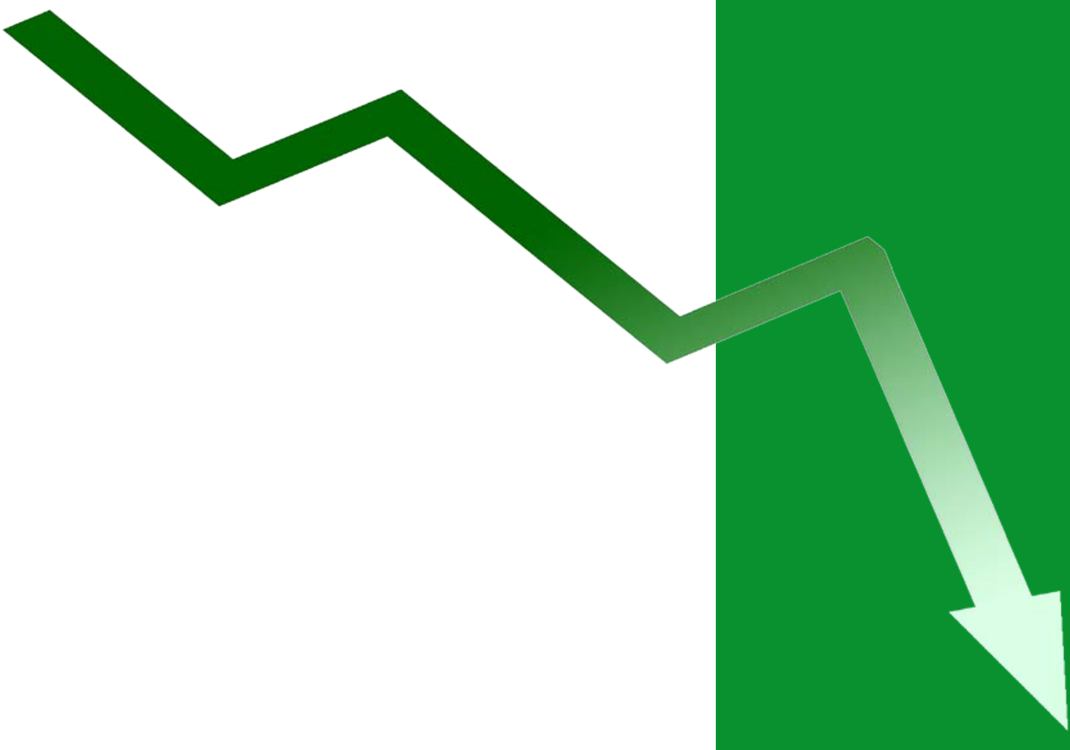
2009

The Lost Decade

A report on the past 10 years of pension fund performance



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Introduction

This report reviews the 1800 or so unit linked mainstream pension funds that are available to UK savers. It takes a ten year view, covering the period up to 31st August 2009, effectively a review of the first decade of the new millennium.

The report is a damning indictment of the state of this market, revealing a number of very striking conclusions; the main thrust of which is the management of funds in this area which has left pension savers in an invidious position. Just one figure of the many we have found demonstrates this: the combined increase in value of all pension funds over the past ten years* is a paltry 21.8%. This is very roughly 2% per year: this is the combined effort of the pension fund industry measured as a weighted return to their policy and plan holders.

Summary Conclusions

Of the £200 billion invested, about half is managed funds.

The report identifies a number of separate and interconnected conclusions:

1. There is approximately a current market value of £200 billion held in mainstream unit linked pension funds.

2. Of this nearly £170 million is in asset areas which relate to the UK; put another way 85% of all money invested is in the geographical region of the UK, demonstrating a striking lack of diversification amongst investors.

3. Of the £200 billion invested, about half is in **Managed Funds;** these funds have spectacularly failed to deliver any return comparable to any respectable measure or benchmark. The failure of these funds is absolute.

4. To evidence this, compare the average returns of the four managed fund sectors with various benchmarks:

Balanced Managed	+14%
Cautious Managed	+23%
Defensive Managed	+28%
Flexible Managed	+16%

This is the return in total over the 10 years to 31.08.2009

<u>Compare this to:</u>

Money Market Funds +40%

Or to typical portfolios** we have constructed from the funds reviewed:

Low Risk +37%
Medium Risk +30%
Higher Risk +39%

This is mismanagement to a stunning extent

Or to the average investment trust:

+92%

It should be stressed that the above is the ***average*** managed fund performance figures, many funds have produced less than the average and many sizeable funds from household names fall into this category.

Here is a random sample of half a dozen, showing their fund size and 10 year return to evidence this:

Friends Provident Managed Fund	£4.4 billion	+10.5%
Lloyds TSB Managed	£3.8 billion	+12.5%
Scottish Life Managed	£2.2 billion	+6.8%
Scottish Equitable Mixed	£6.7 billion	+8.4%
Phoenix Exempt Managed	£1.5 billion	+6.5%
Lincoln Balanced Managed	£1.2 billion	+11.5%

These six funds alone have £20 billion (about 10% of the market) in them and the weighted average return is barely 1% per year over the past ten years. This is mismanagement to a stunning extent.

5. By calculating a weighted average for the whole market we have found that the ***weighted*** total return for the £200 billion invested in these areas is 21.793% over the past ten years, which is almost precisely 2% per year.

6. However from the 30 sectors it is clear that 2 or 3 completely dominate the league tables. Asia Pacific assets produced an average return of 97%, but the only sector which produced a return of more than 100% was the Emerging Markets sector which produced 233.5%. The commodity sector would probably have produced a similar impressive return however there are no listed funds with 10 year performance.

Only about 1.5% of investors' money is in these high performing sectors

However of the £200 billion in total how much is in these sectors?

Asia Pacific £2 billion (approx)
Commodities £0.5 billion (approx)
Emerging Markets £0.7 billion (approx)

So only about 1.5% of investors money is in these high performing sectors.

7. Overall a dramatic lack of diversification is evidenced. With the UK based investments (including managed funds which typically invest in the UK) representing 85% of all assets held, investors are backing UK PLC to be the area almost solely responsible for their return. In investment terms this is nonsensical.

Overall summary

We do not suggest that a backward looking report of this nature should be seen as a blueprint for future decisions. Just because commodities and emerging markets have produced stunning results in the past ten years and most of the rest has been appalling, we don't suggest that investors should rush into these areas. What we do highlight however are a couple of points that should apply for all times: (1) Investors do not diversify enough (2) the overweighting of the UK is not conducive to a balanced, logical approach (3) the pension fund managers fail compared to virtually any other option available to investors (see "are there better ways of investing your pension?") and (4) there is a staggering mismanagement of investors money in the managed fund sector, where the only thing the companies seem to "manage" is to keep savers money below any respectable measure of return.

The weighted average performance of all funds reviewed

We wanted to get a view of the whole 30 sectors as if they were a portfolio held by the UK saver. We therefore took the average return produced by each sector over the past ten years and using the weighting of that sector's size in comparison to the whole amount of money invested we worked out **(please see page 10 for calculations)** a weighted return achieved by the pension fund industry. The result is a total return amounting to 21.793%.

We believe that this compares poorly to virtually any other option that investors could have pursued. If one compares the average Unit Trust (or OEICs), Investment Trust or ETF the returns are much higher. Cash is higher; you would have been better off sitting in cash.

Is this a typical ten year period? No, although it may not be as untypical as one may think, but what is unarguable is that whilst this has been a very difficult decade for investors generally, the managers who should be the skilled navigators for savers through these waters, have produced a devastating impact: they have made things worse. Pension fund management has failed.

Managed funds – Should they be renamed?

How can the majority of these companies continue to justify running the enormous funds they do (often measured in billions) and produce such appalling returns AND TAKE SUCH BIG FEES FOR DOING SO?

We believe that it would not be unfair to suggest that these funds should be renamed mismanaged funds. Investors have handed their money and, in effect, trust to these companies to deliver something back in return for their expertise and entrustment. What do the companies do? Charge the investor/saver for looking after the money and producing a return that the investor could get for no cost simply by sticking the money in a bank account.

Who is to blame? There is probably an argument for suggesting the investor themselves should pay more attention, demand more and be more ruthless with moving their money, there could well be an argument to suggest that advisers who leave their clients in such funds should be judged culpable, but in reality the blame for this must lie with the fund managers of these so called managed funds. We should also ask what about the bosses of these companies? What are they doing about this?

Whatever the reason, wherever the blame should or does lie, the simple fact is that this is not a snapshot, this position has lasted for years; however - such appalling relative performance used to get masked by the more positive returns achieved in former periods. After all if, for example, a managed fund produced 100% over 10 years (and there have been periods in the not too distant past when this may have been the case) and average returns were 130%, investors/savers didn't worry too much, even though the underperformance was still there, because the *absolute* performance was OK.

It is this very difficult market which exposes the true extent of the failure of these managed funds. Investors should start to get out of them at the earliest possible opportunity and find better solutions.

10 Funds that stand out – good

It's not all bad, here are 10 funds which given our review over the various periods we looked at have produced consistent and highly impressive results for investors:

Very difficult market... exposes the true extent of the failure of these funds

Barclays Life Far East Growth
AXA Retirement Distribution
Standard Life Cautious Managed
Zurich Cautious Managed
Scottish Life Defensive Managed
Skandia/Schroder US Small Cos
Friends Provident Fixed Interest
Winterthur Fixed Interest
Skandia/Invesco Perpetual High Income
Prudential/M&G Managed

10 Funds that stand out - Bad

Here are 10 funds that have been highly consistent: that is they are very bad today and have always been bad throughout the past 10 years:

Scottish Equitable Pacific
Scottish Life Managed
Scottish Equitable European
Natwest Opportunity Managed
Abbey International
Lincoln Japan
Scottish Equitable North America

Scottish Life Fixed Interest
Friends Provident European
Scottish Equitable Global

Is there a better way of investing your pension money?

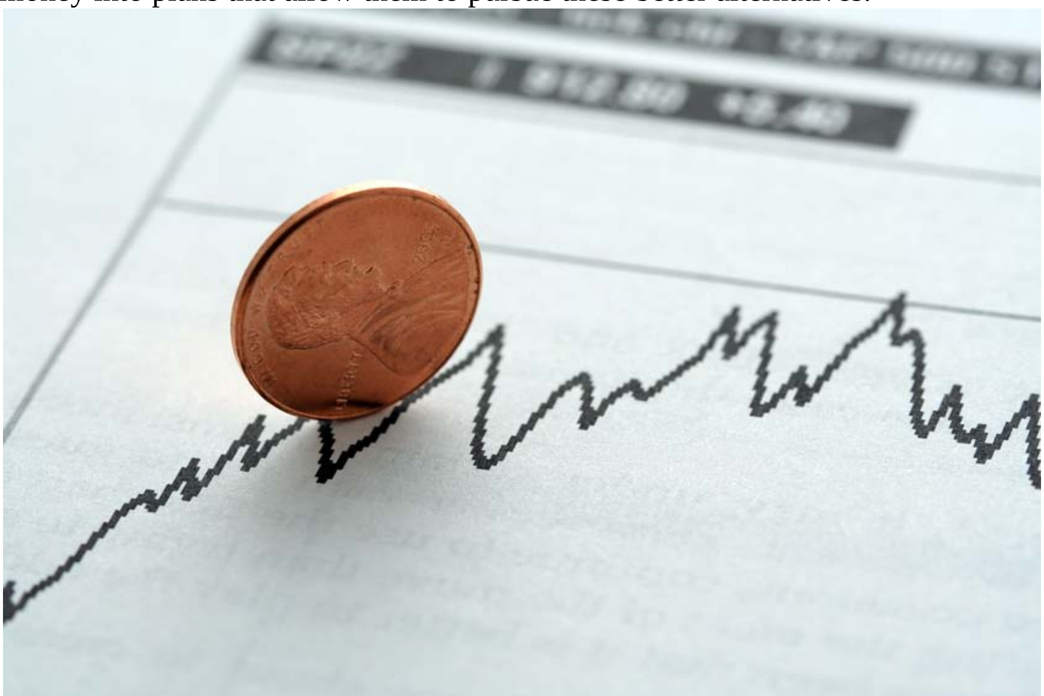
Just about any alternative strategy would be better than relying on the type of unit linked fund offered by the pension companies. One of the most worrying things about the current position is that Managed Funds are often used as “default” funds by savers, particularly those in group personal pension schemes, and it is quite clear that these funds are especially poor. Investors/savers need to find alternative homes.

Using a Self Invested Personal Pension (SIPP) offers far more choice and in the modern world these are no more expensive or exclusive than a typical pension of the sort covered by this survey.

A SIPP allows investors to use direct holdings in shares, to invest into property, into other funds types (Investment Trusts, OEICs, ETFs) and to generally get a process in place which will produce results.

Simply handing your hard earned savings over to the pension companies to place into their own funds seems to fail. Of course there are exceptions but the essence of the findings of this report and others that we have produced (for example we surveyed the whole market about 6 months ago and found that if you applied certain standard benchmarks, 86% of pension funds failed) suggest that the alternatives are almost certainly better and investors need to start taking action to help themselves by moving their money into plans that allow them to pursue these better alternatives.

Using a Self Invested Personal Pension (SIPP) offers far more choice



The retirement planning process

The problem is that investors get lumbered with these funds often through no great fault of their own. Many people hold funds because they were sold a pension by their bank or by a salesman and the whole process was inherently misguided. If the correct process is followed the chances are that the right solutions will be put in place leading to the right results.

We show the process working as follows:

You – The Saver/Investor

Find a great adviser to work with

Between you and your adviser you need to assess your current position and your future requirements

You need to assess your risk attitude and your risk tolerance

Then you put in place a written plan of action. (The plan should include: a summary of your current position, your requirements for the future, what sum you are going to save, where you are going to invest this, what return you are targeting, how often you will review your plan and how often you will rebalance your position.)

This leads onto deciding on how to allocate your assets (the asset allocation part).

And then onto which funds and fund types you will use

Your plan will build in regular future date reviews where you will view how everything is progressing and will allow changes to be made in required to correct any shortfalls in the plan

What to do to improve your position

If you find that you are concerned by your current position and want to look at improving matters then we strongly suggest that you look to kick start the process outlined above.

It's worth it! IF you were able to improve your position the difference to you at the end of the process – when you start receiving your money back – can be huge. Have a look at this example:

A 30 year old who starts with £10,000 and gets a return over 35 years of 5% (net of charges) per year will build up a retirement pot of **£55,160.**

A 30 year old who starts with £10,000 and gets a return over 35 years of 9% (net of charges) per year will build up a retirement pot of **£204,139**

It doesn't matter if you start from scratch, pay monthly, pay yearly or pay a lump sum or series of lump sums, the relative difference is always highly significant.

Getting better returns makes a huge difference to your retirement fund.

To get appropriate help and to receive a review of your position DMP Financial has a review service where you can get immediate help on your position. To get such a review arranged simply <click here> to kick start the process.

Company	Size of Sector (£billion)	Av 10 yr performance %	Ranking	Weighted performance o	
Global Emerging Markets Equities	£0.7	234	**1**	0.7 dived by 198.1 multiply by 233.5	**0.825**
Europe inc. UK	£0.1	172	**2**	0.1 dived by 198.1 multiply by 172.1	**0.087**
Asia Pacific exc. Japan	£2.2	97	**3**	2.2 divide by 198.1 multiply by 97	**1.077**
UK Property Securities	£0.1	70	**4**	0.1 dived by 198.1 multiply by 70	**0.035**
Sterling Coporate Bond	£5.8	69.2	**5**	5.8 dived by 198.1 multiply by 69.2	**2.026**
Global fixed Interest	£0.6	62.9	**6**	0.6 dived by 198.1 multiply by 62.9	**0.191**
Global Property	£0.2	57.1	**7**	57.1 dived by 198.1 multiply by 0.2	**0.058**
Sterling High Yield	£0.3	54.5	**8**	0.3 dived by 198.1 multiply by 54.5	**0.083**
UK Gilt	£3.3	53.5	**9**	3.3 dived by 198.1 multiply by 53.5	**0.891**
UK Index	£2.3	50.9	**10**	2.3 dived by 198.1 multiply by 50.9	**0.591**
Sterling Long Bond	£2.3	49.4	**11**	2.3 dived by 198.1 multiply by 49.4	**0.574**
UK Smaller Companies	£0.4	48	**12**	0.4 dived by 198.1 multiply by 48	**0.097**
Sterling Fixed Interest	£5.4	48	**12**	5.4 dived by 198.1 multiply by 48	**1.308**
Money Market	£15.0	39.6	**13**	15 dived by 198.1 multiply by 539.6	**2.998**
Sterling Other Fixed Interest	£0.4	39.3	**14**	0.4 dived by 198.1 multiply by 39.3	**0.079**
UK Direct Property	£10.8	38.9	**15**	10.8 dived by 198.1 multiply by 38.9	**2.121**
Asia Pacific inc. Japan	£1.1	38	**16**	1.1 dived by 198.1 multiply by 38	**0.211**
Europe exc. UK	£2.5	33.2	**17**	2.5 dived by 198.1 multiply by 33.2	**0.419**
UK Equity Income	£2.7	32.6	**18**	2.7 dived by 198.1 multiply by 32.6	**0.444**
Defensive (up to 35% equity) managed	£1.9	27.9	**19**	1.9 dived by 198.1 multiply by 27.9	**0.268**
Cautious (up to 60% equity) managed	£9.0	23	**20**	9 dived by 198.1 multiply by 23	**1.045**
Flexible (up to 100% equity)	£13.6	15.9	**21**	13.6 dived by 198.1 multiply by 15.9	**1.092**
Balanced (up to 85% Equities) managed	£69.5	14	**22**	69.5 dived by 198.1 multiply by 314	**4.912**
Global Equities	£9.0	5	**23**	9 dived by 198.1 multiply by 5	**0.227**
Protected/Guaranteed	£0.7	4.2	**24**	0.7 dived by 198.1 multiply by 4.2	**0.015**
UK All Companies	£31.0	4.2	**24**	31 dived by 198.1 multiply by 4.2	**0.657**
Specialist	£2.0	0	**25**	2 dived by 198.1 multiply by 0	**0.000**
US Equities	£3.5	-22	**26**	3.5 dived by 198.1 multiply by -22	**-0.389**
Japan Equities	£1.2	-24.4	**27**	1.2 dived by 198.1 multiply by -24.4	**-0.148**
Commodity (Energy)	£0.5		**28**	0.5 dived by 198.1 multiply by 0	**0.000**
Total size of sectors	**£198.1**				**21.794**
					2% p.a.

About www.howmuchdoineedtoretire.co.uk

The web site aims to cover off all the issues which exist in getting you from wherever you are today into retirement. The fact is that this is a subject of immense importance to all of us, to the economy and to society. At an individual level, with better information and guidance, the retirement planning process can be both enjoyable and successful. We aim, through the site, to provide information and guidance which provides a clear explanation of the subject and also how anyone can tackle the requirements of getting into retirement with a process and plan which works.

About

DMP Financial Ltd is a company which runs web sites on a range of financial matters from with-profits to pensions, investments to tax and includes coverage of long term care planning, fund management and the processes involved in getting the best, high quality help and advice. The company operates to the by-line: money information, money education and money inspiration. Our objective is to help consumers better understand all these subject matters and then provide a way forward in tackling them successfully.

Appendix: Research method and details

In reviewing the past decade performance we have sourced our information from the leading fund management performance league tables produced by Morningstar. We have used the ABI sectors, the common industry standard for dividing funds into sectors. We have cross referenced performance results against other industry providers. All figures are assessed as at 31st August 2009. We have also taken a check point, to avoid anomalies thrown up by the timing of the survey, at 2006 and 2003: in other words we looked back to the results at these points to see if there was any great variance in the conclusions we have drawn today, at these points in time.

*The weighted average figures have been calculated by taking the total amount in the funds and dividing the amount in each sector into this figure and then multiplying the performance of that sector to give a sector figure. We then added up the total of all these figures to produce the weighted average for the total of the funds reviewed.

**The typical portfolios we constructed were based on the following asset/sector breakdown in each case:

<u>Low Risk Portfolio</u>
20% Cash; 20% UK Gilt; 10% UK Property; 10% UK Corporate Bond; 10% Overseas Fixed Interest; 10% UK Equity Income; 10% UK All Companies; and 10% US Equities.

<u>Medium Risk Portfolio</u>
10% Cash; 10% UK Gilt; 20% UK Property; 10% UK Corporate Bond; 10% Overseas Fixed Interest; 20% UK Equity Income; 10% UK All Companies; and 10% Global Equities.

<u>High Risk Portfolio</u>
15% UK Index Linked Gilts; 15% UK Property; 10% UK All Companies; 10% UK Smaller Companies; 10% US Equities; 10% Japan Equities; 10% Global Property; 5% Global Emerging Markets; 10% Europe (ex. UK) Equities; and 5% Asia Pacific (ex. Japan).