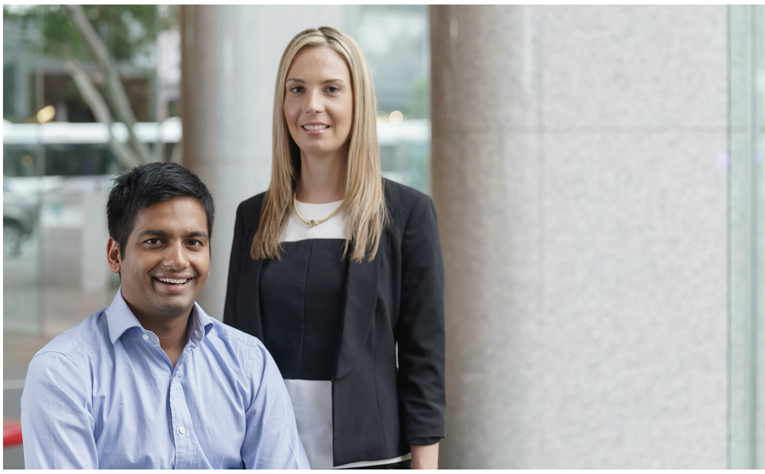
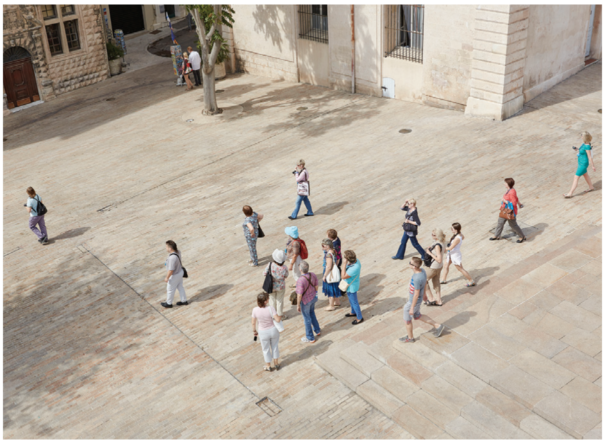
19th Annual Global CEO Survey/February 2016

Key findings in the asset management industry

Redefining business success in a changing world





90% *of CEOs are confident about business growth in 2016*

25% *see global economic growth rates declining over 12 months*

66% *foresee a time when success is about more than profit*

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About the 19th Annual Global CEO Survey

In this year's survey, global business leaders voice fresh concerns about economic and business growth. At the same time, they see a more divergent and multi-polar world where technology is transforming the expectations of customers and other stakeholders. In Redefining business success in a changing world, we explore how CEOs are addressing these challenges. We surveyed 1,409 CEOs in 45 countries and a range of industries in the last quarter of 2015, and conducted face-to-face interviews with 33 CEOs.

Today's business leaders have a tough job finding growth and delivering results year in, year out. But they know an even tougher task lies ahead: to prepare their organisations for a more complex future where customers and other stakeholders increasingly expect them to do more to tackle society's important problems.

To equip themselves for this challenge – and to build trust and ensure long-term success – CEOs are focusing on three core capabilities. Firstly, they're focusing even more strongly on customer needs as well as drawing on their organisational purpose – what their companies stand for – to define a more comprehensive view of how their business operates within society. Secondly, they're harnessing technology, innovation and talent to execute strategies that meet greater expectations. And finally they're developing better ways to measure and communicate business success.

Key findings in asset management

This report is a summary of our survey findings in the asset management sector, based on the answers from 189 asset management CEOs in 45 countries. To see the full results of the 19th Annual Global Survey, please visit www.pwc.com/ceosurvey.

Introduction

Volatile markets have shaken asset management CEOs' confidence in economic growth. Yet in spite of this they remain confident about the outlook for their businesses. Our survey reveals a high level of optimism, which CEOs go on to illustrate in a series of fascinating interviews. They're on the right side of a number of powerful trends. Retirement patterns across the US, Europe and Asia for example are leading to enormous opportunities, as are the opening up of new geographical markets and products that might disrupt banking.

At the same time, CEOs have to deal with a far more complicated world, with new measures of success and wider sets of stakeholders. They're beginning to redefine their purpose beyond the narrow pursuit of profit and to communicate with more stakeholders.

"Asset managers are aggressively moving forward with growth. But they're also adapting their business models to deal with the challenges presented by mega trends, new regulations and stakeholder demands."

Barry Benjamin
PwC's Global Asset Management Leader

Robust confidence in growth, despite volatile markets

Uncertainty is rising and even asset management companies can't escape this reality entirely. Just 30% of asset management CEOs expected the global economic growth rate to improve over the next 12 months when surveyed in late 2015, against 25% anticipating a decline. In the previous year's survey they were more bullish – a higher 39% foresaw an improvement, with just 15% anticipating a decline. Clearly the economic picture is darkening. What's more, as CEOs were surveyed before China's slowing economy sparked a rout in global equity markets, this high level of doubt may have risen since.

In addition to the economy, a whole host of other hazards are preying on CEOs' minds. These include over-regulation, geopolitical uncertainty, exchange rate volatility, governments' reactions to fiscal deficits and interest rate rises. There's a sense that the number of challenges is rising.

Yet, remarkably, asset managers' confidence in their prospects is unshaken. There's considerable optimism about growth in underlying assets. The vast majority of CEOs, 90%, are confident or very confident about revenue growth in 2016, with this majority becoming even greater, at 95%, over three years. This level is similar to 2015's result. By contrast, a lower 82% of CEOs from across industry sectors expressed this degree of confidence for 2016, rising to 92% over three years.

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Explains Peter Kraus, Chairman and CEO, AllianceBernstein: "Volatility doesn't necessarily impact us positively or negatively. What impacts our businesses is taking advantage of specific opportunities that investors are looking for. For example, big opportunities are created as China unveils its currency and becomes a more open marketplace. Retirement trends in the US, Europe, and Asia present interesting opportunities for investors. As interest rates change, so does investors' demand for income and risk. And completely new markets emerge."

As foretold in our *Asset Management 2020 paper*, robust long-term trends are driving growth in the asset management sector. In particular, ageing populations need to save more money for retirement, while new middle classes in the developing world must also save more. Testifying to their faith in this expansion, 65% of the sector's CEOs plan to hire more people in 2016, compared with 61% in 2015.

Yet they're mindful of the volatility in financial markets and the range of other challenges. CEOs are pretty evenly balanced on whether this means the outlook is brighter compared with three years ago – with 63% seeing more opportunity and 56% believing there are more threats.

As is often the case in uncertain times, CEOs have turned to their traditional markets for growth, with some appearing to shelve plans to expand in China. 39% view the US as the most important market outside their country of origin in 2016, with 23% looking to Germany and 13% to the UK. China still ranks second to the US – but only just. While 24% still see China as the most important market for them, this is far lower than 31% in 2014, a level the country had held for several years. Hopes for a surge in business from China's newly affluent middle classes are likely postponed by the economy's mounting problems.

In spite of today's volatility and uncertainty, we see large asset management firms positioning themselves for exceptional growth as they move centre stage in finance, assuming some of the roles previously performed by banks. 58% of CEOs are planning to enter into strategic alliances or joint ventures over the next 12 months. But with such market volatility, they're also keeping an eye on cost in our experience. "A lot of organisations are chasing new opportunities," says PwC's Benjamin. "Private equity managers and sovereign wealth funds are investing in the sector, while firms use alliances and even acquisitions to build the new product expertise they need."

"I think the challenge for all of us in business now is just the complexity of the markets in which we operate. The competition is more diverse. There are lots of different technologies out there. Political interference has increased. There is greater trade uncertainty, and there is greater uncertainty across the whole of Europe because we're not sure of the outcome."

Dr Nigel Wilson
CEO, Legal & General

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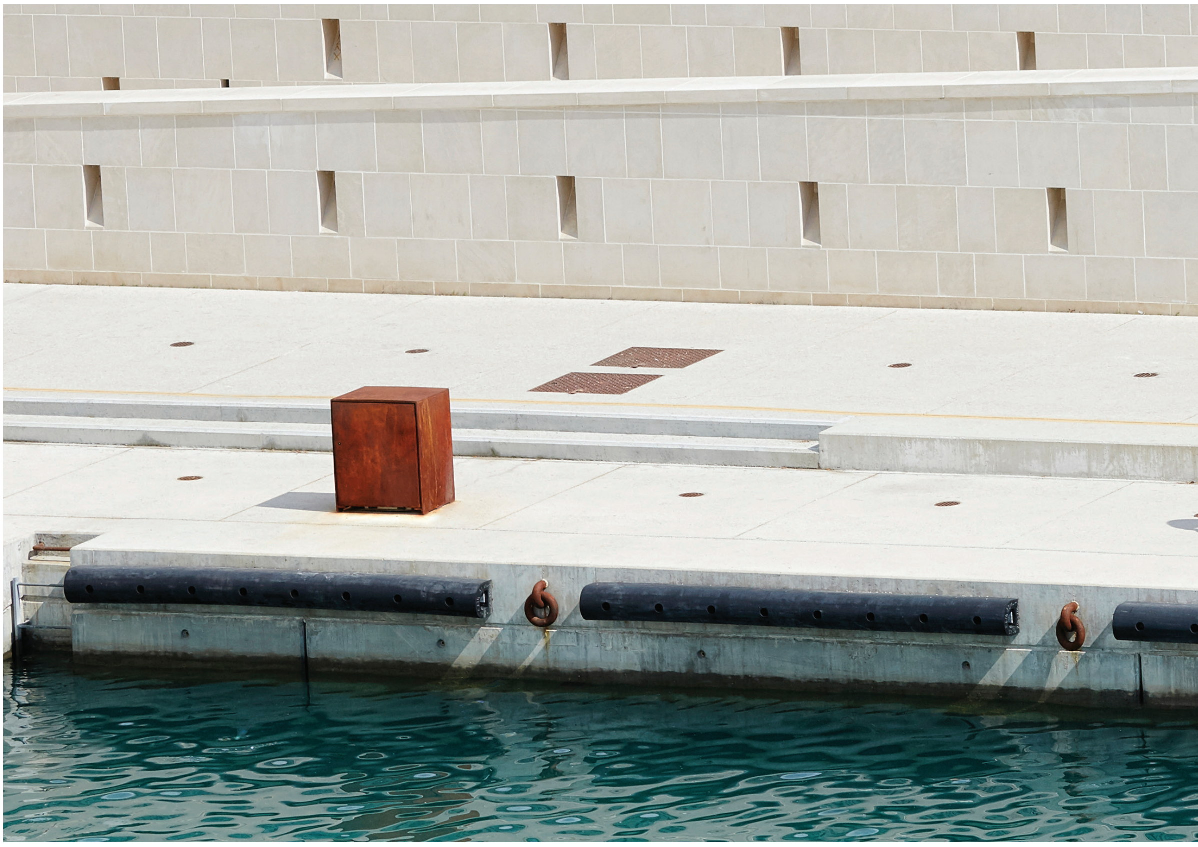

69%

of CEOs identify the shortage of skills, as is natural in a sector that's as heavily dependent on the ability of a few talented people as a team of athletes.

Our CEOs echo this sentiment. Legal & General's Wilson explains: "If we don't get into the voids that are being created and the opportunities being created, there are many other new participants who will come in there. There are some really smart people in private equity that are entering our industry. There are lots of smart but currently very small 'fintech' companies. We will see new competition from China and Japan that we've never seen before, and we'll potentially see firms from Africa, where they've really been very successful at adopting and adapting mobile technology and where they've leapfrogged the European model and moved to a new model. So, if we don't step up others are going to step in, and we're already seeing the beginnings of that happening at the moment."

Eyeing emerging challenges

But in order to grow, CEOs must constantly adapt the firms they lead, tackling a range of challenges. In terms of specific potential issues, 69% of CEOs identify the shortage of skills, as is natural in a sector that's as heavily dependent on the ability of a few talented people as a team of athletes.

Hamid Moghadam, Chairman and CEO, Prologis says: "We're a company with almost $60 billion of real estate assets in 20 countries around the world, yet we only employ about 1,500 people. That means each employee is responsible for an average of $40 million of real estate assets. That makes us a pretty unusual place to work. That's why people are so important in our business.

"We place high demands on our employees. We are careful about our talent level, how we recruit, and how we develop talent. It's almost a cliché to say that, but it makes a huge difference in our business. We are not an IP heavy business. Real estate is one of the oldest industries in the world, but execution is really important. People are the only thing that matter at the end of the day."

Other challenges that more than half of sector CEOs identify as a threat to growth are stock market volatility (61%), cyber security (60%), speed of technological change (61%) and shifting consumer behaviours (61%).

There are grounds for wondering whether asset managers worry enough about some of these hazards. Are they anxious enough about cyber security, disruptive technology and the changing consumer? Significantly more banking CEOs are concerned about these threats. Perhaps the difference can be explained by the fact that a large number of asset managers only have institutional clients.

Towards a multi-polar world

This picture of gathering uncertainty isn't just being shaped by economic and geopolitical trends. We believe there's a fundamental shift taking place, namely from a globalising world to one with many dimensions of power, growth and threats – a transition that we call multi-polar.

Asset managers are keen observers of the trend. More than half of asset management CEOs, 58%, anticipate multiple economic models, while 52% see a rise of nationalism and devolved nations, 76% see multiple rules of law and liberties, and 81% multiple beliefs and value systems.

Such diffusion has practical consequences, creating barriers to fund distribution. In time, however, we believe that four regional distribution blocks could develop, namely: North Asia, South Asia, Latin America and Europe.

The tectonic plates in the balance of political, economic and social power are shifting, changing the existing order. Long used to economic risk being predominant, asset managers now have to judge politics other factors too when managing portfolios and planning business growth.

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Hamid Moghadam
Chairman and CEO, Prologis

Addressing a wider range of stakeholder expectations

Asset management companies have traditionally had a narrow focus on stakeholders – customers regulators and shareholders' interests have come first. Raw investment performance has determined whether firms flourish or fail. Yet there are early signs that this might be changing, with almost a quarter (24%) of CEOs saying they've changed their organisation's purpose in the past three years to take account of the broader impact they have on society.

33%

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For context, just a third of asset management CEOs, 33%, say that they have always had an organisational purpose that includes the broader impact on society. A far higher proportion of CEOs from other sectors – 41% for financial services generally and 45% across all sectors – report always aiming to have a broad impact on society. Many of the asset management firms in our survey are small boutiques, so it's natural that they wouldn't pay so much attention to purpose as larger organisations.

But most asset management CEOs think that 'responsibility' will play an important part in defining their success in five years' time. Most significantly, 86% say they will prioritise long-term over short-term profitability. Furthermore, 69% think they will report on both financial and non-financial matters, while 68% anticipate corporate responsibility being core to everything they do. Perhaps with an eye to providing more direct lending products, 62% think their purpose will centre on creating wider value for stakeholders.

David Booth, Chairman and co-CEO, Dimensional Fund Advisors, says: "As I've gotten older, my view of success has changed. Early on, I thought it was all about the rate of return or maybe the rate of return relative to volatility. That's clearly still very important.

"But I think that success is also measured another way – did clients have a good experience? For sure, that includes good returns. But were we able to do that and feel good throughout? If you can do both, then you have a good experience. That's what success is about – getting good returns and achieving them in a way that enables people to relax just a little bit more."

What's already true is that environmental, social and governance is a term creeping into the industry's lexicon. Big European investors, with nearly €13trn in assets between them, formed the Institutional Investors Group on Climate Change at the 2015 COP21 Paris climate change conference. From a fiduciary perspective, it's becoming accepted that investors need to take into account climate change risks.

Competitive pay remains important

When it comes to attracting top talent, however, many asset management CEOs still believe that the best fund managers will continue to be motivated primarily by hard cash. Almost half, 48%, believe that in five years top talent will continue to want to work for firms providing competitive compensation, against 49% that think shared social values will be more important.

€13trn

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By comparison, 60% of financial services CEOs and 67% of the CEOs across the survey put shared social values first. This reflects the comparatively high pay received by asset managers.

"One slant on this finding is that the sector has produced some of the world's leading philanthropists," says PwC's Benjamin. "So while asset managers might be motivated by money in their professional life, privately they're often passionate about charitable causes."

Reviewing risk management, marketing and technology to remain competitive

The rising tide of regulation, investor scrutiny and enabling technology make this a time of fundamental change for asset management. They're altering what it takes to be competitive. CEOs are not standing still. The survey tells us they're adapting and retooling their businesses.

Almost all CEOs, 92%, are responding to changing stakeholder expectations by looking at how they define and manage risks. In the past, they tended to look only at investment risk. This remains critical; indeed there's a continual reassessment of the best ways to express and manage it. Yet operational risk management has also become a success factor. When conducting due diligence on a new manager, institutional investors such as pension funds probe risk management. Only industrial strength practices will do.

Within marketing departments there's a revolution under way. Are traditional approaches to the brand and PR dead? Some 89% of CEOs say changes in stakeholders' expectations mean they're reviewing how they manage brand, marketing and communications. In our experience, they're refocusing the brand on investor outcomes while reorienting communication towards digital and social media. Content marketing is beginning to have concrete results for the firms pioneering this.

When it comes to technology, asset managers have an opportunity to learn from the ecommerce firms such as Amazon that have harnessed 'big data' so successfully. Some 85% are examining how they use technology so that they can improve the stakeholder experience. Doing so may give insights into clients' shifting product needs, as well as how they're likely to react to different conditions in financial markets.

Finally, 85% of CEOs are looking to respond to shifting stakeholder expectations by reviewing whom they partner with and how they manage these partnerships. As mentioned earlier in this report, asset managers are seeking to fill product gaps as they move to the centre of finance's ecosystem. Partnerships and other alliances are important ways of filling these gaps.

Changing behaviour

When it comes to people, asset management CEOs appear to be focusing on changing behaviours, making remuneration dependent on a wider range of factors than individual contribution to profit.

Asked what aspects of their talent strategy they're changing to make the greatest impact on attracting, retaining and motivating talent, asset management CEOs focused mainly on remuneration. Some 44% of CEOs are making changes to pay, incentives and benefits, with 43% reviewing performance management.

There's little evidence of asset managers seeking the wider skill sets, from more diverse backgrounds, they might need for leveraging social media or big data. Just 16% of CEOs report changing their approach to diversity and inclusion, which would help them to recruit from a wider pool of people, giving them a better chance of finding the right specialists. For comparison, 22% of CEOs across sectors are doing this.

Technology and customer engagement

Technology has the potential to transform engagement with customers in the eyes of CEOs. In a clear sign of change, 64% of CEOs believe that data and analytics are the most effective means for engaging stakeholders, while 52% favour social media communication and engagement indicating that the sector is embracing digital content marketing. Some 58% still think CRM systems are effective.

Firms are also deploying technology to improve online collaboration with their investors. some 43% think web-enabled collaboration tools are effective whilst 42% view investor relationship tools as as a technology capable of generating a high level of return.

Kraus explains how AllianceBernstein is seeking to develop its own disruptive technologies: "Sometimes innovation occurs without any deliberate structure and sometimes within a structure. There is no best way to do it. Recently a group of people in our organization came to me and said they had a way to capture ideas effectively within AB – a crowdsourcing approach to capture innovative ideas and look at them in depth and possibly invest in them.

"Today we call it "AB Labs." It's been very successful. People throughout the organization have contributed ideas. It has enabled us to get inside buy in, which is critical to disruptive ideas."

Nimble organisations

While CEOs in other sectors seem concerned about the barriers to making the changes needed to remain competitive, asset management firms are less so. Their relatively small size and entrepreneurial nature makes them more able to move quickly.

Asset management CEOs do see roadblocks, but they tend to anticipate fewer than their peers elsewhere in financial services. For example, 42% of asset management CEOs view additional costs to doing business as an obstacle. Yet 57% of bank CEOs and 48% of insurance CEOs see additional costs as a burden.

Other significant roadblocks for asset managers include unclear or inconsistent regulation, according to 35% of CEOs, and conflicts between stakeholder interests and financial performance expectations according to 37%.

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Measuring and communicating success

With value drivers changing, and stakeholder expectations evolving, CEOs believe they should be adapting how they measure and communicate success.

52%

think they should be doing more to communicate organisational purpose and values

47%

prioritise non-financial issues such as the brand.

They see the business's success as dependent on a range of factors. Most significantly, 61% believe they should be doing more to measure the impact and value of key risks. But there's also a trend towards measuring impact and value in a range of areas such as: innovation (51%), business strategy (48%), employee practices (44%) and non-financial indicators such as brand (42%).

Legal & General's Wilson explains: "I think by the use of technology we can have much richer measures of success, particularly around customers and around other stakeholders because we can get much more feedback on those."

When it comes to communicating, however, they appear to be planning to talk to both the head and the heart of the 'Millennial' generation. More than half, 52%, think they should be doing more to communicate organisational purpose and values, while 47% prioritise non-financial issues such as the brand.

They also think they should be doing more to talk about innovation (47%) and business strategy (50%).

CEOs believe that regulators will be most influential in making them communicate more on the environment and key risks. However, they see customers as making them say more about non-financial indicators and innovation.

Conclusion

Looking forward to the rest of the 21st century, asset management CEOs anticipate a time when success will be defined by more than just profit. Two thirds see this day coming. While a significantly larger three quarters (76%) of CEOs from across all sectors foresee this eventuality, two thirds is still a high number.

"Asset management is going through a time of fundamental change. This is a time of great opportunity for growth, yet asset managers need to become more innovative, leverage technology, manage a wider range of risks and use digital communication intelligently if they're to remain competitive. In ten years time our sector is likely to be far bigger, but asset management companies will look very different from today."

Barry Benjamin
PwC's Global Asset Management Leader

Contacts

If you would like to discuss the issues raised in more detail, please contact me.

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