Saving for tomorrow

Joanna Sharples considers how today's pension savings can shape tomorrow's world

Pension saving might be for the long term, but the way schemes invest employees' money has a day-to-day effect on the world around us.

We are seeing this trend first-hand. Our master trust, The Aon MasterTrust, has seen nearly a 50 per cent increase in the number of members exploring ESG (environmental, social and governance) investment options since the beginning of 2020.

But it is not enough to think about ESG as a self-select 'fringe option' in a pension scheme. Addressing issues such as climate change need to be part of default fund investing, so that employees who do not want to manage their own fund choices also know their money is being invested responsibly.

These factors, combined with Aon's core belief in the importance of the potential risk and return benefits of responsible investing, have contributed to our decision to use a low-carbon investment approach for all our defined contribution (DC) pension default investment funds.

To achieve that, we've introduced two new funds. In October 2020, we introduced the Aon Factor Service. This is a passive equity fund with a low-carbon overlay, which means the range of companies the fund invests in is based around an index, but the selection is 'tilted' in favour of businesses with lower carbon emissions and away from businesses that are more carbon intensive.

Working with our fund managers and index provider, we want to maintain the right balance between excluding ineligible companies completely and retaining some level of investment in businesses where there is a demonstrable commitment to change. Additionally, the fund eliminates stocks that breach the UN Global Compact, an international agreement which encourages sustainable, socially responsible policies in business.

Carbon emissions for The Aon Factor Service are around 60 per cent less than a traditional market capitalisation-based fund. From October 2020, the fund makes up 25 per cent of our DC default investment strategy for the early years of a member's pension savings (up until around 15 years before retirement) and around 55 per cent of our active default strategy. Crucially, we have achieved this with no reduction in expected returns for members.

We have also created the Aon Managed Global Impact Fund, which is available as part of our self-select fund range. In January 2021 we went a step further and introduced a 10 per cent allocation within our active default strategy for The Aon MasterTrust, and Group Personal Pension.

The Aon Managed Global Impact Fund is an actively managed equity fund – so our investment managers choose the companies they invest in, rather than following an index. Those selections are based both on financial performance and whether the company is making a positive impact on society and/or the environment. For example, we invest in companies involved with electric vehicle battery recycling, water treatment in developing countries, bringing financial services to underserved communities and plant-based alternatives to meat.

As well as generating a positive impact, the fund aims to deliver healthy long-term returns to savers. Using simulated figures, based on actual returns from our three underlying managers and our initial manager allocations, over a three-year period to 31 December 2020 the Aon Managed Global Impact Fund would have generated a return of 20.7 per cent per annum,[1] which was 10.5 per cent per annum higher than MSCI World-ND index, which we use as our benchmark. Crucially, investing in a sustainable way does not mean investors need to accept lower returns.

By focusing on responsible investment in all our DC default investment strategies, we are offering members a better balance between risk and reward as well as the chance to understand how their pension can contribute directly to a more sustainable future for everyone.

Written by The Aon MasterTrust chief investment officer, Joanna Sharples

[1] **Source**: Aon, eVestment. Simulated performance provided over three years to 31 December 2020. Please note that the past performance returns have been simulated and that these returns have not been achieved. The simulation uses monthly returns and assumes annual calendar year rebalancing. The impact of fees and expenses is not included in the calculation. Past performance is not a reliable indicator of future performance.