



News

MANAGED ACCOUNTS COME OF AGE

By Thomas Bignill on 29 September 2011 0 comments

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Since their arrival on our shores about a decade ago, managed accounts have remained largely dormant in Australia. But with continuing market volatility and the imminent introduction of the FOFA reforms, the market seems to be paying them more attention. Thomas Bignill explores why the day of managed accounts is dawning.



Up until recently, there hasn't really been a need to adopt managed accounts. Financial markets were ticking along nicely, investors were happy and planning practices were making money. Against this backdrop, why would an adviser change a business model that wasn't broken?

Managed accounts were also in their infancy. Generally speaking, they were offered for large-cap Australian equities only and product choice was limited, due to the reticence of fund managers about 'sharing their IP'. There was only a small number of managed account providers – and an overarching sense that the sector needed to develop further.

Other obstacles included a lack of knowledge amongst clients as to the benefits of managed accounts and the difficulties, perceived or real, of transferring clients to a new investment model.

Fast forward a few years and the world is a very different place. During the past 12 to 18 months, we have witnessed increasing activity in the managed account sector.

The main impetus has been the fallout of the GFC. This has prompted investors, advisers and regulators to examine the existing financial services model and ask whether there is a better way.

For investors, key concerns have centred on fees, performance and control. Connected to this are questions about the fairness of capital gains tax outcomes for managed funds. Frankly, I don't envy the adviser who has to front up to a client and explain why they need to pay capital gains tax on an investment that has lost money.

As a result, investors have begun demanding "simpler" investments like direct equities and exchange trading funds (ETFs).

According to Investment Trends, new investment in direct shares is expected to rise to 26 per cent in 2013 – an increase of more than 10 per cent from two years ago. As these pressures mount and demand for direct shares increases, structures like managed accounts come into their own.

With managed accounts, the beneficial ownership of the shares sits with the investor. This entitles them to company dividends and franking credits and facilitates personalised capital gains tax outcomes. At the same time, clients continue to benefit from the oversight and input of professional investment managers.

Managed accounts also provide complete transparency so the investor has full knowledge of what they are invested in, how their portfolio is performing and how much they are paying. It provides the investor with a sense of control over their financial outcomes.

It is for similar reasons that managed accounts have experienced significant growth in the US market, particularly amongst high net worth clients and their advisers. Recent figures I've seen out of the US indicate that their managed account market is worth about US\$2.1 trillion, and is growing by about 14 per cent per year.

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Legislation and regulatory reform are also helping support the growth of managed accounts. The Future of Financial Advice (FOFA) reforms echo the concerns of investors with an emphasis on fairer fee models, greater transparency and a requirement to place the investor firmly in the centre of the equation. The high-touch approach of managed accounts is a natural fit with the high-touch approach of FOFA's opt-in provisions and fiduciary duty requirements.

The outcome of all this for advisers is significant. Under FOFA, advisers will be meeting with their clients in the coming months to sign new service propositions. I expect clients will begin to ask questions about fees and value creation and will demand greater accountability.

To keep clients engaged and preserve practice value, many advisers are going to have to reassess their business models. There is a pressing need to redefine value propositions for the post-regulatory environment – to show their clients that they have addressed the problems of the GFC and found a better solution.

It is the transparency of managed accounts that provides a key advantage. When a client engages an adviser, they expect the adviser to know the intricacies of their portfolio. This could be difficult if the adviser is using managed funds which provide monthly or quarterly updates on performance and the 'top 10 stocks'.

With managed accounts, advisers have complete visibility of client portfolio outcomes and can be more involved in investment decisions. This enables the adviser to cement their role and forces closer relationships between adviser and client.

In addition, managed accounts ease the transition to fee-for-service, as the planner has greater visibility of fees, enabling them to better calculate and justify the value they add.

Managed accounts can also provide advisers with the benefits of a managed discretionary account (MDA), thus enabling them to be proactive when markets demand it. Without an MDA, advisers have to move clients individually – and by the time they get through the approval and administration process, the opportunity has often been lost.

Yet despite their benefits and relevance in a post-GFC world, we continue to encounter some resistance when it comes to actually making the decision to implement managed accounts. The reasons are varied, but typically include a lack of investment choice, concerns about technology and the process of transition. Fortunately, the managed account industry has used its time on the sidelines to mature and address many of these concerns.

Firstly, with more providers now in the market, managed account technology and administration systems have advanced considerably, leading to improved efficiency and reliability. Most managed account providers have also integrated their systems with key software programs such as Xplan and Coin.

Secondly, investors are no longer restricted to Australian shares. There is now a broader range of asset classes available such as international equities, fixed interest, ETFs, cash and derivatives. This has been facilitated by improved technology and also a growing awareness and acceptance of managed accounts amongst fund managers. It also allows the adviser to properly diversify a portfolio.

Managed account providers are also placing greater emphasis on transition support, which is critical if the sector is to prosper. Providers are more adept at helping planners structure managed accounts to complement their existing platforms.

At the end of the day, managed accounts are starting to shine because they enable advisers to rebuild their value propositions and deliver what clients and regulators want – a high-touch, transparent and fair approach to investment management that places the client firmly at the centre of the equation.

Thomas Bignill is the managing director of Mason Stevens.

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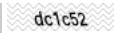
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