New Choices, Big Decisions

Crunch time! Unravelling the impact of the cost of living crisis

The evolution of consumer decision-making and behaviours under pension freedoms and choice

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Sponsored by

the people's pension

STATE STREET GLOBAL ADVISORS

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Foreword

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We are delighted to present to you the fifth wave of our New Choices, Big Decisions research on retirement decision-making.

The series aims to provide rich insights into the challenges of making financial decisions about retirement income by looking in depth at the lives and finances of our respondents and tracking them over time. This wave takes place in a very different economic environment, with a cost of living crisis created by high inflation and markedly higher interest rates.

It is interesting to hear how the participants value the 'bedrock' of the State Pension, around which they can arrange their private savings and other sources of income. We also look at the choices people make in relation to work, with some returning to the labour market after a brief 'retirement'. It is notable how patterns of life and decision-making capabilities change as people move into the later years of retirement.

This reinforces our view that for many people, a guided retirement income product that provides flexible access to the pot in the early years of retirement, along with a stable, guaranteed-for-life income in the later years, will be a valuable approach. As ever, we appreciate the insights of Ignition House and have enjoyed collaborating with colleagues at People's Partnership. We hope you find the report enjoyable, interesting and useful.

It has been a pleasure continuing to work with State Street Global Advisors and Ignition House on this important and unique longitudinal study.

If nothing changes, then this research is a vision of the future. Without reform, it's easy to imagine thousands more people struggling with the same fundamental problem: how to turn capital into income in a sustainable way.

Fortunately, we are beginning to build a much more solid evidence base around how DC decumulation could work better for retirees. It's increasingly clear that the decumulation product or product combination will need to address the main risks faced by retirees. This theme is already important, and we expect it to become even more so as the study progresses, and our pioneers' willingness to take difficult decisions decreases further.

Topically, we see current debates over the uprating of the flat-rate State Pension as critical to the future of automatic enrolment and DC decumulation. It's clear from the study that the State Pension is the bedrock of DC dependent savers' retirement income. Over time, we expect it to retain its central role in how people retire and for its centrality to fade only when DC saving is much more mature.

At People's Partnership, we're proud to have sponsored this work and hope that it sparks further discussion on policy and product development across the sector.

1 Summary and Implications

In 2015, we started a longitudinal study following 80 people as they grappled with their initial decisions under the new pension freedoms. Our findings were published as part of the New Choices, Big Decisions[1] series of reports and have been widely disseminated to industry, policymakers, regulators, and the government. Since then, we have been keeping in contact with as many of the study participants as possible, and this is now the fifth time we have caught up with 35 of our original pension pioneers.

They are starting to experience health issues – in some cases, these are serious - and they are beginning to notice the onset of cognitive decline. Particularly striking is the nascent lack of confidence in managing their investments among those who have previously enjoyed this challenge.

When our study started, many of our original respondents – particularly those who simply took their tax-free cash and left the rest in zero income drawdown (ZID) - were still working, and thoughts of full retirement were quite far away. Seven years later, the situation is very different. Most are fully retired, and they are facing the harsh realities of the decisions they made in the toughest economic climate for years.

In these difficult conditions, our study highlighted the importance of the State Pension as the bedrock of retirement plans. Just how much they relied on the State Pension came as a surprise to some respondents. A few years ago, their expectations of the State Pension were that it was a “pittance” or “not worth much at all”. As the reality of full retirement and no more earned income hits home, they have come to appreciate it more and more. In a world of uncertainty, it is a relief to know that the State Pension is (relatively) simple, reliable, and guaranteed for life.

There was a strong sentiment that the triple lock was a “good thing” for pensioners, and they wanted it to remain in place. However, awareness of what the triple lock actually is was very low. Most understood that it had something to do with protecting pensioners against rising prices. Of course, this is a key element of the promise, but there was little or no awareness of the other two factors. The fact that the state provides this safeguard against inflation for a substantial portion of our retirees' household income is hugely important. Left to their own devices, our respondents did not consider inflation when making their income decisions, even though they had lived experience of its impact.

Retirement planning is an evolving process over many years that is likely to necessitate adjustments as circumstances change. Seeking guidance periodically can be invaluable for retirees, enabling them to make well-informed decisions, optimise their pension funds, and maintain financial security throughout their retirement years. However, there is currently a concerning lack of attention given to the 1.1m pension pots already in drawdown, and our drawdown respondents feel like the forgotten generation. They have not been triggered by any notifications or communications from their provider to think about whether the plans they had seven years ago are still valid today, whether their withdrawal rates are sustainable, or to consider the suitability of their investment choices. They have not conducted any further research and are no more aware of their investment options, the tax implications, optimal withdrawal rates, or other financial aspects than they were seven years ago. Instead, they are thankful that the decision has been made and that they don’t have to think about these complex issues anymore. Except perhaps for inflation, they are no better informed today of the plethora of risks they face than they were back then. Without the motivation to shop around or periodically review their investment objectives, our drawdown gang is simply letting their pension pot take its course without making informed decisions.

Much press attention has been paid to the UK’s ‘Great Retirement’ problem. However, new data from the October – December 2022 Labour Force Survey[2] show signs of a possible reversal. The The Institute for Fiscal Studies (IFS) confirmed that there has been an uptick in those returning to work amongst the over-50s who had been out of work for less than three years – that is, they had left the workforce after the pandemic began. And so, in light of this positive development, we wanted to explore this in a little

[1] New Choices, Big Decisions series of reports: Waves 1-4
[2] https://ifs.org.uk/articles/new-data-show-signs-over-50s-returning-workforce

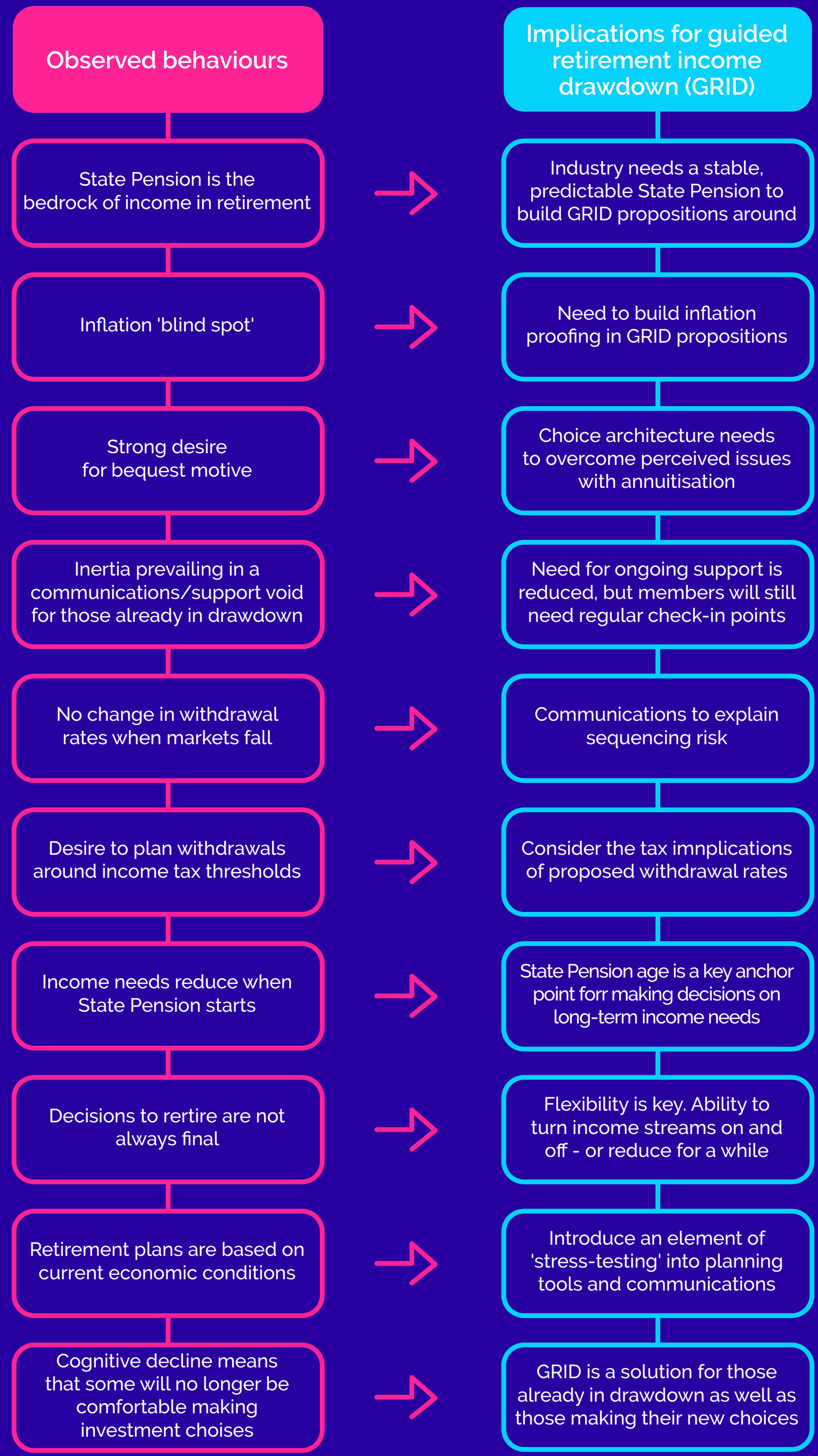
more detail to try to understand what the drivers of this behaviour are and to see if there are any implications for drawdown.

Speaking to 15 people in total about their reasons for leaving and experiences of rejoining the over-50s labour market, we found that there were a myriad of reasons why our re-joiners left their job. However, for the majority, the availability of a pension (DB or DC) played a pivotal role in their retirement choices; without it, many would likely have continued work. Notably, receiving wake-up letters at 55 often sparked contemplation of early retirement. Using their tax-free cash to pay off or pay down any remaining mortgage 'allowed' them to think about giving up work. They are often setting drawdown rates to keep below income tax thresholds, or at £10,000, so that the State Pension provides a replacement income when the time comes for them to claim it.

Looking at what they did next gives useful clues as to how the over-50s might want to participate in the labour market in the future. The message came through loud and clear: even though many were feeling the pinch, they did not want to go back to business as usual and would only return to work on their terms. Our re-joiners still looked for a sense of value and structure in their work, but the types of jobs they wanted were very different from their previous working lives. Typically, their roles now involve low stress and can be characterised as "little jobs" that serve as a means to top up their income or provide extra spending money. They preferred to seek employment opportunities within their local community to avoid lengthy commutes. They got used to being at home during Covid, and their period of retirement reinforced the desire to avoid the misery and expense of the daily grind to and from work. Flexibility is also a key consideration, and they looked for working hours that suited their lifestyle rather than adhering to a strict 9-to-5 schedule. Knowing that they can step away whenever they wish, take breaks for travel, or fulfil caregiving responsibilities is an important motivation.

At the moment, we're still very much in a 'Do it Myself' environment, where those making 'Big Decisions' on what to do with the remaining 75% of their pots are muddling through with limited provider interventions. As the DC retirement landscape gradually transitions from a retail, 'Do It Myself' approach to a more institutional "Do It For Me' model, there are some important lessons to learn from our ongoing study that can help inform the design of these emerging guided retirement income plans.

Figure 1: Key Lessons for Guided Income Retirement



2 Background to the study

Introduction

In 2015, we started a longitudinal study following 80 people as they grappled with their initial decisions under the new pension freedoms. Our findings were published as part of the New Choices, Big Decisions[3] series of reports and have been widely disseminated to industry, policymakers, regulators, and the government. One year later, we checked in with our brave pension pioneers to find out how they had been getting on, to see how their lives had changed, and to understand, with the benefit of hindsight, how they felt about the choices they made. Since then, we've been keeping in contact with as many as possible, and this is now the fifth time we've caught up with our pension pioneers.

Our initial conversations showed that pension freedoms have switched the mental accounting of DC (defined contribution) pensions from a future retirement income choice to a consumption choice. We identified the decoupling of the decision to take tax-free cash — often seen as a 'no-brainer' by members — from deciding what to do with the remaining 75%. This second decision is, understandably, widely recognised to be much more difficult, especially as this generation was the first to take advantage of pension freedoms. They have only ever lived in a 'retail environment' where they are responsible for making choices about what to do with their money, choosing their drawdown product (although most follow the path of least resistance and stay with their own provider), selecting their investment choices (generally choosing defaults or medium to low risk), and deciding how much money to withdraw each year.

According to FCA's retirement income data[4], there are now over 1.6m policies in drawdown and over a million where the initial decision was made some time ago. However, government, industry, and regulatory attention is still very much focused on the initial decision, and very little attention has been given to those already in drawdown and to whether they are getting the information and support they need. This study aims to fill that important information gap.

[3] New Choices Big Decisions series of reports: Wave 1 (Part 1, Part 2), Wave 2 (Part 3), Wave 3 (5 Years On)
[4] https://www.fca.org.uk/data/retirement-income-market-data-2021-22

Figure 2: Evolution of the Study – Waves 1-4

1. 2015

- Thirty minute in-depth interviews'
- Eighty active diary participants
- Five hundred daily posts & 80 video blogs, spanning 8 months
- One-hour end-of-project in-depth interviews with 80 participants

2. 2016 - 1 year on

- One year later, we onducted a one hour telephone call follow-ups with 55 of our 80 participants
- Research explored life changes, any new decisions, and regret and future plans

3. 2018 - check-in

- We conducted 10-15 minute conversations with 21 of the original 80 respondents to renew GDPR permissions for quotes and clips
- We took the opportunity to get top-level insights into how their plans were progressing, whether they had made any further decisions, and future intentions

4. 2020 - 5 years on

- We conducted one hour online conversations with 30 of our original respondents and a further 20 'top up' respondents all of whom had taken tax-free cash (TFC) and further drawdown withdrawals
- We explored retirement plans in light of the Covid-19 pandemic

Figure 3: Pension Personalities

We are very mindful that DC pension decisions are not taken in isolation. The value of this particular study is that we have a holistic view of our respondents. We have taken the time over the years to understand their family situation and their finances at the household level, rather than looking through the rather unsatisfactory lens of an individual pot. We have seen how their circumstances have evolved and how their plans, hopes, and dreams they had for retirement back in 2015 have panned out in practice.

While every person in our longitudinal study has their own unique set of issues and perspectives, we also found some common themes. We identified seven pension personalities based on the approach they took to their initial decision, from the Procrastinating Petes and Paulas, who were overwhelmed by the task at hand, to the I Can Do Better Colins and Claires, who had lost all faith in pensions and would rather have the money in their control.

When our study started seven years ago, many of our respondents – particularly those who simply took their tax-free cash and left the rest in zero income drawdown (ZID) - were still working, and thoughts of full retirement were quite far away. Over the years, we found that not much had changed and they had no need for further withdrawals; either the initial sum was still being spent or they were receiving an income from work that covered their needs. But seven years on, many of our respondents have now reached an age where the need to live off their drawdown money is becoming real - either through their own choice to stop working completely or due to the current economic climate.

So, what plans do they have for their money, and how have they come to these decisions? Did they get the support they needed, and what behavioural drivers are influencing their choices?

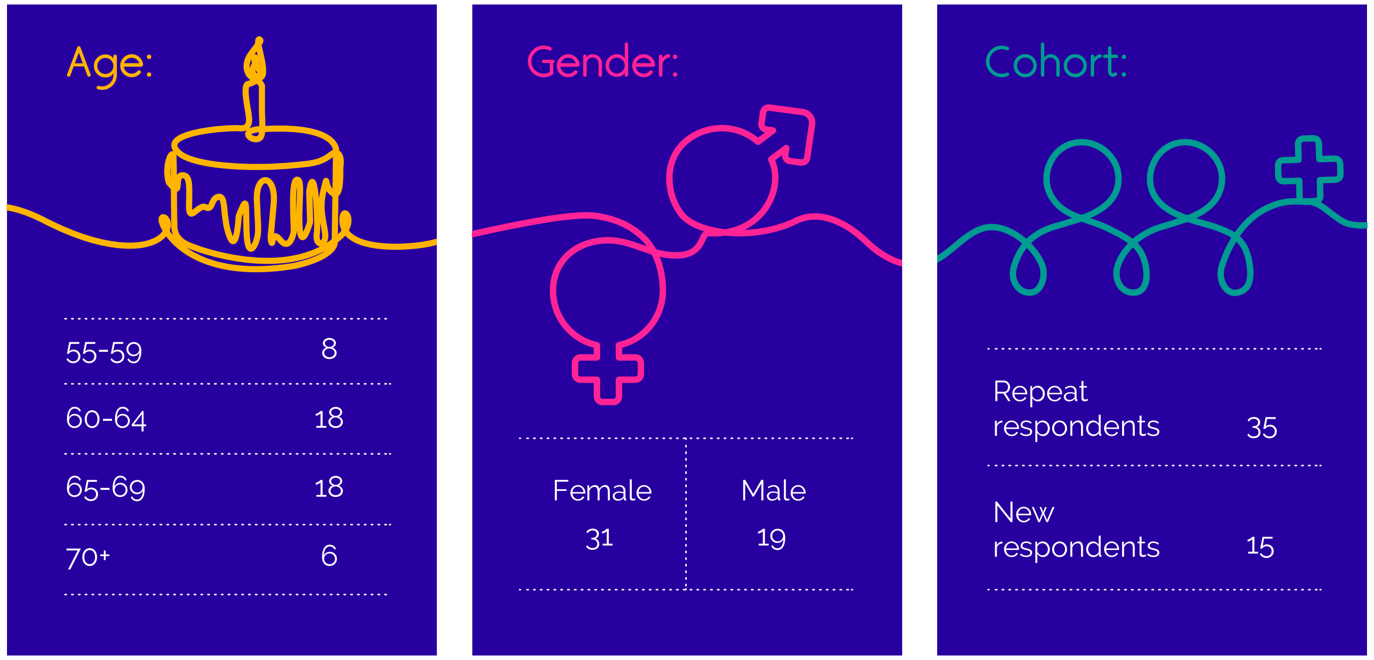
And so much has changed in the last few years. The shiny new cars and kitchens originally bought with their tax-free cash are starting to look a bit shabby, and those once-in-a-lifetime holidays are a dim and distant memory. Now our gang is facing the harsh reality of higher interest rates, food, and fuel costs. This generation has weathered numerous economic storms before and is no stranger to double-digit inflation and interest rates. But did they think it could ever happen again?

In this new economic environment, are they still confident that they have enough to live on in retirement? Have retirement plans been delayed to build up extra financial resilience? The over-50s are the last cohort with significant DB (defined benefit) pension provision. Have those fortunate enough to have this type of pension been somewhat protected from the ravages of inflation?

Understanding the 'Great Retirement': exploring those who have re-joined the workforce

Much press attention has been paid to the UK's 'Great Retirement' problem. Since lockdown, the increase in economic inactivity has been a focus for the current government, with most of the rise in inactivity driven by 50- to 64-year-olds. Yet recent data suggests the trend may be reversing and that some of these older workers are returning to work. In this wave, we wanted to explore what motivates older workers to exit the labour market, and in particular to what extent pension freedoms and the ability to access DC money without annuitisation had on their decisions. We focus our attention on people who have subsequently gotten another job to see what, if any, lessons we could learn from those who had then decided to return to work due to the pressure of rising living costs. To do this, we topped up our original gang with a fresh set of fifteen respondents. We call these our 'Re-joiners'.

Figure 4: Sample composition for Wave 5



[4]https://www.fca.org.uk/data/retirement-income-market-data-2021-22

3

On its 75th birthday, the State Pension is still the bedrock of retirement plans

The State Pension system in the UK was introduced in 1948, making it 75 years old this year. Currently, 12.5m people claim the State Pension[5], and, as a nation, we spend over £110bn a year to fund it.

All of our original cohort of respondents are now over 60, and some are well into their 70s. All bar one of the top-up cohort from Wave 4 are now over 60. Most of our respondents are now getting their State Pension, but the age at which the State Pension started and the amount they now receive vary. Some were getting the old State Pension, but most were getting the new one. Most had the full State Pension, and are therefore getting over £200 per week, but some did not. Some are Women Against State Pension Inequality or 'WAPSI' - women born in the 1950s who feel unfairly treated by the rise in pension age.

We asked our respondents, both those in receipt and those who will get it shortly, how they felt about the State Pension and how important it was to their retirement plans. It's important to note that our respondents were initially selected to have more than £30,000 saved in their DC pots in 2015. The vast majority own their homes outright. Many had additional levels of DB income within their household.

Views on the State Pension have become more positive as the reality of retirement sinks in

Across all of our respondents, irrespective of wealth or other income sources, the State Pension was consistently seen as an important part of their retirement plans, for several reasons:

- The State Pension age (SPA) is often the anchoring age for full retirement.
- The State Pension more or less covers their basic household spending (bills, basic food, utilities), and their DC and DB income tops them up to provide the "little extras" (eating out, leisure, holidays, clothes, home repairs).
- They may be using DC pensions to form an income bridge to SPA and are withdrawing so that their money runs out when the State Pension kicks in, or withdrawing £10,000 (to keep under the tax threshold), which will then be replaced by their State Pension when the time comes.

Reliance on the State Pension came as a surprise to some respondents. A few years ago, their expectations of the State Pension were that it was a "pittance" or "not worth much at all". As the reality of full retirement and no more earned income hits home, they have come to appreciate it more and more.

> I'm very grateful for it. It almost doubles my income. If I hadn't had the State Pension I would've had to seriously think about getting another full-time job, or being really miserable in the job I had.
>
> **Female, 65-69**

> State Pension is very valuable to me. Most of it pays my monthly standing orders for all the main services and the maintenance.
>
> **Female, 65-69**

[5] https://www.gov.uk/government/statistics/dwp-benefits-statistics-august-2022/dwp-benefits-statistics-august-2022#:~:text=The%20 State%20Pension%20caseload%20has,140%2C000%20on%20a%20year%20earlier.

The importance of the State Pension

The recent inflation increase was noted by all in receipt of the State Pension (and many of those who will get it shortly), and the fact that a two-person household now receives more than £20,000 a year is a welcome buffer against the rising cost of living. Furthermore, when respondents heard that they would need to have saved the best part of an additional £250,000 if they were single and half a million for couples if the State Pension did not exist, they were even more thankful that this practically universal safety net remains in place.

In a world of uncertainty, it is a relief to know that the State Pension is (relatively) simple, reliable, and guaranteed for life

Our respondents felt strongly that one of the key benefits of the State Pension is that it is a relatively known quantity. Most had a forecast a couple of years in advance and so were prepared for what they eventually got (although they had no idea how they could check whether the forecast – and the amount they were now receiving - was correct or not).

The ability to top up missing years of the State Pension has relatively high awareness, driven by a combination of friends and family, hearing about it in their workplace, reading about it in retirement literature, and publicity in the mainstream media (particularly on the Martin Lewis Show). Our respondents were less sure about whether or not they could defer their State Pension and why this could be of benefit to them. This felt like yet another difficult decision, and therefore they tended to follow the path of least resistance and claim their State Pension as soon as possible. WASPI women, in particular, felt that they had waited long enough.

> I think it's very generous, to be honest. I think it's £10,000 something a year. I think that's pretty generous. And we had a 10% increase there a couple of months back. I'm happy with it.
>
> **Female, 65-69**

> I've looked on the calculator and allegedly I'm getting a full State Pension. I've been on the online thing where you put in your own under your national insurance number. At one point a couple of years ago I was being offered top-ups but the last time I checked, which was probably last year when I was 60, it said you've got a full record.
>
> **Female, 60-64**

> I got a forecast. A friend told me to do it and so I did. The forecast said if I paid x amount upfront - and it wasn't a fortune we're talking about a few hundred pounds - then I got a much better State Pension. Which is exactly what I did.
>
> **Female, 65-69**

Crucially, our respondents placed a lot of value in knowing that they can rely on the State Pension to be paid every four weeks until they die. It will never run out, there are no investment choices, and it will not go down in value. Given the uncertainties facing those in drawdown, and the common expectation that their DC money would last for only 5-10 years, it was a welcome relief that at least part, and for some, most, of their household income is safe, secure, and guaranteed for life.

For many in our sample, the State Pension is not their only source of guaranteed lifetime income. Many households have some DB; others bought annuities before pension freedoms were introduced. Those with DB have been somewhat insulated from the impact of recently rising prices. However, the importance of the State Pension will only increase as the next generation is fully exposed to a DC world. Those with annuities tended to buy flat-rate, and so are living off an income that is falling in real terms. Increases in the State Pension have partially protected them from this decision.

> I did factor it into my financial decisions that at 67 I'd get a State Pension, and therefore I could take more now from my private savings because when I get to 67 that will be a kind of top-up. But obviously the cost of living sort of makes things slightly different now.
>
> **Female, 60-64**

Yet, the future of the State Pension seems to be under constant scrutiny, and this was certainly reflected in our conversations. Reaching the State Pension age felt like a huge milestone. Up until that point, there were always some niggles in the back of their minds that the government might move the goalposts again. But once State Pension is in payment, they feel they are 'home and dry', confident that rules cannot now change for them.

> If the age doesn't go up, I think I should be all right though. Because God knows what they'll do. I think they are a law unto themselves, aren't they? I don't know how they can afford to run all these pensions really. So no, it's not a given is it by any chance.
>
> **Female, 60-64**

> I think they'd be on very, very dodgy ground if they even considered that [making a change to State Pension for those already getting it]. Although I don't see us going out into the streets protesting like the French do. I don't think they're going to be able to do something like that. I can see it going up to 70, but probably not in my lifetime.
>
> **Female, 65-69**

> You've worked hard all your life so your State Pension probably shouldn't be means tested. You've made decisions in your life to get to the end of the road where you take your State Pension. I don't think that they will tamper with it.
>
> **Male, 65-69**

Triple lock: Please keep it - even though I don't actually know what it is

Barely a day goes by without some news coverage on the future of the triple lock, which is a promise to increase State Pension by the highest of inflation, growth in average earnings, or 2.5%. Recent inflation rates have focused attention on whether the cost of funding the policy is too high or too uncertain and whether the government could better spend the money elsewhere. The power of the grey vote is powerful, and we wanted to test what those affected by any changes to the triple lock think about it.

Not surprisingly, given the amount of mainstream media press coverage, awareness of the words 'triple lock' was very high, with all bar one reporting that they had come across this term before. There was also a strong sentiment that the triple lock was a "good thing" for pensioners, and they wanted it to remain in place.

However, awareness of what the triple lock actually is was very low. Most understood that it had something to do with protecting pensioners against rising prices. This is a key element of the promise, but there was little or no awareness of the other two factors.

> I have heard of it. And I've never really known what it was. It's something about guarding against inflation in terms of pensions. But I don't know why triple, I don't know what the other two things are.
>
> **Female, 65-69**

> Isn't it something to do with inflation? I can't explain it properly, but I think it has something to do with rises in inflation, doesn't it? Or something like that.
>
> **Male, 65-69**

> Triple lock is where they use whatever the rate of inflation is in September to decide what the pension will go up by on 6th of April. I don't know why it's a triple lock. To be honest, I've never thought about it. I know the principle whereby it's linked to inflation. I've never really thought where the triple comes in.
>
> **Male, 70+**

4

Crisis? What cost of living crisis?

The cost of living continues to climb, leaving many individuals and families grappling with financial challenges. From soaring fuel bills to a rapid rise in interest rates, it often feels like the UK's purse strings have been stretched to breaking point. But there is emerging evidence that certain groups of pensioners have been insulated from the worst impacts – and this was certainly true for many of our respondents.

A combination of savings, some DB, and State Pension means that most of our original gang are weathering the current financial storm

Our respondents have a few simple goals for retirement. All they want is their health, quality time with their family, and enough money to pay the bills, do a bit of socialising, and have a few holidays a year. Despite rising costs, most still seem to be on track.

Yes, they have changed their shopping habits a bit and are generally more careful with their money. They had not fully returned to pre-Covid spending habits and are generally spending less on eating out and clothes than they used to, even before the increased cost of living started to bite. Holidays are back, but emerging health niggles mean that they are less likely to go long-haul these days, preferring short stays in the UK and Europe.

> At 68 you don't go out in the town three nights a week like you did when you were 28. You go out for a meal with friends once in a while. I'm not in the mood for a holiday this year. Don't ask me why. In March, I spent a few days in Hampshire. We're going to Edinburgh at the weekend. Things like that I can do, but I'm not really in the mood for one of the usual kind of Lanzarote-type things this year.
>
> **Female, 65-69**

Yes, our 'gang' experienced a rise in energy costs, but the government support package provided to all pensioners helped them get through the winter months. Some felt a little guilty that they had received this additional payment when they didn't need it and felt that the government could have better-targeted support for struggling families.

> I enjoyed the £500 winter fuel bonus at Christmas time which all pensioners got. We went on a holiday. Why should I get the winter fuel benefit at Christmas? It seems bonkers to me, but I'll take it 'cause they gave it to me.
>
> **Male, 65-69**

Yes, they have seen food prices rise, but they were keen to point out that their State Pension went up by over 10%, and many also had DB pensions, which also increased (albeit not to the same extent), which went a long way to covering the increase in the basics.

> I have changed my shopping habits, I think. I now look in the area in the shop where the prices are reduced because it's maybe going to go out of date that day. So I'll buy stuff there and put it into the freezer.
>
> **Female, 65-69**

> We both get full State Pension, which is quite a reasonable amount now. It is nice; it almost pays all our direct debits, our utilities, mobile phones, TV, community charge, et cetera. It just about covers those. We had a nice boost this year actually. It went up by 10%, which was noticeable. It normally goes up, 2-3%. With our lifestyle, it is a really nice start.
>
> **Male, 70+**

Cost of living impact

By this stage in life, they typically have no or very small mortgages to pay, and so the crippling increases in interest rates have had no material impact on their spending power. They are not yet fully aware that inflation is eating away at their cash savings, and they will need to be more savvy with their money. They have started to notice savings rates creeping up, but most are not particularly shopping around for better deals.

Savings have usually been the first port of call to meet additional expenses

In the minority of cases where the increasing cost of living has made life quite difficult and cost-cutting has not been enough, we observed some interesting behavioural responses amongst our drawdown respondents.

Once again, inertia is a powerful driver. We observed a strong tendency for our respondents to withdraw their cash savings first to make up income shortfalls, rather than increase the amount they are taking from their drawdown account. People are creatures of habit, and we noticed that this pattern of behaviour was particularly strong where withdrawals are coming regularly through a direct debit rather than through ad hoc lump sum withdrawals. It had simply not crossed their mind to make a change to their direct debit mandate to get more regular money out, whereas it felt much easier to make a new request for an additional payment.

> When I took the part-time job, I carried on drawing the pension - £400 per month - and if there was anything left at the end of the month, I just put it in the savings account. I don't know why £400; I guess we thought about it and it just topped the State Pension up to a reasonable level. When the prices went up, we didn't change it.
>
> **Male, 65-69**

That said, the fact that drawdown is flexible and payments can be increased (or decreased) depending on the circumstances at the time was very much seen as a positive, especially compared to DB pensions. If taking a bit more now means that money will run out a couple of years sooner, this did not seem to worry our respondents too much, as they still feel the future is so uncertain.

At the extreme, several of our re-joiners (the 15 respondents who had retired and subsequently gone back to work) reported that the key trigger for them to go back into the workplace was watching the value of their savings pot decrease. In these cases, they did not want to increase their drawdown withdrawal amount as they were worried that the money would run out too quickly.

> I mean that's a good thing about having it flexible. Whereas, if I were in a company pension scheme, it would be a fixed amount of money every month. I wouldn't have that flexibility. My pension currently is not due to run out till I'm 80 or something anyway. I'm not going to worry about it. Because I think long term that it is where it is, and it's what it is, and it's all a bit swings and roundabouts. I don't know what my circumstances will be. So I'm not gonna worry about something running out when I'm 78 instead of 80.
>
> **Female, 60-64**

Josephine

Gender: Female
Age bracket: 60-65
Working status: Was fully retired, now working part time
Cohort: New respondent
Pension decision: Taken TFC to reduce mortgage at 61 and withdrawing under the tax threshold

Their situation

After 44 years, Josephine left work due to an illness that was exacerbated by stress. She was pleased to retire, as she could spend more time with her grandchildren and look after her elderly parents.

She started to take a regular income from drawdown to keep under the income tax threshold until the State Pension kicks in. She was managing OK, but then her household costs increased and her mortgage doubled. The shortfall was significant, and she calculated she needed nearer to £20,000 to manage. She thought she could ride it out for a bit by using savings, but seeing her savings buffer fall was causing more stress than working, so she decided to get a job. Luckily, a friend of the family had a flexible position available that allowed her to have time off during the periods when she is ill.

Health permitting, she will carry on working in this job until she reaches the State Pension age and then she will review her finances again.

> I thought I can ride the storm using savings to pay the bills. But it wasn't sustainable. And then with the interest rate rises, my mortgage was going to double. You always think well I've got a little bit of money put aside, and that's okay. I'll use that for a rainy day. But that rainy day came sooner than I thought. And it wasn't for a holiday, it wasn't for something pleasant. It was just to survive. I thought I can't continue doing this otherwise I'm going get myself in a lot of trouble. I didn't want to take more from my pension as it wouldn't last me very long. Not only would I be paying the tax, but it would deplete quite quickly.

5 Inflation and interest rate increases still take everyone by surprise

Our respondents have lived through periods of high inflation, and all were old enough to remember the energy crisis in the mid-1970s. Yet despite these lived experiences, our respondents had not considered what would happen to them if, or when, the historically low levels of inflation and interest rates came to an end.

Any assessment of whether they could afford to retire or not was entirely based on what they were spending at the time and had no margin of uncertainty built in. While admitting that many of these so-called retirement plans were simply 'back of a fag packet' calculations, they also could not recall any warnings that they should be doing something different. They did not recall reading anything or being sent any information by their pension providers that clearly stated that they needed to 'stress test' their numbers to make sure they could deal with any future price increases on their proposed income.

> I get notifications and there's an online thing. I can go in and see how it is. But I don't do that because I just think it goes down, it goes up, you know. This week, it could be this, and next week, it could be something else. If someone's said, 'oh, it's gone down, therefore it's taking a thousand pounds off your income a month,' then that would bother me. But as long as I've got the same amount of income coming in, I don't really mind.
>
> **Female, 60-64**

> I'd tend not to look. At the end of the day, there's not a great deal you can do about it, whether it goes up or down. I'm still taking the same amount of money. I'm in high risk, just hoping for a better return on it.
>
> **Male, 65-69**

Drawdown respondents are oblivious to sequencing risk

The last two years have been a volatile period for the stock market. The markets fell significantly during Covid but recovered and were then hit again by the Ukraine war.

Many in drawdown have chosen to put their heads in the sand, refusing to look at their accounts as they don't want to be frightened by the numbers in there. Some reported feeling a bit powerless as they could see their funds dropping, but they had no idea what to do about it.

> In the pandemic, I think I lost about at least 25% on it. So in that way, it has come back up. But when I looked at 2018 to now, it's only gone up £3,000. I haven't got the knowledge to know what to do. I don't trust any pension advisors. I don't trust any of them or financial advisors. So I just leave it there at the moment.
>
> **Female, 60-64**

Those taking drawdown payments did not change behaviour as a result of the falling markets and typically have not ever thought to do so. They worry that markets (and therefore their pot) will continue to fall, and they would rather run down this riskier asset while they can. They are blissfully unaware of the concept of 'pound cost ravaging' and have no clue that their actions today will make it even harder for their drawdown pot to recover later, thereby making it ever more likely that their biggest worry – their pot will not recover - will come true.

At the extreme, the fall in markets drove a couple, both of whom were very near to full retirement, to cash in their pensions entirely as they felt that they could not run the risk that the pension would fall even further. They put the money into a savings account, locking in the loss forever. Once again, this behaviour highlights the different perceptions of pensions and savings.

Annuity purchasers could not have lived with the stock market uncertainty, but are now regretting having no inflation-proofing

Our annuity purchasers, our Secure Stan and Sue's, are grateful that they have a stable income and don't have to worry about volatile economic situations out of their control. They self-report being very risk-averse and not feeling at all comfortable taking any more risks with their money.

While they may have protected themselves against longevity risk, most of our annuity purchasers simply looked at the headline income figures, worked out the 'pay-back' period, and decided not to inflation-proof their purchase. With the benefit of hindsight, they now recognise this would have been a sensible thing to do and wished the consequences of their actions had been pushed harder by providers.

'I can do better' Colin and Clare, who invested the money themselves, have had their confidence shaken

Our Colin and Clare's are a mixed bag. Some were cashing in pensions to avoid the ongoing risk of a fall in the markets. Others felt that they were able to do a better job at investing. Reactions to the economic situation varied.

Those with money sitting in the bank had no regrets - and felt somewhat relieved they had taken the decision when they did. The money is still in the same savings accounts earning a 'pittance', or in premium bonds or fixed-term savings bonds. They are blissfully ignorant of the fact that their money has been losing around 7-10% of its real value each year. In fact, some are so sure that they did the right thing the first time around that they have subsequently cashed in their remaining pensions.

Those who took the cash and paid 40% tax to be able to invest the money themselves have often not yet made that money back.

Those who have had some success in the past are finding it increasingly difficult to find a return.

> I don't want to have to worry about different scenarios each month. I like the security of knowing exactly what I'm getting. The news doesn't worry me. I didn't want anything that was going to fluctuate each month. I just like to know what I'm getting and that way I know what I can live on.
>
> **Female, 65-69**

Jimmy

Gender: Male
Age bracket: 60-64
Working status: Semi-retired, working part time
Cohort: Original cohort
Pension decision: Total encashment

Their situation

Jimmy cashed in his pensions and paid 40% tax. He has invested in a number of relatively high-risk ventures over the years, with mixed success. Some of his investments delivered a return of around 8%, but others have lost money. Overall, he does not think that he has made much money over the time he has been playing the markets with his pension money, but he has not lost much either.

When specifically probed about whether he has made back the 40% tax he paid back in 2015/6, at first Jimmy said that he did not think about that when making his assessment of whether his investment choices had been successful or not. On reflection, over the last seven years he admitted that he had nowhere near made a level of return to return his investment capital back to its pre-tax level.

Jimmy is now seriously, possibly terminally, ill and does not have the time or the energy to research investment opportunities as he once did. His money is now in a managed SIPP with medium risk. It is unlikely he will ever make back the money he has paid in tax. That said, he has enjoyed the thrill of investing and feels that having this pension money has opened up opportunities that he could otherwise not afford.

> It would have been boring to leave the pension where it was. I really enjoyed the experience. I've got no regrets.

> Since the awful Ukrainian situation, my stocks were hit drastically. They went up and down, and at my age, I don't want that. I got frightened by it. I'm not sure I want to be investing anymore. I don't think I want to be in charge of all our investments. So I took some money out of the market last year. So this is the first time in many years our money is in savings. And as we are taking money out the money in our drawdown is going to go down by the end of the year. And that's never happened before. So it's quite an eye-opener.
>
> **Male, 70+**

> Inflation's gone up a lot. As Julia Robert says in Pretty Woman, 'Bad mistake. Huge.' And with my sort of knowledge of investments and stuff like that, I should have done it. We can all look back on things in our lives, but I should have them index-linked.
>
> **Male, 70+**

6 The only certain things in life are death and taxes

Our original cohort of respondents is now seven years older than when we first spoke to them. The youngest is now 62, and the oldest is 73. They may be getting older, but their lives are still constantly changing. Grandchildren are now very much a feature of many lives, and some have taken on regular childcare responsibilities to help out their working children. A couple has divorced or separated since we last spoke to them. Plans to downsize have come to fruition, and a couple still have a dream to move abroad (although this has become more difficult with Brexit).

Sadly, we are starting to see the emergence of serious health conditions. A handful have different forms of cancer, and in two cases, this is moving into the terminal stage.

Full retirement rarely happened as expected

The winding-down phase is well and truly over for most, and many of our respondents are now enjoying full retirement. We again observed that the decision to fully retire is not driven by a calculated decision that they have enough money to last the rest of their lives, and finances are rarely the key driver for full retirement. Decisions are usually driven by factors such as reaching a specific age, their partner stopping work, or their health. Starting to get a State Pension is a key milestone.

> I had reduced my hours at 60 down to three working days because I started to get a small final salary pension. The State Pension didn't kick in till I was 66, but originally that would've been 60. So I reduced my hours. And then I had a couple of very bad falls. At 65, I fell and broke my arm and my shoulder. It was very nasty and it transpired that I now have osteoporosis and arthritis. Six months after the initial fall I fell again and had to have a hip replacement. I went to a stage three disciplinary for my sick leave and the stress was terrible. In the end, I just left.
>
> **Female, 65-69**

We had several cases where our respondents simply felt that they couldn't keep up with their job anymore or were simply getting fed up with the daily grind.

> I'd always said, 'as long as I'm enjoying work and I'm able to do it, I will carry on.' I started to find myself getting really irritated with customers, and getting very irritated with the management at work. I just kept finding myself saying, 'I'm too old for all this, you know?' And I thought, do you know what, maybe now is the time to retire. And everyone said, 'you'll know when it's the right time.' And I did. And I don't regret it one bit.
>
> **Female, 65-69**

> I was thinking about retiring, but it was kind of forced on me because the company was in trouble at that point after Covid and they weren't going to survive it. I won't work again. As soon as you give your age, you are kind of over the hill a bit for anything really. And I can't think what I could do. And my mobility isn't fantastic these days.
>
> **Female, 65-69**

A couple are still enjoying 'hobby' work to keep active and to earn a bit of extra money, but the majority are now living off the assets they have accumulated over their working lives.

Each stage of our study has explored the age at which our respondents expected to fully retire. Looking back over their plans versus reality, we see that plans have rarely panned out in practice, and few had a 'traditional retirement' where they left a full-time job at 65 to stop working completely.

Cognitive decline is kicking in

For the first time, we asked our older respondents (mid-60s and beyond) about their mental capacity. They are starting to recognise that they are not as sharp as they used to be, and they report that this cognitive decline is manifesting in several ways. It seems to take them longer to digest information and make important decisions. They are less adventurous and less open to change. They seem to be more worried about things that previously would not have bothered them.

A couple of our 'Hobby Horse' investor respondents, who had for many years enjoyed following the stock markets and doing their own investment portfolios, have now given this up. They were a little spooked by the recent market volatility as they felt they had less time to make up any losses, but they also found it more and more difficult to keep track of the market news and generally did not find it as much "fun" to do their research as they used to.

> I do find myself slightly less enthusiastic than I was. I don't think I'm as sharp as I was. I don't think I'm quite on the ball. I forget things sometimes, you know, or maybe I'm not addressing them because they're uncomfortable.
>
> **Male, 70+**

The tax regime, rather than need, is a key determinant of drawdown withdrawal rates for those bridging to State Pension

Managing pension money around income tax rules rather than need appears to be a common behaviour. Respondents were understandably keen to keep their tax bills to a minimum, and they very much begrudge paying income tax on their pensions and savings.

> I hate the whole principle of paying tax on your savings. It's just totally wrong to me. Why should we pay tax on saving money when we've already paid tax on our earnings.
>
> **Male, 65-69**

Our bridging respondents (ie, those who have stopped working or reduced their hours and are using their DC pension as an income bridge until State Pension age) often took annual withdrawals to keep themselves just below the income tax threshold. Tax thresholds are well understood, and so they are comfortable doing this without advice.

They appeared to like round numbers, and so we noted a clustering of withdrawal rates at £10,000. Depending on the pot size, this will either deplete the pension or they will switch off the withdrawals just as the State Pension kicks in. Withdrawing a broadly equivalent amount to the State Pension also meant that they would have a steady income to manage. Before the cost of living crisis, £10,000 may have been a bit more money than they actually needed, and the rest ended up in a savings account. Today, they are finding it a bit more challenging to make ends meet, and there is rarely anything left over for a rainy day.

Awareness of the tax rules at 75 is poor - and the silence from providers is deafening

According to the FCA's Retirement Income data, around a quarter of those in drawdown are aged over 65, and in 2021-22, around 260,000 over 65s were taking regular payments from their drawdown policy.

Fourteen of our drawdown respondents are now in their late 60s and early 70s, and health issues are starting to appear. Now that they are approaching the milestone birthday when the tax rules on death change, we wanted to explore their awareness of the tax rules around age 75 for a couple of reasons. First, some had significant pots left as they had been managing quite well on their State Pension and household DB provision, so any 'mistakes' could be significant for their beneficiaries. Second, we were mindful that serious health issues are emerging and that these particular tax rules may become very pertinent for them and their loved ones.

As we expected, most were aware that pensions pass on tax-free to those aged 75 and under, but knowledge of the post-75 rules was quite hazy. Furthermore, even the most savvy respondents who knew that post-75 their pensions would be subject to their beneficiaries' marginal rate of tax were completely ignorant that this could lead to their loved ones facing a 40% tax bill - both on the pension income they receive and also on their earned income.

This situation arises when the provider does not have a 'beneficiary drawdown facility' and is therefore only able to pay the money on death as a lump sum. Some providers have beneficiary drawdown facilities that allow loved ones to manage their tax liabilities, but some do not. The situation gets murkier as the ability to access beneficiary drawdown may also depend on what type of product you have, even within a provider. Drawdown members are therefore currently running the risk of landing their nearest and dearest with a nasty surprise and a much-reduced pot; a sorry situation that could be easily resolved by simply switching products and/or providers.

Needless to say, our drawdown respondents had no idea that this was even an issue and were completely clueless about exactly what their provider offered. Not one of our drawdown respondents had had any communication about this from their provider, even those approaching 75. They had not read anything about it in the 'wake up' literature, and it did not feature in any conversations with Pension Wise. They felt angry that this had not been brought to their attention and felt that this is just one more example of where pensions are seen to be a 'minefield', fraught with complex rules designed to trip up the unwary novice.

While this is currently an issue for those in drawdown who are approaching or already age 75, the recent changes to the lifetime allowance may threaten the tax-free status of inherited DC pots for those passing away before age 75, widening the scope of the issue.

On a positive note, our conversation about the rules prompted some respondents to go away and nominate their beneficiaries. Again, this might have been mentioned by providers when they took out their TFC, but they could not recall being contacted again to make sure their affairs were in order as they got older.

> I'm a bit less interested than I was, but I do keep up with sort of financial things and I hadn't come across that. Let alone people who are not in the slightest bit interested, how would they hear about it? Unless they heard it on a radio programme or a TV programme or something like that or online, you know? I think everybody should be advised of the situation. But then it's not really in their interest because they'll collect more tax if people don't know.
>
> **Male, 70+**

> My mother died last year. She was 92. She'd had a really good life. But I've been doing her will and the executor's job and probate and it brought it home to me about amounts of my money that were sloshing around that I didn't have any idea where they were going to go if the bus got me tomorrow. I've got quite a big chunk in my pension pot and I'm not quite sure how that would work. I need to follow this up.
>
> **Female, 65-69**

Bequest motive strengthens as awareness of their own mortality increases

We are mindful that many of the guided retirement income products in the pipeline will feature some form of annuitisation to ensure that income can last for life. Some of our respondents in drawdown are in their late 60s and early 70s and are therefore rapidly approaching the age at which they would need to choose whether to annuitise their remaining DC pension money or not. We wanted to test how they would feel about making this decision.

Our first observation is that getting older does not weaken the bequest motive. If respondents disliked annuities when they were in their late 50s and early 60s because the money died with them, this view has not changed over time. Now that they are experiencing friends and family members of a similar age, or slightly older, passing away, they are even more reluctant for their hard-earned money to pay for someone else's pension.

Second, now that they are older, they worry more, not less, about their ability to live long enough to get their money back. Annuities are still not seen as a good deal, and this shorter 'payback' period is seen as a negative, not a positive.

Our respondents are looking at the next stages of their lives and thinking that their big spending days are over. If the triple lock continues to ensure that State Pension covers the same basic living standards as it does today, then living off the State Pension (possibly with a bit of additional DB income) seems quite manageable. If the trade-off they have to make is money left for their family versus additional (marginal) income security over and above the State Pension, then more often than not they are happy to take the risk and keep their DC pension money. Of course, those who were not fortunate enough to have any DB in the household and those with wealthier or no children were more circumspect.

Finally, they feel that life could still change dramatically for them, especially concerning their health, and therefore the flexibility to take all of their remaining DC pot if they need it is more important than ever.

We are mindful that this is a very small sample and may not be representative of the population. Further research will be needed to explore these potential behavioural barriers in greater depth. Nevertheless, our findings indicate that there may be a challenge ahead, as it is by no means certain that all DC pension holders in their 70s will want to annuitise when the time comes. Providers will need to think carefully about the choice of architecture embedded into future guided retirement income plans.

> Annuities are a bit limited. You can never draw from it, and at the end, if there's any money left or anything, it just disappears into the ether.
>
> **Male, 65-69**

> I know my parents did it, and it was an absolute disaster, so I'm sort of steered away from those. I feel like the control's been taken away. I feel somebody else is controlling it because once you're tied in, you're tied in, aren't you, with an annuity? If it came to that and I was running out of money, I'd sell the property and get something smaller.
>
> **Female, 65-69**

> You're gambling on your future health as well, aren't you? You don't know what's going to happen. It might sound good now, but how would it sound in a year or two's time? And you're committed to it once you signed up to it.
>
> **Male, 65-69**

> In some ways it's safe, isn't it? But then again, things do change at times and you probably need to adapt. You might need more money or less money.
>
> **Male, 65-69**

7 The 'Great Retirement': Exploring the path back to work

Much press attention has been paid to the UK's 'Great Retirement' problem. For example, research by the Institute for Fiscal Studies (IFS) highlighted that there has been a significant increase in the over-50s leaving the workforce due to retirement and that these people tended to be relatively well-off[6]. However, new data from the October – December 2022 Labour Force Survey show signs of a possible reversal. Using this data, the IFS[7] confirmed that there has been an uptick in those returning to work amongst the over-50s who had been out of work for less than three years – that is, they had left the workforce after the pandemic began.

In light of this positive development, we wanted to explore this in a little more detail to try to understand what the drivers of this behaviour are. We were particularly keen to see to what extent pension freedoms and the ability to access DC money without annuitisation had on decisions to exit the labour market and what, if any, lessons we could learn from those who had then decided to return to work due to the pressure of rising living costs.

We spoke to 15 people in total about their reasons for leaving and their experiences of rejoining the over-50s labour market.

[6] https://ifs.org.uk/articles/worsening-health-leading-more-older-workers-quitting-work-driving-rates-economices-economic
[7] https://ifs.org.uk/articles/new-data-show-signs-over-50s-returning-workforce

Covid gave the over-50s a chance to reflect and look at life differently.

Figure 5: Reasons for the over-50s fully retiring

- Fed up with working (physical or mental stress)
- Reaching a specific age (eg, SPA, DB entitlement or 60 for WASPI women)
- Partner retiring
- Ill-health or caring responsibilities
- Changes to their working environment. Lack of flexible hours
- Mortgage paid off (often using tax-free cash (TFC) or other significant reduction in outgoings (eg, children leaving home)
- Redundancy. Firms closed or taken over after Covid

As Figure 4 shows, there were a myriad of reasons why our re-joiners left their jobs. However, for the majority, the availability of a pension (DB or DC) played a pivotal role in their retirement choices; without it, many would likely have continued work. Notably, receiving wake-up letters at 55 often sparked contemplation of early retirement. Using their tax-free cash to pay off or pay down any remaining mortgage 'allowed' them to think about giving up work.

Our re-joiners approached retirement planning differently. A couple diligently crafted detailed financial plans using budgeting tools and spreadsheets, but the majority had a more approximate estimate of their basic expenses, typically around £20,000. Despite living through periods of high inflation and high interest rates, they did not build any buffer into their affordability calculations. Again, our re-joiners were keen to minimise their income tax bill and so started to take around £10,000 to keep them under the tax threshold. Many were in a household with a working partner, and they had calculated that this would be enough to cover their share of "the basics".

Everyone has felt, to varying degrees, the impact of rising living costs. As a result, some of our re-joiners found themselves falling short by a few hundred pounds a week and needing an additional income stream to maintain their financial stability in the face of these growing expenses.

Most were taking top-up money from their savings accounts, which worried them as these were the funds they had mentally set aside for emergencies and holidays. The minority who took extra from their drawdown started to get twitchy about their money running out in later life.

Most initially revelled in the freedom that came with leaving the daily grind behind, delighted to finally have the time to pursue their own interests. However, for a small subset of individuals, the absence of a structured routine or reduced social interaction becomes a source of concern. Around 6 months into retirement, the novelty of indulging in their newfound freedom waned. For these people, the additional income from working was a welcome benefit as things got more expensive, but it was not the main driver for going back to work.

Re-joiners feeling the financial squeeze were reluctant to increase pension withdrawals or to see their savings dwindle further

Figure 6: Reasons why the over-50s returned to work

- **Need the income to live off** (due to extra living costs)
- **Worried about pension or savings**
- **Enjoy working and want some social interaction**
- **Want some income for 'treats'** (ie be able to afford 'luxuries' like travel, meals out, socialising, etc.

Laura

Gender: Female
Age bracket: 60-64
Working status: Working part time & winding down
Cohort: Re-joiner
Pension decision: Taken TFC & made further withdrawals

Their situation

Laura was working for a charity while going through a messy divorce. She was good at her job, but a change in management meant that she was no longer given the responsibility she was used to. She moved to a new area and felt that 58 was the right time for her to retire to be able to settle into her new life.

She had a DC pension as part of the divorce settlement. She has a financial adviser who talked her through the amounts she should be withdrawing. She has not changed the amount she is withdrawing due to the rising cost of living and has tried to cut back on spending instead.

However, a few years ago, she saw the pension go down a lot in value, and this was a shock. She was worried about whether it would now last as long as she was told, especially if the war in Ukraine went on for a long time. She was so worried that she didn't look at the value of her pension for a year.

She decided to go back to work to boost her savings. Her daughter mentioned that their local school was looking for exam invigilators, which she has now done for the past couple of years. The money helps, but she really enjoys the work, and it gives her a huge sense of self–worth.

> My pension went down, and it really gave me a shock. And I thought, my God, if it continues like this, you know, what is going to happen in two years or three years? So that really made me look at what I had and almost become even more frugal. With the Ukraine situation, that's when I decided to do a little bit of work. And I absolutely love it. I wish, in a way, I'd done it before because, not at that time for the money, but because I really enjoy what I do. And I love the schools, and I love the people who are in them. I'm doing something that I feel is very fulfilling. Having come out of a very difficult marriage, to feel valued and to feel not invisible is important.

My way or the highway

Looking at what they did next gives useful clues as to how the over-50s might want to participate in the labour market in the future. The message came through loud and clear: even though many were feeling the pinch, they did not want to go back to business as usual and would only return to work on their terms. So what did this mean in practice?

Our re-joiners still looked for a sense of value and structure in their work, but the types of jobs they wanted were very different from their previous working lives. Typically, their roles now involve low stress and can be characterised as "little jobs" that serve as a means to top up their income or provide extra spending money.

Our re-joiners preferred to seek employment opportunities within their local community to avoid lengthy commutes. They got used to being at home during Covid, and their period of retirement reinforced the desire to avoid the misery and expense of the daily grind to and from work.

Flexibility is also a key consideration, and they looked for working hours that suited their lifestyle rather than adhering to a strict 9-to-5 schedule. Knowing that they can step away whenever they wish, take breaks for travel, or fulfil caregiving responsibilities is an important motivation. For some, retirement feels more challenging in the winter, and so they prefer seasonal or temporary work to top up the coffers and fill their time during the dark months when travel and gardening are not possible.

What next?

Plans to continue working often extend out for a few years, with key crunch points being the age at which their partner retires or the age at which their State Pension kicks in.

Once more, the additional income from the State Pension will alter their tax circumstances, a factor they believe will significantly impact their decision to give up working. The additional £10,000 plus DC and any additional DB pensions will bring their estimated annual income to approximately £20,000 to £25,000. This income level closely resembles what they were accustomed to while employed, as they previously held modestly compensated positions, and they are familiar with maintaining their lifestyle with this level of income.

Most cannot see themselves working beyond 70.

Damian

Gender: Male
Age bracket: 65-69
Working status: Was working part time & is now winding down
Cohort: Re-joiner
Pension decision: DB pension

Their situation

Damian had been working as a lorry driver all his working life. He was made redundant in 2000 after taking some time off work due to illness. The firm subsequently went into administration.

Damian took out a pension in the 1970s and paid in for a short while. By the time it came to receiving the income, he couldn't believe how much it was from such a small 'investment'. He currently gets £8,000 a year, and he is already getting his state pension. He owns his flat outright and lives on his own. He doesn't go out for meals very often, preferring to walk in the countryside. He can just about live on this money and has some savings for the "little luxuries" like going on holiday or emergencies.

The cost of living crisis put up energy bills and food, but as the State Pension and his DB pension have some inflation protection and he gets the Winter Fuel allowance from the government he has been managing.

After he had been fully retired for a while, especially after lockdown, he decided that he was bored at home every day and subsequently signed up for agency work as a lorry driver. He confesses to being "very fussy" about the work he will take on. He thinks that he can only carry on for another year or so until he is 70, as he is unlikely to be able to pass a medical at that stage, and the costs to retain his licence get very expensive. He thinks that at that point he will fully give up work.

"I ring them up and say, 'Right, my availability this week is Monday, Tuesday,' and I say 'I have granddad duties on a Thursday and Friday,' so I don't put myself available then. And that's it. I'm picky in what I do. I don't do nights out and I don't do the long distances. I won't do multi multi-drops like your Amazon Prime drivers, who do hundreds of drops a day and things like that. I won't tolerate things like that. I won't do it at all."

8 Mind the support gap: the forgotten generation?

The key finding from our initial wave, some 7 years ago, was the decoupling of the 'New Choice' (accessing tax-free cash without annuitising the rest of their pot) and the 'Big Decision' (what to do with the remaining 75% of their pot). At the time, they followed the path of least resistance into drawdown with their existing provider rather than actively choosing it.

Out of sight, out of mind

Seven years later, our drawdown respondents are still in a state of disengagement when it comes to managing their financial future. They have not conducted any further research and are no more aware of their investment options, the tax implications, optimal withdrawal rates, or other financial aspects than they were 7 years ago. Instead, they are thankful that the decision has been made and that they don't have to think about these complex issues anymore. Except perhaps for inflation, they are no better informed today of the plethora of risks they face than they were back then.

They have not ventured onto their drawdown provider's website, nor do they feel compelled to seek out information or updates regarding their accounts. They recall receiving annual statements, but this feels transactional and is often ignored - except for the headline figure of what their pot is worth. They find themselves in a state of financial complacency, often unaware of the costs and charges associated with their drawdown product and whether it remains competitive within the market. This lack of clarity is compounded by the absence of readily available resources to check and compare their plan against others.

They have not been triggered by any notifications or communications from their provider to think about whether the plans they had 7 years ago are still valid today, whether their withdrawal rates are sustainable, drivers, to consider the suitability of their investment choices.

Without the motivation to shop around or periodically review their investment objectives, our drawdown gang is simply letting their pension pot take its course without making informed decisions.

Half a million pensioners face a tax trap

The number of over-65s paying income tax rose by 390,000 between 2022 and 2023[8]. LCP (Lane Clark & Peacock LLP) estimates suggest that around half a million over 65s will fall into income tax following the increase in State Pension next April.

[8] https://www.moneymarketing.co.uk/news/half-a-million-pensioners-face-income-tax-trap/

Although we have observed our respondents planning withdrawals around the tax regime, we also note that they are making basic errors. Occasionally, respondents were taking taxable funds from drawdown while tax-free cash remained available in another pot. Others found themselves paying income tax on their pensions for the first time as savings rates increased, pushing them over the threshold.

As the value of the State Pension edges ever closer to the frozen personal tax threshold, helping the over-55s understand how to optimise their tax situation becomes ever more important.

Time to rethink annuities?

Historically, our drawdown gang viewed annuities as poor value for money and felt that the long payback period was too much of a risk for them to take. They harked back to the halcyon days when rates were touching double-digits and trotted out the mainstream media rhetoric that annuities are generally a rip-off.

However, annuity rates have increased by 20% in the twelve months to June 2023, with a total increase of 48% since the start of 2022 for a 65-year-old, according to new research from Standard Life[9]. Our drawdown respondents were woefully unaware of this recent uptick in annuity rates and the impact that this could have on their lifetime income.

They do not follow annuity rates themselves and felt that their ignorance has been compounded by a notable absence of proactive information from both financial providers and financial advisors regarding the advantages of locking into these higher annuity rates while interest rates remain high. Furthermore, the idea of partial annuitisation and the advantages of securing a portion of their savings through annuities have often escaped their consideration. Their mindset is that they have chosen drawdown, and they will need a strong intervention to open their eyes to alternative paths.

It is particularly striking that a significant portion of our gang has underlying health conditions – some serious - and yet there remains a general lack of awareness about the availability of enhanced annuity rates.

The advice market is not always delivering what our drawdown respondents need

A small number of respondents have ongoing relationships with financial advisers. Some, but not all, are having yearly meetings with their advisers but the quality of these interactions varies. We heard of instances where our respondents received limited ongoing financial planning from their advisers. Despite the markedly different market conditions drawdown cases now find themselves in, most of our advised respondents felt that their adviser had not engaged them in detailed conversations about budgeting and withdrawal strategies. Most are unaware of and do not use cash flow modelling tools.

Some of our 'Help Me Helens' in particular felt that their relationship with their financial advisers was pretty transactional. But they felt stuck as they did not want to take control of their plan – not really knowing where else to go to switch to – and not wanting to take control of their investments.

[9] https://www.standardlife.co.uk/about/press-releases/standard-life-annuity-rate-tracker

Amy

Gender: Female
Age bracket: 60-65
Working status: Was fully retired, now working part time
Cohort: Original cohort
Pension decision: Taken TFC

Their situation

Amy's husband took a DB to DC transfer with the help of an IFA. She has a smaller DC pension, has taken out her TFC to pay for improvements to the house, and has been helping our her children get onto the property ladder. They wanted to take the DB to DC transfer so that she could have the whole pot if he died, and their children could have whatever was left.

They have had an ongoing relationship with her IFA for some time. She is aware that she is paying a fee, but they are happy to do so as it gives them security and peace of mind. Once she had been made aware that the fees could be in the region of £3000-£6,000 (0.5-1% of the pot), she was less sure.

She felt that she might want to do something different but was worried about taking on the investments themselves.

> "If I was managing it myself, I'd be questioning so much. My husband would probably have more idea than me, but then I would be saying to him, 'Oh, are you sure you we're doing the right thing?' Where if you've got sort of somebody who's a professional, we do feel we're happy with it, you know?"

9 Conclusions

The importance of the State Pension remains as crucial today as it has ever been, and its purpose is clear to our respondents. It provides a solid foundation for the essentials, with their private pensions serving as a supplementary resource for the 'nice things' in life.

The evidence from our study suggests that the triple lock has been fulfilling its purpose of dragging pensioners further up the income distribution. Particularly fortunate are those households that also have access to some defined benefit (DB) pensions in addition to their defined contribution (DC) pots. When coupled with two adults receiving full state pensions, this combination can offer a reasonably comfortable and secure lifestyle in retirement.

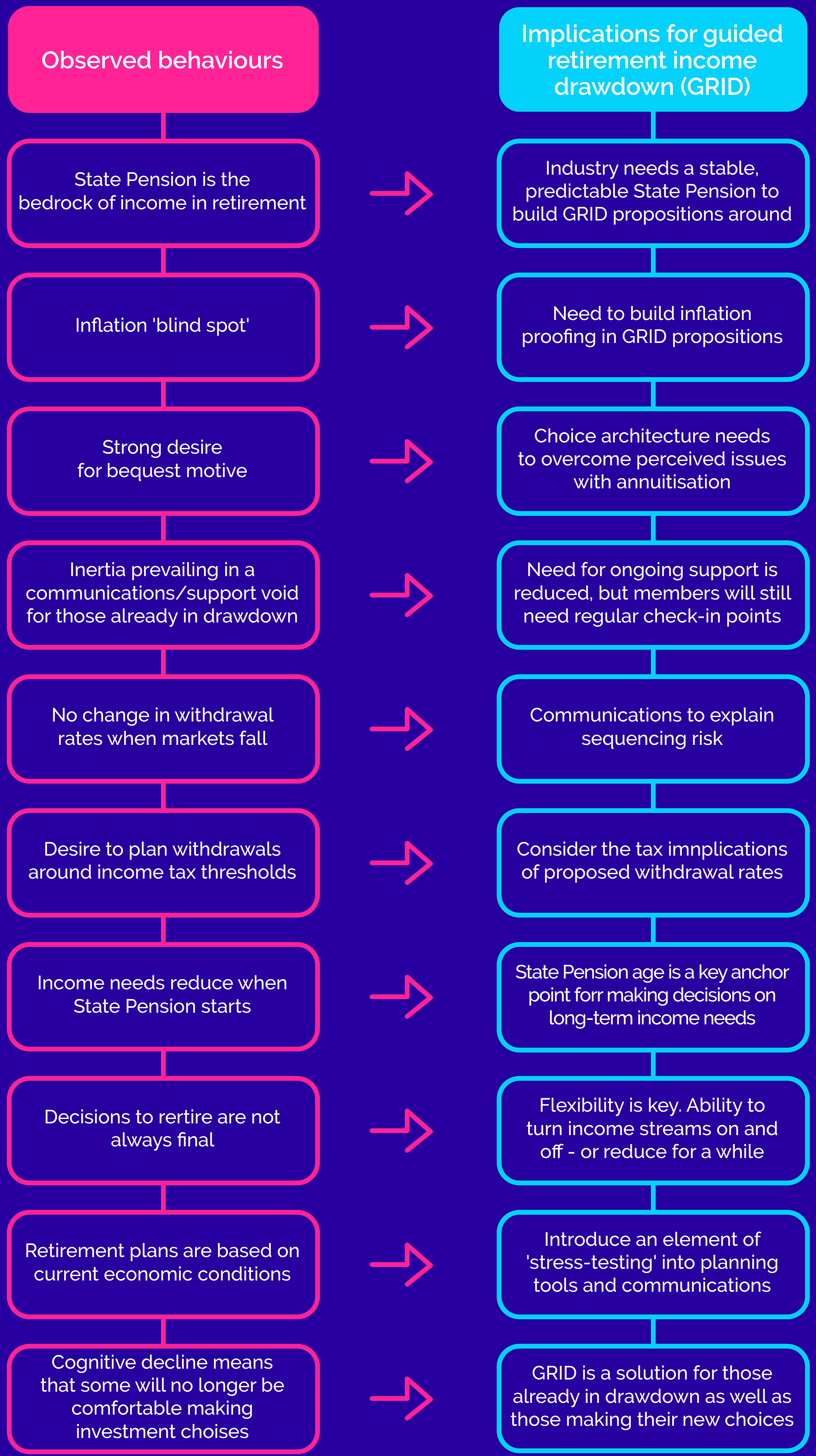
In recent times, the triple lock has also provided a safeguard against inflation for a substantial portion of our retirees' household income. This is hugely important, as, left to their own devices, our respondents did not consider inflation when making their income decisions, even though they had lived experience of its impact. To ensure future pensioners are protected against the ravages of rapidly rising costs, some form of stress testing should be a fundamental component of retirement affordability planning, mirroring its importance in mortgage decisions. This should be incorporated into the planning tools offered by financial service providers, and providers will also need to strengthen the messages in their information and education resources.

Yet the future of the triple lock remains uncertain, and this safeguard is under constant threat. This is a concern for both current and future pensioners. According to the Pension Policy Institute (PPI)[10], at its current rates, auto enrolment will deliver the Pensions and Lifetime Association's (PLSA) definition of a comfortable retirement for just 4 years to those currently aged 22 and on median earnings, or they could have the basic level of retirement for 12 years. Putting State Pension provision on a sound footing is vital to ensuring that the gains of today continue and we do not create a new generation of pensioners in poverty, despite saving all of their working lives.

As the DC retirement landscape gradually transitions from a retail, 'Do It Myself' approach to a more institutional "Do it For Me' model (where default, guided income retirement plans are the norm), there are some important lessons to learn from our ongoing study, which can help inform plan design.

[10] https://corporate-adviser.com/young-workers-face-bleak-pension-prospects-despite-ae-reforms-ppi/

Figure 7: Key Lessons for Guided Income Retirement



Firstly, people typically do not learn from the past. Left to make financial decisions independently, behavioural biases tend to create an inflation "blind spot" in their retirement planning, which means that even those from a generation that vividly remembers interest rates at 15% and decades-long double-digit inflation opt for fixed-rate annuities and build their retirement strategies around the assumption that the economic conditions of the last few years will persist indefinitely. Guided retirement solutions will need to bake in some form of early-years' inflation-proofing.

Secondly, people do not recognise the risks they face in retirement and plan accordingly. They are particularly oblivious to sequencing risk in falling markets.

Finally, our study has also yielded intriguing insights into the decisions that individuals in a "Do it For Me" environment will face in later life. We have observed that the natural tendency to become more cautious and risk-averse as people age may not be enough to counteract the strong desire to leave their pot of money to loved ones. In addition, as annuitisation at 70 or 75 will probably need to be an active decision taken by the member around that age, the length of the 'payback period' -the number of years it takes to get their pot of money back in income payments - will be critical to take-up rates. If our respondents are representative of the broader population, this will need to be 10 years or less. Choice architecture will therefore need to counterbalance the strength of the bequest motive, and some form of 'money-back guarantee' may well be needed.

There is a noticeable paradigm shift in working patterns that is currently unfolding, which has worrying implications for future DC pots, especially as AE at its current levels will not deliver a comfortable income in retirement. According to the latest data from the Office for National Statistics (ONS), approximately one-quarter of individuals over the age of 50, totaling 3.6 million people, are now engaged in part-time employment. What's particularly striking is that the over-50 demographic represents a substantial 42% of all part-time workers. Moreover, there is a significant propensity for individuals to transition to part-time work as they grow older. For instance, 40% of workers in the 60-64 age group are now working part-time, and this proportion increases even further to 66% among workers aged over 65. This shift in employment patterns among older individuals reflects a noteworthy trend in the labour market. If our respondents are representative of the population, there are several key implications:

- The ability to access DC money at 55 is an important driver for going part-time or leaving the workforce completely.
- Job flexibility is key to getting the over-50s back into the workforce, but they are unlikely to return to a job at the same level and will be seeking to protect their pot or savings from depletion rather than looking to build on their funds.
- DC pots are forming a bridge to the State Pension age.

Retirement planning is an evolving process over many years that is likely to necessitate adjustments as circumstances change. Seeking guidance periodically can be invaluable for retirees, enabling them to make well-informed decisions, optimise their pension funds, and maintain financial security throughout their retirement years. However, there is currently a concerning lack of attention given to the 1.1 million pension pots already in drawdown.

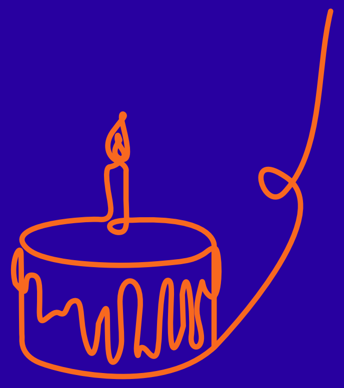
The Financial Conduct Authority's (FCA) new Consumer Duty requirements could potentially help address the existing imbalance between the 'New Choices' and the 'Big Decisions'. Nevertheless, as the number of individuals relying on the state pension and drawdown arrangements continues to grow, it will become increasingly important for financial service providers to enhance their communication and intervention efforts for this group. A vital starting point is ensuring that individuals do not incur unnecessary financial losses due to ignorance of the complexities within the income tax system.

10 Appendix - Sample

In this Wave, we spoke to 50 respondents, 35 from our original cohort and 15 new respondents.

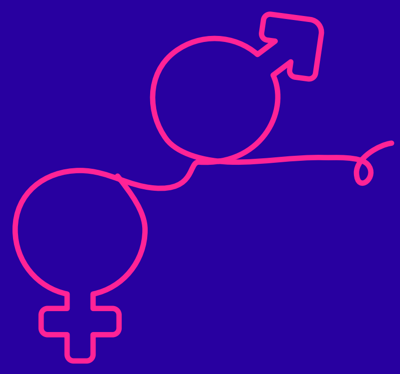
Age breakdown by type of respondent:

	All respondents	55-59	60-64	65-69	70+
All respondents	50	8	18	18	6
Repeat respondents	35	1	13	15	6
New respondents	15	7	5	3	N/A



Gender breakdown by type of repondent:

	All respondents	Gender	
		Female	Male
All respondents	50	31	19
Repeat respondents	35	23	12
New respondents	15	8	7



Working status breakdown by type of respondent:

	All respondents	Working status			
		Working 'as usual'	Winding down	Semi-retired	Fully retired
All respondents	50	15	7	6	22
Repeat respondents	35	3	0	7	25
New respondents	15	0	0	15	15

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