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The new pension landscape

Pensions Policy Institute

Venue: The Chartered Insurance Institute, 20 Aldermanbury, EC2V 7HY

29 November 2016

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Presentation structure

- 2003 landscape report
- Policy changes 2003-2016
- Landscape changes 2003-2016
  - Pensioners
  - Savers
  - Government finances
- Future outcomes
  - Pre-retirement individuals
  - Age 50-SPa cohort
  - Government finances
- Summary and conclusions

2003 pensions landscape

- 10.8 million pensioners typically better off than 1994
  - £11,700 median income AHC (2015 prices)
  - 45% real increase since 94/95
  - 64% receiving private pension income (up 7 points)
  - Average real income from pensions up 36% to £5,100 (2015 prices)
- However:
  - Gap between rich and poor pensioners widening
  - 25% pensioners living in relative poverty
- Prospects for future pensioners less rosy
  - State pension not linked to earnings
  - Employer commitment to pensions weaker
  - Pension participation stalled / falling
- Uncertain prospects and unclear responsibilities

Policy timeline 2003-2016

Simplification, sustainability, choice

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2003

2006
A-day changes

2010
State pension changes

2011
Triple lock

2012
Automatic enrolment

2012
A/E delayed uplift

2014
Changes to public sector schemes

2015
0.75% charge cap

2015
Pension freedoms

2016
Tax allowance changes

2016
Changes to SPA

2016
New state pension

2016 pensions landscape:
Pensioners benefit from triple lock and private pensions

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- 13 million pensioners typically better off than in 2003
    - £15,400 median income AHC (2015 prices)
    - 30% real increase over 12 years
    - 72% in receipt of private pension income (up 8 points)
    - Median of £7,400 (gross) private pension income
    - Age of withdrawal from work rising and younger pensioner units more likely to be in receipt of earnings from employment
- However, 13% living in relative poverty and incomes from investments hit by low interest rates
- New retirees face more complex set of choices in an embryonic market for retirement income
    - Widespread use of the new pension freedoms
    - Supply of new products and scheme drawdown still developing

2016 pensions landscape:

Employee participation up but concerns about exclusions and contribution levels

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- Around 18 million working age people engaged in workplace pensions – more than ever before
- Gaps between public and private, male and female and younger and older participation have all narrowed (or reversed)
- However, 5.3 million employees and 4.8 million self-employed remain ineligible for A/E (but can opt in)
- Median contribution levels to DC have declined as large numbers of new joiners contribute the minimum
- Total 'normal' pension contributions rising again but in 2014 were still lower than 2005 levels
- Lower charges, better governance, growth of Mastertrusts and GPPs

2016 pensions landscape:
Rising benefit expenditure, rising tax receipts from pensioners, flat tax relief

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- Rising number of pensioners, triple lock and increase in disability and attendance allowances
  - Spending on pensioners 68% of all benefit spend
  - 37% rise in real terms since 2003 report
  - £118 billion and 6.2% of GDP in 2015/16
- Tax revenues from pensioners rose by 60% in real terms from 2002/03 to 2014/15
- Cost of tax and NI relief rose steeply between 2003 and 2011 but then fell slightly in real terms
  - Lower allowances limiting contributions from higher earners
  - Automatic enrolment not yet fully implemented

Outlook for future pensioners mixed, particularly younger
Automatic enrolment compensating in part for changes to state pension

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- Policy changes of past 13 years look set to improve retirement outlook for many 'hypothetical' individuals
  - All who qualify for state pension benefit from triple lock (recent years and future)
  - For most hypothetical individuals triple lock offsets reductions from other policy reforms such as rise in SPa
  - Younger without private pensions in baseline benefit most from automatic enrolment but get less from new state pension
  - Pension freedoms leading to uncertain retirement incomes for those with DC pensions
- Cohorts approaching retirement have generally benefited from recent policy changes
  - Women have benefited more than men and gap has narrowed
  - Those aged 50-59 in 2010 gain more than older members of the cohort
  - However, younger members of cohort projected to have lower overall retirement incomes than those closer to SPa

Automatic enrolment boosts the income of the median earning woman

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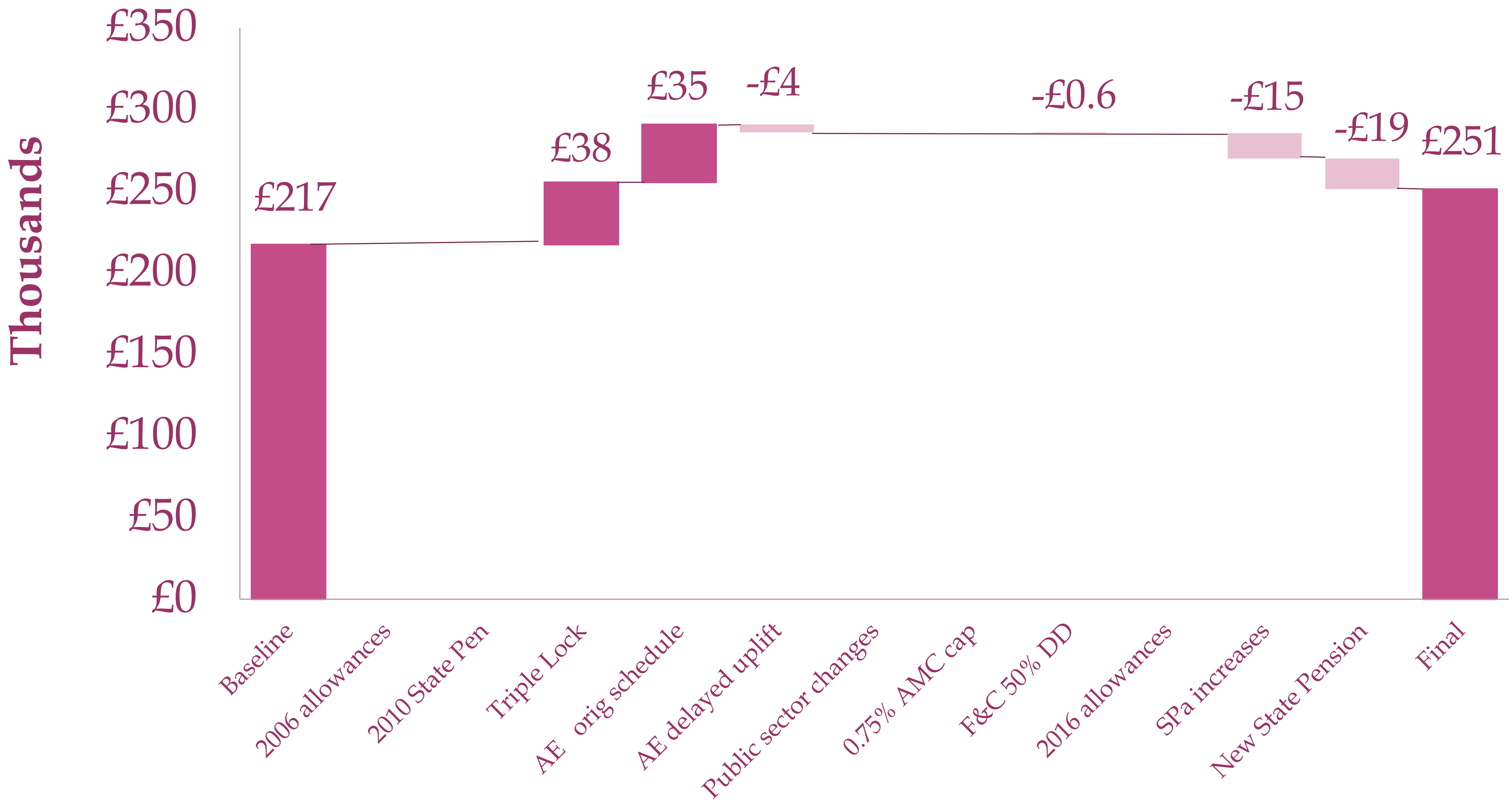
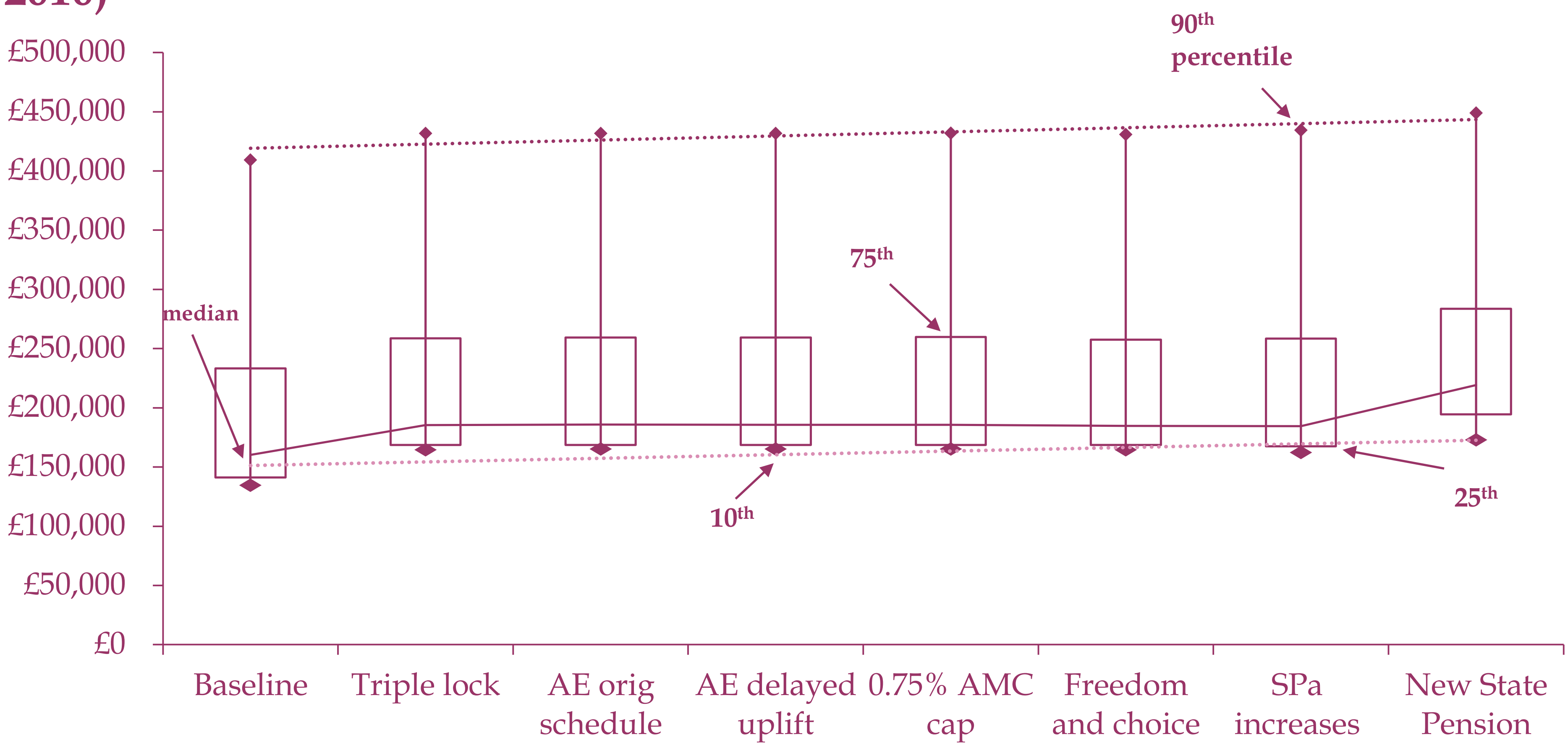
Impact of changes to policy on total post-retirement income of a woman currently aged 45 and earning at the median level in the private sector [individual 20]

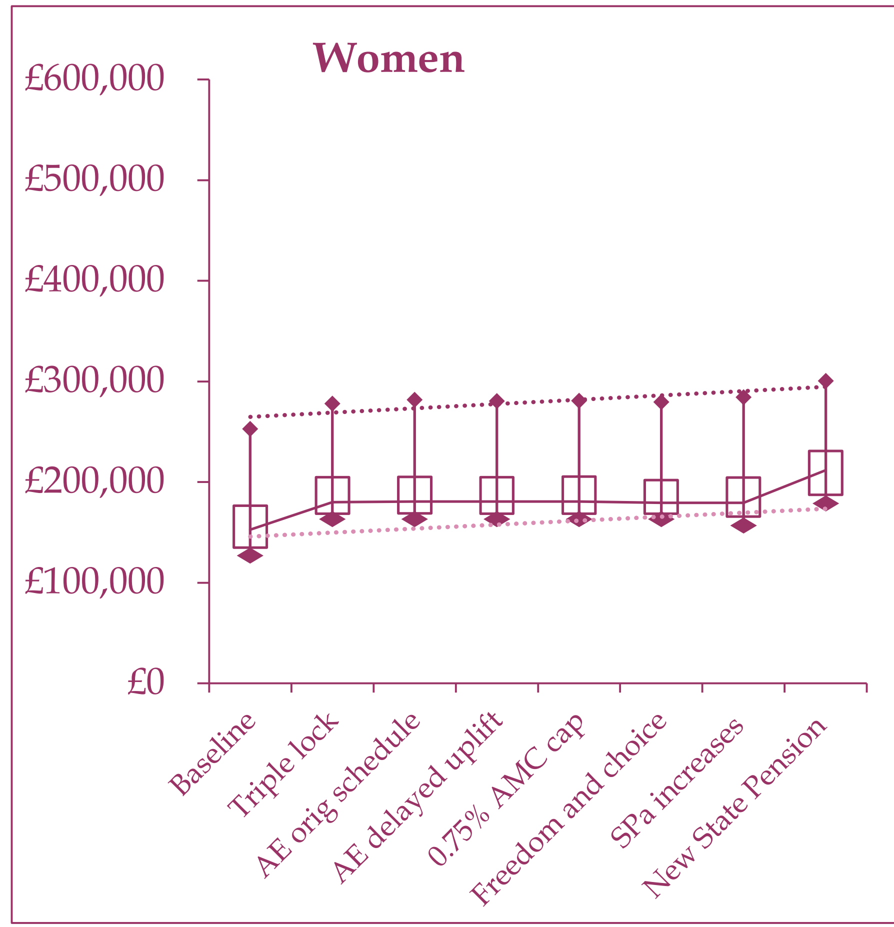


The changes between 2010 and 2016 have increased incomes most for those in the middle of the income distribution

Distribution of post-retirement incomes for entire sample (aged 50 to 64 in 2010)



Women have experienced greater increases but continue to have lower incomes than men



While older cohorts have higher baseline incomes, younger cohorts are projected to experience greater increases

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Baseline and final incomes by age cohort

Age	50 to 54	55 to 59	60 to 64
Baseline income	£132,800	£156,300	£205,300
Final income	£212,700	£219,200	£232,400
Absolute increase	£79,900	£62,900	£27,100
Percentage increase	60%	40%	13%

Government spend on state pensions increases but other costs projected to fall

- Rising numbers of pensioners, new state pension and on-going triple lock could see cost of state pension rise to 7.2% of GDP by 2046
  - Cost of triple lock partially offset by rising SPa
- Triple lock and new state pension bring significant reduction in spend on pension credit from 0.72% to 0.09% of GDP
- Net cost of tax relief projected to fall from 1.2% to 1% by 2046
  - Increase of 0.2% triggered by automatic enrolment
  - Offset by reduction of 0.4% by changes to public sector pensions
- Public sector reforms and changes to SPa reduce spend on pubic sector pensions from 2.1% to 1.6%

In 2046, both the triple lock and the SPa increases affect proportion of GDP spent on state pensions

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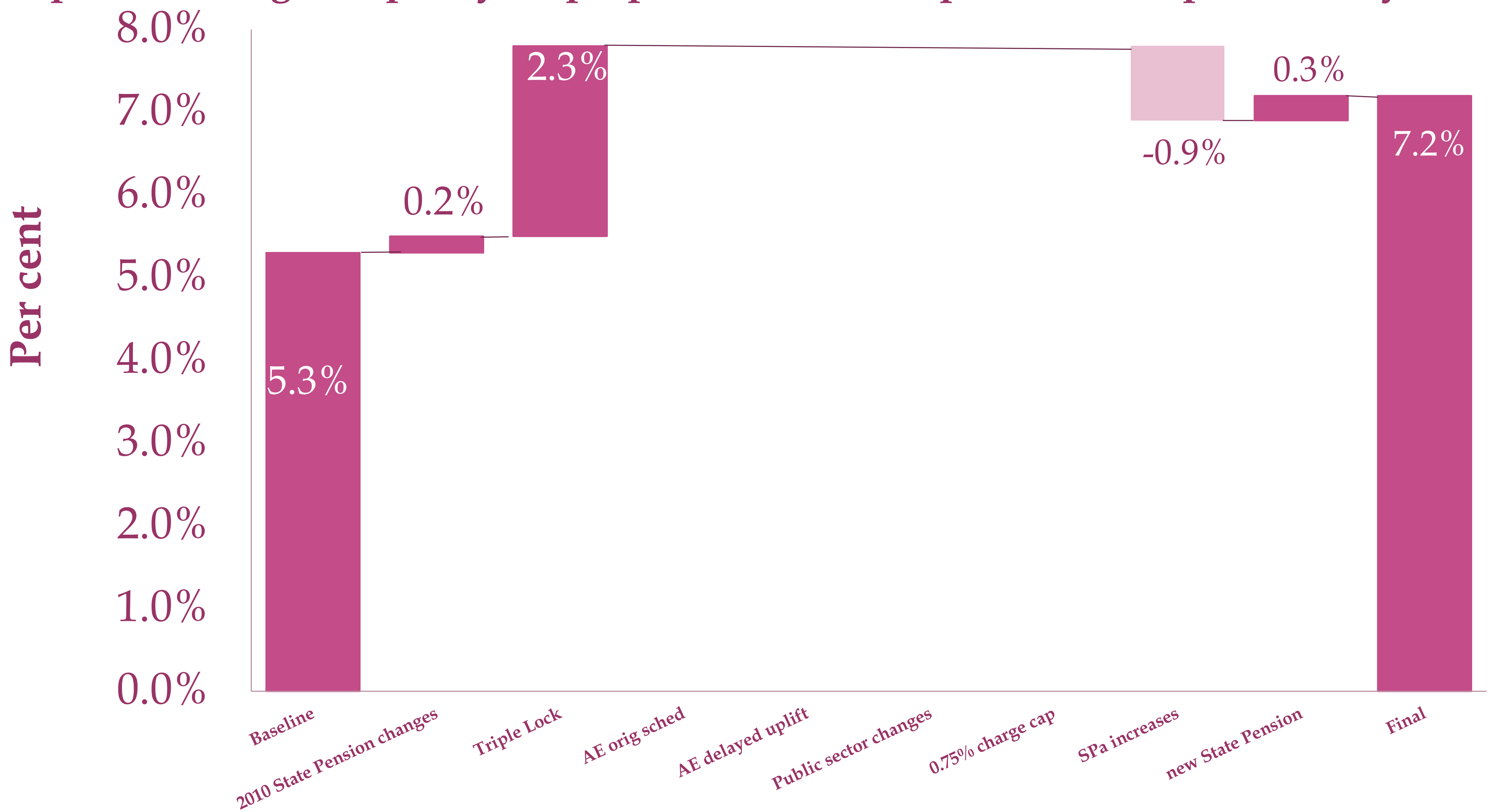
Impact of changes to policy on proportion of GDP spent on state pensions by 2046



Thirteen years of reform provide a strong platform for future

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- Many of the concerns from 2003 have been addressed by the policy changes since then:
  - Clarity on responsibilities flowing from Pensions Commission analysis and recommendations
  - Significant increases in incomes for pensioners and reduction in pensioner poverty
  - Falling levels of participation in workplace pensions have been reversed and surpassed with introduction of automatic enrolment
  - Mastertrusts have introduced new choices for employers setting up qualifying arrangements
  - Changes to governance, charges, default investment strategies should all improve prospects for younger generations
  - Improvements in working lives among older people helps sustain incomes up to and into retirement
  - Pension freedoms provide scope for more flexible retirement incomes suited to new retirement patterns

However, there remain some concerns and uncertainties

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- Pensioner poverty has not been eradicated
  - 1.6 million still in relative poverty: more commonly women and older couples
  - Depressed interest rates continue to limit scope for income from savings
  - For some years to come, state pension will continue to represent bulk of retirement income for many
- Future pensioner prospects also uncertain
  - In spite of automatic enrolment, total 'normal' pension contributions have not yet reached 2005 levels
  - Impact of LISA and increasing automatic enrolment contributions on opt-out levels uncertain
  - Future DC pensioners faced with uncertain prospects for investment returns as economies recover from financial crisis
  - UK employment and income prospects uncertain in face of UK exit from EU
  - Responses to the new pension freedoms from savers, schemes and providers a significant unknown that could transform (for good or bad) future retirement incomes

Clear priorities for future pension policy

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- Continued focus on principles and responsibilities established following Pensions Commission
- Monitoring and evaluating:
    - whether the current projected levels of automatic enrolment contributions are sufficient to deliver adequate retirement incomes
    - the impact of the pension freedoms on retirement incomes, pensioner poverty and means-tested benefits
    - the response of schemes and providers to the pension freedoms and consumer access to solutions
    - the impact of publicly financed retirement guidance and the availability, suitability and affordability of regulated advice
    - the impact of the Lifetime Individual Savings Account (LISA)