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The Future of Funds Distribution in Hong Kong and the Growing Influence of Digital

Hubbis and our exclusive partner for the event, Allfunds, on October 25 hosted a highly informative and thought-provoking one-hour thought leadership webinar on the evolution of funds distribution in the Hong Kong market and the evolution of the digital curation and delivery model. In attendance at this private, by-invitation event were senior delegates from the wealth & asset management industry from across the region. A small panel of experts, all leaders in the wealth & asset management industry, debated issues such as the key opportunities and challenges faced by Hong Kong distributors and asset managers, whether more fund distributors are moving or considering moving to digital platforms and the accordant benefits, the flight path of the industry viewed from a more mature market perspective such as Europe, the additional value-added that fund platforms can provide the wealth industry, and whether the Great Bay Area and Wealth Management Connect initiatives are likely to be game-changers ahead. The panellists' comments were off the record, although we have presented some of the Allfunds observations as attributable in this briefing below.

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INTRODUCTORY WORDS FROM ALLFUNDS

- Sebastien Chaker, Head of Hong Kong, Allfunds: Thank you sincerely for attending this discussion, it is really important for us to discuss these topics in a private forum such as this with wealth industry leaders and decision-makers contributing.
- As head of Hong Kong my priorities for the next 12 to 18 months for Hong Kong and the Greater China area centre on growth in terms of asset owners joining the platform and fund houses, and particularly on the Hong Kong fund houses where there is strong demand right now. The more we are able to connect buyers and sellers of mutual funds on the platform, the more we can bring value to our community of clients, so that is priority number one.
- The second priority is around innovation, and more particularly around locally-driven innovation. This is a global platform, and it's a global business model, which brings the benefit of scale to our customers here in the region. But we do also recognise that Hong Kong and, more broadly, Greater China are unique markets, and they are characterised by tremendous growth, a fast-changing distribution landscape, more Chinese influence in the business, and more Chinese money. And here, we find probably one of the most stringent regulatory frameworks around funds distribution. In short, is it essential for us to understand the clients and market here and then deliver tailor-made solutions and the optimal outcomes for them.
- The third priority centres on strategic engagement with our key clients in the region. Our platform model is relatively new for Asia, and as for every new model, it brings opportunities, but it also brings some challenges. We are somehow disrupting the way fund distributors and fund managers have conducted their business in the region for the last 20 or 30 years, and accordingly, it is absolutely key to maintain an open and active dialogue with our clients to understand and try to solve their challenges and ensure that they all get the most value from our services.
- David Pérez de Albéniz, Regional Manager Asia, Allfunds: I second all of those comments and want to add that Asia is remarkably important for Allfunds. We listed back in April, and since then, Asia is one of the key topics of interest for our investors and shareholders. How are we doing in Asia? What are our plans, and what strategies do we have? Well, I can state that we are totally committed to the region, we offer open architecture, and we are eager to work with the industry, with our clients to develop the best approaches, services and uptake. So, we look forward to this exchange of ideas and insights and will always do our best to refine our platform and our features to the needs of this dynamic market.

The Key Insights & Observations

Automation of funds curation is here to stay

Boosting the range of funds available online, improving their selection, conducting due diligence in advance that allows those funds onto the platforms, helping client intermediaries with digital access and seamless transacting, and ensuring s seamless and 'pleasant' user experience are all key to the future for the wealth management industry. Aligning these features with the right type of ongoing information flows, data/statistics and reporting tools then further enhance these platforms' offerings.

The penetration of funds of all types is increasing apace across Asia

A leading private banker reported how funds penetration was rising fast from their viewpoint, now accounting for some 17% of their bank's AUM, comfortably a historical high. With retrocession fees still the norm in Asia, this represents good business, he remarked, especially as the wealth industry seeks to achieve more balanced revenues, adding that if the bank's DPM mandates are also included, the fund penetration figure would be even higher. He reported their fund selection teams had been expanding in both Hong Kong and Singapore as a result.

The quality and transparency of many active and passive funds have improved

An expert highlighted how the quality and integrity, and transparency of many active and passive funds had improved in recent years. The active manager funds industry has had to work harder to prove their worth amidst widely rising mainstream asset prices. Both the active and the passive funds have had to become more diverse, allowing more investors to express their rising inclination towards thematic investing, the core-satellite portfolio approach and of course ESG-driven strategies.

Asia is gradually emulating the European model where more and more wealth managers work with the platforms

The representative of a leading brand name asset management institution explained that from his experience of working in Europe, the wealth industry had really embraced the digital platforms, and there had been an 'explosion' of cooperation there of the larger wealth managers working with platforms such as Allfunds for their daily funds business. He expected this trend to expand in Asia, including in the nascent Chinese market. He explained how his distribution team in Asia works strategically with platforms to streamline and broaden the distribution of their funds in the region.

The investment allocations of Asian investors have been evolving apace

The experts highlighted how the demand for a more diverse and higher quality range of active or passive funds had increased as wealthy Asian investors had adopted more sophisticated portfolio allocation strategies and also as lower returns on fixed-income investments - that Asian buyers have long loved - had fallen, driving the need for diversification in the hunt for yield and overall returns.

The next phases of development should be very interesting and exciting

The connectivity between the wealth industry and the platforms has been improving all the time, with the platforms continuously steering their ships towards the data, analytics and other features the banks and other wealth providers want. This two-way flow of ideas and imagination will further boost the advantages the platforms can offer. Aggregation of a broader array of data is one area, using AI and ML, and all with the ultimate aim of boosting relevance and outcomes for the end clients, from the mass affluent to the UHNW investors.

The platforms also help drive the democratisation of wealth management

While the core focus of the speakers and guests at the event was on the HNW and UHNW markets in Asia, the mass affluent market is of course vast and for the wealth industry to boost scale, and help with the democratisation of the world of investments, working closely with these platforms is immensely helpful. Many of the mass affluent investors will also go on to become HNWIs or even wealthier.

The Mainland China funds business is an immense opportunity to be grasped

Although it is a tough business for international players, including the platforms, to access, compete in and indeed make money in, the onshore funds business in China is replete with vast potential, as private wealth escalates, and as more and more investors plan more effectively for their futures. The arrival of approvals for 100% foreign-owned asset management companies is likely to gradually help further professionalise and diversify the domestic funds industry.

More domestic Chinese asset managers see the benefits of the platforms

The representative of one of China's oldest asset managers explained why his firm has teamed up with Allfunds for distribution of their funds, and why that also helps them access international investors from EMEA countries, a key target for the future and one already yielding plenty of new sources of money for their firm. The relationship clearly helps the sellers and distributors access Mainland China asset managers without all the hurdles and difficulties of conducting their own due diligence, he reported.

The arrival of Wealth Management Connect will open up a more active two-way flow as well

The Hong Kong funds business is already remarkably active, a guest reported, adding that the Wealth Management Connect and the opening of the Greater Bay Area will further boost volumes, as WMC will help develop a more interactive flow of investors and opportunities in the region, including of course many wealthy Chinese from the Mainland provinces included in the GBA. The goal of course is to capture both sides, the money flowing into the region, and also through the GBA and WMC the money flowing within the region.

Retail access and digital solutions

The representative of a local and substantial Hong Kong bank with an extensive retail network on the Mainland, and further afield in Asia said that he was sure the distribution of funds is going to be much more automated going forward. "We see a lot of the retail banks producing robo-advisory, or automated advisory type tools for clients to tap into the mutual funds market in a more intelligent manner and a more informed fashion, and therefore digital tools to access those funds will be increasingly important, including for Wealth Management Connect (WMC), which will commence as execution-only. The ability to offer a platform with detailed statistics relevant to the clients will be very important to distribute funds to retail and to wealthy individuals."

Rising the ESG wave

Another trend he noted is for the curation of more ESG funds. "We certainly see more and more interest from clients, both from the mainland and Hong Kong, in ESG-driven strategies," he explained. "People are increasingly viewing ESG not as a fad, but as a means to improved returns and enhanced risk mitigation. Accordingly, we are definitely putting a lot more emphasis in offering relevant ESG solutions to clients."

Funds penetration rising sharply in Asia

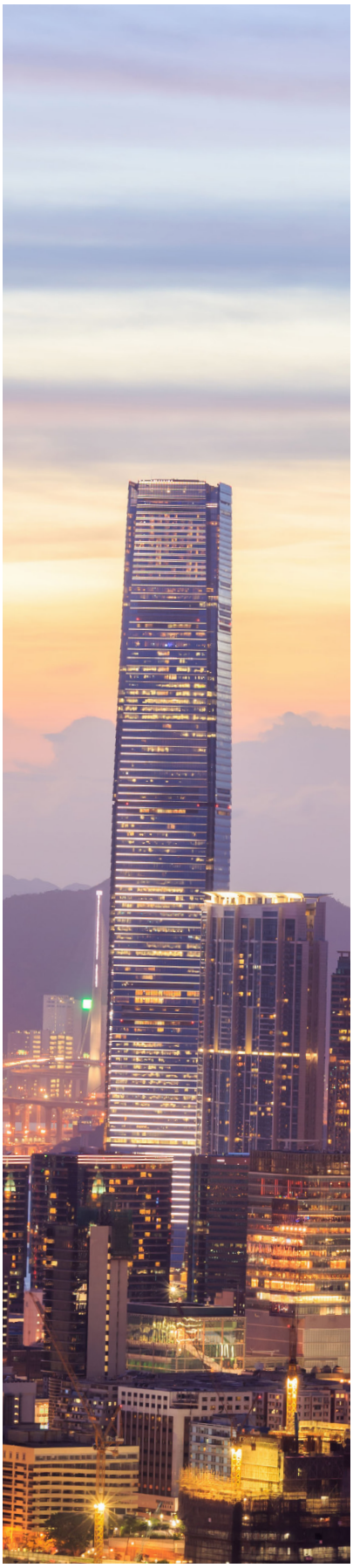
A private bank head then reported that from their perspective, fund penetration had increased "quite dramatically" over the past four years and now stands at 17% of AUM, a historic high. "Obviously, all private banks have been looking at ways to make our income less volatile and less dependent on trading income only, which is very dependent on market shifts, and with retrocession fees still in place in Asia, from a bank point of view, this is important revenue," he reported. "But I also think the quality of many funds has evolved quite positively actually, so it is even more important for clients and us. We are also doing more reporting for clients, especially on the ESG side, and actually expanding our fund team in Singapore and Hong Kong. Same story in Europe."

He explained that this 17% figure does not include their DPM mandates, which represent around 10% of AUM compared with an estimated 9% for the industry. "Our funds activity centres on 41 different external asset managers at this time," he reported.

China's funds business at an interesting point in their development

A medium-sized wealth manager centred in China but also operating offshore explained that they had delivered around USD12 billion of all types of funds to roughly 100,000 HNW clients onshore and offshore in the year recently ended. In the offshore space, he explained they focus on Cayman-listed funds. But the China onshore fund distribution business is tough, he observed, with competitions such that many banks and firms are losing money when they sell funds.

"China is ok to some extent to see some wealth flow into the offshore space, and clearly, with China's economic growth and political intent somewhat in question and the market entering a period of uncertainty, I would say that domestic clients are nowadays more



open to offshore funds. Another second trend is the emergence of ETF demand, not just onshore ETFs, but also offshore ETFs, to help investors to participate in particular trends, themes or sectors or subsectors. And the third trend, which has been ongoing for some years, is Chinese managers entering the alternative space in the offshore assets universe."

Great opportunities on the Mainland

Another banker on the asset management side of a major global brand name focused his views first on China, noting that they were on tenterhooks waiting for final approvals for a 100% owned onshore asset management operation, evolving from the JV operation they had had for quite some years. He explained that they were currently aiming to fill any asset class gaps that exist in the funds offering onshore, making sure they strike a balance with core asset classes as well to mitigate the potential of imbalances caused by more recent investment trends that might not endure.

"We are looking at a product pipeline for China through that lens, to make sure we address the product opportunity for the next 12 months, rather than necessarily three to five years, but also thinking through that multi-dimension of time," he said. "Naturally, we want to play in the core asset class space, to have relevance to our wealth management partners, including our own private bank, among others."

The representative of a leading Chinese domestic asset management company offered his insights, noting that their firm is one of the 10 oldest fund managers in the country. He works in Hong Kong and the mission is to expand the business beyond China, not only in Hong Kong but much more globally as well. He explained they had from Hong Kong launched Cayman-based hedge funds in 2015 and then their first Luxembourg UCIT platforms back in September 2016.

China's asset managers - connectivity through the platforms

"We soon became one of the very early Chinese asset managers to sign up with Allfunds and have our funds distributed on the platform, and we now know the team in the region really quite well. We focus on only Chinese liquid asset classes, so Chinese equities and bonds. We began with only one UCIT fund, the Chinese small midcap growth fund, and it has been growing very well and is now standing at a very large number. We are looking globally, especially EMEA, with some distribution routed through Allfunds, and also other distributors. Our collaboration with Allfunds is not only here in Hong Kong, but also some part in Singapore, and actually quite a bit of business from different parts of Europe, and even in the Middle East as well. This means we have been able to build a global relationship with Allfunds. We are happy with the results, and we have launched the second fund, and this hopefully will replicate the success on the fundraising front. We plan to have a long-term partnership with Allfunds."

Building a brand and presence overseas

He added that their mission is to focus on China and expressed

through UCITs. "We only maybe have a good reputation in China but outside of China nobody knows us," he reported. "The only asset class we can offer is Chinese assets, and we can add value, delivering very good alpha and great performance. We have spent now six years roughly building up our brand awareness in the EMEA region and we were grateful to sign with Allfunds, even with only one fund to offer at the time, whereas most platforms need more funds available from the creator. Being with Allfunds saves a lot of time for the sellers and distributors who would normally need to do the due diligence yearly, but that is taken care of."

Here comes WMC

The discussion naturally turned to Wealth Management Connect, with a contributor noting how buoyant the Hong Kong funds business is currently and that with WMC creating an urgent need for adding HK funds to their own platforms, there was of logjam being created. "The situation has created a constraint on the fund houses and vice versa," he remarked, "and you have a lot of new distributors that are coming onboard, launching wealth management initiatives and creating even more constraints on the fund houses here."

Another expert agreed, remarking that the upside potentially was a huge volume of funds flowing from the Mainland. "But with this volume will come more competitors, who have the branding and who are well-known and embraced by those clients in China, so we are seeing a closed loop, with Mainland China money coming to buy funds managed by international managers which are Hong Kong domiciled."

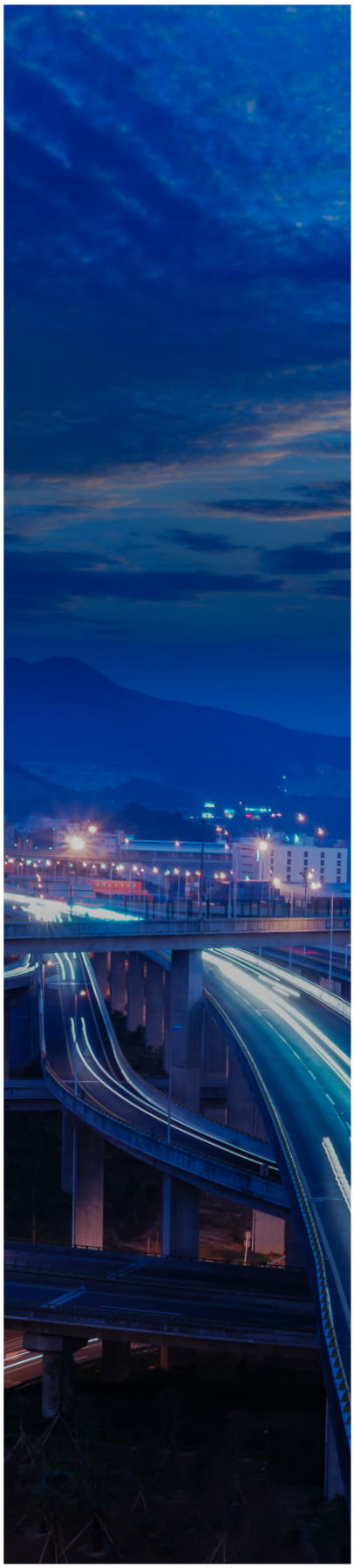
A fellow guest noted that their bank had funds in Hong Kong dating back to the 1970s. But he remarked that while they are ideally positioned for the current China push, if they have the Luxembourg equivalents of a lot of these strategies, they are able to diversify the investor base, as investors in Europe now getting more and more comfortable with Asian equity investments and increasing the portions of their portfolios dedicated to the region. He said they were trying to capture both sides, the money flowing into the region, and also through the GBA and WMC the money flowing within the region, and increasingly so.

Asia trending to European models

Another expert reported that the wealth management industry is increasingly happy to work with the platforms, noting that their firm had been working strategically with the Allfunds teams in the past year. He himself had returned to Asia after a stint in Europe, where they had also worked extensively with Allfunds. "We saw there the explosion of large wealth managers that are using the likes of Allfunds to go about their daily fund flows and funds business, that has been ongoing for a few years now," he reported, adding that he sees the same evolution taking place in Asia. "Accordingly, we work with Allfunds and others to make sure that we capture that opportunity, not just for China, but across the region. We are excited by the potential."

Platforms helping enhance insights and suitability

Offering further insight, he said dialogue with leading digital plat-



forms such as Allfunds enhances their understanding of the market, of demand, or data availability and so forth, helping them to continuously refine their products and proposition, especially gleaning information from those platforms' connectivity with some of the client channels that they as a global asset management house might not themselves have access to. "My distribution team here in Hong think strategically, and we also have a dedicated team member working closely alongside the platforms within our structure."

Digital days ahead

His final comment was that digital is indeed a key pillar in their strategic plan for the decade ahead. "This is not just in terms of providing plumbing and apps for easy trading; it's actually around portfolio advisory, providing analytics to clients to be able to assess style exposures that they might have or unintended biases they might have in a portfolio across funds and single line securities. We're trying to work in that space to bring something pretty cool to the industry, intended for relationship managers, but also end investors too. It's an exciting but very fast-moving space that obviously clearly requires significant investment, and it requires working alongside strategic partners such as platforms."

He explained further, noting that they are looking beyond the transactional platform for buying funds, beyond the portfolio view towards aggregation, towards working in partnership with certain wealth managers to create, for example a platform that could help demonstrate the competitive positioning of their products alongside other products, to show the advantages for example in terms of Sharpe ratio, volatility returns, and thereby to help layer in more of an analytical component to the portfolio formation.

Aggregation and analytics

He commented that platforms such as Allfunds are uniquely positioned to do this, bringing in the aggregation of a broader set of data that an individual asset manager may not have the full view on. "It all comes back to trying to help individual investors or relationship managers talking to investors to realise certain features of their portfolios but using AI and other automation tools. "We are looking to do this in a very selective way with strategic partners, to make sure that we don't make too big a splash without learning from it on the way," he reported.

Private clients are increasingly digitised

Another guest said that with a view to Hong Kong distribution, the approach depends on the target clients. "The typical private banking mutual fund client in Asia is somebody who's well into their 40s up to 60s who has the disposable income to put money away into investment products, and they are still driven by personal sales and advice. The mass affluent market, traditionally ignored by the private banks, are comfortable with the fintechs and apps, and the banks are now trying to connect to them digitally as much as possible, even though in Hong Kong, where there are still so many bank branches, the relationship managers and officers can still handle this. At the same time, the banks are using digital more for upselling and delivering more services around these areas."

Building the ecosystem

Another guest concurred, adding that their bank in Hong Kong was leveraging digital for servicing the client and enhancing the client experience. "We are working in a distribution landscape that itself is changing quite quickly," he explained, "so we have adopted a three-pillar strategy. We are enhancing our distribution through the bank's online channels, we are distributing through online brokerages and platforms like Allfunds, and we are looking at the distribution ecosystem partnership, although the last of these mainly for China. In short, we are building our existing presence and penetration."

Diversification of Asian investor demand

Another perspective came from a guest who noted that Asian investors' focus has evolved, especially since it became clearer that fixed income is unlikely to provide the returns that Asian investors typically achieved relatively easily in the past. "And we are in a potentially lower return environment in the future, globally across all asset classes," he remarked, "so we are as a result seeing in the private banking space, and possibly later in the retail space the increasing demand for multi-assets and solutions and also focus more on outcomes rather than beating benchmarks."

Accordingly, he observed that Asian investors are slowly getting much more comfortable with asset allocation and portfolios that are constructed across a number of different funds, and to do that, effectively, if you're not using your own funds alone, you certainly need sound information on the risk-return factors of other available funds to make sound, timely portfolio construction decisions.

Mutually beneficial relationships

"If platforms can help us do that, then they can serve that purpose," he said. "And as people at these platforms know, if banks are going to use them and as asset managers are going to come on to those platforms, it has to be commercially viable for everybody, it can't be that one party has to give something up at the expense of another. The result is that both asset managers and distributors have to look at the platform and view it as being mutually beneficial to both parties and come to that platform with that outlook. That is certainly a challenge for these platforms."

A word of thanks

Allfunds' David Pérez de Albéniz closed the event with a warm thank you to those who participated. "Our mission is to be highly transparent and make sure anyone we work with fully understands our platform and the model, and appreciates the whole added value we can offer, so they, in turn, can extract maximum value from the platform," said Pérez de Albéniz. "We have enjoyed many insights today, all of which help us refine our approach and mission. We have a great track record in Europe, and we are indeed building understanding and connectivity here in Asia, which is helping boost our business and the understanding and business of those we work with to the advantage of both sides of this equation. Our door is always wide open to discuss these matters further with any of you." ■