) Limited is licensed under the Protection of Investors Law (Bailiwick of Guernsey), 1987, as amended by the Guernsey Financial Services Commission to conduct controlled investment business in the Bailiwick of Guernsey.

Investment products and services are:
NOT A DEPOSIT • NOT FDIC INSURED • MAY LOSE VALUE • NOT BANK GUARANTEED • NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY

Global Fund Services

Plan for the bigger picture.

With our attention to the details.

usbank

Together, we're your advantage.

As your fund administrator, for the past 50 years we have provided expertise, powerful decision-making tools and scalable solutions to keep you moving forward. We're continuously expanding our network across global financial markets to deliver not only services, but unique perspectives to help you navigate shifting landscapes.

We're always thinking about the next step, so you can go further.

At U.S. Bank Global Fund Services, we pride ourselves on helping our clients navigate complex products and strategies. You can rely on us to be more than merely capable of performing a service, but be fully immersed in it. From mutual funds and series trusts to ETFs and alternative products, we continue to invest in the solutions that matter most to you.

MONEY management executive

The Premier News Source for Asset Management Leaders

September 2019 | Volume 27 • Number 9 | mmexecutive.com

SPECIAL REPORT

TECHNOLOGY: AI, automation and applications — how firms are innovating

By Rebecca Stropoli

Digital innovation increasingly plays a key role in asset management.

By next year, according to PwC's report "Asset Management 2020: A Brave New World," most global asset managers will have a chief digital officer. Investment in technology and data management will continue to be critical to distribution, and to managing regulation, reporting and operations.

Money Management Executive reached out to industry leaders to get their take on the latest trends in tech disruption.

"Asset managers, like many businesses today, are being asked to do more with less," says Teri Shepherd, president of Carson Group. "The only way this can be accomplished is by automating certain processes."

Teri Shepherd, president, Carson Group

Chida Khatua, CEO, EquBot

Chida Khatua, CEO of EquBot, adds: "Opportunities for asset management firms to develop ever more customized AI-driven approaches will be a major boon for firms."

For more on what Shepherd, Khatua and other executives had to say about the future of technology in asset management, read our special report.

SPECIAL REPORT, on page 6

PRODUCTS: Vanguard's social-investing error prompts funds to check controls

By Annie Massa, Emily Chasan and Rachel Evans

Asset managers overseeing trillions of dollars in ETFs have been quietly meeting around Wall Street in recent weeks to check the quality controls on their funds, rattled after Vanguard mistakenly added shares of 11 companies, including a gun manufacturer and a private prison operator, to its $578 million socially responsible ETF.

Vanguard apologized to investors, citing a mistake in the underlying index provided by FTSE Russell, and both companies are adding new controls in the aftermath of the error, according to Vanguard spokeswoman Carolyn Wegemann.

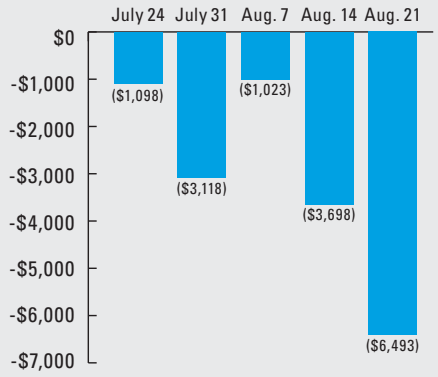
FTSE has agreed to provide justification for all future additions to its ESG benchmarks, and Vanguard will review them independently, she said.

FTSE is "committed to strengthening our processes in this space," according to company spokesman Tim Benedict. He declined to explain how the mistake was made or give any detail about how the firm is responding.

While the error at Vanguard was short-lived and the dollar value small, the mishap raises new questions about how ETF managers monitor the indexes that underlie their portfolios, regardless of whether they have a socially re-

VANGUARD, on page 15

Outflows from long-term mutual funds were $6.5B for the week ending Aug. 21 (millions)



Source: Investment Company Institute

INDUSTRY HIGHLIGHTS

VANGUARD REOPENS DIVIDEND GROWTH FUND

Vanguard announced the reopening of the $36.6 billion Vanguard Dividend Growth Fund (VDIGX) to all investors, effective immediately.

Vanguard closed the fund to most new accounts in July 2016, seeking to protect the interests of existing shareholders by reducing cash flow after a period of rapid growth, according to the firm. Cash flow has subsequently subsided and market conditions have changed since the fund's closing.

"After careful analysis of the fund's current cash flows and asset level, and following consultation with the fund's advisor, we're confident that there is ample capacity to reopen the Fund," said Matthew Brancato, head of Vanguard's portfolio review department.

Vanguard also announced plans to broaden access for sophisticated investors to two actively managed alternative investment funds, the Vanguard Alternative Strategies Fund (VASFX) and Vanguard Market Neutral Fund (VMNFX).

SPROTT TO ACQUIRE TOCQUEVILLE GOLD STRATEGIES

Sprott and Tocqueville Asset Management have entered into a definitive agreement regarding the sale of Tocqueville's gold strategy asset management business to Sprott Asset Management, according to the firm.

The Tocqueville gold investment team, composed of senior portfolio manager John Hathaway and portfolio managers Douglas Groh and Ryan McIntyre, will join Sprott Asset Management on closing.

Based on current asset levels, the transaction will potentially add $1.9 billion to Sprott's AUM, the firm said.

RESEARCH

CAN ORGANIZATIONAL CULTURE DRIVE FUND PERFORMANCE?

Asset managers are more likely than other sectors to say employees regularly go above and beyond the requirements of their jobs, 69% versus 59%, respectively, according to a study. As much as 18% of employees in the industry are also more likely to be highly engaged, outpacing other sectors, according to findings from Oxford Economics and Grant Thornton.

Asset management employees are less likely than others to say their organization's goals for culture include team mentality and collaboration, 46% versus 56%, respectively, or personal accountability for work, 41% compared with 52%.

Nearly 70% of asset management executives say their culture facilitates innovation, compared with 59% of all other industry exectives, the study found. Also, 56% of asset management employees are more likely to say they are fulfilled by their career compared to other industries, at 47%.

RECORD ASSETS IN GLOBAL ETFs AND ETPs

Global ETFs and ETPs gathered net inflows of $60.2 billion in July, bringing the year-to-date net inflows to a combined $269.7

ETF estimated net issuance ($ millions)

	5/3/2017	4/26/2017	4/19/2017	4/12/2017	4/5/2017
Equity	3,534	11,601	4,725	3,101	-6,111
Domestic	-4,264	6,757	1,253	-2,666	-12,761
World	7,798	4,844	3,472	5,767	6,650
Hybrid	-1,393	566	-596	-665	-1,467
Bond	7,171	8,614	3,229	4,275	11,131
Taxable	6,937	7,960	2,743	2,963	10,578
Municipal	234	653	487	1,312	553
Commodity	-14	-7	740	111	-125
Total	9,299	20,774	8,099	6,821	3,428

Source: Investment Company Institute

MONEY management executive

1 State Street Plaza, 27th Floor
New York, NY 10004
(212) 803-8200
financial-planning.com/money-management-executive

Andrew Shilling - Associate Editor

Rebecca Stropoli - Contributing Editor

Jessica Mathews - Associate Editor

Bernadette Berdychowski - Reporter

Paola Peralta - Reporter

Scott Wenger - Group Editorial Director, Financial Planning and Employee Benefits Groups

Michael Chu - Executive Director, Content Operations and Creative Services

Louis Fugazy, Associate Publisher
louis.fugazy@sourcemedia.com
(212) 803-8773

Jamie Billington - Senior Marketing Manager

Customer Service
(212) 803-8500
help@sourcemedia.com

SourceMedia™

Gemma Postlethwaite	Chief Executive Officer
Sean Kron	Chief Financial Officer
Jeff Mancini	Chief Strategy Officer
Dave Colford	Chief Revenue Officer
David Evans	Chief Content Officer
John DelMauro	SVP, Conferences & Events
Lee Gavin	VP, People & Culture

Subscriptions: Domestic rates: Annual $1,750; 2-year $3,500. Foreign rates: Annual $1,750; 2-year $3,500. Multiple subscription rates available.
POSTMASTER: Please send all address changes to **Money Management Executive**/One State Street Plaza, New York, NY 10004. For subscriptions, renewals, address changes and delivery service issues contact our Customer Service department at (212) 803-8500 or email: help@sourcemedia.com.

billion, according to a report from ETFGI, an independent research and consultancy firm covering trends in ETFs and ETPs.

Assets invested in the global ETF and ETP industry have increased by 1.7%, from $5.6 trillion at the end of June to $5.7 trillion, setting a record, according to ETFGI's July 2019 Global ETF and ETP industry landscape insights report.

PRODUCTS

BP CAPITAL LAUNCHES RENEWABLE ENERGY ETF

The index is composed of two distinct constituent groups. The first constitutes 75% of the total index weight, and consists of companies with meaningful revenue from renewable energy production or participation in businesses that rely on renewable energy, such as green transportation.

The second group constitutes 25% of the total index weight and includes companies that are leaders in meeting their primary energy requirements from renewables.

Renewable energy revenue and renewable energy usage are determined by data from Sustainalytics, a provider of global ESG research and ratings.

NORTHERN TRUST ANNOUNCES PERFORMANCE REPORTING TOOL

Northern Trust launched an analytics tool aimed at providing institutional investors with insights tracking, and analyzing risk and performance across their portfolios.

The enhancement introduces Performance RADAR, a proprietary reporting tool providing users with performance data, attribution, contributions and ex-post risk results online across individual and aggregated portfolios.

Northern Trust is leveraging new technologies to deliver more efficient processing and content integration alongside enhanced visualization capabilities. The introduction of persona-based set up enables speed of implementation while delivering the most relevant information to each user.

KENNEDY CAPITAL UNVEILS ESG SMALL- AND MID-CAP FUND

Kennedy Capital Management released a small- and mid-cap mutual fund in accordance with ESG principles, the firm announced. The strategy focuses on companies that have an environmental or societal advantage to effectively compete in the market.

"We believe the small- and mid-cap investment universe offers compelling opportunities for ESG-oriented investors, and our investment team is well-positioned to help clients capitalize on the unique characteristics of this portion of the equity market," said Donald Cobin, CEO of Kennedy Capital.

LOOMIS SAYLES GROWS INSURANCE CAPABILITIES

USFC announced the firm has added its suite of ETFs to FundVestETF, BNY Mellon Pershing's no-transaction-fee ETF platform.

"We have enjoyed a longstanding relationship with Pershing and are excited to participate in FundVest ETF," said USFC CEO John Love. "Investors are always looking for ways to differentiate their portfolios and now can include alternatives in their mix while accessing Pershing's no-transaction-fee environment."

VANECK, SOLIDX ANNOUNCE ETF-LIKE BITCOIN PRODUCT

VanEck Securities and SolidX Management, firms that have together petitioned the SEC for more than a year to approve an ETF that tracks bitcoin, announced a new product it says will use Rule 144A of the Securities Act of 1933 as a workaround to do just that, according to Bloomberg News.

The fund, if approved, would be the first bitcoin product for institutions that features the same creation-and-redemption process found in traditional ETFs, the firm said.

"We are in the midst of a sea change for institutions, for the bitcoin ecosystem and for how market participants define an ETF," said Daniel H. Gallancy, CEO of SolidX.

ARRIVALS

AMERICAN CENTURY HIRES 3 PORTFOLIO MANAGERS

American Century Investments announced the addition of three senior portfolio managers from Dimensional Fund Advisors to support Avantis Investors, the firm's newly launched suite of tax-efficient, low-cost investments slated to launch later this year, according to the firm.

Former Dimensional portfolio manager and Vice President Ted Randall, former senior portfolio manager and Vice President Mitchell Firestein and former senior portfolio manager Daniel Ong bring a combined 45 years of investment management experience to their new roles.

"I worked with them all for over a decade and know they have critical skills that will help us bring reliable, cost-effective and well-diversified investment solutions to our clients. This is an exciting time, and I'm pleased to welcome them to the team," says the firm's Chief Investment Officer Eduardo Repetto.

Daniel Ong

The new strategies managed by the trio are available in both ETF and mutual fund wrappers, and are expected to rely on a proprietary investment approach based on market prices, the firm said.

BRITISH ASSET MANAGER JOHCM APPOINTS CEO OF U.S. BUSINESS

J O Hambro Capital Management, a U.K.-headquartered active asset management company with offices in London, Boston, New York and Singapore, has appointed former State Street EVP and chief growth officer Nick Good to CEO of its U.S. business, according to the firm.

Good, previously responsible for setting overall business strategy and leading corporate development at State Street, will now lead JOHCM's business in the U.S. from the firm's Boston office.

"Nick's leadership and achievements with global asset managers made him the prime candidate to lead our U.S. business," said Emilio Gonzalez, CEO of Pendal Group, JOHCM's parent company. "He has built and grown successful businesses, has deep knowledge of the market and a track record of delivering results." MME

News Scan by Bernadette Berdychowski and Paola Peralta

What Do New Regulatory and Fintech Developments Mean for Your Firm?

Find Out at ICI's 2019 Tax and Accounting Conference

New regulations and technological innovations are changing asset management, and only one event can help you stay one step ahead: **ICI's Tax and Accounting Conference**. Taking place **September 22–25** in **Marco Island, Florida**, this popular event will feature dynamic speakers and in-depth panels, covering a wide range of issues, including:

Domestic and international tax developments	Blockchain and cryptocurrency	Artificial intelligence	SEC reporting modernization	Diversity and inclusion

SPACE IS LIMITED—register today at **www.ici.org/tac**

ICI INVESTMENT COMPANY INSTITUTE®

Milestone Group Chief Technology Officer Phil Davies

Moving away from costly complexity

In asset management, the current technological transformations are vast. CTOs are actively looking to simplify their application architectures to eliminate all unnecessary replication of data and the resultant need for data movement, reconciliation and validation. This is certainly a cost-driven initiative, but also relates to risk and business agility, as firms try to remain relevant in a rapidly changing market.

While nobody suggests that a complex investment business will run on a single platform in the near term, there is a significant trend towards rationalization of systems by moving to a limited number of multi-solution platforms that provide support across multiple business functions, products and asset classes.

This macro trend goes hand in hand with the more heavily discussed themes around standardization of architecture and applications across business lines and geographies, and of course the acceleration of shifting to managed Cloud-based IT infrastructures.

IT departments in asset management firms, now more than ever, need to maintain competitive technological capabilities with limited resources.

Traditional build versus buy decisions are, for the most part, already answered before the analysis is started. Individual firms generally no longer have the human capital to entertain competing with maturing global fintech platforms, which have superior scale, R&D capabilities and agility.

Asset managers must move away from implementing costly and overly complex architectures that are difficult both to manage and change. Some asset managers have become overly dependent for technological advancement on administrators who struggle to maintain the pace of innovation that will match that of fintech firms.

A notable development in Gen 3 outsourcing models is that they are increasingly technology driven with a focus on data, collaboration and hardened oversight and backup NAV capabilities.

These trends are driving a lot of focus on a new operating paradigm to remove friction and contain the costs for asset managers.

Carson Group President Teri Shepherd

The importance of automation

Automation will continue to be at the forefront of strategic planning.

Simply put, asset managers, like many businesses today, are being asked to do more with less. Sell and satisfy more consumers, with less overhead. The only way this can be accomplished is by automating certain processes. On the operational side, that can mean marketing automation, workflows for lead generation and more sophisticated digital compliance and supervisory solutions. On the investments side, that might mean automating risk assessment, market research and trading.

While today's technology is unquestionably more sophisticated and offers higher quality solutions, major problems arise when those tools can't communicate effectively with one another or if the data provided is inaccurate. Integration is key.

The ability to link as much as possible together — creating a single pane of glass — has become a critical differentiator in driving business growth and attracting talented employees. This could include client relationship management (CRM) tools, marketing software, online portfolios, reporting and trading platforms.

This then leaves the internal teams with the ability to focus on the bigger picture and what's best for their clients.

While technology enhancements and collaborations are on the horizon — they are not and will not replace genuine interactive client relationships.

Technology is just a conduit to deliver advice and services more efficiently and transparently for the benefit of the end consumer.

Helios Quantitative Research Chief Investment Officer Joe Mallen

Increasing innovative options

The operational reality for financial advisors is rooted in two key factors right now:

1. Investors are better educated than ever before, and they expect their advisors to know more and provide better results.

2. The advisor marketplace is crowded, and the need to make a real difference for clients is vital to winning business.

Asset managers need to help advisors face these challenges, and managers who harness the power of technology have the ability to be better partners.

We see two key avenues for asset managers to succeed in this realm:

1. They should provide innovative products.

2. They should offer a wider range of solutions.

Advisors are looking to asset managers to design retail-friendly products with a simple story.

Managers who use technology to assess historical trends and design innovative solutions will be the most successful in partnering with these advisors, and satisfying their specific needs..

The level of data that is available to make educated and high-probability decisions is continuously growing.

Embracing technology to make sense of this data can enable advisors to confidently invest their clients' assets.

Managers with a wider array of offerings prove to be stronger partners to advisors as well. Embracing technology can, among other things, help expand services and help advisors run a leaner practice.

We recognize that advisors are looking to do more with smaller teams and still need to find ways to successfully engage the next generation in order to fortify the future of the practice.

Thus, we offer solutions that create new revenue opportunities, save time and drive overall efficiency for the business.

As more advisors look to outsource key services, asset managers who are leveraging technology stand to be better prepared to compete and add differentiated value.

EquBot CEO Chida Khatua

Tracking the AI evolution

When we look to the next evolution of asset management and the role AI will play, we consider three key factors that will continue to drive the use of AI and machine learning

First, data. Ninety percent of all data in existence was created in the past two years, and that pace will only increase. Consequently, decision-making and data analysis will become more of a challenge for the traditional fundamental researcher or manager.

Having the ability to quickly assimilate and understand all this data and make unbiased decisions will therefore not only be advantageous to the forward-thinking asset manager, it will be essential. And, despite the concerns that human jobs will be lost to machines, we believe it's unlikely AI will operate as a complete replacement for human managers and analysts.

Second, innovation around AI-powered products and approaches continues to develop. The introduction and availability of AI-powered investment products and tools is opening new doors for investors. Further, as the category grows, opportunities for asset management firms to develop ever more customized AI-driven approaches will be a major boon for firms.

Third, to the point above, financial institutions are seeing these technological enhancements being applied and reported across other industries. Asset management has historically been somewhat behind the curve when it comes to incorporating new technologies, but we're seeing more direct investment by financial services firms into AI and ML, with the goal of making better investment decisions and becoming more efficient. MME

No one dives deeper into wealth tech

December 5-6, 2019 | San Francisco, CA

Meet the Event Chair

Sebastian Dovey returns to the In|Vest West stage to host this year's digital wealth journey. Dovey is a successful entrepreneur, thought leader, angel investor and board advisor in the fields of global wealth management, consumer insight, scale-up companies and business management.

Register today at InVestWest.Events

IN|VEST WEST

Seize Opportunities in Model Access and Delivery to Create a More Scalable, Efficient Firm

MODERATOR

Lisa Joyce
Contributing Editor,
SourceMedia

Models are a powerful tool to create efficiencies and have become an important part of the investment strategies for asset and wealth managers. But due diligence of how firms provide and deploy models can be burdensome and reporting on and managing a large number of manager relationships can be a challenge. The key for asset and wealth managers is to understand how to use models most effectively.

In August, SourceMedia hosted an executive roundtable with experts in model access and delivery to cut through some of the confusion and complexity of models. Participants shared their insights into the future of what a model driven and distributed investment management will look like.

What follows is an edited version of the lively and informative discussion.

PARTICIPANTS

Jeff Kilburg
Founder and CEO,
KKM Financial

Tom O'Shea
Director of
Managed Accounts,
Cerulli Associates

Steve Camp
Managing Director,
Vestmark Advisory
Services

Alexander Morris
Founding Principal,
Vestmark Manager
Marketplace and
Managing Director,
Vestmark Advisory
Solutions

SPONSORED BY

Vestmark

PRODUCED BY

SourceMedia™ MARKETING SOLUTIONS GROUP | Money Management Executive

Lisa Joyce: How does a model differ from a separately managed account (SMA) or unified managed account (UMA)?

Steve Camp: A model is typically a list of securities from a model provider. Think of a model as a building block for an account. A SMA is a single-style account that is tied back to one model while an UMA can support multiple models and can be tied to an asset allocation strategy. And the latter is where we start to truly see some of the model efficiencies and better outcomes for the end investor come into play.

Lisa Joyce: Is model use growing?

Tom O'Shea: Many asset managers are getting into the model business because they can use models to influence the use of mutual funds and ETFs. The model marketplace consist of about 12% of advisors representing about $2.4 trillion in assets outsourced to a model provider.

About 45% of advisors will never use models. There's also a sizable segment of advisors who use models but then modify them.

Lisa Joyce: What are some of the benefits for advisors in building a model-based business?

Jeff Kilburg: Models allow sophisticated, successful advisors to articulate and formalize their investment strategy while they simplify and scale their practice. And most importantly, models give advisors more time to focus on their clients. Implementing a models-based practice saves about 450 hours a year—or one day per week.

Models also create a consistent, repeatable process that really makes the compliance officers happy.

Lisa Joyce: What should asset and wealth managers consider when deciding which models to use?

Alex Morris: Start by asking if it's appropriate for someone else to implement the strategy you are trying to deliver. Next, consider the counterparty who's going to trade it. Who is on the receiving end of that model? How well is it traded? What are the tools being used?

Models generally come at a lower cost than a traded experience, but if the performance, or alpha, is stripped out, a model probably does not make sense for that strategy and its investors.

Lisa Joyce: What are the leading wealth manager or sponsor reasons to use models? Why do mutual funds and SMAs even still exist?

Tom O'Shea: Advisors are feeling the price compression impacting the entire financial services industry and they recognize that they need to become more efficient. Outsourcing asset management to models is one way to do that.

The second reason asset and wealth managers use models is consistency of returns. The industry has moved to a much more fiduciary position and firms are realizing that a lot of their advisors don't perform well. As a result, many large wealth managers are coaxing advisors into models to get better returns for their clients.

And the third reason is that outsourcing investment selection and portfolio construction to a third party frees the advisor to do the things that really matter to the client.

SMAs still exist because, in certain asset classes, it's hard to deliver certain strategies in a model. For example, there's still value in asset managers trading fixed-income or municipal bonds.

Jeff Kilburg: Advisors who make bespoke investments aren't able to create a consistent repeatable process. The standard deviation in those versus a model portfolio is two-times.

Tom O'Shea: I agree. Not only are bespoke investments riskier with greater volatility, they underperform. On average, we've seen a couple hundred basis points in underperformance for advisor-managed portfolios versus a models-based portfolios over a five-year time period.

Steve Camp: Performance is key. You cannot dilute the performance provided from the asset manager or advisor. If you're seeing a hit on performance in the model versus the SMA, it makes sense to move to a pursue the SMA relationship.

Alex Morris: SMAs traded directly by a manager remain appropriate in those asset classes. Models provided by those managers efficiency and customization. Advisors can take a model and tweak its implementation achieve investors' needs. And ultimately that is where Advisors should spend their time – helping investors' achieve their financial aspirations, not constructing, implementing, tweaking, etc their own models.

"Most forward-thinking advisors and advisory firms are combing models and analyzing the risk return in the portfolio."

– Tom O'Shea

Lisa Joyce: Ideally advisors won't have to choose performance over efficiency—or vice versa. Can managers and sponsors really have it both ways?

Steve Camp: Yes. Vestmark has developed advanced technology around models that allows asset managers to customize models to add alpha. We expose that manager to a discretionary sleeve so they can directly manage it but it's still within the model marketplace.

For sponsors, models provide additional product opportunities and give advisors more options to choose from.

Lisa Joyce: How do managers choose between the models available?

Tom O'Shea: Since a lot of models are strategic asset allocation models of index ETFs or index mutual funds, advisors look at tracking error. They also look at the brand offering the model and, of course, price. Most forward-thinking advisors and advisory firms are combing models and analyzing the risk return in the portfolio.

Lisa Joyce: How do you recommend that asset and wealth managers get started with models?

Jeff Kilburg: Start with small accounts such as retirement accounts under $100,000. Once you create a formal articulated process, move to larger accounts.

Steve Camp: Think about what you are trying to deliver as an advisor and narrow down your model choices to a handful of providers that have a brand you trust and a solution that suits your needs and your investors.

Also consider time and expertise. Does the advisor have the expertise to pick the individual models? If not, advisors may be better going with an outsourced chief investment officer (OCIO) provider.

Jeff Kilburg: The whole model conversation is moving towards that turn-key solution. The faster growing models are on the asset allocation side.

Lisa Joyce: What about fees?

Jeff Kilburg: There's fee sensitivity but alpha continues to be the overarching theme.

Tom O'Shea: Absolutely. If you're going to get paid for it, you have to generate alpha. But so much of what we're seeing now in models is just pure beta plays that are completely or largely passive.

Lisa Joyce: Why did Vestmark build the Vestmark Model Marketplace (VMM)?

Alex Morris: Like a lot of good ideas, VMM came out of frustration. I was a client before joining Vestmark. It was a challenge to make all the different models work in unison with the other platforms that we ran.

We wanted to solve that problem by building a model marketplace with a single-entry point for all asset management content that asset managers, sponsors, and model providers could access. We wanted to build the marketplace in a way that was conflict free. We don't provide investment recommendations or charge asset managers to particiate. We're not conflicted in any of the distribution content on the system.

Steve Camp: I agree that no conflict is the foundation of VMM. We are not involved in individual stock selection nor do we offer advice on which model to use. We do take discretion and we will trade accounts.

Lisa Joyce: How does the model marketplace work?

Steve Camp: Our technology allows us to remove much of the friction. Vestmark has one contract with a model provider and one contract with a model consumer to reduce the contractual obligations of both entities. Vestmark performs due diligence on both entities. We enable model providers that would never be able enter this space join our marketplace.

Model providers want to make sure that the model implementer is maintaining their performance standard so we require that the consumer of the model report key data points to us so we can calculate performance. We provide transparency to all entities to make sure that performance standards are being met.

"We provide transparency to all entities to make sure that performance standards are being met."

– Steve Camp

Lisa Joyce: How does the Vestmark Model Marketplace fit into a distribution strategy?

Alex Morris: If you no longer have access to all of your accounts every day, it's very hard to answer the simple question of how much assets do you manage. Managers are very happy to have easier-to-understand normalized data sets that enable them to more efficiently run trade rotation.

From a sponsor standpoint, if you have 200 to 300 managers on a pretty dynamic program, you need one or two full time staff members to keep those managers fed and happy with data. By centralizing data in one place, we're able to deploy technology with a very sophisticated set of capabilities. We are also able to retain a very deep bench of talented people in our enterprise that we probably couldn't otherwise justify given the fee compression in the industry.

Steve Camp: As the use of models grows, distribution becomes key. You have to provide that model in a very simple and efficient manner—which is what Vestmark excels at. We can even implement the model.

Tom O'Shea: Models give asset managers an opportunity to really deepen their relationships with their distribution partners. In the past few years, the major distribution firms have simplified their product set by decreasing the number of mutual funds and company partnerships they have. That's put a lot of pressure on mutual fund distribution teams to try to retain relationships.

One way to strengthen relationships with distribution partners is to provide them with asset allocation capabilities not only at the firm level, but also at the advisor level. Distribution executives at asset management firms tell us that if they can get someone to use their models, they're

going to be a stronger customer and stay with them through downturns and subpar performance of specific asset classes.

Lisa Joyce: What type of opportunities do models provide for asset and wealth managers?

Jeff Kilburg: The opportunity is limitless. Advisors no longer have to spend 40% of their time administrating portfolios or trading portfolios and making investment decisions.

A model-based practice not only simplifies your practice; it scales your practice with a consistent and repeatable investment process.

Tom O'Shea: Exactly. If you're not sitting around picking stocks and reconciling accounts, you have more time to go out and market yourself to clients, which is how you grow a business.

Jeff Kilburg: We're seeing financial advisors, on average, grow their business 23% through client acquisition. That's a phenomenal number.

"We provide transparency to all entities to make sure that performance standards are being met."

– Jeff Kilburg

Steve Camp: From the wealth manager side, there are more creative models available today. It's not just pure large cap equity, midcap, or small cap. We're seeing ETF and mutual fund models with asset allocations built into them. Wealth managers should be open and looking for new entries into this space that will help complete their product sets.

Lisa Joyce: We've talked about efficiency and performance, but what about risk?

Alex Morris: By centralizing this content and moving some of the implementation to a seasoned pro, there is increased consistency in implementation. If you have to spend most of your day worrying about all of the other things you didn't do or the things you should have been doing, you're not driving new sales or spending ample time looking after implementation.

Deep down, models really solve that problem for both asset managers and sponsors. Asset managers take some risk of being afraid that performance will miss or that their content is being misconstrued or that they might just not have the time to treat all of their accounts equally off the table. On the sponsor side, both the home office and the advisor can rest much more confidently, knowing that the content is looked after by a professional and that it's implemented consistently and regularly across the book of business.

Tom O'Shea: There's litigation and compliance risk if a firm continues to allow underperforming advisors to sell to clients. When advisors underperform, we know exactly what they were doing because it corresponds what is happening in the marketplace. They were quickly getting out of down markets, but not getting back into up markets until it was too late.

Consistency of outcomes mitigates risk for the advisor, it mitigates risk for the firm, and it delivers a better solution for the client.

Alex Morris: Models are here to stay and, most likely, are already a part of a manager's practice whether they know it or not. Managers need to understand how to use them effectively, safely, and efficiently. Knowing how to use models is better for mangers and sponsors, and it will drive better investor outcomes. That is the goal we strive for at Vestmark.

If you want more information on the Vestmark manager marketplace you can send an e-mail to **inquiry@vestmark.com.** — or visit vestmarkmm.com.

About Vestmark

Vestmark is a leading provider of wealth management solutions and services which enable financial advisors and institutions to efficiently manage and trade their clients' portfolios using an innovative SaaS ecosystem. Founded in 2001 and headquartered outside of Boston, Vestmark's mission is to enable investors to strengthen their financial well-being.

With over $1.4 trillion in assets and 4.5 million accounts, we are a trusted partner to some of the largest and most respected players across the wealth management industry. For more information about Vestmark's solutions, call (781) 224-3640, email inquiry@vestmark.com, or visit www.vestmark.com

PRODUCED BY

VANGUARD
from page 1

sponsible mandate.

Last year, S&P Dow Jones Indices failed to remove a company that axed its dividend from an index of dividend-paying companies, the Financial Times reported.

The error resulted in unexpected losses for investors in a State Street Global Advisors ETF that tracks the index, called SPDR S&P U.K. Dividend Aristocrats.

SOCIAL RESPONSIBILITY

In June, when FTSE Russell rebalanced the index, it erroneously included 11 stocks in the benchmark, including Sturm Ruger, Vanguard said. FTSE Russell said the stocks were "inadvertently included" and clients were told as soon as it fixed the mistake.

A representative for S&P Dow Jones Indices declined to comment, but said the index provider maintains "rigorous quality assurance processes."

Though the firm's Sturm Ruger buy was temporary and small — 219 shares worth about $9,000 — it raises questions about the rapid growth of socially responsible investing in general and index strategies in particular.

In September, Vanguard launched its ESGV fund, pegged to FTSE Russell's US All Cap Choice index, which excludes non-renewable energy, weapons manufacturers and so-called vice products. With a cost of just $1.20 per $1,000 invested, the fund quickly attracted about $560 million, making it the 8th-largest ESG-focused ETF.

"Though the exposure to these holdings was very modest, we regret that the error occurred and apologize to shareholders," Vanguard spokesman Freddy Martino said in a statement to Bloomberg. Vanguard's fund sold the shares Aug. 5, and Vanguard is considering adding its own additional controls to prevent future errors.

In a letter the firm sent to investors on Monday, Vanguard also disclosed that it had bought shares of private prison operator Geo and defense contractor Halliburton for the U.S. ESG fund, and erroneously included 20 additional stocks in its ESG International Stock ETF.

"Vanguard's objective in managing index funds is to track the index provided by our index partners; FTSE is instituting additional controls in their process," Vanguard spokeswoman Dana Grosser said in an emailed statement. "Vanguard continuously works to understand index provider policies, procedures and controls; this is part of our evaluation process when partnering with an index provider and part of our ongoing diligence of our index-provider partners."

"It is very much material, diametrically opposed to the objective of the index and the desires of investors in the fund."

Ben Johnson, head of passive strategy, Morningstar

QUALITY CONTROL

Fund analysts say index providers make mistakes like this on occasion, but ESG investors are particularly sensitive to what their funds do and don't hold.

Ben Johnson, head of passive strategy research for fund-tracker Morningstar, said he'd never seen an indexer veer so far from its mandate.

"It is very much material, diametrically opposed to the objective of the index and the desires of investors in the fund," he said.

Manooj Mistry, global head of index investing at DWS, which runs the third-largest ESG ETF in the U.S., says the firm's head of risk asked whether the firm was vulnerable to an indexer error. After reviewing the methodology of MSCI, which provides indexes for DWS, Mistry said he was comfortable with the asset manager's quality controls.

Regardless, portfolio management teams are responsible for what he called a "sense check," to make sure securities are appropriate for their funds.

At State Street, "portfolio management and research teams do systematic analysis to ensure that the index meets its stated objective," according to spokesman Marc Hazelton. BlackRock, which has more than $2 trillion across its ETF products including the two biggest ESG ETFs, didn't comment on how the firm monitors the holdings in its socially responsible funds. Bloomberg, parent company of Bloomberg News, also constructs and licenses indexes.

WIGGLE ROOM

Ultimately, humans have to check what's in an index, said Mike Venuto, chief investment officer at Toroso Investments, which specializes in ETFs.

Portfolio managers shouldn't be "blindly buying" what an index suggests, he said. "The index is a research tool and you can buy bad research. If it's an ESG fund, it shouldn't just be the requirement of an indexer — it should be the requirement of the manager."

ETF portfolio managers are expected to match at least 80% of their holdings to whatever index they're tracking, with wiggle room to allow for pricing execution, liquidity or other concerns. Managers are typically focused on matching a benchmark at the lowest price, rather than the qualities of the underlying holdings.

The small, Frisco, Texas-based manager Impact Shares runs three ESG ETFs pegged to indexes provided by Morningstar.

When the indexes tracked by the funds make changes, the firm reviews the rationale with social-impact partners including the NAACP and the YWCA USA, which also receive a portion of the management fees.

That process, said CEO Ethan Powell, requires Impact Shares to ask whether it's "measuring the right things, do we have the right companies in the fund for the right reasons?" — *Bloomberg News* MME