JUST.

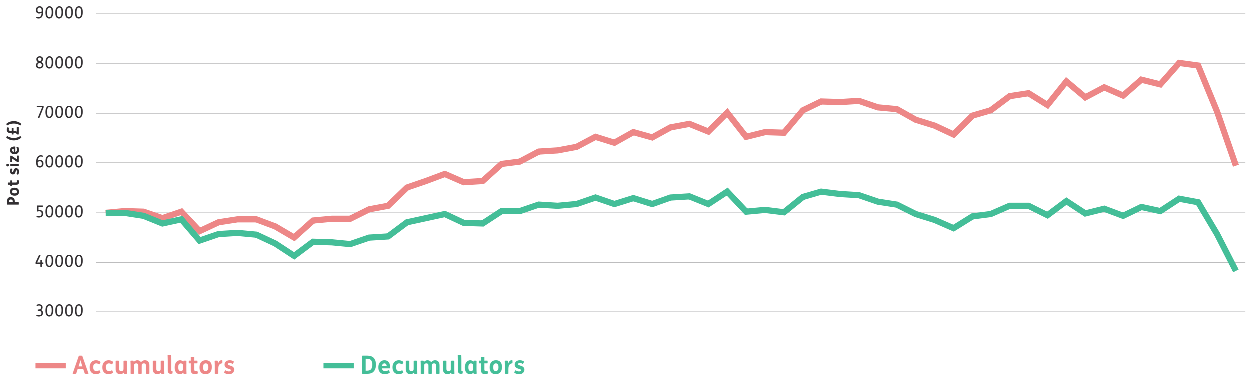
PENSION 'FREEDOM AND CHOICE'

THE FIRST FIVE YEARS

Pension 'freedom' is popular, but is it working? We highlight some key points to help inform the debate.

1. Headwinds and tailwinds. The challenge facing decumulators.

Accumulators vs decumulators

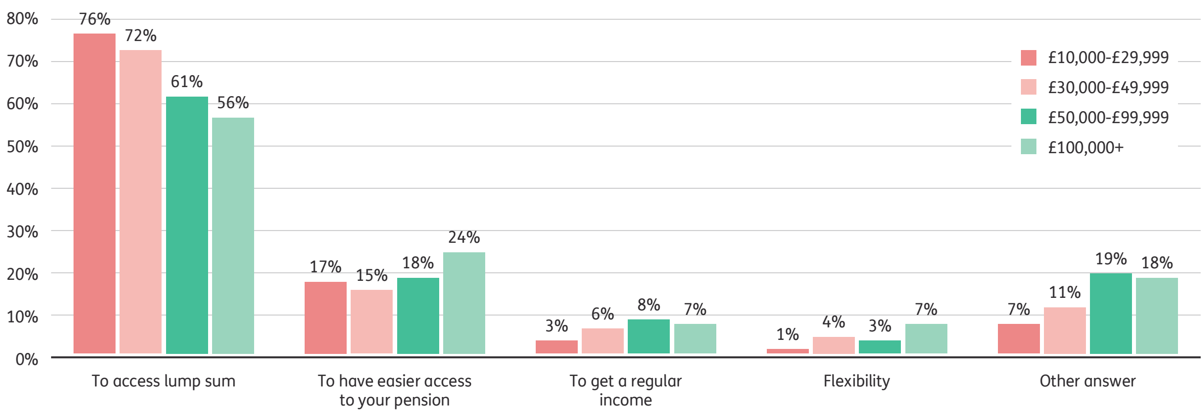


Performance figures in months from 6/04/2015 to 19/03/2020, starting at £50,000, excluding adviser/platform fees. Data: HSBC All-Share tracker fund.

Extracting income weighs heavily on potential returns. This chart shows how a £50,000 investment in a simple low-cost UK All Share tracker fund performed for accumulators (adding £200 a month) compared to decumulators (extracting £200 a month). While the accumulator saw strong returns in the early years, the decumulator has removed value as quickly as it can build. The sharp recent drop is a reminder that financial markets can fall as well as rise. The £200 a month withdrawal was initially a 4.8% withdrawal rate but now represents 6.3% which is higher than most experts think is sustainable over the long term.

2. Pensions are primarily to provide income in retirement, right?

Reasons for moving into drawdown, by pot size

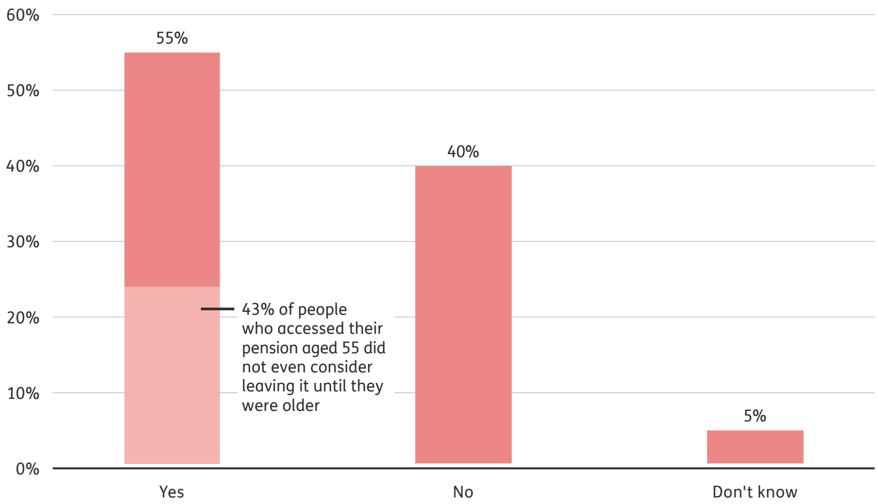


Source: https://www.fca.org.uk/publication/market-studies/ms16-1-3-annex-5.pdf

Pensions are tools to provide people with income to live on during retirement so is that how they are being used? Not according to the FCA who found that among non-advised customers entering drawdown, most were far more likely to suggest pensions were a way to access a lump sum of cash than to suggest they wanted to provide regular income.

3. What's the rush?

Thinking of the pensions you accessed in the last two years, were you aged 55 when you first did this?

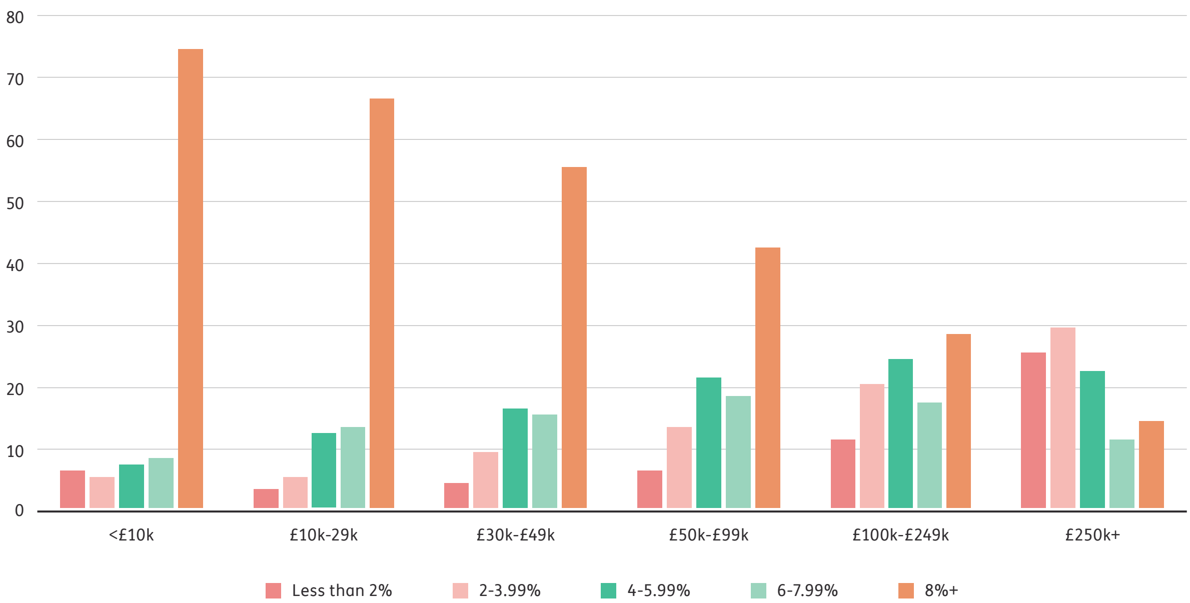


Source: FCA Financial Lives

Most people accessing their pensions are doing so at the earliest possible opportunity. A large number of those (43%) did not even consider waiting until they were older. Pension money taken early will not be available to provide income later. Making up the shortfall may not be possible due to the strict Money Purchase Annual Allowance rules and the fact that many people are forced to give up work early due to redundancy or ill health.

4. Are people taking unsustainably high levels of income?

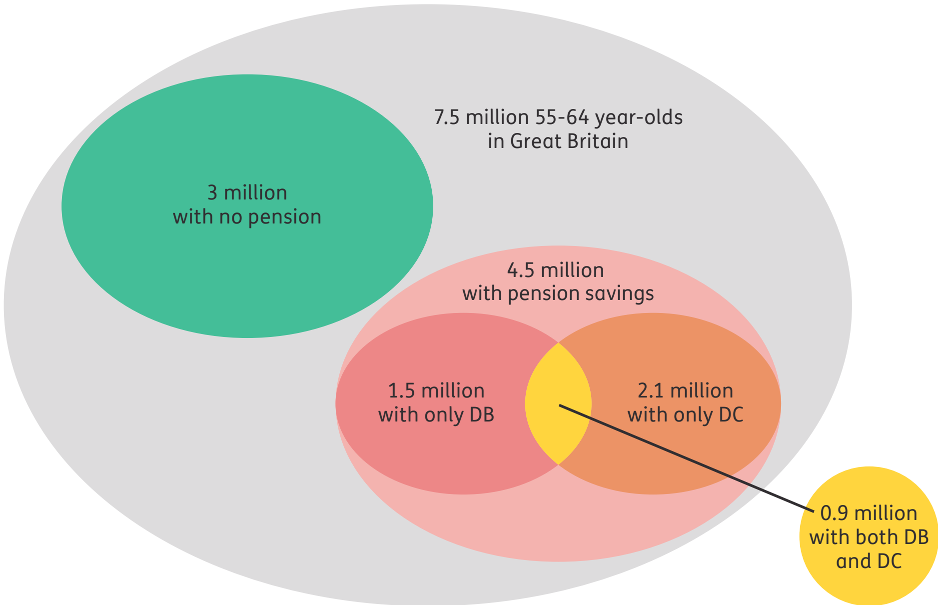
Income withdrawal rates by pot size in %



Source: FCA retirement income market data, 2018/19

In its paper **'Can we help consumers avoid running out of money in retirement?'** The Institute and Faculty of Actuaries suggested a 'safe withdrawal rate' of 3.5% for a 65-year-old or 3% for a 55-year-old. FCA figures reveal the majority of drawdown investors with funds worth up to £250k are withdrawing far more.

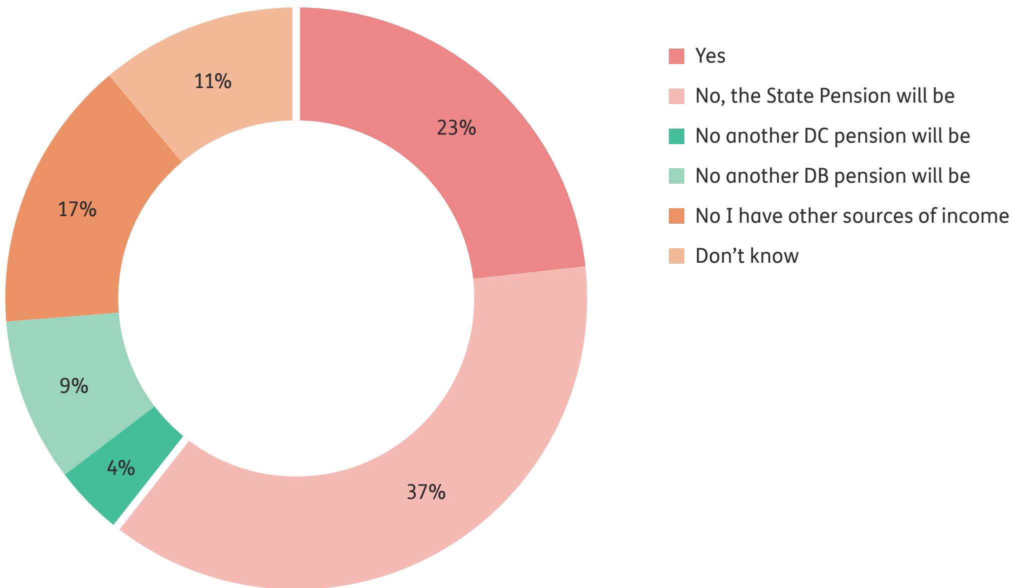
5. Can drawdown investors afford to take high levels of income because they can fall back on a DB pension?



Source: ONS Pension Wealth in Great Britain 2014-18: individuals with pensions not yet in payment

There is very little research showing how people's pensions look in aggregate so it is guesswork to suggest how many can afford to deliberately run down a DC pension pot by making unsustainably high withdrawals because they have other private secure income to fall back on. ONS data shows that of the 7.5 million people aged 55-64, only 12% have both a DC and a DB scheme.

6. Is the pension that people have accessed going to be their main source of income?

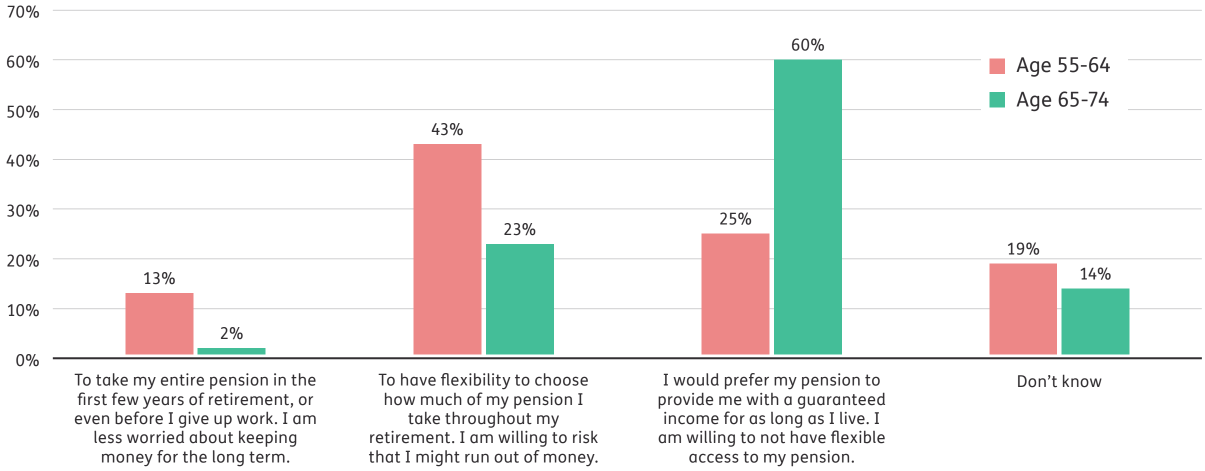


Source: FCA Financial Lives - DC pension accessed in the last two years

People who have accessed a pension are likely to rely for their main source of income in retirement on either the pension they have accessed (23%) or on the State Pension (37%). This strongly suggests that the pots people are accessing will form an important part of their retirement income rather than being an inconsequential holding among other assets. Only 4% said they had another DC and 9% a DB scheme that would be the main source of retirement income.

7. Will people end up regretting the choices of their younger selves?

When thinking about taking money from your pension, which of the following approaches do you prefer?

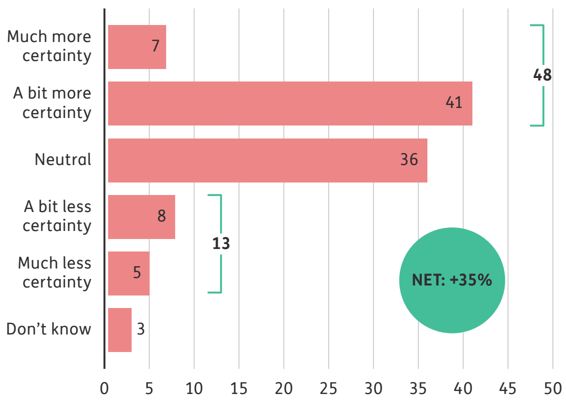


Source: FCA Financial Lives. People who accessed a pension in the last 2 years.

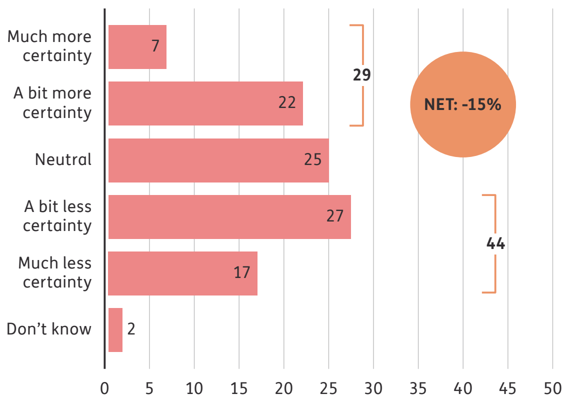
Attitudes towards using pension money change dramatically over time, as the views of those who have accessed pensions show. Younger cohorts, many of whom will still be working, prefer early and flexible access to the cash, even if it means running out of money later. Older cohorts, those most likely to be relying on pension income to pay their day to day bills, overwhelmingly want a secure lifetime income. Pension money taken earlier is not available later.

8. Have pension freedoms created more or less certainty for consumers? Depends which consumers....

'High Net Worth' Consumers



'Middle Britain' Consumers

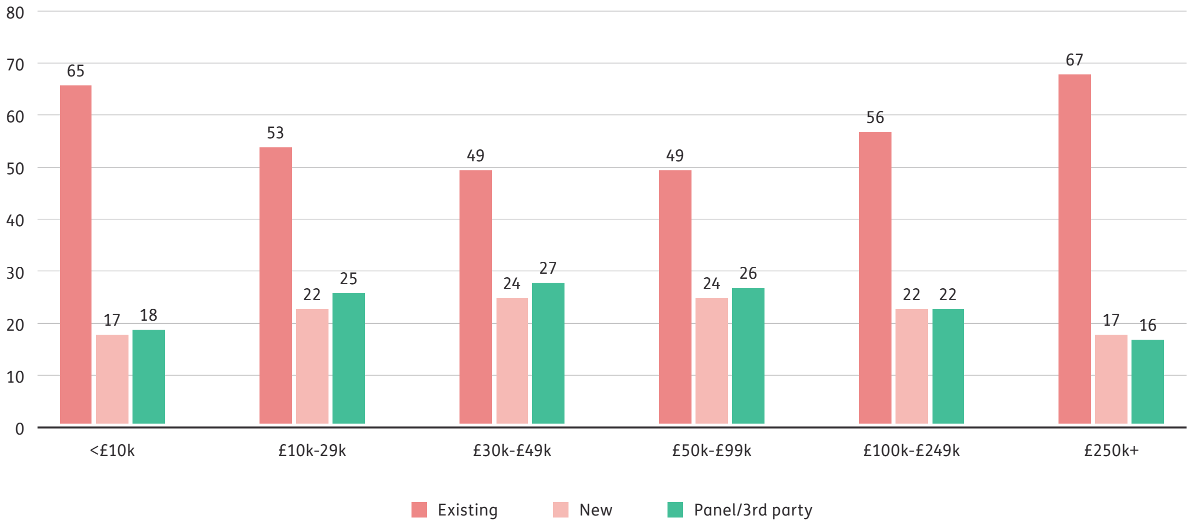


Source: Views of delegates at Just Retirement Leaders Annual Summit 2020.

They've given high net worth consumers far more certainty about what to do with their pension savings, but pension freedoms haven't been nearly as helpful for middle Britain.

9. Are drawdown investors shopping around and switching providers?

Measure of how many drawdown customers (%) continue with their existing pension provider rather than move to a new one



Source: FCA retirement income market data, 2018/19

Before pension 'freedom and choice' it was recognised that consumers weren't shopping around for the best deals and ending up with poor value plans. Five years into pension freedom, the problem persists. For those who do not take professional advice, comparing providers has become more complex.

10. How does the regulator review the 'freedom and choice' landscape?

The FCA has embarked on an ambitious programme to address some of the issues it sees emerging in the early years of the new rules. The Retirement Outcomes Review identified that many consumers "are focused only on taking their tax-free cash and take the 'path of least resistance' when entering drawdown". Last year the FCA announced changes to "stop up to 100,000 consumers a year losing out on pension income when they access the pension freedoms". Among its solutions are:

- **Pension Wise –** encouraging higher take-up of the government's highly regarded free, independent and impartial pension guidance service.
- **Investment pathways –** to encourage better investments and discourage people defaulting into cash.
- **New rules on 'wake up' packs –** earlier contact to discourage pension 'dipping' at age 55.
- **Revised communications –** to deliver clearer information on key factors such as charges.
- **Better annual statements –** to encourage people to see pensions in an income frame rather than as lump sums.
- **Stronger scrutiny of DB transfers –** to address concerns that many transfers are not in the clients' best interests.
- **Anti-scam activity –** to warn people against losing their retirement next eggs to scammers.