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Neil Woodford: the continuing fallout of a scandal

The worlds of sport and art prove that the fallen star manager highlights some hard lessons for the fund industry to learn

Claire Ruffley | FT.COM | 2017

It is more than 18 months since the implosion of Neil Woodford's business spoofed the biggest British investment scandal for a decade. Yet for his former customers, the wounds are still raw.

More than 300,000 individuals who entrusted their hard-earned savings to the famed stockpicker are still waiting to recoup the money. Many have had to delay retirement after nursing loss of thousands of pounds of losses.

Meanwhile, the Financial Conduct Authority, the industry regulator, is under pressure from politicians and consumer advocates to conclude a long-awaited investigation into the affair. Law firms representing thousands of alleged victims are gearing up to take the matter to court.

While the fallout from the Woodford scandal has yet to deliver a satisfactory conclusion for his former investors, there are plenty of lessons that can be learned from what has transpired so far, many of which (sorry) in my new book, Bull Shit & Lies: The Rise and Fall of Neil Woodford and the Fate of Middle England's Money.

The scandal shows a harsh light on a wide range of industry players — from Woodford and his business associates, to the advisers and intermediaries who convinced their clients to invest with him, the fund supermarkets that promoted his products, and, ultimately, the FCA itself.

For retail investors, a lot comes down to investment basics — choosing a fund manager, avoiding the seductive appeal of glamorous performance, and focusing on fundamentals, such as financial performance, liquidity and transparency.

The Woodford drama comes in a bumper crop when he was forced to suspend his Equity Income fund in June 2017 — the fund that was the cope with a range of investors sculpting their cash. These trapped inside have since watched powerfully as the value of their savings has diminished. They stand to lose up to £1m — more than a quarter of the fund's value at suspension.

Woodford — once lauded as "the man who can't stop making money" and "Britain's Warren Buffett" — closed his business a few months later. It appeared to be an ignoble end to one of the investment industry's most celebrated careers.

Given the lack of closure in the affair, it is curious that Woodford last month announced he could back — in an interview with the Sunday Telegraph. His revelation that he planned to launch a new business based in Guernsey inspired the Crown Dependency's financial regulator, who told the FT that Woodford had yet to apply for authorisation and should not use the island as a "back door" to restart his career.

Woodford, who declined to comment for this article, has recently opened a new business in London's Mayfair, with his former colleagues joining him. Mayfair, according to the local preservation society. But despite the central headquarters, the prospects for his new venture getting off the ground appear uncertain given the challenges he faces in finding a regulator to give him the green light.

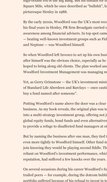
While my book raises questions for professional fund managers, regulators and the government, it highlights key questions for investors. Not only those rising their investment cash but those who have also contemplating putting money into funds, whether for the first time or the umpteenth.

Beware the 'star manager'

Woodford's fall from grace has drawn a line under the investment industry's star fund manager culture.

Throughout the sphere and stepes, investment groups competing for clients spend heavily on promoting individual fund managers. The most professional investors whose performance records are then apart from rivals, but who would also play well in meetings with clients and in media interviews.

Jesse, a cadre of elite managers emerged. Peter Lynch of Fidelity Investments and Bill Miller of Legg Mason become investing superstars in the US, while the likes of Anthony Bolton of Fidelity International dominated in the UK.



Bill Miller, from Legg Mason, and Peter Lynch, of Fidelity Investments — Getty Images

Anthony Bolton, the fund manager of Fidelity's Special Situations Fund — Photo: Bloomsbury/FT via Getty Images

Marketed by their employers, these men were in turn remunerated by influential financial advisers to their clients. The strategy aimed to tap into the long-standing human trait of preferring to follow leaders even teams, and it worked.

The more companies fired up the profiles of these stars, the more they relied on them to attract and retain clients. In short, the more fund managers demanded higher and higher pay, with big annual bonuses for their performance.

A rash of personality developed around the best-known managers, who lived rock-star lifestyles, hanging but cars and luxury mansions.

Woodford's 20 years working in Henley-on-Thames for Perpetual (later Invesco Perpetual) was a textbook case of the rise of the star fund manager.

Born in Berkshire in 1960, he set his teeth in the City in the rather daring the high-octane era of the Big Bang. But his disdain for the City culture of the Square Mile, which he once described as "bullish", led him to move to picturesque Henley in 1988.

By the early 2000s, Woodford was the UK's most recognizable stockpicker. In his prime, he ran Invesco's Perpetual Income fund, a vehicle that gained awareness among financial advisers. So sort upon time Invesco, and in second half of the 2000s, Woodford started to launch such a Fidelity Jupiter, Henderson and Neptune — was Woodford himself.

So, where Woodford left Invesco to set up his own business in 2014, naming it after himself was the obvious choice, especially as he said his co-founders hoped to bring along old clients. The plan worked and within a few months, Woodford Investment Management was managing more than £2bn.

Yet, as Gerry Grimstone — the UK's investment minister and former chairman of Standard Life abrdnets and Barclays — once cautioned, you shouldn' never buy a fund named after someone".

Putting Woodford's name above the door was a clear sign of who was the boss. Woodford was the ultimate stockpicker, and he structured his business into a multi-strategy investment group, offering not just UK equity funds, but global equity funds, bond funds and even alternatives. The founders also hoped to provide a refuge to disaffected fund managers at other investment groups.

But by naming the business after one man, they tied the fate of the venture even more tightly to Woodford himself. Other fund managers were dissuaded to join knowing they would be playing second fiddle. The whole business was reliant on Woodford's investment performance, which, despite his stellar reputation, had suffered a few knocks over the years.

On several occasions during his career Woodford's fortunes had significantly trailed peers — for example, during the dotcom bubble in more when his portfolio suffered because of his refusal to invest in tech stocks. When the bubble was finally pricked, his fund was a big winner and his reputation as a stockpicker soothsayer was established.

"It was the [Internet/bubble bursting that really made Neil," recalled his former colleague Mark Nicholas, who joined Invesco Perpetual in 2000 and ended up being were accused of being antiquated, but when Neil's really good at so counting the stampede. That takes a lot of balls."

The Woodford centric business at Woodford Glen also fostered a culture where staff were expected to Woodford and his side Gill Greaves, Newman had little future at the business.

Two of the company's founders, Nick Hamilton and Guy Smith, resigned within the first year after falling out with Woodford and Newman over the business's compliance culture and the level of due diligence carried out on Woodford's investments in private companies, according to several former WIM staff members.

Hamilton and Smith were even asked to be exit interviews at the FCA to discuss their reasons for leaving. The regulator did not interview in the business for another two years.

A spokesman for Woodford told the FT: "It is true that the FCA did not approach us after the interview, and I am sure would have approached us had them been any concerns raised from the interviews."

The lack of challenge on regulatory issues was unhealthy. Woodford and Newman extracted profits from the business for themselves each year in multimillion-pound dividend payments — close to claims over the five years the business was running — while paying staff fixed salaries. It was, in a way, the logical result of the dominance of high-profile individuals.

Stay alert for style shift

Woodford's reputation at Invesco had been forged on his investment style of selecting large, blue-chip British companies that could be relied upon to produce steady dividend payments, such as pharmaceutical and tobacco companies. Woodford trusted these businesses, which he felt were underrated and resilient enough to withstand an economic downturn.

Stocks who invested in Woodford's main fund throughout his six years at Invesco Perpetual would have seen their investment grow by more than 300%. Would have realised that before the Sunday Telegraph, Woodford was increasingly interested in investing in unlisted and small-science-based companies that have little revenues to steady and dividend payers.

Most investments that Woodford made in science-based start-ups were so small they barely registered within the Equity Income fund, which was huge.

But as my book reveals, during his latter years in Henley, Woodford clashed with his bosses at Invesco over these investments, with one company bringing issues to a head.

Woodford plunged Jurjaan into Xylesca, a US business based on a garage full of scientists, which was seemingly unknown to Invesco Perpetual's investment background. This valued the business at £4.5bn. The size of the investment and value it placed on the company alarmed Invesco bosses, who set up a committee to assess all private investments and ban future investments, according to leaked documents.

Woodford also wanted to launch a new fund at Invesco that would focus on unquoted and small listed companies, similar to the Patient Capital Investment fund he would later set up, according to people familiar with the plans. But his bosses at Invesco rejected the proposal.

"The only reason to launch the [new] fund was to satisfy Neil's desire," said a person close to the business. "It's his guilty pleasure to do these unquoteds, to be the big man."

Feeling his wings were being clipped, Woodford told Invesco executives in early 2013 he was leaving the business and set up Woodford Investment Management a year later.

The new venture created retail investors, many of whom had little appetite for risky start-ups. Equity Income was designed to mimic Woodford's popular Invesco funds and close away as many of his former shareholders as possible.

But as the cash poured in during the heady first couple of years, Woodford wrote scores of hefty cheques to poorly-managed private companies, whose tribulations would ultimately contribute to his collapse.

While Woodford's stock-shift accounts for much of his poor performance compared with his earlier record, ultimately his biggest failing was an inability to pick strong companies and hold on to them.

Woodford's stockpicking process had been what propelled him to stardom — but he'd let him down badly when running his own company. Some analysts had long suspected that, while he was good at making big sector calls, he struggled to identify individual performers within industries, especially start-ups.

When it came to unquoted companies, for every potential winner — such as Oxford Nanopore and Synstogen, which both played starring roles in the fight against Covid-19 — there was a stash of duds. Even in listed companies, where Woodford had long experience investing, his record in the final few years was poor.

An analysis by Morningstar, an investment data provider, found that of the 32 companies Equity Income held in stock, just six had produced a positive return by the time the fund closed in October 2019. Of those, Woodford had sold all but two. The other 26 companies that had value during his tenure, Woodford sold, on average, at a loss.

He had made the classic investor mistake of keeping hold of his losers while selling his winners.

Asked about his role in the failure of his fund, Woodford told the Sunday Telegraph last month: "I'm very sorry for what I did wrong. What I was responsible for was underperformance of the fund. I'm very sorry for my errors running total funds in future to avoid such things happening again in a fund."

But he also stated: "I am very for the things I didn't do." He did not suspend or liquidate the fund, he said. "As history will now show, those decisions were incredibly damaging to investors and they were not mine."

Treat 'buy' lists with scepticism

A spell of more than then former Woodford investors at a recent event hosted by Shareline, the retail investor campaign group, found just a part over were persuaded to back him by independent financial advisers. The rest mostly used investment platforms, or fund supermarkets, which allow investors to select funds themselves.

These websites have proliferated in recent years as more savers search for cheaper ways to invest. But the findings show that those who were willing to pay extra for professional advice were more likely to have suited in the two years leading up to Equity Income's suspension, when Woodford's problems managing his fund's liquidity levels were already known.

Of the investors surveyed, more than three-quarters had invested via Hargreaves Lansdown, the UK's most popular fund platform with more than 1.4m users.

Part of Hargreaves's success is down to its so-called "buy-buy list", a selection of funds it recommends to clients. But buy-lists make investors' lives easier as the funds they feature are tested as the cream of the crop. But such lists tread a fine line between advice and advertising.

From a regulatory perspective, they are not classed as financial advice or guidance, and therefore are not monitored by the regulator. But the way the lists are presented on the platforms often leaves customers confused about whether they are being recommended the products or not.

FT Money readers have frequently complained about the obfuscation. Hargreaves Lansdown has said it has "made investment advice more clear within its website, and the clear process it operates to encourage people into one to invest," said one Woodford investor.

The best fact but helped to convince Hargreaves' army of DIY investing customers to back Woodford was the fund's long-term performance, an important chart, with its customers accounting for 30 per cent of assets in Woodford's Equity Income fund and 60 per cent in the smaller Income Focus fund. Woodford FM received about £500m in fees from Hargreaves' clients over three years.

In January 2019, Hargreaves slimmed down its best-buy list. Incredibly, despite Woodford's poor performance for more than 18 months by this point, his two main funds survived the cull. Equity Income investors were down 17 per cent in 20 months.

As part of the negotiations to stay on the list, Woodford and Newman agreed to reduce their fee to 0.4 per cent, where investors on rival platforms were being charged 0.75 per cent.

When Hargreaves executives later revealed they had had reservations about Woodford's investments in hard-to-sell companies as early as 2017, they failed to shine a light on the fund's long-term performance, which had underpinned Equity Income's suspension more than 18 months later, the platform's credibility took a battering with its customers.

Hargreaves declined to comment for this article, but has previously said the decision to keep the Woodford funds on the best-buy list was not based on the discount alone, but particularly due to its potential investment performance. It has since rebranded its best-buy list.

Hargreaves' failings have also turned best-buy lists in general. Investors who relied on what they believed to be carefully researched lists of the funds with the potential to outperform the market were shocked to discover that the selection were sometimes based more on the level of discount the fund manager offered.

This story has been amended since publication to correct the negotiated fee charged by Hargreaves Lansdown investors for Woodford's company. It was 0.4 per cent, not 0.4 per cent.

Claire Ruffley's Bull-s-t Lies: The Rise and Fall of Neil Woodford and the Fate of Middle England's Money is published by Penguin and is on sale now.

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Sebastianmill 2 MONTHS AGO
@GEORGE about this. Fortunately aggressive tax frequency for flogging his funds to.
Recommend 0 Reply Report

Gabby 2 MONTHS AGO
@Sebastianmill Yes, it is a FCA issue, and most of what they are supposed to watch out for. Tax for Fundamental management is FCA's Client Money Rule, basically, if a company wants to use your money, it must put it into a separate bank account. Plenty of Woodford's Ponzi schemes in the pipeline, prepare for the bill and they hold the cash.
Recommend 0 Reply Report

Mikhail Bulgakov 2 MONTHS AGO Edited

Woodford's fall from grace has drawn a line under the investment industry's star fund manager culture.

Cathie Wood of ARK Invest?

Recommend Reply Share Report

Show More Replies

Ravenswood 54 MINUTES AGO

Yes, re HL. I was very impressed with a piece in their newsletter about the rigorous process they applied to choosing a fund manager for their list. I was told that Woodford hadn't kept to the rules they'd given him. They also said he'd been in a similar position before and come out of it as per this article. I asked what they were doing to make sure that FMs kept to the rules in future, and what they'd do if they didn't. I got no reply.

Recommend 1 Reply Share Report

PeterX 55 MINUTES AGO

In nearly all of the articles and books about this case the role of the Depositary is overlooked. The rules state the following as responsibilities for the Depositary:

carry out the instructions of the Authorised Fund Manager, unless they conflict with:
(a) the applicable national law; or
- *(b) the instrument constituting the fund; or*
- *(c) the prospectus; or*
- *(d) COLL5 (Investment and borrowing powers);*

Therefore, if the fund was investing in securities that were not envisaged by the prospectus and the concentration limits on investments were breached then the Depositary has a duty to call these out. I'm not close to the detail of this situation, but the role of the Depositary to act in the best interest of investors was clearly meant to catch this kind of situation. In summary, either the Depositary missed something or the rules need to be tightened.

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Xi Jinping's Ethics Advisor 1 HOUR AGO

is craig newman involved in his new fund?

Recommend Reply Share Report

Shatner's Bassoon 1 HOUR AGO

He's ruined the shirt + crew neck jumper combo for me, it was my go to dress down outfit on cooler days.
I've got to find new casual city drip.
It isn't easy.

Recommend 1 Reply Share Report

Man_overboard 2 HOURS AGO

I did very well out of Perpetual High Income long before Invesco was involved and certainly not because of the name Neil Woodford, whom I'd never heard of. But that reinforces Owen's point, I was steered to invest in it because it was generating consistent performance, not because of the name of the fund manager. I did invest in Woodford when he left, but was fortunate enough to get out fairly early on. I think for the ordinary punter active investment is like a snake and ladders board: you get aboard a ladder that's climbing steeply and then suddenly you're on a snake plummeting fast – and few have the psychological make-up to walk past the ladders or get off at the right time. The alternative – passive – seems dull and places your faith purely in the belief that markets will go up over time.

Recommend Reply Share Report

Kate P. 2 HOURS AGO

How bold was it for a UK equity income manager to not hold Tech stocks during the dotcom bubble? I doubt any were in his investment universe.

Recommend 1 Reply Share Report

Tech Hub 2 HOURS AGO

No mention here of Mark Dampier who, as head of research for HL, relentlessly promoted Woodford's funds over many years to HL clients despite the obvious underperformance, style drift and widely-held suspicions that Dampier himself had sold his own holdings in the funds.

Also, Dampier and his wife sold £5.6m of HL shares in May 2019 shortly before HL suspended Woodford Equity Income in June 2019. Possibly a coincidence - but HL shares took a hammering after the Woodford suspension was announced a few weeks later.

Recommend 3 Reply Share Report

Shatner's Bassoon 1 HOUR AGO
In reply to **Tech Hub**

Spot on

Recommend Reply Share Report

No extra marks for degree of difficulty 2 HOURS AGO (Edited)

It is odd how the narrative moves towards "investors" being mislead albeit there were some questionable actions after the rot had set in. Woodford published all of the funds individual holdings and so anyone concerned about the quality or marketability of their investments had plenty of time to react. I was a long term holder of Invesco Income and purchased Woodford Equity, however when it became clear the fund was moving in direction I was not comfortable with I sold it, not easy after so many years of outperformance. I remember thinking that I could so easily be wrong to sell as those smaller companies could have had great futures, I had no way of knowing. What I did know was that early stage companies did not sit comfortably with my risk profile and the quality of the quoted holdings was clearly diminishing, this was a big shift in strategy for the fund. How many times do people need to be told that past performance is not a guide? If investors do not have the time or expertise to understand what they are trying to achieve and the risks they are comfortable with to achieve their goals they need to pay for professional help. I know this can be expensive but the right advisor should ensure that problems like this are avoided .

As for not buying a fund named after the manager that is a not a factor anyone should use in their analysis. Some of the best managers set up on their own as , just sometimes, working for a large fund management group can lead to putting fund size before performance and marketing time before portfolio management.

Recommend 2 Reply Share Report

Satisficer 2 HOURS AGO

Reject hubris and stick to your knitting.

Recommend Reply Share Report

...and breathe 3 HOURS AGO

No one can say they did not know what was in the fund. The fund's holdings were published, indeed a far higher level of disclosure than industry norms and certainly, say, Fundsmith, which just lists the top 10, with no %. They don't even put the full accounts on their website, using some short form version which omits the holdings.

Recommend 1 Reply Share Report

Thinkofifthisway 3 HOURS AGO

Nice watch on his wrist! Probably the fees I paid ...

Recommend Reply Share Report

Heysham 3 HOURS AGO
In reply to **Thinkofifthisway**

Well spotted. Scientists have discovered that there is a statistically significant correlation between the size of a man's watch and that of his ego. After all in an age of mobiles you don't actually need a watch.

Recommend 1 Reply Share Report

Latch 2 HOURS AGO
In reply to **Thinkofifthisway**

Probably part of the watch is the fees you paid.

Recommend 1 Reply Share Report

Man_overboard 2 HOURS AGO
In reply to **Latch**

Or maybe the watch is in part the fees he paid?

Recommend Reply Share Report

onemorething 3 HOURS AGO

Great article. Very thorough. Sorry Owen, but I probably don't need to buy your book now...

This is what jumps out to me:

> Hamilton and Smith were even asked in for exit interviews at the FCA to discuss their reasons for leaving. But the regulator did not intervene in the business for another two years.

Either the two departing founders were being economical with the truth about their departure, or the FCA had a couple of Woodford whistleblowers in their hands and didn't know what to do with them.

This, ultimately, is a failure in compliance and regulation. Woodford's hobby investments in unlisted medical companies at inflated psuedo-valuations meant he was breaching the rules of his own UCITS fund. It was that illiquidity that caused the fund to lock investors money away from them.

Woodford was arrogant and HL were complicit to maintain a commercial relationship. No surprises there. But not against the rules.

The problem was that when people wanted their money back, the fund was not in a position to "fail" naturally. If Woodford had been made to operate within the rules, people would have got their money back, and it would just be the story of a fall from grace, rather than a scandal.

Recommend 4 Reply Share Report

Roaring Kitty 3 HOURS AGO
In reply to **onemorething**

Fact they left in such a fashion should have been a pretty clear bloody signal to the FCA. However, then again this is the FCA and over the last few years they've been as much use as a teapot made out of chocolate.

Recommend 3 Reply Share Report

Rambler 3 HOURS AGO

The other biggie in this is that if someone with 20 or 30 years in the business and an army of analysts at their disposal can get picking stocks so wrong, what hope is there for the average Joe to get it consistently right? In 20 to 30 years of doing something you'll be right some of the time, wrong some of the time, and probably horrendously wrong at least once.

Therefore don't put everything in one place. Create a portfolio where if one bit goes wrong there may be several other things doing OK.

Easy to blame Woodford. But more is the fool backing one horse to win.

Why believe anyone can be right all the time? Possibly the most certain thing is that the world's economy will grow over the long term - at different rates, at different times and in different places.

Until the planet decides it's had enough of that malarkey.

Recommend Reply Share Report

Reluctant European 3 HOURS AGO

Even better would be to ignore the article: instead of avoiding pitfalls of active funds, one should rather buy low cost index trackers.

Recommend Reply Share Report

RDS1 3 HOURS AGO

A FM imploding due to his own hubris is not a surprise, and will likely happen again. However, the clear and extremely damaging conflict of interest at Hargreaves is scandalous, yet apart from occasional sidebar comments this seems to be largely ignored by both the media and the regulator.

Recommend 2 Reply Share Report

Obvious 3 HOURS AGO

The book is out of stock on Amazon....

Recommend Reply Share Report

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