

OPINION: The dos and don'ts of offshore manager due diligence

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BY **STEPHEN HAGAN**

As wealth continues to transition from Latin American domiciles into the US offshore market, asset managers and allocators alike are maneuvering to capture as much of the opportunity as possible. However, finding the right vehicle for the end investor is not easy, and there are several elements to consider related to product, process and risk. 1 | 3

According to international funds platform Euroclear, there are over 450,000 retail investment vehicles available to the international investment community. With that kind of choice, finding the right fit can be like trying to find a needle in the haystack.

In addition, Latin America allocators are also tasked with a specific mandate due to the uniqueness of their clients as most of their business is offshore. A client might eventually take up residence in the US, but the truth is that the right investment vehicle would be able to straddle the onshore/offshore divide to cater to the family's generational needs.

The investment products, and platforms through which they are available, are very US-centric. The result is a cumbersome experience for the investor and a missed opportunity for the Latin America allocator.

The challenge of navigating the vast number of investment solutions and the requirements of Latin American investors are the key drivers behind the need for an extensive and thoughtful due diligence process.

Manager due diligence principles

When it comes to developing a process for manager due diligence, I suggest allocators focus on answering four key questions:

1. Why am I looking for a new strategy?

Whether you're looking to replace, add or fill in a gap, focus on strategies that support onshore/offshore advisors and clients. Look for opportunities to differentiate across asset class and style.

2. What are the selection criteria?

Clearly define the metrics and benchmarks you will use to identify new managers. Be careful not to select data points lesser-known managers might not make available. When considering thematic-type strategies, like ESG, be sure to use consistent measurements across the different markets.

3. How will I find the strategy?

Identify the channels through which you will access the strategy (transactional and/or distribution platforms) and take the time to understand the legal nuances of dealer agreements.

4. How do I make a final decision?

Take the time to understand the manager on a qualitative level. Make sure ongoing product education and support are available to both advisors and investors.

Answering these key questions is the foundation for developing and evolving an effective due diligence process, but I believe it is equally important to acknowledge the risks associated with finding the right strategy.

In my view, the five biggest risks for manager due diligence are:

- Lack of platform understanding
- Incorrect share class (price)

- Mismatch with investment window
- Domicile of fund vs. manager
- Appropriate for a US investor

Beyond finding the right manager(s), it's important for allocators to choose the right product for their onshore and offshore investors. Ucits and mutual funds have traditionally been the vehicles used for non-US and US-domiciled investors, respectively. However, there can be some hurdles to overcome when trying to invest in them.

The US, for instance, has certain standards when it comes to approved investment vehicles, while the due diligence for Ucits requires researching both Luxembourg and Irish-domiciled fund companies.

If an allocator is seeking differentiation through a boutique manager or thematic-based fund, it can often be difficult to collect all the necessary data on the manager, and the fund's theme – take ESG for example – might not be appropriate for all investors.

Although mutual funds and Ucits will continue to be a core offering to investors, there is another vehicle garnering more attention in the wealth management marketplace: separately managed accounts (SMAs).

More and more asset managers and allocators are trying to turn to SMAs because they offer the end investor opportunities for customization of and transparency into their investment portfolio. The technology platforms that offer them have also improved dramatically over the years which can help all parties reduce their costs of doing business.

However, SMAs still have some work to do in global markets, especially when it comes to catering to offshore client requirements, growing the number of international strategies available and satisfying the regulatory requirements of various domiciles.

We are still in the early innings of this cross-border transformation for the wealth management industry. But I'm confident all parties involved will create solutions and processes that meet the needs of this dynamic investor.

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