THE BIG PICTURE

Indian jewel in the fund crown loses its shine

International asset managers are struggling to make money in the country, finds *Attracta Mooney*

International asset managers in India are disappearing at an alarming rate.

Goldman Sachs Asset Management, the $1.19tn fund arm of the US bank, became the fourth global investment manager to quit the country last year. It announced plans in October to sell its mutual fund business to Reliance Capital, India's third-largest asset manager.

Just weeks earlier Belgium's KBC Asset Management said it would terminate its push into India with the sale of its stake in Union KBC Asset Management to Union Bank of India.

Fidelity Worldwide Investments, PineBridge Investments and the asset management arms of Morgan Stanley and Deutsche Bank have all sold their mutual fund businesses in the country over the past three years.

The fund houses are reluctant to discuss the reasons behind their exit, but analysts say India has not been the cash cow many asset managers expected.

Sze Yoon Ng, an Asia-based director at Cerulli Associates, the research company, says: "Most [foreign asset managers] are not making money."

Intense competition, regulatory uncertainty and problems getting fund ranges in front of end investors has meant is not unusual for a foreign asset manager in India to make a loss even after 10 years in the country. "It is hard to stay optimistic when your three-year break-even plan stretches to 10 years and counting," says Ms Ng.

Fund companies were initially tempted by India's growth story — its emerging middle class and strong economic expansion. Banking on a population of ready-to-invest consumers, asset managers kept coming to the country, say experts.

"Foreign asset managers saw potential in India: it is a huge country, with great demographics," says Daniel Celeghin, a partner at Casey Quirk, the consultancy. He has worked with asset managers hat have operations in India. "But you have to be willing to put a lot of time and effort in."

Franklin Templeton Investments is one of the few global asset managers to have cracked the Indian market. It set up shop 20 years ago and is now the only fully foreign-owned asset manager among India's top 10 fund houses.

Harshendu Bindal, president of Franklin's operations in India, says many foreign asset managers came to the market too late and failed to understand the nuances of the country's "hyper competitive" mutual fund industry.

The market is dominated by just a handful of asset managers. The 10 largest fund houses account for more than 77 per cent of the $200bn of assets under management in India. Lakshmi Iyer, head of investments and product development at Kotak Mahindra Asset Management, the ninth-largest investment manager in India, says the concentration of assets among the top providers "increases the time taken to break even" for entrants.

Rather than go it alone, several international asset managers have tried to gain a foothold in India by partnering with local banks and other financial institutions to create mutual fund businesses.

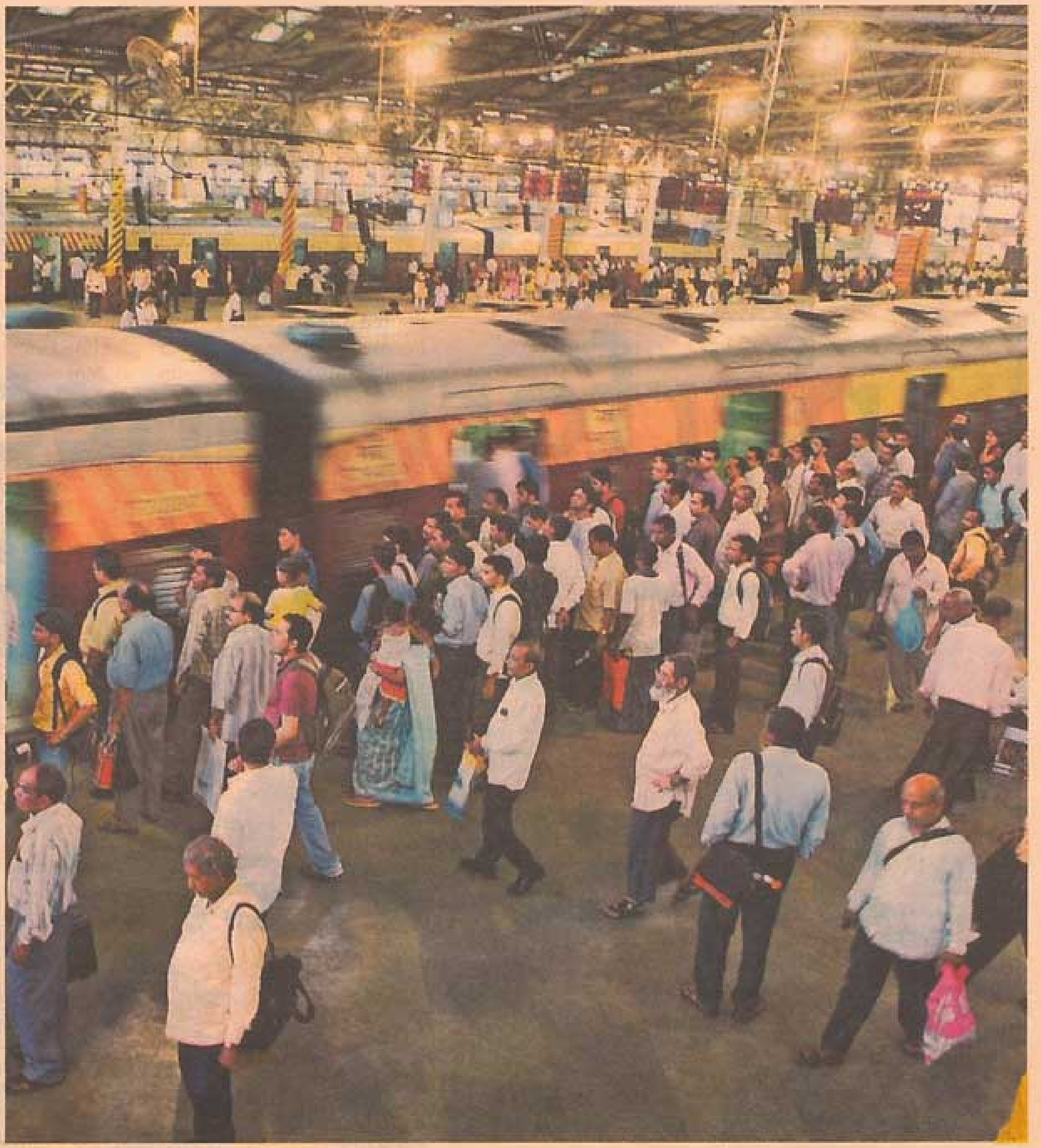
India's biggest asset manager, HDFC Asset Management, is a joint venture between Standard Life Investments, the UK fund house, and HDFC, a bank. Prudential, the UK-listed insurer, and local provider ICICI Bank operate ICICI Prudential Asset Management, India's second-largest asset manager. BlackRock and Amundi Asset Management also have joint ventures in the country.

But international fund houses frequently find joint ventures difficult to navigate. "You have to realise you will be junior partner to a local firm," says Mr Celeghin, adding that this is something global asset managers are uncomfortable with.

Foreign asset managers face several other challenges, including being unable to sell international products, such as mutual funds regulated in Europe. Instead, they need to set up local funds. These are typically focused on Indian stocks and shares, partly because of restrictions on what can be sold to retail investors. "If you want to do business in India, you need to have an investment team in the country to create and run a fund, and that is costly," says Mr Celeghin.

Distribution can also be an obstacle. Banks tend to favour the products of their own asset management arms, according to Cerulli. Meanwhile, the regulatory landscape for financial advisers, which control around 30 per cent of the mutual fund market, has been in flux.

In 2009, the Indian regulator introduced rules for mandatory disclosure of rebates — money paid from asset managers to financial advisers to entice them to sell their products. This was later overturned. The Securities and Exchange Board of India has also mooted phasing out commissions entirely, but this looks unlikely at the moment.



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The number of fund houses that account for more than 77 per cent of the $200bn of assets under management in India

Patience is the key
The secret of Franklin Templeton's success

While one international asset manager after another has fallen away in India, Franklin Templeton Investments appears to have found the recipe for success.

It was one of the first international fund companies to enter the country, setting up after the government announced plans to allow non-banks to manufacture mutual funds in the early 1990s.

Harshendu Bindal, president of Franklin Templeton in India, says its early foray played an important role in helping it become the country's seventh-largest asset manager.

"We are one of the oldest fund houses in the country, with a 20-year record, which gave us a long head start [on other foreign asset managers]," he says.

The fund house, which manages $25bn in assets in India, set up a range of local funds, introduced trail-based commissions to incentivise distributors to sell its products and launched various savings products, such as its Family Solutions range, in order to win business.

Patience is vital to success in India, says Mr Bindal. "A fund house may need anywhere between five and seven years, or at times even a decade, before it turns profitable."

THE BIG PICTURE

India's largest asset managers: the power of a local name

Source: Cerulli Associates

Fund companies were tempted by India's growth story, its emerging middle class and strong economic expansion
Subhash Sharma/FT; Kuni Takahashi/Bloomberg

"The business environment is one where the rules are changing frequently. It is hard to get clear guidance on what twist or turn can be expected in the future," says Mr Celeghin.

Ajit Dayal, chairman of Quantum Asset Management Company, which sells funds directly to investors, says: "While [the regulator] is trying to force the industry to adopt a more transparent practice, the distribution industry is dominated by large banks and brokerages and it is not in their interest to necessarily have a more competitive market."

As a result, foreign asset managers have struggled to mop up assets. Goldman Sachs's Indian fund business had just $1.1bn in assets under management when it announced plans to sell its mutual fund business.

> 'If you want to do business in India, you need to have an investment team in the country to create and run a fund, and that is costly'

But Franklin's Mr Bindal says fund houses that depart are missing a big opportunity. Despite the challenges in the country, India's fund industry is growing rapidly. Since March 2012, the market for Indian mutual funds has almost doubled in size, according to data from the Association of Mutual Funds in India, the local trade association.

He believes investment companies just need to work harder. "India is truly an attractive market for asset managers," he says.