Adapt and Survive

Why technology matters
in the 'new' retirement savings market

November 2014

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Opportunity

The UK retirement savings market is enormous. The value of margin generating pension assets administered in the collective backrooms of UK product providers totalled over £2,400 billion at the end of 2012[1]. And considerable growth is expected over the next decade.

The value of assets invested in defined contribution workplace pension schemes[2] is estimated at around £275 billion, and on the back of Auto Enrolment is expected to at least **double** by 2022[3].

When it comes to funds tied up in annuities, drawdown, ISA savings for retirement and other private assets being used to finance retirement combined, analysts Spence Johnston predict a rise from £145 billion to £289 billion by 2023[4]. Again, a doubling in overall size in 10 years. And within that, they predict annual growth of almost 10% for the drawdown market alone.

Challenge

The challenge for financial services product providers is how to capitalise most effectively on the sheer size of the retirement savings market with particular focus on those areas – the post-2014 Budget at retirement market and associated 'guidance guarantee' requirement springs to mind immediately – in which it is expected to change and grow.

How to capitalise against a background of regulatory, social policy and consumer behavioural change, all of which are crashing together with advances in technology to disturb established business models and perhaps threaten the very commercial survival of some traditional providers.

Technology – the crucial deciding factor

In this paper we assert that the technology underpin a business chooses to adopt will be the crucial deciding factor for commercial success or failure in the 'new' retirement savings market.

That's a very simple statement with a whole story behind it. As with all good stories, make yourself comfortable and let's start at the beginning.

Once upon a time

Once upon a time the mainframe ruled the world. Rigidly constructed to support the administration of particular products designed by particular providers, they were inflexible monoliths that did not talk to one another without considerable persuasion and development.

As the years went by, smaller, nimbler systems began to compete as collectives with the mighty mainframe. The need for these systems to talk to each other was slowly accepted. But development remained mostly about the administration of particular products designed by particular providers and especially that most complicated beast of all – the pension product.

Then along came the internet and aggregation technology, and the world began to turn on its head. Aggregation technology made it easier to manage a lot of information and actions potentially relevant to a particular customer in one place. And with that simple idea, a revolution began.

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[1] Source: ABI Data Bulletin, November 2013
[2] That's both occupational and contract based defined contribution schemes.
[3] Source: Defined contribution workplace pension market study, Office of Fair Trading, September 2013 (Revised February 2014), OFT1505
[4] Source: Spence Johnson, Deeper Perspectives, Number 18, December 2013

The world turned on its head

Instead of rigidly specified, effectively closed and inflexible systems (at least without some serious struggle and resource being involved) gaining competitive advantage has become about building highly configurable, relational databases capable of managing and processing massive amounts of information in flexible ways.

Witness the rise and rise of the platform market in UK financial services.

Offering greater efficiency, transparency, choice and control to consumers and their advisers alike, along with the Retail Distribution Review (more on that later) platforms have driven a coach and horses through a market based on selling products, helping transform it to one based on providing a holistic and ongoing service to individual investors.

At their best, platforms are designed to be flexible, to integrate with and relate to other systems as required and through that to support a holistic approach to managing an investor's affairs.

Reaching the tipping point

Platforms have risen to dominate the writing of new investment business, with research by the Platforum, for example, suggesting that 97% of advised ISA sales and 77% of advised SIPP sales are now flowing in through the platform route[5].

But that's new business. And that's platforms.

What of the £2,405 billion back book of legacy pension business? Is it too specialist and technically difficult to benefit from a similar technological overhaul?

Our answer is an unequivocal no. Quite the opposite in fact. We think a tipping point is now being reached where the demands of the 'new' retirement savings market will compel providers who wish to adapt and survive in the longer term to begin moving their considerable back books of business from legacy systems on to far more flexible and relatable technology underpins.

Let's take some time now to look at the context which led us to that position.

Regulatory change

Regulatory change has dominated development agendas in recent years. The regulator's own figures put the one off costs of implementing the Retail Distribution Review at up to £1.48 billion[6]. Of course, these costs run far broader than just technology change, but they still give a sense of order of magnitude. RDR sucked up vast amounts of development resource across our industry.

RDR was designed to:

- deliver more clarity for consumers on products and services
- allow more consumers to have their needs and wants addressed
- allow competitive forces to work in favour of consumers by moving from a system based on provider led commission payments to consumer led adviser charging
- build confidence and trust through improved professionalism
- make sure firms can deliver on their long term commitments and treat customers fairly

These are all positive things from the consumer perspective. But they have added up to significant downward margin pressure for both providers and advisers.

At the moment this pressure is at its greatest for new business where consumers must now agree and pay an explicit charge for any advice they receive. Due to their scalable, repeatable and flexible nature, we've already noted that platforms are dominating inflows for new business post-RDR.

[5] Platforum weekly email, 23rd May 2014
[6] Source: Money Marketing, "FSA stats: RDR costs could reach £2.6bn in 5 years" by Natalie Holt, 13 March 2014

But it is clear that this margin pressure will inevitably extend to 'legacy' pension business.

On 27 March 2014, as part of a package of measures that we'll examine further below, the DWP announced it would ban adviser commissions from 'qualifying schemes' for pension auto enrolment from April 2016. A blow for those who had hoped to avoid rewriting legacy workplace schemes more in the form of their lower-cost cousins (like NEST, NOW:Pensions and the People's Pension), created specifically for the post-auto-enrolment world.

The very next day the FCA announced that it would be launching a supervisory review to look at whether customers in long standing 'traditional' life and pension policies were still being treated fairly. This potentially covers up to 30 million policies, the vast majority of which will still be administered through legacy systems and which were written in higher margin days.

Although the FCA were at pains to reinforce that this review would not necessarily lead to any positive action on their part, the very fact of its launch was received by many in the industry as a warning shot across collective bows.

In short, margin pressure as a result of regulatory action is here to stay and increasingly likely to impact on the legacy pension business that providers may – at least to some extent – be relying on to subsidise less profitable new business.

The means to administer this business in a far more cost effective and flexible way than can be achieved by tinkering on the fringes of established systems will need to be found.

Strike one for legacy systems.

Social policy change

Next up are the various social policy changes being pursued by government to increase average levels of retirement saving in the UK. The confirmed biggies here are:

- the phased introduction of auto-enrolment for workplace savings (started in October 2012)
- a charge cap of 0.75% on the default funds of all auto-enrolment qualifying schemes
- the banning of sales commission being taken from individual scheme member pots
- the banning of consultancy charges, through which individual scheme members effectively pay for advice received by their employer
- the banning of so called 'active member discounts' which see charges for pension scheme members being raised when they leave the employment to which the scheme is attached
- from April 2015, the freedom for people to withdraw their savings from DC pensions from age 55 however they wish, subject to income tax and the accompanying requirement for all retirees to receive face to face advice/guidance before they decide how to use their money (the 'guidance guarantee')
- the introduction of NISAs, allowing annual savings of £15,000 into any combination of a Cash NISA and Stocks and Shares NISA, and freedom to transfer accumulated savings between the two types of NISA in future years

Together, these changes will amount to further significant margin pressure for providers.

When it comes to the charge cap alone for example, Aegon has indicated that it expects the cap to cost it between £20million and £25million a year[7] and Royal London that it will result in the loss of £61 million from its future profits over the next 10 years[8]. The ban on sales commission and consultancy charging also pose challenges for advisers on their sources of income around workplace schemes. Research for The Pensions Regulator in Spring 2013 found that less than half of small to medium sized employers were prepared to pay directly for advice and support on meeting their auto-enrolment obligations[9].

Add to these pressures:

- the need for administration systems that can accommodate increased flexibility around what consumers do with their pension and NISA savings; and
- the outcome of the practical debate about how to manage the increasing problem for consumers of multiple small sized workplace pension pots that may accumulate over the course of their working life.

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[7] Source: The Herald, "Aegon 'to lose £25m a year to pension cap'", 16 May 2014, Article by Simon Bain
[8] Source: Money Marketing, "Royal London hits out at gov't over £1bn pension charge cap impact", 19 August 2014, Article by Rosie Sells
[9] Source: Employers' awareness, understanding and activity relating to workplace pension reforms, Spring 2013. Report for The Pensions Regulator presented by GfK NOP Financial
[10] ONS Statistical bulletin: Internet Access – Households and Individuals, 2013 (published on 8 August 2013)

Whether we end up with “small pot follows member” or “one pot per member” with multiple employers contributing at different times, or something in between, the one thing that is certain is that there will be a need for systems that are not only flexible in and of themselves, but that are also capable either of aggregating or accumulating data from multiple sources, and deploying practical tools to help individuals – many of whom may not be prepared to pay charges at a level that would make them commercially attractive for a traditional advisory service – understand and manage their combined retirement savings funds in a practical, engaging and accessible way.

Strike two for legacy systems.

Consumers and technology

And then we come to consumers themselves and how they access and use technology today. We now live in a world where consumers:

- **are empowered** by greater access both to information and services and to online peer communities that can actively influence their decision making (over half of all UK adults now participate in social networking[10])
- **have high standards** for the type of seamless and user-friendly service they expect to receive from suppliers when they go online (think of all the things you can now do on a typical airline website for example: from booking your flight through to checking in online, booking ancillary services for your trip if you need to like car parking, hire car, hotel accommodation and being able to access additional advice and support through a live chat link to a customer service adviser).
- **are increasingly used to self-serving** – 50% of all UK adults now bank online for example, rising to 74% in the 24-34 age group[11]. It is now the norm to be in ‘click of a mouse’ control and to get an instant response to requests for information and service. So waiting overnight for a batch process to run or a week for a password reset letter to arrive in the post is likely to result in frustration at best and turn off a customer to your whole proposition at worst
- **expect online service access 24/7 from pretty much anywhere** – at home, at work and when they are mobile. 73% of adults in the UK now access the internet every day and 61% access the internet ‘on the go’, mainly through smart phones and/or tablet computers[12]

In short, we are moving towards an increasingly inter-connected future in which systems – both internally to, and between, different companies – need to be able to talk to each other, to move data between themselves quickly and securely and then to present it in an engaging and user friendly format for the decision-making, mobile consumer.

And in light of the considerable margin pressures we’ve already looked at, those same systems need to be able to adapt and flex in a cost effective way to changing market needs whether driven by regulatory change, social policy change or the changing preferences of consumers themselves.

Strike three for legacy systems. And out.

Let’s move on now to sum all of this up.

The ‘new’ retirement savings market

We believe the ‘new’ retirement savings market will be service led rather than product led, with advisers and providers competing to manage the holistic retirement needs of each individual consumer. It’s no longer all about ‘the pension’. It’s our view that consumers will inevitably come to demand a simple, single view of their entire savings and income profile at any point in time.

What is more, increased workplace savings through auto-enrolment, combined with the requirement for everyone to be offered some kind of guidance on their retirement options from April 2015, means that the retirement savings market this will become far more of a mass market than is currently the case.

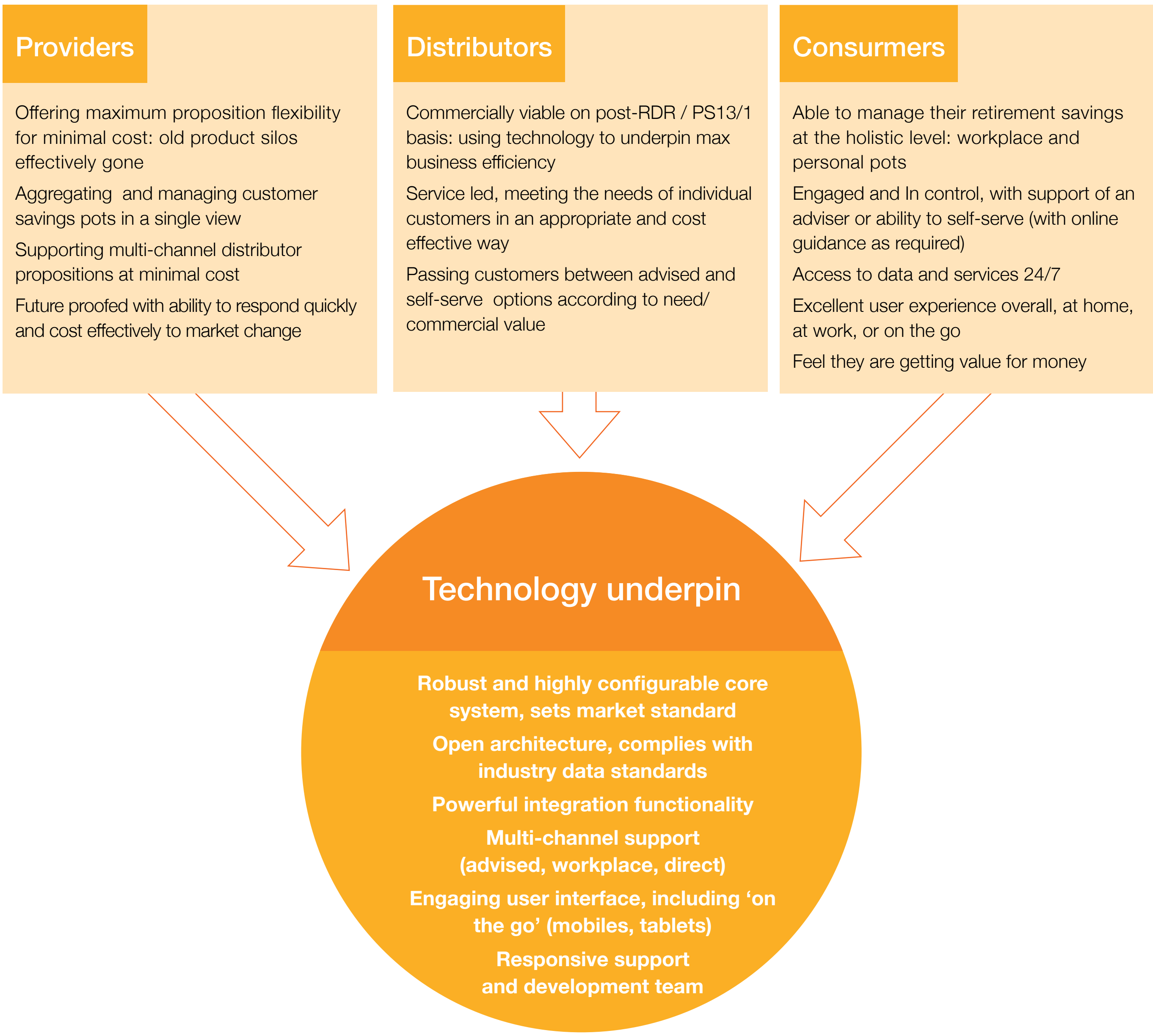
But it will also still be a very complex market. We predict there will be lots of new products (or at the very least changes to

[10, 11,12] ONS Statistical bulletin: Internet Access – Households and Individuals, 2013 (published on 8 August 2013) existing products), with lots of new flexible options for drawing down income. We may reasonably expect to see a phased approach to retirement becoming the norm, with an initial focus on gradually reducing earning whilst beginning to draw some income from savings, then perhaps a move to guaranteed income at a later stage with the characteristics of associated death benefits changing to match.

The winners will be those that can offer:

- repeatable, scalable and responsive services
- services that are tailored appropriately according to the needs of individuals
- services that bring together both workplace and private savings onto a single platform, allowing for the increasing complexity of new product options
- all at competitive prices that are realistically sustainable for their business
- and all underpinned by an excellent user experience both online and face to face.

Fig.1 – The 'new' retirement savings market



Four reasons your technology underpin really matters

We've now looked at why we think the 'new' retirement savings market is driving UK financial services to a tipping point at which we will see a wholesale shift of provider back books to new more open and flexible technology underpins. And in the diagram above we've summarised some specifics around the characteristics of those technology underpins that will support the market in adapting, surviving and then thriving in the face of regulatory, social policy and consumer behavioural change.

Moving to new technology is no small undertaking. It takes capital investment, it takes time and it takes resource. It exposes a business to risk and – if benefits are to be fully realised – it in general also involves committing to a particular strategic direction for a number of years.

For businesses not already committed to the end game of a more flexible, connected technology underpin for pension back books, here are four reasons we think you should change your mind:

1. Operational efficiency

In-house legacy systems tend to undermine operational efficiency. It's not just the cost of updating and maintaining them at the core level. It's the almost inevitable ongoing cost to your business of the associated workarounds, manual processes and clunky add on modules that have evolved over time as the core operating parameters for which they were originally built buckled under the strain of keeping step with market developments.

At a time when margins across the industry are under massive pressure, can you afford to keep carrying this burden? What if the (quite likely highly experienced and expensive) resources that you deploy in the care, maintenance and update of these systems each time another parameter changes, could be refocused on future proposition development?

It's not necessarily about abandoning legacy systems altogether. Rather, it may be a question of understanding the pressure points at which the cost of maintaining them outweighs the benefit, and then scaling back their use to core areas of operational need with smart integration to a more flexible, inter-connected and highly configurable front end.

2. Responsiveness

As George Osborne made his UK Budget announcements in March 2014 on the removal of restrictions around the use of pension savings and the introduction of the more flexible NISA regime, armies of operations and project managers around the industry may have been tempted to reach for the development schedules and block them out again – for at least the next 12-18 months.

Making changes to legacy systems that were built to deliver a specific set of business requirements can be a complex, lengthy and messy process, and one that can't always be sped up by throwing money at the problem. Anything you have to do will likely require the involvement of a relatively small group of in-demand technical experts in your business, whose time and level of commitment has to be negotiated on a business-wide basis.

And that's a problem because all the best thought out plans of your marketing department will count for nothing if they can't be delivered quickly enough to gain competitive advantage. It isn't about being ready with the legislation changes on time that is the key. It is having the flexibility to react quickly afterwards, when the market impact is really known, that will mark the difference between the winners and the losers in the 'new' retirement savings market.

What if you were working with a system that had been built for flexibility and was highly re-configurable without any need for significant underlying development? What if you were not wholly reliant on your in-house IT team having the resource and scheduling capacity to respond to market developments in good time? What if a powerful integration layer meant that you could quickly get ahead of the game – making changes in your customer facing systems without having to significantly disrupt your back-end administration and servicing systems?

3. Multi-channel support

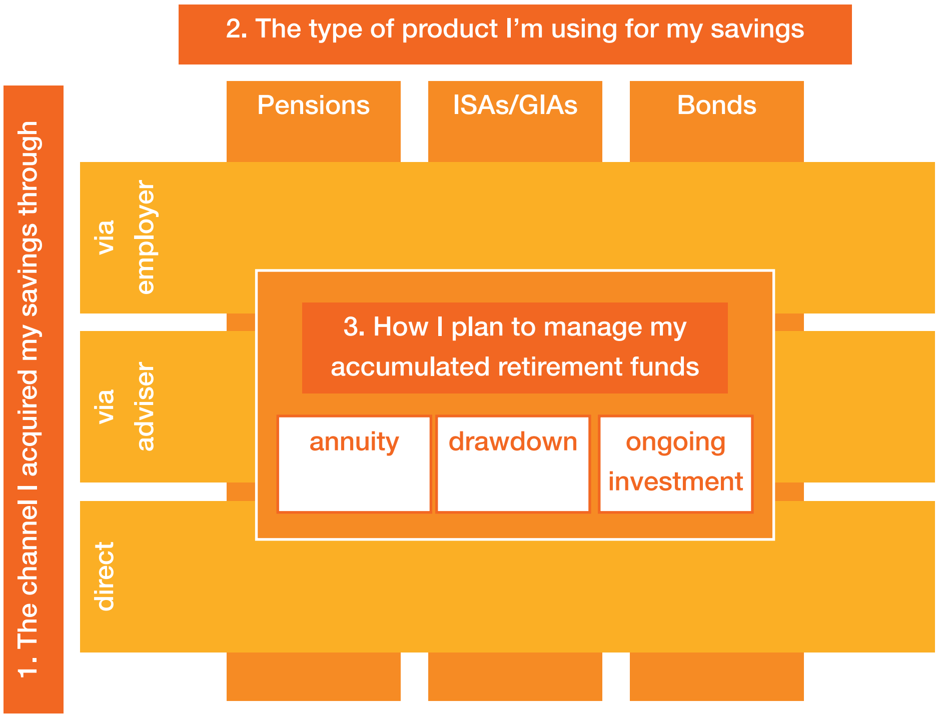
We've seen that the 'new' retirement savings market will revolve around:

- bringing together all of an investors' relevant savings
- supporting their retirement plans from there according to their needs
- and doing it in a cost effective and commercially viable way.

Building separate infrastructure for customer facing, employer facing and adviser facing propositions has tended to be another siloed activity for many providers. It often involves different teams of people within the business, who have different priorities and design different product features. The result can be clunky interconnection at best. Or no interconnection at worst.

It's worth noting at this point that a third level of systems silo also effectively exists inside many provider businesses, dictated by how a customer chooses to use their accumulated savings to fund their retirement. It seems inevitable that these silos will also need to be broken down to allow customers the genuine flexibility with their DC pension savings that George Osborne intended with his Budget 2014 bombshell.

Fig.2 – Three levels of systems silo



This lack of connectedness between systems silos that have evolved over time is a major challenge when we are looking to a future in which our customers will continue to acquire their savings through different channels, but are likely to demand solutions at an extremely flexible holistic level when it comes to using those savings to fund their retirement.

Providers and advisers will both be faced with the challenge of how to service individual customers in a way that meets wants and needs but still generates margin. At some stages a customer may need advice, either face to face or online through technologies such as live chat and video links. At other stages it may be more appropriate for them to self-serve. And they may be accessing these services either through a workplace or private arrangement.

A lesson from Australia?

Experience in the Australian market reinforces the importance of being able to deliver the right sort of advice and guidance at the right stage in each consumer's retirement journey.

A long standing policy of compulsory superannuation contributions means that on average Australian consumers have a decent amount put by at retirement. But consumer behaviour means that doesn't necessarily translate into comfortable retirement. In fact, according to a recent Australian government commissioned enquiry:

- "a quarter of people with a superannuation balance at age 55 have depleted their balance by age 70" when they may have many years left to live
- "half of superannuation benefits in retirement are paid as lump sums"; and
- the ability to use superannuation lump sums to extinguish debt can "encourage higher pre-retirement consumption and borrowing".

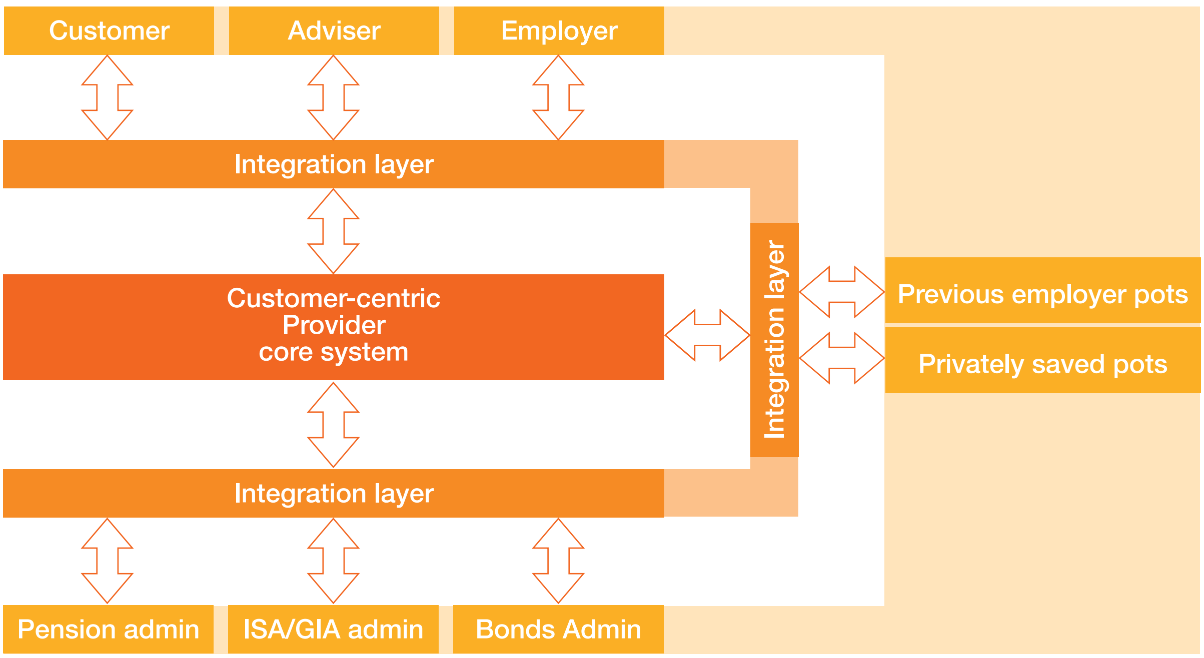
Concern is such that consultation including the idea of mandatory annuitisation is now ongoing.

Both providers and advisers will want and need to be able to pass customers flexibly from one channel to another. And their ability to do this may well in turn make their propositions more attractive to employers who are looking for the best workplace offerings for auto-enrolling their employees. In the longer term, we think this will become increasingly important, especially if we go down the pot follows member road. The starting point for most retirement savers in the future will likely be their workplace. And consumer loyalties will be won and retained not just on the strength of a provider brand but also on their experience of the technology that comes with it.

Making this work will mean starting with a core system that is built around the holistic needs of the individual customer, pulling together and managing details of their accumulated savings. With the ability then to play these details back out in different forms to the customer, their adviser and their employer. And from there to support face to face advice, online advice, online guidance and self-service for any one customer according to their need and potential profitability to the business.

It looks and feels like existing platform technologies, but – compared to most platforms operating in the market today – with the crucial addition of effective support for the particular technical challenges of managing complex legacy pension products along with an extra layer of connectedness between the direct (customer), adviser and employer (workplace) channels.

Fig.3 – Multi-channel support from a flexible core



4. Future proofing

The sum of the three parts we've just looked at then becomes future proofing. By re-aligning your business technology away from product and channel silos so that it revolves around a customer centric, highly configurable and flexible core with the ability to integrate to multiple-existing systems, dealing with major regulatory and social policy change naturally becomes less of a challenge, for the reasons we've just examined.

And if in practice you share your core infrastructure with other providers, and it is managed for you by a technology specialist, development costs can also be diluted, there are fewer resource constraints and you build in greater potential for disposals and acquisitions of back books further down the line. Your specialist provider also builds up cross-market expertise from which all its customers stand to benefit and is commercially incentivised to keep ahead of the game and to adapt its offer quickly in response to market developments.

Summary: adapt and survive

A tipping point is coming that will see providers begin to abandon, or at the very least scale back, their legacy systems. Back book business will move to new technology infrastructures. Infrastructures that are designed to support the holistic needs of the customer from a single, flexible central core. Infrastructures with powerful integration layers that enable straight through links to different user interfaces and different back office systems according to need. Infrastructures that are not channel specific, but work across multiple channels for a single customer: workplace, advised and direct. Infrastructures that offer tools to help with decisions around investment and how and when to take retirement income and that cater to the practical needs and expectations of the increasingly demanding and mobile consumer.

Providers that understand this and build their technology strategies around it will adapt and survive in the 'new' retirement savings market. Those that don't will face an uncertain future.

GBST

UK clients already benefiting from our wealth management technology solutions		
AEGON	AJBell	Alliance Trust Savings
Barnett Waddingham	Fidelity WORLDWIDE INVESTMENT	novia

About GBST and GBST Composer®

GBST's credentials as a technology provider for both the pensions and platform market are well established, rooted in the early development of 'wraps' in the Australian market and refined through many years of international experience since.

GBST Composer® represents the culmination of that experience. It is a robust, scalable solution catering for the complete end-to-end administration of business models. When combined with GBST's proven integration techniques and its powerful and flexible specialist components – including the ComposerLife platform for insurance and pension products and the ComposerWeb front office solution for customer and adviser servicing – GBST is the natural partner for any provider looking to capitalise on the 'new' retirement savings market.

GBST Composer® features

- Ability to integrate to external systems, with various integration techniques available
- Multiple product lines supported
- Proven and market leading Straight Through Processing capabilities
- Support for electronic messaging systems
- Integrated web logins for advisers, employers and customers
- Customer and household centric views supported
- Financial tools and calculators
- Scalable architecture and underlying technology
- White labelling

GBST fact file

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Operating in Australia, NZ, the UK, Asia and North America.

Over 450 employees.

Clients include some of the largest and most influential institutions in global financial services.

Innovate, grow and prosper with GBST

GBST's technology won't constrain your ambitions. It will inspire new products and services that create a sustainable competitive advantage for you and your clients.

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