

FUND MANAGEMENT BRIEF

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This Brief is an update of IFSL's City Business Series report on Fund Management, published in July 2000. The next full edition of the report will be published in Q3 2002. Other sectors covered by the City Business Series include Derivatives, Legal Services, Banking, Insurance, Maritime Services, Securities Dealing, Accounting and Management Consulting. All IFSL's publications can be downloaded from our website at www.ifsl.org.uk.

FUNDS UNDER MANAGEMENT IN THE UK

The UK is one of the largest markets in the world for fund management with identified assets under management totalling over £2,850bn in 1999. Two-thirds of this was managed on behalf of UK institutional clients and a fifth on behalf of overseas clients. The remaining 12% was accounted for by UK private client funds.

London is the largest world centre for the management of institutional equity. On the same basis, Edinburgh and Glasgow have improved their position in recent years and were ranked in 1999 as the sixth financial centre in Europe and fifteenth in the world.

The international orientation of the UK's fund management industry is reflected in the presence of a broad range of UK and foreign-owned firms; in the significant investment in overseas securities; and in the management of overseas clients' assets.

- *Institutional funds* have become increasingly prominent in the UK over the past two decades. In 1999, institutions held £2,477bn of funds, nearly three times the 1990 total, and accounted for over 85% of total identified funds under management. Insurance companies manage the bulk of these funds, although pension funds and unit trusts have increased more in the past decade. A substantial proportion of institutional funds is invested in equity. As a result, institutional investors account for a larger proportion of shares in the UK than in most industrialised countries, nearly 60% in 1999;
- *Overseas clients* In recent years, the UK has consolidated its position as the most important centre for the management of funds on behalf of overseas clients. The Fund Managers' Association's (FMA's) latest available survey showed that in June 1999 overseas clients' funds in the UK totalled £592bn. Overseas share ownership of UK equities more than doubled during the past decade, increasing from 12% in 1990 to over 29% in 1999. Most of these investments are in FTSE-100 companies;
- *Private clients* remain a significant niche in the UK market with around 12% of the total identified funds. In 1999, around 15% of UK equity or nearly £300bn was in the hands of some 12m predominantly small shareholders. Although the proportion of equity held by individuals is lower than in other countries, the greater UK market capitalisation

Funds under management in the UK

£bn	UK clients	Overseas clients	Total
	Dec-99	Jun-99	
<i>Institutional funds</i>			
- pension funds	777	208	985
- insurance companies	1,034	60	1,094
- unit trusts	222	49	271
- investment trusts	60	11	71
- money market mutual funds ¹	7	21	28
- other	-	193	193
less unit and investment trusts held by other funds	-165	-	-165
<i>Institutional total</i>	1,935	542	2,477
<i>Private clients</i>	330	50	380
All clients	2,265	592	2,857

¹ June 2000

Source: National Statistics, ComPeer, Fund Managers' Association, Imoneynet

The top international target cities, 1999

\$bn, ranking by institutional equity holdings

London	UK	2,461
Metropolitan New York	US	2,363
Tokyo	Japan	2,058
Boston	US	1,871
San Francisco	US	726
Los Angeles	US	569
Paris	France	458
Philadelphia	US	419
Zurich ¹	Switzerland	414
Denver	US	340

¹ Note: includes Basel, Winterthur

Source: Thomson Financial, Target Cities Report 2000

implies a more significant penetration of individual share ownership. Within Europe the value of private client funds handled in the UK is probably exceeded only by funds managed in Switzerland.

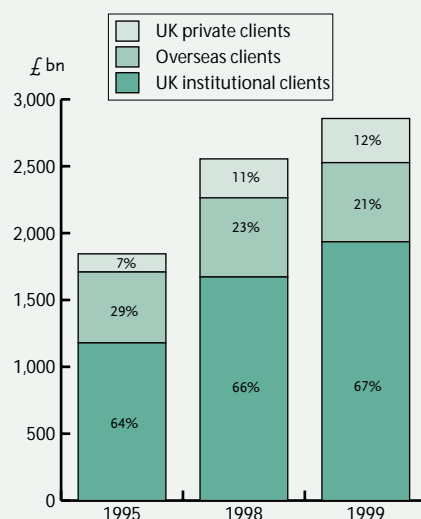
UK investment management organisations include many different types of funds, such as life insurance, pension schemes, unit trusts, investment trusts and money market mutual funds. Most large organisations tend to operate more than one type of fund within the same group.

- *Investment banks* represent integrated banking and securities groups that combine securities firms, i.e. brokers or market makers, and fund management firms within the same group. They accounted for 41% of the UK total identified funds under management in 2000;
- *Insurance companies* held around 37% of total UK funds under management in 2000. The fund management activities of insurance companies are either managed from their internal investment department or from a separate subsidiary which might manage funds of external clients as well as those of its parent company;
- *Independent investment managers'* share of funds increased in recent years to one-fifth of the total. These include any of the fund managers that are not linked to any UK-based banking, securities or insurance groups. AMVESCAP, one of the largest independent investment manager in the world, accounts for more than half of this;
- *Self-managed pension funds* represent separate legal entities set up to manage a company's pension fund assets. Their share has fallen in recent years as companies' pension funds are increasingly managed externally. In 2000, self-managed pension funds accounted for around 2% of total identified UK funds under management.

Fund managers have an array of investment choices available to them at home and overseas including equities, bonds, property and cash. UK institutions have traditionally favoured investments in equity, given the generally good long-term returns. In 2000, an average of 49% of pension fund portfolios was allocated into UK equities with a further 22% invested in overseas equity. This is higher than in most other industrialised countries. Bonds and Government securities accounted for a around fifth of UK pension funds' investments. The remainder was held in cash and property funds. The proportion of equity investment is lower elsewhere in Europe, largely due to investment restrictions which may set a ceiling on certain types of investment.

According to the Watson Wyatt World 500, Barclays Global Investment Managers was the UK's largest investment manager in 2000 followed by AMVESCAP and CGNU. Substantial restructuring in recent years has reflected global developments in the fund management industry. Some of the mergers in the UK have not only been between asset management firms but have also included related industries such as banking and insurance as firms seek to diversify. Recent larger UK mergers and

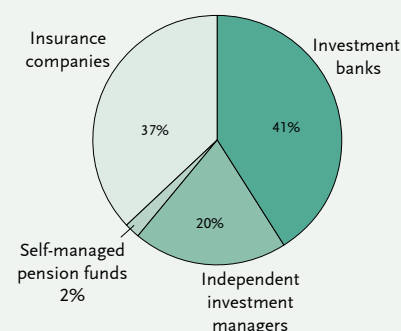
Growth of funds under management in the UK



Source: National Statistics, ComPeer, Fund Managers' Association, Imoneynet

Fund management organisations, 2000

% share of UK funds, survey total \$3.4 trillion



Source: Watson Wyatt World 500, PaI, IPE

Largest UK fund management organisations

	worldwide assets at end-2000	
	\$bn	
1	Barclays Global Investors	801
2	AMVESCAP	402
3	CGNU	329
4	Prudential M&G	235
5	Schroders	198
6	Lloyds TSB	182
7	Legal and General Group	165
8	Standard Life Investments	123
9	HSBC Holdings	123
10	Eureko/F&C ¹	111
11	Royal & SunAlliance	107
12	Hermes Pensions Mgmt.	68
13	Friends Ivory & Sime	55
14	Halifax	50
15	Aberdeen Asset Mgmt.	44

¹ UK/Netherlands
Source: Watson Wyatt World 500, Pensions & Investments

acquisitions include: the acquisition of United Asset Management by Old Mutual, Robert Fleming Holdings by UK Chase Manhattan, Gartmore Investment Management by Nationwide and Perpetual by AMVESCAP.

CONTRIBUTION TO THE UK ECONOMY

Value added While there is no official estimate of the contribution of fund management to UK's GDP, we can attempt an estimate from industry sources. Combining data for identified funds under management with PricewaterhouseCoopers (PwC) estimates of cost margins and cost distribution, our estimate of value added in 1999 is £4.2bn. This is equivalent to some 0.5% of the GDP in "value added" terms and therefore an important component of the financial sector's total contribution to GDP of 5.8%. Fund management's wider contribution to the economy is evidenced by the promotion of an efficient capital market that mobilises and allocates the nation's savings.

Revenue Combining PwC data on revenue margins for institutional funds with data on revenue for private clients separately estimated by ComPeer, we calculate the total revenue of fund management activities to be around £6.5bn in 1999.

Profits Fund managers have maintained consistent profitability in the past six years, according to the PricewaterhouseCoopers annual Investment Management survey, although average margins declined slightly from 29% to 28% between 1999 and 2000.

Employment According to the latest available Fund Managers' Association (FMA) survey, employment in the fund management industry was estimated at 26,436 in June 1999, a rise of 12% over the previous year. Total employment in the fund management industry including the large number of small firms is estimated at around 40,000. These figures do not include retail stockbrokers, who are thought to employ around 12,000 people.

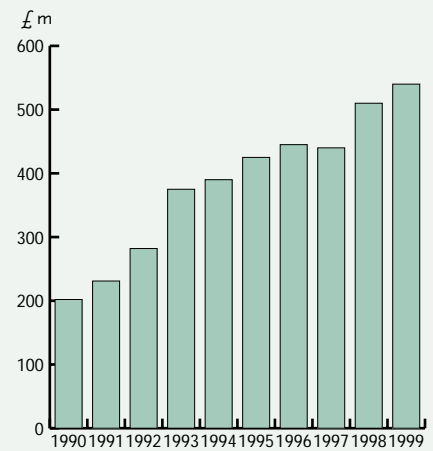
Overseas earnings generated by fund managers' services were estimated at £540m in 1999. A significant proportion of portfolio investment earnings (£1bn) from overseas is also attributable to fund management activities.

Several other financial services benefit from their links with fund managers, particularly banks, Stock Exchange firms and information providers.

INTERNATIONAL COMPARISONS

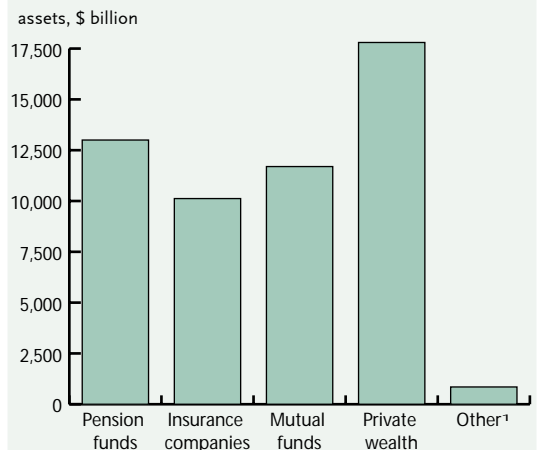
The volume of funds managed internationally has increased substantially in recent years. Global pension assets alone amounted to nearly \$13 trillion in 2000, with a further \$11.7 trillion invested in mutual funds and \$10.1 trillion in insurance funds. Merrill Lynch also estimates private wealth at \$27 trillion in 2000 of which probably about a third is represented in other products. In total, assets of the global fund management industry are

Overseas earnings of fund managers



Source: ONS

Global investment management industry, 2000



Notes: ¹ Private equity and hedge funds
Source: CCF Charterhouse, Merrill Lynch

likely to have exceeded \$53 trillion in 2000, more than double the 1995 total. The UK is a major player in this industry although rankings based on sources of assets understate its position due to the substantial value of funds managed in the UK on behalf of overseas clients.

- **Pension fund assets** Global pension funds assets have increased by over 60% since 1995 partly due to the process of pension reform around the world. The UK's \$1.4 trillion in pension assets accounted for around 11% of the world total in 1999. This was well ahead of other European countries and only exceeded by the US and Japan which have much larger domestic markets. The UK is in a group of countries with the highest ratio of pension assets to GDP, 95% in 1999. This was second only to Switzerland and the Netherlands. On average, more than a quarter of UK pension funds portfolios are invested overseas, mainly in equity. The US remains the top source of cross-border investments by pension funds followed by the UK which accounted for 18% of the total in 1999.
- **Insurance funds** Based on the most recent available country breakdown of insurance funds, the US is the major source of funds with \$3.2 trillion in 1999. UK insurance companies' investments were more than \$1.3 trillion, almost double those of any other European country.
- **Mutual funds** Mutual funds have more than doubled since 1995 to reach nearly \$12 trillion. The US is by far the biggest source of assets with more than 60% of the world total in 1999. Most of the other assets are administered from a few countries. UK mutual funds grew four-fold during the last decade to reach \$370bn or 3.3% of the total. Other important centres include France, Luxembourg, Italy and Japan.

The annual Watson Wyatt World 500 estimates that US owned companies held 41% of the \$35 trillion managed by the top 500 investment managers in 2000. Japanese companies managed 13% of the total, Swiss 10%, UK 9% and German 7%. UK companies that appear in the top of this list include Barclays Global Investors (ranked 5th), AMVESCAP (19th), CGNU (24th) and Prudential M&G (37th).

According to the Federation of Stock Exchanges (FIBV), capitalisation of world's equity markets fell in 2000 by 11.5% to reach \$31.1 trillion at the end of the year. The US accounted for more than a third of this, followed by Japan. The UK equity market is the largest in Europe with market capitalisation of some \$2,612bn, followed by Euronext Paris with \$1,447bn and Deutsche Börse with \$1,270bn.

Total capitalisation of the world's bond markets reached nearly \$30 trillion at the end of 2000. The US has historically been the largest market with 49% of the market share, followed by Japan. The size of the UK bond market is estimated to be over \$1,060bn or around 4% of the total. Non-government bonds have overtaken government bonds for the first time in 1999 and now account for 60% of the outstanding value.

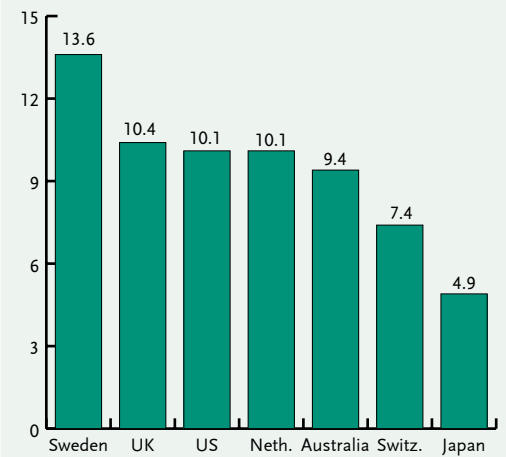
Sources of assets, 1999

\$ billion ¹	Pensions	Insurance	Mutual funds	Total
US	7,765	3,168	6,843	17,776
Japan	1,544	1,825 ²	464	3,833
UK	1,365	1,333	371	3,069
France	71	714	655	1,440
Germany	139	819	237	1,195
Netherlands	427	242	75	744
Italy	71	203	477	751
Ireland	50	40	20	110
Other	1,546	3,156	1,931	6,633
Total	12,978	11,500	11,073	35,551

¹ Conversion rate euro/US dollar 1.07
² IFSL estimate based on 1997 figure
 Source: OECD, CCF Charterhouse, ICI, FEFSI, InterSec

Performance of pension funds

Average real return on pension funds, % a year, 1991-2000



Largest global investment managers

		2000 \$bn
1	UBS Group	1,533
2	Fidelity Investments	1,037
3	Credit Suisse Group	867
4	AXA Group	840
5	Barclays Global Investors	801
6	Kampo	770
7	State Street Global	725
8	Allianz	672
9	J.P. Morgan Fleming	639
10	Vanguard Group	588
11	Deutsche Bank	586
12	Capital Group	561
13	Merrill Lynch	557
14	Mellon Financial	530
15	ING Group	468

Source: Watson Wyatt World 500, Pensions & Investments

PRIVATE WEALTH

Latest estimates of the private wealth market by Merrill Lynch/Gemini Consulting indicate that there were around 7 million people with financial assets in excess of \$1m in 2000. Their combined financial assets totalled \$27 trillion, a 40% increase from 1997. This means that the private wealth industry is larger than the global insurance industry, pensions industry or mutual fund industry. However, these categories overlap since the private wealth industry is also an investor in conventional asset management.

Private wealth grew by 6% in 2000. This was well below the 18% registered in the previous year despite the continued global GDP expansion. The major factor behind the slowdown in 2000 was the poor performance of global equity markets. The Nasdaq was down 40% during the year, the Dow Jones 7% and the FTSE 10%.

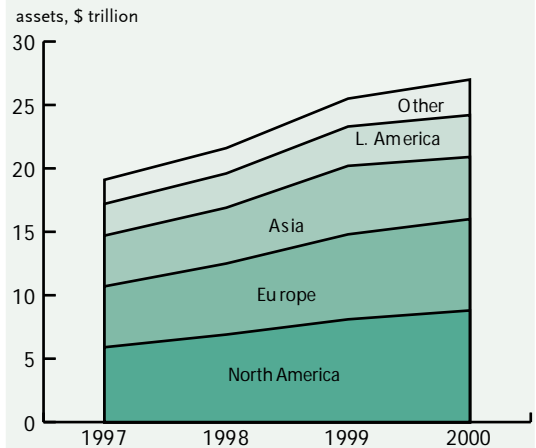
Europe and North America are the major sources of private wealth generating 60% of the total wealth and 67% of the number of HNWI (High Net Worth Individuals). Asian HNWI hold 18% of the wealth and Latin American 12%. The Middle East, Eastern bloc and Africa together account for the remaining 10%.

According to latest available data published by Cap Gemini, in 1997 the potential UK customer base for private wealth services was around 4 million with assets amounting to £770bn. The number of customers is forecast to rise to 4.9 million by 2005 with assets of nearly £2 trillion.

Onshore centres account for an estimated two-thirds of private wealth. The main centres for onshore investment are the major international financial centres, namely New York, London, Tokyo, Singapore and Hong Kong. The offshore market has traditionally been an important destination for private wealth. Switzerland and the UK held the bulk of the offshore market with 33% and 15% respectively in 1999. The US and the Caribbean were the next largest destinations with 12% each.

London is a major centre for international wealth management. As well as expertise in fund management and the general provision of investment advice, there is also considerable experience in international tax and trust law that can meet the needs of clients operating in an international context. It is also possible to obtain advice on specialised products such as emerging market investments and Islamic financial services.

Global private wealth industry



Source: Merrill Lynch, Cap Gemini Ernst & Young

IFSL Research

International Financial Services, London (IFSL) is a private sector organisation, with 30 years experience of successfully promoting the UK-based financial services industry throughout the world.

IFSL's research informs by raising awareness of the UK's role in international financial markets and by highlighting the major contribution of financial services to the UK economy. Financial sector reports in the City Business Series remain the centrepiece of research. IFSL is also producing a separate series of reports that highlight UK product expertise. Other major publications include International Financial Markets in the UK, The City Table and World Invisible Trade.

This IFSL brief has been compiled by Economist, Marko Maslakovic.

Further information on statistics and publications can be obtained from www.ifsl.org.uk or:

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