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ROUNDTABLE

MASTER TRUSTS & GPP DEFAULTS: ROUND TABLE

– THE PRICE OF LOW COST
– DEFAULT DILEMMAS

IN ASSOCIATION WITH

LGIM

ROYAL LONDON

SCOTTISH WIDOWS

DIVERSIFYING THE MIX

We need more data to fully understand whether expanding DC schemes into illiquid assets makes sense for members' pots

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What will it take for the UK defined contribution (DC) sector to come to terms with higher charges? And is the concept of paying higher charges for a richer suite of investment options even a good one?

It is a debate as old as the hills – rehearsed through the active v passive debate for decades. But nowadays we aren't talking about the skill of asset managers and their crystal balls in picking those listed equities that they think will beat the pack. Now the conversation is about whether to embrace a more diverse range of assets including illiquids with considerably higher charges than trackers.

The fantastic returns delivered by equities in the decade following the global financial crisis made life easy for those charged with constructing portfolios for DC pension savers. Equity performance was so strong that it was hard to justify investing elsewhere, certainly for younger savers, but also for those still not far from retirement. Equities probably still are the principal go-to asset class for those with decades to go until they access their pension. As one speaker pointed out at the round table the subject of this supplement, there appears to be no correlation between the cost of the investment strategy and the performance of the growth phase providers.

But as the glide path approaches retirement, a simple switch to bonds isn't always going to cut it, particularly given the fact that in future, increasing numbers of retirees will be moving into drawdown and remaining invested for another 10 years or more.

Many lessons will have been learnt from the challenging investment markets of 2022, not least that long-dated gilts are absolutely not a risk-free investment. It is for those investors in the run-up to retirement where the asset allocation challenge is most complex. And 2022 showed us what a lack of diversity can do to a default, with many investors down 15 per cent or more in the 12 months up to retirement.

But while equities, bonds and gilts all performed badly in 2022, infrastructure stood out with a 4.92 per cent positive return on EDHECinfra's Infra300 index. Infrastructure has roughly a 40 per cent correlation with bonds, giving a scheme genuine diversification. Other illiquids also have their own correlation characteristics that can broaden diversification even further.

Data is by its very nature backward looking, and is famously only a limited guide to the future. But markets do have fundamental dynamics that can be understood by analysis of historic performance. However, despite all the talk about illiquids, private equity and the like, the private nature of these assets means solid data that proves the case for them is hard to come by..

We need more data, over longer time periods, across multiple asset classes and portfolio blends, to fully understand what the optimal approach to investing for retirement should be. And if the answer is we need to pay more for it, then trustees, employers, consultants, providers and regulators must come to terms with the idea.

INSIDE

MASTER TRUST & GPP DEFAULTS: ROUND TABLE

THE PRICE OF LOW COST

A mindset shift on the cost of asset management could unlock innovative, positive new investments. But who moves first, and will the market follow? John Greenwood reports

Who is responsible for the low cost mindset that pervades the workplace pension sector, and is it ultimately self-destructive? This was one of the key value-for-money questions debated by delegates at a recent House of Lords round table.

Jesal Mistry, interim head of DC investment, Legal & General Investment Management, argued that innovation was being stifled because of the continued challenge on price that providers experienced.

He said: "We have an opportunity with the consultation around value for money looking ahead to say actually now is the opportunity where we can do more for members, more in terms of delivering better outcomes, more in terms of generating better returns for them over the longer term and ultimately giving members a retirement they need.

"We feel that at the moment there's some real pressure on charges and costs that means that we can't do things within our investment solutions that we'd like to do. We want to change that."

Tight market

Hymans Robertson partner Mike Ambery said it was important to understand the position the consultant was in, having been asked by the employer to do the market review, and to justify their costs for doing that review. He said: "You'll get procurement asking the question, how cheap can you do that exercise? And then, beyond that, with that lens that follows through how cheap can you then do this. So we will speak to providers and say, 'can you chop a bip off that?' because it's just got to be the cheapest that's available because that's what the procurement team are asking us to do.

"Can we, should we, explain what values and outcomes are? Yes, we should. We should be engaging employers to say yes you can pay more and get better outcomes. The problem is the buyer doesn't believe in that. They have a procurement team that is saying I just want cheaper."

Jamie Jenkins, director of policy and communication, Royal London, said: "Even if it was 10 bps, would that matter. Because there are variations in investment returns of thousands of bips in this [the Corporate Adviser Master Trust & GPP Report] report. So are we focused on the right thing? If that's the conversation we're having?"

Ambery argued that the government's value for money consultation should re-lens what pension consultants do and also require employers to look at the outcomes their auto-enrolment scheme has achieved each year.

Moving client behaviour

Martin Parish, head of pension consulting at Aon Employee Benefits highlighted the need to distinguish between the attitudes of trustees and employers, and between different types of employers.

He said: "Cost is a tangible, measurable aspect of scheme design, but it is only one of four factors that influence outcomes, with the others being time, performance and contributions. We are moving to an education piece. ▶

"But I don't think we can wrap up employers with trustees. Trustees who have perhaps come from a consultancy or actuarial background, are very index led, they're very cost driven because that's been their experience. But you can speak to an employer, for example, in the asset management industry, where people on the governance committee are active investors. Cost isn't such an issue. It's more about fund choice."

Contract versus trust

Parish also noted that the two providers in the report that had cited the highest proportion of members increasing contributions over the employer's minimum were contract-based.

"Is it because those two providers are offering better levels of engagement? We know things like nomination of beneficiaries and app usage is probably higher within contract-based arrangements rather than master trust. That is critical information to share with employers. They want to have a scheme that people value and they can go back to their board and say, from a value employee value proposition, actually our pension ticks all the boxes."

Richard Birkin, head of DC pensions at Isio said he had seen a mindset shift away from just charges determining selection. He said: "We will apply weightings to the nine broad sections that we assess as part of the research. Often we're seeing the charges one removed from the weightings completely. Either you're there or thereabouts. We're not too fussed about what that range looks like because quite frankly, for the big stuff, it's going to be good. We have had a call with the regulator recently where there's a real concern about the TERs. We had a scheme recently that was a couple of billion pounds, where the range was 12 to 17 basis points for every provider on that list, and locking in further milestone reductions.

"But we're definitely seeing for both trustee and employer where they're far more open to a sensible conversation about the quality of the product and the potential outcomes for members."

Investment costs

Parish added: "Is cost something that employees are overly worried about? I think if you showed them 10 per cent growth and a 1 per cent charge, they'd be more than happy to go for that."

David Croker, head of pension consultancy at Mercer Marsh Benefits highlighted a sense of unease amongst HR directors as to the risks that DC schemes

have placed on employees. "When HR professionals go through that experience of someone saying, 'Oh, I want to retire, but I don't think I've got enough money, so I will stay on in work', that's when the penny begins to drop. It has been masked recently because of DB benefits that people have, but this won't always be the case."

Lydia Fearn, partner at LCP said: "We talk about outcomes a lot. But this outcome, what is it? It's as though we've got a crystal ball. We've put our assumptions and our thinking around it, but we're not going to get it right because anything we say today is not going to be correct in 20 years' time. So that's why it's really hard for employers and trustees to think about outcomes."

Performance metrics

Fearn also cautioned that an unintended consequence of the strict performance disclosure requirements in the Department for Work and Pensions' planned value for money framework could be a lack of innovation in investment strategy. "We could get everybody converging towards an investment median again, which we have tried to so hard to get away from."

(Main image) Mike Ambery, Hymans Robertson partner. (This image) Lydia Fearn, partner at LCP

(Top left) Jamie Jenkins, director of policy and communication, Royal London; (Middle left) Martin Parish, head of pension consulting at Aon Employee Benefits; and (Left) Richard Birkin, head of DC pensions at Isio

Iain McGowan, head of fund proposition, Scottish Widows highlighted the wide range of outcomes across the sector revealed in the report. "It shows that charges are largely irrelevant in that context - the variability of outcomes is so great. And I can't tell looking at short term results, who has a better investment philosophy, who will serve members better in the long term. And that's quite healthy because this draws attention to the need for providers, for investment managers, whoever's involved, to explain their investment philosophy."

Mistry questioned whether value for money framework's league tables and rankings would create a herd mentality with no-one wanting to be at the bottom and therefore making decisions which means that they're never going to really deliver anything at the top end. "The reports are great because they draw attention to certain things. But you do get that short termism coming out."

Fearn said: "Often they [league tables] will stop members going in."

Aussie concerns

Jenkins said: "I think the government is slightly obsessed with the Australian system which is broadly based around two strikes and you're out. So in one year, if you deviate from benchmark, you have to write to members and tell them that you might not be providing good value for money. And you've got to take them out of the fund if you continue to underperform. It's very, very short termist and could drive some really significant different and quite dangerous behaviours. There's a danger that we just assume that everything that is done in Australia is a perfect model to follow."

Jenkins also expressed concern at the government's focus on how to use UK pensions assets to support the UK economy.

He said: "It's really unclear what the aim is, to be honest, because it changes by the month. One minute you're talking about infrastructure and net zero funding for 2050 and the next minute you're talking about how do we fund tech start ups, and it's venture capital. At the end of the day, it's not the government's money, it's not our money, it's member's money for their retirement."

Illiquids in DC schemes

While delegates supported the idea of bringing transformative UK investments into DC portfolios, some expressed concern at operational obstacles to implementing this. But Mistry said that Legal & General was already managing to deliver illiquids through DC.

"Within LGIM the hurdle is cost. The hurdle isn't operations, the hurdle isn't daily pricing. It's cost. On the platform we already operate schemes for private market investments over seven-year, ten-year and 15-year time periods on assets. So the operational capability is there, but they cost more. And these clients individually are able to take the view that they feel that's good value."

Russell Wright, senior vice president – DC, Redington pointed out that Nest was also doing innovative investments, ▶

but was able to do that because of its size. "They've got scale, they have a huge amount of assets and maybe that's what we need more schemes to have so they can do similar things," he said.

Mistry said his three years at Legal and General had been "really interesting fighting those battles around charges, costs, value, asset classes and innovation."

Birkin responded: "Trustees don't like change – they are shying away from providers where they are consolidating, for example. And in the same way, if something is quite bold, am I going to put my neck out if we have something cheap and cheerful that does the job?"

Fearn said: "It's a lovely idea [to spend more on investments] and some employers have done it where they pay the fees for members. But we need to see every provider come up together."

Jenkins added: "Yes, I don't think any provider wants to put themselves out on a limb and not win business. In the same way that the whole industry coalesced around auto enrolment and the charge cap and the default, do we need legislation to enable that."

Fearn said: "I think having breadth of investment across your glide path through diversification and risk management is absolutely critical and in that means slightly higher pricing. I think that's the right thing to do."

Parish said: "For those that make the first move in business, whether you're a Richard Branson or Elon Musk, the size of the opportunity is massive." ■

David Croker, head of pension consultancy at Mercer Marsh Benefits

MASTER TRUST & GPP DEFAULTS: ROUND TABLE

DEFAULT DILEMMAS

How should defaults respond to today's high interest rates, and should the fundamentals of portfolio construction be reassessed? **Muna Abdi** reports

Last autumn's market volatility turned glide paths on their heads. The damage to retirement readiness would have not been so deep if the industry had had a better understanding of how members planned to retire. This was one of several topics discussed at a Corporate Adviser round table held at the House of Lords last month.

Investment approach

Delegates debated the unusual impact that the market turbulence of 2022 had had on default glide paths, with many providers' investment strategies delivering worse performance for those investors in the run up to retirement than for younger savers in supposedly more volatile strategies. With high interest rates offering tempting returns, would it be wise for portfolios to move out of equities, given the storm clouds that remain over the stock market?

Iain McGowan, head of fund propositions at Scottish Widows argued it made sense to stick to one's beliefs. He said: "Over the long term investors will be rewarded for risk for taking risk. So equities will outperform corporate bonds and cash in the long term. Opting for 4.5 per cent on cash for a short period might sound like a good outcome, but it's not a long-term outcome. There's always a danger in trying to time the market."

Shorter gilts

McGowan argued that the challenge lies in ensuring that investors are invested appropriately. He said: "The challenge that the conditions in 2022 threw up, though, was that not everybody is invested in the right way for their expected pension income.

"If you're invested in long-dated corporate bonds and they fell by, let's say, a


(Far image, left to right) Russell Wright, DC pensions consultant at Redington; Richard Birkin, head of DC pensions at Isio; and Jesal Mistry, interim head of DC investment at LGIM. (Left) Iain McGowan, head of fund propositions at Scottish Widows

third, well that's okay if you were going to buy an annuity that became commensurately cheaper as a consequence of that. The difficulty for a provider is to know why members are investing."

McGowan said a response to the 2022 experience was to increase allocations to shorter-dated government bonds and reduce corporate bond exposure.

Jamie Jenkins, head of policy and communications at Royal London said: "What we saw in the latter half of last year with the bond and gilt market changes was that the basic premise that government gilts are risk free momentarily wobbled. I'm sure it will find its way into the course books of financial planning exams over time. But it is also a reminder of the conversation over whether there are longer term assets that are less liquid, that may cost more but may give good returns with less volatility."

Growth play

Martin Parish, head of pension consulting at Aon Employee Benefits, argued that the investment approach for defined contribution (DC) schemes needs to change from a liability-focused approach to a pure growth play. He said: "The investment industry needs to change its thinking around their investment strategy and move away from a liability focus, which is a DB legacy and look at a pure growth play."

He made the argument that to provide members with the most freedom and flexibility, the focus should be on fund value at the time they elect to receive benefits.

Parish said buying an annuity was becoming more of an in-retirement rather than at-retirement purchase and that the DC sector needs to shift its perspective and get away from its DB history, which places a liability focus on investments.

Private market focus

Reflecting on the kind of returns available in public markets, Parish pointed out that private markets can offer better returns. He used the FTSE index as an illustration, which has had lacklustre returns in the previous five years. He said: "My concern is, as a private investor, that the better returns are available from the private markets than the public markets."

Parish also noted that income funds and global stock funds have lost money over the past year. He also added, "We're going to see the real pure DC population reach a point where they're making retirement decisions, whether the markets have recovered sufficiently by then, to compensate for the current loss they would be experiencing."

Jesal Mistry, interim head of DC investment at LGIM discussed the difficulties involved in retirement planning and the issues that arise from the government's flexibility. He said: "The issue with flexibility at retirement is that the government gave loads of flexibility and freedoms, which was fantastic. But it's made it difficult to be able to create something that really meets the needs of individuals into retirement."

Liability is a significant consideration, but it's not only about matching income and assets, said Mistry. He said it's critical to think about what a person might do in retirement and how they would access their benefits.

He said: "If you purely focus on pot at retirement, then in the last year from retirement, you should be in cash because that's the only way you're not going to lose any money. But for someone with £150,000, who may access drawdown, their horizon at the age of 65 is still 30 years.

Mistry said, "There's a liability in terms of what they're going to do and how they're going to access their benefits, not in the truest sense of an income and an asset and trying to match the two together but in a different way."

Glacial change

Hymans Robertson partner Mike Ambery expressed concern about the industry's sluggish rate of change, with short service refunds and the pensions dashboards programme as examples of this. Ambery drew attention to the fact that around 90 per cent of people default through everything, including their investments. This begs the question of whether the sector is making sufficient effort to include members and motivate them to take a keen interest in their assets.

He concurred that the sector must do more to promote change and stressed the need for behavioural modification, arguing that members need to be motivated to participate more in their retirement and investing plans. Ambery also emphasised the importance of regularly providing members with useful indicators, such as retirement planning tools.

Ambery called for rapid development in the investment sector and urges all parties to cooperate to find solutions and drive progress. He stressed the necessity of working together with the Treasury and ▶

(Left to right) Martin Parish, head of pension consulting at Aon Employee Benefits; David Croker, head of pension consultancy at Mercer Marsh Benefits; and Mike Ambery, Hymans Robertson partner. (Bottom) Russell Wright, DC pensions consultant at Redington

other organisations to enact substantive change. He said, "We should have that sort of lightning pace of accelerated development, which we see in other industries to help drive that forward."

Default hesitancy

Lydia Fearn, partner at LCP drew attention to the fact that some clients are expressing apprehension and anxiety about their investments, which shows a lack of faith in the default option and a need for information on available investment options.

Ambery agreed that defaulting outcomes and guiding behaviour through meaningful communication are important. Default mechanisms can guide people towards the right behaviour, rather than telling them what to do he argued. Ambery emphasised the importance of making communication and engagement more meaningful, especially through technology like apps that can nudge people towards making better retirement decisions.

He also highlighted the importance of avoiding a one-size-fits-all approach and instead offering personalised options for individuals to choose from. He said, "We're in a society where consumer duty will kick in. You can't tell people what to do, and we shouldn't. We should be guiding and giving not a one size fits all but instead, small, medium, large, and extra-large. Let's give different t-shirts out and then let people pick what's right for them."

Jenkins noted that the trend towards individualised retirement savings plans has resulted in a significant transfer of risk to individuals. With more responsibility placed on the individual to make important financial decisions, the stakes have never been higher.

Jenkins praised the success of auto-enrolment and savings phase as an effective default option for retirement savings. But he made clear that this strategy can only get people so far because they ultimately need to make important choices regarding how to manage their retirement savings. Unfortunately, he said, a lot of people lack access to expert financial counsel and must make these choices on their own.

Negative messaging

According to Jenkins, this lack of guidance and advice has led to a negative and warnings-based approach to retirement savings. Many conversations about retirement savings focus on the dangers of making the wrong decisions rather than offering actionable advice.

He said: "We've created a very negatively-orientated, warnings-based set of guidance. It's all about the dangers of things that could go wrong. I can't tell you where you should invest, I can only tell you that's the wrong thing to do over the long term. It's all in the negative."

Jenkins noted that this approach can be unhelpful and discouraging for individuals who are trying to make informed decisions about their finances. He suggested offering more useful and actionable advice to help individuals make informed decisions about their retirement savings. Ultimately, this will help to ensure that individuals are equipped to manage their finances and make the best decisions for their future.

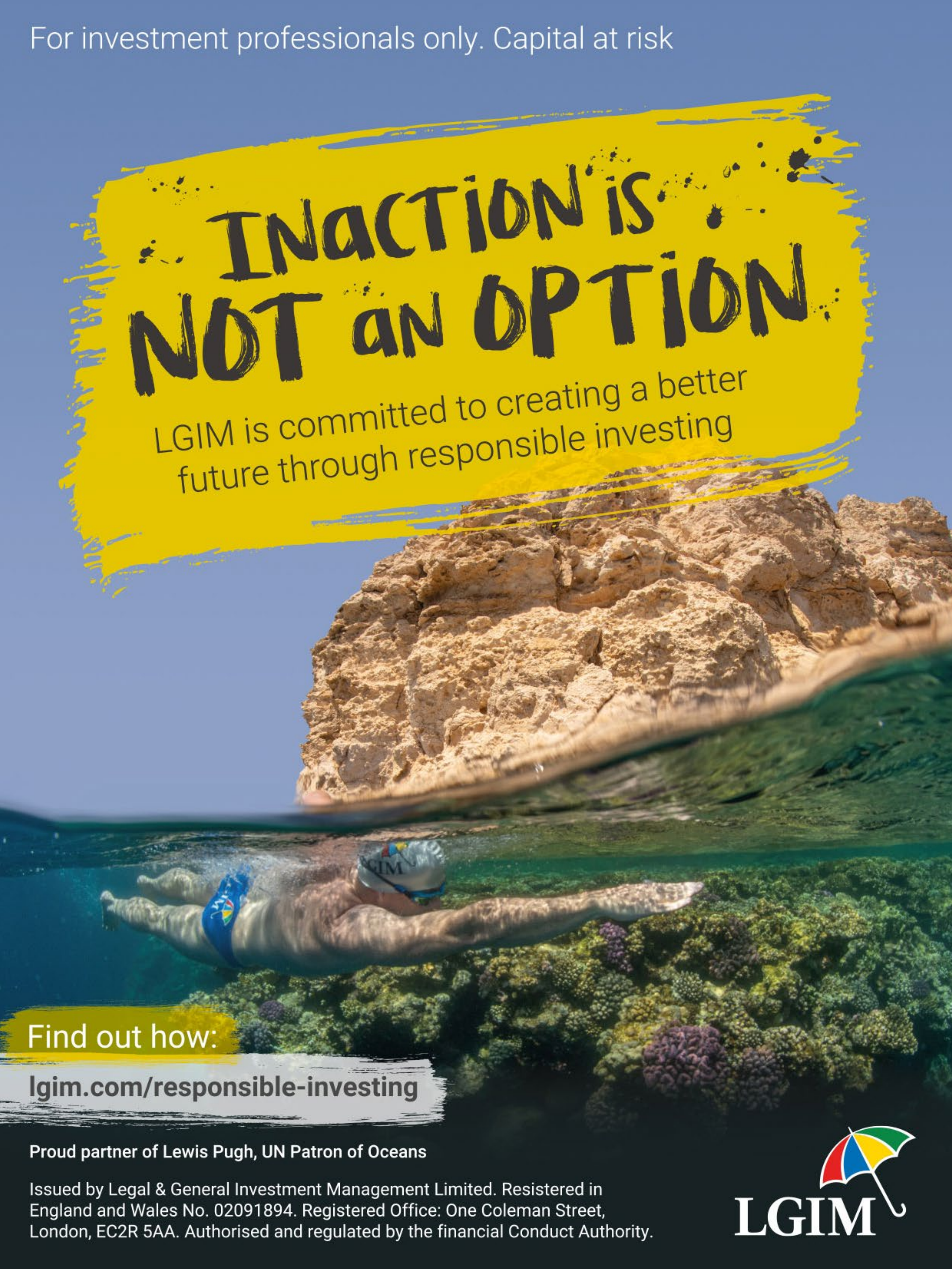
But Russell Wright, DC pensions consultant at Redington reminded those at the debate that when it comes to engagement, people's attention span is limited. He said: "People haven't got the attention span. Compare what people like to engage with, things like TikTok, versus a letter [about pensions] that comes through the door, which is really long, and is full of caveats, full of warnings."

David Croker, head of pension consultancy at Mercer Marsh Benefits pointed to about dashboards and the possibility of new players entering the pension sector with the intention of combining individual pension accounts. He said that given their success with apps and related technology, banks were well placed to succeed.

Wright expressed agreement with the idea that pension providers may not be the ones to provide the ultimate dashboard solution that members choose. He predicted that it will either be the already-active participants in the D2C retail financial services industry or fresh players.

He said: "I think it will be either those existing financial services providers who are already engaging with customers or someone completely left field who's going to do a lot better than a kind of traditional financial services provider."

Mistry agreed and added: "What you'll get is start-ups, fintechs or even the providers delivering their own version of it. So you've got the connectivity to be able to deliver something." ■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OPINION

WHY WE BELIEVE RESPONSIBLE INVESTING IS GOOD FOR BUSINESS – AND PENSIONS

» **Rita Butler-Jones** head of DC, Legal & General Investment Management

When Sir Nigel Wilson was appointed group chief executive of Legal & General in 2012, he followed a long tradition of the company's leaders who brought with them a desire to amplify the financial success of the business – and a social conscience, says Rita Butler-Jones, head of DC at Legal & General Investment Management (LGIM).

Notably, back in the 1970s, Ron Peet, one of Sir Nigel's predecessors as CEO, helped the campaign to support families of children affected by the drug Thalidomide by putting pressure on Scottish drinks and pharmaceutical company Distillers[1] who manufactured the drug in the UK[2].

This is just one example of the principles that continue to guide the Legal & General Group's approach to responsible investing through its investment arm, LGIM.

Over the years, Legal & General and LGIM have described the approach of investing for social good while also generating profits for shareholders as inclusive capitalism.

This means that our purpose is to improve the lives of our customers, build a better society for the long term and create value for our shareholders. Put simply, it's investing capital for financial return and social benefit. We believe that the concept of inclusive capitalism is what sets us apart from our peers.

Balancing risks and returns

In her foreword to LGIM's latest Active Ownership report,[3] LGIM CEO, Michelle Scrimgeour demonstrates how our responsible investment strategy, and the ethos of inclusive capitalism are more relevant than ever in responding to the challenges facing our modern global economy.

Michelle highlights current concerns including the continued threats to nature posed by climate change, the need of governments to balance their net-zero goals with the equally pressing need to provide energy security in the light of geopolitical conflicts such as in Ukraine. She also refers to the global inflationary pressures that spurred the cost-of-living crisis.

> In 2022, 95 per cent of all LGIM's new products were ESG-related. These included net-zero corporate bond funds and exchange-traded funds (ETFs) with Paris-aligned benchmarks

Many of the underlying issues behind the headlines in 2022 are germane to our work as a responsible investor as we need to understand the triggers behind the problems before we can devise strategies to help resolve them.

It's only then that we can develop innovative, responsible investment strategies that our clients want and need. In 2022, 95 per cent of all LGIM's new products were ESG-related. These included net-zero corporate bond funds and exchange-traded funds (ETFs) with Paris-aligned benchmarks.

We also engage with companies, policymakers and other stakeholders on issues

from the living wage, to deforestation, to board level ethnic diversity.

Yet, attempting to tackle these issues through our investment strategy and stewardship isn't just necessary from a socially-responsible perspective: we believe that it's also good for the long-term returns we seek to generate for our clients. This is because we believe that long-term returns can be affected by ESG (environment, social, governance) factors and so it's essential to have an investment strategy that manages risks and unearths financial opportunities.

For those in our DC pension schemes, managing risk is a key part of selecting the funds in which we invest their savings. While we want the best possible returns for our clients and scheme members, we must also consider whether an organisation that is making good returns now is at long-term risk from a failure to future-proof itself from potential threats posed by ESG issues such as climate change. We also consider whether its business operations may cause social and/or environmental harm and need steering towards better practices.

LGIM engages with companies to support them in transitioning to more environmentally and socially responsible operations. We also use our shareholder voting power to persuade organisations to change. In extreme cases, we may even divest in certain eligible portfolios if we believe an organisation is not making suitable progress to address our concerns.

> For many years we've built our credentials as a socially responsible asset manager that considers the impact of our investment decisions on the wider world around us

It's not all about us – why our clients' views matter

Just as it's important to us to invest pension savers' money wisely and responsibly, we also believe that it's essential to listen to the views of members and trustees to determine the level of overlap between our voting policies and the expectations of clients and in developing future engagement topics.

In October 2022, LGIM launched its 'Expression of Wish' digital service in partnership with the Tumelo platform. This first-of-its-kind service enables pension scheme trustees to express their views on upcoming AGM votes – informed by the opinions of their members – directly to LGIM's Investment Stewardship team.

The creation of a streamlined digital feedback loop provides trustees with real-time updates of how LGIM voted and a detailed rationale of why, shortly after the vote.

It also supports pension scheme trustees with their additional regulatory reporting and decision-making in an easy, navigable way.

Our scale means we can give increasing numbers of scheme members this opportunity. Piloted with one of our largest trust-based clients with almost 70,000 members, the service is being broadened to LGIM's DC trustee client base, which represents 2.15 million scheme members in the UK, as well as other interested LGIM clients.

Building better futures – our rationale on repeat

Inclusive capitalism doesn't mean we have to compromise our commercial decisions or the profits we generate for our shareholders, but it does allow us to use our financial influence to help address some of society's biggest problems such as climate change, antimicrobial resistance, housing crises, gender and ethnicity disparity, and the need for regional economic regeneration.

For many years we've built our credentials as a socially responsible asset manager that considers the impact of our investment decisions on the wider world around us. Yet our commitment to creating better futures through responsible investing only gets stronger as the years go by.

For us in LGIM's DC team, doing the right thing never goes out of fashion and we'll continue to keep innovating in the hope of offering financially secure retirements built on responsible investment principles. ■

LGIM

[1] For illustrative purposes only. Reference to a particular security is on a historic basis and does not mean that the security is currently held or will be held within an LGIM portfolio. The above information does not constitute a recommendation to buy or sell any security. [2] Harold Evans, journalist, author and Thalidomide campaigner in conversation with Richard Sambrook, Professor of Journalism at Cardiff University, in 2015. Mr Evans mentioned Ron Peet's influence on the debate over compensation: "A group of shareholders had begun to agitate; sales were affected; and Ron Peet of the Legal & General Insurance company made a big difference saying that it made commercial as well as moral sense to achieve a decent settlement." Full article available at https://theconversation.com/in-conversation-with-journalist-author-and-thalidomide-campaigner-harold-evans-48322. [3] Active ownership 2022: https://www.lgim.com/uk/en/capabilities/investment-stewardship/active-ownership/

OPINION

WE SEEM TO BE AT SOMETHING OF A CROSSROADS ON RETIREMENT SAVING

» **Jamie Jenkins** director of policy & communications, Royal London

We spent much of the 2010s implementing automatic enrolment, adding millions of savers through workplace pensions. It was a huge success. Pension freedoms brought welcome flexibility for those nearing retirement, removing the singular focus on annuities. And the State Pension was significantly simplified.

However, policymaking since then has been at best rather piecemeal, with incremental changes here and there on disclosure requirements, some adjustments to start paving the way for illiquid investments and the usual ups and downs of tax allowances.

There is evidently consensus around certain areas, though:

- Everyone agrees that saving 8 per cent of a band of earnings is unlikely to be sufficient to achieve the retirement pot most people will need when they reach retirement
- Similarly, there is widespread agreement on the need for greater support for people making retirement decisions

On contributions, it's great to see the recommendations of the 2017 automatic enrolment review finally making their way through parliament, albeit simply in an enabling capacity. Reducing the age of eligibility to 18 will help people start saving earlier, and removing the Lower Earnings Limit will significantly increase the amount being saved for people on lower pay. Arguably, these changes pave the way for a more strategic review of the savings levels.

No-one would suggest that we make changes to increase pension contributions significantly at this point. If anything, some people are having to cut back on savings or even dip into them just to get by, while the cost of living remains so high. But having a plan is crucial. Perhaps a plan that is conditional upon economic conditions being right before increases are made, but a plan that is executable when that time comes.

After all, the cost-of-living crisis today is perhaps instructive when considering what an under-saved retired population might look like in future.

It's also becoming increasingly clear that people need more support in making retirement decisions. 'Pension Freedoms' were brought in almost a decade ago and, despite some well-intentioned work around structured guidance sessions, few people are receiving any support or advice as they make what for some will be the most significant financial decisions of their lives.

On contributions, it's great to see the recommendations of the 2017 automatic enrolment review finally making their way through parliament, albeit simply in an enabling capacity

The forthcoming review of the advice / guidance boundary provides an opportunity to put this right, to focus on how we can help people, rather than simply warn them of all the dangers they face. It would also be sensible to focus on how we can reduce costs for advisers, hopefully leading to more people being able to access advice at a cost more proportionate to their needs.

This year's Corporate Adviser report on 'Master Trust and GPP Defaults' provides unique insight into the current market for workplace pensions, highlighting an additional consideration; investment performance. Returns have varied wildly in recent years, most recently during the economic turmoil over the course of 2022. By their very nature, returns are not guaranteed and will never be wholly predictable, but there is more we can do to help people understand how their money is invested and whether that is right for them based upon their personal circumstances.

Certainly, the near singular focus on charges, with workplace schemes often won or lost for a few basis points of difference, is somewhat overshadowed by the 100s or even 1000s of basis points of difference illustrated in the investment returns. If we are to be truly focused on member outcomes then we must focus on the areas which make the biggest difference.

For contract-based schemes – group personal pensions – the consumer duty will bring an increased focus on real member outcomes. This should sharpen the focus on the key issues: adequacy of contribution levels, support in decision making and investment suitability.

With a more strategic focus on the right issues, we may yet avoid the worst of the looming cost-of-living crisis in retirement.

We may even be able to make retirement something for everyone to look forward to. As it should be. ■

OPINION

WILL PENSION SAVINGS WEATHER THE COST OF LIVING STORM?

» **Sharon Bellingham** master trust and IGC lead, Scottish Widows

With households under considerable financial strain from the rising cost of living, many of us have changed the way we manage our finances. Whether it's where we buy our groceries from, wearing extra jumpers indoors, or forgoing a coffee on our way into work, spending habits have changed with a focus on everyday essentials, energy, and housing costs.

Households are impacted in different ways - our 2022 Retirement Report told us that 4 out of 5 people expressed concerns about making ends meet. The latest Scottish Widows Women and Retirement Report showed how women are disproportionately impacted by the rising cost of living, and there's a distinct disparity for lone parents, with single mothers particularly financially vulnerable.

So far, we've seen contributions remain resilient, and there's not been any notable changes with members reducing contributions or opting out. Anecdotal feedback in the market indicates that our position is not unique, and experience so far has been more positive than some early headlines suggested. In the same way that we saw inertia play a role in the success of auto enrolment and how saving via payroll removes behavioural barriers, it's likely to also play a part in contribution levels being maintained and opt out rates staying low, given that it requires a decision and an action. Low levels of engagement may be an influencing factor, but members may also recognise the importance of paying into a pension (and receiving an employer contribution).

At the other end of the pension journey, the rising cost of living may be influencing how and when members are taking benefits – enquiries have increased, and our research shows that around 20 per cent of our members cite this as the main reason for taking their pension.

The latest research* conducted by Lloyds Banking Group (LBG), which explores views and experiences of LBG customers and UK households, shows that consumer sentiment remains subdued. Although inflation appears to be easing, expected further interest rate rises undoubtably cause mortgage-holders concern. After more than a decade of low interest rates, many households are facing increasing mortgage costs, and while these can be managed in isolation, the current strain on household budgets could result in tough choices. Renters are not immune either, as landlords may pass on these increases through rent prices.

> The latest Scottish Widows Women and Retirement Report showed how women are disproportionately impacted by the rising cost of living, and there's a distinct disparity for lone parents, with single mothers particularly financially vulnerable

As the rising cost of living pushes more people into financial vulnerability, Scottish Widows' customers truly benefit from the considerable investment made to support those in vulnerable circumstances –our unique "record and share" facility, helps us identify and safeguard vulnerable customers across all LBG products with only one notification. Customers may share information with us and disclose a vulnerability trigger, but the wealth of data held within LBG means that it's possible to infer whether a customer is potentially close to becoming vulnerable – helping us support them and take action with that in mind.

Money worries are likely to persist in the short term so it's important that employers, trustees, and pension providers get the balance right when engaging with members about their pension savings. Sensitively educating and providing broader financial wellbeing support is key to helping members make informed decisions on what matters now, as well as future financial resilience.

In January, The Pensions Regulator (TPR) urged trustees to support savers amid these economic challenges, outlining clear expectations on governance and oversight expectations and how investment strategies and communications support should be considered, all with the aim of strengthening saver outcomes. Whilst prepared for trustees, it has broader relevance for employers and pension providers as a framework to supporting members. Most notably, any support needs to keep the longer-term impact of the rising cost of living front of mind, and that communications adapt to the economic environment and the challenges that members may face now and in the future. ■

corporate adviser

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