Boutique Chief Sees Most European Banks Exiting Research by 2021

By Hugh Son
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(Bloomberg) -- More than half the investment banks in Europe will shutter their research departments after regulations spur clients to become more selective about the content they use, according to Ed Wolfe, founder and managing partner of Wolfe Research LLC. Because most asset managers will pay for research out of their own pockets, the amount dedicated to paying for analysts' work will collapse after the European Union's revision of the Markets in Financial Instruments Directive, Wolfe said. Within two years, 30 percent of analysts will be dismissed, he predicts, and eventually weaker investment banks will relent and close their research outfits. "There's 11 large banks in Europe who do 70 percent of the research dollars, give or take," Wolfe, 51, said in an interview. "Of those 11, there will be four or five that are doing research" by about 2021 because of "massively reduced budgets," he said. The regulation, known as MiFID II, has forced money managers and brokerages to take a hard look at what they spend or charge for research. The law, which takes effect in January, requires clients to pay for the analysis separately, rather than receiving it from banks in a bundle of services including trade execution. The goal is to give investors more transparency into how much they pay for specific services.

See also: Banks to cut $1.2 billion in research spending, McKinsey says Wolfe isn't a disinterested party. A former top-ranked transportation analyst at Bear Stearns Cos. who went independent in 2008, Wolfe's business model includes picking off top analysts from Wall Street banks. Only well-regarded analysts who can still hustle will survive in the new world, he said. His New York-based firm employs 17 publishing analysts and their teams of associates. Clients have already become more parsimonious, Wolfe said. After one hedge fund suddenly cut its payments, Wolfe visited to find out why and was told the firm discovered it had been overpaying them for years. Money managers hadn't carefully administered the voting process that helps determine analysts' payments, resulting in some personnel receiving higher ratings -- and compensation -- than they were due, he said. Before MiFID, clients didn't bother checking. The common wisdom is that the biggest investment banks and a few boutiques will emerge as winners from the European overhaul, but Wolfe said that everyone will suffer for the foreseeable future. "In a terrible market environment, MiFID gives them a lot of cover to hide behind, to defer votes, to delay payments," Wolfe said. "It's going to suck for everybody for the next couple of years."