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Retirement: What's the full story?

Dedicated to promoting investment excellence



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About us



The Defined Contribution Investment Forum (DCIF) aims to exchange ideas and develop initiatives to promote investment excellence in Defined Contribution (DC) pensions in the UK. The DCIF consists of investment firms and selected other industry participants who believe that members in DC pension schemes deserve the best possible investment services to help them meet their retirement objectives.

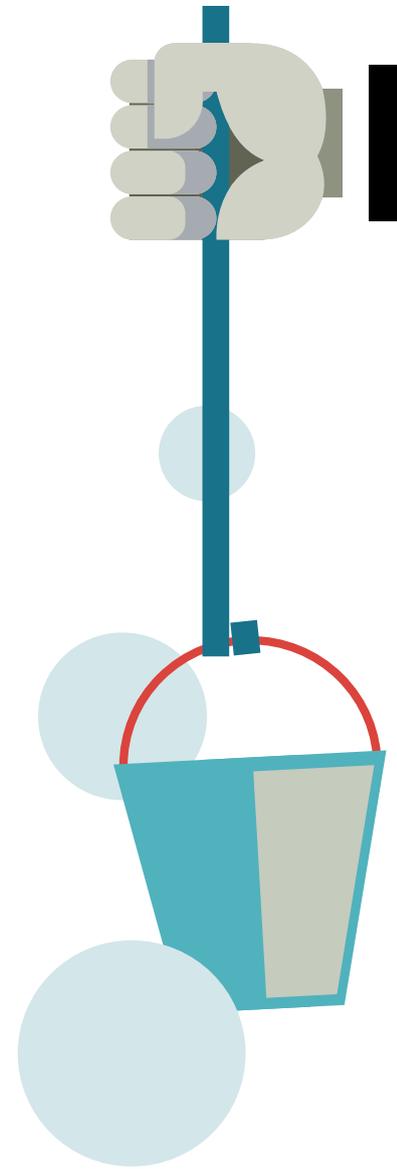


How are defined contribution (DC) schemes navigating drawdown on members' behalfs?

What are the challenges associated with investment design, in the wake of freedom and choice?

And does today's retirement data tell the full story?

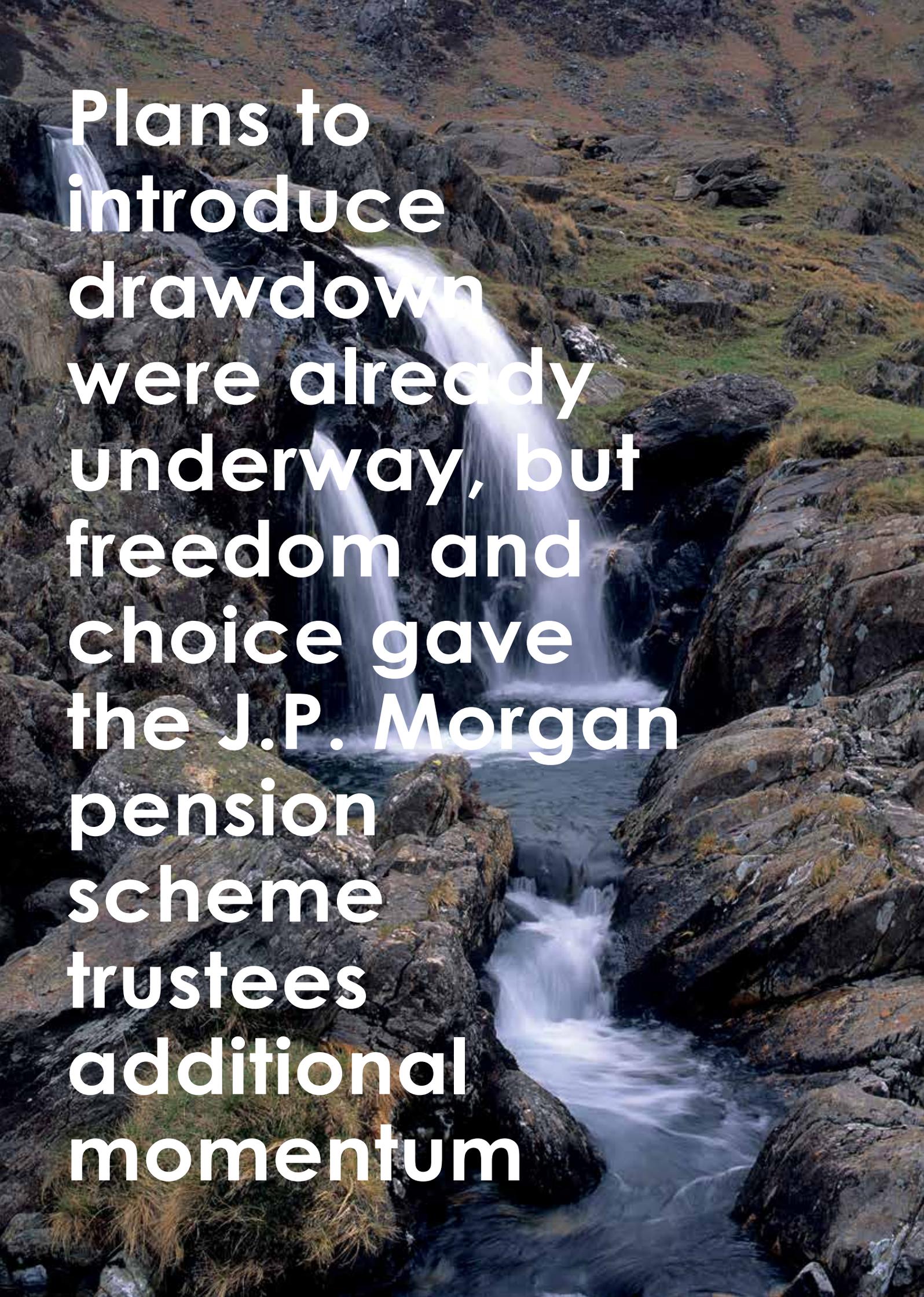
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The roundtable

A group of industry experts, each with a different perspective, gathered to discuss the trends they are observing in this fast-moving landscape. Read on to find out the four key observations they made.

- **Rene Poisson**, chair, JP Morgan UK Pension Plan
- **Nathan Long**, senior pension analyst, Hargreaves Lansdown
- **Lydia Fearn**, head of DC and financial well-being, Redington
- **Imran Razvi**, public policy adviser, the Investment Association
- **Paul Bannister**, chief executive officer, BlueSky
- **Annabel Tonry**, chair of the DC Investment Forum and client and consultant adviser, J.P. Morgan Asset Management
- **Chair: Louise Farrand**, executive director, DC Investment Forum



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Members should not be left to their own devices when they reach the age of 55

The panellists agreed that members should not be left to their own devices when they reach 55 and are able to access their retirement savings. This principle informed the J.P. Morgan trustee board's decision to introduce drawdown. Plans were already underway before the Chancellor's announcement, but freedom and choice gave the trustees additional momentum.

"Our decision was formed from the view that if someone has spent 30 years in this plan and we have spent all that time giving them extremely highly negotiated pricing and value, at the point when they have the most money, to say, 'Okay, you can go off now to the 1% fee environment' or whatever it might be, didn't seem like a particularly obvious solution. And as trustees that was something we wanted to avoid if we could," explained Rene Poisson, chair of the J.P. Morgan UK Pension Plan.

Through the J.P. Morgan drawdown solution, active and deferred members are offered a guidance service in the run-up to retirement. If they opt for drawdown, they can either proceed via a master trust or a SIPP.

"In both cases, there is a – you might describe it as a Morgan section – which provides exactly the same investment choices that are available in accumulation, and all our investment managers have agreed the fees we negotiate for accumulation pass through, so they get an institutional fee rate in drawdown. They also can transfer across with no friction cost, there's no buy/sell, it's done by re-registration. And we have negotiated an institutional wrapper fee, so they don't suffer the retail wrapper fee they would with a third-party solution," explained Poisson.

The size of the scheme helped when it came to negotiating these rates. "One of the advantages of the Morgan scheme is we are a £3.5 billion scheme, so our managers could decide whether they wanted to remain in the accumulation phase or not. Because participation on both sides of that divide was a prerequisite. It was not a difficult negotiation," said Poisson.

Helping members to have a smooth journey from saving into retirement was likewise a priority for master trust BlueSky, explains Paul Bannister, its chief executive. Coincidentally, the team at BlueSky were already building a drawdown option for members in 2014. They were on the final day of constructing the option when the then-chancellor George Osborne announced freedom and choice.

As a result, BlueSky were able to move fast. "We went live with our drawdown offering in May 2015, only a month after the announcement. We used an extension of our original target date funds that we use within the master trust – we use an AB Global strategy that is purchased off the shelf. The price of 75 basis points we get from them matches the price in the accumulation phase," explains Bannister.

"Overall, I think it is proving successful, but we are almost waiting for some competitors in the market. One of the problems at the moment is we can't be compared to anything. So, it's interesting to discuss it and see what other people are doing," says Bannister.

Bannister has been surprised not to see more interest in BlueSky's solution from trust-based pension schemes and wonders what is holding trustees back from introducing drawdown as an option.

Nathan Long, senior pension analyst at Hargreaves Lansdown offers some answers. Hargreaves Lansdown has been offering execution-only drawdown for around 15 years. Since freedom and choice, Long has witnessed a "massive shift" among retail providers. Where they were once cautious about drawdown, they have become much more bullish.

Hargreaves Lansdown is an exception to the rule. Although around 70% of its retiree clients have opted for drawdown post freedom and choice, the provider's clients are typically engaged investors. Drawdown should not necessarily be the new normal, said Long.



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- Paul Bannister

Retirement data may not tell the full story

Today's retirement data may not be a true reflection of people's behaviour. As Poisson points out: "We talk about drawdown, that tends to mean someone has moved to a product capable of drawdown. But actually, they may have taken the cash, parked the money, and they may in fact buy an annuity five or ten years from now. We have no idea today, and it's going to be a long time before we know what people's behaviour will be."

Long also thinks more considered thinking may lie beneath the headline figures. "We were quite interested by the FCA's retirement outcomes review saying that 94% of people doing drawdown aren't shopping around. We looked at the data of people who had done drawdown with Hargreaves Lansdown and 40% had transferred in a pension pot in the four years before that. So, the point is, we think they are consolidating in advance of going into drawdown and choosing their provider in the run-in, which is a sensible thing to do, instead of getting to the point and thinking, 'Oh crikey, who am I going to use?'"

Bannister and the team at BlueSky review the master trust's retirement data every month. Over a thousand people have moved into retirement since freedom and choice, and yet there is no discernible pattern, he reports. "You would think you would find people of a similar age, with similar assets, from similar career backgrounds doing similar things? Nothing."

Only one trend is clear, says Bannister. "Since we introduced drawdown, no one has taken an annuity. Not one member."

At first, the master trust worried that their member communications sounded biased towards drawdown – so they reviewed them and made edits. Yet still, members are not buying annuities.

Now, Bannister wonders whether the lack of appetite for annuities is due to the fact that BlueSky's core drawdown product targets an annuity at 75 anyway. "So, what we are saying is that if you go into drawdown, when you get to 75, hopefully the annuity you buy will be bigger than the one you bought today. But communicating that

to a member is almost impossible.”

Obtaining meaningful data about member decision-making from newer master trusts is going to take ten to fifteen years, estimated Bannister. The fund values that members will build are going to be so small in the short term that people are likely to cash out. But even this is not always the case, he explained.

“We thought we would see a pattern, but we haven’t. We have got people buying into drawdown with funds of £10k. But are they buying into drawdown or are they just parking the money? That’s what they are doing, they are parking the money for another day,” theorised Bannister.

Today’s figures show a propensity for people to take their DC pots as cash at retirement. This is likely to evolve over time, however. As Imran Razvi, public policy adviser at the Investment Association said: “A lot of people retiring at the moment have other income to rely on, and so cash possibly makes a lot of sense for those people. But if we move into a world where people are completely reliant on DC and that trend persists, from an income perspective, policymakers might have some more concerns I would imagine.”

“The jury’s still out on all this,” agreed Long. Part of the move away from annuities can be explained by the positive stock market conditions. “Nobody has had that shock that’s causing them to think, ‘Maybe drawdown wasn’t the right thing for me and I am going to move back to annuities.’”

Another issue is today’s uncompetitive annuity rates, added Long. “We think that if there is an improvement, there will be appetite for people to come back and buy annuities. For example, in January we had a huge surge in web traffic, which we always do, it’s January and everyone goes online and looks at their finances. They looked at annuity pricing and just wouldn’t buy at the prices that were available at that point in time.

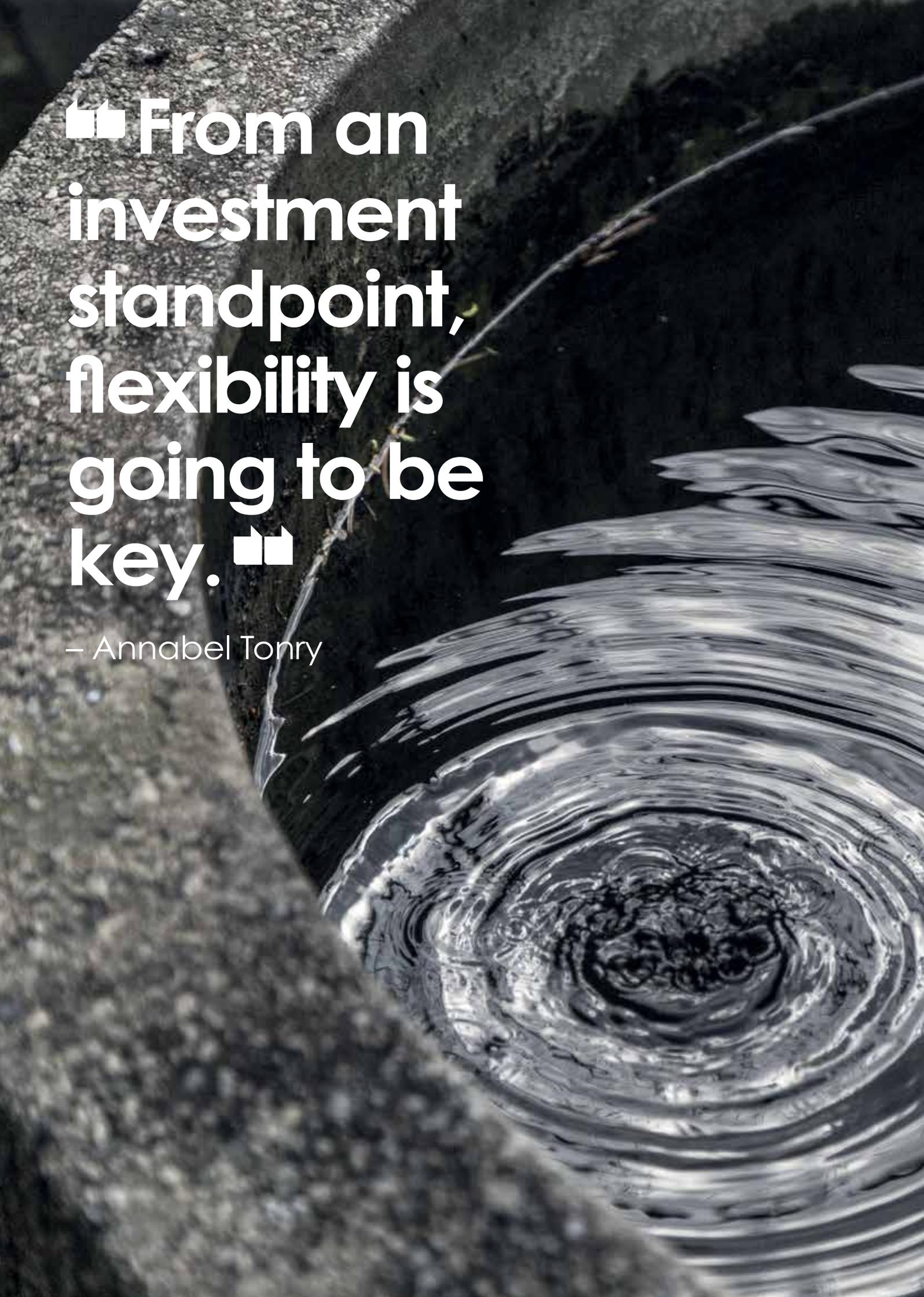
We think there is appetite for annuities, we just think people won’t buy at any price.”

Members clearly need support to navigate new and more complex paths to retirement. However, most trustees are reluctant to take on a larger governance burden, reported Redington’s head of DC and financial wellbeing, Lydia Fearn.

Fearn said: “We see a general trend for single trusts to move members into master trusts to try to remove some of the governance burden. It is a big responsibility for that trustee to manage that member up until potentially they die. That, I think, is causing a lot of concern – who is going to look after those members? I think robo-advice has some way to go – we have seen that take-up isn’t massive. At the moment, I can’t see a world where you have robo-advice and no human element. It is important to have that human element, but obviously that costs money and how do you facilitate that? Demand is brewing but it’s just not there yet. Until you see what people want to do, it is hard to then build a solution around it.”

She added: “Personally, I think we need to make some strides and move forward, we can’t just sit and talk about it, it is going to happen. It’s not going to happen tomorrow, but it is going to happen in five or ten years’ time. In years to come, we will see people with DC pots that are larger and more necessary to support their retirement than DB.”





From an investment standpoint, flexibility is going to be key.

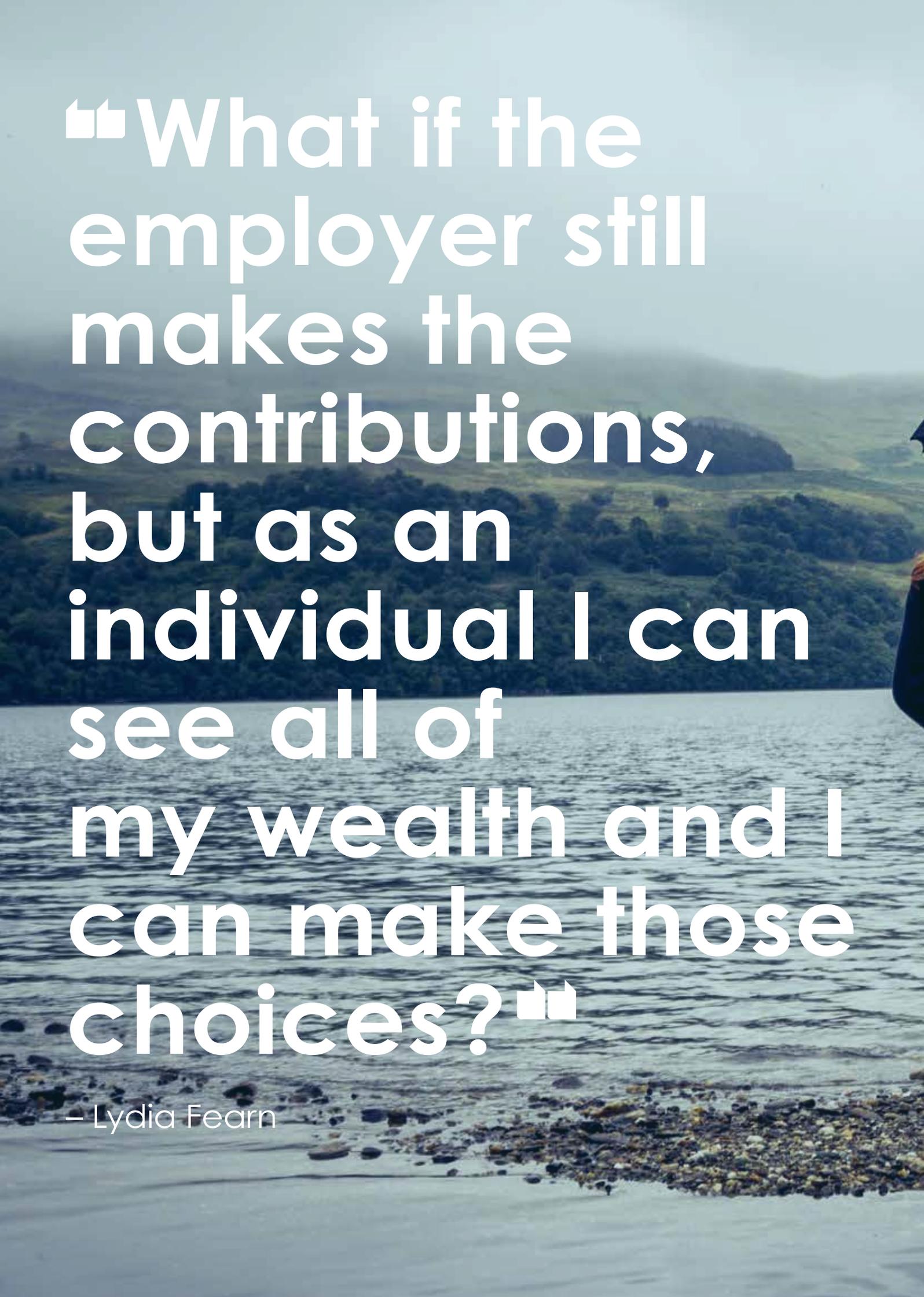
– Annabel Tonry



Flexibility will be key to navigating this brave new world

How people retired ten years ago may look very different to the landscape in another ten years, said Annabel Tonry, chair of the DC Investment Forum and client adviser at J.P. Morgan Asset Management: “It is a real challenge, but I think the key is thinking about flexibility. Part of the reason you will have seen a paucity of investment managers launching products into this market at the moment is there isn’t enough data yet about what people are doing as they approach retirement. From an investment standpoint, flexibility is going to be key.”

She added: “One of the challenges for investment managers is when you think about launching a product, you want to understand what the flows into that product are likely to be. Are you launching something that is going to have demand and sustainability over time? It is very difficult to be clear about where these flows are going to be coming from. In these initial phases, flexibility will be key and a range of products for people with different needs and asset pools to choose from as well.”



“What if the employer still makes the contributions, but as an individual I can see all of my wealth and I can make those choices?”

– Lydia Fearn



Closer links will be forged between the institutional and retail worlds, and more change is likely to come

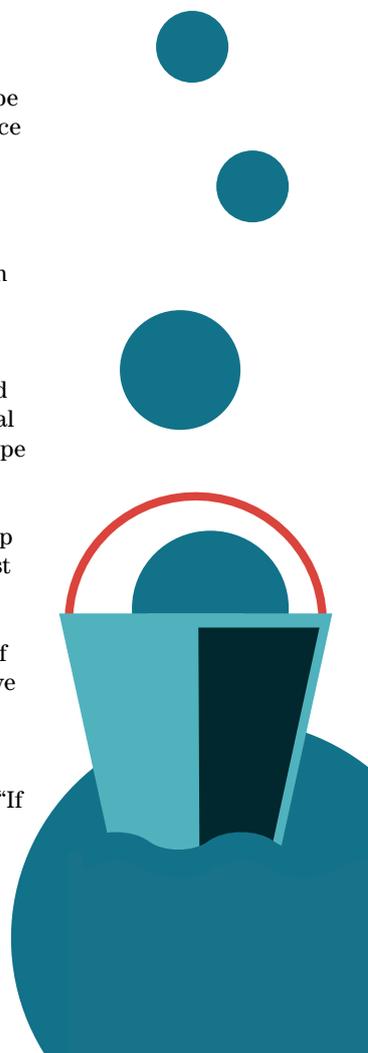
Retail and institutional worlds will become more closely linked in the years to come, the panel concluded. Why? Many trust-based DC schemes do not offer their members the ability to move into drawdown at present, which can lead to inefficiencies and tax penalties as savers try to withdraw their money, says Long.

Retail providers could also help trustees to engage savers when they retire, adds Long. “Trustees can definitely do the engagement piece, but working alongside a retail provider who is used to working with individuals from a wide range of backgrounds is going to be useful.”

Tonry added: “I think it will be useful to see a greater focus on individual, tailored glidepaths, be that through greater levels of usage of robo-advice or more sophisticated offerings that look at and take into account the specific circumstances of individuals. I can only assume that will need to mean a greater level of retail and institution collaboration – but I imagine that is further down the line.”

Fearn believes that member engagement is difficult in today’s DC environment. “When members are auto-enrolled, they are not attached to their savings. This is potentially a controversial view, but what if we created a more Australian-type culture where we decide where our money goes and take the employer out of that loop? So, for instance, as a member, I could have a relationship with BlueSky because that’s my decision to invest in that offering. What if we just removed the employer level, so the employer still makes the contributions, but as an individual I can see all of my wealth and I can make those choices? Until we get to something like that, I struggle to think about how we can improve engagement. Individuals just don’t feel connected.”

“We might not be far off that,” said Bannister. “If we do end up with only five or six master trusts then that is a possibility.”





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