Sustainable pensions: do you have to give up on doing well by choosing to do good?

Ethical investing is not a new phenomenon, but its popularity is growing

Ethical investing often includes green initiatives © Getty Images

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I started thinking more intently about my pension recently, offhandedly wondering where exactly my contribution travels after it comes out of my pay cheque each month.

I asked my friends – fellow young professionals in their late 20s and early 30s – whether they had any knowledge of their own funds. The answer was a resounding "no", and that, like me, they contribute blindly each month and leave the specifics to the experts.

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There's a prevailing sense that many young people tend to be conscious of where their money goes and what it supports. So, it stands to reason that that cohort – as well as many of their seniors – are hoping to take the same care with their pensions, and ensure their contributions are invested in companies that reflect their personal values. But is it common, and even more importantly, is it feasible?

Seeking greater visibility of where pensions are invested and whether the answer reflects personal values is no longer confined to a small group of ethically motivated investors, says Rav Vithaldas, EY Ireland pensions assurance leader, rather "it has become a mainstream consideration for many savers".

"Far more options are available now, and most major pension providers offer some form of sustainable fund. The problem is that the quality varies enormously. A fund having 'ESG' or 'sustainable' in its name doesn't necessarily mean it avoids industries such as fossil fuels, weapons or tobacco. In our experience, genuinely sustainable options are available, but you often have to look under the bonnet to find out what they invest in," Ethico's Ciarán Hughes said.

I began by logging into my workplace pension portal, to get an overview of my portfolio and funds. It took quite a lot of acronym deciphering to understand, but I learnt that a significant portion of my pension is in bonds, and another portion has a sustainability focus already, at the very least.

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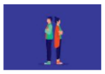
4 
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Ciarán Hughes © Ethico

At present, I have my pension set up so that the provider takes care of it for me, though I am also given the option of taking more control. Within the portal, I was terrified of accidentally clicking on that option, lest I suddenly be handed the keys to my extremely modest financial kingdom.

It immediately became clear that getting a more comprehensive look at the specific funds and their focus or exclusions – never mind taking a more front-seat approach to the operation of my pension – would mean a steep learning curve and a time commitment I think many would be hesitant to give.

> *Your pension contributions are invested in real companies, so where that money goes and what it supports matters*

But it's worth at least investigating where the money goes, Mr Hughes advises.

"Most people think of a pension as money sitting in an account somewhere, but it isn't. Your pension contributions are invested in real companies, so where that money goes and what it supports matters. Someone might spend considerable time, money and effort reducing their personal carbon footprint, while unknowingly having a much greater negative impact through a pension invested heavily in oil, gas and other high-carbon industries," he said.

"You don't need to become an investment expert, but it is worth spending some time with an expert to understand where your pension is invested. For many people, their pension will ultimately be one of the largest financial assets they ever own, so it makes sense to know what your money is funding while it is working towards your retirement."

There are some practical limitations to aligning pension savings with an individual's personal values, Mr Vithaldas says.

Rav Vithaldas © EY Ireland

"First, it's important to recognise that terms such as 'sustainable', 'responsible' and 'ethical investing' can mean different things to different providers and investors. As a result, two funds with similar labels may apply very different criteria when deciding which companies to include or exclude," he said.

"Second, placing significant restrictions on the range of investments available can reduce diversification and may affect long-term investment performance. Investors therefore need to balance their personal preferences with their retirement objectives.

"Third, sustainability data and fund classifications are not always consistent, and concerns about "greenwashing" have led to increased regulatory scrutiny.

"European regulators have introduced measures to improve transparency and standardisation, including ESMA's [the European Securities and Markets Authority] fund-naming guidelines and ongoing reforms to sustainable finance disclosure requirements."

But it is possible, Mr Hughes says, adding that getting financial advice is recommended as pensions in Ireland "can be complicated".

"You can tailor a pension quite significantly. A good place to start is with a simple question: what do you not want your money invested in? For many of our clients, that means avoiding industries such as fossil fuels, weapons and tobacco," he said.

"From there, you can look at increasing exposure to areas such as renewable energy, healthcare and sustainable infrastructure, while also using your position as an investor to encourage better environmental, social and governance standards in the companies you continue to own. But sustainable investing shouldn't mean forgetting the fundamentals. It is still your pension, so diversification, risk, charges and long-term returns remain extremely important."

That is the important balance. "While pension savers generally have more choice than ever before, achieving a perfect alignment between investments and personal values is not always possible or practical. In many cases, some compromise is required between reflecting individual preferences and maintaining a well-diversified portfolio designed to deliver long-term retirement outcomes," Mr Vithaldas added.

A few straightforward questions asked of your provider can give valuable insight into how a pension is invested, says Mr Vithaldas, outlining some examples of what to ask for:

- What is my pension invested in? For example, what is the mix of shares, bonds, property, cash and other assets, and what is the geographical spread?
- Is the default fund the most appropriate option for me, or are alternative investment choices available?
- What level of investment risk am I taking, and is it suitable for my age, circumstances, and retirement goals?
- Are ethical, sustainable or responsible investment options available?
- What fees and charges apply to the different investment options?

- How has my fund performed over the long term, and how does that performance compare with its stated objectives?
- What retirement income or benefits can I expect? Members should request projections and understand the assumptions used, including investment returns, inflation, contributions and charges.

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