



September 2023

Future State of the Investment Industry

Rhodri Preece, CFA, Ryan Munson, Roger Urwin, FSIP, Andres Vinelli, Larry Cao, CFA, and Jordan Doyle



Abstract

This report frames the most significant developments that will impact the investment industry in the next 5 to 10 years. It provides scenarios for investment organizations to navigate and outlines principle recommendations for firms and professionals.

CFA Institute is a global community of more than 190,000 investment professionals working to build an investment industry where investors' interests come first, financial markets function at their best, and economies grow. In the mainland of China, CFA Institute accepts CFA® charterholders only.

© 2023 CFA Institute. All rights reserved.

No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopy, recording, or any information storage and retrieval system, without permission of the copyright holder. Requests for permission to make copies of any part of the work should be mailed to: Copyright Permissions, CFA Institute, 915 East High Street, Charlottesville, Virginia 22902. CFA® and Chartered Financial Analyst® are trademarks owned by CFA Institute. To view a list of CFA Institute trademarks and the Guide for the Use of CFA Institute Marks, please visit our website at www.cfainstitute.org.

CFA Institute does not provide investment, financial, tax, legal, or other advice. This report was prepared for informational purposes only and is not intended to provide, and should not be relied on for, investment, financial, tax, legal, or other advice. CFA Institute is not responsible for the content of websites and information resources that may be referenced in the report. Reference to these sites or resources does not constitute an endorsement by CFA Institute of the information contained therein. Unless expressly stated otherwise, the opinions, recommendations, findings, interpretations, and conclusions expressed in this report are those of the various contributors to the report and do not necessarily represent the views of CFA Institute. The inclusion of company examples does not in any way constitute an endorsement of these organizations by CFA Institute. Although we have endeavored to ensure that the information contained in this report has been obtained from reliable and up-to-date sources, the changing nature of statistics, laws, rules, and regulations may result in delays, omissions, or inaccuracies in information contained in this report.

CONTENTS

Executive Summary	1
Principle Recommendations for Investment Organizations	4
Principle Recommendations for Investment Professionals	4
Introduction	5
State of the Industry	7
Talent and Transition	7
Rise of Retail	7
Passive Pressure	9
Automation and Personalization	11
Alternative Assets	11
Evaluation of the 2017 Scenarios	12
Fintech Disruption	12
Parallel Worlds	12
Lower for Longer	12
Purposeful Capitalism	12
2023 Megatrends and Scenarios Overview	14
The Art of Scenario Planning	14
Megatrends	14
Shifting Demographics	14
Technology Transformation	15
Deglobalization	15
Socioeconomic Imbalances	15
Government Footprint	15
Climate Change and Environmental Degradation	16
Combination of Megatrends Leads to Scenarios	16
Diverging Worlds	17
Deglobalization: The Unraveling	17
A More Unequal World?	18
A Demographic Dividend?	19
The Technology Divide	20
A Cautionary Tale?	22
Sustainable Finance	23
The Climate Challenge	23
An Industry Transformed?	25

Digital Transformation	27
Artificial Intelligence and Big Data	27
An Expanding Universe of Asset Classes and Products	28
Information and Influence in the Digital World	29
Implications for the Industry	30
The End of Cheap Money	31
In the Wake of COVID-19: Tightening the Monetary Belt	31
Easy Money: A Hard Habit to Break	32
Conclusion	34
The Path Forward	35

EXECUTIVE SUMMARY

Where is the investment industry headed, and how can current and aspiring investment professionals best equip themselves for what is to come?

Although one of the key lessons from the last several years is that questions such as these have no easy or definitive answers, that does not mean we should avoid them—or that attempts to address them are not productive. As a saying attributed to Dwight D. Eisenhower states, "plans are worthless, but planning is everything."¹ The same logic applies to envisioning the future state of the investment industry, developing scenarios about what that future might look like, and preparing accordingly.

Individually, such narratives could be lucky or simply wrong. But the process itself—consulting with experts, identifying trends, gaming out scenarios,

and acquiring the skills, expertise, and mindsets to adapt to them—can equip us with the foresight and insight both to anticipate what that future might require and to recalibrate our strategies and perspectives when the unexpected inevitably unfolds.

With that in mind, CFA Institute surveyed its members and consulted with experts to see how they expect the investment industry and profession to evolve over the next 5–10 years and what they are doing to prepare for that evolution. Based on their perspectives and building on our 2017 study, "Future State of the Investment Profession,"² we constructed four scenarios—Diverging Worlds, Sustainable Finance, Digital Transformation, and The End of Cheap Money—each of which reflects a potential development pathway for both the investment profession and the investment professional.

Diverging Worlds

Deglobalization, geopolitical conflict, inequality, demographic disruptions, and technological innovation contribute to increasingly distinct and divided perspectives as targeted content and personalization create alternate realities.

Scenario Summary

- Different goals and values among various geographic, generational, and socio-economic segments lead to diverging opinions and preferences and increase demand for personalized products.
- Financial services participation rates increase globally but vary from one market to the next. Simple, easy-to-access, mobile-first products and platforms that harness client data drive personalization and broaden financial services access across demographic groups.
- Different cohorts both promote and reject sustainability, resulting in more targeted products, such as thematic and impact investments. Improved data and corporate reporting lead to better outcome metrics.
- Direct indexing and tokenization, among other technology-enabled investment products, encourage more targeted capital allocation and an expanded investible universe.
- Aging markets with negative replacement rates challenge existing social safety nets, leading to underfunded pensions and reduced economic growth. Emerging markets with younger demographics provide opportunities to develop more comprehensive retirement income structures and products that better serve future retirees.

¹Garson O'Toole, "Plans Are Worthless, but Planning Is Everything," Quote Investigator (18 November 2017). <https://quoteinvestigator.com/2017/11/18/planning/>.

²CFA Institute, "Future State of the Investment Profession: Pursuing Better Outcomes—for the End Investor, the Industry, and Society" (April 2017). <https://rpc.cfainstitute.org/research/surveys/future-state-of-investment-profession>.

Sustainable Finance

Investors increasingly take environmental, social, and governance (ESG) considerations into account in their decisions, particularly as they pertain to externalities. Much of the business sector and investment industry embraces a multistakeholder focus with an emphasis on long-term sustainable practices and climate change mitigation.

Scenario Summary

- Central banks and regulatory authorities help ensure that business and finance are trustworthy and help manage systemic risks.
- Asset owner institutions exercise more influence through stewardship and the

embrace of ESG criteria, aligning value creation with sustainability and extended time horizons.

- Asset owners and managers work toward net zero as the energy transition gathers momentum and investment organizations adapt their activities to respond to regulatory pressures and societal and customer expectations.
- The talent demands of the investment industry expand in scope as sustainability factors grow in importance. The values of investment organizations become critical in the battle for talent.

Digital Transformation

Rapid technological innovation in the form of artificial intelligence (AI), machine learning, and big data, among other applications, leads to accelerating change in the investment industry. Those firms that best integrate these developments into their talent-acquisition processes and investment teams and best meet client demand for personalized and technology-driven products will outperform.

Scenario Summary

- The AI + human intelligence (HI) equation takes on ever-greater importance as more mundane and rote tasks are increasingly outsourced to large language models (LLMs), such as ChatGPT, and other tech solutions, leaving human

professionals free to conduct more extensive investment analysis.

- Digital assets, tokenization, personalization, and other tech-driven investment solutions grow more ubiquitous, help persuade more individuals to become investors, and enable investment professionals to better serve their needs.
- Social media and other novel modes of communication drive investment behavior, potentially contributing to bubbles and other excesses.
- Regulation and governance structures, among other investor protections, struggle even more to keep up with the pace of innovation and the introduction of new investment products.

The End of Cheap Money

Elusive economic growth, elevated inflation, and greater levels of debt combine to create higher and more volatile nominal interest rates. Central banks have abandoned their zero or near-zero interest rate policies but struggle to balance the need to manage inflation with that of promoting economic growth. The related turmoil in the economy and financial markets encourages innovation and product development in the investment industry.

Scenario Summary

- Central banks continue to manage inflationary episodes and unwind quantitative

easing as well as the near-zero interest rate policies that encouraged relatively stable financial markets, increased risk taking, higher propensity for leverage, asset price appreciation, and economic activity.

- Higher and more variable nominal interest rates inhibit economic growth and continue to disrupt financial markets and institutions.
- Fiscal consolidation and supply-side, geopolitical, and policy shocks contribute to a challenging economic environment and further subdue the appetite for both risk and leverage.

We deconstruct these scenarios into the relevant megatrends that shape them and consider how they could play out in the medium term as a means of distilling the challenges and opportunities they present.

Conducting such analyses is more important for both current and aspiring investment professionals today than at any time in modern memory because the investment industry has entered a new, uncertain, and transformational era. Sometime over the last several years, many of the forces that defined the sector since the global financial crisis (GFC), and possibly for the last five decades, began to shift or even reverse. Investment professionals had come to expect, for example, that low inflation, low interest rates, increasing globalization, and geopolitical stability were, in effect, permanent realities.

That has all changed. The COVID-19 pandemic and the related economic dislocations and monetary and fiscal responses contributed to the sea change, but they were not the only drivers. And the results are stark. Inflation, which had remained low and well managed for a generation in much of the developed world, has resurfaced with unexpected strength and resilience. Central banks have hiked interest rates in response, which has created its own disruptions—the Silicon Valley Bank, Signature Bank, and First Republic Bank collapses are only the most visible recent examples. Globally, the relative stability of the post-Cold War period and its ever more expansive and interconnected markets seems to have ended amid a new war in Europe and resurgent international rivalries.

Yet, although the tide has definitively turned in certain areas, it is surging as strongly as ever in others. The threat of climate change has grown ever more palpable, and ESG considerations are ever more critical for investment analysis as finance seeks to do its part to achieve net-zero targets and build a more sustainable world.

The pace of digital disruption and tech innovation in finance has continued to accelerate, with ChatGPT and other AI and big data applications coming to the fore. More and more investment professionals are integrating Python and other technical knowledge into their toolkits alongside fundamental analysis and more traditional disciplines.

The ramifications of these developments on investment firms and professionals are as enormous as they are unknowable. But as challenging as the next 5–10 years may be, we are confident the investment industry will adapt quickly and that a better, more integrated, more sustainable, and more client-focused sector will result. Through the findings and analysis contained in this report, we aim to help provide readers with the insights necessary to navigate this transition and create better outcomes for their clients and all stakeholders the investment industry serves. In this way, we move closer to fulfilling the mission of CFA Institute: "to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society."

Survey Methodology

Quantitative inputs are culled from a global survey of more than 3,000 CFA Institute member respondents in late 2022.

Qualitative inputs are derived from discussion forums with industry leaders from the CFA Institute Research and Policy Center Advisory Council and the CFA Institute leadership.

Principle Recommendations for Investment Organizations

Based on the scenarios outlined in this report, we offer the following recommendations for firms, expressed as principles that firms can incorporate into their specific business contexts:

1. Build organizational culture around a multistakeholder business model centered on purpose and aligned to a fiduciary mindset. Strengthen the cultural and structural aspects of diversity, and embed inclusion and equitable human capital practices.
2. Evolve business practices and performance measurement toward outcome-driven frameworks aligned with end-investor goals, embracing total portfolio thinking.
3. Build more balance into benchmarks, consider the alignment of incentives and time horizons, and embed more holistic integration of sustainability risks and opportunities.
4. Enhance innovation capabilities through greater resourcing and stronger governance with regard to technology and product development, and embrace data science.

5. Commit to greater collaboration and expand engagement with coalition organizations to address system-wide, complex industry challenges.

Principle Recommendations for Investment Professionals

In the future state of the industry in which change is accelerating, investment professionals must embrace a growth mindset and agility to stay relevant in their careers and capitalize on new opportunities. Based on the scenarios identified, we offer the following recommendations for investment professionals:

1. Build clear purpose into your work. Nurture your values, and live them in your work. Strengthen client relationships by aligning on values. Develop a richer understanding of client preferences and motivations to cater to clients' evolving needs.
2. Understand the opportunities brought about by new technologies and data, and identify where and how to best deploy these advances to serve client objectives. Embrace creative thinking, teamwork, collaboration, and innovation, grounded in ethics.
3. Product life cycles are accelerating, and knowledge continually needs to be updated. Commit to lifelong learning and adaptation. Understand the intersections among finance, data science, and sustainability to be agile in the evolving industry landscape.
4. Build expertise where there are skill gaps. Start as the apprentice and become the mentor to develop future talent and give back to the profession.
5. Broaden your thinking and horizons, develop your T-shaped skills (combining subject matter expertise with a wider understanding of other knowledge domains and an ability to connect them), and strengthen your network connections.

INTRODUCTION

The world is in flux. Economies and markets are under strain as geopolitical instability, aging demographics, digital disruption, energy insecurity, and climate change deepen societal fractures across regional, generational, and wealth divides. Macroeconomic shifts have led to debt overhangs, rampant inflation, higher interest rates, and sputtering equity markets. Changing labor dynamics and the evolving nature of work have created further challenges amid the global recovery from the COVID-19 pandemic.

All these trends are shaping the future state of the investment industry. As firms assess these currents to identify risks and opportunities through the lens of their business models, they must inevitably balance their short-term priorities—to respond to macro policy shifts and client asset allocation pivots, for example—with such long-term needs as embracing sustainability, innovating new products, and enhancing their technological capabilities.

This report analyzes the megatrends shaping the world through the prism of the future of the investment management industry and channels them into four key scenarios: Diverging Worlds, Sustainable Finance, Digital Transformation, and The End of Cheap Money. It does so not through forecasts but rather through narratives that frame the most salient issues, looking ahead as they play out over a 5- to 10-year time horizon. The ability of industry leaders and professionals alike to convert these scenarios into opportunities to serve clients and other stakeholders will help determine their future viability.

This work revisits our 2017 report, "Future State of the Investment Profession," which first introduced the megatrend conceptual framework along with the related narrative scenarios expected to define the investment management industry. Six years after that study, those earlier megatrends and scenarios have evolved and shifted, as we outline later in the "Evaluation of the 2017 Scenarios" section. Lower for Longer, for example, has given way to The End of Cheap Money as higher interest rates and inflation have soared to unfamiliar heights. Fintech Disruption and the digital revolution, meanwhile, continue to develop and reshape how the industry operates. New trends have materialized as well. With the acceleration of net-zero ambitions and the global embrace of ESG criteria, sustainability, in particular,

has pushed to the forefront of the corporate and political agenda.

Indeed, the sustainability challenge stands at a critical juncture. In the medium term, the low-carbon transition faces numerous headwinds that may slow or even derail it. The investment industry has become the focus of a politicized debate around ESG considerations (particularly in the United States). How the sector traverses this fraught path—explored in our Sustainable Finance scenario—will shape its evolution in the years ahead.

The unwinding of the globalization process has accelerated since our previous report. Post-pandemic supply chain problems compounded earlier national efforts—such as those in the United Kingdom and the United States—to reduce dependence on overseas trade and cross-border manufacturing. Ongoing China-US competition and the Russia-Ukraine War have further fueled deglobalization. The Diverging Worlds section considers the potential macroeconomic implications as political instability and the rebalancing of the world order become key drivers of market and economic behavior.

Demographic challenges constitute another megatrend examined in Diverging Worlds. Aging populations and sub-replacement fertility rates in Europe, China, and elsewhere contrast with rapid population growth in Africa. The challenges wrought by these trends will test labor markets and retirement systems across the globe.

The digital revolution continues to gather momentum and will exert a major influence on the investment industry's future, as we explore in the Digital Transformation section. Younger investors—so-called digital natives—are more comfortable with technology³ and have different investment preferences and expectations than their older peers. They are piling into the markets through new platforms, products, and information channels, and they require more personalized products and solutions. Firms that want to increase their assets under management and stave off competition from outside traditional finance will have to innovate. Practitioners will have to harness machine learning tools, big data, and other new analytical methods to increase their skill sets and expand their career opportunities.

³CFA Institute, "Enhancing Investors' Trust: 2022 CFA Institute Investor Trust Study" (2022). <https://rpc.cfainstitute.org/research/surveys/enhancing-investors-trust>.

This report provides a detailed exploration of these dynamics. Our findings are informed by insights from more than 3,000 CFA Institute members surveyed in late 2022 and from consultation with industry leaders. We begin by taking stock of the current state of the investment industry to establish a baseline and review our assumptions from the 2017 "Future State of the Investment Profession" report. We then address the megatrends of today and

the future state scenarios, examining each in turn, and provide a series of recommendations for firms and professionals.

How the industry responds to the challenges we set out here will play a decisive role in how it builds wealth for clients worldwide and how it contributes to society in the decades to come.

STATE OF THE INDUSTRY

Investment management is an industry in transition. Disruption is everywhere. To better understand how the megatrends of today will develop into the scenarios of tomorrow, we first need to assess the current financial services landscape.

Talent and Transition

The war for investment industry talent is growing fiercer. Top business school graduates have long been a central focus of the sector's recruiting efforts, but competition from Silicon Valley, large tech firms globally, and fintech startups has increased staff acquisition and retention costs. This trend combined with downward pressure on management fees and the market's appetite for new products and platforms poses a significant threat to the traditional investment management business model.

The evolution of skill requirements contributes to the talent challenge. Expertise in AI, machine learning, and big data is growing ever more essential, but it remains difficult to identify and recruit for these skill sets. In our survey, 41% of respondents cited a shortage of related talent as a major obstacle to the integration of AI and big data into the investment process. This shortage inhibits firms from expanding their analytical capabilities and raises the premium that practitioners with both finance and data science experience can demand.

The rapid pace of development in the sector means even experienced investment professionals may be rendered obsolete if they fail to adapt. Overall, 37% of CFA Institute members who responded to an earlier Future of Work survey believe their job role will be substantially different in 5–10 years; another 2% believe their job role will cease to exist in that time frame.⁴ Practitioners believe that job role disruption will come from a variety of sources, see **Exhibit 1**.

Such uncertainty reveals the varied challenges the industry faces today and increases the pressure on investment performance. How these factors develop

will inform how practitioners perform their day-to-day roles and drive organizational models in the near term.

Rise of Retail

The "democratization" of finance—expanding access to financial services for all investors—is radically reshaping investment management. Several factors have converged to propel this dynamic. Online trading platforms on mobile devices and personal computers are now ubiquitous. Frictionless no-fee trades (often funded by payment for order flow), fractional shares, and low account minimums have opened financial markets to countless new investors. Cryptocurrencies, too, have provided an entry point for new waves of predominantly younger retail investors, while capital market participation rates among retail and individual investors have spiked since the beginning of the COVID-19 pandemic.⁵

As a consequence, individual investors have overtaken institutional investors in total assets under management (AUM), according to Indefi—see **Exhibit 2**. In 2021, individual investors accounted for 52% of global AUM. That number is projected to rise to 61% by 2030.⁶

A generational shift is also powering the rise of retail. As more baby boomers retire and begin to draw down their savings, millennials and Gen Z are accounting for a larger share of investible assets. With their tech savviness and long-term time horizons, they are confident investors: 70% believe they have the same opportunity to succeed in financial markets as their professional peers.⁷

Of course, such confidence carries certain risks. As the World Economic Forum cautions, "mechanisms such as gamification, retail access to complex products including derivatives, business models such as payment for order flow, and platform outages each warrants study and discussion on whether and how to appropriately protect retail investors."⁸

⁴CFA Institute, "The Future of Work in Investment Management: The Future of Skills and Learning" (2022). <https://rpc.cfainstitute.org/research/surveys/future-of-work-content>.

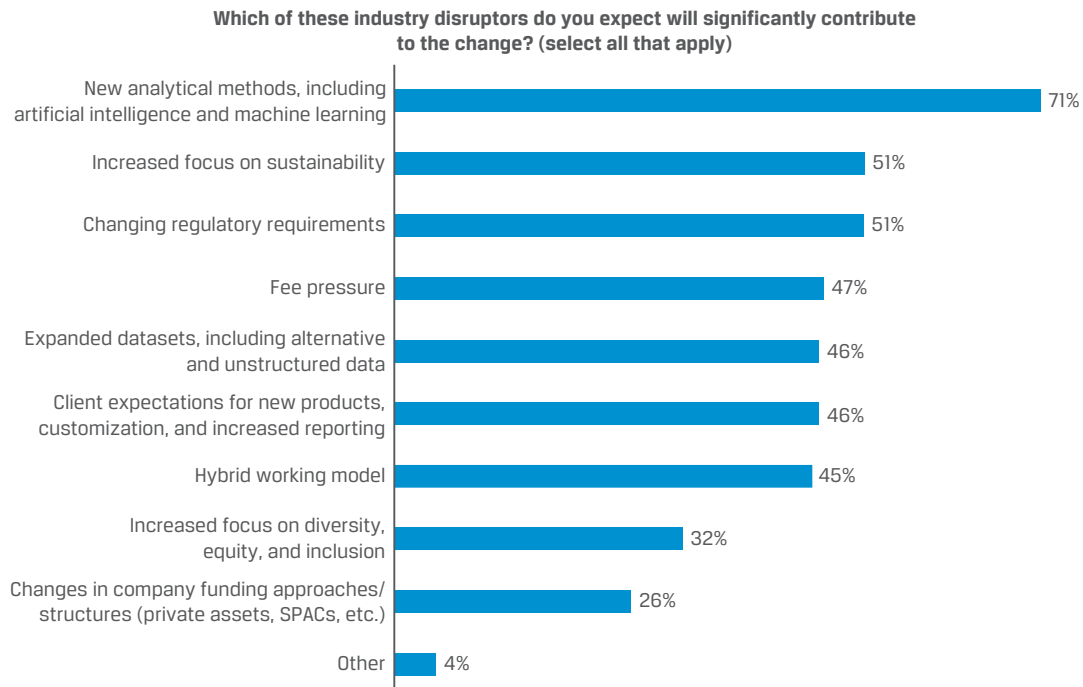
⁵Lu Wang and Elena Popina, "Day Trading Army's Grip on Stock Market Is Tighter Than in Meme Stock Era," Bloomberg (2 February 2023). <https://www.bloomberg.com/news/articles/2023-02-02/retail-army-s-grip-on-stock-market-is-tighter-than-in-meme-era>.

⁶Daniel Celeghin, Richard Bruyère, Ryan Carr, and Jonathan Doolan, "The Future Is Now: Five Waves Reconfiguring Asset Management," Indefi (March 2022). www.indefi.com/wp-content/uploads/2022/03/Indefi-Strategy-The-Future-is-Now.pdf.

⁷World Economic Forum, "The Future of Capital Markets: Democratization of Retail Investing" (August 2022). www3.weforum.org/docs/WEF_Future_of_Capital_Markets_2022.pdf.

⁸World Economic Forum, "The Future of Capital Markets."

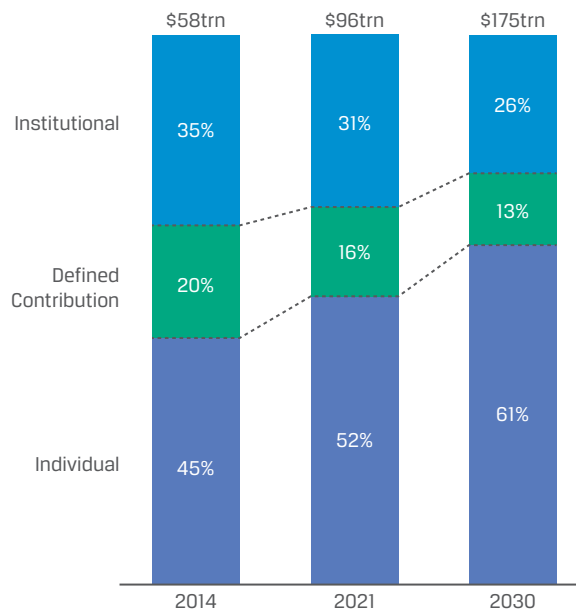
Exhibit 1. Sources of Job Role Disruption for Investment Professionals



Notes: N = 1,079. "SPACs" stands for special-purpose acquisition companies.

Source: CFA Institute, "The Future of Work in Investment Management: The Future of Skills and Learning" (2022). <https://rpc.cfainstitute.org/en/research/surveys/future-of-work-content>.

Exhibit 2. Global AUM by Investor Type



Notes: Per Indefi, "Institutional" represents defined benefit plans, insurance, endowments, foundations, sovereign wealth, and corporate treasury. "Individual" comprises assets from retail and private banks, financial advisers, family offices, and direct retail investments. Percentages may not sum to 100% because of rounding.

Source: Daniel Celeghin, Richard Bruyère, Ryan Carr, and Jonathan Doolan, "The Future Is Now: Five Waves Reconfiguring Asset Management," Indefi (March 2022). www.indefi.com/wp-content/uploads/2022/03/Indefi-Strategy-The-Future-is-Now.pdf.

Passive Pressure

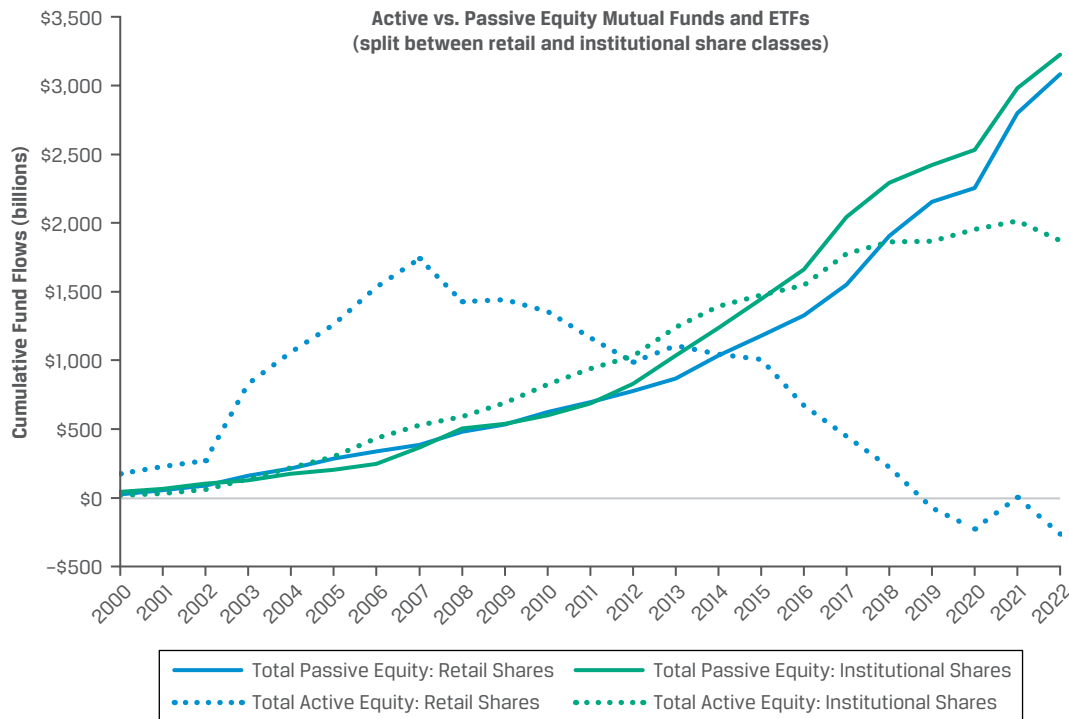
Low-cost passive investment vehicles are also fueling retail's rise, even if the pull of passive investing is not strictly a retail phenomenon. Since 2000, globally, both institutional and retail investors have moved more assets into passive mutual funds and exchange-traded funds (ETFs) than into their active counterparts (see **Exhibit 3**). The resulting competition has driven fund fees lower (see **Exhibit 4**). At the same time, accommodative monetary policies have boosted asset prices, which has made it harder for active managers to consistently outperform an index net of fees.

Questions about the utility of active management are central to the long-running active versus passive debate. By taking active positions in instruments that

deviate from the market benchmark, active managers contribute to price discovery, which should be considered part of the wider value active managers bring when evaluating fee structures.

To be sure, active management can and does outperform in some areas. Although passive investment in fixed income is growing, it still lags active management (see **Exhibit 5**). Over the 2012–21 period, at least 60% of actively managed fixed-income funds outperformed their benchmark across all share classes over 1-, 3-, 5-, and 10-year periods.⁹ Of course, low interest rates and low inflation were the norm in that period. Bond fund performance in the current economic setting may be more challenging on the whole, with possibly greater dispersion between the top and bottom performers.

Exhibit 3. Global Retail and Institutional Fund Flows to Active and Passive Equity Mutual Funds and ETFs



Notes: The data include funds domiciled in all countries contained in the Refinitiv database. Refinitiv defines fund flows as follows: "Estimated net flows are calculated in order to track asset flows of mutual funds, due to sales and redemptions, on a period-to-period basis. This is achieved by calculating the change of total net assets adjusted for the fund's performance over the same period. The performance adjustment is applied to the fund size at the beginning of the period and is then subtracted from the fund size at the end of the period."

Source: Refinitiv.

⁹Ford O'Neil and Celso Muñoz, CFA, "Why Bond Investors May Benefit from Actively Managed Mutual Funds and ETFs," Fidelity Institutional Insights (19 May 2022). <https://institutional.fidelity.com/app/proxy/content?literatureURL=/9860202.PDF>.

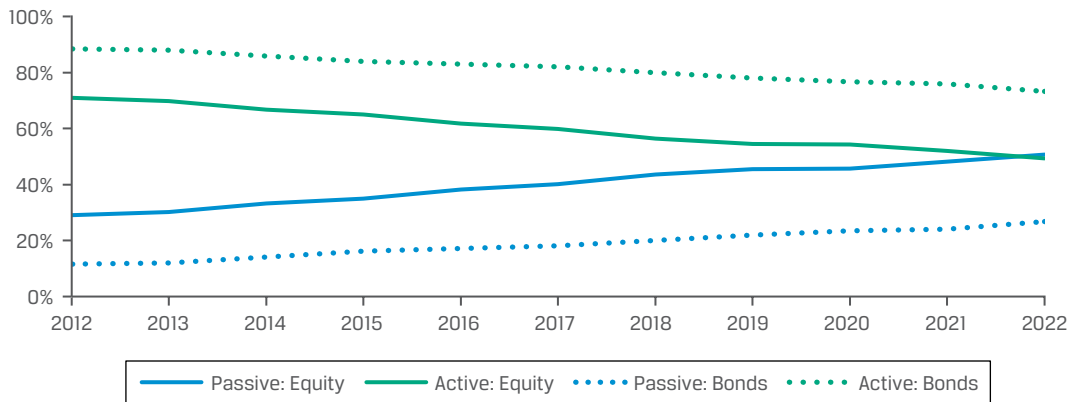
Exhibit 4. Expense Ratios and Ongoing Charges for US and European Active and Passive Mutual Funds

	Passive Equity				Active Equity			
	US Expense Ratios (%)	US Total Net Assets (USD billions)	Europe Ongoing Charges (%)	Europe Total Net Assets (USD billions)	US Expense Ratios (%)	US Total Net Assets (USD billions)	Europe Ongoing Charges (%)	Europe Total Net Assets (USD billions)
2013	0.12	1,086.3	0.40	270.7	0.89	4,829.5	1.56	2,040.8
2014	0.11	1,406.5	0.37	297.9	0.86	5,121.8	1.51	2,080.5
2015	0.10	1,514.8	0.31	326.9	0.84	4,967.0	1.49	2,094.0
2016	0.09	1,832.7	0.32	365.3	0.82	5,097.3	1.44	2,080.3
2017	0.09	2,390.2	0.29	522.5	0.79	6,208.9	1.42	2,745.7
2018	0.07	2,517.1	0.28	524.9	0.74	5,438.9	1.37	2,422.6
2019	0.07	3,342.1	0.28	722.5	0.72	6,648.5	1.35	3,015.9
2020	0.06	3,752.7	0.28	871.9	0.71	7,579.1	1.35	3,722.5
2021	0.06	4,595.2	0.26	1,102.8	0.68	8,643.5	1.32	4,478.1

Notes: "Europe Total Net Assets" includes the European Union and the United Kingdom. Ongoing charges are for EU-domiciled funds, excluding the United Kingdom and the Netherlands, which were markets subject to inducement prohibitions during the period studied and are thus not directly comparable with other European markets. Both expense ratios and ongoing charges are asset-weighted averages.

Sources: Investment Company Institute and Refinitiv.

Exhibit 5. Global Market Share of Active and Passive Funds



Note: The data include mutual funds and exchange-traded funds domiciled in all countries contained in the Refinitiv database.

Source: Refinitiv.

Private equity (PE) is another area of active management with significant investment inflows. Globally, PE AUM reached an all-time high of \$6.3 trillion in 2021, up 38% from 2020.¹⁰ This growth trajectory demonstrates PE's appeal and potential as a source of both outperformance and diversification benefits. Though its higher barriers to entry and legacy structures may make PE a target for fintech disruption, for now, general partners are reaping the rewards.

Automation and Personalization

The nexus between finance and data science is critical not only to the search for talent. AI and machine learning will be integrated into all the core activities of the investment industry—from research and analysis to compliance and customer service.

Robo-advisers, direct index portfolios, and other automated platforms are emerging as critical sources of investment advice. Robo-advisers are projected to reach \$2.76 trillion in AUM in 2023 and \$4.66 trillion by 2027.¹¹ AI and big data investing applications are still at a formative stage, however, and few firms globally have deployed these technologies at scale across their businesses to date.

Similar to robo-advisers, direct indexing offers investors the opportunity to play active roles in their investment portfolios and balance their risk appetite with their personal values. According to Cerulli Associates, direct indexing will grow at a faster rate than ETFs and mutual funds over the next four years, albeit from a much smaller asset base, and will accumulate \$800 billion in total assets in that time frame.¹²

Values-based investing is another developing area of investment management. ESG investing is its most prominent, if at times controversial, iteration, with inflows expected to increase its AUM from \$18.4 trillion in 2021 to \$33.9 trillion by 2026.¹³ According to the CFA Institute Trust Study from 2022, retail investors cite alignment with their personal values as their primary motivation for ESG investing, whereas institutional investors point to the potential for better risk-adjusted returns.¹⁴

Alternative Assets

Although the relative merits of cryptocurrencies and blockchain technology are subject to considerable debate, they have had an undeniable influence on the industry. Cryptocurrencies have persuaded many retail investors to start investing. In fact, cryptocurrencies are the first investible asset for 44% of Gen Z investors.¹⁵ Additionally, fiat-backed stablecoins and central bank digital currencies could increase the legitimacy of cryptocurrencies and help reduce volatility. Indeed, more than 110 countries, representing over 95% of global GDP,¹⁶ are exploring a central bank digital currency offering.¹⁷

Blockchain technology could disrupt various systems and services. Through real-time settlement and smart contracts, it could revolutionize record-keeping and compliance operations. Legacy structures and practices in the highly regulated financial services industry, however, do present sizable obstacles to wider uptake.

Tokenization also has transformative potential. Through tokenization, infrastructure, real estate, and other previously indivisible alternative assets can be divided and securitized for investment purposes.

¹⁰McKinsey & Company, "Private Markets Rally to New Heights" (March 2022). www.mckinsey.com/~/media/mckinsey/industries/private%20equity%20and%20principal%20investors/our%20insights/mckinseys%20private%20markets%20annual%20review/2022/mckinseys-private-markets-annual-review-private-markets-rally-to-new-heights-vf.pdf.

¹¹Statista, "Robo-Advisors – Worldwide" (retrieved 5 April 2023). www.statista.com/outlook/dmo/fintech/digital-investment/robo-advisors/worldwide.

¹²Cerulli Associates, "The Case for Direct Indexing: Differentiation in a Competitive Marketplace" (1 December 2022). www.cerulli.com/resource/white-paper-the-case-for-direct-indexing.

¹³See <https://corpgov.law.harvard.edu/2022/11/17/exponential-expectations-for-esg>.

¹⁴CFA Institute, "Enhancing Investors' Trust."

¹⁵FINRA Investor Education Foundation and CFA Institute, "Gen Z and Investing: Social Media, Crypto, FOMO, and Family" (23 May 2023). <https://rpc.cfainstitute.org/research/reports/2023/gen-z-investing>.

¹⁶Atlantic Council, Central Bank Digital Currency (CBDC) Tracker. www.atlanticcouncil.org/cbdctracker/.

¹⁷For more information on central bank digital currencies, visit: <https://rpc.cfainstitute.org/research/surveys/2023/survey-central-bank-digital-currencies>.

EVALUATION OF THE 2017 SCENARIOS

In our "Future State of the Investment Profession" report, we theorized that the Fintech Disruption, Parallel Worlds, Lower for Longer, and Purposeful Capitalism scenarios would shape the industry over the medium term. These narratives sought to inform industry stakeholders about the forces of change coming to the sector and how to incorporate these factors into their business strategies.

How have these scenarios played out since 2017, and how did they anticipate our new scenarios?

Fintech Disruption

This scenario envisioned smart machines and systems and enhanced data analytical capabilities playing disruptive roles in the evolution of finance. In the intervening six years, although fintech has guided the development of financial services, not much creative destruction has occurred: Tech solutions by new entrants mostly complemented rather than displaced traditional players in a "fin + tech" scenario. Rather than compete in a crowded and highly regulated marketplace, new entrants have partnered with established firms or targeted gaps in the marketplace where new products or tech-driven solutions could address unmet demand.

As a result, the most disruptive technologies have not been those we anticipated in 2017. Automated investment advice, or robo-advice, for example, has targeted the underserved mass market segment, complementing rather than competing with traditional private wealth provision targeted at high-net-worth investors. Blockchain's use cases have expanded into smart contracts and tokenization of previously inaccessible markets or new asset classes (such as nonfungible tokens). AI and big data, however, have had a larger-than-anticipated influence, with firms seeking to apply them across the investment management value chain. Fintech Disruption has given way to Digital Transformation.

Parallel Worlds

This scenario described how various markets, generations, and social groups would engage with financial services in different ways. Greater access to investment markets and products would combine with greater demand for simplicity, personalization, and speed.

This scenario continues to unfold. Low-cost mobile investment platforms and improved banking and payment applications have increased baseline participation in financial services across the board, while thematic products, direct indexing, and custom portfolios have opened the door to greater personalization. Deglobalization, however, may slow progress on these fronts. Indeed, the Parallel Worlds scenario seems to be evolving into Diverging Worlds.

Lower for Longer

This scenario anticipated a "new normal" of low interest rates and low growth with attendant challenges for such things as asset allocation and the provision of pensions. The ultra-accommodative monetary policies that followed the global financial crisis helped support asset prices for more than a decade as passive investment products grew in popularity. This trend continued after 2017, providing the backdrop for financial markets during the ensuing five years. As inflationary pressures emerged in the second half of 2021, however, central banks hiked interest rates and brought the secular bull market in government bonds and other long-duration assets to a close. This regime change will transform risk and return expectations, asset allocation, and fund flows. We examine the implications in the scenario The End of Cheap Money.

Purposeful Capitalism

This scenario set out a positive vision for how capitalism would evolve, with investment firms embracing client-centric operations and organizational cultures and placing ethics, professionalism, and purpose at the core of their business models. It also anticipated that firms would focus on stakeholder and shareholder considerations and recognize asset owners' growing influence on long-term value creation and sustainability objectives. Purposeful Capitalism is an aspirational state for the investment industry and thus a work in progress. Firms now devote more resources to ESG considerations, yet the wider finance sector's incorporation of sustainability faces a number of challenges. We examine these issues in the Sustainable Finance scenario.

We concluded the 2017 study by mapping out the investment industry's future state along two dimensions: benefits to the industry and benefits

to society, illustrated in **Exhibit 6**. The top right quadrant—labeled “professional industry”—is the most desirable state, wherein investment management delivers greater benefits to both the industry and society through aligned values and incentives. Our thesis was that reaching this state would depend on how the industry responded to the scenarios and whether it could build and sustain trust among clients and society at large.

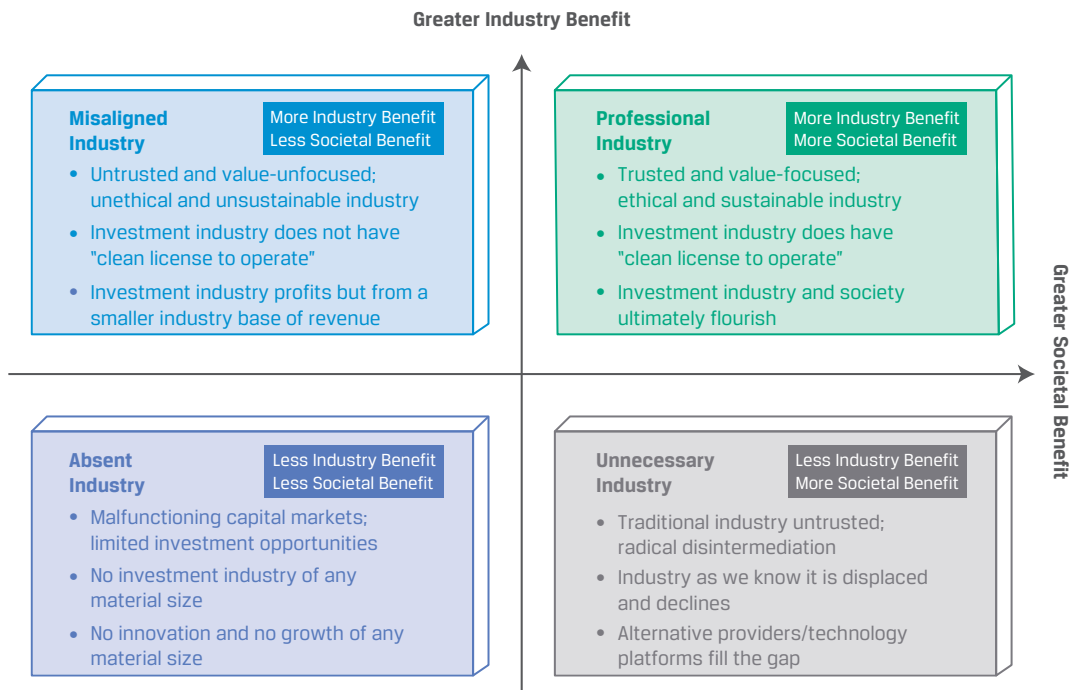
Although the investment industry has progressed toward greater societal benefit, today it faces a proverbial fork in the road. One path continues toward the hoped-for “professional industry” state, and the other, toward the “unnecessary industry” state. Either result should constitute a net societal benefit. The latter path means radical disintermediation and

creative destruction of traditional finance as current industry structures and practices risk obsolescence and displacement in the face of new entrants and technologies. The rise of cryptoassets and their popularity among young investors, along with the potential of decentralized finance (DeFi), suggest that such an outcome is quite possible.

Can these two states coexist and complement one another, or will one eclipse and displace the other? This is a key question facing the investment industry, one that challenges the industry to prove its worth to society over the next 5–10 years. A flourishing and professional investment industry will emerge only by streamlining the value chain, eliminating unnecessary intermediation, and embracing those new technologies that best serve clients.

.....

Exhibit 6. Four States for the Relationship between Investment Management and Society (2017)



Source: CFA Institute, “Future State of the Investment Profession.”

2023 MEGATRENDS AND SCENARIOS OVERVIEW

The Art of Scenario Planning

As we observed in "Future State of the Investment Profession," even when forecasts are directionally correct, they are often specifically wrong. After all, the future of finance is determined by countless moving parts and the outcomes of various, complex interactions, making it impossible to predict with precision. Consequently, we use scenario planning to reveal insights about the future state of the industry, regardless of what version of the future unfolds.

Our scenarios draw on various megatrends—large-scale, omnipresent changes with global implications—that are certain to disrupt the financial ecosystem and reshape both the industry and society as a whole.

Viewed through the lens of finance, these megatrends inform the narrative scenarios through which we frame the critical issues for industry leaders. Our time frame of 5–10 years is long enough for business models to substantively adapt but not so long as to enter the realm of science fiction. **Exhibit 7** shows the mapping of megatrends to scenarios.

In this report, the extra-financial factors that will affect society are overlaid with the finance-specific forces of innovation. How these phenomena will interact and influence one another is key to developing each scenario.

The same megatrends all flow into each scenario, but the narratives differ according to which forces are preeminent.

Megatrends

Shifting Demographics

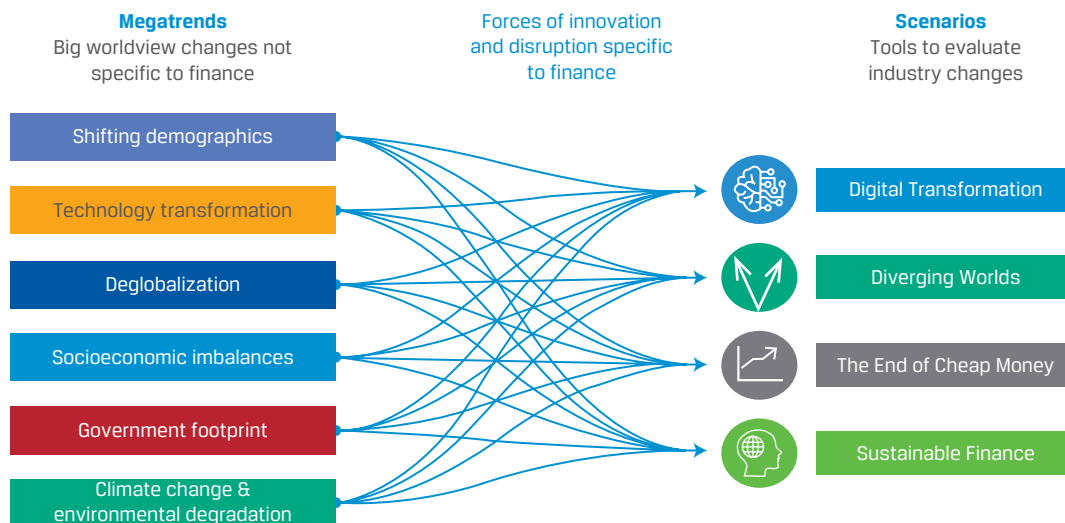
Large-scale global demographic trends will alter societal structures and capital markets. Over the next 5–10 years, we expect the following transitions:

Global population shifts: Negative replacement rates are the norm for Western Europe, China, Japan, and other mature markets where aging populations strain retirement systems and social safety nets. India may have already surpassed China as the world's most populous country. Companies struggle to fill open positions as retirees outnumber workers. Africa's population grows significantly.

Urbanization: Populations migrate to cities, leading to a "brain drain" in rural areas. Urbanization necessitates more infrastructure investment to counter climate change and equip cities for the future. The built environment accounts for an estimated 40% of annual CO2 emissions.¹⁸



Exhibit 7. Megatrends Combine for Possible Futures



¹⁸Architecture 2030, "The Built Environment." Retrieved 17 July 2023. <https://architecture2030.org/why-the-building-sector/>.

Millennial wealth: As the last wave of baby boomers reaches retirement age, millennials likely become the largest asset-holding generation by the mid-2030s. In the medium term, the investor base and asset mix will evolve as this transition unfolds.

Technology Transformation

Technological progress continues to change how we live, work, innovate, and communicate. Technology-focused skills become ever more critical as job roles and tasks undergo transition.

Data: Access to new and better data transforms and improves decision-making processes.

Artificial intelligence and machine learning: Techniques are refined and embedded across more applications. A new generation of talent develops. Advances in automation accelerate changes to the world of work, and the expansion of generative AI boosts productivity. Some job roles are eliminated, and new ones are created as businesses harness the combined power of AI and HI.

Tokenization: New investment opportunities emerge through tokenization of new asset classes and previously hard-to-access alternative investments.

Digital natives: Gen Z and younger millennials—those who have grown up with smartphones and social media—begin to replace retiring baby boomers and bring greater technological sophistication to the workforce.

Social media: Social media-fueled polarization grows and creates echo chambers of self-perpetuating viewpoints.

Personalization: Products and services become increasingly individualized and "mobile-first," creating greater utility for consumers and better customer insights for businesses.

Deglobalization

Geopolitical tension, the aftermath of COVID 19-related disruptions, and rising populist movements contribute to a retreat from global supply chains and international trade agreements.

Geo-economic competition: The shift from economic cooperation to competition intensifies. Concerns over intellectual property, energy security, and net-zero goals heighten tensions. Tariffs and subsidies continue to impede international trade and distort capital flows.

Supply chain pressures: Labor and material costs rise. Interest rates become more variable amid reduced overseas trade and brittle supply chains. Automation in manufacturing becomes more economically attractive. On-shoring becomes more attractive as a means to address supply chain challenges.

Institutional trust: Confidence in the mandates and credibility of longstanding multilateral institutions wanes as geopolitical fault lines grow. Global organizations are challenged to evolve.

Domestic innovation: Investment in 3D printing and manufacturing technologies reduces reliance on international trade but creates unequal impacts in different markets.

Socioeconomic Imbalances

Wealth and income disparities increase as the disproportionate effects of climate change, technological innovation, automation, and inflation limit the economic mobility of lower- and middle-income cohorts.

Economic inequality: As fiscal stimulus subsides, the potential for anticapitalism backlash grows. Climate change and inflation disproportionately affect less affluent households, accentuating class divides.

Diversity, equity, and inclusion (DEI): DEI metrics and accountability are embraced across the corporate world. Societies strive to become more inclusive, although the pace of progress varies, and polarization presents persistent headwinds.

Identities and affiliations: Networks and communities are reset in a hybrid world. Building inclusive cultures amid diverging perspectives and identities grows increasingly challenging.

Government Footprint

Political roadblocks impede effective regulations. Consequently, consensus is harder to achieve and slower to materialize. Governments struggle to legislate effectively amid deglobalization, political polarization, ongoing technological transformation, and other challenges.

Collaboration: Despite greater recognition of the need for wider cooperation to meet net-zero targets, among other goals, the strain of geopolitical competition makes actual collaboration more difficult.

Complexity: Rapid technological innovations lead to new and lightly regulated products and services. Regulators struggle to apply existing laws and

establish new frameworks. The ubiquity of data and the ease with which data are transmitted make effective regulation difficult. The resulting uncertainty and regulatory risks underscore the need for cooperation.

Climate Change and Environmental Degradation

Climate change mitigation proves difficult, but popular support for a more sustainable world remains strong. Global efforts are impeded, however, by nationalist sentiment and widespread distrust.

Net zero: Politicization, greenwashing, and other factors jeopardize progress toward net-zero goals in the near term. Efforts to reduce carbon emissions accelerate as the 2030 and 2050 target dates approach, given limited near-term progress.

Climate: Climate change–related disasters occur with alarming frequency, with material effects on quality of life. Investment in climate change adaptation and mitigation lags before accelerating.

Shareholder engagement: To offset short-termism, shareholder engagement uses corporate voting power to improve societal outcomes and the economy.

Combination of Megatrends Leads to Scenarios

Although each megatrend is tangible and impactful in its own right, how they intersect, interact, and coalesce has even broader ramifications. How each megatrend influences each scenario and to what degree varies, but our four scenarios all lie at the nexus of multiple megatrends.

Diverging Worlds examines the push and pull between the opportunities for the investment

industry to better serve investors and the challenges posed by extra-financial headwinds. Technological innovation enables greater access to and greater personalization of investment products across investor cohorts and markets. Demographic shifts create new capital flows and empower a new generation of investors. The challenges lie in mitigating the trajectory of inequality and deglobalization to maintain institutional trust and spur economic development.

Sustainable Finance considers how climate change and environmental degradation will transform society and the roles government and regulation can play in mitigating their effects. Much of the business sector and investment industry takes a multistakeholder perspective. The industry is challenged to balance impact with returns; new business models, investment models, and measurement models emerge in the face of increasing political polarization.

Digital Transformation highlights how big data, generative AI, machine learning, and other innovations will shape investment management in the years ahead. Such technology will proliferate in the investment process as nascent talent enters an industry where the supply of such skills is limited and thus in high demand. The boost to productivity from these new technologies provides support to economic growth in the face of wider macroeconomic headwinds. Products become more sophisticated as the talent focus for the industry shifts toward a hybrid AI-HI model.

The End of Cheap Money explores how the megatrends intersect with the current macroeconomic landscape. Higher interest rates, inflation, and market volatility create a more challenging environment for economic growth and act as a counterweight to productivity gains from AI technologies. Governments and regulators attempt to carefully balance the removal of stimulus with efforts to bolster growth. Opportunities emerge for new investment products, and there is a renewed appetite for active management.

DIVERGING WORLDS

The world has never been homogeneous. We are a collection of unique perspectives, with different needs and aspirations. The divides created by demographics, belief systems, wealth, and socioeconomic status, however, are widening. Widespread social media, fueled by a relentless news cycle, has enabled a state of quasi-isolation wherein many people retreat into echo chambers with those of like-minded views.

In investment management, this shift from the collective toward the individual manifests in the growth of personalized products and services. Investments are not only a means of wealth accumulation but also of personal expression—of values and beliefs—among different investor segments. In the face of an already gloomy outlook—the International Monetary Fund (IMF) states that global economic growth estimates from 2022 to 2024 remain significantly below pre-COVID-19 averages, with advanced economies leading the decline¹⁹—these trends are likely to constitute headwinds for the capital markets. Firms face pressure to build better products and deliver greater value to clients amid a more difficult macroeconomic backdrop.

Deglobalization, inequality, demographic shifts, and advancements in technology define the Diverging

Worlds scenario. These trends highlight the myriad ways in which investment industry participants engage with financial markets and underscore the complexity of a rapidly evolving economy and marketplace. Amid greater polarization and a challenging economic environment, Diverging Worlds results in increasingly diverse perspectives on the role of financial markets, capitalism, and investment management in the next 5–10 years.

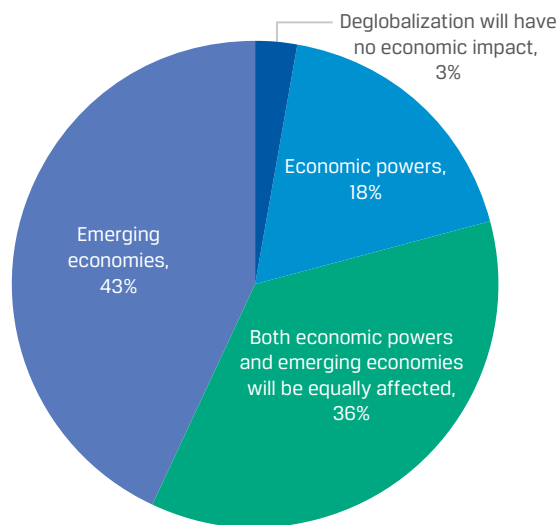
Deglobalization: The Unraveling

Deglobalization's downstream effects influence economic progress in the near term. The COVID-19 pandemic and the Russia-Ukraine War lead a global rethink as nations reconsider their trading partnerships and shore up domestic production capabilities to better control their own economic destinies. The results of such insular behavior vary, however: According to survey respondents, deglobalization will be less disruptive for traditional economic powers, whose size and stability shield them from economic headwinds (see **Exhibit 8**) relative to emerging markets.



Exhibit 8. Impact of Deglobalization on Economic Powers and Emerging Economies

The impact of deglobalization will be most disruptive for: (N = 1,330)



¹⁹IMF, "Inflation Outlook Peaking amid Low Growth" (January 2023).

Greater reliance on domestic resources and manufacturing as well as streamlined trade partnerships accentuate the divide between resource-rich countries and those that depend on commodity imports. Access to human capital from overseas may decrease or grow more expensive. This development, coupled with onshoring, would increase costs. A diverging and more deglobalized world is more inflationary, with greater variability in asset prices and economic growth prospects across markets.

According to our survey, respondents expect more geopolitical tension, higher inflation, and increased market volatility, as well as reduced GDP and lower supply chain efficiency (see **Exhibit 9**). Together, these factors lead to higher prices and production costs and decreased purchasing power and innovation.²⁰ However, greater focus on domestic manufacturing and renewable/alternative energy investment could improve employment rates. This dynamic also creates opportunities for new ventures and business models to emerge, including in green technologies, which may positively affect sustainability outcomes. The promise of more autonomy can also make deglobalization popular.

A More Unequal World?

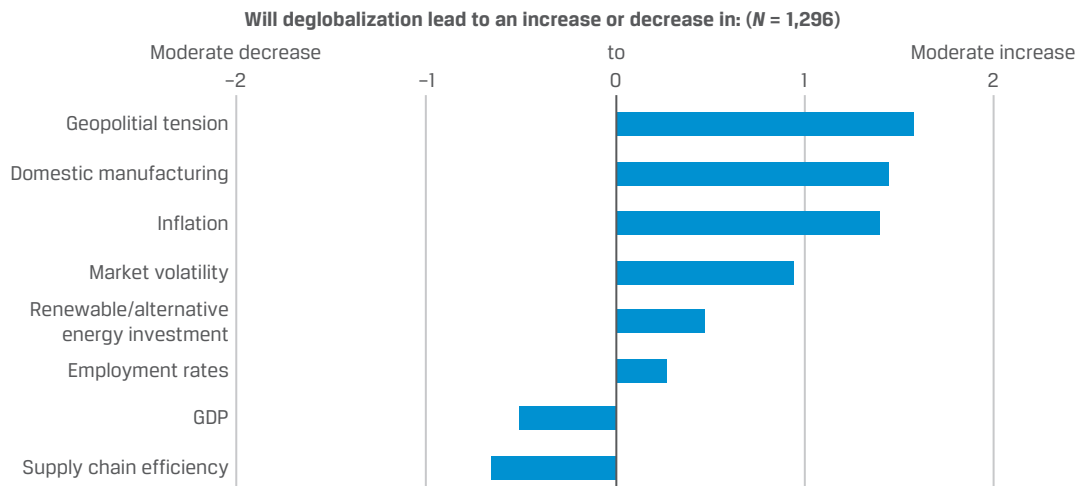
Like deglobalization, increasing inequality reduces economic efficiency. The OECD found that "when income inequality rises, economic growth falls."²¹ This is a concern for investment professionals globally, as shown in **Exhibit 10**.

Rising inequality leads "individuals to switch to more risk-averse [investment] strategies."²² Sustained over the long run, this phenomenon may keep investors from realizing their goals and reduce investment in small and medium-sized enterprises (SMEs), the backbone of most economies. An increase in inequality has negative ramifications at both the macro and micro levels.

Capitalism and financial markets contribute to increased inequality, according to survey respondents (see **Exhibit 11**). The primacy of the traditional shareholder-centric profit model wanes, particularly among younger cohorts.²³ Polarization jeopardizes otherwise successful efforts to overhaul capitalism in favor of a multistakeholder model; political backlash against conscious and inclusive



Exhibit 9. Effects of Deglobalization on Key Economic Indicators



Note: Response options ranged from -3 (significant decrease relative to today) to +3 (significant increase relative to today).

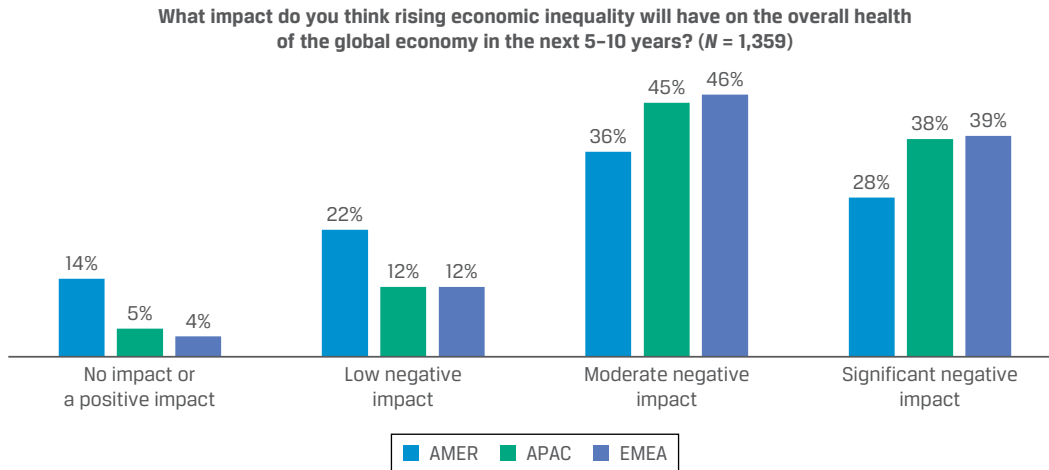
²⁰Ira Kalish, "Economic Brief: How Supply Chains Could Adapt to Deglobalization," *CFI Journal*, Deloitte (30 March 2022). <https://deloitte.wsj.com/articles/economic-brief-how-supply-chains-could-adapt-to-deglobalization-01648666628?tesla=y&tesla=y>.

²¹OECD, "In It Together: Why Less Inequality Benefits All" (Paris: OECD Publishing, 2015). www.oecd-ilibrary.org/employment/in-it-together-why-less-inequality-benefits-all_9789264235120-en.

²²Alexander J. Stewart, Nolan McCarty, and Joanna J. Bryson, "Polarization under Rising Inequality and Economic Decline," *Science Advances* (11 December 2020). www.science.org/doi/10.1126/sciadv.abd4201.

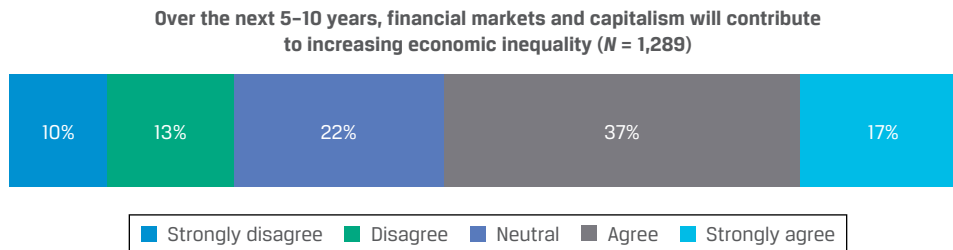
²³Pew Research Center, "Modest Declines in Positive Views of 'Socialism' and 'Capitalism' in U.S." (19 September 2022). www.pewresearch.org/politics/2022/09/19/modest-declines-in-positive-views-of-socialism-and-capitalism-in-u-s/.

Exhibit 10. Effect of Rising Economic Inequality on Global Economic Health



Note: AMER = Americas; APAC = Asia Pacific; EMEA = Europe, the Middle East, and Africa.

Exhibit 11. Impact of Financial Markets and Capitalism on Economic Inequality



Note: Percentages may not sum to 100% because of rounding.

capitalism disincentivizes companies from pursuing extra-financial returns. In Diverging Worlds, capitalism evolves unevenly as different models and maxims emerge across different markets and social groups.

A Demographic Dividend?

Demographics are intertwined with inequality and financial market access in the Diverging Worlds scenario. Aging populations, particularly in developed economies,²⁴ strain social safety nets and pension schemes. According to the "Enhancing Investors' Trust" study, 59% of survey respondents believe that it is "likely" or "very likely" that defined benefit

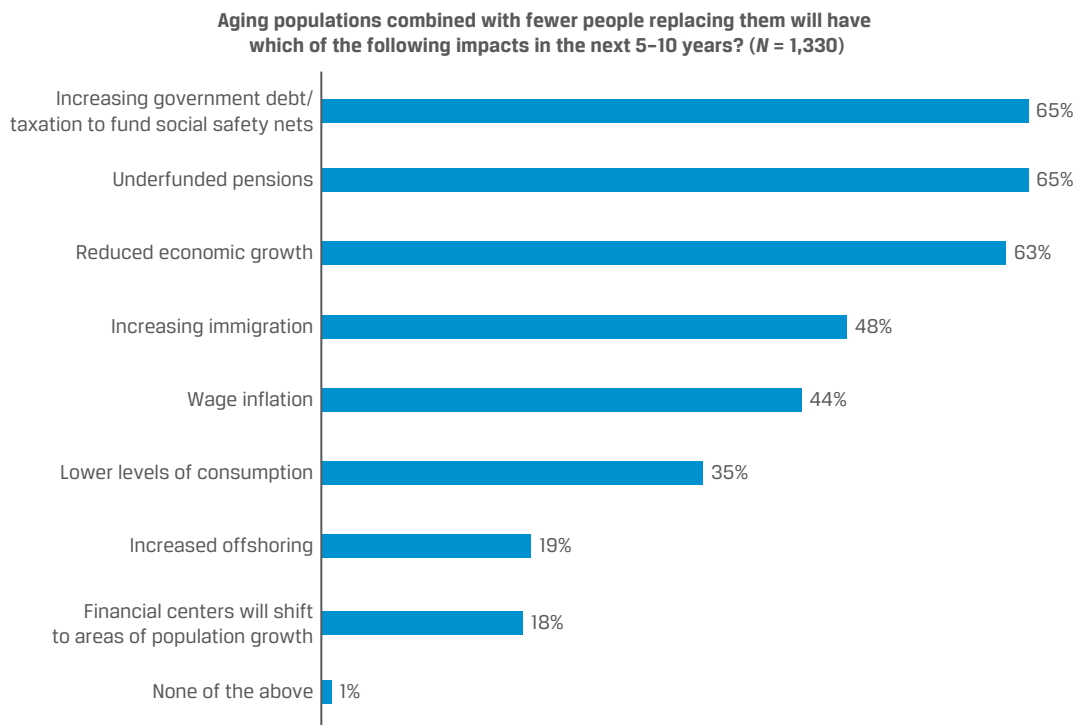
pension plans will need to adjust benefits downward over the next 10 years.²⁵ Reductions in pledged benefits inhibit economic progress as institutional trust degrades and governments struggle to support older populations (see **Exhibit 12**).

The geographic dimension of the larger demographic disruption further upends investment management and transforms the global investment landscape. Mature economies have slowing and sometimes negative population growth rates, while emerging markets experience population booms. China's population has plateaued, and India's is poised to become the world's largest. Africa is growing incredibly quickly, with Nigeria on track to become the world's third most populous nation by the middle

²⁴David E. Bloom, "Population 2020," *Finance & Development*, IMF (March 2020). www.imf.org/en/Publications/fandd/issues/2020/03/changing-demographics-and-economic-growth-bloom.

²⁵CFA Institute, "Enhancing Investors' Trust."

Exhibit 12. Impact of Aging Populations on Economic Factors



of the century.²⁶ These trends are spurring rapid urbanization: By 2050, 70% of the global population is expected to live in cities.²⁷

Absent offsetting productivity gains, economies with downward trends in population growth risk corresponding drops in GDP growth.²⁸ Moreover, long-term productivity rates and the sustainability challenges of emerging population centers present further impediments to growth.²⁹ Therefore, investing in emerging markets continues to carry added risk, commensurate with higher expected returns, whereas mature or even "graying" markets experience lower returns and heightened volatility.

The Technology Divide

Technology plays a crucial role in expanding who can access financial markets and how they do so. The tech-fueled "democratization" of finance has lowered the barriers to entry. More financial products and

services are available to more people. Technology has also driven the personalization trend. Direct indexing and individualized investment products can automatically allocate user capital to savings or investment vehicles based on the investor's profile and preferences. Expanded access to private markets and alternative investment options through tokenization, for example, persuade more individuals to become investors.

Despite the advantages that new technology brings (see **Exhibit 13**), AI and other innovations exacerbate the socioeconomic divide in the Diverging Worlds scenario. Many task-oriented jobs are replaced by automation as workers are displaced. Workers shift from production to support roles or out of the workforce altogether. Most survey respondents believe advancements in technology and automation will increase income inequality, potentially offsetting the productivity gains they create (see **Exhibit 14**).

²⁶Bloom, "Population 2020."

²⁷UN75, "Shifting Demographics" (2020). www.un.org/sites/un2.un.org/files/2019/10/un75_shifting_demographics.pdf.

²⁸Jinill Kim, "The Effects of Demographic Change on GDP Growth in OECD Economies," *IFDP Notes* (28 September 2016). www.federalreserve.gov/econresdata/notes/ifdp-notes/2016/effects-of-demographic-change-on-gdp-growth-in-oecd-economies-20160928.html.

²⁹Andrew Mason and Ronald Lee, "Six Ways Population Change Will Affect the Global Economy," *Population and Development Review* (14 February 2022). <https://onlinelibrary.wiley.com/doi/10.1111/padr.12469>.



Exhibit 13. Impact of Personalized Financial Products on Investment Outcomes

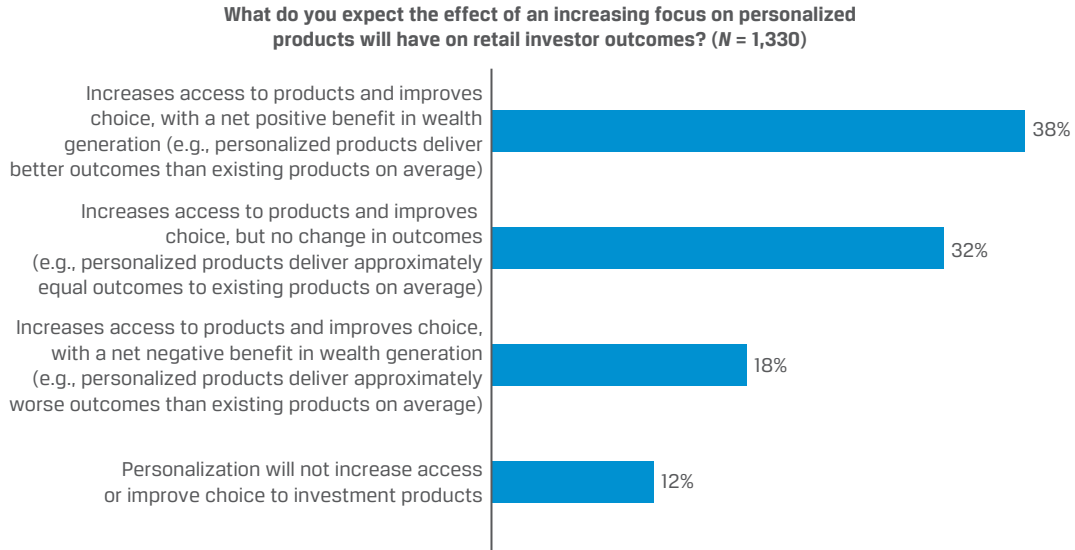
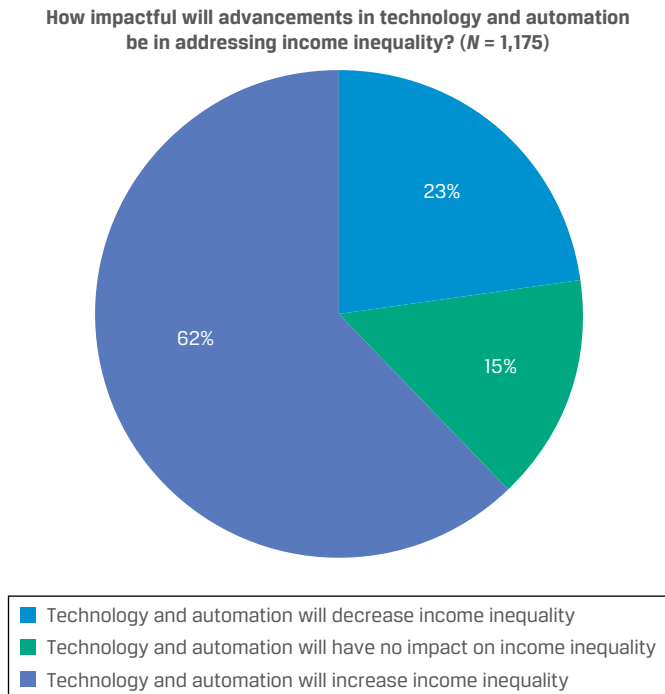


Exhibit 14. Impact of Technology and Automation on Income Inequality



A Cautionary Tale?

Ultimately, the Diverging Worlds scenario emphasizes the need for caution. Demographic trends, enhanced technology, and greater access to new and personalized investment products present great opportunities for investment management and the larger world. In 5–10 years, investors will have more options tailored to their risk and values profile.

In theory, this development should create more efficient investment mechanisms and increase

economic utility. But the trajectory of income inequality and deglobalization could impede economic development. The divergence of our shared experiences will lead to growing distrust and limit our ability to achieve collective progress. To maintain its credibility and have a positive influence on society, the investment management industry must heed this warning and work toward a future built around equal opportunity, fair and open access to markets and products, and ethical values.

Scenario Outcomes

- Trust in public and private institutions erodes as governments and firms contend with increasingly polarized constituencies. Corporate values and purpose become central to gaining clients and attracting top talent.
- Advancements in technology and automation increase financial market participation but have diverging impacts among investor classes. Younger cohorts and "digital natives" more readily embrace new investing tools, products, and platforms but are more exposed to misinformation on social media and other risks that could lead to suboptimal investment decisions and outcomes.
- The people–planet–profit nexus of sustainable investing devolves into diverging camps: those seeking returns benefiting both people and the planet and those solely pursuing the bottom line.
- Proxy voting and corporate engagement grow more contentious as social and political pressures intensify. Polarization comes to the boardroom.
- The politicization of climate change and energy security–related socioeconomic pressures create policy delay on the one hand and competing government subsidies on the other, distorting capital investment.

SUSTAINABLE FINANCE

In the Sustainable Finance scenario, governments, regulators, and the business and finance sectors work toward a more purposeful financial system³⁰ that considers the interests of multiple stakeholders and their stated goals and interpretations of organizational success alongside positive shareholder outcomes over the next 5–10 years.

Politicization and other controversies impede the Sustainable Finance pathway³¹ and create a multi-speed world: Some jurisdictions slow down through regulation and practice, while others accelerate.

Most investors support the incorporation of ESG factors that are material to their portfolio's risks and returns. Others see real-world sustainability impacts as a distinct goal. Of this cohort, most apply impact strategies as a means to achieve better financial outcomes. A smaller proportion pursue impact as an end in its own right.³²

The sustainability debate continues to be influenced by the issue of fiduciary duty. Investors continue to debate the interpretations and applications of this duty. For some, it remains narrowly tied to the shareholder, client, or end investor. Others believe in a more holistic balance that considers the interests of various stakeholders.

A give and take between these two philosophies develops, but gradually the multistakeholder focus gains primacy over the next 5–10 years as businesses embrace a wider purpose alongside their search for profit. Nevertheless, multistakeholder capitalism continues to exist on a spectrum, with certain models staying closer to a shareholder-centric version.

Investment organizations have a very clear takeaway from these trends. To adapt to a world where focus is shifting toward multiple stakeholders, the organizational culture to be nurtured needs to be centered on purpose and aligned to a fiduciary mindset that places client interests at the fore. And investment professionals will need to embed this purpose into

their work, necessitating a deeper understanding of client preferences, values, and motivations.

The Climate Challenge

As the world confronts climate change, resource shortages, and other challenges, businesses and institutions contribute more to sustainable development. For the investment industry, climate change mitigation is a key priority. The 2015 Paris Agreement has set in motion various actions and reactions. The investment industry's initial response has focused on reporting. The principal initiatives from the Task Force on Climate-Related Financial Disclosures (TCFD), the International Sustainability Standards Board, and their forerunners are widely adopted and become reasonably accepted. In the next 5–10 years, investment strategy will evolve to embrace net-zero pathways using science-based methods as framed by the Science Based Targets initiative (SBTi).³³

In the Sustainable Finance scenario, the investment industry exerts an increasingly positive influence on society (see **Exhibit 15**).

Self-serving biases aside, these responses present an encouraging picture. But how will the investment management industry achieve greater positive impact? Stewardship resourcing, growth in innovation in finance, and success with diversity are among the industry's chief levers in the Sustainable Finance scenario.

The last of these three represents a very critical industry step forward. For investment organizations to support this improved impact on society, they will need to strengthen the cultural and structural aspects of diversity and embed inclusion and equitable human capital practices.

Exhibit 16 illuminates the depth of the challenge when it comes to how much value the sector can produce for its stakeholders.

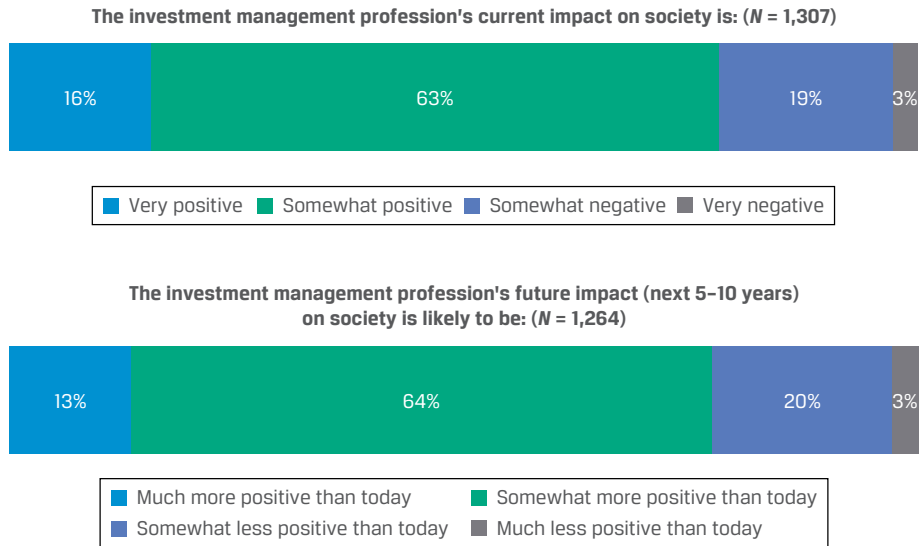
³⁰David Pitt-Watson and Hari Mann, "The Purposeful Corporation and the Role of the Finance Industry," *Journal of the British Academy* (26 August 2022). www.thebritishacademy.ac.uk/documents/4265/JBA-10s5-05-PittWatson-Mann.pdf.

³¹Kenan Institute of Private Enterprise, "Stakeholder Capitalism + ESG Investing" (January 2023). <https://kenaninstitute.unc.edu/wp-content/uploads/2023/01/stakeholder-capitalism-full-01242023r.pdf>.

³²UN Environment Programme Finance Initiative, Principles for Responsible Investment, and Generation Foundation, "A Legal Framework for Impact: Sustainability in Investor Decision-Making." www.unpri.org/policy/a-legal-framework-for-impact/4519.article.

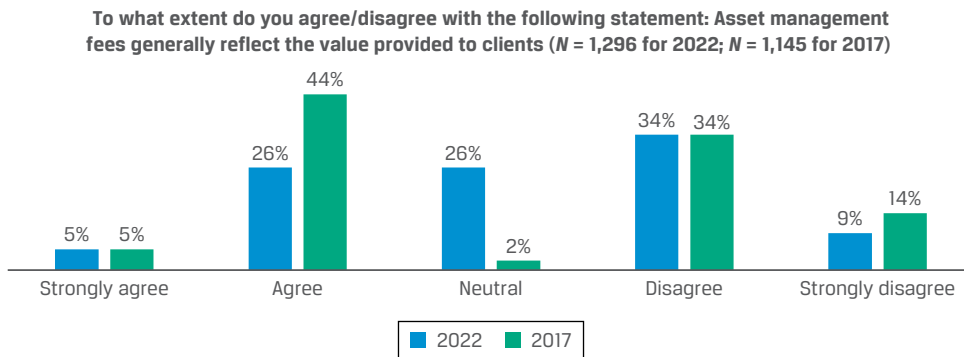
³³Science Based Targets, "Finance Sector: New Guidance on Science-Based Targets and TCFD Reporting" (18 January 2023). <https://sciencebasedtargets.org/blog/finance-sector-new-guidance-on-science-based-targets-and-tcdf-reporting>.

Exhibit 15. Investment Management's Impact on Society



Note: Percentages may not sum to 100% because of rounding.

Exhibit 16. Do Asset Management Fees Reflect the Value Provided?



Note: Percentages may not sum to 100% because of rounding.

More than half of respondents are neutral or negative about whether asset management fees are generally commensurate with the value provided to clients, down slightly from the results of our 2017 survey. This period has coincided with a downward trend in asset management fees,³⁴ as illustrated previously in Exhibit 4.

Many are skeptical about the industry's influence, a point that Exhibit 11 emphasizes: More than half of respondents agree or strongly agree that financial

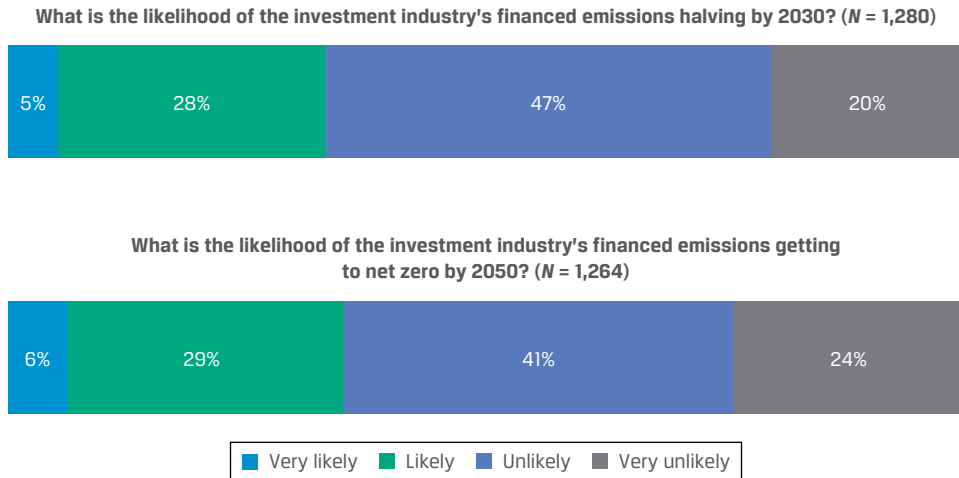
markets and capitalism will contribute to economic inequality over the next 5-10 years.

This lack of confidence in the industry's value proposition is demonstrated acutely in expectations on climate impact. Only one in three respondents believes that the investment industry will achieve net zero in its financed emissions by 2050. A similarly small cohort believes it will halve financed emissions by 2030 (see **Exhibit 17**).

³⁴Chris McIntyre, Simon Bartletta, Ishaan Bhattacharya, Joe Carrubba, Dean Frankle, Marcos Frazao, Lubasha Heredia, Hanka Mörstedt, Kedra Newsom Reeves, Edoardo Palmisani, Neil Pardasani, Martin Reeves, Thomas Schulte, Benjamin Sheridan, Blaine Slack, and Kevin Zhu, "From Tailwinds to Turbulence" Boston Consulting Group (25 May 2022). <https://www.bcg.com/publications/2022/tailwinds-to-turbulence-for-global-assets-under-management>.



Exhibit 17. The Investment Industry's Net-Zero Ambitions



An Industry Transformed?

These disparate perspectives—of an investment industry poised to make more positive contributions while charging more than the value it delivers and failing to meet its environmental commitments—represent a sector at an inflection point. In Sustainable Finance, the investment industry fulfills its promise as a "professional industry"—see Exhibit 6—as investors and institutions largely adapt their business models to contribute to positive real-world outcomes, with effective stewardship practices as the key enabler.

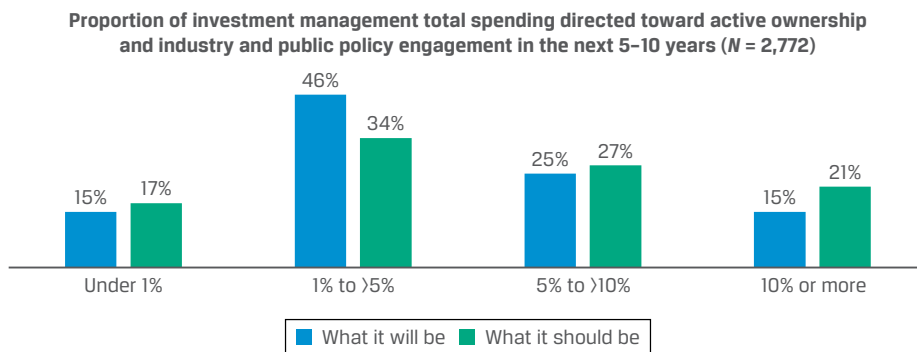
Investment organizations will succeed with this stewardship challenge only with a considerable increase in resources devoted to it. In addition, success will require an evolved stewardship business

model committing firms to greater collaboration and expanded engagement with coalition organizations to address the complex system-wide challenges of the industry and the real world.

Fulfilling its promise entails the investment industry positively contributing to climate change mitigation through the net-zero transition. High-emission companies adapt their business models to a low-carbon future as the investment industry dedicates more resources to ownership and stewardship activities (see Exhibit 18). Social factors also take on added importance. These include diversity and human capital development in workforces, paying decent wages, contributing to communities, dealing fairly with suppliers, disclosing political and labor union management activities and contributions, and holding suppliers accountable in their labor practices.



Exhibit 18. Investment Management Stewardship Practices



Note: Percentages may not sum to 100% because of rounding.

The evolution we envision in Sustainable Finance reflects how individual organizations respond to their social license to operate.³⁵ That is, the privileges society grants to investment professionals (e.g., opportunities to build flourishing businesses) are contingent on the latter realizing certain socially valued goals (e.g., limiting environmental damage or doing no harm). In Sustainable Finance, investors help guide this evolution through their influence on

the cost of capital, through their engagement both at the entity and industry levels, and by embedding more holistic integration of sustainability risks and opportunities. In these evolving best practices, investment organizations need to incorporate much longer time horizons than in prior times and ensure that the benchmarks used and the attendant incentives are fully aligned to fiduciary duty and sustainable outcomes.

Scenario Outcomes

- Investing techniques grow more consistent with the Paris Agreement as the investment industry prioritizes net-zero pathways through new metrics, business models, and investment models.
- ESG considerations become integral to risk management and regulatory framing. Stewardship expands its influence and increasingly involves industry-level actions and public policy engagement as the Principles for Responsible Investment and Climate Action 100+, among other initiatives, encourage greater collaboration between industry stakeholders.
- The investment industry integrates sustainability, particularly climate change mitigation and standard setting, into its regulatory focus. The reporting of emissions by reference to precise standards is mandated widely. Accounting practices embrace materiality (information about ESG impacts on the firm), with double materiality—adding in information about a firm's impact on the world at large—being the ultimate goal.
- Investment strategies increase their emphasis on social factors—in particular, labor rights, supply chain oversight, DEI practices, and social equality—more broadly.
- The public demands investment organizations differentiate themselves through values and culture.
- Investment professionals must expand their skill sets to be conversant with ESG analysis, with a particular emphasis on climate change and the net-zero challenge.

³⁵Hugh Breakey, "Understanding the Social Licence to Operate," *Law Futures Centre Blog*, Griffith University (3 August 2021). <https://blogs.griffith.edu.au/law-futures-centre/2021/08/03/understanding-the-social-licence-to-operate/>.

DIGITAL TRANSFORMATION

The core tenet of the Digital Transformation scenario is that the investment industry will undergo a significant shift from being technology supported to technology driven. As new tools and analytical methods lead to efficiency gains, the industry will enter a transformational phase of product creation and innovation.

The application of AI and big data at scale and throughout many industry processes will be among the most impactful developments guiding this scenario. AI and big data tools are already deployed across the investment management value chain and will come into ever wider use in the years ahead. How firms and professionals apply such technology, particularly in harnessing the combinatorial power and complementary skills of humans and machines on investment teams, will determine organizational success. Professionals who understand the opportunities brought about by new technologies and data, and who can identify where and how these advances can be best deployed to serve client objectives, will be in high demand.

Digital Transformation also encompasses new technology-enabled products and the platforms that cater to them. Tokenization, for example, offers investors access to alternative assets and other previously illiquid investment opportunities, whereas direct indexing, custom portfolios, and other personalized products open new pathways for the industry's evolution. Another theme of digital transformation centers on financial information, social media's role in investment decision making, and the rise of retail trading apps and digital engagement practices.

Artificial Intelligence and Big Data

Large language models (LLMs), such as ChatGPT, will continue to push the boundaries of AI, while other analytical methods from the broader domain of financial data science and machine learning will inform financial instrument selection and portfolio allocation in the next 5–10 years as investment professionals more fully integrate these tools into the investment process.

How well these technologies guide decision making currently depends on the skills of their human

counterparts and the degree to which they leverage data science and investment expertise. ChatGPT, Bard, and other generative AI applications could fundamentally change the way professionals execute certain responsibilities, however, and necessitate a re-evaluation of the types of skills the industry will need in the future. Generative AI's potential to transform the investment workflow makes it fundamentally different from early-stage fintech applications (such as automated investment advice), which worked to mostly complement rather than disrupt existing financial service provision.

Trained on billions of parameters, LLMs can significantly increase labor productivity.³⁶ They summarize reports, write documents, suggest creative ideas, generate computer code for investment applications, and may greatly expand the workflow capacity of investment professionals. By outsourcing many time-consuming, repetitive, and complex tasks to machines, these capabilities—and new ones that are likely in the pipeline—could also enable investment professionals to conduct deeper and more sophisticated analysis. These LLMs also carry certain risks, however, including legal and compliance risks, making public versions of the software unsuitable for certain business applications.

Overall, generative AI tools can serve as a knowledge and computational aid to human capabilities and may accelerate the ongoing transformation of the workplace. Although the AI + HI equation is, for the most part, complementary, generative AI could take labor share from humans and create some redundancies.

Respondents to the Future State of the Investment Industry survey largely believe that HI and AI are mostly complementary rather than substitutable overall: 56% say that their firms are using AI and big data solutions in data analysis, but only 26% say the same for decision making (see **Exhibit 19**). The survey results indicate a more symbiotic relationship between AI/big data and HI—45% of respondents say that such technology allows staff to engage in more productive activities, while only 22% report that AI and big data adoption leads to reduced headcount (see **Exhibit 20**).

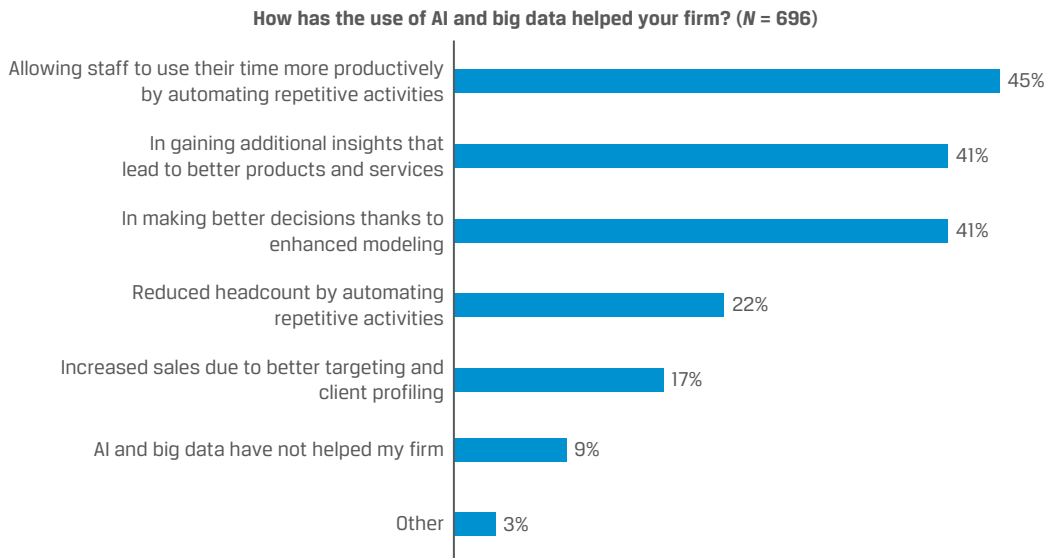
Ultimately, the extent of AI implementation and integration across the business lines of investment management firms will vary.

³⁶See, for example, Bryce Elder, "Surrender Your Desk Job to the AI Productivity Miracle, Says Goldman Sachs," *Financial Times* (27 March 2023). www.ft.com/content/50b15701-855a-4788-9a4b-5a0a9ee10561.

Exhibit 19. Application of AI across Investment Management Organization Business Units



Exhibit 20. Use Cases for AI and Big Data



Where and how firms decide to focus their AI efforts will be a key differentiator. The various ways firms have already deployed AI and big data speak to the depth and breadth of their potential (see Exhibit 20). Through this diversity of AI application, generative AI could be a significant disruptor to today’s status quo. These applications reduce the cost, time, and skill set needed to perform complicated tasks, such as pattern identification, algorithm creation, and data cleaning and analysis. The adoption rate of AI tools across business units and investment organizations will likely increase significantly simply by lowering barriers to entry

and reducing the penalties—development time, talent acquisition expense, investment in new technology products—for testing how AI can work in a given firm.

An Expanding Universe of Asset Classes and Products

Digital assets are integral to the Digital Transformation scenario. Blockchain technology and cryptographic techniques are the building blocks of tokenized alternative assets, including

cryptocurrencies, central bank digital currencies, fiat-backed stable coins, and nonfungible tokens (NFTs). These new asset classes will further increase the appeal for investing and make it more accessible to new entrants. Cryptocurrencies, for example, are already the first investible asset for 44% of Gen Z investors.³⁷ Although tokenization of illiquid assets is still in its nascent stages, the portfolio diversification opportunities offered through investments in real estate, art, private markets, and other previously niche areas will continue to expand as trust in blockchain technology grows.

Personalization and greater access to new and existing investment products are derivatives of the technology-fueled shift in investment product design. Direct indexing, values-based investment portfolios, and other innovations will continue to grow in popularity as technology platforms create more customized solutions for investors. Survey respondents anticipate that demand for such personalized products and access to alternatives will be central themes of new product development (see **Exhibit 21**).

More investment products that better align with the risk and values profiles of investors will better serve

the investor base, yield greater societal benefit, and strengthen support for the industry as a whole.

As investment product life cycles accelerate, firms and professionals must embrace innovation and embed creative thinking, teamwork, and ethics into product development. Innovation capabilities should strengthen through greater resourcing and stronger governance structures surrounding responsible uses of technology.

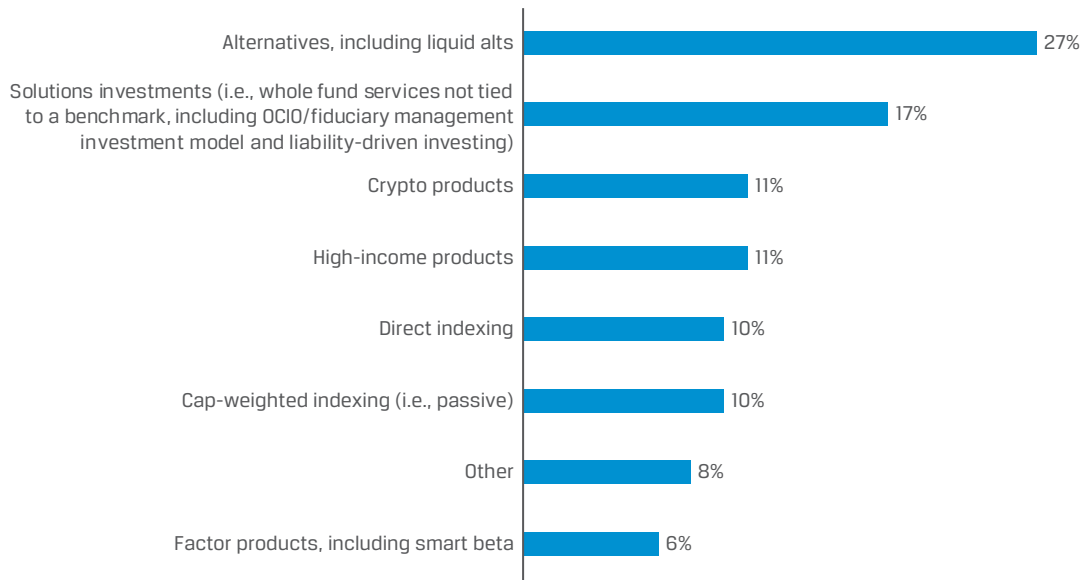
Information and Influence in the Digital World

Another facet of Digital Transformation—an abundance of new sources of information—will introduce novel ways for investors and investment professionals to interact. Social media is the primary source of information about investing and financial topics for 48% of Gen Z investors.³⁸ In particular, financial influencers, or "finfluencers," have an outsized presence on the frontlines of investment marketing, thanks largely to their social media profiles. Although social media platforms are helpful points of access for financial information, they can also lead to herding behavior and other excesses. Moreover, "finfluencers"



Exhibit 21. Key Areas of Product Growth in the Next 5–10 Years

In the next 5–10 years, the strongest growth in product demand will be: (N = 2,631)



Note: OCIO stands for outsourced chief investment officer.

³⁷FINRA Investor Education Foundation and CFA Institute, "Gen Z and Investing."

³⁸FINRA Investor Education Foundation and CFA Institute, "Gen Z and Investing."

may be unqualified to provide investment advice and do not always disclose when they are promoting certain investment products or represent a particular financial firm.

Investing apps are another component of the scenario that will help investors search out opportunities, execute trades, and monitor portfolios. Through gamification practices, or the use of game-playing design elements in products and services, these apps can improve financial literacy and investor engagement.³⁹ Similar to the role of social media in investing, these innovations come with potential risks. Recent research found that 69% of financial app users have received suggestions about specific investments, and 67% of them have then traded based on that digital "nudge."⁴⁰

The ease and speed with which investors can open new accounts have propelled the growth of new investing apps and other fintech services, helping them gain market share from incumbents. The digitization of identification and the streamlining of customer acquisition and onboarding processes has facilitated this transition. Digitization, including the use of AI tools, will reduce frictions and facilitate a higher volume of transactions.

Amid the flood of new and varied investment decision-making data and sources, however, investor protections are paramount. Data quality and the accuracy of financial information must be verifiable and subject to regulatory oversight to help ensure market integrity and investor protection.

Implications for the Industry

The three pillars of Digital Transformation—big data and AI, new asset classes, and new digital information channels and platforms—will combine to create a challenging and uncertain future for the investment industry, filled with unforeseen opportunities for those with the skill and foresight to navigate this transition.

Talent acquisition and development will gain greater focus as firms seek to address skill gaps in the digital transformation scenario. Professionals who understand the intersections between finance and data science (and the application of data science to other scenario domains, such as sustainability) will carry a premium.

Scenario Outcomes

- The firms and professionals that best align AI with HI and capitalize on technological innovation to increase productivity and expand individual and firm capabilities will lead the industry.
- Talent needs evolve as investment organizations require new skill sets amid the transition from a technology-supported to a technology-driven investment industry.
- AI, big data, and other new technologies and investment techniques necessitate new governance and supervisory structures to minimize risks and biases, which may create a bottleneck for technology implementation.
- Regulators must ensure all market participants are on a level playing field and enjoy high standards of investor protection, requiring consistent and holistic regulation, particularly around fintech and financial information.
- As new asset classes and investment applications develop, new investors enter the market in greater numbers. Whether and to what degree firms succeed depends in part on their ability to meet the personalization demands of this new cohort.

³⁹Sivananth Ramachandran, CFA, CIPM, "Fun and Games: Investment Gamification and Implications for Capital Markets," CFA Institute (16 November 2022). <https://rpc.cfainstitute.org/research/reports/2022/investment-gamification-implications>.

⁴⁰FINRA Investor Education Foundation and CFA Institute, "Gen Z and Investing."

THE END OF CHEAP MONEY

Easy money has fueled the financial markets and the global economy for the last four decades. Although interest rates have generally trended downward since the early 1980s, they fell precipitously following the GFC as negative demand shocks prompted central banks to cut rates and conduct other forms of monetary stimulus. Such low interest rates boosted growth and provided policy support to financial markets, driving market stability. They also incentivized risk taking by investors and decision makers who used significant amounts of leverage in the search for yield.

Returns on stocks, real estate, and other risk assets increased. In particular, fixed-income securities tended to perform well, continuing the bull market that started in the early 1980s. Low interest rates compressed net interest margin for banks, which—combined with regulatory demand for higher capital levels after the GFC—led to a relative retrenchment of the banking sector. Capital markets benefited from this retrenchment and enjoyed rapid growth, especially in North America, accelerating the transition toward more market-based financial structures.

The low-interest rate environment also served as a tailwind for the asset management business. Investors sought returns in stocks, bonds, mutual

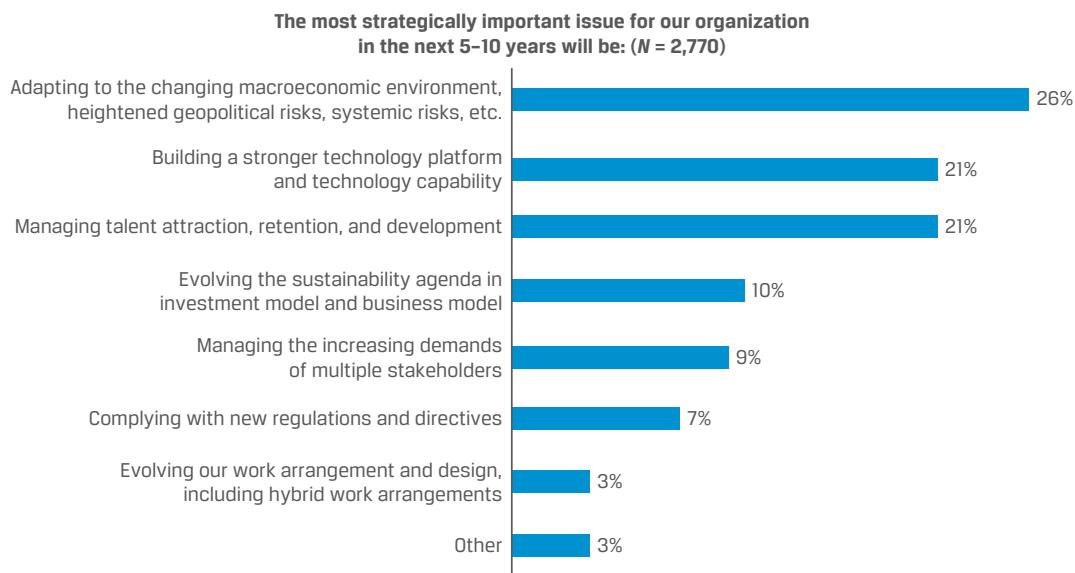
funds, ETFs, and commodities, among other instruments, which boosted volumes and AUM, increasing firm profitability. Near-zero interest rates focused investors on fees, however, because lower discount rates boosted asset values across the board, making passive management relatively more attractive than active management (as discussed earlier) and changing the profile of firms' AUM. Therefore, low interest rates intensified the pressure on fees and profits.

In the Wake of COVID-19: Tightening the Monetary Belt

The social and economic impact wrought by COVID-19 and the related policy responses led to increased fiscal deficits and public debt. In *The End of Cheap Money*, efforts to consolidate fiscal positions through higher taxes and reduced public spending and investments dampen economic growth and lower expected returns in financial markets over the next 5–10 years. Deficit reduction inhibits efforts to combat economic inequality and slowing global growth. How the investment industry adapts to this new normal is the key challenge according to our survey (see **Exhibit 22**).



Exhibit 22. Most Strategically Important Issue



As inequality rises, it exacts a heavy toll on the world economy. The vast majority of respondents expect the impact to be moderate or severe, as Exhibit 10 demonstrated.

As central banks have shifted their focus from discouraging deflation to managing inflation, they have raised interest rates and attempted to reduce the use of more recent, innovative monetary policy tools, such as quantitative easing. The inflation fight and fiscal consolidation will restrain economic growth and subdue the appetite for risk and leverage while increasing market volatility.

Easy Money: A Hard Habit to Break

Accommodative policy is far easier to start than stop. The gradual removal of monetary support is not a linear process and generates periodic market turbulence. As ultra-cheap financing becomes a thing of the past, the unwinding of currency carry trades (borrowing cheaply in one currency to invest in another, higher-yielding currency) exacerbates asset price volatility and reverberates into the real economy.

As asset values are repriced, investors and institutions face liquidity challenges and some even struggle to stay solvent, as demonstrated by the spate of banking failures in early 2023. Combined with fiscal consolidation and supply side, policy, and geopolitical shocks, this situation adds to economic uncertainty. Higher nominal interest rates make fixed-target returns easier to achieve without reaching for yield or increasing leverage, prompting less mechanical risk taking by institutions.

As higher interest rates make borrowing more expensive, market participants try to decrease their leverage, while central banks work to lower inflation and, in some cases, restore their credibility. With subdued economic growth, leverage may decline because higher rates, in general, favor lenders at the expense of borrowers.

Low interest rates and returns put downward pressure on the fees mutual funds can charge and lower cost structures for passive strategies. The End of Cheap Money and its attendant implications for market volatility have a largely benign effect

on active strategies, however, and encourage the creation of new strategies and products.

Firms develop new variants of inflation-protected bonds, insurance, derivatives, and other synthetic products to help clients manage the effects of inflation and their specific circumstances. With markets receiving less support from central banks, valuations become more differentiated, creating opportunities for stock pickers and value investors.

Money market mutual funds (MMMFs) enjoy a resurgence amid higher equity market volatility. Their ability to pay higher rates makes them more attractive, while capital losses in existing bond portfolios prompt investors to liquidate bond positions and park the funds in MMMFs. This favorable environment leads to investor inflows into MMMFs. As capital pours into money funds, mutual fund companies charge higher fees, improving the economic case for MMMFs.

Private equity faces less favorable prospects amid higher rates. Volume and valuations fall for buyout firms given their reliance on increasingly expensive debt. Private markets are slower to mark down prices and more vulnerable to mispricing and sharp spikes and plunges. Surprises are common.

When private capital was abundant and cheap, companies had little incentive to go public. Firms with intangible assets and long cycles of research and development could appreciate in value without submitting to the scrutiny of public reporting requirements. As private capital becomes more costly and harder to access, companies return to IPOs and the public markets as a financing mechanism.

Low interest rates and higher levels of leverage enabled more trading, creating liquidity in the marketplace. As interest rates rise, liquidity is significantly reduced, and disruptions emerge in the trading of financial instruments.

The End of Cheap Money constitutes a regime change. Amid the shift from falling interest rates and accommodative monetary policy to higher nominal interest rates and the gradual but uneven unwinding of extraordinary policy tools, increased debt burdens and supply-side, geopolitical, and policy shocks will inhibit risk taking and reduce the appetite for debt and leverage, with material implications for the economy, investors, and financial markets.

Scenario Outcomes

- Amid a more challenging environment for economic growth, inequality becomes more deep seated and persistent.
- There is less incentive for leverage and risk taking amid liquidity and even solvency challenges in key segments of the marketplace and among investors and institutions.
- Higher interest rates serve as tailwinds for active asset management strategies and vehicles as increased differentiation of valuations creates opportunities for stock pickers and value investors.
- Intermediaries create additional products to help customers manage the effects of inflation. Cash-like products, such as MMMFs, become more attractive, and investor inflows increase.
- With private capital harder to come by, private equity and other private strategies face new challenges, prompting some companies to return to the public markets and IPOs for financing.

CONCLUSION

Our analysis of the megatrends and scenarios for the future reveals several commonalities.

The combination of deglobalization and fragmentation of the investor base, outlined in the Diverging Worlds scenario, points to the need for firms to differentiate their products and services across market segments. And as outlined in the Digital Transformation scenario, new technological capabilities provide the means to develop more personalized products and innovative solutions, enabled by big data and a richer understanding of client preferences.

Personalization and enhanced technological capabilities allow firms to charge higher fees for such offerings. In an environment of higher inflation, market volatility, and more variable nominal interest rates, as articulated in The End of Cheap Money, opportunities for active management will reemerge. Investors are likely to become more discerning in their product choices and more willing to pay higher fees where positive net-of-fees outperformance and outcomes aligned to personal values can be achieved in the medium term. Industry conditions are far more conducive for successful active managers to demonstrate their value to clients than at any point in the previous 15 years.

Further, investors' sustainability preferences and motivations provide additional demand for more personalized and more actively managed products with

different value and impact measurements, enabled by improvements in data and reporting frameworks.

Together, these trends point to a future state of much greater market segmentation, with more diverse opportunities for firms. Rather than seeking to be "one product for all" in their product offerings, firms may gravitate toward the maxim of "one product for each," with each customer expecting personalization. In the broader industry, larger firms will apply advanced technologies at scale, and smaller firms will operate in more niche and focused product areas.

Through more sophisticated investment products, the industry can deliver greater client value and satisfaction. To do this, as well as to achieve its higher purpose, the investment industry must

- hold itself to extremely clear and high standards of professionalism,
- add value that reflects favorably relative to the rewards it enjoys itself, and
- exercise responsible values in its dealings with its multiple stakeholders.

The successful professionals and firms in the next 5–10 years must deal fluently and flexibly with increasingly complex situations and changing circumstances, while always remaining focused on client fulfilment and fiduciary duty.

Investment Product Opportunities

Under the megatrends and scenarios outlined in this report, we expect to see growing demand in the following new product areas:

- Personalization
 - Direct indexing
 - Custom portfolios
 - Thematic investments
- Tokenized securities
- Sustainability

- Impact funds
- Net-zero-aligned portfolios
- Low-carbon benchmarks

We also expect renewed demand for the following traditional investment products:

- Money market funds
- Inflation protection instruments
- Actively managed equity and bond portfolios

THE PATH FORWARD

In assessing the industry in its current and likely future stages, we see several critical challenges and opportunities that we must consider in the path forward, notably in the following areas:

- *People model:* The industry will depend on human capital to create value through strong talent and culture and through DEI.
- *Enabling model:* The industry will depend on a more dynamic and streamlined investment model than in the past, in which collaboration, innovation, and technology will be critical to success.
- *Change model:* In its present state in this fast-changing environment, the industry is unlikely to be able to fully meet its fundamental goals of creating significant societal wealth and well-being, and some organizational change will be needed.

In the next 5–10 years, as we noted earlier, we see the investment industry facing two divergent paths. One path continues toward the desirable *professional industry* state, while the other leads toward

the *unnecessary industry* state, characterized by a decline in trust of traditional finance resulting in radical disintermediation.

The investment industry must strive to avoid this latter path by embracing the progressive use of technology, streamlining the investment model with a value chain that eliminates unnecessary intermediation and delivers desired client outcomes, and evolving its thinking and understanding of industry dynamics to address the challenges of complexity. Examples of these practices set out in this report include using AI and big data applications, such as LLMs, to improve investment processes and enhance productivity; creating innovative, personalized products that align with client preferences and values, delivered through streamlined digital interfaces; and the embrace of systems thinking and collaboration with industry coalitions to address sustainability challenges.

Delivering value in a way that better links purpose with tangible economic benefit is pivotal to landing solidly as the *professional industry*.

Authors

Rhodri Preece, CFA
Senior Head, Research

Ryan Munson
Research Manager, Research

Roger Urwin, FSIP
Research & Policy Center Advisory Council Member

Andres Vinelli
Chief Economist

Larry Cao, CFA
Former Senior Director, Industry Research

Jordan Doyle
Affiliate to the Research & Policy Center

Editor

Paul McCaffrey
Editor, Enterprising Investor

About the Research and Policy Center

CFA Institute Research and Policy Center brings together CFA Institute expertise along with a diverse, cross-disciplinary community of subject matter experts working collaboratively to address complex problems. It is informed by the perspective of practitioners and the convening power, impartiality, and credibility of CFA Institute, whose mission is to lead the investment profession globally by promoting the highest standards of ethics, education, and professional excellence for the ultimate benefit of society. For more information, visit <https://rpc.cfainstitute.org/en/>.

About CFA Institute

CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow. There are more than 190,000 CFA charterholders worldwide in 160 markets. In the mainland of China, CFA Institute accepts CFA® charterholders only. CFA Institute has nine offices worldwide, and there are 160 local societies. For more information, visit www.cfainstitute.org or follow us on LinkedIn and Twitter at @CFAINstitute.