

# *Asset & Wealth Management Insights*

## Asset Management 2020: Taking stock

*Special Edition*

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## Asset Management 2020: Taking stock

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*Three years ago, we predicted that the asset management industry was on the precipice of several fundamental shifts that would shape its future. Our paper, Asset Management 2020: A Brave New World, predicted a huge rise in assets and the emergence of several game changers that would dramatically alter the industry's landscape.*

At the time, asset managers were still distracted by the economic turmoil and regulatory change that followed the Great Financial Crisis, which spanned 2008-2009. The paper laid out trends and drivers to help asset managers plan for the future by anticipating changes in the competitive environment.

Fast forward to today and our projections for an increase in assets under management (AuM) are proving broadly correct, although slightly pessimistic. At the time, we forecast worldwide AuM would rise from US\$63.9 trillion to US\$101.7 trillion by 2020,<sup>1</sup> a compound growth rate of nearly 6%. In fact, growth in AuM is running ahead of our original forecasts, leading us to raise our 2020 AuM forecast to US\$111.2 trillion.<sup>2</sup>

Turning to the game changers, the pace of change in the asset and wealth management (AWM) industry is accelerating, and following a path of creative destruction. The environment and game changers that we described in Asset Management 2020 are evolving. Ahead of publishing a full paper in the autumn, we review our earlier predictions in the following pages.



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<sup>1</sup> We define worldwide AuM as assets managed by asset and wealth managers globally.

<sup>2</sup> PwC Global Market Research Centre.



## *The landscape in 2020*







## The industry expands, the investor base morphs

### Huge rise in assets and shift in investor base

Just as outlined in the original paper, changing markets and investor needs have combined to produce a positive environment and huge opportunities for AWM players. The rise in value of investable assets over the last two to three decades has been driven by increasing financialisation across major economies, ageing of OECD market populations and the shift towards funded / defined contribution plans, disintermediation of commercial banks as regulators have constrained their growth, and imbalances in trade-driven flows and financial savings versus local investment needs across major markets. This is continuing and assets

are expected to be significantly larger by 2020 than today. The increased headline figure of US\$111.2 trillion (up from our earlier forecast of US\$101.7 trillion), compares with US\$78.7 trillion at the end of 2015.<sup>3</sup>

What's changed? Both a faster rise to date in high net worth individuals' (HNWIs') assets, causing us to increase our forecast for total clients' assets from US\$277.8 trillion to US\$283.4 trillion,<sup>4</sup> and the sector's growing ability to capture those assets. We now anticipate the sector will manage 39.2% of them by 2020, up from our original forecast of 36.6% (see table below).<sup>5</sup>

*The rise in value of investable assets that has occurred over the last two to three decades is continuing and they're expected to be significantly larger by 2020 than today.*

Clients	2004	2007	2012	2013	2014	2015	2020*	2020 (new)
Pension funds	21.3	29.4	33.9	35.8	38.7	38.2	56.5	55.8
Insurance companies	17.7	21.2	24.1	26.1	26.2	27.1	35.1	38.8
Sovereign wealth funds	1.9	3.3	5.3	6.1	6.3	6.7	8.9	10.0
HNWI	37.9	50.1	52.4	59.2	69.6	67.8	76.9	83.5
Mass affluent	42.1	55.8	59.5	64.2	67.2	62.5	100.4	96.3
<b>Total client assets</b>	<b>120.9</b>	<b>159.8</b>	<b>175.2</b>	<b>191.4</b>	<b>208</b>	<b>202.3</b>	<b>277.8</b>	<b>284.4</b>
<b>Global AuM</b>	<b>37.3</b>	<b>59.4</b>	<b>63.9</b>	<b>71.9</b>	<b>78.0</b>	<b>78.7</b>	<b>101.7</b>	<b>112.0</b>
<b>Penetration rate</b>	<b>30.9%</b>	<b>37.2%</b>	<b>36.5%</b>	<b>37.6%</b>	<b>37.5%</b>	<b>38.9%</b>	<b>36.6%</b>	<b>39.4%</b>

Sources: PwC Market research centre analysis. Past data based on City UK, Insurance Europe, Financial Stability Board (FSB), Credit Suisse, Towers Watson, OECD and World Bank.

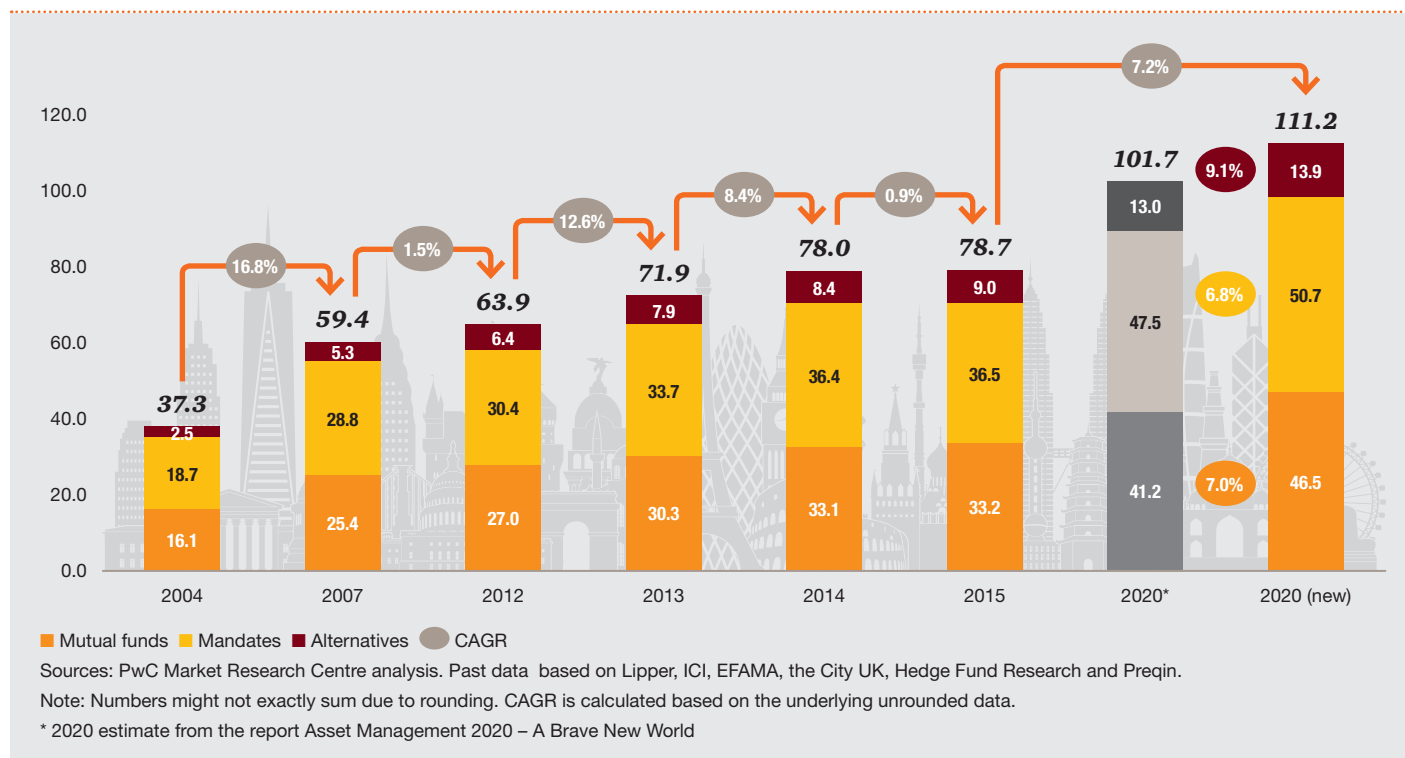
\* 2020 estimate from the report Asset Management 2020 – A Brave New World

<sup>3</sup> PwC Global Market Research Centre.

<sup>4</sup> We define total client assets as investable assets from pension funds, insurance companies, sovereign wealth funds, high net worth individuals and the mass affluent.

<sup>5</sup> PwC Global Market Research Centre.

Global AuM projection by region in USD trillion



### ***The rising importance of South America, Asia, Africa, Middle East (SAAAME)***

Our prediction that AuM in the SAAAME countries would grow faster than those in the developed world in the years to 2020 remains. This is beginning to create new pools of assets that can be tapped by the AWM industry. However, most assets will continue to be in the US and Europe – the global distribution of wealth is changing more slowly than the global distribution of nominal (or purchasing power parity) income.

### ***Growth will be driven by pension funds, insurance companies, mass affluent and HNWIs***

The increasing personal wealth of the mass affluent and HNWIs, coupled with increases in wealth overseen by pension funds and insurance vehicles,

will continue to drive the worldwide expansion in AuM. However, the industry is proving more successful than we originally thought at capturing the assets of HNWIs – many of them in emerging markets. For this reason, we project that total HNWI assets managed in 2020 will be US\$88.6 trillion, rather than the US\$76.9 trillion originally anticipated. This compares with just US\$67.8 trillion in 2015.<sup>6</sup> The single greatest contributor to the surge in mass affluent and HNWI assets remains the increase in SAAAME wealth.

Pension fund assets managed will grow from US\$38.2 trillion in 2015 to US\$56.1 trillion by 2020 (a little lower than our original US\$56.5 trillion projection),<sup>7</sup> lifted mainly by the growth of defined contribution schemes. Both developed and developing countries are seeking to bring more of their labour forces under the umbrella of funded defined contribution retirement plans.

<sup>6</sup> PwC Global Market Research Centre.

<sup>7</sup> PwC Global Market Research Centre.

## Pressures on the industry

The pressures on AWMs (Asset and Wealth Managers) are changing and intensifying. Since the publication of *Asset Management 2020* in 2014, profit margins have been squeezed. Notably, the greater transparency in the wealth management advice model started by the UK's Retail Distribution Review (RDR) and similar regulations, a shift to outcome-based solutions and the expanding market share of passive strategies, are putting relentless downward pressure on fee levels and asset flows, which are skewed towards lower margin products. This is happening at a time when firms must invest in building outcome-based solutions and applying transformational technologies, both internally and externally.

Determined to gain scale, several international asset managers have announced mergers within the past 12 months, including Janus Capital Group

and Henderson Group,<sup>8</sup> Standard Life and Aberdeen Asset Management,<sup>9</sup> and Amundi's acquisition of Pioneer Investments.<sup>10</sup>

Broadly speaking, these mergers are intended to reduce costs as overlapping funds are closed, distribution reach is leveraged and the fixed cost base is spread across greater scale. Additionally, some asset managers, mainly in Europe, have been acquiring wealth managers as they seek to control distribution and the customer relationship. This also gives the appearance of alleviating near-term margin pressure as wealth managers' share of fees appears less vulnerable to the pressures described above, but may not be a long-term solution as regulation increasingly focuses on open-architecture distribution and pushes wealth managers towards greater disclosure and a fiduciary standard of care.

*Determined to gain scale, several international asset managers have announced mergers within the past 12 months*

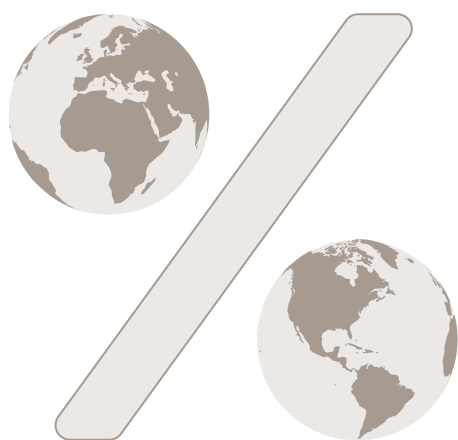


<sup>8</sup> Janus Capital Group Inc. and Henderson Group plc. announce recommended merger of equals; [ir.janus.com](http://ir.janus.com); 3 October 2016.

<sup>9</sup> Statement regarding the potential merger of Standard Life plc and Aberdeen Asset Management plc; [standardlife.com](http://standardlife.com); 4 March 2017.

<sup>10</sup> Project of acquisition of Pioneer Investments; [about.amundi.com](http://about.amundi.com); 12 December 2016.

## Nothing to hide, nowhere to hide and nothing at risk



*In short, the global tax system is broken. As tax information becomes publicly available, and strong populist sentiment continues, so the public will judge whether companies are paying their 'fair share' of taxes in an emotionally charged environment.*

The drive to improve transparency continues unabated. Regulation, investor pressure and tax legislation are all driving more openness. In addition to creating a more fee competitive market, this is also leading to greater costs related to data and reporting.

Since 2014, there has been little newly planned legislation but what was already planned has led to significant investment in systems. In Europe, recent legislation includes the European Market Infrastructure Regulation, Packaged Retail Investment Products, Markets in Financial Instruments Directive I and II, as well as the Alternative Investment Fund Managers Directive, RDR and Undertakings for Collective Investments in Transferable Securities V, VI and VII.

In the US, there have been the Dodd-Frank related amendments to the Investment Advisors Act and two significant new regulatory developments – the Department of Labor's Fiduciary Rule (with implementation dates

currently set for June 2017 and January 2018), and the SEC Liquidity Risk Management Rule (with milestone dates currently set for December 2018 and June 2019). The new US administration has committed to grant some relief from regulations, yet this remains a future prospect.

Investors, too, are demanding greater transparency. As inexpensive forms of beta become easier to access, the market place has begun to break down where asset managers add value.

Turning to tax, what started as a regulatory issue is fast becoming reputational. In short, the global tax system is broken. As tax information becomes publicly available, and strong populist sentiment continues, so the public will judge whether companies are paying their 'fair share' of taxes in an emotionally charged environment. Taxes must now be viewed as an operational risk.





## Game changers set to redefine the industry

*Asset Management 2020 set out six likely game changers that would impact the competitive environment. In our view, understanding, analysing and acting on these would prepare firms for the opportunities the changing landscape presented.*

These were:

- 1 Asset management moves centre stage
- 2 Distribution is redrawn – regional and global platforms dominate
- 3 Fee models are transformed
- 4 Alternatives become more mainstream, passives are core and ETFs proliferate
- 5 New breed of global managers
- 6 Asset management enters the twenty first century.

These game changers have or are coming to pass to varying degrees. Below, we outline to what extent these game changers have evolved in a period of accelerating change.

1

## Asset management moves centre stage

Our prediction that AWM would move definitively out from the shadows of its banking and insurance cousins by 2020 is proving broadly correct. We anticipated that regulation, retirement, urbanisation and the growth of sovereign wealth funds would all thrust AWMs to the centre stage of finance. Broadly speaking, this is happening, with AWMs often taking on the role of first movers and innovators.

AWMs, through new types of investment products, have been continuing to expand into areas vacated by banks restrained by capital regulations. While the Trump administration's stated desire to roll back regulation may increase bank lending in the US, this trend remains powerful elsewhere. Within the European Union, for example, a proposed Capital Markets Union aims to increase the role of capital markets and,

therefore, asset managers, in financial intermediation between savers and users of capital.

Through the private debt markets, asset managers are funding, among other things, real estate lending, leveraged buyouts, SMEs and trade finance. According to Preqin, the private debt industry managed assets of \$595 billion in June 2016, having quadrupled in size since 2006.

Turning to pensions, asset managers are playing a central role in plugging the global pensions gap as the population ages, chiefly through defined contribution pensions. We anticipate that pension funds will grow from US\$38.2 trillion in 2015 to US\$56.1 trillion by 2020. The pensions gap is estimated at \$41 trillion by the Geneva Association, the insurance industry think tank.<sup>11</sup>

*Asset Management 2020* also foresaw urbanisation creating a huge need for new infrastructure. PwC has estimated that close to \$78 trillion will be spent globally on infrastructure from 2014 to 2025.<sup>12</sup> Given the long life of infrastructure assets, banks (with their levered balance sheets and weighted average duration of liabilities of <10 years) are structurally unsuited to intermediating financial flows to fund these assets. On the flipside, the long lifecycles match pension fund liabilities and sovereign wealth funds. This market offers asset managers significant opportunities, although barriers related to political acceptability and transfer of risk are currently holding it back.

*Asset Management 2020 also foresaw urbanisation creating a huge need for new infrastructure. PwC has estimated that close to \$78 trillion will be spent globally on infrastructure from 2014 to 2025.*



11 The Pension Gap Epidemic, Challenges and Recommendations, November 2016. (<https://www.genevaassociation.org/media/954342/the-pension-gap-epidemic.pdf>)

12 Capital project and infrastructure spending: outlook to 2025. (<https://www.pwc.com/gx/en/capital-projects-infrastructure/publications/cpi-outlook/assets/cpi-outlook-to-2025.pdf>).

2

## *Distribution is redrawn – global and regional platforms dominate*



Our prediction that, by 2020, four distinct regional fund distribution blocks would have formed, allowing products to be sold pan-regionally, is looking broadly correct. We anticipated that the four blocks would be: North Asia, South Asia, Latin America and Europe. But, like other commentators, we didn't foresee the strength of political and economic nationalism, which has hindered this trend.

In Asia, we correctly predicted the development of two regional platforms, although it's happening more slowly than we thought. The Hong Kong-China mutual recognition became reality in 2015, but there is little sign of Taiwan joining up to create a Greater China bloc. In Southeast Asia, the ASEAN platform has moved forward, albeit much more slowly than expected, but the APEC Asia

Funds Passport is on track to go live in December 2017. Singapore remains outside this passport for now, although that may change if the perceived taxation imbalances are addressed in time.

Meanwhile, the European UCITS structure continues to gain strength. However, the UK vote for Brexit could, depending on the eventual trade deal between the UK and the EU, introduce more complexity into distribution within Europe.

Finally, the development of a Latin American fund passport that we foresaw remains at an early stage.



## Fee models are transformed

Our prediction that, by 2020, virtually all major territories with fund distribution networks would have introduced regulation to better align the interests of the end consumer, distributor and asset manager is proving accurate. In most cases, this alignment is designed to ensure that the distributor recommends a fund to the consumer entirely on its merits, and isn't influenced by the level of commission.

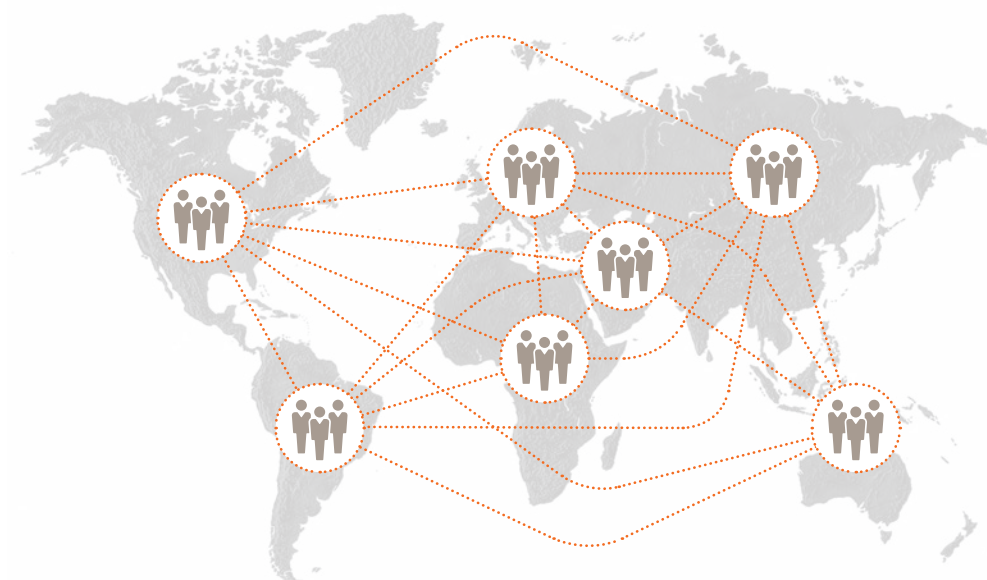
The UK's Retail Distribution Review (RDR) started the trend by banning commissions in 2012. Regulators have since introduced similar measures in Australia, South Africa, the Netherlands and many other countries. Most recently, the European Union has banned retrocessions through its MiFID II directive. In the US, the Department of

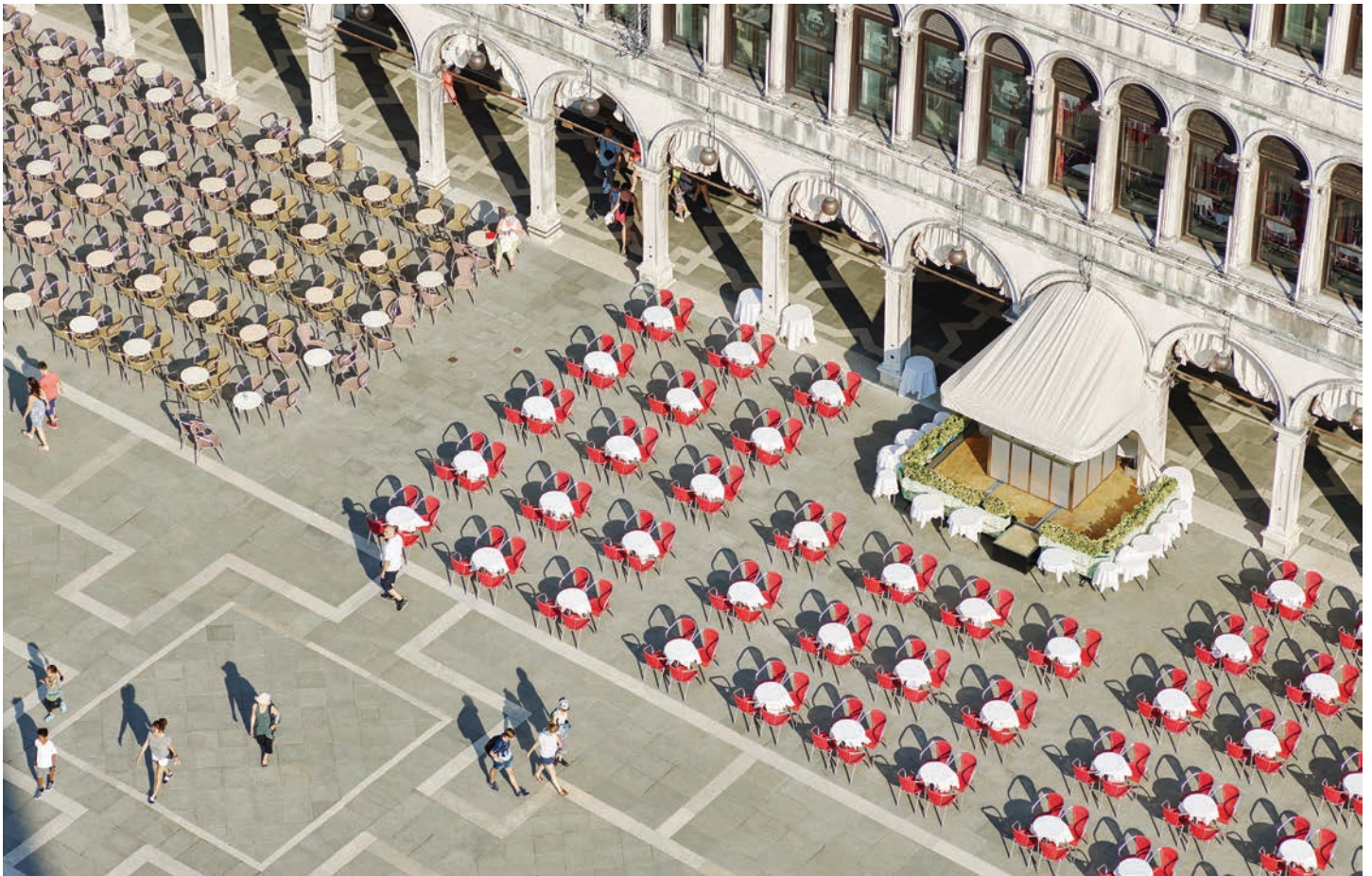
Labor's proposed Fiduciary Rule has led most wealth managers to rationalise 25-30% of retail mutual funds, and asset managers have responded by merging/consolidating mutual fund offerings with similar mandates, launching new share classes ('T' shares, clean shares) and dropping pricing. Although the Trump administration has placed the rule under review, the changes envisioned have already taken place.

In Asia-Pacific ex Japan and Australia, no specific regulations are proposed but there is significant pressure from investors for greater transparency into fees and costs.

This transformation of fee models will continue to put pressure on revenues for both asset and wealth managers.

*Our prediction that, by 2020, virtually all major territories with fund distribution networks would have introduced regulation to better align the interests of the end consumer, distributor and asset manager is proving accurate.*





## 4

### ***Alternatives become more mainstream, passives are core and ETFs proliferate***

Just as we discussed, asset flows away from traditional active management and towards passive and alternative strategies are accelerating. As a result, the overall proportion of actively managed traditional assets under management is shrinking.

By 2020, we forecast in Asset Management 2020 that active management's share of global AuM would have declined to 65%, while passive grew to 22% and alternative to 13%. We have since updated our forecast to predict that active management's share will be 66%, passive's 21% and alternative's 13%. (This compares with

active's 74% share in 2015, passive's 14% share and alternative's 11% share.)<sup>13</sup>

As a result, active management's global AuM will rise from US\$ 58.4 trillion in 2015 to US\$ 74.0 trillion in 2020, passive's will rise from US\$ 11.3 trillion to US\$ 23.2 trillion and alternative's from US\$ 9.0 trillion to US\$ 13.9 trillion.<sup>14</sup>

Within alternative management, we believe that real assets, private equity and new types of private debt funds will take on a stronger role in driving growth. Hedge funds will not fare so well, after a period of disappointing returns.

<sup>13</sup> PwC Global Market Research Centre.

<sup>14</sup> PwC Global Market Research Centre.

5

## *New breed of global managers*

Our prediction that 2020 would see the emergence of a new breed of global manager is happening, although not as quickly as we thought. We anticipated that these managers would emerge as large scale, targeted solutions for a broad array of customers and more trusted brands became more important.

While this hasn't happened in exactly the way we expected, the intense margin pressures playing out in the AWM industry today are likely to force far more consolidation of products and firms in the years ahead.

6

## *Asset management enters the twenty first century*



*65% of CEOs foresaw technology reshaping or significantly impacting competition.*

Technology is poised to become mission-critical for AWMs by 2020, just as anticipated in Asset Management 2020. We stated that it would drive customer engagement, data mining for information on clients and potential clients, operational efficiency, and regulatory and tax reporting. We also predicted that cyber risk would become one of the industry's key risks.

But three years is a long time for technology innovation. Since 2014, the likely impact of technology on AWM has increased hugely. It's likely to disrupt all areas of the industry – from investment advice, through the middle and back offices to client engagement and distribution.

In the AWM section of PwC's 2017 CEO Survey, 65% of CEOs foresaw technology reshaping or significantly impacting competition.<sup>15</sup> Yet, even this majority seemed to understate the potential impact; across financial services as a whole, 77% of CEOs anticipate this happening.

<sup>15</sup> Key findings from the asset and wealth management industry; 20th CEO Survey; <https://www.pwc.com/gx/en/ceo-agenda/ceosurvey/2017/gx/industries/asset-and-wealth-management.html>



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## Conclusion

*In summary, the landscape and game changers that we identified in 2014 are evolving. If anything, the forces of change are becoming more powerful. As a result, this is a critical time of creative destruction. There are great opportunities for those understanding and acting on the likely changes, yet some firms are likely to disappear through consolidation. This update is a prequel to a fuller paper examining these trends that we plan to publish in autumn 2017.*

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