Flexing digital muscle to tap China's funds industry

International asset management firms need to be on top of technological trends in the PRC and put in place the right digital tools if they want to make any headway in the domestic funds market, says Lennie Lim of Legg Mason.

Based on the direction of distribution and investor preferences in mainland China, fund houses must be digitally savvy if they want to enjoy any meaningful success in the rapidly growing local asset management industry.

While other markets in the region are only starting to experiment with the idea of digital distribution of funds, China is way ahead in the game, according to Lennie Lim, managing director and regional head of Asia (ex-Japan) at Legg Mason Global Asset Management.

"China is the only place where you see proper digital distribution of funds," he says. "Digital strategies are far ahead in that country than anywhere else."

DIGITAL ERA

In recent years, online sales of mutual funds have soared in China as investors increasingly bypass banks and financial advisers, opting instead to shop for these investments via their mobile phones. In fact, the average person in China would probably rather lose their wallet that their phone, observes Lim.

Chinese banks have also come to engage their clients in a very effective way. According to one estimate, more than half of all funds in China are now sold online, from almost zero six years ago.

The most favoured style remains money market funds, which are viewed as alternatives to bank deposits but with a slightly higher yield. There is still relatively little demand from Chinese investors for equity and fixed income products, according to experts.

Indeed, even the concept of investing is still new; most customers tend to use their money market fund accounts as cash accounts. So while funds may be widely distributed online, getting Chinese investors to accept financial products as investments, in general, is a tough sell.

LENNIE LIM
Legg Mason

In the 2016 Legg Mason Global Investor Survey, for example, 74% of those aged 40 and over and 77% of millennials in China, regard investing in financial markets as akin to gambling in terms of the odds of success.

Similarly, the view of Chinese investors on the meaning of 'long term' was the shortest among all countries in the survey; about 68% said they believe a long-term investment's timeframe is five years or less.

GROWTH POTENTIAL

At the same time, such findings also show the vast scope of growth for investment products in the PRC, including mutual funds.

In 2016, for instance, AUM for the mainland funds industry climbed to USD7.5 trillion, up 36% from a year before, according to data from the Asset Management Association of China. While a regulatory crackdown led to the growth rate falling significantly from levels in earlier years, market experts believe the upshot could be a more long-lasting – and sustainable – funds industry.

Against this backdrop, digital is expected to continue to be a driving force. And a more collaborative approach seems likely to be an effective and efficient way to go.

This is in line with an official announcement by Legg Mason in late 2016, that it had found a strategic partner to potentially give the asset manager an edge in the tech-driven market.

Shanda Group, run by Chinese billionaire Chen Tianquiao, who made his fortune through online gaming, said publicly that it would increase its stake in Legg Mason from 10% to 15% as part of a long-term strategic investment. The press release also stated that Chen would join the board of the US-listed asset manager as vice-chairman, to lead Shanda's efforts to assist Legg Mason in technology innovation, as well as business development and brand-building in Asia, and China in particular.

INDUSTRY IN FLUX

More broadly, in the global asset management industry, Lim sees some significant structural changes underway. Apart from consolidation among some of the larger private banks, distributors are becoming more demanding, especially with the kind of information they seek from fund houses. "We are working more closely with distributors to ensure we provide them with relevant and timely content. This could be in the form of timely market updates or thought leadership pieces," explains Lim.

"Data mining becomes important here," he adds. "We want to offer content they are interested in." Falling fees and commissions are also challenges for asset management firms. "In an industry that is experiencing margin compression, it becomes extremely important to keep costs under control," says Lim.

While some of this pressure comes from technological innovation, a fair amount is also attributable to the rise of lower-cost passive funds.

According to a report in the Financial Times, citing Morningstar data, passive funds grew 18% to hit USD6.7 trillion in 2016. That rate of growth was more than double than in 2015. Active mutual funds, meanwhile, grew a mere 4% in 2016.

Such trends have led to some of the largest international asset managers, including Legg Mason, making recent announcements that they would cut some administrative jobs. To survive the long haul, Lim believes fund houses need to deliver unique, differentiated offerings. This works to Legg Mason's advantage in Asia.

> **"China is the only place where you see proper digital distribution of funds."**

The group has dozens of product offerings across fixed income, equities and alternatives for clients in the region, including an unconstrained bond fund that has proved to be highly popular among private banks.

The firm is also considering adding more products in the infrastructure segment, given that it is an interesting time for such assets in countries like Japan, the US and even China – all of which are eyeing a boost in infrastructure investments.

"While tactical opportunities are already available, on a more strategic level, infrastructure assets offer a good diversification opportunity as their correlation with equities as well as fixed income is very low," explains Lim. ■