

# DC adequacy: Action needed to match intention

✔ **Clare Freeman and Steven Leigh explore the work DC schemes can do to help members achieve adequate retirement outcomes**

Pension schemes' overriding purpose is to help members save for an adequate retirement. However, defined contribution (DC) schemes have not always been able to articulate what an adequate retirement looks like or, importantly, to identify whether members are on course to achieve it.

Aon's *DC Pensions and Financial Wellbeing Survey 2022* received responses from DC pension schemes across many industry sectors, sizes and types, covering over half a million members.

It was encouraging to see in this research that the most popular aim for DC schemes (46 per cent of respondents) is to deliver an adequate retirement outcome for members. This is a significant shift from 29 per cent in 2020. At that point, benchmarking with peers was the biggest priority.

This change of mindset is badly needed. Our 2021 employee research, *Keeping on track in challenging times*, found that one in three individuals expects to work to age 70 or beyond, and one in four think they may never be able to afford to retire. That uncertainty was being fuelled by concern over poor pension outcomes.

Focusing on outcomes is a step in the right direction, but schemes have work to do to make sure they understand whether members are on track to retire. Our 2022 research found that most schemes (63 per cent) said that they did not know the expected outcome for a typical member of their DC scheme. This is a real cause for concern as it is vital that those making pension scheme decisions understand the

**63%** of schemes do not know typical member outcomes

membership. A starting point would be to review an annual benefit statement for a recent joiner and use this as a baseline for the sort of outcome a member might expect.

The next question is whether this is likely to be enough. Among respondents who said they do know typical member outcomes, the Pensions and Lifetime Savings Association's Retirement Living Standards are the most common method used to assess outcomes (22 per cent of respondents). These 'rule of thumb' guidelines for retirement adequacy have rapidly overtaken the replacement ratios measure for schemes.

Twice as many use 'Retirement Living Standards' compared to 'Replacement Ratio'

It is not just pension schemes that have a knowledge gap. Just 19 per cent of respondents say that their sponsoring employer takes pension outcomes into account as part of its future workforce planning. Poor outcomes could result in future challenges for businesses, including rising employment costs, lower workforce engagement and succession planning issues.

Building an accurate picture of retire-

ment adequacy across a workforce can be complicated. For example, by the time most people approach retirement, they will have savings in multiple workplace schemes, as well as other personal savings and state pension accrual.

However, reasonable assumptions can be made and combined with data from your current DC scheme to create a better understanding of whether pension scheme members are on track.

Tools such as Aon's DC Analytics can help. DC Analytics assigns a retirement target based on the Retirement Living Standards taking into account expected salary at retirement. It then includes state pension and other work-related pensions, as well as future returns. Based on this information, it creates a summary across the scheme of whether members are on track for an adequate retirement.

Schemes can react to any shortfalls by targeting communications to groups of members, encouraging them to increase their own contributions or to help them understand their likely retirement timelines. Employers and trustees can also help to improve the likelihood of members being on track for a good pension outcome, by adjusting contribution design, or by enhancing the investment strategy.

Ultimately, our 2022 research shows that schemes really want to improve member outcomes but lack the data and insights they need to act on that intent. Understanding current adequacy and putting a plan in place to drive improvements are crucial next steps in DC pensions to making a genuine change to pension outcomes.

Download the Aon DC survey here: [aon.io/3u4c73c](https://aon.io/3u4c73c)



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