What is an Asset Management Company (AMC)?

An asset management company (AMC) is a firm that invests a pooled fund of capital on behalf of its clients. The capital is used to fund different investments in various asset classes. Asset management companies are commonly referred to as money managers or money management firms as well.

Different Types of Asset Management Companies

Asset management companies come in many different forms and structures, such as:

- Hedge funds
- Mutual funds
- Index funds
- Exchange-traded funds
- Private equity funds
- Other funds

In addition, they invest on behalf of various types of clients, such as:

- Retail investors
- Institutional investors
- Public sector (government organizations)
- Private sector
- High-net-worth clients

Asset Management Companies Explained

Individual investors usually lack the expertise and resources to consistently produce strong investment returns over time. Therefore, many investors rely on asset management companies to invest capital on their behalf.

Asset management companies are usually a group of investment professionals with broad market expertise. With a large amount of pooled capital, they are able to utilize diversification and complex investment strategies to generate returns for investors.

AMCs generally charge a fee to their clients that is equal to a percentage of total assets under management (AUM). AUM is simply the total amount of capital provided by investors.

An asset management fund may charge a 2% fee on AUM. Consider as an example an asset manager who oversees a $100 million fund. The fees for one year or another time period will be $2 million ($100 million x 2.0%).

Hedge funds are notorious for charging much higher fees, sometimes upwards of 20%. However, hedge funds utilize more unorthodox and aggressive investment strategies to generate returns.

Buy-Side vs. Sell-side

Asset management companies are referred to as “buy-side” firms. It means that they help clients to buy investments. They make decisions based on which investments to purchase.

In contrast, “sell-side” firms, such as investment banks and stockbrokers, will *sell* investment services to buy-side companies and other investors. Sell-side companies provide market research and help to inform buy-side firms with valuable information to entice the buy-side firms to execute transactions with them.

Benefits to Asset Management Companies

There are various benefits to pooling capital together, including:

1. Economies of scale

Economies of scale are the cost advantages that a company can gain from increasing the scale of operations. With larger operations, the per-unit costs of operating are lower.

For example, asset management companies can purchase securities in larger quantities and can negotiate more favorable trading commission prices. Also, they can invest a lot of capital in a single office, which reduces overhead costs.

2. Access to broad asset classes

Access to broad asset classes means that asset management companies can invest in asset classes that an individual investor will not be able to. For example, an AMC can invest in multi-billion-dollar infrastructure projects, such as a power plant or a bridge. The investments are so large that an individual investor will not usually be able to access them.

3. Specialized expertise

Specialized expertise refers to asset management companies hiring finance professionals with extensive experience in managing investments that most individual investors lack. For example, an AMC can hire various professionals who specialize in certain asset classes, such as real estate, fixed income, sector-specific equities, etc.

Downsides to Asset Management Companies

Asset management companies come with a few downsides as well, such as:

1. Management fees

Most asset managers charge flat fees that are collected no matter what their performance was. As a result, over time, the fees can become very expensive for investors. Because of the costs for the resources and expertise required to run an AMC, the fees are high to compensate for such costs and to provide asset managers with a profit as well.

2. Inflexible

Asset managers can become too large to a point where they are cumbersome and unresponsive to the dynamic market. Managing too large of an amount of capital creates operational problems at times.

3. Risk of underperforming

Typically, the performance of AMCs are evaluated in comparison to a benchmark. A benchmark is a standard to compare performance against, usually in the form of a broad market index. There is the risk that asset managers underperform the markets, and if including the management fees mentioned earlier, it can become very costly for investors.