

Facing up to the changes

The latest *Global Pensions* conjecture debate looked at what the future holds for transition management

The latest *Global Pensions* debate on transition management looks at the evolution of the transition management industry through the global financial crisis.

Discussion topics include the key issues affecting equity and fixed income transitions, the changing roles of transition managers, and the industry's struggle to develop a common set of performance measurements.

The latest Conjecture debate, hosted by *Global Pensions* editor Raquel Pichardo-Allison, includes ConvergeEx Group managing director Sam Lundqvist, Citi Group head of US transition management sales Sarah Kirschbaum, Northern Trust head of transition management for EMEA and APAC Simon Hutchinson, J.P. Morgan global head of transition management John Minderides and head of EMEA transition management at Russell Investments Chris Adolph.



Raquel Pichardo-Allison

Raquel Pichardo-Allison: What have been some of the key issues in transitioning assets through the financial crisis?

Chris Adolph: I think one of the key issues we have all faced, be it equities or fixed income, have been significant increases in volatility.

But it has also meant, particularly on the fixed income side, spreads have been significantly wider. Certainly one of the things we have had to face is making sure we are communicating well with the clients that a transition might not have only cost them 20 or 30 basis points, it could be double or even more than that.

Sam Lundqvist: For a while there in the height of the crisis, the FTSE was moving around 150 basis points every hour. You need to be exposed to the right asset class. If you are going from UK equities to UK equities, don't sit on cash. And that could easily happen if you don't manage it correctly. That was especially pointed during that volatility when if you sat on cash for just an hour, you could miss out on a percent or two.

Now, clients make the move to a new manager based on the assumption that they are going to get better alpha, say half a percent, a percent a year. Just by sitting in cash for a single hour, you could erase that, or you could be behind that alpha target for a couple of years.

Sarah Kirschbaum: I think increased transparency in everyone's platforms, increased transparency in terms of spills, [and] a bit of increased transparency in the fixed income market has really been the major development over

the last few years. That has led to a lot more trust between transition managers and clients.

Raquel Pichardo-Allison: Is there a need for transition managers to act more like asset managers?

Sam Lundqvist: I think there is a sell side and a buy side model. The lines are starting to blur more and more. Interim asset management, temporary asset management, is something that has been around for some time. Most transitions are still very, very short term in nature.

John Minderides: I don't think the distinction is just about time here. A longer transition doesn't necessarily make it a fund management mandate.

As a transition manager you are there to manage a market neutral event, and control risk. You are not there to add alpha. That is the distinction, it is about what discretion a fund manager is using to add alpha.

Raquel Pichardo-Allison: How does a pension fund know which type of manager is right for them?

Sam Lundqvist: That is a tough question. There has been a blurring between the buy side and the sell side. So the buy side for example now ... trade directly in the market, on their own, they don't necessarily have to go through the sell side the way it used to be done.

On the other hand, the sell side are now using investment management type tools, risk systems, etc.

John Minderides: It has become very

blurred... I think there is still one main difference though and that is that the buy side still believe, incorrectly, that they are selling themselves with an advantage over the sell side. They think they have a value proposition which is better than the sell side which I disagree with, they have actually got their own inherent problems, such as transparency.

Simon Hutchinson: I would ask about what level of transparency you think is the -?

John Minderides: Well it is less than is portrayed by the buy side.

Simon Hutchinson: Which bits?

John Minderides: Around where commissions are paid, and who is receiving them.

Simon Hutchinson: I would disagree, I think from our perspective, what is disclosed in legal agreements and all the other conversations with the client, the transparency a client gets is very, very high with an asset manager provider.

Sarah Kirschbaum: I think that the development of fiduciary capability for the sell side is a large step in the direction that has allowed clients to become more comfortable with both the buy side and the sell side approach.

Raquel Pichardo-Allison: How do you measure performance and is there ever going to come a point when we just have one uniform performance measurement?

Sam Lundqvist: There are really two parts to that question. I think we do have an agreed upon measurement for transition performance, the T-standard implementation shortfall. Most parties would agree that is probably the best way to measure transition performance.

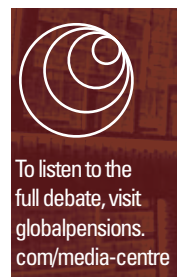
How that is attributed is up to a discussion between the transition manager and the provider. Because again, each event is different, there are different risks associated with it and a



Chris Adolph



Simon Hutchinson



number won't tell you whether it was a good or a bad event. So agreement on how it should be measured, yes. The attribution? I just wonder whether that can actually be finalised and agreed upon by everybody.

John Minderides: The good thing about implementation shortfall is it is a completely objective measure. And it doesn't matter what business model – sell side, buy side – that is irrelevant.

The issue of different events and how you compare one event with another is a difficult one. But I don't think it is actually quite as difficult as we all like to make out, because there is definitely increasing commonality of expectation of implementation shortfall cost outcome. The numbers are getting closer together, the understanding of the variance in those numbers is getting better.

Raquel Pichardo-Allison: There is going to be an industry group put together to see how we can adapt the [GIPS] standards to transition management. Can you take something as concrete as the GIPS standard and apply that to transition management?

John Minderides: GIPS is a process as much as it is a number. And I think a process can be created. Will it look just like GIPS for fund management? No. But will it be something that adds value to clients? Absolutely.

Raquel Pichardo-Allison: What are some of the next steps with regards to the T-Charter?

Simon Hutchinson: You may have more questions about GIPS and about the standardisation. I think that is probably where it will go more than anything else.

Chris Adolph: One of the things that it's important to note is that at the moment, you have got a lot of transition managers effectively who agreed upon this code of best practice. At the end of the day, we all believe we deliver the product for our clients that they want and in the best way



Sarah Kirschbaum

we possibly can. One thing that obviously would help is if there was more industry feedback towards us, we can only take it so far.

John Minderides: The T-Charter was difficult to put together and it set out to create a code of best practice that we all should follow. A lot of the discussion now is around improvements around the actual measurement side of what the T-Charter should represent in terms of a code of best practice.

However, it isn't actually working in a total sense. And to give an example, I lost a transition to competitors who bid zero commission. By definition, anyone that is bidding zero commission is not complying with the T-Charter. So there are still people out there who signed up to the T-Charter who are not complying with it.

Chris Adolph: John makes a very good point. The whole transparency issue is very, very, very important. In the end of the day, if someone is saying it is going to cost you nothing, well, it is not going to cost you nothing.

Raquel Pichardo-Allison: If you are looking ahead 10 or 15 years down the road, what are some of the major differences that you expect to see from the transition management industry.

Chris Adolph: You will see the transition managers a lot more integrated with their clients. You will be developing deeper relationships. It will become more of an asset management exercise, of which transition management is just one of the tools that you use.

Simon Hutchinson: The industry may go more in this route of a bigger split between the buy and sell side in terms of the buy side may go down more the route of asset management, and the add-ons to the asset management side.

Sam Lundqvist: I think integration with clients, whether you are sell side or buy side, is going to be a staple going forward. Transition managers will need to continue to be on the leading edge of all these new financial products that are

going to come in. Because you can't have one of your favourite clients come to you and say, 'Can you help me with this'? And you say, 'I can transition 80% but the other 20%, I can't'. They are going to say, 'Thank you very much, I am going to go to the next provider'.

Sarah Kirschbaum: I think it will be very technology driven. The markets themselves are becoming more driven by technology and less driven by human intervention. So I think that transition management will become more integrated into clients' automatic processes, that their systems will talk directly to the systems that they have chosen for transition management, much like their custody and asset management systems do now. I think that we will see a lot more direct connectivity. I think that little by little [we] will continue to drop out of the process.

However that being said, I think transition management will always rely on a certain amount of human coordination because there are so many parties involved that will not just be able to automatically link to each other.

John Minderides: Looking 10, 15 years ahead is quite difficult and I can't even remember 10, 15 years in the past. We could see some very different structures and I think it is very dependent on what happens to the pension fund industry. It is very difficult to say what a transition manager is doing servicing that industry when that industry could go through some massive changes.

I do agree with Sarah to a large extent that I see us actually moving towards the possibility that transition managers aren't actually needed. And one of the things there is if you do move to more pooled fund structures, or if you do move towards assets that are managed around alpha liability solvency type of relationships, the actual acquiring of assets could take a very different look to what we do now. It won't be about buying and selling assets in the market, it will be quite different. So in 15 years time, maybe transition management doesn't exist. ■



Sam Lundqvist



John Minderides