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STRATEGIC INSIGHT™

GLOBAL FUND INSIGHTS

FIRST QUARTER 2014 RESULTS

$300 Billion Inflow Driven by More Balanced Demand Across Asset Classes

- After gaining almost $1 trillion in net flows in 2013, the global mutual fund industry continued to expand strongly in the first quarter of 2014, totaling nearly $300 billion in net new cash into long-term products despite geopolitical concerns in Europe, an economic slowdown in China and other emerging markets, and increasing discussions around Federal Reserve interest rate hikes in the US.

- Q1'14 net flows were the highest during the past four quarters — 60% higher than the amount collected in the prior quarter — driven by more balanced demand across different asset classes. Equity funds still led the contributions (garnering $110 billion), but bond funds, benefiting from a combination of investors' safety and income needs, rebounded sharply with $90 billion in net gains. Mixed and multi-asset funds gathered $58 billion in Q1, while other types of funds took in a total of $35 billion for the quarter.

- In Europe including both local and cross-border products, European stock and bond topped the best-selling categories during the first quarter of 2014, collecting nearly $60 billion altogether in net flows. Thirty-one funds captured at least $1 billion in net new cash in Europe (including cross-border markets) totaling $53 billion in Q1.

- In Q1'14, flows increased substantially (to $18 billion) for alternative hedge-style funds, compared to $14 billion in net gains for the full-year 2013. The latest quarterly flows were the highest since Q2'07, when including fund of hedge funds tracked in Strategic Insight's Simfund GL database. This is mainly due to the increasing demand for alternative UCITS products.

- Local fund flows in Asia turned positive in Q1 with a small gain of $3 billion, improved from the prior quarter's $9 billion in net outflows. In addition, Asian fund buyers deposited roughly net $9 billion into mostly Luxembourg- and Ireland-domiciled UCITS funds during Q1, accounting for 25%-30% of the worldwide flows into cross-border funds that are registered for sale in Asia, highlighting Asia as an important market for UCITS funds.

- Yu'E Bao, an Internet-based money market fund product introduced by Alibaba in May 2013 in China, saw its AUM exceed $87 billion as of Q1'14, making it the fourth largest money market fund in the world — in only 10 months. For the mutual fund industry in China, this might become a turning point for online distribution of mutual fund products within the country.

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Simfund Global

Data from this report is primarily sourced from Strategic Insight's Simfund Global databases, which cover 120,000 portfolios across Asia, Europe, the Americas, and Australia. Simfund integrates information from various sources and includes net flows, assets, returns, risk, ratings, portfolio holdings, fees, share class details, and hundreds of other fields in a flexible analytical solution.

Publications

This report is provided to clients of Strategic Insight's Global Research Service. Publications include:

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First Quarter 2014 Results

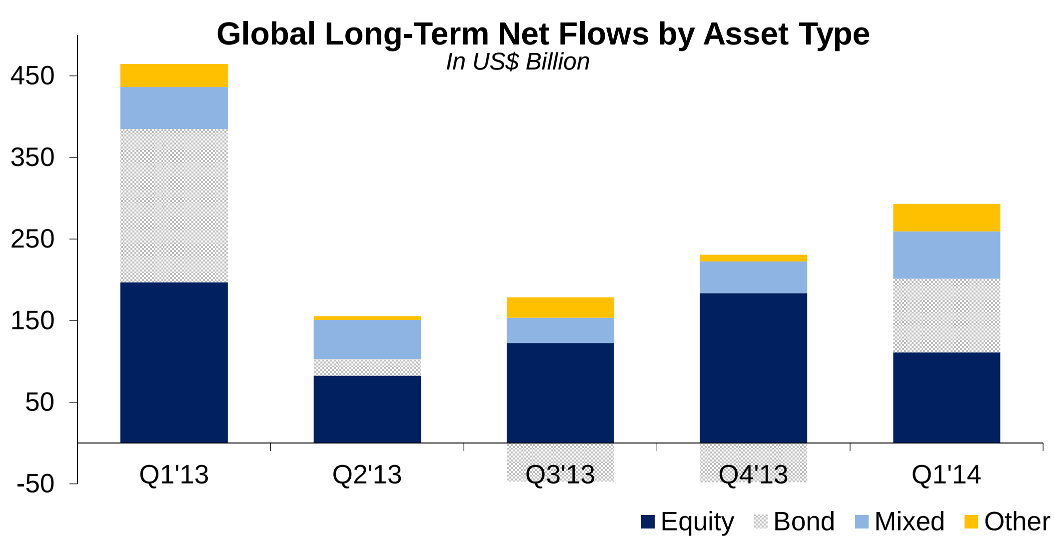
$300 Billion Inflow Driven by More Balanced Demand Across Asset Classes

After gaining almost $1 trillion in net flows in 2013, **the global mutual fund industry continued to expand strongly in the first quarter of 2014, totaling nearly $300 billion of net new cash into long-term products** despite geopolitical concerns in Europe, an economic slowdown in China and some other emerging markets, and increasing discussions around Federal Reserve interest rate hikes in the US**.**

As shown in the chart below, after achieving the record high quarterly result during Q1'13, global mutual funds absorbed less inflows mainly due to the sharply declined demand for bond funds that was triggered by the sudden rise in bond yields that began in May last year. Nevertheless, fund flows worldwide remained stable with $100+ billion quarter by quarter until Q1'14, during which net flows jumped to reach $300 billion, 60% higher than the amount collected in the prior quarter ($180 billion), driven by more balanced demand across different asset classes.

Equity funds still led the contributions (garnering $110 billion), but their share of flows decreased to 38% in Q1'14; in comparison, stock funds captured more than 100% of total long-term fund flows during Q4'13. Bond funds, on the other hand, benefiting from a combination of investors' safety and income needs, rebounded sharply with $90 billion in net gains during Q1, a large improvement compared to $48 billion in net redemptions in the prior quarter. Mixed and multi-asset funds gathered $58 billion in Q1, which was $20 billion higher than during the previous quarter. Meanwhile, 'other' types of funds, including guaranteed, real estate, and alternative investment funds took in $35 billion during Q1'14, the highest quarterly result in three years since Q1 2011.

Figure 1



**Includes US, Asia, Europe and Cross-Border*
Source: Strategic Insight Simfund GL and MF

Excluding money market programs, cross-border and local European funds captured $150 billion (€120 billion) altogether during Q1, the highest volume since the first quarter of last year. Gains were more evenly spread across all asset classes, with bond funds taking the lead and accounting for 36%, while stock and mixed funds took in 22% and 30%, respectively; the remaining 12% went to 'other' types of products.

Figure 2

Global Mutual Fund Net Flows, Q1 2014

In US$ Billion

	Equity	Mixed	Bond	Other**	Subtotal L-T	Money Market	Total
Int'l/Cross-Border	26.2	13.2	34.4	21.6	**95.3**	33.5	**128.8**
Europe (local)	6.1	31.7	20.0	-3.5	**54.5**	5.0	**59.5**
Asia (local)*	7.2	-2.5	-5.2	3.4	**2.9**	96.1	**99.0**
US (ex VA)	71.3	15.2	41.4	14.2	**142.1**	-89.7	**52.3**
Total	***110.7***	***57.7***	***90.6***	***35.7***	***294.7***	***44.9***	***339.7***

** Cross-border funds sold in Asia collected $9 billion in net flows during Q1*

***Other includes Absolute Return, Commodities, Hedge, Guaranteed, Real Estate and certain unclassified funds.*

Source: Strategic Insight Simfund GL and MF

Local fund flows in Asia turned positive in Q1 with a small gain of $3 billion, improved from the prior quarter's $9 billion in net outflows. Excluding China, which suffered $27 billion in net redemptions, locally domiciled Asian funds actually attracted $30 billion in Q1, with more than half of the flows going to equity funds. Japan captured the most inflows with $24 billion, followed by Thailand and India, each contributing around $3 billion. In addition, Asian fund buyers net deposited roughly $9 billion into mostly Luxembourg- and Ireland-domiciled UCITS funds during Q1, accounting for 25%-30% of the worldwide flows into cross-border funds registered for sale in Asia, reflecting the region as an important market for UCITS funds. Indeed, Hong Kong, Taiwan, and Singapore contributed more inflows (around $8 billion in Q1) to cross-border funds than many European markets.

In the US, long-term funds gathered $140 billion in net flows during the first three months of 2014, more than half of which went to stock and asset allocation programs. Bond funds accounted for 29% or $41 billion, after experiencing aggregate outflows of $50 billion in Q4'13. In the equity space, passive ETF and index funds attracted $28 billion, out of which $19 billion were from US strategies; active stock funds gained $43 billion, mostly from international and global strategies. For more details please refer to Strategic Insight's Q1 US report: **Windows Into the Mutual Fund Industry May 2014**.

Globally, money market products garnered nearly $50 billion in net flows during Q1'14, mostly coming from Internet-based products in China ($110 billion), which more than offset the net redemptions out of the US money funds.

European Highlights

In Europe including both local and cross-border products, European stock and bond topped the best-selling categories during the first quarter of 2014, collecting nearly $60 billion in net flows. Bond Europe was especially strong, benefiting from heavy institutional demand, taking in $26 billion during Q1 and surpassing its full-year flows from 2013 ($15 billion). Other best-selling categories included Bond High Yield, Alternative, and Equity North America with net gains between $12 billion and $18 billion for the quarter. Notably, mutual funds with hedge-style alternative strategies[1], excluding funds of hedge funds, attracted nearly $18 billion in net flows, the highest quarterly results since Q2'06.

Excluding target maturity products, mixed and multi-asset categories (including absolute return multi-asset funds) continued to gather stable money flows, with $40 billion added in Q1'14. Global and US bond categories also witnessed inflows in aggregate, but selected Bond Global and Bond USD products, particularly those with longer maturity and duration — such as Templeton Global Bond and Total Return, PIMCO GIS Total Return, and AllianceBernstein-American Income — saw large net redemptions during the quarter.

Figure 3

Best and Worst Selling Strategies, Q1 2014

In US$ Billion

		Net Flows		AUM	Wgt-by-end TR %
	Category	**1Q'14**	**2013**	**1Q'14**	**1Q'14**
Best	Equity Europe	**30.0**	53.3	1,497.6	2.60
	Bond Europe	**26.0**	14.8	1,090.8	2.27
	Bond High Yield	**18.0**	48.6	344.6	2.40
	Alternative	**17.5**	13.5	202.3	0.90
	Equity North America	**12.5**	27.2	386.0	1.45
	Total Above	**104.0**	**157.3**	**3,521.4**	
Worst	Bond Asia Pacific	**-2.1**	-0.7	30.1	0.86
	Bond Emerging Markets	**-6.6**	5.0	218.5	2.09
	Equity Asia Pacific	**-7.2**	16.8	344.6	-1.33
	Equity Emerging Markets	**-11.0**	-4.9	311.9	-1.16
	Guaranteed/Protected	**-11.6**	-25.2	204.0	1.12
	Total Above	**-38.5**	**-9.0**	**1,109.0**	
	Total Europe	***149.8***	***432.7***	***8,151.7***	

**Excludes fund of funds internal and fund of hedge funds; long-term funds only*
Source: Strategic Insight Simfund GL

Overall, the categories with the largest outflows in Q1'14, as shown in the table above, consisted of Emerging Market and Asia Pacific stock and bond funds, as well as guaranteed and protected funds, totaling $38 billion in net redemptions. In fact, both equity categories were the only fund categories experiencing negative returns during Q1, reflecting investors' concerns over emerging market dislocation.

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[1] Based on Simfund Global's propriety alternative categories, excluding non-traditional bond, absolute return, commodity, real estate, and infrastructure products.

During Q1'14, investors focused more attention on products that could generate higher income, have less exposure to rising interest rates, and are less correlated to market volatility, including **flexible multi-sector** and **unconstrained bond**, **high yield bond**, **multi-asset income**, and certain **alternative investments**. According to Strategic Insight's proprietary Simfund Global database, 31 long-term funds captured at least $1 billion in net new cash in Europe (including cross-border markets) — totaling $53 billion in Q1. Bond funds, including Absolute Return Bond, led the contributions with 15 products collecting $24 billion in net flows. Among them, seven Bond High Yield products amassed $9.8 billion altogether, with a significant amount of money sourced from Asian investors through cross-border fund sales, while three Bond Flexible Multisector funds added $6.1 billion.

Figure 4

Top-Selling funds* in Europe and Cross-Border, Q1 2014

Portfolio	Manager	SI Objective	Launch	Domicile	Net Flows Q1'14	2013	AUM 03/14	Perf 12m
M&G Optimal Income	M&G Investments	Bond Flexible Multisector	Dec-06	UK	**3.5**	8.3	32.6	17%
Morgan Stanley Diversified Alpha Plus	Morgan Stanley	Alt - Global Macro	Jun-08	Lux	**3.2**	3.4	8.1	24%
Gestielle Cedola MultiAsset	Banco Popolare	Mixed Flexible	Jan-14	Italy	**3.2**		3.2	
Allianz Income and Growth	Allianz	Mixed Balanced	May-11	Lux	**3.2**	3.4	6.8	21%
Foncaixa Rentas Octubre 2018	La Caixa	Target Maturity	Nov-13	Spain	**2.8**	0.8	3.8	
Generali Inv SICAV USD Inv Grade Corp Bd	Generali	Bond USD	Mar-14	Lux	**2.0**		2.0	
Goldman Sachs Global High Yield Pf	Goldman Sachs	Bond High Yield	Jan-98	Lux	**2.0**	1.4	10.8	7%
Schroder GAIA Sirios US Equity	Schroders	Alt - Long/Short - US	Feb-13	Lux	**1.9**	0.9	2.9	15%
BGF Global Allocation	Blackrock	Mixed Balanced	Jul-93	Lux	**1.9**	2.9	20.1	9%
Generali Diversif USD Inv Grade Corp Bond	Generali	Bond USD	Oct-13	Lux	**1.9**	1.6	3.5	
Ignis Absolute Return Government Bond	Phoenix Group	Absolute Return Bond	Mar-11	Lux	**1.7**	2.3	4.9	18%
Alken Fund - Absolute Return Europe	Alken AM	Alt - Long/Short - Europe	Jan-11	Lux	**1.7**	1.3	3.5	20%
UBS (Lux) Bond Fd - Euro High Yield (EUR)	UBS	Bond High Yield	May-98	Lux	**1.7**	1.3	4.3	19%
ING (L) Renta Fund Global High Yield	ING	Bond High Yield	May-01	Lux	**1.5**	5.1	8.1	14%
Invesco Pan European High Income	Invesco	Mixed Conservative	Mar-06	Lux	**1.5**	1.5	3.5	23%
Invesco Pan European Equity	Invesco	Equity Europe	Jan-91	Lux	**1.4**	1.9	4.9	38%
Goldman Sachs Global Strategic Income Bond	Goldman Sachs	Bond Flexible Multisector	Mar-11	Lux	**1.4**	2.3	4.0	4%
Franklin Biotechnology Discovery	Franklin Templeton	Equity Sector/ Other	Apr-00	Lux	**1.3**	1.0	3.2	49%
Fidelity Funds - Global Dividend	Fidelity	Equity Global	Jan-12	Lux	**1.3**	2.7	4.3	22%
Allianz US High Yield	Allianz	Bond High Yield	Aug-10	Lux	**1.3**	2.5	9.0	6%
DWS Invest Euro Bonds (Short)	Deutsche AWM	Bond Euro Short	Jun-02	Lux	**1.3**	2.1	4.5	11%
PIMCO GIS Income	PIMCO	Bond Flexible Multisector	Nov-12	Ireland	**1.2**	4.1	5.5	4%
Focused Fund - Corporate Bond USD	UBS	Bond USD	Sep-03	Lux	**1.2**	2.4	4.2	1%
Fidelity Funds - European High Yield	Fidelity	Bond High Yield	Jun-00	Lux	**1.1**	1.3	5.8	18%
Pictet-EUR Short Term High Yield	Pictet	Bond High Yield	Jan-12	Lux	**1.1**	2.3	5.2	14%
BNY Mellon Absolute Return Equity	BNY Mellon	Alt - Long/Short - Europe	Jan-11	Ireland	**1.1**	1.0	2.6	15%
DNCA Invest Eurose	Dnca Finance	Mixed Conservative	Jun-07	Lux	**1.1**	1.5	4.0	21%
Vanguard S&P 500 UCITS ETF	Vanguard	Equity North America	May-12	Ireland	**1.1**	2.3	3.7	21%
Neuberger Berman High Yield Bond	Neuberger Berman	Bond High Yield	May-06	Ireland	**1.1**	2.9	13.3	7%
Anima Traguardo 2019 Multi-Asset	AM Holding	Target Maturity	Jan-14	Italy	**1.0**		1.0	
SLI Glo SICAV Global Abs Rtn Strategies	Standard Life	Absolute Return Multi-Asset	Jan-11	Lux	**1.0**	3.4	9.4	
Total					***52.6***	***67.9***	***202.8***	

**Funds with over $1 billion net flows during Q1 2014; Excludes fund of funds internal and fund of hedge funds; Long-term funds only*
Source: Strategic Insight Simfund GL

M&G's flagship Optimal Income topped the best-seller list in Q1, collecting $3.5 billion. It ranked as the second highest cash flow fund in 2013 with $8.3 billion. The $33 billion flexible multisector bond fund, which grew more than tenfold in assets since 2009, is now the third largest bond fund in Europe — only behind Franklin Templeton's Global Bond and Total Return. There are, however, increasing concerns on concentration and capacity risks, as well as market risks, as we have witnessed large redemptions coming from similar sized funds. Examples include Pimco Total Return in the US, Franklin Templeton Global Bond in Europe, and Kokusai Global Sovereign Open in Asia.

Mixed and multi-asset funds continued to draw strong inflows ($16 billion from eight funds), including strategies such as target maturity products (Italy and Spain), traditional global asset allocation (Blackrock), global multi-asset income (Allianz), Europe focused (Invesco and DNCA), and absolute return multi-asset (Standard Life). In the equity space, four stock funds garnered $5 billion, ranging from European equity (Invesco) and global dividend income (Fidelity), to passive US ETF (Vanguard) and the health care sector (Franklin). Among the highlights by selected funds:

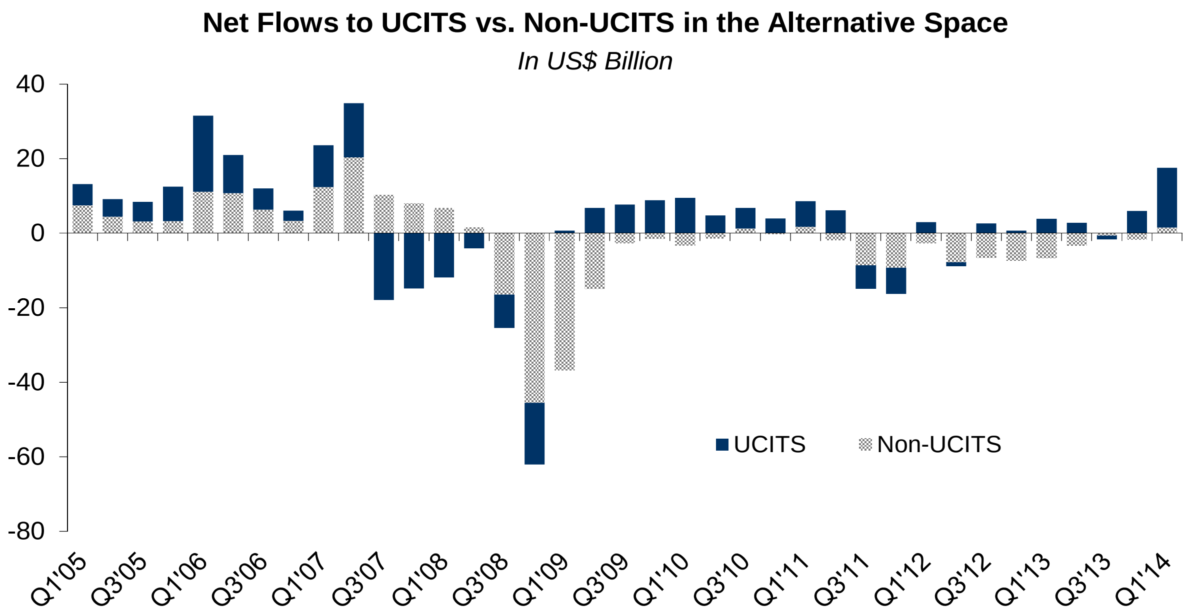
- **Goldman Sachs Global Strategic Income Bond** is a non-traditional bond fund that employs an opportunistic and unconstrained macro and credit strategy and invests in a variety of debt instruments globally. This Luxembourg-domiciled UCITS was launched in March 2011 and raised nearly $4 billion in assets ($1.4 billion in net flows in Q1'14) since inception. GSAM's US '40 Act mutual fund, GS Strategic Income, managed by the same Global Fixed Income Group, has achieved even larger success in the US, raising almost $21 billion in assets since its inception in June 2010, with $6.2 billion in net new money along during Q1'14.
- **Franklin Biotechnology Discovery** seeks tactical opportunities in the health care sector, investing at least 80% in equity securities of biotechnology companies and discovery research firms worldwide (with the majority in the US). The fund, also a Luxembourg-domiciled UCITS, took in $1.3 billion in net flows during Q1, pushing its total AUM to $3.2 billion thanks to a stellar return of 49% during the past 12 months. The fund's US '40 Act version, Franklin Biotech Discovery, only raised $1.5 billion in AUM since its launch in 1998, despite achieving an even better return of 51% for the last 12 months.
- **DNCA Invest Eurose**, gaining net flows of $1.1 billion (Q1'14) and $1.5 billion (2013), is a conservative mixed fund investing in stocks and bonds (including convertible) of Eurozone companies. Equity exposure is limited to 35% but the fund is not constrained to a benchmark. The fund's manager, DNCA Finance, controlled by US private equity firm TA Associates, is one of the largest independent fund management boutiques in France. The fund company has a distribution network covering France, Belgium, Switzerland, Germany, Austria, and Italy. **DNCA Invest Eurose** and **DNCA Invest Evolutif** are among the current best sellers at Cortal Consors, BNP Paribas's direct bank and online platform in France, Germany, and Spain.
- **Ignis Absolute Return Government Bond**[2] absorbed $1.7 billion and $2.3 billion in net flows during Q1'14 and 2013, respectively. The fund aims to deliver positive returns lowly correlated to other asset classes by investing in developed-world sovereign debt and AAA-rated supranational bonds. The fund can also take long and short positions in derivatives, which helps achieve returns even in an environment with rising interest rates. The UK-based investment boutique specializes in absolute return strategies in the bond arena, which is part of the reason that the firm was recently bought by Standard Life, which owns the largest absolute return fund in the word – the $33 billion **Standard Life Investment Absolute Return Strategies fund.**
- A few cross-border funds in the list have the majority of their money sourced from Asian investors. The details are discussed in the Asian Highlights section on page 11.

[2] The fund is classified under SI category Absolute Return Bond, as it focuses largely on long strategies in the bond space.

Alternative and UCITS Platforms

In Q1'14, flows increased substantially (to $18 billion) for alternative hedge-style funds[3] (the best quarter since Q2'06), compared to $14 billion in net gains for the full-year 2013. If we include fund of hedge funds[4] that are tracked in Strategic Insight's Simfund Global database, the latest quarterly flows also reached $18 billion — the highest since Q2'07, when JP Morgan's Highbridge Statistical Market Neutral Fund collected $8 billion in three months[5].

Figure 5



Source: Strategic Insight Simfund GL

Alternative hedge-style strategies now represent almost $300 billion of assets in the European fund industry, with UCITS vehicles that enjoy daily or weekly liquidity accounting for nearly 60% of the total AUM. Indeed, alterative hedge-style UCITS or Newcits funds grew more than five-fold since 2004 and reached $170 billion in AUM as of March this year, according to Simfund GL.

As illustrated in the chart above, alternative UCITS funds generated mostly positive quarterly flows after the 2008 financial crisis, while non-UCITS alternative funds, consisting largely of funds of hedge funds, suffered mostly net outflows. During Q1'14, four alternative funds attracted at least $1 billion in net new cash, and all of them are UCITS vehicles using long-short and/or macro strategies, aiming to generate absolute returns while actively managing risks and liquidity.

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[3] Based on Simfund Global's propriety alternative categories, excluding non-traditional bond, absolute return, commodity, real estate, and infrastructure products.

[4] Funds of hedged funds only garnered $0.1 billion in Q1'14, but suffered $14 billion in net redemptions in 2013.

[5] JP Morgan Highbridge Statistical Market Neutral was launched in November 2006 and collected over $10 billion in net flows during the first half of 2007, then suffered $5.5 billion in net redemptions in the second half of 2007 after posting significant losses in July and August, trigged by liquidity shortage due to the sharp rise in defaults in the US sub-prime mortgage market.

- The $8 billion **Morgan Stanley Diversified Alpha Plus** was the second best-selling fund in Europe and cross-border, absorbing $3.2 billion in net flows during Q1'14 and almost matching the fund's 2013 full year result ($3.4 billion). The fund's objective is to provide a positive return in all market conditions, while actively managing total portfolio risk. The fund manager seeks to identify and exploit inefficiencies between markets, regions, sectors, and asset classes by researching large macro factors across all asset classes globally.
- **Schroder GAIA Sirios US Equity** raised $2.9 billion in assets since its launch in February 2013 ($1.9 billion in Q1'14) and is the flagship fund on the firm's **GAIA platform** (Global Alternative Investor Access). The fund takes long and short positions with a focus on US equities, but it also can invest in fixed income securities and convertible bonds, as well as expand its investments globally.
- **Alken Fund – Absolute Return Europe**, a long-short fund focusing on European equities, aims to generate positive returns and preserve capital, while managing the fund's volatility lower than 50% of the volatility in Stoxx Europe 600. The fund was soft closed to new investors due to the capacity issue after its AUM reached $3.5 billion in March this year.
- Similarly**, BNY Mellon Absolute Return Equity**, another long-short European equity fund but with a UK bias, was also soft closed due to capacity control in March ($2.6 billion in AUM). The fund was launched in January 2011 and is managed by London-based Insight Investment. It shares the same investment strategies as Insight's **Absolute Insight Equity Market Neutral** (also soft closed with over $1.9 billion in AUM in March), a UK OEIC launched in 2005.

There has been increasing demand for alternative solutions packaged within the UCITS framework coming from institutional and high net worth investors in Europe, also in Asia, Latin America, and other regions.

After the financial crisis, fund buyers seem to have gradually steered away from traditional fund of hedge funds approaches as investors globally have placed a greater emphasis on transparency, risk and volatility control, and liquidity — due partially to tightened regulatory oversight. For example, fund of hedge funds that are tracked in Simfund GL collectively experienced $120 billion in net redemptions since the beginning of 2009; on the other hand, hedge-style alternative UCITS funds gained $80 billion in net flows during the same period. Some large hedge fund managers such as **Man Investment** and **GAM** have launched their own alternative UCITS funds, or converted existing hedge strategies into the UCITS format. At the same time, many traditional asset managers have also entered this space by setting up their own alternative investment units and/or introducing alternative UCITS platforms by working with external hedge fund managers around the world. Some of them are highlighted below:

- **Merrill Lynch Investment Solutions (MLIS)**, launched in 2007, is one of the first platforms to offer externally managed hedge funds within the UCITS framework. Currently, the platform has AUM of more than $3 billion in 22 funds managed by 14 external hedge fund mangers — Och Ziff, York Capital, Beach Point Capital, Columbus Circles Investors, GLG Partners, Marshall Wace, Theorema, Boyer Allan, Graham Capital, AQR, Perella Weinberg, TT International, Sandell, and Zweig-DiMenna — as well as by Merrill Lynch's in-house arm of alternative investment.
- Schroders' **GAIA platform** was launched in November 2009 and offers investors access to UCITS funds adapting liquid alternative investment strategies with moderate to low correlations to

traditional stocks and bonds. The GAIA platform currently manages $5.6 billion in seven funds, four of them managed by external hedge fund managers (Sirios, Egerton, CQS, and Avoca), and three managed internally (QEP Global Absolute, Global Macro Bond, and Cat Bond). More recently, Schroders has partnered with John Paulson to launch **Schroder GAIA Paulson Merger Arbitrage fund**, with its fundamental merger arbitrage strategy based on the $1.7 billion Paulson International Limited fund, which has generated an annualized net return of more than 12% since its inception in 1996.

- **Morgan Stanley FundLogic Alternatives Platform** is part of the firm's Multi-Asset Platform and started to provide alternative UCITS funds in late 2010. The platform offers approximately 20 funds, which focus on alternative strategies such as long-short, relative value, event driven, and global macro. The total assets on the platform reached $1.5 billion in 2013. The recently added managers include Broadmark, Dalton, and TCW — all US-based firms.
- Other UCITS platforms include **Alceda** (the largest independent UCITS platform in Europe), ML Capital's **Montlake, SEB Prime Solutions, Deutsche Bank Platinum**, **UBS Liquid Alpha, Lyxor**, **Universal Investments** (the largest UCITS platform in Germany), **Matrix, Merchant Capital, Goldman Sachs International, Signet SERIES, Prodigy Capital Partners,** and **Nomura Enovara.**

Notably, the client base of alternative UCITS funds is still very much European (although also from Asia and Latin America), but many of the managers on the UCITS platform are US based, particularly if the platform providers are also US firms, as the country still owns the majority of hedge fund specialists in the world. Small- and medium-sized US hedge fund managers have shown particular interest in UCITS platforms because they are a cost effective way to access a large number of investors outside the US and meet their increasing demand for greater liquidity and regulatory oversight. For instance, in April **New York based Sandell Investment** launched an event-driven UCITS fund on MLIS, and **Stamford, Connecticut based Ardsley Partners** launched an US equity long-short UCITS fund on MontLake.

Some US hedge fund managers may face more choices regarding promoting their products beyond traditional client bases, as a growing number of hedge fund firms begin to offer their strategies in a 40' Act format. During Q1'14, the demand for market neutral and long-short strategies was also strong in the US, where alternative mutual funds garnered $15 billion of net deposits overall. However, in addition to targeting a different client base outside the US, UCITS funds have an important advantage over 40' Act funds: UCITS funds allow performance fees (many funds charge a performance fee between 15% and 20% on top of a 1.5%-2% of management fee) while US 40' Act funds usually don't charge performance fees. When US hedge fund managers launch similar strategies in the 40' Act format, they have to justify a performance fee charged on hedge fund clients, as some of them might move to the 40' Act funds with similar strategies.

More broadly, the so-called "liquid alternative funds," which include non-traditional bond and strategic income funds, have seen strong demand in the US, Europe, and other regions. As the investment world is increasingly adapting to an asset allocation culture, liquid alternatives are expected to have a great potential to replace some of the traditional bond funds currently used to anchor asset allocation.

Asian Highlights

During Q1'14, local long-term funds in Asia managed to gain a moderate $3 billion in net flows, but the top 20 highest cash flow products attracted nearly $17 billion in the region. Japan led the way (collecting $9.4 billion through 12 funds), followed by China (with $2.9 billion in four funds), while Korea, Hong Kong, Taiwan, and Thailand each contributed a best seller for the quarter.

Notably, stock funds accounted for the majority the net flows ($9.9 billion) and a number of the best sellers (11), but two-thirds of the equity fund flows went to seven passive ETFs. Nevertheless, a few active stock funds with unique strategies also made progress. For example, **Great Wall Healthcare Sector Equity** in China took in $0.4 billion amid the new healthcare measures that encourage private investment in the sector[6]. Japan's **OkasanAM Asia Oceania Good Dividend Growth Equity**, an equity income product, also garnered $0.4 billion during the quarter.

Figure 6

Top-Selling funds in Asia, Q1 2014

Portfolio	Manager	SI Objective	Launch	Domicile	Net Flows		AUM
					Q1'14	2013	03/14
Nomura Nikkei 225 ETF	Nomura	Equity Japan	Jul-01	Japan	**1.8**	2.2	18.3
Nomura Deutsche High Dividend Infra Related Equity	Nomura	Equity Sector/ Other	Oct-10	Japan	**1.6**	4.2	5.6
Nomura NF Nikkei 225 Leveraged ETF	Nomura	Equity Japan	Apr-12	Japan	**1.6**	0.7	2.7
ICBCCS 7 Days Cash Management	ICBC Credit Suisse	Bond CNY Short	Aug-12	China	**1.5**	-0.6	5.5
Fidelity US High Yield	Fidelity	Bond High Yield	Apr-98	Japan	**1.3**	5.9	11.5
Nomura Topix ETF	Nomura	Equity Japan	Jul-01	Japan	**1.0**	1.0	15.2
Samsung KODEX Leverage Derivatives ETF	Samsung	Equity Korea	Feb-10	Korea	**0.9**	0.5	2.6
iShares FTSE A50 China Index ETF	Blackrock	Equity China	Nov-04	HK	**0.7**	0.3	6.9
Daiwa High Grade CAD Bond Open	Daiwa	Bond Other	May-03	Japan	**0.7**	4.7	5.4
Shinko US-REIT Open	Shinko	Real Estate	Sep-04	Japan	**0.7**	5.1	11.0
MitsubishiUFJ Global Financial Organization Hybrid 1401	Mitsubishi UFJ	Bond Global	Jan-14	Japan	**0.5**		0.5
Daiwa ETF Nikkei 225	Daiwa	Equity Japan	Jul-01	Japan	**0.5**	1.4	7.8
Amundi Euro High Yield Bond	Amundi	Bond High Yield	Oct-11	Japan	**0.5**	1.7	2.0
Invesco Great Wall Flexible Allocation	Invesco Greatwall	Mixed Flexible	Aug-13	China	**0.5**	0.1	0.7
Franklin Templeton SinoAm Global High Yield Bond	Franklin Templeton	Bond High Yield	Jun-12	Taiwan	**0.4**	0.4	1.2
Galaxy Sector Selected Stock	Galaxy AM	Equity China	Apr-09	China	**0.4**	0.0	0.8
OkasanAM Asia Oceania Good Dividend Growth Equity	Okasan	Equity Asia Pacific ex-JP	Oct-05	Japan	**0.4**	1.7	4.7
SCB Savings Fixed Income Open	SCB Asset	Bond Asia Pacific Local	Feb-97	Thailand	**0.4**	0.4	3.7
Great Wall Healthcare Sector Equity	Great Wall	Equity China	Feb-14	China	**0.4**		0.4
DIAM Nikkei 225 No-Load	DIAM	Equity Japan	Aug-98	Japan	**0.4**	-0.6	1.4
Total					***16.6***	***28.8***	***107.9***

**Excludes fund of funds internal and fund of hedge funds except for Japan; long-term funds only*
Source: Strategic Insight Simfund GL

In addition to some local currency short/ultra short bond products, high yield bond funds remained popular across Asia, benefiting international managers such as **Fidelity, Amundi,** and **Franklin Templeton**. Other best-selling funds include a Canada Bond and a US real estate fund in Japan, as well as a flexible mixed fund in China.

A few recent developments in Japan could have a big impact on the country's asset management industry in coming years. A newly created JPX-Nikkei 400, jointly developed by Nikkei, Japan Exchange Group, and Tokyo Stock Exchange (and with selection criteria based on ROE, governance, size, and liquidity),

[6] For more details please refer to Strategic Insight's New Funds In Global Markets: Q1 2014

was launched in January 2014. Since then, 18 JPX-Nikkei 400 ETFs were launched in Q1, totaling $0.8 billion in net sales. Moreover, the index is likely to see strong demand from institutional investors, as GPIS (Government Pension Investment Fund), the world's largest pension fund with $1.24 trillion in assets, is adding the JPX-Nikkei 400 Index among new benchmarks, while at the same time reducing passive investments based on the Topix index.

As the old policy of tax reduction on capital gains expired at the end of 2013, Japanese government introduced the tax-advantaged **Nippon (Japan) Individual Savings Account (NISA)** at the beginning of this year. NISA not only works as the tax-exempt account but also aims to encourage the younger generation to participate in growth-driven investments, which means potentially less switching of funds and less frequent dividend payouts. Recently, fund distributors in Japan have been trying to reduce their switching style business and market existing funds for NISA. Some old funds with a long track record and/or with a consistent dividend payout history have been selling well. In the new fund launch space, nearly 900 new funds were launched during 2013 in preparation for the start of the NISA. The majority of these funds only distribute dividends annually or bi-annually — accounting for more than half of the total new fund sales. In comparison, in 2009 and 2010, 60% of the total new fund flows went to funds with monthly distribution payouts. However, the long-term impact of the NISA is not yet known, as the majority of money flows to the NISA so far have been coming from existing investors — they have simply switched their existing investment from regular mutual funds to the NISA.

Beyond the locally domiciled products, Asian fund buyers net purchased roughly $9 billion from cross-border funds sold in the region, with Hong Kong, Singapore, and Taiwan (the core Asian markets for international managers) collecting about $8 billion altogether in net cross-border fund flows during Q1. Stock funds dominated fund sales in the cross-border space in Asia, with European, Global, and sector equity strategies each collecting at least $2 billion, while multi-asset income funds also garnered around $2 billion in Q1. Although bond funds saw net redemptions in aggregate, Bond High Yield remained in demand particularly in Taiwan.

Indeed, some cross-border best sellers have greatly benefited from Asian investors, particularly from Hong Kong, Taiwan, and Singapore. Allianz's **US High Yield** and **Income and Growth** both recorded significant flows coming from Hong Kong Dollar and Singapore Dollar share classes, in addition to large inflows to US Dollar classes registered for sale in the region. **ING Renta Fund Global High Yield Portfolio** attracted another $1 billion in net flows in Taiwan on top of last year's $3 billion, which helped the fund reach $8 billion in assets as of Q1'14 — 59% of them contributed by Taiwan investors. **Neuberger Berman** worked in partnership with E.SUN Commercial Bank to distribute its flagship **High Yield Bond Fund**, attracting $0.5 billion in Q1 and $1 billion last year in Taiwan. Moreover, the firm has expanded its fund range in Hong Kong (11 funds) and Singapore (3 funds) available to retail investors in these two markets. **Franklin Biotechnology Discovery** also saw over 50% of its flows from Asia.

Looking forward, we expect equity strategies focusing on Europe, Global, and selected sectors, as well as bond high yield products to continue to sell well in the Asian cross-border markets. Alternative investment strategies, on the other hand, may have difficulty selling to retail investors in the region, mainly due to scrutiny of regulators, but their appeal to Asian institutional and high net worth investors has been growing.

Money Market Funds and Online Distribution Platform in China

In May 2013, two years after the PayPal Money Market Fund failed in the US, the Chinese mutual fund company **Tian Hong Asset Management** launched **Yu'E Bao**, its first fund product in cooperation with **Alipay,** China's leading third-party online payment company, an affiliate of **Alibaba** that is arguably the largest e-commerce company in the world. This is potentially a turning point for online distribution of mutual fund products within the country.

Yu'E Bao is an Internet-based investment product for settlement funds held by users in Alipay. Alipay is a major form of payment for **Taobao and Tmall** (both are subsidiaries of Alibaba), which are Chinese versions of eBay and Amazon, but with total revenue exceeding the two American giants combined. Alipay users can have cash from their Alipay account automatically invested in Yu'E Bao and can redeem anytime with no transaction fees. Yu'E Bao then invests in Tian Hong's money market fund, which can achieve a much higher return than bank deposits by investing in short-term securities with higher market rates, as **regulated deposit rates have been kept artificially low due to interest rate control in China.**

Yu'E Bao offers an annualized yield of between 4.5% and 6%, higher than the one-year deposit rate of 3% offered by commercial banks — much higher than an annual interest rate of 0.35% in regular savings accounts. According to Simfund GL's March 2014 data, the fund has an expense ratio of 0.63%, and its total AUM has already exceeded $87 billion from more than 80 million investors, marking it the fourth largest money market fund in the world — in just 10 months. Meanwhile, Alibaba acquired a controlling stake in Tian Hong and has signed agreements with several other fund companies, aiming to build China's first online mutual fund shopping mall.

After witnessing the success of Yu'E Bao, other Internet giants in China have followed suit: **Baidu, the Chinese version of Google,** cooperated with China AMC, the largest mutual fund company in China by AUM, to launch its cross-over product, **Baifa,** with a targeted annual return of 8%. **WeChat,** the most popular online chatting tool in China, also worked with leading Chinese fund firms such as China AMC, China Universal, GF Fund, and E Fund to launch its first mutual fund product, **Licaitong,** in January 2014.

In order to compete with Yu'E Bao like products, commercial banks in China started working in December with fund managers to roll out their own MMFs that allow individual investors to invest their savings with the banks into such products. As of Q1'14, there are more than 40 Internet money market products – they are estimated to account for $150 billion - $170 billion in AUM or roughly 70% of the total MMF assets in China.

Indeed, Internet finance in China has been developing rapidly, partly due to the fast adoption of new technology, coupled with the further liberalization of financial and banking systems. Chinese regulators have also closely monitored the further development and evolvement of the industry. It is still true that the complexity of long-term investment funds, including higher market risk and volatility, makes them more difficult to be distributed through the Internet. However, the convenience of the Internet products, the economy of scale due to a huge user base, and the potentially more accurate design and marketing of financial products could really change how mutual funds are manufactured, distributed, and serviced in the future.

Top 30 Active Managers in Q1, ex US

The table below lists the 30 highest cash flow managers outside the US, ranked by total net flows collected through their actively managed long-term funds during the first three months in 2014.

Figure 7

Top Active Managers in Q1 2014

Long-Term Funds In Europe, Asia and Cross-border Ranked By Q1'14 Total Net Flows

Manager	2013 Total Net Flows US$ Bil	Q1'14 Total Net Flows US$ Bil	% of Flows to Total by Asset Type in Q1'14: Equity %	Bond %	Mixed %	Other %
UBS	-3.9	***9.2***	28%	67%	6%	-1%
Blackrock	15.8	***7.5***	37%	23%	34%	6%
JP Morgan	36.9	***6.8***	58%	30%	6%	6%
Generali	3.6	***5.0***	6%	96%	-1%	-1%
Goldman Sachs	8.2	***4.4***	17%	76%	-2%	8%
Allianz	7.3	***4.2***	-22%	15%	105%	2%
Morgan Stanley	2.9	***4.0***	12%	-1%	0%	88%
BNY Mellon	6.8	***3.9***	36%	7%	-4%	60%
Invesco	8.2	***3.9***	26%	48%	24%	2%
Intesa Sanpaolo	6.1	***3.8***	-7%	-20%	97%	30%
Henderson	4.0	***3.8***	41%	7%	10%	42%
Dnca Finance	4.2	***3.2***	18%	8%	65%	8%
Mercer	5.7	***2.9***	31%	50%	13%	6%
Amundi	-2.1	***2.9***	38%	76%	-21%	7%
Neuberger Berman	6.9	***2.8***	32%	68%	0%	0%
Standard Life	14.1	***2.8***	20%	13%	16%	51%
Deutsche AWM	8.8	***2.7***	-35%	119%	35%	-19%
Fidelity	5.6	***2.6***	38%	54%	7%	1%
Nordea	9.1	***2.6***	0%	79%	12%	9%
Santander	0.4	***2.5***	14%	18%	92%	-25%
Pioneer Investments	7.7	***2.5***	41%	62%	13%	-15%
DNB Group	3.3	***2.5***	27%	69%	4%	1%
Union Investment	7.5	***2.3***	6%	27%	60%	7%
Schroders	12.9	***2.2***	-50%	68%	35%	46%
Svenska Handelsbanken	4.6	***2.1***	16%	56%	12%	16%
Alken Asset Management	3.5	***2.1***	15%	0%	0%	85%
Man Group	0.5	***2.0***	21%	35%	0%	45%
AM Holding	4.4	***2.0***	-10%	-9%	104%	15%
M&G Investments	8.6	***1.9***	-77%	151%	4%	22%
Sumitomo Mitsui	4.9	***1.9***	37%	13%	15%	35%
Total Above	***206.5***	***103.0***				

Source: Strategic Insight Simfund GL

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