CAPITA

ACA Conference
Seminar C21
DC investment approaches – trends/changes in

5 February 2016

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For Professional Clients Only

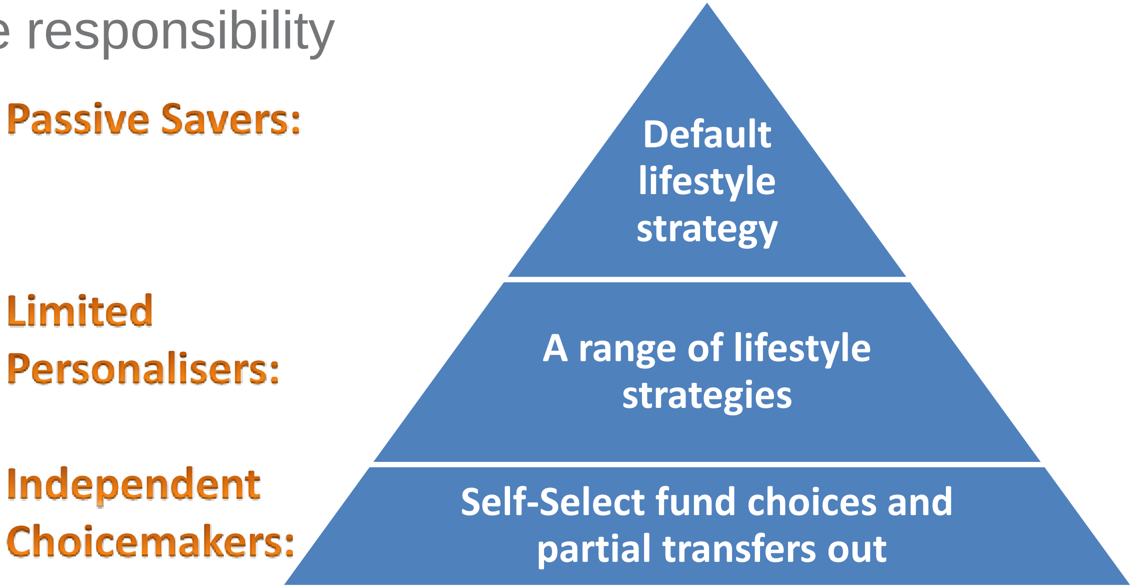
Agenda

- Recap from 2015 ACA presentation
- Member experience
- Market experience
- Some conclusions and trend predictions

Recap from 2015 ACA presentation

Immediate response (first year or so)

- Back to first principles
- Membership profile understanding: crucial
- Investment strategy changes: almost inevitable
- Member communication: more important than ever
- Lots to do, and a great opportunity to help members to take responsibility for their own money!



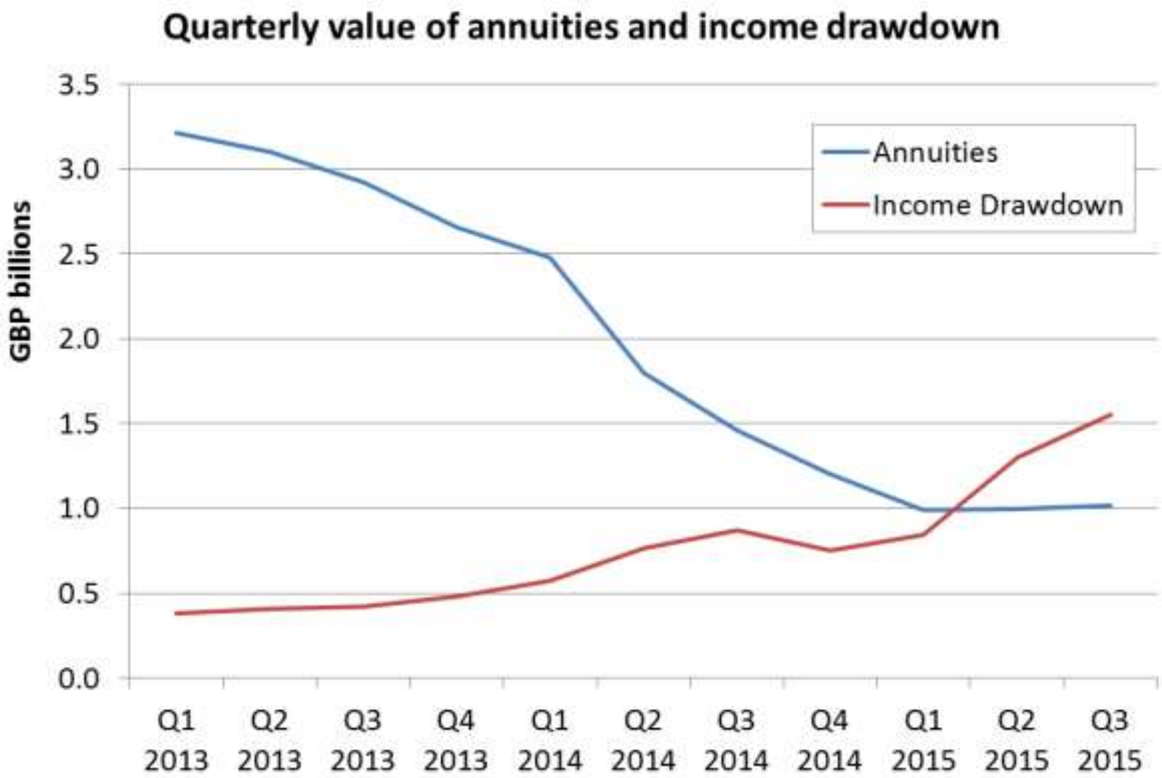
Recap from 2015 ACA presentation

Possible longer-term response

- Review strategies within two or three years
  - Recognise current action is probably a stop-gap
- Member experience:
  - Investment choice as expected?
  - When do members take the money?
  - What do members do with the money?
- Market experience:
  - Increased move towards using investment platforms?
  - Increased move towards index-trackers?
  - Smoother link between collective and individual arrangements?
  - Mis-selling?
  - Innovation around continued investment/flexible income options?
  - Increased use of target date funds?
  - Innovation around annuity options?

Member experience – the first six months…

Options taken by individuals



Q2 +Q3	Amount	
Annuities	£2.2bn	23%
Income Drawdown	£2.8bn	29%
Cash	£4.7bn	48%
Total	£9.7bn	100%

Annuities less popular in favour of cash and income drawdown – found a bottom, or a pause in the trend? Distorted by “dash for cash”, “wait and see”, and expectation that yields are too low and will rise very soon…..?

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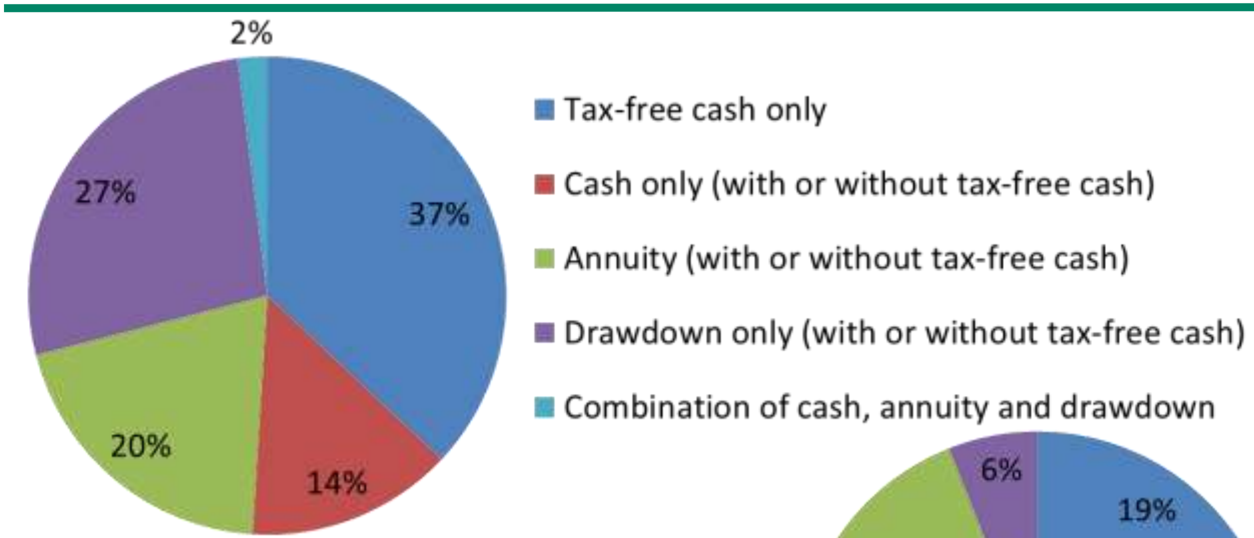
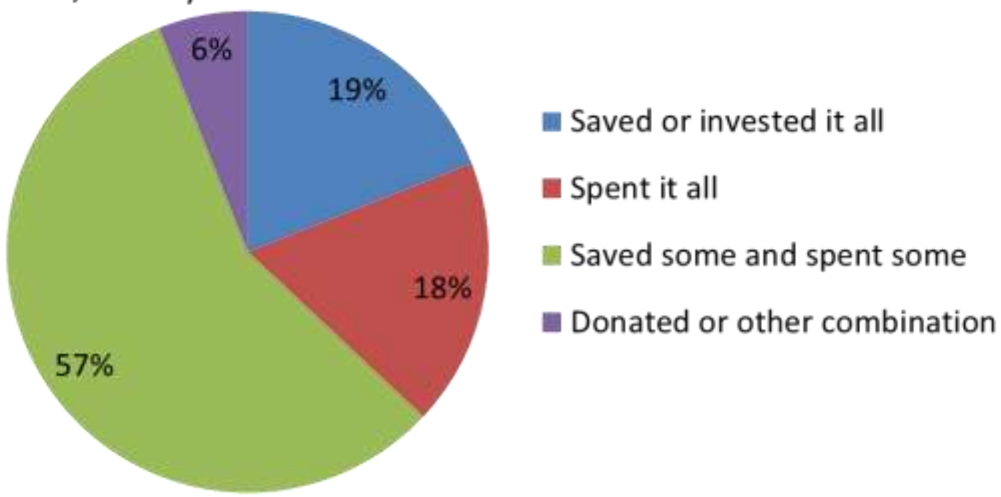
Source: Association of British Insurers

Member experience – survey in summer 2015

Not all cash spent on Lamborghinis…..



Have they splashed the cash?:



Different dataset, but broadly similar experience as for the ABI (first pie chart)

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Source: PLSA

…or was it?

Sales of Lamborghinis race to new record

theguardian

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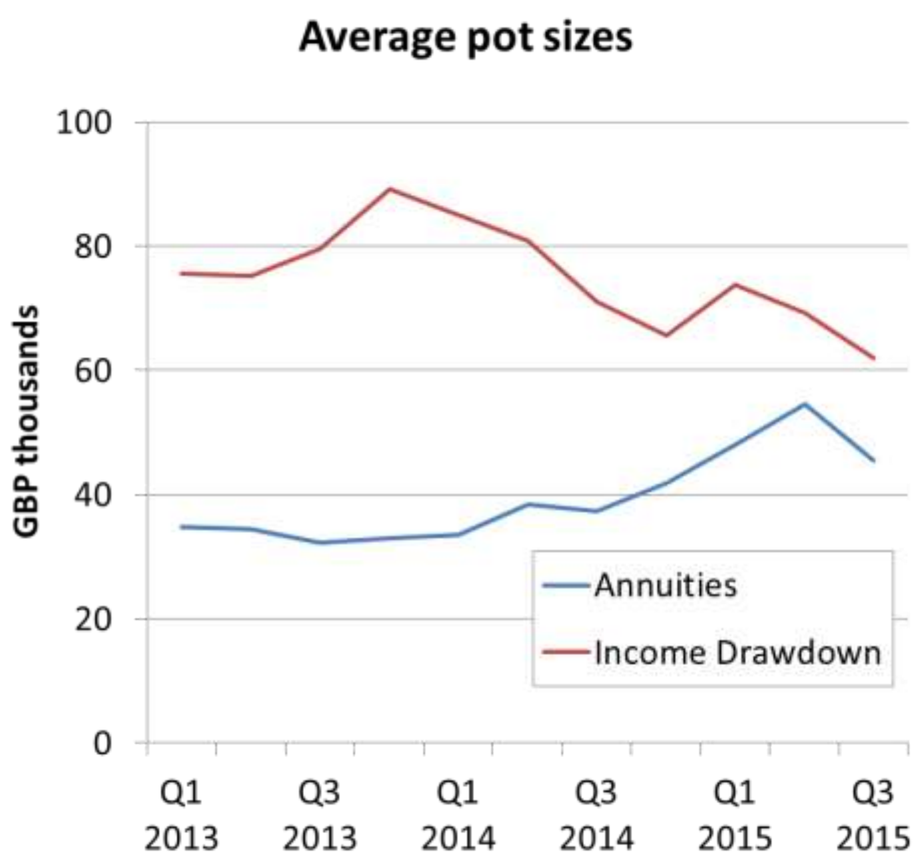
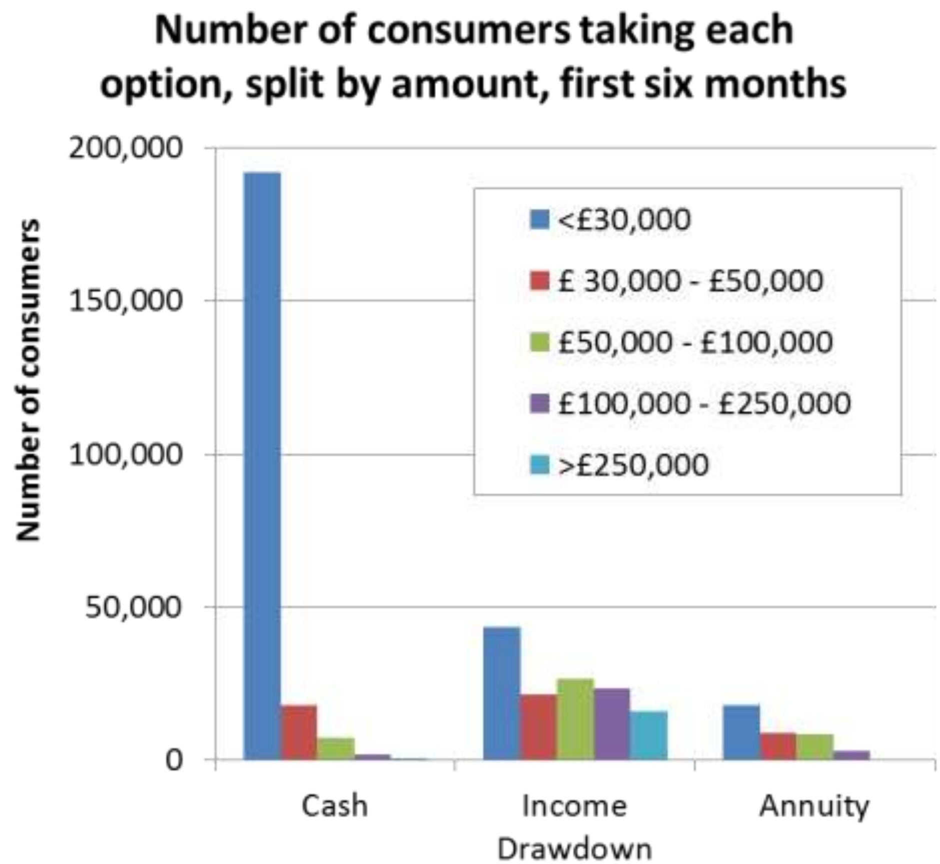
Source: The Guardian, Friday 11 September 2015

Member experience – the first six months…

Size of pots for each option





Average cash lump sum payment of c£15,000 (Q2 + Q3)
Smaller pots taken as cash and larger pots 'invested' – sounds quite sensible!

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Source: Association of British Insurers and FCA

Member experience - providers

Our pension experts dealt with over

60,000 calls

in the first seven weeks

64% of customers

with pots over £50K are taking only tax-free cash

Source: Standard Life

134% increase

in the number of people asking for retirement quotes

Helpdesk calls are up

26% from last year

with calls taking longer

Source: Aegon

58% of people

over 55 in a DB scheme say they will **not** transfer their DB benefits

General increased level of employee engagement

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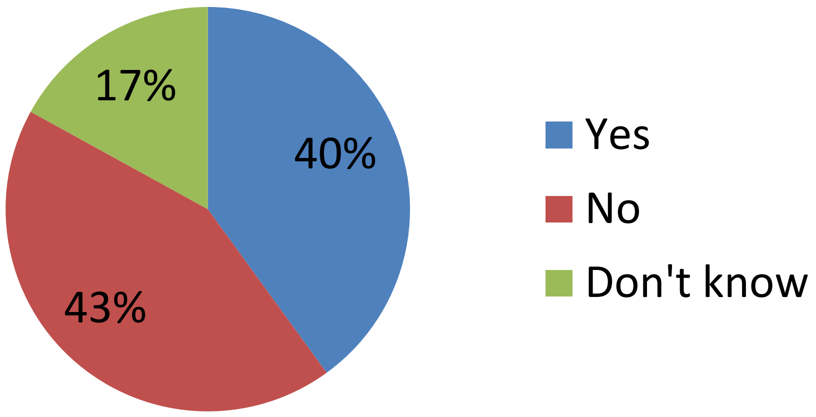
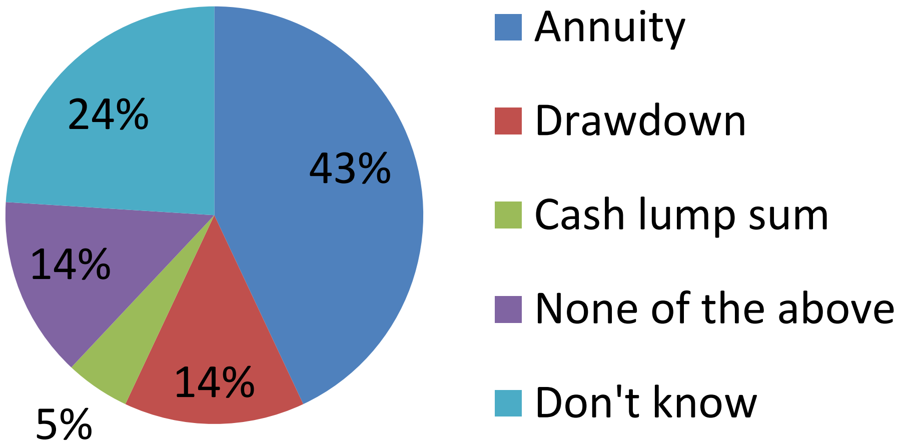
Member experience – survey of employers

- Do your employees have a choice of glidepath covering the three core retirement options?



- If no glidepath is selected by the employees, what retirement income option will the default investment option be targeted to?



Actually, sounds like quite a lot of progress made so far, but lots more to do….

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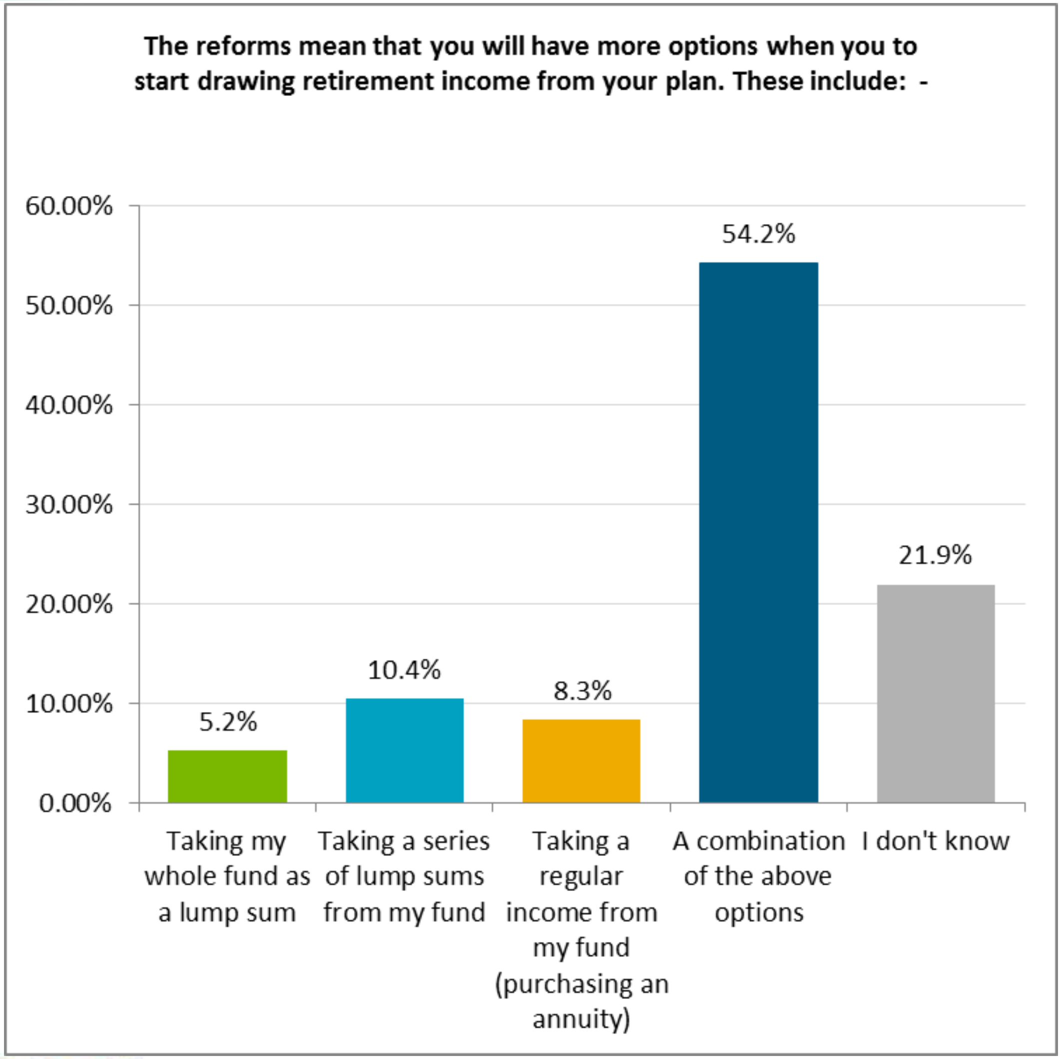
Source: WEALTH at work pension changes survey 2015 (data collected summer 2015)

Member experience – survey of members

For one particular large scheme



Relatively engaged members (ie they answered the survey) expect to use a combination of the different options available.

What is appropriate for default members?

Members want a combination, but will it really all be provided through this one plan?

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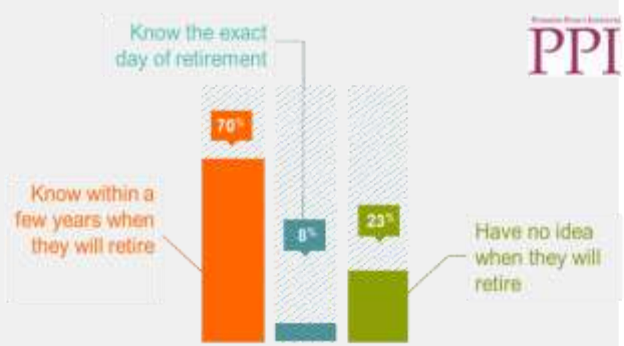
Source: Capita

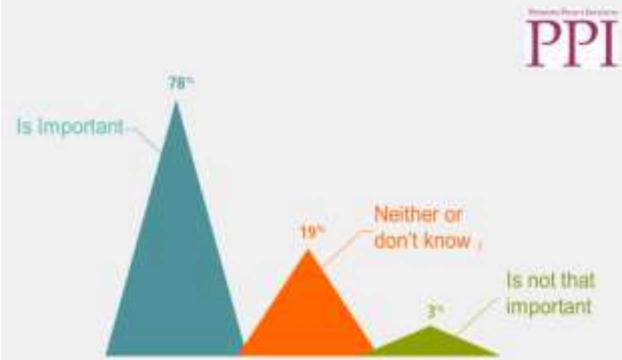
Member experience – pre April surveys still used

Q : Do you know when you are going to retire?

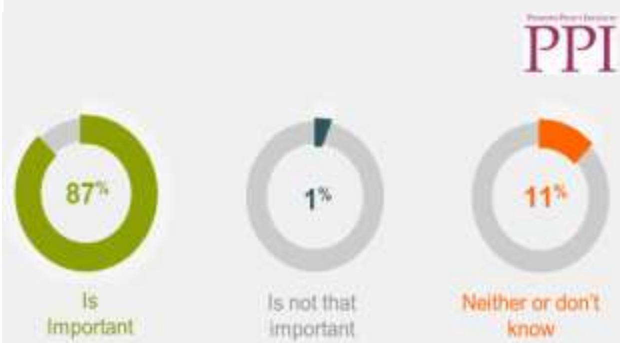


Q : When do you want to make a decision about your savings?

Q: How important is a strategy that is flexible about when you retire?



Q : How important is a strategy that is flexible about how you use your fund on retirement?



Member education is key

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Source: Opinium, August 2014. Survey of more than 1,000 DC savers. © AB.

Member experience – anecdotal trustee evidence

- Increased focus on membership profile
- Introduction of alternative lifestyles
- No clear direction on design of default lifestyle (and often scheme-specific), and fairly relaxed about ‘taking one step at a time’
- Distinction usually made between majority and ‘default members’ (no longer the same thing)
- Opportunity taken to improve lifestyle design and self-select range
- Desire to improve future-proofing (eg platforms)
- Limited impact of charge cap in most cases
- Limited provision of new flexibilities (eg drawdown) within scheme
- Big push on member communication

Market experience

Bullish headlines after 2014 Budget

THE TIMES

YOUR PENSION • YOUR NEST EGG • YOUR ISA

The savings revolution

Osborne launches biggest pensions reform in a century as he targets grey vote

£10,500 1p £15,000 55% £0.5m 24p

5p DAILY EXPRESS

MADELEINE BREAKTHROUGH

Police hunt intruder who attacked five other British girls in Portugal

PENSIONS AND SAVINGS JOY FOR ALL

Chancellor's great news for 'makers, doers and savers'

BUDGET 2014 AT A GLANCE

FULL COVERAGE

Daily Mail FEMAIL MAGAZINE

Millions freed from annuity trap

ISA limit soars to £15,000

High-yield savings bonds for the retired

PENSION POWER TO THE PEOPLE

Finally, the Chancellor stands up for savers!

METRO

If the Pub Landlord did budgets

SO HOT, THEY'RE COOL

RIMMEL

THE Sun

2 FREE TICKETS

Rompin' Van Persie

MADDIE

A BUDGET FOR SUN READERS

WIN-GO!

1 TAX ON BINGO HALLS HALVED

2 2 PENCE OFF PINT OF BEER

3 PENSIONERS CAN CASH IN

4 HELP-TO-BUY EXTENDED

5 EXTRA £500 TAX-FREE PAY

6 ISA LIMIT UP TO £15,000

7 A MILLION MORE JOBS

8 AND FREEZE ON A WEE DRAM!

BUDGET 2014

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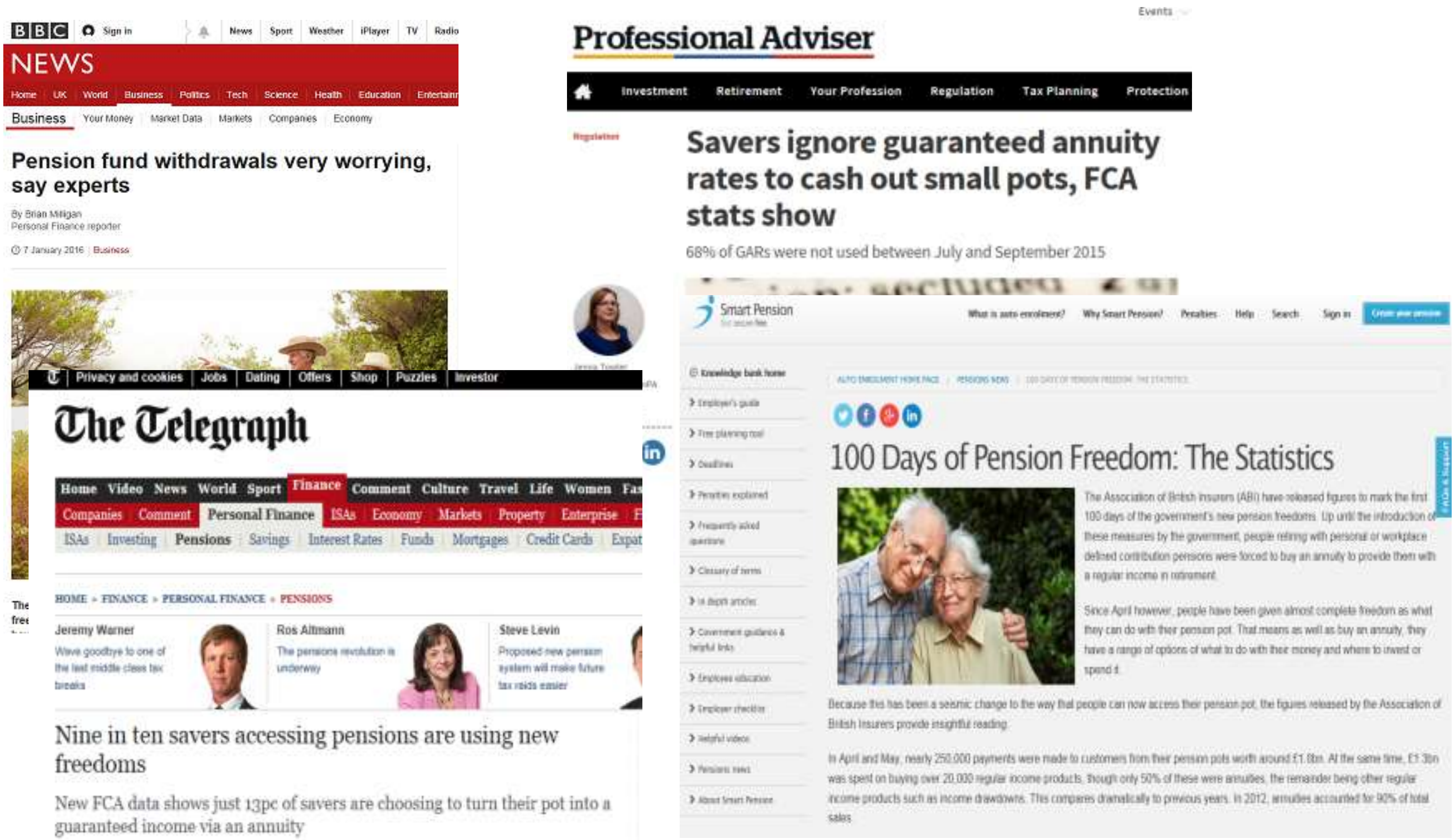
Market experience

More cautious after April 2015



BBC NEWS

Business

Pension fund withdrawals very worrying, say experts

By Brian Milligan
Personal Finance reporter

7 January 2016 | Business

The Telegraph

HOME › FINANCE › PERSONAL FINANCE › PENSIONS

Jeremy Warner – Wave goodbye to one of the last middle class tax breaks

Ros Altmann – The pensions revolution is underway

Steve Levin – Proposed new pension system will make future tax raids easier

Nine in ten savers accessing pensions are using new freedoms

New FCA data shows just 13pc of savers are choosing to turn their pot into a guaranteed income via an annuity

Professional Adviser

Savers ignore guaranteed annuity rates to cash out small pots, FCA stats show

68% of GARs were not used between July and September 2015

Smart Pension

100 Days of Pension Freedom: The Statistics

The Association of British Insurers (ABI) have released figures to mark the first 100 days of the government's new pension freedoms. Up until the introduction of these measures by the government, people retiring with personal or workplace defined contribution pensions were forced to buy an annuity to provide them with a regular income in retirement.

Since April however, people have been given almost complete freedom as what they can do with their pension pot. That means as well as buy an annuity, they have a range of options of what to do with their money and where to invest or spend it.

Because this has been a seismic change to the way that people can now access their pension pot, the figures released by the Association of British Insurers provide insightful reading.

In April and May, nearly 250,000 payments were made to customers from their pension pots worth around £1.8bn. At the same time, £1.3bn was spent on buying over 20,000 regular income products, though only 50% of these were annuities, the remainder being other regular income products such as income drawdowns. This compares dramatically to previous years. In 2012, annuities accounted for 90% of total sales.

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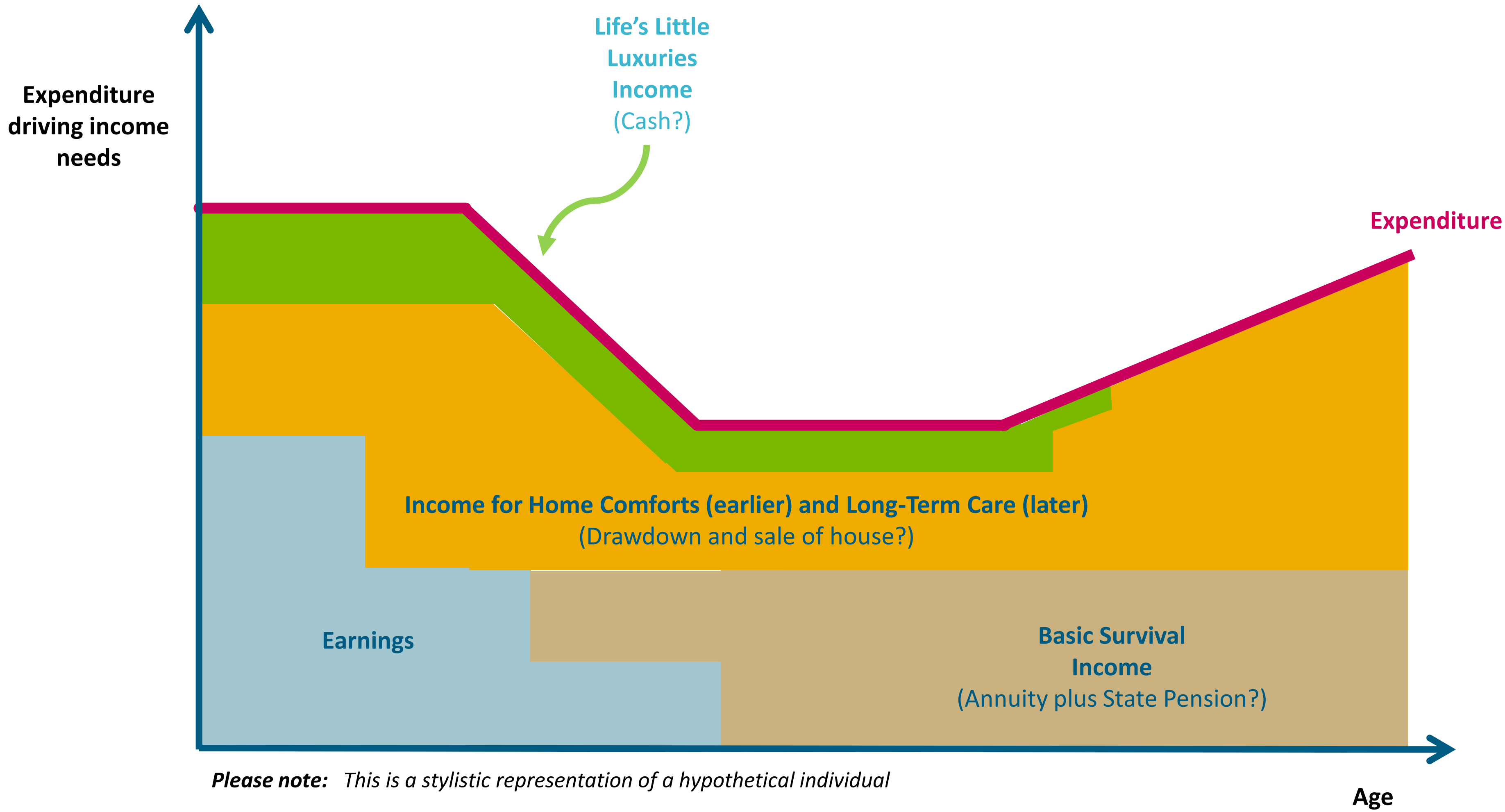
Market experience – going back to basics

Typical post-retirement expenditure and income

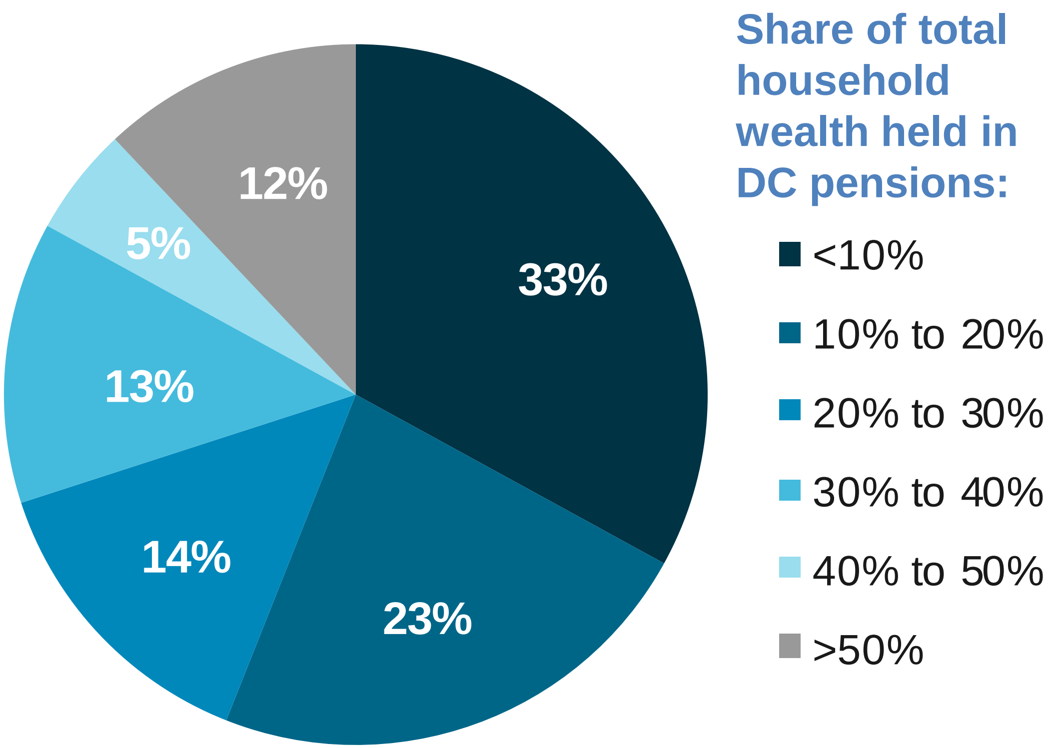


Please note: *This is a stylistic representation of a hypothetical individual*

Source: Capita

Market experience

Pension wealth is only part of the answer



How will this change?

+ DC flexibilities attractive
+ Auto-enrolment
+ Perceived reduced threat of confiscation (eg divorce or tax)
+ Buy-to-let discouraged
+ Secondary annuity market
+ Closure of remaining DB schemes/DB to DC CETVs
- New flat rate pensions tax?
- Further reductions in AA and LTA?
- End of contracting out
- Higher costs and governance
- Poor quality default due to lower charge cap?
- Capping of tax-free cash sum?

Greater recognition that pension wealth is only a proportion of total wealth…

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Source: LGIM/IFS

Market experience

Reclassify investors by use of funds rather than by size of pot

Top Up Saver

Drawdown over a known (and short) period

Retirement Fund Solution

Investment horizon appropriate multi-asset fund

Retirement Income Saver

Optimal income over whole retirement period

Retirement Fund Solution

Income paying multi-asset fund from age 55-75 followed by an annuity

Legacy Saver

Retain capital and receive a predictable income

Retirement Fund Solution

Multi-asset fund, potentially income paying

...leads to thinking about pension savers in different ways...

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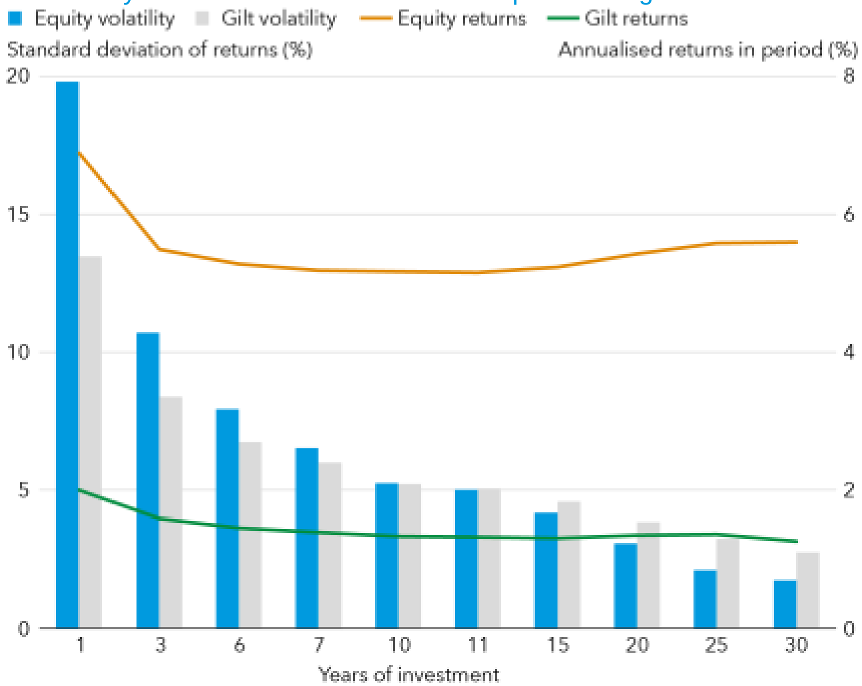
Source: AB

Market experience

Reviewing what we think of different asset classes

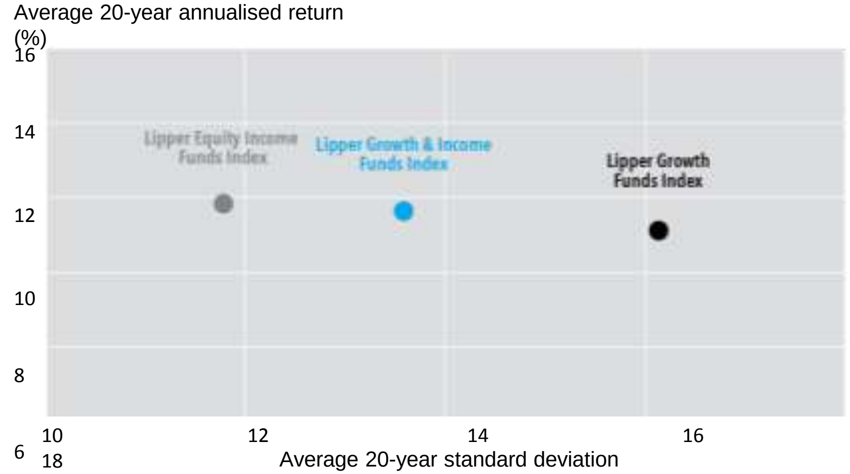
Risk and return over different timescales

UK volatility and annualised real return of equities and gilts 1900-2013



Sources: COURTIERS, Analysis of Barclays Equity Gilt Study 2014

Income-oriented equity strategies: strong returns with lower volatility



Average annualised returns and standard deviations for the rolling 20-year periods from 31 December 1970 to 31 December 2013. Past results are not a guarantee of future results. Volatility is calculated at net asset value, using annualised standard deviation (based on monthly returns), a measure of how returns over time have varied from the mean; a lower number signifies lower volatility.
Sources: Lipper, Capital Group

...leads to thinking about asset classes in different ways

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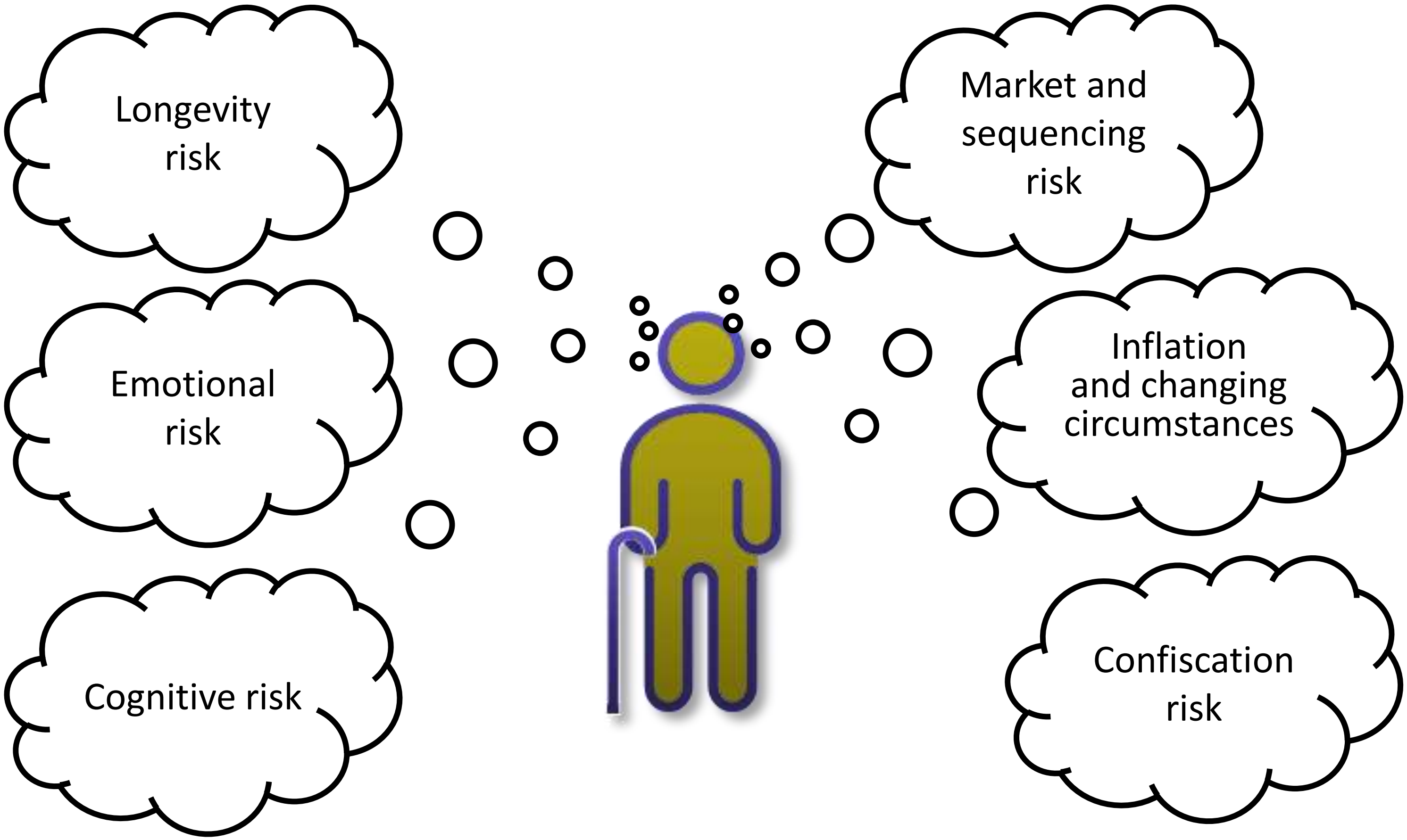
Source: Capital Group

Market experience

Identifying the risks can help to identify the solutions



Some of these risks can still only be addressed by an annuity, particularly for older retirees

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Source: Just Retirement

Market experience – investment options

- Existing funds still available for income drawdown:
  - Multi-asset (eg diversified growth and absolute return bonds)
  - Income (eg dividend yield)
- Limited new funds created:
  - 'Cheap diversified growth'
- GPP providers switch to target continued investment for default and are being more pro-active than trustees in offering DC flexibilities
- Target date funds switch to target cash/income drawdown for default
- Lifetime annuities still available, but as yet no innovative alternatives
- No material progress in bringing together institutional and retail platforms

Understandably, the widely expected innovation revolution has been limited so far. Providers have moved quickly to adopt income drawdown as the default; trustees have been slower to do so, but maybe they are just being more cautious?

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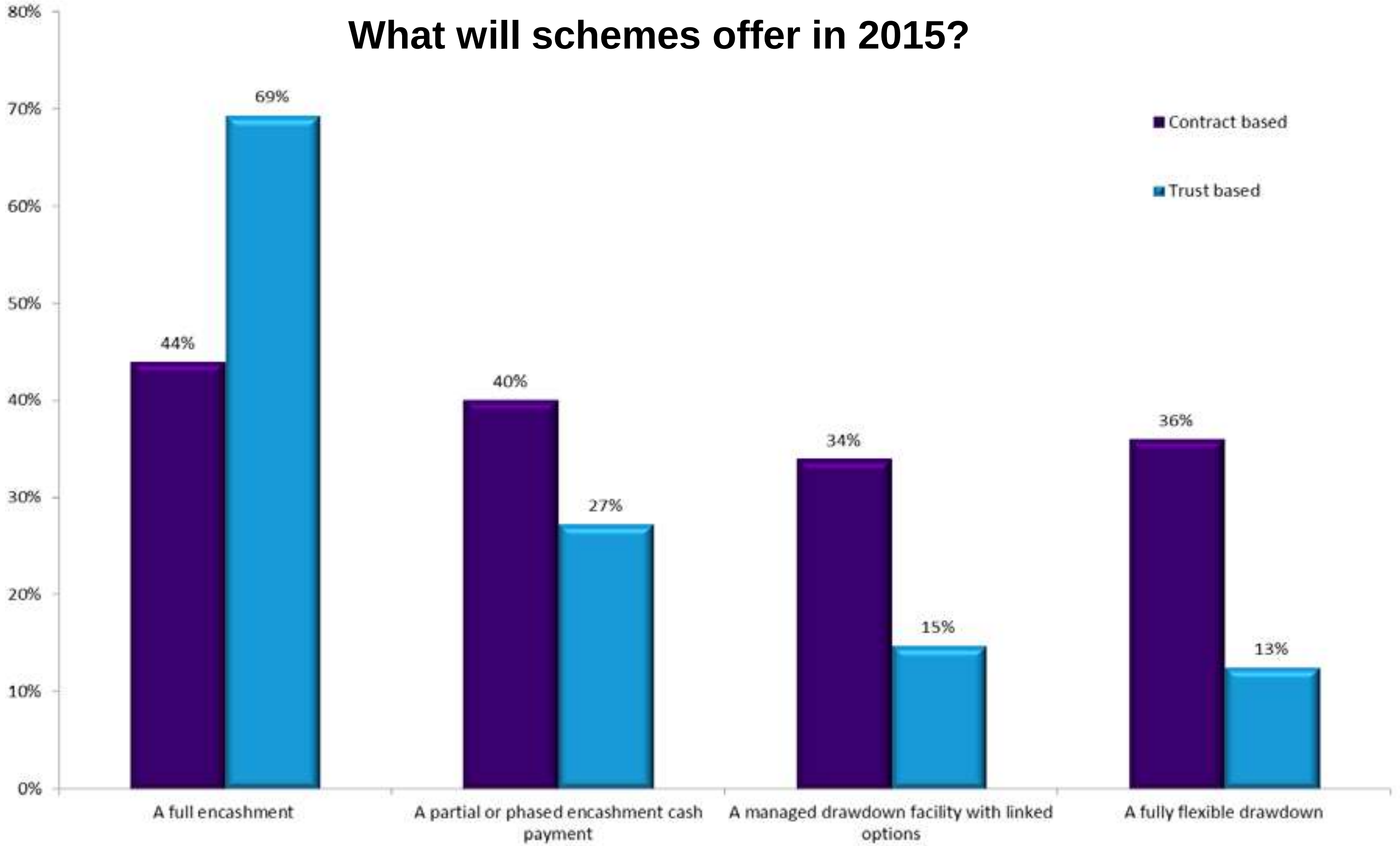
Market experience

Trustees more reluctant than GPP providers to adopt flexibilities



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Source: PLSA, Pension Freedoms: Breaking the deadlock, August 2015
Base: DC schemes trust based (88) SC schemes contract based (50)

Some conclusions and trend predictions

Accelerated use of platforms for trust DC

Focus on cost accelerates use of index-trackers, but is cheap also value for money?

Accelerated move from trust to contract (and death of small DC trusts)

75 is the new 65!

A thriving IFA market, but do actuaries have a better skillset?

Pension wealth falls in favour of ISAs/property/non-regulated investments

There will be some horror stories – will the Govt hold its nerve?

Further AA and LTA reductions

More fiduciary DC

The rise and rise of Mastertrusts

A combination is better and there will eventually be some innovation from insurers…

More focus on overall wealth, but by whom?

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