INSTITUTIONAL GROUP

The hidden costs of standing still.

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The cost of inaction can build over time, making periodic market testing an important part of good governance.

A changing landscape for UK pension schemes

The UK defined benefit landscape has undergone a profound shift in recent years. Trustees now have a wider range of options than ever before. Innovation across investment governance, implementation, and the wider pension ecosystem has created new opportunities for schemes to access specialist expertise, enhance decision-making, and manage risk more efficiently.

This shift has been supported by improved funding positions, higher interest rates, evolving regulations, and changes in sponsor priorities. As a result, approaches that were effective historically may no longer represent the best path forward.

Despite these developments, staying the course can feel like the lower-risk option, particularly where existing arrangements have performed well. When considering a new provider, there's a natural focus on transition risk, implementation complexity, and other uncertainties—all of which understandably attract significant attention. Yet far less attention is paid to the cost of not making a change. In this sense, the absence of reassessment can itself become a source of risk. CMA-mandated tendering and TPR guidance helped reinforce the importance of market testing; however, it does not necessarily replicate the same level of rigour, curiosity, or strategic intent that would accompany a discretionary decision to reassess existing arrangements.

Why inaction feels safer than it is

The temptation to stay the course is understandable and can often be the right option, yet every decision to retain an incumbent is itself an active investment decision. Opportunity cost refers to the value that could have been achieved by pursuing an alternative course of action. For institutional investors, this extends beyond investment returns, to also include risk management, implementation efficiency, and the ability to respond dynamically to changing conditions.

Behavioural economics helps explain why decision-makers often scrutinise the risks of change more closely than the risks of staying in place. It's natural for people to stay with what is familiar to them, as it feels safer. Additionally, making a change seems risky because of the fear of ending up with a similar or worse outcome. This reluctance to change often rules out the possibility of a better outcome.

Regret aversion can further reinforce loss aversion, as decision-makers may place greater emphasis on avoiding a visible negative outcome than on pursuing incremental improvement. Together, these biases can make existing arrangements feel safer than they really are, even when circumstances that may have supported the status quo have changed. It's important to acknowledge the human side of decision-making, especially when the actions made carry significant and long-term implications for pension scheme members across the UK.

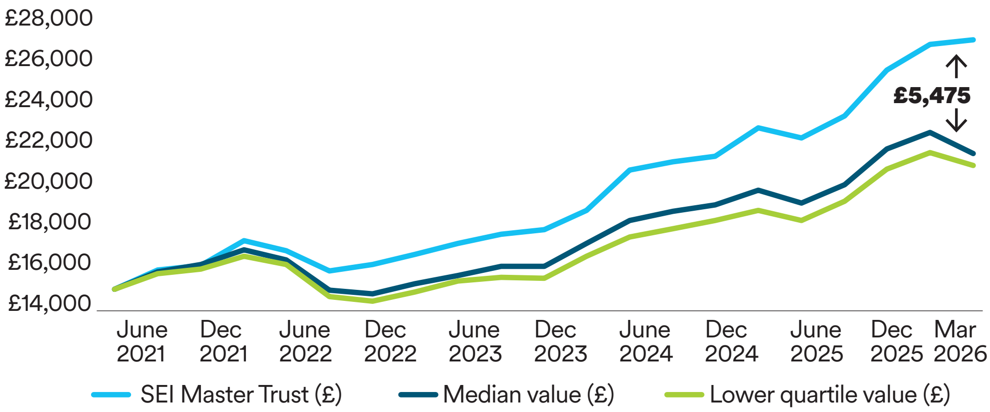
Reluctance to change does not imply a sense of complacency or lack of diligence but rather a natural response to uncertainty. Recognising these biases strengthens the case for periodic market testing. It should be viewed as an extension of good governance rather than a criticism of previous decisions.

The impact of opportunity cost in practice

The most intuitive way to frame the opportunity cost is looking through investment outcomes. It can be seen in the returns foregone when a more efficient portfolio could have been implemented. This can be visualised through the dispersion of realised outcomes across similar investors. Using Defined Contribution (DC) performance data as a proxy for long-term portfolio experience, the difference between providers can become increasingly pronounced over time. A similar exercise can be performed when comparing long-term Global Investment Performance Standards for Fiduciary Management Providers (GIPS)[1] or growth portfolio performance data for defined benefit schemes, reinforcing the same conclusion.

Despite operating in the same market environment and pursuing similar objectives, DC providers produce meaningfully different outcomes for members. This dispersion would not be driven by a single decision, but by the cumulative impact of asset allocation, manager selection, implementation efficiency, and governance over time. Thus, the implication is that inaction carries its own cost. With respect to the chart, the difference between median and top outcomes is approximately 25% after nearly five years. For a defined contribution member with a pot of £15,000, this represents a £5,475 difference which compounds meaningfully and ultimately translates into materially different retirement outcomes for members.

Growth of £15k defined contribution member pot (Jun 2021 - Mar 2026)



Source: SEI. CAPA Data Young Saver. June 2021 – March 2026. Median and lower quartile excludes SEI Master Trust. Past performance is not a reliable indicator of future returns. Performance figures are shown as gross returns.

In the context of defined benefit schemes, even smaller levels of dispersion can have a meaningful impact on long-term funding objectives or augmenting member benefits. For example, for a scheme 90% funded with a 30/70 allocation split between growth and matching assets, a 7.2% differential in growth performance[2] could equate to a difference of approximately three years in reaching full funding.[3] Importantly, switching providers does not guarantee a better outcome, but deciding to review a poor-performing provider allows the opportunity for improvement. The dispersion of outcomes is sufficiently wide that the decision to review, or not review, is itself a consequential investment decision.

Beyond performance: Governance and innovation in the context of fiduciary management

Performance provides a useful illustration of opportunity cost; however, it is an outcome rather than the underlying driver. Opportunity cost can also arise through governance quality and innovation. The dispersion of performance is often a result of differences in governance quality, decision-making frameworks and the ability to evolve portfolios over time.

Governance has become increasingly important as the pension landscape has evolved. The quality and speed of decision-making can materially affect outcomes. For many schemes, the focus has shifted further towards implementation precision and managing trade-offs between risk, return, and endgame execution. Governance models are not static, nor are they all created equally. Providers differ meaningfully in how decisions are made, and in the experience they bring from managing portfolios across different market environments and stages of a scheme's journey. Thus, not only does this influence returns but also the pathway taken to reach an endgame.

The fiduciary management market looks very different today than it did three years ago. Innovation has accelerated as competition has increased and schemes are focusing more heavily on endgame execution. As a result, previous impressions of providers may no longer reflect current market capabilities.

Questions to consider:

1. Does our investment governance model enable timely decision-making?

2. Have we reassessed our provider against today's market rather than historical perceptions?

3. Are we confident our provider continues to innovate as scheme objectives evolve?

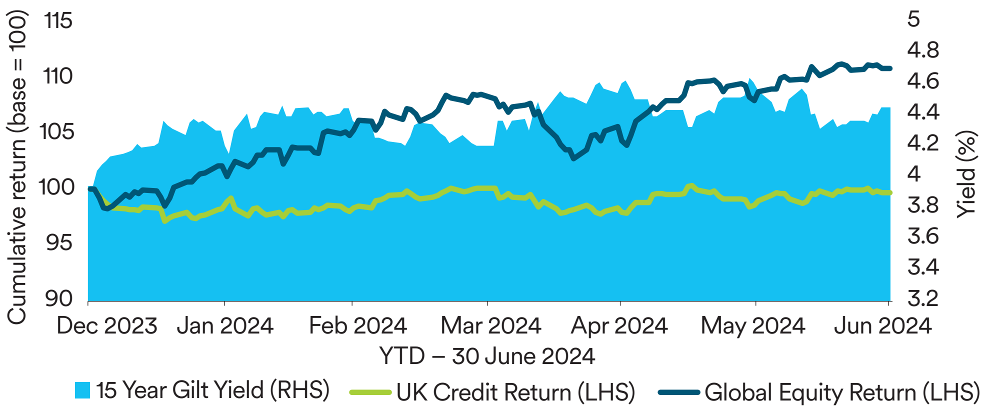
When 'best-in-class' moves

For example, recent developments for our clients have included more robust and transparent LDI governance frameworks, allowing for enhanced control over mandate parameters and improved monitoring of collateral and leverage. Similarly, advances in our portfolio construction now allow ESG considerations to be embedded directly within systematic optimisation processes, to ensure portfolios are calibrated to capture ESG opportunities while mitigating risks.[4]

These developments reflect a broader shift in how fiduciary management is structured, implemented, and governed in practice—including within our approach. Innovation only creates value if schemes can adopt it effectively and at the right time. Consequently, what may have represented a leading approach a few years ago may not fully reflect the opportunity set available today. In this context, relying on a historical understanding of the fiduciary management landscape risks anchoring decision-making to an outdated benchmark. Without periodic reassessment, there is a risk that schemes do not fully benefit from the evolution and, in doing so, risk falling behind.

One example of innovation is the management of cashflows, whether to meet monthly member benefits or to meet LDI collateral calls. The chart below shows the performance of equities and fixed income over 2024. Gilt yields rose over the period, while equities outperformed UK credit. Under a more traditional, prescriptive collateral waterfall, collateral may have been drawn from the underweight UK credit allocation. This could have crystallised losses, further increased the underweight position, and created a subsequent need to rebalance back towards target. By contrast, a more dynamic collateral approach may have allowed collateral to be sourced from an overweight equity allocation. In that scenario, equity market gains could have been realised, while also moving the overall portfolio closer to its strategic target.

Divergence in equity and UK credit returns in a rising yield environment



Source: SEI. Bloomberg. Global equity returns denoted by MSCI World Index performance. UK Credit returns denoted by Bloomberg Sterling Corporate Bond Index performance. 15 Year Gilt Yield denoted by FTSE Actuaries UK Gilts Yield 15 Yr yield. Covers the period 1 January 2024 to 30 June 2024. Past performance is not a reliable indicator of future returns. Index returns are for illustrative purposes only and do not represent actual fund performance. Index performance returns do not reflect any management fees, transaction costs, or expenses. Indices are unmanaged, and one cannot invest directly in an index.

The broader lesson is that implementation flexibility can have real value. In a more dynamic governance model, market movements can be assessed in context, rather than being managed through a static sequence of pre-agreed steps. Over time, the ability to adapt can influence outcomes such as transaction efficiency, portfolio alignment, liquidity management, and the overall resilience of the journey plan, leading to better outcomes for the pension scheme.

Standing still is not neutral.

Therefore, pension schemes that remain static risk missing incremental improvements that can compound meaningfully over time—in much the same way as investment returns. With this in mind, the cost of inaction goes beyond investment performance to include better approaches to governance and risk management.

Our behavioural biases can cause governance frameworks to unintentionally overweight the risks of action and underweight the risks of inaction. As a result, the decision to remain with an existing provider should not be viewed as neutral. In a market where outcomes, governance models, and capabilities continue to evolve, including within our own approach—the benchmark for what constitutes a 'strong' solution has shifted.

Standing still is an active choice and one that carries its own cost.

Get in touch

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SOURCES

[1] The GIPS standards for FMPs are ethical standards for investment performance presentation to ensure fair representation and full disclosure of investment performance. GIPS® is a registered trademark of CFA Institute.

[2] XPS Group, Fiduciary Manager Review 2026, May 21, 2026.

[3] Source: SEI. For illustrative purposes only. On a technical provisions basis. Projections based on SEI's Capital Market Assumptions (CMAs), which include return, volatility, and correlation assumptions for the liabilities and various asset classes. Projections are not a guarantee of future results.

[4] SEI – Not all ESG risks are equal. ESG considerations for active investors.

IMPORTANT INFORMATION

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Source: SEI

The CMAs are revisited regularly on a minimum basis to reflect the changes in the market environment. The forecasts shown on those pages are not necessarily indicative of the future or likely performance of the portfolios, especially over a short-term time period.

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