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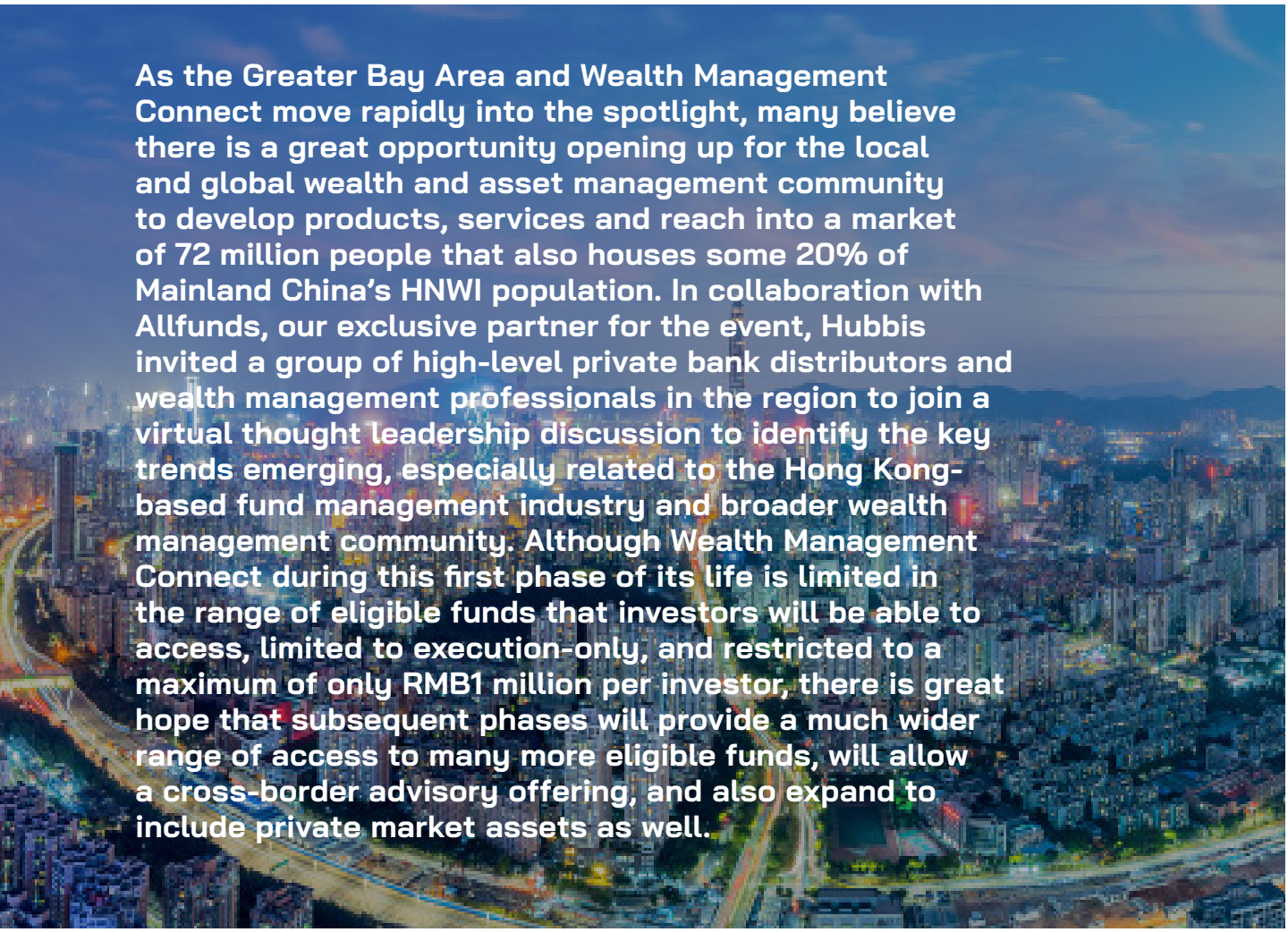
Capturing the Opportunities for Wealth Management Connectivity in the Greater Bay Area



As the Greater Bay Area and Wealth Management Connect move rapidly into the spotlight, many believe there is a great opportunity opening up for the local and global wealth and asset management community to develop products, services and reach into a market of 72 million people that also houses some 20% of Mainland China's HNWI population. In collaboration with Allfunds, our exclusive partner for the event, Hubbis invited a group of high-level private bank distributors and wealth management professionals in the region to join a virtual thought leadership discussion to identify the key trends emerging, especially related to the Hong Kong-based fund management industry and broader wealth management community. Although Wealth Management Connect during this first phase of its life is limited in the range of eligible funds that investors will be able to access, limited to execution-only, and restricted to a maximum of only RMB1 million per investor, there is great hope that subsequent phases will provide a much wider range of access to many more eligible funds, will allow a cross-border advisory offering, and also expand to include private market assets as well.

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The Key Observations in Brief

Wealth Management Connect opens the door to the riches of the Greater Bay Area

Wealth Management Connect (WMC) will allow Hong Kong and Macau residents to buy mainland investment products sold by banks in the Greater Bay Area (GBA), and on the other hand, people in the nine major Guangdong cities will also be allowed to buy investment products sold by banks in Hong Kong and Macau. The Greater Bay Area, or GBA, has a population of around 72 million, and boasts a GDP equivalent to USD1.6 trillion, which places it amongst the top 12 economies of the world. The High-Net-Worth Investor (HNWI) population in the GBA represents more than 20% of the total in Mainland China and is one of the fastest growing anywhere in the world.

WMC will be limited in scope and access for now but should expand over time

This is the first cross border trading scheme to focus on the Greater Bay Area and will be limited to total fund flows of RMB300 billion, roughly USD46.5 billion. It will start modestly and then should expand in several phases. For now, individual investors can only sign up with one bank in their country, and that bank will partner with a bank across the border.

Mass affluent investors are the first key targets for WMC

For the time being, the scale of investment allowed means the focus in on the mass affluent market. The 'southbound' route of the WMC initiative will focus on Mainland China investors who will be allowed to make investments in eligible Hong Kong funds. And as to northbound investments, residents of Hong Kong and Macau will be able to invest in Mainland China through local banks partnering with Mainland banks. There will likely be a quota limit of RMB1 million (roughly USD155,000) per person.

The door to the world of Chinese investors is thus far only creaking open

The mutual fund industry in China is already enormously successful, already the second-largest in the world. The mutual fund industry there, according to one expert on the pane, has grown to USD3.5 trillion equivalent at the end of May, or roughly double where it was three years ago. A tiny percentage of these flows ending up targeting global assets through Hong Kong funds would be an immense leap forward.

For the time being, it is the banks that cater to the retail/mass affluent markets that will most benefit

The WMC regime is execution-only for the time being, and only licensed banks can participate on both sides of the southbound and northbound flows. For southbound flows, investors can buy only

mid- to low-risk Hong Kong domiciled and Hong Kong SFC authorised funds, with risk ratings from 1 to 3. Of the roughly 800 SFC authorised funds in Hong Kong, the final list under these criteria might be as few as 60-80 eligible funds and does not include the European-domiciled UCITs funds, as the aim is to boost the domestic fund management industry.

The global funds sector in Hong Kong is, at least for now, in more of a wait and watch mode

Leading global asset managers are mostly waiting and watching, according to experts in the discussion. While Mainland China investors will want to access global assets through WMC eligible Hong Kong funds, until the eligible range of risk and assets, those leading fund managers are mostly eyeing the second and third phases, when, they hope, the investment size, as well as the risk and asset criteria for eligible funds will be significantly widened. As to northbound investments, the same low to medium risk criteria apply.

Amongst some sceptics, considerable doubts remain as to the merits of the WMC regime

There is genuine scepticism in some quarters as to whether WMC as it stands in Phase I really moves things forward, given Stock Connect already in place, because of the well-established Mutual Recognition of Funds (MRF) regime and others emerging. Some believe this is simply a means to inflate the roles of key banks.

The traditional private banking community is also adopting a wait and see approach

The private banks attending the discussion all indicated that although they see China as a market of incredible potential for the future, WMC as it will be initially, does not offer them many opportunities in their core HNW and UHNW segments. However, for those private banks with a strong retail banking operation in the group, there is more potential for participation. A key deterrent to the mainstream wealth industry is that as WMC offers execution-only, there is no room to differentiate themselves with their core advisory propositions.

Those banks wanting to play in Phase I are already jostling for position

For those banks keen to participate from the outset, they see some key areas of marketing their offerings. These include offering not advice but content such as house and investments views, offering the best possible platform and ease of access, and offering some sign-on discounts or sweeteners, as the clients will be choosing just one preferred banking partner. One banker, for example, explained that they see this as a long-term process, so they want to sign up as many clients early on, in anticipation of a much broader and robust WMC regime in the future.

The wealth industry in Hong Kong mostly sees this as a glass half full scenario

The experts in attendance seemed to agree that given the initial size and scope of WMC, but also looking to the immense potential ahead, they should all see this as a largely positive situation – the glass half full – and then work to lobby the regulators and authorities to expand the eligible investment limits, the range of risks available, and the types of assets that can be included – for example, insurance, derivatives, private markets opportunities.

It is vital to understand the realities and the 'politics' and to see the big picture

An expert observed that the difficulty of licensing for cross-border advisory is entirely understandable but that the wealth industry is working with the regulators to encourage this and to propose ways in which this will be facilitated in the future. Again, patience and a longer-term perspective on the opportunities ahead are vital to the right strategy and psychology.

The development of cross-border investment within the Greater Bay Area

The Greater Bay Area, or GBA, has a population of around 72 million and is, therefore, bigger than all European countries except Germany. There is a Gross Domestic Product (GDP) across the GBA region that exceeds that of California, making it equivalent to one of the top 12 economies in the world. The High Net Worth Investor (HNWI) population in the GBA exceeds 280,000 families, which represents more than 20% of the total in Mainland China, and is one of the fastest-growing anywhere in the world. Many of them look to Hong Kong for guidance on where to invest money outside Mainland China.

We now have Wealth Management Connect (WMC), which was officially launched on 29 June 2020, and will be rolled out in phases. This is important because the door to invest via Hong Kong has been widened beyond the HNWI population to include anyone in the GBA with sufficient assets. This means that people throughout the GBA will be able to go to their local bank and make investments via Hong Kong mutual funds into their preferred securities markets worldwide.

While in the initial stages, there will likely be a quota limit of RMB1m (roughly USD155,000) per person, with an aggregate of around RMB150bn (USD23.2bn) in each direction, this development must be considered one of the best opportunities anywhere for the global fund management industry.

A phased rollout

A guest who has more than three decades of experience working with local and global fund managers, some in Hong Kong, some across the world, offered his views on the implications of WMC. "Unfortunately, apart from banks, everybody else is being excluded for the moment but they'll probably be allowed to participate at some later stage," he reported. "We have to look forward to multiple phases, and the Chinese regulators like to see things in phases."

He remarked that the Mutual Recognition of Funds (MRF) scheme, started exactly six years ago, was designed to enabling funds from Hong Kong to be sold cross border, the first time anything like that had happened between Hong Kong and China. "But MRF had multiple impediments and faults, and the regulators told us they knew but wait for phase II and phase III, and six years later, we are still on phase I. This is a scenario we all want to avoid with regard to WMC."

What exactly is WMC?

This same expert explained that WMC is a scheme whereby residents within the GBA are able to buy mutual funds, bank deposits and certain types of bonds across the borders through their bank. This, he said, means those residents will be able to buy mutual funds in Hong Kong, and people in Hong Kong could be buying mutual funds in China.

Not that many Hong Kong funds are eligible

Aside from a maximum limit of 1 million Renminbi, about USD155,000 per individual account holder, the other key restriction is that the funds permitted are only Hong Kong domiciled funds

and Hong Kong SFC authorised funds. They will also have to be classified risk rating of 1 to 3, in other words, low to medium risk at the maximum.

He reported that there are roughly 800 funds in Hong Kong authorised by the SFC that are Hong Kong domiciled, but that excluding those not allowable such as ETFs and others, the number whittles down to roughly 60 to 80 possible funds that could be eligible.

Locally domiciled funds required to help boost the local market

He also added that the UCIT structure for funds had been dominating Hong Kong for decades, with UCIT funds domiciled in Dublin or Luxembourg representing perhaps 80% of all fund sales in Hong Kong.

"But no UCIT funds in existence today all eligible for WMC," he reported. "Accordingly, many of the global fund houses continue to try to lobby in favour of getting UCITs products into this, but they are going to fail because there is no interest on the part of either the Hong Kong Monetary Authority, or the PBOC in China, to allow product from Luxembourg and Dublin to participate because the purpose of these types of schemes like WMC is to enhance the domestic fund management industry in Hong Kong or in China."

The Hong Kong funds industry has been dragging its feet

This guest also remarked on the slow preparation of the Hong Kong funds industry, noting that in his conversations with leading global asset managers, they report they are waiting for others to move first. "They all said pretty much the same, that they are waiting and watching, which is a somewhat poor reflection of the way the fund industry is operating at the moment – someone else needs to go first."

He also observed how of the 60-80 potentially eligible funds, quite a number are invested in Mainland China securities, but understandably Mainland investors will want to come to use Hong Kong authorised funds to buy into their home markets.

"The Mainland Chinese investor would want to use Hong Kong funds to buy into the rest of the world," he said. "And a very recent survey that has been done on behalf of the Hong Kong Investment Funds Association has shown that, in fact, a lot of the people in the GBA are interested in Hong Kong equities, US equities, and other global equities."

The wealth industry will rise to the occasion

He added that the wealth management industry is clearly going to be looking at this opportunity with keen interest. "The banks have the first bite and the requirement that is being set down by the Hong Kong Monetary Authority and the PBOC, both of whom are the lead signatories, regulators and drivers of this development, is to get it up and running efficiently, and later bring out phase II ," he reported.

He added that he had heard from multiple other interested parties, both in the mainland and in Hong Kong, about their lobbying efforts to participate, for example, private

banks, wealth managers in Hong Kong, insurance companies in Hong Kong, and in China from investment advisory license holders, from wealth managers, and insurers, and securities companies, all of which are really very active in the mutual fund business in China.

China – the giant has already awoken

He also remarked that the mutual fund industry in China is already enormously successful, already the second-largest in the world, and perhaps in terms of numbers of investors the largest, with an estimated 200 million people or more having bought a mutual fund representing equities or other securities, with another roughly 400 million having already bought into money market funds. "What we can see is a truly vast amount of interest, with the mutual fund industry there growing to USD3.5 trillion equivalent at the end of May, or roughly double where it was three years ago."

He concluded that the demand is clearly there, and potentially vast. And once WMC is running efficiently, it will open the door to more financial sector participants, possibly an increased limited per investor, and potentially the rollout of insurance products and potentially higher risk products in the future."

Execution-only, at least for now

And he added that the role of the banks in the front line is to provide an execution-only basis of service. For example, a resident in Guangdong will through a local bank be introduced to a bank in Hong Kong, perhaps part of the same group or a correspondent bank, and through those banks will be able to purchase the eligible funds. "They can do that online, with no advice offered, just choosing from a list of the funds available, or when travel is permitted, they can go to Hong Kong and potentially talk through options with an advisor there, but for now, that is clearly not available."

Some think WMC might be less of a game-changer

Another China expert based in Hong Kong reported that there is a question mark as to whether WMC, as it is initially, actually moves things forward. On the surface, he commented, it seems a little bit redundant because of Stock Connect already in place, because of the well-established MRF, and then there is Bond Connect and very soon IPO Connect, and ETF Connect.

"Why then would you even need WMC?" he pondered. "Well, if we scratch below the surface, we can see that WMC is actually, we think, a way to bring all the commercial banks into the flows of these cross-border wealth flows. As we see it, WMC, in our humble view, is for the use of a cross-border mechanism to sell OTC products, probably without the same liquidity, transparency, and even risk mitigation as the liquid investments. And if we scratch even harder, we see that WMC was meant to look after just a few specific banks; I don't need to mention names here. That is our in-house analysis."

Watching, waiting, hoping

The Asian head of a private European bank said that they

too are waiting and watching, although their sister company, a major European asset management group, seem to be looking more closely at it. "China at this moment is about 10% of our business," he reported. "We want to expand that, and we are interested to learn what similar size competitors are doing to achieve that."

This sentiment was echoed by the Asian CEO of another European private bank. "Greater China has been our fastest-growing market over the last five years, and I fully expect it to be our fastest growing market for the next five years as well," he reported. "The whole GBA is of great interest to us, especially with such close links to Hong Kong, but right now we are not yet entirely clear on how we will participate in [WMC] and details are only recently flowing through."

He explained their bank's targets were especially UHNWIs looking to establish business operations in Hong Kong, in Singapore, in Europe and elsewhere, and who are looking for international wealth management services. "We still operate on the basis that the reason people come to us fundamentally is their relationship manager; I think that is some 60% or 70% of that decision," he explained.

And he added that the bank has a joint venture asset management business in Shanghai, which he described as dipping their toes in the water of the mainland market, but said that at this time, it does not make sense for a private bank of their size to be onshore from a wealth management perspective, because the competition from domestic players is so strong. "As things stand at the moment, I think our principal proposition will remain an international one," he reported.

Why this matters to leading Hong Kong banks

A senior representative of a local Hong Kong bank then explained that the GBA is of great importance to the bank. "We have a very extensive branch network, both in Hong Kong as well as in the GBA to leverage, so aside from the Chinese state-owned banks, we have actually one of the largest branch networks in China, which put us to an advantage when it comes to gearing up for the GBA's WMC, which we see as one of the most important, possibly the most important project, that the bank is currently working on"

With only a limited choice of funds, differentiation against the competition is tough

He reported that in terms of the funds the bank offers and that are eligible for WMC, they number 40 or below and he commented that there is really not much difference between what the banks can each offer at this stage.

"How then do you differentiate when the products are so homogenous among the different banks?" he pondered. "Well, from our perspective, there are three areas where we'll be able to differentiate versus other competitors, and the first would be the availability of content."

The differentiation factors

He elaborated on that, explaining that for the retail clients who are banking through WMC, they may not be the wealthiest but are wealthy enough to probably already have offshore assets, and

want to obtain more international perspective and exposure. "Therefore, the availability of content such as house views, investment views, and things like that will be one differentiating factor," he reported.

The second factor of differentiation will be the platform because WMC is at first execution-only, so the ease by which the clients can place orders through the platform will be essential. "We have been making significant investments to improve the way we help our clients execute trades," he reported.

Sweetening the offering to capture the customers

And the final, perhaps most important differentiating factor will be the discounts or the sweeteners that they offer to the clients to open up WMC accounts. "These clients will have one shot at choosing their preferred banking partner, which means that the competition to onboard the clients will be very fierce from the start because the clients only get to have one choice at least initially. Accordingly, as we understand it, all the banks, as far as I understand things, will be focusing mostly on what type of deal sweeteners they will be able to offer the clients, what type of discounts and what are some of the coupons or cash rewards to offer to win them over."

He explained that like all the banks, they are trying to play the long game and have been lobbying the governments both in China as well as in Hong Kong to open up the availability of products to include higher risk funds, link deposit type of products, even potentially derivatives and private equity.

"The regulators all tell us that this will come eventually, and that goes back to the earlier comments on the phases," he commented. "In short, it won't happen for at least one or two years, so for now, we can focus on the three factors of differentiation."

Will the product availability expand? Yes, but probably not anytime soon.

He added that from the bank's discussions with fund managers, he is not hopeful they will in the foreseeable future create new products for WMC, as they expect phase I to be quite transitory, and many are trying to play the longer-term game. "They say, for example, they are preparing more for WMC opening up, and looking at more thematic funds, at higher risk funds, more international funds, and so forth. We hear from several large fund houses that they are in the process of setting up these new fund vehicles in anticipation."

Don't forget the northbound investor traffic

Another guest, a European private banker, remarked on the flow of investment that will emanate from Hong Kong heading north into the mainland. "If you think about how the Chinese equity and securities markets in general have been opening up and becoming more and more attractive in terms of returns, the managers there are actually becoming more and more sophisticated and are maturing," he observed. "So, how we access that through our onshore network of partners, to access these local Chinese fund managers will be quite key for international banks like us."

Seeing the big picture and playing the waiting game

Another expert guest reported that his organisation had been lobbying actively for a robust version of WMC since before even the first version was announced, going back to efforts made in this regard along with a leading global accounting major back in 2018. He reported that they could predict there would be complications involving the issue of licensing and regulatory jurisdiction and predicted that the authorities would need to address this in the future, but their approach was not to necessarily propose solutions but to flag that in a thought leadership report.

He said they were pleased to see WMC emerge, even though it is quite a bit different from what they had originally lobbied for and envisioned. "We understand that for various reasons, including I think, for optics and political reasons, it makes sense to launch a scheme which is not directly seen as benefiting the wealthier classes before you do something that addresses the mass affluent," he commented. "And therefore, I think it makes perfect sense that they would have kept the quota at this level of 1 million RMB."

Too small and too limited for now, but hopes for expansion ahead

However, he said that the private wealth management sector is clearly less interested in onboarding clients for just RMB1 million of investment per client, and also because they are then limited to execution-only trades. This, he noted, means the private wealth management sector cannot express its key USP of providing advice and becoming trusted advisors to those clients.

He explained that they understand that licensing for cross-border advisory is always going to be extremely complicated. "The authorities clearly just decided to punt that down the road," he said. "They don't want to deal with it right now, and they just want to get this going. And since it's going to be executed only, it makes sense that they would limit this to medium risk or lower products."

He said people might argue a list with no advice available is already the wrong approach, but the dangers are mitigated by those funds all being moderate to low-risk products at the outset.

The glass is half full, and the ball is set in motion

"In short, we see the glass as half full, and to move ahead to Phase II , we can all help the authorities, so our strategy is to concentrate on some thought leadership that we hope will come up with concrete suggestions on how to address these key problems," he reported, "especially on dual licensing or cross-licensing, regulating advisors from one jurisdiction providing advice to clients in another jurisdiction, and risk management. From our experience in the past, the authorities are actually looking for these types of ideas and answers. And risk management is going to be key; they certainly don't want scandals of miss-selling or other major issues."

He also observed that all solutions must recognise the two-way flows; it cannot be simply applying Hong

Kong regulations and practices, as that would not be politically acceptable. "It is really not that relevant to the private wealth community in Hong Kong at this time, unless they have a retail wealth management arm, but they are all keen to see what happens in Phases II and III," he concluded. He explained that, for time being, he and his colleagues and partners continue to focus on boosting Hong Kong as a funds centre and improving the incentives and wider appeals of Hong Kong as a family office hub.

Will WMC open up later to private market assets?

Another guest remarked that there has been significant growth in demand from Chinese investors in private equity and other private assets and expressed some hope that WMC would later encompass such assets. For the moment, he said they are focusing on WMC as it is, working through their strong network on the retail banking side, and see this as a positive with some good tailwinds and an important development for them in the private bank linking through the retail operations in the group.

And one expert confirmed the rising demand for private assets in China, noting that this will be an increasingly important differentiator for private banking players. "We are relatively new in private banking in Hong Kong," he reported, "but we see WMC as part of the broader GBA connectivity, and we see that there is an increased interconnection between China, Hong Kong and Macau." He added that they are not a banking entity in Hong Kong, so not a direct beneficiary of WMC, but that this fits with the broader trend of more European investor buying into Mainland China, and vice versa for Mainland China investors buying international assets, including private market assets.

WMC – perhaps not a game-changer today, but it does offer great potential

The discussion closed with a widespread acknowledgement of the importance of the GBA and the WMC. Although recognising that the potential for the mainstream Hong Kong wealth management providers is limited and also recognising that the appeals for the global funds industry are modest in the early phase of WMC, there was a broad consensus that this is another important milestone in the opening of the Chinese investments markets for cross-border flows and that everyone should watch developments carefully and help encourage authorities to expand the regime as rapidly as possible for both southbound and northbound investment flows. ■

WMC AND ALLFUNDS – POSITIONING THE PLATFORM FOR THE FUTURE

Allfunds is today the world's largest institutional fund distribution network, describing itself on its website as a global marketplace where distributors and asset owners from over 60 countries can reach world-class financial fund groups. David Perez de Albeniz, the Singapore-based Head of Asia for Allfunds, has in past interviews with Hubbis explained in some detail how Allfunds continues to develop its core platform and its premium services, highlighting how demand for the Allfunds outsourced, digital funds marketplace has been growing apace in recent years in Asia, driven by the demand for greater efficiency, by Allfunds' ability to filter best-in-class products, by the ease of use and access, and of course, the resultant cost reductions achieved for distributors and fund creators.

Today, Allfunds offers the largest funds distribution platform worldwide for mutual funds and ETFs, with over EUR1.3 trillion of assets under administration, and access to 2,000 fund providers, 180,000 funds and agreements in place with over 790 distributors. In 2020, Allfunds processed some 10 million trades, all automatically and with no manual intervention.

For Perez, the Allfunds' USP is essentially derived from helping financial institutions the world over to scale up their business without increasing their infrastructure and costs. With its open architecture,

Perez says "the Allfunds platform does not favour any funds or any providers; instead, it targets best of breed solutions for end-customers and delivered at a lower cost and considerably greater ease and speed. And of course, Allfunds is entirely independent with no proprietary funds and no conflict of interests."

As an exclusive partner for the June 23 thought leadership event, Perez offered some brief insights into how they are positioning the platform for WMC and other related developments.

"We were amongst the first to get excited by WMC, and the opportunity to connect fund buyers with Hong Kong based fund sellers with straight-through processing, and with a distribution agreement overlay, and then add a lot of other services around that," he told fellow wealth management experts in attendance. "We have worked on agreements with the managers of the funds for some years – and everyone knows how long an agreement with a fund manager can take to sign - so, we're in a good position now, covering some 90% of what's going to be available [under WMC] at the outset. And frankly, everyone is looking to the longer-term, not only at these initial products."

Perez told delegates in the discussion on June 23 that when Allfunds signs an agreement, it covers all of the products, and all of the sub-funds, meaning that Allfunds is well placed at the table for the future so that when distributors or execution-only players need to access any of these products, they can be accessing them through Allfunds. "I think that gives us an edge vis-à-vis the other platforms," he explained.

He elaborated on these comments, noting that as to the edge any platform can provide, Allfunds has worked diligently to put in place the whole suite of connectivity methods, including APIs, that can enrich the end clients' journeys, for example, content. More importantly, Allfunds is now providing a whole suite of digital solutions, including the development of apps and the design and hosting of fund portals which can include all the necessary static and dynamic data, portfolio management tools, robo-advice, etc.

"All fund managers can publish all the content that they like on the platform through us," he explained. "I continue to think that this [WMC] is probably going to be a great opportunity, maybe not in the very short term, but we will position ourselves to facilitate customers to play it in the longer-term. For the moment, we are investing for that future, and not only fill the shelf with products, but also try to convince as many distributors as we can about the merits of the Greater Bay Area, and we are seeing positive results from that, giving us a network effect, which I hope will benefit all parties in the future."

He also reported that confronted by tough competition, a key differentiation for Allfunds is the remarkable ease of access to the platform. "For Allfunds to help those distributors, especially big banks, to upgrade systems, and also use the online platforms for easy and efficient access to the online dealing system, to build customer satisfaction, these are vital measures," he explained.

In December last year, as an example of the progress and drive Allfunds is making, the platform announced that it had been selected by China Merchants Bank (CMB) Group as its B2B investment fund platform partner, becoming the provider of access to third-party funds for its all overseas private wealth and private banking centres, especially in the Hong Kong and Singapore markets.

In essence, Perez told the experts at the recent discussion, Allfunds wants to be in a position to also help clients onshore in China, including possibly through creating a QFII avenue into the Chinese fund managers that they are signing up and allowing offshore investors to channel money into China that way as well. "That's part of the grand plan, and exciting days are ahead, we believe," he concluded.