

The evolution of Vanguard Advisor's Alpha[®]

From portfolios to people

Vanguard[®]

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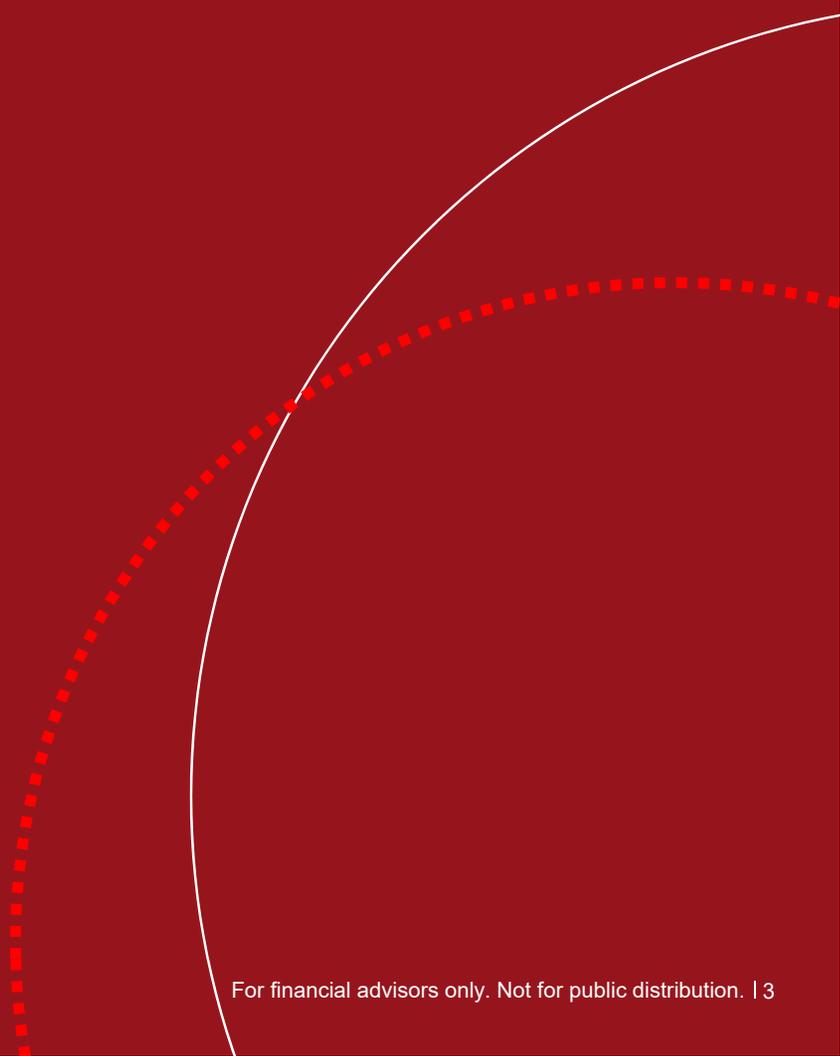


Agenda

- 1. Evolution of advisor's alpha**
- 2. Current influences, lasting impressions**
- 3. Evolution of advisory offerings**
- 4. Evolution of the advisor**

THE EVOLUTION OF

Advisor's Alpha



Advisor's alpha timeline

Advisor's alpha
2001



2014
Quantifying advisor's alpha

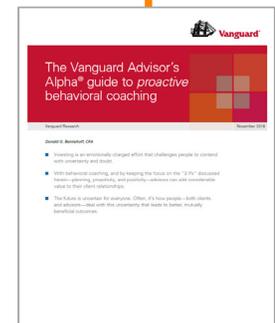
Evolution of advisor's alpha
2018



2018
Institutional advisor's alpha



Proactive behavioral coaching
2018



Vanguard Advisor's Alpha

The Vanguard Advisor's Alpha concept outlines how advisors can reframe their value proposition by *prioritizing client-centric, relationship-oriented services*, rather than solely portfolio management.

Quantification of Vanguard Advisor's Alpha

The value-add of best practices in wealth management

		Benefit of moving from the scenario described to Vanguard Advisor's Alpha methodology
Vanguard Advisor's Alpha strategy	Module	Typical value added for client (basis points)
Suitable asset allocation using broadly diversified funds/ETFs	I	> 0 bps*
Cost-effective implementation (expense ratios)	II	34 bps
Rebalancing	III	26 bps
Behavioral coaching	IV	150 bps
Asset location	V	0 to 75 bps
Spending strategy (withdrawal order)	VI	0 to 110 bps
Total-return versus income investing	VII	> 0 bps*
Total potential value added		About 3% in net returns

*Value is significant but too unique to each investor to quantify.

Notes: We believe implementing the Vanguard Advisor's Alpha framework can add about 3% in net returns for your clients and also allow you to differentiate your skills and practice. The actual amount of value added may vary significantly, depending on client circumstances.

Source: Francis M. Kinniry Jr., Colleen M. Jaconetti, Michael A. DiJoseph, Yan Zilbering, and Don Bennyhoff, 2019. *Putting a value on your value: Quantifying Vanguard Advisor's Alpha*. Valley Forge, Pa.: The Vanguard Group.

Current influences, lasting impressions

Regulations, fees, and technology



Regulatory environment—Global, not local, considerations

- Emphasis on transparency and disclosure
- Genie is out of the bottle: “Great awakening” of investors
- Global phenomenon



Australia

Future of Financial Advice



United Kingdom

Retail Distribution Review



United States

DOL fiduciary rule



European Union

Markets in Financial
Instruments Directive II



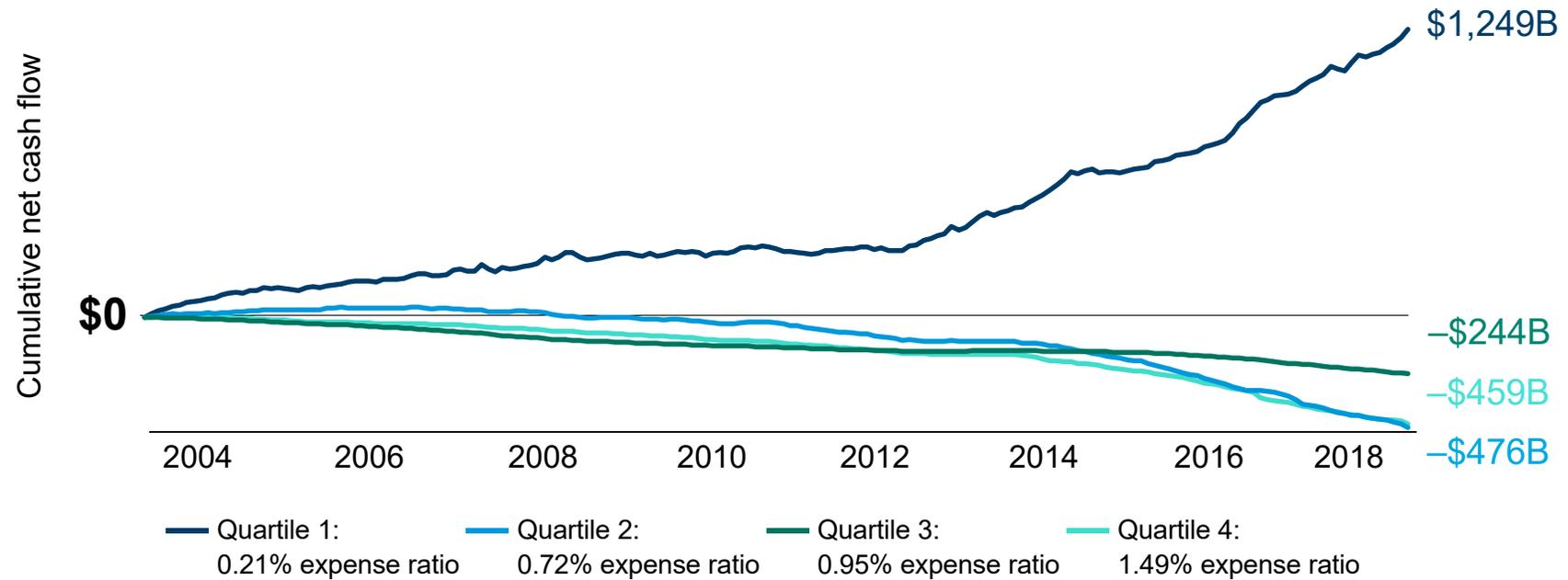
Canada

Client Relationship
Model I/II

Investment management fees: Investors and advisors are voting with their feet

High-cost funds are under pressure

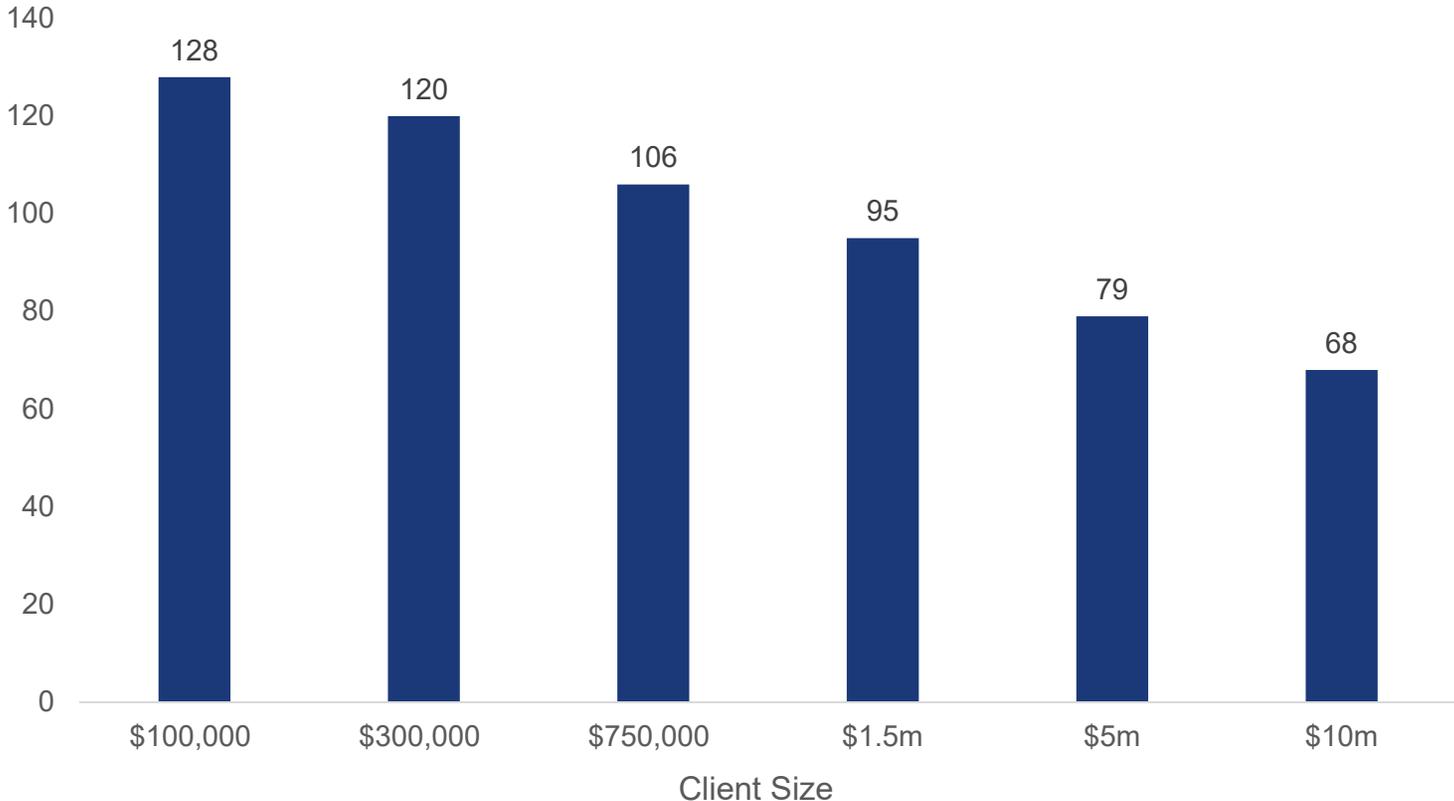
Cumulative equity fund net cash flows by cost quartiles



Source: Vanguard calculations, based on data from Morningstar, Inc., as of December 31, 2018. Notes: Expense-ratio quartiles were calculated annually. Equity funds represented by Morningstar U.S. equity category. Each quartile represents 2018 asset-weighted average expense ratios, determined by multiplying annual expense ratios by year-end assets under management and dividing by the aggregate assets in each quartile.

Advice fees

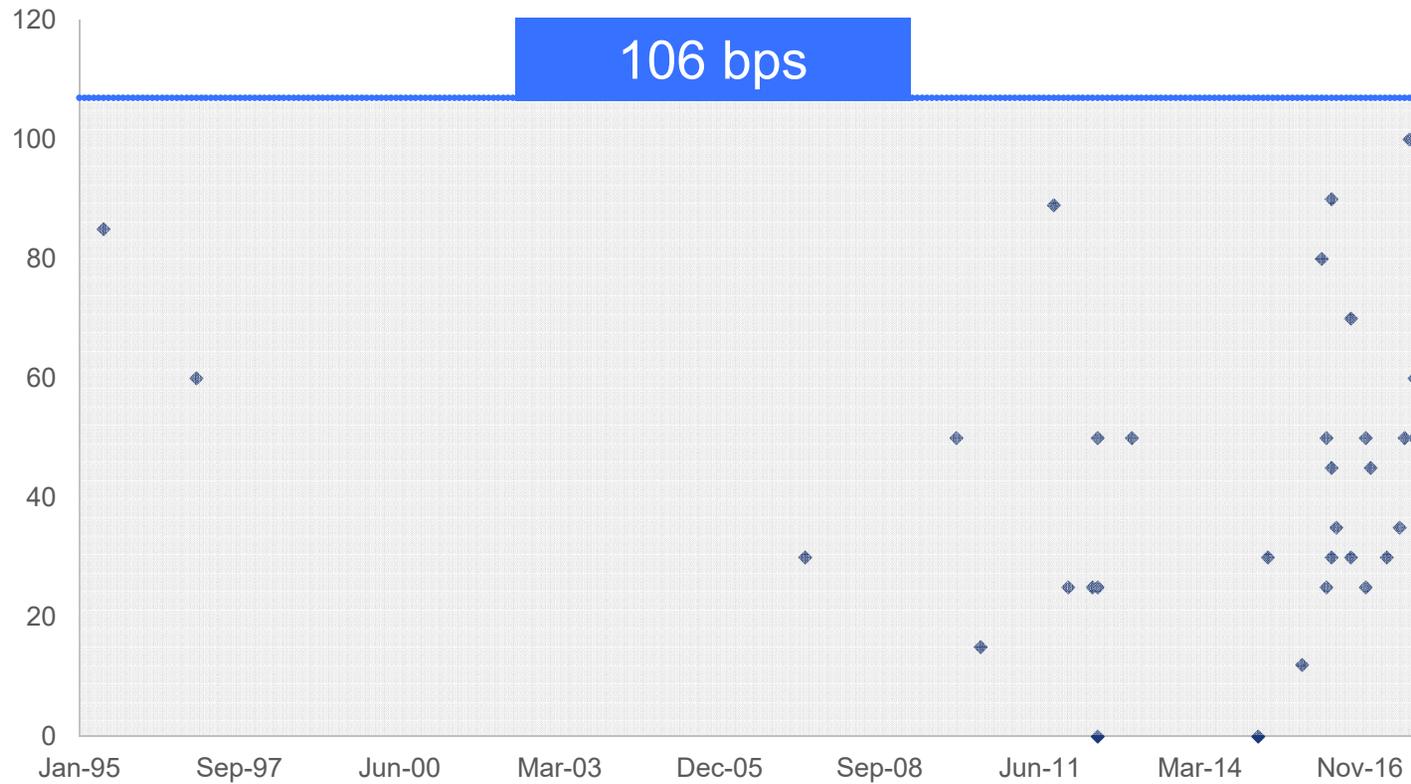
Average AUM-Based Advisory Fees by Client Size (bps)



Source: Cerulli US Advisor Metrics 2019

The march of tech-enabled advice

More in number, lower in price



Source: Vanguard calculations using data from Cerulli and the advice firms' websites as of December 31, 2019.

But advanced skills remain uniquely human

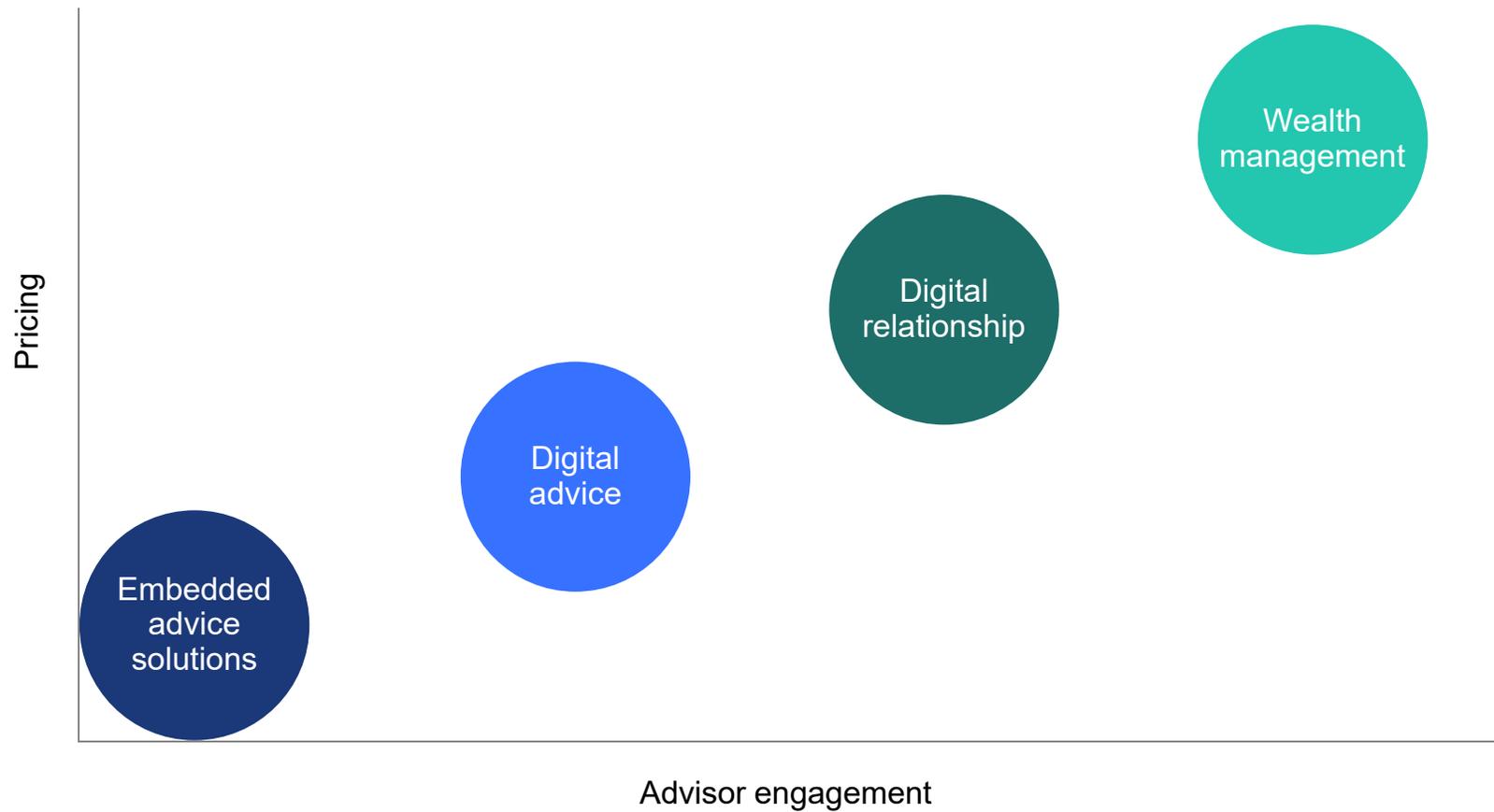
BASIC ●○○	REPETITIVE ●●○	ADVANCED ●●●
Growing Harvesting Digging Moving objects Recording information	Inspecting Monitoring Assembling Getting information Processing information Scheduling	Maintaining relationships Interacting with the public Persuading outcomes Training Developing teams Applying knowledge Strategizing Thinking creatively Solving problems Assisting/Caring for others Judging quality Conducting complex physical movements



Evolution of the advisory offerings

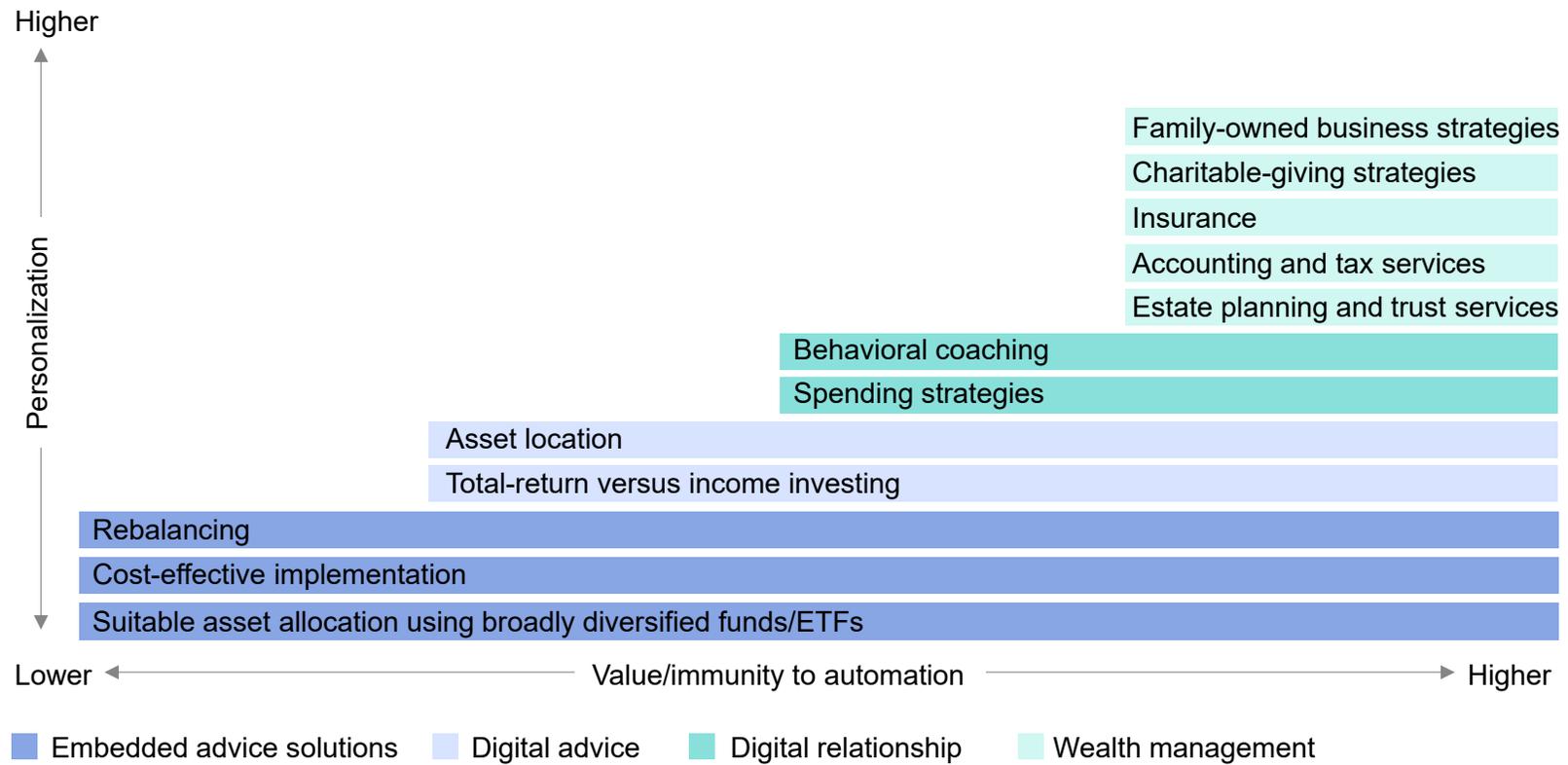
Efficient frontier for advice services

Firms should be indifferent to advice offering as long as price and services are appropriately aligned



Source: Vanguard.

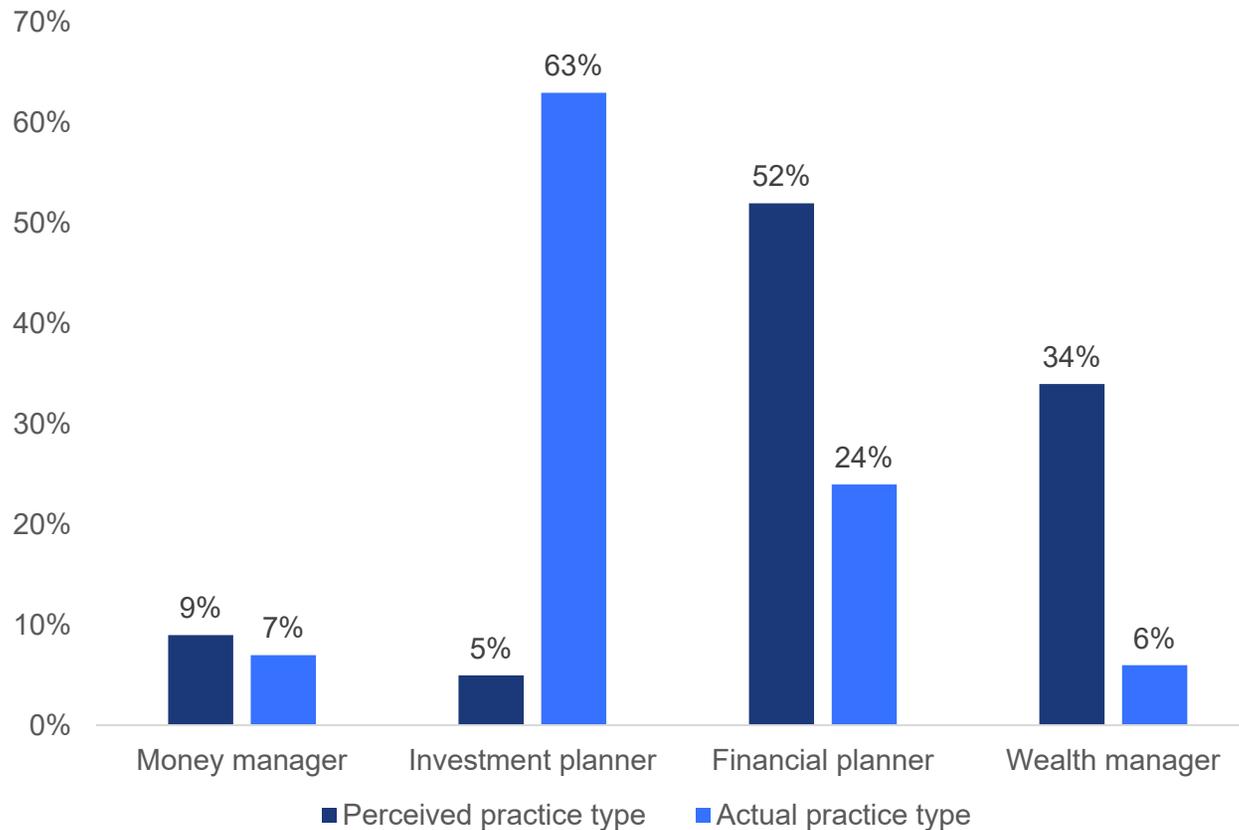
Not all advice can be automated



Source: Vanguard.

Know thyself

Perceived vs. Actual practice type



Sources: Cerulli Associates, Advisors Metrics, 2019. Meridian IQ, Investment Company Institute, Insured Retirement Institute, VARDS, Strategic Insight/SIMFUND, Investment News, Judy Diamond, Department of Labor, PLANSPONSOR, S&P Capital IQ MMD, Financial Planning, Financial Advisor Magazine, and Cerulli Associates, in partnership with the Investment Management Consultants Association, WealthManagement.com, and the Financial Planning Association® (FPA®)

Note: Cerulli assesses actual practice type by services offered, asset under management, professional designation, and team-based structure criteria. For perceived practice type, advisors are asked to select among four concise options that best describe the services that they offer. Advisors are then assigned to a perceived practice type based on their most advice-centric selection.



Evolution of the advisor

Evolution of the advisor

Advisor's alpha
key takeaway:

***Focus on relationship
management, not
portfolio management***

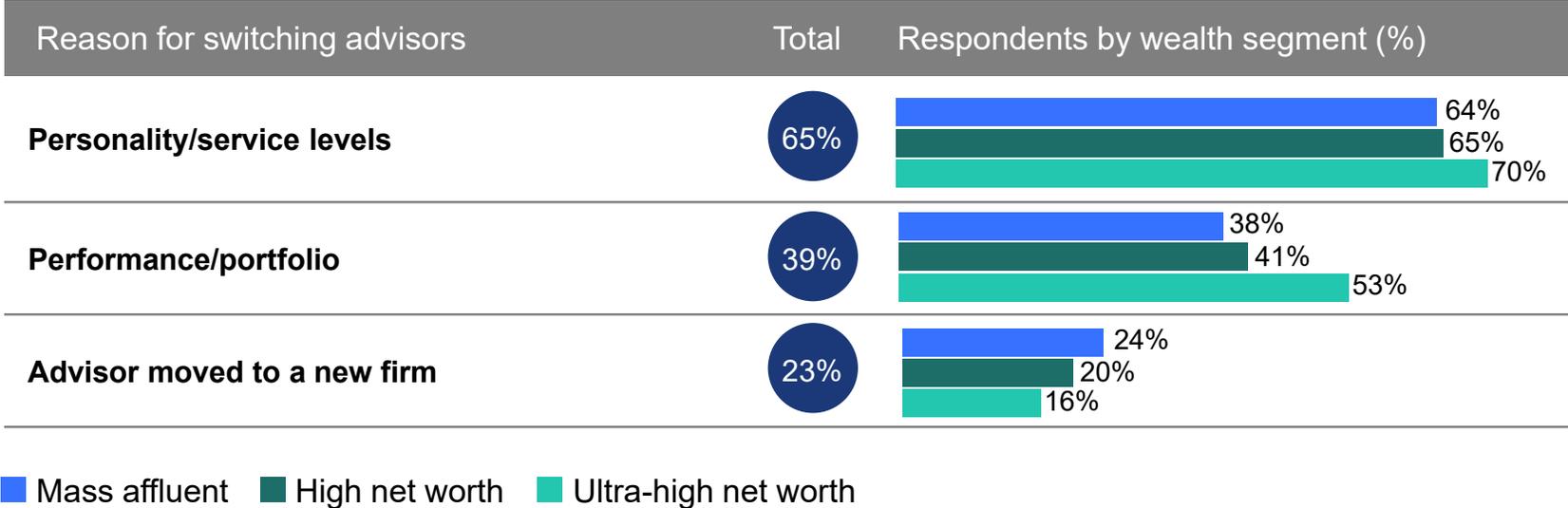
Need to use our
knowledge and
experience **where it
can do the most good**

- Behavioral coaching
- Relationship management

An advisor should
be an **investment
professional, not a
professional investor**

Why relationship management matters

Clients are evaluating their advisor’s performance more than their portfolios’

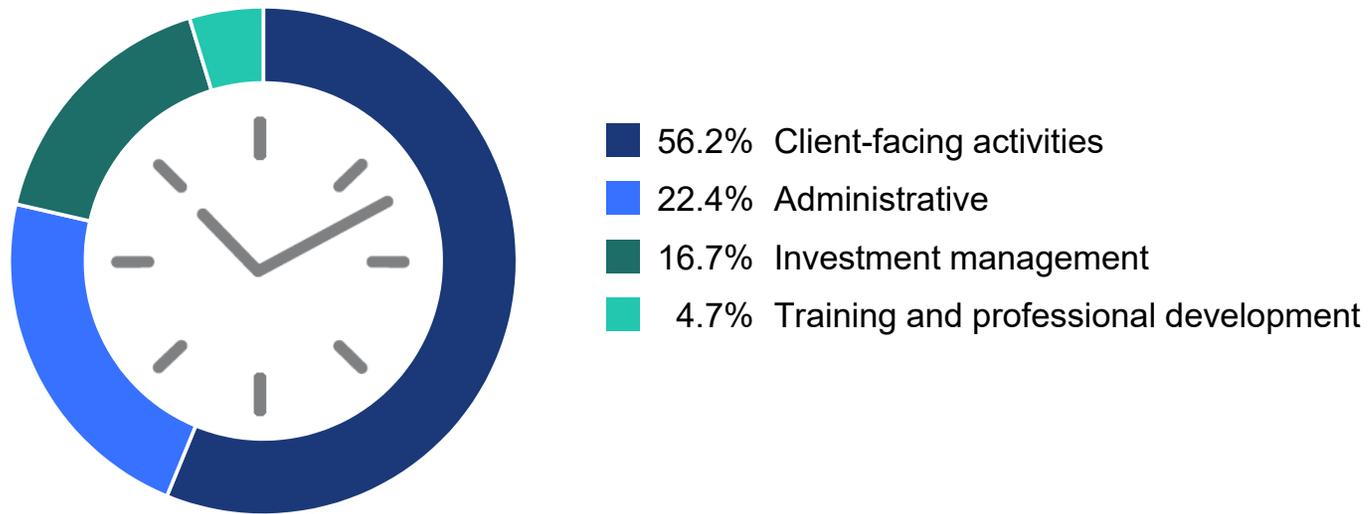


Sources: Vanguard and Chadwick Martin Bailey as of December 31, 2019.

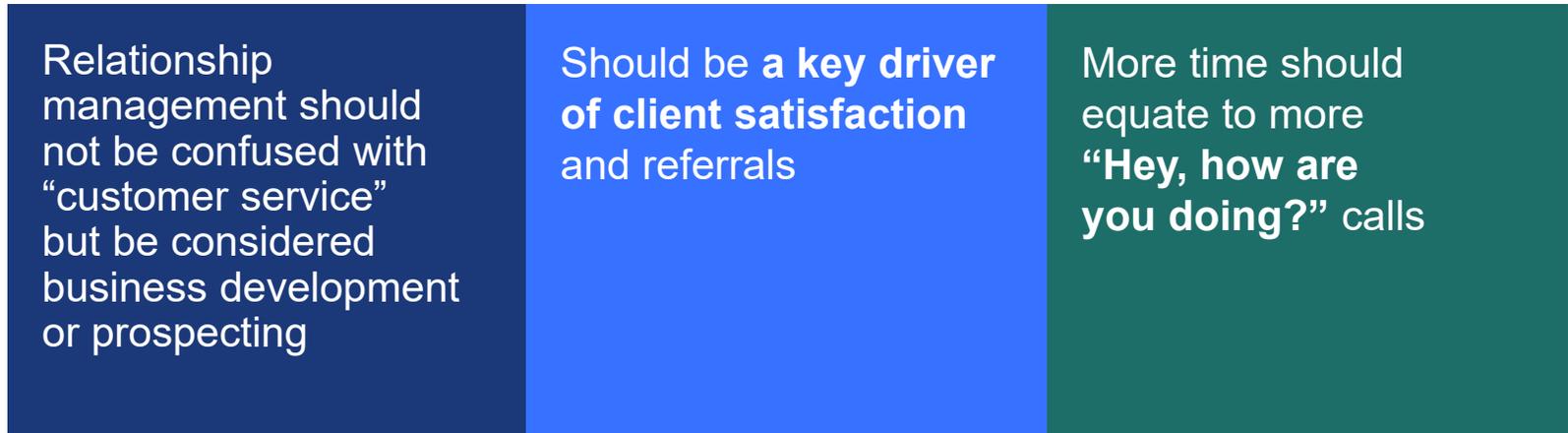
Time is an asset to be invested, not spent

Technology-enabled efficiencies could provide **more time for clients and trust-building**

Advisor time allocation by activity



The return on time



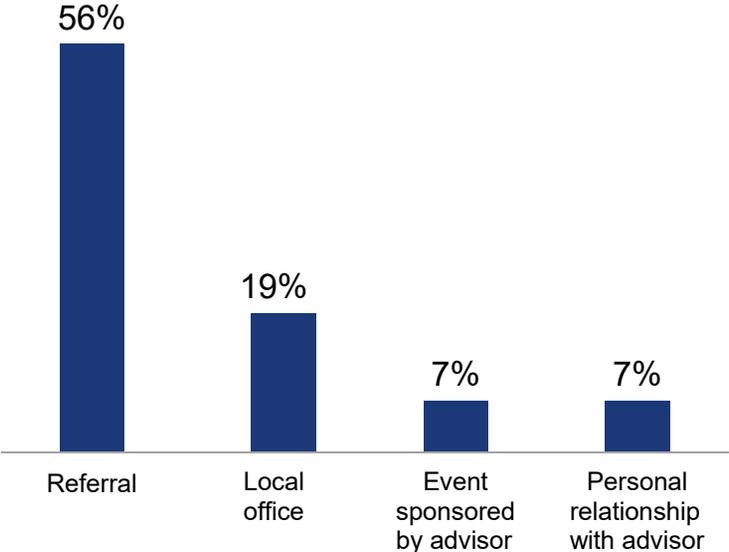
What is your return on time?



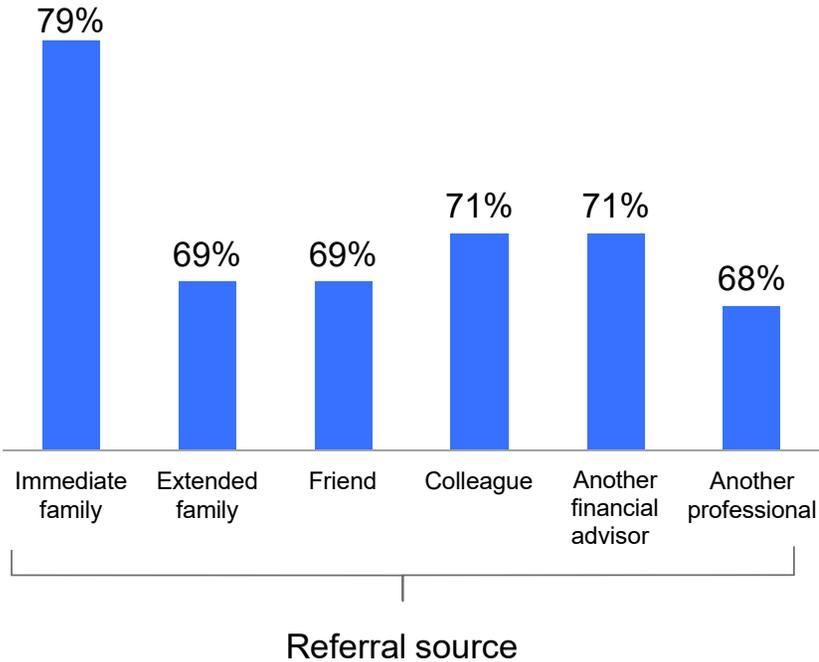
Advised Investor Insights™

Relationship management is business development

How current advisor was found



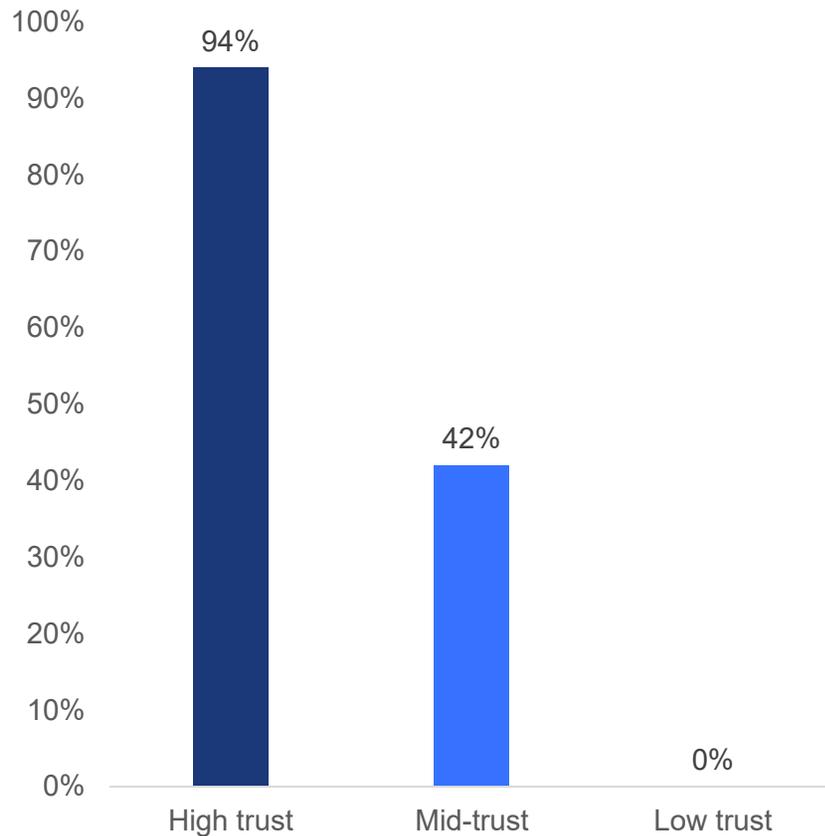
Likelihood of selecting an advisor



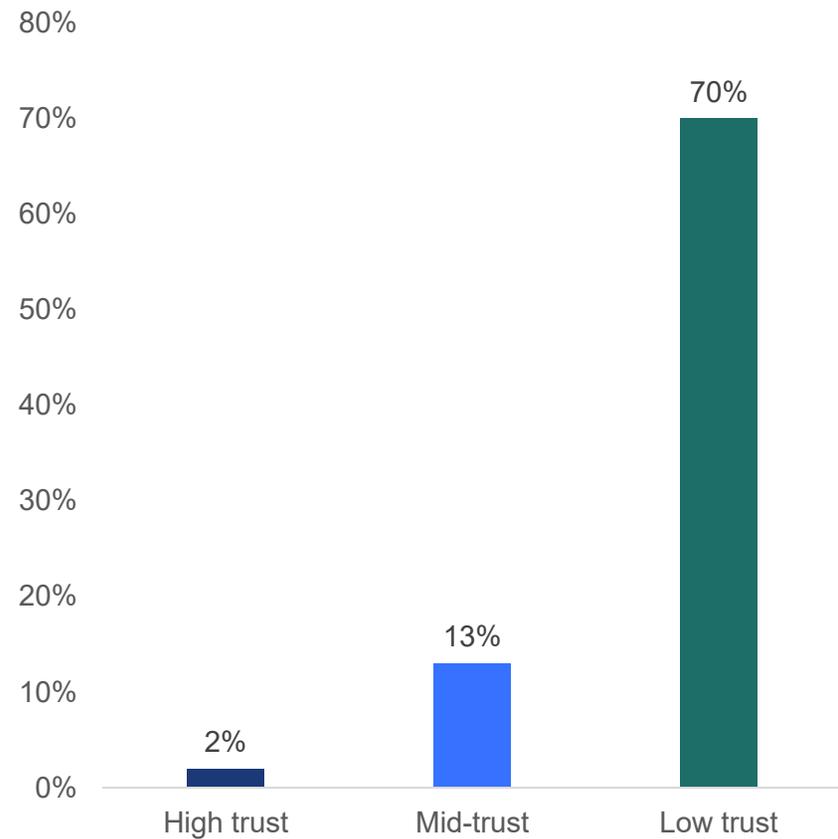
Sources: Vanguard and Chadwick Martin Bailey as of December 31, 2019.
Notes: Proprietary research conducted by Vanguard and Chadwick Martin Bailey, a market research and consulting firm. Vanguard's *Advised investor insights* is an ongoing, proprietary research series that provides actionable insights on investor behavior.

Trust motivates referrals and drives asset retention

Extremely likely or likely to offer referral



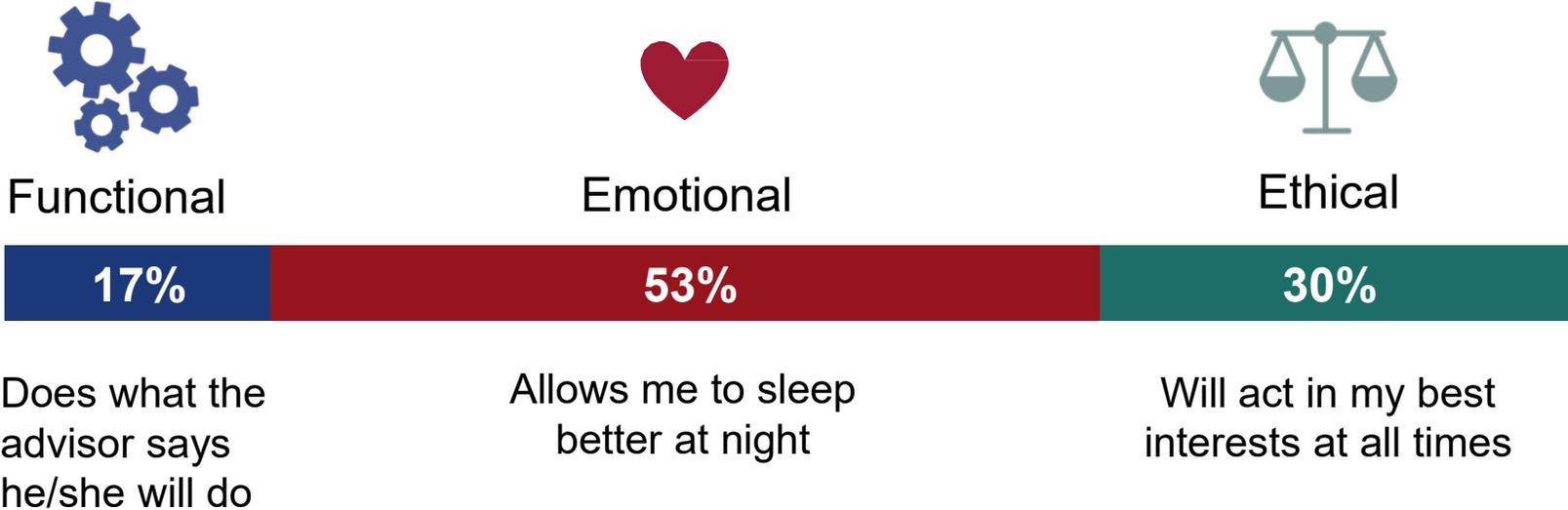
Extremely likely or likely to switch advisors



Sources: Vanguard and Chadwick Martin Bailey as of December 31, 2019.

Advised investor insights: Trust is complicated

Components of trust



Sources: Vanguard and Chadwick Martin Bailey as of December 31, 2019.

What does a financial advisor have to deliver to be trusted?

KNOWLEDGE/PERFORMANCE	HONESTY/INTEGRITY	MAKE ME FEEL VALUED
<p>“Knowledge of various investments, sound recommendations, demonstrated performance over time, good communication skills, [and] being available to clients.” —<i>High net worth, male</i></p> <p>“In pretty much any realm, quality is measured by outcome. So my first thought is that outcomes have to be positive, products offered have to have a history of success and growth while also fitting the client's risk tolerance, needs, and goals. An advisor has to know a client well enough to understand their life, values, goals, and needs, and to then recommend products and strategies that fit the individual.” <i>Ultra High Net Worth, Female</i></p>	<p>“Totally transparent honesty in all discussions, evidence of strong moral character both in business and personal life, clear and concise explanation of the financial plan, and the pathway to achieve the defined end goals.” —<i>Mass affluent, male</i></p> <p>A rational investing approach. Honesty about investment fees & expenses. Honesty about the difficulty in trying to beat the market.” <i>High Net Worth, Male</i></p>	<p>“To be trusted, he must first respect us for who we are, understand that our success turns into his success, and keep close in communications whether times are good or bad. Also, face-to-face contacts go a long way in maintaining that trust.” —<i>Mass affluent, female</i></p> <p>It is more than just products or even advice. I think it is setting some distinct goals and rolling up your sleeves to help someone get there. It is helping them set a budget then meeting with them every three months to see their numbers and helping them have some accountability for a while, etc. It is those types of just little things that really make a difference.” <i>High Net Worth, Male</i></p>

Advised investor insights: Trust is complicated

Components of trust



Sources: Vanguard and Chadwick Martin Bailey as of December 31, 2019.



Conclusion

What you can do?

- Concentrate on lowering investment management costs
- Spend more time building trust with clients than building portfolios
- Leverage technology, teams, and managed portfolio solutions to gain time to invest in your client relationships
- Make clients feel valued and cared for, like people not portfolios
- Practice emotional intelligence

There's no "one way" to do things right as long as you're focused on earning high trust from your clients every day.

Why should you do it? Good for your business—Good for your clients

The advisor's alpha flywheel



Important information

For more information about Vanguard funds or ETF Shares, contact your financial advisor to obtain a prospectus or, if available, a summary prospectus. Investment objectives, risks, charges, expenses, and other important information are contained in the prospectus; read and consider it carefully before investing.

Vanguard ETF Shares are not redeemable with the issuing Fund other than in very large aggregations worth millions of dollars. Instead, investors must buy and sell Vanguard ETF Shares in the secondary market and hold those shares in a brokerage account. In doing so, the investor may incur brokerage commissions and may pay more than net asset value when buying and receive less than net asset value when selling.

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Investments in bond funds are subject to the risk that an issuer will fail to make payments on time, and that bond prices will decline because of rising interest rates or negative perceptions of an issuer's ability to make payments. High-yield bonds generally have medium- and lower-range credit-quality ratings and are therefore subject to a higher level of credit risk than bonds with higher credit-quality ratings. Although the income from a municipal bond fund is exempt from federal tax, you may owe taxes on any capital gains realized through the fund's trading or through your own redemption of shares. For some investors, a portion of the fund's income may be subject to state and local taxes, as well as to the federal Alternative Minimum Tax. Diversification does not ensure a profit or protect against a loss.

Investments in Target Retirement Funds are subject to the risks of their underlying funds. The year in the Fund name refers to the approximate year (the target date) when an investor in the Fund would retire and leave the workforce. The Fund will gradually shift its emphasis from more aggressive investments to more conservative ones based on its target date. An investment in the Target Retirement Fund is not guaranteed at any time, including on or after the target date.

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