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Bank sales of investment trusts and diversifying consumer needs

Nomura Research Institute, Ltd.

Banks have overtaken securities companies as the leading sellers of investment trusts and now account for 40% of assets under management at these funds. However, there are emerging signs that being a bank no longer guarantee success in this market. As consumer needs grow more diverse, product lineups and the ability to propose products tailored to customer needs may come to figure more prominently in the sales performance of individual lenders.

Era of assured growth in bank sales of funds may be ending

After topping 60 trillion yen in 2000, investment trust assets fell to just 34 trillion yen in 2003 after the dot-com bubble burst and the stock market collapsed. By the end of June 2006, however, assets had recovered to 59 trillion yen.[1] In addition to the economic recovery and rising stock prices, which certainly played a role, the growth in assets during this period was driven by bank sales of investment trusts.

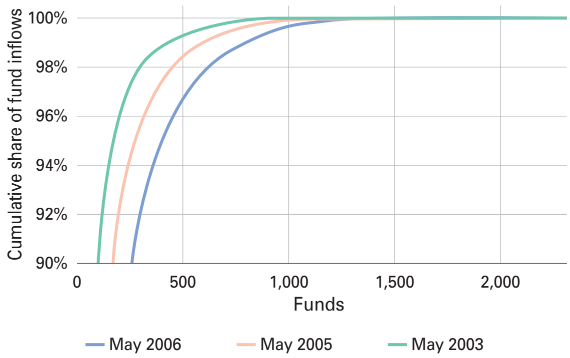
Since the ban on such sales was lifted in 1998, banks' importance as a retail distribution channel has increased from year to year. Banks now account for about 40% of all investment trust sales. But now there are emerging signs of a shift in banks' dominance over securities companies—while bank sales of these products are still rising, growth in market share has begun to slow. If it is accepted that aggregate bank sales are unlikely to continue growing at past rates, we need to examine the specific factors that will affect the performances of individual lenders.

Consumer needs have grown more diverse

There are more than 2,000 publicly offered open-end investment trusts sold in Japan today. The number is even larger when unit trusts are included. That said, only a small number of these trusts are actually bought and sold. Older funds in particular tend to see very few transactions, with most funds flowing into new trusts.

Exhibit 1 looks at the distribution of inflows to such funds in May 2006, May 2005, and May 2003 by examining the leading funds' (in terms of inflows) share of total inflows. In May 2006, for example, just 250 open-end trusts, or roughly the top decile, accounted for 90% of inflows to the entire market, highlighting the extent to which money tends to concentrate in a handful of vehicles.

Exhibit 1. Distribution of fund inflows to open-end investment trusts



Source: NRI, based on Fundmark data

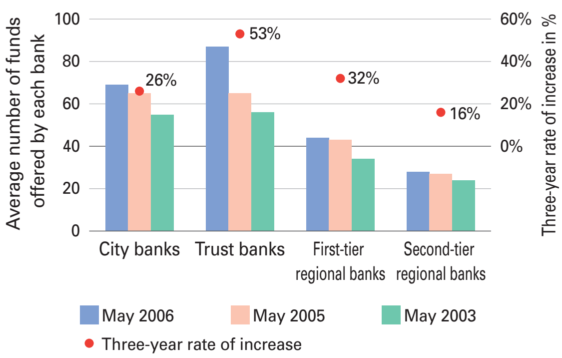
Nevertheless, fund inflows have diversified substantially since 2003, when assets in investment trusts turned up after a long decline and the top 100 funds accounted for 90% of inflows to the market. Whereas three years ago investment trust distributors were able to satisfy the needs of most customers by offering only 100 funds, now they must offer 250.

Product lineups vary from bank to bank

The bank staff responsible for selling investment trusts have differing views on the need to expand product offerings. Some believe that selecting the right funds is more important than simply increasing the number of products on offer. Others say that offering more funds will not necessarily lead to higher sales because sales staff will be unable to explain all of the products. Partly because of these views, not all banks are moving to bolster their product lineups. Still, some banks have worked hard to offer more funds, leading to a growing disparity in product mixes.

Exhibit 2 compares the average number of funds offered by various types of banks at the three points in time noted above.[2] At first- and second-tier regional banks, we looked only at the 10 lenders with the most investment trust assets (as of May 2006) because these institutions were thought to be devoting significant resources to the sale of investment trusts. The comparison highlights the fact that smaller lenders tend to offer fewer products. One factor contributing to this trend is that smaller banks find it more difficult to build a sales organization, including fund selection and the training of sales staff. In addition, a look at the average number of funds sold by various types of banks shows that trust banks recorded the highest growth rate over the last three years, while the lowest gains were registered by second-tier regional banks. Accordingly, although the number of funds on offer increased in both groups, the disparity in growth rates meant that the gap between the two widened steadily over the three-year period. This growing disparity in product offerings can also be observed between banks in the same category.

Exhibit 2. Funds sold through banks



Source: NRI, based on 14 July 2003, 11 July 2005, and 10 July 2006 issues of *Nikkin Toshin Nenkin Joho*

Until recently, the vast majority of assets were concentrated in relatively few funds, making it easy for banks offering a small lineup of products to produce respectable sales figures. This may be why lenders, with their numerous points of contact with customers, were able to dominate the market despite offering fewer funds in many cases. Product strategies have always been important, but as consumer needs grow more diverse it has become increasingly important for banks to offer a wide range of products. The first wave of fund sales to existing customers is largely behind us, and signs of a slowdown in the growth of banks' market share have begun to appear. We think bank sales performance will start to hinge on a number of new factors, including diverse product offerings and the ability to propose solutions tailored to customer needs.

Note

1) Based on data from the Investment Trusts Association.

2) City banks include Mizuho Bank, Bank of Tokyo-Mitsubishi UFJ, Sumitomo Mitsui Banking, Resona Bank, Saitama Resona Bank, Shinsei Bank, and Aozora Bank. Trust banks include Mitsubishi UFJ Trust & Banking, Mizuho Trust & Banking, Chuo Mitsui Trust & Banking, and Sumitomo Trust & Banking. First-tier regional banks include Chiba Bank, Bank of Yokohama, Bank of Fukuoka, Kinki Osaka Bank, Joyo Bank, Nishi-Nippon City Bank, Gunma Bank, Hokuriku Bank, Chugoku Bank, and Ashikaga Bank. Second-tier regional banks include Minato Bank, Kansai Urban Bank, Tokyo Star Bank, Keiyo Bank, Hokuyo Bank, Nagoya Bank, Towa Bank, Momiji Bank, Aichi Bank, and Kagawa Bank. In the case of past mergers, the pre-merger entities are also included. The number of funds includes publicly offered open-end and unit trusts sold by the banks in May of 2006, 2005, and 2003.

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