Aon Defined Contribution Scheme Survey 2017

Navigating the future

Powering the investment engine

Empower Results®

Powering the investment engine

Investment is a key component of getting the right member outcomes.

With a bit of guidance and simple options that aim to look to the future, trustees and scheme managers can boost members' retirement savings to help them reach their target destination.

Key discoveries

Most members go for the default investment option while they are saving and then today often take it all as cash at retirement.

40% of default investment strategies target annuity post pension freedoms. 25% target drawdown and 25% target multiple options.

3 lifestyle options is the standard for around half of all schemes.

Over three-quarters of Group Personal Pensions may go too far, with over 20 self-select fund choices. Less than 5% of own trust plans include this many options.

Over half of respondents would like to offer guidance on investment decisions. While 20% of HR and finance managers do not want any involvement at all.

Unexpected findings

Only 7% of default investments **target cash** at retirement, despite the current trend for taking DC pensions as a cash sum.

Nearly 2 in 3 plans do not have a preferred drawdown option in place.

Despite pension freedoms allowing members flexibility at retirement **over 20% of schemes** have only **one lifestyle option** available.

Obstacles

'Updating our **investment strategy**'

'**Member engagement** especially planning for retirement (investment of DC funds, drawdown options)'

'**Cost-effective** investment management'

Moving forward

Check your default aligns with **your member behaviour.**

Help members engage with their plan by offering simple investment options.

Future-proof your pension plans by ensuring drawdown is supported both pre- and post-retirement.

Investment

Better member outcomes are becoming increasingly important to schemes, and the investment returns achieved are a highly relevant part of this. Yet when it comes to positively affecting the investment experience of members, should schemes be focusing on helping members make better investment choices or should they focus on ensuring the default is appropriate for the majority of members?

In the past, emphasis has often been placed on encouraging members to make their own investment choices. However, while encouraging members to self-select their investments may be well-intentioned, this is not always an effective way forward and may even be counter-productive if members make an active investment decision (away from the default) and then do not regularly revisit this in future.

Our analysis suggests many members want the decision to be made for them, with respondents telling us over 85% of members are using the default option. Although it is worth noting that there are always some who would like to make investment decisions themselves – with varying levels of guidance required. But remember, a member making their own investment decisions does not always provide better results, as can be seen from experience in the US, so it is all the more important to provide an appealing and effective default that is suitable for the maximum possible number of members.

Ultimately, the extent to which you determine the investment strategy on the behalf of members or educate members to make their own decisions will be based upon the requirements of your members.

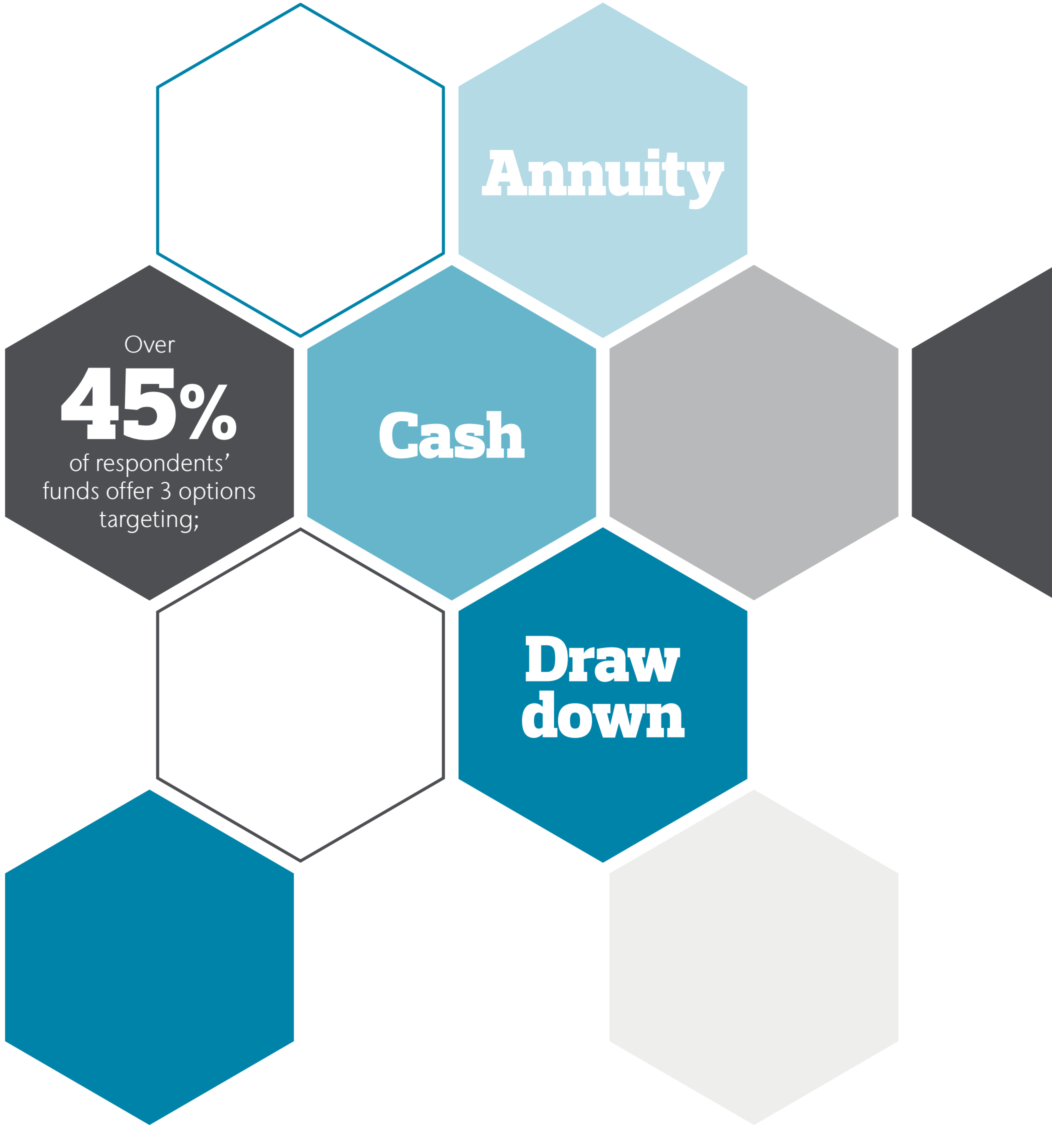
US investment experience

Our research in the more mature US DC market in our report **Help in Defined Contribution Plans (2010)** shows that in 401k plans, members who make their own decisions typically achieve 3.3% pa lower returns than those who receive help in the form of target date funds, managed accounts or online help. Looking under the surface of this figure, this is often because they buy high and sell low, whether that is a particular stock or a manager.

Over
85%
of members are using the default option

Lifestyle options

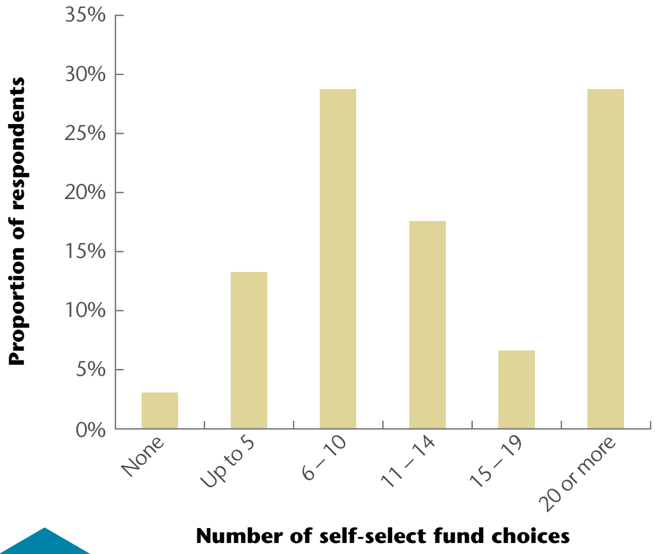
Lifestyle funds or target date funds can be a great option for members. Over 45% of respondents' funds offer three options targeting cash, annuity and drawdown. Members are more aware of when they want to retire and how they want to take their money than they are regarding a decision about what assets to invest in to help acheive their goals. Over 25% of respondents only offered one lifestyle option. Fewer lifestyle options may mean that members have little choice but to make more detailed investment decisions or take more risk close to retirement than they intend, depending on how they want to take their money.



Self-select funds

In addition to a choice of lifestyle options, the majority of respondents also offer self-select fund choices. If most of your membership is going into the default, it may be you could be offering too many options. Especially as, when faced with lots of choice, it can be difficult for members to choose an option that they think is best for them and can lead to disengagement. On the other hand, offering too few options may mean that members will not have the choices they want.

Number of self-select fund choices offered



1 in 4

of respondents offer over 20 self-select funds

Surprisingly, a quarter of respondents offer over 20 self-select funds in addition to their lifestyle options and a quarter of respondents offer between 6-10 funds. The range of the number of funds being offered indicates a clear difference in what schemes envisage as being the best number of funds to offer to members.

We have found that it is most commonly the smaller schemes which offer 20 or more fund options (over 30%). However, GPPs tend to offer a large number of fund options without always providing the appropriate support for members to make an informed choice.

When offering choice to members, communications become highly important. It may be helpful to point members towards information and advice about the decisions they need to make. You also should review the funds being offered to see that they meet the members' requirements.

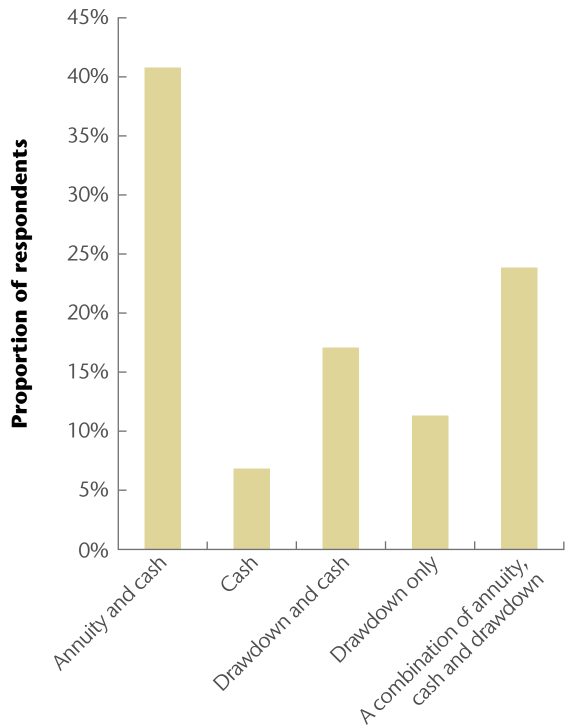
Default fund

Despite the level of choice on offer, our experience is that many members simply do not want to make such in-depth decisions. Our survey results indicate that on average over 85% of members use the default investment option. On this basis, it is all the more important to have a default option that meets members' requriements.

One important aspect of the default investment option is what it targets at retirement. The favourite target among our respondents was 'Annuity and cash' – perhaps surprising considering the new world of flexibilities that we live in. Aon's 2016 DC Member Survey showed only 28% of members were planning to purchase an annuity and the current experience of what members are taking today shown in the FCA Retirement Outcomes Review was that more than half of DC members took the entire fund as a cash lump sum, although noting that the majority were typically relatively small pot sizes.

Based on this you may want to consider updating the default investment target based on what your membership wants from their pension at retirement today. Naturally, you would then need to keep this under review as behaviours are expected to change over time as members become more reliant on pure DC income.

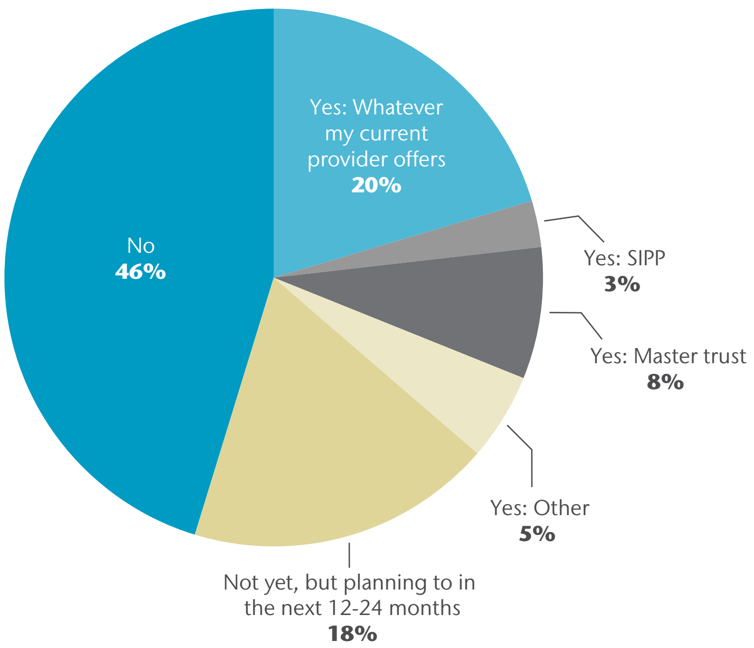
Target of default investment option for new entrants



Preferred drawdown solution

On the basis that Aon's DC Member Survey 2016 showed 53% of members are planning to leave their fund invested and drawdown from this over time, the importance of supporting a drawdown option is clear. Yet 46% of respondents to this year's DC Scheme Survey have not got a preferred drawdown solution in place for members and do not plan to within the next two years. As our research indicates members rely heavily on default options, it may be that many members will be unsure as to how to organise their drawdown solution.

Have you put a preferred drawdown solution in place for your members?



The interim report from the FCA Retirement Outcomes Review (2017) showed significant inertia, with 94% of people without advice staying with the same provider for drawdown and only 6% shopping around. So even if you do not have a preferred drawdown provider your members may behave as if you have, and assume the provider you have selected for accumulation is also good for decumulation.

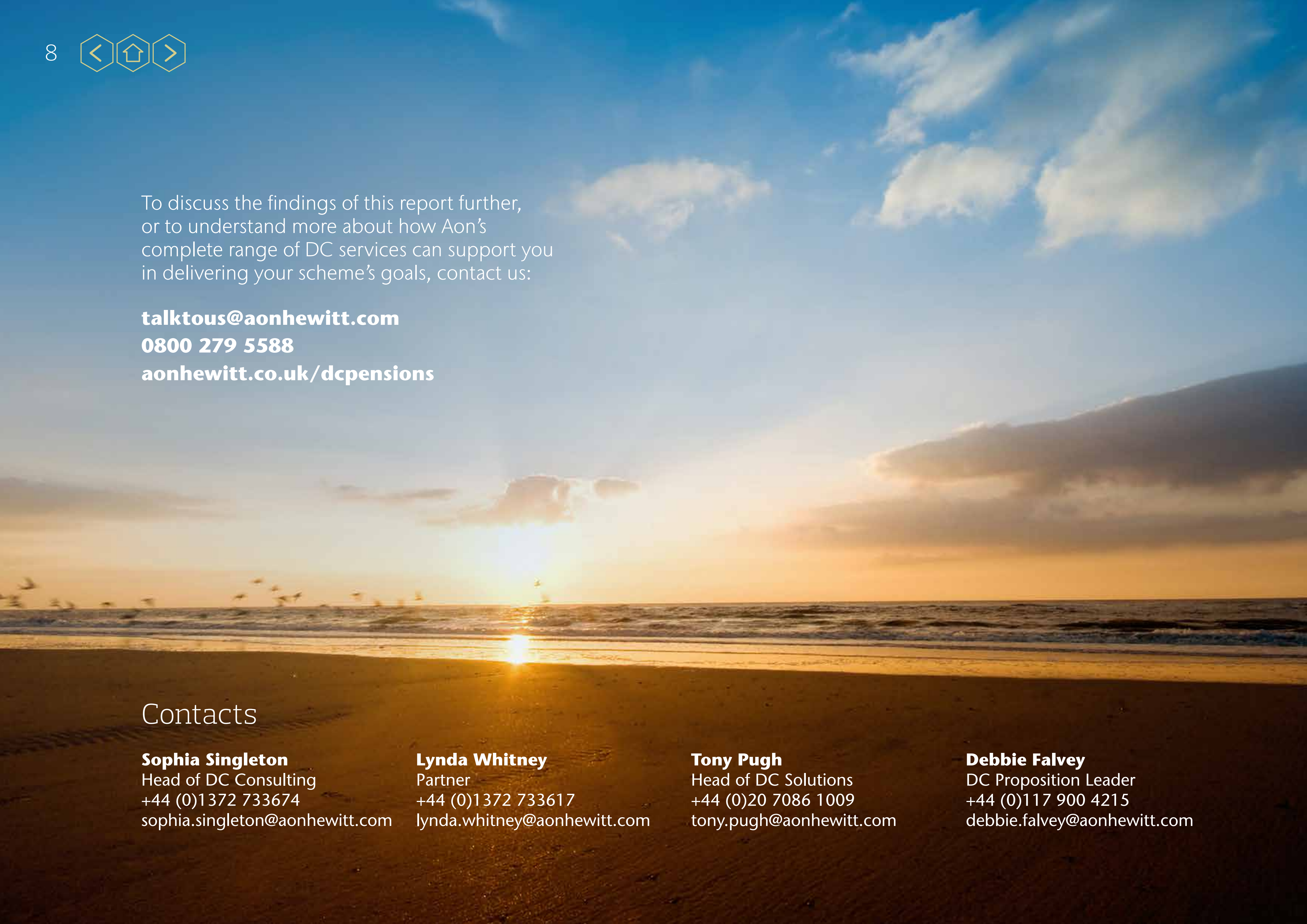
We also note that of those that currently have a preferred solution in place, more than half have opted to offer what their current provider offers. Which begs the question – was this a competitive review or did they assume that their existing provider was good enough?

Drawdown may continue gaining popularity as members' pot sizes grow and they appreciate flexibility in retirement. Putting in place a preferred solution, or offering advice to members at retirement on how to choose the right solution, is a simple way to engage members and help them to get the right outcomes.

FCA report shows that **94%** of people without advice stay with the same provider

Remember

If you have not selected a preferred drawdown provider then your members may assume that your existing provider of accumulation services will be fine, but they may not be getting the best deal.



To discuss the findings of this report further, or to understand more about how Aon's complete range of DC services can support you in delivering your scheme's goals, contact us:

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