The UK Fund Management Pricing Cartel

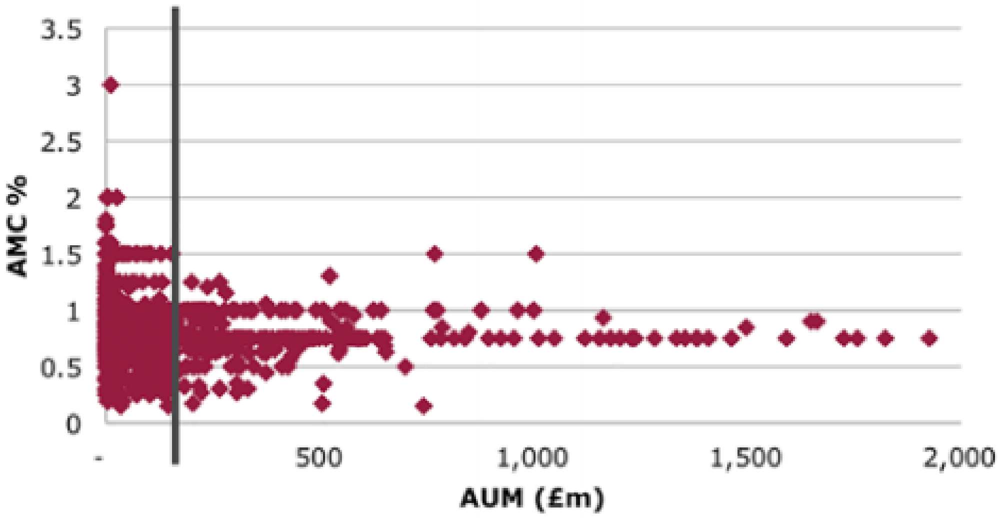
- **New research finds 70% by number and 73% by value of actively managed equity funds charge an identical Annual Management Charge (AMC) of 0.75%; indicating no genuine price competition.**

- **SCM Direct believes their findings are proof of anti-competitive behaviour within the UK active fund management industry, and the regulator should investigate to determine whether some form of price collusion, whether formally or informally, is being undertaken by major fund groups.**

- **This is not only to the detriment of UK investors, but also contravenes the FCA's 'Treating Customers Fairly' principle.**

Recently, the FCA highlighted in its excellent Asset Management Study that '*there is considerable clustering of prices for active equity funds at both 1% and 0.75% for clean share classes (those that do not include distribution payments*).' As the FCA own chart within this report[1], illustrates, the fee received by the fund manager themselves – the AMC - seems similar across the retail class of funds:

Figure 6.15: The distribution of AMC against AUM for equity share classes



Source: AMC data from a sample of asset managers enriched with information from Morningstar Direct. AUM data from Morningstar Direct.

[1] https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf

When you consider that these fund groups hire teams of analysts and expert fund managers who all claim to have a unique investment strategy that can produce better investment returns than their competitors, the price clustering does not reflect this. Different products, with different 'ingredients' and vastly different track records should command different pricing. Whether the fund is run by 2 or 20 people, be managing £200m or £2,000m, have a brilliant or disastrous track record, the price directly charged by active retail fund managers does not seem to change.

Of course, the heavily conflicted Investment Association, recently attempted to deny this price clustering in its amateurish response[2] to the FCA report by looking at the clustering of the charge (OCF) that includes variable third party charges; rather than address the issue of the fixed AMC which its own members directly receive.

This new research from SCM Direct finds that the real price clustering is much worse than even the recent FCA report evidenced.

SCM Direct Research

SCM Direct analysed the non-index or tracker clean share classes of UK equity funds available on five of the leading IFA platforms - Transact, Ascentric, Funds Network, Nucleus and Novia, where the AMC was available via FE Analytics and the data was up to date (31/12/2016 or later).

This provided the team with a sample of 683 funds with a combined Assets Under Management of £320.5 billion.

SCM Direct found that 70% by number of this extensive sample of funds, had an **identical** AMC of 0.75% pa (the overall average AMC was 0.76% pa). In terms of overall, assets managed the figure was slightly higher at 73% of clean chare class funds charging an **identical** AMC of 0.75% pa.

This 0.75% pa is also **identical** to the 0.75% pa AMC fee that was bundled with other charges prior to the 2012 Retail Distribution Review (RDR) which was anticipated to result in downward pressures on fund manager charges for active funds. But our findings show that this has not changed for at least five years, and the perception that AMC fees would fall is therefore completely untrue.

SCM has calculated, based on industry data[3] of £554 bn invested in retail equity funds, of which 88% is 'actively managed', had the underlying AMC reduced by just 0.1% pa, i.e. from 0.75% pa to 0.65% pa, UK savers and investors would be £488m better off every year.

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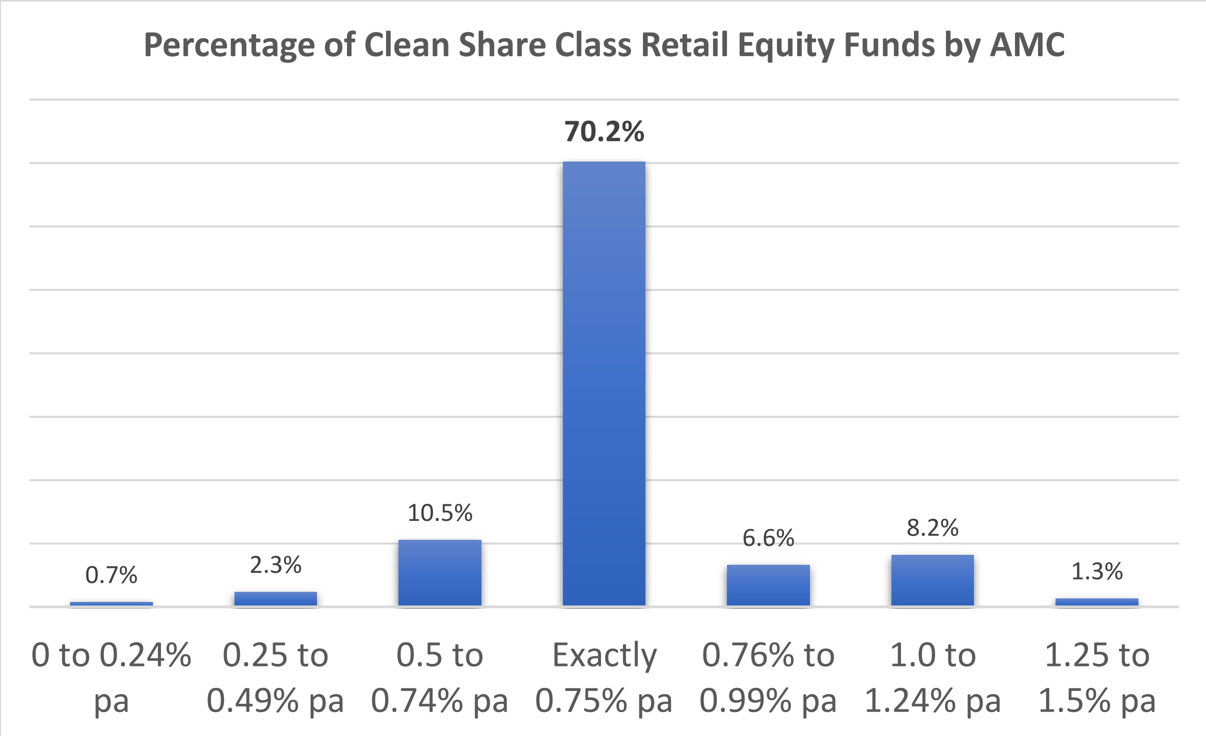
[2] http://www.theinvestmentassociation.org/assets/files/consultations/2017/IA_response_to_FCA_Market_Study_Interim_Report.pdf

[3] http://www.theinvestmentassociation.org/fund-statistics/statistics-by-sector.html?what=table&show=21



Source: SCM Direct

Further investigation into some of the most popular individual fund sectors, show that such price clustering is common place across the board:

Sector	% Found to have identical 0.75% pa AMC fees	Average AMC
UK All Companies	**67%**	0.76% pa
UK Equity Income	**75%**	0.78% pa
European Ex UK	**84%**	0.75% pa
Japan	**78%**	0.72% pa
Asia Pacific Ex Japan	**71%**	0.84% pa
Emerging Markets	**61%**	0.88% pa
North America	**84%**	0.75% pa
Global	**63%**	0.78% pa

Source: SCM Direct

The research also found evidence that the large funds do not pass on their significant economies of scale back to customers through lower prices, and are even **more** likely to charge an identical price:

Fund Size	% Found to have identical 0.75% pa AMC fees	Average AMC
Less than £100m	**66%**	0.77% pa
£100m to £500m	**72%**	0.76% pa
Over £500m to £1,000m	**72%**	0.74% pa
Over £1,000m	**78%**	0.78% pa

Source: SCM Direct

As warren Buffet's latest Investment Letter[4] states:

*'The bottom line: When trillions of dollars are managed by Wall Streeters charging high fees, it will usually be the managers who reap outsized profits, not the clients. Both large and small investors should stick with low-cost index funds…. **When a person with money meets a person with experience, the one with experience ends up with the money and the one with money leaves with experience**."*

Agreements between competitors to fix prices is regarded as one of the most flagrant breaches of competition law. When the merger occurred in April 2014 of the UK Office of Fair Trading and the Competition Commission, to form the new Competition and Markets Authority (CMA), investors in the UK might rightly have expected robust enforcement of competition rules, but this does not appear to be the case in the fund management industry, based on SCM's research findings.

It is surely time for both the FCA and the CMA to investigate price fixing in UK retail actively managed investment funds?

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[4] http://www.berkshirehathaway.com/letters/2016ltr.pdf