High Performance Asset Management
Introduction

More than four years after the financial crisis of 2008, the global asset management industry remains in transition.

While total Assets Under Management (AUM) have recovered from the lows experienced shortly after the financial crisis, industry profitability has not rebounded to the same extent. Industry profit margins, in fact, are well below pre-crisis levels, with headcount reductions and operating model changes partially offsetting declines in fee revenue.

The growth of passive and alternative investments places significant pressure on “middle of the pack” long-only fund managers to develop differentiated strategies and operating models. Similarly, customers’ expectations for a better overall experience have pushed fund managers to develop a tailored approach to client engagement. Some managers are now able to deliver trusted advice along with customized solutions across multiple platforms, including mobile devices and social media.

The consolidation of major distributors and the proliferation of open architecture and/or self-service options increase the pressure on the “manufacturers” of investment products to demonstrate differentiated, high-performance investment management. Meanwhile, leading asset managers are applying new technologies such as Cloud/SaaS, Big Data, analytics, and mobile and social applications to gain competitive advantages in sales and cost efficiency. And, in the face of proliferating regulations, asset managers must adjust their product strategies and operating models to maintain and ultimately increase profitability despite requirements for greater price transparency and lower leverage as well as higher compliance costs.

Indeed, asset managers face challenges on many fronts, ranging from demographics to regulation to macroeconomics and technology. (See sidebar). These converging and interconnected trends are forcing asset managers to re-think their basic business models and adapt quickly or lose share to more flexible and innovative competitors.

Despite these pressures, some asset managers have still managed to achieve high levels of performance since 2008. To explore how these firms accomplished this—and to help identify potential paths to high performance for other asset management firms in the future—Accenture analyzed the competitive landscape of the asset management industry, measuring firms by growth, profitability, productivity and other indices. We used both quantitative and qualitative analysis as well as our own experience and knowledge of the industry to identify five distinct business models used by high performance asset managers.
A World of Challenges

Asset managers are operating in a world that is very different from the one that existed before 2008. Among the challenges that asset managers must confront:

**Demographics**
A global contingent of “baby boomers” is not only entering retirement but will transfer unprecedented amounts of wealth to younger generations. These younger generations, however, may not be comfortable with traditional asset management models. At the same time, improved economic opportunities in emerging markets are creating new middle and upper classes and new opportunities for asset managers.

**Politics**
The stability of the Eurozone remains in question, as poorer countries grapple with austerity measures, high levels of unemployment and low or negative economic growth. The polarization of U.S. politics makes it difficult to establish a clear economic path, while continuing political turmoil in the Middle East contributes to overall uncertainty. The rise of China and India as potential economic superpowers creates significant issues for other countries in the Asia-Pacific region.

**Macroeconomics**
Slow GDP growth has become the norm in many countries, accompanied by extraordinarily low interest rates. Fixed-income asset managers seeking acceptable returns are facing major headwinds.

**Regulation**
While banks were in the media and political spotlight asset managers suffered considerably both from investments in complex (and, in many cases, poorly understood) assets and from loss of investor confidence. Regulators seeking to protect investors are imposing new requirements for capital adequacy, for fiduciary responsibility, and for greater transparency regarding the pricing and suitability of products sold to investors.

**Technology**
The introduction of innovative technologies ranging from cloud computing and Software as a Service (SaaS) to improved data management and business intelligence puts new tools at asset managers’ disposal. The rapid evolution of mobile and social media technologies, however, creates new customer expectations and demands for improved service and better communications.

**Distribution**
Consolidation of the brokerage industries, in some major countries, narrows an important distribution channel, increasing the importance of independent advisors as well as the need for adoption of direct-to-consumer products and programs, often built upon mobile platforms. In the institutional market, request for proposal (RFP) processes have become more demanding, including greater focus on risk management and regulatory compliance.

**Products and Pricing**
Consumers expect greater access to new investment products such as Exchange Traded Funds (ETFs) and alternative investments including commodities and real estate, while also demanding greater price transparency and simpler, easier-to-understand packaged products. Institutional investors have become more focused on outcomes and “solutions” including liability driven investing strategies.
The High Performance Landscape in Asset Management

To create a model for defining and discussing high performance, we examined a broad range of metrics as seen in Figure 1 related to growth, profitability, cost efficiency, productivity, investment performance and consistency.

The difference between top quartile firms and those in the lower three quartiles was significant, with top quartile firms outperforming those in the lower quartiles by an average of 14 points across all of the high performance metrics. Investment Performance and Consistency were the two areas with the most differentiated performance.

The recent period did not favor one strategy or model over another. The high performers we studied thrive by executing against a variety of business strategies and operating models—large scale, relatively small, retail, institutional, and local versus global. Firms under independent ownership led the top quartile along with a few “captive” firms operating as part of universal banks or insurance companies.

Figure 1: Performance Metrics

<table>
<thead>
<tr>
<th>Growth</th>
<th>Profitability</th>
<th>Cost Efficiency</th>
<th>Productivity</th>
<th>Investment Performance</th>
<th>Consistency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 year, 3 year CAGR AUM growth</td>
<td>1 year, 3 year Operating Margin</td>
<td>1 year, 3 year Cost/Income Ratio</td>
<td>1 year, 3 year AUM Turnover Ratio (Revenue/AUM)</td>
<td>1-3-5 year avg excess return (asset weighted)</td>
<td>5 year Median outperformance (Profitability)</td>
</tr>
<tr>
<td>1 year, 3 year CAGR Revenue growth</td>
<td>1 year, 3 year Return on Equity</td>
<td>1 year, 3 year Productivity Ratio (Revenue/Headcount)</td>
<td>1 year, 3 year AUM Turnover Ratio (Revenue/AUM)</td>
<td>1-3-5 year avg top quartile Morning Star Ranking (asset wgt)</td>
<td>5 year Median outperformance (Cost Efficiency)</td>
</tr>
<tr>
<td>1 year, 3 year Net New Money ($AUM)</td>
<td>1 year, 3 year Return on AUM (Operating Profit/AUM)</td>
<td>1 year, 3 year Productivity Ratio (Revenue/Headcount)</td>
<td>1-3-5 year avg top quartile Morning Star Ranking (asset wgt)</td>
<td>1-3-5 year avg top quartile Morning Star Ranking (fund wgt)</td>
<td>5 year Median outperformance (Productivity)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5 year Median outperformance (Growth)</td>
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Distinct Strategies and Operating Models for High Performers

While success is possible under a number of business strategies and operating models, industry forces are driving firms to choose from one of five specific operating models:

1. Global Solutions Provider

Representative Global Solutions Providers include BlackRock and Pimco. These firms excel in managing across geographic boundaries to leverage product, channel and service capabilities. They may also provide institutions with consultative and analytical services in areas such as risk management.

Requisites for success as a Global Solutions Provider (GSP) include a powerful and efficient infrastructure, consistent investment performance, advice-driven relationship management, and, often, robust merger and acquisition capability. On this foundation, GSP firms develop products and Solutions (e.g., target date funds, overlay strategies, liability-driven investing), backed by quality investment research and analytics. They also use quantitative analysis of client preferences to create strong marketing campaigns with well-managed distribution channels.

GSPs use their AUM and profitability increases to support further investments: Creating innovative products and solutions, developing talent and technology, and increasing market penetration through merger and acquisition activity. As is true with other high performance operating models, success helps create a virtuous circle whereby further investment helps reinforce their brands and adds greater differentiation to the firm’s service and product offerings.

2. Focused Alpha Factory

Focused Alpha Factories (FAF) include alternative investment managers such as Blackstone and many privately held boutique fund managers. Typically, FAFs have flat organizations, with a near-total focus on investment performance. In recent years large, publicly traded FAF’s have lagged on our High Performance measures but their sustained inflows suggest investors continue to believe in the FAF model.

In addition to a proven track record of alpha generation, the foundation elements for the FAF model are a strong brand and reputation, well-established investor and consultant relationships, and leadership by proven “investor managers”. On this basis, FAFs are able to attract asset in-flows at premium prices. They invest heavily in research and technology and their attractive economics help them recruit and retain top talent.

FAFs are usually independent from bank or insurance company holding structures, helping keep down overall compliance costs. FAFs that deliver market-leading investment performance enjoy the benefits of a growing asset base and high profitability.
3. Client Experience Champion

Client Experience Champions (CEC) such as Franklin Templeton, Schroders, Henderson and T. Rowe Price make anticipatory investments in client relationship management, retirement products/platforms and integrated multi-channel distribution, increasingly including advice, mobility and social media components. Strong capabilities in data management and analytics help provide the experience desired by both financial advisors and their clients. In the institutional market, CECs are leveraging these capabilities to provide superior client reporting and on demand analytics.

The elements upon which the CEC model is built include an existing fund business, a seasoned management team and diversified product offerings. With these elements in place, CECs invest in integrated multi-channel distribution, brand building, CRM platforms and operations. CECs are able to exploit these advantages to provide an attractive client value proposition, with customized advice, products and services at healthy margins.

4. Enterprise Value Creator

Enterprise Value Creators (EVC) leverage their corporate infrastructure while adding value to banking and insurance relationships. Leading firms using this model—such as J.P. Morgan Asset Management, Allianz/Pimco and Robeco—also succeed as standalone asset managers.

To succeed within a captive corporate structure, EVCs need leadership with “clout” within the enterprise, solid investment performance, a skilled internal sales force, and access to clients in multiple segments. Investments in expanded offerings, in building a national or global brand, and in optimizing operations, as well as in CRM systems and analytics, help EVCs cross-sell efficiently. Although EVCs face heavy compliance costs compared to independent managers, their relatively low capital requirements make them attractive businesses for the enterprise and growth of their asset bases increases the shareholder value of the enterprise.

5. Emerging Markets Leader

The Emerging Markets Leader is a relatively new high performance model. As exemplified by Banco Itau and Ping An, EMLs build on local relationships and distribution channels to capture large shares in emerging markets. They also have strong ties to local businesses and to national and regional governments in the areas they serve.

EMLs invest in technology as well as marketing, sales and distribution to bring the right products to their markets. Their well-known brands and local securities licenses often facilitate a first mover advantage in their home markets. With growing shares in growing markets, EMLs are well positioned both for asset and revenue expansion and for future margin improvements.
Adopting a High Performance Asset Management Model

As seen in Figure 3 below, each high performance asset management model has unique competitive advantages. Moving to one of these operating models, however, requires specific supporting capabilities that must be carefully and deliberately cultivated. The GSP, for example, needs integrated distribution, product breadth, strong operations and technology and a deep, highly skilled management team. Investment performance, while always important, is only one key component to the GSP model. In contrast, the FAF relies heavily upon investment performance and focuses its management capabilities on building a strong team of analysts and investment managers.

Our analysis shows that high performers in asset management succeed by developing clear, capability-based business strategies and aligning their operating model to the chosen strategy. They then "out-execute" the competition in the areas in which they have chosen to excel.

Figure 3: Competitive Advantages of High Performance Asset Management Models

<table>
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<tr>
<th>HPAM Business Models</th>
<th>Relative Importance of Cultivated Capabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Integrated Distribution</td>
</tr>
<tr>
<td>Global Solutions Provider</td>
<td>• Ability to provide institutions with a broad range of tailored solutions across asset classes, geographies and risk appetites</td>
</tr>
<tr>
<td>Focused Alpha Factory</td>
<td>• Ability to differentiate based on investment performance and consistency</td>
</tr>
<tr>
<td>Enterprise Value Creator</td>
<td>• Ability to leverage internally driven capabilities into external markets</td>
</tr>
<tr>
<td>Emerging Markets Leader</td>
<td>• Established position in emerging markets provides distribution, regulatory and operational advantages</td>
</tr>
<tr>
<td>Client Experience Champion</td>
<td>• Leading position and expertise across multiple sales and service channels</td>
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</tbody>
</table>
Building an Asset Management Strategy

The operating models we have explored in this paper are descriptive, not prescriptive. They portray different paths that high-performing firms have taken to establish strong competitive positions in the asset management industry.

Asset management firms seeking to chart a new course in the current economic environment can begin with a three-step assessment process:

1. Current state analysis
   The firm should look at its present performance and see how existing strengths and capabilities match up with the various operating models we have described. It might, for example, examine recent and historic investment performance and determine whether such performance is strong enough in specific areas to merit adapting a FAF strategy. Similarly, if the firm is already part of a bank or insurance holding company, this structure may suggest following the EVC model.

2. Gap analysis
   Once the basic operating model is chosen, the firm then should concentrate on the capabilities needed for successful differentiation using this approach. A GSP will typically have a complete product line spanning passive, active and alternative funds across asset classes, with leading capabilities in sales and distribution, global reach and well-recognized brands. A firm seeking to compete as a GSP should begin the process of determining where and how to invest to reach this level of competence—or if another operating model is more appropriate.

3. Strategic choices
   The operating models described are not mutually exclusive, but in most cases firms will have to make tough decisions about which strategic paths to follow and how to invest for maximum impact. A firm that wishes to become a top-tier CEC may need to exit or de-emphasize certain products or markets. In other cases, it may be desirable to form a strategic alliance with another provider, such as taking an "open architecture" approach to offer customers attractive alternative investment products rather than investing heavily in building up a home-grown alternatives capability.

As Accenture’s research shows, there are a number of roads that asset management firms can travel to achieve high performance. Even the largest and most successful asset managers, however, cannot be all things to all investors. To enjoy lasting competitive advantage, firms must identify the most appropriate course of action and then dedicate themselves to building the skills, resources and capabilities needed for continuing success.
Conclusion

A volatile investment environment, evolving consumer preferences and behaviors and significant changes in distribution make it imperative for asset managers to re-examine their basic operating assumptions.

While cost cutting through headcount reduction and other means has limited the decline in profitability, asset managers must now find ways to grow both AUM inflows and margins.

There are a number of ways to succeed, but asset managers will do best for their shareholders, customers and employees if they match their strengths and resources with a suitable operating model. Doing so may require organizational development and improvements to the IT infrastructure, in particular to data management and analysis, as well as adoption of innovative technologies in areas ranging from distribution to regulatory compliance.

While choosing the right operating model is vitally important, achieving high performance will depend upon effective execution and investing in the capabilities needed for lasting success.
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