Atchison

Research Report
July 2024

SMA White Paper

Illuminating
the way forward

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Industry backdrop

After a decade of growing regulatory pressure, the tide has turned for the financial advice industry. Having emerged as a profession and with compliance pressures receding, the challenge for financial advisers has turned to scalability, efficiency and, for many, work-life balance.

The fragmentation of the industry and exit of major wealth management groups means client acquisition is no longer a problem for most firms. Rather, the focus has turned to how to service a growing cohort of clients efficiently, while adding value and importantly running a profitable business.

Traditionally, more clients has meant more staff and thus more costs. Many firms have chosen the offshoring route for administrative tasks, but this comes with its own friction and associated issues when seeking to build at scale while maintaining consistent client experience.

As the focus of clients and the advice industry moves from product-driven, to wholistic, financial advice, investment decisions are becoming less of a consideration and differentiating point for clients. Despite this, the management of investments and their efficient execution, is one of the biggest time burdens faced by financial advisory practices.

Despite the wide ranging benefits of taking discretion over investment decisions, whether through a managed discretionary account (MDA), or separately managed account (SMA) the growth in the industry remains slower than many predicted.

We put this down to a lack of truly innovative options and a continued focus on the fund manager, not that of the client and their adviser. In this paper, we seek to highlight the benefits of an SMA for your advice practice and most importantly your clients.

What is an SMA?

An SMA or separately managed account is at its core, a financial product issued under a product disclosure statement (PDS). An SMA allows you, the adviser to recommend or invest directly into equities, bonds or any other asset class and benefit from professional management as you would with any other investment.

The SMA pools the underlying investments into a single investment within a portfolio, while allowing the investor to maintain ownership of those assets. Most SMAs are issued via platforms and the underlying investments typically include cash, exchange traded funds (ETFs), managed funds and other unit trusts.

Importantly, the assets within an SMA are not 'pooled' with other investors, meaning the investment decisions of the SMA provider do not impact directly on the investors tax position.

For advisers, SMAs afford the ability to either access the insights of a professional asset consultant or fund manager for a portion or for their entire portfolio. Alternatively, Atchison can also build SMAs that specifically suit your business and client profiles, understanding that one size doesn't always fit all.

Why use an SMA?

For an advice practice and more importantly, for the client, there are four key reasons why SMAs are the future of the industry.

- **Reduce administration costs:** Staffing costs and headcount remain the biggest challenges to scaling a financial advice practice. The requirement to send ROAs for each investment change and to then execute and administer each of these comes at a significant cost for every practice. Not to mention the risk and cost of human errors occurring in a volatile market. Using an SMA brings a significant reduction in administration costs, affording greater resources to focus on client experience.

- **Reducing implementation lag:** An extension to the issue of ballooning administration costs is the lag that is associated with the issue and execution of ROAs. The gap between preparing and executing advice for the most efficient firms can be several weeks, without giving consideration to travel and other interruptions to life. Research shows that the use of SMAs can reduce implementation lag from four-weeks to just a few hours, and prevent 44 per cent of excess returns from being lost.

- **Complete transparency and control:** Among the most common requests of those seeking financial advice, is for greater transparency over their investments and some control of their investment decisions. SMAs, as opposed to most managed funds and alternate products, offer complete transparency into the underlying investments of the portfolio and access to line-by-line data including franking credits and distributions, helping to deal with even the most active, engaged clients.

- **Investment cost savings:** Extended from the ability to reduce administration costs and staff working on non-client-facing tasks, is the ability to significantly reduce the cost of the underlying portfolio of investments. Atchison advises on over $27 billion in assets across institutional and advice clients, which affords us the ability to negotiate significant discounts to the management expense ratios (MERs) of some of the largest and most popular investment funds, reducing the fees you must justify with your client.

> The cost of delay is a costly mistake. A four-week delay saw 44 per cent of excess returns lost.

Why is an SMA better than a managed account?

There remains significant misunderstanding around the different options available to advisers to scale their business. Both SMAs and managed accounts have their own benefits but are ultimately suited to different business types and client cohorts, along with the level of risk that advice firms are willing to accept.

The challenge, as always, is overcoming the vested interest that lies within the financial services industry to determine the most suitable solution for you and your clients.

Having worked closely with several financial advice firms over several decades, but more importantly, working closely with leading retirement investment specialist firm, Wattle, we have found SMAs the more flexible and beneficial option.

Managed accounts are differentiated from SMAs by the fact they are a service, much like an ongoing fee arrangement, which must be signed by the client. As a result managed account services or the balanced funds you may recommend to clients, must be reviewed for their suitability every 13-months at a minimum.

With SMAs more broadly available on multiple platforms, they allow clients to transfer in existing holdings into the portfolio without any capital gains tax implications and importantly, the ability to stay with your current platform, something we know is important to advisers.

SMAs are required to have their own Responsible Entity above them, adding an additional layer of safety, while also having to meet stringent reporting and asset allocation guidelines.

How can SMAs align to you?

The question that advisers should naturally be asking is, *what's in it for me?*

Much of the SMA and managed account industry is focused on asset gathering and a near complete outsourcing of all investment decisions. While this may be suited to some practices, we know that for most advisers, investments are an important, albeit reducing, part of ongoing communications with clients.

This understanding was central to the construction of our suite of SMA products, which begin at the broad, multi-asset and risk profile level, being Conservative, Balanced and Growth, but extend well beyond this in an effort to provide control and input to the practices with whom we partner.

Rather than hiding behind a screen, or expecting advisers to outsource every decision, Atchison makes every sub-asset class sleeve available to each advice firm. This means you can tailor portfolios to the needs of each client, or your business more broadly, holding larger allocations to say alternatives, domestic or global shares as appropriate. We know that asset allocation drives the majority of returns, and using our asset sleeve options allows you to maintain discretion over this important decision.

In contrast to most of the industry, we see SMAs working in different ways for different cohorts of clients. Some may be suited to full discretionary models, others part discretionary and part direct, and then others completely non-discretionary. This understanding has guided the creation of these specialist accounts.

This control is complemented by extensive communication and reporting, that is guided by our experience in the advice industry. Rather the regurgitating common facts and macroeconomic issues, we provide specific, measurable highlights on a monthly basis, along with client-friendly talking points, as we know this is central to supporting discussions around performance.

Ultimately, our aim is to allow you more time to spend with your clients, affording the ability to build deeper relationships and continue to grow your business.

Our commitment to you

The financial services industry has been overly focused on product distributions and funds management, which is why we commit the following to our clients:

- Timely and client-centric communication on performance and portfolio changes.
- Managing risks appropriately and not seeking to time the market in the short-term.
- Not over trading and always remembering that costs and client experience matters most.
- Listening to our clients to understand their needs and expectations.
- Focusing on our fiduciary duty to you, ensuring your clients have few, if any reasons, to be worried about investment performance.

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