European Pensions

Summer 2024

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AI: Friend or foe?

As a journalist, the notion of artificial intelligence (AI) taking over the profession, leaving me out of a job, sends shivers down my spine. But recently, we at *European Pensions* were told that we could use AI services, such as ChatGPT or Claude, to complement our work. And with the European Union on the cusp of introducing the world's first AI regulation, I decided to set it a task – to write my editorial comment for this issue.

Now, you might think I would print it in full below, but that would a) be doing myself out of a job (shivers) and b) not complementing my work but doing it for me. Plus, it was just not good enough!

In my opinion, it was far too cliché, with a hallmark of a marketing graduate desperate for their first big break. ChatGPT writes: "Join us as we illuminate the path toward financial wellbeing and prosperity for all, united by our shared commitment to safeguarding the golden years of every citizen across this vibrant and dynamic continent."

I think, at least for now, AI is not a threat to journalism, but instead a useful tool to complement research and provide inspiration for features and articles. But what about the pensions industry? Already many pension funds and providers use chatbot tools to communicate with members. Robo-advice is also available to those looking for a more affordable advice solution. It remains to be seen what impact the EU's forthcoming AI Act will have on innovation within AI, and its impact on the pensions sector.

> **"ALREADY MANY PENSION FUNDS AND PROVIDERS USE CHATBOT TOOLS TO COMMUNICATE WITH MEMBERS"**

In our *Ask the Industry* this month, we asked industry experts what impact the AI Act will have on the pensions industry and whether AI, generally, will be a help or hindrance – you can read their answers on page 56.

That's not all we look at, as ChatGPT kindly writes: "From Dublin to Dresden, Madrid to Moscow, we traverse borders and boundaries to bring you an unparalleled perspective on the state of pensions in Europe."

Well, that's not completely accurate, but we do explore the changing pensions landscape in Ireland [*page 18*] as it is set to introduce an auto-enrolment pension system. We also examine the sustainability of the Spanish public pension system [*page 42*] and many more topics that our friend AI could not enlighten you about, but that you can do yourself through reading this non-AI generated issue of *European Pensions*!

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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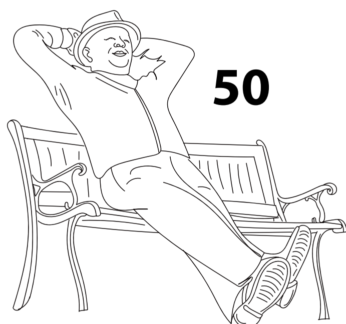

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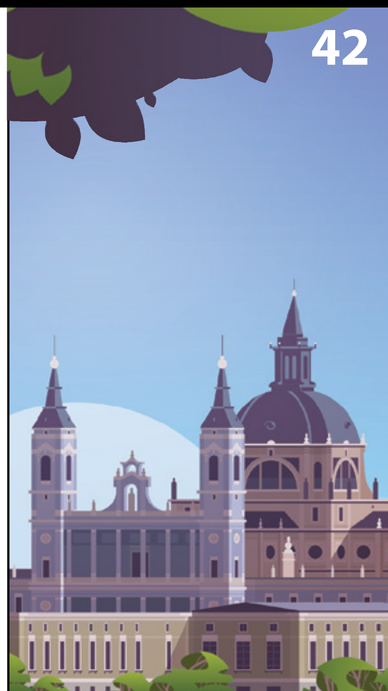

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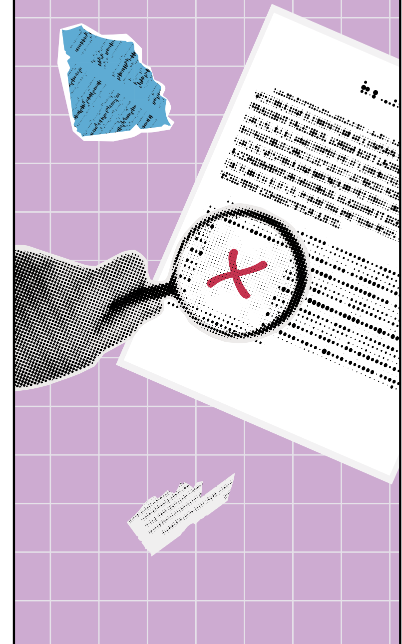

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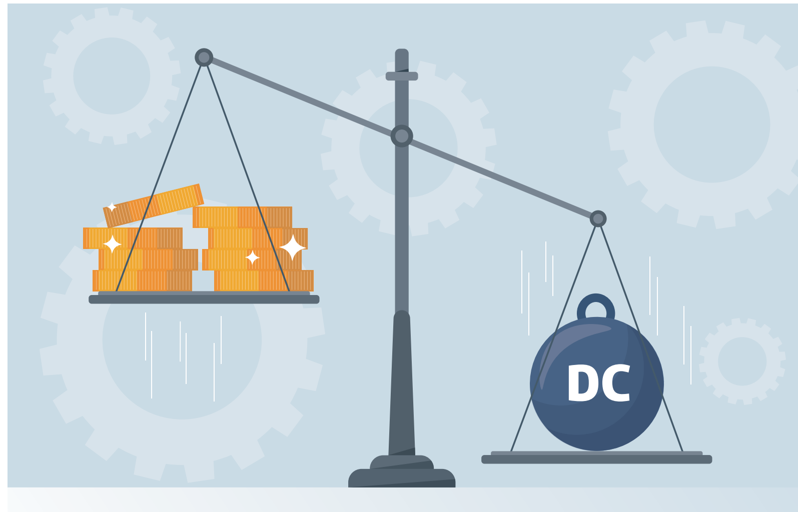

PensionsEurope stresses importance of secure retirement outcomes in switch from DB to DC

THE REPORT OUTLINED RECOMMENDATIONS IN KEY AREAS

Written by: Natalie Tuck and Jack Gray

PensionsEurope has stressed the importance of ensuring pension savers achieve secure retirement outcomes as countries shift from DB to DC pension systems, in its report, *Road to DC: Understanding the Shift*.

The report aims to analyse the ongoing transition from DB to DC pensions across European member states and provide solutions for developing resilient and adequate retirement provisions for a more DC-focused landscape.

Whilst it acknowledged there is no one-size-fits-all solution to DC pensions, due to the differences in the precise nature of DB and DC across member states, it outlined some key principles for achieving good retirement outcomes.

In particular, PensionsEurope argued that workplace DC schemes should prioritise good outcomes for members, based on a "robust yet flexible" design, while investments should be suitable to participants' needs and any default arrangement should be appropriate.

Promoting cost-effective retirement arrangements was also highlighted as important, both in the accumulation and decumulation stages. However, it clarified that while costs and charges should offer value for money, it is essential that a 'race to the bottom' on fees is avoided.

The report added that good communication must ensure members have a clear understanding of what to expect at retirement and how to meet these expectations.

While the shift from DB to DC has been taking place for many years in some member states, the paper indicated that some historically DB/hybrid-dominated systems have been experiencing a more recent transition to DC, with varying magnitude levels.

But despite the growing focus on DC pensions, the majority of members are still currently enrolled in DB schemes.

In the transition, PensionsEurope encouraged robust scheme design, comprehensive decumulation options and tailored legislation to national contexts, and argued that striking a balance between regulation and operational efficiency was essential to safeguard members' interests and minimise the administrative burden.

This has not been PensionsEurope's only recent call for change, as the association also recently called for a cost assessment to be undertaken in relation to the impact of the IORP II Directive before the European Commission reviews the regulation.

The call was made in its updated position paper on the IORP II review, following the European Insurance and Occupational Pensions Authority's (EIOPA) technical advice on the directive in September 2023. Its advice on the directive covers a range of topics, aiming to ensure the "directive can embrace the future while protecting the legacy" of IORPs.

In its position paper, PensionsEurope set out its response to the key recommendations made by EIOPA, covering areas such as governance and prudential standards, cross-border activities and transfers, information to members and beneficiaries and other business conduct requirements, the shift from DB to DC, sustainability and diversity and inclusion.

Overarching all of this was its recommendation for the cost assessment, as the implementation of the IORP II Directive

had a "huge cost increase", especially for small and midsized IORPs.

"Therefore, due consideration should be given to the cost increase of the proposed changes to IORP II, not only for each change but also on an aggregate basis of all proposed changes. For this reason, before the upcoming review, we believe that a proper cost assessment as part of the impact analysis needs to be conducted in order to avoid a disproportionate cost increase falling on all and especially smaller IORPs," the association stated.

In addition, PensionsEurope stressed that the minimum harmonisation aspect of the legislation must continue.

"Due to the occupational nature of IORPs, national social and labour laws and national social partners at the company, industry, and higher levels have set up very different IORP types and IORP activities across Europe," it stated. "This diversity must be fully respected by European IORP legislation, and it is imperative that none of these national occupational pension systems may be harmed."

"It is imperative that none of these national occupational pension systems may be harmed"

Amid the ongoing IORP II review, EIOPA's latest Risk Dashboard also revealed that IORPs' exposure to market and asset return risks remains high due to market volatility and real estate market vulnerabilities.

EIOPA's IORP Risk Dashboard summarises the main risks and vulnerabilities in the IORP sector of the European Economic Area (EEA) for the different schemes.

This showed that annual indicators, such as portfolio return (based on 2022), do not yet capture the positive market performance of 2023.

However, macro risks are at a medium level with macroeconomic indicators showing signs of positive developments. This includes a decline in forecasted inflation and improvements in the GDP growth outlook – economic growth nevertheless remains relatively weak.

Furthermore, liquidity risks are at a medium level but show a decreasing trend compared to the previous quarter, driven by developments in derivative positions. The net asset value of IORPs' derivative positions, which are typically used to hedge against a drop in interest rates, shifted closer to zero from earlier negative readings due to lower market interest rates in Q4-2023.

Reserve and funding risks, meanwhile, remain unchanged at a medium level with a slight deterioration in the financial positions of defined benefit IORPs due to lower interest rates. All other risk categories are currently assessed at a medium level, with increases expected in the risk level for digitalisation and cyber risks over the next 12 months.

News in brief

■ **European** pension providers celebrated their success after dialogue with Shell prompted the energy giant agreeing to disclose its lobbying activities. Dialogue between Shell and Denmark's Sampension, Norway's KLP and Australian NGO the Australasian Centre for Corporate Responsibility (ACCR), means that in the future, Shell will outline its climate and energy-related lobbying activities in five to ten emerging countries that are important to its strategy.

■ The **Finnish** Pension Alliance (Tela) updated its guidelines for occupational pension insurers on the prevention of money laundering and terrorist financing. The update was made in response to changes in legislation, with the guidance now taking into account changes introduced by the partial reform of the Money Laundering Act and the Financial Supervisory Authority's Regulations and Guidance 2022/23.

■ **Spanish** pension funds' assets increased by €3.8bn in the first quarter of 2024, rising to €126.1bn at the end of March, according to the latest figures from Inverco. Inverco attributed the growth to the positive performance of investments in the first three months of the year.

■ **British** LDI funds in Ireland and Luxembourg will need to be able to resist a rise in GBP yields of at least 300 basis points, under new restrictions from EU financial markets regulator, the European Securities and Markets Authority. The requirement was part of ESMA's advice to the Central Bank of Ireland and the Commission de Surveillance du Secteur Financier.

DNB confident of 'smooth transition' to new pension system

THE TRANSITION TO THE NEW DUTCH PENSION SYSTEM CONTINUED AHEAD OF THE JANUARY 2028 DEADLINE

Written by: Natalie Tuck and Jack Gray

De Nederlandsche Bank (DNB), the Dutch pension regulator, is confident of a smooth pension transition, DNB president, Klaas Knot, has said in a keynote speech on the transition.

As well as sharing that he has no doubts the transition will succeed, he used the speech to reiterate the need for the transition to a new pension system, despite the Dutch pension system consistently being ranked as one of the best in the world.

"We have embarked on the biggest financial operation in the history of our pension system: The infusion of potentially €1,500bn into the new system. And by 'we' I mean you, the pension funds, the social partners, the pension administrators and AFM and DNB, the regulators. We collectively," he said. "I know that there are concerns among some of you about whether we can complete the pension transition in an orderly and timely manner. And the current political climate is not entirely helping to allay those concerns either. So let me say this in advance: there is not a hair on my head – and despite the passage of years, there are still a few left – there is not a hair on my head that doubts that we will succeed."

On the need for a new pension system, Knot listed several reasons, such as pension funds not being able to meet their commitments, who have to make cuts, where he referenced funds that were not able to index for over a decade. This, he said, resulted in angry participants who no longer have confidence that their fund will deliver the pension they were promised, and no longer trust the pension system.

Discussing the benefits of the new system, he said pension funds will align investment policies with the risk attitudes of different generations.

"As a result, the risks to which young and old people are exposed better match the risks they are willing and able to take. In addition, the interest rate risk of young people no longer needs to unintentionally fall on older people."

Work by schemes on the transition is well underway, as a number of pension funds have now agreed on their new scheme with social partners, including PFZW and PME Pensioenfonds.

Industry research also found that the Dutch pensions sector is "well on track" with its preparations to switch to the new pension system, despite suggestions that employers could be "taking it easy" with their preparations.

In its paper to the House of Representatives, the Pension Federation said that while the transition was a major operation, all Dutch pension funds were doing everything they can to comply with the deadlines.

This is despite research from Aon Netherlands revealing that employers were "still taking it easy" with their preparations, with 45 per cent having done little or no preparation for the transition.

Furthermore, whilst a large majority of companies were sufficiently aware of the changes to pension legislation, 45 per cent had done little to no preparation for the transition.

Controversy surrounding German pension reforms continues

A POSSIBLE INCREASE IN CONTRIBUTION LEVELS TO SHORE UP THE COUNTRY'S PENSION SYSTEM PROMPTED CONCERN

Written by: Pete Carvill

Controversy has continued to roll in about the recent proposed pension reforms in Germany, after figures in February revealed that more than a third of the federal budget was earmarked for the Federal Ministry of Labour and Social Affairs, which administers the German state pension.

The total allotted amount was confirmed by the Bundestag to be €176.8bn. Of that figure, roughly 72 per cent (€126.87bn) is further earmarked for pension insurance and basic security for the elderly, along with those unable to work. The pension insurance allotment stands at €117.24bn, up from €111.87bn in 2023.

Much of the criticism within the German press has revolved around a possible increase in contributions to shore up the country's faltering pension system, a move that many say will disproportionately impact younger generations.

It was a shift signalled on German television by Social Affairs Minister, Hubertus Heil, of the Social Democratic Party (SPD). Heil said that he was looking at whether to include civil servants and the self-employed in the statutory pension insurance scheme. This, along with other measures, was set out in what is known as 'Pension Package II'.

Other ideas put forward, which have since been dismissed, included a raising of the statutory retirement age.

Speaking on the German channel ZDF, Martin Werding, an economist and pensions expert with the German Council of Economic Experts, said that the higher contribution level proposed would benefit only the elderly while taking money directly from the pockets of younger generations.

Werding said: "Part of the intergenerational contract is to make sure that young people are not burdened too much. And the government is not taking this part of the treaty seriously".

Elsewhere, Werding said to the news service *t-online* that the Pension Package II, as proposed by the government, was a disappointment and that the current government was turning a blind eye to the problems currently faced.

Werding said: "It pretends that demographic change has disappeared. The situation may be favourable now because the labour market has developed well. But just because the next jump in the contribution rate has slipped into the next legislative period does not mean that nothing more needs to be done now. The traffic light raises expectations that cannot be kept".

According to the Federal Ministry of Labour and Social Affairs, proceeding without the package would lead to the average pension soon being worth only 48 per cent of the average wage, falling to 45 per cent in the long term.

Also included within the package was a proposal to raise the contribution rate from 18.6 per cent today to 20 per cent in 2028, then to 22.3 per cent from 2035 to 2045.

Despite the recent controversy, the German statutory pension system recently recorded a new high of €1.09bn in voluntary payments in 2022, according to domestic reports.

According to *HasePost*, the sum of voluntary contributions paid into the statutory system rose fivefold between 2017 and 2022, with preliminary figures placing last year's voluntary contributions at €896m. It quoted figures given by German data journalism organisation *Ippen Media*.

However, this shift, since voluntary contributions were first allowed in 2017, is said by some to underline a fear that private pension provision in Germany is not reliable – or, indeed, is untrustworthy.

But despite February's worrying numbers, it appears that German pension spending by the government has remained largely stable since the 1950s. The DRV says that the federal subsidy amounted then to around 27 per cent of the total expenditure of the pension insurance.

It said: "Since the 2000s, the share of federal grants in total expenditure has remained stable between 22 and 24 per cent. It is to be expected that the share of federal subsidies in the total pension insurance budget will remain largely constant in the future."

Norwegian govt vetoes GPFG expansion to unlisted equities

NORWAY'S GOVERNMENT VETOED THE GOVERNMENT PENSION FUND GLOBAL'S PLANS TO INVEST IN UNLISTED EQUITIES

Written by: Natalie Tuck and Jack Gray

Norway's government has vetoed allowing the country's Government Pension Fund Global (GPFG) to invest in unlisted equities, instead saying it wants to "gather more information" on the asset class.

The decision by the government follows a statement released by the fund's asset manager Norges Bank in November, in which its executive board chair, Ida Wolden Bache, said the expansion to include unlisted equities would be a "natural evolution".

Currently, the GPFG can invest in unlisted real estate and unlisted infrastructure for renewable energy, but unlisted equities are not permitted.

However, in its white paper, Norway's Ministry of Finance said unlisted equities would entail investments that have to be managed in a manner that is substantially different from the current investment management.

Therefore, the Ministry of Finance wants to gather more information about both financial and non-financial aspects of unlisted equities. The Ministry intends for a new, external expert council for the fund, as suggested by the Sverdrup-Committee, to be established in 2024. It will be tasked with assessing the different aspects of unlisted equities.

"The government does not wish to open for unlisted equities now. This is an important decision, and we must allow time to consider it carefully. We wish to establish an independent expert council for the GPFG, and with input from this council we will get a better decision basis and broader debate about all aspects of investments in unlisted equities," Norway's Minister of Finance, Trygve Slagsvold Vedum, said.

In addition, the white paper covered the Government Pension Fund Norway's (GPFN) ownership stakes on the Oslo Stock Exchange. GPFN fund manager Folketrygdfondet has highlighted the potential risk of breaching the management mandate's limit of 15 per cent ownership stakes in Norwegian companies.

As a solution, the government is proposing to establish a rule for annual withdrawals from the GPFN, as of the 2025 budget, with annual withdrawals no larger than what is required to handle the ownership stake challenge.

"There is broad consensus in the Storting that the GPFN is a financial investor. The 15 per cent ownership stake limit is important for the perception of the fund as such. The government now solves the ownership stake challenge for the GPFN," Minister Vedum said.

The Minister also praised the strong results of the GPFG and GPFN in 2023, which saw the market value of the GPFN rise above NOK 350bn and the GPFG reached nearly NOK 15,800bn.

This is not the only area of scrutiny the GFPG has faced recently, as a report from the Nordic Centre for Sustainable Finance found that the fund had USD 18.6bn invested in coal at the end of 2023. According to the report, the fund was invested in 97 coal companies at the end of 2023.

The Nordic Centre for Sustainable Finance said that this "undermines" Norway's climate efforts and the USD 1.51bn donated by Norway to climate financing in 2023.

Future of Swedish AP funds up in air as review deadline pushed back

SWEDEN'S FIVE AP FUNDS WERE LEFT IN LIMBO AFTER THE MINISTRY OF FINANCE DELAYED THE FINDINGS OF ITS REVIEW

Written by: Natalie Tuck and Jack Gray

The deadline for the review of Sweden's five AP funds has been pushed back by almost three months, leaving the funds waiting for an answer about their future.

A review of the funds was announced in October 2023 by the Swedish Ministry of Finance, with departmental adviser, Tord Gransbo, leading it. He was tasked with looking at the AP funds' activities, to modernise and streamline the management of the pension funds, with consolidation of the funds being an option on the table.

Initially, the deadline was set for the end of March 2024, but this has been moved to 17 June.

"An investigator will review the administrative provisions that regulate the activities of the AP funds. The aim is to investigate and propose measures to modernise and streamline the overall management of the buffer capital," the Ministry of Finance said in October.

AP6 CEO, Katarina Staaf, previously said the fund has "no views on how the owner chooses to organise the AP fund system". However, she defended the work of AP6, referencing its strong results.

"We expect that whatever the solution is, our solid expertise and successful strategy in private equity will be taken into account. We have generated SEK 58bn in returns for the benefit of the pension system and over the last five years we have an average return of 16.8 per cent annually," Staaf said.

Whilst awaiting the outcome of the review, the first to fourth Swedish AP funds revealed they added SEK 142bn to the value of the Swedish income pension system in 2023, equating to a return of 8.1 per cent (after costs) combined.

In addition, in October 2023, AP3 and AP4 announced they had jointly procured SimCorp to provide a "future proof" end-to-end system solution covering all essential parts of the business, including analysis, order placement, compliance control, administration and portfolio management, risk and return, alternative investments and financial accounting.

Furthermore, AP7 has introduced a new method of regulating its surplus, in collaboration with the Swedish Pensions Agency (SPA).

The collaboration has resulted in a regulatory function that will allow any surpluses to be returned to savers once a year.

AP7 is the default option for savers within the Swedish premium pension system and its management is not designed to generate surplus over time.

To avoid surpluses, the pre-selection option AP7 Såfa has previously opted to lower its fees to combat the pension fund's surplus.

However, it has decided that a level has been reached where fee reduction as a method of managing its surplus was no longer a viable path, as lower fees than the current level would impair the possibility of maintaining a stable and predictable management fee for savers.

Therefore, as the fund's income is expected to be greater than the costs for longer periods of time in the future, it has developed the surplus allocation method with the SPA.

The first surplus distribution of SEK 458m will take place in May 2024.

Finnish pension assets up €13bn as country eyes up pension reforms

FINNISH EARNINGS-RELATED PENSION ASSETS HAVE BEEN ON THE RISE, BUT PRIVATE SECTOR REMAINS UNDERFUNDED

Written by: Jack Gray and Natalie Tuck

Finnish earnings-related pension assets increased by €13bn in 2023, data from the Finnish Pension Alliance (Tela) has shown.

Assets grew by around €7bn in the fourth quarter of 2023, resulting in total assets of €251bn at the end of the year.

Nominal returns on earnings-related pension investments were 6.3 per cent in 2023, while the real yield adjusted for inflation was 2.6 per cent. Over the past 10 years, the total return on earnings-related pension investments in real terms was 3.5 per cent annually.

Tela acknowledged, however, that private sector earnings-related pensions were underfunded, primarily due to falling birth rates.

But this year is also expected to bring discussions on Finnish pension reform, with the goal of strengthening public finances over the long term by 0.4 percentage points of GDP.

And the earnings-related pension sector has considered ways to increase investment returns, with Tela members suggesting that a 'moderate increase' in equity investments in the portfolio would be a positive change.

"A reform aimed at improving earnings-related pension assets' investment yields can close some of that shortfall, but not all of it," noted Tela analyst, Kimmo Koivurinne. "Shares have provided good returns, but their weighting should only be increased moderately, as a change in the interest-rate environment, in particular, means that other asset classes also give reasonable returns. Drastically increasing the proportion of shares would also significantly lower the benefits associated with investment diversification."

And despite these issues, Tela held up the Finnish pension model as one that could be expanded across Europe, as it set out its goal for the upcoming European elections.

In setting out its policy expectations of a new European Commission, Tela argued that more substantial partial funding of pension liabilities, as currently envisaged in the Finnish model, would increase the resilience of pension systems in larger member states, which currently rely entirely on tax and contribution funding.

Furthermore, the alliance said there is still more to be done in supporting member states' own policy choices to meet the ageing challenge.

"Finland will be among the first to age, but we are also prepared for it," Tela stated. "Unfortunately, many large EU countries have not understood the importance of national pre-funding in financing statutory pensions, in practice reducing the tax and contribution burden."

However, Finnish Business and Policy Forum (EVA) consultant, Jussi Pyykkönen, argued that the Finnish government must make "significant adjustments" to pensions and healthcare if it is to succeed in its goal of creating sustainable public finances.

In an article on EVA's website, Pyykkönen said that of the €6bn adjustment planned by Prime Minister, Petteri Orpo's, government, approximately €3bn has been implemented.

Pyykkönen argued that sustainable public finances require €13bn in adjustment measures. This means the next government will have to make savings amounting to €10bn, unless additional decisions are made.

Given this, he argued that pensions must be frozen for the rest of the government's term and then tied to the consumer price index in the future.

Irish govt publishes AE bill; new public body to be established

THE IRISH GOVERNMENT PUBLISHED THE AUTOMATIC ENROLMENT RETIREMENT SAVINGS SYSTEM BILL 2024 IN A 'LANDMARK' MILESTONE FOR THE NEW INITATIVE

Written by: Natalie Tuck

Ireland's government published the Automatic Enrolment Retirement Savings System Bill 2024, following its approval by the cabinet in March.

Approximately 800,000 workers will be enrolled into the retirement savings scheme from January 2025, with a new public body, the National Automatic Enrolment Retirement Savings Authority, established to administer the system.

Commenting on the bill, Minister for Social Protection, Heather Humphreys TD, said: "This represents one of the biggest reforms of the pension system in the history of the state and is an important milestone in supporting people in their retirement years."

At present, around 35 per cent of private sector workers in Ireland have no occupational or private pension, meaning they will be solely reliant on the state pension when they retire. Automatic enrolment will give employees access to a workplace pension retirement scheme co-funded by their employer and the state, covering all employees aged between 23 and 60 years old, who earn over €20,000 per year, and who are not already paying into a scheme.

In practice, for every €3 put in by the employee, the employer will also contribute €3 and the state will contribute €1.

The government also plans to phase in contribution rates gradually over a period of 10 years *[read more on page 18].*

EU injects €4.7m into European pension finding service

THE EU AWARDED THE EUROPEAN TRACKING SERVICE ASSOCIATION A €4.7M GRANT FOR THE NEXT PHASE OF THE PENSIONS TRACKING SERVICE

Written by: Jack Gray

The European Tracking Service (ETS) Association has been awarded a grant of €4.7m from the European Union (EU) for the next phase of the ETS on pensions.

The association obtained the funding following a successful project proposal submitted by the ETS Association in response to a call for proposals launched by the European Commission in 2023.

The association is looking to provide a 'comprehensive' pension overview, allowing people who have worked in different European countries will be able to access their pension entitlements, regardless of the European country they have worked in.

Members of the association are from national tracking services and pension institutions in Belgium, France, Germany, the Netherlands, and Sweden, as well as the European Association of Paritarian Institutions.

The association has also invited other institutions of all pillars and tracking services to participate.

Consortium partners are building on the results of the ETS Pilot Project, which was co-funded by the EU.

Between 2019 and 2022, the findyourpension website for mobile researchers was broadened and relaunched, and the infrastructure for data transmission was developed.

Belgium was the first country to be connected for a transmission of personal pension data to the ETS.

Following this, in the 'rollout phase', further existing national pension tracking systems are to be connected so that individual pension information can be provided "as comprehensively as possible".

Scam concerns grow in Australia

SUPER CONSUMERS AUSTRALIA HAS STRESSED THE NEED FOR A SUPERANNUATION ANTI-SCAM CODE IN AUSTRALIA

Written by: Sophie Smith

The Australian government has been urged to establish a super anti-scam code, amid concerns over recent super fund data breaches and the increasingly sophisticated scams being seen in the market.

Super Consumers Australia urged the Federal Government to prioritise the safety of Australians' 24 million retirement savings accounts by introducing an anti-scam code, arguing that whilst some are taking the risk of super scams and fraud seriously, "this isn't happening across the board".

Highlighting the need for such a code, the group revealed that up to 178,000 superannuation members across three super funds have been placed at a heightened risk of phishing scams since 2022 due to known super fund data breaches.

A phishing scam involves a scammer sending fraudulent emails or text messages designed to steal personal or financial information. Data breaches lead to an increased risk of phishing scams as scammers can use stolen details to target those who have been affected.

"A super anti-scam code would give the industry the clarity and incentives it needs to lift its game on scam prevention," said Super consumers policy manager, Rebekah Sarkoezy.

US DB funding ratios slip

NEW DATA SHARED ON THE LATEST US DB FUNDING LEVELS

Written by: Sophie Smith

US pension funding ratios fell in April, with the average funding ratio estimated to have declined from 108.2 per cent to 107.6 per cent, Legal & General Investment Management (LGIM) America's Pension Solutions Monitor revealed.

The tracker, which estimates the health of a typical US corporate defined benefit pension scheme, showed that equity markets experienced generally weak performance over the month, with both global equities falling 3.2 per cent and the S&P 500 falling 4.1 per cent.

Plan discount rates were also

estimated to have risen by 45 basis points over the month.

It showed that plan assets with a traditional '50/50' asset allocation decreased 4.3 per cent while liabilities decreased 3.8 per cent, resulting in a decrease to funding ratios by April month-end.

News in brief

■ **PensionBee** announced plans to expand into the US DC pensions market after it entered an exclusive, non-binding term sheet with a US-based global financial institution. Through its proposed strategic relationship, the provider would deliver its US service through PensionBee Inc, which is to be established in Delaware as a wholly owned subsidiary of PensionBee Group, with headquarters in New York. The operations of the US business will be managed by PensionBee.

■ The **Arizona State Retirement System** (ASRS) awarded AXA IM Alts a USD 400m (€367m) mandate, leading on its significant risk transfer strategy. The strategy is designed to provide investors with direct access to banks' core performing assets while offering an efficient way to manage their regulatory capital constraints. It marks the latest move in ASRS' strategy to increase its allocation to alternative credit investments.

■ **US institutional investors** are diverging from investors in Europe, Asia and Canada when it comes to ESG investing, Coalition Greenwich has said. Until recently, institutional investors around the world seemed broadly in agreement about ESG. Although they adopted ESG at different paces, most institutions in North America, Europe and Asia appeared to be moving to integrate ESG metrics into their investment processes and portfolios. "While the process of ESG adoption continues in Europe and Asia, institutional investors in the United States are at an inflection point," Coalition Greenwich global head of investment management, Mark Buckley, said.

Diary dates 2024

The latest events occurring across the European pensions market

EUROPEAN PENSIONS AWARDS
4 July 2024
London Marriott Hotel Grosvenor Square
Now in its 17th year, the European Pensions Awards were launched to give recognition to and to honour the investment firms, consultancies and pension providers across Europe that have set the professional standards in order to best serve European pension funds over the past year. The deadline for entries has closed but bookings for the prestigious gala dinner are now open. This year's event will be hosted by comedian Maisie Adam, known for her work on *Mock the Week* and *Have I Got News For You*, among others.
EUROPEANPENSIONS.NET/AWARDS

IRISH PENSIONS AWARDS
20 November 2024
The Round Room at the Mansion House
The 13th Irish Pensions Awards continue to go from strength to strength, aiming to give well-deserved recognition to those pension funds, pension providers, advisers and pension professionals who strive to maintain the highest standards of excellence and professionalism in everything they do, despite the challenging economic and political landscape they find themselves operating in. This year's gala dinner will take place in a new venue after selling out the past two years.
EUROPEANPENSIONS.NET/IRISHAWARDS

EIOPA ANNUAL CONFERENCE 2024
21 November 2024
Scandic Hotel Museumsufer
The European Insurance and Occupational Pension Authority's (EIOPA) Annual Conference brings together policymakers, industry and consumer associations and this year falls at the start of a new policy cycle. The conference will have a particular focus on the key issues that will shape the insurance and pensions supervision agenda over the next five years, including where artificial intelligence will take us, how to close the pensions and savings gap. This in-person event will conclude with a network drinks reception.
EIOPA.EUROPA.EU/MEDIA/EVENTS

Not to miss...

IAPF AUTUMN CONFERENCE 2024
3 October 2024
CCD, Dublin
iapf.ie/event

PLSA ANNUAL CONFERENCE
15-17 October 2024
ACC, Liverpool
plsa.co.uk/Events

CBBA-EUROPE ANNUAL CONFERENCE
8 October 2024
NH Brussels EU Berlaymont
cbba-europe.eu/eventlist

AEIP ANNUAL CONFERENCE 2024
14 November 2024
Brussels (TBC)
aeip.net/events

Appointments

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@perspectivepublishing.com

MARIA HUMLA

The Swedish government has extended the term of office for Maria Humla, director general of the country's National Occupational Pensions Board (SVP). Humla has been director-general since 2018 and her extended appointment will last three years and is valid until 31 July 2027. Humla said she was "pleased and honoured" to be "entrusted with the opportunity".

MARC NOEL

Amundi has appointed Marc Noel as its chief compliance officer. Noel, who joined Amundi in 2022 as deputy general counsel, oversaw the group's products and market derivative contracts. He started his career in 2002 at Societe Generale as legal adviser in charge of international litigation and then joined the investment banking division of the French Bank Federation in 2005. In 2007, he returned to Societe Generale's Group.

EELKE VISSCHER

The Dutch Pension Federation has appointed Eelke Visscher as director of operations, effective from 13 May 2024. He will form the management team together with general director, Edith Maat. Visscher's areas of focus will be on the further development of the organisation, internal operations, finance and association management; from there he will contribute to the Pension Federation's multi-year work agenda and programmatic tasks.

ALVARO SANTOS PEREIRA

Alvaro Santos Pereira has been appointed as the next chief economist of the OECD, starting on 1 June 2024. Santos Pereira is a leading economist who served as Portugal's Minister for Economy and Employment from 2011-2013, with responsibility for the areas of industry, commerce and services, tourism, energy and public works, transportation, and employment. He was first appointed as the director of country studies on 1 March 2014.

MIRIAM UEBEL

Legal & General Investment Management (LGIM) has appointed Miriam Uebel as deputy head of Europe, institutional. In this newly created role, Uebel will collaborate with the existing team to further expand LGIM's institutional footprint, focus on business development, as well as L&G's private markets offering. She will promote LGIM's investment expertise to help the business grow in strategically important markets.

ALAA BUSHEHRI

BNP Paribas Asset Management (BNPP AM) has appointed Alaa Bushehri as head of emerging markets debt (EMD). Based in London, Bushehri will report to Olivier de Larouzière, CIO fixed income. Bushehri has been with the BNP Paribas Group for 20 years. For the past 11 years, she has been the head of emerging markets corporates within the emerging markets debt team. She joined FFTW in London as a portfolio analyst in 2007, from CIB in Bahrain.

PER LINDGREN

Swedish pension company Skandia has appointed Per Lindgren as the new head of its asset management division, effective from 1 June, replacing Lars-Göran Orrevall when he retires. Lindgren was previously the group manager for asset management at Skandia and has a long history in the Skandia group. Skandia president and CEO, Frans Lindelöw, said: "I am very pleased that Per has chosen to take on the role as head of asset management."

KARIN CEDERBAUM

Alecta has appointed Karin Cederbaum as its new general counsel and head of the legal department. She joins from Säkra Spar where she was CEO and has previously worked as general counsel for the insurance business area at Skandia Liv and as head of compliance at Swedbank. Cederbaum will take up the position at Alecta in October 2024, at the latest.

ÅSA MOSSBERG

The second Swedish Public Pension Fund (AP2) has appointed Åsa Mossberg as the new head of communication and sustainability and will be part of the fund management. Mossberg has been the chairperson of the AP Funds' Council on Ethics since 2021. She joined AP2 in 2018 as a sustainability analyst, before becoming a senior sustainability strategist in September 2020.

JONATAN HOLST

Swedish pension company AMF has appointed Jonatan Holst as its new head of communications where he will report to AMF chief of staff and deputy CEO, Malin Omberg. Holst previously worked for the Swedish Financial Supervisory Authority, where his responsibilities were internal and external communication, and he also previously worked in government offices. Holst said he is "happy and proud" to be working at AMF.

INGVILD GRÅBERG

Oslo Pensjonsforsikring has appointed Ingvild Gråberg as its new HR manager. Gråberg joins from the health section at Avonova Helse AS where she was also HR manager. Previously, she has worked at, among others, Storebrand Livsforsikring, Crawford & Company and Insr Insurance Group. She has a degree in economics from BI School of Business and has many years of management experience.

COUNTRY SPOTLIGHT | IRELAND

Beginner's luck?

Legislation to introduce automatic enrolment in Ireland was recently passed by the Irish cabinet but much work still remains to be done, and the success of the initiative is yet to be seen. Sophie Smith **reports**

10 years since the OECD identified auto-enrolment (AE) as a key pensions reform that the country should implement, Ireland is edging closer and closer to finally introducing this crucial initiative, and leaving behind its title as the only OECD country that doesn't yet operate an AE or similar system as a means of promoting pension savings.

The latest milestone in this journey was seen in April, when the Irish government published the AE Retirement Savings System Bill 2024, which Department of Social Protection assistant secretary general, Tim Duggan, suggested could change the face of the Irish pensions landscape forever.

"The bill is a testimony to the fact that the government of today is still totally committed, the fact that they have approved this bill and are sponsoring it through the house, that's a huge thing for civil servants," Duggan said at the recent Irish Association of Pension Funds (IAPF) Summer Conference.

However, Duggan clarified that "publishing the bill is one thing, but more important than that is getting it debated and passed and then enacted", as both the committee stage and the fourth and final stage in the Dáil remain.

And whilst Duggan said that the Irish government is hoping to get through these final stages "relatively quickly and hopefully before the end of the month [*May*]", he admitted that may or may not be possible depending on the level of engagement there is at committee and the type of amendments that are proposed and how they can or can't be done.

The industry has welcomed this recent progress, with Irish Institute for Pensions Management (IIPM) president, Davin Spollen, suggesting there seems to be a genuine momentum and appetite to have this new mandatory system in operation in 2025, with cross-party support on this goal.

An ambitious timeline

But even if legislation remains on track, Spollen warns that the January 2025 implementation by any organisation's standards, for a completely new approach to mandatory retirement planning, requiring third-party contracts and bespoke systems, would be "highly challenging".

These concerns are shared by LCP Ireland senior pensions consultant, Kathy Keating, who says that "even the extended date of January 2025 is considered ambitious", whilst Mercer Ireland DC and private wealth leader, Caitriona MacGuinness, says that there remains a lot more work for government to complete before the system can be launched.

Building the right framework

And despite recent progress, IAPF CEO and PensionsEurope chair, Jerry Moriarty, believes the 1 January 2025 implementation date "still seems like an ambitious timeline as the administrator of the system has still to be appointed".

"They then have to build a new system that will administer 800,000 employees," he continues, pointing out that legislation is being debated at the moment, while the whole infrastructure of the National Automatic Enrolment Retirement Savings Association (NAERSA) still needs to be put in place.

Speaking at the IAPF's conference, Duggan admitted that this has been "an incredibly difficult piece of work due to the volume and complexity in the information bid".

However, he confirmed that the department is working on the final fitters, with hopes to conclude the procurement for both the administration and investment management services by the end of Q3.

Whether these deadlines will be met is yet to be seen though, as Moriarty points out that the tender for investment managers hasn't even been issued yet.

And broader operational concerns have been raised, as MacGuinness says that whilst the government emphasised "simplicity" as a key feature of its centralised approach, that does not tell the whole story.

One particular teething issue facing those employers who have their own pension plan and who wish to avoid using the central system is that they may be legally restricted from automatically enrolling their employees directly into their own plan. MacGuinness says will place even more importance on the role of employers when it comes to the employee engagement process and ensuring that employees understand the options on offer.

Getting the message out

But this is just the tip of the communication iceberg, as MacGuinness says delivering key messages about the new regime could prove challenging, "especially because it will essentially be mandatory for employees to save for retirement (unless they actively opt out)". "For many, the concepts involved in pension saving will be very new, not to mention the financial implications of related salary deductions," she says.

Communications work is already underway though, as Duggan recently confirmed that Ireland's DSP is undertaking a three-phase communications strategy to launch the AE retirement savings system in the country.

In the meantime, however, there is still a great deal of doubt, as Keating stressed that legislation is still subject to change and there is a great deal of uncertainty on how it will work and be implemented in practice.

"Pension experts are struggling to provide clear advice to employers amidst this uncertainty," she says, "and in turn employers are struggling to prepare for the imminent

"PENSION EXPERTS ARE STRUGGLING TO PROVIDE CLEAR ADVICE TO EMPLOYERS AMIDST THIS UNCERTAINTY"

launch date while ensuring adequate resources and upskilling initiatives are in place."

"FOR MANY THE CONCEPTS INVOLVED IN PENSION SAVING WILL BE VERY NEW, NOT TO MENTION THE FINANCIAL IMPLICATIONS OF SALARY DEDUCTIONS"

Change in a shrinking market

The introduction of AE also comes at a time of existing change for the Irish pensions market, with Ireland's Pensions Regulator, Brendan Kennedy, recently revealing that around 35,000 pension schemes have wound up since the start of 2023.

Whilst consolidation is being driven primarily by the introduction of IORP II legislation and the increase in associated regulatory costs, Keating says the pace of consolidation in the Irish market is likely to continue with the introduction of AE.

Despite the significant growth in the master trust market in Ireland, a recent report from PwC stressed that this growth is "clearly finite", with auto-enrolment set to take around 770,000 participants out of scope.

Moriarty, however, says that AE is "somewhat separate" as the focus is on employers that don't currently offer pensions to their employees, arguing that "existing schemes will always be better than AE" given the relatively low contributions being phased in. The Irish government has also stressed this point, reassuring industry that it has "no intention of undermining occupational schemes".

Speaking at the IAPF conference, Duggan said he has seen no evidence that AE causes damage to occupational schemes, clarifying that, "if anything, it seems to enhance them because for that very reason, people become more aware of them and more willing to engage with them and employers can push them a bit more".

But fellow speaker, Irish Life director of corporate partnerships, Shane O'Farrell, was unconvinced and said he was "concerned".

He also argued that these dilemmas are the government's own making, saying that "it is very busy, it is very intense, but to some extent, they have chosen the most difficult and complicated way to achieve this".

This could risk exacerbating recent capacity constraints, as Spollen points out that Ireland is at full meaningful employment, leaving all businesses resource challenged. "As many of us in the private sector have been looking forward to a reduction in the volume of work, which came in as a result of IORP II, it now appears that any such reduction may be short lived, as we now begin to plan around the significant consultation work that will need to be carried out to address employer and employee needs around understanding the AE system and their strategic/benefits approach to their own pension schemes," he adds.

A window of opportunity?

Whilst much of the recent attention in Ireland has focused on DC offerings amid the launch of auto-enrolment, Irish DB pension schemes have also seen continued improvements in their funding levels, with de-risking volumes set to pass €1 billion in 2024.

LCP Ireland investment and pensions de-risking specialist, Aaron Kilboy, notes that whilst DB plans have faced their share of challenges over the past decade, more recently, higher interest rates reduced liability values, resulting in better funding levels for most plans.

"Coupled with a new era of compliance and governance, this makes it an opportune time to step back and examine what the future holds," Kilboy continues, pointing out that many DB schemes are adopting 'insurer-like' investment strategies and can therefore "run-off" liabilities with a high-degree of confidence, while retaining the flexibility of the trust structure and the benefits that brings to members.

However, Kilboy acknowledges that, how competitive dynamics evolve within the insurance market remains to be seen, which will impact capacity, product range and pricing.

For the time being at least, only the immediate annuity market in Ireland is well developed, and Kilboy clarifies that while a deferred annuity market in Ireland may emerge, it isn't readily available yet.

IIPM president, David Spollen, also acknowledges that the pace of bulk annuity transactions so far in 2024 has been slower than expected, with less than €100 million in total volume anticipated in the first half of the year. However, he notes that further activity is expected in the latter half of 2024, when trustee time frees up following the April IORP II compliance deadline.

But Kilboy admits that while progress has been made to date and all major providers have indicated their willingness and commitment to offering such solutions in the future, there has not been significant non-pensioner transaction activity and a competitive market is unlikely in the near term.

IRELAND'S PENSIONS REGULATOR

Changes and priorities

Pensions Regulator, Brendan Kennedy, **reflects on the consolidation trend in the Irish pensions market, and the work still needed to ensure the best outcomes for savers**

Irish occupational pensions have been undergoing significant change since 2021. It is now becoming possible to see what future Irish pensions will look like and for the Irish pensions regulator to implement its priorities.

An unusual feature of Irish pensions has been the large number of pension schemes – at the beginning of 2023 there were approximately 160,000 defined contribution (DC) schemes and about 500 defined benefit (DB) schemes. These are large numbers by any standards, but particularly for a country with a working population of about 2.7 million. Almost all of these schemes are single employer schemes and about 150,000 of these schemes have a single member.

In 2021, Irish pensions legislation was amended to implement the EU IORP II Directive. The effect of this was to impose higher standards of governance and compliance on Irish schemes, to require the appointment of key function holders in each scheme and to set minimum standards of qualification and experience for the boards of trustees. When transposing the directive, the Irish government decided against any derogations for smaller pension schemes: The smallest schemes would be obliged to meet the same standards of governance and compliance as other schemes, though it did give single member schemes, established before April 2021, an additional five years before having to comply with the new requirements.

In response, the great majority of schemes and their sponsoring employers have decided that it is impractical and/or uneconomic to meet the obligations of the revised legislation. In most cases, existing assets and future contributions are being transferred into master trusts, others are being transferred into personal retirement savings accounts (PRSAs) – a contract-based retirement savings vehicle.

The result has been a considerable amount of consolidation-related activity in the Irish pensions sector in the last two years. There are now 17 DC master trusts operating, and aggregate inflows to these have been averaging over €1 billion per month. For multi-member schemes and newer single member schemes, this consolidation process is expected to be substantially completed in the coming months. Single member schemes, established before April 2021, have until April 2026 to become compliant with the new requirements. However, even for these schemes, tens of thousands have been wound up and transferred.

It is too early to say what the final number of Irish pension schemes will be, but it is clear that by 2026 there will have been very substantial consolidation, which will provide the opportunity for much increased efficiency in the administration and management of pension schemes.

The Pensions Authority is the body responsible for the supervision of Irish pensions. A much smaller number of pensions schemes provides the authority with the opportunity to increase its engagement with each pension scheme, and to implement a supervisory process based on dialogue with the trustees.

The best outcomes for the members and beneficiaries of pension schemes depend on the culture and attitude of the boards of trustees. The Pensions Authority is very aware of the importance of these factors, and monitoring of board culture will be central to its work.

Given the complexity and dynamism of the environment in which trustees look after their members' retirement savings, trustees cannot expect to operate on the basis of a detailed to do list provided by the regulator. Trustees need to take responsibility for the management of their scheme, and to ensure they are informed and active. Engagement between trustees and the authority can serve as a useful check for both in working towards the common objective of good member outcomes.

The change in Irish pensions is not yet complete, but the features of the new landscape are becoming clearer. However, there is still a lot to be done.

PENSIÓN RESEARCH & CONSULTING

The power of behavioural tech

Pensión Research & Consulting founder and managing director, Dr Seda Peksevim**, explains how behavioural and technological developments have the potential to expand pension coverage**

Most European countries adopt traditional policy tools, such as tax incentives, employer matching contributions, and state subsidies, to encourage pension savings. While these policies can promote pension savings to some extent, behavioural and technological developments have significant potential to expand pension coverage and contributions among low-income individuals, self-employed people, and women. In this context, the following suggestions, in terms of behavioural and technological aspects, can be considered for encouraging pension savings in European countries.

Digital nudging tools

By incorporating behavioural economics insights into technology, digital nudges can promote pension savings. The most recently introduced digital nudges include round-up apps, gamification tools, and saving-through consumption platforms. While round-up apps round up an individual's daily purchases and invest the spare amount into their savings accounts, gamification tools integrate gaming elements, such as increased challenges, reward systems, and penalties, into real-world practices to promote pension savings.

One of the most important digital nudging tools in this category includes saving through consumption platforms. Although their details vary, these platforms work in the following way: When someone purchases an item (food, clothing, or a cinema ticket) from a selected retailer, a certain portion of their payment is transferred automatically to their pension account. In other words, these tools automatically transform spending behaviour into saving habits.

Among the applications in this category, Mexico's low-cost platform called Miles for Retirement encourages pension savings, particularly among low-income and self-employed individuals. 'Miles for Retirement' is an app that connects to every user's credit or debit card. After it's set up, the app is on autopilot and transfers savings into individuals' retirement accounts every time they shop. Similarly, a Spanish start-up developed a mobile application called Pensumo, which allows its members to increase their savings by engaging in socially responsible activities (recycling and road safety initiatives), in addition to saving through consumption. Another example is the SuperSuper platform, which aims to reduce the gender gap in retirement income and increase pension savings among Australian women. Recently, China also introduced a saving through consumption platform called Panchumo.

Fintech applications

Fintech tools can lead to the development of digital micro-pensions. As a long-term product of the microfinance industry, micro-pensions allow their members to make small contributions at irregular intervals. These arrangements are ideal for emerging European countries, where low-income and informal sector workers occupying a significant share of their labour force.

Various applications of micro-pensions are available in some African countries (Kenya, South Africa, and Uganda) and Asian countries (Bangladesh and India) but they remain limited and require further technological development. Fintech tools can provide digital application, payment, and distribution services to micro-pension participants at a low cost; for example, an important provider of digital micro-pensions is a global social enterprise called pinBox Solutions that aims to expand micro-pension inclusion to 100 million individuals across Asia, Africa, and Latin America.

Written by Pensión Research & Consulting founder and managing director, Dr Seda Peksevim

GUIDE

Real assets guide: A changing world

Tangible benefits

Appetite for real assets is growing among pension funds, but what makes this an appealing area, and how can investors access them? Sandra Haurant takes a look at the world of real assets

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The evolving world of real assets

BNP Paribas Asset Management head of real assets, Karen Azoulay, discusses what this dynamic asset class can offer European pension fund investors, and explains how the firm is staying ahead of the game

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Private markets: The four key megatrends

The plates under the global economy are shifting, explains LGIM global head of investment strategy & research, real assets, Rob Martin

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In association with

OVERVIEW

Tangible benefits

Appetite for real assets is growing among pension funds, but what makes this an appealing area, and how can investors access them? Sandra Haurant **takes a look at the world of real assets**

As asset classes go, real assets are a broad church, encompassing the likes of infrastructure and real estate, structures producing renewable energy, such as wind and solar farms, forestry and agriculture. Put simply, real assets are things that you can touch.

For pensions, real assets tick a number of useful boxes and, according to the *Real Assets Study 2024* research paper published by Aviva Investors, 69 per cent of corporate defined contribution (DC) pension funds expect to increase allocations to real assets over the next two years, up from 51 per cent a year earlier.

So what makes this collection of assets so appealing? BNP Paribas Asset Management head of real assets, Karen Azoulay, says: "Real assets provide stable and regular cash-flows – income streams for investors/pension funds; cash-flow funds, with a cash-yielding type of strategy on a long-term basis, fit well with pension fund constraints in terms of retirement pay-outs."

Then there is the diversification question. Aviva's research showed that 64 per cent of global institutional investors cited diversification as a primary reason for allocating to real assets today, up from 57 per cent in 2022. "This asset class is also usually considered as a diversifying asset class," Azoulay says. "It offers diversification, either from fixed income for the investment grade type of strategies, or from alternative asset classes and equities."

In the past, pension portfolios would primarily hold equities and bonds, and property provided diversification. Today, the scope of assets held within a portfolio is greater, but diversification is still vital. WTW head of EMEA real estate, Douglas Crawshaw, who works within the real assets team, says: "The reason one invests in diversifying strategies is to diversify away from equity and credit volatility and risks, and because of the nature of what was once just real estate, but is now real assets, they dampen down volatility and therefore act as a diversifier from a from a volatility perspective."

A stabilising influence

In recent years, the resilience of real assets has certainly been tested, says Azoulay: "We've been through several situations during recent years – high inflation, the Ukraine war, and the energy crisis, for example, but our portfolios remain very resilient," she says. "Revenues are inflation-linked. They are mostly de-correlated from traditional credit asset classes or economic cycles. So, from a macro perspective, the fundamentals are very good for the asset class, and fit well with pension funds' investment constraints."

And the variety within the asset class means subsections can provide different benefits. Take infrastructure, for example. Russell Investments head of strategic client solutions, David Rae, says: "Infrastructure comprises the essential assets which underpin modern economic life, and their long-term nature is a natural fit for

many pension funds," he says.

"The recent experience of the pandemic volatility, highest-in-a-generation inflation and rising interest rates have proven the key portfolio benefits of the asset class, which for a long time were only theoretical; return outperformance in times of inflation and low correlation with other assets," says Rae. "At the same time, the investible universe of infrastructure has grown beyond just transportation and utilities, as more services have become essential to modern economic life – from digital communication to the energy transition to sustainable public facilities."

And when it comes to real estate, says Crawshaw, the long-term view of most pensions means they can, and do, ride out the market's cycles. "You own the building or the land, and, with some notable exceptions, nobody can take it away from you. If the market collapses, you've still got the building or the land," he says.

Premium service

The ability to take a longer-term view is, of course, essential with assets that cannot be sold instantly. "Real assets are an illiquid asset class," says Crawshaw. "I don't mean you can't sell them, but it takes time… and therefore you get an illiquidity premium,… an enhanced return, to compensate for the fact that you can't have your money back immediately."

Of course, time horizons vary depending on the life stage of a scheme, and so does the ability to absorb illiquidity; DC and defined benefits (DB) naturally have different requirements. "Infrastructure is an ideal asset class for investors with longer investment horizons looking for growth, inflation protection and the potential for a contractual income stream. Those characteristics make it a highly relevant investment for active members of DC schemes who can tolerate the illiquidity associated with this asset class," Rae says. "In contrast, many corporate DB schemes are looking to increase liquidity given their demographic circumstances and the need to rebalance portfolios."

Sturdy sustainability

ESG strategies form a crucial element of the decision-making process today; according to Aviva's research, fewer than 5 per cent of global respondents did not consider sustainability when making investment decisions, and 57 per cent of institutional investors have a commitment to net zero. But almost three quarters of institutions (73 per cent) said they wanted to prioritise financial returns when investing in sustainable real assets.

> **"YOU OWN THE BUILDING OR THE LAND, AND, WITH SOME NOTABLE EXCEPTIONS, NOBODY CAN TAKE IT AWAY FROM YOU. IF THE MARKET COLLAPSES, YOU'VE STILL GOT THE BUILDING OR THE LAND"**

Crawshaw cautions strongly against implementing ESG strategies "for the sake of it". Pensions, after all, have specific responsibilities. "First and foremost, we have a responsibility to act in the best interest of our investors to give them the best risk-adjusted return; you [*implement ESG strategies]* to get the best risk-adjusted return," says Crawshaw.

And there is plenty of scope within real assets to do just that, says Rae, who adds: "Although [*infrastructure*] has a unique combination of exposures to climate risk (E), political sensitivity (S) and security needs (G), all of which must be mitigated proactively, infrastructure also offers tangible social and environmental benefits, even when investing solely on a return-focused basis." As a result, investors get the benefits of the asset class, while communities on the receiving end of services get the benefits of "decarbonisation, equitable internet access, essential government services, reliable utilities and safe transportation," he says.

A solid future?

Encouraging pension fund investment in the UK is a stated aim of the current chancellor, Jeremy Hunt, whose Mansion House speech called for investment into high-growth UK companies. But, Rae says that the reforms have been "interpreted more broadly to apply to private investments across a range of financial and real assets. Coupled with reform to available products, innovation and increased demand from savers, we're witnessing a change to the way infrastructure investments are made".

Aviva Investors chief investment officer, Daniel McHugh, commented on the firm's research, saying: "The findings from this year's study capture one of the most pertinent structural shifts taking place in real assets investment and retirement saving. DC pension funds represent an increasingly large portion of the pension market, yet this important group of investors have not been able to access – or allocate to – real assets as they would like, or to the extent that optimises investment outcomes." While the nature of this global asset class has made it difficult to access historically, new products – including the Long Term Asset Fund (LTAF) – may begin to lower barriers and drive up demand for those all-important assets you can touch.

BNP PARIBAS ASSET MANAGEMENT

The evolving world of real assets

BNP Paribas Asset Management head of real assets, Karen Azoulay, **discusses what this dynamic asset class can offer European pension fund investors, and explains how the firm is staying ahead of the game at a time of dramatic evolution**

Private markets investing is at the forefront for investors. When it comes to real assets, what are the main reasons for pension funds to look at this asset class?

■ **Azoulay:** We have been in this area of the market for a long time and what we are seeing is that pension funds are considering investment in private markets, and in particular in real assets, firstly because they offer an attractive risk/return profile. So, the absolute yield and relative value is interesting, and that's even more the case given the current interest rate conditions.

At the same time, real assets provide stable and regular cash-flows – so, income streams for investors/pension funds. Cash-flow funds, with a cash-yielding type of strategy on a long-term basis, fit well with pension fund constraints in terms of retirement payouts.

This asset class also offers diversification.

Why do we have these long-term stable cash-flows? Firstly, because we have inflation protection. We've been through several situations in recent years – high inflation, the Ukraine war, and the energy crisis, for example, but our portfolios remain very resilient. Revenues are inflation-linked. They are mostly de-correlated from traditional credit asset classes or economic cycles. So, from a macro perspective, the fundamentals are very good for the asset class, and fit well with pension funds' investment constraints.

Can you tell us about your real assets platform

■ **Azoulay:** Thinking about the investment philosophy behind the platform, I would highlight several key differentiating factors – firstly that we are part of a larger private assets platform. So, we have dedicated people to support our strategies. We have legal, risk, tax, ESG, and so on – that's very important.

What's even more important is that, as the asset class is quite illiquid, it's essential to have strong origination capability within the team. We actually have team members from many different backgrounds – from banks, from the industry, from the equity side, and so on – which lends itself to a very strong origination network, and that network is complemented by a privileged access to the origination capacity of BNP Paribas as a group.

The last point I would highlight is the very strong and thorough ESG process that has been, from the beginning, fully embedded into our investment process, thanks to our internal sustainability centre.

How is the platform evolving?

■ **Azoulay:** We are seeing a trend towards energy transition, as well as digital infra.

On energy transition, we used to finance straightforward renewable assets, and we are now seeing renewable assets benefiting less and less from feed-in tariffs/regulated tariffs. So, more and more merchant risk as they are now reaching what we call risk parity. This means they

do not really need any subsidised tariffs. They are competitive now. As a result, there's been a very strong move into the renewable space. So, it is very important to have the capacity to analyse those transactions.

At the same time, we are seeing new themes emerging around energy transition. For example, hydrogen, battery storage, and bio-gas. We are also seeing interesting opportunities around green mobility – rail electrification across Europe, and electric vehicles charging platforms, for instance. So, there are a lot of exciting new themes in that market.

The fact that we have been very active in energy transition since the early days, combined with the access we have to the wider group, puts us in a strong position, because we have access to industrial experts dedicated to each sector. When we decide to invest in a new sector, we have access to industry experts that are able to provide us with insight, even local market insight, through the teams all over Europe.

It is very important to have access to this local market knowledge before investing in those sectors. And when we invest ahead of market trends, that is when we pick the best assets.

Digital infra is another key area we are focusing on. That means fibre optic networks. There were plans all over Europe to bring high speed internet access to less dense areas. But that's done now, more or less. We are now seeing the refinancing of those transactions.

We've also been very active in green data centres, which are very efficient in terms of energy consumption.

Additionally, we have been active in digital towers. There has been a lot of M&A and refinancing in this field. But we have seen, despite the number of transactions, and despite the interest rate movement and all that has happened recently, those transactions have been quite resilient, and we continue to see a fair amount of transactions in that field. So, being recognised as one of the main players here is important, both for senior and junior debt.

How can pension investors play a role in financing secure and sustainable assets?

■ **Azoulay:** In the beginning, infrastructure investing was all about financing large and tangible assets that benefited from a regulated tariff or a contractual framework, relying on a public entity.

But since then, the market has evolved, because governments have less money to spend on infrastructure. So, the objective is to leverage public money, to attract private money, to use it more efficiently; and pension funds can play a key role here, investing in sustainable assets, not just so they can tick the sustainability box, but because sustainability is very much linked to the long-term performance of those assets.

It is interesting to see that there has been a change in mindset in this area among pension funds – they now understand that connection.

For example, we have launched SFDR 9 funds, and we are keeping the same target returns – so investing sustainably does not mean it is going to be detrimental to the return. Some might argue that assets are more difficult to deploy if you have strong ESG policies and constraints, but that's not the case at all.

BNP Paribas recently launched the Climate Impact Infrastructure Debt fund – what are some of the projects the fund has invested in?

■ **Azoulay:** We are focusing on several sectors, such as renewable energy, green mobility, and circular economy, as well as new energy transition-related sectors such as battery storage, hydrogen, and carbon captures. One may think that if you invest in SFDR 9, then you will only invest in renewable energy, and that's not the case at all. We can invest across different sectors. We keep that diversification as a key feature.

What are some common strategies for mitigating risk when investing in these assets?

■ **Azoulay:** The first is diversification. That's why we are not launching any thematic funds. We are focusing on funds with sectors or geographic diversification so that we don't rely on a specific regulatory framework or on a specific country situation. You want to be diversified – different jurisdictions, different market features. That's important; and having the ability to proceed with our own due diligence process, and being totally ambulant in terms of investment decisions, is key.

There's also a strong need now to have specialised skills in order to be able to analyse and invest in these new sectors. Before now, the asset class had not really evolved much in terms of sectors – we were financing transportation: Motorways, airports, ports and so on. But this has completely shifted to a new type of asset that needs very specific skills to be able to invest, because investing in hydrogen, in battery storage, in bio-gas, it's completely different. Even for the more straightforward sectors such as renewable energy, things have completely evolved.

That is why it is important now more than ever to have the internal capacity to analyse those sectors and, being part of a larger group which is at the forefront of those sectors, is a true differentiating factor for us.

BNP PARIBAS
ASSET MANAGEMENT

LGIM

Private markets: The four key megatrends

The plates under the global economy are shifting

BY **ROB MARTIN**

Rob Martin
Global Head of Investment Strategy & Research, Real Assets

Rob is Global Head of Investment Strategy and Research for Real Assets, having joined LGP in October 2006. Prior to this, he worked for Hammerson as Head of Research, working closely with the board and senior management team on corporate, sector and asset strategies. Prior to Hammerson, Rob was at CBI for two years as a senior economist, and prior to that, he spent three years in the petroleum industry. Rob has a degree in economics and economic history.

Advances in technology, changes in population structures, geopolitical pressures and the drive toward decarbonisation are catalysing the development of new industries and rendering some assets and investment behaviours obsolete.

We believe there are four core megatrends that will influence the investment environment over the short, medium and long term: **demographics, decarbonisation, digitalisation** and **deglobalisation**.

We expect these megatrends to be significant determinants of long-term investment performance and capital allocations in real assets for the remainder of this decade – and beyond.

1) Demographics

To an extent, demography is economic destiny.

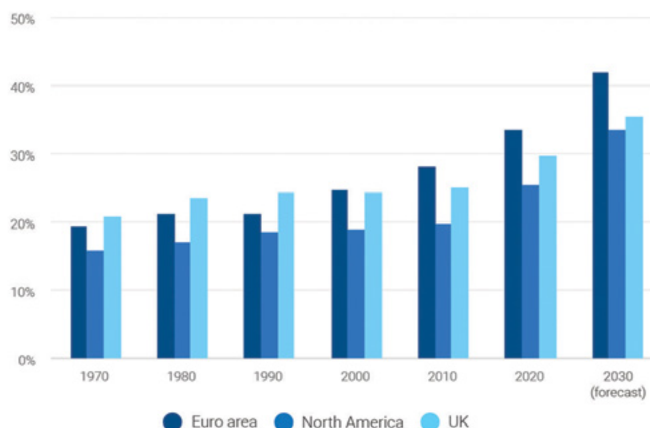
Tailwinds deriving from the post-war baby boom played an important role in many major economies' development in the decades after the 1950s. Alongside a growing and healthier workforce, improving life expectancy and increasing urbanisation contributed to a period of reasonable economic growth, improving living conditions and rising disposable incomes.

In most developed economies, this **demographic** tide is now receding. Many face the dual challenges of shrinking labour forces and increasingly elderly populations. Declining fertility rates and ongoing political sensitivities around immigration mean these issues are likely to become entrenched. In the absence of the natural boost delivered by a young, growing population, these economies will need to increase their productivity to maintain living standards.

This should in turn require greater adoption of technologies like robotics and AI, which can take the place of a shrinking workforce.

We think these trends will create

Age dependency: Ratio of working age population to over 65s



increased investment opportunities in emerging markets that display growing labour forces and favourable demographic characteristics. Weak fertility rates in both high income countries and China mean their share of the global population is expected to fall from 15.7% and 17.8% respectively in 2022, to 12.6% and 12.0% in 2060[1].

Meanwhile, sub-Saharan Africa's share of the global population is forecast to balloon from 14.6% in 2022 to 24.4% in 2060, with India and Southeast Asia's proportion remaining relatively stable over this period[2].

In developed markets with ageing populations (and shrinking workforces) we are already seeing increasing physical and capital requirements for healthcare facilities and technologies, and a need for more specialist accommodation for elderly communities.

From a lifestyle perspective, we expect a growing emphasis on wellbeing and leisure, which should stimulate associated industries.

2) Decarbonisation

There is a growing consensus among policymakers of the urgent need to debarbonise the global economy.

According to the Intergovernmental Panel on Climate Change (IPCC), the world must reach net-zero emissions by 2050 if we are to limit global average temperature increases to 1.5oC above pre-industrial levels.

This is the threshold outlined in the 2015 Paris Agreement and committed to by almost every country in the world.

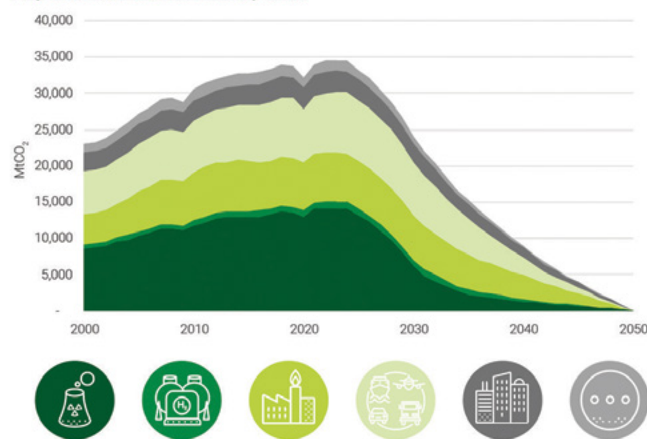
However, progress in **decarbonisation** has been patchy and global greenhouse gas (GHG) emissions are yet to meaningfully decline. One of the key challenges impeding progress is decoupling emissions from economic growth in emerging nations, where rapid increases in population and GDP have in recent decades been correlated with large expansions in GHGs released.

That said, **decarbonisation** has received significant policy focus in the EU and US, with considerable subsidies now introduced in support of constructing the infrastructure required for achieving net-zero carbon emissions. This is resulting in increased electrification as transport, home heating and certain industrial processes substitute burning fossil fuels for electricity.

Simultaneous **decarbonisation** efforts in the power sector have accelerated the buildout of renewable energy capacity, mainly in solar and wind farms. Increased deployment of renewables is placing pressure on power networks and demanding increased battery storage to deal with the intermittency of wind and solar output; addressing both challenges will require significant investment. However, constraints in technology and remaining carbon budgets will likely lead to build-out of carbon capture and storage assets in certain sectors such as cement and power generation. This is likely to contribute to a greater focus on nature-based climate solutions that can assist in offsetting the impacts of hard-to-abate emissions.

However, constraints in technology and remaining carbon budgets will likely lead to build-out of carbon capture and storage assets in certain sectors such as cement and power generation. This is likely to contribute to a greater focus on nature-based climate solutions that can assist in offsetting the impacts of hard-to-abate emissions.

Projected direct CO2 emissions by sector



Source: BloombergNEF as at 20 November 2023.
Assumptions, opinions and estimates are provided for illustrative purposes only. There is no guarantee that any forecasts made will come to pass.

3) Digitalisation

The digital revolution is set only to gather pace.

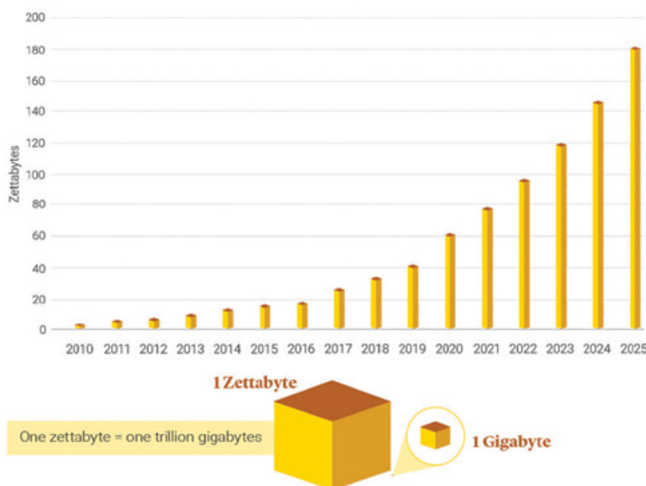
We define 'digitalisation' as the integration of new digital technologies into existing business processes[3].

These technologies have already radically altered business practices across many industries; the pace of development in big data, AI and machine learning is only likely to accelerate, with the scope of their impacts set to grow in parallel.

The growth of robotics, automation and AI-assisted design is likely to facilitate the modernisation of a range of industries and ultimately deliver broad-ranging efficiency savings.

[1] Source: UN, 2022 Revision of World Population Prospects, https://population.un.org/wpp/
[2] Source: UN, 2022 Revision of World Population Prospects, https://population.un.org/wpp/
[3] By contrast, we define 'digitisation' as the conversion of information and documents from analogue to digital formats.

Data generated annually



Source: Statista, Bernard Marr & Co.
Assumptions, opinions and estimates are provided for illustrative purposes only. There is no guarantee that any forecasts made will come to pass.

At the same time, the enormous computational demands of generative AI alone are likely to support long-term demand for associated services like data storage, cyber-security, connectivity networks and hardware components. This should have follow-on impacts for materials, labour and real estate.

Digitalisation is also likely to reshape the global labour force, with some jobs being replaced, and others requiring new skillsets to develop and deploy emerging technologies. As with **demographics**, this should create opportunities in further education and vocational training and could usher in a new era of productivity growth in economies burdened with unfavourable demographic trends.

4) Deglobalisation

What do fraying global connections mean for private markets?

We use the term 'deglobalisation' to describe the weakening global integration of trade, capital flows, people, intellectual property and cooperation.

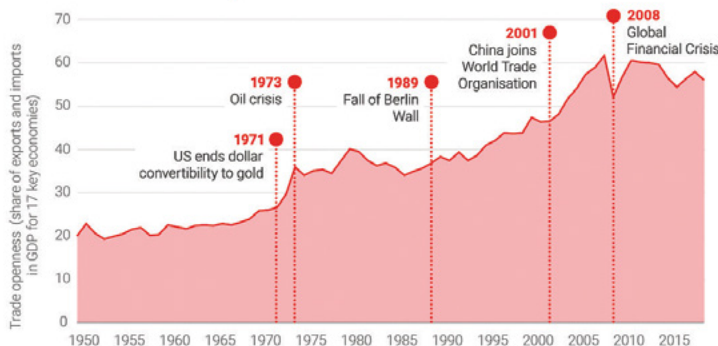
So far, we have seen a slowdown in globalisation, rather than a reversal. Nevertheless, the consequences of weakening global economic integration and political cooperation, particularly between the US and China, represents a material shift in the world's economic landscape. Growth in global trade has stagnated since the Global Financial Crisis; with protectionism on the rise, as exemplified by the USA's Inflation Reduction Act and China's weakening international trade, we believe that 'peak globalisation' may well be behind us.

We believe this will result in the permanent reconfiguration of supply chains, with resilience and diversification of supply prioritised over efficiency, and supply risks mitigated with larger inventories. We anticipate a trend towards onshoring, where supply chains that were once international are reshaped to favour domestic production that carries less political risk, or 'friend-shoring' in countries with more stable relationships with companies' home nations.

In our view, this should translate into more real estate demand, with onshoring and friendshoring likely to be highly selective and focused on key strategic sectors where diversification of supply will remain a priority. Meanwhile, weaker global cooperation and heightened geopolitical tensions are likely to create more macro-economic risks and volatility, favouring more needs-based and countercyclical asset classes.

The above is an extract from our recent publication: The future of private markets.

Globalisation in recent history



Source: World Economic Forum as at January 2023.
Assumptions, opinions and estimates are provided for illustrative purposes only. There is no guarantee that any forecasts made will come to pass.

Key Risk Warnings
The value of investments and the income from them can go down as well as up and you may not get back the amount invested. The details contained here are for information purposes only and do not constitute investment advice or a recommendation or offer to buy or sell any security. The information above is provided on a general basis and does not take into account any individual investor's circumstances. The risks associated with each fund or investment strategy should be read and understood before making any investment decisions. Further information on the risks of investing in this fund is available in the fund offering documents at: www.lgim.com/fundcentre

Company Profiles

BNP PARIBAS ASSET MANAGEMENT

BNP Paribas Asset Management (BNPP AM) is the investment arm of BNP Paribas, a leading banking group in Europe with international reach. BNPP AM aims to generate long-term sustainable returns for its clients, based on a sustainability-driven approach. BNPP AM's investment capabilities are focused around six key strategies: High Conviction Strategies, Liquidity Solutions, Emerging Markets, Multi-Assets, Systematic, Quantitative & Index and Private Assets, with investment processes incorporating quantitative and fundamental analysis.

Sustainability is core to BNPP AM's strategy and investment philosophy. Among the leaders in thematic investment in Europe1, BNPP AM intends to contribute to a successful Energy transition, healthy Ecosystems, and greater Equality in our societies (our "3Es"). BNPP AM currently manages €540 billion of assets (€656 billion of assets under management and advisory) and benefits from the expertise of more than 500 investment professionals and around 400 client servicing specialists, serving individual, corporate and institutional clients in 67 countries.

Legal & General Investment Management (LGIM) Real Assets is a leading investor and owner-operator, fostering long-term relationships that empower us to deliver both positive financial and social outcomes. Managing over £36 billion of assets, providing pension schemes and institutional clients with investment solutions across real estate and infrastructure equity and debt as well as private credit.

Over the past several years we have bolstered our capability in Infrastructure investment, now managing £5 billion of assets across equity and debt (as at Q4 2023). We have launched a new renewable energy strategy in, in partnership with NTR, the Clean Power (Europe) Fund which is structured to allow access for both DC and DB investors. We have also demonstrated innovation in a range of transactions including marketing leading debt-for-nature swaps and first of a kind public-private partnership with a US public school system.

CASE STUDY

AP4 - 50 years of service to Swedish pensioners

AP4 senior portfolio manager, Jan Petersson, **tells** Francesca Fabrizi **how AP4 has been setting the bar high for the European pensions sector for 50 years**

I gather 2024 is a special year for the AP4 fund? Please tell us more.

■ It is indeed. This year, AP4 celebrates 50 years as a buffer fund for the public Swedish pension system, having been founded in 1974. It was reformed in 2001 with the creation of four buffer funds, each starting out with the same amount of capital, SEK 134 billion, and the same mandate. AP4 however is now, together with AP3, the largest of the AP funds, each managing SEK 500 billion. This implies an annual average return since inception in 1974 of 13% and, since reformation in 2001, an average annual return of 6.4%. During a volatile 2023, the return reached 9.6%, topping the league of the AP Funds. The return is the result of a well-developed risk culture in connection with the long-term investment horizon, which has led to a comparatively high allocation to equities in an international context.

Please tell us more about your asset allocation.

■ By the end of 2023, the allocation to the different asset classes was the following: Global equities 34%, defensive equities 5%, Swedish equities 16%, bonds 29% and real assets (listed and unlisted real estate/infrastructure) 16%.

With changes in legislation in 2019 and 2020, the AP funds were given increased flexibility to invest in unlisted assets, which has led to alternative investments growing as a share of fund capital. This, combined with interest rates almost at zero, or even negative for several years, and with equity markets returning far above average return, meant that we saw difficulties in continuing to match historical returns.

So how did we go about it? With an innovative perspective, we

implemented a new asset class called defensive equities in 2022. This new asset class was simply made possible by taking funding funded from the global equities and the bond portfolio. The purpose and goal was to give a higher return than bonds, but without the same risk as the equity market. This made us look for equities with the following characteristics: High dividend yields, strong balance sheets and low earnings volatility. In a relatively short period of time, the new asset class has turned out well.

AP4 historically has been a thought-leader in climate related investment strategies. How is this developing?

■ That's true. AP4 has been a pioneer in climate related investment strategies since 2012. Back then, it was unusual in the investor community to see engagement and investments relating to climate change. This has developed rapidly in the past five to six years, with more funds seeing the necessity of addressing climate change. Even if we did this year, unfortunately, see some institutions, especially in the US, backing off from these strategies, for European investors this continues to be of highest importance.

On our side, we started out with quant strategies in order to reduce CO2 emissions in the global equities portfolio. Four years ago, we also started to manage the resource intensive sectors (energy, materials, utilities and transportation) fundamentally, with a dual ambition – to get a superior return and, at the same time, contribute to the reduction of CO2 emissions within these sectors. These sectors are chosen with the perspective that if we can contribute to the climate transition, it will make a change for the whole equities portfolio.

The ambition is high for these sectors, and we aim at being net zero in CO2 emissions (scope 1&2) in 2040. In the resource intensive sectors, we strive to select either the best-in-class companies when it comes to CO2 emissions, or the ones that might have just started their journey, where it is conducted in an ambitious and credible way, and where we also believe in the equity story.

This strategy means that we do not act like some of our peers, by avoiding the troublesome sectors, but rather we see ourselves as responsible owners and engage with companies in a way that we believe is both responsible for climate transition/ climate change and, at the same time, will give a long-term good return for the companies involved.

For example, we have engaged in the shareholder resolution by Follow This in trying to get Shell to be more precise in their short- to mid-term climate targets being able to meet their long-term ones.

We are realistic in our approach to fossil fuels and we acknowledge that we would not be able to create economic growth and energy security without fossil fuels on a short-term basis, but there is no doubt that we must strive for a future based on renewable energy.

With our investment approach, combining quant strategies and fundamental analysis, we have been very successful in reducing our CO2 emissions so far. Since 2010, the CO2 emissions for the equity portfolio have been reduced by 65%. Ever since our investment strategies in 2012 included CO2 strategies, AP4 has been awarded numerous prizes within the pension industry.

Please tell us more about your equity allocations.

■ The equity portfolio of SEK 280 billion, by end of 2023, was divided by about two thirds in global equities, where the mentioned resource intensive sectors are managed by a fundamental approach and the other sectors are quantitatively managed with an aim to reduce CO2 emissions.

We manage all developed markets internally, while emerging markets are managed by external fund managers.

In the domestic equity portfolio, which represents about one third of the equities portfolio, we are often a large shareholder in the companies we are invested in – we often own between five to ten per cent, making us one of the larger shareholders. Because of this, we put significant effort into shareholder engagement and, in a large part where we are one of the larger shareholders, we work on the nomination committees for the board of directors. We put a lot of effort into being responsible shareholders for all ESG aspects but also, with nominating the best boards, get the companies to generate good returns.

The described strategies have served us well over the years. Looking forward, we must keep striving to achieve the highest possible returns, being a responsible shareholder and keeping our leadership in environmental investment strategies.

We live in a challenging world, both economically and politically, so we must always be on our toes and be able to take risks when we see high possibilities for it to pay off.

"WE LIVE IN A CHALLENGING WORLD, ECONOMICALLY AND POLITICALLY, SO WE MUST STAY ON OUR TOES AND BE ABLE TO TAKE RISKS WHEN WE SEE POSSIBILITIES FOR IT TO PAY OFF"

PODCAST

Stepping up to the challenge

In the latest *European Pensions* podcast, editor Natalie Tuck **talks to PensionsEurope chair,** Jerry Moriarty**, about his new role and the European pension policy agenda**

Many people in the industry will know you as Irish Association of Pension Funds (IAPF) CEO, but you've also been involved with PensionsEurope for many years. Can you tell us about your work there and how you came to be elected as chair of the association in November last year?

■ I joined the board of PensionsEurope in 2012, at the time that it changed from being the European Federation of Retirement Provision to PensionsEurope. The IAPF has been a member of PensionsEurope for quite some time – I think it was one of the founding members. PensionsEurope is an association of pensions associations based in Brussels. We have 24 member associations from 18 EU countries and three other European countries.

In total those associations look after pensions for 90 million people covering about €5 trillion in assets. Primarily, the function is to advocate on behalf of those member associations in Brussels, and recently in Frankfurt as well, with both the European institutions and the European Insurance and Occupational Pensions Authority (EIOPA).

For small countries like Ireland, where so much of our legislation comes from Brussels, it's important that we can lobby on that and be involved in it at its preparation stage. In terms of how I got elected, I'm not quite sure how that happened, but I've been on the board for some time. It is quite a privilege to chair the board.

What does your role as chair entail?

■ When you've been on the board of something for quite some time, stepping up to be the chairperson isn't hugely different. There's a lot more in terms of pulling things together, in terms of dealing with PensionsEurope CEO, Matti Leppälä. We touch base a lot in terms of preparing for board meetings or being a sounding board for Matti and the other directors. The role of the board is working on the strategy of the organisation and ensuring that strategy is implemented. We also feed in a lot to the policy positions that the organisation is taking. There is a lot going on in Europe at the moment so it's quite demanding in that way.

What are the key areas you would like PensionsEurope to focus on during your tenure?

■ A lot of the key issues are issues that are out there anyway and that we do need to look at. We do a lot of thinking about shaping the future of pensions. Particularly with ageing populations across Europe and the role that funded pensions can play in making sure that as we deal with ageing populations people can have good retirements.

Ageing populations put a lot of stress and pressure on the traditional pay-as-you-go systems for most social security systems and so we're finding increasingly that people need supplementary savings.

We're also doing a lot of work in the defined

contribution (DC) space because we're seeing a lot of transition to DC, or particularly in a lot of the newer Eastern European countries that are newer members to PensionsEurope. There are also some other issues, such as the IORP II review and EIOPA has provided its advice to the European Commission on that.

The Capital Markets Union is going to be a huge focus and there's a lot of stuff going on around sustainable finance and then you've got things like the Digital Operational Resilience Act (DORA) or the Financial Data Access (FiDA) framework, looking at open data, which may or may not involve pension funds.

You listed some of the legislation and the consultations that are coming out of Europe currently. What do you think are the key ones that pension funds really need to be thinking about?

■ I think DORA is a big one. That is looking at how pension funds protect their financial data, ensuring systems are adequate. One of the issues we are finding is that as well as the pension legislation (such as the IORP II Directive, which is geared towards pension funds, and is appropriate and proportionate), a lot of other legislation, which is aimed at financial institutions is also now including pension funds.

Pension funds vary in that – well, they have a financial aspect to them. However, many of them are social institutions that have been set up by social partners in many countries, by employers to provide provision for their employees, so they're not the same as financial organisations that are marketing products to clients, but a lot of the time the same rules are being applied and that is becoming a problem. A lot of legislation that is intended to deal with a large financial institution can also catch up in it a relatively small pension fund. We need to try and ensure there's proportionality around that.

It comes into effect in January next year, but a lot of the details and requirements aren't going to be published until the summer, so there's going to be a timeline aspect to that. Then there's a review of the Sustainable Finance Disclosure Regulations (SFDR) and the IORP II review is going to be important as well. However, because we're at a changeover point, as the European elections will take place in June, it will take time for the new commission of parliament to get up and running.

You mentioned the upcoming European elections – what does the association want to see from a new European Commission. Is it more thoughtfulness towards pension funds when developing legislation that affects them?

■ I think we do want to see that. We do understand there's going to be a lot of focus on funded pensions. Like I said earlier, we're seeing ageing populations, we're seeing a lot of pressure on the traditional social security systems. If they operated on a pay-as-you-go basis, where you now have a big shift in the balance between the number of pensioners and the number of workers you have in the economy, that impacts how those can be funded over the long term, so a lot of countries do see more funded pensions as part of that solution.

I think we need regulation that balances proper protection of people's retirement savings but also encouraging pension provision and making it easier for people to do. I do think there needs to be a bit of focus on financial literacy, making sure people understand the need to save for retirement and the need to have a good framework within which they can do that. There are huge issues about gender gap. That's probably more a labour market issue but it does also feed into pension savings as well and women do tend to have much lower pensions than men.

Fixing the labour market issue will address that but there are probably good practices and good things that pension funds can do as well so I think there will be quite a bit of focus on that. Probably that bigger issue is just making sure you deal with the ageing populations and the role that funded pensions can play within that.

How important is that collaboration for the development of pensions policy?

■ I think it's important because our systems are very different and even how they link in with social security systems is very different. However, everybody is trying to achieve the same thing – to ensure that people can have good retirements. I think what we can learn from each other is important but also coming together and understanding the differences we have and working towards that common objective, is a way of achieving the things we want to achieve. Ultimately, to make sure that people can have good retirements, which is important to all of us.

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An eye on currency

FX: The multi-tasker

Lynn Strongin Dodds reports on the strategies pension schemes are applying to currency, including hedging and return-seeking strategies, as pension schemes continue to allocate more to global equities

PAGE 38

Widening the net

Mesirow senior vice president, Katie Renouf, discusses FX cost-saving opportunities and the growing case for agency trading, as portfolios become more diverse across asset types and geographies

PAGE 40

In association with

INVESTMENT

Currency: The multi-tasker

Increased market volatility has sparked greater interest in return seeking currency strategies but hedging remains a significant part of currency strategy as pension schemes continue to allocate more to global equities particularly in the US

WRITTEN BY **LYNN STRONGIN DODDS,** A FREELANCE JOURNALIST

Currency management is not a new theme for European pension funds. They have been hedging their FX exposure to global equities over the past 20 years, but more recently alpha generating opportunities are back on the table as volatility has spiked.

It certainly has been a roller coaster ride since 2020, starting with the outbreak of Covid, followed by Russia's invasion of Ukraine, a mini banking crisis in the US and the more recent war in the Middle East. FX has been caught in the crossfire as interest rates have increased to curb stickier than expected inflation, while growth in the UK and on the continent has stalled. The prevailing view is that central banks will no longer move in tandem, opening the door for return-seeking prospects.

"Central bank policy differences influence interest rates, which in turn influence currencies," says Mesirow Currency Management managing director and senior strategist, Uto Shinohara. "The challenges lie in conditions where central bank policies are all in lockstep where there is less opportunity due to limited divergence, promoting sideways, non-trending environments. More recent divergence in policy between the Federal Reserve and European Central Bank (ECB) promote FX price movements."

"The US presidential election is another risk event on the horizon that can drive currencies, with ramifications affecting geopolitics and global economies," he adds. "These price swings reveal opportunity. The FX market is large and liquid, where the majority of market participants are not speculative but central banks and corporations trading FX as part of their operations, so less crowding."

Making predictions

One of the main issues, though, is predicting which central bank is likely to make the first interest rate cut move. This is not easy given that forecasts have vacillated over the past two years. For example, at the start of 2024, all bets were on the US, but expectations have been pushed back as inflation climbed to 3.7 per cent, which was higher than the 3.4 per cent consensus. As a result, analysts changed their outlook from the six to seven quarter-point rate cuts to perhaps one or two later in the year. In the options markets, many participants put a probability close to 20 per cent on the next move being a rate rise instead.

The European Central Bank (ECB), on the other hand, has been making noises about June, provided there are no nasty surprises in wage or price developments. The latest set of results show that things are going to plan with inflation unchanged in April from March at 2.4 per cent. Some policymakers though are more cautious, concerned over rising energy costs and the ongoing conflicts, which threaten to disrupt shipping and push up commodity prices.

ECB President, Christine Lagarde,

encapsulated the mixed sentiment by stating that eurozone inflation is likely to decline further, and interest rate cuts are on the horizon if its long-standing price growth criteria are met. However, "at the same time, the Governing Council is not pre-committing to a particular rate path", she said. "Risks to the inflation outlook are two-sided. Upside risks include heightened geopolitical tensions, as well as higher wage growth and more resilient profit margins than anticipated."

Reaping rewards

Despite the uncertainty, many schemes are adding currency to the portfolio to reap the rewards. As Russell Investments global head of solutions strategy, Van Luu notes, currency return-seeking strategies are a good diversifier because they are uncorrelated to equities and bonds. He points to 2022 when there was a big sell-off in both markets, and FX was one of the few asset classes that performed well for the first three quarters of that year.

"At the moment, with interest rate differentials staying stable we believe that the carry trade, which has done quite well, will continue to do so," he said.

One of the most popular is the yen carry trade, whereby investors cheaply borrow the Japanese currency to fund investments in higher-yielding assets, such as the US dollar. Although Bank of Japan recently intervened in the market after it plunged to a four-year low, analysts do not see interest waning in the yen/dollar trade until the Fed starts cutting rates.

Emerging markets

Emerging market (EM) currencies are also sparking interest, according to Luu.

"Investors did not look at emerging markets in the past because of the risk but now they are taking a closer look because of performance," he adds. "Our emerging market carry trades has risen 16 per cent over the year and they are still going strong. Some of the trades we are doing are going long on the Mexican peso and South African rand and short on some of the lower interest rate currencies, such as the Korean won and Thai baht."

Record Currency Management chief investment officer, Dimitry Tikhonov, echoes these sentiments: "Exposures to EM currencies generate additional returns because they are exposed to faster growing economies. They also offer access to diverse economies which display different behaviours, with attractive interest and growth rates in some countries. However, you need a very disciplined approach to analysing these countries."

> **"CENTRAL BANK POLICY DIFFERENCES INFLUENCE INTEREST RATES, WHICH IN TURN INFLUENCE CURRENCIES"**

This is particularly true with reverse carry trades, which are more complicated but have recently appeared on the investment radar screen given the returns have been as high as 9 per cent this year. This entails dollar bets funded by emerging market currencies such as the Chinese yuan, Thai baht, Malaysian ringgit and the Czech koruna.

Hedging strategies

Although there has been a renewed focus on alpha generation strategies, hedging remains an important part of the FX equation, especially as European pension funds have been whittling down their domestic exposure for the past 20 years. The approach to both depends on the country, its pension fund framework and national legislation. As Tikhonov points out, active FX management is popular in the Nordic region while Swiss pension funds tend to use a passive approach. Meanwhile, the UK and Germany are interested in both hedging and active management to generate additional returns. Most Swiss and German pension funds have a regulatory obligation to hedge a certain amount of FX risk.

RBC BlueBay Asset Management senior fixed-income portfolio manager, Kaspar Hence, agrees, adding: "European pension funds are highly regulated and are only allowed to take a certain amount of risk. In the FX space, most of this comes from their exposure to global equities. If you look at the typical global FX basket, the US dollar accounts for 40 per cent followed by 30 per cent in euros, 10-15 per cent in the Japanese yen, 10 per cent in China with the rest in other emerging market countries."

This year has been especially difficult due to the strength of the dollar. "With US investments making up the lion's share of international allocations, euro against US dollar has a meaningful influence on the portfolio," says Shinohara. "The swings can be large – euro weakened -20 per cent in 2021 through most of 2022, followed by an +18 per cent retracement into 2023."

The latest figures from the European Fund and Asset Management Association (EFAMA) shows that regardless of these challenges, US equities remain the favourite. This is not surprising not only due to the increased share of US companies in the world equity index, but also robust economic growth and the leading role of its technology companies.

INVESTMENT

Widening the net

As portfolios become more diverse across asset types and geographies, the need for FX cost-saving opportunities increases and the case for agency trading grows

The concept of centralised execution and FX netting is not new, for some time, asset owners have been well-informed of the scope to create cost savings and process efficiencies. The drivers have perhaps changed; counterparty risk and cost savings remain important, the evolving regulatory and reporting landscape, plus imminent US equities move to T+1, all play a role.

In this article, **Katie Renouf** – Senior Vice President on **Mesirow's** Global Investment Management Distribution team, based in London – explores how a rapidly evolving investment landscape, and subsequent FX netting opportunities, has led to increased interest in agency models.

When I think back to the start of my FX career, some 20 years ago, it's fair to say the industry has come a long way.

Wide margins, and a lack of transparency around price methodology and source, underpinned by basic documentation, were commonplace. This led to a fundamental lack of trust – forming the basis for a number of regulatory shifts, principally designed to create a fairer and more stable marketplace.

We have reached a point where competitive pricing is largely accessible to all - where counterparties and third-party providers are required to provide granular detail around pricing source and methodology.

However, when it comes to execution counterparty / liquidity providers, there remains scope for improvement. The FX price might look competitive on a single trade basis, but unless you are considering all FX exposures on a portfolio basis you are missing the full picture.

This is often the case when clients delegate FX to their administrator or custodian.

Each provider adheres to the best execution in context of the managed portfolio(s), but a lack of visibility to see the underlying client's full portfolio and FX exposures hampers order aggregation or netting opportunities.

Additionally, many custodians provide a principal-only execution model – meaning that clients face a single execution counterparty from both a risk and pricing perspective. Not only is this inefficient and expensive, but it can also create a "locked-in" element to the relationship – where FX revenue is used to balance underperforming revenue products such as global custody. This can make it very difficult to extract FX from the relationship in the future.

Having a specialist provider adopt a third-party "birds eye" view of all portfolios can be highly beneficial. By establishing an open architecture framework, connected to delegated managers and service providers, a fiduciary agent can achieve best execution across the asset owner's entire book.

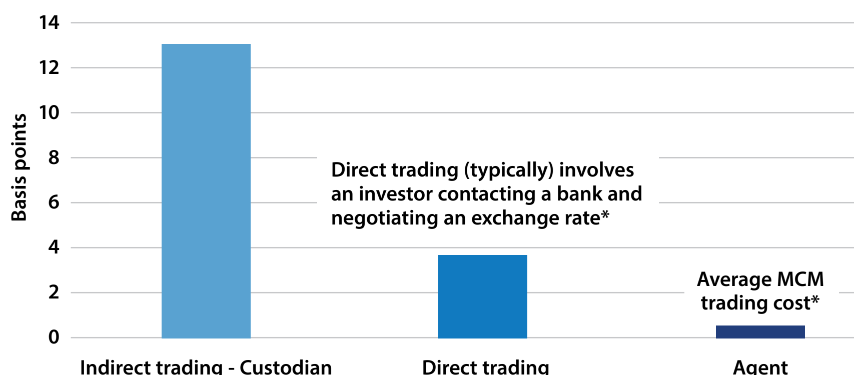
This is particularly topical when we consider the ongoing shift from defined benefit to defined contribution, underlying portfolios are becoming increasingly diverse from both an asset and geography standpoint. Assuming that delegated managers are being used, at least some of the time, this has potential to create an ever-increasing number of siloed currency exposures.

Let's consider an example, Asset Owner A wishes to increase their global equity exposure and re- duce their global bond book, keeping base currencies in GBP for simplicity.

The equities manager liquidates a portion of their portfolio, realising multi-currency cashflows back to GBP, all of which require FX. At the time of writing, the non-GBP exposure of the MSCI World index is more than 96%.

The bond manager also implements the increase to their portfolio accordingly. Currently, the GBP component of the Bloomberg Global Aggregate Bond Index is just

AVERAGE TRADE COST



over 4%.

Whilst both managers could be achieving strong FX execution and pricing terms on an individual basis, their inability to see the other's activity results in far greater FX volumes than needed.

Whilst the currency composition of each index is not identical, applying netting to both portfolios could reduce the execution figure significantly.

Furthermore, the compressed ticket size(s) reduces market impact, typically resulting in tighter spreads.

If you scale up this concept across an ever-increasing number of sub-funds and asset classes, the argument for netting becomes increasingly compelling.

FX execution cost savings generated through an agency provider netting solution can exceed 30% in some cases.

The above scenario could be further complicated by the forthcoming US equities move to T+1; many managers have yet to establish FX trading processes that accommodate this.

The compressed timeframe for settlement means that they may have to act upon unmatched trade estimates – creating enhanced risk of error – or, alternatively, maintain long USD positions to provide liquidity to settle late trades. Neither of these options are particularly efficient from a risk, process or return perspective.

There will also be a marked impact on the huge proportion of managers who settle their trades via CLS. CLS deadlines cannot accommodate the move to T+1, meaning that gross settlement will lead to clients having to maintain larger USD cash reserves.

Again, using a third party agent can be beneficial in this situation. By taking a cross-portfolio view on currency exposure, the agent condenses the net execution figure as far as possible. This compresses not only cost but also counterparty risk, and potentially reduces the USD balance level that needs to be maintained.

Where long USD overnight positions need to be held, Mesirow's cash equitization service can reduce portfolio performance drag. We sweep residual balances into index-linked futures, generating a return far closer to the portfolio benchmark than holding cash.

Many clients are not set up to trade futures, so the cost of implementing this themselves prevents it from being a viable option. Through our strong market positioning, we have access to more competitive pricing terms than many clients can access.

There are asset owners that already centralise their FX execution in-house. Granted, for those names, some of the points highlighted above are not relevant. They are already achieving an efficient level of FX trade netting.

However, the process of establishing and maintaining a broker execution panel is problematic. There are numerous legal documents and credit facilities to consider, combined with the cost and risk aspect of undertaking the process in-house. An FX back office that historically required 2-3 FTE's is now likely to require more.

Furthermore, there is always a critical mass – where volumes become sizeable enough for in-house management to appear the more attractive option. However, due to the points mentioned above and the subsequent cost base increase, this figure now looks a lot higher than in previous years.

One final angle to consider is regulatory reporting. For example, recent changes to EMIR reporting requirements ("EMIR refit") increased the number of reported fields per trade from 129 to 203. Many clients choose to delegate this task, and by reducing the total number of trades, the cost base is reduced accordingly.

Whilst evolving regulation is integral to protecting the interests of market participants, it requires constant monitoring and resource; making it preferable to delegate this element to a third-party FX provider.

To learn more about Mesirow's Fiduciary FX capabilities, contact:
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COUNTRY SPOTLIGHT | SPAIN

Seeking a sustainable system

Spain is reforming its public pension system to ensure its sustainability, but how effective are these reforms likely to be? Jack Gray **investigates**

Like many of its European counterparts, Spain's population is ageing and putting pressure on the country's pension system. An increase in the number of pensioners and a reduction in the number of workers have led to concerns over the system's affordability. "Spain, like the rest of the European countries, has an important demographic challenge that will have a relevant impact on the sustainability of the public pension system, intensified by the access to the retirement pension of baby boomers," notes CPPS Asesores managing director, Mariano Jiménez.

The European Commission's (EC) recent *Ageing Report* for 2024 forecast that Spain was the EU country in which public pension spending would increase the most compared to the 2021 scenario, predicting it would have risen by 3.3 percentage points in 2050 and by 5 percentage points in 2070, due to the 2021-23 reforms. While income from contributions is expected to increase by 2 percentage points to 12.6 per cent between 2023 and 2050, the EC forecast this would be insufficient to cope with the expected advance in spending on pensions.

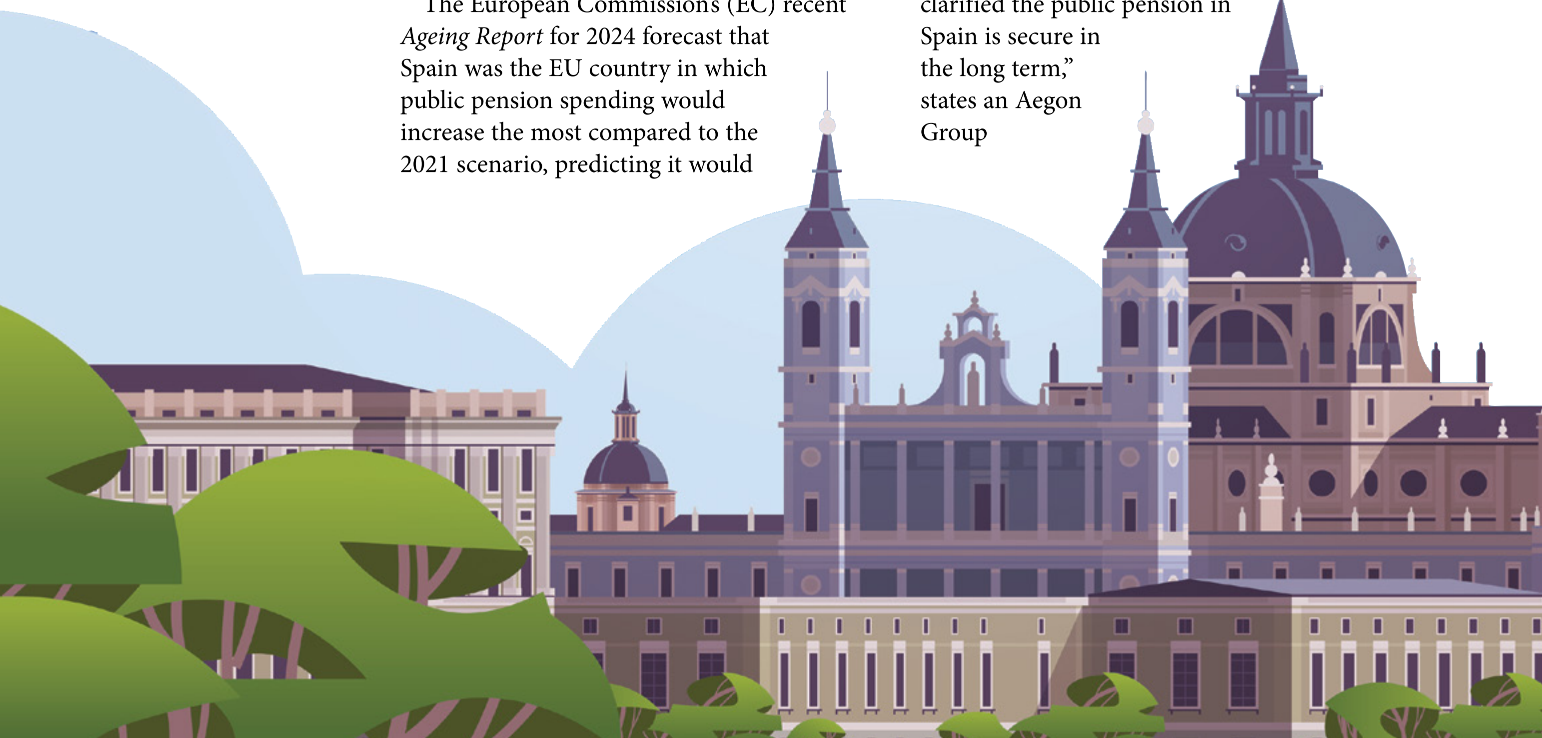
"Pensions are, by far, the largest item in the general state and social security budgets," says Santander Asset Management head of pensions, José González. "Among the main factors that influence the growing pension expenditure is their revaluation based on the Consumer Price Index (CPI), the new pensioners who access this condition and a greater life expectancy.

"Furthermore, a low birth rate and level of unemployment directly affect lower social contributions. This circumstance, together with the fact that contribution income does not grow to the same or greater extent than pension expenses, will be an added difficulty for controlling the system's deficit, which will continue to be combated through transfers made by the state to social security."

Current sustainability

Despite the concerns, many believe that the public pension system is sustainable for the long term, and that appropriate measures will be taken to keep it that way.

"First of all, it should be clarified the public pension in Spain is secure in the long term," states an Aegon Group



spokesperson. “However, what must be taken into account is that, in the coming decades, there could be a fall in the replacement rate. In this scenario, it is advisable for workers to have private saving plans to supplement their public pension and thus maintain their purchasing power at the time of retirement.”

BBVA Research head of economic activities, Rafael Doménech, adds that the system is sustainable as long as the government continues to act to ensure its affordability. The Independent Authority for Fiscal Responsibility (AIREF) will assess the pension spending gap in 2025 and likely ask the government to propose either revenue or expenditure measures to close any shortfall. “If there are no measures, on 1 January 2026 there will be an increase in social security contributions,” explains Doménech. “I’m not sure additional measures will be implemented next year because you always have the adjustment mechanism to say contributions will increase if there is no agreement.

“We assume the system is sustainable, and we assume that these conditions will be met because the political cost of having the system with this deficit will be so huge that, at the end of it, there will be some agreement to avoid a situation where the system would be unsustainable.”

Although these conditions are in place, WTW Spain Retirement associate director, Rafael Villanueva, concedes that public pensions are under “considerable pressure, which calls into question its long-term sustainability”.

“The current distribution model, based on the principle of intergenerational solidarity, faces critical challenges due to an ageing population and one of the lowest fertility rates in the world,” he continues. “We will have to see how the macroeconomic variables evolve, but every indication, including the recent opinion of the EC, suggests that additional measures will be necessary, including possibly on the expenditure side too.”

“EARLY RETIREMENT AND LATE RETIREMENT REFORMS HAVE BEEN UNDERTAKEN TO DELAY THE EFFECTIVE RETIREMENT AGE”

Pension reforms and their impact

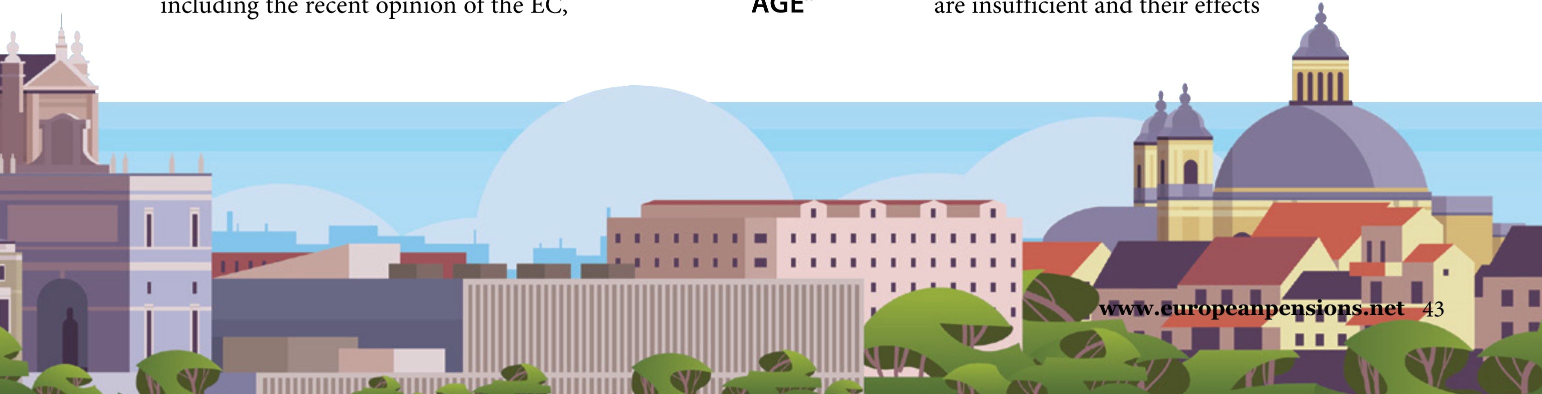
Spain recently underwent a series of public pension reforms that aim to provide greater sustainability to the system. In 2021, price indexation was reintroduced, linking pensions to CPI. “Specifically, it links the annual growth of pensions to the average of the interannual variations of the 12 months prior to December of each year,” González explains.

The intergenerational equity mechanism was also introduced to ensure that annual increases in retirement, survivor, and disability benefits continue to be indexed against CPI. From 1 January 2023 to 31 December 2050, employers and employees will pay a special contribution to build up the public reserve fund, starting at 0.5 per cent and 0.1 per cent of eligible earnings respectively, rising gradually to 1 per cent and 0.2 per cent, respectively.

“The EC’s report has shown that the 2021-23 reform has increased revenues, but has increased expenditure by a larger amount,” notes Doménech, “According to the estimates in the report, the financial needs of the public pension system last year were equivalent to 4 percentage points of GDP. This will increase to 5.7 percentage points by 2050.”

Jiménez adds: “Maintaining the level of pensions by increasing it through CPI is desirable and contributes to the adequacy of the system, but it has a high cumulative cost that is not offset by other measures on the expenses side.

“Early retirement and late retirement reforms have been undertaken to delay the effective retirement age. Although they are going in the right direction, they are insufficient and their effects



will be very limited. It's almost sure that the access to early and partial retirement will suffer another reform in the following months.

"The latest reforms are all aimed at increasing the income of the system but, sadly, not in the necessary quantity."

Villanueva states that the balance of the reforms appears to be in deficit, as the additional revenue measures did not seem to alleviate the increase in expenditure.

"Incentives to prolong working life do not seem to be an important counterbalance to this increase in spending either," he says. "On the revenue side, moreover, it is highly dependent on the evolution of GDP and employment, and therefore on contributions and revenue for the system."

The case for further reform

While some are sceptical about the effectiveness of the 2021-23 reforms, there are several ways in which future reforms could ensure the sustainability of public pensions in Spain. The agreement between the government and the EC gives the government the opportunity to propose measures to tackle the pension spending gap after the AIREF's assessment next year, or automatically increase social security contributions, if there is a shortfall.

There are several other measures that could reduce expenditure, and Doménech states that following best practice observed in other European countries could be a way forward. "A combination of either an increase in the retirement age with life expectancy, and if you want to retire earlier to pay a cost in terms of your initial pension," he says.

"There are other measures, such as taking into account the whole working career and contributions. For us, and this is something we have been proposing for the past 10-15 years, we think a system like the national account systems we have in Sweden, Estonia, and other European countries is not only the most sustainable, but also the most transparent and efficient system.

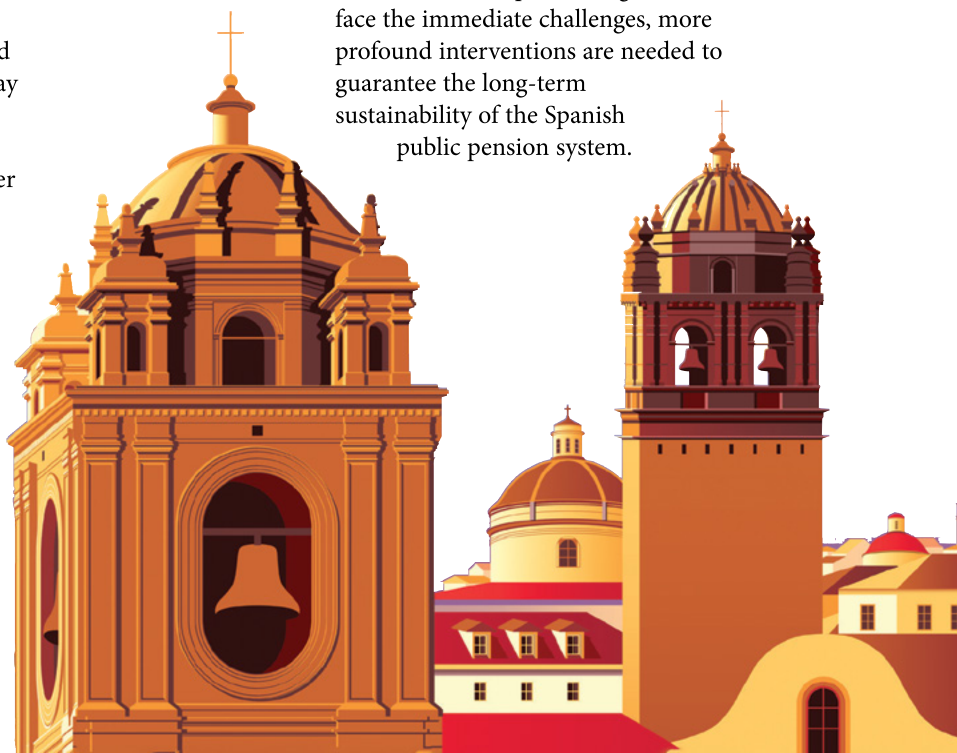
"THE LATEST REFORMS ARE ALL AIMED AT INCREASING THE INCOME OF THE SYSTEM BUT, SADLY, NOT IN THE NECESSARY QUANTITY"

"Then we could introduce additional financial restrictions to ensure the system is sustainable, for example in the Swedish pension system they have a clause condition in case there is a financial imbalance in the system; pensions every year will be conditioned on the imbalance in the system."

The sustainability of the public pension system has also brought the need for private and workplace pension savings into the spotlight. "The Spanish government is working on a law to promote occupational pension plans to encourage savings through companies, a concept that has not been extensively developed in Spain to date, with the aim of facilitating savings to supplement public retirement through the second pillar of social welfare (savings in occupational plans)," says an Aegon Group spokesperson.

Jiménez also points to the government's plans to develop the workplace pension system, including promoting its inclusion in the framework of sectoral collective bargaining and including measures to make it more flexible, attractive, and easy to implement and manage. "Hopefully, we can see an increase in this type of system in the following years in Spain, and a change in the Spanish savings culture, to have a solid and growing market of complementary pensions in Spain," he says.

Villanueva concludes that while recent reforms are a "step in the right direction" to face the immediate challenges, more profound interventions are needed to guarantee the long-term sustainability of the Spanish public pension system.



CASE STUDY

A bite of the apple

Norfolk Pension Fund head of funding and investment, Alex Younger**, and Robbins Geller Rudman & Dowd co-founder and partner,** Mark Solomon**, speak to** Natalie Tuck **about the pension fund's recent success in a class action case against the tech giant Apple**

Norfolk Pension Fund has recently secured a USD 490 million settlement in a class action against Apple, in which it was the lead plaintiff. How did the situation arise?

■ **Alex Younger (AY):** Like most pension funds, Norfolk Pension Fund has had exposure to shares of Apple in its portfolio, some of which were acquired in late 2018 shortly after Tim Cook had made his allegedly false representation concerning iPhone demand in China.

Years before we had retained Mark and his law firm Robbins Geller Rudman & Dowd to monitor our portfolios of listed securities and report instances of losses attributable to possible securities fraud and assist us in monitoring the collection of settlements arising from the hard work of other plaintiffs. As part of this relationship, in early 2019, Mark reported to us that the fund had suffered potential losses on its recent purchases of Apple shares.

The prices had fallen after the truth was revealed at the beginning of that January. From a responsible ownership and stewardship perspective, we were motivated to act.

Coincidentally, I had just attended and had given evidence in a successful three-week securities fraud jury trial against Puma Biotechnology and its CEO in California following over three years of litigation, in which, again, Norfolk was the lead plaintiff.

Apple contested the accusations at every stage, was this expected and how did you overcome this?

■ **Mark Solomon (MS):** There are a few certainties; death, taxes, and the fact that defendants will always file motions to dismiss in every case, no matter how meritorious the case may be.

Given that these defendants had the limitless resources of Apple available to pay their lawyers, we expected the fight to continue through the multi-year discovery phase in the USA and UK; we expected them to fight class certification; and we expected them to continue to contest the case through their attempt to have the court award them summary judgment after all of the evidence had been gathered, presented to, and considered by the court.

True to form, many tens of

millions of dollars were surely expended on defendants' lawyers in all of these futile efforts and more while, throughout, we provided our services to Norfolk and the class on a wholly contingent fee basis at no-out-of-pocket cost to Norfolk or the class.

We were able to reach the proposed settlement and overcome the defendant's often scorched earth defence tactics by being tenacious, focused and determined to invest whatever resources necessary in both our lawyers' time and capital outlay to optimise the outcome. In that effort, we were fully supported and assisted by Alex and Norfolk who, from their track record in winning a jury verdict of over USD 54 million with us in the Puma case, presented themselves as a formidable adversary.

What extra work is involved for a pension fund acting as a lead plaintiff in a class action? How involved was Norfolk Pension Fund in the legal process?

■ **AY:** Every case needs a lead plaintiff otherwise there is no case and no recovery. No law firm other than Robbins Geller identified the claims we made and successfully pursued, so we were concerned that if we didn't act, the wrongdoing could go unaddressed either entirely or in sub-optimal fashion.

Seeking and occupying the lead plaintiff position required us to marshal our data and liaise closely with Mark and his team throughout the case. That required close attention at times to ensure we did all we should to produce evidence of our transactions and process, prepare and sit for my deposition, as well as engage with Mark and team on status updates, strategy, the mediation process, and ultimately oversee the USD 490 million resolution. We believe it is crucial to take the role of lead plaintiff extremely seriously as part of our duties to the class.

The involvement did not impede my ability to perform my regular duties and Norfolk Pension Fund is allowed to seek reimbursement for the time I and colleagues devoted to supporting the case.

What are the next steps?

■ **MS:** An important aspect of the American system is the respect, at the end of the day, for the fact that these class claims are the aggregation of thousands of individual claims.

So, the judge must approve the settlement and allow class members to object or opt-out. That process will occur over the next few months and, if the settlement garners final approval, the claims process will begin leading to distribution of the settlement funds to Norfolk, and the other investors, on a pro-rata basis.

Are there any other class actions that Norfolk Pension Fund is currently involved with or using stewardship to change procedures/strategies at any companies it invests in?

■ **AY:** Yes, we are lead plaintiff of a case in which Mark and his colleagues at Robbins Geller again are lead counsel against Anadarko Petroleum and its former executives which is pending in Houston, Texas.

Essentially, it's alleged that Anadarko was drilling in dry wells, knew it, but kept that information from investors. The Texas judge is about to have a second look at his class certification of the case after the court of appeals instructed him to allow another submission from defendants.

> "WE BELIEVE IT IS CRUCIAL TO TAKE THE ROLE OF LEAD PLAINTIFF EXTREMELY SERIOUSLY AS PART OF OUR DUTIES TO THE CLASS"

What should pension funds consider when looking for a legal representative for a class action?

■ **Alex and Mark:** Any investor considering retaining a US firm to undertake securities fraud class action representation should conduct a careful analysis of the following: Track record – Examine the law firm's track record in securities litigation; its size and capacity; its standing both in terms of the amounts of its historic recoveries and the significance of any corporate governance reforms achieved.

Preferably the information will be derived not just from what the firm advertises but will be supported by commentary from objective third parties, clients, and even judges.

Trial experience – Inquire of the identity and experience of the trial lawyers assigned to the case. Many self-identified securities fraud firms have no trial lawyers or any experience in trying a securities case before a jury. Inquire because it's impossible to maximise the outcome of a case without a credible threat of trial.

Financial strength – Does the firm have the financial capacity to fund the case and is it willing to go toe to toe against defendants with effectively limitless corporate coffers to pay their corporate lawyers? Find out if the firm borrowed from the government during the Covid crisis. All firms that did, thereby attesting that they lack financial capacity, are far less likely to be both able and willing to finance large cases to the optimal extent when the going gets tough.

Cross-border expertise – Does the firm have dual qualified lawyers capable of weighing any competing interests or potential conflicts associated with any proposed course of legal action?

ESG

Part of the problem, or part of the solution?

Laura Blows explores the complex debate around pension funds investing in the defence sector

Do pension funds want to be part of the problem, or part of the solution?

This is the question Netherlands Minister of Defence, Kajsa Ollongren, posed to Dutch pension funds in February this year, as she called on them to increase their investment in defence firms.

Whether to invest in defence is an important debate to have, Impact Europe head of policy and EU partnership, Jana Bour, states.

"How to ensure long-lasting peace? What is the role of institutional investors, such as pension funds in it? How to protect our communities from violent attacks? Is it ethical to help neighbours to defend themself? These are the questions we did not ask ourselves few years ago. The year 2022 *[the start of the Russia/Ukraine conflict]* has changed that for Europe and this important debate now needs to take place," she says.

Two camps

This important debate centres around the thorny issue of ethics, with two opposing camps "both looking at UN Sustainable Development Goal 16 – to promote peaceful and inclusive societies", Bour says.

The first camp believes that governments, investors, civil society and communities need to work together to find lasting solutions to conflict and insecurity and that strong defence systems, including within the cyber space, are a precondition for lasting peace, she explains.

The other camp believes "that there can be no peace and stability while financial institutions continue to fund the production of, and trade in, arms", Bour adds.

These opposing viewpoints can be tricky for pension funds as investors to navigate from an environmental, social and governance (ESG) perspective.

For Swedish pension fund, AP7, there has been a clear shift in the investment debate, "where the defence industry used to be a generally dubious investment, while at least some today think it's the other way around. Excluding the defence industry is the dubious approach", its spokesperson says.

However, the AeroSpace and Defence Industries Association of Europe (ASD) notes that, according to the experience of its member companies, "the biggest challenge for the European defence industry in terms of accessing private funding is currently that, due to ESG considerations, a significant portion of financial market actors in Europe is refusing to invest in companies involved

in defence activities".

"These difficulties must be overcome as soon as possible to ensure Europe's ability to protect its citizens and territory. Financial market operators, such as pension funds, therefore have an important role to play with their investment decisions when it comes to ensuring the security, resilience and sovereignty of our societies and democracies," the ASD spokesperson adds.

The European Commission's (EC) new *European Defence Industrial Strategy*, published in March, states that the EU sustainable finance framework "does not impose any limitations on the financing of the defence sector".

It adds that "with the exception of weapons subject to prohibitions by international conventions signed by member states – which are therefore deemed by the EU to be incompatible with social sustainability – the defence industry enhances sustainability, given its contribution to resilience, security and peace".

Despite this, for some, investing in weapons is just too 'dubious' still.

The Global Alliance for Banking on Values (GABV) issued a Statement for Peace in February, calling on the financial industry to stop financing the production and trade of weapons and arms, stating that the "financing of weapons and arms does not qualify for, and is at odds with, any definition of sustainable finance".

PensionsEurope policy and communications officer, Gabrielle Kolm, also highlights the reputational risk of pension funds investing in defence. "There has been a big change before and after the *[Russia/Ukraine]* war, where we were in a demilitarisation era and now we are moving towards militarising." This needs to be communicated effectively to society, she explains, due to the reputational risk investing in defence may have for pension funds.

PensionsEurope CEO, Matti Leppälä, gives the 2007 example of some of the largest Dutch pension funds investing in clusterbombs and landmines, and the reputational uproar that generated.

It also should not be assumed that 'ethical funds' automatically exclude defence firms, as Morningstar Direct research from April 2022 found that, amongst sustainable funds globally, just 23 per cent have a stated policy of excluding military contractors, with 44 per cent of sustainable funds having some exposure to military contractors (compared to 60 per cent for other funds).

Defining which companies are actually involved in defence is more complex then may first appear. For instance, Leppälä highlights the firm Rolls Royce, which produces engines for planes. "What goes to the fighter planes? What goes to the commercial airlines?" he asks.

"The same defence material can be used for offence as well as defence, or in conflicts that the investor may deem to be unethical," he adds.

Many pension funds have navigated this complexity by investing in defence, but excluding those that manufacture controversial weapons banned under international law, such as anti-personnel landmines, and biological and chemical weapons.

For instance, AP7's spokesperson says there has been no recent change to its approach, and that it has no general restrictions against defence investment, "but we do blacklist companies involved in cluster munitions and nuclear weapons". AP7 invests in defence as part of the MSCI ACWI index, buying all its companies, bar those it blacklists.

Increasing pressure

However, European pension funds may be taking a fresh look at their approach to defence, having received increased pressure to invest in recent months.

The EC's *Defence Industrial Strategy* stated that it would be reaching out to investors to "discuss their intensified participation, identify difficulties and find ways to stimulate private-sector engagement to support defence investments".

In November 2022, Dutch pension funds were called upon by the House of Representatives to invest more heavily in defence, with it claiming that investment in defence companies by the five largest pension funds in the Netherlands stood at just 0.1 per cent of total invested capital, while the government aims to increase the defence budget to 2 per cent of gross domestic product (GDP).

Meanwhile, in Denmark, its new defence financial framework largely points to public-private partnerships, "and this is strongly supported by the pension industry" the Danish trade association, Insurance and Pension Denmark, stated at the time.

"The broad agreement significantly expands conscription, which will of course also increase the need to build and upgrade barracks across the country. We are very positive about the fact that the agreement paves the way for public-private cooperation, where the pension

"PENSION FUNDS REALLY WANT TO BE AUTONOMOUS; THEY DON'T WANT TO BE PRESSURED INTO INVESTING IN DEFENCE FOR POLITICAL REASONS"

industry's experience and expertise in construction can come into play, said its CEO, Kent Damsgaard.

"I have no doubt that we as an industry can play a large part in ensuring proper conditions for our conscripts and defence employees. At the same time, we must of course deliver a reasonable return to Danish pension savers," Damsgaard added.

Growing investment?

According to the GABV, the financial sector invested at least USD 1 trillion between 2020 and 2022 to support the arms industry.

Tikehau Capital head of private equity, Emmanuel Laillier, explains that the global supply chain for defence was weakened by the Covid-19 pandemic, resulting in major original equipment manufacturers considering recurring price increases to their supply chains.

"This unique landscape, characterised by strong market demand and the rebalancing of profit pools across the supply chain, presents an excellent entry point for financial investors to invest in the European aerospace supply chain," Laillier says.

So, are European pension funds being tempted to increase their investment in defence?

"I would say that in the Nordics, the pension funds are much more in favour of investing in defence. In the Netherlands, it is much more controversial, the debate is more heated, and in Germany I think the pension funds are not moving very much into this direction yet," Leppälä suggests.

In 2022, Finnish pension insurance company, Varma, adjusted its *Principles of Responsible Investment* and started to apply enhanced ESG monitoring to defence investments.

"Investing *[in defence]* is possible if activities relating to controversial weapons (for example the manufacture, export and storage of the components of controversial weapons) account for a minor proportion (less than 5 per cent) of the company's activities, and if the primary purpose of the weapons is to prevent conflicts and defend the sovereignty of countries that have signed international arms control treaties," it stated in its *Annual and Sustainability Report.*

Responding to the Dutch Defence Minister's renewed calls in February for greater pension fund investment in defence, ABP, the fund for Dutch state and educational workers, said that the amount it invests in arms companies has increased in recent years.

"We do not invest in weapons that are banned internationally and we look at the risk, return, costs and sustainability of an investment," it added.

ABP said that companies must issue shares or corporate bonds in order for pension funds to be able to invest – and only then "if the conditions are right".

ABP CEO, Harmen van Wijnen, said: "If governments need money to finance weapons, they can issue a government bond that pension funds and other large investors can invest in. We are always ready for a constructive discussion on this with the Ministry of Defence."

Commenting at the time, Dutch pension fund PME chairman, Eric Uijen, also highlighted how it invests in defence, with certain conditions, and so "I therefore do not understand the recent statements by politicians and generals that pension funds are part of the problem in European defence".

Speaking in March about the EC's new defence framework, Insurance and Pension Denmark deputy director, Tom Vile Jensen, said: "We have made it clear that pension companies are welcome to collaborate with both the Danish Armed Forces and invest in the defence industry, but that it is entirely up to each individual company to decide… If politicians want to succeed in raising much more capital from private investors, further targeted initiatives in the EU and Denmark may be needed to create greater acceptance and understanding of the investments."

According to Leppälä, pension funds are requesting sound, long-term policies that provide investment opportunities for them to invest in defence.

"Pension funds really want to be autonomous; they don't want to be pressured into investing in defence for political reasons, but instead approach it from the risk/reward point of view and also from the ESG criteria they have," he adds.

Despite the increasing focus and pressure, and complex nature of the ethical debate, it seems pension funds need the freedom to decide for themselves whether they feel investing in defence would be part of the problem or part of the solution.

There have been many changes across Europe in recent years when it concerns the pensions landscape, but one subject has been particularly rearing its head to bellow its importance.

"It is," says Denton partner, Carolyn Saunders, "the emphasis on the importance of decumulation and recognising that it is as important as accumulation. It's knowing that people cannot be left unsupported when they're making complex decisions."

Talking about and working with the decumulation phases has been a subject taken up by both Amundi and PensionsEurope in reports released in December and October last year. PensionsEurope, in particular, looked at the issue in its *Good Decumulation of Defined Contribution Pension Plans Throughout Europe*, saying that increasing longevity and the cutting back of first-pillar pension provision on the continent was putting increasing weight on DC schemes when it came to the decumulation phase. It is up to these schemes, wrote PensionsEurope, to "provide appropriate solutions".

DECUMULATION

Drawing the future

A look at developments in the decumulation markets across Europe and potential future strategies for decumulation that countries could adopt

WRITTEN BY **PETE CARVILL,** A FREELANCE JOURNALIST

"In DC pension schemes," wrote Amundi in *Optimal Decumulation Strategies for Retirement Solutions*, following up on the subject, "there is no guarantee of pension payments after retirement, so it is important to develop appropriate decumulation strategies to efficiently convert wealth into income."

All of this comes within the general trend across Europe as country after country has moved from DB to DC provision.

"Europe is moving more in the direction," says PensionEurope secretary general, Matti Leppälä, "of DC and individual risk-taking. This means that the decumulation phase is becoming more challenging. We published a paper on this where we recognised the problem and said that the next biggest study will be around the decumulation phase and the challenges it represents."

He adds: "The emphasis has been on the accumulation period; we generally haven't thought about the decumulation process and what the options are."

A heterogenous Europe

The picture is also staggeringly different across Europe, with decumulation being various and varying mixes of people taking out lump sums or opting for annuities. Countries like Germany, Italy, and Spain have strong DB markets, with pensions largely being the remit of governments. Consequently, the DC sector in these nations is relatively underdeveloped. And weaker DC sectors mean that few people can be persuaded into buying an annuity as their pots of saved money are relatively low. Just one or two per cent of people in Italy opt for annuities, with the rest taking a sum from their pots.

Perhaps the biggest transition currently being undertaken is in the Netherlands, which is phasing its DB landscape into a DC one. Whatever happens in this relatively small nation will have huge ripples across the rest of the continent, as the country currently holds pensions assets worth 213 per cent of its GDP (the second-highest in Europe after Denmark at 233 per cent).

The new Dutch pension system is complicated, but aside from the switch to DC, a number of other measures are being put in place. These include the

introduction of three new types of DC scheme (a solidarity contribution scheme, a flexible contribution scheme, and a contribution-capital scheme that is only for pension insurers), flat-rate contributions, the lowering of a minimum age to enter the pension scheme from 21 to 18, the removal of the tax limitation on pension accruals (although it remains on the contributions), the treatment of net pensions almost equal to pensionable salary, and the requirement for transition plans.

That is a lot, but not all: The new act, introduced last year, also allows for partner pensions to be brought into line with current market practice.

"In the Netherlands," McKinsey senior partner, Cristina Catania, says "they have sizeable tax advantages: Contributions are deductible from current taxable income and both returns and capital are tax free. Moreover, from 2000, the government made mandatory for workers in many sectors the participation in a collective pension fund with the introduction of the Act on Obligatory Participation in an Occupational Pension Fund."

She went on: "At country-level, we observe an uneven level of maturity of the decumulation pension market. For example, the Dutch and Danish markets seem to be more mature (and less attractive for pension scheme providers) than the Italian or Irish markets. In fact, while in the first two countries the pillar II and III assets represent over 150 per cent of GDP (151 per cent and 192 per cent respectively) in Italy and Ireland the same ratio does not reach 30 per cent (11 per cent in Italy and 27 in Ireland)."

CDC schemes

One development in recent years has been that of collective defined contribution (CDC) schemes. In 2022, WTW outlined three main benefits of a CDC scheme. The first was that contributions are fixed, resulting in a more-sustainable system. The second was the expectation of higher levels of pension for a given contribution. Lastly, the firm said that the schemes are set up to do what a pension is typically expected to do – provide an income for life in retirement.

"The typical setup with DC schemes," says the company's senior director, Valentina Rocchi, "is to go for an annuity from the scheme or the insurer, along with some kind of lump sum. What's been coming out in the market – and what we haven't seen much of in the UK – are CDC plans, where there's a common, shared pool of assets from where the drawdown is paid out."

A CDC scheme is when both employers and employees pay into a collective fund. This will then pay an income in retirement but without the same guarantees of a DB scheme.

"Basically," says Saunders, "it is a DC scheme but the difference between the two is that a CDC will target a particular level of benefit, and contributions are calculated with that target in mind. If the scheme does well, the benefits can be increased above that target. And if they are doing less well, then they can be cut back. Nothing is guaranteed, but you hope that with the power in a large pool, you can beat the target with economies of scale."

Pensions Policy Institute policy analyst, John Upton, is more sceptical about CDCs: "There's a lot of hope that these will be a silver bullet," he says.

"WE GENERALLY HAVEN'T THOGHT ABOUT THE DECUMULATION PROCESS AND WHAT THE OPTIONS ARE"

"And there is a hope that they will replace the DB schemes that we can no longer afford, and it will stop pensions from being just a big pot of money where you have to make your own decisions about longevity versus a regular income for the rest of your life."

He goes on: "I think a lot of people pin a lot of expectations on CDC to replace DB with something that looks like it. It'll also remove a lot of these decisions from retirement. CDCs can also invest in riskier assets and possibly get more bang for the pension holder's buck."

The next few years are going to be interesting as Europe tries to contend with the fact that its populations are ageing. Shifts in the pension system will be one result of that.

"I think there's going to be a compromise," said Rocchi, "between annuities, duty-of-care protections, and total freedom. It'll be somewhere in the middle where there is some protection, but also freedom. That's where I see the market heading."

One question that remained unanswered is whether there is the political will to make tough decisions impacting on pensions. Certain aspects of pension provision, such as the UK's triple lock, are popular with voters and will be hard to abandon. For most parties in a fractured political landscape, it is likely that there will not be political capital or a determination to make such adjustments.

INTERVIEW

Championing financial planning and advice

Financial Planning Standards Board Ireland chief executive officer, Emer Kirk**, tells** Francesca Fabrizi **why accessible and ethical financial planning advice has never been more important**

Please tell us how you got into pensions/financial services?

■ My journey into pensions and financial services began 20 years ago with ITC, a pension company specialising in trusteeship and self-administered pension schemes. Armed with the QFA and working towards becoming a chartered tax adviser, I was drawn to the area of private wealth management. At ITC, the focus was on pension and tax planning, offering me invaluable experience working alongside financial advisers, tax consultants and their clients seeking greater control over their pension funds.

The year 2009 marked a pivotal moment for me, with the Financial Planning Standards Board (FPSB) Ireland launching the Certified Financial Planner® (CFP®) programme in Ireland and the Graduate Diploma in Financial Planning was introduced. Having been an advocate of lifelong learning and being eager to expand on my technical expertise in asset and risk management, as well as holistic financial planning, I was one of the first enrolled on the course. After graduating from the programme and attaining the CFP® certification, I joined Harvest Financial Services, a boutique wealth management firm where I specialised in long-term financial planning advice, particularly for clients from the point of retirement, until moving to my current position.

You are currently CEO of the FPSB Ireland. Please tell us more.

■ FPSB Ireland is committed to promoting a future where consumers understand the significance and advantages of the financial planning process. We envision a scenario where consumers can readily identify financial planners who adhere to competency and ethical standards, always prioritising clients' interests.

To this end, FPSB Ireland plays a crucial role in establishing, upholding, and promoting professional standards in financial planning, to advance financial planning as a profession with CFP® marking the global standard of excellence. CFP® professionals adhere to the highest fiduciary standards ensuring that clients receive advice of the utmost quality and integrity. Currently there are over 223,000 CFPs worldwide, with almost 1,000 in Ireland.

And we know that many Irish consumers are recognising that long-term financial planning is a good thing. The 2023 FPSB global consumer survey on the value of financial planning found that, across the 15,000 consumers surveyed (1,000 Irish consumers), people who work with financial planners unlock benefits beyond wealth, reporting a better quality of life, enjoying more financial confidence and resilience and are more satisfied with their financial situation.

What are your aims in this role?

■ Looking ahead, my vision for this role is rooted in accessibility and quality. We aim for a future where anyone seeking financial planning advice can readily access it, regardless of their stage in life of financial circumstances. From young professionals entering the workforce and contemplating retirement

savings and homeownership, to seasoned individuals planning their golden years, comprehensive and ethical financial planning advice should be within reach for all.

Over the coming year, a key focus for us will be to conduct and release research exploring the benefits to employers of integrating financial planning onto their core employee benefits package. The research will look into the tangible advantages experienced by firms, including better financial resilience among employees and enhanced retirement preparedness. By quantifying the positive impact of financial planning on workforces' well-being and performance, we aim to empower employers to prioritise and invest in comprehensive financial wellness initiatives, nurturing a more secure and prosperous future for both employees and employers alike.

How have you seen the pensions/ financial services sector change since you started out?

■ Without doubt, the landscape of pensions and financial services has undergone significant transformations since I started my career. The transition from defined benefit (DB) to defined contribution (DC) pension schemes, and the responsibility to fund retirement shifting on to the individual.

Alongside that, the demographic trend of people living longer and evolving complexities around home ownership means that for retiring clients, considerations now extend beyond pension funds to encompass mortgage debt, intergenerational wealth transfer, and long-term healthcare arrangements. Understanding clients' individual goals and objectives and their behaviour and attitudes towards money ensures the best outcomes. Recognising this, FPSB's Global Financial Planning Standards have been updated to include the psychology of financial planning as a guiding framework for CFPs in their advice to clients.

What are the biggest challenges and opportunities in pensions/ financial services in Ireland?

■ There will be as many challenges as opportunities in the Irish pensions and financial services sector over the coming years, so I'll touch on just a few. Foremost among the challenges is the impending introduction of auto-enrolment, which is set to increase retirement savings participation. Its implementation will pose logical and compliance hurdles for employers and providers alike.

And while it promises strides towards pension coverage, it does not address the issue of pension adequacy. A critical gap exists in private sector pension funding for DC savers between what they have and the lifestyle they aspire to in retirement. There is challenge and opportunity in igniting this conversation and rallying efforts towards securing financial stability in retirement for all individuals.

Moreover, the trend of longevity highlights the importance for accessible financial advice. For those potentially navigating a 100-year life, the provision of tailored financial advice is not a luxury but a necessity, offering guidance to enhanced financial well-being and security in an uncertain future.

The government's commitment to improving financial literacy through the National Financial Literacy Strategy presents a unique opportunity for the financial services sector. By equipping individuals with the knowledge and skills necessary to make informed financial decisions, these initiatives not only advance a culture of financial responsibility but also promote consumer confidence and trust in the financial system.

Collaborative efforts between government, financial institutions and educational institutions can further strengthen the impact of these programmes, paving the way for a more financially resilient society.

You co-founded the Connect Women in Pensions Network in 2013 – please tell us about this.

■ In 2013, I had the privilege of co-founding the Connect Women in Pensions Network, which is a platform dedicated to empowering and advancing women within he pensions industry. Through networking events, mentorship programmes and advocacy efforts, the network aims to foster a supportive community where women can thrive, exchange ideas, and overcome barriers to career advancement. Our mission is to promote gender diversity and inclusivity, ultimately shaping a more equitable, diverse and vibrant future for the pensions sector.

Any key messages you would like to leave with our readers?

■ The pension and financial services landscape has transitioned significantly over the past 20 years, I'm sure the next 20 will be just as transformative and challenging. As we navigate changes in pension structures, regulatory landscapes and societal changes, the need for accessible and ethical financial planning advice has never been more important. FPSB Ireland is committed to advancing the profession through rigorous standards, research initiatives and advocacy efforts as we strive to shape a more resilient and inclusive financial landscape and a future where individuals of all backgrounds can achieve financial security and well-being.

You can find out more at: www.fpsb.ie.

FINANCIAL LITERACY

Getting the message

Across Europe, a lack of understanding of pensions could create significant financial difficulty in future, for individuals and for national governments. David Adams **looks at how this problem, a symptom of low financial literacy in general, is being addressed across Europe**

In 2023 only 42 per cent of EU consumers were confident they would have enough money to live comfortably throughout their retirement, according to the European Insurance and Occupational Pension Authority's (EIOPA) 2023 Eurobarometer, which surveyed 29,000 consumers across the 27 EU member states.

A 2022 UK government survey into engagement with pensions among workplace pension scheme members found attitudes to pensions "were characterised by detachment, complacency and fear".

A lack of pensions knowledge also reflects a wider problem with financial literacy. Many governments and pensions industry bodies now run extensive publicity programmes to improve financial literacy and engagement with pensions. Examples include 7 Jahre länger (Seven Years Longer) in Germany, which uses the fact that most people underestimate life expectancy to make them think about how much money they might need in old age.

Messaging may focus on specific national issues. In the Netherlands, changes to the pensions system mean that while most workers are members of a second pillar occupational scheme, most of those schemes will become defined contribution (DC)-based. Wijzer in geldzaken (Money Wise), a platform backed by the government, financial services providers, and industry bodies, provides Dutch citizens information on many financial topics, including pensions. The organisation also works on the Pension3Days, an awareness-raising initiative that has been running since 2011, with participation from employers, pension providers and other financial services companies.

Wijzer in geldzaken spokesperson, Jelle Strikwerda, says one of the most important issues it tries to address is raising awareness around the wide variation in contributions to occupational pensions arranged by employers. "Not enough people are aware of this," he says. "People just think, 'my company is responsible for getting me a good pension.'"

Wijzer in geldzaken's own research shows that overall understanding of and engagement with pensions in the Netherlands has improved during the past decade; and that individuals engaged by these campaigns are almost twice as likely to engage more actively with their pensions.

Reality check

But awareness-raising campaigns are one thing. Arguably the best way to link these issues to peoples' own circumstances is to let them use a pensions dashboard, or pension tracking service, to see (ideally) any defined benefit (DB) and/or DC entitlements or savings from all three pillars of the pensions system.

Examples include Mijn Pensioen Overzicht (My Pension Overview), in the Netherlands, which is backed by the pensions and insurance industry and the Dutch national insurance scheme. In Norway, Norsk Pensjon, a not-for-profit company owned by seven insurance companies also offers consumers a view of pension entitlements from all three pillars.

The organisation also works closely with schools and universities to help improve general financial literacy in the country. Yet despite this, Norsk Pensjon CEO, Trond Tórstadt, admits that "pensions are a low interest issue in Norway, like in other countries".

"I think maybe it's because Norway has quite a good economy, so you don't have to worry about pensions so much as in other countries," he says. "And you get quite a lot from the first pillar."

However, recent reforms in Norway have increased the state pension age, with younger people now likely to have to wait until they are in their 70s to receive a first pillar pension; and the system is making more use of DC arrangements.

In Italy there is a need to encourage more saving in the second pillar. Historically, the country had a DB-based state pension but with the first pillar now DC-based, participation in the additional, voluntary occupational system has become more important.

This change is not yet widely understood, Mefop member of the department of economics and finance, Antonello Motroni, says. Participation in occupational schemes is still relatively low, at around 30 per cent in 2022, according to EIOPA, and is often linked to trade union membership.

Mefop runs online services called Sono Previdente (I'm farsighted) to improve understanding of the pensions and welfare systems in Italy. The Italian government has recently passed new legislation to introduce more financial education, including retirement planning, to schools. Each October in Italy is also dedicated to financial education, with financial services providers and other institutions involved in campaigns and publicity activities across the country.

Another government-backed online tool, Quello Che Conta (What Matters) offers tools and resources to help people understand the pensions system and make long-term financial plans, while a social security dashboard provides a projection of an individual's likely retirement income from the first pillar.

Cutting through

In Sweden, online access to retirement income projections, via the minPension platform, has had a noticeable, positive impact, says Swedish Pensions Agency research director, Ole Settergren. By 2022, 59 per cent of all pension savers in Sweden knew how to find out what their future pension income might be, with that percentage rising to 73 per cent of those aged 55 to 65, according to the agency's figures.

Sweden's system is relatively generous, because the first pillar has several different DB and DC-based components and there is very broad coverage through occupational pensions (about 90 per cent of eligible workers in 2023).

"In general, the compulsory savings through the public pension plan and the occupational pension plans that are semi-compulsory make pensions sufficient," says Settergren. "However, what's true on a general level is not necessarily true on an individual level."

These issues also become more urgent at specific moments during peoples' lives, such as when someone needs to choose how to use DC savings. For many consumers it may be difficult to access or afford expert financial advice. But there is evidence that free or affordable financial guidance services can have positive results. Recent research in the UK by Standard Life found that more than six out of ten people who had accessed free guidance agreed this had helped them to make better financial decisions and understand complex financial issues.

Pensions Policy Institute (PPI) senior policy researcher, Lauren Wilkinson, believes employers have an important role to play too, possibly through financial wellbeing services for employees. She also likes the concept of a pension champions in the workplace: a member of staff who undertakes training with the employees' pension scheme provider, then becomes "the first port of call for other employees".

In the end, says Settergren, whatever effort is put into the financial education of pension savers, policymakers and providers must stay focused on achieving the best outcomes for members.

ARTIFICIAL INTELLIGENCE

Ask the industry:

As the EU became a step closer to introducing the world's first artificial intelligence (AI) regulation in March when MEPs approved the law, *European Pensions* asks: What impact will the AI Act have on the European pensions industry? Do you see AI as a help or hindrance to pension innovation?

In a Danish context we see the introduction of AI regulation as a positive step. As opposed to i.e. the General Data Protection Regulation (GDPR), the risk-based approach in the AI-act is a positive difference, if we manage to focus requirements on 'real risk'.

While finishing the act at political level proved a challenging process, an even bigger challenge lies in ensuring sensible implementation in the coming months. To avoid unnecessarily stringent rules that could undermine the initial risk-oriented approach, it's crucial to maintain the risk-based approach when the AI-act is cemented in standards and guidelines. Striking this balance is key. If successful, the regulation will effectively address genuine risks without imposing unnecessary barriers.

However, history warns us. We have too often seen this balance tip during implementation, leading to an implementation that imposes too stringent requirements relative to the risks it is meant to mitigate; in essence adding unnecessary burdens. In such cases, the regulation could inadvertently hinder innovation in the industry.

Adding to the complexity, implementing the AI Act is that it is in the hands of several players. Even without the challenge of maintaining the initial risk-based approach, just having so many players results in real risks of creating an uneven playing field across the EU.

SIGRID FLOOR TOFT
Insurance and Pension Denmark deputy director

We see the AI regulation as a positive development. It standardises the rules governing AI, drawing many parallels with the General Data Protection Regulation (GDPR) framework. This alignment is practical, as the GDPR has been well-established for some time, and we, along with other companies, have already developed effective governance around it. However, uncertainties remain in interpreting the regulation, and there is still much to learn, adjust and prepare for – for example, assessing to what extent our current and future AI systems within the Finnish pension industry should be considered high risk.

Additionally, it is essential to integrate technological and legal considerations into a cohesive framework to ensure effective and manageable governance under the AI Act. We must also ensure that all requirements of the AI Act can be efficiently implemented across various technology layers and business processes while maintaining minimal bureaucracy and fostering a shared understanding of the Act's objectives.

MIKKO PAKARINEN AND MAIJA NIKULA
Ilmarinen senior legal counsel and director digital transformation & cyber security

We believe that the adoption of AI may lead to better investment outcomes for members, as well as a potential reduction in costs on the back of an increase in efficiencies, though we do expect the expanded use of AI across pension funds to be a longer-term evolution. More broadly, AI has huge potential to improve the operational aspects of pension systems, by analysing data more quickly, improving accuracy, highlighting future risks, reducing costs, improving communication, and reaching members in a more personalised way.

This should provide individuals with a much better experience. Member engagement in pensions is something many schemes have struggled with and the use of AI could lead to significant improvement in member engagement. A live and developing example currently used by multiple leading pension plans is the development of chatbots, but AI could be used to tailor the language used with pension plan members to ensure that it's relevant for individuals and their level of understanding.

EIMEAR WALSH
Mercer European head of investments - wealth

Good laws are usually drafted slowly by experts, without undue rush. Sadly, the European Union AI Act has all the hallmarks of mediocre legislations passed hurriedly: A knee-jerk reaction to the sudden appearance of ChatGPT.

The European Parliament seems particularly proud of having passed the 'first-ever legal framework on AI', as if overregulation on the old continent could hide the fact that, in reality, AI innovation is made primarily by non-European companies in the United States and China. Put simply, it's an illusion to believe one can 'regulate' products or services made by others.

The EU law's requirements are rather vague, and subject to arbitrary interpretation at national and/or industrial sector level, and the enforcement mechanisms are practically non-existent, save for the future establishment of a European AI Office in charge of boosting consumer trust etc.

When it comes to pension products and other financial services, the deployment of AI tools will simply further automatise things: destroying tens of thousands of jobs in banking, financial planning, and pension advice in the process, but I'm not sure it will unleash a new wave of pension innovation.

NICOLAS J. FIRZLI
World Pensions Council executive director

The possibilities presented by AI in the pensions industry are far reaching. Imagine an AI assistant that sorts through your emails, reviews, and challenges advice, and drafts preliminary responses? Imagine a tool that facilitates making tailored investment decisions and monitors the outcomes in real time? Imagine personalised customer interactions tailored to an individual's needs, that seamlessly connects to a human call handler at the right time?

But there's a catch: The importance of trust, clarity and accuracy in such solutions is so critical it can be a barrier to such innovation, particularly in an industry which for many – public and managers alike – is complex and often hard to engage with. The provision of clear guardrails, through the AI Act, establishes a framework that should encourage innovation precisely because it aims to ensure that the technology is developed ethically and transparently, which will go a long way to engender greater trust.

DOMINIC MAKEMSON
Aon associate partner

In their own words...

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

On developments in the decumulation markets across Europe

"At country-level, we observe an uneven level of maturity of the decumulation pension market. For example, the Dutch and Danish markets seem to be more mature (and less attractive for pension scheme providers) than the Italian or Irish markets. In fact, while in the first two countries the pillar II and III assets represent over 150 per cent of GDP (151 per cent and 192 per cent respectively) in Italy and Ireland the same ratio does not reach 30 per cent (11 per cent in Italy and 27 in Ireland)."

Cristina Catania, McKinsey senior partner

On concerns over IORPs' penetration

"The estimated penetration rate of IORPs [continues] to be low when compared to the country GDP. The Netherlands, whose holdings represent more than 153 per cent of the country's GDP, emerged as an outlier as a result of a strong dependence on IORPs as the vehicle for occupational pensions. The vast majority of those employed in the Netherlands participate in an occupational pension scheme via schemes provided by IORPs, and this form of savings is also attractive... as it is tax favoured."

EIOPA spokesperson

On European pension funds facing increased pressure to invest in defence

"Pension funds really want to be autonomous; they don't want to be pressured into investing in defence for political reasons, but instead approach it from the risk/reward point of view and also from the ESG criteria they have."

MATTI LEPPÄLÄ
PensionsEurope CEO

On the importance of accessing financial planning advice

"As we navigate changes in pension structures, regulatory landscapes and societal changes, the need for accessible and ethical financial planning advice has never been more important."

EMER KIRK
Financial Planning Standards Board Ireland chief executive officer

On ageing populations

"Ageing populations put a lot of stress and pressure on the traditional pay-as-you-go systems for most social security systems and so we're finding increasingly that people need supplementary savings."

Jerry Moriarty,
PensionsEurope chair

On reforming Spain's public pension system to ensure its sustainability

"The current distribution model, based on the principle of intergenerational solidarity, faces critical challenges due to an ageing population and one of the lowest fertility rates in the world. We will have to see how the macroeconomic variables evolve, but every indication, including the recent opinion of the EC, suggests that additional measures will be necessary, including possibly on the expenditure side too."

RAFAEL VILLANUEVA
WTW Spain Retirement associate director

On Norfolk Pension Fund's class action success against Apple

"We were able to reach the proposed settlement and overcome the defendant's often scorched earth defence tactics by being tenacious, focused and determined to invest whatever resources necessary in both our lawyers' time and capital outlay to optimise the outcome."

MARK SOLOMON
Robbins Geller Rudman & Dowd co-founder and partner

On introducing auto-enrolment pension saving in Ireland

"Pension experts are struggling to provide clear advice to employers amidst this uncertainty and in turn employers are struggling to prepare for the imminent launch date while ensuring adequate resources and upskilling initiatives are in place."

Caitriona MacGuinness, Mercer Ireland DC and private wealth leader

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