Summary
- When the Covid-19 pandemic first took hold, there was a decline in pension withdrawals, potentially due to the investment market volatility and job uncertainty.
- The latter part of the year saw an increase in withdrawals, but still of lower amounts than 2019. However, in Q3 2020, a higher number of people were accessing their pensions than earlier in the year, which may be as a result of the pandemic starting to negatively affect their finances.
- There may be long-term consequences for individual accessing their pension pot earlier than they expected, such as a reduction in the overall amount saved for retirement, and the risk of falling foul of the MPAA if/when the person starts paying pension contributions again.

Calm before the storm?

The Covid-19 pandemic created concerns that over-55s may raid their pension savings to plug any financial gaps caused by the crisis. However, while the initial response was calm, withdrawals are starting to rise again and the retirement saving decisions made now may have longer-term consequences, finds Laura Blows

Amongst the many fears generated by the Covid-19 pandemic when it first started to take hold were the concerns that people may turn to their pension savings to help them through any financial difficulties caused by the crisis.

Thankfully, these initial concerns that there will be a quick dash to the pension pots seem to be unfounded. Instead, the opposite seemed to occur.

Initial response

According to The People's Pension, director of policy and external affairs, Phil Brown: "We have not seen any significant increase in the numbers of any type of withdrawal from The People's Pension over the past year. Saving into workplace pensions has so far proved to be highly resilient to the pandemic."

In fact, once the pandemic took hold, PensionBee saw a decline in the number of withdrawals from pension pots.

"At the start of 2020, the withdrawal rate for PensionBee customers over 55 was approximately 30 per cent, matching that of Q1 2019," PensionBee CEO, Romi Savova, says.

"But as the pandemic hit in March, customers responded to the economic uncertainty by opting to keep more of their money invested. In turn, we saw only 20 per cent of customers over 55 withdraw in Q2 2020, compared to 33 per cent during the same period in 2019. From Q1 to Q2 2020, the median withdrawal amount also decreased from £8,000 to £6,500."

This depressed activity is also reflected in the numbers booking appointments with Pension Wise, Just Group group communications director, Stephen Lowe, notes. Overall, its numbers are running about 20 per cent down on last year but in the first three months of the lockdown, they were around 40 per cent down, he adds.

ABI head of long-term savings, Rob Yuille, attributes the decline in withdrawals to a combination of factors, including people holding off making decisions while the investment market turmoil earlier this year negatively affected their retirement fund value, and while there was/is increased job uncertainty.

This can also be viewed in a positive light, as Canada Life technical director, Andrew Tully, explains: "It is encouraging to see that people haven't necessarily been rushing to their pension pots to help support their finances through the pandemic. It is worth noting as well that for many the ability to spend has been limited due to lockdown so the idea of using your pension as a cash machine for larger withdrawals for holidays or home improvements is less likely to appeal."

Later uptick

However, things started to move again as we entered the latter half of the year.

A total of £2.3 billion was withdrawn from pensions flexibly in Q3 2020, HMRC finds, which is a 2 per cent year-on-year decrease in comparison to Q3 2019, but remains on par with the total observed in Q2 2020. The average amount withdrawn in Q3 2020 was £6,700, a 7 per cent fall from the same months in 2019.

While the amount may have decreased, the number of individuals taking flexible withdrawals increased to 347,000 in Q3 2020, a 6 per cent year-on-year increase and a 2 per cent rise in comparison to Q2 2020.

HMRC notes that the quarter-on-quarter increase was contrary to seasonal patterns, which "may be attributable" to the impact of the Covid-19 pandemic.

The ABI's findings also reveal a 56 per cent increase in the number of people accessing their pension as a flexible income between April and September, but with figures remaining below 2019 levels.

Comparing September data, when lockdown was starting to ease, with April, when the country was in full lockdown, the ABI finds that the number of people taking only a tax-free lump sum increased by 55 per cent, with the number withdrawing all of their pension in one lump sum increased by 94 per cent – compared to only a 51 per cent increase during the same period in 2019. However, the number of people buying a guaranteed income for life (annuity) increased by 41 per cent.

PensionBee's withdrawal figures also remain below that of 2019. With only 24 per cent of customers over 55 taking money out in Q3 2020, compared to 29 per cent in Q3 2019.

"The third quarter of this year saw an increase in both the total value accessed and the number of individuals taking these payments, compared to the previous three months," Quilter head of retirement policy, Jon Greer, says.

"This is contrary to seasonal patterns, implying more people are requiring additional cash to see them through the pandemic. Interestingly, this is the first time Q3 average value paid to individuals is higher than Q2's value since the stats were first published."

It appears the impact of Covid-19 is now beginning to feed into the figures, so it is going to be crucial watching this going forward as government support schemes are withdrawn, he adds. "It is likely many people might need to dip into their pension to cover bills and expenses, particularly during the early part of next year when mortgage and credit holidays are due to come to an end."

Determining trends

Watching for trends may not be so easy though, Lowe warns.

"We are around nine months into the pandemic and you would expect detailed data on what impact it is having on pension access," he says.

"The reality is a worrying lack of industry-wide data and poor analysis of what we do have. There is no 'early warning system' to spot emerging problems from DC pension access as there is for transfer requests from DB."

Lowe gives the example of the appearance of FCA chief executive, Nikhil Rathi, before the Treasury Select Committee (TSC) on 4 November, where, when asked whether the pressure on people's livelihoods due to Covid had resulted in an increase in people accessing pension pots, he answered: "We haven't data available on the early drawdown of pensions. That's something we can go away and take a look at."

According to Lowe, there has been no follow-up correspondence from the FCA to the TSC on this subject, and the next FCA retirement income market data bulletin (for April 2020-March 2021) is not due until autumn 2021, "so an earlier update would be welcome".

Conducting its own research in July 2020, PensionBee surveyed 961 people in the UK aged 55-70. It found that 22 per cent of people surveyed were more likely to make a pension withdrawal due to the pandemic, with 40 per cent agreeing that if they were to become unemployed due to the pandemic they would access their pension and take money out of it. Only 16 per cent considered reducing their withdrawal amounts on account of Covid-19-induced decreases in pension values.

Longer-term consequences

PensionBee's survey results lend weight to Lowe's concerns that, while many people appear to have acted sensibly, "this general view could well hide a significant minority who did access pension cash unnecessarily as a knee-jerk reaction to the crisis who will end up regretting their decision".

According to Savova, the majority of withdrawals that have taken place this year have been from savers aged 55 to 59.

Accessing their savings at such a young age could have a dramatic impact on their savings, Lowe finds. He gives the example that taking £25,000 tax-free cash from a £100,000 pension at age 55 will leave a pension £45,000 smaller at age 67 (about £135,000 compared to £180,000) assuming investment returns of 5 per cent after charges.

"As we move into 2021 it seems clear there will be an increasing number of people who are unemployed and therefore may want or need to access their pension to make ends meet," Tully adds.

It might not only be the individual's work status and finances driving this, but also due to knock-on effects of the pandemic. For instance, Tully says, since the start of the year, 35 per cent of grown up children have returned to the family home. "This means parents' monthly outgoings have increased by £425 a month. Many of these people may return to university, but others may remain in the family home. While that may be positive from a social and family perspective it may intensify the financial obligations on many families."

One key learning point from recent months, that is relevant at all times and not just during pandemics, Lowe says, is the value of introducing some thinking time into pension decisions.

"In the DB world, the advice requirement for fund transfers of more than £30,000 reinforces the point that this is a big decision that should not be rushed," he explains.

"In the DC environment, the expectation is that access to cash should be seamless and immediate, although we know that when given time to reflect – for example, through a Pension Wise appointment – the majority of people amend their original plan. Even when told about the implications of tax and the Money Purchase Annual Allowance (MPAA) restrictions, it's likely many don't realise the full effects until late."

The MPAA is expected to become an even greater cause for concern. Its current limit of £4,000 a year that can be saved annually for retirement once a person has access a pension pot may easily affect those who access pensions due to redundancy but then go back to work and want to join their workplace pension scheme, Tully says.

Greer is also concerned that some people that trigger the MPAA now, for example by using their pension to top-up income, will be penalised because they can't make full pension contributions when they return to work. "The MPAA rules are designed to prevent recycling, not to punish people that need to supplement their income while they look for a new job," he says.

The MPAA is likely to affect more people in the coming month, Yuille says, as people may have been forced out of work where they have been sick or furloughed, and therefore have taken money out of their pension to pay bills. If they go into another job and are auto-enrolled, "it seems quite unfair that they wouldn't receive tax relief on all of their pension because of that". Therefore, the ABI would like to see MPAA rules relaxed, or for it to be scrapped and replaced with a different vehicle to prevent tax avoidance.

This challenge raises wider questions about the support in place currently for older workers. Yuille adds.

"It is not a good outcome for a person to have to fall back on their pension and have possibly spent their entire pension savings by the time they have reached the retirement age they expected to have," he says.

"It also reinforced the complexity of making retirement decisions, as it is very difficult to know what your retirement is going to look like."

Written by Laura Blows