

This is one of the main services offered by advisers to clients. One of the skills that advisers can offer to clients to maximise the potential returns on investments. One of the main mysteries for advisers is how to provide this service – to offer the clients a diverse investment portfolio that they could not organise for themselves in a cost-effective manner for the adviser.

There are several levels of provision that are available.

- Outsource to a Discretionary Fund Manager.
- Use providers' portfolio funds – multi-manager or multi-fund.
- Make up their own model portfolios.
- Make up bespoke portfolios.

The latter two of these require experience of the markets to build the knowledge to differentiate between various fund offerings. This is fine for established advisers, but still time-consuming to ensure up to date knowledge. Also, to do the job effectively, the adviser should have the discretionary management permission from the FCA, or they will need to get their clients' permission before making alterations to the funds. Although, I have seen one firm move all their clients to cash and then contact them!

I have seen some examples of successful model portfolios, but these can be quite high maintenance. Normally, involving input from several advisers and possibly outside help. The documentation of investment decisions and also regular reports on progress to clients can be quite onerous.

I saw an adviser who monitored his funds daily, which is excellent. He achieved this by using the same 10 funds in all his portfolios in different weightings according to risk tolerances. This is fine until one or two of those funds start to under-perform and need to be changed.

The main issue about running portfolios is the monitoring of the funds, keeping records and having a robust process about dealing within the portfolio. Robust being the operative word in that fund management cannot be knee-jerk reactions and the transactions and rationales need to be consistent.

The discretionary management permission requires a specific investment qualification. Also, the discretionary management permission will probably involve an increase in the costs of Professional Indemnity Insurance. So, this added cost burden does beg the question whether advisers doing fund management on a part-time basis can produce better results than professional managers who do nothing else.

There is a bewildering array of funds available. There are active funds, passive funds, Exchange Traded Funds & Non-Mainstream Pooled Investments, Enterprise Investment Schemes, Venture Capital Trusts and other funds that could be used within portfolios. So, an adviser is reliant on good quality research tools to filter down to the funds that they want to use.

There are some pretty good sources of research, such as Trustnet and Morningstar and most of the platforms have one or other of these or something similar available for use on their portal.

Producing model portfolios gives the adviser complete control over the investment strategy of their clients. It tends to keep the advisers in more regular contact with their clients, which should be a good thing.

The advantage of diversified portfolios is well understood. The split between asset classes and geographical areas should mean consistent returns rather than relying on a narrow investment that could be hit by local issues. However, it is possible to go to the other extreme of having so many funds that performance is totally diluted and any diversification advantages are negated by that dilution.

Outsourcing of investment fund management has the advantage that the adviser will stick to advising and the clients will benefit from full-time professional fund management. All the time taken to running portfolios can be re-directed to advising clients. All of the record-keeping, management and the PI burden disappear. Expertise is brought in to provide the clients with more potential for consistent investment performance.

Discretionary Fund Managers tend to be used for larger funds for clients. This is an added cost, but hopefully a positive benefit. The discretionary fund managers use a far wider range of assets, which can include direct investment in shares and gilts as well as the selection of collective investment funds. This direct investment is an area which holds real value and should lead to consistently better returns.

I am always a little wary when DFMs talk about producing bespoke portfolios for clients. My experience is that these portfolios look suspiciously like all the other portfolios from that fund house. But I am sure that the DFMs could defend that accusation by pointing out subtle differences that a generalist like myself would not notice.

Do DFMs provide better fund performance? This is difficult to confirm as the performance of their portfolios tend not to be published in the same way as retail funds.

Many DFMs do offer a personal service in meeting prospective clients and being contactable directly by the clients. Many clients like the personal service of meeting the person who is running their investment strategy and this is a tangible benefit.

For most clients, the use of multi-fund or multi-manager funds is the most common type of outsourcing. These types of funds offer diversity within themselves and their performance can easily be tracked by clients and advisers.

Many providers offer funds that have names such as governed portfolios, but these funds are simply very well marketed re-badged old-style managed funds. There is nothing intrinsically wrong with these funds, they have always done a decent job. I remember when I was at Pearl being advised that their aim was always to be above average, not necessarily shooting for the stars.

Above average is actually quite an ambition as by definition half of the funds available will be below average. Such are the vagaries of fund management that many respected fund managers have times when their funds under-perform when they have taken positions that do not match the current market thinking. Or simply a couple of their bets have not worked out.

This diversity is relied upon by advisers, perhaps too heavily. All too often, I see advisers putting the hole of a client's investment fund into a single multi-fund on the basis that it offers diversity. It does offer diversity, but it is still only a single fund. In my opinion, this greatly increases the risk of that fund to the client. A medium risk fund is taken up a notch on the risk spectrum.

I find it difficult to see how an adviser can call themselves an investment adviser if all they have done is get a risk questionnaire completed and popped all the money into a fund with an apparently

matching risk tolerance. Also, if they are using a managed fund, why are they still taking ongoing fees for reviewing a fund that is being reviewed by its own manager?

So as advisers strive to provide an ever-more cost-effective method of providing good investment management, the outsourcing of fund management would appear to offer a good solution. Freeing their time to spend with clients and buying in expertise that they may not have. A win-win for everybody.

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