European Pensions

Summer 2022

Pension saving:

Gender gap

How severe is the gender pension gap and what can be done to reduce it?

At retirement:

Decumulation

What options are on offer to savers in decumulation and what is the right mix?

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Subscription rates:
£198 or €299 per annum

www.europeanpensions.net

6th floor, 3 London Wall Buildings,
London, EC2M 5PD
ISSN 1753-5859

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Slava Ukraini!

As I sit here writing this issue's editorial comment, I am still elated at the results of this year's Eurovision Song Contest. The final of Europe's annual song and dance extravaganza took place on 14 May in Italy.

A song contest it may be, but frequently other factors come into play when voters choose their favourite performer. And whilst normally there may be frequent eye-rolling when, each year, you see one country vote for its neighbour, this year said eye-rolling was put aside as voters united in support for Ukraine.

Ukraine, which has been devastated by Russia's invasion, was crowned the winner following an outpouring of votes from people across Europe – in what has been hailed as a declaration of unity with the country.

It is not just Eurovision fans that have demonstrated their support for Ukraine, with people in communities around the world taking in Ukrainian refugees, or organising collections to help those displaced by the conflict. Pension funds took action to show their support by divesting from Russian assets – as much as they could before the Moscow Stock Exchange closed.

This year's Eurovision contest also demonstrated that perseverance is the key to success, with the UK placing second – its most successful result in a decade.

"PENSION FUNDS TOOK ACTION TO SHOW THEIR SUPPORT BY DIVESTING FROM RUSSIAN ASSETS"

Perseverance is also ever present within pensions – whether that be the industry, members or even politicians. Take our cover feature on page 22, for example, which examines the French pension system. President Emmanuel Macron has recently been elected for a second term and is determined to reform the country's pension system, despite big opposition.

Our feature on page 38 considers the decumulation journey for those retiring. With defined contribution schemes becoming more popular, the decumulation stage will become even more important. Whilst not perfect yet, the industry is working hard on finding solutions and products to meet individual needs.

Finally, our feature on the pensions gender gap [*page 44*] looks at the need for perseverance to narrow the gap between men's and women's pension savings. There is no quick fix and it's not just a job for the pensions industry but society at large. What is clear, is that the messages from Eurovision of unity and perseverance are needed more than ever.

Natalie Tuck, Editor

European Pensions has agreements with several associations to reach their membership. For details contact john.woods@europeanpensions.net

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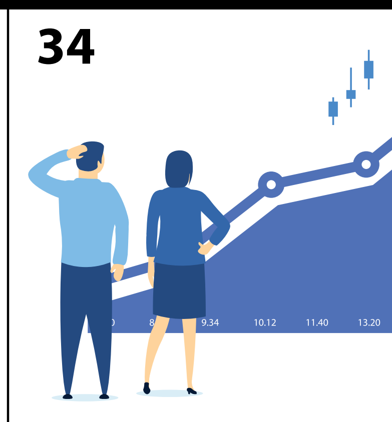

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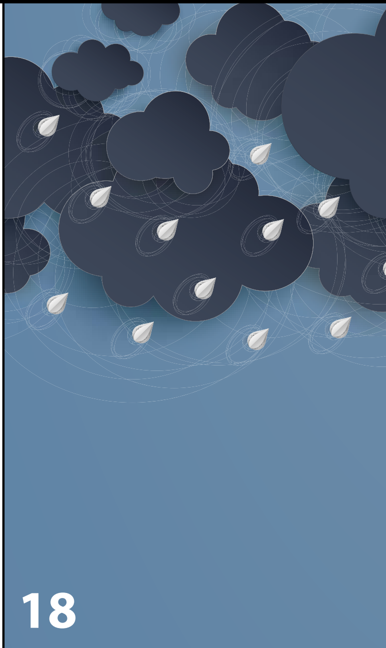

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EIOPA launches consultation on IORPs reporting rules

EIOPA AIMS TO IMPROVE IORPS' RISK REPORTING

Written by: Natalie Tuck and Jack Gray

The European Insurance and Occupational Pensions Authority (EIOPA) has launched a public consultation regarding its regular information requests to national competent authorities (NCAs) for occupational pension information.

The aim of the public consultation is to improve institutions for occupational retirement provisions' (IORPs) reporting, focusing on emerging risks and new challenges and issues observed by NCAs and the pensions industry since its first implementation in 2018.

In the consultation package, EIOPA has proposed amending its current decision by including the provision of the following information: Derivative information to assess actual hedging of various types of risks and how this impacts IORPs risks; cashflow information to calculate comparable and market-consistent values of IORPs' defined benefit liabilities; high-level look-through data on IORPs' investments in UCITs to obtain a complete picture of IORPs' assets and risk exposures; cross-border data by host country to get an accurate picture of the cross-border relationships; and detail on the NACE code, allowing for better assessment of environmental, social and governance (ESG) risks.

Finally, alignment of taxonomies between reporting frameworks, where relevant, was also considered. The alignment follows the principles of the strategy on supervisory data in European Union (EU) financial services defined by the European Commission and should ultimately lead to the reduction of costs for NCAs, reporting entities and EIOPA.

EIOPA has invited stakeholders to provide comments to the public consultation via EU survey by 18 July 2022.

The authority has also launched its first climate stress test to gain insights into the effect of environmental risks on the European occupational pension sector.

Sustainability and the management of environmental risks have become key considerations for long-term investors and in particular for European IORPs.

The 2022 IORP stress test is testing the resilience of European IORPs against a climate change scenario, which was developed together with the European Systemic Risk Board and the European Central Bank.

It reflects a sudden, disorderly transition to climate neutrality due to delayed policy action, which results in a sharp rise in carbon prices. This abrupt carbon price increase triggers transition risk effects to the entire economy.

The stress test focuses on the impact on IORPs' investments, yet also addresses the effects on IORPs' financial situation, including the financing by sponsoring undertakings. Therefore, the climate change scenario is applied to the balance sheet – both national valuations and the common balance sheet.

The scenario sets out sector-specific shocks that provide insights into IORPs' investment portfolios, reflecting the corresponding impairment of the investments, broken down by the most relevant sectors and business activities.

The exercise also includes two specific questionnaires, one to request information following up on the ESG analysis of the 2019 IORP stress test, and another one to allow an analysis to identify and understand the potential effects of inflation on members' and beneficiaries' retirement income, focusing on the extent to which scheme characteristics and national frameworks provide for mitigating measures or

adaptations to protect against inflation.

The results of the stress test are expected to be published in December 2022.

Earlier in the year, EIOPA published its *Supervisory Convergence Plan for 2022*. The plan outlined EIOPA's priorities to enhance supervisory convergence over the course of the year, in line with its mandate to build a common supervisory culture and consistent supervisory practices in the EU.

Its priorities revolve around three 'main areas': common supervisory culture and tools, risks to the internal market and level playing field, and supervision of emerging risks.

EIOPA will continue working on proportionality, supervisory assessments of conduct risks, ESG issues, and group supervision.

With regard to pensions in the area of risks to the internal market and the level playing field, which may lead to supervisory arbitrage, EIOPA will initiate work to establish and address supervisory concerns arising from the recent market development of multi-sponsor IORP providers.

"This work will include fieldwork to better understand providers' different business models and NCAs' supervisory practices in respect of these IORPs"

It noted that the IORP II Directive provided minimum prudential requirements focusing largely on the traditional image of non-commercial purpose IORPs set up by a single sponsor or multiple sponsors of the same sector.

Although it acknowledged that multi-sponsor IORP providers had an "important role to play" to drive market consolidation and provide efficient, low-cost solutions in countries seeking to develop occupational pensions, they also bring new supervisory questions in respect of the governance and risk management.

"This work will include fieldwork to better understand providers' different business models and NCAs' supervisory practices in respect of these IORPs and will take into consideration the proportionality principle," EIOPA stated.

In other news, the Joint Committee of the European Supervisory Authorities (ESAs), which includes the EBA, EIOPA and ESMA published a report detailing its joint work in 2021.

The *Annual Report 2021* revealed that the Joint Committee, under ESMA's chairmanship in 2021, continued to play a central role in the coordination and exchange of information between the ESAs, the European Commission (EC) and the European Systemic Risk Board (ESRB).

A significant part of its work in 2021 focused on developing the regulatory and supervisory framework for sustainability-related disclosures. This included the delivery of two sets of draft Regulatory Technical Standards (RTS) under the Sustainable Finance Disclosure Regulation (SFDR).

News in brief

■ Nordea has agreed to acquire Topdanmark Forsikring's life and pensions business, Topdanmark Life, for €270m. Topdanmark Life is a life and pension company in **Denmark** with assets under management of around €12bn at the end of 2021 and approximately 225,000 customers. The business will be integrated into Nordea. The agreed price for Topdanmark Life is around €270m after a pre-completion dividend has been distributed to Topdanmark.

■ The **Swedish** Pensions Agency reported a strong return for funds in the country's premium pension system in 2021. It said the rise in the stock markets had a positive effect on the value of premium pension funds. The average value development for savers in the premium pension was 29.6 per cent in 2021. Those who remained in the state pre-selection alternative AP7 Såfa had an average value development of 31.2 per cent.

■ **Norway's** Government Pension Fund Global returned -4.9 per cent in the first quarter of 2022, equating to a loss of NOK 653bn, NBIM has revealed. Its return was 0.66 percentage points stronger than the return on the benchmark index.

■ Pension representatives from **Slovenia** have visited several Swedish institutions to learn about best practices in pension communication, as part of a project by the Organisation for Economic Co-operation and Development. The delegation included civil servants, mainly from the Ministry of Labour, Family, Social Affairs and Equal Opportunities and the Slovenian Pension Agency.

Dutch pension system reform a step closer with legislative proposal

THE FUTURE PENSIONS ACT HAS BEEN SUBMITTED TO THE HOUSE OF REPRESENTATIVES

Written by: Natalie Tuck

A major reform of the Dutch pension system is a step closer following the submission of the legislative proposal.

Pensions Minister, Carola Schouten, has sent the Future Pensions Act to the House of Representatives. The Federation of Dutch Pension Funds said it is "an important step towards a future-proof pension system".

Aon Netherlands has also welcomed the "milestone" being reached and noted that the bill is largely in line with the consultation document, with changes relatively limited.

Federation of Dutch Pension Funds chairman, Ger Jaarsma, said: "It is good to see that parliament can now consider this important system change. The new system makes it clearer what pension funds do for members: invest the contributions paid in and make more of them.

"Those returns on investments will flow back more directly to the accrued pensions. Participants can see this effect on their pension statements and because we are moving from a pension commitment to a pension expectation, pension funds no longer have to calculate how much capital they should keep in cash on the basis of a risk-free interest rate. That makes the pension system simpler and the assets in the funds are released sooner."

Jaarsma added that the federation is pleased to see improvements when compared to the consultation document.

"Explainability and feasibility are the most important themes, as is sufficient scope for pension fund directors to make choices that are in the interest of their specific group of participants. Now it's time for the next step. Pension funds have already started preparations. They can now also make concrete choices with social partners that suit their participants. In this way we can all make a success of this transition to a future-proof pension system."

The new system is expected to enter into force on 1 January 2023.

In other news, the average funding ratio of Dutch pension funds increased to 122 per cent in April, according to Aon Netherlands.

Aon's Pensions Thermometer also found that the policy funding ratio, based on the average funding ratio over the past 12 months, remained stable at 112 per cent.

Over the month interest rates rose sharply again, particularly towards the end of the month. Over the first 40 years, the yield curve rose by more than 40 basis points. Due to the higher interest rates, liabilities have fallen. On balance, liabilities fell by more than 8 per cent.

Markets were dominated by sharp rises in interest rates in April, anticipating possible actions by central banks due to high inflation.

Despite the fact that companies showed decent profit figures, future expectations are uncertain due to inflation and geopolitical tensions. Developed market equities and also listed real estate fell more than 5 per cent, in contrast to the small 1 per cent decline for emerging markets.

Only commodities showed a positive return of almost 8 per cent, with the strong rise in the US dollar of 4.8 per cent contributing about half. Rising interest rates once again led to negative corporate bond yields this month (-2.7 per cent). Long-term interest rates rose, causing the entire fixed-income portfolio to fall by more than 9 per cent. On an overall level, the portfolio achieved a negative return of approximately 6 per cent.

Pension returns 'favourable' in 2021; Swedish schemes lead for second year

SWEDISH PENSION INVESTORS CAME OUT ON TOP OF ANALYSIS CONDUCTED BY ETK

Written by: Sophie Smith and Natalie Tuck

Swedish pension investors delivered the strongest returns amid the global economic recovery following the Covid-19 pandemic, according to research from the Finnish Centre for Pensions (ETK).

The comparison, which included 24 pension investors from Northern Europe, North America and Asia, found that most schemes reached a real return of 10-20 per cent in 2021, with real returns on the US stock market highlighted as particularly favourable.

However, for the second year in a row, Swedish public pension scheme, AP6, secured the highest return of 46.2 per cent, thanks to its equity-only investments and specialisation in unlisted high-risk instruments.

This was followed by Sweden's AP1, AP3 and AP4 schemes, which delivered returns of 18.4 per cent, 18.3 per cent and 16.9 per cent, respectively, having benefited from a large rise in the evaluation level of domestic equities and the weak Swedish krona in relation to the dollar and the euro.

Despite this, ETK noted that Finnish pension investors have made a steady return and fared better in this year's comparison than in previous years.

Earnings-related pension provider, Varma, for instance, recorded the largest real return amongst earnings-related pension providers and company pension funds at 16.2 per cent, whilst Keva showed the highest return amongst Finnish buffer funds, at 13.5 per cent.

In addition to this, the average real return of Finnish earnings-related pension providers and company pension funds was higher than that of foreign pension investors subject to similar solvency regulations, at 13.1 per cent compared to 9.3 per cent.

Furthermore, whilst the average real return of Finnish buffer funds fell behind that of their foreign counterparts, at 12.6 per cent compared to 17.4 per cent, ETK said that this gap relates to the AP6 buffer fund, without which the return of Finnish buffer funds would be on the same level as that of foreign buffer funds.

ETK also noted that whilst Denmark's ATP delivered the weakest return of -1.8 per cent, this was "for an obvious reason", as the investment allocation of this earnings-related pension fund differs from that of all other pension funds, as it is focused on fixed-income securities.

Also considering a more long-term period, the survey revealed that the largest real return in 2012-2021 was 12.7 per cent from the Swedish buffer funds AP6, and 10.7 per cent for AP4.

The average annual return of the Finnish pension investors was 6.4 per cent during this period, which ETK noted was at the same level as that of some of the other actors included in the comparison, such as Alecta, PFZW and ABP.

In other news, the average solvency ratio of Finnish earnings-related pension providers stood at 136.3 per cent at the end of 2021, according to data published by the Finnish Financial Supervisory Authority.

The solvency ratio is calculated by dividing pension assets by technical provisions. The end-December 2021 figure is a 1.5 percentage point increase on the solvency ratio at the end of September 2021, which stood at 134.8 per cent.

The pension insurance companies' average solvency ratio was 135.8 per cent, while that of company funds and industry-wide funds was 152.6 per cent.

Earnings-related pension providers comprise of private-sector pension insurers, i.e. pension insurance companies, company pension funds and industry-wide pension funds.

Danish Pension Commission publishes report on improving pension system

ITS RECOMMENDATIONS INCLUDED INCREASING THE AMOUNT OF TIME SAVERS COULD CONTRIBUTE A HIGHER AMOUNT

Written by: Natalie Tuck

Denmark's Pension Commission has published a report with recommendations for improving the country's pension system, which Insurance and Pension Denmark (I&P Denmark) has welcomed.

The commission was set up in November 2020 to make recommendations for the pension system of the future. This report has now been submitted to the government and the parties behind the pension agreement.

I&P Denmark said it welcomes the long-awaited recommendations and hopes that politicians follow up on proposals to improve incentives to save for retirement, which is crucial for future-proofing the Danish pension system.

I&P Denmark CEO, Kent Damsgaard, said: "We completely agree with the Pension Commission that there is a need for a unified, sharp and independent pension policy in Denmark, so that in the future we still have one of the world's best pension systems.

"The commission has looked at the pension system at the seams, and they, like us, are concerned with improving the incentives to save for retirement and making the individual Dane's withdrawal from the labour market more flexible.

"We are pleased that the Pension Commission is proposing to improve old age savings... It is also quite obvious that politicians could make it possible to pause an instalment pension so that able-bodied seniors can return to work without being penalised financially."

The commission has proposed to improve pension savings by removing the set-off when contributing to old-age savings. It has also proposed to allow pension savers to contribute a higher amount for seven years, rather than the current five years, which provides more incentive to save for retirement.

This will mean that the so-called real effective marginal tax will fall from more than 80 per cent to just over 25 per cent. I&P Denmark estimates that there are around 22,000 more people who will benefit from being able to pay the high amount into old-age savings in the future.

"It is absolutely central to the pension system that it pays to save for retirement, so the proposal really hits the spot," Damsgaard said.

However, the commission is also proposing savings of 3.3 per cent of the income of employees and the self-employed who do not save for retirement themselves. According to I&P Denmark's assessment, this will result in a modest contribution to the maintenance in retirement of approximately DKK 1,300 per month after a full working life savings. A regular pension scheme of at least 12 per cent, which is the norm in virtually the entire labour market, is a much better solution, the association said.

"A savings of just over 3 per cent is not an alternative to regular pension savings, but if the proposal becomes a reality, it may contribute to more Danes considering the importance of having real pension savings. Therefore, it is clear that this new minimum savings scheme could be offered by the well-known pension companies," Damsgaard said.

Danish Minister for Employment, Peter Hummelgaard, added: "I would like to thank the commission for a great deal of work in thoroughly analysing the Danish pension system. I and the government look forward to reading the recommendations closely. The Danish pension system is unique in the world and I note that the commission agrees."

Macron 'ready to change timeline' on pension reforms

DURING HIS ELECTION CAMPAIGN, MACRON SAID HE WAS WILLING TO CHANGE THE TIMELINE ON PROPOSED REFORMS, INCLUDING INCREASING THE COUNTRY'S RETIREMENT AGE

Written by: Natalie Tuck

French President Emmanuel Macron said he was "ready to change the timeline" on his planned pension reform, when he entered the final round of the French general election against Marine Le Pen.

As reported by *Reuters*, Macron made the comments on his plans for pension reform whilst campaigning. He announced his plans for reform in March, which included increasing the country's retirement age to 65, up from 62.

It was also reported that he wants the minimum pension to be set at €1,100 a month. This would be a significant increase for some pensioners, such as agricultural workers, who often receive €300-€400 currently.

Whilst campaigning, Macron said: "I am ready to change the timeline and say we don't necessarily have to do a reform by 2030 if I feel that people are too anxious." He was also prepared, he said, to "open the door" on pushing the country's retirement age from 62 at the moment to 64, rather than 65, his initial proposal.

Picture source: Frederic Legrand - COMEO / Shutterstock.com

Pension reform in France is a contentious issue; prior to the pandemic, Macron was met with numerous strikes and protests at his plans to reform the country's pension system. The plans were dropped when the pandemic began but Macron has expressed his wishes to push through the reforms several times since then.

Pension funds announce intention to sell Russian assets

A LONG LIST OF EUROPEAN PENSION FUNDS HAVE EXPRESSED THEIR INTENTION TO SELL RUSSIAN ASSETS, INCLUDING AP7, ABP, NBIM AND AKADEMIKERPENSION

Written by: Natalie Tuck

Several pension funds have joined the long list of those excluding Russian assets from their portfolios, following Russia's invasion of Ukraine.

The Netherlands' PMT, Norway's KLP and Sweden's PP Pension have all published statements detailing their intention to sell Russian assets when it is possible. All of the funds already have very limited exposure to Russian assets.

Pension funds that have decided to exclude Russia, however, have struggled to sell assets due to the closure of the Moscow Stock Exchange and foreign players have been banned from conducting transactions.

In a statement PMT said: "PMT decided today (8 March) to sell its remaining shares in Russia as soon as circumstances permit. The decision was taken after an analysis of the possible consequences. We want to prevent potential negative impacts on the Russian population in terms of their basic necessities by selling the shares.

"However, since PMT currently has no instruments to verify this, such a consideration on an individual basis (per company) is not feasible. In view of the seriousness of the situation and the limited influence on the situation in Ukraine, PMT decided to sell all shares."

Norway's KLP said the decision to withdraw investments in Russia was made on 28 February – leading to the exclusion of 22 companies.

Ireland's Pensions Authority sets out three-year strategy; key focus on consolidation

THE AUTHORITY SAID IT PLANNED TO REVIEW THE STRATEGY AT THE END OF 2023

Written by: Natalie Tuck

Ireland's Pensions Authority has published its strategy for the next three years, setting out its objectives for the Irish pensions industry, including the consolidation of schemes.

Its *Statement of Strategy 2022-2024* covers its vision, mission and values, the operating context, strategic objectives and enablers, as well as its culture statement. The authority plans to review the strategy at the end of 2023. A key focus of this will be to determine how many schemes have wound up and transferred members and assets to multi-employer schemes or to personal retirement savings accounts (PRSAs).

"If the numbers of schemes are not reducing significantly, we will have to assess whether a new or revised strategy is required to achieve our objectives," the authority stated.

Within its statement, the authority said that it will not be "practical or economic" for many schemes to comply with the new obligations brought in with the IORP II Directive. It added that it would not be practical for the authority to apply forward-looking risk-based supervision to tens of thousands of pension schemes.

"It is difficult to see how trustee compliance and forward-looking risk-based supervision can be achieved without considerable consolidation of pension schemes," the report stated.

One of its main strategic objectives is for the Irish pension system to comprise stable and sound occupational pensions that are well managed to appropriately high standards.

Commenting on the launch of the strategy, the Pensions Regulator, Brendan Kennedy, said: "The authority's most important role is the supervision of scheme trustees and PRSAs. This strategy sets out how we intend to undertake our work over the next three years.

"The transposition of the IORP II directive into Irish pensions law represents significant change for Irish pensions and for the authority. The obligations on scheme trustees are much more demanding and complex than they have been before. As a result, the work of the authority has also become more challenging and extensive.

"The legislation obliges us to supervise schemes on a forward-looking risk-based supervisory basis, which will result in more challenging, judgement-based, and intrusive oversight. As well as our supervisory responsibilities, the authority will be expected to provide much more information and guidance than in the past and to make clear what its expectations are of regulated entities."

In other news, Kennedy has stated that Irish pension trustees' own risk assessment (ORA) is their "most important responsibility".

Speaking at the Society of Actuaries in Ireland pension forum, Kennedy said that the ORA should be at the centre of trustees' consideration.

"My own view is that it is possibly the most important responsibility of trustees and if it is done properly, many of the other aspects of trustee responsibilities will fall into place," he said. The requirement for an ORA was introduced with the transposition of the IORP II Directive and is set out in the Pensions Authority's *Code of Practice.*

However, Kennedy has detailed four ways in which an ORA can fall short. These centre around the comprehensiveness of the OEA, a lack of information to support it, a lack of objectiveness from trustees and ORA conclusions not being implemented.

GPFG has divested from 366 companies since 2021 - NBIM

IN ADDITION TO THE DIVESTMENTS, THE BANK SAID IT HAS STRENGTHENED ITS EXPECTATIONS OF COMPANIES AND FOLLOWED UP THROUGH DIALOGUE

Written by: Natalie Tuck

Norges Bank Investment Management (NBIM) has detailed its work on responsible investment over the past year, including its 366 divestments since 2021.

Publishing its eighth report on responsible investment, the fund said that it has strengthened its expectations of companies and followed up through dialogue.

NBIM, which is responsible for the investments of Norway's Government Pension Fund Global (GPFG), said it has had high activity in its work on responsible investment throughout the year. Its primary tool is to influence companies through dialogue and voting.

Despite this, in 2021 NBIM carried out risk-based divestments in 52 companies and, in total, carried out divestments in 366 companies since 2021.

In addition, NBIM has increasingly developed better methods for identifying companies with high risk relating to the environment, social conditions, and corporate governance. In particular, it has considered companies exposed to risk relating to biodiversity, workers' rights, tax and transparency, and corruption.

When dialogue is not successful, NBIM said risk-based divestment might be appropriate. The number of risk-based divestments in 2021 is the second-highest it has had since it started doing this.

Call for pension fund exemption from shell entity tax directive

PENSIONSEUROPE HAS CALLED FOR PENSION FUNDS TO BE EXEMPT FROM A EUROPEAN COMMISSION DIRECTIVE AIMED TO PREVENT THE MISUSE OF SHELL ENTITIES FOR TAX PURPOSES

Written by: Natalie Tuck

Pension funds should be exempt from a European directive that sets out rules to prevent the misuse of shell entities for tax purposes, according to PensionsEurope.

In feedback to the European Commission on its proposal for a council directive to lay down such rules, amending Directive 2011/16/EU (COM(2021) 565, PensionsEurope said it supports the aim of preventing the use of legal entities and arrangements without minimal substance for tax avoidance or tax evasion purposes.

However, the association said that certain adjustments to the proposal are "necessary" to ensure that pension funds and the investment structures they use do not incorrectly fall within the scope and be impacted unintendedly.

"First, although in practice pension funds would not pass the envisaged gateway criterion as they do not present any risk of lacking substance for tax purposes, we believe they should anyway be excluded from the scope for purposes of legal certainty.

"In our opinion, all pension funds should be included in the exemption from the scope of application of this directive provided by Article 6.2, which excludes from the envisaged rules some entities that do not present tax avoidance risks, including 'regulated financial undertakings'," the association said.

In addition, PensionsEurope believes that certain investment structures/entities used by alternative investment funds, such as private equity funds, should also not fall under the scope of the proposed directive.

"These structures are used by pension funds to ensure tax neutrality, to have more flexibility in choosing the preferred risk and structure of the investment, to facilitate easier exit and create greater returns for their members and beneficiaries, and to have more certainty regarding insulation from legal liabilities."

News in brief

■ **Canada's** Ontario Teachers' Pension Plan (OTPP) has partnered with Corio Generation to support the development of up to 9GW of offshore wind worldwide. OTPP will invest up to USD 1bn in development capital. The portfolio will consist of 14 fixed bottom and floating projects in South Korea, Taiwan, Japan, Ireland and the UK, all of which are currently under development by Corio. OTPP will acquire up to half of Corio's stake, supporting development, construction and operation.

■ The **US** Securities and Exchange Commission (SEC) has upheld a shareholder proposal that called for Amazon to publicly disclose global tax practices, payments and risks to investors. In December 2021, Amazon submitted a no action request to the SEC, challenging the shareholder proposal filed by the OIP Trust and Greater Manchester Pension Fund with the support of Pensions & Investment Research Consultants. The shareholder proposal requested that the company disclosed global tax practices by reporting in line with the new Global Reporting Initiative Tax Standard.

■ **AustralianSuper** has acquired half of British Land's interest in the Canada Water Masterplan for GBP 290m and the two have agreed to form a 50/50 joint venture to accelerate the development's delivery. The 53 acre site will be a net-zero carbon development providing 3,000 homes, workspaces for 20,000 workers and extensive open spaces protecting historical wetlands and woodlands.
The investment is part of AustralianSuper's strategy to more than double its UK assets from c. GBP 7bn to GBP 15bn by 2026.

AustralianSuper to increase private equity investments by AUD 13bn

THE PENSION FUND HAS COMMITTED TO MAKING THE INVESTMENT OVER THE NEXT TWO YEARS

Written by: Jack Gray

AustralianSuper has announced that it will invest a further AUD 13bn into private equity globally over the next two years, with the aim of helping to deliver strong long-term returns for members.

AUD 9.5bn of this capital has been earmarked for investment in the US, where the fund is targetting a range of sectors including healthcare, technology, industrials, consumer and financials.

AustralianSuper head of private equity, Terry Charalambous, said the fund will increase its allocation to private equity from 5 per cent to 7 per cent by 2024 as part of AustralianSuper's strategy to increase its investment in unlisted assets.

The fund's overall private equity investment will rise to AUD 26bn over the next two years to help drive AustralianSuper's long-term performance.

AustralianSuper's private equity portfolio is expected to be AUD 50bn within five years.

"To help implement the fund's strategy, our US-based private equity team will grow to 20 members in the next few years, focused on strengthening relationships with well-aligned investment partners and sourcing compelling long-term investment opportunities," Charalambous said.

Canadian funds linked with fossil fuels

REPORT FINDS LINK BETWEEN PENSION FUNDS AND FOSSIL FUEL FIRMS

Written by: Jack Gray

A report from Shift: Action for Pension Wealth and Planet Health has highlighted potential conflict of interest concerns between Canadian pension funds and the fossil fuel industry.

It found that among Canada's 10 largest pension funds, 80 different pension directors, trustees, executives and senior staff currently hold or previously held 124 different roles with 76 different fossil fuel companies.

This includes nine current pension fund directors or trustees that currently hold 13 roles on the board of directors of 12 different fossil fuel companies, and 56 senior staff or investment managers at pension funds who hold 76 different corporate director roles at 39 different fossil fuel companies.

Seven of the 10 pension funds have at least one board member who simultaneously sits on the board of a fossil fuel company. In some cases, over a quarter of some pension fund boards have direct connections to the oil and gas industry.

The report noted that the overlap raised "serious questions" about pension administrators' abilities to objectively manage climate-related financial risks and make critical climate-related investment decisions when they are "deeply entangled" with the fossil fuel industry.

Diary dates 2022

The latest events occurring across the European pensions market

EUROPEAN PENSIONS AWARDS
7 July 2022
London Marriott Hotel, Grosvenor Square, London
Now celebrating their 15th year, the European Pensions Awards are a celebration of the hard work and dedication displayed by pension schemes and providers from across Europe. The evening gala, to be held at the prestigious London Marriott Hotel, will honour the investment firms, consultancies and providers from across Europe who have displayed excellence, innovation and a genuine passion for providing exceptional service in everything they do.
europeanpensions.net/awards/

PENSIONS AGE AUTUMN CONFERENCE
15 September 2022
Waldorf Hilton Hotel London
This one-day conference, which is open to pension scheme managers, trustees, FDs, advisers, pension and HR professionals, will offer delegates the up-to-date knowledge and guidance they need to help them run their pension schemes and meet their members' needs, whether in the DB, DC or hybrid space. A firm favourite in the UK pensions sector, those working in the industry will have the opportunity to learn and network alongside their peers.
pensionsage.com/autumnconference

IRISH PENSIONS AWARDS
3 November 2022
Shelbourne Hotel, Dublin
Entering their 11th successful year, the Irish Pensions Awards continue to go from strength to strength. These awards aim to give well-deserved recognition to those pension funds, pension providers, advisers and pension professionals who strive to maintain the highest standards of excellence, dedication and professionalism in everything they do, despite the challenging economic and political landscape that many businesses have found themselves operating in.
europeanpensions.net/irishawards/

Not to miss...

PENSIONSEUROPE ANNUAL CONFERENCE
9 June 2022
Online
pensionseurope.eu/public-events

SPS ESG & IMPACT INVESTING FOR DUTCH PENSION FUNDS
28 September 2022
Amsterdam
spsconferences.com/conference-calendar

PLSA ANNUAL CONFERENCE 2022
12-13 October 2022
Liverpool
plsa.co.uk/events

IAPF INVESTMENT CONFERENCE WEEK
18-20 October 2022
Hybrid - Online and in-person
iapf.ie/events

People on the move...

The latest news and moves from people within the European pensions industry

If you have any appointments to announce please contact natalie.tuck@europeanpensions.net

ELINA HELIÖ

Finland's Elo has appointed Elina Heliö as its director of people and culture and she will also become a member of the management team. Commenting on the appointment, Elo CEO, Carl Pettersson, said: "Elina Heliö will play a significant role in the position of director of people and culture, which is new to Elo's management team. She will be responsible for Elo's HR services, legal affairs, public relations and communications."

BIRGITTE BRYNE

Norges Bank Investment Management (NBIM) has appointed Birgitte Bryne as chief technology and operating officer. She joined NBIM in 2015 as global head of investment administration. Bryne currently serves as chief operating officer for NBIM – a role she has held since 2020. Bryne is taking on the new role as the Norwegian bank is merging its technology and operations areas.

OLE KROGH PETERSEN

PFA's board of directors has appointed Ole Krogh Petersen as the group CEO at PFA. Krogh Petersen will take up the position on 1 December 2022 and joins from Danica Pension where he served as CEO. PFA chairman of the board, Peder Hasslev, described the appointment: "Ole and PFA are a good match. He has great experience and vast competencies within the pension area."

MARKUS AHO

Finnish earnings-related pension provider, Varma, has appointed Markus Aho as its chief investment officer, commencing on 1 June. At the same time, Aho will become a member of Varma's management team, and he will report to Risto Murro, president and CEO. Aho also worked as Varma's vice president, private equity. Prior to his career at Varma, he worked at Pontus as head of private equity before joining Varma in 2014.

INGRID BONDE

Alecta has re-elected all its members to the board at the board of directors' meeting on 12 April 2022. Ingrid Bonde has been re-elected as the chairman of the board. The 10 ordinary board members are Hanna Bisell, Marcus Dahlsten, Martin Fridolf (who replaced Helena Hedlund during the year), Markus Granlund, Ann Grevelius, Petra Hedengran, Jan-Olof Jacke, Magnus von Koch, Martin Linder and Richard Malmborg.

MICHIEL DELFOS

Michiel Delfos has been appointed as a member of the executive board and chief risk officer of Achmea, filling the vacancy that arose after Henk Timmer stepped down. Delfos joined Achmea in early 2014 as director of property and casualty insurance. In October 2015, he became chairman of the non-life division. Delfos had previously held various management and board positions at Delta Lloyd and ABN AMRO Verzekeringen.

HOLM DIEZ

Holm Diez has been appointed to HDI Germany's board of management, taking over the position from Iris Kremers when she steps down from the position on 1 July due to personal reasons. Diez had been respobsible for the sales department at Neue Leben since 2017 where his areas of responsibilty included expanding cooperation with savings banks in Germany and establishing new products on the market.

MARC VAN NULAND

Aon Netherlands CEO, Marc van Nuland, has taken on a new role as chairman of Aon Netherlands. In addition to this new role, Van Nuland will continue his role as board member of the Dutch Insurance Exchange Association (VNAB). Until further notice, he will continue to lead the Dutch executive team and, together with Eduardo Dávila, CEO Aon EMEA, will ensure a smooth transition for a new CEO to be appointed.

MAARTEN BLACQUIÈRE

Maarten Blacquière has been appointed to the executive board of APG Group as chief finance officer, responsible for the quality and implementation of APG's financial policy and risk management as well as the company's IT strategy. Blacquière brings experience from various management, operational and staff positions with the energy sector over the past 30 years.

MARTIN PRÆSTEGAARD

The board of Denmark's ATP has backed the election of Martin Præstegaard as CEO. Præstegaard, who has served as deputy CEO since September 2019, will replace Bo Foged, taking up the position on 1 July 2022. The Danish Financial Supervisory Authority has approved Martin Præstegaard as fit and proper. ATP chairman of the board, Torben M. Andersen, said Præstegaard is "extremely competent and well-suited to handle the important task".

KATI KORHONEN-YRJÄNHEIKKI

Elo has appointed Kati Korhonen-Yrjänheikki as director of work ability, a new position within the company. Korhonen-Yrjänheikki will begin her work with Elo on 1 June. Commenting on the role, Elo CEO, Carl Pettersson, said: "Kati will play a significant role in finding new ways to prolong our careers and developing Elo's services to support the work ability of our customer companies."

GUEST COMMENT

Weathering the storm

The comparison made by the Finnish Centre for Pensions (ETK) shows that investment returns of major Finnish earnings-related pension providers continued to be strong during the second Covid-19 year of 2021. This was also the case for most of the pension investors from Europe, North America and Asia included in the study

WRITTEN BY FINNISH CENTRE FOR PENSIONS SPECIAL ADVISER, ANTTI MIELONEN, AND LIAISON MANAGER, MIKA VIDLUND

The importance of funding and asset returns has gained increasing importance in recent years. This is driven by population ageing and the associated growth of pension expenditure. For example, in Finland pension expenditures have, for some years, exceeded pension contribution income. This gap is financed by asset returns. In the Finnish case, a one percentage point increase in the long-term real return will decrease the contribution pressure by two percentage points.

The years of the Covid-19 pandemic in 2020-2021 have yielded better-than-expected and, as far as 2021 is concerned, even record-high returns. The common factor for those with high returns were excellent results of their private equity and alternative investments. For example, the highest return in real terms, around 46 per cent, was achieved by the Swedish buffer fund AP6 that invests only in high-risk instruments. The average real return for all investors included in the comparison was 13.7 per cent.

Listed shares also gained in general double-digit returns during 2021. Behind AP6, the following three places went to the Swedish buffer funds: AP1 (18.4 per cent), AP3 (18.3 per cent) and AP4 (16.9 per cent). Even though these funds adhere to stricter regulations than AP6, they benefited from the booming Swedish stock market and the weakening krona, especially in relation to the dollar.

Despite excellent returns during the past year, pension investments should be reviewed with a longer horizon. Fittingly, there is a saying that in pensions one quarter refers to 25 years. Our comparison does not reach that far. However, we include 10-year returns, and arguably this is a more important metric.

During the 10-year period of 2012-2021, the average return for all investors was 7.6 per cent. The highest real returns were recorded by the Swedish buffer fund AP6 (12.7 per cent). Double-digit returns were also recorded by the Swedish buffer funds AP4 (10.7 per cent) and AP3 (10 per cent) and the Norwegian buffer fund SPU (10.4 per cent).

Returns were relatively stable from 2012 through to 2018, when the trade war between China and the US and Brexit started to create uncertainty in the stock markets. However, 2019 turned out to be an excellent investment year as the stock markets recovered and reached record numbers. This was followed by better-than-expected returns during the pandemic years 2020-21.

Ten-year results indicate that those with higher equity weight have benefited from the long-term rise in share prices. However, our comparison does not allow for direct conclusions to be drawn on the success of investments made. Regulations affecting investment decisions are also crucial in this context. In Finland, the effect of solvency rules is currently under discussion. The challenge is that when solvency is sound, insurers can strive for higher returns through riskier investments and vice versa, when solvency is weaker, the regulation will steer investments towards less risky investment instruments. This has led to selling equities when prices are declining instead of holding on to them or even buying more. This is in contrast to the Norwegian State Pension Fund, for example, which is forced to maintain the equity weight even when the stock prices decline.

All in all, the future seems difficult to predict at the moment. The return of inflation, war in Ukraine, a possible new wave of the pandemic and current declining stock markets all place considerable difficulties in achieving returns comparable to recent years. Is it a farewell to good returns while adapting to the "new normal" or are these just cracks in the pension investors' long road ahead? We shall see in the future rounds of our comparison. ■

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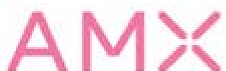

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INTERVIEW

AE in Ireland: Ironing out the detail

There has been big news in Irish pensions earlier this year with the publication of the design principles for Ireland's long awaited Automatic Enrolment Retirement Savings System. What were the IAPF's initial thoughts on the document?

Firstly, it is very welcome that the document has been published and there now seems to be some momentum in moving forward with automatic enrolment (AE) in Ireland. We are facing significant demographic changes over the next 30 years, and it is important that we plan for those. It is clear that automatic enrolment is a proven method of getting more people to save for retirement.

What are the positives?

It is good that the final structure has been outlined and that there is now an implementation date to work to. The final contribution rates of 6 per cent from the employer, 6 per cent from the employee and a 2 per cent state contribution should ensure that the outcomes are adequate for most of the population.

Are there any specific areas where you feel the design principles fall short?

There are still a lot of areas that will require more detail to see how it will really work in practice. Determining the population to be enrolled will be difficult and there will need to be a lot of engagement in advance with employers, employees and payroll providers to ensure people are aware of the introduction of the new system and what it means for them.

Having a different type of tax incentive, where the government pays a direct contribution rather than giving marginal rate tax relief on employee contributions, will definitely add further complication to what is already an overly complex pensions system.

The interaction with existing schemes will also need to be carefully thought through. In some cases, it will be difficult to establish what is an equivalent scheme, particularly with the differing tax incentives.

As an example, an existing scheme could have 6 per cent employee and employer contributions which would match what they would pay in AE. However, the total contributions will be less than the 14 per cent that would be paid in under automatic enrolment, as that would also get a 2 per cent contribution from the state. While issues like this will only arise when the contributions hit the maximum level, 10 years after introduction, it will be important to work through them in advance to ensure that good existing schemes can continue.

The operation of the Central Processing Agency (CPA) will also be crucial. It is taking on a lot of tasks including choosing the investment managers, managing the inclusion of members and the opt-out process, collecting and allocating contributions and all the general administration. It is not clear from the paper if this will operate and be subject to the same regulation as an occupational pension scheme, but it will be regulated by the Pensions Authority. Setting up this new entity will be crucial to getting automatic enrolment up and running in time.

Auto-enrolment has come one step closer to reality in Ireland. Irish Association of Pension Funds (IAPF) CEO, Jerry Moriarty, offers his thoughts on the recent publication of the design principles for the long-awaited savings system

There has been criticism in relation to the fee cap, which has been set at 0.5 per cent – fears are that this is too high and savers will end up spending more than necessary over their lifetimes. Would you agree?

Fees are, obviously, hugely important in ensuring savers get the best outcomes; 0.5 per cent compares favourably with the current UK cap of 0.75 per cent

and the scale in Ireland is much smaller where the potential population to be enrolled is estimated at 750,000. Without further detail on the cost of the Central Processing Authority (CPA) and how that administration system will interact with the investment managers, it is difficult to work out what the appropriate costs will be.

Do you think the design principles have used the best of all AE systems around the world?

I think it has certainly looked at lots of other systems and tried to learn from those. There is a lot of logic in the design, but the real test is how that translates in practice. The decision to enrol employees rather than employers is clearly designed to avoid the accumulation of lots of small pots as people change employers. It should also ensure there is relatively little involvement in the administration of what will mostly be small employers. Splitting the contributions among the four investment managers ensures all members get the same returns, but there also need to be mechanisms for ensuring competitiveness and innovation among the managers to maximise returns. The contribution levels, when they get to 14 per cent of salary, do ensure there is a focus on adequacy as well as coverage. The governance aspects are unclear but it is important that these do use the best systems around the world.

Auto-enrolment is scheduled to come into force in Ireland by the end of 2023 – do you think this is feasible? Will the industry be ready?

There is still a lot to be done and a huge amount of practical detail to be worked through so the schedule is ambitious. It is, though, really important that this is all worked through, and AE gets up and running without any further delays. There is a relatively limited role for the existing industry as the entire administration will be done by the CPA. Getting that set up and operating is likely to be the biggest challenge to the schedule. After that, the main industry role will be the appointment of the four investment managers and there is not any reason that would be any different to general manager appointments that happen all the time. There will be a strong need for a comprehensive communication campaign to ensure employers and employees are aware of what will be happening ahead of the implementation and start date.

There will be implications for existing schemes, particularly those with voluntary membership who will need to consider whether they encourage employees to join their scheme or be auto-enrolled. Schemes will also need to consider whether they are likely to offer equivalent benefits or need to make changes.

> **"FEES ARE, OBVIOUSLY, HUGELY IMPORTANT IN ENSURING SAVERS GET THE BEST OUTCOME"**

What are the other key developments of Irish pensions that are currently keeping the IAPF busy?

There is still a lot of focus on schemes complying with the IORP II provisions, which were only transposed a year ago. Many schemes are still ensuring their processes and procedures are being formalised and properly documented and many key function holder appointments have yet to be made. For some schemes, the level of additional time and cost involved is making it harder to continue on a standalone basis and they will be looking at alternative forms of provision, such as using a master trust. This is likely to result in significant consolidation in the sector over the coming years and we are working with the policymakers and the regulator to ensure this is done efficiently and effectively in order to protect members. ■

COUNTRY SPOTLIGHT FRANCE

Hanging in the balance

Pensions have been a key point of contention in the recent French elections, but what changes the newly re-elected Macron will push ahead with are yet to be seen. Sophie Smith **reports**

WRITTEN BY SOPHIE SMITH

Whilst many countries are having debates as to how to engage the public with their pension savings, France is already facing a much more direct form of engagement in the name of pensions.

More than 50 arrests were made following protests in Paris after thousands of people joined May Day marches to call for pay increases and a halt to plans to gradually increase the pension age, making headlines around the world.

Despite the public unrest, President Emmanuel Macron held on to his title following the latest election, receiving 58.5 per cent of the vote against Marine Le Pen.

Macron had previously outlined ambitious pension reforms as part of his election campaign, including proposals to increase the pension age from 62 to 65. However, campaigning ahead of the run-off vote, Macron hinted that he might soften these proposals, stating that he was “ready to change the timeline” on his planned pension reform.

Building pressure

He also stated that he wants the minimum pension to be set at €1,100 a month, which would be

a significant increase for some pensioners, such as agricultural workers, who often receive €300-€400 currently.

Macron said: "I am ready to change the timeline and say we don't necessarily have to do a reform by 2030 if I feel that people are too anxious." In addition to this, Macron said he was prepared to "open the door" on pushing the country's retirement age from 62 at the moment to 64, rather than 65.

However, his election rival, Le Pen, stated: "There is nothing to expect here from Emmanuel Macron. He will go all the way to the end with obsession because it's a reality that the minimum (retirement) age of 65 is his obsession."

And, when asked about pension reform on *CNBC* shortly after Macron's victory, French Finance Minister, Bruno Le Maire, stated: "When you have a very clear victory, you also have a clear mandate, and you have to stick to your promises. I think that the core of the victory for Macron is he has been able to stick to the promises made in 2017."

In addition to this, whilst Le Maire told *FranceInfo* that the reform "should be the subject of as much discussion and dialogue as possible, with the hope of reaching a compromise", he couldn't guarantee that Macron would not use presidential powers to push through the changes. The issue, perhaps unsurprisingly, remains contentious.

The CGT Union, for instance, says it is against an increase even to 64, with CGT confederal secretary, Catherine Perret, arguing that the union would defend a retirement age of 60 "for all with an income allowing them to live in dignity".

Perret also warned that extending the duration of activity means prolonging hardship, physical and psychosocial constraints, as the union pointed out that there are inequalities in terms of life expectancy, with any delays to the legal retirement age expected to primarily affect the health of the poorest workers.

In addition to this, the union pointed out that the employment rate begins to decline from age 50 in France, with less than half of individuals still employed by age 60, warning that the increase in the number of annuities to be validated will lead to a massive drop in the number of workers able to reach full retirement, and the transfer of costs from the pension system to unemployment, health and minimum social benefits.

"WHEN YOU HAVE A VERY CLEAR VICTORY, YOU ALSO HAVE A VERY CLEAR MANDATE"

These concerns are echoed by OECD senior economist, Hervé Boulhol, who emphasises the need to consider the context of the French labour market, explaining that the average age to exit the French labour market is among the youngest in the OECD countries.

"This generates issues in pensions, but also way beyond pensions, as it is related to low employment after age 60, therefore affecting GDP potential and the overall economy," he continues.

Time for change

Indeed, whilst Boulhol acknowledges that the current minimum age of 62 is "not extremely low compared to other European countries", he warns that it could signal a problem in the context of very low employment rates and increasing longevity.

"We know it takes time to implement pension reforms and we know that if nothing is done, it will be a low retirement age compared to other OECD countries in the future."

And despite public unrest, there is an awareness that change is needed. Recent research from Mercer, for instance, revealed that 62 per cent of respondents do not have confidence in the current retirement system.

"In this survey, where 72 per cent of respondents feel worried about the level of their future retirement, 68 per cent want our President to redesign or make in-depth adjustments to the current system," Mercer France head of retirement and employee savings consulting, Benjamin Sanson, points out. "The figure reaches 85 per cent for 18–24 year olds."

And Sanson argues that those concerns are founded given the demographic challenge that the French pension system is facing.

"A reform is indeed needed, and since French workers have on average five additional years of retirement length compared to the other OECD countries, aiming at postponing the retirement age is only natural," he continues.

However, Sanson shares Boulhol's concern around employment rates, suggesting that any changes to the retirement age should be planned along with employment measures for seniors.

In addition to this, Sanson notes that only 3 per cent of respondents considered the current system to be ideal, highlighting this as a reason to question the relevance of a reform that only affects the legal pension age.

Supplementary pension plans may instead represent an opportunity to address concerns, as Sanson explains that French savers expect the presence of a funded pension system from their company, with 70 per cent of savers believing that the presence of this type of device should be mandatory in all companies in France.

A universal solution?

However, Boulhol argues that the number one problem with the French system is its complexity and fragmentation, pointing out that there are "all these different regimes and rules that people do not understand". This, he says, is "a nightmare" for savers, who do not understand what they are entitled to, as this not only impacts pension entitlements, but also family-related entitlements and survivor pensions.

"This is a big problem," he continues, warning that whilst this generates difficulties in managing the system and making financial projections, it also creates inequalities because contributors tend to be covered by different rules.

"And not only does it create some inequality, but the feeling of large inequality is pervasive," he adds, explaining that whilst the differences may not always be significant, savers often take issue as they may feel they are not well treated.

The OECD has been a long-term advocate for a universal pension system to address this concern, as previously proposed by Macron in 2017. These plans for major reform were initially put on hold amid the impact of Covid-19, with Sanson suggesting that the plans now appear to have been "definitively abandoned".

"And whilst the OECD may be supportive of these plans, other institutions, such as CGU, have come out firmly against them," he adds.

However, whilst Sanson says that systemic reform will not happen, he predicts that the new government will "certainly push forward for the abolition of the special pension schemes in order to align them on the main scheme".

"Instead, a less structuring reform should take shape," he suggests, continuing: "In particular with the gradual extension of the contribution period with a decline of legal retirement age, in accordance with Emmanuel Macron's programme.

"At the same time, the President reconfirmed his commitment to specific measures, linked to the hardship of work or for people who started working young. These measures, which have already existed for several years, should probably be reinforced during this new five-year term."

Reaching a compromise

It is clear that there is no shortage to potential reforms to be considered, with the CFDT, for instance, also suggesting that greater tax on capital could help avoid an increase in the retirement age.

In addition to this, Boulhol suggests that changes could be made to the 25-year reference period for pensions, pointing out that France is one of three exceptions in Europe in this respect.

In addition to this, he notes that as past wages are uprated in line with prices, pension finances in France are very sensitive to real-wage growth, arguing that "this is not a good way to set the rules".

With so many conflicting views, exactly how pension reforms in France will ultimately shape up is yet to be seen. But it is clear that the fight for pensions is well underway. ■

Reform in a time of crisis

WHILST THE PANDEMIC placed the brakes on broader plans for a universal points system, Candriam head of ESG client portfolio management, Marie Niemczyk, notes that it has also impacted French pension funds, with some pension funds, especially in the public space, called upon to make special contributions, often from their reserves, to Covid-19-related funds and support efforts, or in the form of relief or temporary suspensions on pension contributions.

Adding to this, Mercer France head of retirement and employee savings consulting, Benjamin Sanson, points out that there has been "a strong impact on the collection of pension funds (consequence of the pay-as-you-go system) due to the massive use of partial unemployment".

He adds: "This drop in collection has led to an explosion in the system's deficit with a deficit in 2019 of €1.9 billion to €25.4 billion in 2020 according to the Centre d'Orientation des Retraites. Little impact on retirement savings, since in a context where people did not consume as usual, due to health restrictions, French savings focused more on precautionary savings."

A spokesperson for the European Insurance and Occupational Pensions Authority (EIOPA) also points out that almost one third of the national markets reported a decrease in contributions mainly due to shrinking in business (sponsor contributions) and lower personal income.

"The implication of lower contributions were also deemed as a concrete threat to the expected pension benefit. The impacts are foreseen to be more concerning in DB plans as interruptions in funding may have a negative impact on future benefits.

"However, no benefit cuts or changes in the way in which beneficiaries are opting to receive benefits payments were observed."

AAMs: A silver bullet for pension system challenges?

The OECD's Hervé Boulhol **and** Wouter De Tavernier **discuss automatic adjustment mechanisms in pension systems**

WRITTEN BY THE OECD'S HERVÉ BOULHOL AND WOUTER DE TAVERNIER

Pension systems provide individuals with an income both now and in the distant future, which makes them susceptible to uncertainties. In the face of demographic, economic or financial trends, policymakers can choose not to act and accept their negative consequences for financial sustainability or retirement income adequacy. Alternatively, they can adjust pension parameters. These adjustments can be discretionary, by undertaking regular legislative action as circumstances change. Or, change can occur automatically by setting rules about how pension parameters should be adjusted. This last option can be attractive to policy makers as while, for example, the extent of future ageing trends is unknown, the broad impact of how a given demographic evolution affects the pension system is typically well understood. The main chapter of the 2021 edition of the OECD flagship publication *Pensions at a Glance* focuses on automatic adjustment mechanisms (AAMs). It shows that compared to the alternative of discretionary changes, AAMs can be designed to generate changes that are less erratic, more transparent and more equitable across generations.

AAMs in pension systems refer to predefined rules that automatically change pension parameters or pension benefits based on the evolution of some indicator. They can protect pensions from uncertainties: pension indexation can protect pension levels against current and future inflation trends, and, more generally, automatic adjustments can serve various objectives. Whether to make adjustments to pensions, contributions or retirement ages is a fundamentally political question for both discretionary changes and automatic adjustments.

AAMs emerged in the 1930s in the form of pension indexation, ensuring pension adequacy through increasing pensions automatically as prices or wages increased. With population ageing resulting in increasing concerns about pension expenditures, several countries introduced AAMs to maintain financial sustainability. Pensions are for instance adjusted to the ratio of pensioners to contributors in Germany and to the financial balance of the system, defined as the ratio of future pension expenditures to future revenues in Sweden. Several countries are linking benefit levels or statutory retirement ages to changes in life expectancy. Some others completely changed the structure of their pension systems and moved away from defined benefit to defined contribution schemes, both funded and notional, which inherently include some forms of automatic adjustments. About two-thirds of OECD countries now employ AAMs. France is among the third of countries with no AAM, at least formally.

AAMs are meant to adjust for future trends and are not a substitute for bold discretionary measures in a financially unbalanced pension scheme. It is indeed crucial to distinguish AAMs that accompany long-term trends from those that are used to correct imbalances due to entitlements that already accrued. AAMs should ideally be used to prevent the deterioration of financial sustainability, rather than being triggered in case of insolvency. AAMs introduced to correct existing imbalances due to already-accrued entitlements, often at a time of crisis, might result in harsh adjustments in benefit levels and generate political pressure to circumvent their impacts. This has been the case with the suspension of the AAMs in Spain. If the pension system is not financially sustainable given already accrued entitlements, necessary changes are immediate and not conditional on the future developments of some indicators.

As AAMs are meant to operate in the medium or long term, it is critical that they remain politically sustainable. This can be reached through wide political support for their introduction and by designing mechanisms that avoid harsh adjustments. Hence, AAMs are best introduced with a big parliamentary majority and broad public support. ■

The opinions expressed here are those of the authors and do not necessarily reflect the views of the OECD or of its member countries.

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Currency focus:
OVERCOMING HURDLES

Inflation and currency

As inflation has surged worldwide, investors are questioning its effects upon markets and investments globally. Mesirow explores the impact of this on currency

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Lesson leart

As the world tentatively emerges from the worst of Covid-19, Lynn Strongin Dodds reflects on the pandemic's impacts on currency markets and lessons learnt for the future

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INVESTMENT

Inflation and Currency

As inflation has surged worldwide, investors are questioning its effects upon markets and investments globally. With the war in Ukraine and the Russian sanctions pushing energy prices to record high levels, the inflation rate in the Eurozone registered at 7.4% year-over-year in March 2022, the highest on record, more than three times above the European Central Bank (ECB) target of 2%. As global economies remain highly interconnected, the relationship between inflation and FX markets is an important consideration within portfolios. This article breaks down the influence of inflation on currency exchange rates, how the behavior manifests across time horizons, and how central bank policy plays a major role in spot rate movements.

WRITTEN BY UTO SHINOHARA, CFA, MANAGING DIRECTOR & SENIOR INVESTMENT STRATEGIST

In Theory

When examining the relationship between inflation and currency, purchasing power parity (PPP) is commonly used as an economic theory for the determination of exchange rates. Absolute PPP is guided by the law of one price, assuming price levels between two countries should be equal. When comparing exact baskets of goods across countries, absolute PPP suggests the exchange rate will change over time until the baskets are of equal value due to international arbitrage.

$$S = \frac{P_a}{P_b}$$

where S = spot rate, P = price of basket in country a | b

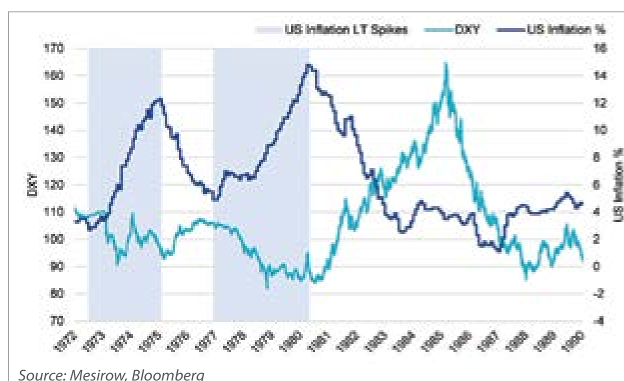
The Big Mac Index, published since 1986 by The Economist, became a popular and easy-to-understand comparison tool for currencies, using principles of absolute PPP, since the Big Mac is universally known and made to the same specifications in all geographies. However, the simplicity of absolute PPP has shortcomings as it fails to consider the existence of inflation and consumer spending, as well as barriers to trade such as transportation costs, taxes, tariffs, and other transaction costs.

Relative PPP addresses the effect of inflation on exchange rates by suggesting a negative correlation between inflation and spot rates – higher inflation will reduce the purchasing power of a currency in the future.

$$S_1 = S_0\frac{(1 + inf_a)}{(1 + inf_b)}$$

where S = spot rate at year #, inf = annual inflation rate in country a | b

The theory behind relative PPP logically deduces that when inflation is high, expensive items are less in demand, which means that the currency required to purchase those items is also less in demand, leading to depreciation. The concept is rational within a frictionless, efficient global market.



Source: Mesirow, Bloomberg

In Practice

To understand the effect of inflation on currencies, we looked back over 50 years to include the high inflationary periods of the 1970s, as well as more recent periods. Since EUR was not in existence until the late 1990s, we analysed USD over earlier periods, followed by EUR over more recent ones.

The Great Inflation of the 70s and 80s reached double-digits, peaking multiple times before receding into the mid-80s. During major inflation spikes in the US, the US Dollar Index (DXY) depreciated until inflation peaked and reversed, lending support to the theory behind relative PPP.

However, over recent decades, relative PPP has not held. When studying the behavior of EUR against USD, overlapped with the inflation differential between the Eurozone and the US, the currency movements have behaved in the opposite manner. When the inflation differential was positive in the direction of the Eurozone, EUR has appreciated against USD although inflation was higher.

Insights & Outlook

Possible explanations of this stark difference in behavior begin with the magnitude of inflation. While inflation is currently high relative to the compressed inflation environments over the past few decades, the levels are dwarfed by the historical highs in the 70s and 80s. The higher magnitudes in the past could have brought higher influence relative to other factors at the time, thus following the behavior theorized by relative PPP. Developed markets inflation is currently still less than half of the peak levels of the 70s and 80s.

While relative PPP has held during episodes of double-digit inflation, more recent behavior has not supported the view that higher inflation leads to currency depreciation. Recent price action has been heavily influenced by central bank policy in response to inflation. Interest rate hikes are a part of the central bank toolbox employed to maintain price stability and to manage economic fluctuations. Policy changes to combat inflation, or even the anticipation of such policy changes, can move markets. Interest rate hikes often lead to currency appreciation since investor funds flow into the country to take advantage of the attractive interest rate. Thus, in the short-term, rising inflation can lead to central banks raising interest rates, which can lead to currency appreciation, running counter to relative PPP. Although inflation has reached record highs in Europe, the inflation differential is negative when compared to higher US inflation. EUR has been under intense pressure against USD since the start of 2021, with the ECB lagging other major central banks' hawkish policies, as the divergence between a very hawkish Fed and a more dovish ECB remains wide.

Source: Mesirow, Bloomberg

Source: Mesirow, Bloomberg, OECD

For European investors with international portfolios, currency exposure returns are dependent upon the euro's future trajectory, with its path going forward highly dependent upon the timing of ECB policy. As the ECB closes the policy gap vs. the Fed, EUR should be more supported, all else being equal.

However, unexpected events can affect trajectory and policy across regions. As the ECB began tilting towards more hawkish behavior to rein in surging inflation, the Russia-Ukraine crisis escalated, delaying ECB tightening as supplies became even more constrained and Europe's dependence on Russian energy became a focal point. While an ECB tilt towards hawkish behavior is expected as inflation persists, the timing of a policy change remains uncertain, balancing the crisis in Ukraine, raging inflation, and Europe's growth prospects. With FX volatility rising in 2022 from policy divergence and the Russia-Ukraine crisis, a currency hedging policy with a dynamic, active element can help navigate uncertain waters by adapting to the changing market backdrop. With EUR reaching lows rarely seen over the past twenty years against USD, actively monitoring undervaluation levels can help manage long-term hedge positions as the euro looks for support over the coming year.

Country	Policy Rate	Implied Policy Rate				
		3M	6M	1Y	2Y	3Y
United States	0.38	1.7	2.42	3.03	2.94	2.7
Eurozone	-0.5	-0.38	0.05	0.87	1.45	1.35

Source: Bloomberg as of April 26, 2022

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INVESTMENT

Lessons learnt

As the world tentatively emerges from the worst of Covid-19, Lynn Strongin Dodds **reflects on the pandemic's impacts on currency markets and lessons learnt for the future**

WRITTEN BY LYNN STRONGIN DODDS, A FREELANCE JOURNALIST

Over the past three years, FX markets have had a tumultuous ride. However, understanding macroeconomic factors is one thing but navigating a pandemic is another. Suddenly traders, well versed in fundamentals, had to become armchair experts in herd immunity and vaccine rates.

"One of the issues is that the scenarios were playing out faster than anyone had imagined," Millennium Global co-chief investment officer, Richard Benson, says. "The market moved in February 2020 from one where the Fed was expected to hike interest rates to one where there was a pandemic leading to de-risking and de-leveraging and a volatility spike."

Mesirow Currency Management managing director, Richard Turner, also notes: "March 2020 was a good reminder that markets can transition very quickly between regimes, both in terms of risk sentiment and general uncertainty, leading to increased volatility. The high level of government intervention in the first few months of the pandemic also meant typical economic indicators were often too slow to capture real time effects and we found measures based on economic sentiment were more useful."

Swift action

Many analysts believe that the swift action by central banks went a long way in mitigating some of the major concerns. They wasted no time in turning to the global financial crisis playbook, which helped dampen down volatility. Estimates are that the US Federal Reserve and its major counterparts in Europe, Japan, the UK and elsewhere pumped around USD 12 trillion into the system to offset the economic fallout of the coronavirus pandemic. They bought a bountiful array of assets and in some cases offered long-term loans to banks in a massive bout of quantitative easing.

These actions changed the rules somewhat for the so-called safe haven assets. As J.P. Morgan Asset Management FX portfolio manager and macro strategist, Neil Weller, put it, "during the initial bout of market stress in March 2020 the dollar surprisingly weakened, before swiftly recovering as it regained the role of a global safe haven asset. The initial underperformance reflected the unusual rise in US yields, where bonds briefly failed to act as a safe haven amid a liquidity driven squeeze on all asset prices".

He says: "The role of the dollar as a safe haven asset is important for investors considering their strategic currency hedging approach, and doubts about the reliability of the correlation between bonds and equities could argue for lower FX hedge ratios on foreign holdings of US assets going forwards."

Russell Investments global head of currency, Van Luu, adds: "In the beginning of the pandemic, the safe haven currencies did benefit from risk aversion, but it was brief. The US Fed, Bank of England and Bank of Japan moved quickly which calmed markets down and added liquidity."

Pandemic influence

One difference between the financial crisis and the pandemic is that the health of nations and not just their respective economies were brought into sharper focus. Traders turned their attention to any correlations between inoculations and currencies for trading signals.

A so-called vaccine spread trade emerged that rewarded those

countries with the fastest vaccination programme. The thinking at the time was that defeating the virus was a prerequisite to a country reinvigorating its economy and thereby bolstering its currency.

For example, Australia's dollar took a dive versus its New Zealand counterpart in February 2021 after Germany cast doubt on the effectiveness of AstraZeneca's Covid-19 shot, which formed part of Australia's vaccination programme.

Britain's pound was particularly sensitive as the country was among the hardest hit with one of the highest death rates. Its inoculation progress offset elevated case rates propelling the pound to new heights while the European Union's chaotic distribution weighed heavily on the euro.

Sterling started 2021 bumping along the bottom as one of the weakest currencies in the G10. However, there is no doubt the currency got a boost due to the success of the vaccination rollout.

Emerging market currencies fared much less well as traders raised concerns about the progress in different regions, sending red flags over the Singapore dollar, Malaysian ringgit and Indonesian rupiah.

Now that the dust has settled, "the linkage between these economic effects and foreign exchange rates is a little weaker, as the stimulus responses varied quite widely between countries," says Turner. "But in general, in the first Covid-19 waves currencies depreciated as the number of cases was peaking and then recovered once cases began to fall."

Although vaccination rates were important, many analysts believe economic drivers were equally as important. For example, the dollar, which was on the other side of the euro and sterling trades, defied expectations and held its own. This was more to do with the resilience and diversity of the economy because responses to the pandemic varied across the country.

"FX markets did at times respond to the daily updates to Covid-19 statistics, but only during a few periods of acute focus on differing speeds of vaccination or differing policies on lockdowns," says Weller.

Trium Capital global macro portfolio manager, Peter Kisler, also notes that the pandemic triggered economic activity that was not expected. "For example, some countries benefitted from higher consumer spending as people turned to online shopping while others were hit by supply chain issues. Also, commodity producing countries had an advantage although they were hurt by the stronger dollar."

"THE PANDEMIC IS NOT OVER YET, WE ARE STILL SEEING LOCKDOWNS HAVING AN EFFECT IN CHINA, FOR EXAMPLE"

Turner adds: "Obviously, each country is unique in terms of its economy, demographics, the severity of the Covid-19 outbreak experienced and the response." He cited the firm's white paper, *Covid-19, Economy and FX: Past, Present and Future*, which shows that countries where services accounted for a higher proportion of the economy experienced a greater economic shock due to lockdowns than those where manufacturing comprised a greater proportion of the economy.

"Intuitively you would expect this, as service industry relies more on interpersonal contact, and it is borne out by the data," he says. "Also, countries that had strong border controls such as New Zealand and Australia, were also able to recover faster after the initial economic shock."

Looking ahead

Looking ahead, Mesirow's white paper shows that the economic effects of future Covid-19 waves would expect to be less pronounced in countries that have a good proportion of the population vaccinated and for Covid-19 to not be such a strong driver of foreign exchange rates for these countries going forward, according to Turner.

"However, the pandemic is not over yet, we are still seeing lockdowns having an effect in China, for example, and the secondary economic effects of the pandemic, with supply chain disruption persisting and the increase in money supply from government stimulus driving inflation, are likely to persist throughout 2022," he adds.

Weller believes there will be a greater focus on the pandemic's lasting impact on global trade, causing major disruptions to globalised supply chains amid heightened demand for consumer goods. "Going forward, there is debate about whether we have passed peak globalisation as focus has shifted towards supply chain resilience, potentially offering some support for 'near-shoring' currencies, such as the Mexican peso," he adds.

Lessons have also been learnt about having the right data and risk management controls in place. "The foreign exchange market is constantly evolving, and the models need to keep up," says Turner.

Not surprisingly, for now, Covid-19 albeit lurking in the background, has taken a back seat to the tragic events in Ukraine and the reverberations it is having across the world in terms of supply side disruption, higher interest rates and soaring commodity prices.

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CASE STUDY

Directing focus

Photo by: Peter Knutson

Tom Dunstan talks to AP7 communications strategist, Mikael Lindh Hök, about the fund's recent engagement campaign and its ESG strategy

Can you tell me about your recent Premium Pension Crash Course engagement campaign?

In total, there are 6.2 million pension savers within the Swedish premium pension system, of which over five million savers have part of it at AP7. Many of these savers may not have the commitment or feel they have time to familiarise themselves with their premium pension. A low level of knowledge about pensions is a constant challenge. In connection with the annual distribution of pension information by the Swedish Pensions Agency, we decided to provide information on social media channels so it would be really easy to take in the knowledge needed to make a well-thought-out decision regarding the premium pension. Together with Futurniture, we produced nine Instagram videos trying to keep the information as basic as possible.

During the campaign that took place in February and March, we reached 650,000 Swedes with a total of 2.4 million views. As we created nine films, we have been able to track what attracted the most attention. Interesting enough it was the film about high fees hindering returns that generated the most interest.

Can you tell us why you chose Instagram to promote the campaign?

To make it easy to reach the broad target group – working age Swedes – we chose Instagram because most Swedes of all ages have an account on the platform.

Are there any plans to develop the campaign in the future?

Yes, we are working on a tool on our homepage based on the same idea of keeping it on a 'for dummies' level and with a similar easy structure. The main objective even there is that no matter what decisions are to be made, it is good if they are based on factual knowledge. We are now developing a simple follow-up to the campaign with a pension knowledge tool on the website that we will launch later in May.

Moving on to AP7's investments, can you tell us a little about your environmental, social and governance (ESG) policy and your work in this area?

As a universal owner, our main contribution is active ownership. We own more than 3,000 companies, vote at all the annual general meetings (AGMs) and file shareholder proposals at some. For example, we filed a proposal at Volkswagen (VW) a couple of weeks ago about the alignment of lobbying activities with climate goals. Collaboration is a cornerstone in our ESG strategy. If you're a global investor and want to achieve real world impact collaboration is key.

Can you go into more detail about your recent proposals filed at Volkswagen (VW)?

Our goal for VW was to nudge it to catch up with other German companies, (Bayer, BMW, E.ON and Mercedes-Benz) on its transparency about its climate lobbying, so it is in line with the Paris Agreement. As a long-term owner, our hope is

that VW will realise this value itself. Together with the Church of England Pensions Board (also AP2, AP3 and AP4, Denmark's AkademikerPension and asset manager Schroders), we proposed changes to VW's articles of association to ensure that its sustainability reporting in the future also includes that its lobbying does not work against the climate goals. We organised it primarily together with the Church of England as we have collaborated on the issue of responsible climate lobbying since 2015. Over the years, the collaboration, which also includes BNP Paribas, has succeeded in getting over 40 companies to report on whether their lobbying is in line with the Paris Agreement. In March this year, we took together the lead of launching a standard for responsible climate lobbying.

How will the new standard for responsible climate lobbying work and what does it seek to achieve?

Lobbying that counteracts the Paris Agreement is a widespread problem. The Global Standard on Responsible Climate Lobbying is intended to achieve a step-change in the commitment of investors and companies to responsible climate lobbying in practice. The objective is to provide a tool through which companies, investors and other stakeholders can ensure that all political engagement is conducted in a way that supports the Paris Agreement. This is regardless of whether the engagement is direct, by the companies, or indirect, via the companies' business organisations.

Could you go into more detail about the recent proposals filed at Woodside and Santos?

The expectations in the resolution submitted to the Australian gas and oil companies Woodside and Santos are that their political influence does not counteract the Paris Agreement and that they stop lobbying for the development of new oil and gas. Analysis shows that both companies continue to be committed to counteracting climate goals. So, as shareholders we request that the companies cease all private and public advocacy, both direct and indirect, that contradicts the conclusions of the International Energy Agency (IEA) and the Intergovernmental Panel on Climate Change (IPCC) on 1.5°C alignment, including advocacy relating to the development of new oil and gas fields.

How effective have your most recent proposals for Volkswagen, Woodside and Santos been?

It is too early to evaluate Woodside and Santos since we are awaiting the results from their AGMs. But regarding VW, they refused to put our proposal on the agenda with reference to legal arguments. This is not unique to VW, there are clearly grey areas of the law to refuse to table shareholder resolutions or dissuade shareholders from filing a resolution. Our next step is to seek clarity in the courts on how to interpret German law. This will help form shareholder engagement strategies in the future.

All in all, our main ambition is to send strong signals to companies about investors' expectations regarding acting in line with the Paris Agreement.

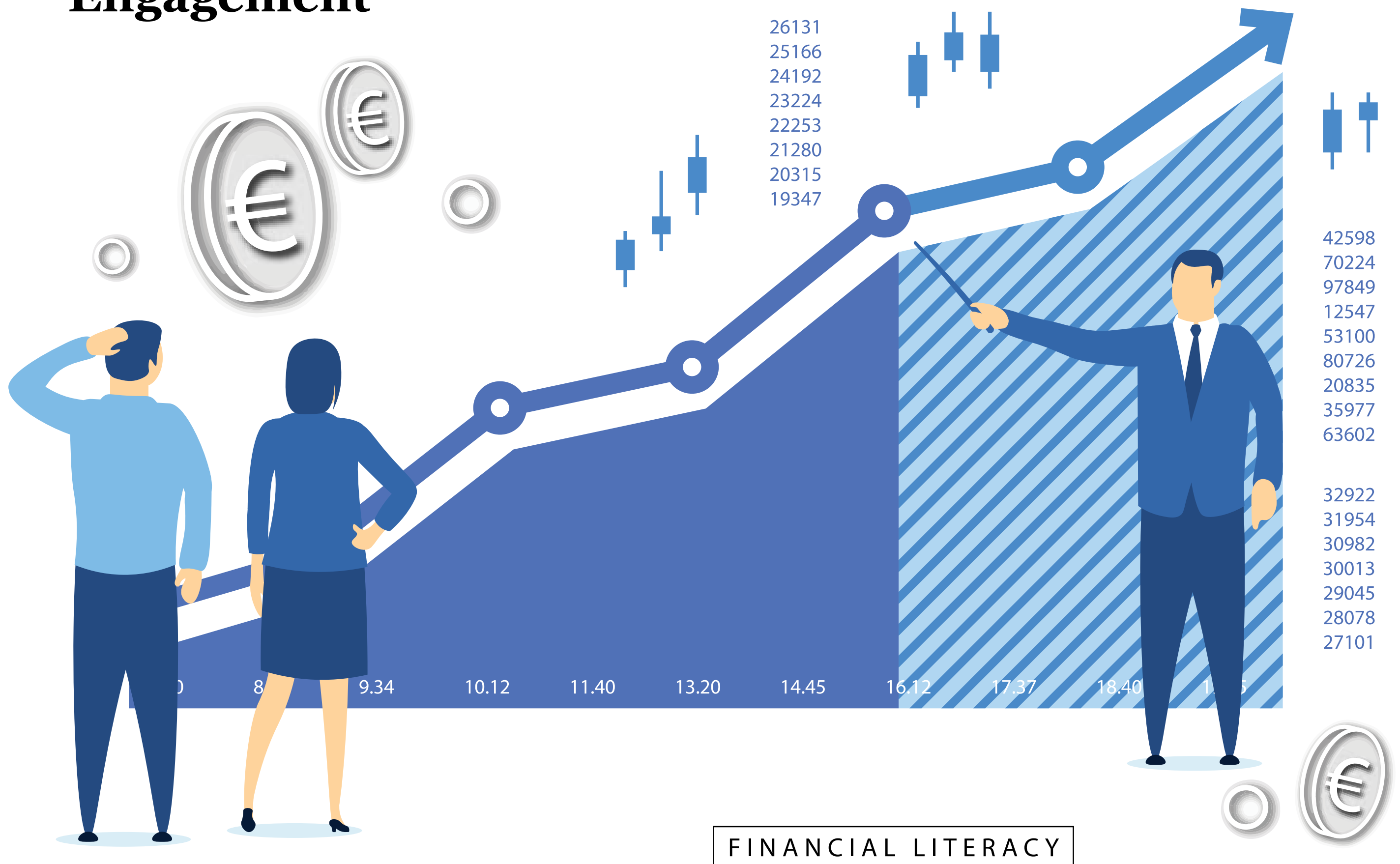
Are there any other companies or organisations that you would like to collaborate on in future?

Since collaboration with other investors is key to success as an active owner, we are embracing several collaborations such as Climate Action 100+ and The Paris Aligned Investment Initiative Net Zero Asset Owner Commitment, which is a global sustainability network for investors who are working to reduce the emissions of portfolio holdings in line with the Paris Agreement. We are also in the steering committee for the Taskforce on Nature-related Financial Disclosures (TNFD) that develops frameworks for risk management and reporting of nature-related risks.

Are there any other areas apart from collaboration that are important to your ESG strategy?

Collaboration with other investors with similar ambitions is vital to achieve momentum as most large universal investors have a limited ownership on their own. The main area in our ESG strategy is active ownership, which can be driven in many ways but mainly through four tools: voting, dialogue, blacklisting and legal processes. In reality, though, that is an over-simplification. In practice, a process comprises of a number of steps using different interacting tools, and every tool in itself has several components. ■

"AS A UNIVERSAL OWNER, OUR MAIN CONTRIBUTION IS ACTIVE OWNERSHIP. WE OWN MORE THAN 3,000 COMPANIES, VOTE AT ALL THE ANNUAL GENERAL MEETINGS, AND FILE SHAREHOLDER PROPOSALS AT SOME"



FINANCIAL LITERACY

Raising the bar

Despite higher rates of financial literacy across the continent, consumer inertia in making pension choices remains an issue

WRITTEN BY GEORGIE LEE, A FREELANCE JOURNALIST

Understanding concepts like savings, investments, and debt is crucial for individuals to achieve a sense of financial wellbeing, both in the short term and in retirement.

Worldwide levels of financial literacy correlate highly with development. According to the *S&P Global Financial Literacy Survey*, Nordic countries and the Netherlands have the highest rates of financial literacy in the European Union (EU), with at least 65 per cent of adults financially literate across Denmark, the Netherlands, Sweden, and Norway.

Rates were found to decrease across central Europe, and further again in southern and eastern Europe – 45 per cent and 49 per cent of adults are financially literate in Greece and Spain, respectively. Meanwhile, 35 per cent of adults in Bulgaria and Cyprus are financially literate, and just 22 per cent of adults in Romania.

Cultures, genders, ages

According to economic think tank Bruegel deputy director, Maria Demertzis, levels of financial literacy in the EU are high in comparison to other parts of the world, though disparities between countries are wide, and levels differ across cultures, genders and ages.

Demertzis says both knowledge and application are important factors with financial literacy levels starting to decrease after the age of 50, by which time many have completed the major financial transactions in their lives. Financial literacy often deteriorates from here, she says, when consumers are tasked with making fewer decisions.

"In terms of identifying 'risk groups', both young and adult groups can go through periods of financial illiteracy. The young are targeted with better policies around training and education, while the elderly is less well catered for, so they can be vulnerable," she adds.

Studies also show there is a persistent financial literacy gap

between men and women, which is prevalent in almost all countries.

According to research by Annamaria Lusardi, the Italian economist who has worked extensively on the concept of financial literacy in society, a third of the financial literacy gender gap can be explained by women's lack of confidence, and that both knowledge and confidence were key deciders in stock market participation.

In this context, Federation of Dutch Pension Funds chairman, Ger Jaarsma, highlights that for a lot of women there are also other factors at play.

"In many countries, men are more financially literate than women, but men overestimate their knowledge more than women do," he notes. "Levels of financial literacy are connected to the way people are likely to take financial actions… many women work part-time in the Netherlands, especially when they have children to take care of. Pension funds work to inform them about the effect of part-time work on income and their pension savings."

Increasingly a priority

European institutions have been driving for greater financial education since the financial crisis, which Demertzis says highlighted a greater need for knowledge around debt.

"During the financial crisis, it became apparent that if people knew how to tackle debt better, we would not have gotten into the situation over indebtedness," she says.

"Financial literacy might have prevented households from taking out a mortgage they could not afford. Of course, the bigger picture is that poorly regulated banks were lending to them in the first place."

Since then, the European Commission's Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA), has been working to scale financial literacy initiatives across the EU. This has involved recently partnering with the OECD's International Network on Financial Education to develop financial competence frameworks for both adults and children, which set out knowledge, skills and behaviours necessary to develop financial wellbeing. The framework for adults was published in January 2022. European regulators have also been active on this issue.

In January, the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and European Securities and Markets Authority (ESA) published a joint resource on financial education, containing 126 national initiatives to encourage consumers to improve their financial literacy. The move came a month after Insurance Europe revealed research findings suggesting 38 per cent of European citizens were not saving for retirement, with 42 per cent of women struggling to save for retirement, compared to 34 per cent of men. Of those who were not saving, 30 per cent reported it was because they could not afford to.

"FINANCIAL LITERACY, OR PERSONAL FINANCE, IS PART OF THE SCHOOL CURRICULUM IN SWEDEN FROM THE FIRST GRADE"

In some countries, designated financial education bodies have been tackling the issue head on. This is the case in Sweden where organisation Gilla Din Ekonomi provides financial education to Swedes at all life stages.

Since 2008, it has been disseminating materials for teachers, Swedish immigrants, at universities, and for people working in pensions and insurance, as well as advising senior citizens.

"Financial literacy, or personal finance, is part of the school curriculum in Sweden from the first grade. There is plenty of opportunities to learn and so we mostly teach people who are already literate about diversifying their investments," says Gilla Din Ekonomi adviser, Therese W. Ekman.

According to Ekman, communication remains an issue: "We realised recently there is a problem with words. We talk about saving and saving in the stock market, but to some people saving is simply keeping money in their account. Given we have been living with a 0 per cent interest rate, this is an area we want to focus on more: what does saving mean to people?"

Ekman says Gilla Din Ekonomi plans to drive stock market education further, explaining that it is currently easier to teach Swedes about mutual funds than it is about picking individual stocks, in part, due to the nation's pension system.

On Sweden's premium pension, 2.5 per cent is paid to the funded pension scheme on a mandatory basis, while deposits move to individual investment accounts with choices implemented. Employees can decide to have their premiums invested in up to five out of 700 mutual funds.

Looking forward

Across Europe, fragmentation remains an issue when overcoming financial illiteracy.

According to an EIOPA spokesperson, European institutions are limited in their ability to implement and promote financial literacy across countries, as areas such as education remain national objectives.

EIOPA's founding regulation is to "review and coordinate financial literacy and education initiatives by the competent authorities" and therefore it generally stops short of setting benchmarks for individual nations.

However, the commission has been working with the OECD to promote lifelong learning initiatives, and, according to Demertzis, encourage banks, which have an incentive to retain financial literate customers, to cater for financial literacy.

Fragmentation is not the only challenge in the way of progress. Cardano Insights director, Stefan Lundbergh, who led a review of the Swedish pension system in 2017, highlights findings indicating that even with high levels of financial literacy, barriers to consumer action remain.

"EUROPEAN INSTITUTIONS ARE LIMITED IN THEIR ABILITY TO IMPLEMENT AND PROMOTE FINANCIAL LITERACY ACROSS COUNTRIES"

In a survey of 2,500 Swedes, Lundbergh found that when participants were asked about investment fund considerations, the majority highlighted the importance of charges, performance and risk.

The name of the provider was listed as the least important aspect. However, when asked to explain details of their portfolio, 50 per cent were uncertain about whether they were investing in an index fund or not, an area they also flagged as critical. Many knew the name of the provider they had.

According to Lundbergh, this suggests financial literacy alone does not ensure consumers will apply knowledge when making decisions.

"No matter whether you are financially literate or not, there is so much inertia involved in actively making pension choices yourself, that most people do not. That is why it is so important to have a policy where people are auto-enrolling in a pension, and if they do not like it, they can opt out. It is a way to help people save for retirement. The most important part at play here is implementing policies that ensure you can choose to opt out, rather than having the onus on the saver to do it themselves." ■

GUEST COMMENT

Working together

OECD economist, Maciej Lis (PhD), **details the organisation's work on pensions with Slovenia and how the country has leveraged the Swedish experience in pension communication**

WRITTEN BY OECD ECONOMIST, MACIEJ LIS (PHD)

The OECD, supported by the European Commission, conducts in-depth pension reviews of interested countries to assess strengths and weaknesses in international comparison and advises on potential improvements. For example, Ireland has faced low coverage of earnings-related benefits while in Latvia high old-age poverty called for bold policy actions. Challenges highlighted for Portugal, the Czech Republic and Slovenia are somehow different. Among them, the Slovenian public pension system covers all employees and delivers average replacement rates, especially for low earners, but its complexity and an ageing population is exerting an increasing pressure on its finances. Private pensions play a minor role in delivering old-age income in these three countries.

Currently, in Slovenia, the average old-age income relative to that of the whole population is close to the OECD average, while old-age inequality is lower than in most other countries. The average labour market exit age is among the lowest due to very low employment rates of older workers – in particular, those above 60.

Financing defined benefit pensions on a pay-as-you-go basis will be challenged by population ageing. Longer lives and low fertility in the past are leading to higher numbers of retirees per worker, exerting upward pressure on pension spending; by 2050, Slovenia is projected to see among the largest increases in pension expenditure as a share of GDP. Without policy adjustments, higher pension spending will put substantial pressure on public finances.

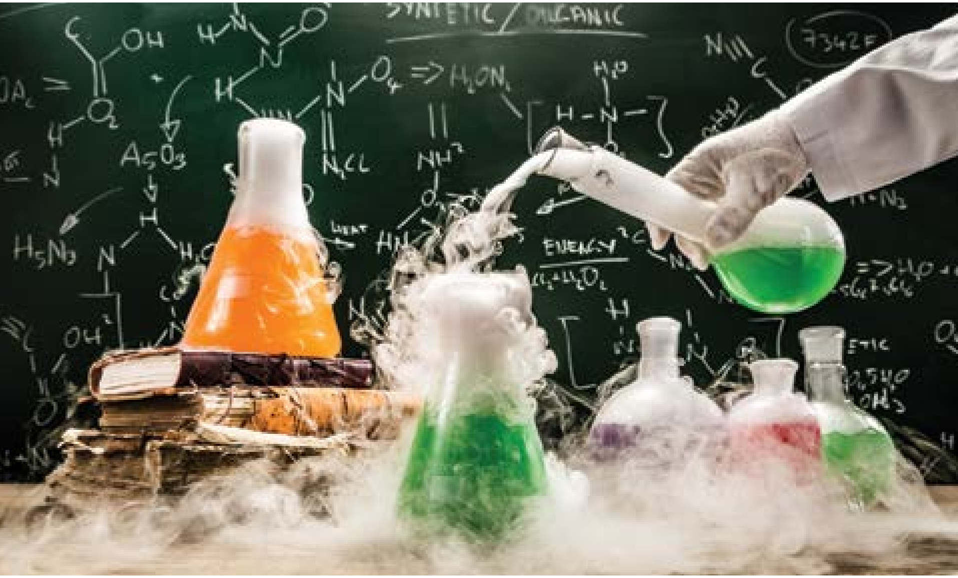
There are many options for Slovenia to simplify its pension system and secure the financing of future benefits. The crucial one is increasing the retirement age and linking it to changes in life expectancy such that, over time, longer lives are not transmitted into longer periods of claiming pensions in the one-to-one manner. Pension indexation could be shifted towards prices from the current mix of wages and prices to lower financial pressures over the longer term. Further options would need to compromise increasing contribution rates, financing pension redistributive components from the state budget and adjusting benefits, including the redistributive features of the pension scheme. To boost future old-age income, private occupational pensions might be strengthened by making them mandatory or making them the default option for workers.

Slovenia reformed its pension system substantially in 2000 and 2012, simplifying its functioning and improving financial sustainability by adjusting benefits and increasing retirement ages. As a result, employment rates of those younger than 60 increased substantially from very low levels, but ageing requires further policy actions. In 2017, the government and social partners signed an agreement, which acknowledges the need for further reforms without deciding on concrete measures. The recent OECD analysis, based on best practices from other countries, is intended to facilitate the implementation of improvements to Slovenian pensions.

To that end, effective communication is a crucial part. To help build communication capacity, Slovenian civil servants visited Stockholm last March to learn about Swedish experiences in this area. Sweden's political process of reform implementation, in particular in the area of pensions, is known to be consensual. However, it was not always this way and the consensus building approach came through pain following a period of strong social unrest in the 1930s. Over the last 30 years pension reforms in Sweden, including the systemic reform in the 1990s, were designed and agreed by the Parliamentary Working Group on Pensions. After the agreement, proposed reforms were implemented smoothly. Similarly today, Sweden is increasing the minimum retirement age and linking it to life expectancy, using a similar reform process.

Apart from implementing pension reforms, communication about pension entitlements among all segments of the pension landscape is well coordinated in Sweden. A portal *minPension* provides up-to-date information about accrued pension entitlements across all pension schemes, i.e. public, individual and occupational, in a user friendly way. Additionally, the Swedish Pensions Agency informs all workers about accrued public entitlements through the famous orange envelope. ■

The opinions expressed here are those of the author and do not necessarily reflect the views of the OECD or of its member countries.



DECUMULATION

Finding the right mix

With DC pension saving becoming the norm across Europe, David Adams **explores the options available for savers in the decumulation phase**

WRITTEN BY DAVID ADAMS, A FREELANCE JOURNALIST

The history of pension provision in Europe has tended to be reactive and experimental and it will be for a few more decades before we know whether the use of defined contribution (DC) pensions in Europe has achieved its goals of risk reduction alongside good outcomes for pension savers.

The experiment is now well underway; the DC market is expected to grow at about 6 per cent per year, according to research from Cerulli. Cerulli estimates that DC assets in Europe will reach €2.2 trillion by 2025 – still only a small share of the overall total, but the direction of travel is clear.

However, during the past decade, against a background of low interest rates, increasing longevity and changes to first pillar provision within some countries, it has become clear that the operation of the DC decumulation phase may also need to change. There are different approaches in each country, but most tend to assume either that a DC saver will buy an annuity at retirement, or they will use a fairly inflexible phased withdrawal product. It is now clear that there is a need for greater flexibility, involving use by some retirees of hybrid solutions, incorporating both annuitisation and drawdown elements.

Freedom and choice

The ideal strategy for each individual will vary according to their financial circumstances, particularly the extent to which they will use other sources of retirement income. The starting point for any change is also different in each country. For example, in Switzerland it is effectively compulsory to use second pillar DC savings to purchase an annuity on retirement, while in Belgium, tax rules tend to dictate that most people take DC savings as a lump sum. But it is in the UK, where the DC experiment has advanced the furthest, that we have seen the most development in adapting the decumulation phase to meet a broader range of needs.

The introduction of freedom and choice for pensions by the UK government in 2015 removed the requirement for most people to use DC savings to buy an annuity at retirement. It created some problems, notably in connection with availability of guidance or financial advice to help people decide how to use their savings. The UK pensions industry has also been relatively slow to develop new drawdown and other products to offer retirees more options, although demand for such products is also only growing slowly, because the number of people retiring with substantial sums saved in DC pension pots is still relatively small. But the UK's reforms may well have blazed a trail for some other European countries to follow.

"The freedom and choice reforms were a significant change in direction, but potentially also an appropriate response, given declining interest rates at that time and their effect on annuity rates," says WTW senior director, global services and solutions, Chris Mayo. "The UK went from one extreme to another and we're now seeing that direction being followed elsewhere, but in more modest steps."

Opening up new options

A shift away from the use of annuities is visible in Ireland, says Mercer DC strategy lead, solutions, Nora O'Connell. "Over the past year we've

seen the start of a trend towards using drawdown, as DC pots have got bigger and members got more comfortable with [*continuing to invest some DC savings after retirement*],” she says.

But, as elsewhere in Europe, Irish pension providers are not yet offering all the products needed to meet different retiree requirements. “There is a recognition that with increased longevity and inflation risk there is a need for something that gives you a guaranteed income; or for a deferred annuity that you might take at age 75 or so,” says O’Connell.

She says the Irish pensions industry and policymakers are monitoring developments around collective DC (CDC) provision in the UK and the Netherlands, which help spread some risks for individuals in the decumulation phase, and the lifetime pension concept, which combines features of annuities and drawdown, now being used in Australia.

In the Netherlands, a series of reforms are encouraging more use of DC pensions, whether via a contractual arrangement that places all the risk on an individual, or through participation in collective, often industry-wide DC schemes in the second pillar. DC savers will have the option to take 10 per cent of their savings as a lump sum at retirement and/ or will also be able to use variable or guaranteed annuities.

Mayo is slightly concerned that many European countries may just be starting to move out of a low interest rate environment at present, so undermining the rationale to move away from annuities. “There is still the option to buy an annuity if you want to,” he points out. “It’s about opening up new options.”

Policymakers in other countries, including France and Germany, are considering and/or encouraging more use of DC arrangements for second and third pillar pension provision, with greater flexibility in the decumulation phase. The best course of action will be determined to a large extent by how dependent an individual is going to be on DC pension savings as a source of income in retirement.

“If you largely depend on benefits coming from first pillar DB pension funds then a lump sum from the second or third pillar – of either DB or DC savings – would be less risky,” says Cross Border Benefits Alliance-Europe (CBBA-Europe) secretary general, Francesco Briganti.

Guidance and advice

Whatever decumulation policy is followed, it will be absolutely essential to provide effective financial education, guidance or advice to help people make the best financial decisions. “In my opinion, policymakers should oblige mandatory advice, to explain the risks of what you’re doing with your pension pot,” says Briganti.

Mayo points out that if an individual does not buy an annuity, they will then have more financial decisions to make at a later date – when this may have become more difficult.

He thinks a significant proportion of future DC schemes are likely to involve some form of CDC provision. Current CDC models, as used in the Netherlands and [*soon to be*] the UK, are not perfect, with notable problems involving shortcomings in how the advantages and disadvantages of such arrangements – including variability in the value of, and flexibility governing, pension benefits eventually paid – are explained to scheme members when they join. But again, the right combination of flexibility, coupled with support to help individuals make the right decision, could result in good outcomes.

“THERE IS STILL THE OPTION TO BUY AN ANNUITY IF YOU WANT TO. IT’S ABOUT OPENING UP NEW OPTIONS”

The CBBA-Europe view of the optimal decumulation strategy, as expressed in a reflection paper on the subject published in 2019, is that it should make use of a “gradual annuitisation strategy”, incorporating investment of some capital after retirement, but with it then converted “gradually into an annuity to secure late-life consumption needs”.

PensionsEurope published a paper on DC decumulation in Europe in 2019. It highlighted the potential value and drawbacks of CDC, the need for effective guidance for individuals making decisions about decumulation; and the value of simplicity, with “pension options … kept as simple as possible in order to minimise both (i) administrative costs (ii) and the risk that the options are not understood.” Meanwhile, a spokesperson for the European Insurance and Occupational Pensions Authority (EIOPA) says that its DC good practices project group will be looking closely at decumulations in DC schemes during 2023.

As the blueprint for DC decumulation slowly comes into focus, it may be that member support is the final, yet perhaps also the most important, part of the puzzle, says O’Connell.

“It’s one thing having fantastic products; it’s another thing getting members to engage and making these products understandable,” she says. The Europe-wide experiment continues. ■

SELF-EMPLOYED

Going it alone

With pension provision for employees well-established across most parts of Europe, Natalie Tuck **explores what's on offer for the self-employed**

WRITTEN BY NATALIE TUCK

There were around 19.2 million self-employed people working in the European Union in 2020, according to Statista. Whilst pension provision for employees is largely well-established across the continent, the picture for the self-employed is very different.

PensionsEurope senior policy adviser, Simone Miotto, says: "Around 40 percent of jobs in the EU today are either as self-employed (14 per cent) or in an employment relationship other than a standard form of work." He adds that from research carried out by several organisations, including the European Commission (EC), the OECD and think tanks, "it seems clear the retired self-employed have on average lower pensions, higher assets, which the EC said indicates a higher tendency to accumulate savings for old age outside the pension system, a higher risk of income poverty, and are more exposed to financial hardship".

Furthermore, Miotto says the way in which pension systems cover the self-employed is "very diverse" across the Euroepan Union (EU): "Notably, the self-employed are less likely to be covered by supplementary pension schemes. Together with less favourable access and accrual conditions in public social security schemes; this can further erode their old-age income adequacy."

According to the OECD's *Pensions at a Glance 2021* report, while the self-employed are required to participate in earnings-related pension schemes in most OECD countries (with around a third of those located in Europe), they only contribute in similar ways to employees in the Czech Republic, Estonia, Lithuania, Luxembourg, Portugal and Slovenia (of those located in Europe). In other countries, although self-employed workers are mandatorily covered by earnings-related schemes, pension coverage is limited because they are allowed to contribute less than employees.

As Miotto highlighted, this leads to lower pensions for the self-employed; the OECD says that self-employed workers with a taxable income (i.e. net of social security contributions) equal to the net average wage before tax can, on average in the OECD, expect to receive an old-age pension equal to 75 per cent of the pension of the average-wage dependent worker in the private sector.

Developments

The 2019 Council Recommendation on Access to Social Protection encourages EU countries to ensure that all workers and the self-employed have access to social protection schemes. As a result, Miotto says that the Social Protection Committee is developing indicators to monitor access to social protection.

"The SPC found that there is no country reporting lack of formal access to old-age benefits for the self-employed but noted that (at least) some groups of them have to opt-in to have access (or can opt-out) in nine member states. In some cases, the voluntary access relates to supplementary schemes on top of the mandatory one."

In some countries in Europe, developments within self-employed pension provision are being proposed and made. In Denmark, for example, its Pension Commission has recently proposed introducing a pillar one scheme, which would cover the self-employed.

Insurance and Pension Denmark director, Karina Ransby, says: "Its idea is that the self-employed and employees without a work-related

pension scheme should save 3.3 per cent of their income in ATP – pillar one. And it will be compulsory for all self-employed workers who also pay in for the maternity scheme and who save less than 3.3 per cent in an alternative pension scheme.

"We think that the proposal can nudge the self-employed and employees without a pension scheme to commence saving more than the 3.3 per cent and hopefully then also supplement with an insurance for invalidity."

Although nothing has been announced yet, change also seems to be on the cards in the UK. In January, the country's Pensions Minister, Guy Opperman, confirmed that work is "in progress" to create better pension saving solutions for self-employed savers. Opperman emphasised that whilst the self-employed are able to sign up to a private pension, it is "much more complicated because you don't have any of the benefits of auto-enrolment (AE)".

The OECD's report also notes that Belgium and Greece have recently taken measures that will affect the future pensions of the self-employed. Belgium has substantially increased self-employed future pension levels without adjusting their contributions. In Greece, however, its reform has reduced the pensions those who are self-employed can expect to receive by reducing their contributions. According to the OECD, this will result in the self-employed receiving a pension equal to less than half of the employee's pension, compared to 12 per cent lower before the change.

In the Netherlands, which is seeing its pension system undergo a huge transformation, with employed workers moved from DB-style schemes to DC-like schemes, the Federation of Dutch Pension Funds is disappointed with the lack of progression for self-employed pensions.

"The new pension agreement does not introduce anything new for the self-employed that will actually make a difference, in our opinion," a spokesperson for the federation says. "That is a pity; a robust pension system for the future should also be inclusive, for all workers. The current regulation falls short on this point. The existing framework is dominant in the new agreement, so there is insufficient room for experiments within which pension funds can organise a suitable offer for the self-employed in an affordable manner."

Riding solo

The general picture painted is that self-employed workers that would like to save for their retirement above the basic provision provided by their country have to go it alone. But what products are available to them?

In Denmark, Ransby notes: "As a self-employed person you can save for a pension at one of the commercial pension savings institutes like PFA, Velliv and Danica etc. Many institutes have pension products specifically aimed at the self-employed – it is voluntary to do so."

However, according to Insurance and Pension Denmark's research, around 50 per cent of all self-employed people do not have a sufficient pension. "They can have sufficient alternative savings for their retirement in e.g. their company. In principle we think everyone should save for their retirement through a pension scheme. In order to obtain this, we think the economic incentives for saving should be so obvious that everyone will do so," Ransby says.

In Ireland, Irish Association of Pension Funds CEO, Jerry Moriarty, notes that there are personal pension products available to the self-employed, such as Retirement Annuity Contracts (RACs) and Personal Retirement Savings Accounts (PRSAs). "As part of the reform and simplification agenda, it is intended to phase out RACs so that PRSAs would be the only product for the self-employed."

This is similar to what is currently on offer in the UK – personal pensions, self-invested personal pensions (SIPPs) and stakeholder pensions. Although not a pension, the UK also offers the lifetime ISA, available to anyone under 40, as another retirement savings product.

For those in the EU, another suitable product will hopefully be on the market shortly – the pan-European personal pension product (PEPP). Regulations for the cross-border pension product have been in effect since March this year, but as of yet, no products have launched to the market. However, this third-pillar product is mainly aimed at people who cannot join occupational pension schemes, Cross-Border Benefits Alliance - Europe secretary general, Francesco Briganti, says: "One of the main targets for PEPPs will be the self-employed who plan to increase their future pension in addition to the statutory/mandatory/first pillar pension. In principle, PEPPs might be ideal for this category of self-employed, but only on condition that their tax/fiscal treatment will be equal (or, advantageous) to the national pension products offered in their state of residence.

Unfortunately, EU member states have not yet disclosed their decision on fiscal treatment for PEPPs operating in their territories," Briganti explains. He raises the point, though, that if an existing national personal pension. For now, at least, the self-employed continue to go it alone when it comes to pension provision. ■

INTERVIEW

Seeking positive change

Federation of Dutch Pension Funds chairman, Ger Jaarsma**, speaks to** Jack Gray **about his first eight months in the role and the upcoming reforms to the Dutch pension system**

How has your first year as chairman of the Pensioenfederatie been?

It's a great moment to be chairman of the Federation of Dutch Pension Funds (Pensioenfederatie). It is a huge federation; we have 178 pension funds in the Netherlands and they are all members of the Pensioenfederatie. We're talking about 5.9 million participants, 3.6 million pensioners and 10 million early leavers, and €1,800 billion assets under management. So, it is a very important association. It's important for almost all people in the Netherlands. On the other hand, it is a good time to become chairman because we had a Pension Agreement that was concluded in 2019 and the Ministry of Social Affairs has converted this into legislation in recent years and now, this year, the House of Representatives and the House of Lords have to decide on it. Then, pension funds have four years to switch to the new system. There is plenty of work for the next five years, so this is a really great moment to become chairman of this federation.

What work has been done at the federation over that time and what are you currently working on?

We've been working with the government. In recent years, the federation has spent a lot of time helping to design the legislation. Not all of our points are in the draft legislation, so now we are very busy with lobbying. I've spoken with a lot of members of parliament; we tell them we are very pleased with the legislation because it is close to the Pension Agreement we made in 2019, but there are some points that we don't agree with the ministry on and that is what we are lobbying for.

The main work has been on this legislation, but there are two other main points. One is communication; as many pension fund participants are not engaged with their retirement, we have set up campaigns to explain to them how the current pension system works, but also how the new pension system will work in the future. We have a lot of projects on communication to involve the people more with their retirement and pensions. There is ample reason to do so. The Netherlands has the best pension system in the world after Iceland, according to the *Global Pension Index* of Mercer and CFA Institute. Ninety per cent of the employees make use of it, the trade unions support the system, and the combination with the state pension is beneficial. As a result, there is little poverty in the Netherlands among the elderly, which not only offers income security but also social stability. We want this to be known by the general public.

The third point is what we call 'Pensioenfederatie 2.0'. The federation was formed 11 years ago from three small federations, and we think now is the time to take the next step in professionalisation, governance and those sorts of things to make the next step.

What challenges have you faced during this time?

In an association, you are always busy finding the solution that is best for most of the members, and you don't always know up front what the right way is. You get to work on and discuss the problems and, in the end, you understand which way most of the members want to go and that's where we go. We are facing the largest transformation ever with the new system and the new legislation, so that is a big issue. We and the ministry want this legislation to be effective on 1 January 2023 and then pension funds have until 1 January 2027 to get it done. This year, the main subject is the new legislation but also communication.

"DUE TO THIS LARGE TRANSFORMATION, PEOPLE'S TRUST IN THE SYSTEM IS NOT VERY HIGH"

Due to this large transformation, people's trust in the system is not very high. They are scared because they do not know what is coming, which is why it is very important that we explain what we are doing now, the good work our members are doing and why we need to move to the new system, as it will be a better system for the people.

What are the important topics for the federation over the longer term?

I would say responsible investing would be the priority for the sector and we are working with policymakers to make sure the environmental, social and governance (ESG) disclosures work well for pension funds. That is the main point for the next 10 or 20 years. The progress in the Netherlands is good, because we have an agreement on climate goals and the larger pension funds have been joining it for a few years now. The smaller pension funds are also now joining it, so every year we are making progress. Sometimes it is difficult because what we see is some pension funds selling their shares in oil and that kind of thing, while other pension funds do not sell but have discussions with the companies about how they can become more environmentally friendly. Pension funds have different strategies, but they are all aware and adopt the carbon reduction plans in order to combat climate change. Every year there is progress, more pension funds are joining the agreement, within which they make steps forward in fighting climate change. We also see a lot of social pressure. Participants within the pension funds put a lot of social pressure on the pension funds' board members to do something with climate goals. Our government has a Minister for Climate, but it is more the social pressure that is moving the boards of pension funds than the government.

The Netherlands has recently appointed a Pensions Minister. What will their role consist of and what impact do you think having a dedicated Pensions Minister will have?

We now have this minister for three subjects: participation, poverty, and pensions. She only has these three subjects, so she can pay a lot of attention to them. We as a federation are very pleased that this government pays so much attention to pensions. We have to [*pay a lot of attention to pensions*], because we are facing the largest transformation ever. What we see, alongside this Minister for Participation, Poverty and Pensions, is a Minister for Climate. This government's new ministers show how important these subjects are. We are in this huge transformation that has been needed for 10 years; it has taken a long time to come to the agreement so it is very necessary that we speed up and having a Minister for Pensions will help as it is one of her priorities. It took a lot of talking to come to the agreement in 2019, but it has to be set up in legislation, which is where the Ministry of Social Affairs has to do its job. Then Covid-19 came and that did not speed things up. The agreement was that this new legislation should be in place on 1 January 2022, but that did not work out as it was too much work and Covid-19 didn't help. Now we are working to 1 January 2023 but that means that both houses of parliament have to decide this year. We hope the House of Representatives will decide in June and then the House of Lords in September/October. ■

GENDER GAP

Unfinished business

The gender pensions gap continues to be a major issue in Europe. Jack Gray **investigates the severity of the problem, how the gap is being tackled and what more needs to be done**

WRITTEN BY JACK GRAY, A FREELANCE JOURNALIST

Pension inequality between genders is a reality facing women across Europe. As the continent moves further into the 21st century, it may seem staggering that the gulf in pension wealth between men and women exists to the extent it does, but it is as a result of long-term societal inequality between men and women. The problem runs deeper than just pensions, and will take more than efforts from just the pensions industry and pension policy reform to fix. However, there are steps the industry and policymakers could be, and are, making to help narrow the gap.

"THE GENDER PENSION GAP IS SEEN AS AN IMPORTANT ISSUE, YET IT IS NOT WIDELY DISCUSSED. MOST OFTEN, CONCERN IS BORNE OF HIGHER POVERTY AMONG ELDERLY WOMEN. THE GENDER PAY GAP IS A MORE FREQUENT TOPIC. IT IS HIGHER IN FINLAND THAN IN THE OTHER EU AND NORDIC COINTRIES"

Severity of the issue

According to data from Eurostat, the average woman in the EU in 2019 aged over 65 received a pension that was 29 per cent lower than the average man's. The same figures show the largest gender pension gap was in Luxembourg (44 per cent), while the lowest was in Estonia (2 per cent).

"The gender gap is a major issue in pensions, and it has been increasingly investigated and discussed," comments PensionsEurope senior policy adviser, Simone Miotto.

"They [*Eurostat*] observed that over time the gender pension gap was 5 percentage points lower compared with 2010 (34 per cent), thus showing that something is moving towards the right direction,

but also that we are still far away from full gender equality."

In Sweden, the average gender pensions gap is around 30 per cent, notes Skandia pension economist, Mattias Munter. He explains that the Swedish pension system is designed to reflect lifetime earnings, therefore as women tend to work fewer hours and in lower paid jobs than men, the gap will not close for the foreseeable future.

"The gender pensions gap is significant in Ireland – as it is across most of the developed world," says Mercer Ireland head of career consulting, Danny Mansergh.

"An additional issue that is often overlooked is that women live longer than men. Therefore, all other things being equal, women need to accumulate larger pensions than men, because they need to provide an income in retirement for longer.

"This is a much bigger issue for those saving through defined contribution plans – and going forward that's going to be the vast majority of people."

Finnish Centre for Pensions head of research, Susan Kuivalainen, adds: "The gender pension gap is seen as an important issue, yet it is not widely discussed. Most often, concern is borne of higher poverty among elderly women.

"The gender pay gap is a more frequent topic. It is higher in Finland than in the other EU and Nordic countries. The gender pay gap, which is largely related to a high labour market segregation, is the main contributor for the gender pension gap. Nowadays, there is no major difference between men and women in terms of average employment rates, career duration or retirement age."

Bridging the gap

Attempting to bridge the gap between men and women's pension savings is a policy area that needs to be addressed in every member state, with the vast majority appearing to be trying to achieve a more equal retirement.

"To tackle the problem, you first have to understand the causes," states Mansergh. "We did considerable internal research on this in Mercer in Ireland in 2020.

"That research indicated that the major contributing factor to the gender pensions gap is the gap in career-long earnings. That career earnings gap is in turn attributable to two things: the gender pay gap and the greater tendency of women towards part-time work and career breaks."

He notes that, "contrary to some popular theories and to some findings in other countries", Mercer did not find evidence of women being reluctant to join pension schemes, having a tendency to contribute less to DC schemes, or risk aversion among women when making investment choices.

"For the problem to be tackled, the gender pay gap needs to reduce and the disparity between the genders in terms of part-time work and career breaks also needs to narrow," Mansergh says. "Education and support also need to address the realities of the gender pensions gap and of longer female life expectancy."

Miotto adds: "The reasons behind these numbers are of a very different nature and strictly interlinked with the national social, economic, and labour markets dimensions of the country considered. Therefore, many different actions have been taken at different levels to tackle the problem.

"From an EU policy perspective, gender equality is a core value of the EU, a fundamental right, and a key principle of the European Pillar of Social Rights. The gender pension gap issue has been flagged as a matter of concern by the EU institutions on several occasions, and its reduction is notably one of the key objectives of the 2020-2025 *Gender Equality Strategy* of the European Commission."

"FROM AN EU POLICY PERSPECTIVE, GENDER EQUALITY IS A CORE VALUE OF THE EU, A FUNDAMENTAL RIGHT, AND A KEY PRINCIPLE OF THE EUROPEAN PILLAR OF SOCIAL RIGHTS"

The national level perspective is also very important, as national governments are best placed to account for and address the factors that can lead to gender inequalities and ultimately to decide on the specific actions to take to tackle the problem, according to Miotto.

"Recent efforts and reforms in different areas led to improvements, but many countries are still far from fully solving the issue," he notes.

In Sweden, a lot of focus is on increasing the minimum pension payments from the national public pension system, Munter explains.

"If successful, this would make the public pensions more gender equal in terms of pension payments," he continues. "A potential downside would be that the driving force for working, that an earnings-related pension system is depending on, could deteriorate."

Finnish Centre for Pensions specialist adviser, Suvi Ritola, details the efforts being made in Finland to bridge the gap: "The pension reform in 2005 included

improvements to pension accrual from childcare periods. The effect is to be seen in future pensions.

"The measures aiming to balance the labour market differences, that is measures outside the pension system, are seen as most essential also from the point of view of pensions. For example, the equal pay programme brings together the measures of the government and central labour market organisations to promote equality in pay.

"In 2022, a family leave reform was introduced, which aims further to divide family leave and care responsibilities equally between both parents in a family and strengthen equality in working life and to reduce pay differences between the sexes."

What next?

Although these measures appear to be a good start at trying to tackle the gender pensions gap, it is clear that more needs to be done to alleviate the issue further.

However, driving major change may be difficult for the pensions industry on its own, with both Kuivalainen and Munter noting that the gap stems from wider issues relating to employment, society and family.

"Full gender equality has not been achieved in any member states, so more needs to be done," says Miotto.

"We must find effective policies that diminish the pension gender gap. I think those aimed at reducing the labour market differences are crucial.

"As for occupational pensions, there are huge gender differences in coverage per sector and female-dominated sectors tend to offer less occupational pensions. Increasing the availability of occupational pensions in sectors predominantly employing women could be an effective policy to tackle the pension gap.

"Raising awareness of the issue and proper communication are also important tools to tackle the gender pension gap." ■

"FULL GENDER EQUALITY HAS NOT BEEN ACHIEVED IN ANY MEMBER STATES, SO MORE NEEDS TO BE DONE"

INVESTMENT TRENDS

Taking it to the next level

The path to net zero 2050 is strewn with obstacles — so should pension funds be doing more now to mitigate the risks of climate change?

WRITTEN BY MAREK HANDZEL

The number of European pension funds that are aligning themselves with the Paris Agreement by aiming to reach net-zero carbon emissions within their investment portfolios by 2050 continues to grow by the day.

Late last year, Cerulli Associates found that some 40 per cent of European-based pension funds had pledged to hit net zero by a certain date, with another 20 per cent planning to do so in the next 24 months.

"Through the European pensions market, environmental, social and governance (ESG) integration has become a 'hygiene factor' especially in France, the Netherlands, and the Nordic region," says Cerulli Associates research analyst, Ross Langbridge. "[*And*] an increasing number are making formal commitments to net zero."

That "hygiene factor" is about to be taken up a notch or two, after the European Insurance and Occupational Pensions Authority (EIOPA) launched its first climate stress test for the European occupational pensions sector. The EIOPA initiative has added to the clamour for pension fund portfolio decarbonisation. But it also means that there is now no escape from some awkward questions that have to be answered as schemes attempt to go green.

"ACHIEVING NET-ZERO CARBON EMISSIONS BY 2030 IS GOING TO BE DIFFICULT"

Taking the right direction

One of those questions is whether there is actually any reliable way to test how resilient pension investment returns are to climate risk.

There are some simple steps that can be taken to determine exposure to climate risk. The size of a fund's allocation to thematic investment vehicles that focus on decarbonisation or similar strategies, such as regenerative agriculture or sustainable water is an obvious one. But, as Tikehau Capital head of ESG, Laure Villepelet, explains, there is no set standard that can give funds an ideal pathway to mirror.

"What we are doing at Tikehau Capital is testing different providers and different methodologies (such as portfolio temperature or climate value at risk). That includes [finding the best ways] to consider risk related to transition risk and physical risk."

Cardano group head of sustainability, Will Martindale, collates the methods to achieve net zero under three broad categories: metrics; scenario planning; and target setting.

In terms of metrics, financed emissions have gained the most traction. This means funds looking at the entire capital structure of

"IF WE WANT TO TACKLE CLIMATE CHANGE WE NEED TO ENTER IN THIS PILOTING, MONITORING MODE, RATHER THAN JUST DOING SOME REPORTING ON A QUARTERLY BASIS"

a company and determining what percentage of debt, equity, and cash they hold as an investor. They then calculate that company's emissions and allocate their ownership of those emissions based on the proportion of their ownership of that company. "And then you can repeat that across your investments," says Martindale. "You can aggregate that and that gives you a sense of how many greenhouse gas emissions, you are responsible for. That tends to be mostly across [*the Greenhouse Gas (GHG) protocol's*] Scope 1 and Scope 2 emissions."

Scenario planning is far more complex, particularly in a world that cannot stop presenting us with Black Swan events. As a result, Cardano advises its clients to use scenarios based on temperature metrics. This involves working out what the financial risks are to a portfolio should the earth warm by 1.5 degrees, as well as physical risks from droughts, rising sea levels, and so forth.

The final category underlines the importance of target setting. Without a date in the calendar, it becomes very hard to make decisions around how, and when, to decarbonise various allocations.

Unreliable measurements?

Undertaking appropriate processes is one thing, but being able to rely on accurate information is another.

As PensionEurope chief economist, Pekka Eskola, points out, climate risk is not a traditional type of risk. Not only is there not enough historical data, there is also great uncertainty as to the likeliness of how and when climate modelling scenarios will emerge. Added to that is the debate over whether climate risk is to some degree already priced into some investments.

"A broad spectrum of models exists in the market but there is a lack of consensus," says Eskola. "There is a dilemma that testing resilience in an appropriate way would require a horizon that is long enough (some decades). But the longer the horizon, the more dependent the reliability of calculations on assumptions, and the results become unrealistic.

"Another challenge is that there is no consensus amongst economists and designers of climate models about the impact of climate change [*on fiscal and monetary policy*], such as interest rates. [*They do not have a clear picture*] on the size of the effect — nor on the direction."

The Scope 3 shadow

Matters are further complicated by the looming requirements involved in Scope 3 emission disclosures.

Speaking at the Irish Association of Pension Funds' (IAPF) spring conference in March, Insight Investment integrated solutions credit portfolio manager, Claire Bews, suggested that pension funds are cautious about building low-carbon portfolios based solely on Scope 1 and 2 numbers, as they could have a "rather unpleasant surprise" when Scope 3 figures — which make up about 70 per cent of total portfolio emissions — are eventually incorporated into their carbon emission reporting. "Having gone through a decarbonisation process in your portfolio you may find that you have to go through it again," she warned.

The potential ramifications of delayed Scope 3 reporting, particularly in relation to fast-tracked net-zero plans, leads to inevitable questions about how realistic some decarbonisation plans really are.

"Achieving net-zero carbon emissions by 2030 [*as some organisations are aiming for*] is

going to be difficult, but it's good to [*at least*] try to aim for [*a certain date*]," says Villepelet.

"You certainly have to think big and be ambitious when it comes to climate transition and low-carbon transition, because it's the biggest threat to our economies and societies."

As Martindale says, it is relatively easy to decarbonise some aspects of a portfolio. There are some industries that clearly emit far fewer emissions than others. But picking low-hanging green fruits has never been the problem. It is sectors such as shipping and aviation, which are very hard to move into a low-carbon world at present, that are causing headaches for sustainability officers. And even if the technology to do so existed en masse from tomorrow, the speed of the rollout would probably be painfully slow and hampered by the huge costs and politics that such a transition in transport fuel sources would inevitably generate.

More talk, more action

These types of challenges make engagement more critical than ever before.

The largest European pension funds are already actively engaging with their investment managers, says Eskola, systematically identifying any negative impact the activities of the investee companies may have on society and the environment, and exerting influence on companies to reduce this negative impact.

This can involve quizzing managers on whether they link employee bonuses at some level to impact targets; and to challenge them on their sustainability measurements. "Initially, they won't be perfect, but that's not so important. What matters is working on the topic," says Villepelet.

"You cannot monitor a manager on a daily basis, but you can challenge them on how they are monitoring risks and really understand whether it's just an external consultant coming in once a year to do some climate analysis, or if they're a bit more active in managing this risk.

"If we want to tackle climate change we need to enter in this piloting, monitoring mode, rather than just doing some reporting on a quarterly basis."

In Cardano's view, engagement is an area that is currently undervalued within the investment industry, says Martindale. "There are successful attempts by investors to engage companies such as the Climate Action 100+ initiative, but we think that there's a lot more potential there. The investors involved in these engagements tend to be asset managers — but pension schemes can play a stronger role in incentivising quality engagement."

Closer interaction with the managers and companies that pension funds are invested in can be boosted by the use of bonuses, suggests Villepelet. "In order to improve, pension funds need to set their commitments and then have people responsible for delivering on that strategy. If everyone is incentivised then that is even better."

Beyond their own investments and activities, pension funds can also have an impact on the discussion more widely in society, says Eskola. This entails conversing openly with members of various international and global initiatives, and then opening dialogue with other stakeholders, including policymakers, academics, and the press.

Martindale agrees: "There are opportunities for pension schemes to be more vocal in order to encourage governments to ensure that there are strong decarbonisation policies in place." ■

"IF EVERYONE IS INCENTIVISED THEN THAT IS EVEN BETTER"

In their own words...

Industry personalities' comments on the hot topics affecting the European pensions space

On financial education in Sweden

"Financial literacy, or personal finance, is part of the school curriculum in Sweden from the first grade. There are plenty of opportunities to learn and so we mostly teach people who are already literate about diversifying their investments.

"We realised recently there is a problem with words. We talk about saving and saving in the stock market, but to some people saving is simply keeping money in their account. Given we have been living with a 0 per cent interest rate, this is an area we want to focus on more: what does saving mean to people?"

Gilla Din Ekonomi adviser, Therese W. Ekman

On achieving net-zero carbon emissions

"Achieving net-zero carbon emissions by 2030 [as some organisations are aiming for] is going to be very difficult, but it's good to [at least] try to aim for [a certain date]. You certainly have to think big and be ambitious when it comes to climate transition and low carbon transition, because it's the biggest threat to our economies and societies."

Tikehau Capital head of ESG, Laure Villepelet

On the Danish Pension Commission's recommendations

"We completely agree with the Pension Commission that there is a need for a unified, sharp and independent pension policy in Denmark, so that in the future we still have one of the world's best pension systems. The commission has looked at the pension system at the seams, and they, like us, are concerned with improving the incentives to save for retirement and making the individual Dane's withdrawal from the labour market more flexible."

KENT DAMSGAARD
I&P Denmark CEO

On the impact of the pandemic on the pension saving landscape in Europe

"Many supervisors across Europe have introduced measures to reduce the administrative burden and ease the fulfilment of legal obligations and ensure the operation and governance of IORPs. EIOPA's 2021 *Consumer Trends Report* reveals that the impact of Covid-19 has not been uniform across countries. Several member states cannot conclusively say whether the Covid-19 crisis has negatively impacted pension contributions. Nevertheless, almost one third of the national markets reported a decrease in contributions mainly due to shrinking in business (sponsor contributions) and lower personal income."

EIOPA spokesperson

On the shift towards drawdown products in Ireland

"Over the past year we've seen the start of a trend towards using drawdown, as DC pots have got bigger and members got more comfortable with [continuing to invest some DC savings after retirement]."

Mercer DC strategy lead, solutions, Nora O'Connell

On the need for reform in the French pension system

"A reform is indeed needed, and since French workers have on average five additional years of retirement length compared to the other OECD countries, aiming at postponing the retirement age is only natural. However, this should be planned along with employment measures for seniors, as France is also a country where the employment rate is one of the lowest in Europe when it comes to people above 55 years old."

BENJAMIN SANSON
Mercer France head of retirement and employee savings consulting

On what the Federation of Dutch Pension Funds is currently working on

"We've been working with the government. In recent years, the federation has spent a lot of time helping to design the legislation [*for the Pension Agreement*]. Not all of our points are in the draft legislation, so now we are very busy with lobbying. I've spoken with a lot of members of parliament; we tell them we are very pleased with the legislation because it is close to the Pension Agreement we made in 2019, but there are some points that we don't agree with the ministry on and that is what we are lobbying for."

GER JAARSMA
Federation of Dutch Pension Funds chairman

On the pensions gender gap

"The gender gap is a major issue in pensions, and it has been increasingly investigated and discussed. They [*Eurostat*] observed that over time the gender pension gap was 5 percentage points lower compared with 2010 (34 per cent), thus showing that something is moving towards the right direction, but also that we are still far away from full gender equality."

SIMONE MIOTTO
PensionsEurope senior policy adviser

On UK defined benefit scheme funding level improvements

"The month end position has again shown an improvement month-on-month and is now back at a level last seen in April 2020. The main driver of the change has been the increase in bond yields. These improvements are good news in the current economic environment."

Mercer UK wealth trustee leader, Tess Page

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