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| Institution: University of Oxford | | |
| Unit of Assessment: 17 – Business and Management | | |
| Title of case study: Influencing the Financial Conduct Authority and Competition and Markets Authority to Regulate Investment Consultants | | |
| Period when the underpinning research was undertaken: 2012-2020 | | |
| Details of staff conducting the underpinning research from the submitting unit: | | |
| Name(s): | Role(s) (e.g. job title): | Period(s) employed by submitting HEI: |
| Tim Jenkinson | Professor of Finance | 01/10/2000 - present |
| Howard Jones | Associate Professor of Finance | 01/02/2005 – present |
| Period when the claimed impact occurred: August 2013 - July 2020 | | |
| Is this case study continued from a case study submitted in 2014? N | | |
| 1. Summary of the impact (indicative maximum 100 words) | | |
| <p>Investment consultants (ICs) advise on GBP1,600,000,000,000 of (largely pension) assets in the UK, but until now it has been impossible for pension funds and other asset owners to judge the value of this advice. Research by Jenkinson and Jones found that recommendations of ICs are at best value-neutral and at worst value-destroying. They collaborated with the UK Financial Conduct Authority (FCA) to study ICs in detail, which resulted in an investigation by the UK Competition and Markets Authority (CMA). Subsequently, the CMA has recommended that the FCA should regulate the IC industry in the UK and ordered that ICs should present details of their past advice in a consistent and transparent format. The changes will allow pension funds to allocate assets without having to take on trust the questionable recommendations of ICs. More efficient allocation of pension assets should positively impact millions of individuals with pensions in the UK.</p> | | |
| 2. Underpinning research (indicative maximum 500 words) | | |
| <p>Investment Consultants provide a range of services, mainly to trustees of pension schemes but also to charities, endowment funds, companies, and insurance firms. A key service is the provision of advice pertaining to investment strategies, asset allocation and selection of asset managers. The scale of assets affected by their advice is huge. In 2019, it was estimated that collectively ICs advised on GBP1,600,000,000,000 of pension scheme assets in the UK and approximately USD40,000,000,000,000 of assets worldwide.</p> <p>Although the value added by their advice on asset manager selection is, given the relevant data, amenable to direct measurement, ICs do not make their past recommendations of asset managers public. Therefore, pension schemes have not been able to evaluate the track record of their advisers.</p> <p>Jenkinson and Jones produced an initial study of consultant recommendations in 2012, drawing on data from one of the largest ICs globally. The study found that, despite its claims, its recommendations did not add value. The IC which provided the data blocked publication of the research because, even though its name was not mentioned in the research, it believed that the data and analysis would allow industry participants to identify it.</p> <p>Together with co-author Martinez, then also at Saïd Business School (now at University of Connecticut Business School), Jenkinson and Jones have since published 2 papers examining ICs' recommendations and use of these recommendations by asset owners [R1, R2]. Using data</p> | | |

from Greenwich Associates, a provider of data, analytics, and insights to the financial services industry, the studies aggregated recommendations from approximately 30 ICs, including all the major ones, with a combined share of 90% of the consulting market in the largest class – US large-cap equities. The research found ICs' recommendations were at worst value destroying, and at best value neutral. These papers were published in 2 leading finance journals and **[R1]** won the 2015 Commonfund prize, which is awarded for the research paper of most relevance to institutional investors.

The research by Jenkinson and Jones raised questions about the advice and recommendations of ICs, and this led the Financial Conduct Authority (FCA) to include ICs in their Asset Management Market Study **[E2]**, and to collaborate with Jenkinson and Jones. Using a data set sourced as part of this Market Study, Jones and Jenkinson co-authored a working paper with Jose Martinez and Gordon Cookson of the FCA **[R3]**. This data set covered a range of asset classes, collected from 7 ICs (including the 3 with the UK greatest market share) by the FCA under its regulatory powers. It compared the performance of funds recommended by ICs with the marketing claims of the ICs themselves and examined whether the disclosures that consultants present to institutional investors are reliable guides to their past performance. It found that claims of value added were mostly false. This paper is currently at the 'revise and resubmit' stage with *Management Science*, a leading academic journal.

The ICs in the sample claimed on average to have achieved excess returns of 1.73% per year. However, the research showed that these claims exceed the actual performance by 1.95%. In other words, there was (again) no evidence that ICs added value for investors. The research also found that, since different ICs exaggerated their performance to varying extents, it was not even possible for pension schemes to arrive at a reliable ranking of ICs by performance. ICs' claims therefore misled pension funds as to both the absolute and relative performance of their asset manager recommendations.

The FCA's Asset Management Market Study also included an analysis of the recommendations of investment platforms (or 'fund supermarkets') for individual investors (rather than the institutional investors whom ICs advise). Research accompanying this Market Study, also co-authored by Jenkinson and Jones, and accepted for publication in a top finance journal **[R4]**, found that these recommendations add substantially more value to individual investors than ICs' recommendations to institutional investors. The comparison is instructive because it shows that ICs' failure to add value by their recommendations may reflect, not an inability to do so, but the incentives and institutional arrangements within which ICs work.

3. References to the research (indicative maximum of six references)

R1. Jenkinson, T., Jones, H., Martinez, J.V. 2016. Picking Winners? Investment Consultants' Recommendations of Fund Managers. *Journal of Finance*, 71(5): 2333-2370.

<https://doi.org/10.1111/jofi.12289> [output type: D]

R2. Jones, H., Martinez, J.V. 2017. Institutional Investor Expectations, Manager Performance, and Fund Flows. *Journal of Financial and Quantitative Analysis*, 52(6): 1-23.

<https://doi.org/10.1017/S0022109017000850> [output type: D]

R3. Cookson, G., Jenkinson, T., Jones, H., Martinez, J.V. 2019. Virtual Reality? Investment Consultants' Claims About Their Own Performance. Available at SSRN:

<http://dx.doi.org/10.2139/ssrn.3214693> [output type: U]. Currently revise and resubmit at *Management Science* [output type: D]

R4. Cookson, G., Jenkinson, T., Jones, H., Martinez, J.V. 2020. Best Buys and Own Brands: Investment Platforms' Recommendations of Mutual Funds. *The Review of Financial Studies*, hhaa057, <https://doi.org/10.1093/rfs/hhaa057> [output type: D]

Awards and Prizes

R1 won the 2015 Commonfund prize, which is awarded for the research paper of most relevance to institutional investors.

4. Details of the impact (indicative maximum 750 words)

[Text removed for publication]

UK pension funds are obliged to seek advice from ICs, and most of the GBP1,600,000,000,000 of UK assets advised on by ICs are held by pension funds. The ability of pension funds to appoint ICs based on a clear record of performance is essential to the efficient allocation of their assets. The regulatory and reporting changes resulting from Jenkinson's and Jones's research mean that pension funds will have this ability in future.

The impact occurred in two stages. First, Jenkinson's and Jones's existing research on ICs raised awareness about the quality of ICs' advice, which led to the Financial Conduct Authority (FCA) including ICs in their 2016–17 Asset Management Market Study. Awareness was raised in academic and practitioner conferences and seminars at which the research was presented and by extensive press coverage (Financial Times 22/09/2013, 29/09/2013, 10/11/2013; New York Times 30/09/2013; Forbes 1/10/2013; and The Economist 05/03/2015). The research done by Jenkinson and Jones as part of the FCA's Market Study then led to regulatory and industry changes in the asset management sector, as detailed below.

The FCA's Asset Management Market Study

The work on ICs which Jenkinson and Jones had been doing since 2012 [**R1**, **R2**] had raised awareness about the value added of ICs' advice and recommendations. The FCA approached Saïd Business School in 2015, asking Jenkinson and Jones to organise a joint University of Oxford–FCA conference on asset management as a precursor to a market study. The conference took place in October that year. Conducted under Chatham House rules and opened by Dame Helena Morrissey, it included 50 speakers, panellists, and discussants, representing asset owners, asset managers, investment consultants, regulators, and academics. [Text removed for publication]

Jenkinson and Jones helped the FCA design the analysis on ICs for the Market Study, using the same methodology that they had used in their earlier research. The interim Market Study was published in November 2016, and the final Study in April 2017. The report findings echoed those of Jenkinson and Jones' earlier research [**R1**, **R2**], stating that *'on average, consultants are not able to identify managers that offer better returns to investors', and that 'many institutional investors struggle to monitor and assess the performance of the advice they receive. There is no standardised framework to assess the quality of advice or to help investors assess whether they are achieving value for money.'* [**E2**]

Working closely with the FCA, Jones and Jenkinson co-authored the section on Investment Consultants in the FCA's Interim Asset Management Market Study in November 2016. This drew on a large sample of data, from a range of asset classes, collected from 7 ICs (including the 3 with the UK greatest market share) by the FCA under its regulatory powers. The research supported the principal finding of their earlier work and showed that across all major asset classes ICs failed on average to add value.

The Market Study recommended, pending consultation, that the IC industry be referred to the Competition and Markets Authority (CMA) for an in-depth investigation [**E1**]. Jenkinson briefed CMA in June 2017 in preparation for its investigation, specifically about the transparency of ICs' claims. The FCA formally referred the matter to CMA in September of that year, the first time it had used the then recently conferred power to refer an industry or sector to the CMA.

The CMA Investigation

Building on the research for the FCA Asset Management Market Study, Jenkinson and Jones conducted additional research with the FCA on the claims of consultants in their marketing

materials, finding these claims to be largely misleading [R3]. This research was shared with the CMA and helped to inform its investigation. The CMA's investigation used the analytical techniques designed by Jenkinson and Jones for the FCA [E3]. After an extensive consultation period, during which ICs were invited to critique the CMA's analysis, the CMA confirmed the findings of the FCA's Market Study, demonstrating a lack of value added from IC recommendations. Moreover, difficulties in accessing information about the quality of their provider of asset management services led to a lack of engagement by some pension schemes in choosing and monitoring their providers.

The CMA published its final report in December 2018, in which it recommended that ICs be required to disclose publicly the performance of any recommended asset management products to a common set of standards, and that the government broaden the regulatory scope of the FCA to encompass greater oversight of the Investment Consultancy industry [E4]. These recommendations were welcomed by the Executive Director of Strategy and Competition, FCA: *'It is essential that competition works well as these services have a significant impact on retirement outcomes of millions of pension savers.'* [E5] The FCA asked the Treasury to extend its regulatory remit to include investment consultancy services and asset allocation advice in February 2019 [E6].

In June 2019, CMA published The Investment Consultancy and Fiduciary Management Market Investigation Order 2019 [E7]. This Order required *'fiduciary managers – who make decisions on behalf of trustees – and investment consultants to provide clearer information about what their customers are getting for their money, and incentivise pension scheme trustees to shop around to make sure they are getting the best deal to suit their needs.'* [E8] In a press release announcing the Order, Chair of the investigation said: *'Millions of people rely on pension scheme trustees to invest their savings effectively... Our investigation found that many trustees lack the information needed to assess and compare investment consultants and fiduciary managers, meaning they may not be getting the best value for their members' money. By putting the requirements of our investigation into law today, we will increase competition and make sure these markets work better for UK pension beneficiaries.'* [E8]

Industry Changes

Trustees, fiduciary managers, and investment consultants were given 6 months from publication of the order (June 2019) to ensure that their practices were in line with its requirements, with the threat those found not in compliance would be taken to court by the CMA [E8].

[Text removed for publication]

5. Sources to corroborate the impact (indicative maximum of 10 references)

- E1. Supporting written statement from Acting Chief Economist, Financial Conduct Authority (FCA).
- E2. FCA Asset Management Market Study, Interim Report, November 2016 and FCA Asset Management Market Study Final Report, June 2017.
- E3. Competition and Markets Authority (2018) Working paper: Asset manager product recommendations, Investment Consultants Market Investigation, 22 March 2018.
- E4. Government Press Release – 'CMA proposes pension investment reforms.'
- E5. FCA response to the CMA's final report on its investigation of investment consultant and fiduciary management services.

E6. FT Adviser, 'FCA seems to extend powers', 26 February 2019; Money Marketing, 'FCA eyes further supervision of investment consultant sector, 27 February 2019.

E7. The Investment Consultancy and Fiduciary Management Market Investigation Order 2019.

E8. Government Press Release – 'Final step taken in CMA reform of investment consultants.'

E9. Supporting written statement from Director of IC Select.

E10. Supporting written statement from CEO, Inalytics.