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Giving good advice

The advisory market place is changing, finds **Rachel Fixsen**, with new sources being tapped by pension funds

While trustees at pension funds may not always be experts in every field of investment, it hardly seems to matter when not only consultants, but banks and asset managers are only too willing to advise them.

Some argue that the independent advice of consultancy firms is the only advice worth listening to. But others say additional sources of advice mean more choice – as long as trustees are able to recognise the interests at play.

The notion of getting as much input as you can on important issues is very sensible, says Neil Walton, head of strategic solutions at Schroders. "Asset managers often have long, good relationships with their clients," he points out, and they are quite happy to offer their own perspective on particular problems.

Because of the nature of their involvement in certain markets, managers have something to offer that consultants don't. "Asset managers will have a very deep resource in whatever their specialisation is, whereas a consultant's resource will be wider," he says.

Walton, an ex-consultant, says that independence is highly valued. But where advice is concerned, it may not be everything, particularly if the listening party is well aware that of the interests of the adviser. "Do you get a better outcome from listening to someone who is not independent, but interpreting that, and bouncing that idea around?" he asks.

So why have investment banks become so involved in offering advice to pension schemes? Partly because of the negative impact that many corporate pension schemes now have on their sponsoring company. Accounting changes have pushed pensions liabilities onto the balance sheets of corporations, so the subject of pensions has moved higher up the agenda of finance directors, says Walton.

Walton: 'get as much input as you can'

As a result, investment banks are getting involved in pensions through their corporate connections, he adds.

The equities bear market in the first few years of the new millennium weakened many pension funds. "The pensions industry found itself in a hole, and that raised the question of whether the relatively narrow pool of advice was in their best interests," says Walton.

John Conroy, principal at consultancy Psolve asset solutions, says he welcomes the fact that advice is now coming at pension schemes from different directions and different types of provider.

"Clients need options," he says. "We want there to be more people in the market doing that. There's been too much separation before."

When the banks also offer advice and ideas it raises the level of the game, says Conroy. Part of the reason why banks and asset managers have traditionally avoided moving into the advice arena is fear that they will step on the toes of existing providers, he says. "Culturally, it hasn't been their playing field."

But he questions the value of independence in the consultancy profession – and the perception of it. "The reality is consultants act as a distribution network for the managers," he says.

In any case, clients can judge the perspective the advice is coming from. "Clients who are interested in integrated solutions will be conscious of where the conflicts are," he says. "It will be incumbent on the provider to demonstrate why a solution is in the interests of the provider."

Peter Brackett, head of international consultant coverage at Morgan Stanley Investment Management and a former Watson Wyatt consultant, says that investment banks and asset managers have been positioning themselves to offer that advice, and that pressure from the regulatory side has also pushed pension funds towards other providers of expertise.

The first Myners review told trustees they should be seeking the best advice on actuarial matters and investment separately, he says. Then in early 2005, the second Myners review said that within investment advice, advisers should be sought separately for asset allocation and manager selection.

"In terms of industry pressure, the Morris Review came out with very similar recommendations," says Brackett. "This places a greater emphasis on the trustees to ensure they've got the knowledge the need to make their decisions, or to make sure they are getting the right advice to support those decisions."

The other factor that is changing, he says, is the resources that are now coming on line. The momentum has been created for providers to come up with innovative solutions that address the pension fund problem, he says.

The solutions, which may be derivative-based, have come from the investment banking community. Now, it is not uncommon for trustees to be sitting in their meeting with investment consultants and also a representative from an investment bank putting the case for using credit-default swaps, for example, says Brackett.

It is not that they are in competition with the investment consultants, but that there are differences of advice given to the same set of trustees but that pension funds find that to consider this type of solution they need the specialist advice of the banks. "The investment consultant would typically have knowledge of derivatives, but wouldn't have the hands-on experience of using them," says Brackett.

Andrea Canavesio of Mangusta Risk in Rome says that in most cases where managers and banks give advice to pension funds, it is of a different nature to that provided by consultants. "Asset managers and investment banks give a more 'operational' advice on single transactions," he says. "But investors usually want to be supported by their independent consultants on this matter also."

Hendricks: 'no one sole adviser to funds'

Robert Burgon, secretary and pensions manager of the Plumbing & Mechanical Services Industry Pension Scheme in the UK, says he is receptive to advice given by parties in the investment process other than consultants. "We would listen to them, but we don't look to them for advice per se," he says.

However, Burgon says that the scheme's investment consultancy is always present when the fund managers are there, and if the managers did come up with ideas, he would take the consultants' advice on how to consider these

Conroy: 'clients need options'

ideas and how to proceed.

And smaller independent consultants have been emerging alongside the larger established consultancies.

Edinburgh-based consultancy Blacket Research, founded just over a year ago, says it aims to help pension funds measure and monitor the quality of the advice they receive from their investment consultants.

Brackett of Morgan Stanley predicts that this kind of firm will, in time, become more prevalent and work alongside trustees. This is likely to be in niche areas such as governance, he says.

It is important that advisers to a pension scheme are truly independent, Burgon says.

Conflicts of interest occur in all walks of life, but the question in the pensions arena is how the parties are dealing with them, says Ruud Hendriks, GSAM's co-head of sales for Europe, Middle East and Africa.

"It is important for a consultant, or any advisor, to say upfront in what capacity they are advising the pension fund – for example, whether it is as an ALM provider or a broker," he says. "It is essential that pension funds are given the necessary information to be able to tell the difference." For this reason, the onus is clearly on the adviser to state its position, and if it fails to do that, the advice has less value, he says.

Pension funds have always received advice from several different sources, from actuarial, accountancy and investment consultancy firms, he says. "There is no one group that can claim to be the sole adviser to pension funds."

But with asset managers starting to advise on matters such as duration extension, the diversity of advisory sources is now more explicit than before.

It can certainly make sense for pension funds to tap other sources of advice as a way of checking the advice they have been given, says Hendriks. For example, GSAM was approached by a Dutch pension fund that had received advice from an ALM provider, which has a dominant share of the market in The Netherlands, he says. The fund simply wanted a second opinion, which is perfectly natural, he says. "It makes sense for a pension fund to regularly check the quality of advice they are getting."