



## **COMPANIES: UK: The costly art of selling pups to the people: Dysfunctional folk in charge**

By John Plender  
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The statistic of the month comes from Ned Cazalet, the independent analyst who persists in talking sense about life assurance.

The UK life sector's spending on overall administration and new business acquisition in 2002 was, he says, a staggering £12bn, equivalent to an absurd £570 for every household in the land. Some £7bn of that sum was spent on acquiring new business.

Mr Cazalet's conclusion is that an industry that spends more than £300 per household a year on seeking new business is "operationally dysfunctional".

Too right. Anyone who holds a with-profits policy has been providing a social security system for the sales people. They have also bought into an industry where pro-cyclical regulation encourages insurers to buy when securities are expensive and sell when they are cheap. That has been the story since the equity market peaked in March 2000. With solvency under pressure, the life sector's fund managers reduced their exposure to equities when the market was down and plunged into gilts bang on time for this year's gilt market slide.

The marketing men are clearly on top in the UK, just as they are in the scandal-prone mutual fund business in the US. There, mutual fund company revenues grew at a real rate of 20 per cent a year in the 1990s. But as John Bogle, the founder and former chairman of the Vanguard Group has pointed out, equity fund expense ratios kept rising despite the enormous economies of scale in the industry.

Costs are now running at three per cent a year. So, while the S&P500 index showed a 12 per cent annual return between 1984 and 2002, mutual funds managed a return of little more than nine per cent. And since most investors joined the party at the peak - when they were encouraged to buy bubble-inflated tech funds - the average fund shareholder earned only 2.6 per cent. They would, says Mr Bogle, have been better off leaving money in the bank.

Coincidentally, the London-based Tomorrow's Company think-tank has published results from its inquiry under Sir Richard Sykes, former chairman of GlaxoSmithKline, into the UK investment system. Among other things, Sir Richard wants greater transparency to promote trust and confidence. And he wants long-term profitability to be achieved by putting the needs of the consumer at the heart of the system. This, he says, will take concerted leadership from the financial and corporate sectors. The snag is that such leadership as there is in the savings and investment business exists chiefly in the marketing departments and works against the consumer interest. Getting from here to there will be an extended marathon.