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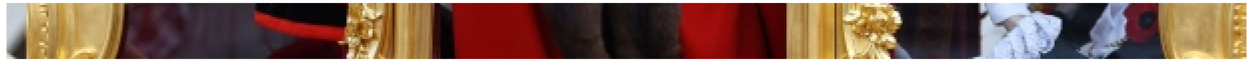
Lord Mayor Hits Back at Criticism Over £50 Billion Growth Fund

Katherine Griffiths and Loukia Gyftopoulou, Bloomberg News



Nicholas Lyons, Lord Mayor of the City of London. Photographer: Hollie Adams/Getty Images , Photographer: Hollie Adams/Getty Images

(Bloomberg) -- Nicholas Lyons, the Lord Mayor of London and a veteran financier, has hit back against industry criticism of his plan for a £50 billion ($62 billion) fund to boost investment in UK growth companies.

The opposition is "from people with a vested interest in trying to prevent modernization of our pension schemes," Lyons said in an interview. Opponents are "throwing up a smoke screen," in focusing on his idea that fund managers could be compelled to hand over a small slice of their policyholders' money to the fund, he added.

Normally, Lord Mayors — a title that has existed for 800 years — are known for waving to crowds from a golden coach and hosting dinners at the ornate Mansion House. In contrast, Lyons may be remembered for stirring a bitter row at the heart of the City of London.

The Lord Mayor — a former banker on sabbatical from the UK's biggest pensions provider, Phoenix Group Holdings Plc — has taken on his one-year role just as politicians from both main parties are crying out for ways to revitalize the UK's capital markets and restore the country's vim following Brexit.

Lyons' idea, set out in March, is for a £50 billion "Future Growth Fund", with the aim of revitalizing the UK's capital markets and helping pensioners. To ensure its success, Lyons suggested the government could force funds to invest 5% of the money they are safeguarding, or at least require them to explain why they won't.

That has gone down badly with many in the investment world. Their main concern is that any mandate to invest in a government-directed fund would clash with a duty to act in the best interests of clients.

More quietly, the industry is also concerned about losing fee income if money is forcibly moved to a new fund, the manager of which is still unknown. Some are furious with Lyons' blueprint and are working to ensure politicians and officials don't run with it, according to people briefed on the matter.

Lyons Den

For Lyons, the situation is uncomfortable given his opponents are industry peers. "These ad hominem assaults suggest that we are hitting a few nerves," he said.

Lyons says he would prefer fund managers to voluntarily agree to plans for a bold new approach to investment in areas ranging from start-ups to infrastructure rather than them being compelled. He also acknowledges that some have spent money setting up businesses to attract new pensions money. "Why should they give that up? I'm not saying they should," he said.

His fund could be just one of many, Lyons added. “There could be £20 billion in a Future Growth Fund, and £30 billion in other competing programs.”

Lyons is not alone in wanting to shake up the sector from within. Nigel Wilson, outgoing chief executive officer of Legal & General Group Plc, has suggested a “nudge” in the form of tax breaks to incentivize investment in growth areas. Several industry participants are also working on a “compact” agreement to expand investment parameters, but without formal direction, people familiar with the matter said.

Concerns in the industry remain. “It’s clear politicians are keen for pension fund assets to go to the UK economy but it’s not clear what the destination is going to be,” said Nigel Peaple, director of policy and advocacy at the Pensions and Lifetime Savings Association, which represents 1,300 workplace pensions with £1.3 trillion of assets. A growth fund would be positive but trustees would want to vet the assets, he added.

Either way, there are nerves about who would take the blame for the extra risks that come with a broader investment approach. “Politicians don’t care about what happens in 10 years because they may no longer be in government,” said Daniel Pinto, chief executive officer of asset manager Stanhope Capital. However, Pinto backs bold reform, as long as managers are free to invest where they want, not just in the UK.

Political Agenda

Every decade or so, British pensions get political. Last time, David Cameron’s Conservative government tried to find as much as £20 billion from pensions to support infrastructure spending. The Pensions Infrastructure Platform withered after funds could not agree on what investments to make, according to one person involved in setting it up. That experience helps to make the case for mandating investments now, the person said.

Today, the sector is touted as the way out of seven years of post-Brexit malaise and a boost for home-grown technology such as climate transition and life sciences. The UK government estimates that the pipeline of potential infrastructure projects will reach £650 billion by 2030, while projects to adapt the country to net zero climate targets alone could cost £400 billion by 2050, according to a 2022 paper by the think tank Policy Exchange.

On a global level, the UK is competing with the $375 billion Inflation Reduction Act stimulus in the US and expanded green subsidies in the European Union. So boosting its spending power with £3.4 trillion of pensions savings – the second largest pot in the world after the US, Policy Exchange said — is politically tempting.

Jeremy Hunt, the chancellor, may announce pensions changes when he speaks at the Mansion House in July alongside an update on his Edinburgh Reforms which cover broader financial services changes, according to several people involved in talks over the matter.

The opposition Labour party has expressed interest in a growth fund and says it is open to mandating contributions. The party's manifesto for the 2024 election could also draw on suggestions from the Tony Blair Institute — a nonprofit set up by its former leader — to consolidate private and public pensions to create "GB superfunds" with assets of as much as £500 billion.

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Divisions and reversals are common in pensions policy, said Steve Webb, a former pensions minister in Cameron's government and now a partner at actuary Lane Clark & Peacock. Government departments have long been conflicted about whether to push for superfunds to consolidate pensions. "Half wants to but another half does not," Webb said.

Supporters of this idea say there's scope to pool nearly 100 pension programs run by local governments to create a sovereign wealth fund. Among them is Tracy Blackwell, CEO of Pension Insurance Corporation, which specialises in taking over pension programs from companies. Local authorities have their own funds — instead of paying retirees from taxes, like the central government pension — so could be more easily restructured, she said.

A consolidated version of the Local Government Pension Scheme would create "a £400 billion fund which, due to economies of scale, would save local taxpayers £1 billion a year," Blackwell said.

Change Needed

Almost everyone acknowledges change is needed. UK pension funds are forced by rules designed to protect retirement funding to skew their portfolios away from the stock market and into bonds.

As well as draining money out of equities, this trend has created new problems, leaving funds exposed to the spike in interest rates over the past year and a seizure in the gilt markets in the wake of Liz Truss's ill-fated budget. This incident also highlighted the risks of less liquid assets that must be repriced daily, even when they won't be sold for years or even decades.

In the next few years, "there are substantial unrealized losses in the bonds part of the portfolio that will work their way through," Lyons warned.

According to think tank New Financial, 53% of pension funds' total assets were invested in UK stocks in 1997, falling to 6% in 2021. British pension funds and insurance companies now own just 4% of the stock market, down from 39% in 2000.

"It is a no brainer" for pensions to be invested in a wider range of assets, said Ros Altmann, a former pensions minister and now a member of the House of Lords. "Unless capitalism breaks down, equities perform better than bonds over long term. So the change would mean better investment returns while also creating a pool of assets that will support the economy."

Many Challenges

Reformers point to Canada and Australia as shining examples of large pension pools that invest effectively in a wide range of assets. Their portfolios often include the UK, where overseas pensions invest 16 times more in British venture capital and private equity than domestic public and private pensions do, the Tony Blair Institute found.

A few big UK pension funds do invest in infrastructure, such as the largest private pension pot, the Universities Superannuation Scheme. But many avoid it due to the complexity, according to Colin Smith, head of the infrastructure deals team at professional services firm PwC. The assets can be "mission and safety critical and can attract public criticism," Smith said.

Highlighting the difficulties, Nest — set up by the government to offer workplace pensions as part of its push for auto-enrollment — won't invest in nuclear projects such as Sizewell C in Suffolk. Nest's fund managers "would need to be confident it offers a good investment opportunity," a spokesman told The Times last month.

For smaller funds, being able to allocate some money to a pooled fund could help access more complex investment, according to Lyons and others. Meanwhile, defined benefit pensions — which promised fixed payouts in retirement — could take greater risks if they could buy a form of insurance against default, potentially expanding the role of the Pension Protection Fund that rescues failing funds, Webb argues.

The regulators will also need to play a part. Plans to loosen Solvency II rules, which were set when the UK was inside the European Union to police insurers' balance sheets, are underway after a prolonged battle between the Prudential Regulation Authority and the industry. The final details will be key to the opening up of pensions investment, with insurers saying they may be able to invest £100 billion in productive assets over a decade if some restrictions are lifted.

New Deal

The broader question is whether the UK wants to tie its vast pensions wealth to wider society, or leave people's savings alone. "At least 25% of everybody's pension fund is from tax relief. Why not use that for social good?" Altmann said.

At the same time, people are set to be poorer in old age. Just 8% of those in defined contribution pensions — where payouts are based on investment performance — are expected to have enough for a comfortable old age, Webb said.

Lyons will move out of the Mansion House in November and go back to his day job as chairman of Phoenix. What if the current pensions fracas dies down without action?

He says it would be a "terrible missed opportunity."

--With assistance from Julius Domoney.