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How sub-advised funds will continue enhancing the fund industry across the globe

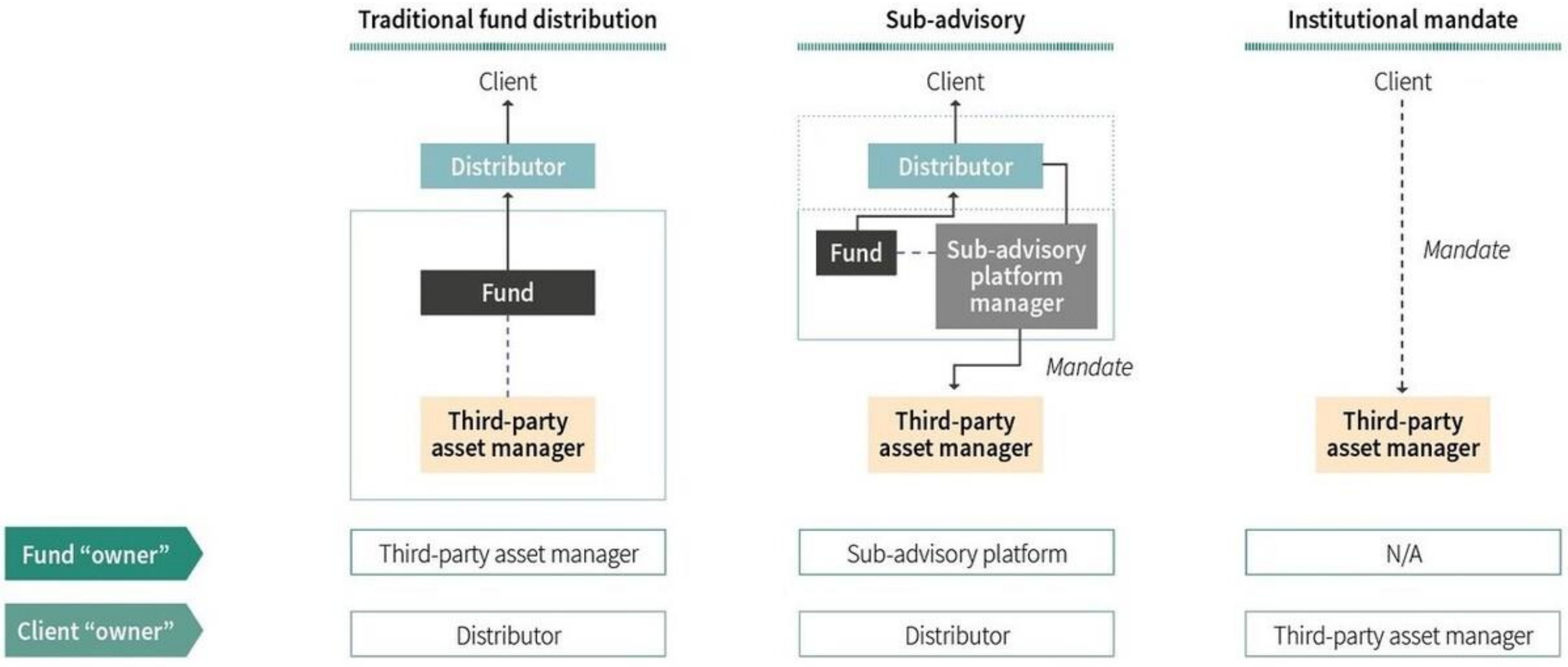
An empirical overview and strategic outlook

Agenda

- Current magnitude of the trend towards combining investment funds with mandates or sub-advised funds across different jurisdictions
- Do funds-of-funds still have a place in the core wealth management offering of a bank?
- Using mandates and exclusive/tailored sub-advised opportunities as a powerful differentiator and profitability enhancer – an empirical case study

Sub-advised funds – a powerful tool in a nutshell (1/2)

- **A sub-advised fund is a mandate, managed by a third-party asset manager in a (white-labelled) fund wrapper.**
- **Typically, institutional distributors (banks, insurance companies etc) use sub-advisory to fill a gap in their product range by complementing in-house capabilities with external specialized expertise from unaffiliated managers.**
- **This instrument can be a powerful competitive advantage and differentiator vs competitors.**



Indefi, 2019.

Sub-advised funds – a powerful tool in a nutshell (2/2)

- The delegated approach enables a distributor to build different risk profiles in white-labelled solutions.

- Sub-advised funds are broadly implemented both within fund-of-funds and/or in discretionary portfolio management of banks and other institutional distributors.

- The sub-advisory model requires a strong ability to select managers with a proven track-record and monitor them on an ongoing basis, combined with an efficient operational model for the distributor to set up the delegation.

- Two key drivers of bank distributors' soaring appetite for sub-advisory programs
  - Searching for new 'structural alpha'
  - Profitability enhancement of distributors' own funds, being sub-advised at a low fee.
  - Specific client needs
    - Example - the next generation of wealth management clients are looking to invest in new asset classes for example, with ESG and impact prerogatives. Some of these strategies can be complicated to achieve internally, and sub-advisory can help with that.

- **A perfect addition to the product mix of a bank in its private banking and/or wealth management business, offering multiple customization options (co-branding, white labelling, exclusivy etc).**

Sub-advised funds – Who benefits?

- **Investors**

  - Sub-advisory is a way for investors to access open architecture at a competitive price. They can benefit from the operational expertise of their distributor and enhanced risk management thanks to an access to the transparency of sub-advised portfolios. This allows the end-client to obtain a better and broader product offer controlled by intermediaries.

- **Asset Managers**

  - The control of the value chain is gradually shifting from manufacturers to intermediaries. There is such an appetite for sub-advisory that asset managers take the strategic decision to provide their sub-advisory expertise to the intermediaries in tailored mandates. An additional advantage are the substantially higher volumes and the option of co-branding.

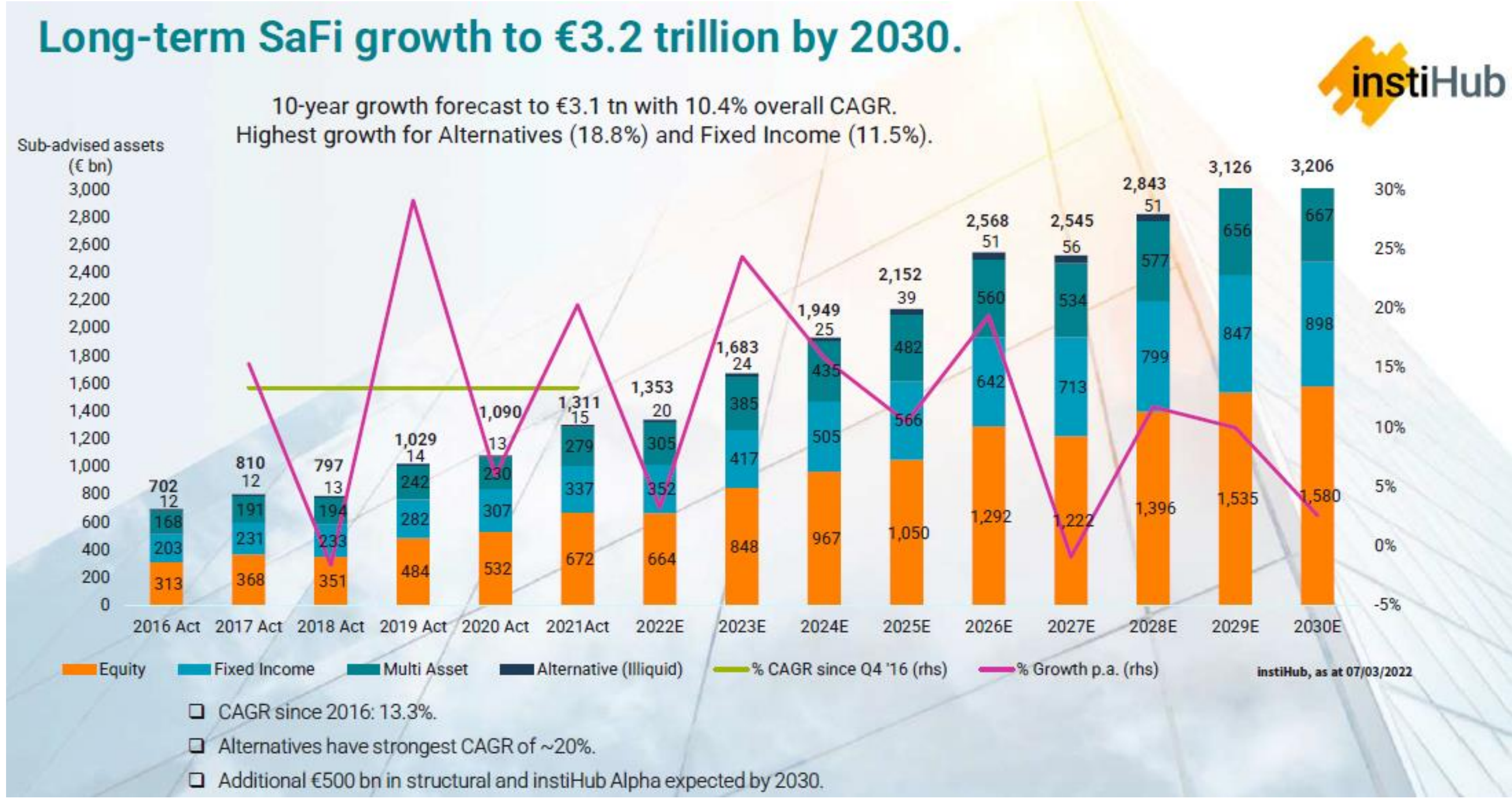
- **Distributors**

  - Sub-advisory enables a customization of the product for a distributor with its own parameters (risk guidelines or specific ESG requirements). This created a strong commercial incentive.
  - Management delegation allows value creation compared to competitors, in open architecture, for end clients, one of the key differentiators in the distribution offer.

- **A win-win-win deal for investors, third-party asset managers and distributors**

Sub-advisory outlook: 2022 and beyond

- The sub-advisory market is in full expansion and is the fastest-growing open architecture segment in Europe and the US
- AUM of sub-advised funds sold in EMEA continued to grow meteorically by reaching more than EUR 2tr in 2022
- EMEA sub-advised fund assets expected to rise to almost EUR3tn in next ten years, says instiHub
- Trend towards sub-advised funds being used inside distributors' fund of funds is increasing with up to 56 per cent of their sub-advised assets gathered from inclusion into the distributors' fund-of-funds

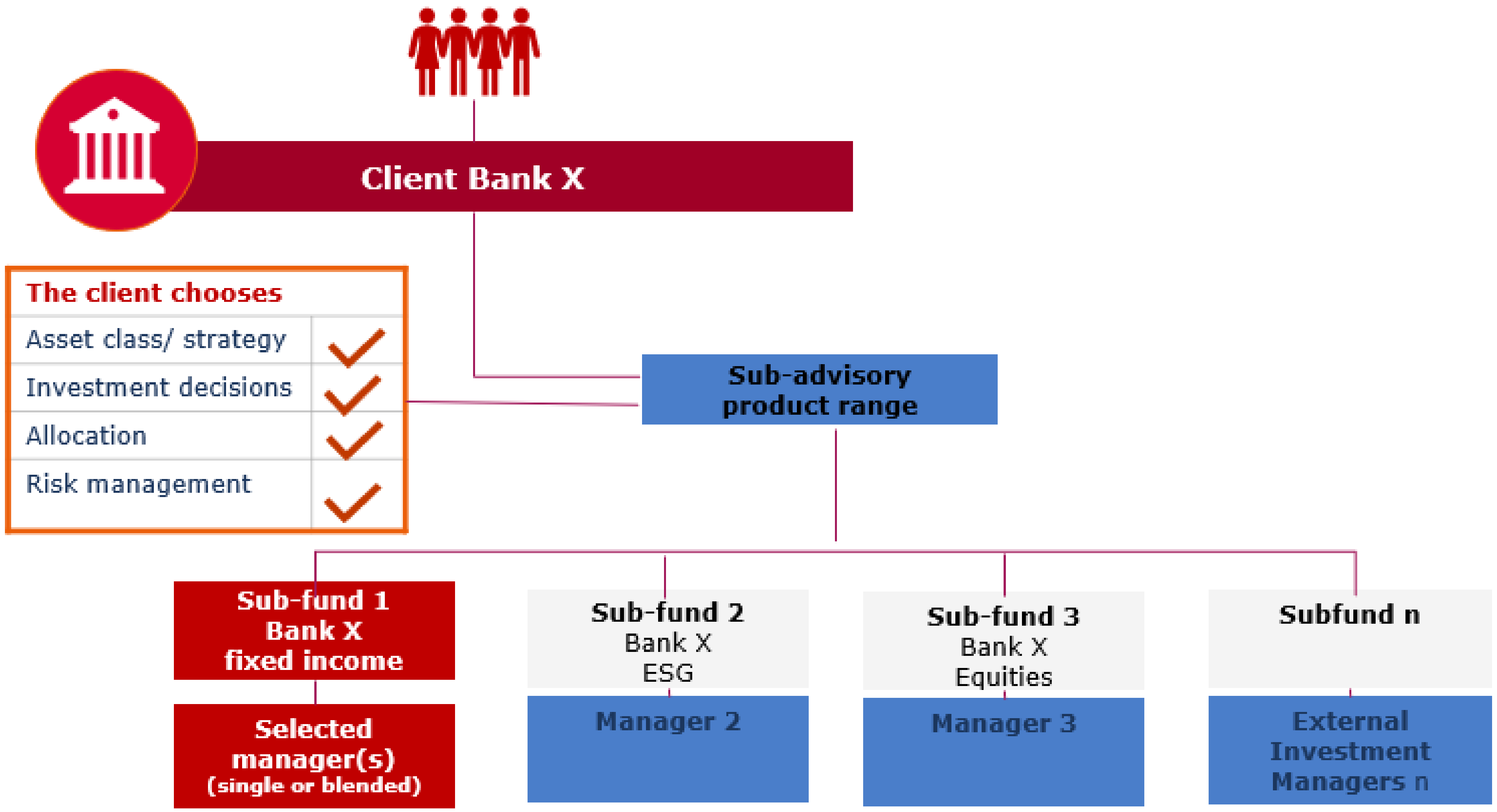


Case study 1

Creating a white-label range of sub-advised funds under UCITS

Rationale behind – broadening the own product offering by blending own strategies with best-of-breed external managers under the own brand and the UCITS transparency

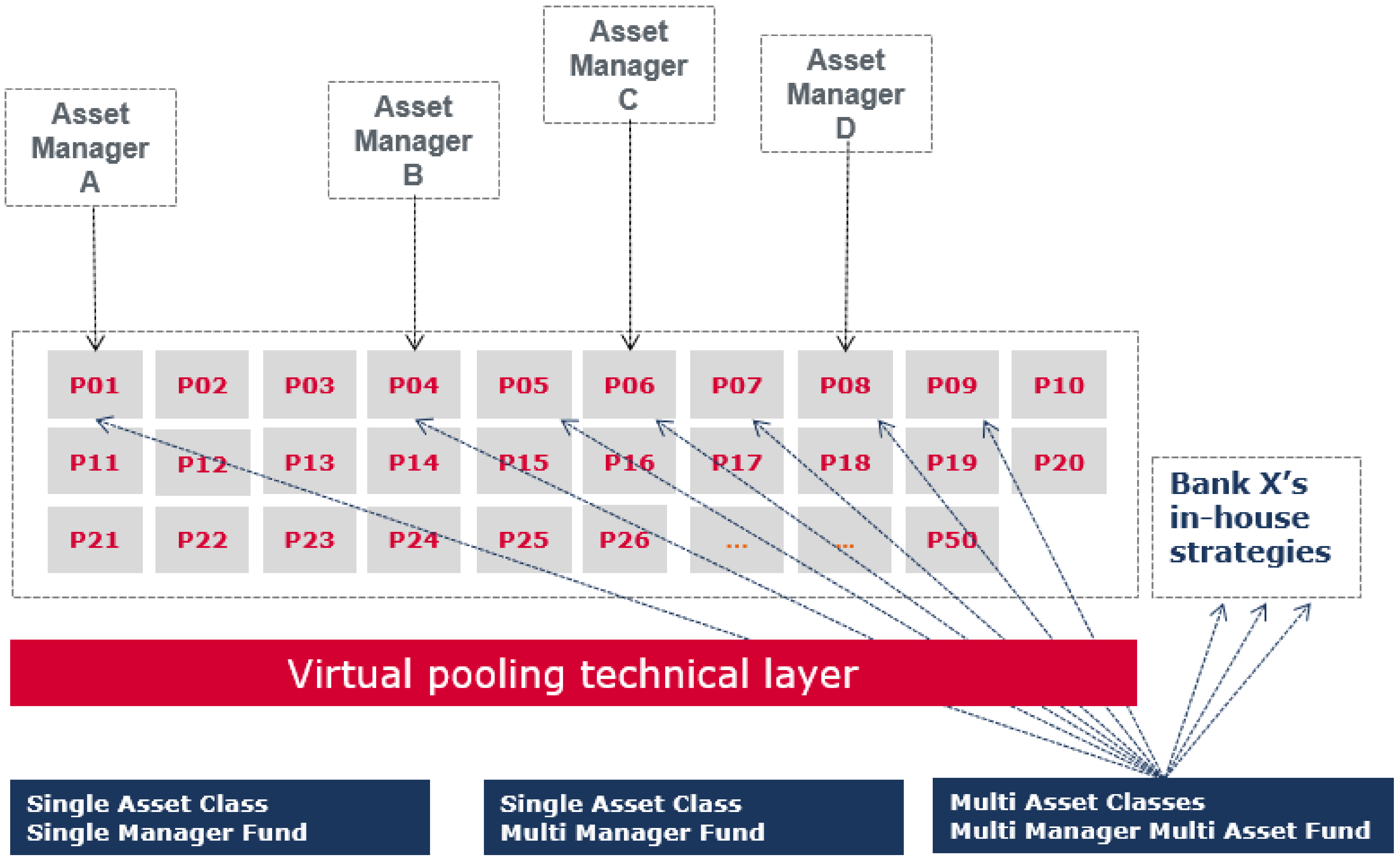
Using sub-advisory to create a UCITS product range: a case study



- **Client's profile**
  - A mid-sized Asian bank looking to offer its clients a range of dedicated UCITS funds, using both in-house and external asset management capabilities
  - The bank plans to integrate these funds in their discretionary portfolio management for different risk profiles (conservative/balanced/aggressive)

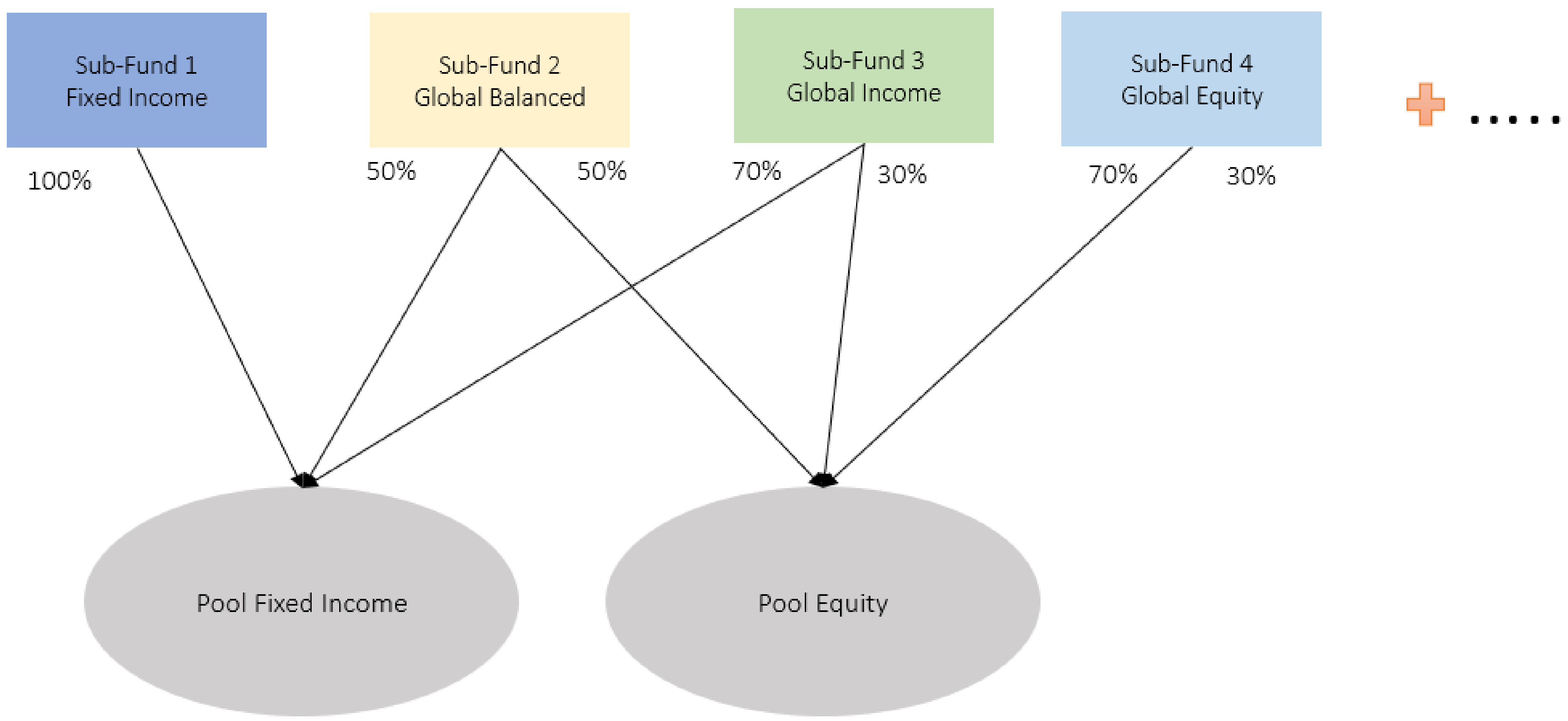
- **Target operating model**
  - Create a UCITS umbrella in Luxembourg, selecting an independant service provider
  - Choose a service provider with sub-advisory capabilities, offering efficient structures to trade via pools and mix them into different risk profiles
  - Create different share classes to accomodate for fee levels, currency hedging, etc.

The asset pooling advantage



Implementing a sub-advised solution –

A strategically planned success story despite challenges



- **The importance of the selected implementation partner**
  - **Creating an own sub-advisory fund range can be a lengthy and complex process.**
  - **When adding the implementation under UCITS regulation, the choice of the right implementation partner is key.**

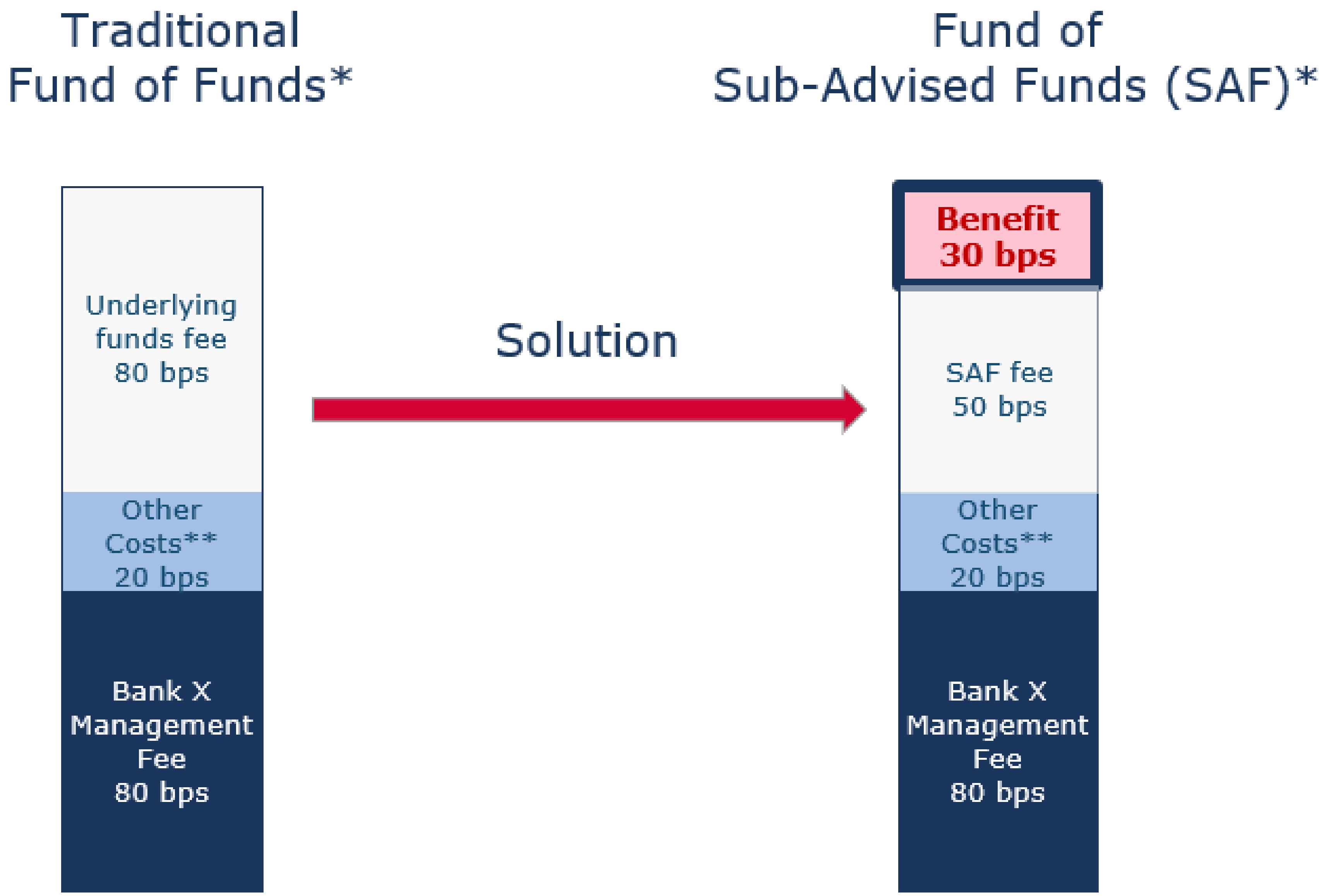
- **Lessons learned**
  - **The sub-advisory model requires scale and operational lead time.**
  - **Scalability, dedicated reporting or performance attribution are elements that make the quality of the partnership crucial.**
  - **The success of this model depends mainly on the manager's selection, but also on the operational capabilities of the chosen service provider.**
  - **This form of outsourcing makes it possible to incorporate expertise in new asset classes, as well as extended geographical coverage.**

Case study 2

Using sub-advised funds to enhance the cost efficiency of the proprietary funds of funds

Rationale behind – in order to improve the cost efficiency of the own FoF range, a bank decides to invest into a selected range of sub-advised single-manager strategies (on a building block basis). Additional advantage – reducing fees for the end-client and benefitting from a comprehensive look-through reporting.

The cost advantage for funds of funds – an example



** Non-rebating share class example*
*** Administrative fees and taxes*

Additional advantage besides reducing fees for the end-client - benefitting from a comprehensive look-through reporting.

Key observations based on empirical evidence – it is not ‘either/or’, it is ‘as well as’

Sub-advisory is on the rise globally

Sub-advisory will continue shaping the product offering of distributors

Asset Managers choose to actively participate in this trend

Sub-advisory can be a powerful instrument for fund of funds and white-label solutions

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Thank you

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