

3 TRENDS IN CLIENT ASSETS AND ALLOCATION

KEY FINDINGS

CLIENT TYPE

- » Institutional clients remain the largest client group accounting for four fifths of assets under management (79%)
- » Pension schemes continue to be the largest institutional client type with 43% of total assets in 2019, slightly down on 2018. Corporate client assets have seen the largest year on year increase accounting for 6% of all assets.
- » Consistent with previous findings, 55% of assets were managed on a segregated basis and 45% on a pooled basis.

ASSET ALLOCATION

- » Allocation to equities increased from 36% in 2018 to 38% in 2019 reflecting the resurgence of equity markets in 2019. Fixed income allocation was the biggest loser falling 1.8 percentage points on last year to 32%. All other asset classes remained largely unchanged from 2018.
- » Within equities the UK allocation fell below 30% for the first time to 29%, representing an 18 percentage point fall in allocation over the last decade. Given performance of UK equities relative to global indices, it is likely that the region continues to attract flows from certain client segments.
- » The shift to overseas fixed income has stalled in 2019 with allocations unchanged at 50% year on year.

GROWTH OF INDEXING MARKET

- » 2019 saw an acceleration in the growth of indexing strategies, which increased four percentage points to reach 30% of total assets.
- » Contributing to the growth in indexing is the very strong growth in ETFs. Total global assets in ETFs increased 30% year on year. Although still largely dominated by US domiciled funds, 2019 saw assets in Irish domiciled funds increasing over 50% to \$620 billion.

INVESTMENT IN THE UK ECONOMY

- » Despite reduced allocations to UK assets as a proportion of total assets, IA members remain significantly invested in the UK economy holding £1.6 trillion in UK equities, corporate bonds, commercial property and, increasingly in recent years, in infrastructure. This is particularly important given government indebtedness and heightened economic uncertainty.
- » Infrastructure investments have reached £45 billion, three quarters of which is invested in economic infrastructure such as roads and rail, with the remaining quarter invested in social infrastructure such as public schools or hospitals. This is up from £35 billion in 2018.



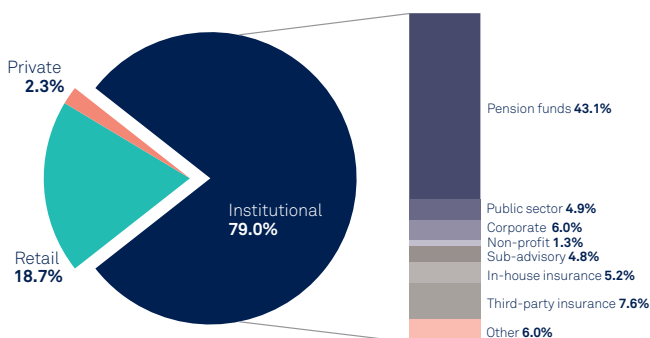
This Chapter looks across the entire UK-managed asset base of IA members and documents how these assets are split between different client groups, how they are allocated across asset classes and geographies, and what proportions are managed on an active or indexed basis. The distinctions are not always entirely clear, for example the line between retail and institutional is becoming increasingly blurred in the context of the growth in DC pensions. The institutional and retail markets are covered separately and in more detail in Chapters 4 and 5 respectively.¹¹

CLIENT TYPES

Chart 6 provides an overview of UK managed assets by client type. The relative size of different client segments changes very little year on year. The vast majority (79%) of assets continue to be managed on behalf of institutional clients in 2019 with retail client broadly unchanged at 21%. The largest institutional client segment are pension funds which make up 43% of all assets under management, down from 46% in the previous year despite a £155 billion increase in assets.

The largest relative increase has been amongst corporate clients who make up 6% of total assets, almost double the level it was five years ago. Combined insurance assets were down once again this year, falling one percentage point to 13% of total assets.

CHART 6: ASSETS MANAGED IN THE UK BY CLIENT TYPE 2019



The definition of pension funds in the IA's data includes all schemes, both defined benefit (DB) and defined contribution (DC) where the scheme has a direct relationship with the asset manager, notably DB schemes and some of the larger DC schemes, including master trusts. However, the direction of travel in the pension provision market, with the ever-increasing importance of DC schemes, is making the distinction between the different client types more challenging.

BLURRING OF CLIENT TYPES

Insurance vs Pension

DC pension assets that are operated via life companies wrapping funds are not included in pension fund assets but are rather reflected in assets managed on behalf of insurance companies. This includes assets managed for personal pension and Group personal pensions (GPPs). This blurs the line between pension and insurance assets and means that the allocation to pension funds understates actual pension investment.

Retail vs Institutional

DC is something of a hybrid between retail and institutional. Pension savers in DC schemes receive an income in retirement that is based on the value of the pension pot they have accrued during their working life. Unlike a DB scheme, where their pension is based on their salary and is ultimately guaranteed by an employer, the value of a DC pension is determined by the contributions an individual makes to their plan and the return on assets they achieve on the investment strategies they select. The ultimate investment risk lies with the individual rather than the employer, and in this regard DC pensions are more akin to retail investments than institutional, albeit they will appear in the IA's data either as Pension fund or Insurance assets.

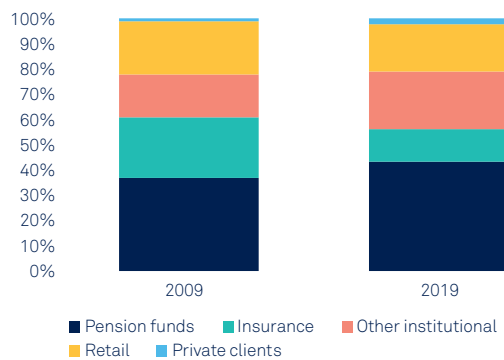
¹¹ Chapter 4 relates to money managed for UK institutional investors by IA members globally. It does not reflect money managed in the UK for all institutional clients.

HISTORIC EVOLUTION OF CLIENT ASSETS

As discussed, there is very little variation in the composition of the client base year on year, however we observe more significant changes in the market when we look back over data from the last decade. The split between retail and institutional clients has remained broadly unchanged for over a decade with about 80% of assets managed on behalf of institutional investors and 20% of assets managed on behalf of retail investors.

The composition of the institutional market is where the most significant changes in client base can be observed (Chart 7). The most consistent long term trend has been the decline in insurance assets, which are almost half the level they were a decade ago as a proportion of total assets. In-house insurance assets have seen significant falls whereas third party insurance assets have increased as a proportion of the overall total, possibly as a result of demerger activity. Insurance assets' share of total assets has fallen 10 percentage points over the last decade. The lost market share has been absorbed by other institutional (most notably corporate clients) and pension assets which have both increased their share of total assets by 6 percentage points over the last decade.

CHART 7: PROPORTION OF ASSETS MANAGED IN THE UK BY CLIENT TYPE (2009-2019)

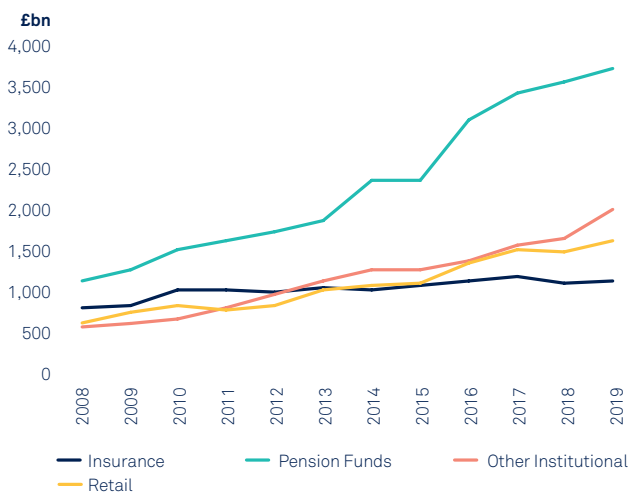


Looking at the growth of assets over time in nominal terms sheds some light on the drivers of the changing composition in the institutional client base. Chart 8 illustrates that since 2013 pension assets have outpaced the growth in retail and Other institutional assets, almost doubling their assets over the period.

As we will see in Chapter 4, a large component of the growth in pension assets has been the significant rise in liability driven investment (LDI) by DB pension schemes looking to manage the run off of their liabilities. To a lesser extent it will also reflect the increased pension participation resulting from automatic enrolment, much of which has been invested into master trust arrangements.

While pension asset growth has taken off, insurance assets have flatlined in nominal terms. We have seen some significant demerger activity over recent years that would explain some of the decline in in-house insurance assets. However, another component of this is the evolving business models of those insurance owned firms. These firms have increasingly diversified businesses and the majority are no longer reliant on the insurance business as the primary source of revenue growth.

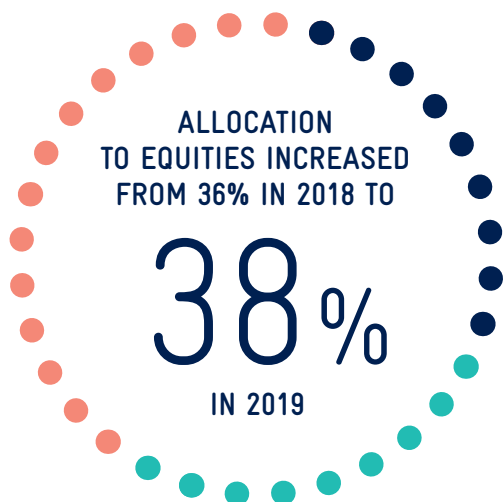
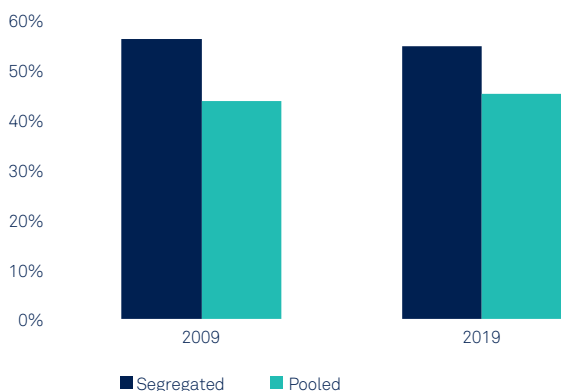
CHART 8: ASSETS MANAGED IN THE UK BY CLIENT TYPE, (2009-2019)



SEGREGATED VS. POOLED

Chart 9 shows the split of total assets under management between segregated mandates and pooled investments. The figures were very marginally changed year on year with 55% of assets managed on a segregated basis and 45% on a pooled basis in 2019. This data has seen very little fluctuation for over a decade despite the substantial evolution in product offerings in the pooled fund universe, particularly the rise of ETFs alongside more established indexing vehicles. Segregated mandates continue to be heavily used in the traditional institutional market.

CHART 9: SEGREGATED VERSUS POOLED INVESTMENT (2009-2019)

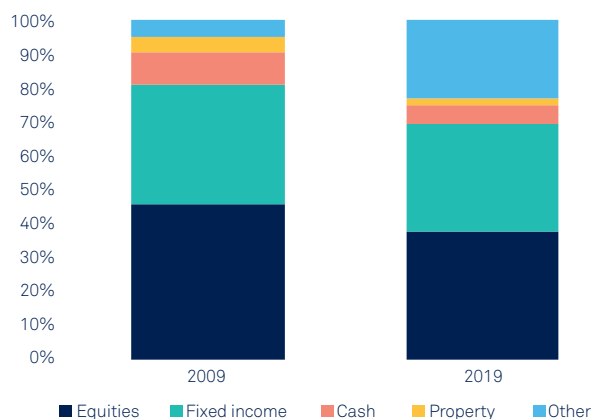


ASSET ALLOCATION

The overall mix of assets at the end of 2019 can be seen in Chart 10 which also shows the evolution in asset class allocation over the last decade. Asset class movements year on year tend to be consistent with market performance. Last year saw a four percentage point fall in equity allocation to 36% due to equity market downturns in the last quarter of 2018. As we saw in Chapter 1, equity markets have rebounded strongly in 2019 resulting in an increase in allocation to 38%. The higher relative allocation to equities came at the expense of fixed income and property which were both down one percentage point year on year to 32% and 2% respectively. Allocations to cash and 'Other' remained broadly unchanged.

The long term trend as shown in Chart 10 suggests a structural shift in asset allocation over the last decade towards a significantly increased allocation to 'Other'. Other assets include assets in private markets and solutions type strategies. The most substantial component of 'Other' will be Liability Driven Investment (LDI) strategies which are largely derivatives based. Allocations to 'Other' have increased from 5% in 2009 to 22% in 2019 however this trend has slowed down since 2015 with assets increasing two percentage points in the last four years. Equity and fixed income remain the two largest asset classes, making up 70% of total assets, however this is down from 81% in 2009. 'Other' overtook cash as the third biggest asset class in 2011.

CHART 10: OVERALL ASSET ALLOCATION OF UK-MANAGED ASSETS (2009-2019)



IA members invest across a range of asset classes. Almost all IA members are invested in equities to varying degrees, with a lower proportion investing in fixed income. Just under one third of Survey respondents (30%) are specialists investing only in either equities or fixed income, often also combining this with allocations to cash.

TABLE 4: PROPORTION OF IA MEMBERS INVESTING BY ASSET CLASS

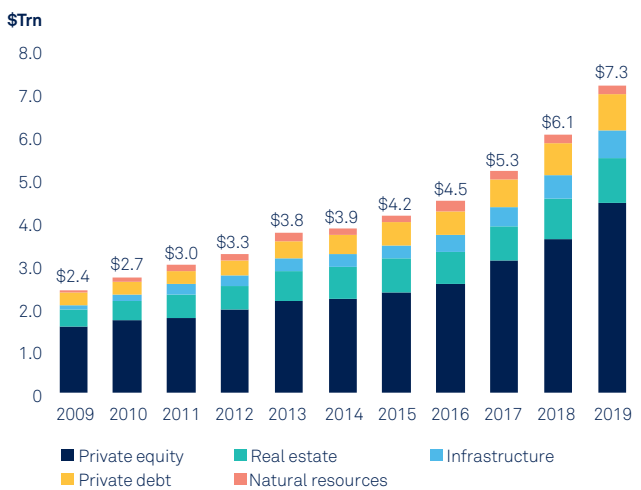
	Percentage of firms
Equities	93%
Fixed income	75%
Cash	78%
Property	40%
Other	57%

GROWTH OF PRIVATE MARKETS

A growing component of ‘Other’ is the allocation to private market assets. We do not collect a granular breakdown of this data, so we cannot quantify the size of these investments by IA members. However, we reference global data to get a sense of the size of the investment opportunity in this space.

As Chart 11 shows, the growth in private market assets under management globally continued to increase through 2019 and has accelerated significantly in recent years. The drivers of this trend in the UK have been well explored, including in previous editions of the Investment Management Survey. From the demand side, record low interest rates have created a ‘hunt for yield’ further afield than the public bond markets. Investors desiring diversification of risk and superior returns are also looking to private markets against a backdrop of long term de-equitisation by UK DB pension schemes.

CHART 11: GLOBAL ASSETS UNDER MANAGEMENT IN PRIVATE MARKETS (2009-2019)

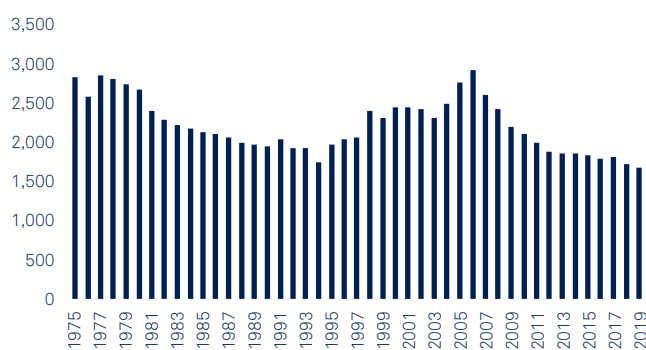


Source: Preqin



On the supply side, many companies have found public market listing a less attractive route for a range of reasons, including perceived complexity and the relative cost of capital elsewhere. In the UK, this has resulted in a decline in listed companies. Chart 12 illustrates the scale of the change over the last two decades, while also suggesting that there could be long-term cyclical elements at work, given previous patterns of decline and recovery.

CHART 12: NUMBER OF COMPANIES LISTED ON UK MARKETS (1975-2019)



Source: World Bank, LSE

DETAILED ASSET ALLOCATION

Beyond the shifts between asset classes, the IA also monitors the trends within equity and fixed income allocations according to type of exposure and this section considers these changes in more detail.

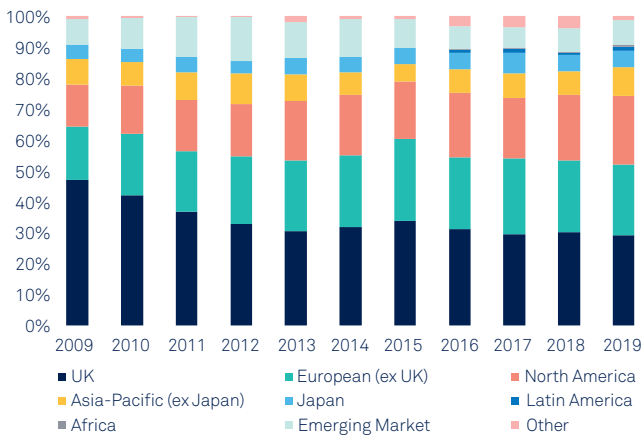
EQUITY BY REGION

The most striking long term trend in regional equity has been the decreasing allocation to UK equity relative to overseas equity (Chart 13). In 2019, this figure fell one percentage point to 29%. Until 2019 allocations to UK equity have fluctuated around the 30% mark for a number of years but 30% had never been breached. The picture is different when looking at allocations to UK equities in the UK funds market (Chapter 5) and in the DB pension market (Chapter 4) which have seen consistent declines in UK equity allocations.

Our aggregate data on UK equity AUM does not allow us to distinguish between market performance and flows so it is difficult to draw definitive conclusions. However, based on market performance data alone we would expect to see more of a decline in UK equity allocations given that UK equities have underperformed global markets over the last few years. Instead, the UK equity allocation has stabilised over the last few years suggesting that it continues to attract quite significant inflows from other institutional investors. Stripping out price return from total return suggests that UK equities produce higher income relative to other global markets. Superior dividend payments from UK equities could be a driver of the continued interest from overseas institutional investors.

Equity allocations are dominated by investments in the UK, North America and Europe which make up 74% of total equity assets, slightly down from 77% a decade ago. European equities has been consistent at 23% for a number of years whereas there has been consistent growth in the proportion of North American equities to 22% in 2019, an increase of one percentage point from 2018. These assets will be heavily dominated by US equities where market performance has been remarkably strong. Asia pacific (ex. Japan) allocations have been more volatile over the last decade but 2019 saw allocations increasing 1.6 percentage points year on year to 9%.

CHART 13: UK-MANAGED EQUITIES BY REGION (2009-2019)



FIXED INCOME BY REGION

Fixed income exposure has historically been more domestically focused than equities. In 2019, similar to last year, 50% of all fixed income assets were in domestic bonds compared with 66% in 2011.

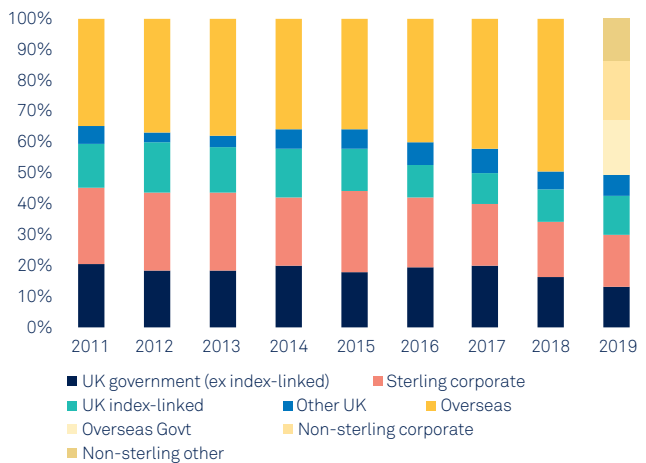
Within the domestic market, the proportion of assets in conventional UK government bonds has continued to decline from 21% in 2011 to 13% in 2019. Allocations to index-linked government bonds have tended to fluctuate year on year but were up two percentage points in 2019. We have collected more data on the overseas market in 2019 and observe that despite the falling allocation, assets in UK government bonds incl. index linked (26%) remain higher than overseas government bonds (18%).

The biggest losers since the Brexit referendum have been sterling corporates, which since 2015 are down almost ten percentage points to 17%. This means that allocation to sterling corporates is lower than the allocation to Non-sterling corporates (19%).

There are a number of potential drivers of these shifts. The growth in allocation to overseas bonds reflects the increasing globalisation of the investment process. However, the acceleration in the growth of allocation to overseas bonds since 2015 has coincided with the UK's decision to exit the European Union. The heightened political and economic uncertainty caused by Brexit has meant that firms have been looking to reduce their

exposure to the UK market. The trend slowed at the end of 2019, despite the imminent departure from the European Union, which suggests that there is a third driver at play. Increased pension scheme derisking as scheme members age and require a higher allocation to bonds is leading to more much money chasing a limited supply of UK bonds. This is causing pension schemes to seek investment opportunities through bonds issued overseas.

CHART 14: ALLOCATION OF UK-MANAGED FIXED INCOME BY TYPE AND REGION (2011-2019)



IN 2019,
SIMILAR TO LAST YEAR

50%

OF ALL FIXED INCOME
ASSETS WERE IN
DOMESTIC BONDS

GROWTH OF INDEXING MARKET

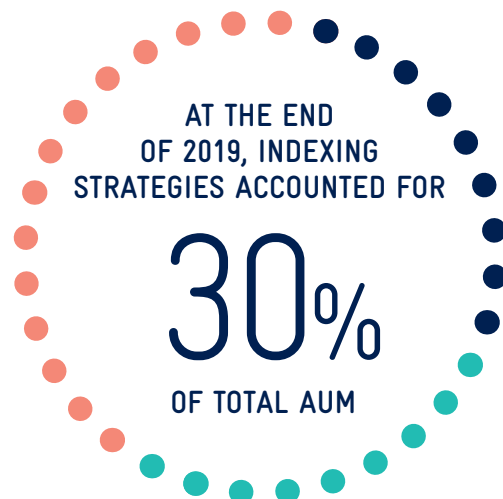
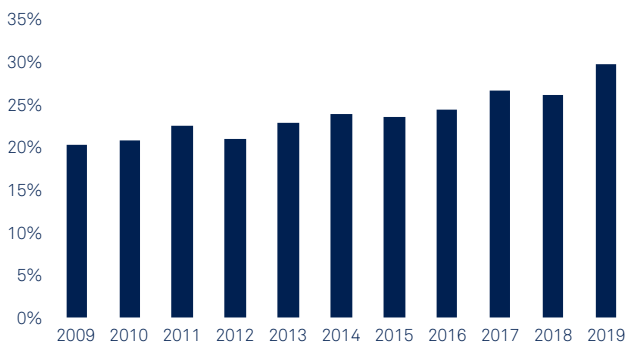
Chart 15 illustrates the use of indexing strategies across the UK managed asset base and how this has evolved over the last decade. In 2009 indexed assets as a proportion of total assets under management stood at 20% and have grown very steadily since then. 2019 saw a notable jump in this figure to 30%, a four percentage point increase year on year.

Use of indexing is more prevalent amongst UK institutional investors but is rapidly increasing amongst UK investors in the retail funds market. IA data on retail fund flows shows 2019 to be a bumper year for net flows into index funds with record net sales of £18 billion. Over the last two years, net retail sales to index trackers have propped up fund sales overall: sales to index trackers were £27 billion over 2018 and 2019 compared with almost £10 billion in net outflows from active funds over the same period.

In 2019 just under half (44%) of equity assets and less than one third (30%) of fixed income assets were managed on an indexed basis.

One striking trend from the last year has been the growth in assets under management in the ETF market. Although only a small number of IA members are active players in the provision of ETFs, it is likely that the growth in demand for these vehicles is contributing to the increasing overall allocation to index strategies.

CHART 15: INDEXING STRATEGIES AS PROPORTION OF TOTAL UK ASSETS UNDER MANAGEMENT (2009-2019)



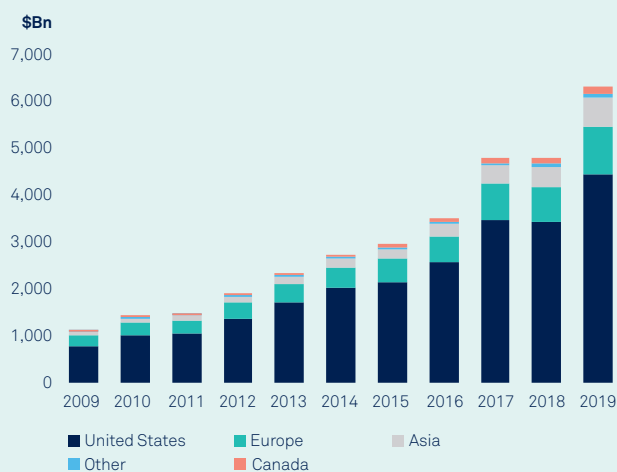
ETF MARKET

An ETF is an open-ended pooled investment vehicle with shares that, like a 'traditional' fund, will offer investors access to a portfolio of stocks, bonds, and other assets, most commonly aiming to track an index. Unlike a fund, it can be bought or sold throughout the day on a stock exchange, which is why ETFs are effectively a hybrid of a tradeable stock and an index-tracking fund.

ETFs have seen explosive growth over the last decade with global assets under management increasing 19% each year on average. After a volatile 2018, which saw total assets flatline, global AUM in ETFs had reached \$6.3 trillion in 2019, representing a 30% increase on the previous year.

Chart 16 shows that ETFs domiciled in the United States make up 70% of total assets, equivalent to \$4.4 trillion at the end of 2019. European domiciled ETF assets grew at a slightly faster rate on aggregate than the US to \$1 trillion in 2019. This was largely driven by remarkable growth in assets in Irish domiciled ETFs which increased 50% between 2018 and 2019 to \$620 billion. Assets in Asian domiciled ETFs reached \$620 billion, up 38% year on year. Assets in Asia are predominantly (65%) in Japanese ETFs, though the increase in assets is driven by a 75% increase in China and Taiwan ETFs.

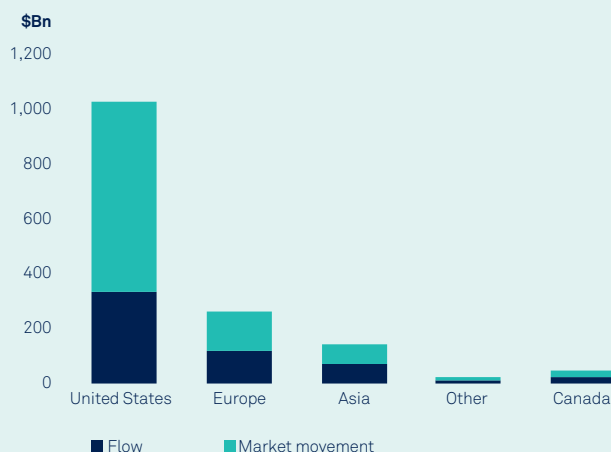
CHART 16: ETF ASSETS UNDER MANAGEMENT BY REGION OF DOMICILE (2009-2019)



Source: Morningstar

Chart 17 splits the growth in total net assets into two components:- market appreciation and net flows. The US has a more established ETF market and although US domiciled funds continue to attract flows, the majority of growth (68%) in 2019 came from market movements while the remaining 32% came from net flows. By comparison almost half of total growth came from net flows in Asia and Europe in 2019.

CHART 17: DRIVERS OF 2019 GROWTH IN ETFS



Source: Morningstar

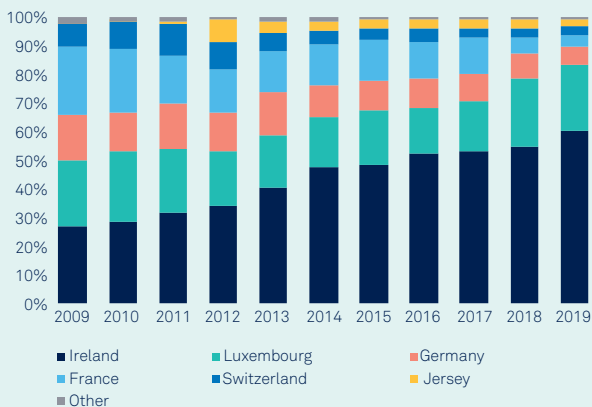
ETFs IN EUROPE AND THE UK

European data show that the UK is not a domicile for ETFs. Ireland and Luxembourg domiciled funds have almost doubled their share of the European market over the last decade, accounting for 83% of total assets. Assets in both Luxembourg and Irish domiciled funds increased significantly in 2019 by 37% and 54% respectively. For Irish funds in particular, 2019 was a bumper year in terms of sales with almost three-fifths (57%) of the growth in AUM coming from a surge in sales.

Given that ETFs can be bought and sold from around the world, domicile is not the best way to capture regional investor appetite for ETFs. ETFs can be listed on multiple exchanges and listing location can be used as a proxy for investor location. There are over 1,200 ETFs listed on UK exchanges with total assets of £330 billion, 93% of which are in

Ireland domiciled funds and the remaining 7% in Luxembourg domiciled funds. The majority of UK listed ETFs are managed by the small pool of IA members who are ETF providers.

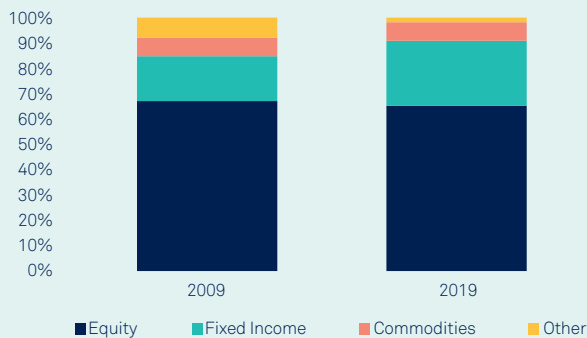
CHART 18: TOTAL ASSETS BY EUROPEAN DOMICILE (2009 - 2019)



Source: Morningstar

The biggest change in asset allocation within European domiciled ETFs over the last decade has been in the fixed income space, with allocations increasing from 18% in 2009 to 25% in 2019 (Chart 19). This trend accelerated in 2019 with assets increasing 54% year on year.

CHART 19: PROPORTION OF EUROPEAN ASSETS UNDER MANAGEMENT BY ASSET CLASS (2009-2019)



Source: Morningstar

ETFs RESILIENT THROUGH COVID-19

The 2020 market volatility triggered by the coronavirus and subsequent economic lockdowns saw total global assets in ETFs fall 16% at the end of Q1 2020. In terms of net flows, some markets held up better than others in March. Most regions were able to attract positive net inflows, albeit at depressed levels. The clear anomaly was in Europe which saw \$24 billion in outflows compared with inflows of \$8 billion and \$16 billion to US and Asian domiciled funds respectively. As was the case in the mutual funds world, fixed income ETFs were most heavily affected and were trading at a significant discount to their net asset value (NAV). Fixed income ETFs domiciled across North America and Asia suffered heavy outflows but this was offset by equity inflows. In Europe however, both equity and fixed income ETFs experienced outflows in March of \$14 billion. As a proportion of assets under management, the outflow from fixed income is significantly more substantial in relative terms..

ETFs remained resilient throughout the crisis despite the high levels of trading on secondary markets, and proved to be effective tools in providing liquidity within investors' portfolios. IA members pointed to the fact that in the fixed income space during March's period of heightened market stress, price discovery was difficult and ETF prices were a much clearer indicator of the value of underlying instruments than the NAV, which reflected stale valuations at the time.

By the end of Q2 2020, total assets under management had almost completely recovered to pre-coronavirus levels given the sharp bounce back in performance across global markets. Sales to fixed income ETFs have also returned to positive inflows across domiciles but at time of writing net sales to equity ETFs remain volatile.

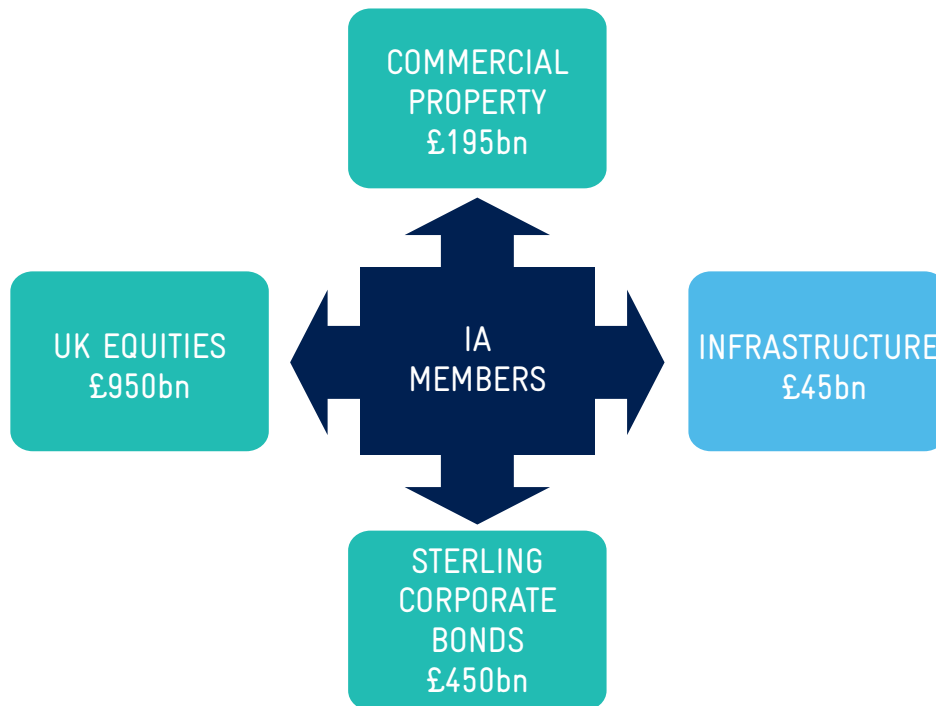
INVESTMENT IN THE UK ECONOMY

The investment management industry channels savings to capital markets and is therefore a key source of funding for the UK economy. This is increasingly important in the context of the pandemic and the highly uncertain economic outlook. Investment management activity has historically focused on more traditional asset classes such as listed equities and bonds but there is increasing use of private markets most notably infrastructure and direct lending. These types of investments are especially attractive to DB pension schemes and insurers looking for liability driven and cash flow driven investment. – see Figure 9.

We have seen that relative to total assets under management there has been a reduced allocation to UK equities particularly amongst DB pension schemes and retail investors which we will discuss in Chapters 4 and 5. However in absolute terms, this figure has continued to increase which means that the £950 billion in UK equities held by IA members represents 36% of total market capitalisation.

Independent research suggests that investment managers have purchased the majority of corporate bond issues in recent years holding almost half a trillion in sterling corporate bonds. Despite this, as we saw earlier in the chapter, corporate bonds have still fallen significantly as a proportion of total fixed income assets since 2016. In 2019, the amounts invested in UK equities and infrastructure have increased 8% and 28% in nominal terms.

FIGURE 9: IA MEMBER HOLDINGS IN UK ASSET CLASSES¹²



¹² The majority of property investment is in commercial property, however a small amount may be allocated to residential accommodation, notably student housing. The majority of infrastructure investment is UK but some may be invested overseas.

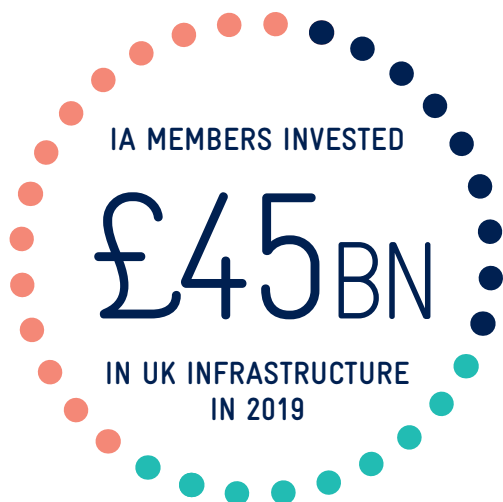
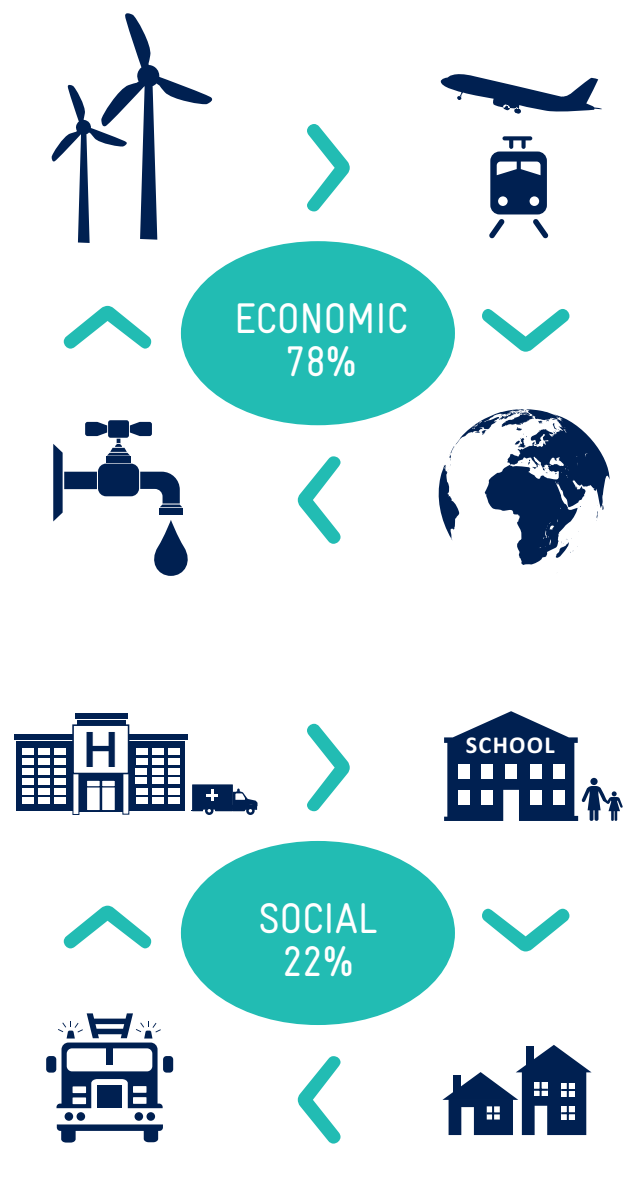
INVESTMENT IN UK INFRASTRUCTURE

The amount of investment reported by UK investment managers into infrastructure increased to an estimated £45 billion in 2019, up from £35 billion in 2018. This reflects both the increase in assets overall but also the increased interest in private market investment reported in recent years.

The proportion of infrastructure investment allocated to economic projects increased slightly (78%) but was broadly in line with recent years where three quarters of infrastructure investment was reported to be in economic projects. These include a variety of schemes such as energy generation and metering, transport, utilities and environmental schemes such as flood protection.

The remaining 22% was invested in projects which offer a social benefit, particularly the construction and maintenance of schools and healthcare-related projects such as the construction of hospitals (see Figure 10).

FIGURE 10: INFRASTRUCTURE INVESTMENT BY IA MEMBERS



The range of projects facilitated by IA members on behalf of their clients is extremely broad and Figure 11 provides a flavour of the type and location of projects that have been supported by UK investment managers in recent years.

Green energy projects are particularly important and a significant proportion of projects supported by IA member firms are solar farms or onshore and offshore wind farms.

In addition to the examples illustrated, members invest in other projects, which have a greater geographical reach and therefore cannot be shown in this figure. This includes projects such as the introduction of new rail rolling stock and the installation of fibre broadband.

FIGURE 11: SELECTION OF UK INFRASTRUCTURE INVESTMENT FACILITATED BY IA MEMBERS

