

## Making difficult decisions more effectively: asset management options

So, you are ready to make your choice of service provider. You've decided how much to put away in savings every month and you know what type of collective investment scheme (CIS, also called a unit trust) you want. You've done your homework on their past performance. You've pulled out and studied their information sheets. But how do you know if the fees that they are asking represent fair value for money?

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It doesn't matter whether you're an individual saving a few hundred or a pension fund trustee representing several billion. It helps to ask a few questions that your service provider probably doesn't want you to ask.

### Information inequity

These questions aim to overcome a ubiquitous problem in financial markets called information inequity. The financial giant that you are considering contracting with typically knows a great deal more about the service that they offer than you do. This is exacerbated by the fact that this is not like a repeat-purchase condiment at your local convenience store, which you can take back if it smells bad when you open it. The financial service is intangible. Its outcome will only be known a long time into the future, with little prospect for recourse. You may not even know at that stage whether they have done a good job or not.

Asking yourself and (if you have one) your financial adviser a few questions about that service before you start should help overcome some of this inequity.

### What is the service being offered?

A unit trust is a bundle of shares in which you have fractional ownership. The unit trust manager chooses these shares on your behalf. All going well, the value of the shares rises over time and, when you are ready to turn your savings into tangible benefit, your return shows that you made a good decision, even though you had to pay fees for the service offered. (Systematic saving is nearly always a good decision, incidentally.)

The manager is offering to create this vehicle, buy and sell shares intelligently and administer the operational infrastructure within a sound governance framework. That description does not make for good marketing. What you are more likely to hear is that saving today will make you rich tomorrow or that the manager has done such a great job of winning performance awards in the past that you can trust him for a repeat in future.

What you are really buying is intelligent decisions and a sound operational framework. You trust it because you

are in no position to deliver it yourself at similar levels of cost effectiveness.

### Is performance guaranteed?

Performance is implied. It is never guaranteed. Avoid being seduced by that implication. Yesterday's performance depended on thousands of yesterday's decisions. If that bundle of shares had been sold an hour later than it was, it would have been badly impacted by the presidential decision to send several missiles into a middle eastern compound in a certain capital city.

When your asset manager wins an award for performing better than her peers, you assume that this is attributable to skill, partly because she wants you to assume this. Some of that performance may indeed be down to better information or better decision-making, but you are not able to distinguish luck from skill, so do not assume that this performance is repeatable.

This unit trust fund beat the market five years running, you say. Still not necessarily skill. How many funds are available on the market? Even if performance were entirely random, one in 32 would be expected to deliver outperformance five years running. And those that didn't? Many of them are probably no longer open to new customers because they are unattractive.

### Do how do I determine a fair price?

All well and good, but is the fee being charged fair for the service being offered, even if I cannot believe the implication of untold wealth? In truth, you don't know, but you can be careful. Do not assume that a fee is fair...

- because it sounds low... *1.0-1.5% of my assets a year is little.*
- because it is comparable to the market... *everybody seems to charge the same.*
- because a portion is paid only if the manager delivers good performance... *Do they also give you a portion of your fees back if they perform poorly?*

The best way to overcome the information inequity is to raise your game. Shop around. Think. Read the print.

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If you are making your own saving decisions, then the consequences of choosing the wrong manager could be significant, but they probably won't be. If you are a fund trustee, however, then you must do your homework very carefully, because your members are depending on your shrewd research and decision-making. **Rob Rusconi**