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Savings & annuity products in the new pensions world



There is no one size fits all solution



- **That was yesterday's model !**
 - **Annuity, level, guaranteed 5, maybe a bit for spouse**
 - **Discredited because**
 - **All families are different**
 - **It was irreversible**
 - **It suited cliff-edge retirement, not today's gradual transition**
- **But most people**
 - **Will not have access to regulated financial advice**
 - **May be very confused by pensions**
 - **Can be blinded by too many options**

Broad Customer Groups



- **Less affluent – least engaged**
 - £40k in DC
 - Little other savings, likely to have debt at retirement
 - State Pension main source of income in retirement
- **Middle Britain**
 - Two in three have an old DB pension
 - £150k in DC
 - Will have other savings, mortgage paid off
- **Affluent – most likely to be advised**
 - £250k in DC, plus DB, other investments, no debt

What will people do from April ?



- **Less affluent – least engaged**
 - Single solution, non-advised
 - DC funds taken as cash up front, or instalments
 - Some may buy an annuity from inertia
- **Middle Britain**
 - More likely to be a mix of products
 - Some purchases may be advised
 - Access to DC funds will be important
- **Affluent – most likely to be advised**
 - Little change
 - Existing pattern of an advised single product likely to continue
 - Access to cash will be an important feature

What does Middle Britain want ?



- **Access to funds, to dip in when needed**
- **More money in the early years of retirement**
- **Certainty of covering basic living costs**
- **Security of not running out of money**
- **Flexibility to change if circumstances change**

Australian Concept – Bedrock income



- Bedrock income required
 - £18,000 pa, for the life of a married couple
- Desirable income, on top of the bedrock
 - £10,000 pa for the first 10 years of retirement
- New State Pension - £15,000 pa
- Joint Life Annuity - £3,000 pa
 - Cost £64,000
- Ten Year Annuity - £5,000 pa
 - Cost £45,000
- Drawdown - £5,000 pa
 - Pot £41,000

Total Pot £150,000

- **Mr Affluent - £250k in DC, plus some DB, plus savings**
- **He wants**
 - **£18,000 pa income from his DC pot**
- **Longevity Insurance**
 - **Deferred Annuity from age 85, £18,000pa**
 - **Cost £27,000** (Source : New York Life Guaranteed Future Income Annuity)
- **Drawdown**
 - **Invests £223,000 in a traditional portfolio**
 - **Draws off 8% pa between age 65 and 85 generating the required £18,000 pa income**

New whizz-bang products for UK ?

(These products already exist in USA)



- **Guaranteed income units**
 - Invested in a range of corporate bonds, will generate a steady income in the absence of defaults
- **Guaranteed Growth Units**
 - Invested in equity index funds, with an underlying ratchet guarantee that protects against market falls
- **Unconstrained units**
 - Invest in any of over 2500 funds on the platform
- **Longevity units**
 - Make single or annual payments to longevity units which guarantee income for life in old age

Secured Pension Unitised Retirement Tool

- **Cash out plan to spread cash over 2-4 years**
- **Traditional Annuity**
- **Fixed Term Annuity**
- **Income Drawdown**
 - **Regular payments**
 - **Fast access ad-hoc payments**
 - **Default fund**
 - **Retirement Income Multi Asset**

- **Traditional model**
 - **Equities to age 55**
 - **Ten year “lifetsyle” switching into**
 - **75% Bonds**
 - **25% Cash**
- **Flawed from April 2015 as**
 - **Many won’t buy an annuity**
 - **Many won’t retire at 65**
 - **Many won’t know what they’re going to do until at most a couple a years ahead of “retirement”**

A new way of thinking for investments



- Funds that take you *to and through* retirement
- Members need
 - Growth before and after retirement
 - More Income generating assets after retirement
 - Lower volatility
 - At outset
 - Around retirement age
 - In advanced old age
- Can be provided with an age and duration related multi-asset fund model

- **What outcome should employers be hoping for ?**
- **We want members to**
 - **Get through the process and draw their pension**
 - **Feel that they were in control and made their own choice**
 - **Know why they chose it**
 - **Understand what it's going to deliver them**
 - **Understand what's not guaranteed**
 - **Get good value for money**

McKinsey's 3x3 Rule



- **Choose from a set of three choices**
- **Then another set of three choices**
- **Followed by no more than a third set of three choices**

Example 3x3 Rule : Choice No 1



- **What sort of retirement income would you like from your pension plan ?**
 - **Take it all at once**
 - **Leave the money invested, draw a regular income with flexibility to take more or less**
 - **Give it to an insurance company who will give you a guaranteed income for life**

Example 3x3 Rule : Choice No 2



- **We've prepared three investment funds for you**
 - **Low risk, lots of cash and bonds, modest but safe returns**
 - **We suggest you draw 4% a year**
 - **Moderate risk, wide balance of investments but they may go down**
 - **We suggest you draw 5% a year**
 - **Higher risk, more exciting investments, hopefully will provide a better return but sizeable losses are possible**
 - **We suggest you draw 6% a year**

Example 3x3 Rule : Choice No 3



- Think about protecting yourself against living so long that your pension fund runs out
 - Single payment of £5000 to insurance company, who guarantee to pay you £200 a month starting at age 85
 - Regular payments of £25 a month to insurance company, who guarantee to pay you £200 a month starting at age 85
 - Do nothing, and rely on other sources of income if you outlive your pension pot

Somebody else seems to be going for the three way choice.....



What can we reasonably expect trustees and employers to do ?

- Here's your money, off you go
 - OR
- Access to carefully chosen solutions, with help and support throughout the transition to retirement
 - OR
- Ongoing management of flexible drawdown account for the remaining life of the pensioner



Minimum standards : taking the whole pot



- **Help with understanding how income tax works and why spreading over two or three years may help**
- **A cash fund to leave next year's instalment in**
- **Help with appreciating how much income a retired person will need to live on**

Actuarial Profession website has published a table showing suggested pensions for different occupations

Minimum standards : buying an annuity



- A simple pension fund statement, containing all the details an insurer will ask for to produce an annuity quote
- A panel of three annuity providers, with internet and telephone contact details chosen because
 - Their rates are good value
 - They are easy to deal with at purchase
 - Their ongoing service is good

“Protection beyond the failed OMO system”

- Access to a drawdown provider with
 - Simple fund range
 - Low charges
 - Suggested withdrawal rate
 - Slick operation for changing monthly payments or taking one-off lump sums
 - Ongoing reviews
 - Strong governance

Drawdown is not a “set and forget” option

- **“It is not from the benevolence of the butcher that we expect our dinner, but from his regard to his own interest”**
 - Adam Smith, 1776
- **An independent fiduciary, acting in the members’ best interests is even more important in retirement than in accumulation**
 - Schemes could offer drawdown within the same trust
 - Although employers may not be so keen
 - Mastertrust
 - IGC’s, with expanded role

- This will not all be sorted for April
- Market will evolve
 - Expect a range of innovative solutions
 - “First mover advantage” probably won’t apply
- Good employers will want to see their employees well looked after
 - They’ve usually paid in most of the money!
- Not a default, but trustees may have a “path of least resistance” in mind as a way to good outcome
- *Let’s share examples of best practice as they emerge !*



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