

Canadian ETF Industry Report: December 2018

Despite December's volatility spike and stock market gains for the year completely wiped out, the industry's AUM grew from \$147.1-billion at the end of 2017 to \$156.8-billion at the end of 2018, according to data from the Canadian ETF Association (CETFA). 2018 has been a hectic year and we saw trends that contributed to the ascending of the Canadian ETF market:

Expanding product range

Over a hundred of ETFs were launched in 2018, including some innovative products like Vanguard's ETF suite that provide a single fund portfolio solution to investors according to their risk tolerance. Thematic ETFs were also among the popular products launched last year. They cover themes such as blockchain, artificial intelligence and Environmental, Social and Governance (ESG). These new ETFs make investing more accessible, whether it is through a one-stop fund or through themes that investors believe in.

Lower Management Fees

The competitive market drove down fees. In 2018, 35 ETFs had their management fee reduced by 2 to 35 basis points (bps). Horizons even launched 0% management fee ETF portfolio solutions. In Canada, Exchange-traded funds remain considerably cheaper than their mutual fund counterparts. Investors slowly turn to these cheaper solutions as they become aware of the impact of fees on their return.

Jump in the number of ETF providers

Last year, nine ETF issuers joined the market, bringing the total count of providers to 33. The new players include Scotiabank, one of the five largest banks in Canada, and iA Clarington, whose parent company is Canada's fourth-largest life and health insurance company. Asset managers are joining the ETF bandwagon during the time that asset flows are moving away from traditional mutual funds to turn to ETFs. Unfortunately, not all of them are able to make the transition. Five sponsors exited the industry, which were mostly through acquisition by bigger players. For instance, WisdomTree Investments acquired Questrade ETFs, Evolve Funds took over Sphere Investments' ETFs, Redwood Asset Management was amalgamated into Purpose Investments and Sun Life Global Investments acquired Excel Funds before exiting the market altogether.

While we expect some of the above trends to persist into the new year, the following catalysts will likely have an impact on the industry in 2019:

Liquid alternatives

Liquid alternatives are available to retail investors as of Jan 3, 2019. Liquid alternatives (or liquid alts) are funds that aim to provide diversification and downside protection through exposure to alternative investments. Up until now, alternative strategies were limited to institutional or high-net-worth individuals due to their complex nature. Several liquid alts ETFs, for example, NBI Liquid Alternatives ETF and Desjardins Alt Long/Short Equity Market Neutral ETF, are waiting to be approved by regulators.

A wave of closures is anticipated

The Canadian ETF product line-up has increased significantly over the past few years. Some of the new ETFs have been very lucrative, attracting over \$300-million in AUM in less than a year of existence, while others did

not attract enough assets to break-even. Profit to an issuer is determined as a percentage of assets invested in the ETF. ETFs without enough AUM to cover costs will presumably be terminated.

Shifts in market share

While the industry remains heavily concentrated, the market share of the three largest ETF sponsors plunged from 86.8%¹ to 78.2%² over a 3-year period in December. In 2019, the arrival of new entrants like National Bank Investments and CIBC will cause even more disruption. We are also anticipating consolidations and exits during the year. BlackRock Canada and RBC Global Asset Management, the first and fifth largest ETF providers, already announced that they are being brought together under one new brand – RBC iShares.

DECEMBER ETF LAUNCHES AND TERMINATIONS:

LAUNCHES

TICKER	NAME	ASSET CLASS	MGT. FEE	EXCHANGE
ZFC	BMO SIA Focused Canadian Equity Fund ETF Series	Equity	0.75%	TSX
ZFN	BMO SIA Focused North American Equity Fund ETF Series	Equity	0.80%	TSX
MEME.B	Manulife Multifactor Emerging Markets Index ETF	Equity	0.65%	TSX
HFA	Hamilton Capital Australian Financials Yield ETF	Equity	0.65%	TSX

TERMINATIONS

TICKER	NAME	ASSET CLASS	DATE	AUM	MGT. FEE
HEUR	Harvest European Leaders Income ETF	Equity	2019-03-21	\$2.6 M	0.75%

BlackRock Canada modified the names, tickers and fundamental investment objectives of the iShares Balanced Income CorePortfolio™ Index ETF and the iShares Balanced Growth CorePortfolio™ Index ETF (CBN). The funds no longer track an index and instead act as a portfolio of ETFs. As a result of the change, their management fees have been reduced.

NAME, TICKER AND MANAGEMENT FEE CHANGES

CURRENT NAME (AND TICKER)	NEW NAME (AND TICKER)	CURRENT MGT. FEE	NEW MGT. FEE
iShares Balanced Income CorePortfolio™ Index ETF (CBD)	iShares Core Balanced ETF Portfolio (XBAL)	0.25%	0.18%
iShares Balanced Growth CorePortfolio™ Index ETF (CBN)	iShares Core Growth ETF Portfolio (XGRO)	0.25%	0.18%

Kimberly Yip Woon Sun

¹ Source: CETFA Canadian ETF Assets as of December 31, 2015

² Source: CETFA Canadian ETF Assets as of December 31, 2018