



---

# Anticipating the Future of the Funds Industry in Light of UCITS IV

*European UCITS IV Survey Results: Executive Summary*

---

Survey Undertaken in Conjunction With



Marc House, 13-14 Great St Thomas Apostle  
London EC4V 2BB  
Tel: 020 7213 9760, Fax: 020 7489 1644  
[www.bluerock-consulting.com](http://www.bluerock-consulting.com)



# Executive Summary

UCITS IV - a Directive designed to help structure the industry on a European scale?

- The UCITS IV initiative was based upon the assumption that existing regulation is a barrier to increased concentration within the European asset management industry
  - In 2006 the European commission wrote in its white paper that regulation did *“not allow fund managers with funds or activities in different Member States sufficient flexibility to organize or restructure businesses. These inefficiencies and constraints are reflected in higher costs and lower returns that are borne by the fund investors. Independent research estimates that a reduction in European fund operating costs to US levels costs would boost nominal investment returns by 3%”*
  - UCITS IV was based on the idea that creating additional regulatory tools, e.g. management passporting, and removing some barriers to fund distribution would allow the industry to fully reshape, help create leading asset managers within Europe and finally lower prices for investors
- Findings from this study heavily challenge the above assumption in at least two different ways
  - The potential for new distribution opportunities within Europe should not be overestimated: When existing markets and level of sophistication are looked at, there does not appear to be clear opportunities for significant growth within European markets
    - Local management is frequently focussed on local needs, be it through local or foreign vehicles (mainly Luxembourg)
    - In most cases, national preferences seem to prevail when determining positioning within the European Market
  - Asset managers are not planning to use UCITS IV as a tool for reorganizing on a pan-European basis. Many are already more structured than was assumed by the European Commission. In most cases management is already heavily concentrated in one or two countries. In many cases a distribution hub is already set-up, particularly in Luxemburg ,with relevant know-how available
- We believe that UCITS IV will eventually prove to be a useful tool for asset managers, even if it’s scope is ultimately expanded beyond its primary purpose and it becomes a brand known and respected on a global basis



# Executive Summary

*Our view is that UCITS IV will deliver only some of the benefits first touted for it*

- It appears that the challenges facing the European fund industry are not primarily caused by existing UCITS regulations
  - There remain **other regulatory barriers** to cross-border distribution: investor reporting, status and constraints on fund administration
  - Taxation systems remain highly heterogeneous
  - Several business issues also limit fund distribution across Europe
    - A large part of distribution remains concentrated in the hands of insurance and banking groups
    - Pan-European distribution platforms allow asset management companies to diversify their distribution across Europe, but costs for cross-border distribution are still high, especially for small and medium-sized managers
    - A preference for own nation funds seems to prevail, especially within the retail segment
  - **Cross-border management of assets has already taken place**, to a certain extent, through management delegation
  
- UCITS IV only brings a partial answer
  - A quicker **notification procedure** will help reduce time-to-market and a more understandable version of the prospectus (**KID**) will increase transparency for the end investor, but these improvements only indirectly contribute to increased sales
  - The **management passport** is an alternative to delegation mechanisms that will continue to be used for cross-border management
  - **Cross-border mergers** could help reduce administrative costs linked to multiple and redundant product ranges, but will largely only be considered when tax issues are clarified
  - The Directive does not significantly address **distribution costs**: KID specific regulation on advertising material will remain (and the KID itself still has to be translated into the language of the country of distribution)
  
- Master-feeder fund structures appear to provide the best opportunity to gain benefit from new Directive
  - It is possible to use UCITS IV for marketing purposes, e.g. local fund, local branding, tailored pricing, etc., whilst at the same time centralizing management activities



- The Directive does not a priori give rise to new market opportunities. The case for more efficiency and larger distribution is related to the same business issues that prevail today. Opportunities and threats have to be considered in this light
- Potential threats to future growth of the fund industry remain, and these won't be addressed by the Directive
  - **Market performance may not improve.** Although UCITS funds can borrow and use derivatives, they are not as flexible as hedge funds in exploring emerging market trends
  - At a time when banks are badly in need of retail funding, **savings products** – together with other investment products such as life insurance – still represent tough competition for fund managers. On the institutional side, structured products also frequently represent an alternative to more traditional fund structures
  - For those countries without strong local know-how in asset management, the passport will eliminate the hurdles to cross-border management imposed by some countries. This creates a **significant threat** of tougher competition for them, but it is partially mitigated since national distribution networks still remain hard to enter
- The real opportunities for further distribution only partially arise from the Directive
  - The best way to access new distribution networks remains the **takeover of a local participant** to use its existing distribution facilities. This consolidation will be related as much to the financial crisis as to UCITS IV. Most likely, master-feeder structures will be helpful in this process
  - **Smaller European markets have low management capabilities**, including those of the Central European countries, and require import of asset management know-how. The shortfall between local demand and supply is limited, but entry costs should be lowered by the ability to use the passport, master-feeder structures, and by streamlined regulatory processes
  - **Master-feeder structures** open huge marketing/branding opportunities, easing the entry into new markets, or allowing adaptation to local constraints in markets already covered
  - **For smaller organisations**, distribution costs will be significantly lowered in the absence of need for local structures, although selling locally requires local sales forces that have a cost anyway. **Bigger organisations** already centralize their management, and will remain local anyway for sales/distribution, non-UCITS business or prestige purposes: the passport is of marginal benefit to them
  - **Fast-growing markets outside of Europe** (BRIC countries) remain the major opportunity. Many developing economies have simply not had the opportunity to develop their own fund legislation to the same standard. It is therefore easier for these countries to “adopt” the UCITS brand as it channels their savings into reliable vehicles, albeit those vehicles and assets are domiciled outside of their own borders



# Executive Summary

*UK based asset managers believe that UCITS IV will change their industry but not themselves*

- UK-based asset managers believe that the European fund market will become more concentrated as a result of UCITS IV, with fewer and bigger asset managers facing greater demands for market transparency and price competition
  - UCITS IV will allow easier access to new markets , with passporting mentioned as the key benefit
  - Change is expected to be gradual, with the winners being those with cross border rather than purely national capabilities
  - This change is driven by product sales and distribution opportunities, not the ability to access internal efficiencies
- However, UCITS IV is not seen as a driver of new business opportunities for most UK-based asset managers
  - There was an almost uniformity of view that the Directive will not change thinking on entry into new European markets
  - Identification of sales opportunities / market attractiveness remains key and the pre-existing tools were deemed adequate
- UK-based asset managers expect UCITS IV to have minimal impact on existing fund ranges and organisational structures
  - It is not expected that there will be any significant merging of funds at a cross border level
  - Interestingly though most of respondents noted that they are actively studying the possibility of adopting master/feeder structures
  - Some centralisation is planned, but largely following implementation of the Directive and based upon actual sales experience
- Further legislation is expected, and in particular clarification of the role of the Depository and greater tax harmonisation
  - There is a feeling that the utility trade-off between increased regulation and market efficiency needs to be better recognised
  - It was felt that larger firms are better placed to handle the additional costs whereas smaller firms may relocate outside of the EU
- The vast majority of these asset managers intend to complete their preparations over the course of 2010/11
  - They have canvassed input widely (although not, it appears, from European forums), they are confident that they understand the Directive, and they state that they have clearly defined plans in place to prepare for implementation
  - However, this level of readiness must be tempered by the fact that they consider lack of clarity and a large number of unknowns to be major issues for them. Are they therefore as ready as they think they are?



# Executive Summary

*What can we conclude for UK-based asset managers?*

- UK-based fund managers cannot afford to be complacent: European competitors are looking at the UK as a potential market
  - The UK funds market is already relatively **sophisticated and deemed well served** by its existing funds providers
  - There remains **potential for growth**, not least as a result of the Savings Reallocation and Savings Trends effects
  - With its relative openness, **the UK funds market is likely to be attractive to European asset managers** looking to diversify geographically
- Quickly go for a European distribution strategy, based on an opportunistic approach
  - Given the size and structure of the European market, it would be highly risky to bet on one single country. An **opportunistic strategy** based on maximizing the re-use of the existing offer, combined with a light investment in new market opportunities should prevail. This will help gain a better knowledge of foreign markets, and seems the safest short term strategy
  - Most of the players in **established markets in Europe are expected to adopt a more defensive position** after UCITS IV
  - Italy and the Eastern European countries are expected to represent the **markets most ripe for exploitation**
- Concentrate on core business – asset management and sales – and find innovative solutions for distribution
  - UCITS IV will definitely not simplify the fund distribution process: creating the KID and receiving a fund distribution passport is only one part of the whole distribution process which also includes handling marketing material, tax issues and transfer agency processes. Reliable solutions already exist to tackle those, albeit at a high cost. **Finding a better and cheaper platform will be part of the solution.**
  - The generalization of **master-feeder structures will help modify the distribution patterns.** We believe it will bring sizable opportunities for UK-based asset managers to offer their management know-how at a competitive price, while leaving the burden of distribution to their local partners. This could prove highly effective for penetrating, for instance, the German market, where distribution is tricky due to both complex regulation and a highly fragmented financial sector
- In the medium term, consider shopping around Europe for M&A opportunities
  - As growth opportunities on local fund markets appear to be rather limited, **we expect the number of players exiting from the market to grow** higher in the coming years. This trend, which is already to be observed in Italy, could spread largely across Europe. With some big banks desperately in need of additional capital to cope with Basel III new requirements, selling non-core activities such as asset management subsidiaries would be an increasingly viable option
  - With several asset managers already among the European leaders, **French players are well positioned** to benefit from this trend and should prepare for further strategic acquisitions



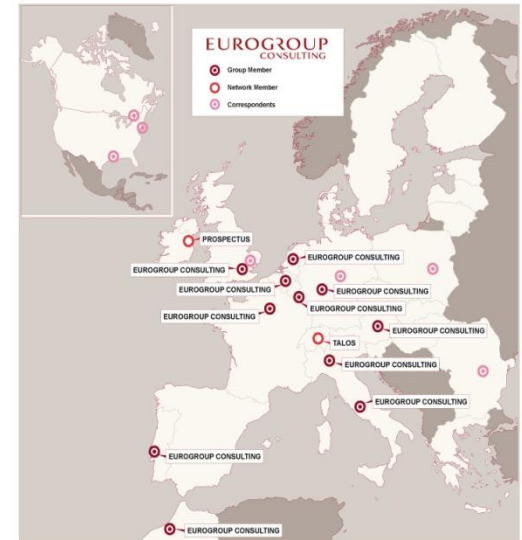
- **Company Profiles**



- Bluerock Consulting Limited is a private limited company formed in 1999
- Our consultants have, on average, over 15 years experience within Financial Services
- We work across multiple sectors, but with in-depth knowledge and experience in each
- We offer four main service lines
  - Business Advisory: Helping clients determine what and how they should achieve their strategic aims
  - Change Delivery: Planning, execution and review of projects & programmes
  - Sourcing: Full range of sourcing from strategy to service, covering all core components of strategy, process, technology, legal, commercial and management
  - World Class IT: Focus on the transformation and optimisation of IT from internal department or external supplier
- Bluerock can call upon a network of subject matter experts sourced via Bluerock Resourcing, a wholly owned resource management subsidiary



- Eurogroup Consulting is a leading European independent consulting firm in organization and management, providing support to its clients in their critical transformation projects
- Eurogroup's independent policy towards IT solutions sales and financial audit activities, guarantees the objectivity of recommendations (no conflict of interest)
- Eurogroup Consulting's approach concerning its consulting activities results in a true and close relationship with our clients, taking into account their business challenges, environment and the respect of their corporate culture
- A European presence – Eurogroup Consulting Group and Network
  - 1200 consultants, 22 offices in 16 countries and a turnover of €130 million





Marc House, 13-14 Great St Thomas Apostle  
London EC4V 2BB  
Tel: 020 7213 9760, Fax: 020 7489 1644  
[www.bluerock-consulting.com](http://www.bluerock-consulting.com)



**Bob Heath**  
Head of Asset Management

Tel: 07767 446018  
Email: [bob.heath@bluerock-consulting.com](mailto:bob.heath@bluerock-consulting.com)