

Asset Management Strategic Imperatives for Asset Managers

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Table of contents

<i>Foreword</i>	<i>1</i>
<i>Executive summary</i>	<i>2</i>
<i>Macro trends</i>	<i>3</i>
Rise and interconnectivity of the emerging markets	
Demographic change	
Social and behavioral change	
Technological change	
Rise of state directed capitalism	
<i>What questions should executives be asking?</i>	<i>9</i>
<i>Contacts</i>	<i>12</i>

Foreword



After the financial crisis of 2007-09, a recession and the volatile markets of 2011, the Canadian, US and global economies have been undergoing a modest, if tentative, upturn, and the asset management industry similarly has been recovering, experiencing improved valuations, increased assets under management and enhanced margins.

Even as it enjoys this mild resurgence, the industry continues to face challenging markets, the implementation of regulatory reform initiatives, competition for clients and talent and new expectations from investors, regulators, industry partners and other stakeholders.

Under such circumstances, asset managers are attempting to generate improved performance results, rebuild profitability, manage risk, compete for talent and achieve the operational excellence that will drive future growth.

This report identifies the strategic imperatives for the asset management industry and the key implications for asset managers, and the questions firms should be asking to best adapt their strategies and take advantage of these new and emerging industry demands.

In spite of these challenges, the asset management industry is well positioned to deliver performance and experience future growth. However, success is not guaranteed nor will it be universal. The firms that succeed will be those that can take transformational steps to adapt to changes in the industry and take advantage of the opportunities opening up in the global marketplace. Those firms that can successfully adapt and compete will be the winners in this larger arena.

PwC is committed to working with its clients and partners in the asset management industry to help them develop effective solutions for the business issues they encounter. We look forward to hearing your thoughts on these issues. Please feel free to contact any of our partners listed in the back of this report if you wish to discuss any of these issues.

A handwritten signature in black ink, appearing to read 'Raj Kothari'.

Raj Kothari, FCA
GTA Managing Partner and
National Asset Management Practice Leader

Executive summary

We are seeing a **transformation of the asset management industry** as traditional guideposts are replaced by a new set of market demands. Economic, technological, behavioral and demographic macro trends are driving the need for firms to re-evaluate their strategies and business models. Asset managers must hone their ability to foresee these future trends and adapt accordingly in order to **secure a competitive advantage** with their clients.

Firms will need to **critically review their corporate strategies** based on projected long-term trends; the outcome should result in innovative products and accessing new and/or rapidly growing distribution channels with a dedicated focus on the evolving needs of investors.

While many asset managers will develop similar product offerings to cater to shifting demographics (e.g., most managers already

offer retirement solutions), **differentiated products that focus on alternatives, exchange-traded funds, hard assets and emerging asset classes will dominate**, as will total and absolute return strategies.

Large organizations with scale, including multi-boutique managers, **will continue to prevail** as they offer a diversified product mix geared to the separation of alpha from beta. Both types of organizations will command a significant competitive advantage over those managers that specialize in traditional asset classes and are unable to diversify into new products.

Organizations that focus on the complete investor experience, from awareness through servicing, will attract and retain more assets. Online presence and **social technology tools will be increasingly leveraged** by asset managers to deliver a superior customer experience.

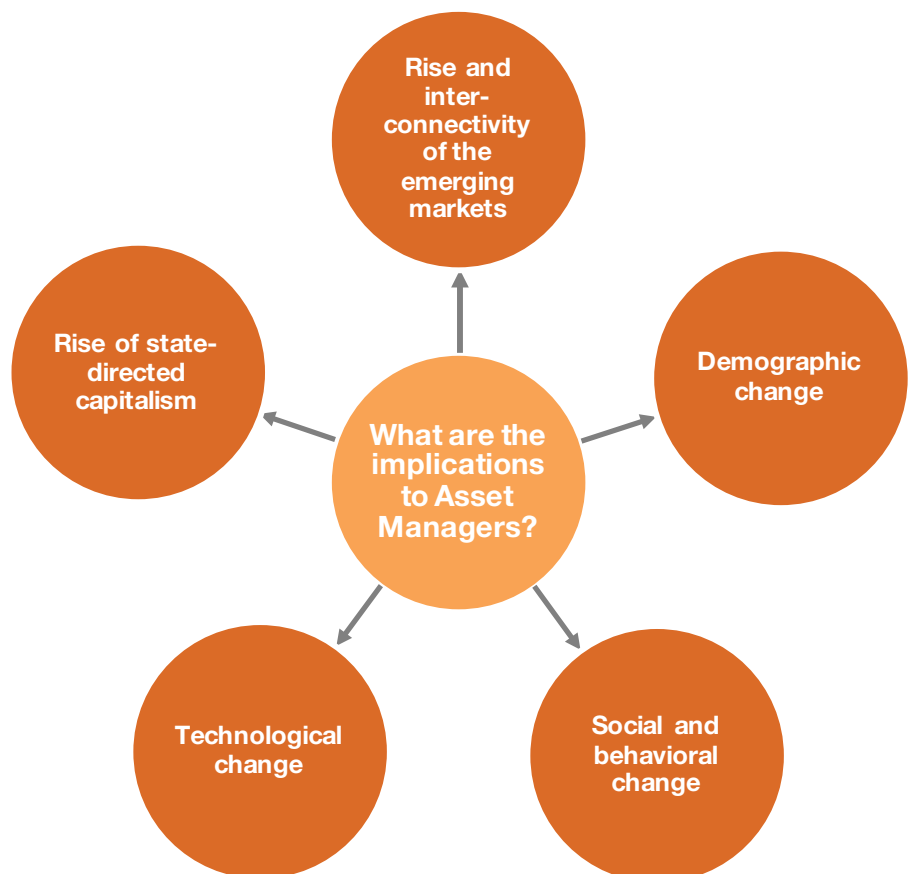
In addition, **new competition may arise from non-traditional sources** (e.g., technology companies providing comparison and distribution of asset management products) who will serve as an arbiter of investment prowess.

Investments in infrastructure and real estate, as well as engaging in Public-Private Partnerships, present opportunities for growth, especially in emerging markets and urban areas. **Recruiting and developing top talent with emerging market experience will be a competitive differentiator.**

Finally, continued **scrutiny by both clients and regulators**, along with demands for additional legislation, accountability, transparency, and low-cost solutions **will continue to challenge the environment** in which asset managers operate.

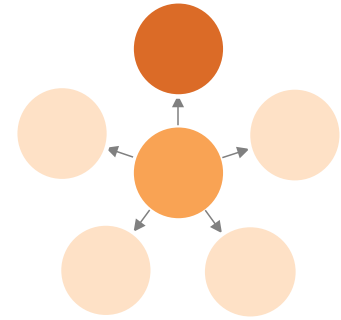
Macro trends

The future will not repeat the past. Five macro trends present both an opportunity and a necessity for business change in the longer term and asset managers must be agile.



Rise and interconnectivity of the emerging markets

The rising wealth and economic progression in South America, Africa, Asia and the Middle East are forcing a greater focus on these regions for global expansion.



Key implications for Asset Managers

Products

- Investment strategies and product offerings should be tailored to local investor needs.
- While products should be global in most instances, they must be accepted in local regions.
- Investments in real estate, as well as other commodities, present opportunities for growth.

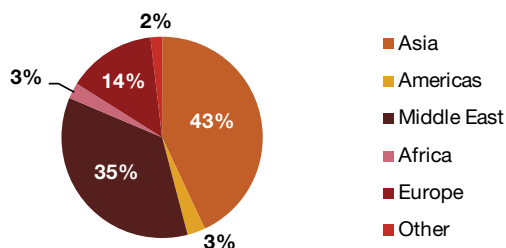
Customer/distribution

- Local expertise and market intelligence are imperative to better understand the region, investor needs, and geopolitical issues.
- Strong brand development and regional marketing are essential to attract assets.
- There are increasing regulatory barriers for foreign institutions; partnering with local distributors or evaluating joint ventures may prove helpful, however local country limits still exist.

Operations

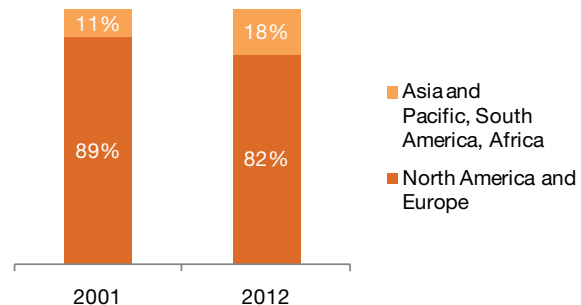
- Multi-hub organizational structures ensure focus on growth and profitable markets.
- Organizations must be able to adapt to a rapid pace of change and handle volatile growth.
- Restructuring service models, including assessing cultural fit, is critical.

Sovereign Wealth Fund assets by region
March 2013



Sources: www.swfinstitute.org, PwC analysis

Percent of registered fund assets by region*

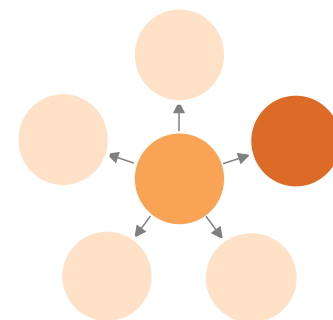


Sources: Investment Company Institute, European Fund and Asset Management Association, and other national mutual fund associations

* Registered assets include mutual funds, UCITS, and funds registered in other jurisdictions. The population of countries that reported assets in 2001 is not identical to the population of countries that reported assets in 2012.

Demographic change

The emerging middle class in some regions, and the aging populations in others, is leading to shifts in investor behavior, demands for greater product diversity, and changes in pension models.



Key implications for Asset Managers

Products

- There is a need to establish retirement systems in emerging and frontier markets. Products that achieve long-term wealth accumulation to cater to state-directed schemes and pension funds will gain traction.
- Demand for capital preservation and income distribution products in regions with aging populations will continue to increase.
- The growing aging population is creating opportunities for products aimed at funding healthcare and infrastructure to support aging communities.

Customer/distribution

- Service and distribution models need to be re-evaluated for cultural fit and to accommodate investor objectives as firms expand into new geographies.
- Retirement systems are underfunded worldwide. There is a need for customer outreach to cultivate relationships, increase education, and better satisfy retirement needs.

Operations

- Organizations and business models will need to be modified to service both the middle class and aging populations; each requires a different approach.
- The creation or expansion of dedicated pension teams to service growing pension assets may prove essential.

Forecast size of the middle class by region, millions

Region	2009	2030	% Growth
Asia-Pacific	525	3,228	514.9%
Sub-Saharan Africa	32	107	234.4%
Middle East & North Africa	105	234	122.9%
Central & South America	181	313	72.9%
Europe	664	680	2.4%
North America	338	322	-4.7%
Total	1,845	4,884	164.7%

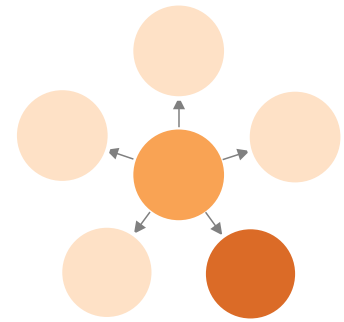
Source: Based on data from table 2 'Numbers (millions) and Share (percent) of the Global Middle Class' from Kharas, H. (2010), "The Emerging Middle Class in Developing Countries", OECD Development Centre Working Papers, No. 285, OECD Publishing.

The old-age dependency ratio for the world is forecasted to reach 25.4% in 2050, up from 11.7% in 2010

Source: "Old-age dependency ratios", The Economist, 9 May 2009. Measures the number of elderly people (65+) as a share of those of working age (15-64).

Social and behavioral change

Investors are becoming more informed, empowered, and demanding, while increasing urbanization is transforming the needs of individuals and communities around the world.



Key implications for Asset Managers

Products

- Product visibility with both regulators and investors worldwide has dramatically increased.
- Investment in urban infrastructure will be a growth market; urbanization increases the stress on physical and service infrastructure which creates demand for investment through private equity, real estate and infrastructure funds, as well as Public-Private Partnerships.

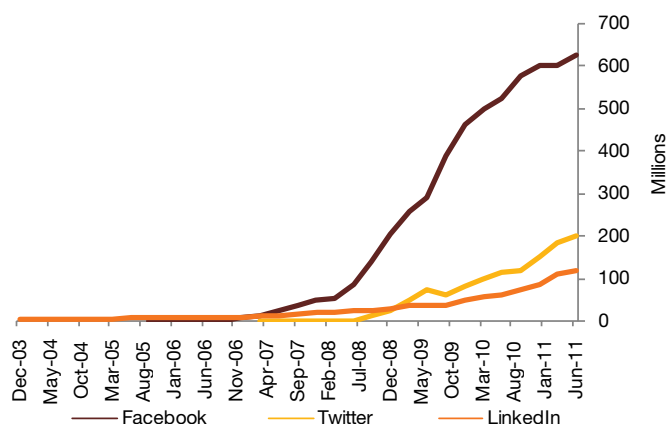
Customer/distribution

- Social technologies make firms global; they provide direct access to existing and potential clients and eliminate the middle man.
- Increasing urbanization is creating new markets for asset managers; a focus on distribution on a city-by-city level (as opposed to taking a regional view) may be beneficial.

Operations

- New resources may be required to respond to the quantity and speed of information received as well as to support increased investment opportunities in urban infrastructure.
- Customer relationship management and a renewed focus on brand management are critical.
- Local talent and operations may prove advantageous to support growing cities.

Evolution of registered users



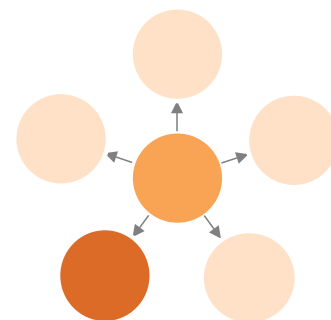
Source: Search Engine Journal

The world urban population is expected to increase by 72% by 2050, from 3.6 billion in 2011 to 6.3 billion in 2050

Source: United Nations, Department of Economic and Social Affairs, Population Division (2012). World Urbanization Prospects: The 2011 Revision.

Technological change

Mobile and internet platforms are increasingly used to research and purchase financial products; technology advances, coupled with big data, are creating new and profitable growth opportunities.



Key implications for Asset Managers

Products

- Customer experience will be as much a part of the product as the investor strategy. The timeliness, ease of access, and quality of information available is critical.
- New enhanced beta product offerings, using different formulas, indicators, and weightings, will be introduced.

Customer/distribution

- Mobile and internet distribution channels will continue to increase in importance as a result of ongoing growth in technology adoption worldwide.
- There is a significant amount of unstructured data available through social media and online platforms; technology advancements to analyze this data, as well as to make informed decisions, will lead to new business models.

Operations

- The importance of IT infrastructure and security continues to increase. Outsourcing non-core operations or partnering with technology firms will be of interest.
- Cloud computing can significantly reduce fixed technology costs although security concerns remain.
- More sophisticated trading as a result of technological advances may increase the volatility of markets.

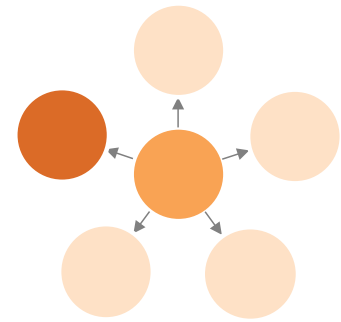
World internet usage and population statistics

World regions	Internet users June 2012 (millions)	Penetration (% of population)	Growth (Dec 2000 - Jun 2012)	Users % of table
Africa	167	15.6%	3606.7%	7.0%
Middle East	90	40.2%	2639.9%	3.7%
Latin America/Caribbean	255	42.9%	1310.8%	10.6%
Asia	1,077	27.5%	841.9%	44.8%
Europe	519	63.2%	393.4%	21.5%
Oceania/Australia	24	67.6%	218.7%	1.0%
North America	274	78.6%	153.3%	11.4%
Total	2,406	34.3%	566.4%	100%

Source: www.internetworldstats.com

Rise of state directed capitalism

While increased regulation and protectionist policies require focus, the increasing number and size of Sovereign Wealth Funds (“SWFs”) and opportunities for Public-Private Partnerships present massive growth prospects.



Key implications for Asset Managers

Products

- Stronger investor protection and transparency demands may limit product innovation and flexibility.
- SWF products must be tailor-made and risk levels, as well as investment policies, need to be adapted to the objectives and regulatory requirements of the state.
- Public-Private Partnerships will be increasingly important to the future of infrastructure investment.

Customer/distribution

- An increase in regulation and protectionism policies will have the potential to limit capital flow and increase cost (e.g., breakup of financial conglomerates will alter distribution channels).
- Governments and policy makers will be treated as clients as their involvement in the industry increases.
- Establishing a local presence or joint venture in new markets may be advantageous as some governments will look first to local or regional firms.

Operations

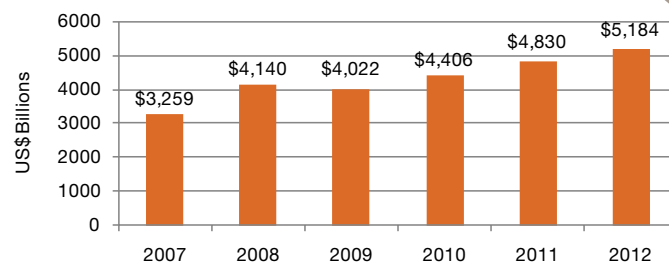
- The volume of new regulatory bodies and rules will continue to cause significant compliance and cost challenges.
- SWFs and Public-Private Partnerships have different service requirements (e.g., increased interaction with policy makers, increased specialization) and will require dedicated teams.

Private participation in infrastructure projects increased from US\$19 billion in 2002 to US\$106 billion in 2011

Source: The World Bank: Private Participation in Infrastructure Projects Database

Note: Data gathered from low- and middle-income countries in East Asia and Pacific, Europe and Central Asia, Latin America and the Caribbean, Middle East and North Africa, South Asia, and Sub-Saharan Africa. Includes projects in the energy, telecommunications, transport, and water and sewerage sectors.

Sovereign wealth fund market size



Source: www.swfinstitute.org

59% growth from 2007 to 2012

What questions should executives be asking?

Rise and interconnectivity of the emerging markets

- Does our footprint reflect the markets we should be focusing on for growth over the next several years? How do we resource this growth from an intellectual and administrative perspective? How do we fund it?

Demographic change

- Does our customer focus reflect where growth is in the market? How will we capture increasing retirement assets across the globe?
- How are customers shifting in terms of their investment behaviors and needs? What products need to be developed in an environment where investment philosophies and styles are changing?

Social and behavioral change

- What investor demands related to information transparency and service capability do we need to prepare for?
- Do we have a presence in expanding urban areas? Are we capable of properly operating from a social, cultural and regulatory perspective in these cities?

Technological change

- How will we leverage technology to differentiate and drive sustainable competitive advantage and cost efficiency while conforming to local, regional and global regulations?

Rise of state directed capitalism

- Are we competitively positioned to penetrate the growth in Sovereign Wealth Funds, engage in Public-Private Partnership opportunities, and invest in urban infrastructure? What business and operating model capabilities are needed to serve this emerging customer base?
- Are we engaged with government and public influencers to manage protectionist tendencies?

Understanding the implications of these macro trends is critical to a firm's future success. Further exploration and discussion of what lies ahead will help a firm identify opportunities to adapt its strategies and take advantage of new and emerging industry demands.

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