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Schemes retaliate over Russia’s invasion of Ukraine

By **Alex Janiaud**, **Angus Peters** | March 1, 2022

Some of the UK’s most prominent pension schemes are dialling down their exposure to Russian assets in response to its attack on Ukraine.

Russian troops crossed into Ukrainian territory in February and have waged a violent campaign against cities, troops and civilians.

Western powers have imposed economic sanctions on Russia in retaliation, while large companies including BP, Shell and Daimler have cut their exposure to the country.

The Moscow Stock Exchange was closed on February 28, while sanctions have sent the Russian ruble into free fall.

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Simon Pilcher, USS

High-profile UK pension schemes have publicly reacted to the conflict. The Transport for London Pension Fund, the Church of England Pension Fund, and the Universities Superannuation Scheme have all announced investment changes in response to the crisis.

Some of the largest master trusts have also acknowledged the crisis, with Nest deciding to sell down its exposure to Russian companies and government bonds as quickly as possible.

The TfL fund, which is the centre of industrial action this week, has frozen all direct holdings in Russia-domiciled investments.

The Church of England scheme and the USS have gone one step further, ordering their fund managers to sell their Russian assets.

The pressure to shield pension schemes’ portfolios from Russian exposure represents the latest step in an increasingly tense environment for trustees surrounding the ethics of their schemes’ investments.

Last week, the Merseyside Pension Fund delayed a decision regarding its exposure to companies operating in the occupied Palestinian territories.

The government in February, meanwhile, backed an amendment to the upcoming public service pensions and judicial offices bill concerning divestments.

Ministers will soon be allowed to issue guidance against public sector schemes from pursuing politically motivated boycotts and divestment policies.

Fiduciary responsibilities come first

The decision to exit Russian assets does not appear to be one taken solely out of moral outrage at Russia’s incursion on Ukrainian soil, which has been widely condemned.

Trustees’ fiduciary responsibilities to their members, which prioritise generating investment returns, have scope to allow the removal of investments on ethical grounds, provided that divestments do not materially harm investment performance.

According to Sackers legal advice, trustees considering divesting from Russian assets in response to the invasion will find it legally more straightforward making their arguments for doing so with financially motivated reasons.

The TfL fund has done just this, instructing its investment managers to make no direct investments or divestments in Russia-domiciled equities or bonds for the foreseeable future.

The fund has a negligible exposure to Russia, which stands at £28mn, or 0.2 per cent of its investment portfolio.

It recognised “the current lack of market for selling these assets and the trustee’s fiduciary duty to act in the best interests of the fund’s members”.

The Church of England scheme, meanwhile, ordered its fund managers on February 24 to sell all of its direct holdings in Russian companies and to cease further investment in Russian businesses.

The fund’s holdings in Russian companies prior to this instruction had sat at 0.16 per cent of its portfolio. It held no investments in Russian sovereign debt.

Simon Pilcher, chief executive of investment management at the USS, told BBC Radio 4 on March 1 that “there is a clear financial, as well as a moral, case for divestment with respect to our Russian holdings”.

The scheme has around 0.5 per cent of its portfolio connected to Russia. It has approximately halved its equity investments related to Russia in the past several weeks.

The BT Pension Scheme told Pensions Expert that 0.05 per cent, or £30mn, of its portfolio had direct exposure to Russian securities.

"We continue to monitor the situation, taking appropriate steps to protect the scheme and its members," a spokesperson said.

Westminster scheme does not have direct Russian exposure

Public sector funds are routinely under pressure from their members over environmental, social and governance investments.

The Scheme Advisory Board for England and Wales has counselled Local Government Pension Scheme funds to assess the implications of sanctions against Russia for their investment portfolios. The SAB told Pensions Expert that it would be requesting data from funds.

Politicians' pension schemes are feeling the heat. In Scotland, Green Party MSP Alison Johnstone has written on behalf of the Scottish Parliamentary Corporate Body to the Scottish Parliamentary Pension Fund trustee in response to reports that the fund is invested in the state-owned Russian bank Sberbank.

Johnstone urged the trustee to ask manager Baillie Gifford to divest all of the Russian holdings it manages on behalf of the fund.

"We recognise that the SPCB cannot direct the trustees in exercising its fiduciary duties on behalf of scheme members, but given the seriousness of the threat against our European neighbours, I am certain that all members, past and present, will be supportive of such representations to Baillie Gifford," she wrote.

We'll be removing all our investment in Russian government bonds and Russian companies as soon as possible

Helen Dean, Nest

The Scottish Public Pensions Agency told Pensions Expert that responsibility for the scheme's investments lies with its trustees.

"We are complying with sanctions, but cannot comment on any trades that are in progress," a Baillie Gifford spokesperson said.

The Parliamentary Contributory Pension Fund, meanwhile, which is the scheme for members of parliament in Westminster, is not aware of any direct holdings its portfolio may have in Russia.

"As responsible investors, the trustees are closely and actively monitoring this fast-moving situation in partnership with their investment advisers, who will act accordingly should any indirect investments come to light," a PCPF spokesperson said.

DC master trusts respond

Defined contribution master trusts have also acknowledged the crisis unfolding in Ukraine. Valuations are currently proving difficult to accurately achieve, however, given the market freeze that is currently in place.

The Nest master trust's latest valuation of its investments in listed Russian companies stood at less than 0.1 per cent of its assets under management, while its Russian debt exposure sat at around the same level.

"In view of the situation in Ukraine, we'll be removing all our investment in Russian government bonds and Russian companies as soon as possible," said chief executive officer Helen Dean.

Most fund managers would not have added to these positions over recent months given the geopolitics

Faisal Rafi, RisCura

The Aviva master trust, meanwhile, said that its direct exposure to Russia is negligible.

It urged pension customers to seek financial advice before making any changes to their investments, emphasising the medium to long-term nature of pension investments.

Russian stocks had been performing well

Western markets have fallen in response to the conflict, as well as Russian investments.

Liquidity is also a problem for investors, with Moscow-listed stocks currently at a standstill, while Russian prime minister Mikhail Mishustin has reportedly temporarily banned western companies from selling Russian investments, throwing divestment efforts into doubt.

One asset owner told Pensions Expert that liquidity is particularly thin, or even non-existent, in Russian bond markets.

As long-term investors, it is unusual for pension schemes to make wholesale changes to their portfolios in response to market shocks.

Trustees will consider a mix of investment and ethical reasons when deciding what to do with their schemes' Russian investments, also ensuring that their funds are complying with economic sanctions currently imposed on Russia.

“It should be noted that Russian equities had been performing well over recent years, and a number of blue-chip companies were held across global emerging market managers and even some global equity fund managers,” observed Faisal Rafi, head of research at RisCura.

“Most fund managers would not have added to these positions over recent months given the geopolitics,” Rafi added.

“What exposure asset owners are left with is a function of their positioning before the start of the escalation towards war and they can now neither add nor sell their positions.”

Most of Spence & Partners’ clients have less than 0.1 per cent of their portfolios exposed to Russia and Ukraine.

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Clients with higher exposure through active emerging market allocations still have on average approximately 0.5 per cent of their investments in the regions.

“The most significant impact to schemes is the wider implications of the invasion, such as inflation, rather than what the local Russian and Ukrainian economies experience,” said Brendan McLean, head of manager research at Spence & Partners.

“Russia supplies about 40 per cent of the EU’s natural gas imports, and both regions are major exporters of key grains and vegetable oils. Therefore, the conflict will result in price rises and increased inflation,” he added.

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Emerging markets were overplayed, but not any more

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