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SALES 2.0

Making Distribution Objectives a Reality in Germany

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Distribution is a controversial topic. Regarded by some as the most important element in the value chain of the asset management industry – since it determines the economic success of the company as a whole – it is seen by others as an inferior kind of activity, necessary though, but nonetheless not as sophisticated and intellectually challenging as managing assets.

Here, I would like to look at distribution strategies from a purely economic advantage. We can examine the sales activities, particularly of non-domestic asset managers, e.g. in Germany, in the same way an analyst would scrutinize the handling of a market of any other company: The analyst would look at the quality of the products, but at the same time at the relative demand of markets and/or market segments for these products, and on the strategic approach the management of the company would follow, when entering new markets.

When it comes to institutional distribution of asset managers, economic considerations are more often than not blurred by other aspects one has to take into account, when gauging their sales and marketing activities. Of course there is reason for it: Sales and marketing measures can be evaluated only within a mid- to long-term perspective, and they rely very much on how they are perceived by individuals. However, what is striking is that although the industry is about 'investing', asset management companies tend not to be too willing to invest in dis tribution, rather opt for opportunistic approaches when it comes to entering new markets, or market segments, or new client bases. Only since margins have been high in the past, approaches dubbed as 'picking-some-low-hanging-fruits' would pass a management discussion at all. Such opportunist forays into a market do not reflect an earnest growth strategy. In fact, they deserve not to be called strategy at all.

What are the particular challenges for sales and distribution of asset managers today, when tackling the German market? I would point out four aspects:
1. Managing sales capacity
2. Defining and allocating resources in view of an extremely fragmented and geographically spread market
3. The risk-dimension of sales and marketing acitivites, as regards the mid-term profitability and long-term reputation of the company
4. The need of marketing and brand-building.

Managing Sales Capacity
Let us start with the necessity and difficulty to manage sales capacity. It is a well known fact that demand for asset classes or products comes in waves, following market developments. Performance of fund products goes through cycles as well. In addition, this observation interferes with the not very much liked fact that 80 % of sales is typically achieved in 20 % of the product range, and that there might be huge differences in the kind of products that sell well in the home market, as compared to sales potential in a foreign market. From the perspective of a head of distribution, there is hardly a time when sales capacity matches demand: either one could sell much more, if and when performance, market demand, etc. are mounting quickly, or – with a time lag – one runs into the trap of having built up sales capacity, head counts, etc., and performance is turning into a weak phase, sales sluggish, and investors are preferring other asset classes.

As one result of these basic parameters, and considering the fact that sales staff is costing some money as well, typically a small sales force tries to reach out to as many potential investors as possible.

Fragmentation and Geography
The second factor that besets sales acitivites in Germany rootes mainly in history, i.e. the fragmentation and geographic spread of the investors landscape. There is not a single industrial, financial, or economic center (nor even just a few of them), and the principal offices of investors are geographically almost homogeneously spread all over the 360,000 square kilometers in every cardinal direction. The fragmentation is boone and bane: there is always lots to do, many to reach out to, a huge address list to work on, while of course making sales trips somewhat tedious, as travel costs, and more challenging, travel times are taking their toll on the local sales force.

Is not a clear focus on a particular group, a pre-defined 'tier-1' bracket of investors then the most natural management decision, and chasing the 'low-hanging-fruits' the right answer to this plethora of investor types? The problem of this kind of capitulation facing a daunting number of prospects is that it is quite a trodden path, and one to enjoy good company with hundreds of competing asset managers. Another point to bear in mind is that investor behaviour has changed somewhat, in that they tend to start business with new addresses with rather small amounts, beefing up their allocations after one, two, or three years of a successful

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cooperation. The sought-after 'fruits' are certainly not of the kind of five to fifteen million investments, but rather the big tickets – 100 to 200 million for example, quite infrequent events of a rare kind. Nothing to base a sales strategy on. The viable alternative is to attend to the 'tier-2' type of clients and engineer a systematic approach to get access to them.

Risk in Sales: Sales inefficiencies
That brings me to the third aspect, the risk-dimension of ill-advised sales approaches. The risk involved is that futile attempts to establish a profitable business base are detected only in hindsight, since there is no fair sales controlling, fitting the time horizon of most sales and marketing activities. This is aggravated, since there is no realistic full cost accounting when it comes to evaluating local sales operations. Even though we typically speak of three to five year time horizons, it is not unfair to state that many (hard) decisions on sales staff, branch offices, etc. are made within much shorter periods of time, like two years. There are two basic kinds of reaction: either the cost base is increased, new budgets given to implement new marketing measures, to hire new/more people, etc., or a frustrated withdrawal from a market, leaving nothing but sunk costs (and the wisdom that Germany is a difficult market). The risk of closing down a local operation is also to incur reputational effects, posing an obstacle to a market re-entry later.

Marketing and Brand Building: Everything under control?
What role does marketing and brand-building play in these situations? Naturally, these packages of measures do have more bearing on retail- and wholesale distribution, which is however not to say that in the institutional world they do not matter. The continuing vacillation between these distribution areas as a source of sales volumes, the rising intersection of Publikumfonds- vs. Spezialfondsinvestments, etc. all contribute to the extended importance of establishing a brand,

no matter which asset class or sales channel. The imperative to orchestrate marketing campaigns, to develop a brand, alongside with an 'industrialized' sales process, puts a strain to the economics of any non-local operation. Needless to add that the quality of what one achieves depends to a large degree on knowing the local mentality, which is also needed to differentiate between the many media, events, exhibitions, etc. Even well-adjusted marketing measures do have a mid-term time horizon to somewhat pay off, but there are many learning curves ahead.

Outsourcing: Rather sales than sorrow

Do all these considerations entail that it might be better to shun the German market, one of the biggest in Europe, at all? Certainly not. What I would rather suggest is to look out for ways of working this market not in a haphazard fashion, but to follow a professional, i.e. economic route. Following the arguments outlined above, what is the objective at hand: To manage shifts in market demand and sales potential over time; to effectively access all relevant client types, and not focus on the top-10 in each category, but establish a profitable business base by firing the broadside at the market; at the same time, to guarantee a floor to the cost base and not suffer reputational risks through high 'volatility' in your sales

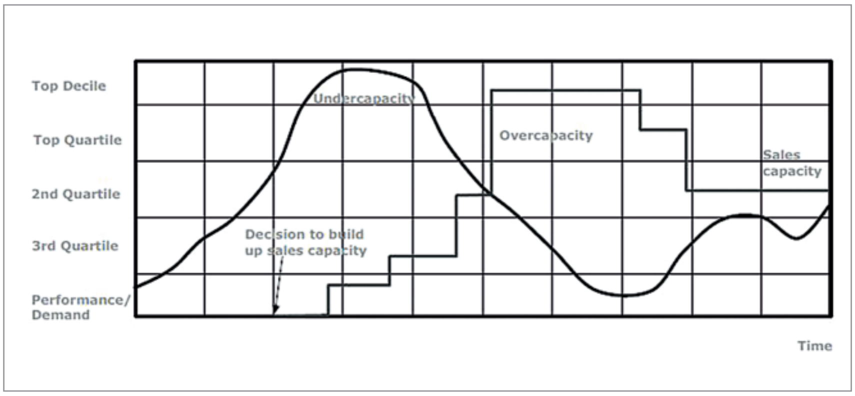

Abb. 1: Capacity

organisation; and, last but not least, support the business development strategy with a marketing and brand building campaign, adapted to the local clientele ('when in Rome, do as the Romans do!'). Let us consider, for a moment, developments in other segments of our industry, e.g. data management and software. Some twenty or twenty-five years ago, nobody would have considered to have an external person, someone not on ones payroll, to deal with software issues: the data would be considered as a treasure trove, to be protected from foreign eyes. Fear of too much transparency when looking at the workflows of an asset manager would have prevented to let somebody not on ones' own payroll do the job of, for instance, programming. On the contrary, to keep a software project inhouse would be considered rather unwise today. One can be sure that budgets will not be held, that time lines will not be kept, and the whole project is likely not to achieve the goals intended. Rather, to contract with a professional partner and outsource the objective is nowadays common procedure. It is possible to delineate within the contract time frames, budgets/costs, and implement incentive schemes to adhere to more than one economic dimension of the project.

When it comes to sales, outsourcing up until today did not seem to be an option. To pose as a solution provider and to be in complete control of the sales managers seem to prevent such a route. But these objections – in conjunction with the fact, that no institution was there to offer these services – resemble the reservations people had against outsourcing software projects or data management. A professional sales organisation would handle the client relationship in exactly the same way a 'captive' sales would do: relieve the fund management ('alpha production') as much as possible from the time consuming sales and client servicing tasks, while at the same time liasing closely with the investments specialists, fund managers, etc., if and when in a 'final'; increase the probability of securing the mandate substantially, when benchmarked with canvassing from door to door.

If we disregard for the time being that except for a few introducers and/or placement agents, whose activities resemble, but do not encompass the full gamut of services described above, hardly any offerings are in existence. What are the criteria to assess with whom and how to work with? Certainly people and their local expertises matter. Before kicking off the sales process, however, it is crucial to evaluate the business case: Is there a fit of product offering and demand? What sales channels should be targeted? What about competition? To answer, experience, market knowledge, network, and independence of the team contribute to the right solution. In establishing a cooperation, similar guidelines as in outsourcing any other duties should be considered, i.e. having a transparent contract, outlining the respective duties of the asset manager and the distribution organisation. The time horizon of the cooperation, the contractual specifications, and all that are also helpful in managing expectations.

Managing Expectations

As of today, outsourcing a local sales operation is not a very common thing. However, it might turn out to be the version 2.0 of non-domestic sales forays into foreign markets, particularly those that are difficult to access with small captive operations. Margin pressure and increasing competition force many asset managers to look beyond and realize growth options in other markets. No matter whether in the 'do-it-yourself' fashion or via outsourcing, it can be done in a much more economic and professional way than we have seen in the last couple of years.

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