ETFs Still Reign; Planners Show Caution When Investing

by Journal staff

When it comes to investing, financial planners appear to have solidified their preference for ETFs over mutual funds, and they are showing continued signs of using caution in the market, with a steady reliance on cash and equivalents.

The FPA 2018 Trends in Investing survey, conducted by the *Journal of Financial Planning* and the FPA Research and Practice Institute™, showed that 87 percent of planners surveyed currently use or recommend ETFs to clients, and 73 percent currently use or recommend mutual funds (non-wrap). This is the widest gap between ETFs and mutual fund usage reported since ETFs overtook mutual funds in recommendation/usage in 2015.

ETF usage has continued to climb over the last eight years when survey respondents first showed a significant jump in using ETFs, with 72 percent of planners using/recommending them in 2010 compared to just 44 percent in 2008.

The 2018 survey also showed that 83 percent of planners are using/recommending cash and equivalents with clients, similar to the 85 percent reported last year, and an indication that planners are continuing to be somewhat cautious when investing. The reliance on cash and equivalents is a significant increase from the 53 percent of planners surveyed in 2006 who used or recommended this category, and a modest increase from the 74 percent of planners who used/recommended cash and equivalents in 2016.

The 2018 survey was fielded in April and May and received 265 online responses from financial planning professionals who offer clients investment advice and/or implement investment recommendations.

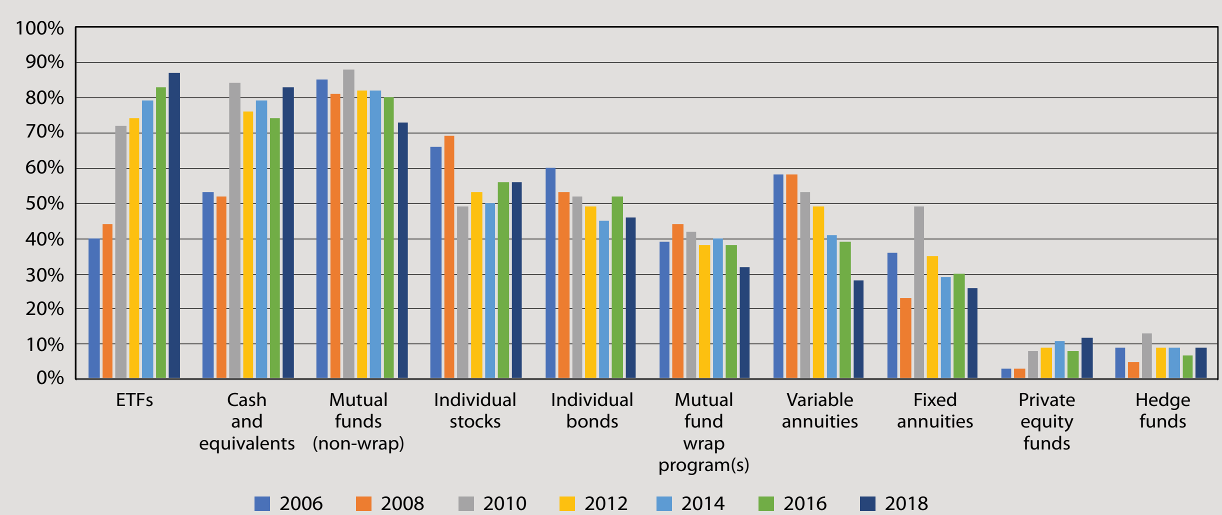
FPA's annual Trends in Investing survey was first conducted in 2006. Looking at results from 2006 to 2018, one can see the effects of the 2007–2008 financial crisis (the bar graph below illustrates this in two-year increments). By 2010, planners had clearly shifted investments out of individual stocks and into index products including ETFs and mutual funds. In 2010, planners also showed a significant shift into cash and equivalents and fixed annuities.

As the economy recovered since the 2007–2008 financial crisis, planners have shown a modest return to individual stocks, but not to pre-2010 levels, while the use/recommendation of fixed annuities has nearly dropped to pre-2010 levels.

For full survey results, download the white paper available at OneFPA.org/Business-Success/ResearchandPracticeInstitute. ■

Changes to Investment Usage, 2006–2018

Q: Which investment vehicles do you currently use/recommend with your clients?



Source: FPA Trends in Investing Surveys (not all options are displayed here, only ones comparable year-over-year; respondents could select all that apply).

How to Use the EPA Website to Advise on ESG Investing

by Srinivas Nippani, Ph.D., and Lirong Liu, Ph.D.

Many financial planners have encountered socially responsible investors who have preferences about where they want to invest their money. According to the group US SIF: The Forum for Sustainable and Responsible Investment (ussif.org), of the $40.3 trillion in assets being professionally managed in the U.S. (as of 2016), $8.72 trillion were SRI assets, up 33 percent since 2014. The 2018 FPA Trends in Investing survey showed that 26 percent of planners surveyed currently use or recommend ESG funds with clients, and 20 percent expect to increase their use/recommendation over the next 12 months.

As more clients prefer socially responsible investment strategies (also commonly called ESG investing, for environmental, social, and governance), it is essential for planners to use all sources of information to help these clients meet their investment goals. One such source is the Environmental Protection Agency (EPA).

A planner who knows how to use the EPA website can potentially help clients in two ways: (1) help SRI investors know if their potential investment is in compliance with their beliefs; and (2) be aware of information that could potentially harm the investor's return.

Check a company's violations:

1. Go to the EPA's online Corporate Compliance Screener tool at echo.epa.gov/facilities/compliance-screener.
2. Enter the name of a company to screen any violations. You can also restrict the screening to show only the specific facilities (based on company name) in certain states or regions.
3. From the search results, you can view a facility's record by clicking on its name or select several or all facilities and generate a report.

This search allows planners to quickly access a company's enforcement (including inspections and penalties) and violation history. The number of quarters a company is in significant violation can be a negative signal on the performance of the company.

Search by industry or geographic region:

1. Go to the EPA's Facility Search tool at echo.epa.gov/facilities/facility-search.
2. Use the red "Search Type" panel to search by air, water, hazardous waste, or drinking water.
3. Use the blue panel to further define the geographic location down to a particular county or ZIP code.
4. Use additional panels to confine the search to major facilities that are active/operating, to view enforcement and compliance histories, or to select among environmental conditions and pollutants.

Check for community environment information:

1. Go to epa.gov and entire a ZIP code in the "Your Community" search box.
2. Access information on that community's quality of air, water, energy, health, and climate.

A planner's knowledge of a violating firm, the severity of the violation, and the screen under which the planner puts a company should be made available to clients, so they can be comfortable with their investment decisions. ■

Srinivas Nippani, Ph.D., and Lirong Liu, Ph.D., are professors at Texas A&M University.

How Planners Invest Today

Q: Which investment vehicles do you currently use/recommend with your clients?

Survey respondents could select all that apply. Results have been ordered here by highest percentage.

Exchange-Traded Funds (ETFs)	87%
Cash and Equivalents	83%
Mutual Funds (non-wrap)	73%
Individual Stocks	56%
Individual Bonds	46%
Mutual Fund Wrap Program(s)	32%
Variable Annuities (immediate and/or deferred)	28%
Fixed Annuities (immediate and/or deferred)	26%
ESG Funds	26%
Fixed Permanent Life Insurance	23%
Individually Traded REITs	22%
Variable Permanent Life Insurance	18%
Other Alternative Investments (bought directly)	17%
Indexed Annuities	16%
Non-Traded REITs	13%
Options	13%
Private Equity Funds	12%
Hedge Funds (bought directly)	9%
Other*	9%
Cryptocurrencies	1%

* When asked to specify "other," survey respondents most commonly answered: separately managed accounts, interval funds, structured notes, and physical assets, such as collectibles.

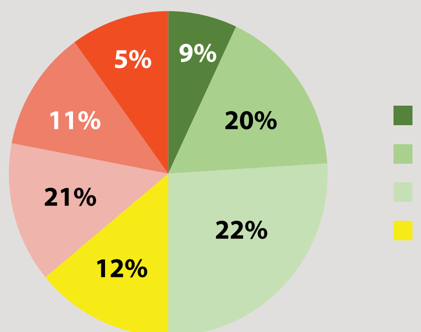
Source: FPA 2018 Trends in Investing Survey

Is a 60/40 Portfolio Still Viable?

Survey respondents were asked how confident they were that a 60/40 portfolio could provide similar returns as it has historically. A slight majority (51 percent) are somewhat to very confident in the traditional 60/40 portfolio, consistent with the 2017 results.

Meanwhile, slightly fewer planners were neutral on this in 2018 (12 percent) than in 2017 (14 percent), and only 5 percent were "very doubtful" that the traditional 60/40 mix could continue to provide historical returns, compared to 10 percent who were "very doubtful" in 2017.

Q: How confident are you in the ability of the traditional 60/40 stocks and bonds portfolio to provide similar returns as it has historically?



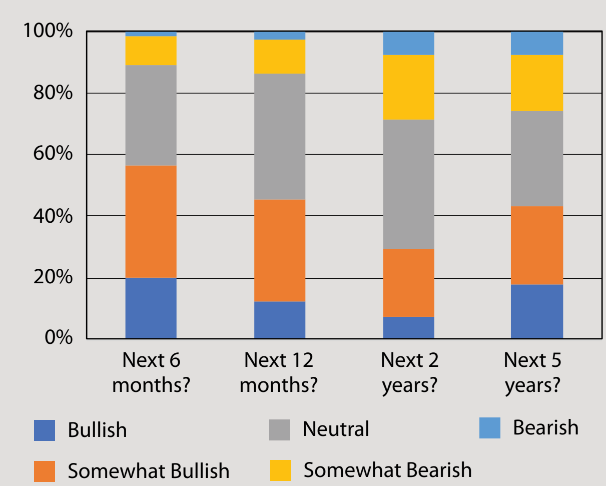
Source: FPA 2018 Trends in Investing Survey

My anticipation is that the outlook is for continued, solid growth.
— Fed Governor Lael Brainard, CNBC

Planners Bullish for the Short Term

Planners were asked about their economic outlook for the next six months, 12 months, two years, and five years. Results show that planners are generally bullish for the next six months, but their longer-term expectations for the economy are waning, with a slight uptick in bearish sentiment for their two-year and five-year outlook.

What is your economic outlook for the...



Source: FPA 2018 Trends in Investing Survey

Taking Another Look at Asset Allocation

Survey results show that most planners (68 percent) were either currently re-evaluating the asset allocation they typically recommend and/or implement, or they had done so within the last three months, compared to 30 percent who had not, and 2 percent who did not know.

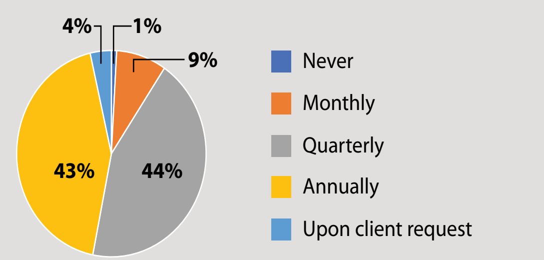
Planners who indicated they were re-evaluating asset allocation were asked about the reasons why. Many were spurred to re-evaluate because of anticipated or existing changes to the economy in general and/or market volatility. About one-third of survey respondents said tax reform (the Tax Cuts and Jobs Act) is cause to re-evaluate, and about one-third also indicated that anticipated changes in inflation is making them take another look at asset allocation. Meanwhile, 64 percent of survey respondents said they continually re-evaluate their asset allocation strategy.

I re-evaluate the asset allocation strategy I typically recommend/implement because of anticipated/existing changes in:

The economy in general	46%
Market volatility	44%
The Tax Cuts and Jobs Act	32%
Inflation	28%
Specific investments	25%
Administrative aspects of investments (cost, lead manager, etc.)	15%
Other*	7%
Health care law	3%
I continually re-evaluate asset allocation strategy I typically recommend/implement	64%

* When asked to specify "other," survey respondents most commonly answered: rising interest rates; valuation of various asset classes; and political uncertainty.
Source: FPA 2018 Trends in Investing Survey

Q: How often do you re-evaluate the asset allocation in your clients' portfolios?

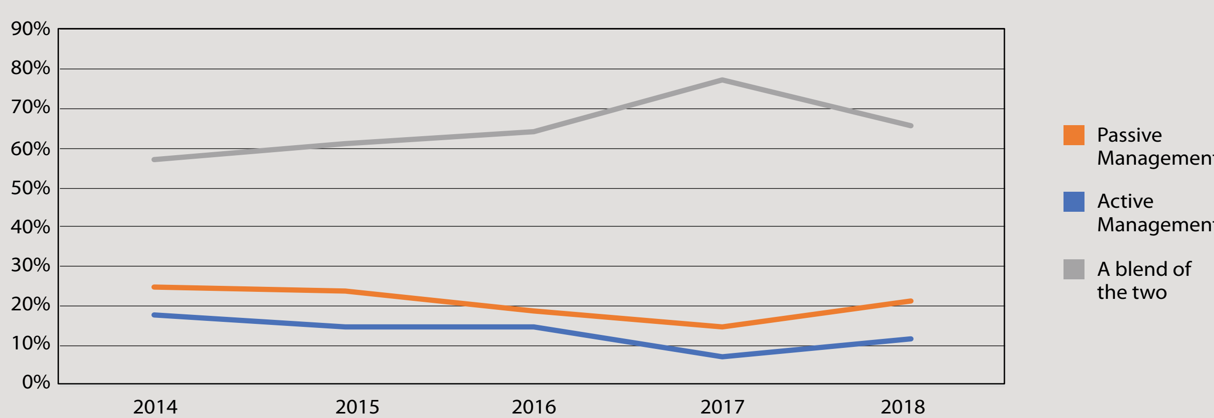


Source: FPA 2018 Trends in Investing Survey

Active Vs. Passive

Planners continue to favor a blend of active and passive management style. This has been a consistent trend over the last five years, however, results suggest a slight shift in 2018 to a bit more of a preference for a passive approach to investment management (note the increase in passive management from 15 percent in 2017 to 22 percent in 2018). As the economic and political landscape evolves, it will be interesting to continue to track this metric into 2019 and beyond.

Q: In general, which type of management do you think provides the best overall investment performance taking into account costs associated with each management style?



Source: FPA Trends in Investing Surveys