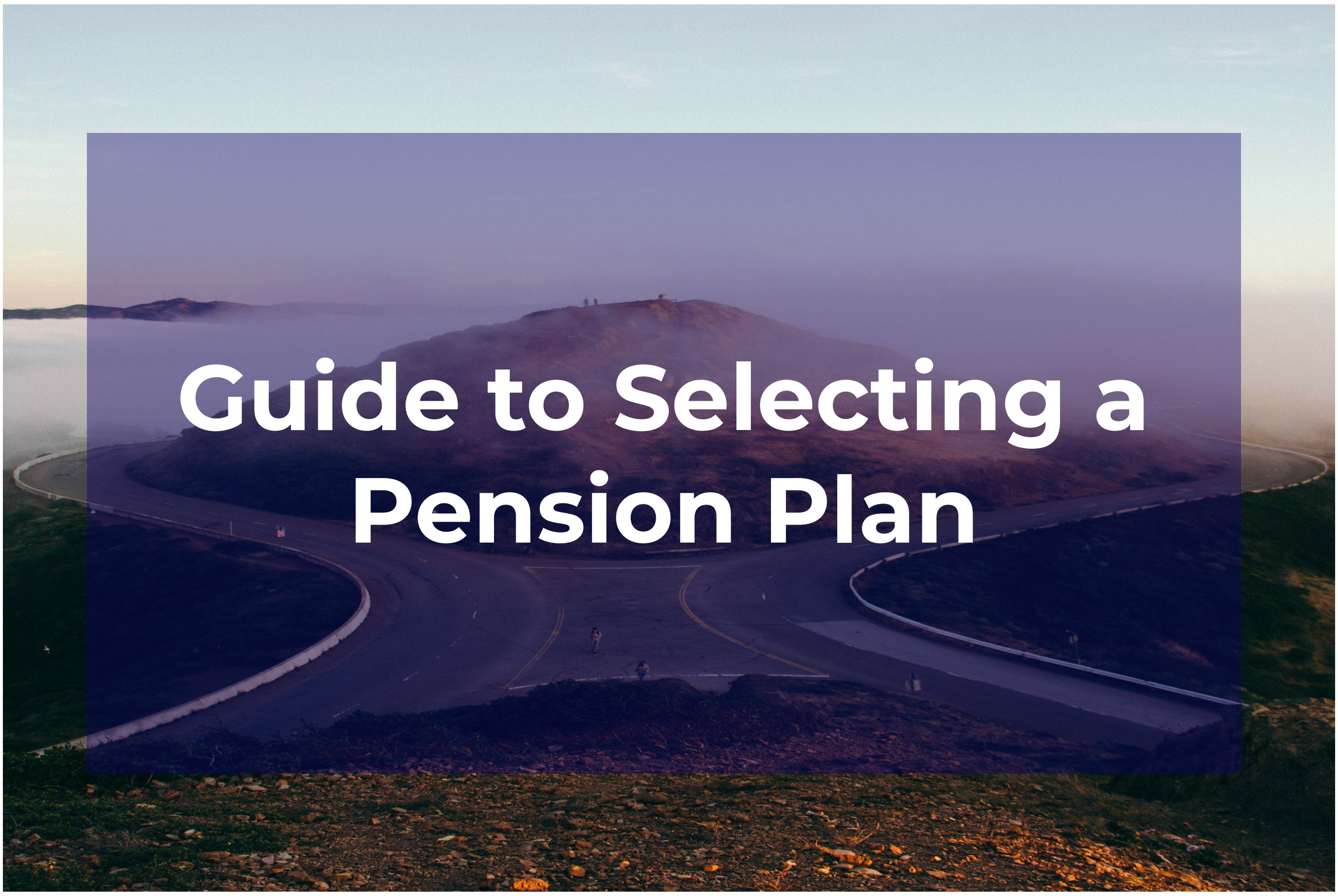
Atkins Bland

Investments • Pensions • Financial Planning



Guide to Selecting a Pension Plan

What does this guide contain?

This guide looks at the broad choices when selecting a personal pension arrangement. It does not attempt to look at any specific plans or cover issues relating to any employer's pension which may be available to you.

If you are employed, you should be a member of a workplace pension scheme with the benefit of employer contributions.

However, paying into a workplace pension may not be sufficient to generate an adequate retirement income, so this guide is relevant to anyone able to consider pension contributions and not just the self-employed.

The "*Atkins Bland Guide to Saving for Retirement*", looks at the general subject of retirement funding, including options other than pension plans, and is available on request.

How is a pension fund invested?

All investment-based pension plans give a choice of investments to use, ranging from just a few to literally thousands.

Most pension funds invest in either the stock markets, the bond markets, infrastructure or real estate, or, in many cases, in a mixture of all of these.

However, these broad areas can be broken down into sub-categories and this creates a huge difference in the level of choice between one pension plan and another.

A key option with more or less all pension schemes is that they give the choice of using broadly-based multi asset managed funds, or a range of specialist funds which allocate capital to particular areas. With the first, all investment decisions are made by the fund management company. With the second, it is up to the pension plan holder, normally in conjunction with their financial adviser, to determine how their capital should be spread amongst the different market sectors and geographic areas, and which fund managers to use for each area.

Some plans also offer "with profits" funds. These differ from most pension funds since there are usually underlying guarantees applying at retirement. In exchange for the benefit of a minimum guarantee, the investor might not receive all the investment growth achieved by the fund. This is because the funds may keep back a proportion of investment growth in a reserve fund to support the guarantees and help ensure they can be met, even if markets suffer a harsh fall.

Another common choice is a "lifestyle" strategy, where asset allocation is designed to match time frame to retirement and automatically adjusted at set dates ahead of that, reflecting the way investment risks change with time horizon.

Whichever style is preferred, access to a wide choice of funds, managed by different companies, is ideal, both to facilitate diversification and to avoid being stuck in a fund where the performance disappoints.

Deciding whether you prefer a multi asset managed fund approach, or a portfolio of specialised funds designed to match your own personal and specific priorities, preferences and objectives is a good starting point to the plan selection process.

Atkins Bland can provide advice on either strategy, and keep the suitability under regular review.

Investing for natural income

A pension fund will eventually be used for income. For some this will be by selling the investments and using the money to buy an annuity. For others it will be through keeping the money invested and taking income from the capital.

It is not easy to know, many years in advance, which will be most suitable, but wise to consider the impact of selecting a plan not well structured for the second option.

For details on the way pension benefits can be taken, please refer to the *"Atkins Bland Guide to Taking Pension Benefits"*, which is available on request.

Unless there is little doubt that annuity purchase will be chosen, it may be best to select a pension where the investment options can generate natural income, which can be distributed.

Most pension plans operated by insurance companies do not offer this at all, so may not be a good choice beyond retirement age, causing a need to change plan or accept the added risk of taking "income" through regularly selling investments.

The *"Atkins Bland Guide to Generating Income from Natural Yield"* looks at this important subject and is available on request.

Screening for ethical or environmental issues

ESG (Environment, Social and Governance) or SRI (Socially Responsible Investing) funds are widely available and more and more investors are wanting to take these issues into account. The most flexible pension plans offer access to more or less the full market of available funds in these categories, while others offer very few.

If ESG or SRI factors matter to you, plan selection should focus on adequate availability of funds in these categories.

The *"Atkins Bland Guide to Socially Responsible Investment"* looks at this subject and is available on request.

What about future fund performance?

The future level of return from any pension investment is unknown, because there are far too many unpredictable variables.

This means it is not possible to know which investment sectors will produce the best results or which investment fund managers will be at the top of the league table, and which will be towards the bottom. Past performance is often used as a guide to fund management quality, but it is not a reliable indicator of the future and there are always other factors at play.

Due to the uncertainty over future results, it is generally wise to have a good spread of investments. It is also useful to have access to a good range of different fund management companies, partly to widen the spread to control risk and partly to be able to easily move from one to another.

How do I know what investments to choose?

In choosing investments to hold inside a pension plan there are two stages to go through.

The first is to decide what types of investment are most suitable. This will be determined partly by economic and investment market condition but also by your:

- Personal preferences
- Circumstances
- Risk preference
- Capacity for investment risk
- Time frame before retirement
- Expectations on how your fund will be used to pay income

The second is to decide which fund management companies, or individual shares, to use to invest in the selected markets.

This is a complex process and should include an appraisal of the long-term performance records and current strategies of both the fund management companies and the individual fund managers.

Once this process is completed, it is important to periodically review the choices, since all the factors used to make the selections can change.

What about charges?

The charges for setting up and running a pension scheme, or most other investments, include three broad costs:

- The administration costs
- The fund management costs
- The costs of initial and on-going advice.

Looking at each of these:

Administration costs

These pay the company operating the plan for the various administration functions required to run a pension plan. While there are exceptions, the difference between the administration charges of different companies tends to be quite modest, due to the need to be competitive. However, the quality and flexibility of the service can vary substantially.

Since the difference in administration charges is usually less significant than the difference in investment flexibility and administration standards, the latter two issues are often the more important factors in making a selection.

Until quite recently, most pension plans were operated by life insurance companies, running their own investment funds and often with little clarity on how total charges were broken down between fund management costs and administration costs.

However, many modern plans are operated by administration companies which have no involvement in fund management and these plans do very clearly show what the administration costs are.

As a guide, administration costs are normally in the range of 0.25% pa to 0.5% pa as a function of the value of the pension plan. With very small plans and if using a company with a fixed charge as well as a percentage-based charge, the costs can be rather higher than this. In contrast, with large funds the percentage cost can be lower as many administrators do pass on economies of scale, to some extent at least.

Fund management costs

These are to pay the company which actually manages your money on a day-to-day basis and decides how it should be invested within the remit of the specific fund in question.

These costs can vary substantially, depending on the nature of the fund and the level of expertise and research required.

The lowest cost funds are normally called “passive” funds, or “trackers”. This means there is no active research and analysis carried out by investment specialists, since the fund simply tracks a market index, or a mixture of indices with a fixed proportion tracking each. As there is no cost for research and analysis and the funds are largely run by computers, these can be very low cost.

Typical management fees for “passive” or “tracker” funds are between 0.1% to 0.4% pa.

Naturally, where a fund’s management involves a team of research analysts and one or more managers making day-to-day decisions on how the money should be invested, this adds to the cost. Funds in this category are usually called “active”, as opposed to “passive”, funds.

The fund management costs and expenses for these do vary a lot but are typically between 0.5% to 1.5% pa, but with highly specialist funds sometimes well above this range.

In theory, active management should allow a fund to produce better returns, but this clearly depends on the quality of the managers and the success of their decision making. Many active funds have failed to out-perform a passive equivalent after their higher costs are taken into account, but many others have achieved this, sometimes quite spectacularly.

Without the benefit of hindsight, it is impossible to know whether any particular active fund will do better or worse than a passive alternative in the same market sector. However, as the vast majority compare results with a benchmark index, it is easy to establish if paying for the fund manager expertise has been worthwhile in the past.

Advice costs

These are to pay an adviser, amongst other things, for:

- Researching the market
- Obtaining details on your circumstances, objectives and priorities
- Analysing these
- Preparing and explaining recommendations
- Implementing any agreed actions
- If required, providing ongoing investment advice, monitoring and servicing.

The specific level of these costs depends partly on the company providing the services, but mostly on the nature of the service required.

For those not wanting proactive advice on their asset allocation, but happy to use multi asset managed funds or a lifestyle strategy, the frequency of ongoing reviews should be lower, so ongoing advice costs reduced.

For those better suited to full on-going monitoring and more frequent reviews, including pro-active advice on the investment strategy, costs are higher, but need not be substantially so.

What options do Atkins Bland offer?

Since we specialise in pro-active investment advice and put a lot of resource into this area, we are able to offer the full range of options.

At one end of the scale, we offer advice on the selection of a low-cost plan using a multi asset managed fund or "lifestyle" approach, which does not require our ongoing services concerning the asset allocation but simply a periodic review of the merits of the funds selected.

At the other end of the scale, we offer advice based on the widest possible range of investment choice, combined with pro-active advice on how your money is invested amongst different companies and market sectors, and on any alterations we feel are wise to reflect changing conditions.

We can also offer a service somewhere between these options; for instance, providing pro-active advice on asset allocation by sector and geographic region, but using passive rather than active funds to keep costs down.

The flexibility in our advice charges relates principally to the issue of on-going advice. The costs associated with our initial advice on plan selection do not vary with the choice of plan, since the work and expertise involved is unchanged.

The "*Atkins Bland Guide to the Cost of our Services"* provides more information on our charging structures.

Are charges or investment flexibility more important?

This is impossible to know in advance, but a detailed look at past records shows that differences in investment performance can often be much more significant than differences in charges, even between the most expensive and the very cheapest.

This suggests that a lot of attention should be given to the investment strategy and choices.

However, the relevance of this will vary with reference a number of factors, such as:

- The amount you are investing – the larger the fund the more the potential to spread between different funds
- The length of time before you retire – the cost of moving between pension providers or individual investments may not be justified if, for example, there is less than five years until retirement, and you plan to buy an annuity when you do retire
- How you plan to take pension benefits - if you do not expect to buy an annuity, the money will remain invested throughout retirement, to generate income. The lowest cost options may not provide access to any income generating investments, so may not be well suited to your needs
- Your preference regarding investment risk – this could impact on the relevance of having a wide investment choice and access to more specialist funds
- Other factors, such as a preference for environmentally friendly or ethical funds may also influence the choice of provider.

Are "illustrations" and projections helpful in selecting a plan?

While illustrations and projections from pension companies do have their uses, care is needed when assessing these since they:

- Should not be considered an accurate guide to actual results
- Are misleading as they assume that values change each year by the same amount rather than go up and down
- Are based on a set of assumptions for investment returns, inflation rates, interest rates and annuity rates which are likely to be quite different from actual future figures
- Assume you do not get any benefit from paying for active management so will show the lowest cost options producing the best results, which might prove very misleading.
- Can only be compared between pension companies if ALL the assumptions used are identical

It is best to work with a professional adviser when comparing illustrations and projections to help ensure any comparison is valid and fit for purpose.

Is it better to have ongoing advice on my investment strategy or to use a multi asset managed fund?

This also depends on a number of factors relating to your personal preferences and priorities.

It is never possible to know if pro-active advice on asset allocation will produce better or worse results than a multi asset managed fund.

A portfolio of specialist funds enables you to use different managers for different areas, thereby taking advantage of specialist expertise.

This benefit can, though, be achieved by selecting a "fund of funds" multi asset managed fund, where the manager spreads the money amongst a range of funds managed by different companies.

Perhaps the key issue is the degree to which you would like a strategy tailored to your own specific circumstances and needs.

For anyone wishing to take an interest in how their money is invested, we believe pro-active advice on asset allocation can be the best choice, but this will not suit everyone.

Those who do not want anything more than the minimum involvement in how their pension money is invested may prefer a multi asset fund approach.

Conclusions

There is no right answer to the question over which pension plan is best, as it depends so much on individual requirements and circumstances.

However, if the selection process achieves a very wide range of investment with a high level of flexibility and solid administration at competitive costs, it is likely to satisfy the needs of anyone and accommodate changes in those needs over time, potentially more successfully than a plan with less flexibility.

Important notes

The value of investments, other than deposit accounts or some guaranteed investments, will fall as well as rise, as can any income produced.

Any opinions expressed on the merits or disadvantages of any options are intended as a general comment only and not as specific advice to the reader.

This document is intended as a supplement to full independent advice and not as a replacement for it and should be read in conjunction with any personalised recommendations provided by Atkins Bland Ltd and with any product brochures supplied.

Any reference to taxation, regulation or legislation is based on our current understanding and details should be checked before any reliance is placed upon its accuracy.

Errors and omission excepted.

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