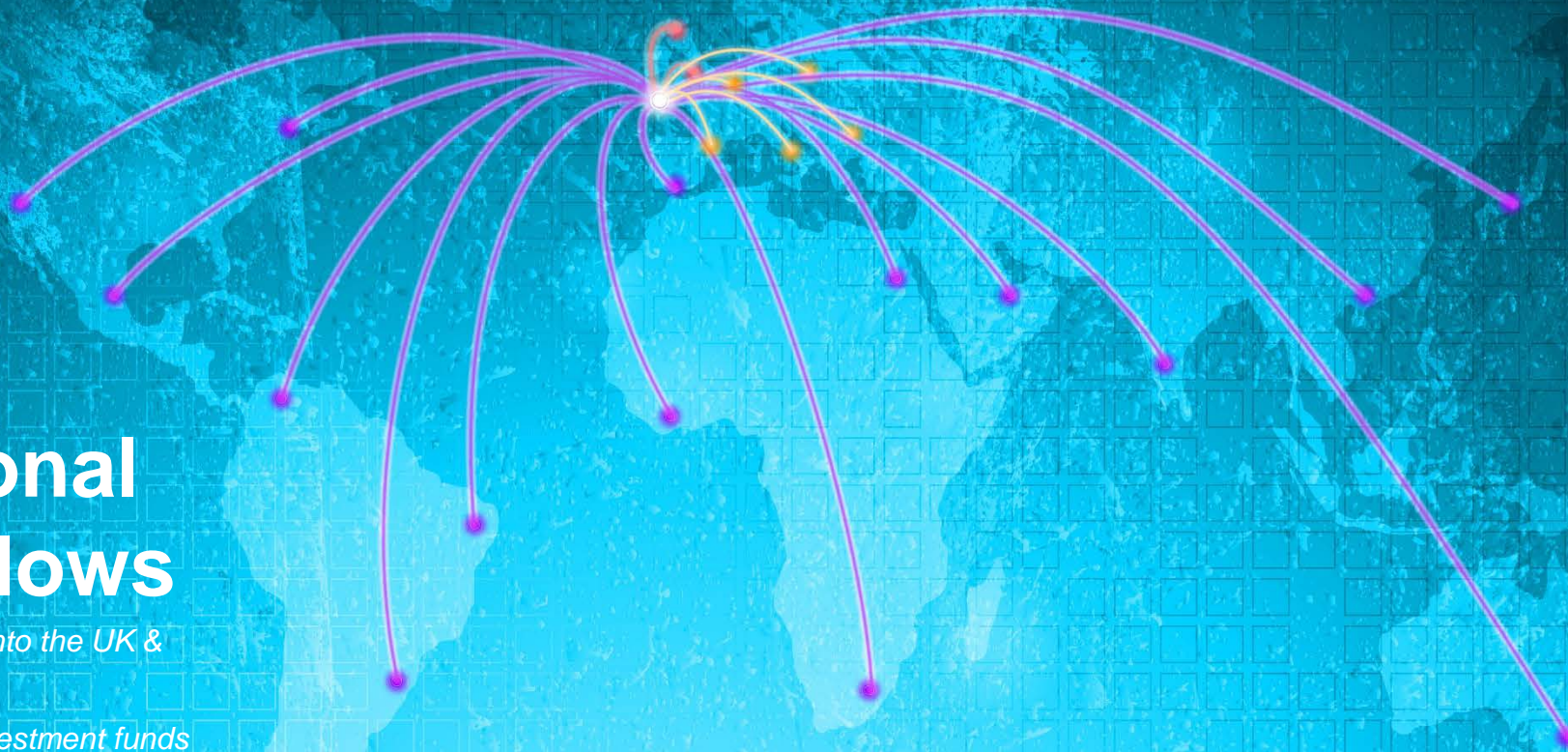




cutting through complexity



International Capital Flows

*International investment into the UK &
Europe:*

*the role of Guernsey's investment funds
sector*

January 2015



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Private and confidential

Chief Minister
States of Guernsey
Sir Charles Frossard House
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Channel Islands
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23 January 2015

The scope of work for this report has been agreed by the addressee and to the fullest extent permitted by law we will not accept responsibility or liability to any other party (including the addressee's legal and other professional advisors) in respect of our work or the report.

Yours faithfully

KPMG Channel Islands Limited

Dear Sir

International Capital Flows

In accordance with our engagement letter dated 27 January 2014 ("Engagement Letter"), we enclose the final report on International Capital Flows.

As stated in our Engagement Letter, you have agreed that this final written report supersedes all previous oral, draft or interim advice, reports and presentations, and that no reliance will be placed by you on any such oral, draft or interim advice, reports or presentations other than at your own risk.

The important notice should be read in conjunction with this letter.

Our report is for the benefit and information of the addressee only and should not be copied, referred to or disclosed, in whole or in part, without our prior written consent, except as specifically permitted in our Engagement Letter.

Important notice

Our work commenced on 3 March 2014 and our fieldwork was completed on 6 November 2014. We have not undertaken to update our report for events or circumstances arising after that date.

In preparing our report, our primary source has been quantitative data from local administrators of Guernsey funds and representations made to us during interviews with key decision makers of the Guernsey funds market including local and UK investment managers, lawyers and sponsors. We do not accept responsibility for such information. Details of our principal information sources are set out within the document and we have satisfied ourselves, so far as possible, that the information presented in our report is consistent with other information which was made available to us in the course of our work in accordance with the terms of our Engagement Letter. We have not, however, sought to establish the reliability of the sources by reference to other evidence. This engagement is not an assurance engagement conducted in accordance with any generally accepted assurance standards and consequently no assurance opinion is expressed.

AIC	Association of Investment Companies	IMF	International Monetary Fund
AuA	Assets under Administration	LSE	London Stock Exchange
AuM	Assets under Management	NAV	Net Asset Value
CISE	Channel Islands Securities Exchange	Other (Regions)	Regions outside Europe
Continental Europe	All European countries excluding UK	PE	Private equity
Europe	All European countries including UK	Regions	Groups of countries represented by Continental Europe, UK and Other
FCA	Financial Conduct Authority	SEC	Securities and Exchange Commission
GFSC	Guernsey Financial Services Commission	SME	Small or medium sized enterprise
GIFA	Guernsey Investment Fund Association	UK	United Kingdom
Guernsey funds	Guernsey domiciled funds		
Global investors	Investors from outside of Europe		
IM	Investment Manager or Investment Advisor providing investment advice to the Guernsey Manager of a Guernsey fund		

The contacts at KPMG
in connection with this
report are:

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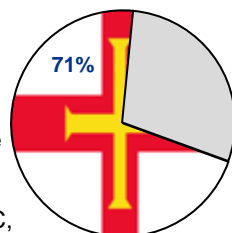
Project Scope

We have been engaged to perform a research project for Policy Council to analyse the economic benefits of the Guernsey funds industry to the UK and Europe. The project was completed in two phases in which the initial phase ("phase A") consisted of information gathering and surveying, and the second phase ("phase B") consisted of analysis

Phase A – Survey and information gathering

We interviewed key decision makers of the Guernsey funds market including local and UK investment managers, lawyers and sponsors to obtain qualitative opinions on the offshore funds industry and to better understand the benefits for using Guernsey structures

We also gathered quantitative data from local administrators of Guernsey funds obtaining a coverage of 71% of the total market by AuA. The data primarily consisted of the geographical region of the investor base, where capital is deployed and where fees are earned



We reviewed publically available information provided by the AIC, Monterey, GFSC, Guernsey Finance and the IMF to assist with the analysis in Phase B; to sense check the consistency of findings

Phase B - Analysis

Integrating the findings of both the qualitative opinions and the quantitative data, we have:

- Summarised the Guernsey funds market assets under management by region of investor domicile and by region of where capital is deployed
- Estimated the sectoral split of Guernsey assets under management and by region of where those assets are invested
- Identified the key asset classes to which assets have been invested
- Identified and explained key trends which may assist in demonstrating the economic benefits to the UK and Europe of the Guernsey Funds sector

The findings of the sample obtained have been extrapolated to build a wider picture of the extent to which Guernsey impacts the UK and European economies

Coverage and assumptions

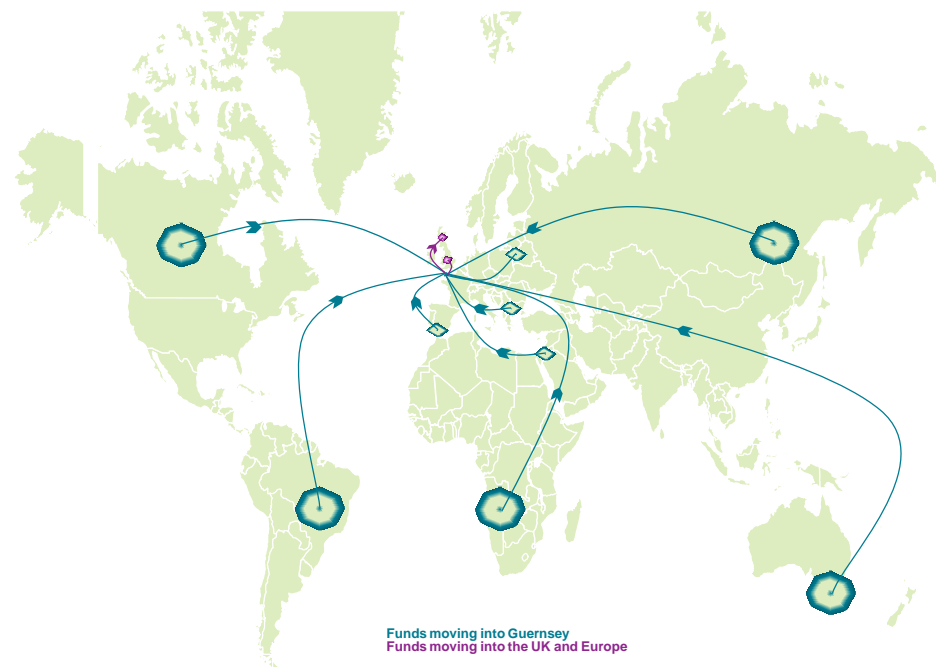
Due to inherent challenges and limitations around data, certain assumptions have been made in arriving at our conclusions. These have included:

- Excluding funds of funds from our population to avoid duplicating data
- Assuming that the sample obtained is representative of the entire population
- Allocating data across a fund portfolio where the administrator was only able to give certain data in total form

We have not sought to verify the accuracy of data provided by fund administrators

Hypothesis

A key objective of our analysis is to demonstrate the economic benefits provided to the UK and Europe through global investors accessing UK and European assets facilitated by the Guernsey funds industry



Executive summary

1 The Guernsey funds industry acts as a conduit for £24.6bn of inward investment into the UK from global investors

2 The Guernsey funds industry acts as a conduit for £51.4bn of inward investment into Europe from global investors

3 European investment companies earn £800m of fees per annum from managing assets in Guernsey funds sourced from non-European investors

4 Guernsey funds facilitate access for UK investors investing £26.5bn into global assets

5 The Guernsey funds industry facilitates inward and outward investment to and from the UK and Europe with a robust and internationally recognised regulatory platform

Summary of funds market population

Guernsey funds have a total population of £155.4bn assets under administration (excluding funds of funds) as at 30 June 2013. The sample obtained by KPMG upon which our analysis has been performed is £109.7bn across 14 administrators (representing coverage of 71%). We have extrapolated our sample results to cover the entire population

Our analysis indicates that the majority of assets from Guernsey funds (46%) are deployed into Continental Europe with 32% being deployed outside of Europe and 22% deployed into the UK

Half of all investors are located outside of Europe demonstrating global investors are comfortable using Guernsey structures. The interviews suggest the key reason for this is the island being well respected and transparent with an established regulatory track record. 23% of investors are located in the UK

Guernsey is a hub for alternative investment assets and a number of our survey respondents recognise Guernsey as the default jurisdiction for Alternative funds. Private equity is the dominant sector in the Guernsey funds market with 70% of all assets being deployed into this sector, predominantly located in Continental Europe and the UK

Infrastructure and Property each account for 8% of the market. Infrastructure assets are predominantly located either in the UK (42%) or outside of Europe (55%). Property assets are predominantly located in the UK (37%) or Continental Europe (53%)

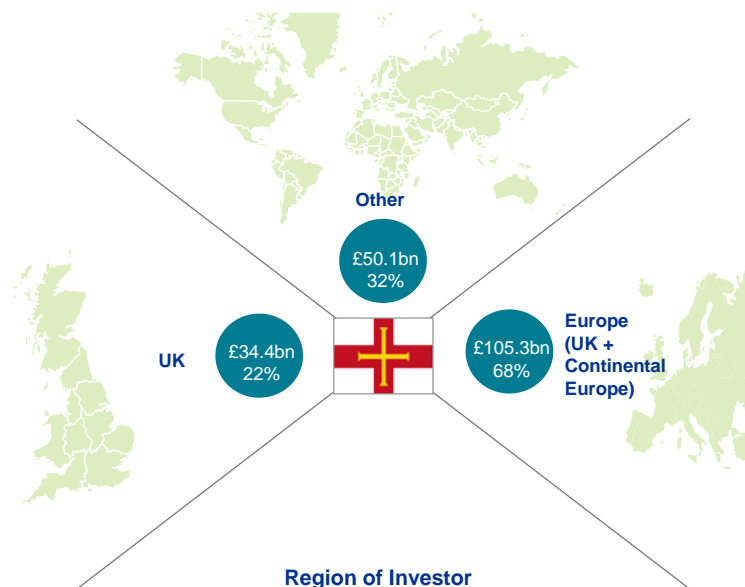
Global facilitation

Guernsey is used as a conduit to facilitate the raising of capital from investors in different countries and subsequently to facilitate the deployment of this capital into global assets

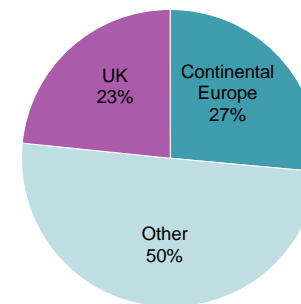
Our analysis shows that less than 3% of funds in Guernsey by number (less than 1% by value) have all of their assets and investors located in one region. Guernsey funds have a diversified investor base, with 86% of funds having investors located in more than one region as well as a diversified asset base with at least 55% of funds deploying assets in more than one region

These statistics support the notion that Guernsey is utilised as a facilitator of global investment and, as a transparent jurisdiction, can play a major role as cross-border investment continues to grow

Region of asset deployment (£155.4bn)



Region of Investor



Economic benefits to the UK

Guernsey funds promote significant inward investment into the UK

Our analysis indicates that £34.4bn from Guernsey funds is invested into UK assets. The majority of this is invested into long term tangible assets, including PE (60%), Infrastructure (14%) and Property (14%). All of these asset classes can provide economic and social benefits to the UK. Social (for example schools and hospitals) and economic (for example airports and roads) infrastructure assets, totalling £4.8bn, serve communities, provide social benefits, support jobs and stimulate economic growth. PE firms, totalling £20.6bn, typically look to invest majority stakes in underperforming companies that have the potential for high growth. Growth in the businesses is delivered by working with the company's management team to improve performance and strategic direction, making complementary investments and driving operational improvements. We have analysed the three largest Property funds by NAV, covering 41% of all property assets invested in the UK. All three invest in commercial property which provide support and facilities to business all across the UK

The majority of investment into the UK via Guernsey funds is from overseas investors (72%, £24.6bn), predominantly non-European investors, which demonstrates Guernsey's role as a facilitator of inward investment to the UK. Our respondents note that the overseas investor base is more likely to use Guernsey than any other jurisdiction when investing into the UK

The UK generates substantial IM fees from Guernsey funds

Guernsey is the offshore jurisdiction of choice for a large number of UK IMs and we estimate that the UK earns £1.1bn in IM fees from Guernsey funds, representing 9% of total UK IM fees

Guernsey assists UK investors with portfolio diversification through access to global investments

Our analysis indicates that UK investors invest £36.3bn into Guernsey funds, of which 73% is then deployed outside the UK. This supports the hypothesis that the Guernsey funds market facilitates UK investors in achieving their goal of obtaining exposure to global alternative assets which they may be unable to do through alternative domiciles. UK investors are predominantly institutional, pension funds, multi asset funds and private wealth managers and can achieve a higher return for their underlying investors through an efficient structure with access to a more diversified choice of investments. During the qualitative assessment it was noted that UK investors are comfortable using Guernsey and Guernsey offers UK IMs and investors flexible structures to enable a wider investment choice. Furthermore, it was noted that the FCA and SEC are comfortable with Guernsey and the GFSC offers a well regulated, respected and efficient service

Economic benefits to Europe

Guernsey funds promote significant inward investment into Europe

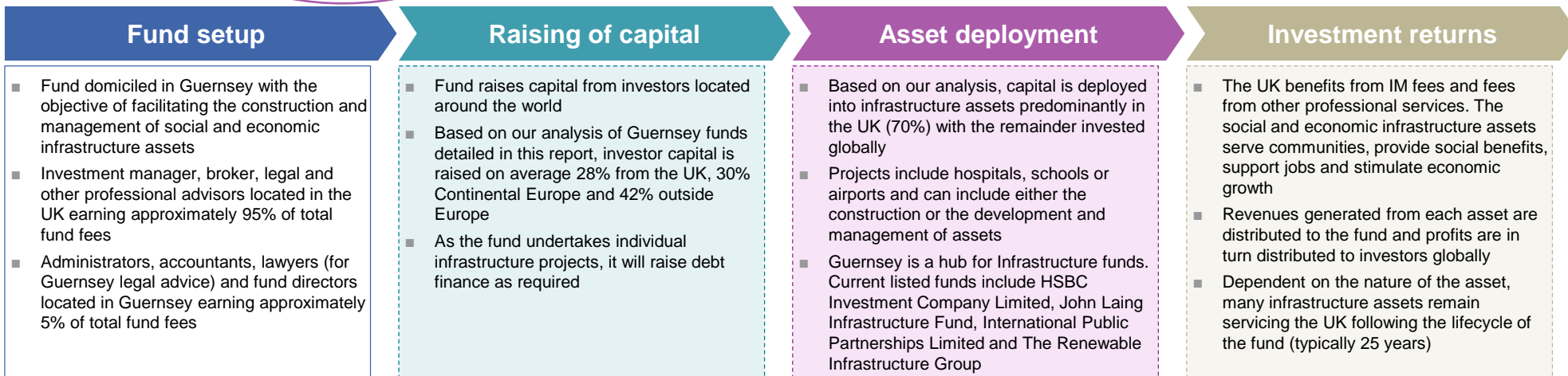
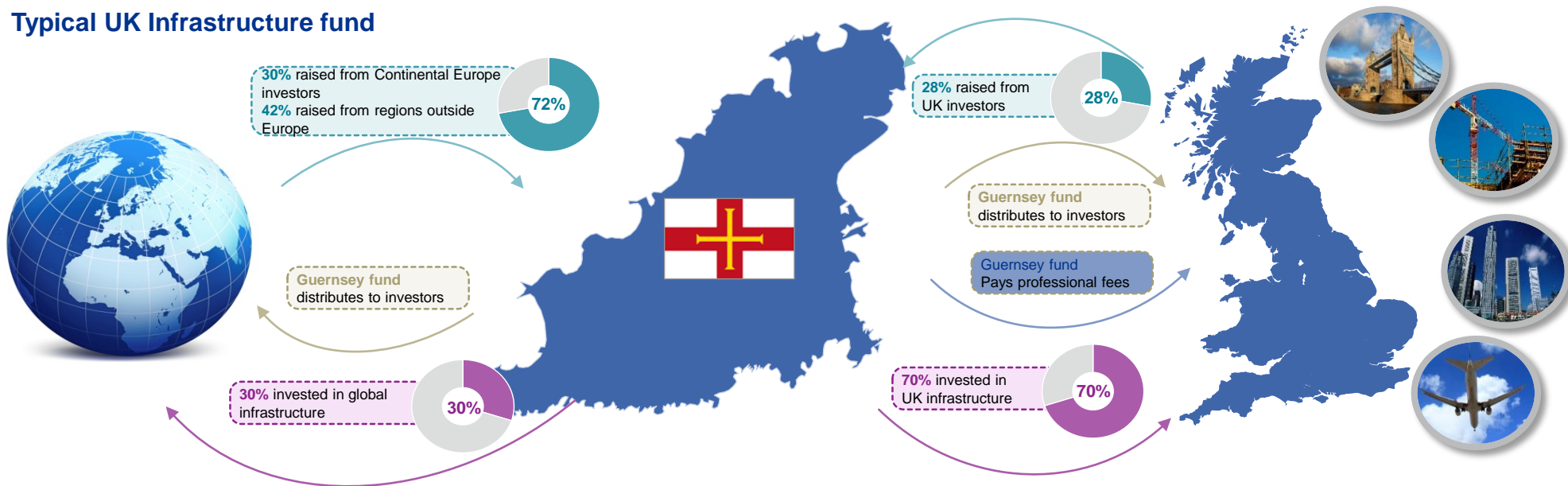
£105.3bn of assets per our population are deployed in Europe, predominantly in PE, Infrastructure and Property. Collectively, these asset classes make up 92% of assets deployed into Europe. Non-European investors contribute £51.4bn (49%) of investment to assets deployed in Europe. Based on our interviews, we believe that the £53.9bn from European investors is deployed in countries that are different from the underlying investor country, thus demonstrating inward investment into individual European countries

Europe generates substantial IM fees from Guernsey funds

Total IM fees earned by Guernsey domiciled funds amount to £1.8bn, of which European IMs earn 90% (£1.6bn) despite providing only 50% of investors and holding 68% of assets

Under the recently implemented AIFMD, Guernsey offers the flexibility of a dual-regime enabling IMs to offer an efficient and appropriate framework for investment into Europe for European and non-European investors. The dual regime ensures Guernsey will become more important in attracting inward investment into Europe and generating fees for European IMs who will be able to remain competitive with non-European IMs

Typical UK Infrastructure fund



UK funds analysis

Impact on the UK – inward investment

Guernsey funds facilitate £34.4bn of investment into the UK

Our review population indicates that PE constitutes the majority (70%) of the Guernsey funds industry by AuA, followed by Infrastructure and Property (both 8%). Assets are deployed globally with the highest proportion (46%) allocated to Continental Europe

£34.4bn of assets per our population are deployed in the UK, predominantly in “real assets” (PE, Infrastructure and Property). Collectively, these asset classes make up 88% of assets deployed into the UK

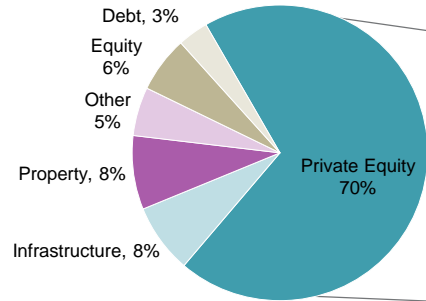
Private equity firms manage and grow companies valued at £20.6bn across the UK, supporting economic growth and supporting jobs in businesses ranging in size from SMEs up to multi-nationals

Guernsey Infrastructure funds (including a hub of Renewable funds) assist with supporting key UK government objectives by facilitating the construction and management of £4.8bn of key infrastructure assets across the UK

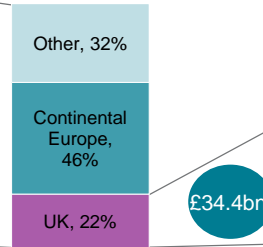
Of the top 3 Property funds (representing 41% of the property industry), all relate to commercial property which provides office space nationwide to British enterprises

Debt funds provide £1.4bn of liquidity to both UK companies and the UK government through the purchase of gilts

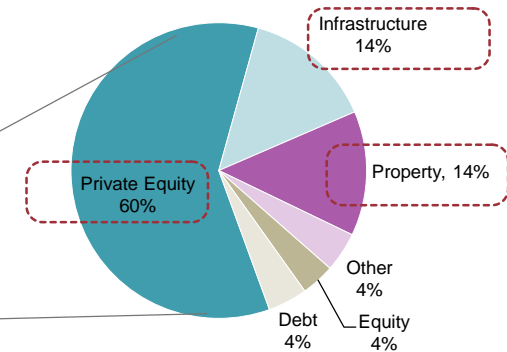
Assets per sector for the Guernsey funds industry (£155.4bn)



Region of Investment



Assets per sector for assets located in the UK (£34.4bn)



Source of all analysis: KPMG analysis

There would be “significant loss to the UK if Guernsey didn’t exist”

Source of all quotations: KPMG interviews of UK IMs, lawyers and sponsors

Impact on the UK – inward investment

Guernsey funds promote significant inward investment into the UK

Guernsey is a key facilitator of inward investment into the UK

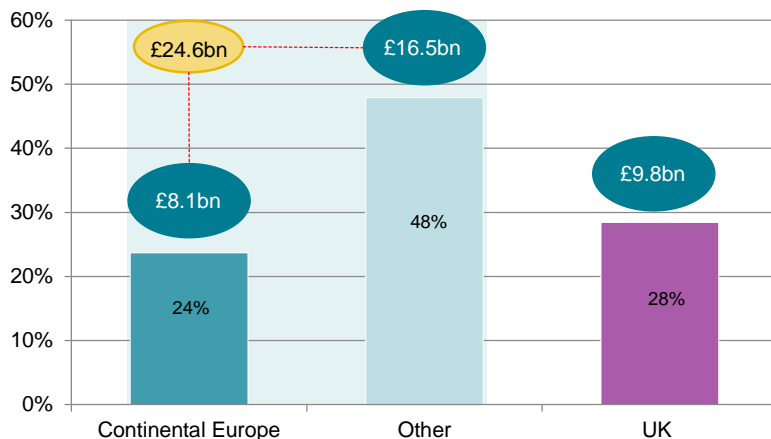
Non-UK investors contribute £24.6bn (72%) of investment to assets deployed in the UK, with only £9.8bn (28%) being sourced from UK investors. This indicates that a Guernsey structure acts as a mechanism to source and facilitate global investors to invest in UK assets as opposed to recycling UK wealth

77% of all PE investors in UK assets are from outside of the UK enabling non-UK investors the opportunity to invest in a wide range of UK sectors leading to potential improvements in UK businesses

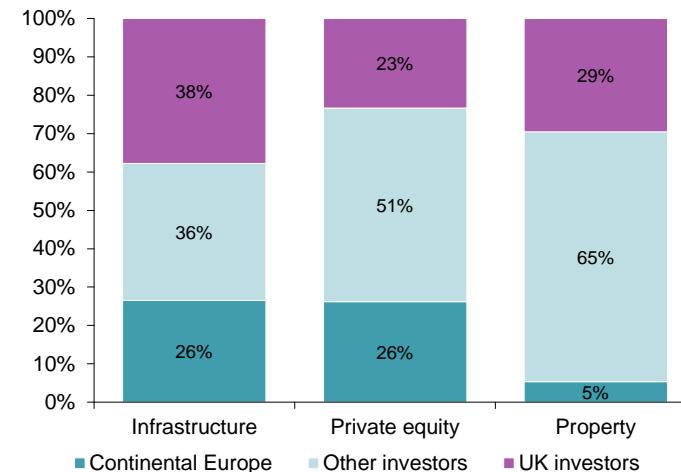
The majority of property investors (65%) are from outside Europe, signifying the attractiveness of UK commercial property to non-European investors

“Without an offshore structure, the IM industry would not be able to provide such a wide range of investment opportunities”

Region of investors for UK investments



Investor region of UK based assets (top 3 asset classes)



“Guernsey provides support to the UK economy through direct investment in assets and employment for local populous”

Impact on the UK - fees

The UK generates £1.1bn of IM fees from Guernsey funds

Total IM fees earned by Guernsey domiciled funds amount to £1.8bn, of which the UK earns 63% (£1.1bn) despite providing only 23% of investors and holding 22% of assets

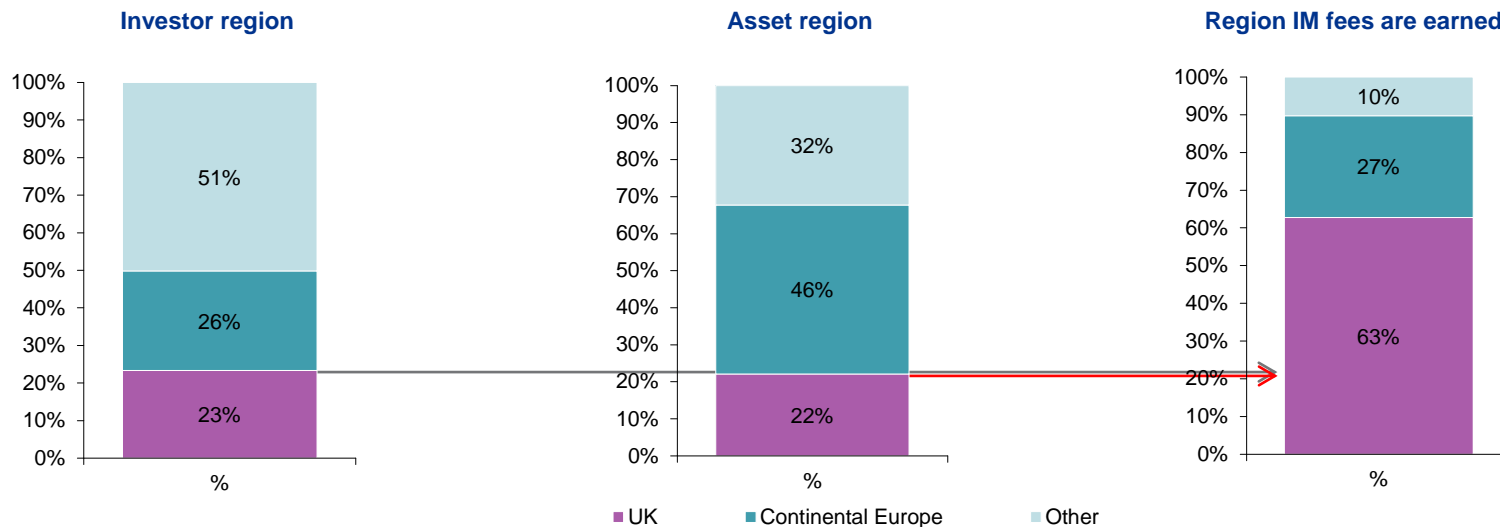
The UK Investment Management Strategy estimates that the UK earns £12bn from the Investment Management industry. Using this metric, our analysis indicates that Guernsey funds contribute 9% of UK IM earnings

UK earned fees for other services providers, including lawyers and sponsors, amount to £138.9m

These fees only include those services provided directly to the Guernsey fund and not any underlying portfolio companies

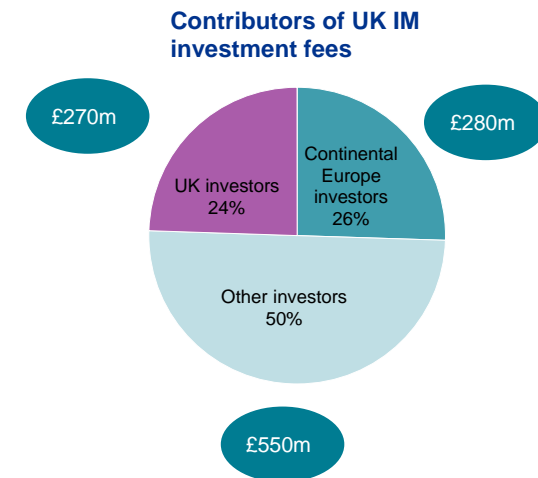
UK IM fees, where funds do not have any assets located in the UK, amount to £484.2m (with other fees of £67.1m)

Non-UK investors contribute £842.3m in UK IM fees



Overseas investors invest £119bn in Guernsey funds of which £34.4bn is invested in UK assets, UK IM's earn total fees of £1.12bn

“Guernsey assists the UK professional services and IM industry which the UK depends on”



Impact on the UK – outward investment

Guernsey assists UK investors access global investments

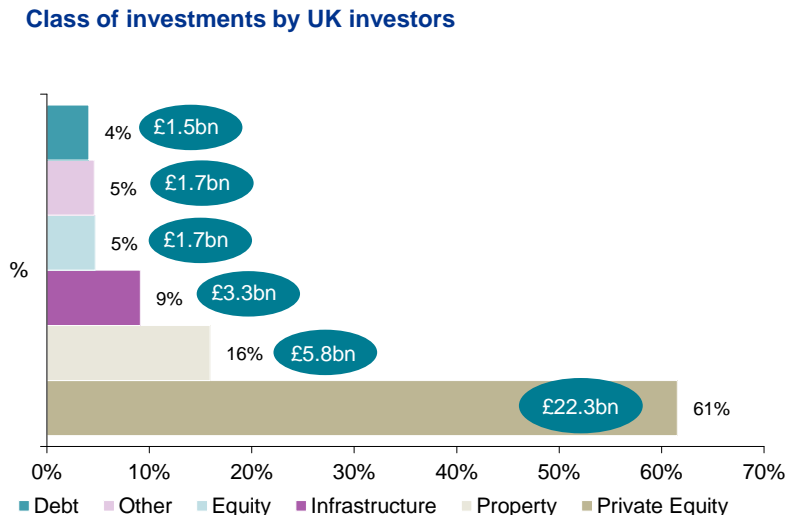
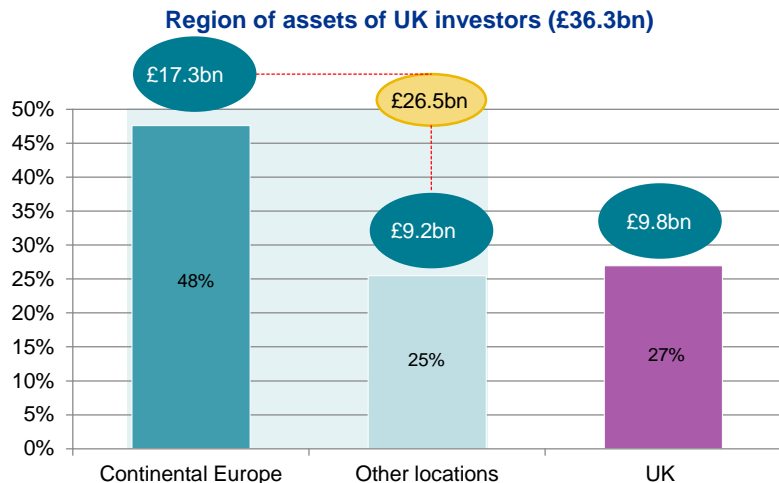
UK investors invest a total of £36.3bn through funds in Guernsey with 73% of their assets (£26.5bn) outside the UK

Guernsey funds market facilitates UK investors to achieve their goal of obtaining exposure to global alternative assets which they may be unable to do through alternative domiciles

UK investors are predominantly institutional, pension funds, multi asset funds and private wealth managers and can achieve a higher return for their underlying investors through a more efficient structure with access to a greater diversity of investments

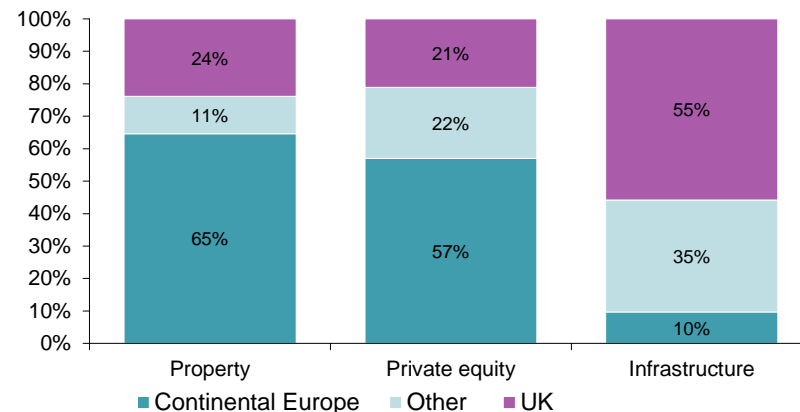
European property and private equity are the main attraction for UK investors investing outside the UK with £16.5bn invested into these asset classes

The stand out asset class for UK investors investing inside the UK is Infrastructure



“UK investors (including pension funds) can generate better returns investing through Guernsey and thus require less UK government support”

Investment region of UK investors (top 3 asset classes)



Global impact

Guernsey facilitates globalisation of investments

Guernsey is used as a conduit to facilitate capital raise from investors in different countries and subsequently to facilitate the deployment of this capital into global assets

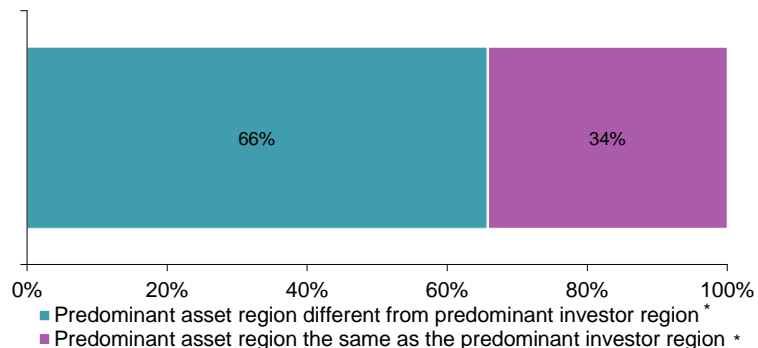
At least 66% of funds deploy the majority of capital in regions that are different to where the majority of their investors are located. 34% invest in the same region but across different countries within this region

Guernsey funds attract a global investor base with 86% of funds containing investors from at least 2 different regions. The majority of funds (77%) can be classified as truly global, attracting investors across all regions

IMs use Guernsey funds to deploy assets globally with 55% of funds investing in more than one region

Less than 3% of funds (<1% by value) have all of their investors and assets in the same region

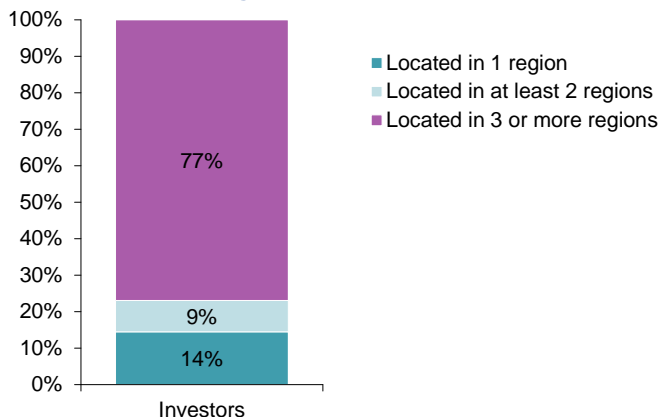
Investor location vs asset location



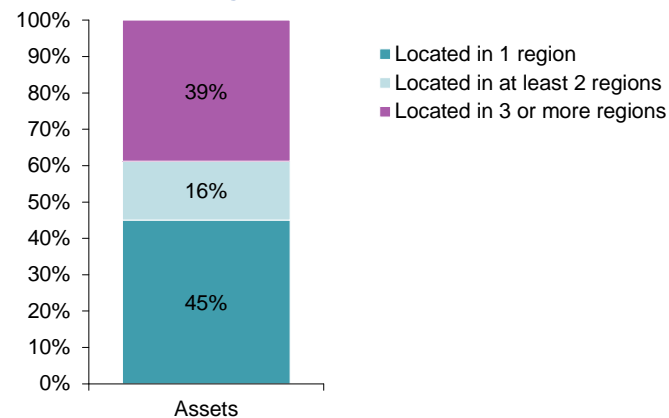
*In performing this analysis we have allocated only one region (the most significant) to each fund for investor base and one region (the most significant) for asset base.

“Guernsey’s tax neutral structures allow IMs to invest in global assets and distribute back to a global investor base without incurring multiple levels of taxation”

Number of investor regions in each fund



Number of asset regions in each fund



European funds analysis

Impact on Europe – inward investment

Guernsey funds facilitate £105.3bn of investment into Europe

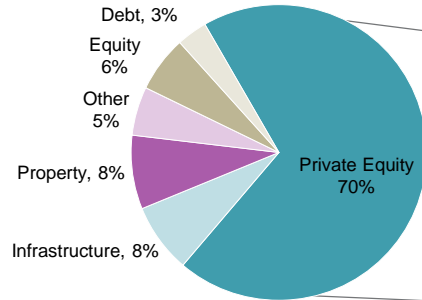
£105.3bn of assets per our population are deployed in Europe, predominantly in “real assets” (PE, Infrastructure and Property). Collectively, these asset classes make up 92% of assets deployed into Europe

Private equity firms manage and grow companies valued at £80bn across Europe, supporting economic growth and supporting jobs in businesses ranging in size from SMEs up to multi-nationals

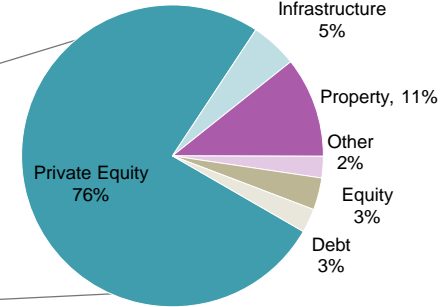
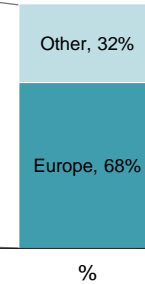
Guernsey Infrastructure funds (including a hub of renewable funds) assist with supporting key European government objectives by facilitating the construction and management of £5.3bn of key infrastructure assets across Europe

Debt funds provide £3.2bn of liquidity to both European companies and European governments through the purchase of gilts

Assets per sector for the industry (£155.4bn)



Assets per sector for assets located in Europe



Impact on Europe – inward investment

Guernsey funds promote significant inward investment into Europe

Guernsey is a key facilitator of inward investment into Europe

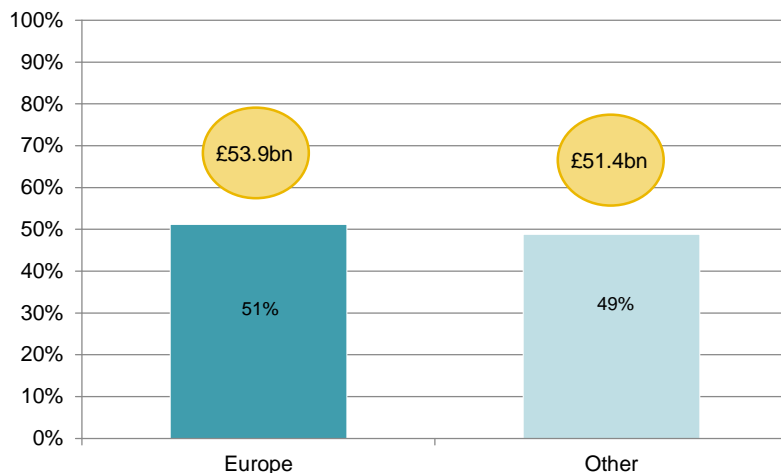
Non-European investors contribute £51.4bn (49%) of investment to assets deployed in Europe. It is likely that the £53.9bn from European investors is deployed in countries that are different from the underlying investor country

This indicates that a Guernsey structure acts as a mechanism to source and facilitate global investors to invest in European assets as opposed to recycling European wealth

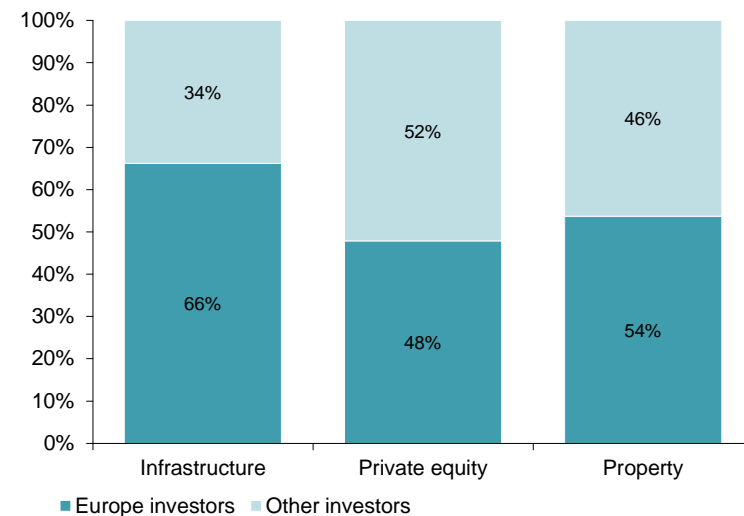
52% of all PE investors in European assets are from outside of Europe enabling global investors the opportunity to invest in a wide range of European sectors

46% of property investors are from outside Europe, signifying the attractiveness of European commercial property to non-European investors

Region of investors for Europe investments



Investor region of Europe based assets (top 3 asset classes)



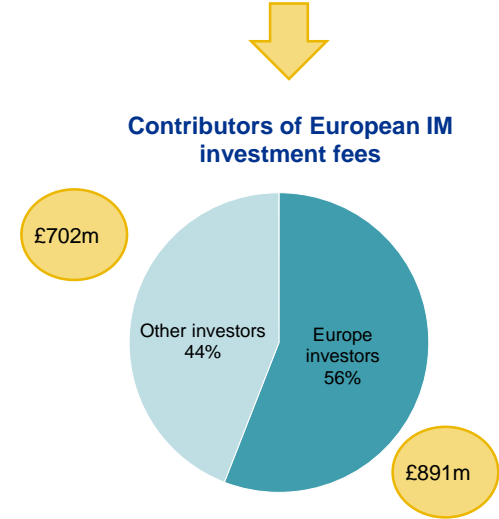
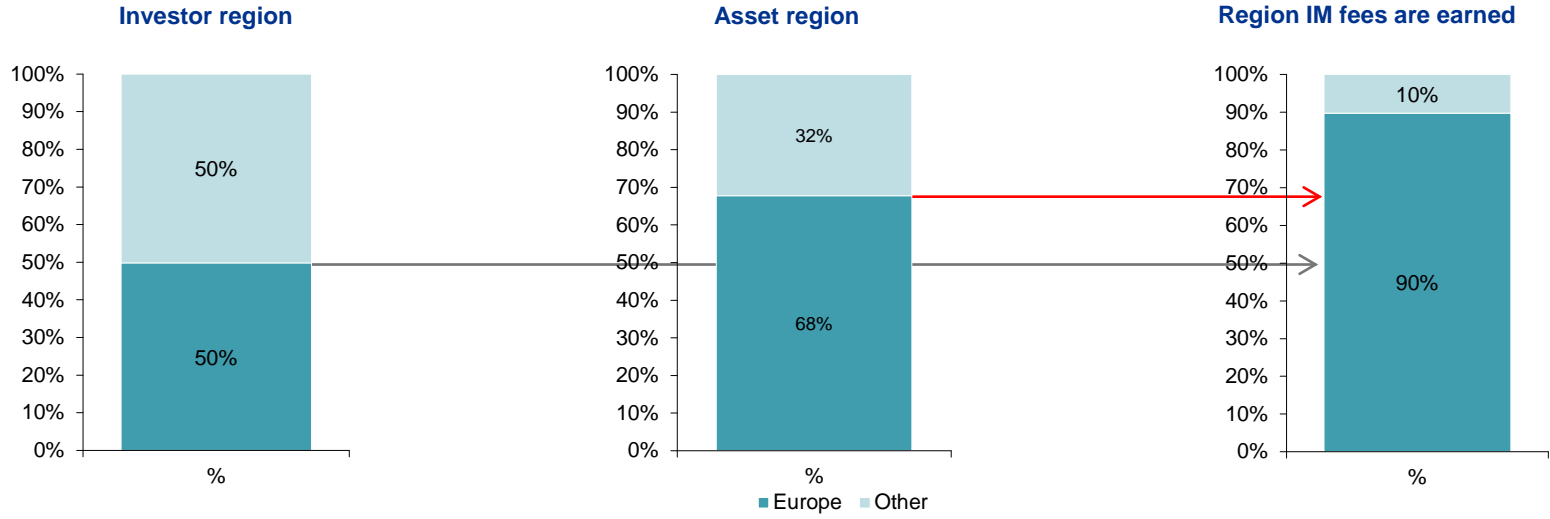
Impact on Europe - fees

Europe generates £1.6bn of IM fees from Guernsey funds

Total IM fees earned by Guernsey domiciled funds amount to £1.8bn, of which Europe earns 90% (£1.6bn) despite providing only 50% of investors and holding 68% of assets

These fees only include those services provided directly to the Guernsey fund and not any underlying portfolio companies European IM fees, where funds do not have any assets located in Europe, amount to £131.6m

Non-European investors contribute £702.6m in IM fees (44% of IM fees) to European investment companies and a total of £800m where additional investment services are included



Impact on Europe – outward investment

Guernsey assists European investors access to global investments

European investors invest a total of £77.4bn through funds in Guernsey with 30% of their assets (£23.5bn) outside Europe

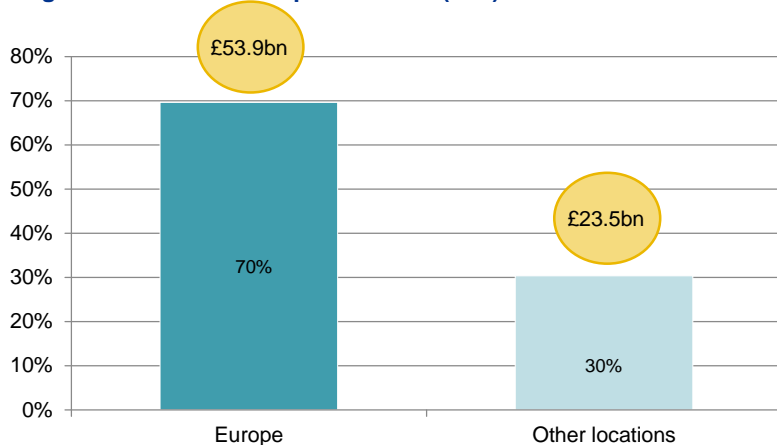
The Guernsey funds market facilitates European investors in achieving their goal of obtaining exposure to global alternative assets which they may be unable to do through alternative domiciles

European investors are predominantly institutional, pension funds, multi asset funds and private wealth managers and can achieve a better return for their underlying investors through a more efficient structure with access to a more diversified choice of investments

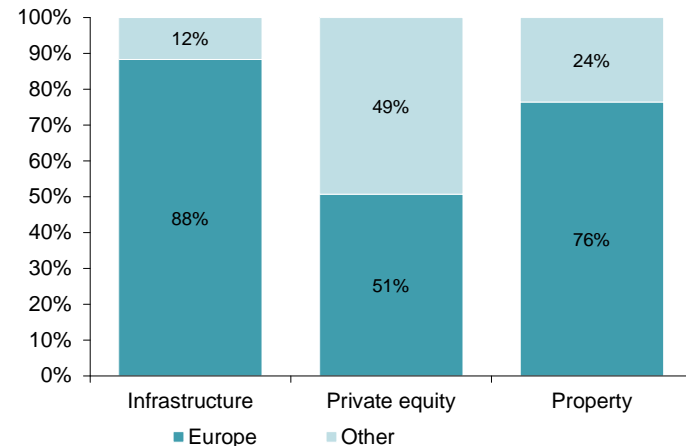
PE is the main attraction for European investors with £50.1bn invested into this asset class

The stand out asset classes for European investors inside Europe are Infrastructure and Property

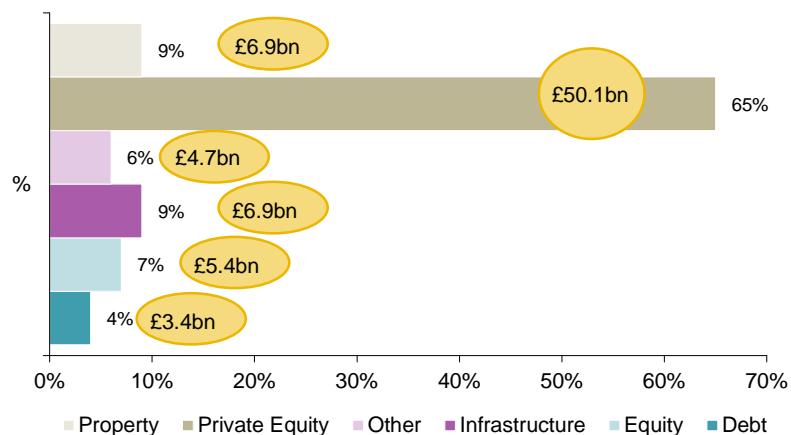
Region of assets of Europe investors (£bn)



Investment region of Europe investors (top 3 asset classes)



Class of investments by Europe investors





cutting through complexity

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