



Hello and welcome to the Winter 09/10 edition of Elite's client newsletter.

A great deal of change has taken place over the past few months since our last newsletter as well as the departure of our esteemed CEO, David Pook, who remains in touch and wishes you all the very best.

In this latest edition we provide you with an insight into how we, as a business, are responding to the two high profile pressures that we all face in this industry at present; the recession and the FSA's ongoing consideration of the Retail Distribution Review (RDR).

Paul Wilcox, Chairman of The WAY Group, recently wrote a piece for New Model Adviser magazine providing an interesting insight into Distributor Influenced Funds

(DIF's), as the FSA refers to them, and how they are as valid today for portfolio style managers as they have ever been and will continue to be, even after the results of the RDR are known.

Andrew Stevens, Chief Operating Officer, describes a recent development in the provision of Fund Accounting services to WAY and all of our Elite Funds.

Meanwhile, I talk about our latest partnership with Cheviot Asset Management and their latest offering, the Climate Assets Fund, a joint venture with Holden & Partners Limited.

Lastly, but perhaps most importantly, is our response to the FSA on the RDR.

We hope you find this information useful and your feedback is, as always, very welcome. It is worth noting that it is my intention, and that of the senior management of WAY, to get round to see our clients on an altogether more regular basis so you should expect to hear from me soon to arrange suitable dates.

Wishing you all a very happy and productive New Year.

David Williams



The pinnacle of adviser funds evolution



Peter and Mary Singer are recently retired and have been taking advice on how to invest their surplus savings which, of course, includes tax-free lump sums from both Peter's and Mary's pensions.

Their adviser works within a major IFA firm which has its own fund management company offering discretionary investment management to clients such as the Singers. They have been advised to place a large part of their available funds within the firm's own portfolio style collective funds with a smaller proportion directly invested in specialist funds and shares. They are concerned as to whether they are being shepherded into a fund which is as much for the benefit of the adviser as it would be for them.

This is an interesting dilemma which in some ways is part of the focus for the FSA's current work on the much heralded Retail Distribution Review (RDR) and their recent thoughts on the merits or otherwise of 'Distributor Influenced Funds' (DIFs).

Following the 1980s scandals surrounding broker bond funds it would be lazy to simply write off 'own label funds' as yet another self-interested money-making idea for adviser firms. In fact in almost all cases this would be an incorrect assumption. To put these portfolio-style funds into context we need to follow their provenance from the discretionary investment services which have existed for more than a century, to their current highly contemporary manifestation.

It was traditionally the stockbroker to whom investors turned and the stockbroking community has a long history of managing individual bespoke portfolios for wealthy investors. The benefit of bespoke services was that each investor's own requirements could be satisfied, by an individually-tailored selection of investments making up a personal portfolio. Furthermore the client was in direct personal contact with their stockbroker and was able to derive confidence from the personal nature of the relationship. Going back one hundred years or more the whole industry worked in a more leisurely and controlled manner than hitherto, commensurate with the limited speed of communications and administration of the day. In spite of increasingly volatile markets throughout the 1920s and 1930s, the manner in which these services operated continued undisturbed.

It was only in the 1980s that a major sea change occurred following Margaret Thatcher's removal of exchange controls in 1979.

Investment managers then had increasing access to the international markets in order to buy shares in successful companies from across the world at the forefront of the new age of globalisation. This coincided with the information age when computerisation and global media access changed

the investment scene forever. From that point on it became extremely difficult to operate effectively as a private client stockbroker whilst holding oneself out as an investment manager. Each of those jobs became so specialised that it was impossible to do both well. Either you were a client-facing stockbroker or you were a specialist investment manager. This demarcation has fed through to the typical high net worth advisory firms of today, whether stockbrokers or financial advisers, and the person you see for advice is generally the GP who within the practice employs investment specialists to actually manage client portfolios.

All very interesting, but the relevance of 'own brand' portfolio-style funds is a direct consequence of this evolution and the various factors behind it.

I remember managing over 700 individual discretionary portfolios back in the 1980s in the build-up to the market crash of 1987. When a change of direction was called for, my colleagues and I trawled through every single portfolio marking out the necessary re-balancing prompted by our strategic decisions. This certainly meant that every client received our individual attention but the process was fraught with stress and difficulty.

I recall many times when we worked through the night, collating all the dealing which we deemed necessary and which, in an ideal world, we should probably have done a day or two earlier had our systems allowed it. The problem was that any decision, say, to reduce exposure to Japan, which had fallen some 12%, in favour of an opportunistic exposure to Hong Kong, which had fallen more than 50%, involved a real decision on each client's individual portfolio.

This was because every single client had a slightly different Japanese exposure, depending on when they joined the service and which Japanese funds were favoured at the time. This scramble to re-balance portfolios rarely involved an examination of each client's Capital Gains Tax (CGT) status because there just was not enough time to take that into account. This could always be justified by not allowing the 'tax tail to wag the investment dog'.

The result of that 1980s stockmarket fallout was a move by investment managers to convert these bespoke portfolios into 'model' portfolios, where clients with similar objectives and attitudes to risk held identical but suitably scaled portfolios.

These were then deliberately managed for investment results and CGT was put to one side. With this new 'model'

approach every single portfolio could be re-balanced in a trice because they were identical and could be managed via a simple spreadsheet.

Then in 1991 the unit trust regulations were changed, to allow collective funds which contained other collective funds to operate on a commercially viable basis. This was the penultimate step in the evolution of unitised portfolio management via portfolio-style funds. Compared with the evolved 'model' portfolios these new collective portfolios offered far greater economies of scale, much keener pricing (because of greater bargaining power) and complete freedom from CGT on underlying management. My own firm 'share-exchanged' most of those 700 portfolios spread across three 'models' into three newly-constituted unit trusts launched specifically for that purpose.

The most recent changes to regulations have allowed collective funds to mix and match underlying funds and direct equity investment, as well as to blend a much wider range of asset classes. This means that contemporary portfolio-style funds can now comprehensively and effectively mirror and replace virtually any (far less efficient) individual, bespoke portfolio.

There may be very good reasons why the Singers should seriously entertain the advice of their financial adviser. The first is that a good local and personal investment management department can be met and 'eyeballed' by the client to offer regular reassurance about the style and substance of the management – there is far more accountability. Secondly a good portfolio manager is not quite the same as a good fund manager. The portfolio manager is running portfolio substitutes and therefore has a keener eye on the overall risk aspects of managing the client's money. The specialist fund manager works to very tight specifications regarding where they can invest and to what extent they can protect their funds by going liquid (the majority of specialist funds require the manager to remain relatively fully invested within their specialist area since that is the objective of the fund as specified in the prospectus).

There is one final word of warning regarding the current obsession with performance tables. Do not be tempted to buy a portfolio-style fund based on performance tables. The job of a portfolio-style fund is to deliver safe and competitive 'portfolio' performance. This means that individual constituents of the portfolio (the underlying holdings) need to be competitive within their own sectors, from a performance perspective, but the overall portfolio itself is meant simply to offer a sensible and rounded financial lifestyle solution.

Paul Wilcox

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WAY Fund Managers' response to the recent FSA paper on the RDR (the Retail Distribution Review)

Overview

It is clear from the timetable of the RDR that the main recommendations contained in the above paper were conceived well before the UK, in common with much of the world, went through the banking crisis and 'credit crunch'.

During this serious economic tsunami a number of features within the UK financial services marketplace became evident which show quite clearly that the focus within RDR on the Independent Financial Adviser community possibly misses the most serious issues facing financial regulation. In a post-mortgage bubble, post-Lehman Brothers, post-Bernard Madoff world the radical aspects of the RDR do appear to be of the nature of a sledgehammer cracking a very small nut.

Furthermore, anecdotal evidence from complaints, statistics and elsewhere, seems to suggest that there are far more serious problems within bancassurers and their vested interests than there are within the IFA community.

Whilst there are obvious problems within the IFA community, the average IFA appears to WAY to be a conscientious advocate of the retail client. The average IFA does appear to operate in a transparent and reliable manner and remains personally answerable to clients within his/her community on an ongoing basis. This is arguably less true of the larger banks and insurance companies which tend to employ a more transient workforce.

The old adage "if it ain't broke don't fix it" has a younger brother in "if it ain't universally, radically broke don't universally, radically fix it". WAY Fund Managers has some fears that fixing the 'IFA problem' may do more harm than good. This does not mean we are against the spirit of the RDR, simply that we feel it is unnecessarily radical. Our following comments are therefore offered in the spirit of the discussions on RDR to date.

Advice Services

Whilst being in favour of making the unsuspecting public far more aware of the nature of the advice they may be receiving, we believe that the requirements being proposed for an adviser to be able to claim 'independence' are far too wide. There are very many advisers doing a splendid job for their clients, particularly those advisers who have been in the industry for two decades or more, who achieve exceptionally good risk managed investment returns for their clients without being specialists across the board in all forms of investment and asset classes. It surely does their clients no favours to relegate their advisers into a second division or even dis-incentivise them to the extent they leave the industry altogether. There is already a skills gap within the IFA community which is only slowly being filled by young advisers who have come into the business over the last 10 to 15 years. Undermining the IFA in the manner implied by the tough new recommendations will only push even more clients into the hands of the less independent bancassurers.

Remuneration Bias

Within Consultation Paper 09/18 at 4.23 it is implied that insurers can already offer a menu of charging bases for remunerating the adviser, whereas fund managers managing collective funds cannot readily do so. This is no coincidence in that insurance products have for many years included the facility to increase adviser remuneration to completely inappropriate levels. Because of this flexibility to incorporate opaque charging structures and pay disproportionate remuneration (we have heard of obscene initial commissions of up to 13%) the insurers are already equipped to deliver variable remuneration deducted directly from the product.

Fund managers, on the other hand, have always been rather better regulated and generally have similar industry-wide charging structures built into their funds (all of which have to be individually approved by the FSA at the outset) – often variable initial commissions of up to 3% and trail commissions of up

to 0.5%. Even in extreme cases where the fund manager is subsidising commissions, the maxima are generally 5% and 1% respectively. But in any case, the primary client document, the contract note, clearly discloses these rates.

The well refined and well regulated nature of collectives means that any measures to incorporate variable regular adviser fees are defective. Operating multiple share classes is a non-starter from a cost and TCF perspective and systems which rely on encashment of units/shares are extremely negative for the investor. Selling units/shares will generate unfortunate and unnecessary HMRC reporting and tax consequences with which most investors will not cope.

The only workable solution for collectives is for there to be a standard rate of potential 'trail commission' to be specified within the fund prospectus – probably 0.5% per annum – to be supplemented by variable rebate facilities, direct to the client in either cash or reinvestment terms, should there be no selected ongoing adviser remuneration. This would avoid any tax or reporting difficulties for investors but would still hold out the prospect of variable remuneration for advisers. Furthermore, it would be quite straightforward to ensure that rules were enforced whereby all contract notes and half-yearly statements included a standard statutory wealth warning about ongoing remuneration. This is already a common method of dealing with clients, such as independent wrap platforms, where trail commission rebating is standard.

Professional Standards

Whilst not wishing to appear negative about all aspects of the RDR proposals we would also advise caution on imposing a blanket requirement concerning IFA qualifications. The principle of 'grandfathering' has worked pretty well across many professions, including financial services. Surely there must be a means whereby grandfathering could be permitted during a transitional period, particularly if it were accompanied by a special status which had to be declared to clients. ■



WAY Fund Managers appointed ACD for Cheviot's Climate Assets Fund

We are delighted to have been selected by Cheviot Asset Management as ACD host for their new Climate Assets Fund. This is due to launch early January 2010 and is managed by Claudia Quiroz, an experienced investment manager specialising in environmental markets.

Claudia started out as an engineer which gave her a very practical and pragmatic approach to the impact that individual companies and their operations can have on the environment. She then worked with Henderson Global Investors for several years, primarily focused on the Industries of the Future Fund, which invests in environmental and social themes. She moved to Cheviot earlier this year to help develop the new proposition.

According to Claudia, Climate Assets Fund is unique and innovative in its scope. In spite of its name it will not be solely devoted to climate change but will focus on the pincer movement which includes climate change, population growth and increasingly scarce resources. Furthermore it will be a multi-asset fund which can incorporate bonds and commodities as well as straightforward equity investment, thereby offering the prospect of smoother returns with lower volatility.

The WAY Fund Managers team wishes Claudia and her colleagues every success with the fund and will be pulling out all the stops to ensure that they are supported in every possible way.

Summary

WAY Fund Managers is one of the UK's largest providers of fund hosting services to the wealth management sector. Founded by experienced personnel from a former leading provider of such services, WAY has been successfully hosting funds on a 'turnkey' basis for almost a decade. With hosted funds of several hundreds of millions of pounds, it continues to be a market leader.

WAY is an ideal 'partner' in facilitating a successful entry into the exclusive world of collective fund management, delivering bespoke portfolio style investment management to your clients.

WAY can help you at every stage of your project, giving you advice and practical assistance as well as handling all of the processes involved from conception and FSA application right through to launch and beyond – including PR exposure and advice on sales and marketing material and methodology to help build funds under management.

WAY can also assist existing managers who are seeking to improve on their current ACD service.

David Williams

WAY administration moves up another gear



The last year has been very challenging for most of us...

In WAY's case we have not spent the time twiddling our thumbs waiting for life to return to its more civilised norm. As the saying goes, "when the going gets tough the tough get going", and this is exactly what we have been doing during this market downtime.

If WAY has any USP on the third party fund hosting side it is our people and their friendly approachable style. It is this benefit which is mentioned by our longstanding clients time and time again. I suppose that in a business which deals with intangibles like money and investments it is the personal touch which makes all the difference to comfort and confidence.

We are delighted that this is our main differentiator but we are also very aware of what underpins this goodwill – the delivery of a quality service. We have spent much of the last few months refining the new Transfer Agency service which we took in-house at the end of last year. Now all queries in relation to client deals, contract notes and settlements are handled by our team in Wimborne which can directly access all relevant aspects of the paper/electronic trail.

The accuracy and convenience of our Fund Accounting services are also important to us and our attention was turned in that direction mid-year. Fund Accounting is the impersonal side of fund management in which we deal with the fund manager and make sure that all underlying dealing and portfolio maintenance is managed to a high standard. This involves accounting for and receiving all income and rebates as well as

accruing and paying out all fund expenses. It also involves daily portfolio valuation and fund pricing.

We have recently made arrangements to switch supplier for Fund Accounting services to Sharefunds, a subsidiary of Share plc, an AIM quoted company specialising in internet stockbroking and administration services. During the course of the next year all of our existing WAY and Elite funds will have their fund accounting moved to Sharefunds.

We are assisting Sharefunds to develop its existing fund accounting service very specifically to suit WAY and its third party clients. The Share Group has excellent software skills and is a real 'can do' company with a culture remarkably in tune with WAY's own outlook. Together we intend to develop the leading fund accounting system available in the UK – with the best available order placing/dealing facilities and straight through processing.

We will be consulting a number of our clients in this process to make sure that we are developing the service in line with clients' real requirements.

Meanwhile, on the home front, we have just negotiated with our landlords a new lease for much increased office space, more than doubling our current footprint. This means that in future our visitors will not be short of parking and they will be entertained in rather more comfort!

Andrew Stevens