https://www.wsj.com/articles/charles-schwab-ending-online-trading-commissions-on-u-s-listed-products-11569935983

MARKETS

Schwab Cuts Fees on Online Stock Trades to Zero, Rattling Rivals

The move by Schwab, the largest e-broker, rattled the sector as it grapples with investor expectations of low or no-fee financial services

Charles Schwab said a new policy, effective Oct. 7, is aimed at making online investing more affordable. **PHOTO:** CHRISTOPHER DILTS/BLOOMBERG NEWS

By Alexander Osipovich and Lisa Beilfuss

Updated Oct. 1, 2019 1:58 pm ET

Charles Schwab Corp. said it would eliminate commissions on online stock trades, one of most dramatic moves yet in a broad-based price war that is crunching profitability across the financial sector.

The move by Schwab—the largest e-broker, with 12 million brokerage customers—rattled online brokers that have been squeezed by investors' expectation that fees for financial services should be low or even nonexistent. Shares of larger banks and brokerages also declined amid a

1% drop in the Dow Jones Industrial Average, reflecting soft U.S. data that reignited concerns about the economic outlook.

Digital upstarts like Robinhood Markets Inc. help popularized the zero-commission model in the online-brokerage business. But the race to zero is also happening in other areas of finance, like asset management, where Vanguard Group and Fidelity Investments recently eliminated fees for many funds offered on their platforms, and financial advice, which some digital advisers are offering free of management fees.

"There are certain parts of finance that have become commoditized," said Devin Ryan, an analyst at JMP Securities LLC. "Trading is one of them."

Shares of TD Ameritrade Holding Corp. AMTD **-25.19%** ▼ plummeted 24% in midday trading, putting them on track for their biggest one-day percentage move since 2006. E*Trade Financial Corp. ETFC **-16.86%** ▼ was down 16%, and Schwab was down 9%. The three firms' declines wiped out nearly $13 billion in aggregate market value.

Another rival, Interactive Brokers Group Inc. IBKR **-9.33%** ▼ —which set the stage for Schwab's price move last week when it announced plans to launch a zero-commission stock-trading service—fell 9%.

E-brokers had already been hurting because of falling stock-trading volumes this year, as concerns over slowing economic growth have made investors more cautious. Interest rate cuts by the U.S. Federal Reserve have dealt another blow, by cutting into e-brokers' ability to collect interest on clients' cash.

Analysts warned other online brokers would be forced to follow Schwab's lead.

"There is no way to sugar coat this development," analysts at Wells Fargo said in a research note. "We were hoping the challenging macro environment (i.e. declining interest rates) would prevent the industry from competing on price like this, but that is clearly not what is happening."

Schwab may be better positioned to weather the storm. Compared with its rivals, it is more reliant on its banking arm and less dependent on commissions, which make up only about 7% of total revenue.

TD Ameritrade, meanwhile, derives about a quarter of its revenue from trading. For E*Trade, commissions comprise about a fifth of total revenue.

Some e-brokers may need to merge with competitors to survive, JMP's Mr. Ryan said. That process has already been under way, with TD Ameritrade acquiring Scottrade in 2017.

Online brokerages like E*Trade became hot during the 1990s dot-com boom, as day trading took off. But they've recently lost ground to the likes of Robinhood, the Silicon Valley startup that has lured many first-time investors and traders.

Founded in 2012, Robinhood has amassed around six million users, many of them millennials, with its smartphone app that lets investors buy and sell stocks without paying a fee. Robinhood's success has sparked an array of imitators offering free stock trades, including Webull, M1 Finance, TradeZero and Dough.

A spokesman for Robinhood said, "The changes taking place across the brokerage industry reflect a focus on the customer that's been inherent to Robinhood since the beginning."

Even the biggest, boldest names in financial services have been forced to play this game. JPMorgan Chase & Co. last year unveiled its You Invest product, which offers customers at least 100 free stock or ETF trades a year and is aimed at younger, first-time investors. Bank of America Corp. 's Merrill Edge also offers some commission-free online stock and ETF trades, an offering it expanded in February.

To make money, zero-commission brokerages like Robinhood rely heavily on a controversial practice called "payment for order flow," in which they route customers' orders to buy or sell shares to electronic trading firms like Citadel Securities and Virtu Financial Inc., in return for cash payments. Robinhood is also a lean operation that doesn't spend money on legacy operations like the bricks-and-mortar storefronts offered by TD Ameritrade and Schwab.

A broad investor retreat from actively managed funds to cheaper index funds has pressured fees charged by asset managers, hurting the profit margins of traditional stock-picking firms. In some cases fees have also sunk to zero.

Last summer, Vanguard Group said it was making online trading free for almost all ETFs bought and sold through its brokerage platform. A month later, Fidelity Investments unveiled in the first zero-fee index funds. Fidelity later expanded the number of ETFs that trade at no fee on its own platform to more than 500.

Free financial advice is also cropping up, disrupting the business of old-school financial advisers who typically charge 1% to 2% of a client's assets annually. In 2014, Schwab announced its system that uses algorithms to provide portfolio-management services. For some customers it has waived fees for the digital advice, in exchange for a relatively high cash allocation that flows into Schwab's bank. Robo-adviser Wealthfront Inc. last year made its automated financial planning free to anyone who downloads the company's app.

Schwab's move on trading fees is set to take effect Oct. 7. It applies to commissions for stocks, exchange-traded funds and options listed on U.S. or Canadian exchanges. The San Francisco financial-services company currently charges a commission of $4.95 for online U.S. stock, ETF and options trades. Charles Schwab said clients trading options will continue to pay 65 cents per contract.

"We don't want to fall into the trap that a myriad of other firms in a variety of industries have fallen into and wait too long to respond to new entrants," Chief Financial Officer Peter Crawford said in a note on the company's website. "It has seemed inevitable that commissions would head towards zero, so why wait?"

Other online brokers grappled with the prospects of a race to zero. TD Ameritrade said it was reviewing the Schwab announcement. "We will remain competitive," a spokeswoman for the Omaha, Neb.-based brokerage said.

A Fidelity spokeswoman declined to say whether her firm was considering a commission cut of its own. "We will always look for ways to leverage our scale to deliver even more value," she said.

Vanguard is "happy to see others in the industry continue to follow our lead in reducing the cost of investing," a spokeswoman said. E*Trade did not immediately respond to requests for comment.

Interactive Brokers said it welcomed Schwab's announcement, which came just five days after the firm unveiled its commission-free "IBKR Lite" platform.

"The more the merrier," the company's Chairman and CEO Thomas Peterffy said in an email.

—Justin Baer and Dawn Lim contributed to this article.

Write to Alexander Osipovich at alexander.osipovich@dowjones.com and Lisa Beilfuss at lisa.beilfuss@wsj.com