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Cost and growth in asset management

Benchmarking analysis and implications for asset managers

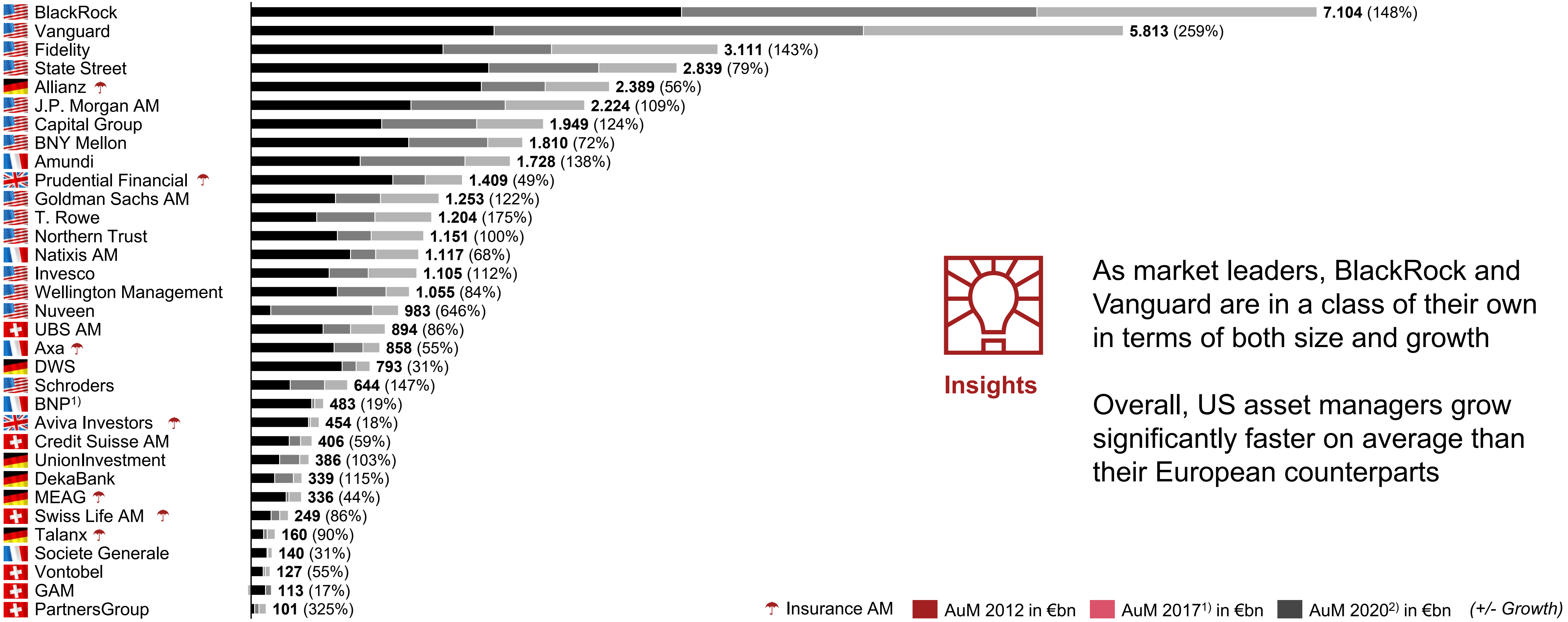
Executive summary

- Despite a **24% growth in AuM** (2018-2020) within our sample of 41[1)] asset managers, **profits** have **decreased by 24%**
- **Smaller asset managers** with **active** business models and a high share of equities remain among the **most profitable**, even at significantly higher costs per AuM
- Overall, the average **CIR has slightly improved,** from ~66.1% to ~65.2% – the continued focus on cost-saving measures has reduced OpEx to AuM from 31.3 bps to 25.6 bps (2018-2020), but the rate of this decrease is slowing
- One relevant group of asset managers on average **lagging behind on market profitability** are **insurance asset managers** (asset managers under the governance of an insurance company. A relevant share are captives)
- **Focus on insurance asset managers:** Our study reveals key traits of insurance asset managers and suggests that for captives, (asset managers providing asset management services only to their parent insurance company) **accepting third-party assets offers** a promising way to catch up with the market as the resulting revenue **more than counterbalances higher cost:**
  - **Profitability:** Revenue is significantly **below market average**. This results in a **below-market average profitability**, despite consistently lower average costs
  - **Third party business:** Insurance asset managers acquiring third party business display **higher growth** (through acquiring new assets) **and profitability**, as higher cost through managing third-party assets is more than offset by higher revenues
  - **Build-up of** third party business: Becoming profitable with third party AM by building the business organically takes between **4-7 years** on average and **€25-75 bn AuM**. Most influential factors are existing range of capabilities, existing offering, existing sales structures, brand and current size. Joint ventures / acquisitions can help to significantly reduce the time taken to reach profitability
- We conclude with suggestions for **top-line growth** through capabilities, i.e. growing business with **existing capabilities in the current market first** before expanding geographically and extending capabilities

1) 41 asset managers in sample with AuM reported at least for 2012, 2017-2020

US market leaders continue to grow significantly faster than European asset managers

Growth of largest and selected AMs (2012 to 2017 to 2020 in €bn)



Insights

As market leaders, BlackRock and Vanguard are in a class of their own in terms of both size and growth

Overall, US asset managers grow significantly faster on average than their European counterparts

1) Additional AuM from 2012 to 2017; 2) Additional AuM from 2017 to 2020;
Source: Strategy& analysis

Ongoing mergers and acquisitions continue to drive size and growth of asset managers

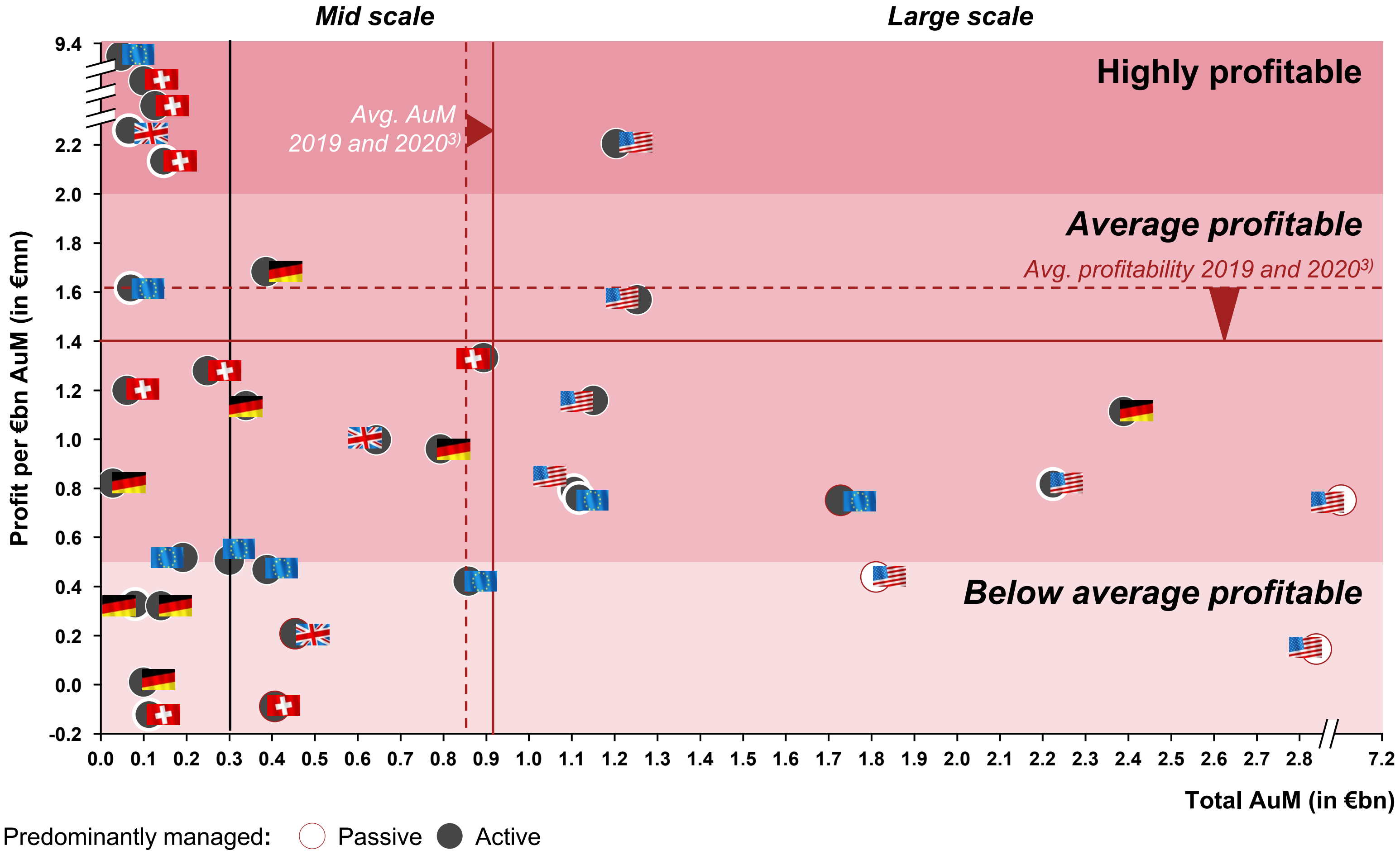
Selected M&A deals/ joint ventures in the AM industry

- **July 2017** – **Amundi** merges with **Pioneer** — 1310 (€bn AuM)
- **August 2017** – **Invesco** acquires **Source** — 802 (€bn AuM); **Standard Life** merges with **Aberdeen**
- **October 2018** – **Invesco** acquires **OppenheimerFunds** — 1200 ($bn AuM)
- **March 2019** – **Brookfield** acquires (most of) **Oaktree Capital** — 475 ($bn AuM)
- **May 2019** – **Charles Schwab** acquires **USAA** — 3900 ($bn AuM)
- **February 2020** – **Franklin Templeton** acquires **Legg Mason** — 1500 ($bn AuM); **Jupiter AM** acquires **Merian GI** — 65 (£bn AuM)
- **June 2020** – **Natixis** cooperates with **La Banque Postale** (to combine their fixed-income and insurance-related AM businesses) — 415 (€bn AuM)
- **February 2021** – **BCPE** to take full control of **Natixis** — 1117 ($bn AuM)
- **April 2021** – **Amundi** to acquire **Lyxor** — 181 ($bn AuM)

Sources: PwC AWM Research Centre, Financial Times, FN London, Investment Europe, press releases of depicted companies, Citywireselector

Slower AuM growth and profits sliding further. Smaller, active asset managers able to maintain pole position in profitability

Outside-in competitive profit benchmarking[1)]



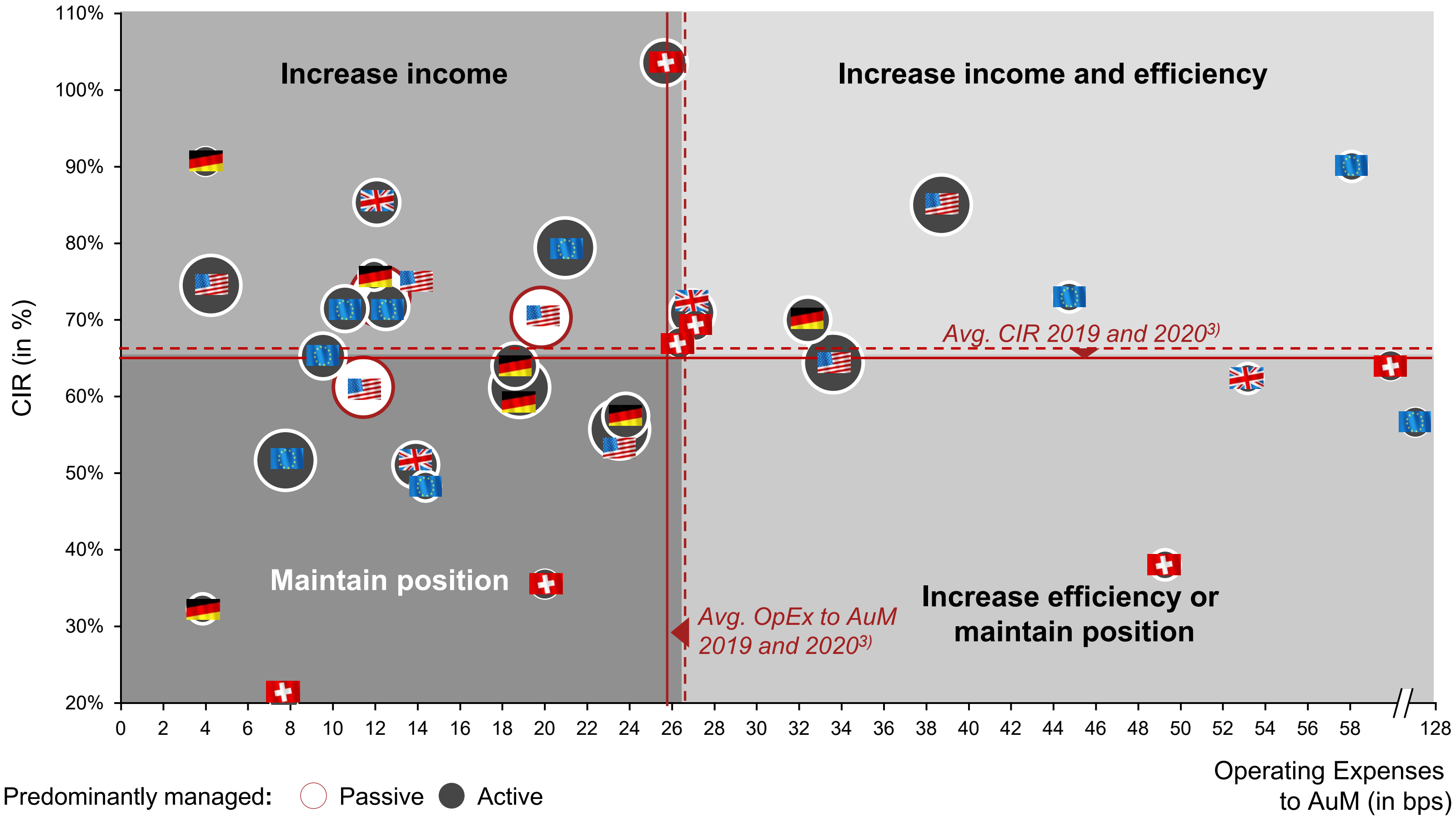
Insights

- In comparison with our 2019 sample study of asset managers:
  - **AuM grew by 6.6%** vs. MSCI World: 15.9% (12%[5)] vs. 27.7%)
  - Profit **decreased by 14%** (12%[5)]) on average (by €0.21m per €bn AuM)
  - However, one in three AMs were able to **increase their profit per AuM,** ranging from 1% to 100%+ increases, a similar result to last year's study
- The **most profitable AMs** are mostly **small** and **active** with business models similar to private equity companies (all with at least around 50% share of equities)

1) Sample of 34 asset managers with 2020 figures; 2) Also includes significant active or passive business; 3) For sample included in 2019 study; 4) 2019 figures for profit and cost; 5) 2019 numbers for comparison
Source: Company reports 2020; Strategy& analysis

Stagnation in cost and CIR – after high focus on costs in recent years, more focus on increasing income required

Outside-in competitive cost benchmarking[1)]



Size of bubble: small (AuM ≤ €250bn), mid (€250bn < AuM < €1,000bn), large (AuM ≥ €1,000bn)

Insights

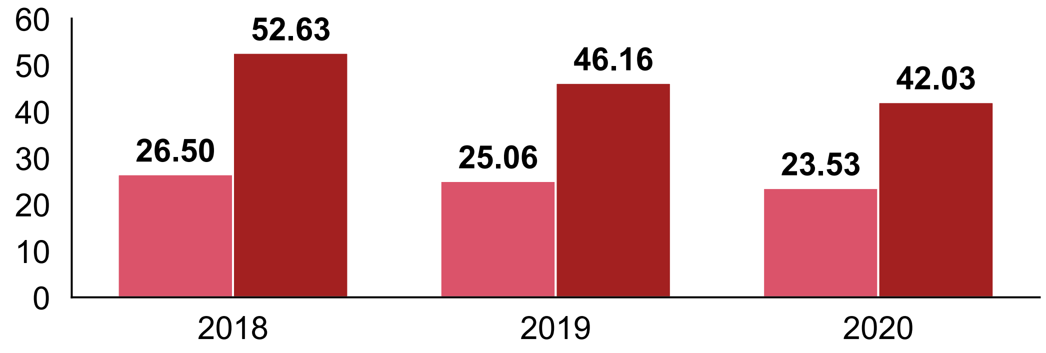
- Low costs do **not necessarily translate** into a low **cost-income ratio (CIR)**
- Successful asset managers with **active investment management** models are able to operate profitably **with high cost and low CIR**
- **Past dedicated focus on controlling costs led to** asset managers being able to slow down the rise in CIR due to falling income
- However, further reducing **cost** is becoming **less efficient**
- Therefore, **greater focus on increasing** income needed going forward
- **In income per AuM, insurance AMs** show **largest deviation from** average market (see deep dive on following pages)

1) Sample of 34 asset managers with 2020 figures; 2) Also includes significant active or passive business; 3) For sample included in 2019 study; 4) 2019 figures for profit and cost
Source: Company reports 2020; Strategy& analysis

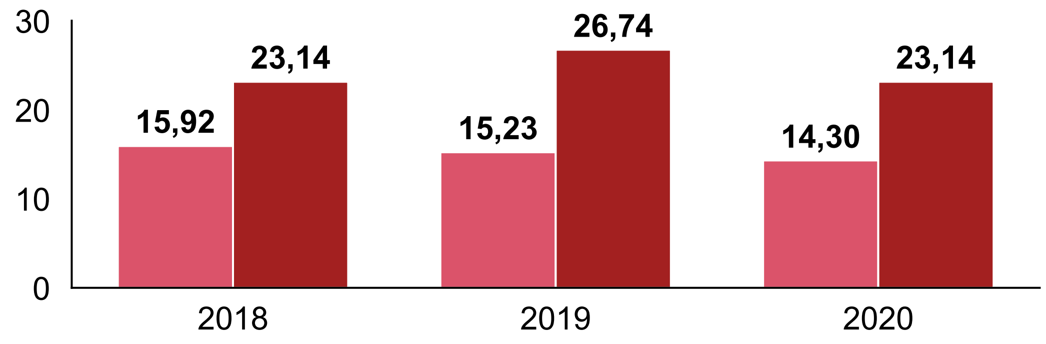
With revenue significantly below market, average good cost management is not enough for insurance asset managers

Insurance asset managers[1)] compared to market[2)]

Revenue per AuM in bps



Expenses per AuM in bps



Insights

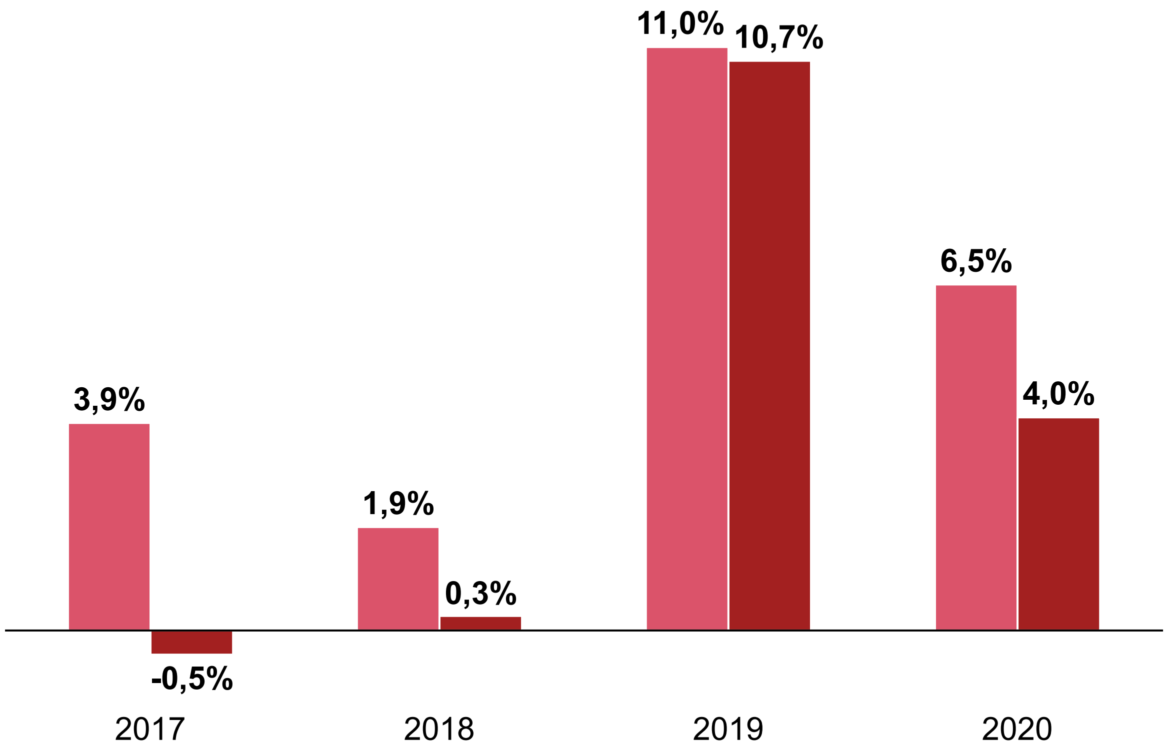
- Many **insurers believe in close control of their asset management** function and do not consider sourcing that capability, i.e. selling their asset manager
- However, **insurance asset manager** revenue is significantly lower than market average according to our analysis, and there is high potential for improvement
- Additionally, the remaining **low-yield environment** combined with a low-risk profile places a considerable weight on low risk, fixed yield products in the asset allocation reduce the chances of a natural increase in income and profitability
- Therefore, a **strategic focus on increasing revenue** is necessary – costs of insurance asset managers have historically been managed at significantly below average market levels.
- Increasing revenue by **acquiring a third-party asset management** business, which also reduces the average cost base, is therefore an interesting opportunity for captives

1) 15 insurance asset managers in sample: Allianz Group: Asset Management, Aviva Investors, Axa Investment Managers, Baloise Group: Asset Management & Banking, Legal & General, MEAG MUNICH ERGO AssetManagement GmbH, NN Group: Asset Management, Provinzial NordWest Asset Management, Signal Iduna, Swiss Life: Asset Managers, Swiss Re, Ampega, Zürich Insurance, SCOR, Die Mobiliar - Asset Management; 2) Sample; Source: Annual reports, Strategy& analysis

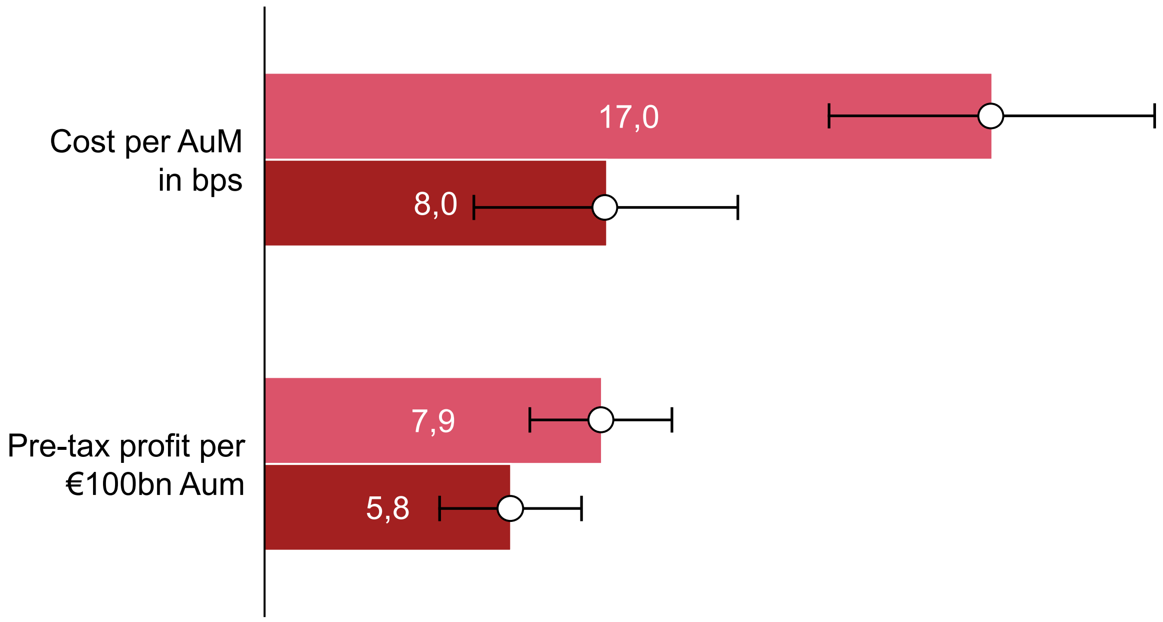
For insurance AM third-party inflows more than counterbalance higher cost through higher revenues

Focus on insurance asset managers

Yearly AuM growth of insurance asset managers 2017-2020[1)]



Cost and profit of insurance asset managers[2)]

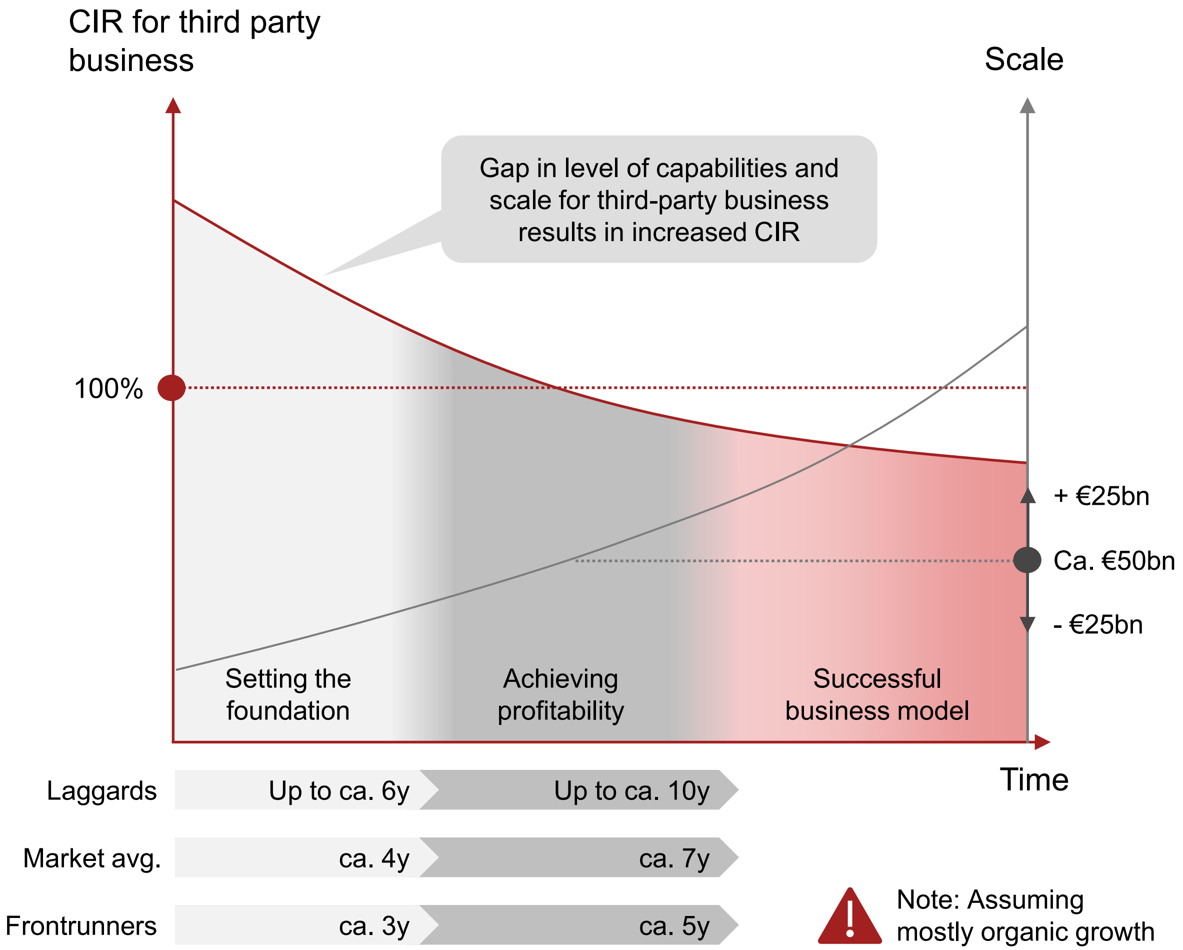


Insurance asset managers with reported third party inflow
Insurance asset managers without reported third party inflow (captives)

1) 15 insurance asset managers in sample: Allianz Group: Asset Management, Aviva Investors, Axa Investment Managers, Baloise Group: Asset Management & Banking, Legal & General, MEAG MUNICH ERGO AssetManagement GmbH, NN Group: Asset Management, Provinzial NordWest Asset Management, Signal Iduna, Swiss Life: Asset Managers, Swiss Re, Ampega, Zürich Insurance, SCOR, Die Mobiliar - Asset Management; 2) Where publicly available; Source: Annual reports, Strategy& analysis

Difficult beginnings – gaps in capabilities and scale need to be bridged to make third-party business sufficiently profitable

Scaling up third party business – the challenge



Note: Assuming mostly organic growth

Insights

- Serving third parties requires **build-up of new reporting and distribution capabilities** for captive asset managers, resulting in economies of scale for third-party business
- Cost of acquiring essential capabilities and scale **significantly increase CIR when starting** third-party business
- E.g. Swiss Life: In its third-party business, the cost-income ratio improved to 84% after 9+ years (previous year: 91%, previous years not reported)
- The time to **reach profitability** in a (mostly) organic way takes on average between **4-7 years** and requires a scale of **€25-75bn**
- Most **influential factors** are the existing range of capabilities, existing offering, existing sales structures, brand and current size
- **Joint ventures / acquisitions** can help to **significantly reduce the time taken to reach profitability** by bridging gaps in capabilities and scale

Source: Annual reports, Strategy& analysis

To bridge capability gaps quickly and scale up, many asset managers utilise joint ventures and acquisitions

Scaling up third-party business – market perspective

Baloise Group

Capability extension with acquisition

Baloise Asset Management acquires stake in Tolomeo Capital to extend capabilities towards institutional investors

Ampega

Extending the business with existing capabilities

Ampega manages assets from Frankfurter Leben run-off (€10bn)

Allianz

Capability extension with acquisition

Allianz GI acquires Rogge Global Partners to strengthen fixed-income capability

AXA

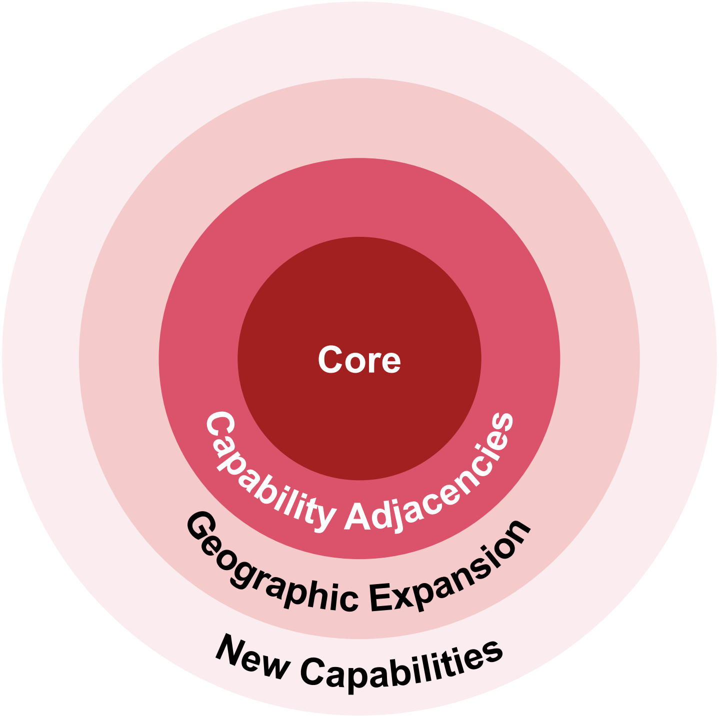
Capability extension with JV

Axa cooperating with Sirius Real Estate in joint venture “Titanium” to conduct alternative investments

Source: Annual reports, press releases, Strategy& analysis

Revenue growth choices are prioritized using a capability lens – business close to core capabilities is the primary focus

Scaling up third-party business – strategic perspective



	Grow with a capabilities lens	Takeaway for insurance AM
Grow core	• Sell more of existing products to existing customers with existing capabilities system • Acquire new customers in same market segment • Enhance depth of current offering	• Increase share of wallet • Seek to manage assets from third parties with similar risk profile and investment focus (e.g. fixed income for other insurers in the same market)
Extend capabilities system	• Leverage capabilities system to expand into new, complementary products and services	• Offer existing investment products for non-insurance clients with similar investment focus • Leverage insurance cat risk expertise to assess alternative investments
Expand Geographic footprint	• Take offerings, capabilities system and way to play to new geographies where they can thrive	• Expand existing offering into other European countries with similar pension / insurance structures and possibly similar regulation
Acquire new capabilities	• Adjust capabilities system – if fundamentals of sales and profitability are changing • Prudently select new capabilities and fill capability gaps, if new opportunities require it	• Offer third-party asset management for new assets classes / different risk profiles

Source: Strategy& analysis

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