Guaranteed income launch write up

Thursday 8th September 16:00-18:00

The Pensions Policy Institute (PPI) held a policy seminar on Thursday 8th September to launch its report **How will future pensioners use guaranteed income products?** The report, based on new PPI modelling, examines how securing a guaranteed income can support people's changing needs and wants in retirement. It shows how different combinations of drawdown and guaranteed income, alternative product types and more in-retirement support with decision-making, could help people achieve greater financial security throughout their retirement.

It is the second and final output in the series, the first of which was a Briefing Note published in May 2022. **Briefing Note Number 130: Set for life? Guaranteed incomes in retirement** looked at how the annuities market has changed since the introduction of pension flexibilities in 2015. This research series has been kindly sponsored by a consortium including B&CE (providers of The People's Pension, Hymans Robertson, Retirement Line, Standard Life (part of Phoenix Group), and State Street Global Advisors.

The event was attended by circa 50 people, with a broad range of stakeholders from across government and industry.

The PPI would like to thank Standard Life (part of Phoenix Group) who hosted this launch event.

Welcome from host, Claire Altman (MD Individual Retirement Solutions, Standard Life, part of Phoenix Group)

Claire welcomed attendees to the event on behalf of its hosts, Standard Life. Claire highlighted that it's an important time to be addressing questions around retirement income. As we see the continued shift from DB to DC and the current cost-of-living crisis, it is vital that the pensions industry focuses on making sure that people are getting the most they can from their pension savings. It is also welcome to see that the report does not approach the retirement income question from a binary perspective of whether or not to annuitise, but also includes consideration of questions around the right time to annuitise and varying features of guaranteed income products.

Welcome from Chair, Andy Seed (PPI Governor)

Andy gave a chair's welcome to the event on behalf of the PPI. Andy spoke about the importance of talking about innovative approaches to accessing DC savings in order to better suit savers' needs, particularly as DC pot sizes continue to grow comparative to DB entitlement. Automatic enrolment has vastly increased the coverage of private pension saving, predominantly in DC, and, for many savers, default strategies solve the investment problem. However, this passive approach during accumulation has created apathetic savers, and it's important to recognise that there is no 'do it for me' solution when it comes to accessing savings in retirement, as well as the fact that differing retirement needs will require greater variation in solutions.

Presentation of key findings from Dr Mark Baker (Senior Policy Researcher, PPI)

Mark first provided a brief overview of the previous Briefing Note in this research series, **Set for life? – Guaranteed incomes in retirement**, which provides context to the current state of the annuity market. Since 2015, there have been two major reductions in the amount of money being used to purchase annuities – the introduction of pension flexibilities and the COVID-19 pandemic. Aside from these two disruptions, aggregate annuity investment has remained relatively stable, and as more savers reach retirement with greater reliance on DC savings, rather than DB entitlement, annuities are unlikely to taper off.

Mark then discussed the annuity puzzle, in terms of the reasons why people are not buying them in higher numbers, given the value many attribute to a guaranteed income, outlining a range of factors, including:

- Low levels of trust
- Low levels of engagement in the accumulation phase
- A lack of understanding of the role that annuities can play
- Low take up of advice and guidance
- A tendency to underestimate life expectancy
- Present bias – with many savers more concerned with the present than the future
- Negative perceptions around the word 'annuity'

The report presents six retirement archetypes based on the wants and needs people may have at different stages of retirement. These are not static, so people will fall into different archetypes at different stages of retirement. The report models different retirement income approaches for hypothetical individuals based on these archetypes. This is discussed both from the perspective of different times to annuitise over the course of retirement, and also in terms of the way in which guaranteed income products can be combined with other products in a hybrid approach in order to provide both security and flexibility. The report also emphasises the need for greater support, especially over the course of retirement, which could include defaults, soft defaults, prompts, guidance and advice, and safety nets.

Panel discussion/Q&A

Andy Seed chaired the panel discussion and subsequent Q&A session. The panel consisted of:

- Carolyn Jones – Head of Money and Pensions Guidance Policy and Strategy, The Money and Pensions Service (MaPS).
- Chris Brooks – Head of Policy, Age UK
- Ruari Grant – Policy Lead on DC Pensions, Pensions and Lifetime Savings Association (PLSA)
- Dr Mark Baker – Senior Policy Researcher, PPI

The remainder of the seminar was held under the Chatham House Rule and the views expressed do not necessarily reflect those of the PPI or panellists.

The following points were raised during the panel discussion and Q&A session:

- **The increasing importance of decisions throughout the course of retirement, not at a single retirement point:** The combined result of the shift from DB to DC and the introduction of pension freedoms is that decisions about retirement income are no longer made at a 'cliff edge' retirement date. They may be made before exiting the labour market, all the way through to older ages when they have long since retired; others may not be planning for a traditional retirement at all. Cognitive decline is not always talked about in discussion of financial risks, but it could start to be an increasing problem for those who moved into drawdown following the introduction of pension freedoms.
- **The challenge of encouraging savers to engage with guaranteed income products:** The report identifies a challenge to the industry regarding what the industry might do to promote guaranteed income products. However, it is not just a case of industry promotion but also improvements in annuity rates – something that is currently happening as a result of the current high inflation environment. Guidance also has a role to play in encouraging greater consideration of guaranteed income products. Many people still value guarantees but need to be helped to better understand the role that annuities could play within the context of their individual complex needs. Engagement could potentially be increased by using different, more accessible terminology that focuses more on the benefits of guaranteed income products and approaches. The report intentionally shifts language towards 'guaranteed income' rather than annuities.
- **Low levels of engagement with advice and guidance:** Low and median earners are less likely to access financial advice compared to higher earners but could still very much benefit from more support. Greater support, guidance and advice should help people to

achieve better retirement outcomes. There are already a lot of positive initiatives in this space, as highlighted within the report, but need to find a way to increase engagement.

- **Complexity:** It is important to recognise the depth, variety and complexity of needs, circumstances and decisions, also recognising how these may change over time. There are many changing circumstances in later life (bereavement, changing health or living circumstances, etc.), and people navigating these for the first time will need support to achieve positive outcomes. However, another side of complexity is that individual customisation of retirement products to meet varied needs is costly and complex to deliver. Building in additional complexity will increase the cost of guaranteed income products and make them less attractive. There is a challenge for the industry in determining which specific types of complexity are worth building into guaranteed income products. There is a need for more research to better understand the reasoning and behavioural factors behind the retirement income decisions people are making, which should help to make it clearer where greater support may be most effective.
- **The current high inflation environment:** While people value the certainty offered by guaranteed income products, many annuities purchased do not have inflation protection, guaranteeing a set amount of income but not guaranteeing how much that income will afford over the course of a potentially long retirement. This is particularly challenging during the current environment of high inflation. Prospective annuity purchasers could benefit from a shift in focus from annual amounts to projected lifetime amounts, which may help to emphasise the value of escalating annuities.
- **The role of defaults:** As more savers reach retirement with substantial levels of DC savings and low or no entitlement to DB, there could be a greater need for defaults in order to mitigate the risks they face. Providers may be apprehensive to developing defaults because of the advice/guidance boundary and concerns about how members may respond. Development of defaults could also face a challenge as we see increasing numbers reaching retirement with several pension pots. If different providers and schemes innovate and develop defaults in different ways then it could become harder to advise on what multiple pot holders should do in terms of which of their available default pathways they may want to choose. Consistency and a joined-up approach across the industry would likely be needed to mitigate this risk.

A Pensions Policy Institute report

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