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CASE STUDY: GOING BEYOND PRODUCT – PORTFOLIO SOLUTIONS USING MANAGED ACCOUNTS

Case study provided by netwealth

A new approach to portfolio management

In 1994, Neal Dunne was starting his career as an adviser in a world that was pretty much dominated by the insurance industry. Fifteen years later, in January 2009 and just after the GFC, Dunne started his own practice. His vision was to align the drivers of his business to the needs of his clients – a connection he felt was lacking in the private bank space.

Dunne, who is now a director at Moore Stephens, saw his role as being to help clients plan for their future; investments were just a part of the larger conversation.

At the outset, he saw the role managed accounts could play in delivering this. Initially, he worked with an individually managed account (IMA) provider, servicing clients with larger account-bases who didn't have much of a desire to involve themselves in the day-to-day, often because they had busy careers or were frequent travellers. But as the managed accounts industry entered the financial services mainstream, he worked out how to use it to balance his entire business.

Beyond product

Despite their rising prominence in Australia, much of the discourse around managed accounts focuses on their utility as an investment product. Quite often, they're compared directly to managed funds, and the conversation tilts towards products similar to traditional managed funds, but with greater transparency and direct or beneficial ownership of underlying assets. A portfolio of Australian equities, for example, but where the investor is an owner rather than a unitholder.

While managed accounts can definitely be seen this way, it's worth exploring how their broader utility can increase back-office efficiency in advice businesses, enable better scalability, and drive much higher levels of client engagement than more traditional approaches. Rather than just seeing managed accounts as a new way for clients to structure their investments, they can in fact be a means of revolutionising how an advice business operates.

To illustrate, Dunne tells the story of one family office client whose usage of managed accounts allowed for a seamless transition to the next generation.

"By taking the mantle of investment decisions away from the father," he explains, "and replacing it with a managed accounts solution, we allowed the next generation to come in and say, 'We know what the structure is, we know who the key investment managers are, and Dad doesn't have to make all of the investment decisions anymore.' Which means the children can get involved even if they don't necessarily have their father's in-depth financial experience.

"We've also been able to shift the relationship we have with the father from a very hands-on situation to one where he can step back and take a 'helicopter view,' which empowers the next generation to take a more active role in the process."

This was, Dunne adds, never going to work with a managed fund structure, because even though they can be useful, “The client had traditionally been involved in the buying and selling of investments, so a move into a unit trust was just not going to happen. The client was used to full transparency of the assets he owned and control over certain aspects of tax, which a unit trust structure could just not offer.”

Managed accounts have come a long way

Dan Miles is an investment manager whose company, Innova, specialises in managed account solutions. He has a deep understanding of the advice industry, having been exposed to his father’s dealer group at a young age.

His early exposure to managed accounts came from advisers who were using model portfolios but actually wanted Miles and his team to implement them on their behalf. At that point Innova was building its own managed accounts internally, but now it relies on providers like Netwealth to manage the process.

“There was a reason why we built our own internal managed account back then,” he says, “and there's a reason why we don't have it anymore: we don't need it anymore. There are now providers out there providing the level of flexibility and functionality and technology that's needed by a practice to run a decent managed account – that wasn’t the case five years ago.”

A whole-of-business solution

The technological piece is important: while technology has enabled a practices’ middle-office to generate statements of advice fairly rapidly, investment implementation in the back-office can be a deeply complex and unwieldy process.

Without a discretionary capability in a client's portfolio, dynamic allocation is more or less impossible, especially given the potential back-and-forth involved in distributing multiple records of advice. This is why direct equities portfolios tend to be highly concentrated in a small number of stocks, because the administration involved in, say, corporate actions over a larger range of stocks is prohibitively expensive and time-consuming.

And as a result of that situation, most direct equity portfolios tend to be dangerously under-diversified compared to managed funds, which can allocate to hundreds of stocks if needs be. Within a managed account structure – whether allocation is handled by netwealth as a platform technology or otherwise – advisers can provide clients with access to a much broader, better-diversified range of assets. This can, by the way, include managed funds and passive strategies.

When managed accounts are looked at outside of the product lens, their use as a holistic portfolio management solution becomes clearer: advisers can integrate and blend any number of different strategies to suit a client’s diversification needs and risk appetite – depending, of course, on the managed account provider being used - without many of the traditional administration headaches associated with monitoring and updating the portfolio over time.

Because of the more consistent and systematised approach of managed accounts as a portfolio management tool, there are also fewer compliance issues to deal with across the business. Miles suggests that by outsourcing to a professional investment manager via a managed account instead of the adviser trying to pick their own stocks or managed funds, the practice is more compliant.

“The old way is a pretty cumbersome process,” Miles continues, “because you can have different clients with different portfolios and portfolio drift amongst them. Some clients may not reply, or it takes a while before you get back to them. One just never knows what could occur.”

This is partly because changes in a managed account are made live on behalf of the client, executed by the platform provider almost immediately. Compare this to a model portfolio, for example, where any change to the model may take many months to execute across all clients in the book, because a practice is required to send out records of advice, get application and redemption forms filled, and so on.

Consistency and reliability

Matt Heine, joint managing director of netwealth, has spent a lot of time talking to advice practices. He also has a passion for looking at how businesses operate and what drives their growth, and commonly cites Uber, Vanguard and Singapore Airlines as some of his favourites, as they use technology to grow via unwavering consistency and reliability.

“By having a consistent and reliable business model,” he explains, “not only do your clients know what to expect and are then more likely to be advocates, but you can scale up your business dramatically. Consistency and reliability equal scalability.

“If you just think about what scalability is for a moment: it’s about being able to do those things that are important to your company’s success consistently and reliably so that you are growing your profit margin regardless of the amount of new sales or business that you bring on.”

More time for clients, what adviser doesn’t want that?

The overall benefit to the scalability of the back-office can be substantial when managed accounts is seen as more than just an investment product, but a whole-of-business solution.

Miles says he’s seen a number of advisers who have wholeheartedly adopted the managed account process, and achieved fantastic results. One such practice, he adds, has reduced its staff count despite seeing more clients today than they've ever seen before. Another practice he spoke to said they see about 40% more clients than when they weren’t using managed accounts, and they haven’t had to add extra staff.

The quote

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"There's no way he would have been able to have seen this many clients without having to put on extra administrative staff if he hadn't used managed accounts," Miles says.

Dunne adds that the use of managed accounts has led to "a business that had a lot more consistencies in it, which is efficient and cost-effective. And because of its systematised approach, it can also save on staff members, because they're not running a huge number of staff dedicated to administration."

Meeting client needs through a better customer experience

Beyond improving the efficiency of advice practices, managed accounts also often provide a better client experience.

From a client's perspective, managed accounts provide a greater level of transparency and control - something many clients are clearly looking for, given the inexorable rise of self-managed superannuation funds. This sense of control - empowerment, in a way - gives clients opportunities to explore different strategies they wouldn't have otherwise considered, largely because they wouldn't have understood them in a different context.

For example, recognising the differences and benefits of a small cap strategy or an income-generating one is going to be difficult for some clients at the abstract level. But with a transparent view of the portfolio, clients can actually see what that strategy comprises in terms of its underlying brands and companies. Which, in turn, enables them to make better (and more informed) decisions about structuring their portfolio in the future.

"You may have a client who thinks they're Warren Buffet," Miles continues, "and they want to go and buy stocks on the ASX. So you might allocate a proportion to a managed account, but exclude Australian equities, and then prorate up the rest of the portfolio. That way the client can go and pick their stocks if they want, but you're not doubling up on that Australian equity exposure. You can't do that in a unit trust. You can only facilitate that in a managed account structure."

Dunne recounts some clients where this holds true: there's often a situation where a person has outlived their spouse, but had no previous involvement or experience in managing the family wealth. With managed accounts, advisers can facilitate a situation where the spouse can take that "helicopter view" referred to earlier, understanding the headline strategy, without having to manage the day-to-day. This changes the conversation from investment ideas to education on strategy.

With FOFA changes now embedded, advice practices are starting to look to the future to develop and build better businesses. Advisers are looking outside of their industry and not only asking themselves how they can become more efficient but how they can service consumers wanting more transparency, more communication, more holistic advice. Managed accounts provide advisers this whole of business solution.

Ultimately, managed accounts should free advice businesses up to deliver their true value to clients, as Dunne described it, "It's about getting back to what it should always have been, and that's having conversations with your client about the important aspects in their lives and planning for their future, rather than just having discussions about investments." FS

CPD Questions

1. Much of the discourse around managed accounts focuses on their utility as:
a) An investment product
b) A savings vechicle
c) A tax structure
d) All of the above

2. What is needed to run a managed account?
a) Flexibility
b) Functionality
c) Technology
d) All of the above

3. One practice manager said they see what percentage of additional clients than when they weren't using managed accounts?
a) 20%
b) 40%
c) 60%
d) 80%

4. Managed accounts provide a greater level of transparency and control.
a) True
d) False

5. Advice practices are starting to look to the future to develop and build better businesses.
a) True
b) False

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