WELCOME TO WHEREVER YOU ARE

THE FUTURE OF PORTFOLIO MANAGEMENT ON PLATFORMS

A WHITE PAPER FROM:

BEFORE WE GET GOING

This paper was commissioned by Standard Life Aberdeen (SLA). It looks at how advisers are managing their centralised investment propositions (CIPs) and some of the issues they currently face. But chiefly, it is about where we at the lang cat think this part of the market is headed.

Those of you familiar with the lang cat will know that we carry out these analyses every now and again, when we think the topic is pertinent, interesting and we have something to add.

We know what you're thinking. But no, this isn't an advert for SLA. This is, of course, a sponsored analysis. And naturally, SLA is going to commission a paper on a part of the market in which it feels it's particularly strong. But we thank SLA for agreeing to sponsor this paper free from any content relating to its proposition. You won't read anything about Standard Life Wrap, XHub, Standard Life Wealth or anything else yellow and blue in these pages.

Even with that, we applied some ground rules. First, SLA didn't get to check or challenge our analysis, especially concerning our view of the shape of the market, though of course they got to read the paper as it evolved.

Second, we made sure that the paper didn't include our views on the relative merits of certain platforms or CIP offerings over others. There's a time and a place for that and it's not here.

Lastly, we believe that organisations hire us for work such as this because of our independence and for the honest, direct and sometimes plain awkward opinions that come with it. The views we express here are our own and SLA had **zero editorial control** or influence on them. The paper is based on a combination of our experience in the market, our own research and views from the advisers we regularly speak to. The day we let ourselves be compromised is the day it all falls apart for us.

Trust that, or don't – but it is the truth.

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A NOTE ON RESEARCH

Throughout this report, we will make use of and make references to our research publications. Our proprietary material consists of:

- *Fixed That For You: State of the Platform Nation,* our 2018/19 guide to the advised platform market.
- *State of the Adviser Nation,* our inaugural study of adviser sentiment.
- *The Platform Market Scorecard,* our quarterly analysis of the advised platform market.

Please contact us if you'd like to purchase any of these publications.

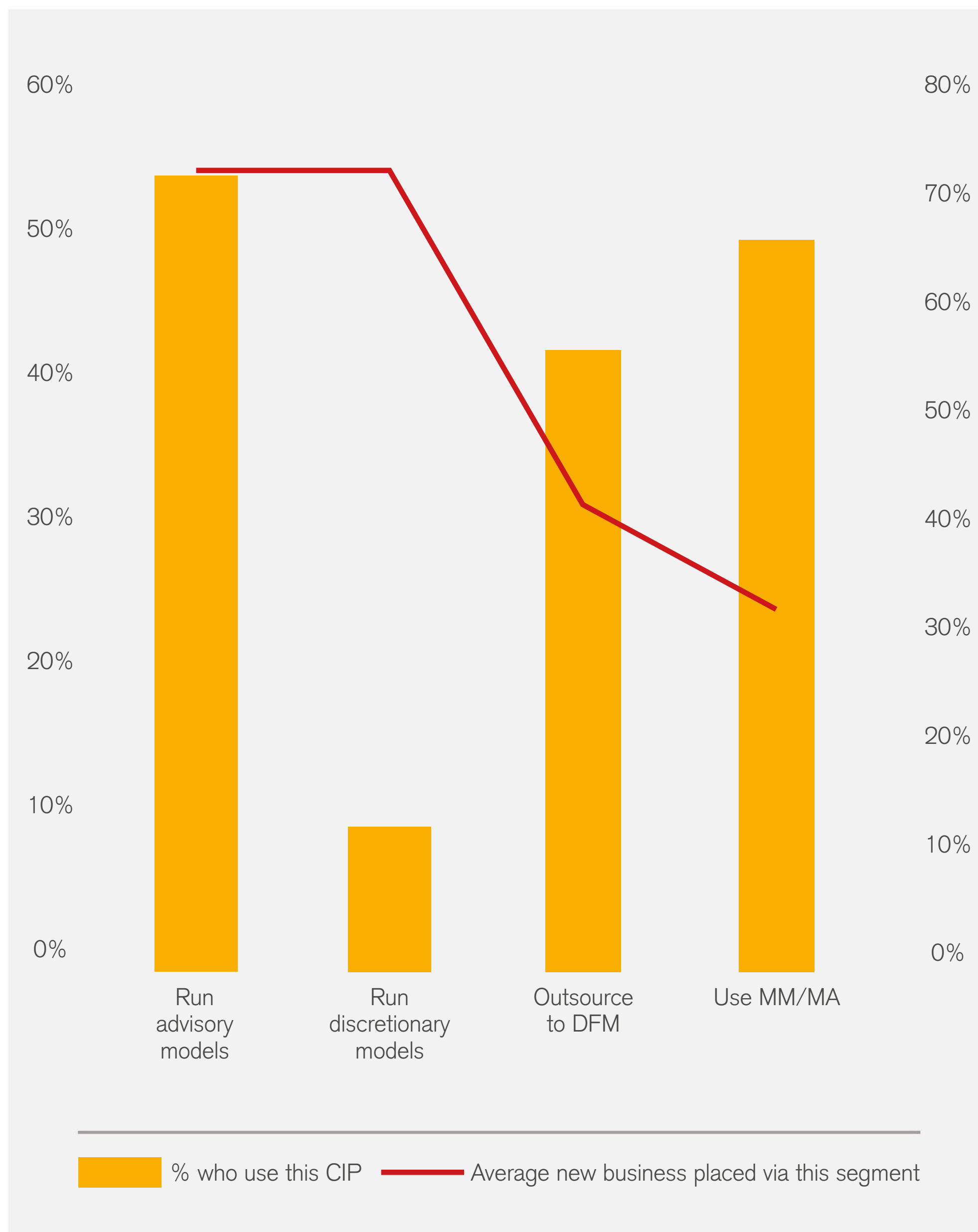
HOW DID WE GET HERE?

First things first, let's establish where 'here' is. Where do we find ourselves in early 2019 in terms of how advisers are constructing portfolios for clients? Who's up to what?

Well, according to our most recent research[1], we live in a market that relies heavily on CIPs, with a whopping 86% of respondent firms stating that they have one in place in one form or another.

ADVISER CIP USE

You can see from the chart below that around 55% of firms run their own advisory models, with significantly fewer running their own models on a discretionary basis. What's interesting, however, is that for those running these forms of CIPs, over 70% of their business (the red line) is allocated in this way.



1. State of the Adviser Nation (December 2018).

A sizeable chunk of respondents also either outsource to a DFM or use multi-manager/multi-asset funds, but you'll notice that a smaller proportion of business on average is placed here. Now, the eagle-eyed among you will have deduced by now that the numbers also don't add up to 100%. This is because many firms have more than one approach in place and are segmenting their client base in some way. We'll touch on this further as we work our way through this paper.

So we live in CIPtown, CIPville, population about 22,000. How on earth did we get here? And, most importantly, did anyone remember to bring bus money?

REMEMBER REMEMBER, THE RDR

CIPs aren't new – in fact plenty of firms were running models well before the retail distribution review (RDR); outsourcing to discretionary models wasn't so popular but certainly wasn't unheard of. But we think it's fair to say there was much more fragmentation of approach, and many more firms were creating bespoke portfolios for each client, albeit sometimes from limited fund ranges.

What a difference a few years made. Platform and portfolio management technology have industrialised model portfolios, open architecture is the norm and the increasingly interconnected world of adviser practice management software and reporting tools is bringing the client experience into the 21st century too.

WHERE WE'RE GOING WE DON'T NEED ROADS…

Rewind again for a moment. The Regulator Formerly Known As The FSA warned several months before the RDR came into force (via its guidance paper, *FG12-16 Assessing suitability: Replacement business and centralised investment propositions*) that it would be vigilant for indications of clients being shoehorned into portfolios not suited to them. But the mass commoditisation of portfolios means that shoehorning inevitably occurred.

The RDR emphasised the importance of consistent outcomes. If client B presents herself with similar needs and risk profile to client A, she should receive a similar proposition. That's hard to argue against, but what's evolved from that logical starting point is a market in which investors are stuck into a box (usually numbered 1-10) which may or may not be much help. In a way, regulation is now responding to a shift that occurred in response to regulation, in some sort of self-actualising *Back To The Future* regulation loop.

At the same time, the labelling of model portfolios and risk-managed solutions has repeated the managed fund sins of the past and made a bit of a mess of itself. The FCA's 2018 Investment Platforms Market Study Interim Report uncovered significant inconsistencies in the labelling and descriptions of risk-rated portfolios. For instance, it found that portfolios with labels including 'moderate' and 'balanced' had allocations to bonds ranging from less than 5% to over 60%. Go explain that variation to an end investor.

And so the industry did what it does: responded to regulatory intervention and tried to walk the line between creating structures which did the right thing by the client, but which were sustainable from a business management point of view. It's this *realpolitik* which has got us to the commoditised portfolio landscape which now unfolds before us. A landscape that has done much to break with bad old traditions – but which has developed a few of its own.

Let's get into a bit more detail.

WHERE IS 'HERE', *EXACTLY*?

We know from our research that the platform CIP market breaks down into the following segments:

- Picking a multi-manager/multi-asset fund range.
- Running advisory model portfolios.
- Running discretionary model portfolios.
- Outsourced to a discretionary fund management (DFM) model portfolio service (MPS).

In order to set the scene, we're going to take a swift look first at what we reckon is good and what might be…well, a bit less so.

MULTI-MANAGER/MULTI-ASSET

Pros

- **Simplicity:** any regular rebalancing carried out by fund manager/s, rather than being the adviser's responsibility.
- **Portability:** most multi-asset and multi-manager funds are available on most platforms.
- **Sleep easy:** if the firm is focused on financial planning the adviser will be content to let investment professionals do what they do.
- **Tax efficiency:** no asset-level capital gains tax (CGT) implications, as rebalancing and selection changes occur within the fund.

Cons

- **Tax inefficiency:** depending on individual circumstances the adviser could be storing up an eventual CGT liability over time (obviously only within general investment accounts).
- **The single line of stock issue:** how does an adviser demonstrate the value of what they're doing for the client when the investment report contains just a single line? There's some work being done in certain parts of the sector to improve look-through reporting and functionality, but it's far from the finished article.
- **Concentration risk:** what if the adviser disagrees with the fund manager outlook, strategy or positioning? Out goes baby, bathwater and all.
- **Charging:** separating investment expertise from the rest of the advice process leads us to question the long-standing adviser charging model. The same point naturally stands for the other outsourcing models, but ad valorem charging set against the simplicity of the multi-manager/multi-asset approach leaves it most open to challenge. To be clear, we're not suggesting that people should value tax planning, behavioural coaching et al less than investment expertise, just that a direct link between adviser charges and investment performance doesn't feel right in an outsourcing environment.
- **Expense:** some of these funds charge a small fortune for what they do – ongoing charges figures (OCFs) of up to 2% are distressingly common.

OWN MODELS – ADVISORY

Pros

- **Staff retention:** doing it yourself enables firms to keep investment expertise in-house. Where portfolio management is outsourced, there is a risk that key personnel will follow it out of the door.
- **Control:** the ability to retain full control of the client proposition to suit client demographics and needs.
- **Differentiation:** the potential to differentiate the firm by demonstrating additional expertise to the client.
- **Succession planning:** a business that 'owns' the intellectual property of investment construction may be more attractive.

Cons

- **Admin:** one person's investment management is another's administration headache. Disclosure alone (post MiFID II) is a huge task.
- **Client permissions:** we reckon this gives advisers a dilemma. Do I do what's best for my client and exceed my permissions or do I wait to hear from them?
- **The trail of dead:** version control and old versions of models with a few recalcitrant clients left in them is a real issue.
- **Scalability:** it might be ok for a one-man band, but we reckon that without the strictest of strict process management this practice could become untenable for larger firms.

OWN MODELS – DISCRETIONARY

Pros

- **Focus:** much of the admin falls away and the firm can concentrate on giving advice and running money.
- **Scalable:** the marginal lifetime cost of adding a client to a discretionary model is far lower than adding one to an advisory model – and probably adds more future value to a business.
- **Kerb appeal:** the tidiness of a well-managed discretionary book may well be attractive to potential purchasers in future.

Cons

- **Expense:** obtaining discretionary permissions is an expensive business, not least because of professional indemnity insurance and capital adequacy cover requirements.
- **Shoehorning risk:** keeping the book tidy and low-impact in terms of admin increases the temptation to put clients into a model whether they truly fit there or not.

OUTSOURCE – DFM MPS

Pros

- **Specialism:** the focus of the adviser firm rests exclusively on the specialism of financial planning, with investment left to those who do that for a living.
- **Regulation:** the approach can help with segmentation by client need (crucial for MiFID II/PROD compliance), especially where firms use more than one outsource partner.

Cons

- **Expense:** often the most expensive route (albeit less so than full discretionary outsourcing), with clients paying the OCF + advice fee + platform costs + ad valorem charge (plus VAT) to access the DFM portfolios.
- **Complexity:** a lack of clarity and consistency from platform to platform on the tripartite arrangements needed between adviser, platform and DFM.
- **Opacity:** it can be very difficult to research these propositions. Research tools are improving, but we're still some considerable distance away from straightforward, whole-of-market research.
- **Tax:** the DFM doesn't know the end client, and so will rebalance with no consideration to the customer's tax position or other holdings outside the model.

THINGS THAT KEEP US AWAKE AT NIGHT

The fact that portfolio management on platforms keeps us from our eight hours isn't necessarily something we'd normally share, but here we are. And if we're up, then you might as well be too.

UNINTENDED CONSEQUENCES

We've identified eight – count 'em! – key issues. Let's run through them one by one. As you read, we'd like you to consider your own portfolio management approach and be honest with yourself as to whether any of them might be applicable to your firm.

SHOEHORNING

WHAT'S GOING ON

Various research studies, including our own, find advisers tend to offer just one form of CIP. With up to 70% of flows going into these models, it's hard to reconcile their flaws with near-universal suitability.

ADMINISTRATION

WHAT'S GOING ON

Advisers encounter a plethora of administration niggles when creating and maintaining model portfolios. These include version control, rebalancing, managing permissions and quality of reporting, and that's when things are working properly.

WHAT MIGHT HAPPEN

The same answer applies for both these issues – it's the technology, stupid.

Next generation tech will bring greater individualisation and control, allowing advisers to create bespoke portfolios that help them comply with their segmentation requirements. Model portfolios will remain the framework, but individuals will have investments tailored specifically to their goals, ethics and needs.

COMPARISON

WHAT'S GOING ON

The lack of transparency around the composition of model portfolios makes them difficult to analyse and almost impossible to compare from peer to peer. Model portfolio performance and volatility data (from a comparative perspective) remain elusive, a disclosure issue that sits very uncomfortably with the post-MiFID II/PRIIPS/Asset Management Market Study (AMMS) world.

WHAT MIGHT HAPPEN

We hope very much that demand-side pressure will lead firms (both advisory and DFM) to embrace a more radical transparency. We suspect regulatory intervention may follow if it doesn't. The good news is that the operational issues involved can easily be solved by some modest technology developments.

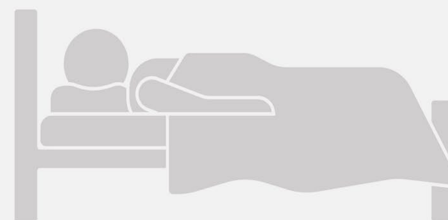
PORTFOLIO COMPOSITION

WHAT'S GOING ON

The overwhelming majority of portfolios we see are large baskets of funds (each with substantial volumes of underlying holdings), meaning that effectively you're often simply buying little more than the index. As the FCA pointed out forcefully in the AMMS, there's a vast amount of passive management that's dressed up as active and for which investors are paying active fees. MPS technology has also driven an almost total reliance on vanilla long-only mutual funds – few portfolios include investment trusts, ETFs or direct equities, for example.

WHAT MIGHT HAPPEN

This shares some DNA with the comparison point – radical transparency will help analysts find and point out those model portfolios which are genuinely delivering something different to a volatility-controlled quasi-indexing approach.



FRAMEWORK

WHAT'S GOING ON

The accepted wisdom underlying most portfolios was first set out in the 1950s, in Modern Portfolio Theory (MPT)[2]. Model portfolios are – in simplified terms – constructed on the basis that the main asset classes are largely uncorrelated, and so diversifying across them reduces volatility.

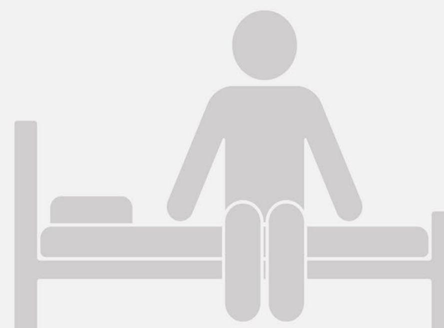
Research by Winton[3], an investment management and data science group, found that until the late 1990s, there was a much closer equities/bonds correlation than many might expect. Similarly, data show that for long periods there has been a positive correlation between US government bonds and the performance of the S&P 500 Index.

Finally, Markowitz's assertion that investors are rational and risk-averse conflicts with our growing understanding of behavioural economics.

WHAT MIGHT HAPPEN

We are already seeing some portfolio management structures break with Modern Portfolio Theory – for example, Scalable Capital's use of Lux and Marchesi's 'fat tail volatility clustering' approach (albeit Scalable is a robo-adviser rather than a full advice firm).

Most portfolios have not been tested for correlation in a full market cycle – if we do head into adverse markets in 2019 and beyond, we think more and more managers will look to revise their approach.



CIP versus CRP

WHAT'S GOING ON

Most firms – over 70% in our recent sample – don't change their models for clients drawing income.

We find it unlikely that existing portfolio solutions are sophisticated enough for the needs of an ageing population in a post-pension freedoms world.

WHAT MIGHT HAPPEN

The market should take care of this – various providers have either launched or are launching income-focused portfolios or multi-asset funds. These range from simple natural income strategies through to more complex three-pot propositions. Right now the proposition set is far too limited.

2. Harry Markowitz, '*Portfolio Selection*', first appearing in the American Journal of Finance, 1952.
3. https://www.winton.com/research/challenging-equity-bond-correlation-assumptions

SCALABILITY

WHAT'S GOING ON

This applies particularly to models being used for clients taking income. Client propositions are built around simple investment portfolios, but complex advice processes including sustainable withdrawal rate theory, sequence risk and in-depth cashflow modelling. Demographics dictate that an ageing client base will place significant stress on service propositions – can firms resource this?

WHAT MIGHT HAPPEN

The investment approach and overall client proposition for those taking income is virtually impossible to untangle. Again, packaged strategies are not widely manufactured or used yet, but these, with greater automation of advice processes and eventually the use of AI, need to take some of the weight off advisers' shoulders for all but the wealthiest clients.

CONCENTRATION RISK

WHAT'S GOING ON

Advisers, DFMs, wealth managers, providers and asset managers by and large all use the same handful of ratings providers. These power risk ratings, asset allocation models and volatility control techniques.

When – not if – we enter a bear market, there is a very high risk that the underlying assumptions on which most portfolios are built will be found to be flawed. Given the concentration in just a few providers, there is a danger of systemic failure.

WHAT MIGHT HAPPEN

We don't think there is a way of stopping this particular very low-speed car crash.

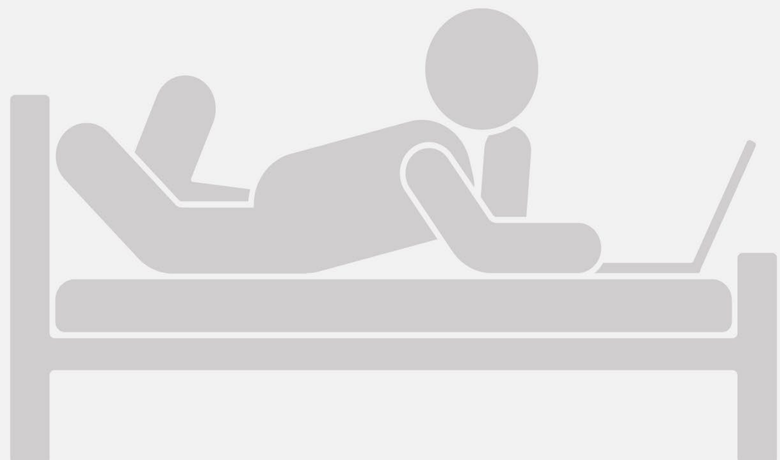
If models are found to be ineffective in adverse markets, this will surface in claims of suitability failures. Advisers and providers don't tend to question the output of the specialists upon which they rely, but it's them that'll be on the hook.

If we see evidence that active management fares better than index replication in adverse markets, this may disrupt some entrenched approaches.

How the future plays out depends on how well platforms, providers (including asset managers) and firms can anticipate and adapt.

On this we tend to concur with Bill Gates – "We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next ten. Don't let yourself be lulled into inaction". He was also responsible for Windows Vista, so bear that in mind.

Right, that's us thoroughly depressed. Let's move onto something more positive.



Here's where we have some fun, put our necks on the line and have a crack at what we think the coming years have in store.

We've identified seven themes; for each we describe them, set out a bit of detail about why we believe they're true and then give each a score out of ten for likelihood.

You have our express permission, future you, to have a read of this in 15 years, look at what's happening and have a right old laugh. That's if the robots haven't taken over by then.

1. DELINEATION OF INVESTMENT MANAGEMENT AND FINANCIAL PLANNING

WHAT WILL HAPPEN?

The functions of advice/planning and investment management will continue to evolve to become separate components of the advice process, both inside and outside individual firms.

WHY?

We believe that running advisory models and investment management functions under the same roof at scale isn't sustainable, given the burden that platform functionality and regulation place on admin. Doing it properly requires either discretionary permissions, outsourcing or simply very good processes with watertight controls. The last is made easier if platform functionality can keep investment management and planning functions separate.

Ultimately, the market will polarise to the point that true advisory models are generally found only in small specialist operations or in firms where functions are separated. With full financial planners on one side and discretionary managers on the other, those in the middle will be squeezed out.

As it stands, many firms have different people or different branches running elements of the same model, each of them dealing with version control, permission and rebalancing issues. If the industry was built again from scratch, this situation would simply not exist.

WHAT ARE THE CHANCES?

We started with an easy one because we see evidence of this happening right now. Of course it depends on the individual firm, but we reckon there's a 9/10 chance of this trend continuing for the time being.

2. BACK TO THE DRAWING BOARD ON MODEL PORTFOLIOS

WHAT WILL HAPPEN?

The technology that underpins model investment proposition construction will fundamentally change.

WHY?

A combination of demand and supply. Demand will be from all sides: the regulator, advisers and investors.

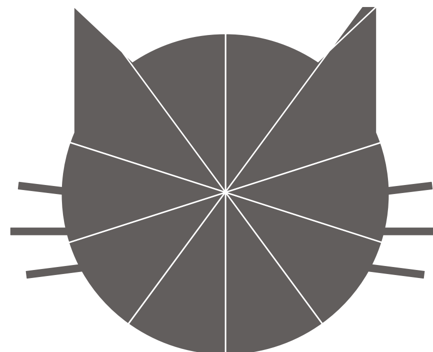
Supply comes in the form of the technology providers that make this kit. Distributed ledger technology has the potential to be a huge disruptor in wealth management and platforms, making certain processes much easier (i.e. know your client (KYC), onboarding), reducing admin costs and building and storing client profiles.

That client profile information could then be shared in a way that is secure, with trusted parties given full or part access and the outcome being a much more streamlined onboarding, fact-checking and transfer process.

And then there's all the stuff we don't know about because no one has thought of it yet. This prediction game is easy!

WHAT ARE THE CHANCES?

Tech will make things better? Slow down, Stephen Hawking! – 10/10.



3. INCREASED INDIVIDUALISATION

WHAT WILL HAPPEN?

Technology will enable adviser firms to cater for individual needs much more effectively.

WHY?

Model portfolios were supposed to answer the questions posed by the RDR by providing consistent outcomes. It hasn't entirely worked out that way.

The natural unit of suitability is one client at a time. Every step towards treating clients as a cohort reduces that suitability. Right now, genuine individualisation at scale is impossible – even in the limited realm of creating portfolios that take into account goals and investment time horizons.

We think the sector will move towards a commonly understood framework that governs how an adviser creates an individualised client proposition. This will be the plumbing that links risk assessment to goal setting to tax optimisation to reporting to rebalancing and so on.

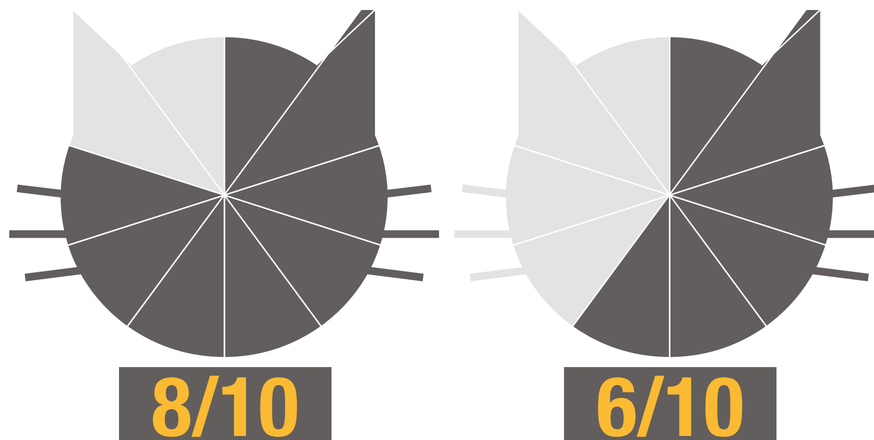
This framework could still maintain and enable a centralised, industrialised approach, but within which there is a degree of off-the-shelf functionality that provides greater flexibility and tailoring.

This, in turn, will allow advisers to tweak and tailor propositions to meet individual client needs and requirements. This has the lovely duality of championing the adviser's expertise by working in tandem with the investment component (which may or may not sit within the same firm) while also helping to deepen the client/adviser relationship.

Stretching it to one logical extension, individual investment propositions *could* become individual structures that are essentially little more than portable funds.

WHAT ARE THE CHANCES?

We think there's an 8/10 chance, given regulatory direction and technology developments, that increased individualisation will be a big theme over the coming years, though our exact predictions on how it shakes out are a 6/10. Many providers are working on this individualisation as we write.



4. A DOWNTURN BRINGS A RECKONING

WHAT WILL HAPPEN?

The current generation of investor assets are in CIPs that have yet to be truly tested by a crash. This next big downturn will be very revealing.

WHY?

As Warren Buffett famously pointed out, "only when the tide goes out do you discover who has been swimming naked". However, as the lang cat contends, "you really should wear pants whenever you're outside".

Regardless, not one discretionary or model portfolio has been through a full market cycle, while only a minority of multi-asset funds have track records going back far enough. Similarly, research suggests that the average fund manager has been in place for just seven years, leaving a vast number who haven't navigated a full cycle.

So what happens when the next big downturn finally happens? Many investors will likely find that downside protection doesn't mean quite what they thought it did. We'll also find out that not all 'balanced' or 'risk level 5' solutions (for example) are the same.

But ultimately, the industry will need to do some serious thinking about where to go next with investment proposition construction. There will be a revisiting of what investment due diligence/suitability looks like and of the need for time horizons to be factored into risk profiles. There may also be a reanimation of certain product types and mixes. We could easily envisage, what with this being a paper about us envisaging things, a swing back to annuities and guaranteed products for example.

WHAT ARE THE CHANCES?

A crash? It's virtually a cert: 9/10. We just don't know when (and we're not going to pretend that we do, even with our prediction hat on).

5. CONSOLIDATORS BECOME THE NEW VERTICAL INTEGRATORS BECOME THE NEW LIFE OFFICES

WHAT WILL HAPPEN?

As vertical integration heads to its logical conclusion, consolidators will effectively become life companies with their own investment solutions, tax wrappers and platform tech.

WHY?

This process is well underway – the businesses in which distribution, product and investment (or subsets of these) are within the same chain are showing no sign of slowing down.

The economic theory of vertical integration is that it's a win-win scenario, with the benefits shared across firms and clients alike. Whether that's the case in reality is a matter of opinion. This is a very polite way of saying that in a lot of instances it's very much not the case, in our view.

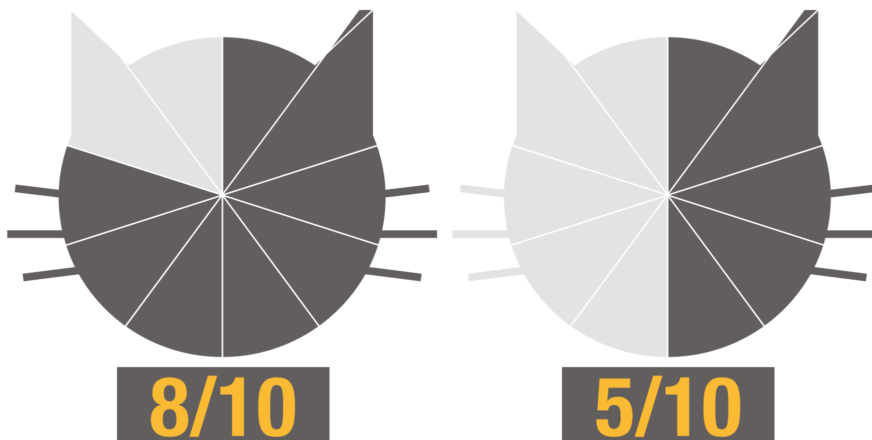
In most industries, competition combined with industrialisation of the supply chain creates downward pressure on the cost to the end user. The outcome in financial services, enabled by the opacity, is the opposite in many, many propositions.

Now, naturally in some instances this isn't the case and there are clearly pockets of good practice to be found. But what happens when the stars align and a consolidator finds a way to provide mass market advice through good technology and a low-cost investment proposition? All bets are off.

WHAT ARE THE CHANCES?

Current momentum continuing? Highly likely: 8/10.

A super, force-for-good Optimus Prime mass market model? Not for a while yet: 5/10.



6. SUSTAINABILITY VERSUS SENSITIVITY

WHAT WILL HAPPEN?

More sophisticated solutions will develop around sustainability of income.

WHY?

The implications of an ageing market for investment advice and portfolio management make for a fitful sleep, as we've already noted.

Servicing the needs of those clients requires managing the often complex matter of ensuring sustainability of income and also communicating the value of the solution, with clients who inevitably have declining capacity to engage with detail.

What's the tipping point? Annuities will continue to play a role (particularly when that crash happens and investor confidence declines) and we may see another generation of sophisticated guaranteed income products (including products that offer flexibility with some element of guarantee).

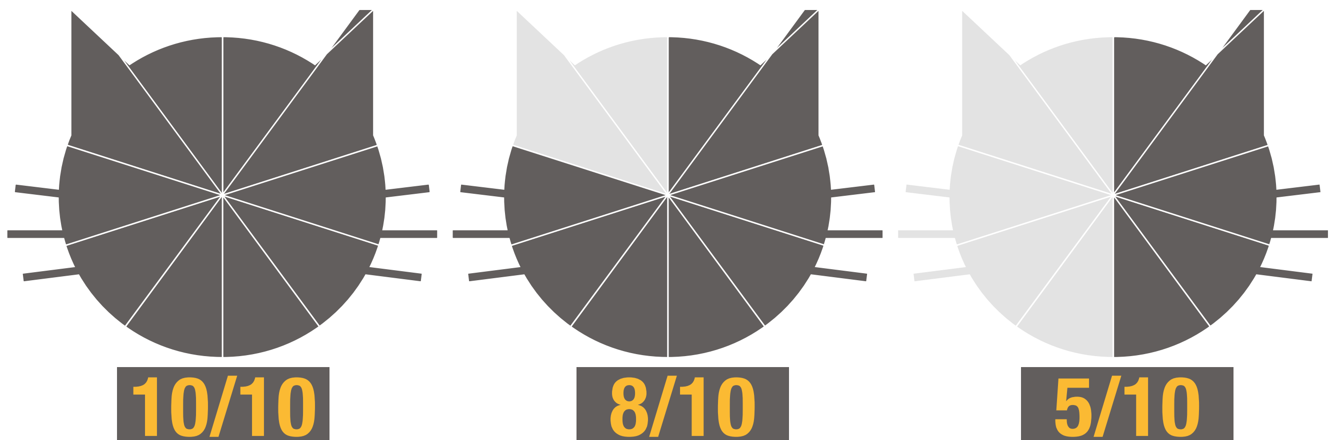
Data and technology will drive the market forward here. Guarantees may become more affordable as the industry harnesses the power of big data to design better products. But we retain a healthy scepticism due to the uncertain asset correlations we talked about earlier.

More pertinently, technology will provide income sustainability solutions. Algorithms that can analyse investment performance in the context of risk and objectives will enable portfolios to be managed, rebalanced and more easily reviewed. These don't exist yet, but they will.

The challenge at that point, however, is the eternal one (to pardon the pun) – engaging investors who really don't want to have to think too much about how long they might live.

WHAT ARE THE CHANCES?

10/10 that the technology to manage income in retirement becomes substantially better, simply because it really has to. We reckon around 8/10 that we see a new wave of guaranteed income products and around 5/10 that they fare better than their forefathers. We're betting on all the horses here!



7. DOWNWARD PRESSURE ON COSTS

WHAT WILL HAPPEN?

The cost of investing will continue to fall, including the cost to advisers of outsourcing to DFMs and the cost of actively managed and multi-asset fund ranges.

WHY?

This will be driven by a cocktail of regulation, technology and competition. Solutions will develop that (with the help of complex algorithms, machine learning and other things that us mere mortals can't hope to understand) make it ever-cheaper to harvest returns in a risk-banded environment.

This will contribute to a fall in the cost of outsourcing to DFMs. For all the advantages of outsourcing, advisers are being asked to carry out substantial due diligence on partners that will charge them between 25bps and 50bps (plus VAT) to run homogeneous risk-managed portfolios which provide returns that aren't necessarily any better than they could generate in-house.

With the regulator increasingly sharp on the value that such arrangements deliver for the end client, something has to give. Some DFM costs will come down to more palatable levels for the consumer, while many DFMs will come under cost and capacity pressure within their businesses.

We'll see actively managed funds and large-scale multi-manager/multi-asset ranges pulled downwards in cost terms too, albeit reluctantly. The Asset Management Market Study didn't pack the punch that many had expected as far as active costs are concerned, although conversations around value for money will have a gradual, long-term impact. The incentives to drive down costs will, for the time being, come from competition.

WHAT ARE THE CHANCES?

Ongoing cuts and efficiencies will happen, but we reckon there's only around a 6/10 chance that this will have a meaningful impact on clients in the near future.

WHAT DOES THIS ALL MEAN RIGHT NOW?

We've talked about things that keep us awake at night and the areas of the sector where we can see portfolio construction processes creaking. And we enjoyed having a crack at predicting changes that might take place in the medium- to long-term future.

But these musings are of little use to adviser businesses living in the here and now, with clients to serve and suitability duties to comply with.

Our sector is a funny old place. Best practice for constructing solutions for clients should flow from those who are closest to the client – advisers. But that's not how we work. Those who specify, build and maintain the core kit that the sector uses to ensure good client outcomes are often the furthest in the chain from the client.

We build first, and understand best practice later.

But that doesn't feel right in this regard. Portfolio construction is a fundamental building block in the edifice of client suitability. All the themes we've identified – transparency, value for money, technology and the ageing population, among others – will form the basis of how not just client propositions but both the advisory profession and the provider sector will evolve.

In short, we can't leave this one to chance, or to any one group. It's time to work together properly.

ACTIONS SPEAK THE LOUDEST

Here's how we think we can work together in the aligned interests of everyone involved – most importantly the client. We could:

- Agree that we are all on the hook as the **enablers of transparency**. Advisers can do more to disclose the details of their models. Exposing underlying holdings, cost disclosure in the post-MiFID II world and enabling proper comparisons of model portfolios are above none of us. Platforms can help by exposing those data in digestible formats. We need to improve the conversations we have and this will help.
- Alleviate day-to-day **administrative logjams** in DFM and adviser businesses through improved processes and controls and by getting different parts of software in the sector talking to each other effectively. That needs advisers and DFMs to be clear on their requirements, and for platforms to hunker down and build the pipes – not as part of a functionality war but in a collaborative way.

- Invest in **better investment functionality** to facilitate different trading and investment strategies, increasing choice and diversity of asset allocation models and investment objectives. Advisers can say thanks by taking time to engage and really understand how the functionality works and use it to the fullest extent possible.
- Take processes such as **portfolio construction and maintenance** (that need to be industrialised to allow scalable and profitable businesses) and overlay individual customer needs and requirements on the top. Some very clever people will develop very clever algorithms. They can come from anywhere; we'd love to see them being developed from the advice community.
- All play our part in alleviating the impending **ageing population capacity crunch**. Cash management functionality, sustainable withdrawal tools and algorithms and investment strategies that are aligned to client needs and goals will all play a key part here from the technology side. Firms can help by planning for scenarios where their advice demand from income-seeking clients increases by, perhaps, a factor of five or more.

YOUR STARTER FOR TEN…

Now, lots of the discussion in this paper has been interesting (we hope), but we have sympathy for adviser firms trying to fulfil their suitability obligations by navigating some 20+ platform propositions that form the market today. Some will have you believe that platform functionality is homogenous across the piece. That's true at a basic level. You can run models on virtually all platforms, for example. Box ticked. But the day-to-day devil is very much in the day-to-day detail and there are scores of differences at a practical level that you need to know about in order to make an informed choice.

With that in mind, we've drawn on our experience of managing platform suitability exercises on behalf of adviser firms to come up with a starter for 10 for the kind of questions we reckon you should be asking of both your potential and current platforms.

It's by no means an exhaustive list and we're focusing on adviser firms who are constructing their own portfolios as it's (a) the largest segment and (b) the one where we feel there is most to be learned in terms of how platforms differentiate.

Of course, if you outsource to a DFM then you're on the hook to research providers, along with key points of platform differentiation (such as 'What are your standard protocols/legal processes for setting up my agreements between the DFM and the client?' Or 'Show me examples of your cost disclosure and client reporting for DFM MPS business.'). Similarly, if you use multi-manager/multi-asset funds then you need to be comfortable that the range you use is appropriately aligned.

And that's it for Welcome To Wherever You Are. Thanks for reading. We'd love to hear your views.

PORTFOLIO CONSTRUCTION: 10 THINGS TO ASK YOUR PLATFORM

- What, specifically, are your processes for maintaining model portfolios? Please provide your process guides, screenshots and demos. How will you help to train the key people in my firm?
- How do you facilitate investment management and maintenance on your platform? Are they segregated functions? Are you able to provide gated access so that my firm can have different people responsible for different functions (i.e. separating out ongoing admin and onboarding)?
- What are your rebalancing protocols? Do you facilitate automatic rebalancing? If so, can you pre-programme automated rebalancing on a tolerance basis?
- How do you help me with version control? Does any aspect of your technology help me with client permission collection, recording and execution?
- How do you help me manage the tax liabilities of my customers? Specifically, if I run models on a multi-portfolio/multi-goal basis do you offer functionality that helps mitigate tax? Do you offer modelling software to help me with CGT liabilities?
- How does your model portfolio architecture help me with clients who enter the at-retirement phase? For example, can you facilitate multiple models for multiple goals?
- Give me an example of your model portfolio reporting. Show me what the client sees.
- If I step out of mutual funds into exchange traded assets, are there additional impacts that I need to be aware of (reporting, functionality, liquidity, cost etc.)?
- Does any aspect of model portfolio maintenance result in additional cost for the client?
- What is your roadmap for future developments specifically relating to portfolio maintenance?

TL; DR: SEVEN THINGS TO LOOK FORWARD TO

1. **Delineation of investment management and financial planning**

   Advice/planning and investment management become separate functions, both inside and outside of individual firms.

2. **Back to the drawing board on model portfolios**

   The architecture that underpins portfolio construction on platforms will fundamentally change.

3. **Portfolios become increasingly individualised**

   There will be much greater ability to easily tailor portfolios to individual needs.

4. **A downturn brings a reckoning**

   The evolution of the retail investment market since the last big downturn means vast amounts of investor assets are in strategies that have yet to be truly tested. This next big downturn will be very revealing.

5. **Consolidators become the new vertical integrators become the new life offices**

   As vertical integration heads to its natural conclusion, consolidators will effectively become life companies with their own investment solutions, tax wrappers and platform tech.

6. **Sustainability versus sensitivity**

   More sophisticated solutions will develop around sustainability of income in order to meet the needs of an ageing population.

7. **Downward pressure on costs**

   Each aspect of the food chain will be forced to justify its value for money for clients. Competition and technology will (gently) force costs down.

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