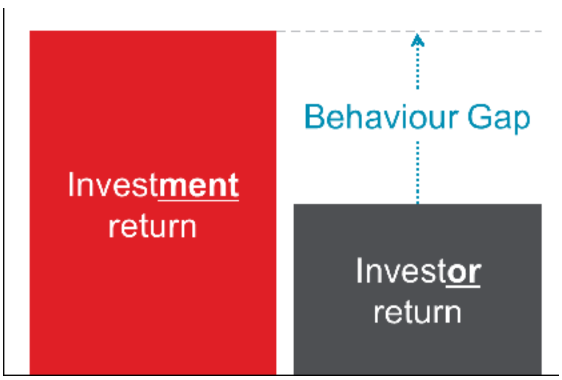
Being ‘active’ pays

Tim Giles, head of investment for UK and Ireland at Aon, explains how being ‘active’ can help to improve your pension scheme’s returns

If we compared all the pension schemes in the UK, we would find a large variation in the returns achieved. In the diagram below, you will see a gap between the investment return and the investor return. This gap in performance is down to behaviour. We have identified four key areas where being active in your behaviour and decisions can add to your scheme’s returns:



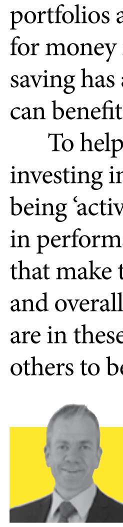
Money: Being dynamic
Where you allocate your money has a big impact on your scheme’s overall outcome. Success means actively changing your allocations based on your long-term funding objectives and the expected timescales to achieve them. Schemes today are at different points on their de-risking journeys, and so it is vital that their portfolios reflect their evolving journeys. Those targeting self-sufficiency (rather than buyout over the medium term) can consider investing in relatively illiquid assets that provide contractual income. This involves diversifying away from traditional fixed-income strategies into income generating assets such as asset-backed securities and private-market debt. Longer-dated cashflow generating assets such as long-lease property and infrastructure debt can also help to generate extra yield. Actively adjusting the asset mix based on attractively priced opportunities in the market can get schemes closer to reaching their end game.

Energy: Active decision-making
Trustees often suffer from ‘decision fatigue’ – the deteriorating quality of decisions made by an individual after a long session of decision making. How many trustee meetings have the investment section in the afternoon…when people are tired and the agenda is rushed. Actively structuring your decision making can help to overcome behavioural biases. This could mean using an agenda structure with strategic, long-term aspects at the start of the meeting, with the more regular business coming lower down your agenda. Putting in place flexi-teams, or dynamic sub-committees comprising people capable of actioning decisions, can ensure that post-meeting momentum continues and projects move forward in a timely way. Structuring meetings in this way can give trustees the energy to make informed, active decisions, which can influence returns.

Time(-liness)
Trustees today are more time pressured than ever; two-thirds spend 20 hours or less on investment matters each year. Given that investment is one of the most vital aspects of running a scheme, being active and spending 100+ hours each year is key. This can be achieved through quarterly meetings with half a day dedicated to investment, via monthly full day sub-committee meetings and/or through ad hoc phone calls in order to make key decisions. But what if you cannot spend this amount of time? You may wish to consider what aspects of the scheme and investing you can delegate to external experts. Also, exploring investment-related actions in between meetings can allow you to make the best use of meeting time, ensuring you are focused on making timely and informed decisions.

Cost/fees
Even if you actively allocate your money and make timely decisions, the effect of excessive fees or hidden costs can erode returns. When it comes to scheme charges, can you comfortably itemise all the fees you pay? Can you be sure that the fees are as low as they can be? Actively accessing and benchmarking your scheme’s asset management costs (see the Institutional Disclosure Working Group’s [IDWG] cost disclosure template) can allow you to achieve greater transparency and can help you to negotiate fee-efficient portfolios and determine whether value for money is being achieved. Every saving has an incremental impact and can benefit your scheme’s returns.

To help close the performance gap, investing in the right areas is crucial. If being ‘active’ can result in a +1% change in performance, what difference would that make to your scheme’s funding level and overall outcomes? How active you are in these areas? Can you challenge others to be more active on your behalf?



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