TOP STRATEGIC INITIATIVES TO FIGHT COMMODITIZATION IN THE EUROPEAN ASSET MANAGEMENT INDUSTRY
INTRODUCTION

Between 2005 and today, total assets under management (AUM) have doubled, reaching more than US$80 trillion worldwide. Over the next decade, the asset management (AM) industry is expected to grow by between five and six percent each year. All in all, the industry seems to be in pretty good shape—good enough deliver strong financial returns and recurring average operating margins in the range of 30 to 40 percent. So, what should the industry be worrying about?

In the European market, only a few mature industries are capable of delivering similar margin ratios, relying on a set of strong and distinctive features to sustain their long-term growth. The luxury industry, for example, appeals to people’s dreams, aspirations and desires with recognizable brands and premium goods. Unfortunately, the European AM industry does not have the same levers and assets at its disposal.

With over 4,000 companies and close to 60,000 funds across Europe, AM is increasingly considered a commodity market. Accenture data show that revenue and cost pressures have grown in the past two or three years. Today, most market participants find themselves caught between large AM companies, which are gathering the lion’s share of institutional net new cash, and fintechs, which are disrupting the profitable mutual fund industry. In this point of view, Accenture suggests seven strategic initiatives that AM companies should rapidly implement to sustain growth and survive in this increasingly complex environment.
FINANCIAL PRESSURES HAVE INCREASED OVER THE PAST TWO YEARS, PUSHING EUROPEAN AM COMPANIES TO ADJUST THEIR GROWTH STRATEGIES AND PLATFORMS

Accenture has identified five key endogenous market trends, all of which are exacerbating revenue and cost pressures in the European AM industry. First felt in the 2000s, these trends have gained momentum in the past few years and will have a growing impact on the industry’s future.
1 A SHARPER DECLINE IN PRICES AT INSTITUTIONAL INVESTOR AND DISTRIBUTOR LEVELS

The downward trend in prices affects management fees on both net new cash (NNC) and total AUM in the medium term, particularly when investors are reviewing their AM company selections. The pressure on financial conditions is much higher since the last two years in the institutional segments, with the lion’s share of NNC gathered through request for proposal (RFP) processes that generate a level of management fees that is often far below the average cost of an AM company (estimated at 17 to 18 basis points of total AUM).

The Italian pension fund segment is a good example of this trend. Management fees applied to mandates, excluding those for guaranteed funds, have fallen by more than 30 percent in the past 10 years. A significant share of that drop—13 percentage points—occurred in the past two years alone. In 2016, the weighted average management fee was just 9 basis points. The performance fees usually applied to these mandates were insufficient to offset the gap to the average cost in the European industry.

This trend is also visible in the wholesale fund distribution market, where total expense ratios (TERs) have decreased by approximately 25 percent for “active” products and as much as 65 percent for “passive” products over the past 15 years, the latter registering a particularly large fall in the past three years.

2 AN ACCELERATED DECLINE IN PRODUCT MIX PROFITABILITY

Over the past 15 years, the share of active funds in total European mutual funds has fallen by 12 percentage points. By contrast, increased demand for passive funds and exchange-traded funds (ETFs), which generate much lower fees, has more than tripled their share of total assets to 15 percent in the same time frame.

Interest in passive investing has accelerated in recent years in Europe, with passive NNC accounting for 22 percent of total NNC in 2014 and close to 40 percent in 2016. Compare this with the US mutual fund market, where passive assets account for 32 percent of total assets, and it’s clear that there is still plenty of room for European passive products to take market share. Combine this growth in passive investing with declining prices and the result is increased pressure on margins in the AM industry.

Mainly from 2007, AM companies have increased their focus on customization to better serve and retain their clients. In addition to products, they now sell solutions and services (e.g., target date and life-cycle solutions, smart benchmarks, enhanced focus on defined-contribution pension funds). These services generate higher revenues and also higher costs, so a continued evolution in this direction will offset only a fraction of the financial pressures facing firms.
ENHANCED COMPETITION FROM LARGE AM COMPANIES

The largest AM companies understand that AUM are key to their growth and ability to cope with challenging market conditions. By driving the industry, large AM companies contribute to the weakening of small and medium-sized firms, forcing them to become increasingly agile and innovative to remain competitive.

In that context, there has been an uptick in consolidation in recent years. Amundi and Pioneer, Henderson and Janus, and Standard Life and Aberdeen are just three examples.

Today, BlackRock and the top 10 AM companies manage 7 percent and 25 percent, respectively, of total assets worldwide.

Each year for the past 7 years, close to 40 percent of total NNC in Europe has been gathered by just 10 AM companies, usually the largest ones. Because growth seems to be a successful strategy and because capital market conditions are expected to worsen, Accenture believes that the battle for size will only intensify in the future.

GROWING COMPETITION IN RETAIL DISTRIBUTION FROM NEW ENTRENTERS WITH INDUSTRY-DISRUPTING TECHNOLOGIES

These new “disruptors”, particularly fintech companies, either target specific points in the AM value chain with innovative solutions and new technologies (e.g., big data, artificial intelligence, blockchain, natural-language generation) or target the entire value chain by acting as an AM company.

Those that have chosen the latter approach currently have an estimated US$300 billion in AUM worldwide and are expected to significantly increase their market share to US$16 trillion in AUM by the year 2025. They will increasingly be competing with established firms, mainly in the fund distribution industry. AM companies currently generate healthy profit margins in this area, but they should expect growing pricing pressure from fintech and be prepared for the possibility of a new wave of disruption from recognized brand names using their strong analytics capabilities to create a competitive edge.

“As a result of the emergence of new technologies, the asset management industry needs to follow suit through the modernization of its systems and processes. A host of new initiatives and flourishing start-ups are constantly rethinking the development of our industry. This is evidence of a highly innovative universe, with strong entrepreneurial minds, that will ensure our trade constantly reinvents itself.”

Naïm Abou-Jaoudé
CEO, Candriam
Chairman, New York Life Investment Management International
The AM industry has been more affected by regulatory constraints since the 2007 crisis than ever before. The proliferation of regulation has accelerated in the past two years, with new requirements that touch all components of the value chain (e.g., Solvency II, EMIR, MAD II/MAR, AML IV, MiFID II, PRIIPs, IDD). This regulatory environment, which provides greater investor protection and reduces risk within the financial system, also increases the AM industry’s costs by approximately 8 percent, or between 1 and 1.5 basis points of total AUM\(^2\). At the same time, these regulations make the total cost of investing clearer to end clients, putting more pressure on pricing.

Market participants need to be increasingly proactive and agile, using the leeway they still have to address these five market trends, or risk being so weakened that they lose control of their own destiny. Those that anticipate change will have a real competitive edge in the industry.
THE TOP SEVEN STRATEGIC INITIATIVES

Accenture has identified seven key initiatives with concrete use cases that can help AM companies generate growth in the long term, keep financial conditions at significant levels and fight commoditization. Most of these initiatives have moved from concept to reality over the past two to three years, highlighting the need for AM companies to better manage their growth, capitalize on opportunities, and welcome new market participants and technologies to the industry.
For decades, the value of brand management has gone recognized in AM, leading to undifferentiated value propositions among industry players. For the most part, branding has been viewed less as a key asset and more as an unworthy cost lacking a tangible return on investment. Market studies often reveal a troubling schizophrenia in the industry, whereby AM companies consider their value propositions impactful, and investment consultants and institutional investors express reservations about their differentiation.

Accenture is convinced that being a “top-of-the-mind” brand is among the key assets required to expand your business, retain existing clients and attract new clients in the long run. Many AM companies, particularly large American players (e.g., BlackRock, Fidelity), already understand the importance of investing significantly in branding. Brand strategy goes beyond a logo or motto to capture and convey a firm’s DNA in a consistent way across the entire investor experience—from websites and social media, to marketing materials and events. Raising brand awareness is how AM companies can mature into sustainable, “all-weather” firms with long-term growth potential.

**USE CASE**

Accenture worked jointly with a medium-sized AM company to enhance its brand impact on social media vis-à-vis its peers. Using an innovative marketing tool, Accenture helped the company target specific client segments through key influencers. Through this project, the company was able to redirect its communication strategy toward clients and better share its value proposition. As the top digital agency worldwide, Accenture increasingly works on branding enhancement in various industries.
Focus on high-potential client segments that align with the company’s DNA and expertise.

Build or update the company’s products, solutions, services and pricing policies to better address client needs.

Build a roadmap by segment and country (i.e., prospects/clients, NNC, revenues, costs, profitability).

Build and monitor a flexible organization that adapts the company’s sales, marketing and communications to selected client segments.

One concrete way to select client segments that align with the AM company’s capabilities is to combine “top-down” and “bottom-up” approaches. A top-down approach, which is often carried out by entities in charge of competitive watch (i.e., market intelligence, market research, marketing strategy), looks at client segments in a given country, identifying existing and future high-potential segments using quantitative measures (e.g., macroeconomic indicators, addressable assets) and qualitative information (e.g., regulatory changes, level of open architecture, expected products and solutions). A bottom-up approach selects which client segments to target based on the AM company’s core values, given country.

Marketing strategies are most successful when they align with branding strategies, are fueled with analytics, and monitored using accounting frameworks that produce detailed profitability analysis by client, country, product and asset class.

## 3 TAKE ADVANTAGE OF FINTECH AND OTHER NEW ENTRANTS TO THE AM ECOSYSTEM

Since the 2007 crisis, fintech has developed exponentially in the AM arena and new players have become key market participants. Between 2010 and 2016, the AM industry’s investment in fintech grew from US$0.4 billion to US$11 billion.13

Fintech companies are reshaping the AM industry, tapping into all aspects of the value chain and largely contributing to the “des-sophistication” of the business. Early on, robo-advisors flooded the market. Since then, a myriad of new fintech and new services have emerged, including Nutmeg (an online investment management company), Invstr (a smartphone app for AM) and SESAMm (a stock market forecasting tool that uses big data and natural-language processing). Fintech has the potential to weaken the traditional positioning of AM companies, but also enhance their value propositions and push them to open to their ecosystem. Consequently, industry players need to revisit their business models and adopt responsive digital strategies to deal with these new entrants.

AM companies can use various strategies in this disrupted environment. A company may choose to enhance its digital culture by integrating data scientists and digital experts from other industries, or engaging in joint research with universities. It might partner with a fintech company to benefit from a specific area of value chain expertise (e.g., UBS and SigFig, BlackRock and Youvestor). Or it could acquire a fintech company to gain exclusive rights to cutting-edge technology (e.g., Fidelity and eMoney Advisor, Amundi and WeSave). Sometimes, companies combine these strategies to enhance innovation and agility, ultimately delivering higher value-added services to their clients.

### USE CASE

Pension funds in southern Europe can show both top-down and bottom-up approaches in action. In Spain, the historical high replacement rate coming from the first pension pillar is not sustainable in the long term due to weak public finance conditions, leading to an acceleration in pension fund development. In Italy, the growing share of the labor force covered by a second-pillar pension system, the high level of open architecture to foreign AM companies, and the regular turnover in asset allocation, which offers opportunities to new entrants, make the pension fund segment increasingly attractive, with AUM already amounting to €150 billion.
New technologies are spreading rapidly and becoming unavoidable in the financial services sector. To deliver revenue growth, added value and client service, AM companies will need to leverage new technologies, including robotic process automation (RPA), information architecture, big data, natural-language generation and blockchain, across the value chain. Strong data management and governance will be critical for making the most of these technologies.

New technologies should be viewed as opportunities for growth, rather than potential threats. Beyond cost-cutting, these technologies can help AM companies revisit their business models and improve overall performance. In the front office, they will make it possible to build additional engines in quantitative investment processes, enhance research in the high-yield spectrum and on sustainable and responsible investments (SRI), and generate alerts on day-to-day activities. In the middle office, they can enhance data quality management, corporate actions management and client reporting. In the back office, technologies such as blockchain are being used to reduce market costs and better understand the liability side of the AM business.

**USE CASE:**

Accenture has teamed up with several banking groups to launch Digital Factories, which aims to generate co-innovation and collaboration via incubation programs, research and product development. The initiative, which is currently being extended to the AM industry, combines Accenture’s innovation capabilities with expertise in banking, and explores the potential integration of additional partners in fintech.

"We have observed major transformations in the Asset Management industry over the last few years, with an increased focus on new technologies both bringing additional value and limiting costs. SESAMm has helped major funds and assets managers worldwide integrate Big Data and Natural Language Processing into their Front Office investment process with analytics and investment signals. Interestingly, while the US market started seizing these opportunities several years ago, the European market is now moving very quickly in the same direction with the advantage of not having to reproduce existing research results, to better focus on mature solutions."

**From Sylvain Forté** | CEO of SESAMm
FinTech Startup

**USE CASE:**

Accenture has supported a large AM company by providing value-added services to its distributors. For example, Accenture built customized and decisional digital reporting to clients of investment financial advisors (IFAs), including sophisticated and differentiated key performance indicators. This project enabled the AM company to attract and retain IFAs, generating additional NNC from clients.
While cost reduction has been the primary motivation for RPA programs in the financial services sector, Accenture believes that this technology can also generate new opportunities and scale up an organization’s capacity to perform key processes.

Many banks have announced significant cost-reduction plans, mentioning RPA as a key lever in the achievement of these programs. Indeed, RPA programs can reduce processing costs, increase productivity (with the potential for 24/7 operations), absorb activity peaks, limit human error and guarantee full compliance traceability. Based on previous experience, Accenture estimates that RPA could reduce middle-office costs by as much as 25 percent in the AM industry.

In many cases, RPA can also be used to scale a business or even enhance a company’s competitive edge. When it comes to automating the proxy-voting process—process optimization gains aside—RPA makes it possible to multiply by three to four the number of general assemblies that AM companies can follow with staff numbers unchanged. By increasing voting decisions, companies can also enhance their external communication as responsible investors.

Accenture believes that the new RPA 2.0 wave, which combines RPA and artificial intelligence (i.e., technologies that gain knowledge from data and learn from experience), will generate numerous additional opportunities across the AM industry’s value chain. First, RPA 2.0 will bring completeness to automated processes, enabling automation where human intervention was previously required. It will make it possible to fully streamline the proxy-voting process, automating any remaining voting instructions that RPA alone is not able to complete. Second, RPA 2.0 will become a key ally in day-to-day investment decisions. Accenture has already spotted several use cases, including the identification of new investment opportunities and the use of new engines in quantitative investment processes.

**USE CASE**

One example of RPA 2.0 is the automation of investment comments production in fund reports, including translation in several languages.

Another example is the re-engineering of internal credit rating processes through a mix of deep learning and natural-language processing. When combined with RPA, these technologies make it possible to automatically build internal ratings on many vanilla bonds and focus research on value-added analysis (e.g., cross-over and high-yield analysis).
AM companies usually have various databases along the front-to-back value chain, inherited from a long history of IT evolution and “shadow” IT practices in the front office. On top of this legacy cost, an increased focus on data management, regulatory pressure and the need to generate alpha from analytics naturally result in increased data storage and infrastructure costs. In addition, the relationship with the ecosystem of financial institutions is increasingly complex and requires greater intelligence in business to obtain a competitive advantage. By enabling a large volume of data to be processed in real time and providing relatively cheap storage, big data is naturally seen as an attractive option.

Although big-data technology is always identified as an enabler for new front-office analytics use cases, it’s rarely viewed as an opportunity to rationalize and optimize AM data architecture. Accenture sees opportunities on a number of AM company projects, both in terms of cost (e.g., regulatory agenda, operational efficiency) and revenue (e.g., front-office analytics, natural-language processing). These initiatives are often uncoordinated and progress in silos across business lines.

Accenture believes that they could be delivered through a centralized big-data roadmap. Here are just a few of the key use cases for a shared, multi-speed architecture using big-data technology:

**Front office:** Enable data analytics and AI initiatives (e.g., sentiment analysis, market data analysis)

**Sales:** Use non-structured information generated by clients to personalize marketing campaigns and sales actions

**Reporting:** Rethink legacy reporting and develop business unit solutions distributed through digital channels

**Operations and risks:** Improve processing with predictive analytics (e.g., break analysis, fraud detection)

**Finance and risk:** Unify information across business areas to improve regulatory responses and guarantee valuations

**Regulatory agenda:** Meet current regulatory constraints, while optimizing time to market for future regulatory changes

**USE CASE**

Accenture has developed an entire big-data backbone in a financial services firm. By using generic and reusable components to speed up data ingestion and deliver high-quality reports, Accenture was able to leverage data from across the value chain. The client gained better views of the ecosystem, resulting in faster strategic decisions across the firm’s various services.
MOVE TO A VARIABLE-COST MODEL AND ENABLE ACCESS TO THE AM ECOSYSTEM

Over the past 20 years, AM companies have progressively evolved away from fixed-cost, in-house models toward variable-cost models with significant outsourcing of back-office—and later middle-office—functions to asset servicers. This transition has forced AM companies to open their internal systems, and share more and more data to and from their production platforms.

Accenture believes that AM companies that choose to modernize and open their IT platforms now will gain a real competitive edge. The ability to share data to and from the company’s internal platform in a secure and reliable way will make it possible to take advantage of innovative externalization opportunities (e.g., outsourcing dealing desk functions). In addition, the development of standardized open application programming interfaces (APIs) and access to microservices that leverage big data or blockchain technology will enable AM companies to hop aboard the innovation train.

A notable example of what can be achieved through an open ecosystem model is the IZNES platform. Launched by SETL, a blockchain fintech, and four AM companies, this co-innovation initiative enables cost reductions across several key tasks (e.g., know your client, order management, corporate actions, reporting), while offering insights on external funds and final investors. An open ecosystem could also make it possible to:

- Access direct information from portfolio managers while visiting clients.
- Enhance interactions and better manage client expectations with differentiated digital services.
- Launch a robo-advisor by acquiring or partnering with a fintech company.
- Distribute client reports through digital channels.

Opening the ecosystem is not an easy journey for AM companies, especially when the existing environment and infrastructure have yet to be modernized. Accenture believes that implementation of an open AM model needs to be clearly identified as a strategic long-term objective on the industry’s agenda. Achieving this objective will require complex transformation and increased agility. Companies will need to modernize legacy infrastructure, move functions to the cloud, tackle key security concerns, enhance data storage and access, develop robust and open APIs and microservices, and invest in development operations activities to reduce time to market.

USE CASE
The development of future open AM digital platforms will enable portfolio management sharing with major clients on a quasi-real-time basis, responding to the growing need to open the ecosystem. This trend will also help put clients and market participants increasingly at the heart of AM organizations. Accenture has cross-industry experience in leading clients to the cloud, resulting in significant IT cost reductions and indirect revenue generation.
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