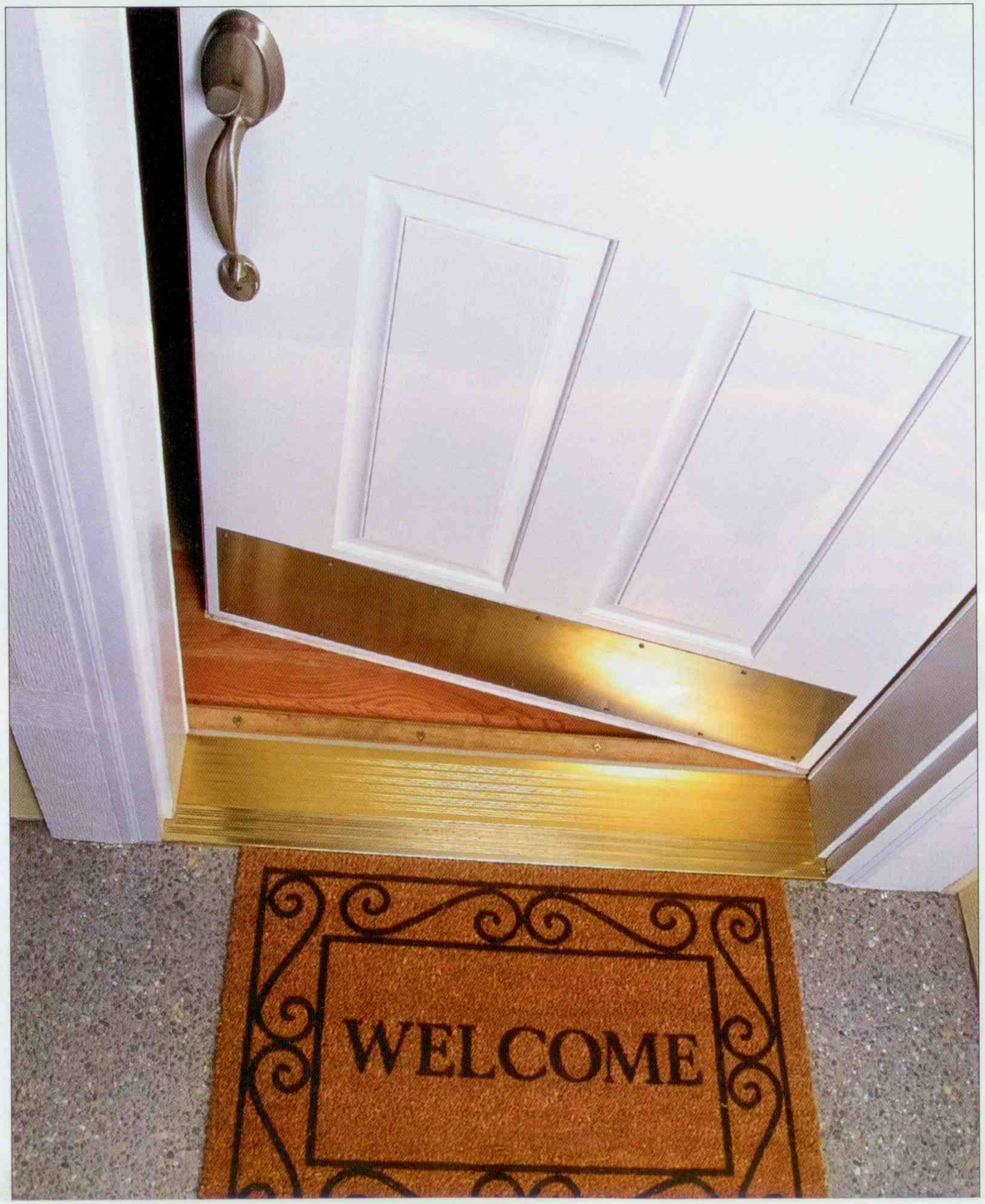

PETE BURTONSHAW

It may have taken over five years of development and debate, but wraps are finally being recognised as a mainstream offering within the UK marketplace. Meanwhile, the international market has moved rapidly on from wraps to the next major platform development: the separately managed account.

In the US, SMA inflows continue to soar as they broaden their appeal as the investment platform of choice. Across the Pacific, Australian analysts predict SMAs have the potential to threaten wrap platform providers, particularly those who rely heavily on independent, third-party distribution. With the imminent arrival of SMAs to the UK, might they have a similar impact here?

Before getting into the detail, the generic definition of platforms – as online services used by intermediaries and sometimes their customers to view and administer portfolios – should be accepted. This definition has been provided by the FSA and reflects definitions adopted internationally in the struggle to encompass the broad range of service offerings marketed under the banner of "platform".

SMAs are fundamentally platforms. They are an online service used to view and administer professionally managed investment portfolios. However, SMAs take advantage of improvements in technology and reporting in a unique manner that allows them to provide more cost-efficient access to professionally managed investments.

They do this by removing the traditional opaque unit to directly purchase the securities underlying the managed fund model. A legal umbrella is then wrapped around the pool of securities to ensure appropriate taxation shelter is provided to investors. The result is a retail collective investment scheme that is more cost-efficient and transparent than a traditional managed fund, plus it comes with all the reporting functions you

control over realisation of capital gains and losses.

As SMAs are relatively new, it is to be expected that they will have some short-term deficiencies when compared to their more developed platform counterparts. They are likely to include a lack of fund manager choice as the early model providers are most likely to be boutiques and specialist managers who have already outsourced their administration functions and are keen to secure additional distribution. However, as distributors flex their muscles and begin to direct fund inflows, the more mainstream managers will become aware of SMAs as another source of inflows.

Some managers may be concerned about their intellectual property being copied in the newly transparent world. However, SMAs do cater for this by providing the ability to delay the appearance of trading activity for several days.

Perhaps surprisingly, some advisers may be worried about increased client interest in their investments and the impact this will have on their servicing capabilities. Although this does require consideration, enhanced client engagement should be seen as an opportunity to build greater loyalty. As the industry moves increasingly away from the product selling to an ongoing servicing model, such engagement and loyalty will be crucial for a viable advice business.

Market impact

So now that more is understood what an SMA is, why SMAs are challenging platforms – and the impacts this might have on the marketplace – can be considered. The established platforms certainly provide many advantages to advisers, but the benefits to the investor are less tangible.

From their perspective, online access is far from innovative given the general development of internet services and use. SMAs have an edge in providing increased transparency and access to professionally managed personalised portfolios, but more importantly, they also deliver real cost benefits.

The relatively recent introduction of SMAs in Australia has begun to shake up the industry as

Come on in: will advisers welcome SMAs with open arms?

A warm welcome for SMAs

SEPERATELY MANAGED ACCOUNTS » SMAs are becoming the platform of choice for the US and Australia but will they challenge the dominance of traditional platforms in the UK

would expect from a platform.

Technological advantage

This use of platform technology to provide more efficient access to managed investments gives SMAs distinct advantages over existing platforms and managed fund providers. These include transparency because not only are all charges transparent, but so are all the underlying stocks. Visibility of real companies is more psychologically appealing for the investor than abstract units and advisers are able to benefit from this by developing deeper and more engaged relationships with their clients.

Another factor is cost. By removing any duplication of administration that normally occurs between the fund manager and platform provider, and by maximising the netting of transactions between fund managers, the SMA can provide cost savings of up to 40 basis points when compared to buying a similar fund through a wrap platform.

There is also the issue of branding. The SMA provides a variety of different branding and service ownership benefits to the adviser, ranging from simple white-labelling to full control over the service, custodian, broker, branding and pricing. For discretionary advisers, the SMA platform enables the efficient and scaleable management of customised portfolios for individual clients.

In addition, the SMA can be offered within a managed fund structure, making them tax-neutral compared to other collectives. Alternatively, they can be "unwrapped" providing increased the dominance of platform manufacturers is threatened and distribution once again gains power.

Australian analysts have predicted that those most threatened by the emerging SMA offerings are the wrap providers relying on independent advisers who are not tied to a single platform and are free to move towards superior offerings that enable them to take increased control of pricing and brand.

Smaller platform providers without deep pockets or sufficient scale to continue to invest to develop SMA capability are also likely to be left behind. Most major financial services companies in Australia now have an SMA development project underway, with many grappling with how to integrate and maintain legacy platform technology with the newer SMA platforms.

These trends should provide food for thought for providers still considering the development of platforms and for advisers who are assessing their options. If advisers do harness the ability for SMAs to give them the control they need to build long-term value in their business, while also providing more efficient access to professionally managed investments, it is possible that similar trends towards SMAs as an alternative to traditional platforms will be seen in the domestic market. Certainly many will welcome the increased potential SMAs offer to tip the industry power balance further away from providers and towards distribution.

Pete Burtonshaw is UK managing director for Præmium

main points

» Wraps are finally being recognised as a mainstream offering within the UK marketplace. Meanwhile, the international market has moved on to separately managed accounts

» Platforms are defined by the FSA as online services used by intermediaries, and sometimes their customers, to view and administer portfolios

» SMAs are fundamentally platforms that take advantage of improvements in technology and reporting, allowing them to provide more cost-efficient access to professionally managed investments

» By removing duplication of administration and by maximising the netting of transactions between fund managers, SMAs can provide cost savings of up to 40 basis points when compared to buying a similar fund through a wrap platform