Research report
November 2016

From disruption to empowerment

How are investors and their advisers dealing with a world of uncertainty; and what's needed from industry and policymakers to ensure that instead of being overwhelmed by a torrent of change, investors are supported and empowered?

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Foreword

2016 will be remembered as a year of unprecedented political change.

The UK's decision to leave the European Union and Donald Trump's victory in the US Presidential Election are symptomatic of a growing trend of anti-establishment sentiment in many Western societies. Many people feel worse off, and that their voice has not been heard for a long time. Their deep-rooted sense of dissatisfaction has been fuelled by a world of low, non-inclusive growth. Electoral tests due across Europe in 2017 could result in further votes against the established order. Political risk is traditionally seen as an emerging-market issue, but looks set to be a fixture of developed markets for the foreseeable future.

When I co-founded Aberdeen in 1983, it was also a turbulent and uncertain time. Much of the developed world was still recovering from a global recession and high levels of unemployment that persisted until the mid-eighties. That downturn contributed to the savings and loans crisis in the US and the debt crisis in Latin America. In the UK, unemployment had reached three million by January 1982, a level not seen for 50 years, and elsewhere in Europe it reached heights not witnessed since the Great Depression. In Asia, there was heightened activity of a different kind: a boom in Japan was followed by a surge in growth by the 'four tigers' (Hong Kong, Korea, Singapore and Taiwan) in the early 80s, quickly followed by Malaysia, Thailand and China.

Our vision in 1983 was to establish a robust, resilient business that would be capable of withstanding the impact of political and other extraneous events, and which would offer investors the investment returns that enabled them to achieve their financial goals. Three decades on, I believe Aberdeen continues to achieve those aims. We remain focused on the long term, investing in good companies, bonds and property around the world and holding them through cycles of uncertainty.

The past thirty years has seen us embrace new technology, foster a culture of innovation, and stay focused on the human capital and team-based approach that are so important to our success and that of our clients.

This research report underlines that, despite the unpredictability that macro-economic and political change can bring, a commitment to long termism is one of the most empowering forces for good in the investment landscape. Aberdeen will continue to stay true to its principles, and I hope that policymakers will do what they can to encourage the conditions to support our industry and better enable us to deliver the investment returns on which our clients, and the wider investment community, depend.

Martin Gilbert
Chief Executive
Aberdeen Asset Management

A commitment to long termism is one of the most empowering forces for good in the investment landscape

Introduction

Today's investors and their advisers face a torrent of change from all quarters. Political, economic and regulatory turbulence is matched only by the speed at which technology is transforming business models, choices and decision-making.

While growth remains persistently low, commodity prices and trade have fallen, external imbalances are increasing, and government finances are stressed, this is actually one of the most prosperous and peaceful periods in recorded history. The contradictory nature of our times compounds the already high level of uncertainty in evidence around the globe.

In a world in which we are also living longer and need to make money work harder, this research addresses the potentially disruptive forces at work across the investor landscape and examines how asset managers and policymakers must respond to ensure that instead of being overwhelmed by the pace of change, investors are supported and empowered.

Research method

The research, undertaken by Gabriel Research & Management Ltd, comprised in-depth interviews among institutional investors and consultants in the UK, Europe and the US, and three distinct online surveys among institutional investors and consultants, independent financial advisers (IFAs) and individual savers and investors.

There were 110 respondents to the institutional survey from the UK, Europe and the US, 205 online interviews with IFAs drawn from a UK-based omnibus panel, and 555 online interviews with a nationally representative sample of UK retail savers and investors, each of whom contribute to a workplace pension scheme and/or pay into a self-invested personal pension, or hold ISAs or other savings or investments intended for their retirement.

Fieldwork dates: IFAs and individual savers and investors - 27 September to 3 October 2016.
Institutional investors and consultants - 3 October to 31 October 2016.

For reasons of client confidentiality comments from interviewees are not attributed.
Some wished to remain anonymous and are not listed under 'Acknowledgements'.

Executive summary

The research comprised in-depth interviews among institutional investors and consultants in the UK, Europe and the US, and three distinct online surveys among institutional investors and consultants, independent financial advisers (IFAs) and individual savers and investors.

Political uncertainty was considered by 74% of institutional investors and consultants and 66% of IFAs as the most likely disruptive force in the investment landscape in 2017, followed by ultra-low interest rates and the threat of global recession (45% and 41% respectively). The majority of institutional respondents (74%) and IFAs (69%) reported that their jobs will be more challenging as a result.

While the majority of institutional investors and consultants were cognisant of the negative impact that uncertainty can have on the financial markets, and somewhat frustrated at the effects of quantitative easing and persistently low interest rates, they were typically pragmatic in preparing for potentially (even more) difficult times ahead. They cited funding liabilities and volatility management as their primary investment objectives for 2017, staying focused on their long-term goals.

Asked about their asset allocation plans for 2017, institutional investor respondents expected to increase allocations to private debt (88%), multi-asset/multi-strategy solutions (77%), private equity (64%), fixed income (52%) and hedge funds (48%), and other strategies that would help preserve capital and manage risk (among them, liability-driven investments and insurance-linked securities).

The cost of hedging against risk was perceived by a number of respondents to be expensive and the controversial subject of liability measurement being based upon gilt yields was a recurring theme.

Our qualitative research among institutional investors and consultants corroborated the quantitative findings and highlighted the trend towards an increasingly 'asset class agnostic' approach.

Insurers and mature defined benefit (DB) schemes were typically invested in property for its provision of secure, long-term income while less mature DB schemes were open to other illiquid opportunities or opportunistic funds.

Infrastructure investment was perceived to offer the potential for attractive risk-adjusted returns, reliable inflation-linked returns, stable long-term yields, capital growth and credit diversification benefits. However, pricing, lack of transparency, political risk and the implications of Solvency II were identified as causes for concern.

Institutional investors and IFAs were unanimous in citing the world's emerging markets (52% and 45% respectively), and Asia Pacific in particular (26% and 35%), as offering the best equity opportunities, followed by the US (23% and 33%).

To help their clients tackle longevity risk, 52% of respondents would like to see asset managers develop new risk management strategies and products, and a similar number (59%) reported that compulsory saving into workplace pension plans is most likely to help.

When asked to propose just one change that would empower the investors of tomorrow (be they institutional or individual), financial education was one of the top recommendations: 82% of institutional investors, consultants and IFAs agreed that the industry and policymakers should allocate more resources to financial education with respect to trustees; and 85% agreed that the same should be done for pension scheme members/individual investors.

Professional investor advice on empowering fellow institutional investors ranged from suggestions that echoed the findings of the Kay review[1] to shorten the investment chain, to "more acknowledgement of the unknown unknowns – to which diversification is the only solution"; and specifically, "increase interest rates".

[1] The Kay Review of UK Equity Markets and Long-Term Decision Making, July 2012

There was also a resounding call for more stability: "What we need is a stable, well-principled regulatory framework for pension scheme provision. Unfortunately we haven't had that."

While digital financial advice platforms are proliferating, IFAs were sceptical about their value but nonetheless acknowledge that they will play a greater role in the future and agree that digital platforms could significantly increase business efficiency, particularly in handling less wealthy clients.

The majority of IFAs (64%) were not changing their business to take account of 'do-it-yourself' investing, although a fifth (21%) were spending more time on financial planning. 82% of IFAs reported an increase in clients seeking investment and planning advice following the pension freedoms.

IFAs felt that education and guidance is more empowering to their clients than lower fees and charges or a wider range of investment products.

Almost four in ten (37%) IFAs spend a lot of time educating clients before offering advice and 71% believe that more time educating and advising clients would empower them towards a better financial future, as opposed to lower fees and charges (18%) and a wider range of products (3%).

For individual savers and investors, the perceived complexity of pensions, saving and investing and the shortage of effective solutions persist as barriers to engagement.

Individual savers and investors responding to the survey said a simpler, easier to understand range of options would best empower their investment decisions (30%), followed by more knowledge about the options available to them personally (28%).

67% said they would save more if they earned more; 40% would save more if the government gave better tax incentives, 25% if their employer matched or bettered their contributions, and 21% if they understood more about where to put their money.

49% would invest more if they could afford to, 40% would invest more if they could be guaranteed a return on their investment, and 29% if they understood more about where to invest.

In conclusion, political and economic uncertainty is adding to the challenges faced by institutional investors, consultants and IFAs, on top of an already highly demanding regulatory environment.

Prolonged, ultra-low interest rates are perceived as a dangerous comfort blanket and there is a significant appetite among professionals for a return to conditions that would allow more fundamental analysis and a 'real' economy.

Individual savers and investors have welcomed the pension freedoms but their underestimation of how much of their annual income might be needed to see them through their life in retirement points to the need for much more financial education.

While technology is transforming the investment sector, services need to be client rather than technology driven. Market participants need to focus on ways in which new technologies might benefit both consumers and markets but will not be able to do so without the right economic and regulatory conditions. This research, as with so many reports that precede it, calls for a period of stability from policymakers and regulators.

Research findings

Research findings

Political uncertainty: a significant disruptive force

Political uncertainty was considered by 74% of institutional investors and consultants and 66% of IFAs as the most likely disruptive force in the investment landscape in 2017, followed by ultra-low interest rates and the threat of global recession (45% and 41% respectively). The majority of institutional respondents (74%) and IFAs (69%) reported that their jobs will be more challenging as a result.

Figure 1A
The Brexit vote is just one factor that has contributed to uncertainty in the political and economic landscape, which can disrupt investment markets. What do you consider might be the most disruptive forces in the investment landscape in 2017?

Institutional investors & consultants

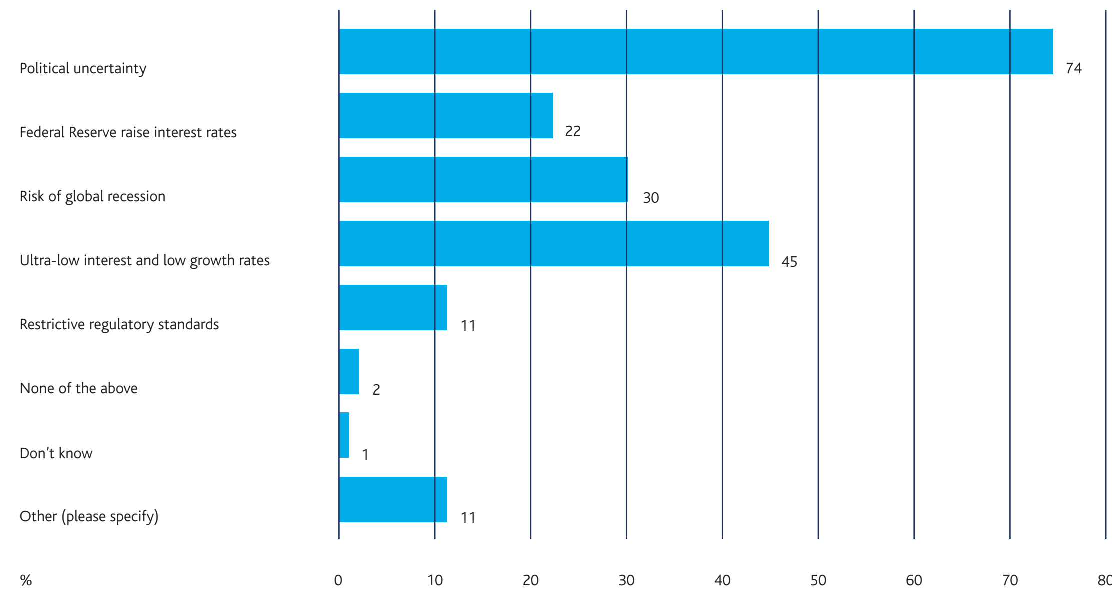
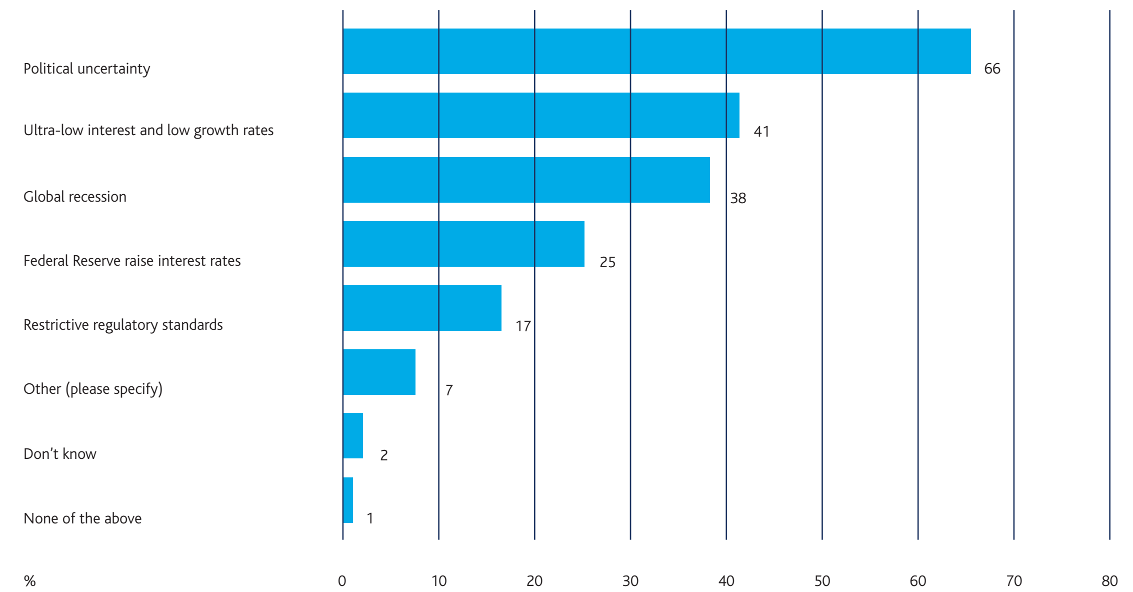


Figure 1B
IFAs



"Five years ago, politics didn't have such a huge impact on markets but the markets currently, and over the last three years, have been particularly sensitive to any political surprise, and there have been quite a few. Regulation, such as Solvency II, is also driving a lot of the technicals in the market place, which again can be very disruptive."

"The impact of the EU referendum pushed down yields even further so our liabilities are increasing."

Central bank monetary policy

Central bank monetary policy was also singled out as a cause for concern and viewed as creating an "artificial" environment that has possibly outlived its usefulness:

"Central banks' quantitative easing has had by far the biggest single impact – a global phenomenon that has just been exacerbated by Brexit."

"It's the domestic scene that worries me more [than the US or global]. I'm not sure the Bank of England will cut rates again but I think I'm in a minority."

"There are people that believe active managers have had a harder time competing against passive because quantitative easing is artificially making everything grow. Without the quantitative easing there would be more room for fundamental analysis, which would help active managers out-perform again. We would certainly like to see a return to a period where active management would be more in favour."

The International Monetary Fund's (IMF) latest report finds that short-term risks to global financial stability have abated since April 2016, but that medium-term risks continue to build.

It states: "The solvency of many life insurance companies and pension funds is threatened by a prolonged period of low interest rates. The political climate is unsettled in many countries. A lack of income growth and a rise in inequality have opened the door for populist, inward-looking policies. These factors make it even harder to tackle legacy problems and further expose economies and markets to shocks."

For us to avoid sliding into a state of financial and economic stagnation, it suggests: "a potent and more balanced policy mix to deliver a stronger path for growth and financial stability."

Our research found that while the majority of institutional investors and consultants were cognisant of the negative impact that uncertainty can have on the financial markets, and somewhat frustrated at the effects of quantitative easing and persistently low interest rates, they were typically pragmatic in preparing for potentially (even more) difficult times ahead:

"We've got pensioners who we still need to pay so we are going to be drawing down more money from our asset managers' funds. We need to get those assets working harder."

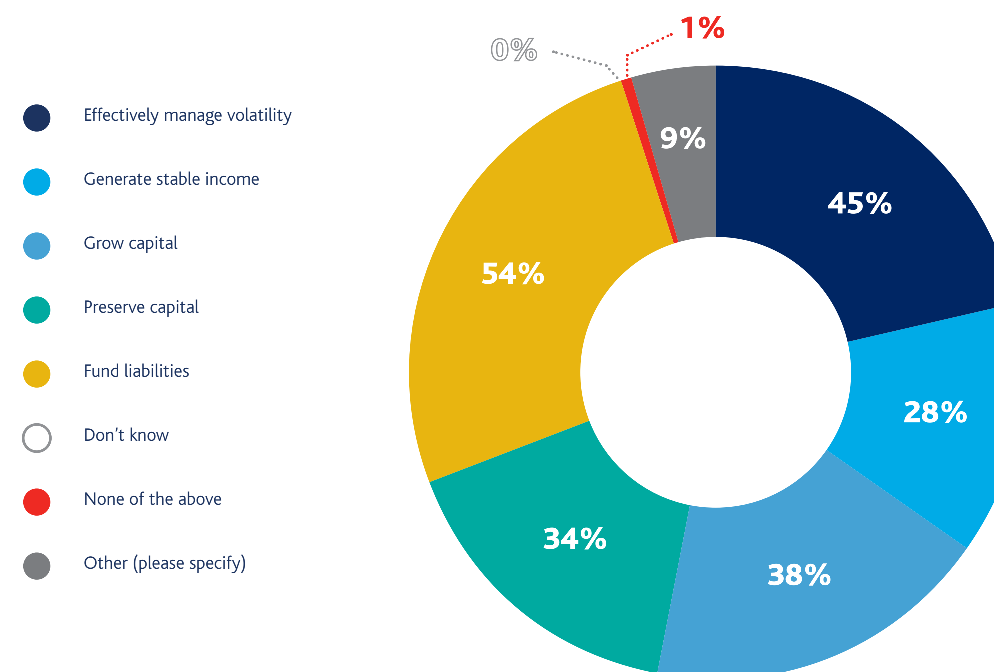
Key investment objectives for 2017: funding liabilities and volatility management

The majority of respondents who were predominantly engaged with fund management, DB pension schemes, insurance or other long-term investment strategies cited funding liabilities and volatility management as their primary investment objectives for 2017, staying focused on their long-term goals:

"We have the same objective every year and that is to deliver the lowest pension costs possible; a combination of good returns and low administration costs for managing the funds."

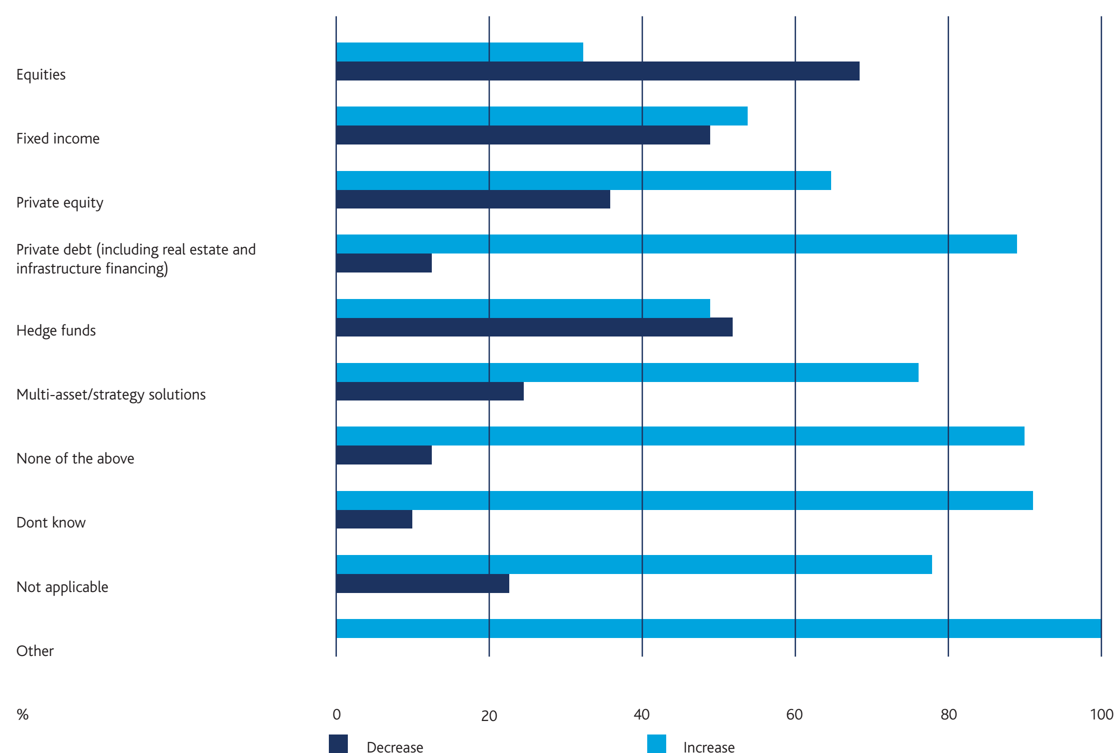
"For us, swallowing short-term volatility or large swings is something to be aware of and it's certainly something that we monitor but it's not going to be something that causes us to hit the panic button or deviate from what we do. We are so long term that we are okay with what occurs in the interim."

Figure 2
What are your/your clients' primary investment objectives for 2017? (Please tick all that apply)



Asked about their asset allocation plans for 2017, respondents expected to increase allocations to private debt (88%), multi-asset/multi-strategy solutions (77%), private equity (64%), fixed income (52%) and hedge funds (48%) and other strategies that would help preserve capital and manage risk, among them, liability-driven investments and insurance-linked securities.

Figure 3
Do you expect to increase or decrease your/your clients' allocations to the following asset classes over the short to medium term?



For one maturing DB scheme, the challenge is how to improve its funding position over the next few years without increasing its deficit in the short term:

"The scheme is maturing so we have a cash flow negative position, which will impact in the next ten years much more. At the moment we use the illiquidity premium, infrastructure, long-lease property, that kind of thing, but we also need to be thinking which assets we are going to use to turn on the taps to pay the pensions later on without going further into deficit now. If we go further into deficit now it's much harder to get back; you need to work twice as hard. "

To hedge or not to hedge?

Low long-term interest rates have led to an increase in the value of pension scheme liabilities, which has in turn affected funding ratios, often despite investment gains. One of the dilemmas facing pension schemes and other institutional investors is whether or not they should wait for better market conditions before hedging liabilities. If quantitative easing is increased and yields fall further it could ultimately prove to be a far more painful decision at some stage in the future. In our research, the cost of hedging against risk was perceived by a number of respondents to be expensive.

"We have looked into using some kind of option or hedging strategy for equity risk but we have found it to be too expensive."

As regards currency risk, while a fully hedged currency position is often assumed to help mitigate volatility, it can actually increase an investment's risk profile, depending on the specific dynamics of the underlying currencies.

"We hedge all fixed income exposure to our currency. Besides that we don't have any hedging strategies or specific strategies to hedge risk."

Liability management and measurement

The controversial subject of liability measurement being based upon gilt yields was a recurring theme.

"If a pension fund considers gilt yields to be fair value then they should fully hedge their liabilities. That doesn't mean they should not seek excess returns, as derivatives can be used to manage the liability risk and free up capital for investment. For investors who believe gilts are over-valued, the key question is: how big do you want that bet to be?"

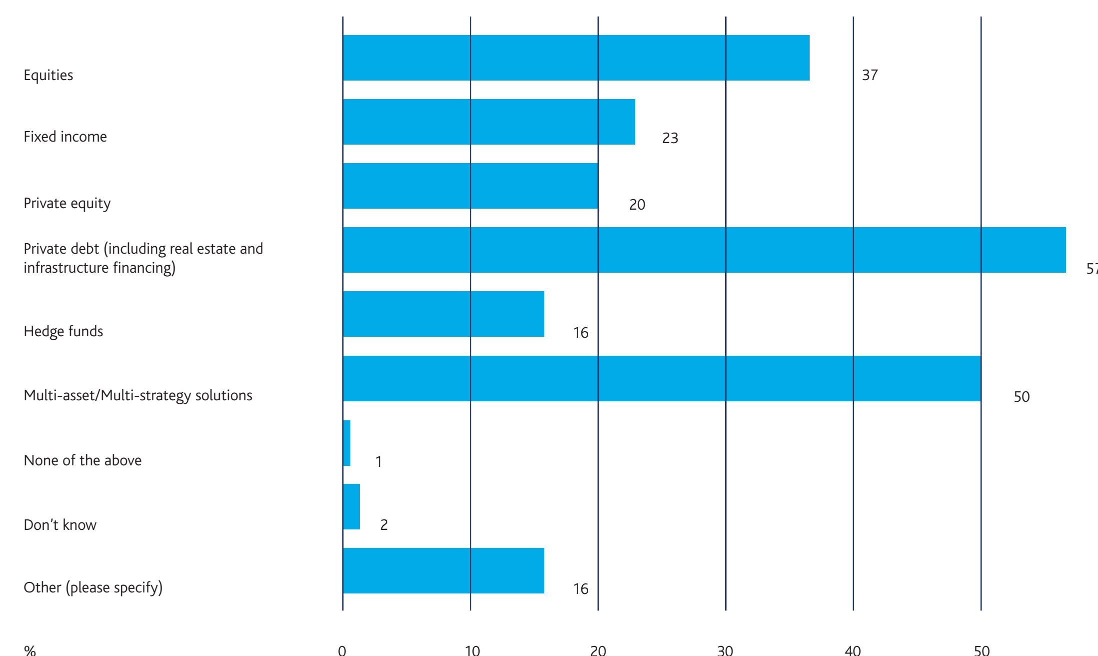
For one respondent, whose DB pension scheme is still open to accruals, the challenge is ongoing.

"If you can perfectly hedge your liabilities with your asset size it doesn't matter if you think rates are going up and down because the assets are going to perform in line with your liability. The issue is that we are still open and we still have 7% growth in liabilities. The best way to view that is the fact that we are still 77% return-seeking as opposed to having a higher hedge ratio. We are about 86% funded – very healthy but we are constantly revisiting and de-risking. When does it make sense? What sort of glide path would we want to adopt? It definitely would not be a quantitative, rule based de-risking strategy. It would be more of a guideline to follow and implement."

The search for yield

Recognising that achieving positive, risk-adjusted returns in the current low growth environment is especially challenging, we asked where investors' search for yield was taking them. Private debt emerged as an effective solution for confronting low interest rates, rising asset correlations, and volatile markets. This relatively illiquid asset class offers the potential for higher yields with less credit risk than similarly-rated public bonds. 57% of respondents were allocating or planning to increase their allocation to private debt, 50% to multi-asset/multi-strategy solutions, and 37% to equities.

Figure 4
Achieving positive, risk-adjusted returns in the current low-interest rate, low growth environment is especially challenging. Where is your/your clients' search for yield taking you?



Our qualitative research among institutional investors and consultants corroborated the quantitative findings and highlighted the trend towards an increasingly 'asset class agnostic' approach:

"We might be splitting our return-seeking assets into a short term cash pool and illiquid strategy, either private credit or infrastructure. The other thing we might do, to boost our yield, is move to a fiduciary manager. In theory they can be a bit more nimble and in terms of buying power, force down fees."

"With equities we are feeling a shift to active rather than passive. We are also looking at diversified growth and absolute return funds."

"We like the low volatility, diversified nature of multi-asset, multi-strategy products, and the fact that they pass down the short-term tactical allocation decision to a professional, the asset manager, rather than leaving it at the trustee level. I would say over 50% of our clients are in a fund which is asset class agnostic in some shape or form."

Private debt, property and infrastructure

Allocations to property have long been part of an investment strategy that aims for 'all weather' protection by delivering better returns than bonds in high growth periods while also proving more defensive than equities in times of lower growth.

Insurers and mature DB schemes in our research were typically invested in property that provides secure, long-term income while less mature DB schemes were open to more illiquid opportunities or opportunistic funds.

Infrastructure investment was perceived to offer the potential for attractive risk-adjusted returns, reliable inflation-linked returns, stable long-term yields, capital growth and credit diversification benefits that are particularly well suited to pension schemes, insurance companies and other institutions with long dated liabilities. However, pricing, lack of transparency, political risk and the implications of Solvency II were identified as causes for concern:

"We are very focused on keeping costs low and for some of those asset classes, such as private equity and infrastructure, we have concluded that the costs are too high for us. The risks are also high because they are not very transparent – there may also be political risks. We had to decide either to increase the exposure and develop internal resources to handle those exposures, or completely get out of everything in private equity, and we chose the latter. We had some very good managers and we had some managers not performing so well. We found on average we had approximately the same returns as we did with listed equities."

"The issue is how to price it [infrastructure investment]. Can you buy it through a fund and spread your risks? Can you get the information you need to populate the regulator returns? And can you get any concession on the capital charge you have to take on it because although the government makes all the right noises about encouraging infrastructure, I've got to be prepared to have it treated for solvency purposes as though it was an equity."

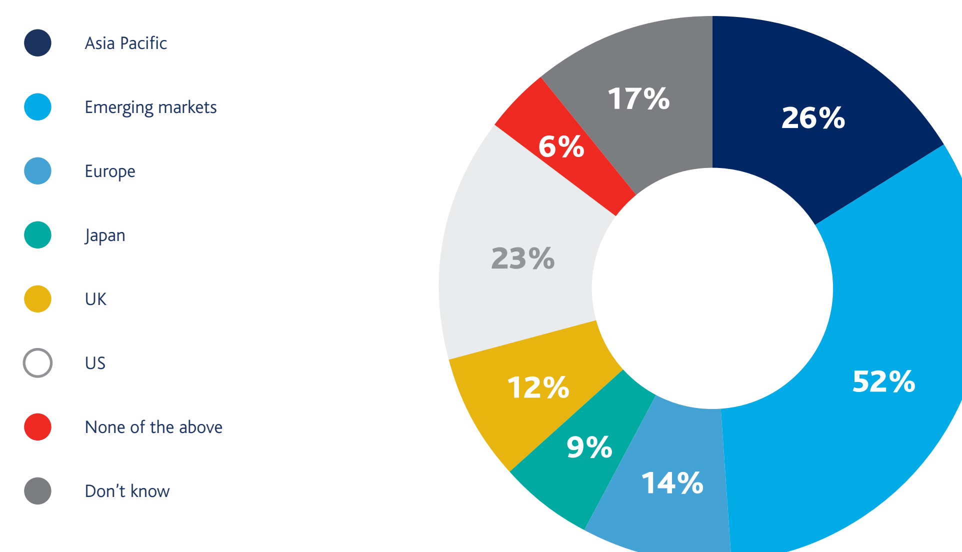
James Hughes, Head of Aberdeen Solutions, says: "The current uncertainty in the economic environment highlights the benefits that infrastructure investment can bring to an investor's portfolio. Infrastructure debt is particularly attractive for its stability through changing macro and credit conditions. There are also the added benefits of defensive characteristics emanating from the provision of essential services and potential value enhancement through active asset management.

Property continues to offer the potential for income, growth, added value through active asset management, with a real asset underpin. However, it usually requires a substantial investment sum and resource-intensive management to access directly, which can also involve complex legal and tax arrangements if you venture outside your region's jurisdiction. As a result, many investors prefer to invest via funds and funds of funds, to best capture the breadth of opportunities available. A multi-manager approach, in particular, can provide access to high quality property funds and managers, offering exposure to any or all of debt and equity, prime and secondary locations, domestic, regional and global investments, and operating assets or developments. We're certainly seeing continued interest from our clients across all variations of real estate."

Best equity opportunities: emerging markets and Asia Pacific

Respondents were unanimous in citing the world's emerging markets (52%), and Asia Pacific in particular (26%), as offering the best equity opportunities, followed by the US (23%).

Figure 5
In which regions do you see the best equity investment opportunities in 2017? (Please tick all that apply)



"We are expecting more return to start coming from emerging markets again."

Devan Kaloo, Head of Equities at Aberdeen, says: "Economic growth is returning to emerging markets on the back of orthodox monetary policy, which stands in stark contrast to the intractable mess developed markets find themselves in. This orthodoxy is beginning to pay off. Having raised interest rates and endured austerity to tame inflation, emerging market central banks positioned themselves to cut rates again and restart growth, which has led bond prices to rally. As yields have fallen equities are also rallying, driving fund inflows and leading currencies to rally too. After working through recessions, both Brazil and Russia are forecast to deliver positive GDP growth in 2017 for the first time in years.

At the same time we are also seeing a recovery in company earnings. Increased company discipline in terms of costs and capital expenditure should also support improvements in returns on equity."

Longevity risk: under control or in need of reappraisal?

Longevity risk has been the subject of some controversy in recent times; the risk that more people will live longer than expected has far-reaching implications not only for life insurance and pension providers, but also those budgeting economic resources and creating shareholder value in public companies. The IMF has been critical of actuarial estimates, warning that if governments and corporations do not change their formulae, they face costs that could cripple both business and economies. We asked institutional investors and consultants for their views on this.

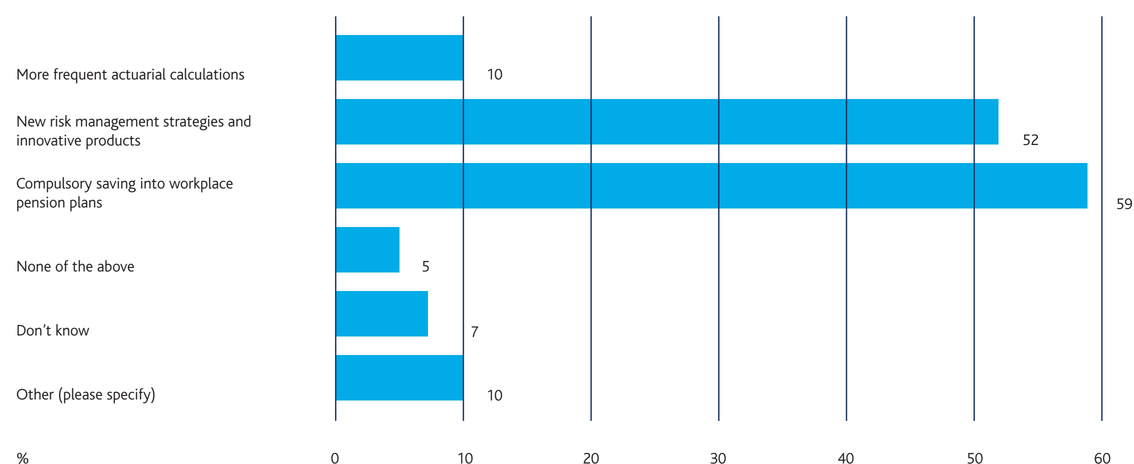
Almost half (44%) of respondents agreed that longevity risk is given sufficient priority whereas 38% believed that it should be given more attention. In the words of one respondent (responsible for DB pension scheme investment strategy):

"It [longevity] is a significant risk but not a 'blow-up' risk – we are managing it without going to the extent of investing in longevity swaps, for example."

"We have had quite a bit of discussion about longevity. At the moment we are deciding not to do anything about it in terms of a buy-in or longevity swaps with an insurance company."

To help their clients tackle longevity risk, 52% of respondents would like to see asset managers develop new risk management strategies and products, and a similar number (59%) reported that compulsory saving into workplace pension plans is most likely to help.

Figure 6
Longevity impacts on the institutional investment community and individual savers/investors. What do you believe will best help manage longevity risk?

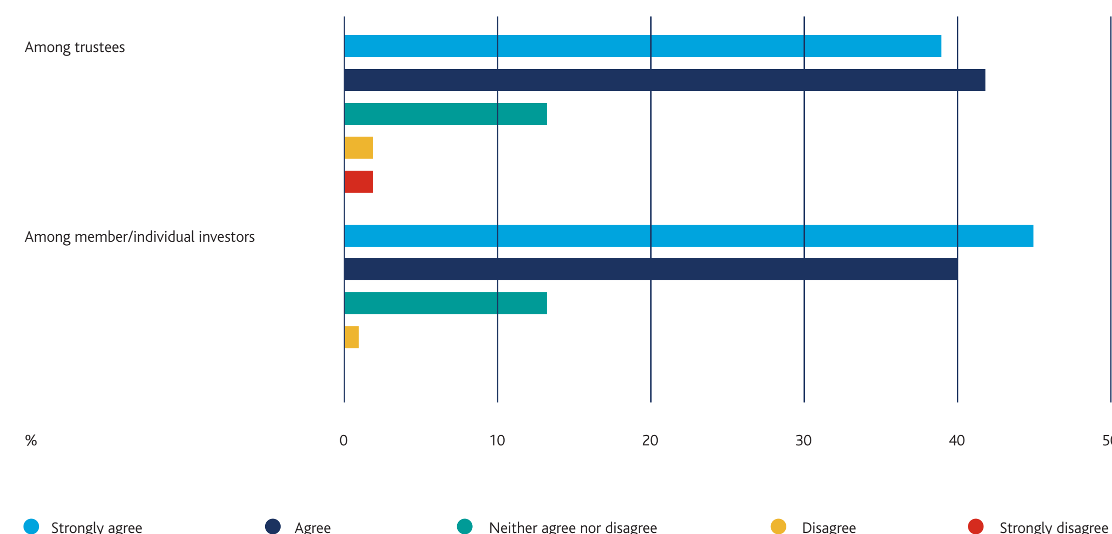


One pension professional suggested that it was much more of an issue for defined contribution (DC) investors: "Then it's less about the actuaries getting it wrong, it's more about the members getting it wrong."

Empowerment through financial education

Institutional investors, consultants and IFAs were unanimous on the benefits of additional financial education as being of fundamental importance to our future financial health. 82% of institutional investors and consultants agreed that the industry and policymakers should allocate more resources to financial education with respect to trustees; and 85% agreed that the same should be done for pension scheme members/individual investors.

Figure 7
Trustees are typically keen to improve their investment knowledge, and studies have found that there is a growing interest in gaining a better understanding of financial markets among the young. Given the complexity of the financial landscape and longevity risk, do you agree/disagree that the industry and policymakers should allocate more resources to financial education?



"Most trustees are lay trustees and there is so much more that could be done in terms of training and understanding the interaction of the assets and the liabilities."

When asked to propose just one change that would empower the investors of tomorrow (be they institutional or individual), financial education was one of the top recommendations: "Make financial education mandatory in all schools (preferably with core GCSE status)"; "education on managing finances for school-aged children"; "educate them about personal finance earlier in life"; "teach all children the benefit of pound cost averaging over a long period of saving."

Suggestions with respect to personal investors also included: "new savings products that allow growth"; "allow the baby boomers to safely and easily transfer wealth to their children and grandchildren before they die"; "put in place minimum non-contributory pension contributions for all employees providing tax benefits to those companies who offer this".

Professional investor advice on empowering fellow institutional investors ranged from suggestions that echoed the findings of the Kay review[2] to shorten the investment chain, to "more acknowledgement of the unknown unknowns – to which diversification is the only solution"; and specifically, "increase interest rates".

There was also a resounding call for more stability: "What we need is a stable, well-principled regulatory framework for pension scheme provision. Unfortunately we haven't had that. "

What we need is a stable, well-principled regulatory framework for pension scheme provision. Unfortunately we haven't had that.

The current somewhat controversial methodology for calculating pension scheme liabilities was a recurring topic. Among the comments from professional investors and consultants were: "Change the assumptions/methodology currently used in calculating DB scheme liabilities so that we can return to worrying more about assets that will produce growing income streams and pay future pensions"; and: "change the accepted wisdom around the basis of actuarial valuations to be non-gilts based."

These policy 'impositions' weren't the only cause for complaint. Solvency II data workstreams were reported by insurers in our research as being a very unwelcome distraction from the business of managing investments to the benefit of beneficiaries.

"We're subject to Solvency II and have done our initial reporting, but we are very concerned about the asset reporting we will have to do at the end of this year. We're a small firm and need to manipulate the data from several sources. We are talking to specialist firms but it's like trying to nail jelly to a mast. We obviously need some kind of resolution which will enable us to be compliant at the year end."

According to PwC: "The biggest challenges are yet to come if they [insurers] are to achieve compliance. Few organizations have implemented the data governance frameworks they designed over the last 12 to 18 months. Establishing a framework is a potentially complex and lengthy process."

[2]The Kay Review of UK Equity Markets and Long-Term Decision Making, July 2012

Financial advice among the robots and algorithms

Patterns of wealth, saving and investment around the world are fast evolving, with the same low interest rate, low growth challenges facing individuals and their financial advisers as we have seen among institutional investors.

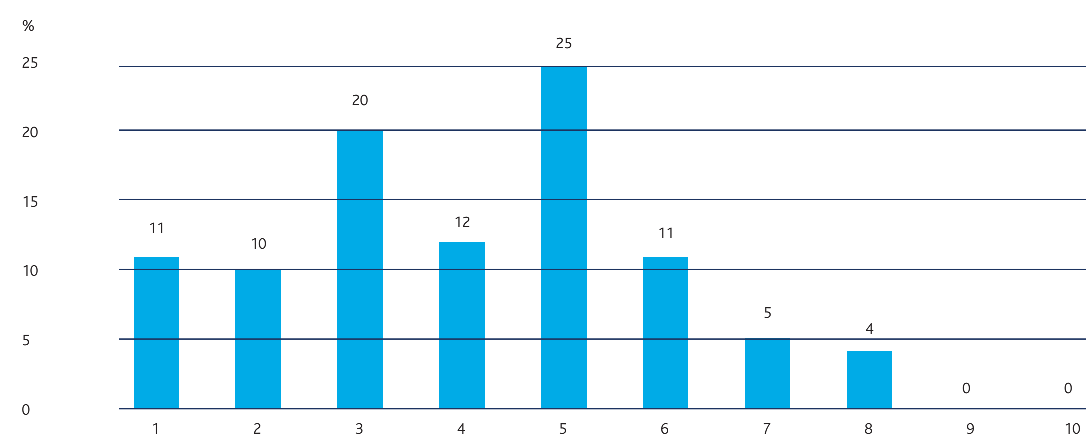
The adviser community is also coming to terms with the rise of automated advice in the form of 'robo' and virtual advisers; these online platforms that offer algorithm-based portfolio management recommendations are especially prevalent in the developed economies.

While digital financial advice platforms are proliferating, financial advisers are sceptical about their value but nonetheless acknowledge that they will play a greater role in the future and agree that digital platforms could significantly increase business efficiency, particularly in handling less wealthy clients.

According to PwC's research, technology advances and regulatory changes have also brought new transparency to the wealth management process and: "Today, clients want more personal, more real-time, more effortless interactions. The inheritors of wealth over the next five to 10 years will not necessarily choose to keep their parents' financial advisers. Companies must design an onboarding strategy for generation X and millennials soon, given that by 2020 they will control more than half of all investable assets, or about USD30 trillion."

Our survey of UK IFAs found that the Fintech phenomenon was not perceived as especially disruptive to the industry in the same way as Amazon and eBay, for example, have disrupted the retail sector. Technology is accepted as part of today's world but respondents thought that direct to consumer personality-based questionnaires are not that effective.

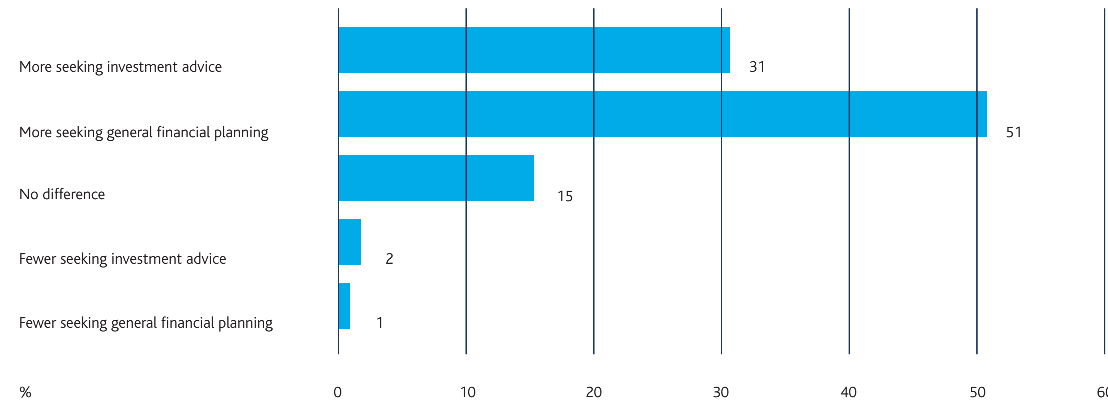
Figure 8
Some online direct-to-consumer investment platforms use behavioural finance-inspired personality-based questionnaires to match clients to portfolios; how effective do you believe these to be (where 1 is not at all effective and 10 is very effective)?



Competition is expected to increase as both new entrants and traditional providers expand their offerings to deliver a more digital-based service, and yet IFAs in our research appeared confident that this would exist alongside the distinctly relationship-based service they provide.

82% of IFAs reported an increase in clients seeking investment and planning advice following the pension freedoms.

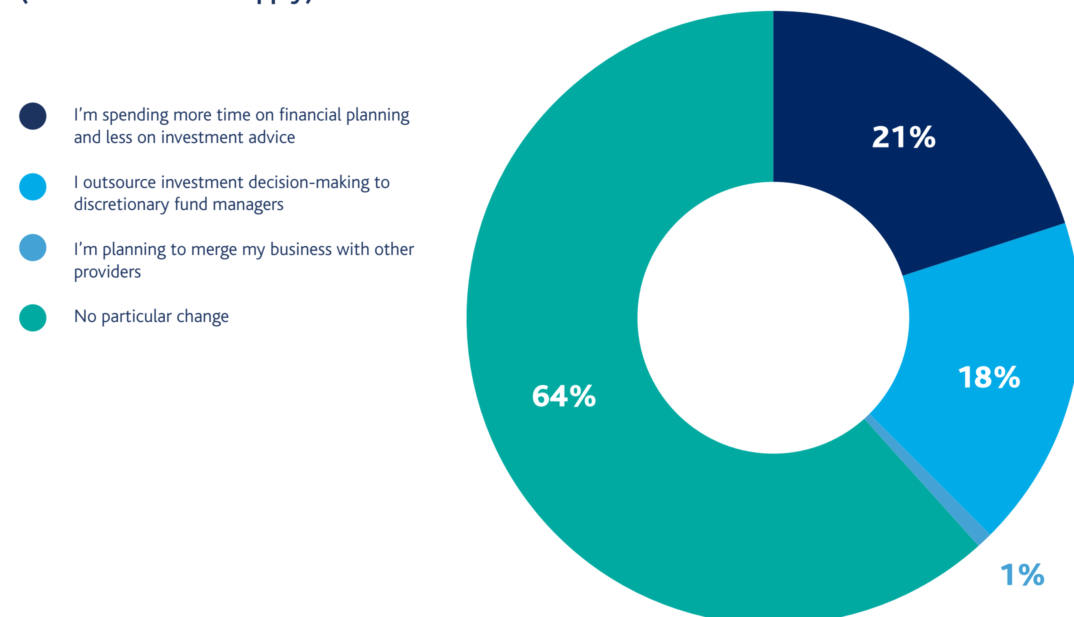
Figure 9
The pension 'freedoms' have led to more choice and some would argue, more complexity and the potential for more confusion (among individual investors). In your experience, are your clients more or less reliant on you for investment guidance than before the pension freedoms came into force?



According to an international study[3], financial advisers will need to become "multidimensional professionals able to provide both specialized advice and life goal-planning…when selecting wealth advisers in the years ahead, investors will continue to use long-standing criteria, such as quality, fees, reputation, and range of services. But investors will also assess wealth advisers on new measurements: their digital capabilities. These include anytime, anywhere, any device access, integrated omni-channel experience, and advanced use of digital technology and analytics. According to providers, over the next five years, advisers will need to adapt their roles in several fundamental ways, including providing more responsive, 24/7 service, offering superior investment advice, becoming digitally savvy, providing a broader range of life-planning advice, and reducing fees. The role of the adviser will take the form of a 'general practitioner,' who can call on a cadre of specialists when necessary."

In our research, the majority of IFAs (64%) are not changing their business to take account of 'do-it-yourself' investing, although a fifth (21%) are spending more time on financial planning.

Figure 10
How are you adapting your business/service to take account of the increase in 'do-it-yourself' investing by means of direct investment platforms and the changing face of financial advice? (Please tick all that apply)



[3]Roubini ThoughtLab, 'Wealth and Asset Management 2021, preparing for transformative change', 2016

Investment perspective: multi-asset, multi-strategy; emerging markets

IFAs are focused on multi-asset and multi-strategy solutions (66%) and equities (60%) in their search for yield.

Figure 11
Achieving positive, risk-adjusted returns on behalf of clients in the current low-interest rate, low growth environment is especially challenging. Where is your search for yield taking you?

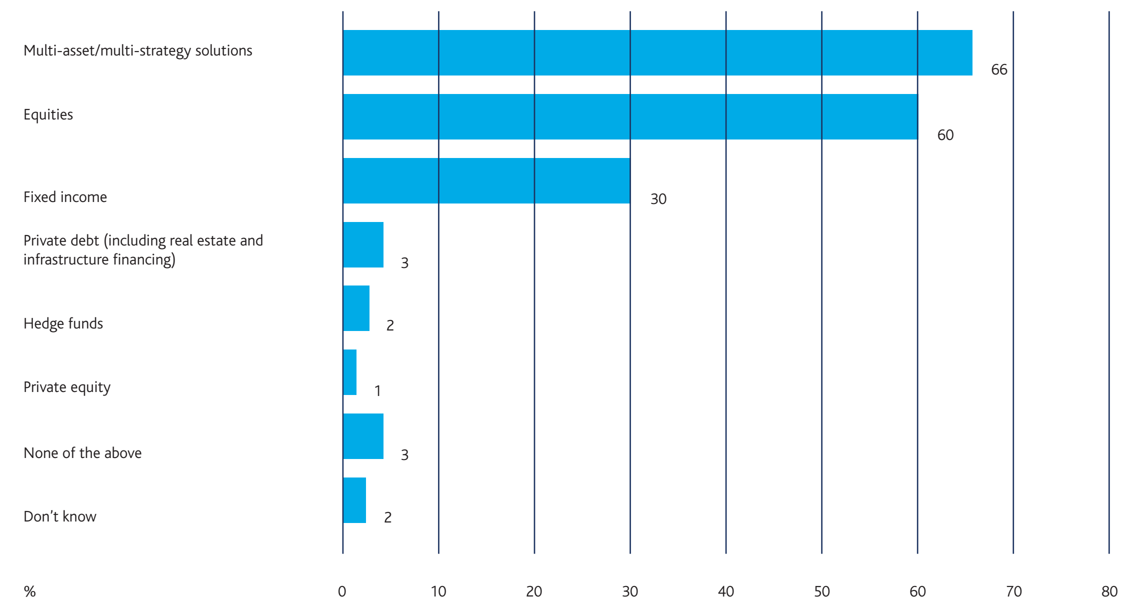
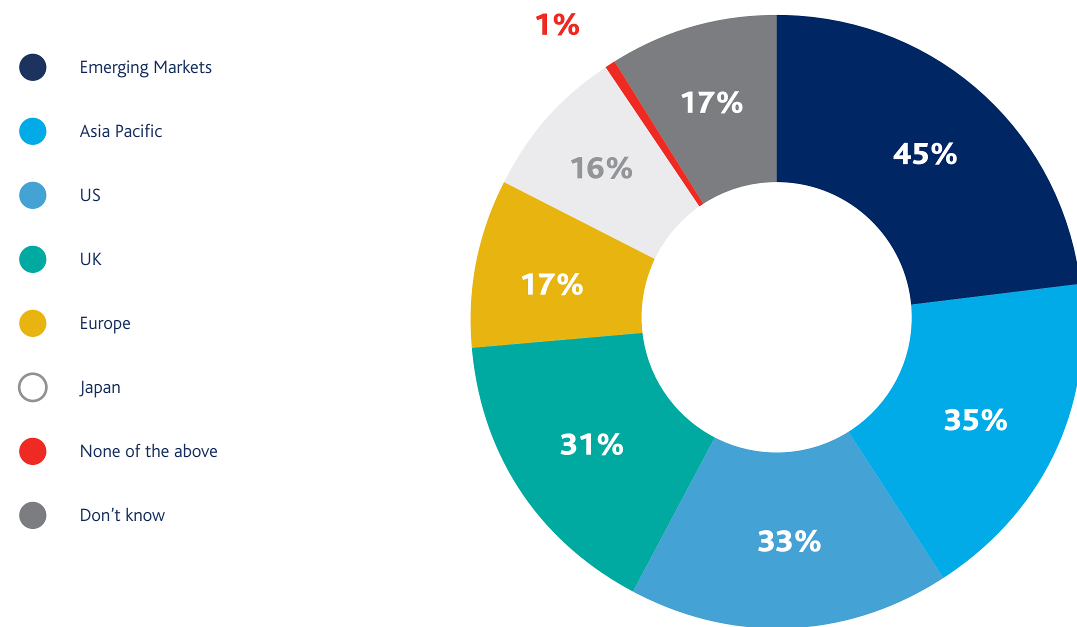


Figure 12
In which regions do you see the best equity investment opportunities in 2017? (Please tick all that apply)



Favoured regions for the best equity opportunities were cited as emerging markets (45%), Asia Pacific (35%), the US (33%) and UK (31%).

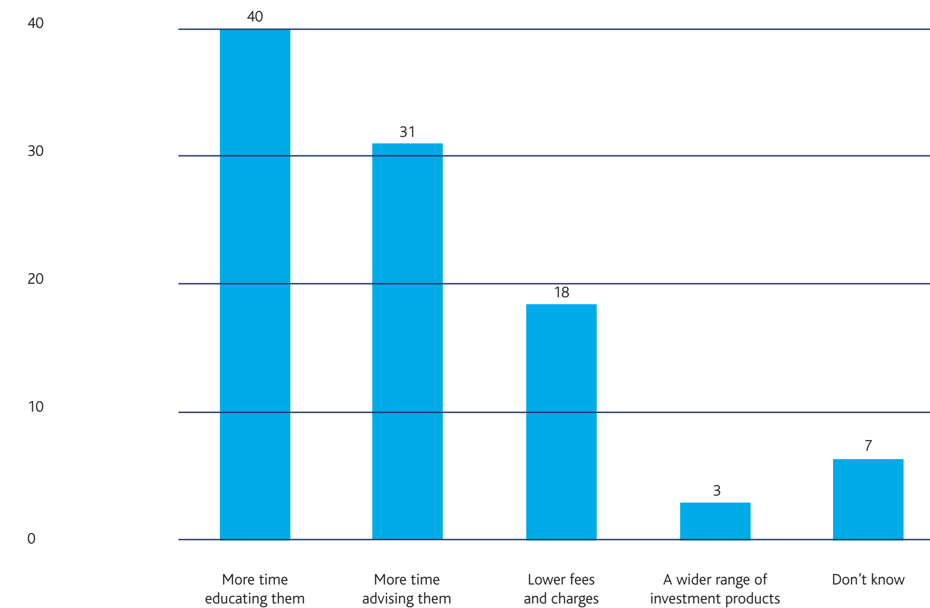
Commenting on the findings, Scott Dakers, Head of UK Regional Sales at Aberdeen, said: "Asset managers need to demonstrate that they understand the challenges that advisers and consumers face and that the products and solutions we offer really do deliver on the factors that they have been selected for. At Aberdeen we have been considering solutions to help in both the accumulation and decumulation stages of life and we believe our multi-asset range can offer stand-alone solutions or can be blended cost effectively to provide advised bespoke portfolios."

Empowering savers and investors towards a better financial future

IFAs reported that education and guidance is more empowering to their clients than lower fees and charges or a wider range of investment products.

Almost four in ten (37%) IFAs spend a lot of time educating clients before offering advice and 71% believe that more time educating and advising clients would empower them towards a better financial future, as opposed to lower fees and charges (18%) and a wider range of products (3%).

Figure 13
If you could offer just ONE of the following to help empower your clients towards a better financial future – at no additional cost to your business – what would it be?



Before empowerment must come knowledge and acquiring knowledge requires a willingness to learn

Savers and investors: confused or just disinterested?

Our research included online interviews with 555 retail savers and investors from across the UK, to provide an up-to-date picture of their financial motives and interests.

The findings reveal some anomalies when viewed in conjunction with the findings from pension scheme trustees, investment professionals and financial advisers.

A number of pension scheme trustees interviewed lamented the persistent lack of interest from members in their retirement planning, pointing to the majority of DC scheme members who choose to invest in default funds as evidence of this, despite the widespread availability of good quality member engagement communications and other sources of financial information.

Before empowerment must come knowledge and acquiring knowledge requires a willingness to learn. The perceived complexity of pensions, saving and investing and the shortage of effective solutions persist as barriers to engagement. Among the suggested solutions from professionals were: "a simple, all in one life-time savings plan"; and "make it simpler to start saving into a pension."

Taking advantage of new technology was also proposed as empowering: "More readily available and understandable advice/information. Making use of technology such as mobile devices to achieve this is the way forward."

For those who were prepared to engage in investment decision-making, the advice was: don't try to time the market, 'think diversification', and stick with investments for the long term.

Our research found that a simpler, easier to understand range of options would best empower savers' and investors' decisions (30%), followed by more knowledge about the options available to them personally (28%). This corresponds with recent research by Nottingham University Business School and Willis Towers Watson: "Factors contributing to the crisis of confidence for savers include a lack of knowledge/information (35%), complexity of investment choices available (25%) and a general distrust of financial institutions (25%)."

Figure 14
Which ONE of the following would best empower you to make effective savings and investment decisions?

James Devlin, Director of Nottingham University Business School's Centre for Risk, Banking and Financial Services said: "From a behavioural economics point of view, one potential solution is to nudge people to engage in more suitable behaviour, using approaches that make the choice process significantly more user friendly. Our research also shows that the UK is somewhat polarised when it comes to knowledge and confidence so any approach must also be personalised to take this into account. Technology should be used to tailor services and communications to individual savers, and make them more engaging and relevant to their specific needs."

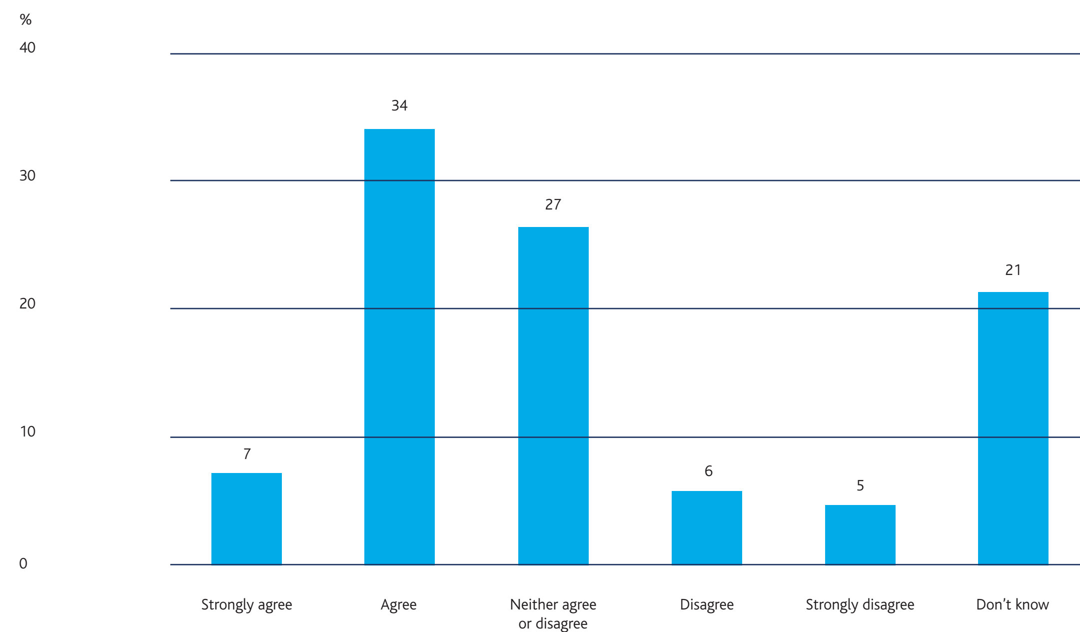
84% of savers and investors surveyed replied that they had confidence in financial technology. This demonstrates that technology has a place, so long as providers can find the right way of using it to deliver simple solutions.

> 84% of savers and investors surveyed replied that they had confidence in financial technology

In the absence of one-to-one financial advice, which is deemed unaffordable to a large majority of savers, could more 'automated guidance' help? In our research, 14% opted for online guidance that directed them to a range of personalised saving and investment options.

Given the substantial increase in the number of direct-to-consumer investment platforms that use personality-based questionnaires to match investors to portfolios or investment products, we asked to what extent personality influences saving and investment decisions. 41% agreed it does but 21% didn't know and 11% disagreed – a finding that is perhaps unsurprising when we consider the wider attitude towards saving and investing for the future.

Figure 15
Some online direct-to-consumer investment platforms use personality-based questionnaires to match investors to portfolios/investment products; to what extent do you agree/disagree that personality influences saving and investment decisions?



Commenting on the findings, Iain Plunkett, Chief Operating Officer and Chief Information Officer at Aberdeen, said: "Ever since the first adviser and client facing platforms were launched over fifteen years ago, savers and investors have become increasingly comfortable with buying funds inside and outside tax wrappers online. More recently, digital innovations have focused on providing online advice and automating portfolios and whilst early take-up has been limited, the clear direction of travel is towards providing algorithm based packaged solutions, rather than open access to markets.

In providing solutions, it is important to remember that clients' repeated plea tends to be for simplicity, ease of access and ease of understanding. All asset managers need to take note of this both in product design and the development of supporting services.

Aberdeen is looking at providing an innovative platform to the corporate workplace market and potentially, via retail partnerships, directly to clients. In developing these new services the balance needs to be made between clients' need for ease of access and simple choice with some decisions; and the need for greater understanding and flexible help and advice for others. All services need to be client rather than technology driven."

All services need to be client rather than technology driven

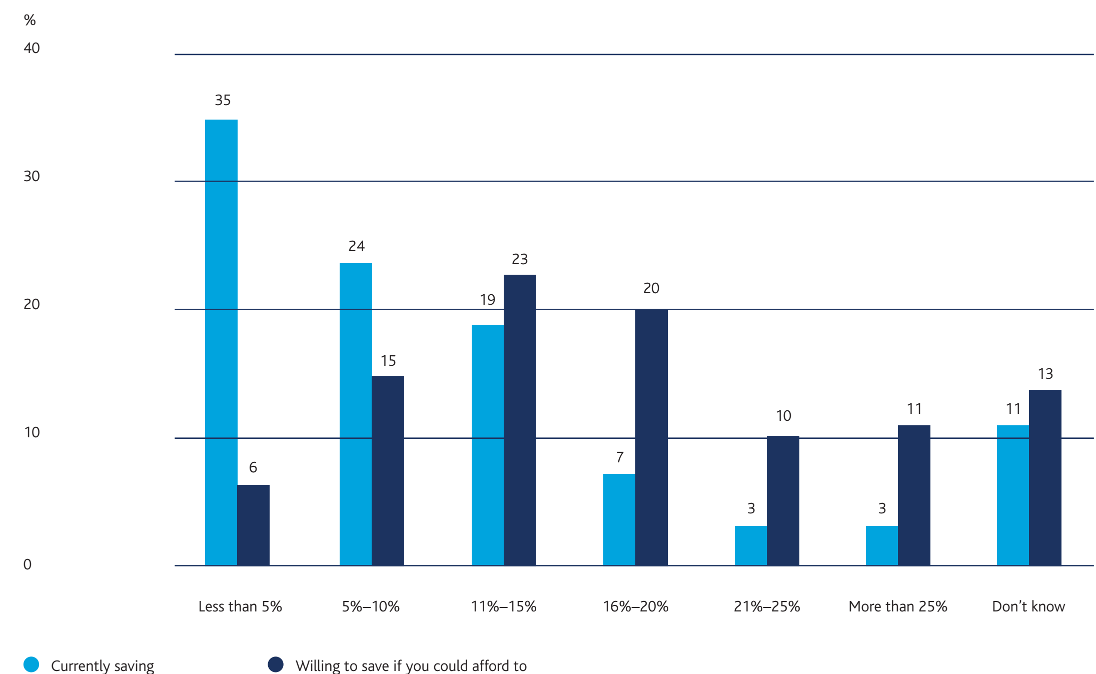
Saving enough to last a lifetime

The inadequacy of retirement provision was talked about as the nation's number one socio-economic challenge at this year's Pensions and Lifetime Savings Association's (PLSA) conference; a large percentage of the UK population are woefully ill-equipped on how best to achieve a good retirement outcome; this includes a significant number who do not appreciate how much they might need to see them through a long life in retirement.

Our research found that 70% of respondents were largely confident that they will have enough money to last through retirement, but were on average saving only 9% of their annual salary. 35% were saving less than 5%. Despite being willing to save on average 16% (if they could afford to) replacement ratio estimates would suggest that this is unlikely to be enough, particularly for those who do not start until their 30s or 40s.

Figure 16
Research has found that the amount we in the UK save towards our retirement is among the lowest in the world (9.2% of income annually compared to, for example, 21.3% in Taiwan and 15.9% in Singapore).

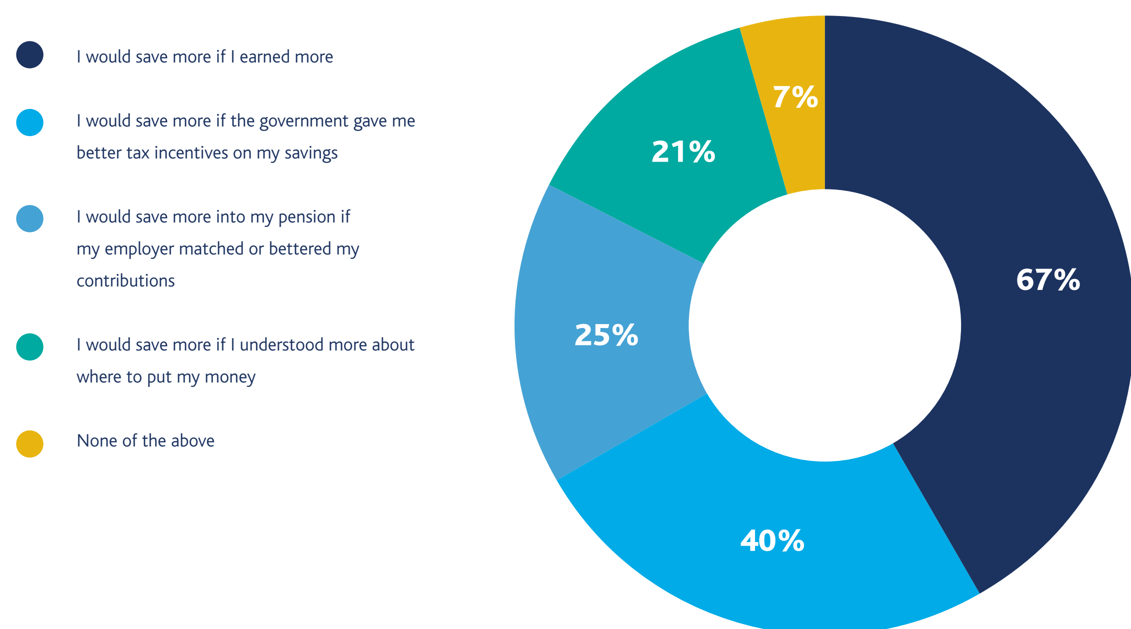
How much of your annual income are you: a) currently saving b) willing to save if you could afford to?



What would encourage people to *save* more?

67% of respondents said they would save more if they earned more; 40% would save more if the government gave better tax incentives, 25% if their employer matched or bettered their contributions, and 21% if they understood more about where to put their money.

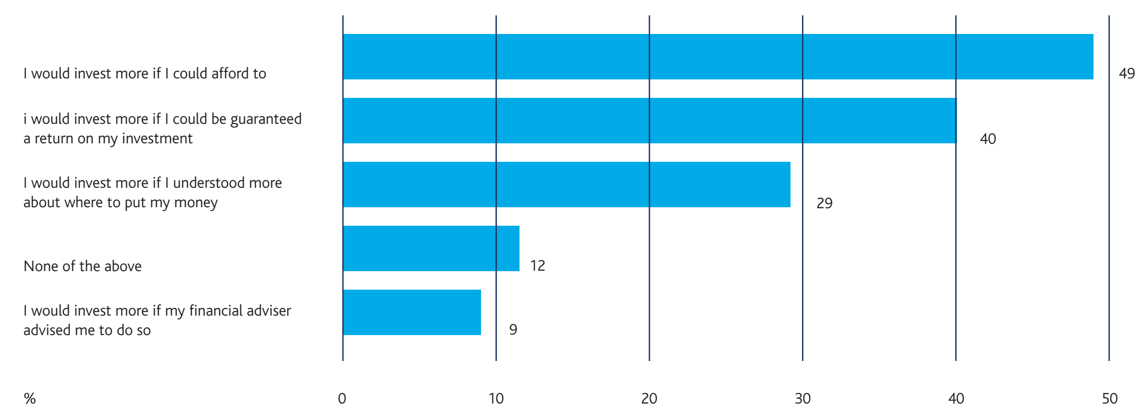
Figure 17
Low interest rates and the threat of rising prices (which can eat away at the value of your savings) mean that saving and investing has become more challenging. What would encourage you to save more? (Please tick all that apply)



What would encourage people to *invest* more?

Recognising that the low returns offered on cash savings mean that some people are turning to investments in order to get more for their money, we asked what would encourage them to invest more, bearing in mind that all investments carry a degree of risk.

Figure 18
The low returns offered on cash savings mean that some people are turning to investments in order to get more for their money, although all investments carry a degree of risk. What would encourage you to invest more?

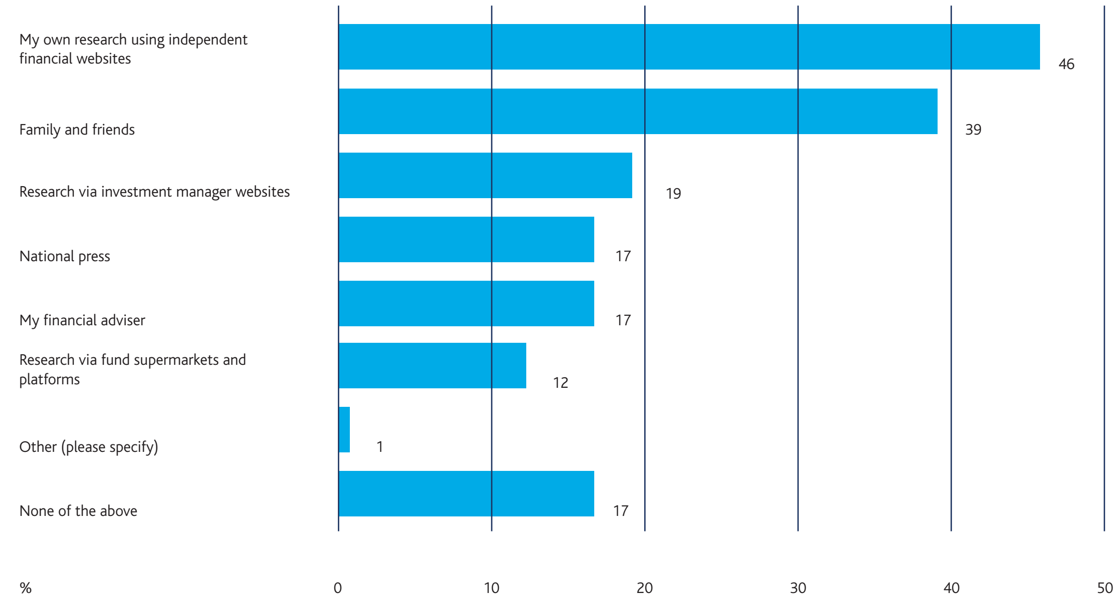


49% would invest more if they could afford to, 40% would invest more if they could be guaranteed a return on their investment, and 29% if they understood more about where to invest.

While respondents found the pension freedom changes and choices more empowering (31%) than confusing (24%) there is a 'pinch point' at which too much choice can be inhibiting. According to Nottingham University Business School and Wills Towers Watson's study: "Employees are suffering from a crisis of confidence when it comes to making financial decisions and are agonising over their long term financial choices and health. The large number of available saving options is one of the main factors contributing to this crisis of confidence – with over a third of consumers (34%) revealing they think there is too much choice when it comes to saving for retirement."

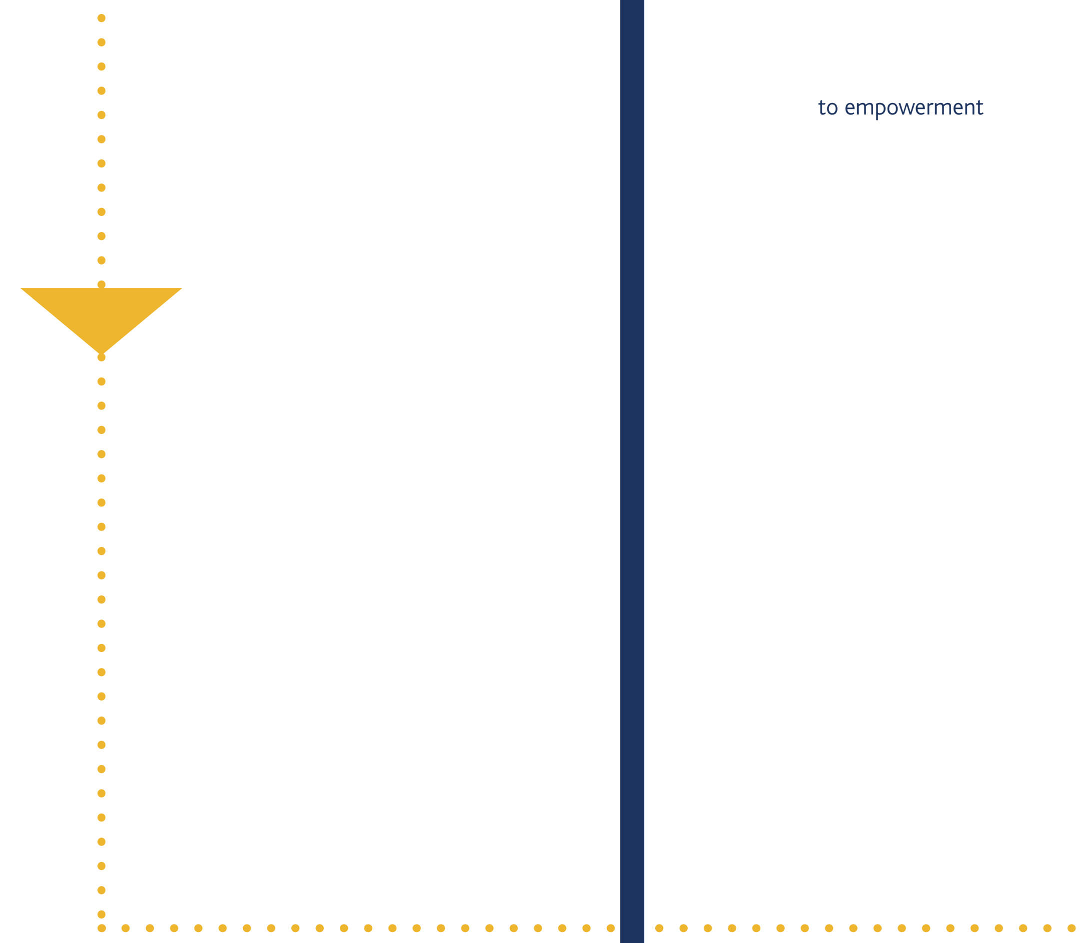
In our research, the majority (63%) were confident they have made the right savings and investment choices for their future and were largely self-dependent in what sources of information they use. 46% do their own research using independent financial websites, 39% rely on family and friends, 19% research investment manager websites and an equal number (17%) use their financial adviser and the national press.

Figure 19
What sources of information do you use in your saving and investment decisions?



Commenting on the findings, Gregg McClymont, Head of Retirement at Aberdeen, said: "A solution to the under-savings crisis depends on the three pillars of the UK's long-term savings system – state, workplace and individual provision – working efficiently together. This means a state pension which is simple to understand, workplace saving as a matter of course, and private provision where value for money is the rule.

The good news is that the UK has made progress in all these areas. But there is much more to do. Increasing savings contributions in the workplace is likely to be the most efficient means of increasing savings rates. But such have been the marvellous year on year rises in longevity that greater savings go hand in hand with longer working lives. The three stage life that has characterised the twentieth century – education, work, retire – is being replaced by a more fluid multi-stage life in which work remains part of our lives for longer. A child born in the West today has a 50% chance of living to 105!"



Conclusions

Political and economic uncertainty is adding to the challenges faced by institutional investors, consultants and IFAs, on top of an already highly demanding regulatory environment.

Prolonged, ultra-low interest rates are perceived as a dangerous comfort blanket. Further quantitative easing is expected merely to extend the artificiality of the investment environment and there is a significant appetite among professionals for a return to conditions that would allow more fundamental analysis and a 'real' economy.

The current economic climate means that all investors – institutional and individual – are missing out on the illiquidity premium that comes with buy-and-hold investing.

Individual savers and investors have welcomed the pension freedoms but their underestimation of how much of their annual income might be needed to see them through their life in retirement points to the need for much more financial education. Otherwise, there is a real danger that the burden of responsibility placed on them for their financial future will be overwhelming.

Technology is transforming the investment sector. Innovations offer the potential to increase transparency, efficiency and competitiveness – they also bring a different set of risk management challenges. All market participants need to focus on ways in which new technologies might benefit both consumers and markets but will not be able to do so without the right economic and regulatory conditions. Yet again, this research, as with so many reports that precede it, calls for a period of stability from policymakers and regulators.

Asset managers and policymakers must work together to ensure that new initiatives, rules and regulations are a help to investors and not a hindrance, to ensure that investors are genuinely supported and empowered towards a better financial future.

This research, as with so many reports that precede it, calls for a period of stability from policymakers and regulators

Aberdeen's response

Aberdeen is a full-service asset manager. Geographically diverse and with investment capabilities across multiple asset classes, we are well placed to meet the long-term needs of investors around the world.

We are responding to political, economic, regulatory and technological challenges in ways that embrace change and harness the power of innovation to ensure that investors are truly empowered. We think in terms of opportunity not threat.

We are committed to capitalising on new technology both to the benefit of clients and to ensure that our business remains competitive. Asset managers are better placed than tech-based firms to deliver what investors need. While we must take heed of opportunities to use technology in order to drive down costs, we must also beware the dangers of commoditisation, the diminishment of manager skill, and the consequent impact on value creation, to the detriment of investors.

Our innovation committee, one of the first in our sector, demonstrates our open, meritocratic commitment to new ideas and the engagement of Aberdeen's younger generation. Of significant focus in this regard is our development of new products, across new channels to satisfy investors across all age-groups to and through retirement, including access to low-cost, easy to understand solutions with transparent costs and fees.

Our drive to innovate and embrace new technology is always advanced within the robust framework of our core strategic vision and values. We never attempt to 'time' a sector or a stock, or to succumb to trends long after the opportunity to profit has passed. Our investment approach aims to weather market volatility over years, not months.

Asset managers have an important, and some would say privileged role to play in helping clients to meet their financial goals. Amid a great deal of uncertainty, we take our responsibilities to clients and the wider investment community very seriously. All stakeholders with whom we engage can rely on us to continue to provide the experience and commitment that will be so important in the months and years ahead.

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Tony English, Principal, Mercer

Trond Todnem, Senior Portfolio Manager, Statoil Kapitalforvaltning

For more information visit www.aberdeen-asset.co.uk

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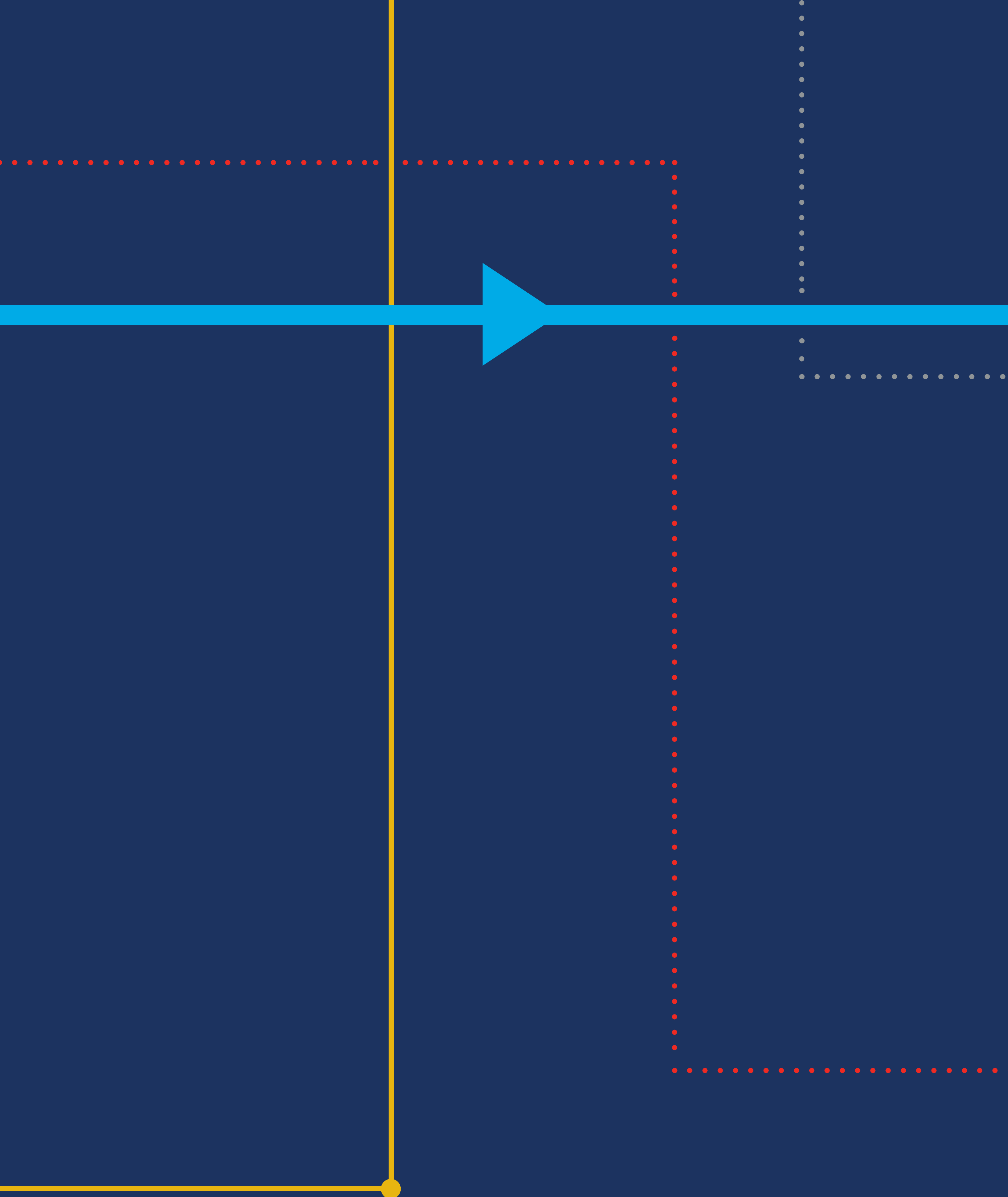

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