Trustee Guide 2022:

A brighter future

Featuring:

- The big issues for pension trustees in the coming year
- Whether investing via low carbon indices goes far enough
- The compelling ESG case for bulk annuities
- How to improve retirement outcomes in the year ahead and beyond
- Why so many still do not plan for retirement
- Net zero through fiduciary management
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Trustee topics for 2022

What will be the big issues for pension trustees in the coming year? *Pensions Age* spoke to a range of companies and industry bodies to gain some insight into the challenges and the hopes

New governance requirements, evolving investment strategies, and the need for good quality data to help drive initiatives such as the pensions dashboards and GMP equalisation: These will be among the priorities that pension trustees will be grappling with in 2022, according to industry experts.

Prominent among the issues raised are governance and investment strategies specifically around DB pension schemes. The new DB Funding Code of Practice consultation from The Pensions Regulator is expected in 2022, and this forms the backdrop for many comments about the year ahead.

Cardano Advisory director, Emily Goodridge, says she expects that the role of covenant assessments will change, with less focus on the rating and more on what sponsor-strength means for the strategies set by DB trustees. "TPR's much-awaited new DB Funding Code of Practice can be expected to require a better articulation of how scheme risks are supported by the covenant, forcing trustees to justify their risk management and journey planning decisions. Even where schemes meet TPR's lower-scrutiny 'fast track' criteria and covenant may be less of a concern, trustees will be reminded it is only a regulatory risk filter and that doing the right thing to protect members will mean going further."

Meanwhile, Aon partner and head of UK retirement policy, Matthew Arends, observes that 2022 will mark 25 years since the implementation of the "little-lamented" Minimum Funding Requirement (MFR), adding: "My fear is that TPR's new DB Funding Code will turn out to be MFR2 and we will, in effect, turn back the clock 25 years on the funding regime. TPR can avoid this by dropping its requirement to measure bespoke compliance with the new regime by reference to the new fast track compliance option. Fast track has a lot of attractions and meets the stated policy aim, but not if it is also used as a yardstick for bespoke compliance."

Many schemes are now much better funded than they were, according to Willis Towers Watson head of retirement, Great Britain, Rash Bhabra, and the focus is therefore increasingly on each scheme's ultimate objective. "2022 should be another busy year for the risk transfer market as schemes reach important milestones on the road to making pensions secure. More effort is also going into enhancing members' experience. Where this involves communicating and expanding options available to reshape retirement benefits it can lead to a reduction in risk," says Bhabra.

End game

Adding a buoyant buyout market and the likelihood of more and more schemes discussing end game strategies to the introduction of the funding code leads APPT chair, Harus Rai, to conclude that

Hopes for CDC schemes

"One big hope for 2022 is that Royal Mail's collective defined contribution scheme is both successfully launched and acts as a positive first mover to encourage others. There's also the hope that the government's commitment to introduce regulations for other types of CDC scheme, such as master trust CDC schemes, and to provide increased flexibility for the concept, bears fruit in 2022."

Aon partner and head of UK retirement policy, Matthew Arends

"we are likely to see a lot of work being done over the next 12 months to make sure schemes are 'buyout ready'".

There is a clear trend, according to Arends, towards more UK DB pension schemes opting for buyout as their long-term target rather than self-sufficiency. Arends says that consequently it's hard not to imagine that trend resulting in significant bulk annuity transaction volumes in the next 12 months. "While more schemes are undoubtedly seeing the way to buyout as their correct course of action, for others it's helped clarify their wish to run on a low-risk basis, either temporarily or in perpetuity, even if they could afford to buy out."

Goodridge goes on to predict that potential regulatory approval of the first DB consolidators in 2022 will kickstart a wave of consolidation discussions driven by covenant concerns, while the Pension Schemes Act 2021 will double down on DB pensions governance requirements for corporates and require greater information sharing and communication between trustees and their sponsors.

Economic indicators

For PTL client director, Clare James, the one important action that all trustees of DB schemes should be considering as soon as possible is reviewing their investment strategies to ensure they are fit for purpose, against the backdrop of a changing economic outlook, with rising inflation and consequent expected rises in interest rates.

Those economic indicators include an annual CPI increase to October 2021 of 4.2 per cent, the highest level it has been since November 2011, says James, while the RPI, to which pension benefits are more often linked, increased by 6 per cent in the year to October 2021.

"Trustees would therefore do well to review the level of interest rate and inflation risks they are running in their schemes and consider what, if any, action may be appropriate," she says. "For example, there might be scope to adjust the level of LDI inflation hedging to increase the level of inflation protection afforded to the scheme."

Data quality

Both the perennial subject of GMP equalisation and the approaching introduction of the pensions dashboards are identified by many commentators as being of importance in 2022, and facilitating those initiatives will be the collection, storage and use of good quality data.

"Vital to the successful execution of nearly everything, quality of data seems to become more important each year," says Arends. "The task of addressing data accuracy will not look so dull if a scheme faces the nightmare of inaccurate data when it comes to complete a member options exercise, buy a bulk annuity, perform GMP equalisation and so on. And don't forget that the pension dashboards are all about data. The bottom line is that having better, cleaner data is key to schemes' ability to make better decisions on their way forward."

Bhabra says the company's surveys show that equalising pensions in a way that balances pragmatism with risk is a major item in most trustees' in-trays, and he hopes that legislation to make GMP conversion easier should help schemes settle on a preferred approach.

Rai also identifies both GMP equalisation and pensions dashboards as key subjects of focus for trustees in 2022. With the former, many schemes will be engaged in dealing with the practicalities, deciding not just on which method to adopt, but also putting in place the building blocks to tackle the issue over the next 12 months.

"There is no overnight fix and, for those schemes affected, this is a huge project that will take diligent planning and execution. It has the potential to be an expensive exercise, so careful managing of budgets will be required."

Rai observes that the pensions dashboards will require input from individual schemes, that there are probably more questions than answers currently, but that things should become clearer over the next few months. "Over the course of 2022, schemes will need to consider not just how they ensure that they provide the information that is needed within any stated timescales, but also how they ensure that the quality of those inputs meet the standards that will be required by the DWP."

There is no doubt that after a challenging 2021, trustees will be kept on their toes throughout 2022 also, needing to pay close attention to new regulations and new expectations.

Written by Andy Knaggs, a freelance journalist

Responsible investing

"Discussions on how pension schemes can support the drive to tackle climate change have resulted in several consultation papers being published and more are expected over 2022. In the next 12 months, schemes will continue to monitor these carefully to understand the impact any changes might have on them, as well as putting in place procedures and policies to tackle these."

APPT Chair, Harus Rai

"One of the most significant new responsibilities for trustees will be the extension of Taskforce for Climate-Related Financial Disclosures (TCFD) reporting. From October, schemes with assets over £1 billion will be required to comply, and smaller schemes will also need to start preparations for when these new duties are cascaded further."

Pensions Management Institute director of policy and external affairs, Tim Middleton

For professional investors

Diversified private markets: Sustainability+?

Trustees face increasing pressure to conform with ever-changing ESG and climate reporting requirements and demand from members. Consequently, DB and DC schemes embrace ESG-aligned benchmarks with enthusiasm, but does investing via low carbon indices go far enough?

The International Energy Agency (IEA) has highlighted the need for $4 trillion annual investment by 2030 to facilitate the clean energy transition and meet the global aspiration for net-zero emissions by 2050. Is there therefore a case for trustees to consider making explicit allocations to climate change related investments beyond simple low carbon passive solutions? The MSCI ACWI Low Carbon Leaders Index (in US$ terms) returned 16.5 per cent in 2020 versus 16.3 per cent for the MSCI ACWI Index. Over the same period BNPP AM's active Energy Transition Fund net of fees returned 164.6 per cent (in € terms) versus 6.7 per cent for the MSCI ACWI Index. Allocating capital to ESG and climate aligned thematics can add genuine value for members and more explicitly direct capital to climate change investments.

Whilst such approaches offer the opportunity to capture what will be a multi-decade trend in equity markets some investors are wary of the volatility associated with equity investments so are there alternatives for trustees seeking to better align portfolios to the Paris Agreement?

Negative real yields, negative cashflows, pressure to diversify risk exposures, funding ratio/price volatility, a focus on costs and changing investment regulations are additional pressures that trustees face when considering investment strategy. These make holding listed equities harder, while low bond yields add to the challenge of sourcing adequate real returns. In this context, one way to improve the risk/return and climate profile of institutional portfolios is to capture illiquidity premiums by investing in diversified private debt and private equity portfolios that also directly finance the creation of green assets, aligned to the Paris Agreement.

The challenge

Many institutional investors have shunned the volatility associated with listed equities and have simply invested in other asset classes. For example, defined benefit pension funds have been steadily moving out of traditional listed equities and into fixed income, index-linked and corporate bonds over the years. By 2020, their equity allocation stood at less than 20 per cent *[Pension Protection Fund, Purple Book, 2021]*.

As an alternative, many institutional investors started investing in UK gilts and listed high-quality corporate bonds. However, their nominal yields have steadily fallen over the past 20 years (with the exception of 2008/2009 during the height of the global financial crisis). Consequently, for the past few years, real yields have been either low or negative (depending on their maturity).

The solution

Private markets can be an attractive substitute to listed equities and bonds, particularly when combined to form diversified portfolios and allow schemes to own directly assets that are linked to the energy transition.

- **Private equity** (PE) is defined as capital invested in companies that are not publicly traded. This asset class includes traditional leveraged buyouts and venture capital (VC) as well as infrastructure (infra) equity and direct real estate (RE) investments.
- **Private debt or credit** is defined as capital invested in the debt of private companies. Private debt is not traded or issued in an open market. It generally includes asset classes such as corporate lending (to SME and mid-market companies), real assets such as infrastructure debt and commercial real estate (CRE) debt.

Whilst offering lower immediate liquidity (as most of these assets are valued once a month or once a quarter and are usually held to maturity) private debt and equity may offer a number of advantages over their listed equivalents.

- Higher returns, captured through an illiquidity premium.
- Lower volatility and a lower market beta.
- Potentially more targeted environmental, social and governance (ESG) oriented investments (based, for example, online by-line selection of well defined green, sustainable and social projects).

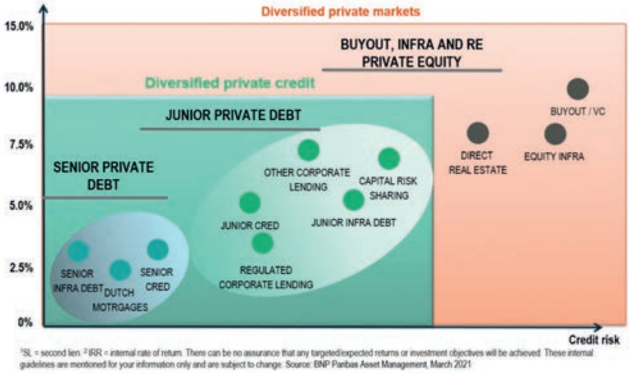
The investment universe

Chart one provides an overview of the investment universe encompassing diversified private credit and equity:

Strategies for investing in private credit and debt

In practice, asset managers have developed different types of investment strategies to meet investors' objectives

Chart one



Source: BNPP AM, November 2021

when entering the private credit and private debt universe:

• **Diversified private credit** strategies generally aim to incorporate various types of real asset debt and corporate lending with some structured finance sub-asset classes and to capture a credit illiquidity premium. They offer a blend of senior and mezzanine investments, countries, currencies, credit ratings and liquidity. They can be structured as cashflow matching portfolios and can be suitable for mature defined benefit pension schemes (cashflow negative with a large majority of retirees).

• **Diversified private markets** strategies add exposures to private equity, direct real estate and infrastructure equity to a diversified private credit portfolio. They aim to capture a blended illiquidity premium. They are structured as alternative growth engines and are suitable for defined benefit pension schemes with active members and defined contribution pension plans with long time-horizons. They typically offer higher expected returns with lower volatility levels than their listed counterparts.

Because of their nature, these strategies are customised to individual client needs with varying features:

• The investment universe can be narrow (for example, focused on corporate lending) or wide (including semi-liquid asset classes such as leveraged loans).

• Fund design – they can be open-ended or close-ended, unitised as a Luxembourg RAIF or a UK-based LP.

• The strategic asset allocation (SAA) can be directive or just indicative, with loosely set ranges allowing for active asset allocation over time.

• They can be evergreen or established only for a pre-determined amount of time.

• They can rely on a fund-of-funds structure or include only single-line investments.

• Diversified private credit and private market strategies can be structured as bundled solutions with streamlined custody, depositary, fund and loan administration services. This helps avoid the complexity of managing multiple illiquid mandates and funds with different service providers. Many institutional investors that pursue a diversified approach are struggling to efficiently manage the complex capital call schedules, as well as principal and interest payments.

For all these reasons, diversified private credit or private market approaches have advantages over investing in single asset classes as well as over listed asset classes.

Other benefits

Beyond the much improved risk/return profile that can be obtained at the portfolio level by combining different private debt and private equity sub-asset classes, it is worth noting that there are other important benefits.

Relative value based asset allocation can be achieved across the investment universe. Depending on the manager and the investment vehicle, the solutions also benefit from holistic risk, liquidity and cash management by a single team, ensuring consistency and coherence.

Diversified private debt and private market solutions have established strict governance arrangements that enhance the flexibility of the SAA and allow for innovation and nimble assessment of investment opportunities as they appear. For example, an annual or semi-annual investment committee meeting can be convened to assess new asset classes, eg credit risk sharing, as they arise or full discretion can be afforded to the asset manager.

Crucially in the context of the pressures faced by trustees, ESG and climate change considerations can be embedded in the private debt and equity transaction filtering and selection process. This provides investors with greater confidence in the quality of their investment portfolios, and a better alignment with pension scheme members beyond passive index or active thematic equity options.

Written by BNP Paribas Asset Management's Phil Dawes, Global Head of Consultant Relations and Head of Sales (UK & Ireland), and Julien Halfon, Head of Pension and Corporate Solutions

The compelling ESG case for bulk annuities

As the global economy pivots to net zero, long-term investing has become yet more challenging. Scale matters – and Aviva, a whole of market de-risking provider – can help schemes of all sizes achieve long-term sustainable outcomes

The traditional arguments for pooling the resources of defined benefit (DB) pension schemes through bulk annuity deals have been economic – lower costs and reduced risk. But the rapid acceleration of ESG investing is bringing a whole new set of reasons.

The old economic arguments are not undermined — indeed, they are more vital than ever. But they are now reinforced with additional reasons that go to the heart of a pension scheme's purpose.

Aviva's annuity asset origination director, Marcus Mollan, says that only the largest and most sophisticated institutional investors can most efficiently finance the innovative transactions that deliver long-term attractive cash flows while helping to decarbonise the economy.

He says the large number of small DB schemes "face challenges in terms of efficient investment, and in terms of the value that can be created from investing those assets from the viewpoint of society".

These goals, he says, are complementary. With time horizons that may extend decades, he says it is vital that investments must take into consideration the changes in both climate and regulation that may happen a long way into the future.

Aggregation of smaller DB scheme assets into the bulk annuity portfolio of a large insurer such as Aviva means "those assets can be invested more efficiently. We can bring much greater firepower to bear when making investment decisions".

Innovation in action

As an example of the complexities of these new investments, Mollan points to the recent innovative deal made by the Aviva annuity business and Aviva Investors with the UK's largest port operator, Associated British Ports, and BNP Paribas. This swap transaction sees the port operator get a discount to its borrowing rate provided it meets certain ESG performance measures, including significantly cutting carbon emissions (both its own and those of direct suppliers) by 2030.

ABP is already one of the UK's largest corporate solar energy producers; the deal gives it a clear financial incentive to continue its aggressive carbon reduction campaign. For Aviva Investors, Aviva's asset management arm, the transaction delivers what head of structured and private debt, Munawer Shafi, described as "tailored sustainability considerations, without compromising on outcomes for borrowers or risk-adjusted returns for our clients".

Mollan comments: "Not even all insurance companies have the ability to do that sort of transaction, and most pension schemes find it even harder."

Mollan gives insights into the complexity of Aviva's investment process in the ESG era. For annuities, the insurance firm invests almost exclusively in investment-grade assets with contractual cash flows. Conventional investment thinking would label these as "very safe" — but with investment horizons in decades it is vital to assess the risk that climate change poses. This can be a physical risk, such as a property investment at risk from extreme weather, or regulatory risk as governments apply sticks and carrots to drive down carbon emissions.

Decarbonisation targets
Aviva has set itself challenging targets for decarbonising its portfolio: not only net zero by 2040 but intermediate targets that are tougher than that required by the Paris Agreement, such as a 60 per cent cut by 2030. These may seem distant, but many of the investments Aviva makes today will still be in the portfolio at that date. Action is needed today.

With investment at scale, it is possible to create frameworks that deliver across multiple investments. For example, Aviva Investors has committed to achieving net zero across its entire Real Assets platform by 2040, which represents approximately £50 billion of assets. This includes developing a proprietary framework for sustainability-linked real estate loans that encourages borrowers to achieve key sustainability targets such as gains in energy efficiency and installation of on-site renewables. The programme, which aims to originate at least £1 billion of loans by 2025, most recently provided £200 million of refinancing to Primary Health Properties plc on behalf of Aviva's annuity business.

Large organisations also have the resources to participate in global initiatives. Aviva, for instance, is a signatory to the United Nations-backed Principles for Responsible Investment, the Finance for Biodiversity Pledge, the Powering Past Coal Alliance, and many other organisations. Such initiatives bring transparency and reassure those who have a pension pot invested with the firm that it is being managed responsibly.

Nuanced decisions are often needed. For example, natural gas is a cleaner fuel than coal, meaning that some gas investments are allowed in the portfolio, but Aviva still needs to undertake a careful evaluation to balance the merits of any such transaction. Aviva has rejected some transactions due to concerns about the risk of methane leakage, since methane is a potent greenhouse gas.

Clearly, energy investing in the current environment requires deep expertise. Mollan says that with long investment horizons, all investments need scrutiny. Climate change will affect whole economies; even government bonds need to be considered through an ESG lens. "Pretty much every long-term investment that we make now, which is pretty much every investment that we make, needs an ESG assessment," he says.

Meaningful engagement
Stewardship is another task that is more effectively done at scale. Engagement not only helps manage risk, but it can also drive investment performance. Aviva can point to many success stories of engaging through its in-house asset manager, Aviva Investors, using its voice to deliver positive change at the companies it invests in. As an active investor, having scale improves the level of influence in being able to build a better and more sustainable future. The alternative is divestment, but doing this means they lose their voice as an investor. Staying invested in a company and speaking up on key issues and resolutions as a shareholder arguably makes more of a difference than walking away, although it is also important to be prepared to divest when an engagement programme has not delivered the results that were hoped for.

The Pension Protection Fund's (PPF) *Purple Book 2021*, the most recent version of the industry's authoritative factbook, estimates the number of DB schemes eligible for PPF protection at 5,220 as of 31 March 2021.

"Some may have in-house investment professionals or large, efficient mandates with external managers," says Mollan. "So they could, in principle, do some of this activity. But the vast majority of those 5,000-plus pension schemes couldn't do it themselves —and there would be significant overheads to them paying an investment manager to do it."

Drill down into the *Purple Book* data, and the lack of scale becomes clearer still. Although giant schemes such as the BT Pension Scheme with its 280,000-plus members get the most attention, they are atypical. 80 per cent of schemes have less than 1,000 members. And 36 per cent of schemes are tiny, with less than 100 members.

Mollan says: "Each of those has their own management structure, their own set of trustees, and in many cases, they're investing, usually with advice from professionals, on their own account. I think that's an inherent inefficiency in the way that pension assets of working people are invested in smaller schemes."

Even before interest in ESG accelerated, smaller schemes were feeling the strain. Managing funding constraints is only one of their many challenges – the constant shift in regulation, keeping down costs, trustee recruitment and training – the overall picture is daunting!

But the real problem, is that small schemes may find it increasingly challenging to access investments that potentially offer higher returns and the new era of ESG and sustainable investing could exacerbate the matter.

There is also the bigger picture to consider. Although mindful of returns, there is a belief that scheme members want their pension savings to work building a better, greener world for future generations.

Mollan says that funds locked up in smaller schemes may struggle to do that: "Those assets can be invested in a more efficient way." If moved under the control of an insurer via bulk annuity transactions, "we can bring significant scale and expertise to the investment decisions we make and the industries we are able to finance from those assets".

Aviva director, annuity asset origination, Marcus Mollan

Better outcomes

Jonathan Watts-Lay considers how to improve retirement outcomes in the year ahead and beyond

The pandemic has clearly affected people's retirement plans in different ways. We carried out research into this and found that more than a fifth (22 per cent) of workers approaching retirement (age 50+) say it made them want to retire earlier and as soon as they can. Conversely, 13 per cent wanted to delay retirement because they realised they enjoy working. However, just over one in 10 (11 per cent) said that they've had to delay retirement as they can no longer afford to. A study by Fidelity suggests 38 per cent of people will put back retirement by around two and a half years.

Whilst this uncertainty can make retirement planning very challenging, what is clear is that pension scheme members are going to need more support than ever as they prepare how to take their retirement income. After all, a report that we produced with the Pensions Management Institute indicated that trustees have great concerns for their members in the run up to their retirement, and it's easy to see why.

Tax implications

In particular, the research found that nine out of 10 trustees (89 per cent) worry that their members will not understand the tax implications of accessing their pension. This may be because members don't necessarily realise the multiple tax considerations to be aware of.

For example, the Financial Conduct Authority (FCA) recently revealed in its *Retirement income market data 2020/21* that 341,404 pots were fully withdrawn in 2020/21. Whilst 108,869 of these were worth less than £10,000, 1,499 people fully withdrew pots worth more than £100,000. Unfortunately, this could mean that many will be paying more tax than needed, ultimately resulting in less income in retirement than what could have otherwise been achieved.

Making retirement savings last

Another concern identified by our survey was that six out of 10 (60 per cent) trustees fear their members will run out of money too soon in retirement. Withdrawal rates could be part of the problem and the FCA's data shows that many retirees continue to draw down their pots at rates of 8 per cent and over.

For example, 43 per cent of regular withdrawals were made at an annual rate of 8 per cent or more of the pot value in 2020/21, up from 42 per cent in 2019/20. Not only this, even fewer took advice than a year earlier. This could be a very risky strategy with many retirees finding themselves running out of money sooner than expected.

Coupled with this, many people live longer than they expect, and so members may underestimate how long they think their savings need to last. For example, The Institute for Fiscal Studies found that those in their 50s and 60s underestimate their chances of survival to age 75 by around 20 per cent, and to 85 by around 5 per cent to 10 per cent. This raises questions around not only what decisions members make at the point of retirement but also the future decisions as they progress through retirement.

Pension scams

Our survey also found that nearly all (94 per cent) of trustees are concerned about their members being scammed out of their savings. This is not surprising when we consider that more than £2 million has been reportedly lost to pension scammers between January and May 2021, according to Action Fraud. It also stated that during this period average losses totalled almost £51,000 which is more than double the average in 2020 (£23,689).

The new regulations that came into force in November, giving trustees and scheme managers the power to intervene and stop suspicious transfers, are really good news for pension savers and an important defence against scammers. However, whilst it might be an effective measure to help prevent pension transfer scams, there is still the issue of members needing a clear understanding of whether the pension transfer they are planning to make is suitable.

Furthermore, it's noteworthy that whilst The Pensions Regulator recognises that not every pension scam can be prevented, it does ask trustees, providers and administrators to pledge to do more to protect scheme members and follow the principles of the Pension Scams Industry Group Code of Good Practice, which is based on three key principles, including raising awareness of pension scams for members and beneficiaries, having robust processes for assessing whether a scheme may be operating as part of a scam, and being aware of the known current scam strategies.

DB pension transfers

The FCA's latest retirement income market data shows that there were over 30,000 defined benefit (DB) to defined contribution (DC) transfers during 2020/21. Our survey found that this is an area of great concern for trustees, with 80 per cent of them having worries about members not understanding the risks around transferring out. This isn't surprising given that XPS Pension Group reported that in November 2021, half of prospective transfers showed one or more warning signs of a potential scam or likelihood of poor member outcomes. Ensuring access to appropriate advice is key, which is of course a requirement for anyone looking to transfer a DB scheme over the value of £30,000.

What role do employers and trustees play?

Trustees and employers play a key role in ensuring members make informed choices concerning their pensions. This includes providing financial education and guidance as it can help members understand their options and what red flags to look out for. It can also help them to decide if they would like further support such as regulated financial advice.

There is currently no legal obligation to provide access to regulated financial advice to members and for a long time there has been a concern that it carries risk. However, a discussion paper from Eversheds Sutherland and Royal London suggests that this theory only looks at 'the risk of doing something and not at the risk of doing nothing'. It highlights that simply referring members to a list of advisers for them to choose from can lead to significantly poor member outcomes and therefore member distrust. In some cases, this can result in reputational damage as seen with British Steel.

It seems that this way of thinking is now becoming common place as on a positive note, our survey found that retirement support provision is on the up, with 49 per cent of trustees providing financial education (3 per cent in 2019), 46 per cent providing financial guidance (28 per cent in 2019) and 3 per cent providing facilitation to regulated advice for members at retirement (21 per cent in 2019).

Carrying out due diligence on providers can make the process far more robust. This should include checking that any financial education and guidance providers are workplace specialists with experience in providing support to members. This can help members understand key issues at retirement such as tax implications, risks around DB transfers and how to spot a pension scam. Due diligence on regulated advice firms should cover areas such as qualifications of advisers, the regulatory record of the firm, compliance process eg compliance checks on 100 per cent of cases, pricing structure, and experience of working with employers and trustees. The responsibility for the regulated financial advice given to members, and the consequences of that, will then rest with the chosen provider and not the trustee or employer.

Retirement planning is a specialist topic that many understandably don't have the skillset for. Ultimately, ensuring robust processes and providing members with access to appropriate support before they access their pensions, will lead to better outcomes for all in the year ahead and beyond.

Written by Wealth at Work director, Jonathan Watts-Lay

In association with

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The need to plan

If retirement planning brings lots of benefits, why are many of us still not doing it?

Planning can make a hugely positive difference to retirement outcomes. Yet most people are not planning enough.

Planners generally expect to retire earlier, enjoy retirement more, expect their money to last for longer and are more confident making financial decisions.

These findings are from Standard Life's *Consumer Attitudes Report, Bringing retirement into focus: 2021*, which surveyed around 5,000 people in the UK in August 2021.[1]

Almost three-quarters (73 per cent) of people say they're doing little or no planning to understand the amount of money they'll need to live on in retirement. And 29 per cent of people say they have done no planning.

Women, Gen Xers and low-affluence participants are among the least likely to plan for their long-term financial futures.

Even between the ages of 50 and 59, 17 per cent of people maintain they only need to think about retirement planning when they get older. It is clear that despite the benefits of planning, barriers exist.

This naturally raises the question: how can we encourage employees – irrespective of their income, wealth, gender or socioeconomic status – to plan more for their retirement?

Articulating the power of planning

It is vital to articulate better the benefits of retirement planning and then give employees the tools and confidence to plan properly. The following three steps may help:

1) Understand your workforce

People all have different needs and aspirations. Age, gender and socioeconomic position can play a role in how people approach financial planning. It's vital to understand how these factors affect a person's confidence in their knowledge of pensions, their expectation and experience of retirement.

Conducting a detailed segmentation analysis can provide a more granular understanding of your workforce, thereby allowing you to cater more effectively for different employee needs.

2) Tailor communications according to different employee needs

Better targeting of existing educational material such as milestone communications, webinars and pension and retirement calculators can help kickstart the engagement that can lead to more planning and better outcomes.

The PLSA's recently updated Retirement Living Standards (Standards) can help to make communications more relatable, by helping people to picture the lifestyle they want when they retire and understand the cost.

The Standards, based on independent research by Loughborough University, are pitched at three different levels – minimum, moderate and comfortable. They include a series of examples, which show what kind of living standard different people could have in retirement depending on their salaries, household and savings.

3) Help employees to make informed decisions in the build-up to retirement

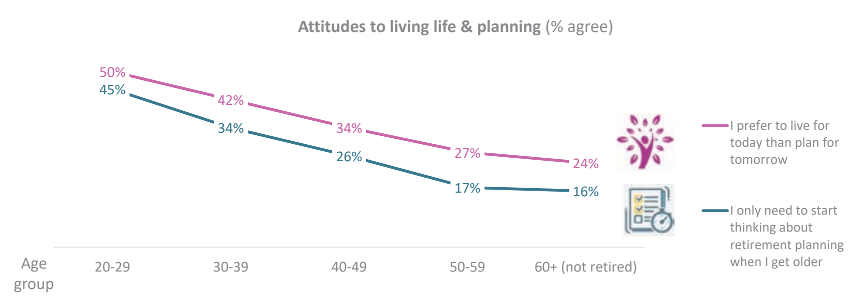
Of course, the more holistic one's financial planning, the better. Retirement planning should consider more than just pensions, and include any debts, expenses, or other sources of income, as well as particular needs employees may have.

Being mindful of employees' short-, medium- and long-term needs – and how these may vary – could help employees to engage more with long-term savings and planning.

At Standard Life we have expanded what we offer this year by trialling a number of engagement and planning tools, including the Homebuyer Hub, introducing an online coaching app to help people plan how to save for their first home, and Money Mindset, an open finance platform.

We will also be developing our guidance proposition and introducing MOTs. By helping people to feel confident and empowered to make financial decisions across all life stages, we can help to build trust and engagement with their retirement savings.

Figure 1: Many people put off planning for retirement – well into their 40s.



Written by Standard Life head of proposition deployment, Donna Walsh

In association with Standard Life

[1] In August 2021, Standard Life commissioned an independent online survey of nearly 5,000 people from around the UK. We supplemented this with focus groups to explore issues coming out of the survey in more depth. The research looked to cover a broadly representative sample of UK adults aged 18 to 80-plus, covering a range by income, savings, region, gender, ethnicity and other key attributes.

Net zero through fiduciary management

Sophie Dapin explores transitioning to net zero through fiduciary management

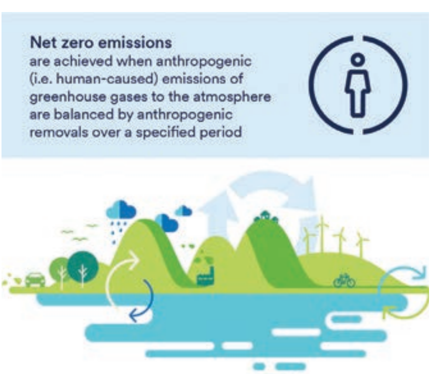
This year, we have seen a flurry of governments, companies and pension schemes the world over announcing net-zero carbon targets. These targets play a crucial role in global efforts to limit warming in alignment with the goals of the Paris Agreement.

But it is not just the Paris Agreement and the 2021 COP 26 climate summit that have sped up the race to net zero when it comes to UK pensions.

It is increasingly recognised that UK pension schemes need to ensure their portfolios are positioned both for the risks and the opportunities ahead while, at the same time, complying with an increasing amount of regulation.

The term 'net zero' gets discussed all the time, but what does it really mean? Here's how the Intergovernmental Panel on Climate Change (IPCC) defines it[1]:

Net zero emissions



For a pension scheme to achieve this, the aggregate emissions across all its underlying portfolios need to achieve this.

We will now explain why trustees should care, actions to take and how fiduciary management addresses key challenges.

Why should pension scheme trustees care?

Climate change will be a defining driver of the global economy, society and markets. All investors, including pension schemes, won't be able to avoid its impacts and accompanying risks to investment portfolios.

Trustees must ensure sure that when reallocating from fossil fuels to low carbon, portfolios tilt towards the likely winners from the climate transition and avoid the worst losers.

Crucially, as well as risks there are also opportunities. Pension schemes have significant influence over the flow of investments in the economy and are well placed to invest in opportunities that will lead towards a lower-carbon economy.

Regulation is also key in the drive towards net zero for pension schemes. Recently, the UK became the first major economy to ensure pension funds are legally required to report on the risks of climate change within their portfolios. Schemes over £1 billion will report in line with the Task Force on Climate-Related Financial Disclosures (TCFD).

Part of this regulation is the 'metrics and targets' requirement. The Pensions Regulator has given examples of targets a scheme may consider in its guidance and some are explicitly related to carbon reduction. For example, one target they suggest is to "reduce their carbon intensity by 15 per cent by 2023 and align with their decarbonisation trajectory up to 2030"[2].

Although encouraging schemes to set decarbonisation targets is helpful, there are risks involved. For example, indiscriminately adopting this approach can lead to overvalued securities like those from the dot com bubble, with potential for a strong market correction occurring. The technology, media and telecom sectors have changed the world, but not before significantly impairing value for investors.

What should pension scheme trustees do?

The first step is to ask the right questions. Before embarking on this journey, trustees need to build their own capabilities and ensure that their providers can demonstrate 'climate competency'. Trustees need to be confident that those providing advice to the scheme have the knowledge and expertise to manage climate-related risks and opportunities.

An investment-led fiduciary management approach can provide significant efficiencies for trustees. With the fiduciary manager directly responsible for the engagement with underlying companies and their emissions targets, compared to having a separate adviser and asset manager, this provides a direct link to those underlying companies.

There are three key questions that trustees should ask their providers:

Three key questions for trustees

Stopping at 'what are the emissions of the portfolio today?' and focusing only on minimising today's emissions is a risk. This could encourage behaviours that lead to overly-concentrated portfolios in certain sectors. It also risks missing out on the bigger picture.

It is crucial for pension schemes to focus on the journey to net zero, rather than solely focusing on being net zero today.

If you move the portfolio too early there are diversification challenges given the current small pool of companies with credible net zero plans. However, if you move too late, there are risks to the value of the assets the scheme invests in.

How might a fiduciary arrangement approach help?

A fiduciary management approach provides significant benefits regarding net-zero targets. It delivers these benefits across three key areas:

1- Effecting real change

Setting a net-zero target should not just focus on changing a portfolio to improve current scores. This is about engaging with companies to improve the portfolio by effecting change to the real economy. Simply divesting from some carbon-intensive companies and passing them on to another buyer won't suffice.

Pension scheme trustees are in a unique position to bring about this kind of change if they put their assets to good use under an effective stewardship programme. For example, Schroders have written to the leaders of UK FTSE 350 companies, calling on them to prepare and publish their plans for decarbonisation. We are then able to track progress across the market.

2- Data

It is not a straightforward task to collect, process, understand and report on the data needed to form a full picture of your portfolio's net-zero status.

Today's carbon emissions and intensity data form a good starting point for analysis, but are backwards looking and far from the whole picture.

We have invested heavily in our proprietary research and tools to deal with data challenges. This helps our fund managers across asset classes to better understand the risks climate change poses to investments and to integrate this into their investment decision-making.

3- Applications across different asset classes

Understanding the application of net zero across different asset classes is an immense challenge for pension schemes. Company emissions data is more mature for listed equities and bonds,. Pension schemes typically have high allocations to alternative asset classes where this methodology is less well developed.

Recognising this, the Institutional Investors Group for Climate Change have produced a Net Zero Investment Framework [3]. This is a useful tool for pension schemes and currently covers how to approach net-zero investments in listed equities, corporate and sovereign bonds and real estate.

Our closeness to the underlying data and integrated approach means we are able to consistently apply this framework across our fiduciary management client portfolios.

Conclusion

Transitioning in a few decades from a global carbon-powered energy system, built up over hundreds of years, to one that is carbon-free, will require significant and rapid transformation to the global economy. Pension scheme trustees need to be prepared for the impact on their portfolios.

Having the right governance structure in place to deal with this is crucial. There are significant benefits to an integrated and investment-led fiduciary management approach.

Written by Schroders fiduciary manager, Sophie Dapin

In association with Schroders

[1] https://www.ipcc.ch/sr15/chapter/glossary/
[2] https://www.thepensionsregulator.gov.uk/en/document-library/consultations/climate-change-guidance/guidance/targets
[3] https://www.iigcc.org/resource/net-zero-investment-framework-implementation-guide/

Company Profiles

BNP Paribas Asset Management

BNP Paribas Asset Management (BNPP AM) is the investment arm of BNP Paribas, a leading banking group in Europe with international reach. BNPP AM aims to generate long-term sustainable investment returns for its clients, based on a unique sustainability-driven philosophy. BNPP AM's investment capabilities are focused around five key strategies: High Conviction Strategies, Private Debt & Real Assets, Multi-Asset, Quantitative & Solutions (MAQS), Emerging markets and Liquidity Solutions, with investment processes incorporating quantitative and fundamental analysis. Sustainability is embedded within BNPP AM's strategy and investment decision-making. Among the leaders in thematic investment in Europe, BNPP AM contributes to the energy transition, environmental sustainability and the promotion of equality and inclusive growth. BNPP AM currently manages EUR 502 billion of assets and benefits from the expertise of around 500 investment professionals and over 400 client servicing specialists, serving individual, corporate and institutional clients in 69 countries.

Source: BNPP AM, as at 30 September 2021

Aviva

Aviva Plc is a savings, retirement and insurance business, with a heritage stretching back over 325 years. It's one the UK's leading insurers and the largest corporate pension provider, with almost £90 billion of pension scheme assets under management. Aviva is the UK's number one individual annuity provider and has £70 billion of annuity assets. Aviva has a long track record in promoting sustainability and is one of the first major insurer worldwide to target net-zero carbon emissions by 2040.

Aviva has a strong balance sheet with a Solvency II cover ratio more than twice the regulatory requirement (Q3 2021). Our financial strength is demonstrated by our ratings AA- (Stable) by Standard & Poor's, AA- (Stable) by Fitch, and Aa3 (Stable) by Moody's (Q3 2021).

Defined benefit solutions from Aviva

It takes financial confidence to provide the certainty employers need in an uncertain world. And it takes the scale and expertise of one of the UK's leading insurers to deliver the defined benefit solutions that help safeguard the interest of your members. This is where Aviva can help.

With over 15 years in the market, our dedicated team has completed more than 600 transactions for schemes of all sizes.

Your members will be able to speak to defined benefit experts from our in-house teams whenever they need to contact us. We've been looking after customers for more than 325 years, making sure we're here when they need us most.

Whether you want to protect your members or reduce your liability, Aviva can help you find the best solution for your defined benefit pension plan.

WEALTH at work

WEALTH at work is a leading financial wellbeing and retirement specialist – helping those in the workplace to improve their financial future.

Established in 2005, we work with hundreds of organisations across both the private and public sector by offering financial education, guidance and regulated financial advice.

Our financial education and guidance services are delivered on a bespoke basis and can be specifically designed to help the entire workforce make informed decisions about their finances.

For example; financial education services cover everything from debt and money management through to optimising employer sponsored benefits and retirement. This can be delivered face-to-face or online and utilises digital nudge technology to encourage employee engagement and participation. A telephone helpline is also provided following this.

Support is also provided through the creation of digital content such as webcasts, animations and interactive tools including the Financial Healthcheck.

All our interactions are measured and can be benchmarked against the industry standard to fully understand the impact. This is of particular importance when meeting financial wellbeing objectives.

Financial guidance services provide one-to-one support on a range of financial subjects which can be accessed face-to-face, via telephone or a virtual call.

As well as this, we provide regulated financial advice supporting those who need specific recommendations regarding their savings and investments, including those who need to make important decisions about their retirement income options. This service also supports those in retirement who may need to adapt their retirement planning in line with their changing needs.

In addition, we also have broad experience in a number of specific projects where we support employees in financial decision making, including; defined benefit pension closures; the introduction of pension changes such as the implementation of a new scheme, share scheme programmes and offering financial helplines to EAP providers. Our services also cover specialist topics including; lifetime allowance, annual allowance and help with redundancy plans.

WEALTH at work
KNOWLEDGE | EXPERIENCE | OPPORTUNITY

Standard Life

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Standard Life is part of Phoenix Group, the largest long-term savings and retirement business in the UK. We're proud to be building on nearly 200 years of Standard Life heritage together.

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Standard Life

Company Profiles

Schroders

At Schroders, our purpose is to provide excellent investment performance to our clients through active management. By serving clients, we serve wider society. Channelling capital into sustainable and durable businesses accelerates positive change in the world. Funding the future is a privilege; we use it wisely and responsibly.

For our UK pension scheme clients, we bring more than 60 years of experience in managing pension assets and liabilities. Through a combination of specialist investment expertise and dedicated Fiduciary Management and Portfolio Solutions capability, our focus is on partnering with our clients to fully understand their position and assist in achieving their objectives. Our clients draw on a wide range of Schroders investment capabilities, including multi-asset, global equities and fixed income that sit alongside £50 billion of specialist expertise across private assets and alternatives delivered through Schroders Capital, our private market division.

Our Portfolio Solutions capability is dedicated to investment strategy and risk management, focussing on working with clients to structure and design outcome-orientated portfolios, including fiduciary management, LDI and cashflow- driven Investment strategies. With approximately £70 billion in UK pension fund assets under management, we offer size, breadth of capability, global reach and over 200 years of investment experience.

Schroders

Pensions Age

Pensions Age is the leading title targeting those managing UK pension funds and their consultants. Published monthly in print since 1996, and daily online, we invest heavily in our circulation and content to ensure we are the clear market leading title. Our in-house editorial team of Francesca Fabrizi (Editor in Chief), Laura Blows (Editor), Natalie Tuck (Associate Editor), Jack Gray (News Editor), and reporters Sophie Smith and Tom Dunstan, ensure we cover the latest news and topical industry issues to help our readers make the best-informed decisions.

www.pensionsage.com is the leading website for pension funds and we look to cover the breaking stories as they happen. With over 24,000 subscribers to our email newsletter service, we offer our readers an unrivalled service. At the core of this is high-quality, news-breaking journalism, combined with in-depth knowledge of the target market and heavy research into data.

Pensions Age also runs highly successful conferences, and the Pensions Age Awards.

We also publish *European Pensions*, which targets pensions funds across Europe, as well as running the European Pensions Awards and Irish Pensions Awards.

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