NEWSLETTER

"A further reason to prioritise a defined benefit pension review"

A well-known pension transfer index has recently published data relating to defined benefit transfer activity and the average transfer value both reducing over the course of 2022, seemingly in step with a general increase in discount rates causing a corresponding reduction in transfer values.

This index reports a transfer value high on 7 December 2021, which has reduced by approximately 22% to the end of July 2022, together with an activity index which is down 18% over the same period.

Because the vast majority of pension transfers are to flexible drawdown plans, with the assets generally invested in equities, any assumed level of transfer value reduction would, of course, need to be considered in line with any corresponding investment opportunity. Since the 22% reduction in average transfer values, noted above, the NASDAQ has fallen by an equal amount and the S&P500 by 15%, over the same period.

Any claim that transfer activity has reduced, because capital values of defined benefits have, would overlook the likelihood that these are only going to reduce further as well as the more important aspect, being the real value of the underlying income stream.

The majority of defined benefit schemes provide inflation offset protection on the amount of deferred pension promised to a member. Statutory inflation offset levels will be linked to either RPI (for benefits earned before April 2011) or CPI (for benefits accrued since) and these will commonly be capped at either 5% (for benefits earned prior to April 2009) and 2.5% (for benefits earned since).

ONS data confirms that the annual increase in RPI, in July 2022, was 12.3%, with the annual CPI increase, in the same month, being 10.1%. Whether the Statutory inflation protection for deferred pensions is as high as RPI capped at 5%, or as low as CPI capped at 2.5%, the actual year-on-year increases, to date, will have already significantly reduced the spending power of defined benefit scheme deferred pensions.

Whether the Bank of England's expectation that inflation will reach 13% before the year end, or predictions from some investment banks of January 2023 inflation levels hitting 22% become true, or not, the economic outlook shows no signs of inflation levels reducing.

With TPR 2021 data confirming a total of 4.93 million deferred members of DB schemes, there remains a significant opportunity to provide specialist independent advice to those who are most likely to be affected by the outlook for inflation, placing even more importance on the value of a review of such benefits to identify whether they continue to align with client objectives and future aspirations.

We welcome the opportunity of providing this service, at a recorded face-to-face abridged advice meeting, for any client of our professional introducer network.