Consolidation in Asset Management Industry

The Indian asset management industry has been experiencing tremendous growth, growing at a CAGR of 15.5% between FY08 – FY18. For FY18, assets under management (AUM) of mutual fund industry crossed INR 23 lakhs crores. Pace of growth in the assets is evident from the fact that industry's AUM had crossed the milestone of INR 10 lakhs crores for the first time in May 2014 and in a short span of about three years, the AUM size had increased more than two folds and crossed INR 20 lakhs crores for the first time in August 2017. Such a drastic growth is, of course, supported by zooming capital market.

The various positive aspects contributing to growth in asset management industry are increase in national savings, increase in awareness about mutual funds, penetration of mutual funds, higher returns from mutual funds as compared to other instruments, etc. However, with increasing regulatory requirements, disclosures and stiff competition, smaller players are facing the heat in the market. Considering AMCs business makes money in the long term and requires deep pocket during intermediate years, smaller AMCs might think of selling stake to foreign owned companies or merging with other players. Additionally, there are several issues such as building of distribution network, management capabilities, high marketing and distribution cost, compliant heavy processes, etc. which dampen the growth of small size mutual funds. It can also be said that running an AMC in India is not only about wide capital base but also about execution, the right kind of products offering, stable team and a brand recognition. Therefore, even some of the large foreign funds were not so successful in running mutual funds business in India and have exited the market long before. Some of the large foreign funds have joint venture with local mutual fund companies and together they are performing well.

While going for an acquisition or a merger, the target company and acquiring company considers several factors in terms of the synergies that they can derive from the consolidation process. Some of the major factors are augmentation of the AUM, increase the investor base, revenue and cost synergies, benefits of diversification which further reduces the risks in the business, displacement of inefficiency of fund managers across different schemes, to boost market share and the overall market for the inorganic growth of the company. Other additional factors also include access to new markets and new product development, attractive complementary product suite, enhancing the brand value of the acquiring company schemes, distribution strength, technology, leveraging fund managers' expertise, etc. Each factors' significance to the company will differ from company to company based on its market competitive positioning, perspective, plan and growth strategy.

Various mergers and acquisitions that took place in the mutual funds/AMC industry, throws out key management insights that went into evaluating those acquisitions. Some of the examples in which above mentioned factors were considered while making merger and acquisition decision are a) L&T Mutual fund buying the Fidelity India's asset management business - the perspective is that while L&T has larger debt assets, Fidelity has larger equity assets which would create a balanced asset base, and L&T has larger dependence on individual financial advisors whereas Fidelity has its dependence on other distribution channels b) Edelweiss Asset Management acquiring JP Morgan's mutual fund business in India with objectives to increase the AUM, enhance growth opportunity across the Edelweiss Group, technology, distribution and growth, attractive complementary advantages in terms of product suite between the schemes of both the funds and broadening of entire asset management platform. c) Birla Sun Life MF acquisition of ING AMC is another one. The objectives for this were to enhance AUM, increase the investor base, take advantage of expertise of fund managers and addition of different schemes that have shown good growth prospects. Another in the list is d) DHFL Pramerica Mutual Fund acquisition of Deutsche Bank's Asset Management Businesses. The benefits that DHFL ascertained were that it will be able to augment its product portfolio, distribution platform and client service resources, and enhance its leadership position in the AMC business. Finally, e) Kotak Mahindra AMC buying PineBridge Mutual Fund assets in India, in which the objectives were to provide further enrichment to Kotak's equity base, value enhancement and AUM expansion.

Although, there were synergies envisaged in each of the above transactions, but post the consolidation, whether those synergies materialized or not is a topic of discussion.

However, such consolidation is likely to be good for the industry due to the recent SEBI guidelines on consolidation of schemes within the mutual funds which has made the competition more intense. It is also likely to render smaller players ineffective to compete in the market. So, for smaller players to exist in the market it is better that they opt for the route of merger or acquisition by larger players in the market so that they derive the synergies from the larger players and vice versa. There would be a risk of appreciable adverse effect on competition due to presence of few larger players in the market as the expense ratio and exit load might increase for the investors. However, such a risk can be mitigated by SEBI issuing guidelines putting a cap on expense ratio and exit load when such event happens so that the investors don’t have to face the music. As the mutual funds industry growth is still in the nascent stage and if the existing investors get dissuaded from the market then it would become hard to attract new investors. Therefore, in a way to further augment the growth of industry in a systematic manner, it is expected that the consolidation in asset management industry would take place and benefit investors as well as market players.