

FTSE  
Russell

# THE DIRECT INDEXING OPPORTUNITY 2022

SURVEY REPORT



An LSEG Business



## Table of contents

Executive summary .....	3
Ranking the direct indexing opportunity .....	4
Figure 1. Level of direct indexing opportunity by client affluence.....	5
Figure 2. Direct indexing capabilities .....	6
Figure 3. Obstacles for implementing capabilities .....	7
Figure 4. Current effectiveness of direct indexing capabilities .....	7
Figure 5. Importance of trading and rebalancing .....	8
Figure 6. Outlook for adding direct indexing solutions by asset class .....	9

November 2022

# The Direct Indexing Opportunity

SURVEY REPORT



# EXECUTIVE SUMMARY

Five years ago, hardly anyone in the financial services industry – outside of a small group of specialised, mostly tax-focused firms – had awareness of direct indexing (DI). Fast forward to 2022, and there is broad industry agreement that DI is expected to be a key growth driver in the industry – especially for wealth firms. It's no surprise that the industry finds broad agreement that direct indexing is undergoing significant growth and that this growth is expected to accelerate over the next three to five years.

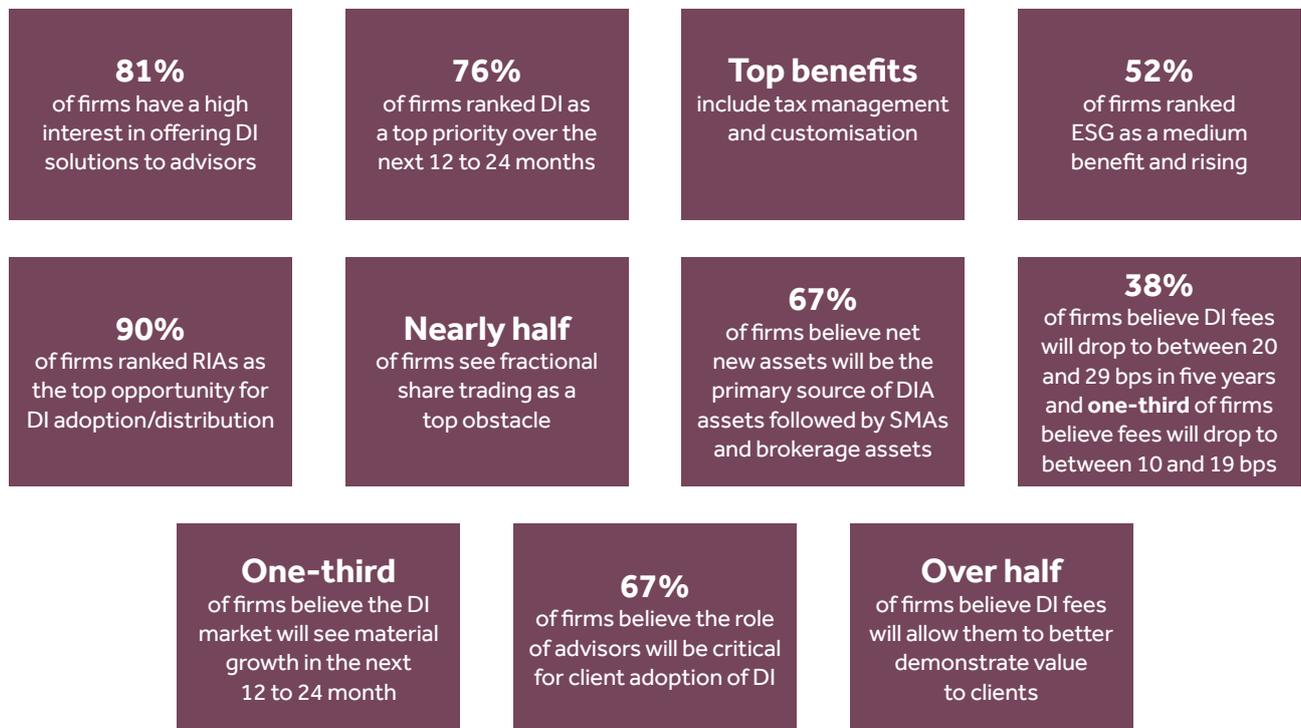
A total of 21 individuals participated in an online survey conducted by Aite-Novarica Group from March to June 2022. Survey participants spanned the wealth industry, including wealth management firms, asset management firms, investment platform providers and digital/robo advice providers. Given the size of the sample, the data in this report is considered to be a directional indication of conditions in the market. Of the firms surveyed, 81% have high interest in offering direct indexing solutions to advisors and 76% ranked direct indexing as a top priority over the next 12 months. The majority (90%) believe direct indexing will allow their advisors to better demonstrate value to clients by delivering personalised solutions such as tax-loss harvesting, efficient management of concentrated positions and portfolio customisation especially related to ESG preferences – all the top drivers of demand.

The survey results indicate that firms may be underestimating what puts the 'index' in direct indexing. The foundation of direct indexing involves the timely capture, calculation and maintenance of accurate, investment-grade index data. Only 10% of surveyed firms ranked custom indexes or performance benchmarking as top obstacles to implementing and scaling a direct indexing solution. Almost half (48%) indicated they would rather build these capabilities in-house than purchase them from a third party.



# RANKING THE DIRECT INDEXING OPPORTUNITY

Out of the firms surveyed, 76% have a high interest in offering direct indexing through advisors, which is critical over the next 12 to 24 months. Beyond the top benefits of tax management and customisation, nearly 70% of firms interviewed look at financial advisors as the primary opportunity for distributing direct indexing solutions and as the best positioned to help clients navigate their investment. All advisor channels rank high, but registered investment advisors (RIAs) are the top target market among 90% of firms surveyed.

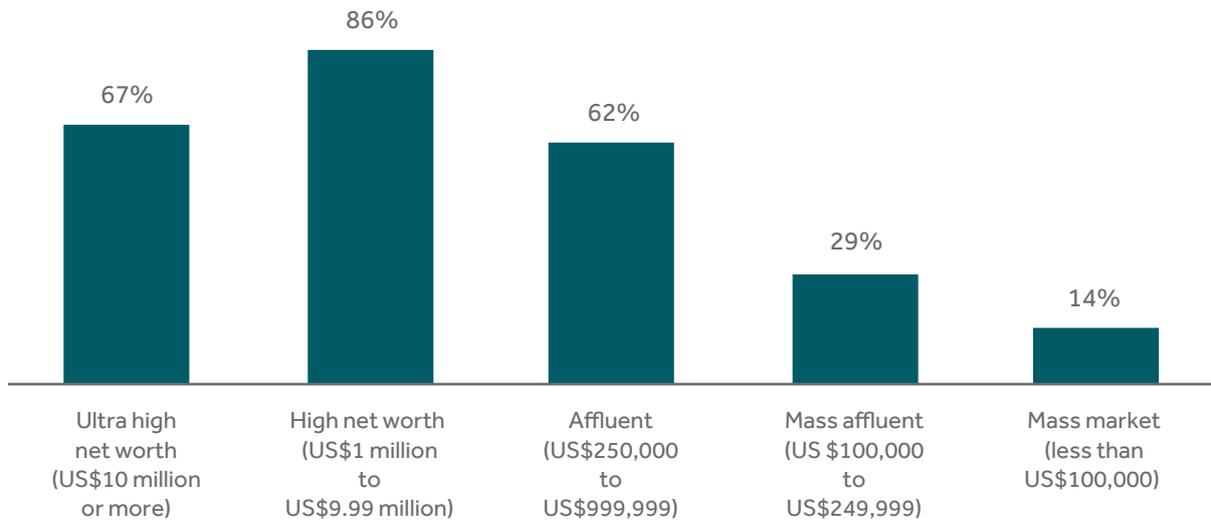


Source: Aite-Novarica Group – June 2022

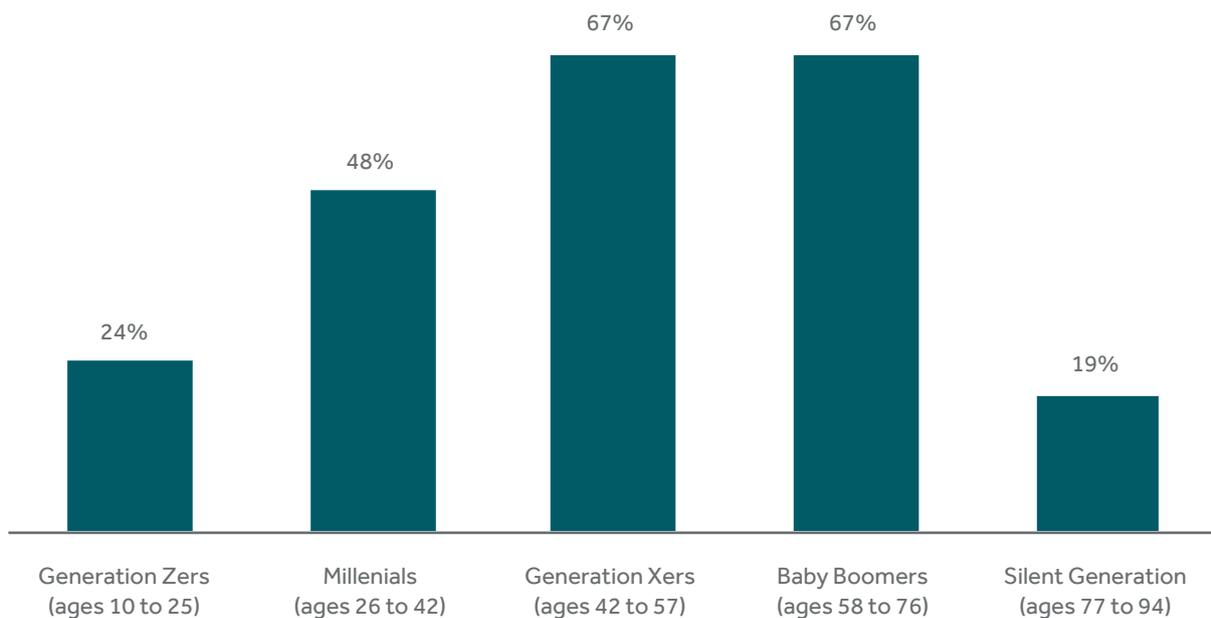
# Figure 1. Level of direct indexing opportunity by client affluence

Direct indexing targets clients across wealth and age tiers. Advancements in technology and brokerage offerings will allow direct indexing to be accessible to a broader range of clients across a wider span of investable assets. Nonetheless, most firms are still focused on more affluent clients, where the benefit of tax management has a more material impact.

Please rate the level of opportunity the following segments of client affluence provide for the distribution of direct indexing solutions (n=21)



Please rate the level of opportunity the following segments of client generations provide for the distribution of direct indexing solutions (n=21)



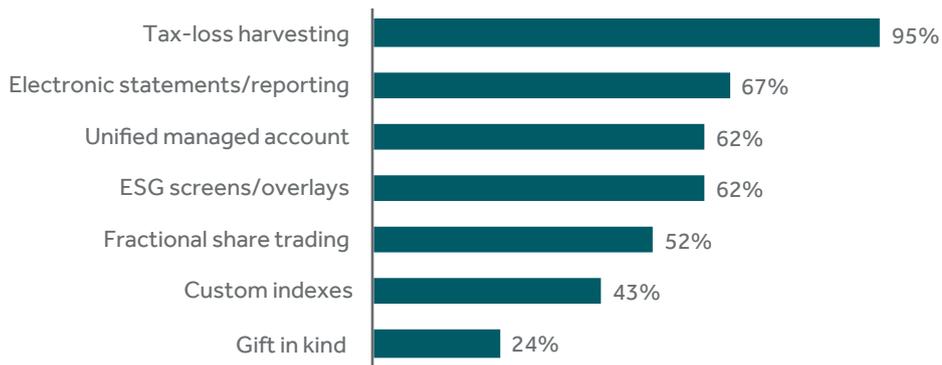
Source: Aite-Novarica Group – June 2022

## Figure 2. Direct indexing capabilities

Firms surveyed rated capabilities that are most important in managing and delivering direct indexing. When asked, respondents stated tax-loss harvesting as by far the most important capability when implementing a direct indexing strategy.

As direct indexing proliferates through the financial services industry, there are a few capabilities that are emerging as key to delivering a comprehensive solution. Tax-loss harvesting was highly ranked among firms looking to provide direct indexing to clients and financial advisors. The ability to provide electronic statements and performance reports, along with environmental, social and governance (ESG) and unified management account (UMA) capabilities, also ranks high. It would be a safe assumption that these four items should be considered table stakes when implementing a direct indexing solution.

How important is it to have the following capabilities for managing and delivering direct indexing solutions? (n=21)



Source: Aite-Novarica Group – June 2022



## Figure 3. Obstacles for implementing capabilities

Nearly half (48%) of respondents ranked fractional share trading as a major obstacle, followed by having a UMA and tax-loss harvesting.

While tax-loss harvesting is ranked highly as a key capability, only 38% of firms stated that it is an obstacle. ESG screens and overlays are also not seen as tremendous obstacles. These findings are important, as they indicate that the industry, as least from a capabilities perspective, is not being greatly hindered by a lack of technology or platform functionality.

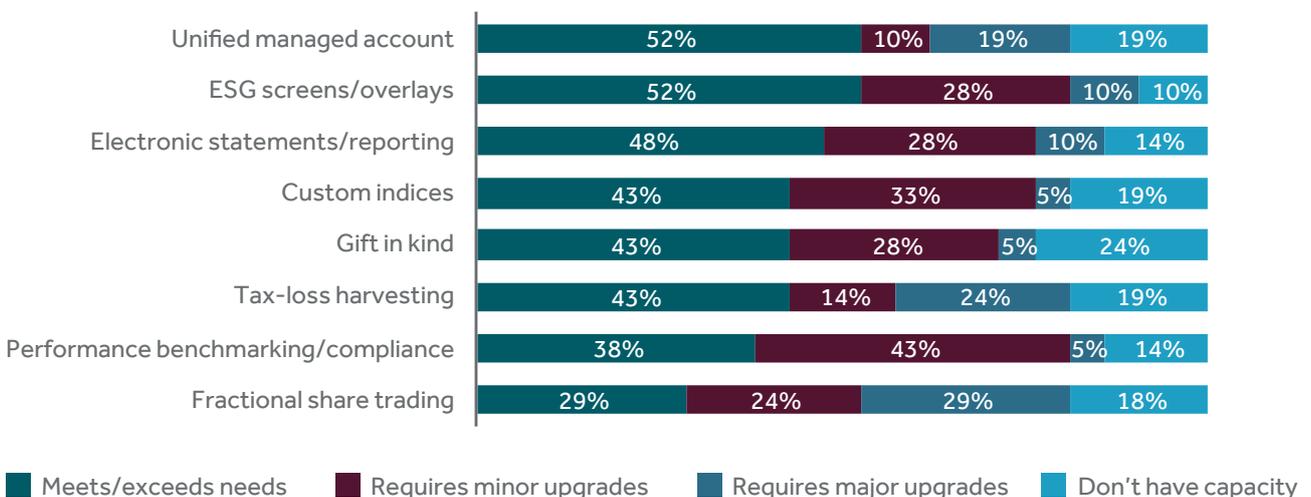
Major obstacles		Medium obstacles	
Fractional share trading	48%	Performance benchmarking/compliance	62%
Unified managed accounts	38%	Custom indexes	48%
Tax-loss harvesting	38%	ESG screens/overlays	43%

Source: Aite-Novarica Group – June 2022

## Figure 4. Current effectiveness of direct indexing capabilities

ESG screens/overlays and unified managed account capabilities ranked as the top two direct indexing capabilities meeting the needs of organisations surveyed, both at 52%.

Please rate how effectively the following direct indexing capabilities are meeting the needs of your organisation (n=21)



Source: Aite-Novarica Group – June 2022

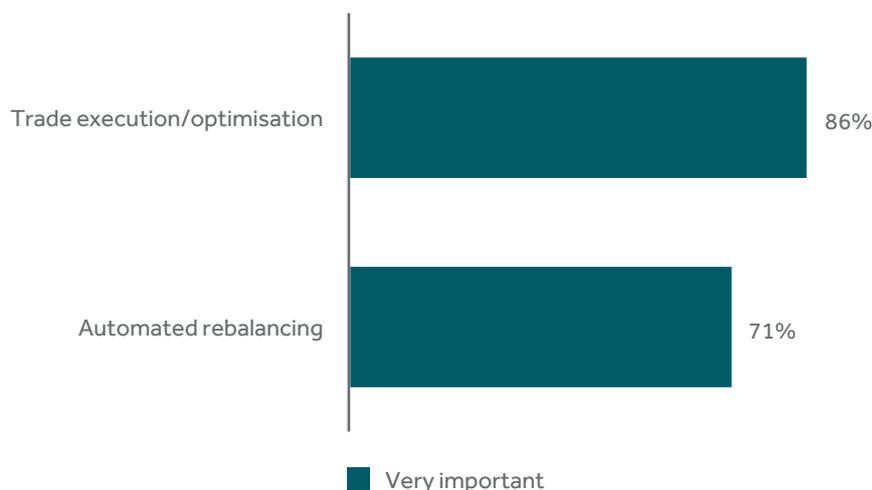
## Figure 5. Importance of trading and rebalancing

Trade execution and optimisation were rated as very important capabilities by 86% of firms surveyed, and automated rebalancing by 71%. Trade execution and optimisation are essential for delivering direct indexing.

Trading and optimisation are significant obstacles among 43% of firms surveyed, while automation is less of a major obstacle at 14%.

While expanding asset classes and index options for the direct indexing market provides greater choice for advisors and investors, it can exacerbate trading and rebalancing challenges. This is especially true for small-cap fixed income, where the inventory of firms and securities that comprise these indexes can be restrictive, underscoring the need to assure firms have access to the most robust trading platform and rebalancing tools.

How important is it to have the following capabilities for managing and delivering direct indexing solutions?



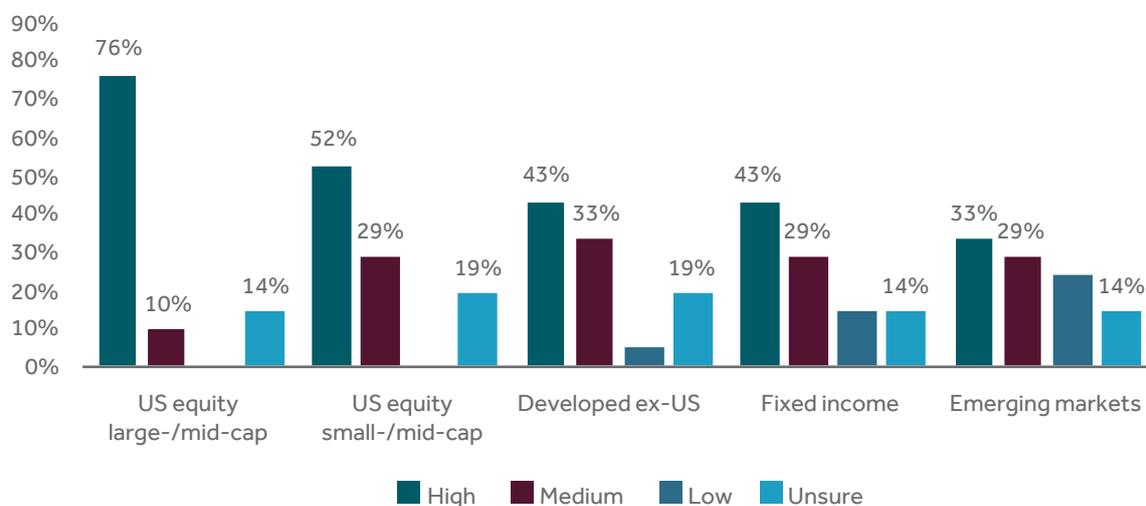
Source: Aite-Novarica Group – June 2022



# Figure 6. Outlook for adding direct indexing solutions by asset class within the next five years

The direct indexing market will continue to grow and expand. Most direct indexing solutions target US equity large-cap. However, 52% of firms surveyed have a high likelihood of launching a US equity small-cap solution and 43% likelihood of launching a non-US index or fixed income solution.

What is the outlook for adding direct indexing solutions for the following asset classes/investments vehicles in the next five years? (n=21)



Source: Aite-Novarica Group – June 2022

## SURVEY METHODOLOGY

A total of 21 individuals participated in an online survey conducted by Aite-Novarica Group from March to June 2022. Participants in the research are at wealth management firms, asset management firms, investment platform providers, and one from a digital/robo or hybrid advice provider. Given the size of the sample, the data in this report is considered to be a directional indication of conditions in the market.

# About FTSE Russell (LSEG)

FTSE Russell is a leading global index provider creating and managing a wide range of indexes, data and analytic solutions to meet client needs across asset classes, style and strategies. Covering 98% of the investable market, FTSE Russell indexes offer a true picture of global markets, combined with the specialist knowledge gained from developing local benchmarks around the world. FTSE Russell index expertise and products are used extensively by institutional and retail investors globally. For over 30 years, leading asset owners, asset managers, ETF providers and investment banks have chosen FTSE Russell indexes to benchmark their investment performance and create investment funds, ETFs, structured products and index-based derivatives. FTSE Russell indexes also provide clients with tools for asset allocation, investment strategy analysis and risk management. A core set of universal principles guides FTSE Russell index design and management: a transparent rules-based methodology is informed by independent committees of leading market participants. FTSE Russell is focused on index innovation and customer partnership applying the highest industry standards and embracing the IOSCO Principles. FTSE Russell is wholly owned by London Stock Exchange Group.

---

To learn more, visit [ftserussell.com](https://ftserussell.com); email [info@ftserussell.com](mailto:info@ftserussell.com); or call your regional Client Service Team office:

## EMEA

+44 20 7866 1810

## North America

+1 877 503 6437

## Asia-Pacific

Hong Kong +852 2164 3333

Tokyo +81 3 6441 1430

Sydney +61 (0) 2 8823 3521

# About Aite-Novarica Group

Aite-Novarica Group is an advisory firm providing mission-critical insights on technology, regulations, strategy and operations to hundreds of banks, insurers, payments providers, investment firms, and technology and service providers.

© 2022 London Stock Exchange Group plc and its applicable group undertakings (the "LSE Group"). The LSE Group includes (1) FTSE International Limited ("FTSE"), (2) Frank Russell Company ("Russell"), (3) FTSE Global Debt Capital Markets Inc. and FTSE Global Debt Capital Markets Limited (together, "FTSE Canada"), (4) FTSE Fixed Income Europe Limited ("FTSE FI Europe"), (5) FTSE Fixed Income LLC ("FTSE FI"), (6) The Yield Book Inc ("YB") and (7) Beyond Ratings S.A.S. ("BR"). All rights reserved.

FTSE Russell® is a trading name of FTSE, Russell, FTSE Canada, FTSE FI, FTSE FI Europe, YB and BR. "FTSE®", "Russell®", "FTSE Russell®", "FTSE4Good®", "ICB®", "The Yield Book®", "Beyond Ratings®" and all other trademarks and service marks used herein (whether registered or unregistered) are trademarks and/or service marks owned or licensed by the applicable member of the LSE Group or their respective licensors and are owned, or used under licence, by FTSE, Russell, FTSE Canada, FTSE FI, FTSE FI Europe, YB or BR. FTSE International Limited is authorised and regulated by the Financial Conduct Authority as a benchmark administrator.

All information is provided for information purposes only. All information and data contained in this publication is obtained by the LSE Group, from sources believed by it to be accurate and reliable. Because of the possibility of human and mechanical error as well as other factors, however, such information and data is provided "as is" without warranty of any kind. No member of the LSE Group nor their respective directors, officers, employees, partners or licensors make any claim, prediction, warranty or representation whatsoever, expressly or impliedly, either as to the accuracy, timeliness, completeness, merchantability of any information or of results to be obtained from the use of FTSE Russell products, including but not limited to indexes, data and analytics, or the fitness or suitability of the FTSE Russell products for any particular purpose to which they might be put. Any representation of historical data accessible through FTSE Russell products is provided for information purposes only and is not a reliable indicator of future performance.

No responsibility or liability can be accepted by any member of the LSE Group nor their respective directors, officers, employees, partners or licensors for (a) any loss or damage in whole or in part caused by, resulting from, or relating to any error (negligent or otherwise) or other circumstance involved in procuring, collecting, compiling, interpreting, analysing, editing, transcribing, transmitting, communicating or delivering any such information or data or from use of this document or links to this document or (b) any direct, indirect, special, consequential or incidental damages whatsoever, even if any member of the LSE Group is advised in advance of the possibility of such damages, resulting from the use of, or inability to use, such information.

No member of the LSE Group nor their respective directors, officers, employees, partners or licensors provide investment advice and nothing contained herein or accessible through FTSE Russell products, including statistical data and industry reports, should be taken as constituting financial or investment advice or a financial promotion.

No part of this information may be reproduced, stored in a retrieval system or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without prior written permission of the applicable member of the LSE Group. Use and distribution of the LSE Group data requires a licence from FTSE, Russell, FTSE Canada, FTSE FI, FTSE FI Europe, YB, BR and/or their respective licensors.