Skipton Building Society J02205 Life and Money Podcast: Episode 2: Is my pension working hard enough?

Tom McDermott: Hello everyone and welcome to this special Skipton building society podcast. The aim is to help you answer the question: is my pension working hard enough? My name is Tom McDermott and I'm joined by two of Skipton's in-house experts to talk about the important role pensions could play in helping you achieve a fulfilling retirement.

Now, you might be planning to retire in the next few years. Or maybe you've got many years of work to go yet, but over this podcast we will help you to think about how you're currently saving towards retirement, ways you might be able to improve your plans and tips and how you could get your pension working. Our aim today is to help you feel more confident in how to prepare for the retirement you're hoping for so that ultimately you get to enjoy doing the things that matter to you. I'm really pleased to be joined by two retirement experts to talk us through the world of pensions. First of all, hello to Gareth Smith who is Skipton's retirement planning lead. Gareth, I understand that a big part of your role is helping to assess the pension plans of Skipton customers.

Gareth Smith: Yes thank you Tom. As said, I'm Skipton's retirement planning lead, and I very much work in the background to help our customers with their retirement planning. That mainly entails looking at regulation, legislation or taxation changes, and then making sure that our colleagues across the business are up to date on everything. So that could be from our customer research team who are helping to analyse the pensions that you may have or helping people like Kevin, one of our financial advisors to make sure that they're up to date with all this and offering the best financial advice that they can.

Tom: Excellent and you mentioned Kevin there. I'm also joined by Kevin Quick, who is a senior financial advisor with Skipton. Hello Kevin, to you too. And I gather you help a lot of customers invest into pensions and make that transition into retirement.

Kevin Quick: Yeah thanks, Tom. I work quite closely with Gareth's team and we share quite a lot of information, which then in turn means I sit down, discuss people's situations, get to know them. And the more you can know about an individual, the better you can actually provide that advice. Sit there, discuss what they're looking for, and then take things from there.

Tom: Great stuff. Now, later on in this episode, we will be joined by Daniel Reynolds, who is a fund manager at Aberdeen Standard Investments.

Daniel will talk about how your pension savings might be invested. Now, before we go any further, the opinions and information provided in this podcast are not to be taken as advice. If you are looking for advice, it's recommended you speak to a financial advisor. As with all investing, your capital is at risk and any tax treatment is based on your individual circumstances and is subject to change. Right then let's get started, shall we? So let's begin today with the basics. The term pension is something we're all familiar with, but I think it's fair to say that what's less well understood is how they work exactly. Gareth, if I can start with you, if I may, can you explain what a pension is?

Gareth: Yeah. So there's broadly two types of pensions. There's a defined benefit scheme and a defined contribution scheme. So a defined benefit, If we start off with, that is very much in the public sector now. Very few individuals in the private sector have them. And it's linked to your salary membership of the pension scheme. And it's also got a factor there. And what this does is it actually offers a sort of a guaranteed level of income at retirement based upon all those different areas.

If we then look at defined contribution schemes, these are very much a scheme where you contribute to them as you imagine from the name. So this could be your personal contribution or your employer pension contributions that have been made. But what happens is that on these plans, they are invested in what's called a fund and you will start to build up a fund entitlement for retirement. Then you've got different options. So you might be looking at a withdrawal. Or an annuity in retirement, but that's, that's what you'd be looking at as different options. And it's a less guaranteed option really.

Tom: For the purposes of today's podcast. We're going to focus on defined contribution pensions. Kevin, what are the tax benefits of having one?

Kevin: Yeah, this is a really good question. I think people really need to take on board about the tax relief that people can get on pension schemes. I'll come on to a little bit about that in a moment. So, if you think about the moment bank and building society accounts, getting half a percent return on a pension, the government are basically going to give you your marginal rate. Bit of jargon they have, but what it basically means is for most customers, so at 20 or 40% uplift in the pension contribution that you're making, if you can imagine a half percent rate of the bank or building society account typically at the moment, 20 to 40% on a pension contribution. There's suddenly a massive uplift in what you're able to get on your money. So really, it's worth having a conversation using these allowances each year where appropriate. 20%, 40% every single year and your contribution over time, that makes a significant difference to your overall ability to, to draw down a pension for retirement.

Tom: Most of us are paying into a pension usually through work but is it fair to say that a lot of us might not be earning enough? For example, I was reading a piece recently from the Pensions Policy Institute that said over 90% of people between the age of 50 and 66 will not receive a comfortable retirement income. What are the reasons for this, Gareth?

Gareth: Yeah so, it's a great question, Tom. So a lot of it is down to people not prioritizing their retirement early enough. This is because you've got things like they're at the early stage of their career. So they're saving up for houses, marriage, early family life. Unfortunately, that often moves into divorce as we're starting to see more frequently. When people actually start to realise that retirement planning is becoming important, it's not too late, but it becomes more of a challenge to start to save for that period of time. And people have been paying either the minimum amount up to that time and they start to realize really that they need to start to contribute more to actually attain what they're trying to achieve. Really the main reason is it's just not prioritized early enough. Well, the really key thing is it's not, it's not too late to actually start to look at it. So you might not achieve what you really wanted to achieve but starting to focus on that retirement planning now can make a big difference to later life.

Tom: How do you know how much you'd be paying in then Kevin?

Kevin: Yeah, million dollar question. There really isn't a sort of right and wrong, every person is different and as Gareth said, we all go through different stages of life and your ability to fund a pension will change. There was an interesting report by 'Which' magazine that went into how much people need. So for example, somebody who's single in retirement, somewhere between £19-31,000 pounds. 19 gives you your base style of living 31, perhaps allows you to do a few more things that you'd like to. For a married couple 19-41, but these are figures that don't mean a great deal to most people. It's really good to give you an idea, but the best way is just to sit down with somebody and discuss what retirement looks like, you know, what do they want to do in retirement? And then you work back from there because if somebody says I want £50,000 in retirement. Okay. That's great, well, let's work. What do you need to put in to try and achieve that? Is it realistic? Do you need to cut back on this? Do you need to add into that? And again, that brings you back to that tax relief, we just touched on tax relief for quite a time and the benefit that's going to add up.

So really it's getting under the bonnet and understanding what it is they're looking for and what they're prepared to do to meet that objective.

Tom: Gareth, just what sort of difference could paying more into your pension make then?

Gareth: So if we just look at some figures here then, so if we start to look at how much an individual tried to target aged 65 and then from the different ages. So someone trying to target £100,000 from age 30, then they'd be able to contribute £89 per month and achieve that target.

Tom: Okay.

Gareth: And that's assuming 5% growth as an average per year on their investment. If they start at age 40 that need to do £168 and if it was from age 50, well then it suddenly starts to jump up. It's actually doubled from the age of 40 to £375 per month for me to contribute towards it. If we then look at targeting £250,000, again, the numbers from age 30, £221 per month. If we look at age 50, it actually increases significantly again to £936 per month you start to need to look to contribute.

Tom: Right. Wow. So this, I guess, really shows the difference that even a small increase in pension savings can make to your future. Kevin, is it just about how much you're paying into pension?

Kevin: Certainly not. It's where you put your money and, and that's the real benefit that we can bring to our customers' conversations and our customers' long-term financial planning. So sitting down with the customer, discussing what it is they want from their money, what they prepared to do and actually quite often what they're not prepared to do. Some people aren't prepared to be really adventurous with their money, they just want a cautious approach, but they want to know that at the end of the day, they're going to end up where they need to be. Like Gareth was just saying, starting earlier has a massive impact on where you ultimately can be because a pension is just an investment. And as long as you're happy and comfortable with where that's being invested, then great.

But it's just having that conversation and making sure people are comfortable where it's going and comfortable with putting that in a pension scheme.

Tom: How do you know Gareth if you've invested in a way that's suitable for you?

Gareth: Yeah. That's probably the problem that many individuals have to be honest. If you've never looked at your investments before, you've never received financial advice, you're probably in the provider's default pension. And that's designed for the masses. So it's not tailored to you. No one's looked at your assessment for risk, but when I'm talking about risk, as Kevin mentioned before, it's, it's looking at how much you're willing to accept versus to achieve long-term benefits versus the losses you might have. There's loads of different pension options from different providers as well. So there's so much to consider and it's really difficult to look at it from that perspective.

Tom: This is a great point to bring in our special guest, Daniel Reynolds from Aberdeen Standard Investments who joins us now. Daniel manages an investment fund, which is the type of place where your pension contributions could be invested. Hello Daniel, can you explain a little bit more about what you do?

Daniel Reynolds: Hi Tom. Yeah, I'm a fund manager on a number of investment solutions, all of which use a broad mix of funds across a number of different types of investment from stocks and shares to bonds and property, their long-term portfolio. So on a day-to-day basis, my job is to make sure we're holding the right investment funds and that they're held with the right mix. I'm also responsible for fund research and selection across a number of the sectors we invest in, including European and Japanese equities, physical property, global real estate, Sterling credits and all passive funds.

Tom: How do you go about deciding what to invest in then?

Daniel: Well, our process has a number of stages, but the main focus of the funds is to deliver returns over the long term without taking heroic bets or using long only asset classes. It starts with a strategic asset allocation where we are combining a mix of different types of investments to give diversified returns based on the future expectations of risk and reward. This gives a framework with an expected volatility. I.e. how much the returns vary over time so it's easy for the investor to understand the risk they're taking by investing in the portfolio. The appropriate fund will then be selected to best represent each of those asset classes. And for passive funds, this will generally be one which closely replicates the market index, which was used when building that original strategic asset allocation.

Importantly, when we're selecting a passive fund, we have a consistent process which must consider a number of important factors such as cost and how well the fund performs in relation to its index.

Tom: Investing comes with risk. What measures do you take to manage the level of risk?

Daniel: The first stage of building our funds is, as I mentioned previously, the strategic asset allocation, which is entirely focused on the expected risk of a portfolio. Our funds are founded on risk levels of one to five. So when you invest your savings in a portfolio, it just goes up and down only as much as you're comfortable, this is based on a percentage of global stock market volatility. You might like a lot, given you’re investing for a pension, which is a long time away and you can afford to see it go up and down, or you might be happier knowing that what you're saving doesn't move much and can grow more slowly, but smoothly. We rebalance these funds very regularly to ensure the stress across the different types of investors is consistent over time. So that volatility is what's expected of you when you save.

Tom: What would you say, Daniel, to people who might think investing in this way might not be for them?

Daniel: It depends why they feel that way. I think we're all painfully aware of how important it is to save for pension given how much longer we're likely to live. And with retirement, probably being some way off, it's sensible to take some level of investment risk because you need something to you’re your savings grow. The important aspects of what Skipton offers is the different levels of risk you can take. So it's likely there's a solution which would suit most investors. If it's investment risk that puts you off, choose a more conservative risk level. But I think you can be reassured that someone's taking care of this risk for you. With Skipton there to guide you, you can make sure it's the right fund for you.

Tom: What would you say about the role that financial advisers like Skipton play in helping people to invest for retirement?

Daniel: I’m going to give a biased answer here, I was a financial advisor for nearly 20 years before I focused only on investments. I feel financial advice is essential. The financial markets are vast, rapidly evolving and we all live very busy lives. So actually taking the time to discuss our goals and aspirations with an expert means we can find the investment and follow-up solution most suitable for our circumstances. Having someone to guide you towards choosing the right level of risk ensures you have an investment journey you're comfortable with, whether you're someone who has a cautious approach or you prefer higher potential returns without losing too much sleep over short-term changes in value.

Retirement may seem a long way off, but it's really important to start as soon as possible because your pension will hopefully have to last a long time when you retire. An advisor is an expert at getting the balance right between what you want to achieve and what you can comfortably do about it.

Tom: How do you find working with Skipton, Daniel?

Daniel: Challenging at times, but in a good way, the Skipton team are extremely thorough in their due diligence. When we're discussing the funds with them, they’re very careful to ensure in detail that what we're doing meets their expectations and the needs of their customers. It's nice to be working with a team of friendly people who are focused on putting the customer first and share the same long-term approach.

Tom: Thanks for your time, Daniel, that was Daniel Reynolds, a fund manager from Aberdeen Standard Investments. So Kevin, now that we've had an insight into how pension contributions are invested, what would you say to people who have not reviewed their pension plans before?

Kevin: This is a really important part of financial planning and it's good to be able to put money away on a regular basis, but you've got to keep an eye on it. I would literally say every single day, I'm sitting down with customers that have not reviewed their plans. They've set up a plan years ago and it's just sat there and continued paying their money into it and they've got their pension contributions as and when, but they don't know where the money's going. It's quite often. It's interesting to ask somebody, you know, why did you choose that particular pension fund? And they don't know, it was something they ticked a box when they went to their employer. And they've been paying into it ever since. It quite often transpires that these funds may not be appropriate for them. You know, everybody's different, but if you don't know where your money's going into, you can't be 100% sure that you know what you're going to get back and where your retirement and what your retirement looks like. So the most important thing I believe is to be able to sit there, review these pension plans, to see how they're doing and provide advice accordingly. You know, risk changes, cost changes, there's so many factors that go into it and a really good qualified financial advisor will be able to go through this with you and support you through that process.

Tom: Is it just about the pension you're currently paying into, Gareth?

Gareth: No, definitely not. I think it's even more important to look at those older schemes more than anything. You think about all the different jobs individuals go through now, different companies that they’re with...those schemes can play a massive part, because it might be, you may only see it as being £10,000, but actually if you start to put them all together, then it's definitely worth reviewing and can really make big changes to someone's retirement. It could be that you could retire an extra year by having that £10, 20,000 pot. So definitely worth reviewing. But, with those older schemes and those older plans, then they might have benefits or penalties attached to them. So it, again, it's really important to think about actually reviewing those before you start to move them anywhere and consider putting them all together just to simplify it. They are really important and can offer serious value to your retirement.

Tom: Kevin, some people listening might be concerned that they're not going to have enough money saved for retirement. What would you say to them?

Kevin: Seek help. Speak to somebody. Gareth said just now about being able to retire early, I take real great pride in trying to find a way for people to retire early if they want to, you know, we're, we're very successful at that. In the past people have decided they wanted to retire at 65, 66 67. And that's what they had, but it's surprisingly how much money sometimes people have in pension funds that actually allows them to retire a few years early, do everything they want to do a few years early, which has got to be a good thing, we don't want to work for all our lives. So sitting down with somebody and looking at what they've got and if they need to make alterations, take out additional pensions or investments or whatever they need to do, that's just part of a real sort of holistic conversation that we had with people.

Tom: Are there limits to how much you can pay into a pension then Gareth?

Gareth: Yeah. Yeah. So this is an interesting point because they, the government, want you to continue to save for retirement. But actually in some instances it can be a bit of a minefield, to be honest. When you look at it, this is where advice can really help. So the basics are you can contribute 3,600 gross after tax relief or up to your salary, the higher off. But there’s also the annual allowance to consider, which for most people is £40,000 per annum, but in individual circumstances, this can be lower. There's the lifetime allowance, which is just above a million pounds, which again, might seem a massive value for the majority of individuals, but this is pensions where a lot of people's wealth and how they will fund their retirement.

So it's surprising how many people can get close to that mark and this is something that we see very often with individuals where they're quite surprised at how much they've gotten the pensions and how close it can be. There's also the fact that, you know, you can't access it until later on in life, because it is a retirement saving product. So currently you can access it from age 55, going up to 57 in a few years' time. So these are all things that you need to consider a way of financial advice can be. You make the decisions and decide whether or not a pension is the best place to go.

Tom: There’s also, Gareth, been a couple of reports of late that the government might look to change one or two of the pension rules that will make them less favourable for people saving for pensions. What can you tell us about that?

Gareth: Yeah, so we've seen lots of speculation. So over the last few years with, mentions about scrapping tax-free cash, making a flat rate, state pension, we've seen the, um, seeing the lifetime allowance recently reduced over a number of years and actually frozen this year when it was expected to go up again.

So that was something that they did this year that restricted pensions a little bit further than normal. It's all speculation though. As I said, we see it very frequently. COVID is something that we know had a big impact not only on our lives but the government's tax revenue. So we know there's some pressing concerns there. If we are likely to see something it is in the next few years, it could be imminent,it could be this year. It could be in a couple of years' time. We don't know, that's the problem. We see lots of things released from the press, from the government, in relation to this sort of thing but we don't always see it come to fruition.

Tom: Kevin as Gareth says there it is speculation at this stage, but what would you suggest to people who are aware of such reports?

Kevin: Yeah, I think Gareth's got a valid point. We don't always see them come to fruition but what I would say is it speaks to somebody. Take advice, go and see a financial advisor, whether that's us, whether that's somebody else, but go in to speak to somebody, get that advice. There are various things you can do within the current tax year. I won't go into details of that at this point; it's probably too technical for today. But I want to say take advice, speak to somebody qualified and then see how they can support you with your pension plan going forwards.

Tom: It might sound, Kevin, like a lot of work planning for retirement.

Kevin: I think a lot of people get scared by it and they get these annual statements that come through and sometimes, just today I discussed with a customer who I think really didn't understand their statements. So it was really quite scary, but we've all got different skills in life. But planning for retirement it's not difficult, but you have to speak to somebody who knows what they're talking about.

I take my car to the garage. They're the experts. I let them sort my car out. People come to us for financial advice, we're the experts. We can really help them out. It's a bit technical, yes, but that's why we have the support of Gareth and his team. And then we put that into a plain English conversation with people so they know exactly what they're doing, how they're doing it. But all I would say is if you're not sure, take advice. Find somebody. But most importantly, just find somebody that you trust. Hopefully, I think of that as ourselves. Talk to them and see what they can do to support you.

Tom: That's really helpful and that's just about all we have time for this edition. My thanks go to Gareth, Kevin and Daniel and thank you for listening. We really hope this has helped you to think about how planning your retirement with Skipton could ultimately free up your time to get on with the things that matter to you the most. If you have any feedback or questions, we'd love to hear from you. Simply subscribe to our Life and Money email updates at 'skipton.co.uk/insights' or call 03452667724. Bye for now.