



## Decent pension returns in turbulent times

Strictly embargoed: Not for publication or broadcast before 00.01 Hrs, April 8th, 2009

Pension fund managers should only invest in companies where they are fully satisfied about the long-term potential for business, according to the former Director General of the CBI, Sir John Banham. In a paper published today by the RSA (April 8<sup>th</sup> 2009), he argues that pension funds and investors should take greater responsibility for how and where their money is invested, with trustees acting as 'owners of companies' rather than as 'speculators in shares'.

The paper is part of the RSA's *Tomorrow's Investor* project, which has been examining how investors can become more informed and engaged in the management of their money. In his paper Sir John argues that investors need to be encouraged to 'bridge the ownership gap', taking greater control in choosing the companies in which their fund managers invest.

In his report, *Decent Pension Returns in Turbulent Times*, he sets out eight tests that companies should pass in order to merit pension fund investment, including:

- *Are they well positioned?* The underlying 'forces at work' in the market must favour the company. Is the company well placed to exploit lifestyle changes such as a greater concern for health and exercise, the environment and so on? Is it well positioned?
- *Do they have the right portfolio?* Does the parent company add value to subsidiaries and provide attention from top management?
- *Is the top line growing in real terms*, without the need for mergers and acquisitions to mask management's failure to offer products and services that customers are ready and able to pay for?
- *Do they have world class assets?* ...plants, people, technology? Assets are crucial to the company's competitive position must be in good repair (people, property, equipment etc).

- *Are they collaborative?* Does the management understand the importance of partnerships, with all the groups with a stake in the company's future: suppliers, customers, local communities and their people?
- *Is their financial position sustainable?* Does the company earn returns that exceed the weighted average cost of capital by a margin sufficient to compensate shareholders for the risks they are running?
- *Is the right leadership in place?* Does the company have sound leadership and an effective management team who build an effective, cohesive work force with shared values and a passion for winning?
- *Is the company accountable?* Is the management held to account by the Chairman and Independent directors? In particular, they will be prepared to resign if they are not fully satisfied that the business is being run in the interests of all the stakeholders rather than the management?

Sir John concludes that worryingly only one in five of the current FTSE 100 constituents would pass his tests. He concludes that the dismal performance of the UK fund management industry is down to a British insistence on seeking to avoid risk, rather than a determination to manage it effectively. He believes this problem is compounded by a 'little Englander' attitude to the way investment funds are allocated to different classes of assets, as well as the ineffective regulation of Britain's major financial institutions. He concludes that this has resulted in a yawning gap between the ultimate owners of UK public companies and their managements, and perverse incentives for those managing other people's money.

**Commenting on the publication of his report, Sir John Banham said:** "The ultimate owners of publicly quoted companies in Britain – pension holders and those managing their savings and investments – must step up to the responsibilities of ownership and bring about a paradigm shift in the way we approach fund management. Whilst improved financial regulation will help, it cannot provide long-term solutions to the crisis we face. Shareholder engagement with the board of directors is essential if we are to prevent the average pension holder having to spend less, save more, and work longer to make ends meet."

*Decent Pension Returns in Turbulent Times* follows an RSA report *Tomorrow's Investor* that argues millions of pounds could be added to the value of the UK's pension pot by reducing charges. It found that people were shocked to discover that charges can swallow up to 40 per cent of the value of their pensions. The RSA is developing proposals for a low

cost pension fund which would seek to better inform and engage people in its decision making.

### **Notes to editors**

- 1. For more information contact Luke Robinson, RSA Head of Media on 020 7451 6893 or [luke.robinson@rsa.org.uk](mailto:luke.robinson@rsa.org.uk)**
2. The Tomorrow's Investor project has been funded by PricewaterHouse Coopers and Invesco Perpetual.
3. The RSA is developing a business plan for a new pension fund, offering investors a highly transparent, accountable, low cost fund with reasonably secure returns at a decent level of risk.
4. Development of the business plan for the 'Tomorrow's Investment Fund' will be led by David Pitt-Watson, founder and former Chair of Hermes Equity.