The Decumulation market: opportunities for providers

October 2022

Contents

Introduction

The decline of Defined Benefit (DB) pensions, coupled with the introduction of pensions freedoms in April 2015, leaves an ever-increasing number of individuals with Defined Contribution (DC) pots which they will need to rely on as their main source of income in retirement. Unfortunately, many individuals will find it difficult to navigate the decision-making process of using these pots to manage the needs and risks they face in retirement. The problem here is further compounded by the lack of effective guidance and available advice, even for those willing and able to afford to pay, which many are not.

In this report we bring together insights from our consumer research and our industry knowledge to look at the following areas:

- The current pensions market landscape: what are the products and choices available to individuals today?
- What impact does the current economic environment have on retirement decision-making?
- How could product innovation assist individuals in this market?
- How are people currently engaging with their pensions and what is being done to try and increase this?
- The retirement planning advice landscape.
- How the use of digital journeys can help with engagement and assist individuals in making choices towards better retirement outcomes.
- The focus of regulators in this area.

Our consumer survey was carried out by Censuswide in June of 2022. There were 2,005 respondents in the 50 to 70 age bracket, based in the UK. The respondents included a mix of those who had retired already and those who were yet to do so. For all respondents, we only looked at individuals for whom their main source of retirement income is (or is expected to be) from a Defined Contribution pension.

Consumers need the right support, guidance and protection today – it cannot wait until the future. As an industry committed to delivering good outcomes, a slow evolution of proposition sophistication is not enough.

There has been a lack of strong regulatory direction from the FCA on aiding consumers on sustainable income – there is no formal 'handrail' for consumers on what is sensible.

All of this is remarkable given how long it's been since Pension Freedoms were introduced. Through our work in the market and wider research, we set out here the main issues that need to be addressed.

Executive summary

Financial inclusion

Our research shows people on lower pot sizes have significantly lower levels of awareness of their retirement options. This is a striking social inequality issue - people with lower pot sizes are less likely to have the insight to make decisions to maximise the income they could get.

Underestimating longevity

International longevity experts Club Vita recently discovered men in the UK underestimate their life expectancy by 3.4 years. For women it was a staggering 7.9 years. This aspect of retirement planning is overlooked and could result in significant financial hardship in later years of retirement unless it's addressed now.

Blended retirement solutions

To meet the needs of future retirees based on the results of our survey (people valuing certainty and flexibility, risk of living longer etc.) consumers will need retirement plans that encompass a range of different products (drawdown, annuity, wider savings vehicles) to create a more holistic plan. This has to be delivered in an engaging way through a non-advised distribution channel, supplementing the advised route which already works for those able to access advice.

Lifetime mortgages

UK housing wealth stands at over £5 trillion. This represents a largely untapped opportunity for boosting income in retirement. It must move from being seen as an option of last resort to a sensible pillar of mainstream retirement planning.

Longevity pooling

Not everyone places leaving a legacy for their loved ones as their top priority. For those that value higher income while they are alive, longevity pooling has the potential to deliver an income in retirement circa 20% higher. And it can be delivered now, without the need for new regulations like CDC.

Digital engagement

Data aggregation, guidance algorithms and smart UX can enable providers to implement the level of proposition innovation required, and can democratise access to the financial support needed for mass consumers, helping to address the financial inclusion and social inequality issues.

Pension market landscape

Recent data from the Financial Conduct Authority (FCA)[1] shows that more than 700,000 new DC retirement pots are accessed each year, with a total value of over £45 billion being accessed. There is an upward trend in the volume of both retirees and pot sizes that are entering the retirement stage and we believe it is an exciting market for providers to be pursuing.

Current products and choices

Research[1] from the Financial Conduct Authority (FCA) has found that only 10% of pension pots being accessed for the first time are going straight to annuity, and 30% are accessed using income drawdown.

Results from our survey found that the proportion of people expecting to use drawdown (23%) was similar to those expecting to purchase an annuity (26%). However, we know that in practice many more have ended up entering into drawdown arrangements in recent years. This may be a reflection of the advice being received at the time of retirement, or of an increased understanding of the products gained as they come closer to making these decisions. A sizeable proportion (20%) of those asked were not aware of drawdown and 33% of those who said they wouldn't use drawdown said that the reason for this was that it was more important to guarantee their income for life.

Generally, the level of understanding suggested by the survey underlines the amount of work the industry has to do to ensure individuals are able to make well-informed choices. Since the age group for our research was those over 50 and therefore in the approach to retirement, this is a concerning trend and emphasises the need for education or other forms of engagement to help individuals understand the choices and options they have.

Firstly, we can look at the two most commonly used options that already exist in the market:

1 Annuities

Although annuities may have fallen out of favour following the arrival of pension freedoms, they can still form an important part of retirement plans.

Annuities can be both attractive and appropriate for those who:

- Have a low capacity for loss, particularly those with smaller pots sizes who don't want to risk being unable to sustain their income needs;
- Don't have any other regular sources of income that can meet their basic needs;
- May have lifestyle or health factors that would mean that favourable pricing could be provided subject to underwriting;
- Wish to purchase protection from inflation;
- Don't want to be subject to market volatility or sequencing risk;
- Wish to ensure a baseline guaranteed income above the level of the State Pension; and
- Don't have a priority to preserve their pension wealth to be inherited in a tax efficient way.

There is also a peace of mind provided by an annuity and this should not be underestimated. This will be most important for the least financially resilient customers but should at least be considered by all.

2 Drawdown

At the other end of the spectrum on product choice, we have drawdown, which provides flexibility and a sense of ownership. Money can be accessed as and when required and the investment choices appeal to those who want to retain control. We also know drawdown's emotional benefit is that people can see their pot and feel that they own it. However, drawdown does pose a number of risks, which should be considered by customers.

The risks involved in drawdown

Although it is a popular choice, drawdown comes with its own drawbacks. The combination of investment risk and the risk that individuals live longer than expected can make it very challenging to calculate a sustainable level of income to withdraw. In contrast, an annuity provides the client with peace of mind, as both the investment risk and the risk of them living longer than they expect are passed to the insurance company.

Considering investment risk first, research by FCA and others have found that retirees can be worried about investing in equities which leads them to adopt an approach which they feel is cautious but in reality, is unlikely to provide the return needed to support the income level required from a drawdown approach. FCA research found that nearly a third of customers not taking advice in drawdown were invested wholly in cash, with over half estimated to be losing out on investment return by holding cash[2]. The same research also found that providers' default funds were cash or cash-like assets and indeed this led to the FCA's introduction of Investment Pathways in February 2021 to provide more support for non-advised drawdown customers in making appropriate investment choices through the use of tailored default funds.

Background on Investment Pathways

The FCA introduced Investment Pathways for non-advised drawdown customers in February 2021. There are 4 possible objectives that a customer can choose from:

1. I have no plans to touch my money in the next 5 years
2. I plan to set up a guaranteed income within the next 5 years
3. I plan to start taking long-term income in the next 5 years
4. I plan to take my money in the next 5 years

The provider then has a default investment solution to match each of these objectives.

Taking life expectancy next.

Understanding life expectancy is difficult and we cannot expect retirees to be experts in predicting their life expectancy. In a **Club Vita survey in 2022 of 1,000 people – aged between 40 and 60 in the UK** - it was found that, on average, people **underestimate their life expectancy** by **3.4 years on average for men** and **7.9 years on average for women**.

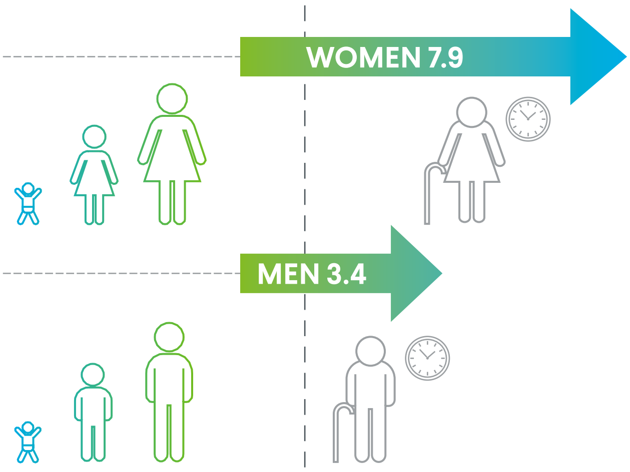
Not only are customers likely to underestimate their life expectancy, but there is also considerable variation in life expectancy based on a range of demographics such as health and lifestyle factors, which makes it difficult to predict with any degree of certainty.

For the women in the survey above, living for 8 years more than anticipated will require significant additional funding, close to £150,000 for a single individual living outside of London, based on the PLSA's moderate living standard.

Other factors in making the choice between drawdown and annuity

Individuals' priorities will evolve over time. For example, an individual may think that inheritance planning and leaving a legacy is important when they first retire. However, gradually the need to prioritise their own income needs, whether due to diminishing funds in a drawdown account or increased awareness of their life expectancy, could change this view and with it the case for annuitisation. In some situations, the death of a partner may reduce household income and create an immediate need for capital to cover funeral and related expenses. It's also likely that an individual's health will deteriorate over time, resulting in additional needs and costs. Yet many individuals struggle to believe that they themselves will be the ones that will experience poor health in later life and as such fail to factor them into their retirement planning. Indeed, Office for National Statistics (ONS) figures[3] show that although the duration of healthy lives has increased recently for 65-year-old males and females, there may be around half of the retirement lifespan which can be classed as not healthy. This will bring about a need for care, whether as additional domestic support, home modifications such as grab rails and chair lifts or full residential care in a nursing home. These life events will

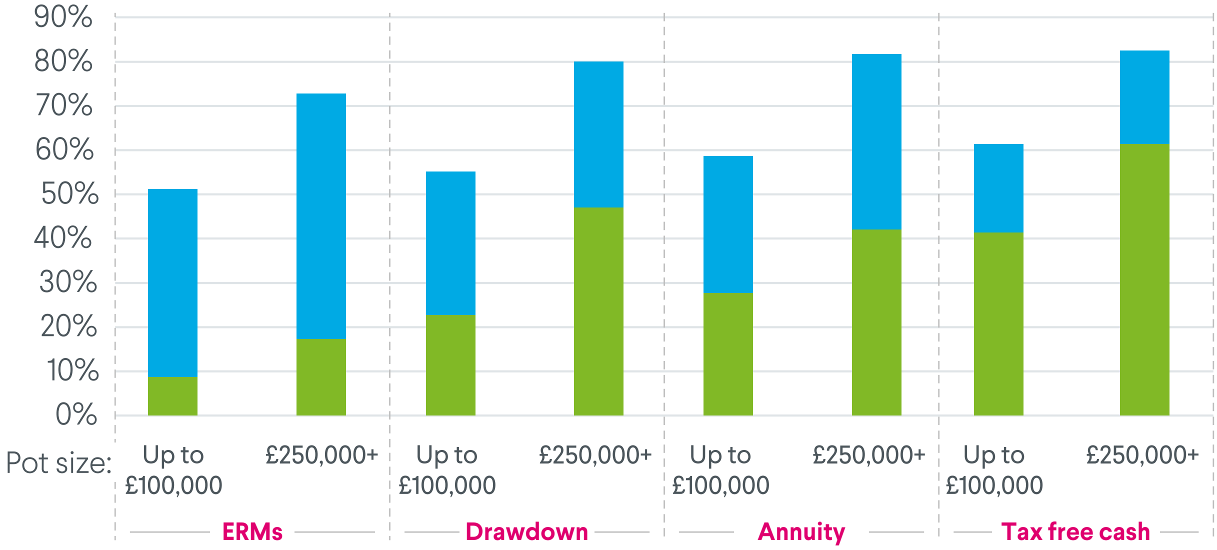
Underestimation of life expectancy (yrs)



have a direct impact on income needs in retirement and so there should be a consideration of how these events may influence the decision-making and the retirement journey.

Financial position can also have a substantial impact on making the choice between drawdown and annuity. Levels of awareness surrounding the different products available can differ greatly dependent on the size of DC pension. According to results from our survey, those with pots over £250,000 had the greatest awareness of all available financial products, with 80% and 82% being aware of drawdown and annuities, respectively. In contrast, when looking at the same figures for those with pots up to £100,000, only 56% were aware of drawdown and 58% were aware of annuities. Only 23% of those with pots up to £100,000 said they were using or intended to use income drawdown in retirement, compared to 46% of those with pots over £250,000. 27% of those with pots up to £100,000 intended to use annuities, compared to 43% of those with pots over £250,000. As mentioned earlier, those with smaller pots may prefer an annuity to drawdown due to the income guarantees, which can be appealing to those with a small risk appetite. In contrast, higher net-worth individuals may prefer the flexibility that drawdown can offer and are more comfortable shouldering a degree of risk when it comes to their pension pots.

Are you aware of the below products and are you using/planning to use them?



Alternative ways to combine product types

We've considered using different products in isolation, but another way might be to incorporate annuities in conjunction with drawdown. Rather than simply going for full annuitisation at the point of retirement, other options could be considered include:

1. Use of part annuity (to cover minimum income) and part drawdown (for discretionary spend/legacy) from outset
2. Planning for later life annuitisation
3. Using fixed-term annuities to bridge the gap between working full time and receiving state pension or other sources of income.

There are broader points to consider here, and we note that some individuals may be eligible for enhanced annuities, which would provide a higher monthly income than a standard annuity. This should be explored for comparison with the sustainable levels of income that are available under drawdown.

Annuities may not be the most suitable choice for high-net-worth individuals. The FCA Retirement Income Market Data discussed earlier showed that less than 4% of pots in the £250,00+ bracket are currently being annuitised. These customers are more likely to be able to live comfortably using drawdown from the investment return earned once they invest their large pots. This will afford them the flexibility to dip into the capital amount should they require additional money to fund luxury items or unanticipated expenses. It would also allow them to transfer wealth to any dependants on death which will often be a priority for this group. These individuals may tend to be more financially sophisticated than the general population and so better able to assess the risk in the choices that they make and be more comfortable with higher risk.

Even for individuals who initially do have a strong preference for drawdown, with life expectancy regularly underestimated, the prospect of later life annuitisation should be explored to guard against the risk of outliving their drawdown fund.

With the more financially resilient individual in mind, we consider the blended annuitisation approaches mentioned above, which don't involve full annuitisation.

Breaking up the retirement journey

One way to address this could be to divide the time spent in retirement into shorter periods that make it easier to plan for what the client is likely to want during that time. This makes the task less daunting and means they aren't locking into a permanent decision. Choosing a period of say five years means that at the end of this period, they can review their situation, look at what finances they have available to them and, again, what their priorities might be over the next period. The process then becomes iterative. There are products currently available that are well placed to meet this structure, giving the customer variety and flexibility in their approach to retirement funding.

Upon reaching age 65 the customer may still have other sources of income. If they didn't feel quite ready to fully retire, they could take up part-time employment in a less strenuous role, or they may have income streams from a business or rental income. They may also have a desire to continue to invest some of their pot and so drawdown could be an attractive option to top up their income during this time. In line with the five-years-at-a-time approach above, they may choose to take this drawdown for a fixed period, rather than for life.

There then comes a natural time for customers to reassess their financial needs when this initial drawdown term expires. At this point, other income streams could have ended and so a mix of drawdown and / or a fixed term annuity could provide an adequate level of income with sufficient guarantee.

By the time it comes of their third review, the customer may be in a position and happy to lock into a guaranteed income. This is where later life annuitisation comes in. At this age, they may also start to have failing health, which could make them eligible for enhanced annuities, providing a higher monthly income than a standard annuity.

Non-pension products

Other non-pension products that could be used to provide retirement income: Equity Release Mortgages (ERMs)

The opportunity in housing wealth

One area that can often be overlooked when considering retirement planning is the wealth held within individuals' properties. The UK currently has around £5.46 trillion of housing wealth relative to £6.45 trillion in private pension pots[4]. As those with DB pensions give way to those needing to manage their retirement income based on their DC provision alone, we know a large and growing proportion of retirees won't have amassed the size of pension savings they'll require to maintain the lifestyle they desire with the annual shortfall in retirement income projected to be over £48bn[5].

It therefore may become a greater consideration for these individuals to access the wealth held within their homes in order to top up their annual income or fund one-off expenses. Equity release products may be well-suited to those individuals who are looking to increase their retirement provision, but who aren't primarily concerned with preserving their wealth to pass on as an inheritance to their dependants.

The challenge

Equity release has previously been viewed negatively due to some unfavourable past practices in the industry. This is evidenced by our survey results, showing that respondents had similar levels of awareness of ERMs compared to other products, but only around 14% of those who had that awareness were planning to use equity release products as part of their retirement provision. We expect there is an emotional aversion to thinking about using the family home to fund retirement spending. The Equity Release Council has worked hard to raise standards and introduce safeguards, however, it still suffers from negative perception in the industry and there's clearly room for further improvement. For example, penalty charges on early repayment can be linked to market conditions and can therefore be difficult for customers to understand or predict.

There is, however, evidence of ERMs becoming a growing market in recent times with £1.6 billion of property wealth withdrawn by customers in Q2 2022 alone - a new quarterly high[6]. It may be that equity release is able to establish itself as a mainstream way to supplement pension income for those with housing wealth and insufficient DC pots.

Impacts of the current economic environment

The economic environment can further complicate retirement choices. This can have a direct impact on how individuals feel about retirement given the levels of uncertainty, as well as when people choose to retire. With household finances being squeezed and continued uncertainty about how far the cost of living will increase, some people might decide to reduce their pension contributions and/or delay their retirement; 29% of respondents to our survey indicated that current economic uncertainty had caused them to decide to retire later.

For those who have made the decision to go ahead with their retirement, the choice between annuity and drawdown will be impacted by both recent market volatility and the increase in interest rates.

For many, the investment risks that we described in the previous section will have been highlighted by stock market volatility in the last couple of years, potentially making drawdown less attractive.

In addition, the increase in interest rates and gilt yields has led to improvements in the annuity rates that are available; in April 2021, a £100,000 pension pot would have provided an annual annuity of £4,800, whereas now the expected income would be nearer £5,800[7].

The other economic impact that should be considered is inflation. In previous years, during which inflation has remained low for a long period, many pensioners didn't factor in the buying power of their income in future years. We see this in the FCA data on annuities which shows that only 16%[1] of annuities that are taken out have inflationary increases built in. If we do experience a period of double-digit inflation, this may become a bigger priority in retirement planning.

Product innovation

Longevity pooling

There has been a lot of recent industry conversation (and research from actuarial groups such as the Actuarial Research Centre (ARC)) on alternatives to the traditional choice of annuity or drawdown. One of the ideas that is frequently considered is the concept of longevity pooling – with the most common design involving a product that in some ways resembles a drawdown, so the individual can still see a pot of money that they can invest in their choice of funds. The one key difference is that on death, the fund is not returned to the individual's estate. Instead, the fund is distributed, in the form of longevity credits to the other members of the longevity pool. These longevity credits serve to effectively increase the return to the individual during their lifetime, almost like a boost to the investment return. For many, this additional boost could be enough to increase the sustainable income in a meaningful way – either allowing for a higher level of income or allowing for retirement to be taken earlier. Indeed, for those with medium-sized (c£100k - £200k) pots, the increase in sustainable income may be the difference between meeting their minimum income requirements or not. We should acknowledge however that distribution would be a challenge for providers to overcome for this segment of the market as longevity pooling products would most likely be sold through advisers and those with this level of pot are less likely to access advice than those with large pots.

We haven't had such a product launched in the UK yet and there are a variety of possible reasons for this:

- As with all new concepts, customers and advisers may not be quite comfortable with the concept to use it confidently
- And linked to this, the providers are possibly waiting until there are other similar products in the market.

Some of this nervousness could be alleviated by using a longevity pooled product alongside the standard drawdown structure – with possibly a gradual move of funds away from drawdown and into the longevity pool. Other options could be to have a product design that allows customers to change their mind and transfer their full pot out of the longevity pool. Alternatively, there could be guarantees or smoothing on the longevity credits which might give more certainty.

Phased strategies

In 2015, Nest set out their blueprint for retirement income, designed to provide inflation-protected income for life, with the benefits of being able to access lump sums and pass on their savings, particularly in the event of early death.

The Blueprint uses an approach of building blocks which cover the three phases of later life set out as:

1

Phase one:

Mid 60s to mid 70s – during this period the focus would be on an income drawdown fund to provide flexibility.

2

Phase two:

Mid 70s to mid 80s – would use a highly liquid investment strategy to continue paying a core income stream.

3

Phase three:

Mid 80s onwards – by this phase, later life protected income would be required, and this would be purchased over time through a series of deferred annuities which pay income during later life. If the right design can be found, these later life annuities may also pay out early in certain circumstances.

Investment solutions

In order to tackle the investment risk aspect of drawdown, some providers have developed specific post-retirement investment solutions. Although they don't fully eliminate the risk of market volatility, there are smoothed funds which have been designed to cope better with the decumulation phase of investing. This is where it is important for funds to be able to generate stable income, with minimal volatility to reduce sequencing risk and the possibility to preserve capital as much as possible. These funds have been developed as unit-linked managed or unitised with profits and are invested in a diversified mix of asset classes. They tend to have a smoothed growth rate with the possibility of market adjustments that can be made during more extreme market events.

Collective Defined Contribution

The use of Collective Defined Contribution Schemes (CDCs) would address some of the challenges discussed in allowing individuals to manage for both investment and longevity risk pooling, but it wouldn't contain guarantees on the income levels that could be achieved.
Although the development of decumulation specific CDC opportunities should be considered in the longer term, they aren't an immediate option due to the need for regulation change. Currently, the initial CDC rules that have been set out will only apply to single employer schemes. It's expected to take a few years for the rules to be in place for multi-employer schemes and it would then be some time in the future when we expect to see rules that allow for decumulation only solutions.
However, this is certainly an interesting development to follow and it's possible that variations could be developed which do allow for some of the risks to be hedged in a way that more certainty can be provided to the members.

What is CDC?

Collective Defined Contribution Schemes could be an innovative new way to blend aspects of both DC and Defined Benefit (DB) scheme designs. The employer and employee contributions are set, but are pooled and invested collectively to achieve a sustainable target benefit level for all scheme members.

Members of CDCs will be paid an income at a target level and increases to this income will be variable, depending on the level of the fund available. In some circumstances, the income level may remain flat for a number of years or even reduce. However, due to the pooling, it's expected that income levels will be more than comparable with alternative schemes.

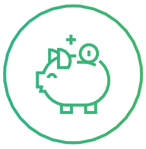
Current pensions engagement

Increasing engagement in pensions is recognised as a top priority. Indeed, the Association of British Insurers (ABI)/ Pensions and Lifetime Savings Association (PLSA) initiative of the Pensions Engagement Season, which is receiving cross industry support, is evidence of this. The aim is to increase awareness and bring retirement saving into everyday conversation. It's hoped that by many of the providers all working together at the same time to amplify and reiterate the key messages about pensions, that the tens of millions of scheme members who'll be represented will feel supported and empowered to learn more about how to enable better outcomes from their pension scheme.

Pensions dashboards:

These are digital platforms that will allow individuals to easily access their pensions information online and in one location, with the hope that this will enable better retirement planning. Individuals will be able to see how much they have saved in various pots, including any forgotten pots, and understand their savings in terms of an estimated retirement income. Information on the State Pension will also be available. Depending on the size and type of scheme, schemes will have to connect with pensions dashboards by the period between August 2023 and October 2025.

What have I got?



Is it enough?

What should I do next?

Being able to answer these key questions above should allow individuals to feel connected to their pensions. If engagement season is successful, providers will hopefully see an uptick in people logging on to check their pension and for many, even just confirming that their contact details are up to date would be evidence of engagement.

This should all tie in well with dashboard further down the line.

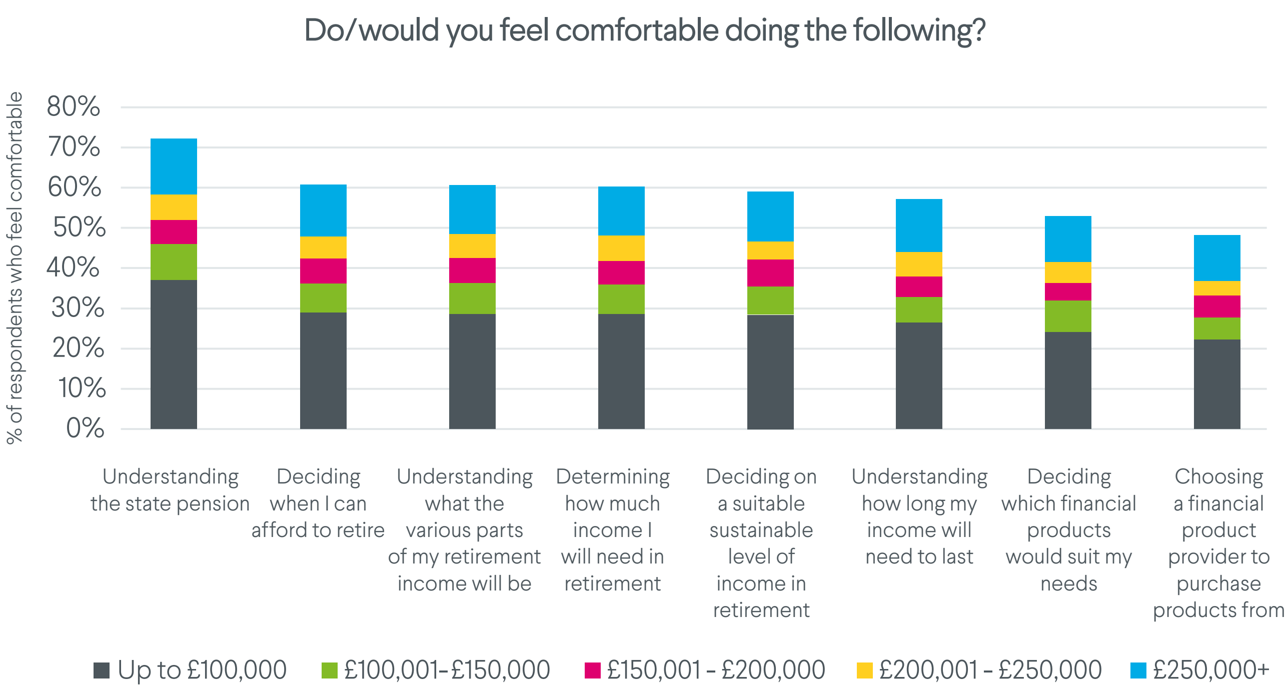
The success of auto enrolment in encouraging ever increasing numbers of pension savers is perhaps good evidence that active engagement is not necessary for the accumulations phase; more than 10.6 million employees are currently enrolled in pension schemes, with an additional £28 billion being saved into workplace pensions in 2020 compared to 2012[8]. However, with important decisions to be made at the point of retirement, the lack of engagement can be a barrier to the most appropriate outcomes. A number of other initiatives are seeking to address this, with increased focus on wake-up packs and stronger nudges to access free advice. When pension dashboards arrive it should help for everyone to be able to see their total pension wealth including pots that might have been forgotten about.

Results from our survey indicated that levels of understanding regarding communications from current pension providers varied largely depending on pension pot size, highlighting the importance of tailoring correspondence to customer circumstances. Amongst those with the smallest pension pots – up to £100,000 – only 59% find communications from their current provider easy to understand. This, however, increases alongside pot size, with 76% of those with pots above £250,000 classing the information they receive as easily understood.

Following on from this, those with pension pots up to £100,000 were more likely to say that the level of communication they received from their current provider was too little for them, indicating that perhaps those with lower-sized pensions are seeking more regular and more easily understood information. In a similar vein, only 62% of those with pots up to £100,000 felt they had access to all the information they need to make important decisions about their retirement, whereas 81% of those with pots over £250,000 felt the same.

This variance is mirrored in respondents' confidence in carrying out various tasks relating to managing their income through retirement, with those with the smallest pots consistently the least comfortable. Once again, those with the largest pensions were ranked the most comfortable. In the group as a whole, respondents felt most comfortable understanding the State pension, with almost 73% placing themselves in this category. However, only 48% and 53% of the group, respectively, felt comfortable choosing a financial product provider to purchase products from and deciding which financial products would best suit their needs.

This highlights a huge opportunity in the market for the development of online tools to assist customers throughout these processes, which can overcome both the barrier of cost and the inefficiencies of generalised communications. There were further deviations when considering different pot sizes; when focusing on comfort in choosing a provider, only 40% of those with pots up to £100,000 said they would feel comfortable choosing a financial product provider to purchase products from, whereas 71% of those with pots over £250,000 said so. This again highlights a greater degree of financial confidence amongst those more affluent customers.



Impacts of Consumer Duty

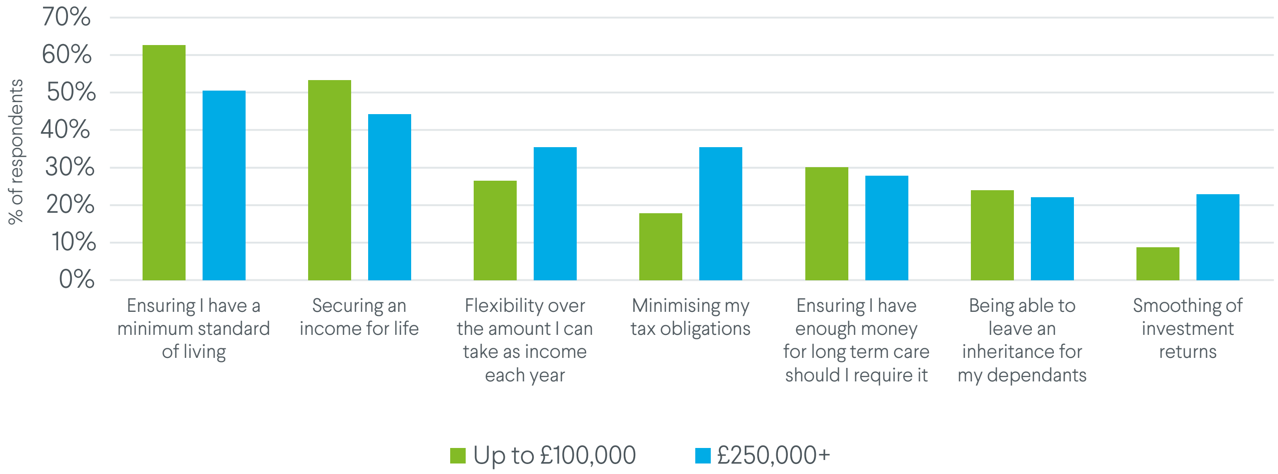
There are aspects of the Consumer Duty that could apply here too. As discussed in our recent article, the Financial Conduct Authority (FCA) has recently confirmed its plans to bring in a new Consumer Duty, which aims to improve how firms serve consumers. It will set higher and clearer standards of consumer protection across financial services and require firms to put their customers' needs first. The FCA are encouraging providers to focus on customer outcomes and one of the four key outcomes is on consumer understanding. Specific points of note on customer communications are that a good outcome is where:

- consumers are given the information they need;
- at the right time; and
- presented in a way that they are likely to understand.

The aim is to allow customers to make effective decisions and these communications should also be tailored to the needs of the target market, bearing in mind that special consideration should be made for any vulnerable customers.

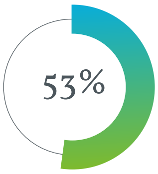
From our survey, the priorities of retirees can also differ depending on the size of their pension pot. Ensuring a minimum standard of living and securing an income for life were the most popular options amongst all pot sizes. However, where those with smaller pots were concerned with ensuring they have enough money for long-term care should it be required, those with larger pots viewed minimising tax obligations and having flexibility over the amounts they can take as income each year as priorities.

When thinking about retirement, which of the below is most important to you?

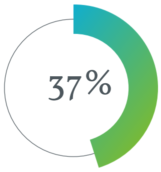


Advice

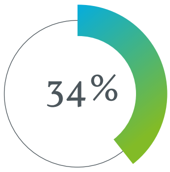
FCA Retirement Income Market data says that from October 2021 to March 2022



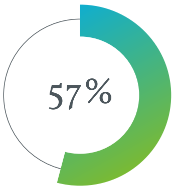
of purchases received no advice



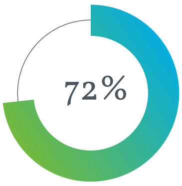
of annuity purchases were unadvised



of drawdowns were unadvised



of sales to those with pots up to £100,000 were unadvised compared to only 22% of those pots over £250,000

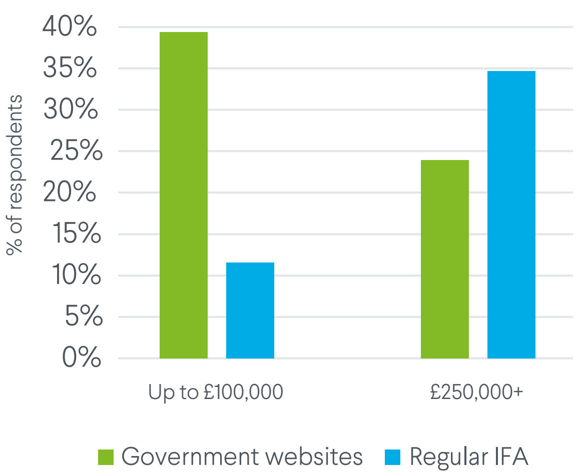


of those with pots over £250,000 made use of regulated advice compared to only 29% of those with pots of up to £100,000

more than double the percentage of small pots used Pension Wise compared to large pots (13% v 6%).

In our survey we saw similar results, with 44% having never used an independent financial adviser (IFA) and a further 18% having not received any advice in the last 5 years. Again, these figures vary with the size of respondents' pension pots; only 50% of those with DC pensions up to £100,000 had ever received advice from an IFA, compared to 76% of those with pensions over £250,000. Those with the smallest pots intended to predominantly make use of free government websites, with 39% of that group saying so, compared to only 23% of those with the largest points, whereas those with the largest pots were the most likely to make use of a regular financial adviser, at 35%, compared to only 12% of those with the smallest pots.

How do you intend to make financial decisions relating to your retirement?



The most popular reason for not using an adviser was deemed to be the cost, with over 50% of those with the smallest pots citing this as the reason they don't plan to take paid advice on their finances. However, even when free guidance is available through the government website 'Money Advice Service' this is not particularly popular, with only 29% of all respondents having used it before. One of the aims of both the Stronger Nudge to Pensions initiative and of the Pensions Engagement Season is that more traffic will be driven to Money and Pensions Service (MAPS), so it would be encouraging to hopefully see these statistics change over time. The level of understanding among those with different pot sizes also varies - we saw that for those with the largest post sizes, their primary reason (with 35% citing this) for not taking paid advice is that they already understand their options and know what they are going to do. This is another indication that individuals with different levels of pension wealth need different sorts of support and the routes to advice or guidance should be tailored accordingly.

Interestingly, one of the more popular sources of advice is to speak to friends and family with half of the group having used that route. While individuals may feel comforted by these conversations, they could be missing lots of vital information by not seeking out professional assistance.

Digital journeys

As discussed in our advice section, there are large segments of the retirement planning market that for a variety of reasons are unlikely to access traditional financial advice.

We live in an increasingly digital world. Even the least tech-savvy individuals have been forced through the pandemic to engage more and more with online technologies, in particular in relation to financial products and communications. Large sections of the retirement market will expect online tools to be available to them in order to access the information they need, at a time that is convenient for them and in a way that they can digest at their leisure. We believe that this offers an opportunity for providers to differentiate themselves through their digital journeys.

We're most excited about how the industry can use online retirement planning tools to democratise access to good quality guidance for those not able to access full financial advice. We know from our experience of building financial technologies that the most successful tools are those that keep things simple. This may be a perfect opportunity to create streamlined online planning tools aimed at those who don't have large enough DC pots (or other sources of income) to require complex tax considerations, but who simply need to understand their own longevity, what is a sustainable level of income for them to drawdown or indeed when may be a sensible time to purchase an annuity and lock into a guaranteed minimum level of income.

Online tools were popular in the research that we conducted, with 31% of those who aren't yet retired saying that they would be the best form of receiving information about retirement planning. There was also strong agreement with the idea of being able to play around with different options to see how income outcomes would be impacted, which is a strength of many tools and gives a sense of ownership to the individual as well as building up their understanding and confidence.

Another advantage of digital tools is the ability to introduce stochastic projections into retirement planning. Whilst stochastic projections do bring additional complexity, when communicated clearly, they can be invaluable in assisting individuals in their journey to understanding the impact their choices can have on retirement outcomes. In particular, it can be difficult to show through a number of deterministic scenarios the variability of both investment returns for given funds combined with the uncertain nature of an individual's life expectancy. Having this information to hand can illustrate what levels of income would be sustainable and importantly the likelihood that a given level of drawdown income would not be sustainable and lead to the fund being exhausted while the individual is still alive.

Use of pre-populated but overwritable defaults within these journeys can help to make the user experience as straight forward as possible and avoid users disengaging before they have meaningful information to make informed choices and take action.

Challenges

There does, however, still seem to be a degree of apprehension around using online tools to aid retirement planning, with 42% saying that they agree that they would have concerns over entering their pension information online. Building trust with customers through brand awareness, regular communication, and initiatives such as pensions engagement season, coupled with access to their pensions information through Pensions Dashboards should all help to reduce this apprehension over time.

Paul Waters
Partner and Head of Digital Wealth

"One of the largest challenges we found in digital engagement with financial products was helping consumers to understand inflation. Ensuring that they appreciate the impact of inflation on their retirement income while not trying to negatively influence their decision was a difficult balance.

Through considered design and extensive customer testing, we addressed this by showing both before and after inflation figures in a simple user interface."

Focus of regulators

Following on from the Retirement Outcomes Review, the FCA have continued to provide a number of pointers on their view of the retirement market and what could be done to improve outcomes for retirees. Some of examples of these and initiatives from other regulators are outlined below:

Stronger nudge to pensions:

The Department of Work and Pensions (DWP) published regulations on pension guidance, which came into force on 1 June 2022. These were designed to strengthen the 'nudge' for members to access guidance relating to their options on funds held in DC Pension Schemes. In order to meet these regulations, a scheme is required to:

- ✔ Offer to book a Pension Wise guidance appointment on behalf of the member and, where the member accepts this offer, take reasonable steps to book the appointment.
- ✔ Where the member does not accept the offer, or where the scheme is unable to book a suitable appointment despite having taken reasonable steps, the scheme must provide the member with details of how to book an appointment themselves.
- ✔ Explain to the member that they cannot proceed with the application to access or transfer their benefits unless they confirm to the scheme that they have received appropriate pensions guidance, or the member opts out of receiving guidance by giving them an opt-out notification.
- ✔ Explain to the member that they can only opt out of receiving appropriate pensions guidance by giving the Scheme an opt-out notification.
- ✔ Continue to deliver the "stronger nudge" in all subsequent interactions with the member about their application until the member either confirms that they have received appropriate pensions guidance or gives the Trustees an opt-out notification.

The stronger nudge to pensions efforts is a good example of the increased coordination between regulators with the FCA consulting at the same time with its own stronger nudge to pensions guidance in PS21/21. We welcome this trend as we recognise the benefits of having both occupational and trust-based schemes being regulated in line with the contract and personal pension market, not least for assisting with individuals' understanding of their pensions.

There were parts of the **Consumer Investment Strategy**[9] as set out in September 2021 that were relevant to the issues facing the decumulation market. In particular, the FCA noted that half of UK adults with £10,000 or more of investible assets did not receive any formal support in making investment decisions and robo-advice was also falling short in terms of the number of people who had accessed it. The FCA had concerns over some of the high-risk investments that were being placed, but also in the fact that savings for the long term were being placed in cash. And of course, the **Investment Pathways** for non-advised drawdown customers was largely put in place to reduce the volume of cash investments.

The FCA and The Pensions Regulator (TPR) have recently published feedback they received from a call for input on what can be done to help engage consumers so they can make informed decisions that lead to better pensions saving outcomes. Both regulators have identified a number of actions they will take in response to this feedback alongside the work they are already undertaking in the area.

Conclusion

What should providers be doing to maximise the opportunities in this market?

Understanding the growing retirement market and the customer needs

Considering whether their product range meets these needs or whether product innovation is required

Investing in digital technologies to ensure smooth customer journeys

Assisting with industry efforts to increase individuals engagement with their pension choices

The retirement market is expanding, providing lots of opportunity to serve these customers and manage their growing DC pots. Many retirees feel underserved in terms of the information they receive and how to go about making the important decisions they face. As we can see from our survey results, the outcomes can be quite different for those with very different pot sizes and other sources of retirement income in terms of being able to meet the financial goals and type of retirement that they would like. This underlines the need for tailored guidance for the different circumstances individuals are facing. With the FCA focussed on consumer outcomes, it's timely to review how all retirees are being served including the information that is provided to them and the products and services that are available to them.

The regulators are becoming more aligned, and the industry is also working together in areas such as Pensions Engagement Season, so positive moves are being made. Below we summarise the key developments that are set to provide improvements for all, along with some further suggestions for breakthrough developments that could help everyone to make their crucial retirement decisions.

What is already happening?	What more could be done?
Introduction of Pension Dashboards – where everyone will be able to see all their pension schemes in one place.	Once fully operational, the Dashboard will be a great place for seeing all pension pots in one place. The next step would involve easier integration of these pots, potentially including a smooth consolidation process.
Outcomes focus, using illustrations to regularly check if retirement savings are 'on track'.	More use of stochastic illustrations which can be much more informative by providing individuals with information around what sustainable income levels might be for their given pot size and retirement choices.
Acknowledgement that everyone will have a different retirement journey.	Much more holistic retirement planning is needed with ways to consider all assets (potentially including housing wealth) and varying retirement income needs.

Get in touch

Our dedicated team of life insurance consultants provide targeted advice across eight areas of focus – product development; digital wealth tooling; risk and capital management; investments and ALM; longevity management; transactions and structuring; and insurance transfers, reporting and property and casualty.

We have over 1000 staff working across a wide range of disciplines and can leverage the wider skills of our firm across investments, risk management and pensions. If you would like to know more please get in touch.

Contributors

Karen Brolly
Head of Products
0141 566 7904
karen.brolly@hymans.co.uk

Paul Waters
Head of Digital Wealth
0207 082 6281
paul.waters@hymans.co.uk

Fyona Murphy
Senior Consultant
0131 656 5182
fyona.murphy@hymans.co.uk

Kirsten Wilkie
Consultant
0131 656 5152
kirsten.wilkie@hymans.co.uk

Other key contacts

Emma McWilliam
Head of Global Insurance & Financial Services
0207 082 6256
emma.mcwilliam@hymans.co.uk

Stephen Makin
Head of UK Insurance & Financial Services
0131 656 5164
stephen.makin@hymans.co.uk

Andrew Gaches
Head of Global Longevity
0207 082 6128
andrew.gaches@hymans.co.uk

Ailsa Dunn
Head of Longevity Licencing
0141 566 7732
ailsa.dunn@hymans.co.uk

Sources

1. Retirement income market data 2021/22
2. Section 1.13, MS16/1.3: Retirement Outcomes Review Final report (fca.org.uk)
3. Health state life expectancies, UK - Office for National Statistics (ons.gov.uk)
4. Total Wealth: Wealth in Great Britain - Office for National Statistics (ons.gov.uk)
5. The-lang-cat-house-rules-final.pdf (langcatfinancial.co.uk)
6. 220729-Equity-Release-Council-Q2-2022-stats-news-release-FINAL-2.pdf (equityreleasecouncil.com)
7. The impact of interest rates on pension annuity rates | Hargreaves Lansdown (hl.co.uk)
8. https://www.abi.org.uk/globalassets/files/publications/public/lts/2022/automatic-enrolment-what-will-the-next-decade-bring/
9. Consumer Investments: Strategy and Feedback Statement | FCA

London | Birmingham | Glasgow | Edinburgh T 020 7082 6000 | www.hymans.co.uk