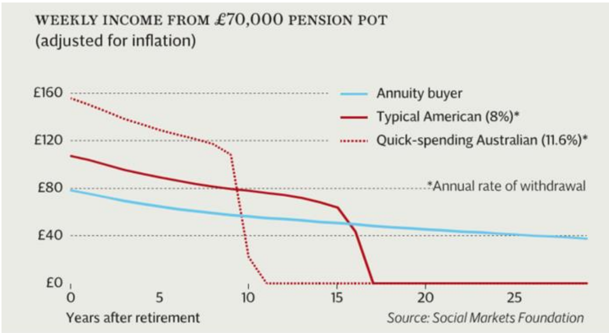
Penniless decade ahead for British pensioners?

An Optimisa Research Point of View

A left of centre think tank has recently claimed that a significant number of pensioners in the UK may be at risk of running out of money earlier than expected. The report, produced by the Social Market Foundation, studied countries where pension freedoms were more established (mainly the US and Australia, but also Canada, Denmark and Switzerland) and used the data to predict how the new rules that came into effect in April would impact on people's long term retirement plans.

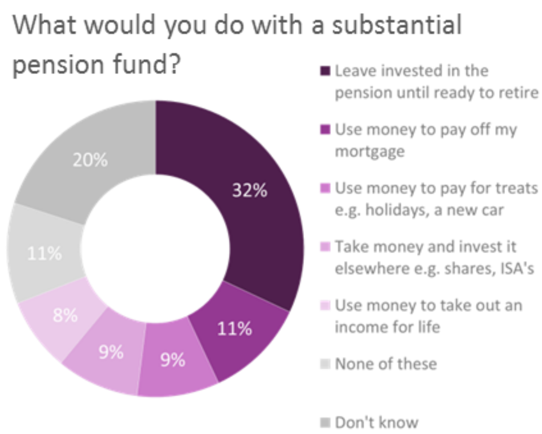
Unsurprisingly it doesn't paint a pretty picture. For example, the average American takes money from their pension at a rate of 8% a year (which is unsustainable and leaves them at risk of spending their final years living off the state) while 4 in 10 Australians will spend all of their money within the first 10 years retirement.



Fears for UK Pensioners

The obvious concern is that this pattern could repeat itself in the UK as the new rules settle in and people become more accustomed to the fact that the choices of how to fund their retirement are now theirs to make.

So what are the chances of this actually happening in the UK?



Self-funded research we conducted in early 2015 showed that, when asked to consider what they would do with a substantial pension fund available to them from age 55 years, two in five respondents (40%) would choose a traditional route (either purchasing a life time income or leaving the money invested until they were ready to retire) while only one in ten (9%) claimed they would use the money to treat themselves in some way. Of equal interest though is the fact that one in five (20%) genuinely didn't know what they would do.

But is it only half the story?

We believe that simply looking at what people plan to do is only half the story. We've found that in order to get a better understanding of the potential impact of the new rules, you also need to take into account the environment in which people are making these decisions.

Research we've conducted into this has shown that pot size and, to a greater degree, the importance it has in people's overall plans, has a massive impact on what they will do. In short, smaller pots that play a lesser role in supporting a person's retirement needs are more likely to be withdrawn and spent, while larger, more important pots tend to be used in a far more conservative manner.

All this seems to suggest that, for the moment, people are generally taking a measured view of how best to use their funds, an opinion shared by Yvonne Braun of the ABI who says "It is clear that people are taking a sensible approach and considering how they will pay for their retirement" (*BBC News online 3 Nov 2015*).

Despite this, there are more than enough signs that point to an uncertain future. Time and again our research has shown that people have a tendency to underestimate how long they will live while frequently being over ambitious about how much they can afford to spend each year once retired.

Combined with a general reluctance to give something up now for a benefit in the future and a deep seated mistrust of the pensions industry (fed by the media and government alike), there is every possibility that individuals will decide that they are better off managing their money personally, even though only half (53%) believe people are actually capable of making the right choices themselves.

The biggest challenge

We all know that one of the biggest challenges is getting people to start saving enough to support themselves during retirement. There are signs that the new pension freedoms can play a part in getting younger generations to consider saving. In our own research one half (49%) of those aged between 25 and 34 claimed that they would be more likely to put money aside in a pension under the new rules.

Overall, there is no doubt that the story being told by the Social Market Foundation is one that cannot be ignored. But by taking into account how those who have lived with these freedoms for some time act and by applying our own understanding of the behavioural tendencies of UK consumers, there is every chance that the mistakes of the markets that have gone through this before us can be avoided.

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