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High Pay Centre briefing: Pension saver views on the social and environmental impact of investments

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Background

Pension savings make up a significant and growing proportion of individual wealth in the UK. The latest government figures from 2018 show that £2.6 trillion is invested in UK pensions, up from £2.3 trillion in 2015.(1)

Pension savings are also one of the most commonly held forms of wealth in the UK. The percentage of adults below the State Pension age actively contributing to a private pension has increased, from 43% in 2012, to 53% in 2018.(2)This rise is likely to be a result of the introduction of auto-enrolment between 2012 to 2018.

Since 2019 almost all occupational pension schemes with 100+ members have been legally required to have a policy on financially material ESG factors as well as on non-financial matters pertaining to the environmental and social impact of the scheme's investments. In contrast to financially material social and environmental factors, trustees are not required to take account of these non-financial matters when making investment decisions. In June 2021, the Department for Work and Pensions launched a 'call for evidence' examining the effectiveness of occupational pension scheme trustees' current policies and practices in relation to social factors.(3) This call was to help the DWP to assess how trustees of these schemes understand "social" factors and how they seek to integrate considerations of financially material social factors into their investment and stewardship activities.

The scale of pensions saving means that most people are invested in the UK's biggest listed companies. Pension funds should be considering the social dimensions of these investments for the following reasons:

[1] Social and environmental factors can have a material impact on investment returns - for example, companies that are good employers are likely to benefit from improved employee engagement and productivity, and positive consumer sentiment. Conversely, the opposite is likely to be true of companies whose labour standards fail to meet regulatory standards or societal expectations. Therefore, it makes sense for pension funds to engage with social issues as a means of identifying financial risks and opportunities.

[2] Pension savers' investments should reflect their values. While there are many ways in which the interests of employees and other stakeholders align with those of investors, it is clearly the case that there are occasions when they are in conflict - recent examples might

include the drop in Ryanair's share price in response to the move to to introduce collective pay bargaining for pilots, or a similar fall in the value of pharmaceuticals companies after suggestions that their intellectual property rights might be suspended in order to widen access to the Covid vaccine.(4)(5) Investments in tobacco, arms and other controversial industries have all proved highly profitable. Given the controversial nature of companies and industries such as these, and the damage they can inflict on society, it is critical that pension funds understand the social and environmental impact of their investments in relation to the values of their members.

[3] The social and environmental impact of investments has consequences for savers. Pension savers have to live in a world that is shaped by the companies and industries that they invest in. Achieving an adequate return on their investment is critical to their standard of living in later life - but so too are factors such as the prevailing labour standards of the day; income levels and inequality, in part determined by the practices of major employers, and their economic and social impact; or the tax contributions of large corporations and the consequences for public services. Therefore pension funds need to consider the social and environmental impact of their investments in terms of the holistic outcomes that result for their members.

While pension funds' investment and stewardship practices should reflect their own informed and evidenced judgement of what represents their members' best interests, it is important to note that investment decisions are often wrapped up in ethical or values-based questions.

Similarly, judgements of the holistic impact of investment decisions on pension fund members are to some extent subjective, and the views of the members themselves are critical to an informed perspective.

So while pension funds' approach to social issues should not be wholly determined by members' views, they should be informed by them. However, this is complicated by the fact that pension savers may not have a sophisticated understanding of pensions investments and may be unfamiliar with many of the social issues associated with the companies in which they are invested.

This can create the illusion of apathy or acceptance on the part of pension savers regarding the social impact of their pension saving, but should not absolve pension funds from their responsibility to engage with these issues. Indeed low levels of financial literacy and understanding of the pensions investment process make it even more important for pension funds to inform and educate their members about how their savings are invested. Similarly, it is critical that funds take steps to understand members' values and holistic interests, and incorporate them into their investment practices, rather than assuming that unless the members approach them, reflects a level of comfort or satisfaction with the social and environmental implications of their investments.

Working with polling company Survation, we have surveyed the public on their knowledge and attitudes towards this issue, to get a better idea of the strength of public support for their pension savings being used for environmental and social impact; and to consider what approaches might be most effective to transfer wealth towards better social and environmental outcomes.

Key findings

- A majority of people (53%) consider themselves to have a low understanding of pensions, investments and financial markets and are not aware if their pension fund has an ethical investment option (53%).
- People haven't looked into how their pension fund is invested because of their low understanding of pension, investments and financial markets (45%), because of their trust in financial professions (40%) or because of a lack of time (30%)
- A large majority of people say it is important to be kept informed on how their pension fund is invested (73%).
- Most people want their pension fund to reflect their ethical values and beliefs (66%).
- Most people believe that pension funds should be required to take steps to understand members' attitudes to ethical investment even if members haven't contacted them directly about it (72%).
- Half of respondents think generating financial returns is an important factor pension funds should consider when investing in companies (50%), but almost as many people said the same of the pay and conditions of a company's workers (42%), the company's environmental impact (37%), and the company's approach to human rights issues (37%).
- Over a third of people (37%) would be willing to accept some reduction in their pension saving, if it were more ethically invested.
- Almost a third of people consider insufficient pension savings as the biggest threat to their quality of life in their later years (29%), but considerable numbers of people see factors such as climate change (21%), the slow growth of the UK economy (19%) or the divide in society between the rich and the poor (13%) as bigger threats.
- People based in London, younger demographics and those with higher understanding of financial issues are the most concerned with their pension savings being invested ethically.
- Older demographics and those with a lower understanding of financial issues are the least interested in ensuring their pension savings are invested ethically.

Methodology

Survation carried out an opinion poll asking twenty questions we selected relating to individuals' knowledge of their pensions and views on how they are invested. Fieldwork was carried out from 9th-15th April. The survey was conducted via an online panel of 1,026 people over the aged 18+ who are paying into a workplace pension. Invitations to complete surveys were sent out to members of the panel. Differential response rates from different demographic groups were taken into account.

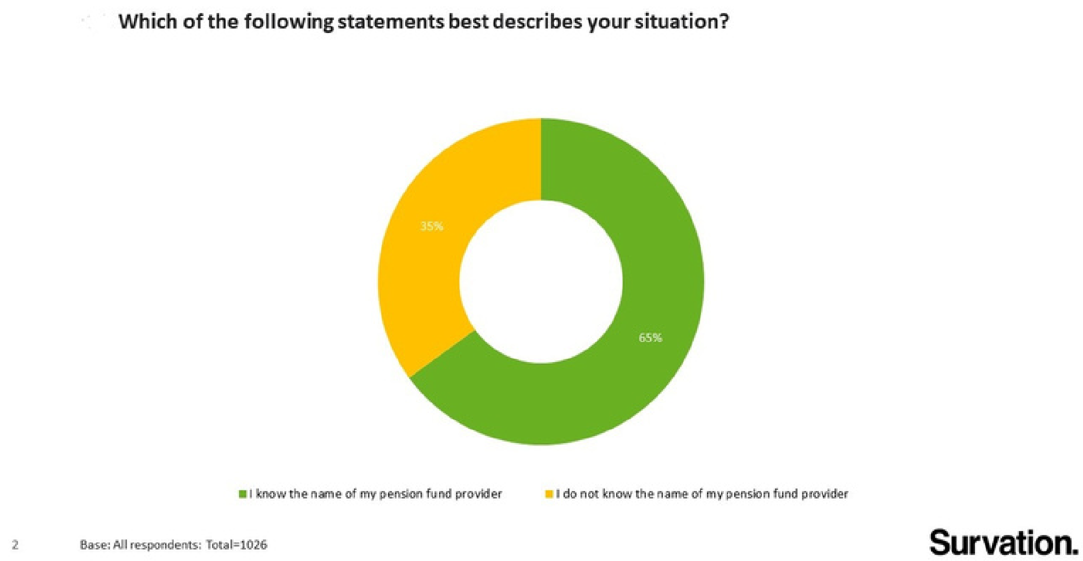
Section 1

Many savers don't know a lot about their pension fund and lack confidence in discussing financial/investment issues.

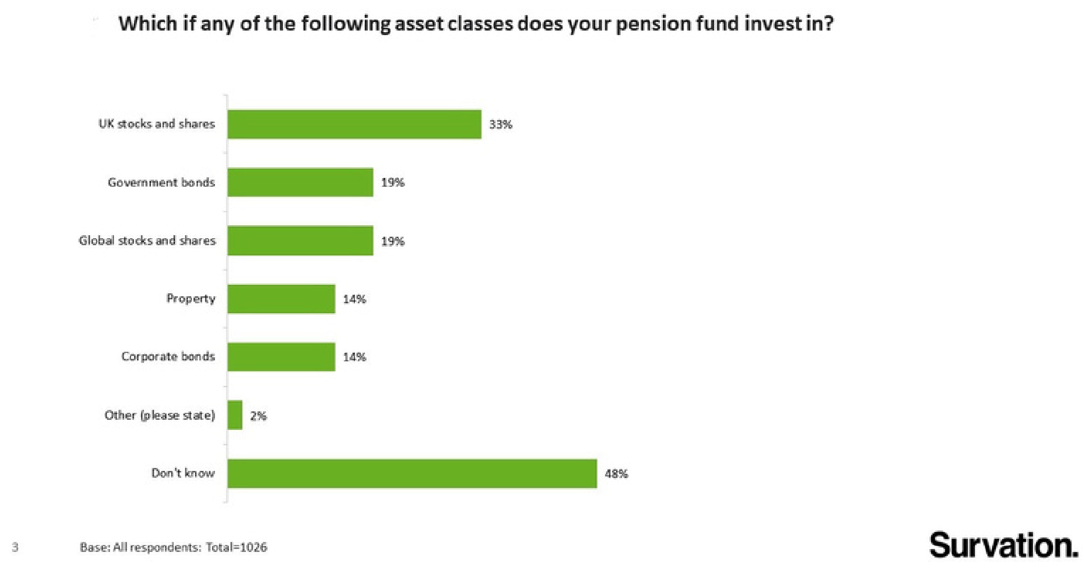
This is unsurprising given that there is no compulsory education on financial economics and many people are auto-enrolled by their employers for their pension.

Key findings from our polling on understanding of pensions and investment emphasise this point:

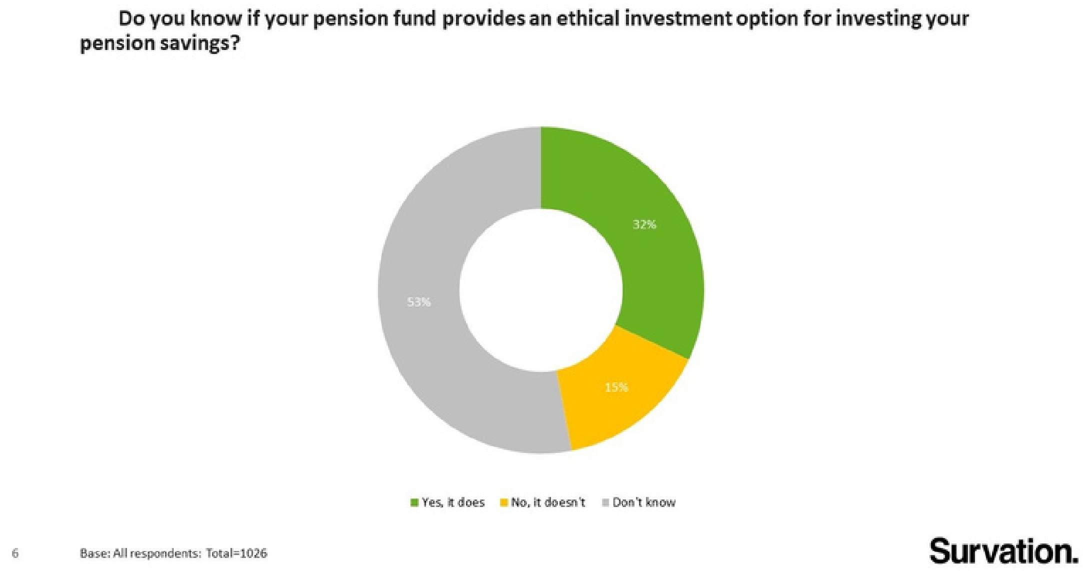
35% of survey respondents were unable to name their pension fund;



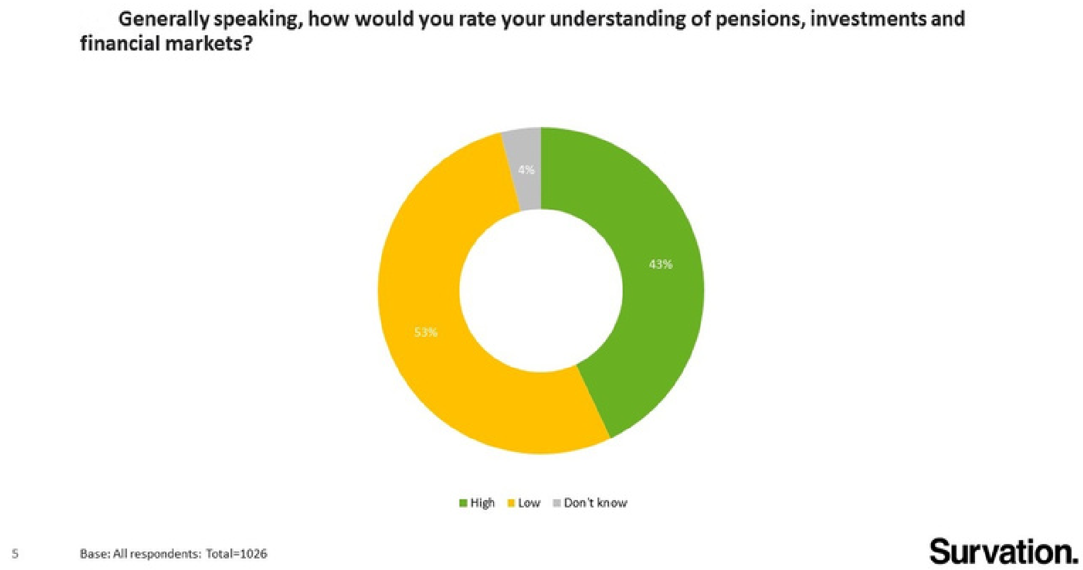
48% can't name an asset class that their pension fund invests in;



53% don’t know whether their pension fund has an ethical investment option;



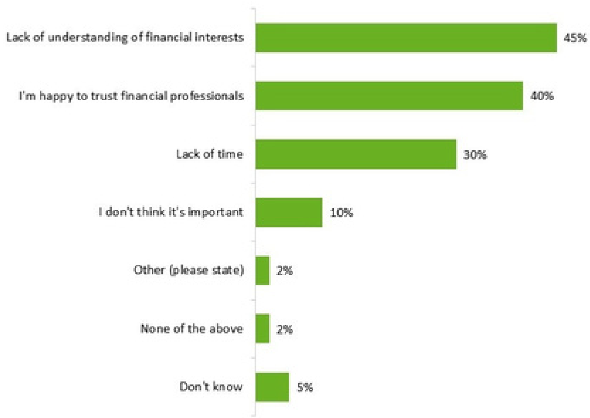
53% consider themselves to have a low understanding of pensions investments and financial markets;



45% of those claiming to have a low understanding of pensions investments stated this as one of the reasons why they haven’t found out more about where their pension fund is invested;

30% cited a lack of free time;

Which if any of the following reasons have prevented you from finding out more about where your pension fund is invested? Please select all that apply



7 Base: Respondents whose answer to Q4 is 'Quite low', 'Very low', or 'Don't know': Total=583

Survation.

This issue is particularly stark among some demographics.

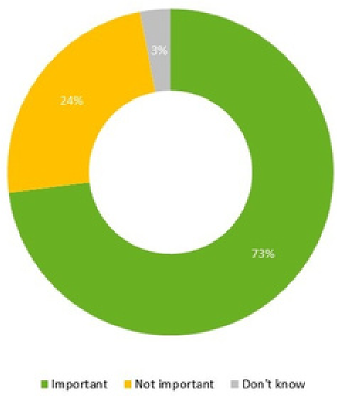
Part-time workers, women, those on low and middle incomes - groups who might be particularly affected by some of the social issues exacerbated by the practices of their investee companies - are all more likely to have responded to the questions in a way which indicated lower than average knowledge and confidence on these issues.

Section 2

Savers are generally interested in how their pensions funds are invested and want them invested in an ethical way. This is the case across all demographics.

73% of survey respondents said it was important for them to be kept informed about where their pension funds are invested.

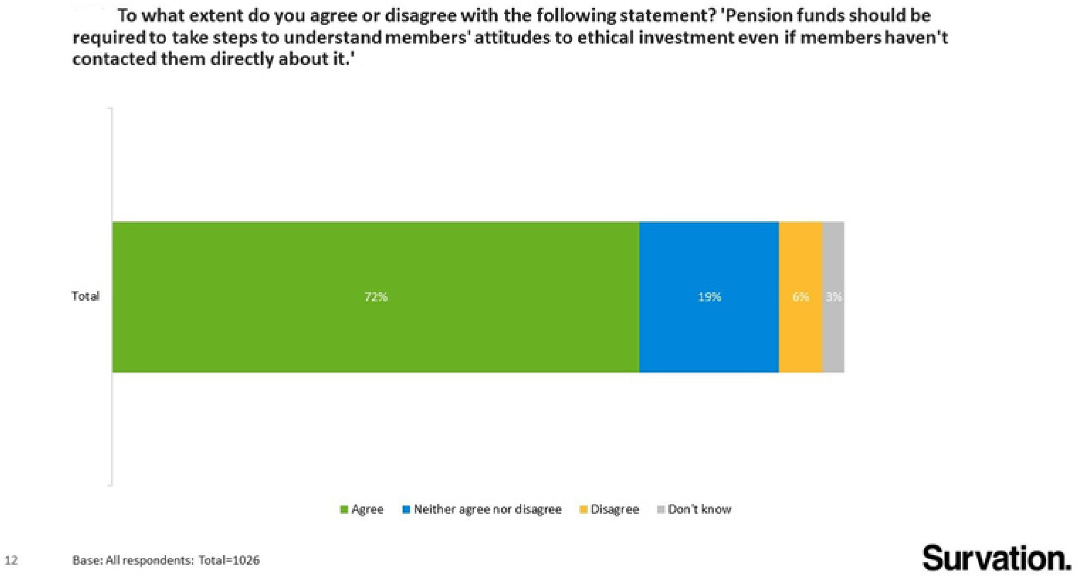
How important if at all is to you to be kept informed about where your pension fund is invested?



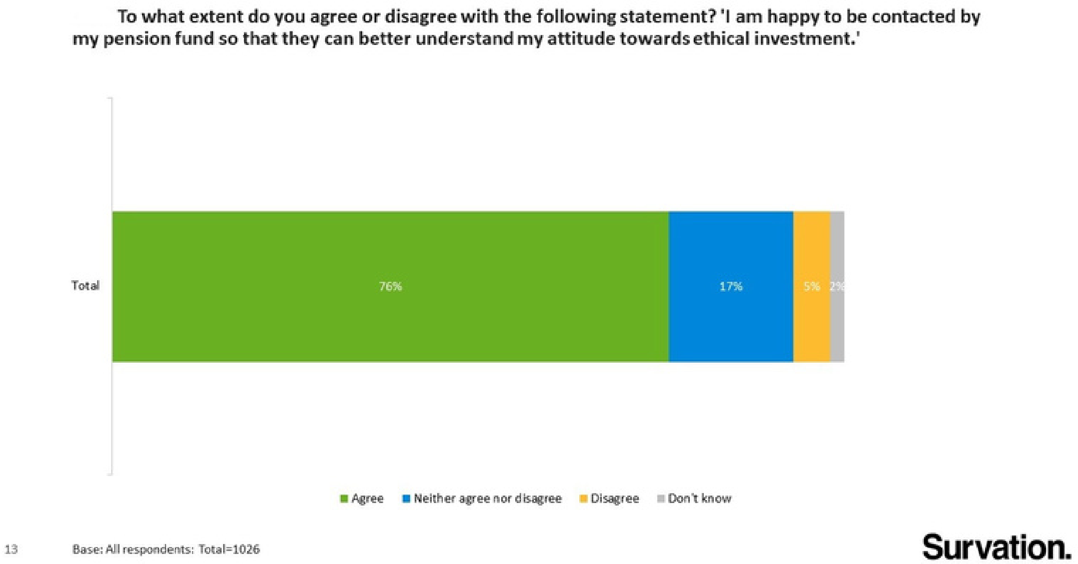
9 Base: All respondents: Total=1026

Survation.

72% agreed with the statement that 'Pension funds should be required to take steps to understand members' attitudes to ethical investment even if members haven't contacted them directly about it.



76% said they would be happy to be contacted by their pension fund, so the provider can better understand the saver's attitude towards ethical investment. The younger respondents are most likely to say that it's important for them to be kept informed about where their pension funds are invested (81% for 18-24s compared to 57% for the lowest group, the 55-64s).



As for whether it is important for people that their pension fund reflects their ethical values and beliefs, more than twice as many respondents said it is important (66%), than those who said it isn't (29%). This was reflected across all demographic groups including those with lower knowledge of pension funds or confidence discussing financial/investment issues such as those employed part-time and those not earning high incomes.

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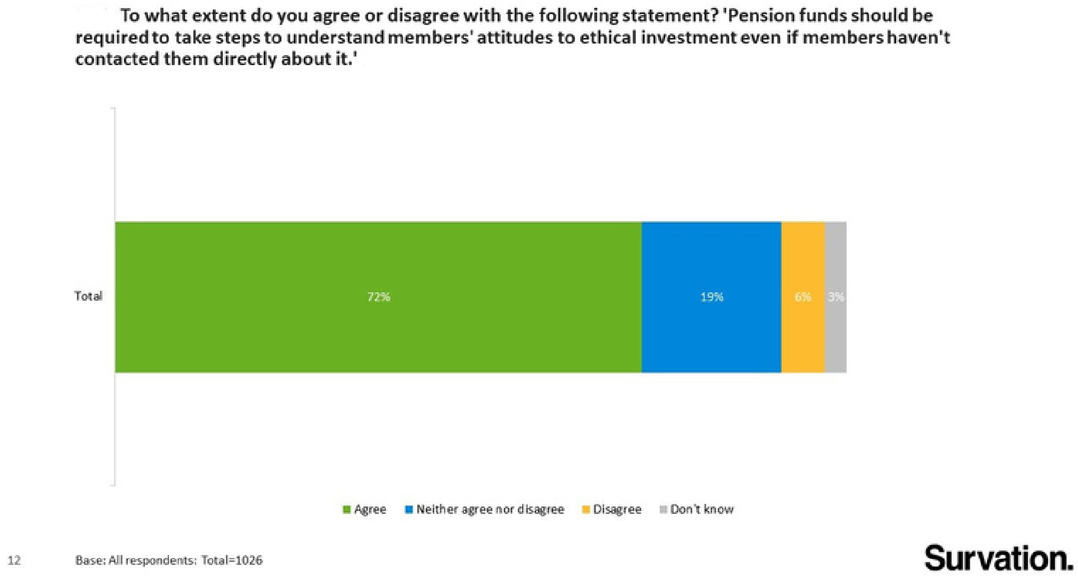

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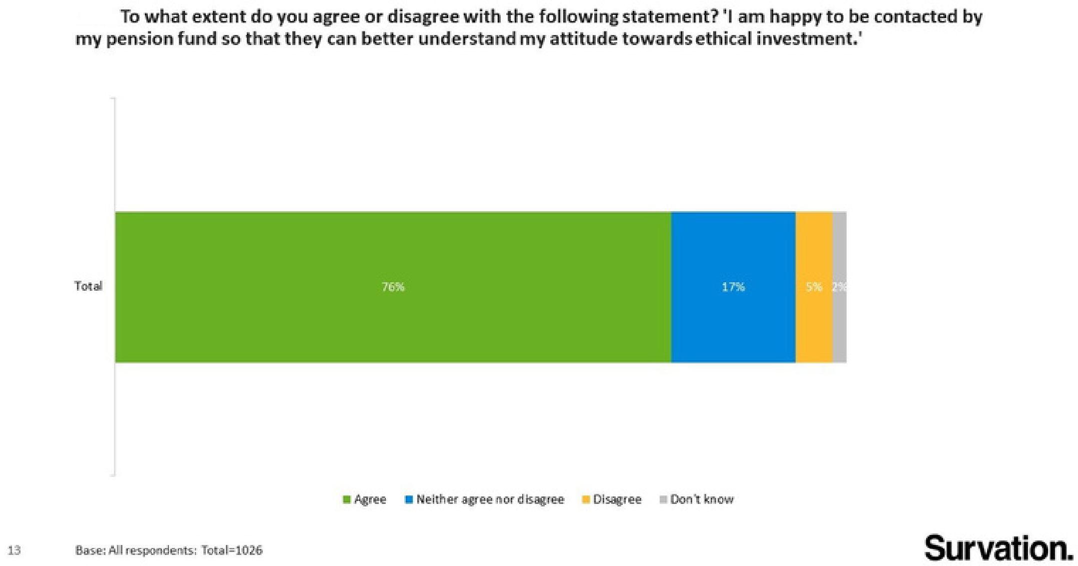

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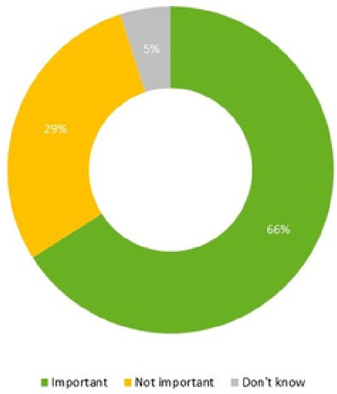
How important if at all is to you that your pension fund investment reflects your ethical values and beliefs?



10 Base: All respondents: Total=1026

Survation.

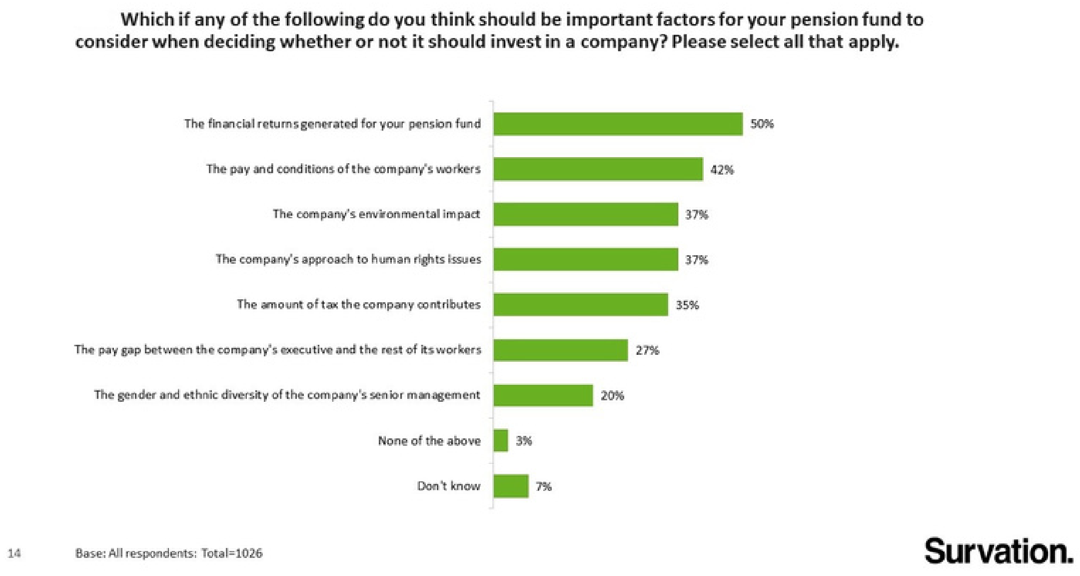
These findings indicate that pension savers would welcome their pension fund engaging them more on how their pension fund is invested to ensure that investments are in line with their values. This seems particularly important, given that there are many people who have responded this way have also indicated that they lack confidence or knowledge on these issues. It suggests that an active role for pension funds in engaging savers is important, so that pension funds are acting according to their members' interests.

Section 3

We polled savers on how important they thought particular social and environmental issues were and what they thought were issues that would affect them in later life.. The findings show that people want their pension fund to prioritise financial returns, but they also recognise the importance of negative externalities. Furthermore they highlight variation among pension savers suggesting that pension funds should seek to understand the range of priorities across their membership

When asked to state three important factors that pension funds should take into account when investing in companies, the financial returns generated by the company for the pension fund was the most frequently chosen factor. However only 50% of respondents chose this option. Other factors considered important include:

- the pay and conditions of the company's workers (42%);
- the company's approach to human rights issues (37%);
- the amount of tax the company contributes (35%);
- the pay gap between the CEO and the rest of the company workforce (27%);
- the gender and ethnic diversity of the company's management (20%).

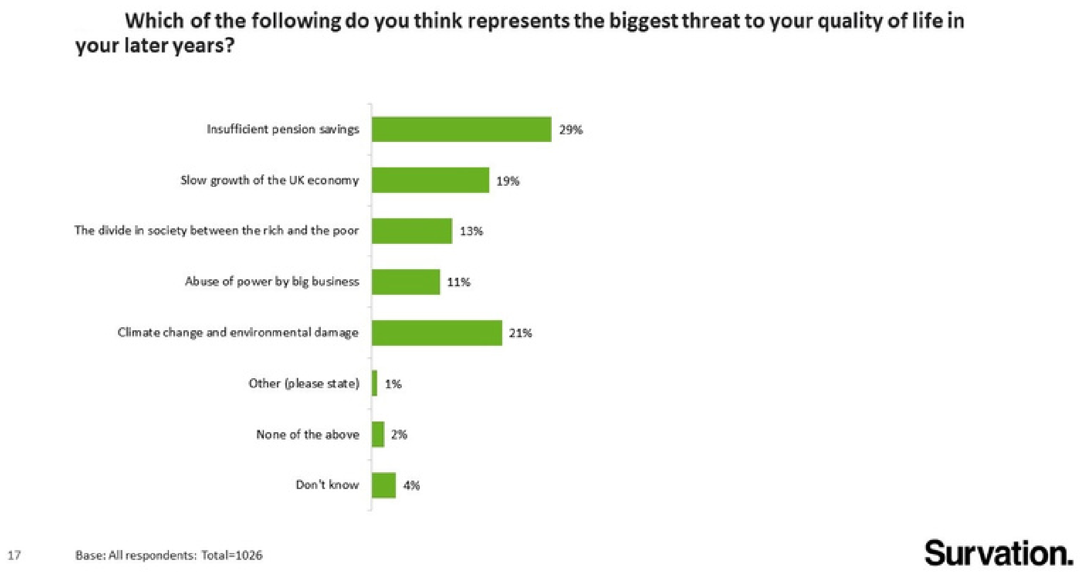


This provides an insight into the kind of issues that pension funds should be monitoring and engaging with at current and prospective investee companies.

Similarly, we asked pension savers what represents the biggest threat to their quality of life in their later years from a series of options.

Again, the most popular answer highlighted the importance of generating healthy returns from pension fund investments. Insufficient pension savings was seen as a risk by 29% of respondents. However, other issues were also seen as being almost as relevant, including:

- climate change (21%);
- slow growth of the UK economy (19%);
- divisions between rich and poor (13%);
- abuse of power by big business (11%).



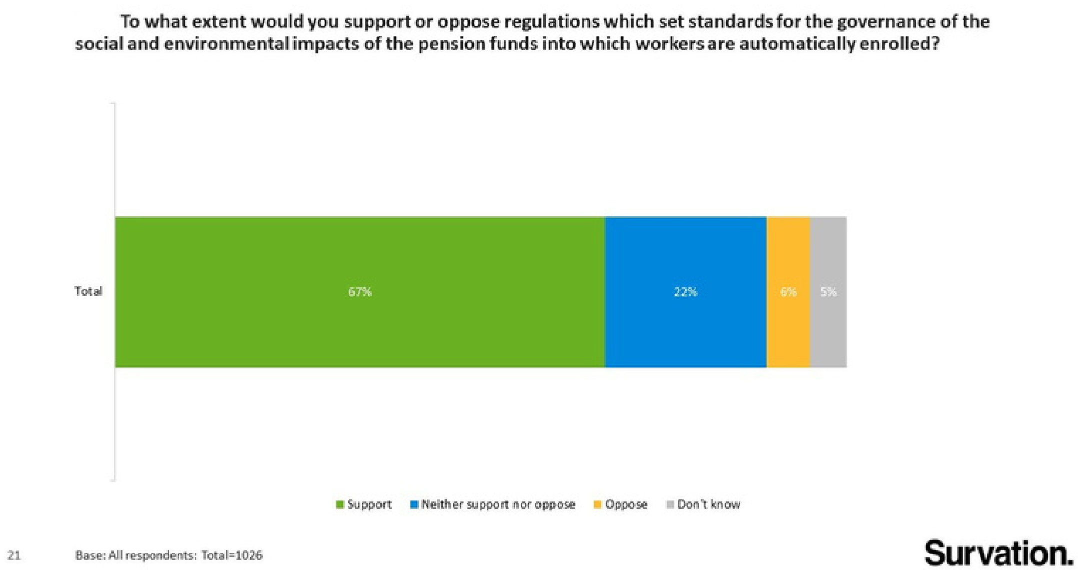
These responses suggest that most respondents recognise the importance of social, economic and environmental factors in determining the quality of their life and offer further evidence that pension fund's investments should be focused on the wider best interests of savers and not merely generating financial returns.

The issues covered by our polling, and the business practices that relate to them, offer some examples of the type of social factors on which pension funds should focus.

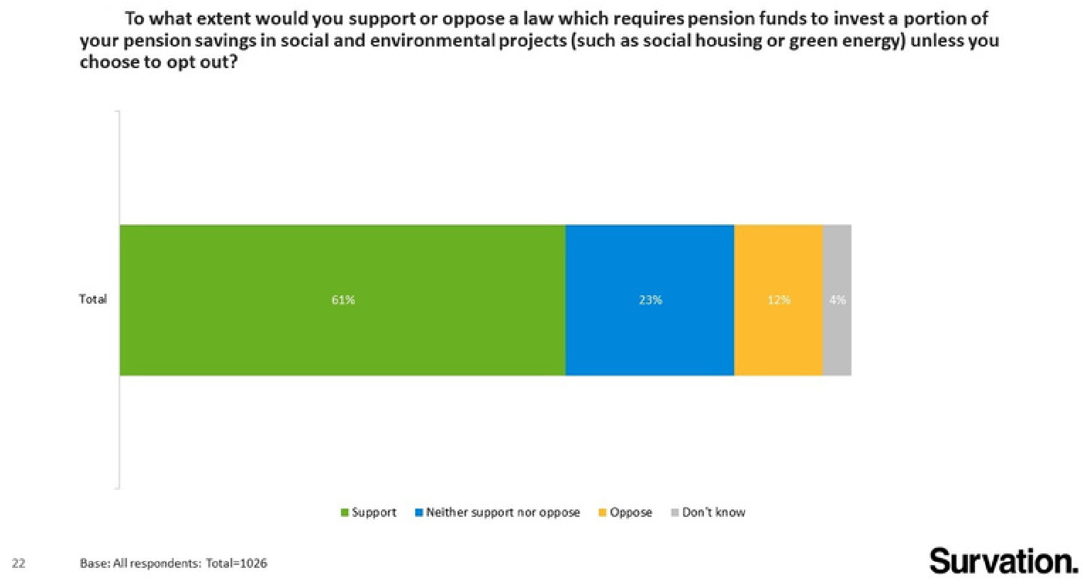
Section 4

Savers' responses to our polling demonstrate strong support for legislation and/or regulations to ensure more ethical investments from pension funds.

67% of those questioned said they supported regulations which set standards for the governance of the social and environmental impacts of the pension funds into which workers are already enrolled.



While 61% say that they would support a law, which requires pension funds to invest a portion of their pension savings in social and environmental projects, unless they choose to opt out.



Conclusion

Our findings suggest that people think companies' social and environmental records should be important determinants of where their pension savings are invested. This indicates that many savers either recognise the link between the employment and environmental practices of the companies they invest in and their own working conditions and wider environment, and/or don't want to be complicit in the mistreatment of workers or the environment by companies they have a stake in.

At the same time, the survey reveals limited understanding of pension funds investments, and a limited capacity to engage with pension funds on environmental or social issues. Responses show that assuming members will make their feelings known if their investments are contradicting their values or long-term interests is naive.

The findings have big implications for pension funds with control over trillions of pounds worth of investment. These investments shape the world we live in, and pension funds have a responsibility to use them to deliver the best possible outcomes for their members. Similarly, there are implications for the policymakers and regulators charged with ensuring that pension funds fulfil those responsibilities. In recent years, the notion of 'Environmental, Social and Governance' (ESG) investing has gained considerable prominence, and there is little doubt that pension funds and the investment industry more widely are - in general - increasingly engaging with environmental and social issues. But in a world in which around 10% of people live in extreme poverty and an estimated 5 million lives are already annually lost to climate change, there is considerable evidence to support the critics who argue that ESG has been more of a superficial marketing initiative than a genuine effort to align investment practices with the interests of people and planet.(6)(7) Deeper engagement by pension funds with their members, and incorporating a more holistic conception of members' interests into investment practices, will be a key way of answering these critics.

Endnotes

(1) Office for National Statistics (2018); Pensions in the national accounts, a fuller picture of the UK's funded and unfunded pension obligations: 2018. https://www.ons.gov.uk/economy/nationalaccounts/uksectoraccounts/articles/pensionsinthenationalaccountsafullerpictureoftheuksfundedandunfundedpensionobligations/2018

(2)Office for National Statistics (2019) Pensions, Savings and Investments. https://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/pensionssavingsandinvestments

(3) Department for Work and Pensions (2021) Consideration of social risks and opportunities by occupational pension schemes. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/972325/consideration-of-social-risks-and-opportunities-by-occupational-pension-schemes.pdf

(4) Katz, B (2017) Ryanair Business Model Under Pressure as Pilots Demand Collective Bargaining, Bloomberg. https://www.bloombergquint.com/onweb/ryanair-pilots-to-set-pay-demands-as-biggest-base-rejects-deal

(5) Kollewe, J (2021); Pharmaceutical firms' shares tumble after US plans patent waiver on Covid vaccines, Guardian. https://www.theguardian.com/business/2021/may/06/pharmaceutical-firms-shares-tumble-after-us-plans-for-patent-waiver-on-covid-vaccines

(6) World Bank Group (2021) Reversals of Fortune: Poverty and Shared Prosperity 2020. https://www.worldbank.org/en/publication/poverty-and-shared-prosperity

(7) Zhao, Q (2021); Global, regional, and national burden of mortality associated with non-optimal ambient temperatures from 2000 to 2019: a three-stage modelling study via The Lancet Volume 5, Issue 7, E415-E425 https://www.thelancet.com/journals/lanplh/article/PIIS2542-5196(21)00081-4/fulltext

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