Your next chapter -

Expansion plans and exit strategies for boutique asset managers

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A call to action

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Several major trends are relentlessly reshaping the asset and wealth management (AWM) industry, and every area of a firm's activities is arguably affected - from front office, middle office to back office functions. Reshaped by forces like increased focus on Environmental, Social, and Governance (ESG) considerations, continued operating model pressures, increasing regulatory scrutiny, shifting workforce trends and greater data and analytics imperative, the industry is undergoing rapid changes. The magnitude of changes is so significant that asset and wealth managers have no choice but to continuously re-engineer their strategies.

Against this backdrop, there is urgency for boutique asset managers, especially those operating in alternative investment strategies such as private equity, hedge funds, real estate, private credit, and infrastructure, to think differently about how to reassess their strategic playbook. Alternative investment strategies have continued to grow steadily in recent years and expected to reach US$18.9 trillion in assets under management (AUM) globally by 2025.

As investors increasingly turn to alternative asset class investments for their diversification benefits and upside potential, the growth in homegrown boutique asset managers in the Asia-Pacific region will continue. Many boutique managers are already well established with strong reputations, serving sophisticated investors around the world.

Boutique asset managers are valued by investors given their differentiated source of returns and counterpoint to large multinational asset managers, which generally focus more on equity and fixed income investments. Their agile and niche focus, often specializing in private multi-asset class solutions is frequently seen as a valuable differentiator and source for delivering alpha.

By truly understanding the unique forces driving change in the industry and the scale and maturity of the business, boutique asset managers will increase their odds of achieving their strategic ambitions.

[1] PwC - Asset and wealth management revolution: The power to shape the future

Becoming fit for the future

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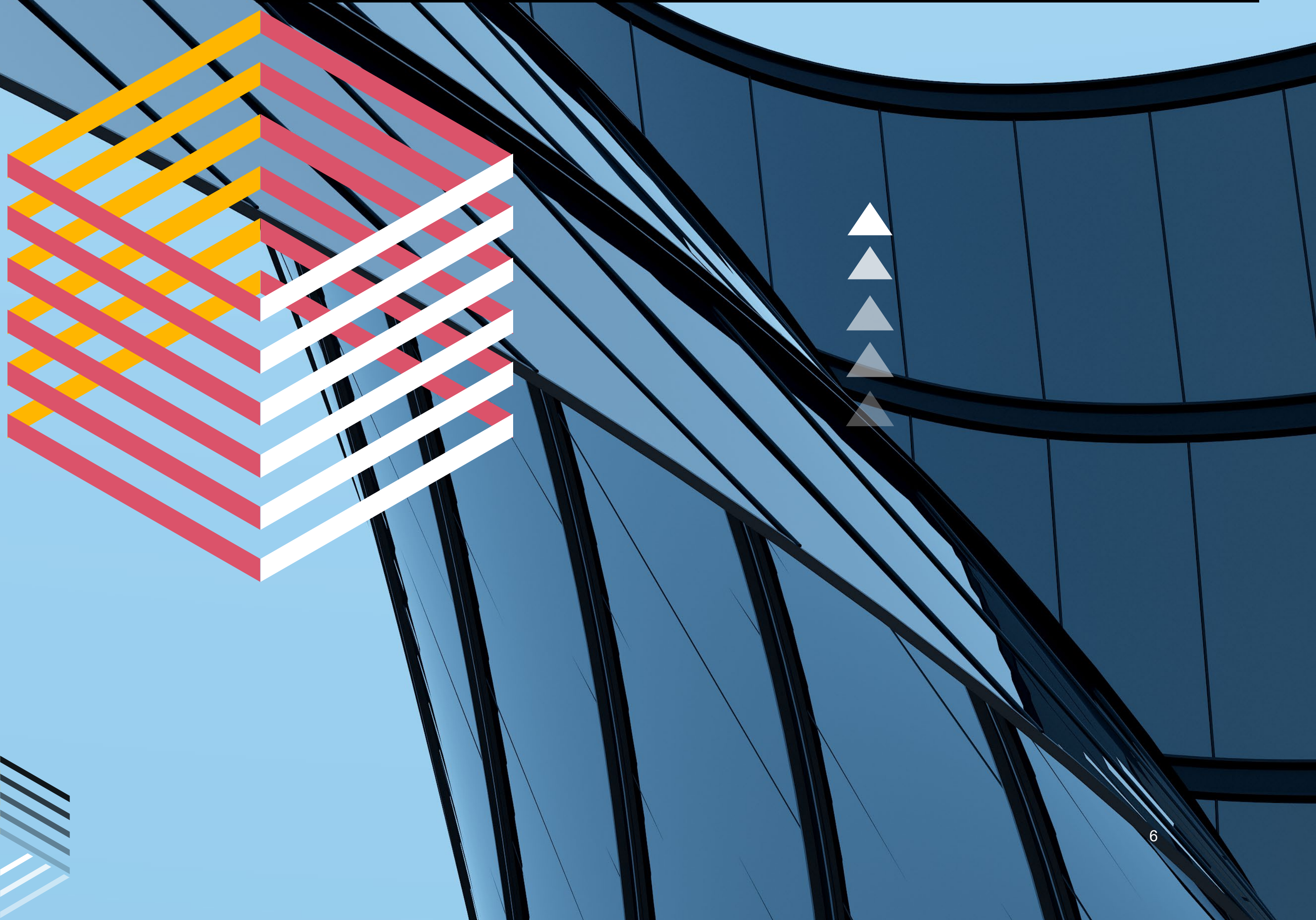
Asset managers should ultimately align their strategies with the ever-evolving investment objectives of investors. With ongoing global macroeconomic uncertainty persisting, changing investor preferences, and greater price sensitivity from investors, there is now mounting pressure for firms to re-think their strategic priorities – be it expanding further through inorganic M&A opportunities, organic growth or capital-raising via an IPO.

In the background, asset managers must also continue to look at reducing costs and generating sustainable returns. As such, proactive preparation has become increasingly important, whether the plan is to expand product offerings in other asset classes to boost profitability and head off competition, reinforce internal capabilities making use of existing talent or divest the business partially or completely to create greater value for shareholders.

Elevate your business through M&A opportunities



Elevate your business through M&A opportunities

M&A activity among asset and wealth managers has reached record levels, and there are sound strategic reasons for this upswing. Firms are seeking to reposition themselves and protect profitability in the face of shifting investor demands, the need to embrace technology, and growing regulatory scrutiny.

The AWM industry remains highly fragmented and further consolidation is likely, especially for large multinational asset managers. This cohort is experiencing significant pressure on profitability and margin compression. Although AUM is set to grow in the medium and long term, fees are likely to continue to decline - influenced by the continued rise of passive strategies and investors' ongoing demand for lower fees. Moreover, increased spending on regulatory compliance and reporting, as well as technology investments and the war for talent is putting further pressure on margins. While asset managers look to continue to push for greater efficiencies internally while balancing costs as they adapt to changes, for many, the answer will be to build greater scale and investment expertise through M&A opportunities.

Many asset managers will also evaluate M&A opportunities outside of the typical forces - such as opportunities for economies of scale and cost synergies. Deal activity involving the acquisition of boutique asset managers, especially those operating in alternative investment strategies has seen an increase in recent years and this momentum is expected to continue. Large multinational asset managers have increasingly looked towards and moved deeper into alternatives, as they look to build capabilities in this asset class to offer more choice for their clients – many of which are finding that traditional asset classes are not as desirable as compared to the past. Adding alternatives expertise is also a means to boost revenue due to higher management fees, in addition to the potential for performance-based fees – an indispensable opportunity given fees are compressing for mutual funds and exchange-traded funds (ETFs). In Asia-Pacific, M&A activity by large multinational asset managers to build scale in alternatives has increased, and the market for deals has become more competitive. While it is an attractive proposition, offering and managing alternative investments is very different from traditional investments.

Within the alternative asset's realm, there is also a trend of boutique asset managers looking to create multi-asset class solutions which highlights the connectivity within private markets. For instance, there is crossover between asset classes in the increased allocations of private equity funds to credit opportunities, hedge fund firms investing capital into private investments, growing private equity investment into real estate, and a focus on infrastructure investments. Boutique asset managers share many of the same types of investors - pension funds, sovereign wealth funds and endowments - and an increasing number of boutiques understand the benefits of being able to offer these asset allocators a full suite of alternative investment products.

The factors driving convergence are contributing to growing consolidation within private markets. Many boutique asset managers now resemble corporate giants, managing as many assets as some boutique banks.

The key advantage of M&A opportunities in the AWM industry is that institutions can quickly obtain multi-asset class capabilities and the supporting talent and technology.

Asset managers that have yet to differentiate themselves are looking to merge with others, hoping the combined firm's resources will create more value. Levelling-up and offering a range of asset classes will put buyers in a sweet spot to attract large capital allocations and tackle complex investment opportunities.

Fundamentals to consider for M&A integration success

Acquisition	• **Pay for performance** The valuation gap could lead to significant performance-based incentives to retain key players after the M&A transaction closes. Increasingly, these incentives are tied to metrics to encourage the continued success that prompted the M&A in the first place. • **Expand due diligence to culture** Many acquired companies are start-ups or founder-led businesses with cultures that are very distinct from their buyers. Incorporating employee-based insight into due diligence can provide an early indication of potential culture pitfalls that could erode deal value.
Integration	• **Maintain agile leadership with clear governance** The target company's success was likely built on taking risks and adapting quickly. Maintaining this DNA is paramount despite new owners coming in. • **Preserve the target company's identity** Successful buyers often avoid rebranding the acquired company and instead retain its individuality with separate goals, metrics, and compensation plans. Maintaining separation can also mean fewer compensation and benefits comparisons between the buyer and seller.
Retention	• **Agree on how much to spend** Top leaders know who their key employees are. In the spirit of autonomy, leaders should help select who receives the most lucrative rewards, and a mixture of cash and equity often is preferred. • **Keep culture top of mind** A defined culture roadmap can highlight the employee experience and show the target company's employees that the larger parent will not simply engulf them. Be wary of mandating "ways of working" or eliminating non-traditional benefits and perks.

Innovate your business and grow organically

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Boutique asset managers generally specialize in a niche asset class with extensive network and experience in their field. Moreover, they distinguish themselves as trusted partners with strong alignment with investors which often leads to superior returns as compared to large multinational asset managers. However, boutiques are operationally sub-scale across the value chain impacting their ability to level up and compete with larger players that have already established scale. With this, boutiques must recognise the need to constantly innovate as major trends and developments continue to reshape every area of their activities – and this includes the front office, middle office, and back office. While most are positioned well as the industry itself will see dynamic growth in the coming years, there is no time for complacency as commercial and operational challenges can arise at any given moment. Boutiques generally have a higher propensity for change and given the industry is undergoing profound changes, now would be an opportune time to act.

Boutique asset managers face a unique set of challenges across the value chain

Front office	• Resource heavy, time consuming and tedious fundraising and networking process through cold calls, emails, face-to-face meetings, and conferences. • Lower yield and outreach success rates to investment opportunities and professionals due to lack of brand recognition and credibility in the industry. • Investment sourcing is resource intensive and for many continues to be on a case-by-case basis.
Middle office	• Data inconsistency and insufficiency from complexity of asset classes, leading to a highly time-consuming due diligence process. • Fragmentated steps within the workflow process that is highly manual and requires various third parties at different stages. • A lack of a “single source of truth” throughout workflows posing a challenge to pull information together for investor reporting, portfolio monitoring and risk management.
Back office	• Manual ‘business as usual’ processes handling increasingly complex operations due to a lack of technology. • Ever-evolving regulatory requirements leading to high costs to adapt. • Ability to have dynamic reporting to cater to specific investor reporting requirements is a significant challenge.

Boutiques that are winning today are the ones that align and build their core capabilities to exceed investor expectations. While there is the constant pressure to compete and the allure of M&A opportunities ever present, it is easy for management and senior executives to overlook a basic principle: build from internal resources and strengths. When boutiques design their capabilities and strategy internally accordingly, they can define how they want to compete, and shape their own future.

Across the front office, middle office, and back office, there will be many opportunities to accelerate growth by reevaluating the way the boutique is operated. Getting stakeholders to collaborate and act on specific programs and initiatives will be key, and speed will be critical to ensure the operating model can quickly respond to the changing dynamics of the industry. By creating agile teams, asset managers will be better positioned to act on sudden market changes - including shifts in investor behaviors and demands, as well as emerging trends and competitor developments. By quickly developing insights and evaluating options, boutiques can also act nimbly to deliver quick wins and plant the seeds to drive longer-term growth.

There has been a significant change in the importance of innovation to the success of boutique asset managers in recent times. Investors' expectations of experiences are changing at an unprecedented rate, and innovation has acted as both a trigger and a catalyst. Innovation is a driver for robust and profitable top-line and bottom-line growth and widely recognised by management and senior executives as being integral to sustaining the long-term future of their business. Some boutiques are already moving aggressively on innovative technologies for everything from investment decisions to risk management and the investor experience.

Due to their agile and niche focus, boutiques can easily adapt to disruptive technologies that are increasingly available in the market. Moreover, they can integrate new technology at a lower cost and faster rate since they have minimal legacy infrastructure. With this, most technology adopters have already reported tangible benefits, from improved decision-making, reduced operational risks and enhanced client servicing top of the list. Ultimately, boutique asset managers should look to achieve a combination of better client service, improved competitive dynamics and greater efficiency.

Traditionally, the end-to-end solution that enabled companies to better manage their investment lifecycle, from operational and portfolio management to performance evaluation and reporting, is becoming less relevant for boutiques. The rise of FinTech companies that focus on specific capabilities are increasingly implementing component sized platforms that address specific process needs rather than end-to-end solutions. This service offering comes at a lower price ticket, which is more suitable for boutique asset managers. However, this might lead to challenges down the line as they look to integrate their systems and data.

Boutiques that are likely to succeed in an ever-evolving market must find the right mix of improvements internally coupled with an optimized operating model. Turning a blind eye and ignoring the quick wins from organic sources and clinging on to 'business as usual', focusing on manual operations and not addressing siloed workflows, can be ill-advised. Instead, boutique asset managers should enforce the building blocks of front office, middle office, and back office functions and strive for operational excellence and adopting technology-focused capabilities where possible.

Considerations and options for operational excellence

Proprietary build out	• Fully internalised front to back operating model. • Digital solutions integrated with in-house systems to support IT transformation and process automation. • Can retain full control, optimizing ability to tailor solutions, investor experience and operating model.
White labelling	• Leveraging vendor to ensure ongoing alignment to industry best practices. • Enables focus to be placed on operational excellence for middle and back-office functions. • Some dependency on vendors but increases scalability.
Outsourcing	• Best in class vendor platforms, optimizes scalability, but reduces ability to customize and may be costly. • Integrated vendor platforms can reduce complexity. • Shared data with vendor, so will not retain full client anonymity and control.

Operating your boutique as a public company

Operating your boutique as a public company

Most boutique asset managers have opted for an M&A deal over an IPO to facilitate their growth or exit in recent years. However, the latter has become increasingly popular and the trend of asset managers tapping into public markets will become more apparent over time. Unlike in other industries, most owners of boutique asset managers do not have the option to pass the mantle on to the next generation, given the nature of how companies are run in the AWM industry. The decision to IPO involves many personal and business considerations and it is only one option for the next step in a boutique's development. From the onset, it is important to involve all major shareholders in the decision-making process, enabling them to discuss the advantages and disadvantages of being public to better understand what the process involves.

While IPOs are associated as an exit from the business, it is better characterized as a capital-raising event. The outlook for IPOs continues to evolve with more recent triggers, such as changes in the global political landscape and interest rate environment, leading to windows of opportunity opening and closing quickly. For asset managers looking to an IPO, it is critical to leverage the right insights to make the right moves at the right times.

One of the most important and earliest decisions an asset manager will make is the market on which to list. Today there are more viable options than ever before - including the stock exchange where the company is headquartered, an international stock exchange, or even a dual listing. The decision made will affect not only the valuation and on-going relationship with investors, but also impact strategy, structure, and processes into the foreseeable future.

Some of the critical components to be evaluated across each market include desired valuations, the depth and breadth of the investor base, liquidity trends in the market, current appetite for new listings, regulatory requirements of the stock exchange, the choices made by competitors, and market timing and speed to market.

Once the decision has been made to go public, asset managers need to be in the right shape to begin the process - and the sooner, the better. Management will be required to meet shareholder and market expectations from day one. In addition, management need to be ready to address new requirements around regulatory compliance, operations, risk management, reporting, investor relations, and much more. Having a compelling equity story is indispensable. However, this may be the least of a asset manager’s worries given the AWM industry’s robust growth prospects and strong fundamentals, where global clients’ wealth and global AUM are expected to grow to US$318 trillion and US$139 trillion in 2025 respectively.

Once listed, an asset manager will be under far greater public scrutiny than ever before, with a vastly expanded universe of stakeholders - and a significantly larger portfolio of new risks, and obligations, to manage. Any underperformance of investment strategies, weakness in systems or failure to comply with regulations may cause a loss of investor confidence and reputational damage. A major concern for many private companies is the loss of privacy that comes with being public. Given this, meticulous planning and consideration must be taken regarding how the business manages its affairs prior to an IPO.

Fundamentals to consider for a successful IPO

Equity story and KPIs	• A strong equity story is key to a successful IPO and will determine the level of investor interest in your company. A strong equity story could be defined by the following factors: ○ Well supported and sustainable top-line growth. ○ Attractive, defensible and growing margins. ○ Leading, attractive, and sustainable financial returns.
Choice of market	• Options include the domestic exchange, an international stock exchange or even a dual listing. Critical factors to consider include: ○ Valuation. ○ Depth and breadth of the investor base. ○ Regulatory requirements - eligibility and ongoing obligations. ○ Listing exchange of peers. ○ Liquidity and index inclusion. ○ Practicality e.g., language, time zone.
Board composition	• A public company will be required to have independent directors to represent the interest of the public shareholders. • There will also be the question of who the Chairman will be, which can be a new experience at the heart of the company.
Selection of advisers	• Boutique asset managers will need to select good quality corporate advisers including: bank(s), broker, reporting accountant, lawyers, public relations, and registrar.
Costs and resourcing	• Preparation and on admission: ○ Adviser costs. ○ Time and resources. • Ongoing compliance costs: ○ External costs including annual exchange fees and registrar fees. ○ Internal costs including Non-Executive Directors. • Strengthen financial, risk and compliance functions.
Tax planning	• Corporate: ○ Boutique asset managers need to understand the impact of the IPO on the tax structure of the group and on current and future investors. An IPO provides the opportunity to optimise the group's tax position and review the Effective Tax Rate (ETR) strategy. • Personal: ○ Opportunity to review personal tax and wealth position.

The path forward

The path forward

The asset and wealth management industry will continue to undergo a transformation journey and boutique asset managers must proactively refine their business strategy as the environment evolves. To prepare for the next stage of growth and unlock value, boutiques must take bold steps in transforming their firm to meet today's challenges, be it expanding further through inorganic M&A opportunities, organic growth or capital-raising via an IPO.

Boutique asset managers need to act now as the industry moves to a new paradigm. Those that do not align their strategies with the ever-evolving environment may face disruption, risk irrelevance or, even if successful in growing, may become too complex to be managed effectively. The firms that are most vulnerable are those that have neither scale nor specialisation and they risk being squeezed out of the picture.

Do get in touch if you would like to learn more.

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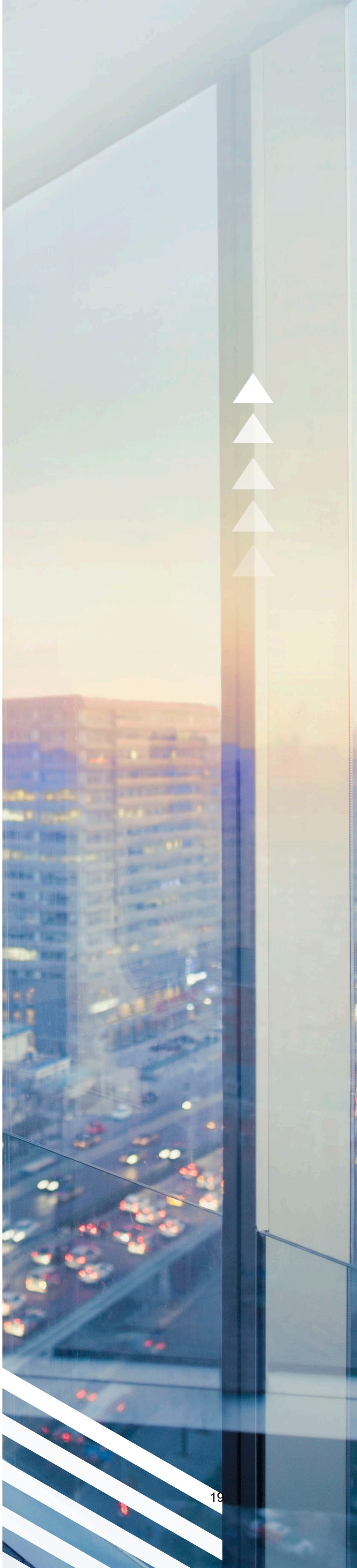

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