Summary
- With a potential 39 master trusts to be authorised at the end of the first phase of authorisation, the market has already more than halved in size.
- Following the first wave, many in the industry are expectant of further consolidation down the road, as even those authorised may not stick around in the market.
- As consolidation takes effect, savers will feel the benefits through lower fees and more investment potential.

Improving trust in a post-authorisation world

As we approach the final stages of the first wave of master trust authorisation and consolidation begins to take shape, it's important to not lose sight of what will make a good master trust in a post-authorisation world

As we approach the final stages of the first wave of master trust authorisation, the shrinking of the market has been stark.

From a substantial 83 master trusts before authorisation took shape, The Pensions Regulator has authorised 31, with a further eight still waiting for their fate to be revealed, at time of writing.

The number is even smaller that the regulator anticipated, after it estimated that 50 master trusts would be left after authorisation. However, while the standards have been raised, it shouldn't be taken for granted that fewer master trusts means better quality.

Atlas Master Trust head of clients, proposition and strategy, Anish Rav, believes that while the authorisation process has produced a strong level of minimum standards to ensure the protection of member benefits, there needs to be just as much effort in enhancing member outcomes.

What is good?

While the authorisation process has put many schemes through the wringer, and given that many will be undergoing supervision from the regulator once authorised, schemes must not get complacent.

According to Rav, pro-active governance, partnership and member focus are the three key principles that master trusts must not forget.

"Pro-active governance is by far the most important thing as it will drive the future of the service, the value and the experience that the employer and its employees will receive and most importantly the member outcome," he says.

Atlas prides itself on having "world-class governance standards" with a strong member focus, a trait that he feels does not extend itself to the wider authorised world.

"The strength and nature of a master trust's governance structure and approach is absolutely critical. Sadly, many authorised master trusts today do not have the requisite governance structures and processes to recognise and adequately drive enhanced member outcomes."

Pensions and Lifetime Savings Association (PLSA) policy lead for master trusts, Craig Rimmer, also believes that a competent board of trustees is vital for a master trust to operate effectively, noting that a good board of trustees should complement each other in their all-round skills.

"It is important to have a trustee board that has good knowledge all round and is cognitively diverse. We believe that there are four key areas of knowledge – legal/regulatory, investment, actuarial and administration – and four competences – communications/interpersonal skills, commercial acumen, intellectual curiosity, and a readiness to challenge."

Another element, according to Rav, is the way in which the on-boarding of new clients is handled. The master trust undergoes a 'get to know you' workshop with the employer, ensuring that the relationship is formed on a 'basis of knowledge and understanding' that could otherwise get lost in larger schemes.

So if the process of authorisation won't in itself drive up the quality of governance among master trusts, will consolidation help? Is bigger better?

Consolidation is king

The regulator will be the first to admit that one of the main goals of the authorisation process is consolidation, and it's clear to see why.

The recently-published *DC Future Book 2019* highlighted a number of ways in which to increase members' savings into a DC pension pot. Besides members simply increasing their contributions or working longer, consolidation of smaller schemes was also noted.

The research, conducted by The Pensions Policy Institute (PPI) and Columbia Threadneedle Investments, found that a median earner saving 8 per cent of total earnings from age 22 to state pensions age could increase their pot between 6-8 per cent if smaller schemes consolidated and dropped charges, due to benefits of scale.

"The average charge in contract or trust-based schemes with five members or fewer is 0.72 per cent. For schemes with a thousand members or more, the average charge is 0.37 per cent in trust-based schemes and 0.45 per cent in contract-based schemes," says PPI head of policy research, Daniela Silcock.

"According to our research, communication and behavioural nudges that result in increased contribution levels and/or longer working, can have the most significant impact on member pension pot sizes… the same applies to a drop in charges arising from scheme growth or consolidation."

Rimmer, believes that the scale will help drive benefits for the members: "We now have the opportunity to utilise large scale to build well-run schemes that support the saver and all points on their pension journey, from their first contributions to living out their retirement and caring for their beneficiaries.

"The master trust market can now develop and grow the possibility of new super schemes. There is the expectation that there will be a wave of further consolidation further down the track.

"In effect we have seen a halving of the number of master trusts already; we would expect to see more mergers and acquisitions and more exits. It is also possible that we will also see more new entrants to the market."

Hymans Robertson head of DC provider relations, Michael Ambery, agrees: "We are expecting to see a race for providers to win business and establish their credentials. This will almost definitely create consolidation through acquisition."

According to Rav, some master trusts that have achieved authorisation could well find themselves being consolidated over the next 12 to 18 months.

"Some authorised master trusts will feel that they do not want to continue operating as they decide that increased governance and the long-term nature of master trusts is not for them."

Does consolidation drive innovation?

As market consolidation starts to take effect, beyond lowering overall charges for members, it could also lead to innovation in the way DC pension funds are invested.

A recent study by research house Cerulli Associates found that pension consolidation was also forcing smaller asset and fiduciary managers out of the market due to increased competition and fee pressure.

The study, *European Institutional Dynamics 2019: Addressable opportunities for asset management,* found that consolidation will drive innovation in the DC space by opening up a broader range of asset classes in default funds.

"It will be one factor that will act as a driver for increased innovation. Increased membership, increased contributions and the maturing of the master trust book will also act as drivers to more innovation in the sector," Rimmer says.

As a result of this, the government has been looking to open up DC pension pools into patient capital, a move which global business consultancy Oliver Wyman believes could add as much as 7-12 per cent into savers' pots.

While Rav believes it is not consolidation itself that will drive innovation, which will be a by-product of scale and efficiencies, he believes innovation will certainly play its part.

"The interesting question is whether that innovation will be focused on truly driving enhanced member outcomes – or trying to simply impress and please various market-makers, advisers and/or commentators," he says.

Commentators agree that consolidation alone will not drive innovation, as policy initiatives, legislation and technology advancements are likely to be the biggest driver. It is the schemes that can put governance at their heart that will thrive the most.

Written by David Andrews, a freelance journalist

In association with atlas

The considered choice of master trust

[1] Financial Conduct Authority, February 2019