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AVIVA INVESTORS

RESEARCH REPORT: MEETING THE INCOME NEEDS OF TODAY'S INVESTOR

Research among independent financial advisers, discretionary wealth managers and individual investors

September 2015

AVIVA INVESTORS

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INTRODUCTION

Every investor needs a specific outcome from their financial products and achieving a sustainable income is one of the key priorities for UK investors. Yet investors in search of income face unique challenges today.

To complicate matters further, the legislative changes that followed the financial crisis of 2007/2008, including the Retail Distribution Review and recent pension reforms have changed the investment landscape forever. This latter change has introduced another level of uncertainty among financial intermediaries, with scepticism from some that the reforms will be modified before too long. With financial intermediaries already under pressure from what they view as persistent regulatory change and increasingly high customer expectations, they are experiencing an upsurge in requests for advice.

This is the background against which we commissioned the research in this publication. It examines the key considerations in the search for income and the challenges facing those responsible for the financial well-being of individual investors.

ABOUT THIS REPORT

This report is based on independent research carried out by Gabriel Research & Management Ltd. They conducted interviews with advisers and wealth managers with clients holding investable assets ranging from £50,000 to in excess of £1 million and with individual investors holding any of the following: pensions, cash or stocks and shares ISAs, other investments.

Research comprised interviews and focus groups among financial advisers (IFAs, chartered financial planners and discretionary fund managers), an online survey of IFAs, and an online survey of 500 individual investors.

FOREWORD

EUAN MUNRO

Chief Executive Officer

Investors face an unprecedented level of personal responsibility in planning for their financial future. Ensuring that they have the income to see them all the way through their retirement is one of a number of challenges, particularly in light of the persistently volatile, low growth, low interest rate environment in which we continue to find ourselves.

In addition to balancing risk and return, the variety of investment options can feel overwhelming. The recent pension reforms set out to support personal responsibility and the 'freedoms' have been welcomed but, as our research confirms, the task of saving enough to last a lifetime is no less challenging.

Our role along with the role of independent financial advisers and wealth managers in guiding investors towards the right outcomes has never been more important.

This research reveals how difficult the job of 'doing right' by clients has become and highlights the challenges faced by financial intermediaries. It also demonstrates how passionate this community of individuals is and how dedicated they are to helping their clients achieve the right outcomes.

It provides valuable insights into investors' income needs, the way in which advisers are responding to them, and the importance of looking beyond the traditional asset mix.

Today's investors need solutions that will help them achieve a sustainable income whatever the markets are doing. This research reveals that both intermediaries and investors believe that an income of 4% is both realistic and sustainable and that promises of higher income, especially in the environment we find ourselves in today, are unrealistic.

As a highly experienced, collaborative, global investment team and trusted brand, Aviva Investors is exceptionally well placed to provide support. We are committed to working with advisers to help today's investors achieve the specific outcomes they need and want.

KEY FINDINGS

- The ability to offer a sustainable, regular income was reported by individual investors as the single most important requirement from investment providers.
- 84% of advisers consider a yield above 4% unlikely to be sustainable, 60% of individual investors agreed
- 75% of advisers rated multi-strategy funds as an attractive proposition
- 60% of investors are not prepared to accept more risk to achieve their income requirements
- 52% of pre-retired investors are concerned they will not have saved enough to last through retirement
- 43% of advisers reported their clients are leaving their pension pot untouched and are looking to other investments to generate income
- 32% of retired individual investors are concerned about the sustainability of their income

PETER TOOGOOD

Investment Director,
City Financial Investment Company Limited

"This report provides a thorough and robust analysis of the challenges faced by intermediaries and their clients in providing a sustainable income in retirement.

The myriad of issues associated with greater pension flexibility are discussed at length, as are the responses from interested parties.

One of the key messages from the report is the significant benefit of maintaining a diversified portfolio for clients - a sentiment which we wholeheartedly endorse."

RICHARD ROMER-LEE

Managing Director,
Square Mile Investment Consulting and Research Limited

"The provision of income in retirement is one of the biggest challenges and opportunities facing the savings and advice industry.

This report provides a really good and important insight into how investors and their advisers are thinking about this issue. It also offers some interesting ideas on what is likely to happen in the future."

EXECUTIVE SUMMARY

Our research examined attitudes among financial advisers, discretionary wealth managers and individual investors to the investment imperatives facing today's investor, focusing on income. More than 240 intermediaries and 500 individual investors from across the UK were surveyed during June and July, 2015.

THE INTERMEDIARY PERSPECTIVE

INVESTOR TRENDS

– Advisers reported that their clients are increasingly looking for more flexibility (in terms of where to invest their money, and access to it) with 78% of advisers noticing this as a key trend.

– Clients taking lump sums from their pension and deferring taking an annuity is also a trend noticed by 58% of intermediaries.

– 43% of advisers reported that their clients are leaving their pension pot untouched and are looking to other investments to generate income.

– Views were polarised on clients' attitudes to risk and return: 40% agreed their clients' attitudes to risk/return have not changed significantly in recent years (within the context of a low-yield environment) and they accept that income levels may not meet their requirements, while 41% believe that they are challenged to deliver the required income levels for clients who do not want to accept the corresponding level of risk. Just 16% believe that clients are prepared to accept more risk in order to achieve their income requirements.

KEY CHALLENGES FACED BY INTERMEDIARIES

– Over half (59%) believe their role has become more challenging in the post 'freedoms' world. Positively, most of these (40% overall) believe it is also more rewarding.

– On advising income solutions to clients, respondents reported the key challenges as: managing client expectations of income levels (66%); compliance administration (60%); and dealing with regulation (48%).

– Advisers reported on the need to 'future-proof' their own advice from the potential risk of mis-selling allegations. They were prepared to turn away one-off pension withdrawal business in this regard, reporting that it was "not profitable, too time consuming, and too risky."

– For smaller firms, complexity of compliance is cited as the main challenge (cited by 68%). The research highlights the burden this imposes on processes and suggests that it is a factor in policy decisions to avoid certain asset classes and strategies.

– Intermediaries confirmed that there has been a surge in the number of investment options available to investors and that more choice has increased demand for more advice and flexibility as regards where and how investors might invest their money.

The ability to offer a sustainable, regular income was reported by individual investors as the single most important requirement from investment providers.

TRENDS NOTICED FOR HIGH NET WORTH AND MASS AFFLUENT INVESTORS

- Among high net worth investors, respondents reported that they need to meet income requirements already established, but by employing different drawdown and income strategies to maximise the new tax advantages. For high net worth investors, wealth is typically spread across different investment products and asset classes and there is more focus on total return rather than regular income.
- Among mass affluent investors, intermediaries are focused on facilitating outcomes for their clients, which were not previously possible, introducing more flexible drawdown options. In doing so, there is a need to protect future income by: preserving the value of their clients' capital investment; educating clients on the implications of drawdown on future income; managing expectations of future income levels; and delivering sustainable income.
- Cashflow modelling tools are increasingly integral to discussions with clients: for high net worth clients with complex needs they help guide decision-making; at the other end of the spectrum, they may be used to help ensure that investors do not run out of money in retirement. Tools vary in complexity and functionality and respondents suggested that there is scope to improve, simplify and include tax implications into their functionality.

WHAT HELP AND SUPPORT DO ADVISERS WANT?

- 'Lack of helpful tools and support' was a challenge faced by just 18% of IFAs with 'cash flow modelling' and 'income tools' cited as possible ways to help overcome these challenges.
- In short: simple, user-friendly tools to help manage the diversity of options, which should ideally take account of tax structures; platforms which offer multi-asset and multi-strategy solutions; and the opportunity to form relationships with investment providers, to inform their awareness and understanding of products, particularly as today's range of options is so extensive.

THE SEARCH FOR SUSTAINABLE INCOME

- The ability to offer a sustainable, regular income was reported by individual investors as the single most important requirement from investment providers: intermediaries need to achieve this within clients' typically modest risk/return appetites (expressed as an average of 3.7 on a scale of 1-10 among those aged 55 and above). 60% of investors overall were not prepared to accept higher risk to achieve higher income levels in retirement.
- When asked what percentage yield they considered realistic in the current market environment, 84% of advisers and 60% investors (who expressed an opinion) replied that above 4% is not likely to be sustainable.
- Multi-asset and multi-strategy funds were considered as offering the best potential for sustainable income by 51% and 46% of advisers respectively, 49% cited income and growth funds.
- In more volatile markets, multi-asset funds were also considered as providing the best potential for sustainable returns by 41% of respondents, followed by multi-strategy funds (40%) and risk-rated income funds (32%).
- However, it is important to note that not all respondents distinguished between multi-asset and multi-strategy funds. Multi-asset funds were reported as having a major role to play because they offer diversification, the potential to deliver income and growth, and sustainability, usually at a reasonable cost; as one respondent put it: "every portfolio should have one". At the same time, respondents agreed that the multi-asset market is becoming crowded and differentiating factors are difficult for advisers (and their clients) to determine.
- Multi-strategy funds were perceived as new and less familiar, although advisers in our research were sufficiently aware for 75% to rate them as an attractive proposition. Multi-strategy funds, they said, offer the opportunity to introduce "DFM-quality" (discretionary fund manager) elements into smaller portfolios.

THE INVESTOR PERSPECTIVE

- Half of all (pre-retired) respondents (52%) were concerned they would not have saved enough to last through retirement; even when retired, one in three (32%) were still concerned about the sustainability of their income.
- Investors are showing a cautious attitude towards the new pensions freedoms; only one in eight (12%) expected to change their plans; even so, one in four (23%) 55-64 year olds expected to drawdown lump sums from their pension and defer taking an income until later.
- Investors are motivated by the idea of leaving some, or all, of their pension as a legacy: one in three (31%) consider it to be very important. Given this, their key sources of income are likely to be equity-based ISAs (held by 46%): the incidence of other investment products is low and only half have any form of non-investment sources to bolster their retirement income.
- Investors were typically cautious in relation to risk too, with an average 4.2 risk rating (on a scale of 1 to 10). As retirement approaches this reduces to 3.7 and investors become less likely to accept risk in order to achieve the income they need or might want.
- There is a significant lack of knowledge about the asset classes in which they are invested: 44% of respondents did not know.
- Only one in four investors has taken, or plans to take, professional advice about their retirement options; those who did (or plan to) are:
  - more likely to hold individual investments and understand what asset classes they are invested in
  - more aware of, and interested in, multi-strategy products and sustainable income fund propositions
- 71% find the concept of an income fund (generating 4% over base per annum regular monthly income, preserving capital with low volatility) to be attractive.
- Everyone who took part in the survey expressed an appetite for support or information on ‘what, when and how’ to save for retirement; the most frequently mentioned was in relation to the most appropriate type of products to help them achieve what they want to do, and earn, in retirement, cited by 46% of respondents.

500

individual investors surveyed

31%

of investors would like to leave some, or all, of their pension as a legacy

4% is the new **5%**

according to 84% of advisers and 60% of investors

52%

of pre-retired investors are concerned they won’t have saved enough to last through retirement

THE BACKGROUND – A CHALLENGING INCOME ENVIRONMENT

With interest rates remaining at record lows, meeting income needs from traditional sources alone, such as cash and UK government bonds, is unlikely to be viable. The investment community is adapting to ensure that in the pursuit of returns it looks further afield; but how far do advisers and wealth managers accept and understand this need to re-think risk and return? What do individual investors know, and need to know? And what are the implications for advisers, their clients and their business? It was clear from our research that the adviser community face very many responsibilities and are often 'time poor', with limited capacity to tackle some of these issues.

In addition to these fundamental investment challenges, the regulatory landscape continues to be another cause for concern among intermediaries. Still coming to terms with the impact of the Retail Distribution Review, the pension reforms announced in April 2015 have introduced another level of uncertainty among advisers and wealth managers with scepticism from some that the reforms will be modified and another round of changes will be embarked upon before too long. The Government's consultation paper published on 8 July 2015, 'Strengthening the incentive to save: a consultation on pensions tax relief', is a likely pre-cursor to this.

Already under pressure from what they view as persistent regulatory change and increasingly high customer expectations, advisers in our research have experienced an upsurge in the requirement for advice but at the same time need to choose their clients carefully in order to preserve their own business profitability – the pension reforms have brought into focus the polarisation of the adviser marketplace.

We talked to advisers and wealth managers with clients holding investable assets ranging from £50,000 to in excess of £1 million. They shared with us their concerns that those who recognise the importance of paying for advice, but who have a limited sum of money to invest towards their future in retirement, feel potentially overwhelmed by the array of investment options open to them and that, as a result, want access to investment solutions that are easy to understand and from a trusted brand.

The pension 'freedoms' have shone a spotlight on the value of staying invested to, and through, retirement and yet how much money is needed, and how long it needs to last remain questions that are difficult to answer and advise upon. This was evident from our research and has been borne out in wider studies. In a survey[1] conducted by the National Association of Pension Funds (NAPF) 82% of consumers surveyed were positive about pension freedoms but many worried about risks; 63% worried they would run out of money before they die; 47% worried they would be mis-sold unsuitable retirement products; and 44% worried they may make bad financial decisions and lose their money. Almost three quarters (74%) of respondents who expressed a preference on how they intended to access their savings were planning to leave a proportion of their savings invested and draw a regular income.

In another study[2] published by the Pensions Policy Institute (PPI), respondents were reluctant or unable to plan beyond the next few years; had a poor understanding of both their spending needs throughout retirement, and their likely life expectancy (in particular, the probability of living beyond age 85).

"The pension freedoms have shone a spotlight on the value of staying invested yet how much money is needed, and how long it needs to last, are difficult questions to answer and advise on."

[1] Understanding Retirement', NAPF, 1 April 2015

[2] 'Supporting DC members with defaults and choices up to, into, and through retirement: Qualitative research with those approaching retirement', PPI, January 2015

> *"The traditional asset mix simply does not offer the diversification required, nor can it adequately protect against the impact of volatility."*

Advisers in our research were challenged to manage the income expectations of some clients within the post freedoms landscape; as one respondent put it: "I don't think my clients' fundamental attitude to risk is changing, what's changing is their perception of the need to take risk if they don't want to buy an annuity when they retire. They are becoming more open to the fact that to maintain flexibility, they need to be more open to more risk, and open to staying invested for a longer period of time."

For those with a higher net worth, attitudes to risk and return are not necessarily any different from the less affluent – they do not need or want to take more risk because they have more money – but there is more choice available to them, and they have a wider range of investments they can draw from to meet their income needs. Investment advisers to this client segment are focused on optimising wealth, making the most of the tax structures available: "The reforms have made financial planning more flexible and offer attractive opportunities for investors and affluent consumers in particular, with the only drawback being the restriction on the lifetime allowance for higher rate taxpayers."

Given the macroeconomic environment, the fact that investors can no longer rely on traditional models, such as UK equities for long-term capital growth, and bonds for income, we asked advisers about the way in which they were advising their clients: what were their sources of income in terms of asset classes, investment products, strategies and geographies? What were their investment priorities? They were in agreement that the traditional asset mix simply does not offer the diversification required, nor can it adequately protect against the impact of volatility. As one respondent told us: "Diversification is still the key…incorporating a broad portfolio of equities, fixed income, property and good geographical diversification as well."

Advisers understood the impact of correlation in this context and the importance of sourcing solutions, such as multi-strategy funds, which combine assets that do not all move in the same direction, to the same degree, at the same time. Still cautious to some extent about the risks surrounding some so called 'alternatives' they also recognised that these asset classes are fast becoming mainstream, and they are advising on a wider than ever range of funds and strategies in their aim to deliver the right outcomes for their clients.

METHOD

This report is based on research carried out by Gabriel Research & Management Ltd. comprising depth interviews and focus groups (in London, Guildford and Bristol) among 34 financial advisers (IFAs, chartered financial planners, discretionary wealth managers and discretionary fund managers), an online survey of a further 200 IFAs, and an online survey of 500 individual investors (all with any of: pensions, cash or stocks and shares ISAs, other investments).

The adviser research groups took place on the 10, 11 and 12 June; the interviews were conducted between 15 June and 17 July and the online survey between 2 – 8 July. The online survey of individual investors took place 13 – 15 July.

INDIVIDUAL INVESTOR RESPONDENTS

Gender	
Men	53%
Women	47%
Age	
Under 35	10%
35-44	17%
45-54	21%
55-64	28%
65-74	21%
75+	3%
Working Status	
Pre-retired	65%
Semi-retired	6%
Fully retired	29%

RESEARCH FINDINGS
ADVISERS AND INCOME: HOW, WHY AND WHERE NEXT?

Just over half (54%) of the IFA firms surveyed belong to networks or use outsourced expertise for fund selection. The more wealth management orientated firms with in-house investment specialists (40%), typically design model portfolios and offer bespoke solutions.

MODEL PORTFOLIOS

Model portfolios, sourced either from third party providers or constructed in-house, play an important role in the way that advisers meet the needs of their clients. They offer what they consider to be tried and tested solutions: low-risk, simple and efficient – for them and their clients.

"We use the model fund portfolios; the same for ethical funds and passives… standard stuff but it makes a good return for our clients; it reduces the risk, everything is rebalanced every quarter and it is really simple."

As a 'time poor' group, typically under pressure from the burden of a heavy workload, model portfolios fulfil what was reported as an important need: saving time.

"To go 'off panel' is time-consuming and if I am paying thirty people to assess new and existing products to make sure they are suitable for my clients I don't see why I should spend more time looking at other options; so I rely on their recommended products."

"The research team actually put together suggested portfolios in the newsletter so if clients wanted an income portfolio, for example, whether it is low, medium or high risk, then the information is all there – we tend to work around that."

Those who adopt a more bespoke approach, typically outsource investment decision-making to discretionary fund managers (DFMs).

THE ROLE OF DFMS AND BESPOKE SOLUTIONS

The DFM plays a central role; for the majority of HNW (typically £150k+) clients, investment decisions are effectively outsourced to them.

"We are one of these integrated companies now. We have our own discretionary fund management arm that does all the investment research and an advisory team who then take that research and either use the DFM as a solution for our client or the research they use in funds and then put that into practice with client portfolios."

"We have a range of DFMs that we use who are selected, filtered and reviewed on a regular basis, but we work with two core DFMs to provide model portfolio services. Then we have an array of multi-asset funds, to make sure that we've got a broad enough coverage both in terms of asset allocation and therefore risk profile and also that, as best we can, we have something for everybody, but also a range of different approaches."

"We used to have investment specialists but in the main we outsource everything to discretionary fund management. I used to like building peoples' portfolios with the research that went with it but we are IFAs, not fund managers."

"We use DFMs over £250,000 typically; that might be a mix of collectives and direct equities, or sometimes just direct equities depending on a client's risk profile. Below that we use platforms. We all get together quarterly as a group of investment advisors to hone down the funds using a risk profiler. We will match a portfolio to that risk profile and then we would get together and take a view on it. For instance, the profiler spits out a medium risk, which comprises a big chunk of gilts in their asset allocation, and that is not where one wants to be at the moment."

CASHFLOW MODELLING: THE EVOLVING TOOL OF THE TRADE

Cashflow modelling is becoming the adviser's basic tool of the trade, offering varying degrees of sophistication ranging from bespoke software programmes to spreadsheets and standardised processes from networks.

"I don't [use one yet] but I will as better solutions options become available. A lot of them are third party investment led but they're not very practical."

"The one I use is incredibly complex but a very, very good tool; but there are some simpler ones out there that do a perfectly good job. I just wish every client could actually have an IFA with cash flow forecasting software to make sure they don't run out of money."

"Everything really should evolve around lifelong cash flow forecasting."

Cash flow forecasting tools were used to help ensure that clients "don't run out of money" and to help meet the goals or outcomes their clients wanted to achieve. But not by all respondents, and there were perceived limitations.

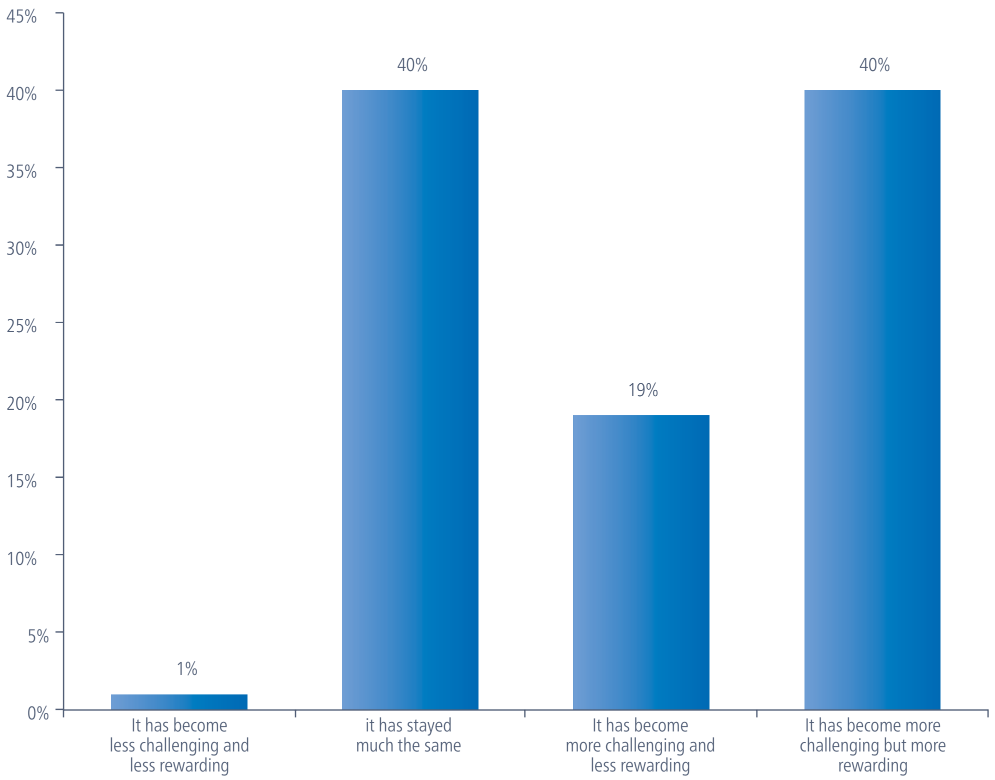
"I don't use cash flow modelling and we don't as a firm. I see no need to. I always say to people, 'Think net money, don't think 'I need £100,000 or £200,000 a year, think net money. What do I need net a month?' I work from there."

"The downside of freedoms is more choice, therefore more complexity"

THE POST FREEDOMS WORLD – CHALLENGING BUT ULTIMATELY REWARDING

In the post freedoms world, tasked with helping clients achieve sustainable income (so that they don't run out of money) life has not become easier for advisers: they perceive their roles in the new landscape to be more challenging than before, but positively, more rewarding.

Q: Which, if any, of the following are you noticing as trends among your client base?



For a large proportion of respondents the pension freedoms mean 'business as usual'; there were no significant changes to the advice they provide, especially at the HNW end of the market. Advisers recognise their role is becoming more focused on achieving flexible, tax-efficient solutions and employing assets in a different way.

"We are coming across clients who don't need income from their SIPP and now with inheritance tax can get potentially better tax treatment, and say, 'I might actually keep the SIPP for capital growth once I've retired and take the income from my ISAs and main account and use that as a more cost effective route'. So, there is a lot changing in terms of the outcome element of it."

"Now we know a pension is like a giant ISA. It is complete flexible access, if you understand both the living and death benefits and the fact that you can regrow the tax free cash sum, there is a bunch of things for the right people that, with careful understanding, can make them really sing and dance. There is going to be a lot more post-retirement pension funding."

"In terms of pensions freedoms we have seen an increase in enquiries. I wouldn't necessarily say our output of advice has changed. The media has brought attention to some of the flexibilities, which perhaps were already there: for instance a lot of clients are saying, 'I believe I don't need to buy an annuity anymore?' but in reality they didn't have to previously."

"If they get to their mid-fifties they've still got potentially thirty/forty years of retirement so they can be retired as long as they are working. So attitude to risk and goal setting is becoming more important to these clients because of the freedoms they've got rather than products. We are matching solutions to what they want to do rather than say 'you need this product'."

NOT ALL BUSINESS IS GOOD BUSINESS

Firms cannot afford to take on ad-hoc pension withdrawals and 'free' advice citing the time and cost to their business, and the risk of mis-selling allegations.

"We decided that for the people who ring up and say, 'We want to take our money out, can you help us do it?' We say, 'Unless you take advice from us and maybe you might have to pay something for it, we aren't just going to facilitate you because you and I both know in five years' time it will be another PPI thing and it is going to be blamed on everyone in the industry apart from the client who may have made the wrong decision."

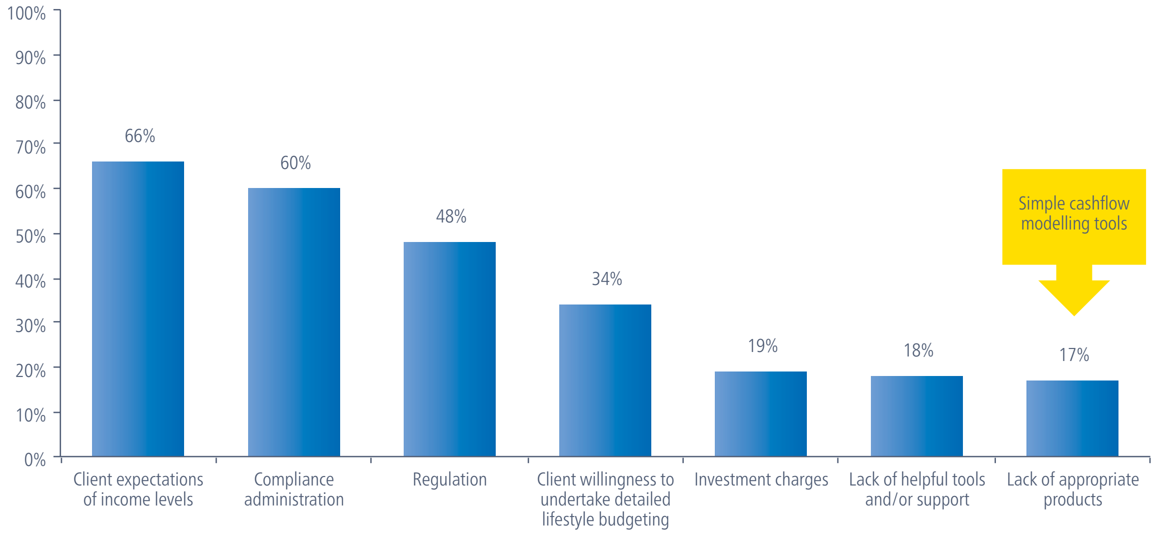
"Everything is like a double-edged sword. On the one hand, people still need advisers and the constantly changing legislation is one of our raison d'etres. On the other hand it is a bit of a nightmare trying to get your head round it, thinking if I get this wrong how is that going to impact?"

"The procedures created have probably taken us a week in man hours and we will in all likelihood throw most cases away because not everyone has got sufficient assets to justify doing this."

CONSTRAINTS: MANAGING CLIENT EXPECTATIONS; ADMIN, ADMIN, ADMIN...

We asked advisers: 'Which, if any, of the following constraints and challenges do you face when advising income solutions to clients?' **Managing client expectations of income levels was cited by 66%,** followed closely by compliance administration (60%) and dealing with regulation (48%). For smaller firms, compliance administration is more of an issue.

Q: Which, if any, of the following constraints and challenges do you face when advising income solutions to clients?



Managing client expectations is the main challenge overall, but for smaller firms, compliance administration was seen as more of an issue.

Respondents expressed real concerns about future-proofing advice and erred on the side of caution in order to stay compliant and keep their business 'safe' from the potential risk of mis-selling allegations.

"In the past regime there was less choice so it was easier to define what was 'best advice' and therefore make your recommendation and hang your hat on it. Now there is so much choice and so many options; my concern is that you do what you think is best for the client and make a recommendation but ultimately there is always scope for someone else to come along later on and say, 'Well that was all wrong' or it has unfolded in a way they weren't fully expecting."

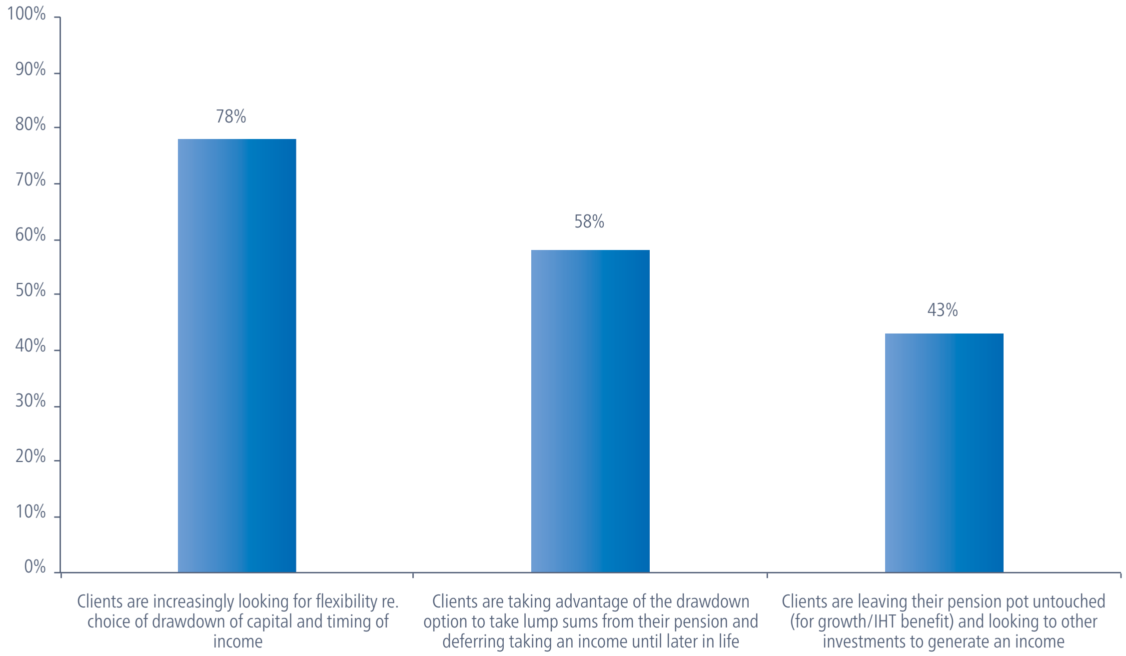
CLIENTS SEEK GREATER FLEXIBILITY

Advisers reported that their **clients are increasingly looking for more flexibility** (in terms of where to invest their money, and access to it) with **78% of advisers noticing this as a key trend**. Clients taking lump sums from their pension and deferring taking an annuity is also a trend noticed by 58% of advisers.

43% of advisers reported that their clients are leaving their pension pot untouched and are looking to other investments to generate income. The freedoms have brought more choice and with that, a greater need for guidance and advice.

While the pension reforms enable investors to provide a legacy from their remaining pension pot some pensions taken out many years ago were designed with a very different retirement journey in mind. Advisers were aware that the regulatory change concerning the transfer of existing pensions to ones that are fully flexible is still unfolding and that dealing with this kind of work is necessary but not especially rewarding.

Q: Which, if any, of the following are you noticing as trends among your client base?



"With the new death benefit rules and the intergenerational stance of the pension scheme, clients can use other assets for income first and try and keep the pension, not as a tax planning tool, but a pot they pass on."

"People will try and retain as much in their pension pot because it makes financial sense."

"I can't think of anybody who has taken a lot out just because the rules have changed. The only people that have accessed any were the ones that were going to access it anyway; they are retiring and they need some cash."

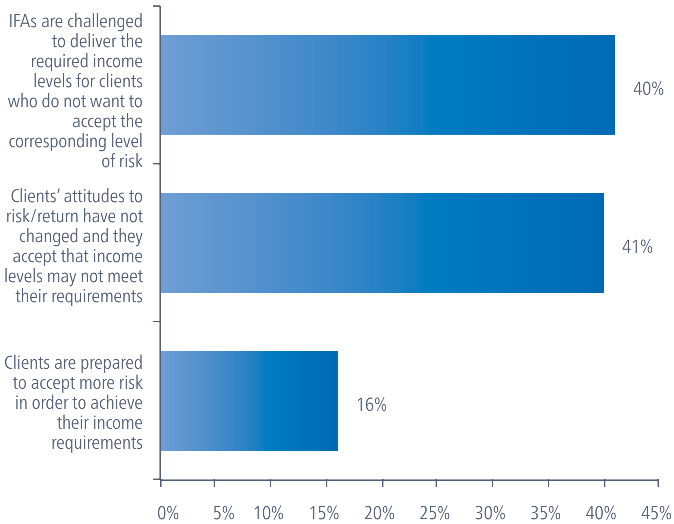
"We've been doing flexible drawdown for clients since it first came out and what we've got now is really just an extension of that to some extent. The flexibility is useful, it means when we're doing cash flow planning and different things are coming out at different times we can mould their pension pot around it. It means we can play with tax a lot better for them."

CLIENT ATTITUDES TO RISK

One of the main challenges for advisers is to demonstrate the relationship between risk and return on income levels. Views were polarised on their clients' attitudes to risk, which was probably reflective of the wide range of client types they advise. 40% agreed their clients' attitudes to risk/return have not changed significantly in recent years (that is within the context of a low-yield environment) and they accept that income levels may not meet their requirements, while 41% believe that they are challenged to deliver the required income levels for clients who do not want to accept the corresponding level of risk. Just 16% of advisers believe that clients are prepared to accept more risk in order to achieve their income requirements.

"What's changing is clients' perception of the need to take risk…they need to be open to taking more risk and staying invested for a longer period of time"

Q: In today's persistently low interest rate environment and accepting that every case is different in terms of wealth levels and risk appetite, which of the following statements do you most agree with?



"Probably all my clients understand that risk and reward are linked together but it is the effect of the risk on what they're doing that is more important, and the risk they are able to take. In some cases [their pension savings] are all they have and in other cases, for people with lots of spare capital, it doesn't really matter too much if it dips in the short term. But it is certainly a big part of what we do."

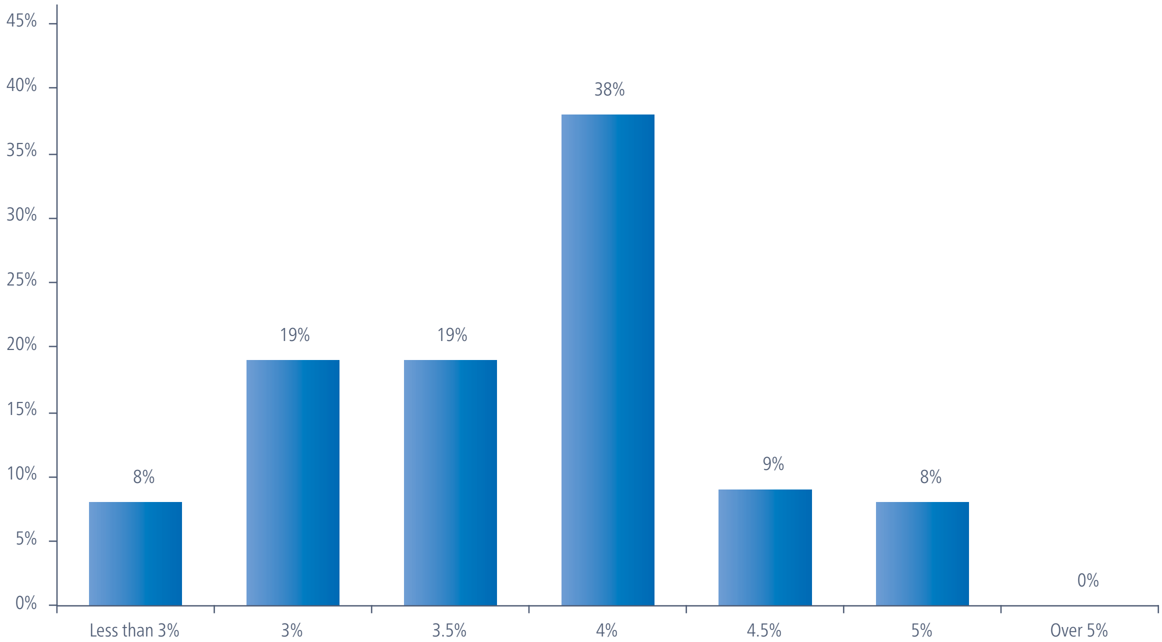
84% of advisers (and 60% of investors who expressed an opinion) replied that above 4% is not likely to be sustainable.

INVESTORS SEE 4% AS THE MOST REALISTIC YIELD

Before the 2008-2009 global financial crisis, achieving a 5% return from deposits was commonplace. In the current low growth, low interest rate environment, advisers – and according to our research – most of their clients, recognise that this is not a level of return that can be achieved without jeopardising capital, and is unlikely to be sustainable.

When asked what percentage yield they considered realistic in the current market environment, 84% of advisers (and 60% of investors who expressed an opinion) replied that above 4% is not likely to be sustainable. Understandably, acceptable yield is highly influenced by size of investment.

Q: In the current market environment, in your opinion, what percentage income yield is a realistic expectation for regular income?



"If you've got a client who is fairly or very cautious they shouldn't really be investing to start with because they won't get the returns to make it work. If you've got a middle risk client that should work – I would say 3.5% to maybe 4%."

"I would err on the side of caution. I would certainly not go above 3.5%. Anything above 3.5% is beginning to get a little but punchy in my view, as we sit at this moment in markets."

"For clients now in post drawdown phase, we are producing an income yield of around 4% for them. Because the market has been relatively kind, the pot is still growing as well. I am a great believer in yields, liability matching. So if a client is taking a 4% income from a pension I try and produce a 4% dividend in interest return for them and hope the pot grows with that."

"With new funds, in the region of 3.75 to 4% is probably more realistic for a brand new portfolio."

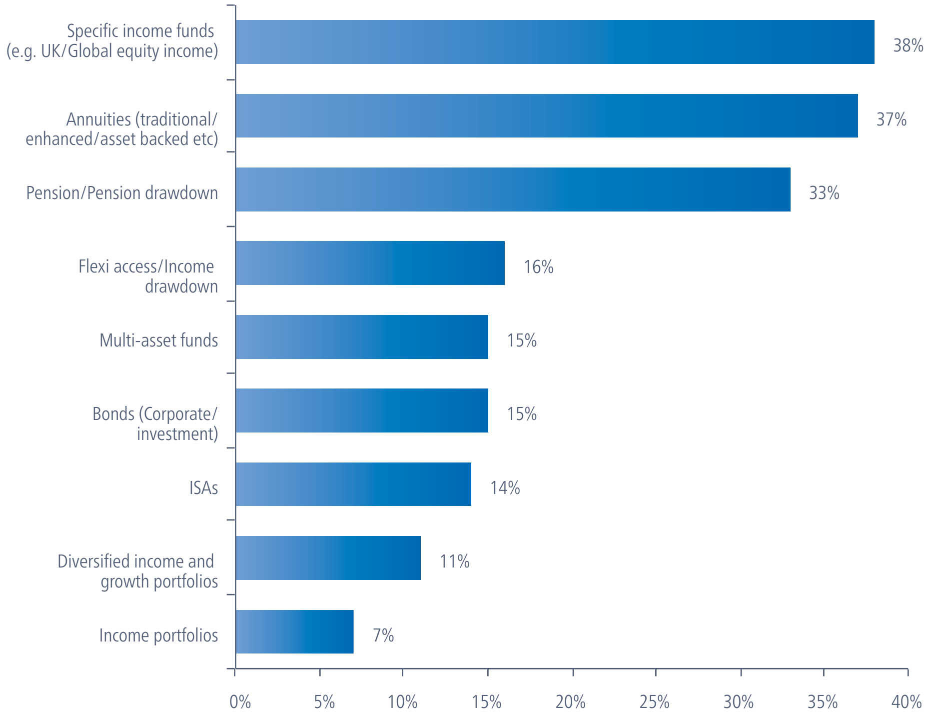
"A lot of our clients have got more assets than most, say, a million pounds and they are only looking to yield maybe a £30,000 a year income. In yield we are talking about 3%. In that respect, you don't need to take risk, you don't need emerging markets or this, that and the other."

SOLUTIONS FOR TODAY'S INVESTOR

Recognising that today's investors need solutions which can: sustain a potentially much longer lifetime, weather inflation and market volatility, potentially support healthcare needs and/or enable investors to leave a legacy, we asked what top three income solutions advisers would recommend. Overall, advisers recommend a blended approach.

Q. What top three income solutions would you recommend to investors, recognising that today's investors need solutions which can:

– sustain a potentially much longer lifetime
– weather inflation
– weather market volatility
– support healthcare needs or enable investors to leave a legacy



Advisers confirmed that income solutions are driven by client fundamentals: the amount they have to invest, their risk profile, including capacity for loss, plus needs and 'wants'.

"I think you have got to have a blend of income funds… because each fund manager will have a different view and that is what you need in most economic environments. Diversification is key even within an asset class."

"For smaller pots, we are very cautious…"

"We are very cautious to make sure that our clients always stay within risk parameters and capacity for loss parameters. We tend to use a multi-asset, multi-strategy fund range."

"I almost always use the natural yield, relying on that for income…creating enough growth from the capital that may be income."

"What I say to the client is if we can keep your yield to 3.5%, then some capital growth will help make it up to more than that overall."

DIVERSIFICATION OF INVESTMENTS ACROSS ASSET CLASSES AND GEOGRAPHIES

Respondents talked about the importance of diversification as crucial to achieving the right outcomes for their clients and recognised that a well-diversified portfolio was much more likely to be able to deliver sustainable income. Among some, there was a reluctance to venture too far into the use of alternatives, although they acknowledged that many so called 'alternatives' are fast becoming mainstream.

"Diversification is still the key thing, not simply targeting fixed income areas which have traditionally been very good, but incorporating a nice broad portfolio of equities, fixed income, property; again we are talking a good geographical diversification as well. What we tend to do when we are using collectives is stick with the same geographical and asset diversification as we would for a growth portfolio but pick up an income producing unit trust instead of an accumulation, but still keeping the core with that sort of diversification. Within the model portfolios that we run we do tend to stick to the main asset classes, overseas, UK equities, fixed income, property, rather than go into alternatives."

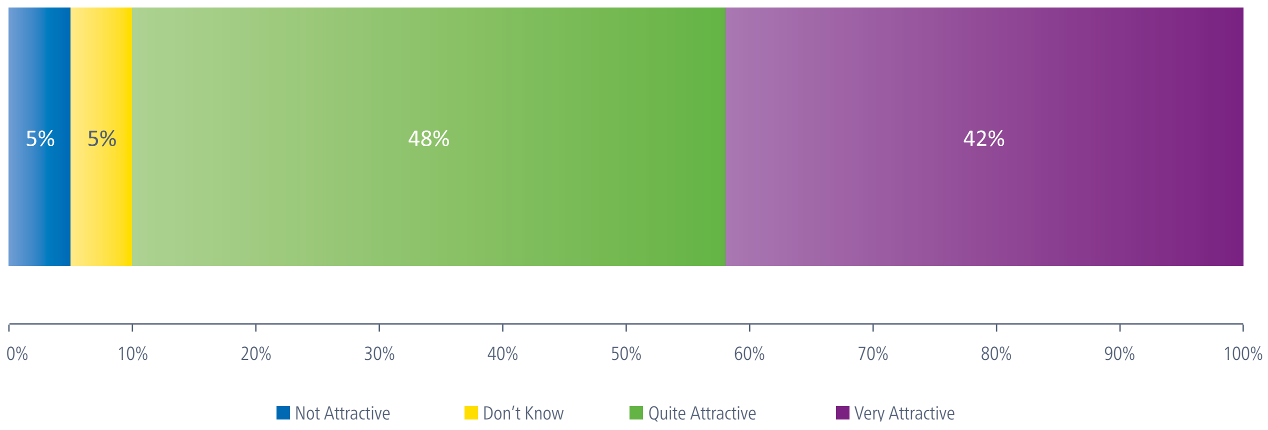
Equity income funds were talked about as being traditional stalwarts for those looking for income, growth or a combination of the two but in today's economic environment, deemed less reliable. Advisers expressed an appetite for alternative solutions.

"In an income and growth portfolio we are going to have commercial property, some fixed interest, some alternative investment strategies so, absolute return. The core of the portfolio from the equity side will be equity income but not only UK, global equity income as well. Then we will have some global markets around that too. Then, depending on how our investment team do, we will match the equity exposure to the risk profile and match the UK and global equity exposure within that to the risk profile as well."

"The idea is to have a diverse range of assets that won't all conspire to correlate downwards at the same time"

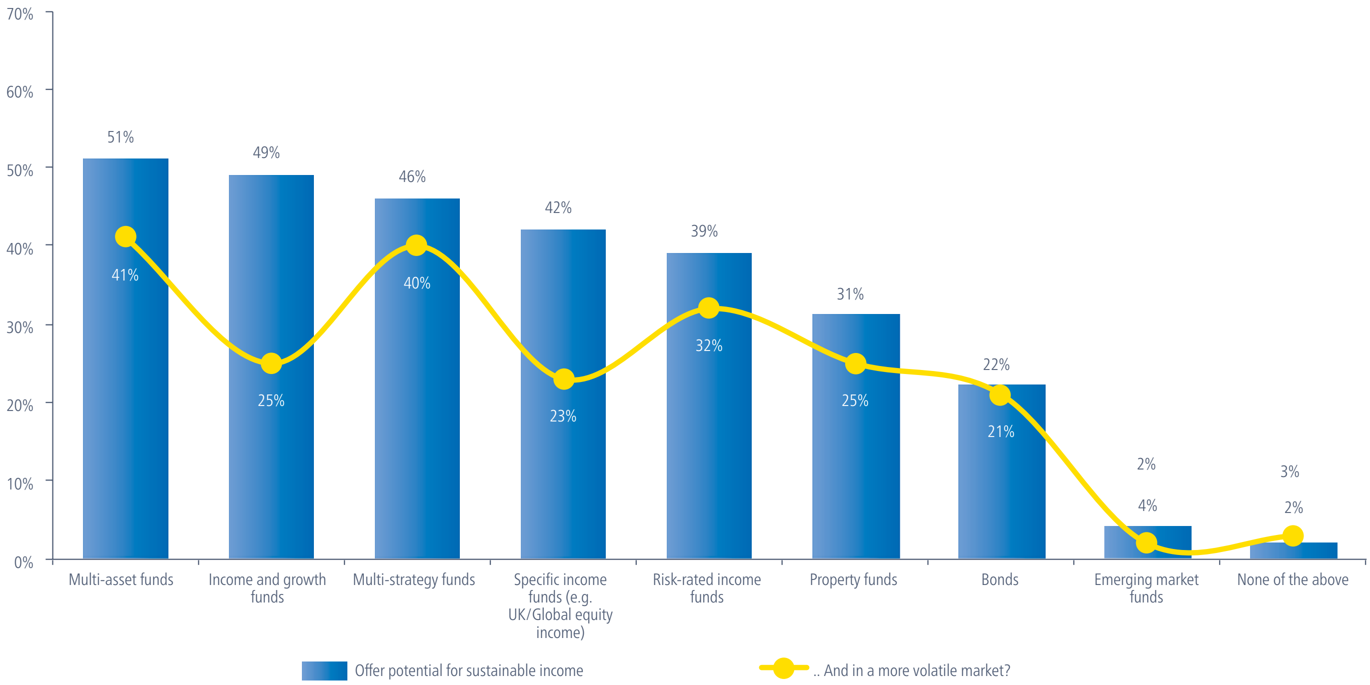
THE SEARCH FOR SUSTAINABLE INCOME

Q: Some would say there aren't enough natural yield products on the market, or enough alternatives to equity income funds. How attractive would you consider an alternative to an equity income fund, which aims to provide regular monthly income, sufficient growth to preserve capital, and is less than half as volatile as global equities over any three-year period?



Clearly from the above response, the overwhelming majority of investors would welcome a fund that delivered a regular monthly income, offered sufficient growth to preserve capital and proved less than half as volatile as equities.

Q: Looking ahead, which of the following offer the best potential for sustainable income? And in a more volatile market?



MULTI-ASSET FUNDS: THE CORNERSTONE OF ANY INVESTMENT SOLUTION

The benefits of using multi-asset funds are recognised widely and seen to have a significant place in most solutions. Advisers gave a number of reasons why they were of appeal; they offer: diversification, an element of smoothing, access to asset classes not otherwise possible, a 'one-stop' solution for mid-range (£50k up to DFM threshold) investors. They also believed them to be the current trend and generally reliable. However, there is perceived to be a plethora of multi-asset products, and the distinguishing features are not easy to identify.

"Our view as a business, is that multi-asset is a cornerstone 'must have' of any investment solution used today. We only use multi-asset solutions."

"I would say of the clients who we don't advise to go to a DFM then probably about 60% of their portfolio will be multi-asset funds."

"For most people, they're the most appropriate way of delivering an income and a bit of capital stability; if a client decides later on that they want to go into an annuity they can."

"Remembering our clients are average investors, middle risk, seeking income, I would probably use a fund-of-funds as the core holding, then a couple of multi-asset funds around that which are trying to do different things in a lower costing format, and then more specialist bonds, commercial property, emerging market equity income funds, what I call satellite funds around the outside, to drive performance and maybe increase the income level. The bigger performance of the portfolio the more of those satellite funds you can incorporate to drive the performance."

"If they are not looking for anything over-complicated, we would use quite a lot of multi-assets…"

"We've got three strategies. For the clients who are building up or starting out with investments or pensions we would typically pick up a single multi-asset fund. For clients who have already got some capital behind them and are either looking for capital growth or income, we can then use the risk-rated multi-asset portfolios. Then clients above about £150,000 we would probably look for something outsourced to discretionary fund management."

"If clients come in with £60-80,000 then we would say, 'use a multi-asset fund for all of it'."

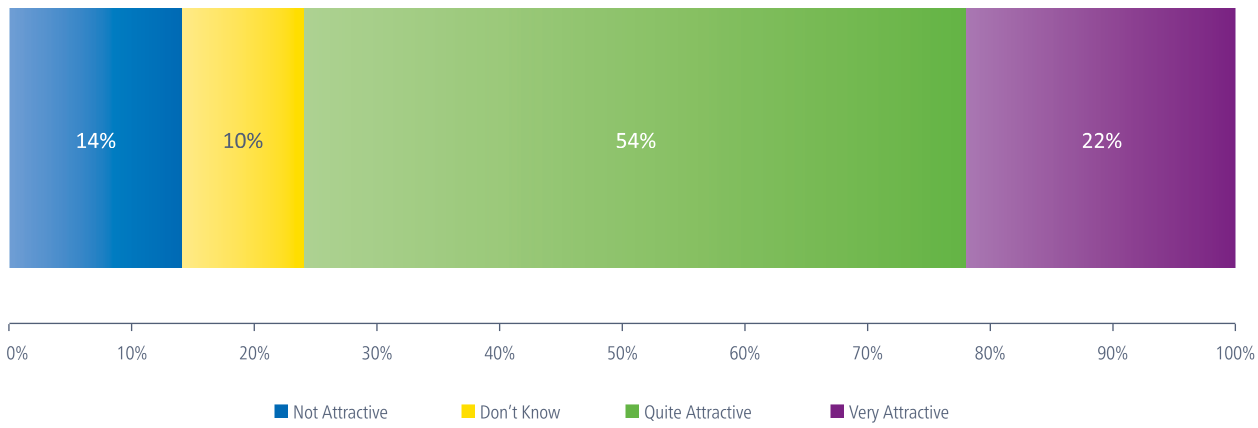
MULTI-ASSET OR MULTI-STRATEGY?

Advisers did not always distinguish between multi-asset and multi-strategy funds and unless prompted to distinguish between the two, typically used 'multi-asset' as a catch-all descriptor.

However, they certainly understood that a multi-strategy fund offers a more sophisticated approach than a multi-asset fund, combining a wide range of strategies to diversify risk and help the fund achieve its targets in many different market conditions. In the current economic climate, this was understandably perceived as "very attractive".

"We believe that multi-asset investing is a key part of any solution, and provides flexibility in managing tough market conditions"

Q: A multi-strategy fund offers a more sophisticated approach than a multi-asset fund, combining a wide range of strategies to diversify risk and help the fund achieve its targets in many different market conditions. How attractive do you consider multi-strategy income funds within the context of today's market conditions and client expectations?



PROTECTING AGAINST VOLATILITY

Advisers recognised that the traditional asset mix cannot adequately protect against the impact of volatility.

"I am not sure that there is any way of effectively doing this with a traditional asset mix. I would attempt to obviate it to a large extent by constructing a broadly diversified portfolio with low correlation, but that said, frequently lack of correlation falls away under strained market conditions. I prefer to engage with clients on the basis that their drawdown portfolio is recognised as being their primary source of income but that they have sufficient liquidity in terms of cash on deposit or near cash investments (usually in the form of Cash ISAs or similar) to provide income for up to three years in the event of market downturns to guard against the effect of negative pound cost averaging."

"With most very wealthy clients I would avoid the need for monthly income payments and manage the portfolio for growth and then strip out any achieved growth on an ad hoc basis. Where monthly income is a necessity then some form of mixed asset fund that is smoothed in some way to reduce volatility is probably the answer."

THE FUTURE OF INCOME: ANNUITIES AND BEYOND

There was a broad-based acknowledgement among respondents that some form of (deferred) annuity has a role to play in the future: this area is seen as potentially ripe for innovative products to emerge.

"We want to sit tight for this year. There is going to be so much innovation from the likes of Just Retirement and other companies who've been hit. It is a question of waiting to see what is going to be coming in. That is the big market. There will be so many new products."

PLATFORMS: ACCESS TO A RANGE OF PRODUCTS TO BUILD SUSTAINABLE INCOME SOLUTIONS WILL BE THE CHALLENGE FOR PROVIDERS

Building sustainable income solutions is the key challenge. The quality of platforms is a key differentiator: respondents were keenly aware that poor functionality and performance will negatively impact on business and that 'good' platforms will have a positive impact.

The challenge for platforms, according to our research, is the delivery of functionality that will aid the construction of sustainable income solutions, and which can offer functionality that simply and efficiently accommodates updates to the prevailing tax regime. Advisers also expressed a clear desire for personal relationships with people who *"understand what is going on…a human being to talk to."*

"…to be able to access on the platform all the range of different products to try and build up this sustainable income from different sources, this will be the challenge to the providers going forward."

"Functionality, the things that we need to do, we want to do efficiently and easily on behalf of the clients. Also service in terms of people at the sharp end; being able to talk to people that understand what is going on and the nuts and the bolts so if we have problems, and invariably they will occur, we have got a human being to talk to."

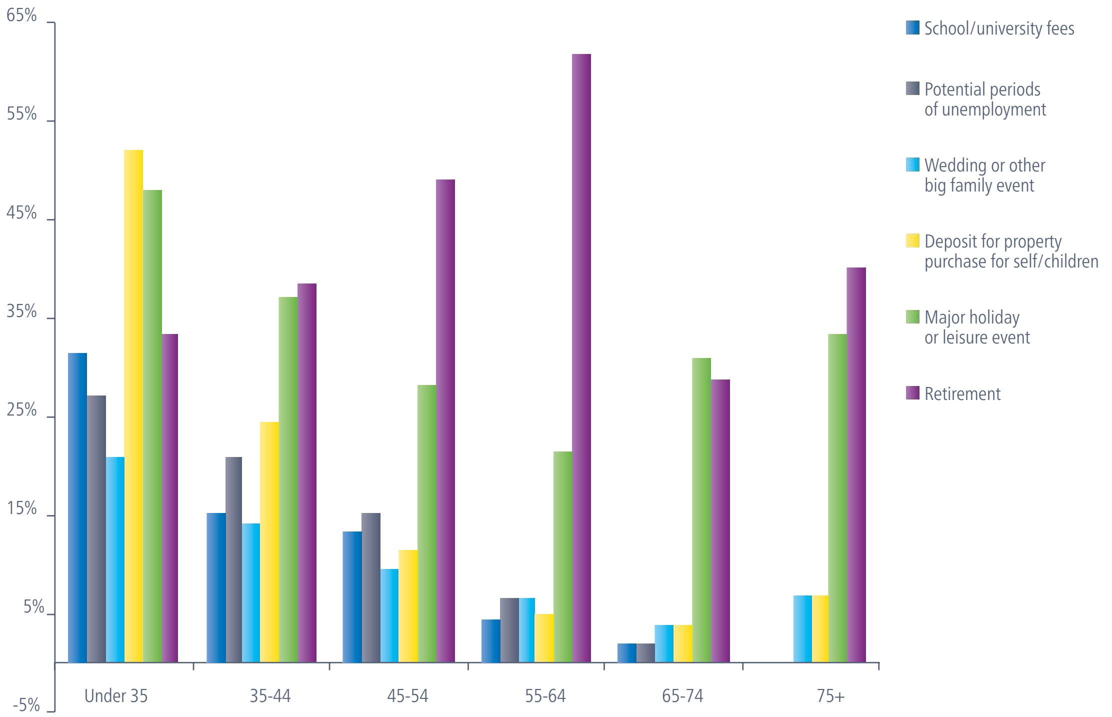
"Administration and support that the provider can offer our client; in other words functionality. Some of our clients like to have access on a daily basis to see how their investments are doing."

RESEARCH FINDINGS
THE VIEW OF THE INDIVIDUAL INVESTOR

To gain an up-to-date picture of how individual investors are planning for their financial future, their reaction to some of the pension reforms and views on income solutions, we invited 500 investors to take part in an online survey. All of them held cash or stocks and shares ISAs, or other investments, and/or contributed to a pension scheme. The survey was completed between 13 – 15 July 2015.

SAVING PRIORITIES ARE DRIVEN BY LIFE STAGE

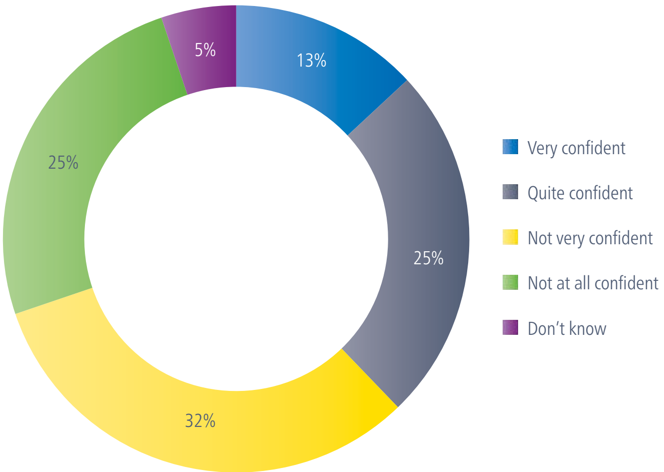
Q: Which, if any, of these events are you saving/ investing for?



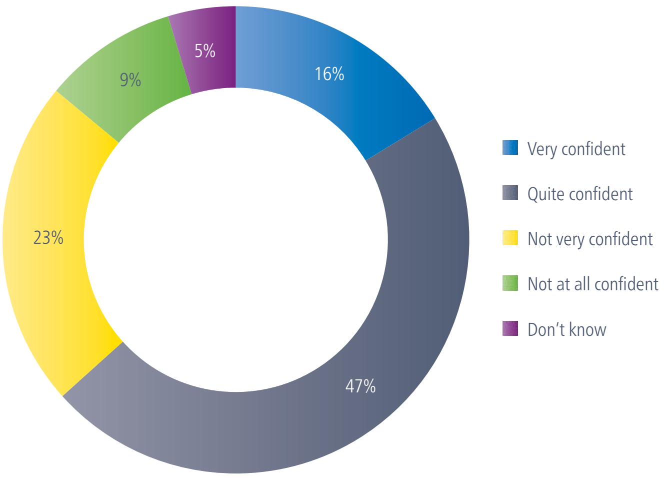
The commitment bulge is very evident among under 35 year-olds. Understandably, there is a strong, almost singular, focus on retirement planning among those aged 55-64.

HALF OF ALL INVESTORS APPROACH RETIREMENT UNCERTAIN THEY WILL HAVE SAVED ENOUGH… ONE IN THREE ARE STILL UNCERTAIN EVEN WHEN THEY HAVE RETIRED

Q. How confident are you that, by the time you have retired, you will have saved enough to last throughout retirement?

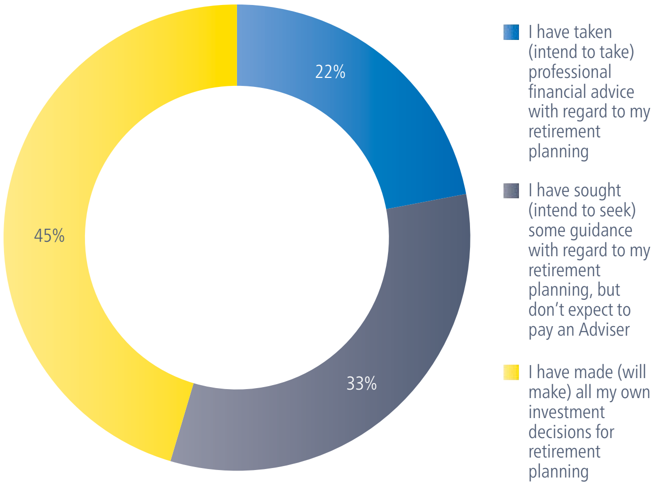


Q. Having retired, how confident are you that your savings and pensions will prove sufficient to last through retirement?



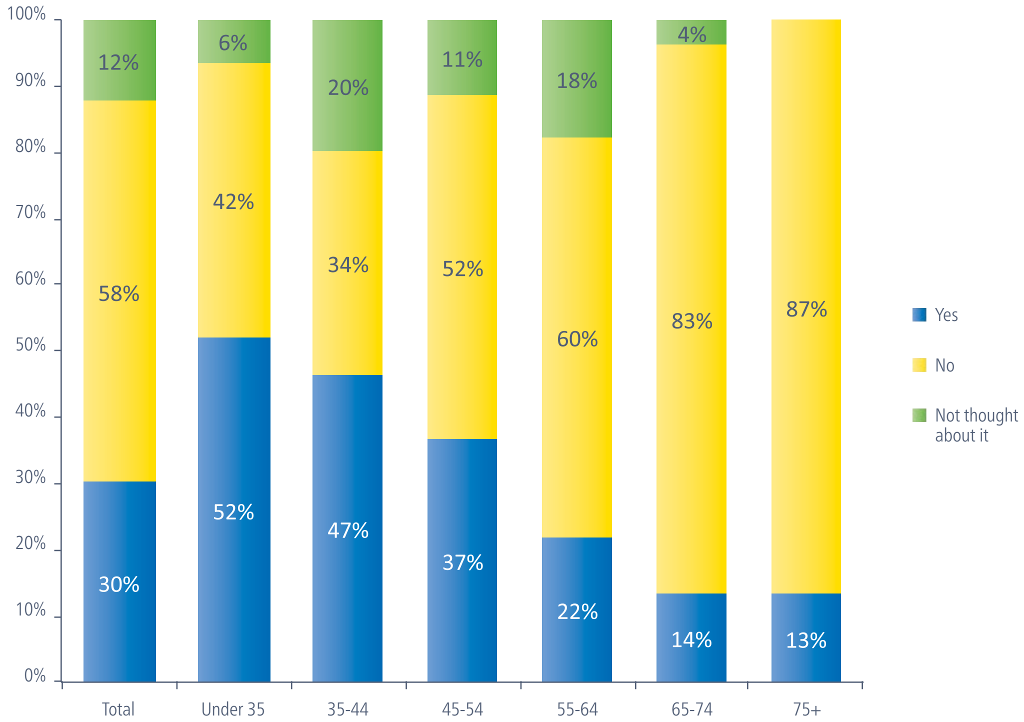
45% HAVE MADE (WILL MAKE) THEIR OWN FINANCIAL DECISIONS

Q. Which of these statements best describes how you make (intend to make) your retirement planning decisions?



THERE IS NO RUSH TO CHANGE INVESTMENT PLANS BECAUSE OF THE NEW PENSION FREEDOMS

Q. Since the introduction of the new 'pensions freedoms' in April this year, have you changed your plans about how to use your investments and/or pension in retirement?



The research shows that despite the pensions reforms, investors are not likely to think of retirement plans until after they reach 45 years old. A minority have changed their plans because of the new freedoms.

YOUNGER INVESTORS WANT TO PRESERVE THEIR PENSION POTS; ONE IN FOUR 55-64 YEAR OLDS WILL TAKE A LUMP SUM FROM THEIRS

Q. Which of the following statements most closely describes where you expect to get your retirement income from?

FOR THOSE NOT EXPECTING TO BUY AN ANNUITY, PRESERVING THEIR PENSION AS A LEGACY IS IMPORTANT

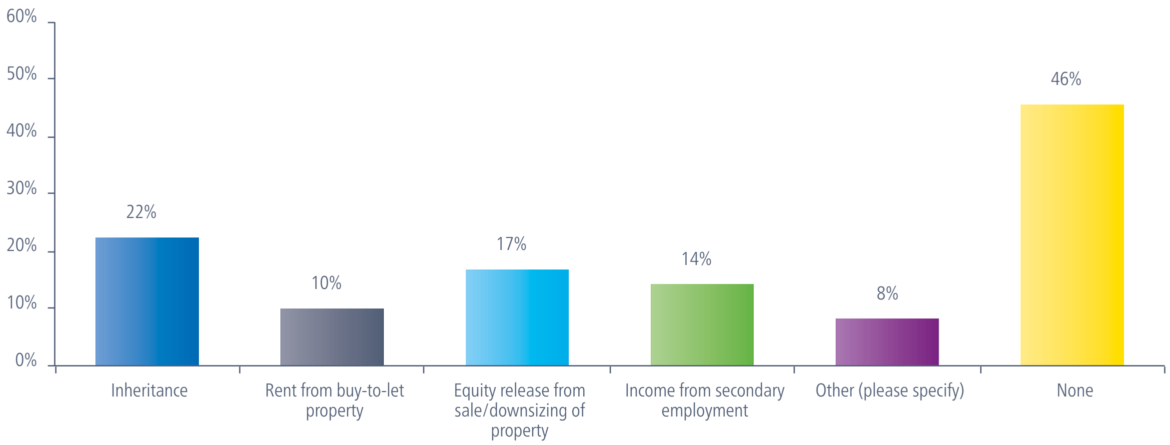
Q. With the removal of inheritance tax on pensions, how important is it to you to be able to pass on some or all of your pension pot when you die?

	Total	Under 35	35-44	45-54	55-64	Over 65
Very important	31%	47%	33%	36%	18%	31%
Quite important	33%	30%	47%	25%	31%	32%
Not important	26%	13%	10%	26%	40%	34%
Not thought about it	10%	10%	10%	13%	12%	3%

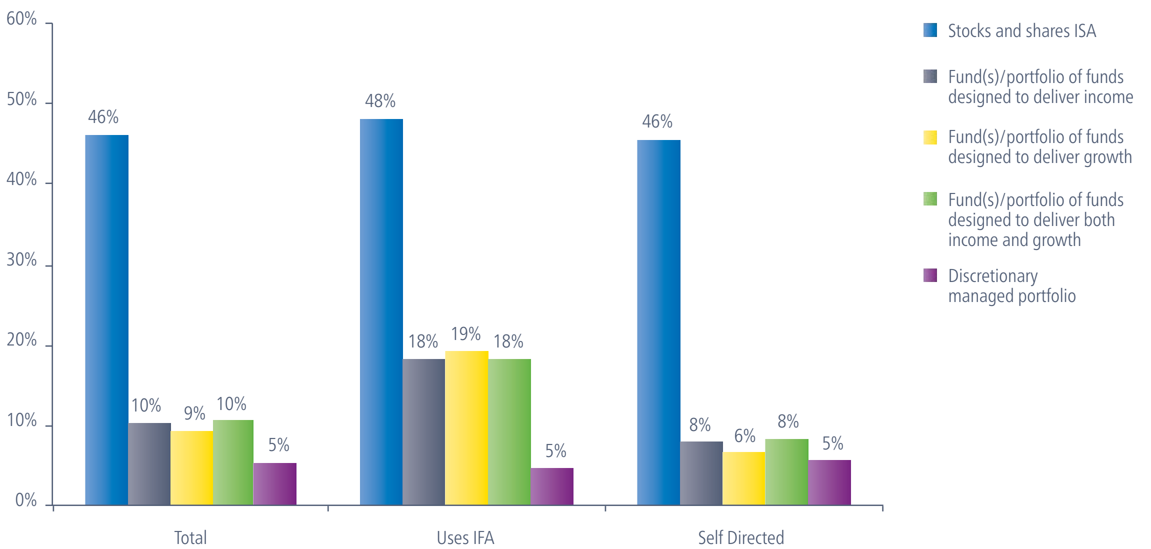
Due to rounding some totals might not add up to exactly 100%

MOST INVESTORS (46%) DO NOT EXPECT TO HAVE ADDITIONAL SOURCES OF INCOME IN RETIREMENT OTHER THAN THEIR PENSION

Q. Apart from your pension, what other sources of income, if any, do you have (expect to have) in your retirement?

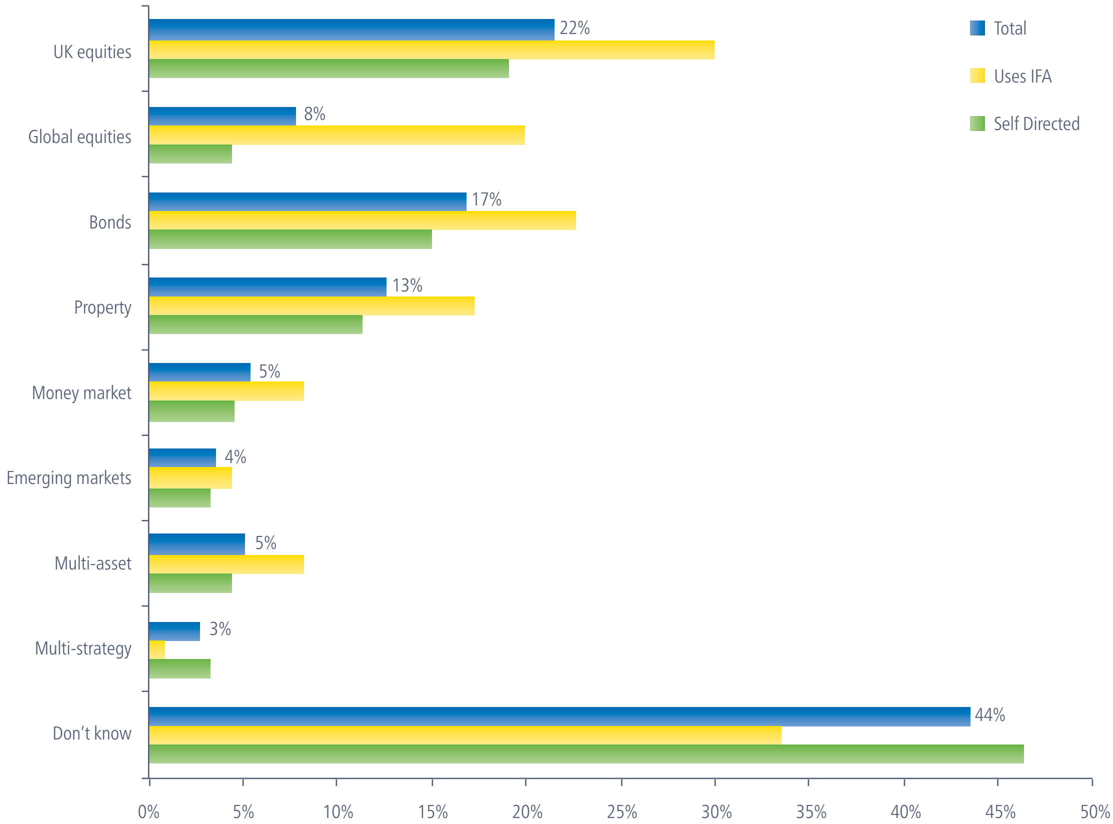


Q. Apart from your pension, which types of investments do you hold?



THERE IS A SIGNIFICANT LACK OF AWARENESS OF THE ASSET CLASSES IN WHICH INVESTORS ARE INVESTED

Q. Which, if any, of these asset classes are your funds invested in?

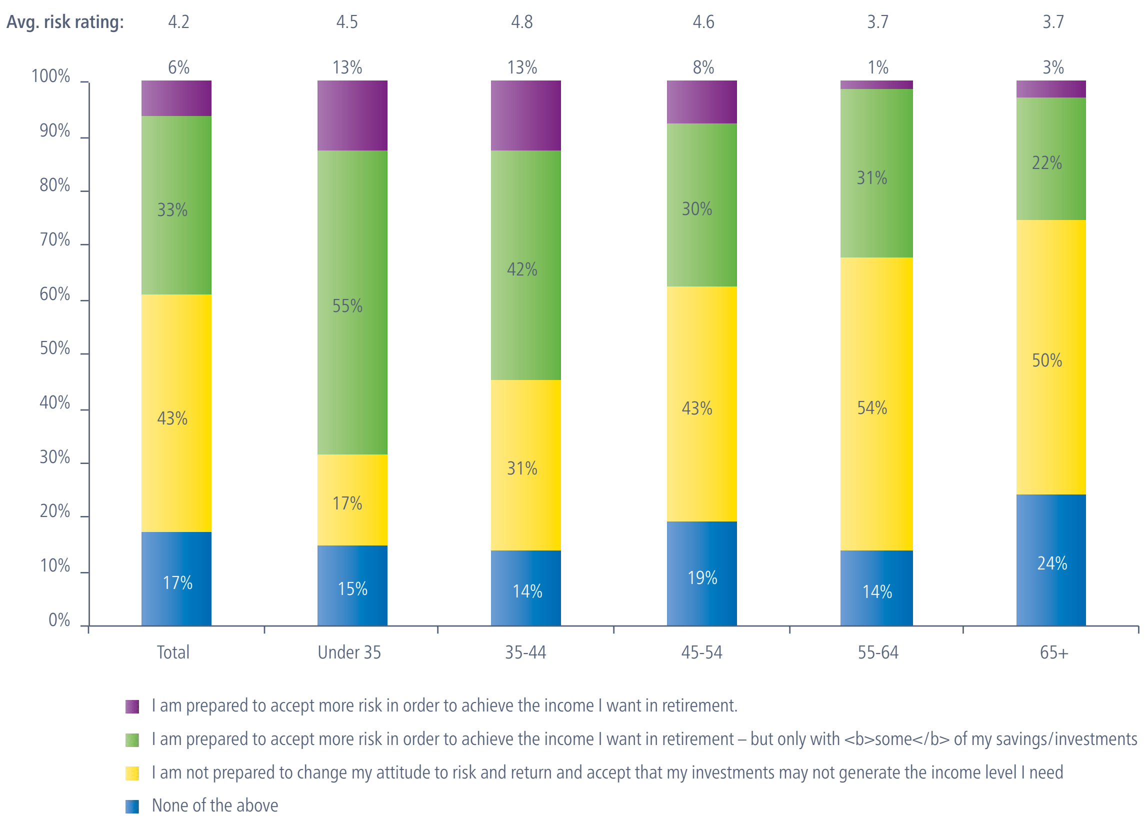


Advised investors are more aware of, and more knowledgeable about, the products in which they are invested.

– Investor attitudes to risk and return are typically low to moderate, becoming more conservative with age. 60% of investors overall were not prepared to accept higher levels of risk to achieve higher income levels in retirement

60% of investors overall were not prepared to accept higher levels of risk to achieve higher income levels in retirement

Q. Thinking about your attitude to investment risk and return, what statement best describes you?



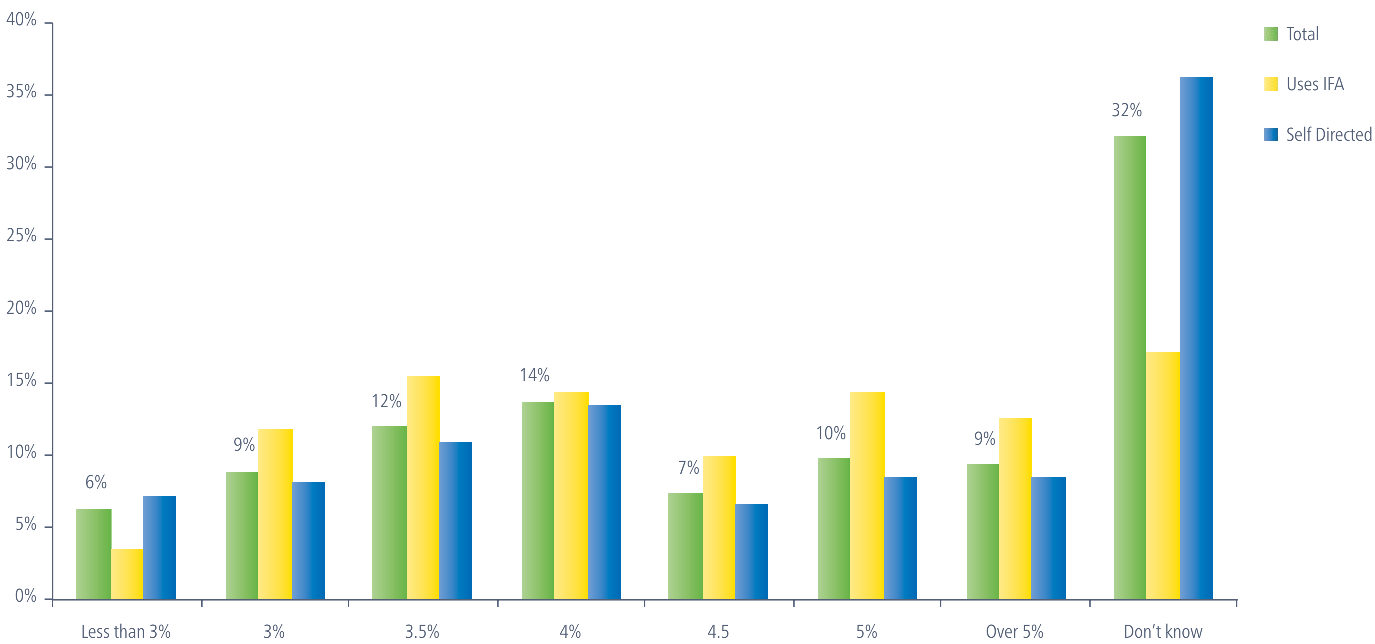
What % of your portfolio would you feel comfortable holding in higher risk investments?

Less than 10%	11%
11-25%	30%
26-49%	38%
50%	9%
Over 50%	9%

Due to rounding some totals might not add up to exactly 100%

INVESTOR EXPECTATIONS OF A REALISTIC YIELD FOR REGULAR INCOME IS ON AVERAGE 4% (BUT 1 IN 3 DON'T KNOW). ADVICE-LED INVESTORS HAVE CLEARER PERCEPTIONS/HIGHER EXPECTATIONS: CITING ON AVERAGE 4.3%

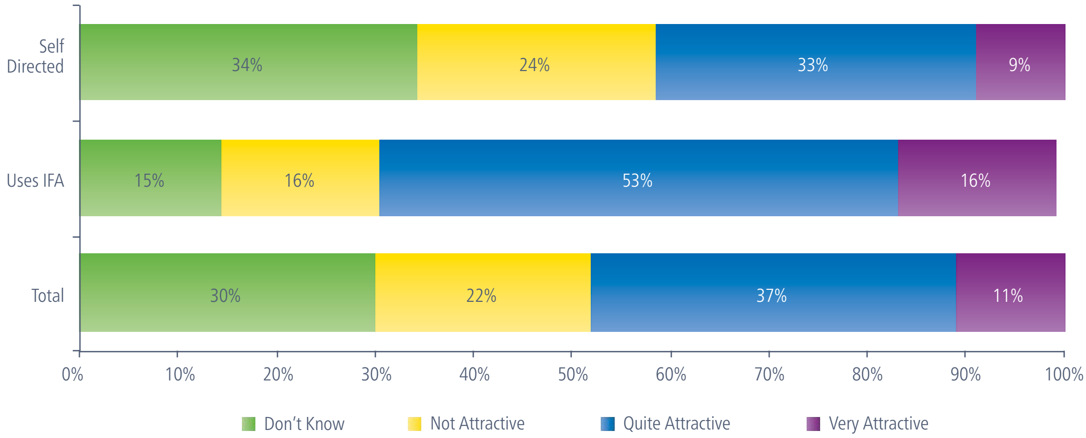
Q. In the current market environment, what % yield do you think is realistic to expect an investment fund to generate for regular income?



ADVISED INVESTORS ARE MORE LIKELY THAN SELF-DIRECTED INVESTORS TO UNDERSTAND MULTI-STRATEGY FUNDS, AND FIND THEM APPEALING

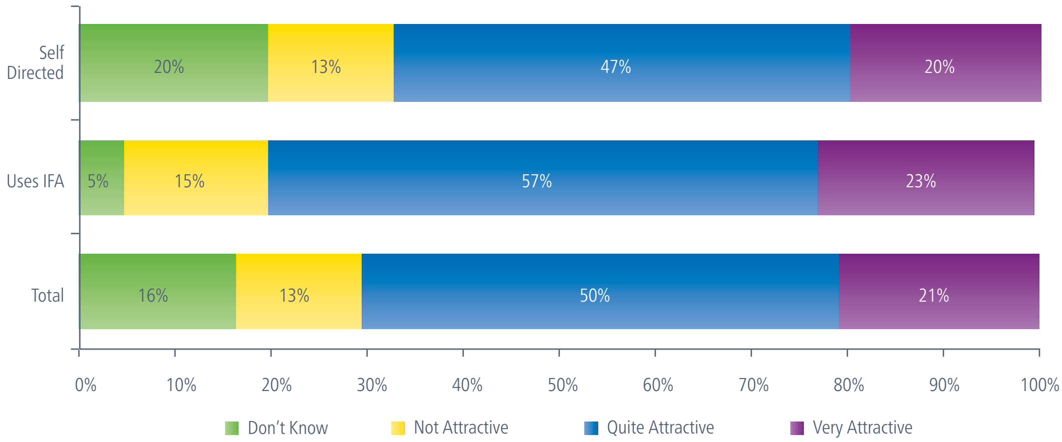
Q. How attractive do you consider multi-strategy income funds within the context of today's market conditions?

A multi-strategy fund invests in a wide range of investment strategies to spread risk and help the fund achieve its income targets even when market conditions are challenging



Q. How attractive would you consider an income fund which:

- Targets an annual income of 4% above the Bank of England base rate (before tax)
- Pays income on a monthly basis
- Seeks to preserve capital
- Aims to be less than half as volatile as equities



YOUNGER INVESTORS WANT TO KNOW: 'HOW MUCH DO I NEED TO SAVE?'
OLDER INVESTORS WANT TO KNOW: 'WHERE SHOULD I SAVE?'

Q. In which of these areas do you need more information or advice to help you plan adequately for retirement?

	Total	Under 35	35-44	45-54	55-64	Over 65
The total amount you need to save in order to achieve what you want to do, and earn, in retirement	26%	52%	33%	29%	20%	17%
Whether or not your savings will generate enough income to last all through retirement	35%	44%	41%	30%	35%	34%
(If you are not yet fully retired) How much you need to save now to achieve the sort of income you want in retirement	25%	40%	30%	36%	26%	5%
The most appropriate type of products to help you achieve what you want to do, and earn, in retirement	46%	35%	34%	38%	51%	61%

WE ASKED: WHAT SORT OF ADVICE OR INFORMATION WOULD BE HELPFUL TO YOU?

"What I need to save now for a certain level of income in retirement"

"How to make the most of what you have got, after all, no-one knows how long you will live"

"A website explaining all options or the opportunity to speak to someone face to face"

"Comparisons of charges of different advisory services. Different types of funds available"

"Where to invest with a guaranteed interest rate"

"How I can have stable and consistent income in retirement"

"Knowing the right things to invest in and for how long"

"Anything that will help me achieve a liveable [sic] income"

"How much actual income I can expect in retirement"

"How much to save each month and where to save it"

"A projection of what my retirement income would be"

"The products available, and how they work and their level of risk explained"

"How to maximise return without risk"

CONCLUSION – INVESTORS NEED ADVICE MORE THAN EVER!

Today's investors face an unprecedented level of personal responsibility in planning for their financial future. Every one of the individual investors who took part in the survey expressed an appetite for support or information on 'what, when and how' to save in order to meet their goals. This research underlines how important it will be for financial advisers, investment managers and policymakers to take a genuinely long-term approach and work together to meet the needs of investors, particularly with regards to achieving a sustainable income without taking undue risk, and leaving a legacy.

Advisers have seen a surge in the number of investment options available to investors. This greater choice has increased demand for advice and requires greater flexibility as regards where and how their clients might invest. For high net worth clients, advisers want solutions that will fit readily into a wider portfolio to meet a specific outcome; they are employing different drawdown and income strategies to maximise the new tax advantages. For mass affluent clients, advisers are focused on facilitating outcomes that were not previously possible, often introducing more flexible drawdown options, taking care to preserve the value of their clients' capital investment, while educating them on the implications of drawdown on future income. Advisers are also seeking to manage expectations of future income levels in order to deliver sustainable income.

In terms of where and how to invest, multi-asset and multi-strategy funds were widely acknowledged as offering strong potential for sustainable income; multi-strategy funds in particular were viewed as offering the best prospect for sustainable income regardless of the investment climate. In addition to offering true diversification and protection against capital loss, multi-strategy funds give advisers an opportunity to introduce "DFM-quality" elements into smaller portfolios.

We certainly believe the research confirms our view that the challenging market environment and the changing investment landscape require a new level of flexibility and a willingness by investors, advisers and providers to consider new income solutions.

Important information

This document is for investment professionals only. It is not to be distributed to or relied on by retail investors.

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