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Discretionary versus Non-Discretionary Management

Given market volatility, it is important for individuals to understand whether or not their financial adviser has the ability to limit drawdowns in a portfolio or to take advantage of market opportunities by repositioning assets. This typically depends on whether the adviser has discretionary or non-discretionary management authority.

In Discretionary investment management, the accountholder authorizes a portfolio manager to make buy-and-sell decisions without referring to the accountholder. These decisions must, however, be made within agreed upon limits. The client’s investment policy statement governs the adviser’s ability to act defensively or opportunistically. For example, if the policy statement does not permit hedging, the portfolio manager cannot use hedging in an attempt to limit losses or achieve gains.

Under Non-Discretionary investment management services, the investment adviser can merely advise the client what may be good or bad for the portfolio. The client reserves full right to take his own decisions. While this gives the client the greatest control over his or her investments, it also places the responsibility for protecting a portfolio in market downturns squarely in the client’s hands. Unless the adviser is authorized by the client, a more defensive or aggressive investment position cannot be taken.

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