Summary
• DC savings play an increasingly important role in pension savings and have received greater focus from the industry as a result, particularly in light of the success of auto-enrolment.
• There is still much more to be done to ensure the market is properly supporting DC savers, particularly in relation to adequacy, engagement and decumulation.
• The DC market is still evolving and new considerations emerging, including around investment options and value for money.

Strong foundations

As the DC pensions market continues to grow, Sophie Smith considers the challenges that the industry should be considering when looking to build a strong base for future generations

DC pensions are fast becoming the norm for most Brits, with figures from the Office for National Statistics suggesting that increased participation in DC schemes has been the main contributor to overall growth in workplace pension participation since the introduction of auto-enrolment in 2012, and the dominant form of pension since 2019.

Indeed, Pensions Policy Institute (PPI) senior policy analyst, John Adams, notes that whilst DB pension schemes historically dominated private sector pension provision, the number of members in private sector DB schemes has fallen from around 8 million in 1967 to just 1.1 million active members by 2020.

"There are a number of reasons suggested for the decline in DB pensions including the cost of the schemes," he explains, "the variability of costs, including the sponsor's liability to make up any shortfall in the funding position, and how that reflects on the company's own balance sheet, the cost of administration and management of the scheme."

And HSBC Bank Pension Trust (UK) Limited trustee chief executive officer, Lisa Young-Harry, points out that not only is DC the dominant type of pension in the UK, from a member's perspective it is often the only type of pension saving of many employees, particularly younger members in the private sector.

"Consequently we are seeing a shift in industry and regulatory focus towards supporting DC members but, in our view, more needs to be done to help DC savers – as ultimately they shoulder at lot more responsibility on their savings."

Indeed, Pension and Lifetime Savings Association (PLSA) head of DC, master trusts and lifetime savings, Alyshia Harrington-Clark, emphasises that whilst everything was effectively sorted for savers in the DB landscape, that's quite different for DC savers.

"There are lots of different choices that people can make, both accumulating and decumulating, that prompt a quite different conversation about what support schemes, employers and others should be providing savers to help them to make the best decision in their savings journey," she explains.

New considerations, and new concerns

Decumulation in particular presents a consideration that DB pensions did not, as Harrington-Clark warns that whilst auto-enrolment has utilised the power of inertia, lots of savers do not realise the choices that will face them in the future.

"Schemes can play a really vital part in helping people," she says however, suggesting that providers could consider offering a soft or real default solution at decumulation, to allow savers to make "all sorts of exciting and interesting choices", whilst also providing a 'worst-case scenario' solution for savers that do not want to engage.

Adding to this, Young-Harry argues that the industry needs to ensure members are supported with education throughout their time saving, so they have more trust in pensions and are prepared to make the right choice for their circumstances at retirement.

"Even for those with larger pots looking at drawdown, more support is needed, we'd like to see more focus from providers to offering a wider range of post retirement investment options (for example focused on providing different post retirement investment solutions such as targeting capital preservation with income drawdown or measured capital consumption over an agreed period)," she continues. "This needs to be accompanied with efficient and cost-effective transfers at the point of retirement."

This is echoed by Adams, who suggests that whilst the complexity of pensions may be a barrier to engagement, improving people's understanding could be a starting point to help give them the ability to engage.

"Increasing engagement may be a way for individuals to take more control and interest in their pension savings," he continues. "It may lead to increasing contributions and therefore making better provision for the future."

Ready and waiting

The industry is willing to step up to the challenge though, with over 30 million pension savers to be targeted as part of a new cross-industry campaign designed to boost people's understanding of and engagement with their pensions.

The campaign, led by the Association of British Insurers (ABI) and the PLSA, has already received backing from 15 providers and schemes, representing 41.5 million savers and customers, as well as support from the Department for Work and Pensions, with a collective investment of at least £1 million for the organisation over the next three years.

And whilst engagement is "really difficult to achieve", Harrington-Clark argues that campaigns such as this will allow the industry to share best practice and harness learnings for the greater good.

"We're not talking about complicated choices," she clarifies, emphasising that much of engagement focuses on the basics, such as helping savers to log in to their pension and see how much they have saved.

Ensuring savers are even aware of their pensions, particularly after changing jobs, can also be a challenge in itself, and whilst Young-Harry acknowledges that pensions dashboards could be key for this, she warns that it needs to have as much information on it as possible, and in an easily accessible way, for it to be successful.

Dashboards are not the only development, however, as Adams points out that small and orphaned pots have been an active policy area with a number of suggestions, including mechanisms where pensions are automatically tracked with the individual, or some other mechanism that ensures pots are held with providers that are appropriate for the individual's current circumstances.

A growing to-do list

A focus on costs and value for money has also been emerging in the DC space, particularly in light of regulatory action from The Pensions Regulator and Financial Conduct Authority.

However, whilst Young-Harry argues that providers and fund managers should be required to fully disclose all costs, she says that this needs to be done on the value it brings the members when accessing opportunities.

"For example," she explains, "while illiquid strategies are likely to be more expensive than more passive approaches, a great deal of diversification and growth potential can be provided through these allocations. With the current focus on low costs, some providers or schemes may be concerned about adding an allocation to illiquid assets, which increases cost to members."

Adding to this, Harrington-Clark says that whilst cost disclosures are a concern, there has already been improvements in terms of the information available, explaining that how this information is communicated and ensuring it is useful for savers is instead of growing importance, particularly in light of the individual decisions that can be made by DC savers.

"A lot of regulation in DC has focussed on disclosure rather than effective governance of a DC scheme or good communication," agrees Young-Harry, noting that the consultation on *Facilitating Investment in Illiquid Assets* has suggested that publicly disclosing and explaining default asset class allocation in the annual Chair's Statement may also help members understand the investments made on their behalf, and potentially engage with the projects they are funding, potentially driving up pensions' engagement.

"We need to realise that members do not read the chair's statement and it is not an engagement tool," she argues, "and instead focus on communications that's tailored for our members, timed when they hit a life event and is digestible and to the point."

DC savings have been thrown further into the spotlight amid the Work and Pensions Committee's ongoing inquiry into pension freedoms, whilst the role of illiquid investments in DC savings has been highlighted by the government's recent changes to the charge cap, and new forms of DC are also emerging with the creation of the collective DC scheme that Royal Mail is introducing.

There is clearly no shortage of considerations on the DC horizon, and that's without even mentioning ESG, but it is a challenge that the industry is surely ready for.