

2011

Seizing the Moment: Building Tomorrow's Winning Asset & Wealth Management Leadership

Asset & Wealth Management Trends



From the Editors

Europe in disarray... American politics gridlocked... Continued deleveraging and headcount reductions across financial services...

A quick scan of today's headlines would suggest that the global financial system is poised for implosion. Yet while these themes help sell newspapers, portraying nothing but gloom and doom is misleading. Similarly unhelpful are the common refrains about how this period in time has become "the new normal" or how "uncertainty is the only certainty." While perhaps interesting theoretically, these approaches offer little guidance in terms of making truly informed and confident business decisions. Moreover, they frequently miss important (if subtle) nuances in the market.

What's needed is a little more science and forward-looking analysis. That's what Russell Reynolds Associates set out to provide with our 2011 Asset & Wealth Management Trends Report. Based on a rigorous, quantitative survey of nearly 30 financial institutions, hundreds of conversations with top executives across the year, and recent roundtables for industry leaders hosted by our team, we are pleased to share with you the following trends and perspectives. We hope the insights are helpful as you consider the future of your businesses and—most importantly—the critical leadership you will need in place.

1. Asset managers are optimistic... but with a healthy dose of caution

Industry performance has improved slowly but steadily since the dark months following the 2008 financial crisis. Asset growth has stabilized and profitability has improved, easing the extreme pressures on many firms. While the industry has regained some level of client trust, economic uncertainty continues to weigh heavily on asset managers, as flows trend away from riskier asset classes, causing a renewed threat to profitability. Investors are becoming more demanding and, with significant funds in motion, future revenues will increasingly become more elusive. To maintain margins in a period of significant volatility and increased regulatory change, fund managers are designing new products, improving transparency, reducing costs and boosting operating efficiency. The largest firms with the best operational infrastructures are dominating flows and charging the highest fees, enabling them to diversify, scale, and attract top talent. Alternatives managers that consistently deliver returns through the extreme turbulence are realizing similar benefits.

2. Client demands are increasing significantly in volatile markets

Although investors saw improved returns over the past year, the financial crisis called into question many traditional beliefs regarding asset allocation and portfolio construction. Investors are skeptical about the industry's ability to deliver sustained performance and increasingly scrutinize investment decisions—for example, questioning the manager's investment philosophies, processes and performance benchmarks. Effective transparency and risk management have become as critical as fund performance. In addition, the nature of the client relationship is shifting as investors demand more high-touch communication and interaction, value-added research, and customized solutions.

3. Product dynamics continue to shift

Product shifts that occurred prior to the crisis are now clearly entrenched. There is visible growth in both allocations to alternative strategies that seek alpha (albeit with less blind faith) and passively managed products such as ETFs that seek beta. Active managers are under more pressure than ever to deliver alpha and diversification. Fund managers continue to ruthlessly assess their competitive positioning and exit strategies where they have no clear differentiation. A key structural development is the growth of customized solutions, such as asset allocation funds, target-date funds, LDI, and other multi-asset solutions directed towards specific outcomes or balance sheet requirements. Further, the Outsourced CIO Model has gained significant traction and a number of managers are investing in talent and infrastructure to deliver this capability to clients as a separate solution. As managers seek to construct these offerings, experience in cross-asset-class investing and technical acumen in portfolio construction and asset allocation are in hot demand.

More specifically, the following product-related trends are driving shifts in demand for investment talent:

- Continued transition away from long-only US equities into global equity strategies.
- Clear shift away from the G-20 with high demand for emerging market equities and debt.
- Institutional investors have returned to alternative strategies where managers demonstrate strong track records, effective risk management, sound operating infrastructures to realize outsize returns, and diversification to meet future liabilities. Significant HNW and retail assets remain in cash and conservative fixed income strategies as capital preservation continues to be a priority.
- Capital flows out of fixed income, private equity and real estate, into hedge funds, allowing investors to maintain their 'alternatives' exposure, while preserving liquidity via shorter lock-ups.
- Hedge Fund seeding is back. Nearly 300 Hedge Funds launched in 1Q11. However, the mortality rate for new funds remains high at 40%.
- Diminished appetite for high yield and distressed corporate credit, with increased appetite for global macro, event driven, fundamental long/short strategies, global equities, and commodity/CTAs.
- Significant increase in direct-lending initiatives ("shadow banking") out of Private Equity and Hedge Funds.
 - These funds are capital-rich, with the ability to disintermediate banks that are in disarray and unwilling to lend to middle-market borrowers.
 - Increased migration of sell-side leveraged finance talent to buy-side mezzanine and direct lending firms.

4. Return to Product Management as a core competency

Product Management—as a core competency—is back, as managers seek to rationalize the product portfolio, innovate strategically, expand globally and accelerate business development success. In 2010, the industry restructured hastily with several large, "shotgun" acquisitions and broader consolidation. Those firms must now rationalize their product set by eliminating redundancies and ensuring brand fit across all products. Further, firms are seeking to focus Portfolio Managers on delivering investment performance. Consequently, demand for Product Specialist capability as a proxy for the Portfolio Manager in marketing and due diligence activities is increasing.

5. The pace of consolidation has tapered, emphasizing niche team lift-outs

Transaction activity in the sector has diminished, resulting in reduced consolidation. Improved macroeconomic trends have eased the pressure on large financial institutions to divest—and there have been fewer large deals over the past year. However, smaller-scale consolidation, designed to fill gaps or enter new markets rather than achieve scale, will continue with select acquisitions and targeted team lift-outs. This is particularly evident in global and emerging market equities. As failures in integration due to "tissue rejection" are common, acquirers must fully investigate cultural fit when reviewing potential acquisition targets. To avoid value destruction with the loss of key talent, a structured, proactive, and high-touch acquisition integration and retention approach is most critical.

6. Reconstructing Sales and Marketing to compete in the “new normal”

Sales and Marketing teams are under review as distribution and access remain intensely competitive. Demand for top distribution talent has intensified as long-only and alternatives managers have continuously upgraded their teams over the past two years—and demand continues. The “classic” marketer is viewed as a relic of the past, as firms pursue a relatively small pool of sophisticated, investment-savvy, and advisory-oriented executives who interact with investors at a peer level. In the retail channel, there is a significant need to upgrade talent as distributor headquarters gain power and consolidate relationships. Further, the “institutional-like” sophistication and unique, long-tail sales process required to penetrate the growing but challenging RIA market, requires re-invention of traditional marketing approaches and talent profiles. Complementing business development, 2011 saw a comprehensive rebuilding of marketing organizations as firms sought to reposition the brand, take investor mindshare via innovative thought leadership, and proactively support parallel sales initiatives.

7. Increasing role of regulation

Clients are demanding best-practice risk management, compliance, transparency and professional management. With continued and highly public failures, risk management and transparency priorities dominate. When firms fail to respond quickly to events, managers can become black-listed by consultants—and investors frequently respond with “sell-first, question later.” In parallel, rigid and uncertain regulatory environments in North America and Europe have the potential to erode profitability and drive shifts in risk management approaches and product strategy. This heightened regulatory environment is creating additional drag on profitability as risk management and compliance costs rise. Interestingly, hedge funds stand to gain from proposed regulation as banks face increasing restrictions on proprietary trading and other activities.

8. Different markets, different challenges

Managers face very dissimilar challenges with respect to competition and talent as they pursue growth in different markets. Mature markets, such as North America, Europe, Australia and Japan, are over-penetrated. That said, there are significant flows into select products, such as emerging market equities, which should be quite robust. Managers are focusing on core strengths—or moving beyond those strengths only selectively—and ensuring an efficient use of resources. Leadership, strategic insight, management discipline, and agility are critical capabilities for senior leaders in these markets. Developing markets, such as Latin America and many parts of Asia, are focusing primarily on building investment and distribution infrastructure, with varied approaches that reflect specific market and regulatory dynamics. The heated market is fueling an intense war for talent as evidenced by excessive compensation and a lack of employee loyalty.

9. Wealth Management reinvents the business model

Wealth Management continued its reinvention in 2011. Ongoing privacy scandals in the “classic” wealth management centers, shifting demographics, demand for open architecture and freedom of information

through the internet are altering the industry's structure. HNW clients are no longer seeking a "country club" atmosphere but, rather, a value-added model, including integrated, self-directed and advisory channels; innovative communications (digital media, social media, mobile transactions); unique access to investment opportunities through a related investment bank; preferred financing for entrepreneurs; advice and expertise from the Private Bank and Investment Bank during wealth creation; and cross-enterprise expert advice teams. In some cases, firms are implementing a "bank-within-a bank" or developing strategic partnerships to deliver these Investment Banking capabilities. With these changes, new entrants and "new school" talent will replace established firms that cannot keep up.

10. Compensation more nuanced than negative

Russell Reynolds Associates surveyed twenty-nine asset and wealth management institutions to understand their views on—and approaches to—2011 compensation. While a number of aspects will vary little from 2010 (e.g., bonus/base as a share of total compensation will remain flat; few firms are leveraging equity bonuses, deferrals and clawbacks; etc.) some interesting nuances emerged, in many cases revealing a more positive outlook heading into 2012. For example:

- Fully 32% of firms expect bonus pools to grow.
- Over half of respondents in the Distribution/Marketing space expect bonuses to rise.
- Perhaps most encouraging, from a broader standpoint, 39% of surveyed institutions expect their workforce to grow in 2012.

Click here to access the complete survey results: <http://www.russellreynolds.com/content/asset-and-wealth-management-compensation-survey-2011>.

11. Leadership: critical yet scarce

The relative stability of the first half of 2011 gave asset managers the courage to reinvest in their businesses in ways not seen since before the financial crisis hit. The second half of the year has proven to be quite a different story. For obvious reasons, we believe the landscape will remain extremely challenging for some time to come. As a result, discipline, courage and fundamental leadership competencies will define the executives and organizations that separate themselves from the pack going forward. Leadership and strategic skills will be crucial to successfully navigating the current environment, as will the ability to motivate teams in light of volatile conditions and compensation constraints. However, these skills are in high demand (and therefore come at a premium) as the pool of individuals with experience leading organizations and teams through uncertainty, while positioning their businesses for growth, is finite. At the same time, leaders must demonstrate the ability to operate both "horizontally" and "vertically," maintaining a critical focus on the organization's strategy while simultaneously executing strong tactical leadership. All the while, they should expect ever-increasing demand for accountability from investors and shareholders.

Unfortunately, few organizations have adequately identified and developed the next generation of leaders. Nowhere is this more apparent than in the hedge fund industry where founders have generally done a poor job proactively planning for their leadership transition. If great organizations are born of difficult times, then this is a once in a generation opportunity to build a lasting, world-class franchise.

2012: Looking Ahead

What are the implications of these trends on talent management through 2012 and beyond?

Boards: Corporate and mutual fund boards will continue to focus on business oversight, governance, and risk management by adding finance and risk-literate directors with the expertise to challenge senior leadership.

Senior Leadership: The scarcity of CEOs and senior executives with the desired mix of leadership capabilities, strategic vision, determination, and global experience has created a real challenge. We expect to see continued movement of executives from other segments of financial services towards Asset and Wealth Management as a result of high demand for creativity—and CEOs will continue to demand high-profile candidates and global searches to round out their teams.

Investment Management: Expect strong demand for global and emerging equities and multi-asset talent. CIO demand will remain strong, in particular for those with diverse asset-class experience, leadership capability, and risk management acumen. We see specific demand for CIO talent as managers build outsourced CIO capabilities. Further, firms will continue to pursue turnkey solutions through additional team moves.

Sales & Marketing: As long-only and alternatives managers continue to upgrade talent, top sales and investor relations advisory talent will become scarce and further accelerate an increase in compensation levels. We expect continued investment in CMOs, Heads of Marketing and Product Management/ Specialist talent.

Risk Management: Expect continued demand for functional risk managers (credit, market, counterparty, operational) and analytical and quantitative risk managers who have experience working on investment teams and as corporate CIOs. There will be particular demand for talent capable of bridging the gap between the models and managers. As firms adapt to increased regulatory oversight and investor scrutiny, we expect continued hiring for compliance and legal officers with a premium on experience in regulatory affairs.

Infrastructure: Expect revitalized hiring of operational leaders as managers reassess their infrastructure platforms. After holding off on technology investments, mid- and back-office infrastructure is dated and needs attention. In the current environment, there is demand for executives who bring a strategic perspective to design and have experience with outsourcing and hybrid models.

Human Resources: Talent management is back to the forefront, as the retention and development of “franchise players,” succession planning, and strategic talent acquisition to support new business initiatives all become points of competitive advantage.

RUSSELL REYNOLDS ASSOCIATES

Leadership for a Changing World. In today's global business environment, success is driven by the talent, vision and leadership capabilities of senior executives. Russell Reynolds Associates is a leading global executive search and assessment firm with more than 300 consultants based in 40 offices worldwide. Our consultants work closely with public and private organizations to assess and recruit senior executives and board members to drive long-term growth and success. Our in-depth knowledge of major industries and our clients' specific business challenges, combined with our understanding of who and what make an effective leader, ensures that our clients secure the best leadership teams for the ongoing success of their businesses. www.russellreynolds.com

Americas

Atlanta

1180 Peachtree St., NE
Suite 2250
Atlanta, GA 30309-3521
United States of America
Tel: +1-404-577-3000

Boston

One Federal Street, 25th Floor
Boston, MA 02110-1007
United States of America
Tel: +1-617-523-1111

Buenos Aires

Buenos Aires Plaza
Manuela Sáenz 323
Seventh Floor, Suites 14 and 15
C1107CBP Buenos Aires
Argentina
Tel: +54-11-4118-8900

Calgary

Suncor Energy Centre, West Tower
#3000, 150-6th Avenue, S.W.
Calgary, AB T2P 3Y7
Canada
Tel: +1-403-538-1972

Chicago

155 North Wacker Drive
Suite 4100
Chicago, IL 60606-1732
United States of America
Tel: +1-312-993-9696

Dallas

8401 N. Central Expressway
Suite 650
Dallas, TX 75225-4404
United States of America
Tel: +1-214-220-2033

Houston

600 Travis Street, Suite 2200
Houston, TX 77002-2901
United States of America
Tel: +1-713-754-5995

Los Angeles

11100 Santa Monica Blvd.
Suite 350
Los Angeles, CA 90025-3384
United States of America
Tel: +1-310-775-8940

Menlo Park

2500 Sand Hill Road
Suite 105
Menlo Park, CA 94025-7015
United States of America
Tel: +1-650-233-2400

Mexico City

Torre Reforma
Paseo de la Reforma
115-1502
Lomas de Chapultepec
México 11000, D.F.
México
Tel: +52-55-5249-5130

Minneapolis/St. Paul

225 South Sixth Street, Suite 2550
Minneapolis, MN 55402-3900
United States of America
Tel: +1-612-332-6966

New York

200 Park Avenue
Suite 2300
New York, NY 10166-0002
United States of America
Tel: +1-212-351-2000

San Francisco

101 California Street
Suite 2900
San Francisco, CA 94111-5829
United States of America
Tel: +1-415-352-3300

São Paulo

Edifício Eldorado Business Tower
Av. Nações Unidas, 8501
11º Andar
05425-070 São Paulo - SP
Brazil
Tel: +55-11-3566-2400

Stamford

301 Tresser Boulevard
Suite 1210
Stamford, CT 06901-3250
United States of America
Tel: +1-203-905-3341

Toronto

Scotia Plaza, Suite 3410
40 King Street West
Toronto, ON M5H 3Y2
Canada
Tel: +1-416-364-3355

Washington, D.C.

1701 Pennsylvania Avenue, NW
Suite 400
Washington, D.C. 20006-5810
United States of America
Tel: +1-202-654-7800

Asia/Pacific

Beijing

Unit 3422 China World Tower 1
No. 1 Jian Guo Men Wai Avenue
Beijing 100004, China
+86-10-6535-1188

Hong Kong

Room 1801, Alexandra House
18 Chater Road Central
Hong Kong
China
Tel: +852-2523-9123

Melbourne

Level 51, Rialto Towers
525 Collins Street
Melbourne VIC 3000
Australia
Tel: +61-3-9603-1300

Mumbai

Unit 9(A), Grand Hyatt Plaza
Santacruz (East)
Mumbai 400 055
India
Tel: +91-22-6733-2222

New Delhi

203, Eros Corporate Tower
Nehru Place
New Delhi 110 019
India
Tel: +91-11-4603-4600

Shanghai

Room 4504, Jin Mao Tower
88 Century Avenue
Pudong, Shanghai 200121
China
Tel: +86-21-6163-0888

Singapore

2 Shenton Way
#08-01 SGX Centre 1
Singapore 068804
Singapore
Tel: +65-6225-1811

Sydney

Level 40, Aurora Place
88 Phillip Street
Sydney NSW 2000
Australia
Tel: +61-2-9258-3100

Tokyo

Izumi Garden Tower 14F
1-6-1 Roppongi
Minato-ku, Tokyo 106-6014
Japan
Tel: +81-3-5114-3700

Europe

Amsterdam

World Trade Center
Tower H, 18th Floor
Zuidplein 148
1077 XV Amsterdam
The Netherlands
Tel: +31-20-305-7630

Barcelona

Edificio Prisma
Avda. Diagonal, 613, 2ªA
08028 Barcelona
Spain
Tel: +34-93-494-9400

Brussels

Boulevard St.-Michel 27
B-1040 Brussels
Belgium
Tel: +32-2-743-12-20

Copenhagen

Østergade 1, 1st Floor
DK-1100 Copenhagen K
Denmark
Tel: +45-33-69-23-20

Frankfurt

Operturm
Bockenheimer Landstr. 2-4
60306 Frankfurt
Germany
Tel: +49-69-75-60-90-0

Hamburg

Stadthausbrücke
1-3/Fleethof
20355 Hamburg
Germany
Tel: +49-40-480-661-0

London

Almack House
28 King Street
London SW1Y 6QW
United Kingdom
Tel: +44-20-7839-7788

Madrid

Calle Miguel Angel, 11
Seventh Floor
28010 Madrid
Spain
Tel: +34-91-319-7100

Milan

Via Mascheroni, 5
20123 Milan
Italy
Tel: +39-02-430-0151

Munich

Maximilianstraße 12-14
80539 München
Germany
Tel: +49-89-24-89-81-3

Paris

7, Place Vendôme
75001 Paris
France
Tel: +33-1-49-26-13-00

Stockholm

Hamngatan 27
SE-111 47 Stockholm
Sweden
Tel: +46-8-545-074-40

Warsaw

Belvedere Plaza
ul. Belwederska 23
00-761 Warsaw
Poland
Tel: +48-22-851-68-38

Zürich

Löwenstrasse 28
CH-8001 Zurich
Switzerland
Tel: +41-44-447-30-30