



Vision 2025

*The future of Hong Kong's
fund management industry*

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Foreword



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Hong Kong's fund management industry is experiencing a period of significant change and disruption in light of the ongoing global macroeconomic uncertainty, and more local challenges such as an ageing population, increasing competition, talent shortages, rising compliance costs and fee pressure. In more recent times, the COVID-19 pandemic has also had an impact on investor sentiment both in Hong Kong and worldwide. However, while the effects of the pandemic are likely to be felt for the foreseeable future, we believe that the long-term vision and opportunities for the growth and development of Hong Kong's fund management industry remain clear and unchanged.

This report, jointly authored by the Hong Kong Investment Funds Association and KPMG China, aims to identify these growth opportunities and to provide an informed perspective on the future of Hong Kong's fund management industry.

The results from a survey and interviews conducted as part of research for this report indicate a positive outlook for the future of Hong Kong's fund management industry, driven by growth opportunities related to the opening up of mainland China's asset management industry, the ongoing development of the Greater Bay Area (GBA), advances in technology-enabled client experiences and ESG investing.

Indeed, the last few years have seen a significant amount of change in mainland China as its financial services industry and capital markets open up to international investors. The scrapping of foreign ownership caps on fund management companies this April, and plans to launch a 'GBA Wealth Management' scheme are welcome developments for fund managers.

Meanwhile, technology-driven change is expected to continue, with investors demanding an improved, increasingly digital user experience. We believe that in 2025, asset managers will no longer be just product providers, and will instead become firms that provide solutions to investors' investment-related needs.

ESG investing will also become the 'new normal', with investors increasingly demanding that asset managers integrate ESG into their investment processes and offer more sustainability-related products.

Hong Kong's fund management landscape in 2025 will look significantly different to its current form today. A number of challenges lie in the way, but they can be addressed by close collaboration and active engagement between industry stakeholders to find smart, sensible solutions. In this report, we put forward recommendations which, if adopted, will help accelerate the growth of Hong Kong's fund management industry and maintain the city's position as a leading asset management hub.

We would also like to thank all the survey respondents for taking the time to provide their input, and the more than 20 senior industry executives who kindly agreed to be interviewed. The valuable views and insights we have received have been instrumental in shaping and enriching this report.

We hope that this report provides you with valuable insights, and we welcome the opportunity to discuss these findings further.

Executive summary

Facing ongoing global macroeconomic uncertainty and a number of short and long-term challenges, Hong Kong's fund management industry is experiencing a period of significant change and disruption. Amid this rapidly evolving landscape, there are a number of notable opportunities for the industry in Hong Kong to develop and grow in the next five years.

This report, jointly authored by the Hong Kong Investment Funds Association (HKIFA) and KPMG China, aims to provide an informed perspective on the future of the fund management industry in Hong Kong, identify current and future growth opportunities and challenges, and develop recommendations to help Hong Kong maintain its position as a leading fund management hub. This publication follows on from the inaugural report, 'Vision 2020', that was published in 2015.

The report is largely based on an online survey of HKIFA member institutions as well as interviews with more than 20 senior industry executives. The survey and interviews were conducted from November 2019 until January 2020.¹

The findings show that despite challenging times ahead, interviewees and survey respondents maintain a positive outlook on the future of Hong Kong's fund management industry, underpinned by the city's experienced talent pool, product diversity, open market, robust regulatory framework and proximity to mainland China. This optimism in the future of the industry is also driven by growth opportunities related to the opening up of mainland China's asset management industry, the ongoing development of the Greater Bay Area (GBA), advances in technology-enabled client experiences and ESG investing.

The last few years have seen a significant amount of change in mainland China as its financial services industry and capital markets open up to international investors. The scrapping of foreign ownership caps on fund management companies this April presents a welcome opportunity for international firms, while plans to launch a 'GBA Wealth Management Connect' scheme will enhance the cross-boundary flow of financial products between mainland China and Hong Kong. For companies with an existing presence in mainland China, evolving their current operating models into

¹ Note: The vast majority of the surveys and interviews were conducted prior to the outbreak of COVID-19.

a coherent target state will be a critical objective, while those who have not yet established a presence on the mainland will need to carefully consider their options for market entry.

Meanwhile, technology-driven change is expected to continue, with investors demanding an improved, increasingly digital user experience. Our interviewees' view is that the next few years will see technology more focused on supporting the industry – achieving efficiencies and making it easier for clients to invest – rather than replacing parts of the industry completely. In 2025, asset managers will no longer be just product providers. They will instead become firms that provide solutions to investors' investment-related needs. This will necessitate partnering and co-developing tools with intermediaries – in Hong Kong, these are primarily banks – to better understand clients' needs and create appropriate portfolios for them.

ESG investing is also slated to become the 'new normal', with investors increasingly demanding that asset managers integrate ESG into their investment processes and offer more sustainability-related products. HKIFA and KPMG believe that a joint effort between regulators and asset managers is needed to create clear ESG standards for Hong Kong.

It is clear that Hong Kong's fund management landscape in 2025 will look significantly different to its current form today. A number of challenges lie in the way, but they can be addressed by close collaboration and active engagement between industry stakeholders to find smart, sensible solutions. The ability to capitalise on the sizeable opportunities related to the development of mainland China, technology and ESG will be key in the coming years to drive growth and ensure a brighter future for Hong Kong's fund management industry.



Key findings

Despite challenging times ahead, interviewees and survey respondents maintain a positive outlook for the future of Hong Kong's fund management industry, driven by growth opportunities related to the opening up of mainland China's asset management industry, the ongoing development of the GBA, advances in technology-enabled client experiences and ESG. Close collaboration and active engagement between the industry and regulators will also be key to driving the development of the fund management industry.

32% expect growth of more than **30%** in total AUM managed by organisations' Hong Kong investment management business in the next five years



Top three trends that will have the biggest impact on Hong Kong's fund management industry

By 2025

Beyond 2025



Regulatory change



Ageing population



Fee pressure



Application of artificial intelligence



Rise of the Greater Bay Area as a financial centre



Increasing connectivity

79% expect their total AUM originating from mainland China to grow by more than **10%** in the next five years



Mainland China remains a key growth market for the industry as it opens up its asset management sector to foreign investors. The ongoing development of the GBA also presents significant business opportunities for Hong Kong.

42% do not have a strategic plan for the GBA, while **37%** expect to formulate a strategy in the next 12 months



A greater proportion of organisations' technology investment is expected to be allocated towards data and client-facing technology



Technology-driven change is expected to continue, with investors demanding an improved, increasingly digital, user experience; this is particularly the case for younger, digitally savvy clients who demand instant, personalised services and lower fees. That said, many clients still prefer a human touch when it comes to making sizeable investments.

79% expect their investment in technology to increase in the next 12 months



89% agree that "Providing sustainable investing-related products is increasingly important to clients"



ESG investing will become the 'new normal', with pension funds and institutional investors continuing to raise the bar for ESG. Greater collaboration between industry stakeholders is needed to create clear ESG standards for Hong Kong.

Greatest skill shortages expected in the local labour market: ESG specialists




Key recommendations


The survey and interview findings culminated in a number of recommendations which, if adopted, will help accelerate the growth of Hong Kong's fund management industry and maintain the city's position as a leading asset management hub.

Overcoming industry challenges


Demographics

-  Hong Kong's rapidly ageing population is a key challenge that requires a multi-pronged solution, including:
 - The creation of post-retirement products and the broadening of investable asset classes for MPF members.
 - The introduction of incentives such as the government's matching of voluntary contributions to spur higher levels of contributions into the MPF system.
 - More, better investor education to help people understand their post-retirement financial requirements, and therefore their current required level of savings; this should encourage them to increase engagement with, and contributions to, their pensions scheme.




Short-term investing mindset

-  Design investor education and incentive systems to encourage long-term investing to improve retail investors' outcomes. This will also help to address the issue of excessive portfolio churn and reduce the fees that investors pay in rebalancing their portfolios.



Mainland China

-  The Hong Kong government, local regulators and industry bodies should partner with authorities in mainland China to:
 - Enhance the existing MRF arrangement between mainland China and Hong Kong by relaxing the 50% cap, as well as allowing the delegation of investment functions outside of Hong Kong to promote a greater variety of global products.
 - Implement the proposed framework for the GBA Wealth Management Connect scheme, with clear guidance on regulatory requirements, products and operational logistics; the scheme should also consider including non-Hong Kong-domiciled funds.

Technology

-  In order to avoid becoming commoditised product providers, asset managers should seek to partner with intermediaries to co-develop tools and solutions to better understand clients' needs and create appropriate investment strategies.
-  To accelerate the growth of AUM in the industry, fund managers should focus on segments that are currently underserved, including the younger, next generation of investors. Solutions like robo-advisory and innovative fintech will assist, while virtual banking may also open up a new route to this segment.
-  The industry, universities and research and training institutes in Hong Kong should work together to develop education programmes and professional qualifications that equip current and potential future fund management staff with relevant tech skills.

ESG

-  At a minimum, asset managers should commit to producing climate-related financial risk disclosures and becoming signatories to the UN Principles for Responsible Investment.
-  The industry and regulators need to:
 - Fast-track the development of industry-wide standards for ESG in Hong Kong. The regulator is also encouraged to work with its counterparts in other key jurisdictions to achieve greater alignment on this issue.
 - Ensure that retail investors are properly informed about the benefits of ESG investing, and dispel the misconception that investing in ESG products means sacrificing returns.
 - Introduce an overarching framework in Hong Kong to maintain minimum standards and oversight of the ESG data provided by third parties, and to improve data integrity and credibility in the market.
 - Develop an industry-wide programme to offer structured ESG training and qualifications that combine both financial and ESG skills and knowhow, using the European Federation of Financial Analysts Societies' ESG Analyst certification programme as a reference.

Industry outlook

Despite challenging times ahead, interviewees and survey respondents maintain a positive outlook for the future of Hong Kong's fund management industry, driven by growth opportunities related to the opening up of mainland China's asset management industry, the ongoing development of the Greater Bay Area, advances in technology-enabled client experiences and ESG. Close collaboration and active engagement between the industry and regulators will also be key to driving the development of the fund management industry.

Amid ongoing global macroeconomic uncertainty – underpinned by slow growth and a low interest rate environment – asset management companies worldwide continue to face a number of challenges. Coupled with more local short and long-term issues such as an ageing population, increasing competition, talent shortages, rising compliance costs and fee pressure, Hong Kong's fund management industry is also experiencing a period of significant change and disruption. Recent social unrest and the outbreak of COVID-19 have also had an impact on investor sentiment in Hong Kong and the region.

Despite these challenges, interviewees and survey respondents for this report maintain a positive outlook for the long-term future of Hong Kong's fund management industry, citing a number of growth opportunities related to the opening up of mainland China's asset management industry, the ongoing development of the Greater Bay Area (GBA), technology-driven change and Environmental, Social and Governance (ESG) investing.

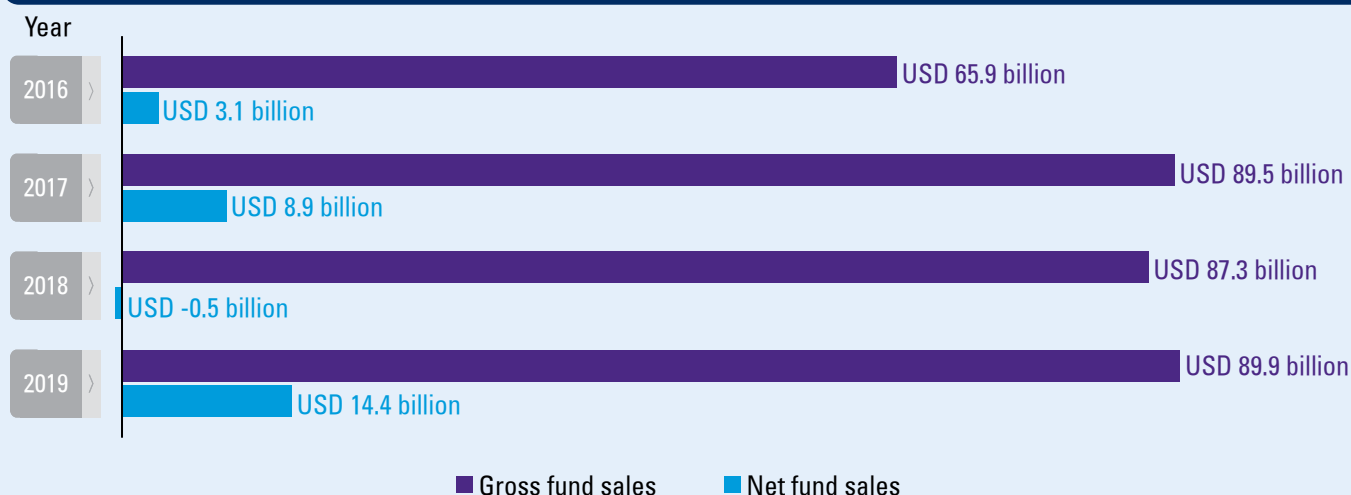
Hong Kong continues to be viewed as the leading asset management hub in Asia in 2025 and beyond, with interviewees and survey respondents citing the city's deep talent pool, investment product diversity, competitive and open market, robust regulatory framework, and cultural and business proximity with mainland China as key differentiators. This view is supported by the numbers, with the city attracting USD 89.9 billion in gross retail fund sales in 2019, according to HKIFA data.² Net retail fund sales for 2019 also hit USD 14.4 billion, compared to USD 0.5 billion in 2018 and USD 8.9 billion in 2017. Hong Kong is consistently seen as a highly desirable place to invest, with the city ranked third globally in terms of ease of doing business, up one place from 2018, according to the World Bank.³

² HKIFA, https://www.hkifa.org.hk/upload/Documents/Retail-Funds/Sales-Redemptions-Data/SnR_cht.pdf

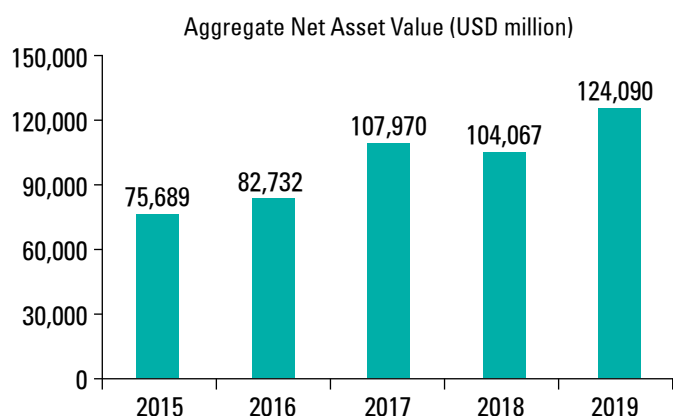
³ <https://www.info.gov.hk/gia/general/201910/24/P2019102400512.htm>

Industry overview

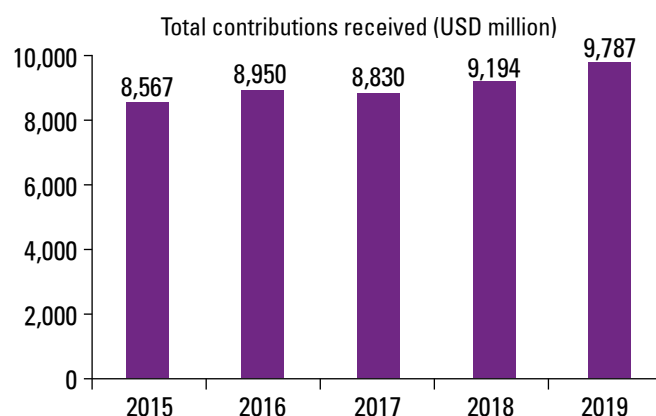
Hong Kong Retail Fund Gross & Net Sales



Aggregate Net Asset Values of all MPF Schemes



Contributions received – MPF Schemes



Net flow under the MRF between mainland China and Hong Kong

Northbound net flow

Year	Net inflow/(outflow) (RMB million)
2017	4,687.89
2018	(3,436.39)
2019	7,158.34
YTD (as of 29 Feb 2020)	621.07
Total net flow since MRF launch	16,763.14

Southbound net flow

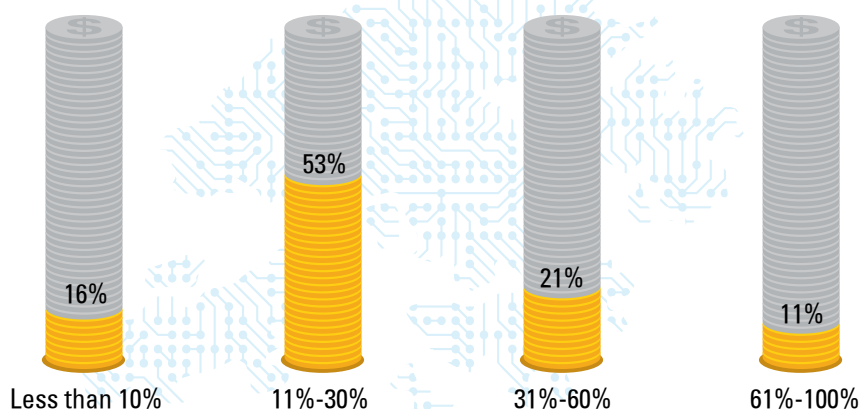
Year	Net inflow/(outflow) (RMB million)
2017	239.83
2018	96.55
2019	(167.46)
YTD (as of 29 Feb 2020)	42.51
Total net flow since MRF launch	286.14

Source: SAFE



A majority of survey respondents expect overall industry assets under management (AUM) in Hong Kong to grow annually by 5% to 10% over the next five years. When it comes to the growth of their own organisations, industry executives have an even more positive outlook. A majority of respondents expect to see their own firms grow more than 10% in total AUM over the next five years, with one-in-three expecting growth of more than 30% (Figure 1).

Figure 1: Expected growth in total AUM managed by organisations' Hong Kong investment management business in the next five years



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

Note: Numbers may not add up to 100% due to rounding



Regulation around AML/KYC and common reporting all adds operating costs to the firms.

Costs in relation to compliance are increasing, but at the same time revenues and profit margins are being squeezed, which is creating quite a challenge for the industry.

KP Luk

Head of Hong Kong,
Fidelity International

Navigating a challenging environment

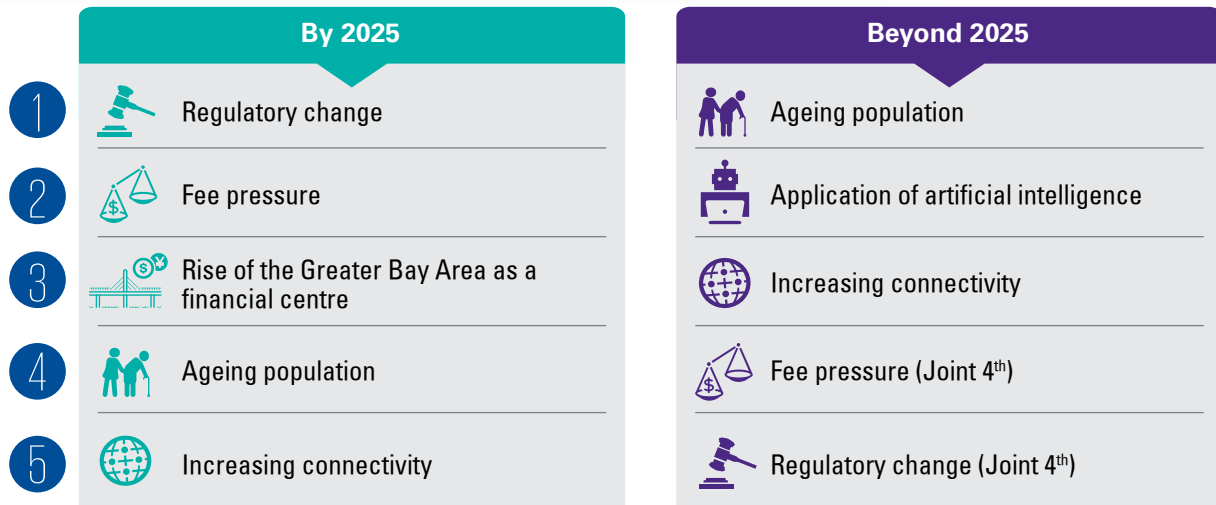
Achieving this growth will hinge on the industry's ability to overcome a number of local and global challenges that threaten to hamper the development of the market, while capitalising on the opportunities. 'Regulatory change', 'fee pressure' and the 'rise of the GBA as a financial centre' are identified by survey respondents as the top three trends that will have the biggest impact on Hong Kong's fund management industry in the next five years (Figure 2). This indicates a slight change in sentiment from five years ago, where respondents from the inaugural joint HKIFA-KPMG report in 2015 cited policy changes in mainland China, increasing connectivity and ubiquity, growing economic influence in the developing world and a growing middle class as the key factors likely to impact the sector.

Regulation

'Regulatory change' was cited by respondents as the trend likely to have the biggest impact on Hong Kong's fund management industry in the next five years. In addition to regulatory change, interviewees highlight the volume and complexity of certain regulation as a potential hindrance to growth and a cost pressure, while at the same time citing the need for greater regulatory clarity with respect to the development of initiatives within the GBA, as well as industry-wide standards for ESG. "Regulation around AML/KYC and common reporting all adds operating costs to the firms. Costs in relation to compliance are increasing, but at the same time revenues and profit margins are being squeezed, which is creating quite a challenge for the industry," says KP Luk, Head of Hong Kong, Fidelity International.

While the interviewed executives commended Hong Kong's regulators for maintaining a sound financial regulatory regime, some raised the issue of gold-plating – where regulations issued by internationally-recognised bodies are then supplemented with additional, local requirements – which has had the effect of actually hampering growth and efficiency in the industry. One example cited by some interviewees is that prior regulatory approval is needed in Hong Kong when changes are made to the prospectuses of UCITS funds, leaving fund managers often waiting for the regulator, and thus slowing down the process. Finding the right balance between investor protection and perceived overregulation will be key to further growing the market while safeguarding the interests of investors.

Figure 2: Trends that will have the biggest impact on Hong Kong's fund management industry



Source: 'Vision 2025' Joint HKIFA-KPMG Survey





We need to focus more on how well we manage our products, rather than slashing

fees to attract investors. If our net of fees performance still outperforms our competitors including passive products or ETFs without lowering our fees, then this demonstrates and justifies the fees that we charge.

Mandy Lui

*Head of Wealth/Retail Distribution,
Greater China & SE Asia,
Baring Asset Management*

Fee pressure

Meanwhile, fee and margin pressure continues to be a major issue for fund managers in Hong Kong, cited by survey respondents as having the second-biggest impact on the fund management industry in the next five years. Indeed, increasing competition in the industry, expectations from investors and intermediaries for lower fees, and growing demand for passive investing continue to squeeze margins.

Some fund managers, in turn, are adopting new strategies to boost revenue by increasingly looking at employing more passive investing strategies alongside their existing active management strategies, offering a wider range of investment options for their investors, and appealing to a more diverse group of clients. Most managers also emphasised the need to maintain or improve the quality of their products to justify their fees, especially for retail investors. "We need to focus more on how well we manage our products, rather than slashing fees to attract investors. If our net of fees performance still outperforms our competitors including passive products or ETFs without lowering our fees, then this demonstrates and justifies the fees that we charge," says Mandy Lui, Head of Wealth/Retail Distribution, Greater China & SE Asia, Baring Asset Management. "Fee pressure is coming from everywhere globally, not only in Hong Kong and Asia," agrees Eric Fu, Managing Director and Country Head, Greater China, Ninety One Hong Kong Ltd. "This is a fact that we have to deal with. We need to ensure that the quality of the products that we manage is high enough, so that we can communicate confidently to clients that they are paying for high quality products. We need to create a stronger proposition to defend."

Ageing population

Hong Kong's ageing population is viewed as a pivotal trend by respondents and interviewees in the next five years, and even more so beyond 2025. Government figures show that Hong Kong's residents enjoy an exceptionally high life expectancy compared to other economies – 87.7 years for women and 82.3 years for men as of 2018. Government projections from 2017 suggest that the ageing of Hong Kong's population will continue to accelerate significantly in the coming years. Excluding foreign domestic helpers, the proportion of elderly persons aged 65 and over is projected to increase from 17%, as recorded in 2016, to 31% in 2036, and rise further to 37% in 2066.⁴ In other words, in 2066 more than one-in-three persons in Hong Kong will be aged 65 and over.

This is no small sum, and also raises the question of how to serve the post-retirement marketplace in Hong Kong where pension options are limited. The Mandatory Provident Fund (MPF) system, now in its 20th year, has a short history compared to the pensions systems in the US and other developed economies. Many industry executives and Hong Kong residents alike believe that the MPF in its current form is not enough to support Hong Kong's post-retirement needs. While the Mandatory Provident Fund Schemes Authority has announced welcome enhancements to the MPF system such as the eMPF Platform, which aims to consolidate and streamline existing processes through innovative technologies, these will not solve the adequacy issue.

Survey respondents highlighted that the criticality of the post-retirement problem will only be exacerbated in the years to come as a forecast period of low inflation, low growth and low yield creates a tougher investing environment. "There are three things to solve when it comes to post-retirement: income replacement, longevity of savings, and in some cases, legacy or the transfer of wealth. The combination of these problems changes for each person," says Terry Pan, Chief Executive Officer, Greater China, Southeast Asia and Korea, Invesco Hong Kong.

⁴ Census and Statistics Department, Hong Kong SAR, <https://www.statistics.gov.hk/pub/B1120015072017XXB0100.pdf>

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The ultimate solution the industry is trying to deliver is to help people understand what they will need to invest today versus what they want as income in the future. The uncomfortable truth is that people do not want to take risks but everybody wants better return, so more education is needed to help investors realise and understand that there is always a trade-off between risk and return.”

Bruno Lee

Regional Head of Retail
Wealth Distribution, Wealth &
Asset Management, Asia,
Manulife Investment Management

“The challenge is then how to solve the problems and continue to find a diversified steady source of income without bearing too much risk and uncertainty. The average Hong Kong investor has a lot of choices, including stocks, bonds, funds, commodities, foreign exchange and property. This is where, from a regulatory standpoint, post-retirement needs to be thought about in a more holistic manner. Pensions investments can and should be diversified, not just in the most traditional asset classes,” says Mr. Pan of Invesco Hong Kong. Indeed, the introduction of new asset classes would give MPF scheme members the option of greater product diversity and sources of return/income; this could even encourage an increase in contributions to the MPF system and mitigate the adequacy issue.

As individuals near retirement, the ‘stabiliser’ in many ‘lifecycle’ retirement products is to increasingly look to exit risk-seeking assets and replace them with fixed income as the individual approaches their date of retirement. “Steady and regular income flows is a key requirement for retirees, and asset managers need to be able to provide simple, cost-effective product strategies that can meet their needs and provide them with the comfort that they can receive a stable income post-retirement,” says Isabella Chan, Head of Global Financial Institutions, APAC and Head of Retail Business, Greater China, Franklin Templeton Investments (Asia).

Interviewees highlighted that a number of studies have been conducted to find out the gap between the required level of saving before retirement and the actual level of savings needed to sustain incomes across an expected lifespan. “In Hong Kong, some findings have shown that there is about a five-year gap between the amount of money that people can have available to them post-retirement and their life expectancy. So how do we bridge that gap? The ultimate solution the industry is trying to deliver is to help people understand what they will need to invest today versus what they want as income in the future. The uncomfortable truth is that people do not want to take risks but everybody wants better return, so more education is needed to help investors realise and understand that there is always a trade-off between risk and return,” says Bruno Lee, Regional Head of Retail Wealth Distribution, Wealth & Asset Management, Asia, Manulife Investment Management.

There is general industry-wide consensus and acknowledgement that more needs to be done to address the issue of Hong Kong’s ageing population and the post-retirement problem it will create. Ultimately, increasing people’s engagement with their pension scheme will help them to better understand their post-retirement options, their current saving requirements based on their future spending needs, as well as the products that are available to them today. Some industry members have called on the government to introduce more incentives to encourage increased pension contributions, such as matching the voluntary contributions of MPF members, as well as the introduction of further tax incentives to spur more voluntary contributions into the MPF system. One recommendation supported by the HKIFA is to separate the HKD 60,000 tax deduction limit that is currently on both MPF tax deductible voluntary contributions and Qualifying Deferred Annuity Policies so that each option is eligible for its own deduction amount of HKD 60,000.

Interviewees note that tackling the problem will require a multi-pronged solution, as well as collaboration between stakeholders in Hong Kong. “Incentives have been introduced in Hong Kong such as extending tax deductions to some voluntary contributions, and one of the objectives of the upcoming eMPF platform is to create room to reduce fees. The funds industry needs to play a part in ensuring that we have well-designed products, and that we have kept pace with the way that clients want to engage with us. We as an industry need to think about responses and how to help,” says Steven Wells, Director, APAC Client Product Strategy, BlackRock.



There is a need for the industry to develop attractive long-term income paying products

for post-retirement. Hong Kong has a significant pension challenge, and it is not going to be solved by any sole group of agents in the system. Solving the post-retirement and pensions problem will require joint action from all relevant stakeholders, including players in the industry, regulators, government employers and employees.

Bonn Liu

Partner, Head of Asset Management,
ASPAC, KPMG China

Short-term investing mindset

Another challenge highlighted by a number of interviewees is the short-term investment mindset of many retail clients in Hong Kong, and the corresponding issue of excessive churn rates in the industry as a result. In other words, the mindset of many retail investors is focused more on trading than investing, which often results in shorter investment horizons and trading more frequently in their search to maximise short-term returns. This can often lead to many investors mistiming the market, while also increasing their fees paid to trade in and out of products. "If you want to grow the market, the regulator and the industry have a role to play in educating people to take a more long-term view on their investments. Industry stakeholders also need to tackle the issue of churn, which requires a shift away from encouraging investors to switch products and rebalance their portfolios more frequently than necessary. To address this issue fully, we also need to change the incentive systems at the major fund distributors," says Vivian Chui, Partner, Head of Securities & Asset Management, Hong Kong, KPMG China.

Solving the aforementioned challenges will certainly go a long way in developing the industry to better serve investors and to enable Hong Kong to retain its status as a leading fund management hub. Alongside the challenges, however, there are a small number of critical business opportunities highlighted by the survey respondents and interviewees; these have the potential to accelerate the growth of the industry in the years ahead: the opening up of mainland China's asset management sector, the development of the GBA, technology-driven change and ESG.

Key takeaways



Overregulation is an issue for some asset managers in Hong Kong, while in some areas, the industry is calling for greater regulatory clarity around the GBA initiative and ESG. Finding the right balance between investor protection and perceived overregulation will be key to further growing the market while safeguarding the interests of investors.



Product quality will be the ultimate arbiter when it comes to fending off the pressure on fees charged by asset managers.



Hong Kong's rapidly ageing population is a key challenge that requires collaboration between industry stakeholders and a multi-pronged solution, including:

- The creation of post-retirement products and the broadening of investable asset classes for MPF members.
- The introduction of incentives such as the government's matching of voluntary contributions to spur higher levels of contributions into the MPF system.
- More, better investor education to help people understand their post-retirement financial requirements, and therefore their current required level of savings; this should encourage them to increase engagement with, and contributions to, their pensions scheme.



One tax incentive should be the separation of the HKD 60,000 tax deduction limit that is currently on both MPF tax deductible voluntary contributions and Qualifying Deferred Annuity Policies so that each option is eligible for its own deduction amount of HKD 60,000.



Design investor education and incentive systems to encourage long-term investing to improve retail investors' outcomes. This will also help to address the issue of excessive portfolio churn and reduce the fees that investors pay in rebalancing their portfolios.





Mainland China

Mainland China remains a key growth market for the industry as it opens up its asset management sector to foreign investors. The ongoing development of the GBA also presents significant business opportunities for Hong Kong.

The last few years have seen a significant amount of change in mainland China as its financial services industry and capital markets open up to international investors. Following the launch of the Shanghai-Hong Kong Stock Connect in 2014, there have been a number of developments such as the launch of the Shenzhen-Hong Kong Stock Connect and Bond Connect in 2017, and the lifting of quota restrictions on the QFII and RQFII schemes in late 2019. Several global index providers also continue to add China stocks and bonds into their benchmarks, which is likely to attract foreign investment inflows. Furthermore, foreign players were permitted to take majority ownership of their asset management joint ventures in 2018, and the scrapping of foreign investment caps on fund management companies entirely this April presents a significant opportunity for international firms.

This is a tremendous amount of change in a very short amount of time, and the impact on Hong Kong has been significant. In fact, for many of the developments in mainland China, Hong Kong has been the common factor and a major beneficiary. "With its close relationship with and proximity to mainland China, Hong Kong is in a great position to take advantage of these developments, and the industry in Hong Kong will play a positive role in engaging, supporting and developing mainland China's fund industry," says Mr. Luk of Fidelity International.



Access to the mainland China market is the biggest opportunity for the fund management industry in the next five years, and Hong Kong will continue to play a key role on two fronts. The first is Hong Kong as a gateway in terms of offshore strategies to the mainland China market. There is still huge room for growth in terms of investing offshore for retail investors in China. The second opportunity is Hong Kong as a sales centre to export the onshore China investment strategies to overseas investors.

Jimmy Ng

Head of Retail Marketing & Product Development, North Asia, Amundi Hong Kong

“



If you want to really take full advantage of the asset management market in mainland China, you need to be onshore. It is great to have support and strategy functions with experienced people in Hong Kong, but at the end of the day if you really want exposure in mainland China, then you need to invest and have people on the ground.”

Florence Chan

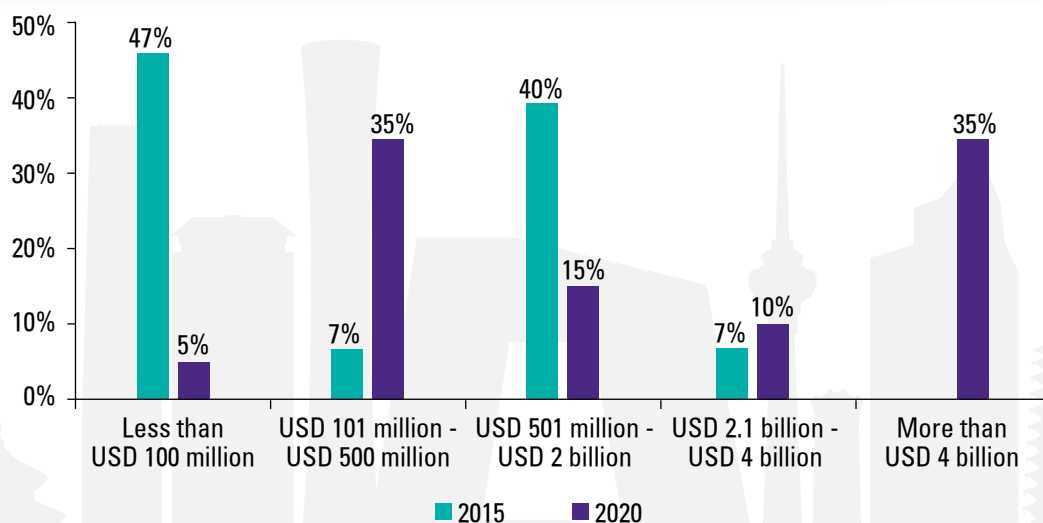
Head of Compliance, Asia Pacific
– International Distribution, Natixis
Investment Managers

For industry executives, the option of full ownership of asset management companies in mainland China offers a new, welcome but complex avenue to grow and succeed in the China market. As it stands, foreign players have a number of ways to access the mainland China market, including, but not limited to, QDLP programmes, joint ventures, wholly foreign-owned enterprises and fully-owned asset management companies. For companies with an existing presence in mainland China, evolving their current operating models into a coherent target state will be a critical objective, while those that have not yet established a presence on the mainland will need to carefully consider their options for market entry.

Whatever the strategy may be, it is clear a considerable amount of investment is needed for entering the market, meeting local regulations and guidelines, setting up infrastructure, building up brand recognition, hiring the right talent and adapting to the local culture. But given the potential size of the reward, all serious competitors are viewing mainland China as a long-term play. “Winning in China requires long-term commitment. If you are looking to be an overnight sensation, then you have misunderstood China. There are some really strong competitors already there,” says Mr. Wells of BlackRock. “For asset managers, mainland China is the big prize. That is where the growth is and where most of the assets are,” says Florence Chan, Head of Compliance, Asia Pacific – International Distribution, Natixis Investment Managers. “If you want to really take full advantage of the asset management market in mainland China, you need to be onshore. It is great to have support and strategy functions with experienced people in Hong Kong, but at the end of the day if you really want exposure in mainland China, then you need to invest and have people on the ground.”

The survey findings show that our respondents have seen a significant uptick in China-originated AUM versus 2015 – when the inaugural survey of member firms was conducted (Figure 3). Furthermore, nearly half the respondents expect their total AUM originating from mainland China to grow by 11-30% in the next five years (Figure 4). A further 11 percent and 21 percent of respondents expect this growth to reach 31-60% and 61-100%, respectively. This indicates that while some fund managers in Hong Kong may have experienced a steady increase in AUM originating from mainland China over the past years, many are optimistic that the future will see an acceleration of that growth.

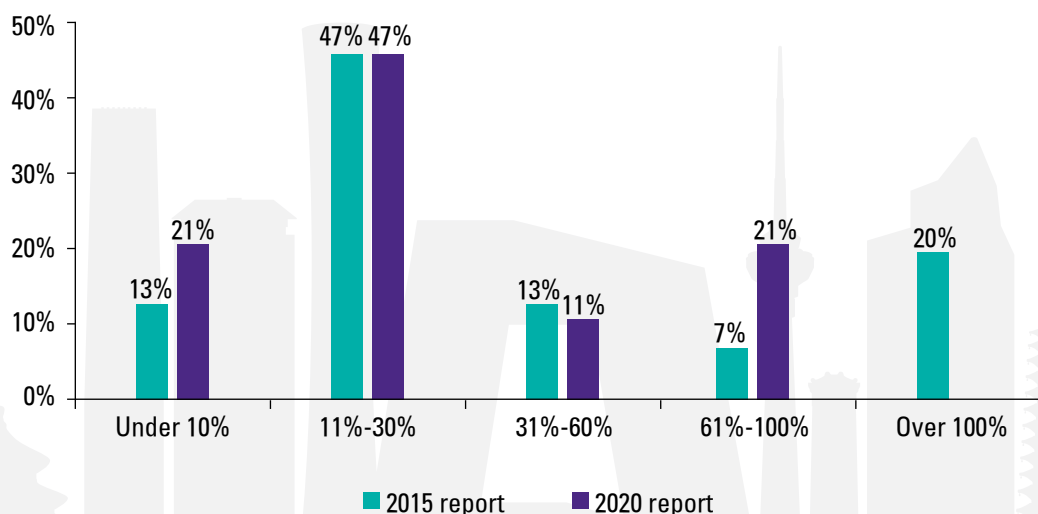
Figure 3: Total AUM originating from mainland China



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

Note: Numbers may not add up to 100% due to rounding

Figure 4: Expected growth in organisations' total AUM originating from mainland China in the next five years



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

'Capital market development', 'renminbi liberalisation' and the 'ongoing development of the Greater Bay Area' are viewed by survey respondents as the specific mainland China developments that are expected to have the biggest impact on Hong Kong's investment management industry in the next five years.

In addition to the Stock Connect and Bond Connect Schemes, the Mutual Recognition of Funds (MRF) arrangements between Hong Kong and a number of jurisdictions, including mainland China, France, Luxembourg, Switzerland, the Netherlands and the UK, offer a range of investment options for retail investors. While Hong Kong's MRF agreements with a growing number of economies have been a welcome development for the fund management industry, some interviewees point out some constraints, especially with regards to Hong Kong's MRF initiative with mainland China. While viewed in a positive light, interviewees note that the 50% cap is constraining growth in China-originated AUM. Interviewees called for the Hong Kong government, regulators and industry to work closely with authorities in mainland China to enhance the existing MRF arrangement by relaxing the cap and by permitting the delegation of investment functions outside of Hong Kong.

“



Foreign asset management companies that have been successful have been able to adopt local market practice to customise solutions for their customers. From our previous experience with QDII and MRF, we see that while there are some similarities, there are also differences between distributors and investors in mainland China and global investors. You cannot use the same formula that you apply elsewhere in the world. What will differentiate the market leaders in the mainland China asset management space will be the ability to adapt to the local regulatory environment and adopt local market knowhow.”

William Law

Head of Compliance and Legal, North Asia, Amundi Hong Kong

“



China is a big market, but for us the GBA initiative stands as a very good opportunity, first because of the proximity of Hong Kong to the region, and secondly because investors in Southern China are more familiar with the companies and their investment products in Hong Kong. For companies that have a strong presence and strong brand recognition in Hong Kong, they will be well-placed to tap into the investor base in the GBA.”

Michelle Chua

Managing Director,
Strategic, Planning &
Client Services, BEA Union
Investment Management

The Greater Bay Area opportunity

Another key strategic component of China's national development blueprint is the GBA, which aims to promote close cooperation between Hong Kong, Macau and nine cities in Guangdong Province to create a globally competitive and world-class city cluster. The GBA is home to 71.2 million people, and while that counts for only around 5 percent of China's total population, the combined GDP of the region's 11 cities totalled USD 1,641.97 billion in 2018, or 12 percent of mainland China's total GDP.

In February 2019, the Outline Development Plan for the Guangdong-Hong Kong-Macau Greater Bay Area was published, setting out the Central Government's vision for the project. The Development Plan identifies Guangzhou, Shenzhen, Hong Kong and Macau as the four core cities to drive the GBA's development, with Hong Kong highlighted as an international centre for finance, asset management, transportation and logistics, as well a global offshore RMB business centre.

As a key hub for asset management, interviewees agree that Hong Kong has a significant opportunity to leverage these advantages in the GBA. “China is a big market, but for us the GBA initiative stands as a very good opportunity, first because of the proximity of Hong Kong to the region, and secondly because investors in Southern China are more familiar with the companies and their investment products in Hong Kong. For companies that have a strong presence and strong brand recognition in Hong Kong, they will be well-placed to tap into the investor base in the GBA,” says Michelle Chua, Managing Director, Strategic, Planning & Client Services, BEA Union Investment Management.

In November 2019, an additional 16 policies for the GBA were announced, with one proposing the establishment of a cross-boundary wealth management scheme, which would allow the cross-boundary flow of financial products between mainland China and Hong Kong. This ‘GBA Wealth Management Connect’ has been welcomed by the business community and investors alike in Hong Kong, with the promise of an expanded investor base for asset management companies, and greater product diversity for investors.

However, industry executives note that a regulatory framework for the GBA Wealth Management Connect is needed in order to realise their ambitions. “The GBA is a major opportunity for any asset manager based in Hong Kong. But we need regulatory clarity to tell us more about the landscape. If the Hong Kong and mainland China authorities are able to create a viable platform that will help fund managers and distributors in the region to work together by leveraging existing products and making it available to investors in the GBA region, that would go a long way in helping to grow the industry in the coming five years,” says Mr. Fu of Ninety One Hong Kong.

“



Winning in China requires long-term commitment. If you are looking to be an overnight sensation, then you have misunderstood China. There are some really strong competitors already there.”

Steven Wells

Director, APAC Client Product Strategy, BlackRock



While there is still regulatory uncertainty as part of the development of the GBA, we also need to understand the investment appetite of investors in the region. We don't want to launch a product just because it has a great track record. If we want to play it smart and well, we need to be unique in our offering to attract those investors and flows of money.

Philip Tso

Head of Institutional Business
Hong Kong and Head of Consultant
Relations Management and Client
Advisory Asia Pacific,
Allianz Global Investors Asia Pacific

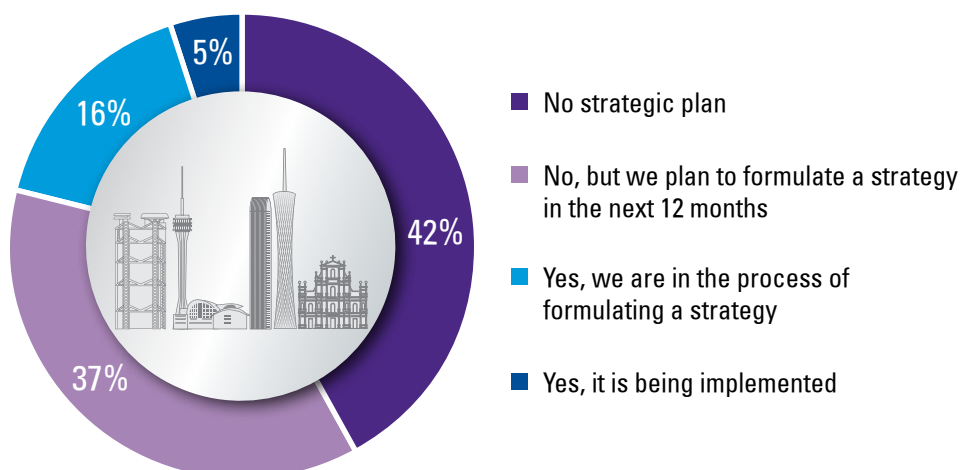
"Regulation is a key challenge, and one that will continue. So the years ahead are not just about business opportunities, but it is also about taking a more active role in working with the regulators to shape the future regulatory environment," says Amy Cho, Chief Executive Officer, Schroder Investment Management (Hong Kong). "For example, instead of waiting to be told what the guidelines are for the Wealth Connect initiative, we could take a more proactive role as an industry in suggesting what could be a good investment proposition for funds to be involved in the initiative. We hope that we can look at the MRF initiative and draw experience from it, though not necessarily to follow the MRF model too closely as there's a difference in context."

"The industry working with the Hong Kong and mainland regulators to explore the reciprocal arrangement opportunity for retail investors residing in the GBA to access Hong Kong-authorized funds through retail banks under the proposed Wealth Connect programme will be key to the strategic development for the Hong Kong and mainland fund industry. This could also be within a 'closed loop', where if a retail investor goes to the bank in the GBA to buy a Hong Kong-authorized fund, when they redeem it then the capital needs to flow back into the mainland," says Mr. Lee of Manulife Investment Management.

"We may not want to constrain Wealth Connect funds to be only Hong Kong-domiciled. Taking into account investor sophistication whilst we do not disregard their need for diversification, we could confine the available product set to be only non-derivative and non-complex products. We would propose this as a start, so that regulators could be less concerned about insufficient investor knowhow," suggests Ms. Cho of Schroder Investment Management.

Survey respondents and interviewees, while acknowledging the potential benefits and opportunities presented by the ongoing development of the GBA, indicated that they have varying levels of preparedness – and indeed focus – on the region. Forty-two percent of respondents say that they do not have a strategic plan for the GBA, while 37 percent say that while they do not currently have a strategic plan, they expect to formulate a strategy in the next 12 months (Figure 5). Acknowledging that the GBA's development is still in its infancy, some interviewees indicated their preference to adopt a wait-and-see approach until a more detailed framework and greater regulatory clarity are in place. Other interviewees stated that their primary focus is on the broader mainland Chinese market as a whole, especially given the accelerated liberalisation of the asset management and broader financial services sector in China.

Figure 5: Does your company have a strategic plan for the Greater Bay Area?



Source: 'Vision 2025' Joint HKIFA-KPMG Survey



In terms of asset management talent in China, the pool is quite small, especially given that there are so many new companies setting up. Then there are the domestic players that are also competing for the same talent. Finding talent that not only meet the regulatory requirements for foreign firms looking to set up operations in mainland China, but that also has the right experience, product knowledge and multiple language capabilities is a huge issue. ”

Rex Lo

Managing Director, Business Development, BEA Union Investment Management

Despite the wait for further guidance and regulatory clarity, there is a lot that firms with a strategy for the GBA can start implementing right away. “We need to think about whether our current business model is equipped to support the GBA, for example, human resources, talent pools, relevant language and skill sets, product knowledge, understanding of the local market, investor needs and appetite, and investor education support. While we are waiting for the release of guidelines, we should include the GBA initiative to the broader part of overall China strategy and start planning ahead,” says Ms. Chan of Franklin Templeton Investments.

Philip Tso, Head of Institutional Business Hong Kong and Head of Consultant Relations Management and Client Advisory Asia Pacific, Allianz Global Investors Asia Pacific, adds: “While there is still regulatory uncertainty as part of the development of the GBA, we also need to understand the investment appetite of investors in the region. We don’t want to launch a product just because it has a great track record. If we want to play it smart and well, we need to be unique in our offering to attract those investors and flows of money.”

Whether the primary focus is on the GBA or on the broader mainland China market, finding the right talent for onshore operations continues to be a major challenge highlighted by many industry executives. “In terms of asset management talent in China, the pool is quite small, especially given that there are so many new companies setting up. Then there are the domestic players that are also competing for the same talent. Finding talent that not only meet the regulatory requirements for foreign firms looking to set up operations in mainland China, but that also has the right experience, product knowledge and multiple language capabilities is a huge issue,” says Rex Lo, Managing Director, Business Development, BEA Union Investment Management.

Overall, the industry remains bullish about the growth prospects in mainland China, including in the GBA. Indeed, the amount of wealth being created in mainland China presents a significant opportunity for asset managers, although gaining access to that wealth is expected to largely be conducted through intermediaries. “Foreign asset management companies have been creating strategies about how to get onshore in China, but for some, that has been at the expense of critical thinking about what to do once they get there,” says Neil Macdonald, Head of Wealth and Asset Management Centre of Excellence, KPMG China. “Asset managers need to carefully consider which client segments to target, how to target these clients – which will inevitably initially mostly be via intermediaries – what (if anything) their brand stands for in China, how to win against the domestic players, and how to hire and retain the right talent.”

Key takeaways



There is a need for foreign asset managers to think beyond how to access the mainland China market, and focus on what to do once their onshore presence is fully set up. This means focusing on selling really good investment products, carefully considering which client segments to target, how to target these clients and build brand recognition and trust, how to win against the domestic players, and how to hire the right talent.



The Hong Kong government, local regulators and industry bodies should partner with authorities in mainland China to:

- Enhance the existing MRF arrangement between mainland China and Hong Kong by relaxing the 50% cap, as well as allowing the delegation of investment functions outside of Hong Kong to promote a greater variety of global products.
- Implement the proposed framework for the GBA Wealth Management Connect scheme, with clear guidance on regulatory requirements, products and operational logistics; the scheme should also consider including non-Hong Kong-domiciled funds. To manage the initial implementation of the scheme, regulators should limit the product range to non-derivative based, non-complex products.



While waiting for further regulatory guidance, firms should already be evaluating whether their current business model is equipped to take advantage of the economic growth in the GBA.

Technology

Technology-driven change is expected to continue, with investors demanding an improved, increasingly digital, user experience; this is particularly the case for younger, digitally savvy clients who demand instant, personalised services and lower fees. That said, many clients still prefer a human touch when it comes to making sizeable investments. The hybrid model of client engagement is here for a while to come.

With the confluence of several technology trends (Cloud, Big Data, Mobile, IoT) and evolving client expectations in the digital space, the ability to leverage technology and harness the power of data effectively is key for the industry's development. This will also be vital for asset managers seeking to tap into the growing customer base in mainland China, where financial products – including simple investment funds – are increasingly marketed, distributed, bought and sold online.

The landscape in Hong Kong is evolving rapidly. For example, the emergence of robo-advisory offerings provides the potential to disintermediate the banks and offer investors the opportunity to directly take charge of their investments. The launch of virtual banks in Hong Kong is also disrupting the landscape for financial services and will raise the bar for customer experience in the financial services business. Although the virtual banks will initially focus on simple banking like deposits and lending, it is likely that many of them will eventually expand into investment and wealth management in the medium term.

Hybrid models here to stay, but digital interaction is growing in importance

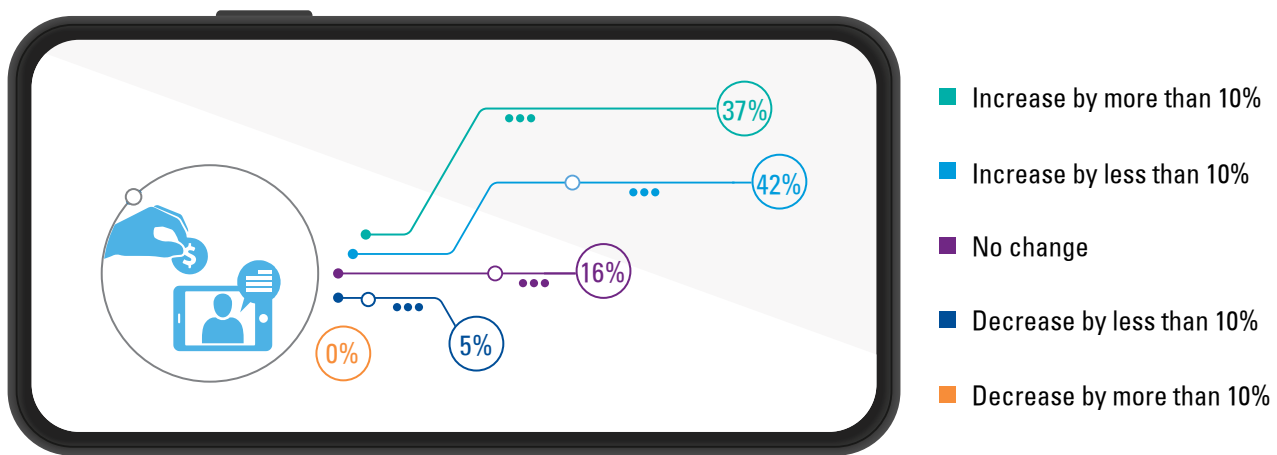
By 2025, interviewees agree that technology will be more focused on supporting the industry – achieving efficiencies and making it easier for clients to invest – rather than replacing parts of the industry completely. “Clients, especially the younger generation, expect quicker turnaround in terms of execution and settlement, as well as cheaper fees and lower transaction and execution costs. The older, more mature investors are also moving towards online investment platforms, but many still want to retain a certain human touch. Technology will certainly disrupt the industry, but will it replace entire parts of the market? I don't think so,” says Ms. Chan of Franklin Templeton Investments.

Despite the preference of many investors to retain some element of face-to-face interaction, issues such as recent social unrest in Hong Kong and the outbreak of COVID-19 are disrupting traditional channels and business models as the public turns to digital platforms and channels for their investing, purchasing and general daily lives. This further stresses the urgency for the industry to figure out how to supplement physical interaction with more technology to service their clients, whether it is a distribution or business partner, or the end investor.

While ultra-high-net-worth clients still prefer to meet in person and have regular reviews with RMs, there are a lot of clients who are underserved, and this is where a digital tool would fit in nicely for their financial planning, says Nelson Chow, Managing Director, AllianceBernstein Hong Kong. "The important thing is to have the tools ready and in place. Whether clients use it or not is another question."

Therefore, somewhat unsurprisingly, most survey respondents expect their investment in technology to increase in the next 12 months, with a significant number expecting this investment to increase by more than 10% (Figure 6). Technology-related strategic initiatives planned over the next three to five years span a wide range of areas, including innovation to enhance customer experience, automation, cloud computing, artificial intelligence (AI), Application Programming Interface capabilities, data analytics and management, robo-advisory and offering optimised digital wealth management platform solutions to clients. Technology will also be used to enhance regulatory and compliance efficiency, and to assist with more specific areas like ESG screening and reporting.

Figure 6: Change in organisations' investment in technology in the next 12 months



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

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Clients, especially the younger generation, expect quicker turnaround in terms of execution and settlement, as well as cheaper fees and lower transaction and execution costs. The older, more mature investors are also moving towards online investment platforms, but many still want to retain a certain human touch.”

Isabella Chan

Head of Global Financial Institutions, APAC and Head of Retail Business, Greater China, Franklin Templeton Investments (Asia)



We are in a time of significant change, and we are investing heavily in

technology, not only on the back end but also the front end. We need to be nimble and agile, across the front, middle and back-end operations in order to transform ourselves in order to meet requests from clients in the region, especially those that are digitally savvy.

Eric Fu

Managing Director and Country Head, Greater China, Ninety One Hong Kong Ltd

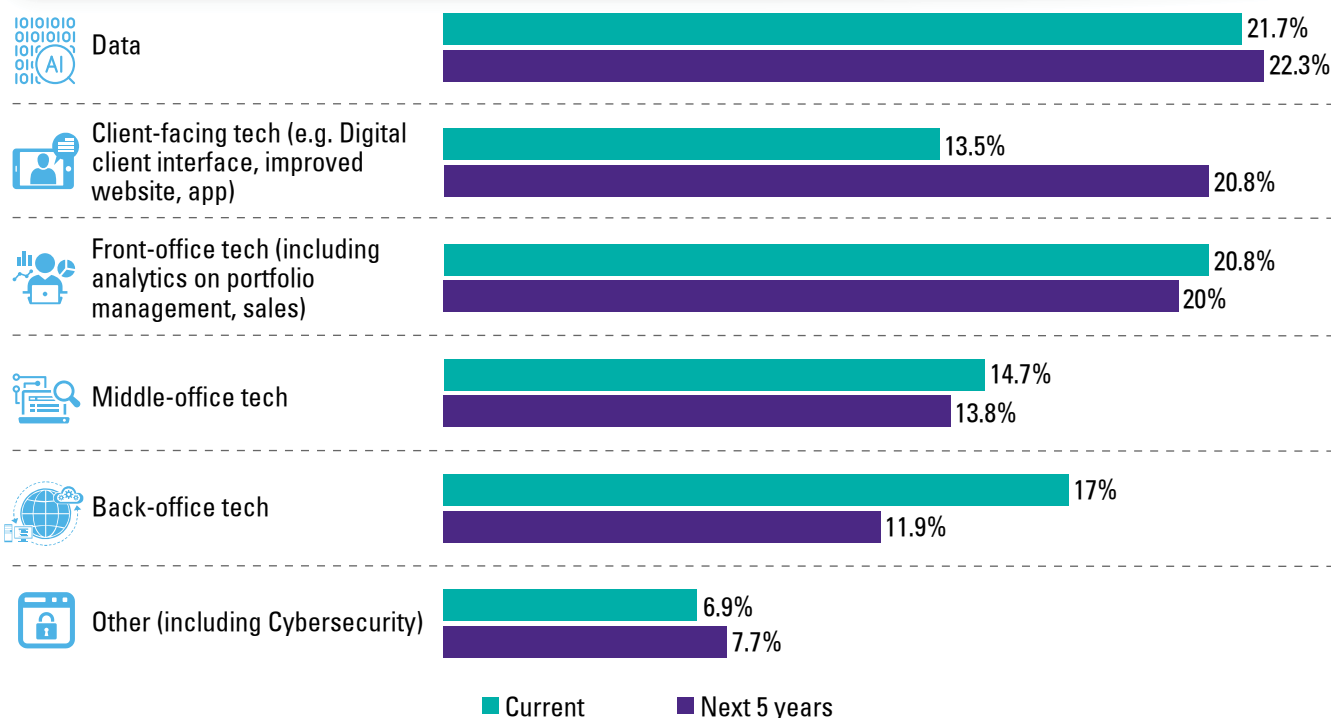
Shifting investment focus in technology

A greater proportion of the surveyed organisations' technology investment is expected to be allocated towards data and client-facing technology (such as digital client interfaces, improved website, apps), and less towards back-office technology (Figure 7). This is largely in line with survey respondents and interviewees' intention to focus more on enhancing customer experience and digital wealth management platform solutions, data analytics and management. "We are in a time of significant change, and we are investing heavily in technology, not only on the back end but also the front end. We need to be nimble and agile, across the front, middle and back-end operations in order to transform ourselves in order to meet requests from clients in the region, especially those that are digitally savvy," says Mr. Fu of Ninety One Hong Kong.

This focus on front-office technology is aligned with the survey finding that web portals and mobile apps (by the organisation) are expected to become more common forms of client communication in the next five years compared to today. Respondents expect slightly less face-to-face communication in the next five years, but it will still comprise a large proportion of total client communications, indicating that firms believe clients will still value human interaction.

Data remains the area that is expected to receive the largest proportion of technology investment from the surveyed organisations. This is perhaps unsurprising given the need for solutions to access information held across multiple, legacy systems spanning front, middle and back offices. Effectively harnessing the power of data will also facilitate better management decisions in near real-time.

Figure 7: Proportion of organisations' current and expected technology investment



Source: 'Vision 2025' Joint HKIFA-KPMG Survey



General investors in Hong Kong are used to the current distribution model with banks as

primary distributors, and continue to maintain a close relationship with their relationship managers. Even with the launch of virtual banks in Hong Kong, I don't expect there to be significant change to the distribution model in the near-term. These kinds of behaviours are difficult to change, especially as banks, given the increasing competition, are increasingly flexible and can offer very attractive fees. Direct competition between fund platforms and banks is still a distance away.



Wallace Tsang

Managing Director of Intermediary Business, Value Partners

Although industry executives note that there is currently limited application of AI among their organisations, by 2025 a majority of surveyed organisations expect to have already implemented AI inside a number of their business processes. This is in line with the survey respondents' view that the 'application of artificial intelligence' is a top issue that is expected to affect the industry in the longer-term horizon beyond 2025 (Figure 2). Indeed, some interviewees highlighted their efforts in building up data science and AI centres to support their existing active management capabilities.

"When we first talked about AI and big data a few years back, people tended to be more focused on enhancements to operations, account opening, like AML/KYC. Now, we are also looking at how disruptive technology can change how asset managers pick securities, construct portfolios and trade in the marketplace. The most disruptive technology will bring speed, scale and accuracy to a new level in coming years. It will also be accomplished with data that are yet to exist or structures to be consumed in a productive way to make real decisions. It will become more important for asset managers to build infrastructure to find, scrub, normalise, model and inject these data into existing or proven strategies and integrate into the investment process," says Ms. Chan of Franklin Templeton Investments.

Will tech drive the disintermediation of the fund management industry?

With survey respondents expecting an increase in investment in client-facing technology and more client communication to occur via electronic channels, could the next few years witness the gradual disintermediation of fund distributors in Hong Kong? This question divided opinion among our interviewees.

Certainly, the advent of virtual banking in the city is one area which is expected to disrupt the traditional distribution model for basic financial services. "When the virtual banks come to market and eventually start to develop their wealth management offerings, the market landscape will drastically change. With no physical branches, virtual banks may have a robo-advisory or other similar service or application that enables the investor to self-serve online for their investment needs, avoiding the physical branch and a traditional bank relationship manager altogether," says Elisa Ng, Managing Director, Head of Funds Business, China & Hong Kong, J.P. Morgan Asset Management.

While industry executives note that they rely heavily on intermediaries for distribution in Hong Kong, and have built strong relationships as part of this, they acknowledge that fund managers need to transform their business models to adapt to rapid technological change. "Asset managers need to transform so they are no longer just a product provider. I certainly don't see the industry looking to disintermediate the banks or do any less in partnership with financial institutions. Rather, we have to acknowledge that with the eventual growth of e-wallets, open banking and data aggregation, distribution dynamics will change and so would client expectations. To stay relevant, asset managers would need to be closer to the end investor, and being more embedded within the ecosystem alongside the banks helps achieve that. We could co-develop tools and solutions with the intermediaries, for example in risk profiling," says Ms. Cho of Schroder Investment Management.

As the Hong Kong retail market is operating primarily under a commission-based model via intermediaries, much of the data on end investors on their investment/risk profile and appetite resides with distributors, including the new emerging digital channels and virtual banks, says Ms. Chan of Franklin Templeton Investments. "Distribution models are unlikely to change dramatically in the near-term. Asset managers can seek to partner with traditional banks or new digital/virtual banking platforms in developing digital tools to better understand the investors' behaviours and needs, and provide appropriate product strategies and portfolio solutions for them."



Asset managers that are thinking about focusing on creating direct to customer

channels will need to fully understand how to leverage data from and about their customers. The fund houses that are able to differentiate themselves from their competitors will be the ones that are able to build a strong brand that stands for high quality products and integrity, offer a great user experience, and focus on education in formats that are understandable to the investor. ”

Vivian Chui

Partner, Head of Securities & Asset Management, Hong Kong, KPMG China

The shift from traditional sales channels to a more digital online model is a clear trend that will continue in the coming years. The use of digital technologies will also be key to engaging with the sizeable group of underserved customers in Hong Kong as well as mainland China. “If everyone is targeting the same segment of customer, then there is a finite amount of money available. Focusing on the underserved – which includes the younger next generation of investors – could help to accelerate the growth of AUM in the industry. Solutions like robo-advisory and innovative fintech will assist, while virtual banking may also open up a new route to this segment,” says Mr. Lee of Manulife Investment Management.

The digitisation of the industry will also have an impact on both the existing workforce, as well as future hires as all employees are increasingly required to have a tech mindset and skills. The existing workforce will also need to be reskilled. “The government and industry need to help transform the existing workforce, who have been adding value to the conventional model, as the business model evolves from product-driven to solution-led and digitally enabled,” says Ms. Cho of Schroder Investment Management.

One way to help foster new talent and retrain the existing workforce is for industry, universities and research and training institutes in Hong Kong to work together to develop education programmes and professional qualifications that equip financial service specialists with relevant tech-related skills that are fit for the future needs of digitally savvy clients.

Furthermore, the industry in Hong Kong can also look to the rest of the GBA to fill tech-related talent gaps. In particular, Shenzhen’s rapid development as an innovation hub could see the city become a major hotspot for tech specialists, data scientists, and customer and user experience designers. This presents Hong Kong with a great advantage and access to a deep tech talent pool right on its doorstep. Additional changes made to tax and work permit requirements as part of the GBA initiative’s development will also help to facilitate greater labour mobility in the region.

With the digitisation of the industry creating opportunities for asset managers and technology players, industry executives also emphasise that maintaining a fiduciary mindset will be crucial to growing and preserving the integrity of the market.

“People are starting to think about linking tech feasibility with fiduciary duty, and are starting to be concerned about the suitability and the advice they provide and the outcome. The regulators are also starting to pay more attention to this. This is another front where the accumulated experience in Hong Kong in this area could be beneficial for Greater China as a whole. Whoever does it right will have a competitive edge,” says Pedro Bastos, Chief Executive Officer, Asia-Pacific, HSBC Global Asset Management (Hong Kong).



Striving for operational efficiency and finding better ways to do the same things faster, more cost-effectively and easier is everyone’s goal, and the technology and digital enablement around that is critical. Operational efficiency is where you can solve the problem regardless of size. How do you be big – in terms of scale, balance sheet, credibility – and small – nimble, smart, fast – at the same time? It is a bit paradoxical, but you need to be both. There are times when you need to show your scale, and times when you need to be fast, and size can’t be a hindrance. ”

Terry Pan

Chief Executive Officer, Greater China, Southeast Asia and Korea, Invesco Hong Kong

Key takeaways



The landscape in Hong Kong is evolving rapidly, with new technologies disrupting the industry. The emergence of robo-advisory could disintermediate the banks and allow investors to directly take charge of their investments. The launch of virtual banks in Hong Kong is also disrupting the landscape for financial services and raising the bar for customer experience.



Asset managers need to be nimble and agile, across the front, middle and back-end operations in order to transform to meet requests from digitally savvy clients.



Data is the key to ensuring that technology applied across the front, middle and back offices are able to function effectively, and to facilitate better management decisions.



In order to avoid becoming commoditised product providers, asset managers should seek to partner with intermediaries to co-develop tools and solutions to better understand clients' needs and create appropriate investment strategies.



To accelerate the growth of AUM in the industry, fund managers should focus on segments that are currently underserved, including the younger, next generation of investors. Solutions like robo-advisory and innovative fintech will assist, while virtual banking may also open up a new route to this segment.



The industry, universities and research and training institutes in Hong Kong should work together to develop education programmes and professional qualifications that equip current and potential future fund management staff with relevant tech skills.





ESG

ESG investing will become the 'new normal', with pension funds and institutional investors continuing to raise the bar for ESG. Greater collaboration between industry stakeholders is needed to create clear ESG standards for Hong Kong.



Within the next few years, as companies increasingly build ESG criteria into their core investment processes, investors may end up buying ESG products without knowing it because most, if not all, products will be ESG products. While some products will be marketed as ESG-themed, most others will have ESG lenses embedded in the investment process.

Neil Macdonald

Head of Wealth and Asset
Management Centre of Excellence,
KPMG China

A key development in the asset management industry is the increasing demands from investors that asset managers integrate ESG into their investment decisions and offer more sustainability-related products. Specifically, investors – both institutional and retail – are increasingly expecting their managers to target positive and measurable ESG outcomes, while generating positive financial returns. “Pension funds and sovereign wealth funds are starting to divert resources and capital towards more sustainable outcomes. Once they start to do it, asset managers and ultimately retail investors will start to move on this as well. The new generation of wealth increasingly views ESG as a very important criterion in their investment decision-making process,” says Mr. Chow of AllianceBernstein Hong Kong.

Overall, sustainable finance is experiencing strong growth worldwide, with the value of assets under management increasing from close to USD 23 trillion in 2016 to USD 30.7 trillion in 2018, according to the Global Sustainable Investment Alliance.⁵ This upward trend is only expected to accelerate in the coming years, with ESG investing poised to become the ‘new normal’ worldwide. “Within the next few years, as companies increasingly build ESG criteria into their core investment processes, investors may end up buying ESG products without knowing it because most, if not all, products will be ESG products. While some products will be marketed as ESG-themed, most others will have ESG lenses embedded in the investment process,” says Mr. Macdonald of KPMG China.

⁵ ‘Global Sustainable Investment Review 2018’, Global Sustainable Investment Alliance, http://www.gsi-alliance.org/wp-content/uploads/2019/03/GSIR_Review2018.3.28.pdf

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ESG is a very big topic for the entire industry, but especially for asset managers that have their headquarters in Europe, where ESG development is already quite advanced, and where there is a high demand for ESG products from investors. ESG may even be advancing to hygiene factor status, with an increasing number of pension funds and institutional investors requiring asset managers to at the very least be a UNPRI signatory.”

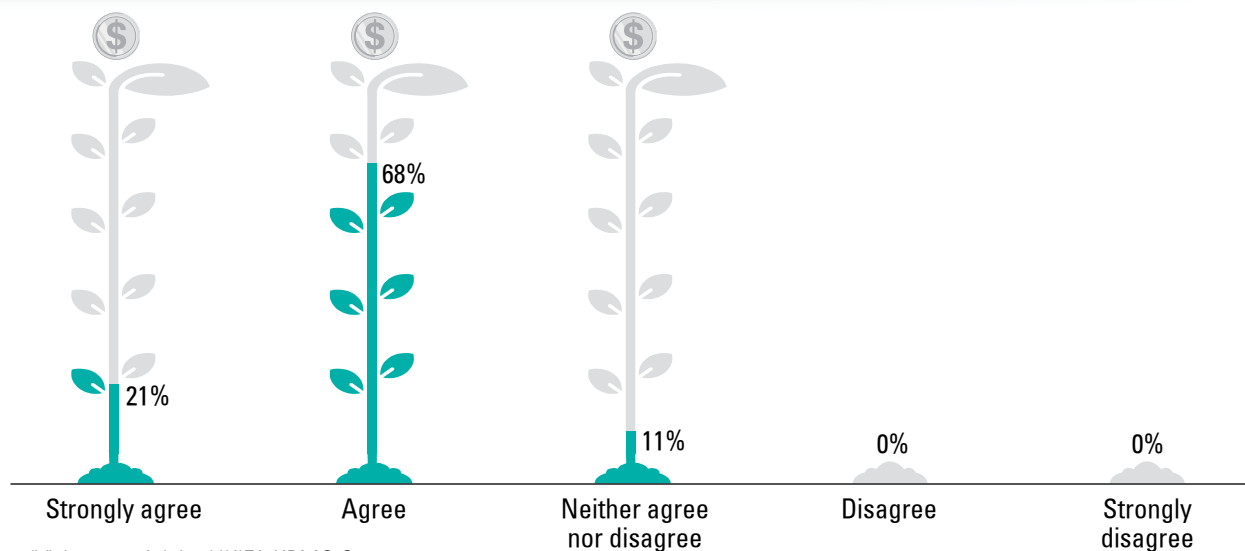
Thibault Gandol

Head of Strategy Asia Pacific, Natixis Investment Managers

While institutional investors – and asset managers – in Europe have been leading in this space, the mindset is starting to shift in Hong Kong and mainland China. ESG as a concept is not new to the asset management industry in Hong Kong. However, the level of true ESG integration varies between asset managers. Fund managers will therefore, if they haven't already, start to ramp up efforts to incorporate ESG into their strategy.

Part of this could include opting into the voluntary climate-related financial risk disclosures – developed by the Task Force on Climate-related Financial Disclosures – and/or adding their names to the growing list of signatories to the UN-supported Principles for Responsible Investment (UNPRI). “ESG is a very big topic for the entire industry, but especially for asset managers that have their headquarters in Europe, where ESG development is already quite advanced, and where there is a high demand for ESG products from investors. ESG may even be advancing to hygiene factor status, with an increasing number of pension funds and institutional investors requiring asset managers to at the very least be a UNPRI signatory,” says Thibault Gandol, Head of Strategy Asia Pacific, Natixis Investment Managers. This trend is reflected in the survey results, with respondents overwhelmingly agreeing that “providing sustainable investing-related products is increasingly important to clients” (Figure 8).

Figure 8: Organisations' view on the statement: “Providing sustainable investing-related products is increasingly important to clients”



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

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Pension funds and sovereign wealth funds are starting to divert resources and capital towards more sustainable outcomes. Once they start to do it, asset managers and ultimately retail investors will start to move on this as well. The new generation of wealth increasingly views ESG as a very important criterion in their investment decision-making process.”

Nelson Chow

Managing Director, AllianceBernstein Hong Kong



Interest in ESG is really starting to grow in Asia, initially from the sovereign wealth funds, but increasingly more so from intermediaries. Clients are starting to ask how they can apply ESG within their existing portfolio. Instead of just underlining the benefits of ESG, we should explain to them what the downsides are of not incorporating ESG.

Amy Cho

Chief Executive Officer,
Schroder Investment Management
(Hong Kong)

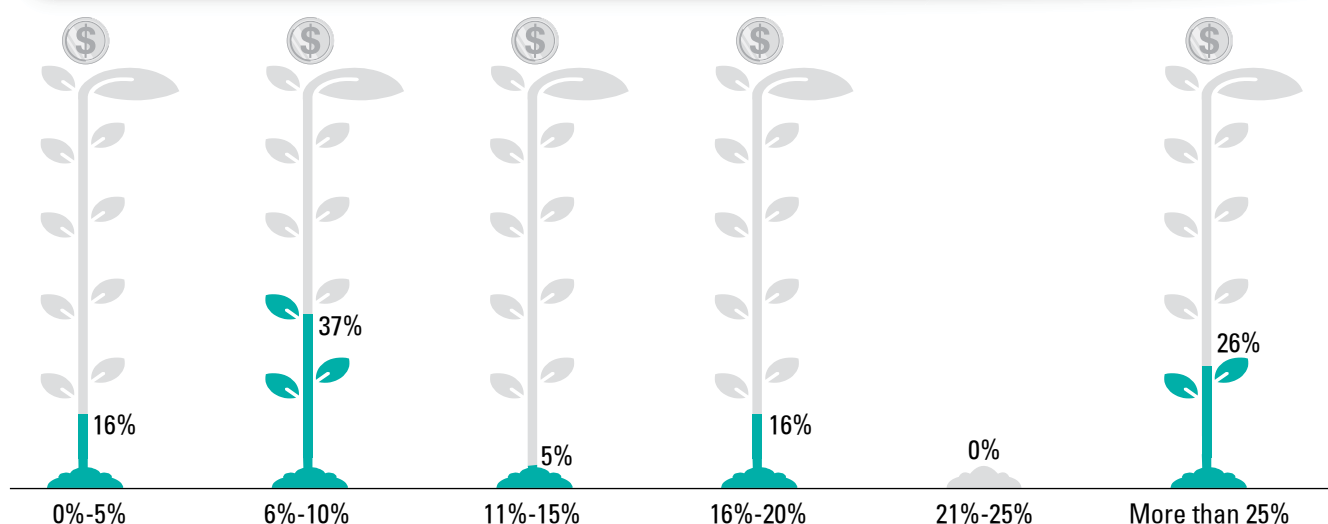
Respondents vary on the proportion of AUM of their investment management business in Hong Kong that they expect to be invested in ESG products by 2025. Eighty-four percent of respondents expect the proportion to be more than 5%, with just over a quarter expecting a proportion of more than 25% (Figure 9). Despite the varying expectations, the overall trend is that in the longer term, ESG will form an integral part of the investment process and fund management industry.

Regulators in Hong Kong are acutely aware of the trend towards ESG and sustainable investing, and have been active in fostering the development of green finance and ESG. In September 2018, the SFC launched its Strategic Framework for Green Finance, which aims to encourage the consideration of ESG factors in the investment and risk management processes, facilitate the development of ESG-related products and enhance listed companies' reporting of environmental and climate-related information.

As part of this framework, the SFC issued a circular in April 2019 to provide guidance on disclosures by SFC-authorised green or ESG funds, and a central database of these funds was made available on the SFC's website at the end of 2019.⁶ In December 2019, the SFC also published the results of its survey of the ESG investment practices of asset managers and asset owners in Hong Kong, which found that there is significant interest among asset management firms to ramp up their ESG efforts and management of environmental and climate risks.⁷

However, the lack of consistency in ESG methodologies and standards worldwide remains a significant challenge. Industry executives interviewed for this report unanimously agreed that the industry and the SFC should work together to fast-track the development of industry-wide standards for ESG in Hong Kong. The regulator is also encouraged to work with its counterparts in other key jurisdictions to achieve greater alignment on this issue, a suggestion echoed in the HKIFA's *Roadmap for the Asset Management Industry to promote Green/Sustainable Finance*.⁸

Figure 9: Proportion of AUM of organisations' fund management business in Hong Kong that is expected to be invested in ESG products by 2025



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

⁶ [https://www.sfc.hk/web/EN/regulatory-functions/products/list-of-environmental,-social-and-governance-\(esg\)-funds.html](https://www.sfc.hk/web/EN/regulatory-functions/products/list-of-environmental,-social-and-governance-(esg)-funds.html)

⁷ 'Survey on Integrating Environmental, Social and Governance Factors and Climate Risks, in Asset Management', SFC, December 2019, <https://www.sfc.hk/web/EN/files/ER/ENG%20Survey%20Findings%20Report%2016%2012%202019.pdf>

⁸ https://www.hkifa.org.hk/eng/news/news_GreenRoadMap_Aug2019.aspx

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For ESG, further education is needed to ensure that clients know that in the long-term ESG investing will pay off. However, the dilemma arises in Hong Kong because investors tend to take a more short-term view on their investments, especially when compared to Europe and the US.”

Elisa Ng

Managing Director, Head of Funds Business, China & Hong Kong, J.P. Morgan Asset Management

While the pendulum is swinging towards ESG as the new normal – primarily led by pension funds, sovereign wealth funds and institutional investors – many retail investors in Hong Kong and mainland China remain sceptical. In particular, there is a belief that ESG investing is a lower-return proposition versus non-ESG investing. There are, however, strong indications to the contrary with academic studies and industry research providing support for ESG-based investing. For example, a study of more than 2,000 research papers on equity returns found that 63 percent of studies reported a positive correlation between ESG and financial performance, while just 8 percent reported a negative correlation.⁹ While these findings are more indicative than substantive, they provide a compelling argument for ESG investing.

Studies and academic research aside, a more concerted effort by both the industry and regulators to educate retail investors in Hong Kong about the benefits of ESG is key to the growth of the asset management industry. “Nowadays, having ESG incorporated into the investment process is not enough. It is also about how to educate investors and help them understand how we define and incorporate ESG, and explain to them what ESG means to our firm. The industry and regulators need to work together to educate the market and communicate the ESG message to the underlying retail investors. First, we need to set standards to define what ESG means, then we need to incorporate this into our literature before rolling out products to investors. A lot of this will be done in the next five years,” says Sam Yu, Managing Director and Head of Compliance, Asia Pacific Ex-Japan, Baring Asset Management (Asia).

Ms. Ng of J.P. Morgan Asset Management agrees: “For ESG, further education is needed to ensure that clients know that in the long-term ESG investing will pay off. However, the dilemma arises in Hong Kong because investors tend to take a more short-term view on their investments, especially when compared to Europe and the US.”

Investment in underlying data and technologies to improve ESG screening, strategies, reporting and overall integration will also be crucial going forward. As increasing amounts of capital flow into ESG products and processes, there is a growing need for more and better data. Deploying big data techniques and machine learning algorithms may improve the quality and timeliness of ESG-related information; this could help to create more consistent company disclosures, transparent research methodologies and reliable ratings. “In 2025, data issues should be resolved. Technological approaches like natural language processing and machine learning will get a lot better at screening out companies that are just paying lip service to ESG considerations,” says Mr. Wells of BlackRock. “We also expect that, with the increasing availability of data, what clients consider to be the minimum is going to be raised. For example, it is already common to screen out certain types of munitions, and increasingly others like thermal coal. Some investors will think ‘why stop there’? Going forward we will see more screened out, and the bar will continue to be raised by investors demanding it.”

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Sam Yu

Managing Director and Head of Compliance, Asia Pacific Ex-Japan, Baring Asset Management (Asia)

⁹ Gunnar Friede, Timo Busch and Alexander Bassen: ESG and financial performance: aggregated evidence from more than 2000 empirical studies, 2015



To uncover the best investment opportunities takes the right people, resources and experience on the ground. Our firm has established a strong responsible investing culture since 1992. Our investment managers, including many of those who started as graduate trainees, embrace this ESG culture from day one of their on-the-job training.

Clarchie Szeto

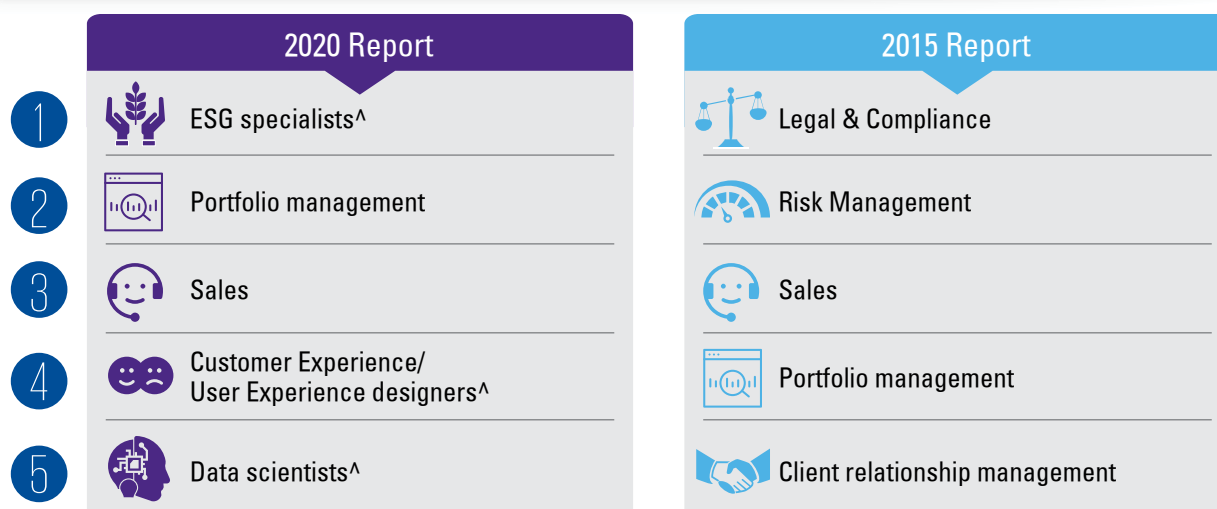
Head of Banks - Hong Kong,
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While the increasing availability of ESG data is a welcome development, the credibility and integrity of this data remains a crucial factor for effective ESG investing. There is currently a lack of standards and oversight around ESG data, with different providers using their own methodologies that can often result in discrepancies between ratings for a single company. With significant amounts of capital now shifting firmly towards sustainable investing, there is a real need for a regulatory-driven overarching framework in Hong Kong to maintain minimum standards and oversight of the ESG data provided by third parties, and to improve data integrity and credibility in the market.

The greater focus on ESG investing, data and investor education will necessitate that asset managers find the right talent to lead and support their ESG initiatives. Hiring and retaining ESG specialists for the investment, research and shareholder engagement teams will be key to industry development in this space in Hong Kong. However, survey respondents expect there to be a shortage of skilled ESG specialists in the local labour market (Figure 10). It is important to note that while there may be a sufficient number of traditional ESG professionals such as environmental engineers in the market, there is a notable lack of skills and understanding in the area where finance and ESG intersect. Finding the right ESG professionals who are also well-equipped and knowledgeable about its application in the financial realm is a key challenge, certainly for asset managers in Hong Kong.

Talent shortages there may be, but many asset managers in Hong Kong are now creating dedicated ESG teams in Hong Kong. Some interviewees of international asset managers are looking to relocate some of their ESG specialists from other offices to Hong Kong, given the size of the opportunity and the trend towards ESG in the region. Others are reskilling and retraining their current workforce rather than building a new team from scratch, or placing greater emphasis on ESG principles and education for new joiners. "To uncover the best investment opportunities takes the right people, resources and experience on the ground. Our firm has established a strong responsible investing culture since 1992. Our investment managers, including many of those who started as graduate trainees, embrace this ESG culture from day one of their on-the-job training. Their research analysis and on-going engagement with companies on ESG issues are supported by a dedicated central team of over 20 ESG experts and 30+ ESG asset class analysts based in different regions. This ensures ESG considerations are fully embedded in the investment process and underpin all our investment activities," says Clarchie Szeto, Head of Banks - Hong Kong, Aberdeen Standard Investments.

Figure 10: Greatest skill shortages expected in the local labour market



Source: 'Vision 2025' Joint HKIFA-KPMG Survey

[^]Newly added to the 2020 Report

In addition to training at the corporate level, an industry-wide programme should be introduced in Hong Kong to offer structured ESG training and qualifications that combine both financial and ESG skills and knowhow. There is evidence of this already happening in Europe, with the European Federation of Financial Analysts Societies (EFFAS) offering an ESG Analyst certification programme to provide necessary training for the efficient valuation, measurement and integration of ESG issues into investment analysis.

Overall, the development of ESG investing is an irreversible trend, the impact of which is already being felt in Hong Kong. Asset managers will need to work with the regulators to create clear ESG standards for Hong Kong. In the meantime, it is crucial that they proactively develop consistent ESG policies and practices that meet the needs of their clients, and provide more detailed disclosures. This will help to raise the bar in Hong Kong, reduce greenwashing in the industry, and enable investors to better identify those asset managers with stronger ESG practices and policies.

“Doing ESG right and in a way where it is more than a marketing gimmick but associates positive outcomes is going to be very important. The industry worldwide needs to understand the liability associated with putting an ESG seal without doing the proper duty of care. This could affect the credibility of the industry as a whole,” says Mr. Bastos of HSBC Global Asset Management (Hong Kong). “Hong Kong has a great opportunity to develop a strong ESG vein, with clear industry standards, to differentiate itself from other jurisdictions and show the world that we offer something different than anywhere else.”

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At the macro level, the growing importance of ESG to asset managers and their investors will be even more pronounced in the coming years as sustainability remains one of Beijing's top priorities. Indeed, we expect it to be a key focus area in the 14th Five-Year Plan which will be announced later this year. Meanwhile, at the fund manager level, it is vital that the whole organisation is aligned on the strategy around ESG. Senior leadership need to take the lead in initiating a cultural shift within their organisations, and ensure that the investment, research and compliance teams are on board with the plan to integrate ESG.”

Pat Woo*Partner, Head of Sustainable Finance, Hong Kong, KPMG China*



Key takeaways



At a minimum, asset managers should commit to producing climate-related financial risk disclosures and becoming signatories to the UNPRI.



The industry and regulators need to:

- Fast-track the development of industry-wide standards for ESG in Hong Kong. The regulator is also encouraged to work with its counterparts in other key jurisdictions to achieve greater alignment on this issue.
- Ensure that retail investors are properly informed about the benefits of ESG investing, and dispel the misconception that investing in ESG products means sacrificing returns.
- Introduce an overarching framework in Hong Kong to maintain minimum standards and oversight of the ESG data provided by third parties, and to improve data integrity and credibility in the market.
- Develop an industry-wide programme to offer structured ESG training and qualifications that combine both financial and ESG skills and knowhow, using the European Federation of Financial Analysts Societies' ESG Analyst certification programme as a reference.



Improving the quality of ESG data would help to create more consistent company disclosures, transparent research methodologies and reliable ratings.



Asset managers should seek to engage with their clients to understand their ESG investment preferences and create ESG practices and processes that are aligned with their specific needs.



In addition to straightforward performance reporting, asset managers should increasingly aim to show their investors evidence of the ESG impact of their investments.



Increasing investment in ESG talent – whether organically or inorganically – is key to meeting the increasing demands in this area. This goes hand-in-hand with ensuring that teams within an individual organisation are aligned in their views and strategies for ESG.

Looking ahead

Hong Kong's fund management landscape in 2025 will be both instantly recognisable and potentially very different. A number of challenges lie ahead, such as Hong Kong's rapidly ageing population, increasing fee pressure and a complex regulatory landscape. Encouraging retail investors to take a longer-term view on their investments will also be an important step towards creating sustainable positive financial outcomes for the industry. Addressing these matters will require a joint effort between the government, regulators and the industry.

"The keys to growing AUM in Hong Kong over time will come down to access to mainland distribution opportunities, using technology effectively, ESG, targeting new client segments, solving the pension problem and educating industry participants. Looking beyond annual business targets towards a five-year horizon and beyond, these are clearly the mega trends for the industry which, if pursued effectively, could help the industry to flourish in Hong Kong," says Mr. Lee of Manulife Investment Management.

A critical factor in capturing the potential gains from the future landscape will be firms' ability to recruit and reshape a talent base fit for that future. Job adverts for ESG specialists, data scientists and Customer Experience/User Experience designers will increasingly feature on asset managers' and recruiters' websites. Greater collaboration between the government, industry, universities and research and training institutes to develop relevant ESG and tech-related education programmes and professional qualifications will be key to growing the talent pool in these areas.

The Hong Kong fund management industry already has much of what it takes to be successful in 2025 and beyond, but survey respondents and interviewees made it clear that all industry stakeholders need to be more proactive to ensure that Hong Kong remains the leading asset management hub for Asia. "Hong Kong is at a crossroads. If we don't act fast and become more forward-looking and have the courage to take a risk and be a leader, we run the risk of falling behind. We can't always wait for things to be 100 percent ready – that will never happen. The industry in Hong Kong needs to show that it can be a leader in the asset management space, rather than a follower," says Mr. Tso of Allianz Global Investors Asia Pacific.

"The next five years will be very challenging for the industry as a whole. We need to consider how to best prepare for 2025, and how to make our products more attractive, efficient and client-centric," says Mr. Bastos of HSBC Global Asset Management (Hong Kong). "The bottom line for 2025 is differentiating ourselves from the rest of the world – using technology with the right purpose, promoting domestically-developed talent and markets, and working with regulators to drive the region towards a more holistic approach to the development of the fund management industry."

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About Hong Kong Investment Funds Association



The Hong Kong Investment Funds Association ("HKIFA") is a non-profit-making trade association that represents the fund management industry in Hong Kong. Incorporated in 1986, HKIFA's key objective is to promote the fund management industry in Hong Kong so as to further bolster its position as a fund management hub within the region and globally.

The HKIFA has two major roles, namely consultation and education. On consultation, we act as the representative and consulting body for our members and the industry in all aspects concerning the regulation of unit trusts, mutual funds, retirement funds and other funds of a similar nature. We actively engage with the Government, regulators and key stakeholder groups in Hong Kong, Mainland and other key jurisdictions to discuss regulatory issues affecting the industry. In all the dialogues, investors' best interests is front and center and our key objective is to come up with an effective and proportionate framework that would accord adequate protection to investors.

Apart from continuously enhancing the regulatory framework, we believe that investor education is pivotal as it empowers them. We educate the public about the role of investment funds in retirement planning and other aspects of personal financial planning, with the ultimate objective of ensuring that investors can make informed decisions and can fully harness the benefits of funds to meet their goals at the different stages of life.

The HKIFA has four categories of members, namely full member, overseas member, affiliate member and associate member.



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Publication number: HK-FS20-0002

Publication date: June 2020