

YourQ&A: How Do SMA Managers Deal with Fee Pressure?

YourQ&A published on Nov 18, 2009

Discuss this YourQ&A Question

Wirehouses are squeezing manager's fees. Are firms planning to invest more resources in RIA and independent broker-dealer channels or stay the course in this environment?

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Answer

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In the very early days of the separately managed account (SMA) industry, fees could be 60 basis points or higher. Today, however, fees are considerably lower and probably haven't bottomed out yet.

I once heard a very senior industry executive essentially say that as long as the big intermediary firms provided distribution, they were not going to subsidize a manager's profit margins. This is especially true when in normal times the asset management industry's collective return on equity has been higher than that of the larger intermediaries.

Finding the appropriate counter to this obvious trend, whether it is focusing more on the independent registered investment advisor (RIA) channel or perhaps dropping SMAs completely, is problematic. Many firms have already chosen to modify the course. We have seen firsthand how some large, multi-channel asset management firms have restructured all or most of their separate account specialists. These firms are not necessarily shelving separate accounts, but they appear to have changed emphasis on traditional separate accounts for now. Whether this was driven by a desire for short-term cost reductions or by strategic purposes remains to be seen. In the immediate term, this does create an opportunity for those firms that choose to differentiate themselves by concentrating on client service. Remember that separate accounts sold through the intermediaries are not going away, and there are a lot of quality people who are under-employed or on the beach right now looking for work.

Meanwhile, exploring the RIA channel is another possible strategy. If you speak to the larger management firms, many already have RIA sales teams. And equally as clear, the independent RIA channel is the fastest growing right now. Keep in mind though that this approach is even more sales- and marketing-intensive than selling to more traditional intermediaries.

Another strategy could be to sell your portfolio models to an intermediary. Although this strategy, at current prices, has much appeal, this approach does come with some risk. This strategy may ultimately prove more susceptible to predatory price reduction than traditional separate accounts. It can force a company to compete against itself for float – especially in asset-constrained disciplines. And some could argue that it may create some brand risk.

Overall, it's probably too soon after the recent market turmoil to predict the future of industry product trends. A possibility is that many firms will keep their options open while studying the emerging approaches. However, times like these can lead to major paradigm shifts in a variety of areas, including financial service products. It is very possible that, right now, no one has a handle on the best approach for the new era.

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