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Key figures for asset management in 2017 - Management company financial data and profitability

The operating profit of the French asset management industry rose sharply in 2017 after falling slightly in 2016. The total in 2017 came out at €3,539 million compared with €2,485 million in 2016. The positive trend was the result of growth in operating revenue (up 11.4% year on year), which, all other things being equal, was stronger than growth in operating expenses (up 8.1% year on year). This report overviews the financial data and profitability of asset management companies in 2017.

A return to growth in operating profit in 2017

After a growth period from 2012 to 2015 and a decrease in 2016, the revenue of asset management companies increased once again, reaching €15,390 million at end-2017, for a record increase of €1,578 million on 2016. Operating expenses have increased continuously in the last five years (by an average 5.1% a year since 2012), totalling €11,851 million at the end of 2017. This two-pronged trend, in income and, to a lesser extent, expenses, resulted in a sharp rise in operating profit, up €694 million or 24.4% on 2016.

A closer analysis of the trend in income and operating expenses shows that 79.4% of total operating income was generated by management fees. Given the strong performance in inflows in 2017 (particularly impressive in collective asset management with an 8.6% increase between 2016 and 2017), collective asset management fees made an 88%

contribution to revenue, up €1,396 million on 2016. In contrast, discretionary management fees contracted slightly, falling 0.4% from €891 million in 2016 to €885 million in 2017.

The increase in operating expenses was logical. Against this backdrop of growth, retrocession fees stemming from product marketing contributed 40.5% of the growth in operating expenses, having increased 9.2% between 2016 and 2017. Meanwhile, payroll expense accounted for 25.9% of the growth in operating expenses.

Focus on the breakdown of operating revenue

Note: Ancillary revenue consists of collective investment scheme turnover fees, subscription and redemption fees, and trailer fees on collective investment schemes (fees that the management company charges in the course of its business, when its clients' portfolios are invested in collective investment schemes managed by another company). Incidental revenue includes fees charged for activities relating to advisory services, the marketing of collective investment schemes, order receipt and transmission, the management of unit-linked arbitrage mandates and venture capital funds. Other revenue consists of provision reversals, expense transfers and operating subsidies.

Management fees

The breakdown of operating income shows that management fees represent the lion's share of the revenue of asset management companies. Management fees accounted for 79.4% of total operating income in 2017, generated mainly by the investment management business (92.8% of total management fees charged) and, to a lesser extent, by discretionary management fees (7.2% of total management fees charged).

Consequently, after falling in recent years, the share of management fees in operating profit stabilised at around 80%. However, this share rose 1.3 points between 2016 and 2017, the result primarily of a 14.8% increase in collective asset management fees.

Management fees aside, the share of all other sources of revenue fell, as the latter rose only slightly compared with the increase in the former.

Other income

At end-2017, ancillary revenue was up 3.7% to €1,631 million, generating 10.6% of the revenue of management companies compared with 11.3% in 2016. This revenue mainly consists of turnover fees (€482 million in 2017) UCITS/AIF subscription and redemption fees (€494 million). These two categories supported growth in the ancillary revenue of French

management companies, unlike retrocession fees on UCITS/AIF assets, which fell 36% and 3.6% respectively between 2016 and 2017. This contraction can be attributed to the impact of the entry into force of the MiFID II Directive in January 2018 and the attendant provisions on the supervision of inducements.

Though having fallen slightly (from 8.4% in 2016 to 8.1% in 2017), the share of ancillary income in revenue has posted the strongest increase in the last few years (up an average 17.5% annually between 2010 and 2017 or overall growth of 209% for the period as a whole). The amount rose by a multiple of 3.1 over the period, from €400 million in 2010 to €1,240 million in 2017. The business activities having made the greatest contribution to the growth in ancillary revenue in 2017 were the management of unit-linked arbitrage mandates (rising 66% from €35 million in 2016 to €59 million in 2017) and investment advice (up 11.8% from €293 million to €327 million). Other ancillary income sources remained relatively stable, with the exception of income generated by the venture capital fund management business (fund raising, advice for target companies, etc.), down 3.1% at 31 December 2017.

A closer analysis by type of ownership structure shows that the breakdown of revenue items in turnover is not uniform for the different types of management companies.

** The “Other” category consists of management companies that are subsidiaries of investment service providers or companies governed by public law.*

Investment management fees represented the largest share of revenues generated for all asset managers. However, for management companies that are subsidiaries of insurance and mutual companies, holding a substantial share of the discretionary management market (38.8% of total assets under management), most of their revenue naturally came from this activity (16.9%).

For boutique firms, 12.1% of revenue in 2017 came from incidental revenue, which consisted primarily of turnover fees (39.4%) and UCITS and AIF subscription and redemption fees (37.1%). Ancillary income accounted for a significant 25.2% share of income in the “Other” category, owing mainly to income generated by the marketing of collective investment schemes.

An analysis by ownership structure also makes it easier to compare and understand the relationship between assets under management and revenue generated.

Logically, and as seen in the graph below, with the exception of boutique firms, the more a category of players concentrates assets under management, the larger the share in total

operating income. This correlation stems from the fact that these products are mainly generated by management fees indexed to assets under management. Management companies that are subsidiaries of credit institutions concentrating 60.4% of total assets under management generate 50.2% of the total operating income of the French asset management industry.

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In contrast, boutique firms accounted for only 7.4% of assets under management but generated 30.5% of operating revenue, of which 78.7% from management fees. This can be attributed mainly to the difference in fee rates charged by this type of company (see below).

Fee rates relatively stable

The overall fee rate for collective management increased from 0.481% in 2016 to 0.508% in 2017, while that for discretionary management remained stable, at 0.055%.

The fee rates of management companies vary substantially depending on the ownership structure. Investment services providers and boutique firms charge the highest fee rates in collective management (see Table 1) and discretionary management. This can be attributed to their types of clients and their specialisation in more sophisticated or niche strategies.

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Conversely, management companies that are subsidiaries of credit institutions or insurance and mutual companies have lower fee rates both for collective and discretionary management. This is because they have considerable assets under management, allowing them to make economies of scale. It should also be noted that these firms have a larger intra-group client base, for which the fee rate is generally lower.

Outperformance fees up owing to collective management

At end-2017 outperformance fees totalled €715 million, up 37.1% year on year (see Table 2). This growth results primarily from the increase in outperformance fees charged in collective management (€688 million, up 40.4% on 2016). In contrast, in individual management, as with management fees, outperformance fees were down at 31 December 2017, standing at €27 million (for a decrease of 15.2% on 2016). It should nevertheless be

specified that the share of outperformance fees in total operating revenue remained negligible as they accounted for just 4.6% of total revenue for the French asset management industry in 2017.

Focus on the breakdown of operating expenses

Operating expenses rose 8.1% year on year in 2017, coming out at €11,851 million. The trend stemmed from an increase in payroll expense, other external charges and trailer fees recorded as operating expenses.

Payroll expense totalled €3,018 million in 2017, accounting for 25.9% of the increase in expenses, notably due to a rise in the number of employees, up 4.5% between 2016 and 2017 (see Graph below). Growing at a similar pace to that of total operating expenses (up 8.2% year on year), the share of payroll expense in total operating expenses was stable.

Other external expenses, comprising shares of management fees paid for financial management delegation and expenses relating to accounting, administration, valuation and the compensation of statutory auditors and depositaries of collective investment schemes, came to €3,253 million (up 7% year on year) and accounted for 24% of the increase in operating expenses.

The breakdown of the various operating expense items in 2017 was fairly similar to that of previous years. However, the entry into force of MiFID II will certainly have significant impacts on some key items in 2018, and in particular on trailer fees recorded as operating expenses (standing at €4,231 million, for an increase of 9.2% at end-2017), notably owing to the gradual introduction of fee-free clean-share classes.

Focus on the profitability of portfolio management companies

Record profitability in 2017 close to pre-crisis levels

The graph below, comparing the trend in the operating margin⁽¹⁾ of asset management players and that of the CAC 40 blue-chip index, shows that the schematic link between the trend in the index and the overall operating margin of asset management companies has reversed relative to last year, resulting in a positive correlation between the two indicators.

The profitability of management companies has reached a new high, returning to pre-crisis levels at 23%.

An analysis of management companies' profitability based on the size of their assets under management (see Table 3) shows that, on average, entities that manage less than €50 million have a low if not negative operating margin, while companies managing €50 million to €150 million have an average operating margin of 6%. Those with €150 million to €500 million in assets under management have an average operating margin of 18%; compared with 21.1% for companies with more than €500 million in AuM.

() For example, this data item can be understood as follows: 10% (or 90%) of management companies with AuM of less than €50 million have an operating margin of more than (or less than) 34.4%.*

Companies with substantial AuM maximise their profitability through economies of scale (depreciation of fixed costs). Consequently, the entities with the most negative margins are in general boutique firms, while management companies that are subsidiaries of credit institutions or insurance or mutual companies have the highest profitability levels in the French asset management industry.

Decrease in the number of management companies with operating losses

The total operating losses of asset management companies was nearly €93 million in 2017, compared with €102 million in 2016 (down 8.4%), and concerned 18.6% of the population compared with 22.7% in 2016. This is the first time in three years that this proportion has decreased.


However, the situation differed significantly depending on the age of the asset management company, with the share of firms in difficulty having recently obtained authorisation (aged under three years) standing at 40.3% in 2017. This percentage fell slightly, by 0.3%, in 2017. In contrast, the share of more mature companies (aged over 15 years) with operating losses has declined continuously in the last three years and fell from 18.3% in 2016 to 14.4% in 2017.

Substantial differences are also to be found depending on the type of ownership structure. The largest number of entities with operating losses (79.8%) is represented by boutique firms. This share has grown every year since 2014, on average by 3.3% a year. Behind boutique firms come investment services providers (9.2%) and the subsidiaries of credit institutions (8.3%).

Notes

1. The operating margin (or profitability) of asset management companies is calculated as the ratio of operating profit to operating income.

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