

The changing face of managed accounts

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Hedge fund managed account platforms were around long before the current boom in interest from investors began in the wake of the industry's liquidity crisis, the bankruptcy of Lehman Brothers and the uncovering of the Bernard Madoff fraud. But now the platform sector is characterised by dynamic change as investor money flows into managed accounts and competition grows from new platform providers from across the industry.

The initial platforms were owned, run and managed by investment banks, headed by Lyxor Asset Management but also including Deutsche Bank. But all this has changed over the past year as a result of the industry problems as well as regulatory changes, as a new generation of managed account platforms starts to emerge at different levels.

Some are being established by administrators, others by big fund of funds managers, and there are signs that a fresh wave of activity is on the way involving investment banks that have not entered the sector already. The result will be more price-competitive, flexible, user-friendly and transparent platforms.

Evolution of the sector over the past 18 months has been driven by price as well as conflicts of interest. The investment bank platforms have many pricing points, from custody and prime brokerage to structuring, risk management and distribution, all of which need to generate revenues. Although a complete in-house solution looks as though it ought to deliver economies of scale, it suffers from lack of competition within the structure.

MAG Consultancy has been involved in the design and establishment of managed account platforms that are not trying to compete with an investment bank's asset management arm, but whose components are delivered by providers that are cost-effective and well-resourced, have well-respected brands and are market leaders at what they do.

One key factor in these changes is much greater acceptance of the concept by hedge fund managers themselves. In the beginning it was assumed that the best managers would not countenance offering managed accounts. However, that view has changed since it became clear that some managers would not offer segregated accounts, such as Madoff, Amaranth or Bayou, because they were committing fraud or taking risks that they were not informing investors about.

The other main driver is big asset-owners with a fiduciary responsibility to their own investors. Pension funds or insurance companies investing large pools of cash have a responsibility to use the most cost-effective platform, employing the best available components and delivering information that allows them to make informed decisions. In this the alternatives sector is simply following the path adopted years ago by the long-only industry.

Managed account platforms has already lowered the barriers to entry for smaller institutions. Small family offices, charities, endowments and pension schemes have long enjoyed the benefits of transparency, liquidity, segregation of assets and verification through investment bank platforms, whether or not they are paying the right price. Now investors are waking up to a richer world of choice.

It's not just about protecting investors from mishaps or fraud, but informing them better about the diversification of their portfolio, how managers are really performing and making their returns, and whether investors can rely upon that information to form expectations about the future and make forward-looking portfolio allocations. It enables them to conduct better risk management and receive better risk-adjusted returns.

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