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BUSINESS INSIGHTS

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Trends in Asset Raising and Cross-Border Distribution

More and more U.S. managers are looking for investor’s capital in Europe – but European asset managers as well are looking over the Atlantic.

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The confrontation with the different countries in the European Union as well as the regulatory restrictions and business aspects pose major challenges for U.S. fund managers. But similar challenges are present in the opposite direction as European fund managers wonder about the best way to enter the attractive investment location that is the United States. How does cross-border distribution succeed in today´s world?

Clear location preference for fund launch in Europe

Identifying the right fund structure is easy, as European investors have a clear preference for EU fund structures. In the area of financial assets, the UCITS fund has successfully established itself worldwide as a trustworthy brand. In addition to their existing US vehicles – such as a US 40-Act fund, named after the investment company act of 1940, a British Virgin Islands (BVI) – or Cayman fund structure – more and more US managers are therefore offering their investment strategies in a new legal framework. Luxembourg is preferred.

Due to its regulatory and infrastructural environment, the country remains as the prime location for fund domiciliation in Europe: 35.9% of European UCITS are launched in Luxembourg, 18.5% in Ireland and 12.3% in Great Britain. It is important to note the differences in percentages Luxembourg maintains, despite the stronger American cultural ties to the Anglo-Saxon culture.

Country	Net Assets of UCITS Industry (in millions of EUR)	Share	Number of UCITS Funds
Luxembourg	3,380,943	35.9%	10,026
Ireland	1,746,418	18.5%	4,193
United Kingdom	1,160,903	12.3%	1,983
France	885,287	9.4%	3,164
Switzerland	443,522	4.7%	891
Germany	365,640	3.9%	1,886
Sweden	309,714	3.3%	542
Italy	250,459	2.7%	1,037
Spain	216,422	2.3%	1,723
Denmark	125,856	1.3%	624

Source: European Fund and Asset Management Association, EFAMA (2017)

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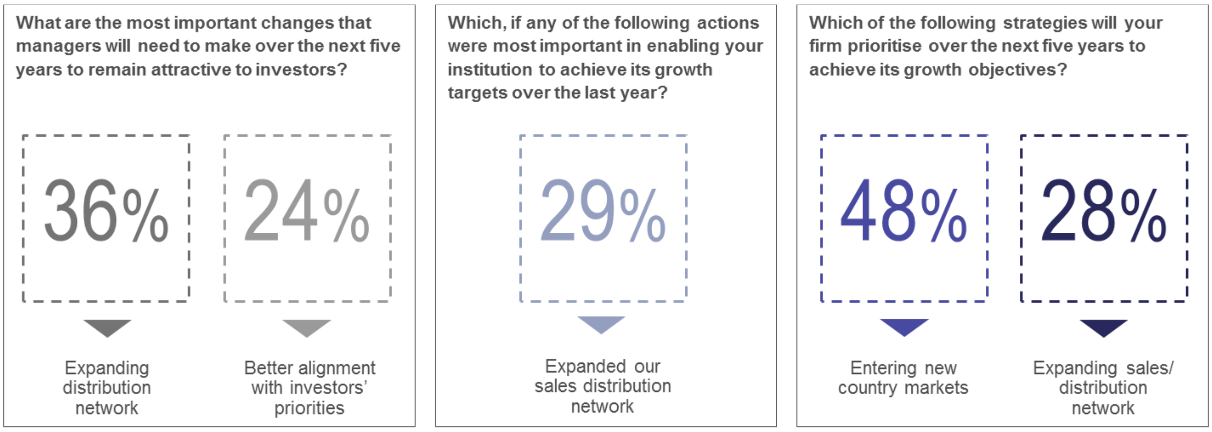
Among foreign fund initiators in Luxembourg, the United States (U.S.) currently tops the list compared to other countries with 20.5%, according to the CSSF.

Thanks to UCITS, the cross-border distribution of funds has become easier over the years due to the “marketing passport”. Following the implementation of the Alternative Investment Fund Managers Directive (AIFMD) in the summer of 2013, there has also been increased change in regard to alternative investments; as a result the offer of adequate structures in this area is much more diverse. With the implementation of the investment strategy as a UCITS fund or an AIF (Alternative Investment Fund) structure, U.S. companies have access to investors worldwide through European markets. For example, UCITS is in demand in various countries in Latin America and in the Asia-Pacific region for pension funds and high net-worth individuals. A similar trend is expected for the AIFMD structures in the coming years.



Source: New Rules of Engagement, State Street Corporation (2017)

In a quickly changing investment industry environment, a recent study found that distribution is high on the agenda for alternative asset managers next to delivering bespoke solutions for individual clients. Many alternative asset managers also recognise that it makes more economic business sense to outsource services to a third-party service provider, which can perform functions more efficiently.

Access to European fund selector is fiercely contested

While cross-border distribution is simplified, access to the actual target group, European fund selectors and institutional investors, is highly competitive. The rising pressure from risk management and audit departments, cost savings and efficiency demands, time constraints and the increasingly centralized decision making underscore the importance of streamlined processes and readily available information. Last but not least, digitisation and new partnerships with Fintech companies have the power to change sales channels and thus the cooperation and communication between investors and asset managers. In the future this effect will only increase as easy access to information and transparency will be essential for decision makers. This is as a successful brand in the domestic U.S. U.S. market does not automatically correlate to a steady inflow of investor capital in Europe. The widespread idea of Europe as a large, unified market for fund distribution needs to change in order to be successful. This in regard on the supplier side requires the ability and willingness to adapt services to different target groups in European countries.

Increasing interest in alternative investment strategies

There are good reasons for U.S. managers with actively managed strategies to rely on European capital and to mitigate competitive pressure through the dominance of passively managed strategies in the USA. While Exchange Traded Funds (ETFs) and other passively managed funds have gained more and more market share in Europe in recent years, according to Lipper Thomson Reuters actively managed strategies still account for 88% of the market. ETFs and index trackers are far behind with 8% each. In addition, due to low interest rates and despite the general preference for equity and bond funds there is interest among asset managers, family offices and insurance companies for alternative investment strategies out of the USA. The U.S. market is regarded as the hub of the hedge fund industry and offers managers an attractive track record and many years of experience.

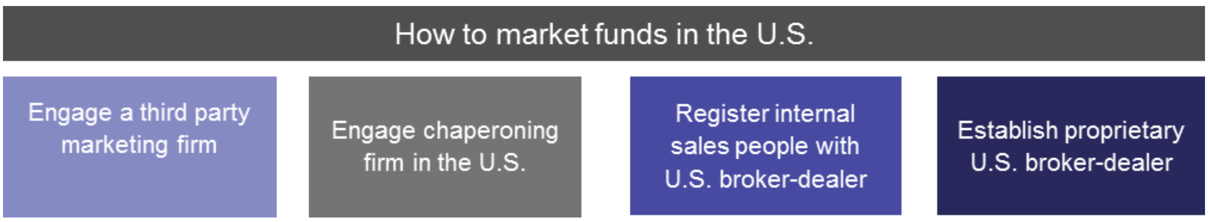
Finding the right partner in Europe

In order to obtain interest and to ultimately become profitable for local investors U.S. Managers require a partner like LRI Group to select appropriate structure and distribution countries. Because entering new markets and building a separate asset management company is cost and resource intensive process, many investment managers give this responsibility to an external management company such as LRI Group and focus on their core competencies: portfolio management and revenue generation.

Unlike other providers in the market, fund initiators maintain their own brand at LRI Group and are positioned accordingly in the market. The fund managers themselves therefore do not have to raise large capital and utilise resources to build up middle and back office structures. The portfolio management function will be assigned to a U.S. investment advisor – the docking to a global distribution network of placement agents, consultants, lead and event providers and not least investors themselves is essential. Together with selected partners, U.S. managers can make their fund distribution smart, practice oriented and optimize and develop it cost-effectively.

Trend is also recognisable vice versa

In Europe, many fund managers still shy away from taking the leap across the pond. The fear of the U.S. Securities and Exchange Commission (SEC) and regulatory pitfalls leaves many doubting whether it is worth to go overseas. But the market volume of around USD 40 trillion, according to the report of Cerulli Associates is immensely appealing. According to EFAMA, the U.S. still accounts for the world's largest market for investment funds with 46.4%. Therefore, particularly in the minds of fund managers, many hurdles are to be overcome. It important to understand the difference between European and US regulatory regimes as the marketing of mutual funds in the U.S. itself is relatively straightforward. In addition to the general consideration of the target group and the appropriate legal clause, the fundamental question of choosing the right partner is also decisive. The central starting point for sales and distribution in the U.S. is the registration as a Broker-Dealer or rather the appointment of a broker-dealer, as the registration as an investment adviser does not yet allow fund distribution.



Source: Foreside Financial Group

Finding the right partner for the U.S. while marketing in new areas of law may involve new regulatory and investment risks, however such risks offer the opportunity to diversify the investor base in the long run. Through working with experienced fund advisors, European asset managers seeking to market mutual funds in the U.S. can reduce their regulatory and financial risk while finding a way through the tax and regulatory system.

About LRI Group

LRI Group is a leading independent investment services company based in Luxembourg. It provides asset managers and investors with nearly three decades of experience in structuring and administration of traditional and alternative investment strategies. Established in 1988, LRI Invest S.A. acts as Super Management Company (Super ManCo) being authorised as Alternative Investment Fund Manager (AIFM) and as UCITS Management Company in Luxembourg. Through LRI Invest Securitisation S.A. it also operates a securitisation platform for a variety of alternative investment underlyings for institutional investors. With LRI Depositary S.A. it also provides depositary services and can act as Register and Transfer Agent for alternative investment funds. LRI Group manages EUR 3 billion in Real Assets especially in Real Estate, Private Equity and Debt and EUR 9 billion in Financial Assets such as Multi Asset Funds, Liquid Alternatives and Funds of funds and has 100 staff.
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