Opinion **Advice & Comment**

Beware of wealth managers quoting data

Ninety-four per cent of providers claim to deliver 'top' performance

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Moira O'Neill YESTERDAY

An investment manager once tried to convince me that a fund of funds, made up of a portfolio of other funds, was likely to perform better than a fund that invests directly in securities such as shares and bonds.

It was my first year of reporting for Investors' Chronicle in 2008 and he was responding to an opinion piece I'd written criticising the expensive layering of charges in these funds of funds, for often mediocre performance.

He showed me a graph of outperformance of funds of funds vs "ordinary" funds. I pointed out that while one period on the graph showed outperformance, the other did not.

However, the chap got so angry about my stubbornness to accept his argument and the “proof” of the graph that I felt obliged to leave — without finishing my hot chocolate. It was a very good hot chocolate, as I remember, but some of his spittle had landed in it.

It’s disappointing that 15 years on, we still need to be cautious when looking at graphs showing “outperformance”. That includes prospective clients of wealth managers, as well as journalists.

In addition to service details, plus associated perks such as exclusive invitations to exhibitions or time-saving concierge services, potential customers will be “sold” the investment performance that the manager delivers for its clients. In this pitch, you’re almost guaranteed to hear the words “we are top quartile”.

To be top quartile in investment performance terms, a firm needs to be in the top 25 per cent of performers in its peer group — that’s among managers investing in similar types of investments. And, when marketing fund performance, nobody wants to shout about being second quartile, let alone third or fourth.

Whether you are browsing websites, reading marketing literature or sitting in a face-to-face introductory interview with a wealth manager, it seems that they can all claim that their investment performance is better than their competition.

How can almost every wealth manager claim to have winning funds? These are regulated products, so they can’t lie to you or they would risk massive fines. Information presented to clients has to be backed by evidence and so it always is.

But there’s scope to cherry pick the best data. And an excellent new piece of analysis has shown just how easy it still is to do this.

The research is by Asset Risk Consultants (ARC), which runs the ARC Indices that collect the performance, net of fees, of over 350,000 investment portfolios supplied by over 140 investment managers, to establish the actual returns being seen by real clients. The analysis shows that up to 94 per cent of wealth managers can claim to deliver first-quartile performance by choosing different criteria to suit their needs.

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Its analysis explains how fund managers can potentially swing the data in their favour by using several different strategies. So, for private clients and their advisers, understanding exactly what performance is being presented is crucial.

First, it found that at any point in time, over half of any given peer group are able to demonstrate top-quartile performance. ARC says the reason is that when investment managers are presenting to potential investors and advisers, they have a great deal of latitude over the time periods used to capture performance.

ARC analysed the performance of discretionary managers in the ARC Private Client Indices ("PCI") Sterling Steady Growth risk category, which represents more than 50 per cent of client portfolios in the PCI universe of more than 200,000 sterling private client portfolios. It looked at four of the most common time periods: one, three, five and 10 years to June 30 2023. It found that 40 per cent of the data contributors could rightly say they delivered top-quartile performance over one of these time periods.

However, there was one manager who was top quartile over 10 years but actually bottom quartile over one, three and five years. Another was top quartile over three years, but bottom over one, five and 10. There were also a lot of managers who were good performers over one year, but poor performers over the long term. But it's the long-term picture that really matters to investors.

So far, this is a matter of selecting the most flattering time period. But the professionals can also use small differences of a few months in reporting periods to create a different performance picture.

This is particularly pertinent because the three-year numbers to the end of June 2023 have just dropped out of the "Covid results" — the period of the first half of 2020 when global stock markets crashed. ARC says that has undoubtedly changed the leading runners and riders, with a "very striking" difference between the top-quartile performers in three-year figures to June 2023 compared with the three years to December 2022.

So if managers can vary the end date on their one-, three-, five- and 10-year figures, between either June 2023 or December 2022, 57 per cent of managers can claim top-quartile performance.

If you queried why the figures aren't up to date in a graph that you're shown, it would be easy for a manager to tell you that their usual pattern of reporting is end of year. I'd insist on having the more recent figures before signing up for a service.

But there are other tricks that managers can use too. Most investment managers are investing lots of portfolios for different types of clients with varying risk profiles, investment mandates, approaches to portfolio construction and differences in holdings. ARC says by selecting a particular investment solution to showcase performance rather than the average outcome, a majority of discretionary managers can present results that show them to be top-quartile performers.

A good question to ask would be: "What proportion of the firm's clients are following the investment mandate that is being presented?"

Technically, they are not misleading you. But you should pay close attention to the data you're given, and make sure the sales patter stands up to reality.

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