

A question

The asset management industry must regain the confidence of investors if it is to make up the ground lost during the economic downturn, **Jervis Smith** tells **Heather McKenzie**



The discussions at this year's Fund Forum International will have a sense of urgency not seen previously, says Jervis Smith, Managing Director, Global Head of Client Executive for Citi's Global Transaction Services.

"There will be a different emphasis at this year's event because of what has been happening in the financial industry during the past year," says Smith. "It will be interesting to hear what the very high-ranking representatives of the global asset management community have to say about the problems they are facing and the issues they are tackling."

Smith is chairing Wednesday's session, "The Future of Asset Management – the Asset Manager Perspective". He will be joined by Mark McCombe, Chief Executive of HSBC Global Asset Management; Massimo Tosato, Vice-Chairman of Schroders; Philip Lambert, Chairman of the Investment Committee at ABP Investments, and Phillipe Marchessaux, Deputy Chief Executive, BNP Paribas Asset Management. They will discuss how asset managers can win investors back and how client trust can be regained.

"Last year Fund Forum International took place just as the credit crunch was beginning to have an impact – but that impact wasn't universal. Not many people last year were talking about how they were going to tackle the fallout from the credit crunch."

That of course has changed and Smith believes different conclusions will be reached about how the industry should move forward. How, for example, will asset managers respond to much smaller profit margins?

"Over the years at Fund Forum, we have debated whether fund companies are well run or whether they have just been lucky during the sustained period of economic boom. Now that we are having a sustained period of economic downturn, I think the chaff will be sorted from the wheat."

It is no secret that the value of assets held by the investment industry has fallen – the second Annual Asset Management Report by the European Fund and Asset Management Association (EFAMA), published in April 2009, found that the value of assets professionally managed in Europe had fallen to around €10.7 trillion at the end of 2008, compared with €13.6 trillion the year before. The decline, said EFAMA, was due to the global financial crisis.

Smith's question for investment managers is: how are you going to win customers back? "It's all good and well for fund managers to talk about a decline in the market and how their fund's performance might be good relative to the rest of the market, but that is no consolation for an investor who is coming into retirement and may have seen the value of their pension fund fall by 50 per cent."

While many people talk about the need for the industry to regain investors' trust, Smith prefers to talk about investor confidence. "I don't think it is a matter of trust as such. We are dealing with a whole generation of investors who may feel 'once bitten, twice shy'. The industry needs to regain their confidence so they will want to invest again."

Another issue has been a recurring theme at past Fund Forum International meetings – product complexity. This has also contributed to the loss of confidence, says Smith, although he adds that fund managers have unfairly carried most of the blame for product complexity. "To some extent, distributors have escaped much of the criticism. In reality, fund managers rarely sell directly to retail or institutional investors. Retail products are sold through banks, broker-dealers or IFAs and institutional products are distributed via consultants. The distributors should also come under examination when questions are raised about the complexity of products."

There are a variety of methods to help claw back some of the confidence of investors. Smith advocates the teaching of investment in schools. Trying to explain the intricacies of retirement investing to people who should have made pension decisions 40 years previously is not a satisfactory approach, he says. He also believes distributors such as IFAs should offer their services on a fee basis, rather than be paid commission. "There is little chance that an IFA will give the best independent advice to an investor if they are being paid a commission to sell one product as opposed to another."

The investment industry, says Smith, has been very complacent and the long-term nature of the business means it is slow to change. "It is quite a challenge to change the culture of an organisation that, during the good times, had money pouring in whether it was good, bad or indifferent. But the money is drying up and these organisations must change their culture to be more commercial."

The winning firms will understand who all of their clients are. "Most asset managers understand the pension and retail investor clients but there are very few that really understand the high net worth area and the role that private banks play." With the number of multi-millionaires growing despite the

of confidence

economic downturn, Smith says asset managers must get to grips with this market sector.

In the medium term, the successful fund managers will be those that can adapt their business model to suit the changing economic circumstances, says Smith. "Firms must ensure that they are properly resourced for both upturns and downturns. A flexible business model where there are not too many fixed costs will allow firms to adapt and change quickly."

While firms need to be flexible, they also need to be certain what their core business is and what they can outsource to a third party. "In times such as these, asset managers should focus on the asset classes they know well and perform well in. If they are good at servicing clients, they should leverage that expertise and outsource what is not core to that. They can no longer be all things to all men as they were during the good years."

Being able to outsource certain processes or functions will help fund managers to face the challenges of the next few years and place operations on a variable cost basis. But fund managers must choose their outsourcing partners carefully – opting for those, like Citi, that can provide

scope, consistency, scale and insight that will help them through their travails, says Smith.

The current market turbulence is testing the fund industry: investor confidence has plummeted and revenues are shrinking. Having ridden high during the economic boom, fund managers are coming back down to earth with a thud. Decisions made now will determine whether these businesses can recover and cope with any future turbulence.

Now more than ever, a winning strategy requires fund managers to rethink their business models. Are they resilient enough to cope with future downturns? Do they fully understand all of their clients? Can they adapt to further change? And, do they know what is really core to their business? Finding the answers to these questions does not have to be a solitary task – with the right partner, fund managers can plan for what today appears to be a very uncertain future. **FFI**

