

# Adding sustainable investments to higher education retirement plans



Sustainable development. Clean energy. Fair employment practices. Corporate responsibility. These are some of the prominent issues on college campuses today. Students and faculty have long called for school endowments to invest more responsibly, and now issues related to sustainable investing are becoming more mainstream.

According to survey data gathered by the Natixis Center for Investor Insight, 82% of respondents would like their investments to reflect their personal values. And more than six in ten indicated they would be more likely to contribute to – or increase – their retirement plan contributions if they knew their investments were doing social good.<sup>1</sup> The academic community has a history of leadership in this type of thinking, and now there are new ways to put theory into action.



Developed by Natixis Investment Managers in partnership with the Intentional Endowments Network

The Intentional Endowments Network supports colleges, universities, and other mission-driven tax-exempt organizations in aligning their endowment investment practices with their mission, values, and sustainability goals without sacrificing financial returns. In doing so, this broad-based, collaborative network will make a significant and critical contribution to creating a healthy, just, and sustainable society.

**FIGURE 1:** Today's Plan Participants Want Investments to Reflect Their Personal Values<sup>1</sup>



**82%**  
want their investments to reflect their **personal values**



**72%**  
of Millennials would **contribute more** if it advanced social good



**74%**  
would like more **socially responsible investments** in their retirement plan offering



**FIGURE 2:** ESG Factors Cover a Broad Range of Issues

Environmental issues	Social issues	Governance issues
Carbon emissions	Labor practices	Management structure
Water management	Human rights	Board structure
Waste management	Community involvement	Compensation policies
Deforestation	Diversity	Political contributions
Air and water pollution	Data protection and privacy	Risk oversight
Energy efficiency	Customer satisfaction	Shareholder engagement
Energy mix	Animal welfare	

Many plan administrators may not realize that there are investment options suitable for retirement plans that use sustainable and ESG (environment, social, governance) criteria in the investment process. Adding these types of funds to the plan option menu is a way to give all members of the academic community the ability to choose investments that align with their beliefs.

**ESG 101: What is ESG investing?**

ESG is a general term for investment strategies that consider environmental, social, and governance factors in the fundamental analysis of potential holdings. ESG criteria can be used to assess corporate responsibility, and may allow investors to identify investment risks and opportunities, as well as to align financial assets with personal values. There is no standardized list, but Figure 2 highlights some of the factors used most frequently.

There are many ways to implement ESG factors into an investment strategy, both to seek better returns and to manage the risk of loss. Investments using ESG-based strategies have generally performed as well as the broad market over time, according to analysis by MSCI (Figure 3).

In some cases, ESG analysis may help identify issues that could lead to corporate scandals or other reputational risks.

A recent example is Volkswagen, which claimed to have a positive environmental record, but had governance issues that led to cheating on emissions tests. In the week following the issuance of the EPA’s notice of violation to Volkswagen, investors punished the company and the stock lost 33%. Deep ESG research could well have revealed some of these governance issues.

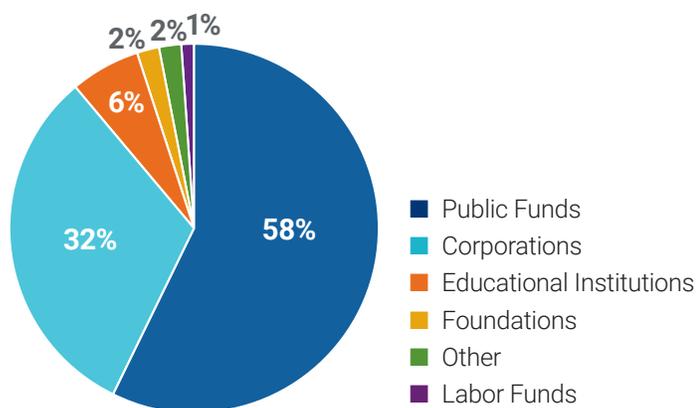
**ESG investing and educational institutions**

According to US SIF, educational institutions constitute the third largest pool of institutional capital with ESG assets, after public funds and corporations. A growing number of institutions are committing money to sustainable investment funds (Figure 4) and specifying ESG considerations in their investment policy statements. Given this trend, adding ESG-driven funds to qualified retirement plans can be a logical next step.

**FIGURE 3:** ESG-Focused Equity Index Has Kept Pace with the Broad Market  
Hypothetical growth of \$100 (10/1/17–12/31/17)



**FIGURE 4:** Educational Institutions Hold the Third Largest Share of ESG Assets



As fiduciaries for plan participants, plan sponsors are subject to Department of Labor (DOL) regulations. Until quite recently, there were no specific rules relating to ESG or sustainable investments in retirement plans, but in 2018 the DOL updated its guidance for plan sponsors. The new rules specify that adding ESG or sustainable funds to the lineup should be no different from adding any other new investment option. They are subject to the same due diligence process as any other fund.

### Opportunities for action

Plan sponsors interested in pursuing ESG or sustainable investment options may want to start by determining which types of funds would be the best match for their plan. There are three common ways to implement ESG considerations into a fund strategy: negative screening, best-in-class, and ESG integration. Each can be used on its own, or in conjunction with the others, depending on the desired result.

- **Negative screening** relies primarily on excluding industries, products, or countries based on moral or faith-based values. While this approach can help avoid specific ESG risks, it often leads to underperformance relative to traditional investment strategies, as it may exclude large sections of the investable universe.
- **Best-in-class** analysis seeks to invest in companies with better or improving ESG scores relative to their industry peers. This approach encourages progress in each sector, but without excluding any of them.
- **ESG integration** puts the emphasis on absolute ESG factors to evaluate companies and their associated investment risks and opportunities. This style seeks to identify businesses that may be more resilient over the long term because

**On April 23, 2018**, the Department of Labor published Field Assistance Bulletin No. 2018-01 addressing the use of ESG factors in ERISA plans. Overall, this bulletin continues the DOL's long-standing position that fiduciaries may not sacrifice investment return to promote collateral or social goals. The primary investment guideline for ERISA fiduciaries is to select prudent, well diversified funds with reasonable risk/reward tradeoffs. ESG funds should be evaluated alongside other competing fund alternatives – ESG or not – as part of the fiduciary's normal due diligence process.

their environmental, social, and governance policies may contribute to better financial performance. Unlike best-in-class, decisions are not made relative to industry peers.

A second consideration is whether the new sustainable investment options would complement or replace current funds in the plan. In this case, the primary categories are equity, fixed income, balanced, and target date funds.

- **Equity funds** – Sustainable equity funds can be domestic, international, or global in scope. Some funds are broad-based, investing in a full range of sectors, while others are concentrated or focused on a specific sector, such as carbon neutrality companies.
- **Fixed income funds** – Green bond funds specialize in bonds issued to finance projects that provide positive environmental impact, and are the most popular way to access sustainable themes through fixed income.
- **Balanced funds** – These funds combine equity and fixed income, and may generally be used as a QDIA.
- **Target date funds** – Designed specifically as a retirement plan QDIA, target date funds adjust their equity and fixed income allocations, seeking to optimize returns based on the participant's intended year of retirement.

There are a variety of ways to incorporate sustainable investments into a 403(b) plan, depending on the plan's objectives and investment policy statement.

## Key takeaways

- **ESG considerations** are economic factors that can help investment managers identify themes and risks.
- **Sustainable investing** aligns with businesses positioned to grow, thrive, and shape the world 10 or 20 years from now.
- **For these reasons**, the investment framework inherent in ESG aligns with the interests of long-term investors and may be a good fit for retirement plans.

## Next steps

Visit [im.Natixis.com/ESGTargetDateFunds](http://im.natixis.com/ESGTargetDateFunds) where you'll find opinions on DOL rulings, plan participant research, and communication strategies.

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- 1 Natixis Investment Managers, Survey of Defined Contribution Plan Participants compiled by CoreData Research, August 2016. Survey included 951 US respondents.
  - 2 US SIF: The Forum for Sustainable and Responsible Investment ([www.ussif.org](http://www.ussif.org))

➤ To learn more about adding sustainable investments to your 403(b) plan, talk with your plan advisor or a Natixis Investment Managers representative.

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