

WITH STEPHEN CUCCHIARO OUT, LIZ ANN SONDEERS TAKES THE WINDHAVEN REINS

6.27.14 Originally Published By Lisa Shidler, RIABiz

Brooke's Note: This is a pretty stunning development both for who is exiting — Steve Cucchiaro, the supposed magician behind Windhaven — and because of who is replacing him: Liz Ann Sonders. Sonders has demonstrated her own golden touch in predicting market direction — often contrary to what the crowd believes. With her magnetism and competence, it seems as if Walt Bettinger may have made a shrewd personnel move here in the wake of his smart move in purchasing the Schwab Advisor Services client for \$150 million.

Stephen Cucchiaro is leaving the firm he founded, Windhaven Investment Management, and Liz Ann Sonders, senior vice president and chief investment strategist of The Charles Schwab Corp., will now head up the firm's investment committee.

It is unclear why Cucchiaro is leaving the firm. Schwab spokesman Greg Gable wrote in an e-mail: "Steve decided to leave for personal reasons."

But it comes on the heels of nearly four years in which Windhaven funds have had a hard time beating their benchmarks. More recently, its rate of inflows has slowed down.

ETF portfolios cooling

In the two years following Schwab's purchase of Windhaven, the company's assets soared from about \$4 billion to \$12.5 billion. This growth can be attributed to major selling by Schwab's branch brokers, sources say.

"There was a period of time when they were banking in \$100 million a month that was coming in through the branches," says Tom Lydon, president of Global Trends Investments and editor and proprietor of ETFtrends.com. "Schwab keeps a tight vest on the number. There is no doubt that ETF portfolios are in demand. But the flows have slowed. Have they reversed? No, they've not reversed and I don't think we can throw rocks at it."

Asset growth has certainly slowed at Windhaven, but that could be because the products are better designed for down markets, Chicago-based Morningstar, Inc. analyst Gaston Ceron adds. "On a sequential basis, the assets are a little bit slower. I'm not a funds analyst, but I think these products are better designed for down markets. This could be a product that attracts a lot of interest if the market goes into a tailspin."

Harvest time

From its inception in 2001 until it sold to Schwab in 2010, Windhaven grew assets 56% annually on average, according to the press release by Schwab related to the Boston company's purchase.

But chances are he's doing just fine, according to **Dan Seivert**, chief executive of **ECHELON Partners** of Manhattan Beach, Calif.

“It should not be a surprise that he is moving on as most entrepreneurs reach their shelf life when they move inside of larger corporations that demand a different skill set. Most entrepreneurs are fine with being shot from the corporate cannon back out into the open waters of small business and entrepreneurship. This ending is also a beginning as they take their proceeds and begin their next cycle of creativity, development, commercialization, and harvest.”

Canny player

Meanwhile, Sonders has shown over time an ability to stay both impressively independent in her investment analysis and work life even as she plays the Schwab corporate political game of keeping both Chuck Schwab and Walter Bettinger, chairman and CEO of the company respectively, happy with her. Sonders is known for being bullish after the 2009 crash when so many others were hyper-cautious. She has maintained her conviction in the stock market's strength as others have called for a massive pullback.

Sonders was the bright spot in the otherwise questionable decision by Schwab to purchase U.S. Trust in 2000. She had joined the New York-based matriarch in 1999 and joined Schwab from it in 2002. U.S. Trust was sold by Schwab in 2007.

But as Sonders approaches her 50th birthday, she has been entrusted with greater hands-on control of Schwab's money-managing decisions, teaming with Tony Davidow, Schwab's vice president, alternative beta and asset allocation strategist. The two will help Schwab usher in a new era of non-correlated, income producing alternative assets on the Schwab inventory shelf, according to sources.

Cucchiaro had not responded to a request for comment by deadline.

Windhaven has long been viewed as a hedge-type product in that it is hyper-diversified and built to weather down markets — a reason, perhaps, why its performance has been lackluster at best during the four years that Schwab has owned it, a period that best rewarded forward-leaning, long-only-type funds.

High-wattage execs

But Schwab's ability to attract assets to Windhaven in the face of returns often short of benchmarks has been plenty strong.

Since Cucchiaro sold his company to San Francisco-based The Charles Schwab Corp. in 2010 for \$150 million in cash and stock, Windhaven's assets under management have grown from \$4.2 billion to more than \$19 billion today.

Cucchiaro, a pioneer ETF strategist, had a winning strategy that was successful for years. He has a mathematics degree from the Massachusetts Institute of Technology, an MBA from the Wharton School of the University of Pennsylvania, and was a technology entrepreneur and Olympic-grade yacht racer.

Sonders, a popular TV commentator and investment strategist, has been an active member of the Windhaven advisory board and is one of the most well known Schwab executives next to Charles Schwab himself.

Back at the controls

These sudden changes are puzzling to Lydon.

"Honestly, I have no idea. I know Steve and I talked to him in the past month and nothing was said. They've got a pretty tight ship there. It may have been something as easy as the guy's in a great position and he's ready to go," he says.

"But to have Liz Ann Sonders taking over, is big because she's very smart. I believe she's got it in her blood to manage money. This gets her back into the seats of managing controls and managing money again, which is great. It says a lot about Schwab's ETF business to be putting one of their most popular faces as the head. Change is good for everything. Steve is a great guy and he started this from nothing. He's got a lot to be proud of. I'll miss him."

Big slice of revenue

It is hard to track the exact inflows and outflows at Windhaven and the discussion of lagging flows and performance has been a hot topic among industry leaders.

What is certain is that Windhaven makes up an important part of Schwab's revenues, says Ceron.

"Windhaven's revenue is split into a few buckets but the advice-solutions bucket is a very important one to the firm. If you look at that revenue line you can easily see that it has been growing nicely. It's very important to Schwab, particularly as the asset-management industry has faced headwinds because of low interest rates. This is an area that is doing well."

For example, Schwab earned \$199 million in its advice-solutions revenue in 2014's first quarter, and while that category includes a number of products, a good chunk of that money is from Windhaven, Ceron says. Windhaven commands a revenue-friendly .95% of assets.

That \$199-million amount would make up about 13.5% of Schwab's revenues.

"It's hard to break down that entire category but it's fair to say this is a very important business to Schwab and has done very well for them at a time when other asset management streams have had some hurdles."

Market-proof?

Windhaven manages portfolios, comprising primarily of exchange traded funds, that are built to help investors weather bad markets by lessening their risk, although often they do not generate quite as much return in an up market. The company uses its own set of proprietary models, ranking asset classes and adjusting portfolio weightings several times a year for the highest returns given the risk.

Since Windhaven came on the scene, dozens of competing strategists have emerged, but Lydon still believes that Windhaven has a bright future.

“Windhaven is the biggest in terms of being an ETF strategist,” Lydon says. “If there’s a strategist that hits a soft spot people start talking about it, and I’m not hearing that about Windhaven. I think it’s been a five-year equity bull-market and they’ve had some decent years in there.”

Deft navigation

Cucchiaro certainly had an amazing run at Windhaven, **Seivert** says.

“You have to credit Cucchiaro for his entrepreneurial success: He developed the company from the ground up, he guided it through multiple levels of scale, he orchestrated a successful liquidity event with the ultimate strategic buyer, and assisted with the post-acquisition growth phase. In addition, I think he did the majority of this as both a CIO and CEO. Creating a rapid growth company and navigating the challenges that come with that is no small feat.”

ABOUT ECHELON PARTNERS

ECHELON Partners (ECHELON) was formed in 2001 to offer investment banking and consulting to a subset of the financial services industry known as “investment product developers and distributors” (IPDADs). Since that time, ECHELON’s professionals have helped hundreds of senior executives envision, initiate, and execute a multitude of complex business strategies and transactions. ECHELON’s business is making companies more valuable through delivering advice and orchestrating transactions. Accordingly, ECHELON measures its success in the enterprise value it creates for its clients. Companies that strive to outperform their peers choose to work with ECHELON because we are as passionate about their results as they are.

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