INVESTMENT INSIGHTS

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Creating more personal connections with retirement plan lineups

Menu aimed at participants' appetite for ESG may improve engagement

Efforts to get retirement plan participants to take an active — or more active — role in their retirement planning have largely centered on automatic features of defined contribution plans such as auto enrollment and auto escalation. More recently, some plan sponsors have begun using elements of behavioral finance to encourage participants to get involved.

A new twist on the use of behavioral finance tweaks a plan's investment lineup to drive participant engagement.

"It's the idea that the investment menu can serve as a tool to create better behaviors and therefore better outcomes," said Ed Farrington, head of retirement at Natixis Global Asset Management.

The idea focuses on millennials and their high level of social responsibility.

Over the last several years, Natixis has surveyed 401(k) plan participants on issues such as how they invest, what motivates them and what outcomes they are seeking. The firm has found, not surprisingly, that most respondents — 82% — want to see their personal values reflected in their investments. And 70% see investment opportunities in such areas as clean water and clean energy.

That's where things get interesting.

"If you ask folks, would you invest more or invest for the first time if the investments in your plan also did social good, you start to see a strong score from millennials," Farrington said. "Seventy-one percent of millennials state that they would, in fact, invest more or invest for the first time in their plan if their investments also did social good."

Farrington said it's the first time that the connection between a plan's investment menu and participant behavior has been illustrated so strongly.

"Millennials are saying overwhelmingly that an offering of ESG-like investments will actually create better behaviors and create a higher level of engagement, which is kind of the nirvana for all plan design," he said. "We've looked at things for years that work like auto escalation or auto enrollment but now you're seeing for the first time that we could use the investment menu to really drive behavior."

71%
of millennials would likely increase plan contributions if they knew their investments were doing social good*

Farrington explained that the interest in linking investments to social outcomes began to emerge over the last couple of years across generations, including baby boomers and members of Generation X, but the interest among millennials really stuck out. One reason, he said, is that millennials are coming of age at a time when most have a high level of financial uncertainty.

"Most don't have the promise of a defined benefit plan. They have less faith in Social Security. They have the burden of college loan debt," he added. "And that's changing the way they think about their ability to participate in the workplace. If we can show them that we can tap into their other interests — the world that they envision living in — and follow the themes that ESG exposes them to, we think we can get them to better behaviors."

According to Natixis' research, millennials specifically are interested in investments that focus on the environment and values-based investments.

"They want to know that the companies they're investing in are holding themselves to some standard when it comes to workers' rights, human rights, ethical behavior and environmental standards," Farrington said. "There's a desire to see that the companies they're investing in are actually holding themselves accountable to these social values."

And, like many ESG investors today, millennials don't believe that investing in a socially responsible manner means giving up return. "They do not accept that there has to be this tradeoff. I think it comes from growing up in a world with access to information being very high," Farrington said.

Armed with this information, Farrington and his team worked to create an investment option that would meet the criteria.

"The further we got into it, the more we recognized that using ESG screens to blend active and passive, equity and green bond, international and U.S. companies, could provide us with the outcomes that plan sponsors would desire," he explained. So the target-date fund series that Natixis created along with its ESG affiliate Mirova, glidepath manager Wilshire Associates and fixed-income specialists Loomis, Sayles & Co., includes international and U.S. equities, green bonds, an S&P 500 carbon-neutral sleeve, a U.S. value-tilted ESG sleeve and government bonds.

"I believe this is the next step, creating connectivity with the investment menu in a way that makes sense to people so that they're not only thinking about the amount of money they'll have on the day they retire but the type of world they want to live in on that day," Farrington said. "You've seen all these innovations over time — daily balances, target-date funds, auto enrollment, auto escalation. We have to always be saying, what's the next step?" ■

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*Data represented is from the Natixis Global Asset Management Survey of Defined Contribution Plan Participants compiled by CoreData Research, August 2016. Survey included 951 respondents.

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