For adviser use only

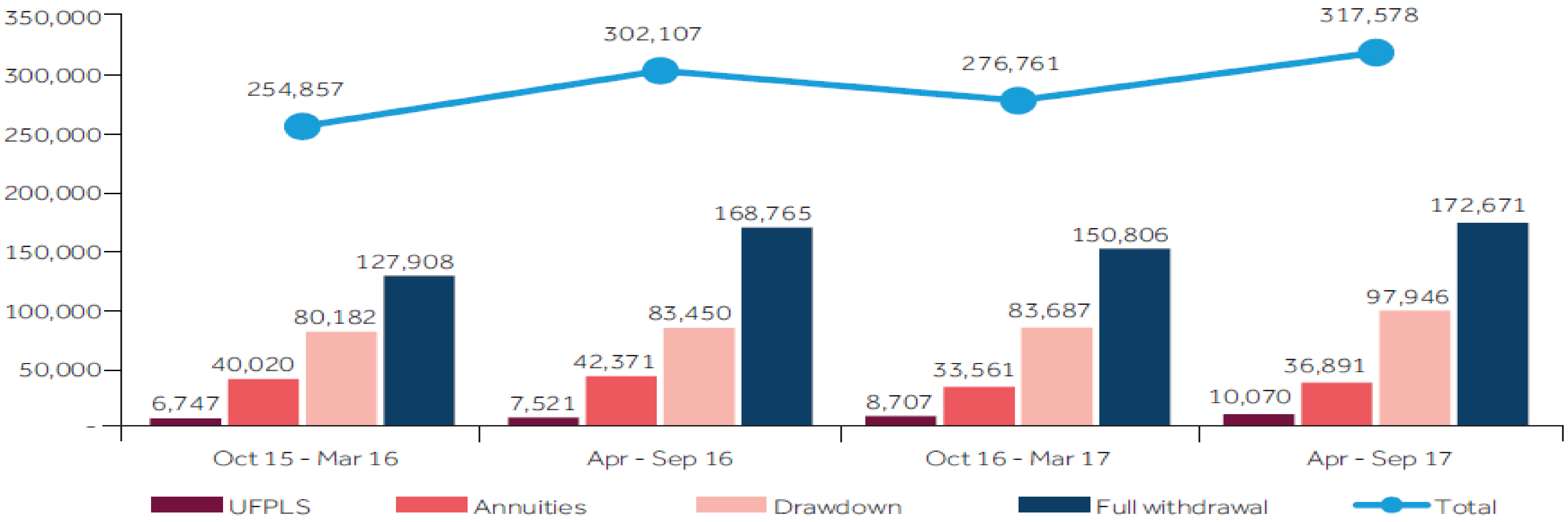
Sheffield Life & Pensions Webinar
Retirement Income: Strategies to manage Underspend and Overspend risks

Jeremy Martin
Pension, Tax and Estate Planning Specialist, Canada Life

Learning objectives

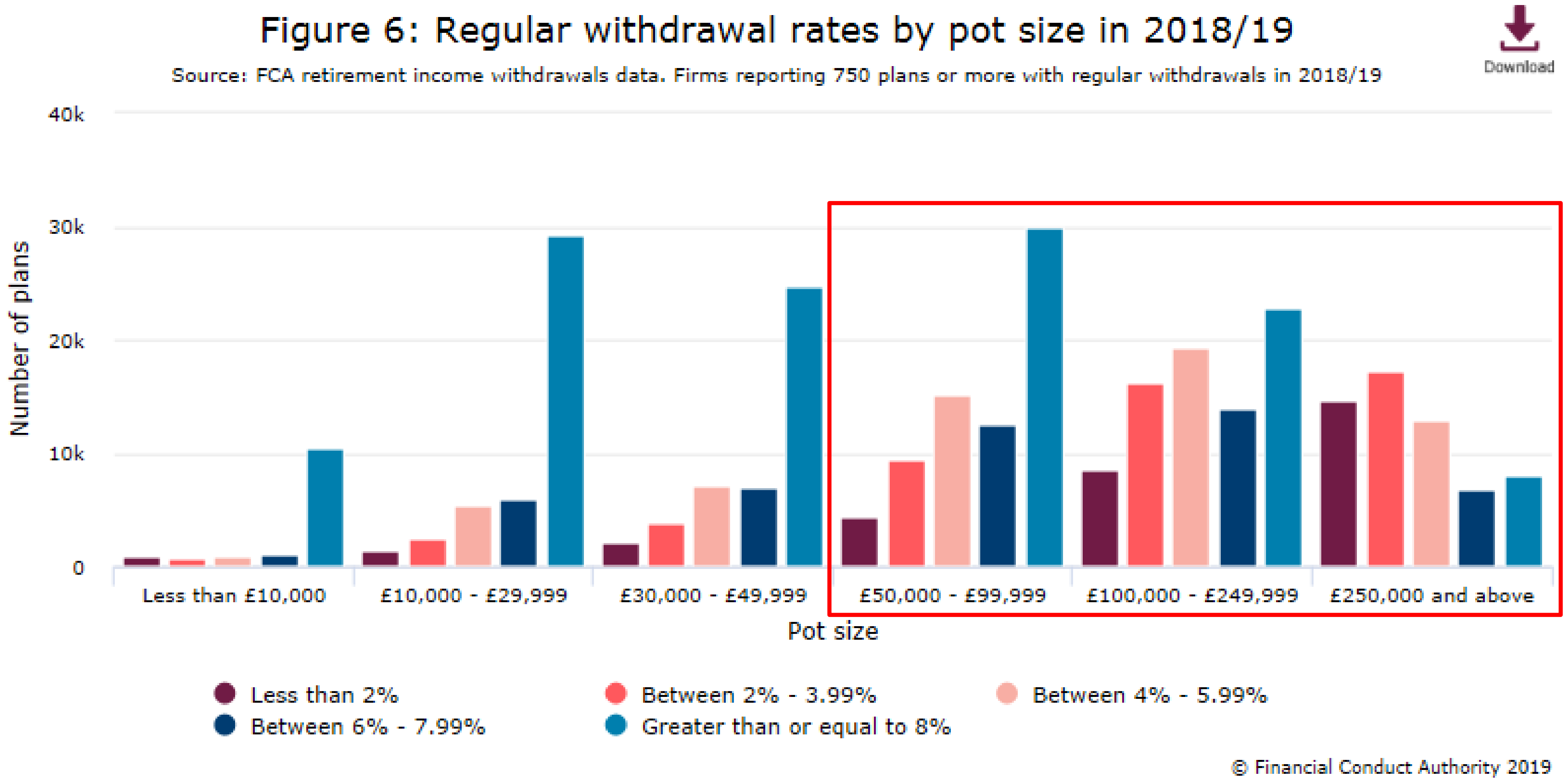
- Discuss how a holistic approach can be adopted by advisers to deliver flexibility and certainty for clients in retirement, with reference to the FCA's 'Dear CEO' letter of January 2020.
- Demonstrate the pros and cons of income sustainability, exploring the 'probability-based' approach and methods often used as part of this
- Explore the pros and cons of securing some essential incomes using state pensions and a client specific guaranteed income within a flexible drawdown proposition
- Explain how Pension Freedoms created space for innovation that Defaqto have written about. Resulting in an award winning retirement solution, combining pension savings, income drawdown and guaranteed income within a single wrapper

Pension Freedoms: changed and created new ways to access your pension



Source: FCA analysis of retirement income market data collected from 56 providers

Sustainable income: what is happening in market?



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FCA Dear CEO letter: pushed back but not gone away

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21 January 2020

Why financial advisers are a key FCA priority

We have identified four key ways in which consumers of financial advice may be harmed:

- receiving unsuitable advice for their needs and objectives
- falling victim to pension and investment scams
- not receiving redress as a result of the non-payment of FOS awards and/or failing firms being unable to compensate consumers
- paying excessive fees or charges for products and services

There will be increased focus on these areas as part of our wider supervision of firms over the next two years.

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There will be increased focus on these areas as part of our wider supervision of firms over the next two years.

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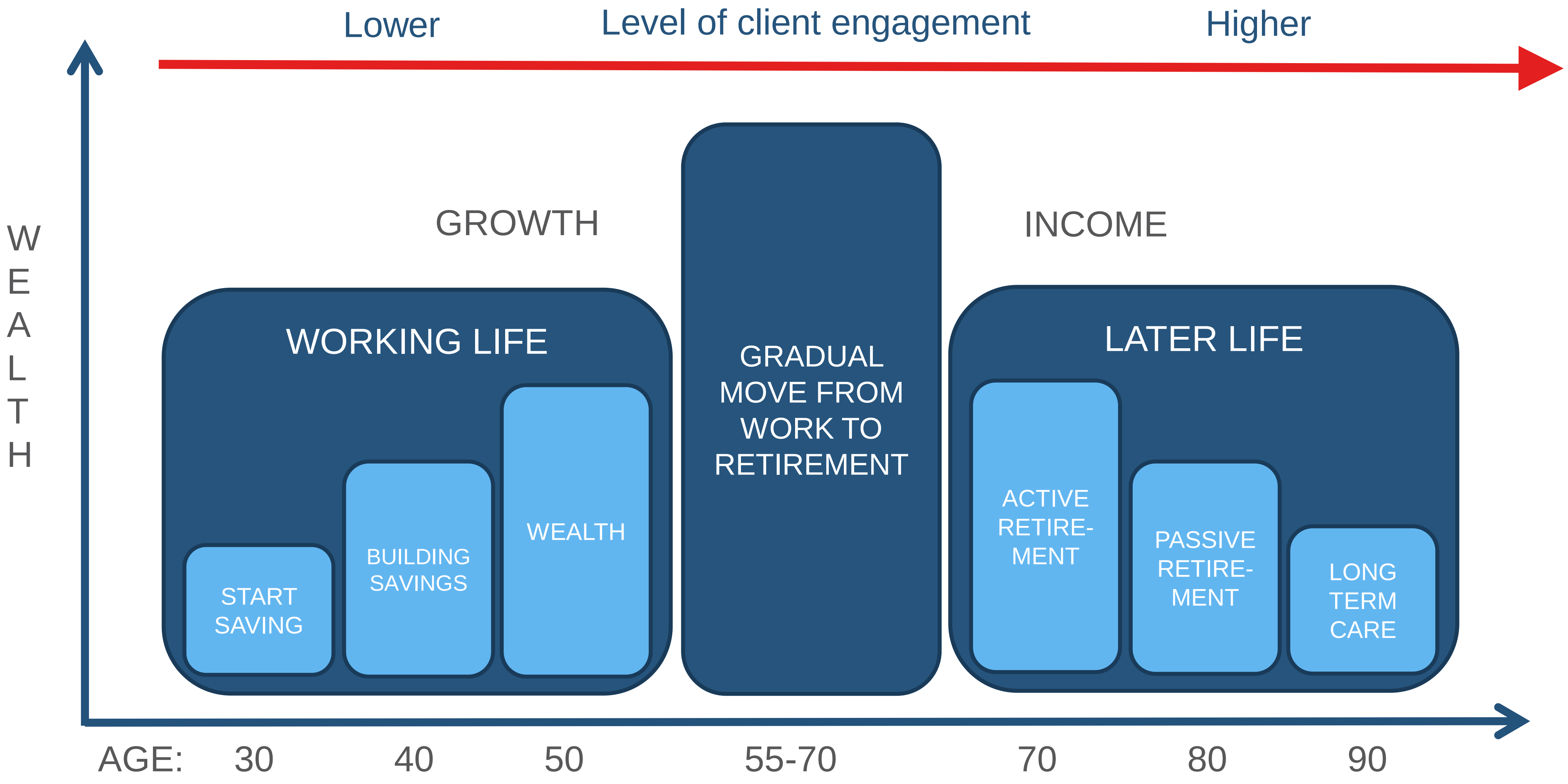
Centralised Retirement Proposition: Evolution not revolution



Assessing Suitability – Is a CRP mandatory?

Answer – No, however…..

> *They're (the FCA)* ***not*** *going to ask specifically about your* ***target market****, but they could ask* ***how you decided*** *that a solution* ***was appropriate*** *for your target market,* ***and if you can't show them****, that's a rule breach.*

(Mike Barrett – The Lang Cat)

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The Fundamental Question – things to assess

Cash-flow forecast

Legislation changes

Asset Access Tax effectively

Interest rate Assumptions

Investments risk aligned

Longevity

“Do I have enough money for retirement?”

Health change impact

Tolerance for loss

Guaranteed income required

Substituted decision makers

Cash buffer agreed

Sequencing risk

Investment Assumptions

Inflation impact

Income Needs

Review frequency

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Looking for security (managing underspend and overspend risk)

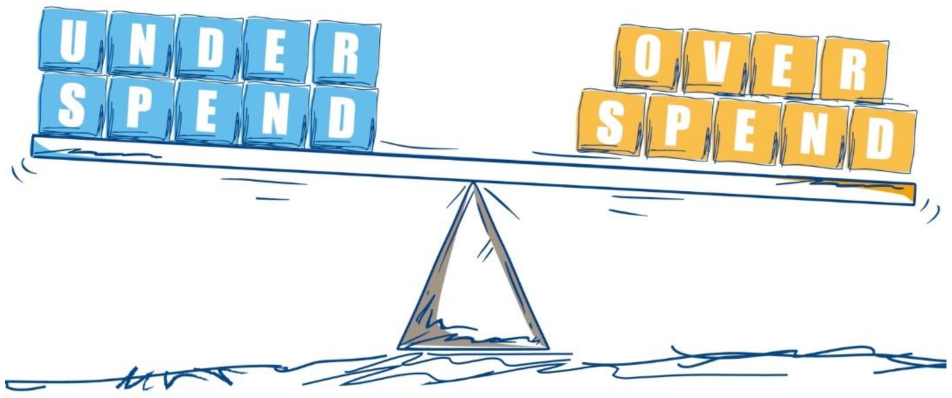
The major risk for client seeking income is the ongoing erosion of capital from falls in their investments.

Review their current position

1. Switch off unnecessary income
2. Guarantee essential expenditure
3. Consider a risk targeted fund range to manage sequencing risk
4. Manage costs

Protecting your drawdown clients from long term movements of the market whilst providing genuine growth.

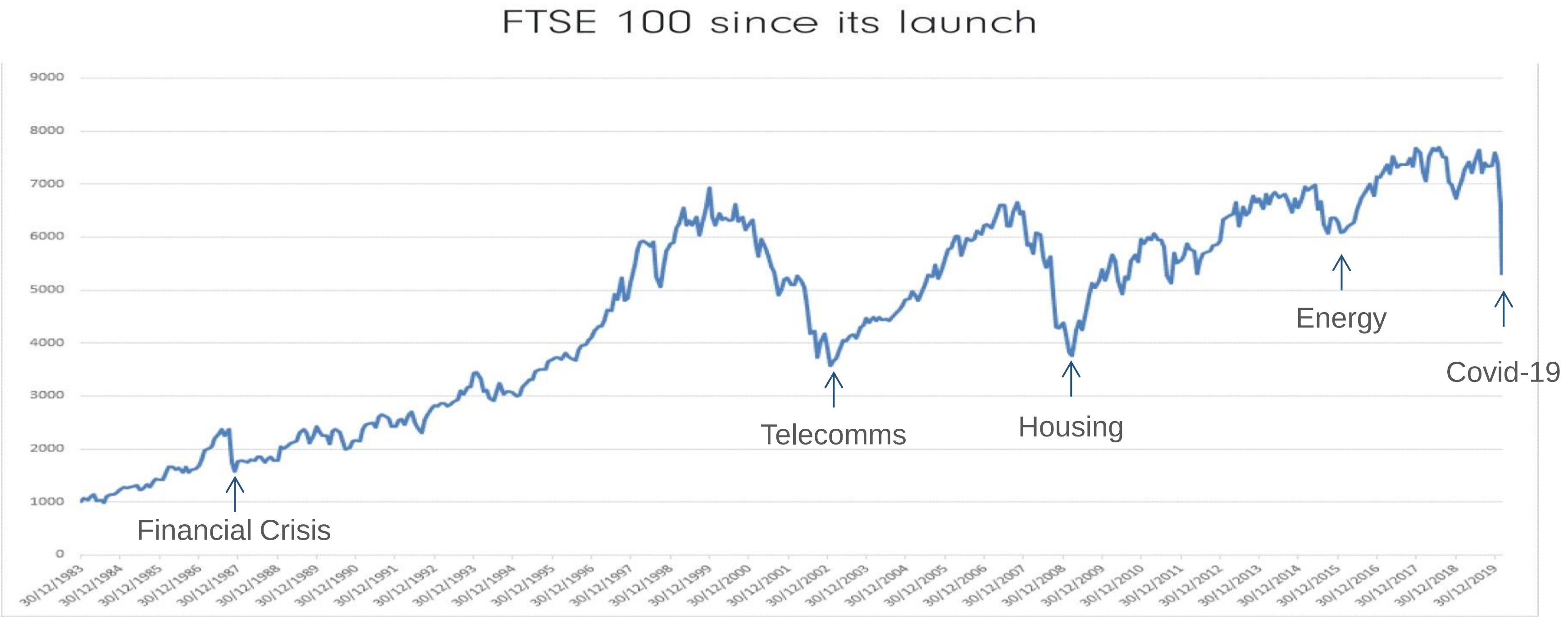
- Blended / hybrid solutions
- Portfolios designed for different demands



Which way forward for clients approaching or in retirement?

FTSE 100 at 21 Feb 2020 - 7,403.92

On 23 March 2020 FTSE reached it's lowest point – 4,993.89 during the Covid-19 pandemic.



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Which way forward for clients approaching or in retirement?

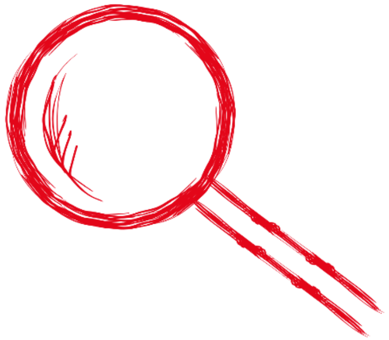
History has shown us that markets tend to recover, **HOWEVER**, nothing is guaranteed

Client's looking at retiring in the next 10 years have three challenges in front of them, do they;

1. Security of income – crystallise their losses and/or buy guarantees or protection.
2. Sit tight – take the view that the market will recover at some point.
3. See this as an opportunity to buy into a recovery.

Pension and Lifetime Savings Organisation (PLSA) – helping the focus

51% of people focus on current needs
Only 23% confident they know how much need to save



Three sets of ‘Living Standards’:

- ‘Minimum’ -
- ‘Moderate’
- ‘Comfortable’

Includes: basket of goods for each containing -

Household Bills / food and drink / holidays and leisure / clothing and personal items and helping others

(Source PLSA 17/10/2019)

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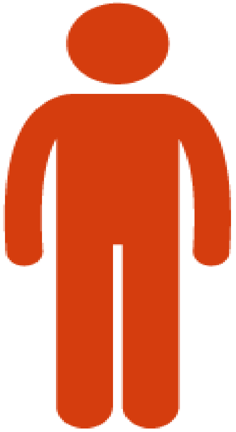
Pension & Lifetime Savings Organisation (PLSA) – ‘standards’

Results - Single



Minimum: £10,000

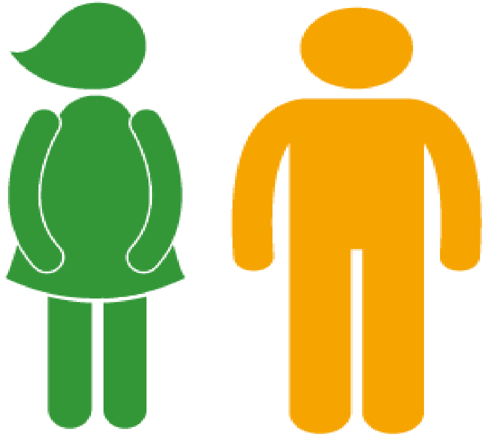
Moderate: £20,000

Comfortable: £30,000

‘Retirement Living Standards’ (RLS)

PLSA Ambition: RLS to become adopted as Industry standard

Results - Couples



Minimum: £15,000

Moderate: £30,000

Comfortable: £45,000

(Source PLSA 17/10/2019)

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Observations of ‘drivers’

Planning Issues – income sustainability

FCA DP 19/2: A backdrop of decline in annuity market **81%**:

2018/19*

- **55%** of Consumers withdrew pension pots as cash
- **30%** Opted for drawdown

2018 Joint strategy FCA & TPR:

- Identified **overarching** harm – people may not have adequate income, or income they expected in retirement.

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Vulnerable Clients Policy

The Vulnerable Client Policy is **part** of the **advice process**:

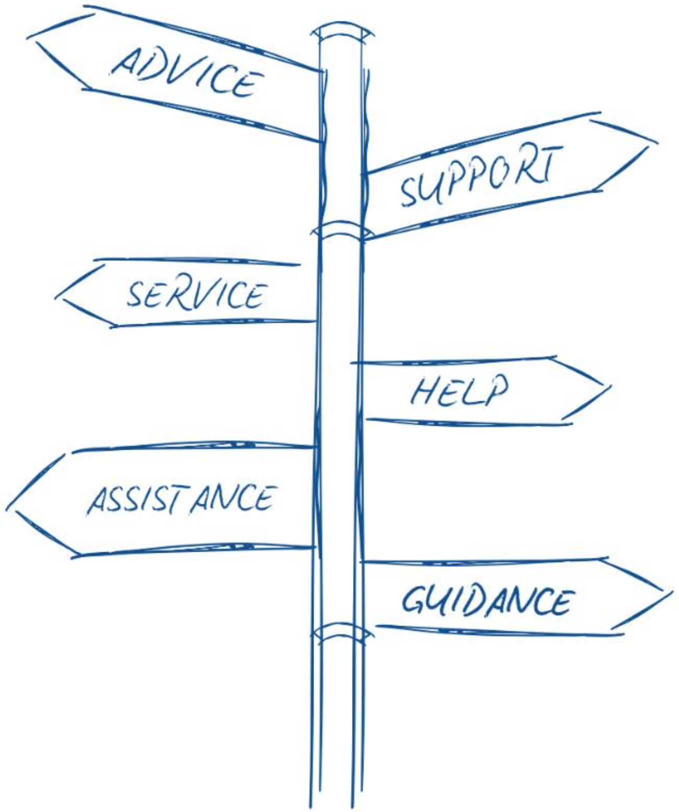
Vulnerability is not always visible

How does it **interact** with the **CIP**?

How does the **CRP engage** with this?

E.g. Long term nature of retirement

- Need to review
- Changes in risk attitude
- Changes in cognition and understanding
- **Health** issues current or onset / **reviewed**?
- Is the **current product** choice flexible and modern enough to deal with 35+ years?



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For how long do we plan?

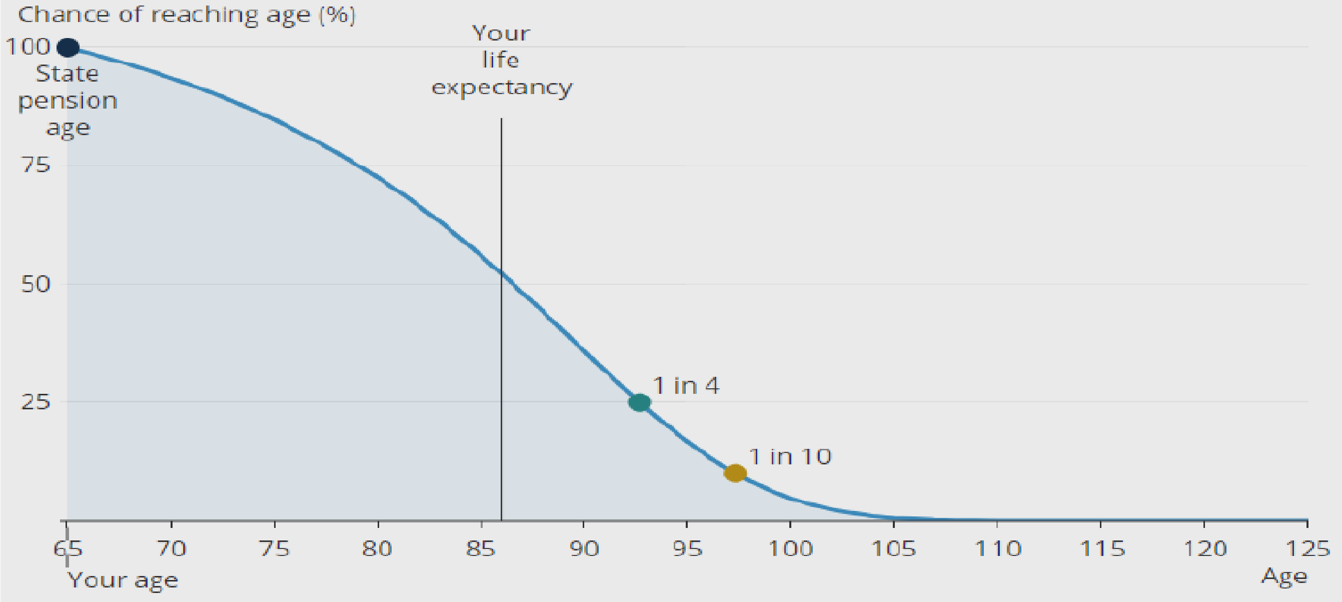
Your average life expectancy is...

86 years

(that's **21** years from now)

However there's a chance you might live longer...

1 in 4 chance of reaching	1 in 10 chance of reaching	Chance of reaching 100
93	**97**	**4.7%**



(Source: ONS [DA Norman – TCF Investments])

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State pension factoids: bedrock for peoples retirement

20,967,473 viewed online statement
(4 April 2016 to 30 May 2020)

57,720 viewed statement between 23 and 29 December 2019

1,320,023 – Digital
8,307 - Paper
(1 April to 30 May 2020)

1,364,107 in receipt of new state pension
(6 April 2016 to 30 November 2019)

984,713 receive state pension with no protected payment

379,394 receiving more than the full amount – Protected Payment

Full amount 2020/21
£175.20 p.w. = £9,141.68 p.a.

Cost to buy maximum state pension £302,751**

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Source: Canada Life illustration RA90002275 10/01/2020. Assume healthy, single life, escalating 3% per annum**
Source: https://www.gov.uk/performance/state-pension-statement/transactions-by-channel FOI DWP dashboard April 2019

Top up to cover personal essential expenditure – the use of guarantee

£211,433

Flexible Drawdown pot

£88,567

3% Esc Annuity @ = 66

£2,859 a year

Max State Pension.

= **£9,141 a year**

Personal income guarantee need £1,000 a month

Age 66

* Healthy rates – targeting £2,859 a year, paid monthly. 15/05/2020 Illustration RA90005873
Source: Based on £300,000 transfer – Split £88,567 TRA Annuity purchase price and £211,433 Invested DD; Healthy 66 yr old, Single Life, 3% escalation

Deferring your annuity: impact of age and health

Age	Healthy rate % rate	*Mild conditions % rate	**Moderate conditions % rate	***Severe conditions % rate
60	3.89%	4.21%	5.31%	6.96%
65	4.67%	5.07%	6.14%	7.85%
70	5.28%	5.80%	7.00%	8.93%
75	6.44%	7.18%	8.68%	11.03%
80	8.11%	9.31%	11.25%	14.26%

Source: Canada Life, TRA Annuity - £50,000 purchase price, single life, level (Illustrations dated 15/05/2020)
*MILD: Normal height & weight, long-term smoker with HBP and cholesterol medication
**MODERATE: Overweight, (same conditions as mild) plus diabetes with minor complications and angina diagnosed 2 years ago
***SEVERE: Overweight (same conditions as mild) plus diabetes. Had heart attack 2 years ago with bypass surgery but has recent complications and under care of cardiologist

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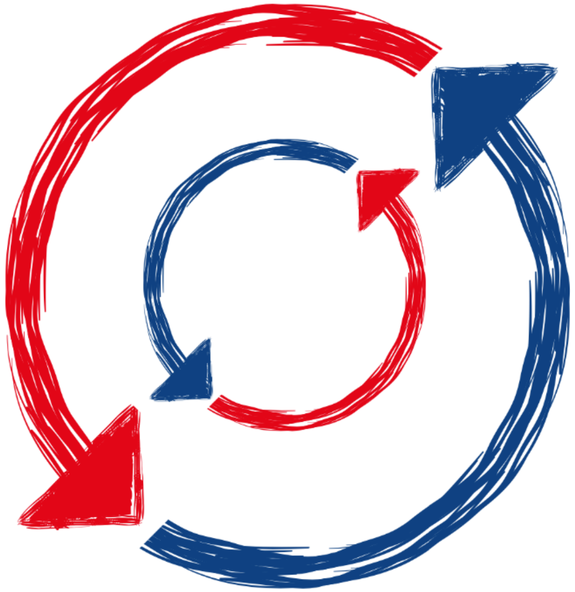
Which way to go?

'Probability-based'



'Safety-first'

Does it need to be one or the other?

Probability vs Safety First – Summary (paraphrased)

	Probability-based	Safety-first
Budget	High Level	Detailed Budget
Modelling tool	Historical or Monte Carlo, WPS*	Cash flow, essential vs discretionary
Longevity risk	Managed via survival probability	Hedged via contractual guarantees
Withdrawal strategy	Rules-based	Liability matched to needs hierarchy
Trade-off	Adjust income in severe markets	Income prioritised to cover essentials
Upside	Income in times of good markets	Essentials not subject to markets
Retirement income product(s)	Diversified investment portfolios	Annuity (inc. investment-linked), Diversified portfolios for discretionary
Risk Profile	Medium to high	Low to medium
Ability to flex income	Medium to high	Low to medium
Maintenance	High	Low
Difficulty	Complex	Simple

(Source: Abraham Okusanya)

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The Safe withdrawal rate

*…the safe withdrawal rate (SWR), the **fixed rate** at which **systematic withdrawals** can be made from a portfolio of typically risky assets over a **defined period***

(Chris Wagstaff – Senior visiting fellow, Cass Business School)

Dependant on a number of variables and risks such as Health, Longevity, investment returns and inflation….

*…Taking account of these…**risks**, it probably isn't any surprise that **most people**…..also crave the **security**, but **not** the **rigidity**, of an…..annuity…..and therein lies the **conundrum**:……how can a SWR meet these seemingly **conflicting objectives**….?*

(Chris Wagstaff – Senior visiting fellow, Cass Business School)C

Is it a binary decision?

Safe withdrawal rates and return assumptions – future gazing

William Bengen – USA – 4% Inflation adjusted from Equity Bond Portfolio

Professor Wade Pfau – UK – 3.05% based on 50/50 equity bond portfolio

(Source: Abraham Okusanya)

Annualised real returns for UK assets (%)

UK Asset Class	20 years	50 years
Equities	2.0	4.7
Gilts	2.5	3.2
Index-Linked	3.0	
Cash	-0.1	1.1

Source: Barclays Equity Gilt Study

(Source: DA Norman – TCF Investments)

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Safe withdrawal rates – future gazing

Safe Withdrawal Rates for UK Retirees

The table below shows the safe maximum historic withdrawal rates (SAFEMAX) and the failure rates for a 4% and 5% withdrawal rate for various portfolios.

	SAFEMAX	10th Percentile	% Failures for 4% Withdrawal Rate	% Failures for 5% Withdrawal Rate
Perfect Foresight Assumption	3.77	4.17	3.8%	27.5%
UK 50/50 Portfolio	3.43	4.01	9.30%	55.60%
Global 50/50 Portfolio	3.26	3.55	17.90%	31.00%

Source: Wade Pfau (2010, 2014) Assumptions include a. perfect foresight portfolio, b. a fixed 50 / 50 domestic equities/bond allocation and c. a fixed 50 / 50 global equities/bond allocation, a 30-year retirement duration, no administrative fees, annual inflation adjustments for withdrawals, and annual rebalancing.

(Source: DA Norman – TCF Investments)

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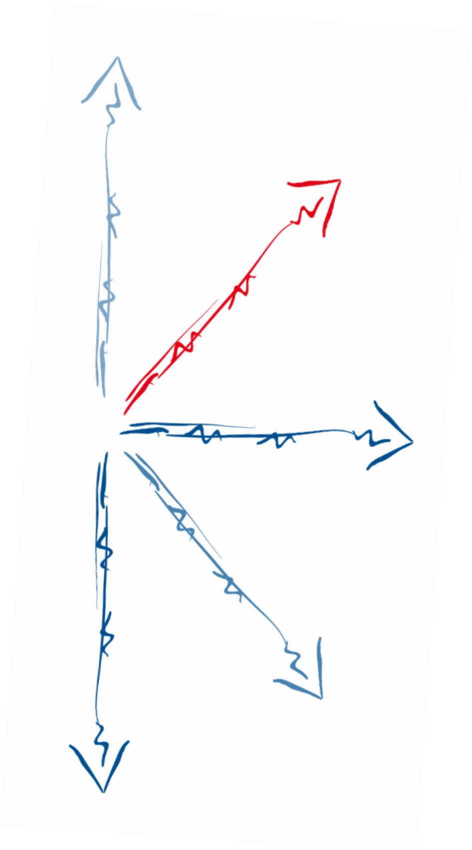
Market Activity – what's happened



Year	Cautious	Balanced	Growth
2019	8.44	11.64	15.64
2018	-3.28	-5.15	-6.22
2017	4.51	6.95	9.78
2016	8.28	9.90	13.11
2015	0.20	1.12	2.31
2014	4.98	4.82	4.76
2013	4.17	8.57	13.77
2012	6.20	8.12	9.60
2011	1.18	-1.90	-5.62
2010	7.47	8.53	12.14
2009	11.04	15.48	20.01
2008	-10.63	-15.60	-21.20
2007	-0.05	1.39	4.07
2006	5.33	6.80	10.09
2005	8.74	12.89	19.88
2004	7.37	9.58	10.18
2003	8.49	14.79	18.57
2002	-0.10	-10.91	-17.37
2001	1.59	-3.58	-11.20
2000	7.09	2.77	-2.95
1999	0.88	12.73	24.84
1998	12.99	11.45	10.95
1997	15.02	18.40	12.97
Average	4.78	5.60	6.44
Best	15.02	18.40	24.84
Worst	-10.63	-15.60	-21.20

Year	Cautious	Balanced	Growth
	0-35%	20-60%	40-85%
Average	4.78	5.60	6.44
Best	15.02	18.40	24.84
Worst	-10.63	-15.60	-21.20

Typical recovery timescales:

Cautious: 2 years, long-term return circa **4.5%pa**

Growth: 3 or 4 years, long-term returns circa **6.0%**

(Source: FE Analytics [DA Norman – TCF Investments])

Withdrawal strategies for Income Drawdown

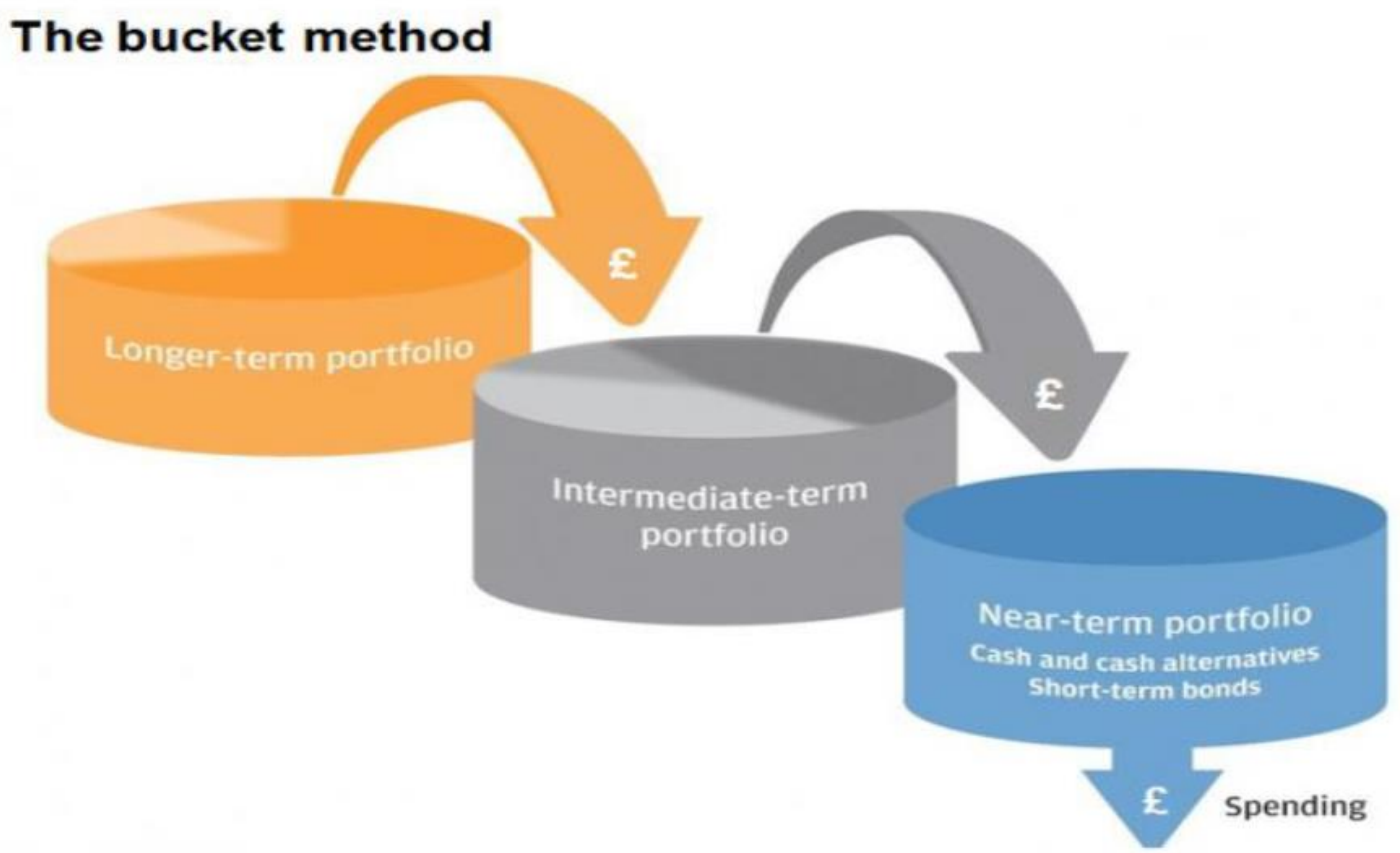
Sustainable Withdrawal Rate

Natural Income Producing Funds

Time Frame Investing

"Pot" Investing

Pot strategy – aka 'bucket strategy'



(Source: DA Norman – TCF Investments)

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Managing the income - Pot Strategy

Potential Asset split:

Pot	Investment
Cash reserve	two - four years income plus five years capital items
Medium term pot: 4 – 10 years	Managed portfolio c. 40% equity (possible income bias)
Long term pot: 10 years on	Passive portfolio c. 75% plus equity
Optional buffer pot: potential annuity/reserve	Low cost portfolio c. 50% equity (possible income bias)
	Overall c. 60 – 80% equity

(Source: DA Norman – TCF Investments

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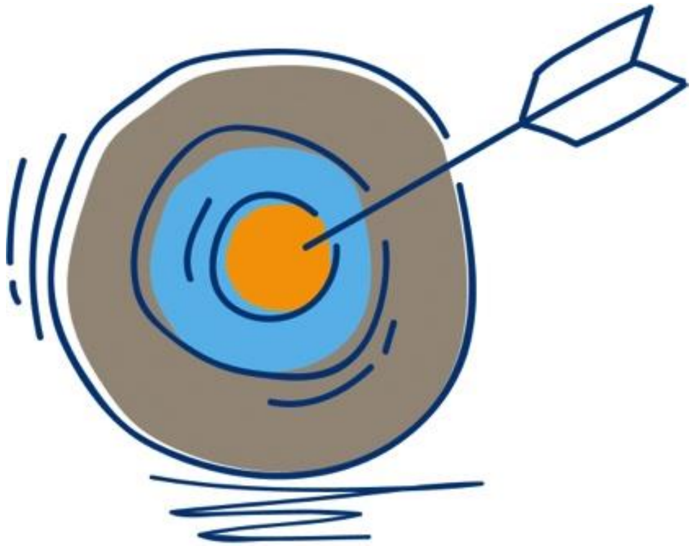
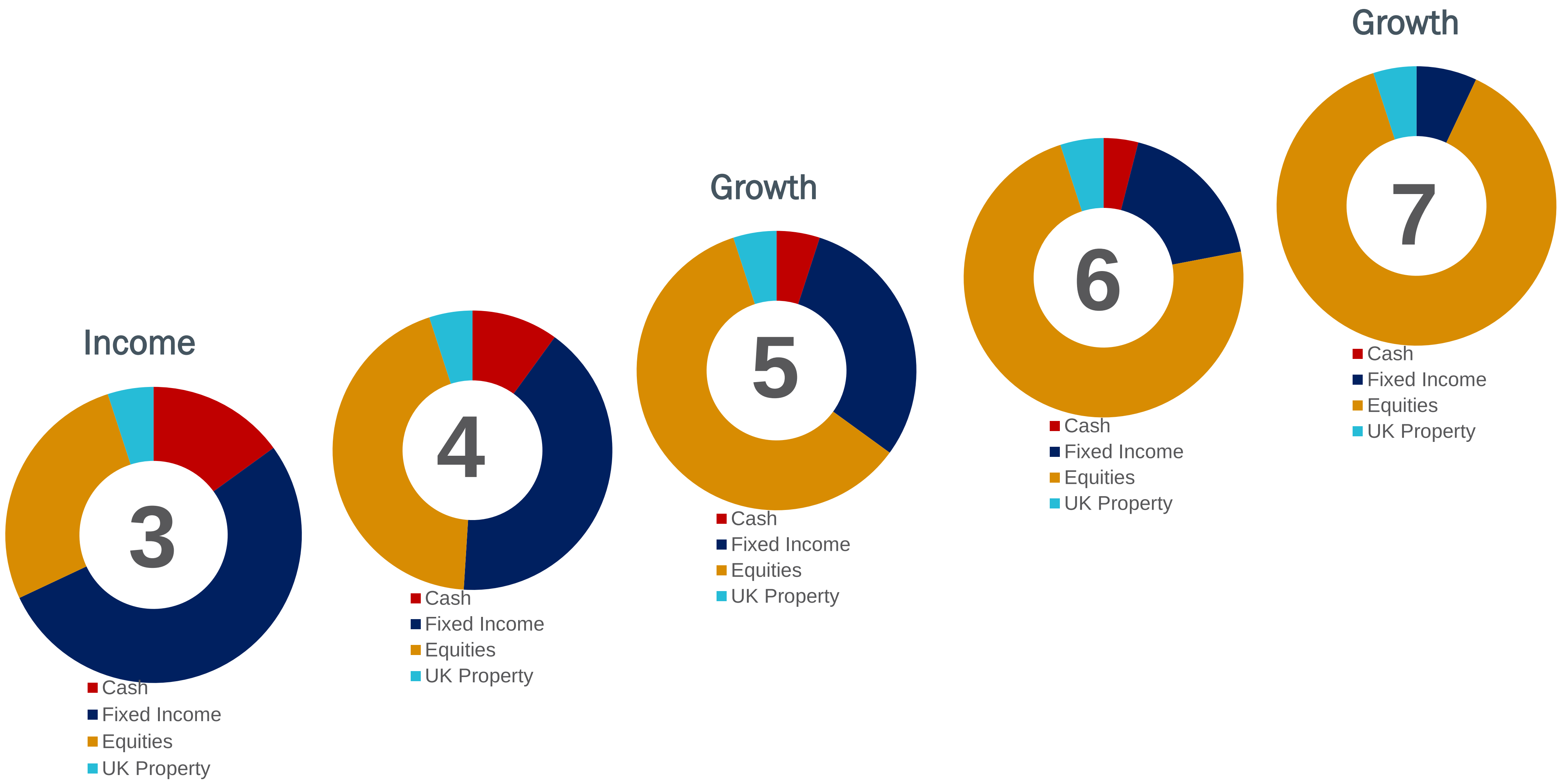
One size doesn't fit all

- Try and avoid the use of a single fund – helps manage sequencing risk
- Retirement planning requires the management of growth, security and income. One fund is unlikely to be able to achieve all three
- Target the right fund to meet the income need of the client
- Review and set realistic sustainable income withdrawal levels OR …
- Explain the consequences of exceeding these levels



Utilising the pots strategy with risk focused funds



Source Canada Life Investments – Asset Allocation month end December 2019

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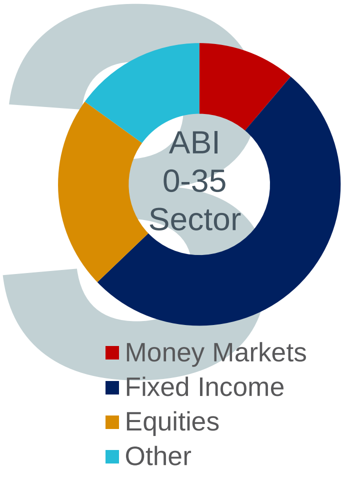
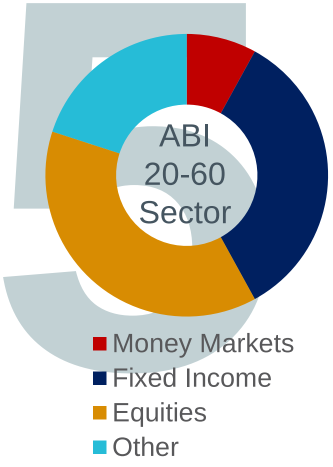
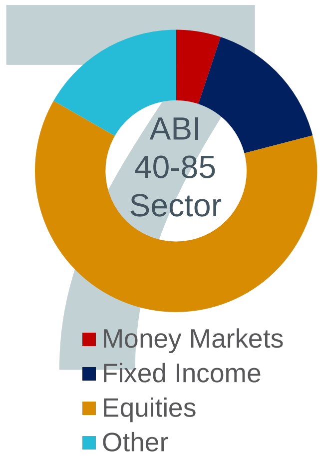
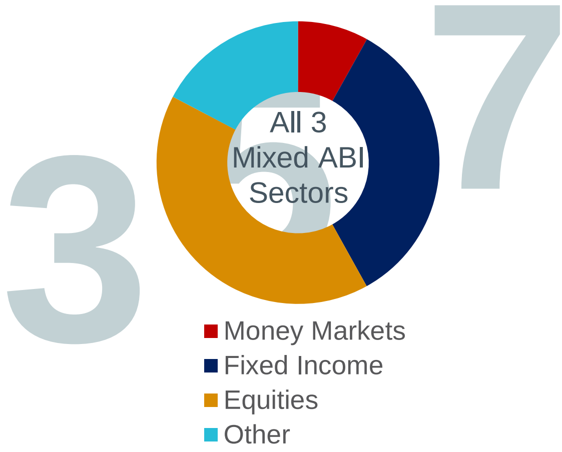
At retirement – one thousand simulations

These figures are based on simulated performance for illustration purposes









Percentage of 1000 simulations where Drawdown pot lasted 30 years				
6% Starting Income (1% Fee)	44.9%	38.3%	44.9%	51.8%
5% Starting Income (1% Fee)	87.1%	71.5%	67.0%	92.4%
4% Starting Income (1% Fee)	99.6%	92.9%	86.0%	100%

Source: Canada Life Investments & Morningstar. Figures based on the ABI Mixed Investment 0-35, ABI Mixed Investment 20-60 & ABI Mixed Investment 40-85 to month end Oct 2018. Calculated a thousand simulations on the actual returns of the ABI Mixed Investment sectors. Each simulation randomly mixed the last 30 years of returns (to account for sequencing risk) to help calculate the likelihood of the pot lasting. **Past performance is not a guide to future performance. The value of investments may fall as well as rise and investors may not get back the amount invested.**

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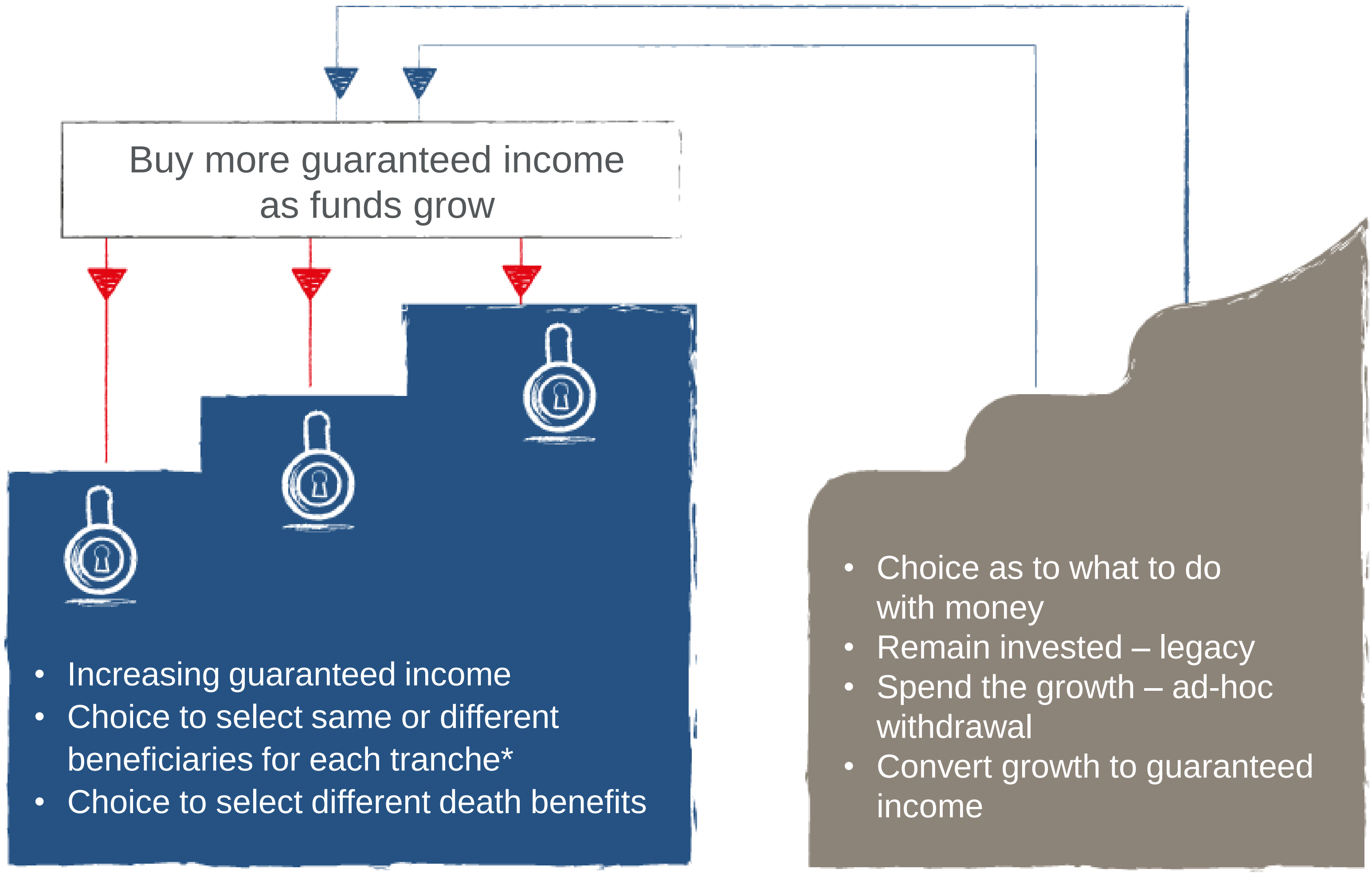
Buying more guaranteed income:
create increasing income and de-risk portfolios

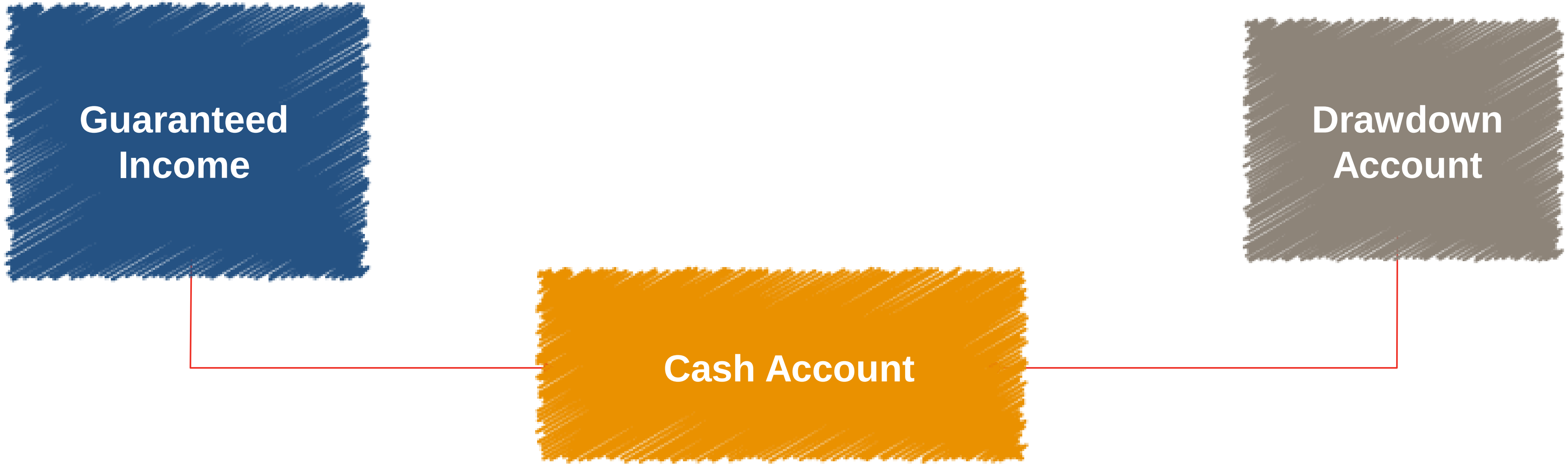


Reasons to buy more guaranteed income:

- Attitude to investment risk changes
- Health worsens
- Rates get better with age
- Mortality drag

* For dependant or dependant + Income Guarantee options a spouse or civil partner must be named when the guaranteed income is purchased; or an unmarried partner who is living with and financially dependent (or interdependent) on the policyholder when the guaranteed income is purchased.

Flexibility: reinvest surplus income



Guaranteed income can be held in the cash account or invested into any of our investment solutions without leaving the wrapper. Therefore:

- Not treated as a contribution as income hasn’t left the wrapper
- Not taxed as it hasn’t left the scheme
- Access when needed and annuity income can be re-started at a later point

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Key aspects of a CRP

Investment

Investment strategy
Sequence of returns
Inflation

Income sustainability

Withdrawals
Investment return
Longevity

Managing tax

Withdrawals
Lifetime Allowance
Death

Others

Vulnerable clients
Death of partner/divorce
Regulatory/political

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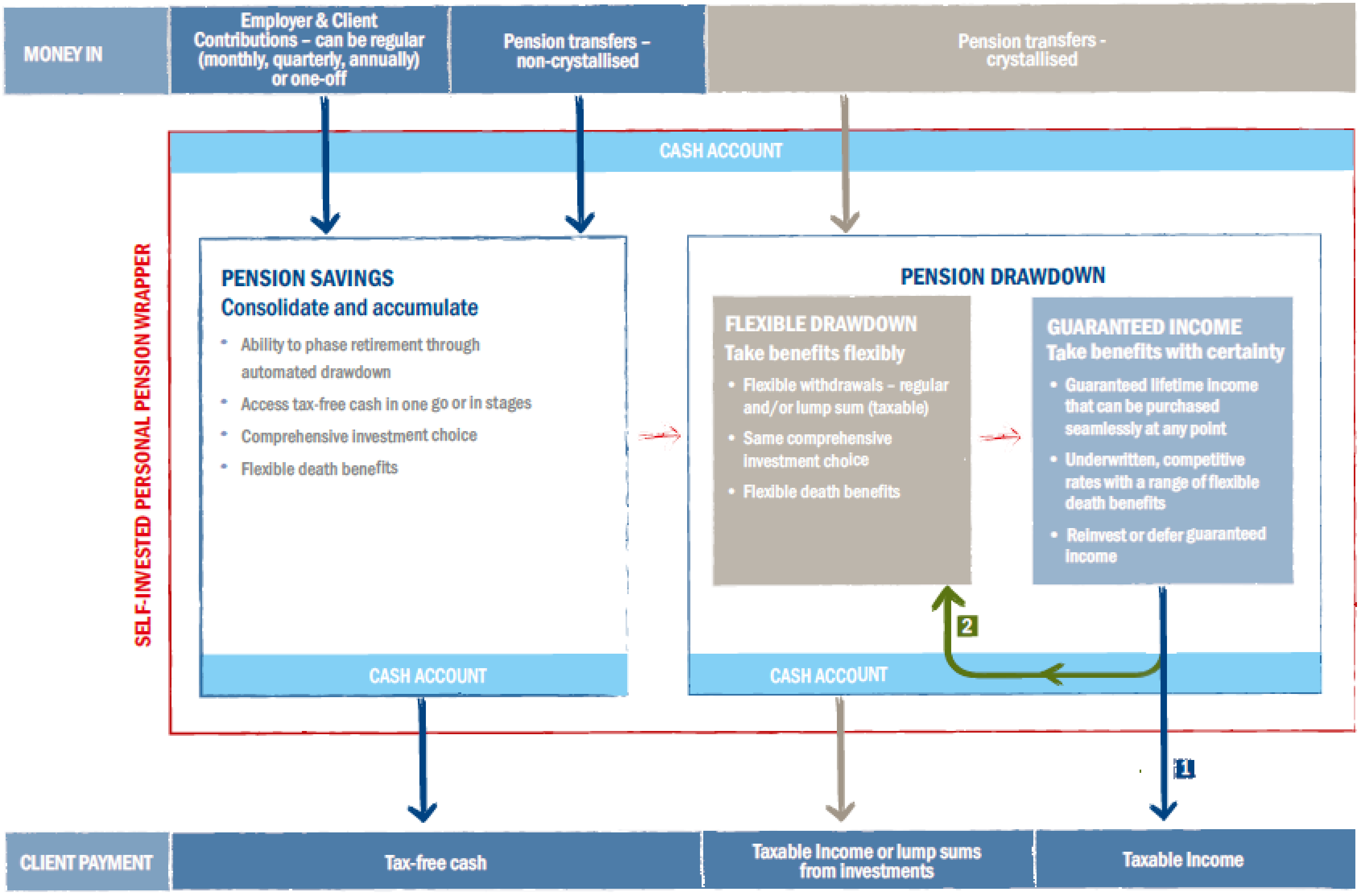
The Retirement Account: product structure



With guaranteed income, you can:-
1 Take income (taxable)
2 Reinvest income*

* Guaranteed income can be seamlessly reinvested in Pension Drawdown through any of our investment solutions or left in the cash account. No tax payable until the income is paid out.

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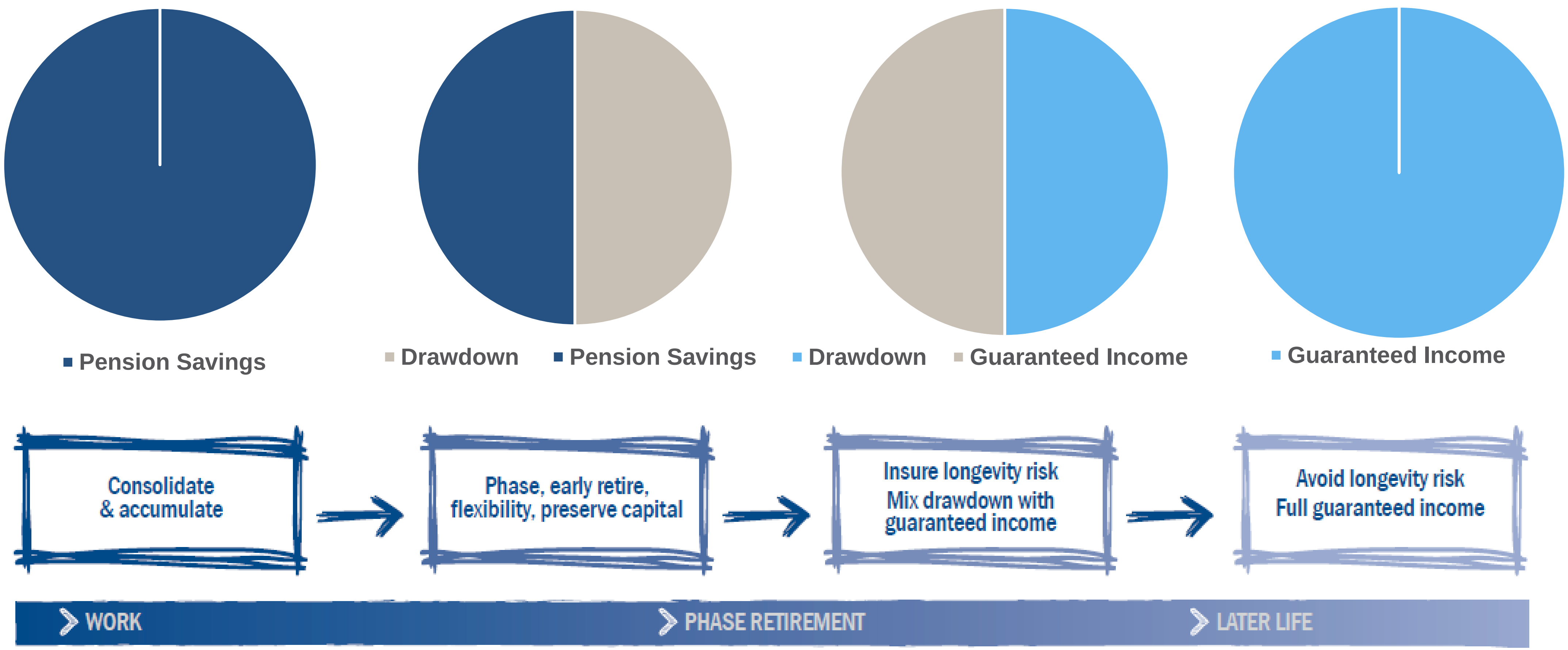
Integrated retirement account

It's suitable whether clients are still working, close or at retirement.



This is an example of how The Retirement Account may be used

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Phased Drawdown

The Retirement Account allows phased drawdown which provides clients with the ability to:

- Control the mix of tax-free cash and taxable income
- Phase only tax-free cash (MPAA will not apply so retain annual allowance)
- Phase tax-free cash and some income, (for example to use up the remainder of the basic rate band but not higher rate)
- Phase tax-free cash in stages (there's the potential to generate more tax-free cash from the accumulation replacing what's been spent – dependent on investment growth) *

Early retirement

Reducing working hours

Tax planning

Bridging income gap

University fees

*The value of investments can go down as well as up

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Do you have any clients like these?

Defined Benefit transfers

Defined contribution pension consolidation

70 + Income Drawdown

Drawdowns up to £300,000

Existing Guaranteed Pension plans

Low risk Investors 80/20 Drawdown

Active Investment

Passive Investme

Blended Investment

Model Portfolios

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So…

Clients are looking for a solution with the following qualities …

- ✓ Consolidation facility so they have everything in one place
- ✓ The ability to make regular contributions or one off payments
- ✓ Flexible enough to change when their circumstances do
- ✓ Access to a wide range of investment options
- ✓ Tax-efficiency for themselves and their families with a range of death benefits
- ✓ True blend of pension savings, guaranteed income and pension drawdown

Welcome to **The Retirement Account**

You're in control

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- Oldest Canadian life assurance company, formed in 1847
- Operated in the UK since 1903
- Canada Life (UK) Ltd is part of Great-West Lifeco
- Financially strong

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Contact us: Canada Life adviser support & commitment

Wealth Management
Onshore & Offshore Bonds
Comprehensive trust offering
Low cost innovative Retirement Account

Enquires: 0345 606 0708 or your local Sales Consultant

Asset Management
Core and Governed range of low cost risk targeted and risk managed, active and passive portfolios

Enquiries: 0345 606 6180

Insurance
Group and individual protection (pension, non pension & bespoke solutions)
Protection: Individual
Annuity: bulk and individual

Enquiries 0345 223 8000

Home Finance
Main residence
Second home
Buy to let

Enquiries: 0800 068 0212 or your local Sales Consultant

Award winning *iCan* Technical Support Team
Email: ican@canadalife.co.uk

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Learning outcomes

- Discuss how a holistic approach can be adopted by advisers to deliver flexibility and certainty for clients in retirement, with reference to the FCA's 'Dear CEO' letter of January 2020.
- Demonstrate the pros and cons of income sustainability, exploring the 'probability-based' approach and methods often used as part of this
- Explore the pros and cons of securing some essential incomes using state pensions and a client specific guaranteed income within a flexible drawdown proposition
- Explain how Pension Freedoms created space for innovation that Defaqto have written about. Resulting in an award winning retirement solution, combining pension savings, income drawdown and guaranteed income within a single wrapper

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Thank you – Questions?

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