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representing pension savers



IAPF TRUSTEE NETWORK EVENT

Pension Investment – are you being responsible?

Tuesday 3 December 2019

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John Griffith
Council Member, IAPF

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Pension Investment – are you being responsible?



What is Responsible Investment?

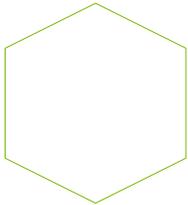


Responsible investment is an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions, to **better manage risk** and **generate sustainable, long-term returns**.



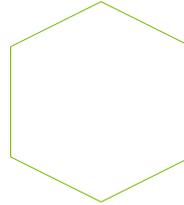
What does it mean to invest responsibly?

Some combination of....



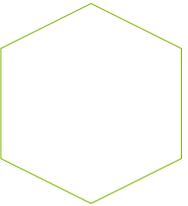
Exclusion

Avoiding investment in companies or sectors due to product or conduct based views



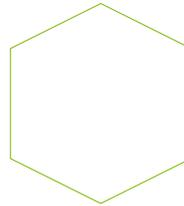
Integration of ESG considerations

Incorporating of wider set of factors in decision making to improve portfolio risk and return



Impact

Achieving specific non-financial outcomes linked to theme or mission

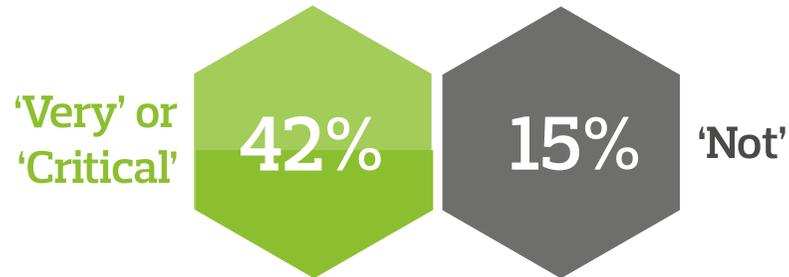


Engagement

Actively seeking to influence change through invested companies or assets

Changing global attitudes to responsible investment

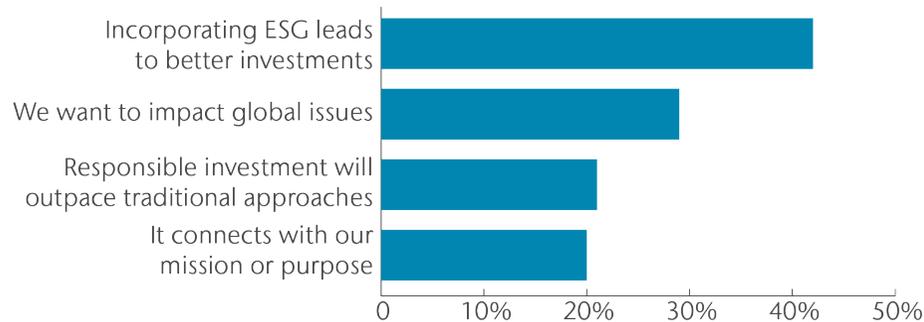
Is responsible investment important?



Does responsible investment impact manager selection?

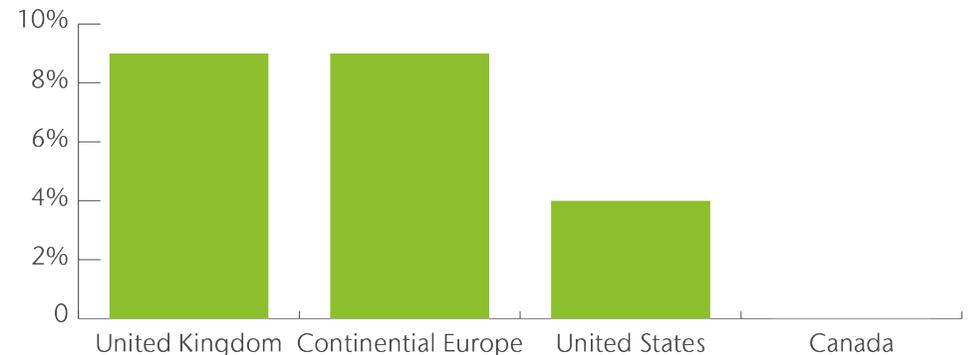


Why do responsible investing?



Source: Aon – Global perspectives on responsible investing 2019

Would you sack an outperforming manager who wasn’t living up to expectations on responsible investment...?



What is driving discussions on Responsible Investment?



In the UK: increasing regulatory and industry expectations



**The Pensions
Regulator**
issues ESG guidance

**Environmental Audit
Select Committee**
writes to top
25 DB schemes

**Department for Work
and Pensions**
issues new regulations
for pension trustees

Minister for Pensions
writes to top 40 pension
schemes

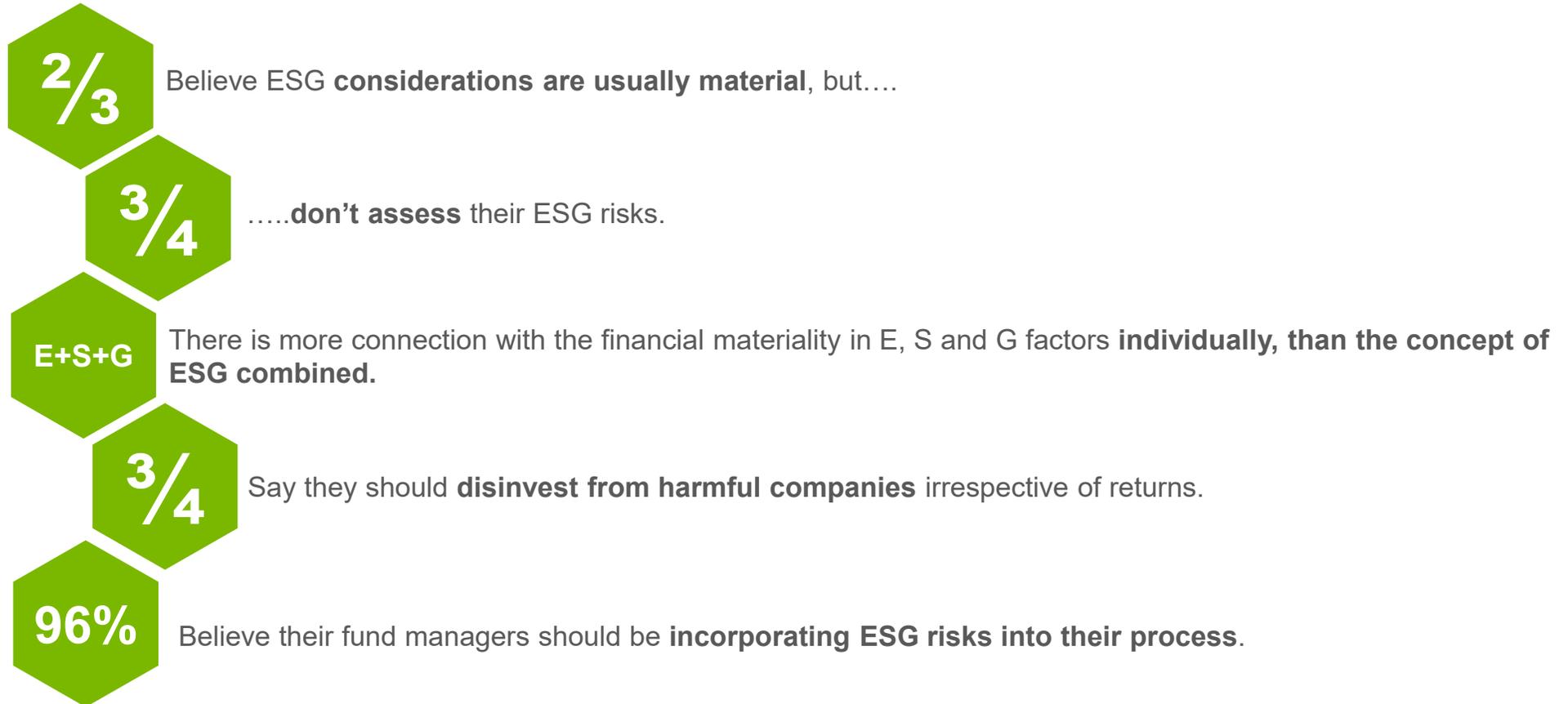
In the UK: implementation of EU Directives



- Financial and non-financial matters
- Stewardship and engagement
- Fund manager relationships
- Monitoring costs, performance & remuneration

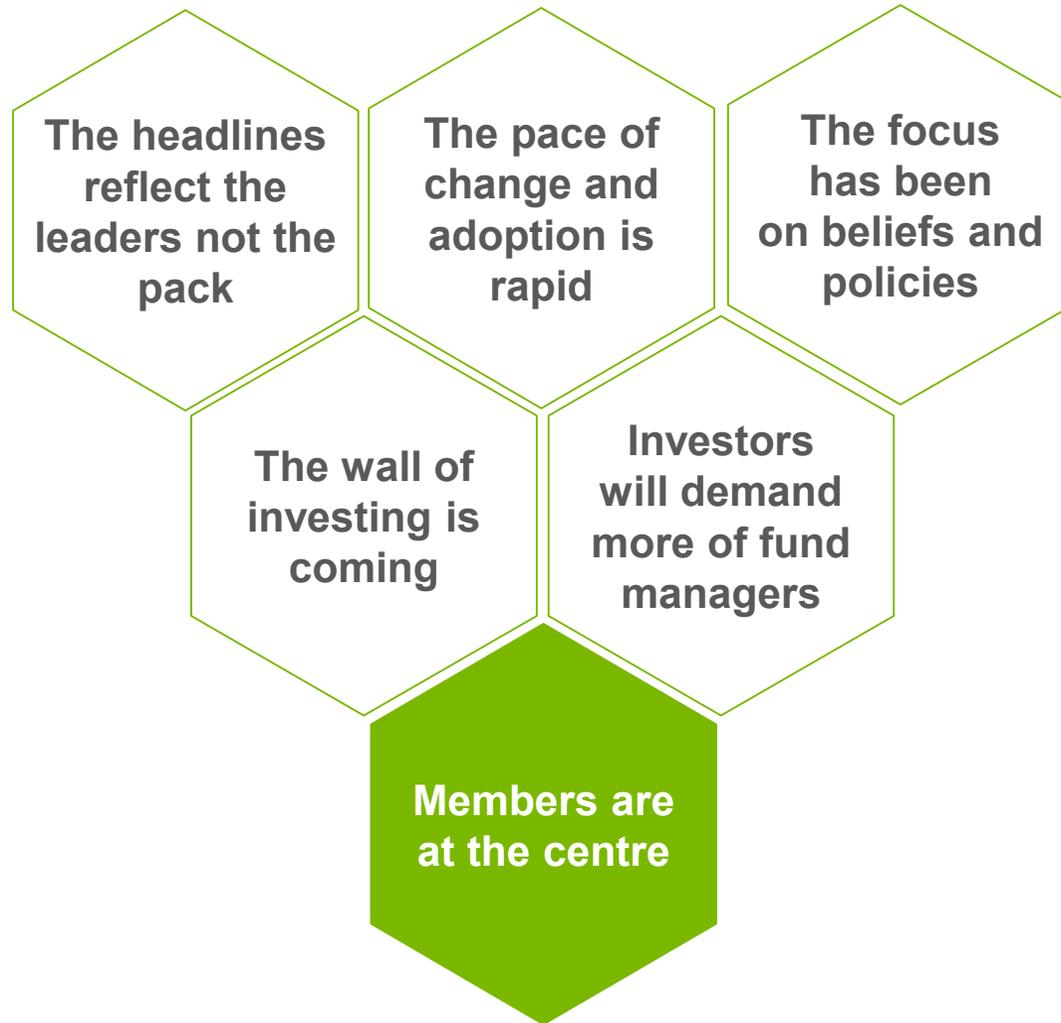
- Statement of Investment Principles
- Implementation Statement (DC)
- Engagement Policy Implementation Statement (DB)

In the UK: discussions and developments



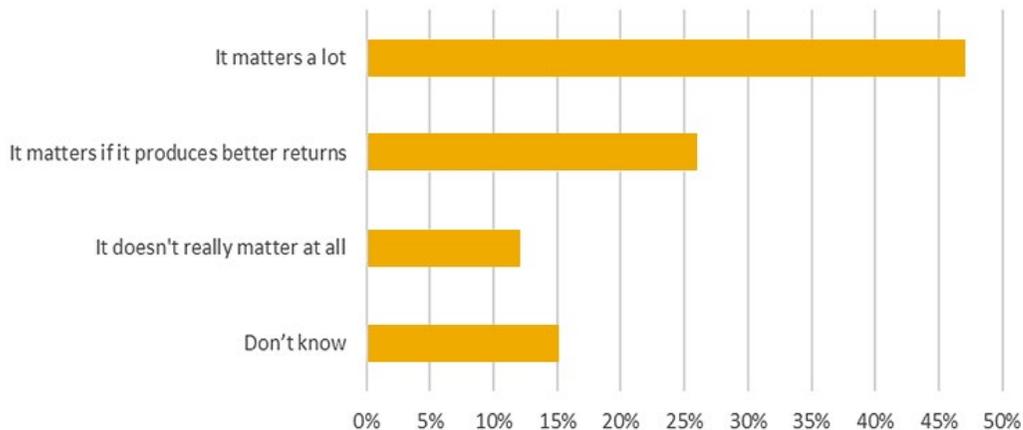
Source: Aon

In the UK: discussions and developments



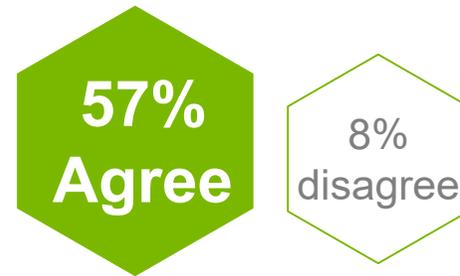
Members want their pensions to reflect their values

How important is it that your pension scheme considers how the companies and markets they invest in are run, and how they treat the planet?



Source: Nest, Building new norms, 2018

➤ Responsible Investments would make me want to engage more with my pension:



➤ RI would make me want to pay more into my pension:



Source: Defined Contribution Investment Forum, Navigating ESG, Q4 2018

Uncovering members' revealed preferences, not expressed



How much do savers value sustainability?

Median saver would prefer sustainable investments even if they have to sacrifice up to 2.5% pa returns



Who values sustainability the most?

- Younger and inexperienced savers
- No significant difference between income level, education and gender
- No difference in preference was detected between environmental and social themes



What other factors influence fund choices?

Savers showed a stronger preference for avoiding funds rated poorly for sustainability

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Leaders Group**

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Changing the way we communicate with members

Your £10,000 pension savings had the following impact:

CLEANER ENERGY 

Generating
18 MWh
of renewable energy

equivalent to the annual energy use of **1 European household**



RESOURCE EFFICIENCY 

Avoiding
8 tons
of CO₂e emissions

equivalent to the energy use of an average European house for **1 year**. Saving **£144** in avoided carbon costs.¹



WATER MANAGEMENT 

Treating
100k litres
of waste water

equivalent to the total annual waste water generated by **1 European household**



ENVIRONMENTAL SERVICES 

Recycling or recovering
2 tons
of waste materials

equivalent to the total waste produced by **2 European households** per year. Saving **£180** in reduced landfill costs.²



WELL-BEING 

1 person
benefitting from preventative care and/or healthy living programmes

saving **£980** in avoided healthcare treatment costs.³



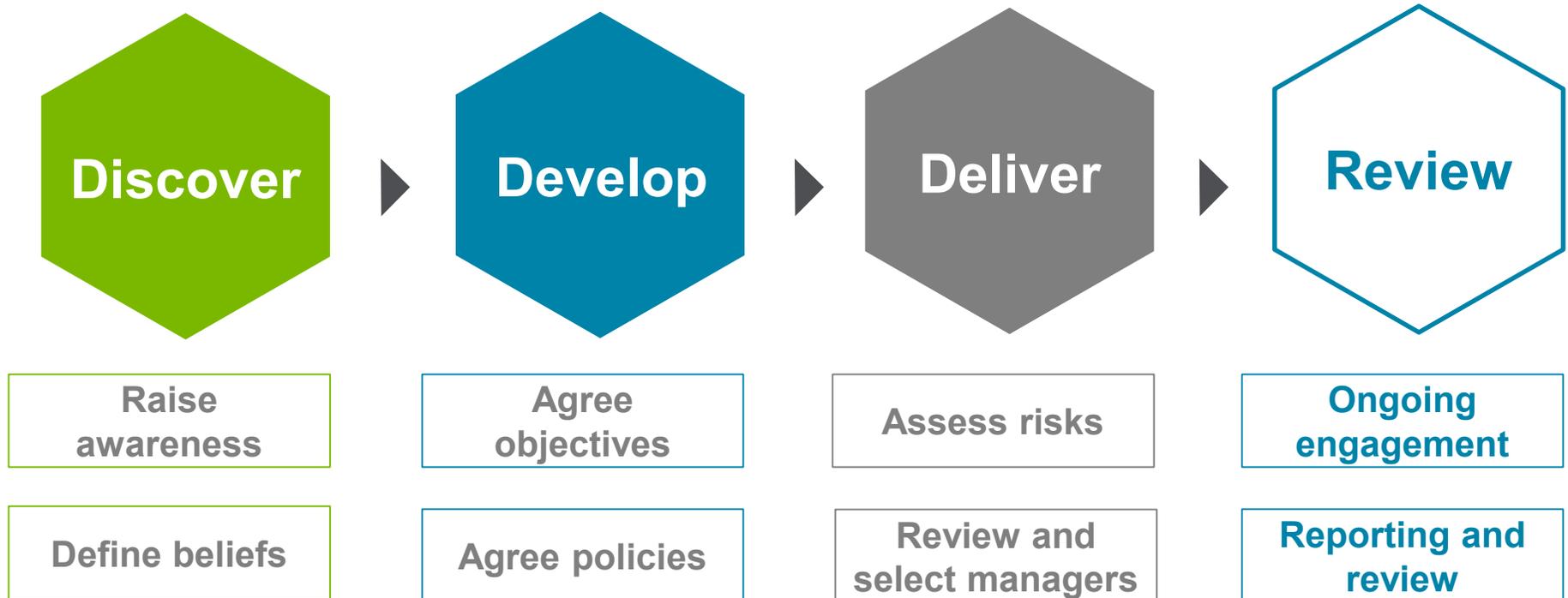
EDUCATION 

Students receiving
1 day
of tertiary education

supporting **£35** of increased annual future earnings potential.⁴



Roadmap for Responsible Investment



Impact Investment

Four tenets of impact investment



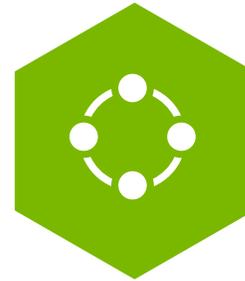
Intentionality

Investors must possess the intention to deliver positive social or environmental impact.



Financial Return

Investments are expected to generate a financial return on capital.



Range of Assets

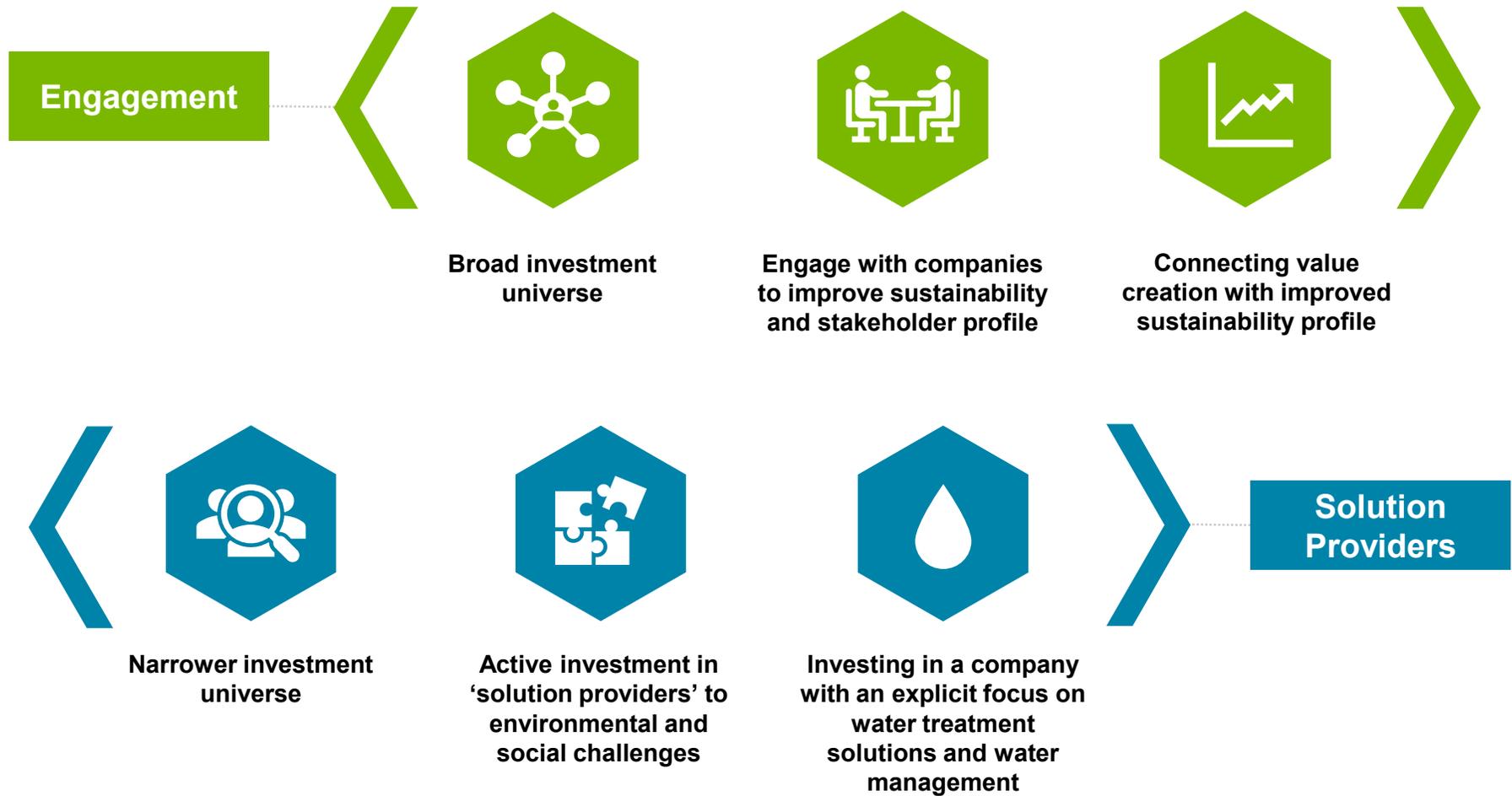
Impact investment can be conducted across a range of asset classes, with a range of return expectations.



Measurement

The measurement of impact, with respect to stated social and environmental aims, is essential.

Impact Investing in publicly traded equity



Reporting on impact

The Cambridge Impact Dashboard



Source: University of Cambridge.

IMP: Deconstructing “Impact”

Impact	dimension	Impact questions each dimension seeks to answer
?	What	<ul style="list-style-type: none"> What outcome(s) do business activities drive? How important are these outcomes to the people (or planet) experiencing them?
👥	Who	<ul style="list-style-type: none"> Who experiences the outcome? How underserved are the affected stakeholders in relation to the outcome?
📏	How much	<ul style="list-style-type: none"> How much of the outcome occurs – across scale, depth and duration?
🤝	Contribution	<ul style="list-style-type: none"> What is the enterprise’s contribution to the outcome, accounting for what would have happened anyways?
!	Risk	<ul style="list-style-type: none"> What is the risk to people and planet that impact does not occur as expected?

Source: Impact Management Project Analysis.

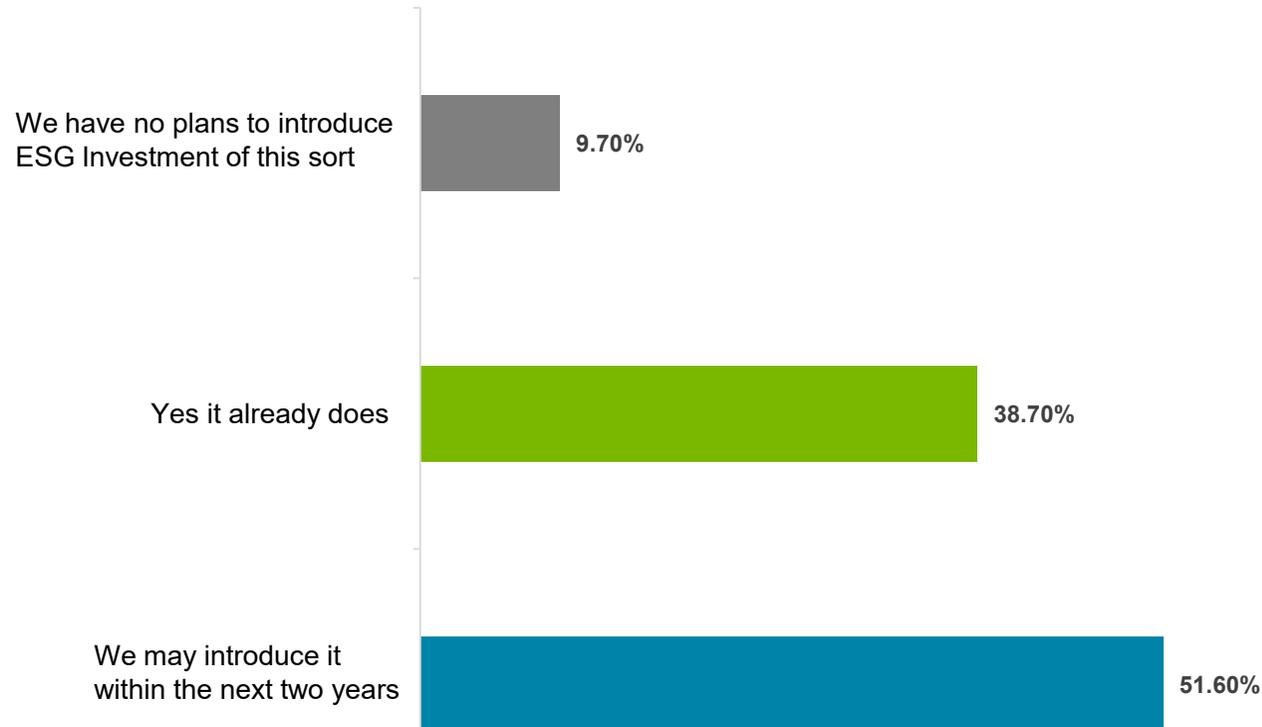
Public attitudes are changing



Source: Irish Times

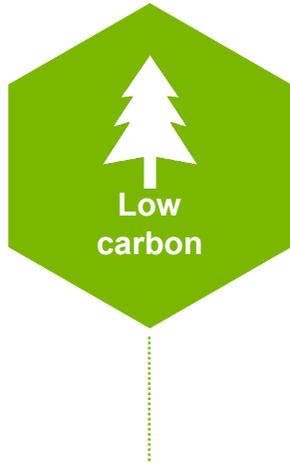
Change is coming

Does the default fund invest in any funds that adopt an ESG screening or tilting process that goes beyond voting?



Source: Corporate Adviser Intelligence

Evolving Investment Solutions



Filter the investment universe to positively tilt towards companies with a lower carbon footprint



- Coal companies
- Tobacco products
- Companies with involvement in controversial weapons
- Companies that violate the UN Global Compact*

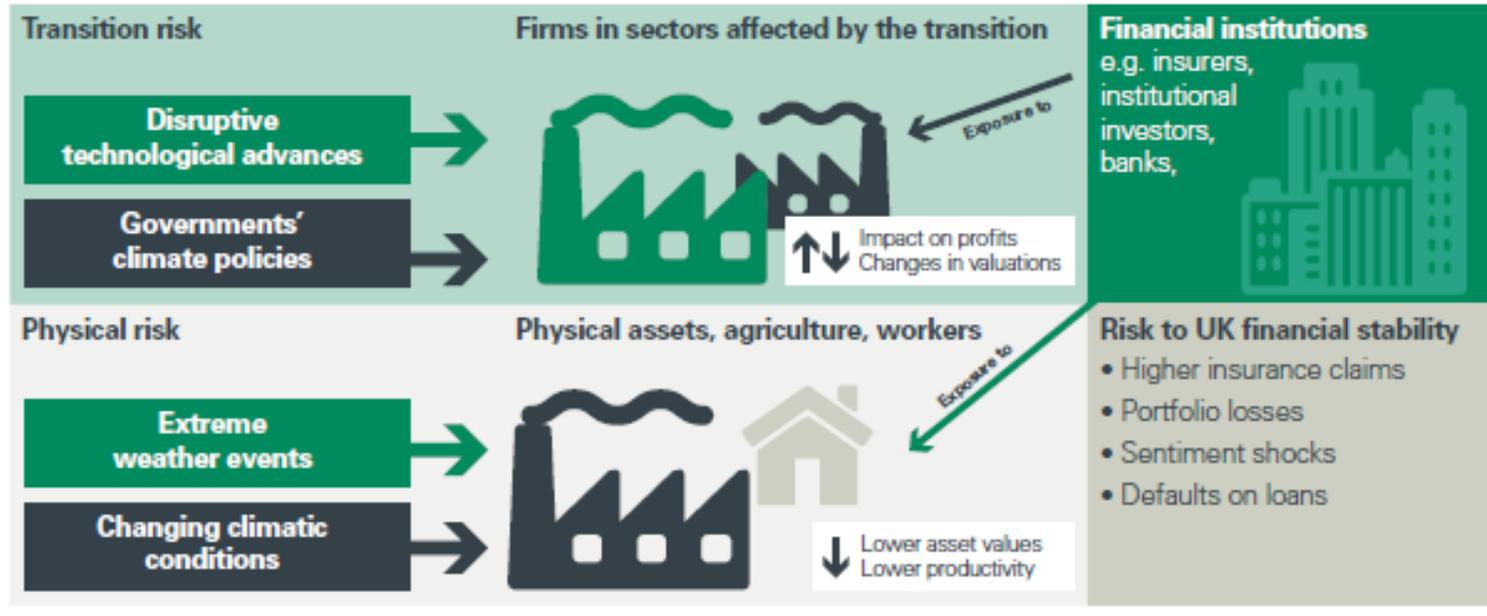


Reduce weighted average carbon intensity of the fund by 46% compared to a market-cap index**

Addition of a low carbon tilt and a series of exclusions from some of the most controversial companies and sectors while preserving the underlying return and risk characteristics

**These are companies involved in serious violations of fundamental norms who have proven unresponsive or have failed to address their controversies over a reasonable time. **Based on simulations.*

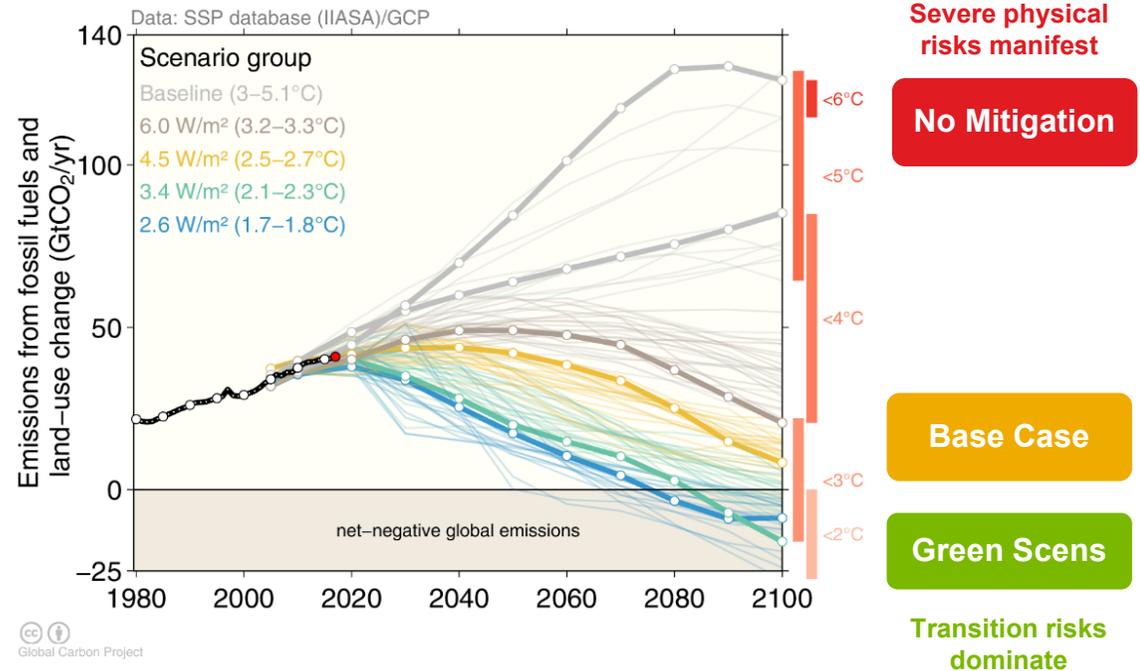
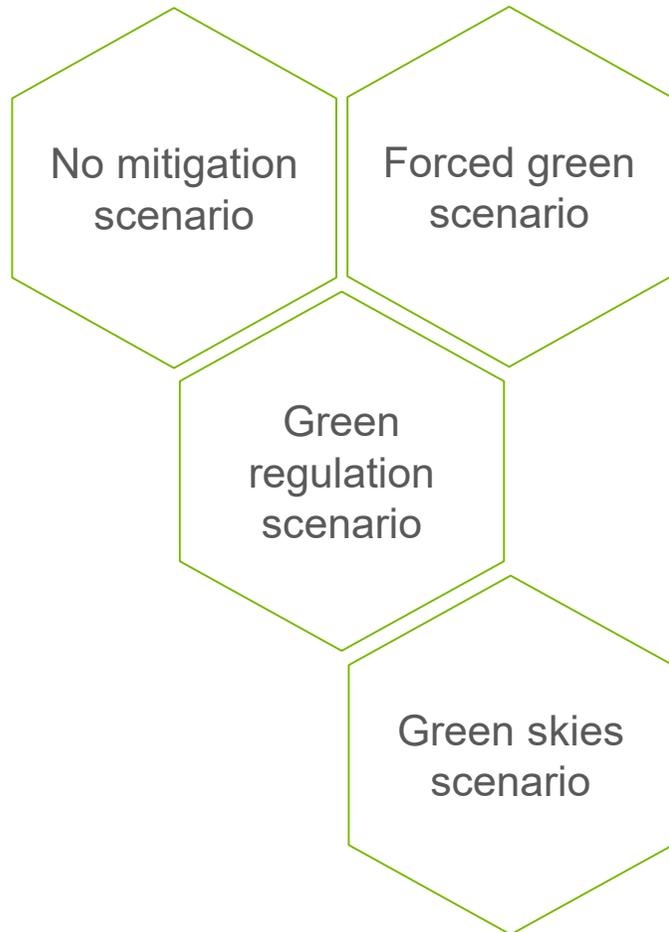
Climate change brings many types of risks



Source: Bank of England (2017)

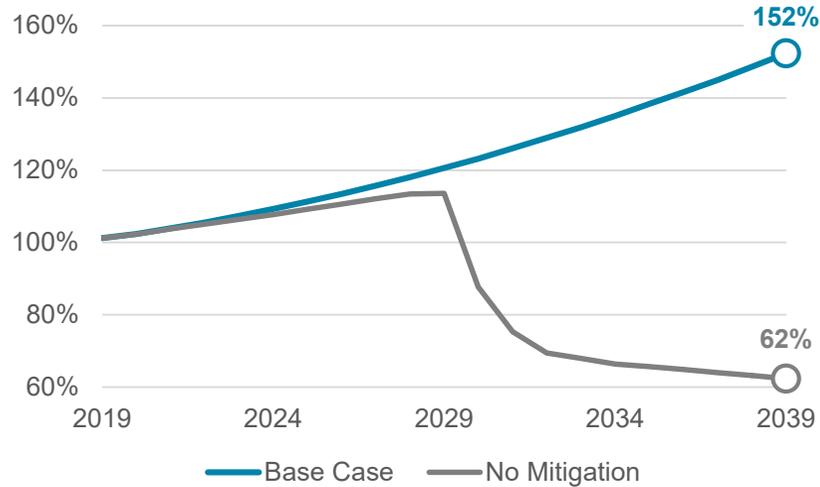
Depending on the types and coverages of insurance or assets invested in, risks could arise if third parties have suffered damage or losses from the effects of climate change and seek compensation.

Climate change scenario modelling – four scenarios

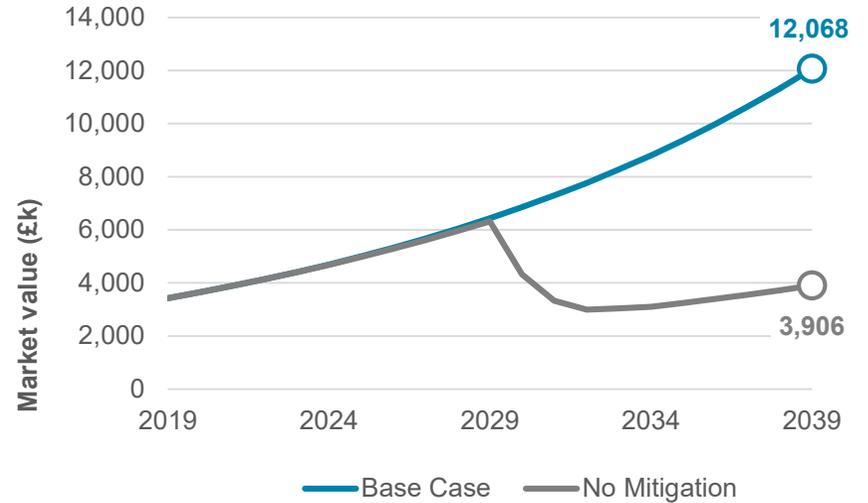


If the impact of climate change is not mitigated, what could happen to...

Your funding level?



Your equity portfolio?



Your deficit...

€90 million higher in 20 years relative to the base case



Equivalent to...

10 years of annual deficit contributions



Underperformance...

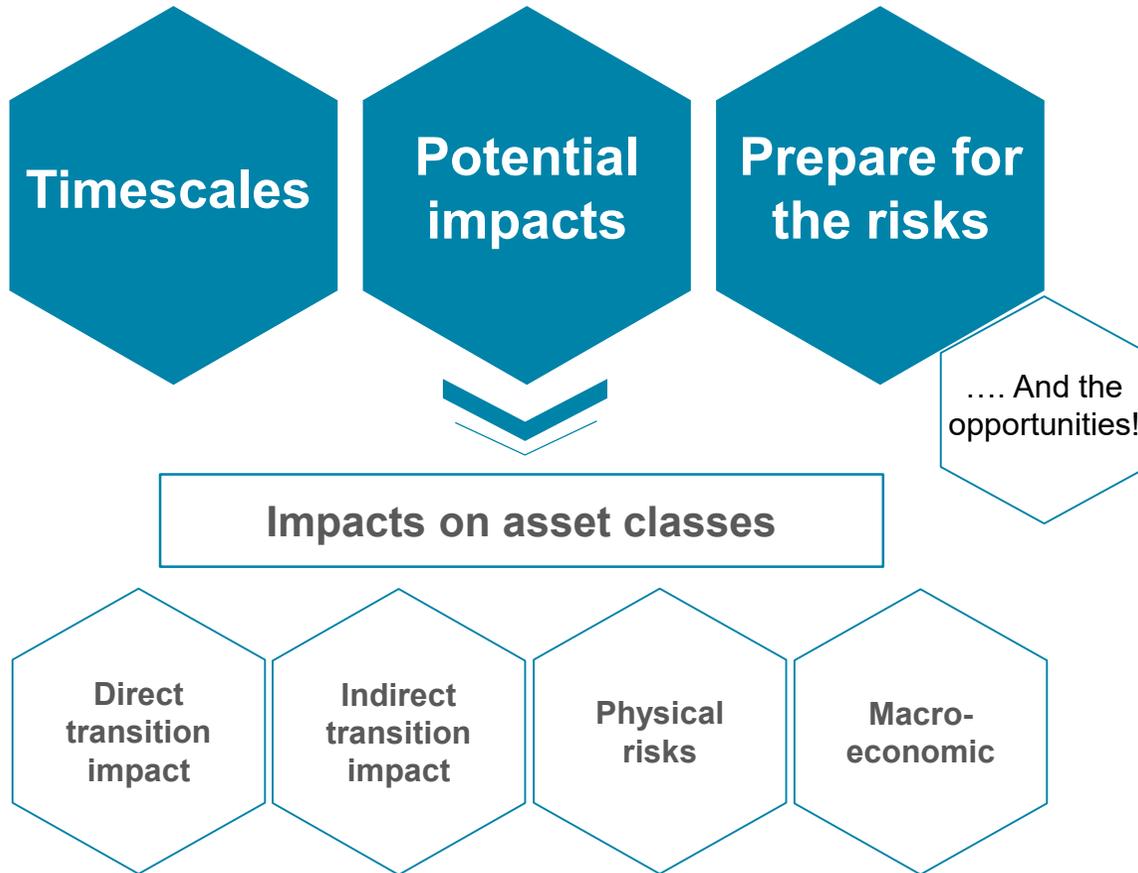
5.8% p.a. relative to the base case equity return over 20 years



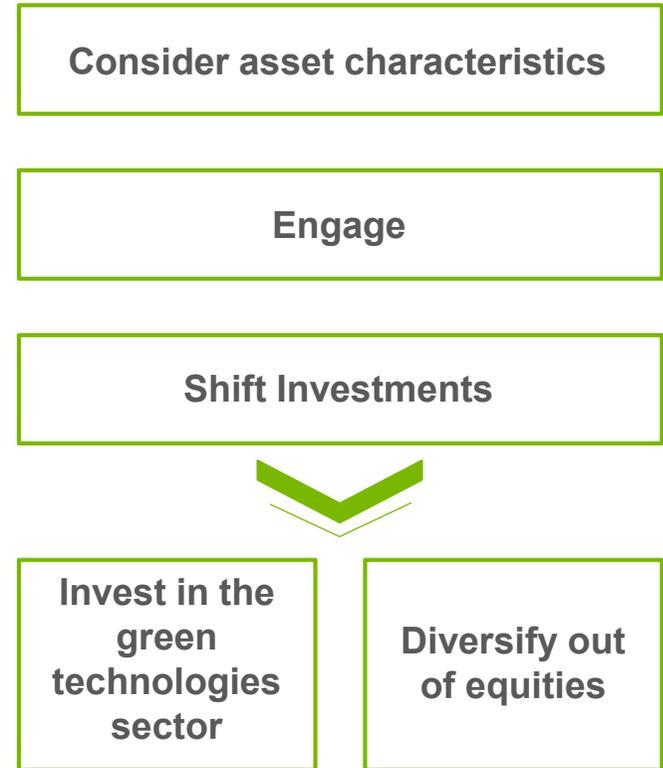
Equivalent to...

2.0% p.a. hit to overall expected returns over 20 years

Why is climate change scenario analysis useful?

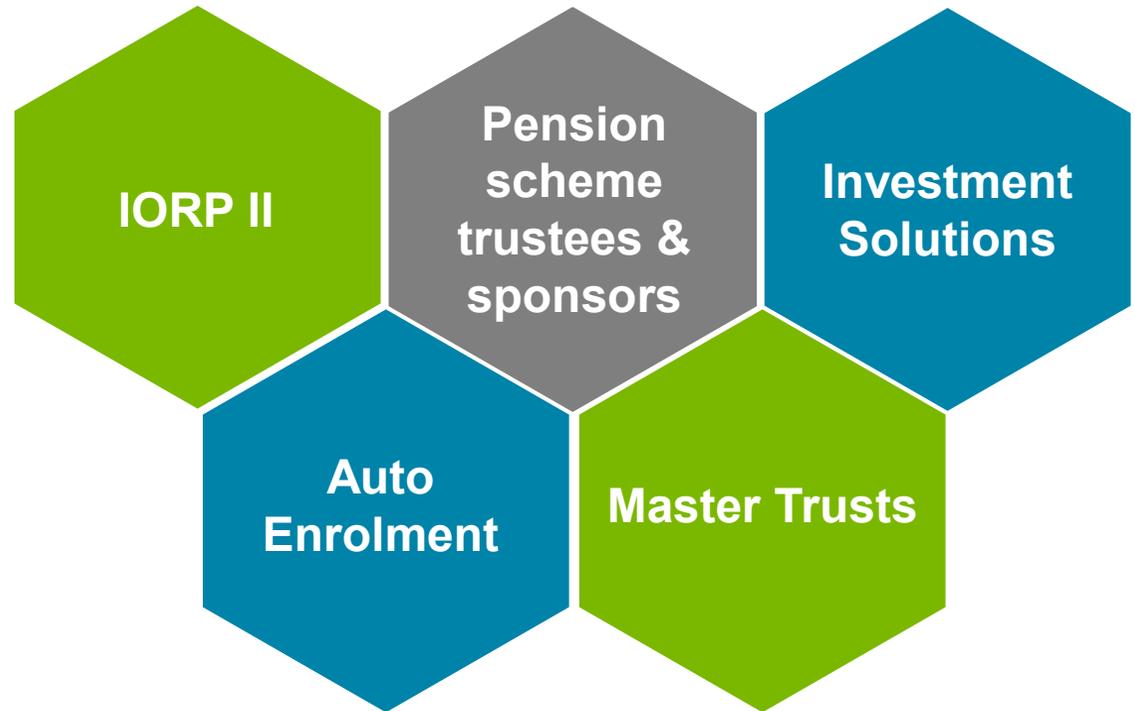


What can you do?



“Scenario analysis is an important and useful tool for understanding the strategic implications of climate-related risks and opportunities.” – TCFD

Responsible Investment – now and in the future



PENSION INVESTMENT – ARE YOU BEING RESPONSIBLE?



Tim Manuel, Aon

Darren Tuohy, Aon

John Griffith, IAPF

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