

## **AOV Costs Analysis**

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## Part 1: Background

For the assessment of value exercise, there is a need to compare the costs of the shareclass with other shareclasses of the fund, other shareclasses of the manager and other shareclasses in the market.

There is also a need to consider economies of scale.

In doing so, we need to be cognisant to not only look at the headline AMC fees but also to look at all the costs that the investor experiences.

In this document we consider the following:

- Part 2 - our approach to consideration of costs.
- Part 3 – an overview of the different costs that the investors suffer
- Part 4 – overview of regulatory requirements in respect of cost disclosures
- Part 5 – MIFID 2 Transaction Costs
- Part 6 – Extracts from the EMT

## Part 2: Conclusions - our approach to consideration of costs

In deciding on what costs to compare and with specific regard to the contents of the EMT, we have decided to

- Focus on ex ante costs
- Ignore reference to “acquired” entry and exit charges (amounts payable to fund) as these are not typical (usually payable to Manager).
- We have had limited regard to exit costs, as they are atypical in practice.

Our different shareclass are in some cases developed for specific distributors and as such may have initial charges or discounts for those advisers.

EMT Item	Description	Mandatory?
07020_Gross_One-off_cost_Financial_Instrument_maximum_entry_cost_non_acquired	This data is a maximum cost not acquired to the fund.. It is indicative and should be adapted by the distributor receiving the file to take into account the commercial agreement with the asset manager. Conditional to the existence of this feature	M
07025_Net_One-off_cost_Financial_Instrument_entry_cost	This data is optional and could be used in the event of only one layer of intermediation or in a case where distributor up fronts are paid equally to all distributors. The costs reported in this field is a Net disclosure and therefore the distributor upfront is equal to the difference between 07020 and 07025.	O
07050_One-off_costs_Financial_Instrument_maximum_exit_cost	Maximum fees not acquired to the funds that could happen at a certain time during the life of the product. Conditionnal to the existence of this feature	C
07100_Financial_Instrument_Gross_Ongoing_costs	Ongoing costs include management fees and distribution fees, and exclude transaction costs, incidental costs and performance fees	M
07110_Financial_Instrument_Management_fee	These fees are included in total on going costs. These fees are used by distributors to calculate their retrocession fees	M
07120_Financial_Instrument_Distribution_fee	Only applicable if the product has this feature (legal wording in the documentation). These fees are included in total on going costs and are not included into the management fees.	C
07130_Financial_Instrument_Transaction_costs_ex_ante	0 for structured products. Costs within the products	M
07140_Financial_Instrument_Incidental_costs_ex_ante		M

07145_Financial_Instrument_Performance_Fee_costs_ex_ante	This fee is included in total in incidental cost. Only applicable if the product has this feature or a carried interest feature	C
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Note:

- In practice we have no funds with shareclasses which charge performance fees. Therefore, we do not consider this cost.

Accordingly, in summary:

Scenario	Approach
When comparing the different shareclasses of a fund	<p>We consider, having regard to factors such as minimum dealing fees</p> <ul style="list-style-type: none"> <li>- Initial costs</li> <li>- AMC costs</li> <li>- Distribution costs</li> </ul> <p>We do not consider:</p> <ul style="list-style-type: none"> <li>- The other fund costs (custody fees, registration fees etc.)</li> <li>- Transaction costs (as these should be consistent for all shareclasses – considered separately in data quality oversight)</li> </ul>
When comparing the shareclass to other shareclasses in our fund range	<p>We consider, having regard to factors such as minimum dealing fees</p> <ul style="list-style-type: none"> <li>- Initial costs</li> <li>- AMC costs</li> <li>- Distribution costs</li> </ul> <p>We do not consider:</p> <ul style="list-style-type: none"> <li>- The other fund costs (custody fees, registration fees etc.)</li> <li>- Transaction costs (as these should be consistent for all shareclasses – considered separately in data quality oversight)</li> </ul>
When comparing the shareclass to other shareclasses in our fund range	<p>We consider, having regard to factors such as minimum dealing fees</p> <ul style="list-style-type: none"> <li>- Initial costs</li> <li>- AMC costs</li> <li>- Distribution costs</li> </ul> <p>We do not consider:</p> <ul style="list-style-type: none"> <li>- The other fund costs (custody fees, registration fees etc.)</li> <li>- Transaction costs (as these should be consistent for all shareclasses – considered separately in data quality oversight)</li> </ul>

<p>When comparing to other funds in the market</p>	<p>We consider, having regard to</p> <ul style="list-style-type: none"> <li>- Initial costs</li> <li>- AMC costs</li> <li>- Distribution costs</li> </ul> <p>We do not consider:</p> <ul style="list-style-type: none"> <li>- The other fund costs (custody fees, registration fees etc.)</li> <li>- Transaction costs (as these should be consistent for all shareclasses – considered separately in data quality oversight)</li> </ul>
<p>When considering economies of scale compared to the market</p>	<p>We consider vs the market, having regard to the different AUM sizes etc.</p> <ul style="list-style-type: none"> <li>- Our on-going costs</li> <li>- The other fund costs (custody fees, registration fees etc.)</li> <li>- Our transaction costs (although noting that these are affected by turnover)</li> <li>- Our combined on-going costs and transaction costs</li> </ul>

## Part 3 – an overview of the different costs that investors suffer,

By way of background, we consider below the total costs of investing.

			Ongoing or one off	Payable by	Payable to
1	Initial fee	This is the initial fee disclosed in the prospectus. It is an upfront cost of investing. It is often waived or discounted. This amount is paid to the Manager, not the fund.	One-off	investor	Typically to manager, rather than to fund. They are not “acquired”
2	Exit costs	These are the exit fees charged on redemption of investment. This typically only applies to large investors and typically only to redemptions within a certain time period. This amount is payable to the Manager, not the fund.	One-off	investor	Typically to manager, rather than to fund.. They are not “acquired”
3	AMC	This is the annual management charge, the fee charged by the management company as disclosed in the prospectus. This amount is paid by the fund to the Manager	Ongoing	fund	manager
4	Other fund fees	Custody, transfer agency, fund accounting, professional fees etc.	Ongoing	fund	Service provider
5	Performance fees		ongoing		
6	Distribution costs - Platform cost and adviser fees	These are the costs that an investor has to pay to access the fund through a platform or payable to IFAs etc for advising on the investment	Ongoing	investor	platform
7	Other fund expenses	Transaction costs etc, incurred by the fund Incidental costs	Ongoing	fund	Brokers etc.

\*the AMC and the other fund fees are collectively the OCF – “ongoing charges figure.”

### Specific shareclasses

As regards the distribution on platforms and IFAs, it is the case that for some distributors:

- The initial fee charge who can discount the initial fee.

**Where these costs are seen in the KIID and EMT.**

As set out in Part 4,

- the prospectus sets out information on the initial fee, AMC, Exit costs and other fund fees, as separate costs.
- The KIID sets out the ongoing charge which includes the AMC and other fund fees but not performance fees, the platform costs, adviser fees, transaction costs, incidental costs etc.
- MIFID 2 requires a range of cost disclosures.



## Part 4 – overview of regulatory requirements in respect of cost disclosures

The Disclosure of Charges is complicated and currently under-going a period of reform. Below we summarise the relevant industry disclosures:

Relevant Regulation	Summary
Prospectus	<p>The prospectus will disclose:</p> <ul style="list-style-type: none"> <li>- The AMC fee as well as any initial fee, exit fee, performance fee</li> <li>- Other fees such as custody, transfer agency fees, professional fees.</li> </ul>
KIIDs and Factsheets – the OCF	<p>Before MiFID II, the ongoing charge (OCF) was commonly used by fund managers to communicate their costs and charges.</p> <p>The ongoing charge is provided by fund managers within the Key Investor Information Document (KIID) for all UCITS funds.</p> <p><b>The OCF includes charges</b> such as the fund's <b>annual</b> management charge, registration <b>fee</b>, <b>custody fees</b> and distribution <b>cost</b> but excludes the <b>costs</b> of buying or selling assets for the fund (unless these assets are shares of another fund).</p> <p>It is similar to the Total Expense Ratio published by non-UCITS fund managers.</p> <p>This charge does not include the transaction costs</p>
MIFID 2 – PRIIPs KID, EMT and EPT	<p>MIFID II requires much more extensive cost disclosure, including in the PRIIPS KID.</p> <p>These are calculated in line with the prescribed MiFID II methodology, and include additional costs and charges which did not previously feature in the ongoing charge.</p> <p>This includes transaction costs, such as financing costs (bank interest charges, derivative financing costs).</p> <p>These costs must also be presented over different time horizons, including on an:</p> <ul style="list-style-type: none"> <li>- ex-ante (expected at the time of the investment decision); and</li> <li>- ex-post (actual accrued over a certain historic period)</li> </ul> <p>Note: the other fund charges figure (custody, registration etc.) is not</p>



## Part 5: MIFID II Transaction Costs

Question	Answer
Who needs to comply with the MifID II regulatory reporting regime	FCA regulated UCITS firm
What do the MIFID II (including PRIIPs) regulations mean for disclosure of costs and charges?	<p>The introduction of MIFID II has changed the way that costs and charges are presented for funds. A number of costs which were not included in the ongoing charge or TER are now part of the MiFID and PRIIPs requirements.</p> <p>These include transaction costs</p>
What is meant by ex-ante and ex-post costs?	<p>Ex-ante costs are the expected costs and associated charges to the fund/class.</p> <p>Ex-post costs are the actual costs incurred by the fund/class in a historic period.</p>
What are transaction costs?	<p>Transaction costs are the costs associated with buying and selling the underlying investments within a fund. These are made up of:</p> <ul style="list-style-type: none"> <li>- Explicit costs (including transaction costs);</li> <li>- Implicit (arrival) costs;</li> <li>- The impact of anti-dilution measures.</li> </ul>
How can transaction costs be negative?	They can be negative where the impact of the implicit (arrival) costs and anti-dilution measures is negative.
<b>Explicit transaction costs</b>	
What are explicit transaction costs	<p>Explicit transaction costs include, for example, broker commissions and transaction taxes paid on each purchase or sale of investments.</p> <p>Explicit transaction costs have been disclosed in fund annual financial reports for the last number of years, showing the taxes and commissions paid by the fund both as a percentage of the average fund net asset value and as a percentage of the total transaction values.</p>
What factors can influence the transaction costs figure disclosed?	<p><u>Broker commissions</u></p> <p>Broker commissions vary dependent on the type of market and the type of transaction.</p>

Question	Answer
	<ul style="list-style-type: none"> <li>• In general larger cap securities should have lower commissions than smaller cap securities.</li> <li>• Bond transactions do not have any explicit commissions.</li> </ul> <p>Note: commissions historically used to include research costs, but from the start of 2018 onwards, this cost is no longer included.</p> <p><u>Transaction Taxes</u></p> <p>For example, stamp duty in the UK is 50bps on purchases.</p> <p>A number of other markets have taxes, e.g. financial transaction taxes in France and Italy, and some emerging markets also have taxes.</p> <p><u>Portfolio Turnover</u></p> <p>Both implicit and explicit costs will increase as the portfolio turnover of a fund increases.</p>
<p><b>How is turnover calculated</b></p>	<p>The industry standard portfolio turnover rate calculation methodology only includes the turnover of physical holdings: bonds and equities. As the industry has developed and the use of derivatives has increased, the portfolio turnover rate calculation has become less relevant. Therefore, for those funds which use derivatives, the portfolio turnover rate will not include all transactions and be quite misleading, and so the costs associated with these types of funds can often be higher than the portfolio turnover rate would suggest.</p> <p>In addition, the costs of FX transactions are now included in transaction costs. These types of transactions typically do not have any explicit costs and the costs are included in the spread or all-in rate applied to the transaction. The impact of these costs will depend on the FX exposure and strategy of the fund.</p> <p>The FX transactions relating to hedged share classes are allocated to those particular share classes. The costs on these types of transactions are normally very small, but given the scale of the FX exposure on some of funds, these costs can become sizeable.</p>

Question	Answer
<b>Implicit Costs</b>	
<p>What are implicit costs / arrival costs</p>	<p>This is sometimes referred to as the arrival cost, which is the difference between the price of the transaction and the mid market price immediately before the order for the transaction was made.</p> <p><u>Implicit costs / Arrival costs</u></p> <p>In addition, the implicit costs are required to be included in the cost disclosure. This is sometimes referred to as the arrival cost, which is the difference between the price of the transaction and the mid market price immediately before the order for the transaction was made.</p> <p>Implicit costs can be positive or negative, and they can vary depending on the type of instrument. For example, large cap equities can often be traded almost instantly, whereas smaller cap equities can take longer to trade, which means that the price has more opportunity to change from the point the order is placed to the time it is executed. This movement could go in the fund's favour, resulting in a negative cost. This difference in liquidity also impacts the bid-offer spread, with large cap equities having lower spreads than small cap equities.</p> <p>This arrival price methodology only became mandatory for PRIIPs from January 2018, and before this date a number of different approaches were taken to provide a historic estimate of implicit costs.</p>
<p>Is the arrival price method mandatory</p>	<p>This arrival price methodology only became mandatory for PRIIPs from January 2018, and before this date a number of different approaches were taken to provide a historic estimate of implicit costs.</p>
<p>Why is the arrival methodology controversial</p>	<p>It has been widely reported in the industry press, that some asset managers have adopted the PRIIPS slippage methodology, which has led to the disclosure of negative transaction costs on a number of funds, whilst other funds have reported costs which appear to be excessively high. These anomalies are thought to be a result of unreliable historic arrival price data provided by data vendors.</p>

Question	Answer
	Accordingly, distributors face challenges when comparing the fund transaction costs of different asset managers.
How can implicit costs be negative	Implicit costs can be positive or negative, and they can vary depending on the type of instrument. For example, large cap equities can often be traded almost instantly, whereas smaller cap equities can take longer to trade, which means that the price has more opportunity to change from the point the order is placed to the time it is executed. This movement could go in the fund's favour, resulting in a negative cost. This difference in liquidity also impacts the bid-offer spread, with large cap equities having lower spreads than small cap equities.
<b>Anti-Dilution Measures</b>	
What are anti-dilution measures and how are they taken into account	<p>Where a fund employs anti-dilution techniques, these techniques can be offset against the total transaction costs of the fund/class.</p> <ul style="list-style-type: none"> <li>• Dual priced funds, a daily adjustment is included based on the net dealing into and out of each particular fund; and</li> <li>• On the single-priced funds, when the price is swung, the dilution adjustments made are offset against the transaction costs.</li> </ul>

**PRIIPs transaction cost calculation also required for Mi**

**Estimate per PRIIPs asset class**

Transaction costs =  $\frac{\text{Cost per each asset class}}{\text{Estimate of portfolio turnover in each asset class}}$

Costs per PRIIP asset class

- ▶ NON-OTC products: use of index constituents data
- ▶ OTC-products: survey

Turnover

- ▶ Deriving turnover per each PRIIP asset class by classifying each transaction into an asset class

**Arrival price method**

Actual costs per transaction =  $\frac{\text{Purchase/sale}}{-1/1} \times \left[ \frac{\text{Net realized execution price of the transaction} - \text{Arrival price}}{\text{Units}} \right]$

Arrival price

- ▶ At the time, when trade has been transmitted to the market
- ▶ Sourcing of opening prices and bid and ask price ticks
- ▶ Heavy effort to collect and to push data through the value chain

## Part 6: Extracts from the EMT

Field and Use	Used	example	Explanation	Relevant field for Funds-Axis AOV
AMC		0.85		Used
07010_Structured_Securities_Quotation	No		Specific to structured products	Not currently used
07020_One-off_cost_Financial_Instrument_entry_cost		0.05		Use calculated field "Entry Costs"
07030_One-off_cost_Financial_Instrument_maximum_entry_cost_fixed_amount_Italy	No	0	Specific to Italy	Not currently used
07040_One-off_cost_Financial_Instrument_maximum_entry_cost_acquired		0		
07050_One-off_costs_Financial_Instrument_maximum_exit_cost		0		Use calculated field "Exit costs"
07060_One-off_costs_Financial_Instrument_maximum_exit_cost_fixed_amount_Italy	No	0	Specific to Italy	Not currently used
07070_One-off_costs_Financial_Instrument_maximum_exit_cost_acquired		0		
07080_One-off_costs_Financial_Instrument_Typical_exit_cost		0		
07090_One-off_cost_Financial_Instrument_exit_cost_structured_securities_prior_RHP	No		Specific to structured products	Not currently used
07100_Financial_Instrument_Ongoing_costs		0.0213		Use calculated field "On-going costs"
07110_Financial_Instrument_Management_fee		0.0085		
07120_Financial_Instrument_Distribution_fee		0.0085		
07130_Financial_Instrument_Transaction_costs_ex_ante		0.0044		Use calculated field "Transaction costs"

07140_Financial_Instrument_Incidental_costs_ex_ante		0		Use calculated field "Incidental costs"
08010_One-off_cost_Structured_Securities_entry_cost_ex_post	No		Specific to structured products	Not currently used
08020_One-off_costs_Structured_Securities_exit_cost_ex_post	No		Specific to structured products	Not currently used
08030_Financial_Instrument_Ongoing_costs_ex_post		0.0213		
08040_Structured_Securities_Ongoing_costs_ex_post_accumulated	No		Specific to structured products	Not currently used
08050_Financial_Instrument_Management_fee_ex_post		0.0085		
08060_Financial_Instrument_Distribution_fee_ex_post		0.0085		
08070_Financial_Instrument_Transaction_costs_ex_post		0.0044		
08080_Financial_Instrument_Incidental_costs_ex_post		0		

**END**