CASE STUDY

Smart Pension Master Trust

The IMPACT INVESTING PRINCIPLES *for* PENSIONS

Smart Pension

PENSIONS FOR PURPOSE

What are

The Impact Investing Principles for Pensions?

The Impact Investing Principles are a practical guide to impact investment and provide four concrete steps pension schemes can take to pursue an impact investing strategy – *see figure*.

Drawn up to meet the growing need for best practice guidelines on how to set, implement, review and measure an impact investment strategy, The Principles were designed by the *Impact Investing Institute* in partnership with *Pensions for Purpose* in consultation with leading practitioners and with input from stakeholders including pension funds, investment consultants and managers as well as member associations.

Increasingly pension schemes want to reduce negative impacts and risks that arise from carbon emissions, biodiversity loss, poor governance and inequality, which affect their portfolios. Pension funds are interested in investment opportunities that have a positive impact on the environment and society, and also secure a competitive financial return. The Principles make it easier for pension schemes to reach that goal.

The Principles were designed to be dynamic and to reflect the fast-evolving nature of impact investment. Pension schemes already working with the Principles participate in *Pensions for Purpose's* Community, a peer-learning platform that shares relevant resources and hosts events. This group, along with other initiatives and partnerships, provides evidence-based feedback to ensure the Principles remain cutting-edge and responsive.

Smart Pension Master Trust (SPMT)

We spoke to James Lawrence, Director of Investment Proposition at *Smart Pension Master Trust* to compile this case study

Fund facts, November 2023

Assets under management (AUM): **£4bn**

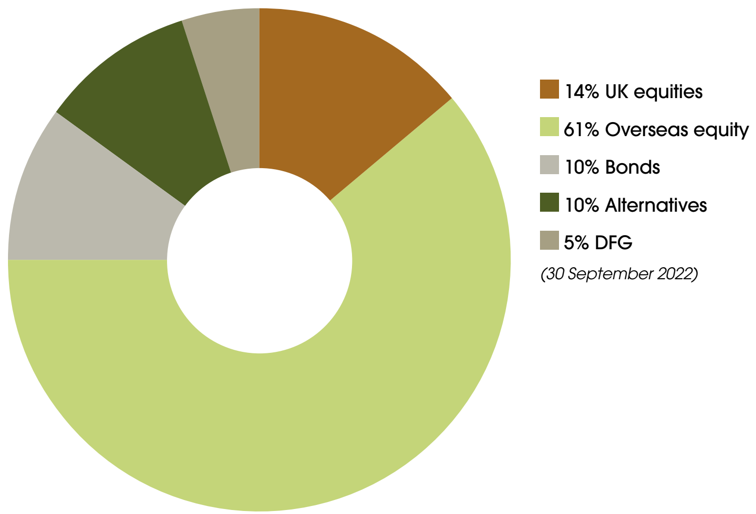
Employers represented: **70,794**

Number of members: **1,400,000**

Impact journey facts:

- Embedded The Principles into responsible investment policy.
- At the end of 2022, increased impactful investments with two new fund managers for biodiversity equities and green bonds, as well as a 20% allocation to specific climate transition equities managed by *J.P. Morgan*.
- The *AXA* Biodiversity Fund aims to take advantage of alpha return opportunities and mitigate biodiversity loss by investing in best-in-class companies offering innovative solutions to address issues such as pollution on land and water.
- The *Mirova* Global Green Bond Fund aims to contribute to the low-carbon transition, making a twofold impact: financial and environmental.

Fund's asset allocation



Impact Investing Principles for Pensions

Smart Pension

How did you get buy in for impact from trustees?

Across the organisation, we felt impact investing represented the future of investment, particularly for defined contribution (DC) funds. Alongside providing strong long-term returns, we believe it is important to deliver a positive impact with the money we have been entrusted with. Impact investment fits our goals well. Fortunately, our trustees were aligned with us on this approach, as were our investment consultants, who were at the forefront of our impact thinking. David Brown also influenced us, due to his association with *Pensions for Purpose*, and the *Impact Investing Institute*. Interestingly, at the outset, member interest was lower – this is now changing as members are increasingly concerned about their pension's impact.

Why did you choose to use The Principles?

The framework is a useful way to integrate impact considerations into our investment and engagement strategies, managing financial risks and associated issues such as climate, biodiversity, poor governance and inequality. The framework has been useful to help us align our investments with our values and carry out 'gap analysis' to monitor our progress towards achieving these values.

We have embedded The Principles into our own Responsible Investment (RI) Policy and impact investing framework. The policy now explicitly states we aim to identify sustainable companies and capture investment opportunities offering solutions to environmental and social challenges provided they are aligned with the investment objectives and strategy of our fund offerings. When assessing opportunities for new investments, we also use the *United Nations' (UN)* sustainable development goals (SDGs) and the *UNs' Principles for Responsible Investment's (UNPRI)* investing market map, which aim to bring more clarity to the process of identifying mainstream impact investing companies and thematic investments so asset owners and fund managers can assess better opportunities in this market.

How have you progressed with each Principle?

Set impactful objectives

1

We use frameworks and regulations to evolve our impact investment beliefs, which are outlined in our Responsible Investment Policy, along with our objectives. As mentioned, the SDGs and the *UNPRI's* impact investing market map help create an investable universe of impact investments. The trustee supports the recommendations from the *Taskforce for Climate-related Financial Disclosures (TCFD)* and reports yearly on the climate profile of the default funds, the carbon footprint of members' investments, and our responsible investment and stewardship activities, as we are a signatory of the *UNPRI* and the UK Stewardship Code. These reports summarise and monitor the activities of all our assets, including our impact allocations. As well as this, they have influenced the changes made to our RI, climate and nature, and voting and engagement policies.

All our policies, which include our objectives and beliefs in relation to responsible and impact investing, are reviewed on an annual basis. In addition, we disclose our activities annually in our *PRI, TCFD* and Stewardship Code reporting.

Document impact objectives – our impact goals are documented in our RI Policy, which is available online and signposted in our Statement of Investment Principles (SIP). Impact objectives have been embedded in our wider responsible objectives. Some of these beliefs are:

- ESG, including climate risks, poses a real and material threat to retirees' outcomes. Generating an appropriate and sustainable financial return for members while also addressing global challenges helps mitigate these risks.
- Responsible investment factors influence long-term performance presenting opportunities and risks. Each stage of the investment decision process: investment strategy, investment selection and reporting, must consider ESG climate risks.

Consider stakeholder views – all material changes to policies pass through relevant sub-committees and then the main board of trustees. They are also presented to the Founder, at regular strategy meetings. Views from this process are taken into account before changes are finalised. The *Smart Pension* investments team works collegiately with all parties, including investment advisers, to ensure the investments are as impactful as possible.

Member views are considered through webinars, surveys and ad-hoc requests. We have taken into account member views in recent changes, for example, adding a fossil-fuel free fund to our range. In 2022, we surveyed our members about investing responsibly, sustainably or even with impact. The results helped determine the language used to communicate to members, the types of exclusions members are interested in, and the flexibility members do and don't want. While there is a long way to go in members' understanding of pensions, and in particular impact

How have you progressed with each Principle? *continued...*

1 Set impactful objectives *continued*

investing, it was useful in reframing how we approach this with our members and the types of investments we make.

Target positive social and/or environmental impact opportunities – within our default growth fund, the *Smart* Sustainable Growth Fund, where the majority of members are invested, we allocate 13% to impact strategies. These are the *AXA* Biodiversity Fund and the *Mirova* Global Green Bond Fund. The remainder of the fund is allocated to sustainable funds, which are Article 8 or 9 (or equivalent) under SFDR.

Additionally, all other funds our schemes offer have ESG-integration, with the exception of two; the gilt fund and the Shariah fund. These include our Sustainable Growth Plus Fund with a 60% allocation to impact strategies, and two standalone impact equity and impact bond funds. We are targeting as much as possible to positive impact opportunities.

Impact investment examples – our impact allocation aims to strengthen risk management and returns. The *AXA* Biodiversity Fund aims to take advantage of alpha return opportunities and mitigate biodiversity loss by investing in best-in-class companies offering innovative solutions to pollution on land and water, land degradation, sustainable materials and recycling. The *Mirova* Global Green Bond Fund aims to contribute to the low-carbon transition while making a financial and environmental impact.

2 Appoint investment consultants & managers with impact integrity

Consultants and investment managers bring new strategies and ideas for the *SPMT* in-house investment team and trustee to consider. Our investment consultant will be present at any meetings discussing the impact allocations, new manager presentations to provide financial advice on the allocation to impact strategies.

We have bi-weekly meetings with our investment consultant and engage with our managers as needed. Managers are also formally reviewed and invited to trustee meetings at least annually. Our SIP, RI, climate and nature, voting and engagement policies are available and provided when updated. These policies are also critical when appointing new managers (and consultants).

Investment consultants embedded impact at the strategic asset allocation level, providing us with Section 36 investment advice on the suitability of our allocations to impact strategies and adding 13% to impact strategies within our default.

In line with the *Investment Consultancy and Fiduciary Management Market Investigation Order 2019*, we have set strategic objectives for our investment consultants and review them annually. If these are not met, this could lead to a formal review of our investment consultant appointment. For our investment managers, we have an escalation procedure set out in our oversight policy.

How have you progressed with each Principle? *continued...*

Use your voice to make change

3

Our voting and engagement policy sets out how we implement our objectives in our Responsible Investment Policy. These objectives include our impact strategies and how we pay particular attention to the SDGs, by categorising opportunities through the *UNPRI's* impact investing market map.

We review our investment managers' stewardship activities and performance against our priorities in our annual stewardship report. As mentioned, we have an escalation procedure, set out in our oversight policy. We would be able to reduce, or remove, their allocations if they were not meeting our expectations or standards. Engagement with industry groups or initiatives on stewardship include *ShareAction* and *ClimateAction 100+*.

We have also carried out member surveys in the past to gain an understanding of members' views or priority of certain issues and topics. We also engage with members in other ways:

- The trustee mailbox is open for members to send feedback.
- Active monitoring of member behaviour including self-select fund choices.
- We also created a member-friendly *TCFD* report, which has received positive feedback from consultants and *DWP*.
- We have webpages for our impact allocations and videos on renewable energy and biodiversity.

Our members have varied views. While we consider them as a 'gap analysis', no investments are changed solely on these views.

Manage and review your impact

4

Physical and transition risks are assessed through carbon footprint, climate scenario and temperature-alignment analysis by the trustee. Our analysis adheres to guidance for schemes on climate governance and *TCFD*, produced by the *Pensions Climate Risk Industry Group*. We assess our impact by considering the objectives and investments of our funds, through climate metrics and exposure to the SDGs. As set out in our SIP, we choose fund managers with policies for managing financially material considerations. We are working with our managers to assess our portfolio's exposure to deforestation. We use our impact investing framework to identify impact investing gaps, through the *UNPRI's* impact investing market map.

Managers are challenged directly by the trustee and their investment consultant on the impact of anything significant including, where appropriate, ESG issues that may affect the prospects for return from the portfolio, as well as backwards and forward-looking voting activity.

Next steps – We are assessing our exposure to commodity-driven deforestation and how we can reduce our negative impact while supporting natural capital. New asset classes on our agenda are green infrastructure and private equity, offering impact opportunities and improved risk-adjusted returns. Given limited resources and capacity, we are looking at how we can work with our consultants to integrate this into our reporting cycle.

“The framework has been useful to help us align our investments with our values and carry out ‘gap analysis’ to monitor our progress towards achieving these values.”

James Lawrence

DIRECTOR OF INVESTMENT PROPOSITION, SMART PENSION

PICTURE CREDIT: LUÍS EUSÉBIO, UNSPLASH

“Smart’s clear and powerful philosophy around ‘ESG, including climate risks, posing a real and material threat to retirees’ outcomes’ is incredibly powerful and demonstrates that fiduciary duty is no barrier in recognising ESG and impact in a pension fund investment process.”

Charlotte O’Leary

CEO, PENSIONS FOR PURPOSE

WEBLINK
Find out more about the Principles

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