

Investors Identify Pros and Cons for Direct Indexing

Hearts & Wallets Qualitative Research Explores Product Concept Some Consider to be the Managed Product of the Future

(Sept. 19, 2023, Rye, NY) – New qualitative research reveals individual investor reactions to direct indexing to inform product and innovation strategies, according to [Hearts & Wallets](#), the independent research and benchmarking firm that specializes in saving, investing and financial advice.

“Direct Indexing Managed Account” (vs. Traditional Managed Products like Mutual Funds, ETFs, SMAs): How to Engage Consumers in the Managed Account Structure of the Future

examines investor reactions to the direct indexing product concept in comparison to mutual funds, exchange-traded funds (ETFs) and separately managed accounts (SMAs). The report is the first of six from the *Explore Qualitative 2023: Money Movement & Strategic Industry Dynamics* series. Explore 2023 analyzes what “simplicity,” the #1 driver of money movement, means to consumers, as well as industry-level dynamics between asset managers and distributors, reactions to new pricing mechanisms and consumer understanding of managed product structures. Hearts & Wallets Explore Qualitative™ (EQ) research foresees how unmet needs may change the competitive landscape. This qualitative research has a track record of anticipating competitive trends 3 to 10 years into the future.

This Explore Qualitative™ series uses a life event segmentation because households who have experienced life events are twice as likely to move money, and 2 of 3 households who move money have experienced life events. This life event segmentation separates consumers into *Wealth-building* and *Wealth-eroding* life events, with *No Life Events* for comparison.

Pros and Cons

Overall, participants in the nationwide focus groups were highly favorable toward the concept, giving it mostly positive grades. In comparison to earlier concept tests, such as “Long-term Retirement Investment” and “Hybrid Active and Passive Fund,” this concept had more positive grades and fewer negative grades.

The report identifies the two main benefits and the potential of the “Direct Indexing Managed Account” concept test based on analysis of focus group participant input. Of the two main benefits – tax efficiency and customization – tax efficiency is the bigger positive.

“The big word for me was tax efficiency and tax savings. Because I’m sick of getting smoked every day,” said a *Wealth-eroding Events* female in *Boston*.

The ability to customize holdings within the index is a potential plus, but downsides are serious.

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“Customizing a personalized index can create pride of ownership,” Laura Varas, CEO and founder of Hearts & Wallets said. “Some people appreciate being able to avoid companies they don’t like. Still, our qualitative research found customization can be complicated, time-consuming, beyond the interests/skills of ‘the average investor,’ and even risky.”

A *Wealth-building Events* male in Boston said, “I agree there's no way if you did not offer the option of hiring managers to do this on my behalf, it's too much work. In other words, my time is worth something.”

A *Wealth-building Life Events* male in Minneapolis said, “If you decide that you just really like Tesla and you just want to buy a bunch of Tesla, that's far more risky than an S&P index fund.”

Positioning, Channels and Pricing

The report contains a number of other insights of how to position direct indexing, including a startling finding that the term “direct indexing” may need to be reconsidered as the name of this technique. The full report provides analysis of consumer discussions within the focus groups, examination of differences across segments, go-to-market considerations, and detailed insights to aid trial conversion, positioning, pricing and distribution channels.

At least some investors in the focus groups think the technique currently called “direct indexing” could be the diversified managed investment product structure of the future.

“The technique currently called direct indexing holds great promise,” Laura Varas, Hearts & Wallets CEO and founder, said. “Individual investors are interested. Qualitative research is the best way to think about turning nascent concepts into established products with benefits and pricing that make sense for defined target segments, utilize appropriate distribution channels, and ensure marketing messages that generate flows.”

Methodology

The “*Direct Indexing Managed Account*” (vs. *Traditional Managed Products like Mutual Funds, ETFs, SMAs*): *How to Engage Consumers in the Managed Account Structure of the Future* report is drawn from Explore Qualitative™ Database, which supports firm initiatives to foresee how unmet needs may change the competitive landscape. The report is the first of six from the *Explore Qualitative 2023: Money Movement & Strategic Industry Dynamics* series.

The Explore 2023 nationwide focus groups were held in Los Angeles, Minneapolis and Boston in the spring. All 72 participants were actively involved in money movement, either having recently concluded a transaction or considering one in the next 12 months. The groups included participants ages 35 to 64 with sole or shared responsibility for investment decisions and over \$250,000 in investable assets (excluding the primary residence) and over \$50,000 outside their workplace retirement.

About Hearts & Wallets

Hearts & Wallets is the independent research and benchmarking firm that specializes in saving, investing and financial advice. Leading firms rely upon Hearts & Wallets research reports, software and benchmarking to make strategic decisions that lead to growth by improving products, distribution, pricing, positioning and targeting. For more information visit www.heartsandwallets.com.

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