2013 SURVEY OF THE ASSET MANAGEMENT INDUSTRY

Operations and Compensation Metrics and Best Practices

Selected Highlights

INVESTMENT ADVISER ASSOCIATION

INTRODUCTION

Having recovered from the financial crisis in fits and starts, the asset management industry appears to have finally regained its footing. Economic stagnation, political uncertainty, global unrest, and market volatility all took a back seat as equity markets surged in 2012, lifting the value of assets under management. Asset growth was driven largely by market appreciation rather than new asset flows from investors, which didn't begin again in earnest until early 2013. Larger firms tended to see more growth than small ones, but median asset growth across all firms in the survey was an impressive 9.5%.

Fee realizations slipped along with a widespread shift toward lower fee asset classes or investment vehicles, but asset growth meant higher revenues for most firms. Improvements to profitability were less uniform. Hiring and spending on technology and operations are accelerating once again after a dip in the previous year, denting profit margins at some firms as they aim to position themselves for another phase of growth.

Some firms are preparing themselves in other ways, by expanding their breadth of product strategies managed or packaging their expertise in new vehicles. The globalization of portfolios continues, for example, most recently manifesting itself with a newfound emphasis on international fixed income. A focus on yield is also evident as firms look to add fixed income derivatives and real estate to their client portfolios.

Note to Readers

This document contains selected highlights only. Survey participants receive an in-depth 40 page report along with a full set of data tables tabulated by asset size (see below).

Please refer to the end of this document for more information on the contents of the full report as well as information on how to participate in the next survey.

AUM Peer Groups

Group	AUM
XL	$5B+ AUM
L	$2B - $5B AUM
M	$1B - $2B AUM
S	$500m - $1B AUM
XS	<$500m AUM

With increasingly sophisticated models, more extensive research, heightened client expectations, and growing regulatory demands, the technical infrastructure required to run an investment firm is increasingly complex. Firms are responding by upgrading systems, hiring personnel, and ensuring that they hold onto their existing employees by offering appropriate benefits and structuring their compensation plans competitively. Seven out of ten employees at firms surveyed in 2013 saw their compensation rise from the prior years, with the biggest gains often seen at the most senior levels, which had largely been bypassed in the earlier phase of the recovery. Barring any serious market disruptions, the war for talent is likely to pick up once again.

This periodic survey is conducted by the Advent Users Group (AUG), an independent organization of Advent product users, to provide leaders in the asset management business with the data and insights necessary to make informed decisions. Last carried out in 2012, the survey once again delves into an array of topics ranging from technology budgeting and operational practices to personnel policies and employee compensation (See Figure 1).

Advent Software and the Investment Adviser Association co-sponsored the 2013 survey, in which 109 firms participated. The results represent one of the most comprehensive sets of industry metrics available. We are grateful to all those who took the time to participate. Your contribution is greatly appreciated, and we hope you find the results informative and useful as you plan for your firm's future.

SELECTED FINDINGS

PRODUCT TYPES

Domestic equities remain the most commonly managed asset class, but international equity continues to find more users. Portfolios are decidedly less exotic than a year ago, with fewer firms reporting the use of private equity, hedge funds, or derivatives. Bank loan products ticked upward, in line with broader industry trends. Approximately 15% of firms in the survey say they plan to add new asset classes within the next year. Most are focused on globalizing portfolios, with a newfound emphasis on international fixed income.

FINANCIALS

Market appreciation drove widespread asset growth in 2012. While financial performance generally improved, growth eluded a growing number of firms. Larger firms typically saw more asset growth than small ones. Asset growth resulted in revenue gains for most firms, with 84% reporting higher revenue than a year earlier. Median revenue growth was 5.0%, but ranged significantly from one firm to another (Figure 1). While those in the top quartile saw revenue climb by 15.3% or more, those in the bottom quartile saw no improvement. It should also be noted that this gain also represented a slowdown from the previous two years, in which median revenue gains of 16% (2010) and 10% (2011) were reported.

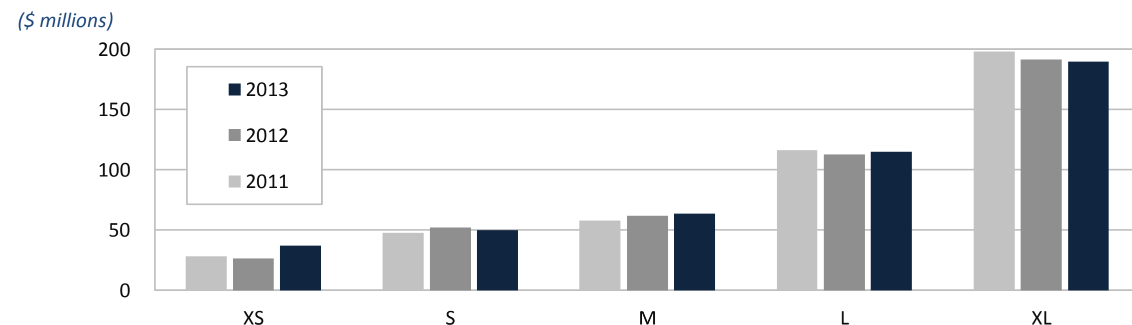
Figure 1. Revenue

Median $000s	ALL	XL	L	M	S	XS
2011	5,670.0	28,319.0	11,420.0	7,150.0	3,731.0	1,305.0
2012	6,217.0	33,500.0	12,635.0	8,500.0	3,738.0	1,362.5
1 Year % Δ	5.0	3.4	10.4	4.6	6.3	0.0

PERSONNEL

Economies of scale are clearly visible when AUM per employee is compared across peer groups. The largest firms report a median $190 million of AUM per employee, compared to $37 million per employee at the smallest firms surveyed. Nevertheless, the smallest organizations saw the biggest gains over the past year. Larger firms saw this particular metric remain relatively static as increased hiring took its toll on overall productivity (Figure 2). The efficiency stemming from large scale operations usually trickles down to the bottom line. The largest firms participating in the survey reported an average EBITDA per employee of $278 thousand, compared to the $48 thousand recorded by the smallest firms.

Figure 2. Median AUM per employee over past 3 years



IT AND OPERATIONS BUDGET

Spending on technology and operations is accelerating once again after a dip in the previous year. With seven out of eight firms reporting higher IT budgets than a year earlier, average spending rose by almost 17% (Figure 3). Double digit increases were common but particularly pronounced at the smallest firms, which can face substantial costs relative to their size when building out infrastructure from such a small base.

Slightly more than half of all respondents to the survey say they think disaster recovery initiatives are causing IT costs to rise, but this represents a decline from a year ago. Network security, on the other hand, is increasingly seen as a driver of higher costs. Other areas attracting significantly more attention as cost drivers include client reporting, mobile access, and knowledge management efforts. Data warehousing is an example of an area that was previously seen by more firms as a major contributor to higher costs, but has since become less prominent.

Figure 3. Current and projected IT and operations expenses

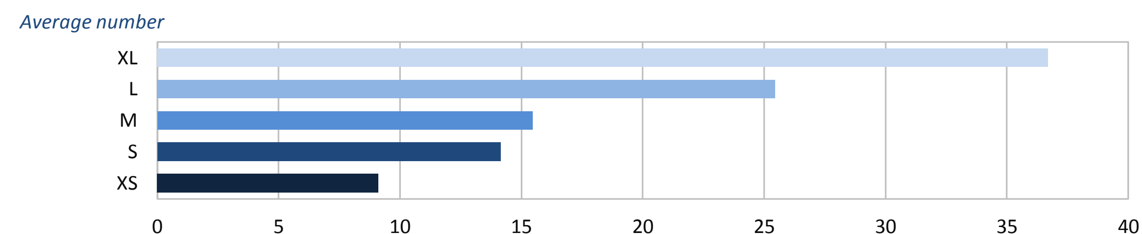
Average $000s	ALL	XL	L	M	S	XS
2012	600.8	1,362.8	557.3	978.9	281.7	150.1
2013 (est.)	677.4	1,533.6	589.7	1,139.9	288.0	199.1
% change	16.6	12.9	12.9	15.6	4.3	34.3

TRADING AND SETTLEMENT

While the average number of brokerage relationships rose across most AUM cohorts, the largest firms continue to prune the number of brokerage houses with whom they do business. The same cannot be said about custodians and prime brokers. Firms in the survey now deal with an average of 19 custodians and prime brokers on a regular basis (Figure 4). This is a significant increase from a year ago. The increase was widespread, occurring in firms of all sizes except the very largest.

Figure 4. Number of custodians and prime brokers dealt with on ongoing basis

Average number



Clients often have multiple portfolios with the same manager or advisor. An average of approximately five portfolios per client was reported across all firms, with a median of two. Operational complexity and costs have a tendency to increase with the number of portfolios involved, and the scale of the challenge is evident when one considers the sheer number of distinct portfolios involved. Firms with more than $5 billion under management reconcile and maintain an average of more than 3000 portfolios on their systems. The average across all firms is almost 1600 portfolios. Despite the additional operational burden larger firms often gain something back in the form of scale. Median assets per portfolio across all firms are $1.5 million, but this ranges from $680,000 at the smallest firms up to $16.2 million at the largest organizations.

ACTIVITY METRICS

After widespread efficiency gains in 2012, there was some slippage in 2013. Operational tasks like reporting, reconciliation, and billing all took longer this year than they did a year earlier (Figure 5).

Figure 5. Investment operations activity metrics

Median	ALL	XL	L	M	S	XS
Hours per month spent reconciling	40.0	45.0	75.0	40.0	30.0	20.0
Hours per quarter spent on reporting	50.0	80.0	74.0	40.0	30.0	50.0
Hours per quarter generating bills and tracking receivables	22.5	40.0	40.0	26.0	20.0	12.5
Business days after quarter end to complete all reporting	12.0	15.0	15.0	10.0	12.0	10.0
Business days after quarter end to invoice all accounts	15.0	15.0	15.0	10.0	15.0	10.0

WEBSITES & SOCIAL MEDIA

Despite the prevalence of social media and considerable discussion about its use in corporate settings, it has not caught on in any meaningful way with investment firms. Two out of three firms in the survey say they use no social media of any kind. Even LinkedIn is used by less than 30% of firms.

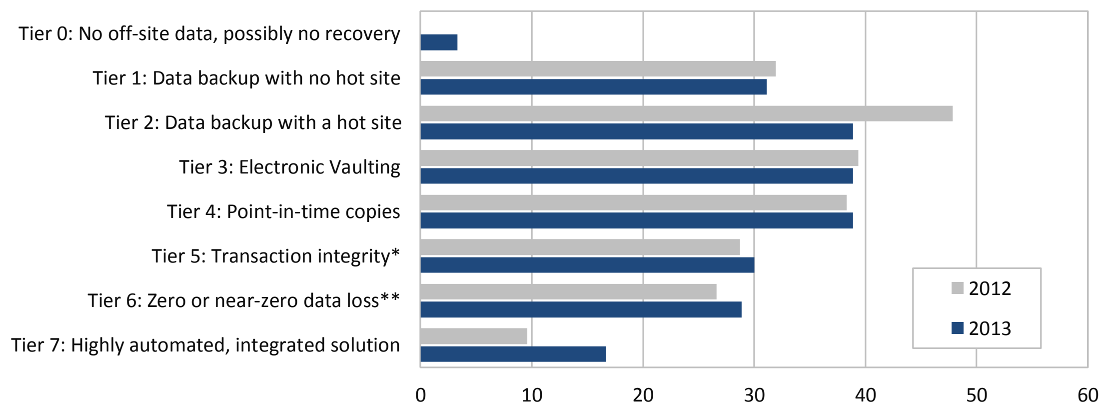
Social media's low rate of penetration among investment firms stems from the lack of a clear value proposition. Regulatory issues remain a significant obstacle to a more widespread embrace of social media by investment firms. Despite widespread ambivalence, more firms are getting prepared by establishing firm-wide guidelines for social media use. Almost 87% now say they have such guidelines in place, compared to only 83% a year earlier and less than 60% two years ago.

DISASTER RECOVERY

Business continuity is of critical importance to investment firms. Disaster recovery is consistently ranked as a top budget priority, and the bar continues to be raised as firms upgrade their systems and processes to minimize any potential disruption to their businesses. Higher tier solutions are being deployed more widely, and 17% of firms now report having Tier 7 solutions, meaning that disaster recovery is addressed in a highly automated fashion via an integrated solution (Figure 6). This represents a significant increase from the prior year. Tier 4, 5, and 6 solutions also saw broader adoption.

Figure 6. Disaster recovery solutions currently employed

% of respondents



** Host-based replication*

*** SAN-based replication*

EMPLOYEE BENEFITS

Almost all firms participating in the survey offered health insurance to their employees. Dental plans are less common, and vision insurance even less so. All types of insurance are more commonly found at larger companies. Family members of employees are usually covered by insurance plans, but premiums are sometimes subsidized to a lesser degree than they are for employees.

Health savings accounts (HSAs) and cafeteria plans are each currently offered by approximately half of all firms surveyed (Figure 7). Cafeteria-style plans are more commonly found at larger firms, where up to six options are offered. These tax-advantaged accounts will remain available under Obamacare, but they will be subject to new limitations and requirements, so it remains to be seen how popular they will be going forward.

Figure 7. Flexible health plans

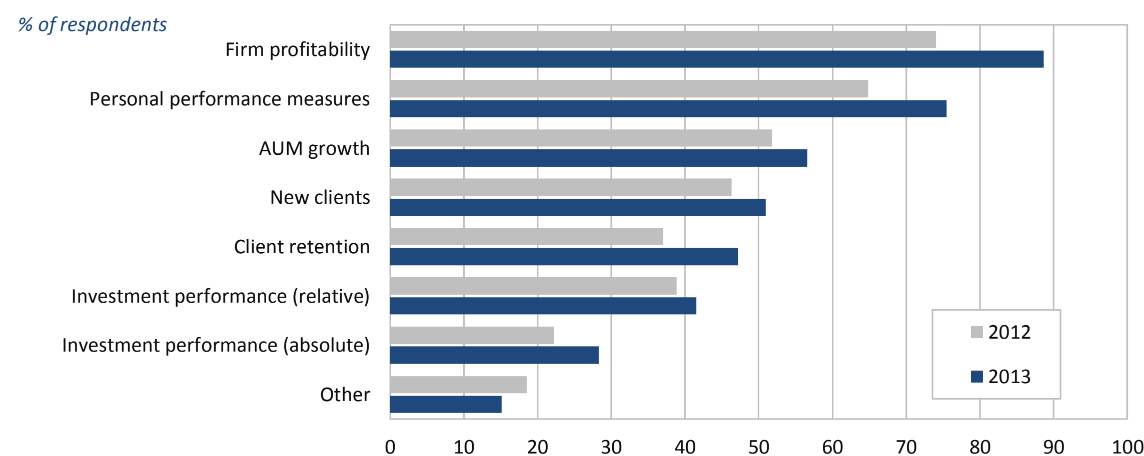
% of respondents	ALL	XL	L	M	S	XS
Health savings account (HSA)	45.8	45.5	57.9	40.0	53.3	33.3
Section 125 cafeteria plan	51.8	90.9	57.9	55.0	33.3	33.3

COMPENSATION STRUCTURE

Investment firms structure compensation packages in a wide variety of ways, but the one thing most have in common is a large variable component. In a business where personal or team performance as well as the market environment can easily have significant effects on a firm's fortunes for better or worse, it makes sense that the vast majority of firms would rely heavily on annual cash bonuses. Over half also have a profit sharing plan in place. Long-term incentives are less common.

Discretionary bonuses are the norm in the investment industry, but some firms rely on objective measures to determine bonuses in part or exclusively. The popularity of quantifiable metrics rises and falls along with the business climate. In volatile or uncertain environments, subjective measures prevail. A more stable environment lends itself to objective measures. Overall firm profitability remains the most often used metric when awarding bonuses, followed by personal performance measures and asset growth (Figure 8). Profitability is often used to determine the size of the bonus pool before allocating awards based on measures of personal or team performance.

Figure 8. Objective (non-discretionary) measures used to award incentive pay



COMPENSATION DATA

Detailed compensation information was collected for forty-one positions ranging from CEOs to receptionists. Salary information, incentive pay, and ownership distributions were captured to arrive at total compensation figures. Other pieces of information captured at the individual level include experience level and how compensation compared to the previous year. Compensation data was gathered for more than 1,600 individuals.

Seven out of ten individuals (excluding new hires) saw their compensation rise from a year earlier. Most of the remaining individuals saw no change in their total compensation, and fewer than one in ten experienced a decline.

The size of compensation packages is correlated to firm size for some, but not all positions. Senior executives in particular are more likely to be paid more at larger firms. Even in their case, the correlation between firm size and overall pay is not particularly strong, with considerable variation within AUM peer groups.

Other factors affecting compensation levels include the type of firm and types of products under management. Firms identifying themselves as asset managers, for example, pay their CEOs slightly more than firms identified as independent RIAs. More significant is the presence of alternative investment strategies. Firms managing alternative products alongside traditional strategies paid their CEOs an average of 15% more than long-only firms.

Professional designations can also make a difference, particularly in the compensation of senior executives. Leaders with multiple designations (e.g. MBA, CFA, and PhD) are generally paid more than those with one or less.

The majority of senior executives had pay increases, but they were also more likely than any other group to see compensation fall from the previous year. More than one in four CEOs, for example, experienced declining compensation. Still, strong growth at the upper end of the pay scale meant average compensation rose to new highs well above the 25th percentile for CEOs and CIOs.

Approximately two thirds of investment professionals reported higher compensation than the previous year, a significantly smaller proportion than the previous year. Their gains also tended to be more modest than those seen by senior executives. Compensation levels among investment professionals are not closely tied to asset size. It is not unusual for portfolio managers at small firms to make more than their colleagues at much larger organizations, oftentimes because they are also a member of the senior management team.

Sales and marketing professionals generally saw their compensation rise, for the second consecutive year. Dedicated sales and marketing staff are much more common at larger firms. Distribution functions at small organizations are often handled by individuals playing other functional roles in investments or business management Operations staff saw the most widespread pay increases of any group. Employees at larger firms tend to command higher pay packages, but the difference is only pronounced at the largest organizations.

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