

THE  
INVESTMENT  
ASSOCIATION

# ASSET MANAGEMENT IN THE UK 2017-2018

The Investment Association Annual Survey

September 2018



## CONTENT ENQUIRIES

Ruth Meade, +44 (0)20 7831 0898

## CONTRIBUTORS

Ruth Meade

Anastasia Petraki

Alastair Wainwright

Jonathan Lipkin

### **The Investment Association (IA)**

Camomile Court, 23 Camomile Street, London, EC3A 7LL

[www.theinvestmentassociation.org](http://www.theinvestmentassociation.org)

@InvAssoc

September 2018

© The IA (2018). All rights reserved.

No reproduction without permission of the IA.

# CONTENTS

Index of Charts, Figures and Tables	5
About the Survey	8
Survey Foreword	10
Executive Summary	12
<hr/>	
<b>1. UK ASSET MANAGEMENT INDUSTRY: A GLOBAL CENTRE</b>	<b>14</b>
Role of asset management	15
Size of the UK industry	16
Scale of wider industry	17
Scotland as a major centre	17
Position of UK asset management industry in Europe and worldwide	18
Overseas client market	19
Importance to UK service exports	19
Services to overseas funds	20
Safeguarding the global position of the industry	20
Supporting the UK economy	21
Investment in UK infrastructure	22
<hr/>	
<b>2. CHANGING DYNAMICS OF ASSET MANAGEMENT IN THE UK: TOWARDS A NEW MAINSTREAM?</b>	<b>25</b>
Evolution in the investment ecosystem	26
Public vs private markets	27
Role of asset managers in funding SMEs	29
Increasing emphasis on responsible and sustainable investment	29
Ongoing change in product demand	33
Rapid technological change	34
Diverse patterns of corporate M&A activity	35
Significant regulatory and policy scrutiny	38
EU-level change: Impact of MiFID II	39
UK context	42
Stewardship and corporate governance	43
Broader economic contribution	43
<hr/>	
<b>3. TRENDS IN CLIENT ASSETS AND ALLOCATION</b>	<b>44</b>
Client types	45
Longer-term evolution of client base	46
Segregated vs pooled investment	47
Asset allocation	47
Detailed asset allocation	48
Equity by region	48
Fixed income by region	48
Balance between active and passive	50

<b>4. UK INSTITUTIONAL CLIENT MARKET</b>	<b>54</b>
<b>Client breakdown</b>	<b>55</b>
Pension schemes	56
<b>The shape of the UK pension market</b>	<b>56</b>
<b>Trends in the third party institutional market</b>	<b>58</b>
Mandate breakdown	59
Investment trends within specialist mandates	60
Geographic allocation	62
Active vs passive	64
Segregated vs pooled	64
<b>5. RETAIL FUND MARKET</b>	<b>66</b>
<b>Funds under management</b>	<b>67</b>
Funds under management by asset class	67
Drivers of growth	68
<b>Retail fund sales</b>	<b>69</b>
Retail sales in overseas funds	69
Explaining flows	69
Holding periods of UK funds	71
<b>Investor objectives</b>	<b>71</b>
Outcome and allocation in the ascendancy	72
A structural shift	74
Stronger equity growth sales, but outside the UK	75
<b>Passively managed funds</b>	<b>76</b>
<b>Trends in fund distribution</b>	<b>78</b>
Distribution of passive funds	79
Wrappers used by retail investors in the UK	79
<b>Fund of funds</b>	<b>80</b>
<b>Industry structure and concentration</b>	<b>81</b>
<b>UK Market in European context</b>	<b>82</b>
<b>6. OPERATIONAL AND STRUCTURAL ISSUES</b>	<b>84</b>
<b>Revenue and costs</b>	<b>85</b>
<b>Employment in the asset management industry</b>	<b>86</b>
<b>Direct employment</b>	<b>87</b>
Distribution of staff by activity	87
<b>Industry concentration</b>	<b>89</b>
<b>Asset manager ownership</b>	<b>92</b>
<b>Boutiques</b>	<b>92</b>

# INDEX OF CHARTS, FIGURES AND TABLES

## CHARTS

Chart 1: Total assets under management in the UK (2002-2017)	17
Chart 2: UK-managed assets by UK regional headquarters (June 2008-2017)	17
Chart 3: Export earnings of fund managers and contribution to services exports (1997-2016)	19
Chart 4: Change in proportion of assets managed for UK and Overseas (2015-2017)	20
Chart 5: New housing association financing by banks and capital markets	24
Chart 6: Number of listed domestic companies in traditional markets	26
Chart 7: Equity raised via U.S. IPOs vs. equity raised via private offerings	27
Chart 8: Net retail sales of ethical funds as a percentage of funds under management (2008-2017)	29
Chart 9: Proportion of SRI relative to total managed assets in 2016	30
Chart 10: Dedicated investment according to specific ESG criteria	31
Chart 11: Assets managed in the UK by client type	45
Chart 12: Assets managed in the UK by client type (2008-2017)	46
Chart 13: Segregated versus pooled investment (2009-2017)	47
Chart 14: Overall asset allocation of UK-managed assets (2008-2017)	47
Chart 15: UK managed equities by region (2008-2017)	48
Chart 16: Allocation of UK-managed fixed income by type and region (2011-2017)	48
Chart 17: Corporate bond allocation by country of issuer (2016-2017)	49
Chart 18: Fixed income ownership by parent group type (insurance vs. non-insurance)	49
Chart 19: Active and passive as a proportion of total UK assets under management (2008-2017)	49
Chart 20: Assets managed in UK listed ETFs (2008-2017)	50
Chart 21: ETF assets under management by region of domicile	52
Chart 22: European ETFs by country of domicile	52
Chart 23: European domiciled ETFs by asset class	53
Chart 24: ETF contribution to asset growth	53
Chart 25: ETF net sales by asset class	53
Chart 26: UK institutional market by client type	55
Chart 27: UK institutional market by client type (2011-2017)	55
Chart 28: Pension participation for private sector jobs	56
Chart 29: UK institutional client market by client type	59
Chart 30: UK institutional client mandates including LDI	59
Chart 31: UK institutional client mandates: Multi-asset vs. specialist	60
Chart 32: UK institutional client mandates: multi asset vs. specialist (2011-2017)	60
Chart 33: Specialist mandate breakdown by asset class (2011-2017)	60
Chart 34: Specialist mandate breakdown by asset class	61
Chart 35: UK DB pension fund asset allocation (1993-2017)	61
Chart 36: DC asset allocation, selected FTSE100/FTSE 250 schemes	61
Chart 37: Specialist mandate breakdown by asset class among UK pension funds	62
Chart 38: Geographical equity allocation of specialist mandates by client type	62
Chart 39: Geographical equity allocation of specialist mandates (2011-2017)	63
Chart 40: Geographical equity allocation of specialist mandates among UK pension funds	63
Chart 41: Specialist fixed income allocation by client type	63

Chart 42: Fixed income allocation of specialist mandate types among pension funds	64
Chart 43: Specialist fixed income allocation (2011-2017)	64
Chart 44: Active and passive third party mandates by client type (sample-adjusted)	64
Chart 45: Segregated and pooled mandates by institutional client type	65
Chart 46: Institutional segregated and pooled mandates (2011- 2017)	65
Chart 47: Segregated and pooled mandates among third party pension funds	65
Chart 48: Industry funds under management (2008-2017)	67
Chart 49: FUM by investor domicile	67
Chart 50: FUM by asset class (1997-2016)	68
Chart 51: Funds under management by fund/asset type	68
Chart 52: Drivers of industry growth (1980-2017)	68
Chart 53: Net retail sales (2003-2017)	69
Chart 54: Gross sales by fund domicile	69
Chart 55: Average holding periods of retail investors (1997–2016)	71
Chart 56: Net retail sales by different investment objective (1998–2017)	71
Chart 57: Net retail sales of mixed asset funds (2003-2017)	72
Chart 58: Net retail sales targeted absolute return funds by asset class (2008-2017)	73
Chart 59: Net retail sales of money market funds (2008-2017)	73
Chart 60: Net retail sales of fixed income funds (2008-2017)	74
Chart 61: Net retail sales of income-focused funds (2008–2017)	74
Chart 62: Net retail sales of equity funds by regional focus (2008-2017)	75
Chart 63: Property sales and FUM (2008-2017)	76
Chart 64: Funds under management of passive funds by asset class (2008-2017)	76
Chart 65: Net retail sales of passive funds by index investment type (2008-2017)	77
Chart 66: Contribution to funds under management in passive funds (2008-2017)	77
Chart 67: Gross sales of passive funds as a percentage of gross sales by asset class (2008-2017)	77
Chart 68: Gross retail sales by distribution channel (2012-2017)	78
Chart 69: Net retail sales by distribution channel (2012-2017)	78
Chart 70: Tracker Net retail sales by distribution channel (2012-2017)	79
Chart 71: Retail investing trends (net retail sales through fund platforms)	79
Chart 72: Net retail sales of fettered and unfettered funds of funds (2003-2017)	80
Chart 73: Contribution to funds under management in fund of funds (2008-2017)	80
Chart 74: Number of firms reporting to the IA (2003-2017)	81
Chart 75: Combined market shares of top firms by funds under management (1998-2017)	82
Chart 76: Net sales of UCITS in Europe (2016-2017)	83
Chart 77: Assets in European UCITS and AIFs	83
Chart 78: Industry net revenue vs. revenue and costs as a percentage of average assets under management (2008-2017)	85
Chart 79: Distribution of asset manager profitability	85
Chart 80: Industry headcount estimate vs. UK assets under management (2008-2017)	87
Chart 81: Direct employment by staff segment (2012-2017)	88
Chart 82: IA member firms ranked by UK assets under management (June 2017)	90
Chart 83: Market share of largest firms by UK assets under management vs. HHI (June 2008-2017)	91

Chart 84: Top ten firms by UK-managed and global assets under management	91
Chart 85: Assets under management by region of parent group headquarters – ten year comparison	92
Chart 86: Breakdown of UK assets under management by parent type – ten year comparison	93

---

## FIGURES

Figure 1: The role of asset managers in channelling savings to investments	15
Figure 2: Who are the IA's members?	16
Figure 3: Wider asset management industry	17
Figure 4: Assets under management in European countries (December 2016)	18
Figure 5: Assets managed for overseas clients	19
Figure 6: IA member holdings in UK asset classes	21
Figure 7: Infrastructure investment by IA members	22
Figure 8: Selection of UK infrastructure investment facilitated by IA members	23
Figure 9: Notable M&A Activity during 2017-2018	36
Figure 10: Regulatory overview	38
Figure 11: Overview of the UK's pension landscape	57
Figure 12: Assets domiciled in European UCITS and AIFS 2017	82
Figure 13: Direct and indirect employment in asset management in the UK	86

---

## TABLES

Table 1: Global assets under management	18
Table 2: Proportion of IA members investing by asset class	47
Table 3: Reasons for seeking financial advice	70
Table 4: Net retail sales into fund of funds by distribution channel	80
Table 5: Distribution of staff by activity (direct employment)	87
Table 6: Estimated numbers of staff employed by activity (direct employment)	88
Table 7: Distribution of asset management jobs by region	89
Table 8: Assets managed in the UK by IA members by firm size	90

# ABOUT THE SURVEY

**THE SURVEY CAPTURES ASSET MANAGEMENT UNDERTAKEN BY MEMBERS OF THE INVESTMENT ASSOCIATION (IA) ON BEHALF OF DOMESTIC AND OVERSEAS CLIENTS. UNLESS OTHERWISE SPECIFIED, ALL REFERENCES TO 'UK ASSETS UNDER MANAGEMENT' REFER TO ASSETS, INDEPENDENT OF DOMICILE, WHERE THE DAY-TO-DAY MANAGEMENT IS UNDERTAKEN BY INDIVIDUALS BASED IN THE UK. THE ASSET VALUE IS STATED AS AT DECEMBER 2017.**

## **THE FINDINGS ARE BASED ON:**

- Questionnaire responses from 70 IA member firms, who between them manage £6.5 trillion in the UK (84% of total UK assets under management by the entire IA membership base).
- Other data provided to the IA by member firms.
- Data provided by third party organisations where specified.
- Publicly available information from external sources where relevant.
- Interviews with senior personnel from 14 IA member firms.

**THE IA WOULD LIKE TO EXPRESS ITS GRATITUDE TO MEMBER FIRMS WHO PROVIDED DETAILED QUESTIONNAIRE INFORMATION AND TO THOSE WHO TOOK PART IN THE INTERVIEWS.**

## **THE SURVEY IS IN SIX CHAPTERS:**

1. UK Asset Management Industry: A Global Centre
2. Changing Dynamics of Asset Management in the UK: Towards a New Mainstream
3. Trends in Client Assets and Allocation
4. UK Institutional Client Market
5. Retail Fund Market
6. Operational and Structural Issues

## **THERE ARE ALSO SEVEN APPENDICES:**

1. Summary of assets under management in the UK
2. Summary of data from the UK institutional market
3. Major UK and EU regulatory developments affecting asset management
4. Notable M&A deals in the UK asset management sector (2009-July 2018)
5. Definitions
6. Survey respondents
7. Firms interviewed

## **A NUMBER OF GENERAL POINTS SHOULD BE NOTED:**

- Not all respondents were able to provide a response to all questions and therefore the response rate differs across questions.
- The Survey has been designed with comparability to previous years in mind. However, even where firms replied in both years, some may have responded to a question in one year but not in the other or vice versa. Where meaningful comparisons were possible, they have been made.
- Numbers in the charts and tables are presented in the clearest possible manner for the reader. At times this may mean that numbers do not add to 100%, or do not sum to the total presented, due to rounding.



IA MEMBERS HOLD  
**ONE THIRD**  
OF UK PLC

MANAGE  
**35%**  
OF ALL ASSETS  
MANAGED IN  
EUROPE

**£1.2**  
TRILLION  
MANAGED FOR  
UK FUNDS

**£3.1**  
TRILLION  
MANAGED FOR  
OVERSEAS  
CLIENTS

**£1.7**  
TRILLION  
MANAGED FOR  
OVERSEAS FUNDS

**SECOND  
LARGEST**  
ASSET MANAGEMENT  
CENTRE AFTER  
THE US

**£7.7 TRN**  
MANAGED BY IA  
MEMBERS IN  
THE UK



# SURVEY FOREWORD



THE SIXTEENTH EDITION OF THE IA ASSET MANAGEMENT SURVEY SHOWS THE CONTINUED IMPORTANCE OF THE UK ASSET MANAGEMENT INDUSTRY TO INVESTORS WORLDWIDE. THE UK MAINTAINS ITS STATUS AS A PRE-EMINENT GLOBAL CENTRE OF ASSET MANAGEMENT EXPERTISE. IA MEMBERS ARE MANAGING £7.7 TRILLION FOR INDIVIDUALS AND INSTITUTIONS FROM THE UK AND AROUND THE WORLD.

As Brexit approaches, there is an increasing spotlight on this international position. With £3.1 trillion being managed for overseas clients, our industry clearly has the talent and infrastructure to attract clients from around the world. Safeguarding and building on these strengths will be critical in the years ahead. Particularly as the reality is that the European market is currently our largest source of overseas business.

A key investment theme in our report this year is greater interest in private markets. Bank lending is no longer as widely accessible, governments are increasingly limiting their borrowing and public listing is becoming less attractive for some companies. In this world, new opportunities are emerging for asset managers. Our industry is able to help its customers meet their income and diversification needs, while providing a different way of funding the wider economy.

One particular area of focus is infrastructure. The demand for infrastructure from pension schemes and insurance companies is not new, but it is becoming more prominent. Our Survey this year contains more detail as to how asset managers are directing capital into long-term UK projects, be it social infrastructure (eg. social housing, public buildings, education and healthcare facilities) or economic infrastructure (eg. energy, transport and utilities).

Opportunities – and challenges – are also emerging from the evolving UK pensions landscape. Both automatic enrolment and the Pension Freedoms are game-changing in terms of the level of individual responsibility and investment risk that savers are being asked to take. On the DB side, ever more specific funding needs have seen the value of liability driven investment strategies break through the £1 trillion point, as asset managers work more closely in partnership with schemes.

The increased number of UK pension savers using the services of asset managers will inevitably change the way our industry operates. This is already evident in the growing focus on transparency and improved disclosure.

At the same time, we are also starting to see a greater interest in responsible and sustainable investment from savers, complementing an intensifying focus from Government, regulators and international bodies.

All of this takes place against the backdrop of increasing technological change, which is impacting every level of industry activity, whether it is the way we communicate with investors, the way we distribute our services or how we improve back office technology so that we become more efficient. The UK is becoming a key FinTech centre creating the potential for significant disruption and re-invention. The launch of Velocity, the IA's own accelerator, reflects the changing realities for us all.

This is a very exciting time in the history of UK asset management. Certainly, we face a continued period of uncertainty as the UK develops new trade relationships with countries around the world and the industry responds to searching questions posed by regulators about the value we deliver to customers. But the depth of expertise within our industry means we are well placed to adapt to the challenges.

I hope you enjoy reading this report and I encourage you to get in touch with any suggestions you may have to make it better or more useful in the years to come.



**Chris Cummings**  
Chief Executive



# EXECUTIVE SUMMARY

## 1. UK ASSET MANAGEMENT INDUSTRY: A GLOBAL CENTRE

- » Total assets managed in the UK by the IA's members increased by 11% during 2017, ending the year at a record £7.7 trillion. This represents around 85% of the wider asset management industry which reached an estimated £9.1 trillion at the end of 2017. £1.7 trillion was invested in the UK economy via equities and corporate bonds and in domestic commercial property and infrastructure projects.
- » The UK remains the largest centre of asset management outside of the US. It is the largest centre of asset management in Europe, where it accounts for 35% of all assets under management. UK asset managers manage £3.1 trillion for overseas clients, which translates to earnings representing 6% of net services exports.
- » Assets managed for European clients increased by almost 30% year-on-year, bolstered by extremely strong flows into EU UCITS funds in 2017.

## 2. CHANGING DYNAMICS IN ASSET MANAGEMENT IN THE UK

- » The number of companies listed on public markets has reduced in the last decade, notably in the US and to a lesser extent in the UK and mainland Europe. At the same time, there has been increased interest in private markets as asset managers have expanded into real assets such as infrastructure and, more recently following the reduction in bank activity after the financial crisis, direct lending.
- » The range of responsible and sustainable investment approaches has led to a varying picture of how much money is managed in these strategies. Dedicated ESG investment remains the domain of the larger pension schemes. Among retail investors, interest is more muted, with the proportion of investment into UK authorised funds categorised as 'ethical' standing at just 1.3% of funds under management. Nevertheless there is increased adoption of responsible and sustainable values into mainstream investment processes by asset management firms.
- » Over the last decade there has been a shift in product demand towards more solutions-focused strategies (including liability-driven investment) and

alternative asset classes (including infrastructure and direct lending). In the institutional market this shift has been fuelled by interest from defined benefit (DB) pension schemes and insurers in investments that offer ways to more closely match their liabilities and cash flow needs.

- » Demand for passive investments has also been strong, driven by a desire for lower-cost solutions. The growth of passive investment via the ETF market has been particularly marked, with assets in UK-Listed ETFs increasing from £11 billion to £250 billion in the last ten years.
- » Harnessing technological innovation is an increasing priority for the industry. Three key areas are:
  - improving the efficiency of back office systems such as transaction processing.
  - using big data to improve decision making and achieve better investment outcomes either by increasing the sophistication of factor-based quantitative strategies in the smart beta environment, or in informing the investment decision making of fund managers responsible for active strategies.
  - enhancing the investor experience and making investment easier than ever for the individual by facilitating access to funds through a variety of media.
- » The distribution of retail funds in the UK remains heavily intermediated. Asset managers are increasingly considering how they can improve their connection with customers. A range of approaches are possible including vertical integration.
- » The regulatory and policy environment continues to reflect a mixture of challenge and opportunity for the industry in the UK and globally. Questions about the role played by the asset management industry focus both on the customer delivery side, and the wider contribution to the economy. They fall into two categories:
  - How can the value of asset management to its customers be demonstrated, broadened and maximised.
  - How can the needs of the broader economy be met from asset management activity.

### 3. TRENDS IN CLIENT ASSETS AND ALLOCATION

- » Almost four fifths of assets under management (79%) were managed on behalf of institutional investors. Pension schemes remained the largest client type although for the first time in more than five years pensions failed to increase as a proportion of total assets, remaining almost unchanged from 2016 at 44%.
- » Demand for real assets such as infrastructure and real estate continued in 2017 and these asset classes are expected to be a key growth area in the coming year. This demand is driven by pension schemes and insurance companies looking to manage their liabilities and match cash flows.

### 4. UK INSTITUTIONAL CLIENT MARKET

- » IA members managed £3.8 trillion for UK institutional clients in offices around the globe. Pension funds were the largest client type, with 63% of institutional total assets under management, followed by insurance companies at 25%. An estimated £1.1 trillion of this was managed in liability-driven investment strategies.
- » Once in-house mandates were excluded from the institutional data, assets under management stood at £3.1 trillion. Pension funds were even more dominant in the third party market, with 71% of third party assets.
- » Multi-asset, or 'balanced' mandates, now account for almost a quarter (24%) of total mandates once LDI mandates are excluded. Single-asset mandates accounted for the remaining 76%. The increase in multi-asset mandates may in part reflect the use of multi-asset strategies in defined contribution (DC) default funds.
- » Within specialist mandates, global equity mandates increased to 50%, while UK mandates continued to fall, dropping by another percentage point to 23% of specialist equity mandates. For the first time sterling corporate mandates were not the largest category within specialist fixed income mandate. Global bonds was the largest category, at 29%.

### 5. RETAIL FUND MARKET

- » UK investor funds under management in UK authorised and recognised funds grew to £1.2 trillion. £147 billion of this was held in funds domiciled overseas, suggesting UK investors are not shying away from overseas funds following the Brexit referendum, although UK equity funds remained out of favour in 2017.
- » Net retail sales were £47.1 billion in 2017. This was partly a bounceback from weak 2016 sales, but may also reflect structural changes encouraging investment into UK funds.
- » Outcome and Allocation funds were most popular with £13.8 billion of net retail sales. Fixed income funds also had a very strong year, with retail sales of £13.2 billion as the desire for income continued unabated.

### 6. OPERATIONAL AND STRUCTURAL ISSUES

- » Operating profit fell from 30% to 28%. Despite rising revenue (£20.6 billion), costs rose more quickly. Profitability at individual firm level continued to vary widely.
- » An estimated 38,000 people were employed directly by asset managers at the end of 2017 up by around 1% on the 2016 figure. Jobs in the asset management industry vary by location, with the largest proportion in London being employed in investment management and operations, while fund administration is of greater importance in Scotland. Staff in Compliance, Legal and Audit have grown most significantly over the past five years with the proportion of staff employed in these roles more than doubling in absolute terms.
- » The UK asset management industry remains relatively unconcentrated. 43% of assets were managed by the top five firms and assets managed by the top ten firms increased by two percentage points to 58%. Merger and acquisition activity between traditional asset managers continued but managers also bought in expertise in private assets, technology and distribution.

# 1 UK ASSET MANAGEMENT INDUSTRY: A GLOBAL CENTRE

## KEY FINDINGS

### THE SIZE OF THE ASSET MANAGEMENT INDUSTRY IN THE UK

- » Total assets managed in the UK by the IA's members increased by 11% during 2017, ending the year at a record £7.7 trillion. This represents around 85% of the wider asset management industry which reached an estimated £9.1 trillion at the end of 2017.
- » £615 billion is managed by IA members in Scotland. Almost a quarter of assets (23%) managed by UK-headquartered asset managers are represented by managers with their headquarters in Scotland.
- » The UK is the largest centre of asset management outside of the US. It is the largest centre of asset management in Europe, accounting for 35% of all assets under management.
- » Assets managed for European clients increased by almost 30% year-on-year, bolstered by extremely strong flows into EU UCITS funds in 2017.
- » 40% of the assets managed by UK asset managers are from overseas clients. £3.1 trillion is managed for investors from overseas, which translates to earnings representing 6% of net services exports.
- » £1.7 trillion is managed in the UK for overseas funds (up from a revised £1.3 trillion at the end of 2016). The vast majority of this (84%) is managed for funds domiciled in Ireland and Luxembourg.
- » £1.7 trillion is invested in the UK economy via traditional asset classes such as equities, corporate bonds and commercial property, and more recently via other assets such as infrastructure and direct lending.



## ROLE OF ASSET MANAGEMENT

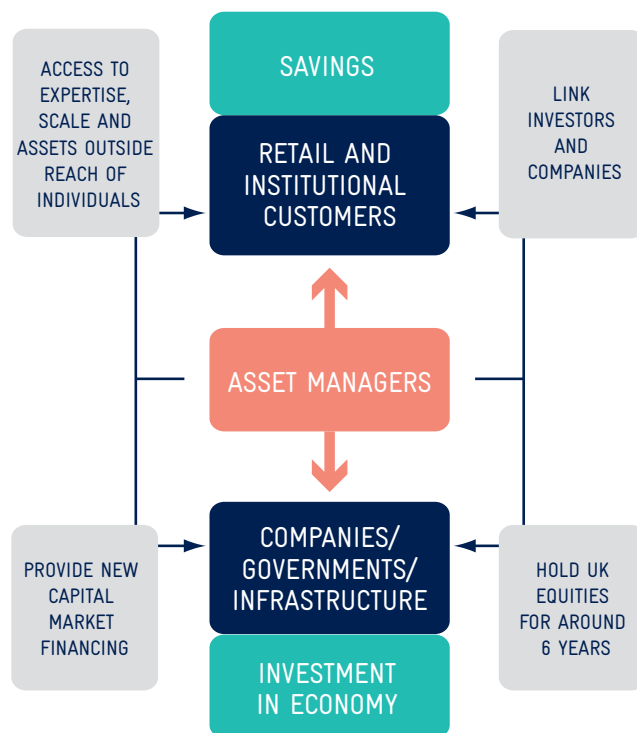
The UK asset management industry has a central role in the economy, channelling savings into investment (see Figure 1). As this report explores, the industry’s clients are both retail savers and institutions such as pension schemes and insurance companies, who act on behalf of millions of individuals, in the UK and all over the world.

The fundamental purpose of asset management is to deliver good outcomes to those clients. This includes providing expertise and achieving economies of scale that allow access to a wide range of assets that would normally be out of reach for individual investors. Using shares, bonds and other assets such as property, asset managers can deliver returns over many years while managing the risk appropriately. The sophistication of the services varies, with some clients, e.g. defined benefit (DB) pension schemes, facing increasingly complex challenges.

A second side of the industry’s role reflects the actual investment and here the purpose of asset managers is to ensure that capital markets work effectively for this investment to take place. In allocating capital, asset managers contribute to market efficiency and to correct price information. This facilitates both primary issuance when companies or governments are trying to raise money, and secondary trading of different instruments. Without this, capital markets cannot grow effectively and may even destabilise. Asset managers thus contribute to sustainable growth, benefiting both clients and non-clients.

Asset managers are not unique in this as other financial institutions and individuals contribute to capital market efficiency but the industry has historically been at the heart of long-term capital allocation. And as long-term holders of investments, asset management firms also have an important responsibility to undertake stewardship activity over the companies they invest in. UK asset managers hold UK equities for approximately six years.<sup>1</sup>

**FIGURE 1: THE ROLE OF ASSET MANAGERS IN CHANNELLING SAVINGS TO INVESTMENTS**



“IT’S NOT JUST ABOUT RETURN, IT’S ABOUT RESPONSIBLE DEPLOYMENT OF CAPITAL TO BUSINESS AND THEN MAKING SURE THOSE BUSINESSES ARE WELL MANAGED. THAT LEADS TO GROWTH, WHICH ALLOWS PEOPLE TO HAVE A BETTER RETIREMENT. OUR INDUSTRY FACILITATES THAT WHOLE PROCESS.”

<sup>1</sup> The contribution of asset management to the UK economy, July 2016, Oxera

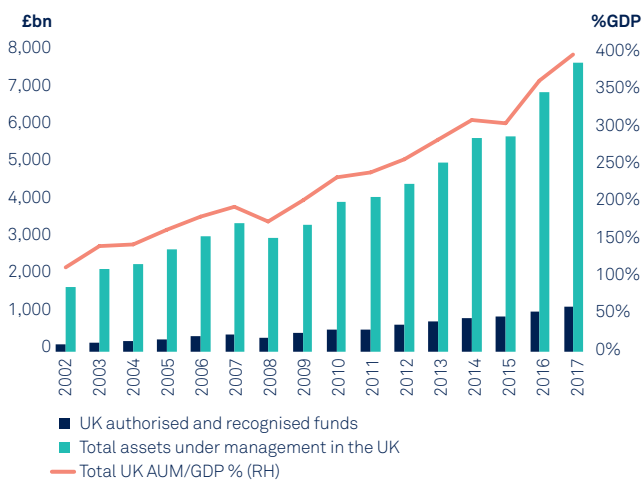
## SIZE OF THE UK INDUSTRY

At the end of 2017, IA members, as outlined in Figure 2, managed £7.7 trillion in the UK, an 11% increase from the end of 2016 (see Chart 1).

This growth partly reflected strong asset performance, particularly in overseas equities as double-digit returns were seen in many markets during 2017.

At the same time, a combination of high inflows and strong market appreciation saw total assets held specifically in investment funds reach £1.2 trillion, up 15% year on year.<sup>2</sup>

**CHART 1: TOTAL ASSETS UNDER MANAGEMENT IN THE UK (2002-2017)**



Source: IA, ONS

The continued growth in assets under management was also reflected in the industry's size relative to that of the UK economy. At the end of 2017, the size of the industry had grown to four times the size of the UK's GDP, up by around 30 percentage points from last year.

By comparison, the latest data available for Europe excluding the UK indicated that the industry there has almost a 1:1 relation to GDP. This means that asset management is considerably more important to the UK economy than it is to the economies of other European countries.<sup>3</sup>

**FIGURE 2: WHO ARE THE IA'S MEMBERS?**

Full members of the IA can be broken down into five broad groups.

**1 Large asset management firms** (both UK and overseas-headquartered), which may be independent or part of wider financial services groups such as banks or insurance companies. They undertake a wide range of asset management activities across both retail and institutional markets and manage substantial amounts for overseas client in the UK. Such firms will typically be managing >£50 billion from the UK, but a number of international firms have a smaller UK footprint.

**2 Small and medium-sized asset management firms**, primarily focused on UK and/or European clients, which undertake a diverse range of activities, of which asset management is a constituent part.

**3 Fund managers**, whose business is based primarily on authorised investment funds.

**4 Specialist boutiques and private client managers** with a smaller asset and client base and, typically, a specific investment or client focus.

**5 Occupational pension scheme (OPS) managers** running in-house asset management services for a large scheme.

<sup>2</sup> Includes assets in both UK authorised and recognised funds, capturing overall UK investor holdings in funds. See Chapter 5.

<sup>3</sup> IA analysis of EFAMA data.





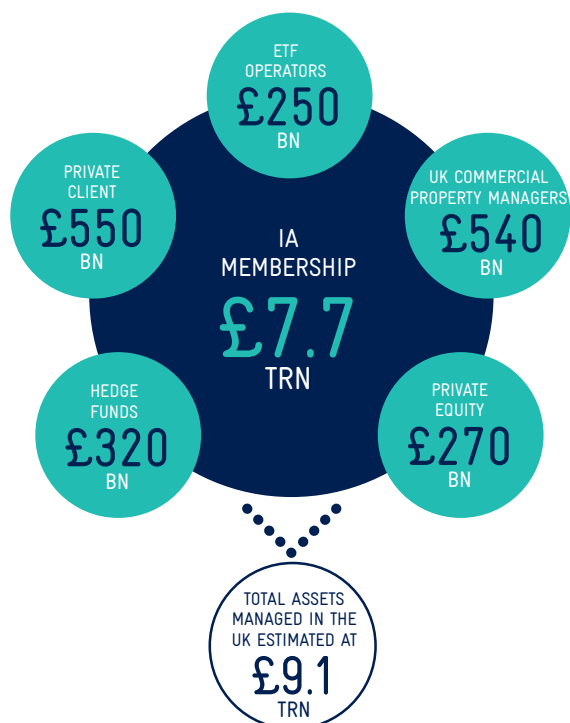
## SCALE OF WIDER INDUSTRY

IA members represent the majority of the UK asset management industry in asset terms (85%). Firms not covered in detail in this report can be broadly split into the following categories:

- Hedge funds
- Private equity funds
- Commercial property management
- Discretionary private client management
- A small number of dedicated ETF operators
- Firms who are not members of the IA for reasons not noted above

Figure 3 provides estimates to show how these wider parts of the industry contribute to total assets under management in the UK.

**FIGURE 3: WIDER ASSET MANAGEMENT INDUSTRY**



Source: ComPeer, Morningstar, Hedge Fund Intelligence/ EuroHedge, Investment Property Forum, IA estimates based on external data where necessary.

## SCOTLAND AS A MAJOR CENTRE

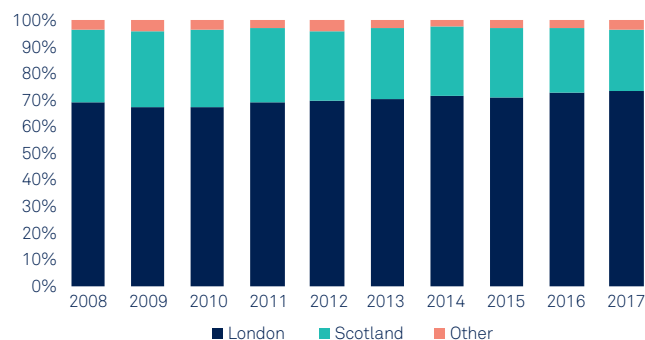
Although the City of London remains the leading centre of asset management activity in the UK, Scotland, and particularly Edinburgh, plays a key role nationally. Almost a quarter (23%) of the assets managed by UK-headquartered asset managers are represented by managers with headquarters in Scotland (see page 92).

Looking at this from a different perspective, assets managed in Scotland represented 8% of total assets managed by IA members at the end of 2017, accounting for £615 billion of total assets.

The fact that lower levels of assets are managed in Scotland than would be suggested by the location of firm headquarters is indicative of the fact that, whilst firms may have their headquarters in Scotland, many IA members headquartered in Scotland undertake asset management activity in other regions, most notably in London. This is reflected in the IA's data on location of staffing, which shows that London is more likely to be a location for portfolio manager jobs than other areas of the UK (see page 89).

Chart 2 shows that the regional split has remained relatively unchanged from a decade ago, with more than two thirds of UK-managed assets run by firms with a headquarters in London, although the relative importance of London does appear to show a gradual increase in recent years.

**CHART 2: UK-MANAGED ASSETS BY UK REGIONAL HEADQUARTERS (2008-2017)**



## POSITION OF UK ASSET MANAGEMENT INDUSTRY IN EUROPE AND WORLDWIDE

The UK continues to dominate the asset management industry within Europe, although its market share fell slightly from 36% in 2015 to 35% in 2016 (see Figure 4).

In recent years, the UK has outweighed the next three largest European countries put together. This is still the case. Spain has appeared in the list of the top ten European countries for the first time, increasing its market share to 1%, making it the eighth largest centre of asset management in Europe.

In a global context, this puts the UK as the second largest asset management centre in the world after the United States, and ahead of Japan as third largest.

**TABLE 1: GLOBAL ASSETS UNDER MANAGEMENT**

	Assets under Management (local currency) <sup>4</sup>	Assets under Management (£ equivalent)
US	\$35 trillion	£22.2 trillion
Europe	€23 trillion	£19.6 trillion
Japan	¥514 trillion	£3.4 trillion

**FIGURE 4: ASSETS UNDER MANAGEMENT IN EUROPEAN COUNTRIES (DECEMBER 2016)**



Country	Net assets (€bn)	Market share
1. UK	8,093	35%
2. France	3,971	17%
3. Germany	2,093	9%
4. Switzerland	1,646	7%
5. Netherlands	1,326	6%
6. Italy	1,229	5%
7. Denmark	386	2%
8. Spain	314	1%
9. Belgium	301	1%
10. Austria	132	1%
Other	3,360	15%
<b>TOTAL</b>	<b>22,851</b>	

Source: EFAMA

<sup>4</sup> US estimate based on North America Data from Global Asset Management 2018, BCG, 2018. European data from Asset Management in Europe, 10th Annual Review, EFAMA (provisional at time of publication). Japanese data from Japan's Asset Management Business 2017/2018, NRI

## OVERSEAS CLIENT MARKET

The UK maintained its position in 2017 as a pre-eminent centre for portfolio management on behalf of investors worldwide with £3.1 trillion, ie. 40%, of all assets in the UK being managed on behalf of overseas clients.

The largest client base remains the EEA, for which the UK industry manages approximately £1.7 trillion. Around £130 billion in assets is managed for clients in other parts of Europe, notably Switzerland (see Figure 5). Assets managed for European clients increased by almost 30% year-on-year, bolstered by extremely strong flows into EU UCITS funds in 2017.<sup>5</sup>

**FIGURE 5: ASSETS MANAGED FOR OVERSEAS CLIENTS**

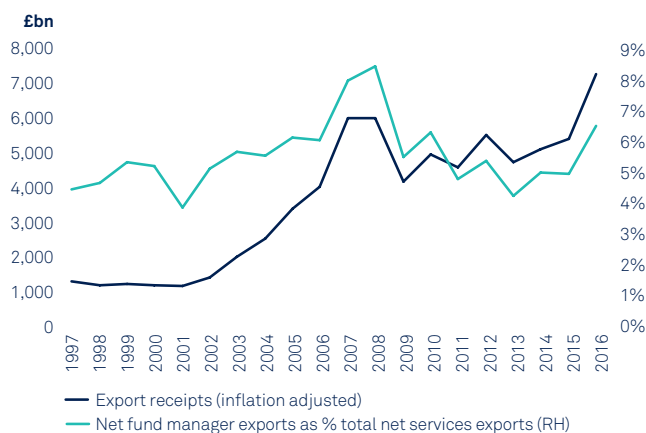


## IMPORTANCE TO UK SERVICE EXPORTS

Given the size of its overseas client base, the asset management industry makes a significant contribution to the UK's service exports. The value of export receipts has increased sevenfold on an inflation adjusted basis in the last 20 years. Chart 3 indicates that although there has been some volatility from year to year, export earnings represented an average of 6% of total net exports over the past ten years.

Chart 3 captures earnings by independent asset managers and is thus likely to understate earnings from asset managers that are part of a wider financial services group such as an investment bank or insurer. As such, the actual contribution of asset management overall to service exports is likely to be higher.

**CHART 3: EXPORT EARNINGS OF FUND MANAGERS AND CONTRIBUTION TO SERVICES EXPORTS (1997-2016)**



Source: ONS

<sup>5</sup> European Quarterly Statistical Release, EFAMA Q1-Q4, 2017. Note there is a residual of overseas clients invested in pooled arrangements where the location of underlying client cannot be easily identified

## SERVICES TO OVERSEAS FUNDS

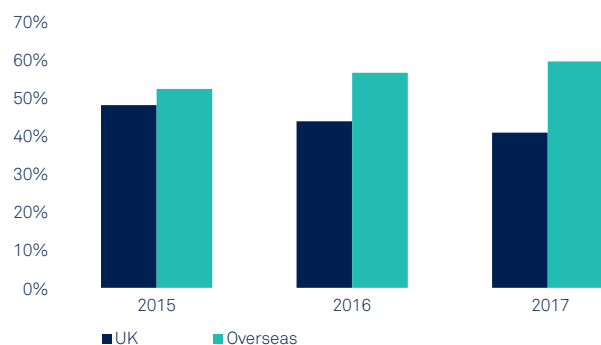
In addition to the size of the overseas customer market, we capture a related but distinct data point relating to overseas-domiciled fund assets that are managed in the UK. These may be sold either to UK or overseas customers.

New data suggests that, at the end of 2017, £1.7 trillion was managed in the UK for overseas funds (up from a revised £1.3 trillion at the end of 2016). The vast majority of this (84%) was managed for funds domiciled in Ireland and Luxembourg.

The proportion of overseas funds managed for the various overseas domiciles has stabilised over the last three years, with around half (53%) managed for funds in Ireland and a third (31%) for funds domiciled in Luxembourg.

Although the split across overseas domiciles has remained broadly stable, the split between UK and overseas domiciles has changed in favour of overseas. Specifically, there has been a gradual increase in the proportion of assets managed by IA members for funds domiciled overseas in comparison to UK-domiciled funds (see Chart 4).

**CHART 4: CHANGE IN PROPORTION OF ASSETS MANAGED FOR UK AND OVERSEAS FUNDS (2015-2017)**



## SAFEGUARDING THE GLOBAL POSITION OF THE INDUSTRY

The UK's place as a pre-eminent centre of asset management has been undisputed for a number of years but this is by no means guaranteed in the future. Brexit raises a range of challenges for the industry, from immediate regulatory questions such as fund passporting through to business operation issues, including maintaining access to talent and facilitating the seamless transfer of data.

Many UK managers already have fund ranges both in the UK and at least one member of the EU27, most commonly in either Ireland and/or Luxembourg. Consequently the changes they reported having made to date to their businesses in preparation for the UK leaving the EU were fairly specific and included:

- Ensuring the firm has a UCITS Management Company located within the remaining EU27 countries.
- Locating a MiFID regulated entity in one of the remaining EU27 countries.
- Creating limited jobs in the EU27 offices to enable them to continue to distribute funds more easily across Europe post Brexit.

Where jobs were reported being created outside of the UK the numbers are small – “in the tens not the hundreds” – confirming what members had reported to us in the last two years.

The concern most commonly shared was that asset managers around the globe are permitted to continue to delegate asset management activity to offices where the most relevant expertise is located, whether this is the UK, continental Europe, the US, the Far East or elsewhere.

The ability to delegate asset management to areas of expertise was widely stated as being fundamental to delivering a high quality service to investors all over the world. This will require Regulatory Cooperation Agreements to be put in place prior to the UK becoming a third country.

## SUPPORTING THE UK ECONOMY

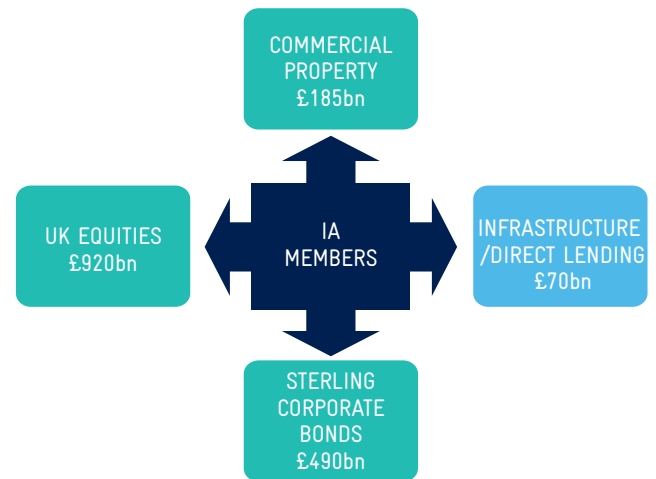
Through channelling savings to capital markets, the asset management industry is a key source of funding for the economy providing financing through different asset classes including equities and bonds as well as real assets such as property and infrastructure – see Figure 6.

In 2017, the industry had £920 billion invested in UK equities representing roughly one third of the UK market capitalisation. The exposure to UK equities as a proportion of holdings over the past twenty years has fallen significantly (see page 48 for further discussion). This has been driven both by two main factors. First, a sustained erosion in ‘home bias’, mirrored in other countries, whereby institutional and retail customers are accessing a more international basket of shares (see page 63 and page 68). Second, significant changes in institutional pension allocations which has seen a de-risking, reflecting both regulatory/accounting changes and maturing DB schemes.

Moreover, the UK’s asset management industry continues to play a primary role in corporate debt financing having almost half a trillion invested in sterling corporate bonds. Independent research suggests that asset managers have purchased the majority of corporate bond issues in recent years, as companies have turned increasingly to the debt markets to raise capital.<sup>6</sup>

Importantly, investment is increasingly taking place via more diverse asset classes such as infrastructure and direct lending, which are especially attractive to DB pension schemes and insurers looking to match their liabilities and cash flow requirements. Infrastructure investment particularly has seen considerable growth as discussed in the next section.

**FIGURE 6: IA MEMBER HOLDINGS IN UK ASSET CLASSES<sup>7</sup>**



<sup>6</sup> The contribution of asset management to the UK economy, July 2016, Oxera

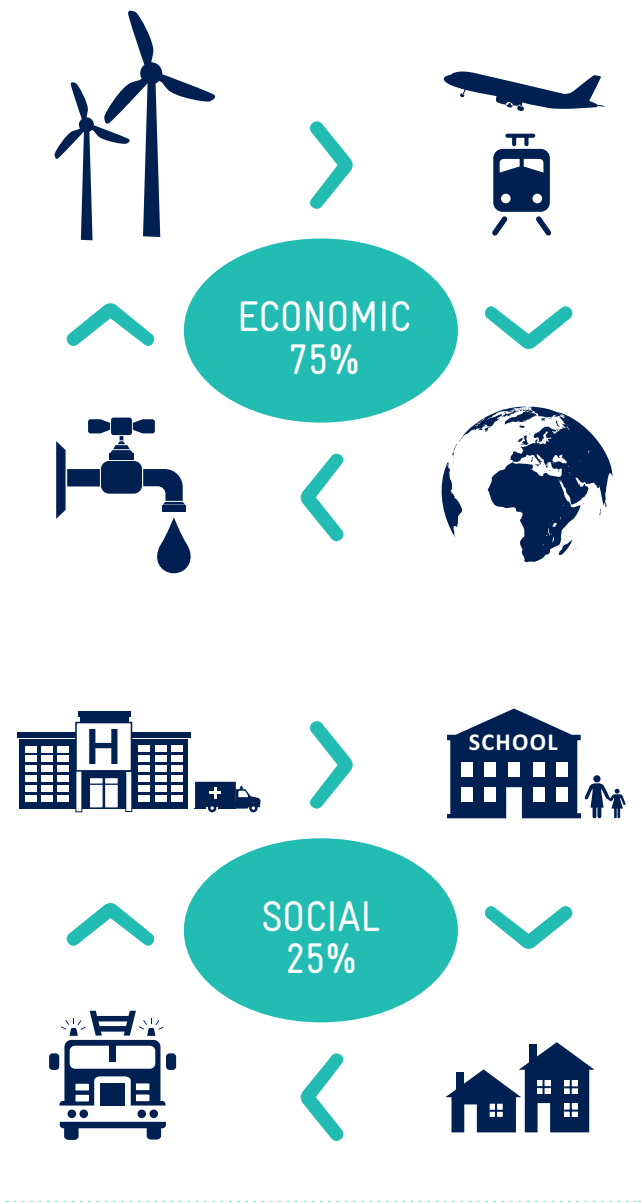
<sup>7</sup> The majority of property investment is in commercial property, however a small amount may be allocated to residential accommodation. The majority of infrastructure investment is UK but some may be invested overseas.

## INVESTMENT IN UK INFRASTRUCTURE

The amount of investment reported by UK asset managers into infrastructure remains low in absolute terms, but grew to £40 billion by the end of 2017, from £29 billion reported at the end of 2016.<sup>8</sup> Although improvements in data reporting have partly contributed to this growth, increased investment is the central reason. On a like-for-like basis, assets increased by 24% year on year.

Similar to the findings in 2016, three quarters of the total invested by IA members at the end of 2017 (75%) was in economic infrastructure, which includes projects such as energy, transport, utilities and environmental. The remaining quarter was invested in projects which offer a social benefit, particularly social housing (see Box 1) and healthcare-related projects such as hospitals (see Figure 7).

**FIGURE 7: INFRASTRUCTURE INVESTMENT BY IA MEMBERS**



<sup>8</sup> IA data captures the majority of investment by asset managers in the UK. Infrastructure investment is also facilitated by companies outside of the IA membership such as overseas asset managers and specialist infrastructure managers, which will not be captured in the IA's data.

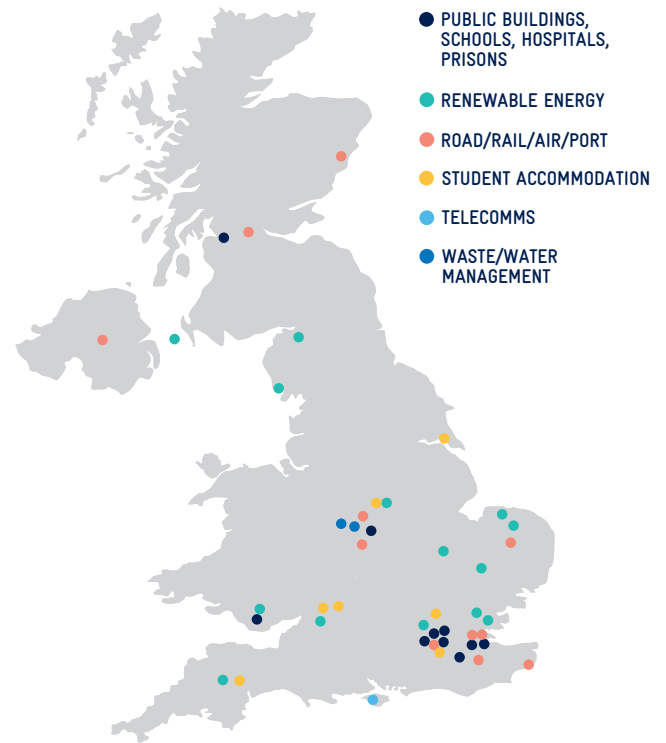
The majority of this investment is estimated to be in UK infrastructure projects. Most UK asset managers will also consider investment in overseas projects that can meet the strict criteria required by their institutional clients.

“MUCH MORE COULD BE DONE AROUND INFRASTRUCTURE AND FUNDING, CAPITAL PARTNERSHIPS AND HOME BUILDING – PRODUCING CAPITAL PROJECTS THAT BENEFIT THE BROADER ECONOMY.”



The range of projects facilitated by IA members on behalf of their clients is extremely broad and Figure 8 provides a flavour of the projects that have been supported by UK asset managers in recent years.

**FIGURE 8. SELECTION OF UK INFRASTRUCTURE INVESTMENT FACILITATED BY IA MEMBERS**

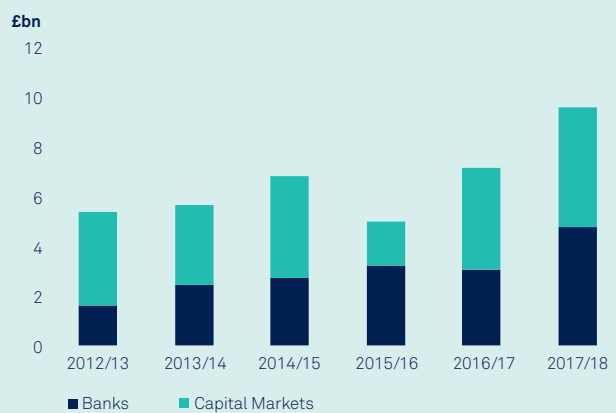


## BOX 1: FINANCING SOCIAL HOUSING IN THE UK

The funding of social housing has undergone a number of step changes over the last 40 years. In the early 1980s housing associations were funded by the Housing Corporation, which provided grant funding. During the 1980s high street lenders entered the market financing housing that would provide them with what was effectively a government guaranteed rental stream, backed by housing benefits. As long-term finance from high-street lenders has become harder to come by housing groups have looked towards the capital markets for funding, via the bond market and private placements.

Housing Associations accounted for around 60% of social housing stock in 2017/2018 and almost half of housing association financing now comes from capital markets. IA members are a key facilitator of this funding, helping to meet the UK's housing needs by financing social housing via capital markets.

**CHART 5: NEW HOUSING ASSOCIATION FINANCING BY BANKS AND CAPITAL MARKETS<sup>9</sup>**



Source: Homes and Communities Agency

<sup>9</sup> Quarterly survey of private registered providers, Homes and Communities Agency



# 2 CHANGING DYNAMICS OF ASSET MANAGEMENT IN THE UK: TOWARDS A NEW MAINSTREAM?

## KEY FINDINGS

The asset management industry is entering a period of accelerating change encompassing six key themes. Some are particular to the UK market, but others reflect trends seen elsewhere in Europe and the rest of the world:

- 1 An evolution in the investment ecosystem.** The number of companies listed on public markets has reduced in the last decade, notably in the US and to a lesser extent in the UK and mainland Europe. At the same time, there has been increased interest in private markets as asset managers have expanded into real assets such as infrastructure.
- 2 An increasing emphasis on responsible and sustainable investment.** Investment remains dominated by the larger DB pension schemes but growing numbers of younger people saving in pensions as a result of automatic enrolment suggests that responsible investment could grow significantly in popularity. Although negative screening dominates dedicated responsible strategies, asset managers are incorporating ESG criteria into their mainstream investment strategies.
- 3 An ongoing change in product demand.** Over the last decade there has been a shift in asset allocation out of traditional equity and fixed income into more solutions-focused strategies including liability-driven investment, infrastructure and direct lending. In the institutional market this shift has been fuelled by interest from DB pension schemes and insurance companies looking for investments that offer ways to more closely match their future liabilities.
- 4 Rapid technological change.** Technology continues to be a fundamental element in changing how asset management firms serve their wide range of investors. Three key areas are:
 
  - improving the efficiency of back office systems such as transaction processing.
  - using big data to improve decision making and achieve better investment outcomes.
  - enhancing the investor experience and making investment easier than ever for the individual by facilitating access to funds through a variety of media.
- 5 Diverse patterns of corporate M&A activity.** Mergers and acquisitions are still occurring between traditional asset management firms but asset managers are increasingly diversifying their capabilities into other areas including private markets, technology or provision of advice. They are also exploring ways to improve their distribution capabilities either directly to end investors or by strengthening their relationships with platforms and financial advisers.
- 6 A significant regulatory and policy focus on the industry.** The regulatory and policy environment continues to reflect a mixture of challenge and opportunity for the industry in the UK and globally. Value delivery for customers is a key theme, alongside an ongoing look at the industry's wider role from a financial stability perspective.

The asset management industry is entering a period of accelerating change. Six key themes are identified and discussed in this chapter. Some are particular to the UK market, but others reflect trends seen elsewhere in Europe and the rest of the world:

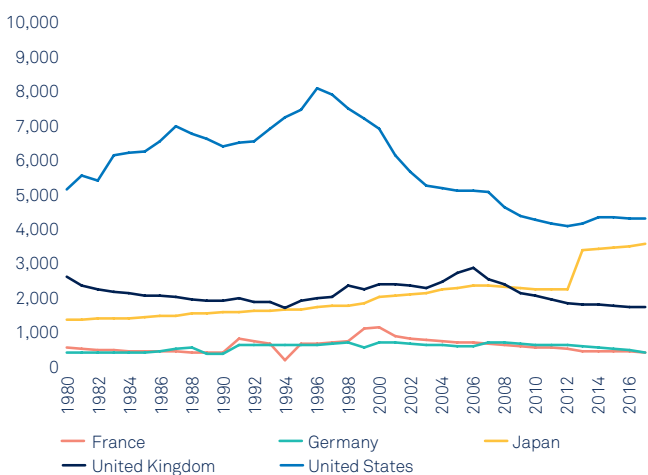
- 1. An evolution in the investment ecosystem** that has seen an increasing emergence of private markets, particularly in the context of wider expectations of market-based finance in the post-2008 environment.
- 2. An increasing emphasis on responsible and sustainable investment**, as a result of tangible threats from environmental damage and broader socio-political concerns to ensure a more inclusive and accountable capitalist model.
- 3. An ongoing change in product demand** towards greater solution and outcome-based investment strategies.
- 4. Rapid technological change**, which has the potential to transform every aspect of the asset management value chain, from capital markets through to fund products and retail distribution. The flipside of this innovation is an ever more complex set of risks in terms of cyber security.
- 5. Diverse patterns of corporate M&A activity**, which are seeing both horizontal and vertical consolidation as some asset managers deepen their capabilities in the advisory and distribution space.
- 6. A significant regulatory and policy focus on the industry**, with a key theme of value delivery for customers, alongside an ongoing look at its wider role from a financial stability perspective.

## 1. EVOLUTION IN THE INVESTMENT ECOSYSTEM

### PUBLIC VS PRIVATE MARKETS

The number of listed companies in many of the key public markets for UK asset managers has fallen in recent years. Chart 6 shows the fall is most significant in the US, where numbers are almost half what they were in the late nineties.

**CHART 6: NUMBER OF LISTED DOMESTIC COMPANIES IN TRADITIONAL MARKETS<sup>10</sup>**

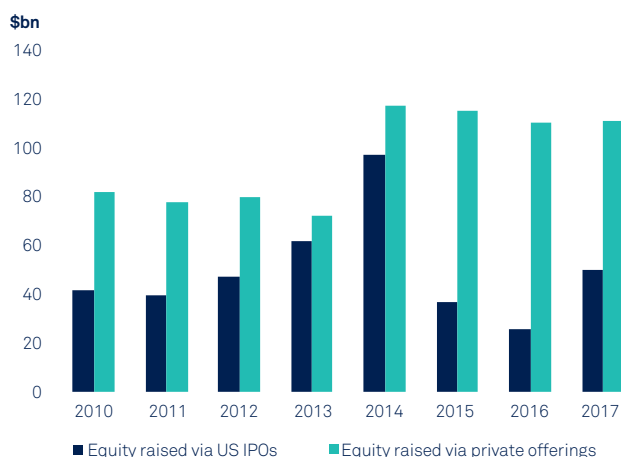


Source: World Bank, LSEG

Much of the decline in the number of public companies in the US since the mid-nineties is related to the number of business failures and delistings following the dot.com bubble. It has become more stable since the financial crisis of 2008 but in an environment where the number of companies overall is increasing, it suggests that many of today's new companies have chosen to grow outside the public equity market raising capital in many forms such as venture capital, private equity or debt financing (see Chart 7). Companies listing publicly in the US more recently have tended to be more mature in contrast to the prior boom-bust cycles.<sup>11</sup>

<sup>10</sup> Listed domestic companies, including foreign companies which are exclusively listed, are those which have shares listed on an exchange at the end of the year. Investment funds, unit trusts, and companies whose only business goal is to hold shares of other listed companies, such as holding companies and investment companies, regardless of their legal status, are excluded.

<sup>11</sup> Looking behind the declining number of public companies. An analysis of trends in US capital markets, EY, 2017

**CHART 7: EQUITY RAISED VIA US IPO VS EQUITY RAISED VIA PRIVATE OFFERINGS<sup>12</sup>**

Source: Professor, Hal S. Scott, Nomura Professor and Director of the Program on International Financial Systems (PIFS), Harvard Law School, U.S.A

Europe has experienced a similar trend. In the UK, numbers have fallen to less than two thirds of the figure they were just over a decade ago. Markets in continental Europe have not experienced drops of this scale, but nevertheless the trend has clearly been downward in the last ten years.<sup>13</sup>

Looking specifically at the UK, there are ever more companies. At the end of 2017, four million companies were on the Companies House register compared to 3.4 million in 2014. A large number of these will be extremely small, but many firms appear to be choosing not to list on public markets. Reasons for this may include:

- the increased burden of registration
- tougher corporate governance and transparency regulations
- debt becoming a more attractive way of raising capital than equity

The reduction in the size of traditional public equity markets has occurred alongside the shift into more diversified assets among IA members. Part of this has been a notable increase in the demand for real assets

in recent years from institutional investors looking for alternative sources of yield and diversification. The growing involvement among IA members in infrastructure investment (£40 billion at the end of 2017) has already been explored (see page 22).

At the same time, asset managers are exploring investment opportunities in the loan market as bank involvement has decreased following the financial crisis. A number of IA members are now engaging in direct lending and members reported around £31 billion in assets under management in direct lending vehicles at the end of 2017. Around one fifth of this (£6 billion) was reported to be in private placements, which involve the sale of securities to a relatively small number of institutional investors, with the remainder being in a variety of arrangements such as commercial real estate finance, structured finance and other private loans and mortgages.

The market has seen the start of a number of new direct lending funds in recent years. Increased competition has led to some reports of the need for investors to move down the credit spectrum in order to achieve the returns they are looking for.<sup>14</sup> Nevertheless, members frequently mentioned private markets as one of the most likely growth areas for the next twelve months. Reasons behind the attraction of private markets included the search for returns relatively uncorrelated to the mainstream asset classes and the continuing appetite for attractive levels of yield now not possible in more traditional sectors.

**“IF YOU LOOK AT THE INSTITUTIONAL SPACE THERE IS MASSIVE DEMAND FOR PRIVATE MARKET INVESTMENTS. IT’S PROBABLY THE MOST DEMANDED CATEGORY THAT WE HAVE, WHETHER IT’S INFRASTRUCTURE, REAL ESTATE OR PRIVATE DEBT. THAT TREND WILL CONTINUE.”**



<sup>12</sup> Contribution to Panel 4 discussion IOSCO Annual Conference, Professor Hal S. Scott, 2018. Full presentation available on the IOSCO website.

<sup>13</sup> Listed domestic companies, World Bank Open Data

<sup>14</sup> Revisiting Direct Lending. KPMG investment advisory, April 2018

## ROLE OF ASSET MANAGERS IN FUNDING SMES

The UK asset management industry has long directed investment towards smaller firms via small cap equity markets. While starting from a lower base, since 2008 funds under management in the IAs UK Smaller Companies sector have increased by 270% to £16 billion, compared to an increase of 130% for the UK All Companies sector (to £173 billion).

Furthermore, after the financial crisis, the contraction of bank lending led to the emergence of asset managers as a significant source of capital for companies looking for private investment. One of the beneficiaries of this has been small and medium sized enterprises (SMEs). Investment in this size of enterprise lies outside the scope of many IA members, and some felt quite strongly that the industry is an allocator of capital rather than a provider of funding.

There are a range of challenges in investing in SMEs for asset management companies, affecting availability to both institutional and retail investors. These are currently being explored in the UK under the auspices of the Patient Capital Review, as well as the Investment Management Strategy II.<sup>15</sup> Issues for the asset management industry relate to both the demand and supply side, and include:

- Ensuring that fund structures can be adapted to less liquid investment (an issue not just for the SME part of the market, but illiquid assets more generally).
- Scalability for funds, where the challenge of finding suitable companies to invest in may become evident at relatively low levels of assets under management.
- A lack of customer demand in parts of the market, particularly in DC default arrangements, where there is sometimes a lack of familiarity with the asset class amongst trustees.<sup>16</sup>

Nonetheless, a number of IA member firms are actively developing expertise in this part of the economy, not least via some of the direct lending funds referred to on page 27. As with other private assets, appetite from insurance companies and pension funds is high.

“IF THE QUESTION IS CAN ASSET MANAGEMENT PLAY A NEW ROLE IN ALLOCATING CAPITAL TO SMES WHERE PREVIOUSLY IT HAD BEEN DONE BY THE BANKS?, THE ANSWER HAS TO BE YES.”



It was also mentioned that asset managers could assist on an ongoing basis by using their expertise to help smaller companies to continue to grow and succeed in a sustainable way.

“IT’S OFTEN THE PROVISION OF EXTERNAL ADVICE AND GUIDANCE THAT GETS COMPANIES THROUGH THE DIFFICULT PERIOD WHERE THEY ARE GROWING INTO SOMETHING MORE SIZEABLE. THE ASSET MANAGEMENT INDUSTRY HAS A ROLE TO PLAY IN THAT TERRITORY.”



<sup>15</sup> The UK Investment Strategy II, HM Treasury, 2017. See chapter 7

<sup>16</sup> Putting Investment at the Heart of DC Pensions, IA position paper, 2018.

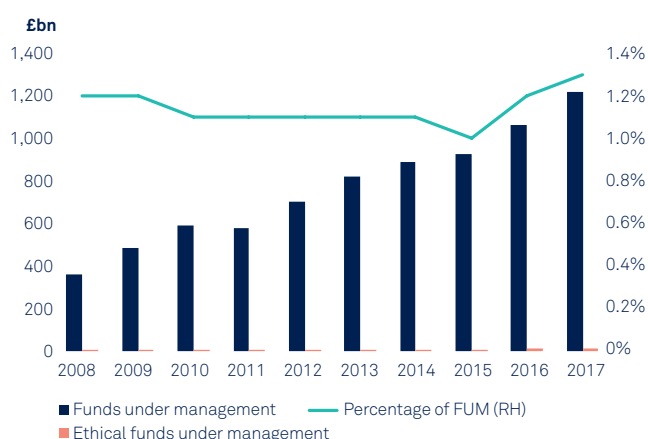
## 2. INCREASING EMPHASIS ON RESPONSIBLE AND SUSTAINABLE INVESTMENT

Recent years have seen an increased emphasis on responsible and sustainable investment. This has resulted, in part, from the global threats from environmental damage, but also from broader socio-political concerns, which have led to demands of greater accountability and scrutiny on how companies are run and their impact on wider stakeholders beyond measures of pure price valuation.

There are different ways to measure the value of assets managed according to these criteria, with varied terms including: ethical, sustainable, socially responsible, Environmental, Social and Governance (ESG).

IA monthly fund statistics suggests that investment into UK funds traditionally categorised as ‘ethical’ has remained proportionately unchanged in the last decade (1.3%), although there are some signs of an uptick in the last two years – see Chart 8. This difference likely reflects the narrow definition of the ‘ethical’ flag.

**CHART 8: NET RETAIL SALES OF ETHICAL FUNDS AS A PERCENTAGE OF FUNDS UNDER MANAGEMENT (2008-2017)**



This is consistent with our discussions with member firms, which suggested that dedicated ESG investment

remains primarily the domain of the larger pension schemes, most frequently those in northern Europe.

However, a range of shifts in Government and societal attitudes in the UK are starting to change the approach to responsible and sustainable investment:

- Following a report from the Law Commission, the Government is consulting on stronger requirements for pension scheme trustees in considering and reporting on ESG issues, something which the FCA intends to mirror for Independent Governance Committees (IGCs) in insurance-run DC schemes. The proposals also include broader stewardship.
- There is an increasing body of evidence that younger people may prioritise ESG investments. With the advent of pensions automatic enrolment (see page 56), this could over time drive much greater pension scheme focus on these issues, as well as having a wider impact in the UK retail fund markets.

As well as implementing dedicated bespoke strategies asset managers may implement ESG principles within mainstream investment in a number of ways, including:

- Actively engaging with companies to promote good practice to reduce investment risk. In 2017 the IA found that nine in ten asset managers carried out active engagement with the companies they invest and almost two thirds reported that engagement with UK companies resulted in better investment decisions.<sup>17</sup>
- Taking them into consideration to ascertain their impact on company valuations so as to deliver improved investment outcomes for clients, rather than taking a moral view on the suitability of an investment, although whether the two are separate is not clear cut.

“THE VALUATION AND MORAL QUESTIONS ARE LINKED BECAUSE RETAIL CUSTOMERS WILL NOT END UP DOING BUSINESS WITH THOSE COMPANIES IF THEY THINK THEY ARE A NEGATIVE INFLUENCE.”



<sup>17</sup> Stewardship in Practice Asset Managers and Asset Owners, The IA/PLSA, September 2016

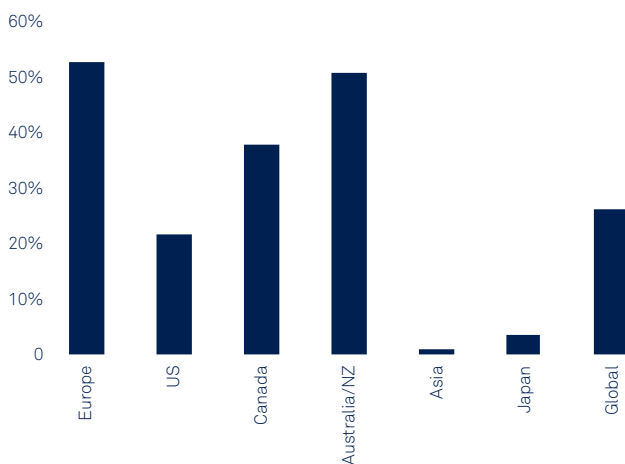
In a world where the stewardship responsibilities of asset managers are increasingly in the spotlight, some firms might consider all their assets under management as being managed according to ESG criteria. Other firms would only consider ESG strategies to apply to a dedicated set of funds or mandates with customised investment approaches.

The Global Sustainable Investment Alliance (GSIA) reported that \$23 trillion of assets are being managed according to responsible investment strategies around the globe.<sup>18</sup> This incorporates assets being managed according to a wide range of strategies including:

- Negative/exclusionary screening
- Positive/best-in-class screening
- Norms-based screening
- Integration of ESG factors
- Sustainability themed investing
- Impact/community investing, and
- Corporate engagement and shareholder action.

Within Europe, the GSIA suggests that more than half of the assets managed in Europe are managed according to SRI criteria (see Chart 9).<sup>18</sup>

**CHART 9: PROPORTION OF SRI RELATIVE TO TOTAL MANAGED ASSETS IN 2016**



Source: Global Sustainable Investment Alliance

<sup>18</sup> Global Sustainable Investment Review, 2016, GSIA

<sup>19</sup> Growing a Culture of Social Impact Investing in the UK, Independent Advisory Group, 2017

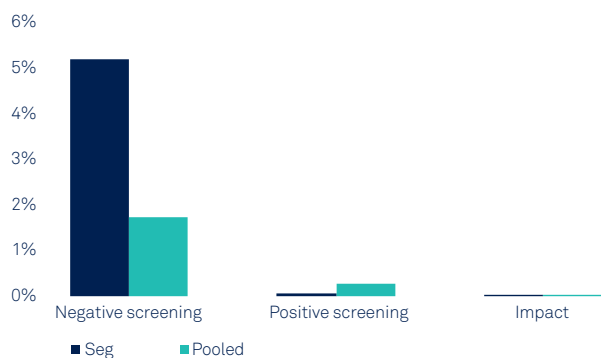
This mixed approach to interpretation makes it difficult to determine what is motivating investors, and how they are choosing to apply their own beliefs and values to their choice of investment strategy and work is ongoing nationally and internationally to provide greater clarity (see Box 2).

The Survey therefore approached this subject slightly differently in 2017 and asked members to provide a total figure for investment according to any ESG criteria, but, more specifically to report mandates and funds that were managed according to the following criteria:

- **Negative screening.** An approach where the investor avoids investing in businesses that are harming people or the planet, such as oil, tobacco, or weapons production. This can be motivated by seeking to protect financial value by limiting exposure to risky practices, and / or ethical concerns.
- **Positive screening.** This approach seeks to enhance value by proactively screening for businesses that are seeking to work for the benefit of all their stakeholders, not just shareholders or owners.
- **Impact-driven investment.** Impact investments are those that help to solve pressing social or environmental challenges, as well as generate a financial return. This includes 'social investment', (investment in regulated social sector organisations, such as charities and social enterprises) as well as investment in regular profit-seeking business that are also helping tackle a societal challenge.

Approximately 7% of assets in total across pooled and segregated investments were managed by screening out companies according to responsible investment criteria. A further 0.4% of assets were managed by positively screening investments according to sustainable investment criteria. Levels of investment according to impact-driven criteria were at extremely low levels, albeit there is growing interest from government for asset owners to become more actively involved this area (see Chart 10).<sup>19</sup>

**CHART 10: DEDICATED INVESTMENT ACCORDING TO SPECIFIC ESG CRITERIA**



The adoption of screening strategies is becoming increasingly mainstream and there have recently been a number of high-profile announcements from asset management firms. For example, in November 2017 BNP Paribas Asset Management announced it would divest from tobacco stocks altogether.<sup>20</sup>

“IN FIVE YEARS’ TIME IT’S NO LONGER GOING TO BE ACCEPTABLE TO INVEST IN A NUMBER OF LISTED COMPANIES. ESG WILL BECOME COMPLETELY EMBEDDED INTO EVERY ASSET MANAGEMENT BUSINESS.”

This contrasts with the view of some of those interviewed this year, who considered that it was the decision of the asset owner whether or not to exclude investment in specific stocks or sectors, rather than something that should be imposed upon them by an asset manager.

“AT THE END OF THE DAY CLIENTS GIVE US CONSTRAINTS AND OBJECTIVES AND THEN IT’S OUR JOB TO MANAGE TO THOSE OBJECTIVES AND CONSTRAINTS TO GENERATE THE BEST PERFORMANCE WE CAN.”

Others felt that having a strong approach to ESG investment, as part of a mainstream strategy, made their service more saleable and attractive to investors even when those investors were not be looking to impose specific value-driven constraints.

<sup>20</sup> BNP Paribas announces new measures regarding the financing of tobacco companies, November 2017

## BOX 2: SUSTAINABILITY AND RESPONSIBLE INVESTMENT

Never before has there been a greater focus on the impact that the asset management industry has on society and planet. From governments, to the media to investors, there is growing demand for the asset management industry to turn a lens on itself and consider its role in the transition to a more sustainable economy.

At national and international level, major policy developments are taking place, including the European Commission's Sustainable Finance Package. This package, through which the Commission seeks to connect finance with the needs of the European economy and the EU's agenda for sustainable development, was published on the 24 May 2018 and includes proposals on:

- A taxonomy for sustainable finance
- Harmonised disclosures on the integration of sustainability risks and relating to sustainable investments
- Amendments to the MiFID II Suitability Assessment to take account of ESG preferences
- Amendments to the Insurance Distribution Directive also to take account of ESG preferences
- Introduction of low carbon and positive carbon impact benchmarks

In particular, the proposal for a sustainable finance taxonomy cuts to the heart of a key stumbling block with respect to the growth of sustainable and responsible investment – the lack of common language. Supporting the development of common language is a key priority for the asset management industry.

Domestically, a Taskforce for growing a culture of social impact investing in the UK – a collaborative approach between Government and industry – is focusing on ways of boosting social impact investment and identifying how to attract capital to contribute to solutions to social problems. A further UK-based initiative, bringing together public and private sector, is the Green Finance Taskforce that is looking for ways to mobilise capital on the scale necessary to meet the two degrees or less scenario agreed in Paris 2015.



### 3. ONGOING CHANGE IN PRODUCT DEMAND

Product demand among UK clients over the last ten years has shifted in two key ways related to client objectives, which we cover in more detail through Chapters 3-5:

- Greater demand for yield, both in the retail and institutional market, in the context of a low interest rate environment.
- Greater demand for outcome-oriented strategies. Examples include LDI in the institutional market to absolute return and volatility controlled funds in the retail market.

This has been reflected in asset class diversification, partly to provide access to yield (eg. infrastructure, direct lending) and partly to deliver outcome-oriented strategies. A particular driver here is the demand from pension schemes and insurance companies looking to manage their liabilities and match their cash flow requirements.

The combined effect has been to produce an evolution in asset allocation away from traditional equity and fixed income into a range of assets such as:

- Infrastructure
- Derivative overlay strategies
- Private equity
- Direct lending
- Hedge funds

“THE GREATEST CHALLENGE AND OPPORTUNITY ARE BOTH IN THE SAME SECTOR. A NUMBER OF FIRMS HAVE GOT INVOLVED IN REAL ASSETS. THERE IS HUGE DEMAND FROM PENSION FUNDS THAT ARE TRYING TO HEDGE LIABILITIES. THE GREATEST CHALLENGE IS THE ORIGINATION OF THE ASSETS THAT ARE GOING TO INTEREST THESE CLIENTS. YOU ARE NOT JUST WANDERING ONTO THE STOCK EXCHANGE TO BUY THESE ASSETS. YOU’VE GOT TO GO AND LOOK ACTIVELY FOR THEM. SO THAT’S PROBABLY BOTH THE GREATEST CHALLENGE AND THE GREATEST OPPORTUNITY.”



The search for outcome-oriented solutions more widely is expected to continue in both the institutional and retail space. Multi asset and other outcome-oriented solutions are likely to benefit from this demand, particularly in the growing market associated with the drawdown of DC pensions in retirement. As the population continues to age people will remain invested into older and older ages, adding to the demand for products that deliver income with an element of downside capital protection.

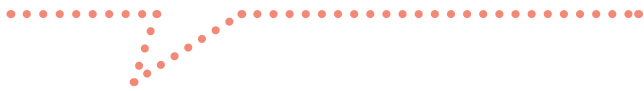
“INCOME IS THE KEY WORD AND WHETHER IT IS IN MULTI-ASSET OR IN PROPERTY, FIXED INTEREST OR EQUITY, INCOME IS WHERE THE ACTION WILL BE FOR THE NEXT GENERATION.”



## 4. RAPID TECHNOLOGICAL CHANGE

Technology is increasingly central to industry delivery, from trading to managing risk, back office operations and customer service. Harnessing technological innovation continued to be a priority for those we interviewed for the Survey this year.

“IF YOU THINK ABOUT SOME OF THE MORE COMPLICATED PROBLEMS LIKE TRADING, PUTTING PIECES OF ARTIFICIAL INTELLIGENCE IN TO DETERMINE THE RIGHT ALGORITHM FOR A PARTICULAR TRADE IS A TRANSFORMATIONAL IMPROVEMENT IN PRODUCTIVITY. CUSTOMERS WILL GET A MUCH BETTER OUTCOME.”



“TECHNOLOGY ALLOWS YOU TO FIND OUT WHAT COMPANIES ARE REALLY DOING, INCLUDING FACTORS SUCH AS HOW THEY TREAT THEIR STAFF. IT IS OFFERING US OPPORTUNITIES TO GET MORE DATA ON WHAT GOOD LOOKS LIKE.”



There were three areas where technology was considered to be particularly important:

**Improving the efficiency of back office systems such as transaction processing.** At the cutting edge, this could extend to the use of approaches such as blockchain in transaction processing. 2017 saw the first use of a blockchain-based platform to purchase funds.<sup>21</sup> This process of change is expected to accelerate significantly.

**Using big data to improve decision making and achieve better investment outcomes.** This might include using information about individual customers for more targeted marketing and to create products that can be customised to a degree that was not possible in the past. From an investment perspective it might also include the use of market data not previously available to help improve investment management strategies. This will likely require the automation of data analysis, with the more detailed information either being used to feed into more sophisticated factor-based quantitative strategies in the smart-beta environment, or to inform the investment decision making of fund managers responsible for active strategies.

**Enhancing the investor experience.** When it comes to the use of technology in communicating with the end consumer there was still a strong sense among some of those interviewed that when people are investing their own money, even where the amounts are relatively small regular payments, they often want a human connection. It was felt that this was the case even with younger investors who are more technologically confident. Nevertheless a plethora of app-based investment platforms have appeared from the FinTech sector in recent years which aim to meet a range of investor needs, including:

- Allowing individuals to access investments normally only available to institutions (e.g. corporate bonds).
- Amalgamating robo-advice with fund investment, often via ETF investment, with varying choices of ongoing management tailored to cost.
- Analysing spending habits and saving according to the amounts individuals can afford.
- Offering investment portfolios to individuals with lower barriers to entry than would normally be available.
- Rounding up purchases and saving the difference into stocks and shares ISA.
- Facilitating crowdfunding for seeding new businesses.

<sup>21</sup> Natixis AM completes blockchain transaction in fund distribution Investment Europe, July 2017

The speed at which technology is transforming the asset management industry creates opportunities for asset managers to differentiate their business, but also introduces a new type of operational risk, namely cyber security risk. Firms emphasise the extent to which the potential cyber security risks need, as a matter of priority, to be understood, managed and mitigated. In some cases this will require new and innovative approaches to security controls.

Cyber-attacks are most likely to come from organised crime groups or from a malicious insider. Risks can materialise across the entire value chain of an asset manager, including risks to client data processed by third party administrators and custodian banks.

There are key actions which help build an effective cyber security capability.

- Boards engaging fully, having an understanding of cyber security issues, and establishing clear accountability for action.
- Developing technical ability and processes to detect, respond and recover from incidents; and cyber security risks being managed effectively across the supply chain.
- Educating all employees around cyber security risks and good behaviours.

Effective collaboration across the industry can help create economies of scale and pooling of expertise that may be essential in managing this risk.<sup>22</sup>

## 5. DIVERSE PATTERNS OF CORPORATE M&A ACTIVITY

Investment management acquisition activity may take a variety of forms:

- Outright purchase and rebranding by the new parent of the acquired firms product set.
- A 'multi-boutique' approach where individual brands co-exist and compete with a shared set of common resources provided by a parent company.
- Variations of the above, where groups contain distinct brands with their own separate operations.
- Purchase of specific capabilities through the lift-in of investment teams from rival companies, which some see as much more efficient than purchasing an entire company, which was likely to come with a number of unwanted elements.

Figure 9 shows recent examples of M&A activity with more historic detail in Appendix Four. Purchases of, or mergers with, other asset managers remain the most common type of transaction. However, a number of other themes can be seen, including:

- Access to distribution
- Enhanced private market expertise
- Greater ETF capability
- DFM / advisory focus
- Stronger technological capability
- Private equity / asset manager deals

The distribution theme reflects the reality that the retail funds market in the UK remains heavily intermediated. The key routes to market are:

- Non advised sales either direct to the investor or via a fund platform
- Fully advised sales via financial adviser.

<sup>22</sup> Building cyber resilience in asset management, IA/KPMG, 2018

**FIGURE 9: NOTABLE M&A ACTIVITY DURING 2017-2018**



Advised sales continue to account for the majority of sales to UK investors. However, the use of platforms is growing and asset managers are increasingly considering how best to reach retail customers.

Those interviewed for this Survey believed that the greatest change in the next few years is likely to be in the nature of distribution. Scale continues to be important in the context of fee compression and increasing regulatory complexity. Consolidation activity may lead to a smaller number of very large managers with significant distribution capability, whether within the group or through third party relationships.

“IN THREE YEARS’ TIME, IT MIGHT NOT HAVE CHANGED THAT MUCH BUT IN TEN YEARS IT PROBABLY WILL HAVE CHANGED RADICALLY. YOU’LL HAVE A NUMBER OF VERY BIG FUND MANAGEMENT BUSINESSES WITH GREAT ACCESS TO DISTRIBUTION IN AREAS LIKE WORKPLACE PENSIONS OR WEALTH CHANNELS. THE MODEL OF A FUND MANAGER JUST BEING BRILLIANT AT WHAT THEY DO AND EXPECTING THAT OPEN ARCHITECTURE PLATFORMS WILL FIND THEM MIGHT CHANGE. THEY MIGHT HAVE TO BE CLOSER TO THE DISTRIBUTORS WHO INFLUENCE GUIDED ARCHITECTURE SO THAT THEY GET THEIR PRODUCT PUSHED THROUGH THE RIGHT PIPES.”

“I THINK THE DISTANCE BETWEEN ASSET MANAGERS AND INVESTORS MAY HAVE INCREASED IN THE LAST TEN YEARS, BE IT PLATFORMS OR OTHER INTERMEDIARIES. THAT MAKES OUR JOB AS FUND MANAGERS INCREDIBLY DIFFICULT BECAUSE SOMETIMES YOU’RE HAVING CONVERSATIONS WITH THREE PEOPLE BEFORE YOU ACTUALLY GET TO THE PERSON THAT OWNS THE PRODUCT. SO I DO THINK THAT WHETHER THROUGH CONSOLIDATION OR PARTNERSHIP, ASSET MANAGERS NEED TO GET CLOSER TO THE CLIENT AND THERE MAY BE MORE INTEGRATED DISTRIBUTION.”

There is likely to be continued blurring of roles as this consolidation continues, with asset managers playing a greater role in distribution and distributors moving ever more into the area of asset allocation. It is also not yet clear where advice will fit into the future delivery model.

Although a growing proportion of investors may no longer seek financial advice from traditional sources, the need for advice is likely to grow in a world of multiple employments, pension freedoms and varied savings habits.

“ADVICE WILL NOT GROW BACK TO THE LEVELS PRE RDR, BUT IT IS NOT GOING TO DISAPPEAR. MORE AND MORE PEOPLE NEED THAT TOUCH POINT. IT’S HOW TO DO IT AT A COST EFFECTIVE PRICE THAT IS THE TRICKY BIT. IT ALWAYS LOOKS GOOD WHEN YOU SAY ROBO-ADVICE, BUT IT ONLY GETS SO FAR. MANY PEOPLE’S PORTFOLIOS ARE COMPLICATED. THEY HAVE SEVERAL PENSIONS, ONE HERE, ONE THERE. SOMEONE MAY HAVE LEFT THEM SOME MONEY. IT’S JUST NOT SOMETHING YOU CAN PLUG INTO A MACHINE THAT EASILY.”



## 6. SIGNIFICANT REGULATORY AND POLICY SCRUTINY

The regulatory and policy environment continues to reflect a mixture of significant challenge and opportunity for the asset management industry, both in the UK and globally. Figure 10 shows how the questions about the role played by the asset management industry fall broadly into two categories – first, delivering for customers; second, serving the broader economic system.

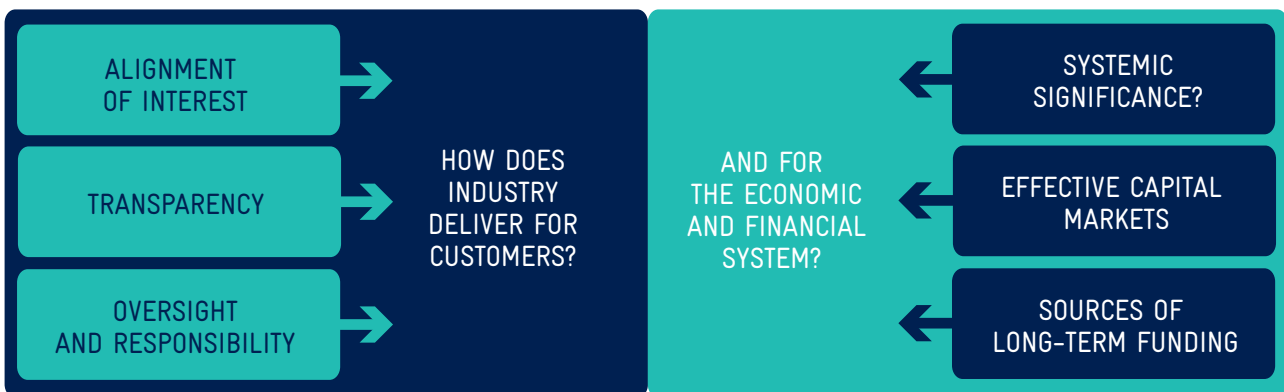
Broadly, policymakers and regulators are asking:

- How can the value of asset management to its customers be demonstrated, broadened and maximised?
- How can the needs of the broader economy be met from asset management activity (directly through market-based finance and effective capital markets, or more indirectly through minimisation of systemic risk)?

Compared to the very different operating context of the 1980s and 1990s, these questions reflect a number of factors:

- Weakened traditional sources of finance, notably banks and Government.
- Increasing individual dependence on financial markets for life-time savings needs (particularly in the context of automatic enrolment in the United Kingdom post-2012).

FIGURE 10: REGULATORY OVERVIEW



- Subdued economic growth, declining productivity and constrained wages.
- Lower equity market returns since the end of the dot com bubble of the late 1990s.
- Significant regulatory worries about further destabilisation emanating from within the financial system following the 2008 global financial crisis.

## EU-LEVEL CHANGE: IMPACT OF MIFID II

Against such a backdrop, the industry has faced increased scrutiny in domestic, European and international regulatory and policy fora. Arguably the most significant, and certainly the largest, single regulatory initiative is MiFID II / MiFIR (see Box 3).

### BOX 3: WHAT IS MIFID II / MIFIR?

Implemented on 3 January 2018, this provides the framework of EU legislation for investment intermediaries providing services to clients in relation to shares, bonds, units in collective investment schemes, derivatives and the trading of financial instruments. At a high level the Directive sets out Europe-wide conduct of business (COB) and organisational requirements for investment firms; authorisation requirements; regulatory reporting; transparency obligations; and rules on admission of instruments to trading.

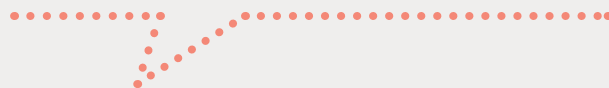
The new regulation includes a range of themes that have come to define the post-2008 environment for financial services. A particular focus is greater customer protection through transparency and alignment of interest (eg. aggregation of fees and costs and prohibition of bundled research provision), and a focus on market behaviour that uses the tool of transparency (eg. pre- and post-trade disclosure requirements, transaction reporting) alongside harder constraints on aspects of investor activity (eg. volume caps).

## PERSPECTIVES ON MIFID II

“MIFID II WAS A GOOD EXAMPLE OF HOW REGULATION CAN DRIVE POSITIVE CHANGE AND POSITIVE DEBATE WITH THE INDUSTRY. THE IMPLEMENTATION WAS CHALLENGING BUT IT MOVED US TO A WORLD WHERE WE CAN BE BETTER FIDUCIARIES TO OUR CLIENTS.”



“MIFID II HAS BROUGHT A DEGREE OF FURTHER TRANSPARENCY FOR THE CLIENT WHICH IS A POSITIVE IN TERMS OF THE SEPARATION OF RESEARCH COSTS. HOWEVER, RESEARCH PROVIDERS NEED TO WORK OUT HOW TO CLEARLY PRICE RESEARCH. THAT REMAINS A BIG ISSUE.”



“IT'S TOO EARLY TO TELL IF IT WAS WORTH IT. THERE IS QUITE A TIME LAG BETWEEN TRANSPARENCY AND THE IMPACT ON BEHAVIOURS SO I THINK TIME WILL TELL.”



Asset managers interviewed for this survey felt MiFID II to have been a huge but generally manageable change process.

The scale and technical demands were emphasised by all participants, with respondents pointing to the challenge of complex internal project management as well as significant dependence on third party suppliers. For global firms, ensuring consistency across their business internationally was a particular issue.

The separation of research payments from execution was recognised to be one of the most significant outcomes from MiFID II. Firms were generally cautiously positive, but emphasised considerable uncertainties relating to future pricing and availability of research for some parts of the market – eg. smaller companies. Again, the challenge of international consistency is evident (see Box 4).

For some participants, it was clearly still too early to make a judgement on the overall outcome for markets and customers.

#### **BOX 4: ASSET MANAGERS AFFECTED BY MIFID II RESEARCH RULES IN OVER A THIRD OF KEY NON-EU JURISDICTIONS**

MiFID II has had a significant impact on arrangements for the receipt and payment of research requiring the complete separation of payment for execution and research. This new regulation not only affects activities within the European Union (EU), but also situations in which managers have delegated asset management activities to jurisdictions outside of the EU. A Global Survey on Payment for Research published by the IA in March 2018 provided information on whether separate payment for research is permitted in a range of non-EU jurisdictions. The Survey was intended to assist firms to implement the new research requirements across their global operations which may cover multiple legal entities.

Of the 33 jurisdictions covered in the Survey:

- Two jurisdictions did not permit hard payment – this included Indonesia and the United States. The United States is included in this category as the Securities and Exchange Commission's no-action relief letter is a temporary measure.
- Eleven jurisdictions permitted separate hard payment under certain conditions – this included Hong Kong, China, Bermuda, India and Brazil, amongst others.
- Twenty jurisdictions permitted hard payment for research, including jurisdictions such as Japan, Canada and Singapore.



From a customer disclosure perspective, MiFID II, combined with PRIIPs, represents a paradigm shift for the asset and fund management industry. There are three particularly significant elements of this shift:

- The inclusion of all transaction costs incurred during the investment process, both explicit (brokerage, taxes) and implicit (seen in the difference between buy and sell prices in different markets as well as market impact).
- The aggregation of all costs (including product charges, transaction costs and distribution charges) into a single number accounting for overall economic experience of monies invested.
- The replacement of past performance in point of sale retail disclosure in the PRIIP Key Information Document with a range of (future) performance scenarios.

While the industry has been strongly supportive of the move towards enhanced transparency across all products and services, teething difficulties with MiFID and PRIIPs have been particularly evident in the area of transaction cost reporting and the construction of performance scenarios. Here, opinions were generally quite critical of the methodologies being deployed, with particular concern about the outcome being greater complexity and opacity, rather than simpler information on costs and performance. These areas have already been the subject of a call for evidence by the UK regulator, the Financial Conduct Authority (FCA).

“I WANT TRANSPARENCY OF WHAT IS GOING ON. A SINGLE FIGURE FOR THE COST OF DEALING IN SECURITIES THAT INCLUDES MARKET IMPACT IS CHALLENGING BECAUSE THERE IS NO SINGLE MEASURE OF MARKET IMPACT. IT IS MUCH BETTER TO ACTUALLY TELL PEOPLE ABOUT THE VOLUME OF TRANSACTIONS: IE. HOW MUCH DEALING DOES A FUND DO. DO YOU WANT A FUND THAT TURNS ITSELF OVER TEN TIMES OR A FUND THAT HOLDS LONG TERM AND WHERE TURNOVER IS VERY LOW. THAT IS USEFUL INFORMATION FOR THE INVESTORS.”



## UK CONTEXT

In the UK market specifically, the FCA has financial services competition powers that are concurrent with those of the wider competition regulator, the Competition and Markets Authority (CMA). These have been increasingly exercised in recent years and as at summer 2018, the UK asset management industry was the subject – directly and indirectly – of three studies:

- FCA Asset Management Market Study (AMMS), in implementation phase.
- FCA Investment Platforms Market Study (IPMS), in interim phase.
- CMA Investment Consultants Market Investigation (ICMI), in interim phase.

The themes raised by the FCA in the AMMS focus fundamentally on value delivery with the remedies falling broadly into the three categories outlined in Figure 10:

- **Alignment of interest.** Strengthened duties are being placed on Authorised Fund Managers (AFMs) to act in the best interest of investors, in particular through the use of a published value assessment by AFM Boards. This borrows elements from the 15(c) process and the US Gartenberg Principles for 1940 Act mutual funds.<sup>23</sup> There are also more specific requirements, notably on box profits and legacy share classes.
- **Transparency.** The FCA reinforces the MiFID requirements (see above) with a significant emphasis on greater granularity in the UK institutional market<sup>24</sup>. It also calls for greater industry focus on clarity of objectives, use of benchmarks, and reporting of performance. As part of this focus, the UK industry is undertaking an initiative on clearer use of language across all fund documentation.
- **Oversight.** As part of the new emphasis on alignment, AFM Boards will be required to have at least two independent directors (or a minimum of 25% of total Board). These independent directors will have commensurate responsibilities at Board level, including the new value assessment.

The interim findings of the FCA IPMS, published on 16 July 2018, raised a number of comparable themes, notably:

- Transparency and comparability of different forms of platform fee
- Clarity of objectives, benchmarks and risk in model portfolios sold on platforms
- Treatment of ‘Orphan clients’, where customers may be paying advisory fees on a services no longer provided.

The CMA Provisional Decision Report, published on 18 July 2018, noted a weak demand side, with trustees relying heavily on investment consultants but having limited ability to assess their services, relatively low levels of concentration in both investment consultancy and fiduciary management, barriers to expansion restricting new consultants developing their business and vertically integrated models creating conflicts of interest.<sup>25</sup>

<sup>23</sup> A long-established U.S. legal standard to determine whether a mutual fund adviser has breached its fiduciary duty under Section 36(b) of the Investment Company Act by allowing a fund to charge excessive fees.

<sup>24</sup> Asset Management Market Study Final Report, 1.26: Remedies which will drive competitive pressure on asset managers. June 2017.

<sup>25</sup> See Appendix Three

## STEWARDSHIP AND CORPORATE GOVERNANCE

Alongside the FCA Market Study, stewardship and corporate governance have continued to be key areas of UK policymaker and regulatory focus:

- **BEIS corporate governance reforms.** Through 2017, the Department for Business, Energy and Industrial Strategy (BEIS) completed an exercise designed to strengthen UK corporate governance and competitiveness, with three key themes: executive pay; employee and customer voice; and corporate governance in large private firms. As part of the BEIS package, the IA delivered a new public register on shareholder voting, aimed at increasing accountability and transparency of those listed companies that see significant shareholder dissent during the AGM season.
- **FCA supervisory focus.** In the spring of 2018, the FCA confirmed a new focus on stewardship as part of its supervisory activity. While this still remains to be defined in detail, it means the FCA now looks at asset managers through three lenses (role as good agents to their customers, good market participants and good stewards of investment).

With the intensifying focus on ESG, the stewardship and corporate governance themes are extending further in a number of ways. At Government level, the DWP has been consulting this year on new rules that will clarify and strengthen duties on pension scheme trustees to consider and report against ESG factors (to be mirrored by the FCA for Independent Governance Committees for workplace pension schemes).

## BROADER ECONOMIC CONTRIBUTION

The emphasis on stewardship and corporate governance links to changing expectations of the role that the UK industry plays in the domestic economy. Although this starts from a relatively low base, this is particularly seen in increasing activity in corporate funding through private markets, and infrastructure funding (see page 26). Some of the areas within the economy are not historically associated with asset management activity, eg. social housing (see page 23).

At the same time, both UK and international regulators continue to look at a range of themes linking to the wider stability of capital markets and the economy. Following the property fund suspensions in the aftermath of the Brexit referendum, the FCA initiated a policy discussion about the wider issues raised. Although the FCA focus was particularly on customer impacts, it noted the wider relevance to the global debate on risks to the financial system. Notably, IOSCO has been focusing more closely on liquidity mismatch and the use of leverage in open-ended funds as these two issues were identified, among others, by the Financial Stability Board as structural vulnerabilities arising from asset management activities. Alongside this, the Bank of England has also been pursuing a range of initiatives to look at the wider issue of system vulnerabilities.

# 3 TRENDS IN CLIENT ASSETS AND ALLOCATION

## KEY FINDINGS

### CLIENT TYPE

- » Almost four fifths of assets under management (79%) were managed on behalf of institutional investors.
- » Pension schemes remained the largest client type although for the first time in over five years pensions failed to increase as a proportion of total assets, remaining almost unchanged from 2016 at 44%.

### ASSET ALLOCATION

- » There was a small increase in equity allocation from 39% to 40% but the relatively strong returns seen in equity markets compared to other asset classes would actually suggest some outflows from the asset class. All other asset classes remained unchanged from 2016. The allocation to other assets remained stable at 21%.
- » Within equities the UK allocation continued to fall and now stands at 30% compared to 51% ten years ago.
- » A similar story was seen in the fixed income allocation, which saw the allocation to overseas bonds increase to 42%, up from 34% in 2011 when data were first collected.

### ACTIVE VS PASSIVE

- » Three quarters of assets are managed on an active basis, down from 83% a decade ago. There has been a gradual growth in the allocation to passive strategies strengthened by the increased use of ETFs, which has seen UK-listed ETFs increase from £11 billion at the end of 2008 to £250 billion in 2017.



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 actively or passively managed. 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 (see Box 5). The institutional and retail markets are covered separately and in more detail in Chapters 4 and 5 respectively.<sup>26</sup>

## CLIENT TYPES

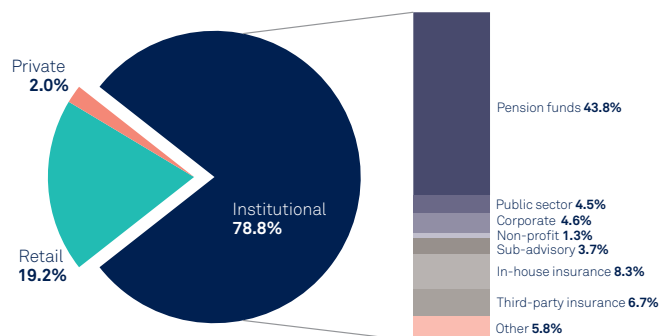
The £7.7 trillion of assets managed in the UK is managed for a broad range of client types. Chart 11 shows the breakdown by client type, reflecting assets managed in the UK for both institutional and retail clients. This includes assets from both domestic and overseas clients.

There was little change in the breakdown of assets under management by client type from last year. Once again, around four fifths of assets managed in the UK were managed on behalf of institutional investors (79%).

Pensions failed to increase as a proportion of clients overall for the first time in over five years. Interestingly, the proportion was almost unchanged from 2016 whilst the absolute value of assets increased from £3 trillion to £3.4 trillion. This would suggest that the slight fall in the relative value of pension assets (from 44% to 43.8%) reflected a difference in the growth rate of client types. The actual value of assets managed for all client types increased in 2017.

The definition of pension funds in the IA's data includes all schemes, both DB and 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 (see Box 5).

**CHART 11: ASSETS MANAGED IN THE UK BY CLIENT TYPE**



## BOX 5: 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 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

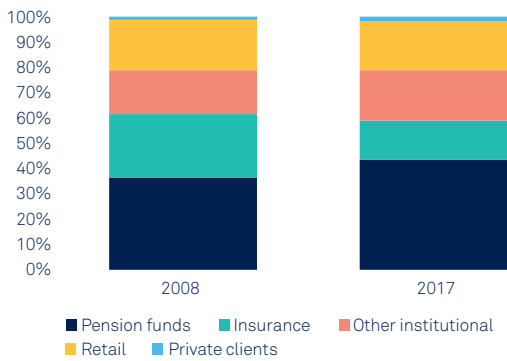
DC is something of a hybrid between retail and institutional. Pension savers in DC schemes receive an income in retirement that is based on the value of the pension pot they have accrued during their working life. Unlike a DB scheme, where their pension is based on their salary and is ultimately guaranteed 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.

<sup>26</sup> 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.

## LONGER-TERM EVOLUTION OF CLIENT BASE

Looking at the long term trends, there has been a sustained decline in insurance assets relative to pension funds and other institutional clients (Chart 12). The pace of this fall seems to be slowing, with the proportion of assets managed for insurance clients being almost exactly the same as last year.

**CHART 12: ASSETS MANAGED IN THE UK BY CLIENT TYPE (2008-2017)**



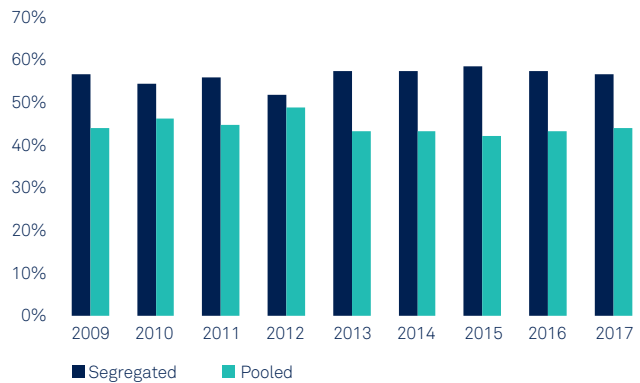
The general trend in recent years has been an increase in the proportion of pension fund assets. This is likely to be attributable to a continued focus on liability driven investment (LDI) by DB pension schemes looking to manage the run off of their liabilities, though this growth may be peaking as the level of hedging in place has now reached very high levels.<sup>27</sup> 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.

The private client figures included in Charts 11 and 12 only relate to the portion of the private client market where members of the IA provide dedicated private client investment services. As can be seen from Figure 3, the actual private client market is significantly larger than this and IA members are estimated to manage around one quarter of this market.

## SEGREGATED VS POOLED INVESTMENT

Chart 13 shows the ratio of segregated to pooled assets has remained relatively stable since 2013. In 2017, 56% of assets were managed on a segregated basis. Segregated mandates remain heavily used in the traditional institutional market although there has clearly been a significant evolution in the pooled fund universe in recent years with the rise of ETFs alongside more established indexing vehicles such as investment funds and life funds (see page 52).

**CHART 13: SEGREGATED VERSUS POOLED INVESTMENT (2009-2017)**



<sup>27</sup> The Age of Peak LDI, Hymans Roberts, Nomura, April 2018

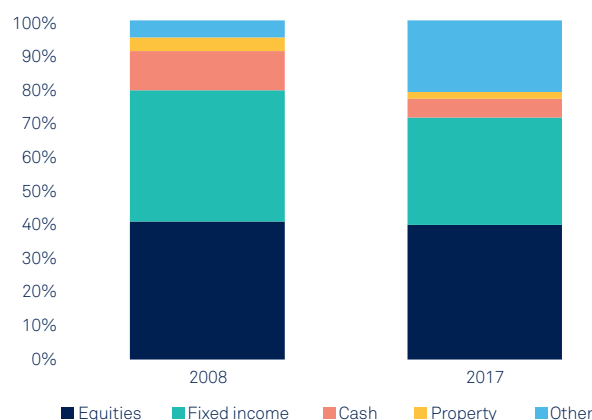
## ASSET ALLOCATION

Equity markets posted strong positive returns during 2017.<sup>28</sup> All else being equal, investment returns would have led the proportion of equities to increase during 2017 and fixed income to decrease. Despite this, there was only a very small increase in equity allocations from 39% to 40%, suggesting that there were some further flows out of equities during the year. This is not consistent with the inflows of £9 billion observed into equity retail funds during 2017 (see page 71), suggesting this is continued institutional market de-risking.<sup>29</sup>

Allocation to all other asset classes remained almost unchanged year on year. For the first time in several years the allocation to other assets remained stable at 21% but given the broad range of investment in this category, it is not possible to infer whether this is a result of slowing allocations or market movements (see Chart 14).

Nevertheless it is clear that over the last decade there has been a shift towards other assets, which include more solutions-focused strategies (such as liability-driven investment) and alternative asset classes (such as infrastructure and direct lending). In the institutional market this shift has been fuelled by interest from DB pension schemes and insurers in investments that offer ways to more closely match their liabilities and cash flow needs.

**CHART 14: OVERALL ASSET ALLOCATION OF UK-MANAGED ASSETS (2008-2017)**



**TABLE 1: PROPORTION OF IA MEMBERS INVESTING BY ASSET CLASS**

	Percentage of firms
Equities	96%
Fixed income	84%
Cash	71%
Property	47%
Other	65%

<sup>28</sup> Most major equity markets posted at or near double digit returns in sterling terms during 2017, compared to near neutral returns on global bonds in sterling terms.

<sup>29</sup> Net retail sales of Equity Growth funds were £10 billion. There was an outflow of £0.8 billion from Equity Income funds

## DETAILED ASSET ALLOCATION

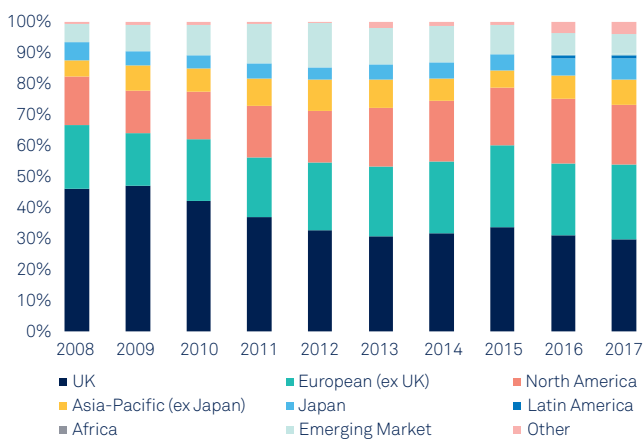
Beyond the shifts between asset classes, the IA also monitors the trends within equity and fixed income allocations according to type of exposure and this section considers these changes in more detail.

### EQUITY BY REGION

Chart 15 shows equity allocations on a regional basis. The most striking feature remains the falling allocation to UK equities relative to overseas. This now stands at 30% compared to 70% in overseas equities which is a significant change from a decade ago where the allocation stood at 51% versus 49%. Notably, this decline in UK equity allocation is driven by trends in both the institutional and retail market (see page 63 and page 68). Particularly within the former, a key driver has been the de-risking within DB pension schemes (see page 61 and Chart 26).

Within the last year there was also a slight increase in Europe ex-UK to 24% as well as a slight decrease in the allocation to North America to 19% from 21% in 2016.

**CHART 15: UK-MANAGED EQUITIES BY REGION (2008-2017)<sup>30</sup>**



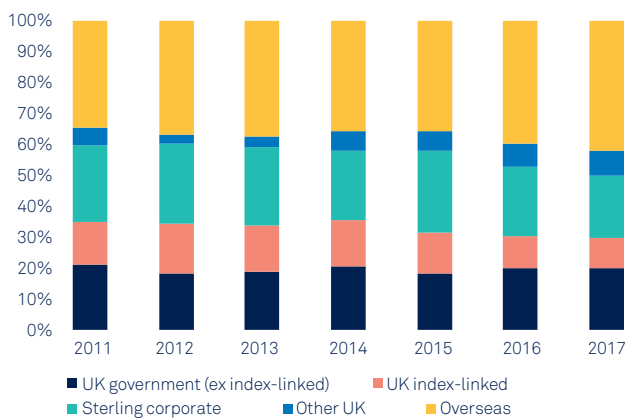
<sup>30</sup> The IA is now collecting more granular data on the allocation to Latin America and Africa, and these are detailed separately from 2016 in Chart 15. Although these allocations are small it should be noted that comparisons to the 'Other' country segment will not be directly comparable with previous years.

### FIXED INCOME BY REGION

Within fixed income, the allocation to overseas bonds continued to increase, largely at the expense of UK corporate bonds (see Chart 16):

- Overseas fixed income finished the year up two percentage points at 42%.
- Sterling corporate bonds fell three percentage points to 20%.

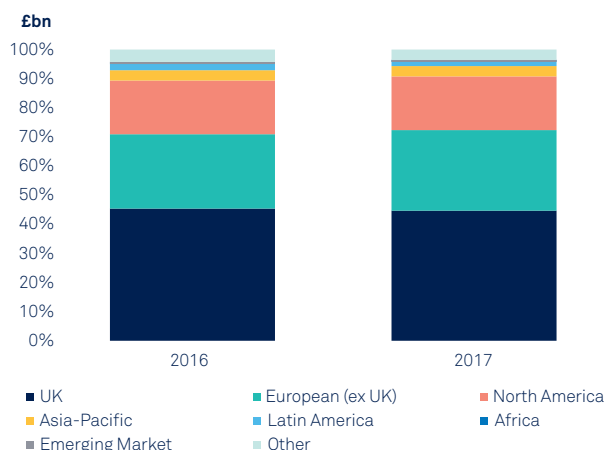
**CHART 16: ALLOCATION OF UK-MANAGED FIXED INCOME BY TYPE AND REGION (2011-2017)**





Within sterling corporate bonds there does not appear to have been any shift towards overseas issuers. The breakdown by issuer country remained almost unchanged from 2016. Bonds issued by UK companies represented 45% of all sterling corporate bonds compared to 46% in 2016 (see Chart 17).

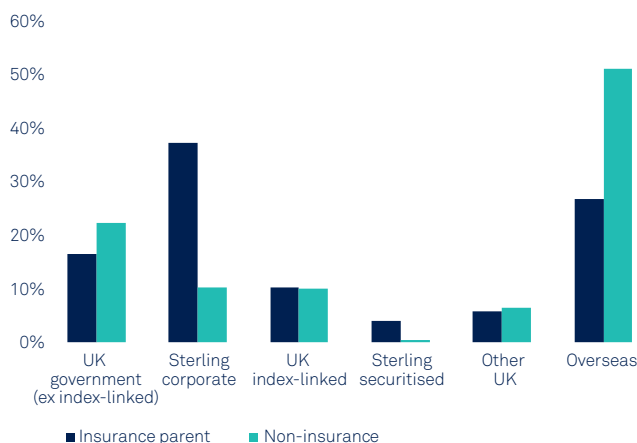
**CHART 17: CORPORATE BOND ALLOCATION BY COUNTRY OF ISSUER (2016-2017)<sup>31</sup>**



**FIXED INCOME BY CLIENT TYPE**

Fixed income allocations differ depending on the category of the underlying client. Insurance companies, for example, have very specific requirements, partly driven by the nature of their product set (ie. annuities, protection such as life insurance) and partly driven by prudential regulation. If we look at how the allocation alters depending on whether the asset manager has an insurance parent or not (see Chart 18) that difference becomes very clear. Insurance-owned groups have a much higher exposure to sterling corporate securities and, a lower exposure to overseas bonds.

**CHART 18: FIXED INCOME OWNERSHIP BY PARENT GROUP (INSURANCE VS. NON-INSURANCE)**

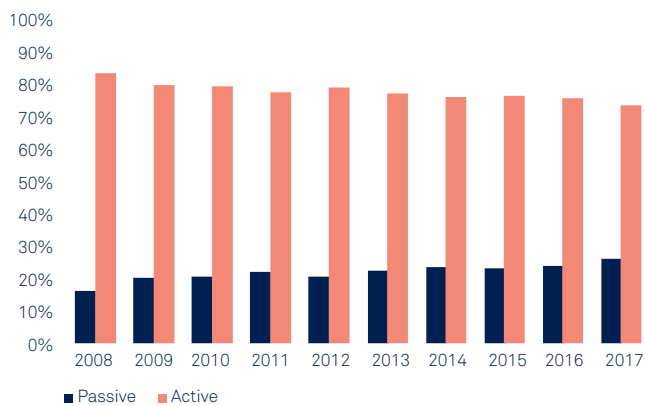


<sup>31</sup> Data collected since 2016

## BALANCE BETWEEN ACTIVE AND PASSIVE

Across the overall base of UK-managed assets, almost three quarters of assets are still actively managed (74%). This is down from 83% a decade ago (see Chart 19).

**CHART 19: ACTIVE AND PASSIVE AS PROPORTION OF TOTAL UK ASSETS UNDER MANAGEMENT (2008-2017)**



The split between active and passive at this macro level reflects a number of factors. First and foremost, it may relate to greater use of either active or passive investment strategies within each asset class, for example, there could be increasing demand for passive products to achieve equity market exposure. Second, but equally important, it may reflect changes in the allocation between asset classes where more money is allocated to strategies that involve by nature more active management, such as multi-asset or outcome-focused.

The trends we observe in Chart 19 above reflect both factors. On the one hand, there has been increasing demand for passive products particularly within equity. For example, Chapter 5 discusses how passive equity FUM have increased by more than 700% since 2008 (see page 67). This would support the upward trend of passive assets under management. On the other hand, this Chapter reports on how the 'other' category

has been on the rise given the continued demand for solutions-based investment strategies (see page 47). This would account for what appears to be only a gradual rate of increase in the proportion of passive assets in Chart 19.

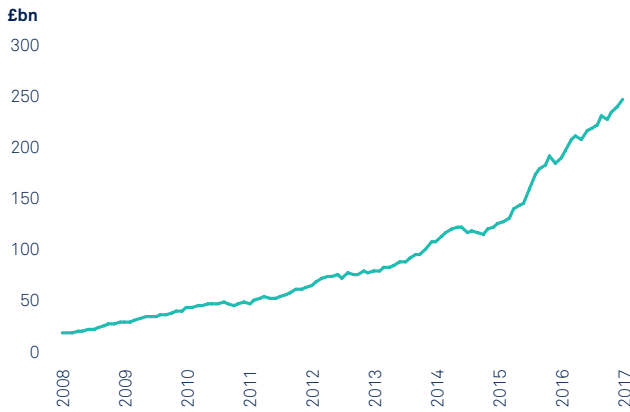
A way to distinguish between the two factors would be to look at the trends in use of passive strategies where these are mostly relevant, which is more the case for equity and fixed income rather than multi-asset and outcome oriented products. In 2017 the IA began to collect the active/passive split separately for equities and fixed income. Passive management was more prevalent among equities than fixed income. More than half of equities were being managed on a passive basis (53%) compared to just over one third of fixed income (34%).

Another way of looking at the long-term trend is therefore to adjust for the wider asset allocation / strategy shifts, and examine the amount of assets managed on a passive basis only as a proportion of total equity and fixed income assets, since these are the asset classes most likely to be passively managed. Doing this indicates that passive is increasing at a slightly faster rate than is indicated in Chart 19, and that passive assets account for more than one third of the total equity and fixed income allocation (36%).

The growth of ETFs in the UK will also influence the prevalence of passive assets. 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.

UK-listed ETFs have increased in value from £11 billion at the end of 2008 to £250 billion in 2017 (see Chart 20). Most of this is managed in the UK by IA members, who report that almost all assets they manage in ETFs are managed on a passive basis. Chart 19 has also been adjusted using data collected in 2017 to reflect those ETFs listed in the UK that are not included in data reported to the IA by its membership as part of this Survey.

**CHART 20: ASSETS MANAGED IN UK LISTED ETFs (2008-2017)**



Source: Morningstar

Data from the IA's monthly fund statistics shows an incomplete picture of the use of passive strategies, capturing conventional investment funds but not ETFs.<sup>32</sup> The proportion of funds under management in passive strategies stood at 13.5% at the end of 2017, a slight increase from 2016 but still more than double what it was in 2008. At the same time, gross retail flows into equity tracker funds have decreased as a proportion of overall sales over the last three years (see Chart 67), suggesting that new money into funds is more likely to be directed towards actively managed strategies than passive ones.

As ETF data is currently not included in IA monthly fund statistics, a proportion of retail investment activity may not be captured within this analysis. That being said, it would seem that the majority of ETFs still lies with the institutional market in the UK. Indeed, it was recently reported that only 10 to 15% of total ETF assets in Europe are held by retail investors.<sup>33</sup> Further detail on the ETF market is available in Box 7.

“ETFs ARE STILL IN THE EARLY STAGES IN EUROPE BUT WITH THE GROWTH OF FEE-BASED ADVISORY, ETFs ARE INCREASINGLY BEING USED BY WEALTH MANAGERS. IN ADDITION INSTITUTIONS ARE USING ETFs TO ALTER THEIR MARKET EXPOSURE, TO FIND LIQUID VEHICLES TO ACCESS LESS LIQUID ASSETS AND USING THEM AS DERIVATIVES. SO WE SEE THE AMOUNT WE MANAGE IN ETFs INCREASING SIGNIFICANTLY IN THE NEXT FIVE YEARS.”



<sup>32</sup> IA monthly data on UK funds does not include investment in exchange traded funds.

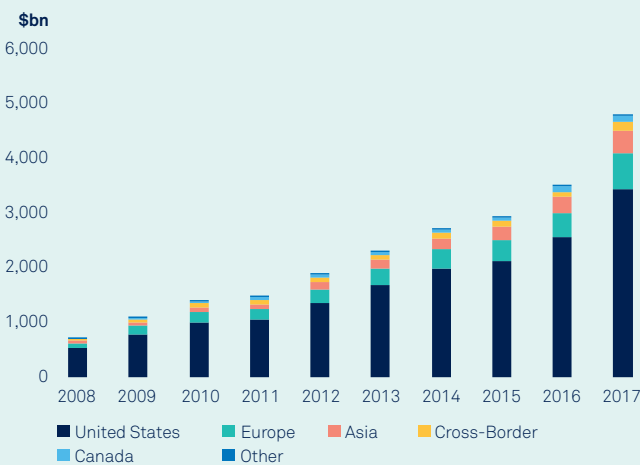
<sup>33</sup> European Commission, Distribution systems of retail investment products across the European Union, April 2018.

## BOX 7: THE ETF MARKET

ETFs have become a significant investment vehicle in the global market. In the ten years to the end of 2017, global ETF assets under management have grown almost six-fold from \$714 billion to \$4.8 trillion.

Chart 21 shows the majority of assets reside in the United States, \$3.4 trillion in 2017. European-domiciled ETFs stood at \$634 billion and Asian domiciled ETFs had assets under management of \$411 billion. Canada is the largest single country of domicile outside of the United States with \$117 billion held in ETFs.

**CHART 21: ETF ASSETS UNDER MANAGEMENT BY REGION OF DOMICILE**



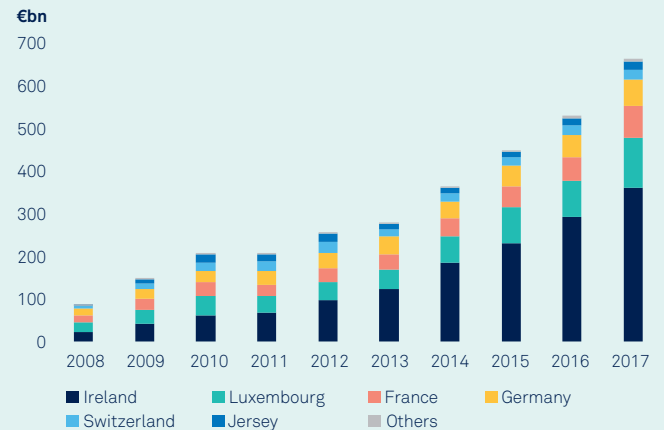
Source: Morningstar

## ETFs IN THE UK

It is not possible to isolate the UK market for ETFs as it is for UK authorised and recognised funds – by domicile or by investor location. There are only eight Exchange Traded Products (ETPs) domiciled in the UK, but more than 800 listed on UK exchanges. An ETF’s domicile does not determine where it is bought and sold as investors from around the world can access UK equity markets. The location of the investor is therefore unknown and it cannot be assumed that an ETF bought in the UK has been bought by a UK investor

Chart 22 shows where ETFs in Europe are domiciled. Ireland clearly dominates with 55% share (€362 billion) of European ETF assets. Ireland is a popular domicile for ETF issuers due to its regulatory practice, availability of expertise and well developed ETF ecosystem.

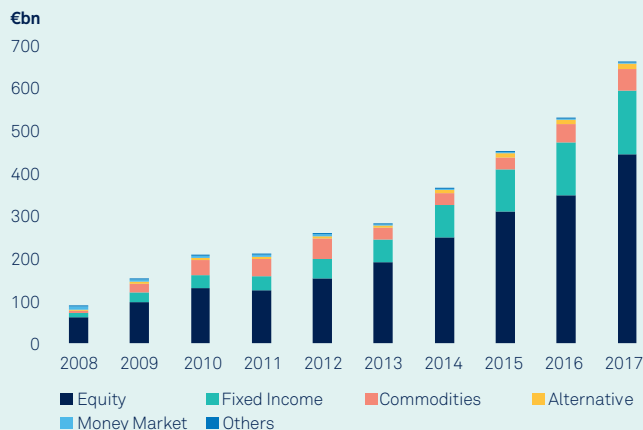
**CHART 22: EUROPEAN ETFs BY COUNTRY OF DOMICILE**



Source: Morningstar

Chart 23 shows the growth in European ETF assets under management broken down by asset class. Equity ETFs represent about two thirds of the market with €444 billion invested at the end of 2017, while fixed income ETFs follow with €151 billion under management.

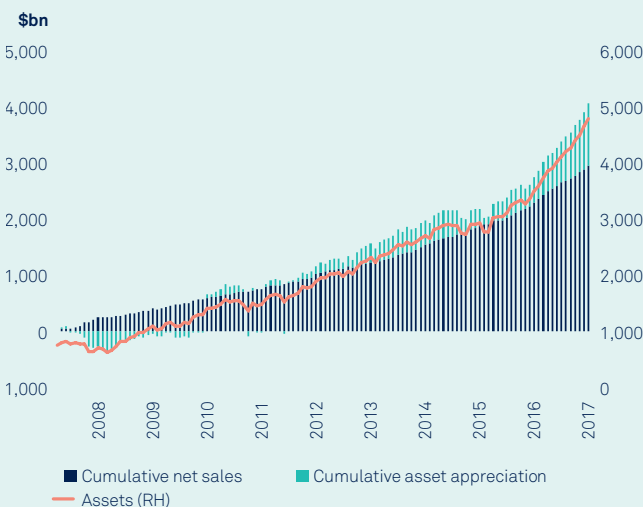
**CHART 23: EUROPEAN DOMICILED ETFs BY ASSET CLASS**



Source: Morningstar

Chart 24 shows the growth in global ETF assets under management broken down into sales and asset appreciation. Sales make up the dominant part of the growth in ETFs in contrast to traditional funds (see page 68). This may reflect the smaller asset base of the ETF universe. At the end of 2017, sales accounted for 62% of AUM growth within the ETF universe compared to 40% for funds.

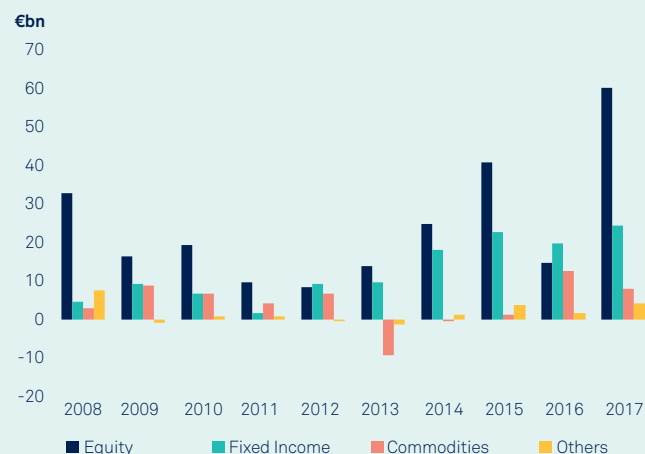
**CHART 24: ETF CONTRIBUTION TO ASSET GROWTH**



Source: Morningstar

Total net sales into European ETFs were €100 billion in 2017, €60 billion of which went into equity ETFs.<sup>34</sup> Fixed income ETFs gathered €24.4 billion in new investor money through the year and commodity ETFs took in €7.6 billion. It should be noted that this data relates to primary market transactions and reflects the growth in the ETF universe, it does not factor in secondary market transactions.

**CHART 25: ETF NET SALES BY ASSET CLASS**



Source: Morningstar

<sup>34</sup> Not comparable to sales data in the UK Funds chapter of this report as ETF sales cannot be differentiated between retail and institutional.

# 4 UK INSTITUTIONAL CLIENT MARKET

## KEY FINDINGS

### MARKET OVERVIEW

- » IA members manage £3.8 trillion for UK institutional clients in offices around the globe. Pension funds are the largest client type, with 63% of institutional AUM, followed by insurance companies at 25%.

### PENSIONS

- » £2.4 trillion is managed for UK pension schemes by IA members, representing 63% of the market.
- » Automatic enrolment has been a success with over nine million people enrolled into pension schemes as a result. In order to ensure that this new generation of pension savers achieves good outcomes there will need to be:
  - More emphasis on the importance of the investment process in generating returns for DC default funds
  - Greater facilitation of efficient asset allocation in default investment strategies
  - Increased contributions and engagement

### THIRD PARTY MARKET

- » Once in-house mandates are excluded from the institutional data, assets under management reduce to £3.1 trillion.
- » Pension funds are even more dominant in the third party market, accounting for 71% of third party assets.
- » Assets managed in liability-driven investment strategies broke through £1 trillion for the first time in 2017, with an estimated £1.1 trillion of institutional assets managed in LDI strategies.

### MANDATE TYPES

- » Multi-asset, or 'balanced' mandates, now account for about a quarter of total mandates once LDI mandates are excluded. Single-asset mandates account for the remaining three quarters.
- » The breakdown of specialist mandates has been relatively unchanged from 2016. Global equity mandates increased to 50% (up from 45%) and specialist UK mandates dropped slightly to 23%.
- » Global bonds overtook sterling corporate bond mandates for the first time, increasing to 29% of all specialist mandates.
- » 66% of assets were managed actively. All institutional client types were more likely to be managed on an active than a passive basis.
- » Almost two thirds of third party institutional mandates were managed in segregated mandates (65%). The increase in segregated mandates observed over the last couple of years appears to have stabilised.



This Chapter examines more closely the shape of the UK institutional client market and reports on specific aspects including the different client types and their relative importance, the size of the third party mandate market and the long-term trends in mandate types, as well as the developments in the pensions market and particularly the shift from DB to DC.

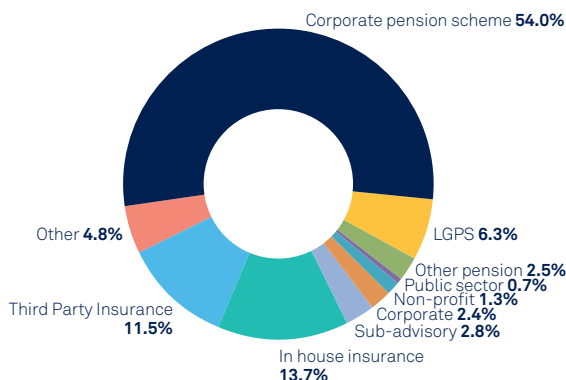
The analysis differs from that in Chapters 1 and 2 in two ways:

- It focuses on the nature of a mandate rather than on the underlying assets. So a global equity mandate will appear as such, rather than being broken down into the underlying constituent countries.
- It looks at the UK institutional client market regardless of asset management location (ie. the focus is on clients based in the UK rather than on assets managed in the UK). However, we estimate that an overwhelming majority of the assets are managed in the UK (approximately 93%).

## CLIENT BREAKDOWN

IA members manage £3.8 trillion for UK institutional clients globally.<sup>35</sup> As Chart 26 indicates, pension funds and insurance companies (including in-house and third party management) account for the majority of UK institutional assets (88%)<sup>36</sup>, with pension funds remaining the largest client type.

**CHART 26: UK INSTITUTIONAL MARKET BY CLIENT TYPE**



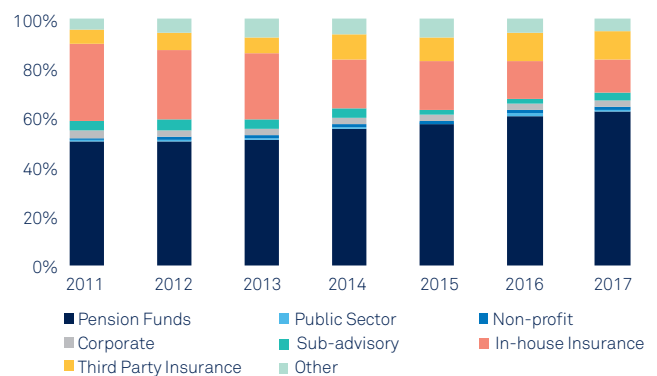
<sup>35</sup> Implied figure based on data collected on an estimated 84% of the institutional client base.

<sup>36</sup> The remaining 12% of assets is made up from mandates managed for corporations (outside of pension assets) sub advisory, not for profit mandates and public sector mandates. 'Other' client types generally refers to a variety of open-and closed-ended pooled vehicles, and investors from the more specialist areas of private equity, venture capital and property.

Since the IA began monitoring the breakdown of the institutional client base in the UK, there has been a marked increase in the proportion of assets managed for pension funds and a decrease in insurance assets, most notably in-house insurance.

DC pension assets operated via an intermediary platform through an insurance company are reflected in the IA's insurance assets. Consequently this shift in assets towards pension funds is even stronger than is implied in Chart 27.

**CHART 27: UK INSTITUTIONAL MARKET BY CLIENT TYPE (2011-2017)**



## PENSION SCHEMES

In 2017, pension funds continued to account for the majority of the institutional client base (£2.4 trillion).

The IA divides pension scheme assets in three categories:

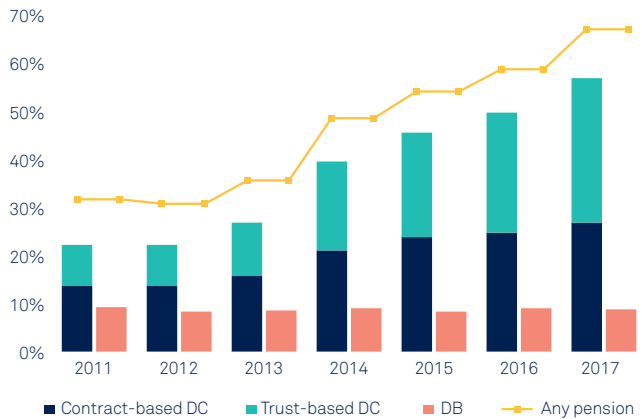
- Corporate pension funds, which at £2.1 trillion represented the majority of UK pension fund assets in 2017. This category includes a number of in-house Occupational Pensions Scheme (OPS) managers, which manage an estimated £170 billion in assets.
- The Local Government Pension Scheme (LGPS) which accounted for £240 billion of assets in 2017, indicating that IA members manage around 92% of LGPS assets.
- Assets managed for pension schemes that do not fit into either of these categories, such as those run for not-for-profit organisations, representing £95 billion.

## THE SHAPE OF THE UK PENSION MARKET

The IA estimates the size of the UK pension market to be £3 trillion at the end of December 2017.<sup>38</sup> This includes all assets in DB and DC pensions, as well as those assets in some form of drawdown arrangement, plus assets backing annuities.<sup>39</sup> Figure 11 provides an estimate of how these assets are broken down across the different scheme types.

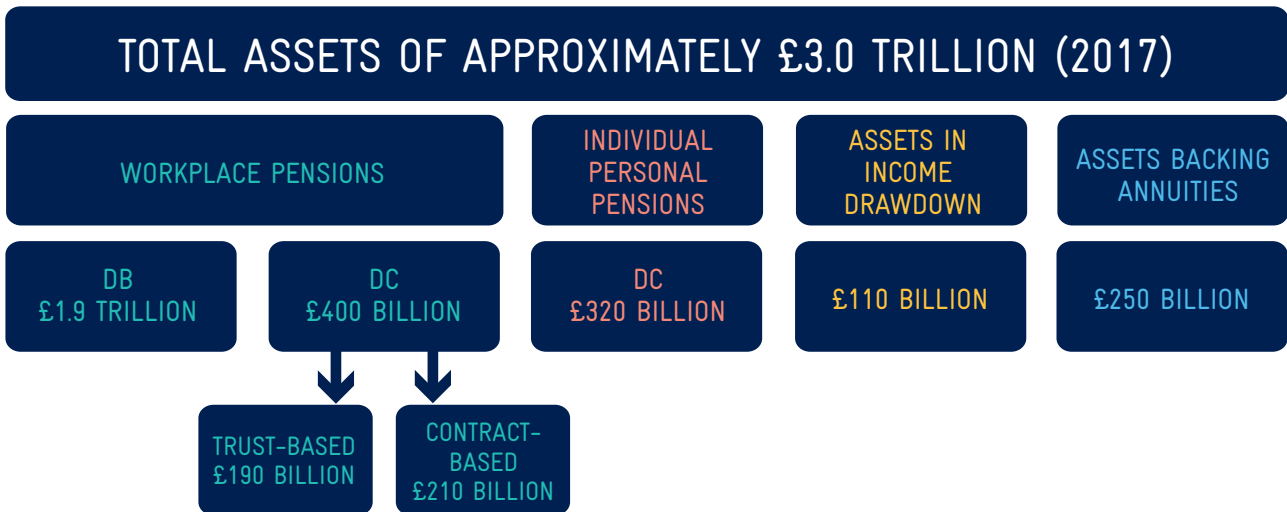
DB (funded) assets continue to make up the majority of the UK pension market, at £1.9 trillion in assets at the end of December 2017.<sup>37</sup> However, the number of savers into DC schemes now exceeds those actively saving into DB schemes. This shift is largely a result of the introduction of automatic enrolment. The majority of DB schemes that remain open to new members are linked to jobs in the public sector. Therefore when only private sector pension saving is taken into account the shift from DB to DC is even more stark (see Chart 28).

**CHART 28: PENSION PARTICIPATION FOR PRIVATE SECTOR JOBS (2011-2017)**



Source: ONS

**FIGURE 11: OVERVIEW OF THE UK'S PENSION LANDSCAPE<sup>40</sup>**



<sup>37</sup> This figure is not directly comparable to the £2.1 trillion managed for corporate pensions by IA members as some DB assets will be managed by non-IA members and some DC pension assets will be directly managed by IA members. Also IA DB figures include LDI data on the basis of liabilities hedged which is likely to be higher than asset value.

<sup>38</sup> Significant progress has been made in the last two years and the data below has been collected and inferred from a number of sources. External sources include ONS, Pensions Policy Institute, PPF and TPR. Nevertheless this data should still be considered indicative as not all data are updated with the same frequency or at the same date. Where possible estimates have been made to equalise the data at the end of 2016. Data on the DC market sourced from a number of sources at different dates. Numbers have been estimated so they are comparable at end December 2017 using returns on the IAs mixed investment 40-85% shares sector, a proxy for a typical DC default investment.

<sup>39</sup> The assets of DB schemes are reported in Figure 11. The liabilities attributed to these schemes would result in higher figures as funding levels currently average around 85%.

<sup>40</sup> Source: ONS, FCA, PPI, IA, DCLG



## BOX 6: PUTTING INVESTMENT AT THE HEART OF DC PENSIONS

Since 2012 automatic enrolment has brought over nine million new people into pension saving. A combination of adequate contributions and long-term returns will now be needed to facilitate good retirement outcomes. The IA has proposed a number of key areas where there is scope for pension schemes and the investment industry to collaborate to improve member outcomes.<sup>41</sup>

### MAKING INVESTMENT COUNT

- Investment should have the same priority in all forms of pension, whether DB, DC or Collective Defined Contribution (CDC).
- An emphasis on the investment process in DC scheme design, selection, governance and value assessment will facilitate better long-term member outcomes. At the heart of this are clear member objectives for the default arrangement.
- Transparency of investment costs for decision-makers in bundled workplace DC schemes should extend to separating the investment component from other costs. This will help to enhance the value assessment process for investment.
- Responsibility and sustainability in the investment process are increasingly important themes. The IA and the investment management industry are working to build on existing frameworks to support customers going forward.

### FACILITATING EFFICIENT ASSET ALLOCATION

- In relying on diversified market returns, DC schemes are inherently no different to DB schemes (or any other institutional investors), either in their needs, or in the economic function of the capital that schemes put to work on behalf of savers.

- The question as to what are the barriers DC schemes face in relation to investing in illiquid assets has been widely asked in recent years. We conclude that a range of supply and demand side changes could facilitate a different approach to investment by DC schemes, making it more straightforward to access opportunities such as infrastructure.
- Demand side behaviour could be supported by further regulatory guidance on investment design for default arrangements. There is also scope to explore whether a new fund vehicle could better facilitate access to less liquid asset classes.

### INCREASING CONTRIBUTIONS AND ENGAGEMENT

- The risk of inadequate contributions relative to anticipated outcome is high in the current DC environment. The IA supports automatic escalation to facilitate higher contribution rates.
- Inertia-based tools are not enough on their own. Real engagement is necessary, and could be facilitated by the further development of decision-making tools that draw on behavioural insights and harness technological innovation.
- Engagement also depends on confidence. One important element here will be clearer and consistent communication. This will require a combination of changes. Some are pension specific such as moving away from the term 'default'. Others relate more to the nature of investment management.

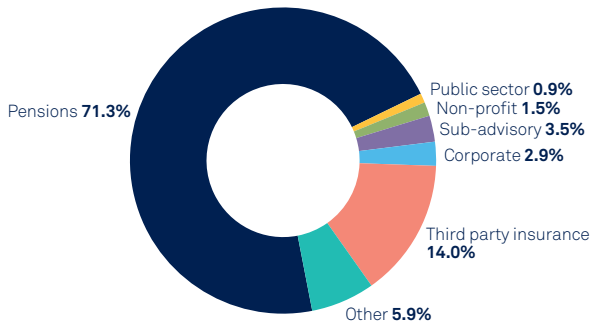
<sup>41</sup> Putting Investment at the Heart of DC Pensions, IA position paper, 2018.

## TRENDS IN THE THIRD PARTY INSTITUTIONAL MARKET

Full details of the asset allocation and investment strategy for the entire institutional market are available in Appendix Two. The remainder of this chapter looks more closely at IA data from the institutional market that is available to third parties (excluding mandates managed in-house by insurance parent groups and occupational pension schemes).

Once in-house mandates are excluded from the institutional data, assets under management reduce to £3.1 trillion. Pension funds become even more dominant (see Chart 29), representing 71% of third party assets, with the remaining insurance assets representing only 14% of the market.

**CHART 29: UK INSTITUTIONAL CLIENT MARKET BY CLIENT TYPE**

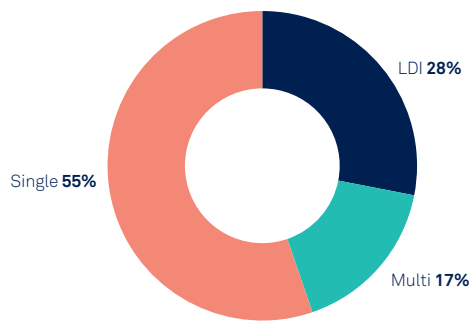


## MANDATE BREAKDOWN

Chart 30 breaks the institutional market down into three categories of mandate:

- Single-asset, or ‘specialist’ mandates, which focus on a specific asset class or geographical region. Specialist mandates remain the most popular form of investment among institutional investors, with more than half of assets managed on this basis.
- Multi-asset, or ‘balanced’ mandates, which would cover a number of asset classes and regions. These account for 17% of total mandates. Stripping out the LDI mandates below, the balance between specialist and multi-asset is 76% single asset versus 24% multi-asset.
- LDI mandates, which are specifically designed to help clients meet future liabilities. These mandates frequently make greater use of derivative instruments. They are therefore included on the basis of the notional value of liabilities hedged, rather than the value of physical assets held in the portfolio. An estimated £1.1 trillion is now being hedged in LDI mandates.

**CHART 30: UK INSTITUTIONAL MANDATES INCLUDING LDI**

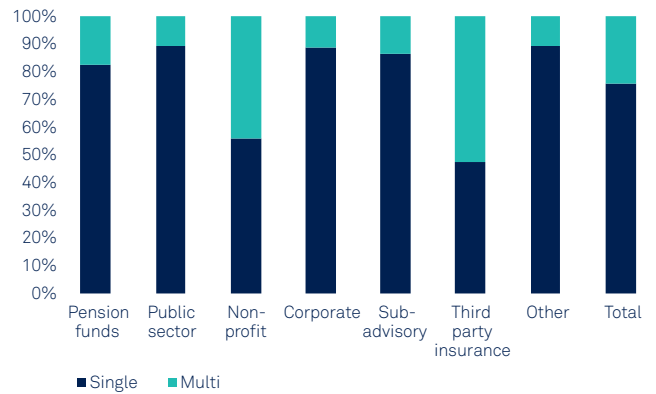


Although DB pension schemes remain a significant proportion of the institutional market, the fact that they have very specific requirements means that their LDI allocations can mask trends that might otherwise be observed in the market. For that reason we exclude the value of LDI mandates from the asset allocation analysis on pages 60 to 65 and focus purely on whether clients are favouring multi-asset or specialist solutions other than explicit liability management.

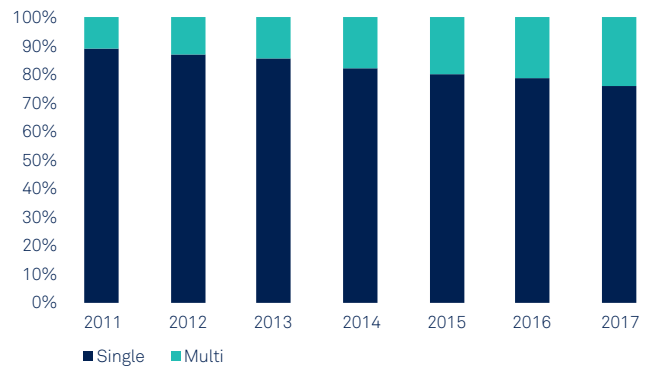
Chart 31 indicates that the preference for specialist mandates remains high, with 76% of assets being invested in this way, although Chart 32 shows that this figure has gradually reduced in recent years.

24% of third party institutional assets are allocated to multi-asset mandates, up from 21% in 2016, which seems consistent with the use of multi-asset funds in DC default strategies and the increase of assets primarily due to automatic enrolment.<sup>42</sup> Contribution rates in this space began to escalate in 2018. The extent to which employees will continue contributing higher rates or decide to opt out of their schemes possibly due to lack of affordability, will be a key determinant of whether this trend continues in coming years.<sup>43</sup>

**CHART 31: UK INSTITUTIONAL CLIENT MANDATES: MULTI-ASSET VS. SPECIALIST**



**CHART 32: UK INSTITUTIONAL CLIENT MANDATES: MULTI-ASSET VS. SPECIALIST (2011-2017)**



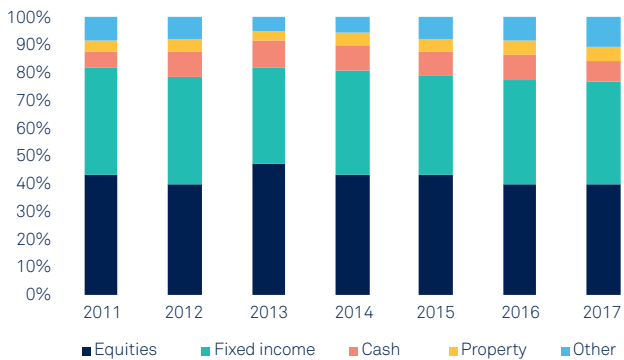
<sup>42</sup> Excludes any assets managed in-house by occupational pension schemes or insurance companies

<sup>43</sup> Increases in minimum contribution rates for automatic enrolment pensions, TPR

## INVESTMENT TRENDS WITHIN SPECIALIST MANDATES

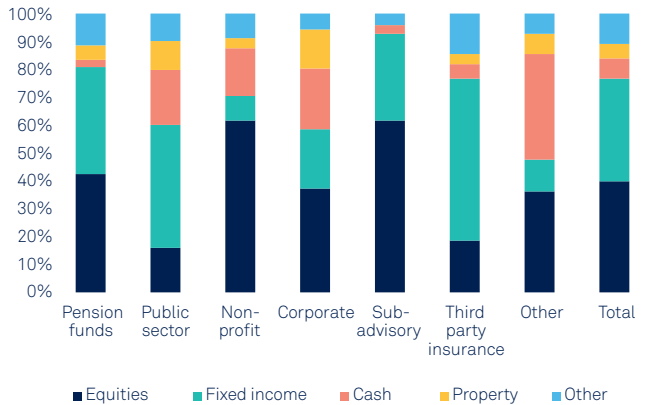
Equity remained the most popular type of specialist mandate with the proportion staying unchanged at 40%. There was generally little change apart from a decrease in the cash allocation and a corresponding increase in other assets. Chart 33 shows the progression since 2011 and there is no clear trend outside the increase in other assets particularly in the last five years, which is consistent with the growth of private assets.

**CHART 33: SPECIALIST MANDATE BREAKDOWN BY ASSET CLASS (2011-2017)**



Different types of institutional client have very distinct requirements and the headline split between single asset classes masks a wide variation in the type of mandate required by each client type. Insurance companies for example have particularly high allocations to fixed income mandates. Pension funds also have higher than average fixed income allocations, led by particularly high allocations among corporate pension schemes (see Chart 34).

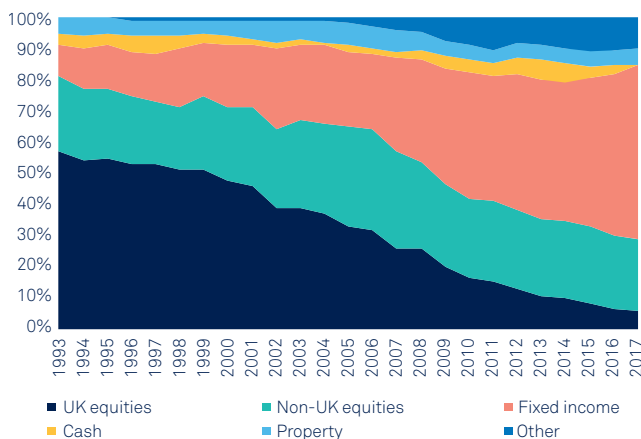
**CHART 34: SPECIALIST MANDATE BREAKDOWN BY ASSET CLASS**



As is evident from the increase in assets managed according to LDI strategies, many DB schemes are moving away from using traditional scheme-specific asset allocation benchmarks and are now closer to those that match their assets to their liabilities and manage their deficit volatility.

Chart 35 shows what this has meant for the change in asset allocation of DB pension scheme in the UK over the last 20 years. In the early 1990s, a typical DB scheme would have been heavily invested in equities (>80%), and particularly domestic equities, with a small allocation to fixed income assets and other asset types, notably property. The growing maturity of DB scheme membership has increased scheme appetite to hold assets that behave in a similar way to liabilities and led to the evolution of their investment strategies. So a typical DB scheme is now likely to hold a much smaller proportion in equities, which itself includes more overseas than domestic equities, and a considerably larger allocation in fixed income assets, and have a significant exposure to alternatives (10% compared to 1% in the mid-1990s).

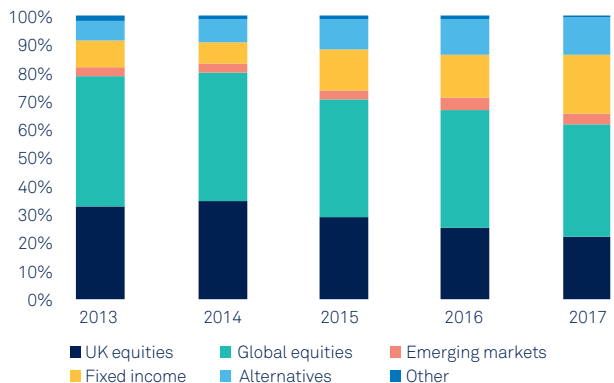
**CHART 35: UK DB PENSION FUND ASSET ALLOCATION (1993-2017)**



Source: UBS/PPF

In contrast to DB schemes, the asset allocation of DC schemes shows a much higher allocation to equities. Although the proportion allocated to equities, and particularly domestic equities, among DC schemes is also following a downward trend, it is still at approximately two thirds of assets (see Chart 36).

**CHART 36: DC ASSET ALLOCATION, SELECTED FTSE 100 / FTSE 250 PENSION SCHEMES**

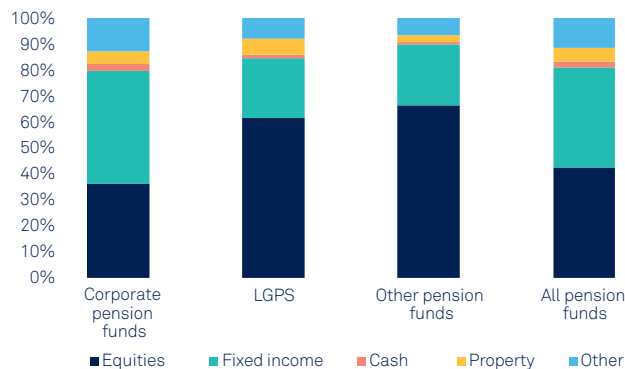


Source: FTSE Default DC Schemes Report 2017, Schroders

This in large part reflects the difference in demographic between the membership of DC and DB schemes. As occupational DB schemes are now almost entirely closed to new entrants and moving to being cashflow negative, DC schemes are likely to have a much higher proportion of younger members, with a far longer-term investment horizon than that of the more mature DB schemes. This means they are able to have an increased allocation to riskier asset classes rather than asset classes targeting either a regular income stream or an inflation protected return. Nevertheless, longer term as DC schemes mature, there is no reason why the DC market should not be characterised by the same degree of sophistication of discussion around the role of different asset classes and the investment process that characterises DB delivery.<sup>44</sup>

Chart 37 shows the change in asset allocation of pension schemes in aggregate. There is a wide variation depending on the type of pension scheme in question. This year's data is consistent with the findings of previous years, the key amongst these being that the LGPS has a higher allocation to equities than corporate pension schemes (62% vs 36%). As with DC schemes, the LGPS has a rather different membership makeup than other DB schemes. Scheme membership is comparatively less mature than closed corporate DB schemes and the LGPS funds function within a different regulatory framework to corporate schemes and are thus subject to less pressure to implement de-risking investment strategies. Consequently, they can maintain a higher allocation to return-seeking strategies.

**CHART 37: SPECIALIST MANDATE BREAKDOWN BY ASSET CLASS AMONG UK PENSION FUNDS**

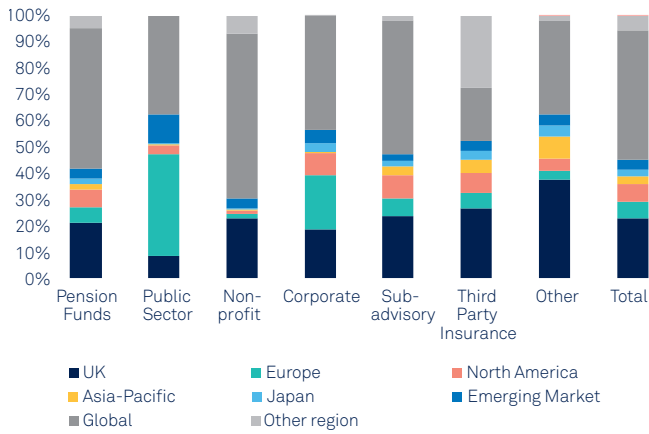


<sup>44</sup> Putting investment at the heart of DC pensions – IA position paper, June 2018

## GEOGRAPHIC ALLOCATION

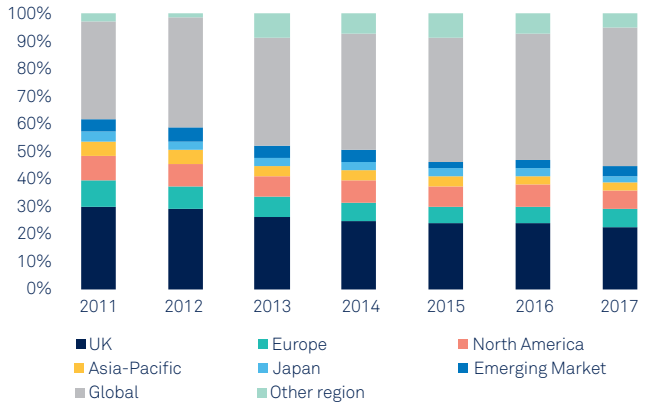
Chart 38 shows the breakdown of specialist mandates in 2017. There was very little change in the overall allocation from 2016.

**CHART 38: GEOGRAPHICAL EQUITY ALLOCATION OF SPECIALIST MANDATES BY CLIENT TYPE**



Overall the globalisation of investment in the institutional market remains a key theme as more than three quarters of specialist equity mandates apply to non-UK mandates. Chart 39 shows that global equity mandates increased to 50% of all specialist mandates at the end of 2017, while specialist UK mandates fell another percentage point ending the year at 23%.

**CHART 39: GEOGRAPHICAL EQUITY ALLOCATION OF SPECIALIST MANDATES (2011-2017)**



Looking at UK pension funds, once again it is evident that there are further significant differences between the LGPS and other schemes. 26% of LGPS specialist mandates managed by IA members at the end of 2017 were in UK equity mandates, a two percentage point increase from 2016 (see Chart 40).

This is in contrast to corporate pension funds which held only 20% in UK equity mandates. So the LGPS remains more focused on equities and within that, on domestic equities.

**CHART 40: GEOGRAPHICAL EQUITY ALLOCATION OF SPECIALIST MANDATES AMONG UK PENSION FUNDS**

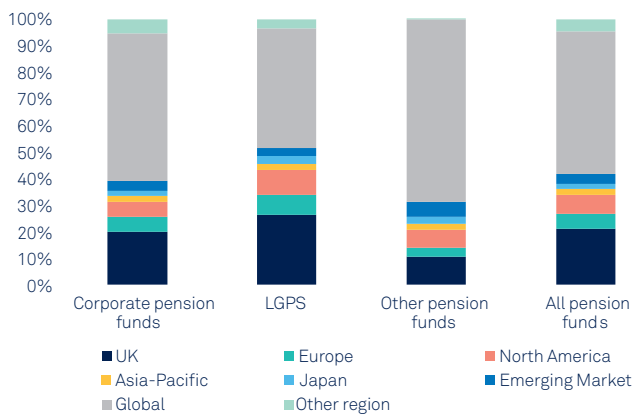
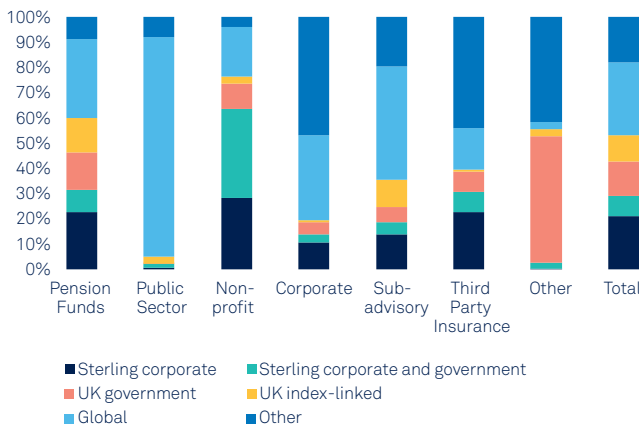
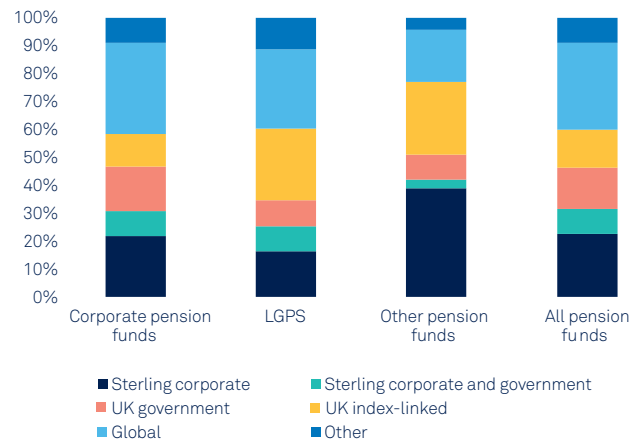


Chart 41 shows that within fixed income, global bonds are now the largest category of specialist mandate, at 29% (up from 21% in 2016). The amount allocated to government bonds (including index-linked) fell slightly, to 24%, but the big drop was in sterling corporate bonds, which fell from 27% to 21% year on year.

**CHART 41: FIXED INCOME ALLOCATION OF SPECIALIST MANDATES BY CLIENT TYPE**



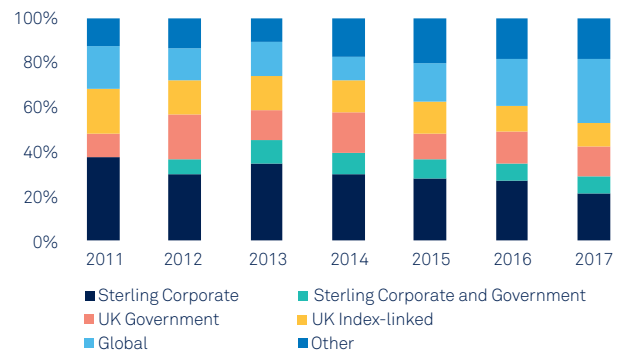
**CHART 42: FIXED INCOME ALLOCATION OF SPECIALIST MANDATE TYPES AMONG PENSION FUNDS**



Looking at the trend in fixed income allocation over the last five years, building on the increased allocation last year, global bonds overtook sterling corporates as the largest specialist mandate type for the first time in 2017, increasing to 29% of all specialist mandates.

Chart 41 also shows how fixed income allocation can differ by client type, and this difference is clear in the differences exhibited by different types of pension scheme. The LGPS has a significantly higher allocation to index-linked gilts and a much lower allocation to sterling corporate bond mandates than corporate pension schemes (see Chart 42).

**CHART 43: SPECIALIST FIXED INCOME ALLOCATION (2011-2017)<sup>45</sup>**



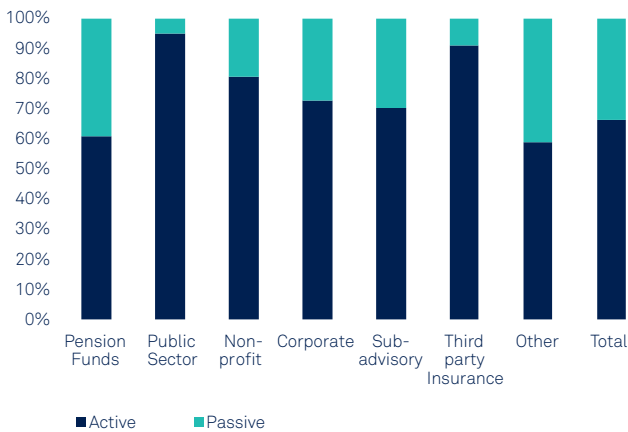
<sup>45</sup> £ Corporate and Government not separated out in 2011

### ACTIVE VS PASSIVE

Just under two thirds of assets (66%) were managed by IA members on an active basis, up from five years ago (61%).

All institutional client types this year were more likely to be managed on an active rather than a passive basis (Chart 44). This may reflect changes in asset allocation, and particularly the increased allocation to other assets, rather than any conscious shift out of passive and into active.

**CHART 44: ACTIVE AND PASSIVE THIRD PARTY MANDATES BY CLIENT TYPE (SAMPLE-ADJUSTED)**

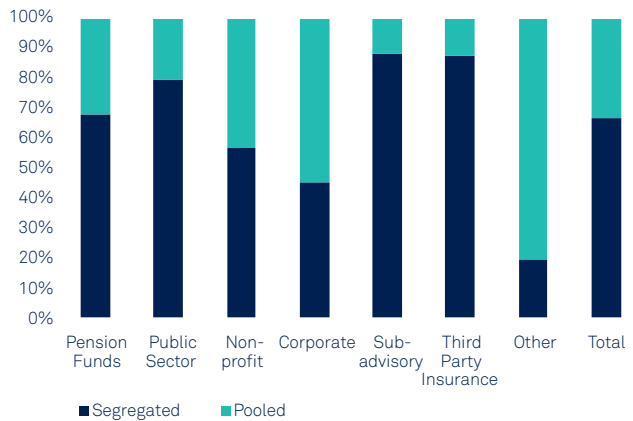


### SEGREGATED VS POOLED

Chart 45 shows that segregated mandates represented approximately two thirds (65%) of assets managed for third party institutional mandates at the end of 2017. Almost all mandates managed for third party insurance and sub-advised mandates were managed on a segregated basis in contrast to corporate mandates.

Other clients represent a wide variety of clients including family offices and private wealth firms and these assets are significantly more likely to be managed on a pooled basis.

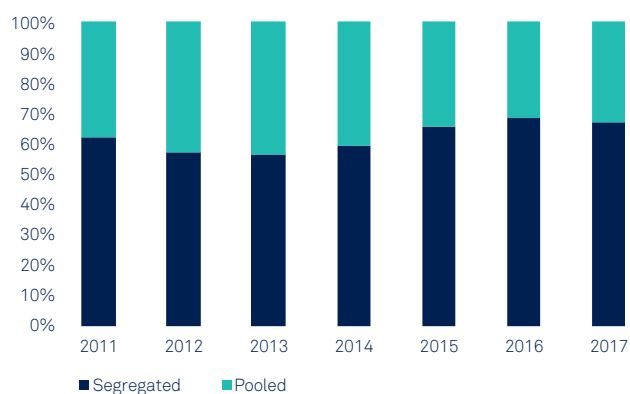
**CHART 45: SEGREGATED AND POOLED MANDATES BY INSTITUTIONAL TYPE**





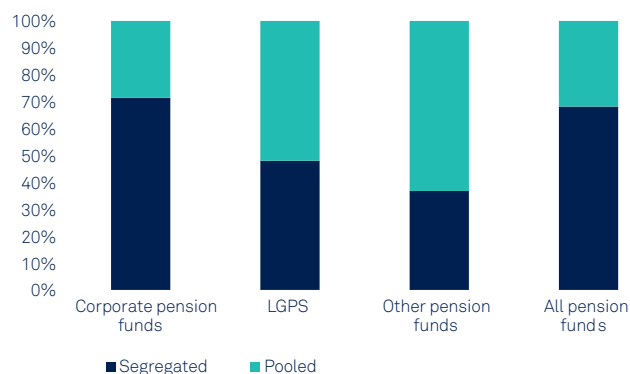
The increase in segregated mandates that was observed in the last four years may have reached a plateau as there was no further increase in 2017 (see Chart 46). However, it remains to be seen in the future whether the share of segregated mandates has stabilised at this level.

**CHART 46: INSTITUTIONAL SEGREGATED AND POOLED MANDATES (2011-2017)**



Corporate pension schemes use segregated mandates to a much greater extent than the LGPS funds and other pension schemes (see Chart 47), which may be partly related to scale. The pension schemes within the other category, which include pensions for smaller institutional clients such as charities, are more likely to use pooled management arrangements.

**CHART 47: SEGREGATED AND POOLED MANDATES AMONG THIRD PARTY PENSION FUNDS**



# 5 RETAIL FUND MARKET

## KEY FINDINGS

### FUNDS UNDER MANAGEMENT

- » UK investor funds under management in authorised and recognised funds domiciled in the UK and overseas grew by 15% to £1.2 trillion in 2017. £147 billion of this is held in funds domiciled overseas suggesting UK investors are not shying away from overseas funds following the Brexit referendum.

### ASSET MIX

- » Equity funds accounted for the largest proportion of funds under management, although their market share decreased slightly to 53%. UK equity funds fell to 20% of assets and non-UK equities increased slightly from 2016 to 34%.
- » The allocation to Fixed Income funds remained unchanged during the year at 18%.
- » Mixed Asset fund allocations fell slightly, partly reflecting the launch of the IA's Volatility Managed sector in April 2017 into which some mixed asset funds moved. The Other category saw the greatest growth in 2017 increasing by 1.7 percentage points to 12.5%.

### RETAIL FUND SALES

- » Net retail sales were £47.1 billion in 2017. This in part reflected a rebound from weak sales in 2016 following the Brexit referendum, but higher sales seen after the financial crisis may also be a response by investors to a number of structural changes encouraging investment into UK funds, in particular the low interest rate environment and the introduction of Pension Freedoms

### INVESTOR OBJECTIVES

- » Three themes dominated demand in 2017. Outcome and allocation funds continued to be in high demand with £13.8 billion in net retail sales. Fixed income was the second best selling strategy with £13.2 billion in net retail sales, consistent with continued demand for income-producing strategies. Equity growth sales were strong at £10 billion, although UK equity remained out of favour in the aftermath of the Brexit referendum.

### PASSIVELY MANAGED FUNDS

- » Index tracking and passively managed funds increased market share to 13.7% of the industry, continuing the overall trend towards passive investment. However, gross retail sales data, particularly for equity funds, indicated that investors have shown an increasing preference for active funds since 2015.
- » Mixed asset was the most popular choice in passive investment, with £2.9 billion in net retail sales.

### TRENDS IN FUND DISTRIBUTION

- » Fund Platforms remain the largest distributors in the UK with 43% of gross sales totalling £106 billion. Off platform sales through advisers increased by 49% in 2017 to £66 billion.

### INDUSTRY STRUCTURE AND CONCENTRATION

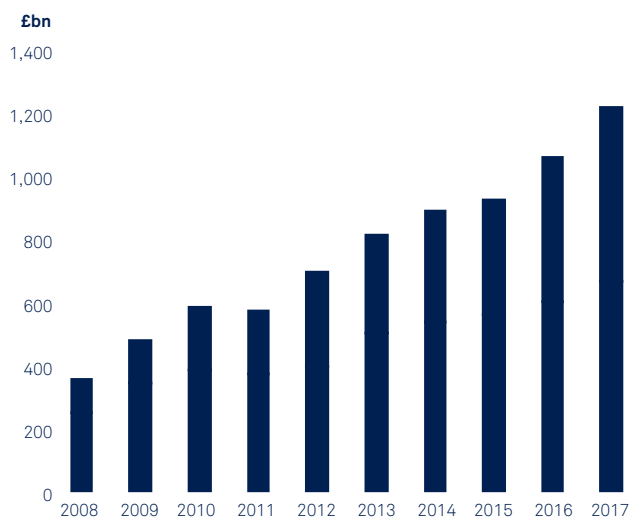
- » The ten largest firms increased their market share by two percentage points in 2017 to 46%.

This Chapter focuses on investment in UK authorised and recognised funds, which are approved for promotion and sale to retail investors in the UK and overseas. Although the Chapter discusses primarily sales to retail investors, institutional investors may also choose to invest in these funds and institutional comparisons have been included where relevant.

## FUNDS UNDER MANAGEMENT

Funds under management (FUM) for UK investors reached £1.2 trillion at the end of 2017, marking an average growth rate of 11.7% per year over the past five years – see Chart 48.<sup>46</sup> This is broadly in line with the growth rate of wider UK assets under management discussed in Chapter 1.

**CHART 48: INDUSTRY FUNDS UNDER MANAGEMENT (2008-2017)**



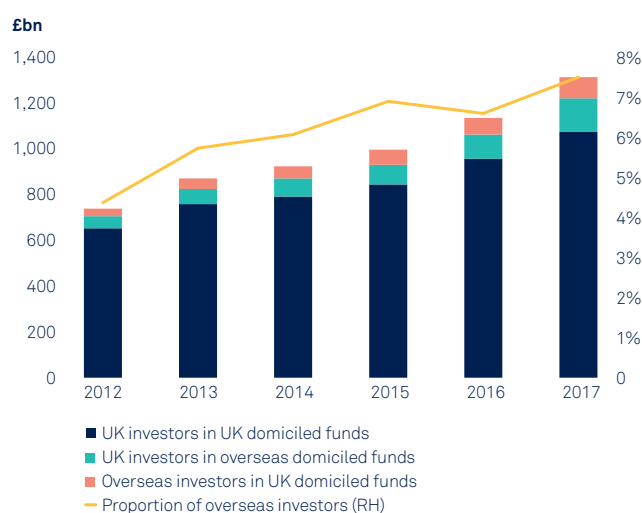
## INVESTOR DOMICILE

As part of a broader fund market characterised by significant cross-border activity, the UK market reflects activity of both UK and overseas investors.<sup>47</sup> Chart 49 breaks down the total FUM into three categories: FUM held by UK investors in UK-domiciled funds, FUM held by overseas investors in UK-domiciled funds; and FUM held by UK investors in overseas-domiciled funds.

It is quite clear that UK investors tend to invest in UK-domiciled funds, accounting for 93% (£1.1trn) of total FUM. This does not preclude appetite for investing in overseas-domiciled funds, as FUM held by UK investors in such funds reached £147 billion in 2017, which was a 37% year-on-year growth and a 178% increase since 2012. This would suggest that, as yet, UK investors are not beginning to shy away from overseas-domiciled funds following the Brexit referendum. As discussed later, IA data implies that this may rather be reflected in continued outflows from UK equity funds.

Notably, there has also been further demand for UK-domiciled funds by overseas investors who now hold 7% of UK-domiciled FUM, up from 4% in 2012.

**CHART 49: UK FUM BY INVESTOR RESIDENCE**



<sup>46</sup> Includes all assets held by UK investors whether in funds domiciled in the UK or overseas

<sup>47</sup> For example, the European Parliamentary Research Service estimates that over half of UCITS are distributed in two or more EU countries. See: EPRS, Cross-border distribution of investment funds, April 2018.

## FUNDS UNDER MANAGEMENT BY ASSET CLASS

The asset allocation of UK funds over the last twenty years has followed a similar pattern to that seen in the overall market, with the proportion of assets invested in equities, particularly the UK, falling, and the allocation to the Other asset class increasing (see Chart 50). UK Equities continued to lose market share in 2017, falling by 1.5 percentage points to 19.8% of the market, which is the lowest on record. In contrast, the share of non-UK equities has been growing steadily in the past five years, reaching 33.6% in 2017.

**CHART 50: FUM BY ASSET CLASS (1998-2017)**

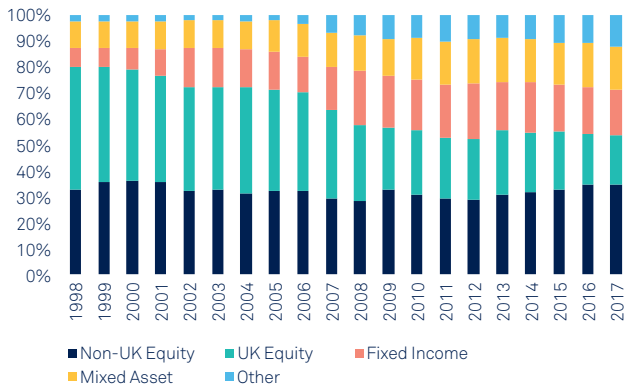
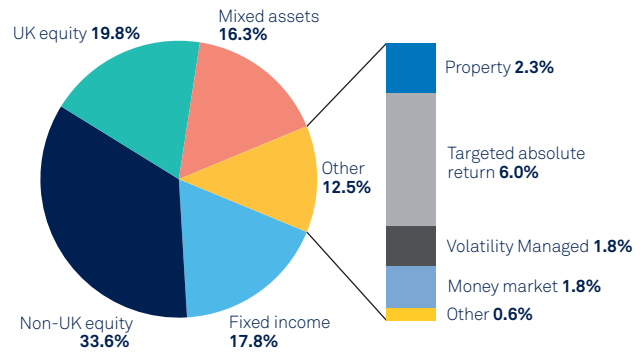


Chart 51 breaks out the Other category in more detail. One reason for the year-on-year increase (from 10.8% to 12.5%) was the introduction of the Volatility Managed sector which moved some funds from the Mixed Asset category. The other significant reason was the growth of the Targeted Absolute Return which increased by 14% from last year, and now accounts for 6% of total FUM.

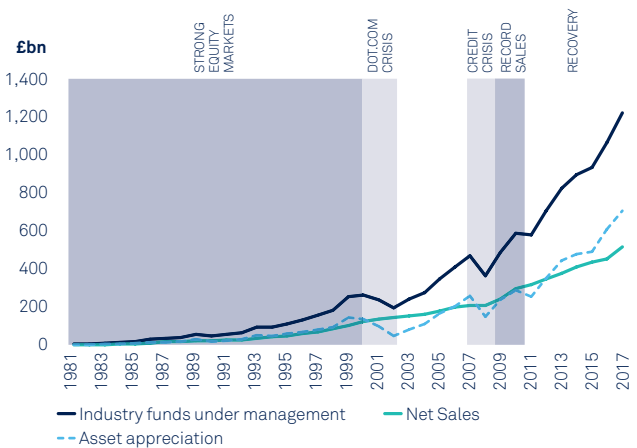
**CHART 51: FUNDS UNDER MANAGEMENT BY FUND/ASSET TYPE**



## DRIVERS OF GROWTH

Chart 52 shows the importance of both sales and asset appreciation to the increase in FUM since 1980. Over the period each has contributed broadly half of the growth in FUM. Whether this pattern will continue is unclear, as the potential changes to the structural drivers of retail sales could be leading to an increase in net annual sales figures (see page 69) at a time when market returns are likely to become more of a challenge.

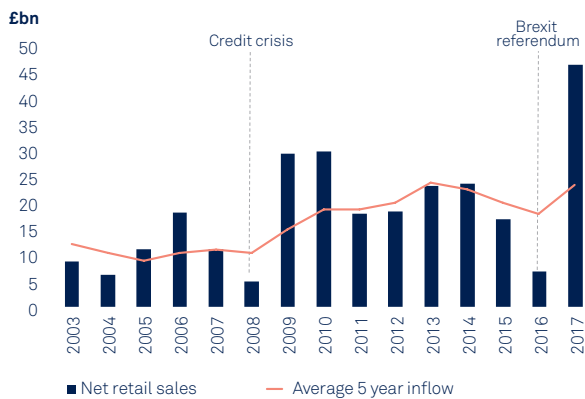
**CHART 52: DRIVERS OF INDUSTRY GROWTH (1980-2017)**



## RETAIL FUND SALES

2017 was a record year for net retail sales in the UK fund industry with £47.1 billion of new money being invested – see Chart 53. This could be reflecting a bounce back from the extremely low retail sales seen in 2016 which reflected concern around the Brexit referendum and the substantial outflows that followed from both equity and property funds.

**CHART 53: NET RETAIL SALES (2003-2017)**

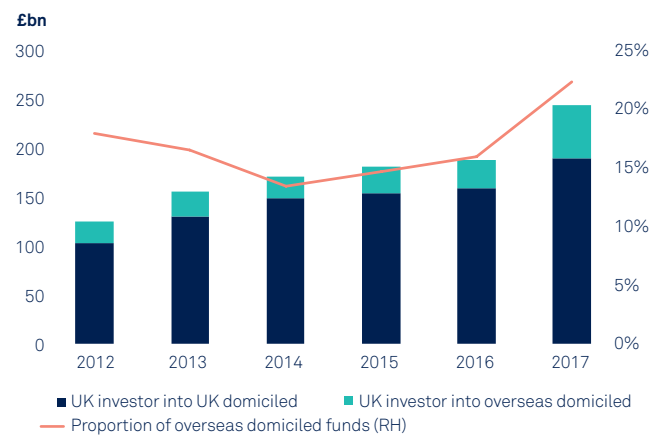


## RETAIL SALES IN OVERSEAS FUNDS

Gross sales are perhaps more indicative of investor demand for funds than net sales. During 2017, £189 billion of gross sales was invested in UK-domiciled funds and £54 billion in overseas-domiciled funds – see Chart 54.

The fact that 22% of UK investor money was directed towards overseas-domiciled funds, the highest since 2012 when the IA started collecting this data, suggests that any concerns over passporting of investment products following the UK's departure from the EU are not yet having a significant impact.

**CHART 54: GROSS UK INVESTOR SALES BY FUND DOMICILE**



## EXPLAINING FLOWS

In any given year, the drivers of retail fund demand are likely to reflect a wide-ranging set of factors. In the short-term, it would appear that the strength of 2017 was linked to the weakness of 2016 when negative sentiment around Brexit significantly dampened aggregate flows, impacting on specific asset classes (see Chart 56).

Longer-term, the aggregate retail flows into funds after the global financial crisis of 2008 have generally been higher than those seen previously. This is not obviously correlated with the pattern of UK aggregate savings rates which, while spiking through 2009-2010, are now lower than they were in 2008 after a steep fall through 2017.<sup>48</sup>

Based on research with financial advisers, the IA has tested the salience of four specific factors for explaining the current strength of flows into investment funds:

- 1. Low interest rate environment.** Following the financial crisis in 2008, the UK Official Bank Rate fell to 0.5% and has remained at that level or below until the 0.25% rate hike announced in August 2018.<sup>49</sup> This is obviously part of a global pattern that has created a hunt for yield among both retail and institutional investors. IA analysis from 2010-2011

<sup>48</sup> Households and NPISH saving ratio, ONS

<sup>49</sup> Between August 2016 and November 2017 the Bank of England lowered the rate even further, to 0.25%.

suggested a strong substitution effect as existing investors moved cash from banks and building societies into fixed income and later equity income.<sup>50</sup> This substitution effect would inevitably slow over time. Recent strength (last five years) of retail sales may indicate new savings being allocated to funds over more traditional sources such as cash ISAs.

- 2. Pension Freedoms.** Introduced in 2015, pension freedoms have allowed investors to take control of their own investment decisions during retirement, removing the virtual requirement to purchase an annuity that existed prior to that date. According to FCA data since October 2015, 55% of pension pots accessed have been fully withdrawn and 30% have entered drawdown.<sup>51</sup> The FCA also note that annuity sales are on a downward trend with new sales falling 13% in the period April to September 2017 compared to the same period in 2016. Pension freedoms also introduced the possibility for individuals to transfer out of private sector DB schemes into DC schemes for the first time.
- 3. Inheritance of wealth.** Recent research has underlined how significant bequests remain, whether as a result of direct bequest motive or precautionary saving, or a combination of these factors.<sup>52</sup> Although it is not uncommon for individuals to utilise the wealth accumulated in their primary housing in later life, the majority of individuals do not currently do so. As the demographics of those reaching retirement changes and individuals become more reliant on DC rather than DB pensions, it could be expected that the proportion of individuals accessing their housing wealth may increase. When it comes to financial wealth (excluding pension saving) the picture is rather different and the evidence suggests that the majority of financial wealth will be passed on rather than spent during retirement. The combination of these factors implies that significant wealth is likely to be inherited by younger generations via financial and housing assets.
- 4. Unwinding of buy-to-let property investment.** In recent years, buy-to-let investment has generally been viewed as a core investment option for those looking either for a stable income and/or for the potential for capital growth. However, recent changes

to incentives for landlords may have had a negative impact on this form of investment. In April 2016 the Government introduced an extra 3% stamp duty for landlords and those buying second homes. In April 2017 the Government introduced further changes which reduced the mortgage tax relief that is claimable, which could reduce the profits of many landlords. Recent data shows buy-to-let lending down by a fifth year-on-year.<sup>53</sup> The question then becomes whether this may result in stronger inflows into other investment markets.

In order to explore these possibilities in more detail, the IA commissioned Opinium to undertake research among UK IFAs, asking them how important various factors were in prompting investors to seek advice from them during the last twelve months (1 being low in importance and 5 being high). The results of this survey are shown in Table 3.

**TABLE 3: REASONS FOR SEEKING FINANCIAL ADVICE<sup>54</sup>**

	Importance Ranking (1-5)
To review the suitability of current investment portfolio	3.6
Seeking an alternative to cash kept in savings accounts	3.3
Transfers from defined contribution pension schemes	3.2
Inheritance of wealth	3.2
Cash released under new pension freedoms	2.9
Transfers from defined benefit pension schemes	2.7
Unwinding of buy-to-let property investment	1.7

With the exception of the unwinding of buy-to-let property investment, which ranks relatively low in importance, each of the four reasons outlined above does seem to be significant in prompting individuals to seek advice. Drivers of flows into investment funds therefore appear diverse, but the pension reforms of recent years are starting to feed through alongside the longer-standing themes.

<sup>50</sup> Asset Management in the UK 2010-2011, IA

<sup>51</sup> <https://www.fca.org.uk/publication/data/data-bulletin-issue-12.pdf>,

<sup>52</sup> The use of wealth in retirement, IFS Briefing Note BN237, Rowena Crawford 2017

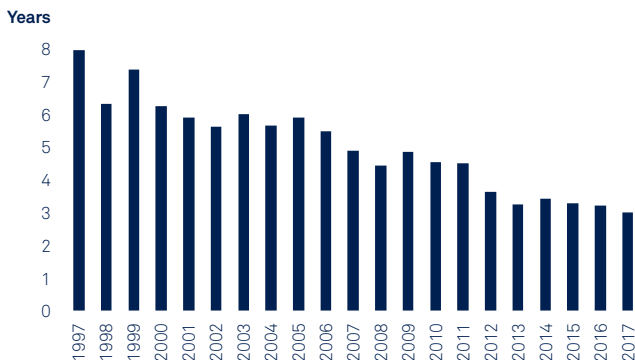
<sup>53</sup> UK finance

<sup>54</sup> Source: IFA omnibus survey conducted by Opinium in July 2018

## HOLDING PERIODS OF UK FUNDS

The length of time that retail investors hold a particular fund has more than halved over the past 20 years from around eight years in 1997 to three years in 2017 (see Chart 55).

**CHART 55: AVERAGE HOLDING PERIODS OF RETAIL INVESTORS (1997-2017)**



The reasons behind this are numerous and include:

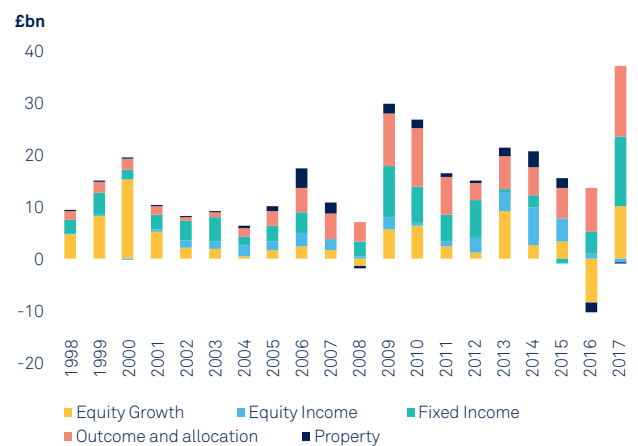
- Improved technology, particularly in regards to platforms. Retail sales through fund platforms have increased fourfold in the last ten years, with the greatest increase seen in relation to personal pensions (see Chart 71).
- Increased engagement as investors take more interest in managing their own money.
- An increase in the availability of independent research which can highlight new trends to investors.
- Increased concentration of funds selection through a variety of professional services designed to help investors and advisers.

## INVESTOR OBJECTIVES

Chart 56 shows that three themes dominated investment demand by retail investors during 2017:

- Outcome and allocation funds continued to be in high demand with £13.8 billion in net retail sales.
- Fixed income was the second best-selling strategy with £13.2 billion in net retail sales, consistent with the persistent demand for income-producing strategies.
- Despite a strong rebound in overall equity growth sales, UK equity remained out of favour in the aftermath of the Brexit referendum. UK equity sectors saw an outflow of £2.6 billion but the overseas equity sectors experienced strong investor demand so that equity growth as an objective received £10 billion in net retail sales – the highest since the year 2000.

**CHART 56: NET RETAIL SALES BY DIFFERENT INVESTMENT OBJECTIVE (1998-2017)**



## OUTCOME AND ALLOCATION IN THE ASCENDANCY

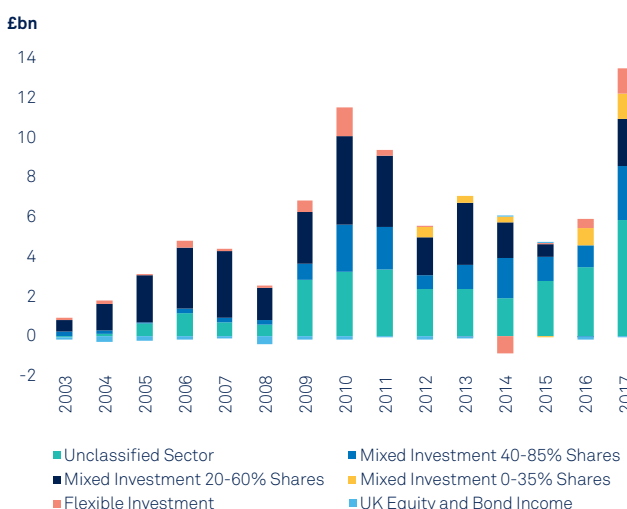
A diverse set of funds and sectors is included within the outcome and allocation category, with the unifying characteristics of active allocation and/or specific risk management objectives relating to volatility or absolute capital preservation:<sup>55</sup>

- Five Mixed Asset sectors, with retail inflows of £7.6 billion in 2017. Notably passive mixed asset funds accounted for £2.9 billion.
- The Targeted Absolute Return sector, which was the best-selling individual sector with an outcome and allocation objective categorisation. The TAR sector had net retail sales of £3.2 billion.
- The IAs newly-launched Volatility Managed sector saw positive retail sales of £1.9 billion since its launch in April 2017.
- Money Market sector funds attracted inflows of £1.3 billion.

## MIXED-ASSET

Chart 57 shows the net retail sales into mixed asset funds broken down by specific categories within this (including those in the Unclassified sector). The Unclassified sector makes up a large share of the mixed asset universe and had the highest net retail inflow in 2017, £5.8 billion.

**CHART 57: NET RETAIL SALES OF MIXED ASSET FUNDS (2003-2017)**



There are a significant number of mixed asset funds in the Unclassified sector.

There are two reasons for this:

- These funds may change their asset allocation more often than those in the mixed-asset sectors, making them less comparable to other mixed asset funds.
- The mixed-asset sector parameters are largely based on the fund's exposure to equities. Funds which change their asset allocation relatively frequently could end up switching between mixed-asset sectors fairly often, meaning that not one sector would be appropriate.

<sup>55</sup> Data in the outcome and allocation objective exclude funds in the IA's unclassified sector. Where possible the analysis on pages 72 to 73 includes unclassified funds allocated to various asset classes

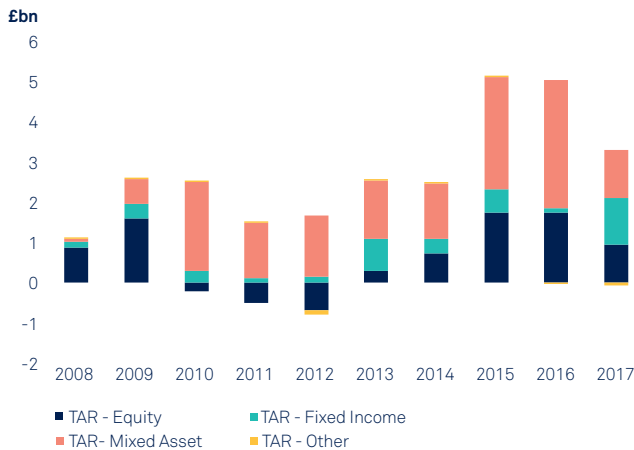


**TARGETED ABSOLUTE RETURN**

The Targeted Absolute Return sector was the third best-selling sector for UK retail investors in 2017 with £3.2 billion in net retail sales. FUM grew by 15% reaching £81.3 billion at the end of 2017.

Looking at the asset class split within this sector, Mixed Asset and Fixed Income absolute return funds both had net retail sales of £1.2 billion in 2017 – see Chart 58. Equity funds had slightly lower net retail sales at £932 million.

**CHART 58: NET RETAIL SALES TARGETED ABSOLUTE RETURN FUNDS BY ASSET CATEGORY (2008-2017)**



**VOLATILITY MANAGED**

The IA launched the Volatility Managed sector in April 2017 for funds that are managed within specific volatility targets.

These funds are designed to carry investors through their investment cycle. Namely, earlier in their life investors may be looking to grow their investments over the long term and be prepared to take on more risk as a result. Nearer retirement investors are likely to have a shorter term investment horizon and may be more

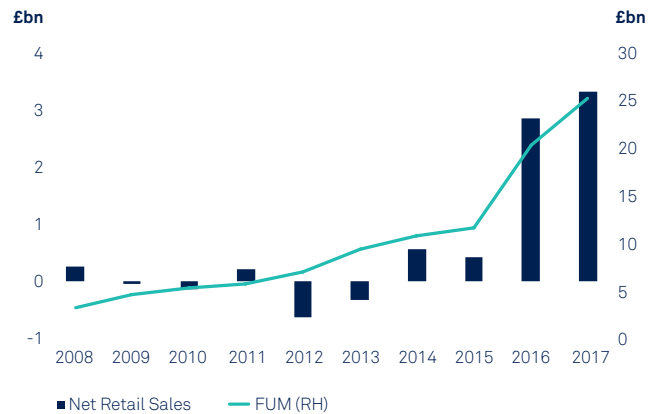
concerned about preserving the capital they have built up. Consequently, they would typically require lower volatility investments to meet their needs.

The sector launched with 87 funds in April. By the end of the year, it counted 98 funds. Funds under management grew from £20.2 billion in April to £24.8 billion in December, largely due to strong retail flows that averaged £216 million per month (including institutional flows the average was closer to £400 million).

**MONEY MARKET FUNDS**

After receiving a (then) record net inflow of £2.8 billion in 2016, Money Market funds (including those in the IA's unclassified sector) experienced another record year, with net retail inflows of £3.3 billion (see Chart 59).<sup>56</sup>

**CHART 59: NET RETAIL SALES OF MONEY MARKET FUNDS (2008-2017)<sup>57</sup>**



The large flows into Money Market funds began in the second half of 2016, following the Brexit referendum, and continued well into 2017, with the majority of assets coming through advisers. Overall, this could be reflecting increased cash allocations in model portfolios and discretionary management.

<sup>56</sup> When institutional investor channels are included net sales into Money Market funds were £8.7 billion in 2016 and £4.2 billion in 2017.  
<sup>57</sup> Includes money market funds in the IA's unclassified sector, which saw inflows of £2 billion in 2017.

## A STRUCTURAL SHIFT?

Outcome and allocation funds have been particularly popular with retail investors for over 20 years. Notably, there has not been a single annual outflow since the IA started collecting data in 1995. The last ten years specifically have seen a step change:

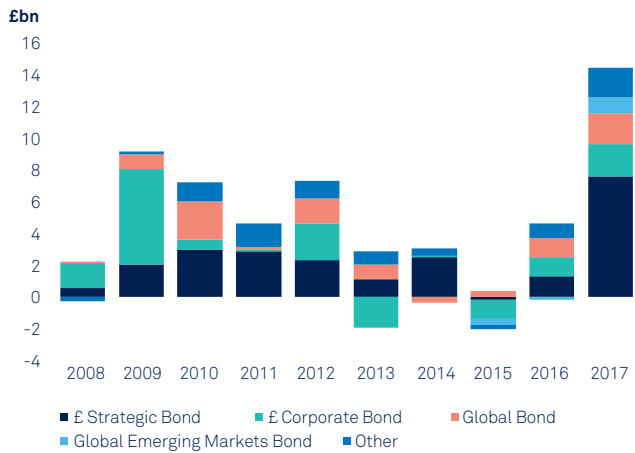
- Outcome and allocation funds accounted for 40% of total net retail sales since 2008 compared to 20% in the decade before that.
- Adding income funds (equity and fixed income), 80% of flows since the financial crisis of 2008 have been destined for funds that have an income, allocation or wider risk-management objective. This compares to 60% in the 1998-2008 period.

This universe expands the definition of active management well beyond stock and securities selection into areas where value is added by specific expertise – eg. asset allocation or risk targeting. This holds true independently of whether the underlying components are active or indexed. The rise of passive multi-asset (see page 72) is one illustration of this, with allocators needing to take a view on asset classes, geographies and possibly factors such as investment styles, which is ultimately an active allocation decision.

## ONGOING FOCUS ON INCOME

Bonds are the natural home for investors looking for income provision and they clearly dominate this space (see Chart 60). Sterling strategic bond funds drew the lion’s share of net retail sales in 2017 with £7.5 billion invested. The next best-selling was sterling corporate bond at £2.1 billion. Strategic bond funds tend to have wide investment mandates allowing access to bonds across the fixed income spectrum as well as more freedom to manage interest rate risk. Flows into this sector in 2017 are consistent with investors preferring bond funds with greater investment flexibility during a more uncertain investment environment.

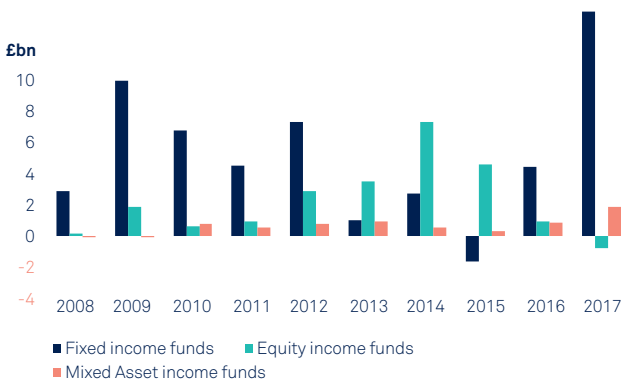
**CHART 60: NET RETAIL SALES OF FIXED INCOME FUNDS (2008-2017)**



Sales into income-focused mixed asset funds were strong as well, with a record of £15.3 billion of net retail sales. This would suggest that investors may be finding other sources of income-generating strategies.

In contrast to fixed income and mixed asset income funds, 2017 was the first year since 2000 when there was an outflow from equity income funds. Given that this group is skewed toward UK equity income funds (79% of assets are UK focused), this outflow could be linked to broader investor asset allocation decisions and the general outflows from UK equity that we have been observing throughout 2017 as discussed in the next section (see Chart 61).

**CHART 61: NET RETAIL SALES OF INCOME FOCUSED FUNDS (2008-2017)**



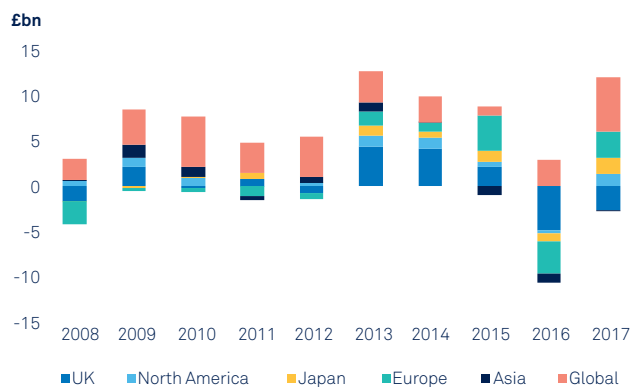
**STRONGER EQUITY GROWTH SALES, BUT OUTSIDE THE UK**

Equity growth funds saw positive net retail sales of £10 billion following an outflow in 2016. The drivers behind this were Global and European equity funds with £5.6 billion and £2.9 billion in net retail sales respectively (see Chart 62).

In sharp contrast, the UK All Companies and UK equity income sectors saw outflows of £1.7 billion and £1.1 billion respectively. Notably, outflows from active UK equity funds have been partially offset by inflows into passive UK equity (see page 77).

Still, cumulatively, UK equity funds have seen outflows of £7.5 billion over the last two years, suggestive of a more negative view of UK equities since the Brexit referendum. In the context of continued investment of UK investor money in overseas funds and vice versa (see page 67), this would imply that any concerns on Brexit relate more to the chances of future growth in the UK equity market rather than the continued existence of the infrastructure that allows seamless cross-border distribution.

**CHART 62: NET RETAIL SALES OF EQUITY FUNDS BY REGIONAL FOCUS (2008-2017)**



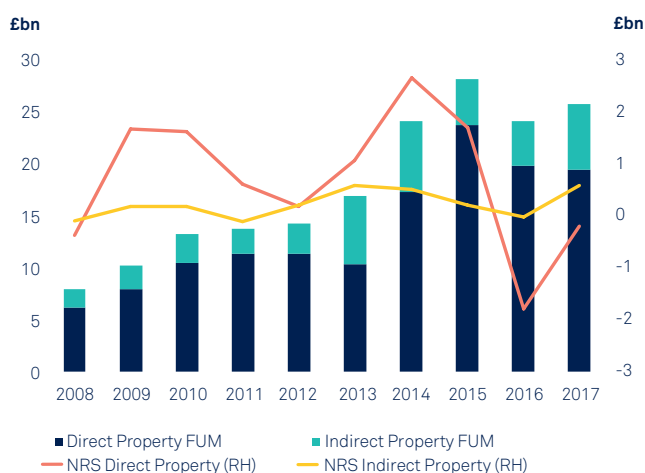
## OTHER SECTORS

### PROPERTY

Both 2016 and 2017 have been difficult for the Property sector. Large scale redemptions following the Brexit referendum ended a seven year run of positive annual net retail sales. There was a further, albeit much smaller, retail outflow from the property sector in 2017, of £137 million. Ultimately, it was due to asset appreciation that FUM overall grew by 7% to reach £25.7 billion.

Chart 63 shows the Property sector funds under management and net retail sales broken down by direct property funds that invest in buildings, and indirect property funds that invest in property related equities. Indirect property funds suffered less in 2016 with a small net retail outflow of £23 million and actually attracted an inflow of £580 million in 2017. Direct property funds experienced net retail outflows in both 2016 and 2017 of £1.8 billion and £207 million, respectively.

**CHART 63: PROPERTY SALES AND FUM (2008-2017)**



## PASSIVELY MANAGED FUNDS<sup>58</sup>

Passively managed funds continued to take market share from active funds in 2017, accounting for 13.7% (13.1% in 2016) of the UK fund market. Their net retail sales were £9.2 billion in 2017 and FUM grew by 20% to £187 billion (including fund of funds).

Although UK equities still make up the largest strategy representing 34% of passive funds, this share is falling, with faster growth seen in the Global Equity and Mixed Asset strategies (see Chart 64).

**CHART 64: FUNDS UNDER MANAGEMENT OF PASSIVE FUNDS BY INDEX INVESTMENT TYPE (2008-2017)**

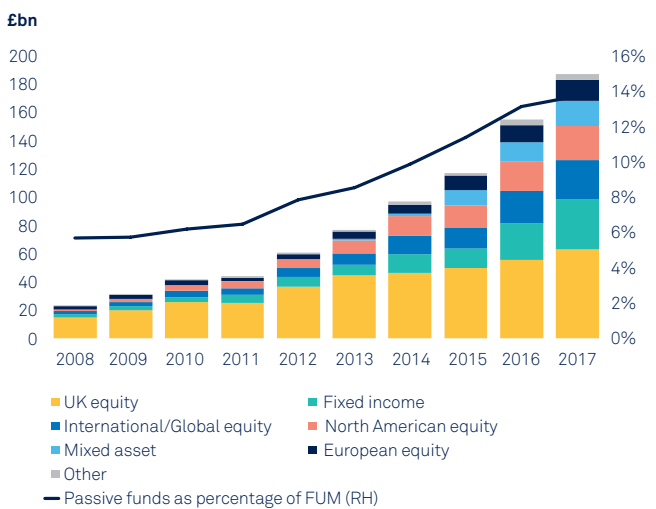


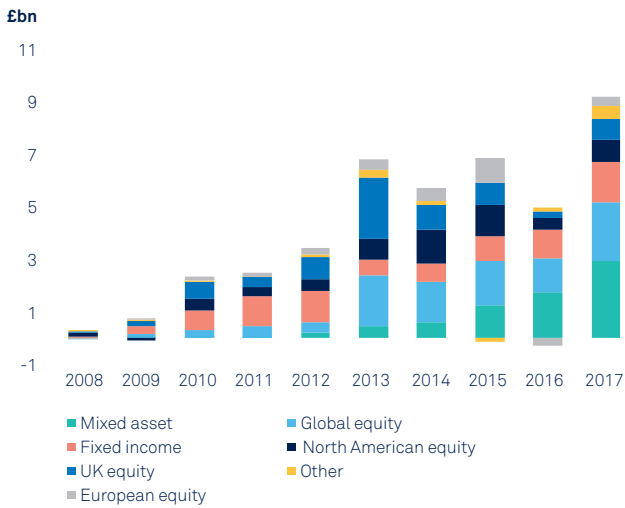
Chart 65 breaks down net retail sales for passive funds into underlying strategies. The best-selling passive strategy was Mixed Asset with net retail sales of £2.9 billion. This is a significant growth Chart 67 shows accelerating growth in this area since 2009, when net retail sales were just £13 million.

Similar to the active fund universe, Global equity was a popular strategy within passive funds with £2.2 billion in net retail sales.

Notably, unlike their active counterparts, passive UK equity funds received positive net retail sales, with an £800 million inflow.

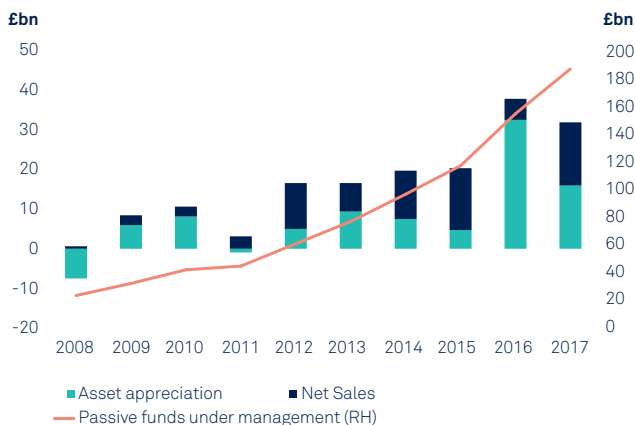
<sup>58</sup> IA data focuses on open-ended funds, and does not currently include ETF flows.

**CHART 65: NET RETAIL SALES OF PASSIVE FUNDS BY INDEX INVESTMENT TYPE (2008-2017)**



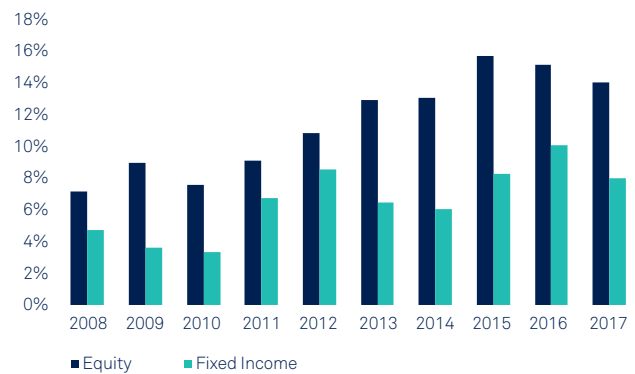
Net sales (retail and institutional) into passive funds were £16.2 billion in 2017 which marked a significant increase on the £5.3 billion invested in 2016. Asset appreciation was lower at £15.8 billion, compared to £32.6 billion in 2016.

**CHART 66: CONTRIBUTION TO FUNDS UNDER MANAGEMENT IN PASSIVE FUNDS (2008-2017)**



The proportion of gross sales attributed to passive funds fell in 2017 to 14% for equities and 8% for fixed income (see Chart 67). Whilst the proportion of FUM in tracker funds continues to increase, the gross sales data suggests that investor appetite for active funds, equities in particular, has recently increased.

**CHART 67: GROSS SALES OF PASSIVE FUNDS AS A PERCENTAGE OF GROSS SALES BY ASSET CLASS (2008-2017)**



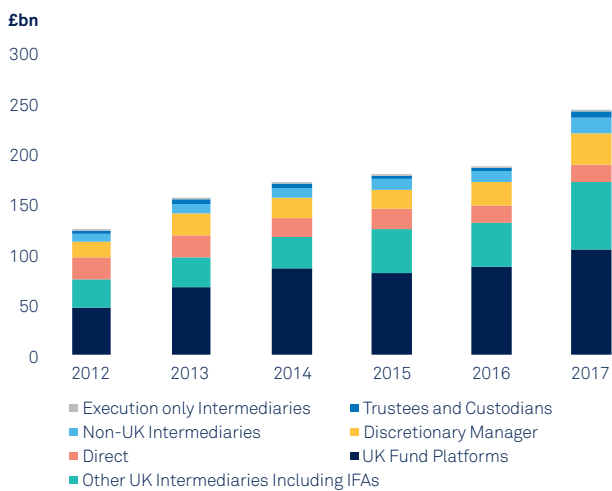
## TRENDS IN FUND DISTRIBUTION

Fund platforms continue to be the largest sales channel for investment funds in the UK (see Chart 68).<sup>59</sup> In 2017, gross sales through direct-to-consumer and adviser fund platforms were £106 billion, a 21% year-on-year increase. Platforms accounted for 43% of the total £243 billion of gross sales last year.

Sales through the Other UK Intermediaries including IFAs channel increased by 49% with gross sales of £66 billion with the market share increasing to 27%. Direct sales increased slightly from £17.7 billion in 2016 to £17.9 billion in 2017, however, their market share was at only 7%.

This reflects a new state of the retail distribution landscape following the structural change brought about by RDR. For example, in 2012 the Direct channel accounted for 18% of gross retail sales while platforms were only at 38%.

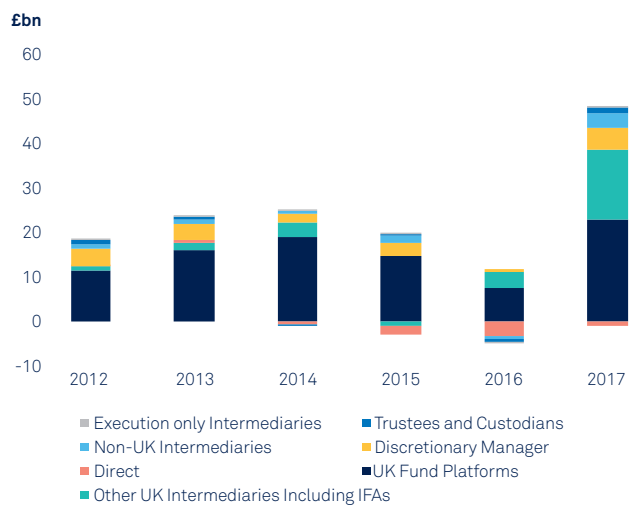
**CHART 68: GROSS RETAIL SALES BY DISTRIBUTION CHANNEL (2012-2017)**



Of the record £47.1 billion net retail sales in 2017, £22.9 billion of net retail money came through platforms and £15.5 billion came through the Other UK Intermediaries including IFA channel (see Chart 69).

The Direct channel was the only one to experience a net outflow in 2017, by £759 million. This was significantly lower than the outflows seen in 2015 and 2016 (£2.1 billion and £3.2 billion respectively). The fact that the Direct sales channel had similar gross sales in 2017 to 2016, but lower net outflows, would suggest that fewer investors sold out of their direct investments in 2017.

**CHART 69: NET RETAIL SALES BY DISTRIBUTION CHANNEL (2012-2017)**

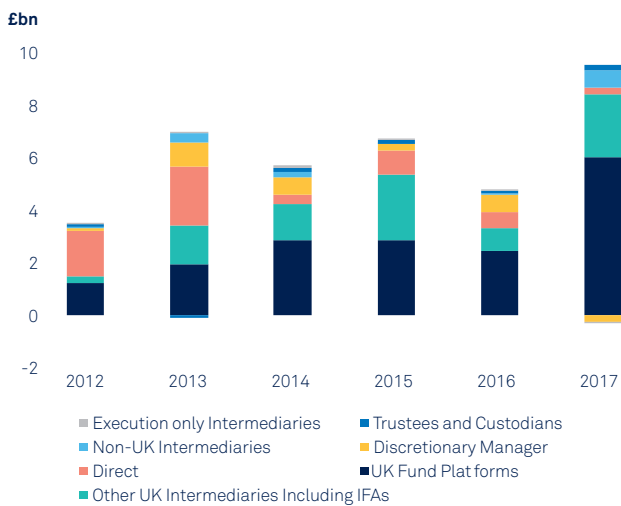


<sup>59</sup> Five fund platforms provide data to the IA. These are Cofunds, Fidelity, Hargreaves Lansdown, Old Mutual Wealth and Transact.

## DISTRIBUTION OF PASSIVE FUNDS

Chart 70 shows the distribution of passive funds in more detail. UK Fund Platforms were the dominant sales channel in 2017 with £6 billion of net retail sales. Advisers are the second largest channel with net retail sales of £2.4 billion. Discretionary managers had an outflow of £277 million, which implies that they showed a preference for active strategies in 2017.

**CHART 70: TRACKER NET RETAIL SALES BY DISTRIBUTION CHANNEL (2012-2017)**

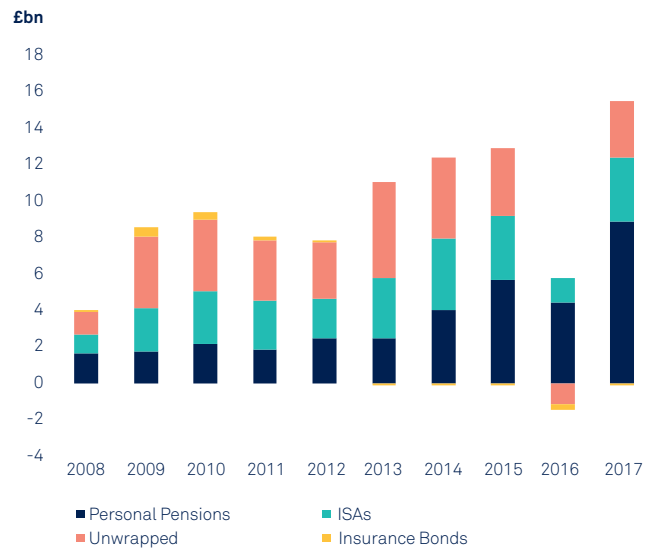


## WRAPPERS USED BY RETAIL INVESTORS IN THE UK

Chart 71 uses data provided by five UK fund platforms with combined assets under administration of £261 billion to show how retail investors use various tax efficient vehicles to buy funds.

- The largest absolute growth was in personal pensions with a 104% year-on-year increase. Since 2008, net retail sales have grown from £1.6 billion in 2008 to £8.9 billion in 2017.
- ISA sales have increased from £1 billion in 2008 to £3.5 billion in 2017. ISA allowances have increased by a similar factor, from £7,000 a year in the 2007/08 tax year to £20,000 in the 2017/18 tax year.

**CHART 71: RETAIL INVESTING TRENDS (NET RETAIL SALES THROUGH FUND PLATFORMS)**



## FUND OF FUNDS

Fund of funds also had a record breaking year in terms of sales in 2017, helping their market share increase to 12.5% of industry assets (£153 billion). The choice between fettered (constructed by a single manager) and unfettered (whole of market) was relatively evenly split with £5.2 billion in net retail sales into fettered fund of funds and £4.6 billion in unfettered funds (see Chart 72).

**CHART 72: NET RETAIL SALES OF FETTERED AND UNFETTERED FUNDS OF FUNDS (2003-2017)**

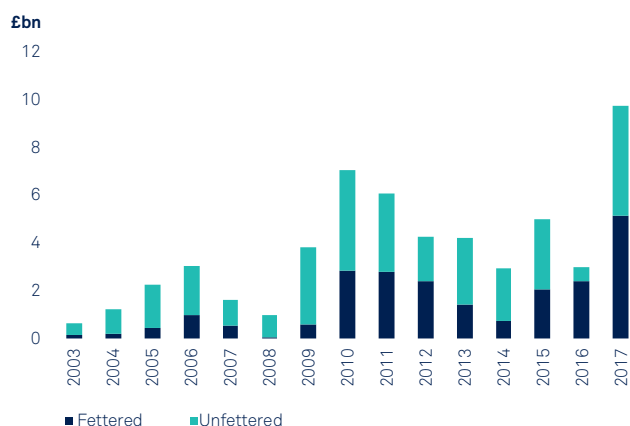


Chart 73 shows the annual contribution made to FUM growth by sales and asset appreciation. Net sales have been positive in each of the last ten years, even when asset appreciation has been negative.

**CHART 73: CONTRIBUTION TO FUNDS UNDER MANAGEMENT IN FUND OF FUNDS (2008-2017)**

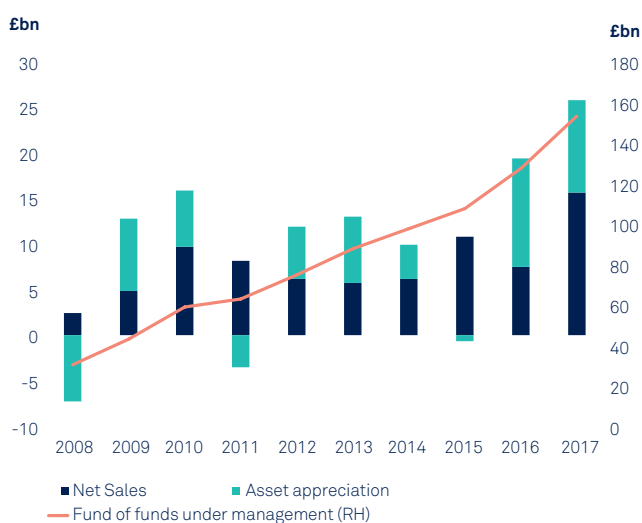


Table 4 shows the breakdown of net retail sales into fund of funds by distribution channel.

**TABLE 4: NET RETAIL SALES INTO FUND OF FUNDS BY DISTRIBUTION CHANNEL**

	Net Retail Sales Fettered £'s	Net Retail Sales Unfettered £'s
UK Fund Platforms	4,278,152,805	2,690,186,242
Other UK Intermediaries Including IFAs	594,016,861	651,083,372
Discretionary Manager	304,629,449	669,900,951
Trustees and Custodians	181,746,236	-85,301,927
Non-UK Intermediaries	97,584,505	203,286,280
Execution only Intermediaries	-254,301	2,585,028
Direct	-262,290,498	489,952,689



## INDUSTRY STRUCTURE AND CONCENTRATION

Despite M&A activity and the widespread use of third party CIS Operators, the number of fund management companies reporting data to the IA increased in 2017 to 158. This includes a number of new members joining the IA in 2017.

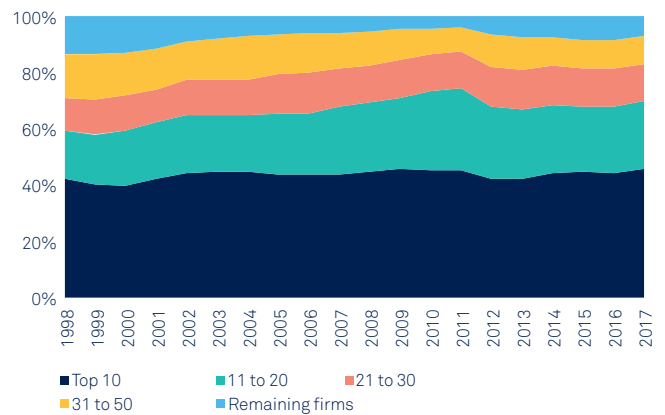
Chart 74 shows the number of firms reporting to the IA over the last 15 years. The sharp increase in 2012 is due to the change in the way the IA reports data from a UK-domiciled to UK investor basis. From 2012 onwards, the data included overseas funds operated by firms reporting to the IA which include money from UK investors.

**CHART 74: NUMBER OF FIRMS REPORTING TO IA (2003-2017)**



In terms of industry concentration, the ten largest firms increased their market share by two percentage points in 2017 to 46%.

**CHART 75: COMBINED MARKET SHARES OF TOP FIRMS BY FUNDS UNDER MANAGEMENT (1998-2017)**



## UK MARKET IN EUROPEAN CONTEXT

The UK remains the fifth largest European fund domicile with €1.6 trillion equivalent in UK-domiciled funds.

**FIGURE 12: ASSETS DOMICILED IN EUROPEAN UCITS AND AIFS 2017**



Country	Net assets (€bn)	Market share
1. Luxembourg	4,160	27%
2. Ireland	2,396	15%
3. Germany	2,038	13%
4. France	1,929	12%
5. United Kingdom	1,646	11%
6. Netherlands	843	5%
7. Switzerland	551	4%
8. Sweden	335	2%
9. Italy	321	2%
10. Denmark	301	2%
Rest of Europe	1,103	7%
<b>TOTAL</b>	<b>15,623</b>	<b>100%</b>

Source: EFAMA

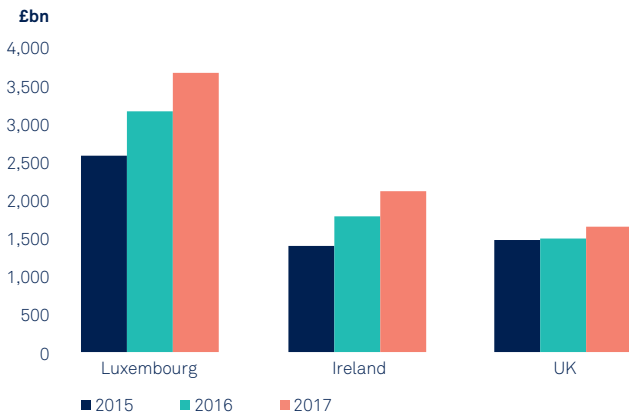
Flows into funds across Europe were high during 2017 (see Chart 76).

**CHART 76: NET SALES OF UCITS IN EUROPE (2016-2017)**



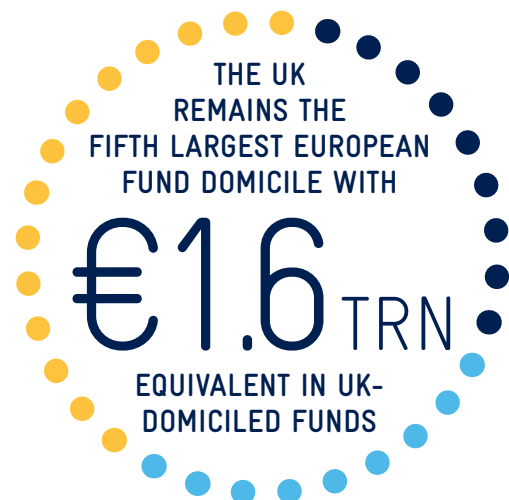
Source: EFAMA

Chart 77 shows the growth in assets of UCITS and AIFS in Luxembourg and Ireland, compared to the UK. Luxembourg and Ireland showed the greatest increase overall, in 2017.

**CHART 77: ASSETS IN EUROPEAN UCITS AND AIFS**

Source: EFAMA, figures displayed in sterling terms

Nonetheless, the UK experienced the greatest growth in UCITS assets outside of these two centres, suggesting there is no particular appetite among investors to move away from UK-domiciled funds as a result of uncertainty around Brexit.<sup>60</sup>



<sup>60</sup> Quarterly Statistical Bulletin, EFAMA

# 6 OPERATIONAL AND STRUCTURAL ISSUES

## KEY FINDINGS

### REVENUE AND COSTS

- » Total average industry revenue after commission stood at £20.6 billion in 2017, a 17% increase in nominal terms, likely reflecting the strong asset growth experienced in the second half of 2016. This equates to 28bps of total assets, same as in 2016.
- » Total operating costs in 2017 increased to £14.4 billion. In basis point terms this represents an increase from 19bps to 20bps.
- » Once again costs increased at a higher rate than revenue during 2017, meaning that profitability for the year averaged 30%, down 2 percentage points from 2016.

### EMPLOYMENT IN THE ASSET MANAGEMENT INDUSTRY

- » We estimate that the UK asset management industry directly employed 38,000 people at the end of 2017, up by around 1% on the 2016 figure.
- » Jobs in the asset management industry vary by location, with the largest proportion in London being employed in investment management and operations and fund administration being of greater importance in Scotland.
- » Staff in Compliance, Legal and Audit have grown most significantly over the past five years with the proportion of staff employed in these roles more than doubling within this time.

### INDUSTRY CONCENTRATION

- » The UK asset management industry remains relatively unconcentrated. Assets managed by the top five and the top ten firms increased slightly from 2016, to 43% and 58% of total assets respectively.
- » The number of small firms, with assets below £15 billion, increased from 84 to 88 in 2017. This is likely to reflect a change in IA membership rather than any industry trend.
- » The median figure for assets managed by IA member firms was similar to 2016, at £10 billion, compared to a mean figure of £50 billion.

### ASSET MANAGER OWNERSHIP

- » The proportion of assets run by independent asset managers was at 40%, slightly up from 2016 but almost double the proportion in 2008 (21%).
- » Asset managers that are owned by a UK parent represent 43% of assets under management, down from 58% in 2008. US owned managers represent 46% of assets under management, up from 27% in 2008.

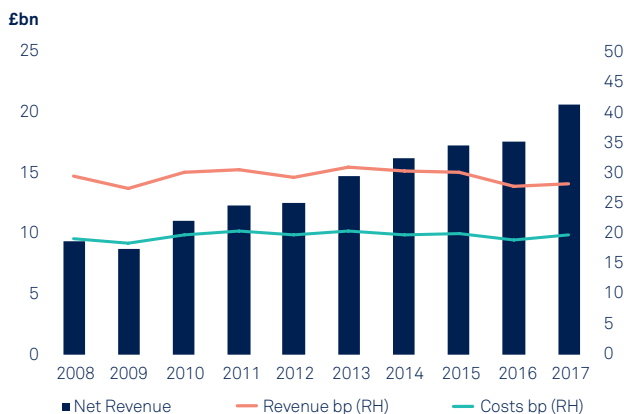
This Chapter focuses on asset managers as firms. It covers three broad themes: industry revenue and profitability, employment and M&A activity.

## REVENUE AND COSTS

Chart 78 reports aggregate revenue and cost figures for the industry, covering both in-house and third party business.

- Total average industry revenue after commission stood at £20.6 billion in 2017, a 17% increase in nominal terms, likely reflecting the strong asset growth experienced in the second half of 2016. This equates to 28bps of total assets, equal to 2016.<sup>61</sup>
- Total operating costs in 2017 increased to £14.4 billion. In basis point terms this represents an increase from 19bps to 20bps.
- Once again costs increased at a higher rate than revenue during 2017, meaning that profitability for the year averaged 30%, down 2 percentage points from 2016.<sup>3</sup>
- Viewed over a longer time horizon, average profitability has declined from 35% in 2008.

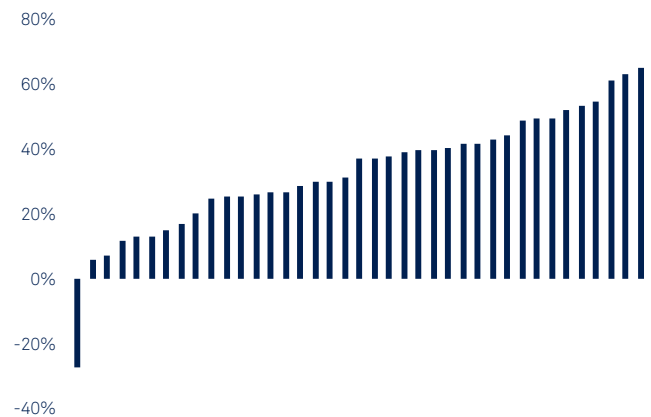
**CHART 78: INDUSTRY NET REVENUE VS. REVENUE AND COSTS AS PERCENTAGE OF AVERAGE ASSETS UNDER MANAGEMENT (2008-2017)**



The average profitability in any one year does not fully reflect a very diverse operating environment. Chart 79 shows the distribution of profitability of respondent firms in 2017.

Profitability ranged from -27% to 65%, with one quarter of firms having profit margins below 25% and one quarter above 43%.

**CHART 79: DISTRIBUTION OF ASSET MANAGER PROFITABILITY**



<sup>61</sup> Calculated as net revenue less costs divided by net revenue.

## EMPLOYMENT IN THE ASSET MANAGEMENT INDUSTRY

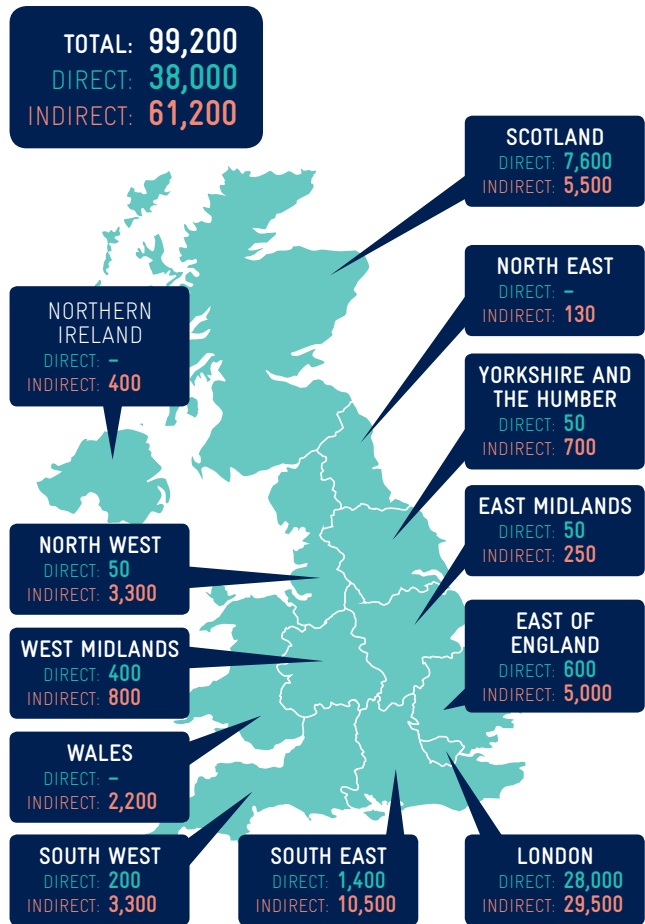
IA data indicates that the UK asset management industry supports just under 100,000 jobs in the UK both directly (38,000) and indirectly (61,200) in fund and wider administration services and securities and commodities dealing activities. The bulk of this resource is concentrated in London and South East England, with a broader regional footprint, particularly seen in a strong Scottish industry.

Figure 13 shows this in more detail. Specifically, IA members have offices across the UK. Locations include: Bristol, Birmingham, Bournemouth, Cardiff, Chester, Chelmsford, Harrogate, Henley, Leeds, Manchester, Norwich, Oxford, Peterborough, Southampton, Swindon and York.<sup>62</sup>

Beyond this immediate employment base, there are further associated professional groups:

- An estimated 26,000 independent financial advisers in the UK, a proportion of whom are involved in the distribution of asset management services.
- An estimated 61,000 people are employed by FinTech companies in the UK. Only a small proportion of these are likely to be working directly in support of asset management but this is an area of employment that is likely to grow in significance in the coming years.<sup>63</sup>

**FIGURE 13: DIRECT AND INDIRECT EMPLOYMENT IN ASSET MANAGEMENT IN THE UK**



Source: IA estimates from information provided by members and publicly sourced information. All regional numbers have been rounded to the nearest 50 and therefore may not add to exact total

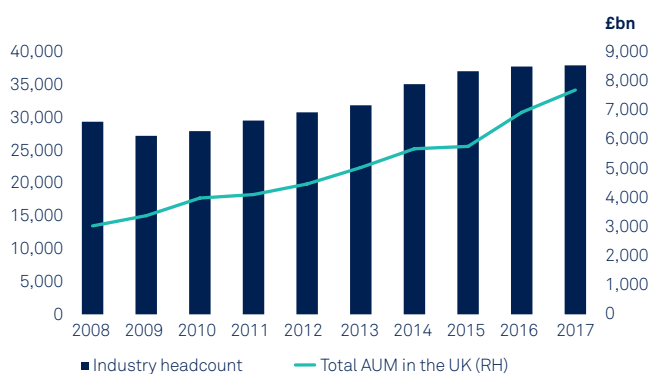
<sup>62</sup> It is difficult to identify jobs associated with asset management among firms that have a remit that extends wider than their asset management support, such as consultants, lawyers and accountants. In addition, a substantial number of roles in areas such as IT are outsourced to third party organisations and cannot be discretely measured. The figures provided below should therefore be viewed as a conservative estimate of those employed in asset management related roles.

<sup>63</sup> UK FinTech On the cutting edge An evaluation of the international FinTech sector, EY, 2016

## DIRECT EMPLOYMENT

The number of people directly employed in the asset management industry in the UK increased by 1% during 2017, albeit at a slower rate than that seen in recent years. The total reached 38,000 (see Chart 80), representing an overall increase of 29% since 2008

**CHART 80: INDUSTRY HEADCOUNT ESTIMATE VS UK ASSETS UNDER MANAGEMENT (2008-2017)**



Around three quarters of asset management firms outsource at least some of their staffing to external organisations and so these figures are likely to understate the numbers working to directly support asset management activity.

“THE INVESTMENT MANAGEMENT INDUSTRY IS A SIGNIFICANT EMPLOYER AND A SIGNIFICANT PART OF THE UK FINANCIAL ECOSYSTEM AND THE ECONOMY.”

## DISTRIBUTION OF STAFF BY ACTIVITY

Table 5 provides more detail on the number of employees directly employed by asset managers in the UK by function. The breakdown of staff activity was little changed from 2015. The proportion of staff in frontline investment management was up slightly at 25%, but still down from the high of 28% in 2014.

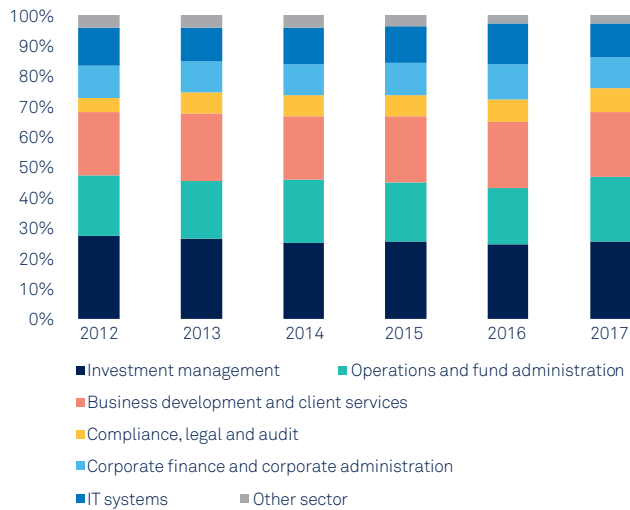
**TABLE 5: DISTRIBUTION OF STAFF BY ACTIVITY (DIRECT EMPLOYMENT)**

Activity	Percentage of total headcount
<b>Investment Management of which</b>	<b>25%</b>
Investment management (asset allocation and stock selection)	69%
Research, analysis	24%
Dealing	7%
<b>Operations and Fund Administration of which</b>	<b>20%</b>
Investment transaction processing, settlement, asset servicing	35%
Investment accounting, performance measurement, client reporting	40%
Other fund administration (incl. CIS transfer agency, ISA administration etc.)	25%
<b>Business Development and Client Services of which</b>	<b>21%</b>
Marketing, sales, business development	69%
Client services	31%
<b>Compliance, Legal and Audit of which</b>	<b>8%</b>
Compliance	34%
Risk	36%
Legal	22%
Internal audit	7%
<b>Corporate Finance and Corporate Administration of which</b>	<b>11%</b>
Corporate finance	40%
HR, training	25%
Other corporate administration	35%
<b>IT Systems</b>	<b>12%</b>
<b>Other Sector</b>	<b>4%</b>

Over the longer term some trends in staffing levels do emerge. On a like-for-like basis over the last five years, Chart 81 and Table 6 show the following changes:

- Investment management accounts for a slightly smaller proportion of total employment (25% from 27% in 2012), although overall numbers have risen.
- Operations and fund administration roles have also seen a two percentage point fall (18%). Again, overall numbers have grown.
- In stark contrast, the levels of staffing in compliance, legal and audit have increased by three percentage points. In absolute terms, the number of people employed have more than doubled since 2012. (see Table 6).

**CHART 81: DIRECT EMPLOYMENT BY STAFF SEGMENT (2012-2017)**



**TABLE 6: ESTIMATED NUMBERS OF STAFF EMPLOYED BY ACTIVITY (DIRECT EMPLOYMENT)**

	2012	2013	2014	2015	2016	2017
Investment management	8,300	8,300	8,700	9,300	9,300	9,600
Operations and fund administration	6,200	6,000	7,400	7,300	7,000	8,200
Business development and client services	6,400	7,200	7,400	8,000	8,200	8,100
Compliance, legal and audit	1,400	2,100	2,400	2,600	2,700	2,900
Corporate finance and corporate administration	3,300	3,300	3,500	4,000	800	3,800
IT systems	3,900	3,600	4,200	4,500	4,500	4,300
Other sector	1,400	1,400	1,600	1,300	5,200	1,000

Table 7 shows that the type of activity undertaken in different locations differs widely:

- London is the main centre of asset management activity and business development.
- Operations activities and finance are more important outside of London. There is a marked contrast with Scotland in this regard, also seen in IT roles.



**TABLE 7: DISTRIBUTION OF ASSET MANAGEMENT JOBS BY REGION**

	London	Scotland	Elsewhere in the UK
<b>Investment Management of which</b>	<b>28%</b>	<b>20%</b>	<b>12%</b>
Investment management (asset allocation and stock selection)	67%	75%	86%
Research, analysis	26%	18%	13%
Dealing	7%	7%	1%
<b>Operations and Fund Administration of which</b>	<b>16%</b>	<b>29%</b>	<b>34%</b>
Investment transaction processing, settlement, asset servicing	44%	17%	22%
Investment accounting, performance measurement, client reporting	39%	53%	21%
Other fund administration (incl. CIS transfer agency, ISA administration etc.)	17%	29%	57%
<b>Business Development and Client Services of which</b>	<b>22%</b>	<b>15%</b>	<b>19%</b>
Marketing, sales, business development	72%	56%	79%
Client services	28%	44%	21%
<b>Compliance, Legal and Audit of which</b>	<b>9%</b>	<b>6%</b>	<b>9%</b>
Compliance	35%	31%	42%
Risk	34%	45%	40%
Legal	25%	16%	12%
Internal audit	7%	8%	5%
<b>Corporate Finance and Corporate Administration of which</b>	<b>10%</b>	<b>12%</b>	<b>13%</b>
Corporate finance	37%	47%	50%
HR, training	26%	26%	11%
Other corporate administration	37%	27%	39%
<b>IT Systems</b>	<b>10%</b>	<b>16%</b>	<b>11%</b>
<b>Other</b>	<b>5%</b>	<b>2%</b>	<b>2%</b>

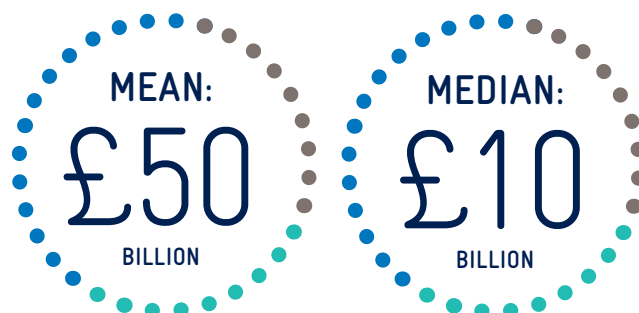
## INDUSTRY CONCENTRATION

Chart 82 illustrates that the asset management industry in the UK continues to comprise a small number of very large firms but a long tail of medium- and small-sized organisations.

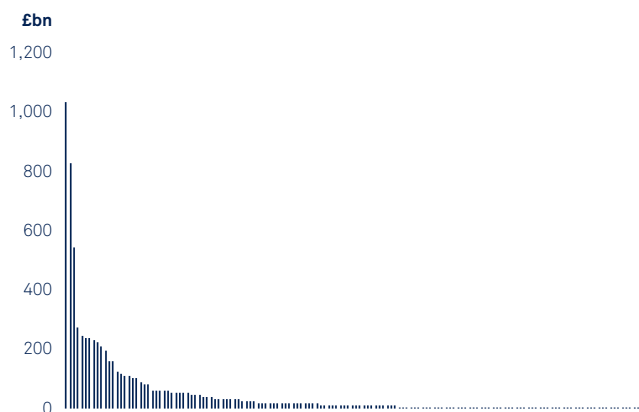
This has historically been the pattern within an industry that has been characterised by a diversity of operating models and comparatively low barriers to entry. As discussed in Chapter 2, there is an expectation that in the future the industry may well see greater focus on larger managers. These would be able to use scale to their advantage and offer a full suite of investment products and perhaps even operate via a more vertically integrated business model, alongside a range of boutique managers offering specialist expertise (see page 92).

“THE MARKET WILL CONTINUE TO BECOME POLARISED. YOU ARE STILL GOING TO HAVE ALL THE SMALL BOUTIQUES AT ONE END, BUT IT’S THE MIDDLE GROUND WHERE YOU ARE GOING TO SEE FEWER AND FEWER PLAYERS AS THEY JUST WON’T BE ABLE TO COMPETE.”

## AVERAGE ASSETS UNDER MANAGEMENT AT JUNE 2017



**CHART 82: IA MEMBER FIRMS RANKED BY UK ASSETS UNDER MANAGEMENT (JUNE 2017)**



This expectation seems to be confirmed by what we observe in the distribution of member firms by the level of assets they have under management. Looking at the data for the last five years there has been a steady increase in the number of large firms with more than £100 billion under management (see Table 8).

Continuing M&A activity among asset management firms is entirely consistent with the increase in the number of larger firms that is evident from IA data (see Table 8).

At the same time, the number of firms with under £1 billion under management has also increased quite significantly. Although there have been anecdotal concerns around barriers to entry in recent years, some amongst those interviewed pointed out the continued activity in this space.

“THERE IS STILL ROOM FOR SMALL BOUTIQUE FIRMS, PROVIDED THEY ARE NIMBLE AND HAVE A LOW COST BASE.”



There was no particular concern that the hurdles for entering the market would restrict the setup of new boutiques as the process for boutique creation was seen to be a natural product of the talent-based focus of the investment management industry. Successful portfolio managers building a reputation with larger firms but then desiring more control over their own investment strategies was expected to continue.

**TABLE 8: ASSETS MANAGED IN THE UK BY IA MEMBERS BY FIRM SIZE**

AUM	No. of firms (June 2017)	No. of firms (June 2016)	No. of firms (June 2015)	No. of firms (June 2014)	No. of firms (June 2013)
>£100bn	18	15	13	11	12
£50-100bn	13	13	14	14	15
£25-50bn	14	15	13	14	13
£15-25bn	14	11	13	14	14
£1-15bn	69	70	68	70	69
<£1bn	19	14	15	22	18
<b>Total</b>	<b>147</b>	<b>138</b>	<b>136</b>	<b>145</b>	<b>141</b>

“THE REGULATORY ENVIRONMENT IS TOUGHER BUT WHERE SOMEBODY CREATES SOMETHING INTERESTING, DIFFERENTIATED AND INNOVATIVE, AND THEY HAVE PERFORMANCE, THEY’LL FIND BACKING TO BE ABLE TO BUILD THE BUSINESS.”



Another explanation for the growth in smaller firms could be that it partly reflects an expansion of IA membership among small firms. This category accounts for 50% of the increase in IA members between June 2016 and June 2017.

Nevertheless the UK asset management industry remains relatively unconcentrated. The five largest firms represent 43% of assets, up three percentage points from 2016, and the ten largest firms represent 58% of industry assets, slightly up from 2016, largely as a result of merger and acquisition activity. A figure of less than 1,000 on the Herfindahl-Hirschmann Index, a standard measure of competition, represents low concentration. The value for the asset management industry stands at just above 500 (see Chart 83)

**CHART 83: MARKET SHARE OF LARGEST FIRMS BY UK ASSETS UNDER MANAGEMENT VS. HHI (JUNE 2008-2017)**

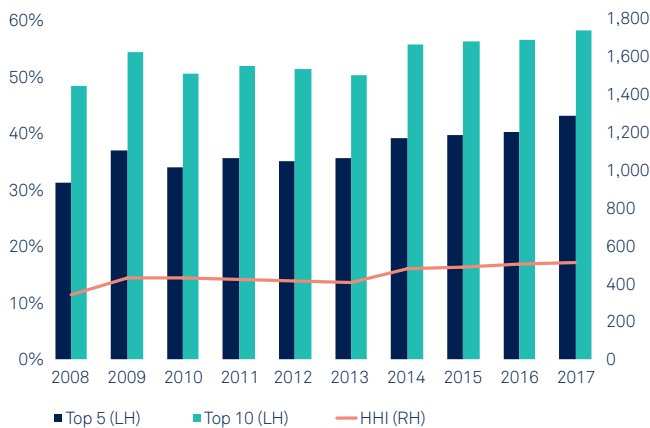
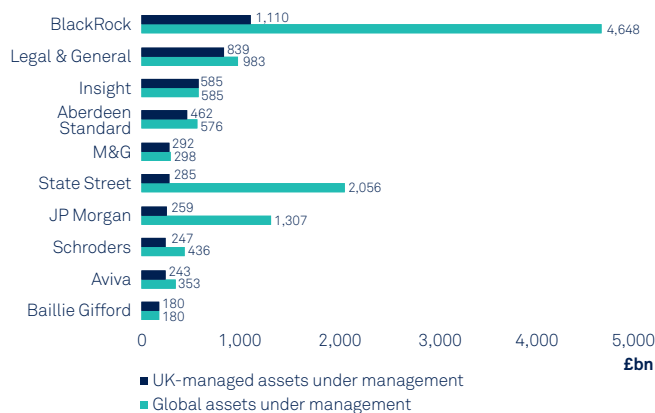


Chart 84 shows the ten largest firms in the UK, measured by UK assets under management supplied to the IA in response to the Survey questionnaire. The top ten includes a mix of active and passive managers. There is also a wide variety of group types in the top ten, including independent asset managers, as well as managers that are part of a larger insurance group, or bank. Unsurprisingly, with institutional clients representing around 80% of assets under management in the UK, the assets of the top ten managers are dominated by institutional client assets.

As the difference between UK and global assets shows, a number of the largest asset managers are primarily UK focused, whereas others have a much wider global footprint

**CHART 84: TOP TEN FIRMS BY UK-MANAGED AND GLOBAL ASSETS UNDER MANAGEMENT<sup>64</sup>**



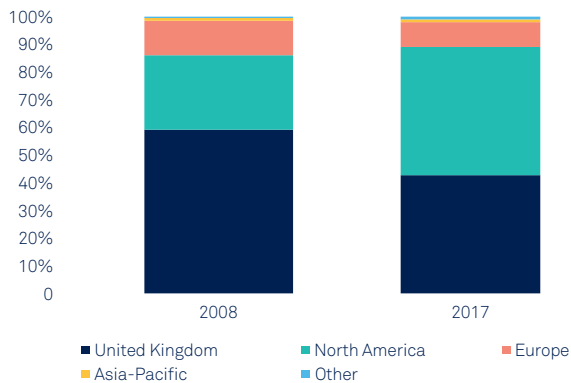
<sup>64</sup> Assets under management figures may reflect the value of wider economic exposure managed for clients in addition to securities within segregated or pooled portfolios.

## ASSET MANAGER OWNERSHIP

Compared to a decade ago, significantly more assets are managed in the UK by organisations headquartered overseas, especially in the US. This has changed from 41% in 2008 to 57% in 2017. Despite the ongoing high levels of merger and acquisition activity, Chart 85 shows there has been little change on the geographic breakdown of ownership in the last three years:

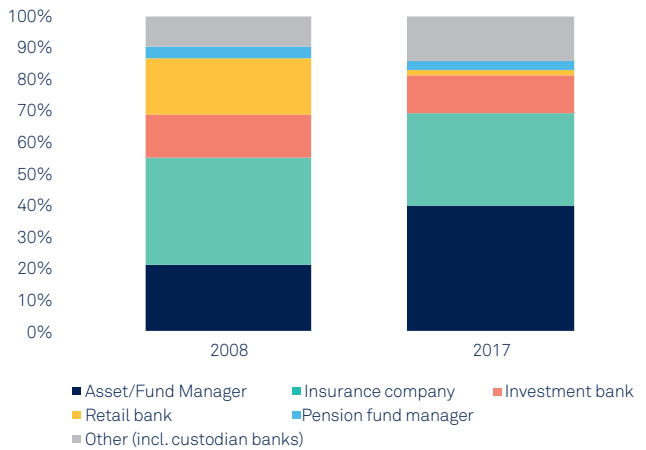
- UK-owned asset managers now account for 43% of assets managed in the UK.
- The proportion of assets managed in the UK for US-owned asset managers stands at 46%.
- Assets managed by European-owned firms remain at a relatively low proportion of total assets managed in the UK, at around 9%.

**CHART 85: ASSETS UNDER MANAGEMENT BY REGION OF PARENT GROUP HEADQUARTERS (2008-2017)**



At the same time, a structural shift has occurred in the ownership of asset management companies. Chart 86 illustrates the number of independent asset managers now stands at 40%, which is similar to 2015 but markedly up from 18% ten years ago. This relates to the M&A activity discussed in more detail in Chapter Two

**CHART 86: BREAKDOWN OF UK ASSETS UNDER MANAGEMENT BY PARENT TYPE (2008-2017)**



## BOUTIQUES

The IA membership contains a number of boutique managers. The definition of a boutique firm is not based purely on the size of the firm. There are four broad criteria:

- Being independently owned
- Managing assets of less than £5.5 billion<sup>65</sup>
- Providing a degree of investment specialisation
- Self definition.

According to these criteria the number of boutiques within the IA membership increased from 21 in 2016 to 22 in 2017. Although the number of firms remained almost unchanged the individual firms categorised as boutique changed due to two main influencing factors:

- Some boutique firms increased in size such that they no longer classified.
- The membership of the IA increased during 2017 and a number of new IA members fell into the boutique category.

<sup>65</sup> Increased after 2013 from £5bn in line with overall asset growth.

# APPENDICES

# APPENDIX 1

## SUMMARY OF ASSETS UNDER MANAGEMENT IN THE UK<sup>1</sup>

	TOTAL
<b>Assets under management in the UK (£m)</b>	<b>7,702,427</b>
<b>Segregated or pooled (%)</b>	
Directly invested on a segregated basis	56.1%
Managed on a pooled basis	43.9%
<b>Active or passive (%)</b>	
Actively managed	73.6%
Passively managed	26.4%
<b>Asset allocation (%)</b>	
<b>Equities of which:</b>	<b>39.9%</b>
UK	29.6%
Europe (ex UK)	24.3%
North America	19.4%
Pacific (ex Japan)	7.9%
Japan	6.8%
Latin America	1.2%
Africa	0.5%
Emerging market	6.4%
Other	3.8%
<b>Fixed Income of which:<sup>2</sup></b>	<b>31.6%</b>
UK Government (ex index-linked)	20.0%
Sterling corporate	20.1%
UK index-linked	10.0%
Other UK	8.0%
Overseas	41.9%
<b>Cash/Money market</b>	<b>5.3%</b>
<b>Property</b>	<b>2.4%</b>
<b>Other</b>	<b>20.7%</b>

<sup>1</sup> This includes all assets under management in this country, regardless of where clients or funds are domiciled.

INSTITUTIONAL								ALL INSTITUTIONAL	RETAIL	PRIVATE CLIENT
Pension funds	Public sector	Corporate	Non-profit	Sub- advisory	In-house insurance	Third party insurance	Other institu- tional			
3,376,486	344,060	355,843	98,751	286,915	642,051	516,891	450,544	6,071,542	1,478,283	152,600
43.8%	4.5%	4.6%	1.3%	3.7%	8.3%	6.7%	5.8%	78.8%	19.2%	2.0%

## APPENDIX 2

# SUMMARY OF DATA FROM THE UK INSTITUTIONAL CLIENT MARKET<sup>2</sup>

	<b>TOTAL</b>
<b>Total Institutional Market (£m)</b>	<b>3,828,656</b>
<b>Segregated or pooled institutional assets (%)</b>	
Assets directly invested on a segregated basis	69.2%
Assets managed on a pooled basis	30.8%
<b>Active or passive (%)</b>	
Actively managed	71.7%
Passively managed	28.3%
<b>Multi-asset, LDI or Specialist (%)</b>	
<b>Multi-asset</b>	<b>17.0%</b>
<b>LDI (notional)</b>	<b>28.8%</b>
<b>Single-asset / specialist of which:</b>	<b>54.2%</b>
<b>Equities of which:</b>	
UK	29.8%
European (ex UK)	5.7%
North American	6.4%
Asia Pacific	2.7%
Japan	2.2%
Latin America	0.0%
Africa	0.0%
Emerging Market	3.5%
Global	45.0%
Other	4.8%
<b>Fixed Income of which:</b>	
Sterling Corporate	20.7%
Sterling Corporate and Government	7.2%
UK Government	13.6%
UK Index-linked	9.2%
Global	32.9%
Other	16.4%
<b>Cash/Money Market</b>	<b>6.8%</b>
<b>Property</b>	<b>6.3%</b>
<b>Other</b>	<b>9.4%</b>

<sup>2</sup> This includes UK institutional client mandates, regardless of where assets are managed.



	Pension funds			Public sector	Corporate	Non-profit	Sub-advisory	In-house insurance	Third party insurance	Other institutional
	Corporate	Local government	Other							
	2,066,373	240,567	95,110	28,039	91,303	48,440	108,779	525,865	438,844	185,337
	54.0%	6.3%	2.5%	0.7%	2.4%	1.3%	2.8%	13.7%	11.5%	4.8%
	72.1%	46.8%	37.0%	79.2%	58.8%	57.7%	86.2%	98.5%	56.5%	35.6%
	27.9%	53.2%	63.0%	20.8%	41.2%	42.3%	13.8%	1.5%	43.5%	64.4%
	63.6%	69.2%	47.4%	95.1%	72.9%	80.9%	70.4%	95.0%	91.3%	59.0%
	36.4%	30.8%	52.6%	4.9%	27.1%	19.1%	29.6%	5.0%	8.7%	41.0%
	<b>9.3%</b>	<b>9.3%</b>	<b>16.6%</b>	<b>7.0%</b>	<b>11.4%</b>	<b>43.8%</b>	<b>13.1%</b>	<b>22.7%</b>	<b>51.9%</b>	<b>9.8%</b>
	<b>49.5%</b>	<b>4.4%</b>	<b>33.9%</b>	<b>34.2%</b>	<b>0.0%</b>	<b>1.2%</b>	<b>1.8%</b>	<b>0.0%</b>	<b>1.1%</b>	<b>9.7%</b>
	<b>41.2%</b>	<b>86.2%</b>	<b>49.6%</b>	<b>58.7%</b>	<b>88.5%</b>	<b>55.0%</b>	<b>85.1%</b>	<b>77.2%</b>	<b>47.0%</b>	<b>80.5%</b>
	<b>36.3%</b>	<b>61.7%</b>	<b>66.4%</b>	<b>16.1%</b>	<b>37.0%</b>	<b>61.8%</b>	<b>61.6%</b>	<b>23.8%</b>	<b>18.7%</b>	<b>36.1%</b>
	19.9%	26.4%	10.4%	8.5%	18.4%	22.6%	23.8%	75.1%	26.8%	37.4%
	5.5%	7.4%	3.6%	38.7%	21.0%	2.0%	6.7%	1.6%	5.7%	3.7%
	5.9%	9.6%	6.7%	3.6%	8.1%	1.3%	8.8%	3.4%	7.5%	4.4%
	2.2%	2.2%	2.1%	0.3%	0.6%	0.3%	3.1%	1.4%	5.4%	8.7%
	1.6%	2.8%	2.7%	0.4%	3.2%	0.4%	2.4%	1.7%	3.0%	3.9%
	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.2%	0.0%	0.0%
	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	4.0%	3.0%	5.7%	11.2%	5.2%	3.8%	2.5%	1.0%	3.8%	4.4%
	55.4%	45.0%	68.8%	37.3%	43.4%	62.7%	50.9%	14.7%	20.2%	35.7%
	5.4%	3.5%	0.0%	0.0%	0.1%	6.9%	1.8%	0.8%	27.6%	1.9%
	<b>43.4%</b>	<b>23.0%</b>	<b>23.2%</b>	<b>43.9%</b>	<b>21.7%</b>	<b>8.5%</b>	<b>31.1%</b>	<b>56.7%</b>	<b>58.1%</b>	<b>11.4%</b>
	23.1%	16.4%	38.9%	0.8%	10.6%	28.2%	13.7%	19.1%	22.5%	0.3%
	9.0%	9.0%	3.0%	1.4%	3.2%	35.3%	5.0%	3.5%	8.2%	2.3%
	15.4%	9.5%	9.2%	0.2%	4.7%	9.9%	5.9%	13.8%	8.1%	50.3%
	11.7%	25.3%	26.0%	2.8%	0.9%	2.9%	10.8%	5.6%	0.7%	2.6%
	32.0%	28.4%	18.6%	86.8%	33.6%	19.6%	45.0%	49.1%	16.4%	2.7%
	8.7%	11.4%	4.2%	8.0%	46.9%	4.1%	19.7%	9.0%	44.1%	41.7%
	<b>2.8%</b>	<b>0.9%</b>	<b>0.9%</b>	<b>19.6%</b>	<b>21.8%</b>	<b>17.3%</b>	<b>2.9%</b>	<b>5.2%</b>	<b>5.1%</b>	<b>37.9%</b>
	<b>4.8%</b>	<b>6.4%</b>	<b>2.9%</b>	<b>10.6%</b>	<b>13.9%</b>	<b>3.3%</b>	<b>0.3%</b>	<b>11.0%</b>	<b>3.4%</b>	<b>7.3%</b>
	<b>12.7%</b>	<b>7.9%</b>	<b>6.6%</b>	<b>9.7%</b>	<b>5.6%</b>	<b>9.1%</b>	<b>4.0%</b>	<b>3.3%</b>	<b>14.7%</b>	<b>7.3%</b>

## APPENDIX 3

# MAJOR UK AND EU REGULATORY DEVELOPMENTS AFFECTING ASSET MANAGEMENT IN THE UK

### CAPITAL MARKETS AND INVESTMENT

#### CSDR

- The Central Securities Depositories Regulation was adopted in September 2014, seeking to harmonise the regulation and supervision of Central Securities Depositories in Europe and harmonise securities settlement practices.
- The initial measure was to impose a maximum settlement cycle of T+2 for trades executed on-exchange in Europe. This was adopted by most markets in October 2014, ahead of the mandated change in January 2015.
- CSDR will also impose a more harmonised settlement discipline regime, including mandatory buy-ins where trades do not complete within a short period after the intended settlement date and the imposition of financial penalties on those that cause settlement delays.
- The technical standards for the settlement discipline regime were adopted by the European Commission in May 2018 and, absent any objections from the European Parliament and Council, will apply from Q3 2020.

#### MiFID II

- MiFID II became effective on 3 January 2018.
- **Client Reporting**  
Firms are in the process of implementing the new obligations, setting out how, and how frequently, firms should report to their clients. The first monthly and quarterly reports will have been sent to clients but firms may not yet have sent out the first annual reports. There is considerably more detail set out in MiFID II, and less flexibility in differentiating between professional and retail clients.
- **Charge and cost disclosure (C&C)**  
MiFID II introduces a paradigm shift in this area. All portfolio transaction costs (implicit and explicit) are included. All product, distribution and advice costs are presented in an aggregated way.
- **Best Execution**  
MiFID II requires firms to publish extensive information on where they execute trades and details of the quality of execution achieved. This represents a significant data gathering exercise, including obtaining information published by venues, which must then be analysed and used by asset managers. Firms have published their first set of these reports, but it is recognised by ESMA that these may lack the granularity and detail that future reports should include.
- **Research**  
MiFID II has introduced a structural change in the way that asset managers acquire research. MiFID II requires, among other things, that there is a clear and demonstrable demarcation between the payment for execution and payment for research. There are also significant obligations on related issues such as corporate access.
  - Under the SEC Securities Exchange Act section 206(3), US brokers cannot receive direct payment for research unless they register as an Investment Advisor in the US. Registering as an Investment Advisor is problematic for brokers as it places restrictions on their ability to trade on a principal basis and creates a fiduciary duty to act in the best interests of their clients. The SEC issued no action relief for MiFID II business to deal with the clash of regimes.
  - This relief is time limited to 24 months from January 2017. Once this relief runs out, further action will need to be taken by the SEC to allow MiFID II business to continue.

- **Transparency**

MiFID II brings enhanced transparency requirements in both the equities and fixed income world. In addition it provides a Europe-wide standard definition of spot FX v financial instruments.

- The double volume cap (DVC) limits trading in the dark for equities across Europe.
- Bonds which are determined to be 'liquid' by ESMA have additional transparency obligations.

- **Trading Obligations**

The trading obligation for both equities and derivatives will potentially have an impact on asset managers. It requires that instruments listed in the EU are traded on an EU trading venue.

- **Product Governance**

The MiFID II rules are two dimensional. They aim at product development and oversight on the one hand and closer oversight of distribution of financial instruments to ensure robust investor protection throughout the supply chain on the other

**SFTR**

- The Securities Financing Transactions Regulation has applied since January 2016, but will also impose a trade reporting regime. The European Commission has stated it intends to endorse the technical standards for this but will amend certain details ahead of go-live in Q1 2020.

## FUNDS AND DISTRIBUTION

**Sunset for legacy commission payments**

- On 5 April 2018 the FCA confirmed in Policy Statement PS18/8 on the implementation of the market study remedies that, while it would continue to consider the question of trail commission, it did not intend to make any further changes at this stage.
- The FCA had previously decided not to impose a sunset clause in relation to the grandfathering of ongoing commission payments to advisers for undisturbed business written before the adviser charging rules came into force on 1 January 2013.
- While a 6 April 2016 sunset clause that affected all provider payments to platform service providers meant that the payment of commission to advisers through platforms would end at that date, commission on legacy business that is paid directly by the provider to the adviser was not addressed.
- The FCA Market Study interim and final reports indicated the FCA were not intending to introduce a sunset clause for legacy commission payments to advisers, but would instead explore other options for increasing consumer awareness of these.

**Packaged Retail and Insurance-based Investment Products (PRIIPs)**

- Following a delay, the PRIIPs regulation was applied on 1 January 2018. The new PRIIP Key Information Document (KID) provides a range of information including costs, risk and performance scenarios. The methodologies have been controversial and in July 2018, the FCA launched a call for input on initial experiences.
- UCITS, and AIFs where national regulators have extended the UCITS KII requirements (as the FCA has on a voluntary basis for NURS), are exempt from the PRIIPs Regulation until December 2019.
- However, if other PRIIP providers (such as insurers) are using UCITS or NURS, they will require information about the product from manufacturers that are compatible with the PRIIPs regulation.

**AIFMD**

- The Commission has commenced its review on AIFMD by commissioning KPMG to prepare a report on the effectiveness of the AIFMD implementation, to be completed by October 2018.
- The Directive and related Regulation has applied since 22 July 2013. It captures a wide range of UK vehicles, including NURs, QISs, unauthorised unit trusts (UUTs), charity funds, investment trusts, and specialist vehicles (e.g. hedge funds, private equity funds, venture capital funds and real estate funds).
- It provides a passport for the marketing of AIFs to professional investors and imposes detailed regulation on the managers of AIFs (AIFMs).
- ESMA has been working on identifying third countries which should be deemed to be sufficiently equivalent that the AIFMD passporting regime should be extended to them. In 2016 they submitted advice to the Commission regarding 12 third countries, however the Commission has yet to publish its proposals. This process has proven politically contentious and may be further impacted by the Brexit negotiations.

**Venture Capital Funds and Social Entrepreneurship Funds**

- Changes to the EuVECA and EuSEF regulations were agreed by the Council and the European Parliament in 2017 and came into force in March 2018.
- The EuSEF (European Social Entrepreneurship Funds) and EuVECA (European Venture Capital Funds) Regulations, approved in March 2013, created labels or “designations” for small AIFMs and internally managed AIFs that comply with the organisational requirements and investment rules.
- The regimes created a passport enabling registered managers to market their EuVECA and EuSEF to professional and “semi-professional” investors throughout the EEA.
- There has been a reasonable take up of the EuVECA label, with 70 EuVECA funds being notified to ESMA to date. However, the EuSEF label has achieved little success to date, with only four EuSEF funds having been notified to ESMA.
- On 14 July 2016, the Commission published a proposal to amend the EuVECA and EuSEF regulations intended to improve the take up of these funds. This followed a public consultation issued in September 2015.
- The Commission proposes changes to the EuVECA and EuSEF regulations to extend the range of managers eligible to market and manage EuVECA and EuSEF funds, increase the range of companies that EuVECA funds can invest in, and make cross-border registration and marketing of these funds easier and cheaper.

**Money Market Funds**

- Commission proposals for Money Market Funds (MMFs) were issued in September 2013 and political agreement was reached on the text in November 2016. The text has now been formally adopted and came into force on 21 July 2018. Existing MMFs must submit their applications for authorisation under the MMFR by 21 January 2019.
- The Regulation provides for both Variable Net Asset Value (VNAV) and Constant Net Asset Value (CNAV) MMFs. Two designs of CNAVs are provided for, Low Volatility Net Asset Value MMFs (LVNAV), and Public Debt CNAVs.
- The final Regulation also includes transparency requirements to ensure all MMF investors are aware of risks that may result in MMFs being revalued, restrictions on eligible assets, diversification and concentration limits, prohibitions on external support (eg. from a parent bank), requirements on MMFs to calculate their NAV on a daily basis and requirements for LVNAVs and CNAVs to have liquidity fees and redemption gates available for use in stressed periods.

- ESMA issued a consultation in May 2017 covering various Level 2 and 3 measures and issued its final report in November 2017.

- In January 2018, the Commission wrote to ESMA stating its opinion that the Reverse Distribution Mechanism (RDM) was not compatible with the MMFR. The RDM is used by many existing constant NAV MMFs, which will convert either to LVNAV MMFs or Public Debt CANV MMFs, to reflect negative yields in currencies such as the Euro or the Japanese Yen while maintaining a constant net asset value. Discussions on the opinion are ongoing. If upheld, the opinion could cause difficulties for LVNAV MMFs and Public Debt CNAV MMFs in negative yield currencies.

- The US Securities and Exchanges Commission (SEC) adopted new Money Market Funds Reform rules on 23 July 2014. The new rules require a floating net asset value (NAV) for institutional prime money market funds and introduce contemporaneous changes to accounting and tax rules to make the shift work.

#### **Local Government Pension Scheme (LGPS)**

- LGPS pooling reforms have been continuing with all eight pools now operational and assets beginning to be transferred into the pools.
- Under MiFID II LGPS clients are classified as retail investors but can elect to opt up to professional investor status following the completion of an opt-up test, set out in FCA rules and conducted by the client's investment manager. All English and Welsh funds have opted up with existing managers under the new rules. Notably, when entering a relationship with a new manager each LGPS client is considered a retail investor for the purposes of that relationship, regardless of whether they have successfully opted up with another manager. Asset managers have continued to sign up to the LGPS in its Code of Transparency, launched in May 2017. This has been designed to help the LGPS measure its investment costs (fees and transaction costs) on a consistent basis across individual funds.

#### **DC pensions charge cap review**

- Following a review in 2017 the Department for Work and Pensions announced in November 2017 that it would make no change to the level or scope of the charge cap on DC workplace pension default strategies for the time being. The DWP will re-visit this decision in 2020 and will consider whether the current cap of 75bps should be lowered and/or whether it should include some or all transaction costs.

#### **Pan-European Personal Pension (PEPP)**

- In June 2017 the European Commission released a draft regulation for the introduction of a Pan European Personal Pension (PEPP) product across the EU.
- The PEPP is a voluntary personal pension scheme that will offer consumers a new option to save for retirement. It could be offered by a broad range of providers including insurance companies, banks, occupational pension funds, certain investment firms and asset managers.
- The draft regulation covers areas such as product authorisation, design, distribution and disclosure.
- Following the publication of the Commission proposal the draft regulation has been subject to debate within the European Parliament and Council. The trilogue process begins in Autumn 2018 and it is unclear as to when the regulation will come into force.

#### **FCA Retirement Outcomes Review**

- The final report of the Retirement Outcomes Review was published on 28 June 2018.
- The review looked at how the retirement income market was evolving following the introduction of the pensions freedoms in April 2015. The findings focus on non-advised customers purchasing income drawdown products.

- There are weak competitive pressures and low levels of switching. Most consumers choose the 'path of least resistance', accepting drawdown from their current pension provider without shopping around.
- One in three consumers who have gone into drawdown recently are unaware of where their money was invested.
- Some providers were 'defaulting' consumers into cash or cash-like assets, but holding cash is highly unlikely to be suited for someone planning to draw down their pension over a longer period.
- The FCA considers that consumers might pay too much in charges. It found that charges for non-advised consumers vary considerably from 40bps to 160bps between providers, and are, on average, higher than the 75bps charge cap on DC default investment strategies.
- Drawdown charges can be complex, opaque and hard to compare.
- There is no evidence thus far of significant product innovation for mass-market consumers.
- The FCA has proposed a number of remedies around improving the effectiveness of communications prior to consumers accessing their pension savings, nudging consumers to make an active choice over how to access their pension and on the information to be sent to consumers once they are in drawdown.
- The FCA has left open the option to introduce a charge cap but chosen not to do so at this point.

## FIRM REGULATION

### FCA Market Study

The Final Report of the FCA Asset Management Market Study (AMMS) was published in June 2017 with the main conclusion being that there is weak price competition in a number of areas of the asset management industry and specifically for retail active management services. To address this, the FCA proposed three sets of remedies:

#### • **Enhanced consumer protection**

- **A new fund governance regime.** Following consultation in the summer of 2017, new requirements were introduced in 2018 for authorised fund managers to assess and report on value delivered using criteria that among others include performance, quality of service, level of charges, and economies of scale. Notably, these criteria are closely aligned with the Gartenberg factors that are considered as part of the 15(c) process for US funds.
- **Box management.** New rules will no longer allow firms to retain risk-free box profits but flexibility in determining how these profits are distributed to clients will be permitted.
- **Legacy share classes.** New guidance was introduced to facilitate mandatory conversions by making the process less onerous. Namely, investors will now need to be given a simple, one-off notification with at least 60 days' notice, which will not require a response.

---

- **Driving competitive pressure on asset managers**

---

- **Disclosure of costs and charges in the retail market.** The FCA has decided to implement MiFID II disclosure requirements rather than introduce a structural change in the way charges are taken from the fund. Further consideration of the way in which the effect of charges is communicated is given as part of the Investment Platforms Market Study.
  - **Standardised disclosure of costs and charges to institutional investors.** The FCA formed the independently chaired Institutional Disclosure Working Group (IDWG) in September 2017 which published a summary of its recommendations in July 2018. The recommendations include a proposal to use a suite of templates for collecting and reporting cost data and the formation of a new group to curate and update the templates. The FCA is working with interested bodies with a view to announcing the new group in the autumn of 2018.
  - **Clarity and usefulness of investment objectives.** The FCA convened and chaired the Fund Objectives Working Group (FOWG) to discuss how greater clarity of language could be developed in the expression of investment objectives, policy and strategy in fund products. New guidance on disclosure of fund objectives and rules on the use of benchmarks were proposed as part of Consultation Paper CP18/19 in April 2018.
- 

- **Improving the effectiveness of intermediaries**

---

- **Investment Platform Market Study (IPMS).** The IPMS was launched in July 2017 as a separate market study, aiming to address the effectiveness of intermediaries in the retail space. The interim report published on 16 July 2018 concluded that the market works well in many respects but not when it comes to a number of specific areas, notably: shopping around and switching between platforms; clarity of language in model portfolios; investors holding large amounts of cash on platforms; and 'orphan clients' that pay for an ongoing advice service but no longer receive advice.
  - **CMA Investigation.** This investigation looks to address the effectiveness of intermediaries in the institutional space. The CMA published its Provisional Decision Report on 18 July 2018. Findings included a weak demand side, with trustees relying heavily on investment consultants but having limited ability to assess their services, relatively low levels of concentration in both investment consultancy and fiduciary management, although the latter was at risk of greater concentration in future, barriers to expansion restricting new consultants developing their business and vertically integrated models creating conflicts of interest. The CMA proposed a number of supply and demand side remedies, as well as an overarching remedy to recommend to government that the scope of the FCA's regulatory perimeter be extended to include relevant services provided by investment consultancy and fiduciary management.
- 

**Senior Managers & Certification Regime (SMCR)**

- SMCR had already implemented in banks and building societies from March 2016 and with Consultation Paper CP17/25 the FCA extended it to all solo-regulated firms. Near final rules were introduced with Policy Statement PS18/14.
  - Key new requirements for asset management firms, planned for implementation in late 2019 include:
    - Senior Managers Regime replacing the Significant Influence Function, with senior managers individually responsible and accountable for every area of a firm's activities, and approved by FCA.
    - Certification Regime that applies to employees who could pose a risk of significant harm to the firm or any of its customers approved internally by firms.
    - Set of conduct rules that apply to almost all other staff.
-

<b>General Data Protection Regulation (GDPR)</b>	<ul style="list-style-type: none"> <li>GDPR came into effect on 25 May 2018. It is directly applicable in all Member States without the need for implementing national legislation.</li> </ul>
<b>Fifth Money Laundering Directive</b>	<ul style="list-style-type: none"> <li>The Level One text has been finalised. The Directive, which amends and extends the Fourth Money Laundering Directive, is scheduled to apply from 10 January 2020.</li> <li>The implementing regulations are awaited.</li> <li>The HMT Money Laundering Regulation will need to be amended, consulted on and implemented.</li> <li>The JMLSG Guidance will need to be consulted on, the final version will depend on any changes to the HMT Regulation following consultation.</li> </ul>
<b>EU Benchmark Regulation</b>	<ul style="list-style-type: none"> <li>Benchmark producers will have until the end of 2019 to ensure that they are registered or authorised. To date, the FCA is the only authority to have authorised or registered any providers.</li> <li>While the Level One and most of the Level Two text is now published, one piece awaits finalisation, the delegated action conditions for objective reasons for endorsement of third country benchmarks. This is not expected until late 2018.</li> <li>Firms should have identified all the indices that they use (as defined in the Regulation) as benchmarks for their funds, and continue to work to ensure that these will be available to them when the Regulation comes in to force.</li> </ul>
<b>Enhanced transparency of charges and costs</b>	<ul style="list-style-type: none"> <li>Requirements under MiFID II, PRIIPs and UK pensions law will lead to enhanced disclosure of investment charges and transaction costs across all client segments of the asset management industry.</li> </ul>



## APPENDIX 4

## NOTABLE M&amp;A DEALS IN THE UK ASSET MANAGEMENT SECTOR (2009-JUNE 2018)

## 2017-2018

ACQUIRER	PURCHASE
Amundi Group	Pioneer Investments
BlackRock	Cachematrix Holdings First Reserve Energy Infrastructure Funds Scalable Capital (minority stake)
BNP Paribas Asset Management	Gambit Financial Solutions (majority stake)
Brewin Dolphin	Duncan Lawrie Asset Management
Canada Life Group (UK)	Retirement Advantage
Candriam	Tristan Capital Partners (strategic partnership)
Close Brothers	Adrian Smith and Partners
Crux Asset Management	Oriel Global and European funds from City Financial
Federated Investors	Hermes Investment Management (majority stake)
Franklin Templeton	Edinburgh Partners
FundRock	Fund Partners
Impax Asset Management	Pax World Management LLC
LGIM	Canvas
Link Group	Capita Asset Services
Lovell Minnick Partners/ Existing Management Team	BNY Mellon Investment Management (CentreSquare Investment Management Real Asset Boutique)
Natixis Global Asset Management	Investors Mutual Ltd
Nikko Asset Management	ARK Investment Management (minority stake)
Nomura Asset Management	8 Securities (majority stake)
Principal Global Investors	Internos Global Investors
RWC	Pensato Capital
Sandaire	Joint venture with Delancey
Schroders	Adveq Holdings AG Alonquin
SJP	HJP Independent Financial Advisers
Standard Life Investments	Aberdeen Asset Management (merger)
Stonehage Fleming	OmniArte
Swiss Re	L&G mature savings business
TA Associates	Old Mutual Global Investors (single strategy funds)
Thesis Asset Management	Cambridge Fund Managers

## 2016

ACQUIRER	PURCHASE
Aberdeen	Arden Asset Management, Parmenion Capital,
Aegon	Cofunds
AJ Bell	Indexx Markets Ltd, Allium Capital
Alliance Bernstein	Ramius Alternative Solutions
Allianz	Rogge Global Partners
Amundi	Kleinwort Benson Investors
Columbia Threadneedle	Emerging Global Advisors
Courtiers	JRH Asset Management
Franklin Templeton	AlphaParity
Henderson Global Investors	Janus
Legal and General Investment Management	Aegon annuity portfolio
Legg Mason	EnTrust Capital, Clarion Partners, Financial Guard
Liontrust	Alliance Trust Investment
Momentum	London and Capital adviser business
Standard Life	AXA portfolio services
State Street Global Advisors	GE Asset Management
Stonehage Fleming	FF&P Wealth Planning

## 2015

ACQUIRER	PURCHASE
Aviva	Friends Life
BNY Mellon	Cutwater Asset Management
Henderson	90 West (increased holding to 100%) Perennial Fixed Interest Partners/Perennial Growth Management
Broadstone	Blythwood
Brooks Macdonald	Levitas Investment Management Services Ltd
Legal and General Investment Management	Aerion
GAM	Singleterry Mansley Asset Management
Maitland	Phoenix Fund Services
Stonehage	Fleming Family
Threadneedle	Columbia (merger)
Vontobel	TwentyFour

## 2014

ACQUIRER	PURCHASE
Aberdeen	Scottish Widows Investment Partnership
Bank of Montreal	F&C
Broadstone	Blythwood
Brooks Macdonald	Levitas Investment Management Services Ltd
Family Investments	Engage Mutual
GAM	Singletery Mansley Asset Management
Legg Mason	Martin Currie
Octopus	MedicX
Rathbones	Jupiter Asset Management Limited's private client and charity investment management business
River and Mercantile	P-Solve (merger)
Standard Life	Ignis Asset Management
Thomas Miller	Broadstone Wealth Management

## 2013

ACQUIRER	PURCHASE
Aberdeen	Artio Global Investors Scottish Widows Investment Partnership
Aviva	Solar portfolio from Ecovision Renewable Energy
Barings	SEI Asset Korea (SEIAK)
BlackRock	Credit Suisse ETF Business
Bank of Montreal	F&C
Henderson	H3 Global Advisers Northern Pines Capital (50%) 90 West (33%)
Liontrust	North Investment Partners
Miton	PSigma
PSigma	Axa Framlington private client business
Royal London	Co-Operative (Insurance and asset management businesses)
Schroders	Cazenove Capital Management STW Fixed Income
Standard Life Wealth	Private client division of Newton

## 2012

ACQUIRER	PURCHASE
Brooks Macdonald	Spearpoint
Bridgepoint & Quilter	Quilter (MBO)
Broadstone	UBS Wealth's corporate pension arm
Franklin Templeton	K2 Advisors
Goldman Sachs	Dwight
Insight	Pareto
Legg Mason	Fouchier Partners
Liontrust	Walker Crips
Natixis	McDonnell
Punter Southall	PSigma
Rathbone	Taylor Young

## 2011

ACQUIRER	PURCHASE
BT	JO Hambro
Close	Cavanagh Wealth Management
Close	Allenbridge Group
Cyrus Finance	SVM Asset Management
Franklin Templeton	Rensburg
Henderson	Gartmore
Investec	Evolution
Liontrust	Occam
Principal	Origin
Punter Southall	Brewin Dolphin's corporate pension arm
Royal London	Royal Liver
SGBP Hambros	Barings' private client business
Threadneedle	Liverpool Victoria
Williams de Broe	BNP Paribas' private client business

## 2010

ACQUIRER	PURCHASE
Aberdeen	RBS' multi manager and alternatives business
Alpha Real Capital	Close Brothers' property fund management business
AMG	Artemis
Aviva Investors	River Road
Close	Chartwell Group
F&C	Thames River Capital
Investec	Rensburg Sheppard
Man Group	GLG Partners
Marlborough	SunLife Financial of Canada's funds
Schroders	RWC Partners (49%)
State Street	Bank of Ireland

## 2009

ACQUIRER	PURCHASE
BlackRock	BGI
BNP Paribas	Fortis
BNY Mellon	Insight
Henderson	New Star
Ignis	Axial
Invesco	Morgan Stanley's retail fund business
Marlborough	Apollo
Neuberger Berman Group	Management buyout of Lehman asset management business
Rathbone	Lloyds' RBS PMS client portfolio and two private client portfolios
Sumitomo Trust	Nikko

## APPENDIX 5

# DEFINITIONS

### CORPORATE CLIENTS

Institutions such as banks, financial corporations, corporate treasuries, financial intermediaries and other private sector clients. Asset management services for fund products operated by financial corporations are included under 'Sub-advisory'.

### FUND OF FUNDS

Funds whose investment objective is fulfilled by investing in other funds rather than investing directly into assets such as cash, bonds, shares or property. These may also be referred to as 'multi-manager products'.

### IMPACT-DRIVEN INVESTMENT

This approach seeks to enhance value by proactively screening for businesses that are seeking to work for the benefit of all their stakeholders, not just shareholders or owners.

### IN-HOUSE INSURANCE CLIENTS

Refers to assets that insurance-owned asset management firms manage for their parent company or an insurance company within the parent group.

### INVESTMENT FUNDS

All pooled and listed vehicles regardless of the domicile of the client or fund (ie. unit trusts, investment companies with variable capital including ETFs, contractual funds, investment trusts, and hedge funds) but it does not include life or insurance funds.

### LIABILITY DRIVEN INVESTMENT (LDI)

Defined as an approach where investment objectives and risks are calculated explicitly with respect to individual client liabilities.

### MULTI-ASSET MANDATE

Also called 'balanced', these types of mandate invest across a range of asset classes and geographies without a specific focus on a particular universe.

### NON-PROFIT CLIENTS

Includes charities, endowments, foundations and other not-for-profit organisations.

### 'OTHER' CLIENTS

Assets managed on behalf of client types that cannot be classified under any other category as well as unidentifiable client types, eg. closed-ended funds or institutional pooling vehicles.

### OVERSEAS BONDS

Include overseas government bonds as well as debt denominated in overseas currencies.

### OVERSEAS CLIENT ASSETS

Assets managed on behalf of non-UK clients. Includes assets delegated to the firm from overseas offices and assets directly contracted in the UK.

### PENSION FUND CLIENTS

Incorporates both defined benefit (DB) and defined contribution (DC) provision, where the respondent has a relationship with a pension fund, irrespective of type. Where the DC provision is operated via an intermediary platform, particularly a life company structure wrapping the funds, the assets are reflected in 'Insurance'.

### POOLED VEHICLES

Comprises investment vehicles operated by a manager for several clients whose contributions are pooled. More specifically, as used throughout this survey, the term includes: authorised unit trusts, open-ended investment companies (OEICs), unauthorised investment vehicles (eg. unauthorised unit trusts), close-ended investments (eg. investment trusts), exchange-traded funds (ETFs), life funds, operated by insurance companies.

### PUBLIC SECTOR CLIENTS

Encompasses central banks, supranational bodies, public sector financial institutions, governmental bodies, public treasuries and sovereign wealth funds as well as the non-pension assets of local authorities and other public sector clients.

### PRIVATE CLIENTS

Comprise assets managed on behalf of high-net-worth and ultra-high-net-worth individuals as well as family offices.

## RETAIL

Includes investment into unit trusts, open-ended investment companies (OEICs) and other open-ended investment funds irrespective of domicile. It incorporates assets sourced through both intermediated sales (ie. made through fund platforms, supermarkets and other third parties) and direct retail sales. It does not include life-wrapped funds, which are classified under 'Third Party Insurance'.

## RESPONSIBLE INVESTMENT

An approach where the investor avoids investing in businesses that are harming people or the planet, such as oil, tobacco, or weapons production.

## SEGREGATED

Assets directly invested within segregated portfolios, and managed on behalf of one client. This would also include mandates run on behalf of a single pooled vehicle (eg. a 'pooled' insurance fund run for an insurance parent company).

## SINGLE-ASSET

Also called 'specialist', these types of mandate are overwhelmingly focused on one asset class, and therein usually a specific sub-type (either geographic or other; eg. a US equity mandate or an index-linked gilt mandate).

## STERLING CORPORATE DEBT

Exposure to Sterling-denominated debt, irrespective of whether it is issued by UK or overseas companies.

## SUB-ADVISORY

Business as part of which the respondent provides investment management services to third party fund products. It may therefore include business that is institutional to the respondent, but may ultimately be retail (eg. 'white-labelled' funds or manager of manager products).

## SUSTAINABLE INVESTMENT

This approach seeks to enhance value by proactively screening for businesses that are seeking to work for the benefit of all their stakeholders, not just shareholders or owners.

## THIRD PARTY INSURANCE CLIENTS

Assets sourced from third party insurance companies (ie. from outside the respondent's group), where the mandates are seen as institutional. It includes both unit-linked assets (ie. funds manufactured by the respondent and distributed with the respondent's brand through a life platform) and other third party assets.

## UK ASSETS UNDER MANAGEMENT

Assets where the day-to-day management is undertaken by individuals based in the UK. This includes assets managed by the firm in the UK whether for UK or overseas clients contracted with the firm. It also includes assets delegated to the firm's UK-based asset managers by either third party asset managers or overseas offices of the company or group. With respect to fund of funds and manager of manager products, the figure only includes the size of the underlying funds managed by the firm's UK-based managers.

## UK FUND MARKET

This primarily covers UK-domiciled authorised unit trusts and OEICs, which are by the far the largest part of the UK retail fund market, but also used by institutional investors. A small but growing part of the fund market is represented by funds domiciled overseas though often with portfolio management performed in the UK. There are also some UK-domiciled funds that are sold into overseas markets. The term 'UK funds' used throughout the survey applies specifically to UK authorised and recognised investment funds, which include (authorised) Unit Trusts and OEICs. These investments are collectively referred to as the 'funds industry' and are analysed in detail in Chapter 5.

## UK INSTITUTIONAL CLIENT MARKET

Covers mandates or investment in pooled funds by UK institutional clients. We analyse this market on the basis of client domicile, not domicile of funds invested in or location of asset manager. This is in contrast to the analysis of UK assets under management, which covers assets managed in the UK regardless of domicile of funds or clients for whom firms manage money.

## APPENDIX 6

# SURVEY RESPONDENTS

Aberdeen Standard Investments	Majedie Asset Management Ltd
AllianceBernstein	Man Fund Management (UK) Ltd
Aberforth Partners LLP	Martin Currie Fund Management
Allianz Global Investors	McInroy & Wood
Artemis Fund Managers Ltd	Morgan Stanley Investment Management Ltd
Aviva Investors	Natixis Global Asset Management
AXA Investment Managers UK Ltd	Newton Investment Management Ltd
Baillie Gifford & Co Ltd	Odey Asset Management LLP
Baring Asset Management Ltd	Old Mutual Global Investors (UK) Ltd
BlackRock Investment Management (UK) Ltd	PIMCO Europe Ltd
Brewin Dolphin	Premier Portfolio Managers Ltd
Canada Life Asset Management Ltd	Principal Global Investors (Europe) Ltd
Carvetian Capital Management Ltd	Pyrford International plc
CCLA Investment Management	Rathbone Unit Trust Management
CRUX Asset Management	RBS CIF
Columbia Threadneedle Investments	Royal London Asset Management Ltd
EFG Asset Management	Ruffer LLP
FIL Investment Management Ltd	RWC Partners Ltd
Franklin Templeton Investment Management Ltd	Santander Asset Management UK
Guinness Asset Management Ltd	Sarasin & Partners LLP
Hermes Fund Managers	Scottish Friendly Asset Managers Ltd
HSBC Global Asset Management (UK) Ltd	Schroder Investment Management Ltd
Independent Franchise Partners LLP	Skagen AS
Insight Investment Management (Global) Ltd	Smith & Williamson Fund Administration Ltd
Invesco Perpetual	State Street Global Advisors UK
Investec Asset Management Ltd	SVM Asset Management Ltd
Janus Henderson Investors	T. Rowe Price International Ltd
J P Morgan Asset Management	Tesco Pension Investment Ltd
JO Hambro Capital Management Group	Troy Asset Management Ltd
Kames Capital	TwentyFour Asset Management
Lazard Asset Management	UBS Global Asset Management (UK) Ltd
Legal & General Investment Management	Vanguard Asset Management Ltd
Lindsell Train	Way Fund Managers
Lyxor ETF	Wellington Management International
M & G Investments Ltd	Zurich Investment Services (UK) Ltd



## APPENDIX 7

# FIRMS INTERVIEWED

Aberdeen Standard Investments

Aviva Investors

AXA Investment Managers UK Ltd

Baring Asset Management Ltd

Blackrock Investment Management (UK) Ltd

Guinness Asset Management Ltd

Hermes Investment Management

HSBC Global Asset Management (UK) ltd

Invesco Perpetual

Kames Capital

Martin Currie Fund Management Ltd

Miton Group plc

Schroder Investment Management Ltd

T. Rowe Price International Ltd

# NOTES

# NOTES

# NOTES





**The Investment Association**

Camomile Court, 23 Camomile Street, London, EC3A 7LL

[www.theinvestmentassociation.org](http://www.theinvestmentassociation.org)

 @InvAssoc

September 2018