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Wealth in Thailand: ready for the next big step forward?

There is plenty of liquidity in the Thai financial markets, but where should it be invested? Hubbis and J O Hambro Capital Management invited a group of private banking, asset management, and other selected wealth management experts to a private discussion in Bangkok this April to discuss the future of wealth management in Thailand.

THE BEHIND-CLOSED-DOORS DISCUSSION at the St. Regis Hotel focused on current topics of interest such as the growing trend for retail and HNW investors to invest more in equities rather than their traditional fixation with fixed income; the rising interest in overseas investments and alternative assets; the evolution of the local financial markets; the impact of regulation on the wealth and asset management sectors; the arrival of more foreign private banks; and leveraging the major banks' and insurers sales and distribution power.

The discussion began with one expert focusing on the local regulatory environment that, although on the liberalisation path, has thus far somewhat hampered attempts by the financial community to promote the sale of overseas investment products to retail or private investors as rapidly as many would like. "It was only about two years ago that the Bank of Thailand allowed more flexibility for retail and accredited investors to go abroad," said one expert.

"This means that the advice and the services for the investors here are somewhat lagging as we have not had the experience necessary. Moreover, the regulatory relaxation is only partial, and many minor obstacles remain in terms of providing these services to investors."

Nevertheless, he also conceded that the general investment market environment has improved markedly. "As it currently stands, we are now able to provide the investors here access to almost every investment product in the world, including hedge funds or private equity. However, as this is fairly recent there are clearly limitations to our local know-how and to investor confidence and understanding."

It is to some extent into this partial vacuum that, as another attendee noted, foreign private banks have been drawn, encouraged also by the rapidly growing high net worth (HNW) segment in Thailand, as the economy and asset markets both expand.

Offshore private banks ride the wave of rising wealth

"Global and specialist private banks have certainly become more visible and active in Bangkok of late," one attendee reported. "Their licenses might be from Singapore, Hong Kong, Switzerland and so forth, but they have employed Thai professionals in those respective countries and have come to mine money out of the Thai HNW and ultra HNW segments here. Many such investors have not already sent some or most of their wealth abroad, but there are plenty of others that these international banks can hope to convert."

The same banker argued that despite this influx of competition, the universal Thai banks do not consider this much of a threat to the major local banks and wealth firms. "I do not personally think

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the foreign private banks are such a big concern in the near term as they generally open representative offices here and they largely do not apply for local trading and derivatives licenses. So, they will be restricted in what they can do, and unless they take over some local securities or other firms, they will not be such a threat.

He pointed out that the growing trend is, in fact, more towards joint ventures to align the skills and products of the offshore private banks with the compelling local strengths and distribution power of the major local banks and financial institutions.

Partnerships of powerful local and foreign brands

A banker from a leading Thai bank confirmed this trend. He explained that his own bank's partnership with a bespoke Swiss private bank was helping them rapidly beef up their offshore investment expertise and distribute product through their Bangkok relationships managers to HNW individuals they know well. "We are now partnering to offer products to the customers; this is a development that is one step further than the Thai bank having all the customer interface," he explained.

"But perhaps the key impediment, for now, is human resources, so we need to increase the skill levels of our people because we are creating a joint venture; the mixture of the people there will be critical to how they are going to provide the service and make it a seamless service. We need to make sure we internationalise but keep our Thai qualities and character."

The international private bank model in Thailand works exceptionally well alongside the extensive coverage and distribution power of the leading Thai banks that have blanket coverage across the country. "Backed by this very powerful engine our number one goal right now is to educate clients," he added.

"We are not afraid of introducing more complicated products or sophisticated instruments as long as it helps their portfolios," explained another expert. "So, we take a lot of time to boost the skills of the RMs and help the clients build their core products, not for trading, but with the philosophy of a snowball type effect of the business, building and building scale and solidity."

But another expert did sound a note of caution. "It does concern us that the leverage that international private banks have encouraged related to fixed income products in other markets might find its way into this market. Aside from excess leverage of some fixed income products, I think for example that the Singapore insurance sector is potential perilous due to the high leverage in some of those life insurance products."

He also cautioned that for Thai investors, leverage, when applied to overseas dollar assets, is especially dangerous, if the exchange rates move unfavourably.

"We need to make sure we do not copy some of the worst practices from abroad because Thailand now has a relatively clean slate and it is in a strong position. We need to balance sensible practices while also taking advantage of the ongoing liberalisation of the financial markets here."

Looking to equities and offshore assets

The fund management business is evolving rapidly in Thailand, creating new growth opportunities for local and global players.

But there is great room for growth—experts estimate that less than 50% of Thai investors buy mutual funds, whereas in neighbouring Malaysia that figure is around 80% and still growing. Thailand's mutual fund industry today boasts AUM of roughly Thb4.8 trillion (equivalent to USD155 billion).

A core challenge for the industry is to increase the share of equity funds in the mutual fund sector; today equity funds account for only about 21% of the market, while the majority, some 54%, are still in fixed income funds, with the balance comprising a variety of property, infrastructure and other funds.

Thailand enjoys a large and growing population that is becoming increasingly well-educated and prosperous, and as that happens, the penetration of asset management products will inevitably rise.

And investment behaviour will become more diversified. It used to be that Thai investors would invest only, or mainly, in fixed income funds, but in the past ten years they have been moving gradually beyond fixed income to equity, offshore, real estate, commodities, and other asset classes. Many therefore see the market becoming more accepting and understanding of products with greater complexity that cater for the more demanding investment outcomes many investors are looking for.

Given the continuing low-interest rates in Thailand, investors are aware that the returns on global funds are considerably higher than Thai bonds or Thai deposit rates. Moreover, while the Thai bond market has developed steadily during the past ten years, there is still not enough product and liquidity in the market.

One of those present at the discussion explained that while there is huge liquidity in Thailand, especially amongst corporates, there are only modest investment opportunities at home.

"The corporates either use their liquidity to acquire businesses or they tend to place money in deposits or money market and fixed income funds," he explained. "They do not borrow so much as they are cashed up and that restricts economic expansion. Accordingly, our GDP growth of around 4%, albeit solid, is lower than less developed neighbours that are posting 6% to 8% annual growth and similarly developed ASEAN countries such as Malaysia and Indonesia, which are registering some 5% annual expansion."

products, albeit this growth coming off a small base."

An estimated 20% of the fund market is now in foreign or alternative assets. Central bank data shows the Thai mutual fund industry's AUM rose 7% in the nine months to September 2017, with the growth helped by funds that invest abroad, which grew by some 15%.

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Fixed income still dominates... but other asset classes rising

He explained that it is partly because of the limited diversification opportunities at home that the Thai mutual fund industry is still more than half invested in fixed income.

"The idea of expanding to overseas products is a natural development, and that is also why we see robust growth in foreign fund products, albeit this growth coming off a small base."

One attendee gave some insights into his clientele of around 10,000 clients, with an average age of about 60 and split roughly evenly between men and women, and with some 70% still owning their own business and around 30% have inherited their wealth. "Most of their investments are still

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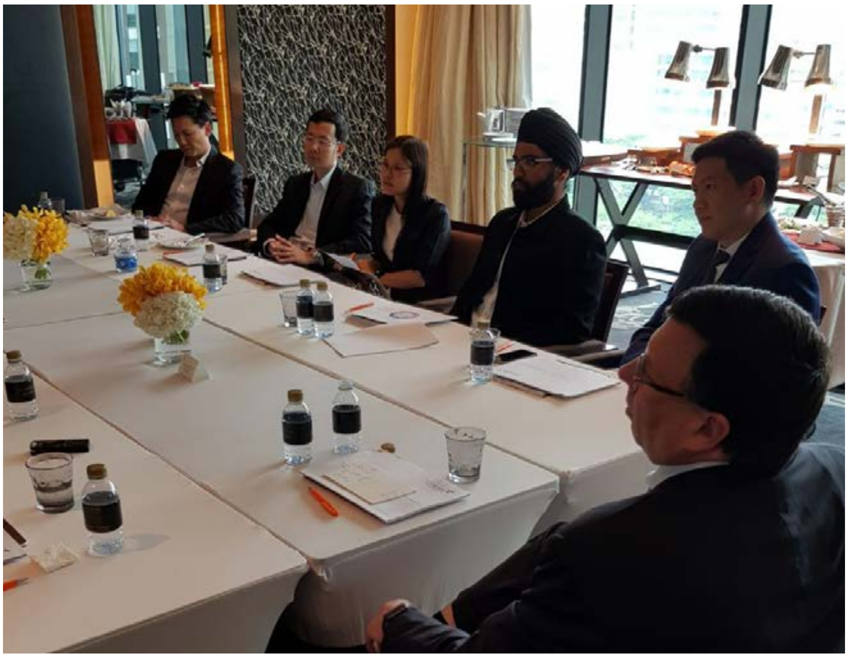

in fixed income," he explained, "but we see a gradual roughly 5% a year movement to long-term multi-asset investments that we design with the help of five international banks and private banks."

Sophistication of service providers set to rise

He added that to develop the market further, the sophistication of the clients and the bankers must improve in parallel. "When we have the floodgates open and we have more complex products coming in which theoretically will benefit the investor, both sides of the equation need to be sufficiently sophisticated to understand the products, or we risk more harm than good."

A representative from a global life insurance company noted that his firm's life fund stays in the domestic market while foreign investment is via their unit-linked products, an area that has enjoyed considerable expansion in recent years. "We started our unit-linked business about three years ago, and foreign funds account now account for over half of all the clients' holdings, of which roughly two-thirds would be equities and one-third global fixed income."

Fund houses are therefore positioning themselves to benefit from the gradual diversification of risk and return, rolling out more funds focusing on offshore assets.

He added that while interest rates in the Thai market remain low - the 10-year government bond yields about 1.5% - unit-linked products continue to be attractive. "This could change if rates rise notably, as investors here prefer safety, but for the time being low rates here encourage greater risk taking in terms of investments." It is for these reasons that wealth management experts believe mutual funds offering equity and foreign exposure have such great growth potential. Fund houses are therefore positioning themselves to benefit from the gradual diversification of risk and return, rolling out more funds focusing on offshore assets.

Banks and insurers expand open architecture

Linked to this diversification trend is the rise, since around 2016, of open architecture, whereby the leading banks are increasingly selling the funds of other asset management firms, as well of course as their own in-house products.

In opening this door ever wider, the banks are aiming to retain their clients and migrating those customers to fee-earning products while the net interest margins for the banks remain so low.

The same expert highlighted the evolution of the distribution model for the major banks, which now employ open architecture.

"In the past," he reported, "the major banks would sell only their subsidiaries' funds, but now the major banks and insurance companies have onboarded funds on their unit-linked businesses. So, when an independent company like us wants to have our funds sold at branches of a major bank, for example, we simply need to make sure that our funds are different to that bank's own offerings."

Some firms add in free enticements such as health insurance, privileged car parking and so forth. "This," explained one representative from an asset management firm, "helps us as we are not affiliated to a major bank here and we strive to be creative and innovative. Every time there are new initiatives, whether it is from the Stock Exchange of Thailand [SET] or whether it is from Securities & Exchange Commission [SEC], we always try to be their guinea pig as a pioneer. And the same goes for initiatives from the Office of Insurance Commission [OIC]."

He explained, for example, that his firm had created two funds, one with life insurance attached and one with health insurance. And encouraged by the SEC the firm created funds that can list in other ASEAN countries such as Malaysia and Singapore.

"This is all about us trying to be the first to the market with new ideas and to provide new and interesting ideas to the customers out there."

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Locals build enduring client relationships

In keeping with the theme of the leading Thai banks and wealth providers retaining their customers, the managing partner of an independent research and advisory firm commented that HNW, ultra-HNW and family office clients in Thailand report a considerably higher level of satisfaction with the banking and the investment services that they receive in Thailand than those they obtain overseas.

"It is a slightly unfair comparison because historically the Thai banks have offered a much narrower range of services," he explained, "but in general RMs in the Thai private banks build more enduring relationships with clients than the RMs in international private banks. To add to this, the liberalisation we have seen here is positive as people now have far greater access to ideas, products and services to help their overall wealth management strategies."

One expert noted that Thailand certainly needs more alternative investment opportunities, for example, hedge fund opportunities and private equity.

And another of those present added that greater liberalisation of the insurance sector would also help. "As an insurance company, regulations in Thailand have

become more relaxed, but we remain more restricted in what we can do than, for example, ultra HNW individuals."

An international insurance company representation concurred. "That is why we have been moving more away from the traditional product to the unit-linked arena," he reported. "You can see over the past ten years that savings are far higher than investments made. With low rates here, there are key challenges for the insurance companies like us, so we need to invest offshore to diversify and achieve higher returns."

Another perspective came from an attendee who highlighted the introduction of technology, especially data analytics, as well as further deregulation. "In terms of risk spectrum, clients at a certain risk level maybe able to buy more complex funds with reduced size requirements. Right now, certain funds that we sell with a minimum size requirement of Thb550,000 [equivalent to almost USD18000] might be seen as too big for the average retail client to buy, but if those funds can be marketed as retail funds that might help gain exposure and help build AUM for asset managers."

A wealth market for the future

The discussion concluded with general agreement that the opportunities for wealth management and the asset management industry in Thailand are primarily positive going forward.

"It is all about education," said one attendee, "it is all about driving clients to a steady and more diversified portfolio, but changing only the satellite portion, so they have a safe, steady portfolio with a smoother return."

To do so, he said, the industry needs further regulatory encouragement. He conceded that the increasing availability of open architecture from banks and insurance companies is benefitting everyone, but pointed out that the industry needs to see more diversification down to the average retail client. "We need further assistance from additional regulatory evolution and support to help develop the industry so that people are more aware of asset allocation and opportunities." ■