Four opportunities for independent wealth managers in Asia

Recent moves to lower costs and increase investment minimums by private banks in Asia have independent wealth managers perfectly positioned to assist underserved, yet affluent, clients, says Mark Nelligan of BNY Mellon's Pershing Securities Singapore.

Much has been said of the growing opportunity for independent wealth managers is Asia, but its enormity and the actual numbers involved deserve reiteration for smart professionals who recognise its potential. This is according to Mark Nelligan managing director, BNY Mellon's Pershing Securities Singapore Pte Ltd. "A hyper-focus on profitability at the region's private banks have seen 2016 restructuring trends continue well into 2017," he says, "including staff cuts and ongoing increases in minimum investable asset requirements from several major players."

The reasons make sense. As margins grow tighter, Nelligan sees private banks focusing on more profitable segments, realising the UHNW cohort is more lucrative than those less affluent. Indeed, portfolios of individuals with USD10 million or more in liquid assets grew at a compound annual rate of 9.7% between 2010 and 2014, and are expected to grow at a compound annual rate of 11.7% from 2015 to 2019, according to a Barron.com article in April 2016, entitled 'Asia's Super Rich Focus of Private Banks Shakeup.'

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MARK NELLIGAN
Pershing Securities Singapore

The boost in minimums, in particular, with some as high as USD20 million, is presenting a problem for investors that would typically qualify as HNW, yet nonetheless find themselves below these private banking requirements, explains Nelligan.

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MORE PENETRATION EXPECTED

Independents currently account for an estimated 4% to 5% of all AUM in the private banking space.

And these percentages are expected to increase significantly in the near-term, with some market practitioners predicting a 10% to 15% market share in the next five years.

"Specifically," predicts Nelligan, "opportunity presents itself for independents able to occupy the space between private banks with said multi-million dollar minimums that charge clients 150 to 200 basis points just for the 'privilege' of investing, and lower-net-worth, self-directed retail investors (with an emphasis on robo-advice services) they ignore."

He has seen much of the industry's press and attention centering on the trends towards cheaper and simpler services through the use of passive ETF strategies, rather than how this void between private banks and the average retail investor is – or can be – filled.

"Some of the reason for low market penetration is attributed to the mistaken impression that independent wealth managers act in a manner similar to fund managers, and perform the investment function only," he explains.

Advocates for the independent space note the competitive differentiator that exists in allocating client assets to those investments most suited to their given situation and needs.

"It's similar to what's currently occurring with their North American counterparts," adds Nelligan.

Here, more wealth managers and financial advisers in the US are leaving wirehouses (private banks) to become registered investment advisers (independent wealth managers), with the latter growing assets at a faster rate, on a percentage basis, than any other sector of the American financial services industry, so said a report on Benefitspro.com in September 2016, entitled 'RIAs Growing Market Share While Wirehouses Shrink: Cerulli'.

Nelligan says part of it is due to the unconflicted nature and higher payouts the independent space affords, yet a more robust value proposition in the form of allocation and advice services as differentiating factors are also frequently mentioned.

"Independent wealth managers can similarly differentiate their services by positioning themselves in a way that makes it clear about what they do – and do not – provide," he says.

"Doing so not only defines who they are in the eyes of clients, but also other industry professionals, allowing them to collaborate, rather than compete, with complementary players."

OPPORTUNITY ONE: REDUCE ADMINISTRATIVE OVERHEAD

In addition to a more focused value proposition, three other factors point to success for those that are currently occupying, or at least contemplating, a move to independent wealth management in order to address the growing gap between UHNW clients and those firms servicing lower-end retail investors. "The various administration and infrastructure issues are making it more difficult for private banks to compete," adds Nelligan, "as competition to offer new and better technology capabilities in part drive expense."

He believes that smaller firms with lower embedded costs and more nimble independent wealth managers can therefore often better compete on price.

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OPPORTUNITY TWO: MANAGE INVESTMENT COST

This is especially true with the current move by many independents to passive ETF products. A record USD3.07 trillion of assets were held in ETFs globally in 2016, according to 'The Evolving ETF: Using Exchange-Traded Funds in Client Portfolios' from BNY Mellon's Pershing LLC.

Additionally, there were 6,240 products, 12,042 listings and 277 separate firms offering the product. "ETFs are an egalitarian solution with the same minimum investment size and cost structure, whether it's an institutional investor, financial adviser or direct investor," according to the Pershing study. "They are, therefore, increasingly popular in international markets."

The number of ETFs listed in Asia, specifically, has doubled in the last three years, while total assets in the region have reportedly grown 33% to more than USD130 billion.

In 2016 alone, the region's ETF assets grew a net 20%, according to an article entitled 'Asia's ETFs need to crank up the volume', on Asia.nikkei.com in March 2017.

"Independent wealth managers in Asia are using ETFs to alleviate price sensitivity by realising competitive returns akin to those received from private banks, but without the associated costs that traditionally accompany their mutual fund and similar product counterparts," says Nelligan.

As this cost of investment becomes increasingly negligible, independents are charging for advice, leading to greater transparency and alignment of adviser offerings with client objectives, he adds. "They're typically compiling ETF baskets with between eight and 12 securities per basket."

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OPPORTUNITY THREE: CONSIDER A MORE FLEXIBLE COMPENSATION MODEL

According to Nelligan, many experienced private bankers and relationship managers are reluctant to leave the structure, support and, yes, salary, of their affiliated institutions.

But for those seeking to shed the governance associated with many private banks for a newer, more flexible model, he says they are finding it in the independent wealth management space.

"Additionally, those looking for more consistent compensation in the form of regular payouts, as opposed to the 'Swiss model' of lower base rates with the potential for bonuses, are finding the independent channel attractive," adds Nelligan.

OPPORTUNITY FOUR: BE VIGILANT ABOUT RULES AND REGULATION

Conflicted advice is all too prevalent in financial services, underscored by the frequency of regulatory sanction and fines, and most recently, action involving fee-sharing arrangements.

"Many private bank clients are therefore wary of transferring assets, as many consumers of independent wealth management services are unsure of what to expect in terms of the extent of the compliance policies in place, given the lack of brand equity of individual firms," says Nelligan.

As a result, he believes that a strong commitment to compliance is therefore a key component – and something increasingly being seen within the industry as a whole. "Ultimately, each of these four factors can cause excitement and apprehension for those professionals committed to, or considering, the independent wealth management space," adds Nelligan.

In all cases, partnering with the right custodian – which means one suited for the manager's experience, asset size, client base and technology requirements – can, he believes, alleviate the associated stress, provide necessary resources and support, and ensure the right frame of mind for success. ■

For more on trends in ETFs, read this whitepaper from BNY Mellon's Pershing