Inflation, inflation, inflation

Tom Murray explains how equity release can support those with low or fixed incomes throughout the cost of living crisis we are currently witnessing

One word will dominate everything we read in the financial press for the next 12 months; that word is inflation. The increase in the inflation rate has been well reported over the past 12 months, and forecasts predict that this increase will quicken as we head into winter, reviving the bogeyman of the 1970s.

Everywhere one looks or listens, articles and programmes discuss ways to reduce your outgoings, whether by insulating your home to reduce energy expenditure or changing where you shop to get more bang for your buck.

The talk of an Armageddon in the cost of living is everywhere.

After decades of high economic growth in a low inflation environment, the effect of rapidly rising prices was bound to shock the general population, many of whom would not have experienced these conditions before. The spiralling rise in the cost of living, and the fear of it increasing exponentially for many months to come, is driving increased demands for wage rises to help meet these expenses.

The airwaves are filled with calls for Government intervention to moderate or offset increases in the cost of essential goods, and the situation is creating a general sense that all is not well with the world.

Vulnerable citizens

Those who are likely to suffer most when prices rise rapidly are the people on fixed incomes. In particular, the situation will be difficult and even frightening for pensioners. They are not in a position to increase their income by looking for better paid work or increasing their working hours as those currently in the workforce may be. While the Government's triple lock will ensure a substantial rise next year in the state pension - it is guaranteed to be the higher of average earnings, 2.5% or CPI, and CPI will almost certainly win this race – but this won't come until April 2023.

Between now and then, there looms a long, hard winter of rising prices and even higher energy costs that will be very difficult for pensioners to cope with.

Many are afraid of the bills associated with heating their homes and could be tempted to leave off their heating when they really need to be heating their homes or cut back on food and other essentials to make ends meet. This is not the situation we expect to find pensioners in, in what is one of the wealthiest countries in the world.

Rich in bricks and mortar

Yet, in the UK, pension wealth is far lower than property wealth among those over 65. Research by Opinium in 2017 showed that the amount of property wealth held by those over 65 was almost five times as high as the pension wealth held by the same group (£1.6 trillion v £336 million).

It is a tragedy that pensioners could end up shivering in the cold while surrounded by their biggest asset – their house. Yet ironically, that may well be the case for many pensioners this winter, who will risk hypothermia or cut back on food as the cost of living rises.

Tapping one's assets

There are already products on the market designed to allow people to tap into their property wealth. However, these products have historically had a low level of take-up. Given that pensioners are no longer working and cannot increase their income, it seems bizarre that more of them are not seeking to use the largest asset they own to support themselves in their old age.

But there has always been a marked reluctance among older people to use equity release type products to gain access to the wealth inherent in their residence.

Fear of the unknown

There are a number of reasons for this. Firstly, there is a general lack of understanding about the product. One of the things that people in retirement like about owning their own home after having paid off their mortgage is the sense of security it gives them. Releasing the equity by taking out a lifetime mortgage seems like taking a big risk with that security.

They have spent so many years paying off the mortgage while employed and fearing losing their job in case they lost their home, that taking out a lifetime mortgage seems to be risking putting them back into the same position. The fact that they will never lose their house under a lifetime mortgage isn't well known enough, so they are wary of taking one out.

This reluctance to take on 'debt' in retirement is admirable. Still, it is an area that consumers need to be helped with, with advice focused on the difference between a lifetime mortgage and standard debt.

This is where the ability to get proper financial advice is crucial to a good outcome.

Educate advisers

This brings us neatly to the second issue. Not many financial advisers are actively considering equity release when drawing up retirement plans for their clients – only about one in 10 are, according to a recent report by Lang Cat. There needs to be a major education programme if there is to be an increase in the number of people properly considering this as part of their life plan.

This dearth of advisers considering equity release as part of a solution is compounded by the fact that so few people are currently getting financial advice as they approach retirement. General guidance rules provided freely by the Government and independent websites rarely mention the possibility as a suitable option.

Suppose those approaching retirement, or those already in retirement, are seeking to increase their drawdowns to cope with rising costs. In that case, if they are to get an accurate picture of their financial options, consumers must be able to properly consider the possibility of accessing the value of their house.

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Party time?

Thirdly, many people who do buy equity release products tend to do so for big single purchases. They use it to pay off outstanding debts when they retire or for one-off projects such as building a conservatory or taking a cruise. While there is nothing wrong with this, it is missing the opportunity to see equity release as an option to provide pensioners with a better lifestyle across their retirement.

This could be based on the quality of advice they are getting or indeed not getting (see the previous point).

But to get people thinking like this requires a mind-shift in the approach to equity release. Because it is essentially about large sums of money, people tend to think about it in terms of buying large items or making major changes to their homes. The concept of drawing it down in smaller instalments and using it to supplement their pension is not widespread.

However, it could be vital in ensuring a relatively comfortable lifestyle during a downturn like the one we are facing. Retirement planning needs to be thought of in terms of meeting the gas and electricity bills, rather than spending the winter in the Caribbean.

While a once in a lifetime holiday is a great idea and can seem to be a just reward after a lifetime of toil, pensioners face many years in a high inflation environment. Unfortunately, the purchasing power of fixed pensions will be rapidly eroded by high levels of inflation, and we need to think of the bigger picture when planning for the future.

Passing (it) on

Finally, there is the issue that many people wish to pass their property on in their will. This inheritance is a huge motivation felt by much of the population, particularly about houses. Successive Governments have been afraid to tackle it, as shown by the various approaches to providing care that have been suggested. Many of these put a cap on the amount that can be funded by the residential property belonging to the customer as if the ability to pass on one's property wealth was somehow sacrosanct.

However, if the pensioner had accumulated an identical amount in investments rather than residential property, they would be expected to contribute to their own day-to-day living costs, and the Government wouldn't support them. The question must be asked, why should a property be regarded in a different light? Tapping into that wealth to provide for one's day-to-day living costs is a natural use of the money and, therefore, shouldn't be seen as somehow immune to the process.

Regulate and recommend

Clearly, there is risk involved in equity release, just like there is with any financial product. That is why there needs to be stronger regulation of the area by the FCA accompanying a push to ensure that IFAs and guidance, in general, raise the possibility of tapping into that wealth with pensioners and those approaching retirement.

The industry, Government and regulator need to sit down and work on an approach that actively promotes the use of equity release to support those with low or fixed incomes throughout the cost of living crisis that is currently happening and shows no sign of abating over the next two years. Without a straightforward centralised approach to the problem, pensioners will suffer unnecessarily, and alleviation of their plight will land entirely on the taxpayer while the accumulated wealth of their working life remains intact.

Tom Murray is Head of Product Strategy at Majesco