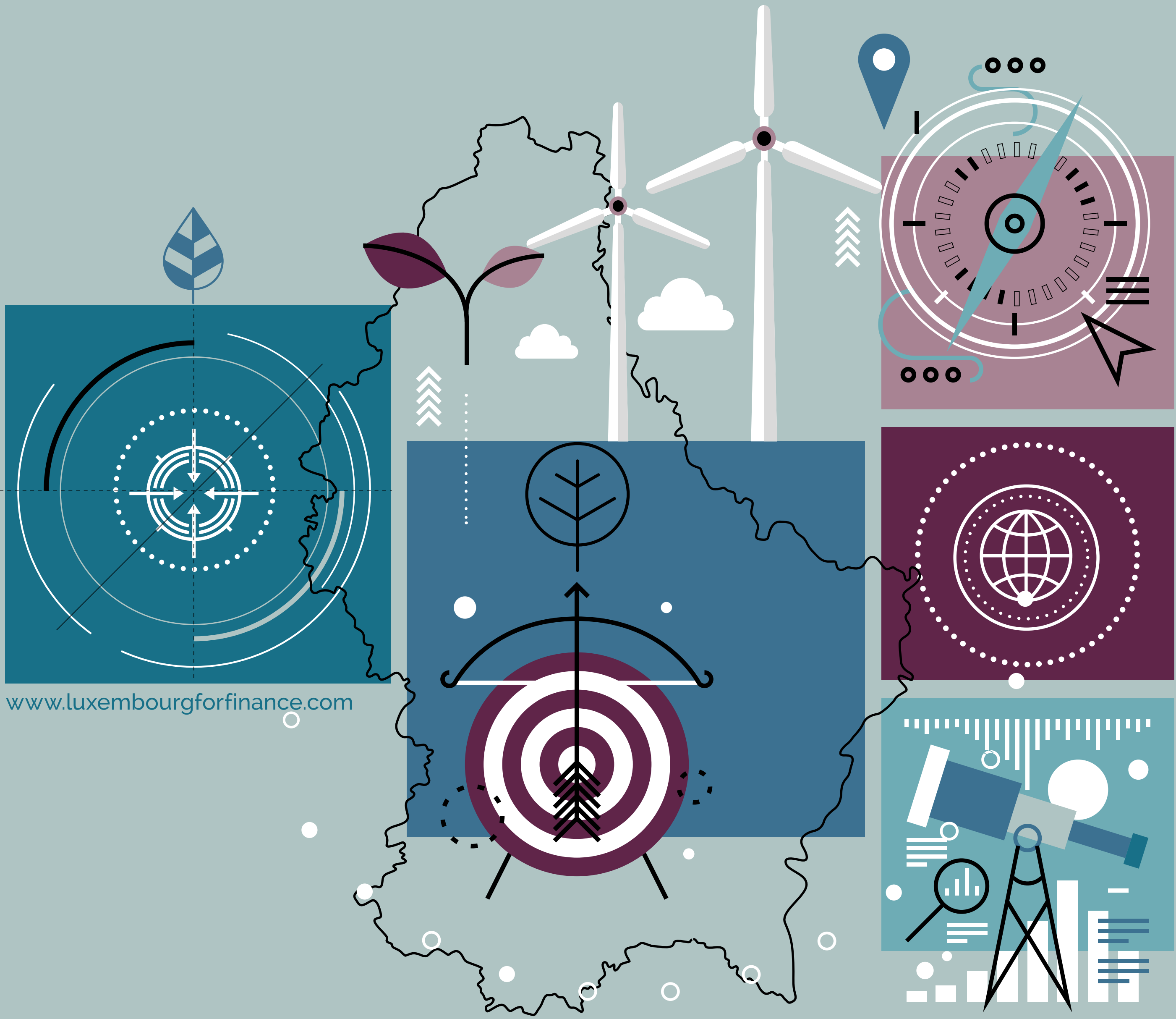
Amazonisation

is the future of European Financial Services



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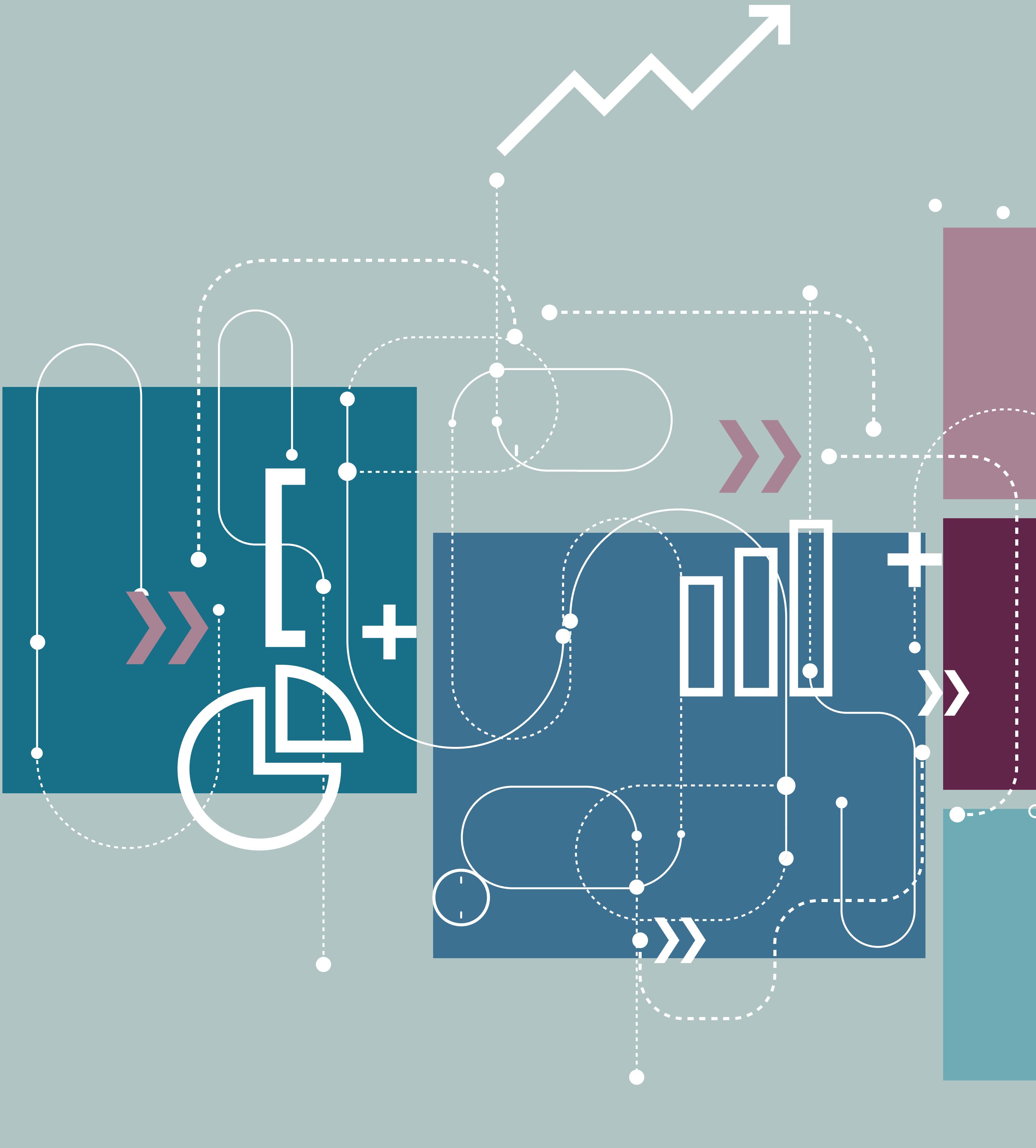

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Foreword

PIERRE GRAMEGNA
Luxembourg Minister of Finance

Observers outside of the European Union could be forgiven for thinking that the future of European financial services is entirely determined by Brexit, given the extent to which this topic has been in the limelight of public debate these past few years. However, as this report shows, there are larger global trends that will have much more profound and long-lasting effects on the EU financial services' landscape than Brexit: these include the far-reaching impact of digitalisation, a global shift towards sustainable investments and, importantly, the need for Europe's financial industry to be able to compete successfully with the US and rising Asian centres.

While Brexit is an issue that European governments and the financial industry have to deal with in the short- to mid-term, the strategic priority should be the strengthening and further completion of the European Single Market for financial services. Paradoxically, Brexit has not only increased pro-EU sentiment in the remaining EU member states but has also underscored the benefits for companies, be it in finance or in other industries, of having unfettered access to the world's largest economy and trading block.

The EU has come a long way since the Global Financial Crisis (GFC) and the ensuing debt crisis in the Euro Area. Thanks to the banking union, a project that many at the time doubted would ever come to fruition, Europe's financial industry is today better equipped to weather storms than in the past. The banking union is indeed a regulatory project of unprecedented scale, which has managed to restore trust in Europe's banking sector.

Over the past decades, Europe's financial sector has grown ever closer: UCITS has created, arguably, Europe's most successful export product, and AIFMD is on the right track to repeat this success in the European alternative investment fund industry. Thanks to MiFID and IDD, investors are benefitting from increased transparency and better investor protection across the EU. While SEPA, PSD and PSD2 have lowered the barriers to entry and costs for pan-European payments, these initiatives have driven innovation in payments and have inspired regulators in other parts of the world.

At the same time, there is no reason to be complacent. Compared to other regions, and especially the US, Europe's capital markets remain fragmented and the continent is still overly reliant on banks when it comes to financing. European firms, in particular small and medium enterprises, today still primarily turn to bank lending to finance their growth, notably due to a lack of alternative sources of financing, especially in a cross-border context. Similarly, less than 20% of European households' financial assets are invested in shares, bonds and investment funds.

There are sufficient grounds for optimism, however: EFAMA figures show that thanks to increasing integration through EU regulations such as UCITS, AIFMD and MiFID, the share of cross-border funds in Europe has steadily grown from 25% in 2008 to 32% in 2017. The European fund industry is indeed a perfect illustration of a well-functioning value chain in the Single Market, relying on the complementary expertise of European financial centres such as London, Paris, Frankfurt, Dublin and of course Luxembourg.

Completing the Capital Markets Union (CMU) should therefore be a priority, as it will help speed up the further completion of the Single Market, increase access to a wider source of cross-border financing, as well as create new cross-border investment opportunities.

In June 2017, a year after the Brexit referendum, the European Commission updated its CMU action plan. This new version, which one could also call CMU 2.0, includes provisions aiming to encourage financial technology in capital markets and develop a more sustainable approach to finance. These are rightly seen as priorities as both represent opportunities for Europe's financial sector to remain competitive in a fast-changing global environment. In order to compete globally with the US and China, which are home to the worlds' largest tech giants and Fintech firms, Europe has to break down regulatory and digital barriers. In parallel to the CMU, the EU's Digital Single Market project has a crucial role to play in this context.

It is not surprising that out of Europe's five Fintech unicorns, three are payment service providers. Thanks to the payment services directive, payments is the only Fintech segment directly benefitting from EU-wide regulation and consequently passporting across European markets. This example shows that by generating cross-border opportunities, a frictionless Single Market can be a catalyst for creating European champions that can compete on a global scale.

Europe is already the leading market for sustainable investment, accounting for 73% of global sustainable investing assets in 2018. Driven by client demand, especially institutional investors, new product innovation, as well as increased scrutiny and regulatory initiatives, sustainable investing will continue to grow and to move from niche to norm. Thanks to ongoing regulatory action on a taxonomy for environmentally sustainable activities, disclosure and benchmarking, the EU is well positioned to play a leading global role in sustainable finance.

Whether it is in financial technology or sustainable finance, Europe is larger than the sum of its parts and stands to benefit from the economies of scale that only the Single Market can provide. Rather than as a group of domestic markets, it is only through a pan-European financial sector that the EU can truly compete at the global level with the large and homogenous economic blocks that are the US and China.

NICOLAS MACKEL

Luxembourg for Finance CEO

The aftermath of the financial crisis has played out differently in Europe, in the US and in Asia. While financial institutions in Europe battle to digest the increased burden and costs of compliance and risk management regulation, the sector has bounced back with energy in Asia and in the US, and has thus been able to forge a stronger position for itself in the global marketplace.

A lot has been written about each of the three major trends impacting the industry: amazonisation, Brexit and sustainable finance, but the interest of this report lies in showing how they will profoundly change the European financial services industry together.

While Brexit is an epoch-making event that will alter the organisational set-up of the institutions as well as the market; digitalisation will be transformative by changing the very nature of the activities as well as of the players and sustainable finance is ultimately existential to mankind's survival.

These three trends of amazonisation, mainstreaming of sustainable finance and multipolarisation will certainly test the industry beyond what we can predict today and we will witness many innovators struggling with the dilemma of changing their business model to adapt to the new circumstances. This capacity for adaptation is what will define success in the future, for individual institutions as well as for financial centres.

If we want to create the necessary scale to boost innovation in financial services, it is crucial that we tackle these three trends via action at the EU level. It is vital if we want to make sure our climate-related activity has adequate impact and we can use our weight as leverage to rally others behind our actions. More EU action is also needed to mitigate the effects of the departure of the UK from the single market and to build a true EU Capital Markets Union.

Please allow me to thank colleagues from PwC for their work and partnership in producing this report, as a valuable contribution to the debates on the issues affecting the financial industry in Europe and beyond.

JOHN PARKHOUSE

PwC Luxembourg Senior Partner and CEO

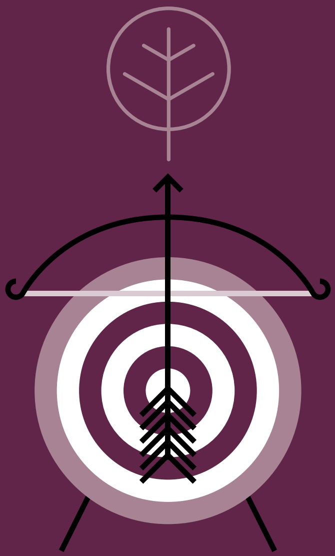
It has been a little over ten years since the Global Financial Crisis and its effects remain. It is ever pervasive in the minds of those working in the financial services sector. The actions that we take are guided by the lessons learned, and perhaps more importantly not learned, from this event. With many experts stating that a slowdown of the global economy is coming, we constantly ask ourselves whether we have done enough to ensure we are protected.

Regulators and institutions across the globe will continue to introduce new regulations, provide supervision and attempt to keep risks under control. However this requires walking a fine line to regulate without stifling competition. As we look into the future of European financial services in this report, we note that this balance must be struck. European financial services must not be subjected to such strenuous rules that it is unable to compete on the global stage, it must be able to flourish and grow. At the same time, we cannot afford to repeat the mistakes of the past.

China continues to grow and the US remains the leading financial services destination. European asset managers have lost pace and banks and insurers are struggling with the low interest rate environment. However, as new regulations are introduced they are relaunching competitiveness in areas such as Banking and Payments. The growth of Defined Contribution plans will help insurers close the pension gap and the rise of investment platforms in the Asset and Wealth Management space changing the very face of distribution. At the same time, technology has become inescapable and we are seeing the rise of FinTech players across the spectrum and new partnerships across the financial and technological sector.

It is crucial that Europe grabs hold of the opportunities within its grasp, from those stemming from technology and the rise of new generations, to the growth of continental European financial services stemming from Brexit. We are keeping a firm eye on the horizon, taking the best from new developments and opportunities, exchanging views from a number of experts situated throughout the region, and ultimately, positioning Europe as a leading financial services destination.

Executive summary



Barack Obama once said of Europe, "Your accomplishment – more than 500 million people speaking 24 languages in 28 countries, 19 with a common currency, in one European Union – remains one of the greatest political and economic achievements of modern times."[1] Europe's financial services (FS) sector plays a crucial role in advancing this achievement – promoting European businesses, funding infrastructure projects, helping individuals save and creating employment.

Despite murmurings of a divided Europe once more, often spurred by Brexit, Europe is larger than the sum of its parts. This resonates keenly with the financial services sector – economies of scale and the strong links between financial centres contribute to unlock investment for, and in, Europe. Despite sustained effects from both the Global Financial Crisis of 2008 and Sovereign Debt Crisis on European Financial Services, Europe has recovered well in recent years.

Low interest rates have pushed bond prices up, increasing the value of liquid assets held by banks and improving their liquidity ratios. Additionally, the cost of refinancing debt has reduced and EU member states have been able to lower their debt to GDP ratios – enabling them to invest more freely into rejuvenating their economies. European markets have also seen a strong recovery. The boat rocked slightly in 2018 with overall market volatility, but assets have continued to rise and the trend looks set to continue. Asset owners, especially institutional, continue to drive debate in this area, specifically concerning governance and sustainability.

Regulations are creating both burdens and opportunities for financial institutions in Europe. They have, as expected, increased costs and the need for reporting. However, regulations, such as Markets in Financial Instruments Directive II (MiFID II), have begun to make investor protection a reality, and Basel IV is set to further strengthen and harmonise banks capital requirements. Regulations such as Payment Services Directive II (PSD2), are said to help foster next-level innovation.

Looking to the future, we postulate how the European Financial Services landscape is set to develop up to 2025. We have identified four main sectors, namely Banking and Capital Markets, Asset and Wealth Management, Payments, and Insurance, which constitute the majority of financial services. Naturally, there are themes that echo across sectors, such as fading profitability, rising compliance costs, changing client preferences and emerging technologies.

Looking forward, we believe the future of the European financial services industry will be driven by three trends, namely amazonisation, sustainable finance and multipolarisation. This reflects a fundamental shift that is occurring across Europe's financial services industry.

The drive towards client centricity, both retail and commercial, is a clear factor leading toward amazonisation. This means that clients, rather than going to individual FS firms, will use digital platforms to inform, compare and execute their financial transactions and this applies to both retail and commercial clients. Such platforms will seek to become a marketplace by aggregating as many financial services products as possible, including third party products and their own. This will provide the client with a transparent comparison of the characteristics and pricing of products, as well as comments of other clients who bought their products. Clients will then be able to select the product they believe will provide them with the best value for their money. We could have named this report the "Facebookisation" or "Expediasation" of European financial services, but we selected Amazon due to its unique connection to the platform operating model.

The rise of environmental and social awareness in societies across the world is already leading to an increased demand for sustainable finance products and we expect this to continue. In fact, in our view, the second largest key success factor for European FS players will be sustainable finance, driven by the rise of the millennial population and their client preferences. Financial actors across the globe, from regulators and associations to banks and asset managers have begun to put sustainable finance at the forefront of their thinking. Sustainability will become a necessity for FS players as they look to satisfy client demand and meet the shift in investor behaviour.

Finally, driven by Brexit and the loss of a global financial centre, namely London, European financial services is set to become multipolarised. While the loss of London will be a setback, it also serves as a silver lining for many European financial centres to hone their specialisations and increase their complementarity. Some centres will exceed others, becoming specialists in certain industries and leading industries globally and in Europe.

1. Barack Obama, Remarks by President Obama in Address to the People of Europe, Hannove Messe Fairgrounds, Hannover, Germany, 25 April 2016.

These centres will leverage on their expertise to make Europe one the leading financial services hubs worldwide.

While themes will emerge across sectors, each will see unique factors that will drive its growth.

Amazonisation will push banks to become whole solution providers

Change is becoming more and more pressing as European banks have been losing their competitive edge globally, especially in comparison to countries such as China and US. We believe, in order to succeed in the future, European banks will need to embrace Amazonisation, becoming aggregators of products and one-stop shops for clients' banking needs.

European banks are currently experiencing profitability struggles and upcoming regulations are set to increase their already stringent lending requirements. Banks must therefore look in a new direction. They must take advantage of new developments taking place in the open banking sphere and product ranges linked to sustainable financing.

Banks must become aggregators of not only their own, but others' innovative products. This means leveraging technology and regulations to determine where to gain cost efficiencies, while still providing excellent client service.

Amazonisation of AWM is a blessing and a curse

Pressure from all angles is intensifying in the Asset and Wealth Management (AWM) space. Investors and regulators are calling for firms to adhere to their fiduciary duty, to lower fees and provide a frictionless technology-enabled, available experience. At the same time, increased competition means European managers must now become best-in-class.

Amazonisation will separate the wheat from the chaff. Managers must strive to provide the best value for money to investors, embrace transparency as an opportunity, adapt to new realities, drive new business through platforms and support the challenges facing the European economy. Managers cannot afford to ignore the growing pressure that they face regarding ESG (Environmental, Social and Governance). It is critical that managers align their strategic plan with investors' evolving needs, otherwise European AWMs risk falling further behind.

Amazonisation of payments set to lead the charge towards cashless societies

Amazonisation will hit payments specifically at the point of sale (POS). Challenger banks and FinTechs will further exploit the inefficiencies of current cross-border money transfer fees and processes to disrupt this area. More and more European countries are moving towards becoming cashless, spurred on by rapid technological advancement, a new consumer generation and a regulatory environment that encourages innovation.

Payment Service Providers (PSPs) have already begun to analyse client purchasing behaviour, but this will go further, providing consumers with intelligent systems that maximise the value of each payment. As the sector further Amazonises, traditional players must look to those companies on the leading edge of innovation and follow their examples.

Amazonisation set to disrupt insurance distribution value chain

When looking to adapt to Amazonisation, insurers must focus on improving the client experience. Transparency of products and pricing will be key as consumers gravitate towards the products best suited to their needs. In order to disrupt the traditional insurance world, insurers must adopt a "do or die" mentality. At the same time, leveraging the mountains of data will be crucial to profitability as more and more customers demand usage-based insurance.

Our recommendations

Amazonisation will drive Europe's financial services sector in the coming years and a number of opportunities will present themselves. Europe must be proactive and seize these opportunities where possible. We make a number of recommendations that we believe must be considered in order to position Europe for growth and success:

1. Firms must disrupt themselves
   As Amazonisation takes hold across the financial services industry, players will need to become the disruptors themselves lest they lose out to players who do. This requires firms to become cost effective, nimble and highly competent. Technology will be key for these players and they will need to ensure that they are using data in the most efficient manner possible in order to have a long term sustainable business model.

2. Deepen cross-border integration of Financial Services
   Financial integration across Europe is critical for creating pan-European financial champions who are able to compete on a global level. More effective and deeper financial markets will allow companies better access to credit. To achieve deeper cross-border integration, a unified banking union and a finalised CMU are crucial to create a holistic European Financial Services sector.

3. Strengthen innovation and the digital dimension of Europe's single market
   Rapid technological innovation has become a major driver of global growth within the financial services industry and will continue to propel growth for years to come. Europe needs to proactively seek out opportunities to make innovation a priority. The European Commission has already made innovation a critical element of its future plans, with many FinTechs especially attracted to Europe. However, the lack of uniform regulation can make accessing the single market a difficult task. These issues will need to be addressed before Europe can truly compete on a global scale.

4. Lead the sustainable finance race
   Climate change has already affected all aspects of financial services in Europe, with the European Union having been vocal in its support of the United Nations' Sustainable Development Goals (SDGs) and the Paris Climate Agreement. We have already seen European Financial Services step up to the plate in some areas. The EIB, for example, has allocated EUR100 billion annually to help close the giant funding gap required to meet the SDGs. Europe also leads the race in terms of sustainable investing, with just under half of ESG assets stemming from Europe. However, with North America rapidly gaining on Europe in this space, there are a number of actions that European regulators and businesses could take, such as common taxonomy development, portfolio screening and making sustainability reporting mandatory. While profitability could shrink in the short term, businesses that respond fastest to client demand in this space should reap the benefits on a long-term basis.

In recent years, European financial services have escaped the shadows cast by the GFC and recent Sovereign Debt Crisis and made a strong comeback. However, in order to maintain a strong global presence in the future, financial services companies in Europe must look beyond their P&Ls and look to harness emerging trends. Europe must become more proactive, investing in new technologies and pushing for sustainable investment, rather than reactive. Should all actors align on a future vision for Europe and work towards it, setting ambitious yet achievable goals, and ensuring they make concerted efforts to come together to achieve these goals, Europe will remain a major player in the financial services space.

1.

Looking into the mirror: Ten years post the Global Financial Crisis

Across the globe there are renewed talks of a market slowdown. Financial markets have begun to falter, GDP growth forecasts have been revised downwards for both developed and developing countries, and quantitative easing programs are tapering or have already ended. It's not all doom-and-gloom for Europe – Eurozone household debt fell to its lowest levels since 2006, new regulations provide consumers with more protection and pave the way for innovation, and Europe is one of the leading regions driving the sustainability agenda.

Overall, the recovery from the last crisis was lengthy and Europe lost footing on the global stage. Brexit (at the time of writing negotiations were still ongoing) is set to further weaken the sector significantly. But there are opportunities that, if grasped, could allow Europe to remain competitive in the coming years.

EUROPEAN ECONOMIC RECOVERY WAS LENGTHY AND WEAK

Economic rebounds differed across regions; the US was quick to react and recovered swiftly, while developing and emerging Asia GDP almost doubled in the decade following the crisis. China was, naturally, the shining star – posting sustained economic growth (12.9% CAGR between 2007 and 2017) and implementing ambitious fiscal and monetary measures, albeit at the cost of increasing public and private debt. Europe, on the other hand, stagnated somewhat as the region's competitiveness fell[2] and the Sovereign Debt Crisis further lengthened the recovery.

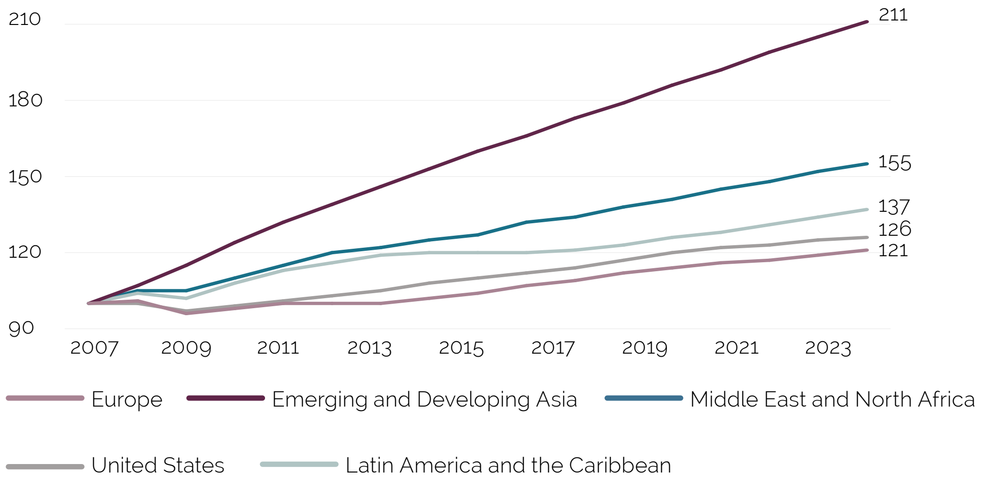
The effect of the Sovereign Debt Crisis is visible on European GDP (see Figure 1).

The recovery process stalled and set the region significantly behind others. The tight links between governments and banks, the so-called Sovereign-Bank Nexus[3], worsened the resolution of the Euro Area crisis as banks had increased exposure to bonds in order to ensure liquidity. Banks had a home bias, especially in countries where the risk premium was higher, investing in local bonds and tightening the connection between their financial position and the country. Additionally, they had substantially increased their balance sheets due to the 0% risk weight for local sovereign bonds. These factors compounded the already serious debt crisis and were worsened by the fact that Europe's unconventional monetary response was delayed, with Quantitative Easing only being introduced as of 2015.

2. Europe's financial market competitiveness, based on the World Economic Forum's Global Competitiveness Index, plunged from 4.9 in 2007 to 4.1 in 2015, rising slightly to reach 4.3 at end 2017. Despite the minor rise, Europe stands significantly lower than both the US (5.7) and Asia (5.0).

3. The Sovereign-Bank Nexus refers to the fact that banks and sovereigns of one country are mutually exposed to each other's stability, performance and future outlook. It operates through three channels: sovereign-exposure channel, safety net channel and the macroeconomic channel. More information on the Sovereign-Bank Nexus can be found here: Dell'Ariccia, Giovanni, et al., Managing the Sovereign-Bank Nexus, 2018.

Figure 1: Evolution of GDP in constant prices, 2007-2023e



Source: PwC Market Research Centre, past data based on International Monetary Fund
Note: Base is 100 in 2007

Europe's financial services sector has faced many challenges since the financial crisis. Despite having overcome these, other challenges persist. Non-performing loans (NPLs) remain, although the ratio of NPLs in percentage of total gross loans and advances has consistently decreased, down 1.2% year-on-year[4], eventually falling to 3.4% as of the end of Q2 2018. The incomplete CMU, delayed by Brexit, has weakened progress on Europe's financial integration considerably.

This integration will be crucial for spreading risk across the union, thereby reducing the effects of country-specific shocks. It will also help foster economic growth, provide new sources of financing, and support innovation throughout the union. Another challenge lies in monetary policy normalisation, which is creeping ever to the fore. However, whether the ECB plans to return to interest rate levels seen prior to the crisis or if there is a new normal, is yet to be defined.

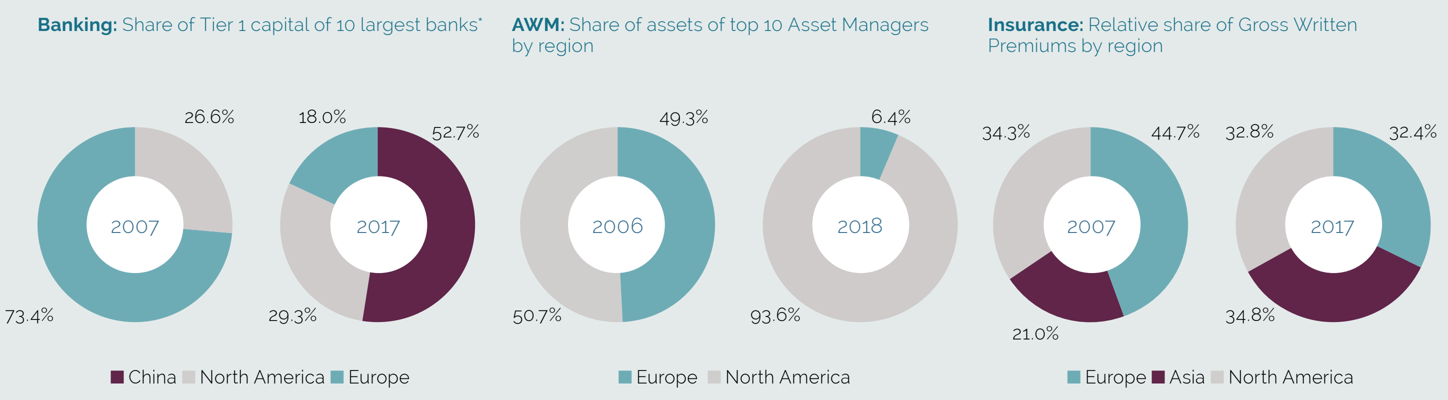
4. European Commission, Third progress report on the reduction of non-performing loans and further risk reduction in the Banking Union, November 2018.

THE EUROPEAN FS SECTOR HAS LOST SIGNIFICANT GROUND

The impact of legacy systems, weak performance and paltry profitability has weighed on the European FS sector. US and Chinese banks dominate the global rankings, Europe-based asset managers have fallen far behind their US competitors, and Asian insurance markets now dwarf others across the globe (see Figure 2). However, challenges facing the industry prior to the crisis still remain, in particular the technological changes that require businesses to reassess their operating models. The globe has undergone fundamental changes and Europe must adapt before it falls further behind.

Post crisis, European banks have consistently lost ground, both in terms of assets and profitability, while Chinese and US have gone on to dominate global rankings. As of end 2017, the top 10 European banks' profit before tax amounted to US$90.4 billion, compared to US and Chinese counterparts, who amounted to US$159.8 billion and US$237.6 billion respectively[5]. The US Treasury's quick introduction of the Troubled Asset Relief Program (TARP)[6] ensured that US banks' competitiveness was quickly restored following the crisis. China's strong economic growth naturally contributed to booming bank business in the Asian region and local support from the government continues to be a strong driver of bank growth.

Figure 2: European Banks, Asset and Wealth Managers and Insurers fall behind



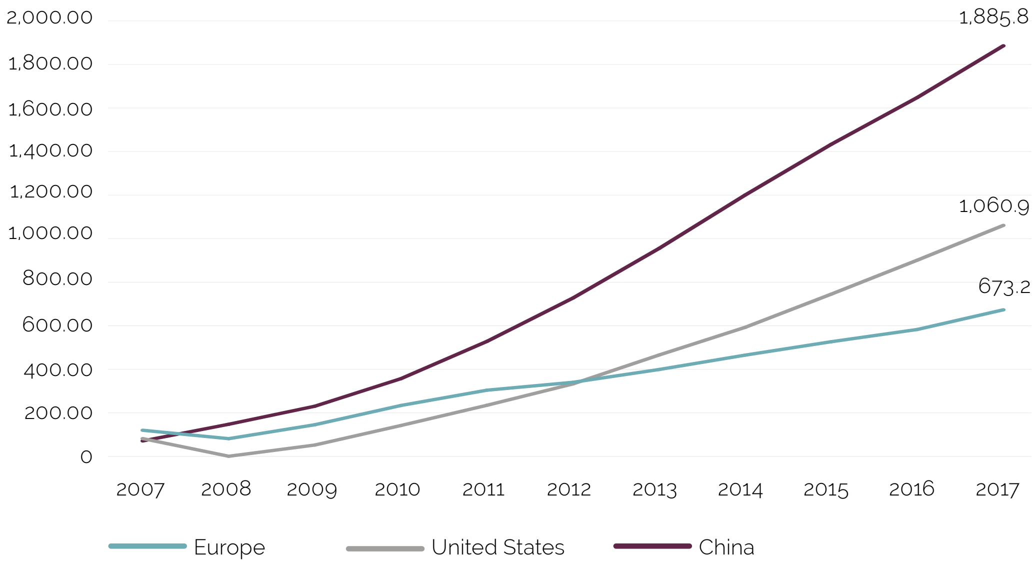
Source: PwC Market Research Centre based on The Banker, IPE, Insurance Europe and OECD
*China not included in 2007 as no Chinese banks were present in the top 10

5. PwC Market Research Centre based on The Banker
6. TARP was signed into law by President George W. Bush on 3 October 2008. Originally authorised expenditures amounted to US$700 bn, however this was later revised down to US$475 bn. The program effectively came to an end when the US treasury sold its remaining holdings of Ally Financial on 19 December 2014. TARP, in total, recovered US$441.7 bn from an investment totaling US$426.4 bn, therefore making a profit of US$15.3 bn.

Historically low interest rates dragged down bank profitability following the crisis (see Figure 3). The ECB's refinancing operations rates were set at low levels and returns from earning assets declined significantly. An additional factor was that Europe's fee and commission revenues were low compared to the US as well. The outlook for European banks remains unclear, with higher than average NPLs posing a continued challenge to profitability. In the coming years, tightening monetary conditions could help allay fears of sustained diminished profitability, however this is likely only to be seen from 2020 onwards.

Europe's AWM industry has suffered similar setbacks, with the top ten managers holding only US$6 trillion in AuM at the end of 2017 compared to the US top ten who held US$22 trillion. Asian managers might hold significantly fewer assets, but their growth has been phenomenal, with the top ten posting a 19.3% CAGR over the last ten years. Many European managers failed to capitalise on passives in the early stages, while certain US managers jumped on the bandwagon at an early stage.

Figure 3: Cumulative profits before taxes of top ten banks by region, US$ billion



Source: PwC Market Research Centre based on The Banker

While AWMs' profitability has yet to truly be hit, this is expected in the coming years. Management fees have seen a downwards trend in recent years, with European active funds seeing a decrease of 4.9% between 2012 and 2017, and passive funds' management fees dropping by 13.2% over the same period.[7] With the somewhat recent introduction of MiFID II, management fees are likely to sharply decrease in the future.

Insurers in Europe tell similar stories. Shrinking Gross Written Premiums (GWPs) following the crisis, due to decreasing penetration and the low interest rate environment, have led to the sector significantly losing weight globally. Asian GWPs, on the other hand, flew past both European and North American markets, increasing by 78.9% from 2007, compared to Europe's decrease of 16.7%. The global non-life sector has hit a weak spot in the profitability cycle, with a high level of capital fund, weak investment performance and poor underwriting conditions.

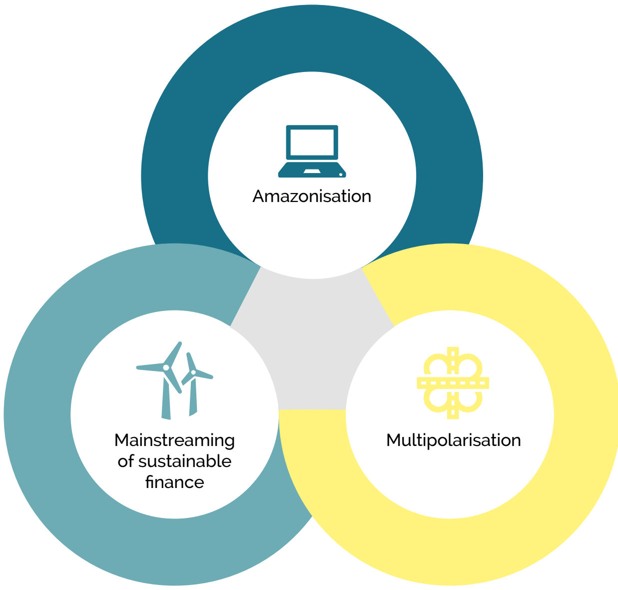
The weak spot was fairly prevalent in advanced economies, with Europe maintaining a 3.1% growth rate in 2017 thanks to growing private medical insurance, alongside household and residential covers and motor insurance. Rates are clearly under pressure, with the US recording a 4.8% growth rate, whereas China recorded a 10% growth in 2017. On the life side, however, markets have rebounded from the poor performance seen in recent years, with Europe growing at 5.4% between 2012 and 2015. The UK fell significantly behind and only recorded a 1.6% growth rate between 2012 and 2017. China once again surged ahead, growing by 18.3% between 2012 and 2016. Clearly advanced markets are feeling the pressure and insurers have begun to fall behind.

7. PwC, *Asset and Wealth Management Revolution: Pressure on profitability*, October 2018.

2.

Three trends shaping the future of the European financial services industry

The future is always somewhat uncertain, but we have identified three trends which we believe will structure the future of European financial services.



Amazonisation

Amazonisation relates to the shift of power towards the client, where platforms will be the dominant client-facing usage interface within the financial services industry. Retail and commercial clients will be able to search, buy and manage the products, providing them the best value for their needs according to the parameters defined by them on the platform at the best price. Further, they will be able to see comments and reviews from other buyers before making their choice.

These platforms will allow for transparency and comparability. They will either be run independently, offering only third-party products, or run by financial services companies offering access to a marketplace of both their own- and third-party products. The leading platforms will cover the majority of products on the market and will be easy to use. In order to adapt to this shift, businesses must promote client focus and ease of use, provide best value for money and whole solutions, and be at the forefront of innovation and new technology implementation.

The increased level of access to and sophistication of technology means that online platforms will become not only valuable comparison tools for FS customers, but new product distribution methods. In other words, these platforms can become a one-stop shop for both comparing and purchasing products. This empowers the customer through better access to information, enabling them to select the best value products.

Millennials are set to become the dominant demographic in the consumer population and this will also drive Amazonisation across financial services. The shifting attitudes of financial services customers will facilitate the aforementioned move to online platforms where financial services providers can offer their products. However, with younger people perhaps more hesitant to trust corporations, FS companies will also rely on peer-to-peer and independent reviews rather than on traditional marketing in order to sell their products. Each product will be assigned a ranking based on set KPIs, with the products providing best value for money on the top of the list.

Another aspect that has arisen from the spread of digital technology is the collection of client data. With data analytics rising to the fore, FS companies are now able to harness client data in order to deliver what their customers want. The rise of AI will further accelerate this process, with AI programs able to use this data to build a client profile for each individual customer. AI will then be able to suggest FS products for each individual which fall in line with their client profile. In this situation, the client will only need to confirm this decision, thereby expediting the decision process and offering a more personalised service.

Meanwhile, regulators globally are keen to avoid the same pitfalls that led to the GFC just over a decade ago, hence we have seen a raft of new regulations implemented across all FS sub-sectors. The focus of many of these, such as MiFID II and PRIIPS, has been primarily on offering more transparency. This trend towards transparency enables financial services customers to clearly determine the value for money that products offer, therefore enabling them to accurately compare the offerings of different financial services providers.

In the context of Amazonisation, the EU recently agreed on a new set of rules that seek to boost the transparency and fairness of third-party online platforms (PSD2). In this environment, the FS providers who offer the best products and best value will be able to rise to the top, promoting product innovation. In this future, where data and online platforms will be vital to success, current technology players such as Google, Apple and Amazon will have the opportunity to provide marketplaces for FS products. From a financial services player's perspective, now is the time to withdraw uncompetitive captive products and move towards becoming the best-in-class. Alternatively, FS firms may look to fully evolve into an independent platform, providing value for money solutions to clients.

Mainstreaming of sustainable finance

There is also an increased awareness among the global population regarding the environment. This has slowly changed all facets of everyday life and is fundamentally changing the way consumers look at financial products. Millennials will soon also become the dominant demographic in the consumer population, a shift which will drive the burgeoning sustainable finance industry even further. With a massive wealth shift expected between baby boomers and millennials, as well as their desire for impactful investments, we expect to see strong growth in this segment in the coming years.

In the future, we believe that almost all FS products will be sustainable. FS institutions who sell products that do not comply will have to declare their product non-compliant and make it transparent to their customers.

Becoming an ESG promoter may therefore soon become a necessity for European FS institutions. Fortunately, there is plenty of evidence suggesting that ESG investments are often at least as profitable as ordinary ones. AWM start-up Arabesque found that S&P 500 companies in the top quintile for ESG factors outperformed those in the bottom quintile by more than 25 percentage points between 2014 Q1 and 2018 Q2. In addition, those in the top quintile for ESG also had less volatile stock prices.[8]

Financial services companies that have serious internal ESG policies are also often operationally sounder. For instance, a Deutsche Bank study found that companies with high ESG ratings have a lower cost of debt and equity.[9] Following on from this, more and more major institutional investors now expect companies to take a proactive approach to these policies, meaning ESG is critical for securing finance. Morningstar also revealed that companies selected on ESG indices tended to be less volatile and possess stronger competitive advantages and healthier balance sheets than their non-ESG equivalents.[10]

Clearly, ESG-related risk can impact the market value and reputation of a firm. For example, companies with high emissions or those involved in scandals such as pollution spills have seen their profits sink. Millennial employees also care more than ever about their company's values, meaning that internal ESG policies will be important for retaining skilled workers.

As financial services traditional business models come under increased scrutiny and pressure they are nearing the end of their lifecycle. New models are now being developed and entering the ecosystem and sustainable finance has the ability to upend the current paradigm. International institutions have already implemented policies to channel financing towards more sustainable initiatives and a number of institutional investors are already implementing sustainable strategies.

The transition to a sustainable economy will take time and will require a complete overhaul of a number of sectors. While the financial sector has already begun the process, rules and behaviours will need to be formalised to ensure that there is a positive outcome on businesses.

Brexit will lead to a multi-polarised European financial services landscape

Europe's financial industry was, until Brexit, led by London as a truly universal financial centre with a global reach,

8. Arabesque Asset Management
9. Deutsche Bank
10. Morningstar

meaning it offered a full range of financial services to clients not only in the UK or even in Europe, but around the world. Clearly, there have always been several other financial centres in the EU, some large but with a more domestic role such as Frankfurt and Paris, some with a cross-border EU focus but more specialized like Luxembourg and Dublin.

While at the time of writing this report the UK has not yet left the EU - nor is the date or form of Brexit known - it has already been anticipated by the financial industry. Indeed, as financial services are a regulated business requiring a license to operate within the EU, all those institutions that served clients in the EU out of London had to set up alternative operations and thus relocate activities.

These relocations have revealed certain interesting trends and show that Brexit has redistributed the cards for years to come. One feature that emerges very clearly is that activities tend to be relocated to where the local ecosystem is best geared towards supporting a particular activity, in most cases because of preexisting similar activities.

In the banking sector, the bulk of the activities being relocated out of London into the EU is derivatives trading and investment banking for EU clients. Both Frankfurt and Paris emerge as clear choices when it comes to these two activities with the majority of banks choosing either or, as well as for some either and or. These cities were already active trading and investment banking centres, albeit on a smaller scale than London and in most cases for the domestic market..

Dublin also has seen some banks choosing to relocate their EU headquarters there. Luxembourg has seen banks move wealth management activities to the Grand-Duchy.

As regards asset management, the vast majority of firms have chosen to relocate management companies and investment funds as well investment advisory firms to either Luxembourg or Dublin, as these were already well-established cross-border hubs in this particular segment.

Notwithstanding this general trend, some individual firms have also opted for Paris or Frankfurt for their future EU activity in the area of asset management.

Amsterdam has been a very popular choice for a significant number of market infrastructure operators.

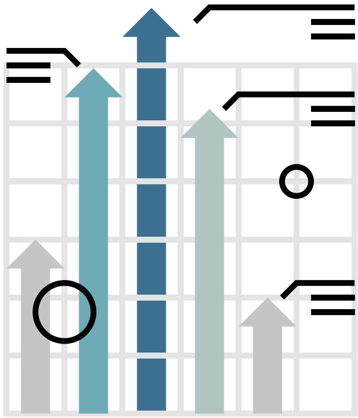
Furthermore, Luxembourg, Dublin and Amsterdam emerge as the future EU payments hubs with many players from this segment choosing one of the three cities to set up their post-Brexit EU hub.

The insurance industry was particularly concentrated in London, around the Lloyd's market. With Brexit, firms have chosen primarily Luxembourg or Dublin as their new post-Brexit EU platforms. However, Lloyd's of London itself has decided to set up its new EU entity in Brussels. Some insurance companies have chosen Paris or Amsterdam.

Overall, the relocations can be simplified as drawing investment banking and trading activities to Frankfurt and Paris, the investment fund industry to Luxembourg and Dublin, the payment industry to Luxembourg, Dublin and Amsterdam, while the insurance industry seems to have opted for Luxembourg and Dublin in most cases. Next to setting up new EU platforms, a number of financial institutions are also reinforcing their presence in the larger EU markets such as Germany, France, Italy and Spain to be able to better serve clients in these markets directly. Finally, some institutions have also relocated activities to other hubs such as Madrid and Milan.

None of these hubs will, in the near to medium-term, be in a position to replace London as Europe's truly universal financial centre with a global reach.

While the industry is of course regretting the ensuing fragmentation of their operations, one can possibly also see a silver lining in this increased multi-polarisation, i.e. an increased specialisation of different financial centres and an increased complementarity between them.



AMAZONISATION WILL PUSH BANKS TO BECOME WHOLE SOLUTION PROVIDERS

Banking systems across the globe have undergone fundamental changes since the financial crisis. This will not only continue, but gain pace in the coming years. Banking's future is currently in flux, but what we do know is that it will be vastly different from today, completely integrated into clients' lives and available 24/7. Enabled by technology, banks will have a light physical footprint and will require an online presence that goes far beyond today. The future for European banks will be modelled on platforms like Amazon. Their success will lie in their ability to organise and analyse the mass of data available to them, using the insights gleamed from that data to improve personalisation and to bring new offerings to the market in response to client demands.

Change is becoming more and more pressing as European banks have been losing their competitive edge globally in comparison to countries such as China and US. China dominates the share of Tier 1 Capital, having not appeared on the ranking ten years ago (see Figure 4).

However, European banks also have a profitability issue. For instance, the magnitude of this problem is demonstrated by the fact that the top five European banks had net profits of only US$17.5 billion in 2017, below JPMorgan's, alone, profit of US$24.4 billion. In addition, the same top 5 banks in Europe have the highest average cost income ratio of the three regions (see Figure 5).

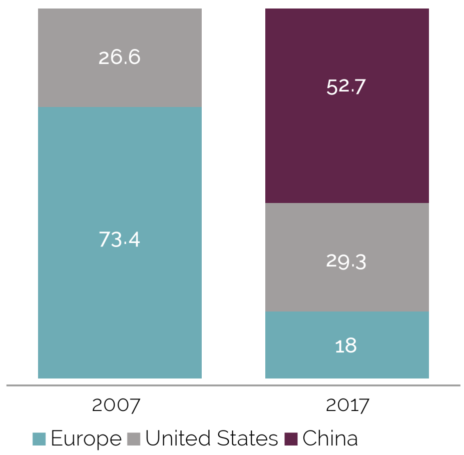
To thrive in the coming years banks need to adopt Amazonisation. This means becoming an aggregator of products, a one-stop shop for clients' banking needs. By focusing on becoming an open banking platform, banks of the future will run a lean, technologically enabled sustainable business model, offering best of breed products, whether their own or third party. This also entails adapting their offering to new products on the commercial side linked to sustainable financing and adapting to market changes that the CMU will bring to beat the profit crunch that they are currently experiencing.

Regulations will facilitate Amazonisation of banking

Regulations, such as the Open Banking initiative, are changing client demand and reshaping the banking landscape. This will lead to a significant evolution of banking business models in the future. New players without legacy operating models and processes are taking advantage of this and entering the market with a state of the art digital presence without branches. They are more transparent in terms of pricing and they realise that data is their most useful asset. In addition, they operate beyond their borders, offering ease of use across Europe, be it to open an account, execute a transaction or view their accounts.

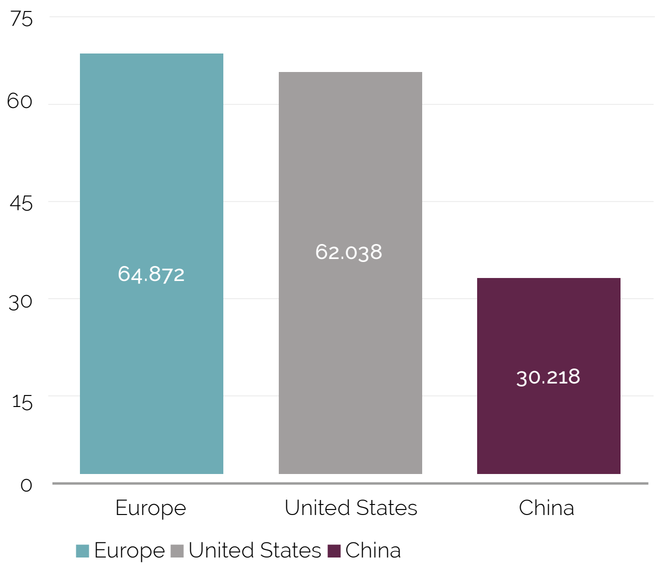
Incumbent players in Europe are struggling with cost inefficiencies and high investment requirements due to the move from legacy systems and competition from challengers coming from outside the traditional banking sector. Traditional banks now face a two-pronged attack on their operations, from digital challenger banks and from FinTech players.

Figure 4: Banks' share of Tier 1 Capital (%)

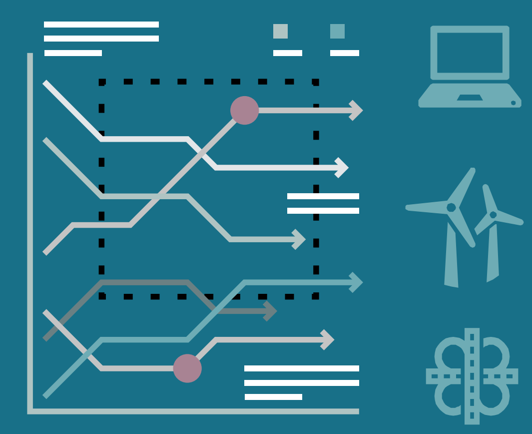


Source: The Banker

Figure 5: Cost income ratios of top 5 banks from each region (%)



Source: The Banker



European banks can no longer maintain their current business models if they wish to survive in the future. Although we believe there will be multiple banking models in the future, in our view, they have only one option available to them if they truly wish to prosper – to become an aggregator-as-a-platform (see Figure 6). This means opening their platforms to third party products, in addition to their own, and becoming a marketplace.

This model will bring new clientele to the bank as they offer new value added services and banks will benefit from being able to truly monetise the mountains of data that they are sitting on. Competition will, however, increase as more banks begin to take on this role. New entrants are already well prepared – they are agile and technologically-enabled, but they do not yet have the requisite scale.

The European Economic Area (EEA) passport has bolstered challenger banks' popularity in Europe and the continued growth of these players speaks to the strength of their value propositions. Traditional banks, often seen as laggards, will need to catch up quickly should they wish to prosper in the long term. They have the data, scale and brand to make the move, but many have yet to do so.

Figure 6: Four options for future banks[11]

Value-added services

Aggregator

Benefits

1. Launch new products and business initiatives
2. Retain and attract client base
3. Collaborate with TPPs

Considerations

1. Operational compliance modifications, investment in development of VAS, integration with TPPs
2. New revenue stream

Aggregator-as-a-Platform

Benefits

1. Acquisition of new client base (not strictly including banking services)
2. Collaborate with TPPs to serve new clientele and drive innovation

Considerations

1. Compliance and IT infrastructure investment
2. Enhance overall digital capabilities
3. Different possible revenue models (fixed charges, etc.)

Compliant Bank

Benefits

1. Fully compliant with the regulations

Considerations

1. Operational compliance modifications (ICT, security, processes)
2. Unvaried revenue model while potentially losing out on additional revenue stream

Bank-as-a-Platform

Benefits

1. Acquisition of new client base who are looking for a provider of technology and digital services, with processing capacity

Considerations

1. Compliance and IT infrastructure modifications
2. Enhance technical and analytical expertise
3. Retain traditional revenue model while offering technology services to competitors

Opening and monetisation of data

11. Compliant Bank: Banks choosing this route opt to invest in compliance of procedures, processes and contracts in order to open up to the market and obtain access to back-office services from third-parties.

Aggregator: Banking players that integrate information and initiate payment transactions on competitors' current accounts. These players opt to create partnerships with third parties, which may reduce development and innovation costs and improve "go-to-market".

Bank-as-a-Platform: Banking players investing in IT infrastructure and security to provide a compliant environment which benefits from network effects and economies of scale.

Aggregator-as-a-Platform: Banking players handling large volumes, have substantial cross-sector customer base, take advantage of their capacity of process and investments in technology and marketing.

As a result, many banks have begun to partner with FinTechs in recent years. However, as competition and rising costs begin to erode margins, we expect this trend to accelerate further. Whether traditional banks maintain digital pace through internal means or through acquisition, it is clear that they will struggle to survive without change.

Sustainable finance as a foundation for future success

On February 15th 2019, thousands of European students walked out of school to protest a lack of action and to demand measures for climate change. This socially conscious generation will soon be consumers of financial services and it is reasonable to assume that they will demand sustainable products. Additionally, with US$201.8 billion of additional investments required annually to achieve the EU's 2030 targets, including a 40% cut in greenhouse gas emissions, there is plenty of reason to expect sustainable finance to bulge in the coming years. Banks will have a major role to play in closing the green financing gap.

The current lack of a green financing is arguably due to a lack of a common classification system. However, with ISO/AWI 14097[12] under development, there will soon be a framework that banks can use to assess the potential impact of financing activities on climate change. Once implemented, the standard will provide some much-needed clarity to financial institutions as to how they can contribute to sustainable financing.

While many banks have already taken steps to reduce their direct impact on the environment, their largest contribution will arguably lie in providing support and financing for green projects and companies. For example, banks are beginning to offer sustainability-linked loans and positive impact loans, where high sustainable performance achieved by the borrower is rewarded with discounts.

Commercial banks have helped to fuel the growth of green bonds, with their total issuance in 2018 almost doubling the previous year's total, making them the largest issuers among financial institutions. There are also other types of labelled bonds that are looking to promote sustainability, with frameworks being introduced in 2018 to help distinguish between green and blue bonds, social bonds and sustainable bonds. The latter two, for example, raised US$14.2 billion and US$21 billion respectively in 2018.[13]

Looking to the future, central banks and other financial lawmakers could play a pivotal role in establishing sustainable finance as a norm. Central banks and other organisations recently released a report that makes recommendations to financial regulators regarding how they should implement and monitor green financing.[14] An effective implementation of new sustainable financing rules would be a major step towards making sustainable finance a norm among financial institutions.

However, despite the efforts of central banks and other organisations to promote sustainable financing, the true responsibility lies with individual banks around Europe to generate support for this activity. An example of how this can be done is the formation of the Principles for Responsible Banking, where 28 leading banks from across the globe, representing more than US$17 trillion in assets, have come together through the UNEP FI.[15] Here, participating banks are obliged to set goals and publicly report their progress in alignment with the UN's SDGs and the Paris Climate Agreement.

European banks must follow the example set by the EIB, which launched its first Sustainability Awareness Bond last year, and by the European Commission, which recently published new guidelines for reporting climate impacts as part of its "Action Plan on Sustainable Finance." These guidelines illustrate the EU's forward-looking attitude and may act as a precedent for sustainable finance reforms globally.

12. ISO/AWI 14097 - Framework and principles for assessing and reporting investments and financing activities related to climate change

13. Climate Bonds Initiative

14. Bloomberg, With climate losses rising, central banks push greener finance, April 2019

15. United Nations Environment Programme Finance Initiative

Given that global sustainable bond issuance more than quadrupled between 2015 and 2018, it seems likely that the sustainable financing will continue its upsurge in the coming years.[16] European banks are well positioned to take advantage of this opportunity, however they must remain proactive in their stance if they are to become a global leader in the sustainable finance realm.

Moving towards a sustainable business model

European banks are facing a profit crunch. Their current business models are often outdated and rely too heavily on traditional bank loans to drive profits. In the current low interest rate environment, this has put severe strain on their profits. As interest rates are not expected to rise significantly in the medium term and market fragmentation is hampering cross-border loan growth (see Figure 7), banks in Europe must move towards a sustainable business model.

This outcome is made even more likely with the impending Basel IV regulation, which will raise capital requirements and therefore reduce banks' profit-making capabilities from traditional loans. The EBA recently noted that "the full implementation of Basel [...] increases the weighted minimum capital requirement (MCR) by 24.4%, leading to an aggregate capital shortfall of EUR135.1 billion."[17] In light of this, banks will need to look to other forms of financing.

Ultimately, in terms of public market-based financing, the CMU will be one of the key factors determining the success of Europe in the future. Specifically designed to build a more resilient and efficient financial system, the CMU will ultimately provide SMEs with better access to finance through a revitalized securitisation market. It's critical then that European banks bolster their public market financing, i.e. debt securities and equity financing. In this space, it's very clear that Europe has fallen behind (see Figure 8).

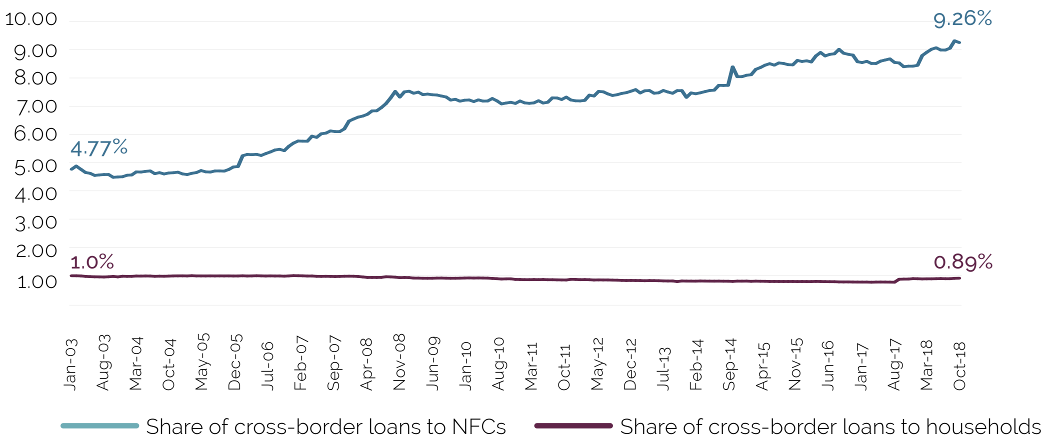
If banks do not move into the space, our forecast for debt securities' outlook remains moderate up to 2025, largely due to faltering issuance activity, the CMU delay, a more conservative economic environment and the fact that SMEs are mostly excluded from public market-based finance. However, should European banks become more active in public market financing, it could grow at a far higher rate. Equity financing has a far rosier outlook, with the positive momentum seen in 2017 to continue up to 2025. Doubts remain in this space as well, with tax treatments incentivising debt, unwillingness to issue equity and dilute ownership and Brexit all contributing.

Basel IV[18], Open Banking initiative[19], PSD2[20] and the CMU[21] will increase pressure on traditional banks. Alongside this, the rise of new, more transparent entrants with cheaper pricing models and ease of use through technology will pose an increasing threat to incumbents. This becomes all the more apparent as the workforce shifts towards millennials and Generation Z and they become banks' dominant customers.

In order to relaunch European competitiveness banks must become open architecture whole solution providers, become more cost effective and customer centric. They will need to fill Europe's finance gap, offer new types of products, and look to integrate alternative sources of finance and sustainable finance products into their selection. European banks must be able to thrive on low margins, which will require them to make their costs as variable as possible and reduce deadweight. Ultimately, banks will need to adopt an Amazon-like approach.

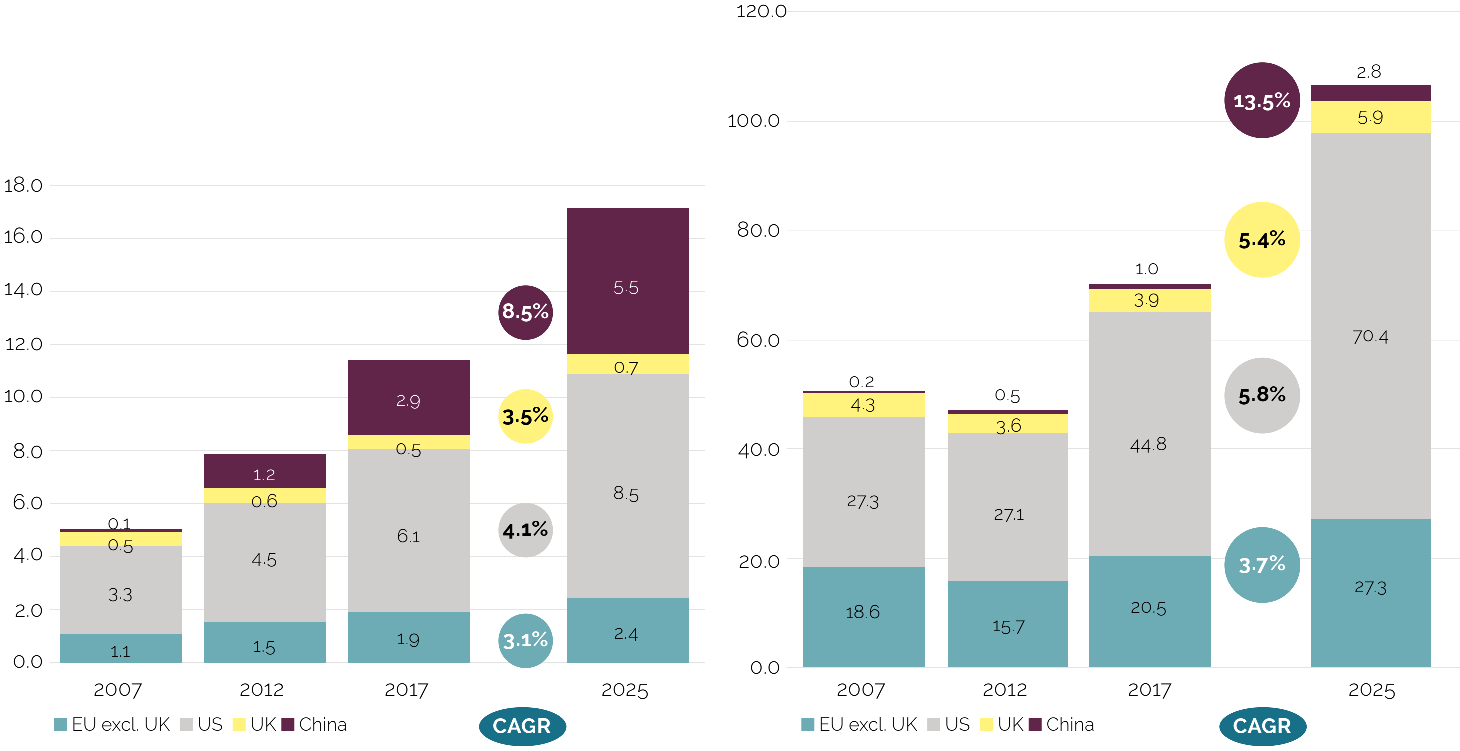
16. Bloomberg, Sustainable Debt Market Sees Record Activity in 2018, January 2019
17. EBA, Basel assessment sees impact driven by large banks, July 2019
18. Basel IV: A reform of Basel III regarding international banking standards, created to reduce the risk of a financial crisis. Aimed to be introduced in 2022, it limits capital reduction, introduces a standardised floor and higher leverage ratios for banks affiliated with the BCBS.
19. Open Banking Initiative: This defines how financial data should be created, shared and accessed. The goal of the initiative is to improve banking services by enabling third parties to access banking consumers' data, with their consent, through the use of application programming interfaces (APIs).
20. PSD2: "The revised Payment Services Directive (PSD2) entered into force in the European Union in January 2018. By law, banks must make customer data available in a secure manner and, where applicable, grant third parties access to their customers' accounts. The revised directive encourages the use of innovative digital tools and at the same time regulates service and payments practices in place."
21. CMU: The Capital Markets Union, developed by the European Commission, aims to mobilise capital in Europe by creating a true single market for capital in the region. The CMU aims to develop a diversified financial system, which complements bank financing by unlocking capital in Europe and creating a genuine capital market where investors can take advantage of the region irrespective of location.

Figure 7: Share of cross-border loans, % of outstanding amounts



Source: Deutsche Bank and ECB

Figure 8: NFCs' debt securities (L) and equity financing (R) liabilities, USD trillion



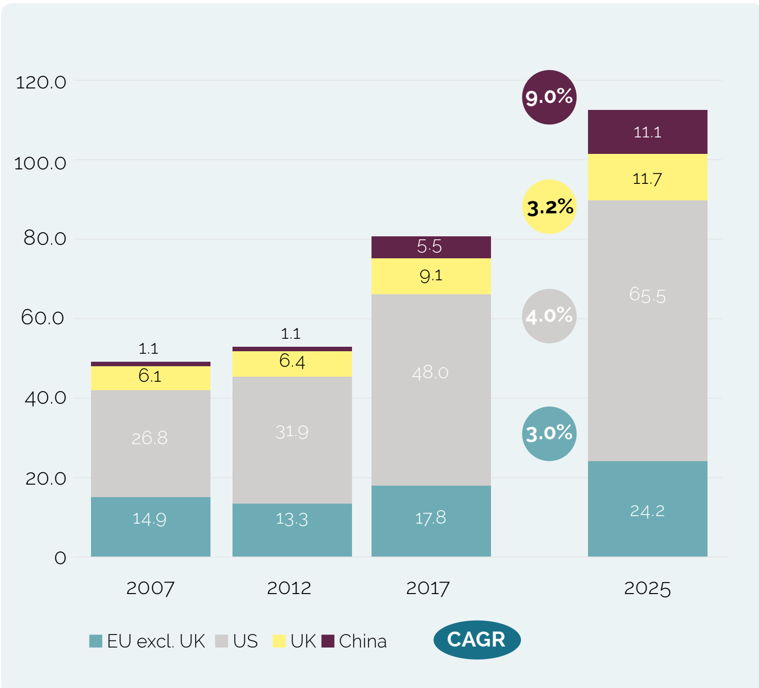
Source: PwC Market Research Centre analysis based on BIS, ECB, National Central Banks, EIB, VoxEu and Reuters

AMAZONISATION OF AWM IS A BLESSING AND A CURSE

The future of how retail funds will be bought, in our view, is platforms. Either clients will buy funds through standalone platforms or through independent financial advisors, who will use B2B platforms to purchase funds on behalf of their clients. These platforms will benefit from significant technological developments and will offer various comparisons based on KPIs and other client recommendations, echoing the likes of Amazon and Expedia. This trend will drive assets to the best-in-class product providers, offering real value for money and making them successful. At the same time, those asset managers who will not be able to provide a unique value proposition will find it difficult to have a long term sustainable business model.

Despite the sustained bull market, we believe there is still room for significant growth in the AWM industry, however this growth is set to slow (see Figure 9) and margins are set to fall. In order to survive in the coming years, managers must embrace efficiency to the maximum, becoming disruptors themselves and adopting an Amazon-like mindset.

Figure 9: AuM evolution by region, US$ trillion



Source: PwC Market Research Centre analysis. Past data based on EFAMA, ICI, AMAC and Foreign Policy

Margins set to fall

The AWM industry is at a crossroads. With compliance costs rising and management fees set to drop, serious pressure is being put on fund managers' margins. This is forcing many asset managers to reassess their operating strategies. We believe Amazonisation is the answer to these struggles, with managers having to provide the best value for money independent of product provider, adapt to ongoing market trends and focus on evolving client needs.

With regulators cautious in the wake of the GFC, regulations such as MiFID II have been passed that seek to protect investors and provide them with more transparency. At the same time, management fees have simultaneously been on a downward trend. While Europe is expected to see the slowest asset growth in percentage terms, it will see the highest fall in fees for both passives and actives (see Figure 10) up to 2025. While much of this can be attributed to fee transparency brought about by MiFID II, changing client preferences (i.e. the shift to best value for money products) will also be a significant driver.

Passive managers are facing extreme fee pressure as the fee war heats up in Europe, with some players in the industry slashing their fees to zero or introducing ETF platforms with no transaction fees. These low fees, as well as the performance of some active managers, has seen a significant number of investors shift to passive. This has also put strain on active managers' fees and, as a result, active players will see a 19.3% decline by 2025, but this drop in fees will vary across regions. The US, where fees are already at lowest levels, will witness a 13.5% fall, whereas Europe's will face nearly double of that (26%) by 2025.

Figure 10: Management fees set to fall across the globe

	2012	2013	2014	2015	2016	2017	2025	% 12-17	%17-25
Active + Passive	**0.52**	**0.51**	**0.49**	**0.47**	**0.45**	**0.44**	**0.36**	**-14.3%**	**-19.4%**
Active	**0.59**	**0.58**	**0.57**	**0.55**	**0.54**	**0.54**	**0.44**	**-8.6%**	**-19.3%**
US	0.48	0.45	0.45	0.44	0.43	0.43	0.38	-9.5%	-13.5%
Europe	0.82	0.85	0.82	0.80	0.78	0.78	0.58	-4.9%	-26.0%
Asia Pacific	0.88	0.90	0.78	0.63	0.60	0.58	0.43	-34.6%	-24.6%
RoW	0.83	0.84	0.82	0.79	0.78	0.72	0.62	-12.8%	-14.5%
Passive (MF + ETFs)	**0.20**	**0.19**	**0.18**	**0.17**	**0.16**	**0.15**	**0.12**	**-25.7%**	**-20.7%**
US	0.18	0.17	0.16	0.16	0.14	0.13	0.11	-26.4%	-16.9%
Europe	0.27	0.26	0.25	0.24	0.23	0.23	0.15	-13.2%	-34.9%
Asia Pacific	0.55	0.52	0.56	0.56	0.52	0.45	0.30	-17.8%	-32.1%
RoW	0.33	0.31	0.31	0.29	0.30	0.32	0.25	-3.6%	-22.1%

Source: PwC Market Research Centre analysis. Past data based on Lipper and Morningstar.
Note: Management fees are measured as end of year AuM-weighted average. These figures include both retail and institutional share classes of mutual funds and ETFs. Percentage changes may not correspond due to decimal approximation.

On the institutional asset management side, we believe alternatives are set to shine. Institutional investors have developed an appetite for these mostly illiquid investments not only because of low interest rates and high equity market valuations making both sovereign bonds and equity markets less attractive, but also the benefits that alternatives offer, such as higher returns, illiquidity premium, diversification and low correlation to other assets. However, alternative asset managers will also face dropping fees as investors become more critical of aligning their interests with those of asset managers (see Figure 11).

With falling operating margins, managers will need to do as much as possible to make their costs variable. At the same time, in order to capture the new generation of investors, they will need to be adaptable to new demands and operating models. With the coming rise of fund platforms that will mimic the model of Amazonisation, funds will soon be comparable through set KPIs, independent assessment agencies (e.g. Morningstar) and comments of clients who bought the product. With this extended transparency, there will be pressure on fund managers to provide products that are most relevant and fair to the needs of investors.

Fund platforms have massive potential in this space, with managers and third party providers set to do battle as they look to establish themselves as the Expedia for AWM. In order to compete with third party providers, asset managers will have to offer both their own and other third party products in order to provide a marketplace which offers a wide enough coverage of products.

In order to achieve this, we recommend that Asset & Wealth Managers consider three points:

1. **Focus on digital decision making in order to allow investment professionals to gain a competitive advantage:** This requires connecting new data points with each other, implementing visualisation tools to improve the analysis of the data and facilitate better decision making, and finally optimising investments by creating actionable insights from the data.

2. **Implement cost-reducing technologies in the middle and back office that will optimise operational performance:** Multiple options exist for managers in this space, from taking advantage of new low-cost outsourcing providers, to create a standardised operating model that will drive down costs and operational risk. This should also create the flexibility required for future innovation to be less cumbersome.

3. **Transform the client relationship process, which will provide bottom-line benefits to both the client and asset manager:** The creation of digital channels in sales and distribution will allow for smoother client interaction, immediate access and lower costs. This should also further the spread of the direct-to-consumer model across the AWM space.

Figure 11: Global Alternative Fees (%)

Source: PwC Global AWM Research Centre analysis based on Preqin and HFR.
Note: Percentage changes may not correspond due to decimal approximation

Providing solutions to challenges for the European economy

In addition to integrating Amazonisation, we believe it is crucial for European asset managers to address the challenges facing society in order to revive the somewhat damaged image of financial services companies during and post-GFC. Through positive action, European fund managers can demonstrate to policymakers and the public that they can provide real value to society, while at the same time leveraging these opportunities to regain their position globally. With banks' lending capacity insufficient, AWM firms will have a key role to play in closing both the pension and infrastructure gaps, along with financing Europe's SMEs. AWM firms cannot afford to keep their operations compartmentalised.

Europe is facing a pension bomb with its ageing populations, higher life expectancies and low birth rates. The current pay-as-you-go system of European countries will not be sustainable unless major changes are implemented. Old age dependencies are going to rise significantly in Europe, even in comparison to other regions across the globe who will experience similar problems (see Figure 12).

With growing strain on financing pension schemes, we have seen Germany raise their retirement age and offer tax incentives to individuals who invest in their pensions themselves (in addition to their organisation's pension schemes). Meanwhile, in the US, 401(K) plans have proven to be a popular option for saving. In fact, assets held in these plans stood at US$3.7 trillion at the end of March 2019, just under a fifth of total US mutual fund assets.[22]

With the US' success in this field, there are questions over whether a 'European 401(K)' could succeed. The European Commission and EIOPA have been pushing for the formation of a Pan-European Personal Pension Product (PEPP), a scheme that would give EU citizens access to personal retirement plans that can be used to save into a single retirement savings vehicle on a cross-border basis. From an AWM point of view, this would surely provide a large boost, with capital previously allocated to life insurance flowing into European asset managers. However, asset managers will have to provide suitable and easy to understand products for future pensioners. With an ageing population that will live far longer than previous generations, asset managers should enhance their target client range to persons of 65+ and provide products suitable to this group of clientele.

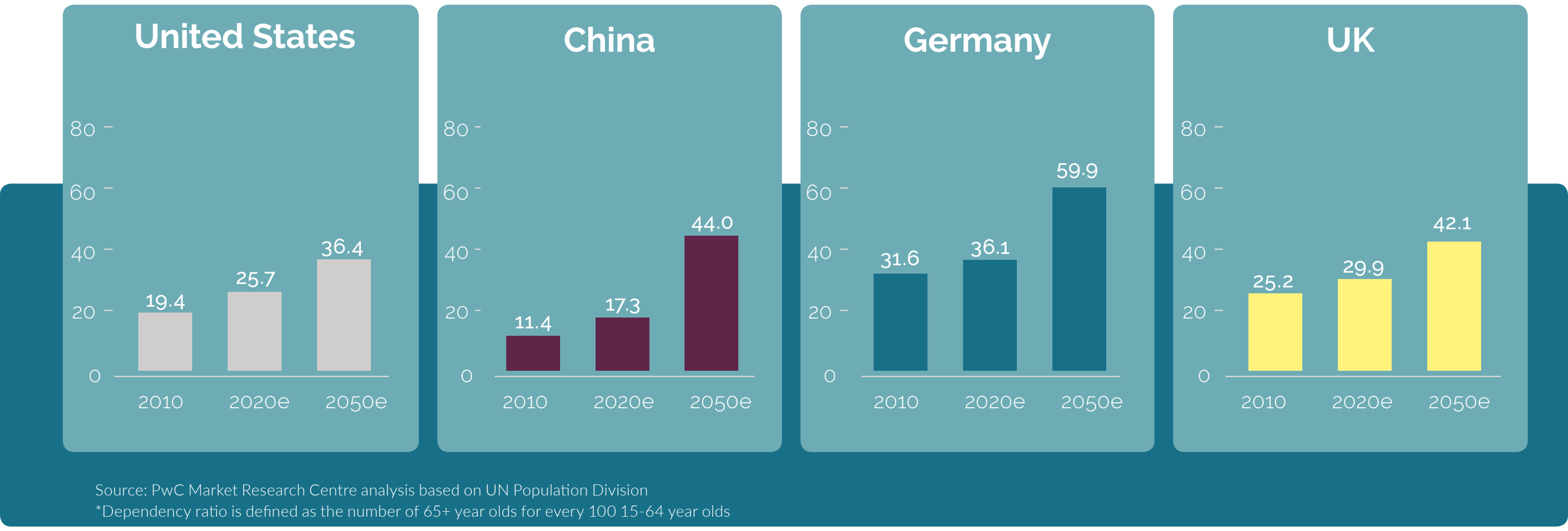
Another investment gap in desperate need of filling is infrastructure. Again, European asset managers have a vital role to play in financing this gap. European AWMs should look both internally and externally in terms of infrastructure. Externally, there is a vast need for funding of greenfield projects in emerging economies that offer attractive returns, while internally managers can look towards both infrastructure renewal and funding of sustainable infrastructure projects.

Fund managers could also look towards high value-add and innovative companies, which often struggle to access traditional financing channels. A well-developed private market, however would give financial systems an edge up on diversification, enhancing resilience and efficiency.

In light of this, venture capital (VC) financing has finally reached pre-crisis levels in Europe. A well-developed VC market is critical for high-potential start-ups to have the necessary means to succeed and bring their innovations to the economy. The US and China will, by 2025, have an edge up on Europe, which could mean that the competitiveness gap of European companies with North American and Asian ones may widen due to insufficient private financing. However, should European AWMs become more active in this space, we believe this growth could expand faster than expected.

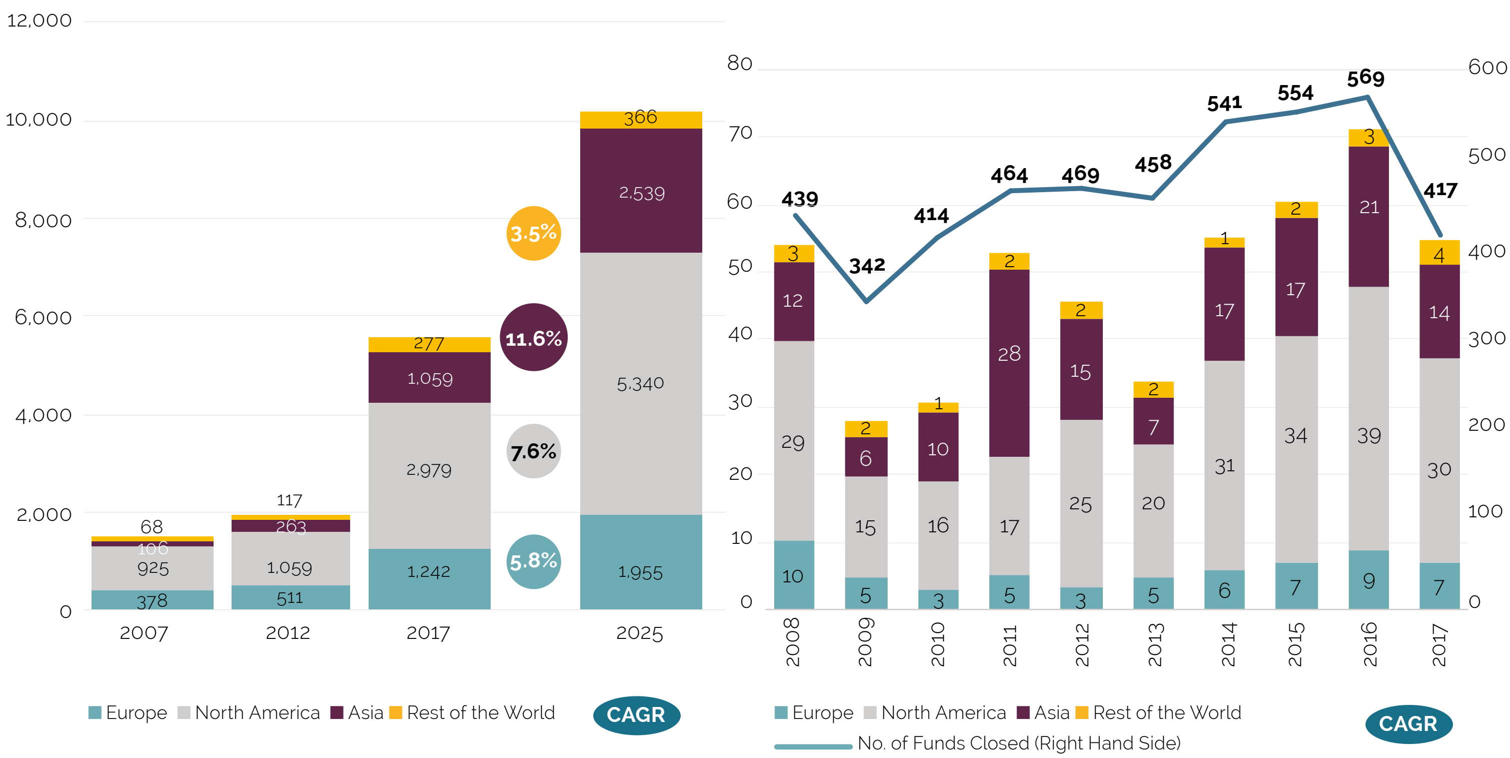
22. Investment Company Institute

Figure 12: Old-age dependency ratios*



Source: PwC Market Research Centre analysis based on UN Population Division
*Dependency ratio is defined as the number of 65+ year olds for every 100 15-64 year olds

Figure 13: PE AuM evolution by region (L) and Annual VC fundraising by geographic focus and funds closed (R), US$ billion

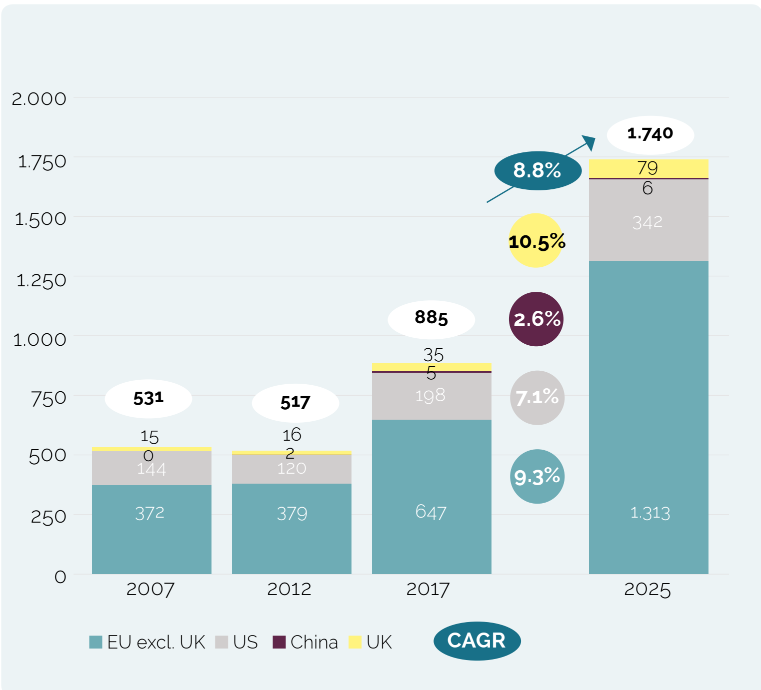


Source: PwC Market Research Centre based on Preqin, EIB, EIF and OECD

If AWM firms are not able to harness these opportunities, alternative sources of financing may take up the space. ICOs, for example, can take different forms including a security, utility token or digital currency. However, still largely unregulated to date, ICOs seem to be at somewhat of a crossroads. Start-ups raising capital via ICOs brought in just over US$118 million in Q1 2019, compared to US$6.9 billion in the same period in 2018.[23] Given the unregulated nature of ICOs, their future will largely depend on legislation, which could help protect investors by reducing both misleading information and fraudulent behaviour.[24]

ICOs have potential in funding SMEs and innovative start-ups; they can catalyse the use of technology and hence can be recognised as an essential part of the CMU.[25]

Figure 14: Global ESG funds AuM, US$ billion



Source: PwC Market Research Centre analysis based on Lipper data

Meanwhile, certain asset managers are even beginning to offer crypto funds, with some regarding it as a new, risky asset class.

Along the same vein as ICOs, crowdfunding has fast emerged as an alternative source of financing for start-ups and SMEs, with the market expected to grow to US$300 billion by 2025.[26] However, this form of financing can also be risky, with a high proportion of P2P loans having defaulted. The European Commission (EC) submitted a legislative proposal to the European Parliament in March last year[27], which could greatly reduce the risk attached to crowdfunding as a method of financing. The proposed rules dictate that companies would have to give investors clear information about their insolvency risk. This could be a major step towards being able to compete with the US and China.

With concepts such as ICOs and crowdfunding coming to the fore, it is possible that we will see a tokenisation of the AWM industry. In this future, investors would be able to buy tokens which represent a fractional share in a given project, such as the building of a new road. This would enable the "retailisation" of previously unattainable assets for smaller scale investors. Investors would then be able to buy and sell these tokens on secondary markets, providing them with liquidity and choice.

23. Financial Times
24. PwC, 4th ICO / STO Report, 2019
25. European Parliament, Report on the proposal for a regulation of the European Parliament and of the Council on European Crowdfunding Service Providers (ECSP) for Business, November 2018
26. Fundly
27. European Commission

Financing gaps represent significant opportunities for AWM, although European fund managers must be proactive if they are to take advantage of these opportunities. Following the spirit of Amazonisation, European fund managers should look to harness these ongoing market trends.

Europe leads the burgeoning sustainable investment race

A new generation of investors are far more aware of the impact their investments will make. According to a Morgan Stanley study, "millennials are twice as likely to invest in a stock or a fund if social responsibility is part of the value-creation thesis".[28] There is a fundamental change occurring and, in the same vein as how Amazon became famed for its client-centricity, the investment industry will need to evolve to answer its clients' demand for sustainability.

We believe that in the future, as a general rule, all funds will need to be ESG compliant and will have to label themselves as non-compliant if this is not the case. We are seeing this trend being pushed by investors and regulators alike. For instance, the Norwegian SWF, which manages US$1 trillion in assets, announced in March that it is seeking to divest from firms that explore for oil and gas.

We believe Europe will emerge as a leader in this space, with the region set to experience the most important growth of all advanced economies, reaching a projected US$1.3 trillion in 2025 (see Figure 14). While the UK holds the highest projected CAGR for this period, this is due to its significantly lower base AuM in 2017. Part of the EU's success comes from EU legislation, which is encouraging a move to sustainable investment that could eventually make ESG-investing the default approach for fund managers. For instance, the EU's March 2018 Action Plan seeks to promote low-carbon, sustainable investments within the financial sector. Through this plan, a number of regulations will be put into force by late 2020.

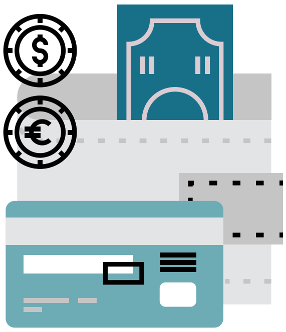
In June 2019, the Technical Expert Group (TEG) on sustainable finance, set up by the European Commission, published reports detailing an EU taxonomy for ESG investment, disclosure requirements and standards for green bonds and other labelled products. A primary factor behind the publication of these frameworks and criteria is the desire to prevent "green-washing", where companies or financial products are advertised as being green despite the fact that they do little to promote ESG ideals.

On a practical level, these rules will make it mandatory for asset managers based in the EU to release detailed information concerning both their ESG investments and the potential negative ESG impact of their other investments. It is hoped that ESG investment will therefore become the default approach for European asset managers, a shift which would further propel the growth of Europe's burgeoning ESG investment industry.

While the UK's low ESG AuM is attributable to its overall fund industry trailing other advanced economies, China's ESG industry has simply never taken its feet off the ground despite its overall fund industry seeing significant growth since 2007. China is set to register the lowest CAGR (2.6%) between 2017 and 2025, even though it also holds a miniscule base in comparison to the other economies. While the US has been successful in developing a strong level of ESG AuM, the SEC's lack of a clear vision has stunted growth somewhat.

With strong momentum behind ESG and sustainable investment, Europe is strongly positioned to capitalise on this opportunity and gain an advantage over its regional rivals. However, AWM firms must be proactive in developing ESG products, not only to meet demand but to create an awareness and further demand for these products.

28. Morgan Stanley



AMAZONISATION OF PAYMENTS SET TO LEAD CHARGE TOWARDS CASHLESS SOCIETIES

The rise of ecommerce and mobile payments, driven by their convenience and by millennials becoming a dominant consumer demographic, will cause digital payments to spike. Global e-retail sales are expected to grow to US$4.8 trillion by 2021, more than double the value of 2017's total.[29] Meanwhile, for physical transactions, mobile payments also represent a significant threat to the future of cash and physical card usage.

As a result, we are seeing more countries transition towards becoming cashless (although none have reached true 'cashlessness' yet). This trend has led to a number of technology players entering the payments market, with Google Pay, Alipay and Apple Pay prime examples. The Amazonisation of the payments market is well underway, with clients able to choose their favourite payment method at the POS, be it physical or digital.

We believe that in the future, as this Amazonisation accelerates, intelligent apps will provide consumers with recommendations as to which method of payment to use in order to reap the biggest advantage. Hence, the EU must remain proactive in its approach, encouraging the implementation of payments infrastructure and regulation to help further develop a multi payment environment increasing competition and benefitting the consumer.

Mobile set to revolutionise physical POS payments

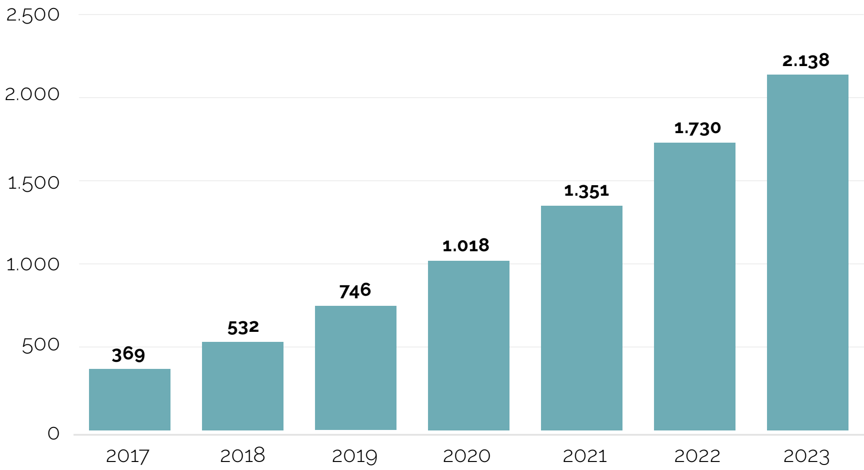
With over half of the world's population being mobile internet users as of January 2019[30] and an estimated 20.8 billion connected devices online by 2020[31], the payments landscape is set to change dramatically in the coming years. Consumers are no longer limited to cards or cash at the physical POS, with mobile payments promoting a move towards a pre-dominantly cashless society. We expect to see a large portion of the industry's innovation to arise at the physical POS, with the focus primarily on becoming more client-centric.

Global mobile POS payments transaction value is anticipated to reach approximately US$2.14 trillion in 2023, growing at a CAGR of 32% from 2018 (see Figure 15). On a global level, China is currently surging ahead, with projections indicating that the country will witness a whopping US$1.62 trillion worth of overall mobile transactions in 2023.[32] A significant driver behind this growth is the continued expansion of Chinese mobile payments giants Alipay and WeChat Pay, which each claim to have over a billion active monthly users.[33] Apple Pay, one of the largest players in the US, has just 383 million in comparison.[34]

Europe and the US have been somewhat left behind when it comes to the adoption of mobile payment systems. This could be partly due to the ageing payments infrastructure in these

29. eMarketer
30. Statista, We are social, DataReportal, Hootsuite
31. Visa
32. Statista, Digital Market Outlook
33. Company Websites
34. Loup Ventures

Figure 15: Global Mobile POS Payments Transaction Value, US$ billion



Source: Statista, Digital Market Outlook

advanced economies. In economies that have developed more recently, modern payment facilities and mobile payments have gained significant traction. Regardless, with transaction value set to surge, mobile POS payments are set to be in the vanguard of the charge towards cashless societies and the gradual expulsion of cash and card POS payments.

We believe that the future of mobile POS payments will be characterised by choice. For instance, when checking out at a brick and mortar store, we believe that customers will have the ability to choose from a far wider variety of payment service providers (PSPs), with each PSP fulfilling different client preferences and offering different incentives and rewards through partnerships for repeated usage of their service.

Intelligent applications, which can analyse client purchasing behaviour, will look to pinpoint the best choice of PSP for each individual consumer and maximise the value of each transaction. In the case where a customer consistently purchases clothing, intelligent applications will review this historical data and select PSPs that reward their clients with incentives and discounts in clothing shops..

This Amazonisation of payments requires current players to have a clear strategy that promotes client centricity if they are to succeed. European players will have to develop a strong value proposition, providing strong incentives to ensure that their service is used at the POS. A data-driven business model will be vital in ensuring that PSPs can harness purchasing behaviour and therefore offer the most suitable incentives. Players that have scale will hold an advantage over smaller players as they will have access to more data and will be more capable of adapting to lower costs in the competitive and innovative environment.

As legacy infrastructure in more developed regions evolves, we expect to see a faster pickup of mobile payments. In Europe, the EU and national governments have a major role to play, with facilitating the spread of mobile payments infrastructure set to be a vital step towards growth. European PSPs must ensure that they are at the forefront of this shift, implementing new technologies in order to expedite the process.

Money transfers will become instantaneous

Within the money transfer realm, we expect to see a definitive fragmentation of the market, with peer-to-peer payment platforms and innovative challenger PSPs set to do battle with banks, the traditional money transfer service providers. These new kids on the block will look to leverage their ability to process fast and cheap money transfers around the globe, exploiting the inefficiencies of the current money transfer system.

For instance, many current money transfer players charge high costs and have needlessly long settlement periods, especially in cases where money is being transferred between countries and regions. We believe that the future with Amazonisation will see the emergence of platforms, where clients can find the most suitable money transfer option available to them.

In this space, where competition is becoming more and more fierce, successful players will need to provide high value propositions. This will likely come in the form of faster settlement speeds, lower costs, stronger security and more transparency for challenger PSPs, meaning existing players with legacy systems will need to adapt. These types of players will therefore have to make a choice between upgrading their systems or partnering with newer players. Partnerships would represent a win-win relationship, where traditional players can take advantage of newer technology and new players can access a far larger client base.

Meanwhile, as clients request more and more convenience, payments are now being offered in real time. Payments players will need to be prepared to plug into real-time systems in order to meet this demand. Across the globe, we have already seen a number of countries adopt real-time payments, with many more in the beginning phase of implementation. The redesign and upgrading of payments infrastructure is allowing for innovation to take place in markets around the world. Clients are demanding seamless payments and players in this space are well on their way to providing it.

Overall, Europe's payments sector is in a strong position to confront the industry's ongoing trends. Players must continue to hold a proactive stance, ready to adapt to future changes by promoting innovation and encouraging the use of modern technologies such as mobile real-time payments.

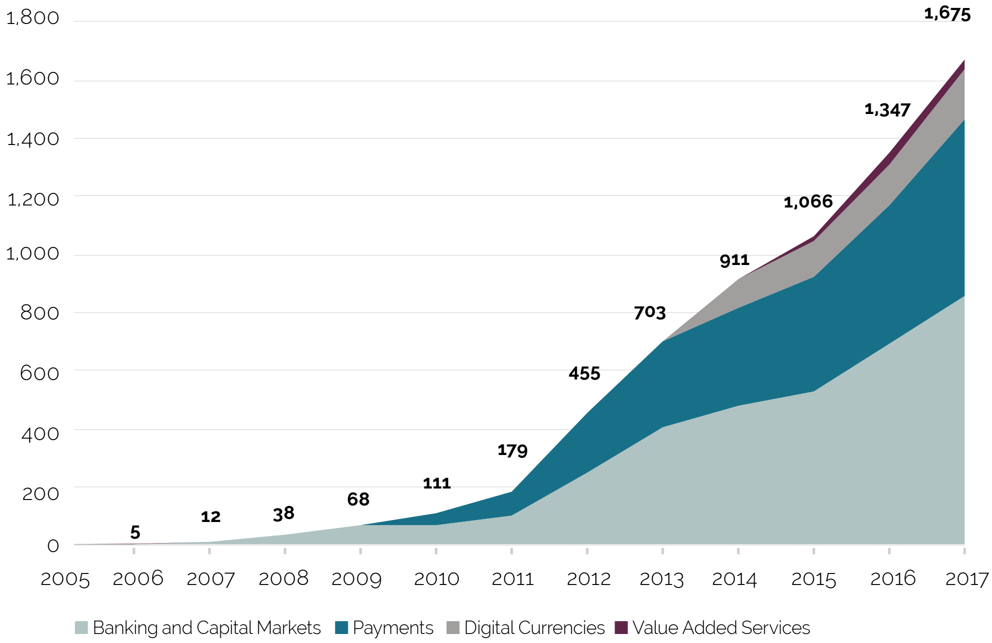
Payment regulations will support Amazonisation in Europe

Overall, we believe that the European market will see healthy growth up to 2025, but will remain in second place. It is dwarfed only by China's massive payments boom where payment volumes increased more than six-fold between 2007 and 2017. Due to demographic trends (an estimated population of 1.4 billion people by 2025), the development of payments infrastructure and a growing middle class, China's boom is set to continue in the coming years (see Figure 16).

Figure 16: Transaction values by geography, USD trillion

Source: PwC Market Research Centre analysis based on BIS, ECB and National Central Banks

Figure 17: Evolution of APIs related to financial services



Source: Programmable Web, Celent analysis, Cognizant, Raconteur

Behind China, Europe will lead advanced economies, boosted by regulation, creation of real time payments infrastructure through TARGET Instant Payment Settlement (TIPS) and ECB efforts to strengthen the Eurosystem's market infrastructure for payment and settlement services. In the US, growth will be positive due to strong economic activity and inflation levels remaining relatively stable. While the UK will see a small positive growth, 2.1% CAGR between 2017 and 2025, this is largely linked to Brexit and a smooth transition. Should the UK be excluded from the EU's payments infrastructure, growth is likely to be revised downwards.

The PSD2 framework has been key to the success of the European payments landscape in recent years. Increased competition has given rise to the development of new products and services, as banks alter their service offerings to retain existing clients and gain new ones. Moreover, with new entrants not required to bear heavy infrastructure burdens in order to comply with regulations, the payments space is easy to disrupt.

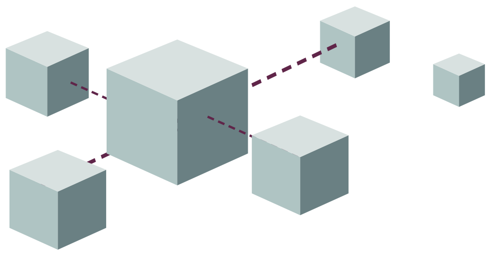
The initiatives in this space have led to the adoption of an API[35] economy (see Figure 17); FinTech companies in Europe are able to build upon existing bank services to provide better products and services, enhance customer experience and make intuitive recommendations using the mountains of consumer data that are available. Consequently, existing banks are having to upend their business strategies and operating models to work with FinTechs under this framework.

It is not just FinTech companies and traditional banks that are changing the payments landscape, however. Telecommunications companies, social networks, global card networks and online retailers are all playing a role. For instance, Facebook's Libra, a proposal for a new virtual currency, is threatening to disrupt the payments landscape.

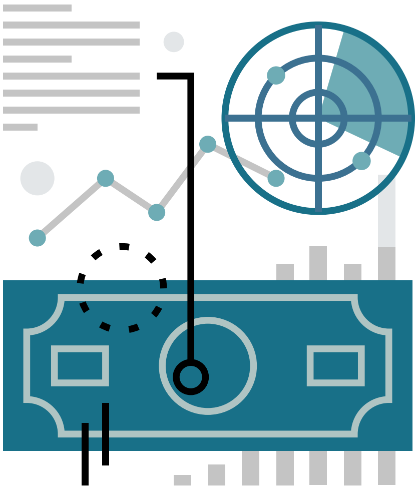
In preparation for this, Facebook has set up a subsidiary payments service, named Calibra. If the Libra project proceeds, the Calibra service would be embedded into Facebook's messenger app, enabling Facebook's 2.4 billion users to conduct purchases and transfer money in a fast and simple manner. Given Facebook's large client base and with Calibra having already partnered with existing PSPs Visa, Mastercard and Paypal, along with companies such as Spotify, Uber and eBay, the Libra project has the potential to push cryptocurrencies into the mainstream just as Bitcoin attempted to do.

However, response to the announcement has been mixed at best, with many in the industry issuing stark warnings about the proposal. Some worry that Libra could cultivate the formation of an oligopoly, where just a few large tech companies hold massive sway over the FS industry. Others point to Facebook's withering credibility and have stressed the potential danger in giving the largely distrusted social media new, rich sources of data. Finally, and perhaps most significantly for regulators, Libra would be unaffected by monetary policy, potentially erasing the ability of central banks to monitor and control financial systems.

The ball is now in the regulators' park. Given the potential disruptive effects and systemic risk attached to the project, it is expected that Libra will be under the microscope and held to high levels of scrutiny before ever being allowed to proceed. Regardless, there is clearly an ongoing shift in the industry towards digitisation. Incumbent players who do not adapt and introduce cutting edge technologies will begin to fall behind.



35. API (Application Programming Interface) - A set of functions, procedures and commands that allow developers to access the features or data of another operating system, application, or service.



AMAZONISATION WILL DISRUPT THE INSURANCE DISTRIBUTION VALUE CHAIN IN THE NEAR TERM

We believe the Amazonisation of the insurance industry will be driven by online platforms providing access to a marketplace where clients can immediately compare and evaluate insurance offerings from multiple providers. Technology players moving into this space will further strengthen the trend. This Amazonisation will disrupt the traditional value chain of insurance products, predominantly through tied agents, especially for standardised retail insurance products.

With premium growth slowing and compliance costs rising over the last decade, Europe's insurance sector is crying out for innovation. The industry is ripe for disruption and players who embrace Amazonisation will benefit in the coming years. Integrating new products and technologies, while facilitating the evolution of the traditional operating model in order to better serve clients, would enable European insurance to regain the momentum it lost during the GFC.

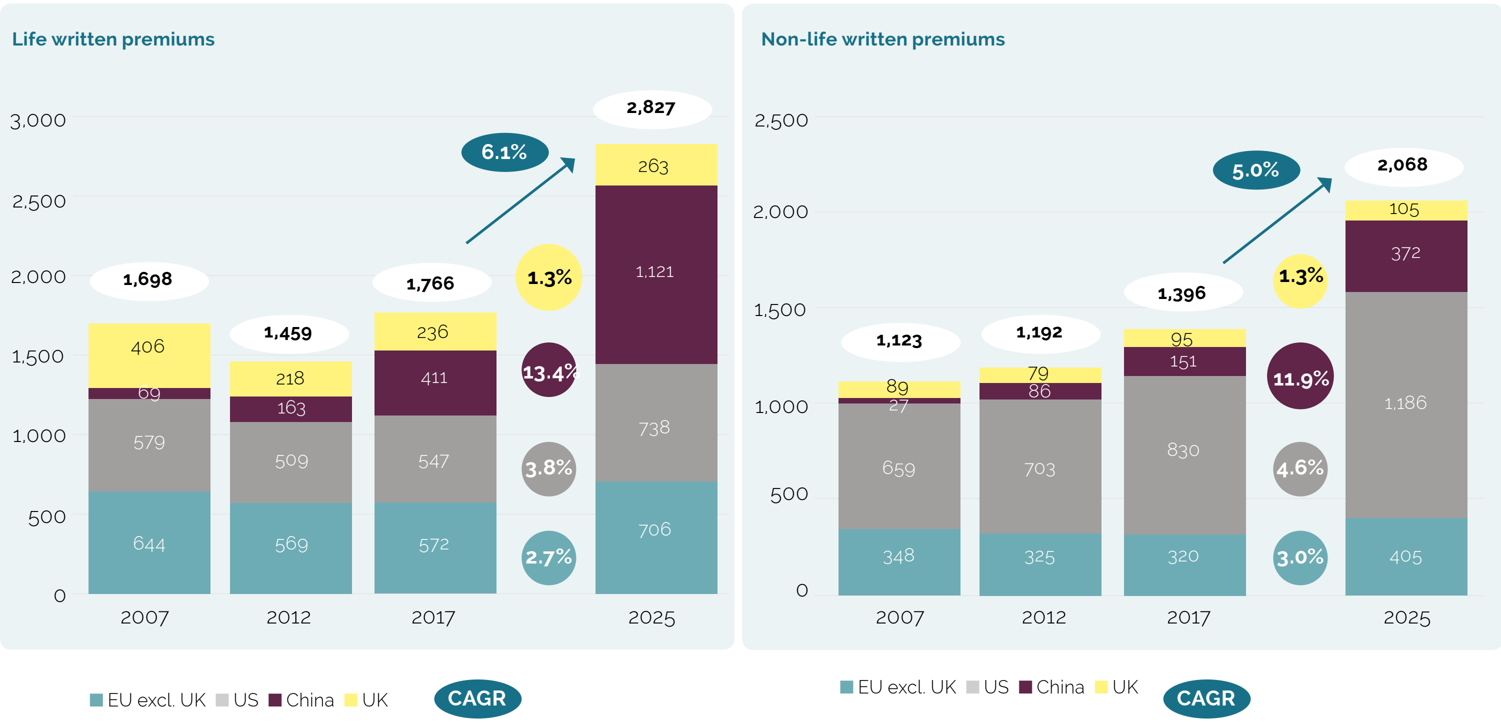
Life insurance premium growth in Europe stalled significantly in the last decade and slow growth is expected to continue up to 2025, at a CAGR of 2.7% (see Figure 18). Faltering returns stemming from years of low interest rates, combined with ageing populations and rising life expectancies, have had a considerable impact.

In the non-life sector, we see a similar trend, with the EU-27 projected growth trailing far behind China and the US. Here, Europe's fall down the podium is partially a result of a long-term decline in trade, which is likely to have adversely affected non-life insurance premiums.[36] An increase in bilateral agreements has led to fragmented regulation, challenging insurers' profitability as cross-border transactions become more costly. Meanwhile, a decline of guaranteed advantages is leading investors to deploy their money elsewhere. This, combined with falling gross written premiums (GWPs), is driving revenues downwards.

Fortunately for European insurance, opportunities for innovation remain via technology and evolving customer demand. In order to harness these trends, European insurers must seize the initiative, taking proactive steps so that they can play a leading role in the industry's next disruption. In order to be successful, they will need to streamline their operations, using cutting edge technology to drive down costs and lower risks. At the same time, insurance players should embrace the opportunities presented by a fast-changing world driven by technology and client behavioural change.

36. SwissRe, Sigma5/18 Global economic and insurance outlook 2020, 2018

Figure 18: Global Insurance Life & Non-Life GWPs, US$ billion



Source: PwC Market Research Centre analysis. Past data based on Insurance Europe, Swiss Re and Munich Re.

On demand and personalisation will drive the future of insurance

The rise of the telematics industry and sharing economy has already had a profound impact on the sector, enabling insurance companies to provide pay as you go insurance, with the growth of this product offering set to accelerate in the coming years. Traditional value chains of the industry are being disrupted slowly but surely. Leveraging new technologies will help insurers to take advantage of new risks and products, providing new sources of revenue.

The acceleration of connected devices will provide insurance companies with more data than ever before, therefore offering a better risk profile of their clients. On one hand, this will reduce the risk of claims and will therefore lower insurance premiums. However, the overall impact of telematics will be a positive one, with new insurance products to sell being a key factor.

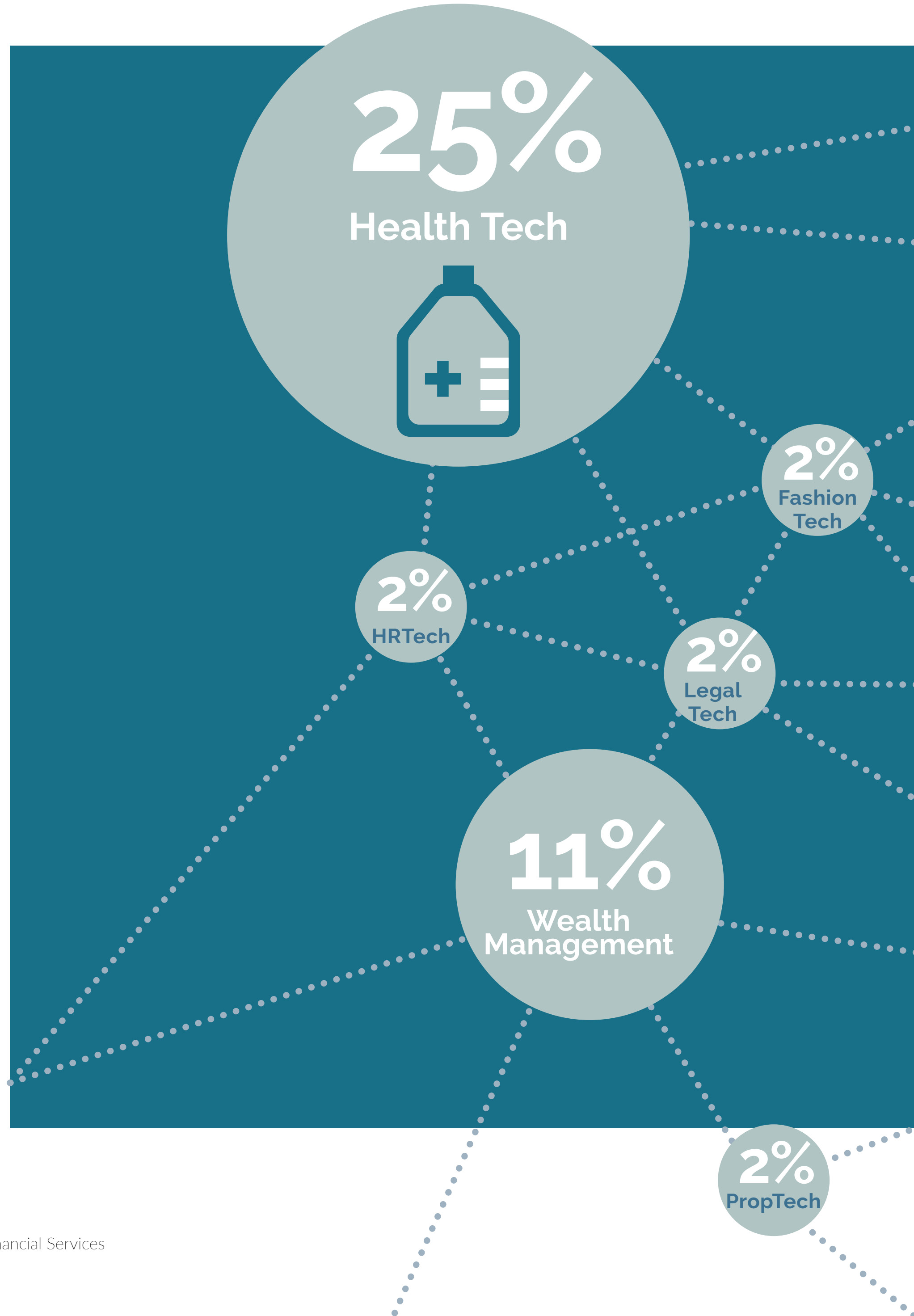
For instance, the rise of the sharing economy will push people away from owning assets in the future. This poses questions for insurers, as people will only require insurance at the time of using an asset. One clear answer to this is the rise of usage-based insurance, where driving behaviour and mileage is tracked in order to calculate car insurance premiums. With a growing number of devices connected to the cloud and a more sophisticated Internet of Things (IoT), this market is set to experience rapid growth.

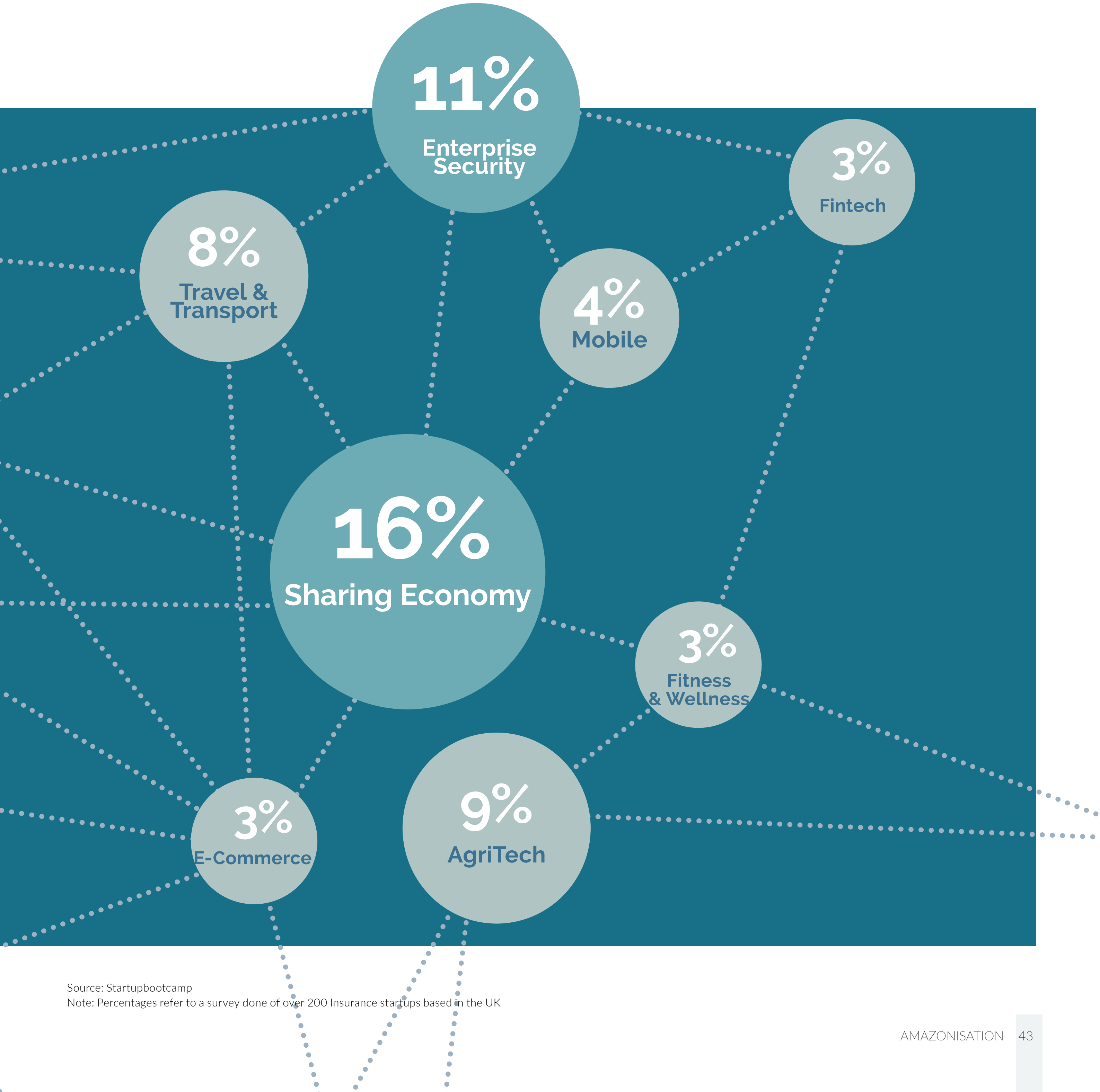
Insurers should consistently look to access new data sources and find new ways to drive value from data. An increasing number of InsurTech start-ups are focusing on adjacent industries and are looking to leverage the associated data for the traditional insurance sector (see Figure 19). This rise of start-ups from beyond insurance will offer a large number of solutions and will help insurance companies to target new customers and increase premium income.

For insurers, this represents the opportunity to cover emerging risks. For instance, PropTech, with the use of IoT in property, helps owners to predict and prevent different types of damage. The advanced use of drones and satellites in agriculture – AgriTech - helps to predict environmental factors and can reduce crop claims. Furthermore, as the digital world become increasingly inter-connected, cyber-insurance will be pivotal. European insurers should look to collaborate with start-ups from adjacent industries such as agriculture, aircraft manufacturing, health, cyber-security, maritime and general transport in order to gain access to these new potential revenue streams.

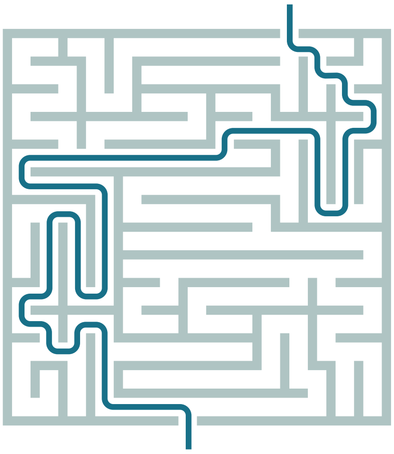
However, data alone is not enough to generate profit. European insurers should use this data to improve personalisation and act as a one-stop shop, providing one insurance contract that bundles the clients' various needs together. This type

Figure 19: InsurTech ecosystem – British start-ups focus on adjacent industries





Source: Startupbootcamp
Note: Percentages refer to a survey done of over 200 Insurance startups based in the UK



of contract would be adapted over time as material changes occur. The need to have a transparent and competitive pricing system will be a prerequisite in an ever-transparent world where information and competition will always be one click away.

Rise of sustainable insurance will provide opportunities for players

Sustainable insurance is another example of an adaptation to customer preferences, where insurers aim to contribute to environmental, social and economic sustainability in their portfolios. While this may entail investing in ESG products, it can also be achieved through boycotting potential clients who engage in business practices that are antithetical to sustainability. We believe that sustainable insurance will also grow because it is in insurers' best interests to limit climate change.

For example, a French insurer, based on the most optimistic scenario of a COP21 model, calculated that its losses would double by 2050 (20% of this would be due to climate change). Firms also seek to predict other potential costs, with one company in particular assessing its exposure to a "responsibility risk", which refers to the reputational risk associated with failing to become sustainable. From both a cost perspective and from a client retention perspective, it is clear that insurers must embrace sustainability.

Insurance companies are large institutional investors and can play a major role in the support for new products, especially ESG-based retirement products. Therefore, a synchronised effort by insurers to decarbonise their portfolios could therefore have significant effects, both by attracting new clients and by significantly reducing costs in the long-term. For instance, the collective investments of the top 40 US insurance groups in fossil fuels was US$459 billion in 2017, illustrating the large room for improvement which could be made.[37] In Europe, progress is ongoing, with seven major European insurers having already announced measures to withdraw support for companies reliant on coal.

With EIOPA having joined the Sustainable Insurance Forum last year, we may soon see regulation in this space which would further encourage sustainable insurance. However, given Europe's position as a global leader in ESG investment, European insurers should not find the shift towards sustainable investment a difficult one. They must therefore take the initiative and adopt their investment strategies accordingly, without waiting for regulation to force them to do so. While Europe's insurance industry has fallen in the previous few years, sustainable insurance is an opportunity for the region to gain a head start over its regional rivals and benefit over the long-term.

Technology and evolving value chain will drive consolidation

Various ongoing trends in the insurance industry, such as high costs, technology and the disruption of the traditional value chain, will give rise to consolidation of the market. Forward looking insurers should consider the value of partnerships and acquisitions in order to strengthen their market position or integrate new technologies.

Post-crisis years have yielded significant consolidation, specifically in advanced economies (see Figure 20). The number of domestic insurance companies fell drastically as limited organic growth opportunities, increased competition in the market, higher costs and a progressively weaker pricing environment forced many insurers to turn to mergers & acquisitions for growth.

Given that these competitive pressures are likely to persist in the coming years, insurers should seek to incorporate RegTech into their operations in order to transform compliance into a competitive advantage. If insurers do not successfully trim costs, however, we believe that they will continue to seek out deals in order to gain scale.

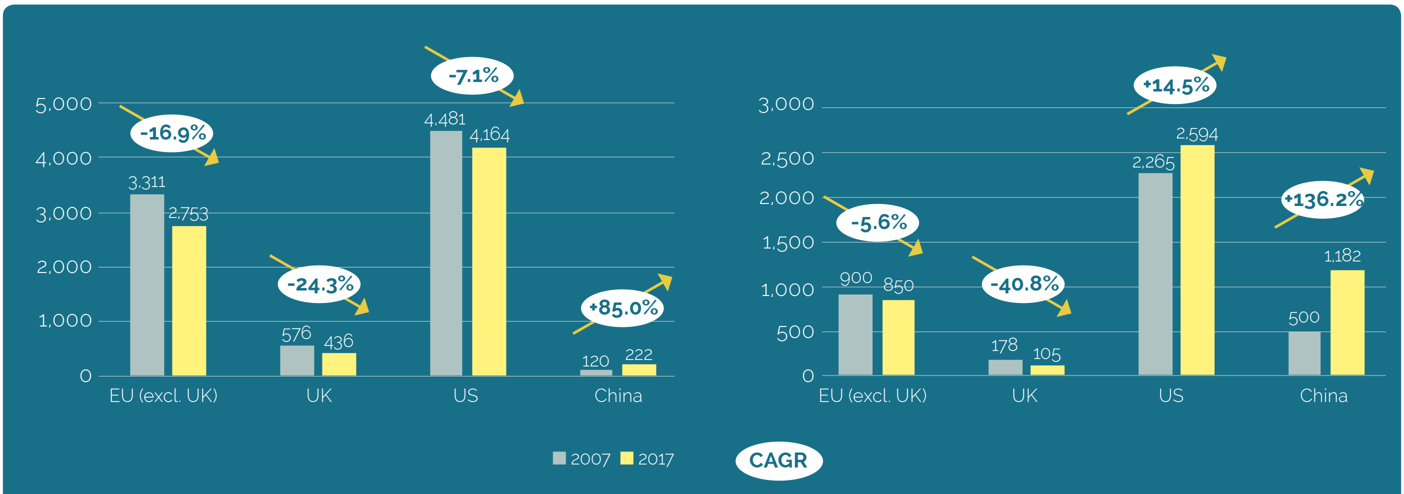
Other factors will also drive M&A activity. For instance, the development of driverless cars will make roads safer, leading to lower insurance premiums and further hindering profitability.[38] Meanwhile, the shift towards car sharing will push the ownership of cars predominantly into the hands of carmakers and other companies. As a result, car insurance will be negotiated by these companies rather than by individual drivers, therefore disrupting the typical value chain.

Within life insurance, we will see increased competition from the AWM industry. This will be driven by policymakers pushing for a level playing field by eliminating tax and other advantages for insurance products, as

37. UN and Sustainable Insurance Forum, *Sustainable Insurance: The emerging agenda for supervisors and regulators*, 2017

38. Harvard Business Review

Figure 20: European economies see a fall in the number of insurance undertakings (L) and direct number of employees in thousands (R)



Source: PwC Market Research Centre analysis based on Bureau of Economic Analysis, Insurance Europe, Eurostat and OECD

well as a long-term low interest rate environment leading to a fall off of guaranteed return products, which will pose survival challenges to this segment of the industry.

In light of this, insurers who are engaging in M&A will need to search for opportunities where deals can open access to new markets, create operational efficiencies, or improve product diversification. Given that European insurers will seek out ways to integrate new technology into their operations, we expect many traditional insurers to acquire or collaborate with InsurTech companies. Indeed, with a record-high 85 InsurTech deals totalling US$1.42 billion globally in Q1 2019[39], the industry appears to already be heading in this direction. European insurers must be proactive, with fast and decisive strategic choices, if they want to seize the opportunities that new technologies present to them.

While technology can provide vast benefits to insurers, it is no substitute for having a strategy geared towards gaining and holding clients. We believe that, in the spirit of Amazonisation, insurers must do more to answer the demands of clients and serve their needs. In practical terms, this involves developing an effective communication and marketing strategy and providing products that appeal to their clients.

39. CB Insights

3.

Driving Europe to the fore: our recommendations

It is very clear that Europe's financial services sector is undergoing a significant change. New regulations, technologies and client expectations are forcing this change. We believe that Amazonisation should be a key consideration as the future path is forged for financial services.

In practical terms, FS firms must promote client focus, which will often involve looking to offer online platforms that increase transparency and ease of use. Firms must also look to be innovators, whether that means by offering new products or adopting new operating models. In addition, firms must seek to leverage customer data so that they can understand and adapt to evolving client needs.

Below, we explore four recommendations that we believe will help Europe's financial services remain competitive in the coming years.

Firms must disrupt themselves

Amazonisation will affect all facets of the global Financial Services industry and players in this space will need to push efficiencies while balancing costs in order to adapt to the new era of FS. Players will need to create value, not only for themselves, but also their clients and the European economy as a whole. This will require implementing new innovative technologies in their operations, adapting to changing client preferences and ensuring that they have a strategic plan.

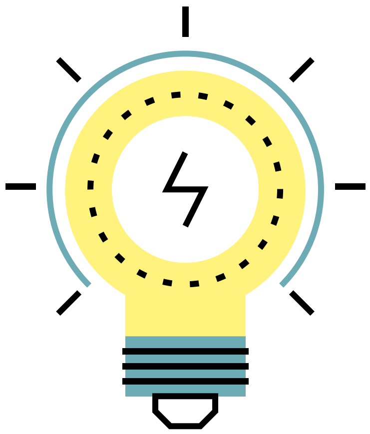
As data becomes increasingly monetised, firms must ensure that their systems are not only compliant with regulations, but also secure enough to give clients peace of mind. This will enable trust to be built between the end user and financial companies, something that is still lacking in many ways today. Insights gleamed from this data will also allow for the creation of new revenue streams as the financial ecosystem evolves beyond the traditional.

Players must become disruptors themselves if they are to survive and thrive in the coming years. The introduction of new technologies should, in the longer term, optimise costs and increase efficiencies. While some firms will not survive the coming years, those that do will have made costs variable and brought about significant changes across their operating models.

Deepen cross-border integration

Despite the European Single Market, Europe has struggled with cross-border integration, especially in finance. As the world becomes increasingly connected and the Amazonisation of the global FS sector accelerates, it is crucial that European FS firms deepen their cross-border integration. While steps have been taken, such as the Single Supervisor and Single Resolution Authority, more needs to be done. However, this is on the books. Several much-awaited reforms will see significant changes and increased integration.

The Banking Union has already seen important results, including lowering overall risk, increasing capital and lowering leverage. Nonetheless, different rules apply in different countries and there will need to be more political



consensus surrounding the Single Resolution Fund and European Deposit Insurance Scheme. National regulations continue to fragment the banking market and we would suggest improvements to the liquidity management procedures by cross-border banks. Finally, a completed CMU would provide better financing of SMEs. Should the CMU be successfully completed, the capital markets would be able to offer additional financing and contribute to bolstering innovation in the region.

Integration is not synonymous with centralisation. Financial Centres across the single market should be allowed to specialise and flourish. Fragmentation has never been a winning strategy and more needs to be done to bring markets together.

Strengthen innovation and the digital dimension of the single market

Innovation and the digital trend will continue to transform the financial services landscape. European players must therefore be proactive, leveraging this trend in order to boost their competitiveness on a global scale. For instance, the rise of technology will enable online platforms to become valuable comparison and purchasing tools for FS customers. In addition, with data analytics already sophisticated, European FS companies must ensure they harness client data in order to deliver what their customers want.

In order to boost innovation in the region, the European Commission has taken steps to prioritise FinTechs and support new technologies.[40] Despite these steps, new entrants often face significant hurdles, such as a lack of uniform regulations across markets, licensing rules, access to capital and unfavourable competitive conditions.

To counter this would take concerted efforts to align regulation across markets, promote easier access to capital and foster competition across the single market. This should be the ultimate aim of the European Commission if the European financial sector is to truly flourish in the future.

Lead the sustainable finance race

Europe is already ahead of the curve in this space, however much work will need to be done if it wishes to stay there. There is already a US$5 trillion to US$7 trillion funding gap that is needed to meet the SDGs. UN estimates point to the fact that in Europe alone, for it to achieve its energy and climate policy targets, an additional EUR170 billion per year is required.

Clearly there is room for improvement and for business in this space. The financial sector can play a crucial role by ensuring that capital flows towards sustainable investments, renewable energy, low-carbon technologies and other climate friendly strategies. While Europe already accounts for nearly three quarters (73%) of ESG investments, more work can be done. European banks must implement sustainability lending and asset managers should listen to their own calls for the companies they invest in to be more ESG compliant.

The EU has voiced its support for the UN's SDGs and the Paris Climate Agreement. An action plan has been released and should establish a framework that will facilitate sustainable investments, propose regulations regarding sustainability risks and amend benchmarking regulations. In the shorter-term, this is an area where Europe can thrive and lead the pack, all the while working on ensuring that Europe remains competitive in others.

40. As an example, in March 2018, as part of its FinTech action plan, the European commission presented a proposal for a regulation on crowdfunding service providers.

Appendix

In terms of our projections, we use econometric modelling to obtain our estimates. The relevant indicator (AuM, GWP, loans, payments transactions etc.) is used as the target variable (generally based on data from 2000 to 2017) and various macroeconomic indicators from IMF are used as explanatory variables for the EU excluding UK, the US, the UK and China. We use statistical software to test various models and have shortlisted those statistically significant models for each country or region. In addition, we have included PwC experts' points of view on the future key trends within the different industries.

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