

INVESTMENT CONSULTANTS MARKET INVESTIGATION

Summary of hearing with Punter Southall Limited (Punter Southall) held on 23 November 2017

Introduction

1. Punter Southall explained that it primarily offers investment consultancy (IC) services to professional clients. They also provide oversight of fiduciary management (FM) services.

Competitive Landscape

2. Punter Southall said that they typically work with pension schemes with assets of less than £100m. These clients need to minimise their professional fees and this can be done by using particular asset selection such as diversified growth funds. Their experience is that larger pension funds (those with assets under management of greater than £3bn) tend to appoint the larger ICs, although some smaller consultancy firms appear to have been successful in competing for this business (such as Hymans with Local Authorities and Redington with larger pension funds). This tends to create a 'Big / Small' market.
3. Punter Southall explained that the core of their offering is to work with the client to develop the client's Strategic Asset Allocation. This details the recommended asset classes that the client should invest in. Punter Southall said that IC and FM is fundamentally about helping the client to manage and control their risk and the competence of the advice being given.
4. They agreed with the results of the FCA's manager selection work and they do not promise their clients that their recommended managers will out-perform. They focus on risk management and competency of the asset manager.
5. Punter Southall stated that their clients tended to be smaller funds (i.e. those with assets under management of less than £100m).
6. Punter Southall said that there are 15 firms in the FM sector.

Current regulation

7. Punter Southall said that they are covered by the FCA requirement for CFA30; most investment consultants are also fellows of the Institute of Actuaries.

Tendering for Contracts

8. Punter Southall stated that all IC clients would regularly review performance (the Pensions Regulator makes it a requirement of good governance that Trustees should review their advisors). All clients will assess performance on different criteria, but all will value:
 - (a) A lack of mistakes;
 - (b) An ability to communicate complex ideas and issues clearly and succinctly, and
 - (c) Delivery of the agreed level of service in a timely manner and to the specified budget.
9. They said that if clients are unhappy with the service provided, they will seek to replace the incumbent provider, often through a competitive tender. Notwithstanding this, Punter Southall have had some clients for 10 – 20 years,
10. Punter Southall would tender for contracts for any client and can find themselves competing against a wide range of firms active in the market.
11. Punter Southall said that they currently take part in 30 tenders a year, though this number is growing. Tenders can be roughly broken down into two broadly similarly sized types:
 - (a) Clients wanting only IC services, and
 - (b) Clients approaching the Group for a wider range of services (for example, including actuarial services). Around two thirds of their clients buy a full service from them.

Their experience is that clients find it easier to switch providers if they are seeking only IC services.
12. Larger mandates tend to be for a fixed period; smaller mandates are more likely not to be time limited.

Barriers to entry and expansion

13. Punter Southall did not consider there to be any major barriers to entry or expansion in IC, although there has not been a large number of new entrants over the last 15 years.
14. They believe that it is very costly for a firm to move assets when it changes FM. The selection process could also take up to a year.

Fiduciary management oversight service

15. Punter Southall stated that, historically, ICs would convert clients to their own FM service, however, over the last three years this has changed. Punter Southall's experience is that currently the majority of FM mandates are awarded through competitive tender.
16. Punter Southall said that they had taken a commercial decision not to offer a FM service. They do offer FM oversight and evaluation. Punter Southall explained that evaluation of a FM tender may take anything from 3 months to 1 year.
17. They have seen the use of FM evaluation services grow in the last 3 years.
18. Punter Southall said that they made a recommendation of a FM to a client following a review of how well the FM will meet the business objectives of the client. They review costs, including the exit costs of leaving that FM. Exit costs are much higher if the assets are held in the FM provider, not the scheme's name. It would be easy for a mandate of about £80m to incur costs of £250k in switching FM provider.
19. Punter Southall said that many clients find the FM market to be very opaque. Individual client solutions are generally considered to be bespoke in spite of there being underlying common factors. When Trustees want to assess the performance of their FM, they have to rely on the services of a third-party oversight firm to carry out assessments.
20. Whilst MiFID II will improve the level of transparency across the market, it will not go down to the level of detail that would be required to allow clients to assess the performance of FMs.
21. They were aware of the initiative by IC Select to develop an evaluation tool for ICs and FMs. They considered that IC Select have been working on this solution for some time, but have not produced many results so far. IC select had found it difficult to assess the performance of FMs.

Evaluation of investment consultants

22. Punter Southall explained that evaluating the performance of an IC is difficult as the Trustees may not follow the advice of the advisor, or may not execute this advice in a timely manner - the outcomes for the client may not be reflective of the advisor's advice. The sponsoring employer also has a role to play in decisions taken, so the scheme (and IC) are not fully accountable for scheme performance.

Client satisfaction ratings

23. Punter Southall considered that including some form of client satisfaction rating of ICs and FMs could have some benefits. They noted that Greenwich Associates currently produce some satisfaction data in their annual survey.

Conflicts of interest

24. Punter Southall stated that both IC and FM were not unusual in presenting, and having to deal with, conflicts of interest. Conflicts of interest should be similar in both markets as FM should reflect the execution of the advice that an IC would have given.
25. When acting in an oversight role, Punter Southall are aware of the potential conflict of obtaining information and assessing their competitors. In order to manage this conflict, Punter Southall ensured that there was no internal contact between the teams dealing with the overview and other adviser teams, the overview team sign strict non-disclosure agreements with the other companies.
26. Punter Southall said that increased transparency when handling potential conflict situations reduces the risks of conflicts occurring.
27. Punter Southall also said that advisers should not be offering their own asset management products as the conflict of interest created is clear.

Fees

28. Punter Southall explained that they generally operate on a fixed fee basis.

Moving clients to fiduciary management

29. Punter Southall said that they regularly reviewed their clients' position. Occasionally, clients would approach Punter Southall having decided that they want to move to a fiduciary management arrangement, on other

occasions, Punter Southall will mention fiduciary management as one of the options, or even a recommendation, for a client and the client will decide that such a move is appropriate. Punter Southall would seek to offer independent advice for clients to help facilitate this move.

Potential remedies

30. Punter Southall said that they did not support compulsory IC tendering. They explained that, even if this was every 10 years, it could result in hundreds of tenders each year which would be too many for most firms to take part in.
31. Punter Southall considered that Trustees should put all new FM mandates out to tender. The CMA should consider making this mandatory.
32. Punter Southall said that compulsory retendering would be more difficult to justify. The level of costs clients would incur to tender a service they may be satisfied with could be difficult to justify. An alternative may be that firms should have to document the reasons for their satisfaction with the current provider.

Master trusts

33. Punter Southall said that clients see master trusts as a solution to some specific problems – such as how to deal with additional voluntary contributions (AVCs). Whilst a credible solution, this can lead to conflict where the adviser has a master trust. Whilst the scale of the issue can be small (for example for many DB scheme AVCs form less than 1% of assets), the conflict can be greater where master trusts are being used for DC pension funds.