

# CIPFA Pensions Network



Using the call for evidence to build for the future

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# Agenda

- Focus on costs
- Asset pooling approaches (and management)
- Current developments
- Summary



## What fees do LGPS funds pay?

## Cost 'estimates' in the public domain

- Local Government Financial Statistics England (2013)
  - LGPS Investment and admin costs for 2011/12 of £468m
  - 89 funds in England and Wales with total assets of c.£145.2bn
  - Equates to fee of 32.2 bps
- London Boroughs' cost assessment
  - Investment management cost 32bp on average
- FTfm article published on 28 May 2013
  - Fee rate disparity; some councils paying three times that of others

Are data sources reliable?



What gets measured  
gets managed



## Local Government Pension Scheme Benchmarking Results



CEM Benchmarking UK Limited

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[www.cembenchmarking.com](http://www.cembenchmarking.com)

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## CEM Benchmarking Inc

- Global pension cost benchmarking specialists
- Extensive database of global client data
  - Consider embedded costs
  - Full look through costs on alternatives
- Providing a truly global reach
- Ability to aggregate fund data to compare costs for a group of (LGPS) funds with a comparable larger fund

## Comparison analysis

### **CEM aggregated 15 LGPS funds and compared with a peer group of comparable aggregate size**

- Fees paid by LGPS funds comparable with those paid by larger schemes
  - Generally negotiated competitive fee levels
  - Suggests savings from pooling likely to be lower than expected?
  - Governance costs comparable with large comparators
    - ◆ Surprising? Different governance models?
- But, fees for alternatives higher in LGPS funds

# Fees versus asset allocation

Asset class	Annual fees	Allocation
Alternatives	300-400bps?	8%
Property	90bps	8%
Bonds and cash	22bps	20%
Active equity (International)	35bps	40%
Active equity (UK)	25bps	
Passive – bonds	10bps	24%
Passive – equity	5-8bps	

## Total fees\*



Source Hymans Robertson, indicative fees, not an actual fund



# Can we access alternatives more efficiently?

- Existing approach largely uses fund of funds for diversification
- Impact on returns

	Potential cost saving* (per annum)
Stop using FoFs	c200bps
Direct management**	c300-400bps

\* Source: CEM research paper

\*\* Very large funds only – larger than combined LGPS

- Pooling alternatives could remove layer of fees, but
  - needs scale
  - cost savings may accrue slowly

# Building suitable internal resource

## Significant project, examples include:

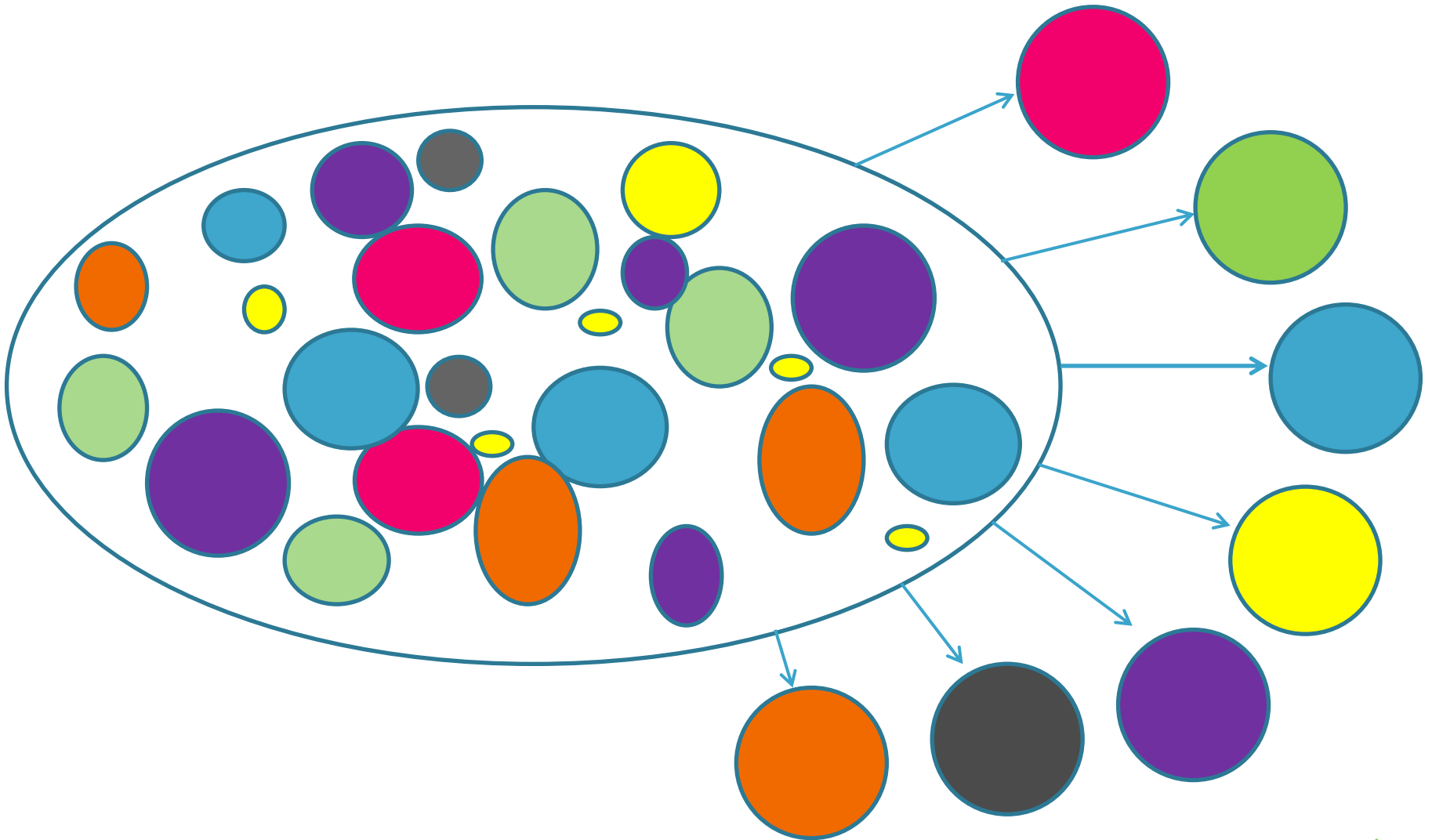
- Pension infrastructure platform
  - July 2012 - original announcement
  - Late 2013 - managers appointed
  - February 2014 – first fund launched (equity tranche only)
  - Yet to make an investment
- Norwegian oil fund
  - 1998 – Fund established
  - 2010 – First investment in alternatives
  - 2014 – Fund announces doubling of equity specialists

**Governance arrangements key!**



## **Asset pooling (listed assets)**

# Funds managing common mandates



# Advantages of asset pooling – scale benefits

## Global Equity fee scale

Asset value	fee
First £50m	0.60%
Next £50m	0.45%
Next £100m	0.40%
£200m+	0.35%

## Fee impact diminishes with size

Asset Value	Effective fee
£50m	0.600%
£100m	0.525%
£200m	0.462%
£400m	0.406%
£1bn	0.372%

Scale benefits without fund merger?

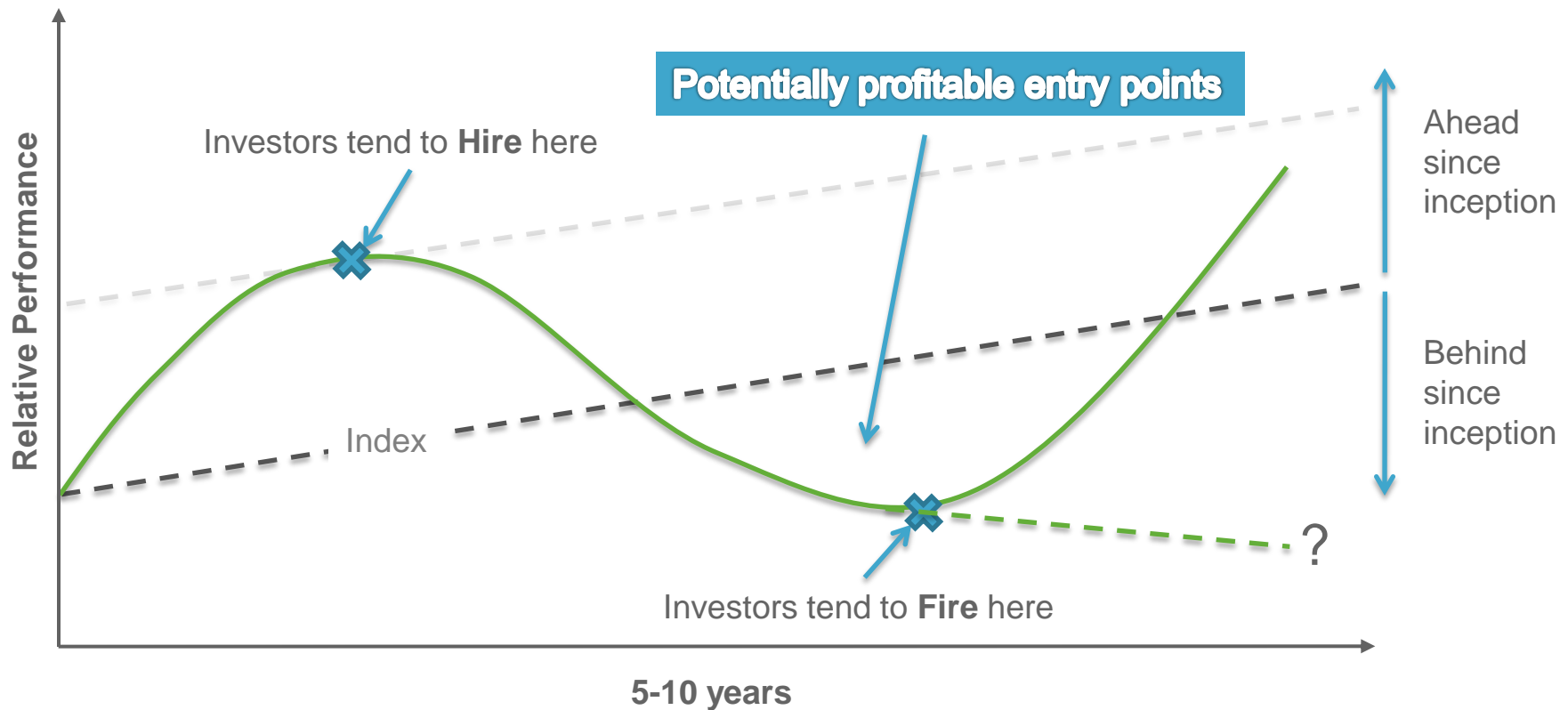
## Disadvantages of pooling

- Some control over manager selection must be ceded
- Choices may be limited,
  - e.g. global rather than regional mandates for equities
- Cost of set up

## Benefits of pooling

- Central monitoring and management
  - Time can be re-focused on strategy?
- Scale benefits without fund merger?
- Improve the quality of manager decisions?

# Manager selection: timing entry and exit



Short-term performance is cyclical and a poor leading indicator

# Different ways to pool assets

Options include ...	What is it?
1. Fund managers treat LGPS as “one investor”	<ul style="list-style-type: none"><li>- Each fund manager treats separate LGPS funds as though were one customer</li><li>- Individual fund IMAs</li></ul>
2. Common Investment Vehicle to wrap existing assets	<ul style="list-style-type: none"><li>- Multiple asset classes</li><li>- Tip current mandates into CIV</li><li>- Individual funds retain ability to choose their preferred mandate within each asset class?</li></ul>
3. Common Investment Vehicle CIV board selects managers	<ul style="list-style-type: none"><li>- Multiple asset classes</li><li>- Tip current assets into CIV</li><li>- Board selects managers</li><li>- In specie asset transfers + transition</li></ul>



# The impact on decision making

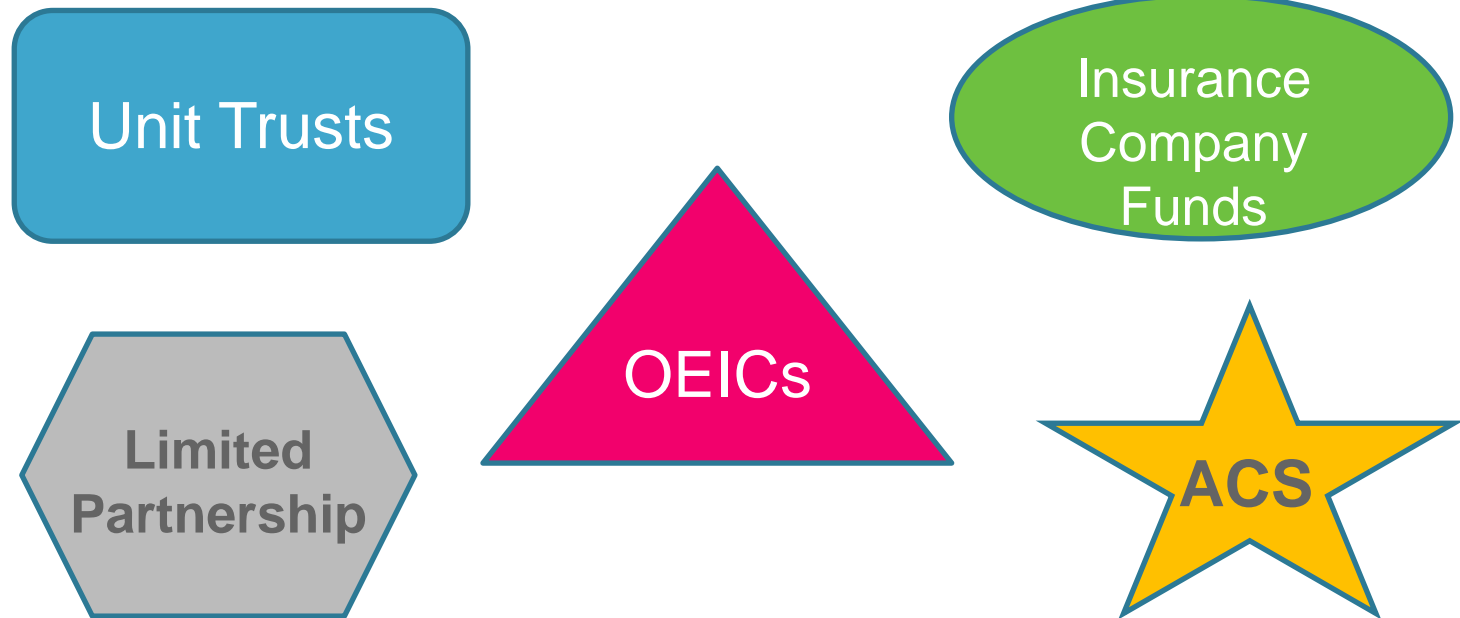
Decisions	Performance monitoring	Manager structure	Minor asset allocation	Major asset allocation	Contribution strategy	Employer liaison	Member administration
Collaborative	?	✓	✓	✓	✓	✓	✓
Elective pooling	C	?	✓	✓	✓	✓	✓
Alternative pools	C	C	✓	✓	✓	✓	✓
Elective CIVs	C	C	C	✓	✓	✓	✓
Non elective CIVs	C	C	C	✓	✓	✓	✓
Superpool	C	C	C	C	✓	✓	✓

**C** – decision transferred to central resource



## Types of asset pools

## Broad range of pooling vehicle available



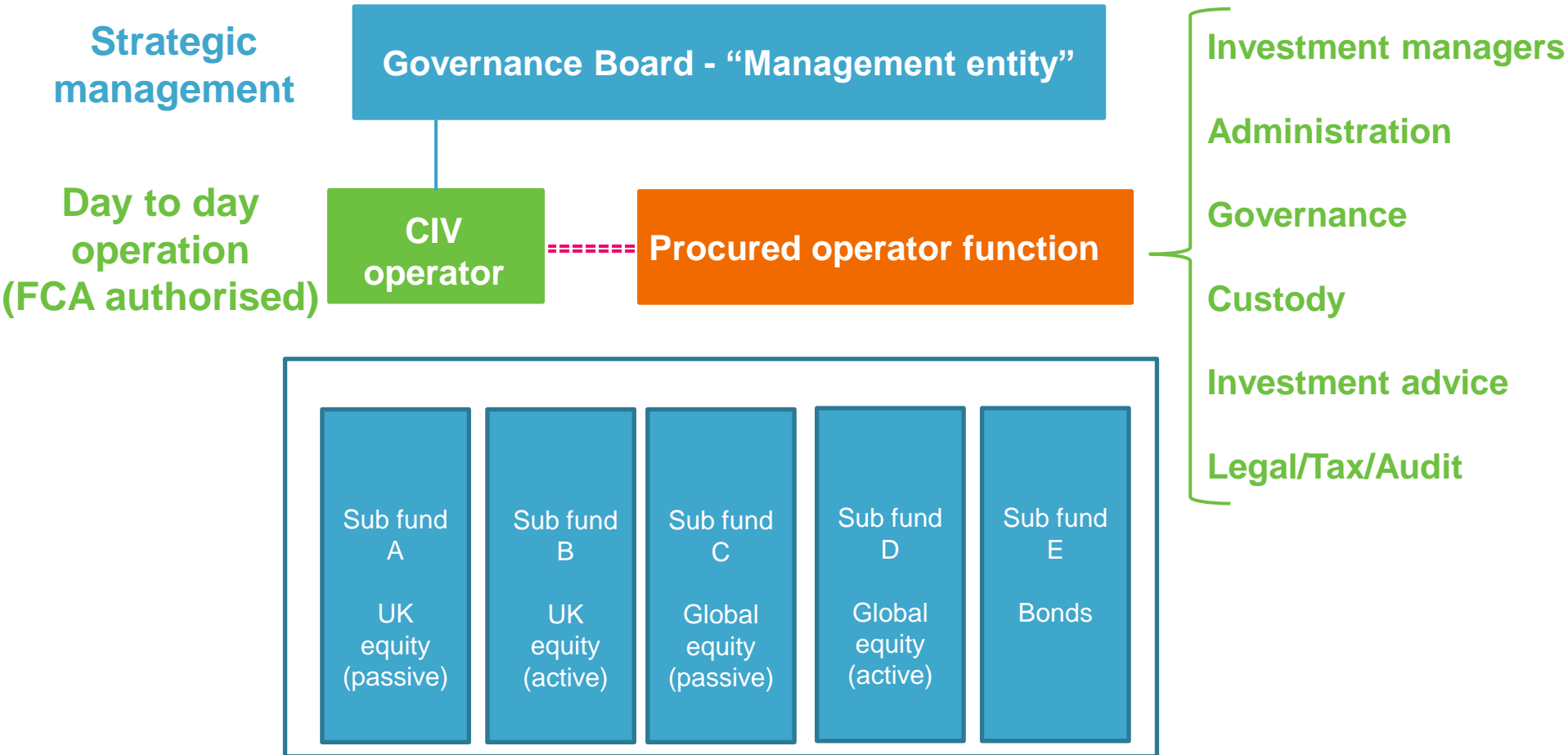
- A means of pooling assets across investors
- Range of structures each with different attributes
  - Tax, ease of set up, asset classes, etc.

# Authorised contractual scheme



- Vehicle newly established by HM Treasury in 2013
  - Tax transparent fund, competes with Luxembourg / Dublin
- Otherwise, contextually similar to OEICs (for listed assets)
- Partnership variant available for alternative assets

# Structure of an umbrella CIV



Could operate multi-manager approach within sub-funds



# Current developments

# Current developments

- DCLG's recent cost-benefit analysis
  - Three options for restructuring LGPS in England & Wales
    - ◆ Single CIV
    - ◆ 5-10 CIVs
    - ◆ 5-10 merged funds
- Next consultation expected end March/April 2014
- A CIV for London
  - Based around Authorised Contractual Scheme vehicle
- Berkshire, Buckinghamshire, Oxfordshire

# Shadow Scheme Advisory Board

The Board made the following 7 recommendations

1. Consultation on structural options asap
2. Agree realistic implementation timetable
3. Board should set baseline of data for Scheme Annual Report
4. Introduce legislation for reform & implementation timescale



# Shadow Scheme Advisory Board

Board recommendations (contd):

5. In its consultation on options, the Government should:

- Consider alternative methods for managing deficits and
- Analyse cost/benefits & barriers to greater use of passive, collective investment vehicles & in-house management

6. Board will support Government by developing options for managing deficits & further research on costs/benefits of options

7. Ensure that Call for Evidence reforms are consistent with other LGPS policy work, e.g. governance and investment regs.

## Summary

- Improved data quality will help decision making
- Asset pooling should offer scope for savings
  - Larger pools lower the marginal cost on traditional assets
  - Larger pools allow alternatives to be diversified with lower cost
- Appropriate governance arrangements will be key

Reforms could deliver significant benefits if implemented well

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