From pension pots to income streams: Overcoming retirement challenges

Geoff Marchment, head of master trust development at Aviva, discusses how the stages of retirement are changing and how guidance could help to ensure a financially comfortable journey

The pension landscape has undergone a profound transformation over the past decade, marked by pivotal initiatives aimed at increasing both the participation rate and flexibility for using pots. Automatic enrolment in 2012 and the introduction of pension freedoms in 2015 provided the legislation, and schemes provide the facilitation.

With two successive Mansion House statements from two governments, coupled with the launch of the recent Pensions Investment Review consultation, the stage seems set for yet more change.

A very personal problem

A host of challenges face today's defined contribution (DC) pension members as they navigate the complex journey of converting their pension pots into sustainable income streams for retirement.

Compounding this challenge is the rising cost of housing and the decline in home ownership, which have left many workers with less financial security as they approach retirement. Additionally, increased longevity means that retirees must plan for longer periods of financial independence, a task made even more daunting by the potential for cognitive decline, which can impair financial decision-making abilities. As a result, today's retirees face several obstacles that require careful planning and support to ensure a stable and secure retirement.

Aviva's *Working lives* research in 2024[1], found that more than a quarter (28 per cent) of employees are not confident planning for a financially comfortable retirement. More than one in five (23 per cent) have not done any planning and three-quarters (75 per cent) want more support and guidance from their employer about planning for a financially comfortable retirement. Additionally, many of those sought more information on how to make their pension pot last throughout retirement (60 per cent) and more information on how they can build up their pension pot (51 per cent).

Unlike defined benefit (DB) schemes, DC pensions have placed the onus on individuals to manage their retirement savings. It has been shown that people who take financial advice have boosted their wealth by an average of £47,000 over the past decade.[2]

For those that do not seek out support from an adviser – and there are many reasons why advice is not sought – that leaves both an advice gap and a confidence gap. Whilst only 9 per cent of the population have funded advice in the past two years, falling from 11 per cent in 2023[3], scheme members increasingly seek to fill these gaps through support provided by their trustee, their employer, their pensions provider, the government, friends and family, ChatGPT and TikTok.

These all carry varying degrees of both perceived trust and risk. Some have a duty to act in members' interests, others may only have their own interests at heart.

From a members' perspective, holistically planning for their retirement can be viewed simply as a few straightforward steps: **what do I have?, what do I need?,** and **how do I turn what I have into what I need?**

What do I have?

This initial step involves taking stock of all available resources, including DB and DC pensions, state pension eligibility, savings, investments, and any other financial assets. However, this seemingly simple task can be fraught with challenges. Many individuals may not have a clear understanding of their total financial picture, especially if they have multiple pension schemes from different employers or various investment accounts.

Trustees should make it straightforward to provide members with both a current valuation and a valuation at retirement. Consolidation of pots into active arrangements may also be beneficial to their long-term outcomes.

What do I need?

This involves estimating the amount of money required to maintain their desired lifestyle throughout retirement. This step can be complex, as it requires members to consider a range of factors such as life expectancy, inflation, healthcare costs, and potential changes in living expenses. For instance, retirees may need to account for increasing healthcare costs as they age, or the possibility of needing long-term care. The Department of Health and Social Care estimates that one-in-seven individuals over 65 will face lifetime care costs of more than £100,000[4].

Financial literacy challenges every member, and understanding their investment options, tax implications, and withdrawal strategies can help them optimise their retirement income.

Trustees should look to offer varying degrees of support for this part of the process, whether through guidance tools and modellers, or providing access to pre-retirement financial education or advice services.

How do I turn what I have into what I need?

Turning accumulated retirement savings into a sustainable income stream is a critical challenge for many retirees.

Whilst members may have been able to navigate the first two questions, developing a comprehensive withdrawal strategy that considers taxation, investment risk, pot erosion and inflation may be challenging.

Trustees should be clear with scheme members and provide clarity regarding the options that are available to them under their scheme rules. Increasingly, members are seeking income options through drawdown rather than cash or annuitisation. Where these options are not available within the trust, trustees may consider partnership with a drawdown provider to make these options available.

An increasing challenge for our industry

Aviva's research suggests almost 3.4 million 32-40 year-olds saving into their defined contribution pension could accumulate £225,000 or more in pension savings by the time they retire in 2050[5]. This significant number of savers with defined contribution pensions will need to navigate complex decisions about how to convert their pension wealth into a sustainable income stream throughout retirement.

At Aviva, we support employers and trustees with detailed insights on their scheme through our Insight Hub. A key recent development which projects every member pot through to retirement, and maps these against the PLSA Retirement Living Standards. With the ability to segment the data, this allows targeted strategies to be developed to help members make informed decisions about their contributions, investments, and options for using their pension pots, ensuring they're on track to meet retirement goals.

With the increasing value of DC pension pots and a greater reliance on DC pensions funding retirement, attention is now turning to innovative developments in the workplace market for those members looking to convert those pots into an income throughout their retirement.

Default decumulation legislation

Ensuring adequate retirement income is also a key objective from a regulators point of view.

Legislation is under consideration[6] which aims to ensure that all pension schemes offer a set of decumulation options including a default income solution for members who do not engage actively with their retirement planning. This legislation is expected to have significant implications for trustees who will need to decide on their default income solution that members will be opted into if they do not make an active choice. This ensures that all members have access to a secure retirement income. Trustees could opt to provide decumulation service through partnerships with schemes such as the Aviva Master Trust.

Supporting trustees to deliver retirement solutions

The Aviva Master Trust already supports employers and trustees who need to provide retirement solutions outside their existing trust-based arrangement. With a rigorous focus on a positive member experience, these partnerships enable trustees to access the full range of pension freedom options. They also provide access to Aviva's extensive development and innovation expertise to support members throughout their retirement.

For more information search "Aviva Master Trust"

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[1] Working Lives Report 2024 : Working for the Future - https://www.aviva.co.uk/business/workplace-wellbeing/working-lives-report/
[2] Financial advice not only pays for itself, but boosts confidence and preparedness for retirement, Nov 2020, Longevity Centre - https://ilcuk.org.uk/financial-advice-not-only-pays-for-itself-but-boosts-confidence-and-preparedness-for-retirement/
[3] https://www.flipsnack.com/langcat/advice-gap-report-2024/full-view.html
[4] https://assets.publishing.service.gov.uk/media/61d5d4bfd3bf7f1f6f74330f/adult-social-care-charging-reform-impact-assessment.pdf
[5] Aviva's research in conjunction with WPI Economics – Planning for retirement in the 2050s - https://static.aviva.io/content/dam/aviva-corporate/documents/newsroom/pdfs/reports/Aviva%20Report%20Planning%20for%20retirement%20in%20the%202050s.pdf
[6] https://www.gov.uk/government/consultations/helping-savers-understand-their-pension-choices-supporting-individuals-at-the-point-of-access