In Asia, a More Electronified Equities Market Feels the Impact of MiFID II

2018 Greenwich Leaders: Asian Equities

Q1 2019

Although a tumultuous 2018 ended up being an overall positive year for most leading Asian equity brokers, owing to an active first half, the industry enters 2019 facing profound questions about how changes in regulations and market structure will affect the traditional institutional brokerage business model.

The two most impactful changes are new rules on equity research payments put in place by European regulators in MiFID II, and the continued "electronification" of Asian equity trading.

Amid these shifts, Morgan Stanley has retained its status as the leading Asian (ex-Japan/Australia) equity broker in terms of both trading and research/advisory services. In trading, Morgan Stanley is trailed closely by the trio of Bank of America Merrill Lynch, Citi and Credit Suisse, which are statistically tied in terms of market share, and then by J.P. Morgan, UBS and CLSA Asia-Pacific Markets, which are also tied. These firms are the 2018 Greenwich Share Leaders℠ in Asian Equity Trading.

Greenwich Share Leaders — 2018

Asian Equity Trading Share[1,2]

Broker	Statistical Rank
Morgan Stanley	1
Bank of America Merrill Lynch	2T
Citi	2T
Credit Suisse	2T
J.P. Morgan	5T
UBS	5T
CLSA Asia-Pacific Markets	5T

Asian Equity Research/Advisory Vote Share[1]

Broker	Statistical Rank
Morgan Stanley	1
Citi	2
Credit Suisse	3
UBS	4T
Bank of America Merrill Lynch	4T
J.P. Morgan	4T

Asian Equity Algorithmic Trading Share[3]

Broker	Statistical Rank
Morgan Stanley	1T
Bank of America Merrill Lynch	1T
UBS	3T
Citi	3T
Credit Suisse	3T

Note: Top 5 leading brokers cited including ties. [1]Weighted by spend of accounts. Vote share and trading share represent a broker's relative importance to the buy-side institutions within the Greenwich Associates universe. Based on interviews with 231 respondents at Asia Pacific institutions for Asian Equity Research/Advisory Vote Share (portfolio managers) and 104 for Equity Trading Share (traders). [2]Equity Trading encompasses sales trading, execution, portfolio trading, and electronic trading. [3]Based on 74 respondents.
Source: Greenwich Associates 2018 Asian Equity Investors Study

The 2018 Greenwich Leaders in Asian (ex-Japan/Australia) Equity Research/Advisory Vote Share are Morgan Stanley, Citi, Credit Suisse, and UBS, Bank of America Merrill Lynch and J.P. Morgan, the last three of which are tied in terms of their share of the institutional research/advisory "vote."

Citi and UBS are the 2018 Greenwich Quality Leaders℠ in Asian Equity Sales Trading & Execution Service. Morgan Stanley takes that title in Asian Equity Research Product & Analyst Service. Citi, CLSA Asia-Pacific Markets, Credit Suisse, and Morgan Stanley share this year's title for Quality Leader in Asian Equity Sales & Corporate Access.

Greenwich Quality Leaders — 2018

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Greenwich Quality Leader 2018

Asian Equity Sales Trading & Execution Service Quality[1]

Broker
Citi
UBS

Asian Equity Sales & Corporate Access Quality[2]

Broker
Citi
CLSA Asia—Pacific Markets
Credit Suisse
Morgan Stanley

Asian Equity Research Product & Analyst Service Quality[2]

Broker
Morgan Stanley

Asian Equity Electronic Trading Product & Service Quality[3]

Broker
Bank of America Merrill Lynch
Citi
Morgan Stanley

Note: Leading brokers are shown in alphabetical order. [1]Based on 104 respondents. [2]Based on 231 respondents. [3]Based on 73 respondents.
Source: Greenwich Associates 2018 Asian Equity Investors Study

MiFID Reshaping Business Models

MiFID II went live in Europe in January 2018, but its impact has spread far beyond the Eurozone. Rather than maintaining separate sets of practices for Europe and the rest of the world, most global asset management firms and banks are extending their MiFID II-compliant models to the world at large. The result has been a global "unbundling" of research from trade execution. For brokers, that means each side of the business will now have to stand on its own.

This change is already having a clear impact. For the 12 months ending Q3 2018, Greenwich Associates estimates that institutional investors based in the Asian time zone paid brokers $2.8 billion in commissions on trades of Asian equities—up about 10% from the prior year. About 52% was used to compensate providers for their Asian equity research/advisory services by the average investor, though the proportion is much lower at 40% among larger institutions, both well below the 60% levels in 2017.

Meanwhile, the share of investor spend allocated for execution-related services jumped to 48% on average and to 60% among larger funds.

In addition to changes in how investors allocate their spend, there has been a noticeable shift in who receives these payments. The top research providers in the market—all global investment banks—are capturing a growing share of institutions' research "vote," as their aggregate share increased two percentage points from 2017 to 2018. Although institutions are planning to rely more on internal research capabilities in the MiFID II era, as a group they have yet to make significant cuts to the overall number of research providers they use. However, these early results suggest that the research/advisory business is concentrating into the hands of the biggest global brokers.

"Given that this is the first year of MiFID II, it is too early to predict the precise long-term impact, but many of these changes are here to stay," says Greenwich Associates Managing Director John Feng. "The one thing that is certain is that every full-service broker is reassessing its business model and resource allocation in light of these changes."

E-Trading and Technology are Changing the Game

To that end, all major brokers are already moving in lockstep on one front: They are investing in electronic trading capabilities. For the first time, large institutional investors (excluding HFT firms) last year split their Asian (ex-Japan/Australia) equity trading volume evenly between traditional high-touch single-stock trades and low-touch trades made up of algo trades, crossing and portfolio trades. These institutions expect single-stock electronic trading alone to comprise 49% of their execution volume within three years, with growth coming at the expense of high-touch trades.

"There is increasing overlap between the list of Greenwich Share Leaders in e-trading and those in Asian equity brokerage overall," says Parijat Banerjee, Principal at Greenwich Associates. "And it's clear that brokers see e-trading capabilities as a key driver of future growth."

Morgan Stanley and Bank of America Merrill Lynch top the list of 2018 Greenwich Share Leaders in Asian Equity Algorithmic Trading, followed by UBS, Citi and Credit Suisse, which are statistically tied. The 2018 Greenwich Quality Leaders in Asian Electronic Trading Product & Service are Bank of America Merrill Lynch, Citi and Morgan Stanley.

What's also clear is that the growth of electronic trading is altering the way investors conduct business and interact with brokers. A primary example is the growing use of "algo wheels," which increasingly automate execution and in turn fuel further growth in electronic activities.

Technology is affecting how institutions select brokers in other ways as well. Although institutions still select their Asian equity research providers on the basis of traditional factors like quality of analyst service and corporate access, a new item is increasingly taking center stage: data. Nearly 10% of investors' research/advisory budget is allocated for a combination of fundamental data and alternative data, and close to 40% of portfolio managers expect data—particularly alternative data—to become more important going forward.

Consultants Jay Bennett, John Feng and Parijat Banerjee advise on the institutional equity markets in Asia.

METHODOLOGY

Between July and September 2018, Greenwich Associates conducted interviews with 231 Asian equity fund managers and analysts and 104 buy-side trading desks at institutions based in Asia. Interview topics included overall market trends, compensation and broker relationships.

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