



# UK Sustainable retirement solutions

Update from the IFoA Defined Ambition research working party

arise  
mentorship  
Thought leadership  
Progress  
Community  
Sessional Meetings  
Education  
Working parties  
Volunteering  
Research  
Shaping the future  
Networking  
Professional support  
Enterprise and risk  
Learned society  
Opportunity  
International profile  
Journals  
Support-

## Motivation

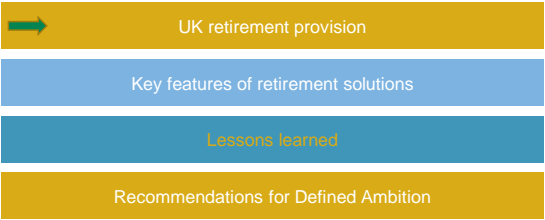
- Retirement income a key area of public interest
- Significant shift in how UK retirement income is provided
- Some sectors of the population face significant risks
- Actuarial profession should address the problem



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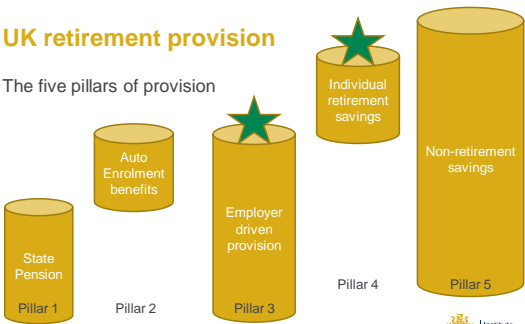
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## Agenda



## UK retirement provision

The five pillars of provision



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All change: Budget 2014



Individual groupings

- Cross subsidies an inherent feature of retirement provision
- Risk pooling/sharing key aspect of actuarial science
- Risk sharing evident even within DC

	Age 30	Age 45	Age 60
Income £10k pa			
Income £30k pa			
Income £100k pa			

Pillar 1 – Flat Rate State Pension (£7,488pa)

Replacement ratio	Age 30	Age 45	Age 60
Income £10k pa	75%	75%	75%
Income £30k pa	25%	25%	25%
Income £100k pa	7½%	7½%	7½%

- Political risk decreases with age (change in policy)
- Political risk decreases with lower incomes (means testing)

Pillar 2 – Auto enrolment benefits

Replacement ratio	Age 30	Age 45	Age 60
Income £10k pa	75% pillar 1 85% pillars 1+2	75% pillar 1 79% pillars 1+2	75% pillar 1 76% pillars 1+2
Income £30k pa	25% pillar 1 44% pillars 1+2	25% pillar 1 33% pillars 1+2	25% pillar 1 26% pillars 1+2
Income £100k pa	7.5% pillar 1 16% pillars 1+2	7.5% pillar 1 11% pillars 1+2	7.5% pillar 1 8% pillars 1+2

- Steady State (DC) auto enrolment contributions assumed
- Implications for future changes to auto enrolment rates
- Retirement at age 65

Pillar 5 – Non retirement savings

- Average house price: £175,000 (c £7,500 pa)
- Inheritance – healthcare
- Underestimating the cost of saving for retirement
- Ease of access – it often rains

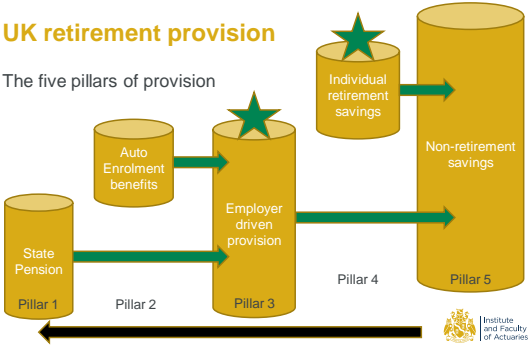


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UK retirement provision

The five pillars of provision



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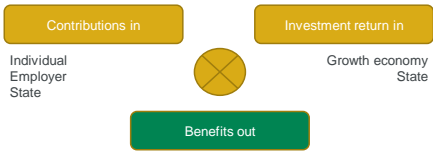
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Agenda

UK retirement provision
➔ Key features of retirement solutions
Lessons learned
Recommendations for Defined Ambition



Key features of retirement solutions

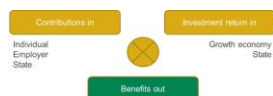


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## Key features of retirement solutions

- Risk pooling / smoothing
- DB generational / DC semi-generational
- Improvements for one group are at expense of another
- Social – the only neighbour without a swimming pool
- Society – standard of living in different geographies



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## Pillar 4 – Individual retirement savings

- US model of self reliance
- Financial education
- Certainty and security over commitments
- Incentive – including tax efficiency for high earners
- Allocation between retirement and non-retirement savings



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## Overview of modelling rationale

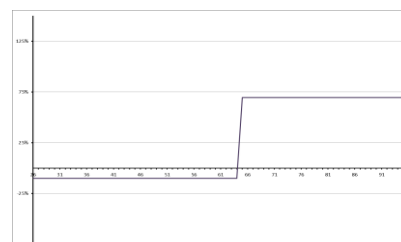
- Explore fundamentals of what these wealth sharing vehicles deliver to all stakeholders
- Evaluate efficiencies resulting from mechanism decisions:
  - Funding
  - Investment
  - Reduce contributions and/or benefits
  - Split member/sponsor



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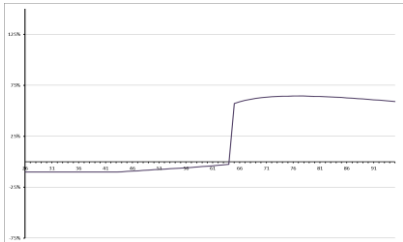
## Net cashflows – complete market, 'perfect' world



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Net cashflows – ‘prudent’ assumptions



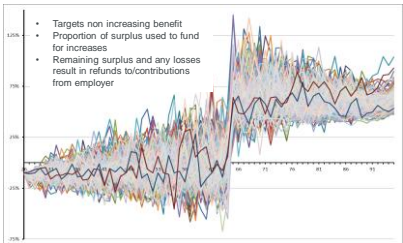
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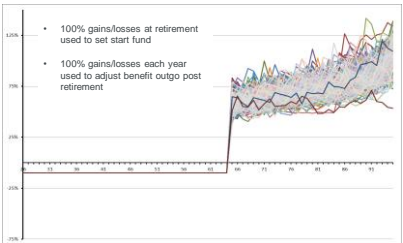
DB type vehicle



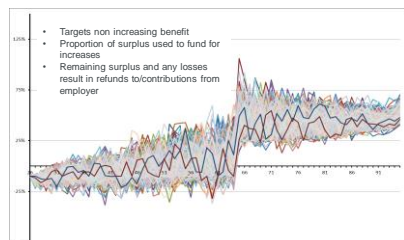
DB-lite type vehicle



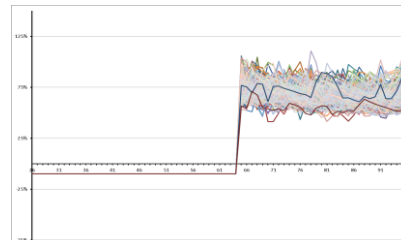
CDC-type vehicle



### DB-lite type vehicle on a more prudent funding basis



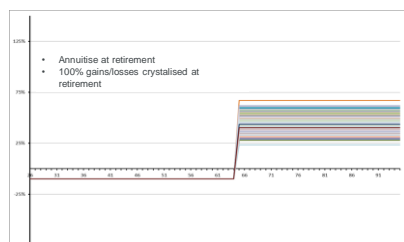
### CDC funded on an more optimistic basis



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### DC type vehicle – pre Budget!



### Refinements to the model – different types of member

- Outputs by member
  - Income during retirement (distribution)
  - Stage of lifecycle
- Funding decisions
- Investment decisions – in particular the de-cumulation period
- Alternative economic scenario models
- Stochastic decrement modelling

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## Lessons learned ...

- Past UK pitfalls
- International trends
- New retirement savings landscape
  - Enabling a market
  - Overcoming barriers (enabling regulations, employer appetite?)
  - Dust to settle on Budget 2014 (Where does DA fit in the brave new liberalised world of pensions?)

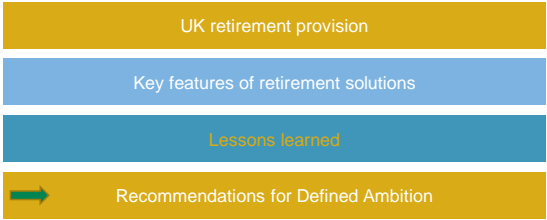
## International trends

- State benefits redesigned to tackle declining 'support ratio'
  - Link to longevity improvements
  - Incentivise deferred retirement
  - UK support ratio may not fall as sharply as some other countries (fertility, migration)
- General shift to DC/ self reliance model
  - US, Australian superannuation
- CDC/ Pension income builder plans
  - Dutch and Danish experiences
  - Social contract important

## New retirement savings landscape



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Recommendations for Defined Ambition

- How the situation may evolve
  - How different vehicles distribute wealth
  - Economy
  - Lessons on release valves
- Who picks up the risk sharing – the State?
- What if the State gains?
- Engagement from employers



Recommendations for Defined Ambition

- Flexibility to change benefit structure
- Appropriate funding/investment framework
- Risk sharing mechanism separate from government
  - Non-governmental regulator?
- The role of actuaries in shaping DC?



Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

