Institute and Faculty of Actuaries

ICAT (IFoA Covid-19 Action Taskforce)

Covid-19 and pension saving: A perspective of product providers

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February 2021

A consequence of the pandemic and the resulting furloughs and/or lay-offs is not just the loss of immediate income. The pension contributions that would be levied on the salaries are also foregone. It is natural to have focused on how to help employees who have lost some or all of their immediate income and the difficulties of meeting day to day needs. However, the loss of future income cannot be ignored. Various pieces of research report on the impact and responses of employers to the funding of pension benefits. The impact on defined benefit funds of missing contributions leads to funding issues and impacts the broad security of members' benefits. Missing contributions in defined contribution plans causes similar funding issues at the individual's level.

Meanwhile, there has been some concern over the behaviour of members of defined contribution schemes at the end of March 2020 when Western investment markets tumbled as the implications of business lock downs created negative investor sentiment. The adage of "it's not market timing, it's time in the market" was reinforced by the results of those who may have been motivated by flight to cash and then missed out on the rebound during the summer and then with announcements of a vaccine.

In a discussion with representatives of leading defined contribution providers, members of the Institute's ICAT DC work stream[1] learned of the behaviours of employees in response to COVID-19 during 2020. We[2] heard about the activities of the providers and the actions necessary to help pensioners become more financially secure in old age. The format of the discussion was a virtual round table where selected questions were posed and the representatives spoke to their firms' experience followed by some general discussion. The providers were able to quote from various research reports they had compiled recently as evidence of the behaviours of their client base. The following is a semi-verbatim report on the discussion. The points made here paraphrase the points each of them made[3].

Callum: What behaviours have you seen in terms of members ceasing contributions and accessing their pension pots? And how did members react to the volatility of markets as we went into and through lock down?

Dale: Aviva carried out surveys[4] of members on attitudes to retirement prior to Covid and then again during the summer. The trends in the responses provide interesting perspectives from different locations.

Generally those who might be considered better-off indicated they felt even better-off than they were previously (perhaps due to people having spent less during lock down). For those in areas with more restrictions, furloughs, hospitality restrictions and lay-offs, the general feeling was members were worse off.

Looking forward, levels of confidence for the future have fallen, indicated by increases in predicted or intended age at retirement. Indeed there was a drop in the number of retirements in April versus expectations (of the order 50%). Perhaps this was led by the drop in fund values, but now the trend has reversed. There has been a recent up-swing in the number of retirements, although the amount of fund withdrawals is still low by historical measures and expectations.

It seems that these are informal retirements; people are looking to boost their income. Lots of members are simply accessing their tax free cash via drawdown - there has been a 100% increase in the number accessing tax free cash.

Finally, from the surveys, the plight of younger members is summed up in a greater sense of concern in retirement planning whereas middle age and older members seemed to be in the same mindset, relatively confident in their prevailing plan.

Sharon: Building on Dale's examples of retiree decision making, there were examples within Scottish Widows membership[5] where retirees had actually reduced their drawdowns having gone back to work "for something to do". Meanwhile younger members have been significantly affected by furloughs and lay-offs. There have also been concerns over scams across their membership. Scottish Widows have responded with more frequent and more prominent messages to members to think twice before acting on advice from third parties.

Donna: At Standard Life, contribution levels seem to be holding at pre-Covid levels. We have seen many examples of employers topping up furlough level payments to the full amount of pension contribution. The number of opt-outs within auto-enrolment (AE) still average around 6%. However, there are clear indications of fewer new joiners, presumably on the back of fewer new hires as employers try to hold on to their business plans. That said, there are some employers who are growing: those for whom Covid and lock downs actually present an opportunity. There have been a small number of employers who have struggled to pay contributions at all - while any defaults are regrettable, the numbers here are thankfully not significant.

In terms of investment strategy, there were a small number of members switching to lower risk strategies in March and April. There were more seemingly opportunistic switching following various "vaccine announcements" - again, not a significant number. However, the market volatility and potential increase in pension scams meant that Standard Life increased their "stop & think" messages. We have also seen members accessing pension pots early "to live on" suggesting a need to tap retirement savings for bare necessities. Standard Life continue to offer additional and relevant support for members with vulnerabilities including those facing financial hardship, which is on the increase, to see how they can be assisted further.

Kate: At Aegon, we have increased our member communication. One concern we had during lockdown was the increased risk of pension scams. Scammers have been targeting people working from home through scam websites. People can be more vulnerable when they are working from home, isolated and googling pension opportunities. It is worth remembering that pensions and jobs are inextricably linked. While employers have been able to retain employees due to the furlough scheme, there have been some reductions in contributions to auto-enrolment (AE) levels. The increase in the number of members who have been furloughed shows up in the reduction in contributions - the average contribution rate has fallen. However, contribution rates seem to be recovering. We saw the number of AEs (new joiners) dipping in August, but the AE numbers are up again to levels pre-Covid now. Turnover rates of members is down as it appears members are staying in current positions rather than risk moving job. This is one trend we might be seeing – people might be staying in their jobs longer, and only leaving if made redundant. On the whole, pension saving so far has been holding up. The real impact will be seen once the job retention scheme ends. The various negative impact measures appear to have affected the younger and female members to a greater extent. Aegon's members have not made significant investment decisions such as switches, apparently focusing on other things. However where members have made investment switches, decision-making has been poor, probably out of fear, such as switching to cash after market drops and failing to take advantage of the subsequent upswings. Aegon has looked at financial resilience. In a survey[5] of our members' savings arrangements (including ISAs) 25% of those who said they were worried about the future had stopped saving. However, 33% of those who were confident had actually increased their level of savings. Some 37% were now more likely to establish a "rainy day fund". When asked "what would a sensible cash position look like?" the typical response was up from 3 months' to 6 months' salary. Covid appears to have increased the necessary safety level in terms of being able to get by for longer on a loss of income.

Donna: We are committed to doing the right thing for members which includes mitigating the risk of them being scammed. It is important that members understand that we are doing extra checks to help protect them and not trying to delay payments to them.

James: At Fidelity, there were similar decreases in the level of withdrawals early in 2020. They have started to return to pre-Covid levels but over the whole period the volume of withdrawals will have been lower due to a pause immediately after the onset of the pandemic. Fidelity hasn't seen any significant change in the level of opt-outs. We did observe a significantly higher level of investment switches in March 2020, with many self-selecting members switching into cash. Slowly members have been re-risking their asset allocations but as at September 2020 the amount of assets held in cash was still increased. Consequently those who switched may have missed the upswing in markets.

However, self-selecting members are a small minority with most being invested in default investment arrangements which in general have better protected members' savings. Fidelity's customer service centre has experienced (and continues to experience) a significant increase in telephone calls to discuss account management. It seems pension scheme member engagement is heightened at the moment. Broader financial resilience is also a key issue in itself as well as its influence on peoples' capacity to save. Fidelity research[6] shows that, whilst on average those currently employed have savings sufficient to cover 4 months' everyday expenses, 10% could cover less than one month's expenses. Separate research we undertook revealed 60% of people accessed their savings during the pandemic, with the number doing so increasing amongst younger age groups. Even 80% of those who were furloughed had accessed their savings to get by. Meanwhile, 25% of people actually increased the value of their savings accounts. As observed by other providers, different segments of society have been impacted differently.

Gareth: Nest has a younger membership than some of the other providers here and probably because of that we have not seen the same level of changes in retirement claims that others have. Overall we haven't seen significant changes in member behaviour through the pandemic. The opt-out rate of our membership has increased only marginally from 10% to 12%. The rate at which members leave the scheme beyond the opt-out window is also broadly stable, as are the contributions we receive from members and employers. The area which has seen the biggest impact is new joiners, which has fallen from previous levels. Clearly that is likely to be the result of more challenging employment market at the moment.

We have also looked into the effect of the pandemic on the financial wellbeing of our members through survey research. In an internal survey 44% reported that Covid has negatively affected their finances. This rose to 74% amongst those that had been furloughed. Younger members and the self-employed[7] also tended to report higher levels of negative financial impact. On the other hand, the impact of Covid-19 has been unevenly distributed and 20% of members report a positive financial impact as a result of the pandemic.

To provide some context about the impact of the pandemic on the Nest membership, from the same survey 17% say that they have been placed on the Job Retention Scheme. Amongst those under 29 this rose to 24%.

Two thirds of those surveyed said they didn't know what impact Covid-19 had had on their pension pot or that it would not have had any impact. The fact that the impact of Covid-19 on pensions may not be front of mind for members may have been helpful in sustaining participation through the pandemic.

We also asked members about rebuilding following the pandemic. There was broad support for the concept of build back better, with almost 60% saying that it was either very important or essential to them that their pension was invested in a way that supports a green economic recovery post-Covid.

Sharon: While there has been some switching activity, they have reacted through "think twice" messaging. There have been slightly more opt-outs while new joiner rates have been similar to historical levels. The Scottish Widows "Women in Retirement" report indicates the pension gender gap has been reinforced as a high proportion of women work in hospitality means more women have been furloughed or retrenched meaning their contributions may have been suspended.

Callum: Having reviewed Covid related recent behaviours, what should we expect in terms of future trends?

James: Consolidation of smaller schemes. Perhaps Covid will energise this and make it happen sooner rather than later.

Gareth: As survey research is showing that there are many people whose finances have been quite significantly impacted by the pandemic we will need to think carefully about the level of contributions that is right for different groups. And for some groups that have been more negatively impacted – for example the young people in the Nest membership – some element of flexibility and liquidity like Nest Insight's sidecar trial may well be very important for helping them to save.

Donna: Indeed, we need to support people with what is important to them at any point in time and this is likely to vary based on several factors such as life stage and level of wealth. One example of where we can link accessible savings and retirement savings is through Jars/sidecar savings. With this solution there is an auto roll over of savings into retirement pots when the savings pot has reached a target level set by each individual.

Dale: The financial planning story board needs to be looked at more strategically. I think there's a need to balance the requirements for both life assurance and immediate cash needs ("rainy day preparation") with longer term financial planning.

James: Investor engagement measures should be reconsidered. It's not necessarily right to assume that pension scheme members that have self-selected their investments are, or remain, engaged. We might see firmer expectations or provisions to allow fiduciaries to take steps to protect members from adverse outcomes where active engagement is not confirmed.

Dale: Investor engagement is certainly an issue. HMRC data shows us that the amounts in Cash ISAs versus Stocks & Shares ISAs are 8:1, at a time when the interest rates on Cash ISAs are historically so low.

Donna: Identifying what investors may need, guiding them through options, including default funds or investment pathways and then monitoring their behaviours/actions can help people both save for and then spend in retirement. A good example here is where we communicate with members when their retirement withdrawals are not in line with how they told us they planned to take their retirement savings when they moved into drawdown via guided investment journeys. Communications to prompt members to their online drawdown review or to call us for support can help towards better outcomes for members.

Dale: Indeed, this is necessary but also presents the dilemma of whether such activities on the part of the providers constitute "advice" or "guidance". Moreover, such communications may be interpreted as unsolicited marketing, offending regulators.

Kate: I think we still need to be concerned about some of the older generation running out of money having accessed funds earlier or to a greater extent recently.

Dale: Although this is mitigated by some retirees who have not taken funds given there are limited opportunities to spend during lock down.

Callum: So, finally, a quick-fire round of opportunities in the near term?

Gareth: Greater connection between the thinking about the short-term financial challenges members face and their ability to save in a pension over the long-term.

Donna: The desire for and increased spotlight on responsible investing could provide a pathway to increased member engagement levels. With an increased focus on climate change and many companies announcing net-zero carbon targets we are seeing more employers looking for responsible investing defaults for their members. Our research also shows that people are looking for other, more targeted, investment options in line with what is important to them, including water and waste and gender diversity. This gives us a great opportunity to boost member engagement with their pension by talking to them about their investments and helping them make sure they are aligned to their needs.

Kate: Improving financial wellbeing and resilience in the workplace by working with employers. It's not just about pensions, but wider savings.

Dale: Better workplace driven guidance on retirement planning.

Sharon: Benefits consolidation.

James: Connecting the issues and impacts of general, mental and financial health. The savings industry has an important role to play in supporting consumers' health and resilience.

Concluding remarks:

Laura: Obvious Covid themes of concern may revolve around investment market volatility, missing or lower contributions, and those rushing to access pension accounts because they are desperately short of cash. However, increasing instances of 'delayed retirements', due to there being little to do or spend money on in that retirement, is clearly an emerging issue[8]. Many have reappraised their lives during the Covid pandemic, and priorities may have changed during the last year of lockdowns. Once these start to ease, it will be fascinating to see whether retirement patterns revert or whether some of the Covid patterns are here to stay.

Danny: There is a mounting body of theoretical and evidence-based research circulating. We have isolated the Association of Consulting Actuaries' (ACA) 2020 Pension Trends Survey[9] which provides some corresponding data to contrast with the findings of our panelists above. In particular their headline: "52% of employers support higher minimum auto-enrolment contributions and 62% think more flexibility would increase employee saving". The report also found that "11% of employers saw more employees leave their pension scheme(s) last year, and this increased to 26% following the COVID-19 outbreak" which is indicative of the shifts in momentum in retirement savings activities. The UK government is not alone in providing support to employers and employees for their immediate cash flow needs (a sample of countries shows a variety of such measures[10]). However, the support for longer term savings needs to be getting the same attention at a policy level.

Notes:

1. The ICAT DC working stream is the Institute COVID-19 Action Taskforce addressing the impact on members of Defined Contribution pension schemes.
2. The Institute ICAT DC working stream was represented by
    a. Callum Stewart, Hymans Robertson
    b. Laura Andrikopoulos, Hymans Robertson
    c. Danny Quant, Milliman LLP
3. The providers were represented by
    a. Dale Critchley, Aviva
    b. Sharon Bellingham, Scottish Widows
    c. James Carter, Fidelity
    d. Kate Smith, Aegon
    e. Donna Walsh, Standard Life
    f. Gareth Turner, NEST
4. https://www.aviva.co.uk/business/business-perspectives/support/age-of-ambiguity/Scottish Widows research
5. https://www.aegon.co.uk/content/ukpaw/news/pandemic_causes_peopletore-evaluatetheirfinancialresilience.html
6. https://retirement.fidelityinternational.com/financial-wellness/global-financial-wellness-survey/
7. https://www.nestinsight.org.uk/wp-content/uploads/2020/12/The-impact-of-Covid-19-on-self-employed-peoples-saving-outlook.pdf
8. https://www.hymans.co.uk/insights/webinars/covid-19-the-long-term-impact-on-dc-pensions/
9. https://aca.org.uk/employers-support-higher-minimum-contributions-but-more-than-a-quarter-say-covid-has-increased-the-number-of-employees-leaving-pension-schemes/
10. https://www.milliman.com/en/insight/employers-face-challenges-on-managing-and-funding-pensions-after-furloughs

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