Changing landscape of unit trust industry

By Wade Witbooi

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The landscape of the retail unit trust industry has changed quite markedly since its humble beginnings in the 1960s. The expansion of the industry has been quite robust, from offering two funds in 1965, to 107 funds in 1996, and more recently investors have approximately 1000 unit trust funds from which to select.

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Along with the increased number of funds and management companies, has arisen a plethora of investment strategies to suit varying investor needs and risk profiles. As the landscape has evolved, investors have continually taken note of the new industry offerings and role players by migrating to various investment funds and strategies over time. At the end of the day it seems that investors have voted with their feet. Let's have a glance at the industry to see where their footsteps have led.

Robust growth

The unit trust industry has shown robust growth over the past number of years with average q/q growth figures (greater than that of market movements) over the same period at 4% q/q. Industry net flows and assets under management (AUM) data have been a great indicator of investor behaviour over the years. By analysing this data we are able to identify how investors are changing their views on different asset classes, investment houses and funds within the industry.

As at the end of the second quarter of 2013, Multi Asset funds (formerly known as Asset Allocation funds) have dominated market share, controlling 45% of the industry's AUM. Somewhat surprisingly, interest bearing - money market funds are the second biggest category within the industry, accounting for 18% of AUM, with equity funds following closely behind, controlling 17%.

With the newly established ASISA fund classification system promulgated on 1 January 2013, a large portion of assets previously classified as "fixed interest varied specialist" were re-classified as "multi asset income" portfolios and this has further added to multi asset fund dominance in the industry. Even with the exclusion of those assets, multi asset funds have continually shown strong growth on a quarterly basis, comfortably dominating inflows into the industry. Investors are clearly favouring the multi asset approach, allowing the portfolio manager the scope to apply their investment view and diversify across asset classes and various geographical regions.

Low equity and high equity

Within the multi asset category, two sub-categories stand out in terms of attracting flows, namely: "low equity" and "high equity." Low equity funds may have a maximum equity exposure of 40% and cater primarily to cautious investors, whereas high equity funds are allowed a maximum equity exposure of 75% catering to moderate and moderately aggressive investors. In recent times we have discovered that investors are more in favour of high equity funds (commonly known as "balanced" funds) as opposed to equity funds due to their ability to combine different asset classes and ability to increase risky asset exposure as the manager sees fit. When evaluating quantitative measures, this approach has borne fruit over the last five years. The category average of the high equity sector has returned 9.3% p.a. compared to 8.5% p.a. returned by the FTSE/JSE All Share Index over the same period. In addition, this performance was achieved at lower levels of volatility when compared to the All Share Index. When considering these quantitative measures it becomes easier to understand why investors have been favouring these portfolios and why flows into pure equity funds have been declining.

Upon analysis of outflow data during the second quarter of 2013 we have observed that of the 10 funds to experience the largest outflows, six were general equity funds. Similarly on the inflows side, six of the 10 largest gainers over the quarter were multi asset funds. This data once again indicates that investors seem to be favouring multi asset funds above general equity portfolios.

Upon analysis of the AUM of the high equity category, a strong concentration is prevalent as the four largest funds in the sector account for approximately 60% of the total AUM. The Allan Gray Balanced Fund (currently R75bn) accounts for more than a quarter of the category's AUM and is the biggest fund in the unit trust industry. As a matter of interest, the fund is larger than the market cap of Woolworths (JSE: WHL). The remaining three largest funds are managed by Coronation, Investec and Foord respectively. Market share within the low equity category is similarly as concentrated, with the five biggest funds in terms of AUM accounting for more than 50% of the category's assets. Asset managers with the largest market share include Allan Gray, Coronation, Absa, Nedgroup and Prudential.

Asset management houses have become aware of the ever increasing investor appetite for high equity funds. The number of funds within the category has nearly doubled over the last five years and this trend also spills over into the low equity category.

Worldwide - multi asset - flexible category

A category which has recently attracted strong inflows is the worldwide - multi asset - flexible category. Net inflows into these fully flexible portfolios increased strongly by 49% q/q during the second quarter of 2013. This recent influx could be attributed to the outstanding performance generated by these portfolios (category average of 28%) over the one year period to 30 June 2013. Another consideration which could explain the influx is more demand from investors seeking investment vehicles without constraints per asset class or region.

The landscape of the unit trust industry is further evolving with the establishment of smaller boutique asset managers having become more prevalent in recent times. These boutique houses have generally been established by senior investment professionals previously at large investment firms who have decided to start up their own specialised investment offering. These houses generally have smaller, but highly experienced investment teams focussing on their core competencies.

The evolution of technology has made the world a much smaller place. Through social networks the views of your favourite market commentators, strategists, news agencies, and even portfolio managers are freely available on a daily basis. The ease of accessing investment information has created smarter investors who don't just want to invest, but want to apply their own flair into their investment choices. With investors being more savvy, the importance of sound financial advice is increasingly important to align investor demands and objectives with realistic outcomes.

The unit trust industry has definitely proved to be dynamic over the years, and going forward it is likely to remain that way.

Not only are asset management houses becoming more aware of client trends, but clients are becoming more aware of their investment choices. As investors continue to vote with their feet, it is important to ensure that their footsteps continue to be directed towards their desired long term investment destination.

Source: UBS Investment Research, Sanlam Multi Manager International, the Association of Savings and Investments South Africa

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