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Guide to Managed Accounts

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Managed accounts structures demonstrate maturity in face of COVID-19

The level of faith directed by financial advisers towards managed accounts structures appears to have been justified by the durability they have exhibited in the face of the COVID-19 pandemic.

There seems little doubt that, by and large, managed accounts structures have proved durable and effective in so far meeting the challenges of the COVID-19 pandemic.

As we mention elsewhere in this *Money Management* Managed Accounts Guide, the managed accounts sector finished 2019 in good shape and so it was axiomatic that it should be well placed to deal with some the extraordinary challenges which confronted the whole of the Australian financial services industry in March and April, 2020.

Indeed it is probably indicative of the robust shape of the managed accounts sector that in the midst of all the COVID-19 uncertainty, managed accounts services were continuing to be launched with the most recent being that of Endorphin Wealth which is indicative of the manner in which firms have been accessing the product set.

Endorphin's managed discretionary account (MDA) service is the product of a collaboration between investment consultant Oreana Portfolio Advisory Services, licensee Lifespan Financial Planning and platform provider BT Financial Group.

As *Money Management's* recent managed accounts webinar showed, collaboration and clarity represent key elements of managed accounts delivery with the sector having grown and matured significantly over the past decade to represent a significant portion of total funds invested by financial planners.

This is made clear by the most recent IMAP Milliman Census revealing that as at 31 December, 2019, funds under management (FUM) in managed accounts stood at $79.29 billion, an increase of $7.9 billion on the 30 June 2019 FUM total of $71.383 billion.

What was important about that data was that it followed on from a doubling in net inflows into managed accounts in the previous census period.

The net funds inflow from 30 June, 2019, to 31 December, 2019, was $5.722 billion or 8% increase on total FUM.

I hope you find this year's Managed Accounts Guide informative and useful.

Mike Taylor
Managing Editor

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In this time, *Money Management* has rapidly evolved from a B2B newspaper into a respected provider of accredited education and training, research, professional support and advocacy as well as thought leadership in the financial services space.

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Managed accounts proving resilient amid COVID-19 woes

Mike Taylor writes that managed accounts appear to have lost a number of their attraction to financial advisers and their clients despite the uncertainties and volatility generated by the COVID-19 pandemic.

While the impact of the COVID-19 pandemic has adversely impacted many investment products, managed accounts appear, thus far, to have weathered the extraordinary circumstances well.

Of course, the managed accounts industry entered the pandemic in good shape, with the Institute of Managed Accounts Professionals (IMAP) Milliman Managed Account Funds Under Management (FUM) census showing strong growth right up until the end of 2019 and with early indicators that the current census will show little slowing.

The IMAP/Milliman Census covering the

Continued on page 6

Managed accounts

Continued from page 5

period to 30 June, last year, showed that net inflows to managed accounts had doubled with FUM increasing to $71.383 billion. The 31 December census showed that FUM in managed accounts had increased to $79.29 billion.

With the census process currently underway covering the first six months of 2020, IMAP chair, Toby Potter said that the early indicators were that there had be no significant slackening in interest in managed accounts.

"And I suppose in the current circumstances you need to look at the counter-factual," he said. "If you did not have a managed account, what would you have?"

But that is not to say that financial advisers should be blind to the impact of COVID-19 on managed accounts, or their benefits.

A white paper generated by Philo Capital Advisers director, James Freeman suggests that one of the advantages of managed accounts structures in volatile times such as COVID-19 and, indeed, during the global financial crisis (GFC) is the speed of execution.

Freeman said that his research suggested that if financial advisers and their clients took the typical three months to activate a strategy, they could risk losing a significant portion of their advantage.

Indeed, Freeman suggests that the typical three-month delay might lead to the loss of up to 80% of the active excess return.

According to Freeman's white paper, the implementation delay generated by commonly used financial advice processes is "material, detrimental and avoidable".

"Our modelling shows the effect to be:

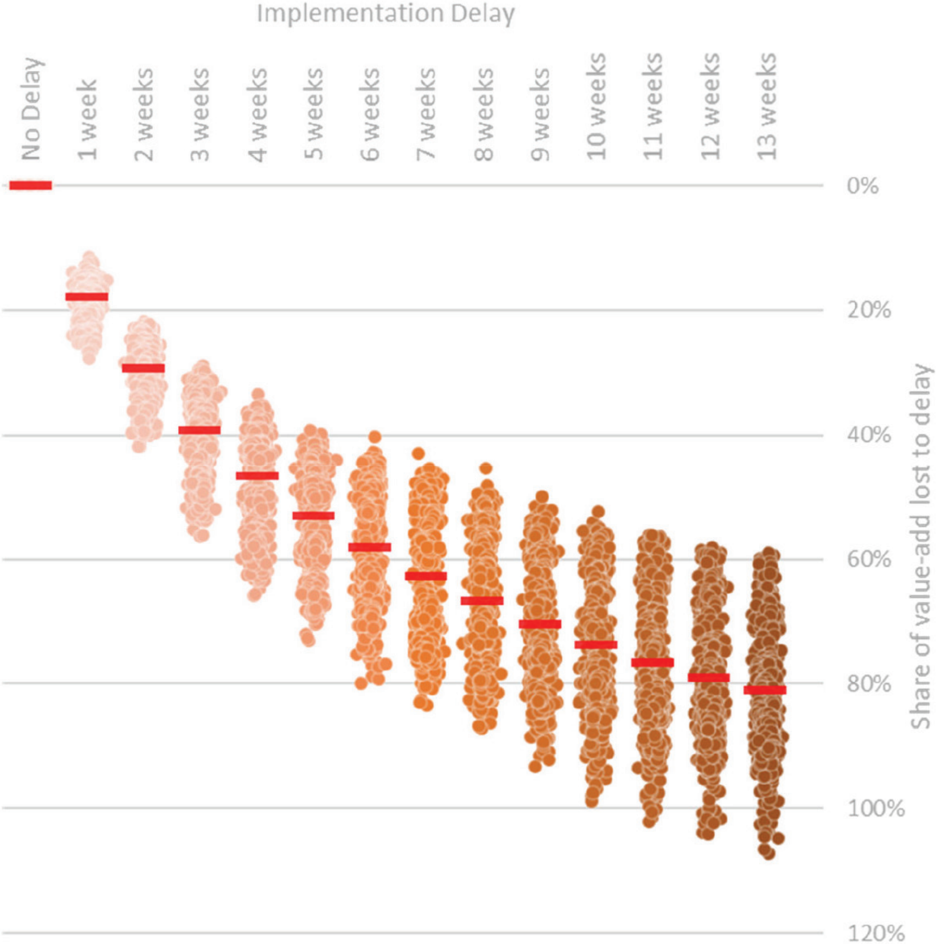
- Material – an average of 50% of excess returns are lost in the first four-weeks of delay;
- Detrimental – while some delays may, by chance, result in little/no effect, the average and vast majority of impacts were decidedly negative; and
- Avoidable – the most common cause of delay is the time needed to prepare, send and return a record of advice (ROA). It is common for a portfolio change to take up to three months before all clients respond and have their portfolios updated."

Freeman said that advice firms using discretionary management structures, such as managed accounts, implement model changes in a matter of days, avoiding the costs quantified in his white paper.

"Prompt implementation preserves the full value of an active asset allocation program. However, speed depends on the advice model being used. Implementing a model change via the record of advice (ROA) process can take up to three months or more to be completed for all clients, at the same time eroding up to 80% of any active excess return in that time," the white paper said.

And while the managed accounts segment is continuing to weather the COVID-19 challenges, it is doing so in the knowledge that, for now, the industry is not facing any immediate regulatory tightening with the Australian Securities and Investments

Chart 1: Share of excess return lost to delay



Source: Philo Capital Advisers

Commission (ASIC) in late March signalling that it was suspending work on its managed discretionary account (MDA) project.

The regulator was in 2019 undertaking an information gathering exercise which it said was aimed at better understanding the sector how it works.

ASIC has not yet outlined its timetable for resuming its managed accounts consultation process.

How managed accounts can help you navigate turbulent times

Managed accounts are an effective tool for advisers to efficiently implement their clients' investment advice.

Their strength is never more apparent than in turbulent markets when the ability to make timely tactical portfolio changes helps to prevent investors' long-term strategies being compromised by irrational reactions to market conditions. BT's Head of Managed Accounts, Zac Leman explains

A solution for volatile markets

Managed accounts can be an ideal solution for advisers when managing clients and their portfolios through an unprecedented market fall, like the one we've just experienced. Portfolio changes and rebalancing can be managed quickly and efficiently across multiple clients.

In late February 2020, financial markets were making headlines with their record highs. But at the same time, the world was on the brink of a health crisis. Parts of China were already in lockdown, new cases of COVID-19 were increasing dramatically, and Australia had only just started to feel the first ripples of what was about to come.

As the risks increased, some investment managers began to position their portfolios more defensively. Within a month, the Australian market had fallen by over 35 per cent. But by the time the market reached its bottom, Australia had already started to flatten the COVID-19 curve. This presented opportunities for investment managers to buy back into risk assets and position for growth, as sentiment improved, and the market recovered almost half its losses over the next two months.

BT's Head of Managed Accounts, Zac Leman explains "trying to implement this scale of change across a large number of individual or bespoke portfolios can be problematic and could take weeks for advisers to execute. During this time, the opportunity may be lost on both the downside and upside".

In contrast, managed accounts provide professional portfolio management based on a rational and systematic view of the market. This helps advisers minimise the risk of their clients making untimely emotional decisions that could permanently impact their future wealth.

Leman highlights one of the disturbing trends we often see when markets fall. "Investors often sell at the worst possible time. They crystallise their loss and then sit in cash or defensive assets while the markets rally."

Managed accounts continue their rise

"Long before COVID-19, the demand for managed accounts was already steadily growing," said Mr Leman.

Typically, advisers have recommended managed accounts to clients for their transparency, tax efficiency and portability. Unlike traditional managed funds, the transparency gives

Continued on page 10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Strategies

Continued from page 8

clients clear visibility of what they own within their portfolio and advisers can use this information to engage, educate and reassure them through challenging times.

Technology leads the way

Not only can managed accounts help fulfil compliance and governance obligations, they can also deliver material practice efficiency benefits. Although there's still the upfront work involved in making a suitable investment recommendation to a client, it's the implementation of that advice through a managed account that often yields the real benefits, including significant time savings around client reporting and communication.

An adviser must still determine the needs and objectives of each client and find the appropriate investment to meet their circumstances. But once invested into a managed account, ongoing portfolio management (including asset selection and allocation), corporate actions and rebalancing is generally done by the investment manager without the need for ongoing advice or consent. And provided the portfolios are managed within the parameters of the portfolio investment mandate or investment program, an ROA should not be required.

Leman goes on to describe how BT saw an 80% increase in the use of its digital advice tools in March as the pandemic hit. "Investors have 24/7 access to their portfolios through the BT Panorama desktop or mobile app, where they can see their holdings, transactions, fees and more. Visits to the mobile app doubled from the beginning of February to end of March, and of the total investor logins to BT Panorama, 50% of those were through the app."

Building stronger engagement

The broad range of managed account solutions means advisers can use them for a variety of clients and to suit their business. No longer reserved just for high net worth individuals, providers like BT are partnering with licensees and advisers to create their own managed accounts offer. It allows lower balance clients to access professional portfolio management, where tactical investment decisions may protect their wealth or help to capitalise on market moves.

In turn, advisers can better articulate and demonstrate the value of their advice and develop deeper relationships with clients. The role of an adviser as an educator is increasing, and Leman believes this is why managed accounts will continue to grow in popularity, especially during changing and turbulent economic times.

Learn more about how BT can help you find a portfolio construction or managed account solution for your business at bt.com.au/portfolioconstruction.

Managed portfolios helping to meet the growing consumer demand for sustainable investments

With over $79 billion in FUM[1], managed portfolios continue to surge in popularity, providing mutual benefits to clients and advisers.

Research by Investment Trends indicates that adopting managed portfolios can save advisers 13 hours a week[2]. That's a day and a half of extra time to spend getting to know your clients and understanding their goals and needs.

Aligning investments to client values

Increasingly, advisers are finding that clients want to invest in companies which reflect their own personal values. As such, managed portfolios are being shaped to reflect both the investment objectives and social priorities of investors in Australian and international markets.

These managed portfolios with an environmental, social, and governance (ESG) framework allow clients to make investments that either support companies that are making a positive contribution in matters of the environment, society or good governance or screen out those that are not.

ESG investment is no longer a fringe issue

In general, consumers now expect their money to be invested responsibly and the common misconception that there is no benefit to performance has been debunked.

Continued on page 12

Strategies

Continued from page 11

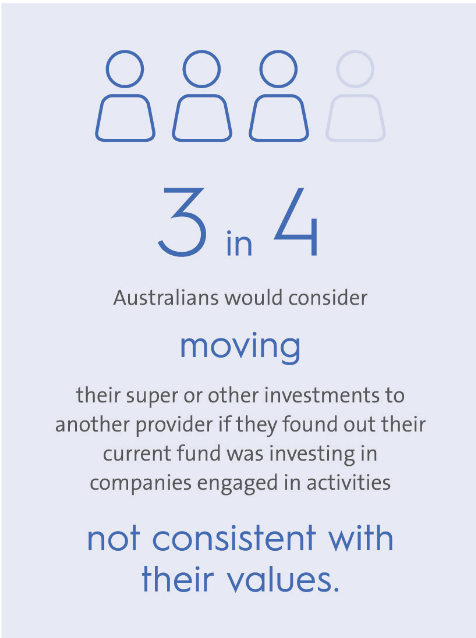
9 in 10 Australians feel it's important that their financial institution invests responsibly and ethically, and 3 in 4 would consider moving their investments if they found out their fund was investing in companies not consistent with their values.[3]

Guiding clients through responsible investment options

To meet the objectives of this large cohort of clients, advisers need to be equipped to guide them through responsible investment options. Australians rate being knowledgeable about responsible investment options the second most important factor when working with a financial adviser, behind prioritising maximising investment returns. In fact, 90% of Australians believe it's important that their financial adviser invests responsibly and ethically across the board[3].

Beware of greenwashing

The lack of common ESG definitions and standards has resulted in a wide variation of sophistication and depths of ESG practices across investment managers and asset classes. Unfortunately, this proliferation of products with immaturity of standards has also given rise to greenwashing. In investment management, greenwashing is when a company makes exaggerated claims about ESG-related



practices, products, impact or performance. This has proven to be a challenge for investors seeking truly sustainable funds.

The AMP Research team conducted a review of investment managers to understand their true capability in sustainability investing and to ascertain whether their sustainable philosophy is embedded in their investment processes.

MyNorth Sustainable Managed Portfolio

The MyNorth Sustainable Managed Portfolio is designed for investors seeking sustainable investment. It aims to deliver financial returns while making a positive sustainable change. An actively managed portfolio that invests in all asset classes, the portfolio includes managed funds that integrate ESG factors into their investment decisions.

The AMP Research team selected investment managers that aligned to the ESG principles for the managed portfolio. Fund selection for the portfolio is guided by three sustainability principles:

1. transitioning to a low carbon economy
2. avoiding material investments in thermal coal, tobacco, gambling, pornography and controversial weapons, and
3. encouraging positive ESG outcomes for the community.

The MyNorth Sustainable Managed Portfolio is designed by the Pendal's Multi Asset team using the hand-picked investment options by the AMP Research team. The portfolio has a balanced profile (70% growth and 30% defensive)[4] and offers an efficient way for you to deliver a sustainable, packaged value proposition to your clients.

Want to know more?

To find out more about ESG investing and how you can use the MyNorth Sustainable Managed Portfolio to help your clients invest based on their values visit **www.amp.com.au/mynorthesg** or contact an AMP business development manager on 1800 644 644.

1. IMAP Milliman Managed Accounts Account FUM Census Results as at 31 December 2019
2. Investment Trends February 2020 Managed Accounts Report, pg. 12
3. Responsible Investment Association Australia, From Values to Riches 2020: Charting consumer expectations and demand for responsible investing in Australia, pg. 5, 13 and 14.
4. The portfolio seeks to maintain a higher capital growth and may experience higher variability of returns or loss in any given year.

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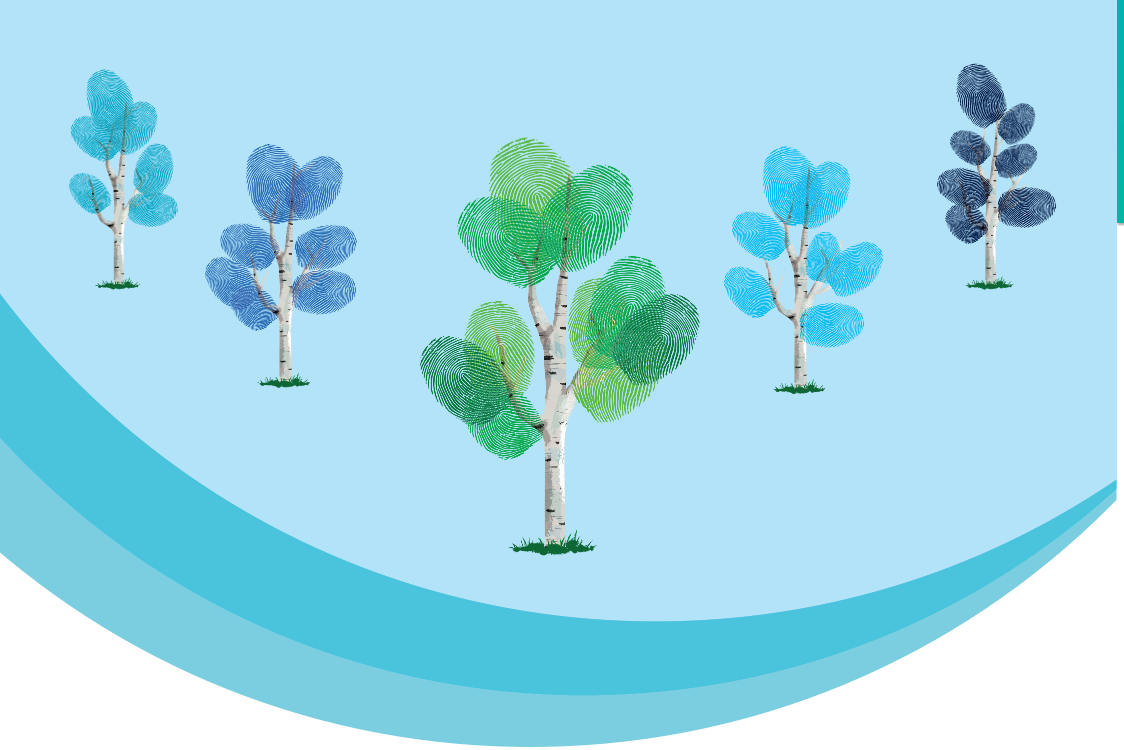

MyNorth Sustainable Managed Portfolio. A diversified portfolio focused on your clients' values.

MyNorth® now offers sustainable investing. Each investment is hand-selected by experts and combined in a multi-asset managed portfolio that helps your clients invest based on their values. All of which is why MyNorth is more than a platform.

Learn more and download our sustainable investing guide at **amp.com.au/mynorthesg** Issued by NMMT Limited. Read the PDS.

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- cash options.

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