

EXECUTIVE SUMMARY

UK INVESTMENT MANAGEMENT INDUSTRY: ADAPTATION TO A NEW ENVIRONMENT

- » Total assets under management (AUM) managed by IA members fell to £8.8 trillion at the end of 2022, a 12% decrease on the previous year. After strong growth in AUM for the past decade, a broad-based market correction has been the main driver of this fall, reflecting monetary policy regime change, hot war in Europe and a range of economic, political and security uncertainties internationally.
- » The UK maintains its position as a leading international investment management centre. This is measured on four metrics: overseas clients (48% of total AUM), global investment (78% of shares and bonds invested in overseas markets), internationally-headquartered firms (60% of total AUM) and economic contribution (5.5% of total net services exports).
- » Despite the continuing strength of the industry's international position, there is rising concern across the industry about threats to competitiveness and the potential knock-on effect for the domestic market. We cover six themes: stimulating innovation; facilitating cross-border business; focusing on the cost of doing business; modernising the regulatory process; calibrating risk appropriately; and targeting regulation effectively.

THREE KEY AREAS FOR TRANSFORMATION AHEAD

- » With innovation-driven competitiveness and regulatory reform as overarching themes, there are three specific areas that are defining the evolution of the industry's relationship with the wider economy and society.
 1. Technology: In investment management, as elsewhere in the economy, technological development is increasingly focused on Artificial Intelligence (AI) and tokenisation. While AI has been the prevailing theme of 2023, the potential for tokenisation to transform the operational backbone of the fund and wider capital markets remains significant.
 2. Sustainability: Firms are of the view that the Sustainable and Responsible Investment (SRI) agenda will remain a defining one for the industry, particularly with respect to the urgency of tackling climate change. We set out a series of factors that are contributing to a challenging delivery environment for firms both domestically and internationally.
 3. Culture: At the heart of the cultural transformation agenda lies the increasing focus across the industry on Equity, Diversity and Inclusion. We see parallels with sustainability in that there are significant business risks for firms of not getting this right sitting alongside the wider imperative to better reflect and support the society in which they operate.

TRENDS IN CLIENT ASSETS AND ALLOCATION

- » The share of assets managed on behalf of retail clients grew again from 22% to 25%. While the Covid-19 pandemic appears to have increased retail participation and total retail AUM through 2020-2021, a further year-on-year increase through 2022 may be more the result of differential asset class returns across client groups.
- » Through 2022, the proportion of assets invested in equities was broadly unchanged in part due to the relatively strong performance of UK equities compared to global peers. The share of fixed income assets fell from 30% to 28% as fixed income assets – especially domestic bonds – fell more sharply than the equity markets.
- » Global diversification continues to be a key theme in asset allocation. In 2022, 60% of fixed income assets were held in overseas bonds compared with 55% last year and over a third (37%) of holdings ten years ago. UK equity holdings continue to decline as a proportion of total equities, falling to 22%. North American equities have significantly surpassed UK equities as the largest region for equities managed from the UK (32% from 30% in 2021).
- » Indexing strategies now account for a third of total AUM, a one percentage point increase from 2021 and a twelve-percentage point increase over the past decade. Exchange Traded Funds have been an important contributor to the growth of indexing strategies in recent years.

- » Investment managers continue to make a major contribution to the domestic economy, managing some £4.6 trillion for UK customers, both retail and institutional. They hold an estimated £1.4 trillion in UK shares, bonds, property and infrastructure.

UK INSTITUTIONAL CLIENT MARKET

- » IA members now manage £3.9 trillion globally on behalf of UK based institutional clients, which represents a fall of 16% from a year earlier, driven by sharp falls in UK bond markets.
- » Third-party AUM stood at £3.3 trillion, once in-house mandates are excluded from the institutional data, down from £4.0 trillion in 2021. Pension funds remain the largest client type, accounting for 63% of third-party assets though this is substantially lower than the 69% reported in 2021.
- » Total assets in liability driven investment (LDI) strategies fell 28% on a matched basis to an estimated £1.17 trillion, after an exceptionally turbulent period in the UK gilt market. When LDI assets are excluded, specialist mandates continue to be the predominant approach in the third-party institutional market, accounting for 80% of total assets.
- » Within specialist third party mandates, the proportion of assets in equity mandates decreased by one-percentage point over the year (to 38%) despite the weak equity performance environment. The share of assets in fixed income mandates fell to 32%, a four-percentage point fall on the previous year and its lowest level in the past decade.

UK RETAIL FUNDS MARKET

- » UK investor funds under management (FUM) fell 14% to £1.37 trillion over 2022. After the second highest inflows on record in 2021, we saw the first year ever to record a calendar outflow, with net redemptions of £25.7 billion.
- » Rising inflation and the changing monetary environment played a major role in the dislocation, which was felt strongly across both equity and fixed income markets. The central driver of the fall in FUM was returns (77% of total fall) rather than redemptions.
- » SRI was not immune from the correction, although robust in comparison with the wider market. FUM growth remained marginally positive and sales to responsible investment funds remained resilient at £5.4 billion over the year, down from £15.9 billion in 2021.
- » 2022 saw a sharp reversal of the resurgence in sales to actively managed funds. Net retail outflows of actively managed funds were a record £36.6 billion, amidst robust sales to trackers of £11.0 billion.
- » At the level of total FUM, the share of fixed income (17.4%) fell back to the lowest level in fifteen years. UK equities continued what has become an extraordinary decline as a proportion of total FUM to reach a new low of 12.8%, after accelerating falls since 2016.

OPERATIONAL AND STRUCTURAL ISSUES

- » Total industry revenue after commission stood at £23.3 billion in 2022 while costs stood at £18.3 billion. Operating profitability dropped to 22%, reflecting faster drops in revenue than in costs.
- » As of 2022, the UK investment management industry supports approximately 126,400 jobs, of which approximately 46,200 people are directly employed, a 3% increase on the previous year. We estimate that a further 80,200 people are indirectly employed in supporting industries.
- » Despite accelerating M&A activity, the UK investment management industry remains relatively unconcentrated. Total assets managed by the top five and the top ten firms stood at 43% and 58% respectively.