An overhaul for funds distribution in Asia

The funds industry is undergoing some sweeping changes which could lead to an exodus of providers along with a shake-up in terms of distribution channels, says Edouard Hoepffner of UBP.

In five years' time, the investment funds industry in Asia could look vastly different from what it is today – via more specialisation and fewer players – in turn impacting the product platforms of private banks operating in the region.

More specifically, as far as asset management firms go, increasing costs, tightening regulations and dwindling returns could lead to the exit of weaker players from the market.

"There is definitely more pressure on product manufacturers to rationalise their product range by decommissioning products that no longer bring any value to the table," says Edouard Hoepffner, senior managing director and head of investment services at UBP in Asia.

To justify the higher fees associated with an actively-managed fund, it will need to strongly and consistently outperform its passive counterparts, says the Singapore-based product specialist. Those funds – and firms – which are not up to this task will be "weeded out".

FOCUS AND SCALE THE KEY

The upshot of such a trend is likely to be a more specialised focus on strategies that work. "Fund houses won't be able to offer the full spectrum of products without having a particular edge in any one thing," predicts Hoepffner.

As in private banking, AUM is key, so fund houses which expect to be able to run that on lower fees will have little chance of surviving unless they offer strategies that deliver consistent outperformance.

Scale will matter too. Without this, smaller asset managers will continue to find it difficult to secure a foothold in what has become a highly-competitive marketplace. Consider the area of research capabilities, for instance. Bigger firms tend to have a large number of analysts to carry out extensive on-the-ground research compared with smaller firms who might have just a couple of individuals trying to do something similar.

EDOUARD HOEPFFNER
UBP

"You may be an exceptional investor, but the amount of information you can gather will put you at a disadvantage vis-à-vis the bigger firms," says Hoepffner.

Technology might also add to the pressures on product evolution and distribution channels going forward.

Robo advisory services, for instance, are expected to eventually gain traction among private banking clients, especially at the lower end of the pyramid. "Robo-advice, if anything, is likely going to push investors towards ETFs and traditional mutual funds," says Hoepffner. This is also in line with his expectations of seeing growth in passive product acceptance in Asia in the coming years.

"Clients increasingly want to speak to a specialist in the product that they want to consider," adds Hoepffner. "This means someone with whom they can engage with in a genuine discussion."

TOUGH TO FIND TALENT

But getting the right individuals to fulfil this role remains a challenge. Apart from the obvious cost of hiring and onboarding, there is also frequently a lack of expertise within internal support teams about compliance, legal and other requirements when it comes to selling products effectively and correctly.

"It becomes an increased risk that banks don't want to pursue," says Hoepffner. "Outside of the traditional bonds, equities and mutual fund space, recommending anything to clients is a much more difficult proposition."

"With the cost burden increasing for every bank, you could inevitably see a potentially smaller list of recommended products."

Scale will also be crucial for private banks, as many continue to struggle to grow amid tightening regulatory requirements and increasing cost pressures – either from hiring more people or maintaining large product platforms.

"With the cost burden increasing for every bank, you could inevitably see a potentially smaller list of recommended products," he explains.

Yet this might not necessarily lead to lower performance if the due diligence is done right, and there is greater understanding and expertise for those products which are recommended.

This creates a Catch 22 for the banks. Given today's low-interest rate, low-growth world, investors are becoming more interested in alternatives to potentially enhance yield.

"I think there is room to get exposure to those kinds of assets after looking into the client's portfolio and adding these allocations to help overall returns. However, in terms of risk, it is getting increasingly difficult to deliver these types of assets within a private bank," he adds.

FINDING FAVOUR WITH FUNDS

None of this looks likely to help deepen mutual fund penetration within private banks generally in Asia, which remains relatively low, on average, in the single digits.

However, some banks are bucking this trend. At UBP, for example, the penetration of funds is much higher than the industry average, according to Hoepffner.

He says this is the result of a concerted effort to encourage clients to look more deeply into active funds. "We have been engaged with our bankers to establish how best to position these funds using allocation grids," he explains. "We've managed to create a bit more interest around investing in funds by highlighting their key benefits."

The bank has also organised educational forums for its bankers, including 'fund days' twice a year where bankers speak directly with fund houses to understand why some strategies are performing better than the rest, and to learn how to have more needs-based conversations with clients.

"It doesn't mean we don't recommend individual or other products to our clients," he adds, "but we are trying to promote the idea of diversification and active management to clients, where it makes sense."

For 2017, meanwhile, UBP remains upbeat about generating more business after its integration with the international business of Coutts.

"The investments in Asia, both on the asset management and the private banking sides, will continue, so that's a good message," says Hoepffner. ■