Something's gotta give

Summary
- The impact on individual pension scheme savings varies greatly based on factors such as age and scheme type – but all have been impacted by Covid-19.
- How members will react is still yet to be seen, although it seems likely that more may turn to their pension to supplement income where possible.
- Prioritisations must take place, and auto-enrolment is likely to be hit, but the industry can support members in rebuilding their funds after the pandemic.

As Covid-19 sends the markets into flux, Sophie Smith looks at what impact it has had on pension scheme savings, and whether pensions should be a priority for savers in the current crisis

"Good pensions depend fundamentally on a strong economy," highlights Lane Clark and Peacock partner and former Pensions Minister, Steve Webb, "so there is no doubt that the current crisis will have a significant impact on pension outcomes". He clarifies, however, that what that impact is will differ vastly depending on a range of factors, such as age or pension type, and on the actions taken by members themselves.

"The volatility and market falls we've witnessed lately will have unnerved many savers," adds Canada Life technical director, Andrew Tully, stressing that "anyone tempted to look at the value of their pension today is likely to be in for a shock". And while those in DB schemes will be pleased to learn that they have been somewhat protected by the headline-grabbing market falls, those in the DC space may not have the same reassurances, stresses Pensions and Lifetime Savings Association (PLSA) head of DC, master trust and lifetime savings, Lizzy Holliday.

"For those in DC schemes, information about falling pot values will be worrying, and so it is important that the industry gets the message out that pensions are about the long term," she explains. The regulator itself has also stressed the importance of getting member messaging right, most recently calling on trustees to issue a letter to any DB scheme members who wish to transfer to DC, in order to warn them of the potential risks.

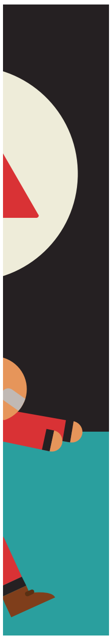
Falling on deaf ears?

But whether members will genuinely hear this message is yet to be seen, as Tully emphasises that "it's simply too early to call how scheme members are going to react to the global pandemic". Echoing this, Nest director of strategy and corporate affairs, Zoe Alexander, confirms that member activity hasn't been out of the ordinary for the scheme, clarifying that despite a peak at the end of February, member website visits and pot access have remained steady, or even slightly lower, than that seen at the start of the year.

However, there are suggestions that trends are beginning to emerge, with Intelligent Pensions technical director, Fiona Tait, pointing out that there has been discussion with clients about delaying access to their pension plan or reducing their current levels of withdrawal and using other deposit-based assets to fund current income needs. She highlights that while this is a "tax-efficient strategy", other anecdotal evidence has pointed towards more concerning trends amongst members.

Digging a hole

"We have heard anecdotally that some older individuals have chosen to withdraw all of their pension savings as a result of the crash in order to invest 'safely' in cash," Tait explains, "this not only consolidates their losses but is also likely to result in a considerable tax bill,



as well as the loss of tax-free growth on the invested funds".

Recent research from AJ Bell also suggests that savers may be beginning to approach their retirement funds to supplement their income, with 11 per cent of over-55s with a pension having either already accessed, or planning to access, their retirement pot earlier than anticipated, due to the pandemic.

It is not only those who are approaching retirement who will be feeling the strain during the current crisis though, and as Alexander notes, these are "difficult and uncertain times across the board", with many people struggling financially.

"If household budgets come under strain as a result of the economic effects of Covid-19, there is certainly a risk that some people may choose to cut their contributions or even choose to opt out of auto-enrolment (AE)," states Holliday, stressing that savers who choose to do so will not only miss out on the traditional incentives, such as employer contributions, but also any investment growth that could occur as the markets recover.

And whilst Nest data could seem reassuring, showing no marked increase in opt outs or cessation, Alexander emphasises that this could yet change as the situation progresses. Tully however, argues that a dip in contributions is already well under way thanks to the government's job retention scheme.

"One of the unintended but clearly acknowledged consequences of how the scheme operates is a reduction in member contributions as a result of individuals' pay decreasing", he explains, adding that many employers use salary sacrifice for pension arrangements with furlough potentially altering this also.

Considering the circumstances though, it seems likely that members may not even notice such changes, and while industry experts such as Holliday are quick to highlight key incentives such as tax relief and employer contributions, many savers may still be wary of prioritising their pension when they may be unsure of whether their employer will even exist in a year.

A mountain out of a molehill?

"Any break in paying contributions has a clear impact on the final result," argues Tully however, noting that longer savings time horizons are in fact particularly worse hit because of two factors.

"The power of interest compounding has a greater effect the longer you have to save, and by not buying into equity markets now means people will miss out on any recovery," he explains. Agreeing, Holliday notes that ideally a person would opt out for as short a period as possible, especially if they are quite young and therefore potentially missing out on years of investment growth.

Webb however, highlights that younger workers will have more time to recover, provided that they stay in work, and therefore should be in a better position to weather the current crisis in the long term. But even those who are fortunate enough to gain back financial stability after the crisis could face obstacles when trying to rebuild their pension, with Webb highlighting the Money Purchase Annual Allowance (MPAA) as a "real barrier".

The journey to recovery

"The MPAA has long been viewed by many as an unreasonable restriction," agrees Tully. "People being able to take some of their pension in this unprecedented situation can be hugely beneficial. In future members may want to make up for those withdrawals by paying in more to their pension, so it seems bizarre the rules may restrict their ability to do so."

Indeed, the removal of the MPAA is not a new ask, and as Tait emphasises, was already viewed as somewhat of an anachronism within the context of pension freedoms. However, while industry experts seem united against the MPAA, just what to do to best ease its effects is a slightly more divisive issue. For example, while Tait and Webb acknowledge the benefits of an easement or relaxation of the allowance, others have argued more staunchly for its complete removal, and even for those willing to consider easements, there is a difference in approach. Webb, for instance, has previously suggested that the limit be increased to £10,000, meanwhile Tait suggests a relaxation of the rules that would allow people who have withdrawn funds during the coronavirus window to make contributions up to the normal annual allowance until their fund reaches pre-crisis levels.

One thing that is for sure though, is that this is an area that the industry seems keen for change in, especially to support those members worst hit by the pandemic. Tully emphasises that while the government may have been reluctant in the past to make changes to the MPAA, "lately we have seen dramatic changes to many rules", which should make the scrapping or amending of MPAA "minor in comparison, but nonetheless a change the government should make".

One step at a time

These issues are not necessarily the top priority for many savers currently however, and as Tully notes, pensions are, quite rightly, playing second fiddle to overall family health.

"We all have a role to play in proactively communicating with members, whether that be advisers, schemes or providers," he adds, and ensuring there are not obstacles working against members who try to do the right thing in rebuilding their savings is just a part of this. But it is this almost invisible support that will allow the industry to protect members, supporting them when cuts must be made, and encouraging them back once the time is right.

Written by Sophie Smith