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INTERACTIVE

viewpoint

Keeping you connected to today's UK financial services market

Welcome to the seventh edition of *viewpoint*, Harris Interactive's UK financial services newsletter.

For this edition we explore how we think the forthcoming pension reforms are going to impact the working population.

We look at why these reforms are needed, the anticipated success of the reforms and the challenges the reforms face.

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Pension Auto Enrolment is just around the corner!

Auto enrolment is on its way from the 1st Oct 2012. Over a period of time it is estimated that more than 10 million people will be enrolled into a new workplace pension.[1]

If you are aged between 22 - 64 years old in employment, currently earning over £8,105pa and not presently in a company pension, you will be auto enrolled into a pension in the near future.

The Government wants everybody to take responsibility for saving for their own retirement and our research[2] shows that the majority (55%) of the UK population agrees with this sentiment.

Over the next few years (by 2017) every working person within the above criteria will have the ability to join a pension and the individual will have to opt out of a pension if they feel this is not the right savings medium for them.

This has to be a good thing for people of all ages; helping them save for their retirement by providing a platform to save and continue to save throughout their working career – hasn't it?

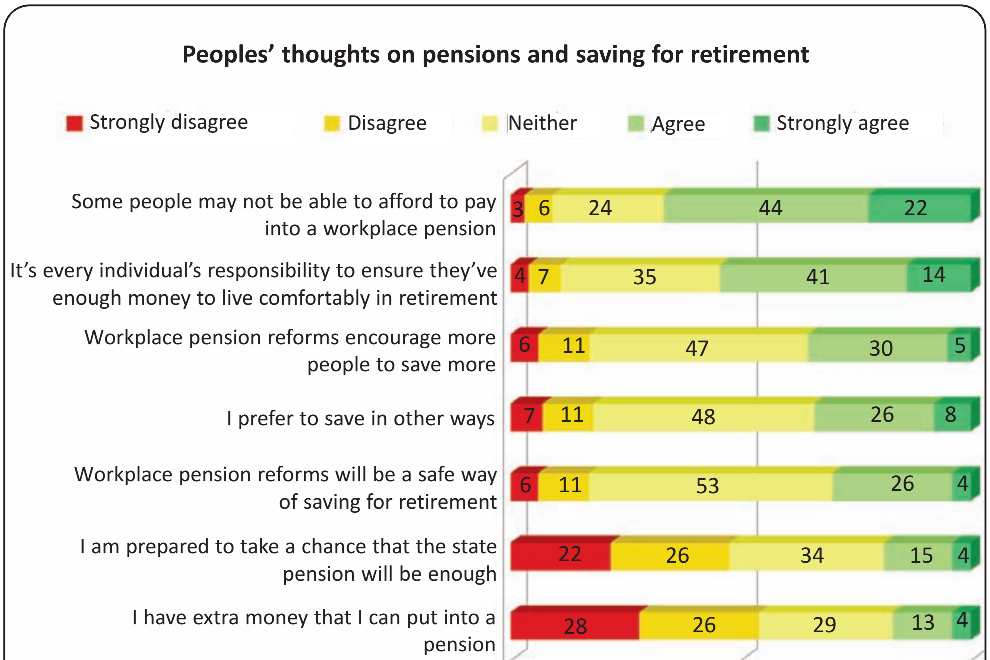

Chart 1

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- Retirement pipe dream
- No such thing as a free lunch
- The cost of a crisis

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Why is Reform Needed?

The population is living for longer

As the baby boomer generation grow older, the number of people retiring increases at a faster rate which is borne out by 22% more people reaching retirement this year compared with last. With an increasing number of people retiring over the next 25 years the size of the problem is only going to escalate. For the first time this year, those over 65 are set to become a greater proportion of the UK population when compared to the under 16's, bringing the number of retired people to 11.8 million.[3]

It is also known that 1.2 million pensioners have no income other than the state retirement pension and state benefits.[4] If this trend continues it will mean that there are increasing numbers of retirees in the UK having to solely rely on government handouts, which we simply cannot afford.

Funding retirement is not top of mind

For many, funding their retirement does not figure highly in peoples' minds until it is too late. Twice as many people think on a regular basis about socialising and going out (37%) rather than funding their retirement (18%). In fact our research shows only 10% of people without a pension think about funding their retirement on a regular basis. This means that the government has not only to provide a platform to save (auto enrolment) but also a significant period of continuous education to influence mindset so that the message of "saving for your future" is taken on board to keep people enrolled.

The population is not saving enough

Quite frankly more people should be saving for their future retirement.

Our research shows that 44% of the UK population lack confidence in the amount of provision they have made for retirement and a massive 21% of people we surveyed have not made any provision for their retirement whatsoever. This is a staggering 5.6m people in the UK who at present do not have any safety net at all.

Recent DWP figures show that only 26% of UK private sector workers are active members of their employers' pension schemes, down from 31% in 2007. The DWP also reports that the number of private sector companies offering workplace pensions has fallen from 41% to 31% in five years.[5] Both schemes and scheme members are falling away and auto enrolment could change this.

The reality is that a lot of these future pensioners will be working well into their 70s if not 80s purely because they have underestimated the amount of savings needed to retire on.

This is backed up by Mark Wood of the Telegraph who quoted that the "...average amount set aside for pension savings in the UK is just £25,000 which will currently buy a pension of little more than £15 per week". The article goes on to say that the typical auto enrolment contribution rates suggest that this is not going to change much – which is extremely worrying.[6]

Pensions, savings & investments currently owned to provide support in retirement

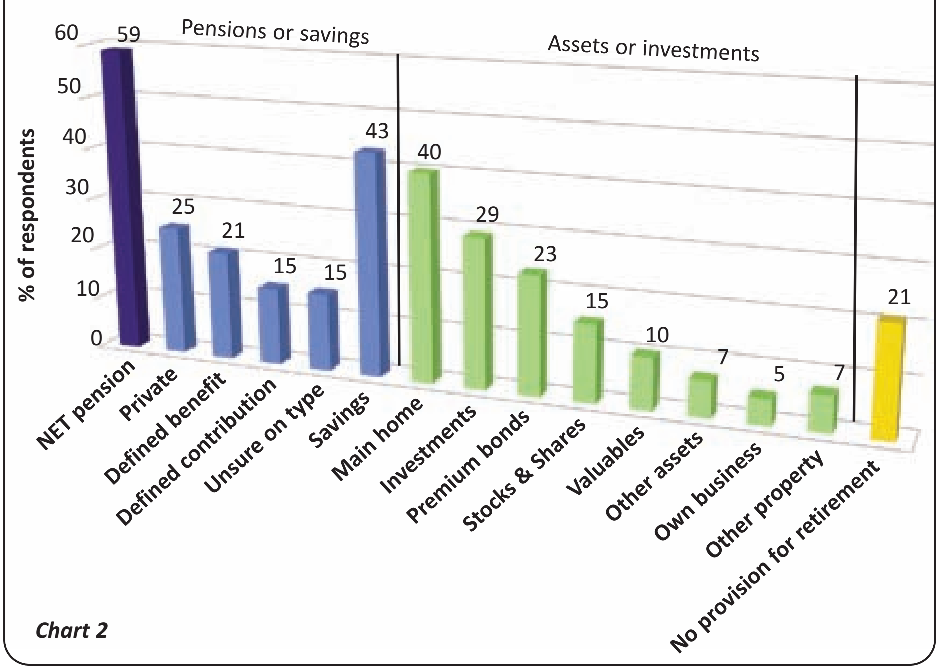

Chart 2

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How successful are the reforms likely to be?

It depends how you measure success. If you consider increasing the number of people who contribute to a pension to be a success measure, our research is saying that 46% of working people would stay opted into a pension, 42% are unsure and 13% would opt out.

However further examination of the findings shows that only 25% of those currently without a pension would stay enrolled. The real success will be to encourage these people to stay opted in and increase the amount saved for retirement across the board.

But the reforms face the following challenges:

Younger generations have other priorities

The younger generation is burdened with student debt and struggling to get jobs. Those lucky enough to have a job desperately want to jump on the housing ladder. They think less about saving for retirement and more about living for today. Generally it is acknowledged that over 75% of under 30 year olds have not got a pension. Their priority at this point in their life stage is "saving for a deposit to buy their own house" rather than saving for their future retirement.

However, for younger people getting on the housing ladder is becoming increasingly difficult with tighter mortgage lending resulting in the need for greater deposits on already expensive housing. This is pushing

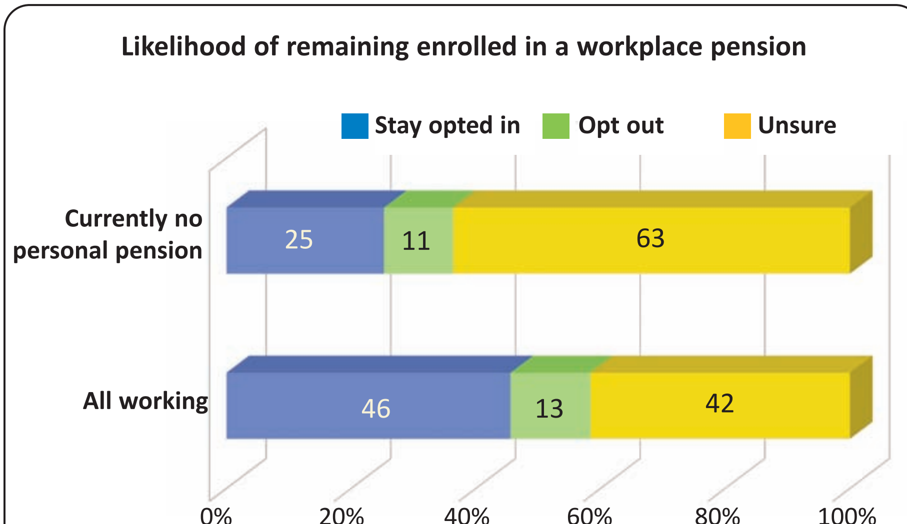

Chart 3

the age of first time buyers up and further delaying funding for their retirement.

Worryingly, 40% of all people we surveyed expected their main home to support them financially in their retirement; this shows that there is a huge gap between the reality and expectations of retirement planning. The stagnant housing market will further impact on the size of future funds. A lot of people today are expecting their houses to continue to increase in value to pay for their retirement and for inflation to reduce that mortgage debt - in both cases, unfortunately this is no longer true.

Increased personal debt held for longer

In the current "buy now save later approach" to life, debt can figure strongly throughout a person's working life. Paying off debt is delaying saving for retirement which is another significant factor affecting retirement. Recent research by MGM Advantage shows that people approaching retirement have an average of £22,500 of debt. This is an increase of 150% on recent retirees. Even if they intend to clear this debt with lump sums from their retirement pots, it obviously means less for funding their retirement.[7] However, increasing debt levels throughout the UK population from students to pensioners - general inflation, stagnant wages, redundancy and recession all mean that less is being saved for retirement... at the moment.

Affordability

At the end of 2011 30% of the UK population were finding it a constant struggle to keep up with their bills and other repayments. In today's straitened times encouraging people to contribute each month for something that's so far in the future is hard going, especially when they are currently living day to day.[8]

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Our research also indicates that around 54% of people say they cannot afford the extra payment to put into a pension. This is going to prove a strong challenge for the government to overcome as these are probably the people that need to save for their future the most.

Through using inducements such as tax saving and employer contributions this will hopefully go some way to encouraging people to saving for their future.

Relevance of the reforms

Are the pension reforms going to help those who are 10 to 15 years away from retirement? Especially if they have outstanding current debt.

In most cases these people will not have the capacity to save enough in the 10 or 15 years before their retirement and perhaps should prioritise paying off the debt first and save later. If they are not in debt there is an argument that these people should be exhausting ISA allowances before they contribute significant amounts to a pension.

Could this in fact be a future mis-selling scandal? Auto enrolling people into pensions later on in their working life when it is not suitable for them? But that is for a financial advisor to assess.

Right now the way pensions are geared means that auto enrolment should benefit the younger generation the most as they have the longest time to build up a significant sum before retirement. But with fluctuating financial markets, if they see their investment going down, will they continue to contribute?

Building trust in pensions

In the short term the government needs to ensure that when individuals are auto enrolled into their company scheme that they remain in the scheme for the foreseeable future.
Our research shows that 41% of people do not trust pensions whatsoever and a significant 61% of people will opt out or be unsure about remaining enroled. This means the government and pension companies will have to work hard at improving trust in pensions, or design similar new products to encourage long term saving and simultaneously building trust.

So why don't people trust pensions? Consumers believe there is an issue around unreliable returns, as well as trust in financial institutions as a whole, which has been exacerbated with the recent financial crisis.

It doesn't matter if the reactions are true or not, what is important is that it is a perception and as such needs to be addressed either by dispelling doubt or re-designing products so that perceptions change. This is going to be a real challenge for all involved.

Trust in pensions to provide sufficient retirement income

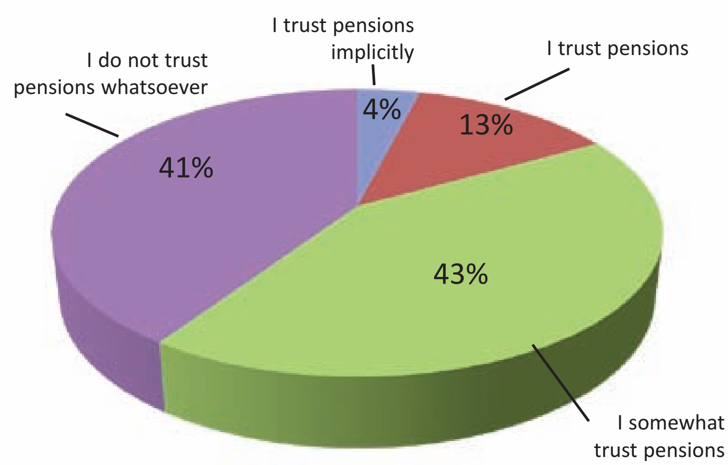

Chart 4

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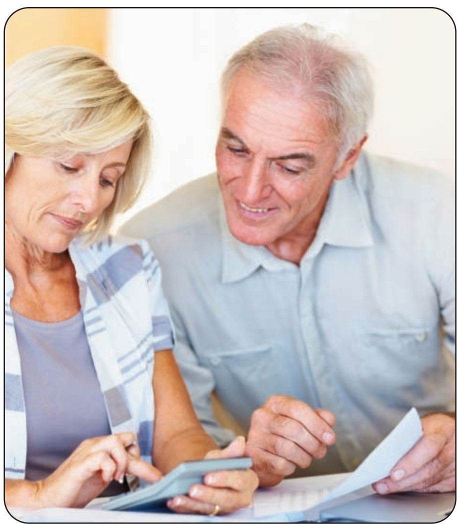
Is it a good initiative?

Overall the research shows that 63% of people think that auto enrolment is either "a good or very good idea"; it is encouraging that people recognise what the Government is attempting to do and it is a positive step to encourage us to save more and for longer. However when we look at our research on a more personal level doubts start to appear, with 74% of people who do not have a pension claiming that they are 'unsure' or that they would opt out.

As discussed before, is a pension the most suitable savings vehicle for those closer to retirement? It is a major challenge to ensure the government and the pensions industry keep pension products relevant to their customers as their needs and expectations change and evolve as they become more financially sophisticated. If they don't, pension companies risk becoming alienated and shunned for other investments and savings at the very least.

Look at learnings from another market, in the US, take up of the IRA (Individual Retirement Account) plans are high as they allow the individual to access funds pre-retirement for key life events (weddings, buying your first home, job change or loss for example) if needed. It is this flexibility that encourages people to save for their retirement knowing they can have access to their funds and repay them before they retire. Why don't the UK authorities and pension companies offer a similar type of product in the UK?

There is no doubt that auto enrolments will be good for most workers that do not have a pension at present. However the real benefits of this scheme will not be felt until many years into the future and only then if this initiative is part of a larger and ongoing education programme stressing the benefits of individuals taking responsibility for saving for their future retirement.



This leads us to another fundamental question, we all know that a varied multi strand approach to retirement (ISAs, shares, pensions, property.....) is the right way to spread risk, however, are pensions the right medium/format for saving for the future in today's ever increasingly fast moving flexible world or are they beginning to be outdated even now, never mind 20 years from now...I think I will save this debate for another time!

Reference sources & useful links

1. DWP 2011 Auto-enrolment & Workplace Pension Reform

2 (& charts 1-4). Harris Poll Global Omnibus. Survey conducted online between 7th-15th August 2012, amongst 1997 GB Adults 16+. Data weighted to be representative of GB population.

3.MGM Advantage - Our Retirement Nation 2011 Report

4. Source: Households below average income, DWP, GB. Updated Sept 2010

5.DWP Employers' Pension Provision survey 2012

6.*Export-led growth vital as tax burden rises from an ageing population* - Daily Telegraph Saturday 25th August 2012

7.MGM Advantage - Our Retirement Nation 2011 Report

8. Harris Interactive viewpoint Newsletter December 2011

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