Brown Brothers Harriman

Fund Distribution Outlook

How to Differentiate Distribution in 2024

The trends and strategies shaping an industry in flux

EXECUTIVE SUMMARY

There's no debating that this is a challenging period for asset managers. The industry continues to face incessant downward fee pressure, slow market growth, continued growth of passive funds, regulatory challenges, and increasingly sophisticated client and investor expectations. In this environment, it may be easier to retain and upsell to existing investors with new and differentiated products than acquire new investors. This places more importance than ever on the quality of the investor experience.

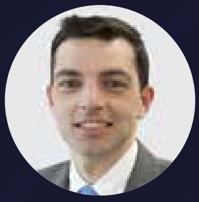
So how do managers differentiate their products?

Having a coherent and efficient distribution strategy is paramount in this environment. Some would argue that an effective distribution strategy is now on a par with investment strategy and performance. With over 65,000 funds presently for sale in Europe, managed by over 5,000 managers, competition is fierce. Evolving technology, regulation, and investor requirements present an opportunity to reduce client acquisition costs, increase participation of a broader range of investors in more locations, and provide additional asset classes to a greater cohort of investors.

What's the key to success in this complex environment? Respondents confirm there is no one single optimal strategy; instead many disparate elements must work in unison towards a common goal that ultimately achieves consistent asset growth. Nonetheless, a consistently positive investor experience is non-negotiable for client retention and lays the foundation for cross selling opportunities.

Factors such as brand, investment strategy, and historic performance are key for both prospective and existing investors. However, what makes a material difference in winning, retaining, or losing an investor is a host of smaller, often technical, or administrative matters, that can vary depending on the investor type, location, preferences, and expectations.

Adrian Whelan
Global Head of Market Intelligence, BBH



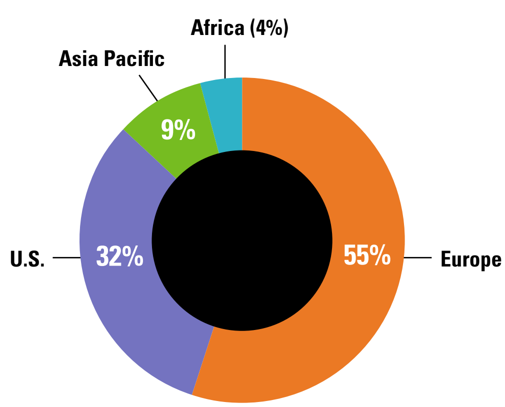
Killian Lonergan
Head of Distribution Intelligence, BBH

In the following report, we highlight three ways that managers can differentiate their distribution efforts in 2024 and beyond:

Our outlook captures the feedback and opinions of a diverse range of global asset managers, as well as fund sales and distribution experts, based on interviews and conversations held by BBH's Market Intelligence Group across 2023. It also includes quantitative insights from our 2023 survey of more than 100 asset managers covering both the current and future distribution landscape.

Who We Surveyed

(105 asset managers)



TREAT DISTRIBUTION AS A TEAM SPORT

Fund managers are regularly looking to promote relatively similar products – with similar performance and price points – often sold to the same investor segments, if not the same investors. To differentiate and increase assets under management (AUM), managers must be strategic in engaging both internal and external "teammates" as part of their ecosystem. With face-to-face "pitch" meetings no longer the primary sales strategy, new skills and more modern approaches are needed to access digital natives and engage the technology-led data hungry platforms and client interfaces that currently dominate the asset allocation landscape.

To respond, asset managers are shifting resources to data, technology, and talent and implementing new and diverse skill sets through a mixture of in-house subject matter expertise as well as connecting with specialist partners. This ecosystem approach, paired with adaptability and responsiveness to customer preferences, builds a strong foundation for distribution success and investor loyalty.

Tactical Switch: Evolving In-house Talent

Survey respondents indicated that while growing sales teams has been the focus in recent years, resources will be shifting to adding client service team members over the next three years. The growing importance of data in the relationships between the buyer and the seller has also impacted the sales role, necessitating a resource shift toward hiring different skill sets including data scientists. In addition, asset managers shared they are pivoting towards attracting web designers and social media experts to fulfill their digital marketing needs.

Building Bench Strength: Extending External Resources

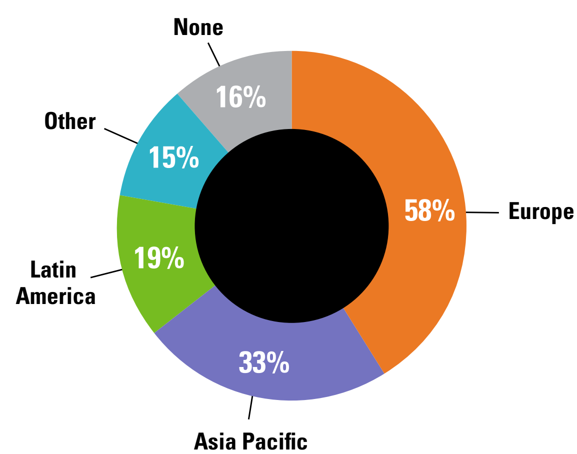
Alongside internal team shifts, asset managers must carefully coordinate a growing network of distribution partners to complement in-house talent, each contributing their own skill sets and value propositions.

This is especially true as firms have been expanding into new markets over the past three years, with Europe (58%) and Asia Pacific (33%) topping the list of new markets where survey respondents have been actively raising assets.

Managers are prioritizing external partners to navigate the operational requirements such as tax reporting, local fund registration, and trading connectivity as they expand to new regions. To complement their internal market entry teams, respondents were particularly interested in partnering with a legal advisor, followed by service providers such as transfer agents.

When asked which roles are most important to their distribution success, managers indicated third party marketers, local placement agents, and Know Your Distributor firms, who help to simplify and standardize important regulatory requirements, particularly in Europe. Transfer agents are also a crucial partner within the distribution ecosystem as they play a significant role in ensuring seamless relationships with the end investor, key platforms, local distributors, and intermediaries.

Have you been actively raising assets in any new regions over the past 3 years?



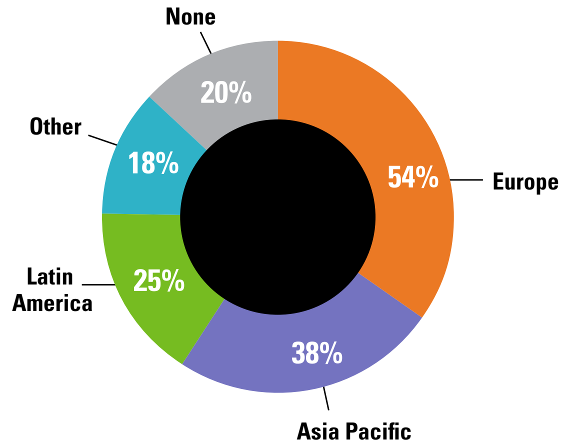
Protect and Grow

Europe remains, by some distance, the largest cross border fund distribution market. However, its proportion of the overall market is diminishing. The European cross border funds market is mature, hyper competitive, and in some asset classes, saturated. It is evident that firms need to do much better at attracting European pensions and other asset owners into investment funds.

Owing somewhat to European stagnation, many respondents are looking to newer vibrant geographies such as Asia-Pacific and Latin America for growth, particularly for their UCITS funds.

Perhaps more notable is the relatively high number of respondents who do not plan to raise assets in new regions. This is a surprising finding since asset raising opportunities appear to be more plentiful in less mature markets with a strong appetite for offshore fund expertise.

What new regions do you plan to actively raise assets in within the next 3 years?



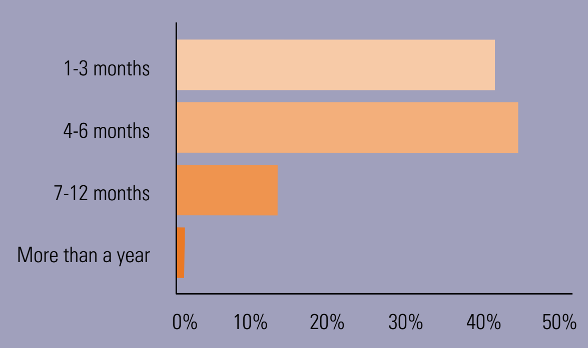
DID YOU KNOW?

Distribution Agreements

One of the cited causes of frustration in our survey was the inevitable slowdown in investor onboarding as the bilateral process of agreeing to a standalone distribution agreement takes time – even months in some countries.

There are firms providing a service that allows a fund manager to sign an agreement which gives access to ready-made distribution agreements with hundreds of distributors and platforms across Europe. For some investor gatekeepers, the use of such distributor agreements is a 'must' before engaging in discussions with an asset manager.

Time Spent Negotiating Distributor Agreements

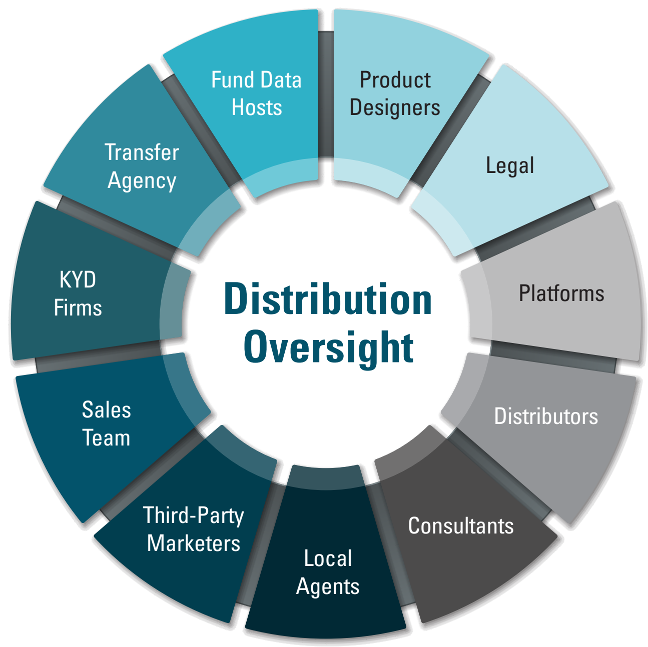


Managing the Ecosystem

More partners necessitate more oversight to meet the regulatory expectations of overseeing distribution with regards to the corporate governance structure. It's an area where specific market knowledge, and access to timely and accurate distribution data, is crucial. This dynamic is particularly notable in the UCITS space in Europe. Firms must take a buttoned-up approach across sales and service models globally, with service partners mirroring that for connectivity. When building out that oversight framework, managers should consider:

- The specific roles of each distribution "teammate"
- Time needed to build partnerships
- Who your competitors are using
- Whether your partners are a cultural fit for your firm
- Budget/return on investment

A successful distribution ecosystem should be greater than the sum of smaller parts, with each participant keeping the investor experience at the heart of their strategy.



PRIORITIZE CLIENT EXPERIENCE AND SERVICE

Many managers are shifting resources from new sales efforts to bolstering the client experience in response to increasing distribution fees for new sales and an ongoing volatile market. The shift is also being necessitated by heightened investor expectations. Retaining clients – building loyalty and trust with a view to growing the relationships – should now be regarded as important or more important than attracting new investors.

Managers should take the following steps to ensure a differentiated client experience:

First Impressions Matter: Simplify Onboarding

It's increasingly evident that investors and distributors expect servicing partners who are proactive, seek to help the onboarding process – from account opening to AML checks – and make life as easy as possible. Any undue delays or perceived unnecessary complexity can be off putting and either nix a sale or reduce the opportunity for retention or further sales.

Every Interaction Counts: Perfect the Day to Day

With the proliferation of funds in the market, there is an abundance of choice for investors. Investors increasingly can and do switch funds if their experience is not as they expect. Ease of doing business, responsiveness to general fund queries, or data requests must be done swiftly and accurately. Expectations are rightly high and client retention is based on ongoing good service, and not just impressive pre-sale interactions.

Future Focused: Leverage Technology

Data, process simplification, and a seamless consistent experience for investors are all technology driven. Investors expect to receive information they ask for in a timely, accurate, and easy to use manner. Investor portals, where information is openly shared and allows for self service of fund data, are now the norm. Poor responsiveness, inaccurate, or hard to access information is no longer tolerated in an increasingly data-led funds market. The availability and accessibility of investor education and liquidity management tools will be key to product innovation.

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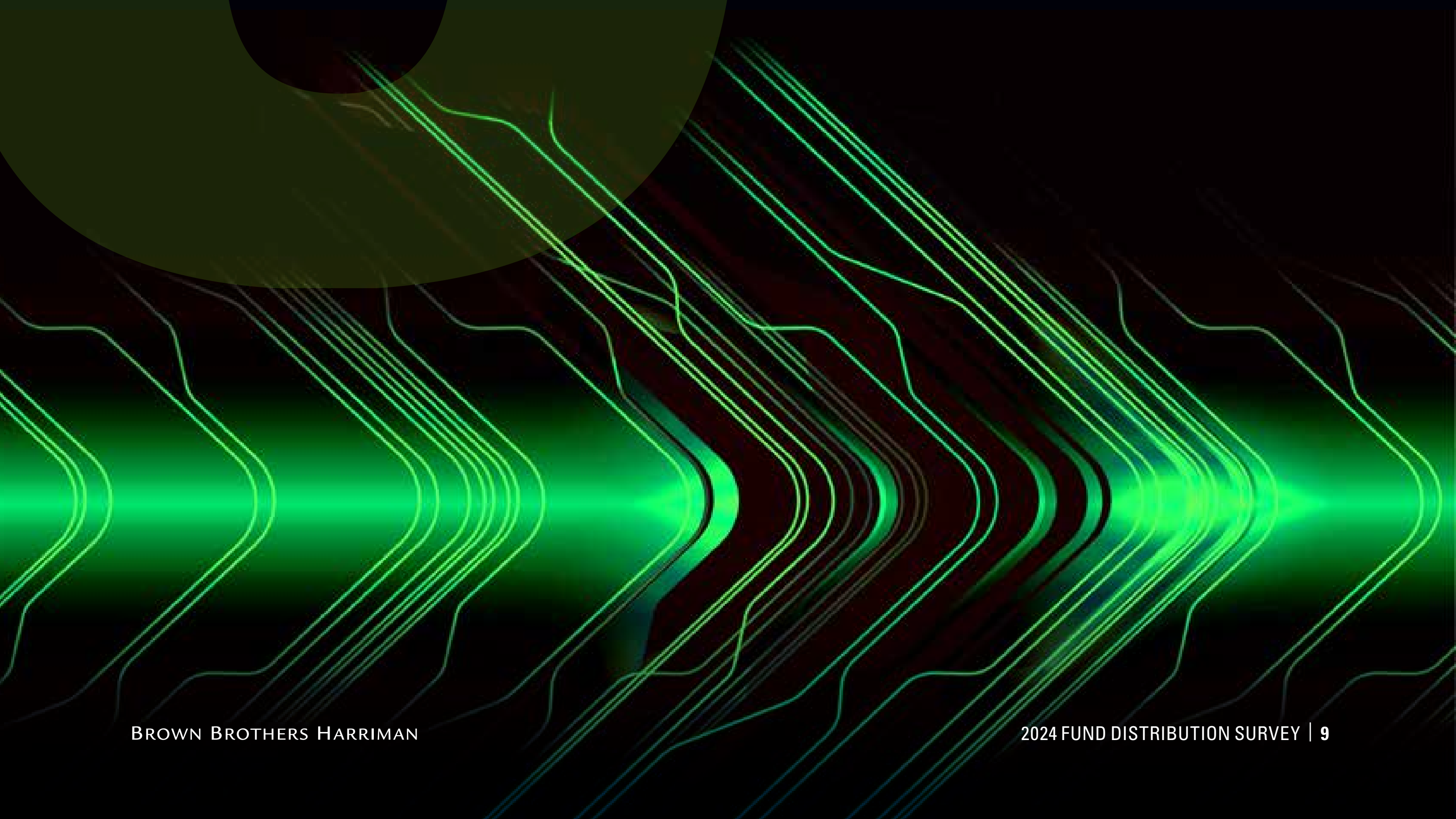
MAXIMIZE PRODUCT INNOVATION

As managers plan to add more innovative products such as alternatives and active ETFs, the ability to scale and address operational hurdles are critical requirements. Making these products available to a wider range of investors also requires a coherent data strategy that allows for easy to access, timely, and accurate information.



Alternatives – Democratizing Private Markets

Managers plan to roll out more alternatives products, with the ELTIF market alone predicted to reach €50 billion by 2028 (up from €11.3 billion at the end of 2022). Nearly 50% of survey respondents are looking to go to market with ELTIFs and LTAFs in the next three years. Regardless of the chosen fund structures, more open-ended private market vehicles are expected to come online, targeting a wider range of investors as the democratization of private markets continues apace. Investor education and the ability to deploy liquidity management tools are two crucial areas relative to the democratization theme.

With this anticipated growth of private markets, managers must think ahead to possible roadblocks, including investor onboarding, operational connectivity, ability to manage a wide range of minimum holding periods and liquidity terms, as well as ongoing investor engagement and often complex reporting requirements. They are looking to platform providers and market infrastructures to make investor access to private market funds look and feel similar to how they currently access traditional mutual funds.

This raises key considerations for managers:

- The ability to scale: particularly with respect to investor reporting and product distribution when looking to raise capital from retail clients and how to navigate potentially dealing with hundreds or thousands of investors
- The ease of doing business: These buyers of alternative funds are the same investors who regularly purchase mutual funds directly or on behalf of their underlying clients. And they want to trade and settle in the same way, or at the very least with as little disruption to their existing models as possible
- Addressing operational hurdles: Adapting marketing and investment structures to accommodate a large inflow of high-volume retail capital; considering suitability, price and heightened regulatory risk of serving retail; and adapting to more complex fee considerations in alternative funds and the disclosure, calculation, and onwards dissemination of such information

Active Exchange Traded Funds

Investor interest in ETFs continues to grow, with the active ETF space particularly compelling to many managers as a strategy to combat fee pressures and grow into new distribution channels.

BBH's 2023 Global ETF Survey showed that 82% of investors planned to increase or maintain their exposures to active ETFs as conversions from mutual funds into actively managed ETFs intensify. 92% of investors bought an active ETF in the 12 months preceding the survey, with much of that capital coming from mutual funds (see table below).

Where investors allocated capital from to buy actively managed ETFs in last 12 months

(Respondents could choose multiple responses)

	TOTAL	U.S.	Europe	Greater China
Cap weighted passive ETF	28%	23%	20%	44%
Smart beta ETF	29%	24%	25%	38%
Index mutual funds	46%	46%	42%	50%
Active mutual fund	42%	43%	33%	50%
Separately managed accounts	29%	32%	23%	34%
Allocated new investment dollars	20%	27%	14%	22%
I did not purchase active ETFs	8%	10%	10%	4%

BBH's 2023 Global ETF Survey

However, it is not as simple as saying *"Yes, I want to launch an ETF."* There are specific technical elements that are different, and education remains key on the nuances of the ETF market regardless of region.

Thus, when adding actively managed ETFs to their portfolios, managers may benefit from the following key considerations:

- Targeting markets where active ETFs maintain a good growth pace (such as the U.S. and Europe) and markets that face a promising start (such as Japan, Hong Kong, and South Korea)
- Launching active ETFs with complementary strategies – this provides a new distribution channel giving managers exposure to a new pool of investors
- Considering new processes and personnel – this involves a strategic pairing of talent and technology, such as adding a Capital Markets team

One to Watch: European ETF Market

While the hurdles to launching ETFs in Europe have lowered, it is still a very complex model for new entrants, particularly those from overseas. Interestingly, in Europe, the market is currently dominated by "off exchange" trading, where trades are executed OTC via RFQ platforms. While there are regulatory initiatives to coax retail investors into European ETFs, for now the addressable distribution markets look very different in Europe than they do in the U.S.

Data and Innovation

Managers have a wide spectrum of opinion when it comes to the importance and benefits derived from distribution data. Whether it's prospecting new clients, monitoring investor behavior and appetite, tracking meetings and client interactions, or data used for regulatory reporting, many are swimming in data. Unfortunately, many are also drowning due to the absence of a coherent integrated data model.

However, what is clear is acknowledgment that digitization of processes and using data for better business outcomes is a priority moving forward. Whether it's being more efficient with Client Relationship Management tools such as Salesforce or more ambitious goals such as utilizing cloud computing platforms and APIs to automate distribution, data reporting and feeds, asset managers want data to act as a distribution enabler rather than a liability into the future.

Furthermore, a coherent data strategy that allows for easy to access, timely, and accurate information in different file formats is now a hygiene factor when dealing with the larger investment platforms and institutional asset allocators. Having a service partner who can provide self-service portals and understands the external landscape is increasingly crucial to investor retention and growth.

DID YOU KNOW?
OpenFunds

OpenFunds is an industry-led data structure standard that allows asset managers to distribute key datapoints about their funds to distributors and other interested parties. This data standard grew out of the need for distributors to limit the volume of different data files they were receiving. Several large fund platforms and asset allocators have shared that the data points on this file are essential for their operating model. Specifically, to onboard any funds and have their global bank network list and sell each fund, it's essential for them to know in which countries the funds are formally registered for sale. If these data points are missing, or incorrect on the datafile, the larger fund platforms will simply not onboard the fund as they will not take the risk of having their network inadvertently mis-sell in a jurisdiction the fund is not registered in. Updated versions of this file are consistently rolled out, and Q1 2024 sees significant updates. Managers need to be on top of these changes and working with internal or external partners to make sure distributors aren't adversely effected.

CONCLUSION

As competition continues to grow, regulatory overheads continue to encroach, and with technology yet to fully deliver meaningful shortcuts to success, it is imperative that managers embrace the ever-evolving fund distribution landscape. This means seeking out trusted partners who can be additive to their value proposition and embrace customer centric technology as a core strategy.

We now sit at an inflection point where heightened investor expectations around technology and the investor experience mean there will be discernible winners and losers from this dynamic.

We expect those who see distribution as a team sport, rather than an individual pursuit, to thrive into the future. Those who embrace a client focused, technology-led approach will best overcome challenges and grasp future opportunities.

Fund distribution success is possible for firms of all sizes, but the reality is that favorable outcomes will more likely come to managers who build a strategic ecosystem of internal teams and external partners, prioritize the client experience at all stages, not just first point of sale, and take a thoughtful, practical approach to innovation and exploring new product offerings.

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