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INDEPENDENT ASSET MANAGERS IN SWITZERLAND
TREND REPORT 2007 - 2010

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Key findings

Client advisory services and care come first: The clear core competence of independent asset managers is advisory services and care of their clientele and the client relationship.

Focus on private clients: Over 60% of independent asset managers have exclusively private clients. Only 2.5% of independent asset managers have institutional clients only.

General decrease in client loyalty anticipated: The industry expects client loyalty in all client segments to decrease over the next three years. Additionally, company size is negatively linked to client loyalty.

Differing growth strategies: Small independent asset managers generally follow an increase in "Share of Wallet" as their primary growth driver, whereas large companies concentrate on the acquisition of new clients.

Large growth potential: Increasing demand for independent asset management in Switzerland and a simultaneous decrease in the age of customers promise healthy growth potential.

Increasing company size in trend: The critical size for independent asset managers seems not yet reached, resulting in above-average overheads.

Decrease in offshore assets expected: All regions of Switzerland anticipate a relative reduction in foreign assets over the next three years.

Further increase in the problem of succession in individual companies until 2010: Smaller companies generally favor other independent asset managers as buyers. Larger independent asset managers in particular see banks and strategic investors as suitable partners in connection with continuation in business and implementation of new business models.

Threat of further regulation cause for concern: Additional regulatory measures would make the independent asset managers industry less attractive. Alternative regulation statuses, e.g. in the form of a securities dealer, are being considered by 5% of companies.

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Starting point

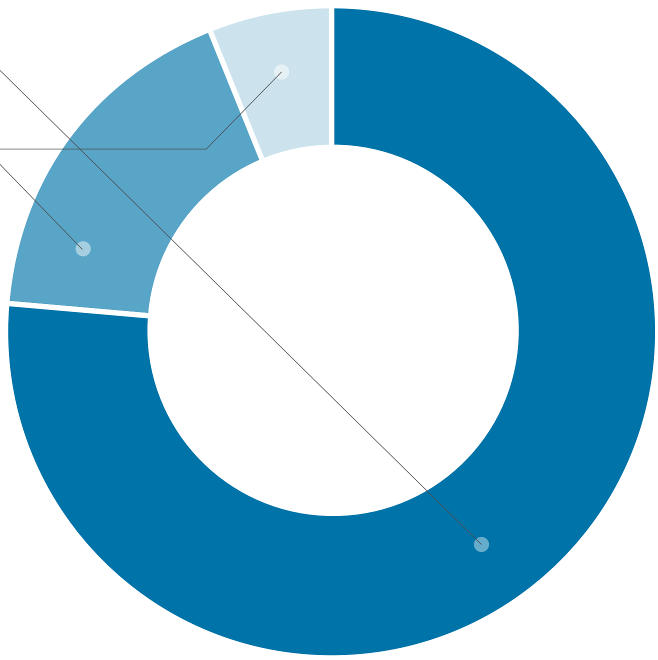
The Swiss Banking Institute of the University of Zurich carried out a written questionnaire (1391 questionnaires were distributed in April 2007) to find out where independent asset managers (IAMs) in Switzerland see the problems and challenges of their industry both today and in the future and the changes they anticipate.

The sample covered all language regions of Switzerland. Figure 1 gives an overview of the responses from which the information in this study was taken.

Figure 1:

Overview of response rate

Region	Responses	Return rate
German-speaking Switzerland	233	24.3 %
French-speaking Switzerland	54	15.7 %
Italian-speaking Switzerland	18	20.2 %
Total Switzerland	**305**	**21.9 %**

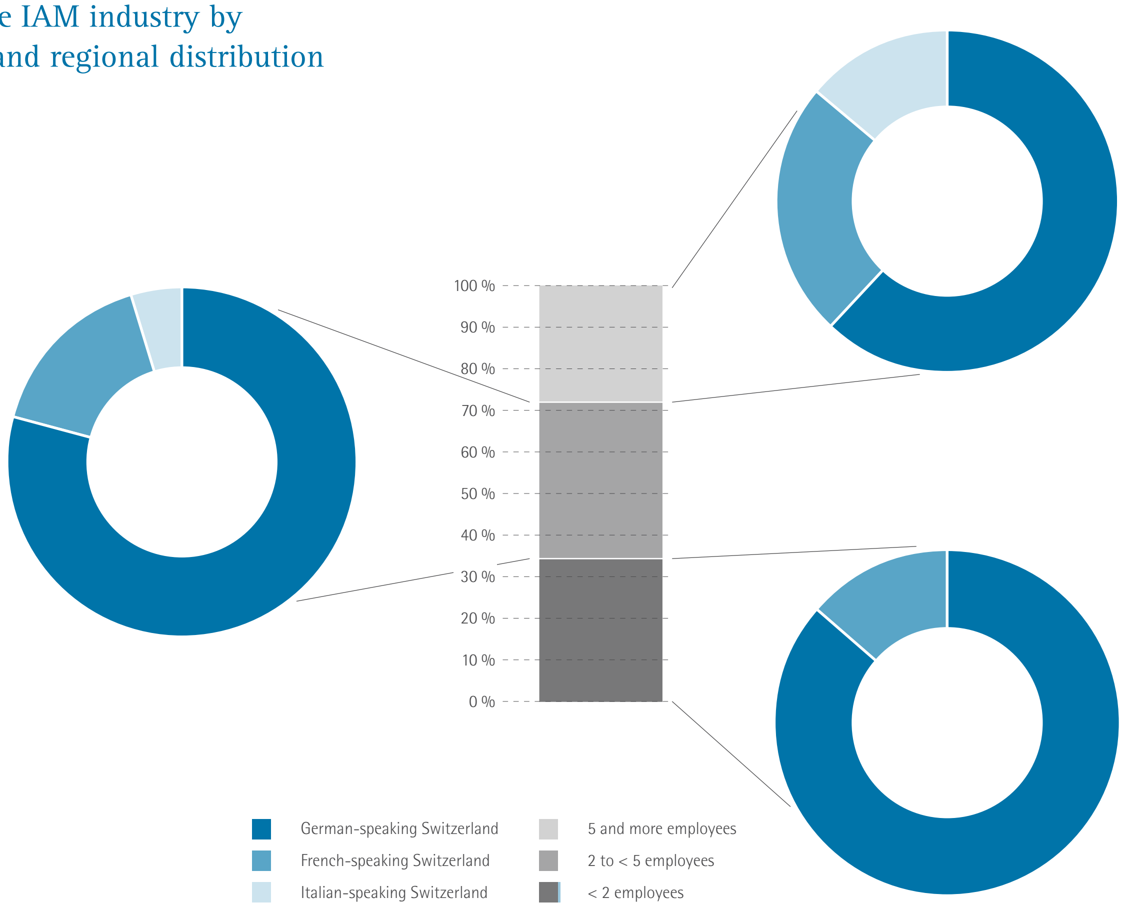


Structure and typology of the industry

It would seem that a small company size is in the nature of independent asset management. One third of IAMs registered with the Swiss Commercial Registry Office (HR) have less than two full-time employees. Another third employs two to less than five people and the rest of IAMs have five or more full-time workers.

As regards regional distribution, one person companies are most frequently found in German-speaking Switzerland and larger companies in French-speaking Switzerland and Italian-speaking Switzerland (cf. Figure 2).

Figure 2:
Overview of the IAM industry by company size and regional distribution

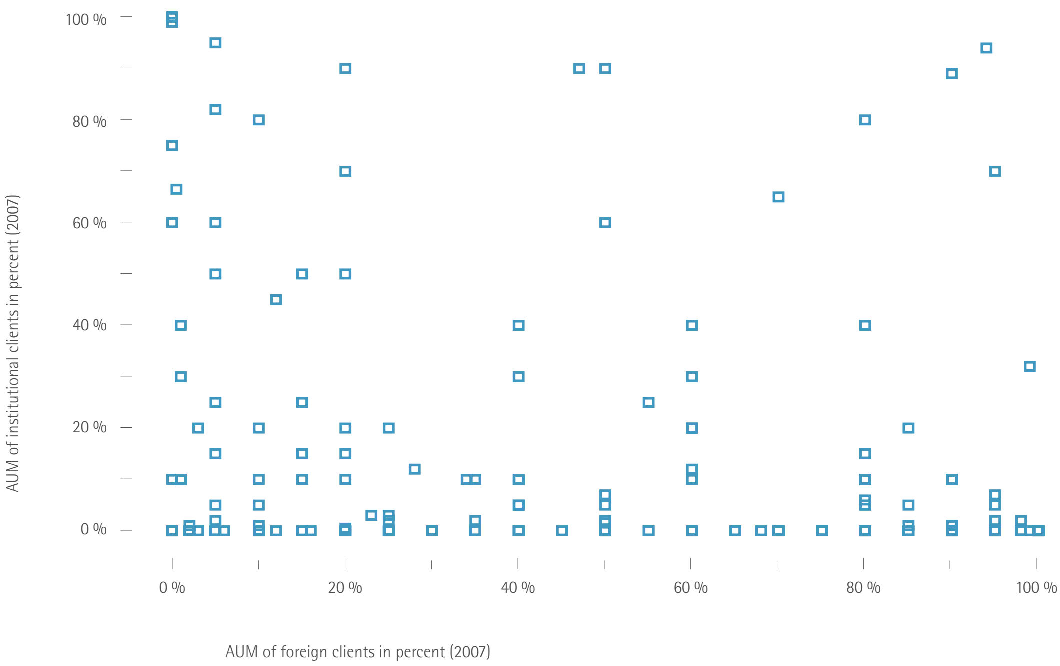


If one positions companies according to their client portfolio, a rather clear picture emerges (cf. Figure 3). Business with institutional clients seems the exception: Over 60% of IAMs have only private clients (cf. also Figure 16, Appendix).

A more varied result is shown in an analysis of the origin of clients. Around 10% of IAMs have client relationships with either only foreign or only Swiss clients respectively. The average percentage of foreign assets under management (AUM) is 53%, the median is 60% (cf. also Figure 17, Appendix).

Figure 3:

Positioning of respondents by composition of assets under management



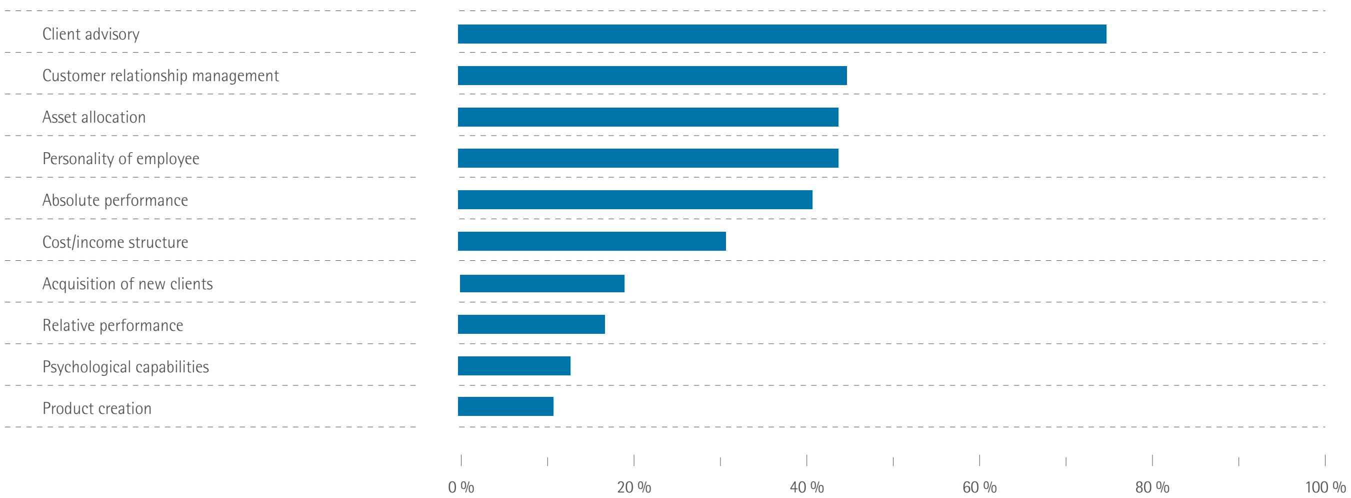
Structure and typology of the industry

Independent asset managers know exactly where their strengths lie. Thus, advisory services are at the top of the list of core competences mentioned (cf. Figure 4).

In second place is customer relationship management and in third place asset allocation is given. The latter is an investment-technical aspect which can impact investment performance. Soft skills dominate the business.

Figure 4:

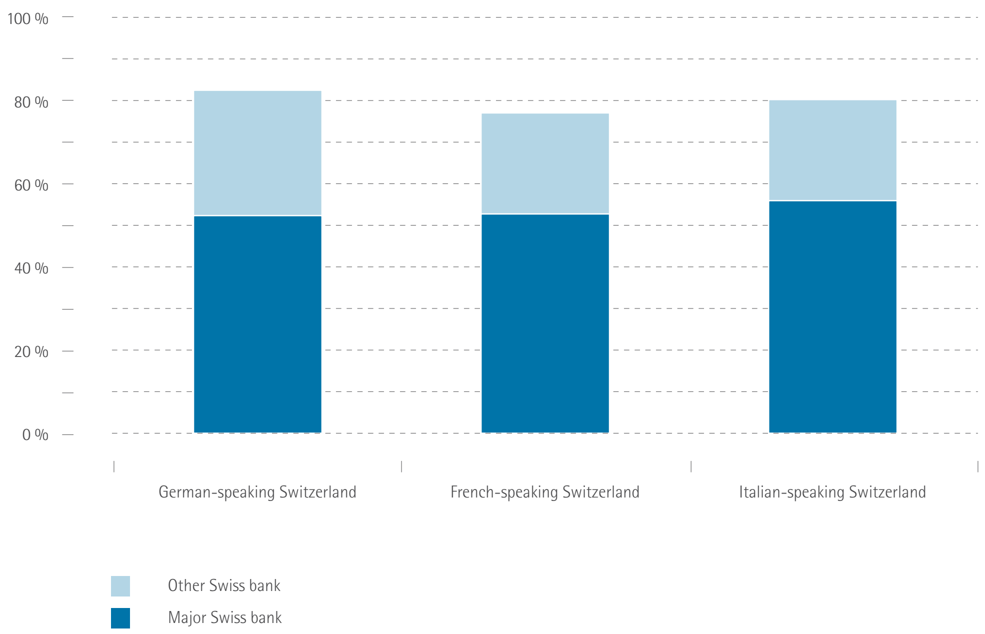
Self-assessment of entrepreneurial core competencies



The skills shown in Figure 4 are in most cases acquired at Swiss banks – principally major Swiss banks. Thus, around 80% of independent asset managers are former bank employees (cf. Figure 5). One can therefore assume that the majority of IAM clients used to have their assets managed by a bank.

Figure 5:

Professional background of independent asset managers



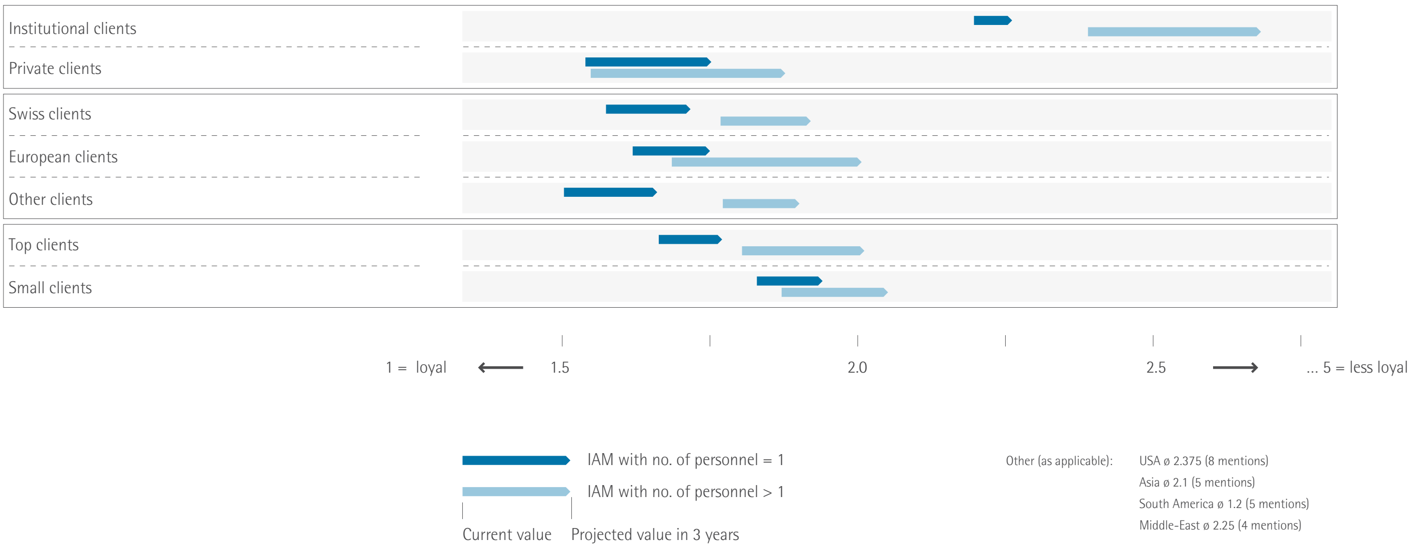
Client characteristics and behavior

The general prognosis regarding developments in client loyalty is rather gloomy. The industry anticipates a decrease in client loyalty in all segments over the next three years (cf. Figure 6). In principle it can be shown that one-person companies consider their clients more loyal than do larger companies.

This is no surprise as IAM clients seem most interested in a one-to-one relationship and personal advisory services. However, whether one could venture a theory that with increasing company size, client loyalty is generally on the decrease is questionable. It is prudent at this point to mention that data is based on respondents' qualitative estimates.

Institutional clients are considered least loyal. On the one hand, these client relationships can be characterized by more quantitative elements such as investment performance or pricing. On the other hand, most IAMs clearly focus on wealthy private clients and therefore have limited know-how which would allow them to address and service institutional client needs.

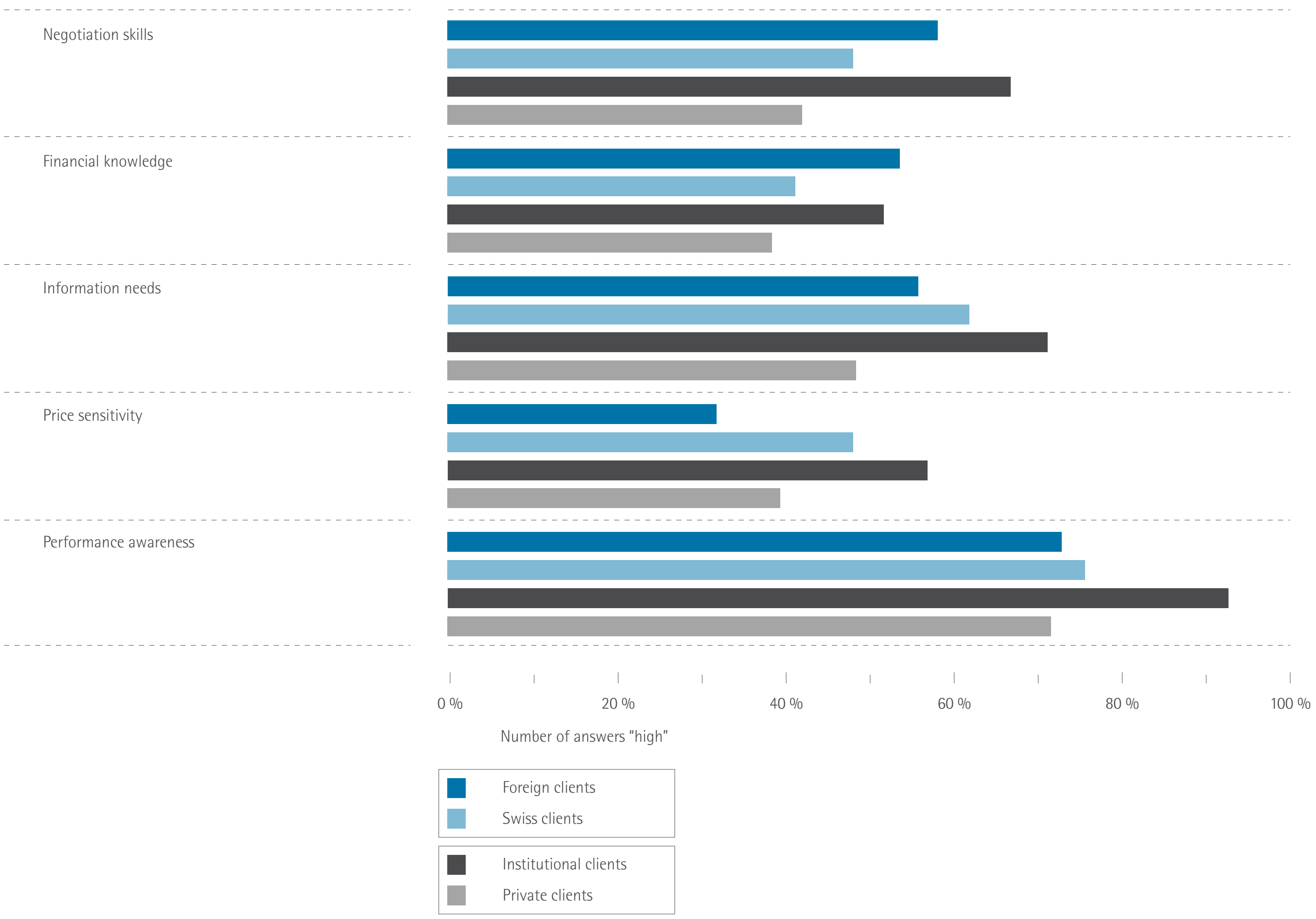
Figure 6:
Trends in client loyalty



Of interest is the discovery that top clients (the wealthiest 20% of IAM clients) are considered more loyal than less wealthy clients (the least wealthy 20% of IAM clients). This can doubtless be explained by the higher costs involved in a change. At the same time one can say that clients with increasing confidence in services seem to increase their "Share of Wallet" with their IAM. Thus, long-term these clients become top clients. The IAM's top clients are generally given most attention which also increases confidence.

Figure 7 shows how certain client segments are assessed according to various economic characteristics. It is hardly surprising that institutional clients dominate other client segments as regards these characteristics. The characteristic where foreign clients take the lead is with financial knowledge. The latter are also less price-sensitive. It seems that in most cases lucrative net yields can be earned with tax advantages despite high administrative costs.

Figure 7:
IAM assessment of various client segments

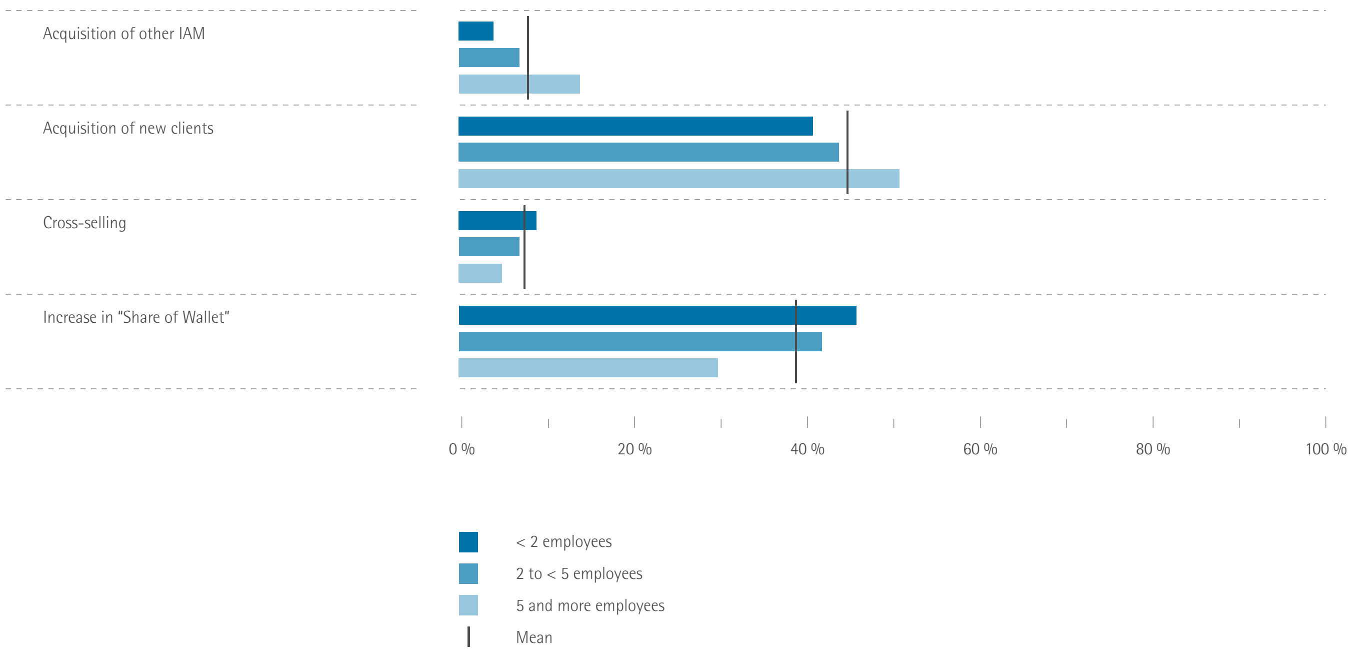


Growth

An increase in managed assets in the IAM industry is generally strived for by increasing the "Share of Wallet" of existing clients or via client acquisition (cf. Figure 8). Further development and the deepening of existing client relationships is the dominant growth strategy of smaller IAMs in particular. Cost advantages in comparison with alternative growth opportunities seem to play an important role here, acquisition of new clients is of course significantly more expensive.

Growth by acquisition of other IAMs is an important alternative particularly for larger IAMs. Through acquisition, the latter strive towards a consolidation of the industry.

Figure 8:
Assessment of strategic importance of specific growth drivers



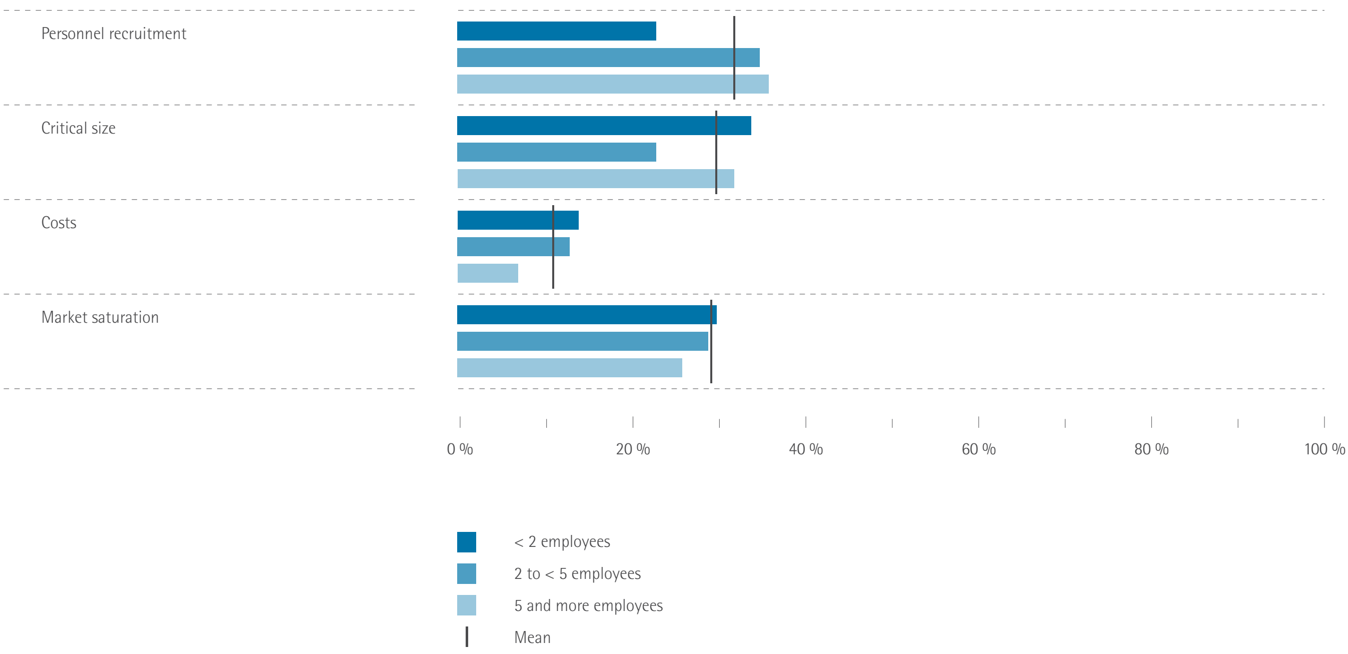
A particular threat to the sustainable growth of the industry appears to be the difficulty of drawing talent with attractive working conditions and pecuniary incentives, and being able to keep them (cf. Figure 9). However, this could be a cyclical phenomenon as the alternative employer – the bank – is currently in a position to make very attractive remuneration packages due to the excellent development of stock markets.

Perceived market saturation is deemed an indicator for an emerging consolidation. Additionally, the perceived zenith which the Swiss financial centre sees in its skill in attracting foreign money would make itself felt on the market (cf. also Figure 12).

Also striking is that critical size is perceived as a growth impediment. Investments which would in many cases be necessary for a growth strategy do not seem financially viable for many IAMs. Seen from this perspective, providers with the advantage of size could tap into attractive growth potential.

Figure 9:

Assessment of the relevance of certain growth impediments for the individual IAMs

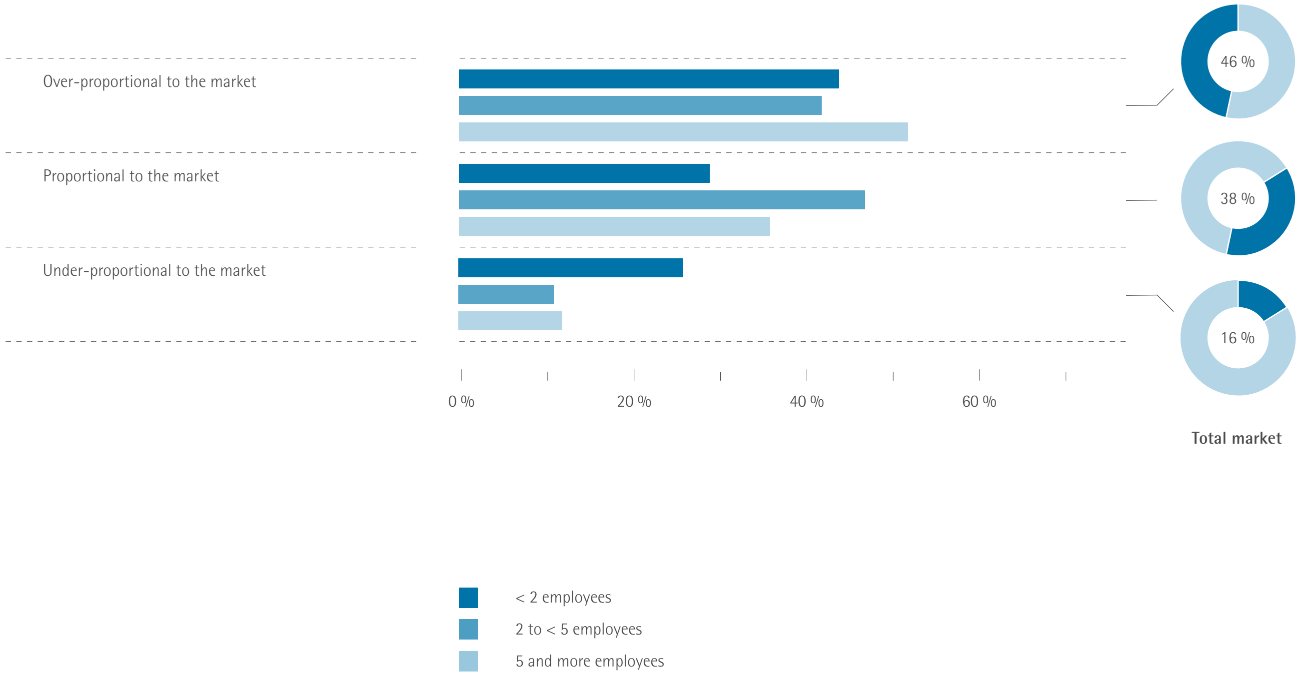


Growth

A large number of respondents see a growing demand for independent asset management in Switzerland from private clients. Latent market potential has evidently been detected. Growth opportunities are certainly identifiable; however, it would seem that it is large IAMs in particular who think their skills sufficient to be able to seize these opportunities. These IAMs are thus expecting above-average growth. Small IAMs, on the other hand, assess their growth potential much more pessimistically and assume less than average growth (cf. Figure 10).

A dichotomous development would appear to result: Small companies will stay small and large companies will become larger. It is important to note, however, that the nature of asset management enables existence without growth. This is due to the special price model (fixed fee dependent on portfolio volume) which guarantees a constant source of income. Therefore growth in the IAM industry is not as vital as in other sectors as long as a minimal client volume is reached.

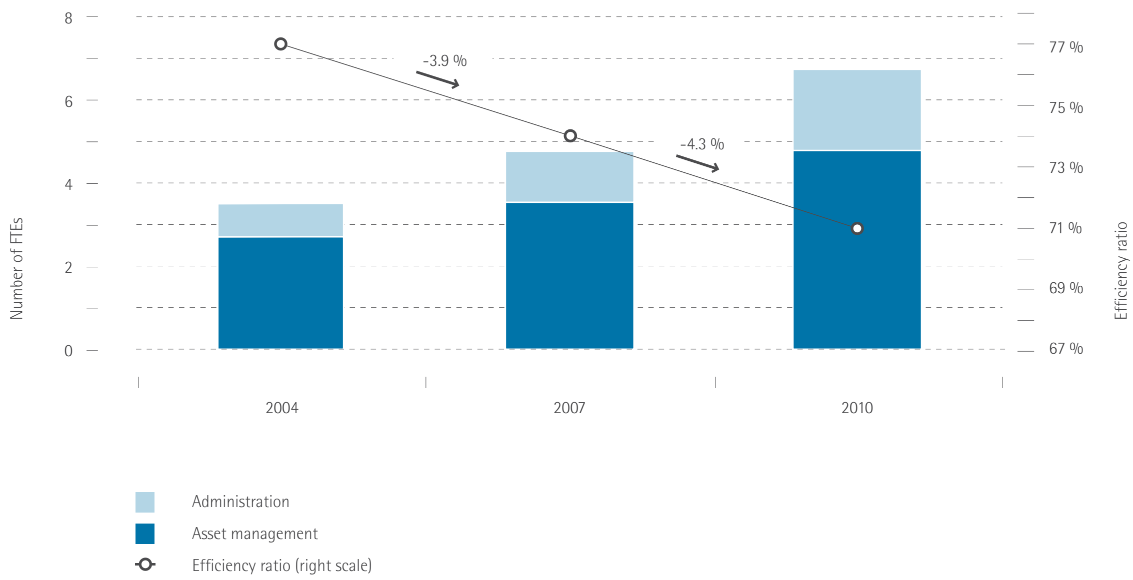
Figure 10:
Assessment of growth in the individual IAMs in comparison to entire market



It must come as a surprise to the industry to discover that the most significant anticipated increase in personnel is expected in administration (particularly regulation) and only to a small extent in asset management (cf. Figure 11). Such a development would rather result in a significant worsening of IAM operating efficiency and therefore underpins the apprehension that increasing regulation would increase (administrative) costs. The industry assumes that in 2010 an IAM has on average 6.7 employees (FTEs) of which 4.8 employees (FTEs) are credited directly to asset management.

Figure 11:

Development of number of employees and operating efficiency of an average IAM (FTE: Full time equivalent)



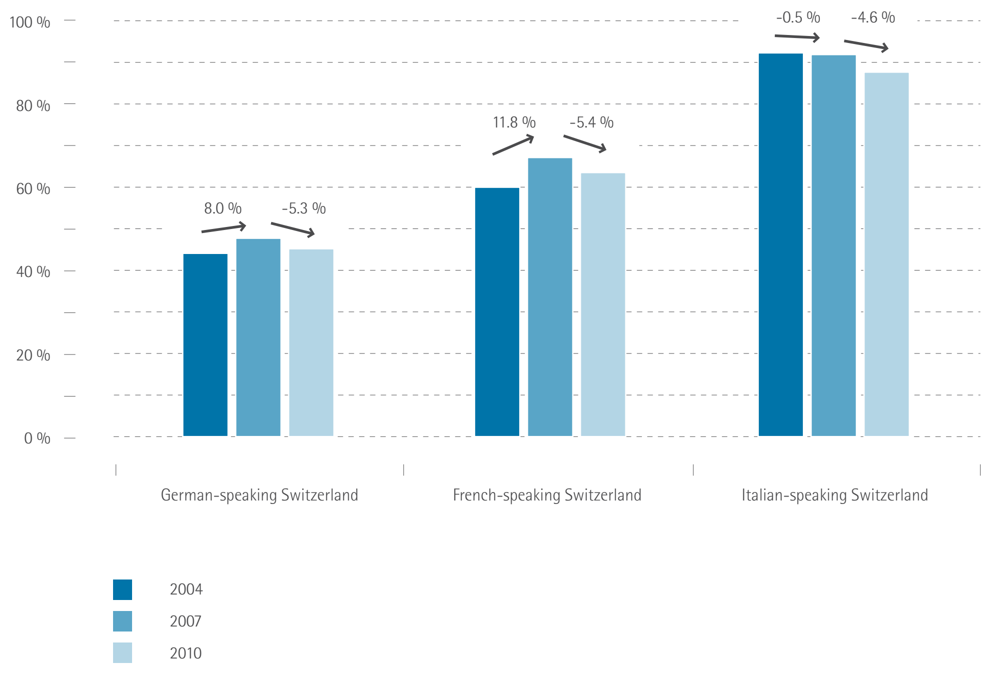
Growth

Of paramount importance for the financial centre are questions relating to the development of the foreign client segment. Figure 12 illustrates this importance for IAMs, although also here one cannot speak of a homogenous industry – there are IAMs for which the number of foreign clients is of no importance (cf. Figure 17, Appendix).

IAMs in the Italian-speaking part of Switzerland are particularly dependent on foreign money. Here 90% of clients come from outside Switzerland. Striking is therefore that one would generally anticipate a reduction in the importance of foreign clients. Although this should not lead directly to a drain on funds, a continuous inflow of money from abroad can no longer be expected.

Figure 12:

Development of foreign AUM against entire AUM of an average IAM



This development hits IAMs harder, for instance, than the banking world. The latter make up for part of these losses with onshore activities in the home markets of clients. In this case the lack of size is fatal for IAMs: Expansion strategies abroad with the associated costs and enormous risks are not within the reach of most companies.

Trends

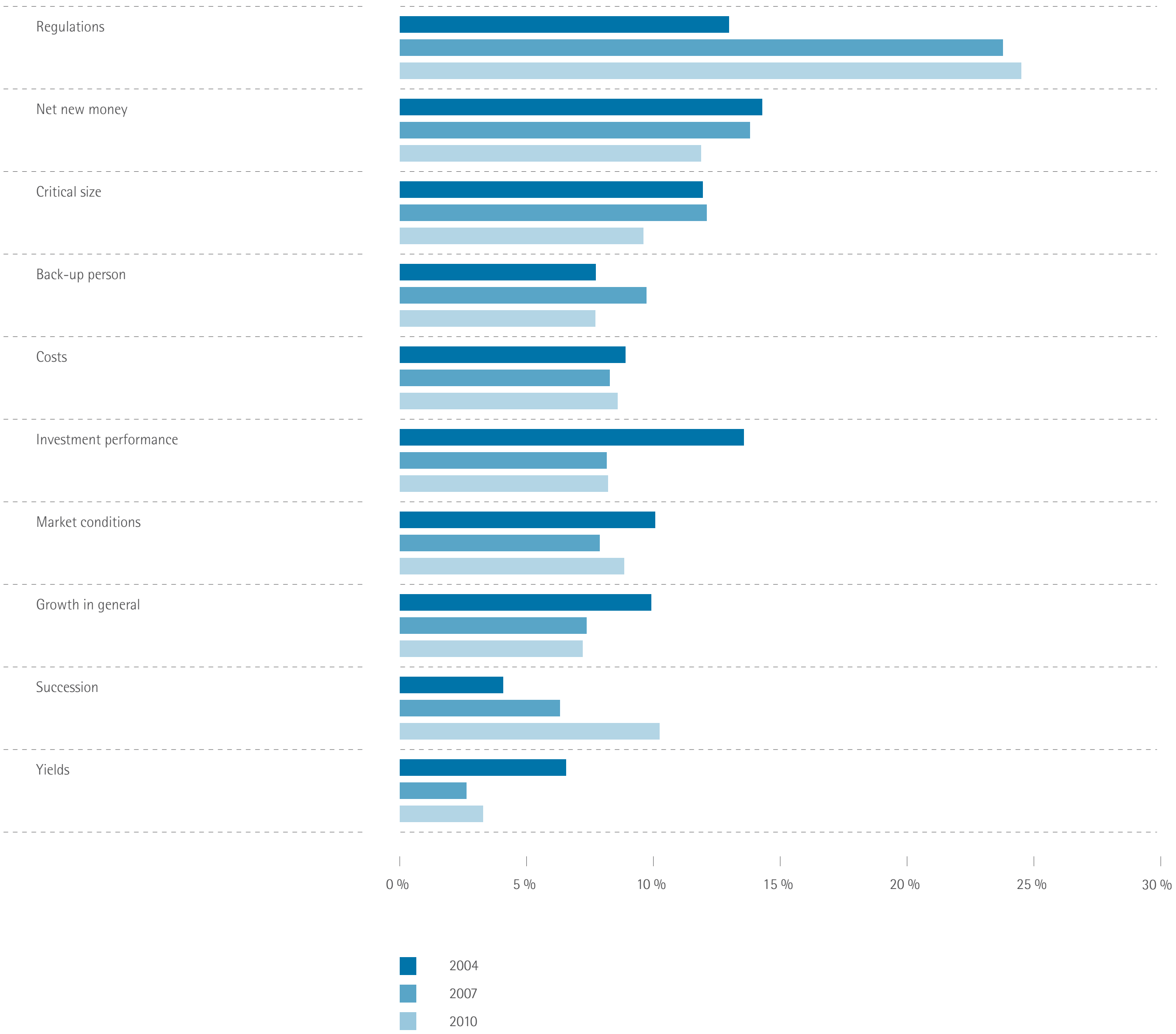
Issues that will increasingly attract the attention of IAMs in the coming years are clearly identifiable: Regulation, costs and succession.

The regulatory aspect is doubtless closely connected to the cost issue, whereby the latter is intensified by developments in IT. Many IAMs may have delayed making the necessary investments (even a Web presence, now considered a necessity, is far from professional for most IAMs) and are faced with significant investments. For portfolio management, reporting or online access to accounts, technically mature solutions are available and expected by clients but require massive investment. Additionally, multifaceted solutions for the entire area of business process outsourcing are available today which, however, would require long-term planning (whether all IAMs have the necessary time left to amortize such investments is doubtful). One should also not disregard the stealthy development of increasing complexity in products, systems and solutions, which lead to sustained cost pressure.

Regulation is still considered a stumbling block by IAMs and the rest of the financial sector. Three quarters of IAMs assume that the industry will lose some of its attraction because of further regulation over the next years. The fact that requirements in this area have increased over the past few years should not be dismissed. However, one should not disregard the fact that this has also occurred to protect the industry itself. A certain amount of discomfort is unavoidable. Important seems that the surge in regulation should not become a permanent condition. An accentuation in the increase of regulatory requirements carries the danger that the IAM business becomes lastingly unattractive. The authors detect sensitivity in the regulators to these problems; however respondents view this (still) as doubtful.

Figure 13 shows an overview of the most frequently named problems in the industry over time. To keep the balance between the optimists and pessimists, respondents where asked to name three issues for each year given. Regulation is currently the most pressing subject. The industry also assumes that the problem will not lessen over the next three years which is the case, for example, for critical size.

Figure 13:
Overview of certain problems and challenges in the IAM industry over time



Looking back in time shows that new money and investment performance in the years following the Internet bubble were the dominant issues. The extremely poor performance figures during this time not only led to a general disgruntlement in clients. From a psychological perspective, the problems were also a challenge for asset managers because of their close relationship to their clients. New money acquisition was extremely difficult in this phase (as it was for the entire financial sector) and the prospect of new clients was overshadowed. Investment performance is not currently an issue (hardly surprising in one of the longest bull markets of the last few decades), but will of course quickly reappear in worsening market conditions.

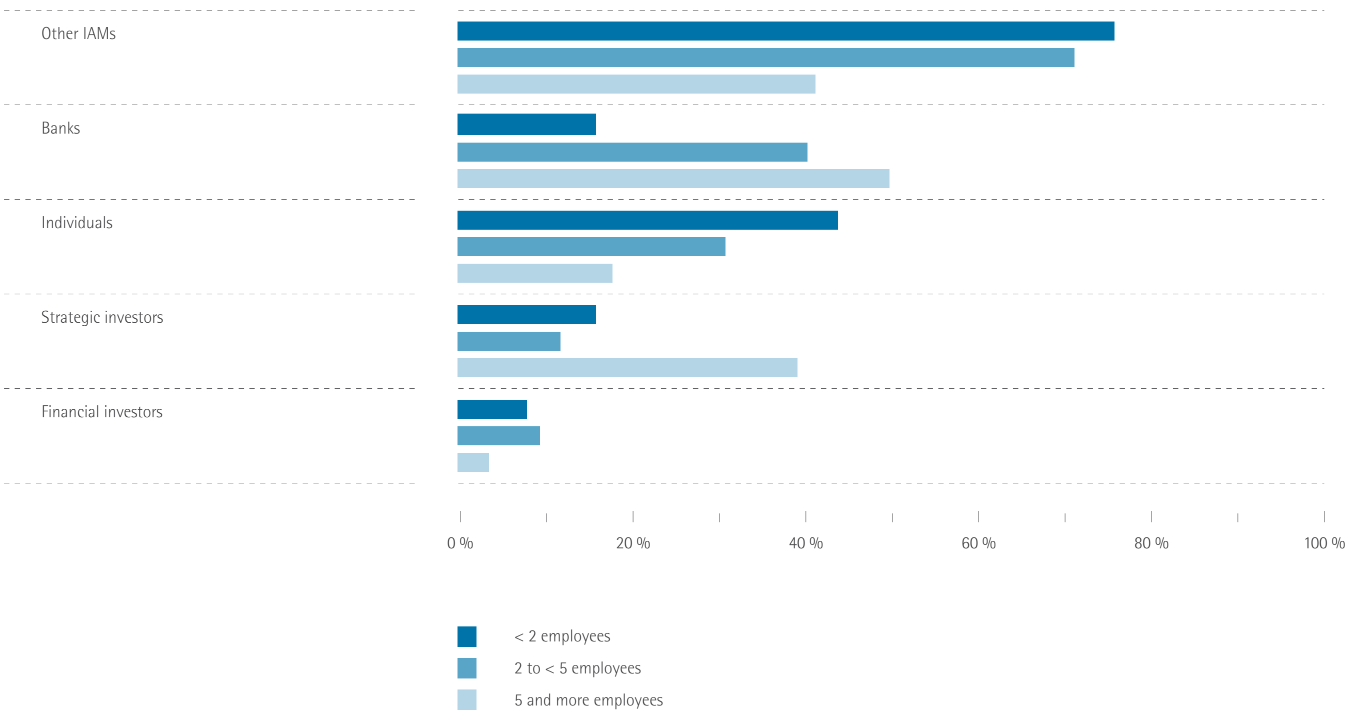
Succession is the real "leader" of the problem areas. In the coming three years, this aspect is one of the serious challenges. In an industry strongly characterized by individuals, where the problem of succession poses a "natural" challenge, it is only surprising that the problem was not considered an issue earlier. To what extent a psychological crowding-out effect plays a role can only be guessed at.

The fact is that this problem is on a collision course with the industry and will lead to a fundamental change in its structure. As the problem of succession will soon accumulate in the industry, early solutions to these questions will bring important advantages to "early movers": What happens on markets when everyone wants to use the same door at the same time is plainly demonstrated to investors time and time again.

Trends

As regards the notion of an ideal or suitable buyer for independent asset managers, it can be seen that with small companies emotional reasons are often dominant, or that holding on to conventional business strategies is a priority. These companies therefore prefer individuals or other IAMs as buyers. This stands in contrast with larger companies who favor banks or strategic investors. Figure 14 shows the type of successor preferred by the individual companies.

Figure 14:
Overview of preferred buyers by size of individual IAM



The industry is therefore looking towards a phase of increasing competition, competition which will probably intensify as soon as the current stability on capital markets decreases. The question of critical company size in the future is possibly more complex than even industry representatives anticipate. The trend here to an increase in critical company size should evolve out of the operating constants just with the increase in fix costs. However, striking is that amongst the IAMs heterogeneous models do exist.

In certain cases, it seems that it is small structures which are most efficient. Thus, the IAM industry is rather characterized by a dichotomous tendency of "away from the middle". On the one hand, this would speak in favor of a continuation of small structures and, on the other hand, for an increase in size for middle-sized structures. The anticipated consolidation would then come about for middle-sized IAMs in particular.

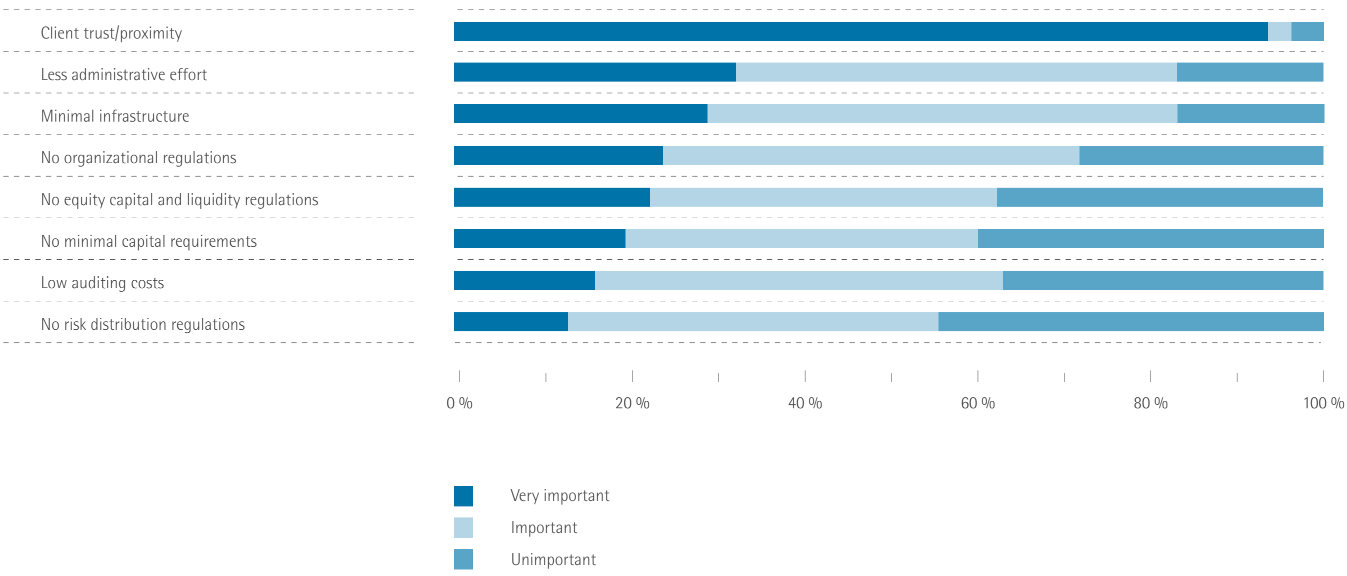
Regulation

Regulation has emerged as the largest current problem area for IAMs. For this reason, a number of more detailed questions were asked. Of particular interest is to what extend the advantages or disadvantages of alternatives are assessed, e.g. the choice of securities dealer status (the status closest to that of the IAM). In principle the main difference in comparison with a securities dealer is seen as the more intense relationship to the client which is far more dominant in IAMs (cf. Figure 15).

This is, however, a question of strategic positioning which is not given per se by the regulatory status. As also became clear from other answers in this study, the client relationship is the fundament from which the industry takes its image.

On a more factual-quantitative level, responses suggest that the regulatory corset worn by the securities dealer is not attractive for IAMs. In particular, the increased administrative and organizational effort is viewed as obstructive.

Figure 15:
Assessment of various regulatory advantages of the IAM compared with the securities dealer



It is therefore hardly surprising that only 5% of IAMs would consider the possibility of a change to securities dealer status and only 3% the transformation to the status of a bank. Although from a regulatory point of view, closer supervision appears preferable, it can be determined that IAMs currently see no suitable and realistic alternative to their regulatory status. From a business policy perspective, the incentives for a change of status seem too small: IAMs do not see a better reputation with clients through stricter supervision as a securities dealer. Only being subject to the banking and professional secrecy act and easier access to European clients are seen as being clear advantages for securities dealers and banks.

Appendix

Figure 16:
Distribution of IAMs by AUM of institutional clients

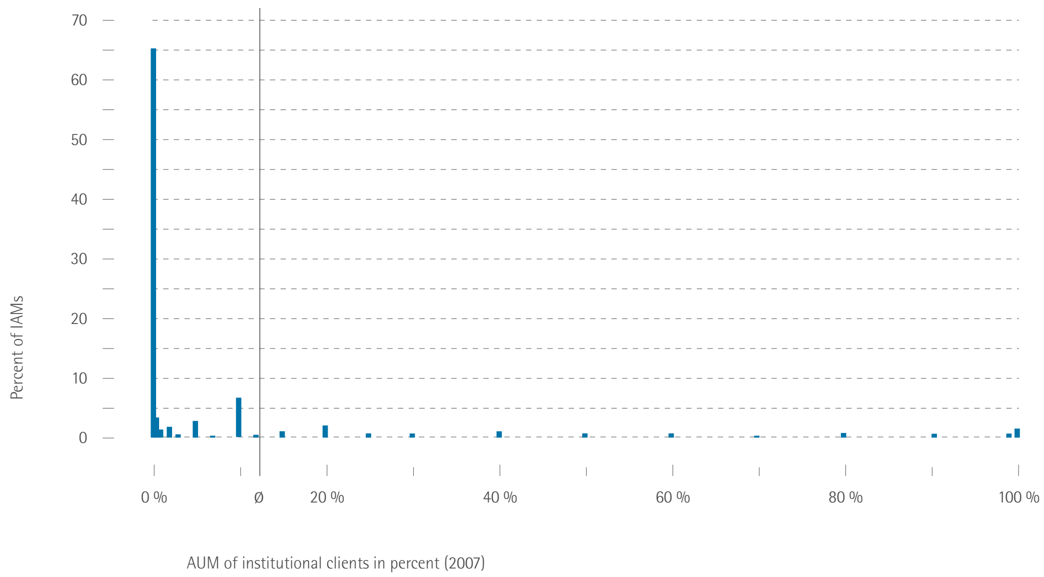


Figure 17:
Distribution of IAMs by AUM of foreign clients