Summary

- Current financial literacy amongst savers is low.
- The industry has not been very good at communicating investment matters in an engaging manner.
- The focus needs to be on improving savers' understanding and confidence around investment concepts.
- Basic improvements in financial knowledge can help avoid investment scams and help individuals look past any wariness they may have of the financial sector.
- There is a debate whether savers should be encouraged to make their own investment decisions during the accumulation stage. However, it is increasingly necessary for them to make investment decisions themselves when approaching retirement, due to the freedom and choice reforms.
- Peoples' attitudes toward making their own investment decisions can broadly be split into three categories – 'capable', 'willing to learn' and 'not interested'.
- Following freedom and choice, all areas of the industry need to focus on and improve how they communicate investment matters to members.
- Members can receive investment information through a mix of pensions communications, advisers and online tools.
- It is recommended that communicating investment matters is done using plain, simple language and through the use of relatable examples.

Talk money

The freedom and choice reforms mean an increasing number of people will have to understand investment matters, having never done so before. Laura Blows explores the current level of investment knowledge and interest amongst DC scheme members, how to communicate investment matters and why improvements need to happen fast

"We are in the process of people moving from savers to investors as a result of the freedom and choice reforms", former shadow pensions minister and Aberdeen Asset Management head of retirement saving Gregg McClymont declared at a recent PLSA event.

Freedom and choice has meant that people now have more choice with what to do with their money at retirement. As Columbia Threadneedle head of pensions and investment education Chris Wagstaff says: "We have moved away from collective passivity to individual responsibility."

But are people prepared to handle this responsibility, and do they even want it?

Low financial literacy

Overall financial literacy amongst the public is generally low. According to Nest's *Improving saver confidence in saving for retirement* report, many do not even broadly understand how pension saving works, considering it akin to a savings account, never mind understanding how the complex world of investment works underneath.

For Newton head of DC Catherine Doyle, the absence of financial education in the school curriculum until recently has meant that basic financial concepts are viewed as challenging to the average saver.

"Although the industry has given up on the idea of education, this issue does need to be addressed if individuals are to appreciate the value of long-term savings. If they remain unaware of basic financial concepts such as compounding, pound cost averaging and value for money, their level of engagement is destined to remain woefully low," she adds.

However, a lack of understanding is not the same as a lack of caring. Nest's research indicates that historic disengagement should not be interpreted as apathy.

"In fact, consumers are extremely passionate about building a retirement income, and what interests and concerns them the most is investment – though they are unlikely to put it in those words. For them, what happens to their money, how 'safe' it is and what they can expect to get out at the end are of the utmost importance and together define the product," it explains.

One reason why it is difficult for many people to become interested may be because the industry simply has not been very good at communicating investment matters.

The industry has a duty to communicate these issues, of course, and The Pensions Regulator provides guidance about communicating investment choices to members. This includes ensuring members are regularly made aware of their investment strategy and what this means for them, clearly naming funds and explaining their risk profiles, providing quality information and for costs and charges to be presented in a clear and simple format.

However, Nest's research found that when presented with a standard disclaimer for retail investment products – such as that investments can go up as well as down and there is no guarantee that you get back all the money you invest – participants responded with anxiety and lost confidence in the product, as the statement was taken as a warning against the product rather than simply being transparent about the risks.

Improving knowledge and confidence

So, if messages such as the above do not work, how should the industry be communicating investment matters?

We have moved on from the industry trying to teach people to become knowledgeable investors. After all, as Nest says in its report, "evidence from behavioural sciences and the impact of financial education projects suggest that gains in financial understanding does not necessarily improve financial decision making".

Instead, the focus needs to be on improving savers' understanding and confidence around investment concepts.

For instance, Nest found that the word 'risk' has a negative connotation for members, so instead of explaining risk, a better approach may be to discuss how the downside of risk is managed. "The priority should be on reassurance rather than boosting financial literacy," it adds.

To reassure about volatility, Redington head of DC and financial well-being Lydia Fearn says communications should be framed to demonstrate that while there is volatility in the market over the short term, in the long term equities can add value.

Also, equipping savers with just a basic investment understanding can help them make better investment decisions, such as avoiding scams.

Providing information to members about the current low interest rate and low inflation environment, and that it doesn't matter as consistency of returns is what is important, could help them see when a potential scammer provides them with a message that is 'too good to be true', Wealth at Work director Jonathan Watts-Lay advises.

Another murky area to address is the preconceived notions members may have – their glimmers of investment 'knowledge', such as equities being a 'risky' investment, their house alone being their retirement investment, or, in Wagstaff's example, that a conversation in the queue at a fish and chip shop is enough investment 'advice' needed to make investment decisions.

Whose responsibility it is to counter these notions is still subject to debate, Willis Towers Watson head of DC investments Nico Aspinall says, because "as soon as the industry talks about these things they run the risk of it being 'advice'".

Accumulation versus decumulation

It is also because of the old adage that a little knowledge is a dangerous thing that many are sceptical of encouraging people to make investment decisions during the accumulation stage.

However, Wagstaff expresses concern that people in default funds do not know what they are invested in, and simply trust that it suits them the most. "It is difficult to make people competent and confident to invest outside of the default," he says, "and we would be misplaced to do this in any great degree, but some on the margins could do better."

While the vast majority of people being in defaults during the accumulation stage has been a cause of concern for the industry, Doyle points out that there is a category of active defaulters who have reviewed the default fund and has actively chosen to place their money there.

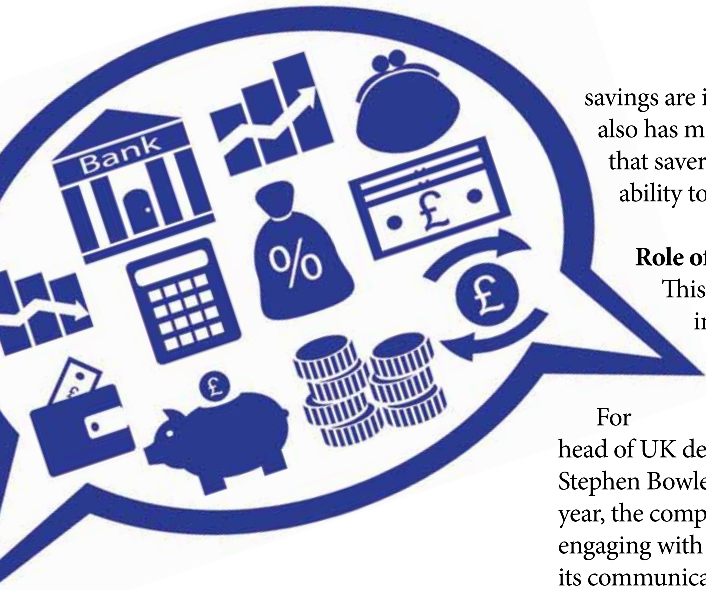
"Striving to move savers towards this middle ground through an increased appreciation of long-term investment and savings would seem to be a reasonable and achievable objective for the industry," she says.

Despite the wariness of people making investment decisions during the accumulation stage, thanks to freedom and choice, by the time individuals approach retirement they need to become more financially aware than they currently are.

And there does seem to be a willingness to learn. A recent PLSA report, *Pension freedoms: No more normal*, which surveyed people aged 55-70, found 55 per cent wanted to research and make decisions about funding their retirement themselves, while 33 per cent wanted the product research done for them, but they make the final decision. Just 10 per cent wanted someone to do both the research and choosing for them.

Different types of saver

The association also discovered that those with DC pots not yet in payment fell into three categories when considering their retirement options – 'investigators' (63 per cent), inactives' (23 per cent) and 'actioners (14 per cent)'.



However, PLSA is not the only company trying to analysis member responses to investment communication. Nest found four distinct groups of people when presented with investment-related information – the cynical, the compliant, the cautious and the curious.

Likewise, Fearn, categorises savers into 'do it for me', 'some help needed' and 'self selectors'.

Individuals themselves understanding the type of investor they are, for example the degree to which they are risk averse, could help them understand if they are invested in the best way for their attitude and needs.

However, there are concerns about the usefulness of risk-profiling questionnaires – the online surveys that make you just a few clicks away from understanding your attitude towards investment risk.

According to Aspinall, getting a 'static reading' on risk is tricky, as "if people are asked if they are risk averse during a drop in the market they are more likely to state they are". Therefore, tools such as online surveys assessing an individual's attitude to risk is useful as a 'hook' to get people engaged, but "I am worried about it being used to make financial decisions", he adds.

Thanks to freedom and choice, individuals are increasingly responsible for determining how their retirement savings are invested. But the industry also has more responsibility, ensuring that savers have the information and ability to make these decisions.

Role of the industry

This is affecting all areas of the industry, including those that previously were not so customer-facing.

For instance, Schroders head of UK defined contributions Stephen Bowles says that over the past year, the company has spent more time engaging with the end user to develop its communicative skills when talking to trustees and members.

There are many ways in which savers can get access to the information they require. Despite the low take up of Pension Wise, PLSA, among others, feel it has an important role to play in increasing member understanding, along with the use of online tools such as websites, social media, apps and so-called 'robo-advice'.

"Online tools can help savers understand their investments better, and 'robo-advice' will provide the opportunity for more engagement with savers' investments," Selectapension national account director Peter Bradshaw says.

For some, getting advice from a human instead will also be extremely helpful. However, Aspinall expresses a note of caution. For instance, he says, an IFA may struggle to promote buying an annuity as they cannot know if it is good value for money until it is known whether the recipient lives for a long time.

Best practice

No matter the method a member may use to gather information, the most important thing is how the message is communicated.

Plain, simple language is a must. Members also need to be reassured that making choices is not necessarily complicated.

Bowles feels that a lot of 'signposting' is needed for members, including sticking to a couple of key messages and continually repeating them.

It is recommended that best practice should be designed around the behavioural framework EAST, meaning that communications should be easy to understand, attractive, social by enabling people to chat about choices and timely.

Like Minds communications consultant Trevor Rutter highly recommends case studies to help members understand complex investment matters and choices. "Providing real examples through case studies drags pensions into peoples' real lives," he explains. "It highlights the practical implications of all this far more than talking about stocks and bonds. However, the information needs to be put in the wider context of their overall savings and retirement aims."

According to Nest's research, connecting people with what happens to their money is helpful, as for those with the worst preconceptions about investment, it shows that thought is given to the management of their money. Giving examples of real companies in which their money is invested also provides a better a mental picture for members, it adds.

It is this idea of ensuring that investment matters are explained to members in a way that is relatable and easy to understand – without being patronising – that is key. As Rutter says: "At the risk of sounding like a bad 90s rapper – keep it real."

Written by Laura Blows