CORPORATES AND THEIR PENSION SCHEMES

HELPING EACH OTHER BE MORE SUSTAINABLE

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From left: Mark Walker, Global CIO, Unilever Pension Fund, Rob Lake, Independent Responsible Investment Advisor and Charles Nichols, Group Financial Controller, Unilever

SUMMARY

INTRODUCTION

The NAPF, the PRI, WHEB Asset Management and Carnstone Partners brought together industry experts to discuss what lessons pension schemes can learn from their corporate sponsor, and vice versa, in order for both to achieve more sustainable investment and business practices respectively.

The context for this discussion was the acknowledgement that in recent years many corporates have spent considerable resources understanding both the threats and opportunities posed by the challenges of sustainability.

Similarly, many pension schemes are increasingly recognising that, as long-term investors, they need to be conscious of the sustainability of their investments over an appropriate time horizon. The pension fund's assets can play an important role in shaping the future society that members will face, and thus, the real value of their retirement income.

Furthermore, two additional developments fostered interest in this discussion.

Firstly, the UK Pensions Regulator has only recently been given a new statutory objective with respect to sustainable growth. This has prompted the question of whether there is scope for corporates and their pension schemes to work more closely together to deliver more sustainable outcomes on behalf of their members, employees and wider society?

Secondly, many UK corporates have now gone through the implementation process of automatic-enrolment which has brought many millions of employees into pension savings for the first time. A number of firms are now considering whether they can better align their stated corporate purpose with their pension offerings to their employees.

The conference opened with the high level story of how one multinational has achieved market leadership in sustainable business and what this now means for their staff pension fund. This was followed by two panel discussions on why and how trustees and scheme officers should engage with these issues.

CASE STUDY

USING SUSTAINABILITY TO GROW MARKET SHARE

A multinational with three billion consumers globally, has embedded sustainable practices across its organisation. The company believes that sustainable business practices are critical to growing the business in the coming years.

They highlighted the rise of young consumers—those in the 18-34 year old bracket—who are becoming more demanding about the impact of products on the environment including how products are sourced and packaged.

Fiona Reynolds, Managing Director, PRI

The company is also looking towards emerging markets for growth, which carries with it a number of other sustainability risks. For example, those countries which have challenges around issues such as water, waste and energy will have an impact on the company's future business model.

MANAGING THE SUSTAINABILITY PERFORMANCE OF A BUSINESS?

There are five factors that are considered when trying to define the value of sustainability? These are:

1. Reputational risk.
2. Regulatory issues.
3. Margin expansion (trying to get more for less).
4. Intangibles (e.g. positive influence on graduate recruitment).
5. Long-term growth (to meet the needs of stakeholders—both customers and suppliers).

In order to be successful in embedding sustainability, it was suggested that companies need to start by clearly articulating what 'success' in sustainable business practices looks like. This then needs to be supported by putting in place effective reporting systems across the business to measure the degree of success.

Internally, it is crucial to create alignment and win the 'hearts and minds' of people within the organisation. Externally, the focus needs to be on collaboration with other stakeholders in order to create the circumstances to move the agenda.

One company – even a large one - cannot drive sustainability forward on its own.

TRANSLATING SUSTAINABILITY THEMES TO PERFORMANCE OF THE PENSION SCHEME?

The corporate pension fund is keen to take a leadership role in sustainable investing practices. However, it realises that this is not without difficulties.

As an example, the pension fund representative pointed to the fact that full sustainability accounting is a very difficult process to undertake. Unlike traditional accounting, which has been in existence for more than 100 years, sustainability accounting has only been in existence for a much shorter period[1].

In order to make progress, sustainable investment considerations need to become much more relevant to the decision-making process. Ultimately, the company believes that sustainable business models produce better returns in the long-term and this is a belief shared by the pension scheme.
The pension scheme has found that working with external research organisations has proven useful for looking at sustainability trends across both equity and corporate bond portfolios. One such trend which is gaining momentum is improving the understanding and accounting for a company's carbon exposure.

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Following the case study discussion, attendees then had the opportunity to hear from a number of other industry specialists during two panel presentations. The first panel discussion focused on the question of why trustees and pension scheme officers should engage with sustainability issues. The second panel dealt with the question of what practical steps can a scheme take to integrate sustainable investment into corporate scheme practices?

Sustainable business practices have been a key focus for many corporates for many years. This is not easily transferred to corporate pension schemes because of various factors such as the complexity of measuring and communicating the business benefits, legal barriers between the sponsor and the pension scheme, complex and conflicting terminology, and capacity issues.

LACK OF CAPACITY AT TRUSTEE LEVEL

There is often a weak relationship between companies and their pension fund's on sustainability matters. There are a number of issues at play here:

- Time and capacity constraints were raised as a barrier to trustee engagement.
- Trustees have arrived late to the party but their participation is improving. Some companies now have a working party to consider ESG issues with a trustee board sub-committee tasked with making sure the scheme is engaged.
- The experience of the panellists was that it is important to identify trustees who can champion this agenda. The initial steps are the hardest, but once some momentum is generated, the ways in which ESG/sustainability can add value become clearer.
- The role of the unions and Member-nominated Trustees (MNTs) in this agenda is important as they often have a high degree of interest and expertise in many of these aspects.
- The level of trustee understanding about sustainable investment practices can be low. This is too often a language issue whereby sustainability is interpreted as meaning taking an 'ethical' investment approach.

COLLABORATION WITH INVESTMENT CONSULTANTS AND INVESTMENT MANAGERS

- One reason cited for low trustee awareness was the lack of proactive support given by the investment consultants and / or their investment managers.
- It was stressed that it is down to trustees to make sure they bring their investment managers up to the mark.
- Crucial to this is a clear set of investment beliefs which will guide trustees in their longer-term thinking. Does the pension scheme believe that taking sustainability factors into account leads to better risk-adjusted performance over the longer-term? Given that quantifying the financial performance attributed to sustainability is hard – investment beliefs will help push back on short-term performance pressures.
- 'Stewardship' was highlighted as a useful development as it has allowed pension funds to take a tougher line with the asset managers enabling them to hold them to account for the implementation of recommendations stipulated in the Stewardship Code.

1 The Global Reporting Initiative, arguably a basic form of sustainable reporting, was set up in the late 1990s.

- A fund ran their investment manager's portfolios through third party software in order to identify stocks that had particular ESG risks. This process helped the trustees to then query their investment managers as to the reasons which lay behind these investments; they also asked their investment managers to provide an example of how they disinvested or engaged differently when poor ESG scores were identified.
- Building a network with academics and related stakeholders can also be helpful – as an example, it was mentioned that CalPERS has been able to build a robust business case through extensive collaborative research with academia.

REPORTING AND COMMUNICATION

- Having robust reporting structures is an important ingredient for success in ensuring that expectations and policies are being delivered in practice.
- Engagement of individuals with the concept of retirement savings is very difficult. It is currently difficult to get individuals to save but perhaps better communication about where and how their savings are invested may help with this.
- It was commented that while Defined Benefits schemes will be with us for a long time to come, it will be the Defined Contribution schemes which will represent the future. It was suggested that a DC environment will require a much more active communication approach.
- Increased communication between the corporate sponsor and the pension fund is encouraged - to exchange insights which should be viewed as a free resource.

SEMINAR SPEAKERS

- **Charles Nichols**, Group Financial Controller, Unilever
- **Mark Walker**, Chief Investment Officer, Unilever Pension Fund
- **Michael Deakin**, Chairman, Manifest information services and trustee
- **Peter Montagnon**, Associate Director, Institute of Business Ethics
- **Julia Rebholz**, Group Sustainability Director, Centrica
- **Daniel Ingram**, Head of Responsible Investment, BT Pension Fund
- **Inder Dhinga**, Trustee, Lloyds Banking Group DC Pension Scheme
- **Lesley Alexander**, previously CEO, HSBC Group Pension Fund and now Managing Director, Ferrier Pearce Creative Group.
- **Helene Winch**, Director, Policy and Research, UN-PRI