ASSET MANAGEMENT IN THE

UNITED KINGDOM

LOCAL MARKET FOCUS

MARKET OVERVIEW

The UK remains one of the largest centers of investment management in the world, second only to the US and the largest center of investment management in Europe, where it is responsible for 37% of total assets under management.

Against a backdrop of volatile markets, total assets managed in the UK by the Investment Association's members were relatively resilient in 2018, ending the year unchanged at £7.7 trillion. This represents around 85% of the wider UK investment management industry estimated at £9.1 trillion in 2018.

The UK investment management industry remains relatively unconcentrated, with assets managed by the top five and the top ten firms stood at 42% and 57% of total assets respectively. Both were one percentage point lower than 2017. The proportion of assets managed by independent investment managers now stands at 44%, more than double the level in 2008 (21%). This is in large part a reflection of high levels of M&A activity seen in the industry over that period.

Almost 40,000 people were directly employed by the UK investment management industry at the end of 2018, up 4% on the 2017 figure, and an estimated 115,000 jobs are supported by the UK investment management industry, either directly or indirectly

However, the UK Asset management industry is under pressure, due to margin squeeze, an ever increasing regulatory burden, macro-economic and political change, such as Brexit, and disruptive business models, such as 'robo-advice'. But this is a market where merger and acquisition may continue to offer valuable synergies and economies of scale.

CURRENT TRENDS

Amid unprecedented economic turmoil and regulatory change, the industry stands on the precipice of a number of fundamental shifts that will shape the future of the asset management industry.

The growth within the UK and global asset and wealth management remains strong. However margins are being squeezed, owing to increasing research, reporting, and technology investment costs and the challenge of justifying and sustaining fee levels.

For active managers, the pressures are heightened by the growing competition from passives and newer low-fee products, like smart beta, along with performance focused active management charging models.

There have been a number of notable recent trends, ranging from the customer centric, to policy, delivery of customer value and an associated emphasis on alignment of interest, transparency and oversight.

One of the most prominent topics on policy has been Environmental Social Governance (ESG). Last year 65.1% of issuers disclosed that they have ESG policies, strategies and goals, whereas regulation remains a key driver for asset managers. Disclosure of ESG strategy and policy is a particularly important factor for the UK market, which topped in ESG strategy, globally, with 92.9% penetration.

There has also been a growing importance of private markets. On the supply side, market-based finance has been more widely used since the Global Financial Crisis and there has also been a decline in the proportion of listed companies. In a persistently low interest rate environment, demand for alternative assets has been strong, particularly in the institutional market.

Another key trend has been challenges surrounding liquidity issues. In January this year, the City watchdog wrote to fund bosses warning that funds are failing to offer customers good value and pledging action on the issues highlighted by the collapse of Woodford Investment Management.

The Financial Conduct Authority (FCA) said in the letter to investment management chief executives that fund governance 'generally falls below our expectations', resulting in funds that 'do not consistently deliver good value, frequently due to failure to identify and manage conflicts of interest’. The intervention from FCA director of wholesale supervision Marc Teasdale comes as the regulator faces criticism of its oversight of fund groups following the high-profile collapse of Woodford Investment Management.

The letter did not name Woodford, but tackles issues highlighted by the collapse, such as fund liquidity and the role of fund authorised corporate directors (ACD). There is a clear disconnect between the appetite for private markets solutions and liquidity within the UK market, thus this could potentially give way to some creative structuring in 2020.

UK WHOLESALE

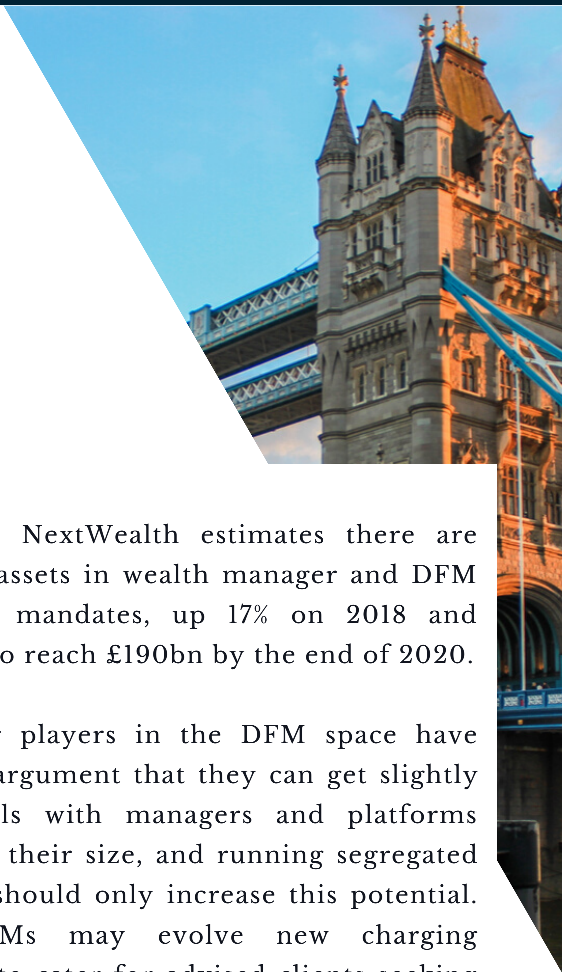
The UK retail funds market has grown significantly over the last 10 years and is increasingly focused on meeting investor demand for investment solutions and outcome-oriented funds.

Both RDR and MiFID II have increased the pressures of transparency on asset managers and continue to have a substantial impact on the cost structure of the industry. RDR was conceived in 2006, based on a ‘fair deal’ for retail investors to provide greater transparency and value-to-cost for the customer. Implemented in the UK in December 2012, RDR was designed to end the potential conflict of interest that arose when investors used independent financial advisors to source funds.

The UK regulator believed some of these advisers were directing their clients to funds that would provide the largest commissions for the advisers. In short,investors were not necessarily receiving the best investment advice. The new regulation increases transparency by making firms outline the fees that an adviser is charging a customer. RDR is now spreading, particularly in Europe, and RDR or similar regulation on fee models and the related disclosures will apply to all major markets including Asia.

Investment firms have been increasingly investing in different models for the mass affluent – it is simply becoming too expensive for many firms to service retail investors, and was a result look to offer more self-directed services. As the mass affluent market becomes increasingly self-directed, the online direct retail platforms stand to benefit.

With a whole raft of commissions taken out of the structure, lower cost models have been driven across the asset management spectrum. The absence of distribution commissions based on a management fee has eliminated incentives for distributors to sell products with high-expense ratios that have no incremental value, further opening up the market for passive and other low-cost products, such as ETFs.



DISCRETIONARY FUND MANAGERS

Key to the success of the top DFMs has been their ability to gradually evolve their business models in recent years. This has driven a number of notable trends:

Centralisation of Decision Making:
Across the five main household names of Brewin Dolphin, Brooks Macdonald, Charles Stanley, Rathbones and Quilter Cheviot, the average increase in profit over their last reporting period was 15.5%. The more established players in the space still have in-house advice arms which sit alongside their discretionary propositions. Brewin Dolphin has been particularly successful in increasing its income from financial planning, which was up 18% last year amid a raft of hires into its new high-net-worth offering, 1762 by Brewin Dolphin. Meanwhile, financial statements from Brooks Macdonald note that its in-house financial planners are a "major introducer" of funds into the wider group.

Institutionalisation of the Process:
A real consensus has emerged that DFMs are becoming more bespoke, and have turned their attention up the value chain towards only the highest-net-worth clients. As the larger DFMs get even bigger, we predict an increase in the use of segregated mandates – funds run exclusively on behalf of a particular client, attempting to marry the best of institutional management with the retail space. Major advice firms like St James's Place use this as a cornerstone of their investment offering. But it is increasingly being adopted by DFMs to fill their model portfolio solutions.

Data from NextWealth estimates there are £112bn of assets in wealth manager and DFM segregated mandates, up 17% on 2018 and predicted to reach £190bn by the end of 2020.

The larger players in the DFM space have made the argument that they can get slightly better deals with managers and platforms because of their size, and running segregated mandates should only increase this potential. Some DFMs may evolve new charging structures to cater for advised clients seeking more passive solutions.

Consolidating Headcounts

Larger players still appear to be able to take on significant increases in assets without a huge rise in staff numbers. Rathbones increased its investment managers from 273 to 277 last year. Though headcount only went up by 4, the firm took on 2,000 extra clients, to reach 50,000. Other big players have seen funds, revenues, and profits increase significantly while reducing headcount.

Brooks Macdonald was down by 2% and Charles Stanley by 4.6%. Some of the smaller or lesser-known players have seen even faster profit growth (albeit from a lower base). LGT Vestra increased profits from £8m to £11m, a rise of some 37%. James Hambro has a higher profit margin than Rathbones, Brewin Dolphin, Brooks Macdonald and Charles Stanley, while LGT Vestra tops Brooks Macdonald and Charles Stanley – again, while also reporting a 7% increase in staff numbers.

RETAIL (ADVISORY), NATIONAL NETWORKS & PLATFORMS

Investors demand for outcome-oriented and mixed asset funds is a long-term trend, suggesting a permanent shift in investor expectations and an increasing emphasis on the role of retail fund managers as asset allocators.

Outflows from UK equity funds have been notable since the Brexit referendum in 2016. Retail outflows over this period of £11billion represent 4.6% of the average UK investor funds under management.

The proportion of UK investor funds under management in passive index-tracking funds has grown gradually to 16% in 2018. The pace of growth has accelerated since 2013 when the retail distribution review (RDR) was implemented. Notably, net flows to tracker funds were one-third of total net sales between 2013 and 2018, a significant increase on the previous five years.

Mintel's ISAs UK report shows that the most important factor for retail investors when choosing the most popular retail investment, a stocks and shares ISA, is clarity on charges (45%). The next two equally important factors are the provider's reputation and the ability to manage the investment online, at 34%. In 2018, UK fund platforms remain the largest distribution channel for UK retail investors by gross and net sales.

45% of gross retail sales flow through UK fund platforms including Hargreaves Lansdown, AJ Bell Youinvest, Charles Stanley Direct, Fidelity, Vanguard etc. Most recently the £45bn merger of Tilney and Smith & Williamson has been put on the back burner, after the Financial Conduct Authority (FCA) uncovered "a number of issues" with the current proposal.

As part of the regulatory process to approve the proposed transaction, the financial regulator has identified a number of concerns with how the deal was being structured.

GLOBAL FINANCIAL INSTITUTIONS

With asset managers paying increased attention to the 'Global Accounts / Global Banks' channel referred often as 'GFI or FIG channel', we have observed numerous internal Head of Global Financial Institutions appointments normally based in London, Zurich or Frankfurt.

This mandate is typically detrimental in leading virtual sales team across all European jurisdictions; ensuring the alignment of servicing and growth within this channel.

TALENT IN DEMAND

Sales teams have been greatly affected by the recent trends in the UK wholesale channels with several notable trends emerging:

1. Smaller, more centralised teams based outside of London: The rise of the retail platforms, national networks, D2C channel and increased consolidation within the discretionary channel has instigated a decrease of traditionally large regionally based sales teams.

Large UK asset managers are looking to further consolidate their regional sales professionals, whilst medium to small asset managers are covering the UK wholesale market with an average of only 3 sales professionals. Furthermore, since most of the decisions within the discretionary channel are now being made in London, sales professionals tend to arrange regional trips once their funds are on their buy list.

2. Institutionalisation of the wholesale channel: As the process of winning mandates/ establishing partnership in the UK wholesale channel becomes more and more institutional in nature, there is an increased demand for sales professionals who can demonstrate a high technical aptitude (quasi product specialists) and provide a more sophisticated level of service traditionally expected within the institutional channel.

Generally speaking, the most desirable skills for sales professionals are currently:

- Highly technical and solutions oriented.
- Institutional in approach and delivery.
- High in activity, but focused on long term partnerships.
- Established relationships across all segments of the UK Wholesale channel.

RECENT MARKET MOVES:

Edward Malcom joins J.P Morgan Asset Management as Executive, Director UK Distribution; **Phil Middleton** has been promoted to Head of UK Intermediary at Schroders; **Howard Fryer** has moved to Fulcrum Asset Management as Sales Director; **Fay Hendon** has moved from Aviva Investors to HSBC Global Asset Management as Head of UK intermediary business development; **Fergus McCarthy** is now UK Distribution Director for Regional Accounts at Standard Life Aberdeen, whilst **Michael Beveridge** left Standard Life Aberdeen for BNY Mellon Investment as Head of UK Intermediary Distribution.

Kristy Barr has been appointed to UK Distribution Director, Head of Key Accounts at Aberdeen Standard Investments; **Mark Thomas** has moved to Jupiter Asset Management as Head of UK sales; Both **Andy McNulty** and **Angus Duncan** have moved from JP Morgan Asset Management, to join Fidelity International and UBS Asset Management respectively. **McNulty** is now International Director of Wholesales Sales and **Duncan** is Head of Discretionary Sales

Mark Buckley has joined Janus Henderson Investors as Associate Director for South East Sales; **Alex Dacres-Hogg** is now at Muzinich & Co as Associate Director, UK Wholesale Distribution; **Steven Adam** has moved to Neuberger Berman as Relationship Manager; **Alex Beck** joined Kames Capital as Business Development Manager (South East of England); **Rod Ringrow** has moved to Invesco where he will now be Head of UK Fund Sales; **Ravinder Azad** has joined Windsom Tree where he will head up UK & Nordics Sales.

KEY CONTACT

ANA MARIA TULIAK
PARTNER
ANAMARIA.TULIAK@LUDGATESEARCH.COM
+44 (0) 20 3 145 3363

Ana Maria holds a 1st class degree in International Business and speaks Italian, French, Croatian, and Slovenian.

Ana Maria began her career at a boutique search firm where she was responsible for developing their Distribution, Asset Management desk. In 2012, she joined BRUIN Financial, sister company to Ludgate Search, to grow and lead their European Distribution team, focused specifically on senior assignments in Asset Management, Alternatives and Wealth.

In 2017, Ana Maria was mandated to grow Ludgate Search, the Executive Search arm of The FISER Group. She focuses on senior distribution mandates, specifically capital raising roles in Europe including roles based in UK, Nordics, Germany& Austria, Benelux, France, Switzerland, Italy and Spain.