New type of pension scheme launches in Britain

Collective defined contribution pension schemes offer a ‘middle ground’ option between existing schemes.

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A new type of pension scheme has opened for applications in Britain.

Collective defined contribution (CDC) pension schemes offer a “middle ground” option between existing schemes.

With defined benefit (DB) schemes, such as final salary schemes, employees are promised a guaranteed income, and with defined contribution (DC) schemes, which are more common nowadays, the saver bears the risk of how much pension they eventually end up with.

DB schemes have become increasingly rare as they are expensive to run with people living for longer.

CDCs have the potential to provide improved retirement returns for savers, with more predictable costs for employers, the Department for Work and Pensions (DWP) said.

Both employers and employees contribute to a collective fund from which individual retirement incomes are drawn, with trustees responsible for oversight to ensure schemes are viable and can meet their legal requirements and commitments to members.

Minister for pensions Guy Opperman said: “CDC schemes have the potential to transform the UK pensions landscape.

“We have seen the positive effect of these schemes in other countries and it is abundantly clear that, when well designed and well run, they have the potential to provide a better retirement outcome for members, and can be resilient to market shocks.

“I have no doubt that millions of pension savers will benefit from CDCs in the years to come.”

The new schemes were made possible following the passage last year of the Pension Schemes Act.
Regulations currently provide for single CDC schemes or ones where employers have some sort of connection.

Some parties have already expressed an interest in expanding CDC models, including multi-employer CDC schemes, the DWP said.

Nigel Peaple, director of policy and advocacy at PLSA, said: “CDC blends some of the desirable elements of defined benefit, such as clearer target outcomes for the saver, and of defined contribution schemes, such as predictable contributions for the employer and member.

“By pooling longevity risk and the ability to invest money over a longer period, CDC has the potential to provide new and better approaches for benefit provision.

“There are, of course, challenges, including how to ensure savers understand the variability of benefits, and ensuring new models can deliver in practice once reserving and regulation is in place.

“Nevertheless, we are confident that this ambitious proposal will provide the incentive and momentum to overcome them.”

The DWP plans to consult later this year on a package of prospective design principles and approaches to accommodate new types of CDC schemes.

CDC authorisation and ongoing supervision will be administered by the Pensions Regulator.

Managers Still Bullish on ESG: Survey
By Michael Taffe
FUNDfire
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Asset managers remain bullish about the prospects for environmental, social and governance investing despite growing scrutiny from investors and consultants around greenwashing, a new survey suggests.

On average, managers expect 40% of their portfolios to include ESG elements 12 months from now, according to a new survey from the Index Industry Association. This marks a 13 percentage point increase from a survey taken in 2021.
Respondents in the survey, which included 300 global asset management firms, also said they expect ESG elements to be incorporated in 64% of their portfolios a decade from now – a notable increase from 52% in the 2021 survey.

The fastest growth appears to be happening in the fixed income space.

The proportion of managers implementing ESG factors in fixed income portfolios rose sharply to 76% from just 42% in 2021, the study found.

ESG investing initially grew in popularity within equities markets, relying on metrics of a company’s sustainability.

Rick Redding, CEO of the association, known as IIA for short, said he views ESG factors being included in other asset classes like fixed income portfolios as the next natural progression.

“What we’ve seen in the last two years is [that] ESG indexes were the fastest growing by a wide margin, [the] most we’ve ever seen.”

One reason that ESG historically concentrated in the equity space was greater availability of data, said Amanda Tepper, CEO of Chestnut Advisory Group.
“It was easier to do equities, and that probably just has to do with the databases,” Tepper said.

The bond market can be more complicated to navigate than the publicly traded equity space, and many issuers historically did not provide ESG-oriented metrics that could be neatly sorted into databases, she noted.

Issuers of government bonds are beginning to pay more attention to demand for data on ESG factors, said Jeff Strange, relationship manager at Fuse Research.

“In Europe, there are much clearer standards, for better or worse around what it means to be in different levels of ESG investment and classifying companies, so it works better. I think we’re starting to see that same type of investment process and standards,” he said. “I think some of it does just have to do with the landscape for governments becoming more sensitive to ESG, and issuing bonds in that vein.”

Breckinridge Capital Advisors, a Boston-based asset manager, recently rolled out new reporting for sustainable municipal bond portfolios in response to demand and increasing availability of ESG data for municipal bonds, said Rob Fernandez, the firm’s director of ESG research.

“There does seem to be certainly growing interest and attention being paid to encourage municipalities to disclose more in a more standardized way about their climate risks and other ESG risks,” he said.

The interest rate environment over the past two years could have delayed some investors adopting fixed income ESG strategies, Fernandez said.
“It's more about investors taking a little bit of a wait and see approach to allocating to fixed income more generally, because of the direction and interest rates, because of inflation rising, interest rates have risen,” he said. And so that that's where we've seen a little bit of a change in investor sentiment about allocating to fixed income. And we view that as temporary.”

While the underlying data has improved rapidly, there are still some remaining hurdles to the expansion of ESG product, Redding said.

“Obviously one of the big issues that the asset management community is facing is creating product, and then making sure that the investors understand what that product really entails,” he said. “And that's why this corporate-level data is so important, to give people confidence that they're truly investing in something that meets their principles of investing.”

Advisors may also face challenges explaining to their clients why they are invested in ESG if the strategies aren’t performing as well in the current economic environment, Strange said.

“They're trying to do what's right for their client, but there's a risk there for them to say we put you into this lower-performing fund because you wanted investments that were more environmentally sound,” he said. “The investor might say, ‘well, that's not what meant.’ I think the advisors lack some protection because of the lack of standards.”