

# Maximising investment opportunities: The rising relevance of DFMs

In August 2022, Discovery launched Cogence, South Africa's first truly global discretionary fund manager (DFM) as well as the first DFM to fully model retirement solutions by taking health experience into account.

As an independent DFM, Cogence plans to fill a gap in the country's burgeoning DFM industry stemming from the increasing scale and sophistication of global markets, as well as the vital link between health and wealth.

At a time when local investors enjoy unprecedented access to these markets, they also bear the burden of investment, as well as behavioural and longevity risk.

To take advantage of all that the world has to offer, the local advice industry stands to benefit from DFMs that blend local knowledge with truly global asset management expertise to deliver optimally diversified portfolio solutions.

To adequately consider the multi-dimensionality of individual retirement journeys alongside risk in a volatile and uncertain world, a blend of industry-leading technologies is essential to guide the conversation between financial advisers and their clients.

Yet, many retail investors – and indeed many investment professionals – are unclear about the added value provided by this once-niche complement to traditional financial advice.

Kenny Rabson, CEO of Discovery Invest, weighs in on why financial advisers should pay attention to DFMs.

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## What is a DFM – in a nutshell?

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A DFM is an established asset manager with the requisite licence and mandate to buy and sell investments on behalf of its clients.

In ideal cases, they have the research teams capable of assessing the vast global investment universe of unit trusts and passive solutions and the know-how to select from these to construct optimally diversified investment portfolios on behalf of financial advisers. Single-asset managers typically select investment instruments from within a unit trust fund. By contrast, a DFM, also known as a retail multi-manager, selects from multiple of these managers' funds to construct its solutions.

While some DFMs offer bespoke portfolio solutions to financial advisers, others focus on providing model portfolio solutions for a range of risk profiles that suit an adviser's clients.

Regardless of the approach, DFMs all essentially fulfil the day-to-day active investment management of clients' portfolios, therefore simplifying the investment process and creating efficiencies to the benefit of both adviser and client.

Best of breed DFM's pair global reach and expertise with technologies that are able to help digest the enormous complexity of markets and translate this into both real-time and forward looking insight relevant at the level of the individual portfolio.

## Why the interest in this sector?

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Globally, as well as locally, the use of DFMs has grown rapidly in recent years and most advisers expect this trend to continue.<sup>1</sup>

On the one hand, the investment universe grows ever more complex and sophisticated as well as more volatile and uncertain. As the number of investment options increases it is becoming practically impossible for advisory practices to build the internal research teams needed to keep abreast of it all.

While global diversification has become vital to local investors given successive relaxations to the offshore limits of regulation 28 of the Pension Funds Act, this complexity grows by orders of magnitude when looking abroad.

There are few companies in the world that have the analytic capabilities and global presence required to carry out the research to develop a comprehensive understanding of the risks and opportunities that exist in such a vast, volatile, and sophisticated investment landscape. On the other hand, the regulatory environment is becoming more onerous for advisers, which increases the compliance risk they face in their practices.

By bringing in a deep and broad level of local, and ideally global, investment expertise to perform asset management advice, DFMs allow financial advisers to focus on what they do best – providing financial advice.<sup>2</sup>

## What are some of the benefits of a DFM?

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The principal benefit of DFMs is that they offer much more investment and research expertise than advisers generally can.

Many DFMs emerge from other asset managers, and they have dedicated teams whose job is to focus on managing investments.

In the South African context alone, there are more than 1,000 unit-trust options available to investors. To know all their details requires significant research capability.

At Cogence we have brought in RisCura – who has established themselves within the South Africa manager research environment, with over 20 years of experience, and a dedicated team that conducts research on every fund manager in the country – to select the local component of fund manager selection.

Clearly, when looking abroad – as is necessary given that clients can now have 45% of their money invested offshore under Regulation 28 of the Pension Funds Act – this scope expands enormously.

We believe that a truly global footprint, with a presence and skillset in most major markets, is required to keep abreast of the global investment universe, which is why we have partnered with one of the world's leading asset managers, BlackRock.

DFMs have a FAIS Category 2 licence from the FSCA, which allows them to make changes easily on behalf of the individual client according to the investment mandate signed with the DFM. This removal of paperwork enables rapid changes to a portfolio in response to, or anticipation of, market events and opportunities.

A further benefit comes by way of the efficiencies of scale.

DFMs that reach a significant size can negotiate wholesale fee classes in the unit trusts selected, thereby reducing – or even nullifying – the overall DFM costs experienced by the end client.

This scale also allows DFMs to provide enhanced access to investments such as private equity, global hedge funds, broad passive solutions and private credit.

As we enter a period characterised by high inflation and uncertain, volatile equity market returns, these alternatives are growing in popularity.

Technology is another key benefit.

The pace and complexity of global markets alongside changing consumer behaviours in the wake of the Covid-19 pandemic and the increasing need for personalised, real-time, reporting and portfolio monitoring is quickly making the use of advanced technology indispensable in the world of financial advice. For instance, Aladdin Wealth™, an industry-leading portfolio analytics and risk management technology brought to South Africa by Cogence, equips advisors with a wide range of sophisticated tools that leverage data driven insights to help improve portfolio management and reporting.

This technology allows advisers to test their ideas for suitability against a client's portfolio while also being able to stress-test against future risk scenarios, such as a repeat of the sub-prime mortgage crisis.

Technology is also essential for factoring in modern demographic and behavioural trends that are becoming central to mapping out individuals' retirement journeys.

Finally, the combination of technology and expertise can greatly enhance reporting as a DFM can offer full transparency and a real-time overview of a client's investment picture based on a variety of personalised metrics.

Personalisation through digitisation can guide the conversation between adviser and client to overcome biases and help investors stay on track to meet their long-term goals, despite market volatility.

A DFM introduces top-quality strategic allocation, increases efficiencies in the advisory practice and improves investor governance, while allowing advisers to build better relationships with their clients, focus on their needs and find solutions to those needs.

Ultimately, as most advisers are focused on performance when selecting a DFM, the partnership should work to improve the investment outcome for clients.

<sup>1</sup> What are advisors thinking – NMG consulting on Ninety One <https://ninetyone.com/en/south-africa/insights/what-are-advisors-thinking>. 2020

<sup>2</sup> SOUTH AFRICAN DFMs, MULTI-MANAGERS & WEALTH MANAGERS – Insights into Investment Boutiques, RMI 2018 <https://bit.ly/3TYrEwH>