The investment platforms market – pay attention class!

by Peter Parry

One of the problems for private investors is that topics regularly come up which at first sight look as though they ought to be labelled like some types of medication: 'Warning; this product may cause drowsiness'. Often, however, these are of vital importance to investors and need to be understood and taken into account when making investment decisions. This is true of the issue of charges levied by platform providers for the use of their platforms and any exit fees when switching platforms. Following publication of the FCA's interim report and consultation on the subject, Roger Lawson of ShareSoc has recently written an excellent blog on the subject. As I cannot improve on it, Roger has given kind permission for us to reprint his blog in full below.

In its consultation the FCA poses a number of questions. Many are complex and technical. UKSA and ShareSoc are considering how best to respond but plan to make appropriate joint representations to the FCA. If you have any comments or thoughts of your own, please let us know.

Roger Lawson's blog and advice to investors

The Financial Conduct Authority (FCA) have just published an interim report on their study of "investment platforms". It makes for very interesting reading. That is particularly so after the revelations from Hardman last week. They reported that the revenue per assets held on the platform from Hargreaves Lansdown (HL) was more than twice that of soon to be listed AJ Bell Youinvest. HL is the gorilla in the direct to consumer platform market with about 40% market share. HL earns £473 per £100,000 invested while Youinvest earns only £209.

That surely suggests that competition is weak in this market. Indeed the FCA report highlights that investors not only have difficulty comparing the charges of different platforms, but they do not seem too concerned about high charges as they focus more on other aspects of the service provided. It also says on page 23 of the report: "Our qualitative research also found that consumer satisfaction levels are sometimes linked to satisfaction with overall investment returns, which tend to be attributed to the performance of the platform. This suggests some confusion about consumers' understanding about platforms' administrative function as opposed to the performance of investment products. So it is possible that consumers' relatively high satisfaction levels with platforms could be influenced by the positive performance of financial markets in recent years". In other words, the consumers of such services are very complacent about the costs they pay at present.

Another piece of evidence that this is not a competitive market obtained by the FCA was that they found that when platforms increased or decreased prices it had no significant impact on flows in and out of the platform. No doubt some platform operators will read that with joy, but others despair! Indeed when I made some comments on Citywire effectively saying I thought it suspicious that there were so many positive comments about Hargreaves Lansdown in response to an article reviewing the Hardman news, particularly as they were clearly much more expensive than other platforms who provided similar effective services (I use multiple ones) I was bombarded with comments from lovers of the HL service. Bearing in mind that platform charges can have a major impact on overall returns in the long term from stock market investments, you would think investors would pay more attention to what they are being charged.
One particular problem is that switching platforms is not only difficult and a lengthy process but can also incur charges. This is clearly anti-competitive behaviour which has been present for some years and despite complaints has not significantly improved.

The FCA summarises its findings as:

- Switching between platforms can be difficult. Consumers who would benefit from switching can find it difficult to do so.

- Shopping around can be difficult. Consumers who are price sensitive can find it difficult to shop around and choose a lower-cost platform.
- The risks and expected returns of model portfolios with similar risk labels are unclear.
- Consumers may be missing out by holding too much cash.
- So-called “orphan clients” who were previously advised but no longer have any relationship with a financial adviser face higher charges and lower service.

That’s a good analysis of the issues. The FCA has proposed some remedies but no specific action on improving cost comparability and the proposals on improving transfer times are also quite weak although they are threatening to ban exit charges. That would certainly be a good step in the right direction. Note that a lot of the problems in transfers stem from in-specie transfers of holdings in funds and shares held in nominee accounts. Because there is no simple registration system for share and fund holdings, this complicates the transfer process enormously.

One interesting comment from the AIC on the FCA report was that it did not examine the relative performance of different investment managers, i.e. suggesting that lower cost investment trusts that they represent might be subject to prejudice by platforms. They suggest the FCA should look at that issue when looking at the competitiveness of this market.

In summary, I suggest the platform operators will be pleased with the FCA report as they have got off relatively lightly. Despite the fact that the report makes it obvious that it is a deeply uncompetitive market as regards price or even other aspects, no very firm action is proposed. But informed investors can no doubt finesse their way through the complexities of the pricing structure and service levels of different platform operators. I can only encourage you to do so and if an operator increases their charges to your disadvantage then MOVE!

The FCA Report can be found here: https://www.fca.org.uk/publication/market-studies/ms17-1-2.pdf