Safety in numbers

Following a number of high-profile acquisitions and mergers, it is not just pension schemes that are consolidating, but the industry as a whole. Jack Gray looks at what impact this could have on the future of pensions, who will be the big winners and losers, and whether there is safety in numbers

Summary
• Company consolidation may lead to improved benefit security and standard of service, but it could also stifle innovation and restrict choice.
• DC consolidation continues to progress rapidly, with The Pensions Regulator's master trust authorisation regime driving change.
• Consolidation in the DB market, especially in superfunds, may be being held back by uncertainty surrounding the lack of regulation.

Safety in numbers is a common survival technique. As the pensions industry moves towards consolidation in a variety of ways and vicinities, it could be interpreted that the industry is using this primal technique to improve benefit security for members. However, safety in numbers can bring about issues, as it does not work for everyone and it may not be as simple as using the tactic adopted by living things for millions of years.

Mergers and acquisitions

During 2018 and 2019, there has been a number of high-profile acquisitions and mergers. In April 2019, Marsh and McLennan (M&M) announced that it had completed the acquisition of Jardine Lloyd Thompson Group for $5.6 billion (£4.3 billion). This year also saw Cardano agree to purchase Now Pensions, which will result in group assets under its management exceeding £25 billion, while in 2018, Aegon acquired BlackRock's UK DC platform and administration business, transferring £15 billion of assets and 450,000 customers to Aegon.

"Consumers and advisers will increasingly be able to access the full suite of services from a single provider," begins BlackRock interim head of DC, Alex Cave. "Some of the larger providers are beginning to compete head on with the retail banks to own the whole consumer and be their central saving, investment and insurance hub."

Large, consolidated companies may result in smaller providers having to either adapt, exit the market or consider consolidating themselves. "Those that remain have to have a clear value add proposition," Cave adds.

"There are participants in the market who want to be known for the sophistication of their proposition and the quality and flexibility of their investment products.

"Others have created distinct propositions for both ends of the market and worked on the integration with their retail/wealth platform."

Cave believes that this will make competition for customers "fiercer" and, although there could be less participating firms, they will have "broader and more equal" offerings.

"This means hitting the key decision points for both trustees and their advisers will be critical and will make providers more selective on the tenders they go for," says Cave.

There is some concern that this could create a lack of choice for consumers. LifeSight head of propositional development, David Bird, believes that there will be four main types of provider in the future – auto-enrolment specialists, life company providers, employee benefit consultants and accidental master trusts, such as the Universities Superannuation Scheme.

He continues: "Employers seeking to outsource to a master trust may be looking at a long-list of around 20-30 providers, with fewer than 10 providers dominating the market and accumulating employers, assets and members."

However, Cave does not think there will be a lack of options. He concludes: "I don't think that the merger and acquisition activity we have seen in the platform space has reduced choice. Those acquired platforms still exist under a re-branded guise."

Administration

There has also been recent merger and acquisition activity in the administration market, with XPS Pensions Group acquiring both Kier Pensions Unit and Royal London Corporate Pension Services Limited in the past eight months, while Aegon purchased BlackRock's administration business.

TPT Retirement Solutions head of direct distribution, Adrian Cooper, believes that this is a problem area. "There is an issue in the pensions administration in its reduced capacity," he says. "Some are providing an excellent service, but some aren't. If schemes are thinking of switching administrators, there aren't many options."

Despite this, Cave says there is an opportunity for administration consolidation to improve member experience. "Administration is definitely a scale game and both asset managers and platform providers will seek greater assets to drive down costs, which are passed on to members," he explains.

DC consolidation

Defined contribution consolidation is being primarily driven by The Pensions Regulator's (TPR) master trust authorisation regime. Supporters believe that it will help drive down costs for the member, provide greater benefit security and achieve the economies of scale needed to invest and capture more opportunities, improving member outcomes. Redington director, Jonathan Parker, says that DC master trusts provide "sufficient flexibility for employers that want to retain a bit of control".

He continues: "They can have trust structure while still having control over investment strategy. You want to make sure that schemes are run well, but not many have the funds or expertise to do it. In three to five years I think there will be less than 20 master trusts – we don't need more than 20."

Parker adds that the "incredibly thorough" authorisation process was the correct way forward as "people need to trust in their provider".

Some industry members think that the DC master trust market will continue to grow. "We can imagine that there may be some regulatory convergence and that this will push even more employers towards master trusts.

"There will remain some employers with the time, energy, commitment and resources to run single employer trusts but we can expect that increasingly to be a minority," Bird says.

However, some do not have as much confidence. A recent survey from the Pensions Management Institute (PMI) found that 77 per cent of industry members think that less than half of DC single-trust schemes will transition into master trusts.

Furthermore, there is concern that smaller schemes could be squeezed out of the market as they won't be able to compete and will not have the funds to meet stricter regulations. In March 2019, Welplan Pensions exited the market due to TPR's authorisation regime, which it believes has made the practise "cost-prohibitive" for many smaller schemes.

Welplan Pensions chief executive, Bruce Kirton, said at the time: "Over the past six months it has become increasingly clear that the master trust regulatory environment is one that favours much larger scale.

"There is now no meaningful place for a small or even medium-sized specialist business such as Welplan Pensions. This is something we've already seen with other smaller providers being acquired by larger ones."

DB consolidation

Within the DB space there are two main forms of scheme consolidation – superfunds and DB master trusts. The PMI's survey found that 67 per cent believe DB consolidation to be a good idea, although most concede that schemes have to look at their individual requirements and decide whether to consolidate, seek a buyout or achieve self-sufficiency.

Hymans Robertson partner and head of trustee DB, Susan McIlvogue, says: "It is important that trustees and sponsors keep an open mind, consider the options available and objectively reach the best decision for their members.

"There is no doubt that consolidation can create value for many small schemes, through reduced running costs, good governance and more effective investment strategies. Consolidation can also reduce the cost of ultimate buyout."

Cooper, however, highlights that it may not be that simple for smaller schemes. He concludes: "Smaller schemes cannot access certain assets and schemes that are not well funded may find it difficult to survive without consolidating.

"For smaller schemes, recruitment and retention of trustees is hard. Where will trustees come from? Either professional trustees need to be employed or the scheme needs to consolidate.

"DB consolidation is not going away, it just depends on the pace of change."

Written by Jack Gray