



Asia's growing fund business

BY TAN CHONG KOAY |

The global fund management industry saw a re-recovery last year after three years of decline from 2000 to 2002, following the collapse of the US tech bubble.

According to London-based International Financial Services, total global assets under fund management stood at US\$42.4 trillion as at end-2003. The US accounted for 46% of the total global source of funds, followed by Japan with 12%, the UK with 8%, France with 5%, Germany with 4%, and the Netherlands and Switzerland with 2% each. The rest of the world accounted for the remaining 21%. Outside Japan, Asia as a source of funds remained relatively small in the global context, but it is a region with strong growth potential given its fast-expanding economies and rising private wealth.

The Asian fund management industry is centred on Tokyo, Australia, Hong Kong and Singapore. While the Australian fund management industry is larger, it is more domestic oriented. Hong Kong and Singapore are generally regarded as more internationally oriented.

The overall Asian fund management market had a good run last year, driven by a rebound in global equity markets and an improving fund management regulatory environment. In particular, Hong Kong and Singapore further improved their policies to promote their fund management industries, while the emerging giants of China and India also started implementing policies to attract international players. An increasing availability of a greater variety of fund products, notably in hedge funds and real estate investment trusts, has helped.

More boutique fund managers (BFMs) have also been established recently, but collectively, they still account for a small proportion of the assets under management.

BFMs normally possess the following characteristics:

- Their founders have extensive experience in fund management;

- They specialise in particular strategies and styles, and/or in particular markets;
- There is hands-on involvement by the founders;
- They have a flat management structure and are highly responsive to the market;
- Service is personalised; and
- They have strong performance track records.

Singapore and Hong Kong

According to data from the Monetary Authority of Singapore, total Singapore-based fund management assets grew from \$65.9 billion in 1994 to \$465.2 billion last year — an annual compound average growth rate of 24.3%. There were 230 asset management companies at the end of last year, of which 96 were local. Of last year's fund assets, 54.7% was managed on a discretionary basis; of the total discretionary portion of \$254.6 billion, 70% was sourced from outside Singapore.

Given Singapore's position as a "staging post" for global portfolio investment coming into Asia, the discretionary portion of Singapore-based fund management assets comprises mostly foreign funds centralising their regional portfolios in Singapore. At the retail level, total asset management under various investment products also saw a commendable 36% growth from \$14.1 billion in 2002 to \$19.2 billion last year. For the first time, capital guaranteed funds surpassed equity funds to become the largest investment product category at \$7.6 billion, with a 41% growth for the year. Equity funds were at \$7 billion and fixed income funds, at \$2.4 billion. Hedge funds saw a tenfold rise to \$88 million, albeit from a very low base.

Data from the Hong Kong Securities and Futures Commission showed that total Hong Kong-based fund management assets were relatively stagnant between 2000 and 2002 before seeing a growth of 80.2% to HK\$2,947 billion last year. Last year, about 63% of the total fund management assets was sourced from non-Hong Kong investors, a decline from 73% in 2000. Institutional and pension funds

accounted for the two largest sources of funds at 43.1% and 16.5%, respectively. Not surprisingly, 40% of total Hong-Kong based assets are invested in Hong Kong and China, with the rest of Asia accounting for another 33%. Equities remained the largest investment asset class at 62% of total assets, followed by bonds at 27%.

Challenging task

As in other parts of the world, independent fund managers in Asia operate under considerable odds to build an enduring franchise. This is particularly the case for BFMs that have yet to establish an institutional franchise.

The challenges include:

- Lack of economies of scale. Fund management is a scale business;
- "Chicken and egg" issue. Many institutions won't invest with a BFM unless it has achieved a certain size. Many institutions have an internal "20% rule" — their total funds managed by a BFM cannot exceed more than 20% of the BFM's total fund size;
- General perception that a BFM has higher risk due to over dependence on the founders, greater dependence on a few clients, limited resources, having systems and investment processes that are seen as less structured and rigorous, and a relatively short performance track record; and
- Lacking a strong distribution machinery, hence the need to rely on external distributors who demand a big cut of fees.
- Investment consulting firms' traditional bias against BFMs (although that is starting to change); and
- Traditional attitude of institutions in Asia — believing that they can replicate the skills of BFMs, hence their unwillingness to pay for such services.

Overcoming the odds

In the 10 years Pheim has operated in Malaysia and its nine years in Singapore, assets under its management have grown steadily.

Having established a long track record of outperformance, we have been able to attract clients that include government agencies, government-linked companies, corporations, insurance companies, unit trusts and mutual funds. Our client base includes a Luxembourg-registered fund that is distributed by New Private Bank (based in Zurich, Switzerland), a Cayman Island-registered fund that is distributed by Aizawa Securities, an established independent securities house in Japan, two British Virgin Island-registered funds established in 1995, the Asean Emerging Companies Growth Fund Ltd and The Vittoria Fund Ltd.

Pheim Malaysia has been profitable every year since 1994, while Pheim Asia has been profitable every year since 1995, except for a small loss in 1998. We attribute our success to five key factors: persevering and seizing opportunities; being disciplined and focused in our business; being customer-centric; practising strong operational control and compliance; and avoiding conflicts of interest. We have a policy of not engaging in proprietary trading and not accepting invitations to sit on boards of companies we invest in. We also have strict control on staff's own-account trading.

To conclude, the overall fund management industry in Asia is expanding again after a lull. As a result of improving economic fundamentals in Asia, there has been funds flow from Europe and, to a lesser extent, from the US. At the same time, more Asian funds are available for fund management as a result of improving equity markets in Asia, growing economies and the expanding pension fund industry. A DBS report estimates that the amount of Asian liquidity has increased 50% over the past four years to US\$5.5 billion currently.

All these factors should bode well for the overall fund management business, and we see room for independent fund managers to maintain a share of the expanding pie. For most independent fund managers, particularly BFMs, the key to their continued success will depend on their ability to maintain a strong track record of good performance. **E**

Tan Chong Koay is founder and chief strategist of Pheim Asset Management