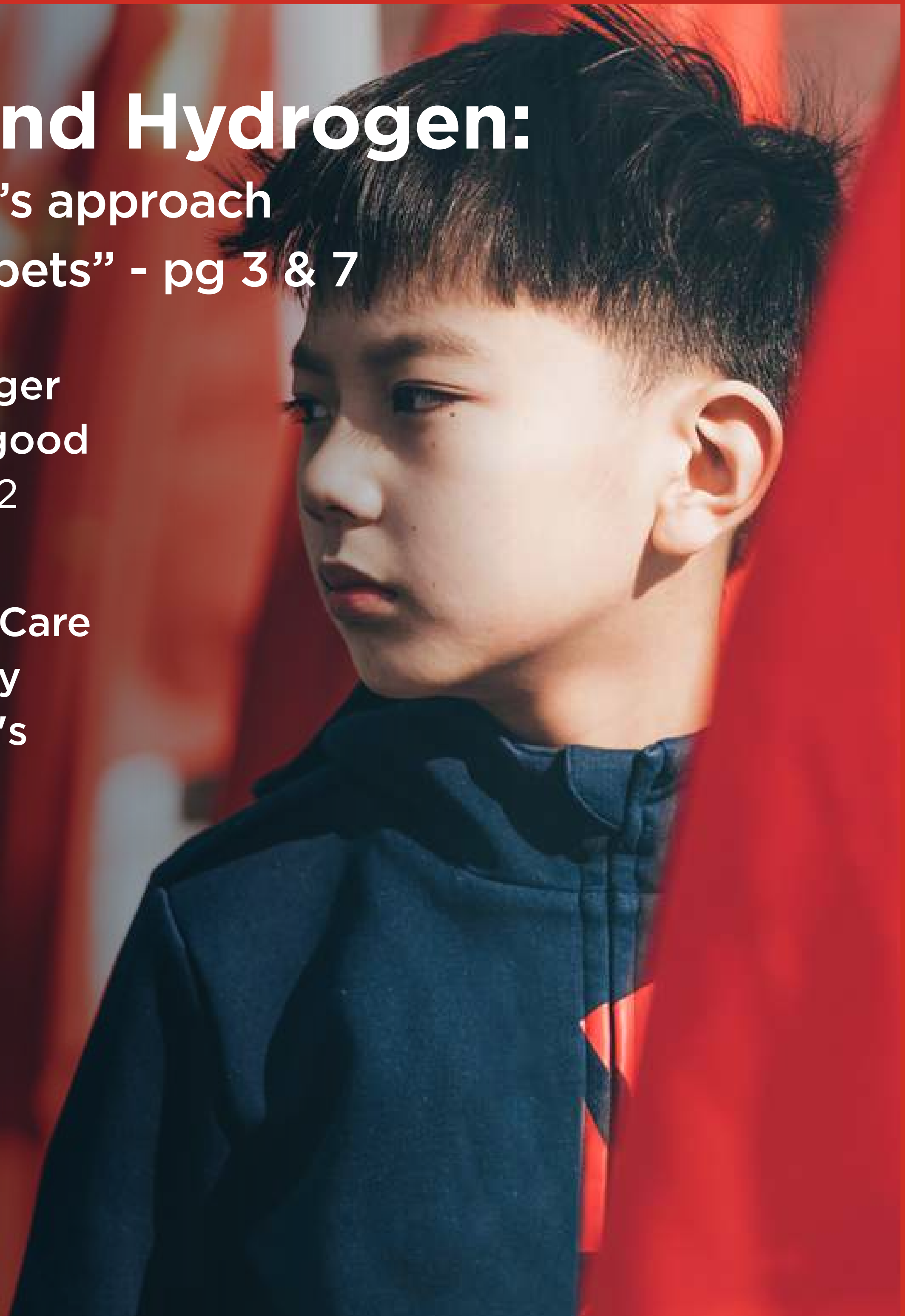
Money Matters

WREN STERLING

NAVIGATING THE FINANCIAL LANDSCAPE

Winter 2021



China and Hydrogen:

The investor's approach to two "big bets" - pg 3 & 7

Is working longer in retirement good for you? - pg 12

Will Later Life Care be improved by the Chancellor's Levy? - pg 19

IN THIS ISSUE

3
What China's populist pivot means for investors
7
The promise of Hydrogen
12
Thinking of working longer in retirement?
15
Separate futures? Sharing your pension
19
What the Health and Social Care Levy doesn't cover
24
What's happening in the defined benefit pension market?

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Welcome to the Winter 2021 edition of Money Matters.

Once again, we're grateful to some of our investment partners for their insight in this magazine. A plus of being an independent financial adviser is that we can work with multiple investment managers and benefit from diversity of opinion and expertise.

Firstly, China has become a complex beast for investors. It is increasingly adversarial to Western democracies, yet it is the economic consumption and production powerhouse of the world and cannot be ignored. Brewin Dolphin has taken a deeper look at the issues and opportunities available.

Similarly, as the world looks ahead to a greener future after Cop 26, could hydrogen be the answer to many problems? Waverton has a fascinating piece on the potential of the world's lightest element.

On top of that, there's an article on the benefits and drawbacks of working for longer, what happens to pensions after divorce and an update on the final salary market, which Wren Sterling is proud to support.

I hope you enjoy Money Matters and I want to wish you and your loved ones all the best for the festive season and the New Year.

Ian Halley
Chief Executive Officer
Wren Sterling

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WHAT CHINA'S POPULIST PIVOT MEANS FOR **INVESTORS**

Several forces have pushed Chinese stocks lower in 2021, with the authority's heightened regulatory focus a key headwind.

Wren Sterling asked Paul Danis, Brewin Dolphin's Head of Asset Allocation, to explain the implications for investors.

What's going on in China?

The Chinese authorities shocked markets last autumn by pulling the IPO of Ant Group a mere two days before the event was due to take place. It was set to raise $37bn, which would have made the listing the largest ever by a wide margin. Since then, there has been a steady stream of announcements from Beijing which has made clear the authorities will take an increasingly hands-on approach to regulating companies and managing the economy. Chinese president Xi Jingping unveiled his populist 'common prosperity' plan, which is designed to reduce social / economic imbalances. In a nutshell, the plan entails beefing up public services and the safety net, reducing inequality and expanding the middle class.

What are the implications for the Chinese economy?

Most investors buy in to the view that the Chinese economy will continue to expand at a significantly faster pace than most other countries for the foreseeable future. But it's debatable whether Xi's common prosperity drive is going to help or hinder China's already superior structural economic growth trajectory. On the one hand, less inequality and a bigger social safety net will likely result in a lower aggregate household saving rate in China (which at around 30% is currently very high). That means less saving and more spending which should support growth. On the other hand, common prosperity policies and greater regulation could weigh on private companies' willingness to invest.

> Since 1995, the Chinese economy has grown over 2000%, while Chinese equities have provided a USD total return of only 124%

Isn't a positive economic outlook good news for China-listed equities?

Since 1995, the Chinese economy has grown over 2000%, while Chinese equities have provided a USD total return of only 124% (as of September 2021). The regulatory pivot by the authorities doesn't inspire confidence that the relationship between economic growth in China and equity performance is about to change. At any rate, the greater regulation and the higher wages and taxes that could result from Xi's common prosperity drive should probably be considered headwinds for the Chinese corporate sector over the medium term.

How has the Chinese stock market reacted?

Chinese equities began to sell off sharply in February this year. The peak coincided with a realisation among investors that the authorities' regulation drive was more than just about

reining in Ant and its founder Jack Ma, who had been critical of government policy. The MSCI China index put in a tentative bottom in August after a peak to trough decline of 32% (in USD total return terms). This was bigger than the 22% loss the index made at the height of the Covid-19 crisis, but less than the 78% loss that Chinese equities made during the 1997 Asian financial crisis.

Are some areas of the Chinese market affected more than others?

The tech-like internet companies (such as Alibaba and Tencent) have been hard hit. This reflects the authorities' drive to correct what they view as anti-competitive practices, limit time playing video games for under-18s, and address privacy concerns, among other things. Another factor at play is that many of the hardest hit Chinese companies are listed on US exchanges. This hasn't been the cause of their poor performance, but there is some concern that these might ultimately need to be delisted from the US and re-listed on one of the Chinese bourses. Uncertainty remains with regards to how this will ultimately unfold. A forced US delisting may weigh on share prices around the time when it happens. But this probably isn't the factor that investors need to be most concerned about.

Don't lower valuations provide an attractive buying opportunity?

The MSCI China equity index is trading at a 27% discount to the global market on 12-month forward price to earnings ratio, which is bigger than its historical average discount of 18%. This is certainly a much more attractive multiple than Chinese equities were trading on earlier this year. However, it's not clear if it is low enough given the profit headwinds many of China's most valuable companies are now facing due to the new regulatory reality. Chinese equities have been cheaper before: they traded on a 42% discount following the 2015 sell off. Meanwhile, Chinese profit margins are high relative to history. After enjoying an almost straight-line expansion since 2013, margins are now vulnerable to some compression.

Should I avoid Chinese equities entirely then?

China is not one of our currently favoured equity benchmarks. However, we believe it makes sense to have some exposure. While there's room for Chinese profit margins to decline, there likely won't be a collapse. China's authorities are taking greater control, but the country is not going 'full Soviet'. It's still going to be an extremely innovative and entrepreneurial place.

The Warren Buffet approach to investing is to be "fearful when others are greedy, and greedy when others are fearful". The dominant market emotion toward China at present is fear. Mid last month, 'China's attack on tech' made it onto the cover of The Economist magazine, widely thought of as being a contrarian indicator. Personal finance writers are also raising doubts about investing in China, which perhaps indicates the risks are widely appreciated. The

negativity toward China can be observed in the fund flow data as well. Global equity funds have cut their exposure to China and Hong Kong, and there's been a surge in emerging market flows going into exchange traded funds (ETFs) that exclude China.

There are also cyclical reasons to not want to become overly bearish toward China at this juncture. Chinese economic growth slowed sharply this summer due to a Covid-19 wave, which now looks to have been brought under control. In addition, after tightening fiscal and credit policy in the first half of this year, signs have emerged that the authorities are shifting to a more supportive stance. All this implies a cyclical growth rebound in China, which should support the equity market.

Brewin Dolphin is one of Wren Sterling's investment management partners.

It's still going to be an extremely innovative and entrepreneurial place.

The value of investments, and any income from them, can fall and you may get back less than you invested. Neither simulated nor actual past performance are reliable indicators of future performance. Performance is quoted before charges which will reduce illustrated performance. Investment values may increase or decrease as a result of currency fluctuations. Information is provided only as an example and is not a recommendation to pursue a particular strategy. Information contained in this document is believed to be reliable and accurate, but without further investigation cannot be warranted as to accuracy or completeness.

THE PROMISE OF **HYDROGEN**

John Buckland, Analyst, Waverton Investment Management

The planet is warming and over the coming decades the global economy will be reshaped by our efforts to limit and mitigate its effects. Amid these threats lie opportunities for investors who can spot them. Waverton's John Buckland explains.

All our energy comes from the sun. Some 350 million years ago, its rays nurtured woodlands that grew, matured and died, laying down the carbon-rich material that eventually powered the industrial revolution.

Freeing the energy in that stored sunlight has got us into trouble, releasing greenhouse gases and cranking up the heat in our atmosphere and oceans. To counter this trend, we must switch to energy sources that will release less carbon and last for as long as the sun burns.

Enough sunlight bathes the earth in an hour to satisfy global energy needs for a year. Winds whipping over the planet's surface carry sufficient energy to fulfil global consumption seven times over. This is all the energy we need. The challenge is getting it into usable forms and to where it is required.

Wind and solar energy have three major drawbacks. One is that they can be harnessed only to supply electricity, which today represents just 20% of global final energy consumption. The other is that they are variable, available only when the sun shines and the wind blows. Finally, the energy they contain must be converted into another form for transportation (in the jargon, they are not dispatchable).

But there is a solution that can harness renewable electricity. It is a carbon-free fuel that suffers none of these disadvantages: hydrogen.

Hydrogen's advantages are many: it contains a lot of energy (pound for pound, three times that of gasoline and more than 100 times Li-Ion batteries); unlike conventional fuels it is not poisonous; the right kind of hydrogen is carbon free; and, unlike the lakes and rivers that power the world's hydroelectric plants, it can be transported.

Exploiting hydrogen means overcoming some tough challenges, ranging from the physical to the economic. The chief physical problem is hydrogen's low density compared to other gases. One kilo takes up nearly 15 times as much space as a kilo of air, for example, so it must be compressed at very high pressures and/or very low temperatures for efficient storage and transportation, requiring heavy and expensive containers. A typical hydrogen tank weighs twice as much as the gas it contains. Hydrogen gas is also the smallest known natural molecule, which means it can sneak through the tiniest fissures in tanks or pipelines, making loss through leakage a particular challenge. The physics means the industry relies on specialist skills and expensive materials and equipment.

This is where the economic challenges come in. Hydrogen is designated by a variety of colours depending on its environmental footprint: grey (the most common form today, created from natural gas or methane in a process that generates CO^2); black or brown (created from coal or lignite and generating more CO^2 than grey); blue (grey, black or brown hydrogen but with most of the resultant CO^2 captured and sequestered); and green (generated by electrolysis using electricity from renewable sources, and carbon free). Blue and, particularly, green hydrogen are the promising environmental fuels of the future, but they are more costly to produce than polluting brown or grey.

Until the cost can be brought down to comparable levels (or the costs of more polluting varieties raised through carbon pricing) industry is reluctant to embrace them, although there is increasing pressure to do so to meet CO^2 targets. The Hydrogen Council, an industry group, forecasts that this will happen within the next decade, while some participants suggest blue hydrogen can be produced competitively now.

Hydrogen also faces a social challenge. As with nuclear power, spectacular public disasters have tarnished public views of hydrogen as an energy source, but out of the public gaze hydrogen has been playing an important role in the production of electronics and the desulphurisation of gasoline and diesel. It was not long ago that ‘town gas', which contains 50% hydrogen, was used to light our streets and to heat our homes. As we write, there are projects underway in the UK to use hydrogen for these purposes again, blending it with natural gas. Countering popular reticence will take careful education and public relations. Hydrogen is indeed highly flammable (that's the point), but it also disperses rapidly when released into air and, because of its low density, tends to rise quickly out of harm's way. Demonstrations have shown that a fuel fire in a hydrogen-powered vehicle can burn out completely with little damage to the vehicle, in contrast to the conflagration of a gasoline fire.

If these challenges can be overcome, and there is every reason to be optimistic, there is a bright future for green hydrogen as a renewable, clean source of energy. The Hydrogen Council expects hydrogen to represent around 20% of the energy mix by 2050, with production increasing from around 80mt per annum now to some 600mt. At US$2/kg this would generate revenue of US$1.2trn. Adding equipment sales could turn hydrogen into a US$2.5tn pa industry. One market analyst breaks it down thus:

If these challenges can be overcome, and there is every reason to be optimistic, there is a bright future for green hydrogen as a renewable, clean source of energy.

- Hydrogen gas sales US$1,400bn
- Fuel cells for transport US$360bn
- Fuel cells for stationary power US$203bn
- Electrolysers US$215bn

Add to this billions in sales of equipment for industrial uses and investment in infrastructure expansion such as pipelines and storage, and the size of the opportunity begins to take shape. Necessity is the mother of invention, and now she is giving birth to the next industrial revolution. Hydrogen promises to play a big part. The IEA in its recent report, 'Net Zero by 2050', forecasts that "every month from 2030 onwards, ten heavy industrial plants [will be] equipped with CCUS [Carbon Capture, Utilisation and Storage], three new hydrogen-based industrial plants [will be] built, and 2 GW of electrolyser capacity [will be] added at industrial sites."

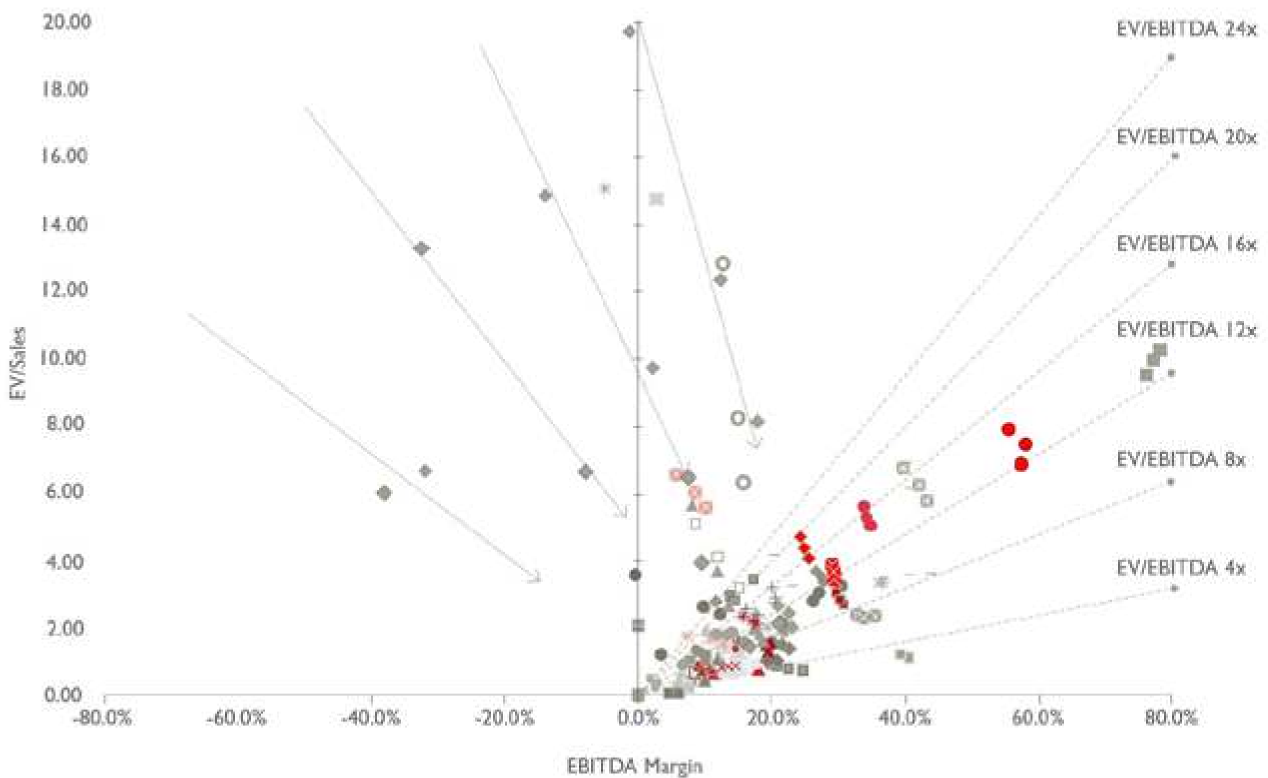

Figure 1. Hydrogen Infrastructure and Usage
Source: Siemens Energy, Waverton

Notes: On this "snail trail" chart, each point traces the change for a company from this year (FY1) to 2023 (FY3) based on consensus expectations. The Enterprise Value / Sales (EV/Sales) ratio measures the value of the business relative to its sales revenue, but the change in this ratio can also indicate growth.

The arrows (top left) are predominately for the small pure play fuel cell and electrolyser makers. Many of these companies have low revenue and are currently loss making as they spend on R&D and build manufacturing capacity. The downward direction of the arrows, their length and the gaps between points on the chart show how fast the company is growing (higher sales means lower EV/ Sales ratio) and by how much profitability is changing (EBITDA margin is also a quasi-indication of cash flow margin). The apparent overvaluation now is an indication that the market is discounting the expectation of rapid growth and a move to positive profitability.

The crowding of points to the right of the origin shows that most businesses have varying levels of profitability and relatively modest growth, reflecting their existing operations, sector dynamics and the economic environment. Companies with high margins and high profitability deserve high valuations. The radial lines are lines of constant EV/EBITDA valuation.

Key to hydrogen's role is achieving scale in the supply of the less polluting green and blue varieties of hydrogen fuel, a task that is already in train thanks to government policy and financial support. The EU and some Asian countries are leading the way. There has been a proliferation of new hydrogen projects here, and momentum is gathering: in July 2021 the Hydrogen Council listed 359 projects, backed by investment of US$500bn. The UK has issued its own first ever Hydrogen Strategy and is aiming to reach 5GW of low carbon hydrogen production capacity by 2030. It estimates the sector could be worth nearly a billion pounds by then, generating 9,000 high-quality jobs.

Old hands may be familiar with the mantra that hydrogen will be our salvation. Previous waves of hydrogen enthusiasm—during the 70s oil shock, in the 90s as climate change concern went mainstream, and in the 2000s with the 'peak oil' conjecture—all petered out. But this time really looks different. The need to decarbonise is urgent and widely accepted. Infrastructure is already in place, with over 4,000 km of hydrogen pipelines already in place in the US and Europe and some 300 km in the rest of the world. Fuel cell technology is being adopted in trucks, trains, aircraft and ships (in 2023 Norway will launch the world's biggest fuel-cell driven cruise ship, offering carbon-free tours of the fjords). There are few more dangerous words in investing than 'this time it's different', but the evidence is stacking up decisively in hydrogen's favour.

In the meantime, hydrogen can play a central role in tackling the toughest CO^2 abatement challenges. Replacing grey hydrogen initially with blue (using carbon capture and storage - CCS) and later with green hydrogen will offer a lifeline to the oil & gas and chemical industries and will encourage wider acceptance of hydrogen as a fuel and feedstock. It will also help in pushing technological advancement and building the required scale in hydrogen production.

> The hydrogen story offers many opportunities for investors with different time horizons and risk appetites.

Renewables and electricity networks will be important in supporting green hydrogen production and adoption. Global capacity of renewable electricity generation could reach 34 TW by 2050 (from 3TW currently). Approximately 80% of the cost of green hydrogen is determined by the costs of renewable electricity, but developing green hydrogen production capacity can, in turn, support demand for power, underpinning demand in the sector.

The hydrogen story offers many opportunities for investors with different time horizons and risk appetites. To identify them we must trace the sequence of steps needed to build the supply infrastructure and the potential products that will use green hydrogen:

- What is going to happen first and fastest?
- Which areas will be the largest and longest lived?
- Which segments have the most favourable competitive environments?
- Is it better to go for pure plays, or companies where the hydrogen business is currently small but provides future options?
- Is the hydrogen business adding net positive incremental growth, or offsetting an existing business in decline or facing obsolescence?

Using these criteria Waverton has identified a group of around 100 companies that hold promise. We are already invested in some of these, and others may prove of interest over time. The list is not definitive: companies will be added as their circumstances change or will fall off as consolidation eliminates the losers.

Figure 2 (opposite) gives an idea of how Waverton is tracking potential winners.

The chart gives an idea of the number and diversity of companies delivering the hydrogen economy, including in: renewable electricity generation; infrastructure, plant and equipment; distribution networks; and supply of end user

products. The chart shows how the list spans a wide range of profitability and valuation metrics and the extent of change expected over the next three years.

Things will change. Some pure play hydrogen companies will grow rapidly and become highly profitable, with commensurate valuations and returns for shareholders. Small hydrogen related operations embedded in larger companies could be equally transformative for their parent.

The red points on the chart highlight some stocks that are already on the Waverton global and regional recommended stock lists or are owned in the Waverton equity fund portfolios. Thus, while we continue to identify and assess the best long-term hydrogen opportunities, Waverton clients already have some exposure to hydrogen and the energy transition.

Waverton is one of Wren Sterling's investment manager partners.

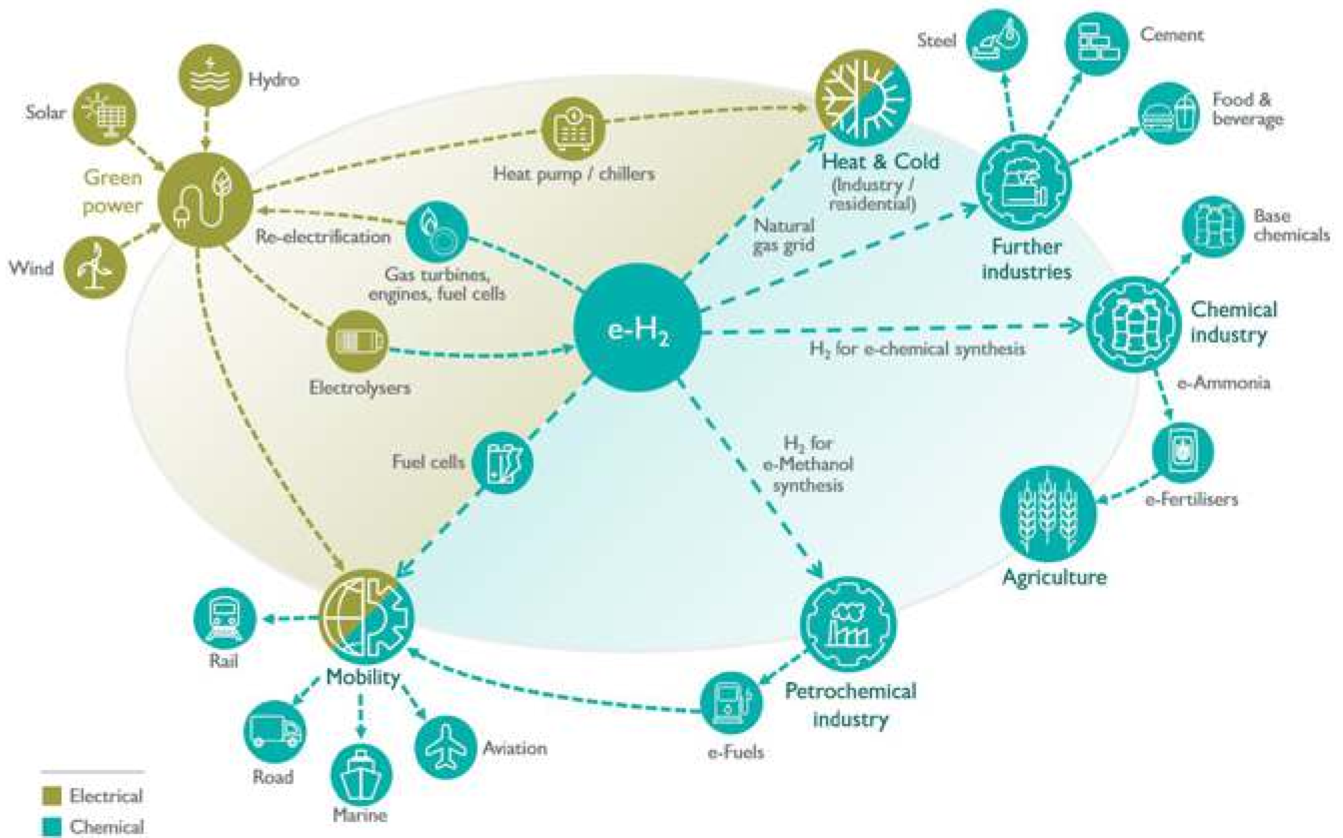

Figure 2. Hydrogen / Energy Transition Universe - Valuation Matrix
Source: Factset, Waverton.

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THINKING OF WORKING PART TIME OR FROM HOME TO STAY IN WORK FOR LONGER?

What it might mean for your financial plans - and is it good for you?

The Office of National Statistics recently released a paper assessing the likely impact of working from home on the employment habits of older workers[1].

It found that the proportion of older workers who are planning to work from home following the coronavirus (COVID-19) pandemic is higher than the proportion who worked from home prior to the pandemic.

This probably doesn't come as a surprise, as the more sapping aspects of work for those who can do their job at home are taken out of the equation. No more 6.30am sardine-like trains or snarled up traffic and plastic sandwiches for lunch. More time for exercise and income still coming in – sounds like a win-win situation.

Is working for longer medically good for you?

We're often told that the most valuable commodity in life is time. Time to pursue the hobbies that bring us joy and satisfaction, or time with friends and family.

For the majority of people, striking a balance between time and earning the money required to lead their preferred lifestyle is a tough place to be, which is why financial advice is so important, as it can help people make this decision.

Financial advice doesn't just look at the financial implications of decisions. We're focused on achieving the most suitable outcome for people and helping provide them with the retirement they want to have. So, telling someone to work for longer in a job that is detrimental to their physical or mental health just to secure more income would not be good advice.

A substantial global study published in BMC Health concluded that working in later life can have mixed results for people.

It concluded: "Extending working life (particularly part time) may have benefits or a neutral effect for some, but adverse effects for others in high demand or low reward jobs. There is the potential for widening health inequalities between those who can choose to reduce their working hours, and those who need to continue working full time for financial reasons. There is a lack of evidence for effects on quality of life, and a dearth of interventions enabling older workers to extend their healthy working life."[2]

So, it really comes down to what you're doing and the state of your mental and physical health. The point now is that societal norms can enable a better working environment for older workers, while retaining them in the economy.

In April to May 2021, older workers aged 50 to 69 years who were working from home reported that it improved their work life balance and well-being.[3]

The trend does appear to be ingrained in our working economy too. Online job adverts including terms related to 'homeworking' have increased at a faster rate than total adverts, with homeworking adverts in May 2021 three times above their February 2020 average.[3]

1 ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/ageing/articles/livinglongerimpactofworkingfromhomeonolderworkers/2021-08-25
2 bmcpublichealth.biomedcentral.com/articles/10.1186/s12889-021-11423-2
3 ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/articles/businessandindividualattitudestowardsthefutureofhomeworkinguk/apriltomay2021

Phil Jenkins, Chartered Financial Planner, Wren Sterling

What are clients doing?

Phil Jenkins, a Chartered Financial Planner in Wren Sterling's London office specialises in working with clients who have complex circumstances.

"Working flexibly and for longer has been a trend that started pre-Covid. It's rare now that people have a cliff-edge retirement, when they reach their mid-sixties and decide to give up and lie on a beach the very next day. I've seen a lot of phased retirements where clients are asking their employers to go down to a few days a week, discovering new ways to fill their free time and generally feeling more in control of their situation.

"As financial planners, we bring this to life using cashflow planning technology. We can demonstrate to clients that they might not run out of money, which is often their biggest fear. We might find that they can go to three or four days a week and spend a day doing something creative or volunteering. Realising that they've got enough money can be a really liberating moment, as we spend most of our lives worrying about saving enough for retirement."

It's true that Covid has accelerated the adoption of this trend.

"Other real-life examples include people who were sick of commuting. Now that they don't have to do it as much, they're working for longer because they're happy to work in their profession without the hassle of commuting."

Phil says there are a few things to consider.

"If you dramatically reduce your income and you're forced to dip into taking your pension, the Money Purchase Annual Allowance will kick in and you won't be able to add more than £4,000 per annum to your pension without incurring a tax charge. So proper budgeting and financial advice can help you meet everyday expenses and keep your options open for topping up your pension at a later date.

"There are certain sectors that lend themselves to workers being burnt out more than others, such as investment banking and from a wellbeing perspective, it might not be advisable for clients to dip in and out of this world with the goal of phasing retirement, as in my experience, the job doesn't really allow that. Again, if we've done the sums and decided that actually the client has enough money to sustain their lifestyle in retirement, it could be time to do something else.

"There's a balance to strike though. I see clients who really don't know what to do in a cliff edge retirement scenario and I've regularly seen the positive effects of staying mentally and physically active on my clients.

"Finally, if someone has decided to retire earlier, their funds will run out sooner if they're not professionally managed. The rate at which a pension fund depletes can have a dramatic impact on quality of life in retirement, so our projections include the assumption that the funds are professionally managed and the funds that are not withdrawn are achieving a certain growth percentage each year."

Paul Mitchell, Director of Corporate Solutions, Wren Sterling

How are companies supporting people who want to work longer?

Paul Mitchell says: "Companies have been paying more attention to how they accommodate older workers since the default retirement age was scrapped in April 2011.

"The law states that firms must provide cover in group schemes (Group Risk, Group Income Protection, Private Medical Insurance, for example) up to the State Pension Age (SPA). It is then down to the individual company to decide whether it wants to extend that for its workforce. I have some clients who are extending cover to employees who are 70 or even 75 because they want to retain them.

"This is a really powerful benefit for employees as premiums can increase substantially at this age."

It's not just about providing benefits though. The trend towards working for longer and flexibly is causing companies to help employees better understand their options.

"After Pension Freedom in 2015, I've seen a need for more financial education in the workforce. As Phil described, the trend now is for a phased retirement supported by professional advice. We're explaining retirement options to employees and reinforcing the fact that people can take multiple retirement pathways and phase their retirement. Employers are looking to us to deliver this education because of the positive impact it has on the employee's personal circumstances and also because it helps clarify the eventual retirement age in their employees' minds, which helps succession planning strategies."

If you are reconsidering your retirement plans, please contact your adviser to discuss creating a revised plan.

Or if you know someone else who might benefit from speaking to an adviser about their retirement, please ask them to arrange an appointment with us.

When investing your capital is at risk.

SEPERATE FUTURES: SHARING YOUR PENSION

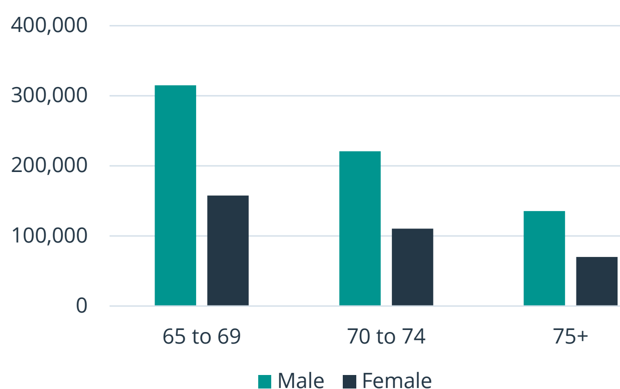
David Yates, Independent Financial Adviser, Wren Sterling

Lots of thought goes into combining a couple's finances. And the longer a marriage, the more finances become entwined.

If they've decided on divorce, a lifetime of assets will need to be divided – and not just joint bank accounts and household bills, but also pensions. It can be tempting to ignore pensions, due to their complexity and fears over fees, but the income from these will directly affect future quality of life.

Fortunately, there are tried and tested approaches available for couples who need to divide a lifetime of entangled finances; from "sharing" pensions 50/50 upon divorce, "earmarking" funds to be divided at a later date, or "offsetting" – where one person keeps the pension in return for keeping other assets (such as the family home).

For those aged 65 years and over, with pensions in payment, median pension wealth of men is nearly double that of women. Median pension wealth for pensions in payment, for individuals with this type of wealth, by age band, and sex, Great Britain, April 2016 to March 2018.



We spoke to David Yates, Independent Financial Adviser at Wren Sterling, about the support he provides to divorcing clients, "Quite often a divorcee will come to us with a Pension Sharing Order and will want support with the lump sum they are about to receive. They're often looking for peace of mind knowing that their money is being dealt with properly, as they may not be confident managing their own money, and have now been put in charge of a large lump sum."

Untying the knot of finances on divorce

It's not compulsory to share your pensions in divorce. If a split is amicable, the couple may want to avoid the expense of court, making an informal agreement with their now ex-partner. But a court order is unavoidable, as it is needed for any agreement to be enforceable.

Pension Sharing is one option available to couples hoping to have an amicable split, that doesn't leave either having to 'start from scratch' with their retirement plans. Without such agreements, there are fears of retirement poverty for one party, as it is rare to have an even split in the pension wealth, or for pension schemes to be in the name of both partners.[4]

What is Pension Sharing?

A Pension Sharing Order is a type of court order that is used to allow a couple to divide their pension funds on divorce. This is an arrangement that can be flexible – starting with discussions of a 50/50 split, but allowing

clients to amend the percentage going to each party depending on the other assets involved (like the family home), or their circumstances. For example, if one person is retired and the other is not.

Once divided, Pension Sharing ensures that the other person no longer has any control over how the funds are used – rather than divorcees continue to be reliant any of their ex-partner's financial decisions. Funds can be transferred into a new or existing pension – or, depending on the scheme, divorcees may be able to join an ex-partner's scheme independently.

David says: "We're often asked to help once the Pension Sharing Order has been produced, and the client has a piece of paper saying, 'I've got this, what do I do?' Our job is then to look at their circumstances and find a fund that matches your needs and attitude to risk – either to start drawing on now or in the future."

Where to start when discussing the future after divorce

Detaching our emotions from money discussions is just one benefit an Independent Financial Adviser supporting their clients as they plan their newly separate futures. Not only as a neutral party, but also as a financial expert. Once you have a Pension Sharing Order, the first step to splitting resources is to find out the extent of your own wealth. A Wren Sterling adviser like David can gather information about your plans, investments and even find lost pensions and can work alongside your solicitor to ensure this is all done at the right time.

David says: "A divorce signals a huge change in a client's circumstances. But this does present an opportunity for them to be in charge of the kind of pension they want. We often discuss more flexible options like Pension Drawdown. Why? Because at this time of their life things can take some time to settle down. If they don't know what's happening with their income, expenditure, level of savings, we won't know what they're going to need in retirement.

"Pension Drawdown can mean retirees can take funds at any point from age 55 , taking 25% of the pot tax free, taking the rest as income when they want but it would be taxable. The downside to that is that once the pot is gone its gone and they could run out of money. They can either manage their money – or get support from an IFA."

A clean break with a Defined Benefit pension

A Pension Sharing Order can affect all types of occupational and private pension schemes, including those that are already in payment. The only exclusions are the basic State Pension, and Widows Pension rights. As usual, Defined Benefit pensions (also known as Final Salary schemes) are more complicated. Very few defined benefit schemes are likely to allow the ex-spouse to stay in the scheme, forcing the whole sum to be transferred away.

David adds: "In the majority of cases I've been involved with, the divorcees have been in their 50s or 60s, and don't have much time to build up their pension assets before retirement.

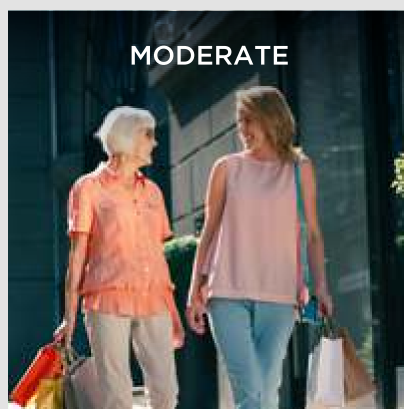
The Pension Sharing Order represents a fundamental part of their income moving forward. They're not looking to get too technical, and want to feel that they are not alone when setting up their finances"

The PLSA's Retirement Living Standards can give you an idea of how much you'll need for the retirement you want

Covers all your needs, with some left over for fun

Single - £10,900
Couple - £16,700

More financial security and stability and flexibility



Single - £20,800
Couple - £30,600

More financial freedom and some luxuries

Single - £33,600
Couple - £49,700

Sometimes, Pension Earmarking could be preferable, where an amount is ring fenced for the future. But as the final decision for when a DB fund is transferred depends on the named recipient, this is not the 'clean break' which Pension Sharing offers.

Getting divorced in retirement

No one wants the question 'Can I afford to get divorced' to be part of a decision about whether or not to end a relationship. A Pension Sharing Order can be put in place, even if one party's pensions are in drawdown. This will mean a significant reduction in the expected pension income.

According to the Retirement Living Standards report from the PSLA, retirement is more expensive when you're not sharing the cost of living. Split pension benefits may no longer provide enough for the quality of life previously anticipated. Divorcees will need to re-calculate how much they think they will receive in retirement – and how much they think they will need.[5]

Setting the date

It's best practice to wait 28 days before applying for a Decree Absolute to dissolve the marriage.[6] How long each of these processes takes will depend on the complexity of the couple's situation, and how easily they are able to provide the required documentation.

No matter where you are in the process of a divorce, talking to a Wren Sterling adviser could help you untangle and make the most of your plans. Typically, your solicitor will contact an independent financial adviser if a pension sharing order is required, so it's worth telling your solicitor that Wren Sterling provides this service.

"How long it will take to set up a new pension will depend on how far along a client is in the divorce process when they get in touch," says David. "If the Pension Sharing Order has already been settled, we'll need to get a letter of authority signed by the person who owns the pension to get the information we need about the pension that's already in place, double check if we're able to keep the funds in the same scheme, that could take a month or two – depending on how quickly

the providers come back to us. It could take eight to twelve weeks to get everything completed.

"But it's not only pensions we can advise on. Any joint protection plans will be null and void, and insurance is particularly important if there are young children involved, if the divorcee suffers from disability, or is unable to work. They may wish to look at continuing to build on their pension pot they've created, and if there's other parts of the settlement that aren't pensions – they might look to invest. It's just a matter of looking at the overall picture and finding what's possible. In the end it's just basic financial planning! After all there are lots of people in this situation, and we work with clients all the time to put these plans in place."

Once the settlement is complete, your Financial Adviser can look at other areas of your finances that have become intertwined. Clients may need to consider Power of Attorney, Trusts, making a new Will, and ensuring that their investments continue to perform well in order to grow and provide retirement income.

The final season of the blame game

The Divorce, Dissolution and Separation Act has been delayed, but should come into force on 6 April 2022. This is the first reform divorce law for 50 years, allowing couples to divorce without assigning blame or fault to either party.

Current rules state that a couple must evidence that they have been separated for two years (if both parties consent to the divorce, five years if not) or provide proof of fault. Even if a party is able to evidence adultery, unreasonable behaviour or desertion, this often has little or no financial advantage in a final settlement.

Even with this amendment to the law, a Divorce Order is still likely to take six months or more to complete. We anticipate that as no-fault divorce rules come into play will see a slight rise in the number of applications, mostly from disappointed couples who had hoped to begin this process 2021.

If you or someone you know is going through divorce, it is always worth having a conversation with an independent financial adviser to prepare you for the financial side of divorce.

This is the first reform divorce law for 50 years, allowing couples to divorce without assigning blame or fault to either party.

4 manchester.ac.uk/discover/news/pension-inequality-a-major-issue-when-couples-divorce-research-finds
ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/incomeandwealth/bulletins/pensionwealthingreatbritain/april2016tomarch2018 (chart)
5 retirementlivingstandards.org.uk/Retirement-living-standards-in-the-UK-in-2021.pdf
6 stephens-scown.co.uk/family/divorce-and-separation/pension-sharing-orders-waiting-28-days-for-decree-absolute

The value of an investment and income from it is not guaranteed, investors capital is at risk
The Financial Conduct Authority does not regulate taxation advice.

BEHIND THE HEADLINES

What the Health and Social Care Levy Doesn't Cover

Clive Barwell, Head of Later Life Advice

Matthew Bell, Independent Financial Adviser

In November, MPs backed an amendment to the Health and Care Bill required to implement the government's proposed cap on care costs by 272 votes to 246.

Back In September, the Chancellor, Rishi Sunak, announced that there would be widespread rises in National Insurance Contributions (NICs) to pay for a new NHS and social care levy. With the issue of paying for healthcare having been kicked down the road for decades, this represented a move to divert resources towards fixing a system straining to deliver essential services.

Commentators are divided on whether the levy will prove to be sufficient, with Paul Johnson of the Institute of Fiscal Studies suggesting that the levy may need to more than double to 3.15 per cent from 1.25 per cent by the end of the decade.[7]

What does all this mean for people approaching retirement and their financial planners? Unlike other aspects of life that can be budgeted for, we don't know whether we will ever need care and as this interview shows, the financial liability for it can vary enormously according to individual circumstances.

Clive Barwell and Matthew Bell are both Society of Later Life Advisers (SOLLA) accredited advisers and they specialise in financial advice at the latter stages of life. Nick Moules spoke to them about the announcements, their thoughts on the likely impact, what people need to know about paying for later life care and what might come next.

> Unlike other aspects of life that can be budgeted for, we don't know whether we will ever need care...

Nick Moules: What was your reaction when you first saw the news?

Matthew Bell: I think there's an acknowledgement that the Government is looking at a problem that has been around for a long time, but I'm not sure the Government can fund all of that and there is likely to be a further tax burden in future. The Government is saying that when someone's assets drain down to £100,000 the Government will take over, but we will have to wait and see. My view is that there will not be enough funding to satisfy everyone's needs.

Clive Barwell: What I think people are missing is the fact that at the £100,000 'upper threshold', the Tariff Income of £1 a week per £250 will apply, so anyone with £100,000 will be determined to have £320 a week income and as a result of that, their capital will get eroded very quickly.

Someone with just the State Pension would have an income of just under £180 a week, meaning they would be deemed to have an income of virtually £500 a week.

Some local authorities won't pay anything more than £500 for a care home anyway, so your income is sufficient to cover your costs, meaning the local authority won't contribute.

MB: If you look at house values alone, most of our clients will be paying for care for a long time. I see these measures as supporting those with the lowest income and asset levels only.

CB: I'm dealing with a new client now when the person with Power of Attorney has just sold the main property for £1.4m but the care costs are currently £6,000 a month. They've asked whether these announcements change anything for them, and I've said probably not.

NM: In terms of the quality of care itself, it seems to me that it is unlikely to improve. In your experience, what is the real difference between privately funded and state-provided care?

MB: Privately funded healthcare can be very expensive. It depends what you want to do though. If you bring in a live-in carer that can be expensive as they need a room and require a day off a week, for example. You can have someone come in several times a week for example, or you can do residential care, where you live in a facility.

CB: If you're prepared to pay for it, residential care can be top quality. There are plenty of care homes out there with restaurant settings and you end up in what is effectively a suite in a hotel. It can cost several thousands of pounds a week though, so it is seriously expensive.

To contrast the difference between what you get if you pay for it versus what the council provides, a care home local to me in Leeds, the self-funders all live in lovely rooms with en-suite bathrooms and balconies overlooking the gardens. The minute you run out of money, they move you into another wing where you are sharing a bathroom and the rooms are much more basic.

The quality of the care is still there but the facilities changed remarkably.

NM: So, is there any sort of protection that people can put in place for care costs?

CB: Not really. There are some companies who have a care fees option on Whole of Life contracts, so if you fail three activities of daily living, you can claim on that to cover care costs. However, it's very expensive and if you never go into care, you will have paid a significant amount extra in premiums, so I can't see it being attractive. The only thing that's available now is an Immediate Needs Annuity, which can be bought at the time when someone enters care, which caps the cost of it.

I've quoted for lots of these over the years but very few clients have taken it up. My rule of thumb is that whatever the income shortfall is,

The Activities of Daily Living[8]

- Functional mobility, which includes the ability to walk and transfer in and out of a chair or bed. Essentially, it's the ability to move from one place to another as a person goes through their daily routines.
- Personal hygiene, oral care and grooming, including skin and hair care
- Showering and/or bathing
- Toileting, which includes getting on/off toilet and cleaning oneself
- Dressing, which includes selecting appropriate attire and putting it on
- Self-feeding

it will cost you about six years' worth of that shortfall to buy that annuity. If you've got an income shortfall of £50,000 then it will cost you around £300,000 up front to buy the annuity. Clearly if you die two years into that contract, it is poor value for money for your estate.

MB: I find that when I get to the point where I present the numbers, the Powers of Attorney just can't make the decision because they just don't know how long the person is going to live and they're concerned about money being wasted.

CB: There's an each-way bet with a deferred annuity available where you pay the capital up front and you can defer for up to five years, so the cost of the annuity is less because the Insurer is less likely to have to pay up.

These are the only ones clients have taken up recently.

MB: You can build in capital guarantees to some policies. They look good on paper but when they say, for example, you have a 50 percent guarantee if the policy holder dies within a given time period, that means you get 50 percent of the premium back minus whatever has been paid to the care home in that period. Often that can mean the bulk of that money has been used and you pay a premium for the product in the first place, so it can be poor value.

NM: It sounds like there's a real opportunity for businesses to innovate in the market. Do you see it going that way or do you think firms are looking at the open-endedness of the situation and thinking that there's no way to manage their costs?

CB: At the end of the 1990s a few providers came in and created products that would pay out when clients failed three key activities of daily living. The problem with these products is that compared to life insurance for example where people know they're going to die so they take out life insurance for their loved ones, you can't be sure you're going to need care – and you hope you never do.

It's really down to the individual and their health record. For example, if someone has heart problems, there's a chance they will die of that, rather than of old age in a care environment. That isn't meant to sound macabre, it's just the sort of reality that people confront at this stage.

Insurance companies have long memories and I don't think they're going to innovate particularly quickly. The only thing I've heard is that another major insurer might enter the Immediate Needs Annuity market, so that might swell the number of providers.

NM: To paraphrase then, it looks like the biggest issues are that the market is expensive, not really many suitable products and there is no guarantee on the quality of care they will receive. If you speak to clients who are a way off retiring but they say they're concerned about paying for care in the future, what do you say to them?

> "One of my clients actually said it would be cheaper to go on a cruise for the rest of his life, such is the cost of care!"

MB: There's not really a great deal people can do about this until they actually need it. However, it is possible to use trusts to protect assets upon the first death, assuming the couple is married. I know of Will writers who are doing that, but it can be expensive.

One of my clients actually said it would be cheaper to go on a cruise for the rest of his life, such is the cost of care!

CB: If married couples sever the joint tenancy on their property and put trusts in their Wills, this means that on the first death, half of the value of the property goes into trust so cannot be considered for paying the cost of care. Generally speaking, it is only after the first death that care becomes a reality anyway. The person going into care can genuinely say that they only own half the property and it ringfences those assets. Most clients feel that by doing that, they've done enough.

NM: So, what would you say are the biggest issues that clients might not be aware of in the care industry?

CB: I get a bit hot under the collar about Dementia. Where people say the NHS treats physical illnesses, like cancer or heart attacks, that's true to a point but when they've done what they can, they return a patient to the community. Clearly that can't be done with Dementia because it can't be treated effectively. It requires 24-hour care in some cases then that becomes an NHS issue - it's misleading to think of it in terms of the diagnosis, this is about the level of care required.

If someone cannot support themselves then they enter the realms of means-tested care, which can be invasive and inconsistent.

MB: The upshot is if you don't qualify for means-tested care, you need to pay for it yourself and as we have discussed, that can be very expensive.

CB: We also haven't discussed the care cap. The Government has stated that £86,000 is the cap, so once you've spent £86,000 on your care, regardless of any other means-testing considerations, they will pick up the amount of care not covered by your income. The hidden issue with this cap is only based on what the local authority would pay for care. So, if you're paying £2,000 a week for your care and the local authority only pays £600.

Also, the part that hasn't been clarified is the only portion that goes towards it, your £1,400 doesn't.

When they did the original calculations ahead of the Care Act 2014 when the original cap was planned to be introduced, they worked with a national average figure of £200 as accommodation. The Government has now announced that the accommodation figure will be set initially at £200 not £230. So, in this example, only £400 a week (£600 - £200) would count towards the cap and until then, you could spend a fortune.

This will come in from 2023 and anything you've spent on care prior to this point will not count. Until you hit the £86,000 you pay for everything. Clearly this will impact people more in areas of the country where care is more expensive, typically the South of England.

The real issue with this is that every local authority across the country is struggling to administer clients who cannot pay for their care. So, if someone fails the means test (i.e. has more than £23,250), they can't always easily access the care they need from their local authority.

From 2023, every single person is going to need an account with their local authority so they can keep track of the cap. That's going to cost a fortune in administration.

MB: We also have an ageing population, so the problem is only going to get worse.

CB: It is my view that most people will die before they hit the cap to be honest, so while the cap is a backstop of sorts, the way it is constructed will not save people much money if they live for a long time in a care environment.

NM: Okay, if someone doesn't have a financial planner and they're concerned about the cost of care, what can they do?

MB: I find a lot of people ask if they can take their money out and move it about, so for example taking it out of Dad's account and putting it into Mum's. If you're about to go into care you could breach the Deliberate Deprivation Act.

CB: If the need for care is foreseeable and you move assets around to try and avoid them being included in the means test, the local authority will deem that you still have those assets.

If someone cannot support themselves then they enter the realms of means-tested care, which can be invasive and inconsistent.

In a recent case, a lady had qualified for the attendance allowance at the day rate. Lots of people qualify for the day care rate and the local authority decided that the need for care was foreseeable because she had qualified. That's the type of watershed authorities are looking at. Some of my clients are very fit and healthy but they have some care supplied, so any attempt to give money away from here would be regarded by the local authority as deliberate deprivation.

Advisers like Matthew and I can help people to understand what the rules are and what is available to them. A financial planner can sort out estate planning and work as much out as possible in advance of any care being required.

Then from that point, if and when the client goes into care, we can assist with the administration of the estate and advising on the very latest rules.

IMPORTANT: This article is a discussion between experienced practitioners ahead of the planned introduction of the Health and Social Care Levy in April 2022.

Readers should NOT take action as a result of reading this article, except to speak to their adviser.

7 https://www.cityam.com/swelling-nhs-and-social-care-costs-will-force-sunak-to-more-than-double-ni-warns-ifs/
8 https://www.iow.nhs.uk/our-services/community-services/occupational-therapy/Paediatric%20occupational-therapy/Activities%20of%20daily%20living

WHAT'S GOING ON IN THE FINAL SALARY PENSION MARKET?

Financial advisers are accustomed to dealing with unintended consequences of decisions made by those who set policies.

One such area that has garnered more column inches than most is the Final Salary / Defined Benefit (DB) pension scheme market.

One thing everyone agrees on is that these types of pensions, which were commonplace for years, have proved to be unaffordable for the companies or public bodies that offer them, in the long run.

A population that lives for longer needs more money to pay for retirement. A scheme that promises to pay a level of income for the rest of retirement may have a level at which it becomes impossible to meet its commitments. We've seen with the collapse of some schemes (BHS and British Steel for example) that this happens, while other schemes have discovered a 'black hole' in their finances – essentially, there's not enough cash to cover liabilities.

This is where the Pension Protection Fund has stepped in to take over the administration of those schemes.

The rush to transfer

All of this might never have materialised, but for the single biggest change to pension policy for generations. Demand for advice to transfer DB pensions was driven initially by the introduction in April 2015 of 'pension freedoms' which provided for much greater flexibility in the use of defined contribution (DC) pension pots. This growth was reinforced by surging transfer values (primarily reflecting ultra-low interest rates) and a relatively permissive / benign regulatory regime.[9]

Cue a rush for companies with these schemes to de-risk themselves by offering members the opportunity to transfer out for a lump sum.

As is often the case, cracks emerged in the market several years ago, with malpractice coming to light. Clients were given the green light to transfer without proper processes being followed. The highest profile example of this being British Steel, where some scheme members were provided with improper advice.

The regulator acted and banned 'contingent charging' – a practice whereby advice firms offered advice regarding a pension transfer and the client only paid if the recommendation was to proceed. With the transfer, clearly this would wrongly incentivise the firm to recommend a transfer and we have always operated an objective process to determine the advice we give, not influenced by whether there's a fee to charge.

The ban on this activity has led to a reduction in advisers willing to provide advice on transfers from DB pensions because it became unaffordable for some clients to pay for the advice, alongside rises in the professional indemnity insurance premiums required to operate in this market.

Advising on these pensions is a specialism. Wren Sterling invests significantly into technical qualifications and ongoing training for our advisers, as well as the infrastructure to support our advisers, which includes highly qualified business quality monitors and financial modelling software to generate the financial information required to provide advice.

It has also left those with relatively small DB pension pots without a place to turn. It is a legal requirement for the holder of a pot valued at over £30,000 to get financial advice before the scheme will facilitate a transfer. In some cases, the fees for such work eat into the potential value to such an extent that it is pointless.

Why we're committed to the market

Wren Sterling believes that it is our responsibility to help clients evaluate whether a transfer is the best outcome for them. It must be said that in the overwhelming majority of cases, it is not. Very often the benefits of the scheme and the likely impact on a client's quality of life in retirement cannot be bettered by transferring and we recommend that clients remain in the scheme. We provide this advice to individuals and scheme members for some of our corporate clients, sometimes advising hundreds of members in the same exercise.

We've been awarded the Pension Transfer Gold Standard quality mark from the Personal Finance Society. The Gold Standard is a voluntary code of good practice for safeguarded and defined benefit pension transfer advice, based around a set of principles.

We have adopted this standard and principles, so people can be confident they are dealing with a firm that is going beyond minimum requirements when giving financial advice in this area.

Issues for clients:

- Declining choice. In the course of three years, suppliers of DB advice in the market have halved, to around 1,500 firms.
- Difficulty telling apart the good from the bad
- Paying for advice, only to be told it's best to stay in the scheme. This is a difficult message to hear but advisers have to remain impartial
- The cost of advice in this market is more expensive because of the cost of providing the service, including the public liability insurance (PI) premiums required to operate
- An increasing prevalence and sophistication of pension scams means individuals can receive many unwanted approaches, challenging trust in the industry

IMPORTANT: Accessing pension benefits early is not suitable for everyone and may affect your entitlement to certain means tested benefits. When investing your capital as at risk.

9 "Mind the transfer advice gap?"- A joint paper from LCP and Aviva on the current state of the DB transfer market, September 2021

THE FUTURE OF **DB PENSIONS:**

with Paul Chafer, Wren Sterling's Chief Commercial Officer

MM: What will the recent changes to charges mean for DB pension holders in the future?

Paul Chafer: Irrespective of pensions freedoms and other legislative changes, or the number of IFAs providing advice – people need this advice. Your DB pension could be worth as much as your home and may be the largest asset to consider when planning your retirement income.

This is why the Pension Transfer Gold Standard is so helpful, as it signposts which advisers are able to provide this advice and have committed to excellence in this area. Clients can also look at how many clients an adviser has supported, and what they have to say. At Wren Sterling, we have supported a number of large corporates with Defined Benefit Transfer advice for their employees.

We're going to see increasing demand as there's still a lot of people in final salary schemes, against reducing supply of advice. Recently the regulator said that firms must demonstrate value for money and make it frictionless for customers to enter and exit products.

MM: What does that mean for Wren Sterling?

PC: I think we always challenge ourselves to think 'are we providing value for money to clients?' After all, if we didn't give value for money, our clients will quickly go elsewhere! A number of large corporates look to us to support their employees with regular advice programmes. To do so, we employ top class advisers, and a supporting team of Paraplanners and Administrators. We acknowledge that advice isn't cheap, but I do believe we provide value for money – and always have the customers' interests at heart.

MM: What about those with smaller pots?

PC: Anyone under £30k can transfer away without needing advice. Self-administering can have its own challenges as few people will be used to filling in pensions paperwork. The process is the same whether your pension is worth £30,000, £300,000 or £30,000,000!

MM: Do you anticipate it being harder for a client to transfer their DB pension?

PC: Where transferring is right for the client, and they find a qualified adviser, I don't think it will be any more difficult. Where it's not right for the client, they'll find difficulties in transferring – but you could argue that's not a bad outcome. There will always be clients who want to transfer because they've seen a friend or family member transfer recently – but it won't be the right decision for them and could leave them worse off.

If I say to you "you shouldn't transfer your pension – because you can get what you need in the happy environment of a safeguarded

pension" but I then help you fill out the forms for this, I would be found wanting from an ethical standpoint.

There may be the option to do a 'partial transfer'. This hasn't always been possible, and is quite rare, but I think it will increase over time.

MM: What is a partial transfer? Could this help people who need a bit more flexibility in a DB pension?

PC: If you have a DB pension, you are usually facing a binary decision; to transfer or not to transfer. Let's say you need to downsize or make changes to your home, but a full transfer isn't recommended. With a partial transfer, you could supplement your income by taking a portion of your DB pension. This could leave you a comfortable level of income in retirement, and the flexibility to do what you need to do with the remaining pot.

I think partial transfers will help with immediate needs, and will help manage emotions around your retirement because you'll need to rely on these funds. For some, even if a transfer is the right decision, clients are hesitant to transfer away. Particularly for people who are quite risk averse, or only have their DB pension as their source of retirement income, a partial transfer would allow you to mitigate that risk.

Your DB pension could be worth as much as your home and may be the largest asset to consider when planning your retirement income.

However, only around 1 in 5 schemes currently offers partial transfers. The difficulty is the demand on the Scheme Administrators so at the moment, there are two choices, stay or transfer. I can see this changing as more people begin to see the benefits of a partial transfer and administrators find a way to offer it to members. As technology improves for example, I do think we will see more schemes offering partial transfers.

IMPORTANT: Accessing pension benefits early is not suitable for everyone and may affect your entitlement to certain means tested benefits. When investing your capital as at risk.

About Wren Sterling

Wren Sterling is a nationwide independent financial planning business that specialises in all aspects of investments, protection, and retirement planning. We pride ourselves on navigating clients through their financial journey by providing uncompromised and objective advice.

Our advisers are committed to developing longstanding client relationships that span generations to achieve our clients' lifetime financial goals.

Where we are

We have advisers throughout the UK, based in seven regional offices including our head office in Nottingham.

- Glasgow 0141 341 5240
- Halifax 0333 0438 900
- Nottingham 0115 908 2500
- Warwick 0333 043 9001
- Grantham 01476 560 662
- London 0370 1432 100
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