How to increase fund penetration in the Middle East

Fund penetration in the Middle East can only increase with greater understanding among clients about the value of diversification, as well as efforts to package funds into outcome-focused investments and overall portfolio solutions.

Increasing the penetration of mutual funds among investors in the Middle East is crucial amid efforts to build more sustainable portfolios in a region in need of diversity.

This is only likely to come about via more investor trust and education, combined with the ability to structure the offering in a way that creates a clear and consistent outcome for a client.

These are key elements which many product gatekeepers and fund selectors in the region – both from local and international retail and private banks – said at a roundtable in Dubai that they believe are key to delivering the right offering.

This is also the right thing to do for clients, which means it becomes good business for the bank in the long-term. At the same time, this will enable the banks to develop recurring revenue via stickier flows of business.

CHANGING MIND-SETS

For banks to be able to achieve this, and therefore deliver something relevant, practitioners need to better understand the motivations and needs of their clients, and then educate them about the opportunity to deliver more funds-led, outcome-based or packed solutions. Getting clients focus on the benefits of funds is also a vital element to address any negative perceptions about funds that have developed in this timezone.

This is not uncommon, given that a number of clients invested in a fund at the wrong time. They might, for example, have bought a tech fund in the late 1990s, or a real estate fund in 2007. A broader stumbling block has been the general mind-set towards investing. Most clients are not oriented

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towards alternative investments; instead, they tend to ask only for a simple income-oriented portfolio, or one that may demonstrate a local bias towards bonds.

It is crucial, therefore, for wealth managers to have asset allocation-based discussions with clients. This can involve funds directed towards achieving a specific goal – and even if the income target is lower than for a single bond, it is likely to be more realistic and reliable.

Helping the situation is the fact, say product gatekeepers across the industry, relationship managers (RMs) and investment advisers are pushing for more managed solutions using funds.

They are aware that this means there isn't the same requirement for them to be monitoring portfolios so intently on a daily basis.

A STEP TOWARDS SOLUTIONS

But the way forward, suggest fund selectors, lies in creating a different way to package and sell the funds – more as solutions.

Although not easy, this is possible. Shifting clients away from a one-fund solution to what might be considered a 'model portfolio' offering, is one avenue to explore.

This requires both the selection of relevant funds coupled with a specific advisory process to dictate how RMs can interact with clients, given individual risk profiles.

This is important as a balance is needed. The more funds put into a model portfolio, for example, the more complicated it gets for an RM to explain that to a client. Plus, it is more hassle for an RM to actually subscribe the client to it.

There can be further complications. For the client, while a model portfolio comprising perhaps up to 10 or so funds should meet the goal of being uncorrelated, there are also administrative costs.

RMs, meanwhile, must sign a time-consuming subscription form for the client for each of the funds in the model portfolio. So, if a client has put a weighting of say 7.5% in one fund and 15% in another, the RM has to tally up to the monetary value, which gets quite cumbersome.

One of the reasons for this is the bureaucratic arrangement for paying registration fees for funds. Every time a bank onboards a fund, it has to get approval from the regulator and pay them.

But this is about to change, with the onus in future being on the asset manager to pay the registration fees.

Some people believe this will encourage the growth of easily-available funds from the current universe of around 50 to something like 550, or more.

This is a significant increase from the 50 to 100 or so mutual funds that most local banks might currently have on their own platforms at the moment.

MAKING SELECTIONS

As the universe grows, however, the problem might become selecting from the large number of funds for the portfolio solution, to tailor it to each client. Past performance can serve as a guide to some extent, but this means little going forward.

Warming up to discretionary

On the portfolio side, while discretionary portfolio management (DPM) as a concept is yet to catch on in any meaningful way in the Middle East, such ideas are gaining in popularity.

Practically, product gatekeepers welcome this. It means they can avoid the need with model portfolios to register multiple funds on their platform and then get clients to subscribe and register into each fund, and then seek client permission for any desired changes.

Discretionary mandates are more flexible to manoeuvre around the funds within the content and guidelines of a mandate.

But whether institutions can tweak their propositions sufficiently to give engage clients in portfolio set-up discussions, and create enough flexibility and tailoring to make the DPM possible is still an unknown.

For instance, allowing clients to meet the portfolio managers can be an important as part of the selling proposition.

This, in turn, requires there to be the expertise on the ground to support such an offering.

There are some independent reference options out there. Morningstar's analyst ratings, for example, come from one-on-one meetings with the fund managers to determine the opinion. ■