Three factors affecting fund industry growth in the Middle East

The funds industry is struggling with some key challenges, but the potential of the Middle East market remains undimmed, say experts at a roundtable involving leading asset management firms organised by Hubbis in Dubai.

Regulatory change may have caught the Middle East asset management industry by surprise in 2016, but there are other key issues that continue to hamper funds penetration.

This was the view of senior experts from the asset management industry who gathered to discuss the key market trends at a roundtable organised by Hubbis in Dubai.

As one participant noted, conversations about regulations are now taking up 35% to 40% of the time in discussions with peers – an indication of how much the issue has come to the fore.

Nevertheless, while a lack of regulation is bad news, effective regulation is.

The issues, in this case, are the pace of change and short time frames in which companies have to transition to the new regime.

LIVING WITH CHANGE

The latest regulatory changes from the Emirates Securities and Commodities Authority (SCA) place the responsibility on asset managers – including ETF providers – to register funds, along with increasing costs.

While the registration charges are just a starting point, representing about 1% of the entire process of selling and advising on funds, they still represent a fair challenge for fund houses to implementing the new rules quickly. In addition, the extension of regulations to funds with insurance products has injected new uncertainty, and possibly higher costs, into the whole issue as well.

Adding to the confusion is that there is also an insurance regulator, which regulates that segment, which has not commented on this issue. Clarity is still awaited on the matter, according to the market participants.

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IN THE RIGHT SPIRIT

While participants agreed that the basic goal of the regulation was to protect the consumer and grow the industry,

the fact that there is so much discussion about the challenges of implementing the new rules suggest that the overall goal of growing the market isn't necessarily being achieved.

Participants at the roundtable agreed that while the spirit of the regulatory changes is good, the challenge lies in implementation.

On the plus side, the new rules have united different participants into considering how they, as an industry, can tackle the regulations as an industry.

DRIVING DEEPER PENETRATION?

In the long run, strengthening regulations, of course, is also expected to drive greater fund penetration.

With the recent changes in laws, distributors may be forced to consider new revenue models that are not predominated by sales of wrap products. That rethink on business models could lead to a greater appreciation of funds.

As one participant noted, mutual fund product managers working at banks, who used to be focused on wrap products, have become very active.

Now, senior management is reaching out to these managers, asking them to figure out alternatives that can compensate for any potential loss in revenues occurring as a result of changes in business model.

EDUCATION

Apart from regulation, education was deemed by participants as important to develop and deepen funds penetration as part of a more holistic wealth solution.

There was agreement that the mind-set of most relationship managers (RMs) has to change, shifting from making money upfront towards building a more annuity-based business.

For clients, education is strongly needed, said participants, in the area of understanding the need for diversification and moving away from heavily leveraged products.

Some participants noted that education was important not just for RMs, but also for senior management; they need to rethink business models that reward RMs via commissions.

Instead, a system in which bonuses are based on AUM could drive more sticky flows and sustainable revenues, rather than an approach of 'selling' products to clients.

Most participants agreed that all this, however, can only really come once the right regulations are in place. In addition, rather than being regulatory-led, these efforts should be initiated by distributors.

Indeed, some local banks are already doing their bit to improve the skill-sets of their employees. Training academies, for example, can help improve the knowledge and skills of their staff to discuss investments. Educating clients about the risks of using too much leverage was also mentioned by participants.

Further, there is an expectation that with evolving regulations and improving education, clients might start to opt for products that are not highly leverage-driven. Nevertheless, to start with, they could be satellite investments rather than core holdings.

DATA

Finally, another challenge that experts from fund houses believe exists, relates to getting reliable data in the Middle East.

While the general perception is that there are billions of dollars waiting to parked in investment portfolios, the reality is that getting an accurate picture of the market is tough.

As some participants pointed out, it's difficult to understand accurately how much money actually flows out of the Middle East via private banks in Singapore or Geneva.

Lack of market data also challenges asset managers when drawing up plans to enter or grow in the region. Decisions such as how many staff to employ based on assumed market potential are essentially educated guesses.

Even when making internal presentations, participants said they struggle to present an accurate picture of the market, which often undermines efforts to add more resources in the region. ■

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