1 UK INVESTMENT MANAGEMENT INDUSTRY: A GLOBAL CENTRE

KEY FINDINGS

UK INDUSTRY SIZE AND SCALE

- In 2023, assets under management (AUM) by Investment Association (IA) members increased by 3%, reaching £9.1trn. The rise of 3% in 2023 compares with a record fall in AUM in 2022 of 12%. Investment managers are adapting to a new market cycle and the end of the era of low interest rates and quantitative easing.
- UK funds under management (FUM) grew by 4% in 2023, reaching £1.4trn. This growth marginally outpaced growth in overall AUM.
- In the period following the global financial crisis between 2008 and 2021, AUM grew on average by 9% each year whilst FUM grew by 11%.
- In Scotland, IA members managed £490bn in 2023. Scotland's share of UK-managed assets is 5.4% of AUM and Edinburgh remains the second largest centre of investment management in the UK outside London.
- IA members account for 83% of total UK AUM. When including non-IA members, total UK AUM is estimated at £10.9trn.

UK INDUSTRY IN A GLOBAL CONTEXT

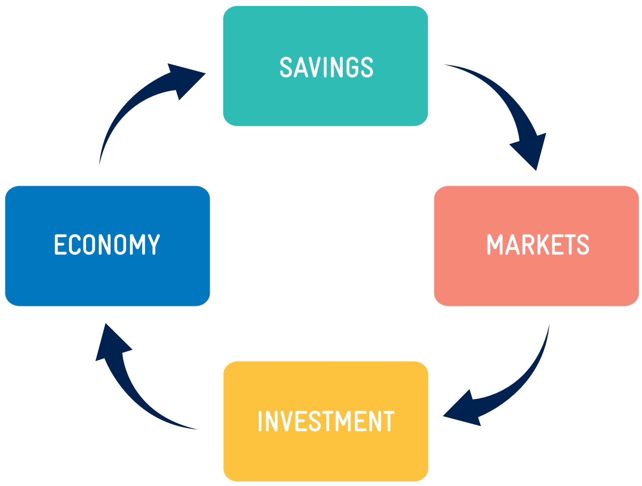
- Global AUM grew 12% in 2023 to $119trn, with Europe reaching €29trn and the UK representing 36% of the European market.
- By 2023, 49% of AUM managed in the UK was on behalf of overseas clients, up from 38% in 2013. Total assets managed on behalf of overseas clients grew by 7% over 2023.
- The largest share of overseas client assets is managed for Europeans, whose AUM grew by 5% in 2023. Over the past decade, these assets have seen a significant 71% increase, reaching £2.5 trillion.
- The highest growth at 12% was in assets managed for Middle Eastern clients, which are now £275bn. US client assets also rose by 9% in 2023 to £925bn.
- UK-managed investment fund assets in both UK and overseas domiciled funds stood at £4trn in 2023, which is unchanged from 2022. 68% of these assets sit in overseas domiciled funds where the portfolio management takes place from the UK.

This chapter provides an overview of the UK investment management industry, highlighting areas of growth, placing it in a European and global context, and emphasising the ways in which the UK investment management industry continues to thrive as a globally recognised centre for excellence in portfolio and asset management.

ROLE OF INVESTMENT MANAGEMENT

The investment management industry plays a central role in the economy, channelling savings into investment opportunities which deliver returns for a wide range of clients including individual savers or institutions such as pension funds. Figure 1 illustrates how capital is deployed in the economy to drive economic growth.

FIGURE 1: THE ROLE OF INVESTMENT MANAGERS IN CHANNELLING SAVINGS TO INVESTMENTS



The primary role of investment managers is to deliver good investment outcomes for their customers, including individual savers and institutions like workplace pension schemes or insurance companies. This includes passing on the benefits of economies of scale, delivering expertise in areas such as risk management, and providing access to a wide range of investments which would normally be out of reach for individual investors. The ultimate goal is to deliver a diversified portfolio of shares, bonds, and other assets, such as property, which can generate a good return for customers over the long term while being suitable for their willingness and ability to take risk.

Beyond facilitating the investment process, the role of the industry includes ensuring the efficient functioning of capital markets. Capital from individual savers and institutions is channelled to companies which use it to finance their operations and achieve growth. Investment managers play a pivotal role in maintaining properly priced markets and effective transactions between buyers and sellers. Efficient markets allow for accurate pricing of information that helps direct the capital available for investment to the highest-valued market participants, making them essential for the growth and stability of market economies. Investment managers contribute to sustainable economic growth by actively participating in and promoting the efficiency of capital markets, benefitting their investors and the companies they invest in but also the broader society at large.

Investment managers are not alone in their efforts to enhance capital market efficiency, as other financial institutions and individuals also play a role. However, the investment management industry has traditionally been central to the long-term allocation of capital, whether through stocks, bonds, or other assets. As long-term holders of investments, UK investment managers hold UK equities for approximately six years. The industry, therefore, carries a significant responsibility to engage in stewardship activities with the companies they invest in to safeguard the value of their clients' investments. This responsibility now extends beyond traditional considerations to encompass broader issues such as environmental sustainability and executive remuneration.

INDUSTRY SIZE AND SCALE

UK assets under management (AUM)[1] saw a return to growth in 2023, with AUM increasing 3% to reach £9.1 trillion. This follows 2022, a year in which industry assets fell an unprecedented 12% from £10.0 trillion to £8.8 trillion. 2022 saw economic and political instability as Russia invaded Ukraine and globally economies battled with escalating inflation. The monetary policy response to high inflation was to raise interest rates, marking the end of the economic cycle of low interest rates that began in 2008 amidst the global financial crisis. The recovery in AUM through 2023 is a sign that the industry is adapting to a new market cycle and remains resilient. UK funds under management (FUM)[2] rose by 4% to reach £1.4 trillion over the same period in 2023, marginally outpacing AUM growth.

Growth in industry AUM is a function of net flows and market performance. Market performance continues to be the biggest driver of growth. By the end of 2023, most major markets showed positive returns for the year, as markets started to price in higher interest rates. In the UK, the Bank of England's Monetary Policy Committee made its final rate hike in August 2023, pausing at 5.25% where the base rate remained through to the end of the year, even as inflation continued to move towards the 2% target rate (see Box 1 for a more detailed market overview).

"We've had high inflation and falling markets until recently, so that is a fundamental challenge for our industry. High inflation is reversing now which is good."

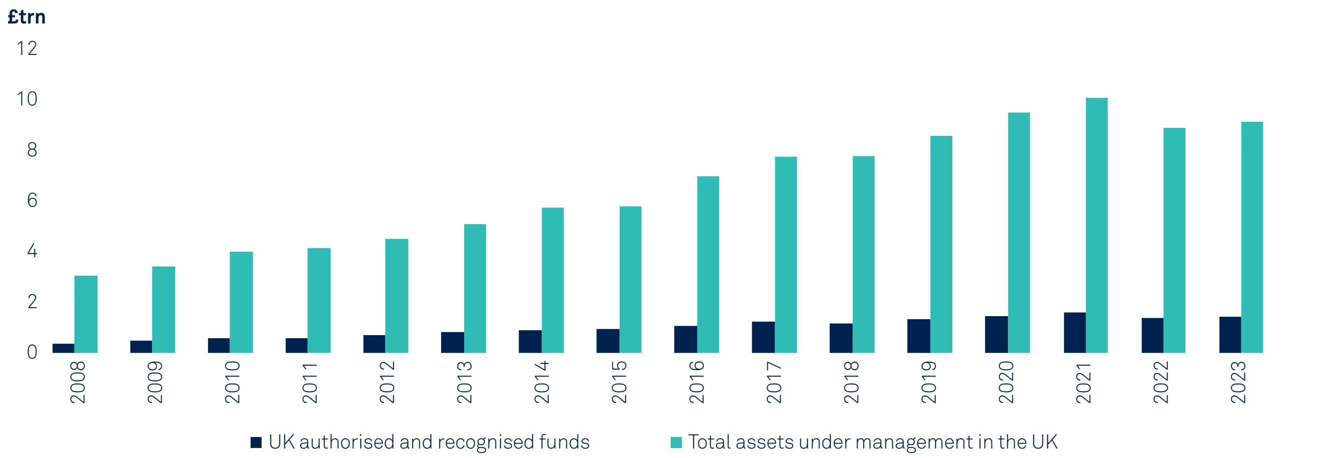
Chart 1 illustrates how industry assets and funds under management have evolved over the past fifteen years, and how the recovery in assets over 2023 compares to the fall in assets during the Global Financial Crisis in 2008:

- In the decade leading up to 2021, we observe that the compound annual growth rate (CAGR) for AUM was 9% per annum, while the CAGR for FUM was11% each year. Asset growth was boosted by low interest rates and central bank quantitative easing.

- While both AUM and FUM saw sharp falls of 11% and 23% respectively in 2008, this was followed by strong rebounds the following year of 12% and 33%. Central banks were able to cut interest rates to boost the economy during 2008 and this helped to support a rebound in the markets.

- The 3-4% recovery in assets in 2023 looks relatively muted by comparison but is a recovery in a materially different macroeconomic environment. The turn in the interest rate cycle through 2022 and 2023 has been driven by attempts to cool inflationary pressures across the real economy and this had a negative impact on markets.

CHART 1: TOTAL ASSETS UNDER MANAGEMENT IN THE UK AND IN UK FUNDS (2008-2023)



Sources: The Bank of England, The Investment Association, The Office of National Statistics

[1] UK AUM represents assets managed from a desk in the UK on behalf of UK and overseas clients.
[2] UK funds under management represent UK investors in authorised and recognised funds domiciled in the UK and overseas (principally in Ireland and Luxembourg).

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BOX 1: 2023 GLOBAL CAPITAL MARKETS IN REVIEW

Chart 2 looks at the annual total return in sterling of the major equity and bond indices over 2023. It illustrates that in 2023, markets recovered, and all the major equity regions showed positive returns, with China being the notable outlier.

Across the bond markets, the total return of UK government and corporate bonds was positive. This contrasts with the surge in UK gilt yields in 2022, which caused steep falls in the price of UK bonds. The global aggregate bond index, which is a mixture of government and corporate bonds, returned 0% over the year.

EQUITY MARKETS

In 2023, US equities showed the strongest performance with total returns of 19% over the year for the Russell 3000 index which includes large, medium and small cap companies. US markets were hopeful that easing inflation would prompt a Federal Reserve rate cut, but although this did not materialise, share prices still rose strongly. This was a significant bounce back from 2022 when the index was down 9% over the year and it puts the valuation of the Russell 3000 at roughly the same level as at the end of 2021. In the US, the "magnificent seven" technology stocks saw the largest increase in the value of their share prices relative to the growth in company valuations seen in the broader indices. In 2023, the pace of AI adoption was accelerating, which also helped to boost the share prices of companies like Nvidia.

The UK equity market returned 8% through 2023, compared with a 0.3% return in 2022. In contrast to 2022, when 0.3% beat the returns of the US, Global and European equity markets, the UK's performance in 2023 lagged the growth of its US, European and Japanese counterparts as capital markets rebounded.

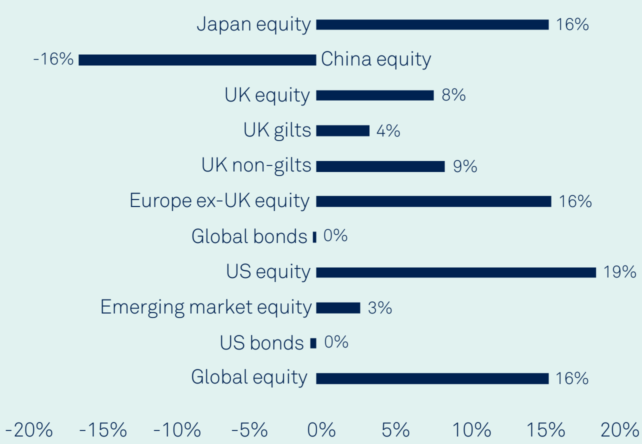
The Japanese stock market was a notable gainer in 2023 as corporate governance reforms on the Tokyo Stock Exchange bore fruit making listed companies more attractive and the Bank of Japan moved interest rates to positive territory, which symbolised the end of deflation in Japan. A weaker Japanese yen also helped to boost exports in 2023.

The MSCI China index saw negative returns of –16%, with hopes disappointed for a significant bounce-back in market valuations following the lifting of restrictive zero-COVID policies at the start of 2023. China has seen a prolonged property slump and ongoing geopolitical tensions, especially with the USA, have weakened investor confidence. Investors shifted their focus from China to India, which grew by 14% over 2023 as the Indian government showed a more positive stance to international business and investment compared with China.

BOND MARKETS

The performance of UK gilts and corporate bonds rebounded in 2023 after a very challenging 2022, when the September 2022 gilts crisis caused gilts yields to rise by 130 basis points over 3 days. Bond prices move inversely to the yield, and UK gilts returned 25% over 2022. As yields have stabilised in 2023, the performance of UK gilts and UK corporate bonds has improved, returning 4% and 9%, respectively.

CHART 2: TOTAL RETURNS ON SELECTED INDICES (2023)



Source: Morningstar

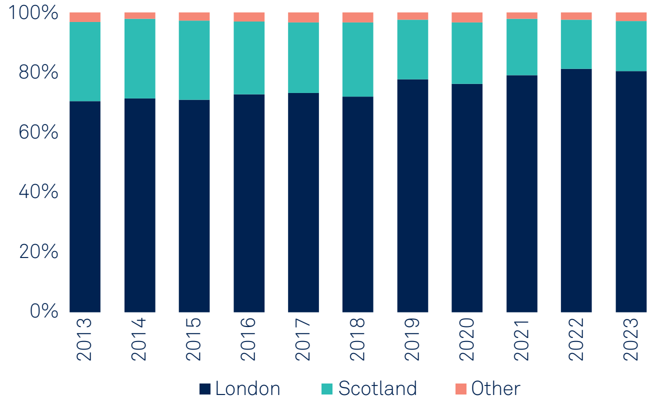
SCOTLAND AS A MAJOR CENTRE

The largest centre of UK investment management activity is London, which far exceeds other cities in the UK by headcount and the value of assets managed. Edinburgh is the second largest investment management hub in the UK and Scotland is a major centre of UK investment administration. Whilst AUM is one marker of the importance of Scotland to the UK industry, it can only tell us about the about the value of assets managed from Scotland, which is affected by a relatively small number of firms, but is not indicative of the development of Scotland's assets under administration. In 2023, assets managed from Scotland were £490 billion (5.4% of UK-managed assets), a one and a half percentage point fall from the previous year (£498 billion in 2022) despite total UK AUM growing over that period.

Chart 3 shows UK-managed assets broken down by the regional headquarters of UK-based investment managers. From 2013 to 2023, the share of assets managed by investment managers headquartered in London has increased ten percentage points reaching 80% in 2023. Assets managed from Scotland have fallen to 17% in 2023 from 26% ten years ago. The fall in share of assets managed in Scotland is due to a combination of factors including merger and acquisition activity amongst Scottish firms and the relatively high growth of assets managed in London.

The proportion of assets managed from other regions remains relatively unchanged over the last ten years ranging between 2-3% of assets. The concentration of UK assets managed by firms headquartered in London aligns with a broader trend observed in our employment data, where portfolio management is becoming increasingly centralised in London (See chapter 6 for further analysis of UK employment data).

CHART 3: UK-MANAGED ASSETS BY REGIONAL HEADQUARTERS (2013-2023)



Source: The Investment Association

UK ASSETS UNDER MANAGEMENT SAW A RETURN TO GROWTH IN 2023, WITH AUM INCREASING 3% TO REACH

£9.1TRN

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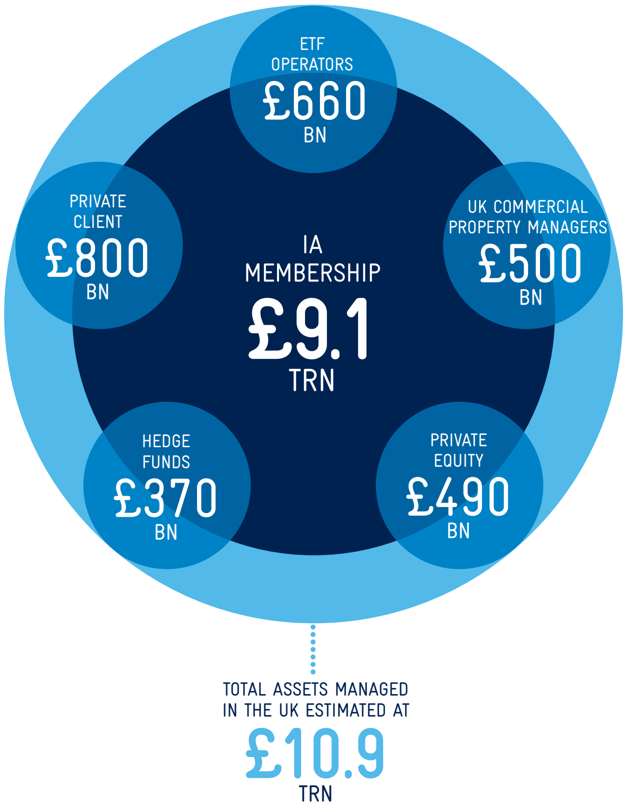
SCALE OF WIDER INDUSTRY

Investment Association (IA) member firms manage the majority of UK AUM (83%). While the profile of IA members remains diverse, the types of firms not covered by this report can be categorised in two groups:

- **Firms specialising in alternative investments:** The majority of firms not captured in the report typically specialise in alternative investments, including: hedge funds, private equity funds, commercial property management, discretionary private client and private debt management and natural resource management firms. However, more IA members are buying firms with expertise in managing alternative investments and so the proportion of alternative assets managed by IA member firms is increasing
- **Investment management firms that sit outside the IA membership:** It is difficult to accurately size and describe the profile of firms that are not IA members due to the lack of consistent third-party data.

Using third-party data and proprietary estimates, we estimate that assets managed by IA members and the wider industry are £10.9 trillion, up from £10.3 trillion in December 2022. Figure 2 provides estimates that highlight how various sectors contribute to the total AUM in the UK. The data in Figure 2 on ETF operators, UK commercial property managers, private client, hedge funds, and private equity represents assets managed not only by the wider industry but also by IA members. As such, there is overlap between the £660 billion managed by ETF operators and the £9.1 trillion managed by IA members, which includes assets in ETFs managed by IA members.

FIGURE 2: WIDER UK INVESTMENT MANAGEMENT INDUSTRY (2023)



Source: The Investment Association, Compeer, Investment Property Forum, Morningstar & Preqin.

THE UK IN A GLOBAL CONTEXT

The global investment management industry rebounded in 2023 after a difficult 2022. AUM in the United States grew from $47 trillion to $56 trillion, a 19% increase, reaffirming the dominant position of the US with nearly half of global AUM. This recovery was driven by improved equity markets and more favourable economic conditions, which saw GDP growth rise to 2.5% in 2023 from 1.9% in 2022.

In Europe, AUM rose slightly in Euros from €28 trillion to €29 trillion but remained flat at £25 trillion in sterling terms, reflecting ongoing inflation and slower growth. Japan's AUM increased from ¥888 trillion to ¥909 trillion, but in sterling, AUM dropped from £6 trillion to £5 trillion due to currency depreciation. While still significant, Japan's global share of AUM fell to 5%.

Overall, global AUM recovered 12% to $119 trillion[3] (£95 trillion) after a 10% decline in 2022, with the US leading the rebound. However, Europe's flat performance and Japan's currency challenges underscore the uneven nature of the recovery across key regions.

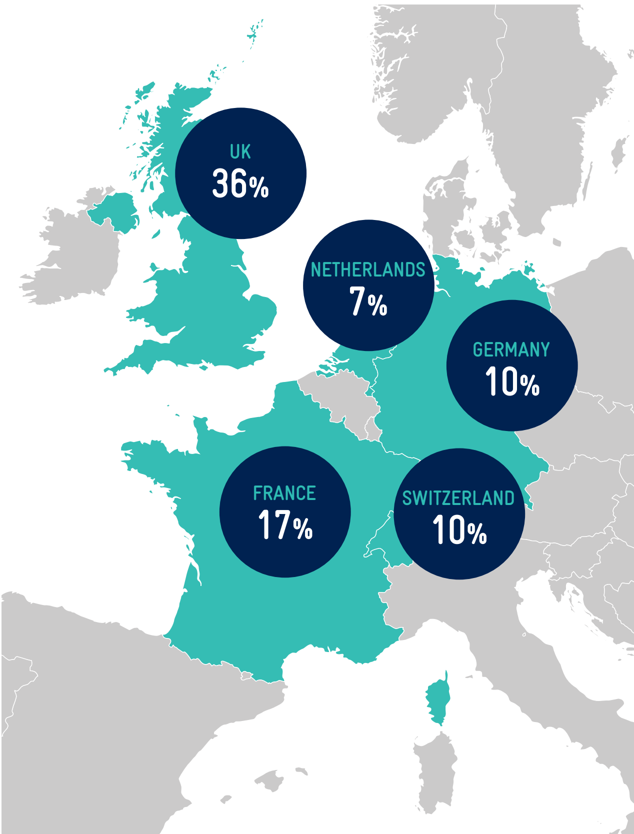
TABLE 1: GLOBAL ASSETS UNDER MANAGEMENT (2023)

	AUM (local currency)	AUM (£ equivalent)
United States[4]	$56 trillion	£44 trillion
Europe[5]	€29 trillion	£25 trillion
Japan[6]	¥909 trillion	£5 trillion

Source: HM Revenue & Customs, Boston Consulting Group, EFAMA, Nomura Research Institute

Figure 3 shows the share of assets managed in different European countries. The UK has the greatest market share of European assets at 36%, a slight decrease from the 37% recorded in 2021. The next three largest centres are France (17%), Switzerland (10%) and Germany (10%), the combined share of these markets is almost equivalent to the UK. The top ten countries have a 91% share of the European investment management industry.

FIGURE 3: ASSETS UNDER MANAGEMENT IN EUROPEAN COUNTRIES (DECEMBER 2022)



Source: EFAMA Asset Management Report (2023)

[3] Boston Consulting Group, AI Transformation: Global Asset Management 2024.
[4] Boston Consulting Group, AI Transformation: Global Asset Management 2024.
[5] EFAMA, Our industry in numbers (data estimated as of September 2023).
[6] Japan's Asset Management Business 2023-24, NRI (data as of March 2023).

MULTIPLE DIMENSIONS OF INTERNATIONAL ACTIVITY

A key driver of the scale of total AUM is the international nature of the UK investment management industry, both in terms of the customers and businesses served and the underlying assets. Figure 4 highlights four key metrics that illustrate the extent to which the UK investment management industry is highly international – and becoming more so over time:

- Assets managed on behalf of overseas clients.
- Assets invested in overseas markets.
- Overseas assets delegated to UK based portfolio managers.
- Assets managed by firms headquartered overseas.

OVERSEAS CLIENT MARKET

Chart 4 (overleaf) illustrates the distribution of assets for UK and overseas clients. By the end of 2023, overseas client assets accounted for 49% of the £9.1 trillion of UK-managed assets. Since 2019, the overseas segment of client assets continues to make up an increasing share of total UK assets.

Determining the factors behind changes in the number of overseas clients is difficult without flow data at the AUM level. The shifts likely result from a combination of factors, including client behaviour, operational decisions related to investment management capabilities, capital market returns, and exchange rate fluctuations.

There has been a gradual shift in the client base, with assets managed for overseas clients rising by one percentage point in 2023 to 49%. Over the decade, this share has increased from 38% in 2013 to 49%, reflecting an eleven-percentage point rise. This trend indicates that the UK continues to be seen by overseas clients as a centre of excellence for portfolio management.

FIGURE 4: FOUR MEASURES OF A GLOBAL INDUSTRY (2023)

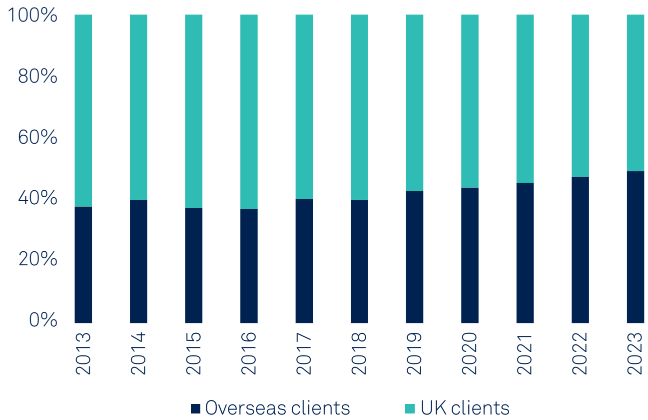
CUSTOMERS
49% of total assets managed in the UK are for overseas customers. Over half of those are in the rest of Europe.

MARKETS
78% of the shares managed in the UK are invested in overseas markets – for domestic and overseas customers.

COMPANIES
The UK attracts firms from around the world. Companies headquartered outside the UK are responsible for **63%** of total assets managed here.

ECONOMIC CONTRIBUTION
6.7% of total UK service exports from the investment management industry.

CHART 4: CHANGE IN PROPORTION OF UK AND OVERSEAS CLIENTS (2013–2023)



Source: The Investment Association

Figure 5 illustrates the regional distribution of overseas client assets. Nearly half (£4.5 trillion) of AUM is managed on behalf of overseas clients. Overseas client AUM grew by 7% over 2023, up from £4.2 trillion at the end of 2022:

- Assets managed on behalf of Europeans saw the biggest change over the last 10 years, increasing 71% to reach £2.5 trillion in 2023. Europeans remain the largest overseas client group and AUM grew by 5% in 2023.
- North American client assets grew 9% to reach £925 billion in 2023. US clients account for approximately 21% of the overseas client base.
- The highest levels of growth in overseas client assets in 2023 were seen for Middle Eastern clients (12% growth) and Latin American clients (11%). Growth in Latin American client assets was from a low base.
- Assets managed on behalf of Asia-Pacific clients grew by approximately 6% to £720 billion from £680 billion in 2022.

FIGURE 5: ASSETS MANAGED ON BEHALF OF OVERSEAS CLIENTS (2023)

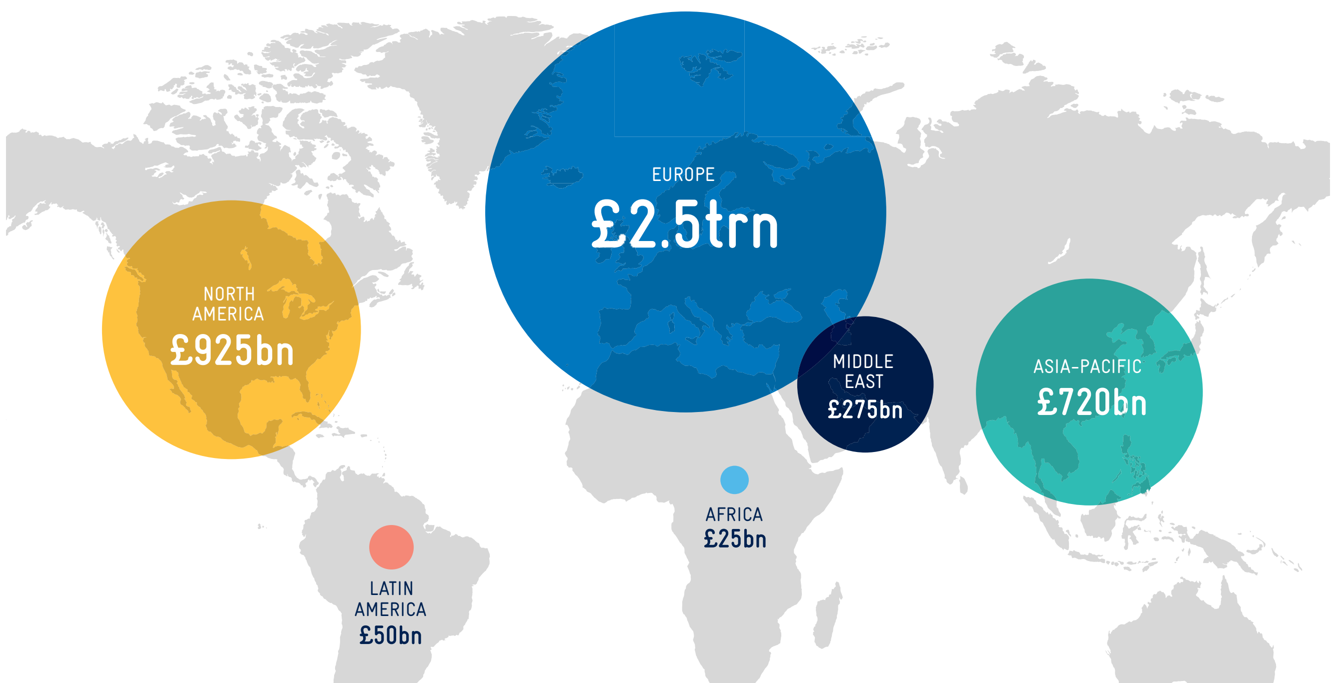
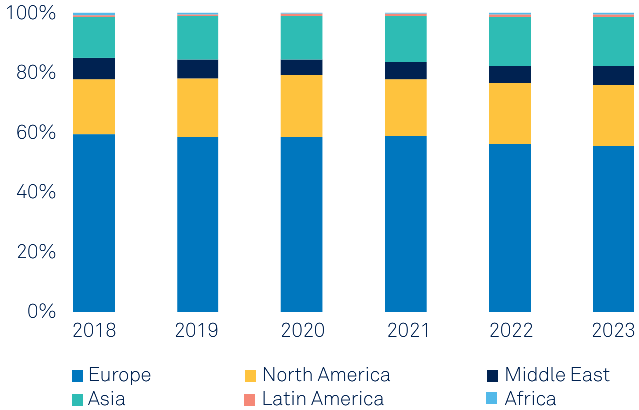


Chart 5 illustrates the change in the percentage share of assets managed on behalf of overseas clients by region:

- The proportion of assets managed on behalf of North American clients has steadily increased, growing from 19% in 2018 to 21% in 2020. This share has remained stable since the pandemic and remains at 20.7% in 2023.
- Europe's share of managed assets has consistently decreased, dropping from 59% in 2018 to 55% in 2023. While Europe still represents the largest proportion of assets, its dominance is gradually declining, indicating that assets managed on behalf of clients from other regions are growing at a faster rate.
- The share of assets managed on behalf of Middle Eastern clients is 6% in 2023, growing from 5% in 2020.

CHART 5: PROPORTION OF OVERSEAS CLIENT ASSETS BY REGION (2018-2023)



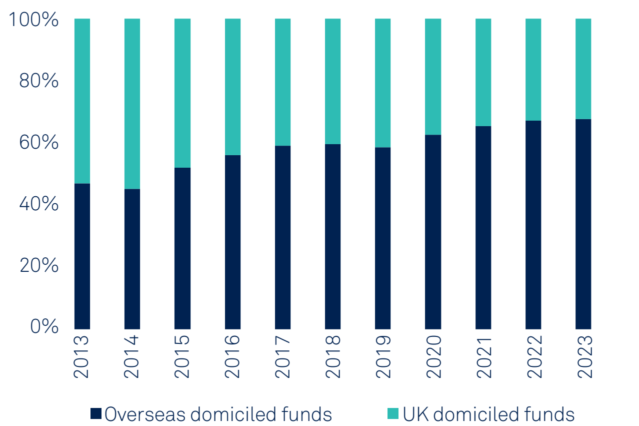
Source: The Investment Association

SERVICES TO OVERSEAS FUNDS

UK-managed investment fund assets in both UK and overseas domiciled funds stood at £4 trillion by the end of 2023, which is unchanged from 2022. As illustrated in Chart 6[7], 68% of these assets (approximately £2.7 trillion) sit in overseas domiciled funds where the portfolio management takes place from the UK:

- Luxembourg accounted for 15% of overseas domiciled assets managed from the UK in 2023, the same level recorded the previous year.
- Dublin remains the largest overseas domicile for UK-managed assets representing a 30% share in 2023. This share has fallen by three percentage points over 2023.
- The share of UK-managed assets domiciled in the UK is 32%, down from 33% the previous year.
- Overall, 54% of UK-managed investment fund assets are in funds domiciled in Luxembourg, Ireland or within the European Economic Area (9%). The proportion of assets in funds domiciled from outside the EEA is much smaller at 13%, although this is a one percentage point rise from 2022.

CHART 6: PROPORTION OF ASSETS MANAGED IN UK AND OVERSEAS FUNDS (2013-2023)



Source: The Investment Association

[7] Chart 6 includes data captured from open-ended funds, investment trusts, ETFs, hedge funds and money market funds (MMFs).

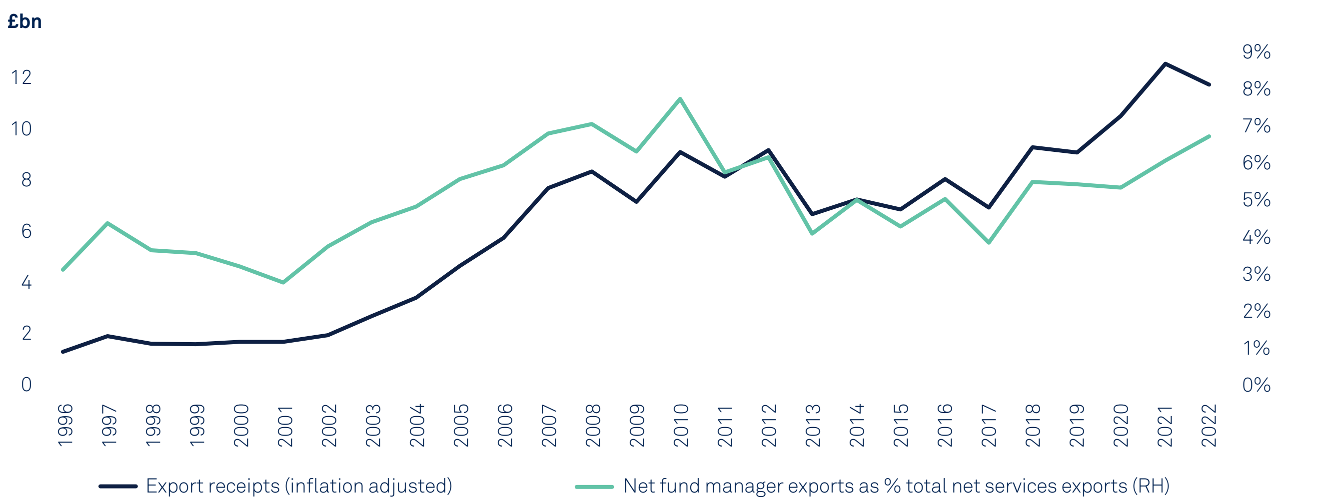
IMPORTANCE TO UK SERVICE EXPORTS

The UK investment management industry has a strong track record in providing services to international investors and has seen continued growth in the delegation of portfolio management from overseas domiciled funds to UK based portfolio managers. UK investment management is an important example of an industry that has seen success in exporting its services globally.

Chart 7 examines the industry's contribution to total UK service exports earnings from 1996 to 2022. Whilst industry export earnings decreased by 7% in 2022 to £11.7 billion compared with 2021, industry export earnings in 2022 are still the second highest in ONS data on an absolute basis. The revised ONS data show that industry export earning start to rise consistently year-on-year between 2002 and 2008 (from £1.7 billion to £7.5 billion). Since 2020, inflation-adjusted export earnings have consistently been over £10 billion annually.

The industry's contribution to total net exports stood at 6.7% in 2022, this is marginally up from 6.1% in 2021 and higher than the consistent 5.5% contribution observed between 2018 and 2020. The 2010's peak contribution of 7.8% was largely driven by the slowdown in the growth of other services exports following the Global Financial Crisis.

CHART 7: INDUSTRY EXPORT EARNINGS AND RELATION TO UK SERVICES EXPORTS (1996-2022)



Source: The Office of National Statistics