

Asset Management in the UK 2014-2015

The Investment Association
Annual Survey

THE
INVESTMENT
ASSOCIATION
MAKING INVESTMENT
BETTER

September 2015



CONTENT ENQUIRIES

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ABOUT THE SURVEY

THE SURVEY CAPTURES ASSET MANAGEMENT UNDERTAKEN BY MEMBERS OF THE INVESTMENT ASSOCIATION ON BEHALF OF DOMESTIC AND OVERSEAS CLIENTS FROM THE FOLLOWING PERSPECTIVES:

- Assets managed in the UK on behalf of institutional and retail clients, irrespective of the country in which the underlying client is located (Chapters One and Two).
- Assets managed for UK institutional clients by member firms, irrespective of the country in which the asset management activity is undertaken (Chapter Three).
- UK domiciled (authorised) Unit Trusts and Open Ended Investment Companies (Chapter Four).

IT IS BASED ON:

- Results of questionnaire responses from 72 Investment Association member firms, who between them manage £4.6 trillion in this country (84% of total UK assets under management by the entire Investment Association membership base).
- Other data provided to The Investment Association by member firms.
- Third party data where specified.

The Investment Association would like to express its gratitude to member firms who provided detailed questionnaire information and to those who took part in this year's interviews.

THE SURVEY HAS FIVE CHAPTERS:

- Industry Overview
- Shaping the Future of Asset Management
- UK Institutional Client Market
- UK Fund Market
- Operational and Structural Issues

THERE ARE ALSO SEVEN APPENDICES:

- Summary of assets under management in the UK
- Summary of the UK institutional client market
- Major UK and EU regulatory developments affecting asset management
- Notable M&A deals in the UK asset management sector (2009-July 2015)
- Definitions
- Survey respondents
- Firms interviewed

A NUMBER OF GENERAL POINTS SHOULD BE NOTED:

- Unless otherwise specified, all references to 'UK assets under management' refer to assets, wherever domiciled, where the day-to-day management is undertaken by individuals based in the UK. The asset value is stated as at December 2014. For a more detailed explanation of the term please refer to Appendix Five.
- 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 multiple years, some may have responded to a question in one year but not in another. Meaningful comparisons have been made where possible.
- 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 issues.

SURVEY FOREWORD



THE INVESTMENT ASSOCIATION'S ASSET MANAGEMENT SURVEY IS NOW IN ITS THIRTEENTH YEAR. THE SURVEY MAY HAVE A NEW LOOK THIS YEAR TO REFLECT OUR CHANGE OF NAME TO THE INVESTMENT ASSOCIATION BUT MANY OF THE FINDINGS ARE ON FAMILIAR THEMES.

Asset management in the UK continues to go from strength to strength, with assets growing significantly faster in the UK than globally in recent years. The industry continues to be highly international, with around 40% of the £5.5 trillion of assets under management in this country coming from overseas clients. The industry is a significant exporter for Britain.

As the industry grows, so does the scrutiny it receives from clients, regulators, policymakers and the media. Asset managers will need to respond appropriately in the coming years as their role in the economy and society continues to expand.

The majority of assets are still actively managed but the debate is intensifying about the relative cost and delivery of active and passive management. While there is much focus on the evolution of the indexing product set, the increasing solutions and outcome focus within the wider industry suggests that active management may need to be defined more broadly than simply stock and securities selection.

Pension schemes are still the largest client type but today's pension assets are very different from the domestic defined benefit schemes that dominated the industry 20 years ago. In future, the emergence of millions of new savers automatically enrolled into defined contribution schemes, together with the new pension freedoms, are likely to redefine asset managers' relationships with the pensions market and mean that the industry is more visible than ever before.

While savers are being given more responsibility to invest for their financial futures, asset managers also have significant responsibilities. They will need to offer an appropriate range of investment choices that can generate income, protect capital and provide the new generation of retirees with the solutions they need to meet their requirements. This poses asset managers with a big challenge in the coming years but it also offers a significant opportunity to evolve the expertise we already have in the UK to a new mix of investment needs.

I hope you enjoy reading this year's survey and welcome any ideas you many have to improve future editions.

A handwritten signature in black ink that reads "Daniel Godfrey". The signature is fluid and cursive, written in a professional but personal style.

Daniel Godfrey
Chief Executive

EXECUTIVE SUMMARY

- Assets under management in the UK by members of The Investment Association hit another record high at the end of 2014, reaching £5.5 trillion. £2.8 trillion was managed for UK institutional clients by Investment Association members globally.
- Two fifths (39%) of assets managed in the UK were managed on behalf of clients located outside of the UK.
- Authorised funds also reached a new high for assets under management, increasing to £835 billion by the end of 2014 from £770 billion in 2013. Equity income and property funds remained popular as investors continued to look for yield in a low interest rate environment.
- Passive remained a comparatively small part of overall UK asset management activity (20%). However, this increased to 23% once approaches such as smart beta were included, compared to 22% in passive strategies in 2013.
- Within authorised funds passive investment continued to be popular producing a record high retail sales figure of £4.9 billion. In the wider industry the pressure towards passive management was illustrated by the introduction of a charge cap on defined contribution (DC) default funds and the Government's proposal that the Local Government Pension Scheme (LGPS) should move to passive management to reduce costs.
- The proportion of assets represented by insurance continued to fall to an all-time low of 18%, with consistently slower asset growth than other client groups. Pension funds remained the largest client type at 38%. However, this understates assets managed for pension savings as many DC pension assets are wrapped into products accounted for under insurance assets. The ratio of institutional to retail assets remained constant at 80:20.
- The demand for alternative assets continued to increase as investors diversify more widely and search for investment opportunities that can offer other sources of return or income in today's challenging environment. Allocation to alternatives increased from 11% in 2013 to 13% in 2014.
- The demand for income is widespread, from savers looking for an alternative to bank saving, pensioners in search of some form of stable income in retirement and from institutional defined benefit (DB) schemes looking to meet future cash flows.
- Equities remained the largest asset class at 42%, down from 46% in 2013 but still high based on international comparisons.
- The new DC pension freedoms, coming on the back of automatic enrolment, are likely to lead to a transformation in retirement saving, as pensioners leave their assets invested throughout their retirement. This is expected to lead to increased demand for outcome-focused funds, income generation and more diversified multi-asset portfolios.
- There is significant scrutiny of the asset management industry by clients, politicians regulators and other stakeholders. Some of this scrutiny relates to a lack of trust in the industry and firms acknowledge that more must be done to ensure that asset management enjoys greater confidence as its role in the economy and society expands.
- The accelerating impact of technology on the industry was a key theme in this year's survey. While firms are less worried about the immediate scope for technology to facilitate new entrants in the investment product manufacturing space, distribution is an area where there is concern about the possibility of significant disruption



KEY STATISTICS

£ 5.5 TRILLION

[£5.0 TRILLION IN 2013]

TOTAL ASSETS MANAGED IN THE UK BY THE INVESTMENT ASSOCIATION'S MEMBERS AS AT DECEMBER 2014

£ 835 BILLION

[£770 BILLION IN 2013]

MANAGED IN UK AUTHORISED FUNDS (OEICS AND UNIT TRUSTS)

£ 2.2 TRILLION

[£2.0 TRILLION IN 2013]

ASSETS MANAGED IN THE UK ON BEHALF OF OVERSEAS CLIENTS

£ 895 BILLION

[£775 BILLION IN 2013]

UK-MANAGED FUNDS DOMICILED OFFSHORE

32 PER CENT

[30 PER CENT IN 2013]

UK DOMESTIC MARKET CAPITALISATION ACCOUNTED FOR BY THE INVESTMENT ASSOCIATION'S MEMBERS' UK EQUITY HOLDINGS

37 PER CENT

[35 PER CENT IN 2012]

TOTAL EUROPEAN ASSETS UNDER MANAGEMENT MANAGED IN THE UK AS AT DECEMBER 2013 (LATEST AVAILABLE).



1 INDUSTRY OVERVIEW

KEY FINDINGS

ASSETS UNDER MANAGEMENT

STRONG GROWTH IN UK INDUSTRY OUTSTRIPS GLOBAL GROWTH.

- Total assets under management were up 9% year-on-year at £5.5 trillion. Global assets rose 8% in comparison.
- Assets managed in UK authorised funds increased by 8%, to £835 billion.
- While only 9% of assets under management in the UK were actually managed in Scotland (£485 billion), Scottish-headquartered firms account for one quarter of total assets managed in the UK by UK headquartered firms.

CLIENT TYPES

PENSIONS REMAIN THE BIGGEST CLIENT TYPE, WITH THE PROPORTION OF INSURANCE ASSETS CONTINUING TO FALL.

- 38% of assets were managed on behalf of pension fund clients.
- The proportion of assets represented by insurance continued to fall, standing at 18% at the end of 2014, down from 20% in 2013.
- Overseas client assets remained steady, representing two-fifths of assets under management in the UK, at £2.2 trillion.

ASSET ALLOCATION

NO CLEAR DIRECTION IN EQUITY/FIXED INCOME SHIFT BUT GROWTH IN ALTERNATIVES CONTINUES.

- 2014 saw the share of equities fall to 42% from 46% in 2013. This brings the equity allocation back to the levels of two years ago. Fixed income increased from 34% in 2013 to 36%.
- The allocation to alternative assets increased from 11% to 13%, consistent with the trend for investors seeking complementary sources of return and income.

PORTFOLIO TYPE

DEMAND FOR PASSIVE STRATEGIES ONGOING IN THE FACE OF CLIENT, POLITICAL AND REGULATORY FOCUS ON COSTS.

- 54% of assets were managed in segregated mandates, and 46% in pooled vehicles, almost unchanged from 2013.
- Active mandates still represent the overwhelming majority of assets managed in the UK, with more than three quarters of assets actively managed at the end of 2014. Twenty per cent of assets were managed on a strictly passive basis and 3% of assets were managed using strategies classified as neither active nor passive, such as smart beta.

1 INDUSTRY OVERVIEW

The UK asset management industry serves a wide variety of institutional and retail clients from all over the world. This survey focuses on the activities of members of The Investment Association, encompassing MiFID-regulated asset management firms and UCITS-regulated fund management firms.

FIGURE 1: WHO ARE THE INVESTMENT ASSOCIATION'S MEMBERS?

The membership 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 clients 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.

The term 'UK assets under management'¹ covers all forms of asset management activity, broadly split into pooled vehicles (run on behalf of multiple clients who pool their investment exposure in a fund), and

segregated mandates (bespoke portfolios managed on behalf of an individual client by an investment manager, governed by a specific agreement).

Pooled vehicles include:

- Authorised unit trusts
- Open-ended investment companies (OEICs)
- Unauthorised investment vehicles (eg. unauthorised unit trusts)
- Closed-ended investments (eg. investment trusts)
- Exchange-traded funds (ETFs)
- Life funds, operated by insurance companies

The term 'UK authorised funds', in contrast, applies specifically to UK-domiciled authorised 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 Four.

INDUSTRY SIZE

Total assets under management by members of The Investment Association were £5.5 trillion at the end of December 2014. This represented an increase of 9% on December 2013 and was yet another record high for the industry.

Investment Association membership remained relatively stable during 2014, therefore this figure can be assumed to be driven by a combination of market movements and net flows.²

Funds under management in UK authorised funds, increased 8% year-on-year, reaching £835 billion at the end of December 2014. The increase was split equally between net flows into funds and market movements.

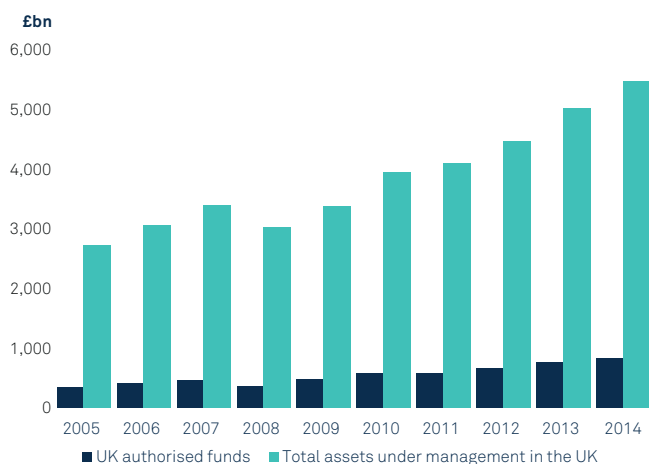
Assets managed in UK authorised funds continued to represent 15% of overall assets. This proportion has increased from 12% ten years ago but has been relatively stable over the last five years.

¹ Defined as assets where the day-to-day management is undertaken by managers within the firm and based in the UK. For a more detailed definition please refer to Appendix Five.

² We do not collect data to allow us to distinguish between the impact of flows and market movements on total assets. Flows are driven by both client decisions and organisational change, eg. changes in where money is actually managed.



CHART 1: TOTAL ASSETS UNDER MANAGEMENT IN THE UK AND IN UK AUTHORISED FUNDS (2005-2014)



The global asset management industry has grown at a slower pace than that of the UK in recent years.³ At the end of December 2014 global assets under management stood at \$74 trillion (£47 trillion). This had grown from \$55 trillion (£35 trillion) in 2007 and \$31 trillion (£20 trillion) in 2002.⁴ Authorised fund assets have shown the strongest growth over the period (see Table 1).

TABLE 1: AVERAGE ANNUAL GROWTH IN UK VS GLOBAL ASSETS UNDER MANAGEMENT SINCE 2002

| | |
|-----|-------------------------|
| 13% | AUTHORISED FUND ASSETS |
| 10% | TOTAL UK-MANAGED ASSETS |
| 8% | GLOBAL ASSETS |

Chart 2 illustrates the growth in UK assets under management over the last two decades against the growth in UK pension fund assets. Pension funds have historically been the largest client type and now represent 38% of assets under management in the UK.

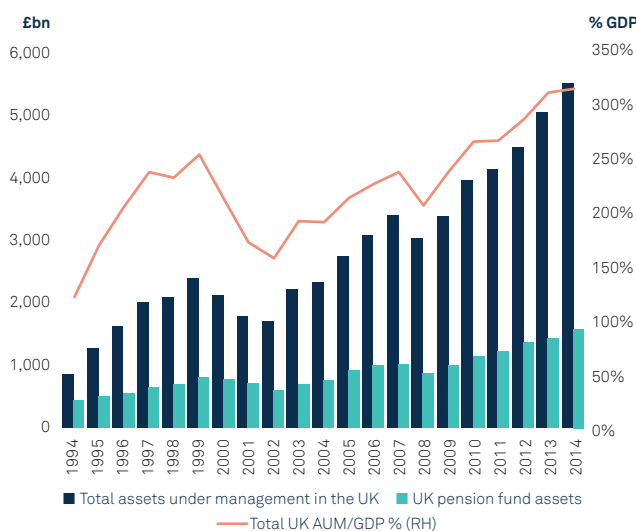
However, if we consider the proportion of the market that is represented by UK pension funds, 20 years ago that figure stood at 51% but it has now fallen to 29%. This illustrates how the overall asset base has moved beyond domestic pension assets, primarily due to growth of the overseas client market.

Thirty-nine per cent of assets managed in the UK at the end of December 2014 were managed on behalf of overseas clients (almost unchanged from 40% last year). This equates to £2.2 trillion.

The breakdown between European and other overseas clients was 54% (£1.2 trillion) for European clients and 46% (£1 trillion) for other overseas clients.

Chart 2 also demonstrates assets under management relative to UK GDP. This provides a useful measure of the change in scale of UK asset management. Over the past 20 years assets under management in the UK have grown from 122% of GDP to 316% in 2014 (2013: 313%). This compares to around 150% of GDP in France, the next largest European market, and 110% in Europe as a whole.⁵ This reinforces how strong the growth in assets has been and the scale of the importance of the industry to the UK economy today.

CHART 2: TOTAL ASSETS UNDER MANAGEMENT IN THE UK AND UK PENSION ASSETS (1994-2014)



³ Growth rates expressed in nominal terms

⁴ BCG Perspectives, Global Asset Management 2015: Sparking Growth with Go-to-Market Excellence

⁵ Data for France and European average sourced from EFAMA 2013 data.

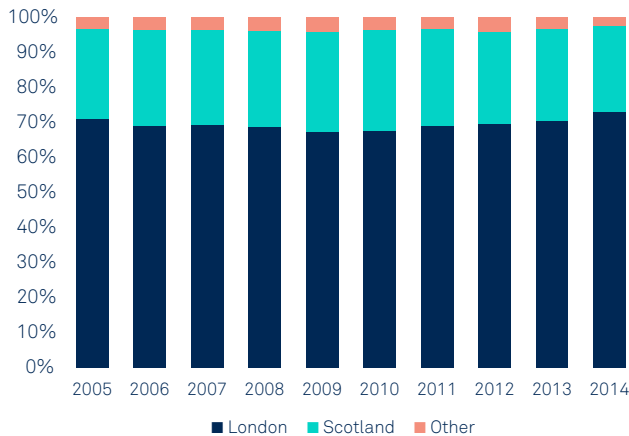
SCOTTISH BUSINESS

Assets managed in Scotland represented 9% of total assets managed by Investment Association members at the end of 2014, amounting to £485 billion. This is a significant drop on the previous year and can be mainly explained by M&A activity feeding through into 2014 data.

The picture of assets managed by firms with headquarters based in Scotland is rather different, with around one quarter of assets managed by Investment Association members with a UK headquarters being managed by companies with a headquarters in Scotland. This reflects the fact that a number of asset managers with headquarters in Scotland also have substantial asset management capability located outside of Scotland, most notably in London.

There has been some year-on-year fluctuation in this figure but Chart 3 shows that the regional split is relatively unchanged from a decade ago, with almost three quarters of firms still headquartered in London.

CHART 3: UK-MANAGED ASSETS BY UK REGIONAL HEADQUARTERS (2005-2014)

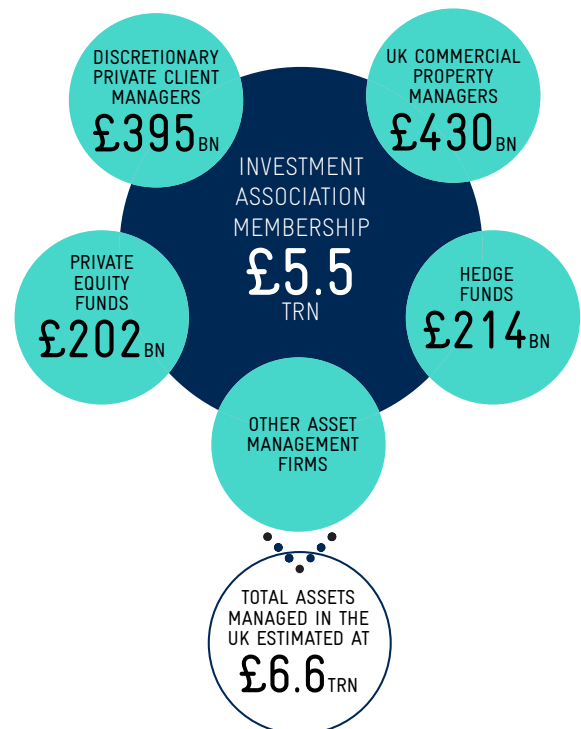


WIDER INDUSTRY

While The Investment Association's members represent the majority of the UK asset management industry in asset terms (83%), a significant number of firms contributing to the industry's activity lie outside The Investment Association membership and are not covered in detail in this report. These can be broadly categorised into the following groups (see Figure 2):

- Hedge funds.
- Private equity funds.
- Commercial property management.
- Discretionary private client management.
- Firms who are not members of the Investment Association for reasons not noted above.⁶

FIGURE 2: WIDER ASSET MANAGEMENT INDUSTRY



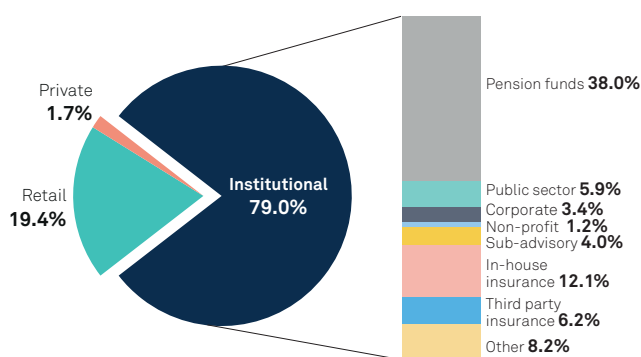
Source: ComPeer, Hedge Fund Intelligence/EuroHedge, Investment Property Forum, Investment Association estimate based on BVCA return and flow data for 2014.

⁶ This last group is more difficult to size as there is no consistent third party data available.

CLIENT TYPE

Chart 4 shows the split of the £5.5 trillion managed from the UK by client type. This chart reflects assets managed in the UK for both institutional and retail clients and includes clients based overseas as well as in the UK.

CHART 4: ASSETS MANAGED IN THE UK BY CLIENT TYPE

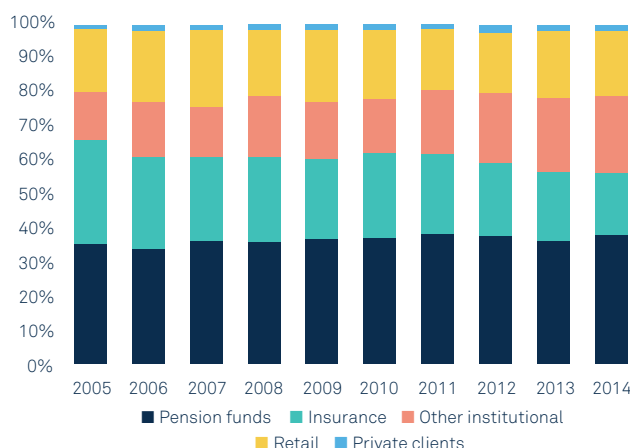


The vast majority of assets managed in the UK are managed for institutional clients. In line with data from previous years 79% of the assets at the end of 2014 related to institutional clients, and 21% to retail clients.

The pension fund category, which includes both defined benefit (DB) schemes and defined contribution (DC) schemes with which the asset manager has a direct relationship, continued to be the largest institutional client type (38%). DC pension assets that are operated via an intermediary platform are not included in this figure but are reflected in the insurance client data.

The decline of insurance assets relative to pension funds continued in 2014, with insurance assets falling to 18.3% from 20.4% in 2013 and 31% in 2005. Chart 5 shows the change in the institutional client base over the last decade and the sustained decline in insurance assets relative to pension funds and other institutional clients more clearly. Insurance assets have continued to grow in absolute size during the period, but at an annual rate of 2% since 2005, compared to the 9% annual growth of pension fund assets.

CHART 5: ASSETS MANAGED IN THE UK BY CLIENT TYPE (2005-2014)



The proportion of assets managed for in-house insurance fell once again to 12.1% of total assets, continuing to support the view of an industry becoming less vertically integrated but also reflecting assets re-categorised as third party insurance following M&A activity.

While there is some year-on-year variation, the proportions of other client types have been largely consistent in recent years. 2014 did show a small uptick in the 'other' category from 7.8% to 8.2%. This category is primarily populated by different types of pooled vehicles where it is not possible for respondents to identify the underlying client type.

The figures reported for private clients should be treated with some caution as they only relate to the portion of the private client market where members of The Investment Association provide dedicated private client investment services, which we estimate to be around a quarter of all private client assets under management.

The changes in client type proportions have largely been restricted to the institutional client base, with the overall split between institutional and retail remaining substantially unchanged over the years at 80:20.

Investments by retail investors may account for around 20% of assets at a headline level but the retail/institutional split is becoming increasingly blurred as a result of a number of developments, including the growth of platform intermediation and the growing DC market which has strong retail as well as institutional characteristics.

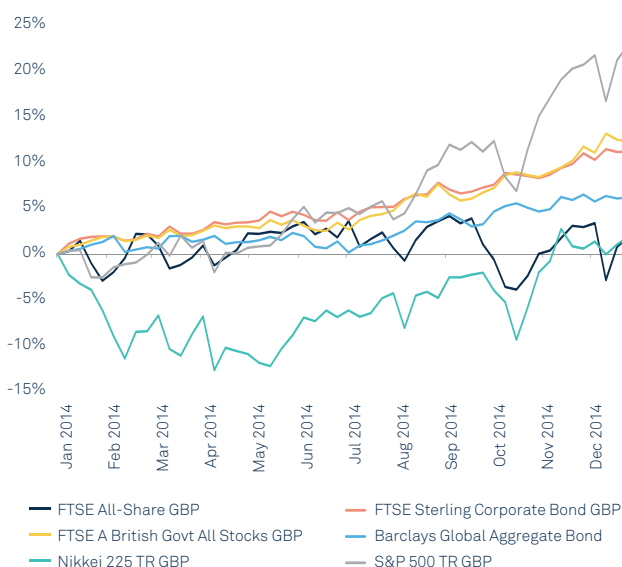


ASSET ALLOCATION

Chart 6 shows the returns of major asset classes in sterling terms. Equity and fixed income markets both posted positive returns during 2014. US equities were the strongest performers on the back of strong domestic growth. UK equities had a less upbeat year, finishing 2014 up only slightly in spite of the reasonable economic backdrop. Japanese equities had a volatile year but recovered strongly in the last quarter.

Sterling corporate and government bonds on the other hand posted double digit returns, boosted by fears of deflation in the UK.

CHART 6: CUMULATIVE PERFORMANCE OF SELECTED EQUITY AND BOND INDICES (2014)



Source: Morningstar

Equity holdings fell from 46% to 42% year-on-year, back to the same level as two years ago, potentially a reflection of the geopolitical risk seen during 2014. Over the same period, the fixed income allocation increased from 34% to 36%, possibly reverting to the trend we have observed in recent years of a gradual shift out of equities in favour of fixed income and other assets.

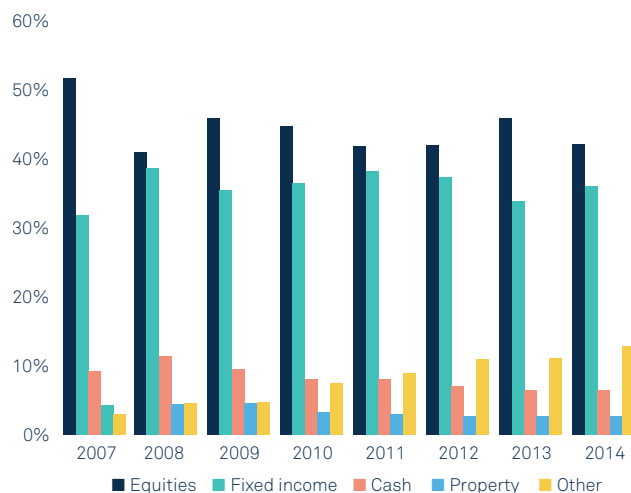
Property allocations remained stable at 2.6%. Although market returns were strong, the overall allocation to property is still small as a percentage of total assets so year-on-year variations are less obvious than for some other asset classes.

2014 saw a continued move towards other assets, with the allocation increasing to 12.8% from 11.1% in 2013. A broad range of investments are included within this category, including commodities, private equity and infrastructure. This figure will also include the nominal value of derivatives contracts, of which members are using a range including equity and interest rate derivatives, currency options, FX swaps, swaptions and variance swaps.

The increase in the allocation to other assets is consistent with the trend in recent years of investors broadening their horizons in search of return.

Cash allocations remained unchanged from the end of 2013, at 6.5%.

CHART 7: OVERALL ASSET ALLOCATION OF UK-MANAGED ASSETS (2007-2014)



In general, The Investment Association's membership comprises firms that invest primarily in mainstream asset classes (Table 2).

TABLE 2: PROPORTION OF INVESTMENT ASSOCIATION MEMBERS INVESTING BY ASSET CLASS

| | Percentage of firms |
|--------------|---------------------|
| Equities | 96% |
| Fixed income | 85% |
| Cash | 64% |
| Property | 44% |
| Other | 62% |

Nevertheless, more than half invest in some form of alternative asset class.

INFRASTRUCTURE

In this year's survey we were particularly interested to explore the activity of our members in the area of infrastructure investment. The definition of infrastructure encompasses a broad selection of underlying projects, including transport, social (housing and education), water, energy and communication.

The proportion of Investment Association members investing in infrastructure remains relatively small. 12% of respondents provided some detail on how they invested in this asset class during 2014. However, those asset managers are using a wide variety of methods to obtain their exposure, which include equity, public listed bonds, private placements and bilateral loans, mezzanine and non investment-grade debt.

Members interviewed for this year's survey viewed infrastructure as a good potential source of return for a variety of investors, not just the traditional large DB pension schemes. They also saw it as a way for the asset management industry to be seen to have a more positive impact on the economy and to invest in assets which are more tangible to the end investor.

"THE OTHER THING THE INDUSTRY NEEDS TO DO IS ALLOCATE MORE TO THINGS LIKE INFRASTRUCTURE AND NOT BE BOUND BY DC SCHEMES NEEDING DAILY LIQUIDITY. THAT IS GOOD FOR THE INDIVIDUAL'S RETURN AND SUPPORTIVE OF THE ECONOMY TOO. I THINK THERE WOULD BE DEMAND FROM DC - AT INDIVIDUAL AND FUND LEVEL AND IT IS LONG TERM."

"IT'S HARD BUT THERE'S A GAP BETWEEN WHAT WE DO AND HOW WE ARE PERCEIVED. WHAT WE DO ISN'T TANGIBLE AND IF WE CAN SOMEHOW MAKE IT TANGIBLE, LIKE "I HELPED BUILD THE FACTORY THAT MY GRANDDAUGHTER WORKS IN" - THEN IT STARTS TO MAKE IT FEEL MORE LIKE A GOOD INVESTMENT."

MANAGING VOLATILITY

Poor equity returns during the financial crisis and the more recent unease about the potential direction of fixed income markets have contributed, according to those we interviewed, to real concerns among investors around volatility.

Some of those we interviewed felt there was a great opportunity to add value for clients, and a role for active managers to add value across a range of global markets.

"OUR GREATEST CHALLENGE IS FINDING A WAY TO NAVIGATE THE MARKETS. LOW INTEREST RATES, EQUITY VALUATIONS AT THE HIGH END, CURRENCY WARS, PEOPLE ARE NERVOUS. THESE ARE ALL OPPORTUNITIES TO OFFER VALUE AND STEP UP BUT IT'S A VERY CHALLENGING ENVIRONMENT TO ADD VALUE..."

"IF YOU CAN LIVE WITH VOLATILITY WE ARE PRETTY HAPPY WITH THE POTENTIAL RETURNS YOU COULD MAKE BUT YOU'VE GOT TO BE HAPPY WITH VOLATILITY."

However, others identified a step change in investor sentiment, and a greater emphasis on downside protection.

This in turn has led to increased interest in 'liquid alternatives', which attempt to utilise the investment flexibility offered by hedge funds but may have lower investment minimums and are governed by regulations covering leverage and daily liquidity.

Globally, 'liquid alts' are the fastest growing segment of the asset management industry, increasing at around 40% a year since the crisis⁷. Interest in Europe is strong. Just under two thirds (64%) of EMEA respondents to a recent survey said they invest in alternative UCITS products (compared to 28% in Asia Pacific and 11% in the Americas). More than three quarters of those currently investing plan to increase their allocation over the next year.⁸

The limitations that liquid alt funds are subject to may negatively temper their performance potential. However the lower levels of risk and the greater ease of investment access may appeal to investors looking for sources of potentially more consistent, risk-adjusted return.

"CUSTOMER EXPECTATIONS HAVE CHANGED AND ARE DISPROPORTIONATELY FOCUSED ON THE DOWNSIDE - I DON'T WANT TO LOSE MY MONEY BUT I STILL WANT 5%"



Some members interviewed this year did, however, voice concerns about the levels of sophistication required from clients to understand the increasing variety of alternative investments, and the potential reputational risk to the industry should these investments not fulfil expectations.

GEOGRAPHIC EQUITY SPLIT

At a more granular level, The Investment Association monitors the geographical breakdown of members' equity and fixed income allocations.

On a regional basis equity allocations were relatively stable in 2014. Most notably, UK equity holdings increased by one percentage point to 32% of total equity holdings at the end of 2014, finally halting a steady decline from a high of 59% in 2006.

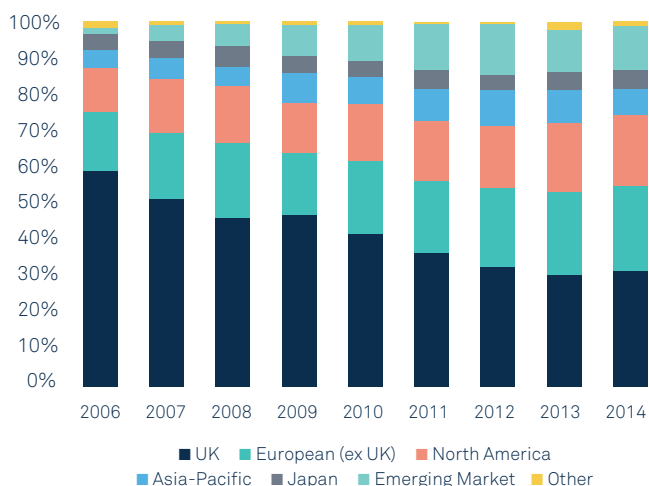
- The Europe ex-UK allocation remained unchanged from 2013, at 23%.
- The allocation to North American equities increased by one percentage point to 20% year-on-year.
- There was a drop in allocation to Asia-Pacific ex-Japan to 7% from 9% a year before.
- The allocations to Japan and emerging markets remained unchanged year-on-year at 5% and 12% respectively.

⁷ From Alternatives to Mainstream (Part Two), Deutsche Bank, 2014

⁸ Deutsche Bank Alternative Investment Survey, 2015



CHART 8: UK-MANAGED EQUITIES BY REGION (2006-2014)

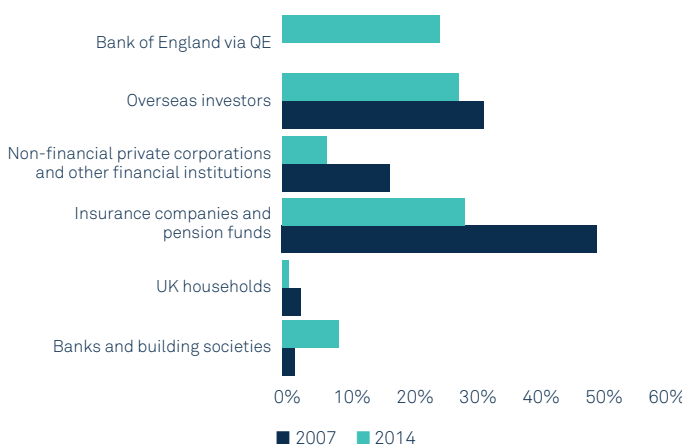


FIXED INCOME

Historically, most UK government debt has been owned by UK insurance and pension funds. However, the Bank of England’s quantitative easing programme has led to a major shift in the ownership breakdown of UK gilts.

The Bank of England has acquired an additional 25% of the UK gilt market as a direct result of QE. The large purchases undertaken by the Bank of England have reduced the supply of government bonds available on the open market, increasing the pricing pressure and contributing to the fall in gilt ownership by UK pension schemes.

CHART 9: CHANGE IN UK GILT OWNERSHIP (2007-2014)



Source: ONS, Bank of England⁹

⁹ Q 3 data

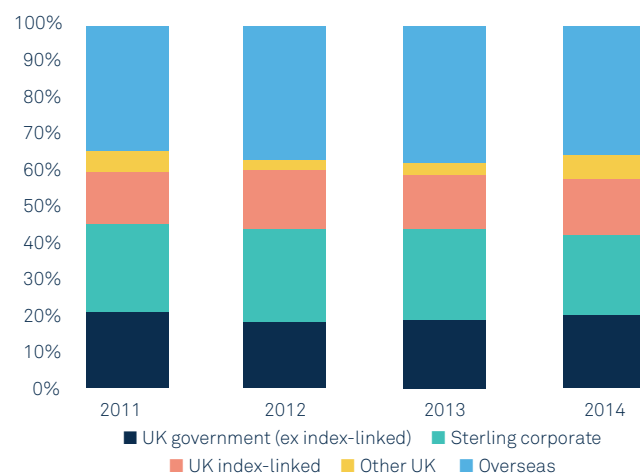
Even at today’s prices gilts remain an important asset for pension schemes and insurance companies:

- DB pension schemes continue to look to reduce risk and match their long term liabilities.
- Insurance companies, which are still holding significant amounts of UK government and sterling corporate debt to fund their annuity pools.

Data collected this year supports this as, overall, the fixed income allocation in 2014 shifted marginally back towards the UK. The allocation to overseas fixed income fell back from 38% to 36%, whereas:

- The allocation to UK government debt remained largely unchanged in 2014 (36%). Within government bonds, the allocation to conventional gilts increased by one percentage point to 20%. Index-linked bond allocations remained unchanged at 15%.
- The allocation to UK corporate securities fell from 25% to 22% but the allocation to ‘other UK’ securities increased from 3% to 6%. This category includes some mandates, which can be categorised as UK fixed income but for which members were not able to provide the underlying breakdown.

CHART 10: ALLOCATION OF UK-MANAGED FIXED INCOME BY TYPE AND REGION (2011-2014)



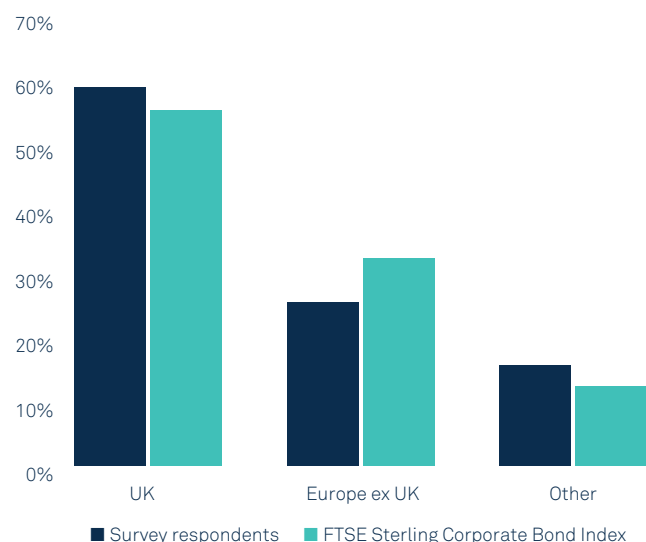
In March 2014, the Chancellor announced that DC pension savers would no longer be effectively forced to purchase an annuity when they retire. These changes will pose significant challenges to the industry. However, they also present opportunities for asset managers to evolve services that are suitable for savers up to and after retirement.

It remains too soon to know what impact the recent changes will have on asset allocation choices after retirement but fixed income is likely to continue to play a significant role in any post-retirement strategies. The ramifications of the changes to UK pensions are discussed in greater detail in Chapter Two.

For the first time in the 2014 survey respondents were asked to provide a breakdown of their UK corporate bond allocation by country of issuer. This provides a more meaningful geographical breakdown of bond exposure and better reflects the asset management industry’s importance to the provision of finance to international markets.

Chart 11 shows that 41% (by asset value) of sterling denominated corporate bonds in our survey sample were issued by companies outside of the UK, with one quarter being issued by European companies.

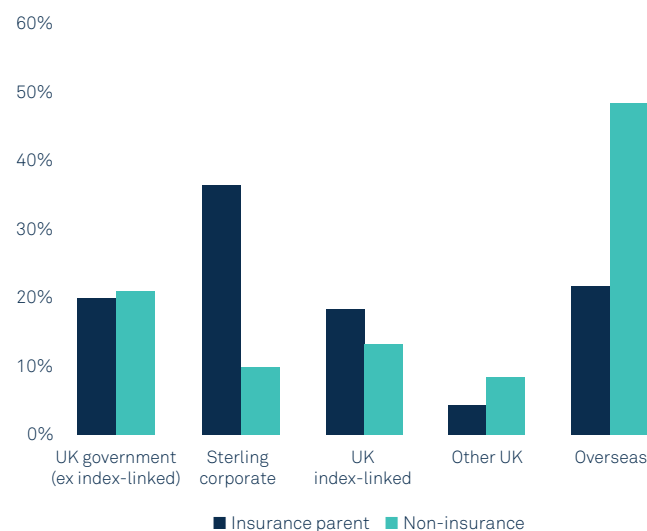
CHART 11: BREAKDOWN OF STERLING CORPORATE BOND ALLOCATION BY COUNTRY OF ISSUER



Source: Investment Association, FTSE

Fixed income allocations differ significantly by client type, with insurance companies in particular having very different requirements to other institutional investors. If we consider how the allocation alters depending on whether the asset manager has an insurance parent or not, that difference becomes very clear. Insurance-owned groups have a much higher exposure to sterling corporate securities and, to a lesser extent, to index-linked gilts.

CHART 12: FIXED INCOME OWNERSHIP BY PARENT GROUP (INSURANCE VS. NON-INSURANCE)



The data based on the respondent sample to The Investment Association’s survey tends to over represent insurance-owned asset managers. Therefore if we adjust the allocation to be more representative of the market as a whole we see, not surprisingly, that the allocation to sterling corporate and index-linked holdings drops slightly and the allocation to overseas bonds increases to 38%.

TABLE 3: HEADLINE VS. SAMPLE-ADJUSTED FIXED INCOME OWNERSHIP¹⁰

| | Headline | Sample-adjusted |
|------------------------------------|----------|-----------------|
| UK government (excl. Index-linked) | 20.4% | 20.4% |
| Sterling corporate | 22.2% | 19.6% |
| UK index-linked | 15.5% | 15.0% |
| Other UK | 6.4% | 6.8% |
| Overseas | 35.6% | 38.1% |

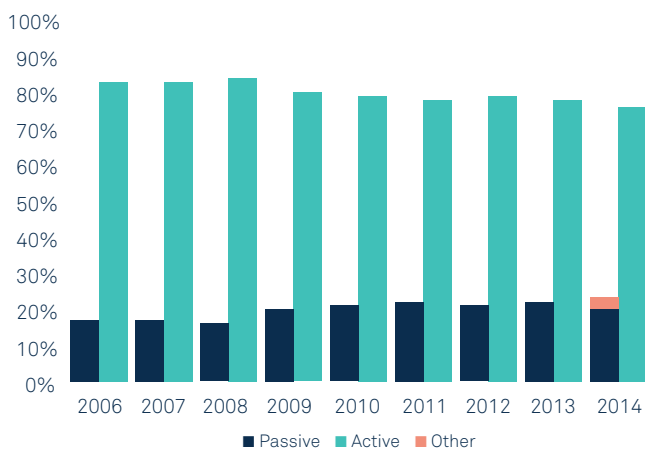
¹⁰ Results are adjusted to reflect The Investment Association’s membership, which has a lower proportion of insurance-owned firms than the respondent sample within the survey

TYPE OF MANAGEMENT

ACTIVE AND PASSIVE

Chart 13 illustrates the evolution of active and passive management over the past nine years. The proportion of assets being managed using passive strategies has increased year-on-year since 2008.

CHART 13: ACTIVE AND PASSIVE AS PROPORTION OF TOTAL UK ASSETS UNDER MANAGEMENT (2006-2014)



Cognisant of the growth of strategies such as 'smart beta', for the first time in in 2014 we asked respondents to report separately on assets that are managed using strategies that do not fit neatly into either the category of active or passive.



Chart 13 assumes that these strategies have been included under 'passive' in previous years as we cannot be sure of the historical breakdown. Therefore some caution must be applied when comparing the results pre and post 2014. Overall, however, there has been a slow move towards greater use of passive, including smart beta.

What is smart beta?

There is no single agreed terminology or definition in this area, and other terms include enhanced indexation and strategic beta. Smart beta describes strategies that are not designed purely to track the return of a given index, but seek to add value using quantitative approaches that are different to the active securities and stock selection that characterise traditional asset management.

The proportion of assets being managed in this manner at the present time is relatively small. However, recent data suggests that interest in the use of smart beta strategies is increasing among institutional investors and that interest is particularly strong among European asset owners. Investors are more likely to use (40%) or be evaluating (58%) smart beta as part of a mix of active and passive equity allocation rather than as part of a single approach.¹¹

The majority of the ETF market lies outside of The Investment Association's data so it is likely that the passive figure is somewhat understated in Chart 13. At the end of December 2014, the value of ETF/ETPs with a primary listing in the UK was around £120 billion.¹²

¹¹ Smart beta: 2015 global survey findings from asset owners, FTSE Russell

¹² ETFGI, Bloomberg, ETF/ETP providers

“I THINK THE PROPORTION OF PASSIVE WILL GROW ALTHOUGH IT IS FROM A PRETTY LOW BASE AS A PROPORTION OF OVERALL ASSETS... WHEN YOU GET TO THE ADVICE MARKET I THINK MORE PEOPLE WILL TURN TO ETFS AS A SOURCE OF ASSET ALLOCATION.”



“PEOPLE ARE BEING MORE SELECTIVE ABOUT WHERE THEY WANT TO BE ACTIVE AND WHERE THEY WANT TO BE PASSIVE, AND THAT IS ALL CONNECTED TO THE WHOLE ‘SMART BETA’ DISCUSSION. SO I THINK THERE WILL BE MORE MOVEMENT TO PASSIVE BUT MORE FLOWS INTO SMART BETA WHERE THERE CAN BE BETTER WAYS TO CONSTRUCT INDICES.”



“ACTIVE AND PASSIVE CAN CO-EXIST BUT THERE IS CLEARLY INCREASED FOCUS ON TRANSPARENCY WHICH HAS LED TO COST BEING THE OVERRIDING FACTOR. VALUE NEEDS TO RE-ASSERT ITSELF AND ACTIVE MANAGERS NEED TO DEMONSTRATE THEY CAN CONSISTENTLY ADD VALUE, AND FOR ME IT’S THAT WORD CONSISTENCY...PASSIVE STRATEGIES CAN’T BE COMPLETELY DYNAMIC AND IN TODAY’S EVER CHANGING WORLD YOU NEED THAT.”



The active vs passive debate has been fuelled from two areas during 2014:

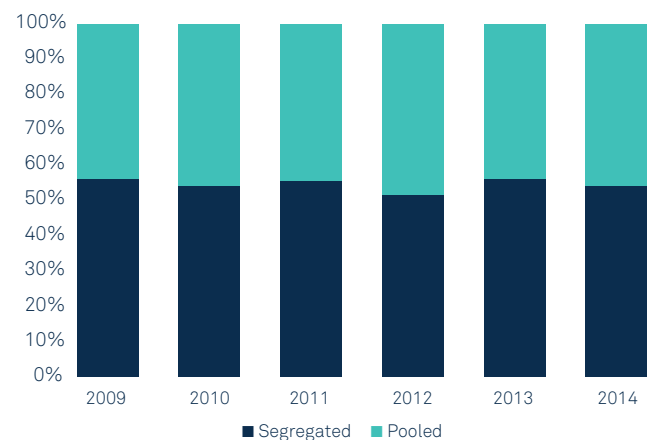
- Intensification of the debate about the relative cost and delivery of active and passive management. The Government put forward proposals that the Local Government Pension Schemes (LGPS) in the UK should shift to passive listed investments via collective vehicles to reduce costs.
- The announcement in March 2014 of the introduction from March 2015 of a charge cap of 0.75% on default funds being used for the purposes of automatic enrolment. The cap covers all member borne charges including investment management (excluding transaction costs) and administration.

SEGREGATED MANDATES AND POOLED VEHICLES

The means by which investment management services are accessed will differ by investor type. Retail investors typically invest via pooled vehicles such as OEICs and UCITS funds, but institutional investors more generally invest via a combination of pooled and segregated investments depending on fund size and asset class.

The balance between segregated and pooled assets remained stable again in 2014. Fifty four percent of assets were managed in segregated mandates, compared to 46% in pooled vehicles - almost unchanged from 2013.

CHART 14: SEGREGATED VS. POOLED ASSETS AS PROPORTION OF TOTAL UK ASSETS UNDER MANAGEMENT (2009-2014)



2 SHAPING THE FUTURE OF ASSET MANAGEMENT

KEY FINDINGS

THE IMPORTANCE OF THE UK AS A CENTRE FOR ASSET MANAGEMENT

▶ THE UK IS SECOND ONLY TO THE US, WHICH HAS AN ESTIMATED \$37 TRILLION (£24 TRILLION) UNDER MANAGEMENT

- The UK remains the largest asset management centre in Europe. The gap to the next largest country widened to 17 percentage points at the end of 2013 (from 16 percentage points in 2012).
- 57% of assets managed in the UK, are managed by asset managers with overseas parent organisations, up from 39% a decade ago.
- The value of overseas domiciled funds managed in the UK increased by 16% year-on-year to £895 billion.
- The proportion of assets run by independent asset managers increased again to 41%, from 37% last year and from 15% in 2003.

▶ TRANSFORMATION IN RETIREMENT SAVING

- The asset management industry already has a wide product offering that is likely to require evolution, rather than revolution, to meet the needs of the new market.

MEETING CLIENT EXPECTATIONS

▶ AS PEOPLE LIVE LONGER AND KEEP ASSETS INVESTED THROUGHOUT RETIREMENT, THERE IS LIKELY TO BE MORE DEMAND FOR OUTCOME-FOCUSED FUNDS, INCOME GENERATION AND MORE DIVERSIFIED MULTI-ASSET PORTFOLIOS.

- Investment solutions may need to interact with annuities, which are still likely to play some role for a portion of retirement assets, or in the form of deferred annuities.

- Downside capital protection will be key to a risk-averse client base.
- Increasing trust and confidence will require higher levels of transparency to the end investor.

MULTIPLE LEVELS OF SCRUTINY

▶ CHANGES IN THE POLITICAL AND REGULATORY ENVIRONMENT, AS WELL AS IN CLIENT EXPECTATIONS, ARE COMBINING TO INCREASE SCRUTINY OF THE INDUSTRY.

- The scrutiny is seen in multiple areas, including fees, broader disclosure, the systemic significance of managers and their wider role in the economy (notably, stewardship responsibilities).
- Firms recognise more still needs to be done to improve client trust, with a particular focus on better communication.

WIDER USE OF TECHNOLOGY

▶ THE KEY DANGER POINT FROM TECHNOLOGICAL DEVELOPMENT IS DISTRIBUTION.

- 'Big data' will be transformational in many aspects of the product design, manufacture and distribution process.
- Improved digital communication with investors opens up potential for direct to consumer distribution.
- In terms of external disrupters, the key concern is in the area of distribution rather than product manufacture.

2 SHAPING THE FUTURE OF ASSET MANAGEMENT

This chapter looks at the key factors shaping the asset management industry at the end of 2014 and brings together data points from within this report, as well as insights from member interviews and external sources.

FIGURE 3: KEY FEATURES OF THE ASSET MANAGEMENT INDUSTRY AT THE END OF 2014

Importance of the UK as a centre for asset management

- In an increasingly global industry, the UK faces the challenge of consolidating and building on its position as a centre for excellence in asset management.
- In the mutual fund arena, the UK remains behind Dublin and Luxembourg as a fund domicile.
- The volume and variety of UK, European and Global regulatory initiatives continue to impact on the value chain.
- The shape of the industry is changing with more assets being managed by independent asset managers.

A transformation in retirement savings

- In the UK, automatic enrolment has created five million new pension savers since 2012.
- Changes to annuity rules have increased choice and the potential for investor engagement throughout retirement.
- The rate and scale of change provides opportunities but also significant responsibility for the asset management industry.

Meeting client expectations

- The industry continues to evolve away from the component-based benchmark focus that characterised it a decade ago.
- Product demand in both the retail and institutional markets reflects this structural shift as well as more cyclical trends.
- Income is a key theme across client groups as maturing DB schemes look to manage cash flows and DC pensioners and retail investors negotiate the low interest-rate environment.
- The ongoing closure of DB schemes and importance of DC as a conduit for automatic enrolment continues to place more focus on individual investors.

- Retail and DC investors' fear of loss means greater prioritisation of capital preservation is becoming paramount.
- Saver trust in financial services remains critically low following the financial crisis.

Multiple levels of scrutiny

- The shift towards passive strategies is escalating pressure on active managers to demonstrate their added value in a challenging return environment.
- Following the banking crisis, there is growing scrutiny of the potential for asset management to pose a systemic risk to the UK economy.
- There are growing demands on asset managers to act as responsible stewards of client assets as part of a wider focus on the role of market-based finance.
- Greater transparency is demanded across all aspects of the industry.

THE IMPORTANCE OF THE UK AS A CENTRE FOR ASSET MANAGEMENT

The US remains the largest centre of asset management by far, accounting for half of global assets under management (total global assets stood at \$74 trillion, £47 trillion, at the end of December 2014).

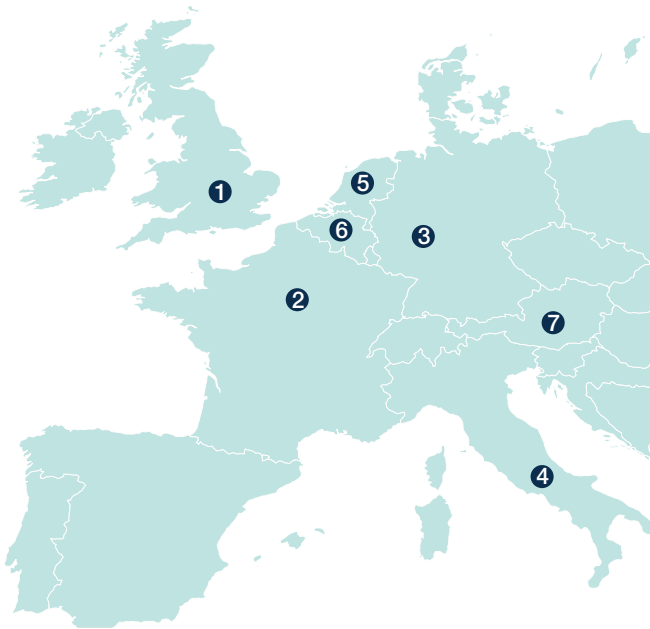
At the end of March 2014 (latest data available) assets managed by asset management companies in Japan were estimated to be £2.2 trillion (¥415 trillion)¹³. This is a slight increase from ¥387 trillion in March 2013 but represents a fall in sterling terms (from £2.8 trillion) as a result of the yen weakening by around 7% versus the pound during the year.

Closer to home, the UK continues to dominate the asset management industry within Europe, with its market share increasing from 35% in 2012 to 37% by the end of 2013 (latest available data).¹⁴ The UK has more in assets under management than the total amount managed in the next three largest European countries added together.

¹³ Nomura Research Institute. Japan's Asset Management Business 2014/2015

¹⁴ The 12% increase in assets in euro terms managed in the UK reflects a small weakening in the pound versus the euro during 2013 of around 2% and is therefore slightly lower than the actual growth reported in last year's Asset Management Survey of 13%.

FIGURE 4: ASSETS UNDER MANAGEMENT IN EUROPEAN COUNTRIES (DECEMBER 2013)



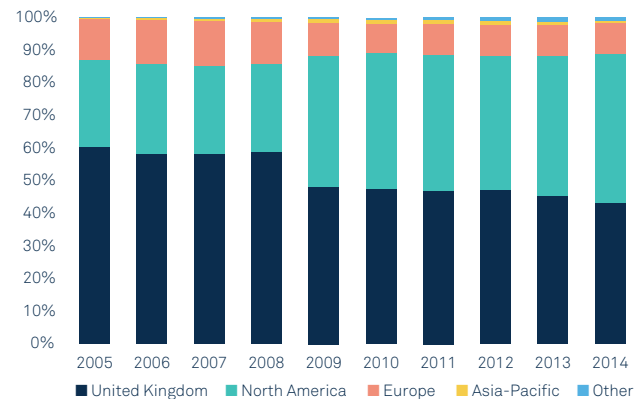
| Country | Net assets (€bn) | Market share |
|--------------|------------------|--------------|
| UK | 6,101 | 37% |
| France | 3,258 | 20% |
| Germany | 1,613 | 10% |
| Italy | 881 | 5% |
| Netherlands | 469 | 3% |
| Belgium | 229 | 1% |
| Austria | 85 | 1% |
| Other | 3,820 | 23% |
| TOTAL | 16,456 | |

Source: EFAMA

In previous surveys we have highlighted the increasing internationalisation of the asset management industry. Over recent years the UK has benefited from managing assets for organisations headquartered overseas, especially in the US. Chart 15 shows:

- UK-owned asset managers now account for 43% of total assets under management compared to 61% ten years ago.
- The proportion of assets managed in the UK for US-owned asset managers has increased to 46% from 25% a decade ago.
- Assets managed on behalf of European-owned firms have fallen. However, the level has remained largely stable at around 9% since 2010, following the initial disruption caused by the financial crisis.
- Firms from Asia-Pacific and other regions remain unchanged at 1% of assets each.

CHART 15: ASSETS UNDER MANAGEMENT BY REGION OF PARENT GROUP HEADQUARTERS (2005-2014)



Under its Investment Management Strategy, the UK Government has committed to ensuring that the UK will remain competitive when organisations are deciding where to carry on their business.

Specifically, the Government has said it will:

- Simplify and streamline taxes in the sector.
- Create a more responsive regulatory environment.
- Improve marketing here and overseas to promote the UK as an international investment management centre.



Firms interviewed as part of the survey this year welcomed the steps made in the promotion of the UK but stressed the importance of maintaining and improving the competitiveness of the UK as an attractive centre for asset management.

“FROM THE TOP DOWN, THERE SHOULD BE BROADER RECOGNITION THAT THIS IS AN INDUSTRY WHICH IS GLOBAL AND INCREASINGLY CAN BE LOCATED ANYWHERE. THERE IS REAL BENEFIT TO UK PLC THROUGH HAVING A HEALTHY CLUSTER OF HIGH QUALITY ASSET MANAGEMENT COMPANIES, BOTH IN EARNINGS AND EMPLOYMENT TERMS.”

“INVESTOR PROTECTION COMES FROM A STRONG ROBUST AND COMPETITIVE INDUSTRY. THE GOVERNMENT NEEDS TO MAKE SURE WE ARE COMPETITIVE AND ATTRACT THE BEST CAPITAL, TALENT, THINKING, PRODUCTS OF WHICH UK AND INVESTORS AND THE ECONOMY ARE A BENEFICIARY.”

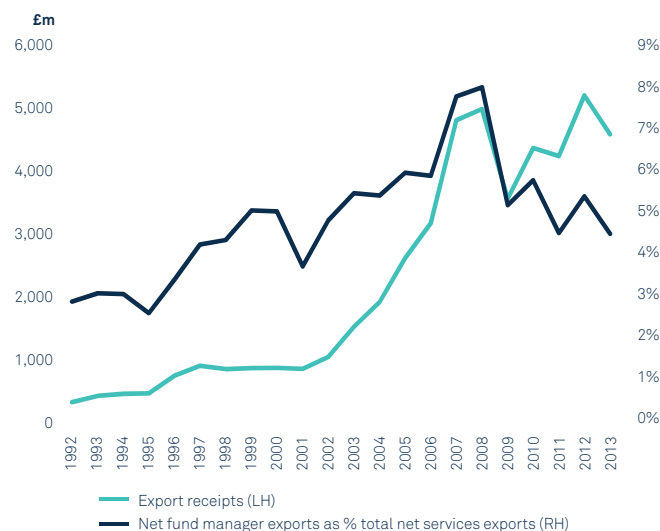
They also emphasised the broader importance of the international dimension in creating a virtuous cycle of quality and innovation that benefits both the UK industry and its domestic client base. Attracting investment and global talent promotes high quality asset management activity in the UK. This in turn is likely to boost the industry’s reputation, benefiting the UK economy and attracting further talent and investment from abroad.

CONTRIBUTION TO EXPORT EARNINGS.

At the end of 2014, 39% of assets managed in the UK were managed on behalf of overseas clients, consistent with the findings in 2013.

Looking at wider data, one proxy for monitoring the international nature of asset management is its contribution to net export earnings. Asset managers have represented an average of 6% of total net exports over the past ten years, although as Chart 16 indicates there has been significant volatility in this figure in recent years, partially driven by the lower contribution from financial services as a whole immediately after the financial crisis. As a proportion of financial services exports the contribution of asset management has been more stable, averaging 10% since 2005.

CHART 16: EXPORT EARNINGS OF FUND MANAGERS AND CONTRIBUTION TO SERVICES EXPORTS (1992–2013)



Source: ONS

OVERSEAS DOMICILED FUNDS WITH UK ASSET MANAGEMENT

The value of overseas domiciled funds managed in the UK increased by 16% during 2014 to reach £895 billion at the end of year.

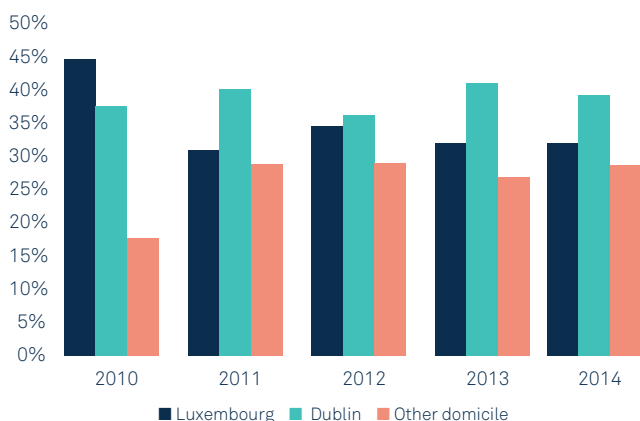
This growth bucks the trend in recent years, which has seen assets managed for the UK-domiciled market increasing at a faster rate than overseas domiciled funds (see Chart 17).

CHART 17: UK AUTHORISED FUNDS VS. OVERSEAS-DOMICILED FUNDS WITH ASSETS MANAGED IN THE UK (2010-2014)



In terms of the location of overseas-domiciled funds, Dublin is the largest source of assets, followed by Luxembourg (see Chart 18).

CHART 18: LOCATION OF OVERSEAS-DOMICILED FUNDS WITH UK-MANAGED ASSETS (2010-2014)



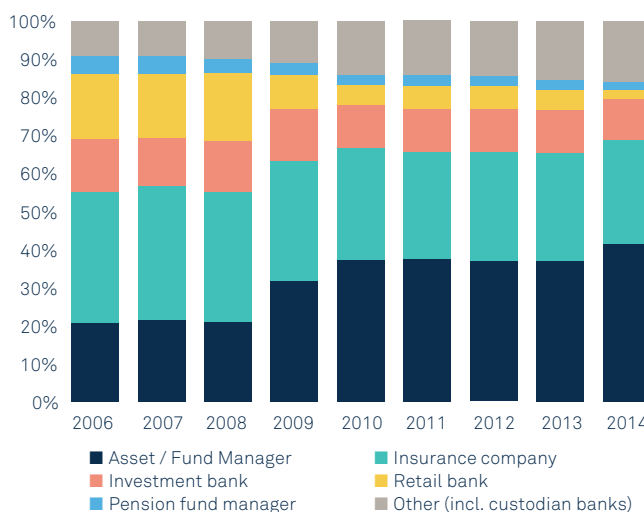
A wide range of locations were cited in the ‘other’ domicile category. The most common were the US, the Cayman Islands, Bermuda and the Channel Islands. However, UK asset managers manage money for funds around the globe in North and South America, Asia and Australia.

OWNERSHIP

Over the past few years there has been something of a structural shift in the ownership of asset management companies. The proportion of assets run by independent asset managers has grown significantly, up from 16% a decade ago to 41% in 2014.

This has increased from 37% last year and we have also seen a small drop in insurance company owned managers as a consequence.

CHART 19: BREAKDOWN OF UK ASSETS UNDER MANAGEMENT BY PARENT TYPE (2006-2013)



A TRANSFORMATION IN RETIREMENT SAVING

At the end of December 2014 there was approximately £2.1 trillion in UK pension assets in the UK.¹⁵

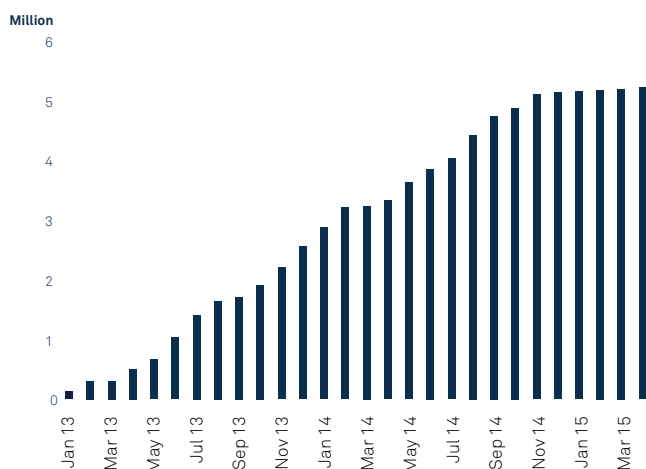
Back in the 1980s the majority of pension scheme members were beneficiaries either of a DB ‘promise’ or a with-profits insurance fund. DB assets still represent the bulk of pension assets in the UK (71%, or £1.5 trillion) but when the pension split is viewed in terms of the number of current members it is evident that the direction of flow of assets into the pensions market will make DC far more important to the asset management industry in the UK in the coming years.

¹⁵ Global Pension Assets Study 2015, Towers Watson



Over five million people have been automatically enrolled into a workplace pension since its launch in October 2012.

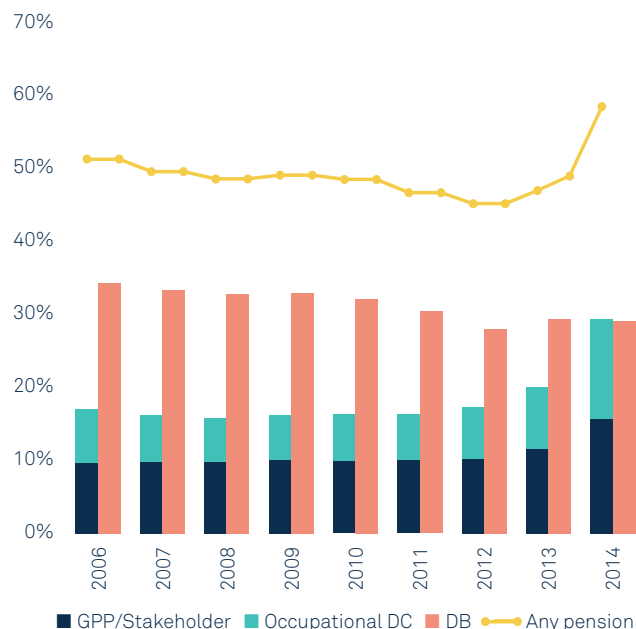
CHART 20: NUMBER OF EMPLOYEES AUTOMATICALLY ENROLLED TO DATE



Source: The Pensions Regulator

Membership of workplace pension schemes has increased to 59% of the workforce in 2014 from a low of 46% in 2012. The increase was primarily driven by increases in membership of occupational DC schemes, group personal pension (GPP) and stakeholder schemes following the introduction of automatic enrolment. For the first time since 1997 occupational DC schemes represented more than half the total active workplace pension membership in the UK.¹⁶

CHART 21: PROPORTION OF EMPLOYEES WITH WORKPLACE PENSIONS BY TYPE OF PENSION (2006-2014)



Source: ONS

The use of trust-based schemes has accelerated compared to contract-based schemes in the past year, which may reflect the greater likelihood of smaller employers using master trusts to fulfil their automatic enrolment obligations. The government-created National Employment Savings Trust (NEST), which has a universal service obligation, is a multi-employer trust-based scheme. At least 3.4 million people have so far been automatically enrolled into the two largest mastertrust providers.¹⁷ This is somewhat contrary to general industry expectations three years ago that the future of defined contribution pensions was likely to lie in contract-based schemes.

¹⁶ ONS, ASHE Pension Tables 2014

¹⁷ NEST had 2 million automatically enrolled members at 25 March 2015. The People's Pension had automatically enrolled 1.4 million at end June 2015.

The evolution may reflect the greater focus on governance issues, which is also affecting the delivery of contract-based schemes. Contract-based workplace pensions, such as group personal pensions and group SIPP are, from April 2015, required to put in place Independent Governance Committees (IGCs), which will act in the interests of scheme members in assessing the value for money of workplace pension schemes.

In asset terms the impacts of automatic enrolment are yet to bite as contributions from both employers and employees remain low. The minimum total contribution requirement under automatic enrolment is only 2% until September 2017. Not until October 2018 does that increase to 8%.

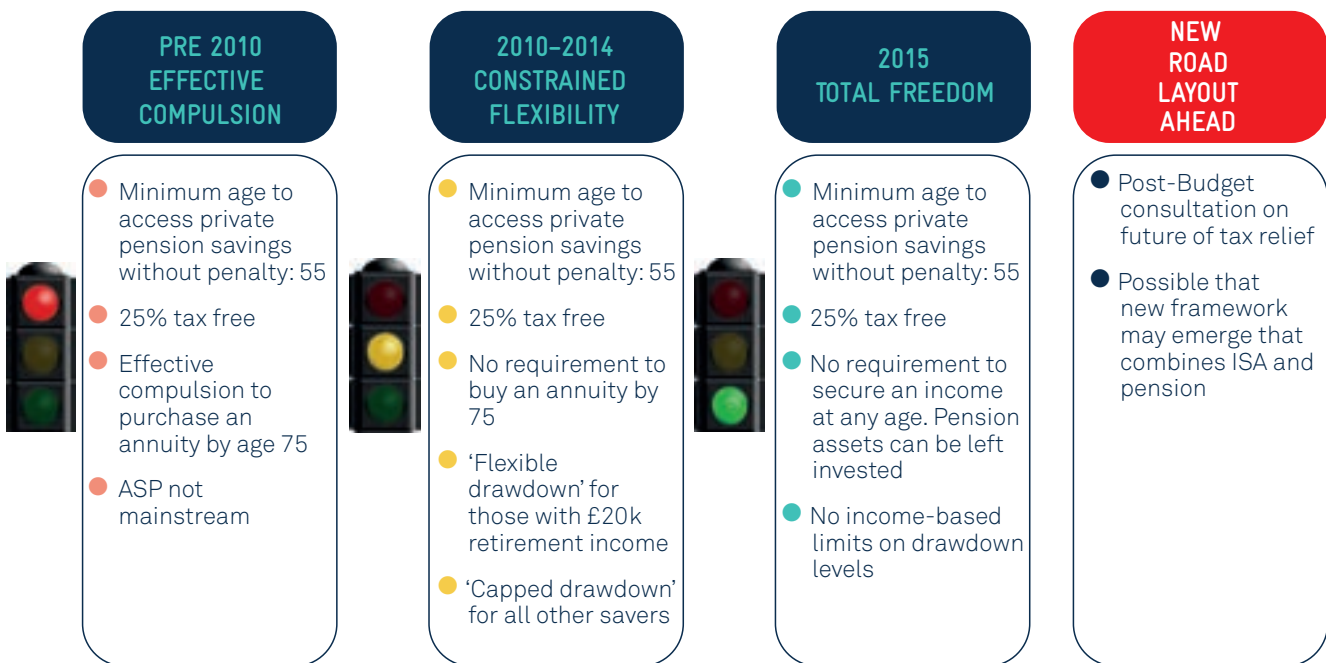
The increase in DC pension saving, much of which will be incorporated in the assets managed by members of The Investment Association on behalf of pension providers (both insurance companies and master trusts), will continue to blur the boundary between retail and institutional. In a DB arrangement the asset manager manages pension assets on behalf of an institution that is ultimately responsible for meeting the scheme liabilities. As DC becomes more dominant,

asset managers will increasingly be managing the retirement savings of individuals, who will each be bearing the investment risk associated with their own investment choices, whether those choices are proactive or entered into by default.

Over time, this is likely to significantly change the relationship between asset managers and individual savers. This is particularly true in light of the new budget freedoms announced in 2014, which removed the existing effective requirement for the majority of pension savers to purchase an annuity at retirement. Indeed, individuals may now leave their assets invested throughout their retirement. The 25% tax free allowance still remains but savers may now access the remainder of their pension savings in far more flexible ways, such as:

- Withdrawing cash in a single lump sum, paying the marginal rate of income tax on any amount over the 25% tax free allowance.
- Drawing down their savings as required, with each withdrawal being 25% tax free and the remainder taxed at the individual's marginal rate, effectively spreading the 25% tax free allowance over time.

FIGURE 5: THE ROUTE TO PENSION LIBERALISATION



In Budget 2015 these freedoms were extended to enable, in principle, pensioners to exchange existing annuities for a cash lump sum, although this has now been delayed until 2017.

The Government estimates that by the time automatic enrolment is fully rolled out it could potentially bring in nine million new pension savers. Consequently, there is no doubt that the new freedoms offer significant opportunities for the asset management industry but they also mean the industry has an increasing level of responsibility to the individual investor as the risk shifts to them via the increased use of DC provision.

As life expectancy increases we could see people continuing to invest substantial sums well into their later years.

In the Summer 2015 Budget the Government also announced a consultation on the future of tax relief that could lead to a new framework emerging that would combine ISA and pension saving. This could lead to a radical simplification of the retail savings environment.

We asked members how they are likely to respond to these opportunities and challenges. The general view of industry leaders was that the new pension freedoms will require an evolution of the existing investment offerings but that the changes will not be revolutionary.

“OVER TIME WE SEE OPPORTUNITIES FROM THE SHEER VOLUME OF THE MARKET THAT MAY NOT BE IN ANNUITIES. WE HAVEN'T MADE ANY SPECIFIC CHANGES AS WE'VE LAUNCHED A RANGE OF MULTI-ASSET AND INCOME-FOCUSED FUNDS FOR THE WIDER MARKET WHICH ARE SUITABLE. A LOT OF WHAT WE SELL IS ONTO PLATFORMS WHERE IT'S WRAPPED SO WE ARE NOT DEVELOPING THE WRAPPERS BUT THERE MAY BE MORE DEMAND FROM THAT AREA.”



“THE PENSION REFORMS ARE A CHALLENGE AS WELL AS AN OPPORTUNITY. MAKING SURE THAT, AS AN INDUSTRY, WE HAVE THE RIGHT TYPES OF PRODUCTS FOR DC INVESTORS THAT ENCOURAGE SAVING. IF SAVERS HAVE A BAD EXPERIENCE IN TERMS OF INVESTMENT OUTCOMES, THAT MAY NOT BE THE WAY TO GET THOSE SAVERS BACK. THE PRODUCTS NEED TO BE DESIGNED TOWARDS RETIREMENT INCOME AND WE NEED TO ENSURE THAT WE CAN CONNECT THE DOTS BETWEEN ASSET MANAGEMENT AND INSURANCE-BASED SOLUTIONS. COMMUNICATION AROUND THIS IS GOING TO BE ONE OF THE BIGGEST CHALLENGES.”



MEETING CLIENT EXPECTATIONS

When considering the types of strategy that would be necessary to meet the expectations of individuals in retirement the most common term used among members interviewed this year was 'solutions-based', continuing a similar trend seen over the past five years. The general view was that members had not felt the need to create a wide range of new products and that the knowledge and expertise to meet client objectives already existed. However, there will need to be an ongoing evolution of strategies as demand from clients becomes clearer.

As people live longer and retire later, asset managers most commonly expect to see demand for:

- Outcome focus
- Income generation
- Capital protection
- Multi-asset portfolios offering greater diversification and risk management.

A number of respondents had developed, or were in the process of developing, 'target date funds' (TDFs) that could apply an appropriate de-risking strategy to individual's assets. However, the challenge for TDFs is that there is no longer a set retirement date and individuals are likely to retire at widely different ages and more commonly incorporate part-time working into their retirement than they do today.

"WE ARE ALREADY SEEING INCREASING DEMAND FOR OUTCOME FOCUSED WHICH HAS BEEN A REAL CHALLENGE TO CLASSIFY BECAUSE THEY ARE NOT ALL SIMPLE OR DOING THE SAME THING."

"WE ARE NOT TALKING TDF TERMINOLOGY AS WE DON'T THINK PEOPLE HAVE TARGET RETIREMENT DATES SO IT'S ABOUT A SENSIBLE DE-RISKING STRATEGY BUT NOT AIMED AT A SPECIFIC DATE."

"MOST OF THE FUNDS EXIST – YOU WILL SEE MORE EMPHASIS ON OUTCOME-FOCUSED AND ON INCOME-BASED FUNDS. THEY'LL INCREASE IN DEMAND. ONE OF THE BIGGER OPPORTUNITIES FOR ASSET MANAGERS IS THAT WHEN PEOPLE ARE GIVEN MORE CHOICE THEY TEND TO SPEND MORE TIME IMPROVING THEIR UNDERSTANDING."

"PEOPLE WANT REAL RETURN WITH DOWNSIDE PROTECTION. THEN OF COURSE INCOME IS A BIG CONCERN AND WE ARE SEEING A LOT OF INTEREST IN EQUITY INCOME AND MULTI-ASSET INCOME. PEOPLE ARE CONCERNED ABOUT INCOME STREAMS."

It is still too soon to determine what savers will actually do with their pension savings, but recent research suggests that the emphasis from members of The Investment Association on income generation is well-placed. Only 12% of those asked recently thought they were likely to take their entire pension in cash. More than two thirds expected to take some form of regular or guaranteed income. However, one fifth did not know what they planned to do with their pension pot, which highlights the difficulty asset managers are facing in developing strategies that can de-risk in the most appropriate way on the run up to retirement.¹⁸

¹⁸ NEST insight 2015 Taking the temperature of auto enrolment. Based on representative sample of all ages

TABLE 4: LIKELY CHOICES OF PENSION SAVERS AT RETIREMENT

| | |
|---|--|
| ▶ | Leave assets invested and draw down an income. |
| ▶ | Secure a guaranteed income eg. purchase an annuity. |
| ▶ | Take as cash but invest in income generation eg. buy-to-let. |
| ▶ | Take as cash and spend as preferred. |
| ▶ | Mix and match approaches to suit requirements. |

THE ROLE OF ANNUITIES

With annuity rates at their lowest level for two years it is difficult to see any sustained increase in demand for the time being. Demand for annuities was 55% lower in March 2015 than a year earlier.¹⁹ However, as illustrated in the table above, some savers are still expressing a preference to receive a guaranteed income from their pension savings. The feeling among members interviewed this year was that there is likely to be a place for annuities, albeit on a more limited scale, in two main ways:

- Using a portion of retirement funds to purchase an annuity to cover essential living expenses.
- Purchasing a deferred annuity to guarantee an income in the later stages of retirement.

“WHAT I THINK WILL HAPPEN IS THAT ANNUITIES WILL HAVE A ROLE FOR ALMOST EVERYONE BUT NOT AT 65. GROWTH IN DEFERRED ANNUITIES – IF PEOPLE INVEST IN THEM AS AN ASSET CLASS AS OPPOSED TO A CONTRACT IT COULD BE VERY MARKET CHANGING.”

“WE HAVE DEVELOPED A SERIES OF INCOME-GENERATING FUNDS TO PRODUCE AN ANNUITY-LIKE STREAM OF CASH WITH HALF THE VOLATILITY OF EQUITY..... THERE IS A PROPENSITY TO PUT IN PLACE COMPLICATED ARRANGEMENTS. THAT’S ALRIGHT WHEN YOU ARE 55 BUT WHEN YOU ARE 80 PEOPLE AREN’T INTERESTED...WHAT TO DO AT THE BACK END IS THE CHALLENGE.”



A continuing role for annuities suggests that product innovation is likely to be driven by cross-industry collaboration as insurers and asset managers work together in the retirement market to meet the needs of savers.

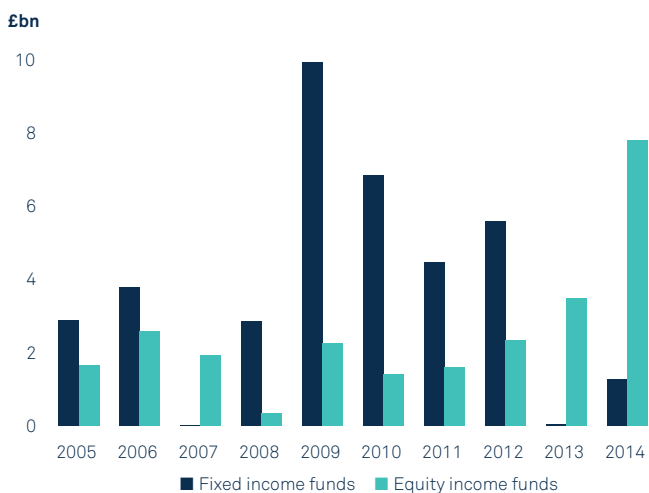
THE DIFFERENT NEEDS FOR INCOME

The need to provide income to those in retirement as a result of the pension freedoms is evident but we have already observed income being in greater demand from the retail market. Investors are looking for an alternative to the low interest rates available elsewhere.

Flows into fixed income funds peaked in 2009-10, but have now recovered substantially from their low of 2013, when net flows reached only £30 million. 2014 saw that figure increase to £1.3 billion but that is still significantly below historical levels, likely reflecting the cyclical uncertainty currently affecting fixed income yields. Only 2013 and 2007 produced lower levels of net flows. Consequently, investors are exhibiting a strong preference for equity income and sales of equity income funds increased to £7.8 billion in 2014.

¹⁹ IRESS news release, 30 April 2015.

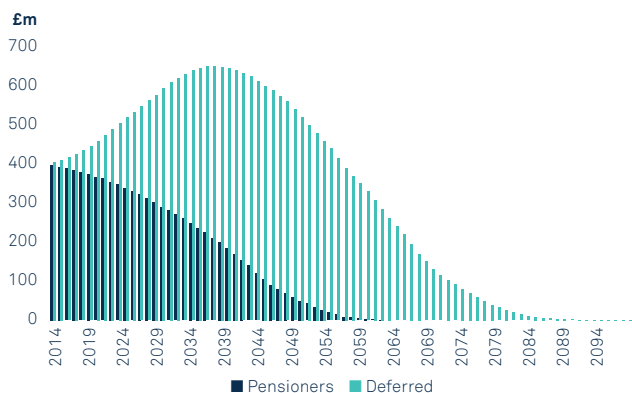
CHART 22: NET RETAIL SALES OF FIXED INCOME FUNDS AND EQUITY INCOME FUNDS (2005-2014)



Demand for income is not limited to the retail market. Members are also seeing a growing demand from the institutional market as DB schemes look to manage their liabilities and invest in ways that more accurately reflect their future cash flows.

Chart 23 illustrates the future cash flow demand of schemes transferred to the Pension Protection Fund. Although it does not encompass the entire DB market it is helpful in illustrating the shape of cash flow demand we can expect as the DB run-off progresses. It suggests that cash requirements are likely to increase until around 2037 before decreasing to near zero in about 75 years.

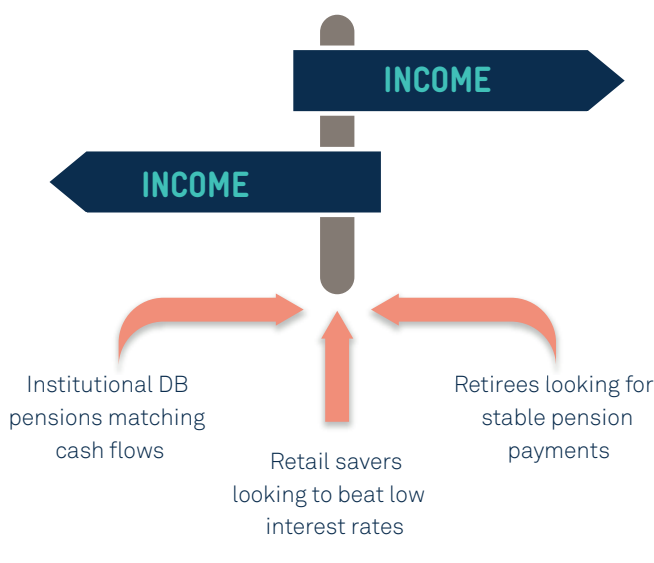
CHART 23: TOTAL EXPECTED FUTURE CASH FLOWS FOR SCHEMES TRANSFERRED TO THE PPF



Source: Pension Protection Fund

While DB schemes are open to new members or future accrual there will be some cash flowing into the scheme from pension contributions. However, as most schemes are now closed to new members, and many to future accrual for existing members, the need to generate cash from other sources is becoming more urgent. In a market where the natural fixed income investments have been expensive for a sustained period, schemes are looking for other sources to provide them with a reliable income stream.

FIGURE 6: THE MANY ROADS THAT LEAD TO INCOME



SCRUTINY OF THE ASSET MANAGEMENT INDUSTRY

In recent years, scrutiny of the asset management industry by regulators, government and clients has intensified at all levels. Some elements of this scrutiny have been driven directly by the reaction to the global financial crisis, for example the debate on systemic significance. Others, notably transparency and disclosure, date back much further but have been given a specific context in the UK by accelerating pension reform, including the new retirement income freedoms.

IMPACT OF REGULATION

In the UK, Europe and globally, regulatory demand has increased significantly. We asked members what they saw as the greatest emerging or regulatory challenge for their business. The two things most consistently mentioned during the interviews were:

- The volume of regulation currently being created in both the UK and Europe.
- The inconsistency of regulation, particularly for those managers that operate in markets globally.

“THE REGULATORY BURDEN IS THERE AND REAL. IT’S HARD TO BE A UK FIRM, IT’S EVEN HARDER TO BE A GLOBAL FIRM WITH REGULATORY CHANGE AROUND THE WORLD HAPPENING AT DIFFERENT PACES, AT DIFFERENT INTENSITY. A LOT OF TIME AND EFFORT GOES INTO THAT.”

“A REGULATORY TSUNAMI. WE DON’T KNOW WHAT THE RULES WILL BE EVEN THOUGH WE KNOW THE DEADLINE.”

Drilling down into specific areas, members most frequently referred to the levels of scrutiny on the industry and MiFID II as of greatest relevance to them:

- The asset management industry is under scrutiny as never before. In the FCA’s business plan 2015/16, the FCA’s continued focus areas for the asset management sector are pension reforms, increased competition, benchmarks, and the industry’s preparation for MiFID II/R and MAD/R changes. The FCA is also looking at charging, competition, and understanding customers. The review of how dealing commission is used to pay for research has been a major theme, alongside guidance on the use of hospitality.

“I UNDERSTAND WHY REGULATORS ARE WORKING AS THEY ARE BUT IT HAS TO BE MORE JOINED UP AND IT HAS CHANGED THE FACE OF OUR BUSINESS. PEOPLE TALK ABOUT FUND MANAGERS MAKING TOO MUCH MONEY – MAYBE FAIRLY, BUT THEY SHOULD ALSO TALK ABOUT THE AMOUNT OF MONEY SPENT ON CONTROLS AND THE INCREASE IN COST.”

- MiFID II will come into force on 2 January 2017 and will bring significant changes to the operation of both wholesale and consumer markets in the following areas:
 - Investor protection issues - Inducements.
 - All commodity derivatives that do not qualify as hedges for commercial activities will be subject to position limits (with certain exemptions).
 - High frequency trading.
 - Those derivatives that become subject to the central clearing requirement under EMIR will also be subject to an obligation to be traded on a MiFID trading venue to provide a check on OTC transactions.
 - The definition of algorithmic trading will be determined in the 2015 level 2 negotiations. Firms considered to be operating such technology will be subject to material additional systems and controls. It is expected the definition will be drawn very widely.

"MIFID II DEALS WITH ISSUES THAT ARE NOT NECESSARILY GOING TO SOLVE THE PROBLEMS OF OUR CLIENTS. IT'S A HUGE OPERATIONAL CHALLENGE. THERE IS NOT ENOUGH COST/BENEFIT ANALYSIS DONE BY REGULATORS. IT IS IMPORTANT PEOPLE RECOGNISE MIFID II ISN'T JUST ABOUT DEALING COMMISSION - IT IS FAR BROADER THAN THAT."

"MY WORRY IS THAT SOME OF THESE REGULATORY INITIATIVES ARE CONTRADICTIONARY AND THAT IS DIFFICULT WITH AN INTERNATIONAL BUSINESS. QUITE APART FROM WHETHER YOU LIKE THE REGULATIONS IT'S WHETHER YOU CAN MAKE SENSE OF THE ARBITRAGE."

Full details of these and other regulatory issues affecting asset management can be found in Appendix Three.

BUILDING TRUST AND CONFIDENCE IN ASSET MANAGEMENT

Financial services continues to be the least trusted industry globally, and financial advisers/asset management are less trusted than banks and insurance. Trust is much lower in the UK and the rest of Europe than in other parts of the world, with levels of trust in Asian-Pacific countries significantly higher, although trust in financial services in the UK did increase slightly in 2014 (to 37% from 35%).²⁰

Members consulted in the writing of this survey felt the industry as a whole and firms individually had made progress in building trust in UK asset management but that a lot more needed to be done both individually and collectively.

"A LOT HAS BEEN DONE ACROSS THE INVESTMENT INDUSTRY TO ENGAGE WITH CLIENTS AND THEIR ADVISERS BUT THE UNFORTUNATE FACT IS THAT TRUST AND CONFIDENCE STILL HAVE TO BE STRENGTHENED AND WE NEED TO RECOGNISE THAT FOR ALL WE HAVE DONE SO FAR MORE REMAINS TO BE ACHIEVED."

Trust is a particular issue in retail financial services, but it is important to appreciate there is a difference between consumer trust in the asset management industry and consumer trust in individual asset managers. Trust in individual providers is influenced by a number of factors, including:

- Effective communication
- Integrity
- Expertise
- Values
- Concern about customers' interests

Research has shown that consumer trust in individual financial services providers is consistently higher than trust in the industry as a whole, and trust in investment companies can be higher than trust in a number of other organisations with which individuals have contact, such as their supermarket, mobile provider or even the NHS.²¹

²⁰ Edelman TrustBarometer 2014, Annual Global Study

²¹ Financial Services Research Forum, Research Note: Trust: Trends and Analysis, September 2012

“THAT IS WHERE BRANDING IS IMPORTANT BECAUSE WHAT THEY BUY IS TRUST SO WE HAVE AN ENORMOUS RESPONSIBILITY. WE TRY TO MAKE IT CLEAR INTERNALLY THAT THERE IS A PERSON AT THE END THAT IS OUR CLIENT – NOT JUST A PENSION TRUSTEE OR A CONSULTANT.”



The most significant factor members interviewed this year felt was important to build trust and confidence was for asset managers to have a greater focus on the underlying investor, taking a client-centric approach to designing investment strategies, rather than designing ‘off the shelf’ products to sell to investors.

“WE HAVE HAD A MORE CLIENT-CENTRED APPROACH TO HOW WE DESIGN PRODUCTS AND ENGAGE. MORE OF A SOLUTIONS-ORIENTED APPROACH TO BUILDING FRONT OFFICE CAPABILITIES. HOW WE SET OUR PRODUCT STRATEGY IS MUCH MORE CLIENT CENTRIC THAN IT WAS IN THE PAST SO I THINK THAT’S A BIG STEP FORWARD.”



Members also recognised the importance of improving communications with clients but believed that this was sometimes difficult in a heavily intermediated environment. This is important, because trust between consumers and providers is typically strengthened by contact with frontline members of staff, which does not frequently occur in the asset management industry.

The importance of communicating effectively with investors and the potential for increased direct contact with consumers is a theme that will run throughout this survey as technological advances play an ever-increasing role in the delivery of asset management services. The use of social media was seen as vital in this area, with the potential for its use in building brand trust pointed out by a number of firms.

“IT’S BIZARRE YOU CAN PRICE SHOP FOR A BOOK BUT FUND MANAGEMENT STILL HAS LOADS OF LAYERS – IT IS MUCH LESS TRANSPARENT AND DIRECT. IF WE DON’T SORT OURSELVES OUT THERE WILL BE A NEW VARIATION ON IT THAT WILL BE VERY DISRUPTIVE. THERE COULD BE SOMETHING MORE APPEALING TO THE MARKET THAT IS MORE LIKE SUPERMARKET SHOPPING.”



Considering the industry more widely, factors mentioned as positive moves taken by the industry collectively included:

- The Statement of Principles for Investment Managers, setting out what the responsibility of managing other people’s money means in practice for corporate culture and individual mind-set.²²
- The accelerating move towards greater consistency and transparency of fee structures, although this was tempered by the fact that more still needs to be done. The industry is concerned also to try to ensure that the data is as meaningful to end users as possible.

“WE HAVE SPENT A LOT OF TIME TRYING TO MAKE SURE PEOPLE DON’T THINK OF US AS BANKERS BUT THAT DOESN’T ADDRESS THE ISSUE OF CREDIBILITY WHICH COMES DOWN TO COSTS, TRANSPARENCY OF COSTS, TRANSPARENCY OF WHAT THE INVESTMENT OBJECTIVE IS.”



²² The Investment Association–Statement of Principles

“WE HAVE SEEN SOME GOOD RESPONSES TO SOME OF THE GOVERNMENT INITIATIVES THAT HAVE COME OUT...WE ARE DOING WELL ABOUT BEING MORE INVESTOR FRIENDLY AND TRANSPARENT...IMPROVING OUR DISCLOSURES ALL THE TIME, LOWERING PRICES, BEST PRACTICE FOR COMMISSIONS. ASSET MANAGERS ARE EMBRACING THAT CHANGE – IT’S UNCOMFORTABLE IN SOME RESPECTS AND DIFFERENT BUT – SLOWLY BUT SURELY. WE NEED TO CONTINUE TO MAKE SURE WE DELIVER VALUE AND ACTIVELY PROMOTE WHAT WE DO AND HOW WE DO THINGS.”



Firms also reflected on different ways in which the industry could demonstrate its positive impact in a more tangible way to improve how it is perceived by the Government, regulators and end investors:

- Channelling funds from savers to investors via the capital markets as an important alternative source of capital in the face of reduced bank lending.
- Acting as responsible stewards for client assets.
- Taking a more holistic approach to managing client assets, moving away from the specialisation of management versus a specific benchmark and making more dynamic asset allocation to help maximise the chances of achieving the client’s objective.

“WE NEED TO RENEW THE DEBATE ABOUT THE VALUE OF FUND MANAGEMENT CAPITAL ALLOCATION, THE INVESTMENT RETURN ON SAVINGS TO SOCIETY AND THE PROVISION OF FINANCE FOR CAPITAL SPENDING, WHICH IS SADLY LACKING...THERE NEEDS TO BE MORE PROMOTION OF COOPERATION AND COLLABORATION TO SHOW THAT SAVERS, COMPANIES AND FUND MANAGERS ALL HAVE A VESTED INTEREST IN EFFECTIVE COOPERATION.”



SYSTEMIC RISK

Members interviewed recognised the need for a regulatory framework to protect the financial system and economy from any future financial crisis. Two global regulatory discussion bodies – IOSCO (the International Organization of Securities Commissions) and central banks’ club, the Financial Stability Board – have been attempting to devise such a framework for asset managers, among others. However, members were clear that the ‘too big to fail’ framework that quite correctly was applied to banks would be unsuitable for asset managers, partly because it is, if anything, the fund and not the manager that can have an impact. A manager’s collapse does not result in harm to customers’ investments because they are segregated from the manager’s balance sheet. Measures addressing the manager could, therefore, load costs onto managers without there being any risk identified, let alone mitigated.

Members have instead pointed IOSCO and the FSB towards the activities of any asset managers that might give rise to unsafe levels of interconnectedness and leverage on the part of funds, rather than individual firm or fund size.

A second question raised by IOSCO and the FSB concerned the theory that asset-price crashes can be systemic. This was the subject of some debate, since it appeared increasingly unlikely that this could be the case in the absence of banking collapses. In any case, members noted, the underlying investor is generally responsible for the overall asset allocation, with asset managers responsible only for tactical asset allocation.

“I HAVE NOT SEEN A COMPELLING ARGUMENT TO SAY THE ASSET MANAGEMENT INDUSTRY POSES A SYSTEMIC RISK TO THE ECONOMY SO STOP TREATING US LIKE WE DO. OUR SUCCESS DEPENDS ON LONG TERM RELATIONSHIPS WITH OUR CLIENTS. WE ARE NOT IN IT FOR TRANSACTIONAL ACTIVITY, WE ARE IN IT TO DELIVER LONG TERM RETURNS, MORE SO NOW THAN AT ANY OTHER POINT IN THE PAST SO TREAT US LIKE A LONG TERM PARTNER TO SAVERS’ CAPITAL – NOT BANKS.”



STEWARDSHIP AND ESG TRENDS

Members reported significant increases in the attention being paid to the stewardship activity being undertaken by asset managers.

- Industry representatives reported that stewardship was being driven as much by asset managers themselves as by clients. It was seen as one of the cornerstones of being an efficient allocator of capital as well as a key driver of investment returns.
- Clients are concerned about the alignment of interest between companies, board executives and shareholders and are looking for their asset manager to effect change that will have a meaningful impact on the return of the security. However, the level of direct involvement from clients varied significantly across client groups.

The former point was reinforced by The Investment Association’s annual report on adherence to the FRC’s stewardship code, which found that investment managers, life companies and pension funds are committed to engagement, albeit there is still room for improvement. Human resource dedicated to engagement had increased by 19 percentage points in the year to 30 September 2014 and over 80 per cent of that increase was represented by portfolio managers and analysts – showing that stewardship is increasingly becoming integrated into the investment process rather than being treated as a standalone activity. Three quarters of managers also reported that all or some of their mandates referred to stewardship.²³

When asked what proportion of their mandates had imposed some ethical, social or governance requirements, just over half of respondents to this question²⁴ reported they managed at least some portion of their assets on this basis (53%). Where respondents stated they did manage assets in this way on average one fifth of assets were subject to ESG requirements.

“[STEWARDSHIP IS] ALWAYS IN POCKETS. INCREDIBLE DEMAND IN CERTAIN COUNTRIES TO DELIVER PRODUCTS WITH ESG/SRI. THOSE POCKETS HAVE HAD A GOOD INFLUENCE ON THE REST OF THE WORLD.”

“THERE ARE SOME REALLY BIG PENSIONS THAT HAVE TAKEN IT SERIOUSLY FOR A LONG TIME AND THEY HAVE RAISED THE BAR RECENTLY SO I THINK IT WILL CONTINUE TO GROW IN IMPORTANCE. THE TYPE OF ESG INVESTMENT HAS MOVED FROM NEGATIVE SCREENING TO POSITIVE – REWARD GOOD BALANCED SCORECARD FIRMS.”

“WE ARE ALSO SEEING DC DEFAULT FUNDS REQUIRING AN ESG APPROACH. DC MOVES AN INSTITUTIONAL APPROACH TOWARDS RETAIL, WHERE MILLIONS OF PEOPLE WILL ACTUALLY HOLD THE PRODUCTS. IT WILL BE THE PENSION FUNDS THAT DRIVE MORE ESG MANAGEMENT, AS WE DON’T SEE DEMAND BEYOND THAT CURRENTLY.”

Concern among clients for ESG investing was far less marked outside some of the largest pension and sovereign wealth funds. However it was noted that there was an emergence of interest in ESG requirements in DC default funds and that, as more and more younger savers invest in pensions, the pressure on employers to consider ESG considerations when choosing a default fund for their pension offering may increase.

However, the current situation is supported by data collected on UK authorised funds, which are identified in accordance with the Experts in Responsible Investment Solutions (EIRIS) classification. There are a number of definitional issues in this area, but the ESG flag essentially covers funds investing with a Socially Responsible Investment (SRI) or an Environmental, Social and Corporate Governance (ESG) focus.

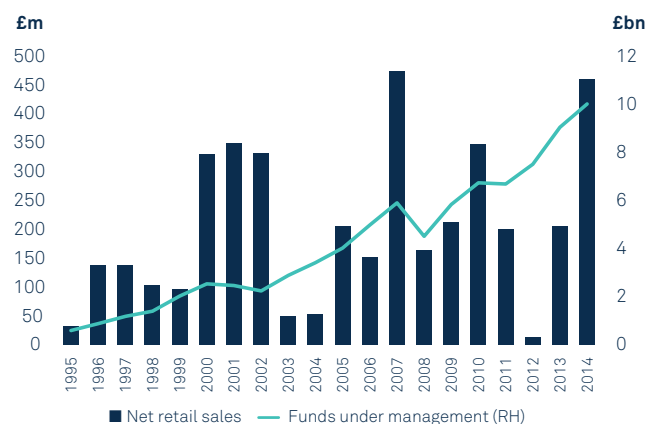
Chart 24 shows the evolution of ESG funds under management and net retail sales from 1995 to 2014. Net retail sales of ESG funds have seen an extraordinary rebound over the past two years and stood at £460 million in 2014. However, this rebound was from a very

²³ Adherence to the FRC’s Stewardship Code, At 30 September 2014

²⁴ 34 members responded to this question

low base and total assets under management in ESG funds remained at only £10 billion at the end of 2014, so annual fluctuations in sales can seem large but remain tiny compared to net sales of funds overall. It is therefore still too early to conclude whether or not this represents a significant change in investor behaviour or just year-on-year fluctuation.

CHART 24: ESG FUNDS UNDER MANAGEMENT VS. NET RETAIL SALES (1995-2014)



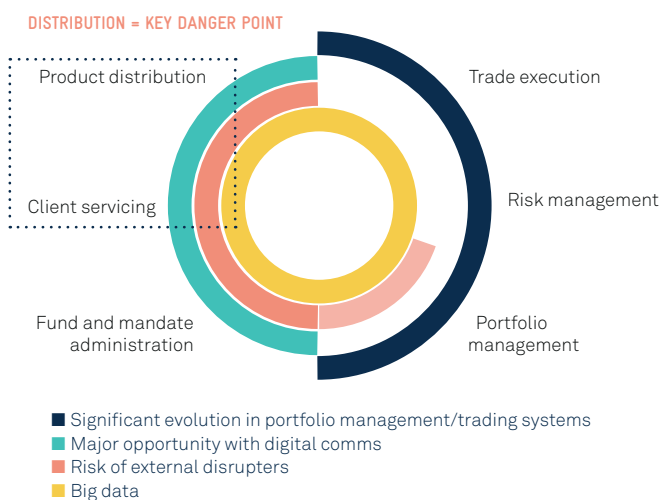
“THERE IS SOME MOMENTUM ON ESG – FROM YOUNGER GENERATIONS. IT WOULD BE WRONG FOR PEOPLE TO SUGGEST THESE ARE FACTORS WHICH WILL CONTINUE TO BE ONLY A SMALL PART OF THE INDUSTRY. AS THEY HAVE LARGER POTS THEY MAY WANT TO PUT MORE EMPHASIS ON ESG FACTORS.”

WIDER USE OF TECHNOLOGY

We explored two key ways in which advances in technology might affect the way asset managers conduct their business:

- Using technology to aid and improve the investment process.
- The potential for third parties, such as one of the large technology companies, to enter the industry in some way.

FIGURE 7: KEY THREATS AND OPPORTUNITIES – THE ROLE OF TECHNOLOGY



Members reported significant developments in portfolio management and trading systems but felt that developments in this area were an ongoing part of asset management. There were, however, a number of new areas in which they believed technology was influencing decision making in the asset management industry.

Big data refers to the use of data from numerous sources, such as social media news feeds or publicly available information, to provide insights that would otherwise not be available. The idea of 'big data' is commonly used in a number of sectors but is still a relatively new area to asset management.



FIGURE 8: KEY SOURCES OF BIG DATA



The main areas in which those we spoke to believed big data could be used in the investment management industry were in gaining insights into client preferences to help optimise investment solutions, particularly in an era which is likely to see increasing use of online tools to guide investment decisions.

“THE OTHER ELEMENT IS BIG DATA THAT FEEDS INTO OUR KNOWLEDGE OF THE CUSTOMER AND WHAT THEY WANT TO DESIGN OR ANTICIPATE THE KIND OF SOLUTIONS THAT ARE RIGHT FOR THEM. WHEN THEY ARE LOOKING AT THE END IT’S BEEN NARROWED DOWN BASED ON WHAT WE KNOW.”

Secondly, big data was seen as being of use in helping to monitor financial markets or companies. For example, using big data could help asset managers monitor the ESG activities of companies and reduce their reputational risk.

“BIG DATA PRESENTS INTERESTING OPPORTUNITIES FOR ANALYSIS, WHICH FEW ASSET MANAGERS ARE DOING TODAY. IT GIVES AN OPPORTUNITY TO DEEPEN OUR ANALYSIS OF WHAT WE UNDERSTAND ABOUT COMPANIES AND INVESTORS. SOME OF THE BIG RETAIL ORGANISATIONS MAKE HUGE USE OF THIS ALREADY TO THEIR ADVANTAGE.”

One other area in which big data analytics may also be used is in helping asset managers to meet stricter regulatory requirements by allowing them to better identify non-compliant or even fraudulent activity in their firm or helping them to identify and report suspicious transactions.

The area in which members felt technology could have the most transformational impact, and potentially posed the greatest risks to the industry, was in retail distribution.

“THIS IS ALL ABOUT DISTRIBUTION. HAVING AN IPHONE APP IS ONE OF THE BIGGEST OPPORTUNITIES AND THREATS FOR OUR WHOLESALE BUSINESS AND FOR THE REST OF THE MARKET BECAUSE WHEN TECHNOLOGY BECOMES AN END NOT A MEANS –WHAT A DISRUPTER THAT WOULD BE TO US...”

A number of industry leaders took the view that the increased use of digital technology for communication, particularly as younger savers feed through from the automatic enrolment market, will open up opportunities for external players to enter the market. The most likely contenders would be the large technology companies, that have experience in communicating in this way and benefit from much higher levels of consumer confidence than traditional financial services.

When it came to the provision of general news and information online search engines were found to be the most trusted source globally, trusted by 72% compared to 63% for traditional media.²⁵ Search engines are also the first port of call for people looking for general information and 'advice'. Such organisations are already using developments such as big data to understand their customers and could have a significant head start on the asset management industry in this regard.

"THERE IS A LOT OF EXAMINATION IN THE INDUSTRY ABOUT DISRUPTERS EG. IF WE ARE GOING MORE INTO THE RETAIL MONEY, ARE THERE PLAYERS THAT ARE BETTER PLACED TO GET THAT MONEY?...IT COULD BE THAT ASSET MANAGEMENT FIRMS GO DIRECT TO CONSUMER. IT'S EASY TO SAY BUT EXPENSIVE TO DO. THE BIGGEST SINGLE QUESTION IS HOW TO GET TO MARKET EG. VIA PHONES."

"ADVANCES OPEN UP DISTRIBUTION CHANNELS. IT ALLOWS DIFFERENT DISTRIBUTORS WITH GOOD RELATIONSHIPS WITH THEIR CUSTOMER TO OPEN UP THEIR BUSINESS TO INVESTMENT MANAGEMENT SERVICES. SOCIAL MEDIA COULD CHANGE THIS – FRIENDS RATING EXPERIENCES – LIKE TRIPADVISOR OR EXPEDIA"

However, the level and complexity of regulation and the increasing scrutiny on the asset management industry were seen as a significant barrier to new entrants from the technology sector in disrupting the delivery of asset management itself. It was felt that any disruptive capability would be limited to the area of distribution.

Consequently, a number of managers told us they were considering taking a more active role in the direct to consumer market. This is particularly relevant in light of the recent pension changes as many of those now approaching retirement but unsure how to invest may not be able to afford, or may simply choose not to pay for, advice.

"POST RDR I CAN COUNT ON ONE HAND THE NUMBER OF PEOPLE THAT WILL VISIT A FINANCIAL ADVISER – THEY WILL DO IT ONLINE THEMSELVES SO WE HAVE TO GIVE THEM THE TOOLS TO DO THAT OR WE WILL BE LEFT BEHIND."

Overwhelmingly, those interviewed believed that asset managers needed to improve their methods of communication with the end investors and to play a much greater role in improving financial literacy.

"WE NEED TO FACILITATE IMPROVEMENT IN FINANCIAL EDUCATION FOR ALL GENERATIONS AND THIS COULD BE A SIGNIFICANT OPPORTUNITY TO DRIVE AN INCREASE IN FINANCIAL AWARENESS AT GRASS ROOTS LEVEL. THAT WILL BODE WELL FOR THE INDUSTRY IN THE LONG TERM BECAUSE PEOPLE WILL INVEST IN MORE SOPHISTICATED PRODUCTS – OUR PRODUCTS"

"I THINK WE NEED TO FIND A WAY TO EXPLAIN AN INVESTMENT STRATEGY WITHOUT HAVING TO TEACH PEOPLE ABOUT DERIVATIVES AND BOND MATHS... WE HAVE AN OBLIGATION TO EXPLAIN AND WE FEEL THAT PEOPLE WILL COME TO THE TABLE. IN GENERAL PEOPLE WILL CARE ABOUT THEIR SAVINGS AND RETIREMENT."

A broader issue here remains how savers will be supported across working life and into retirement. The lack of clarity on the nature of guidance versus regulated advice continues to be a concern within the industry as well as to a wider set of UK stakeholders. With the announcement in the summer of 2015 of the Financial Advice Market Review, further Government action is likely.

²⁵ Edelman Trust Barometer 2015



3 UK INSTITUTIONAL CLIENT MARKET

KEY FINDINGS

MARKET OVERVIEW

 GROWTH IN INSTITUTIONAL ASSETS REMAINS STRONG AND INVESTMENT ASSOCIATION MEMBERS MANAGED AN ESTIMATED £2.8 TRILLION FOR UK INSTITUTIONAL CLIENTS AT THE END OF 2014.

- Pension funds accounted for more than half of these assets at £1.5 trillion (52%).
- Insurance assets represented 32% of institutional mandates, equivalent to £0.9 trillion.

THIRD PARTY MARKET

 AN ESTIMATED £2.1 TRILLION WAS MANAGED FOR THIRD PARTY MANDATES, WHICH EXCLUDE IN-HOUSE INSURANCE ASSETS AND ASSETS MANAGED IN HOUSE BY OCCUPATIONAL PENSION SCHEMES.

- Pension funds accounted for approaching two thirds of third party assets (£1.4 trillion).

PENSIONS

 DB PENSION SCHEMES CONTINUED TO DE-RISK BUT OVERALL PENSIONS STILL HOLD AROUND 45% IN EQUITIES – ONLY AUSTRALIAN PENSION FUNDS ALLOCATE MORE TO EQUITIES.

- LDI strategies continued to be popular among DB schemes. We estimate that including the notional value of liabilities hedged increases the size of the third party market from £2.1 trillion to £2.3 trillion.

MANDATE TYPES

 THE SHIFT AWAY FROM SPECIALIST MANDATES CONTINUED, IN FAVOUR OF MULTI-ASSET PORTFOLIOS AND LIABILITY DRIVEN INVESTMENT.

- The proportion of third party assets in specialist equity mandates fell from 47% to 43% year-on-year.
- Specialist fixed income mandates increased to 37% from 35% in 2013.
- The reduction in specialist UK equity mandates may be bottoming out as their allocation remained stable at 25%.
- Sterling corporate mandates remained the largest category of specialist fixed income mandate, making up 30% of specialist fixed income.
- 68% of third party institutional assets were managed on an active basis.
- 59% of third party mandates were segregated at the end of 2014, the same as last year.

3 UK INSTITUTIONAL CLIENT MARKET

This chapter explores the state of the UK institutional client market. The analysis differs from that in Chapter One in two important ways:

- It focuses on the nature of mandates 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 believe that an overwhelming majority of the assets continue to be managed in the UK (approximately 93%).

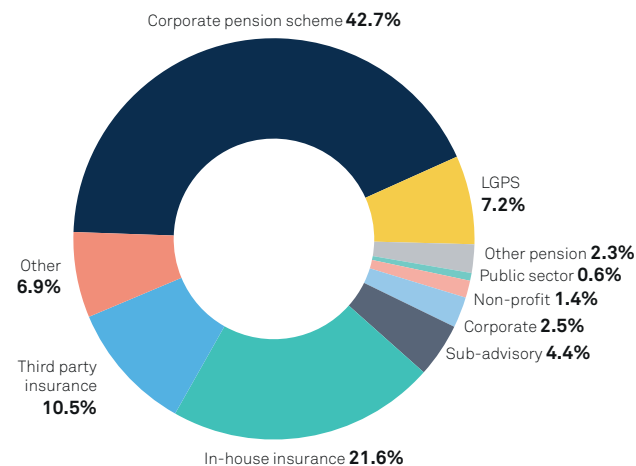
The data suggest that Investment Association members manage £2.8 trillion²⁶ for UK institutional clients globally.

Between them, pension funds and insurance companies account for just over 84% of the institutional client market (including in-house and third party management).

Investment Association pension fund data includes DB and DC schemes where the asset manager has a direct relationship with the fund – generally trust-based schemes. In 2014 pension funds continued to account for more than half of the institutional client base (£1.5 trillion).

DC pension assets that are operated via an intermediary platform are reflected in The Investment Association's insurance assets. Insurance mandates accounted for 32.1% of institutional business, almost unchanged from 2013. However, there has been something of a redistribution between in-house and third party managed insurance assets, which is likely to be in large part due to significant corporate ownership changes.

CHART 25: UK INSTITUTIONAL MARKET BY CLIENT TYPE



The remaining 16% was made up of mandates managed for corporations (outside of pension assets) sub advisory, not-for-profit mandates and public sector mandates. 6.9% remained assigned to 'other' client types, which 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.

In terms of distribution, the UK institutional market remains highly intermediated, with consultants playing a central role. In recent years, the boundaries between asset management and consulting in this market have become more blurred, with the emergence of implemented consulting and fiduciary management. Such approaches see the traditional roles of asset manager and consultant eroded, but data does not yet suggest extensive usage.

Nationally, 5% of DB pension schemes are thought to be using fully delegated fiduciary management. This figure increases to 8% if partially delegated mandates are included. However, the provision of fiduciary management is still skewed towards implemented consultants rather than specialist providers or investment managers.²⁷

²⁶ Implied figure based on data collected on an estimated 86% of institutional client base.

²⁷ 2014 KPMG UK Fiduciary Management Market Survey, Data as of June 2014

PENSION SCHEMES

The Investment Association divides pension scheme assets into three categories;

- Corporate pension funds, which represent the majority of assets. In 2014 corporate funds represented around £1.2 trillion of the £1.5 trillion total pension assets. This category includes a number of in-house Occupational Pensions Scheme (OPS) managers, which we estimate manage around £130 billion in assets.
- The LGPS, which accounted for around £205 billion of assets at the end of 2014.
- Assets managed for pension schemes that do not fit into either of these categories, such as those run for not-for-profit organisations, £65 billion.

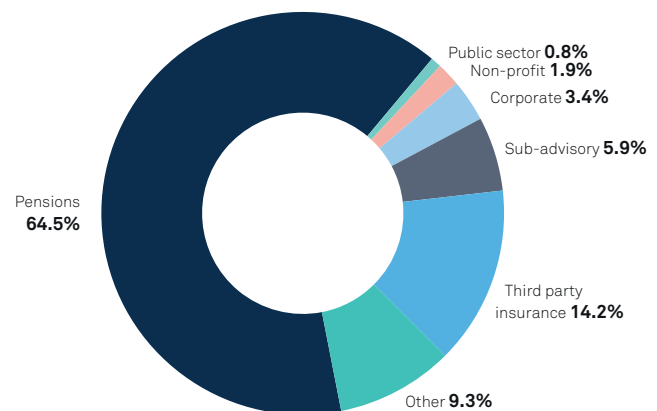
Corporate pension scheme assets are still dominated by DB schemes, which held £1.2 trillion in assets at the end of December 2014. These schemes are almost entirely closed to new entrants, only 13% were still open in March 2014 and almost a third had closed to future accrual for all members.²⁸ As these schemes continue to mature the pressure on schemes to de-risk their investment holdings becomes stronger.

Full details of the asset allocation and investment strategy of all UK institutional assets managed by Investment Association members are available in Appendix Two. The remainder of this chapter looks more closely at The Investment Association's data for institutional assets that are managed for third parties, therefore excluding mandates managed in house by insurance parent groups and internally-managed occupational pension schemes, as at the end of 2014. We estimate the size of this third party market to be £2.1 trillion.

THIRD PARTY INSTITUTIONAL MARKET

Once in-house insurance mandates are excluded, pension funds become even more dominant, representing nearer two thirds of assets, with the remaining insurance assets representing only 14% of the market.

CHART 26: THIRD PARTY UK INSTITUTIONAL CLIENT MARKET BY CLIENT TYPE



MANDATE BREAKDOWN

The following section breaks the institutional market down into three categories of mandate:

- Single-asset, or 'specialist' mandates, which might focus on a specific asset class or geographical region.
- Multi-asset, or 'balanced' mandates, which would cover a number of asset classes and regions.
- LDI mandates, which are specifically designed to help clients meet future liabilities.

Specialist mandates remain the most popular form of investment among institutional investors, with 64% of physical assets being managed on this basis for third parties, down one percentage point from 2013. Multi-asset mandates represented 14% of total assets and 22% of physical assets are represented by LDI mandates, most of which is held directly by segregated pension schemes, with a small proportion being held by other client types, most notably pooled funds.

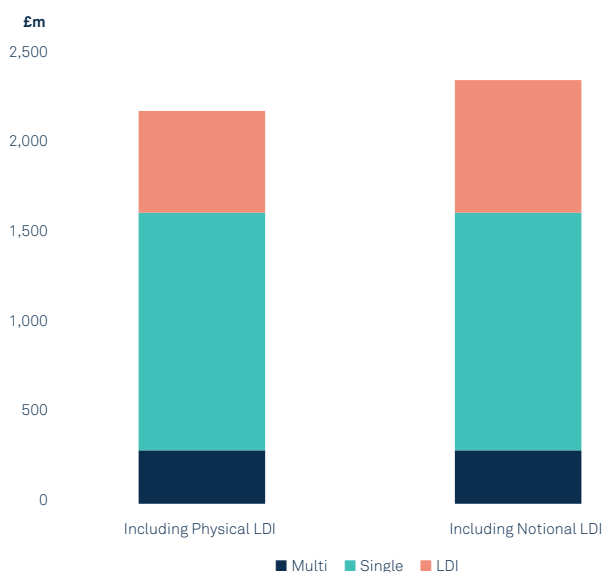
²⁸ The Purple Book, TPR/PPF

When looking at the size of LDI mandates it is more appropriate to consider LDI by the notional size of liabilities hedged, rather than by the size of physical assets under management, since these mandates frequently make greater use of derivative instruments. For this reason Chart 27 shows the estimated size of the UK institutional market on the basis of both physical and notional assets.

Taking into account the notional value of liabilities hedged, we estimate that LDI represents closer to 29% of the market and the size of the UK third party market would increase from £2.1 trillion to £2.3 trillion.

The use of LDI increased significantly in 2014 with external estimates showing the size of the notional value of liabilities hedged increasing 29% to reach £660 billion, up from £510 billion at the end of 2013.²⁹ Pooled mandates are becoming increasingly important in delivering LDI, either because schemes are looking for simpler solutions, or because they are too small to warrant a segregated mandate.

CHART 27: UK THIRD PARTY MARKET BREAKDOWN BY MANDATE TYPE

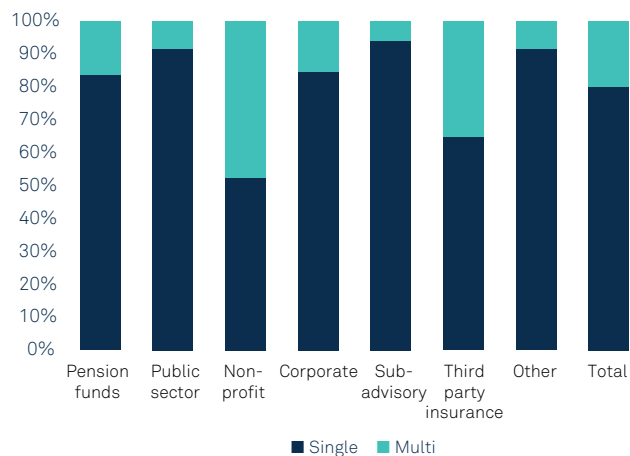


“IN THE UK, DEFINED BENEFIT PENSION SCHEMES WANT US TO HELP THEM SOLVE THEIR FUNDING PROBLEMS – GET THEM TO SELF-SUFFICIENCY OR BUYOUT – GET THEM THERE IN A RISK CONTROLLED WAY. SOME BUY THE BLOCKS – EG. LDI AND SOME SAY TO US PUT YOUR CAPABILITIES TOGETHER – LET US RUN THE STRATEGY AND GET THERE IN A RISK CONTROLLED WAY. MULTI-ASSET IS PART OF THAT.”

If we exclude the notional value of LDI mandates and focus purely on whether clients are favouring multi-asset or specialist solutions outside of explicit liability management, the preference for specialist mandates remains, with 82% of assets being invested in this way. However, this is a fall from 85% last year and 87% in 2012.

This continues to support the theme in recent years that specialisation may be reaching its limits and clients are beginning to once again favour multi-asset mandates, with managers taking on more responsibility for monitoring overall investment objectives rather than managing one asset class versus a specified benchmark.

CHART 28: UK THIRD PARTY INSTITUTIONAL CLIENT MANDATES: MULTI-ASSET VS. SPECIALIST MANDATES



²⁹ Navigating the UK LDI Market, 2015 KPMG LDI Survey

NATURE OF SPECIALIST MANDATES

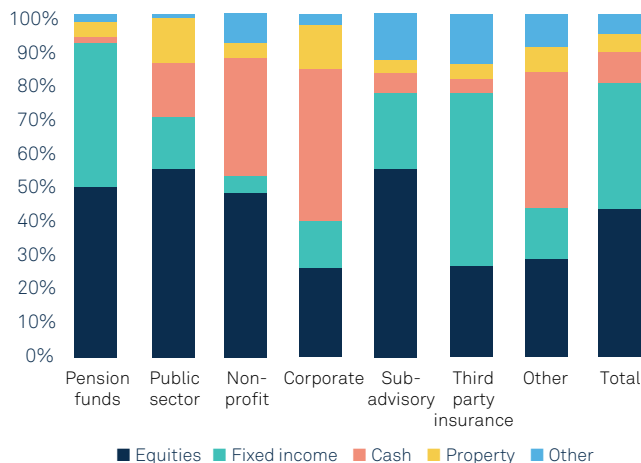
Specialist equity mandates accounted for 43% of all specialist mandates in 2014 with fixed income mandates representing 37%. However, this headline figure shrouds a wide variation in asset allocation by client type.

Pension funds and insurance companies have particularly high allocations to specialist fixed income mandates (42% and 50% respectively), so when in-house assets are included the allocation to fixed income increases to 43%, at the expense of equities.

Not-for-profit organisations and corporate entities on the other hand still have a high allocation to cash and money market funds to facilitate efficient cash management.

The 'other' category predominantly represents mutual funds for which it is not possible to accurately identify the underlying client split.

CHART 29: SPECIALIST MANDATE BREAKDOWN BY ASSET CLASS

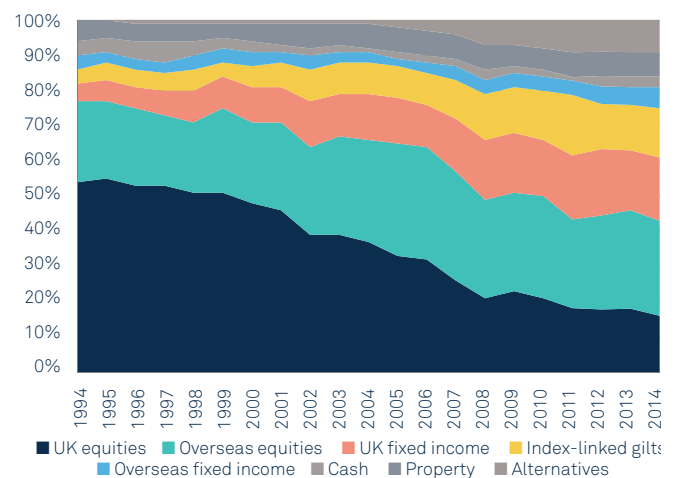


Considering the asset allocation of pension funds in greater detail corporate pension funds continue to be most heavily invested in specialist bond mandates, many of which will be DB schemes that are closed to new members or future accrual and have a maturing membership. These schemes will be particularly focused on de-risking and are likely to be shifting their equity allocations into fixed income assets or customised LDI mandates.

In the early 90s a typical defined benefit (DB) pension scheme in the UK would have been heavily invested in equities (>80%), with a small allocation to fixed income assets and other asset types, notably property.

The growing appetite to hold assets that behave in a similar way to liabilities has led schemes to re-assess their investment strategies. As well as the shift out of equities into fixed income that has been ongoing since the early 90s, many DB schemes are moving from using traditional scheme-specific asset allocation benchmarks to those that more closely match their liabilities.

CHART 30: OVERALL UK PENSION FUND ALLOCATION (1994-2014)

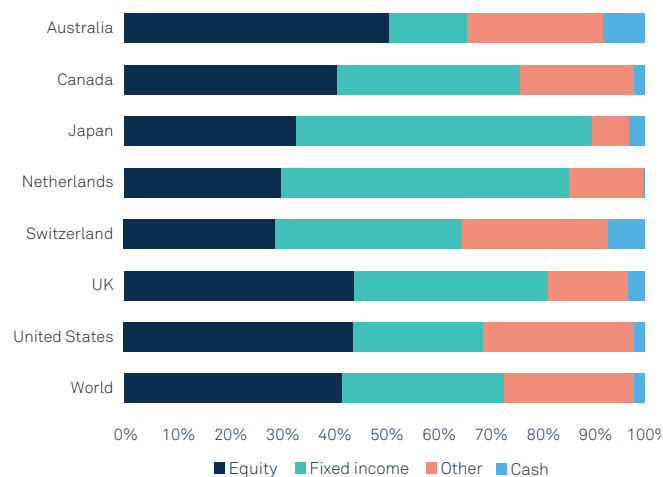


Source: UBS Pension Fund Indicators

In spite of the aggressive de-risking being undertaken by DB schemes, on a global comparison UK pensions continue to be relatively high allocators to equities. This is likely to reflect the high base of equity holdings from which DB schemes started and the growth of DC in the UK, where higher allocations to equities are common during the growth phase. The allocation to alternatives also continues to increase as pension schemes still search for an element of return generation in order to eliminate their deficits as well as looking for income to help manage their cash flows.



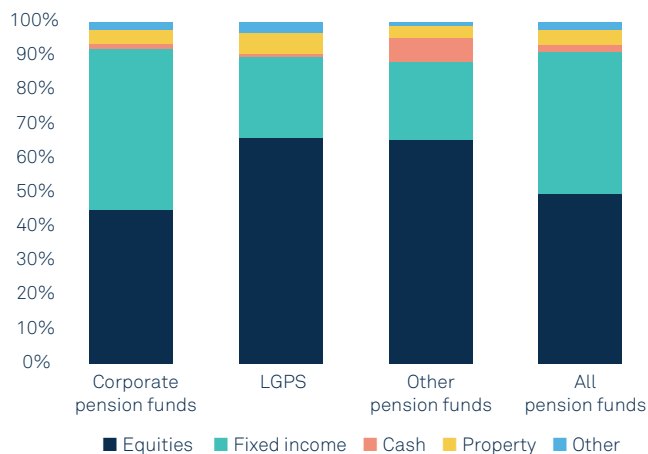
CHART 31: PENSION FUND ASSET ALLOCATION IN SELECTED COUNTRIES 2014



Source: Towers Watson Global Pension Assets Study 2015

Chart 32 also shows that the LGPS is invested very differently to corporate pension schemes. It has historically held much higher equity allocations than corporate DB schemes, albeit there is significant variation between underlying local authority funds. Scheme membership is also comparatively less mature and the LGPS funds function within a different regulatory framework to corporate schemes and therefore experience less pressure to implement de-risking investment strategies.

CHART 32: SPECIALIST MANDATE BREAKDOWN BY ASSET CLASS AMONG UK PENSION FUNDS

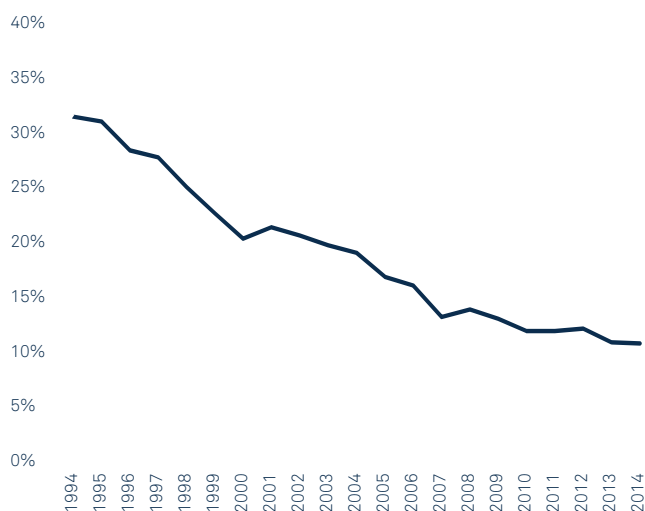


GEOGRAPHIC ALLOCATION

This year's data showed minimal change in specialist UK equity mandates at 25% of specialist third party equity mandates (down from 26% in 2013).

The movement of institutional clients out of domestic equities into overseas assets over the last 20 years is very clear (see Chart 33), albeit there are signs from this year's data that UK equity allocations may be showing some signs of bottoming out.

CHART 33: PENSION FUND OWNERSHIP OF UK EQUITIES, MEASURED AS A PROPORTION OF TOTAL DOMESTIC MARKET CAPITALISATION (1994-2015)



Source: Investment Association calculations based on data from London Stock Exchange and UBS Pension Fund Indicators

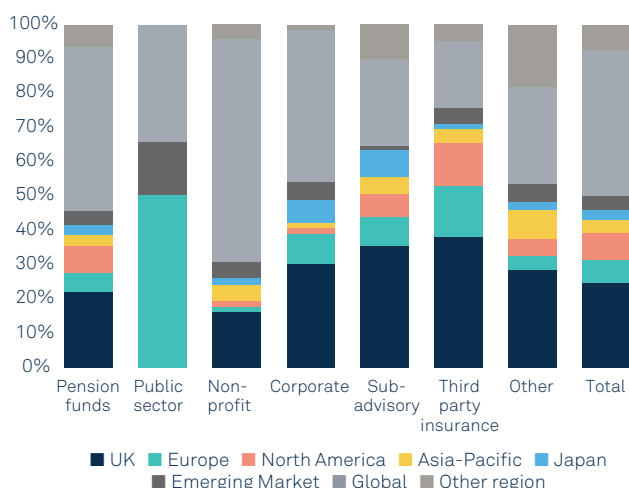
Global equity mandates represented 42% of all specialist equity mandates, up from 39% in 2013.

Once again there is a wide dispersion in specialist mandate type by client, with third party insurance still allocating 38% to UK equity and public sector clients in our respondent sample allocating zero.

The higher allocation to UK equities by insurance clients means that, once in-house assets are included, the UK equity allocation increases to 31% and the global equity allocation reduces to 35%.

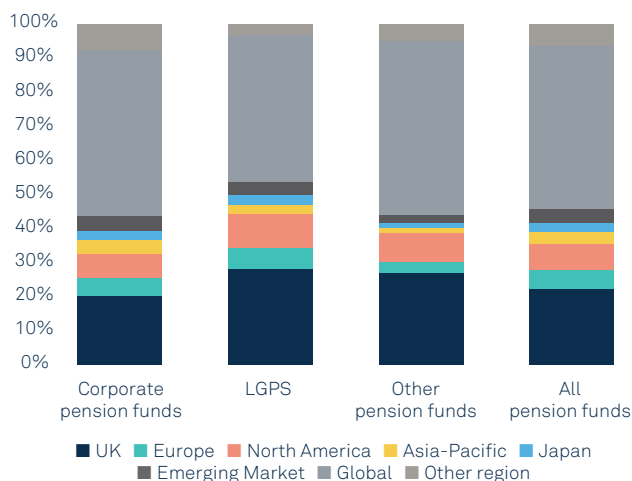
Chart 34 shows that, overall in the UK institutional market, the globalisation of investment remained little changed as three quarters of specialist equity mandates applied to non-UK mandates.

CHART 34: GEOGRAPHICAL EQUITY ALLOCATION OF SPECIALIST MANDATES BY CLIENT TYPE



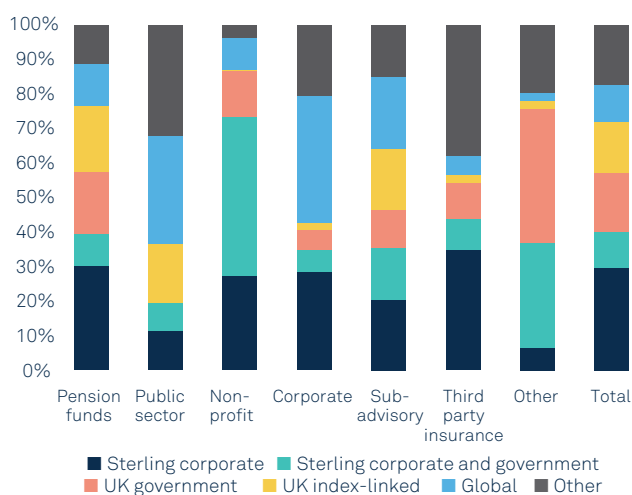
Looking at UK pension funds, once again it is evident that there are further significant differences between the LGPS and other schemes (see Chart 35). Twenty eight per cent of LGPS specialist equity mandate assets managed by Investment Association members at the end of 2014 were in UK equity mandates. This is in contrast to corporate pension funds which held only 20% in UK equity mandates. So the LGPS remains not only more equity-centric but also more UK-centric than other types of scheme.

CHART 35: GEOGRAPHICAL EQUITY ALLOCATION OF SPECIALIST MANDATES AMONG UK PENSION FUNDS



Sterling corporate bond mandates remained the largest category of specialist fixed income mandates (30%). The amount allocated to index-linked gilt mandates remained unchanged at 15% but the allocation to conventional gilt mandates increased from 13% in 2013 to 17% (closer to the 20% level seen in 2012).

CHART 36: FIXED INCOME ALLOCATION OF SPECIALIST MANDATES BY CLIENT TYPE

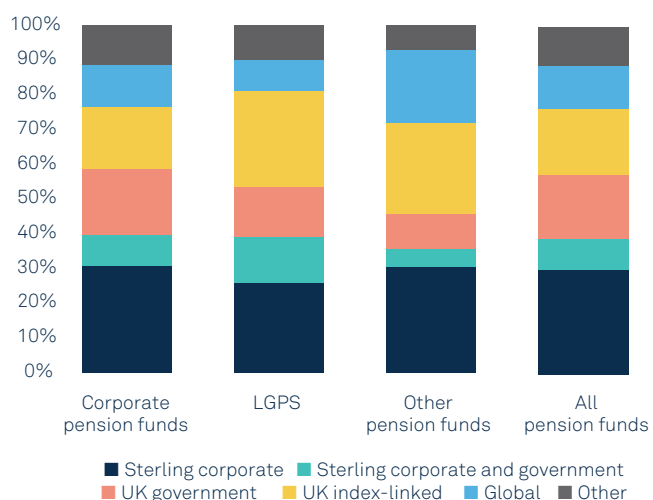


Once in-house mandates were included in the analysis:

- Sterling corporate bond mandates reduced to 25% of total fixed income assets.
- Sterling corporate and government mandates showed a significant increase, from 13% to 22%, due to strong representation in the in-house insurance category.
- Index-linked mandates decreased from 16% to 13% but conventional gilt mandates were largely unaffected.

The allocation to conventional gilts by corporate pension funds rose from 12% in 2013 to 18% in 2014 (see Chart 37). The allocation to global and other fixed income mandates fell slightly from 27% in 2013 to 23% in 2014.

CHART 37: FIXED INCOME ALLOCATION OF SPECIALIST MANDATES AMONG PENSION FUNDS

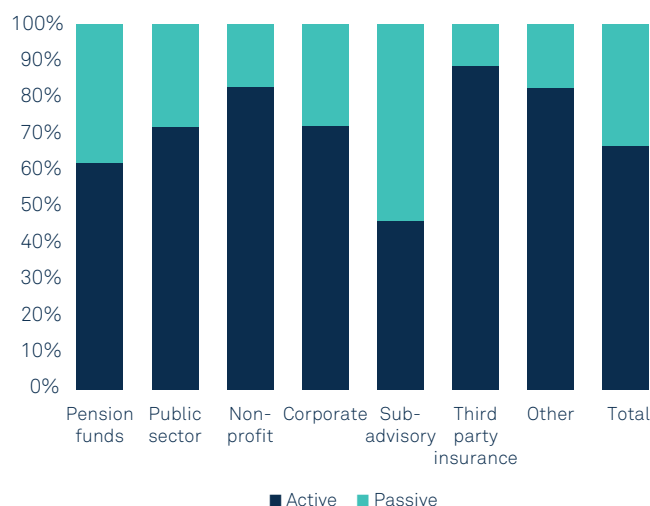


ACTIVE VS PASSIVE

Overall around two thirds of third party assets were managed by Investment Association members on an active basis (68%). Only sub-advisory mandates were more likely to be managed on a passive rather than active basis, although a significant proportion of pension schemes are passively managed (38%).

We have already noted the potential pressure on pension mandates to move towards passive in a move to reduce costs. The passive figure for pension funds in 2014 was slightly lower than that reported last year (2013:41%) and we will monitor this figure closely in future editions.

CHART 38: ACTIVE AND PASSIVE MANDATES BY CLIENT TYPE (SAMPLE-ADJUSTED)



In May 2014 the Government issued a consultation on whether the LGPS should shift to passive pooled investments.³⁰ The consultation suggested that moving to passive fund management of all listed assets, accessed through a common investment vehicle could result in an annual saving of £420 million.

Any element of mandation of passive management for LGPS funds will feed the debate among other institutional investors on the value for money provided by active fund management.

³⁰ Local Government Pension Scheme: Opportunities for collaboration, cost savings and efficiencies

“THERE ARE SOME REALLY WELL RUN LGPS (FUNDS) OUT THERE...TO LOWER EVERYTHING TO THE LOWEST COMMON DENOMINATOR IS HUGEY DAMAGING.”



In the Summer 2015 Budget the Government announced it would work with LGPS administering authorities to ensure that they pool investments to significantly reduce costs, while maintaining overall investment performance.

Local authorities have been invited to put forward their own proposals to meet common criteria for delivering savings.

SEGREGATED VS POOLED

Segregated mandates represented over one half (59%) of assets managed for third party institutional mandates at the end of 2014. Almost all mandates managed for third party insurance were managed on a segregated basis in contrast to corporate mandates where the number falls below half (46%).

Pension funds tended to be managed on a segregated basis with 56% of assets being managed in segregated mandates. However, a significant proportion of pension assets were allocated to pooled vehicles, particularly those in the ‘other’ category, which includes pensions that do not fall into the other two categories, such as those managed for not-for-profit organisations.

CHART 40: SEGREGATED AND POOLED MANDATES AMONG THIRD PARTY PENSION FUNDS

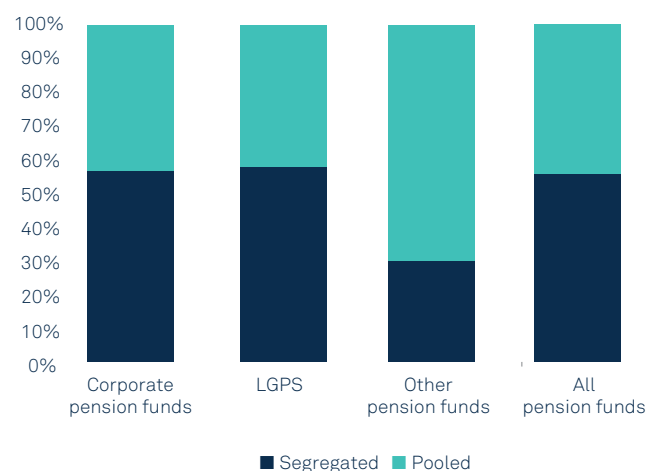
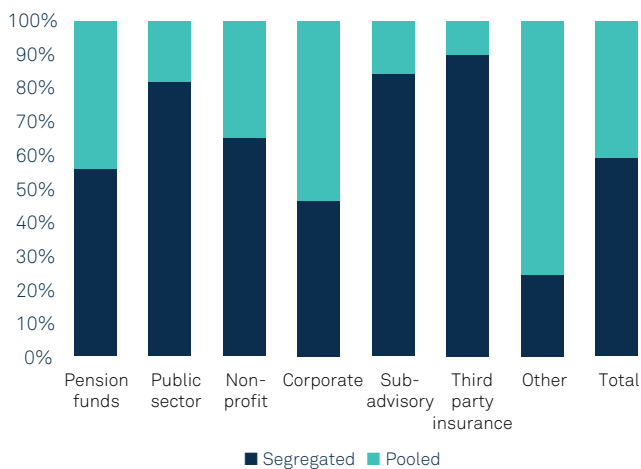


CHART 39: SEGREGATED AND POOLED MANDATES BY INSTITUTIONAL CLIENT TYPE





4 UK FUND MARKET

KEY FINDINGS

TOTAL FUNDS UNDER MANAGEMENT

 THE UK FUND INDUSTRY CONTINUES TO EXPERIENCE RECORD LEVELS OF FUNDS UNDER MANAGEMENT.


- Total UK-domiciled investment funds at the end of 2014 were £835 billion, up by 8.2% from a year earlier.
- Funds under management in retail funds represented 70% of the total in 2014, down slightly from 72% (revised) last year.
- Total investment funds managed in the UK (including both UK authorised and overseas funds whose assets are managed in the UK by Investment Association members) are estimated at £1.7 trillion.
- Market movements in 2014 accounted for £31 billion of the increase in funds under management with net investor inflows amounting to a further £32 billion.

ASSET MIX IN INVESTMENT FUNDS

 THE PROPORTION INVESTED IN EQUITIES APPEARS TO HAVE STABILISED AFTER A DRAMATIC DECLINE IN THE AFTERMATH OF THE DOT.COM CRASH.


- Equity funds represented 54% of total funds under management, down slightly from 55% in 2013.
- Fixed income is broadly unchanged at 15% of the total.
- Mixed asset funds fell slightly to 13%, compared with 14% last year, while property funds increased to 2.6% (up from 2.2% in 2013).
- Targeted absolute return funds increased to 4.7% in 2014, up from 4.4% in 2013.

RETAIL FLOW LEVELS INTO AUTHORISED FUNDS

 AFTER THE DRAMATIC GROWTH THROUGH 2009-10, SALES PATTERNS SUGGEST A 'NEW NORMAL' EMERGING.

- Net retail sales were £21 billion in 2014, broadly in line with 2013.
- Five year average flow levels are £22 billion, up from a low of £12 billion just before the financial crisis.

PRODUCT PREFERENCES

 PRODUCT PREFERENCES REFLECT BOTH STRUCTURAL AND CYCLICAL TRENDS, WITH A MOVE TO INCOME AND SOLUTIONS ALONGSIDE ONGOING INTEREST IN EQUITIES AND PROPERTY

- Equity funds were the best-selling asset class during 2014 at £8.7 billion net, although this was lower than the £11 billion seen in 2013.
- Equity income funds represented the overwhelming majority of this flow at £7.8 billion, more than double the inflows they saw in 2013 (£3.5 billion).
- Mixed asset funds had another strong year, though down slightly from last year's sales of £4.6 billion, at £3.9 billion.
- Property fund sales more than doubled to £3.8 billion, up from £1.5 billion in 2013.
- Fixed income funds had a much stronger year in 2014, with net sales of £1.3 billion, up from near zero last year.
- Targeted absolute return funds posted another strong year with net sales of £2.1 billion (£2.8 billion including overseas-domiciled funds).

ACTIVE VS PASSIVE

 WHILE PASSIVE FUNDS ARE STILL A SMALL PART OF THE OVERALL MARKET, THE LATEST ANNUAL FIGURE REPRESENTS THE HIGHEST EVER NET RETAIL SALES OF INDEX-TRACKING FUNDS.

- Tracker funds continued to report strong figures in net retail sales, at £4.9 billion in 2014 – up from £3.4 billion in 2013.
- Index-tracking funds represented 11% of industry total funds under management at the end of 2014, up from 6% in 2004.³¹

UK INDUSTRY AND CONCENTRATION

 THE FUNDS INDUSTRY REMAINS RELATIVELY UNCONCENTRATED, WITH DATA NOT SUGGESTING MARKED CHANGES IN STOCK OR FLOW CONCENTRATION.

- The top ten firms represented 47% of total UK authorised funds under management at the end of 2014, up two percentage points from a decade ago.
- Fund size remains significantly skewed with a median fund size of £97 million compared to a mean of £367 million.

UK FUND MANAGEMENT IN CONTEXT

 EUROPEAN ASSET MANAGEMENT LEADER BUT LAGGING AS A FUND DOMICILE.

- European investment funds under management amounted to €11.3 trillion (£8.7 trillion) at the end of 2014, a 15% increase since 2013.
- The UK continues to be the fifth largest fund domicile in Europe, representing 12% of the total European investment fund industry as at the end of 2014. Luxembourg marginally increased its share of the market to 27%.

³¹ Investment Association data does not include exchange traded funds.

4 UK FUND MARKET

This chapter of the survey covers UK-domiciled authorised unit trusts and Open Ended Investment Companies (OEICs), which reflect the majority of the UK fund market.

A growing part of the fund market is represented by funds domiciled overseas, where the portfolio management takes place in the UK. There are also some UK-domiciled funds that are sold into overseas markets.

The main investors in UK unit trusts and OEICs are retail investors, although institutional investors such as pension funds and insurance companies are able to invest in them and may do so for a variety of reasons, for example:

- To gain access to specific portfolio manager skills.
- To reflect investor preferences within unit-linked life products that offer access to third party funds. There has also been periodical restructuring of assets out of life products and into OEICs in recent years.

The analysis in this section is based primarily on The Investment Association's funds data, which is more detailed and has a longer history than the data collected annually as part of the annual survey. This data captures holdings and flows for individual funds on a monthly basis. In 2014, The Investment Association collected this data for a total of 2,513 funds domiciled in the UK.

Investment Association figures on retail investment include sales through fund platforms, other intermediaries such as wealth managers, stockbrokers, tied agents and IFAs, as well as direct sales.

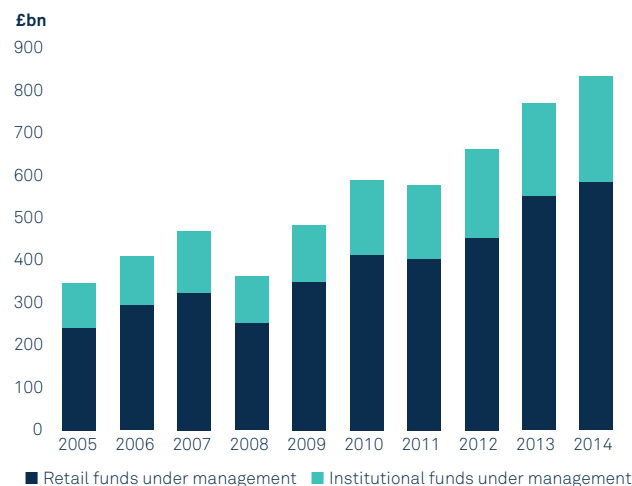
As we reflected earlier in this survey, sales to investors through insurance companies, whether as investment bonds or as part of pension arrangements (including workplace and personal pensions) are classified as institutional insurance assets.

TOTAL FUNDS UNDER MANAGEMENT

At the end of 2014, funds under management in UK-domiciled funds stood at £835 billion (see Chart 41), up by 8.2% from £770 billion in 2013. Funds under management in retail funds made up the majority of the total, accounting for over two thirds (70%) of assets, a similar level to ten years ago.³² Holdings by UK investors in overseas domiciled funds³³ totalled £74 billion at the end of 2014.

A further £895 billion was invested in overseas-domiciled funds where the asset management of the fund takes place in the UK. This brought the total investment fund assets managed in the UK to £1.7 trillion, up from an estimated £1.5 trillion in 2013.

CHART 41: INDUSTRY FUNDS UNDER MANAGEMENT (2005-2014)



After a significant drop in assets in 2008, the UK funds industry has proved extremely resilient post-crisis, in spite of challenging and volatile market conditions. In nominal terms the funds industry has grown by 78% since the end of 2007 and by 130% since its low in 2008.

³² In this context, 'retail funds under management' comprises assets held by retail funds. These are defined as funds with a minimum lump sum investment amount of up to £50,000 and with at least one-third of gross sales over the preceding three years being retail.

³³ These funds comprise open-ended investment funds that are domiciled outside of the UK, are FCA recognised and sold into the UK with reporting status or UK distributor status.

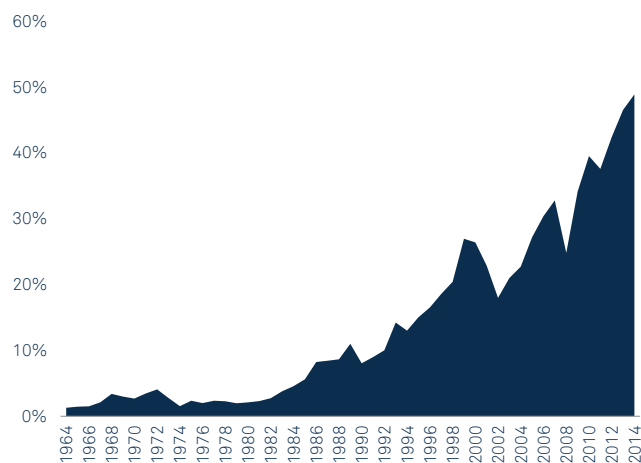
TABLE 5: AVERAGE ANNUALISED GROWTH RATE OF TOTAL FUNDS UNDER MANAGEMENT SINCE 2007 VS THE FTSE ALL SHARE

| | UK-domiciled funds | FTSE All Share ³⁴ |
|--------------------|--------------------|------------------------------|
| Nominal | 8.6% | 4.7% |
| Inflation adjusted | 5.5% | 1.8% |

Looking at funds under management as a percentage of GDP provides a useful comparison against which to measure industry growth. Fifty years ago funds under management in the UK equated 1% of GDP (see Chart 42). By the end of 2014, the equivalent figure was equal to almost half (49%).

The annualised growth rate of UK funds from 1960 to 2014 was 17% in nominal terms and 11% in real terms.

CHART 42: FUNDS UNDER MANAGEMENT AS PERCENTAGE OF GDP (1964-2014)

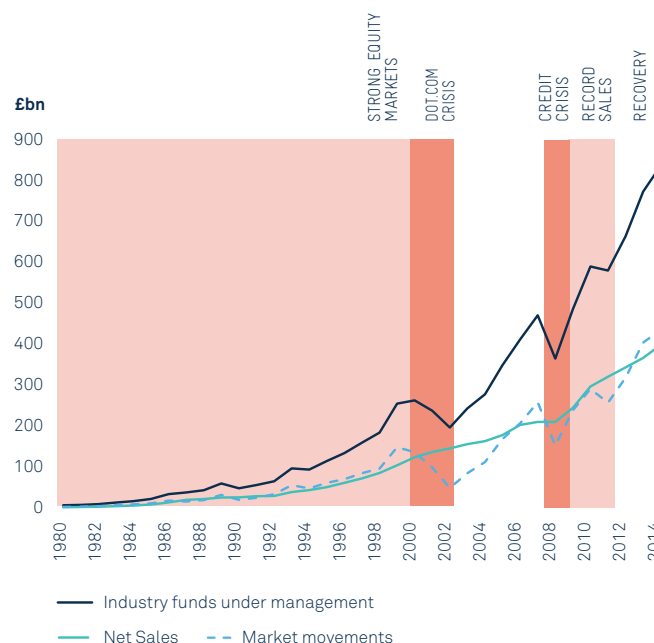


Source: The Investment Association, ONS

Chart 43 shows that industry growth since the early 1980s is the product of broadly equal net flows and market movements, albeit market movements are subject to higher levels of volatility compared to net flows, which have increased on a relatively consistent basis year-on-year.

Up until 1999, flows and market movements moved closely in line. In the early 2000s the relationship altered as markets fell after the dot.com crisis but net flows continued to accumulate. Between 1980 and 2014 no year saw negative net flows out of UK authorised funds.

CHART 43: DRIVERS OF INDUSTRY GROWTH (1980-2014)



There has been a shift in the industry in recent years, which has contributed to the flow of assets into funds as insurance assets have been moved into OEICs. However, there are also a number of external factors that have influenced investor behaviour, including:

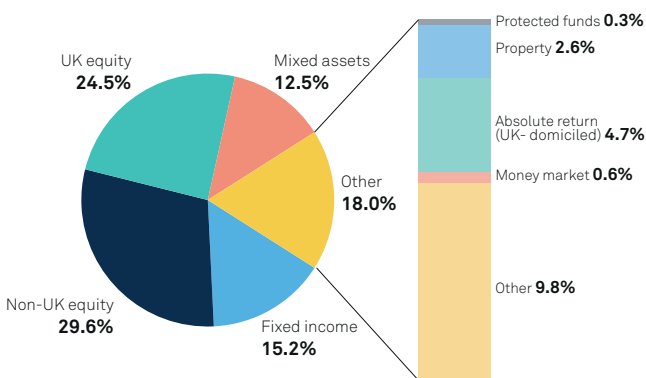
- Strongly performing equity markets during the 1980s and 1990s led to consistently strong sales of equity funds.
- A shift into a broader range of assets in the 2000's as equity markets fell after the dot.com crisis.
- The financial crisis led investors to flock to fixed income funds looking for comparative safety for their assets.
- The recovery of equity markets, which began towards the end of 2012, attracted robust flows on top of increased asset values.

³⁴ FTSE growth rate includes income reinvested

ASSET MIX OF HOLDINGS IN UK AUTHORISED FUNDS

The overall asset mix of UK funds as at the end of 2014 is shown in Chart 44.

CHART 44: FUNDS UNDER MANAGEMENT BY FUND/ASSET TYPE



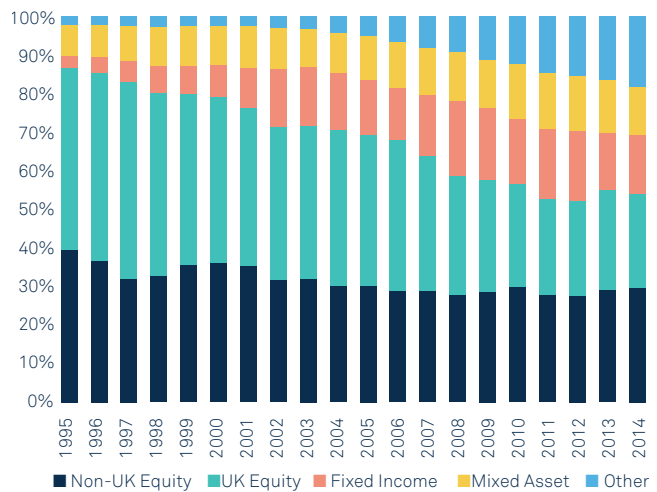
- Equity funds represented 54% of total funds under management at the end of 2014, down only slightly from 55% in 2013.
- Funds under management for fixed income funds remained steady at 15% of the total. Despite the increase in sales of fixed income funds in 2014, compared to a very poor 2013, the level of sales was still below that of recent years.
- Mixed asset funds made up 12.5% of the market at the end of 2014, slightly below their level of 13.7% in 2013.
- Strong performance and inflows in the UK property sector helped funds in this sector increase their market share to 2.6% (up from 2.2% in 2013). This is still below the peak in 2006 when property represented 3.0% of total assets.
- Targeted absolute return funds continued to increase in significance, up from 4.4% in 2013 to 4.7% of total funds under management.³⁵

- Money market funds accounted for a very small proportion of funds under management with only 0.6% market share. Funds in the retail space should not be confused with the large institutional money market funds managed out of the UK, which do not form part of The Investment Association's fund data.

Over the longer term the asset mix has changed significantly. Equity funds have represented an ever decreasing proportion of the market as investors have become increasingly wise to the different types of asset classes available and have diversified their savings away from more traditional equity holdings.

In 1995, equity funds represented 87% of funds under management. Since then they have fallen consistently, however, based on data from the last three years the market share of equity funds appears to be levelling off and stabilising at around 55%.

CHART 45: CHANGE IN FUNDS UNDER MANAGEMENT BY ASSET CLASS (1995-2014)



³⁵ This refers to the proportion of total funds under management made up by UK domiciled targeted absolute return funds.

RETAIL FUND SALES

Table 6 shows net retail sales of the main fund categories since 2011, reflecting Investment Association Sector classifications.³⁶

TABLE 6: NET RETAIL SALES BY FUND TYPE (2011-2014)

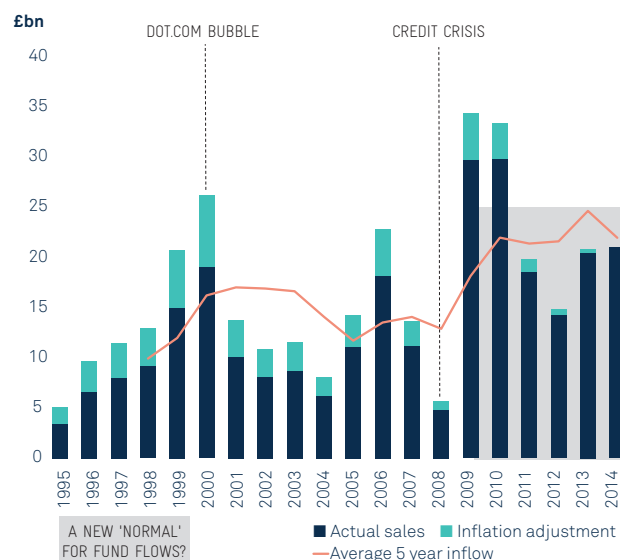
| Fund type | Net retail sales (£m) | | | |
|-------------------------------|-----------------------|---------------|---------------|---------------|
| | 2011 | 2012 | 2013 | 2014 |
| Equity | 3,209 | 3,677 | 11,459 | 8,708 |
| <i>of which tracker</i> | 1,275 | 1,215 | 2,691 | 3,783 |
| Fixed Income | 4,486 | 5,607 | 30 | 1,280 |
| <i>of which tracker</i> | 685 | 345 | 31 | 293 |
| Mixed Asset | 5,878 | 2,846 | 4,554 | 3,933 |
| Targeted Absolute Return | 933 | 866 | 2,208 | 2,119 |
| Property | 535 | 391 | 1,530 | 3,822 |
| Money Markets | 151 | -52 | -92 | 63 |
| Others | 3,349 | 916 | 813 | 1,148 |
| All funds | 18,540 | 14,251 | 20,502 | 21,071 |
| <i>of which fund of funds</i> | 5,478 | 3,527 | 3,935 | 3,266 |

Note: Numbers may not add up due to rounding

Net retail sales during 2014 were £21 billion (slightly higher than the level in 2013). This continued the trend of high net retail sales observed since 2009. The financial crisis had a significant impact on the behaviour of retail investors and the funds industry saw a big increase in flows coinciding with the fall in the base rate, which meant savers were unable to achieve satisfactory returns from banks or building societies.

Flows appear to have stabilised, at least for now, at a significantly higher level than before the crisis, with the five year average inflow on an inflation adjusted basis now standing at £22 billion, up from a low of £12 billion in 2005.

CHART 46: NET RETAIL SALES (1995-2014)³⁷



Source: The Investment Association, ONS

Looking at net retail sales in a broader historical perspective shows how investors' fund choices have developed over 20 years in response to evolving market conditions (Chart 47).

It appears that investors are responding to both structural and cyclical drivers. Equity growth funds were the dominant product choice throughout the 1990s but, since the early 2000s, investors have shown an increased appetite for funds that:

- Generate income.
- Focus on investment outcome, for example targeted absolute return funds and capital preservation funds.
- Offer a greater level of diversification and return opportunities from asset allocation.

One third of net flows in 2014 were into outcome and allocation type funds.

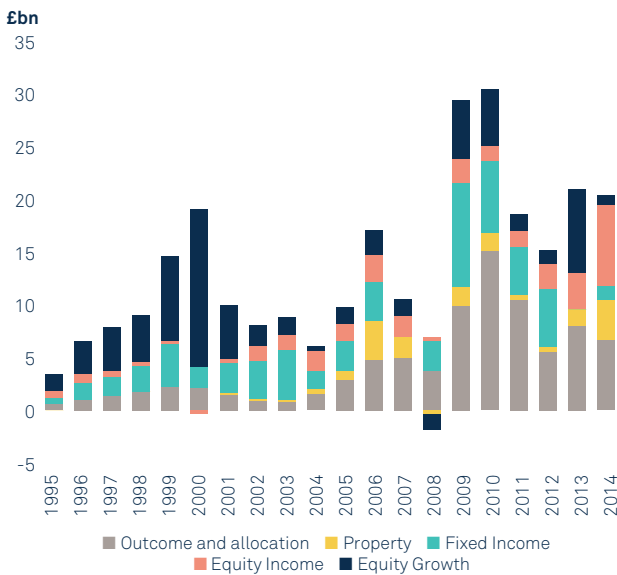
However, investors are also responding to cyclical drivers as we can see from the large spike in net sales of equity growth funds in 2013 against a backdrop of strong equity returns and concern about the impact of potential unwinding of QE on fixed income markets.

³⁶ In this context, the Targeted Absolute Return sector is the renamed Absolute Return sector and net flows shown are for UK-domiciled funds only.

³⁷ Includes an adjustment for inflation to illustrate the historical purchasing power of money using the latest rate from 2014.

In 2014 we also witnessed a significant increase in flows into property funds of £3.8 billion. Flows of this size into property funds have not been seen since 2006, shortly before the last fall in the property market. The 2014 inflow could represent investors following property returns, or it could reflect the greater demand for income that we are seeing more widely across the asset management industry.

CHART 47: NET RETAIL SALES BY DIFFERENT INVESTMENT OBJECTIVE (1995-2014)



EQUITY FUNDS

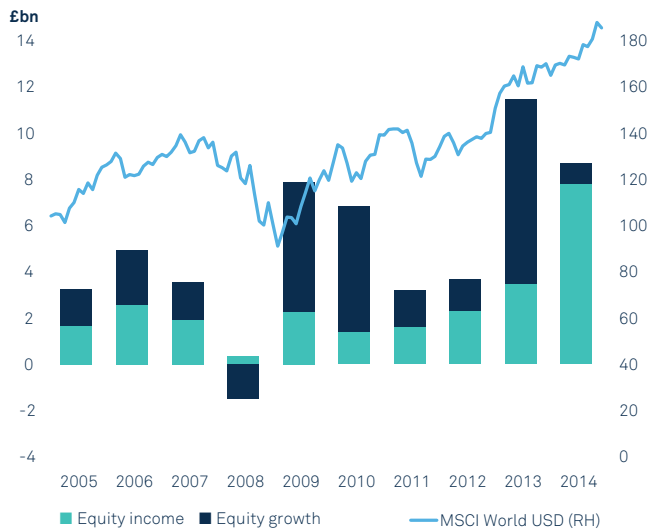
Despite the resurgence in equity growth funds during 2013, net retail sales of equity growth funds barely registered as a percentage of overall sales in 2014. Only £900 million flowed into these funds during the year.

Geopolitical risk was a key driver. The Ukraine crisis led to market upheaval in March, while the advances made by Islamic militants in Iraq and Syria, led to further turmoil mid-year. In the fourth quarter fears of slowing US economic growth, along with further troubles in Greece and the ebola crisis, led to yet further volatility.

However, equity funds overall remained the most favoured asset class, with equity income experiencing a seven month run as best seller between June and December. Equity income attracted 40% of net flows during the year (£7.8 billion).

Chart 48 shows the equity net retail sales versus the movement of the MSCI World Index over the last ten years, which indicates that there may be a link between flow levels and returns over the longer term.

CHART 48: NET RETAIL SALES OF EQUITY FUNDS VS. MSCI WORLD INDEX (2005-2014)



Source: The Investment Association, Lipper IM (calculated on a capital return basis, rebased at 100)

Equity sales by sector

The majority of Investment Association equity sectors saw a drop in net retail sales from the levels of 2013. The most notable exception to this was UK Equity Income, which was the strongest sector in 2014. It saw high net retail inflows of £6.3 billion, up from £1.7 billion in 2013.

The 2014 sales for UK Equity Income were greater than the combined totals of all the other equity sectors. This partly reflects concentrated investment in some new fund launches but primarily appears to be a response to the ongoing search for income from investors.

Last year's best-selling equity sector, Global Equity Income, continued to record high inflows and was the third best-selling equity sector in 2014.

Despite being the fourth best performing sector, European ex-UK inflows fell by almost half to £698 million.



Among the Smaller Companies sectors, inflows in the UK all but disappeared, falling from £1 billion in 2013 to only £7 million. European Smaller Companies suffered a similar fate, moving from a £798 million inflow in 2013 to a £516 million outflow in 2014. A similar shift was seen in the US, where flows moved from £199 million to a negative £198 million.

TABLE 7: NET RETAIL SALES AND FUNDS UNDER MANAGEMENT AMONG EQUITY SECTORS (2013-2014)

| | 2013 | 2014 | 2014 |
|-----------------------------------|------------------------|------------------------|------------------------------|
| | Net retail sales £m | Net retail sales £m | Funds under management £m |
| UK Equity Income | 1,741 | 6,334 | 57,312 |
| Global | 1,242 | 1,487 | 77,655 |
| Global Equity Income | 1,753 | 1,483 | 12,765 |
| Europe Excluding UK | 1,348 | 698 | 40,766 |
| Japan | 639 | 442 | 11,353 |
| Global Emerging Markets | 873 | 206 | 14,947 |
| Asia Pacific Excluding Japan | 781 | 97 | 28,686 |
| Technology and Telecommunications | 21 | 61 | 1,053 |
| Europe Including UK | -54 | 35 | 2,171 |
| Japanese Smaller Companies | 27 | 12 | 303 |
| UK Smaller Companies | 1,010 | 7 | 10,978 |
| China/Greater China | -100 | 5 | 1,823 |
| Specialist | 26 | -19 | 37,283 |
| Asia Pacific Including Japan | 58 | -50 | 1,928 |
| North America | 966 | -127 | 36,988 |
| North American Smaller Companies | 199 | -198 | 1,628 |
| European Smaller Companies | 798 | -516 | 3,860 |
| UK All Companies | 132 | -1,246 | 157,985 |
| Total | 11,459 | 8,708 | 499,484 |

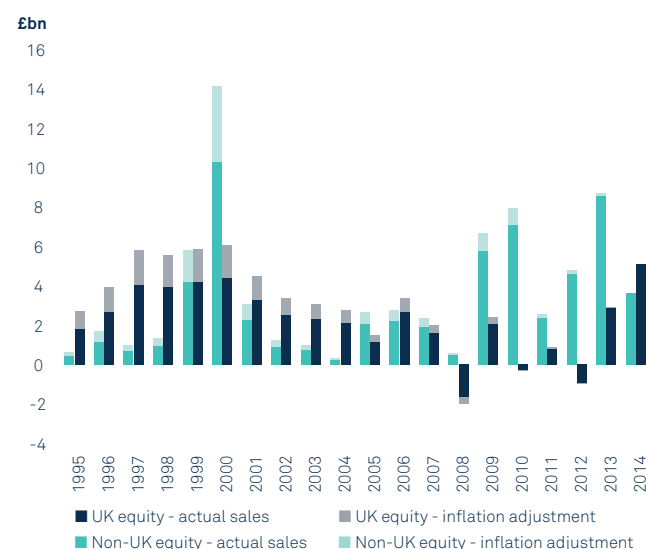
Note: Numbers may not add up due to rounding

After rebounding to achieve a small positive net flow in 2013 the UK All Companies sector recorded another very weak year in 2014, with outflows of £1.2 billion.

Regional Equity Sales

UK equity funds had a very strong year with net retail sales of £5.1 billion, albeit this was driven by the very strong flows into UK equity income rather than growth funds. It halted a seven year run of UK equity sales lagging behind those of overseas. This is consistent with data collected on wider assets under management which has hinted at a reversal of the decline in relative UK equity holdings. However, in real terms, the 2014 sales are still below the peak of 2000.

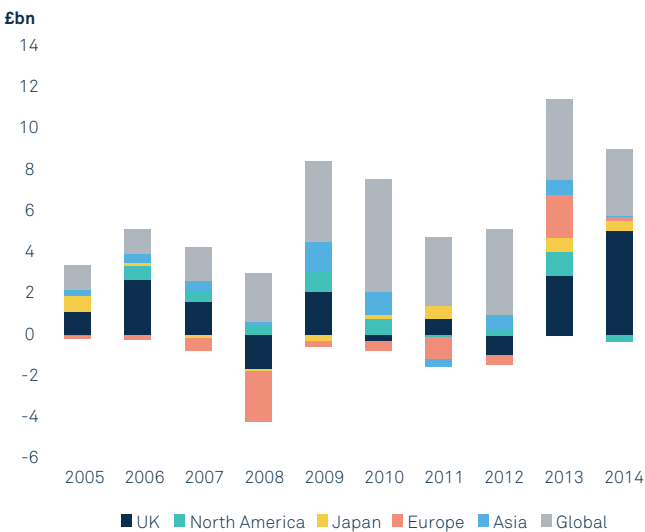
CHART 49: NET RETAIL SALES OF UK AND NON-UK EQUITY FUNDS (1995-2014)



- Global equity funds, which include a diverse range of funds that do not fall into the other specific regional categories, were down slightly on last year's total but were still the second best selling in 2013 with a net inflow of £3.2 billion. This likely reflects the preference of a significant proportion of investors for the higher levels of diversification offered by global funds in a market where volatility of individual country returns has been relatively high.
- European equity funds saw far more modest inflows (£216 million), albeit positive following persistent outflows from 2004 to 2012 as European economies continued to look fragile, with even Germany barely avoiding re-entering recession.

- Japan equity funds had another good year with a strong net inflow of £454 million, in spite of the volatility experienced in the Japanese equity market during the year. This may reflect the fact that strong earnings growth has kept Japanese equities cheap relative to other markets and export earnings are expected to continue to be strong as a result of the weaker yen.
- Asian equity funds, once again subject to variable macro-economic conditions, saw their net retail sales scaled back considerably, as they only registered a total net inflow of £52 million in 2014.
- North America was the only region to see a small net outflow (£325 million) in spite of the relative strength of its economic recovery during the year.

CHART 50: NET RETAIL SALES OF EQUITY FUNDS BY REGIONAL FOCUS (2005-2014)



The above chart shows how global equity investment became increasingly popular after the 2008 crisis, suggesting investors were looking for greater levels of diversification and return generation.

Flows into UK equities have shown more cyclical behaviour in recent years as strong returns in 2005, 2012 and 2013 were followed by relatively high flow levels in the subsequent years.

Over the longer term the proportion of funds invested in equities has continued to decline. However, it is important to note that this does not represent an absolute reduction in equity holdings. The UK

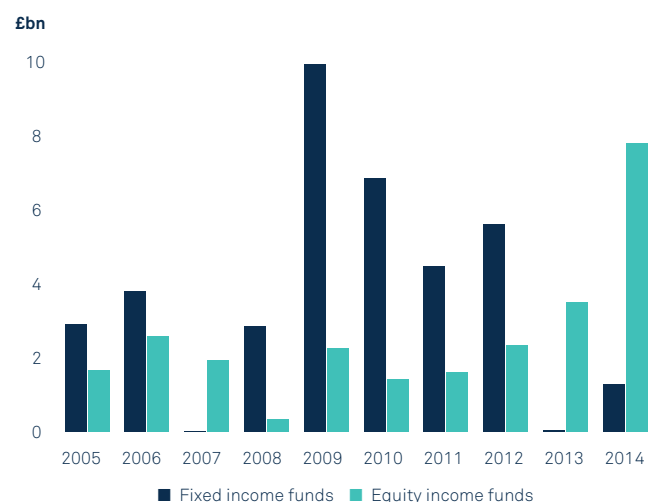
authorised funds market only totalled £92 billion in 1994, whereas it represented £835 billion in assets at the end of 2014. Therefore, in real terms, total equity holdings are far higher now than at the start of this period, or at any time over the intervening year. This is true for both UK- and overseas-focused equity funds.

UK equity funds accounted for 6% of domestic market capitalisation in 1994. This has risen steadily to around 9% at the end of 2014. Bearing in mind that other Investment Association sectors also have some UK equity exposure, the figure is likely to be higher.

FIXED INCOME FUND SALES

Demand for fixed income products increased dramatically after 2008 as investors were attracted to assets that were perceived as lower risk and provided yields above those available from other sources. More recently it has been clear that there is an ongoing sensitivity about the potential for QE unwinding and the risks to bond valuations should interest rates rise sharply. Amid intense uncertainty about the timing and scale of any rate normalisation, the demand for fixed income from retail investors has decreased below pre-crisis levels.

CHART 51: NET RETAIL SALES OF FIXED INCOME FUNDS AND EQUITY INCOME FUNDS (2005-2014)



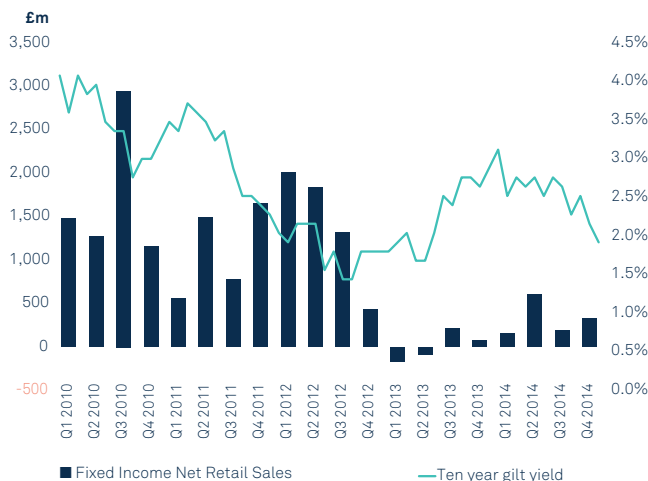
Source: The Investment Association, Morningstar



In 2014 net sales into fixed income funds were £1.3 billion, which was an improvement on 2013 (£30 million)³⁸ but still low compared to the years immediately following the financial crisis. Chart 52 shows the stark contrast of the last two years compared to 2009-2012. As recently as 2012, fixed income funds were the best-selling fund type with £5.6 billion of net retail inflows.

There was a small increase in fixed income sales as yields showed signs of increasing mid-year but they dropped off as yields returned back to extremely low levels by the end of 2014 placing further pressure on the cost of fixed income investment.

CHART 52: TEN YEAR GILT YIELD VS. FIXED INCOME SALES (2010-2014)

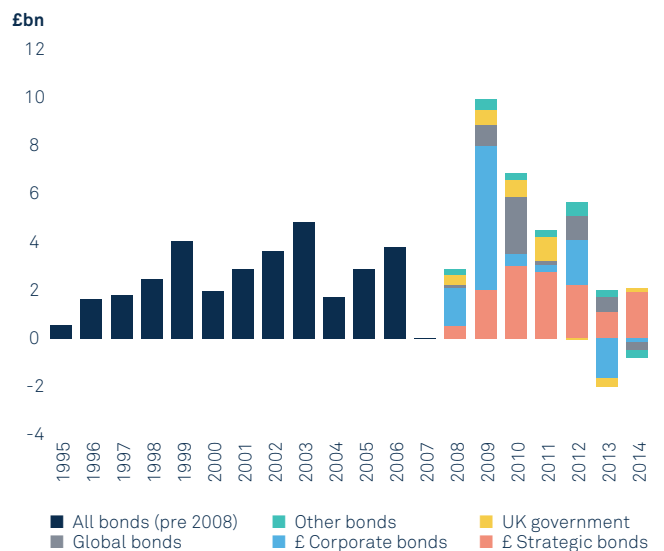


Source: The Investment Association, Lipper IM

Fixed income sales by sector

Chart 53 shows the annual net retail sales of fixed income funds from 1995 to 2014, including a sector breakdown from 2008 onwards.

CHART 53: NET RETAIL SALES OF FIXED INCOME FUNDS (1995-2014)



Within the fixed income sector the most consistent flows have been seen into the £ Strategic Bond sector, where funds may hold a range of different bonds with no limits on levels of exposure to specific fixed income sectors within the fund.

In 2014 the best-selling fixed income sector was once again £ Strategic Bond with a total of £1.9 billion, up from £1.1 billion in 2013.

UK government bonds include both the UK Gilts and UK Index-Linked Gilts sectors. UK government bonds were the only other fixed income class that received a net inflow during 2014 (£162 million).

The Global Bonds sector experienced a £336 million outflow after being the second best-selling fixed income sector in 2013.

£ Corporate bonds saw their second consecutive year of negative flows, with £182 million leaving the sector in 2014 on top of £1.6 billion the previous year.

³⁸ Revised from an outflow of £20million reflected in the 2013-2014 Survey

OUTCOME AND ALLOCATION FUNDS

The majority of funds under management in The Investment Association's outcome and allocation funds are managed in mixed asset and targeted absolute return funds. There are also a small proportion of funds managed in money market funds and funds that offer some form of capital protection to the end investor.

Mixed asset funds

In general, mixed asset funds afford the manager greater discretion over asset allocation, and more flexibility in rebalancing the constituent portfolios.

The Investment Association has five dedicated mixed asset sectors:

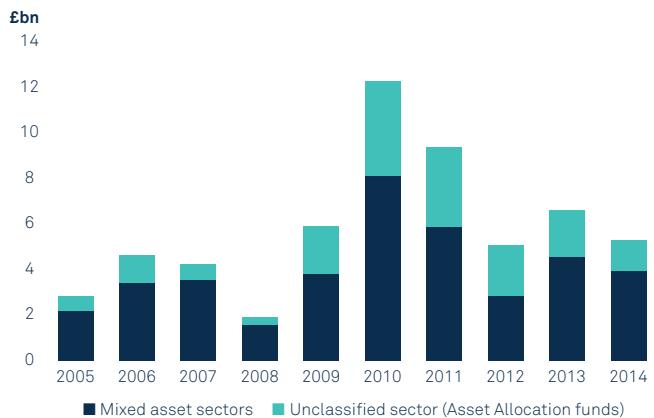
- Mixed investment 0-35% shares
- Mixed investment 20-60% shares
- Mixed investment 40-85% shares
- Flexible investment
- UK equity and bond income

In addition, over 58% of funds in the Unclassified Sector (45% by total assets) are also categorised as 'asset allocation funds'. These funds aim to maximise investment returns to retail investors within the risk constraints matched to investors' risk profiles. Mixed asset funds can therefore be used as part of the investment strategy to meet a wide range of investor objectives and are therefore addressed separately in this section.

Mixed assets funds continued to be the second best-selling asset class after equity for the third successive year, although the figures for 2014 revealed that they were only marginally ahead of the next best-selling fund type - property.

Funds in the mixed asset sectors saw a fall in net retail sales to £3.9 billion during 2014, down from £4.6 billion in 2013. Including asset allocation funds in the Unclassified sector added a further £1.4 billion to net retail sales to bring the total to £5.3 billion. Although this represented a decrease in sales from £6.6 billion in 2013, mixed asset funds remained popular with investors looking for more diversified strategies. The net retail sales of mixed asset sectors and asset allocation funds in the Unclassified sector are shown in Chart 54.

CHART 54: NET RETAIL SALES OF ASSET ALLOCATION FUNDS (2005-2014)



Source: The Investment Association, Morningstar Direct

Considering the range of mixed investments in greater detail, the inflows during 2014 were almost entirely accounted for by two Investment Association sectors:

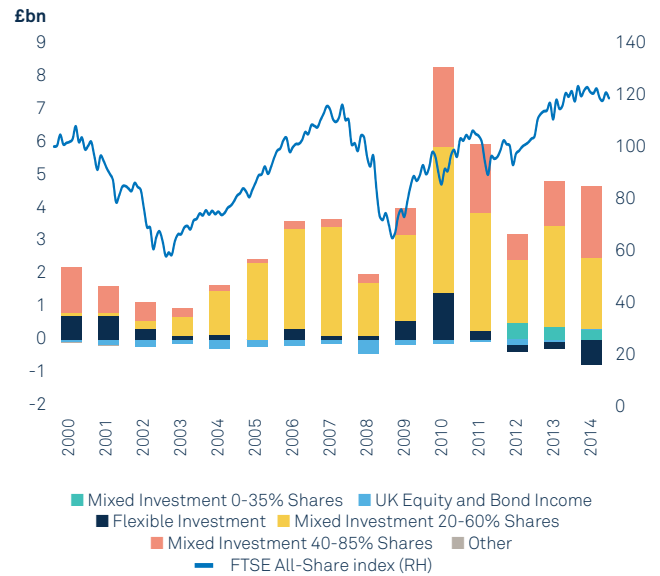
Net retail sales



The proportion of total sales flowing into the sector with the highest equity allocation (40-85% shares) increased to 55% in 2014, the highest level since 2001. Mixed Investment 20-60% Shares continued to sell well but historically low interest rates, and signs of improving growth, may be motivating investors to take higher levels of risk while retaining an element of diversification outside of equities.

This follows a lengthy period between 2003 and 2008 when investors turned away from mixed investment funds with high equity allocations as risk aversion appeared to increase, even as equities performed strongly.

CHART 55: NET RETAIL SALES OF MIXED ASSET FUNDS VS. FTSE ALL-SHARE INDEX (2000-2014)



Source: The Investment Association, Lipper IM (calculated on a capital return basis, rebased to 100)

Table 8 shows a breakdown of net retail sales for each of the classified mixed asset sectors spanning the last two years:

- Mixed Investment 40-85% Shares overtook Mixed Investment 20-60% Shares as the best-selling sector over this period, albeit only marginally. Between them, these two sectors took the lion's share of net retail sales for mixed asset funds.
- The total net retail sales for mixed asset funds was down on the previous year, and funds under management fell slightly from £116 billion in 2013.
- UK Equity and Bond Income overturned 14 consecutive years of net outflows to register positive net retail sales in 2014.
- There were net outflows from Flexible Investment funds for the third year in a row.

TABLE 8: NET RETAIL SALES OF MIXED ASSET FUNDS BY SECTOR (2013-2014)

| | 2013 | 2014 | 2014 |
|--------------------------------|------------------------|------------------------|------------------------------|
| | Net retail sales £m | Net retail sales £m | Funds under management £m |
| Mixed Investment 40-85% Shares | 1,355 | 2,177 | 50,295 |
| Mixed Investment 20-60% Shares | 3,098 | 2,152 | 40,473 |
| Mixed Investment 0-35% Shares | 366 | 277 | 4,727 |
| UK Equity and Bond Income | -85 | 63 | 2,387 |
| Flexible Investment | -181 | -737 | 17,473 |
| Total | 4,554 | 3,933 | 115,355 |

Targeted absolute return funds

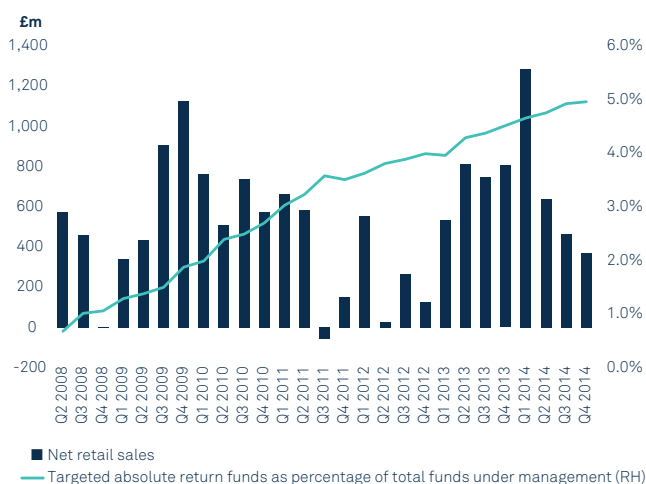
The Investment Association Targeted Absolute Return sector, created in April 2008, includes funds managed with the aim of delivering positive returns in any market conditions, but where returns are not guaranteed.

This section includes data on both UK- and overseas-domiciled targeted absolute return funds to reflect the importance of overseas-domiciled funds to this sector.

Taking both into account, the proportion of funds under management in targeted absolute return funds increased slightly from 2013 to just under 5%. Assets in UK-domiciled funds increased at a similar rate.

Net retail sales reached a high in the first quarter but then dropped away slightly and finished the year slightly lower than the level in 2013 (£2.9 billion), at £2.8 billion. Figures for UK-domiciled funds in this sector showed a similar decrease from £2.2 billion in 2013 to £2.1 billion in 2014.

Against the backdrop of an extended low interest rate environment, investor demand for outcome-oriented products appeared to be growing in strength, alongside the returning investor appetite for equity-specific funds. As discussed earlier in this chapter, this may reflect the fact that this is more of a structural shift in the approach to investment rather than a temporary trend.

CHART 56: QUARTERLY NET RETAIL SALES OF TARGETED ABSOLUTE RETURN FUNDS VS. TARGETED ABSOLUTE RETURN FUNDS UNDER MANAGEMENT AS PERCENTAGE OF TOTAL FUNDS UNDER MANAGEMENT (2008-2014)

Source: The Investment Association, Morningstar Direct

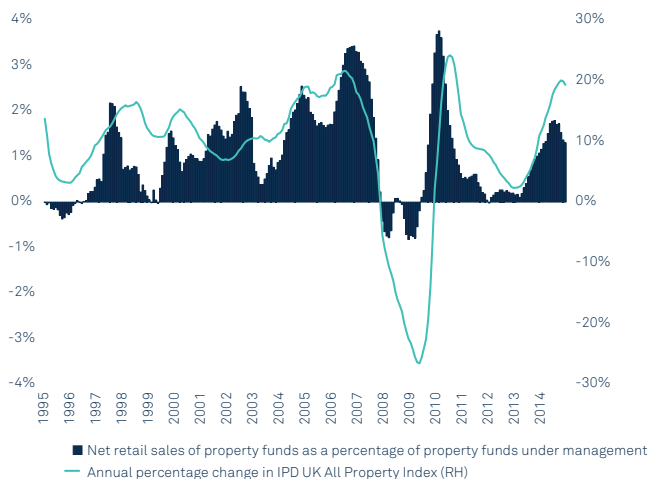
PROPERTY FUNDS

The Property sector posted another year of very strong investment returns as the IPD UK All Property Index increased by 19% during 2014 on a total return basis.

Once again, strong property performance was reflected in sales of property funds during 2014. Net retail sales reached £3.8 billion, which was the highest ever annual figure for the sector.

As we have observed in previous surveys the accuracy with which net retail sales as a percentage of property funds under management track movements in the property market is remarkable. This provides further support to the idea that flows into property funds in 2014, as well as reflecting investor demand for income, may signify cyclical rather than structural investor behaviour.

CHART 57: NET RETAIL SALES OF PROPERTY FUNDS VS. IPD UK ALL PROPERTY INDEX (1995–2014)³⁹



Source: The Investment Association, Lipper IM

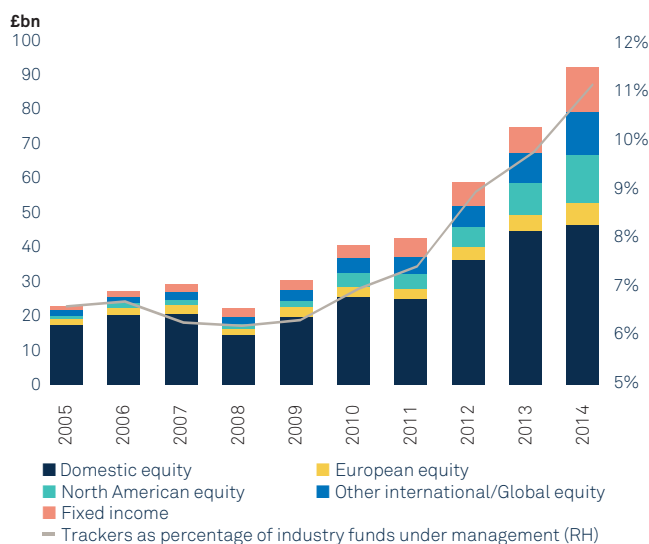
ACTIVE VS PASSIVE FUNDS

Within both retail and institutional distribution channels, the decision to invest only in active or passive strategies is not common. Rather, clients are increasingly becoming exposed to investment processes where there is an element of both strategies within the wider objective.

The Investment Association data on passive index-tracking funds encapsulates figures for UK authorised funds only. The wider ETF market, which continues to expand apace as an increasingly significant subset of the indexing universe, is not included within the figures. At the end of December 2014, the value of the ETF/ETP with a primary listing in the UK was around £120 billion.⁴⁰ The global ETF market saw record flows in 2014, breaking through £300bn (£192 billion) for the first time. There was very strong demand for exchange traded products across Europe in spite of the challenging economic environment, with \$60.1 billion (£39 billion) net inflows. This was more than three times the figure for 2013.⁴¹

Passive UK-domiciled investment funds saw record funds under management of £93.2 billion at the end of 2014.⁴² This represented an increase of 23.5% from 2013 and took their overall share of industry funds under management to 11.2%, compared with 9.8% at the end of 2013. Looking back over a ten year period, passive funds as a proportion of the total were comparatively stable (6%). Post-2008 there has been a significant increase.

CHART 58: FUNDS UNDER MANAGEMENT OF TRACKER FUNDS BY INDEX INVESTMENT TYPE (2005–2014)



Domestic equity trackers showed more modest growth in 2014 compared with the previous year. All other index investment types witnessed double-digit percentage increases in 2014. The fastest growing tracker investments were:

- Fixed Income trackers, which increased by 77% to £13 billion; and
- North American trackers which increased by 51% to £14 billion.

³⁹ Net retail sales of property funds are charted as a six-month moving average of net retail sales as a percentage of property funds under management over the period. The IPD UK All Property index performance is charted as the year-on-year change of the IPD UK All Property Monthly total return index.

⁴⁰ ETFGI, Bloomberg, ETF/ETP providers

⁴¹ Blackrock ETP Landscape

⁴² Includes passive equity flows incorporated within The Investment Association's mixed asset sectors

Passive funds also saw net retail sales of £4.9 billion, which was a new record in its own right (Chart 59). In more detail:

- 94% of net retail sales in index tracking funds, were made through equity fund investments.
- In absolute terms, both Global and UK equity trackers continued to attract large retail inflows of £1.7 billion and £1.2 billion, respectively.
- North American equity trackers had the largest year-on-year increase and were the third best-selling equity tracker behind Global and UK, with net retail sales of just under £1.2 billion.
- European equity trackers saw the smallest increase and recorded a net retail inflow of £442 million in 2014.
- Fixed Income saw a resurgence and a total net inflow of £293 million in 2014.

CHART 59: NET RETAIL SALES OF TRACKER FUNDS BY INDEX INVESTMENT TYPE (2005-2014)

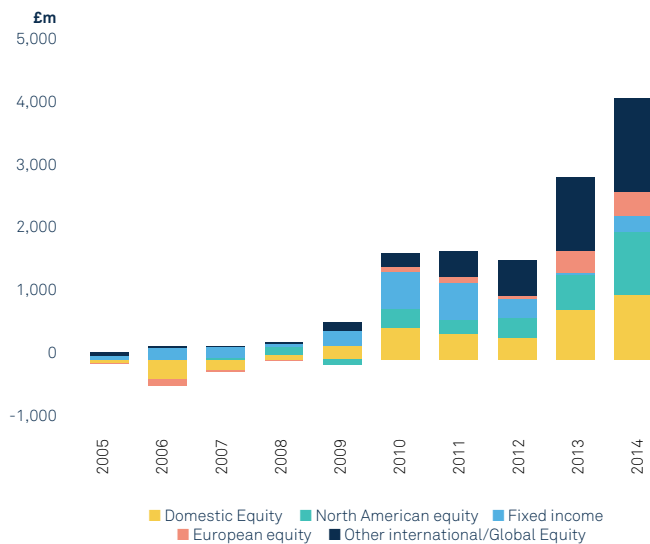
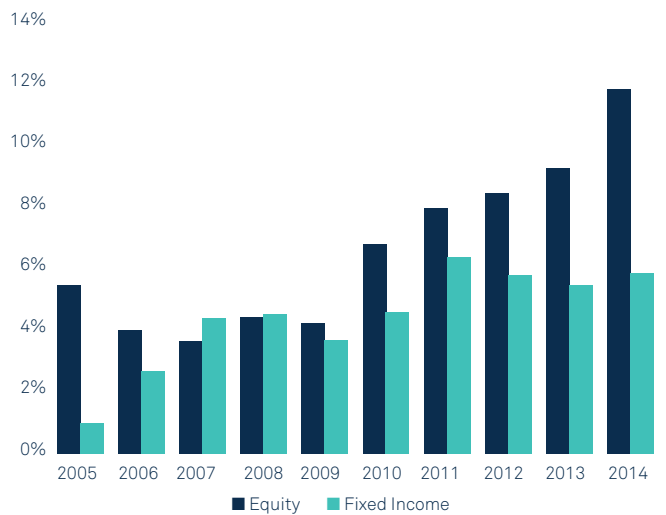


Chart 60 gives an indication of how the popularity of passive funds has increased in recent years. The proportion of fixed income sales that are being directed into passive funds is slightly higher than the levels seen before 2008. However, the really significant change can be seen in the sale of equity funds, where the proportion of sales into passive funds has increased from 4% in 2008 to 12% in 2014.

CHART 60: GROSS RETAIL SALES OF TRACKER FUNDS AS A PERCENTAGE OF TOTAL GROSS RETAIL SALES (2005-2014)⁴³

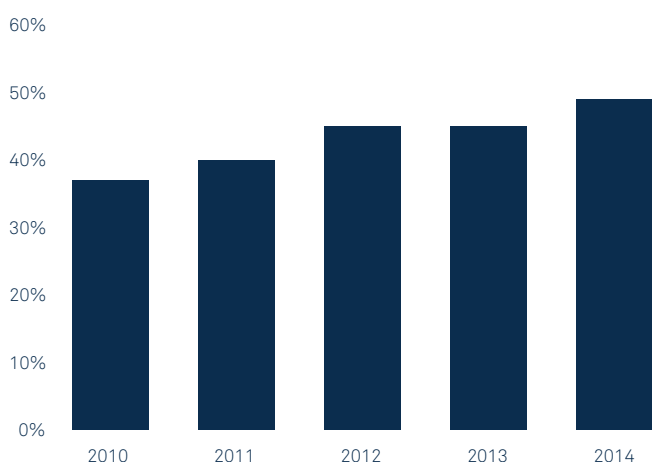


⁴³ Representative sample of funds included in The Investment Association's Equity and Fixed Income sectors. Gross retail sales figures have been plotted in this chart as net retail sales were negative in some years.

FUND DISTRIBUTION

In 2014, UK fund platforms accounted for more than half (55%) of industry gross retail sales (£85 billion), rising from 49% in 2013.

CHART 61: PLATFORM SALES AS A PERCENTAGE OF GROSS RETAIL SALES (2010–2014)



Gross retail sales for Other Intermediaries (includes Wealth Managers, Stockbrokers and IFAs) totalled £58.7 billion in 2014 representing a market share of 38% (42% in 2013).

Direct gross retail sales reached their lowest market share in 2014 at 7.5%, compared to 8.3% in 2013.

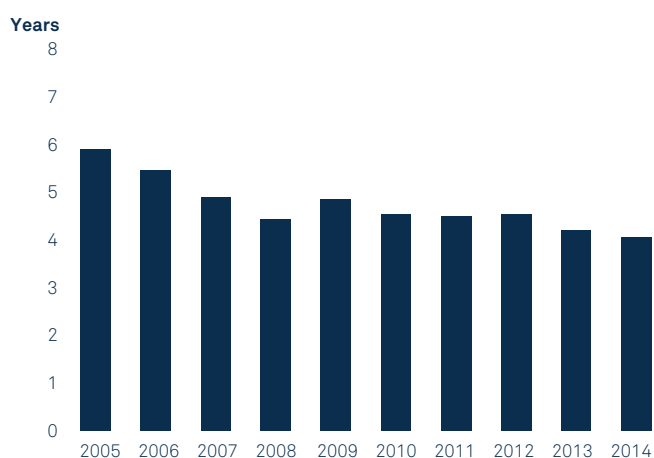
Total net retail sales through fund platforms were £18.4 billion, up from £16.0 billion, in 2014. Platforms therefore accounted for 89% of total net retail sales in 2014.

The increasing popularity of platforms as a distribution channel is also supported by the data we collect directly from five fund platform operators.⁴⁴ These platforms account for three-quarters of the platform market in terms of total transactions. By the end of 2014, they had fund holdings of £182 billion up from £164 billion in 2014. This represents a year-on-year increase of 11.5% compared to a wider industry growth of 8.2%.

Tax-efficient wrappers are the most popular products purchased through platforms. Personal pensions make up 28% of total gross sales followed by ISAs at 27%. Our figures indicate that these five fund platforms held around 45% of the total ISA-wrapped funds in March 2014, up from 32% five years earlier when this information was first collected.

Advances in technology have been a key driver in the evolution of platforms as an intermediary. It is now much easier for investors and financial advisers to buy and sell funds, as well as monitor their performance. These developments are likely to be one of the reasons why fund managers have been experiencing greater flow volatility and fund holding periods have fallen. Nonetheless, Chart 62 shows that the rate of decrease in holding period has slowed significantly and they have been relatively stable between 4 and 4.5 years since 2010.⁴⁵

CHART 62: AVERAGE HOLDING PERIODS OF RETAIL INVESTORS (2005–2014)



⁴⁴ These platforms are Cofunds, Fidelity Platform, Hargreaves Lansdown, Old Mutual Wealth and Transact.

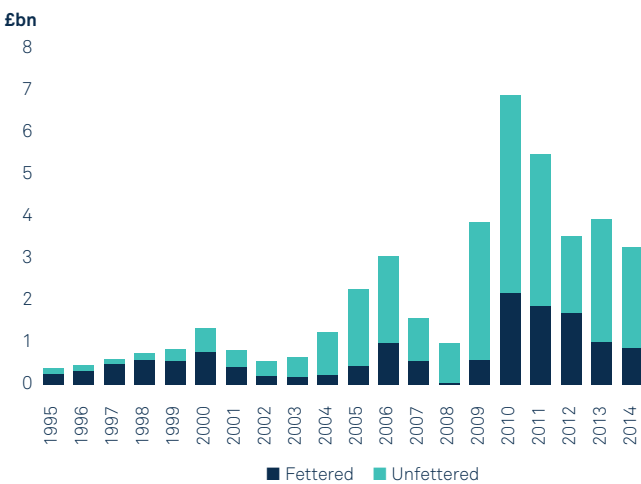
⁴⁵ We calculate the average holding period for retail investors as the inverse of the average redemption rate for retail funds.

FUND OF FUNDS

Funds under management for fund of funds increased by 11% year-on-year to reach £97.6 billion at the end of 2014, accounting for 11.7% of industry funds under management, compared with 11.4% in 2013. This small increase continues the growth in significance of fund of funds over the last ten years. A decade ago fund of funds accounted for just 5.5% of industry funds under management.

Net retail sales for fund of funds in 2014 were £3.3 billion, down from £3.9 billion in 2013 and the lowest since 2008. Net retail sales of fund of funds that invest across a range of asset managers (unfettered) were £2.4 billion in 2014, compared to £870 million for fund of funds invested into the funds of a single manager (fettered). Chart 63 shows that investment in fund of funds was extremely strong in the years following the financial crisis and the trend in recent years may indicate a reversion to more normal levels.

CHART 63: NET RETAIL SALES OF FETTERED AND UNFETTERED FUND OF FUNDS (1995-2014)



In terms of net retail sales, Chart 63 shows that net sales of fund of funds have been on a downward trend since 2010, albeit still well above levels of a decade ago. Unfettered fund of funds have consistently outsold fettered funds in every year since 2002.

Fettered fund of funds now represent just under half of the total holdings in fund of funds. This figure has fallen steadily from ten years ago when it was 55%.

By definition, fund of funds invest across a range of funds and are therefore likely to invest in a mix of assets. Consequently, the majority of fund of funds

assets are accounted for within The Investment Association's mixed asset sectors.

Conversely, mixed asset funds accounted for 48% of the total funds under management among fund of funds. At the end of 2014 fund of funds represented 41% of mixed asset funds.

NEW FUND LAUNCHES

There were 104 newly launched funds classified to Investment Association sectors in 2014, which together received £6.0 billion in net retail sales over the year.

Chart 64 shows the breakdown of these flows between the different asset categories:

- Equities were the predominant choice for flows into newly-launched funds, particularly UK equity funds, which represented over one-half of all new flows.
- Fixed income funds represented a slightly higher proportion of new sales than last year (2013: 6.8%), while both Property and UK-domiciled targeted absolute return funds fell substantially in proportional terms. Property is down from 26% to 14%, and UK-domiciled targeted absolute return is down from 20% to 4.8%.
- The Other category includes funds in the Unclassified sector that cannot be assigned to one of the other broader asset classes.

CHART 64: NET RETAIL SALES OF NEWLY LAUNCHED FUNDS BY FUND/ASSET TYPE

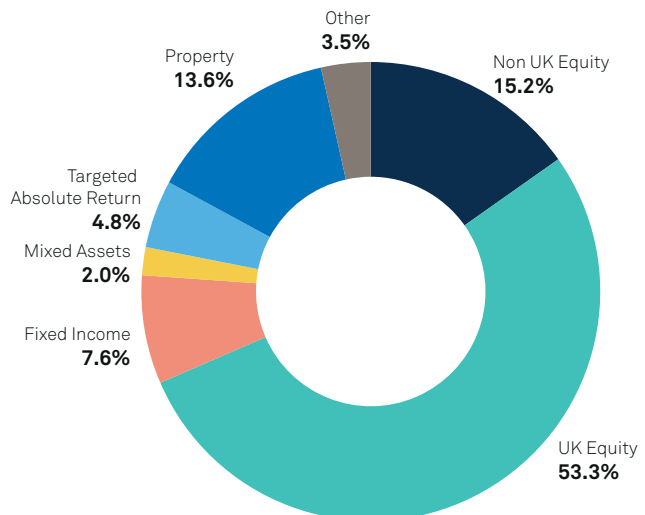


CHART 65: TOP TEN UK FUND OPERATORS BY TOTAL FUNDS UNDER MANAGEMENT

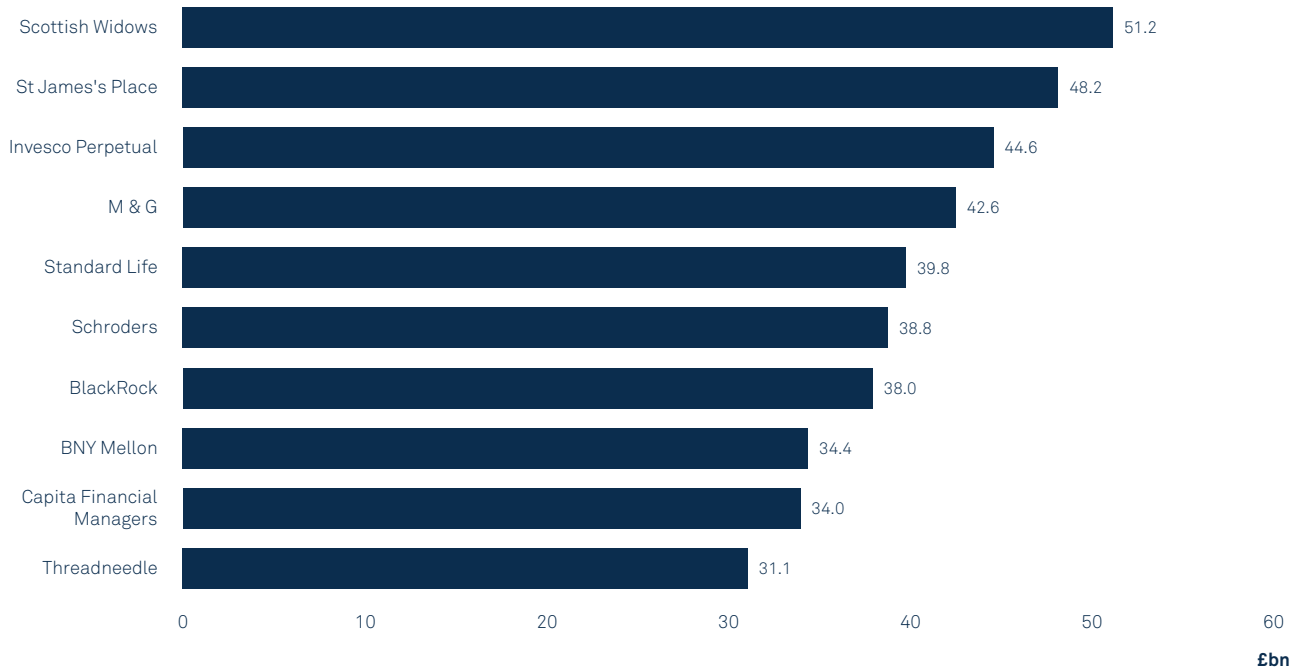
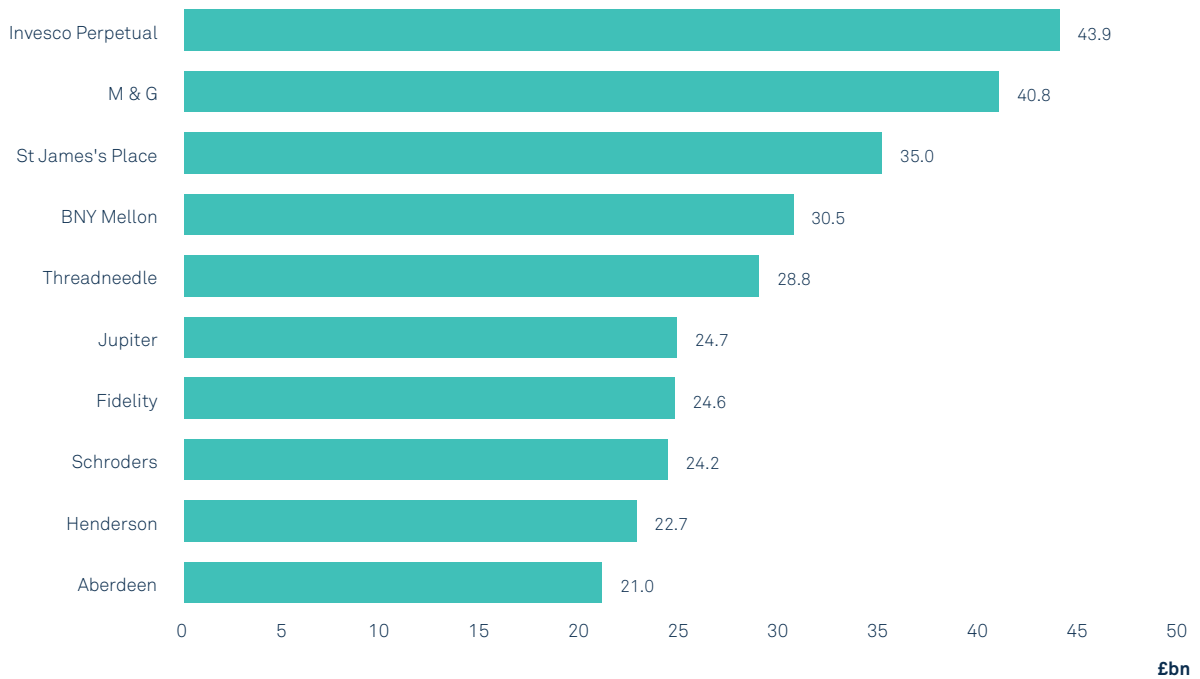


CHART 66: TOP TEN UK FUND OPERATORS BY RETAIL FUNDS UNDER MANAGEMENT



UK INDUSTRY CONCENTRATION AND STRUCTURE

At the end of 2014, we collected data on 103 Collective Investment Scheme (CIS) operators, by which we mean companies operating funds but not necessarily undertaking investment management.

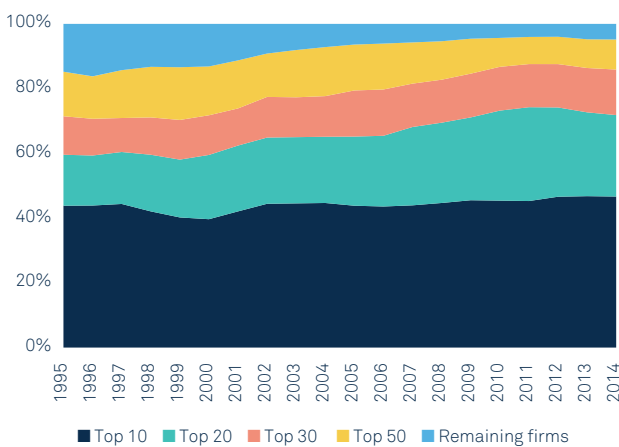
This figure is considerably lower than the 124 groups reporting data a decade ago, and this is predominantly down to substantial M&A activity during this period.

The concentration of the UK fund management industry remains low, with the top ten firms representing 47% of the total UK authorised funds under management at the end of 2014. This proportion has remained broadly unchanged since the early 1990s, underlining the competitiveness of the industry at the top end.

Chart 65 shows the top ten fund operators by total (retail and institutional) funds under management, while Chart 66 shows the top ten firms by retail funds under management only.⁴⁶

The share of the top ten firms in terms of total funds under management has changed little over the last 17 years (see Chart 67). However, this is somewhat misleading as the fund managers within the top ten have varied substantially.

CHART 67: COMBINED MARKET SHARES OF TOP FIRMS BY FUNDS UNDER MANAGEMENT (1995-2014)



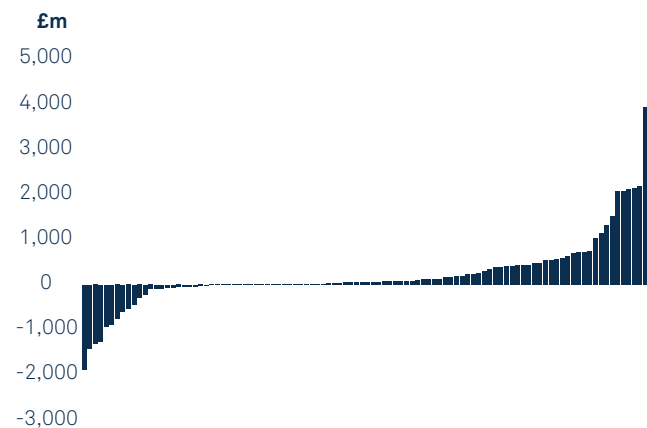
The biggest changes in market share occurred beyond the top ten. For instance, the combined market share of fund companies ranked 11th to 20th increased from 16% in 1995 to 29% at the end of 2011, bringing the share held by the top 20 companies to 74%. That figure has fallen off slightly more recently and stood at 72% at the end of 2014.

Meanwhile, the market share of companies ranked from 21st to 30th increased only slightly between 1995 and 2014, from 12% to 14%. Overall, the top 30 companies took 86% of the market in 2014 – up from 71% in 1995.

When measuring concentration at the manager level, we have used market shares of funds under management rather than sales. This is because funds under management are the main determinant of the industry’s revenue stream, and are most representative of the service that the industry delivers to its investors – the management of their money.

Chart 68 shows the net retail sales for each of the 103 individual fund operators from whom we collected data in 2014, with positive net retail sales reported by 69 CIS operators. This highlights that while overall industry net retail sales were positive, only two-thirds of fund operators actually registered a net inflow. These fund groups reported net retail inflows of £33 billion, offset by outflows of £11 billion. This is at a comparable level to the figures for the previous year.

CHART 68: FUND OPERATOR NET RETAIL SALES (2014)



⁴⁶ In this context, retail funds are defined as funds with a minimum lump sum investment amount of up to £50,000 and with at least one-third of gross sales over the preceding three years being retail.

CONCENTRATION AT ASSET CLASS LEVEL

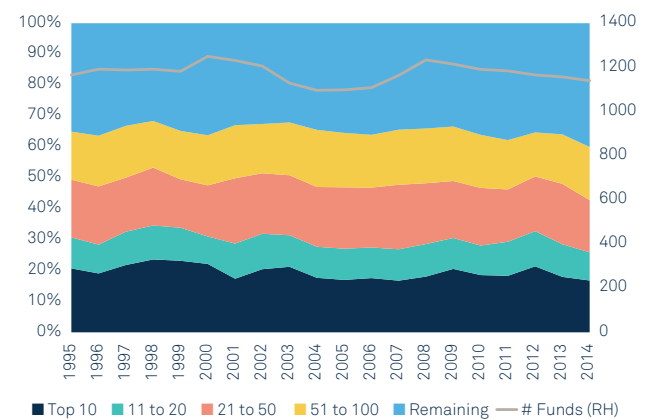
We also considered flows at asset class level to analyse the variations in concentration since 1995. Specifically, we examined the major asset classes of equity, fixed income and mixed asset. The conclusions are as follows:

- Equity fund concentration, as represented by gross flows into the largest 50 funds, has been stable for much of the last 20 years (as has the number of funds), but has dropped since 2012. Overall, there is little sign of increasing concentration within this asset class.
- The number of fixed income and mixed asset funds has grown significantly over the past 20 years. As this has happened, concentration in gross flow terms has fallen, with the largest ten funds accounting for a much smaller part of the market. The market share of the top 100 has also fallen, although to a lesser extent.

As we have previously outlined, the UK funds industry was very equity-focused in the nineties, with equity funds accounting for an 87% of total assets in 1995. Chart 69 shows the concentration of flows into equity funds over the last 20 years and how they have altered. The top 50 equity funds, measured by gross retail sales, represented almost one-half (49%) of the market back in 1995. This remained relatively constant until 2012 but has dropped to 43% at the end of 2014.

Chart 69 also shows the number of equity funds reporting data to The Investment Association and this has been relatively constant over the entire period at just under 1200 funds. This is much higher than either fixed income or mixed asset and so it is not surprising that investors are comparatively more likely to invest in equity funds outside of the top 100.

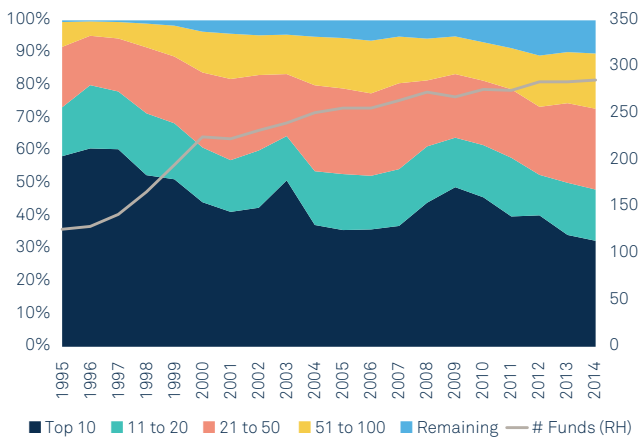
CHART 69: COMBINED MARKET SHARE OF TOP EQUITY FUNDS BY GROSS RETAIL SALES (1995-2014)



The number of fixed income and mixed asset funds available in the market has increased considerably since 1995 and both of these fund types sold particularly well in the times of risk aversion after the dot.com crisis and the credit crisis.

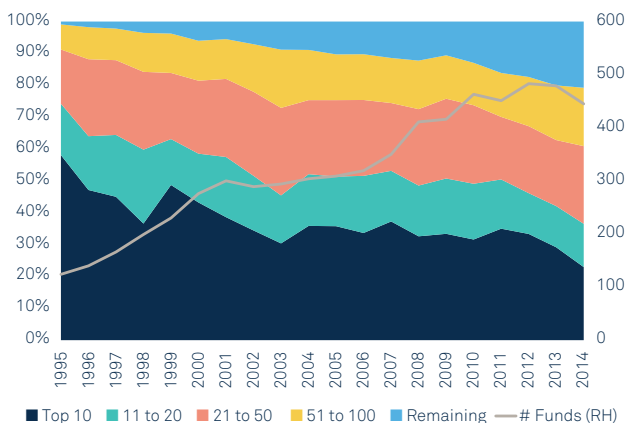
As more fixed income funds have been launched the relative concentration has continued to fall, particularly among the top ten and top 20 funds. However, the market share of the top 100 has remained high (90%).

CHART 70: COMBINED MARKET SHARE OF TOP FIXED INCOME FUNDS BY GROSS RETAIL SALES (1995-2014)



Market concentration also continued to fall as more mixed asset funds were launched, and that trend appears to have continued despite a fall in the number of funds over the last two years.

CHART 71: COMBINED MARKET SHARE OF TOP MIXED ASSET FUNDS BY GROSS RETAIL SALES (1995-2014)



The above charts indicate that the concentration of the market reduces in line with the number of funds available and it makes sense that as the number of available funds increases, more competition will dilute total flows.

We can also look at the distribution of fund assets by comparing the mean and median fund sizes. Table 9 shows that the distribution of fund sizes is highly skewed. At the end of 2014, the average fund size was £367 million but one half of all funds managed less than £97 million, indicating that there are a small number of very large funds.

TABLE 9: MEAN AND MEDIAN FUND SIZES (2005-2014)⁴⁷

| Year | No. of funds | Mean (£m) | Median (£m) |
|------|--------------|-----------|-------------|
| 2005 | 2,003 | 185.1 | 63.0 |
| 2006 | 2,034 | 215.9 | 71.3 |
| 2007 | 2,178 | 230.6 | 69.6 |
| 2008 | 2,366 | 165.5 | 46.6 |
| 2009 | 2,411 | 217.0 | 59.6 |
| 2010 | 2,461 | 259.9 | 69.4 |
| 2011 | 2,480 | 255.7 | 66.3 |
| 2012 | 2,527 | 288.4 | 72.3 |
| 2013 | 2,526 | 336.9 | 88.8 |
| 2014 | 2,513 | 367.1 | 97.3 |

⁴⁷ Figures post 2010 may vary year on year as these figures reflect backdated data for current Investment Association membership

UK FUND MANAGEMENT IN CONTEXT

This section looks at UK authorised funds in the context both of wider UK household savings behaviour and the European fund market.

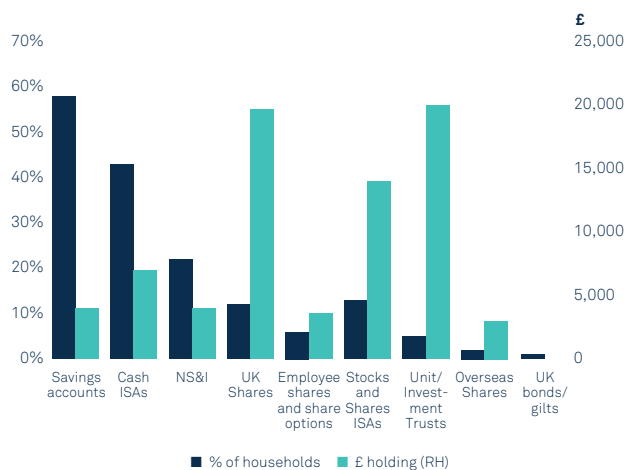
AUTHORISED FUNDS IN THE CONTEXT OF WIDER SAVING

There are three main routes by which retail investors will access authorised funds in the UK, all of which may involve the use of regulated advice:

- Direct investment in units, more commonly intermediated now by a platform rather than a sale by a fund management company.
- Investment via an ISA.
- Investment via a pension, which will show in Investment Association data as institutional flows.

Only around 5% of households invest directly into unit or investment trusts.⁴⁸ This figure has remained relatively stable over the last six years. However, 13% invest in stocks and shares ISAs, the vast majority of which are invested in shares via authorised funds. This has increased from 10% since 2006/08.

CHART 72: PERCENTAGE OF HOUSEHOLDS WITH FORMAL FINANCIAL ASSETS



Source: ONS

⁴⁸ Wealth and assets survey 2010-2012, ONS

⁴⁹ Defined as all pension wealth other than the state pension

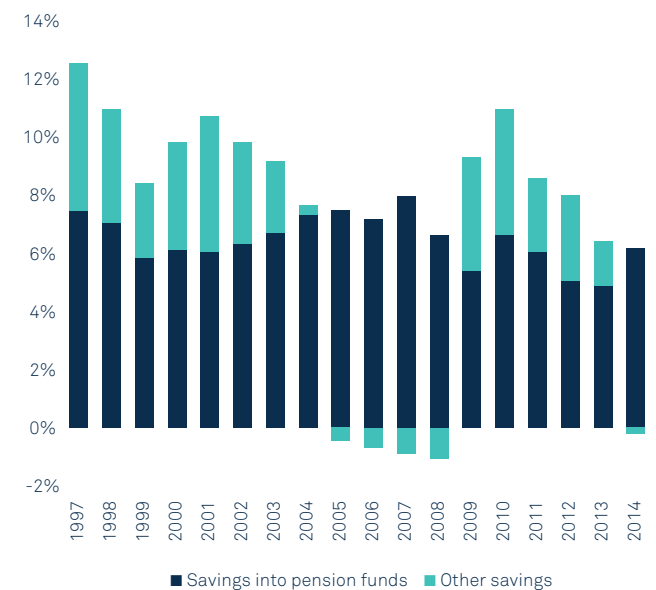
⁵⁰ Figures for household pension savings have been revised by the ONS since the 2013-2014 Survey due to changes in pension accounting methodology outlined on the ONS website.

The above data does not include private pension wealth.⁴⁹ As we see from Chart 73 pension saving represents the overwhelming majority of saving in the UK and in fact other types of saving fell into negative territory during 2014.⁵⁰

Aggregate savings rates for UK households were slightly lower in 2014 (6.0%) than in the previous year (6.4%). This may reflect households feeling a little more confident about the economic outlook and being more willing to spend some more of their income rather than save it.

The average annual savings rate over the four-year period from 2009 to 2012 was 9.2%, which is consistent with the backdrop of greater economic uncertainty prevalent amongst UK householders during that period.

CHART 73: HOUSEHOLD SAVINGS AS A PERCENTAGE OF HOUSEHOLD'S RESOURCES (1997-2014)

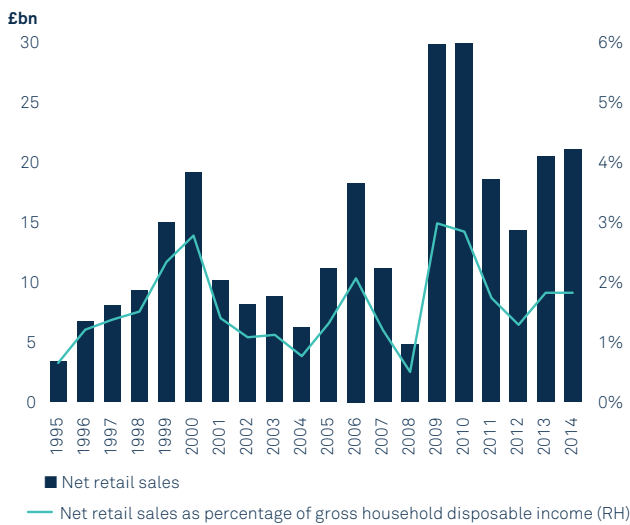


Source: ONS

With millions of new savers now saving via pension arrangements, it would seem likely that the importance of UK authorised funds as a savings vehicle is likely to grow in future, albeit this saving will be reflected in the Investment Association’s institutional data. The retirement income reforms of 2014-15 (p.29) may also be reflected in retail data in due course.

Chart 74 shows that in 2014 households invested 1.8% of their disposable income into funds, which is equal to the level in 2013.⁵¹ These figures suggest that the industry is benefiting from a relatively positive view among investors, especially post-crisis, as investment levels into funds since 2009 have averaged 2.1%, slightly above the long term average of 1.6% per annum.

CHART 74: HOUSEHOLD SAVING INTO FUNDS AS A PERCENTAGE OF DISPOSABLE INCOME (1995-2014)



Source: The Investment Association, ONS

The growing prominence of funds as a vehicle for retail investment is further highlighted in Chart 75, which shows year-on-year growth of the funds under management. The 2014 data shows retail funds of £587 billion, up from a revised £554 billion at the end of 2013. However, the latest data does show that retail funds under management represent a lower overall proportion of total financial assets than last year. Nevertheless, the longer term savings trend remains upward and it is too soon to tell whether this year’s data reflects any permanent change in savings behaviour.

CHART 75: RETAIL FUNDS UNDER MANAGEMENT AS A PERCENTAGE OF TOTAL FINANCIAL ASSETS (2005-2014)

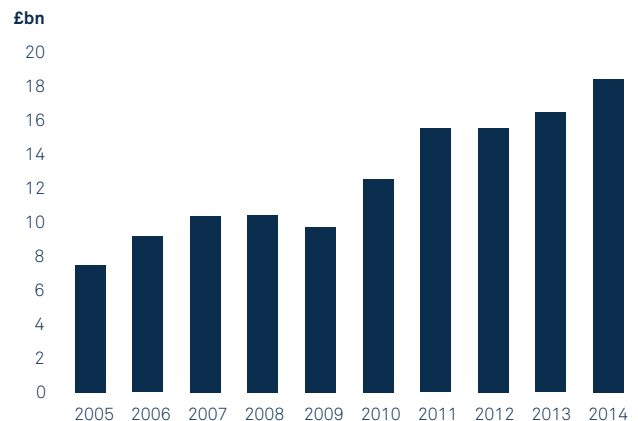


Source: The Investment Association, ONS

INDIVIDUAL SAVINGS ACCOUNTS (ISAS)

Subscriptions into stocks and share ISAs have been increasing steadily, reaching £18.4 billion in the tax year ending April, 2014. The increase in the allowance to £15,240 for the tax year 2015-16 is only likely to contribute to the continuation of this trend.

CHART 76: SUBSCRIPTIONS INTO STOCK AND SHARES ISAS (2005-2014)



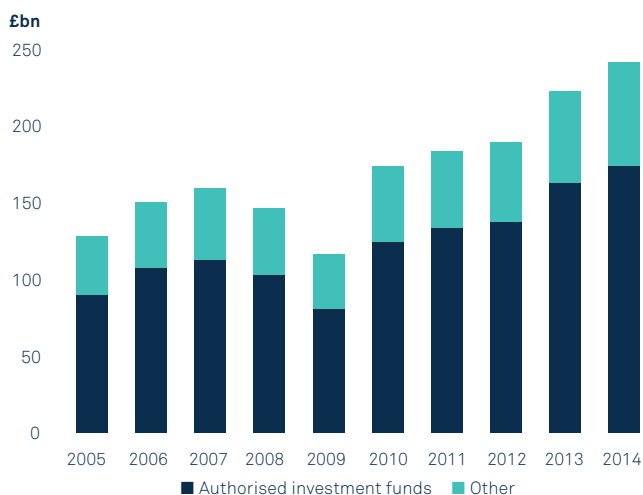
Source: HMRC (tax year ending April 2005 to 2014)

Authorised investment funds are by far the most popular vehicle for individuals to use, with over 70% of ISA assets being invested through them.

⁵¹ Includes direct investment and the portion of the ISA market covered by Investment Association data



CHART 77: FUNDS UNDER MANAGEMENT IN ISAS (TAX YEAR ENDING APRIL 2005-2014)⁵²



Source: HMRC (tax year ending April 2005 to 2014)

There is an increasing number of ISA providers such as wealth managers from which The Investment Association does not collect data. As a result, The Investment Association’s data covered only 77% of the stocks and shares ISA market in funds at the end of the 2013/14 tax year compared to 92% at the end of the 2007/08 tax year. As a proportion of industry funds under management, ISAs have been falling from 31% in March 2004 to 22% at the end of March 2014.

EUROPEAN CONTEXT

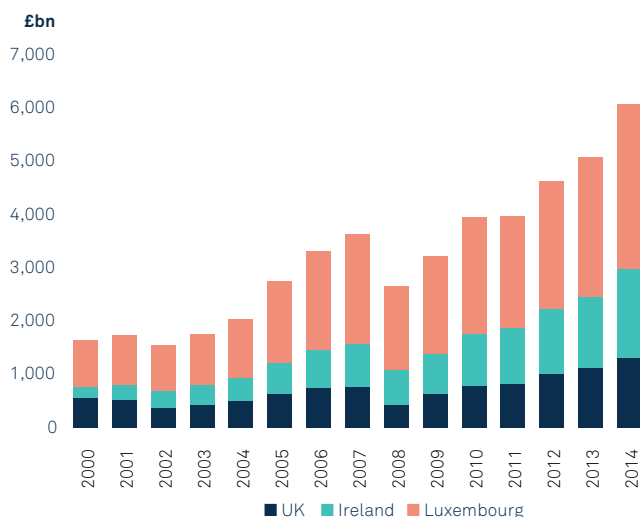
The European investment fund industry had a record year in 2014 with investment funds under management increasing by 15.7% year-on-year from €9.8 trillion (£8.2 trillion) at the end of 2014, to €11.3 trillion in December 2014 (see Figure 9). There are a number of potential reasons for such strong growth, including:

- The search for returns against a backdrop of low interest rates.
- The protection offered to investors by European funds.
- The wide range of available investment strategies.
- Central bank intervention to promote economic growth.

There was no change in the UK’s position as a fund management centre in 2014, remaining fifth, with its market share almost unchanged from 2013 at 11.6%. Ireland made the most significant improvement, rising from fourth place (13.7%) in 2013 to second (14.6%) at the end of 2014.

UCITS accounted for 70% of the total with funds increasing by 16% to €8.0 trillion from €6.9 trillion (£5.6 trillion) at the end of 2014.

CHART 78: FUND ASSETS BY DOMICILE, UK, IRELAND, LUXEMBOURG (2000-2014)



Source: The Investment Association, EFAMA

Looking at this data on a relative basis shows that Luxembourg is still the dominant fund domicile. Although its relative share has fallen very slightly it is still maintaining more than 50% of the share of the three domiciles. The UK on the other hand has recovered somewhat from its lowest showing in 2008 of 17% but seems unable to break through the 22% level, where it has been stagnating for the last three years.

⁵² Authorised funds includes HMRC holding data on Unit Trusts, Shares in OEICs and Corporate Bond Funds

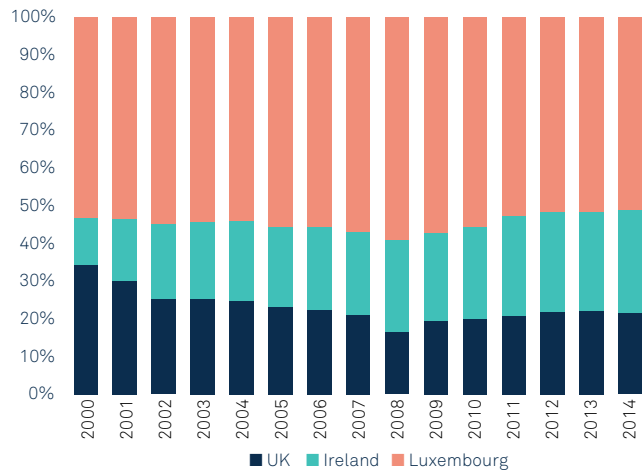
FIGURE 9: EUROPEAN INVESTMENT FUNDS BY COUNTRY OF DOMICILE (DECEMBER 2014)



| Country | Net assets (€bn) | Market share |
|------------------|------------------|---------------|
| 1 Luxembourg | 3,095 | 27.3% |
| 2 Ireland | 1,661 | 14.6% |
| 3 France | 1,584 | 14.0% |
| 4 Germany | 1,582 | 13.9% |
| 5 United Kingdom | 1,319 | 11.6% |
| 6 Switzerland | 416 | 3.7% |
| 7 Sweden | 253 | 2.2% |
| 8 Italy | 248 | 2.2% |
| 9 Denmark | 230 | 2.0% |
| 10 Spain | 230 | 2.0% |
| Other | 723 | 6.5% |
| TOTAL | 11,341 | 100.0% |

Source: EFAMA

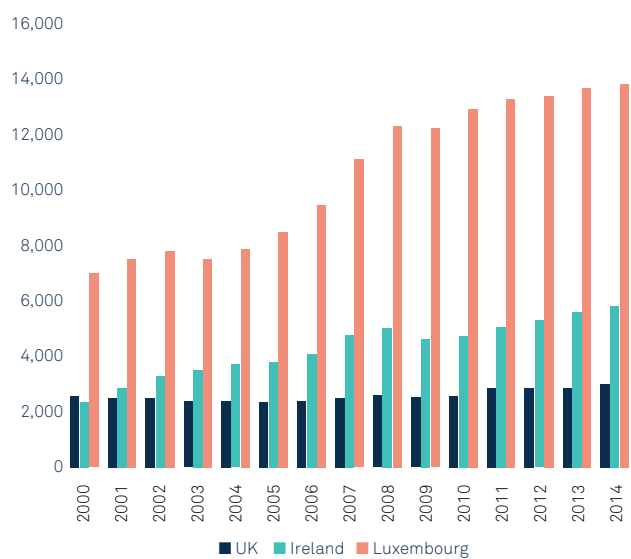
CHART 79: PROPORTION OF FUND ASSETS BY DOMICILE, UK, IRELAND LUXEMBOURG (2000-2014)



Source: The Investment Association, EFAMA

Considering the three locations in terms of the number of funds domiciled there tells a similar tale. Since 2004 the number of funds managed in the UK has increased by an average of 2.3% each year compared to 4.6% for Ireland and 5.8% for Luxembourg.

CHART 80: TOTAL NUMBER OF FUNDS BY DOMICILE, UK, IRELAND, LUXEMBOURG (2000-2014)



Source: The Investment Association, EFAMA



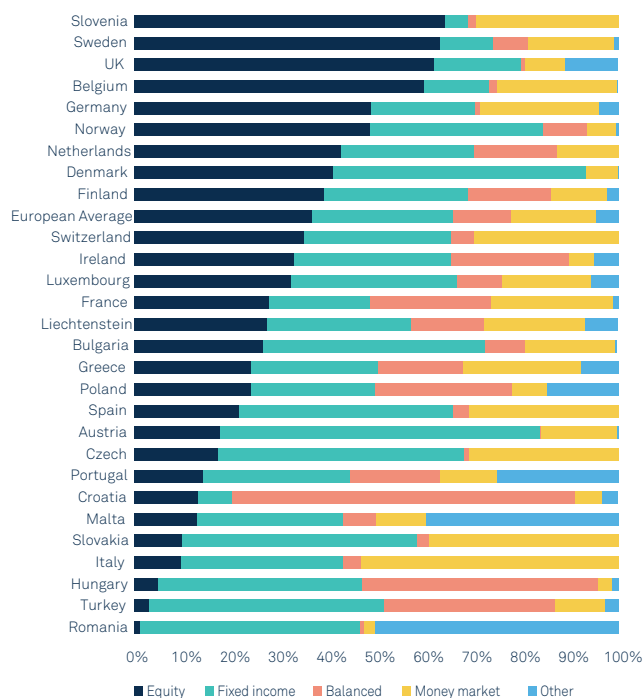
Comparing the types of funds managed in various fund domiciles shows a wide dispersion across European countries. Equities continue to be popular in the UK with only Slovenia and Sweden reporting a higher equity market share.

Sweden is a much larger market than Slovenia, and has been boosted by compulsory funded pension contributions. The European average equity exposure (excluding the UK) is only 29% compared with 62% in the UK.

This is not necessarily a reflection of high risk-taking among UK retail investors, but rather the fact that fund holdings and overall wealth and risk exposure should be assessed in terms of other holdings, such as bank and building society savings or property ownership. Nonetheless, it is widely observed that historically UK (and US) retail investors have a higher tolerance of equity risk than is seen in other large European markets, such as France, Germany and Italy.

Another clear distinction between the UK and the rest of Europe is the popularity of money market funds. Some European retail investors use money market funds as many UK investors would use bank or building society deposit accounts.

CHART 81: BREAKDOWN OF FUNDS UNDER MANAGEMENT BY FUND DOMICILE

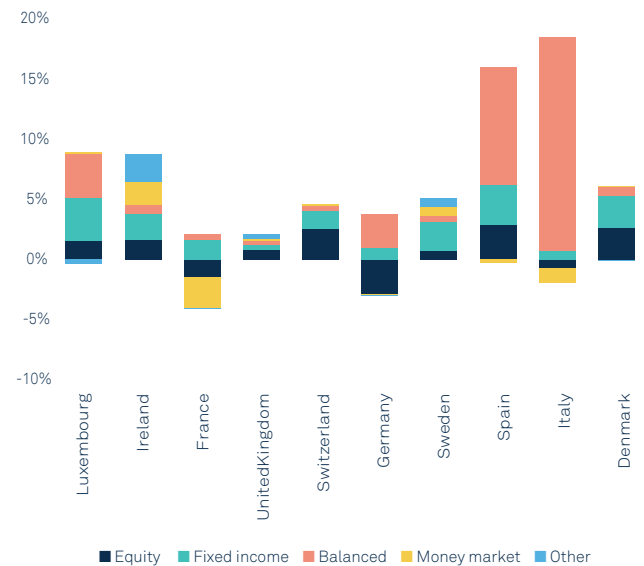


Source: EFAMA

In terms of overall sales, European UCITS experienced net inflows of €464 billion (£362 billion), up from €229 billion (£191 billion) during 2013. Balanced funds reported strong inflows as did fixed income funds, in contrast to the UK. They took in €187 billion (£146 billion) and €191 billion (£149 billion) respectively.

Only money market funds experienced outflows, for the sixth year in a row, of €5 billion (£4 billion).

CHART 82: NET SALES OF UCITS BY ASSET CLASS AS PERCENTAGE OF TOTAL UCITS FUNDS UNDER MANAGEMENT, SELECTED COUNTRIES



Source: EFAMA

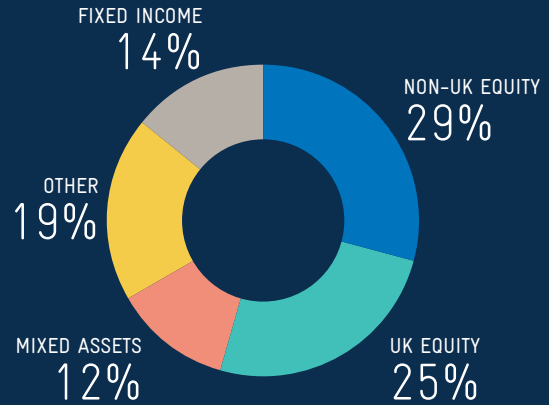
UK AUTHORISED FUNDS

JUNE 2015 UPDATE

FUNDS UNDER MANAGEMENT:



FUNDS BY ASSET TYPE:



TOTAL NET RETAIL SALES: £7.4 BILLION

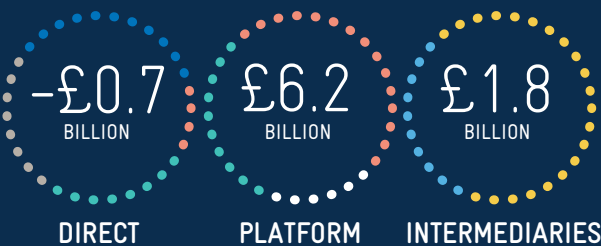
ASSET CLASS:

| | |
|---------------|--------------|
| EQUITY: | £1.9 BILLION |
| FIXED INCOME: | £0.4 BILLION |
| MIXED ASSET: | £1.1 BILLION |
| MONEY MARKET: | £0.6 BILLION |
| PROPERTY: | £1.6 BILLION |

TOP THREE EQUITY REGIONS:



DISTRIBUTION CHANNEL:

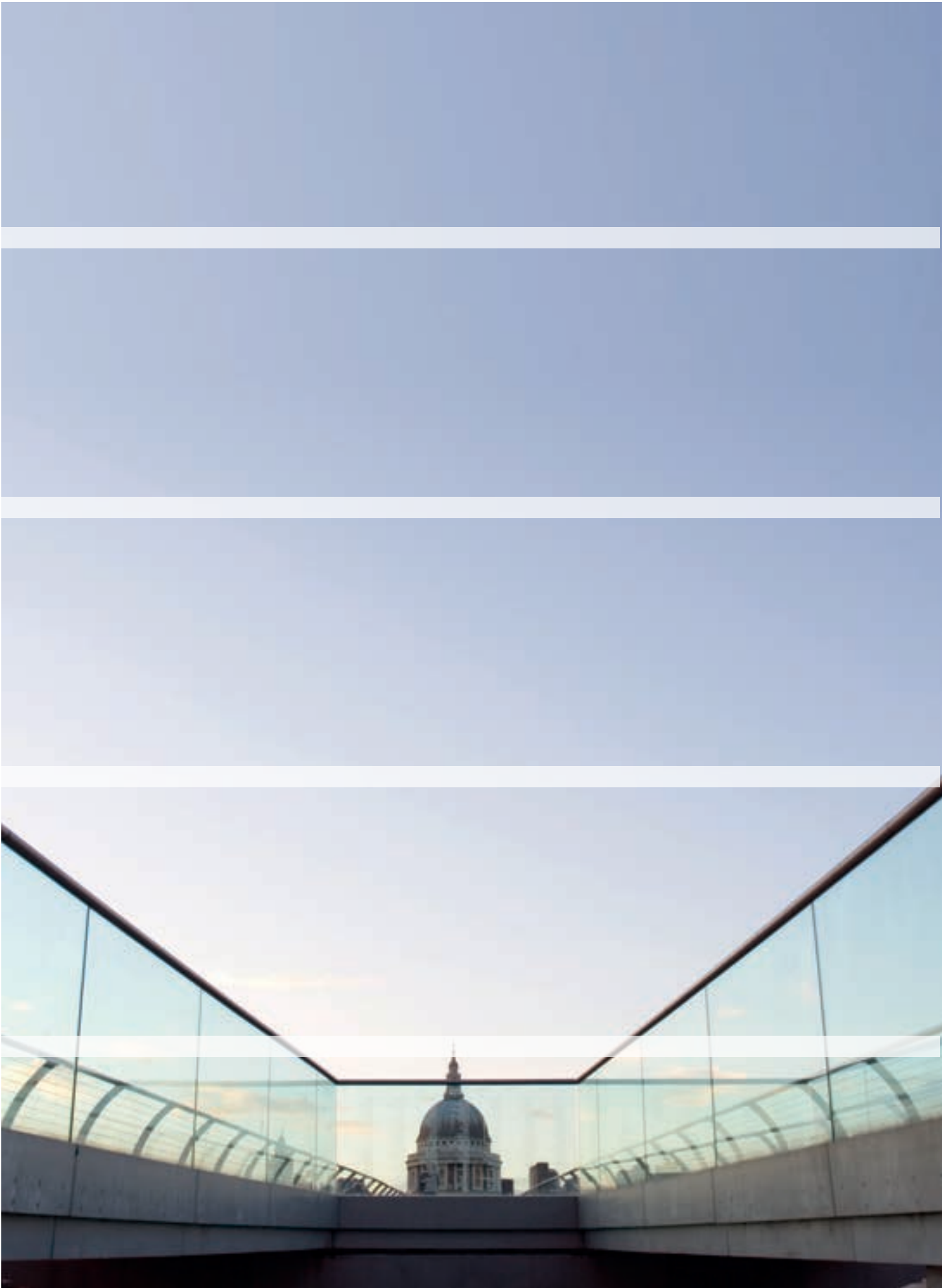


FUND TYPE:



TOP FIVE SECTORS:

- 1 TARGETED ABSOLUTE RETURN: £1.9 BILLION
- 2 EUROPE EX-UK: £1.7 BILLION
- 3 UK EQUITY INCOME: £1.6 BILLION
- 4 PROPERTY: £1.6 BILLION
- 5 GLOBAL EQUITY INCOME: £0.8 BILLION



5 OPERATIONAL AND STRUCTURAL ISSUES

KEY FINDINGS

MARKET OVERVIEW

ABSOLUTE LEVELS OF COSTS AND REVENUE INCREASED SLIGHTLY BUT REMAIN UNCHANGED IN PERCENTAGE TERMS.

- Average industry net revenue (including all activity – in-house and third party) was 31 bps (unchanged from 2013). In absolute terms this represented £16 billion.
- Total operating costs in 2014 were £11 billion, up from £10 billion in 2013 but unchanged at 20 bps.

PERFORMANCE-BASED FEES

NO INCREASE IN USE OF PERFORMANCE-BASED FEES. REMAIN FOCUSED ON INSTITUTIONAL BUSINESS.

- 83% of respondents used performance-based fees during 2014 (80% in 2013).
- 15% of assets under management were subject to performance-based fees.
- 42% applied performance-based fees to retail assets (40% in 2013).
- Only 5% of respondents felt performance-based fees were becoming more prevalent.

EMPLOYMENT IN THE ASSET MANAGEMENT INDUSTRY

EMPLOYMENT IN UK ASSET MANAGEMENT HIT 35,000, WITH SOME BUSINESS OUTSOURCED BY THE MAJORITY OF ASSET MANAGERS

- We estimate that the UK asset management industry directly employed 35,000 people at the end of 2014, with a likely 60,000 employed indirectly in closely related activities.
- Staff in Compliance, Legal and Audit have grown most significantly over the past five years with 52% more people being employed in these roles than at the start of the period.
- Outsourcing continues to be common. More than three quarters of firms (78%) outsourced some part of their business.

INDUSTRY CONCENTRATION

THE UK ASSET MANAGEMENT INDUSTRY REMAINS RELATIVELY UNCONCENTRATED, ALTHOUGH ASSETS MANAGED BY THE FIVE LARGEST FIRMS INCREASED FROM 35% LAST YEAR TO 39% IN 2014.

- There are a large number of small firms in the industry. The median figure for assets under management was £8 billion, compared to a mean of £34 billion.

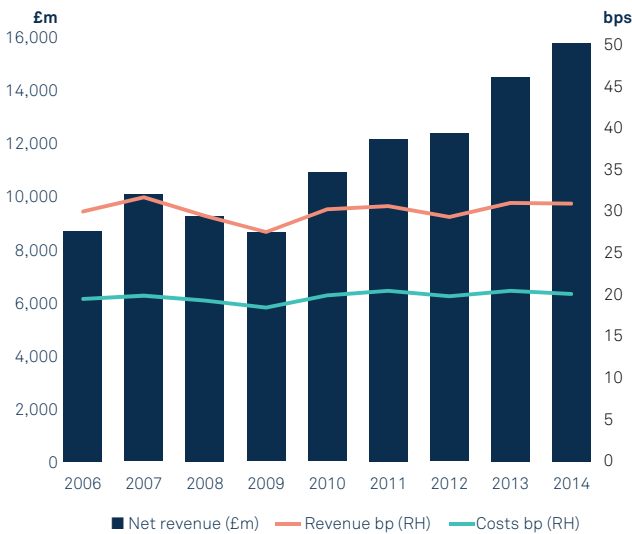
5 OPERATIONAL AND STRUCTURAL ISSUES

REVENUE AND COSTS

The figures shown in Chart 83 cover both in-house and third party business:

- Total average industry revenue after commission was £16 billion, up from £15 billion in 2013. This figure equates to 31bps, the same level as 2013. This compares to global average net revenues of 29 bps.⁵³
- Total operating costs in 2014 were £11 billion, up from £10 billion in 2013. This equated to 20 bps, down marginally from 2013 on a like for like basis.
- These figures imply an operating margin of 35%, slightly increased from 34% in 2013.⁵⁴

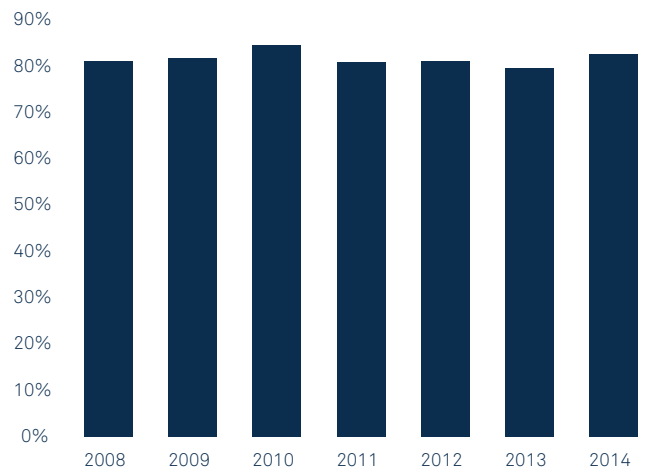
CHART 83: INDUSTRY NET REVENUE VS. REVENUE AND COSTS AS PERCENTAGE OF AVERAGE ASSETS UNDER MANAGEMENT (2006-2014)



PERFORMANCE-BASED FEES

Eighty three per cent of respondents this year reported that they used performance-based fees, slightly higher than 2013 (80%) but generally in line with results from past years.

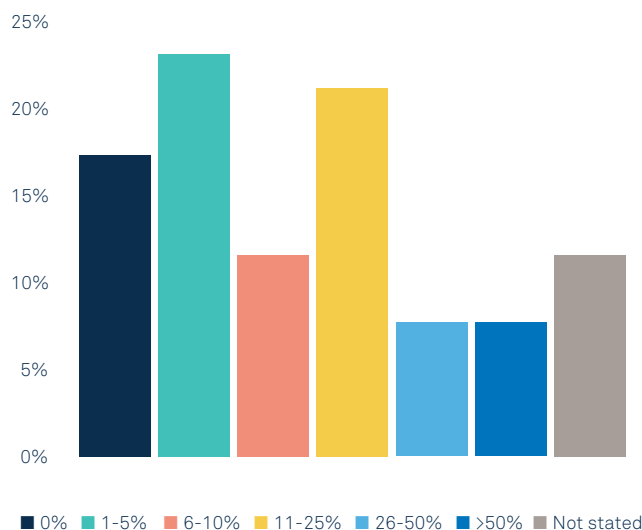
CHART 84: PROPORTION OF RESPONDENTS USING PERFORMANCE-BASED FEES



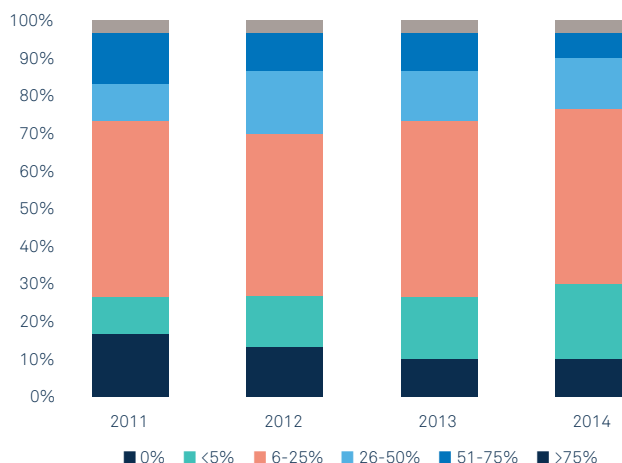
On average, performance-based fees were applied to 20% of assets under management per asset manager. However, the proportion of fees affected is not evenly distributed (Chart 85). Therefore when calculated on an asset-weighted basis, our data suggests that around 15% of industry assets overall are subject to performance-based fees.

⁵³ BCG Perspectives 2015

⁵⁴ Calculated as net revenue less costs divided by net revenue.

CHART 85: NUMBER OF FIRMS APPLYING PERFORMANCE-BASED FEES GROUPED BY THE PROPORTION OF THEIR ASSET SUBJECT TO SUCH FEES


Considering the distribution of assets subject to performance-based fees on an historical like for like basis shows that performance-based fees are more likely now to be used on under 5% of assets under management.

CHART 86: PROPORTION OF COMPANIES USING PERFORMANCE-BASED FEES SPLIT BY PERCENTAGE OF ASSETS TO WHICH THEY APPLY (2011-2014)


Performance-based fees are predominantly applied only to institutional assets. However, 42% of respondents also applied performance-based fees to retail assets.

Consistent with findings in previous years, segregated accounts, hedge funds and targeted strategies were the most common areas of business to which performance-based fees applied.

TABLE 10: PROPORTION OF ASSETS UNDER MANAGEMENT SUBJECT TO PERFORMANCE-BASED FEES

| Percentage of respondents | Total UK assets under management (£bn) | Assets under management subject to performance-based fees (£bn) |
|---|--|---|
| 0% | 201 | – |
| 1-5% | 1,475 | 60 |
| 6-10% | 158 | 16 |
| 11-25% | 993 | 167 |
| 26-50% | 466 | 149 |
| >50% | 180 | 120 |
| Total using performance-based fees | 3,473 | 512 |

Performance-based fee assets under management as a percentage of total

14.7%

Note: Proportions have been rounded to the nearest whole number for each respondent. 12% of respondents used performance-based fees but did not report the proportion of assets relating to them.

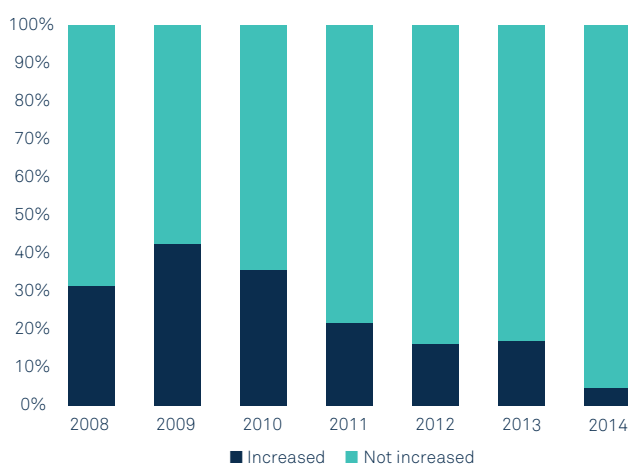
TABLE 11: VIEWS ON THE PREVALENCE OF PERFORMANCE-BASED FEES

| Change in prevalence of performance-based fees over 2014 | Percentage of respondents | Percentage of assets under management subject to performance-based fees | Assets under management subject to performance-based fees (£bn) |
|--|---------------------------|---|---|
| More | 4.8% | 25.8% | 60 |
| Less | 14.3% | 13.1% | 32 |
| Same | 81.0% | 13.8% | 416 |
| | 100.0% | | 507 |

Fewer than 5% of respondents reported that performance-based fees had become more prevalent over the last year. The overwhelming majority felt they had either remained the same or were less prevalent than a year ago.

This continues the trend seen in recent years, which has indicated fewer and fewer respondents believe performance-based fees are becoming more prominent. This is consistent with a gradual reduction in assets subject to these fees from 16.1% five years ago to 14.7% in 2014.⁵⁵

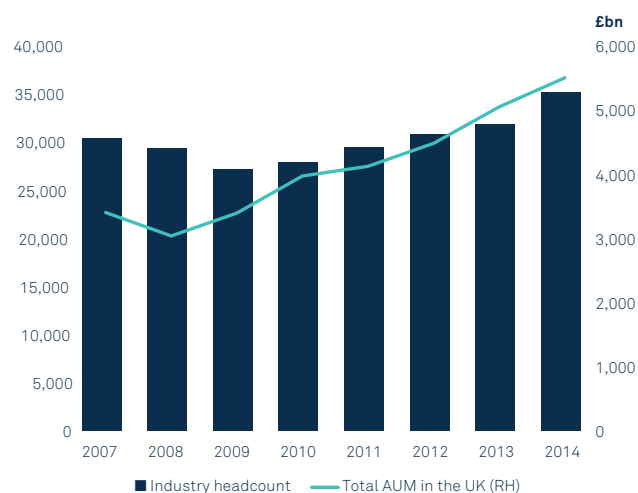
CHART 87: INCREASE IN PREVALENCE OF PERFORMANCE-FEES (2008-2014)



EMPLOYMENT IN THE ASSET MANAGEMENT INDUSTRY

We estimate that the number of people directly employed in the asset management industry in the UK increased from 31,800 to 35,100 illustrating the continued expansion of the industry from its recent low point immediately after the financial crisis.

CHART 88: INDUSTRY HEADCOUNT ESTIMATE VS. UK ASSETS UNDER MANAGEMENT (2007-2014)



In addition to those people employed directly in fund management activities The Investment Association estimates that a further 60,000 people are employed in activities closely related to asset management such as fund and wider administration and securities and commodities dealing activities.⁵⁶

⁵⁵ Last year the figure fell to 12.7% of total asset but this would seem to be somewhat of an anomaly in the gradual trend otherwise noted.

⁵⁶ Source ONS Nomis.

TABLE 12: DISTRIBUTION OF STAFF BY ACTIVITY (DIRECT EMPLOYMENT)

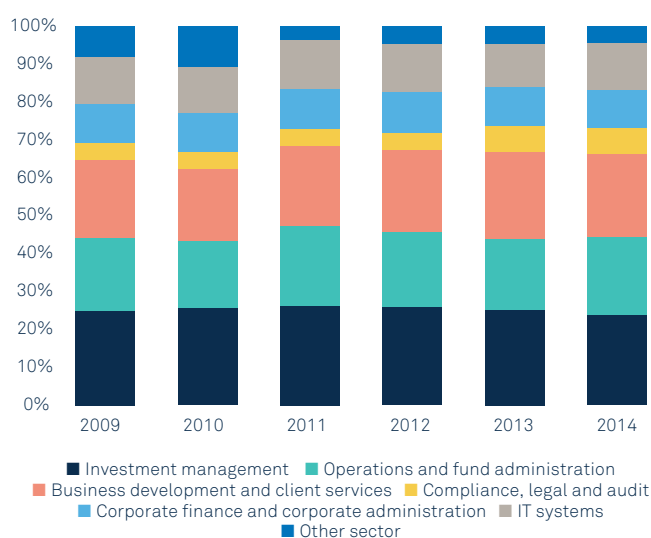
| Activity | Percentage of total headcount |
|--|-------------------------------|
| Investment Management of which | 28% |
| Investment management (asset allocation and stock selection) | 68% |
| Research, analysis | 25% |
| Dealing | 6% |
| Operations and Fund Administration of which | 20% |
| Investment transaction processing, settlement, asset servicing | 37% |
| Investment accounting, performance measurement, client reporting | 41% |
| Other fund administration (incl. CIS transfer agency, ISA administration etc.) | 22% |
| Business Development and Client Services of which | 20% |
| Marketing, sales, business development | 66% |
| Client services | 34% |
| Compliance, Legal and Audit of which | 7% |
| Compliance | 45% |
| Risk | 29% |
| Legal | 22% |
| Internal audit | 4% |
| Corporate Finance and Corporate Administration of which | 10% |
| Corporate finance | 40% |
| HR, training | 22% |
| Other corporate administration | 38% |
| IT Systems | 11% |
| Other Sector | 4% |

Table 12 provides more detail on the number of employees directly employed by asset managers in the UK by function. The proportion of people employed in the largest activity, investment management research and dealing, remained largely unchanged from 2013. There was a small increase in staff working in operations and fund administration; up two percentage points from 18% in 2013. The only other activity experiencing a change was IT which fell one percentage point for the second year in a row.

As absolute year-on-year changes by staff segment are generally relatively small it is potentially more helpful to consider the trend in distribution by staff segment on a like-for-like basis over the last five years. Over that period staff in Compliance, Legal and Audit have grown by 52%, albeit from a relatively low base of 5%. This is consistent with the views we encountered during our survey interviews that the regulatory obligations on firms have increased significantly in recent years.

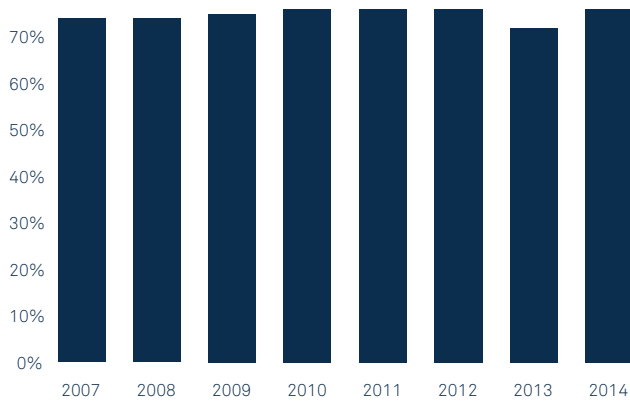
Staffing in operations and fund administration has increased by 6% and staffing in Business Development and Client services by 6%.

Staffing in IT has fallen marginally in the last five years and investment management is 4% lower than its level five years ago.

CHART 89: DIRECT EMPLOYMENT BY STAFF SEGMENT (2009-2014)

An element of staffing in the asset management industry continues to be outsourced both within and outside of the UK. The exact amount is difficult to estimate as firms may not be aware of the precise number of employees taking part in outsourced activities. However, the number of firms reporting that they outsource some part of their activity is significant and there is no meaningful sign of the proportion decreasing. Over three quarters (78%) of firms outsourced some part of their activity at the end of 2014.

CHART 90: PROPORTION OF FIRMS OUTSOURCING SOME PORTION OF THEIR ACTIVITY (2007-2014)



Operations and fund administration were most commonly outsourced. Where respondents provided information on the proportion of activity outsourced, they outsource around two thirds of their operations and fund administration when they outsourced in the UK but slightly less if they outsourced abroad. Ireland was the most common location mentioned.

IT and Compliance were also areas outsourced by a small number of firms (under 10%). Once again firms were less likely to outsource these activities outside of the UK.

INDUSTRY CONCENTRATION

The asset management industry in the UK comprises a small number of very large firms but a long tail of medium- and small-sized organisations. This is indicative that the industry in the UK remains very competitive.

AVERAGE ASSETS UNDER MANAGEMENT AT JUNE 2014

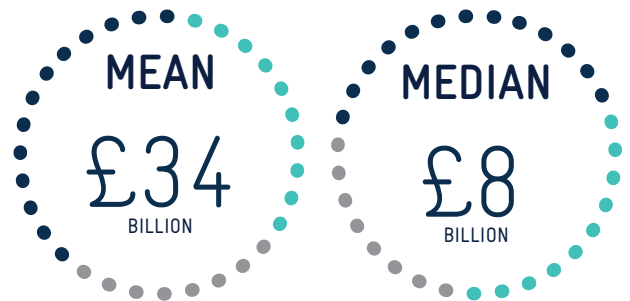
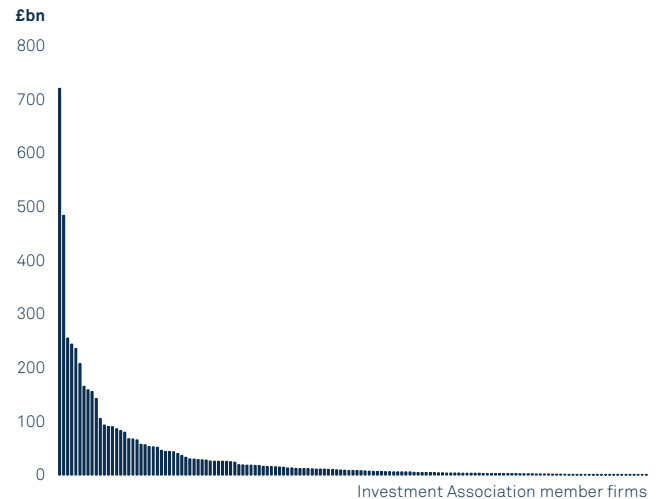


CHART 91: FIRM RANKING BY UK ASSETS UNDER MANAGEMENT (JUNE 2014)



The Investment Association monitors the distribution of member firms by the level of assets they have under management. The distribution has remained relatively stable in recent years. The fall in firms below £1 billion observed in 2013 (June 2013) does not appear to be the start of a trend, as the number recovered to 22 in 2014 (from 18 in 2013).

TABLE 13: ASSETS MANAGED IN THE UK BY INVESTMENT ASSOCIATION MEMBERS BY FIRM SIZE

| Assets under management | No. of firms (June 2014) | Survey respondents (Dec 2014) |
|-------------------------|--------------------------|-------------------------------|
| >£100bn | 11 | 12 |
| £50-100bn | 14 | 10 |
| £25-50bn | 14 | 10 |
| £15-25bn | 14 | 6 |
| £1-15bn | 70 | 24 |
| <£1bn | 22 | 3 |
| Total | 145 | 65 |

The UK asset management industry remains relatively unconcentrated, although as the red line in Chart 92 shows, there has been an increase in concentration in 2014, as measured by standard competition metrics.

The five largest firms represented 39% of assets in 2014, up from 35% last year. Once again, this reflects M&A activity in 2014. The ten largest firms now represent 55% of industry assets, back to levels last seen in 2009.

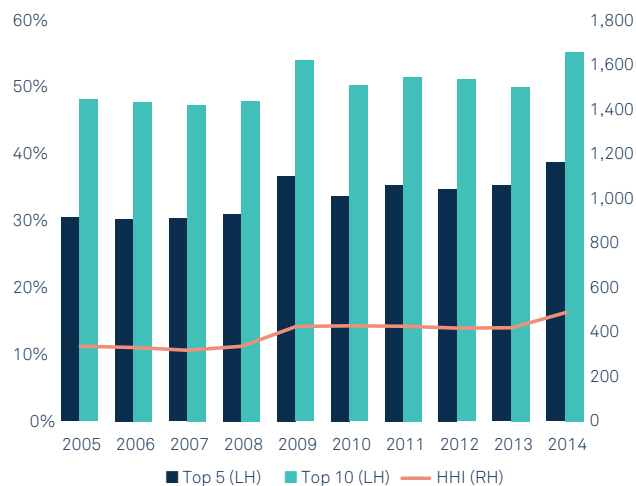
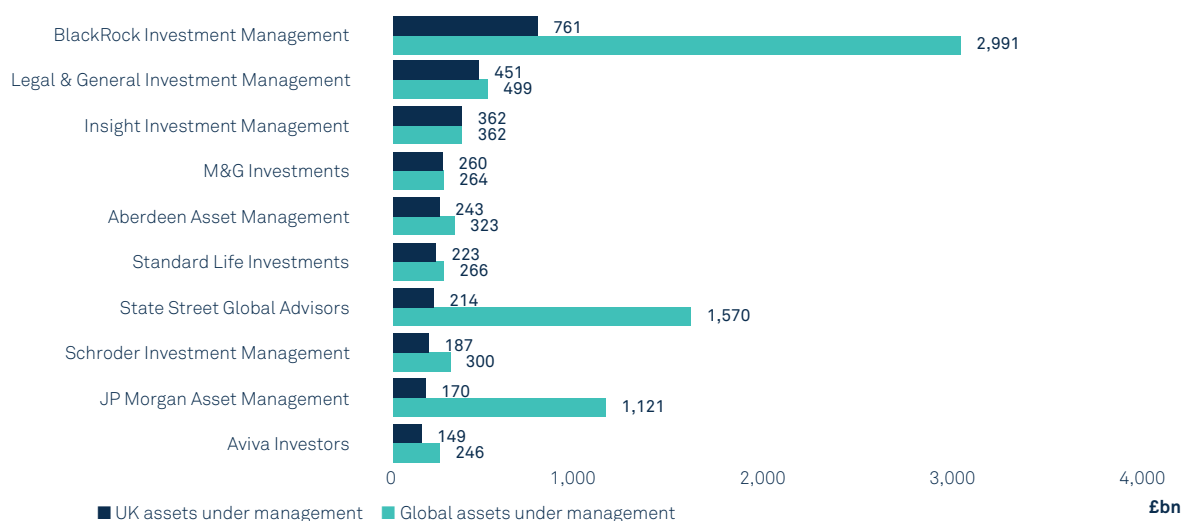
CHART 92: MARKET SHARE OF LARGEST FIRMS BY UK ASSETS UNDER MANAGEMENT VS. HHI (JUNE 2005-2014)⁵⁷


Chart 93 shows the ten largest firms in the UK, measured by UK assets under management.⁵⁸ The top ten includes a mix of active and primarily passive managers. There is also a wide variety of group types in the top ten, including independent asset managers and managers that are part of a larger insurance group or bank.

As the difference between UK and global assets shows in Chart 93, a number of the largest asset managers are primarily UK focused, whereas others have a much wider global footprint.

CHART 93: TOP TEN FIRMS BY UK AND GLOBAL ASSETS UNDER MANAGEMENT


⁵⁷ Herfindahl-Hirschmann Index – a reading of more than 1,000 is usually taken to indicate mild concentration

⁵⁸ Based on headline data supplied to The Investment Association in response to the Survey Questionnaire

BOUTIQUES

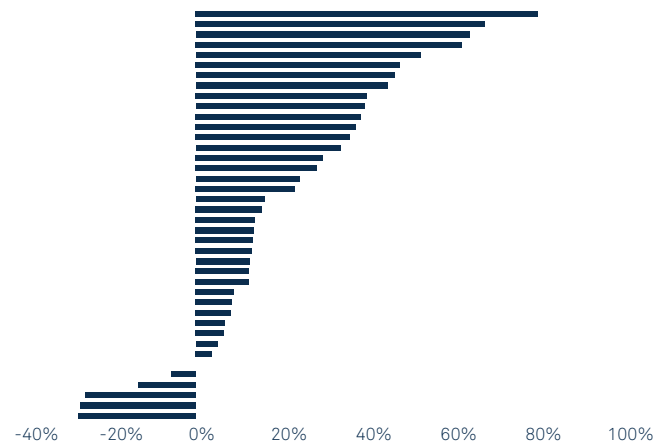
The Investment Association membership contains a number of boutique managers, firms that we broadly define as:

- Being independently owned
- With UK assets below £5.5 billion⁶¹
- Providing a degree of investment specialisation
- Self definition

Thirty four such firms were Investment Association members at the end of 2014. The fall in numbers results from a number of boutique members being acquired by other asset managers and a very small number of members whose rate of growth no longer qualifies them for boutique classification according to our criteria.

Assets managed by boutique managers grew at a slightly lower rate than the industry as a whole 6% vs 9%.

CHART 94: PERCENTAGE CHANGE IN UK-MANAGED ASSETS ACROSS BOUTIQUE INVESTMENT ASSOCIATION MEMBERS (2013-2014)



⁶¹ Increased from 2013 in line with overall asset growth.

APPENDICES

APPENDIX 1

SUMMARY OF ASSETS UNDER MANAGEMENT IN THE UK¹

| | TOTAL |
|---|------------------|
| Assets under management in the UK (£m) | 5,495,462 |
| Segregated or pooled (%) | |
| Directly invested on a segregated basis | 54.0% |
| Managed on a pooled basis | 46.0% |
| Active or passive (%) | |
| Actively managed | 76.4% |
| Passively managed | 20.2% |
| Enhanced index/other | 3.4% |
| Asset allocation (%) | |
| Equities of which: | 42.1% |
| UK | 31.7% |
| Europe (ex UK) | 23.3% |
| North America | 19.6% |
| Pacific (ex Japan) | 7.0% |
| Japan | 5.1% |
| Emerging market | 12.1% |
| Other | 1.2% |
| Fixed Income¹ of which: | 36.0% |
| UK government | 20.3% |
| Sterling corporate | 22.2% |
| UK index-Linked | 15.5% |
| Other UK | 6.4% |
| Overseas | 35.6% |
| Cash/Money market | 6.5% |
| Property | 2.6% |
| Other | 12.8% |

¹ This includes all assets under management in this country, regardless of where clients or funds are domiciled. Caution should be used in undertaking direct year-on-year comparisons with previous surveys. Where relevant or possible, we have used matched results in the survey analysis to validate observations of change.

| INSTITUTIONAL | | | | | | | | ALL INSTITUTIONAL | RETAIL | PRIVATE CLIENT |
|------------------|------------------|-----------|------------|------------------|-----------------------|--------------------------|-----------------------------|----------------------|-----------|-------------------|
| Pension funds | Public sector | Corporate | Non-profit | Sub- advisory | In-house insurance | Third party insurance | Other institu- tional | | | |
| 2,090,534 | 322,255 | 185,210 | 66,736 | 219,644 | 666,490 | 341,025 | 449,346 | 4,341,240 | 1,063,382 | 90,840 |
| 38.0% | 5.9% | 3.4% | 1.2% | 4.0% | 12.1% | 6.2% | 8.2% | 79.0% | 19.4% | 1.7% |

APPENDIX 2

SUMMARY OF DATA FROM THE UK INSTITUTIONAL MARKET²

| | TOTAL |
|--|------------------|
| Total UK institutional client market (£m) | 2,846,220 |
| Segregated or pooled institutional assets (%) | |
| Assets directly invested on a segregated basis | 65.6% |
| Managed on a pooled basis | 34.4% |
| Active or passive (%) | |
| Actively managed | 74.3% |
| Passively managed | 25.7% |
| Multi-asset, LDI or specialist (%) | |
| Multi-asset | 13.6% |
| LDI | 21.8% |
| Single-asset / specialist of which: | 64.6% |
| Equities of which: | 38.2% |
| UK | 30.7% |
| European (ex UK) | 8.4% |
| North American | 8.9% |
| Asia-Pacific | 4.3% |
| Japan | 2.6% |
| Emerging market | 3.9% |
| Global | 35.1% |
| Other | 5.9% |
| Fixed Income of which: | 41.8% |
| Sterling corporate | 25.5% |
| Sterling corporate and government | 21.9% |
| UK government (ex index-linked) | 16.8% |
| UK index-Linked | 12.6% |
| Global | 8.3% |
| Other | 14.9% |
| Cash/Money market | 9.4% |
| Property | 6.0% |
| Other | 4.6% |

² 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 | | | | | | | |
| | 1,216,068 | 203,517 | 65,149 | 17,820 | 70,548 | 39,453 | 124,054 | 615,460 | 297,896 | 196,255 |
| | 42.7% | 7.2% | 2.3% | 0.6% | 2.5% | 1.4% | 4.4% | 21.6% | 10.5% | 6.9% |
| | | | | | | | | | | |
| | 57.7% | 57.9% | 30.0% | 81.5% | 46.3% | 65.2% | 84.3% | 88.7% | 90.0% | 24.2% |
| | 42.3% | 42.1% | 70.0% | 18.5% | 53.7% | 34.8% | 15.7% | 11.3% | 10.0% | 75.8% |
| | | | | | | | | | | |
| | 65.7% | 75.3% | 33.7% | 69.7% | 72.3% | 85.2% | 46.1% | 89.6% | 90.2% | 85.2% |
| | 34.3% | 24.7% | 66.3% | 30.3% | 27.7% | 14.8% | 53.9% | 10.4% | 9.8% | 14.8% |
| | | | | | | | | | | |
| | 10.4% | 8.7% | 3.0% | 10.1% | 12.9% | 47.3% | 5.8% | 15.0% | 34.7% | 7.5% |
| | 32.5% | 24.3% | 0.6% | 0.0% | 11.2% | 0.0% | 0.0% | 8.8% | 1.0% | 8.4% |
| | 57.2% | 67.1% | 96.4% | 89.9% | 75.9% | 52.7% | 94.2% | 76.2% | 64.3% | 84.0% |
| | 43.5% | 65.8% | 65.7% | 54.9% | 26.1% | 47.6% | 55.3% | 26.5% | 26.7% | 28.7% |
| | 19.8% | 28.1% | 27.0% | 0.0% | 30.5% | 16.6% | 35.5% | 58.5% | 38.2% | 28.6% |
| | 5.7% | 6.3% | 3.3% | 51.6% | 8.6% | 1.2% | 8.6% | 15.0% | 14.8% | 4.2% |
| | 7.9% | 10.0% | 8.6% | 0.0% | 1.7% | 1.8% | 6.7% | 13.2% | 12.5% | 4.7% |
| | 3.8% | 2.7% | 1.3% | 0.0% | 1.6% | 4.8% | 4.8% | 6.4% | 4.1% | 8.5% |
| | 2.7% | 2.7% | 1.6% | 0.0% | 6.7% | 1.9% | 8.0% | 1.8% | 1.7% | 2.3% |
| | 4.6% | 3.8% | 2.4% | 16.1% | 5.2% | 4.7% | 1.1% | 2.0% | 4.4% | 5.2% |
| | 48.0% | 43.2% | 50.9% | 32.3% | 44.2% | 64.8% | 25.4% | 2.9% | 19.5% | 28.5% |
| | 7.4% | 3.2% | 5.0% | 0.0% | 1.4% | 4.2% | 9.9% | 0.1% | 4.8% | 18.0% |
| | 47.5% | 23.5% | 22.6% | 15.0% | 13.7% | 5.1% | 21.6% | 53.6% | 50.2% | 14.9% |
| | 30.1% | 25.8% | 30.5% | 11.5% | 28.5% | 27.4% | 20.7% | 17.8% | 34.9% | 6.5% |
| | 8.6% | 13.2% | 5.3% | 7.9% | 6.5% | 46.1% | 15.6% | 45.3% | 8.9% | 30.5% |
| | 19.4% | 14.4% | 9.8% | 0.0% | 5.6% | 13.2% | 11.1% | 15.0% | 10.6% | 38.9% |
| | 19.9% | 27.6% | 26.4% | 17.1% | 2.1% | 0.4% | 18.0% | 6.0% | 2.1% | 2.1% |
| | 11.4% | 9.1% | 21.0% | 31.4% | 36.9% | 9.2% | 20.8% | 3.8% | 5.7% | 2.4% |
| | 10.5% | 9.9% | 7.0% | 32.0% | 20.3% | 3.7% | 13.8% | 12.2% | 37.7% | 19.5% |
| | 1.4% | 1.0% | 7.2% | 15.9% | 44.2% | 34.1% | 6.0% | 11.0% | 4.3% | 39.5% |
| | 4.7% | 6.5% | 3.3% | 12.6% | 12.8% | 4.8% | 3.6% | 8.0% | 4.2% | 7.4% |
| | 3.0% | 3.2% | 1.2% | 1.7% | 3.2% | 8.4% | 13.5% | 0.9% | 14.5% | 9.4% |



APPENDIX 3

MAJOR UK AND EU REGULATORY DEVELOPMENTS AFFECTING ASSET MANAGEMENT

REGULATORS

Regulatory focus on asset management sector

- As set out by Martin Wheatley in the FCA business plan 2015/16, the FCA's continued focus areas for the asset management sector are pension reforms, increased competition, benchmarks, and the industry's preparation for MiFID II/R and MAD/R changes. The FCA is also looking at charging, competition, and understanding customers. The review of how dealing commission is used to pay for research has been a major theme, alongside guidance on the use of hospitality.

ESMA

- ESMA, and ESAs in general, are growing in resources, responsibilities and workload as part of adopting a more direct role in regulation

CAPITAL MARKETS AND INVESTMENT

CSDR

- The Central Securities Depositories Regulation was adopted in September 2014.
- It seeks to harmonise the regulation and supervision of Central Securities Depositories in Europe and harmonise securities settlement practices.
- Although an initial measure would be the imposition of a maximum settlement cycle of T+2 for trades executed on-exchange from January 2015, most European markets, including the UK, anticipated this and moved to T+2 voluntarily in October 2014.
- We expect Regulatory Technical Standards governing settlement discipline, including the operation of the mandatory buy-in regime following a settlement fail, to be adopted in late this year and come into force in 2017.

EMIR

- The detailed implementation of EMIR will continue into 2014. ESMA issued further consultation papers on the mandatory clearing obligation for certain financial instruments. This included interest rate swaps and certain foreign exchange instruments among others.
- The BCBS / IOSCO work on bilateral margining requirements for non-cleared OTC derivatives continued at an international level. ESMA issued a consultation paper to mirror their work implementing the requirements into the EU.
- The European Commission has put out a consultation paper on its required review of the implementation of EMIR in relation to OTC Derivatives, Central Clearing Counterparties and Trade Repositories.
- In view of ongoing issues with the current dual-sided trade reporting regime and the disproportionate burden this is imposing on firms we are preparing to advocate a move to single-sided reporting in our response to the European Commission's review of the legislation.

MiFID II

- MiFID II will come into force on 2 January 2017. This will bring significant changes to the operation of both wholesale and consumer markets.
- Investor Protection Issues: Inducements
 - MiFID II inducements rules are different to the UK RDR regime and the FCA has the task of adopting MiFID II while retaining the logic of RDR. It set out some of the implementation options in a discussion paper issued in March 2015 (DP15/3).
 - MiFID II bans acceptance and retention of fees and commissions, RDR bans payment or receipt. We expect FCA to keep the RDR standard. MiFID II treats independent advice and non-independent advice differently, while the RDR commission ban applies equally to independent and restricted advice. We expect the FCA to maintain its stance.

DP15/3 set out three options, but the most likely result would seem to be an RDR-style commission ban.

- Minor non-monetary benefits: The FCA clarified its view on inducements in non-Handbook guidance issued in January 2014 (FG14/1). The most recently available MiFID II draft regulation looks to be at least as restrictive, although it does permit “minor non-monetary benefits... [that are] reasonable and proportionate and of such scale that they are unlikely to influence an investment firm’s behaviour in any way that is detrimental to the interests of the relevant client”, which seems to be very much open to interpretation. The FCA guidance in FG14/1 remains valid.
 - Quality enhancement: While this requirement is not new, the draft regulation and its list of conditions that would indicate that a fee, commission or non-monetary benefit paid to a distributor by a product provider was not regarded as designed to enhance the quality of service, and therefore not permitted.
 - Product governance: Although MiFID II does not apply to insurance companies or UCITS management companies, the FCA already covers much the same territory through its Regulatory Guide, “The Responsibilities of Providers and Distributors for the Fair Treatment of Customers”, and its supervision activities.
 - All commodity derivatives that do not qualify as hedges for commercial activities will be subject to position limits. Derivatives related to electricity and gas supply are exempted, provided that they are exclusively physically settled, are traded in the new organised trading facilities and are held up to maturity by end-users. Oil and coal related derivatives are not exempted but benefit from a temporary exemption from EMIR CCP clearing and bilateral risk management provisions.
 - High frequency trading:
 - The method of defining the high frequency trading category will be determined in the level 2 negotiations.
 - Firms classified as operating a high frequency trading strategy will be subject to additional systems and controls requirements.
 - Additional market making and presence requirements will be layered on to such firms.
 - Those derivatives that become subject to the central clearing requirement under EMIR will also be subject to an obligation to be traded on a MiFID trading venue to provide a check on OTC transactions.
 - The definition of algorithmic trading will be determined in the 2015 level 2 negotiations. Firms considered to be operating such technology will be subject to material additional systems and controls. It is expected the definition will be drawn very widely.
 - MiFID II will outline significant new transparency requirements for both equities and bond markets.
- Sunset for legacy commission payments**
- The FCA 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 affects all provider payments to platform service providers will mean that the payment of commission to advisers through platforms will end at that date, commission on legacy business that is paid directly by the provider to the adviser would not be affected.
 - One possible outcome is that the combined impact of MiFID II and the likely stance of the FCA in implementing its requirements into UK regulation is that, in effect, such a sunset would be imposed from 3 January 2017, but the Association is planning to take this up with the FCA in order to seek clarity around its intent.

MAD II

- Issued by the Commission in October 2011, the proposals replace the 2003 MAD with a Regulation and a Directive.
- Lobbying targeted numerous issues including the nature of inside information, Chinese walls and exemptions/'safe harbours' from the abuse regime obtained improved near final text by the end of 2013.
- ESMA issued technical advice to the Commission on possible delegated acts concerning the Market Abuse Regulation in February 2015. ESMA's regulatory technical standards regarding MAR will be delivered in July 2015.
- The MAD II package will be implemented on 2 Jan 2017 in line with MiFID II.

Short Selling Regulation

- Implemented in Nov 2012, it regulates short sales, requires the disclosure of significant short positions, bans uncovered short positions in sovereign credit default swaps (CDSs) and grants significant emergency powers to ESMA.
- A review of the implementation was undertaken by ESMA in 2013 Q1.
- ESMA reviewed the implementation of the SSR, to which the Association submitted its views.

LIBOR

- Following the Wheatley Review, IOSCO consultation and work by ESMA in 2012, there is a continued move to regulating indices and their use.
- The British Bankers' Association (BBA) transferred responsibility for LIBOR in 2013, the FCA now has regulatory oversight.
- The FCA is now regulating LIBOR as a significant benchmark.

Solvency II

- Implementation 1 January 2016, with initial reporting by insurers and reinsurers within 20 weeks, with all such firms required to produce a Solvency and Financial Condition Report (SFCR) in prescribed format.
- One issue with SFCR is that some of the information to be published could be confidential or potentially price sensitive.
- In addition to EIOPA templates there are also a number of national specific templates (NSTs). The PRA has consulted within CP16/14 and CP24/14.
- SII continues to have implications for asset managers in terms of disclosure requirements (line-by-line security), service-level agreements and NDAs (possible IP issues); as well as possible implications for asset re-allocation should capital charges be considered too high by insurance clients when reviewing assets held within portfolio.
- Bank of England considering some assurance measures when asset information is published on public websites of insurers.

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

- The Investment Association submitted its response to a Joint Committee Discussion Paper on key options for the content of the Key Information Document, addressing in particular how cost, risk and performance scenarios could be disclosed
- A second, more technical discussion paper was released, looking at how to calculate measures of risks, performance and costs. The European Commission has commenced consumer testing of different presentational options, the results of which will inform the drafting of Regulatory Technical Standards.
- 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.

UCITS V

- The UCITS V Directive was published in August 2014.
- The Directive broadly extends the AIFMD requirements on manager remuneration policy, depositary liability and sanctions.
- ESMA was asked to develop technical advice for the European Commission on two aspects of the depositary provisions. One of these relates to the conditions for fulfilling the requirement for the depositary and manager to be independent of each other.
- The Investment Association provided input to the ESMA consultation and continues to argue for the highest standards for independence; namely, that the depositary and manager should not be permitted to belong to the same financial group. In the UK, this represents current practice and has served investors well.
- Commission L2 measures are expected in Q3, 2015. Member States must implement UCITS V by 18 March 2016.

AIFMD

- The Directive and related Regulation came into force on 21 July 2011. Member States were required to transpose AIFMD into national law by 22 July 2013.
- The Delegated Regulation on information to be provided by Member States to ESMA has been published in the Official Journal. It came into force on 16 April 2015.
- AIFs are any collective investment undertaking that is not a UCITS (irrespective of legal structure, listing, authorisation or domicile).
- The Directive therefore captures a wide range of UK vehicles, including NURs, QISs, unauthorised unit trusts (UUTs), charity funds, investment trusts, and specialist vehicles (eg. hedge funds, private equity funds, venture capital funds and real estate funds).
- It provides a passport for the marketing of AIF to professional investors and imposes detailed regulation on the managers of AIFs (AIFMs), including requirements on organisation, remuneration, safekeeping of assets, liquidity management, valuation and pricing, disclosures to investors and extensive reporting to regulators.
- In November 2013, ESMA issued its guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2) and (4) of the AIFMD. ESMA also issued its opinion on the collection of information for the effective monitoring of systemic risk under Article 24(5), first subparagraph, of the AIFMD and related IT technical guidance and templates.

Venture Capital Funds and Social Entrepreneurship Funds

- 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.
- The EuVECA label appears to have gained some traction over the past year, with 26 EuVECA funds being registered across the EU to date, of which half are domiciled in the UK. However, the EuSEF label has been less successful with only three EuSEF funds having been registered to date.
- The Commission asked ESMA to provide advice on certain Level 2 measures, which ESMA published in February 2015.
- The ESMA advice covers the types of goods and services or methods of production for goods and services that embody a social objective, conflicts of interest, procedures to measure social impacts and the content and procedures for provision of information for investors in EuSEF.

European Long-Term Investment Funds (ELTIFs)

- Political agreement on the ELTIF Regulation was reached at the end of 2014, and the final ELTIF Regulation was published in the Official Journal of the European Union on 19 May 2015.
- The Regulation came into force on 8 June 2015 and takes effect from 9 December 2015.
- ELTIFs will be a regulated sub-set of AIF that invest into long-term illiquid investments such as infrastructure, transport, sustainable energy and small or unlisted companies.
- The fund must be domiciled in the EU, have an EU manager, be closed-ended and of a fixed term. Limited redemption rights may be offered to retail investors from half-way through the lifecycle of the fund.
- Funds authorised under the ELTIF regulation will be able to use the label 'ELTIF' and market across Europe to professional investors and certain categories of retail investors.
- ESMA has been asked to provide the Commission with proposed Regulatory Technical Standards on eligible derivative contracts for hedging risk, determining the lifecycle of a scheme, the orderly disposal of assets, cost disclosure and the facilities available to retail investors.

Money Market Funds

- Commission proposals for Money Market Funds issued September 2013
- The proposed Regulation requires:
 - Certain levels of daily/weekly liquidity in order for the MMF to be able to satisfy investor redemptions;
 - Clear labelling on whether the fund is short-term MMF or a standard one;
 - A capital cushion (the 3% buffer) for constant NAV funds that can be activated to support stable redemptions in times of decreasing value of the MMFs' investment assets;
 - Customer profiling policies to help anticipate large redemptions;
- Some internal credit risk assessment by the MMF manager to avoid overreliance on external ratings.
- There were polarised opinions when the dossier was debated in the European Parliament. Members agreed on a text on 29 April this year. Once Member States have found a general approach in Council, both houses will enter negotiations to agree on a compromise text for the regulation.
- Meanwhile, the US Securities and Exchanges Commission (SEC) has 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.

Appropriateness and the treatment of Non-UCITS Retail Schemes (NURS)

- ESMA's Technical Advice to the Commission stated that all non-UCITS collective investment funds should be treated as complex.
- This outcome would create problems for those managing and distributing NURS funds in the UK as it would mean appropriateness assessments would need to be carried out before execution only trades.
- If the Commission publishes delegated legislation that follows the advice from ESMA, the Association will seek to discuss with the FCA how it can design an appropriateness regime that is aligned to the actual consumer risk involved.

Local Government Pension Schemes (LGPS)

- The outcome of a Government consultation that could profoundly change the way in which LGPS funds use investment management services is expected shortly.
- At meetings with the Department for Communities and Local Government and the Cabinet Office, the Association submitted that the solution to the problems facing

LGPS lay in a combination of approaches, including better governance, rather than a mandatory move away from actively managed investment mandates.

- An Association working group, including members with a strong interest in providing asset management to LGPS funds and involving key people from LGPS (Norfolk CC), has been considering whether to establish an asset management framework to help schemes in the efficient appointment of asset managers.

FIRM REGULATION

CRD IV

- Institutions are required to implement the new Capital Requirements Package from 01/01/2014 with full implementation on 01/01/2019.
- It affects all firms already under the scope of CRD III. The national regulators do have discretion to apply the existing CRD III rules on some MiFID firms. The FCA allows firms who cannot hold client money and who do not carry out MiFID regulated activity which goes beyond portfolio management and the execution of orders on behalf of clients to be subject to the CRD III rules.
- Member states are required to introduce a harmonised sanctions regime.
- The package requires all managers to carry more base capital sets a new, narrower definition of what qualifies as 'capital' for some managers and introduces additional obligations to build up capital buffers.
- Firms are obliged to comply with new liquidity rules and to provide at any time a stock of high-quality liquid assets to meet liquidity outflows. The liquidity coverage ratio will be implemented gradually till 2018.
- New rules on remuneration and bonus caps are introduced.
- Pension fund deficits will have to be deducted from capital.
- By December 2015 the European Commission will have to prepare a report on a prudential regime for investment firms and the treatment of firms which are currently kept under the CRD III requirements.

Remuneration

- EBA published its draft guidelines on sound remuneration under CRD IV
- ESMA published its draft guidelines on sound remuneration policies under the UCITS Directive and AIFMD
- UCITS V will have to be implemented in 2016.
- MiFID II (proposed remuneration elements to be in force by 2016).
- Whilst directives target different key staff, and may overlap in specifics, all of them apply on a firm-wide basis and focus on greater alignment between remuneration, risk-taking and the client's best interests.

CASS

- Following a consultation in 2014, the final FCA rules were implemented 1 June 2015. The changes included:
 - New Acknowledgment Letters for all client money bank accounts (replacing the previous Trust Letters)
 - Client agreements where a firm is utilising DVP exemption
 - Unbreakable Term Deposits no longer than 30 days
 - A reminder of the requirement to issue client money statements at least annually.

- A further FCA consultation will take place in December 2015 on the changes to CASS Rules within MiFID II – however the Level 2 test (due summer 2015) is already broadly in line with the FCA CASS 6 & 7 rules
- There are some CASS requirements within UCITS V, but these will apply mainly to depositaries
- HMT is expected to issue a consultation later in the year to consider SAR arrangements within firms (CASS 7A) and consequences for client assets and client money in the event of a failure of a firm

EU Benchmark Regulation

- The Commission draft legislation has the explicit aim of restoring confidence in the integrity of benchmarks.
- While there are still potential problems around access to some third country indices, the risk that managers who ‘blend’ indices to produce a bespoke benchmark for their fund are deemed to be benchmark administrators has been avoided by getting amendments implemented.

INTERNATIONAL ISSUES

FATCA

- Following publication of a model intergovernmental agreement (IGA) in July 2012, FATCA has been in force since January 2013.
- It impacts funds, their operators, asset managers, platforms and distributors, which are required to report information about US nationals to their tax authorities, which exchange information with the US under existing double taxation treaties and transfer of information exchange agreements.

Dodd-Frank

- Dodd-Frank introduces extra-territorial rules for firms operating in the US or selling to US citizens.
- Concerns that UCITS and NURS managed by subsidiaries of US banking groups or non-US banking groups with operations in the US might themselves be deemed banking entities under the Volcker rule (and thereby subject to restrictions on proprietary trading) have been largely allayed by the publication by the Federal Reserve of a FAQ in June 2015. The FAQ clarified the Agencies view that foreign public funds would not be deemed banking entities provided no more than 25% of the voting shares of the fund were owned by the banking entity after a reasonable seeding period.



APPENDIX 4

NOTABLE M&A DEALS IN THE UK ASSET MANAGEMENT SECTOR (2009-JULY 2015)

| | ACQUIRER | PURCHASE |
|----------------------|-----------------------|--|
| 2014-15 (TO DATE) | Aberdeen | Scottish Widows Investment Partnership |
| | Bank of Montreal | F&C |
| | BNY Mellon | Cutwater Asset Management |
| | Broadstone | Blythwood Group |
| | Brooks Macdonald | Levitas Investment Management Services Ltd |
| | GAM | Singletery Mansley Asset Management |
| | Henderson | 90 West (increased to 100%) Perennial Fixed Interest Partners/Perennial Growth Management |
| | Legg Mason | Martin Currie |
| | Octopus | MedicX Holdings Ltd |
| | 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 | Aberdeen | Artio Global Investors |
| | Aviva | Solar portfolio from Ecovision Renewable Energy |
| | Barings | SEI Asset Korea (SEIAK) |
| | BlackRock | Credit Suisse ETF Business |
| | 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 | 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 |

ACQUIRER

PURCHASE

| | ACQUIRER | PURCHASE |
|------------------------|--------------------|--|
| 2011 | BT | JO Hambro |
| | Close | Cavanagh Wealth Management |
| | Close | Allenbridge Group |
| | Cyrun 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 | Aberdeen | RBS' multimanager 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 Sheppards |
| | Man Group | GLG Partners |
| | Marlborough | SunLife Financial of Canada's funds |
| | Schroders | RWC Partners (49%) |
| | State Street | Bank of Ireland |
| | 2009 | BlackRock |
| 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'.

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 FUNDS 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'.

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.

POOLED

Comprises investment vehicles operated by a manager for several clients whose contributions are pooled. It also includes assets in segregated portfolios that are held indirectly via pooled vehicles managed by the respondent.

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'.

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 managers products).

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 managers 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.

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 Asset Management | Insight Investment Management |
| Aberforth Partners | Invesco Perpetual |
| Aerion Fund Management | Investec Asset Management |
| Allianz Global Investors | JO Hambro Capital Management |
| Architas Multi-Manager | JP Morgan Asset Management |
| Artemis Fund Managers Ltd | Jupiter Asset Management |
| Aviva Investors | Kames Capital |
| AXA Investment Managers | Lazard Asset Management |
| Baillie Gifford & Co | Legal & General Investment Management |
| Baring Asset Management | Lindsell Train Ltd |
| BlackRock Investment Management | Liontrust Fund Partners |
| Brewin Dolphin | M & G Investments |
| Canada Life Asset Management | Martin Currie Fund Management |
| Capita | McInroy & Wood |
| Carvetian Capital Management | Morgan Stanley Investment Management |
| CCLA Investment Management | Neuberger Berman |
| Columbia Threadneedle Investments ¹ | Newton Investment Management |
| Edinburgh Partners | NGAM UK Ltd |
| Family Investment Management | Odey Asset Management |
| FIL Investment Services | Old Mutual |
| Franklin Templeton Investment Management | Pictet Asset Management |
| GLG Partners Investment Funds | PIMCO |
| Guinness Asset Management | Pioneer Global Investments |
| Henderson Global Investors | Premier Portfolio Managers |
| Hermes Investment Management | Principal Global Investors |
| Hewitt Risk Management | Pyrford International |
| HSBC Global Asset Management | Rathbone Unit Trust Management |

¹ Rebranded from Threadneedle Investments in March 2015

RBS Collective Investment Funds

Record Currency Management

Royal London Asset Management

Ruffer

Santander Asset Management

Sarasin & Partners LLP

Scottish Friendly Asset Managers Ltd

Schroder Investment Management

Sharefunds

Skagen

SMT Fund Services (UK)

Standard Life Investments

State Street Global Advisors UK

T.Rowe Price International

TwentyFour Asset Management

UBS Global Asset Management

Vanguard Asset Management

Wellington Management International

APPENDIX 7

FIRMS INTERVIEWED

Aberdeen Asset Management
Allianz Global Investors
AXA Investment Managers
Baillie Gifford & Co
BlackRock Investment Management
Columbia Threadneedle Investments
FIL Investment Services
Henderson Global Investors
Invesco Perpetual
JP Morgan Asset Management
Jupiter Asset Management
Kames Capital
Legal & General Investment Management
M & G Investments
Miton Group plc
Newton Investment Management
Robert Talbut (Independent Director)
Schroder Investment Management
Standard Life Investments
State Street Global Advisors UK
T.Rowe Price International
UBS Global Asset Management
Vanguard Investments

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