



Aon Investment Research 2020

Covid, climate and compliance— are you ready for the new investment challenges?

Focus on investment governance

Contents

Foreword	3
About the research	3
Aon insight	4
Could Covid-19 change scheme governance forever?	5
Looking to the longer term	7
The shape of investment decision-making	9
Contacts	11
Further reading and resources	11

Foreword

2020 has been a year of significant change for UK pension schemes' investment strategies — even before we take the effects of the COVID-19 pandemic into account. Governance has come under ever-greater scrutiny from The Pensions Regulator, responsible investment is rising rapidly up the trustee agenda, and pension schemes are demanding ever greater cost transparency from their providers.

Over the summer, we set out to listen and to understand how investment decision-makers were responding to all these changes and accompanying challenges. Through a series of in-depth interviews, we were able to gain real-world insights into key trends, common approaches — and differences — to paint a picture of current thinking in pensions investment.

Inevitably, the pandemic was a common thread running through all the discussions. And, while it's still too early to understand its longer-term effect on schemes and markets, the crisis has already started to reshape investment strategy decisions and the way these are made.

Now, more than ever, investors need support to continue to protect the retirement income for their members and to manage the increased pressure and demands on their investment governance and operational strategies. We have specialist teams and deep expertise to help you to rise to all these challenges — from governance, responsible investment and investing for the endgame to costs and transparency and the DB funding code of practice.

We look forward to continuing the discussion with you.



Emily McGuire
Partner, Aon

About the research

In July and August 2020, Maggie Williams, an experienced pensions commentator, writer and editor, carried out in-depth interviews with 20 pension scheme decision-makers on behalf of Aon. Interviewees were drawn from a wide range of disciplines — professional, independent and member-nominated trustees, third-party evaluators and pensions managers — representing both defined benefit (DB) and defined contribution (DC) schemes. Scheme sizes ranged from a £10 million defined benefit scheme, to over £10 billion.

The interviews focused on five key areas:

- Investment governance
- Responsible investment
- Investing for the DB endgame
- Costs and transparency
- Investment implications of the DB funding code of practice

Our thanks go to everyone who took the time, during very difficult and challenging circumstances, to participate in this research and to provide valuable insights.

Aon insight

Investment governance



Prior to COVID-19, trustees of both DB and DC schemes were facing an increasing governance burden, brought on by a raft of new regulations and compliance requirements. The pandemic further added to this burden and tested governance processes to their limits. The economic crisis demanded fast decision-making, and even faster action, to rebalance investment portfolios – at a time when Boards were quickly reorganising the day-to-day running of their schemes. As a result, investment decisions are now made very differently: shorter, more frequent and focused remote meetings have replaced the pre-pandemic quarterly meeting schedule.

For some, this change has enabled much nimbler decision-making, and those schemes with more resources and sufficient resilience built into their investment strategies have fared well. Conversely, schemes with relatively limited resources experienced a more challenging time and often lacked access to the full range of investment strategies needed to navigate a crisis.

It is interesting to observe the comments by some interviewees that they expect the pandemic to accelerate levels of interest in delegated investment. This is certainly something we are seeing through our work with schemes of all sizes, both DB and DC. Our most recent Global Pension Risk Report showed that interest in delegated investment was expected to grow. We are also seeing a similar trend in DC. Aon's UK DC Pension Survey 2020 showed that 35% of employers with their own trust-based arrangements and 20% of those with contract-based plans are looking to move to a master trust. Of these, 54% with their own trust wanted to move due to the cost, time and resource pressures of running their own plan.

There is no sign that pressures on costs, time and resource will abate any time soon – and, the outlook remains incredibly uncertain, with continued market volatility and dislocations expected. Delegated investment offers a way to respond to all these challenges and for schemes to achieve their objectives with more certainty. As with all governance models, it has been robustly tested during the pandemic and through the market turmoil – and, the benefits of the delegated model have really come to the fore.

More information about how we have been positioning our portfolios and supporting our delegated clients is available in the *Further reading and resources* section of this report. We also welcome the opportunity to discuss how our teams can support you as you continue to protect your members retirement income and navigate the significant operational challenges you're facing at this time.



Tony Baily
Investment Partner, Aon



Sonia Gogna
Fiduciary & OCIO Solutions, Aon

Around
2/3

of DB scheme delegate manager monitoring to their advisers

Source: Global pension risk survey, 2019 UK findings

1 in 3

DC schemes do not measure progress against their objectives

Source: How do you measure up? Aon DC survey 2020

Could COVID-19 change scheme governance forever?

COVID-19 has caused many difficulties for pension schemes and their members. But it may have initiated the biggest shake-up in scheme governance for decades. Trustee boards have had to rapidly re-invent many aspects of how they run their scheme on a day-to-day basis. Respondents reported more frequent ‘bite-sized’ remote meetings instead of all-day quarterly meetings, carefully prioritised agendas structured around questions that require immediate answers, and faster decision-making.

Almost all participants said that this has been beneficial for general decision-making and that trustees had quickly got used to a new style of working. The logistics of setting up a board, or investment sub-committee, meeting have been simplified because trustees no longer need to travel to a meeting, and there is less requirement for traditional large meeting packs.



“Our governance has held up really well, I think. We have been able to make quick decisions and that has probably been helped by the fact that people don't have to be in the same room. Also, that you don't have to find the time for people to travel – because we have people from all over the country on our boards – has actually helped the governance structure.”

[Investment specialist, DB multi-employer scheme](#)

However, some aspects of trusteeship, such as discussing complex, contentious topics, are less well suited to video conferencing. Chairs of trustees said that they found it difficult to ‘read the room’ over a video conferencing link, and so understand whether trustees understand a proposal correctly, or to use cues such as body language to understand their response to it. Two professional trustees expressed concerns that elements of investment oversight were being put on hold or given a ‘light touch’ during lockdown.

Boards that were close to making major changes to their investments – either as a result of a review of their investment strategy or appointing a new manager – have had some of the biggest challenges during lockdown. Trustees and advisers said that they have had to carefully question whether decisions made in a pre-COVID-19 market environment were still suitable in the light of the pandemic.



“We will do fewer in person meetings and we will do more ad hoc online meetings. It has been quite a learning experience for many executives in our organisation who have never really held conference calls, let alone shared screens and worked with Zoom.”

[Independent trustee, large DB scheme](#)

Whether new approaches to governance will be retained over time remains to be seen. Some schemes are already reporting plans to move back to more traditional quarterly trustee meeting structures, but in other instances there is more enthusiasm to retain the benefits of more regular, remote meetings.



“Where there's a really sharp focused decision to make, governance during the lockdown has been better than it was before. However, if something needs training and developed discussion, that's where it becomes much more challenging.”

Professional trustee, large DB schemes

Respondents were hopeful that boards and the rest of the pensions industry will continue to streamline some governance processes post-pandemic. These include making greater use of technology to resolve barriers to action, such as the requirement for ‘wet signatures’ to action a new mandate.

Three participants said that their schemes have seen a reduction in the amount of executive support available to the trustee board over time. This has made tasks such as preparing board meeting packs more difficult. They felt that shorter, more frequent, meetings that have been driven by the COVID-19 crisis, were better suited to this more limited support.



“We did have a few practical difficulties at first when we went into lockdown, because some of the asset managers were still very insistent on hand-signed forms to set up new mandates. A very pleasing side effect of the crisis has been wider recognition that actually you can move to a more modern set-up using tools such as DocuSign.”

Professional trustee, large DB schemes

Looking to the longer term

Aside from the short-term shocks of the COVID-19 pandemic, many longer-term challenges remain for investment governance.

While scheme size is not directly correlated to the quality of board governance, there was a consensus among our respondents that larger schemes with bigger governance budgets are able to consider a wider range of investment opportunities and approaches. They are also able to act more efficiently when it comes to decision-making around investment strategies and implementing new ideas.



“On a practical level some schemes still don't spend enough time, effort or resource on their governance framework. And that it itself can then limit the options that advisers can bring to the trustees.”

Professional trustee, large DB schemes

Several third party evaluators talked about the importance of an appropriate governance framework that enables trustee boards to use the limited time they have to discuss investment in the most effective way. That framework needs to include a clear strategy, investment beliefs and investment principles that can guide future decision-making.

However, several professional trustees expressed concern that increased pressure from The Pensions Regulator is driving boards to spend more and more time on compliance — which is not always equivalent to good governance. The result is that, even for schemes with a clearly defined governance framework, investment decision-making is sometimes being pushed to one side by compliance demands.



“So, irritating though it may be, it is useful and, in a way, comforting. You can always scream and shout and hurl abuse, but actually, TPR are drawing attention to things that we would not have dealt with otherwise. So, they might even get a Christmas card.”

Member-nominated trustee, large DB scheme

For DC schemes, the chair's statement was identified by several trustees, third party evaluators and other decision-makers, as an example where excessive compliance is hindering good investment governance. “Trustees have only got so much time available. If they are spending the whole time talking and worrying about the chair's statement, are they actually looking at the investments properly?” asked one professional trustee.

Respondents also said that in some schemes, employers are questioning the costs of in-house DC scheme governance within trust-based schemes. This is starting to accelerate a trend towards using master trusts and GPPs for DC provision, which eliminates the need for an in-house trustee board.

Where DC schemes continue to operate in-house, there is a move away from creating bespoke or white-label default funds, and towards using off-the-shelf solutions or delegated approaches to investment. Related to this, some respondents felt that trustees of DC schemes are not always sufficiently aware of the complexities of what is required of them investment-wise, especially when it comes to factoring in freedom and choice.



“Trustees are spending a hell of a lot of time on compliance. Not governance, compliance. I don't think it is enhancing the governance as a result. Because they have only got so much time available, if they are spending the whole thing talking about, the DC chair's statement, are they actually looking at the investments properly? ”

[Member-nominated trustee, large DB scheme](#)

Changing models of trusteeship, whether a shift to sole trusteeship for DB schemes, or encouraging more diversity on trustee boards in DC schemes, is also affecting scheme governance according to several respondents. In particular, one respondent felt that this could drive better engagement with aspects of investment such as responsible investment. “The increase in the use of sole trustees will force the responsible agenda more. Sole trustees can express their views on it, rather than having to take account of widely-ranging views often seen on trustee boards. That could lead and accelerate change.”

Trustee education is also an important aspect of long-term governance. Associated with this is the perceived competence of trustee boards to manage investment governance and decision-making.

The shape of investment decision-making

Respondents reported varying quality of investment decision-making in the schemes that they work with – but are also exploring an increasing number of tools and approaches to help trustee boards of all types and sizes.

Those include fiduciary management for DB, better use of investment subcommittees, appointing an independent trustee or using an investment platform for DB or for DC. Deciding which solutions, or mix of solutions, would help an individual scheme depends on the scheme's circumstances and their broader framework for decision-making.

In one instance, a large scheme that had been able to drive investment innovation with its asset managers because of its size, wanted to make the solution it had created available for smaller schemes to use as well. One of its trustees said: "I think there is a part for larger scheme to play, to help smaller schemes. I think you have a responsibility to do that. We want to give that opportunity for other, smaller, schemes to be able to do some of these things we've been able to do. It's important to be open with your ideas and let them be shared."



"My challenge with trustees is, they like talking investments. It's sexy. They like seeing managers. They like having beauty parades. In my view, it is completely pointless. It's, do you buy the Aldi cornflakes or the Kellogg's cornflakes? They're both going to be cornflakes. So, do you actually need to open them up and see the individual pieces, without tasting them?"

[Professional trustee, DB and DC schemes](#)

Aon's 2019 Global Pension Risk report showed that around a quarter of UK DB schemes delegate full fiduciary mandates and 30% are using partial mandates. Respondents in this research said that they were seeing interest in fiduciary management grow, particularly from DB schemes.

Most of the interest was for full mandate appointments, rather than single strategy solutions – although some professional trustees and third party evaluators speculated that they may see more interest in single strategy solutions in future. Some respondents anticipated that the market volatility caused by COVID-19 could accelerate interest in fiduciary management, as also occurred after the 2008 global financial crisis.



"Our view is that trustees should focus on high-level strategic decisions. My experience is that there has been a lot of focus on things that are interesting but don't move the needle. Of course, delegation needs to be framed properly because the trustee board retains accountability. The goals of the investment committee remain the same, but they are seeing the strategic decisions only."

[Investment professional, large DB and DC scheme](#)

However, there continues to be resistance to fiduciary management from some trustee boards that see day-to-day decision-making as the trustee’s responsibility, even though in some instances respondents, and especially professional trustees, felt that this lengthens decision-making time and may limit the investment options available to the board. One trustee chair argued that better resourcing for trustee boards would be preferred over fiduciary management: “there is an argument that fiduciary management works better for small schemes with less resource – but so would getting more resource.”



“I’m an unashamed fan of fiduciary management. Because it stops meddling. It stops procrastinating, and it stops all the subjectivity that trustees and companies can bring. It brings the buy-in power, it brings the economies of scale, it enables you to be buying people’s best ideas. I don’t think it’s any coincidence that the schemes I’ve had that have been in fiduciary have got to a far better place far quicker than the others that haven’t. That doesn’t mean the traditional model doesn’t work, because it does. But it’s just harder for it to work.”

[Investment professional, large DB and DC scheme](#)

Where fiduciary management is being used as part of a DB scheme’s investment governance, third party evaluators report more interest from schemes in oversight of the manager, “That is definitely part of retender exercises,” said one. “A lot of schemes that went into fiduciary management without a competitive exercise are taking action.”

Contacts

Emily McGuire

Investment Partner
emily.mcguire@aon.com

Tony Baily

Investment Partner
tony.baily@aon.com
[LinkedIn](#)

Sonia Gogna

Fiduciary & OCIO Solutions
sonia.gogna@aon.com
[LinkedIn](#)

Joanna Sharples

Partner, Head of DC Investment Strategy
joanna.sharples@aon.com

With thanks to our researcher and author:
Maggie Williams

Maggie is an experienced pensions commentator, writer and editor with over 20 years' writing and interviewing experience. You can find out more about her through her [LinkedIn profile](#).

Further reading and resources

[Delegated Investment Webinar: The Bear – and now The Bull?](#)

[COVID-19 Response Webinar: Investment Focus - Navigating Uncharted Territory](#)

[How to get the right balance of DC pensions quality and time commitment](#)

[Aon's UK DC Pension Survey 2020](#)

[Global Pensions Risk Survey 2019](#)

Trustee Effectiveness Toolkit

10 questions to test your crisis resilience – **DB & DC**
Crisis resilience planning – **DB & DC**

Aon Investment Research 2020

This report forms part of a body of research into current thinking in pension investment.

Access all the reports in the series to discover key trends and common approaches among pension scheme decision-makers as they rise to the challenges presented by covid, climate and compliance.

About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

© Aon plc 2020. All rights reserved.

This document and any enclosures or attachments are prepared on the understanding that it is solely for the benefit of the addressee(s). Unless we provide express prior written consent, no part of this document should be reproduced, distributed or communicated to anyone else and, in providing this document, we do not accept or assume any responsibility for any other purpose or to anyone other than the addressee(s) of this document.

Notwithstanding the level of skill and care used in conducting due diligence into any organisation that is the subject of a rating in this document, it is not always possible to detect the negligence, fraud, or other misconduct of the organisation being assessed or any weaknesses in that organisation's systems and controls or operations.

This document and any due diligence conducted is based upon information available to us at the date of this document and takes no account of subsequent developments. In preparing this document we may have relied upon data supplied to us by third parties (including those that are the subject of due diligence) and therefore no warranty or guarantee of accuracy or completeness is provided. We cannot be held accountable for any error, omission or misrepresentation of any data provided to us by third parties (including those that are the subject of due diligence).

This document is not intended by us to form a basis of any decision by any third party to do or omit to do anything.

Any opinions or assumptions in this document have been derived by us through a blend of economic theory, historical analysis and/or other sources. Any opinion or assumption may contain elements of subjective judgement and are not intended to imply, nor should be interpreted as conveying, any form of guarantee or assurance by us of any future performance. Views are derived from our research process and it should be noted in particular that we can not research legal, regulatory, administrative or accounting procedures and accordingly make no warranty and accept no responsibility for consequences arising from relying on this document in this regard.

Calculations may be derived from our proprietary models in use at that time. Models may be based on historical analysis of data and other methodologies and we may have incorporated their subjective judgement to complement such data as is available. It should be noted that models may change over time and they should not be relied upon to capture future uncertainty or events.

To protect the confidential and proprietary information included in this material, it may not be disclosed or provided to any third parties without the prior written consent of Aon.

Aon does not accept or assume any responsibility for any consequences arising from any person, other than the intended recipient, using or relying on this material.

Copyright © 2020. Aon Solutions UK Limited. All rights reserved.

Aon Solutions UK Limited Registered in England and Wales No. 4396810 Registered office: The Aon Centre, 122 Leadenhall Street, London, EC3V 4AN.

Aon Solutions UK Limited is authorised and regulated by the Financial Conduct Authority. Aon Solutions UK Limited's Delegated Consulting Services (DCS) in the UK are managed by Aon Investments Limited, a wholly owned subsidiary, which is authorised and regulated by the Financial Conduct Authority.

www.aon.com

Compliance Code: A272-310321