Executive summary

The asset and fund management industry has grown significantly in the last decade, with surveys indicating about 65 percent growth since 2007, to over USD 80 trillion in assets under management worldwide.

As its importance to the world financial system – linking those with money to invest with enterprises and activities that require funding – is increasingly recognized, so both the industry and the regulators that police the sector become more prominent.

The industry and regulators are coming under pressure from a range of “external” voices – demanding investors and consumer groups, clamoring political and economic needs, changing priorities and hopes of civil society, an increasingly noisy press, the explosion in social media and the rapid growth of new technologies.

This sea of voices is directly influencing the regulatory agenda and increasing expectations on the industry. A fundamental rethink of firms’ mindset and investment offerings is required.

Structures and remits are in flux as regulators and supervisors adapt their agendas and working methods to a changing environment. Supervision of the sector is both broadening and deepening, and supervisors are turning to technology to help them perform their roles more efficiently.

There is new rule-making in some areas and in some jurisdictions, but agendas are increasingly focused on the monitoring and review of the myriad of post-crisis rules. There are demands from policy-makers and regulators for yet more data, and there are demands from the industry and institutional investors for a rationalization of requirements and for greater global regulatory convergence.

The identification and containment of systemic risks became the overwhelming priority of policy-makers and regulators after the 2008 financial crisis. Eleven years on, the financial crisis is now a distant memory for many, but policymakers are still highly attuned to the fragility of markets. Again, there are calls for more data.

As the asset management industry expands, so debate around it intensifies, but there are conflicting views about the most appropriate regulatory response. Regulators are deepening their examination of systemic risks in the sector, with a focus on liquidity and leverage. Exchange-traded funds and money market funds remain on the watch list.

As we emphasized in last year’s report, governance and conduct are global regulatory preoccupations. That ethos is spreading. It is no longer enough for firms simply to adhere to rules and regulations. They need to think more broadly about the impact of their culture and conduct. The public loudly demands that firms serve their clients with skill and care.

There are increasing calls worldwide for individuals within the financial services industry to be held personally to account for their action. Diversity, remuneration and stewardship are all on the agenda. Fund distribution and financial advice rules are being further strengthened, and the industry’s governance of delegated or outsourced activities is under scrutiny.

The regulatory search continues for perfect disclosures to investors, with a focus on the calculation and presentation of costs and charges. A small but increasing number of regulators are also probing the level of costs, in response to persistent voices that call for a different equilibrium to be found between what is reasonable for investors to be charged and the profits of investment firms. “Closet trackers”, the use of benchmarks and performance fees are all under the regulatory microscope.

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Many markets are opening, but others are becoming more restrictive and there remain frictions in the cross-border distribution of investment funds. In particular, “Brexit” is impacting cross-border flows between the UK and the rest of the EU, and this impact is likely to increase. Meanwhile, the EU regulatory approach to delegation is being more stringently supervised, with US and Asian firms potentially affected, too.

Elsewhere, use of the Asian fund passports remains low but is slowly rising. Bilateral fund arrangements are flourishing, developing economies continue to open up their capital markets to foreign firms and investors, and new fund structures seek to compete. Around the globe, there are new opportunities for asset managers and investment funds in the retirement savings market, but in some cases more conditions or restrictions are being imposed.

Voices arguing for climate-aware investing and carbon controls are increasing. Demand for ethical treatment of employees, customers and other stakeholders is also growing, as is indignation about poorly-managed companies. Consideration of environmental, social and governance (ESG) factors is now a must.

The investor voice is already having a significant impact on asset managers’ investment processes and strategies. Regulators in some jurisdictions are seeking to catch up, but their responses vary, and industry and investor reactions to their proposals are mixed. Most, but by no means all, institutional investors believe sustainability should be incorporated into portfolios. However most, but not all, investors believe that ESG measures should not be mandated.

Meanwhile, fintech developments are coming thick and fast, and are already a powerful external driver of regulation. The regulators have a dilemma: they are called on to support and help nurture nascent industries that increase efficiency and help consumers to access financial services, but they are concerned about new and heightened risks, in particular the protection of personal data.

Regulators are rethinking how they regulate the industry, both new fintech entrants and existing businesses that are encompassing fintech developments. Existing conduct rules were largely written in a paper and face-to-face world. Are the rules fit-for-purpose in a digital age?

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<th>Key questions for CEOs</th>
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<td>• Are we fundamentally reviewing our business ethos and offerings in recognition of stakeholder demands?</td>
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<td>• Are we anticipating evolving regulatory agendas and supervisory practices? Can our data management and analysis systems accommodate yet more data demands?</td>
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<td>• Do our governance model, culture and conduct conform to new regulatory expressions of good practice and increasing client expectations, including accountability, remuneration, diversity and stewardship?</td>
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<td>• Are our disclosures to investors transparent and meaningful, and do our services and products demonstrate an appropriate and acceptable balance between what investors are charged and the firm’s profits?</td>
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<td>• Are we quickly identifying new market opportunities and responding to increased restrictions?</td>
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<td>• Do we recognise that consideration of ESG factors is now a must? Are we in front of or behind the curve in developing our investment processes and product offerings?</td>
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<td>• Are we both embracing technological developments and ensuring full consideration of the attendant risks?</td>
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A sea of voices – Evolving asset management regulation
The full report is available to download on kpmg.com/eamr2019

Contact us

Tom Brown
Global Head of Asset Management
KPMG International
T: +44 20 7694 2011
E: tom.brown@kpmg.co.uk

Julie Patterson
Head of Asset Management, Regulatory Change
FS Risk & Regulatory Insight Centre, EMA
T: +44 20 73112201
E: julie.patterson@kpmg.co.uk