Summary
• Early reports indicate that the 'inertia factor' has persuaded most workplace pension scheme members to accept higher minimum contribution levels rather than opt out.
• The real test could come in April 2019, when the second of the two-stage increase kicks in.
• While opting-down is an alternative that cash-strapped employees can explore, the onus is on them to request it from their employer.
• Many employers could do more in promoting the culture of regular savings and making better provision for retirement.

Auto-enrolment: A pivotal moment

The first of two increases in minimum contribution levels kicked in from April, triggering fears that some workplace scheme members could either opt out or opt down

An increased minimum wage and higher personal tax allowance cushioned the impact, but an estimated 5.6 million people auto-enrolled in workplace pension schemes might have noted from the latest payslip that a bigger slice of their salaray is now taken.

From April the minimum contribution rose to 5 per cent from 2 per cent, as the employee's contribution tripled to 3 per cent and that of the employer doubled to 2 per cent. A further rise, to 8 per cent, is due in April 2019, with 5 per cent coming from the employee and 3 per cent from the employer.

By any measure, auto-enrolment in the UK can be rated a success. Since its introduction in 2012, around nine

million people have been enrolled into a workplace pension by around one million employers. Government forecasts that around two in three workers would opt to remain in their company's scheme proved overly pessimistic as the actual figure has been 90 per cent.

So will the two-stage increase derail this success story? It's still too early to gauge the impact, but the Society of Pension Professionals (SPP) president Hugh Nolan is encouraged by reports that few employees in auto-enrolment schemes have yet decided to opt out.

"Employees paid weekly will have noticed the change, but it's likely to have registered only recently with those on a monthly paycheque," he notes. "The tripling of the employee contribution might sound substantial, but the actual amount involved is small and those on, say, no more than £10,000 a year will notice little difference.

"Given the improved minimum wage and higher tax allowances, possibly the real impact won't be felt until the second increase in 2019."

Nolan's view is supported by JLT Employee Benefits head of DC investment consulting Maria Nazarova-Doyle. "This year's increase will go largely unnoticed as my experience suggests a large proportion of companies have been originally auto-enrolling employees on a slightly higher rate than the AE minimum anyway," she suggests. "So, for many firms the first round of auto-escalation has been a non-issue as they are already in that camp.

"However, next year's jump from 5 per cent to 8 per cent next year will be felt a lot more. My concern is that many people will notice what will be a substantial deduction from their paycheque, particularly for relatively low earners whose disposable income will be squeezed even further."

Nazarova-Doyle wants the pensions industry to concentrate over the next 12 months on educating DC savers on the importance of saving for later life. "If we do not succeed, it may be that the power of inertia alone will not be enough to keep people in DC schemes," she warns.

A recent report by the Finance & Technology Research Centre (F&TRC), *Making Saving Affordable*, also questions whether next year's increase may squeeze some scheme members too hard. "Speaking to employees and financial advisers, it's clear that most people are aware they need to save regularly and make their own provision for retirement savings on the basis that state provision may have disappeared in, say, 50 years' time," says the Centre's head of workplace research, Jason Green.

"But as the report finds, for millennials what might happen in 2068 ranks as a fairly low priority."

Green also points out that while an employee contribution of 1 per cent represented around 4 per cent of their disposable income, April's rise to 3 per cent lifted that percentage to 13 per cent. "Next April's further increase to 5 per cent will equate to 21 per cent of disposable income or one-fifth of their salary.

"Workshops the F&TRC has conducted with millennials and feedback we've received suggest this will be too much for many, who may have no choice than to opt out rather than cut back on other expenses. Too many people struggle with their day-to-day finances and may find saving for an event so far in the future impossible when they're suffering financial stress."

Maintaining momentum

If the inertia factor is starting to wear off, the message that enrolling in a pension scheme and saving regularly is worthwhile needs to be emphasised.

"What's really important is that we focus on the significant increase in wellbeing that will result from people, many for the first time, building up a decent retirement savings pot," says Nest Insight executive director Will Sandbrook. "For someone earning around the UK's average income, the recent increase in minimum contributions could mean paying less than one pound extra per day, and if they keep saving, a pot of around £125,000

could be waiting for them at retirement.

"The incremental increases are an excellent helping hand to get people saving enough for their retirement, but engagement also has an important role to play. Exploring how to engage savers at the right times is a key challenge that the industry is looking to tackle."

The TV advertising campaign periodically run by the Department of Work and Pensions (DWP) to promote auto-enrolment under the slogan 'We're all in!' proved successful in generating enthusiasm for the concept. However, it carried "an air of finality" and marked only a start in getting people more involved in their own pension provision, says Like Minds communication consultant Trevor Rutter.

"Pay increases might have begun rising again after more than a decade of negative growth, but there's a lot of catching up to do," he notes. "Indeed, it seems likely that the lifetime earnings of the current generation of millennials will for the first time fall below those of the preceding generation.

"However, there's much potential in communicating the importance of retirement savings so that it becomes more real to people. That means talking in real money terms rather than percentages. You need to make it something people can relate to; for example by explaining while their payslip might show them £5 worse off that's offset by £20 being put into their pension plan.

"At the corporate level, companies could be encouraging employees to save for a number of reasons, not only pensions. More are offering savings schemes and company share plans. Those able to take a more creative approach will stand out from their competitors."

Indeed, recent research by trust-based DC workplace scheme The People's Pension shows one in five employers intend to pay more than the minimum contribution this year, reports head of policy, Andy Tarrant – but a growing number are unsure whether to pay more than the minimum in 2019.

"We know that the majority of employees highly value their employer pension contributions as an important benefit and consider them when looking for a new job," he adds. "So, increasing employer contributions above the minimum requirements may not only help employees save for their retirement but could also benefit businesses when it comes to recruiting and retaining staff."

The consolidation of small pension pots into something more substantial, such as via a pensions dashboard, could make a difference and persuade more employees to take an interest in their pension provision, says Royal London director of policy and external communications Steve Webb.

After the April 2019 increases push the overall rate to 8 per cent, it's likely that contribution levels will stay unchanged for some time – although "a figure of 12 per cent would be a more realistic than 8 per cent in providing adequately for retirement," notes Scottish Widows corporate pensions relationship specialist Robert Cochran.

He cites Australia as a country that has handled auto-enrolment more deftly than the UK. Its own scheme, the Superannuation Guarantee Fund, was introduced in the early nineties "at a time of economic growth rather than at the tail end of a major financial crisis".

In 2002 the minimum contribution level was increased to 9 per cent of annual salary and over the six years 2013 and to 2019 it is steadily being raised, via increments of 0.5 per cent, from 9 per cent to 12 per cent.

A realistic option?

Conversely, there have been predictions that some cash-strapped British workers might choose to 'opt down' and reduce their contribution rather than opt out of schemes. It's not an alternative that The Pensions Regulator (TPR) wants employers to publicise, so the onus is on the employee to specifically request it and the employer must ensure that he/she understands the implications of opting out.

"While opting down is in essence better than opting out altogether, the resulting shortfall in retirement will be so large that it may negate the benefits of saving anything at all," notes Nazarova-Doyle.

She notes that after various estimates, the industry consensus is that to have a fighting chance of a reasonable standard of living in retirement, instead of "a cliff edge into poverty," any savings rate below 15 per cent of income will prove insufficient. "So instead of offering an opt-down, we should be looking at different approaches to increase the contributions rather than decrease them.

"For example, the US uses an approach whereby an employee 'pledges' part of their future salary increases as an additional pension contribution. It's less difficult to give up something you don't yet have and when the increase in contributions coincides with a salary increase it's also less noticeable."

Written by Graham Buck, a freelance journalist