

Review of Westminster City Council

Custodian and Foreign Exchange Benchmarking Reports

May 2015

Summary

Amaces is a specialist custodian benchmarking firm formed in 2002 providing detailed analysis of the operating performance and financial impact of the services provided by Global Custodians. Our client base is primarily UK pension schemes (local authority and corporate) and investment managers. We are however expanding in to the US and European markets and well represented with new clients in both regions. We have around 90 clients subscribing to our custody and treasury module and over 40 clients subscribing to foreign exchange, although we do in fact benchmark more than 140 different counterparties. Whilst we have developed good relationships with the custodian banks we do not undertake and work for them, preferring to retain our unbiased independence.

The relationship with Westminster City Council goes back to late 2009 and during the time we have provided the Council with monthly reports and analysis and in addition fee reviews and advice when required. We currently charge the scheme £10,000 p.a. for each report having reduced from £12,000 p.a. at the end of 2012. We have looked at the latest reports for the end of March 2015 and our review of each report follows.

Custody and Treasury update

We have paid close scrutiny to the results since the transition to Northern Trust as compared to the performance of The Bank of New York Mellon. Our comparisons are against; other clients of Northern Trust; UK peer group of pension schemes; total universe of 90 clients. The high level analysis will place Westminster in either the top middle or bottom category denoted by traffic light status Green, Amber and Red.

- Late Settlements – not really under the control of the custodian but more affected by the activities of the underlying manager and respective broker. Experience is generally acceptable at Amber (middle third) across all comparison groups, with a slight increase at the time of the transition of assets to Northern Trust. Volumes and values have trailed off over the last few years as Westminster moved more in to pooled funds.
- Income collection – Generally has been good with one poor month in September 2014 under BNYM and some late items again around transition time. Under Northern Trust the experience is in the top third (green).
- Tax Reclaims – Both banks have done a decent job with this service and Westminster is in the top third in terms of service.
- Voting – some voting has been missed by managers over the course of the last 12 months placing the service in the bottom third (red) but realistically the figures are skewed by very

few voting opportunities. As Westminster have moved in to pooled funds voting becomes less relevant.

- Accounting – both Banks have done a decent job in reconciling the end of month reports back to the managers and have met the stated deadline 11 months of the year.
- Foreign Exchange – In custody we measure small trades under \$200,000 which is seen as income repatriation and not to be confused with trading activity. The volumes have all but dried up with only 6 trades over the last year so any analysis is not realistically comparable.
- Interest conditions – we flagged to Westminster that after the transition no earnings were being made on cash balances, with sterling the major currency. This has now been rectified and interest is being earned since January on GBP cash balances at a rate better than the average for our other clients. Balances in Euros and Dollars are tiny and returns irrelevant. No significant overdrafts have been experienced over the last year.

In summary the new relationship with Northern Trust has got off to a fairly decent start bearing in mind however the low trading volumes that exist.

Foreign Exchange

Volumes over the last year have fallen from over 500 trades per annum to now around 200. The report measures the foreign exchange activity of just one manager now – Insight who will use numerous counterparties on a negotiated basis to transact foreign exchange on the back of their trading activity.

The result over the last 12 months has been excellent with Westminster experiencing rates as near to mid-market (zero bps) as possible. Westminster are therefore in very good company with some very large investment management firms who struggle to achieve the same pricing, especially when one considers the low value comparatively (US\$350 million per annum). That experience continues through all the trading activity irrespective of size. All trades are freely tradable currencies (non-restricted).

We understand that Westminster will continue to use Insight but will in time move to a pooled fund instead of segregated. It is of course in the interest of Insight to maintain the level of competitiveness in their foreign exchange activity to prevent any drag on fund performance. I would expect them to continue to trade as efficiently in the future pooled or not.

Amaces and Westminster City Council

Moving forward we have enjoyed an excellent relationship with Westminster and we would enjoy continuing the relationship but we do understand the dynamics of the relationship with the Custodian have changed as Westminster move entirely in to pooled funds.

We do have other pension scheme clients in a similar place but they continue to see value in having Amaces there not just to provide reports but also as a consultant and adviser to custodian activities.

The reports we produce however will have less value to Westminster and so we would propose changing the scope of the reporting which will be reflected in pricing.

For custody a number of the KPIs will not be applicable such as settlements but others will apply such as interest conditions. We are also available to conduct periodic fee reviews as part of the service in addition to publishing the monthly reports. Amaces is also happy to attend custody meetings and answer questions or clarify issues connected with the sector. We are intending to roll out a new product named 'Custodian Capability Report' which will serve as an annual paper on the views of our pension fund clients about their respective custodians. It will give a great deal of insight in to how your own custodian is viewed and perceived by your peers. In consideration of the less importance of the report, however I do propose reducing the custody charge from £10,000 to £6,000 per annum once all segregated funds have disappeared. Should Westminster venture back in to segregated we can then review accordingly.

Foreign Exchange activity is likely to disappear altogether once the Insight mandate is converted to pooled and therefore the foreign exchange report will no longer be required at a cost of £10,000 per annum.

We value the relationship we enjoy with Westminster City Council and we would very much like to retain you as a client and hopefully the reduction in cost from £20,000 a year to just £6,000 per year will go some way to compel the Council to continue what we believe is a very important monitoring service of your custody service. We could of course extend this service to the Tri-borough at very little additional cost.

Tony Child
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