3 TRENDS IN CLIENT ASSETS AND ALLOCATION

KEY FINDINGS

CLIENT AND MANDATE TYPE

- In 2021, institutional clients continued to account for the majority (77%) of industry assets. Assets managed on behalf of retail clients increased for the second year in a row, rising two percentage points from 20% to 22%.

- Assets managed on behalf of pension clients, the single largest client group, dipped to 40%, five percentage points lower than in 2018.

- The proportion of assets that sit within segregated mandates versus pooled investment vehicles has seen little change over the last decade. In 2021, 53% of assets were managed on a segregated basis, which is unchanged on the previous year.

ASSET ALLOCATION

- The proportion of the asset base invested in equities has increased for the third year in a row, rising three percentage points in 2021 to 42% of total assets. The proportion of fixed income assets fell two percentage points to 30%, reflecting the volatility observed in fixed income markets in 2021.

- Looking at a regional breakdown of equity holdings, the largest change in 2021 has been the proportion of total equity investments held in North American equities, which rose a substantial six percentage points over the year to 30%. Holdings in UK equities continued to fall in 2021, dipping to 23% which is a 14 percentage point fall over the decade. This meant that for the first time, UK equities were overtaken as the largest region for equity investments.

- Diversification of holdings through investment in overseas markets is also a theme in the regional fixed income holdings. Over half (55%) of fixed income assets are held in overseas bonds, compared with one third of holdings a decade ago.

INVESTMENT IN THE UK ECONOMY

- Total investment in the UK economy across UK equities, sterling corporate bonds, UK infrastructure and commercial property stood at £1.6 trillion in 2021, a small dip on the £1.7 trillion reported in 2020.

- In 2021, UK infrastructure investments held by IA members stood at £40 billion, which has been broadly unchanged for a number of years now. This figure is largely (70%) made up of investments in economic infrastructure projects with a smaller proportion (30%) invested in social infrastructure projects. A large number of the economic infrastructure projects are focused on renewable energy, primarily wind and solar farms. Social infrastructure projects are largely investments in public buildings related to healthcare and education.

GROWTH OF INDEXING MARKET

- Year on year growth in indexing strategies slowed in 2021 but continue to be an increasingly significant proportion of the asset base, rising from 22% of total assets in 2011 to 32% in 2021.

- Global ETF data show another substantial increase assets, which grew 29% over 2021, reaching almost $10 trillion. The two notable trends in the ETF market have been the rise in actively managed ETFs and the growth of sustainable investment ETFs. Actively managed ETFs accounted for 4.2% of total assets in 2021, up from 1.6% in 2016. Sustainable investment ETFs were responsible for 4.0% of assets in 2021, up from 2.9% the previous year.

This chapter provides insight into the composition of the UK-managed asset base of IA members, with particular focus on three key dynamics: client groups, allocation across asset classes and geographies, and active- vs. indexed-based asset management styles.

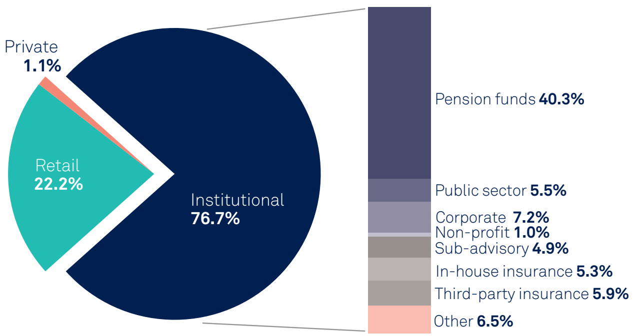
CLIENT TYPES

Chart 9 provides a general overview of the types of clients that the UK asset management industry serves. The industry primarily provides products and services for clients who broadly fall into either the retail or institutional category, while a small number of IA member firms also operate directly in the private client market. However, as Box 3 outlines, there is an increasing blurring of the lines between the broad categorisation of assets in this way.

In 2021, assets managed on behalf of institutional clients continued to make up the majority (77%) of assets, while just over a fifth (22%) was managed on behalf of retail clients. Pension clients are the single largest client group in the institutional market and account for 40% of total assets under management.

Among the rest of the institutional client market, insurance clients represent the second largest group, representing 11% of AUM.

CHART 9: ASSETS MANAGED IN THE UK BY CLIENT TYPE IN 2021



BOX 3: BLURRING OF CLIENT TYPES

Insurance vs. Pension

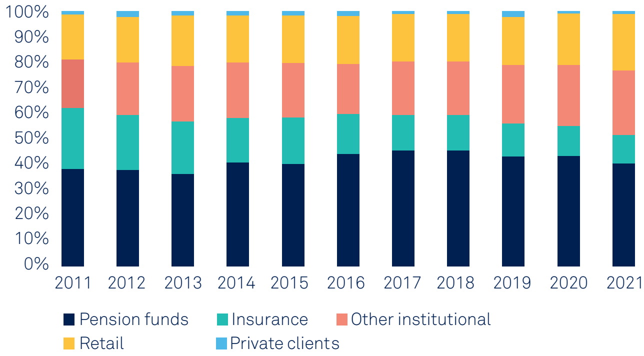
DC pension assets that are operated via life companies wrapping funds are not included in pension fund assets but are rather reflected in assets managed on behalf of insurance companies. This includes assets managed for personal pension and Group Personal Pensions (GPPs). This blurs the line between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

Chart 10 offers a comparison of the breakdown of assets managed in the UK by client type over the last decade.

CHART 10: ASSETS MANAGED IN THE UK BY CLIENT TYPE (2011-2021)



The most notable trends of the past decade have been:

- **An increase in the proportions of assets managed on behalf of pension funds:** The pensions market has seen large scale reforms over the last decade, much of which are a reflection of changing demographics and increased longevity. These changes have seen pension assets become a larger share of the industry's asset base over the last decade, rising almost consistently from 38% of total assets in 2011 to a peak of 45% in 2018. Since 2018, pension funds' share of the total asset base has fallen, dipping to 40% in 2021. While pension assets continue to rise in nominal terms, growth has slowed, particularly in comparison with assets managed on behalf of corporate and retail clients.

- **An increasing share in the assets managed on behalf of retail clients:** Retail client assets have increased for the second year in a row after a decade of very little movement, rising from 20% in 2020 and reaching 22% of assets in 2021.

- **A decline in the proportion of assets managed on behalf of insurance clients:** Insurance client assets have decreased thirteen percentage points over the last decade from 24% to 11% in 2020. The decline has been very consistent each year over the last ten years. In nominal terms, assets have remained flat whilst assets from other client groups have experienced strong growth.

- **The share of assets managed on behalf of private clients continues to fluctuate between 1% and 2%:** Private client assets peaked at 2% in 2012 and again in 2019 but have remained unchanged between 2020 and 2021 at 1%.

- **An increase in the proportion of assets managed on behalf of corporate clients:** Corporate client assets have more than doubled since 2011, growing from 3% of AUM to 7% in 2021.

SEGREGATED VS. POOLED

Over the past ten years, the proportion of assets under management within segregated mandates versus the proportion within pooled vehicles has experienced little fundamental change, even as the diversity of investment strategies available in pooled vehicles has widened significantly. Chart 11 illustrates that between 2011 and 2021, the proportion of assets within segregated mandates remains fairly consistent at 56% in 2011 and at 53% in 2021, which is unchanged from the previous year. This is down three percentage points since 2011. The remaining 47% of assets sit within pooled vehicles (which is up from 44% in 2011).

CHART 11: SEGREGATED VERSUS POOLED INVESTMENT (2011-2021)

TRENDS IN ASSET ALLOCATION

Table 3 looks at the proportion of IA members invested across different asset classes. We observe that almost one third (29%) of respondents are invested across all five categories listed in Table 3. Almost all (93%) of the respondents to the Survey are invested in equities and the majority (78%) are also invested in fixed income. One quarter (25%) of respondents are either equity or fixed income specialists, investing only in one of these asset classes. Property and cash remain niche areas of investment.

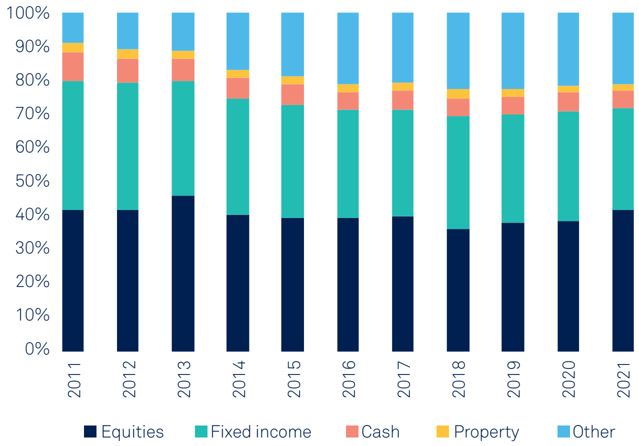
TABLE 3: PROPORTION OF IA MEMBERS INVESTING BY ASSET CLASS IN 2021

	Percentage of firms
Equities	93%
Fixed income	78%
Property	41%
Cash	19%
Other	66%

Our data also allows us to look at total assets invested in each of the broad asset classes listed in Table 3. Although we are unable to differentiate between market movements and a genuine reallocation of client assets, market movements play a significant role in year on year changes in AUM. On aggregate, Chart 12 shows that asset class movements in 2021 were broadly consistent with poor fixed income performance and relatively strong equity market performance (see Box 1 on page 16 for more detail):

- Total holdings in equities rose three percentage points between 2020 and 2021, rising from 39% of total assets to 42% of assets. The proportion of assets invested in equities have risen each year since 2018, rising from 36% to 42% of assets. This is largely a reflection of the very strong equity market performance over that period and the rebound in equity performance following the market downturn in Q4 2018.
- Fixed income returns were volatile in 2021, with the major indices seeing negative returns over the year. This is borne out in our 2021 data, where total assets in fixed income fell two percentage points year on year to 30%. Looking over the long-term, this is the lowest level of fixed income assets since we began collecting the data a decade ago, down eight percentage points since 2011.
- Total assets within the 'Other' category have seen the most substantial growth over the decade with the proportion more than doubling from 8% in 2010 to 21% in 2020. Much of this growth occurred between 2011 and 2016, and the proportion has remained fairly consistent since then. The majority of assets in the 'Other' category are solutions type strategies, such as Liability Driven Investing (LDI). As we discussed in Chapter 2, a small proportion of these assets are in traditional alternatives such as infrastructure and private equity.

CHART 12: OVERALL ASSET ALLOCATION OF UK-MANAGED ASSETS (2011-2021)



DETAILED ASSET ALLOCATION

In addition to monitoring the shifts between asset classes, the IA assesses trends within equity and fixed income holdings according to type of exposure. This section considers these changes in more detail.

EQUITY BY REGION

Chart 13 illustrates the equity split by region over the past ten years. There are a few notable trends in regional breakdown both in 2021, and when looking at the evolution over the long-term:

- The most striking trend in 2021 has been the surge in the proportion of assets held in North American equities which, for the first time, account for the largest share of total equity assets at 30%. North American equities rose by six percentage points over the year and are almost double the level recorded ten years ago. The growth in assets has been supported by a run of outperformance of US equities compared with the other major equity markets over the last few years.

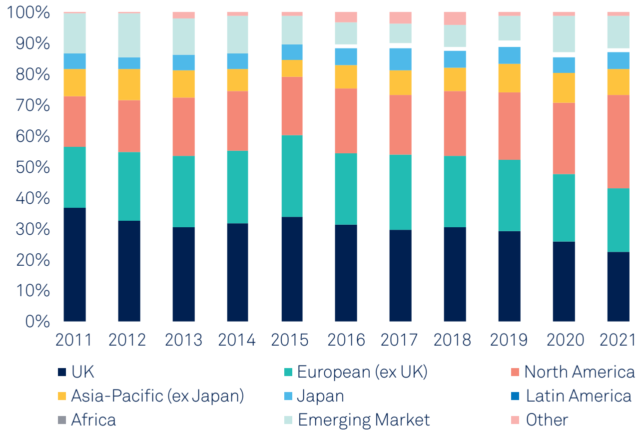
- The UK equity market performed well in 2021 after a number of years of underperformance. Yet, a strong 2021 was not enough to halt the move away from domestic equities and holdings fell two percentage points from a revised 24%, reaching a new low of 23%. This represents a fourteen-percentage point fall since 2011.

- Assets invested in European equities reached a nine year low falling one percentage point year on year to 21%.

- The proportion of assets invested in all other regions were 27%, down from 30% in 2020. The largest regions within this group are Asia Pacific (8%) and Emerging markets (11%), which saw allocations reduced by two and one percentage point respectively.

The changing allocations are partly a performance story, and partly a reflection of a broader shift towards more globally diversified portfolios. We see this trend reflected in Chapter 5 which shows a sustained sell off among UK retail investors out of UK equity funds since 2016. As discussed in Chapter 2, from a UK competitiveness angle, the UK investment management industry's ability to invest in global capital markets is a key draw for both overseas and domestic investors.

CHART 13: UK-MANAGED EQUITIES BY REGION (2011-2021)



FIXED INCOME ASSETS BY REGION

In 2021, the majority (55%) of fixed income assets were invested in overseas bonds. This was not always the case. Prior to 2016, almost two thirds of fixed income holdings was to sterling denominated or sterling hedged bonds. We have seen a consistent year on year increase in the proportion of assets invested in overseas bonds since 2016. This is again partly a global diversification story as investors increasingly seek to diversify portfolios and reduce exposures to a single market.

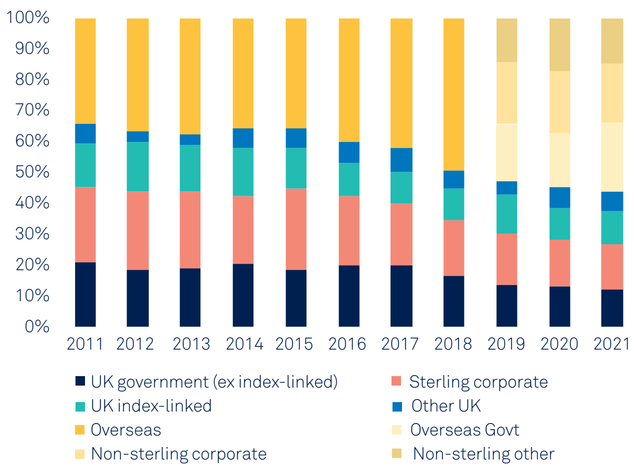
The fallout from the Brexit referendum has also had an impact, with the outlook for the UK economy impacted. Sterling depreciation has caused bond investors to reduce their holdings in UK bonds, as we see a corresponding rise in overseas bonds that could be denominated or hedged to the US dollar. This is a reflection of the US dollar's position as the world's dominant investment and funding currency.

Chart 14 provides a breakdown of fixed-income assets by type with a regional dimension over the past ten years. Two trends are particularly worth noting:

- The proportion of assets invested in sterling corporate bonds fell for the sixth year in a row in 2021. Sterling corporate bond assets now account for 15% of fixed income assets, ten percentage points lower than in 2011. Non-sterling corporate bonds fell by one percentage point in 2021 (down to 19%) yet remain higher than the allocation to sterling corporates.

- UK government bonds made up a third (35%) of fixed income assets in 2011 but accounted for 23% of assets in 2021, a twelve-percentage point fall over the decade. Much of this fall has been from non-index-linked UK government bonds which have almost halved from 21% to 12% in that time. Index linked government bonds have dipped but more modestly, falling from 14% to 11%, as institutional investment managers have moved to allocate to bonds that are protected against rising inflation.

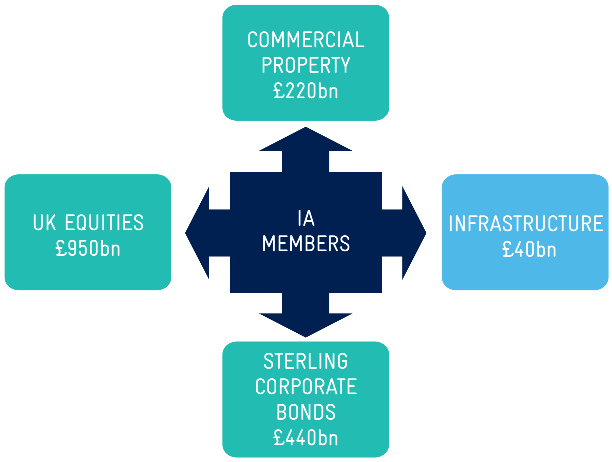
CHART 14: ALLOCATION OF UK-MANAGED FIXED INCOME ASSETS BY TYPE AND REGION (2011-2021)



INVESTMENT IN THE UK ECONOMY

As a major allocator of capital, the investment management sector has a direct impact on the UK's economic prosperity. In the aftermath of the financial crisis, the reduction in bank lending led to an increased use of investment finance through the capital markets. This has led to overall growth in industry assets and increased investment in the UK economy over the last 10-15 years. IA members have invested £1.6 trillion in the UK economy through equities, sterling denominated bonds, infrastructure and commercial property (illustrated in Figure 10). Of this, £950 billion is held in UK equities, unchanged since 2020 in nominal terms. This is approximately 33% of total UK equity market capitalisation. Sterling corporate bond assets fell £10 billion in nominal terms to £440 billion, reflecting poor performance in 2021.

FIGURE 10: IA MEMBER HOLDINGS IN UK ASSET CLASSES IN 2021[11]



[11] 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-based but there are some investments located overseas.

INVESTMENT IN UK INFRASTRUCTURE

Infrastructure investment has garnered increased focus in recent years both as a result of the growing reliance on market-based finance, and the increased focus on the role that investment managers can play to support the UK's commitment to decarbonisation and the "building back better" agenda post-pandemic. In 2021, UK asset managers held an estimated £40 billion in infrastructure projects, which has remained unchanged since 2019.

Figure 11 presents how we categorise infrastructure investments. There are two broad categories – economic and social. Economic infrastructure includes investments in renewable energy, utilities, transport and telecommunications, and accounts for the majority (70%) of infrastructure projects in the UK. Social infrastructure mainly involves public health, education and building, construction and maintenance. Social infrastructure investments make up 30% of total infrastructure investment in the UK.

Though limited to a selection of projects, Figure 12 maps out the types of infrastructure projects facilitated by IA members on behalf of their clients. These investments span across the UK, though notable clusters of investments in public buildings can be seen around major cities. Renewable energy projects make up a significant proportion of investment in UK infrastructure projects, which mainly consist of offshore and onshore wind farms.

Increasingly, members are also investing in nationwide initiatives includes regional waste and water management services, national grids for the provision of fibre broadband and international transportation networks. Because they are nationwide, these projects do not appear on the map.

FIGURE 11: INFRASTRUCTURE INVESTMENT BY IA MEMBERS

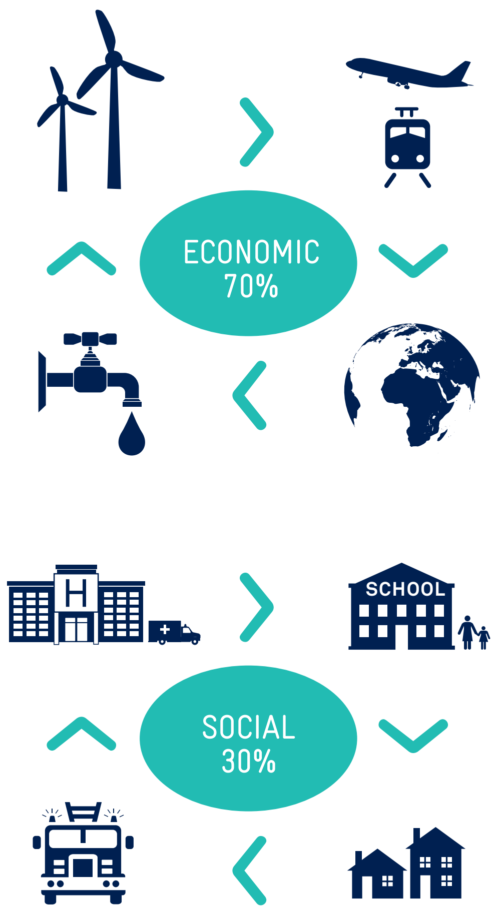
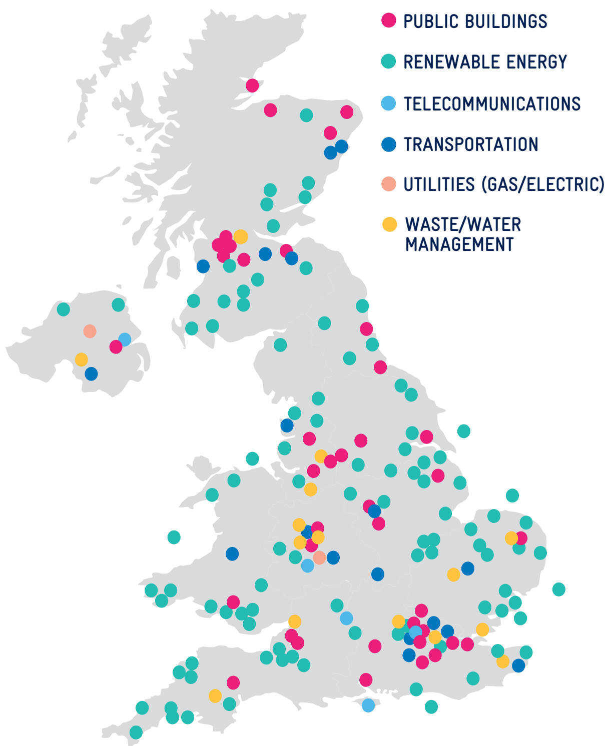


FIGURE 12: SELECTION OF UK INFRASTRUCTURE INVESTMENT FACILITATED BY IA MEMBERS IN 2021



3

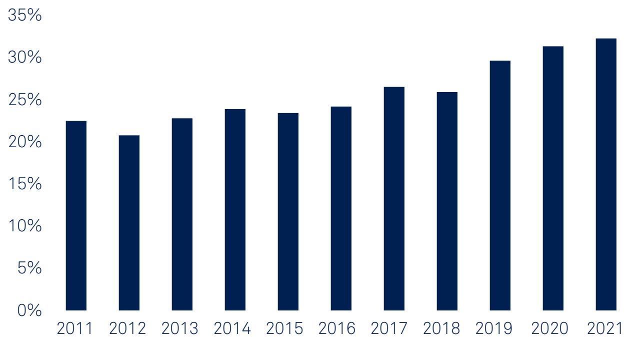
GROWTH OF INDEXING STRATEGIES

Indexing strategies have become an increasingly significant proportion of the asset base over the last ten years. In 2011, assets in indexing strategies made up 22% of total assets. This proportion has risen to 32% in 2021, one percentage point higher than 2020.

As indexing funds replicate the performance of the indices that they track, performance follows the pattern of the markets. A high proportion of indexing assets are tracking equity indices. This helps to explain the pattern of growth at the AUM level, which is mirrored in our funds market analysis in Chapter 5. Strong growth in assets in 2019 follows the downturn in markets at the end of 2018. There has been a slowdown in growth through 2021, compared with the previous two years, although assets have continued to rise. Chapter 5 data show that active strategies had a very strong year in terms of net flows in 2021, which could explain some of the slowdown in indexing strategies as a proportion of total assets. The majority of responsible and sustainable investment strategies are active and the strong performance demonstrated in 2021 may also have had an impact. Assets in index trackers grew 9% year on year, compared with 5% growth in active assets. By comparison, in 2019 tracker assets grew 26% compared with 5% growth in active strategies.

The data in Chart 15 includes assets held in ETFs. ETFs, which are largely index tracking vehicles, have seen very significant growth over the last few years. It is likely that the growth in ETFs has contributed to the acceleration of the growth in indexing we have seen since 2018. For a more detailed overview of 2021 trends in the ETF market, see Box 4.

CHART 15: INDEXING STRATEGIES AS PROPORTION OF TOTAL UK ASSETS UNDER MANAGEMENT (2011-2021)



IN 2011, ASSETS IN INDEXING STRATEGIES MADE UP 22% OF TOTAL ASSETS. THIS PROPORTION HAS RISEN TO

32%

IN 2021

BOX 4: ETF MARKET

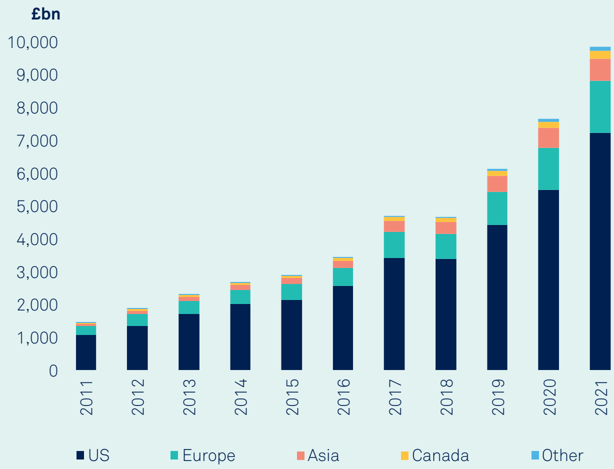
An ETF is an open-ended pooled investment vehicle with shares that, like a 'traditional' fund, will offer investors access to a portfolio of stocks, bonds, and other assets, most commonly aiming to track an index. Unlike a fund, it can be bought or sold throughout the day on a stock exchange, which is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

Among the IA's membership, less than a fifth of members manufacture ETFs as part of their product offerings. Among the members that we interviewed this year, some were of the view that increasing demand for highly transparent and liquid solutions would see the demand for ETFs rise considerably in Europe over the next few years.

Globally, total assets in ETFs approached $10 trillion at the end of 2021, an increase of 29% year on year. As illustrated in Chart 16, assets in US domiciled ETFs outpaced global growth and reached $7.3 trillion, a 32% rise over the year. Although in line with 2020 growth rates, assets managed in European domiciled funds grew at a slower rate than the US, increasing by 25% to $1.6 trillion. It should be noted that assets in Irish domiciled funds saw a 30% increase year on year but growth in other regions such as Luxembourg, Germany, France and Switzerland slowed to rates between 5 and 22%.

In 2021, AUM in Asia domiciled ETFs slowed considerably, growing just 5.2% over the year to $650 billion. The slowdown in growth alongside considerable growth in assets managed in other regions saw the share of assets in Asia domiciled funds fall from 8.1% in 2020 to 6.6% in 2021. It was also the regions lowest growth rate since 2008-09.

CHART 16: ETF ASSETS UNDER MANAGEMENT BY REGION OF DOMICILE (2011-2021)



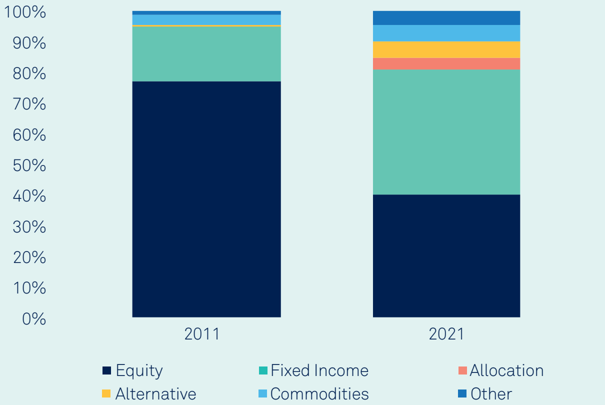
Source: Morningstar

There have been two standout trends in the ETF market over the last few years. The first is the rise in assets within actively managed ETFs and the second is the rise in sustainable investment ETFs.

Actively managed ETFs on the rise

Between 1993 and 2008, only ETFs tracking specific indices were approved for sale in the US. In 2008, SEC rules were amended to allow for the sale of actively managed ETFs fifteen years after the launch of the first index tracking ETF in 1993. Active ETFs globally have grown steadily since 2008 but growth has accelerated rapidly over the last five years, increasing almost eight fold since 2016 from just over $50 billion to over $400 billion in 2021. This far outpaces the growth in index tracking ETFs and has resulted in active ETFs having an increased share of the overall market, rising from 1.6% of total assets in 2016 to 4.2% of total assets in 2021. The North American markets, namely the US (71%) and Canada (17%) are largely where assets in active ETFs sit. The European and Asian markets account for 7% and 2% respectively, significantly lower than their share of index tracking ETF assets.

CHART 17: ACTIVE ETF ASSETS UNDER MANAGEMENT (2011-2021)



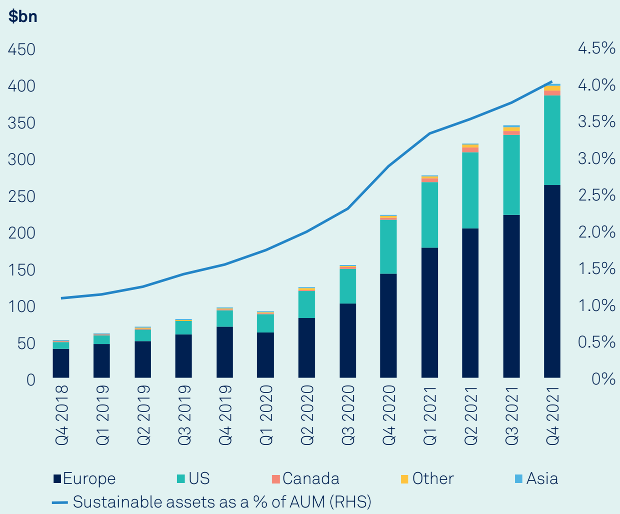
Source: Morningstar

The asset class composition of the active ETF market differs from index tracking ETFs. Equity index trackers represent the majority (77%) of ETF tracker assets, almost double the proportion (40%) of assets that sit within actively managed equity ETFs. Fixed income is marginally the most popular (41%) asset class in the active ETF market, whereas just 18% of total assets sit within ETFs tracking fixed income indices. Alternatives (5%) which can include derivatives-based strategies and more recently, cryptocurrencies also have a much higher relative allocation among active ETFs. At 4%, total assets in active mixed asset Allocation ETFs, which are termed allocation ETFs by Morningstar, are higher in absolute terms than in ETF index trackers.

Accelerating growth in sustainable investment ETFs

Sustainable investment is also a standout trend in the ETF market. According to Morningstar, which categorises a fund as sustainable based on prospectus disclosures, total assets within sustainable investment ETFs crossed $400 billion at the end of 2021, an 80% increase over the year and an eightfold increase over the last three years. This growth rate far outpaces the 29% growth in global ETF assets, resulting in sustainable investment ETFs market share rising from 2.9% at the end of 2020 to 4.0% at the end of 2021. Chart 18 shows that two thirds (66%) of sustainable ETF assets sit in funds domiciled in Europe, despite Europe being a smaller ETF market by asset size than the US. The sustainable investment market is less developed in the US than in Europe. In contrast with mutual funds, the sustainable investment product offerings are predominantly (96%) index trackers, and heavily (83%) equity products with almost all of the remaining (17%) assets in fixed income products.

CHART 18: INCREASE IN SUSTAINABLE AND RESPONSIBLE INVESTMENT OPTIONS IN ETFS (Q4 2018 - Q4 2021)



Source: Morningstar

ETFs in 2022

Asset values in ETFs across domiciles have been affected by the volatility in global capital markets in 2022. By mid- year 2022 total net assets in ETFs had fallen 15% to $8.5 trillion, an almost $1.5 trillion dollar fall. In contrast to the heavy H1 2022 retail outflows from UK mutual funds (see page 71 for more detail), and despite the sharp fall in asset valuations, ETFs have continued to draw net inflows in 2022. In fact, the $400 billion of inflows in the first six months of the year have been the second highest H1 inflows on record. While it is unclear what is driving this investment, some commentators have suggested that the inflows are being driven by long-term buy and hold investors looking to acquire undervalued assets.