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Ongoing Charges for UCITS in the European Union, 2022

KEY FINDINGS

» **Average ongoing charges for equity and fixed-income UCITS have declined since 2013.** In 2022, the average ongoing charges for equity and fixed-income UCITS were down 21 percent and 32 percent, respectively, from 2013.

» **The downward trend in average ongoing charges for equity and fixed-income UCITS continued in 2022.** The average ongoing charge for equity UCITS fell 3 basis points from 1.21 percent in 2021 to 1.18 percent in 2022; the average ongoing charge for fixed-income UCITS fell 2 basis points from 0.69 percent in 2021 to 0.67 percent in 2022.

» **Investors tend to concentrate their assets in lower-cost UCITS.** In 2022, the simple average ongoing charge for all equity UCITS was 1.38 percent, compared with an asset-weighted average of 1.18 percent. The simple average ongoing charge can overstate what investors actually paid because it fails to reflect the fact that investors tend to concentrate their holdings in lower-cost funds.

» **Retail investors still pay for the cost of distribution even when it is not included in the total ongoing charge.** Direct comparisons of average ongoing charges between UCITS share classes that "bundle" distribution in the ongoing charge with those that "unbundle" distribution from the ongoing charge can be misleading. In unbundled share classes, retail investors typically pay distribution costs directly out of pocket.

» **Average ongoing charges for equity and fixed-income UCITS ETFs have decreased since 2013.** In 2022, the average ongoing charges for equity and fixed-income UCITS ETFs were down 41 percent and 20 percent, respectively, from 2013.

» **Cross-border UCITS provide European investors with a much larger range of investment options, but such funds often incur additional marketing or registration costs.** In 2022, the average ongoing charge for cross-border equity funds was 1.34 percent compared with 1.23 percent for single country equity funds.

What's Inside

James Duvall, Economist, Eva Mykolenko, Associate Chief Counsel of Securities Regulation, Casey Rybak, Senior Research Associate, and Shane Worner, Senior Economist, prepared this report.

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For a complete set of data files for each figure in this report, see www.ici.org/files/2023/per29-08-data.xlsx.

The following conditions, unless otherwise specified, apply to all data in this report: (1) UCITS that invest primarily in other funds are excluded from the data to avoid double counting, (2) UCITS not domiciled in the European Union (EU) (i.e., UK UCITS and UCITS in Iceland, Liechtenstein, and Norway), in addition to UCITS domiciled in the Netherlands, are excluded from data for ongoing charges, (3) UCITS primarily intended for sale in the United Kingdom and the Netherlands are excluded from data for ongoing charges, and (4) euros and percentages may not add to the totals presented because of rounding. In addition, for simplicity, this report will sometimes use "funds" to refer to Undertakings for Collective Investment in Transferable Securities (UCITS).

Introduction

The UCITS[1] Directive has become a global success story since it was first adopted in 1985. Net assets in UCITS domiciled in the European Union and the United Kingdom were €11.1 trillion at year-end 2022 (Figure 1).[2] Investments in these funds are held by investors from Europe and other jurisdictions worldwide.[3]

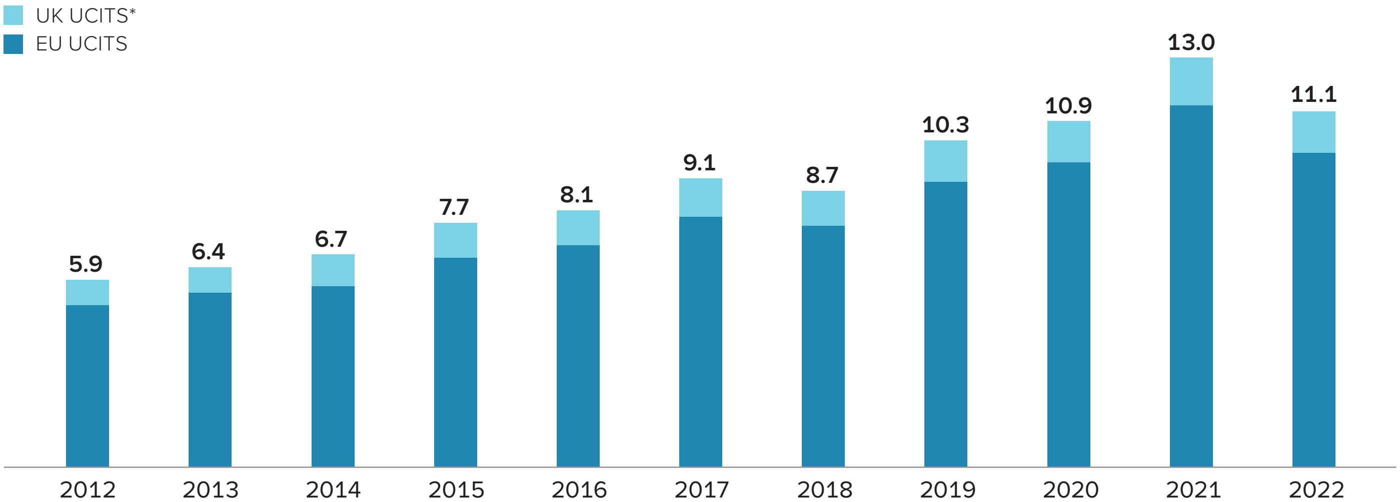
UCITS provide many important advantages to investors, including professional management services, access to global markets, the benefit of regulation and supervisory oversight, and access to a wide array of investment options via "passporting." For example, investors in equity UCITS had access to more than 120 different investment objectives with €4.5 trillion in net assets at year-end 2022.

UCITS investors incur ongoing charges that cover a host of services, including portfolio management, administration, compliance costs, accounting services, legal costs, and payments to distributors. The total cost of these charges is disclosed to investors through either the total expense ratio (TER), often found in a UCITS' annual report and other disclosures and marketing documents, or the ongoing charges figure (OCF), found in the UCITS Key Investor Information Document (KIID) or Packaged Retail and Insurance-Based Investment Products (PRIIPs) Key Information Document (KID).[4] Ongoing charges among UCITS vary, and these differences depend on a variety of factors. Because ongoing charges are paid from fund assets, investors pay for the investment-related services associated with them indirectly. The way in which fund costs are disclosed to investors has changed over time as regulation, industry practice, and the distribution landscape have evolved.[5, 6]

FIGURE 1

Net Assets of UCITS in the European Union Fell in 2022

Trillions of euros, year-end



* UK UCITS are included in total net assets because UK UCITS regulation currently aligns with EU UCITS regulation.

Note: Data include money market funds, exchange-traded funds, and UCITS that invest primarily in other funds.

Source: European Fund and Asset Management Association (EFAMA) 2023

Other Costs Investors May Pay for Investing in UCITS

In addition to ongoing charges, investors may pay one-off costs—entry and exit costs—when purchasing or selling shares or units of a UCITS.[7] One-off costs are calculated as a percentage of the sales or offering price of a fund share class and are taken directly from the investment amount. Investors also indirectly pay costs, such as transaction costs, which the fund may naturally incur when it trades its underlying assets,[8] and other costs associated with the management of the fund, such as payments for investment research that may either be paid by the UCITS manager or by fund shareholders (if properly disclosed).[9]

Entry costs are paid by investors at the time of share purchase (or on subsequent share purchases) to compensate financial professionals for assistance. These costs are reported as some maximum value, as advisers or distributors often waive all or a portion of the entry cost for investors who meet certain criteria (such as meeting a minimum initial investment threshold). In 2022, maximum entry costs were most commonly set to 3 percent or 5 percent, and about 56 percent of UCITS share classes reserved the option to charge an entry cost.[10]

Exit costs are paid by investors upon sale of their investments.[11] These costs are also reported as some maximum value, as advisers often waive these costs if an investor has remained in the fund for some minimum length of time. In 2022, maximum exit costs were most commonly set to 1 percent or 3 percent, and about 6 percent of share classes reserved the option to charge an exit cost.[12]

Transaction costs may be incurred by UCITS from the purchase or sale of their investments. Some examples of such costs include explicit costs, such as exchange fees and transaction taxes, and implicit costs around the market impact—the amount the price of a security may change when making a large trade—of buying and selling securities.[13] These costs affect the return an investor receives and are paid indirectly. According to recently available data, the median transaction cost was 0.14 percent of a fund's net assets.[14, 15]

UCITS Share Classes

Share classes are an efficient mechanism through which a UCITS can provide different features to investors based on their preferences.[16] For instance, a UCITS can offer share classes based on whether the income generated by the fund's portfolio investments is reinvested (often identified as "accumulation" shares) or distributed to the investor (often identified as "income" or "distributed" shares). Also, many UCITS offer share classes denominated in various currencies to appeal to local preferences of investors in different countries. Some UCITS offer share classes that hedge against certain factors, such as currency risk or interest rate risk.[17] Some of these types of share classes require different levels of management than others (e.g., hedging can be costly), and therefore the management fee may be different among share classes. The average UCITS had 6 share classes in 2022, with some funds having 50 share classes or more.[18]

UCITS also use multiple categories of share classes with different costs and charges to appeal to specific types of investors (such as retail and institutional investors). For example, ongoing charges may differ between UCITS share classes based on how investors pay for distribution (e.g., commission payments to an investment professional for advice).

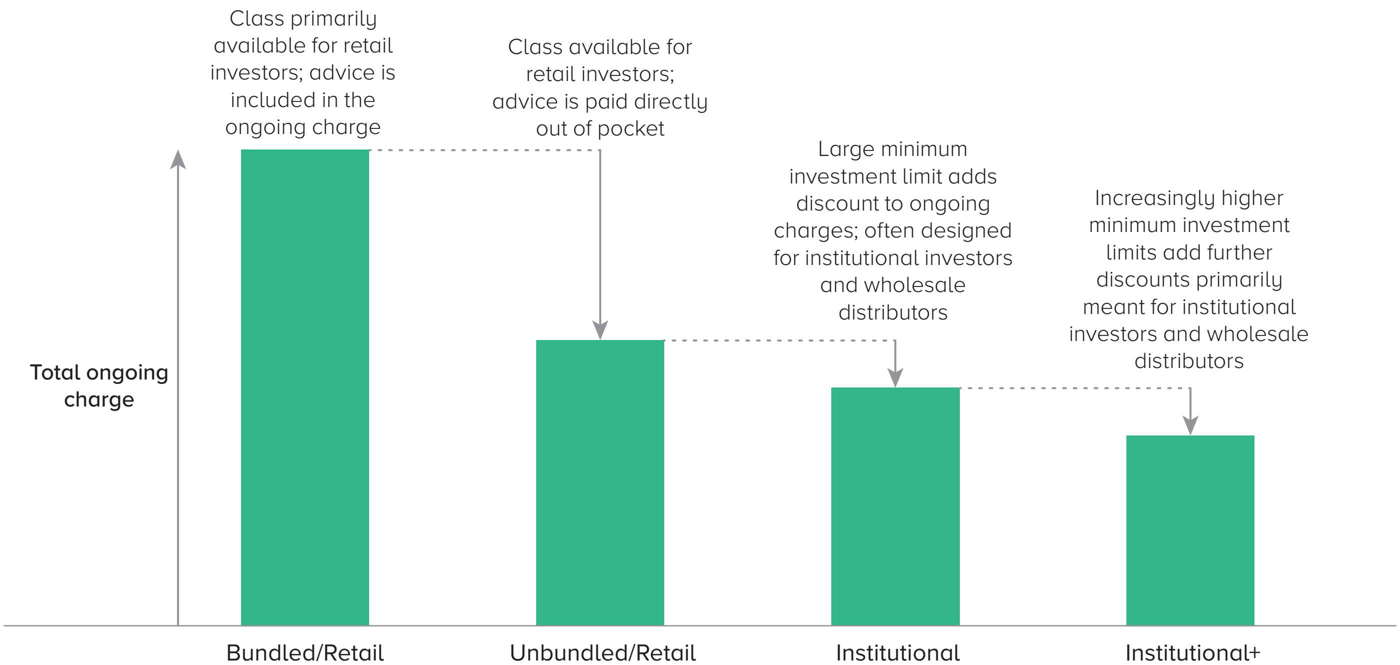
Distribution costs may be *bundled*, meaning they are included in the ongoing charge of the share class (Figure 2). Bundled share classes are traditionally offered to retail investors with small accounts, and ongoing charges sometimes differ in these share classes based on whether an entry cost is charged. For investors who rely heavily on the advice of their investment professionals, bundled share classes can offer a cost-effective way to pay for those services.

Distribution costs also may be *unbundled*,[19] meaning that the ongoing charge is devoid of commissions and investors pay for advice through an asset-based fee that comes directly out of the investor's pocket (Figure 2). Unbundled share classes were traditionally offered to institutional investors or retail investors with large account balances (e.g., high net worth individuals). However, many UCITS now offer at least one unbundled share class intended for retail investors with small accounts, or those who contact or meet with their investment professionals on a limited basis.

The number of unbundled share class offerings for retail investors has increased in recent years, as regulators and policymakers have encouraged advisers to move toward fee-based advice. The UK Retail Distribution Review (RDR) and the Netherlands' Authority for Financial Markets (AFM) banned intermediary commission payments—both with implementation dates of January 1, 2013—from being included in the ongoing charge. Under certain circumstances, MiFID II banned intermediary commission payments for UCITS as of January 3, 2018.[20]

FIGURE 2

Ongoing Charges Are Different for Various Types of UCITS Investors



Source: Investment Company Institute

EU Retail Investment Strategy and a Focus on "Undue Costs"

The UCITS Directive does not specify the fees and costs that a UCITS may charge. The UCITS Level 2 Directive, adopted in 2010,[21] however, obligates Member State regulators to require management companies to act in such a way as to prevent undue costs from being charged to the UCITS and its unit-holders. In mid-May 2023, the European Securities and Markets Authority (ESMA) issued an opinion setting out suggestions to the European Commission for possible clarifications of the legislative provisions under the UCITS Directive and the Alternative Investment Fund Managers Directive (AIFMD) relating to the notion of "undue costs."

On May 24, 2023, the European Commission published a legislative proposal on the Retail Investment Strategy (RIS) with comprehensive reforms to the EU framework for retail investors through revisions to multiple legislations, including the UCITS Directive, MiFID II, and PRIIPs. The RIS proposal includes new requirements and enhancements to the investor protection framework in a wide range of areas, including undue costs and value for money, simplifying disclosures, a ban on inducements paid from manufacturers to distributors for execution-only sales, an enhanced best interest standard, stricter rules on marketing communications, enhanced standards for wealth managers, and strengthened supervisory enforcement.

As part of the RIS, the Commission has proposed changes to the UCITS Directive and AIFMD to insert a value-for-money assessment framework that would require management companies to have an internal pricing process to ensure that no undue costs are charged to funds or their investors and that the costs are justified and proportionate. Under the proposal, as part of the fund's pricing process, the management company would be required to compare the fund's costs with a cost and performance benchmark to be developed by ESMA. A deviation from the relevant benchmark would introduce a presumption that the costs and charges are too high and that the fund will not deliver value for money, unless it can be demonstrated otherwise. The proposal does not specify how such a cost and performance benchmark would be constructed.

The European co-legislators have begun their deliberations on the RIS. It is too early to know what changes will ultimately be included in the final agreement, which is not expected until late 2024 or early 2025.

UCITS adapted to these rules in different ways. Some added unbundled share classes specifically for new retail investors, while others simply waived or removed the minimum investment limits on their preexisting unbundled or institutional share classes.

Share classes primarily intended for institutional investors generally have substantial minimum investment amounts such as €100,000 or €1 million (Figure 2). Further, some UCITS offer multiple share classes with increasingly higher minimum investment limits (e.g., €5 million, €10 million, or even €100 million), but progressively lower ongoing charges (referred to as institutional+ share classes in Figure 2). Some institutional+ share classes are meant for very specific types of accounts, such as those that are distributed through wholesalers (e.g., packaged with other investment products) or those that combine the accounts of a large number of individual retail investors.

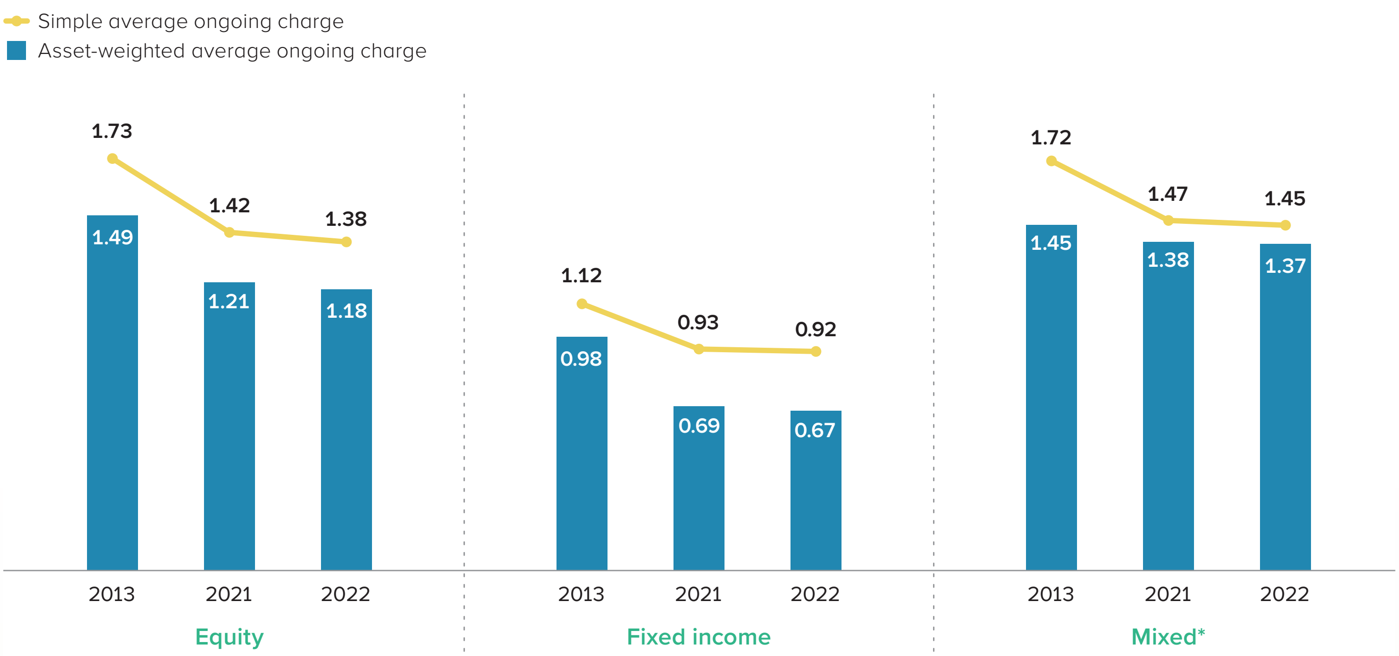
UCITS Investors Are Concentrated in Lower-Cost Funds

On an asset-weighted basis,[22] average ongoing charges paid by investors in equity and fixed-income UCITS have decreased since 2013 (Figure 3).[23, 24] In 2013, the asset-weighted average ongoing charge for equity funds was 1.49 percent, or €1.49 for every €100 in assets. By 2022, the asset-weighted average was 21 percent lower, falling to 1.18 percent.[25] Asset-weighted average ongoing charges also declined for fixed-income funds, falling 32 percent from 0.98 percent in 2013 to 0.67 percent in 2022. Average ongoing charges for mixed funds have decreased modestly over this same period—1.45 percent in 2013 compared with 1.37 percent in 2022.[26]

FIGURE 3

Investors in UCITS Pay Below-Average Ongoing Charges

Percent



* Mixed funds invest in a combination of equity and fixed-income securities.

Note: Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

In each year from 2013 to 2022, the asset-weighted average ongoing charges for equity, fixed-income, and mixed funds were below their respective simple averages, showing that investors tend to concentrate their assets in lower-cost funds. For example, the simple average ongoing charge for equity funds was 1.38 percent in 2022, compared with an asset-weighted average of 1.18 percent (Figure 3).

Asset-weighted average ongoing charges of UCITS may fall in any given year for a variety of reasons:

- Ongoing charges of individual funds may have fallen
- Assets may have shifted to lower-cost funds
- New, lower-cost funds may have entered the market
- Higher-cost funds may have left the market

Most of the decline in average ongoing charges of equity and fixed-income UCITS since 2013 is from assets shifting to lower-cost funds, lower-cost funds entering the market, and higher-cost funds exiting the market. This does not mean, however, that the ongoing charges of individual equity and fixed-income UCITS have been unchanged. In 2022, 28 percent of equity UCITS saw their ongoing charges decrease, while 17 percent saw their ongoing charges increase (Figure 4). Similarly, 25 percent of fixed-income UCITS saw their ongoing charges decrease in 2022, compared to 19 percent that increased.

One way to gauge whether assets are shifting to lower-cost funds is to examine the concentration of assets in lower-cost UCITS over time. Figure 5 shows the percentage of assets in equity and fixed-income UCITS with ongoing charges in the lowest quartile of all equity and fixed-income funds from 2013 to 2022. The share of assets among funds with ongoing charges in the lowest quartile has increased since 2013. In 2022, 36 percent of the net assets in equity UCITS were in those among the lowest quartile of ongoing charges, up from 28 percent in 2013. For fixed-income UCITS, 44 percent of net assets in 2022 were in funds among the lowest quartile of ongoing charges, up from 31 percent in 2013.

The entry of lower-cost funds and the exit of higher-cost funds (through liquidation or merger) likely also has contributed to the downward pressure on asset-weighted average ongoing charges for equity and fixed-income UCITS. Since 2013, simple average ongoing charges for newly opened funds and fund share classes have trended down (Figure 6). As distributors adapted to the MiFID II rules, some UCITS created new unbundled share classes for retail clients, which naturally had lower ongoing charges (see Figure 2). Additionally, new index tracking UCITS, which generally have lower ongoing charges, have opened to meet increased demand for index funds (see page 15). At the same time, simple average ongoing charges for funds exiting the industry by liquidating or merging were higher than those of newly opened funds in the same year.

FIGURE 4

How Ongoing Charges of UCITS Share Classes Changed in 2022

	Percentage of total share classes for which expense ratios in 2022:		
Category	*Fell*	*Were unchanged*	*Rose*
Equity	28	55	17
Fixed income	25	56	19

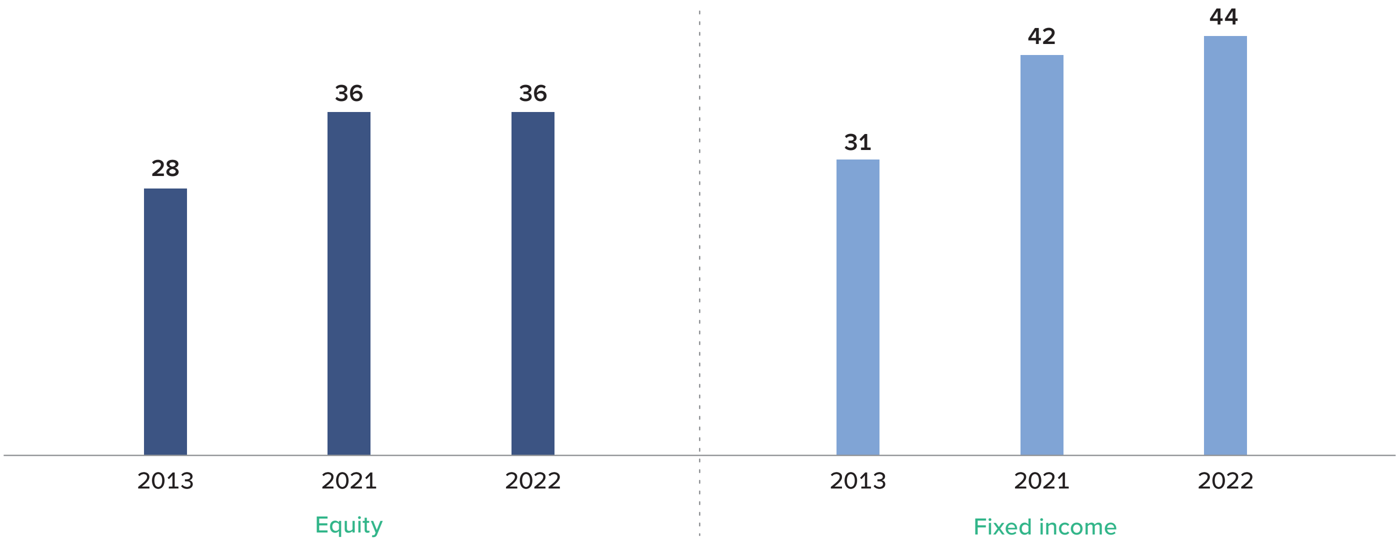
Note: Calculations are based on a consistent sample; that is, a share class must have existed in both 2021 and 2022.

Source: Investment Company Institute calculations of Morningstar Direct data

FIGURE 5

Investors Generally Concentrate Their Assets in Lower-Cost UCITS

Percentage of UCITS net assets with ongoing charges in the lowest quartile



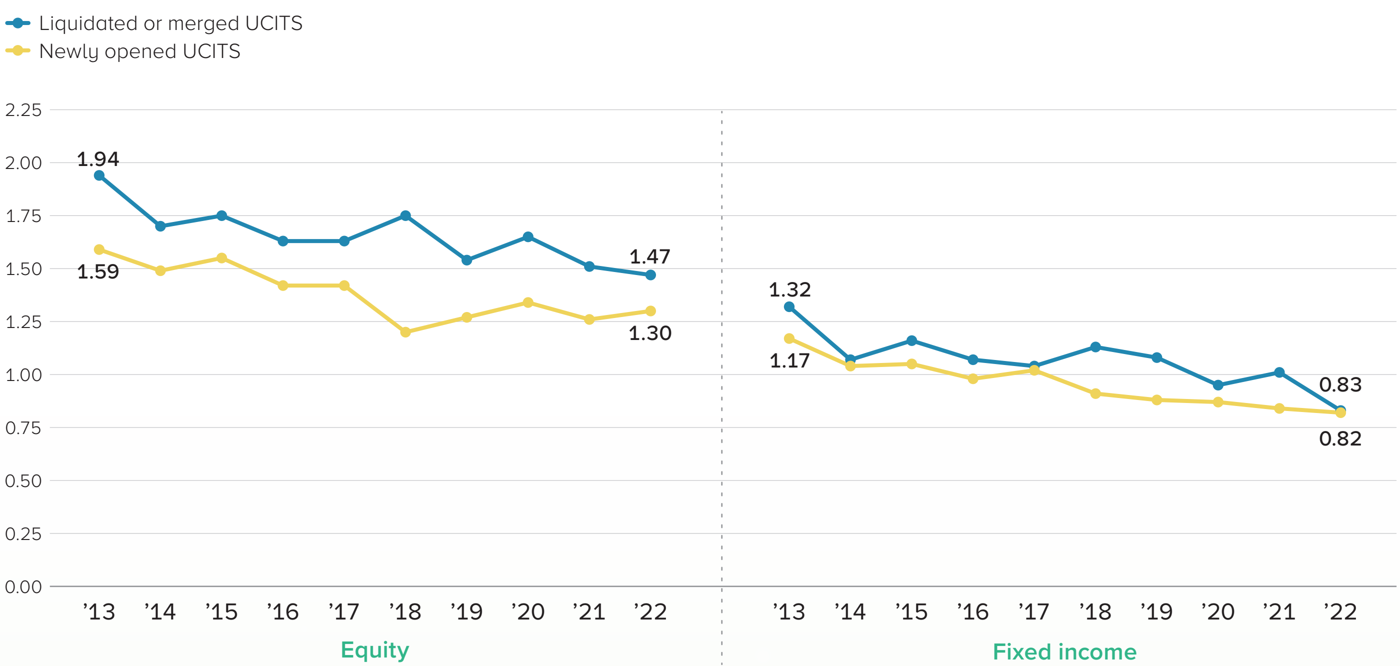
Note: Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

FIGURE 6

Simple Average Ongoing Charges of Newly Opened UCITS Have Trended Downward

Percent



Note: Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

Ongoing Charges Vary Across UCITS

Like prices of most goods and services, ongoing charges of individual UCITS vary considerably across the array of available products. Outside of distribution structures (or compensation arrangements), there are many factors that affect the ongoing charge of a UCITS share class, including investment objective, fund assets, cross-border availability, and whether the fund is actively managed or tracks an index.

UCITS Investment Objectives

Ongoing charges for UCITS differ based on their investment objectives (Figure 7).[27, 28] For example, fixed-income funds tend to have lower ongoing charges than equity funds. Among equity funds, ongoing charges tend to be higher for funds that invest in a given sector, such as health care or real estate, or those that invest in mid- and small-cap stocks, because such funds tend to cost more to manage. Additionally, ongoing charges can vary considerably even within a particular investment objective. For example, 10 percent of emerging market fixed-income funds have an ongoing charge of 0.39 percent or less, while another 10 percent have ongoing charges of 1.93 percent or more. This variation reflects, among other things, the fact that portfolios of emerging market securities can be substantially different from one another. Some funds might invest solely in one emerging market economy, while others may spread out their investments across many countries. This distinction is important because investing in certain countries can cost more to manage as information may be less readily available or access to certain markets might be difficult (or costly) to obtain.

FIGURE 7

UCITS Ongoing Charges Vary Across Investment Objectives

Percent, 2022

Investment objective	10th percentile	Median	90th percentile	Asset-weighted average	Simple average
Equity	**0.48**	**1.25**	**2.33**	**1.18**	**1.38**
Europe equity large-cap	0.40	1.19	2.24	1.14	1.30
Europe equity mid/small-cap	0.72	1.51	2.45	1.54	1.55
US equity large cap	0.34	1.04	2.21	0.93	1.23
Global equity large cap	0.42	1.11	2.16	1.08	1.27
Sector equity	0.71	1.43	2.38	1.54	1.49
Fixed income	**0.26**	**0.80**	**1.67**	**0.67**	**0.92**
Europe fixed income	0.20	0.63	1.39	0.53	0.74
EUR government bond	0.16	0.47	1.10	0.44	0.58
US fixed income	0.31	0.85	1.80	0.72	0.97
Global fixed income	0.29	0.80	1.62	0.80	0.92
Emerging market fixed income	0.39	1.01	1.93	0.80	1.14
Mixed*	**0.65**	**1.44**	**2.25**	**1.37**	**1.45**
Money market	**0.05**	**0.14**	**0.45**	**0.13**	**0.21**
Memo:					
Index equity	**0.08**	**0.29**	**0.74**	**0.25**	**0.36**

* Mixed funds invest in a combination of equity and fixed-income securities.

Note: Each share class is weighted equally for the median, 10th, and 90th percentiles. Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

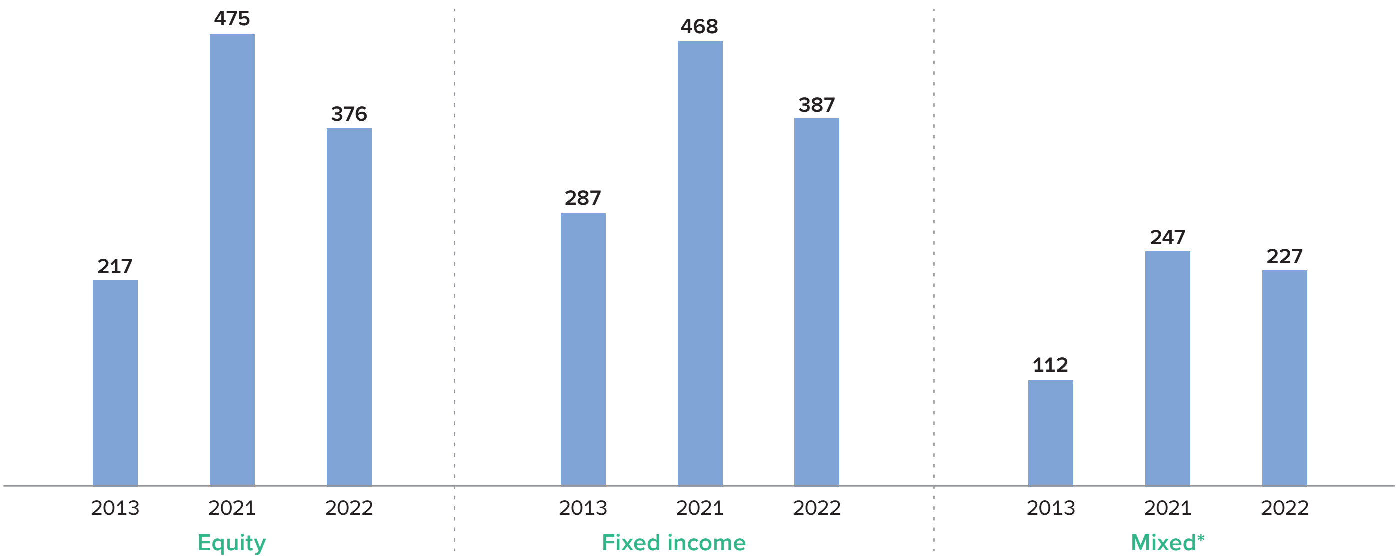
Fund Size

The amount of net assets in a fund is another important element that affects ongoing charges because of economies of scale. Some fund costs—such as transfer agency fees, accounting and audit fees, and depository fees—are relatively fixed in euro terms, regardless of fund size. Growth in a fund's net assets places downward pressure on average ongoing charges as fixed costs become an increasingly smaller share of net assets. The average size of equity, fixed-income, and mixed UCITS in 2022 were all higher than in 2013—this growth in assets explains part of the decline in average ongoing charges over the period (Figure 8). For example, in 2022, the average size of equity funds was €376 million, compared with €217 million in 2013.

FIGURE 8

Average Net Assets of UCITS Fell in 2022

Millions of euros, year-end



* Mixed funds invest in a combination of equity and fixed-income securities.

Note: Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

Average Ongoing Charges in 2022

In 2022, the average ongoing charge of equity UCITS decreased 3 basis points to 1.18 percent. Uncertainty around several macroeconomic factors (e.g., Russia's invasion of Ukraine, ongoing global supply chain issues, high inflation, rising interest rates, and a general concern of a global economic slow-down) contributed to an 18 percent decrease in the total return on global stocks in 2022.[29] This uncertainty led to estimated net cash outflows of €94 billion for equity UCITS, and net assets decreased nearly 20 percent to €3.8 trillion by year-end. One would expect that a decrease in overall assets would increase costs, since fixed costs (e.g., accounting fees) are spread across a smaller asset base. In 2022, this does not seem to be the case. Despite the down markets, competition among equity UCITS remained strong and funds continued to face pressure to lower their expense ratios as the popularity of index UCITS and exchange-traded funds (ETFs) continued to grow. Demand for lower-cost equity funds also contributed to the overall decrease in average ongoing charges. Even though equity funds saw outflows, in aggregate, global and US large-cap equity funds—which tend to have lower ongoing charges (see Figure 7 on page 10)—experienced aggregate net inflows of €24 billion. Together, these factors helped pull down the asset-weighted average equity UCITS ongoing charge in 2022.

The average ongoing charge for fixed-income UCITS decreased from 0.69 percent in 2021 to 0.67 percent in 2022. With the ECB raising interest rates in 2022 to combat rising inflation, investment grade European bonds experienced capital losses of 14 percent[30] and fixed-income UCITS saw estimated net cash outflows of €135 billion. Accordingly, net assets of fixed-income funds fell about €480 billion to €2.2 trillion by year-end 2022. This sharp decrease in fixed-income fund net assets would typically put upward pressure on their expense ratios, but demand for low-cost fixed-income funds more than offset this. In particular, euro-denominated government bond funds and index tracking funds had €16 billion and €21 billion in net inflows, respectively, and these types of funds tend to have the lowest ongoing charges among fixed-income UCITS (see Figures 7 and 12). The positive demand for these funds helped put downward pressure on the asset-weighted average ongoing charge for fixed-income UCITS.

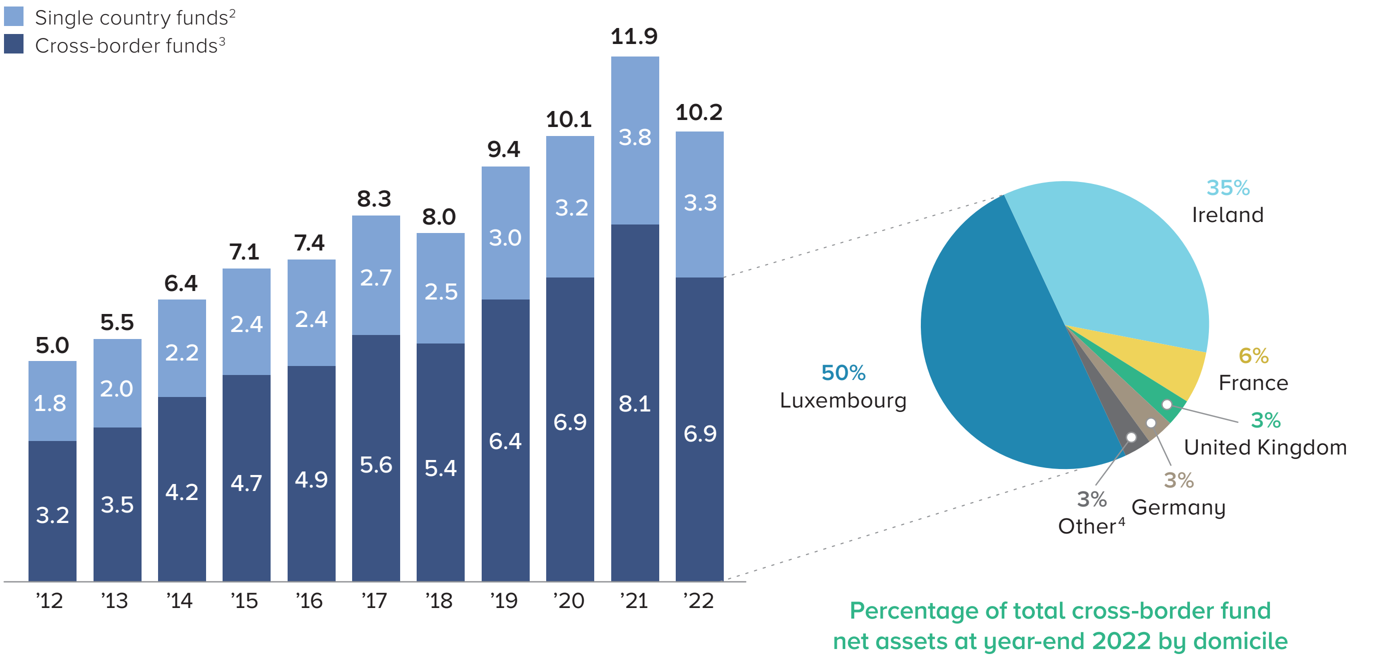
Cross-Border Distribution

The growth of UCITS in the European Union owes much of its success to EU passporting; that is, a UCITS established in one country can be sold cross-border into one or more other European countries.[31] By year-end 2022, net assets of cross-border funds domiciled in the European Union and the United Kingdom were €6.9 trillion (Figure 9),[32] 85 percent of which was domiciled in Luxembourg and Ireland. Cross-border funds also have been approved for sale in jurisdictions outside of Europe with a large degree of success—about 26 percent of net assets in UCITS and alternative investment funds (AIFs) were held by investors outside of Europe in 2022.[33]

FIGURE 9

Cross-Border Funds Represent Two-Thirds of Total UCITS Net Assets

Total UCITS net assets in trillions of euros,[1] year-end



[1] Total UCITS net assets reported by Morningstar in this figure are less than those reported to EFAMA by its member countries as shown in Figure 1. Part of the difference is attributable to the exclusion of UCITS that invest primarily in other funds in the Morningstar data. While UCITS net assets in Morningstar data are still lower than those reported by EFAMA after this adjustment, Morningstar has more detail on cross-border availability for individual funds, which is necessary for ICI's identification of cross-border funds.

[2] Single country funds include funds registered and available for sale in one country. Single country funds also include round-trip funds—funds domiciled in one country but primarily intended for sale in a different country.

[3] Cross-border funds are defined as funds registered and available for sale in three or more countries.

[4] *Other* includes Sweden, Belgium, Austria, the Netherlands, Finland, Denmark, Malta, Slovenia, Estonia, Latvia, Lithuania, and Spain

Note: Data include UCITS domiciled in the United Kingdom and the Netherlands (representing 12 percent of net assets at year-end 2022). Data also include exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

An important distinction from cross-border funds are "round-trip" funds—UCITS that are domiciled in one country but primarily intended for sale in only one other country.[34] For example, as Luxembourg grew in popularity as a prominent cross-border fund domicile, asset managers in some EU Member States domiciled their funds in Luxembourg with the sole intent to sell those funds in their home country. This report treats round-trip funds as single country funds because they are only intended to be sold in one country. Round-trip funds were 29 percent of the €3.3 trillion in net assets of single country funds at year-end 2022.

The availability of cross-border funds in Europe has many benefits for investors. For example, cross-border funds provide European investors with additional options over other investment products in their home countries, which helps foster competition. Additionally, being available for sale in multiple countries gives cross-border funds access to more investors—allowing cross-border funds to gain economies of scale. Indeed, the average size of a cross-border equity fund was €504 million, more than twice the average size of a single country equity fund (€233 million).

Nevertheless, ongoing charges in cross-border funds tend to be higher than for single country funds in part because average fixed costs in cross-border funds tend to be larger (Figure 10). For example, most EU Member States impose local requirements on the marketing of cross-border funds, thereby incurring costs for funds in each country in which they are registered and available for sale.[35] There are also additional administration costs to cover the complexity of offering different share classes in different countries, which are often in different currencies.[36] Recent reforms have attempted to converge or remove local requirements imposed on cross-border funds by EU Member States. However, some EU Member States have sought to maintain or even strengthen the requirements they impose.

FIGURE 10

Fixed Costs Tend to Be Larger for Cross-Border Funds

Percent

[1] Cross-border funds are defined as funds registered and available for sale in three or more countries.

[2] Single country funds include funds registered and available for sale in one country. Single country funds also include round-trip funds—funds domiciled in one country but primarily intended for sale in a different country.

Note: Fixed costs are estimated as the difference between the simple average ongoing charge and the simple average management cost. Data exclude funds with performance fees because the performance fee cannot be separately excluded from the total expense ratio. Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

Index Trackers

Index trackers generally seek to replicate the return on a specified index. Under this approach, portfolio managers buy and hold all, or a representative sample of, the securities in their target indexes. Index tracking funds tend to have below-average ongoing charges for a couple of reasons. First, their general approach to replicating the return on a target index lends itself to being less costly. This is because portfolios of index tracking funds tend not to change frequently, and therefore have lower turnover rates. Second, index tracking funds are larger on average than actively managed funds, which, through economies of scale, helps reduce ongoing charges. In 2022, the average size of an index tracking equity fund (€785 million) was more than twice the average size of an actively managed equity fund (€338 million).

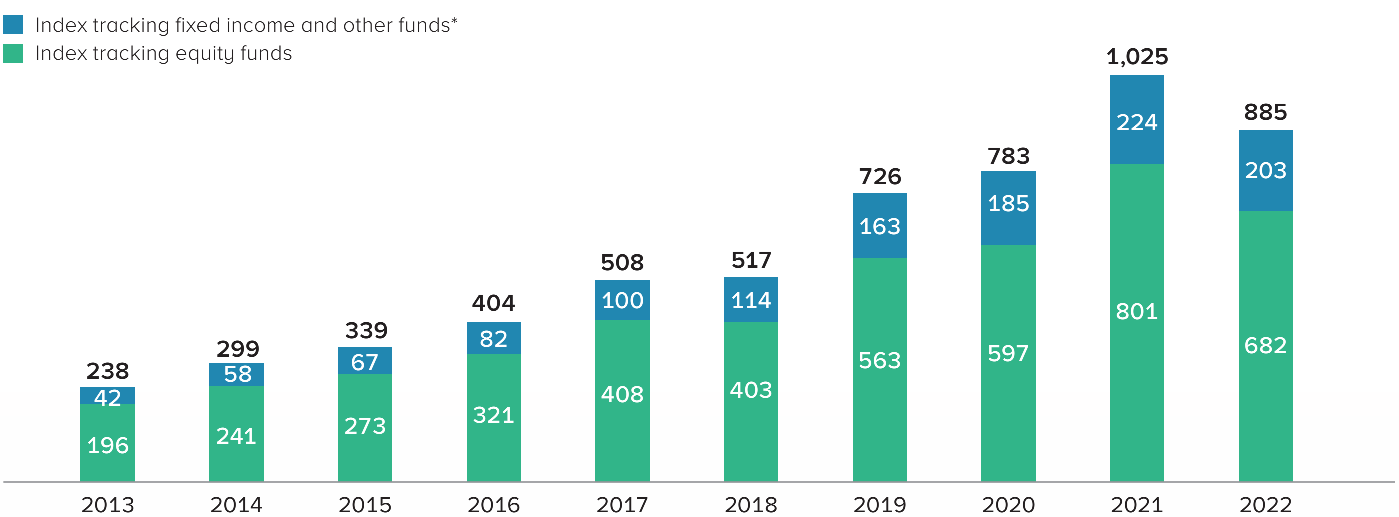
By contrast, under an active management approach, managers have more discretion to increase or reduce exposure to sectors or securities within their funds' investment mandates. Active managers may also undertake significant research about stocks or bonds, market sectors, or geographic regions. This approach offers investors the chance to earn superior returns or to meet other investment objectives, such as limiting downside risk, managing volatility, under- or overweighting various sectors, or altering asset allocations in response to market conditions. These characteristics tend to make active management more costly than management of an index tracking fund.

Growth in index tracking funds has also contributed to the decline in asset-weighted average ongoing charges for equity and fixed-income funds. Since year-end 2013, net assets in index-tracking funds have grown substantially from €238 billion to €885 billion (Figure 11). However, net assets in index trackers are still relatively small when compared to net assets for all funds, representing 11.8 percent of UCITS net assets at year-end 2022.

FIGURE 11

Net Assets in Index Tracking UCITS Have More Than Tripled Since 2013

Billions of euros, year-end



Percentage of UCITS total net assets

2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
5.5	5.8	6.0	6.8	7.5	8.2	9.8	10.2	11.2	11.8

* *Fixed income and other funds* includes fixed income, mixed, commodities, alternatives, miscellaneous, and convertibles.

Note: Data include index tracking UK UCITS and index-tracking UCITS domiciled in the Netherlands (representing 38 percent of net assets at year-end 2022). Data exclude money market funds and exchange-traded funds.

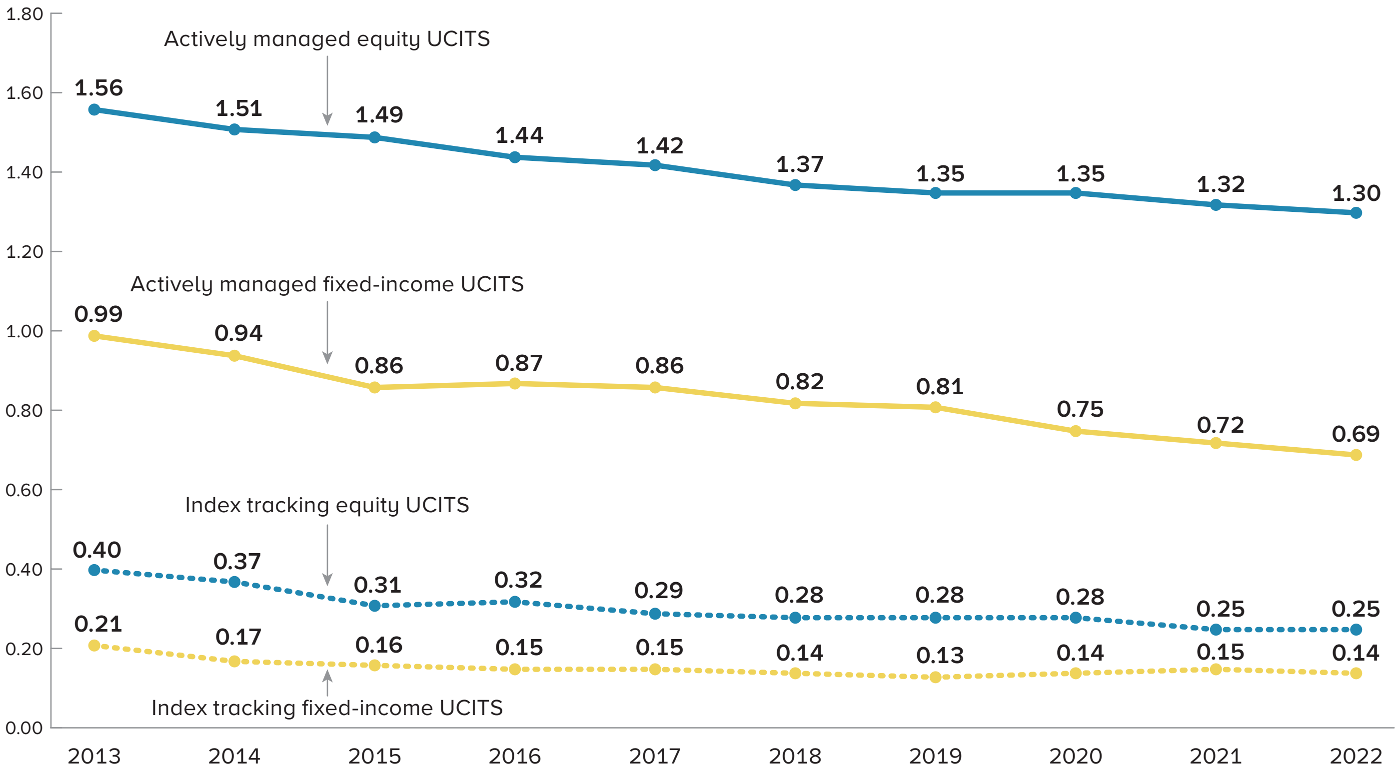
Source: Investment Company Institute calculations of Morningstar Direct data

While index tracking funds generally have lower ongoing charges than actively managed funds, it is important to note that decreases in ongoing charges of both index tracking and actively managed funds have contributed to the overall decline in UCITS ongoing charges. From 2013 to 2022, average ongoing charges for index tracking equity funds fell from 0.40 percent to 0.25 percent, while the average ongoing charge for actively managed equity funds fell from 1.56 percent to 1.30 percent (Figure 12).

FIGURE 12

Ongoing Charges for Actively Managed and Index Tracking UCITS Have Fallen

Percent



Note: Data exclude exchange-traded funds.

Source: Investment Company Institute calculations of Morningstar Direct data

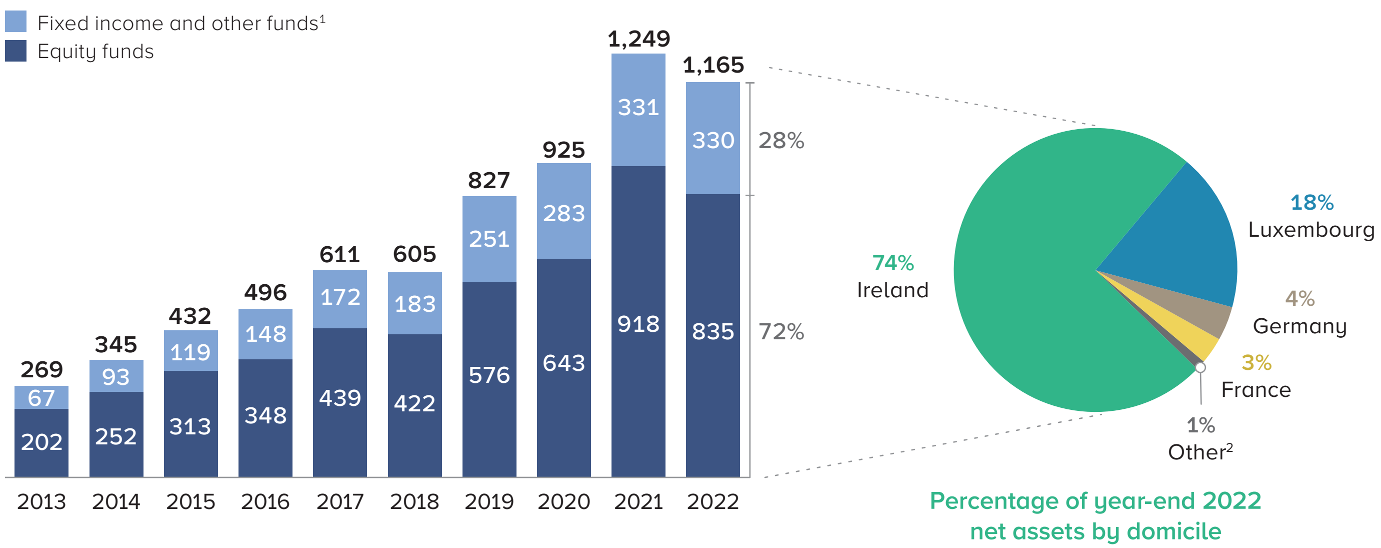
UCITS Exchange-Traded Funds

UCITS exchange-traded funds (ETFs) have become increasingly popular with investors. Authorized under UCITS, this segment of the EU fund industry enjoys many of the same benefits as its other open-end peers, such as passporting across EU Member States. By the end of 2022, net assets in UCITS ETFs were almost €1.2 trillion, an increase from $269 billion at year-end 2013 (Figure 13). Equity ETFs represented 72 percent of the net assets of UCITS ETFs at year-end 2022, and the majority (74 percent) of UCITS ETF net assets were domiciled in Ireland.

FIGURE 13

Total Net Assets of UCITS ETFs Have Grown Substantially

Net assets in billions of euros, year-end



[1] *Fixed income and other funds* include fixed income, commodities, miscellaneous, alternative, money market funds, mixed, and convertibles.

[2] *Other* includes Sweden, the Netherlands, Finland, Spain, Norway, Iceland, and Greece.

Note: Data include a small number of actively managed exchange-traded funds, representing 2.0 percent of net assets or less in any given year. Data also include exchange-traded funds domiciled in the Netherlands (representing 0.1 percent of net assets at year-end 2022).

Source: Investment Company Institute calculations of Morningstar Direct data

The vast majority of UCITS ETFs are indexed to a specific benchmark—therefore, they require lower management costs (and lower ongoing charges) to operate when compared to actively managed funds. Actively managed UCITS ETFs represented 1.5 percent of net assets in 2022. Average ongoing charges for equity UCITS ETFs fell from 0.39 percent in 2013 to 0.23 percent in 2022, likely related to economies of scale as net assets of equity UCITS ETFs have surged. Average ongoing charges for fixed-income UCITS ETFs decreased slightly from 0.25 percent to 0.20 percent over the same period (Figure 14).

Conclusion

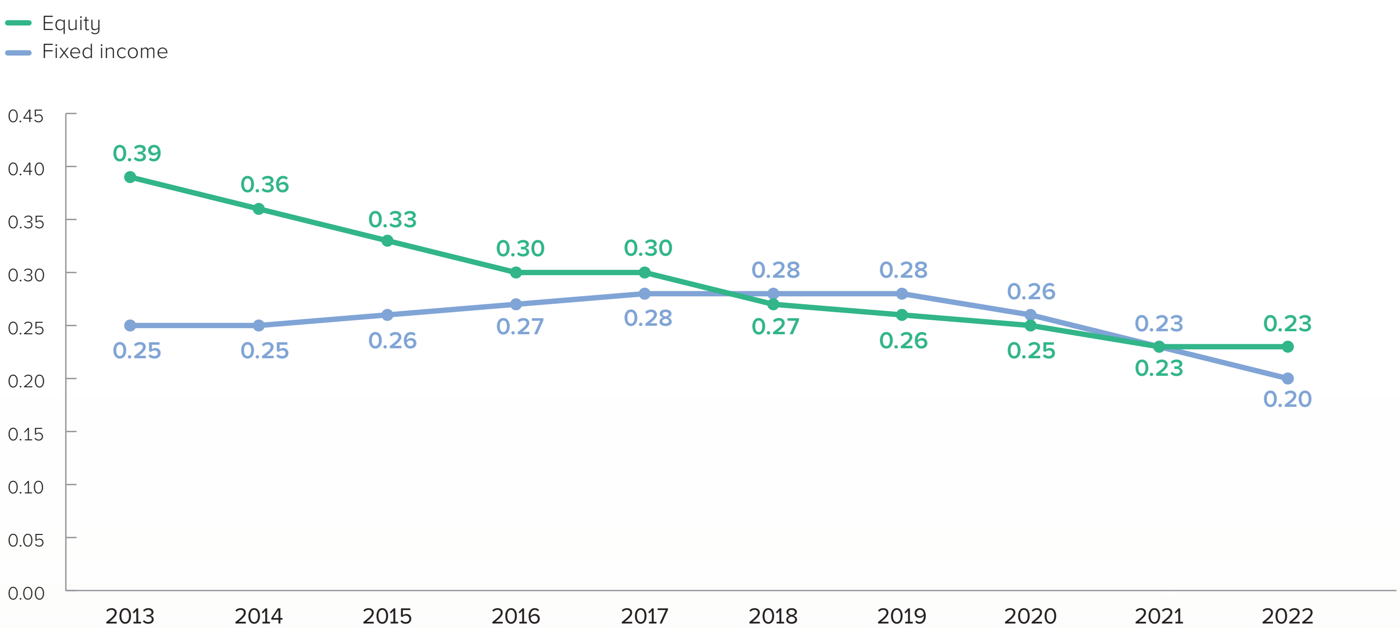
Since its inception in 1985, the UCITS Directive has undergone numerous changes affecting the way funds disclose costs and charges to investors. These changes have been designed to make the fees that investors pay for their investments as transparent as possible, especially regarding how investors pay for distribution. During this time, UCITS have introduced new unbundled share classes, which exclude commission payments for advice, that distributors have made readily available to retail investors. These unbundled share classes have lower ongoing charges, but it is important to note that investors who use these share classes and receive advice typically pay for that advice directly out of pocket.

Ongoing charges for equity and fixed-income UCITS have trended down since 2013. Although part of the decrease is a result of declining ongoing charges as UCITS realize economies of scale, most of the downward pressure has come from assets shifting to lower-cost funds, lower-cost funds entering the business, and higher-cost funds closing. Two important factors driving the decline in UCITS' ongoing charges are the increased number of unbundled share classes that have been made available to investors to take account of new regulations and the higher popularity of index tracking UCITS and ETFs.

FIGURE 14

Ongoing Charges for Equity and Fixed-Income UCITS ETFs

Percent



Note: Data include a small number of actively managed exchange-traded funds, representing 2.0 percent of net assets or less in any given year.
Source: Investment Company Institute calculations of Morningstar Direct data

Notes

[1] UCITS, or Undertakings for Collective Investment in Transferable Securities, are collective investment schemes established and authorized under a harmonized EU legal framework, currently EU Directive 2014/91/EU, as amended (UCITS V), under which a UCITS established and authorized in one Member State can be sold cross-border into other Member States without a requirement for an additional full registration (often referred to as the UCITS "passport"). Since it was first adopted in 1985, the UCITS Directive has been modified several times to take into account developments in financial markets.

[2] Despite their exit from the European Union at the end of 2020, data for UK UCITS are included in net assets (in Figure 1 as well as Figures 9, 11, and 13) because the current UK UCITS framework is effectively identical to the EU UCITS framework.

[3] EFAMA 2023 finds that about 26 percent of net assets in UCITS and alternative investment funds (AIFs) were held by investors outside of Europe in 2022. In 2022, Morningstar data indicate that 12.5 percent of cross-border UCITS were registered and available for sale in Asia, 6.5 percent in the Middle East and Africa, 4.2 percent in Latin America, and 3.0 percent elsewhere.

[4] Beginning in January 2023, UCITS that are sold to retail investors need to produce a PRIIPs KID. UCITS that are not sold to retail investors may continue to only produce a UCITS KIID; but for those sold to retail investors, the PRIIPs KID satisfies the obligation to produce a UCITS KIID.

[5] The recast Markets in Financial Instruments Directive (MiFID II) 2014/65/EU entered into force on July 2, 2014, with an implementation date of January 3, 2018, banning commissions paid to or by investment firms under certain instances (Article 24(9)); see https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065&from=EN. The European Commission (EC) issued a mandate to European Supervisory Authorities (ESAs) on October 13, 2017, to "issue recurrent reports on the cost and past performance of the main categories of retail investment, insurance, and pension products" (see European Commission 2017). The most recent report released by the European Securities and Markets Authority (ESMA), "Performance and Costs of EU Retail Investment Products," was released on January 30, 2023. See European Securities and Markets Authority 2023.

[6] For a look at how UCITS cost disclosure has changed over time, see Duvall and Mykolenko 2022.

[7] This report will refer to *shares* or *units* of UCITS as simply shares of UCITS; as used in this paper, the term also includes investment into units of fund vehicles such as unit trusts.

[8] For the purposes of this report, performance fees are not considered in this section since they are included in the TER.

[9] MiFID II requires investment managers to develop budgets for investment research. They may pass the cost of this research to clients through agreed-upon research payment accounts or pay for the research themselves out of their own profit and loss.

[10] Information derived from Investment Company Institute calculations of data from Morningstar Direct.

[11] In this context, exit costs exclude any costs that are applied to a fund redemption intended to correct for the effects of dilution (such as through anti-dilution levies or swing pricing).

[12] Information derived from Investment Company Institute calculations of data from Morningstar Direct.

[13] For more information on transaction cost disclosure under MiFID II and PRIIPs, see J.P. Morgan Asset Management 2022.

[14] Use of Morningstar data requires the following disclaimer: *© 2023 Morningstar. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.*

[15] Data are as reported in Morningstar Direct's MiFID II view as of September 2023. The field used for this statistic was "transaction fee actual," which is reported as an annual figure as required by the MiFID II reporting standards for ex-post costs and charges. Share classes where this field was missing were excluded from the calculation. The vast majority of the most recently reported transaction fees of UCITS spanned the period of June 2022 through August 2023.

[16] The types of UCITS share classes discussed in this section are not meant to be an exhaustive list. For guidance on factors ESMA believes UCITS should consider when setting up new share classes, see European Securities and Markets Authority 2017.

[17] ESMA has issued its opinion on the compatibility of such hedging arrangements with the requirement for a UCITS to have a common investment objective. See European Securities and Markets Authority 2017.

[18] Information derived from Investment Company Institute calculations of data from Morningstar Direct.

[19] The terms *bundled* and *unbundled* are loosely based on Morningstar's nomenclature for share classes in which payment for advice is either internalized (bundled) or externalized (unbundled).

[20] See note 5.

[21] See Commission Directive 2010/43/EU at Article 22(4), available at https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:176:0042:0061:EN:PDF.

[22] ICI uses asset-weighted averages to summarize the ongoing charges that shareholders pay through UCITS. In this context, asset-weighted averages are preferable to simple averages, which would overstate the ongoing charges of UCITS in which investors hold few euros. ICI weights the ongoing charge of each fund share class by its year-end total net assets.

[23] Throughout this report, the ongoing charge is represented by the TER in Morningstar Direct. For share classes where Morningstar does not report a TER, the OCF is used if available. Because the only major difference between the TER and OCF is the inclusion of performance fees in the TER, and the number of funds that charge performance fees is relatively small, ICI finds that this methodology is appropriate. The use of the TER to analyze costs paid by UCITS investors is consistent with other analyses. See European Securities and Markets Authority 2023. Between 2020 and 2022, when neither the TER nor the OCF are included in Morningstar Direct, the KIID ongoing charge is used. The missing data are only replaced by the KIID ongoing charge if the reported date of the KIID is as of the current year's total expense ratio data.

[24] In this analysis, ICI excluded ongoing charges of UCITS share classes domiciled or primarily intended for sale in the United Kingdom and the Netherlands. These share classes were excluded to minimize, as much as possible, any influence of the effects of either the RDR or AFM ban on intermediary commission payments, both of which had an implementation date of January 1, 2013. An in-depth analysis of UK costs and charges by ICI can be found at Investment Company Institute 2017.

[25] In this report, the average unmodified coverage—represented as the percentage of UCITS net assets where either the TER or the OCF is reported—between 2013 and 2022 is 58 percent, based on Morningstar. Beginning in 2016, if the ongoing charge in Morningstar is missing in the current year but non-missing for the prior year, then the ongoing charge is carried forward at the same level. Reported results are robust to these assumptions, as there are minimal differences between the reported results and the results in which the missing ongoing charges are not replaced with the prior year's ongoing charge. Beginning in 2020, if the ongoing charge is missing in Morningstar, it is replaced by the KIID ongoing charge, if available (see note 23). Following these adjustments, the average modified coverage between 2013 and 2022 is 75 percent, with coverage increasing from 74 percent in 2019 to 96 percent in 2022.

[26] Mixed funds invest in a combination of equities and fixed-income securities.

[27] See note 14.

[28] Investment objectives for Figure 7 in this report are based on Morningstar's global broad category group (equity, fixed income, mixed, and money market), global category (Europe equity large-cap, Europe equity mid-/small-cap, US equity large-cap, global equity large-cap, Europe fixed income, US fixed income, global fixed income, emerging market fixed income), and Morningstar category (aggregation of various sector equity categories) data fields.

[29] Data were measured using the MSCI All Country World Daily Total Return Index.

[30] Data were measured using the ICE BofA Euro Corporate Total Return Index.

[31] See note 1.

[32] In this report, cross-border UCITS are defined as funds registered and available for sale in three or more countries. Data include UK UCITS.

[33] See note 3.

[34] In some instances, the manager of a round-trip fund may be domiciled or established in the country in which it is primarily distributed.

[35] For a description of regulatory fees charged by EEA Member States, see Annex 11 of European Commission 2018.

[36] See Deloitte Touche Tohmatsu Limited 2016.

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James Duvall

James Duvall is an economist in the industry and financial analysis section of ICI's research department. Since joining in 2012, Duvall has primarily participated in research examining US mutual fund fees across the industry and in retirement plans, as well as the costs and charges of UCITS. He also contributes to research on closed-end funds, worldwide regulated funds, and environmental, social, and governance (ESG) issues. He graduated from Virginia Tech with a BS in mathematics and a BA in economics and holds a master's degree in computer science from Johns Hopkins University.

Eva Mykolenko

Eva Mykolenko is Associate Chief Counsel, securities regulation with the Investment Company Institute and ICI Global. Mykolenko advocates on behalf of US and global, regulated funds and their investors to securities regulators and multinational organizations in the United States and abroad. She started with the Institute in 2008 after more than eight years in private practice at Willkie Farr & Gallagher LLP and Shearman & Sterling LLP. Mykolenko received her undergraduate degree from the University of Michigan and her law degree from the University of Michigan Law School.

Casey Rybak

Casey Rybak is a senior research associate in the industry and financial analysis section of ICI's research department. Since joining in 2019, Rybak has participated in research examining trends in US mutual funds and ETFs. He also contributes to research on target date funds, closed-end funds, and systemic risk. He graduated from the University of Florida with a BA in economics.

Shane Worner

Shane Worner is a senior economist in the industry and financial analysis section of ICI's research department and undertakes research on international and European asset management issues. He has 30 years of experience spanning investment banking, asset management, academia, and public policy formation (both domestic and international), including holding a position as an economist with the Australian Securities and Investment Commission (ASIC) and heading up the Market Intelligence and Data Analytics department for the Madrid-based securities markets standard setter, IOSCO. Shane holds a PhD (Economics) from the Australian National University and a B.Ec from the University of Wollongong.

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