THE CHANGING FACE OF INSTITUTIONAL GERMANY

The German institutional asset management market has long been considered complex, risk-averse and too driven by existing banking relationships to be attractive for international and/or independent asset managers. Changing regulations and tax laws, the introduction of AIFMD, the persistence of low yield and the advent of Solvency II are changing the face of this market and making it more and more attractive for third-party managers with the right approach and in-depth understanding of the opportunity.

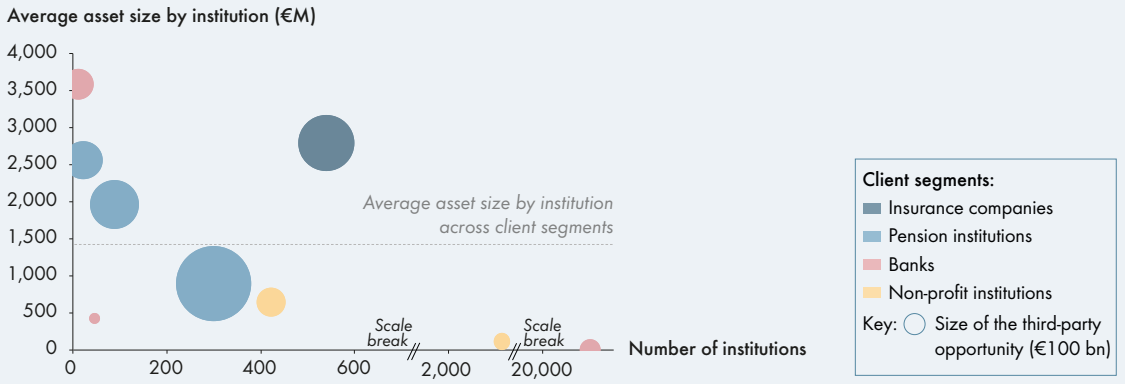
We have recently had the opportunity to update our regular analysis of the German institutional market, speaking to a wide array of market participants and investors[1]. The outcome of our analysis provides a clear picture of greater risk appetite, growing inclination towards private and other non-traditional assets and hiring non-domestic asset managers.

While traditionally open, pension-driven markets in the North of Europe (Netherlands, Scandinavia) are currently proving more challenging for international asset managers (cost pressure, switch to passive, reinsourcing), Germany is offering attractive growth opportunities and should take centre stage for a successful pan-European business development strategy.

COMPLEXITY IS A SMOKE SCREEN

The German institutional market is notoriously fragmented, opaque and hard to navigate. Superposing regulatory regimes govern different institutional segments. The use of wrappers to address regulatory and legal compliance or tax issues adds to the complexity. This should not be seen as a discouragement. It has acted as a barrier to entry for many players who have found easier routes-to-markets elsewhere for their products and services. The complexity has not gone away, but a lot of it remains outside the 'scope' of asset managers as it is handled through Master-KVGs or other service providers. Additionally, a more sophisticated asset allocation with exposure to non-traditional fixed income and illiquid assets has also brought a significantly increased willingness to use existing fund structures – rather than tailor-made mandates – lowering the barrier to entry to an increasingly broad group of asset managers.

A complex and fragmented market



Source: INDEFI.

GERMAN INSTITUTIONS ARE READY TO ASSUME RISK

The pressure to generate returns has forced a rethink towards the assumption of risk with certain asset classes benefiting more than others. A long-established familiarity with domestic private debt is translating into a wider allocation and outsourcing trend where German institutions can be seen to be playing a trailblazing role.

"You cannot keep the promise of a 4% yield if you only invest in traditional assets classes such as fixed income or equity. We, thus, increasingly feel forced to look at alternative asset classes including private debt." Versorgungswerk

"Private debt is a very attractive asset class. We have increased and diversified our investments in this asset class in the recent years so that, we currently hold senior loans in real estate, infrastructure, aviation and corporations." Corporate pension fund

"We just started to invest in private equity and private debt, implemented by two different external managers. So far, we have only invested a little amount but we plan to increase in the near future. We are open towards all alternative asset classes, investments in infrastructure are also possible. The main reason for our change of mind is the need for additional yield." Insurance company

1. Insurance companies, corporate and other pension institutions, non-profit institutions, banks.

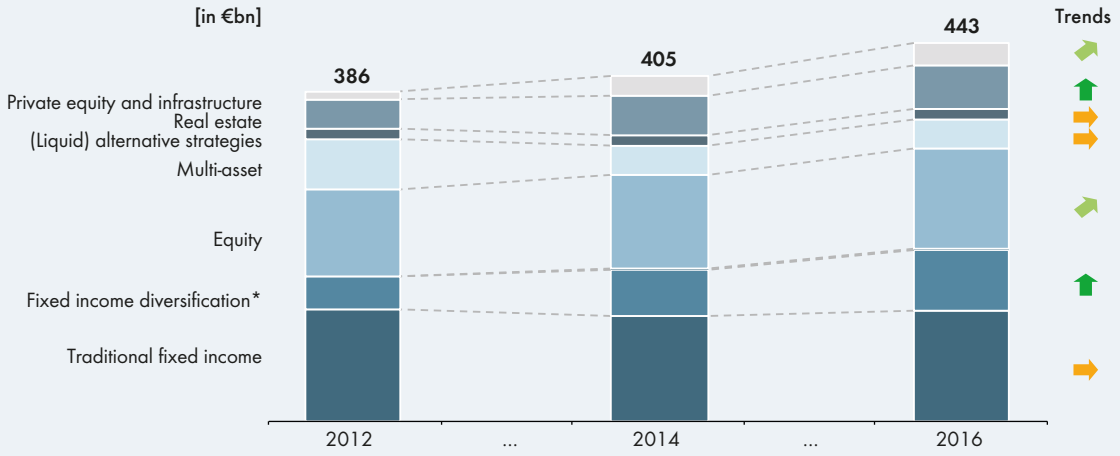
THE CHANGING FACE OF INSTITUTIONAL GERMANY

MORE OUTSOURCING AND OPEN-MINDEDNESS TOWARDS INTERNATIONAL ASSET MANAGERS

The appetite for non-traditional markets and asset classes has quite clearly translated into an accelerated penetration by sometimes unexpected players. Witness some remarkable success stories of non-domestic asset management firms which have gone from being entirely absent to having built an impressive book of business in only a few years.

Key ingredients include: recognised expertise in fixed income diversification, private assets, smart beta or other differentiated asset classes in demand, combined with a technically-proficient sales team, able to navigate the complex institutional landscape, and clearly mapped-out business development opportunities and priorities.

Breakdown of the third-party outsourcing market by asset class



Note: (*) Including high yield, emerging markets debt, international bonds, private debt. Source: INDEFI.

CONCLUSION

The European third-party asset management landscape is changing and the opportunity for business growth is undoubtedly shifting from pension-driven markets, traditionally seen as more open for international asset managers, towards insurance-driven markets.

We anticipate that the advent of Solvency II, the persistence of low yields, the assumption of more risk and the readiness to outsource will make Germany the cornerstone market for growth in third party delegation for the asset management industry for years to come.

ABOUT INDEFI

INDEFI is a strategy advisor for the investment management business in Europe. Our exclusive focus on top line growth in one industry, the use of our own field research and the skill diversity of our consultants form the bedrock of our consulting philosophy. This gives us an unparalleled vantage point from which we aim to serve our clients - asset managers, private equity and infrastructure investors (and their portfolio companies) - with understanding, insight and actionable advice. We provide strategic business growth advice to our clients which can cover markets, products, client groups and a combination thereof.

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Richard Bruyère
Managing Partner
+33(0)1 5688 3473
richard.bruyere@indefi.eu

Ric van Weelden
Senior Partner
+33(0)1 5688 3470
ric.vanweelden@indefi.eu

18, rue Royale 75008 Paris - France | **www.indefi.eu**

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