Key Dynamics: A market overview

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*Alternatives, ESG adoption and further fund consolidation are the key trends highlighted by IND*EFI

Key points

- The Dutch pension market sets the tone across Europe
- The role of the fiduciary manager is being redefined
- Exposure to private assets is continuing to increase
- Virtually all Dutch pension funds have adopted ESG practices

The Netherlands has long been considered a cornerstone of the institutional asset management market in Europe. With assets under management totalling €1.8trn and a steady annual growth rate exceeding 6% over the past five years, it is one of Europe's leading asset management markets. It is heavily skewed towards the pension segment (€1.4tn), where defined benefit (DB) pension plans make up about 80% of total assets and have enjoyed a dynamic annual growth of nearly 10% – a figure predominantly driven by industry-wide pension funds.

Not only is the Dutch pension market one of the largest in Europe, it also often sets the tone with regards to regulatory reforms, emerging trends in outsourcing and the adoption of ESG investing. The Dutch experience continues to hold lessons for the future and sheds light on similar trends throughout other markets.

Consolidation of pension funds

Like most of its European counterparts, the Dutch pension market has been riding the wave of consolidation. The number of funds has dropped from 514 in 2010 to 233 today. Driven by a complex regulatory environment, the market is expected to shrink further to under 150 funds. Active players in this consolidation include not only pension funds themselves, but also newly-minted APFs (general pension funds), which provide a platform for new players. Alongside pension funds, both insurance companies and fiduciary managers are leveraging on these vehicles to break into the market, betting on the growth of defined contribution (DC) to open opportunities as the market rebalances.

Ric van Weelden

Pensions funds empowered
Parliamentary debates around the role of fiduciary managers have seen observers predict the demise of fiduciary management. Although this conclusion has turned out to be premature, the role of the fiduciary manager is being redefined as pension boards are urged to claim their rightful place at the centre of investment decisions. Both fiduciary managers and pension funds have protested this move, the former asserting it will undermine their ability to effectively implement their advice, the latter fearing the scarcity of necessary resources at board level.

Redefinining fiduciary duties
Caught between increasing regulatory pressure to separate advice from implementation, on one end, and lower fees on the other, fiduciary managers have had to adapt their business models. The departure of a few international players from the sector was interpreted as the death throes of a market stifled by razor-thin margins failing to compensate for the associated risk, the omnipresence of passive investing and burdensome regulation. Our research shows that this is not true. The recent retreat of pension-affiliated fiduciary managers has left a space open for grabs. Only a dozen significant players are left within a growing, albeit precarious market.

Christel Tarneaud

As INDEFI research outlines, successful fiduciary managers have gone down one of two routes towards designing a sustainable model for their business:

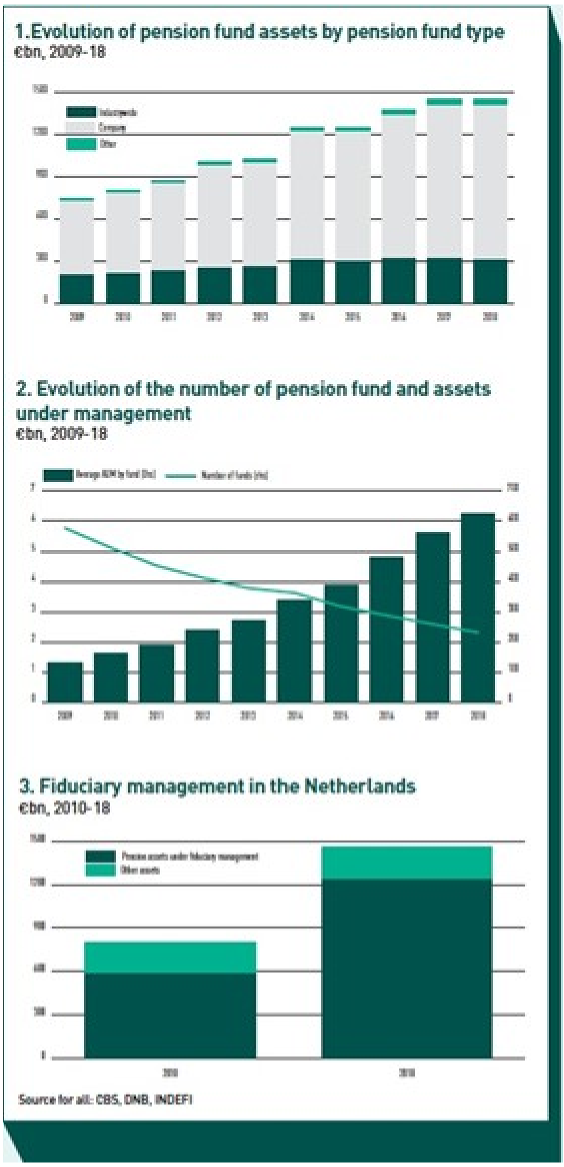
● Fiduciary management as a platform, fostering economies of scale by leveraging a 'one-size-fits-all' fiduciary service, which pension funds can marginally tweak to adapt to their specific requirements;

● Fiduciary management as a range of services (from pension administration to investment advice), managing each service as its own profit centre by scrupulously monitoring the associated costs.

The model chosen has significant implications in terms of governance and asset allocations, which in turn affects the way they should be addressed by third-party asset managers.

The adoption of ESG and SDGs
Driven by increasingly vocal investor demand and the example of their larger counterparts, virtually all Dutch pension funds have adopted ESG practices. VBDO, the Dutch Association of Investors for Sustainable Development, forms a powerful pressure group whose annual ranking of ESG-compliant pension funds has provided an incentive for players to promote their achievements. Initially limited to active asset classes, ESG application is rapidly being mainstreamed in a conscious effort by pension funds to act upon the awareness of the long-term nature of their liabilities.

The dominant trend from active to passive management, which has been apparent since the turn of the century, appears to have peaked.



Several large funds have already implemented concentrated, long-term active investment approaches in line with a more long-term risk / return approach. It remains to be seen whether ESG will play into the hands of active asset managers, leveraging investment strategies supporting impact and the UN Sustainable Development Goals (SDGs). Alternatively, smart beta and ESG-driven factor investing could prevail as tomorrow’s reference framework.

Private assets remain popular
Nowhere is the tension between enhanced oversight from the pension board and optimal investment management clearer than in allocations to alternative assets. Exposure to private assets, currently at about 10%, will continue to rise, possibly to as high as 25%, driven by a growing demand for mortgages, direct lending, infrastructure debt and private equity.

This trend masks a growing market polarisation, with larger funds hoarding an ever-greater share of private assets under management. Their affiliated fiduciary managers, looking at the large Canadian and American funds as an example, tend to favour in-house investments or co-investment programmes, strengthening their private asset in-house teams and seeking out arrangements with like-minded investors.

On the other hand, smaller pension funds are withdrawing from an asset class often considered too complex for their board members. This retreat should prove transitory, as the sustained need for return (illiquidity premia) should spur asset managers to step up their game to address a growing need for support and education.

The opportunity ahead
The polarisation of the outsourced opportunity, the gradual dispersion of passive into smart beta and ESG-driven factor investing, and the continued push towards a diverse range of private asset classes, make for a vibrant, albeit challenging, opportunity for third-party asset managers. At the forefront of the trends gradually reshaping its neighbouring counterparts, the Dutch institutional market provides, in many ways, a blueprint for the future of European institutional outsourcing.

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