Shareholder activism: The pension fund/asset manager relationship

Investment Association director of corporate governance and engagement Andrew Ninian speaks to Natalie Tuck about the role of the asset manager in pension fund shareholder activism

Can you explain the process of how the relationship works between pension funds and asset managers in relation to shareholder activism? For example, who attends the AGMs? Will the pension fund advise their fund manager on what they want them to vote on?

It depends on what has been agreed between the pension fund and the asset manager but I think normally most pension funds will give the responsibility of voting the shares at the AGM to the asset manager. From an asset management perspective, they see it as part of the investment process. If you look at why an asset manager takes an interest in corporate governance for the companies which it invests in, it is because it wants to invest in companies which generate long term returns for the pension funds. Companies that are well run, that have good governance and have the right strategy are more likely to deliver those long-term returns. Asset managers, on the whole, see governance as an integral part of the investment process. A key part of that is engaging with the individual companies on governance issues, so voting their shares at the AGM.

What other kinds of action do fund managers take to hold companies to account?

There are a number of ways in which asset managers can hold companies to account, first is setting out their expectations of what they expect from the companies in which they invest. We've seen that from asset managers in the last couple of months particularly on executive pay and setting out their stance quite publicly. For every company, asset managers have a set of policies which are usually voting policies which set out their expectations for the companies in which they invest. Furthermore, we as the investment body for asset managers within the UK have our own expectations and guidelines through our principles of remuneration and other guidelines such as our share capital management guidelines, which says collectively, as UK asset managers this is what we expect.

The second action surrounds engagement and there is a lot of engagement that goes on between companies and asset managers, both through the normal course of business but also to discuss one off or individual events. There is engagement between management teams and fund managers around the strategy and performance of the business, and there is a lot of engagement between chairman of companies and fund managers and governance teams around the governance of the company. In particular at the moment there is a lot of engagement between remuneration committee chairs and asset managers over the structure and levels of executive remuneration in companies.

What are the biggest concerns pension funds are asking their asset managers to focus on?

It slightly depends on the individual pension fund but we are hearing from our members that there is a lot of focus on executive remuneration but also on sustainability, environmental and social risks. Those two broad areas are getting increasing attention from pension funds and they are increasingly raising those issues with their asset managers and asking them how they are holding companies to account. I think the way that we would look at it, is that as asset managers we expect the companies in which we invest in to be managing the material risk to their business. We want companies to outline what is their material risk to their business and how are they managing those risks over the long term. If asset managers disagree with that list and believe that climate change or water usage or the way that they treat their employees should get greater attention by that board that is when the asset manager will engage with the company and say 'what are you doing on climate change etc because we

don't think that you are dealing with that risk sufficiently'.

How does a fund manager deal with different client's views when voting at an AGM, for instance?
The starting point is that the asset manager has got to do what they think is in the best interest of the client, that's the underlying principle that asset managers have to work on. From that point there may be, although this slightly depends on the relationship between the asset owner and the asset manager, and what has been agreed, there may be some ways that they may split the vote depending on the client and the fund.

Since the 2008 financial crash has there been a change in attitude from companies themselves, in terms of their willingness to engage with investors?
Yes, I think the first point to note is that asset managers have done a lot of work on engagement for a number of years and I think companies, particularly if you look at the now binding vote we have on executive pay, has focused a lot of companies' minds. In particular, the AGM season in 2017 is going to be very important because around two thirds of companies in the UK are going to be seeking a new policy, so that has focused directors' minds and there is a lot more engagement on executive pay. However, more broadly directors and companies are willing both proactively and reactively to speak to their investors on specific issues or just really to understand the concerns or views of their shareholders to make sure they are managing that relationship appropriately.

Likewise, has there been an increase in the number of investors, particularly pension funds, who are bringing these issues up with their fund managers?
We are certainly hearing that in recent years the level of client requests and information requests that pension funds are raising with asset managers have increased. These range from 'how did you vote on a particularly high profile company', or 'what are you doing on this issue to make sure that my investments are being managed in an appropriate way'. There seems to be a lot more client interest in governance and environmental and social issues.

How do things differ between active and passive management?
There has been an argument in the UK that passive investors do less on stewardship or governance but actually we believe the opposite of that. We believe that the big houses in the UK devote a lot of resources on corporate governance and stewardship and the reason to it is because they don't have the choice to sell their shares if they think the company is being run inappropriately, and the only way that they can get a better return is by improving long term returns and improving governance within those companies so there are big passive fund managers who devote a lot of resource on governance issues because that is one way that they can increase the return to their end client because they believe better run companies will generate better long term returns for the client.

Written by Natalie Tuck

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