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Securing retirement incomes — A growing global challenge

The importance of a well-functioning retirement system simply cannot be overstated.

There are a whole host of sobering statistics that highlight why a sustained focus on getting retirement "right" in all countries is paramount. Across the Organisation for Economic Co-operation and Development (OECD) countries, the old-age dependency ratio (people aged 65+ per 100 working-age individuals) has risen from about 21 in the 1990s to around 33 today and is projected to reach roughly 55 by 2050.[1]

As highlighted in Mercer's 2025 paper, *Future-Proofing the Longevity Economy* (which was written in collaboration with the World Economic Forum as part of our Longevity Economy Series), the traditional balance between the years spent in productive employment and in retirement is rapidly becoming unsustainable. This demographic shift is placing a growing strain on pension systems globally, making it increasingly critical for them to provide adequate and sustainable income in retirement. It has elevated this issue to become a key economic and social policy concern.

At the same time, we are seeing personal and occupational defined-contribution (DC) pension plans becoming an increasingly dominant source of an individual's income in retirement, replacing occupational defined-benefit (DB) plans. The OECD notes that "more than 50% of assets were held in either (occupational) DC plans or personal plans in 19 out of the 21 reporting OECD economies."[2]

While employers still play an important role in offering DC occupational pensions, there is undoubtedly a significant individual responsibility under this model, and the implications of this are far reaching. Leveraging Mercer's on-the-ground experience of advising on pension schemes and systems (across the globe over many decades), this paper highlights that there is more that binds us together than separates us when it comes to navigating this issue.

We recognize that every country's retirement system has evolved in its own distinctive way and that there will be inevitable nuances to consider for each. To help anchor discussions on this topic, we consider the key challenges facing retirees. We also look at the importance of having solutions that are aligned with what we know tends to matter most to retirees.

In the context of a world where personal and occupational DC pension plans increasingly dominate, this paper homes in on the common challenges that are faced (and the solutions that are typically available) once an individual has stopped working (often referred to as the "decumulation" or "post-retirement" phase). This is a critical phase in the retirement journey and warrants significant focus and debate globally.

[1] OECD, 'Pensions at a Glance 2024'.

[2] OECD, 'Pensions at a Glance 2024'.

Retirement income — how much is enough? How long does it need to last?

These questions get to the heart of income adequacy and income sustainability — crucial aspects of an individual's security in retirement.

With retirement systems that have (for the most part) been historically dominated by DB arrangements, these questions have been primarily the domain of employers and actuaries (as they determined the costs associated with providing people with a defined income for life). In a DC context, answering these questions is primarily the responsibility of individuals. This can be a daunting prospect for many people as they are forced to contemplate issues that they are arguably ill-equipped to deal with. William Sharpe, famed creator of the Sharpe ratio, described the retirement challenge as "the nastiest, hardest problem in finance," which gives a sense of the scale of the task at hand.

Income adequacy — the question of "how much is enough" is largely subjective. However, a helpful yardstick has been provided by the emergence of retirement living standards (in countries such as Australia, the UK, and Ireland). These set out absolute levels of income that are needed to meet different retirement lifestyles.

Income sustainability — naturally, retirees want the security that their income is going to last as long as they do. However, given current post-retirement life expectancies, this is becoming an increasing concern.

It is clear that income adequacy and sustainability are inextricably linked and that the retirement solutions most likely to succeed need to consider them both in tandem.

The retirement challenge

Before considering the types of solutions that retirees might need, it is important to anchor ourselves with a clear understanding of the main finance-related risks that need to be navigated by retirees once they have stopped working, as well as the features we know to be universally important. These are:

- **Longevity** — the risk that a retiree outlives their savings.
- **Market** — the risk that a retiree loses a significant portion of their savings due to a sudden fall in investment markets or a prolonged period of poor returns.
- **Inflation** — the risk that inflation diminishes the real value of a retiree's savings.

Set out below is a list of those things that retirees around the world typically list as desirable features when it comes to accessing their savings in retirement. It is important to recognize the inherent conflict between many of these features and the inevitable variation in needs and preferences between specific retiree populations.

Naturally, the emphasis placed on any one feature in a given country can be heavily influenced by factors such as home ownership rates, state income (including both the level of the state pension and the long-term sustainability of the state system), retiree inflation (e.g., senior care costs), and the health care support available in retirement.

Stability of income — there is good evidence from more mature DC markets that retirees tend to rank stability (if not certainty) of income near the top of their list of priorities in any retirement solution. This is consistent with research pointing to people becoming more risk averse as they age.

Access to savings — as a retiree's circumstances change, having the flexibility to access or change the structure of their retirement savings (if required) is always preferable. The ability to meet unexpected expenses if they arise is also important.

Potential for capital growth — although this requires taking on some degree of investment risk, capital growth is generally needed to generate returns that support an adequate retirement income. Volatility in capital is undoubtedly unwelcome and causes financial stress. However, the ultimate risk is an extended or permanent fall in the pension's capital value.

Easy to understand — retirees tend to have a preference for retirement strategies that have a low complexity, are transparent, and can be communicated easily. For many people, the dynamics around understanding will likely change as they age.

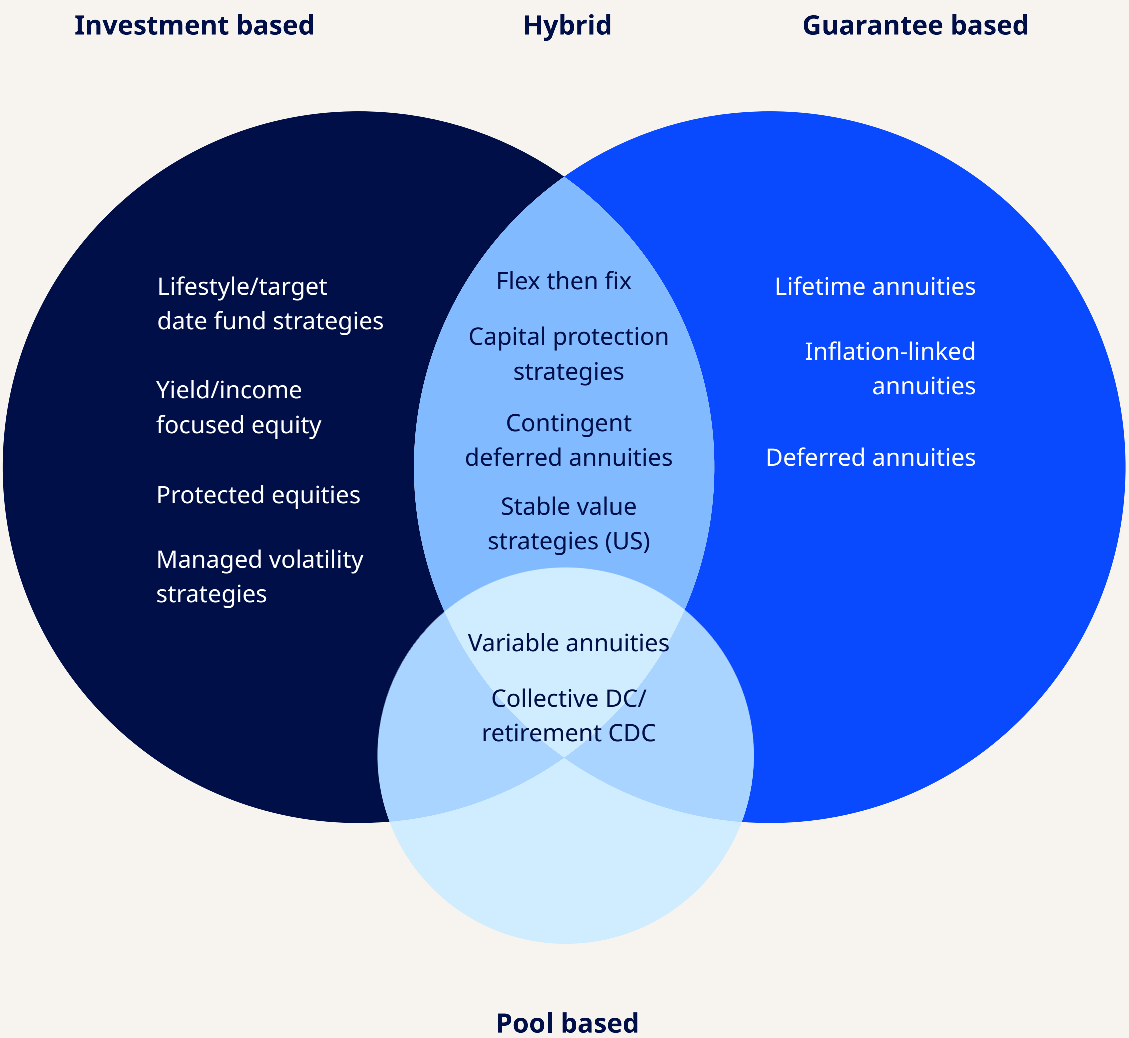
Low costs — solution development in the retirement phase will need to consider a complex set of factors that are, perhaps, less of an issue in the accumulation phase. Innovation is clearly important, however, the cost sensitivity of retirees and the likely benefits of scale must be borne in mind.

Retirement strategies

There is a growing range of retirement strategies that seek to address the key objectives of retirees in different ways.

Figure 1 highlights the range of retirement strategies that we have typically seen emerge in different countries around the world. Some of these solutions are country specific in terms of their popularity and usage. However, they all broadly fall into one or more of three categories: investment-based, guarantee-based or pool-based strategies.

Figure 1 Spectrum of retirement strategies



For illustrative purposes only.

Investment-based strategies — involve allocating capital across asset classes and instruments to achieve specific financial objectives, while managing risk, liquidity, and time horizon constraints.

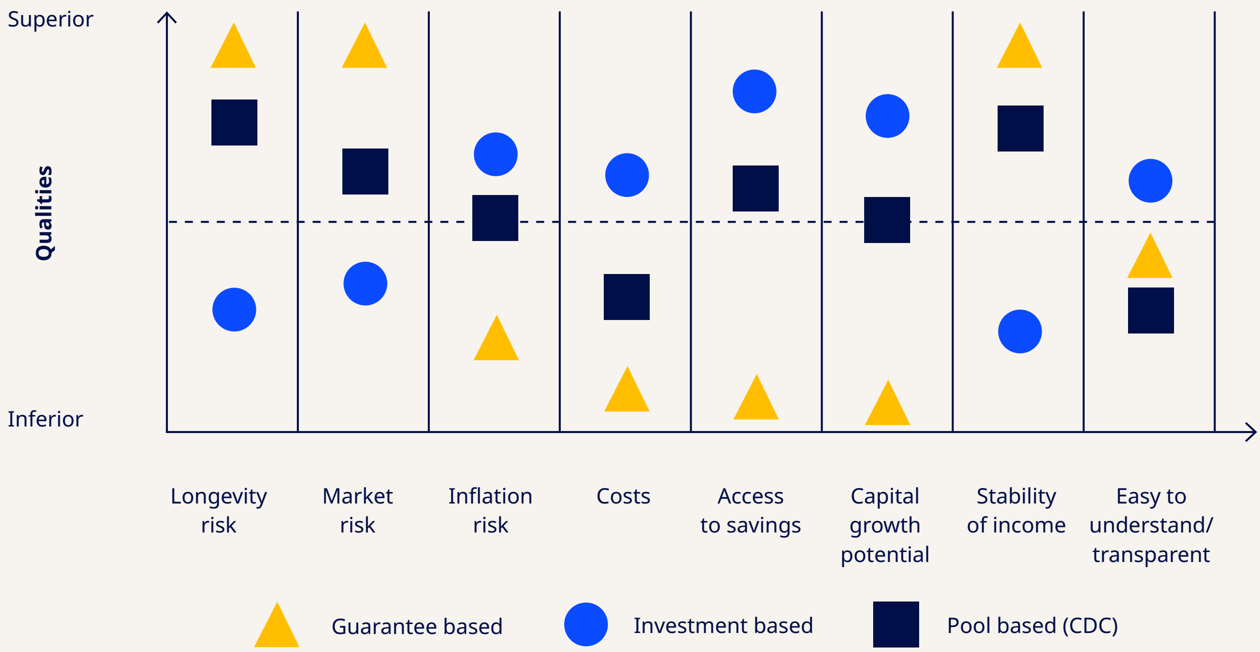
Guarantee-based strategies — typically involve a lifetime annuity. This is an insurance contract that, in exchange for a lump-sum premium, provides the purchaser with regular, guaranteed payments for the remainder of their life.

Pool-based strategies — involves a collective arrangement that aggregates contributions from many members into a single fund to provide retirement income or benefits. This approach shares longevity, investment, and administrative risks across the pool to seek cost efficiencies, smoother outcomes, and improved diversification.

This paper does not delve into the detail on any of these specific solutions, but Figure 2 helps us consider how each of the broad categories fare when held up against both the key retirement risks that have to be navigated and the (previously noted) features we know to be important to retirees.

Of course, the analysis set out in Figure 2 is qualitative in nature and we recognize there could be different types of solutions utilized under each category, which might result in a different relative score on any given measure. For the purposes of this comparison, we have broadly assumed the following solutions: Investment-based (Lifestyle/target date fund), Guarantee-based (Lifetime annuity) and Pool-based (Retirement collective DC).

Figure 2 Comparing retirement income strategies



For illustrative purposes only.

As illustrated in Figure 2, trying to design a retirement solution that simultaneously addresses all the risks and preferences of retirees is challenging. In some instances, this will be resolved by considering individual preferences or product availability. Consensus is growing in some markets that combining solutions from different categories may best serve the needs of retirees over the long term. Obviously, considerations in this regard are complex. However, the power of pooling (in one form or another) is clear. It allows individuals to share key longevity and market risks, which they would otherwise need to navigate alone. This approach is being introduced or explored in detail in some markets.

Key themes and insights across regions

Based on our experience across different regions and over multiple decades, we see several themes and insights that we believe should be front of mind when designing solutions for retirees.

Alignment

In any retirement system, it is possible to create innovative solutions that are thought to be in the best interests of individuals. However, unless they align with the preferred features of what people actually want, they are unlikely to receive broad-based support.

State support

The availability of state support for income and health needs in retirement can be hugely influential in shaping the "best fit" solution for any given country. However, rapidly changing demographics may materially change the support available for future retirees, which complicates this consideration for current employees.

Advice

The role of financial advice is key. However, a universal challenge across all retirement systems is making this advice available to retirees at scale and at an affordable level.

Digital

While innovation in product design for retirement solutions might capture more headlines, technology advancements are also helping to revolutionize how DC plans and their members interact (particularly when accessing guidance and/or advice).

We believe the best digital solutions are those that consider the viewpoints, preferences, and skill-sets of all cohorts of retirees.

Future of work

In many economies, work is evolving and the concept of retirement is also changing. We believe the best DC pension arrangements should therefore support flexibility in working patterns and preferences. They should also allow the easy aggregation of a lifetime of different retirement accounts.

Pooling

When navigating one's income needs in retirement, the ever-increasing shift of responsibility to the individual is significant. As a result, the potential advantages of enabling individuals to pool together when navigating risks such as longevity is becoming key. Pooling is now playing a big part in how some retirement structures are evolving.

Complexity

Today, designing solutions to help people access their income throughout retirement requires consideration of a more complex set of factors (relative to the accumulation phase). This is an area where inherent conflicts often exist. To date, the global debate has been skewed towards accumulation. We strongly believe that more balance is required.

Summary

In light of the demographic and societal trends shaping our future, the need for a robust retirement income system has become increasingly important. Mercer has considerable experience with advising on (and designing) retirement solutions around the world. This helps us to better understand why different ideas and norms in retirement systems have taken hold over the years. Equally, learning from our local experience helps us to bring a more holistic perspective when reflecting on many of the common themes (listed above) that run through all retirement systems.

We know that regulatory backdrops and culturally entrenched practices can be hugely influential in shaping how a given country's retirement system evolves, as can the maturity of the DC market in a country. The high-level frameworks set out in this paper (where we consider the key risks and preferred features of any retirement solution) are intended to provide an anchor to discussions in any country or region.

Securing the retirement incomes of future generations is a growing and global challenge. Our ongoing work with the Mercer CFA Institute Global Pension Index highlights both our commitment to meeting this goal and our desire to lead research and discussions on this crucial topic.

The size of the DC market is growing rapidly, and, as this paper has illustrated, the issues faced by individuals as they save, plan for, and manage their retirements are significant. We believe it is crucial that the regulatory background and market solutions available continue to evolve. This should happen in a way that helps to ensure the primary goals of adequacy and sustainability are recognized and delivered for current and future retirees.

Find out more

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