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Retirement Solutions

New, but with experience:** TPT Investment Management's managing director, Nicholas Clapp, and investment director, Peter Smith, talk to Pensions Age about how its new fiduciary management offering blends its own experience of managing pension fund money with the opportunity to invest in private markets and focus on climate change, due to its long-term investment horizon* ***p88

The fiduciary management reckoning:** Louise Farrand considers the continual impact from the 2022 gilt crisis and the fiduciary management reviews it has generated* ***p90

Fiduciary management focus:

The next stage

TPT Investment Management's managing director, Nicholas Clapp, and investment director, Peter Smith

Nicholas Clapp

Peter Smith

New, but with experience

TPT Investment Management's managing director, Nicholas Clapp, and investment director, Peter Smith, talk to *Pensions Age* about how its new fiduciary management offering blends its own experience of managing pension fund money with the opportunity to invest in private markets and focus on climate change, due to its long-term investment horizon

TPT Retirement Solutions is entering the fiduciary management market, as TPT Investment Management (TPTIM). It is doing so with quite a unique background, being owned by an asset owner. What benefits do you feel TPTIM's fiduciary management operating model provides schemes?

Nicholas Clapp: TPTIM is new but it's not new. It's new in so much as we're launching fiduciary management as a standalone service to pension schemes. At the same time, we've been doing fiduciary management for well over a decade, it's just been part of the solution that we provide inside our master trust.

We come with a different slant on what fiduciary management can look like, bearing in mind our ownership structure. We've got a past track record. We've got successful performance and we've got scale.

Peter Smith: What we are doing is providing non-master trust schemes access to our investment strategy, which has been developed over the past 15 years. It's not something we're having to build from scratch and create a track record. Also, our private market allocation has been built up over this period. Therefore, it has a different risk, return and exposure profile from something that is being built from scratch today.

Having an asset owner perspective means we're generally thinking 20 to 30 years ahead. I think it gives us a different time horizon compared to other fiduciary managers, particularly around important topics like climate change, and how we engage with the underlying investee companies that the trustee has a holding in.

Clapp: Because of our ownership structure and the operating model that we deploy, we offer something that is different to the rest of the market. We don't have an asset manager thought process. We don't have a consultant thought process. We have an asset owner thought process. We don't have to worry about other stakeholders in the business that require certain targets for us to hit. We are here solely for that singular focus on what that client's end goal is.

Historically, fiduciary managers have been heavily invested in public markets, due to pension schemes' need for high liquidity and low fees, thereby limiting the scope for alternative assets and alpha generation. How does TPTIM approach asset allocation and to what extent are the private markets a part of that?

Smith: When I started at TPT back in 2008, pension fund strategies were very much equity and corporate bond focused, with a small allocation to property. But because we are historically an asset owner, we started looking at diversification into unlisted assets. We have long-dated liabilities with some of our clients open to new accrual, meaning we have a long-term mindset when it comes to asset allocation. This means we can get exposed to long-dated, more complex, illiquid assets, such as unlisted infrastructure, which we believe can ultimately can provide an uptick in return and an increased level of portfolio diversification.

We are willing to give up liquidity if we think we can get access to a return premium not available in the public markets. It provides diversification to the portfolio, recognising it might not be the lowest cost option. Private markets are generally more expensive than public markets, but as long as the net return is above our return objective we're willing to do that. Ultimately, it's around value for money, rather than just cost.

One such change in pension schemes' investment strategies in recent years has been an increased focus on climate change. How does TPTIM measure climate risk for its clients?

Smith: We explicitly incorporate positive allocations to things that can help solve the climate problem. That generally sits in the private market space. For example, we have a significant allocation to renewable infrastructure, be it energy generation, or storage, or grid.

Every three years we stress the portfolio against a number of climate scenarios, and then seek to understand the potential impact on the portfolio, recognising that climate scenarios are still very nascent. We take this into account when we're looking at future asset allocation, particularly on the solutions side.

When we're working with external managers, we look at how they incorporate climate change into their investment philosophy, portfolio construction and security selection to ensure that it is consistent with our views. With regards to reporting, all our clients will have access to carbon footprinting data. One of the things we're currently doing is exploring how to do that consistently across all of the portfolio given data challenges. At the moment, we're rolling that out to infrastructure and the next challenge with that is private credit.

Clapp: Whatever we do here for our largest client we can apply to our smallest client, as we're able to make sure that these solutions are scalable.

The growth in the fiduciary management market in recent years has compelled many providers to streamline their operations. While having generated some advantages, it can also be argued that some fiduciary managers have, as a result, somewhat pivoted away from clients' specific needs. How does TPTIM balance ownership and alignment?

Clapp: We've taken the opportunity to refresh our capability of how we deliver for clients at scale. That's taken a significant amount of work over the past 12 months in order to set up new fund structures and enhance our systems and reporting. All of which is very operational, but it leads to a better solution strategically for the client. This means that we don't have the problem of a change of business model diverging away from what the client requires.

Probably at the heart of that is the ownership structure, where TPT is ultimately owned by a pension fund. So, we're very close to understanding our clients and the issues they are grappling with. We're very empathetic to that. Our solution is designed explicitly with that in mind.

Smith: We deliver good outcomes for a range of pension schemes. We manage schemes ranging from £10 million up to £2.5 billion. Whilst they all have slightly different requirements in terms of endgame target, return and risk objectives, ultimately what they're trying to do is deliver good member outcomes. We recognise that scalability is key in doing that. We've managed to think about designing that into what we've built in the fiduciary management space.

How do you ensure that TPTIM is positioned to deal with changing scheme requirements?

Clapp: There's the changing regulatory environment and changing funding levels that are generating different trends, in terms of where schemes might actually end up or what they're targeting as an endgame.

Then there is the changing requirements on the responsible investment side of things as well. For all of these changing requirements the tide continues to only move in one direction.

Talking to trustees, their job is vastly different from the job they did even three or four years ago, let alone 10 years ago. They see it as only becoming more complicated in terms of where they spend their time. So, the more that we're able to free their bandwidth up as a fiduciary manager, the more they can focus on the areas that are strategically important to them.

Smith: Ultimately it comes down to making sure you have a good enough understanding of what the trustees' objectives are. I think the key bit that's changed over the past 18 months is what level of illiquidity they require in the scheme, given that flexibility towards the endgame choice.

If a scheme has a very firm view that they want to run on, allocating to long-dated illiquid assets is still an option for them. For those schemes that want to keep their options open, it's making sure that you give them the flexibility to change their investment strategy at relatively short notice. One thing that we have been able to do is, by bringing about pooling and scale, we can create effectively a market where we can allow schemes to benefit from different endgame objectives. We can actually facilitate schemes changing their investment strategy at relatively short notice. By bringing together a large number of schemes within a pooling arrangement we can provide increased flexibility to individual schemes.

The fiduciary management reckoning

Louise Farrand considers the continual impact from the 2022 gilt crisis and the fiduciary management reviews it has generated

Summary
- Fiduciary management is entering a new phase, prompted by several seismic events: The gilts crisis in autumn 2022 and the Competition and Markets (CMA) review of the market.
- More broadly, the market is evolving and maturing, as new players enter the market and consolidation happens.
- Many DB schemes are going through strategy reviews to learn lessons from the gilts crisis. What should they consider – and what other trends are defining fiduciary management?

The repercussions of the gilts crisis of autumn 2022 are still reverberating for many DB pension schemes. Trustee boards were already concerned that they were not responding quickly enough to fast-changing markets; the financial crisis of 2008 demonstrated that investing in a straightforward mix of equities and bonds would not deliver their funding objectives.

Few pension schemes were able to move quickly enough to take advantage of opportunities in the aftermath. "Post 2008, and going into 2009, trustees were slow to move into what turned into a 15-year bull market," observes TPT head of investment, Peter Smith.

The introduction of in-house chief investment officers and fiduciary management gathered pace in the UK after the events of 2008. But despite all the lessons learned, DB schemes were unprepared for a seismic event like the gilts crisis of autumn 2022.

Nobody expected it. The gilts crisis categorically debunked the myth that equities and bonds are uncorrelated and raised questions about DB pension schemes' widespread use of liability-driven investment (LDI) strategies.

Despite their post-2008 move towards delegated governance and the implementation of swifter decision-making, many DB schemes – and their fiduciary managers – were not immune to the volatility. As XPS Group head of fiduciary management oversight, André Kerr, recalls: "There were some fiduciary managers that had an absolute disaster during the gilts crisis."

TPT commercial director, Nicholas Clapp, adds: "The gilts crisis threw everyone into a spin. I thought that six months later there would be a collective review of where people were, because the fiduciary management governance structure did not hold up well in the gilts crisis. I anticipated that would result in new appointments and reviews. However, the pace has been slower than anticipated, and we are only getting to that now."

The reason for the delay is the abrupt improvement in DB schemes' funding levels, adds Smith. "There has been a whole heap of work to be done from an investment perspective. DB schemes have had to get on top of that first. They are in an entirely different place, so what does their end goal now look like? Only after that has been established can schemes start think about what vehicles will take them to that destination."

Governance reset

The majority of DB schemes which use fiduciary management are going through a strategic review at present, reports Isio partner and head of fiduciary management oversight, Paula Champion. Trustee boards are resetting their objectives and thinking about different governance options, she says. In particular: "They are thinking about whether they get help and guidance and assistance with assessing their fiduciary manager and making sure they are doing a good job," she reports.

Fiduciary managers are also learning lessons from what happened during the eventful autumn of 2022 – particularly in terms of managing their exposure to illiquid assets. Champion explains: "Off the back of the gilts crisis, trustees were much more conscious of having enough cash collateral for their LDI portfolios and making sure those were managed effectively. There is a need and a want for trustees to have more liquid portfolios and to monitor the liquidity of their portfolios over time.

"This means two things for fiduciary managers. One, they want to make sure they have got differentiating assets that are illiquid – so alternative illiquids. And two, they are ensuring they have their reporting and communication aligned to what trustees want – so, evolving their reporting for fiduciary clients to give them greater visibility and shed light on the liquidity of the portfolio."

Under pressure

Before the gilts crisis, fiduciary managers were growing fast. "Gilt yields were falling, so even if they did nothing they were growing. I think most fiduciary managers expected that trend to continue," recalls Kerr, adding: "When things started to turn it became a very different situation: cost pressures, gilt yields going in the opposite direction, fees going down because of new entrants to the marketplace. It was not the easiest of marketplaces for fiduciary managers to operate in and it put a lot of pressure on them as businesses."

Champion agrees, adding: "We have seen fees ticking up. One in three fiduciary managers have increased their fees over the past year or two. So, while there was an increased saving on the back of the CMA review, I think some of that has been whittled away by inflation and the pressure on fiduciary managers."

The CMA review has had other positive effects on the market, Champion qualifies. "When the review happened, we were in a position where a lot of schemes had to take their fiduciary managers out to a competitive tender. I think that helped fiduciary managers to sharpen their pencils, not just in terms of fees, but also in terms of servicing, trying to very succinctly communicate their USPs as well. It helped to put a little bit of space between the different types of fiduciary manager and their areas of expertise. In that way, it made the market clearer and more transparent."

Kerr is still unconvinced that the market is transparent, particularly when it comes to comparing performance. He argues: "Fiduciary managers have a massive asymmetry of information, and I would argue that most trustees aren't able to make a judgement call on whether they are doing a good job or not."

He suggests trustees should be unafraid to challenge their fiduciary manager and have a strong framework in place: "Don't just accept that what they say is correct. The difficulty is, a lot of people don't feel they are able to challenge properly; they don't like asking questions that make them look difficult or feel stupid. Generally, if you have a question that you want to ask, ask it! Other people will probably not know the answer as well. Don't be afraid to channel your inner five-year-old and keep asking: 'Why?'"

What's next for the fiduciary management industry?

Larger mandates are becoming more common, reports Clapp. "Fiduciary management has worked its way through the sizes over the years – slowly going up through the sizes, starting with smaller schemes."

Now, very large schemes are thinking about it, Clapp says, explaining: "In the big picture of things, UK DB schemes are small asset owners. It's not about UK rankings – it's the context of who are the global asset owners that are able to negotiate strong contracts with different fund managers to the benefit of their clients."

With many boasting much improved funding levels, DB schemes are also reviewing what their end games now look like. Champion says: "All these discussions are very active. In terms of the proportion of schemes that have come to a conclusion on that, we are less sure at the moment … fiduciary managers are very cognisant of the fact that they need to address that with trustees and talk about it."

Another growing trend is a reshaping of the fiduciary management market, with new entrants to the market – such as TPT Investment Management – and consolidation of fiduciary managers, says Zedra client director, Daniel Walsh. "Mercer are acquiring Cardano, and there's a sense that this may not be the end of consolidation."

Trustees should be unafraid to ask hard questions, says Walsh. "If you've appointed a manager because you believe in their philosophy and their approach, if they're then acquired or acquire another firm, what does it mean? Ask what's happening and what it means for the proposition going forward."

Fiduciary managers are confident about the future. "We anticipate there is significant growth still to happen – both in terms of schemes embracing it and schemes switching over for a different approach," says Clapp. "We also think there will be more options in terms of endgame solutions but also in terms of operating models available to pension schemes in the fiduciary management world."

Written by Louise Farrand, a freelance journalist