PENSIONS POLICY INSTITUTE

PPI

Retirement Outcomes Review: Investment pathways and other proposed changes to our rules and guidance – consultation response from the Pensions Policy Institute

Summary

- Automatic enrolment in workplace pensions has vastly increased the numbers of people saving for retirement.

- Overall, engagement with pensions remains low, and people may not be in a position to make informed decisions about their pension pots.

- Pre-designed investment pathways represent an opportunity to solve this, but care needs to be taken to ensure that they work in the best interests of users.

- Investment pathways should work alongside other systems that can help people engage with their pensions, such as pensions dashboards.

- Automatic enrolment will see growing numbers of people with multiple pension pots in retirement, and investment pathways should be designed to allow people to maximise their pension outcomes.

- Investment pathways will not necessarily drive engagement, and could even serve to lessen it.

Response

1. The Pensions Policy Institute (PPI) promotes the study of pensions and other provision for retirement and old age. The PPI is unique as it is independent (no political bias or vested interest), focused and expert in the field, and takes a long-term perspective across all elements of the pension system. The PPI exists to contribute facts, analysis and commentary to help all commentators and decision-makers to take informed policy decisions on pensions and retirement provision.

2. This submission does not address all of the specific questions in the consultation, neither does it seek to make policy recommendations. Rather,

this response outlines relevant PPI research findings into individuals' decision-making and choices in retirement.

Automatic enrolment in workplace pensions has vastly increased the numbers of people saving for retirement.

3. Since the introduction of Automatic Enrolment in 2012, many more people are saving for retirement, with 10 million people having been enrolled[1], with 99% in the default fund.

4. The vast majority of people who have been automatically enrolled into workplace pensions remain with the default fund of their provider[2].

Overall, engagement with pensions remains low, and people may not be in a position to make informed decisions about their pension pots.

5. Automatic enrolment has in part succeeded through a strategy of 'harnessing inertia' whereby people are not expected to engage with their pension during the accumulation phase.

6. Upon reaching retirement, or the age at which they can withdraw from their pension pots, savers are faced with the need to make active decisions about how best to use their pensions savings.

7. In 2018, PPI produced a report on evolving retirement outcomes, which examines people's decision-making in decumulation[3]. It showed that people's understanding and engagement with their pensions is low, even among those who have already made decisions about how to access their retirement savings.

8. When people are asked about where they might turn for advice, only 39% said that they would consult an independent financial adviser and 34% their

---

[1] Written Parliamentary Statement by the Secretary of State for Work and Pensions, 11.02.19.
[2] 95% of members of DC schemes with 12 or more members are invested in the scheme's default strategy; https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-presentation-of-scheme-return-data-2018-2019
[3] Evolving Retirement Outcomes, PPI, London, 2018. Available at https://www.pensionspolicyinstitute.org.uk/research/research-reports/2018/2018-07-12-evolving-retirement-outcomes/

pension provider. 40% said that they would turn to Pension Wise; however, this service offers only guidance rather than advice.

9. While people much prefer to have face-to-face advice, 45% would not be prepared to pay for it. Automatic enrolment has meant that there is a growing number of people with relatively small pension pots, the size of which may prove a barrier to accessing paid-for advice.

10. Some financial advice firms operate with a minimum pot threshold, whereby they will not provide advice to people whose pension pots are below a certain level. This acts to restrict the market for people with small pots.

11. While small pots are unlikely to provide a substantial level of income through retirement, they could make a significant difference for someone on a low income. Given this, there is a growing need to optimise financial decision-making for people with small pots.

Pre-designed investment pathways represent an opportunity to solve this, but care needs to be taken to ensure that they work in the best interests of users.

12. According to NEST[4], there are four key features that should be considered when designing investment pathways;

- Simplicity
- Value for money
- Freedom to opt out
- Clear choice architecture

13. In drawdown, pre-designed investment pathways would be modelled cautiously in order to limit the risks of individuals running out of money. This may mean restrictions on withdrawal rates and lower returns from a conservative investment strategy. This would create a drawdown that closely resembles an annuity, though without a lifetime guarantee of income. The design of investment pathways should take into account that individuals may purchase a financial product that has some of the drawbacks associated with an annuity, but none of the advantages.

[4] NEST (2014), The future of retirement; a retirement income blueprint for NEST's members.

Investment pathways should work alongside other systems that help people engage with their pensions, such as pensions dashboards.

14. There is a case for linking investment pathways to the forthcoming pensions dashboards, allowing individuals the opportunity to see all of their pension pots in one place, potentially facilitating better decision-making.

Automatic enrolment will see growing numbers of people with multiple pension pots in retirement, and investment pathways should be designed to allow people to maximise their pension outcomes.

15. Individuals with multiple pension pots may also pose a problem for designing investment pathways. If people are to make optimal decisions regarding retirement income, they will need access to a holistic view of their total pension savings.

16. Individuals with multiple pots will need to be able to make decisions based on an understanding of their total pension accumulation across different providers and schemes, and how to maximise their outcomes by choosing the most appropriate decumulation strategy for each pension pot.

Investment pathways will not necessarily drive engagement, and could even serve to lessen it.

17. Investment pathways have the potential to assist people to optimise their retirement outcomes, but in order to do so, a balance should be found between the aim of helping people avoid poor outcomes and enabling them to achieve best outcomes.

18. Investment pathways could provoke engagement, in that individuals will have to make an active choice about what to do with their pension pot at or near the time of retirement. However, in order to do this, accurate information and impartial guidance may be required to support those who will struggle to make an informed decision. 'Wake up' packs have a role to play, but are unlikely to prove a simple solution to the problem of engagement.

19. While investment pathways may protect some individuals from avoidable poor outcomes, they may also actually reduce longer-term engagement, meaning that individuals may forgo potentially better returns on their investments.

20. Investment pathways could offer a route to better retirement outcomes for people with less financial capability or engagement levels. However, their existence may deter some people who could benefit from paid-for advice from accessing it to their detriment.