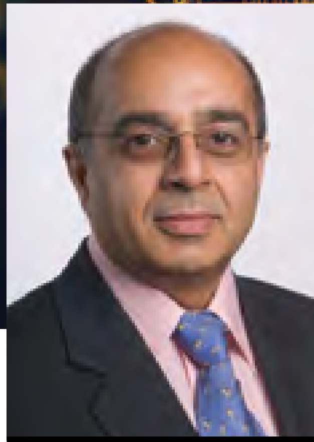
Schneider Electric: A circuit change



Schneider Pension Plan's trustee board chair, Rodney Turtle, and pensions manager, Jerry Gandhi, speak to Natalie Tuck about the journey of switching from a traditional manager mix to a single fiduciary manager

Fiduciary management (FM). The competitiveness of such providers was at the centre of the Competition and Markets Authority's (CMA) recent investigation. Its outcome has seen a number of proposals, such as the requirement for trustees to run a competitive tendering process and set strategic objectives for schemes.

Hiring a fiduciary manager is a big step for a scheme; it involves delegating all, or part, of a scheme's investment processes to an external manager. Such a decision must not be taken lightly. When the Schneider Pension Plan (SPP) began its switch to FM in December 2018 it was one step ahead of the CMA. The plan has now switched from a traditional manager mix to a single fiduciary manager – Aon – after implementing a thorough strategic plan and running a very diligent tendering process.

The scheme

Schneider Electric is a French multi-national corporation operating in the energy management and industrial automation sectors. Its defined benefit (DB) pension scheme has a total membership of 3,532, of which 2,049 are deferred members and 1,483 are pensioners. It closed to future accrual in 2010, but retained the salary link for members until March 2019. As of March 2019, it had assets of £392 million and liabilities of £486 million, giving it a deficit of £94 million.

Rodney Turtle, who has been the chair of the trustees since March 2016, says the SPP is the main vehicle for delivering DB pensions to employees in the UK.

Looking back over recent years, he notes that the plan was very traditional, with assets consisting largely of gilts and equities. The plan has always had a good relationship with the company, but in recent years, "every triennial valuation was fairly challenging", he states.

The beginning

It was this that flicked a switch. The trustee board knew that the industry was evolving, and there were lots of opportunities. "We needed to break out. And as we've always had a very good relationship with the company, we wished to do that together," says Turtle.

This didn't mean an initial switch to FM; instead, they looked at various options. The first challenge was convincing the wider group that moving away from a traditional manager mix was the right move, as that was where globally Schneider Electric had been, pensions manager Jerry Gandhi explains.

Initially, Turtle says there were many conversations about liability-driven investments (LDI), but this broadened into looking at options that would include everything. The plan considered several options, such as LDI plus existing investments, LDI with partial FM, and full FM.

The first thing the trustees decided, with the help of their consultant, XPS, was

the need for LDI, which was completed in March 2018. The tendering for that was robust and open, says Turtle, with trustees given the opportunity to attend the beauty parade and briefings.

As Gandhi notes, the easiest option would have been to go with the existing managers or consultants, but "in order to get the best opportunity you need to go wider". As a result, an LDI structure using broadly half the scheme's assets was put in place. This allowed for some leverage to control certain downside risks.

The path to FM

In parallel to that, the trustees began looking at the other half of their assets. "We had a time horizon of 2024/25, to get to full funding. The current recovery plan, which committed cashflows from the employer, hedging from the LDI and outperformance from the return-seeking assets had to deliver that," Gandhi says.

Turtle notes that it was encouraging, when reviewing the triennial valuation, that the goal was feasible, and feasible using relatively prudent assets. With a plan the size of £400 million, they knew that gilts would be easily obtainable, however other illiquid assets, more diversified illiquids suited the scheme's time horizon, would have been very difficult to obtain, Turtle says.

"As a trustee board of the size that we were, we had to get ourselves educated on them, we had to have governance around them. Our pot size wasn't going to be terribly big, so it made it difficult to find the right things. So, for all those reasons, it seemed that the FM route suited us and our objectives," he notes.

Gandhi adds that the move made "logical sense". Initially, they considered just using FM for the return-seeking assets, but this developed into full FM after some consideration.

"We considered the return-seeking assets and the opportunities there, but concluded that going down the FM route, and wrapping in the LDI, would give an opportunity to work across a broader asset base, which could give the scheme slightly lower risk. Value at risk (VaR) was the important number. The shallower the glidepath, the lower the VaR, the smoother the journey to our outcome would be," Gandhi explains.

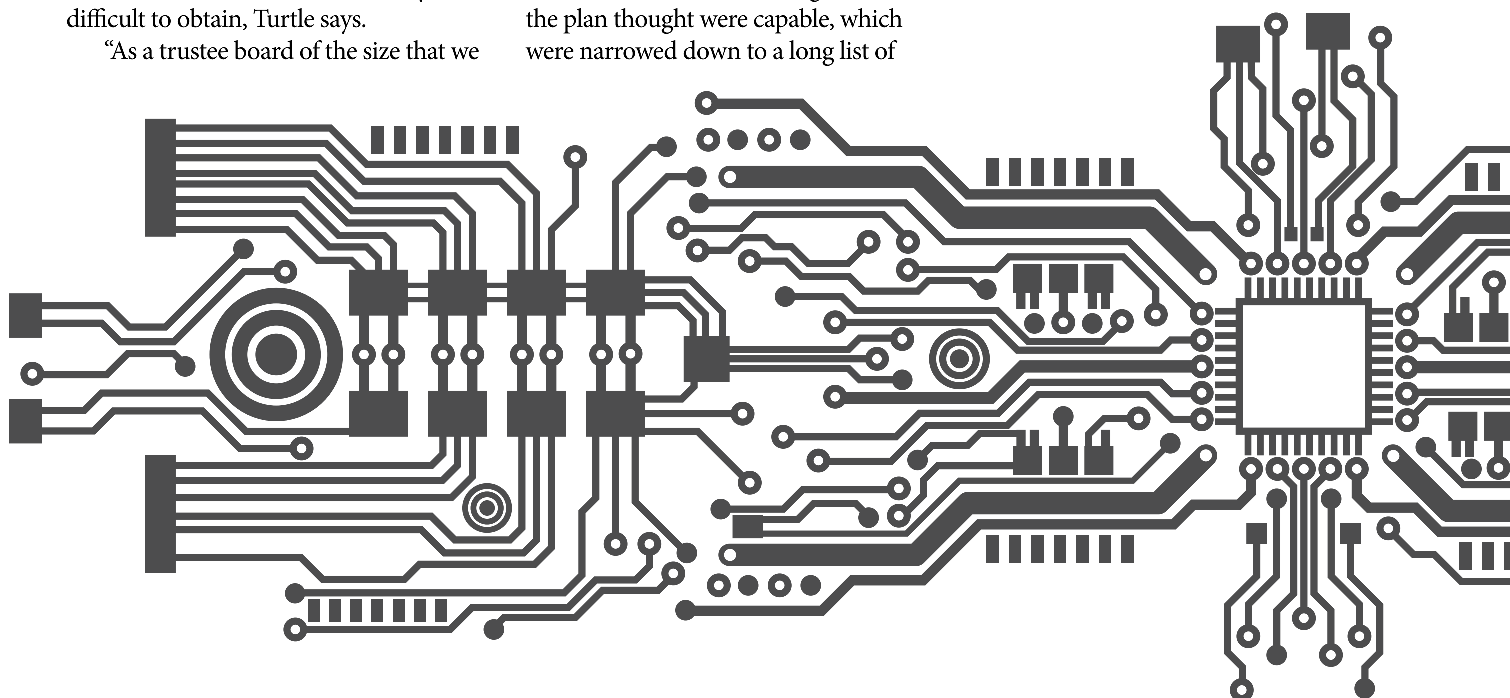
Before going to market, the trustees educated themselves on FM, hearing talks from two FM managers on what it meant. After that, the trustee board knew that it was the route they wanted to take, and asked their consultant to help them find the right FM manager.

After going to the market, there were around nine FM managers that the plan thought were capable, which were narrowed down to a long list of six, who received a request to put in a formal proposal. Turtle says this is where consultants are valuable, as they helped the scheme work out what they were asking for. Following that, the plan trustees met with four of them, visiting their offices, which was very important to get a feel for their culture.

"Going to the offices allows you to assess the culture of the place a bit better, even if it's only how they meet you, how they greet you, how they take you upstairs, what room they show you into. How they've decided to engage with you. What team they wish to bring along," Gandhi explains.

Criteria for choosing the FM involved a mix of things, such as culture, but the trustees also had evaluation reports. After the meetings, the trustees would record discussions of their initial impressions. After some time away, the trustees met again and went through a formal scoring matrix; there were about six dimensions, and one of them was gut feel, Turtle says.

"The idea wasn't to add it all up and then pick the one with the highest score, although that was important. The idea was to discuss all the dimensions of the scoring matrix, and properly talk about each of the shortlisted managers against



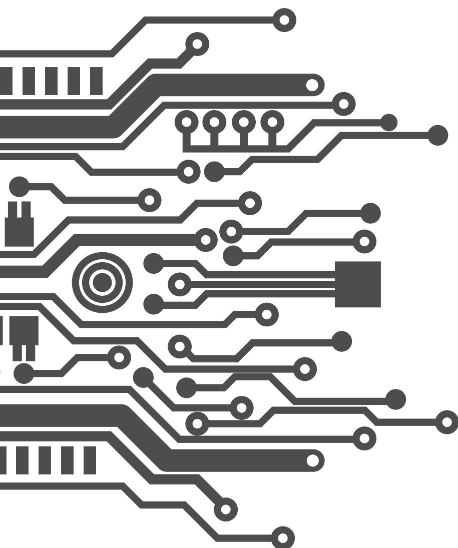
each of those criteria. Of the four, three of them could have done a good job. Of the three, there were two that stood out. It was then very hard to split the two, and it required a lot of discussion before we chose Aon," Turtle explains.

Gandhi adds that a key part of the tendering process involved discussion on fees. "We didn't rely on our consultant to do the fee negotiations. We pushed for the best fees from each manager, ourselves. The fee discussion formed part of the first phase when contacting those on our shortlist, and we actively negotiated both the quantum and structure of the fees with the final two. I believe we managed to negotiate fees that surprised the consultant."

Completing the process

The plan had found a FM, but the process was by no means complete. Work then began to sell their existing assets so they could be reinvested. Turtle notes that it's important to have a strategy, highlighting that liquid can be divested first, but some assets may have trading limits, or longer lead times.

"The implementation of the strategy was actually quite difficult in terms of bits of paper. I remember with some amazement that some of the fund managers required their documents to be faxed back to them. Also some of them allow you to sign in counterpart and when you've got trustees in various different locations – if you all have to sign on exactly the same sheet of paper that can be quite tricky."



The LDI was transferred over into the pool in June 2019, along with the remaining assets, completing the process. So far the plan has been "positively impressed" by the reporting and results. It is now in the process of putting in place FM oversight.

How important was the consultant's role within the process? "I believe that there's probably certain stages in the process that require statutory advice. So it's important that you have a consultant along for that," Turtle states. "Remember we're not experts and the SPP will only do what we've just done – we hope – once."

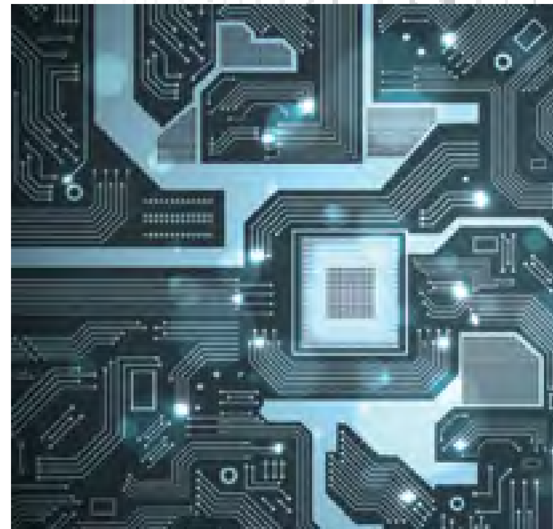
The Schneider Pension Plan took a very diligent approach to hiring an FM, but did this have anything to do with the CMA's investigation? Gandhi says that the CMA has been useful but Schneider Electric has a policy of being very open in its tendering process.

Turtle adds: "Because we're a multinational, operating globally, we aim to ensure we operate with full transparency in every contract negotiation wherever/whatever that might be fore. As a company we firmly believe it is unacceptable, even dangerous not to do so. Therefore, even though the CMA guidance on process was still evolving, our selection/appointment process fully complies with the now accepted best practice.

The benefits of FM

Gandhi says the company is hoping for no surprises, or continual ever-widening deficit as a result of the switch. It is working closely to support the trustee with an asset strategy designed to deliver a smooth flightpath to achieve the plan's target of being self sufficient by the mid-2020s.

Turtle also believes that having an FM will take any stress away from the



relationship with the company. Both believe that having an FM makes the investment process less burdensome and saves time and effort. Strong results are also key.

"In the FM reports we can see the LDI is delivering the required risk control. With the FM's appointment we also have access to a wider range of funds. This is providing us with the ability to achieve the target investment objectives but at lower risk and volatility. That would have been pretty much impossible on a DIY basis," Turtle adds.

Advice for other schemes

"The key thing is really be clear on what your objectives are," Gandhi says. "Where do you want to get to by when? If you go to the FM marketplace with a clarity of what that looks like they can come back to you with clear proposals of how they can support you."

He also advises schemes not to underestimate the paper trail and processes involved in appointment and transition. Schemes should work to manage the process tightly all the way through. "Have a project plan. It doesn't have to be the most sophisticated, but one with key milestones, and measure against them."

Written by Natalie Tuck