FCA Asset Management Market Study

Peter Parry
Policy Director

Many UKSA members will have seen press comment about the FCA's report. It has been praised for its thoroughness in identifying the shortcomings of the industry and, in particular, in its treatment of its customers. However, many of the weaknesses identified have been known for a long time and there has also been criticism of the regulator's failure to propose immediate action in some areas – a stance which smacks of obfuscation and foot-dragging by the FCA.

Members might like to read Martin White's article in the March edition of The Private Investor ('The FCA's Asset Management Market Study') and UKSA's submission to the FCA in February for the regulator's study of the asset management market. Both can be found in the members' section on the UKSA website.

In the following article Cliff Weight gives a personal view of the Asset Management Market Study Final Report of the Financial Conduct Authority published on 28 June 2017. Cliff is a member of both UKSA and ShareSoc and is also ShareSoc's Policy Director. The article was written as a blog for the ShareSoc website. Cliff's views and comments are forthright and make a valuable contribution to the debate.

Peter Parry – Policy Director

Damning FCA report but no quick remedies to asset manager problems

In November 2015, the FCA launched its market study into asset management. We are now 20 months later, the "Final Report" has been published and little progress has been made apart from a lot of wringing of hands. The 113 page report is essential reading for investors who wish to preserve their wealth.

The report is damning, e.g.:
"There is weak price competition"
"firms do not typically compete on price, particularly for retail active asset management services"
"lower prices do not seem to be available for equivalently sized retail funds" (whereas, as the report notes, prices tend to fall as the size of the investment mandate increases for segregated mandates sold to larger institutional investors)
"there is no clear relationship between charges and the gross performance of retail active funds in the UK".
"There is some evidence of a negative relationship between net returns and charges."
"the worst performing funds were more likely to be closed or merged into better performing funds."
"retail investors do not appear to benefit from economies of scale improving their money together."
"high levels of profitability, with average profit margins of 36%."

However, the remedies seem rather tame and of limited impact in the short-term. For example, "we continue to support the disclosure of a single all-in fee to investors" fails to mandate this or recommended it as best practice. Many of the other recommendations require further consultation.

Nevertheless, the highlighting of the high levels of profitability will put pressure on the industry to reduce its charges, which can only be good news for the retail (individual) investor in the long term.

My personal views

The failure of the engagement process between shareholders and companies has led to a breakdown of trust between companies and shareholders. One consequence of poor engagements is media reporting of egregious pay, shareholder revolts, uprisings and Shareholder Springs that further fuel the general low levels of trust by people generally in companies and their directors. This contributes to a downward spiral of trust which needs to be broken. The low levels of trust of UK business by the UK people, is reflected in Mrs. May comments (e.g. Theresa May is drawing up legislation to tackle unscrupulous bosses and excessive boardroom pay, as proof she intends to build a Britain 'that works not for a privileged few but for every one of us').


Cliff Weight

The changes needed will not be easy. There are three key points, which need to be addressed, but make change difficult. Those with personal interests will resist change not to their personal advantage.

First, the ownership structure of public corporations is **corrupted** (a strong word, but it is true and needs to be said). Too many shares are controlled by institutions whose interests are not the same as **the beneficial owners**. To make any meaningful statement about the place of shareholders in the governance system it is essential to distinguish between those who are beneficial owners and those who are not. Further, it is essential to acknowledge the existence of beneficial owners who are not shareholders. Many regulation, governance codes and consultation documents do not define these terms (investor, asset manager, beneficial owner, pension fund member) nor distinguish between them.

Second, the individual investor is often exploited by the financial services industry.

Third, the financial services industry is fundamentally conflicted vis-a-vis promoting good corporate governance, e.g. the investment banking businesses of debt and equity funding, 'corporate actions' (i.e. acquisitions and disposals) and general corporate advice rely on transactions as a revenue source, regardless of whether those transactions are beneficial to their clients. There is a bias for action, which may not be in the best interests of shareholders, or the company in the long term.

My personal views on how to invest:

For myself, the report confirms my views about investment strategy and I will continue my investment strategy of:

- Exposure to overseas stock markets, via (i) low cost passive funds (e.g. Vanguard) and (ii) a limited range of active funds of overseas stocks with reasonable charges held in a cheap wrapper to gain the benefit of reduced fees.
- A buy and hold strategy of FTSE100 companies.
- An active portfolio of smaller growth companies (mostly AIM) selected mainly from those who present at ShareSoc investor events. This is the smallest part of my portfolio.

Two good articles in the FT are worth reading:

- Carry on Consulting — an achingly slow fund regulation farce. FCA needs to act faster and the industry must stop prevaricating by **Merryn Somerset Webb**. See here (requires FT subscription).

- Asset managers ripping off customers is nothing new: The FCA's report is a travesty that is bereft of remedies, writes Gina Miller. See here (requires FT subscription).

by Cliff Weight