Top Trends to Watch in 2019

In 2019, global asset management wants to make an impact. Managers also seek bright spots in active investing and avenues for distribution.

Here, Cerulli analysts examine:

1. The global state of environmental, social, and governance (ESG) investing
2. Bright spots for active managers
3. Avenues for distribution

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1. ESG ARRIVES

GLOBALLY, ESG integration is amidst a reckoning beyond just the habitual flows coming from institutional investors. While wider-spread interest has ebbed and flowed, the collective chatter throughout global markets is now at its highest pitch. Asset managers are ramping up ESG product development, coinciding with an increasing proportion of wealth being passed onto younger generations. Artificial intelligence and greater access to data further the cause as firms can now better benchmark and analyze real-time ESG investment performance.

IN THE U.S., more firms view incorporating ESG/socially responsible investing (SRI) criteria into the investment process as a priority. The activity is now perceived to be at least somewhat of a driver for organizational change in the product team, according to 83% of large managers and 60% of medium and small asset managers.

IN U.S. RETAIL, advisors are more open to discussion but are still wary of the impact ESG allocations will have on overall portfolio performance. Broader ESG adoption in the retail space may instead come at the investor level through model platforms available through major wealth management firms.

IN EUROPE, three-quarters of the managers Cerulli surveyed do not believe that merely applying screening or exclusion criteria is sufficient to capitalize on investor demand for the integration of ESG factors. They believe that a more active approach is required. But ESG demand and the level of integration at the investment product level vary from country to country.

IN THE NORDICS, ESG integration is table stakes for many investors, rather than an add-on feature, with sustainability now mandated by new statutory requirements. Elsewhere in Europe, cross-border managers estimate that overall growth will be slower in countries such as Germany, Italy, and Spain.

IN ASIA, Australia and Japan have emerged as leaders in ESG investing, while Taiwan and Malaysia are making increasing efforts toward ESG adoption. Elsewhere, ESG investing has not picked up as much as some may have expected. Nevertheless, there are focused efforts from managers in this direction. The early signs of ESG adoption have come in two main forms—employing it as a part of the investment process, or having an ESG-themed product.

JAPAN has the largest share of SRI assets. Within the mutual fund space, Japan also accounts for the biggest proportion of assets under management (AUM) of products specifically labeled as ESG funds.

IN MALAYSIA, the Employees Provident Fund, one of the region's largest pension funds, provides a clear example of the overlap between Shariah and SRI strategies. Shariah investing is seen as a subset of ethical investing with an added filter on leverage, sustainability, and structure. The Malaysian Securities Commission (SC) also launched SRI fund guidelines in December 2017, covering a range of products, including mutual funds, ETFs, real estate investment trusts, and private equity.

2. BRIGHT SPOTS FOR ACTIVE MANAGERS

IN THE U.S., rising interest rates prop up a yield-starved market and pique the interest of investors looking for actively managed bond funds, a neglected space due to historically low rates. With much attention on the Fed's planned increases and the belief that equity values are cresting, fixed income represents a potential safe haven for active managers that have struggled to differentiate themselves during the nearly decade-long bull run.

U.S. ALTERNATIVE MARKETS see increased attention from product development teams as selective innovation is the name of the game for firms looking to diversify and grow their business, particularly through tech-driven retail platforms. In addition to liquid alts, multi-asset-class offerings look primed for a broader rally as firms recognize that objectives-based solutions once applied mainly to serve institutions can be leveraged in the retail space.

IN EUROPE, the mutual fund subadvisory space continues to be dominated by active management arrangements. Fund launch activity is particularly high in the U.K. and Italy. In the U.K., the majority of asset managers are likely to increase the amount of time they spend on client segments with higher profit margins and focus more on high-margin asset classes such as alternatives.

IN EUROPE institutional, manager consensus is that there will be a gradual shift back toward active strategies, with interest being driven by enhanced index, semi-active, and factor solutions.

IN ASIA, sustainable investing, smart beta, and quant models have made their way into several markets. Variations of multi-asset, all-weather solutions continue to pop up as a means of diversification and income generation. The search for alternative strategies could increase as investors chase yield and focus on diversification efforts amid volatility in public markets.

IN CHINA, fund management companies' subsidiaries refocus away from "channel business" toward actively managed funds and alternative investments (asset-backed securities, private equity, funds of funds) as they look to attract long-term pension and insurance business.

IN SOUTHEAST ASIA, most managers hold firm in their belief in the value of active investment strategies. Although institutions are investing in foreign-listed ETFs, commissions-driven distribution models help active management hold an edge.

IN LATIN AMERICA, even amidst a fair share of recent political drama, onshore mutual fund and pension industries stabilize as economic conditions improve and currencies stabilize. Investors are moving more money into longer-term mutual funds, hybrids, and multimarket funds in response to a strengthening equity market and lower interest rates—particularly in Brazil. Meanwhile, active managers' standing among pension funds is on the upswing.

3. AVENUES FOR DISTRIBUTION

IN THE U.S., with fees for some products now at zero, managers are figuring out new packaging mechanisms (e.g., digital platforms) in order to protect their distribution margins and perceived value. For many firms, scalability of asset allocation models and availability of underlying service components at low fees safeguard their place in an increasingly competitive distribution network.

IN EUROPE, multi-factor and low-volatility strategies remain the most popular options, but managers should be wary of overcrowding in the latter sector. Platforms and robo-advisors contribute to the growth of ETFs and Cerulli expects them to maintain their momentum, perhaps coming to fulfill a business-to-business function. Almost half of respondents to a Cerulli cross-border market survey expect robo-advice services offered by traditional advisors such as banks and independent financial advisors to have significant marketshare in the U.K. in five years; another one-third of respondents expect a similar dynamic across Continental Europe.

IN EUROPE, MiFID II has given the subadvisory market a boost. The subadvisory model is especially popular in the U.K., Switzerland, and Italy; it is less popular in Spain and Germany, where investors favor funds of funds. However, Cerulli expects subadvisory to gain traction in more European markets. European subadvised alternative assets increase significantly during the next five years in response to regulatory changes, the need for bespoke products, and heightened demand for specialist expertise.

IN CHINA, an expanding middle class and an increasing number of high-net-worth investors fuel robust asset growth and provide a massive distribution opportunity for asset managers. The Chinese government aims to liberalize the investment market through regulatory reform that should open the door for foreign fund managers. In addition, third-party online platforms show potential for growth.

IN SOUTHEAST ASIA, adoption of digital platforms remains nascent among banks and asset managers, although some headway is being made in Thailand, Indonesia, and the Philippines.

IN INDIA, online platforms and robo-advisors are increasing in number. Independent financial advisors will still be the channel to tap clients outside the top cities. But they would have to scale up their game with changing regulations and a digitalization drive.