Summary

- Historically, fiduciary management services were the preserve of large pension schemes, but offerings have now expanded to smaller schemes. Solution innovation is at the heart of the fiduciary management space and continues to evolve.
- Fiduciary management was originally suited to the mid-sized schemes of around £100 million to £300 million.
- The 2016 KPMG *Fiduciary Management Survey* found that 64 per cent of schemes using fiduciary management in the UK had under £250 million in assets under management.
- In a traditional consulting model, smaller schemes experience inconsistencies in the level of reporting and costs compared with larger schemes. This recognition is likely to lead to more schemes of this size considering fiduciary management.
- Trustee boards are now more tuned-in and better equipped to challenge their fiduciary providers than ever before.
- For many smaller pension schemes fees can be lower than legacy solutions, more transparent and better value for money.

Infiltration and beyond

Fiduciary management is now increasingly available to small-sized DB pension schemes. Adam Cadle analyses this development and looks at how fiduciary management works in this sized market

Historically, bespoke fiduciary management services were the preserve of large pension schemes, but offerings have now expanded to smaller schemes. Solution innovation is at the heart of the fiduciary management space and continues to evolve at the required pace to keep up with the investment needs of many pension scheme trustees.

An evolving scenario

According to Aon senior partner and head of European distribution Sion Cole, fiduciary management was "originally suited to the mid-sized schemes, of around £100 million to £300 million" but solutions now also cover the smaller schemes.

"Solution innovation has been so rapid more recently that over the past year or so, some providers are now able to offer fiduciary solutions specifically designed for schemes £5 million in assets upwards."

Initially smaller schemes were priced out of many fiduciary management solutions, Russell Investments director UK fiduciary management Paul Wharton states, due to "minimum fees that many fiduciary managers operated with".

"As competition in the market has evolved, so the fees on smaller mandates have reduced, enabling more trustees to take advantage."

Indeed, the 2016 *KPMG Fiduciary Management Survey* found that 64 per cent of schemes using fiduciary management in the UK were under £250 million in assets under management.

One key trend in this segment, SEI institutional group managing director, EMEA, Patrick Disney comments, "is the recognition by the industry that in a traditional consulting model, smaller schemes experience inconsistencies in the level of reporting and costs compared with larger schemes".

"This recognition is likely to lead to more schemes of this size considering fiduciary management because, through their scale and resources, fiduciary managers are not only able to provide smaller schemes with access to a broader range of investment styles, asset classes and investment managers than would otherwise be available to them but are also able to offer a bespoke level of reporting regardless of size."

Within the fiduciary management market a greater choice of provider is now available, as more players have entered the market. Asset managers are able to bring operational platforms and risk management techniques to the fore, which provides greater comfort to schemes.

Head of the client strategy team for BlackRock's outsourced chief investment officer services Sarju Mehta comments that "a greater focus on the governance of fiduciary appointments, and monitoring of providers, has pushed trustees to increase their awareness and understanding in this area".

"Trustee boards are now more tuned-in and better equipped to challenge their fiduciary providers than ever before. This has also provided opportunities for the truly independent evaluators to ensure a level playing field. Transparency of fees and quality of reporting are key areas that are now in the spotlight."

Benefits

So what can fiduciary management actually offer to small pension schemes? "Fiduciary management offers schemes the ability to be more dynamic in the face of increasingly challenging markets and continued pressure on scheme funding levels," Mehta states.

"It also provides trustees with more time to focus on the most important decisions, such as agreeing the funding plan, defining a risk budget and setting overall investment objectives, by delegating the implementation to an investment specialist. For smaller schemes in particular, where there may be less in-house expertise and assets are lower, fiduciary management allows trustees to access more sophisticated investment at a lower cost than they would have been able to otherwise. Fiduciary management also provides a way for trustees who have avoided liability hedging, for example due to a view that interest rates can only rise, to move into liability driven investment strategies while minimising their 'regret risk'."

Cole adds that fiduciary management comes with "enhanced reporting benefits that covers the entire portfolio, rather than reviewing multiple managers' reports, and, because the LDI and growth are managed holistically together, it means the trustees don't need to worry about cash calls and collateral management".

Interestingly however, Gatemore Capital Management managing director, UK, Mark Hodgson believes that the fiduciary management case "is not for everyone" and one of the biggest criticism of fiduciary management is that "advisers are blaming trustees for their historical decision making and selling fiduciary management as the solution".

"However, it is the same investment firm then being sold as the fiduciary management provider, with the same decision makers but at a higher cost – it is not always the panacea."

It must be noted as well that fiduciary management offerings for small pension schemes compared to large pension schemes do differ. This is a point raised by Mehta, who says that the three main differing areas are around "discretion, customisation and frequency of interaction".

"Larger schemes often retain the option to keep more discretion over multiple aspects of their portfolio, perhaps because they have in-house experts who are well equipped to form part of the investment decision making process. While the range of services offered is similar for small and larger schemes, larger schemes usually ask for more customisation. Larger schemes also typically look for a higher frequency of interaction with a fiduciary manager and require more adhoc analysis and advice."

Fees

As with any offering comes the issue of cost. Not so much an issue for the large pension schemes, but are small pension schemes put off by the costs associated with fiduciary management? Disney thinks not.

"It is a popular misconception that fiduciary management is more expensive for smaller schemes than a traditional model. In our experience this is just not the case. For many smaller pension schemes fees can be lower than legacy solutions, more transparent and better value for money. The reduced investment management fees that come from a fiduciary manager's bulk buying power can offset the cost of the additional and higher value services delivered. When you consider that a fiduciary manager also replaces the existing investment consultant, thus removing the need for their fees, the total investment budget may not need to change and can be even lower."

The future looks bright for the number of small schemes utilising fiduciary management provider capabilities to enhance their portfolio returns and ultimately achieve the ultimate objective of continuing to pay their members. Cole believes that the take up of fiduciary management by schemes under £30 million "will soar".

"The Pensions Regulator recently reminded trustees of smaller schemes that investment opportunities continue to develop and innovate to assist with risk management."

Hodgson is of the same opinion but with it issues a warning.

"Fiduciary management will continue to grow but trustees should be buying it based on need, not having it sold to them," he argues.

Written by Adam Cadle