Retirement Planning – A Decumulation Strategy

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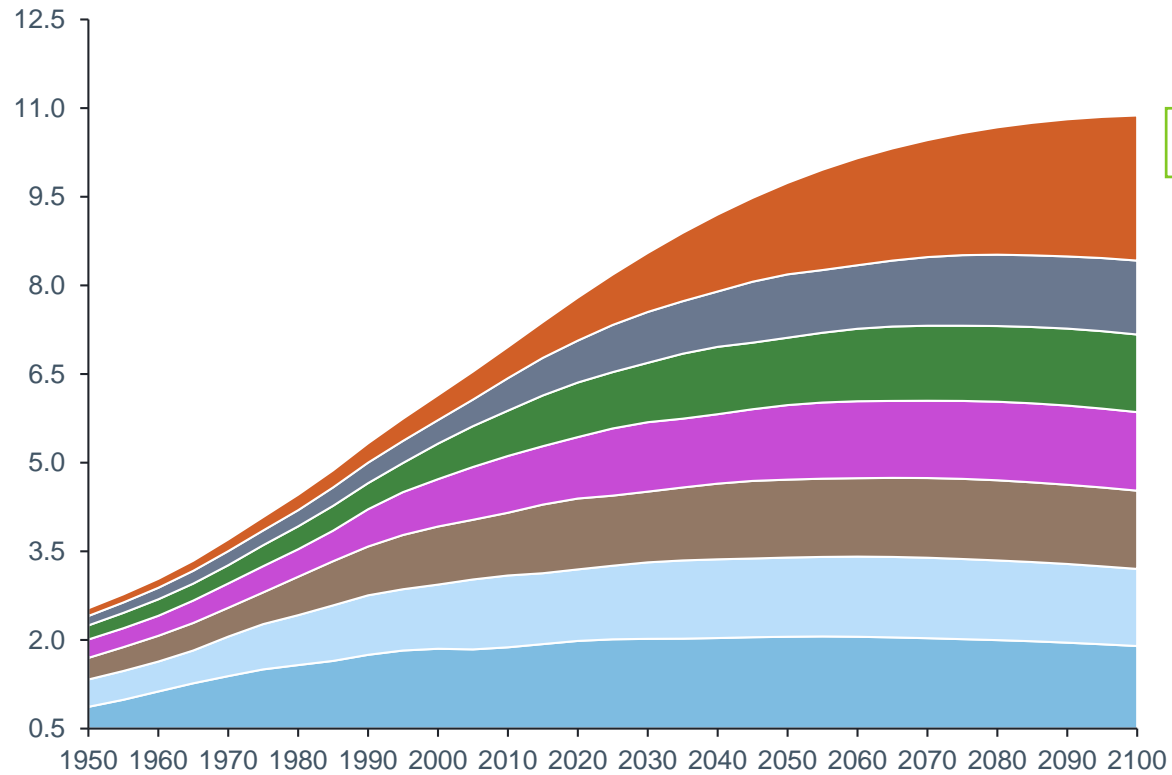
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The world population is aging

Demand for retirement solutions will continue to rise

World population (in billions)

	By 2050, the 65+ population is expected to double		
	2015	**2050**	**CAGR**
65+	**8%** →	**16%**	**2.7%**
55-64	9%	11%	1.5%
45-54	12%	12%	0.8%
35-44	13%	13%	0.7%
25-34	16%	14%	0.4%
15-24	16%	14%	0.3%
Under 14	26%	21%	0.2%

The world is going grey

Source: Fidelity International, United Nations World Population Prospects 2019 https://population.un.org/wpp/Download/Standard/Population/.
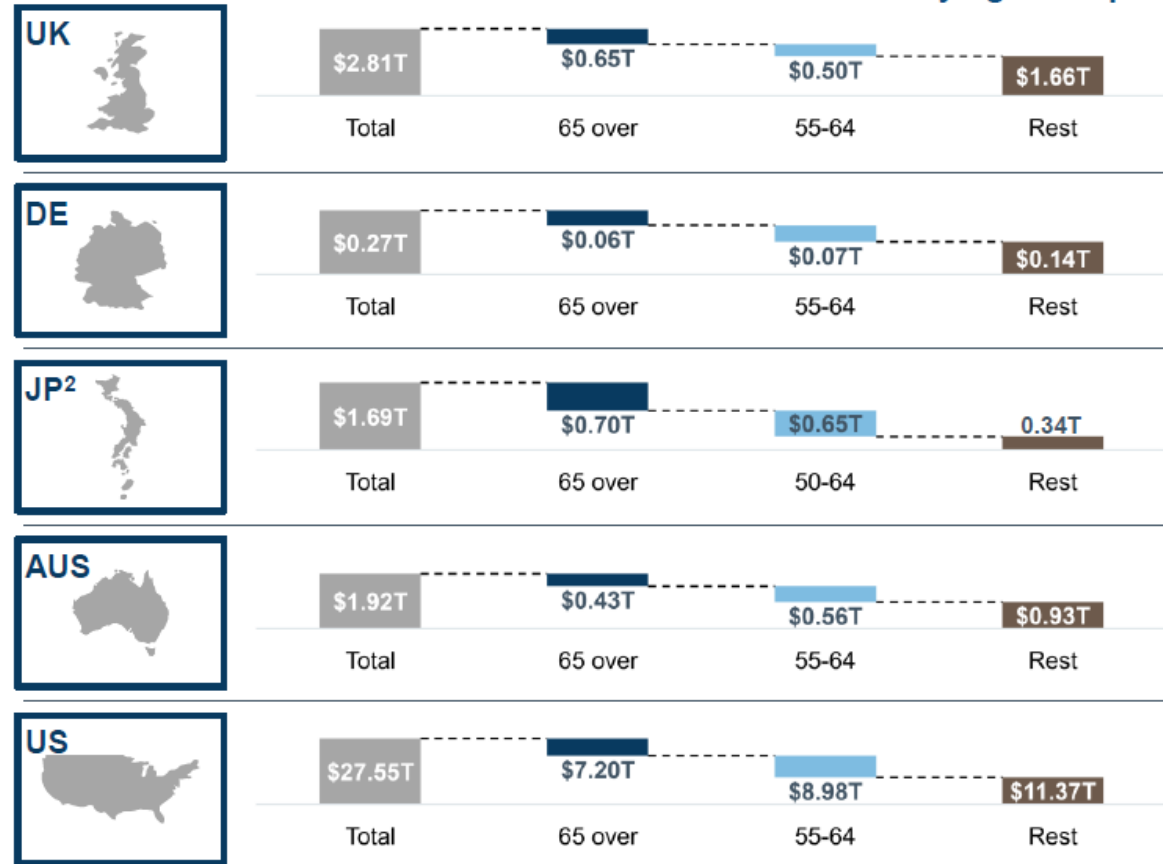
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As a result, assets in retirement present significant opportunity

With additional assets reaching retirement in coming years
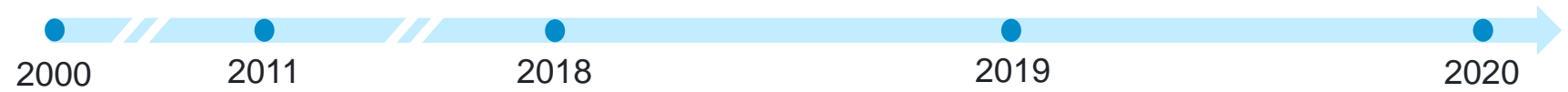

~$43T (USD)
Private Pension Assets[1]
Globally

Estimated Breakdown of Pension Assets by Age Group

UK

$2.81T	$0.65T	$0.50T	$1.66T
Total	65 over	55-64	Rest

DE

$0.27T	$0.06T	$0.07T	$0.14T
Total	65 over	55-64	Rest

JP[2]

$1.69T	$0.70T	$0.65T	0.34T
Total	65 over	50-64	Rest

AUS

$1.92T	$0.43T	$0.56T	$0.93T
Total	65 over	55-64	Rest

US

$27.55T	$7.20T	$8.98T	$11.37T
Total	65 over	55-64	Rest

Government initiatives encourage retirement planning

2000	2011	2018	2019	2020

	Product	**Incentives**
Protection	• Government-certified hospital insurance plans under Voluntary Health Insurance Scheme (VHIS) (2019)	Tax deductions for VHIS (2019)
Income	• HKMC Reverse Mortgage Programme (2011) • HKMC Annuity Plan (2018) • Qualifying Deferred Annuity Policy (2019)	Tax deductions for Qualifying Annuity Premiums (2019)
Growth	• MPF investment funds (2000)	Tax deductible MPF Voluntary Contributions (2019)

Source: Fidelity International, 2020.

A stylized retirement journey
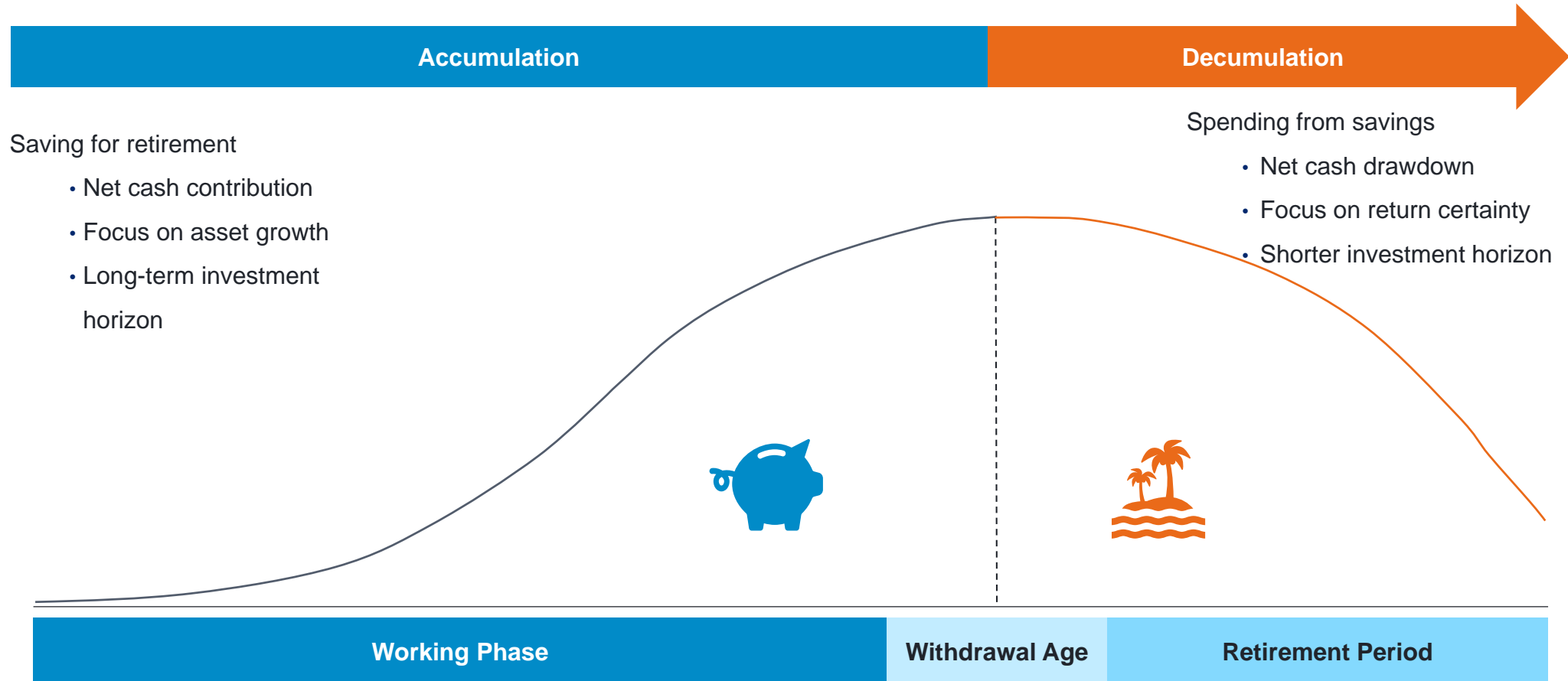
Accumulation

Decumulation

Saving for retirement

- Net cash contribution
- Focus on asset growth
- Long-term investment horizon

Spending from savings

- Net cash drawdown
- Focus on return certainty
- Shorter investment horizon

Working Phase

Withdrawal Age

Retirement Period

Source: Fidelity International, 2020. For illustrative purpose only

What does end customers need for decumulation?

"This is where you invest for recurring income to sustain a living. So it has to be stable and low risk."

"It's always good to have more investment options for us so that we can make better use of our MPF funds."

"As you retire you tend to slow down, you don't want to spend so much time monitoring how much you could get each month, or when to trade. You just want things to be simpler so that you can relax."

"Annuity is for those who are not interested in investment and don't want the effort in monitoring the market. It just feels better than putting the money at the bank (fixed deposit) in terms of return."

Source: Fidelity International, 2020. For illustrative purpose only

What does end customers need for decumulation?

Depending on the market, some of the needs may be more pronounced

People generally don't have a good idea on how much they need to cover necessities and essentials in retirement

Proportion of Income Spend on Living Expenses[1]

~15%

Expected: 34%
Actual: 49%

Non-Retired
Retired

Worried about paying for basic necessities at some point in retirement[3]

Men: 47%
Women: 51%

People want to pursue their personal interests and stay engaged in retirement

Priorities in Retirement[2]

72% Leisure-Related

14% — Hobbies
15% — Ent. & Exc.
21% — Travel
22% — Family Time

Look forward to pursuing hobbies & interest in retirement[3]

Men: 73%
Women: 78%

People think about health care and their legacy

Expected Capital Allocation in Retirement[1]

17% Healthcare
9% Inheritance
6% Support Family
32%

Worried about not being able to cover medical or care expense in retirement[3]
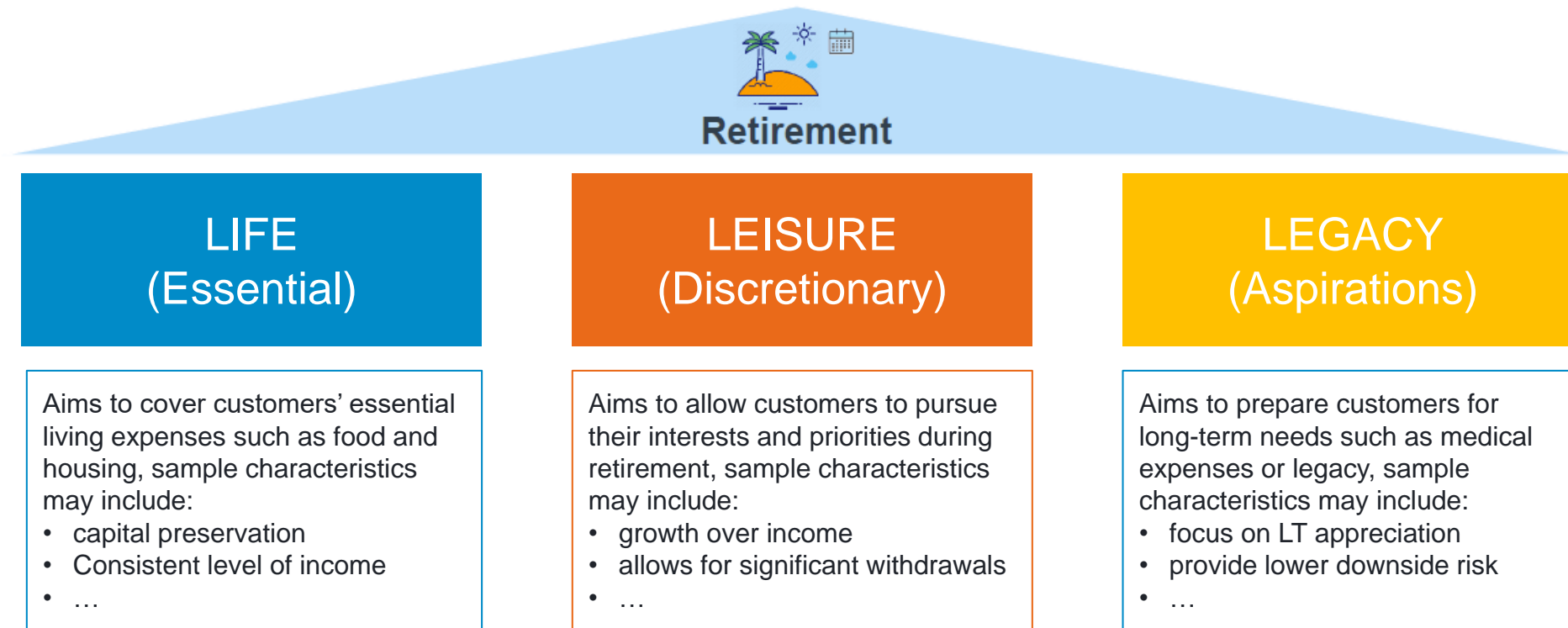
Men: 55%
Women: 60%

Notes: 1) both retired and non-retired populations, n = 22,000 across 30 countries; 2) U.K., n= 10,000; 3) Working age men and women, n = 17,405 across 16 countries;
Source: "Global Investor Study 2018 – Saving for a Comfortable Retirement" – Schroders; "Future of Retirement – Global Factsheet 2018" – HSBC; "Great British Retirement Survey" - Interactive Investor; Fidelity International, 2020
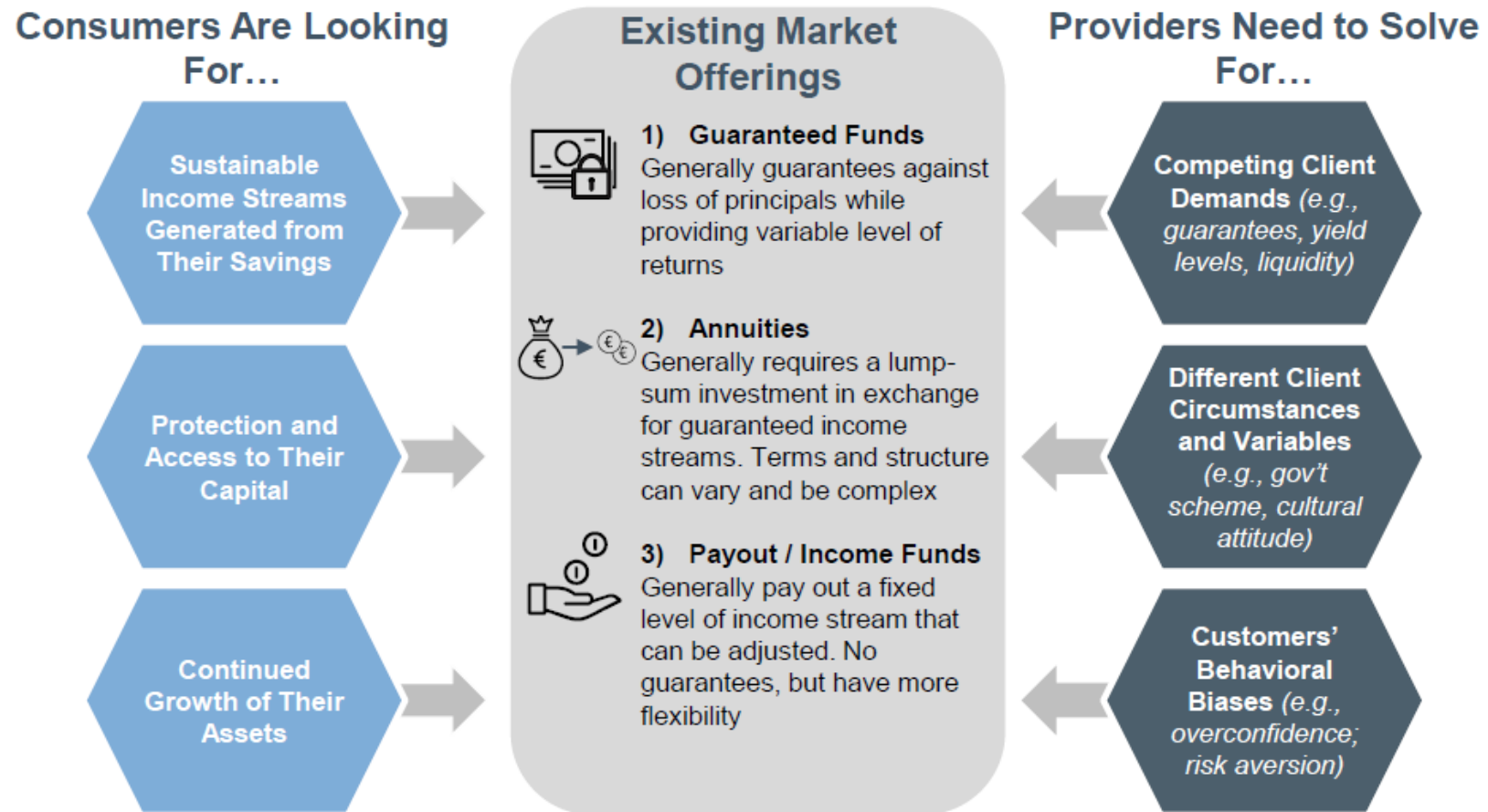
How to achieve the desired outcome

Break down decumulation into distinct, goal-oriented constructs

Retirement

LIFE (Essential)	LEISURE (Discretionary)	LEGACY (Aspirations)
Aims to cover customers' essential living expenses such as food and housing, sample characteristics may include: • capital preservation • Consistent level of income • …	Aims to allow customers to pursue their interests and priorities during retirement, sample characteristics may include: • growth over income • allows for significant withdrawals • …	Aims to prepare customers for long-term needs such as medical expenses or legacy, sample characteristics may include: • focus on LT appreciation • provide lower downside risk • …

Source: Fidelity International, 2020

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How to achieve the desired outcome

Current market landscape

Consumers Are Looking For…

- Sustainable Income Streams Generated from Their Savings
- Protection and Access to Their Capital
- Continued Growth of Their Assets

Existing Market Offerings

1) **Guaranteed Funds**
Generally guarantees against loss of principals while providing variable level of returns

2) **Annuities**
Generally requires a lump-sum investment in exchange for guaranteed income streams. Terms and structure can vary and be complex

3) **Payout / Income Funds**
Generally pay out a fixed level of income stream that can be adjusted. No guarantees, but have more flexibility

Providers Need to Solve For…

- **Competing Client Demands** (e.g., guarantees, yield levels, liquidity)
- **Different Client Circumstances and Variables** (e.g., gov't scheme, cultural attitude)
- **Customers' Behavioral Biases** (e.g., overconfidence; risk aversion)

Source: Fidelity International, 2020

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A few things to consider

Longevity

People expect to live another 20+ years post retirement

Life Expectancy at Birth (Male and Female), 1971 - 2019
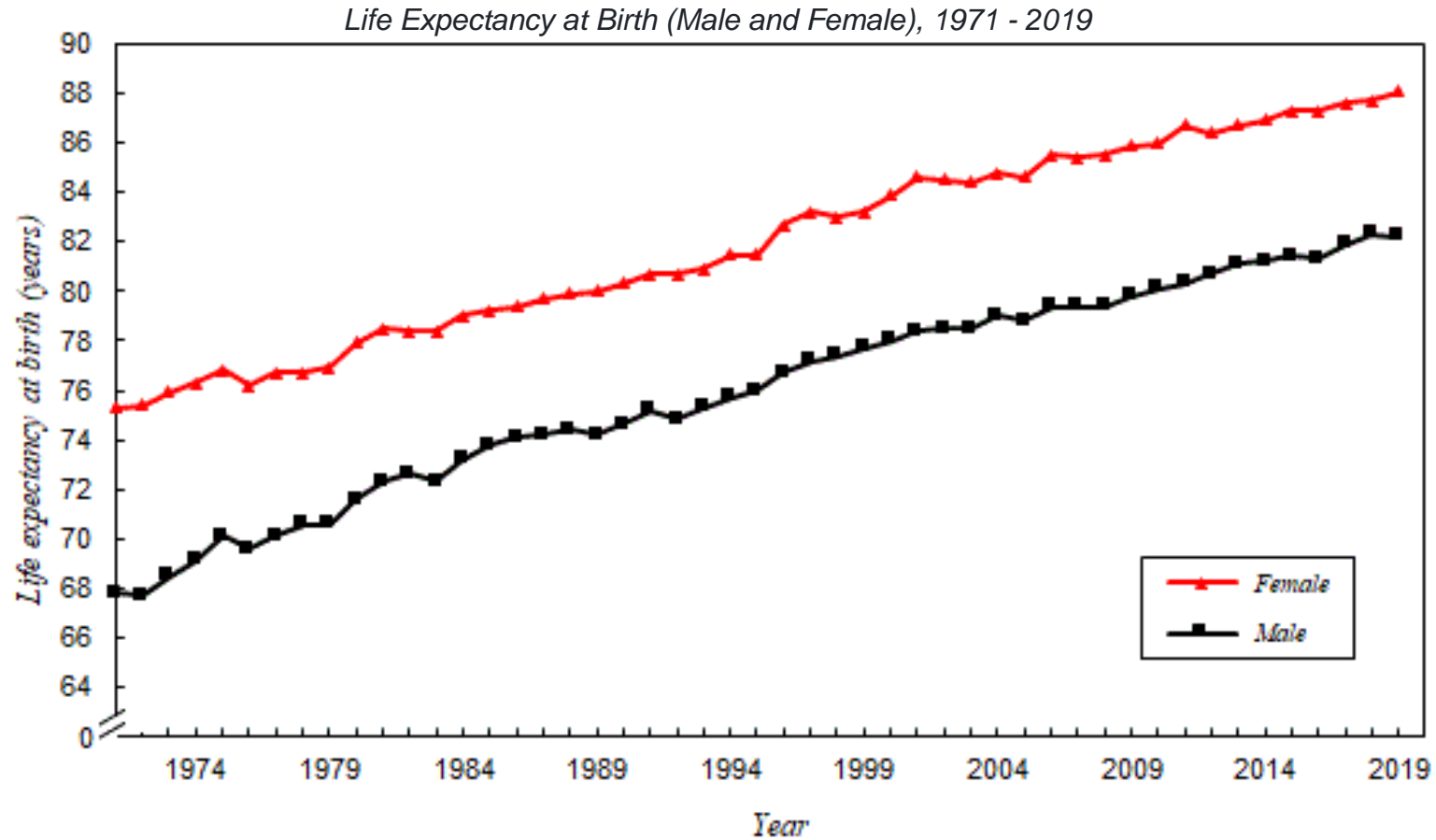
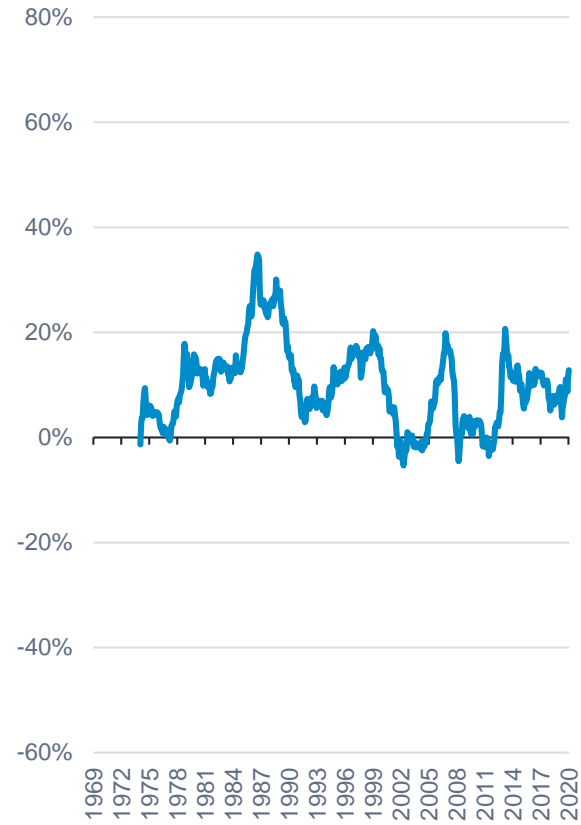Source: Census and Statistics Department, The government of HKSAR, 2019.

A few things to consider

Investment horizon

Rolling 1-year total return of global equities

Rolling 5-year annualised total return of global equities

Rolling 10-year annualised total return of global equities

Source: Fidelity International, Refinitiv Datastream, as of 12/31/2020, Global equity is proxied with MSCI World Total Return Index.

A few things to consider

Preserve purchasing power

In the current low yield environment, bond yields alone are not sufficient to cover inflation

Source: Fidelity International, Refinitiv Datastream, as of 12/31/2020. HK inflation forecast based on IMF World Economic Outlook Database October 2020. DM equity is proxied with MSCI World index, EM equity is proxied with MSCI Emerging Market index, Greater China equity is proxied with MSCI Golden Dragon index, global government bond is proxied with ICE BofA Global Government Bond Index, global corporate bond is proxied with ICE BofA Global Corporate Bond index, Asia Investment Grade Dollar Bond is proxied with ICE BofA Asia Investment Grade Dollar Bond Index.
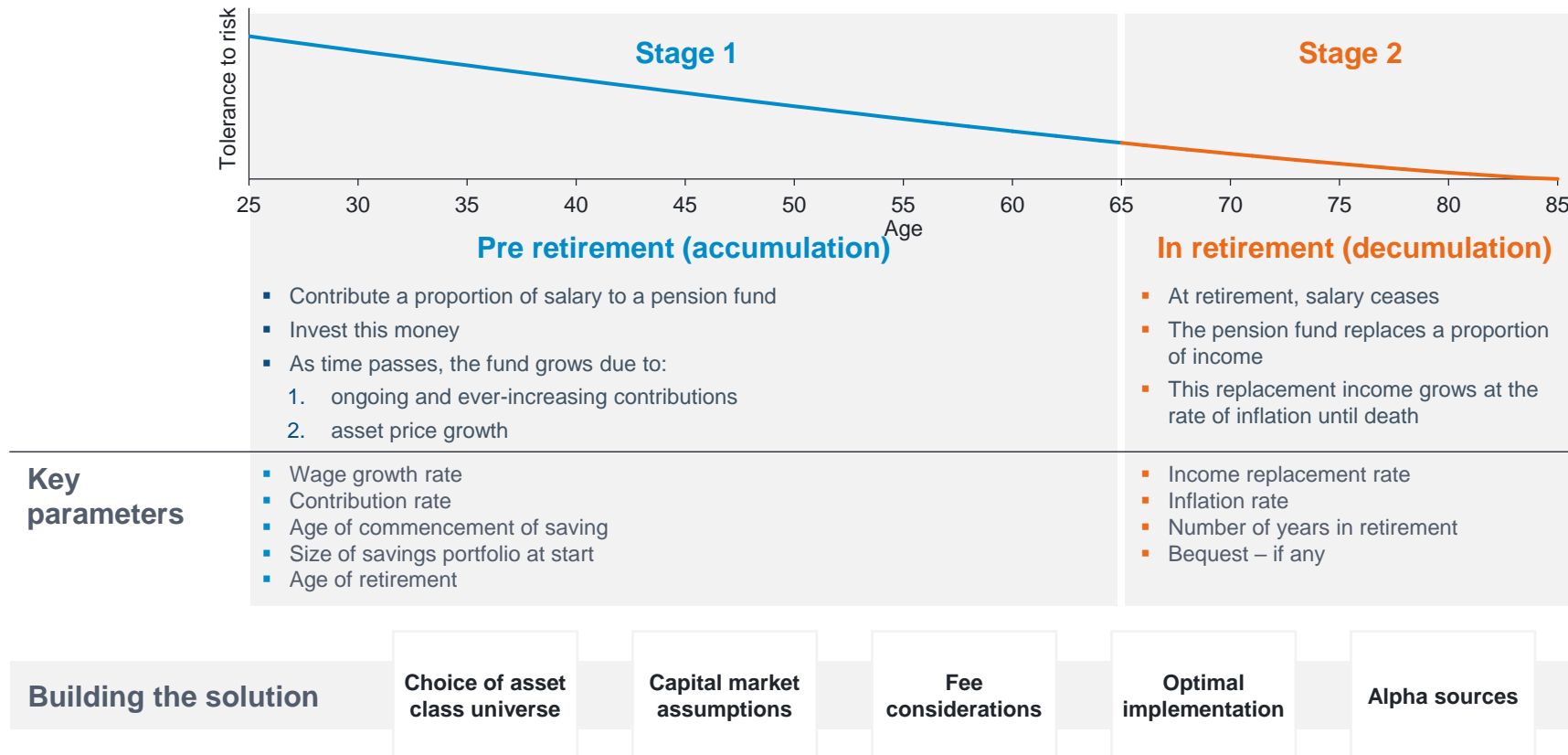
A few things to consider

Diversification

Calendar year return of major asset classes

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
China Equity 66.7%	US 10Y Govt. 21.2%	EM Equity 62.8%	REITS 31.3%	US 10Y Govt. 16.9%	China Equity 22.9%	US Equity 32.6%	REITS 40.5%	REITS 12.8%	Global HY 14.8%	China Equity 55.3%	EM LC 4.9%	US Equity 31.6%	China Equity 28.3%
EM Equity 33.6%	EM LC 10.2%	China Equity 62.7%	Gold 29.3%	Gold 11.1%	REITS 21.0%	World ex US Equity 21.6%	US Equity 13.4%	EM LC 3.4%	US Equity 11.6%	EM Equity 31.0%	Cash 1.0%	REITS 26.9%	Gold 24.8%
Gold 31.8%	Gold 3.1%	Global HY 62.0%	US Equity 15.4%	EM HC 7.3%	Global HY 19.3%	Global HY 8.0%	US 10Y Govt. 10.9%	US Equity 1.3%	EM LC 10.6%	World ex US Equity 24.8%	REITS 0.3%	China Equity 23.3%	US Equity 21.4%
World ex US Equity 12.9%	Cash -2.5%	World ex US Equity 34.4%	EM Equity 14.4%	EM LC 6.4%	EM HC 17.4%	China Equity 4.0%	EM LC 8.7%	EM HC 1.2%	EM HC 10.2%	US Equity 21.9%	US 10Y Govt. -0.1%	World ex US Equity 23.2%	EM Equity 19.5%
US 10Y Govt. 9.6%	Global Corporate -4.7%	EM HC 29.8%	Global HY 13.9%	REITS 6.0%	EM Equity 17.4%	EM Equity 3.8%	China Equity 8.3%	US 10Y Govt. 1.0%	EM Equity 10.1%	Gold 12.6%	Global Corporate -1.7%	Gold 18.7%	US 10Y Govt. 12.6%
EM HC 6.2%	EM HC -12.0%	REITS 28.4%	EM HC 12.2%	Global Corporate 5.2%	World ex US Equity 17.0%	EM LC 0.9%	Global Corporate 7.8%	Cash -0.2%	REITS 9.6%	EM HC 10.3%	Gold -1.7%	EM Equity 18.5%	World ex US Equity 8.1%
US Equity 6.0%	Global HY -27.9%	US Equity 27.1%	EM LC 9.7%	Global HY 2.6%	US Equity 16.1%	Global Corporate 0.1%	EM HC 7.4%	Global Corporate -0.2%	Gold 9.0%	Global HY 10.2%	Global HY -3.3%	EM HC 15.0%	Global HY 8.0%
EM LC 5.5%	US Equity -37.1%	Gold 27.1%	World ex US Equity 9.4%	US Equity 2.0%	EM LC 14.1%	Cash -0.2%	EM Equity 5.6%	World ex US Equity -2.6%	Global Corporate 5.7%	EM LC 9.8%	EM HC -4.3%	Global HY 13.7%	Global Corporate 7.7%
Global HY 3.1%	REITS -41.7%	Global Corporate 16.3%	US 10Y Govt. 8.6%	Cash -0.8%	Global Corporate 10.8%	REITS -1.8%	Global HY -0.1%	Global HY -4.2%	World ex US Equity 3.3%	Global Corporate 5.2%	US Equity -4.5%	EM LC 12.9%	EM LC 7.5%
Global Corporate 2.6%	World ex US Equity -43.2%	EM LC 6.7%	Global Corporate 7.4%	World ex US Equity -11.8%	Gold 5.6%	EM HC -5.3%	Cash -0.2%	EM Equity -5.4%	China Equity 1.2%	US 10Y Govt. 2.1%	EM Equity -9.7%	Global Corporate 11.5%	EM HC 5.3%
Cash 0.8%	EM Equity -45.7%	Cash -3.5%	China Equity 5.1%	EM Equity -12.5%	US 10Y Govt. 4.3%	US 10Y Govt. -7.6%	Gold -1.8%	China Equity -7.7%	US 10Y Govt. 0.9%	Cash 0.1%	World ex US Equity -13.6%	US 10Y Govt. 9.5%	Cash -1.8%
REITS -21.0%	China Equity -51.1%	US 10Y Govt. -9.4%	Cash -1.6%	China Equity -18.3%	Cash -0.5%	Gold -27.3%	World ex US Equity -3.9%	Gold -10.4%	Cash -0.1%	REITS -5.4%	China Equity -18.6%	Cash 0.8%	REITS -17.5%

Source: Fidelity International, Refinitiv Datastream, 2021. US equity is proxied with MSCI USA index, China equity is proxied with MSCI China index, World ex US equity is proxied with MSCI World ex US index, EM equity is proxied with MSCI Emerging Market index, US 10-year is proxied with US Benchmark 10 year DS government index, Global corporate is proxied with ICE BofA Global Corporate index, Global high yield is proxied with ICE BofA Global High Yield index, EMD HC is proxied with JPM EMBI Global Diversified index, EMD LC is proxied with JPM GBI EM index, Cash is proxied with ICE BofA 3-month US treasury note index, Gold is calculated using gold bullion LBM price.
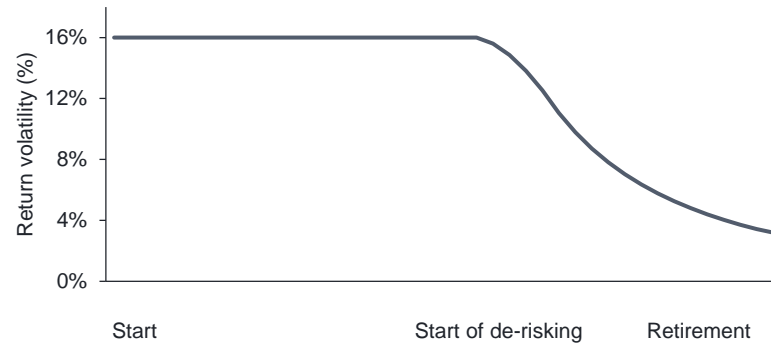
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A mathematical framework to model the retirement journey

Stage 1   **Stage 2**

Tolerance to risk — Age (25 to 85)

Pre retirement (accumulation)

- Contribute a proportion of salary to a pension fund
- Invest this money
- As time passes, the fund grows due to:
  1. ongoing and ever-increasing contributions
  2. asset price growth

In retirement (decumulation)

- At retirement, salary ceases
- The pension fund replaces a proportion of income
- This replacement income grows at the rate of inflation until death

Key parameters

- Wage growth rate
- Contribution rate
- Age of commencement of saving
- Size of savings portfolio at start
- Age of retirement

- Income replacement rate
- Inflation rate
- Number of years in retirement
- Bequest – if any

Building the solution

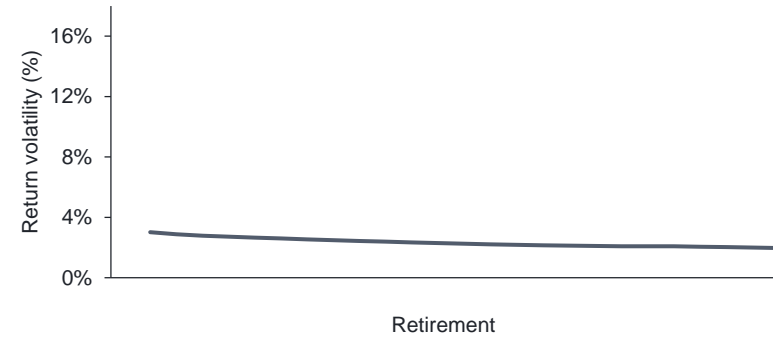| Choice of asset class universe | Capital market assumptions | Fee considerations | Optimal implementation | Alpha sources |

Source: Fidelity International, 2020

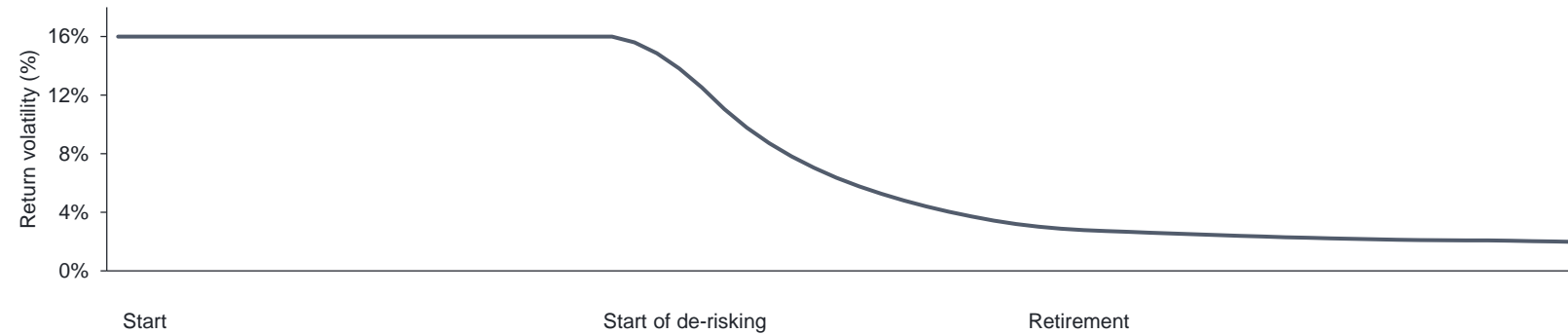# Accommodate various part of the retirement needs

Accumulation only ("to retirement")

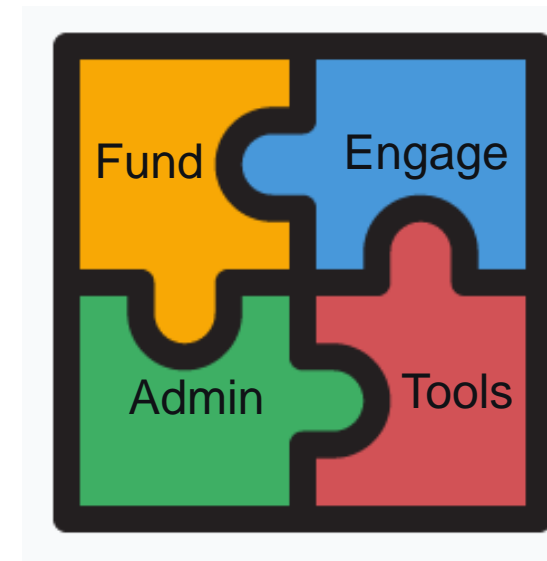**Decumulation only ("in retirement")**

Both ("to and through retirement")

> **A unified and consistent framework for the entire retirement journey**

Source: Fidelity International, 2020. For illustrative purposes only

A decumulation solution should help people to live the retirement life easily

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