

---

## 5. The Consumer – Market Shape And Size

*'In efficient markets, the preferences of the end-consumer will ultimately drive behaviour and market structure. However, where consumer influence is weak, these preferences may be dissipated by intervening structures and incentives as these are transmitted through the system'<sup>12</sup>*

It is against a backdrop of significant regulatory change that this project has been conducted and against which the size and shape of the potential market needs to be assessed.

This section of the report describes:

- Key aspects of consumer savings attitudes and behaviour;
- The nature and size of the pool of possible buyers of Stakeholder products;
- 'What if' estimates of possible market size and value;
- The potential impact that could be created by different distribution channels; and
- Some conclusions concerning the size and shape of the potential market.

The following research has fed into this analysis:

- Views collected from providers and distributors during meetings conducted for this project and market research that has kindly been passed to us from those organisations;
- Existing data sources and analysis in the public domain;
- Responses to the Stakeholder products consultation process;
- Deloitte & Touche's own existing research, specifically Wealth & Portfolio Choice, a model of wealth and savings behaviour of the adult population (18+years) built in 2002 and based upon a survey of more than 3000 adults in Great Britain<sup>13</sup>.

Data from Wealth & Portfolio Choice has been used extensively throughout this extract. Other data sources such as the British Household Panel Survey and Family Resources survey are based on longitudinal studies and/or have larger samples but do not provide for a detailed analysis of savings behaviour and wealth. By contrast, the Deloitte study provides for detailed analysis but is based on a snapshot survey conducted in early 2002. Where possible, the Wealth data has been validated against other comparable data sets.

---

<sup>12</sup> Ron Sandler, 2002

<sup>13</sup> See appendix one for further details of the quantitative research

## 5.1 Savings activity

Whether individuals are saving sufficiently to adequately meet their needs, particularly in later life, has become an increasingly high profile topic. Many believe as a nation we are not saving at adequate levels, although a number of judgments concerning how much is 'enough' are necessary to reach this conclusion.

Despite these concerns, more than half of adults in Great Britain<sup>14</sup> currently do save something other than savings in ordinary deposit based savings accounts<sup>15</sup>, a proportion that does not fall below 50% even for low income groups. Research carried out in 2000 by the Personal Finance Research Centre (sponsored by AMP/Pearl) also concluded that the majority of low to middle income consumers do save during their lives and that long-term non-saving as a pattern of behaviour is 'very rare'. However, those on low incomes do have a greater tendency to save occasionally rather than regularly. The proposals for Stakeholder products are intended to make it easier for those who wish to and are able to save to do so more easily and with greater confidence. In a study conducted by B&W Deloitte in 2000, 88% of UK working age adults acknowledged the importance of saving<sup>16</sup>:

- 41% agreed that 'it is important to save through a pension'
- 41% agreed that 'it is important to save through a pension and other savings plans'
- 6% agreed that 'it is important to save through but not through a pension'

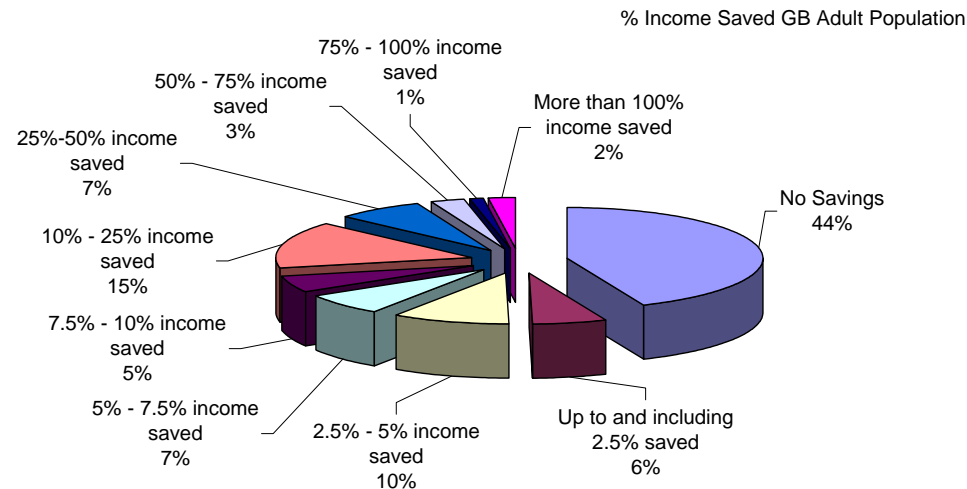
As shown in the chart below, across the GB population as a whole, 44% of the population claims not to have put funds into any of the following products in 2001: savings endowments, equity ISAs, cash ISAs, national savings, premium bonds, pension (own contribution), direct share holdings and unit trusts. Of the remaining 56%, half save less than 10% of income, half more. Taken as a whole, the average contribution across the GB adult population represented 12% of average income saved.

<sup>14</sup> Wealth & Portfolio Choice 2002 – described in further detail in Appendix One

<sup>15</sup> Actively putting money into savings endowments, equity ISAs, cash ISAs, national savings, premium bonds, pension (own contribution), direct share holdings and unit trusts in 2001.

<sup>16</sup> Mapping the Future of Pensions, B&W Deloitte 2000.

Chart 5.1 – Percentage of income saved (GB adult population)<sup>17</sup>



Among the 19.3 million who do not actively save in the way described below are:

- 5.2 million who are retired (although 48% of all retired do save);
- 7.4 million who are not working for other reasons (although 31% of those who do not work for other reasons do save);
- 4 million aged under 25 (although 30% of those under 25 do save);
- 3.9 million who made positive net savings in a bank or building society account;
- 11 million who nevertheless describe themselves as regular or occasional savers;
- 3.2 million who are paying off a mortgage.

Whilst the numbers above are mutually exclusive, they do indicate that the majority of those who could be expected to save, do so to some degree.

<sup>17</sup> Wealth & Portfolio Choice, Deloitte 2002. Measured as gross contributions flowing into savings endowments, equity ISAs, cash ISAs, national savings, premium bonds, pension (own contribution), direct share holdings and unit trusts as reported in Wealth & Portfolio Choice study. Excludes those saving through bank and building society accounts. Averaged across the whole population and measured as a % of total individual income. Not all of this saving will come directly from own income, some may come from switching from one savings vehicle to another, from gift or inheritance or from another individual's income. It does not therefore represent purely new savings. The average includes both those paying single contributions and regular contributions

---

## 5.2 *Barriers to Saving*

The proposals for Stakeholder products come at a time when many consumers have become disenchanted with the retail financial services industry, due in part to:

- Headlines that continue to focus on misselling by the industry;
- Poor returns in the past few years reflecting stock-market performance;
- Headlines concerning the problems associated with the UK pension system;
- Lack of simplicity and transparency in products;
- The withdrawal of the home service agent or the local bank branch;
- The tendency in recent years for advisors to focus on higher income or net worth clients;
- The high profile closures or sale of previously respected brands.

Consumers have, as a result, become more distanced from the industry with some resultant changes to savings behaviour. Many have chosen to revert to cash savings that they understand and that are perceived to be risk free. Others have chosen to divert savings to paying off their mortgage early or to extending their mortgage, thereby increasing the importance of a single property in their savings portfolio.

Other barriers identified by Sandler and other research perceived complexity of the market, a perception that significant sums of money are required to 'invest', a perception that investment is too risky, inertia and finally a lack of willingness to 'tie money up'.

Consumer motivation for saving is driven in part by changing expectations of the role of the state. Many consumers believe that it will be the responsibility of the individual to finance (at least a substantial part of) their needs in retirement. Whilst the vast majority of consumers (86%) believe that the state should provide for them in retirement<sup>18</sup>, only 36% trust the state to do so<sup>19</sup>, whilst 70% expressed the view that it is the individual's responsibility to make their own financial arrangements<sup>20</sup>.

Taken together the above analysis suggests widespread acceptance of the need to save but an inadequate response to this need in the form of savings activity. Encouragement for consumers to act upon this recognised need falls to the industry and Government through the creation of a market environment where consumers feel they can make informed choices about their retirement plans and other savings, have access to good value, simple, saving vehicles and feel confident about achieving good returns.

---

<sup>18</sup> Mapping the Future of Pensions, Deloitte 2000. "I believe that the state should provide good pensions for us all when we retire". Those responding agree strongly or agree slightly.

<sup>19</sup> Mapping the Future of Pensions, Deloitte 2000. "I trust the state to provide". Those responding agree strongly or agree slightly.

<sup>20</sup> Mapping the Future of Pensions, B&W Deloitte 2000. "It should be the responsibility of each individual to make their own financial arrangements". Those responding agree strongly or agree slightly.

---

## 5.3 *The Market for Stakeholder Products*

The size and profile of the market for stakeholder products is likely, in the early days, to be shaped most by the willingness and ability of sales channels to reach out and influence the market. Industry response is difficult to gauge with any certainty and represents one of the key sensitivities in the ultimate size and shape of the market and the extent to which it reaches those who are currently not engaged by the industry.

Views on the market for stakeholder products are diverse. On the one hand, the market could be considered to be the majority of the adult population, many of whom need or want to save and currently do so. On the other, the market could be very constrained by the need to consider a variety of factors to safeguard consumers. The analysis below does not restrict the market to low and middle income earners but rather seeks to find consumers who may be considered appropriate for providers and distributors to target.

### 5.3.1 *Filters on market size*

It is widely acknowledged that, in order to reduce the potential for consumer detriment under the proposed FSA sales regime (DP19), it will be necessary to introduce formal or informal guidance on those consumers for whom Stakeholder products are deemed to be unsuitable. The criteria for filtering out 'unsuitable' consumers could include:

**The consumer's debt position.** Individuals who have 'uncomfortable' levels of debt in relation to their incomes should perhaps not be recommended to start saving but should instead be guided to repay debt. The more extreme view taken by some is that any individual with debt of any kind (even a mortgage) should not also be saving. However, this view would lead to many consumers deferring saving until their 50's and achieving an asset mix disproportionately invested in one asset, their own home. Furthermore, for many the repayment of some debts (e.g. personal loans) cannot always be restructured at a sensible cost and too strict an application could prevent those who are able and wish to save from doing so. A more detailed analysis of the impact of debt on market size is provided below.

**Access to emergency funds.** It is generally accepted that consumers should not invest in equities without first building up an adequate reserve of 'safe' and accessible savings in cash. Various views exist on how much cash this should be with three months income an oft-quoted amount. The amount an individual should or chooses to hold will vary with personal circumstances, the economic climate and attitudes to risk. It can be argued that lower income groups should hold a greater proportion of their portfolio in cash but this view could lead to what Ron Sandler refers to as 'reckless conservatism' in investing. A more detailed analysis of the impact of cash savings on market size is provided below.

**Willingness to take risks.** Attitudes to risk vary according to income with the majority of those on low or moderate incomes expressing a reluctance to invest in products where the nominal value of their capital is at risk. Only among those earning above £22,000 pa does the majority view switch to being prepared to take some risk with a proportion of a portfolio of savings. However, a further analysis of those who express a preference for no risk reveals that approximately 40% of those on low and moderate incomes already hold products that are wholly or partly invested in equities<sup>21</sup>. The impact of removing those with a low acceptance of risk from the market is analysed in further detail below.

---

<sup>21</sup> Wealth & Portfolio Choice, Deloitte 2002

---

**Adequate life and income protection cover.** Analyses conducted by a number of organisations shows consistently that a large number of people do not have adequate (or in many cases any) life cover. According to the Family Expenditure Survey, 46.5%<sup>22</sup> of households do not have at least one protection product. Data from consumer research conducted for Deloitte & Touche in 2000<sup>23</sup> shows:

- One-quarter of the population claiming to own whole life assurance, with levels of ownership varying only marginally by income;
- 5% of the population claiming to have term assurance not related to their mortgage, with ownership correlated to income;
- Death in Service benefits, frequently linked to pension ownership, is strongly correlated to income but can of course be lost immediately on loss of job.

There will however be a group of consumers that may value savings more than protection and may therefore chose to save rather than take out a protection product. At the extreme therefore, filtering out those who have 'inadequate' cover would appear to reduce the size of the market considerably, particularly among low and medium income groups. Moderating for consumer preference and individual circumstances will reduce the market by a smaller proportion. Whilst the Wealth & Portfolio Choice study provides a detailed analysis of savings and investments, it did not provide similar evidence of adequate protection coverage nor did it identify consumer preference for savings versus protection. Given the paucity of data in this area, the analysis below does not exclude from the pool of possible buyers those with inadequate protection cover. However, it is acknowledged that the development of greater distribution capacity in the market may lead to both protection and savings gaps being reduced.

**Interaction with state benefit.** The issue of the interaction of savings and state benefits is a complex one and difficult to assess in detail within this project. A variety of different assumptions can be made, both simplistic and complex. At a simplistic level, individuals earning less than £10,000 pa can be excluded from any estimate of the market. However, this does not take account of a) those individuals on low individual earnings living in a high income household who would not qualify for benefits in any event and b) those on low incomes at an early stage in their career and whose incomes over a lifetime may rule them out of state benefits. We explore below the impact of removing from the potential market those individuals on low incomes and aged over 45.

The size of the potential market will be informed further by the on-going debate between Government, FSA, industry and consumer bodies that will conclude with greater clarity on the rules to be applied by the industry in the application of the DP19 sales process. The issues under debate include:

- The definition and degree of prescription applied to any filter questions;
- The degree to which the Government believes that current individual or household income should be considered in assessing suitability;
- The obligation on the salesperson to collect information relating to these questions or the reliance on the consumer's own assessment;
- The ability of the salesperson to continue in dialogue with consumers who do not appear to meet the criteria but nevertheless have a desire to purchase one of the products;
- The confidence with which the industry feels able to embrace the new sales process or seeks to apply further constraints.

---

<sup>22</sup> ABI analysis of the Family Expenditure Survey, 2000/01

<sup>23</sup> IFA Futures, Consumer Research, Deloitte 2000

In the analysis conducted, we have been unable to anticipate the outcome of this debate but have nevertheless attempted to size and profile the possible pool of buyers of Stakeholder products. We have then further estimated the volume and value of new contracts that could be expected to be sold in any one year for the purposes of assisting the profitability modelling described in the full report.

### 5.3.2 Possible Buyers of Stakeholder Products

The table below has been produced using the Deloitte Wealth & Portfolio Choice research to estimate the possible size of the market for Stakeholder products, segmented by income groups and applying a variety of potential filters.

Table 5.1 – Market size using various filters

Number of Individuals (million)	Low Income	Moderate Income	High Income	Low/High Income	Total GB Adult Population	% Population
<i>Single Filters</i>						
Total Population with no filters	15.44	13.53	8.42	7.03	<b>44.43</b>	100%
Total Population with at least 3 months savings	6.35	5.22	3.66	4.59	<b>19.82</b>	45%
Total Population with at least 6 months savings	5.00	3.84	2.35	2.77	<b>13.95</b>	31%
Total Population with at least 12 months savings	3.46	2.35	1.03	1.84	<b>8.68</b>	20%
Total Population with cost of debt including mortgage <40% income	13.19	11.79	7.92	6.46	<b>39.36</b>	89%
Total Population with cost of debt including mortgage <20% income	11.29	10.07	5.85	4.71	<b>31.93</b>	72%
Total Population with no debt	7.37	6.91	.81	1.18	<b>16.28</b>	37%
Total Population prepared to take risks with savings	5.20	4.47	5.53	3.77	<b>18.97</b>	43%
<i>Combined Filters</i>						
1. Total Population with at least 3 months savings excluding those with > 40% debt and not in difficulty with repayments	6.27	5.21	3.66	3.76	<b>18.91</b>	43%
2. As 1. but excluding those aged over 70, those with income of less than £10000 pa and aged over 45 and those under 45 with income of less than £5000pa	<b>1.78</b>	<b>3.31</b>	<b>3.48</b>	<b>3.55</b>	<b>12.13</b>	<b>27%</b>
3. As 2. but excluding those unwilling to take risks	.83	1.64	2.57	2.12	<b>7.16</b>	16%

Table 5.2 – Variable descriptions

Low Income	Individuals with total gross income from earnings, investment income, benefits and pensions of less than £10,000 pa and with household income of less than £25,000.
Moderate Income	Individuals with total gross income from earnings, investment income, benefits and pensions greater than or equal to £10,000 pa and less than £22,000 and with household income of less than £25,000
High Income	Individuals with total gross income from earnings, investment income, benefits and pensions of £22,000 pa or more and with household incomes of £25,000 or more.
Low/High Income	Individuals with total gross income from earnings, investment income, benefits and pensions less than £22,000 and with household income of £25,000 or more. Also included in this group are a small number of individuals who have recorded high personal incomes but low household incomes in the research.
(3/6/12) months savings	Total savings in cash-based products (building society/bank savings accounts, Cash ISAs, National Savings, Premium Bonds) as a proportion of total annual income.
Cost of debt	Total cost of servicing household debt (mortgage repayments, loan repayments, credit card repayments etc) as % of household income.
In difficulty with debt	A self-diagnosis of difficulty in repaying mortgage and/or other debt (separately). Those scoring as 7 or more deemed to be in difficulty. Questions posed:  “On a scale of 1 to 10 with 1 being no difficulty and 10 being very difficult, how easy or difficult is it to keep up with mortgage payments?” “On a scale of 1 to 10, where 1 means it is very easy and 10 means it is very difficult, how easy or difficult would you say it is to keep up with all of your loan or card repayments?”
Willingness to take risks	A response to the question “Which one of the following statements best describes your attitude to savings and investment risk?” 1. I am not willing to take any risk with my savings or investments 2. I am prepared to have some of my savings or investments in higher risk products than in building society/bank savings accounts 3. I am prepared to take risks to get higher return 4. Don't know Those who answered 2 or 3 were deemed to be prepared to take some risks.

---

Given the difficulties described above in specifying precisely the pool of possible buyers of Stakeholder products, we have, for the purposes of profiling potential buyers and sizing the market, used the second of the combined filters, i.e. 12.1 million individuals who:

- Have 3 months of income in cash savings;
- Do not appear to be struggling unduly with debt because debt repayments are less than 40% of income **and** have not stated that they are having difficulty servicing their debt (mortgage or other debt);
- Are aged under 70;
- Have income of more than £5000 pa if under 45 or income of £10000 or more if aged 45 or more.

As expressed, the size of this pool could increase or decrease depending upon the detail of the filters, the targeting and distribution approaches adopted by the industry, the state of the economy and the response of consumers. For example:

- Excluding all of those earning £10,000 pa (either because the filters suggest that this should be the case or because industry does not take an interest in those earning so little) reduces the 12.1 million to 10.35 million;
- Excluding all of those earning less than £22,000 shrinks the market to 3.48 million. If income is used as a proxy for affordable contributions and industry adopts approach of targeting only those with high incomes or takes the view that lower income consumers should predominantly save in cash vehicles, the market could be considered to be one third of the size whilst generating higher average contributions;
- Excluding all of those with 'inadequate' protection has the potential to shrink the market still further, perhaps by more than half;
- Excluding all of the above and those not prepared to take risks with their savings will reduce the pool of potential buyers to a very small size;
- An increase in unemployment, increases in interest rates, increases in over-indebtedness could all lead to further shrinkage of the market;
- Including some of those individuals who do not meet the criteria of the 12.1 million but who express a desire to save and are prepared to take some risk with their savings could increase the market substantially.

The sensitivities around market size are explored further in section 5.4 below.

Appendix Three to this extract contains a more detailed profile of the 12.1 million by income segment. In summary, the demographic analysis reveals the following dominant characteristics for each group:

- Low income - young, single, female, part-time workers in the C1/C2 socio-economic group, many of whom are not yet home owners;
- Moderate income – older, retired, children have left home, home owners
- High income - middle-aged, male, married, southern, home-owning, full-time workers in AB socio-economic group;
- Low/High income – older, female, AB, home owners with children at home whose partners work.

---

## 5.4 Market Size

Although we have described a pool of 12.1 million possible buyers, clearly not all of these can be expected to purchase a Stakeholder product in the first year of the new market. Indeed, were the industry successful in reaching all 12.1 million in one year, it is unlikely that adequate capital would be available to support the new business strain, the second year would see a collapse in new business results and the impact on the economy from such a switch from consumption to saving would be immense. Some will never buy due to their preferences to save in other vehicles (or not at all), particular personal or household circumstances not captured by the filters or the industry's reluctance, or inability to target all of those in this group.

Whilst the size and profile of the market will in many respects be in the hands of future distributors of stakeholder products, it was felt worthwhile to try to gain some sense of how large the supplementary Stakeholder market may be for providers and distributors. Below, we outline estimates of the number of contracts that could be sold in any one year, the average contribution levels that might be expected and from these, the value of the total contribution income that may be derived from this business. Whilst we have sought to isolate those who are not currently being reached by the market, it is impossible to create a fully isolated sense of the market size for Stakeholder products and the numbers shown below may include some 'halo' effect of consumers switching activity from current to new products. The following modelling continues to use the central pool of possible buyers of 12.1 million individuals. Of necessity, much of the analysis is speculative and based on a 'what if' approach and should not be taken as a scientific and precise forecast of the future market size.

In order to focus on the additional business that could be available to providers, we have concentrated the analysis on regular contribution business. In the financial modelling, we have assumed that a small amount of additional lump sum business will also be available. Implicit in this assumption is that consumers with lump sums to invest are already being accessed by the industry and that whilst some of this business may gravitate towards Stakeholder products, it represents replacement rather than true new business.

### 5.4.1 Regular Contribution Savings Contracts

#### *Volume of sales*

During the late 1980s, ABI members were selling 1.5 million new savings endowments per year (plus 2 million mortgage endowments)<sup>24</sup> – an implied 3% of the total adult population. Prior to the removal of tax relief in the early 1980s, sales are believed to have been higher still. Whilst no industry analysis of the profile of the buyers of such products is available, analysis from Wealth & Portfolio Choice shows that of the 11.7 million individuals (26%)<sup>25</sup> who claim to have a savings endowment, 46% have incomes of less than £22,000 pa. Current sales have fallen to just 20% of the 1988 figure due in part to the withdrawal of the home service distribution channel, in part to consumer disenchantment with mortgage endowments and poor stock market performance. In part, endowment sales have been replaced in recent years by equity ISA sales, although the number of individuals saving regularly through equity ISAs has never matched that of endowments with 1.75 million in total saving regularly through

---

<sup>24</sup> Analysis provided to Deloitte & Touche by ABI

<sup>25</sup> Whilst the questionnaire sought to differentiate between endowments held to repay mortgages and those used for savings, it is believed that some respondents may have included mortgage endowments that are no longer assigned (formally or informally) to their mortgages.

equity ISAs in 1999 falling to 1.6 million at the end of 2002<sup>26</sup>. An analysis of the 1.4 million individuals that claim to be saving on a monthly basis through equity ISAs in the Wealth & Portfolio Choice model reveals that 32% have incomes of less than £22,000 pa.

An optimistic view of potential market size might lead to the conclusion that a return to the heyday of sales in excess of 1 million new contracts per annum is possible. If drawn entirely from the 12.1 million pool of possible buyers, this would represent 8% of the pool buying each year. However, in arriving at a base case assumption for the market size, we have adopted a more conservative assumption of the new market reach.

By looking further at the savings activity and potential of the pool of 12.1 million, it is possible to isolate 4.2 million who are saving less than 5% of their incomes (in pension, endowments, National Savings, Premium bonds cash ISAs or equity ISAs) with the remaining 7.9 million already saving in excess of 5% of their incomes. There is a marked difference in purchasing activity of equity ISAs and savings endowments between the two groups with negligible activity among the 4.2 million, whereas approximately 9% of the 7.9 million invested in equity ISAs in 2001/2002 (mostly lump sums) and, in addition, 2 % took out a new savings ISA. As already noted above, the non-saving group's inactivity does not appear to stem from a lack of willingness to save or a view that spending is more preferable to saving.

In arriving at a view of the percentage who could be reached from these smaller more targeted groups if distribution capacity is developed and industry is willing to target them, 3% of those who currently save very little or nothing and 1.5% of the larger group who already save would appear to be a prudent starting point for sizing the supplementary stakeholder market. The results of sensitivities on these numbers are shown below. If these numbers can be persuaded to buy a Stakeholder savings plan each year, this will yield a total new market of approximately **245,000 new contracts** (ie a quarter of the number implied if the optimistic view above were taken). This is without any business being generated from the remainder of the population. It is important to stress that this number is drawn from an analysis of what might be reasonably achievable rather than an assessment of what any given charging level might achieve. Inherent in the analysis is an assumption that the charging level for stakeholder products is sufficiently attractive to the industry to begin targeting those with low to moderate incomes and those who do not currently save.

If spread evenly across the four segments (in practice, increasing the savings activity of the lower income segments more than the higher income segments who already save), the 245,000 contracts would be distributed as follows:

Table 5.3 – Mix of possible savings plan buyers

Low income	Moderate income	High Income	Low/High Income
<b>42,000</b>	<b>70,000</b>	<b>64,000</b>	<b>69,000</b>
<b>17%</b>	<b>29%</b>	<b>26%</b>	<b>28%</b>

The eventual shape of the market will depend upon the willingness and ability of distributors to reach those on low incomes and the willingness of those individuals to save through these products.

<sup>26</sup> IMA

### Average contributions to regular savings plans

In order to arrive at a view on likely average contributions, the following information was analysed:

- Current average contributions to savings endowments* – ABI data shows average new contributions to be approximately £40 per month (average new contributions for mortgage endowments are in excess of £100pm). The average for all those claiming to be saving through endowments in the Wealth & Portfolio Choice study is £98 per month (66% paying under £100pm). The average among the 12.1 million pool currently saving through endowments is slightly higher at £120 per month distributed as shown below across the segments (this average includes older and newer cohorts of buyers). The marked difference between the ABI and Deloitte data are likely to arise from those respondents who have attributed mortgage endowments as savings endowments (perhaps because the policy is no longer assigned to the mortgage) and potentially those saving very small amounts forgetting the existence of the contract, thereby inflating the average.

Table 5.4 – Average endowment contributions

Low income	Moderate income	High Income	Low/High Income
£ 85pm <sup>27</sup>	£ 74pm	£ 171pm	£ 102pm

- Current average contributions to equity ISAs* – ABI members reported an average of £100pm for new regular contribution equity ISA business in 2002. Among those claiming to save monthly in equity ISAs in the Wealth & Portfolio Choice study the average is £117pm. The average among the pool of 12.1 million who save monthly in equity ISAs is claimed to be £126pm distributed as follows:

Table 5.5 – Average ISA contributions

Low income	Moderate income	High Income	Low/High Income
£ 34pm <sup>28</sup>	£ 65pm	£ 163pm	£ 90pm

<sup>27</sup> Small sample of fewer than 50 respondents

<sup>28</sup> Small sample of fewer than 50 respondents

- *Average total savings for the 12.1 million* - on average the 12.1 million potential buyers currently save 20% of their individual incomes<sup>29</sup> (including those who save nothing). This rises to 24% among those with low individual income but high household income group (Low/High) and falls to 13% among the low income group.

In order to arrive at average contributions for the central financial modelling, a view was taken based upon the analysis shown above and the following averages derived.

Table 5.6 – Average contributions for modelling

Low income	Moderate income	High Income	Low/High Income
£ 30pm	£ 75pm	£ 220pm	£ 130pm

If on average, the 245,000 new savers can be persuaded to save on average £120pm (on average 7% of their incomes and the weighted average of the monthly contributions shown immediately above), this would generate a market value (measured in new contributions pa) of **£355million**.

## 5.4.2 Regular Contribution Pensions Contracts

### Volume of sales

Recent purchasing data for pensions is less clear containing as it does significant numbers of transfers from old style personal pensions and includes transactions that result from an individual leaving one job and scheme and joining another (therefore adding nothing in net terms to the number of pensioned). In addition to the savings activity outlined above, an estimated 1-2% of the total population (a higher proportion of those who are eligible) is estimated to be taking out a new pension contracts (or joining new schemes) in a typical year. Whilst the sale of in excess of 1 million regular contribution stakeholder pensions in 2001 and 2002<sup>30</sup> would suggest higher volumes, it is recognised that some of this business relates to the reclassification and transfer of personal pensions and not to new savings activity.

<sup>29</sup> Measured as gross contributions flowing into savings endowments, equity ISAs, cash ISAs, national savings, premium bonds, pension (own contribution), direct share holdings and unit trusts as reported in Wealth & Portfolio Choice study averaged across the whole population and measured as a % of total individual income. Not all of this saving will come directly from own income, some may come from switching from one savings vehicle to another, from gift or inheritance or from another individuals income. It does not therefore represent purely new savings. The average includes those paying single contributions and regular contributions.

<sup>30</sup> Deloitte & Touche estimates derived from ABI and IMA statistics, and Wealth & Portfolio Choice

Analysis of Wealth & Portfolio Choice data relating to pensions reveals the following proportions of each segment in pension schemes:

Table 5.7 – Pension ownership

	Low income	Moderate income	High Income	Low/High Income
% members of any pension, past or present but not yet drawing	41%	55%	86%	66%
% currently members of scheme or plan	23%	41%	79%	46%

Of the 12.1 million, 8.1 million are employed or self-employed and a further 2.1 million are non-working for reasons other than retirement (the remainder are retired). Of these 10.2 million, 40% claim to have no pension (either current or from previous employment). Future new pensions could come from those without a pension at all, those who are not current members and those who have pensions but either move job or move pension.

The potential for new pension business is greatest among the low income group. However, propensity to buy a pension is likely to remain highest among the higher income and who may choose to supplement an occupational scheme with an individual stakeholder plan if the new Inland Revenue pension rules are implemented.

Predicting how much new stakeholder pension business is likely to arise is an even more imprecise science than for new savings contracts. With the support of new distribution and active marketing, it may be possible to attract 3% of those with no pension and 1.5% of those with existing pensions to buy a new Stakeholder pension each year. This will yield a total market of approximately **213,000 new contracts**. This number appears low when compared to the 1 million plus stakeholder pensions sold already. However, the number reflects the fact that much of the market that is easy to reach has already purchased and the lack of 'transfers' to stakeholder that will take place this time round.

---

If the same penetration rates are applied to all four segments (in practice, increasing the savings activity of the lower income segments more than the higher income segments who already save), the 213,000 contracts would be distributed as follows:

Table 5.8 – Mix of possible pension buyers

---

Low income	Moderate income	High Income	Low/High Income
<b>46,000</b>	<b>48,000</b>	<b>58,000</b>	<b>61,000</b>
<b>22%</b>	<b>23%</b>	<b>27%</b>	<b>29%</b>

The eventual shape of the market will depend upon the willingness and ability of distributors to reach those on low incomes and the willingness of those individuals to save through these products. Some of these plans may have been sold in any event under existing stakeholder pension legislation, although more and more providers are withdrawing from the market leading to greater financial exclusion, particularly for those who wish to buy individual stakeholder plans and for those on low incomes.

### **Average contributions to regular pension plans**

In order to arrive at a view on likely average contributions, the following information was analysed:

- *Current average contributions to pensions* – ABI data shows current average contributions to stakeholder pensions to be approximately £140 per month (including tax rebates). The averages shown by the Deloitte research for the 12.1 million currently saving through pension as £124 per month (*grossed up for basic rate tax rebates into contracts but excluding employer contributions*) distributed as follows across the segments:

Table 5.9 – Average pension contributions (excl employer)

Low income	Moderate income	High Income	Low/High Income
£ 42 pm	£71 pm	£ 260 pm	£74 pm

We estimate that approximately 15% of those with no current pension may also receive contributions from an employer (based on an assumption of 25% of employers of low income buyers and 35% of higher income buyers and 51% of those eligible being employed) and 18% of those with a pension (25% of employers of low income buyers and 35% of higher income buyers contributing and 75% being employed).

Combining the current averages for the segments, allowing for those employers who do contribute to match the individual contribution (and then rounding), leads to average contribution levels shown below.

Table 5.10 – Total average pension contributions used for modelling

Low income	Moderate income	High Income	Low/High Income
£ 50 pm	£130 pm	£ 380 pm	£110 pm

If new savers can be persuaded on average to save £175 per month (including tax rebates and employer contributions – the weighted average of the contributions shown above) as above, this will generate a market value (measured in new contributions pa) of **£447million**.

---

### 5.4.3 Total market size (regular contributions)

Whilst the same 12.1 million pool of potential buyers is used to assess both the regular contribution savings and pensions, the analysis would suggest that it is possible for both markets to emerge separately leading to a total possible market size of:

- 459,000 new regular contribution contracts per annum;
- £802 million new regular contributions per annum;
- Average monthly contributions of £146.

This compares to current market sizes of in excess of £4.3bn of new regular contribution life and pension business<sup>31</sup> and an estimated £2bn of regular savings ISAs<sup>32</sup> in 2002.

£802million of new regular contributions implies market growth of approximately 13% on current new business levels.

For these base case results to emerge, it will be necessary for the following market behaviours to be realised:

- Distribution channels to emerge that embrace DP19 regulation;
- Distribution channels to emerge that engage with low and moderate income consumers and others who do not currently save;
- Consumers to trust the stakeholder brand, new channels and the providers;
- Marketing effort on the part of Government, providers and distributors.

In turn for much of this to emerge, the profitability of the products must be such to attract capital to the market and the potential size of the market must be sufficient to warrant investment and be seen to be capable of supporting competition.

---

<sup>31</sup> ABI Statistics

<sup>32</sup> IMA Statistics

#### 5.4.4 Market Size Sensitivities

The following table shows how different market sizes and values could emerge under different results to those described above.

Table 5.11– Market size sensitivities

	Number of contracts 000 pa	£m New Contributions pa (regular contribution business)	Average Contributions £pm
Base Case	458	802	146
50% of number saving	229	401	146
150% of number saving	687	1203	146
50% of average contributions	458	401	73
150% of average contributions	458	1203	219
Worst of both	229	201	73
Best of both	687	1805	219

---

The worst case described above implies only 3% market growth with few new customers and low average contributions. Any or all of the following could result in this scenario occurring:

- The existing industry lacks confidence in the FSA's DP19 rules and new players are nervous of entering the market;
- Media discourage consumers from buying and industry analysts discourage capital investment;
- The Stakeholder brand lacks punch with consumers;
- The economy becomes more uncertain;
- Employers lack confidence in allowing worksite marketing;
- The price cap is set at a level that discourages investment in distribution to the mass market;
- Few new sales channels developed or those that do are not trusted by the consumer;
  - Banks do not embrace change
  - No new salesforces emerge
  - Worksite marketing fails under DP19
  - Retailers lack punch
  - Direct offers not persuasive.

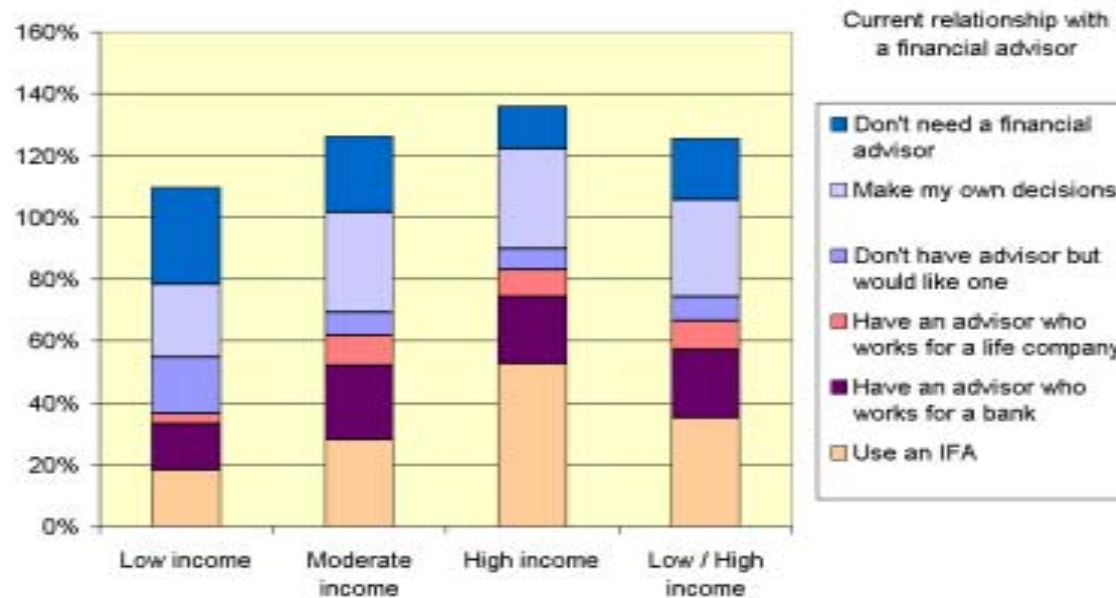
By contrast the best case results in almost 30% market growth. For this to be realised, all or most of the following will be necessary:

- DP19 option 2 is endorsed and clarity emerges from the Financial Ombudsman Service regarding the potential for future misselling;
- The media is convinced of and promotes the consumer benefit;
- Industry analysts are convinced of the potential profitability of the contracts and encourage capital investment;
- Consumers are attracted by the simplicity and transparency of the contracts and are encouraged to increase their level of saving;
- Economic stability and an improvement in stock market returns;
- Pensions simplified;
- Focus on regular savings;
- Channels emerge quickly and target a wide range of consumers;
  - New 'home service' style
  - Employers support worksite
  - Banks embrace
  - Retailers support
  - Direct offers attract the top end of the market.

**5.5 Reaching the market**

If the size and shape of the market is determined largely by the future DP19 sales channels and the desire of the Government is to extend the market to low and middle income consumers, it is necessary to consider charging structures in the context of the ability of different channels to 'persuade' consumers to buy Stakeholder products and those that may have a natural affinity with the target market for financial services. An examination of current uses of distribution channels across the income segments (within the 12.1 million described above), reveals that those on low and moderate incomes are significantly less likely to have an advisor of any kind in the current market environment and that almost one in five of those on low incomes express a desire to find an advisor. Before the decline of the home service salesforces, this picture may well have looked very different with a significantly high proportion of low income consumers laying claim to an advisor from a life company.

Chart 5.2 – Current Relationships with Financial Advisors <sup>33</sup>



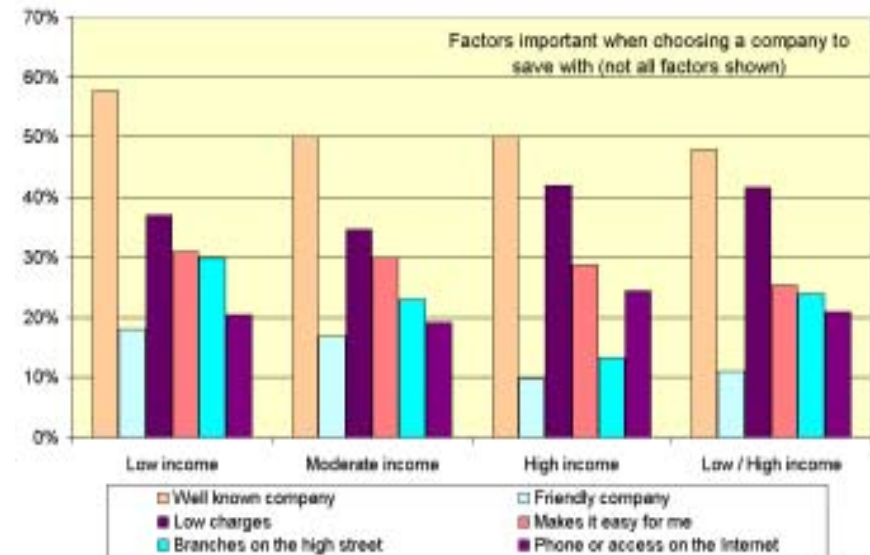
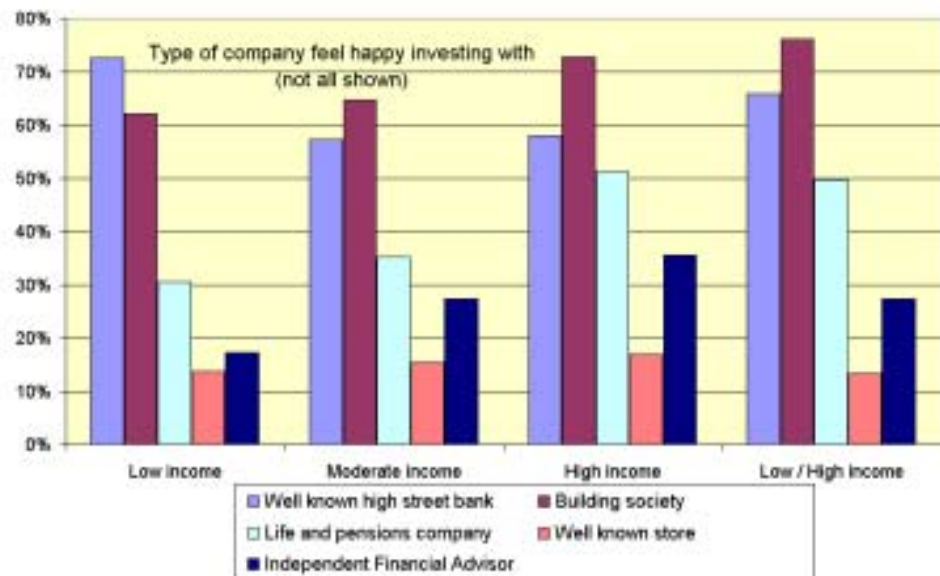
<sup>33</sup> Wealth & Portfolio Choice, 2002. Respondents able to choose more than one response. Full set of responses shown in Appendix Three

Further analysis of those using an IFA reveals that only 2% of those in low income groups are reached through worksite marketing compared to 14% of high income groups suggesting that at present, this is one of the least exploited and perhaps (due to the working patterns of low income groups) the least effective methods of reaching this group.

As the charts below show, banks and building societies are however a popular choice among low income groups as a suitable place to go for savings and investments, a large part of which may be related to a strong affinity to safer cash savings. Only a minority of all income groups feel a particular affinity with retail stores for savings, although higher income groups have a stronger affinity with new internet savings and investment brands (not shown in chart).

Well-known companies that are perceived to be friendly with branches on the high street are particularly likely to attract the low income groups whilst low charges, financial strength and past performance are particularly strong factors for higher income groups (not all shown in chart). Although low charges feature strongly for all segments, there remains little evidence that low charges alone will attract consumers to a provider or product.

Charts 5.3 and 5.4 – Type of company feel happy investing with and factors important when choosing a company<sup>34</sup>

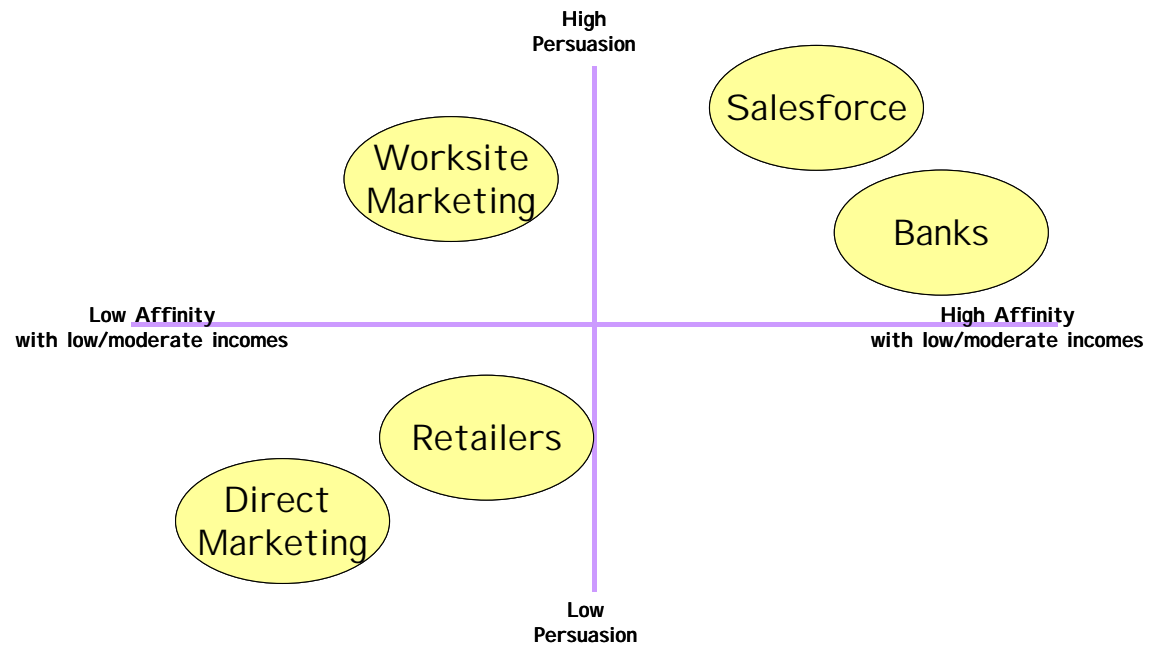


In the financial modelling of this report (not included with this extract), five different channels are tested, all of which are deemed to be operating under the DP19 regime and could be tied, multi-provider or independent.

<sup>34</sup> Wealth & Portfolio Choice 2002. Both tables exclude some responses to the questions. Full set of responses shown in Appendix Three.

As the following Chart demonstrates, it would seem likely from the analysis above that a DP19 salesforce could have the potential to effect the greatest 'persuasion' and have the greatest affinity with low and moderate income customers, particular if they can reclaim the ground of the home service salesforce and seek out the target market. Banks (or building societies) by contrast currently seem a more natural place to save for these consumers but are likely to have a less persuasive effect, relying as they do upon customers coming into branches.

Chart 5.5 – Channel prospects



---

Worksite marketing in its current form does not reach many of the low and moderate earners. However, in its new form under DP19, this could change to some extent. However, low income transient workforces are often decentralized (hotels, restaurants, retailing) and are likely to remain difficult to reach through this channel.

Direct marketing and retailers (the latter in their current mode of operating) do not have any strong persuasion to save built into the sales process, and as a result tend to reach only those segments of the population who are self-directed. Although not exclusively the case, in practice this generally means those on higher incomes that research the market.

This analysis has informed some of the assumptions made in the financial modelling contained in the full report.

## 5.6 Conclusions

The conclusions of this part of the report can be summarised as:

- Whilst barriers to saving do exist, the majority of consumers in all income groups recognise the need to save and indeed most do save in one way or another;
- Critical to the size of the market are the potential filters that the FSA or distributors themselves place to identify those for whom Stakeholder products may be appropriate. Particular uncertainties lie in the interaction with state benefits, attitudes to risk and those with inadequate life, critical illness or income protection;
- Filtering out those who do not have three months cash, are struggling with debt, are aged under 70 and are on particularly low incomes leaves a potential pool of 12.1 million consumers who may have the potential to buy stakeholder products;
- Among the 12.1 million, 4.3 million have very low levels of income flowing into savings and 4 million are eligible for but do not have a pension (with some overlap between these groups);
- Should:
  - 3% of those who do not save plus 1.5% of the remainder of the 12.1 million pool be persuaded to buy a new stakeholder savings plan; and
  - 3% of those without a pension plus 1.5% of those with a pension be persuaded to buy a new stakeholder pension each year; and
  - Average contributions of £146 per month (varying by income segment) achieved,a new market of £802 million could emerge.
- Banks and new salesforces may be critical to success in reaching the low and moderate income market;
- Support from media, analysts and Government will be critical to consumer and industry engagement.

A price cap that supports face-to-face marketing of stakeholder products profitably under the DP19 regime will be essential to engage industry support and in turn the consumer.