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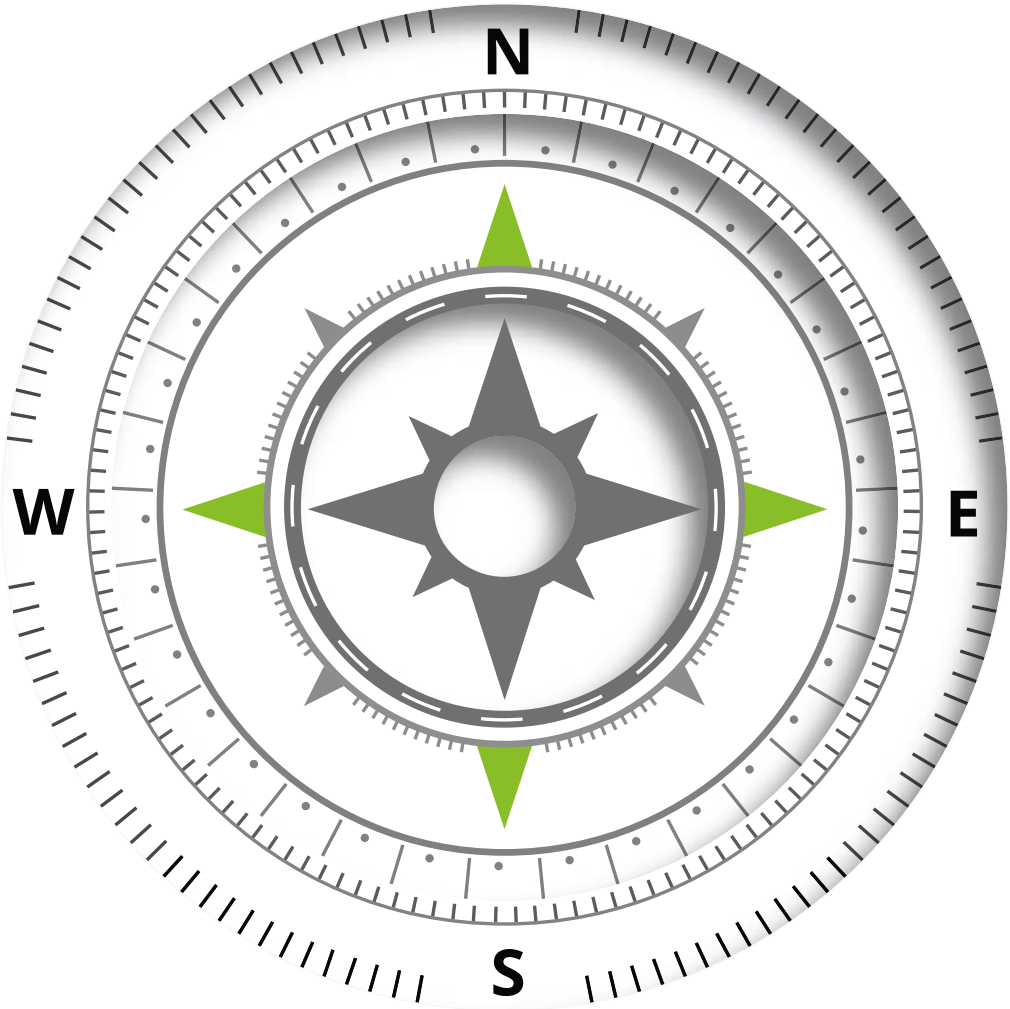

Future of Distribution in Asset Management

How Impact & Innovation Win
on a Price & Product Playing Field
December 2021

Digitalization, sustainability, novel ways of working and an increasing number of client conscious customers have triggered massive changes in the way companies manage their distribution departments in almost every industry. For asset management companies to tackle the many challenges arising from these trends and succeed in turning them into competitive advantages, sales staff will have to undergo radical change as well. Both retail and institutional sales teams must reinvent their distribution strategy using new channels and products as well as focusing on internal challenges, such as how to make intelligent use of automation and optimize their sales and remuneration systems. Considering the pressure on small to medium-sized asset managers from deteriorating margins and increasing consolidation, the speed of transformation and the associated cost concerns may quickly become a matter of survival.

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Leading asset managers focus on expanding their ecosystems and entering into partnerships for both retail and institutional sales

New Channels

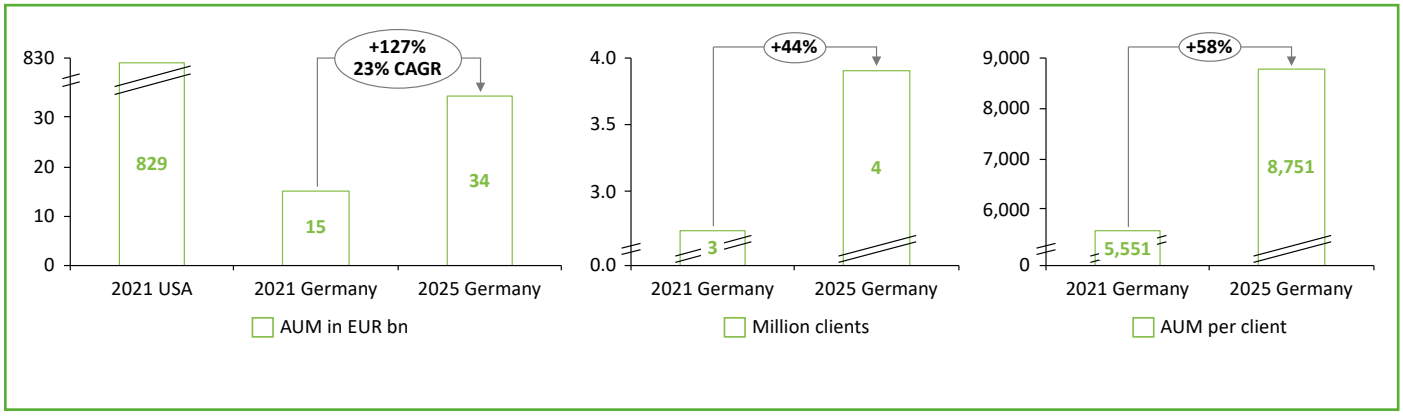


Figure 1: AUM managed by robo-advisors in USA and Germany and expected growth of client and AUM until 2025 (Statista) (Source: Deloitte 2021, Statista 2021)

With an ever-increasing number of digital investment platforms and FinTechs entering the market for retail investors, asset managers have started reviewing and innovating their retail distribution strategies. AUM by robo-advisors are expected to increase by 86 percent to €15bn in 2021, with an additional 23 percent increase in each of the next four years. Compared to US firms, however, this is still a low figure, despite an expected 46 percent growth in the client base and a whopping 86 percent growth in investment per client during the same period. While most investment firms have already set up in-house robo-advisors over the past three to five years, new market entrants have succeeded in capturing market share by creating customized client experiences for their target groups.

The robo-advisors that entered the market early with a more standardized offering used to struggle with profitability issues due to low AUM levels. Now they face a situation where AUM levels are rising, but they are unable to capture the full market potential. By contrast, target-group-oriented robo-advisors with customized client offerings and dynamic portfolio optimization that anticipates market movements have succeeded, as seen in first quarter of 2020. It is no surprise that consolidation started to gain traction in 2020, as market share became increasingly scattered. Asset managers need to make their robo-advisors more competitive to capture market share in this growing market.

In addition to digital distribution channels, both retail and institutional sales teams are too reliant on selling their own funds and excelling with in-house expertise. They risk losing retail clients to open, independent and more transparent platforms. Institutional clients may, on the other hand, take their assets to more competitive providers. Regardless of the industry, companies that are willing to embrace a broader ecosystem will succeed in strengthening their overall competitive position, as Deloitte Insights demonstrated in an analysis from 2021

There is also huge untapped potential in partnerships with major market participants outside the financial industry. Only a few innovative investment firms have taken this path so far.

It can be challenging to identify eligible cooperation partners, and an ill-advised partner can result in a negative brand impact and opportunity costs. Industries from insurance, travel and mobility to health care and retail lend themselves particularly well to partnerships, as they have a large client base of target customers that may also be in the market for saving and investment solutions. However, choosing the right partner will depend on the particular market position and situation of each asset management firm, and may vary in terms of size, investment focus, brand value, client base and more. There are four partner archetypes with increasing levels of maturity, ranging from a Selling Ally to a Cocreator, and each asset manager will have to find the model that fits best for their sales strategy.

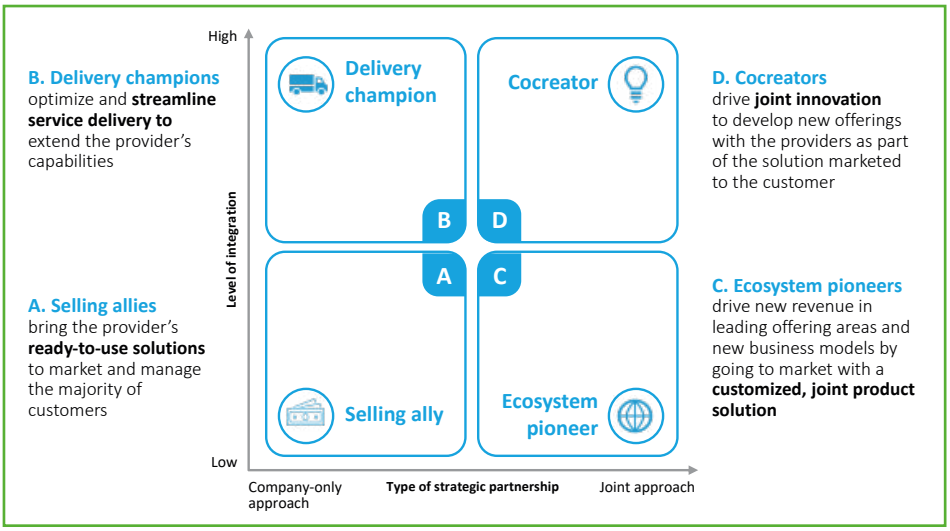


Figure 2: Partner archetypes and movement between partners, Deloitte. (Source: Deloitte Insights 2020)

The dawn of new products and the need for action

New Assets

Crypto assets, and cryptocurrencies in particular, are a hot topic today, and even though they remain extremely volatile, it is hard to imagine a world without them. These products do not only get a lot of coverage in the media, but there is also a record number of investors chasing highs in trading volumes of digital currencies. Studies confirm that the younger generation of retail investors (e.g., GenY and GenZ) have a high willingness and desire to invest in cryptocurrencies. That means crypto products are likely to become an integral part of the investment universe for the next generation of investors.

More recently, an increasing number of institutional investors are also considering investing in crypto currencies. Positive momentum in the regulation of this entirely new market is driving this trend, with alternative investment funds permitted to include up to twenty percent of these assets since July 2021. Furthermore, uncertainty around taxation of cryptocurrencies and other digital currencies is expected to improve since the EU-commission will include them in their action plan for automated exchange of information in its Directive on Administrative Cooperation (DAC8) to achieve fair and equitable taxation.

While total global cryptocurrencies' market capitalisation versus leading global indices including gold remains small, it is catching up with European indices and both, asset managers as well as investors will closely watch its future growth. Additionally, asset managers and institutional investors have started to assess benefits of tokenized real assets and securities and respective demand is evolving.

Cryptocurrencies, however, are not the only novel investment products being championed by a new generation of customers. We are also seeing an ever-increasing interest in and passion for "green" products across different generations of retail and institutional investors, making ESG criteria the new standard for investing. Apart from merely catching up with current trends, firms stand to gain valuable experience by integrating cryptocurrencies and ESG-optimized investment strategies into their existing investment products. This is particularly relevant for today's asset managers, as we can expect new financial product innovations to emerge with increasing frequency as future investors frantically search for above-market returns. Asset managers who are willing and able to become early adopters of these trends will have an advantage over larger competitors and may potentially be able to tap into the very lucrative customer group of younger risk-seeking and trend-driven investors.

As we see it, these changes in investment philosophy will have far-reaching consequences for the distribution strategies of asset managers, and immediate action is required to build competitive edge for the future. Sales divisions need a deeper understanding of how crypto investments, tokenization and ESG investing will impact their current value chain, and they must be able to explain and solve any apparent contradictions for their clients. That means a dedicated training strategy regarding investor education, advice and communications to enable sales professionals to offer tailored investment solutions aligned with investor preferences in terms of crypto, ESG and any new investment products that will inevitably emerge in the future.

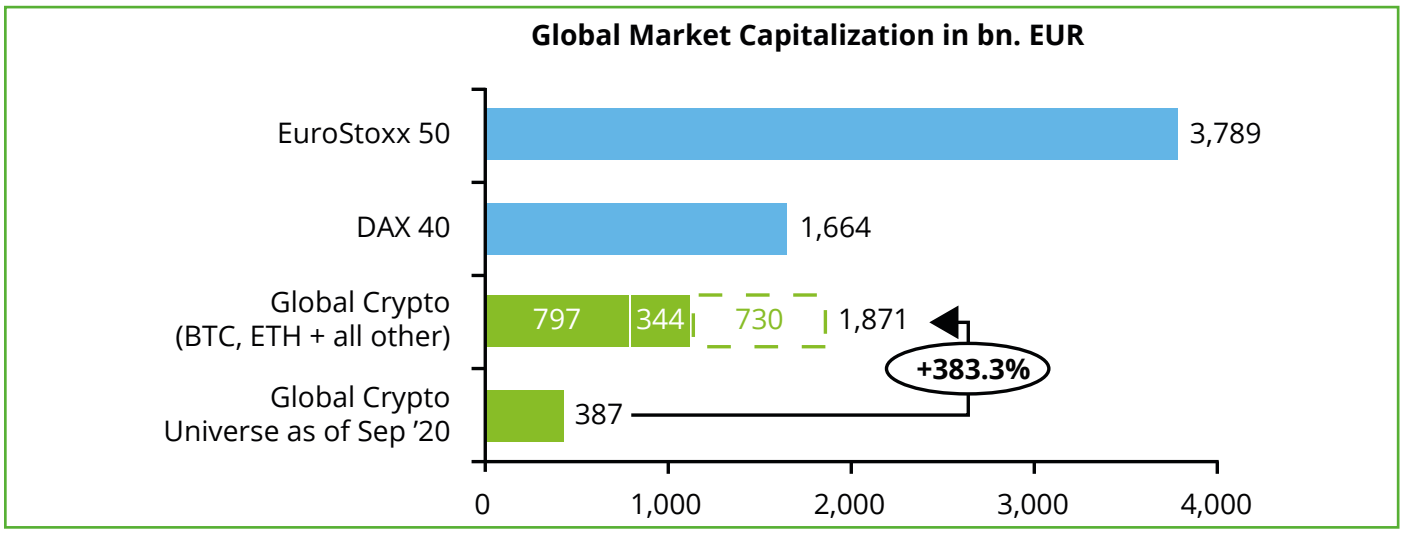


Figure 3: Total Cryptocurrency Market Capitalization has grown by over 380 percent and has surpassed the DAX within last twelve months (Source: Deloitte, Boerse, Coinmarketcap, Sep, 22nd 2021)

ESG integration has become a prerequisite for successful distribution teams

ESG

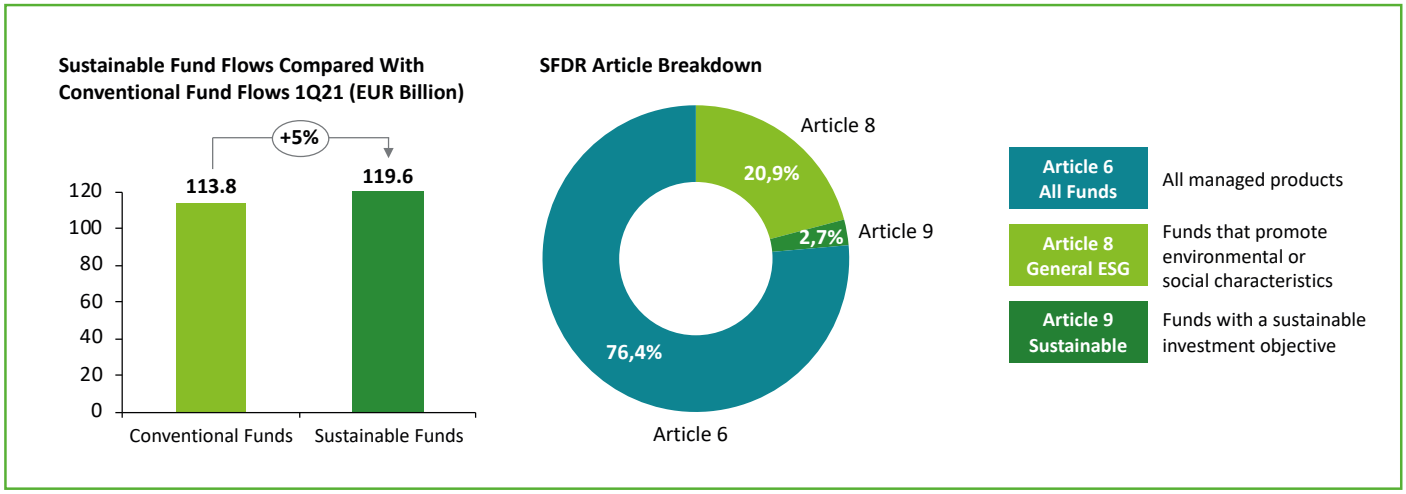


Figure 4: ESG-related funds are becoming more and more mainstream (Source: Morningstar Direct, Manager Research, April 2021)

The huge growth in and demand for sustainable investments is not only reflected in a massive increase in sustainable AUMs, but also in customer behavior. Asset management firms welcome the trend of multi-generational customers integrating sustainability not only in their own lives, but also in their financial decisions. For both retail and institutional clients, asset managers have started to develop and implement ESG strategies to a transformative degree – ESG has become one of the most relevant aspects for asset managers thinking about their future distribution strategies.

Investments with an ESG strategy designed and implemented across portfolios are becoming standard, although firms may find that offering a "bouquet" of individual solutions will help differentiate their products, especially in terms of sales. Investors' demand for information is not only focused on investment opportunities, but also on the asset manager's own overall ESG goals. They want comprehensive information about the latest developments, trends and dynamics as well as political and social developments that will not only contribute to but also support their investment decisions. They want to be kept up to date with the latest ESG developments of their holdings, so that they are well-equipped to make decisions about monitoring, categorization and expectations. Providing customers with tailored ESG intelligence can be an incredible differentiator for sales departments in asset management firms.
Investors are also increasingly interested in the ways environmental, social and governance metrics can be incorporated into asset monitoring. Particularly for institutional investors with unique investment requirements, asset managers benefit from having analytical tools for dynamic modelling of changes to ESG profiles (e.g., when regulatory requirements change) as an extension to structural analysis tools – always with the overall goal of keeping risk-return profiles stable.

With regard to an asset manager's own sustainability targets, less frequent travel is a convenient way for sales divisions to reduce environmental impact and achieve higher ESG goals. However, this is not a particularly effective response relative to the enormity of the challenge, nor is it a particularly far-sighted action in terms of strategy. Morningstar introduced the new ESG commitment level rating in 2020, which measures the extent to which asset managers incorporate ESG factors into their investment processes. According to their own analysis, 40 percent of asset managers achieve a "Basic" score, while another 30 percent were rated "Low". Since then, many competitors have not only accelerated the process of implementing a holistic ESG strategy, but they have already introduced impactful measures. For all those asset managers still at the beginning of the process, the pressure has increased significantly and is likely to have a major impact on their ability to achieve targets, on their brand perception and, ultimately, also on customer satisfaction as well as business success.

Strategy
- Reviewing business model sustainability
- Adapting business strategies
- Measuring impact on risk strategy

Processes
- Integrating sustainability risks into risk-relevant processes
- Certifying and structuring services as well as audit support
- Managing data maintenance and data integration
- Implementing ESG criteria

Audit Services
- Conducting audits of annual financial statements, taking ESG topics into account
- Supporting internal audit departments

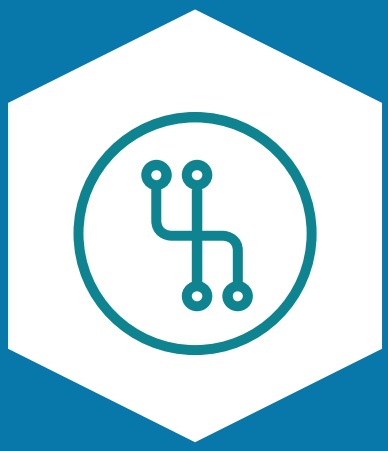
Governance
- Creating one role with overall responsibility, adjusting roles and responsibilities
- Adapting existing organizational structure
- Developing a sustainability framework

Methods & Models
- Quantifying and managing ESG risks
- ESG stress testing of (credit/investment) portfolios; so far mainly climate risks

Reporting
- Product level: Transparency for investors
- Company level: Reporting on non-financial information in accordance with CSR-RUG, GRI Reporting Standards and TCFD requirements

Digitalization paves the way to superior client interaction through artificial intelligence

Digitalization



Natural Language Processing (NLP) & Natural Language Generation (NLG)	Analyzes and understands natural language. NLP thus provides a basis to capture, process and structure textual data for its application within ML models. Generates textual content for use and consumption by human readers.
Domain-enriched Machine Learning	In highly complex domains such as financial markets, human domain knowledge or expert knowledge improve the learning process of ML technologies.
Connection of knowledge	Knowledge graphs use data from different sources to create a network that comprises entities, their semantic types, properties, and the relationships between entities.
"White-boxing" machine learning models	The transparency and interpretability of algorithms is key, mainly due to regulatory demands and a desire to inspire trust in the ML models among human users. Recent research provides methods designed to "white-box" complex ML models.
Robotics Process Automation (RPA)	Automate business processes by coding regular, reoccurring procedures. Higher-performing robots operate leaner, less error-prone and less customized processes.

Figure 5: Smart solutions which Deloitte most frequently uses (Source: Deloitte 2021)

Digitalization has created vast opportunities as well as challenges for every segment of an asset manager's value chain. With increasing demand for funds and services online as well as an increasing number of start-up companies with digital platforms, we have seen the digitalization trend accelerate considerably over the last five years. However, we have not yet seen very many firms leverage the opportunities of artificial intelligence. In a Deloitte survey of Germany-based asset managers in 2021, only ten percent of front office respondents reported already using artificial intelligence in front office processes. 25 percent of firms said they plan to invest in smart solutions over the next three years, but compared to other sectors outside the financial industry, that figure is still well below average. A representative global Deloitte survey from 2020 revealed that more than 50 percent of respondents plan to implement smart solutions during the same time horizon. Artificial intelligence (AI) solutions allow asset managers to enhance distribution in three ways:

They can improve and personalize their interaction with retail clients by using chatbots and voice bots. Natural language generation (NLG) tools have paid off particularly for those asset managers who had a solution in place during the first quarter of 2020. The pandemic made a lot of retail investors uneasy and caught some asset managers off guard – who were only able to answer one out of every ten phone calls.

AI-enriched data analytics tools can help asset managers plan meetings with institutional investors more efficiently and reduce meeting preparation time by an impressive 30 percent on average.

Using a client's current investment holdings and general investment objectives as a basis, asset managers can deploy automated tools to select the right products, services and market trends as well as optimizing their client portfolios.

Insights on market trends and products can also be used for proactive outreach to both existing and prospective retail and institutional clients in online communications and client meetings with sales professionals. Thanks to sophisticated screening tools, asset managers can analyze a broad universe of data, news and social media to identify the needs of different target groups, translate them into customized solutions and offer them on the most appropriate distribution channels.

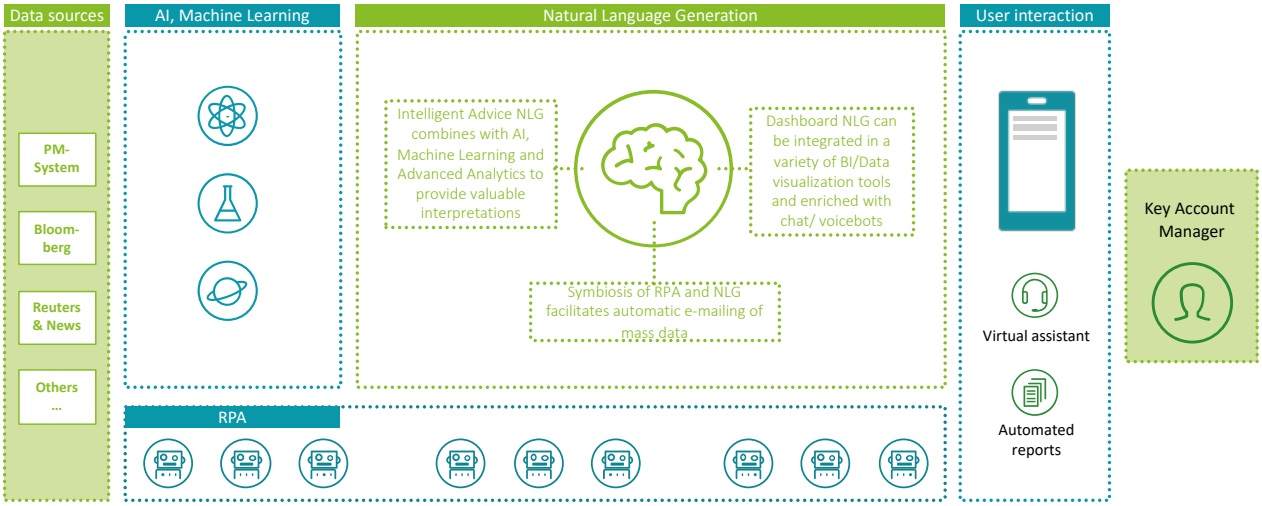


Figure 6: Sales Team Key Account & Market News Podcast (Source: Deloitte 2021)

Sales teams need to transform in line with other shifts in the asset manager's core business

Sales Staff Excellence

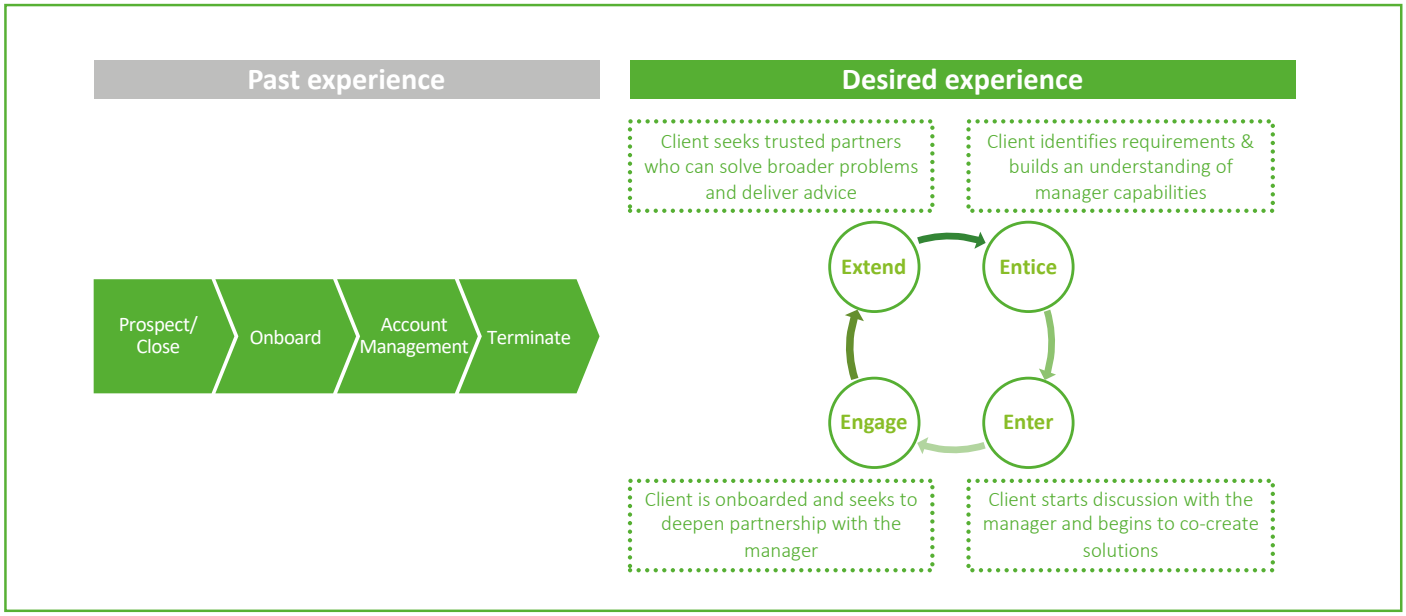


Figure 7: Interactions with clients are bound to become less linear and more continous (Source: Casey Quirk 2021)

With novel distribution channels, offerings and investment philosophies ushering in a new era of asset management, sales staff will have to adapt. Today's hierarchies, incentives and tools may not necessarily work in a world where clients are increasingly expecting tailored solutions. And thanks to growing market consolidation, a lot of small to medium-sized sales teams will be forced to keep fighting uphill battles with their larger and more resourceful competitors. Several asset managers have faced up to this reality and started getting their sales teams ready for the future by aligning incentives, leveraging technology and rethinking outdated processes.

One example for this type of alignment comes from a leading financial services firm. In line with the strategic ambitions of senior management, we redesigned the sales-based compensation and bonus system for a broad range of financial products. We also introduced a new career model with strategic goal-oriented promotion criteria, resulting in a more concise and transparent compensation model that allows for more frequent, clearly-defined career advancement for sales staff. Apart from incentives and previously discussed technological tools, we have found that asset management companies often underestimate the power of processes in sales. Agile working environments have proven successful far beyond their IT origins, and their potential to improve sales is a testament to that claim. In our own experience, we found that transforming a traditional cooperation model into an agile working environment can yield overall efficiency gains of 25% and reduce time-to-market for new products and innovations by 10-30% on average. In a market where M&A activities have shifted the power balance decisively towards asset management behemoths, the greater flexibility and increased speed of agile ways of working can enable smaller firms to get a foot in the door with lucrative emerging investment trends.

Perhaps even more important than simply becoming faster and more efficient, we are seeing a cultural shift in the sales space driven by customer expectations. A recent analysis by our partner firm Casey Quirk identified four distinct areas that clients felt were important for their interactions with the sales teams of asset management firms. These areas were coined the "four E's": extend, entice, enter and engage (see illustration). Generally, they indicate a shift from a more rigid, linear customer journey towards a continuous, accretive and often two-way relationship.

This novel dynamic requires a new set of largely automated, yet customized processes with dedicated sales and CRM tools. Self-service portals and risk management tools operated by the clients themselves are ideally suited to this purpose. When sales staff take the initiative to offer tailored add-on services or investment opportunities that reflect the client's business and investment priorities, clients become more engaged and sales staff can create elegant cross or upselling opportunities. Asset managers will have to acknowledge that the growing complexity of investment options, such as crypto or ESG, not only pose a serious challenge for themselves, but also for their clients. Helping them navigate the market as a true partner can become a significant value proposition and real differentiator.

Asset managers can turn market developments into favorable conditions

Conclusion

Competition has increased in the past couple of years and put serious pressure on medium-sized asset managers in particular, yet there are still numerous opportunities for companies to position themselves and to expand their market position for the future.

Asset managers continue to transform their product offering with ESG-focused products and novel products for both institutional and retail investors. They have also launched initiatives to improve the efficiency of their sales teams, to foster automation and to cut costs to cope with margin pressure due to higher regulatory expenses and cheaper competitors. However, if they want to keep pace with the rapidly changing market environment, asset managers will have to continue rethinking their strategy, offerings and habits – smaller firms in particular cannot afford to be left behind.

The time is now for sales teams like yours to harness the momentum of change. Get in touch and find out how you can market new and enhanced products to your customers as effectively as possible by targeting new distribution channels, leveraging smart (AI-based) technology and making sure you have a superior sales team with a competitive compensation model.

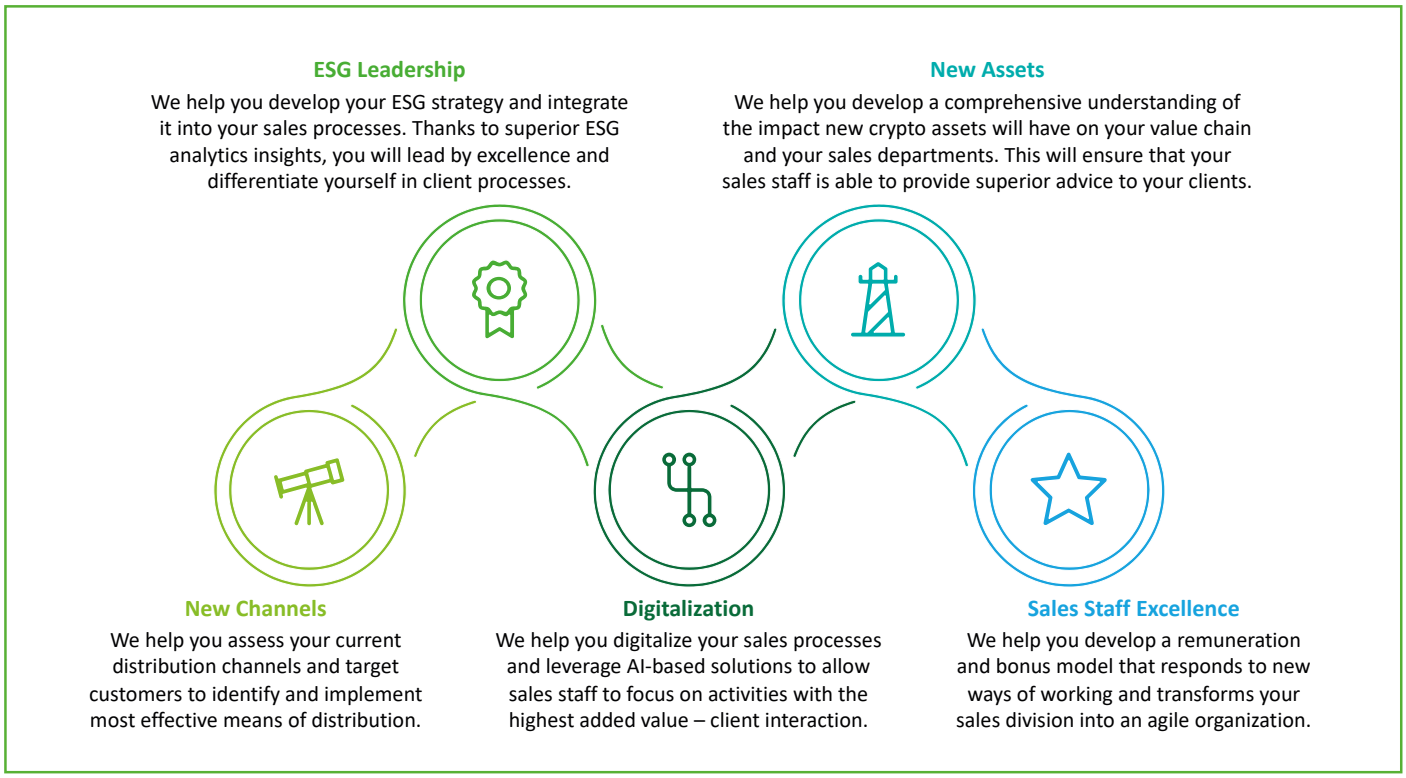


Figure 7: Deloitte can help you putting yourself in a strong position for the future (Source: Deloitte 2021)

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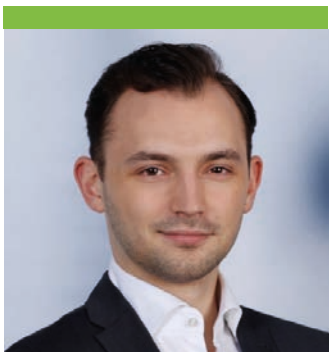

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