FLEXIBLE DECUMULATION

A popular option?

Member states across Europe are waking up to the idea that a fixed-term annuity may not be the only answer. Could flexible decumulation be the answer?

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The at-retirement market is often overlooked when compared to the long run in of the accumulation phase, meaning innovative new developments are few and far between, but changes are afoot.

As the switch from defined benefit (DB) to defined contribution (DC) takes hold across the continent, and savers' work-life balance requires an increasingly flexible pensions system, more innovative solutions are required if savers are going to maximise their savings pot.

In April 2019, the Cross-Border Benefits Alliance-Europe (CBBA-Europe) published its *Reflection paper on new strategies for decumulation*, noting that the key to a secure life after retirement is customisation of a number of investment products to suit an individuals' needs.

It added that in most European member states savers are often only offered two choices at retirement: A fixed annuity at retirement or a phased withdrawal strategy. "Each solution has its advantages and disadvantages, but neither, taken in isolation, is perfecty suited to an individual retirement savings solution," the report said.

No one size fits all

Many savers and industry professionals understand that buying an annuity should not be the only option at retirement, and while the industry is looking into alternative pathways, nothing concrete has emerged yet.

European Insurance and Occupational Pensions Authority (EIOPA) pensions policy coordinator, Sandra Hack, says: "It is the starting point where some member states are rethinking their approaches because if you have a relatively small savings pot in a low interest rate environment the value of the annuity might be too low. It does not make sense to have annuities in all circumstances."

Mercer partner, Brian Henderson, agrees: "We are experiencing the rise of drawdown to the detriment of annuities and pensions for life. I think that is definitely a trend that we are seeing across markets, as well as more control over how you spend your money."

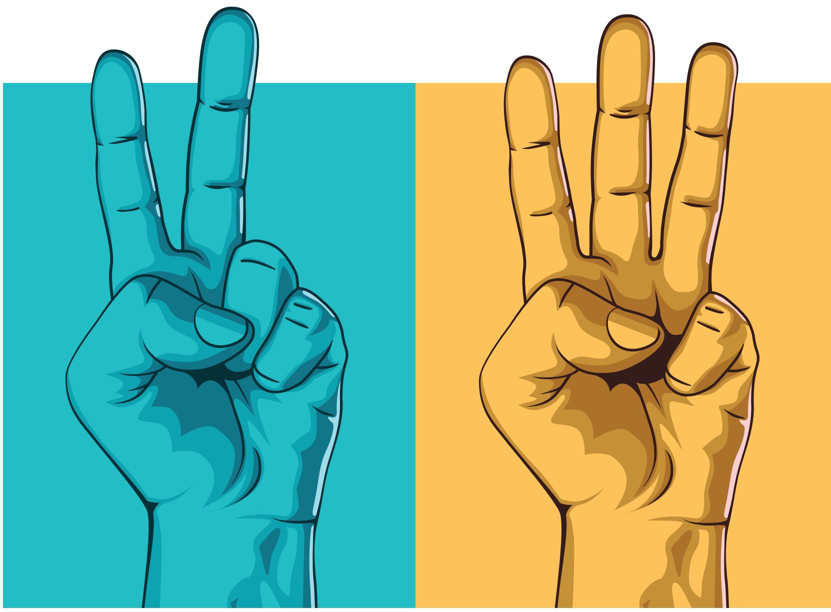
Part of this, of course, is down to longer life expectancy over developed nations and thus the ability to flexibly work past retirement age if required. As life expectancy has risen steadily over the past century, now standing at 83.5 for women and 78.3 for men across the European Union, people's ability to work in retirement has increased.

In light of this, the Netherlands introduced the flexible annuity in December 2016, with some varying success. "Research shows that only 5 per cent of people opt for variable benefits," Aon senior ALM consultant, Corine Reedijk, notes.

"Most employees want certainty about their pension, especially for low earners. This means that, with the current low interest rate, pensions under a DC scheme often are somewhat disappointing."

Hack, who has led much of the policy work behind the pan-European personal pension (PEPP) product, believes that much of the benefits of the incoming product could be felt in occupational pensions across Europe too. "This is a personal pension product, but some of the findings over the last couple of years are equally applicable to occupational pensions, at least some of the principles," she says.

"In terms of decumulation, the PEPP is very free and the reason for that is that decumulation is often determined by the national solution to the fund. We believe in a mix, like partial withdrawal but also a lump sum from your retirement savings. Maybe in addition, because there is the risk you might be outliving your pensions and savings, is the role of deferred annuities. We would



like to see a bit more across the markets."

There has been signs of more product offerings over the past year, which has been in part down to the mandatory transition from DB to DC in the Netherlands, including the transfer of all past DB services to DC plans. According to Reedijk, in the European free market, the share of DC plans has grown from less than 7 per cent in 1995 to more than 70 per cent in 2018.

What price for freedom?

While retirees in the Netherlands might already be able to opt for a flexible annuity, policy makers on the continent tend to be a bit more reserved when it comes to more out of the box solutions, such as the freedoms seen in the UK.

DB savers in the Netherlands will soon see a new option introduced at retirement, the possibility to take 10 per cent of your pension capital at once as a cash payment at retirement age, but Reedijk believes this is as far as it should go.

"We think that more freedom is not useful as people cannot foresee the choices they can make. The pension system in the Netherlands is already quite complicated. We therefore think that communication becomes more and more important," Reedijk explains.

Having watched freedom of choice unfold in the UK, Hack agrees that freedoms offer a difficult conundrum for Europe, which views pensions much more in the context of social security.

She says: "It does make sense that you want to ensure that people are making the right choices. From a personal point of view, it also makes sense to ensure that people are different. It's to prevent you from spending all your savings and you fall back on social security, which of course is not in the interest of any government."

Communication, Henderson notes, is a major theme across European pensions at the moment, and is tied in with building trust and having greater transparency.

"Pre-retirement costs and charges are scrutinised pretty closely and good value is accepted as the norm but when you flip that to post-retirement all of that goes out of the window. How do we make the two join up together – as well as transparency?

"It's about building trust around the solutions that are offered. It has been largely under scrutinised and trust goes along with that."

According to a State Street survey of 10,000 members across eight countries, more flexibility in early retirement and security in getting older seems to make people across Europe happier.

However, the survey also revealed that members are not aware of the choices they already have. Providing more insights is key.

"The more choice, the more need for member advice on occupational pensions. There seems to be an emerging advice vacuum in pensions. We must fill this gap as soon as possible and learn from countries like the UK, which already experiences pension scams and is developing solutions to fill the advice vacuum," State Street Global Advisor senior pensions strategist, Jacqueline Lommen, argues.

What could help the market, and a process that the UK is currently trying to push through big developments, is the rise of fintech to help people navigate their way through the jump from the pre-to-post-retirement phase.

"There are more digital interventions made available to make the transition smoother. There's a rise in fintech or pensions tech to allow people to navigate their way through without going through the huge expense of getting an adviser to do that for them," Henderson said.

"That is a trend we have spotted and are participating in, we recognise that there are those who want to self-serve and do it online, without paying people a few grand that they are never going to see again."

While more solutions will no doubt provide the flexibility that the market is looking for, the ability to communicate them in a way that builds transparency and trust must be the way forward for member states. ■