Press Release

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Despite AuM rises, mutual fund fees to fall by almost 20% by 2025

Tuesday 23rd October: In a new report entitled *Asset & Wealth Management Revolution: Pressure on profitability*, PwC predicts that fees will continue to fall up to 2025 as the Asset & Wealth Management industry (AWM industry) faces sustained pressure from investors and regulators. PwC estimates that mutual fund asset-weighted fees will fall by 19.4% from 0.44% in 2017 to 0.36% in 2025. As passive funds continue to grow in popularity and price becomes a key differentiator, they will see the sharpest fall of 20.6% up to 2025, whereas active mutual funds will see a decline of 19.3%.

This new report suggests how managers can consider the four foundations for a future-fit operating model during these industry changes. The model encourages managers to pay attention to value for money, finding a strategic positioning, understanding that technology is the key to future success and winning the battle for talent.

Olwyn Alexander, Global Asset & Wealth Management Leader for PwC stated that:

"Based on our sample of 64 AWMs with over $40 trillion in assets under management they have been able to improve their margins by 15.91% since 2012, largely due to strong AuM growth and lower costs achieved through economies of scale. However, going forward they will need to adapt their business models in the coming years in order to win in a new environment as fees continue to fall and improving or even maintaining operating margins will become much more challenging."

Key Findings:

- AuM is set to rise to US$145.4 trillion by 2025;
- Traditional mutual fund management fees are set to fall by 19.4% by 2025;
- Europe and Asia will see the strongest declines in mutual fund management fees of 26% and 24.6% respectively up to 2025.
- Passives will see a strong fee decline across the board as popularity for these products increases competition;
- Alternative fees have remained somewhat resilient; however as fee innovations lead the sector to become more outcome-based, PwC predicts management fees will fall between 13.1% and 16.4% by 2025 depending on the asset class;

- Total expense ratios are set to fall faster than management fees during the forecasted period, indicating that investors will benefit greatly in the coming years;
- In the developed markets, up to 25% of all mutual funds will close while exchange traded funds (ETFs) will grow significantly.
- In Europe and Asia, ETFs will continue to expand as they are more broadly accepted by retail investors;
- The ratio of revenue-to-AuM of traditional asset managers is estimated to fall by 22.4% up to 2025. This is despite PwC predicting that AuM will rise to US$145.4tn by 2025, indicating a sustained pressure on business models;

What does this mean for the industry ?

- For the fittest, opportunities abound to take advantage and capitalise on predicted AuM growth;

- As pricing concerns grow, the industry, in certain developed markets, will undergo significant consolidation with leading firms being acquired and laggards languishing. We estimate up to 20% of firms in developed markets will be eliminated by 2025;
- The number of mutual funds in the developed markets could fall by up to 25% by 2025;
- In order to maintain their margins, PwC has outlined four foundations upon which AWMs can build a future-fit operating model.
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- AWM managers need to clearly articulate why and how they provide value for money;
- AWM managers also need to focus on their strategic positioning – what's the plan?
- If managers don't transform through technology they will be eliminated;
- AWM industry could lose the battle for talent, unless they appreciate and understand the changes and challenges that are coming their way;

Olwyn Alexander further commented:

"To be fit for the future and able to adapt to operations in a lower revenue environment, managers should focus on a future in which the majority of costs are variable and therefore easier to manage.

"Managers who are quick in adapting to the changes that AI, data and analytics, and robotic process automation will bring to the industry will see success quicker than those who don't.

"Firms need tech-savvy talent in many different functions and the younger generation are increasingly seeking companies that reflect their values, challenge them and offer work and life opportunities. In order for the AWM industry to keep up in this revolution, it is very important they understand this movement in talent."

"In order to be fit for the future, managers should consider four crucial elements of their target operating model"

The four foundations that PwC recommend in this report are:

Articulating value for money
Investors are looking to the AWM industry to provide value for their money. This means further alignment with investors and those managers that fail to align will fall by the wayside. The constant introduction of new regulations amidst competitive developments in the market will push managers to be even more efficient and to adapt their pricing. Managers must react to the industry's changing price structures. New fee models are being developed, and investors are

searching for the firm that will provide superior investment returns with excellent client service at competitive prices.

Strategic positioning – what's the plan?
Regulatory and compliance burdens are driving up costs, at the same time investor and regulatory scrutiny are forcing fees lower. Managers need to ensure that investment products and related services are continuously updated to align with investors' wants and needs, and this forces firms to focus on their strategic positioning. Market leaders have already begun to position themselves through acquiring horizontally, vertically, or both across both product and distribution channels. With the low fee environment fast approaching, PwC advises managers to plan their future position carefully and critically evaluate their distribution and product strategies. Firms with a clear strategic positioning plan are more likely to succeed during the AWM revolution.

Transform through technology – or be eliminated
Advances such as artificial intelligence (AI), machine learning, data harvesting and processing and robotic process automation have begun to already have a significant impact. Firms who have yet to invest in these technologies will find themselves to be highly uncompetitive and many will be eliminated. There is potential for these technologies to create efficiencies and cut costs, particularly in the front office and in sales and service. Managers must embrace these developments and adopt an integrated platform that will make the insights from using AI, data and analytics actionable. Managers who have done so are optimising their business from front-to-back and are ready to face the new reality of lower revenues due to sustained fee pressure.

AWM – fight the battle for talent
Despite the pressures on profitability that are outlined in the report, investment in top talent is essential to ensure the ability to transform and drive success into the future. As technology becomes more central to the AWM industry, talent needs are changing. Managers will need to replace siloed working groups with integrated, multi-skilled teams in order to compete with other companies. These changes will come with costs, but will also provide value in the long run. Winning managers are offering diverse, inclusive, flexible and exciting careers with international programs, digital upskilling and internship initiatives. Laggards in this space risk an "analog death spiral" as they fall behind leaders, FinTech firms, and technology companies who attract top talent.

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Notes to editors:

Find the full report: https://www.pwc.com/gx/en/asset-management/asset-management-insights/assets/pwc-awm-revolution-pressure-on-profitability.pdf

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About the research
PwC analysed the evolution of management fees of over 100,000 funds globally and the annual reports of 64 asset managers globally with over $40 trillion assets under management as to evolution of revenues and expenses.
We gathered historical data from well-established, industry-standard sources, including Morningstar, Lipper, Hedge Fund Research and Preqin, along with PwC's proprietary resources.
We collected global insights across multiple regions (U.S., Europe, Asia-Pacific and the rest of the world) and across the major asset classes (equity, bonds, money market, multi-assets and alternatives).

We forecasted the fees for over 100 series using multiple econometric approaches. We analysed multivariate approaches, as well as time-series forecasting. Ultimately, we proceeded with a decomposition of the time-series components (trend, seasonality and residuals) and we forecasted them up to 2025. For this purpose, multiple models were tested, from the random walk with drift to the ETS family and ARIMA models. Finally, the model that was selected due to its outperformance and flexibility was exponential smoothing, namely the cubic smooth spline. Furthermore, we complemented the results of our model with a qualitative analysis based on discussions with PwC industry experts in order to provide an insightful depiction of the industry's future.

About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 158 countries with over 250,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com.