Drawdown: Is it working for consumers?

An analysis of consumer trends and behaviours in flexi-access drawdown

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Overview

It's three years since the Government revolutionised the retirement market by scrapping rules that compelled many people to buy an annuity.

Since then, consumers have embraced their new freedom, with twice as many people now putting their pension into drawdown, as buying annuities[1].

But while more and more people are moving into drawdown, little is known about how it is working for the first wave of pension freedom retirees embarking on it.

This report – based on a sample of almost 750 people – is the first and largest study to explore the impact of drawdown on both the financial and emotional well-being of consumers.

Overall, we find that drawdown has been a clear success from the point of view of consumers, who are embracing the freedom and flexibility it gives them over their pension savings. Eight in 10 people, for example, would choose to put their pension into drawdown if they were making the decision again.

However, a number of areas of potential concern are also starting to emerge:

- **First-time investor gap** – the highest proportion of consumers moving into drawdown have no investment experience, yet a significant number of these individuals are not seeking either advice or guidance
- **Drawdown gender gap** – compared to men, women in drawdown reported lower levels of investment experience, financial confidence, and engagement – pointing to the potential emergence of a new drawdown gender gap
- **Income sustainability gap** – initial evidence suggests that consumers could be making poor choices over their withdrawal strategy, taking the same level of income regardless of how the stock market has performed
- **Later-life security gap** – while the population in drawdown is rising, few consumers are making adequate plans for managing drawdown in old age, meaning there could be no one to manage their pension if they no longer can

The need for financial advice and guidance is greater than ever and, as we find in this report, will increase as the population in drawdown grows and ages. Understanding what more can be done to encourage consumers to seek advice or guidance is crucial to helping retirees secure a decent, lifelong income.

Alistair Wilson

Head of Retail Platform Strategy,
Zurich UK

[1] FCA Retirement Outcomes Review: Interim Report

Methodology

The study is based on a YouGov survey of a UK sample of 742 people who have moved into drawdown since the pension freedoms were introduced in April 2015. The survey was carried out between 14 December 2017 and 24 January 2018.

Section 1: Who's in drawdown?

Key figures: Drawdown in numbers

Men vs Women in drawdown

71% vs 29%

Age of most consumers in drawdown

age 61

Average drawdown pot size

Mean average: **£192,000**

Men: **£211,000**

Women: **£132,000**

Receiving advice: **£234,000**

Occasional advice: **£171,000**

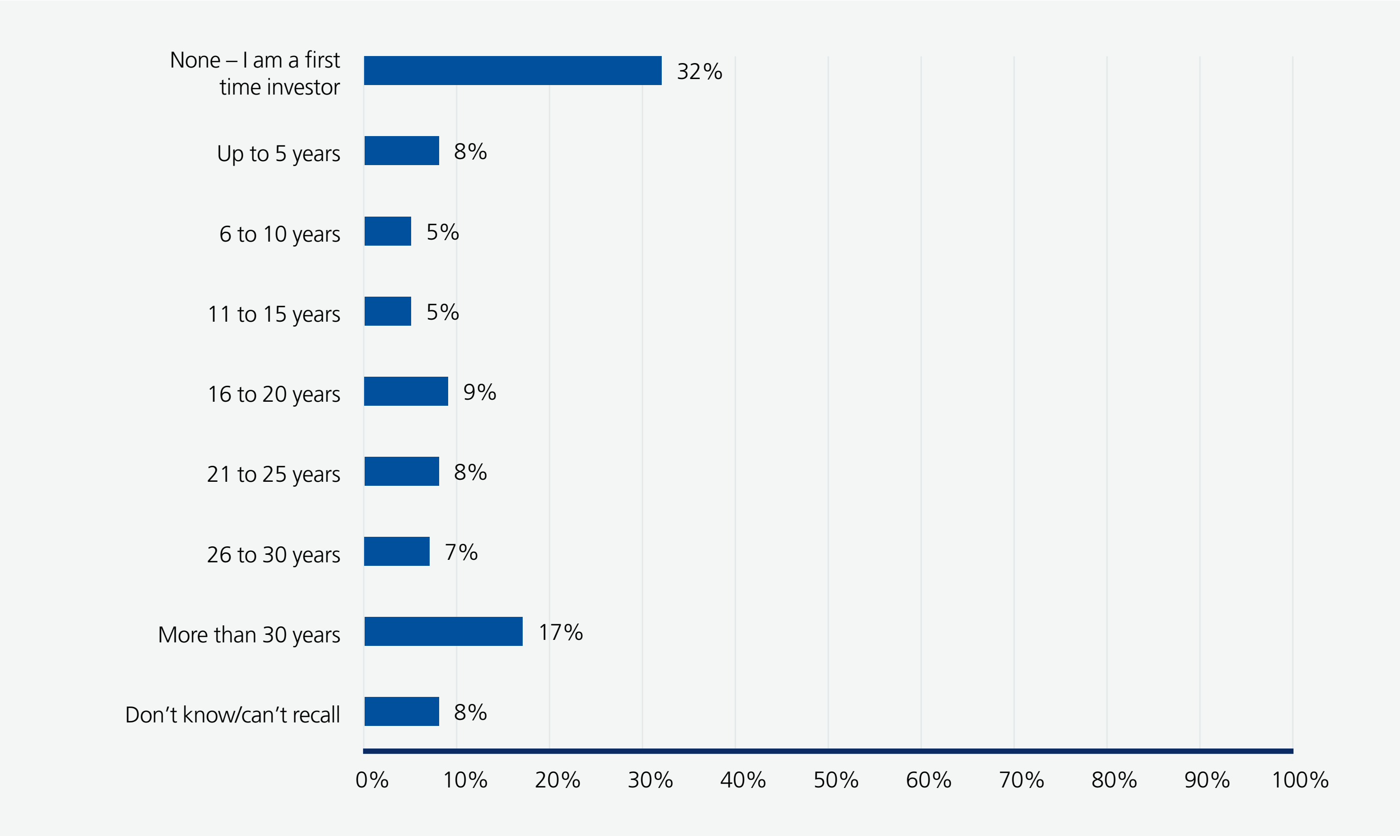
Received advice before putting pot into drawdown, but no longer seeking advice: **£152,000**

Not sought any advice: **£157,000**

Percentage relying on drawdown as main retirement income

33%

How much investment experience do consumers in drawdown have?



Drawdown can be complex, especially for consumers who are managing investments for the first time.

We found that a third (32%) of people surveyed – making up the highest proportion of those who have moved into drawdown – don't have any investment experience.

Women were more likely than men to be first-time investors (29% vs 41%) while men were almost three times more likely to have been investing for over 30 years (21% vs 8%).

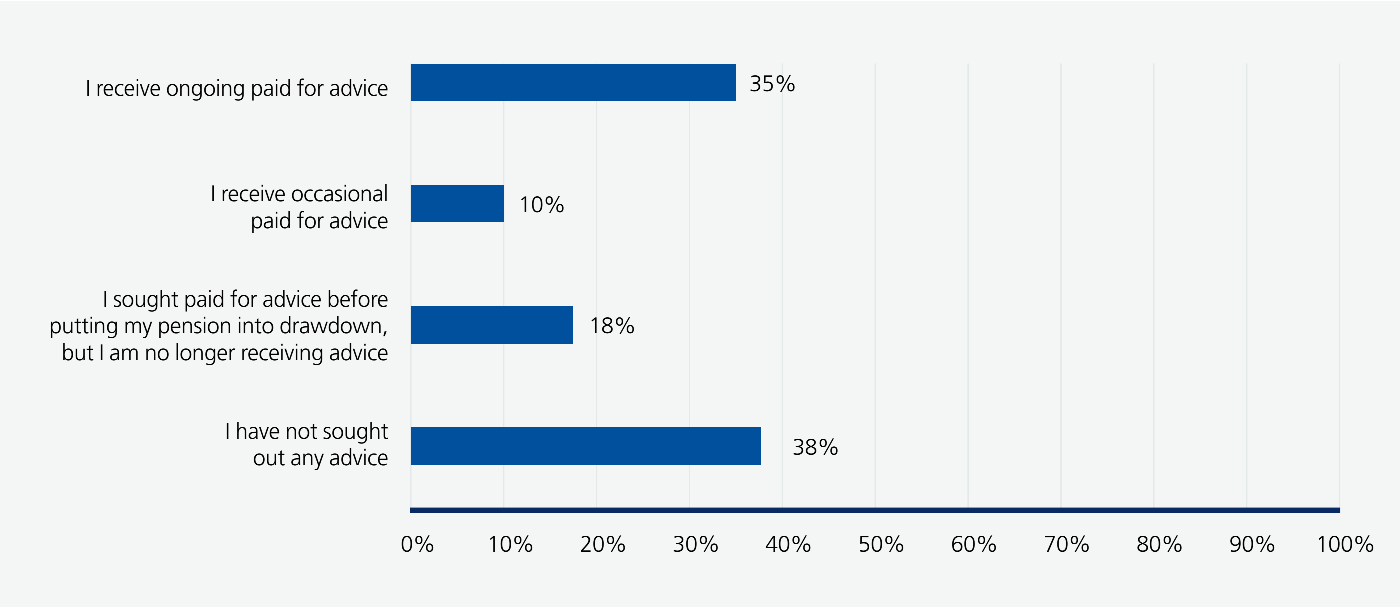
Take-up of advice among first-time investors was roughly split. Some 46% are getting either ongoing or occasional advice while 54% are not receiving any advice at all.

More worrying, however, was the finding that two in five (41%) first-time investors who aren't getting advice haven't sought guidance either. Given the potential complexity of drawdown, these consumers could be at higher risk of poor outcomes.

The trend could be explained by the fact that some consumers had other sources of income or small pots. Yet for two in five (37%) first-time investors, drawdown was their main source of retirement savings. A quarter (25%) also had drawdown savings of £201-£300k and 16% had more than £500k.

Section 2: Trends in advice and guidance

Are people getting advice in drawdown?



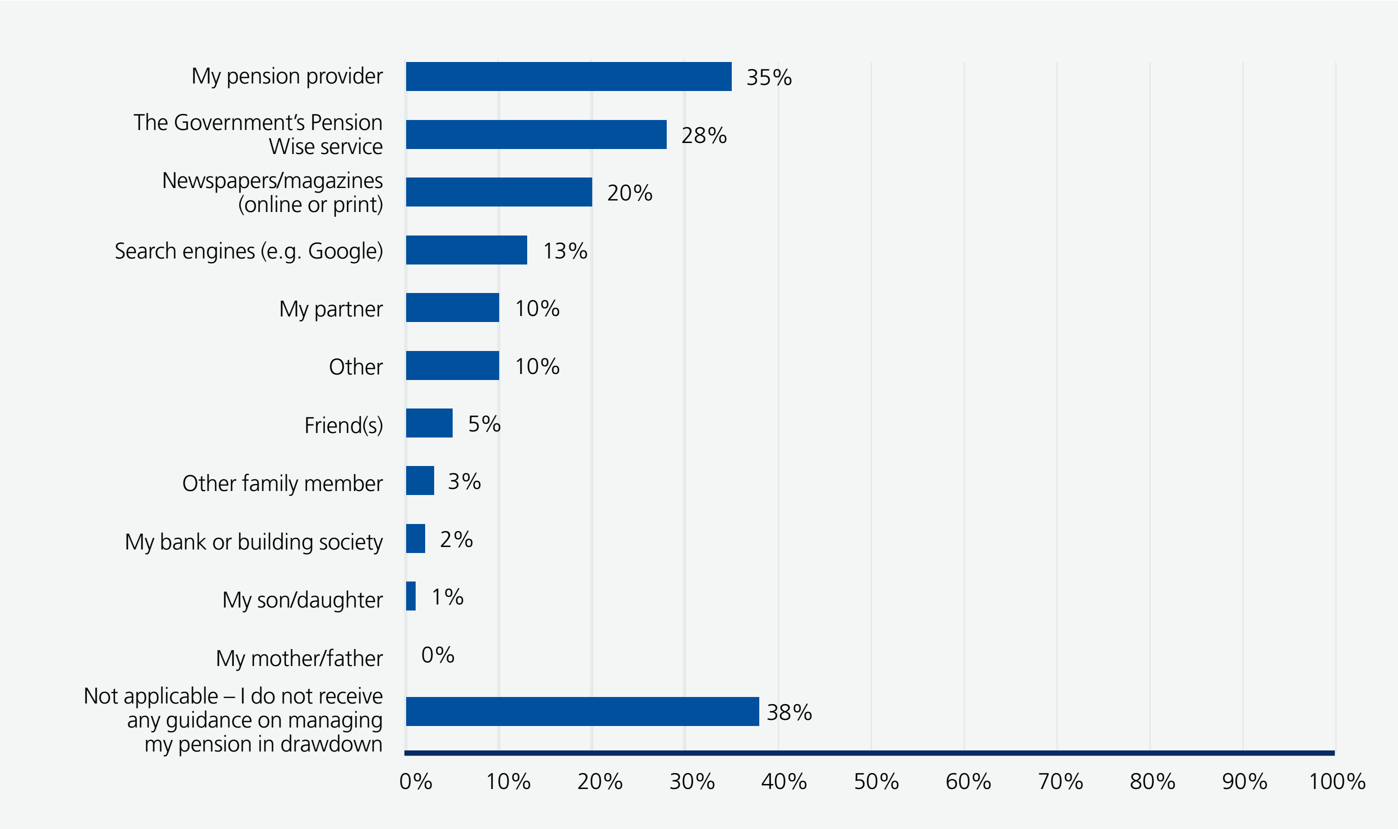
Given the potential risks and complexity of drawdown, financial advice or guidance can help consumers make more informed decisions.

Just under half (45%) of people are getting ongoing advice or occasional advice on managing drawdown – a healthy number in the main. However, this still leaves more than half (55%) who aren't currently speaking to an adviser.

Small pots that don't warrant advice are likely to account for some of these but we also found that a third of non-advised consumers (30%) had assets of £201-£300k and nearly a quarter (22%) more than £500k.

Adviser Focus
Almost 28% of people say they are seeking occasional advice or sought advice before putting their pension into drawdown. Are we seeing the emergence of a new segment of consumers who are looking to dip in and out of advice? How are advice firms set up to respond to this? And do advisers have the fee structure, or even appetite, to cater for the expansion of this market?

If people aren't paying for advice, where are they getting guidance?



Pension firms were the leading source of guidance for a third (35%) of consumers not receiving ongoing advice. However, grey areas over what constitutes guidance and advice could be restricting providers from providing greater support.

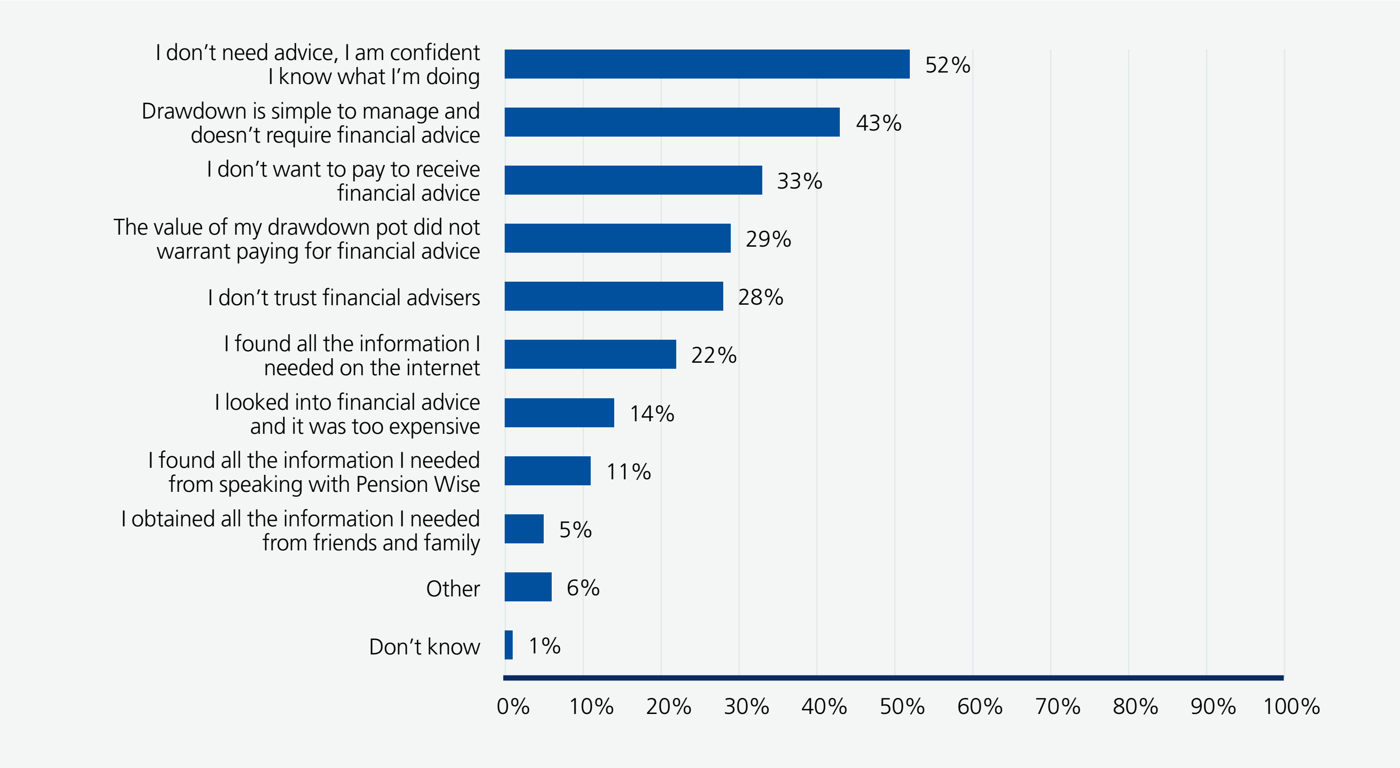
More than a quarter (28%) of people said they were relying on Pension Wise – which was the second most popular source of guidance for non-advised consumers. This is encouraging but suggests more could be done to boost take-up of the service.

Non-advised consumers with more than 30 years of investment experience were more likely to turn to newspapers and magazines than Pension Wise (26% vs 17%), while it was the reverse for first-time investors (13% vs 30%).

There were also clear differences in the guidance being sought by men and women. Men were twice as likely as women (24% vs 12%) to look at newspapers and magazines while women were five times more likely than men to rely on their partner (22% vs 4%) – potentially leaving them more vulnerable should their partner pass away or lose mental capacity.

Of greatest concern was the finding that almost two in five (38%) non-advised consumers are not receiving guidance either – raising the prospect that they are navigating drawdown completely alone.

Why aren't people seeking advice in drawdown?



Two in five (43%) people who had not received guidance or advice said it was because drawdown is simple, rising to almost one in every two (47%) among first-time investors. This may suggest that some consumers are underestimating the complexity of drawdown.

A third (33%) of consumers also identified cost as a barrier, saying they didn't want to pay for advice, while 14% sought advice but considered it unaffordable. Again, it could be that some drawdown pots were too small to warrant advice but only a third (29%) of people agreed this was the case.

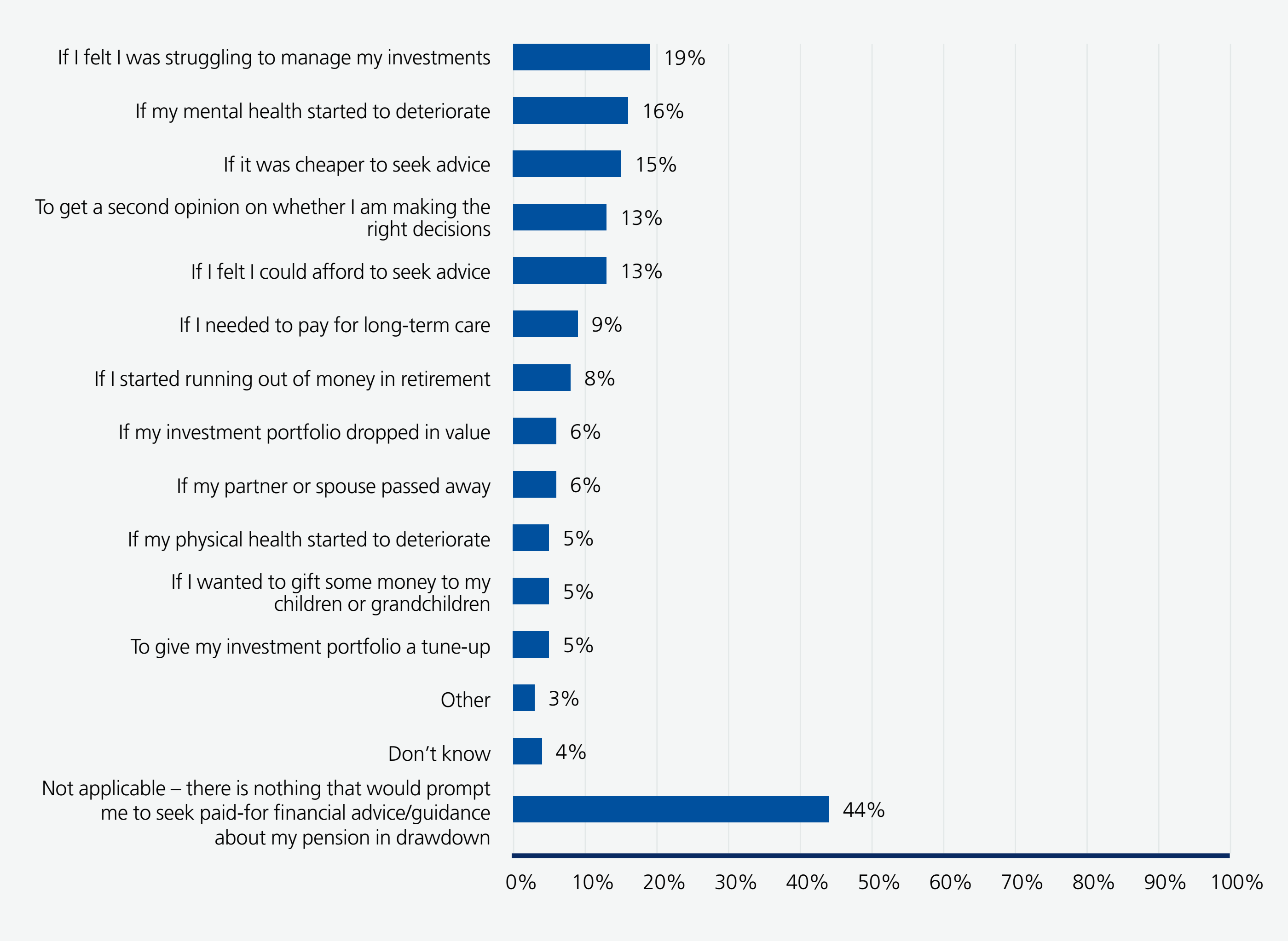
And with a quarter (28%) of consumers saying a lack of trust stopped them speaking to an adviser, the industry still has work to do in communicating the value of advice and building trust in the profession.

Adviser Focus

When it comes to getting advice in drawdown, there appear to be significant differences between the men and women. Men were more likely than women to say they don't want to pay for advice on drawdown (36% vs 25%) and were also more likely to say drawdown is simple and doesn't require advice (46% vs 35%), pointing to potential overconfidence among men.

Women were less likely than men to say they did not want to pay for financial advice (25% vs 36%) and were less confident than men of managing drawdown without it (33% vs 60%) – but still fewer women take advice. Women are clearly open to advice on drawdown – but are not engaging with it in the way it's currently being offered. Does the industry need to find a better way of communicating the value of advice?

When would consumers in drawdown pay for advice?



For almost half (44%) of non-advised consumers, there appear to be no triggers that would encourage them to seek advice in drawdown, even if their personal or financial circumstances changed dramatically.

However, two in five (19%) would get advice if they were struggling to manage their investments and 16% if their mental health was failing – pointing to a potential increase in demand for advice in later life.

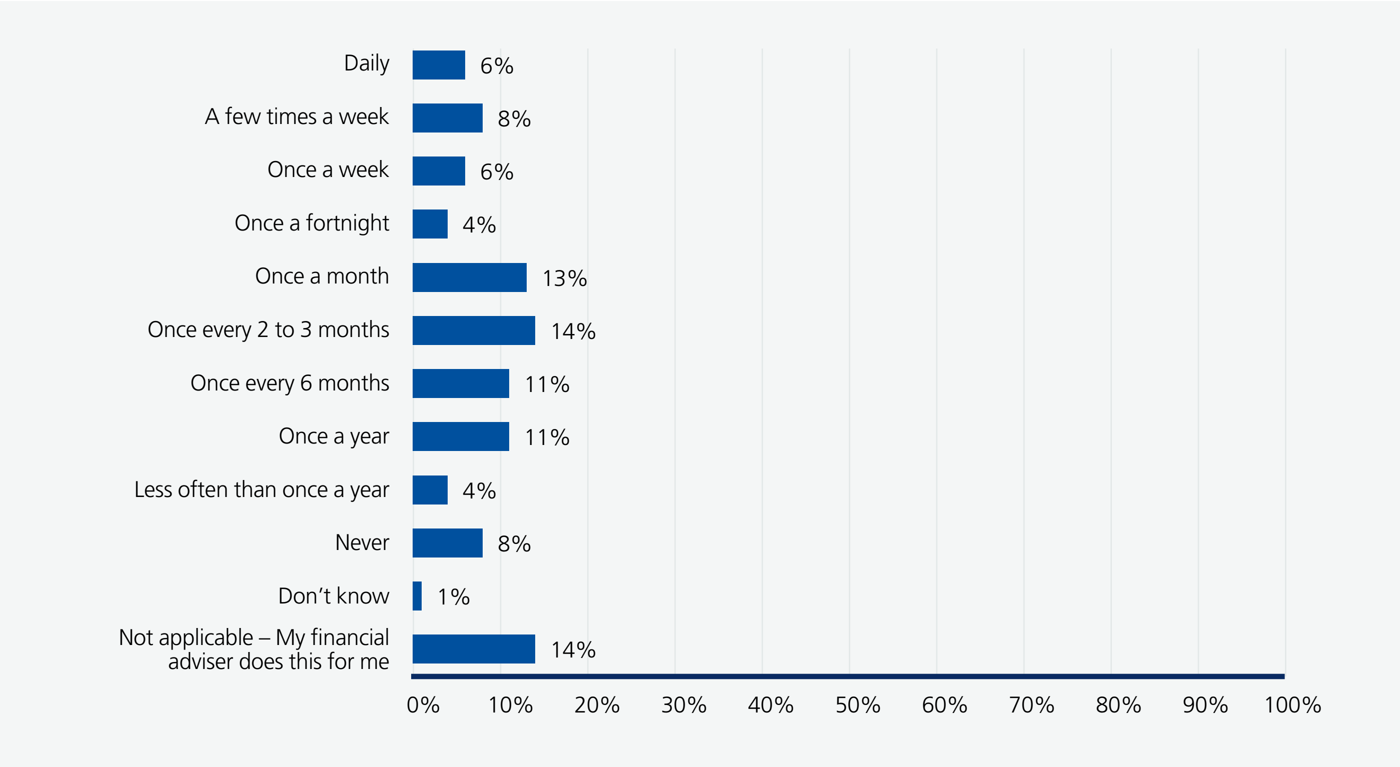
Twice as many women (24%) as men (12%) would seek advice if it was cheaper.

Adviser Focus

In the top two responses, consumers appear to acknowledge that managing drawdown in old age might become a challenge. As the number of people in drawdown rises, are we likely to see new specialist advice firms emerging that focus exclusively on retirement income? Consumers also said they would speak to an adviser for a second opinion. Is there an opportunity for advisers to launch investment clinics or drawdown MOTs offering one-off advice to help consumers check they are on track? How does regulation need to change to help the industry provide new advice solutions for the changing retirement landscape?

Section 3: Consumer engagement in drawdown

How often do consumers check the performance of their investments?



Consumers in drawdown need to actively manage their portfolio and keep a regular track of how it's performing.

More than a third (37%) of consumers surveyed are checking their investments at least once a month – a healthy level of engagement.

However, one in 10 (11%) only check it once a year and a similar number (8%) never check it at all – leaving it completely to chance.

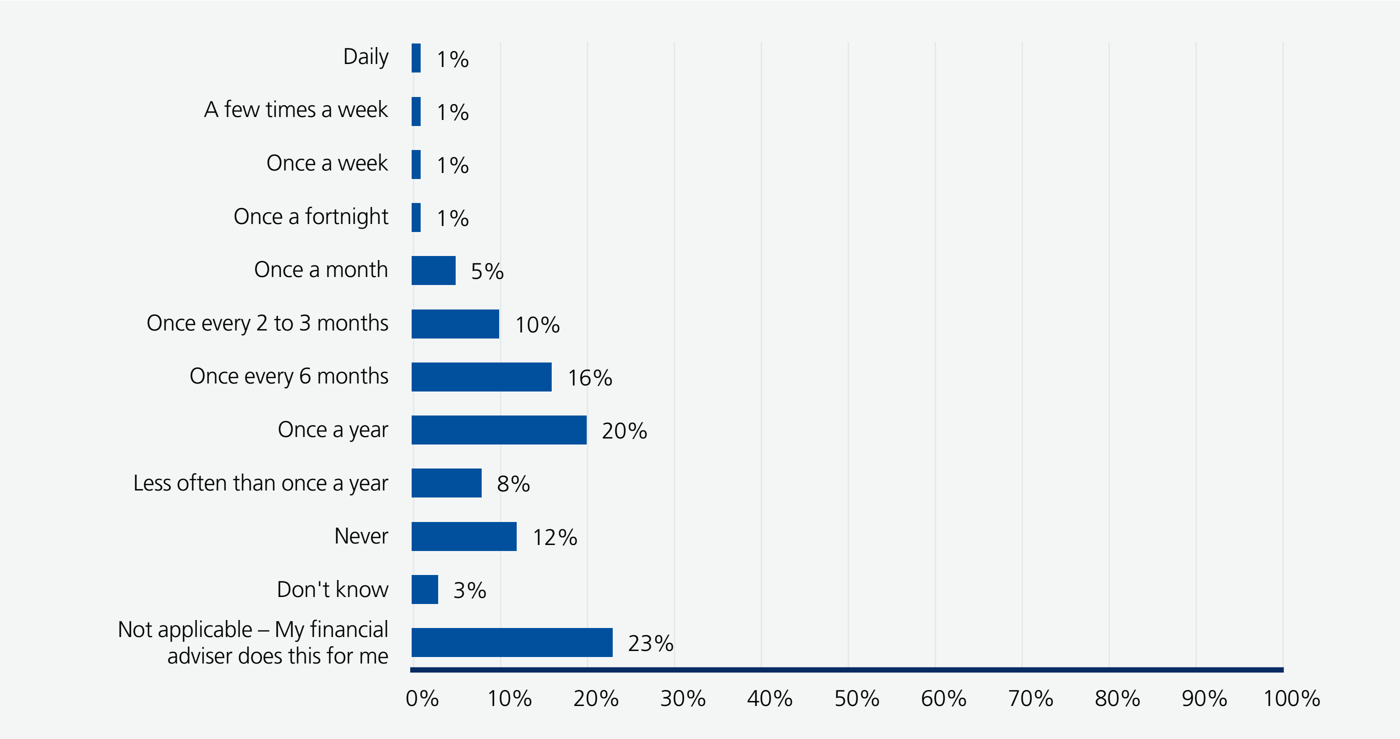
Women are less inclined to look at their investments across nearly all intervals, and twice as likely as men (13% v 6%) to never check them at all.

Just under a third (31%) of non-advised consumers never check their investments or check them once a year or less often.

Adviser Focus

Consumers are logging on to check the performance of their investments with an unexpected frequency – highlighting the value to them of being able to view their portfolio online. Advisers shouldn't assume that older clients aren't interested in accessing information in this way. Consumers may not be checking their investments as often as their bank accounts but nonetheless it must be made easy for consumers to do this online.

How often do consumers review and adjust their investments?



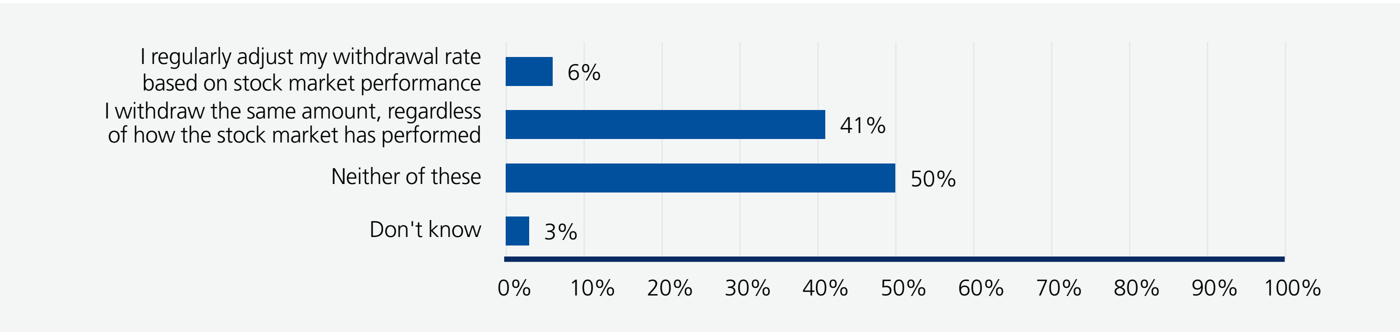
Reassuringly, most consumers have grasped the ongoing need to fine-tune their portfolio, with half (55%) reviewing and adjusting their investments at least once a year.

Again there are differences in engagement levels among men and women. Almost one in five (17%) women never review and adjust their investments, compared to one in 10 men (10%).

Almost one in 10 (9%) consumers are potentially over-trading by reviewing and adjusting their investments at least once a month.

Adviser Focus
Among consumers receiving ongoing advice, just 2% never review and adjust their investments, compared to 20% of those who have not sought advice – highlighting the clear role advice can play in improving potential outcomes for consumers.

Are consumers adjusting their withdrawal rate in drawdown?



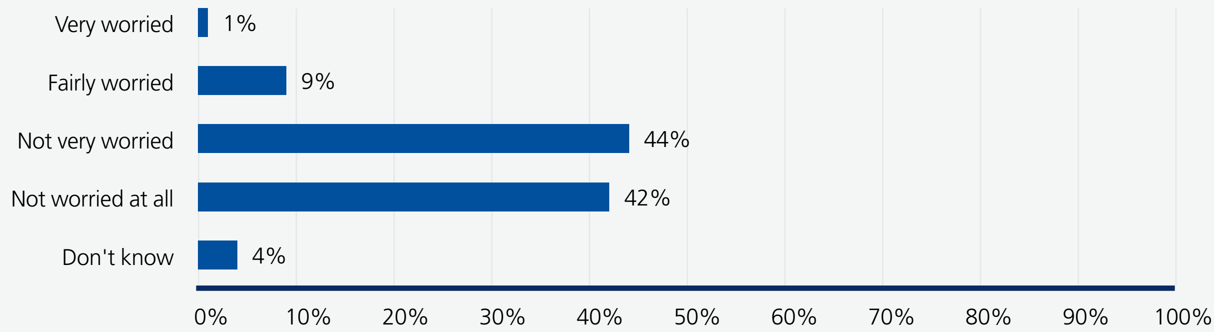
Consumers need to take a flexible approach to withdrawing income from their pension. Withdrawing money when markets are falling can erode a pot quicker than taking the same amount in a rising market, especially in the early years of retirement.

However, two in five (41%) consumers are withdrawing the same amount from their pension, regardless of how the market has performed.

While further investigation is needed, this may be an early warning sign that some consumers are adopting an unsustainable withdrawal rate, which could reduce their chances of achieving a lifelong income.

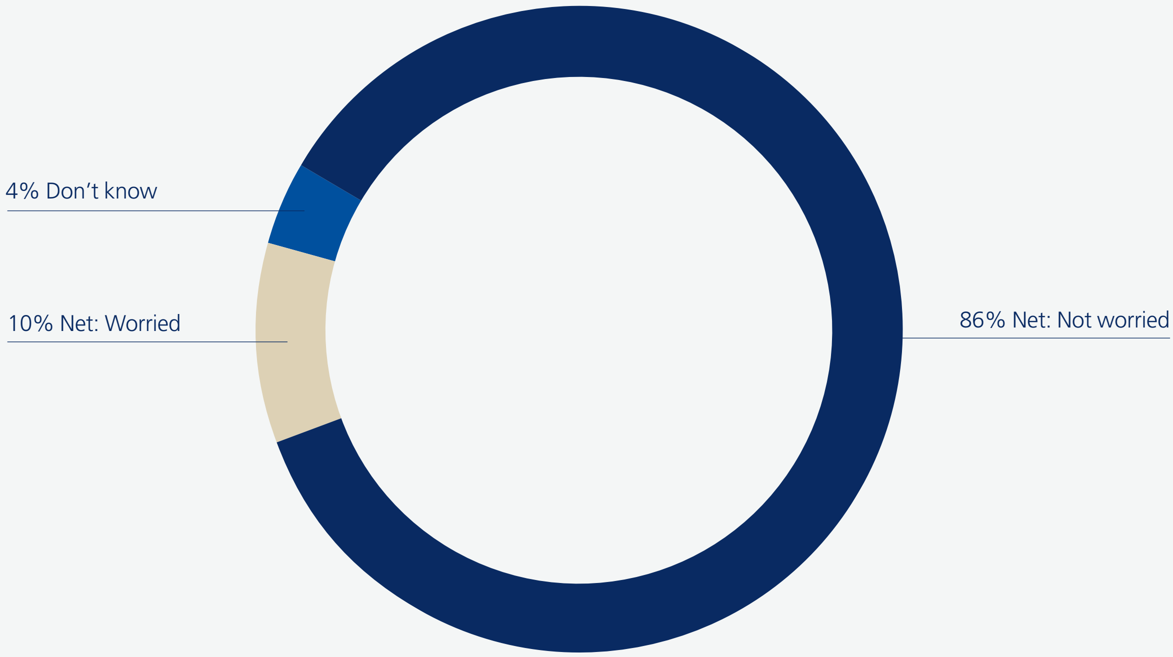
Section 4: Growing old in drawdown

Are people worried about growing old in drawdown?

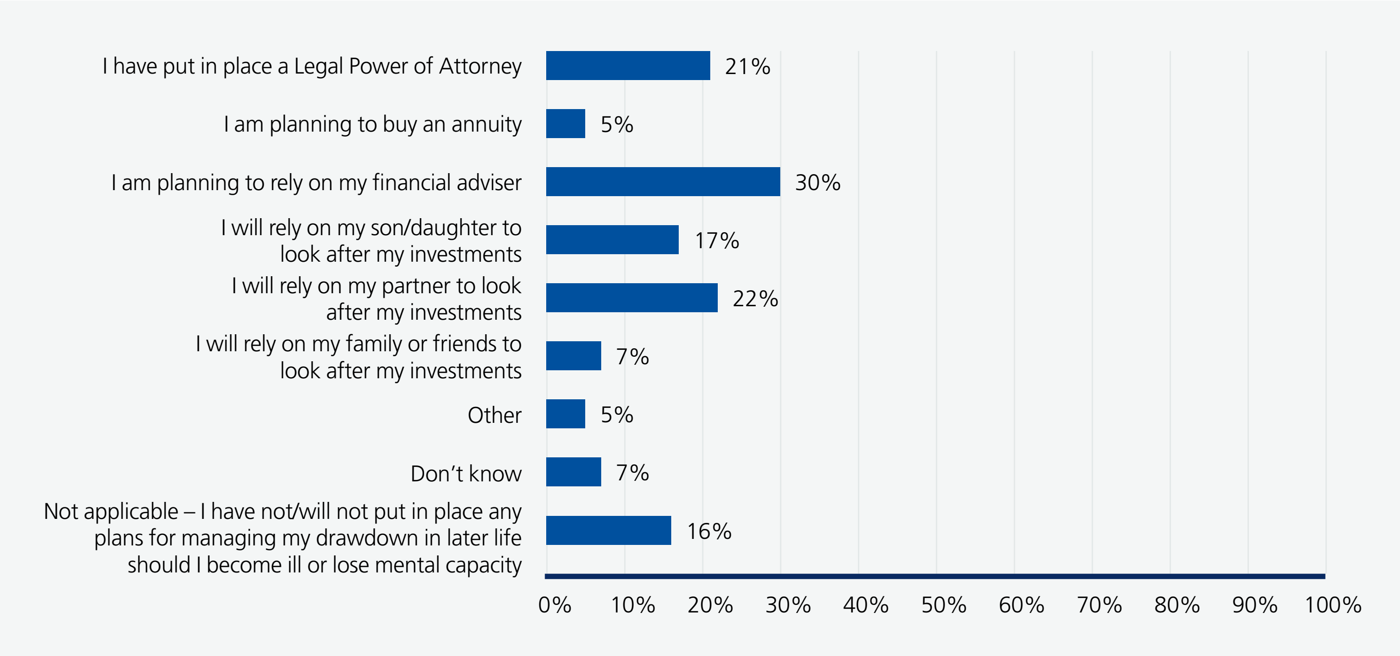


Keeping on top of a drawdown portfolio requires investors to make ongoing decisions over withdrawal rates and risk. As people grow older, they may suffer from periods of ill-health or declining mental capacity, which could make managing drawdown more challenging.

Consumers don't appear concerned by this prospect, with nearly nine in 10 (86%) saying they are not worried about how they will cope with drawdown in old age. While this is a positive finding on the whole, it's also important that consumers plan for a time when managing drawdown might be too much.



Are consumers prepared for a time when managing drawdown might be too much?



One way for consumers to manage the financial risks of ageing is to take out a Lasting Power of Attorney (LPA). This allows someone else to run their finances if they no longer can.

Just one in five (21%) people in drawdown have so far taken out an LPA – meaning that for the majority, their pension savings could be left in limbo if they were unable to look after them. Unsurprisingly, advised consumers were most likely to have an LPA in place.

About a third (30%) of consumers expect their financial adviser to manage their investments if they aren't fit to. However, many advisers don't hold discretionary investment powers, and even if they do, they may not be able to take the same action as someone with a power of attorney.

Almost one in five (17%) will rely on their children to look after their drawdown investments. This hints at the wider social changes likely to be initiated by the shift from annuities to drawdown, with younger generations taking on greater responsibility for the financial security of the elderly.

Meanwhile, almost a quarter (22%) will rely on their partner to take over their drawdown if they are no longer able to manage it. However, this assumes that their partner will still be around or able to support them. Earlier findings also showed that women are more likely to rely on their partner for guidance on managing drawdown, which may create financial challenges for them if their partner is no longer capable of assisting them.

Interestingly, consumers don't see buying an annuity in later life as the solution to managing drawdown in old age, with just 5% backing this option, despite the fact rates improve with age and declining health.

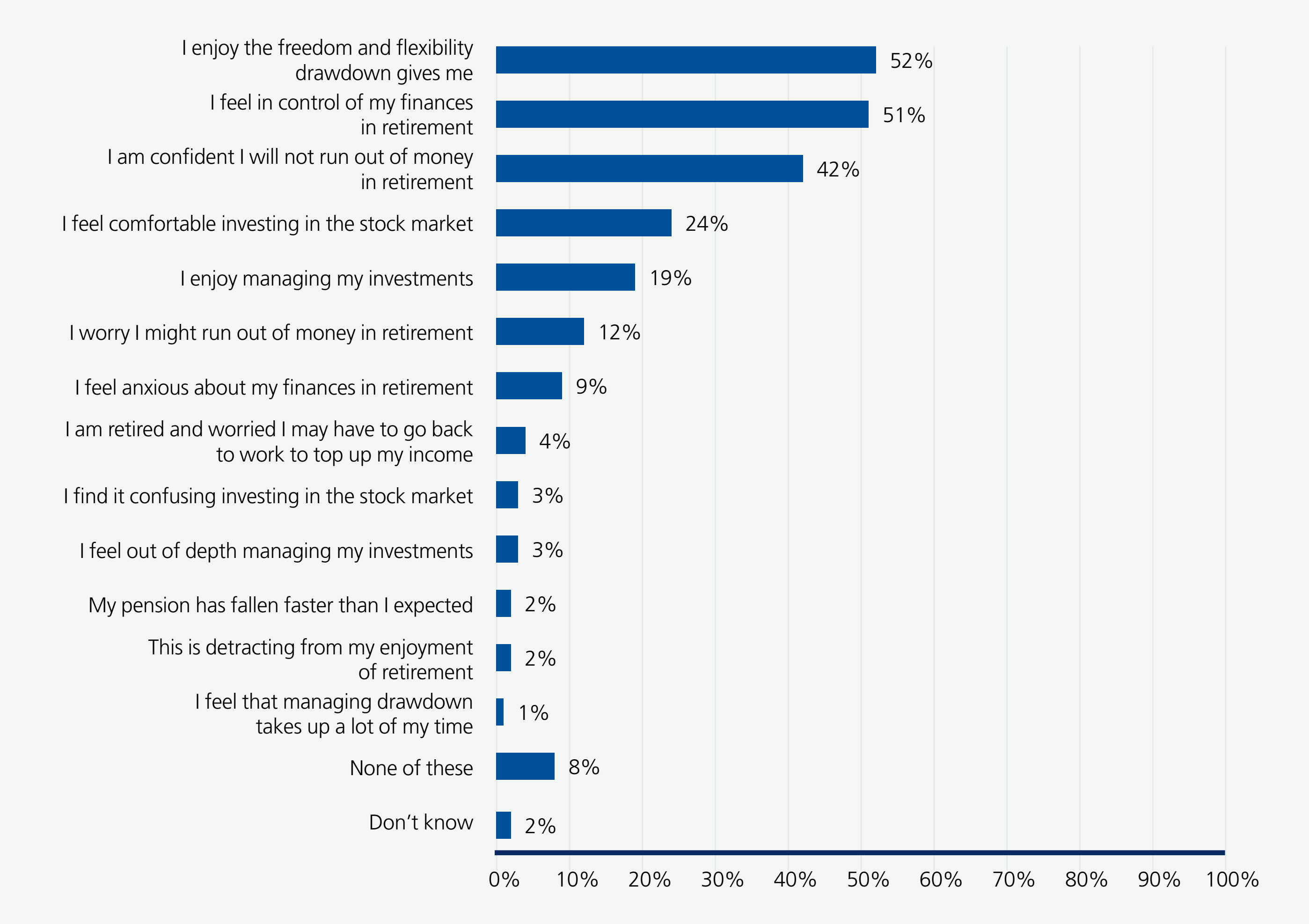
Almost one in five (16%) said they haven't or won't put any plans in place at all. This could again be attributable to small pots, although 14% of those who had savings of £201-£300k said this.

Adviser Focus

From paying bills to checking bank statements, younger generations already play a vital role in helping elderly parents with day-to-day money matters. As drawdown becomes the norm, this may also extend to supporting parents with their retirement income. This could be challenging for some carers, especially if they have no investment experience themselves. How many will turn to financial advisers? And will those who already have an adviser pass them on to their parents – overcoming almost at a stroke the older generation's mistrust of advisers? 'If they are good enough for my son/daughter, they are good enough for me… ' Either way, with drawdown numbers on the rise, the market for supporting older consumers in drawdown is ripe for growth. But are advisers and their businesses set up to cope with the diverse needs of older consumers? And will we see a greater regulatory focus on vulnerable customers?

Section 5: Drawdown: The consumer verdict

Do consumers like drawdown?

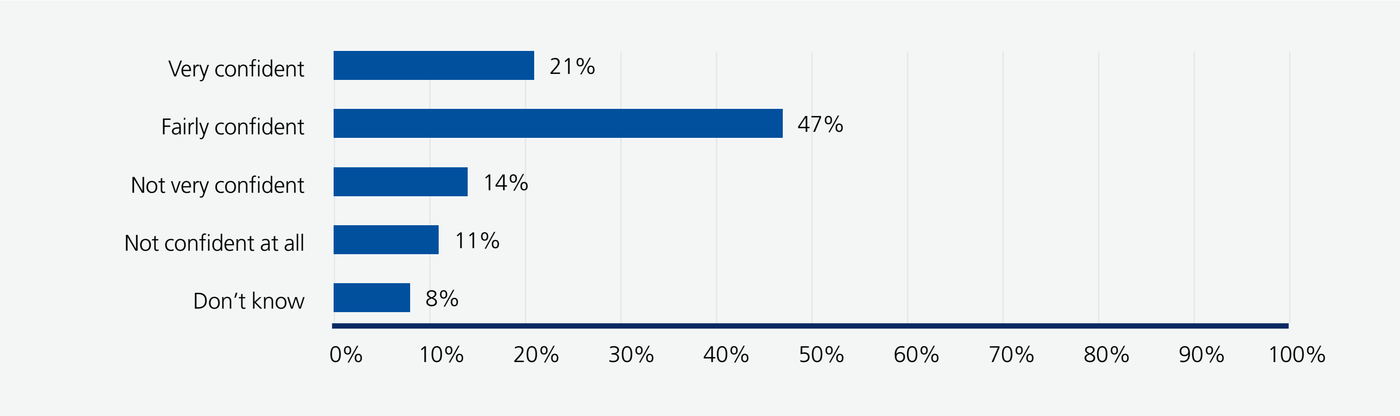


More than half of consumers say they enjoy the freedom and flexibility of drawdown (52%) and feel in control of their finances (51%), two of the fundamental aims of the Government's pension reforms.

Very few feel out of their depth managing investments (3%), confused by investing in the stock market (3%), anxious about their finances (9%) or that drawdown is detracting from their enjoyment of retirement (2%).

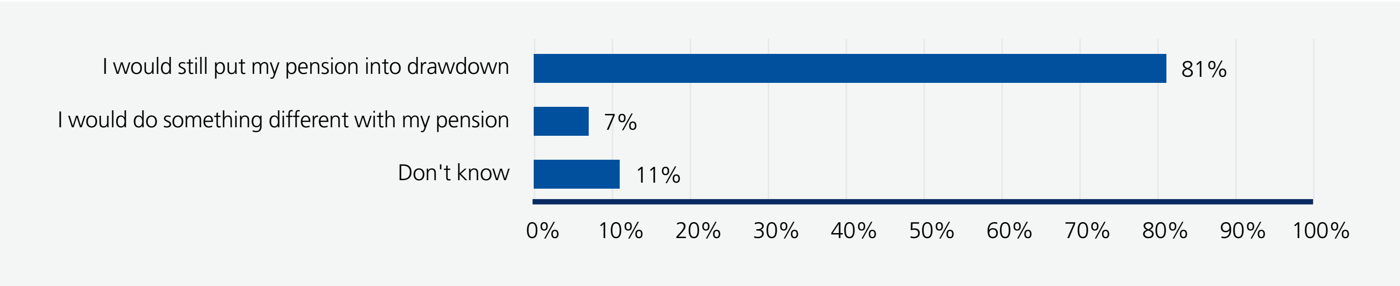
However, half the number of women as men say they feel comfortable investing in the stock market (13% vs 29%) and women are almost three times less likely to say they enjoy managing their investments (9% vs 24%).

Are consumers confident of not running out of money in drawdown?



Almost seven in 10 (67%) people are confident that their pension in drawdown will last for the whole of their retirement. While this is another positive indication of the confidence people have in drawdown, the figure is high given only a third of consumers said drawdown was their main retirement pot. Women were less confident than men (60% vs 70%) while consumers seeking ongoing advice were more confident than those who have not sought out any advice (77% vs 60%).

Would consumers choose drawdown again?



Given a second chance, eight out of 10 people (81%) would still put their pension into drawdown – a powerful indicator that consumers like drawdown. One in 10 (11%) are undecided, with women twice as likely as men to be unsure (19% vs 8%).

Consumers who have not sought any advice are twice as likely to express uncertainty over their decision, compared to those who are getting ongoing advice (16% vs 8%). Just 7% of people would do something different with their pension.

Adviser Focus

Consumers speaking to an adviser were more confident of their decision to move into drawdown than those who are not. It's fair to say that flexi-access drawdown has had a soft landing – having been introduced during a time of generally rising markets, and when the majority of consumers have other sources of savings to rely on. In times of prolonged depressed markets, and as those with defined-benefit pots decline, could the gap in satisfaction between advised and non-advised consumers grow?

Conclusions

Drawdown has transformed the retirement landscape yet little was known about its impact on consumers personal and financial well-being.

In the largest study of its kind to date, we find that drawdown is popular among the vast majority of consumers. Eight in 10 people (81%), for example, would choose to put their pension into drawdown if they were making the decision again and just 2% say that drawdown is detracting from their enjoyment of retirement.

The transfer of investment and longevity risk from annuity providers to consumers also appears to have had little impact on their personal or financial well-being. Just one in 10 report feeling anxious (9%) about their finances in drawdown or worry that they might run out of money (12%).

Furthermore, healthy numbers of consumers are seeking advice on drawdown, with just under half (45%) getting ongoing or occasional advice while consumers also appear engaged in managing drawdown, with a third (37%) checking their portfolio at least once a month.

But some gaps are emerging…

While drawdown overall appears to have been a success, our findings also reveal that four potential gaps are emerging where further advice, guidance and information could help consumers.

The ‘first-time investor’ gap

We found a clear gap in the take-up of advice and guidance among first-time investors. A third of consumers (32%) – making up the highest proportion of those in drawdown – have never actively invested in the stock market. Despite this, two in five (41%) have not received guidance, and are either not currently receiving advice or have never received advice.

Poor decisions in drawdown can mean consumers take on too much risk, miss out on investment growth or make unsustainably high withdrawals. These hazards are likely to be amplified for consumers with no investment experience and who have not sought advice or guidance to help them make more informed decisions.

One of the drivers behind this appears to be a lack of consumer understanding about drawdown. Almost half of first-time investors who had not received advice thought drawdown is simple (47%) and doesn’t require advice while a third said they were confident in what they are doing (29%) – despite having no investment experience. This could indicate some consumers are underestimating the complexity of drawdown or overestimating their ability to manage it.

Either way, it may strengthen the case for introducing additional protections to ensure consumers moving into drawdown seek some form of advice, guidance or information.

Recommendations

- The Government should reconsider the case for introducing mandatory guidance for drawdown, requiring non-advised consumers to either opt in or out of receiving guidance before accessing their pension
- FCA should investigate the potential for providers to offer a small set of clearly defined / named drawdown lifestyle (or target dated fund) solutions that consumers could pick based on their individual circumstances. These could take account of the age of consumers and one or more could be aligned to the purchase of an annuity at a pre-determined age

The ‘gender drawdown’ gap

We found evidence that a greater number of women than men could be at risk of poorer outcomes in drawdown, potentially highlighting a new gender gap in retirement.

Women were more likely than men to have no investment experience (41% vs 29%). They were more likely to say they never review and adjust their drawdown investments (17% vs 10%) and twice (13% vs 6%) as likely as men to never check the performance of their pension portfolio in drawdown.

Women not getting advice were five times more likely to rely on their partner for guidance on managing drawdown (22% vs 4%) – leaving them more vulnerable should their partner pass away or lose mental capacity. Women were less likely than men to contact Pension Wise for guidance (25% vs 30%). Women also reported lower levels of confidence in handling drawdown without advice (33% vs 60%) – yet fewer are speaking to an adviser (36% vs 32%).

However, men were more likely than women to say they don’t want to pay for advice on drawdown (36% vs 25%) and were also more likely to say drawdown is simple and doesn’t require advice (46% vs 35%), highlighting the risk of potential overconfidence.

Before the pension freedoms, men and women who bought an annuity received a guaranteed income for life which meant they faced relatively equal risks. But drawdown has led to new complexities that require consumers to manage their own investment and withdrawal strategies, as well as longevity risk.

Overall, our findings suggest these risks could have a bearing on a greater number of women, who reported lower levels of investment experience and financial engagement. It could mean that women, who already face barriers in accumulation, including a gender pay gap, time taken out of the workplace to raise children and lower paid part-time working, may now face new challenges in decumulation too.

These challenges are likely to be magnified by the fact that women on average live longer than men, have smaller pots (£132,000 vs £212,000) and are more likely to rely on drawdown as their primary source of retirement income (35% vs 33%).

Advice and guidance is at the core of addressing the risks both men and women face in drawdown. However, we found cost was a clear barrier preventing women from accessing advice. Twice as many women (24%) as men (12%) who haven’t received advice said they would do so if it was cheaper. And double the number said they would get advice on drawdown if they felt they could afford it (21% vs 10%).

Women appear to recognise the need for advice but either cannot afford it or don’t consider it value for money at the price the market is giving them. Addressing this requires raising awareness of the importance of guidance and advice, and the value of both in improving financial outcomes in retirement.

Recommendations

- Conduct an FCA or Government select committee inquiry into the impact of gender on retirement outcomes in the new pension landscape and how more women can be encouraged to take up retirement advice and guidance
- Take forward the interventions identified in the CII’s *Securing the financial future of the next generation: The moments that matter in the lives of young British women today*

The ‘sustainability’ gap

Although it’s still early days, there was some initial evidence that consumers could be making poor choices over their withdrawal strategy. Two in five (41%) of those in drawdown are withdrawing the same amount regardless of how the stock market has performed.

Without a full picture of people’s personal circumstances, it’s difficult to draw any firm conclusions. Many consumers are also taking ad hoc withdrawals, making tracking of sustainability more difficult. However, consumers withdrawing more than the investment return of their portfolio, or when it has dropped in value, will deplete their savings quicker than expected. It’s crucial that consumers understand the importance of carefully controlling their withdrawals and remaining flexible about their income.

This issue highlights how new forms of advice and guidance could benefit consumers in the changing retirement landscape. We found a significant number of consumers are seeking occasional, rather than ongoing advice, hinting at demand for dipping in and out of advice. For consumers who don’t want full advice, drawdown MOTs or investment clinics offering one-off financial advice or guidance could help consumers check they are on track in drawdown.

Recommendation

- Ahead of publishing its final Retirement Outcomes Review, the FCA should take a temperature check on the levels of consumer withdrawal rates in drawdown
- Estimating a safe withdrawal rate is key to helping individuals manage their retirement savings. With more people expected to select pension drawdown over the purchase of an annuity, the Government should introduce a UK-relevant safe withdrawal rate to help consumers manage their retirement savings. The Government Actuary Department already publishes GAD rates for capped drawdown, which should be made relevant for consumers in flexi-access drawdown and published on the new Single Financial Guidance Body’s website
- Explore the potential for the new Single Financial Guidance Body to offer non-advised consumers a drawdown MOT at age 74, ahead of 75, when the taxation of pension death benefits changes. This would help consumers to reassess whether drawdown remains the right choice for them
- Pension providers should issue periodic communications to customers reminding them to review the level of withdrawal relative to portfolio returns and the importance of keeping their drawdown portfolio under review

The ‘later-life security’ gap

Finally, our findings suggest there is more consumers could do to prepare for managing drawdown in later life.

Before the pension freedoms, the vast majority of people bought an annuity. While these were restrictive and for many poor value, they guaranteed a lifelong income and avoided challenges arising from ill-health or declining mental capacity. By contrast, consumers in drawdown need to actively manage their investments into old age.

Our research shows nine in 10 (86%) people are not worried about how they will cope with drawdown in later life. While this is positive in the main, consumers should plan ahead for a time when looking after their investments might become more difficult, or even impossible.

However, we found few consumers are taking steps to protect their financial security in old age. Just one in five (21%) in drawdown have a Lasting Power of Attorney in place, which ensures someone they trust can step in to manage their finances if they no longer can. Given that a pension is likely to be one the largest assets they own, it’s vital that more consumers take out an LPA to ensure their loved ones can make decisions on their finances, should they fall ill or lose mental capacity.

As more consumers age in drawdown, the demand for advice is likely to grow. Our findings suggest this demand will come not only from new and existing drawdown clients but from their families too. Perhaps unsurprisingly we found that when people can no longer manage in drawdown they will call on their children for support. While paying bills and checking bank statements for elderly relatives is already the norm for younger generations, many may choose to seek advice when it comes to managing tens of thousands of pounds invested in the stock market.

All of this points to the enhanced role the advice industry could be set to play in safeguarding the financial security and well-being of the UK’s ageing population. This will bring with it new challenges and opportunities for the industry. Could we see the rise of specialist advice firms focusing exclusively on financial planning solutions for people in later life? How are advice firms set up to deal with a growing number of older clients, not least when it comes to supporting vulnerable customers? And are sufficient numbers of younger advisers entering the profession to cope with the potential surge in demand? How the industry responds to an ageing population in drawdown has the power to change both retirement outcomes for consumers and the future shape of advice.

Recommendations

- Expand the number of adviser apprenticeship schemes and increase the uptake of firms supporting them, to help introduce new advisers to the market
- The Government, financial services industry and other relevant stakeholders should work together to raise awareness of the importance of LPAs for consumers in drawdown, and help demystify them for consumers

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