

Fidelity

RETIREMENT INDICES

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TABLE OF CONTENTS

Page 1: Introduction

The retirement challenge

Page 2: Index Definitions

What each index shows

Page 3-4: Results and Key Findings

Interpreting the results

Page 5: Geographical Breakdown

Results for the UK regions

Page 6: Summary

Improving retirement readiness



INTRODUCTION

Simon Fraser,
President, Fidelity Institutional Business

It is widely accepted that the UK is facing a pensions crisis, but there are still many unanswered questions about exactly how it will affect us all. What sort of lifestyle are people hoping for in retirement? How much income can they realistically expect to have? Are they on track to meet their expectations? Are people in the South of England in a better position than those in the North? Does the type of pension scheme people have make a real difference?

In an effort to throw some light on these difficult questions, Fidelity International has undertaken an extensive research project. More than 1,100 people of working age, from all walks of life and from across the UK, told us about their hopes and plans for life after full-time work. From this data, Fidelity has built a set of retirement indices – snapshots of the nation's retirement prospects.

The Fidelity Retirement Indices do not paint a cheery picture. Our research indicates that the average Briton's retirement income will be significantly less than the two thirds that the Pension Commission's proposals seek to enable the average worker to achieve. They will have to get by on just 42% of what they were earning before they retired.

Fidelity also found that people had unrealistic expectations for retirement.

They overestimated how much income their savings could generate and were hoping for a standard of living well above what they were on track to be able to afford.

In addition, the Fidelity Retirement Indices quantify – for the first time – the stark differences between members of defined benefit and defined contribution pension schemes and make regional, gender and generational comparisons that highlight where the real problems lie.

Fidelity International will update the Retirement Indices once a year.

Index Definitions

The Fidelity Retirement Indices use public and private data to build a picture of the typical UK household's retirement prospects. Information on pension and savings arrangements, projections of their state benefits and their nominated retirement dates are all included in the calculations.

By putting this data through sophisticated computer models, it is possible to estimate the level of retirement income for the average household. This estimate is then compared with a range of targets.

FIGURE 1: DEFINITIONS OF EACH INDEX

**THE FIDELITY
RETIREMENT
INDEX**

Provides a snapshot of the typical household's retirement readiness. It shows how much people will receive in retirement, expressed as a percentage of the amount they are likely to be earning just before they retire.

A high figure illustrates a high degree of "replacement income" in retirement.

**THE FIDELITY
RETIREMENT
EXPECTATION
INDEX**

Measures a household's retirement prospects against what people expect their savings and benefit entitlements to generate. Respondents were asked to say how much income they expected to have in retirement, as a proportion of the amount they are likely to be earning just before they retire. This number was then compared with what their savings are likely to produce.

A high figure illustrates that people have a realistic expectation of their retirement income.

**THE FIDELITY
RETIREMENT
SATISFACTION
INDEX**

Provides a gauge of a household's retirement prospects against what they think they need to enjoy a comfortable retirement. People were asked to say how much they would need in retirement, as a proportion of the amount they are likely to be earning just before they retire. This number was then compared with what their savings are likely to produce.

A high percentage figure indicates a high likelihood that people will achieve a retirement income that is in line with their goals.

Results & Key Findings

RESULTS & KEY FINDINGS

The results for the three indices are displayed in Figure 2.

FIGURE 2:

Fidelity Retirement Index	Fidelity Retirement Expectation Index	Fidelity Retirement Satisfaction Index
42%	66%	53%

The first index – the Fidelity Retirement Index – is the broadest measure of people’s retirement prospects, showing how much income they can expect when they stop working full-time, as a proportion of the amount they are likely to be earning just before they retire. On current trends, the average household is on track for just 42%, far below the two thirds that the Pension Commission’s proposals seek to enable the average worker to achieve.

What does this mean in practice? Take the case of someone who is currently earning the national average salary of £22,900 (source: ONS, 2004/05 tax year) and is about to retire. The Fidelity Retirement Index suggests he or she will have an annual retirement income of £9,618. This is equivalent to a weekly gross income of £185 – less than £30 a day.

Part of the problem is that people have unrealistic expectations for their retirement

income. The second index – the Fidelity Retirement Expectation Index – shows that the average household will only generate 66% of the retirement income they expect to produce. Quite clearly there is a gap between reality and belief – the retirement illusion.

A similar picture of unrealistic expectations emerges from the third index, the Fidelity Retirement Satisfaction Index. This looks at how satisfied people are likely to be with their post-retirement income. It compares the income they are likely to have after they retire with the amount they think they will need. The result is expressed as a percentage. A high percentage indicates a high satisfaction rating – an income that is close to what is required. Unfortunately, the income that the typical UK household receives in retirement is likely to be only half as much as they think they will need.

RESULTS SPLIT BY LIFE STAGE

As Figure 3 shows, results for all three indices vary dramatically when spilt by age. Perhaps not surprisingly, retirement readiness and satisfaction increase with age.

The over-55s are, on average, on track for nearly 60% of their forecast final earnings, compared with a replacement rate of just 39% for those aged under 35. Yet even the older generation, while they have more realistic expectations about their savings, are still only on course for 63% of the retirement income they think they will need.

FIGURE 3:

Age	Fidelity Retirement Index	Fidelity Retirement Expectation Index	Fidelity Retirement Satisfaction Index
<35	39%	62%	50%
35-54	44%	67%	54%
55+	58%	77%	63%

Results & Key Findings

RESULTS SPLIT BY GENDER

The Fidelity Retirement Index also shows a disparity in the results for men and women. The average woman in the UK is only on course for 40% of her forecast final earnings, compared with 47% for the average man.

FIGURE 4:

	Fidelity Retirement Index
Women	40%
Men	47%

RESULTS SPLIT BY DIFFERENT TYPES OF PENSION SCHEME

Until now, no-one has been able to quantify the disparity in retirement readiness between workers on defined benefit and defined contribution pension schemes. The results from the Fidelity Retirement Indices, shown in Figure 5, vary considerably according to the type of pension scheme people belong to. Retirement readiness, expectation and satisfaction are much higher for those in defined benefit schemes than

they are for members of defined contribution schemes.

Significantly, the replacement ratio for members of defined contribution schemes is highly sensitive to the level of employer contributions. As can be seen in Figure 6, people who benefit from employer contributions are in a much better position than those who do not.

FIGURE 5:

	Fidelity Retirement Index	Fidelity Retirement Expectation Index	Fidelity Retirement Satisfaction Index
Defined benefit	81%	91%	82%
Defined contribution	38%	65%	51%

FIGURE 6:

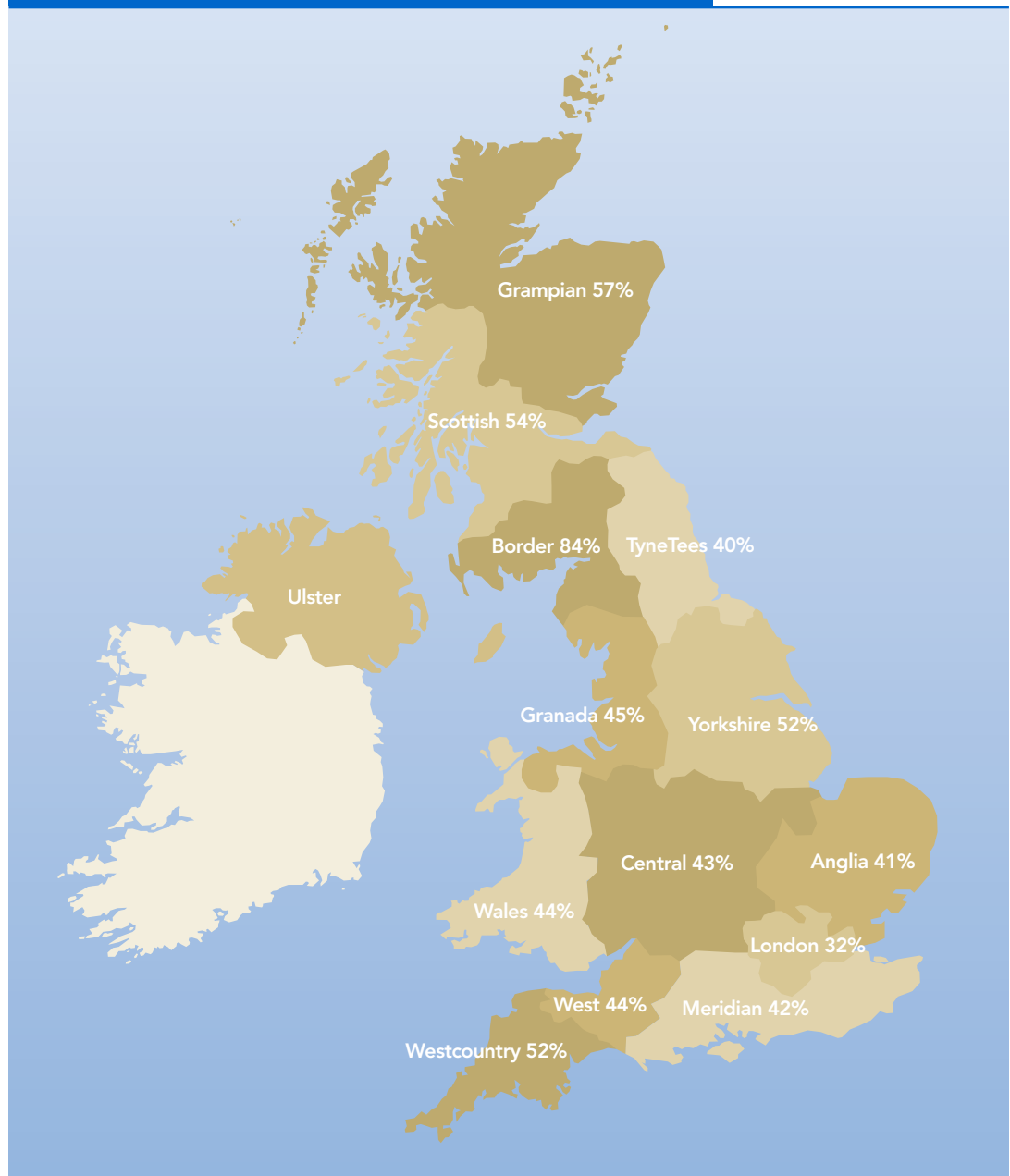
	Fidelity Retirement Index
Defined contribution schemes with employer contributions	51%
Defined contribution schemes without employer contributions	35%

Geographical Breakdown

Figure 7 shows how well prepared people in different parts of the country are for retirement. Those in the Border ITV region appear to be leading the way, with a replacement rate of

more than 80%. Perhaps surprisingly, the average Londoner is only on course to replace 32% of their forecast pre-retirement income.

FIGURE 7: FIDELITY RETIREMENT INDEX SPLIT BY REGION



The regions above represent the UK's TV regions. The regional split for the Ulster region is not available.

Conclusion

IMPROVING RETIREMENT READINESS

The results from the Fidelity Retirement Indices are unambiguous. Firstly, they confirm that the general level of retirement readiness in the UK is very low. There is also a high level of retirement illusion – our research indicates that people dramatically overestimate the true value of their retirement savings. What's more, there is a satisfaction time bomb ticking as, on average, people will only achieve half the level of income in retirement that they would like. Unless people do more to prepare themselves for retirement, few are going to be able to continue enjoying their current lifestyle when they stop working.

Beneath the top-level results there is clear evidence of the "haves" and the "have nots". Members of defined benefit pension schemes are much better prepared and much more likely to achieve a satisfactory retirement. It is perhaps a consequence of this that older pre-retirees are also better prepared.

Younger people and members of defined contribution pension schemes lag behind. Clearly, employer contributions play a vital role in the success or otherwise of these schemes. However, just as important is the role of individuals in taking an active role in managing their pensions themselves to avoid disappointment.

FIDELITY INTERNATIONAL

Fidelity International is the largest mutual fund management company in the UK and manages £85 billion in retirement assets*. The company manages over 300 UK defined contribution pension plans as well as £20 billion in defined benefit schemes for 385 corporate clients.

NOTES TO EDITORS ABOUT THE RESEARCH METHODOLOGY

The survey was conducted on behalf of the Fidelity Retirement Institute by NOP. It included 1,141 people from all parts of the UK. The respondents are in work and are not yet retired. They are also the financial decision makers in their household. Interviews were completed in February 2006.

The Fidelity Retirement Indices were calculated by Towers Perrin using a method, known as stochastic modelling, which examined hundreds of different investment scenarios for each of the people surveyed.

The Fidelity Retirement Index represents the median (or mid point) of the results produced. The Fidelity Retirement Expectation Index and the Fidelity Retirement Satisfaction Index represents the average of the results produced where the underlying data was capped at 100%.

Projections of future incomes are based on the following assumptions:

- pre-retirement earnings will rise in line with National Average Earnings (currently 3.6%)
- retirement incomes include a full state pension
- the Basic State Pension will rise in line with increases in the Retail Price Index
- payments from SERPS and State Second Pension will rise in line with National Average Earnings (currently 3.6%)

Statistics on employer contributions to defined contribution schemes depended on whether respondents were able to say whether their company was making payments into their pension schemes.

*Fidelity retirement assets are based on an estimate.

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