



IQPC Fiduciary Management Summit

A new way forward for Europe's pension funds?

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Outline

- What is FM and why use it?
- Impact of increased regulation
- Challenges for FM
- Future trends
- FM in DC
- Conclusions



What is FM?

- Outsourcing management & daily investment operation
- Trustee usually retains overall governing role
- Fiduciary Manager acts as CIO-type role with LDI, e.g.
 - Asset-Liability modelling
 - Asset Allocation
 - Portfolio construction
 - Risk budgeting
 - Manager Selection
 - Risk management
 - Ongoing monitoring



Different approaches to FM

- Consultants dominant + boutiques/specialist providers/asset managers
- UK – implemented consulting
- US – investment outsourcing
- Started in Netherlands over 10 years ago
 - 75% externally managed Dutch pf assets under FM
- UK - £40billion assets under FM – 4% of total
- Germany, Switzerland, Scandinavia, Italy starting



UK take-up slow

- UK market still dominated by traditional consultants
- Large consultants prefer to control many moving parts!
- Trustees reluctant to cede control
- UK funds notoriously slow to adopt new approaches
- FM not yet proven, immature
- FM most suited to small/medium schemes



Why might funds need FM?

- Increasing complexity and sophistication
- Stronger regulation and weaker sponsors
- Bigger deficits and tighter funding/solvency rules
- Increased pressure on trustees, professionalisation
- Inadequate resources
- Lack of investment and risk management expertise



Trustee challenges

- Need to modernise / professionalise investment approach
- 'Expected' returns, not same as *achieved* returns
- No 'loyalty bonus' for taking equity risk
- Need more explicit consideration of liabilities
 - Salary inflation, lpi, cpi, rates, duration, longevity
- Better protection against falling assets or rising liabilities
- Just switching to bonds not enough



No easy answers for trustees

- Bonds don't match liabilities
- With large deficit and weak sponsor, will lock in the deficit
- May reduce 'volatility' but increase risk of not being able to pay pensions!
- Trustees need more sophisticated approach
- Diversification of asset classes beyond equities/property
 - Hedge funds, private eq, infrastructure, swaps
- But many schemes can't do this themselves

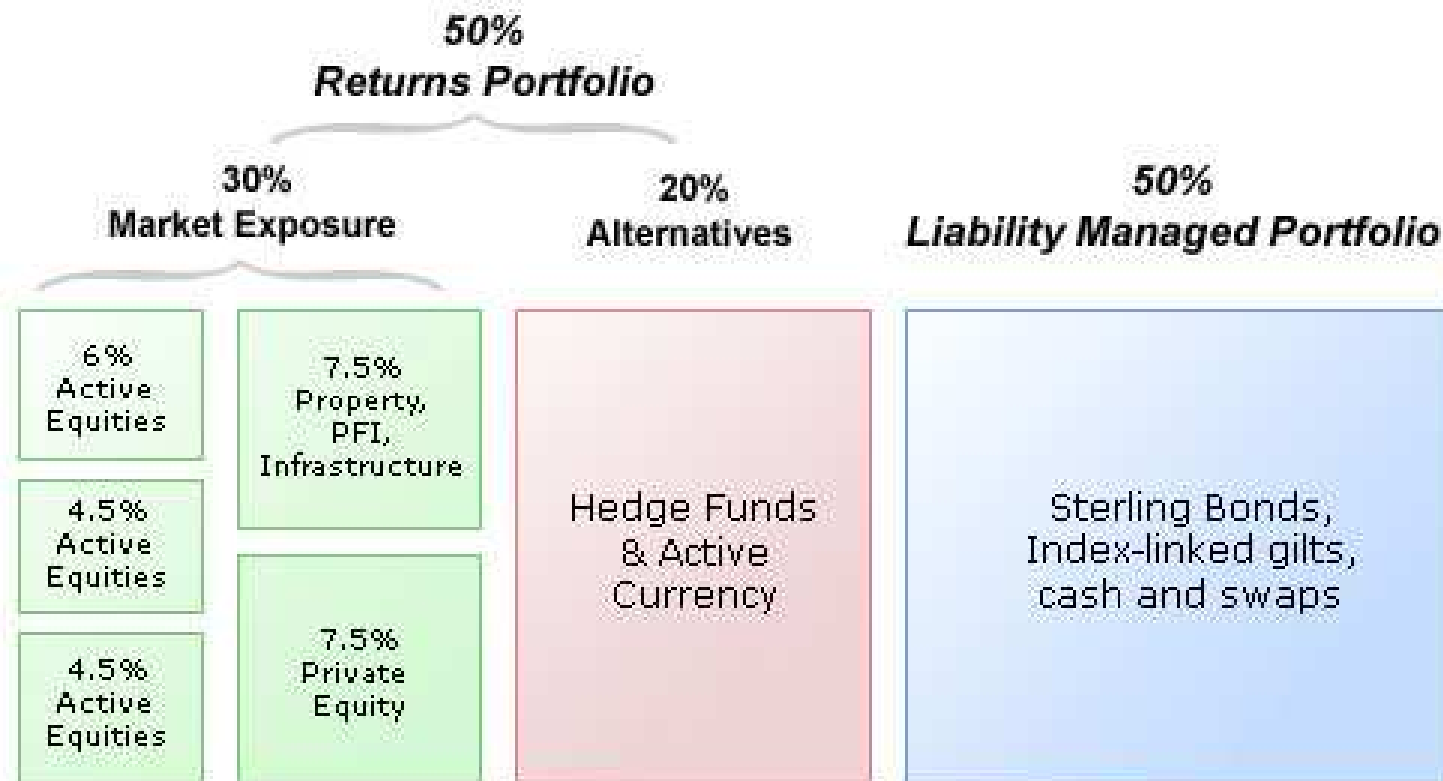


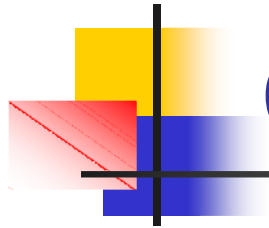
Impact of increased regulation

- Trustees must tighten up their operating procedures
- FM helps adapt to regulatory pressures
- Better governance and new funding rules can be met
- More sophisticated management and reporting
- Need specialist expertise

Case study – new approach

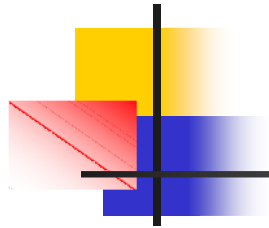
Small funds can't do this alone!





Challenges of FM

- How to measure success, failure, value added?
 - No standard performance benchmarks
- Fees? – Performance fees based on scheme funding?
- No code of conduct or standardisation
- Transparency and monitoring
- Need external review of risk budget and investment management



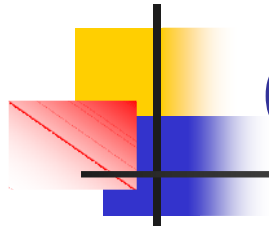
Future trends for FM

- Uncertainty over future growth as initial growth tailing off
- Not yet becoming mainstream
- As market matures, should get easier comparisons
- More competitive tenders, better transparency
- FM vs. longevity hedges, buy-in, buyout
- Use in DC schemes, not just DB



FM in DC

- DC schemes less complex than DB
- Large parts of risk absent
- But still need to ensure optimal asset allocation
- DC could benefit from better focus on delivering pensions
- Targetted income approach too difficult for many in DC
- FM might adapt but would need collective approach



Conclusion

- Complexity and sophistication drive move to FM
- UK slow to respond to increased challenges
- Consultants dominate
- Lack of standard benchmarks, performance and fees
- FM has great benefits for smaller/medium schemes