America's top 300 money managers

With internal growth increasingly difficult to produce, money managers are rethinking size — despite the merger mania.

DESPITE THE RAPID PACE AND EVER-increasing size of money management acquisitions, the industry still shows only modest signs of concentration, particularly at the top. Although assets grew smartly at the largest firms, the giants have a long way to go to achieve true market dominance.

At the end of 1997, the top 300 money management firms ranked by *Institutional Investor* ran some $12.9 trillion in assets for third parties — up 21.7 percent for the year. The ranks of the ten biggest firms, led for the sixth consecutive year by Fidelity Investments, shifted slightly, and as a group their market share rose by 3.75 percentage points, to 31.07 percent. Consolidation played a larger role in the next tier: The top 25 firms boosted their combined share from 47.6 percent in 1996 to about 53.8 percent in 1997.

Mergers accounted for most of the increase in assets under management of the top 20 players. Merrill Lynch & Co. leapfrogged from eighth place to third after its $5.3 billion December deal with London-based Mercury Asset Management nearly doubled its assets, to $446 billion. Bankers Trust Co.'s acquisition of Alex. Brown & Sons added $13.7 billion to its assets and moved that firm up three slots, to sixth place, with $317.8 billion. Morgan Stanley Group's $10 billion deal with Dean Witter, Discover & Co. boosted its assets by $90.4 billion and its rank by eight notches, putting Morgan Stanley Dean Witter in ninth place.

But looks are deceiving. In a year when the Standard & Poor's 500 index rose 33 percent, the industry's gains were largely the result of soaring stock prices. Nor did everyone grow at that rate. Bond accounts added little in the way of market performance to totals, and new business was hard to come by.

Indeed, internal growth seems tougher to generate. It's hard to grow fast off a broad base, particularly for firms that have just merged. But companies have also seen the effects of one asset class cannibalizing another, slackening growth of defined benefit flows and less net new business from related industries like banking. Several major players therefore contend that the U.S. industry is maturing. Fidelity could attest to that fact: Assets at the No. 1 U.S. money manager grew by about 21 percent last year, but only about 3 percent of that gain came from net new business. In coming years, according to the investment banking firm of Putnam, Lovell, de Guardiola & Thornton, the asset pool will grow by about 12 percent annually, based on an assumption of 8.5 percent market appreciation.

By such a rule of thumb, Fidelity's 1997 showing was poor, since it generated less than a fifth of its growth internally. Barclays Global Investors grew 26 percent, and internal growth ran 7.3 percent. Mellon Bank Corp. similarly generated 9 percent growth internally (overall it grew 21 percent). Among the biggest players, only State Street Global Advisors and Bankers Trust gained new business at a double-digit pace, with the former racking up 18 percent internal growth (32.3 percent overall), while the latter gained 17 percent (of 40 percent).

Do these signs of maturity portend anything? Several top money managers conclude that only the firms least interested in size for its own sake will generate real internal growth long term. As assets expand, they say, clients are growing more sophisticated, increasingly aware that portfolio size can erode performance of even the best money managers, particularly in active equity management. Some money managers are therefore also shifting their focus. New mandates look at size as well as the performance and profit prospects of the asset classes a firm offers.

At indexer Barclays Global Investors, CEO Fred Grauer certainly pursues a strategy based on size. "The more revenue you generate relative to fixed costs, the higher the profits will be," he notes. Size, distribution and brand name, he adds, all help boost revenues and profits.

But even at mighty Fidelity, size no longer seems quite as paramount. "Assets are very important," says Robert Reynolds, president of Fidelity Investments Institutional Retirement Group. "But they're not the sole determinant of success. If one firm grows by $10 billion, you have to look at what they paid for that growth and what they earned from it."

Barclays' Grauer agrees, but for different reasons. "Size is important for economies of scale and in securities lending, which needs both a broad and deep client base and inventory," he says. "But when it comes to active management, we're not looking for market share that eliminates alpha. We want a dominant market share in our asset classes by virtue of the sum of what we do. We have to be the best at bringing *new* value-added products to market." Alpha, of course, is outperformance over a benchmark. Without that, sophisticated investors in all but straight index products are quickly turned off.

Grauer argues that difficulties loom as investors' wealth outstrips the ability of active managers to absorb new assets efficiently. "In active management," he says, "the game is to grow through diversification so that you don't feed off the same alpha source, and that's a tough game, because alpha ideas do not grow on trees."

Several firms have evolved the multimanager philosophy pioneered by United Asset Management Corp., No. 20, with exactly that diversification strategy in mind. The difference: Newer entrants do not generally fully own their boutiques as UAM does — preferring to leave ownership incentives partly with the money managers who run the firms. Boston-based Affiliated Managers Group has bought partial ownership in 11 firms since it was founded in 1993 and went public last year, raising $187 million. Today AMG (ranked No. 81) owns pieces of everything from quantitative manager First Quadrant to value manager Tweedy, Browne Co. and presides over assets of $54.3 billion. Boston-based Quadra Capital Partners launched a similar strategy in 1995, but its five affiliates pool only central marketing capability, client service and portfolio analysis — and each one, together with Quadra's principals, actually owns a piece of the parent. And Value Asset Management in Westport, Connecticut, headed by former Chancellor LGT Asset Management president David Minella, has started up a similar venture whose three affiliates now run $8 billion.

One key to the newest business strategies: Avoid trading outperformance for size. Even some of the largest players condemn driving growth solely through acquisitions. "We have demonstrated a real ability to get true new growth," says William Cvengros, the chief executive of Pimco Advisors Holdings. "And we will look at new acquisitions. But we're not searching for growth for growth's sake. Others who don't have the ability to grow internally need to do that. We do not."

Neither, seemingly, does Bankers Trust. "We do not focus on assets under management but instead on revenues and profits," asserts Jeremiah Chafkin, whose $250 billion quantitative unit was separated last year from Bankers' active business. "In the U.S. and globally, the market is getting much more sophisticated," he says. "And that's why we decided to restructure and to have one unit to focus on structured products — indexing, quantitative active and portable alpha products. We've staked out the intellectual high ground."

With more tightly focused businesses, Bankers has been able to market both units more effectively. Sales took off as mutual fund groups such as AMR Investment Services, Scudder Kemper Investments and Fidelity bought BT private-label indexing products; insurance giants like Equitable Cos., Travelers Group and American Skandia Life Assurance Corp. have also become BT clients. "Vanilla indexing is volume-driven," Chafkin notes. "There are high fixed costs and terrific efficiencies once

Rank			Total assets under management ($ millions)		1997 Portfolio mix ($ millions)							Tax-exempt assets under management ($ millions)
					Equities		Fixed-income securities					
1996*	1997	Firm	12/31/97	12/31/96	Dom.	For.	Dom.	For.	Cash and equivalents	Real estate	Alternative investments	
1	1	**Fidelity Investments** (Boston, MA)	**$625,864**	$515,518	$402,763	$ 49,066	$65,262	$ 1,704	$104,589	$2,480	—	$349,654
2	2	**Barclays Global Investors** (San Francisco, CA)	**485,771**	385,449	264,160	125,142	44,551	23,986	27,788	—	$ 144	462,566
8	3	**Merrill Lynch & Co.** (Plainsboro, NJ)	**446,279**	234,060	68,448	155,056	74,692	39,832	108,251	—	—	33,841
		Hotchkis & Wiley	12,249	10,113	8,540	2,721	988	—	—	—	—	12,086
		Mercury Asset Mgmt	167,529	—	2,704	124,737	4,328	35,760	—	—	—	—
		Merrill Lynch Asset Mgmt Group	230,418	198,037	54,620	26,344	56,828	1,383	91,243	—	—	12,066
		Merrill Lynch Capital Mgmt Group	36,083	25,910	2,584	1,254	12,548	2,689	17,008	—	—	9,689
3	4	**State Street Global Advisors** (Boston, MA)	**398,682**	300,947	169,399	78,108	28,442	1,695	119,014	240	1,784	368,899
5	5	**Capital Group** (Los Angeles, CA)	**343,526**	270,616	161,598	111,873	30,146	4,259	35,650	—	—	176,580
		Capital Group Int'l	32,255	23,131	—	28,234	—	1,318	2,703	—	—	13,652
		Capital Guardian Trust	66,961	56,687	22,164	35,653	5,409	1,651	2,084	—	—	64,873
		Capital Research and Mgmt Co.	244,310	190,797	139,434	47,986	24,737	1,290	30,863	—	—	98,055
9	6	**Bankers Trust Co.** (New York, NY)	**317,753**	226,909	157,272	40,016	29,639	6,857	78,968	2,147	2,854	228,153
		Alex. Brown Capital Advisory	6,550	—	1,758	102	485	—	4,142	63	—	500
		Alex. Brown Investment Mgmt	7,169	—	6,079	—	771	—	319	—	—	4,720
6	7	**Mellon Bank Corp.** (Pittsburgh, PA)	**313,431**	258,923	125,125**	5,708	64,340	1,164	116,782	206	106	181,600
		Boston Co. Asset Mgmt	21,568	16,977	11,222	1,084	4,613	—	4,649	—	—	15,735
		Dreyfus Corp.	92,593	80,415	19,119	1,818	21,548	207	49,901	—	—	5,100

* *Rankings for 1996 reflect firms' updated data and may differ from rankings published in last year's II 300.*
** *This figure does not reflect the sum of the portfolio mixes of Mellon's subsidiaries.*

you get there, so we want large additional pieces of business. Any large mandate, any way we can get it, is attractive to us." Chafkin has also had success with risk-controlled alpha-tilt products, which attempt to add returns to any given benchmark through quantitative methods.

Mellon has chosen to go almost entirely with internal growth since buying Dreyfus Corp. in 1994. "It's hard to get, and we're getting it," says Mellon Asset Management CEO Christopher Condron. "Sure, we'd like a trillion dollars. But size is a funny thing." He says he'd rather be known as a significant manufacturer, a performance powerhouse and a leading distributor in every market channel than as merely a giant.

Not surprisingly, BGI's Grauer agrees. "If acquisitions are made by distribution-driven organizations, they can be a great idea, but that strategy requires a strong belief in the economies of scale and the nonlinearity of distribution," he says. "The more volume you acquire, the more product you can put through and the more income you can get." The catch, he contends, comes in active management, where gigantism can undermine clients' performance goals. Although big, efficient and cost-effective distribution can sell more assets, money managers need to be vigilant that "new marketing doesn't dilute alpha," says Grauer.

The II 300 defines money management as the management of assets for third parties for a fee. However, the magazine includes the in-house assets of pension funds and foundations large enough to make the ranking. In a separate table, we report the total assets for which institutions have investment responsibility — their own assets as well as those of clients.

Data for all the tables are assembled from hundreds of questionnaires sent to the nation's leading institutional managers, under the direction of Senior Associate Editor Jane B. Kenney. Our research staff also makes hundreds of follow-up calls, rechecking information and gathering additional data. But some institutions — 1838 Investment Advisors; Ruane, Cunniff & Co.; and WorldInvest — chose not to be included in this year's ranking and so do not appear.

Some of the divergence from figures and rankings published last year stems from adjustments reported by the institutions themselves. A dash in place of a 1996 ranking indicates that the manager did not qualify for the list last year or chose not to supply numbers. An investment subsidiary is listed under the parent's name only if it manages at least $3 billion.

Firms with a prominent U.S. presence are reported in the ranking even if they are wholly or partly owned by foreign firms. These companies report only assets from U.S. sources, whether gathered in the U.S. or internationally, and assets gathered abroad for investment in the U.S. Foreign subsidiaries of U.S. companies are also included.

Real estate managers subtract from the value of their portfolios any third-party debt used to acquire properties, since the securities managers record only assets given to them for investment, not the value of holdings acquired with leverage. Preferred stock is classified as a fixed-income asset, and convertible securities are included under equities. Bank figures do not include assets for which a bank serves only as the custodian or trustee, and insurance company assets exclude policy loans.

This overview was written by Senior Editor Alyssa A. Lappen.

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					Equities		Fixed-income securities					
1996	1997	Firm	12/31/97	12/31/96	Dom.	For.	Dom.	For.	Cash and equivalents	Real estate	Alternative investments	
		Franklin Portfolio Associates	$ 13,824	$ 10,750	$ 13,522	$ 302	—	—	—	—	—	$ 9,846
		Mellon Bond Associates	47,262	36,526	—	—	$ 18,609	—	$ 28,653	—	—	46,324
		Mellon Capital Mgmt Corp.	63,524	49,759	47,959	2,248	8,927	$ 320	4,070	—	—	56,281
		Mellon Equity Associates	16,957	11,312	13,583	—	2,865	—	509	—	—	16,931
		Mellon Private Asset Mgmt	39,190	30,057	28,234	—	8,233	—	2,517	$ 206	—	719
4	8	**Prudential Insurance Co.** (Newark, NJ)	**298,286**	271,722	73,980	9,608	148,303	14,594	35,636	13,792	$2,373	149,254
		Intech	5,217	5,171	5,217	—	—	—	—	—	—	4,630
		Jennison Associates	37,769	33,053	19,500	5,962	11,388	238	681	—	—	37,755
17	9	**Morgan Stanley Dean Witter** (New York, NY)	**268,649**	143,674	73,897	45,587	104,101	8,337	32,500	1,770	2,457	153,895
		Dean Witter InterCapital	90,470	—	36,013	4,883	21,254	148	28,172	—	—	32,800
		Miller Anderson & Sherrerd	60,023	41,141	16,332	1,740	39,760	2,021	170	—	—	54,530
		Morgan Stanley Asset Mgmt	66,580	54,902	4,488	36,901	11,279	5,988	3,697	1,770	2,457	52,934
		Van Kampen American Capital	51,576	47,631	17,064	2,063	31,808	180	461	—	—	13,631
7	10	**Equitable Cos.** (New York, NY)	**262,837**	234,857	118,582	13,827	83,067	14,961	24,063	—	8,337	122,851
		Alliance Capital Mgmt	218,653	182,792	109,585	13,827	57,386	14,961	22,688	—	206	99,520
		DLJ Asset Mgmt Group	11,987	5,595	4,250	—	4,537	—	—	—	3,200	2,187
10	11	**J.P. Morgan Investment Mgmt** (New York, NY)	**256,609**	208,605	86,722	33,793	70,268	25,599	33,133	5,283	1,811	183,377
13	12	**Putnam Investments** (Boston, MA)	**235,086**	173,443	140,178	20,902	63,810	6,890	3,236	—	70	98,624
24	13	**Scudder Kemper Investments** (New York, NY)	**218,668**	117,935	64,375	23,100	101,920	3,030	26,243	—	—	40,488
12	14	**Franklin Group of Funds** (San Mateo, CA)	**217,836**	174,951	54,752	89,066	63,149	3,248	3,684	149	3,788	25,323