

STRUCTURED INVESTMENTS

À la carte fine dining or 'Big Macs'?

Christopher Taylor explains the need to differentiate between 'structured products', which can just be sales and marketing driven, and 'structured investments', developed by research-backed investment thinking

Structured investments add an important dimension in the investment arena, providing wealth managers with compelling compliments or alternatives to traditional investment funds and other investment products.

Growth in the market has been cyclical at certain points over the years, but support has trended upwards over time, dramatically at times. The UK has recently lagged other global markets in its use of structured investments – partly due to distribution factors, ie the UK investment market is dominated by fragmented firms of wealth managers, as opposed to a small number of major institutions.

However, even in the UK, the main target market for Blue Sky Asset Management (BSAM), retail structured investment sales increased by nearly 25 per cent in 2008, resulting in record sales volume just shy of £10bn (€10.63bn), with nearly 100 providers issuing nearly 1000 retail products see (Figure 1).

Against other investment options, including traditional mutual funds, sales growth and volume of this magnitude makes it irrefutably clear that structured products have established themselves as mainstream and value adding investment solutions, that appeal to and are embraced by an ever increasing number of highly opinionated UK wealth managers and advisers.

The diversity of offerings and flexibility to add value in so many



Christopher Taylor

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ways in portfolios makes structured investments indispensable in the eyes of many leading wealth managers.

However, and exactly as is the case with traditional mutual funds, naturally our view of the industry is that it polarises in terms of different investment approaches and at a provider, product and

value level. Sales volume on its own certainly does not automatically reflect investment value or integrity per se, across the board.

We think wealth managers must demonstrate working knowledge, research, due diligence and differentiation, at provider and product level if they are to tap into the structured investment firms and propositions that can maximise investment and client value.

Wealth managers who are assessing and researching the industry, providers and products, need to consider factors that differentiate the different investment approaches on offer. In particular, as the sector booms, they need to think about the hallmarks that characterise different providers and propositions.

“STRUCTURED PRODUCTS” OR “STRUCTURED INVESTMENTS”?

The first hallmark is, to our minds, the most obvious – but also the most fundamental. At its most basic, are providers talking ‘products’ or ‘investments’?

The fact is, unfortunately to our minds, that most structured product providers, at least those active in the UK, can be characterised as simply marketing products. In fact, the clue is in the terminology – they promote ‘structured products’ not ‘structured investments’.

It takes all types of providers to make any investment universe function, but typical structured

product providers are culturally and fundamentally sales driven, with products pitched on headline rates, and little else.

Talk with a typical provider, look at their business or pull open their product literature and you will presumably be able to find out 'what' products they have and 'what' their products do, but ask 'why' or 'why a product makes investment sense', from a research based, asset allocation driven, portfolio planning perspective and the conversation may dry up rapidly.

Many structured product providers offer nothing more than 'trigger happy product issuance' – but try to have an intelligent conversation about investment outlook and silence may quickly replace sales patter.

RESEARCH-BACKED INVESTMENT THINKING

The second 'hallmark' is critical and identifies or defines a structured investment provider, or structured asset manager – an altogether rarer breed, in an otherwise product driven universe. The hallmark is 'research-backed investment thinking'.

Optimal investment solutions of any type surely require intelligent investment thinking – and, to our minds, this means research-backed investment thinking. Yet, one of the fundamental differences between mutual funds and structured products is all too obvious. There is an almost total lack of research-backed investment thinking - or even basic investment thinking - within the structured products industry.

Scratch the surface of a typical structured product provider or product and the lack of research-backed investment thinking will probably be immediately apparent. There simply might not be any.

Research can embed investment views in structured investments and give them a purpose and raison d'être, other than sales. A structured investment provider's first consideration will be identifying compelling investment opportunities - and working with wealth managers to identify and solve portfolio planning/asset allocation needs. A structured product provider will identify cheap derivatives, and then try to find an investment story to wrap around them.

This, to our minds, is the way and reason that many of the structured products coming out of London, Paris, New York, etc, are developed – and is why many structured products look so spurious to wealth managers looking for the investment rationale.

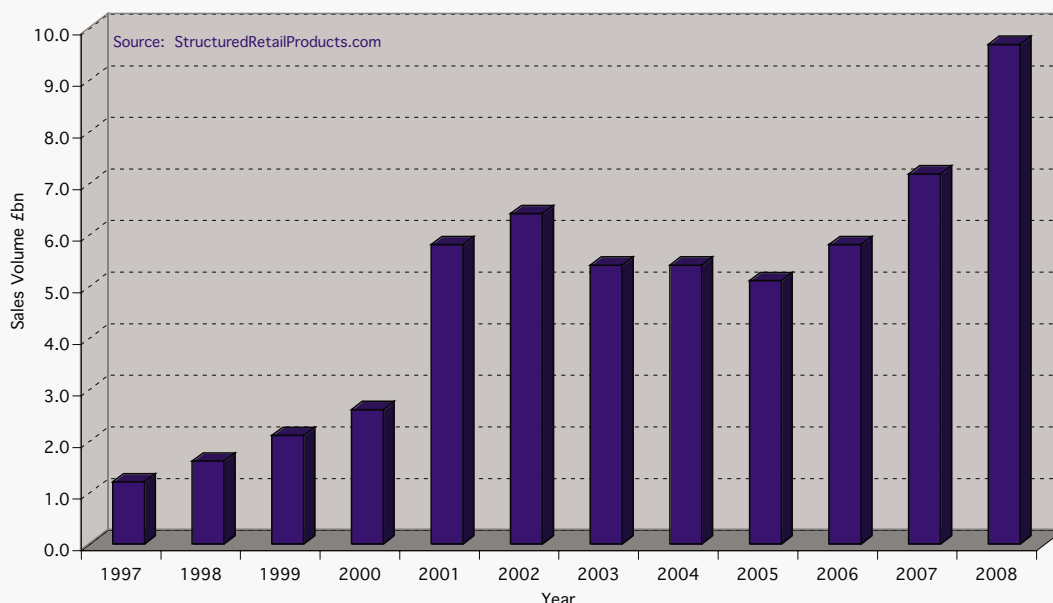
At BSAM, we put research-backed investment thinking at the heart of what we do, in fact in front of everything that we do. We do so with an independent and proprietary research function in place – in our case via a specialist strategic research partner.

Research informs all of our investment thinking and shapes our investment propositions. But this is unusual. In fact, it is fundamentally different.

Structuring, to us, is actually secondary – in fact we do not even consider ourselves a structured product provider, although we do, clearly, use structuring. However, we use structuring, ie derivatives, to optimise the risk and return profile, of our identified investment strategies, to position/capture the investment view that we are targeting.

As should be clear, we think this

Figure 1: UK Retail Structured Product Sales Volume (£bn)



point is a key differentiator and pivotal in deciding what type of investment or product provider wealth managers are dealing with.

Intelligent structured investments should be developed based upon research-backed investment thinking, with the aim of opening up and optimising investment opportunities for investors, as opposed to easy structured products, based on headline rates and cheap derivatives, designed to maximise 'one size fits all' sales for providers.

THE IRONY OF RESEARCH CAPABILITIES

The irony of research capabilities in the structured investment industry seems to us to be that those that have them, the big brand institutions, do the least with them, and those that need them, the independent asset managers, do not have them.

As explained, many major providers place no emphasis whatsoever upon investment rationale – as is clear from their product literature. Investors are not credited with thinking about investment drivers. Conversely, some providers, who want to be associated with the idea of research-backed investments, make attempts to put some investment content on their brochure pages.

But, look closely, the data or charts will usually be sourced to the underlying counterparty investment bank which has provided the assets for the product. Piecing together research post

trading structured products, based on borrowed, out of date, research, is little more than dressing up sales and marketing messages.

TRUSTED PROVIDERS AND CLIENT CENTRIC PARTNERS.

For wealth management firms and individual advisers looking for solutions to the prevailing economic conditions and investment challenges – which, presumably means all wealth management firms and advisers - structured investments provide unparalleled scope to find value adding investment propositions for investors.

“THE IRONY IS THAT THOSE THAT HAVE RESEARCH CAPABILITIES, THE BIG BRAND INSTITUTIONS, DO THE LEAST WITH THEM”

Importantly, bespoke and exclusive plans can be also be tailored (forgive the pun) to develop investment propositions that meet precise individual wealth management views and client needs.

Bespoke and exclusive plans give wealth managers greater knowledge, understanding, input and control over what they are investing in or offering clients, through working with a 'trusted

provider/partner'. But, clearly, wealth managers must look for providers who have the pre-requisite capabilities to offer an 'à la carte approach' – and who are also culturally consultative and collaborative in their business approach and ethos.

Working closely with a trusted provider can add real client - and commercial - value, as opposed to simply plucking standard options off the industry shelf.

Input into aspects and areas over and above just the overt investment proposition is also possible, for instance with regard to the basis of fees/commissions and counterparty due diligence and selection.

This latter point is, of course, pivotal and key to many wealth managers at this time – though the benefits at a counterparty level are only available through working with an independent provider, ie not a bank or issuer directly.

As we enter 2009 the economic and investment backdrop has clearly never been more challenging. Structured investments are an unrivalled sector in terms of being able to provide responsive, innovative and compelling investment solutions.

But, wealth managers and investors must check the hallmarks of the different providers they deal with to ensure they do enjoy fine dining and à la carte capability and choice, not processed, commoditised 'Big Macs'.

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Blue Sky
ASSET MANAGEMENT
OPTIMAL INVESTMENT SOLUTIONS

Blue Sky Asset Management (BSAM) is an award winning UK based boutique investment firm specialising in research backed structured investments for retail and institutional investors. The firm was established in 2007 by a team of directors with industry leading experience, gained through senior positions held in major banking and global asset management institutions, at the forefront of the structured investment industry. Industry awards gained by BSAM in 2008 include 'Best in UK' and 'Best Research Process' and, notably, the firm is recognised for its emphasis in championing structured investments based upon investment quality, not sales quantity. Blue Sky Asset Management works closely in collaboration with leading global investment banks and institutions to design and develop innovative structured investment solutions. www.bluesky-am.com