For professional clients only

First State Investments

MILLENNIALS & RESPONSIBLE INVESTMENT

Is the investment ecosystem ready to meet the needs of the next generation of investors?

MILLENNIALS - TOMORROW'S INVESTORS

Much has been made of the demographic changes underway in each generation but none more so than that of millennials who are far from being old enough to retire, but have reached working age. They not only have a major influence on consumption trends, particularly in the digital arena, but also disposable incomes that will grow with age and look set to have their own demands and characteristics in terms of financial services. This applies equally to individuals' savings and pension funding, which though may be a distant concern for most millennials, are an important financial consideration of our current time.

Introduction and objective

In the summer of 2018, First State Investments and KeplerCheuvreux undertook a joint research project to test the views and preferences of millennials regarding their understanding of and attitudes towards sustainable and responsible investment, which we are naming RI in this report to capture all types.

The sample comprised approximately 540 responses and included both millennial and non-millennial respondents in order to enlarge the scope and allow for a level of comparison and benchmarking between the groups. The broadest definition was used to span those born between 1980 and 2000; our cohort comprises around 79% millennials.

The process was supported by new media platform Market Mogul[1] who have a high proportion of both millennial readers and content contributors and carry a significant amount of financial, political and economic news, information and commentary and therefore provided the ideal access to our target audience.

The purpose of the research was to ascertain:

- The influence and impact millennials may have through their intended preferences on the many component parts of the investment chain and therefore the wider investment ecosystem
- The requirements of millennials that are not currently being met by various market participants suggest to take this out to be consistent with style throughout
- What actions might be taken to attract and engage millennials and, more importantly, keep them engaged as their earnings, inherited wealth and disposable income rises.

1. https://themarketmogul.com/about/

Millennials have been described as both ‘disrupters’ and ‘innovators’

Background

Much has been written about millennials and their consumer practices and behaviours but little work has been done to consider how such behaviours may translate in terms of their choices as consumers of financial products and services.

Millennials have been described as both ‘disrupters’ and ‘innovators’, however, they are now arguably the world’s most powerful consumers. They worry about climate change, get outraged by bad company behaviour and social injustice and prefer to work for ethical companies but as yet there has been little attention given to attracting millennials to investment.

Financial planners in a post trail commission world are unlikely to be seen as a first point of reference for millennials as the upfront fees required for advice are likely to be a major hurdle, so where can they go to for financial advice? This is where social media platforms and fin tech advisers can prove to be key influencers.

Our research highlighted a number of areas that warrant further serious consideration for members of the investment chain and ecosystem.

Key trends identified

1.

Overwhelming majority interested in Responsible Investing

A significant majority class themselves as interested or very interested in RI. Over 80% of millennials in our survey that don't already invest in RI are either 'interested' or 'very interested'.

In one respondent's words, RI is 'allocating capital to investments that materially benefit society or the environment'.

2.

A new generation more at ease with Environmental, Social and Governance (ESG) concepts

Millennials are widely touted as having more interest in sustainable consumption than other segments of the population. There is significant potential for this drive for responsible purchasing to be applied to financial services. The majority (79%) of millennial respondents thought friends/colleagues of their age are more easily convinced than previous generations of the importance/reach/interest of responsible investments.

3.

Real demand for education on products

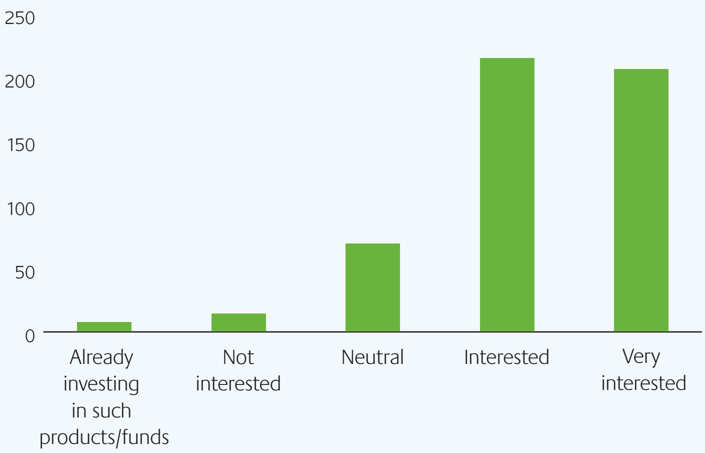
81%, the majority of respondents - both millennial and non-millennial - want more education on the topic of RI and RI products. This presents an opportunity for those in the industry who see their role as awareness raisers in making responsible investments as a whole more accessible and easily understood to a much wider consumer market.

4.

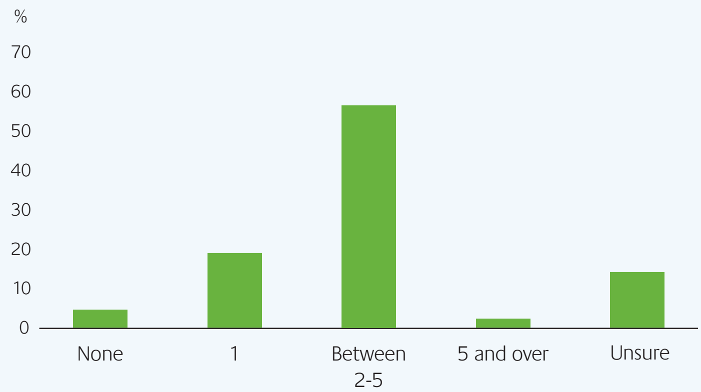
RI expertise is now expected from investment providers

Well-established specialisms in RI are a major factor in encouraging investment in a particular provider. The majority (78%) of respondents say that expertise in RI would be a reason for choosing an asset manager/financial services provider over another.

How interested would you be in investing in 'socially responsible' or 'sustainable investment' products?



How many controversial company incidents over a 12-month period would it take to cause you to change an investment fund?



The momentum for sustainable and responsible investment (RI) has never been greater. However, as the variety of self-labelled RI products, services and assets under management grow with every passing year, will the next generation of consumers remain interested and push the growth momentum into the long term? Our research points to a number of key trends.

5.

Environmental concerns still reign: Respondents focused on the 'E' in ESG

The environment is the most important area of focus - over a third thought it the most important broad thematic. This was also the case in the US, where despite widespread threats to support at a policy level, the investment theme of greatest concern was climate change.

6.

Slight majority perceived a boost to long-term returns

Whilst a significant body of studies show correlation with RI methodologies and competitive long-term returns, the mainstream financial community sometimes remains sceptical and defaults to an 'RI underperforms' mind set. In our survey, which was not posted on a specialist ESG platform but a generalist site, a slight majority of respondents thought the application of ESG investment methodologies would boost long-term returns. This applied almost equally for millennials as it did for all respondents including all age groups at 57% and 56% respectively.

7.

Perception of 'responsibility' remains sensitive to company controversies

We asked how many controversial company incidents over a 12-month period would cause an investor to change an investment fund. The majority (58%) replied that it would only take between two to five controversies to sway their choice. RI products may have a greater potential vulnerability around perceived corporate controversies than is currently realised. This leads to an increasing expectation on disclosures for such events even though they may not be in line with the stated fund's intent.

The Defined Contribution Investment Forum (DCIF) recently published a report – Navigating ESG – A Practical Guide (2018)[2] whereby they asked if they thought those that are making investment decisions for their defined contribution (DC) pension already incorporated RI - 25% of millennials believed they were, with another 26% suspecting so. This mis-placed expectation could compound the negative surprise of learning that this isn't always the case, further eroding confidence in the pension system.

8.

Financial services needs to adapt to the first 'digital native' generation

Almost half believed going digital could be a driver in increasing uptake of RI products. This could be via easier access to investment platforms, including via live-chats and other online interactions alongside a higher level of information on the RI characteristics of a specific product.

Digital could be a driver in increasing uptake of RI products

2. https://www.dcif.co.uk/

Millennials' perceptions of RI show that they expect rigour in methodologies

Key takeaways

Whilst actual investment in RI funds was at this point small, we note that overall interest is strong. Although assets in RI funds are growing globally, millennials are yet to be fully engaged by financial services providers in investing and deploying their capital into RI funds or products.

We would highlight particular demands for heightened standards emerging around RI products and services. Millennials' perceptions of RI show that they expect rigour in methodologies from financial service providers and asset managers in order to be fully engaged and that even a relatively small range of between two to five controversies within a portfolio would be enough to weaken confidence.

Expectations may need to be set not only in what dedicated RI funds can achieve but how they achieve it. Investor education is critical here with the vast majority of those surveyed claiming the need for greater education of RI products and services across the board whether they belong to the millennial generation or otherwise.

What might this mean for the investment ecosystem?

The research has provided us with some insights into the potential opportunities and risks for participants in the investment chain and ecosystem. We believe the following areas are worth further consideration by the various groups.

DC scheme operators and their trustees/sponsors

- Trust based schemes will need to clearly explain their polices on sustainable investment
- Governance committees (including Master trusts) need to become more informed on ESG
- Trustee boards should be required to undergo training and increase diversity
- Consultants will be asked to provide greater support to trustees and provide a framework for discussions with their asset managers
- Millennial workforce want more education and product information
- Reporting on the ESG performance and controversies relating to investments should be considered for both internal governance but also externally for scheme members

Member education emerges as an opportunity for scheme sponsors to further align with their millennial members' interests. Although the majority of scheme members tend to be invested in the default fund, there is potential to add RI specific funds to the choice menu or to go further and design default products to incorporate RI in the investment process to meet the interest in the subject.

This consideration of ESG factors, including climate change and stewardship policies, has been mandated for trust based pension schemes by the Department of Work and Pensions (DWP) by the 1st October 2019[3] to appear on their public Statement of Investment Principles.

3. https://www.gov.uk/government/consultations/pension-trustees-clarifying-and-strengthening-investment-duties

What might this mean for the investment ecosystem?

To engage an increasingly affluent millennial generation, fund managers will need to rethink how they measure and disclose performance

In addition, scheme members are likely to expect a higher level of information on RI outcomes from their scheme providers. This means an engaged trustee will need to develop a higher level of knowledge and awareness of RI to fulfil the requirements of the role in future.

The value of education and connection to RI is also supported by the DCIF's ESG research report, which showed that members are even more interested in RI when they realise they actually own real assets through their pension, increasing their engagement in their own savings.

Their report also found that RI can help build trust and build engagement, particularly with the millennials - 59% of whom would want to contribute more if they felt their pension money was being used for RI.

Investment managers

- Investment managers should disclose ESG outcomes alongside financial performance against an industry agreed framework
- ESG/sustainability integration examples should be provided
- Managers should provide resources to inform and educate their clients on their beliefs and approach to RI
- ESG expertise should be strategically developed and nurtured within and across organisations (it attracts millennial talent)
- Portfolio managers should have a part of their incentives tied to the quality of their ESG integration processes

The question of returns is central to the investment world. Whilst a slight majority (57%) of millennials though that the application of ESG would boost long-term returns, some responses indicated that more promotion of how sustainable businesses are more profitable, especially over the longer term, was indeed required. This reflected a more thorny issue of the perception of RI as sometimes requiring a sacrifice on returns, particularly within the financial services industry. In fact, of those volunteering free form opinions, only 10% focused solely on the need for returns in RI with a few respondents who still don't believe RI can offer superior long term returns. There may be some element of confusion at play here in terms of what respondents believed RI actually is.

Research has shown that consumers of financial products are often confused by the technical jargon that accompanies fund performance information. Standards and regulations exist for how fund performance is to be displayed, however no such standard as yet exists for how to disclose the ESG performance of investment portfolios.

Our research indicated an increasing desire to understand this and we believe that this will become a factor in fund choice. Evidence from the US indicates that the perception of the quality of sustainability[4] of a mutual fund is influencing investor appetite and being reflected in fund flows.

To engage an increasingly affluent millennial generation, fund managers will need to rethink how they measure and disclose performance in relation to the social and environmental outcomes associated with their investment products.

4. Chicago Booth Business School

As one consultant noted of pension fund trustees, “do a bunch of 50+ year olds really understand the needs and interests of millennials?”

What might this mean for the investment ecosystem?

Regulators and Policy Makers

- The Pensions Regulator should develop a sustainable investment training module as a minimum requirement for trustees as part of the Trustee toolkit in time for the DWP deadline
- Pension trade bodies should consider introducing best practice standards for diversity (gender and age) ,for example a ‘30 under 50’ club (30% of trustees under 50 years old) for trust based schemes
- Resources and education materials on RI and its features and benefits should be considered by the Regulator to encourage millennials to engage with their retirement schemes
- Pension trade groups should support the use of consistent definitions for RI in classifying funds and other financial products
- Pension fund trustees and their advisers should require assurance of RI claims and use of independent measures to support minimum industry standards of practice for RI

In the UK and continental Europe, public policy has and continues to play a major role in the uptake and awareness of RI. In the UK, the DWP has made a significant advance in the recent clarification of trustees’ duties and the range of fast developing policy streams at the European Commission via the Sustainable Finance Action Plan are setting a direction of travel. To ensure the success of these policy advances, trustees, investment advisers and pension scheme sponsors will need to be encouraged and indeed required to advance their own understanding of RI and enhance their policies and processes.

We also assessed whether stimulating RI take up via tax tools was desirable. Around 30% of those surveyed believed that it was. This indicates wider support for tax subsidies / advantages to encourage this form of investing, these measures already exists in some forms internationally i.e. via the Livret Developpement Durable (LDD) tax exempt retail savings scheme in France.

More broadly the accountability of RI related investments was a concern with some respondents venturing opinions that greater regulation of RI was needed – particularly as there is no fixed definition of it. One respondent summed up the reservations in requesting “proof they (RI investments) are what they say they are.”

The question of the diversity of the governance boards of pension and insurance schemes is a key issue. As one consultant noted of pension fund trustees, “do a bunch of 50+ year olds really understand the needs and interests of millennials?” Diversity is not limited to gender, but also age and skills knowledge and awareness. Trustees tend to be limited at best in their knowledge and awareness of sustainability and RI and this is an issue that needs addressing and cannot continue to be ignored.

The majority of responders look to 'Going Digital' as a positive expectation for responsible investing

Investment platform providers/fund selectors

- Platforms and their fund selectors should provide more RI information to ensure all relevant information is available to users and to attract millennials as the clients of tomorrow. Note the large majority 81% of responders' citied 'More education' as a key driver
- Develop and publish information on fund manager competency and RI expertise
- Provide a greater selection of sustainable investments and provide tools to allow meaningful comparisons with other funds
- Develop technology to provide 'at a glance' ESG overview of funds, for example a climate profiler, SDG impact or for a 2 degrees alignment.

Investment platform providers play a crucial role in allowing investors to view, evaluate and invest in a wide range of financial products and securities. Many platforms will provide a range of fund level information as well as general market commentary. To date, few of the major providers carry any RI information in any depth or often at all. Platform providers who continue on this path run the risk of not attracting millennials as users of their services in future.

Information, education and digital access are key components to attract millennial investors and this provides a huge opportunity for providers to attract the clients of tomorrow. We noted that the majority (55%) of responders look to 'Going Digital' as a positive expectation for responsible investing.

Finance sector trade bodies and NGOs

- NGOs should develop collaborative lobbying programs for better financial education in schools
- Trade groups should offer sustainable investment training and education in the form of accredited programs
- Highlight models of industry best practice and fund specific information based upon minimum standards of disclosures
- Forcefully call out poor practice and in particular 'greenwashing'
- Develop media strategies to engage and attract millennials linking real world impacts to the activities of companies and the role and influence of investors (the Greenpeace/Iceland 'Rang Tan' commercial is a good example) in corporate practices and behaviours

Transparency and access to data were themes that came up in the respondents open text responses. Investors want to be able to confirm that companies are not just "box ticking" according to one respondent who in our view represents a wider feeling amongst millennials.

This is an area where trade groups such as the UK's Investment Association and its European wide sister organisation EFAMA (European Fund Management Association), NGOs and groups such as the PRI, sustainable finance organisations such as Eurosif and ShareAction can all play a role both in providing an independent market perspective free of commercial conflict. In addition such groups can provide important information on market trends and asset flow across different RI approaches tracking the popularity and performance of RI funds.

They also have a role in highlighting best practice deployed by fund managers in terms of integrating ESG considerations in their investment processes and the quality of the disclosures of the outcomes of such a process to better inform and educate investors.

Summary

The research undertaken by First State Investments and KeplerCheuvreux underlined the emerging interest in RI from the younger millennial generation. As this generational cohort go through their working lives and become the savers and investors of tomorrow, RI looks likely to be a significant feature of their thinking and choices.

Our analysis and ideas are intended to add to the industry debate around how RI can continue to develop and meet the needs of an increasing number of financial consumers.

Today, the financial services industry is arguably ill equipped to capture this emerging interest and as we have suggested from our research, there are many things that can be done by all parties in the investment ecosystem to nurture, develop and gain from the growing interest in RI.

In our view, successful industry leaders will take a strategic approach as to how RI fits within and becomes deeply embedded into their organisational culture, beliefs and processes, providing millennial investors with a range of exciting options and choices as to where to deploy their precious investments, pensions and savings. As one responder noted, into: "... investments that materially benefit society or the environment".

Methodology

The research was carried out in the summer of 2018 and consisted of a short questionnaire posted and promoted via the Market Mogul website. The questionnaire was anonymous. Responses were collated by the Market Mogul team and subsequently reviewed and analysed by KeplerCheuvreux's ESG team who have previously issued in depth research around millennials within the frame of RI.

Although by the nature of its service offerings, Market Mogul has a high proportion of millennial readers, any age group could participate and it was not limited to millennials nor limited by the geographic location of participants. During the period the survey was open, 540 responses were received and analysed from all over the world, 79% of whom identified as millennials. Responders were also asked to state whether they were employed within the financial services sector, to which 45% identified as working in the industry.

This analysis forms the basis of this white paper which was prepared jointly by First State Investments and KeplerCheuvreux. The key takeaways and recommendations for courses of action were developed jointly by First State Investments and KeplerCheuvreux.

Appendix

TABLE 1: SUMMARY OF KEY QUESTIONS & CONCLUSIONS

Question	Key Conclusions
When were you born?	79% respondents were millenials by broad definiton covering birth years1980-2000
Male/ Female?	Almost three quarters male respondees (26% Female)
Where are you based geographically?	53% UK, 19% Europe ex UK , 9% US, ROW 19%
Broad Income Band	Majority in less than 35,000GBP equivalent bracket
How much disposable income are you currently saving?	Majority in less than 500GBP bracket including no savings
How much disposable income do you hope to be saving in 10 years	Majority in the 1500GBP+ category
If you were to inherit in the future, what % approximately are you likely to save/invest	Half willing to save / invest 70% or more
Are you employed within the financial services sector?	Around 45% involved in financial services sector in some form
How does application of ESG (Environmental, Social and Governance) methodologies affect improve returns?	56% thought it would boost returns vs 8.5% shrink returns% (and 36% neutral)
How interested would you be in investing in “socially responsible” or “sustainable investment” products?	81% either interested or very interested
Do you currently hold any SRI investments	Only 2% hold SRI investments out of 47% holding funds of any kind
Do you feel friends/colleagues of your age are more easily convinced than previous generations of the importance/reach/ interest of SRI Investments?	79% of our millennial respondents in our survey thought friends/colleagues of their age are more easily convinced than previous generations of the importance/ reach/interest of SRI Investments
What could drive investing in SRI?	
More education	Large majority (81%) of responders’ citied “More education” as a key driver
Overcome perceived lower financial returns	48% think there is a perception of lower returns from SRI and 44% percieve higher fees
Academic requirements in all business courses and universities	25% think SRI education should be taught in higher education
Lack of interest in sustainability topics	Only 10% think there is an actual lack of interest in sustainability
What are some critical factors in choosing an SRI Fund ?	
Lack of information and analysis around sustainable performance of the fund	40% think there is a lack of information around performance
Lack of easy access (e.g. digital investment platform, easy-to-open accounts etc.)	Lack of easy acccess is a potentially important factor with 48% wanting improvements in ease of use
Reputation of parent company investing in the fund	33% thought reputation of parent company important in choosing a fund
Going Digital	55% of responders look to “Going Digital” as a positive expectation for responsible investing
What broad issues or themes are you most sympathetic to?	Environmental is the most important area of focus - over a third thought it the most important broad thematic
Would expertise in socially responsible/sustainable investing be a reason for you to choose an asset manager/financial s ervices provider?	78% of respondents say that expertise in RI would be a reason for choosing an asset manager/financial services provider over another
How many controversial company incidents over a 12-month period would it take to cause you to change an investment fund?	58% replied that it would only take between 2-5 controversies to sway investment decisions

Source: First State, KeplerCheuveux

Authors: Will Oulton First State Investments, Sudip Hazra KeplerCheuvreux

Edinburgh
First State Investments
23 St Andrew Square
Edinburgh EH2 1BB
United Kingdom
Telephone: +44 (0) 131 473 2200

Frankfurt
First State Investments
Westhafen Tower
Westhafenplatz 1 60327
Frankfurt a.M.
Germany
Telephone: +49 (0) 69 710456 −302

Hong Kong
First State Investments (Hong Kong) Limited
Level 25, One Exchange Square
Central
Hong Kong
Telephone: +852 2846 7566

London
First State Investments
Finsbury Circus House
15 Finsbury Circus
London EC2M 7EB
United Kingdom
Telephone: +44 (0) 20 7332 6500

Louisville
First State Investments
400 West Market Street Suite 2110
Louisville, Kentucky 40202
United States of America
Telephone: +1 502 912 5506

Melbourne
Colonial First State Global Asset Management
Level 10, 357 Collins Street
Melbourne VIC 3000
Australia
Telephone: +61 3 8628 5600

New York
First State Investments
10 East 53rd Street, Floor 21
New York 10022
United States of America
Telephone: +1 212 848 9293

Paris
First State Investments
14, Avenue d'Eylau
75016 Paris
France
Telephone: +33 1 73 02 46 74

Singapore
First State Investments
38 Beach Road
#06-11 South Beach Tower
Singapore 189767
Singapore
Telephone: +65 6538 0008

Sydney
Colonial First State Global Asset Management
Ground Floor Tower 1 Darling Park
201 Sussex Street
Sydney NSW 2000
Australia
Telephone: +61 2 9303 3000

Tokyo
First State Investments
8th Floor, Toranomon Waiko Building
12−1, Toranomon 5-chome
Minato-ku
Tokyo 105-0001
Japan
Telephone: +81 3 5402 4831

MAR000482-006_0619_UK/EU