UK Defined Contribution Pension Survey 2020

How do you measure up?

For professional clients only

Aon
Empower Results®

You want the best fit for your members and business. But do you have the right measures of success?

Get the measure of how the UK market is changing with Aon's 2020 Defined Contribution Pension Survey results.

Executive summary

In this report, we see how DC schemes in the UK measure up across key areas, including strategy, scheme design, contribution levels, investment approaches and member engagement. The report includes insights from Aon experts on what the findings mean now and for the future shape of workplace savings objectives.

You want the best fit for your pension scheme members – and your business. But how do you compare, and do you have the right measures of success?

In our 2020 Defined Contribution (DC) Pension Survey we sought the views of trustees, pension scheme managers, finance directors and HR managers from a wide range of sectors, about the challenges they face and their aspirations for their scheme members.

Responses were received from representatives of over 200 DC schemes, covering over half a million members and £50bn of assets.

Our research shows that respondents want to offer competitive, 'good value', DC pensions. Most want to do more than the minimum level required, but many do not measure whether they are succeeding in meeting their objectives. There is an opportunity to make DC pensions more tailored towards retirement goals, lifestyle, income and behaviours.

Some key findings include:

- More schemes aim to benchmark with peers than aim to deliver sufficient funds for employees to retire.
- One in 3 schemes do not measure progress against their objectives.
- Two-thirds of respondents do not know what level of pension outcome their default rates will deliver.
- Two-thirds want to spend more time on communications.
- Most schemes do not measure levels of engagement with their pension and wider wellbeing programmes.
- Only 1 in 10 assess their range of investment options against ESG criteria.

Throughout, charts may not add to 100% for reasons of rounding.
Unless otherwise stated, all data is from Aon's 2020 DC Pension Survey

Contents page

If you want to offer a great fit for your pension members and your business, is it time to review your approach?

What are the current strategic trends?

SECTION 1

Get the measure

Q. What are the current strategic trends in DC pensions?

In this section, we explore how DC schemes measure up against others and also how they measure against their own aims and objectives. Do schemes have the information they need to do this accurately or are they shooting in the dark?

1 in 3

schemes do not measure progress against their objectives

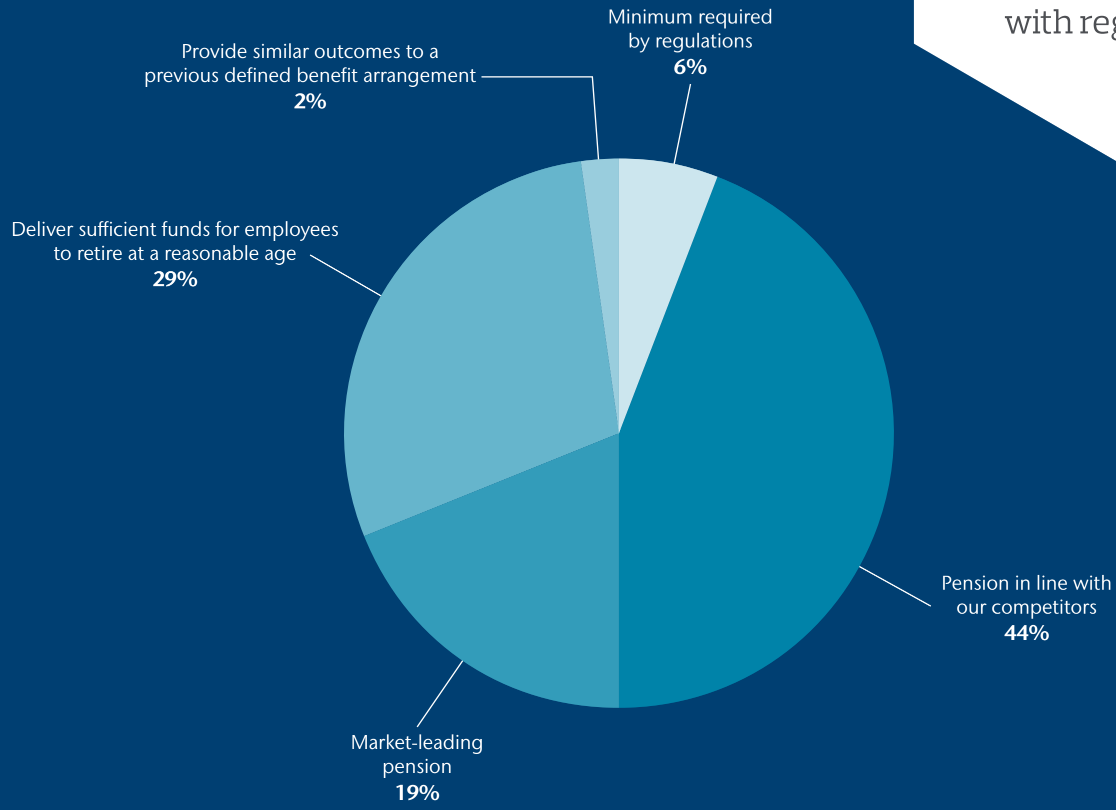
4 in 10

schemes' main aim is to offer a pension in line with the competition while only **3 in 10 aim to deliver a sufficient pension**

Value for members and **better member outcomes** are objectives for around three-quarters of DC business plans

We asked schemes how they would best describe their main aim for their DC arrangement. While all schemes are trying to provide a pension for employees in retirement, we found a range of views on how to approach retirement provision.

- The most popular response was to offer a pension broadly in line with the competition, ie, to use what is offered by others as a benchmark. The rationale for this approach is often to seek to retain employees by offering a similar level of benefits to other employers. However, there is limited evidence to show that employees leave or stay with an employer due to pension benefits alone.
- The next most popular response focuses on outcomes. A challenge with this approach is to reach consensus on how much is a sufficient retirement income, with only 2% saying that they aim to replicate benefit levels that were provided under a previous defined benefit (DB) arrangement. We consider the question of what an adequate level of retirement saving could be for members in Section 3 – Fit for the future.
- Around one in five respondents want to set themselves apart by offering a market-leading pension. In practice this could mean very different things to different people, so it is important to define what market-leading looks like.



1 in 20

say they do nothing more than aim to comply with regulations

Q. Which of these objectives are in your scheme's business plan?

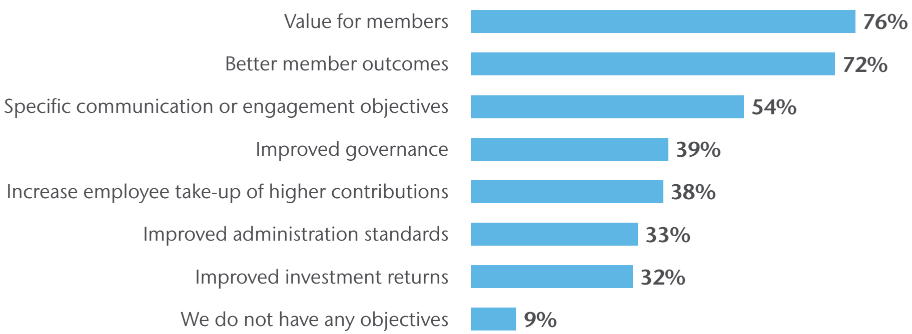
It is not a surprise to see that over seven in ten schemes have 'delivering value for members' and 'improving member outcomes' as objectives. This is similar to our research in 2017 and aligns with The Pensions Regulator's guidance on DC. However, it is how schemes work towards meeting these objectives that is really important.

What is perhaps more of a surprise is that fewer than four in ten aim to increase the take-up of higher contribution rates by employees. Could concerns over the costs to the sponsor be an issue? We found that very few sponsoring employers are considering the long-term impact of insufficient retirement savings on their future workforce profile. As such, many employers are heading towards an ageing and more potentially more expensive workforce.

One objective found to be less popular than in our previous research is that of improving scheme governance. This may be due to improvements over the preceding two years, meaning more schemes are comfortable with the governance arrangements they have.

Just under a third of respondents include specific objectives relating to investment returns. This may be because investment objectives are not included in the business plan, rather than being reflective of schemes not taking an interest in their investments. For trust-based pension schemes these objectives are usually covered in the Statement of Investment Principles and could cover measures such as volatility and growth targets, benchmark tracking or downside protection. In Section 4 – Made to measure, we consider DC investments in more detail.

Which of these objectives are in your scheme's business plan?

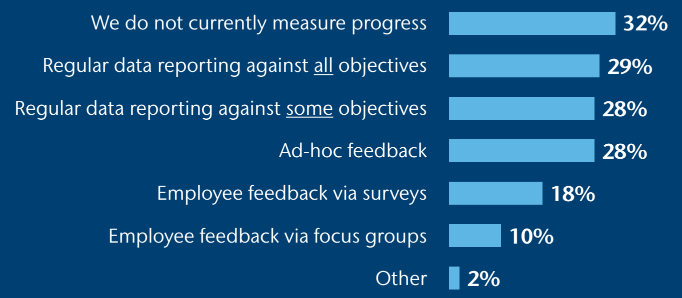


Making sure your objectives are aligned

It is important to take into account the views of all stakeholders when setting objectives to make sure everyone is pulling in the same direction. For example, if the HR team has an objective to encourage employees to contribute more to take full advantage of higher matching company contributions, but the finance team has an objective to minimise increases in benefit costs, there will be a conflict between different parties. (In this instance it would be perhaps more sensible to consider a change to the contribution design, so that members can be encouraged to save more while costs can be controlled for the sponsoring employer.) Aon's Viewpoints Discover tool was designed to help groups of individuals to understand the range of positions and reach consensus.

Measuring progress against objectives

What approaches are used to measure progress against objectives?



Collating data and ad-hoc feedback were the most popular methods of measuring progress towards objectives. It was somewhat surprising to see that nearly three in ten respondents say that they receive regular data reporting against all of their objectives, given that this number includes those with objectives, such as improved governance standards and specific communication or engagement objectives, which can be difficult to assess with quantitative measures.

Only 2/3 of schemes measure progress against objectives

Quick win

- For each objective in your business plan include one or two practical actions which will help work towards it.
- Consider objectives used by other plans and whether they could be appropriate for you.
- Consider sensible measures you can put in place to use information already available to monitor your objectives.

Longer term

Consider other useful measures of progress towards your objectives, both quantitative and qualitative, and consider how to source the information that would be needed on a regular basis.

Measuring tools

Collecting the right data to measure progress towards objectives can be difficult. Aon's Well One app provides a wealth of (anonymised) data on the finances, health and wellbeing of individuals, teams and the wider business using simple health scores. Analysing data from four areas – physical, emotional, social and financial – Well One can bring focus and clarity to strategy and communications while enabling healthy behavioural change for employees.

https://www.aon.com/wellone/

Aon point of view

While it may seem important to benchmark with the competition in the short term, we strongly believe that the objectives of a DC pension should focus on providing employees with sufficient funds to be able to retire at an age with which they and the employer are comfortable.

The leading DC schemes and employers are helping employees to understand how much they will need in retirement and how to get there. By using financial aggregation tools such as Aon's Well One Money, they can bring together DC pension funds with wider savings and other assets to provide employees with the full picture.

What is the biggest challenge over the next two years?

There is a range of different challenges ahead for DC schemes over the next few years. While each scheme is different, a number of emerging themes can be seen in our ‘responses word cloud’. The remaining sections of our survey report cover what others are doing in some of these areas and include our own insights on how to measure up today and in the future.

Could delegation help?

SECTION 2

Weigh up your options

Time to focus

The options for DC scheme structures are wide-ranging. Not only does a decision need to be made on the overall structure of your scheme, but also on who is responsible for the day-to-day tasks such as administration and investment.

We asked those running DC schemes whether they are comfortable with the amount of time they are spending on DC. We found that fewer people are at ease compared to our 2017 survey, particularly those running contract-based schemes where 41% said they are not happy with the amount of time they are spending on their DC plan.

This section considers the different types of DC pension structure, and options available to delegate more to focus on the areas that matter to you.

50%

increase in the numbers not reviewing their DC provider in last three years

1 in 3

Trust-based plans expect to move to a master trust within five years

2 in 3

want to spend more time on their communications

Aon has been working with a number of trustee boards and employers, helping them to become more strategic and effective.

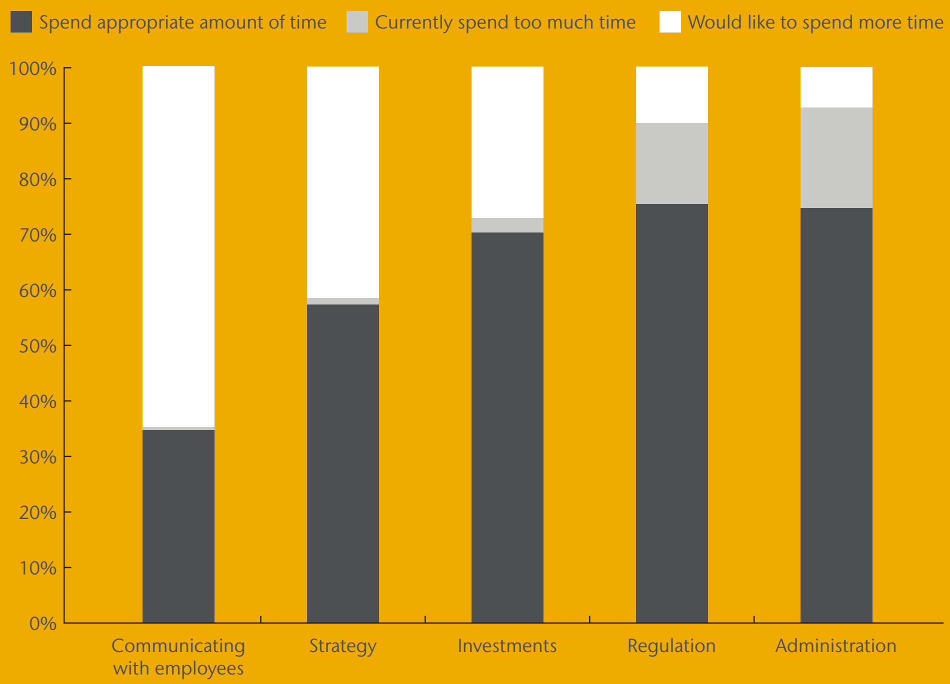
Find out more

Q. How happy are you with the amount of time you spend in the following areas?

Almost 65% of respondents wanted to spend more time communicating with employees on DC pensions, and those in contract-based or trust-based schemes also wanted to spend more time on strategy.

It is important that those running schemes have the right scheme structure and resources in place, especially given the increasing levels of regulatory oversight. Schemes should consider a structure that gives them the time they need to focus on their priority areas.

Amount of time spent in the following areas



Our biggest challenge is:

Review of legacy arrangements

Future DC structures

Our results this year show a continuation of the trend from 2017. Respondents expect there to be a significant move towards master trusts in the coming years. Around a third of those currently running their own trust-based schemes expect to move to master trusts in the next five years. This trend is even more pronounced in bundled schemes, which could be because this would be a less significant change to the current structure than for unbundled schemes.

For trust-based schemes, the governance requirements and the time and resources required to run the scheme are the key triggers for a discussion regarding whether the current structure remains appropriate. On the other hand, for contract-based schemes, the triggers are slightly different, with the main considerations being that other structures may give better outcomes and improved governance. Given the level of delegation in a contract-based scheme compared to a trust-based scheme, this is perhaps unsurprising.

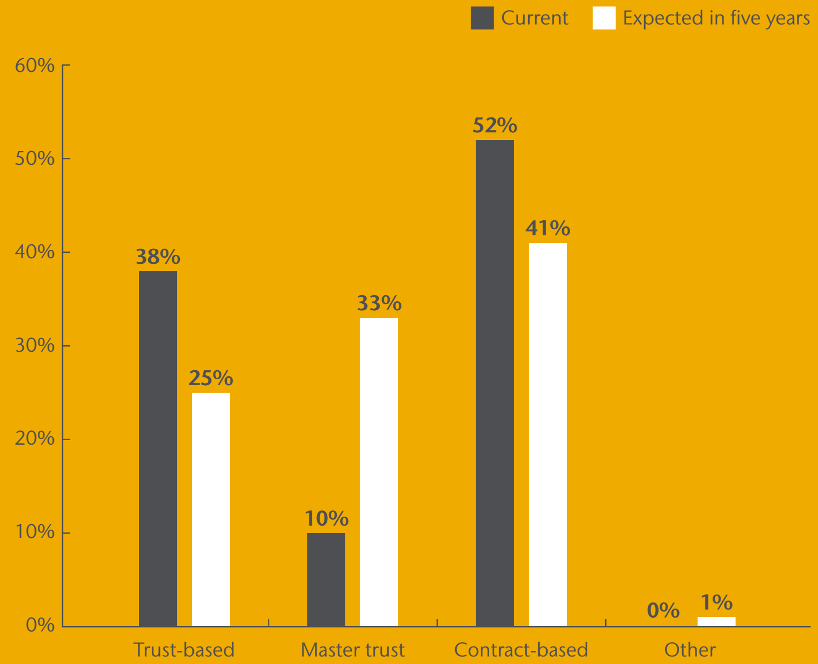
Jargon buster

Bundled trust-based scheme – one provider delivers administration, communication and investments.

Unbundled trust-based scheme – different providers are used for administration and investments.

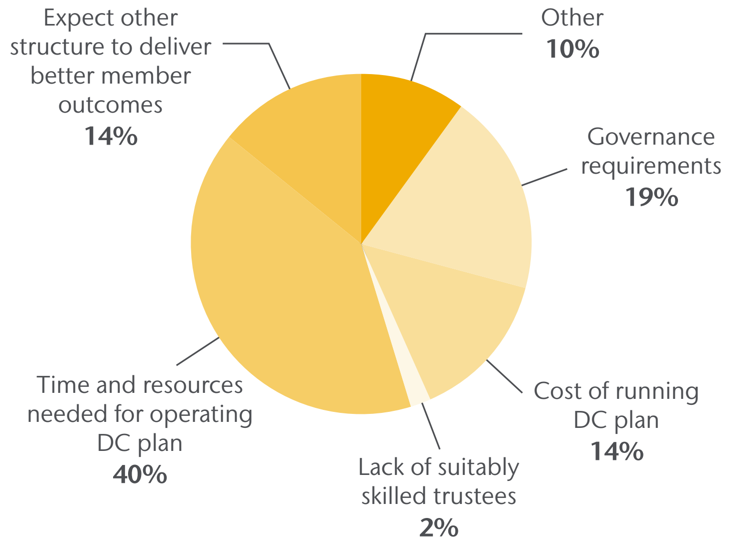
Q. What type of pension plan do you use to provide your main DC benefits? What would you expect it to be in five years' time?

2019 – Current vs. Expected in five years

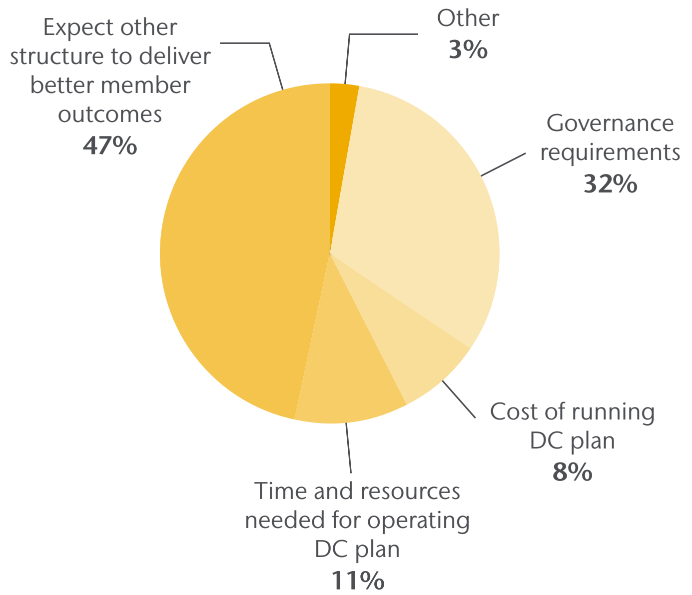


Reasons for moving from current governance structure

Currently trust-based



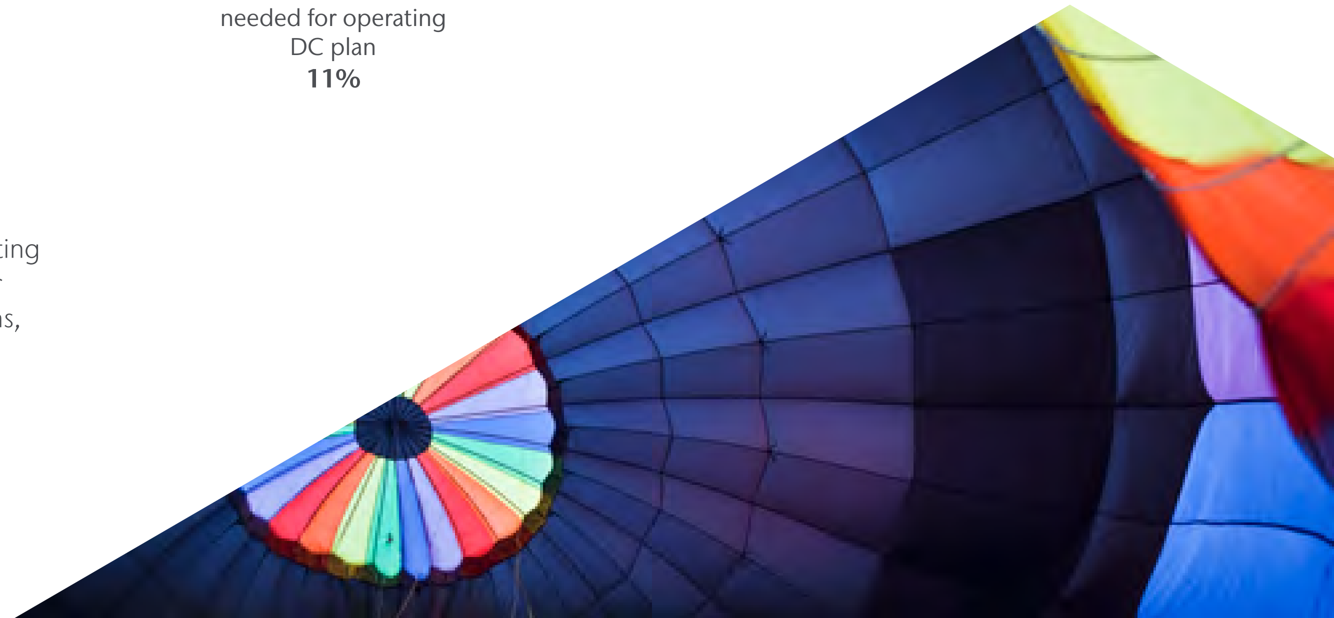
Currently contract-based



> Our biggest challenge is:
> Managing increased cost due to governance requirements

Aon's DC solutions

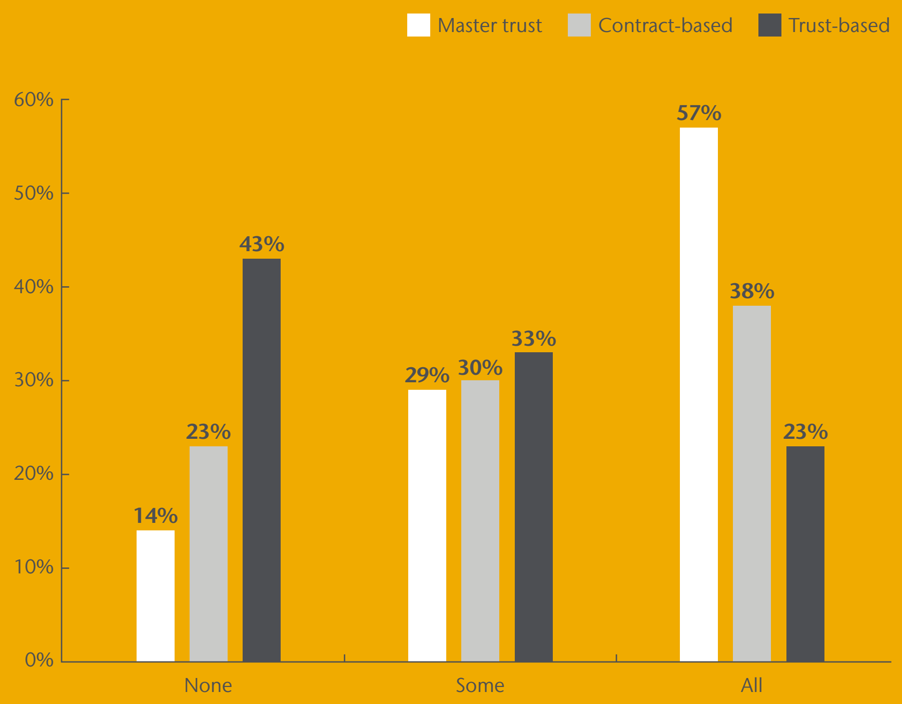
Aon can help with the full range of DC pension options – from consulting services and our delegated investment-only and bundled solutions for occupational trust-based schemes, through to our standalone solutions, The Aon MasterTrust and BigBlue Touch (Aon's GPP).



Delegating roles

One method to free up time for those running DC schemes is to delegate responsibility to third parties, for example the administration or investment. We found that over a third do not delegate any investment decision-making responsibility to a third-party investment professional, with this being four times more likely for a trust-based arrangement compared to a master trust. However, one in six trust-based schemes expect to delegate more over the next three years.

How much responsibility is delegated to third-party investment professionals?



1/3

do not delegate any responsibility to a third-party investment professional

Our biggest challenge is:

"Keeping up with governance and changes in compliance"

Aon point of view

Those responsible for pension schemes should regularly review whether their current operating model meets their objectives and delivers the best possible outcomes for their members. We expect the trend towards more delegation to continue, either through moving to a master trust structure, or by delegating specific functions like administration or investment. This will allow those running DC plans to free up more time to focus on the areas they want, such as strategy and member communications.

What are the desired outcomes?

SECTION 3

Fit for the future?

Q. What are the desired outcomes?

For members of DC schemes, good outcomes are about building an adequate level of savings to be able to retire at a time of their choosing.

For sponsors, the ultimate outcome is for employees to be able to retire, but shorter-term issues can sometimes take priority, such as benchmarking benefit levels to peers or controlling costs.

Contributions paid over time are one of the main drivers of the amount of pension fund for an individual. How that fund is used subsequently in retirement can also make a real difference to an individual's quality of later life, or even whether they can afford to retire at all.

Most individuals expect to rely on their company and State pensions in retirement (as found in our 2018 DC member survey – 'Living the Dream?'). Many will, of course, have other sources of income as well. It can be difficult for schemes to take these into account when considering retirement outcomes, we explore this more in Section 5 – Calibrate your comms.

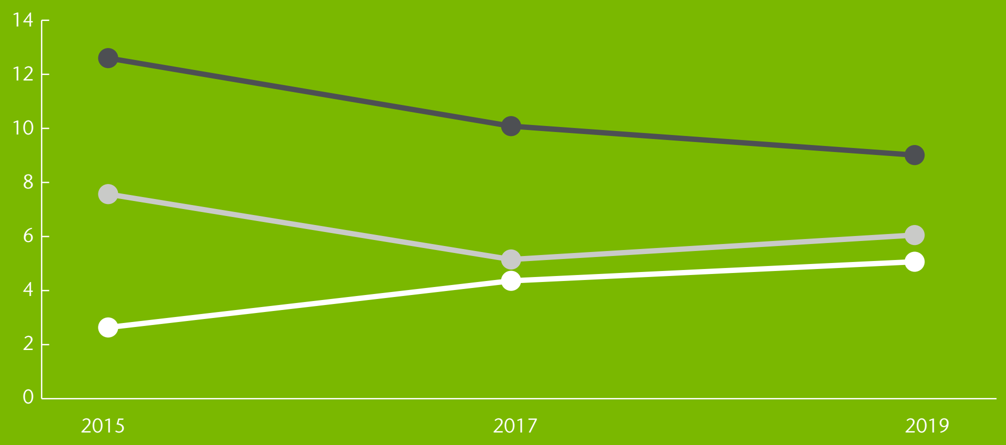
1 in 4

have employees on legacy DC contribution designs

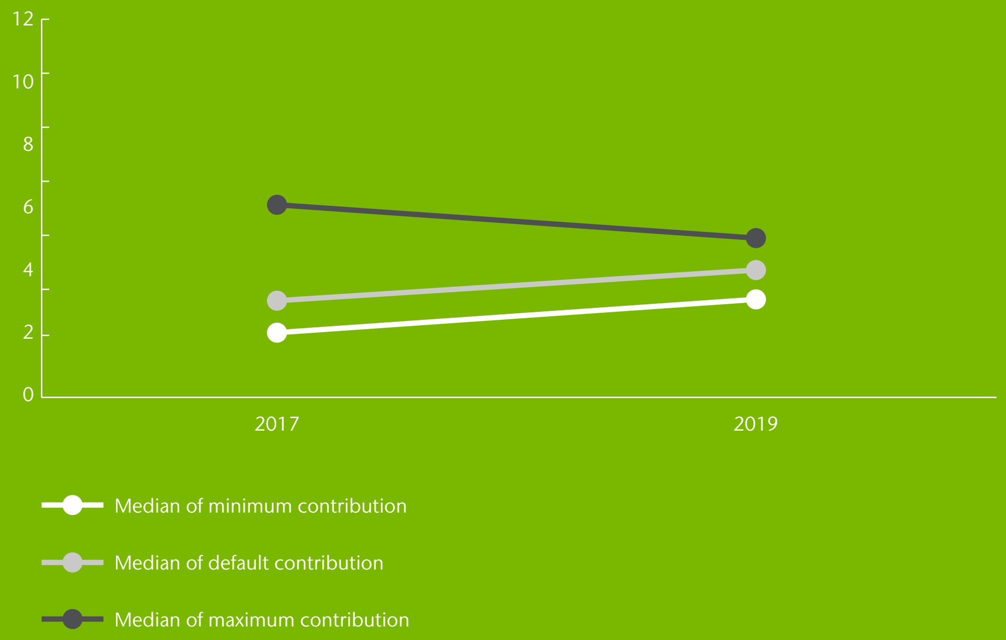
Most schemes are not supporting members with drawdown solutions

There is still a lack of awareness of expected retirement outcomes among those running schemes

2015 vs 2017 vs 2019 Average company contributions



2017 vs 2019 Average member contributions



Sources: 2015, 2017 and 2019 Aon DC Pension Surveys

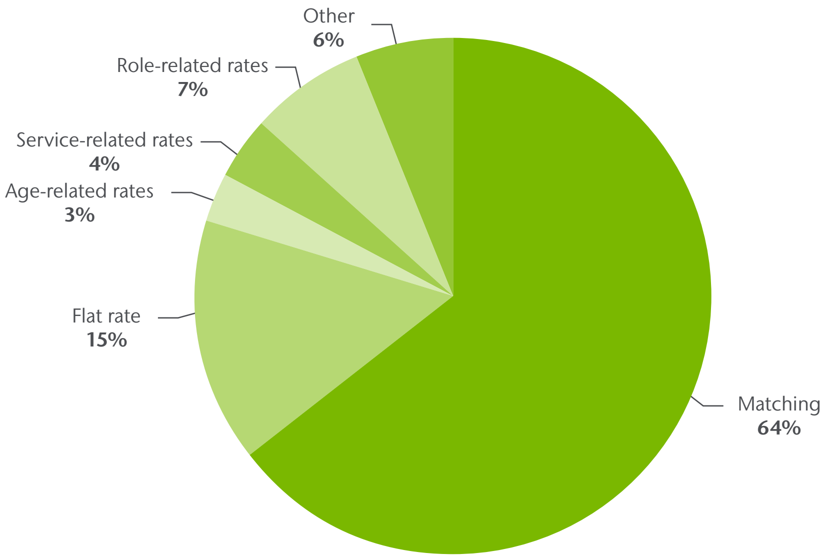
The level of contributions made by employers and members into DC schemes has a significant impact on outcomes at retirement.

Employers have had to meet the mandatory increases in minimum auto-enrolment contributions in 2018 and 2019, so we look at how that has affected both company and employee contribution rates.

Looking at contribution levels, our respondents' average default contribution rate is 10% (4% employee and 6% employer). This is higher than the average default found in our previous scheme survey in 2017, where it was 9%. However, the employer rate has remained stable at 6% while the employee rate has increased by 1%.

As more than 10% of employers are highlighting how to increase employee contributions as one of their biggest challenges in the next 12–24 months, whether this trend continues will depend on their success in overcoming this challenge.

How would you describe your contribution structure?



The default contribution level only tells part of the story on contribution rates, as the majority of schemes do not just offer a flat rate of company contributions.

A matching contribution design remains the most prominent scheme design, with around two-thirds of respondents offering members the option to increase their contribution levels and receive higher company contributions.

This type of design incentivises employees to save more and focuses spend on employees who are most engaged with the scheme.

Ranges of contributions offered

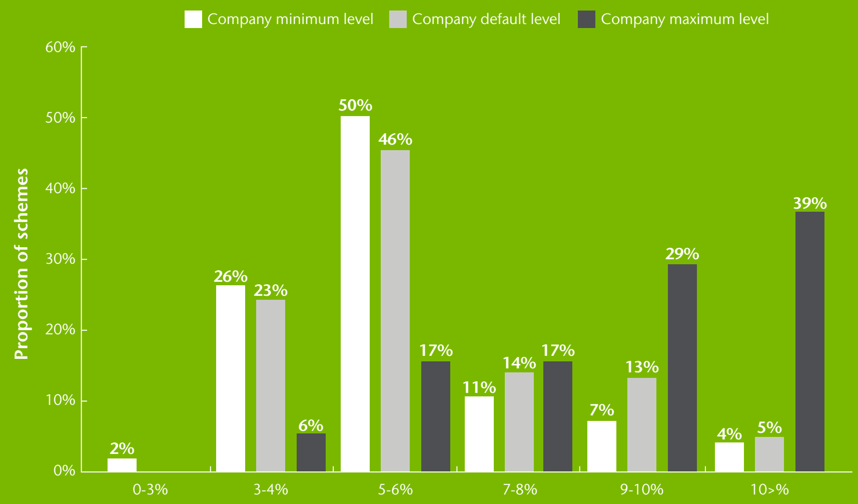
The spread of the minimum and maximum contribution rates (both employee and employer) has narrowed significantly since our previous survey.

Contribution rates are now more clustered around the median level. In part, this may be due to the auto-enrolment increases in the minimum levels, but it could also suggest that employers are carrying out more analysis of what competitors and the wider market are doing.

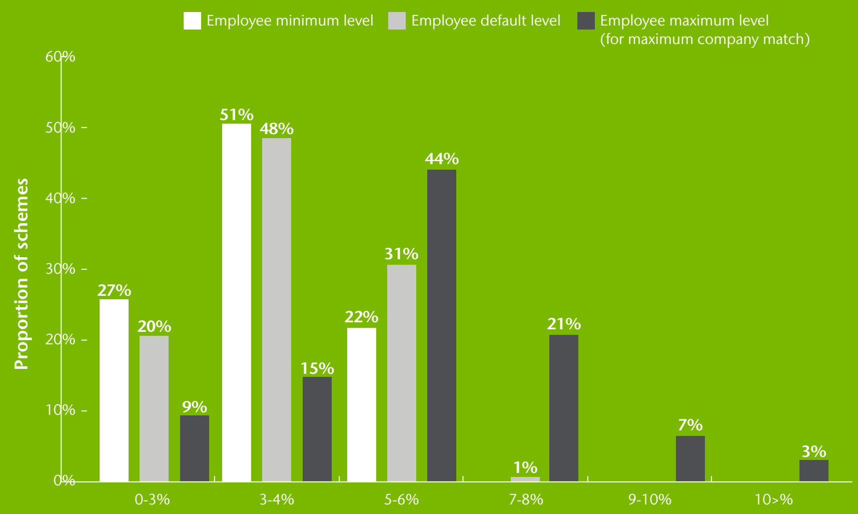
At Aon we have seen an increase in requests to benchmark pension contribution rates as well as other benefit levels.

This can be against a particular sector, a specified peer group or simply when compared with local competition for recruiting and retaining talented employees. Though the spread of contributions has narrowed, there is still a material difference between company contributions of 4% and 7%. Considering contribution levels without also looking at expected pension outcomes can be a risk for employers and will store up problems over the longer term.

Company contribution levels



Employee contribution levels



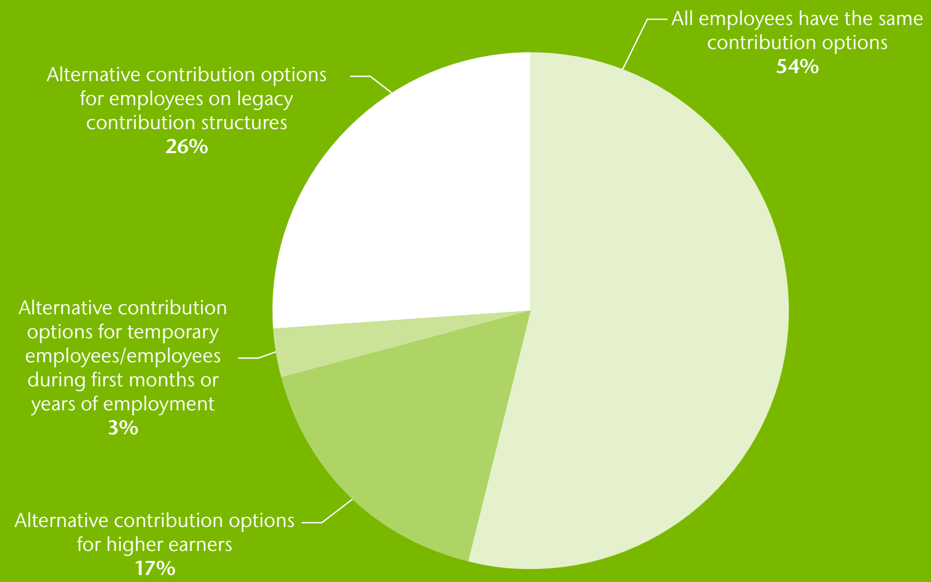
Q. Are all employee options equal?

We asked whether all employees are offered the same level of DC pension contributions.

Perhaps surprisingly, only around half of companies offer a consistent contribution design for all employees. Around a quarter have legacy contribution designs, in which the benefit level available for two employees in the same role could be different simply because of when they started work with the company.

17% have alternative options for higher earners. This may be to offer flexibility to those impacted by the annual allowance and tapered annual allowance restrictions on the tax relief available on pension contributions for higher earners.

There are schemes where higher contributions are offered to those at more senior role levels (around 7% of schemes as shown on page 21); these designs are becoming less common as the tax relief restrictions impact more individuals.



Thinking about the future – measuring the outcomes

We asked what the expected replacement ratio (pension income in retirement compared to pre-retirement earnings) would be for a typical lifetime member of their scheme.

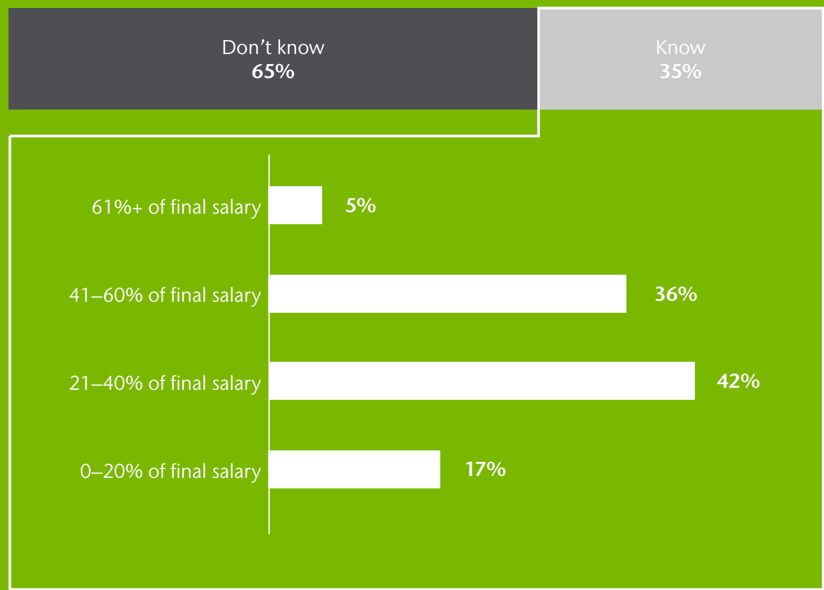
Two-thirds of respondents did not know what the ratio would be. Interestingly, most of these responses were from pension and HR managers.

Our 2018 DC member survey – 'Living the Dream?' – found that around two-thirds of employees rely on their employer when deciding how much to save towards their retirement.

As noted earlier, employers not thinking about contribution levels in the context of whether their employees will be able to afford to retire could be storing up a huge problem for the future.

Of the respondents who did know what the expected replacement ratio was, most of them are expecting a typical employee to receive between 21% and 40% of their final salary.

What is the expected replacement ratio (excluding State pension) for a typical lifetime member?



Aon point of view

We believe that most individuals and schemes focus too strongly on what contributions are being paid rather than how much they might receive in retirement.

Looking at projected outcomes across a scheme's membership using tools like Aon's DC Analytics can help those running schemes to identify how many are on track for an adequate retirement and which groups need more help.

Encouraging members to set a target to work towards, such as the PLSA/Loughborough University Retirement Living Standards (see next page), is an important step in helping them to understand their pension and how it fits into their wider retirement savings.

The Standards are the property of and are provided by the Pension and Lifetime Savings Association and Loughborough University.
https://www.retirementlivingstandards.org.uk

The Pensions and Lifetime Savings Association (PLSA) recently launched its Retirement Living Standards. These are the levels of income required to achieve a defined standard of living in retirement – Minimum, Moderate or Comfortable. The moderate level was determined to be around £20,000 per year for a single person living outside London. The State pension will likely make up a portion of this, but most employees will be looking to their company pension plan to make up the rest.

Section 5 – Calibrate your comms, looks in more detail at how you can use these Standards to support members.

The Retirement Living Standards aim to encourage individuals to think about how much they will need to save for retirement, but are employers considering whether their employees will have enough?

Astonishingly, only 25% of our survey respondents said that the employer had considered pension retirement outcomes in future workforce planning. This is a high-risk approach for companies as reliance on DC pensions grows over time.

The inability of members to afford to retire is likely to lead to an ageing workforce, with potential benefit cost implications. This could also limit career progression opportunities for younger employees and cause succession challenges.

At retirement

We know that drawdown is becoming the most popular method of taking DC pension funds at retirement. Our 2018 employee survey found that over three times as many employees expect to access their DC pension using drawdown (65%) compared to buying an annuity (20%) or taking a single cash lump sum (14%).

This is an area where many schemes are still lagging behind their members' needs. Most have not put a preferred drawdown solution in place for their members, and those who do have one often rely on whatever their current provider offers. This may not always be the most suitable solution for their members. Some schemes may only have a few members retiring at the current time, but those that are accessing DC funds will still need support to get the best outcome.

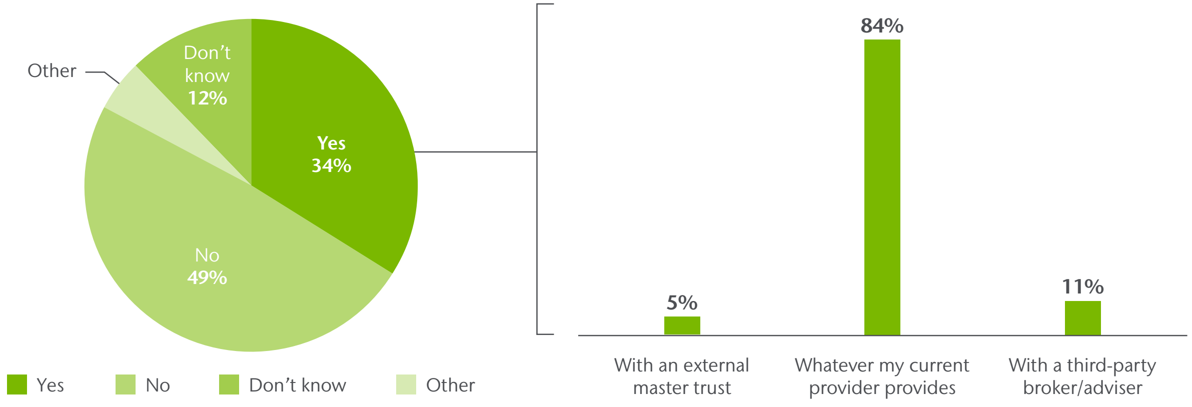
Quick win

Ask your DC adviser to update you on what retirement support for members is available in the market, including drawdown solutions. Compare this with what is offered by your current DC provider to understand whether this is the best option for your workforce.

The Aon Retirement Service is a multi-platform support service for scheme members approaching retirement.

It provides education on the different options available, allows members to speak to an expert for guidance, to transact for best-buy annuity purchase or a default drawdown option.

Have you put a preferred drawdown provider in place?



SECTION 4

Made to measure

An ever-changing investment landscape

DC investments and charges

We are now nearly five years on from the Pensions Freedom changes which led many DC schemes to rethink their default investment approach.

> Our biggest challenges are making sure our employees are being charged fair fees (no hidden fees), have a good return on investment and are prepared for Brexit.

Generally, since the 2008 financial crisis, we have experienced a sustained period of positive returns across most asset classes. How do schemes plan to address new challenges, such as finding returns for their members with the expectation of a lower-growth future, and the emerging demand for a greater focus on responsible investment, including new regulatory requirements? How can your DC plan stay on its 'A' game?

Investment to-do list:

- Check your default aligns with your members' needs.
- Streamline your selection of self-select funds to increase engagement.
- Consider the integration of responsible investing into your default fund option and use it as a tool for engagement with members by explaining the connection between their pension savings and the impact on the wider world.
- Review your investment charges on a regular basis to ensure your members benefit from any reductions.

1 in 5

investment defaults still target annuity purchase

Just 8%

of default funds invest in ESG funds

Investment default charges are falling, but underlying fund charges less so

Default investment options

A DC scheme is required to provide a default investment option if it is to be used to comply with auto-enrolment legislation. Most members will remain in this default option rather than making their own investment choices.

Typically, schemes offer a lifestyle or target-date default investment option. This is where a member's DC pension savings are initially invested to target higher growth and gradually switched as the member approaches retirement into assets designed to be appropriate for the method by which they wish to access their savings.

Only

11%

of individuals purchased annuities with their DC funds in 2018/2019

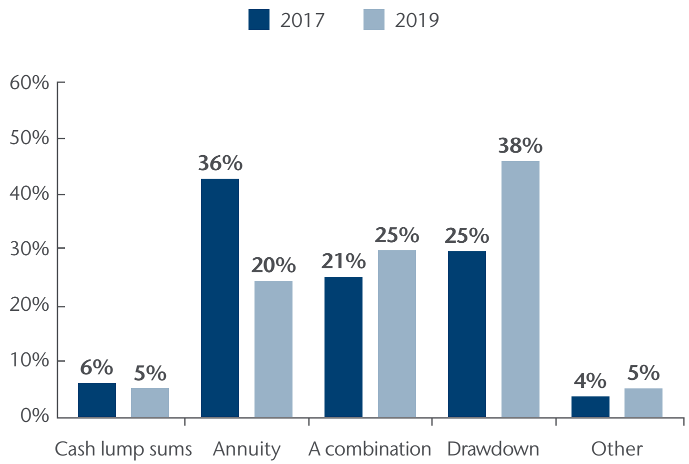
Following the Pensions Freedoms introduced in 2015, there has been a major change in how DC members access their savings. Prior to this, nearly all DC members who could not take their funds under trivial commutation rules used their DC funds to buy an annuity at retirement. By 2018/19, the Association of British Insurers reported that the percentage of individuals purchasing annuities with their DC funds was just 11% of the total.*

The new FCA retirement pathways requirement for contract-based schemes will soon also require a default investment path in retirement. It is likely that trust-based schemes will follow over the next few years.

* Source: FCA website

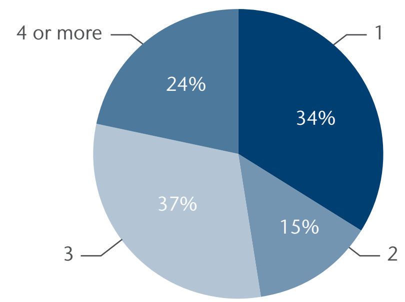
Our survey found that DC schemes have been adapting to these changes in member behaviours. Flexible drawdown is now the most popular target for a default investment. A ‘keeping your options open’ approach is the next most popular, with one in four DC schemes offering a mixed target approach for their default investment. It could be argued that these two approaches are very similar in that they both result in a multi-asset investment mix that aims to maintain above-inflation growth potential.

While annuity purchase at retirement has become less common over the last two years, our research discovered that a surprisingly high one in five schemes still offer an annuity target as their default investment option. Is this an active decision or a lack of a review?



Our research found that the most common approach is three lifestyle or target date options. Around a quarter of schemes only offer one, and around the same number offer four or more options to members, with contract-based pensions having the highest proportion of schemes in this category. Master trusts are the least likely to offer four or more.

How many lifestyle or target date funds do you offer to members?



While drawdown is the most popular choice, some members choose to access their DC funds in other ways. Schemes are generally looking to accommodate this by offering alternative lifestyle or target funds, aiming to target different options at retirement.

Choices, choices, choices

In society today, we are bombarded with choice. Whether in fashion brands, mobile phone models, or eating out, we are surrounded by a sometimes unfathomable list of options.

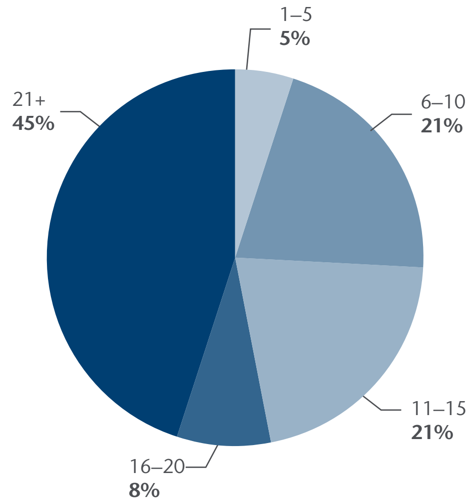
The same can often be said for pension members. Being able to offer an extensive range of individual self-select funds to members was once viewed by some as an important aspect of DC schemes. It gave members flexibility and choices to determine their own future. However, it has become more widely accepted that for most DC members, a large number of investment choices can be a negative.

Too many investment options can make a pension seem overly complex; members are ill-equipped to make investment decisions about their pension savings which can reduce engagement. In addition, offering a high number of self-select funds will increase the complexity of the scheme governance, potentially impacting the trustees' or governance committee's ability to monitor their members' investments adequately.

Aon's DC Solutions

The investment approach taken by Aon's own delegated DC Solutions offers a simple and concise investment menu. It accommodates members under three behavioural characteristics: 'Do it for me' (target date options), 'Help me do it' (objective based funds) or 'Give me full control' (choice of asset classes and specialist funds).

How many self-select investment options do you offer to members?



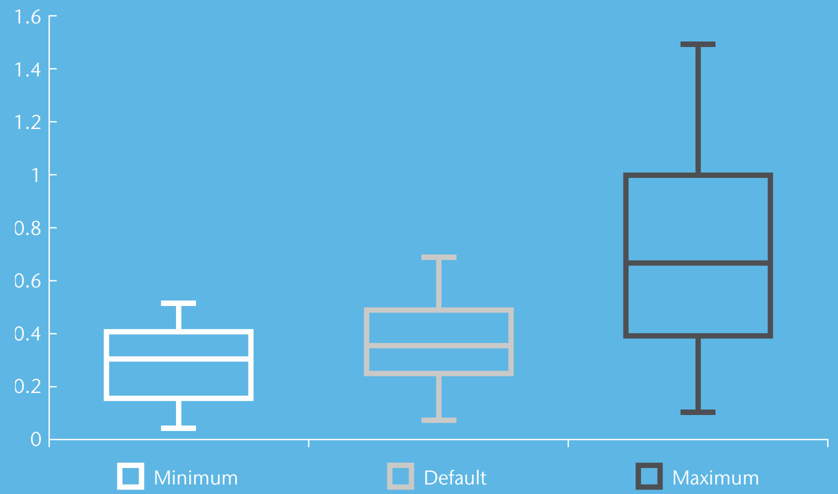
At Aon, we believe in making pensions easy for members. Our DC consultants work with schemes to agree an appropriate range of member investment choices. We help schemes to understand the appropriate level of ongoing monitoring and whether they have adequate governance in place, need to make changes, or should consider delegating this aspect of running their DC scheme. See Section 2 – Weigh up your options, for more on how DC schemes delegate different aspects of their operation.

Charges

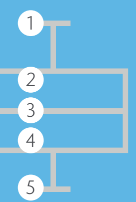
Our analysis found that average charges for default investments have fallen over the last two years, but underlying fund charges have been broadly unchanged.

The fall in default charges may be due to the increase in scale as DC fund values have grown since 2017. However, a much smaller reduction in the typical minimum fund charge (such as a passive fixed-interest investment option) suggests that there are other considerations at play. It is likely that many schemes are taking a more passive investment approach in their default option, perhaps being driven by a focus on cost. While this may seem appropriate in a period of sustained growth, there may be more risk to members in the event of a prolonged market downturn when paying a higher charge for diversification may be invaluable for savers. When considering the investments offered to members, we believe the focus should be on value and potential outcomes, rather than cost in isolation.

Q. What charges do members pay?



Reading the box plot charts



The centre line (3) in each box represents the median average result, while the top and bottom of the ‘box’ represent the second (4) and third (2) quartiles (ie, the middle 50% of answers).

The end of the whiskers represent the bottom (5) and top (1) deciles, so any results outside these lines are either in the bottom 10% or top 10% of scores.

Responsible Investing

Those running DC schemes are being compelled to consider Responsible Investing – and not just by societal pressure. The Pensions Regulator now requires trustees of DC schemes to state their policy on financial and non-financial matters in relation to ESG.

Historically, the view was that Responsible Investing would very much fall into the non-financial category, ie, it was a matter of ethics and therefore most trustees and employers took the view that it was up to individual members to choose whether they wanted to invest in this way. However, this view is changing.

We are seeing increasing pressure on governments to curb carbon emissions and reduce nations' impact on local ecology (eg, Brazil and the Amazon rainforest). People are becoming more aware of issues relating to how goods are produced, such as concerns about slave labour, fair pay or cruelty to animals.

Companies linked to environmental damage or social issues are under increased scrutiny in the public eye.

Many companies developing environmentally friendly technology or a reputation for being socially aware have gained a strong footing in their respective fields. As a result, investing in funds aligned with these factors can be increasingly profitable and is seen as a sustainable way to generate financial growth.

Jargon buster

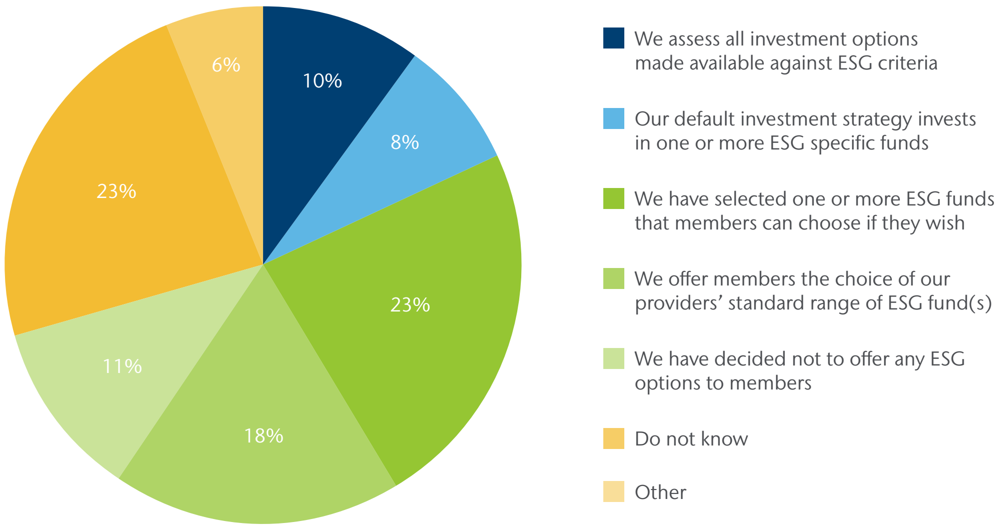
ESG stands for Environmental, Social and Governance.

ESG investing aims to take positive environmental, social and governance factors into account in investment decisions.

The most popular approach, taken by around two in five schemes, is to offer one or more self-select ESG investment options to their members, either through design or based on their provider's standard offering as shown in the pie chart. Only half as many actively incorporate ESG principles on behalf of members, either through investment as part of the default option or by assessing all funds offered against ESG criteria (the blue segments).

Our 2019 Responsible Investment Survey found that over 85% of UK investors consider Responsible Investing to be at least 'somewhat important'.

Approach to Responsible/ESG Investment



57%

of members would be more engaged with their pensions as a result of Responsible Investing

Some schemes are also using Responsible Investment as a way to engage with members. According to the Defined Contribution Investment Forum in Q4 2018, a survey focused on ESG investments found that Responsible Investing would make 57% of members more engaged with their pensions. Schemes that can share 'good news' with their members about how their pension savings are working to make the world a better place, as well being invested to grow, will be able to engender pride and raise engagement with members.

Alternative asset classes

Despite the increasing prevalence of investing alternative assets in DB plans and consultations about extending this type of option to DC, just 6% of DC schemes say that they would like to extend the range of investment opportunities but are unable to offer the investment types they would like to provide.

This is perhaps surprising, particularly given the focus on exploring ways in which DC members can benefit from the **illiquidity premium** associated with infrastructure or private market investments. There may be various reasons for this: the addition of alternative asset classes can seem extremely challenging, or schemes may feel that their current governance structures or knowledge levels are not suited to effective monitoring of these types of investments. There may also be concerns about potential delays in accessing illiquid investments when schemes need to pay benefits. This can be solved by receiving further training from your investment consultant or delegating investment responsibilities, as covered earlier in this report in Section 2 – Weigh up your options.

Jargon buster

The **illiquidity premium** is the idea that investors should expect to receive a premium, or higher return, on investments which require funds to be committed for a longer period of time in return for the risk of not being able to easily access them.

Quick win

Ask your adviser or provider to deliver a training session on alternative investments and different methods of accessing them for a DC scheme. Then you can balance the potential benefits with any challenges to decide whether you think they could improve outcomes for your members.

How Aon can help

Aon consultants can provide analysis of the range of outcomes from your scheme's investment strategy, by using stochastic modelling of projected outcomes of different asset allocation models for your representative members. This approach informs trustees and scheme managers, allowing them to understand the expected range of returns and downside risks that their default investment strategy and alternatives could have for their members. Trustees and companies should consider whether the current investment strategy remains appropriate or whether a delegated approach might help deliver better outcomes for members.

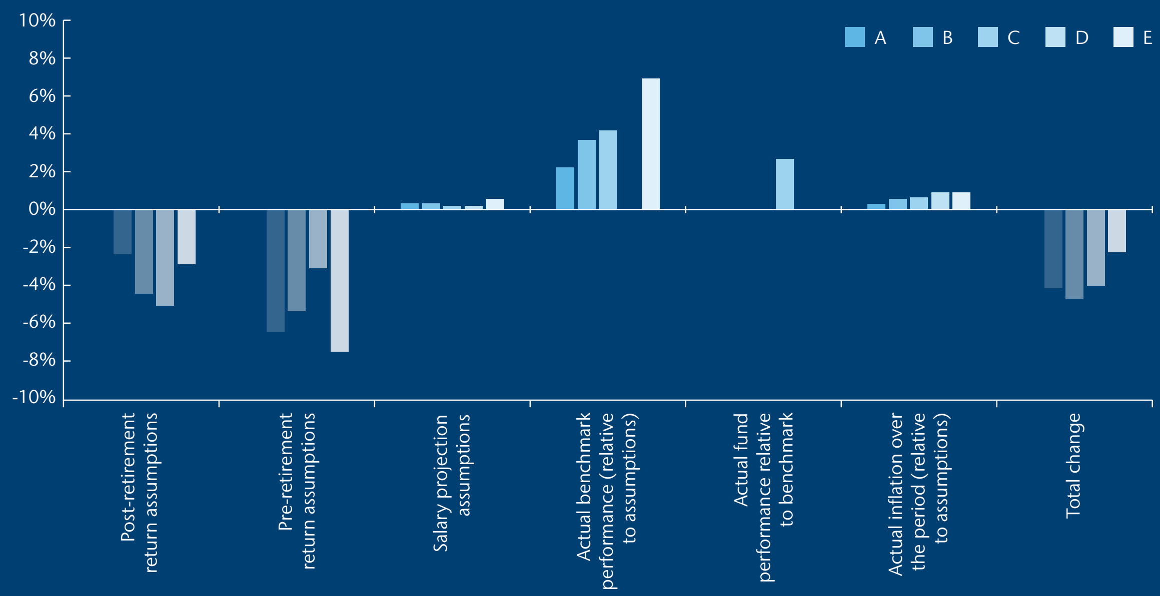
Aon point of view

It is important that investment defaults are aligned with member needs, not just in terms of how DC benefits will be taken at retirement, but also in terms of appropriate target levels of investment risk and return at different stages.

Scrutiny of pension schemes' approaches to Responsible Investment is on the rise and, increasingly, members will want to know where their savings are being invested.

The expected lower growth future environment may mean that DC default funds need to adapt to achieve appropriate levels of growth. Those running schemes should seek to understand new types of DC investment opportunities and whether they are appropriate for their members.

Example member retirement outcomes analysis



Effective measures

Most DC schemes measure the performance of their underlying investment funds against benchmarks, but this may not give them the full picture. It can be useful to measure the aggregate performance of the building blocks at different stages of a lifestyle. These can be measured against objectives such as a specific return target in the case of the growth stages, or volatility or maximum downside targets in the later stages as members approach retirement. Some schemes are now measuring changes to projected member outcomes. These look not only at historical inflation and fund performance data, but also consider changes to forward-looking assumptions to understand how the projected retirement savings of typical scheme members are changing over time.

SECTION 5

Calibrate your comms

We need to talk about pension plans and financial wellbeing

Target-setting for retirement

37% of employees believe that the Government's minimum automatic-enrolment contributions rate is the recommended amount to save for retirement*.

This shows that more needs to be done to help employees understand how much they need to save. This is backed by the results from Aon's 2018 DC member survey – 'Living the Dream?' – which showed that around two-thirds of employees rely on their employer when deciding how much to save towards their retirement, and that more than half have not set a target for how much to save before they can fully retire.

Both employers and trustees of pension schemes need to focus their attention on encouraging employees not just to save more, but to save at adequate levels for the standard of retirement they desire.

Increasingly, it is being recognised that pension saving is not something that individuals consider in isolation, but as part of their wider financial situation. Leading DC plans are working with sponsoring employers to support members with their overall financial and wider wellbeing.

* Source: Pensions and Lifetime Savings Association employee survey September 2019

1 in 3

schemes communicate targets to encourage employees to save at an appropriate level

Around **30%**

Creating a **financial plan** and **saving outside of pensions** are the main areas where schemes plan to expand

50%

of schemes do not measure members' engagement with retirement and financial programmes and only 25% measure on a regular basis

Q. What methods do you use to encourage employees to save at appropriate levels for retirement?

Our biggest challenge is:
I want to deliver value for money from a company perspective

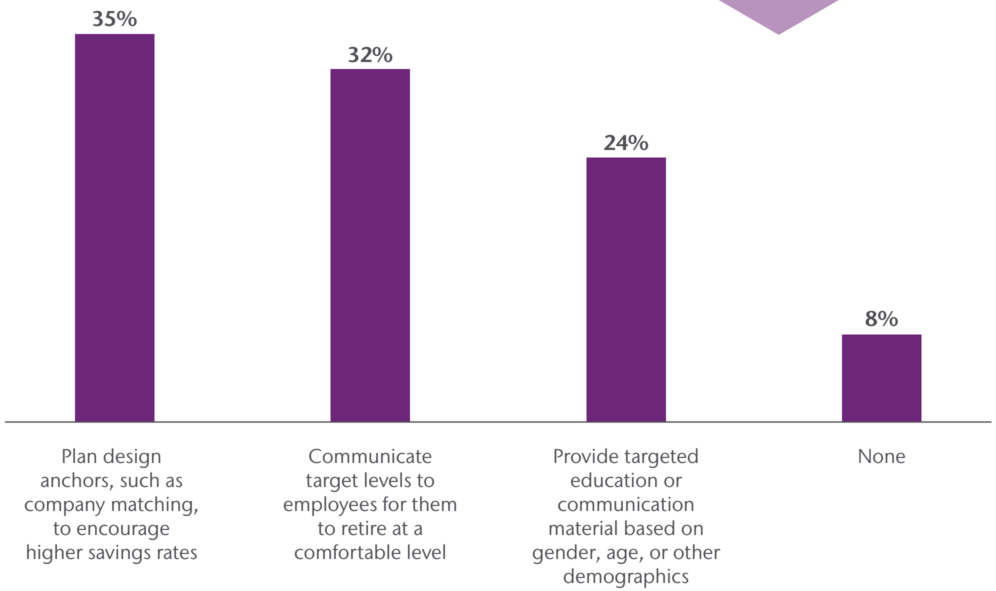
The most popular method used by those running schemes to encourage members to save more is the use of plan design anchors, such as matching contribution rates. Research carried out by Age UK* in 2014 showed that the impact of introducing matching contribution rates varies across income levels, with those on lower incomes the most difficult to target to increase contributions, even when there are higher rewards on offer. This research suggests that relying on plan design alone will not ensure that members are on track to maintain their standard of living in retirement.

Jargon buster

Auto-escalation is the automatic increasing of contribution levels on a regular basis.

Around a third of those running schemes communicate one or more targets to their employees to help them retire at a comfortable level. This covers those who provide target contribution rates, target fund values and target retirement income levels. These can be used as part of regular communications, member presentations or online tools that members can access.

We are starting to see some schemes implement the auto-escalation of contributions. This could either be as a choice for members or as a default position. The phased introduction of contribution levels for auto-enrolment and subsequent low level of opt-outs following the increases has shown that this is an effective way to achieve higher contributions into DC schemes.



* Source: 'Building an income for retirement: approaches to encourage more pension savings' a discussion paper by Age UK, September 2014

The use of targets to help engage employees is consistent with the message behind the PLSA/Loughborough University Retirement Living Standards, recently launched by the Pensions and Lifetime Savings Association (PLSA). These are designed to help people consider the standard of living they want in retirement and understand how much it would cost them to attain this. The PLSA says that 70% think that retirement income targets would encourage them to save more so they can achieve their ultimate target.

What else can those running schemes do to encourage members to save more? Aon's research shows that approximately a quarter use targeted communications or education material based on member demographics as a method of encouragement. Using demographics to target communications is just one option, so it is important to consider other factors such as role or member attitudes.

The key to effective communication and engagement is understanding these differences and ensuring that content is both relevant and informative for the group you are targeting.

The PLSA/Loughborough University Retirement Living Standards

As covered in the previous section, the PLSA has introduced retirement income targets* to help savers understand how much they need in order to have a minimum, moderate or comfortable retirement. These lifestyles are defined in reference to a number of pre-defined categories.

	Single	Couple
Minimum	£10,200 p.a.	£15,700 p.a.
Moderate	£20,200 p.a.	£29,100 p.a.
Comfortable	£33,000 p.a.	£47,500 p.a.

"Our biggest challenge is: Engaging people to save more as a habit, not just in pensions"

Aon's DC Analytics can help you to determine and regularly monitor who is on track for a reasonable retirement outcome and who is not.

This analysis can then be used to decide where to focus your efforts as it can identify specific factors which are impacting outcomes.

Contact your usual Aon consultant or email talktous@aon.com to learn more about Aon's DC Analytics and other defined contribution services and solutions that Aon can offer to help encourage your membership to save more.

Aon point of view

Member presentations and workshops can help support your members in understanding what they should be targeting in retirement. For example, using a target-setting presentation as part of the annual enrolment exercise could help members to visualise what they want in retirement and the planning tools available.

* Source: The PLSA/Loughborough University Retirement Living Standards (https://www.retirementlivingstandards.org.uk/)

Financial wellbeing support

Financial wellbeing is a hot topic on many agendas, and pensions is a key part of any programme.

The most popular financial wellbeing support currently offered is ‘saving for retirement’, followed by ‘insurance’ and ‘creating a financial plan’. At Aon, we summarise financial wellbeing support into four key areas using our four P’s framework: prepare, plan, protect and preserve. The most popular wellbeing support focuses on ‘plan’, building a short-, medium- and long-term plan, and ‘protect’ against the unexpected.

Our research shows that those running schemes are planning on expanding their support in all areas, with understanding and creating a financial plan, saving for emergencies and saving for long-term goals other than retirement all priorities flagged for the near future.

Prepare – build financial knowledge and skills

Plan – build a short-, medium- and long-term plan

Protect – against the unexpected

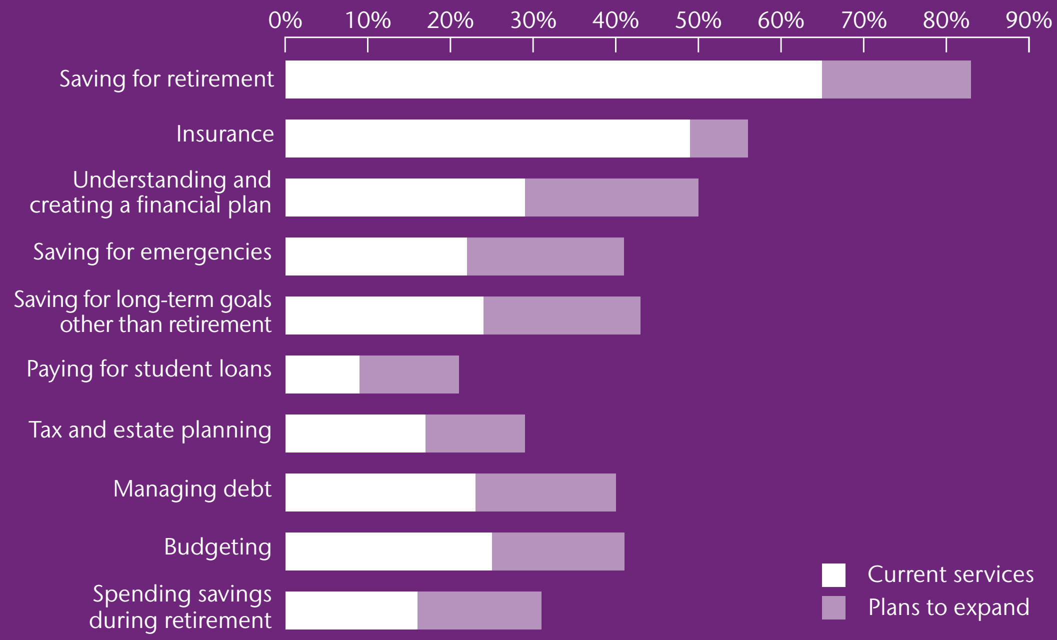
Preserve – understand needs after work and transition to retirement

“Our biggest challenge is: Getting members to own their future financial security”

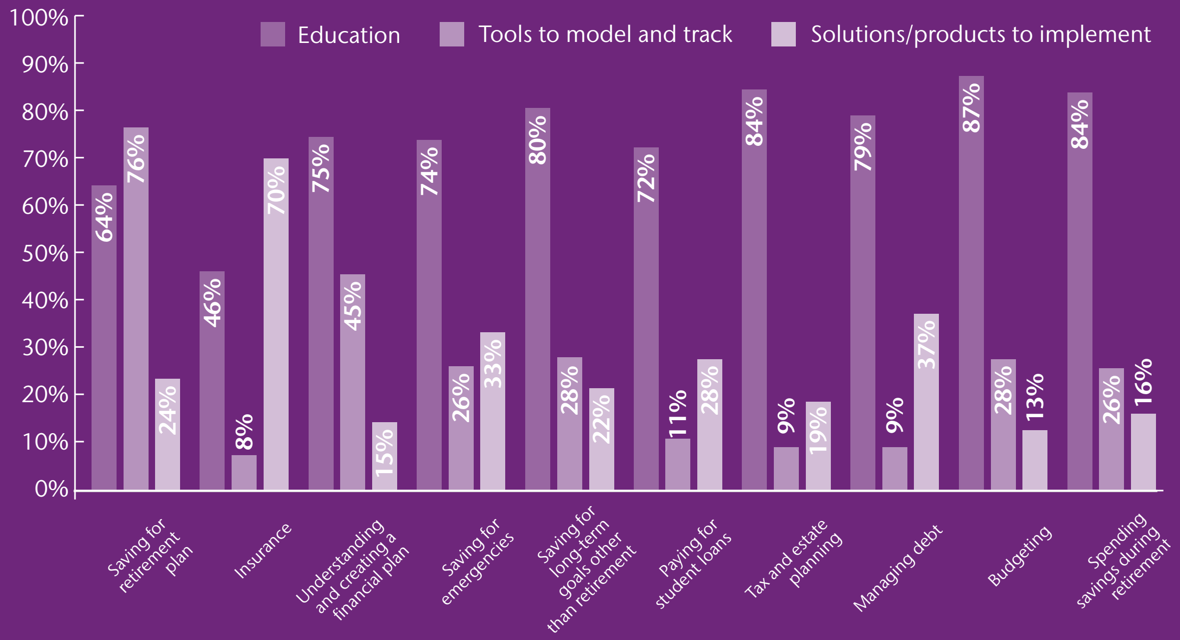
From Aon's 2018 'Living the Dream' survey, we found that most individuals in the early part of their career would like their employer to provide some sort of support on financial topics and as people progress towards retirement, the focus turns from day-to-day financial needs to more specific areas.

Q. Do you offer services in any of these financial wellbeing areas?

From our 2018 member survey, in person one-to-one education sessions were the top choice for getting support on managing finances. Tools or technology to track success were also popular, as well as financial products offered through the employer. Our survey this year shows that employers are responding to their employees' needs as financial education is the most commonly offered service in financial wellbeing support. However, modelling tools and products were less common, suggesting that employers could look to expand what they offer in those areas to meet employee needs.



Q. What types of service, if any, do you offer in each of these financial wellbeing areas?



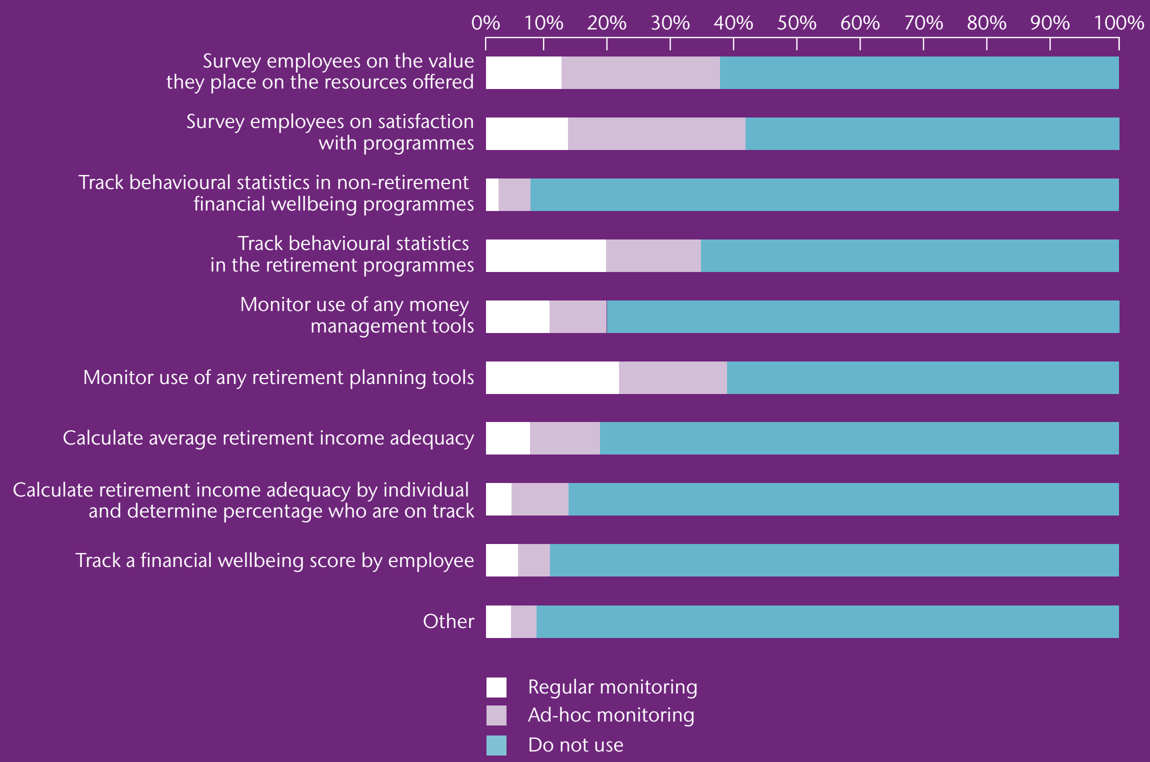
Aon's financial education team runs a range of seminars for our clients targeted at different groups, for example those joining a company, those towards the middle of their career or those approaching retirement.

Measuring success

Our research shows that while there is a variety of ways in which employee engagement with retirement and financial wellbeing programmes can be measured, the majority of those running schemes do not measure success.

Q. How do you measure employee engagement with your retirement and financial wellbeing programmes?

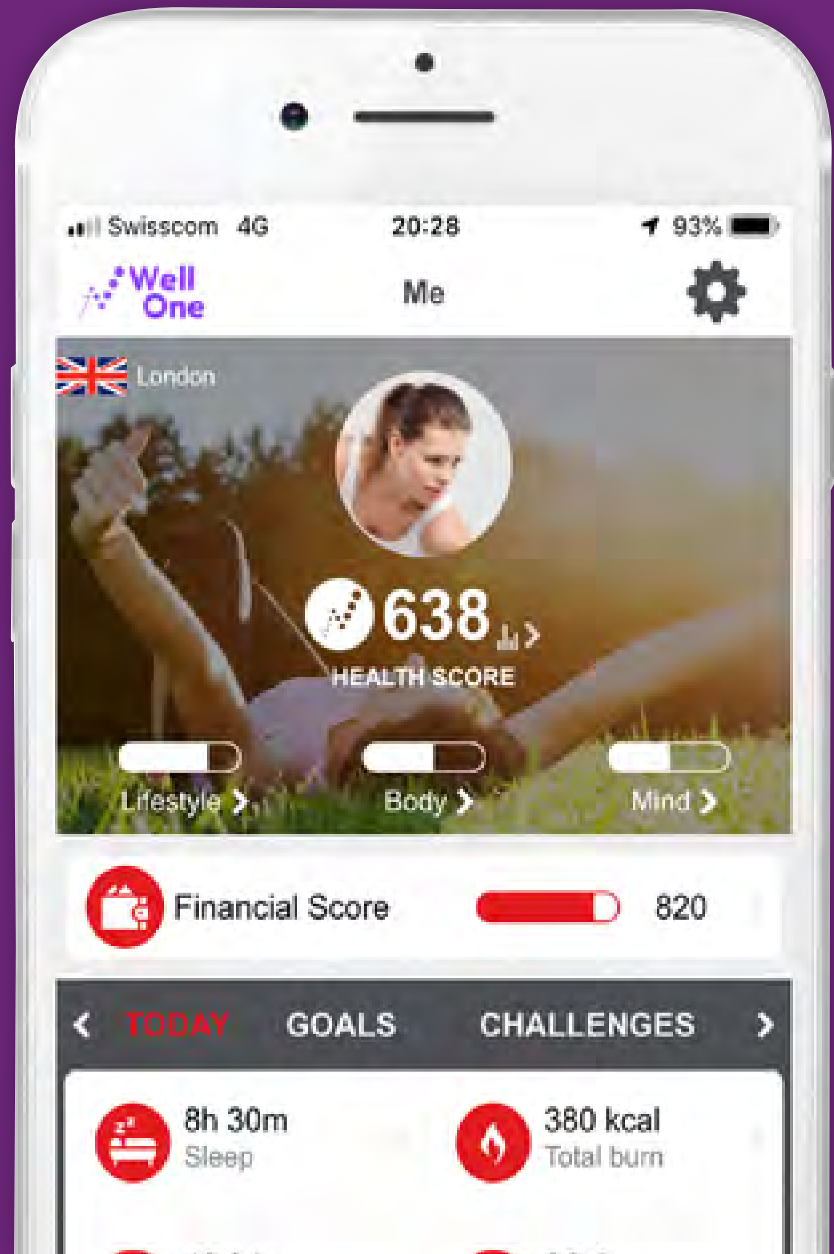
Determining whether initiatives have met your objectives is key to maintaining a successful strategy – and there are several ways in which this can be done. The most commonly-used methods include conducting employee surveys and monitoring employees' use of the tools in place. Another option is monitoring which members are on track for an adequate retirement outcome; however, only 14% of those who currently monitor employee engagement do this.



Reviewing changes to retirement adequacy is vital to measure success as this is a key objective for many running DC schemes

Well One

Our Well One app provides clear, data-driven insights on the wellbeing of individuals, teams and the wider business using simple health scores. Analysing data from four areas – physical, emotional, social and financial – Well One helps bring focus and clarity to strategy and communications, while enabling healthy behavioural change for employees.



Do you know where to focus?

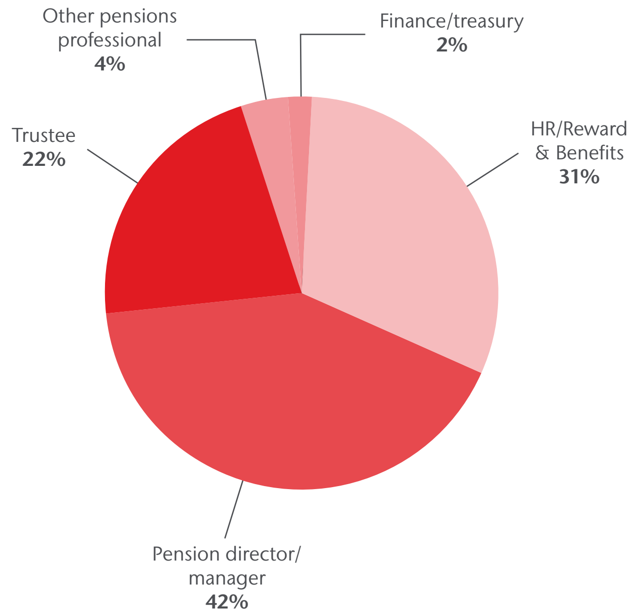
Our financial wellbeing audit identifies your employees' financial wellbeing needs and the appropriateness of your current benefits to meet these.

Breakdown of survey participants

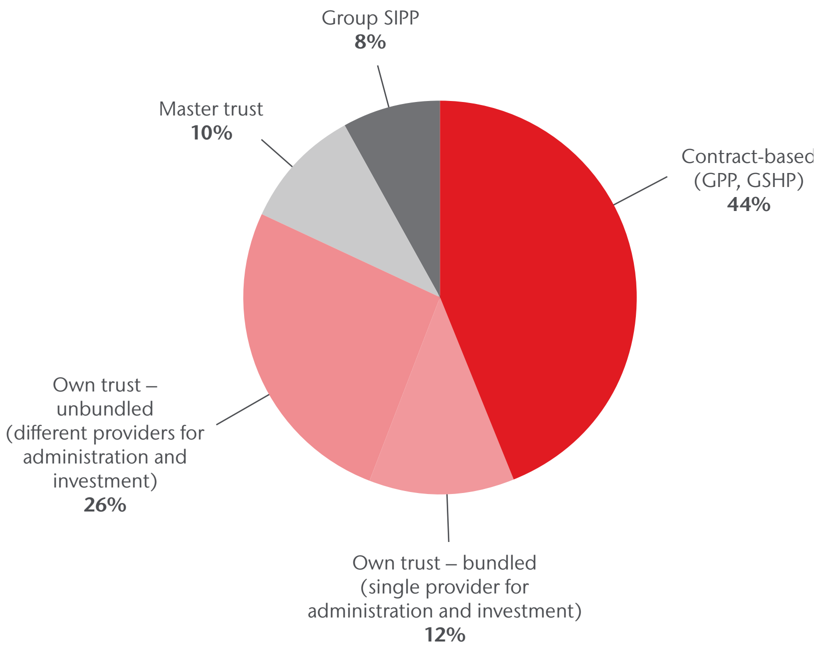
This research encompassed a wide range of DC schemes, including occupational trust-based schemes and Group Personal Pensions, as well as a broad range of scheme sizes.

Despite the broad range of structures and sizes, many of the experiences and views expressed through the survey are very similar. Where we have seen differences by type or size, we have highlighted them.

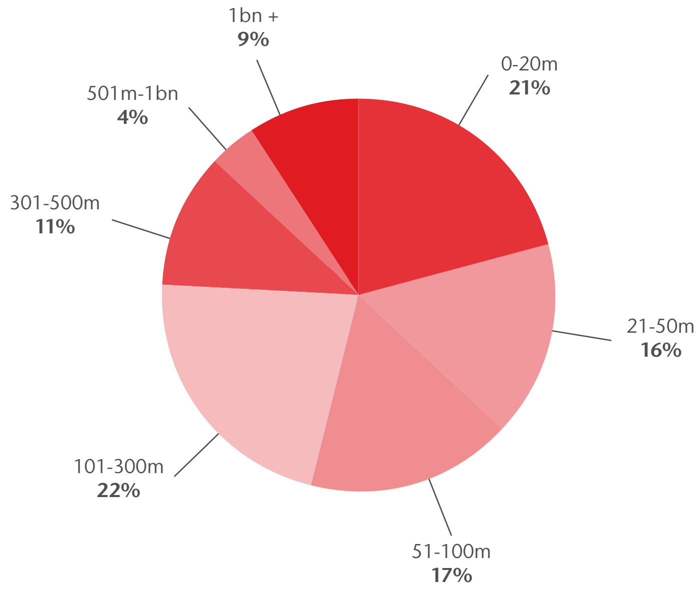
Role of respondents



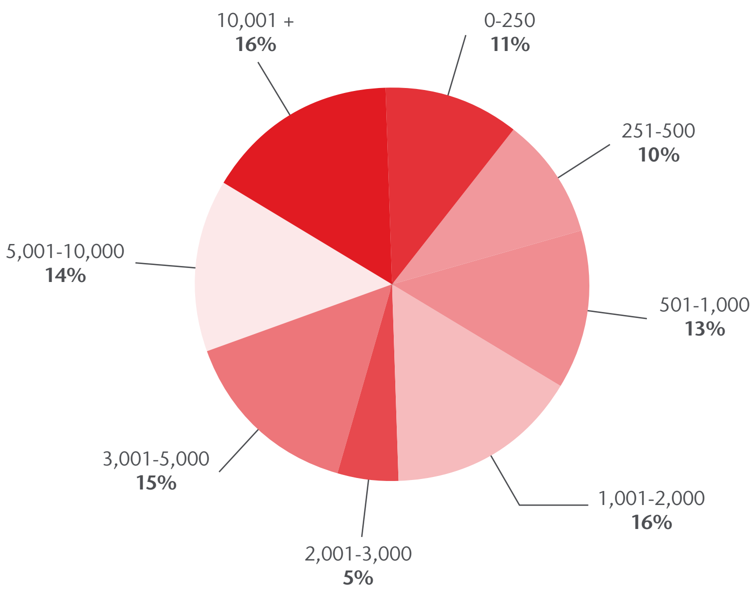
Type of DC plan



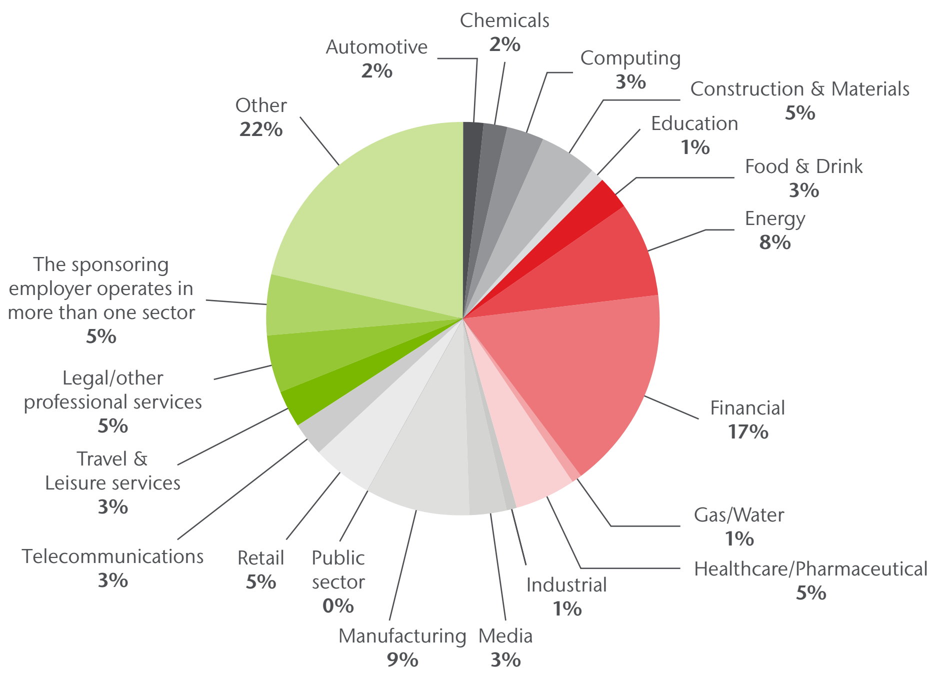
Size of DC plan



Total number of DC members



Sector of sponsoring employer



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About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

For further information please visit: aon.mediaroom.com

Empower Results®