

## NZ Funds Management CIO Michael Lang talks KiwiSaver, calls on providers to undergo rating's evaluation. Your view?

By *Amanda Morrall*

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By **Amanda Morrall**

KiwiSaver provider NZ Funds Management is challenging the sector to invite greater scrutiny of their investment management practices through a rating system that would look at underlying factors behind performance.

The call comes on the heels of the fund manager having recently undergone a six-month qualitative review conducted by Australian rating agency **Lonsec** [3], a firm that does for managed funds what Standard & Poor's and Moody's does for debt issuers.

While Lonsec routinely provides ratings for superannuation schemes in Australia, the funds management sector in New Zealand has not been subject to the same degree of scrutiny. The sector has also attracted negative reviews for its lack of rigour. Research house Morningstar has issued New Zealand scores of D - twice in a performance report of the sector. ([See article by Amanda Morrall here.](#)) [4]

Chief Investment Officer Michael Lang said the industry's obsession with performance overlooked equally important issues around management and business practices. He said the sector needed to be judged on both quantitative and qualitative criteria, the latter which was addressed by Lonsec in its evaluation.

The rating agency, in its evaluations, probes such issues as the company managing the fund, its balance sheet, profitability, management, ownership structure, corporate strategy, risk management, counterparty risk, downside protection, and the investment team.

"Quantitative looks backward, whereas qualitative looks forward," said Lang. "So it asks how an investment performance was generated, was there a key individual behind the performance, is there systems and processes in place so that level of performance is repeatable going forward. It's to give you an insight into the stability of an organisation, and the likelihood of it being able to repeat the performance it has generated in the past."

A relative newcomer to the KiwiSaver space, NZ Funds Management has three funds on offer: its **Income Strategy** [5] (which Lonsec rating of "highly recommended"), and **Inflation Strategy** [6] and **Growth Strategy Funds** [7], both of which were rating "recommended."

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Lang said the self-imposed process, which cost the company NZ\$60,000, was in keeping with international standards overseas.

"It's long, expensive and thorough and it has to be done every year. It's a significant hurdle for smaller boutique providers, but for the larger providers who are already profitable, I think it's an essential cost rather than discretionary and that's something your fees should go toward.

"I think over the next few years, everyone will end up going through a combination of the quantitative and qualitative placing the industry as a whole in a better position to determine who got lucky with their performance, who is sustainable, and what risk managers are taking to generate the sort of returns they're advertising in the newspapers."

### Should we trust the ratings?

But with the reputation of ratings agencies themselves in tatters should ratings carry that much weight?

Lang said criticism, while understandable, was unwarranted, at least in the case of Lonsec. He said while the rating agency had a vested interest in the business of assessing fund managers, the livelihood of their businesses and brand depended on their brutal honesty and professionalism.

"It's an organisation that is providing research to over 100 different investment organisations in Australia and around the world, the only reason people are subscribing to their research is because they feel that Lonsec has proven itself as a credible ratings agency. For them to put that reputation at risk for the sake one fund manager is economically, a poor decision.

"The economic incentive is for them to do the best job they can to protect their brand."

Given the technical nature of the reports Lonsec produced, Lang said the information was mainly of benefit to financial advisers who would use it to help clients choose the most KiwiSaver schemes and funds.

Lang rejected suggestions that having to rely on a financial advisor to interpret the information would make the investment itself even more remote to KiwiSavers.

"They'd (financial advisor) be maximising the chance they'll be able to identify weaknesses with the investment process and excess risk taking and other things financial advisers are familiar with, so they can warn their clients about that a product might not be appropriate for them."

Lang said that should not stop KiwiSavers from taking greater interest themselves.

"The two things need to go hand in hand. The general population has to become more educated about financial matters. It's a big issue and as the industry grows, more time will be spent educating everyday New Zealanders."

(Removes link to Lonsec reviews on funds which, by law, can not be made public).

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