dpl financial partners

RIA Retirement Planning Survey 2021:

Executive Summary & Key Findings

The 2021 RIA Retirement Planning Survey provides insight into how this era of low interest rates is impacting advisors' retirement income planning practices and trends in attitudes and usage of strategies to deliver income for clients.

Overview

If 2020 was a year of social and financial anxiety as the world waited to see where the COVID-19 pandemic would leave us, 2021 is turning out to be a year of realization and tepid acceptance that the world has changed and we'll need to adapt to new realities, even if we would prefer not to.

For RIAs, already grappling with industry shifts that threaten their competitive value proposition, the persistence of low interest rates and a bleak forecast for bonds are calling into question time-honored strategies for investing clients' retirement portfolios, as well as billing methodologies.

Some see the need to rethink their approach while others cling to investment biases no longer in sync with market realities, that expose clients to unnecessary risks while leaving large portfolio allocations in exceptionally low-yielding assets like cash and bonds. While traditional strategies like bucketing still make sense, the allocations within those buckets often don't.

We hope these findings serve as a mirror for advisors and help them make needed changes, even if they would prefer not to.

About DPL Financial Partners

DPL Financial Partners is the first and leading RIA turnkey insurance management platform that brings commission-free insurance solutions from a variety of the nation's top carriers to RIA practices. DPL has created a marketplace of commission-free insurance products that enables RIAs to incorporate insurance and annuities into their practices to more holistically serve their clients. Clients benefit from products that offer competitive pricing and fiduciary implementation rather than commissioned, sales-driven ones. www.dplfp.com

Methodology

DPL Financial Partners conducted the study in June and July 2021 in an online survey format. A total of 203 advisors completed the survey including a mix of small-, mid- and large- sized firms.

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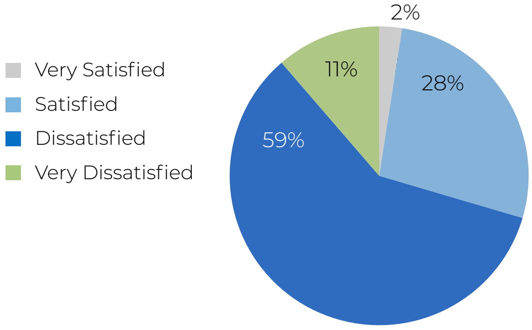
Advisors’ Evolving View of Fixed Income

When compared to previous years’ findings, this year‘s survey provides insights into how attitudes and practices are evolving over time and nowhere was this more evident than when tracking advisors’ evolving views of fixed income.

Seventy percent of those surveyed said they were dissatisfied or very dissatisfied with their fixed income returns, up from about 55% last year. The increase in dissatisfaction aligns with a lackluster forecast for fixed income returns, which more than half of respondents expect to be less than 2.5%. This data supports the idea of a growing awareness among advisors of the realities of a secular decline in bond yields that has been solidifying for more than a decade.

As advisors come to grips with the persistence of low interest rates, many are shifting client assets into alternative investments to supplement or even replace fixed income allocations in portfolios. Consistent with last year’s survey, many advisors rely upon total return strategies to meet clients’ retirement income needs.

Relative to historical returns, how satisfied are you with the current fixed income market and your fixed income returns?



We have long been concerned about the implications for retirees when riskier investments are used to generate retirement income, particularly to fund essential expenses, and have presented academic study that demonstrates a strong alternative to bonds in a financial plan. We also have seen that the downturn in fixed income yields is driving advisors to invest an increasing share of client portfolios in riskier assets such as equities and alternative investments to generate income.

However, a new question we added to the survey this year suggests a second factor could be exacerbating the trend toward greater risk in retirement portfolios, a factor that creates a disturbing financial conflict of interest: A significant portion of advisors said they are charging reduced fees—or no fees at all—on fixed income assets.

Advisors are Risk-On

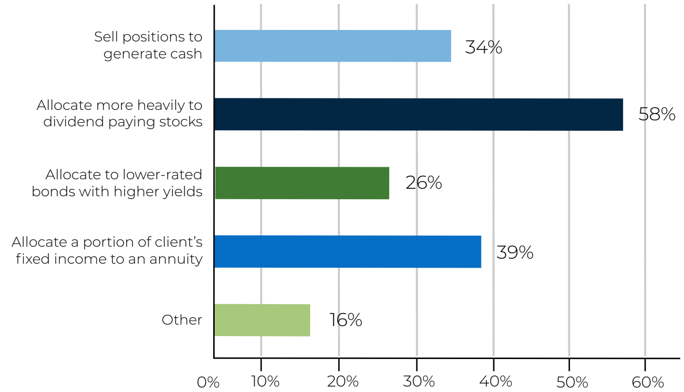
There is little doubt advisors are putting more of their clients’ capital at risk. In its Winter 2021 Advisor Insights Guide, BlackRock analyzed more than 20,000 advisor portfolio models and found there was a 25% increase in risk over the last two years in the average moderate advisor model (or nearly 10% per year)[1].

[1] https://www.orionportfoliosolutions.com/wp-content/uploads/dlm_uploads/2021/02/advisor_insights_guide_winter_2021_pdf_0E1g8klU.pdf

And the same BlackRock report projects that investors won't necessarily be compensated for ramping up risk. While stocks returned 13.7% from 2010 to 2020 and bonds 3.6%, the firm's capital market assumptions for the next decade are much more modest at 5% per year for stocks and just 80 basis points for bonds[1].

Respondents to our survey backed up those findings, with 58% indicating they have been allocating more heavily to dividend-paying stocks (versus 45% in 2020) and 26% adding to riskier credit investments (versus 22% in 2020).

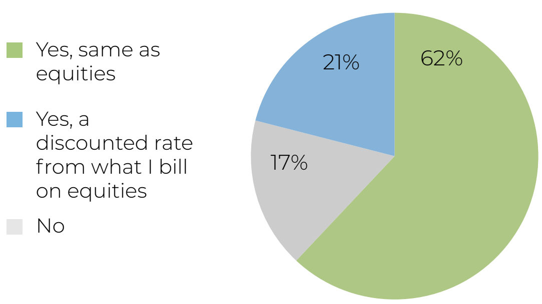
With the recent market volatility, what strategies have you employed to bridge the gap between your pre-retirees and retirees desired retirement income and the yield from their bond portfolios? Select all that apply.



The Fiduciary Dilemma of Disparate Fees

Low interest rates are having an impact on how advisors traditionally manage client assets and our survey revealed that interest rates are affecting traditional billing practices as well. Well over a third of respondents said they either charge reduced fees on fixed income assets or no fees at all.

Do you currently bill on fixed income?



Charging reduced or no fees on different asset classes creates a financial conflict of interest, akin to having different commission levels on products. This creates the perception that asset allocations or product choices may be guided by factors other than the best interest of the client.

At DPL, we have seen a similarly problematic compensation rationale whereby advisors believe they shouldn't bill on annuities because they require less management than other actively managed assets in the portfolio. This belief can lead to a reluctance to recommend annuities to clients who could benefit from them.

It is our strong opinion that the value fiduciary advisors bring to clients is their ability to deliver plans that achieve client goals rather than whether they are actively managing client assets. Advisor expertise and guidance is what clients pay for, regardless of the investment vehicles advisors use to deliver the best results.

It is fiduciary best practice to treat all assets equally, thereby avoiding even the appearance of a potential conflict.

[1] https://www.orionportfoliosolutions.com/wp-content/uploads/dlm_uploads/2021/02/advisor_insights_guide_winter_2021_pdf_0E1g8klU.pdf

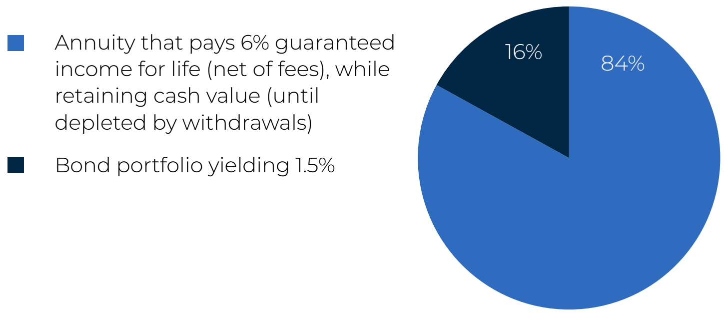
Attitudes Toward Annuities

"When you're a hammer, everything looks like a nail."

We continue to see advisors bring an investment bias to try to solve every problem with their investments-only hammer despite clear evidence that there are better solutions for some client needs.

A clear indication that this bias still permeates some corners of the advice industry was revealed in one question in particular.

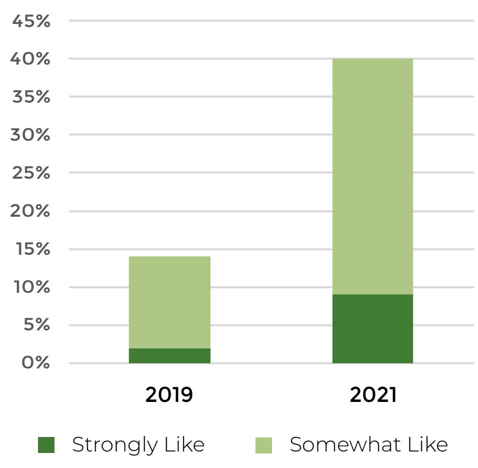
When choosing between the two options below, which would you rather choose?



For the third year in a row, we asked advisors if they would prefer an annuity that pays 6% guaranteed income for life (net of fees), while retaining cash value (until depleted by withdrawals) or a bond portfolio yielding 1.5%. The vast majority of respondents said they would take the annuity, while 16%—almost half as many as last year—said they would pick the bond portfolio.

Though this suggests that some advisors feel personally more comfortable with bonds - irrespective of whether that is the best solution for the client - there was strong evidence of a growing openness among respondents to the role annuities can play in generating income when bonds aren't up to the job. More than 38% reported allocating some client assets to an annuity, versus 29% last year.

What are your clients' attitudes towards annuities (2019 v. 2021)



This year's survey results indicate a general increase in the use of annuities, and a growing trust from advisors and clients alike may be why. Client attitudes toward annuities are shifting as illustrated by the over 26% increase in respondents since 2019 who said clients "strongly like" or "somewhat like" the products.

And, advisors are catching on that annuities shine in a low interest rate environment. Almost three quarters of respondents believe a low interest rate environment is a good time to use an annuity, an increase from 59% a year before.

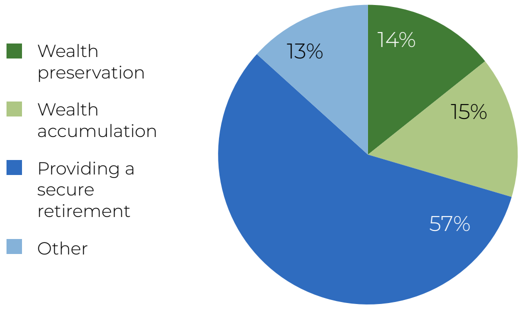
The upward trend in positive annuity opinions coincides with an increase in advisors' familiarity with different annuity products. Nearly half of respondents said they are "very familiar" with the various types of annuities, and 82% said they had a good working knowledge of both Variable Annuities and Fixed Annuities.

This begs the question: If advisors are familiar with annuity products and their uses, why aren't more using them when they have acknowledged that their clients want the benefits annuities provide?

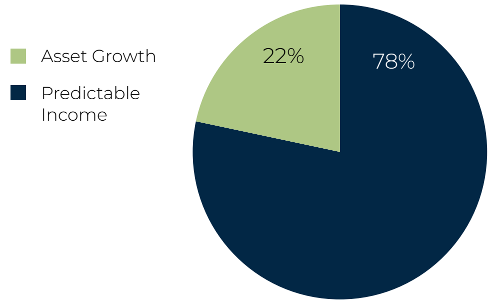
Advisor Perceptions of Client Needs & Financial Planning Practices

Advisors understand their clients' desires for secure retirement income. Over half said the primary job their client has tasked them with is providing a secure retirement, an uptick of 4% since 2019, and just under 80% said predictable income is more important to clients than asset growth, a number that has been consistent since 2019. Despite the lack of emphasis on asset growth, market-related anxiety grew once clients retired. Over half of retired clients, according to advisors, worried about portfolio performance more than they did before stepping down from their jobs.

As their financial advisor, what is the primary job your clients have tasked you with?



Generally, which is more important to your clients in retirement?

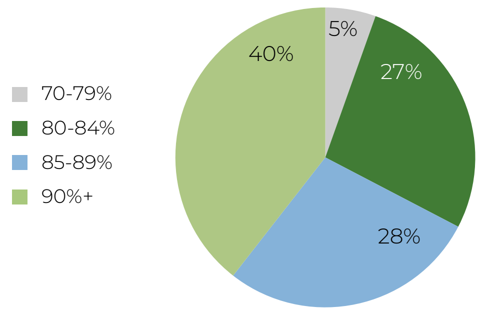


Most respondents said they create financial plans for more than three quarters of their clients over the age of 50 and the majority (52%) said they plan for a life expectancy of 90-95 years. Most advisors (72%) said they use goals-based planning software. More than half (60%) of advisors said they are comfortable with a Monte Carlo score of less than 90% for the financial plans they create for clients.

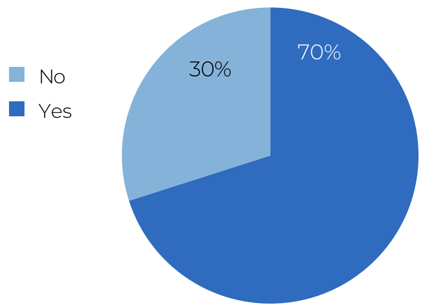
When asked whether they distinguish clients' essential expenses from discretionary expenses in the financial plan, most respondents (83%) said they do consider essential vs. discretionary expenses differently, up 10% since the previous year, and over two-thirds say they look to fund essential expenses differently, a jump of 18% since 2019.

However, their response to the follow-up question, "Apart from social security, how do you typically fund essential expenses?", suggests that while the majority of advisors distinguish essential expenses, they fund them using investments like they do for discretionary expenses. For these advisors, the distinction appears to be a data point rather than the driver of a funding strategy in the plan.

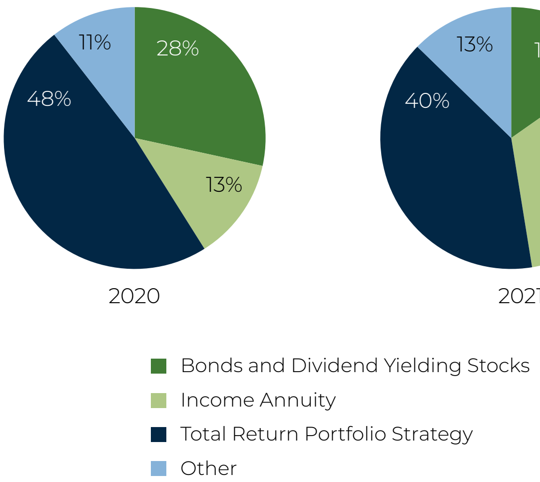
What is the ideal/target Monte Carlo score for your clients' retirement plans?



Do you look to fund essential expenses differently than discretionary?



Apart from social security, how do you typically fund essential expenses?



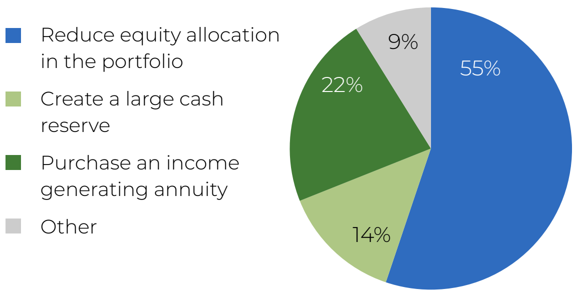
When we compare annuity usage to previous years we see a jump of nearly 20% of advisors who indicate they fund essential expenses with an income annuity from 2020 to 2021. This corresponds to a decrease in advisors who use bonds and dividened yielding stocks (-13% from 2020) and total return strategies (-8% from 2020 and -20% from 2019).

Though a move in the right direction, the percentage of advisors who limit themselves to investments only for income is disturbingly high as they are leaving retirees exposed to sequence of returns risk at a time when their portfolios may not be able to recover from a down market. Annuities are designed to solve for this risk.

Views on Equity Risk and Sequence of Returns Risk

As clients become more risk-averse when they approach retirement, advisors indicate they are taking steps to address their worries. In response to clients' reduced risk tolerance, most respondents said they reduced equity allocation in the portfolio. It's worth noting that the investments advisors are using to de-risk are riskier than fixed income like bonds that was traditionally used to rebalance retirement portfolios.

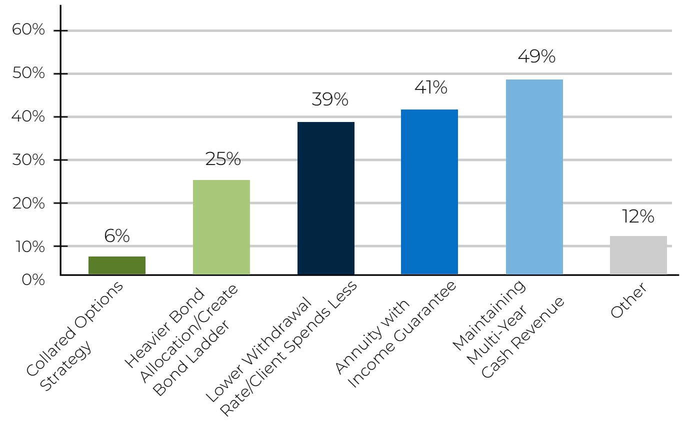
How do you adjust portfolios in response to clients' reduced risk tolerance?



When asked how they mitigate sequence of returns risks for clients, most advisors, just under half, responded that they maintain a multi-year cash reserve. While down 8 points from 2020, this long popular strategy is riskier given today's low interest rates when cash is earning negative real returns.

Though still not the top choice, purchasing an income generating annuity in response to clients' risk concerns has become more common; advisors choosing this option increased from 9% to 22% since 2020.

How do you mitigate sequence of returns risk for clients? Select all that apply.



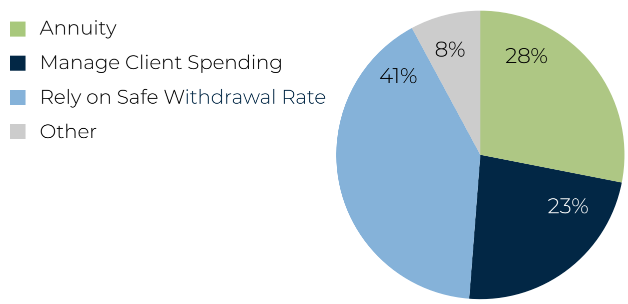
In fact, David Blanchett calls cash the riskiest asset in a portfolio because it locks in losses that can threaten the plans' overall success.

The number of advisors using an annuity with a guaranteed income rider has grown steadily in the three years since we started this survey and is now the second most popular choice with 41% of respondents choosing this option.

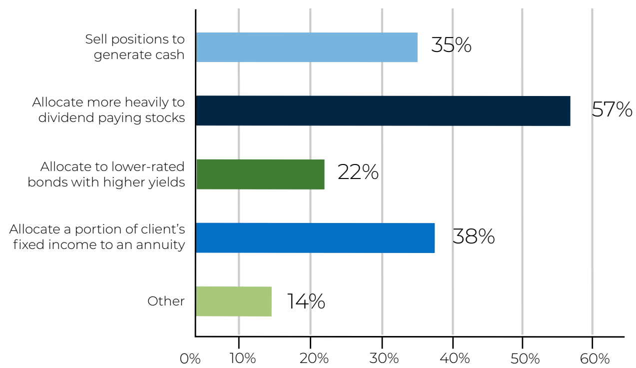
The responses to the question "How do you primarily address longevity risk?" shows a similar trend. Most advisors still rely on "safe" withdrawal rates, but this practice seems to have slowed, dropping 12% since 2019. And, advisors are increasingly turning to annuities, up 20% since 2019.

When asked about the strategies they have employed to bridge the gap between pre-retirees and retirees desired retirement income and the yield from their bond portfolios, 57% of respondents still opt to allocate more heavily to dividend paying stocks.

How do you primarily address longevity risk?



In a low-yield bond market, how do you bridge the gap between your clients' desired retirement income and the yield from their bond portfolio? Select all that apply.



This is yet another example of the disconnect between advisors saying they de-risk retirement portfolios while they continue to allocate to riskier investments in search of yield for income.

Annuity allocation is becoming a more popular option, however, with 38% of respondents indicating they allocate to an annuity to fill an income gap from low bond yields in 2021 compared to 32% in 2020 and 23% in 2019.

The products advisors say they have increased their usage of include Fixed Annuities (74%), Fixed Index Annuities (59%), Single Premium Immediate Annuities (56%), Deferred Income Annuities (46%), and Structured (Buffered) Annuities (38%).

Bond Market Yields and Approaches to Retirement Income

As noted previously, most advisors said predictable income was more important to their clients in retirement than asset growth. Interestingly, in a reversion to the trend two years ago, advisors seem to be planning for income and discussing it with clients a bit later in the relationship than in 2020.

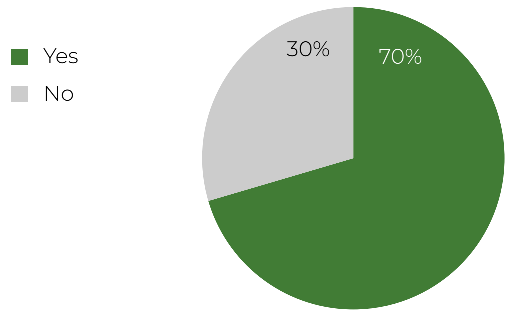
Also noted, while the majority of advisors allocate more heavily to dividend yielding stock to fund an income gap due to low bond yields, more are allocating to annuities for income than in years past.

Consistent throughout the survey, findings suggest that advisors are more aware of the benefits of annuities in this era of low interest rates, and more are using them.

Seventy percent of respondents understand that a low interest environment is a good time to use an annuity, up 11% from 2020.

And more advisors are exploring annuities as an alternative to fixed income, with 58% saying they have considered annuities, a jump of 17% since 2019.

Do you believe a low interest rate environment is a good time to use an annuity?

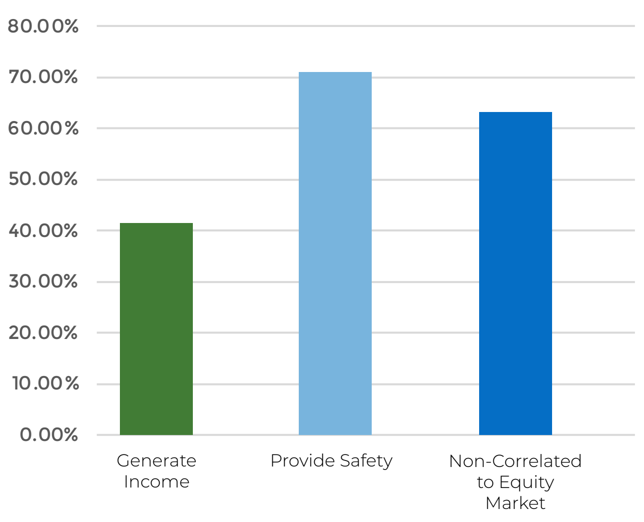


Despite an increase in annuity usage, findings suggest a cohort of advisors who are unaware or unaccepting of the benefits of annuities and the limitations of bonds today.

Only 67% of respondents are aware that leading academics and economists support annuities as a more efficient means of generating income than fixed income portfolios, despite evidence that some annuities can generate income as much as 40% more efficiently than bonds.

And, in response to a new question added to this year's survey about how advisors use bonds today, over 40% indicate to "generate income", and just over 70% to "provide safety" to the portfolio. While it is stunning that 60% of advisors don't view bonds for income anymore, it's equally surprising that 40% still look to them to generate income with yields where they are. A 40%-50% allocation to fixed income for retirees, just to provide safety and have some non-correlated assets in the portfolio, is inefficient and very, very expense insurance.

Traditionally, bond investments have been utilized to generate income, provide safety and provide non-correlated exposure to the equity market. Do bonds still serve these purposes today? Select all that apply.



As we strive to understand advisors' rationale for their appproaches to retirement planning, one belief is vital to take into consideration. When asked to comment on what they consider a "safe" withdrawal rate today, given that the "Bengen Rule" of 4% was identified in 1994, a surprising 50% of respondents said the rate is the same, and 18% believe it to be higher. Only 1 in 3 advisors believe it to be lower.

For perspective, Retirement Researcher Wade Pfau pegs the safe withdrawal rate today at closer to 2.3% before taxes and fees[1].

The delta between what some advisors believe to be a safe withdrawal rate and the rate academics support is concerning given the additional finding that 41% of respondents rely on safe withdrawal rates to manage longevity risk for clients. Twenty-eight percent use an annuity and 23% manage client spending.

The only way to safely address longevity risk is with an annuity, a product designed to deliver guaranteed income for the life of the client, even after the account value goes to zero.

[1] https://www.thinkadvisor.com/2020/04/14/wade-pfau-virus-crisis-has-slashed-4-rule-nearly-in-half/

Conclusion

RIAs are in a tough position. Traditional brokers are coopting their fee-only models but still enjoy the support and resources of their parent organizations (not to mention their insurance products and license). In the meantime, their clients are looking to them for secure retirement solutions in a world where bond yields remain near historic lows and many experts are predicting that equities are unlikely to deliver the outsize returns of the last decade plus, even as the risk remains the same.

Though searching for answers, many advisors seem unwilling to leave their comfort zone to find effective solutions. Coming to terms with interest rates and no longer billing on fixed income, they are using a traditional, investments-only approach to solve a problem investments can't adequately solve.

Without insurance and annuities in their retirement planning toolkit, RIAs are replacing the trusty old bond with riskier investments and ever more complicated strategies to deliver income that can include dividend stocks, and alternatives like convertible arbitrage, REITS, SPACs, and more. What must this presentation sound like to clients who are looking for secure income? And for clients in poor health or cognitive decline, how must it sound when their advisor says "trust me" then tells them they'll be expected to adjust their spending each year for the rest of their lives based on market performance?

While this year's survey reveals more advisors are using annuities, many "fiduciaries" continue to employ strategies that increase risk in retirees' portfolios while disregarding more secure solutions that are readily available to them. We can't help but wonder: How bad will it have to get before advisors are willing to update legacy strategies that no longer work today, and expand their retirement planning toolkit to include solutions that can give clients secure, predicable income they say they want?

Commission-free annuities provide safe, efficient income and are backed by extensive academic research supporting their use for income in retirement. While we are encouraged by signs from this year's survey of a growing openness to consider insurance products for their clients, advisors' hesitancy to use annuities for income—the very purpose for which they are designed—continues to be a concern.

We understand that many RIAs have been running their business one way for 20+ years and are worried about the changes taking place in the industry that may necessitate they change as well . DPL is committed to educating advisors about today's new generation of commission-free annuities and helping them leverage these products to bring effective, fiduciary solutions to their clients that will in turn strengthen their firms.

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