

Introduction

In any pensions-related debate, the demographic number that usually gets most attention is the increasing support ratio: the number of people over state pension age whose pensions need to be 'paid for' by each person of working age. But there is an arguably more important set of numbers that tend to get overlooked. These are just as important in the cost of pensions, and are more important to everyone's individual life prospects. These numbers are:

- What chance do we have of living to start collecting a pension at age 65?
- How long can we expect to then collect a pension for?

This Briefing Note updates an earlier PPI analysis¹ of these questions using the latest projections of future longevity². These are on a cohort basis which means that the prospects for each generation can be shown separately. They show that lives are going to be longer than people expect. And as such projections have always turned out to underestimate longevity improvements³, actual experience may turn out to be even better than these latest figures suggest.

Living to 65

Our state pension system was not designed so that everyone should receive it.

Of the generation who would reach age 65 in 1950 and benefit from the start of the new 'Beveridge' system, many died before reaching adulthood. A good measure of who might expect a pension is the proportion of those who, having got through the hazards of young life to, say age 25, then lived through working life to age 65. Only just over 60% of the 'Beveridge' generation did so. (Chart 1). This illustrates that the state pension was never intended to be a benefit which everyone would have, as if it were a private savings pot.

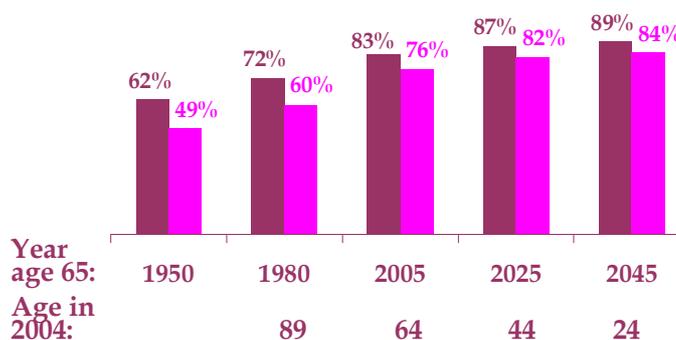
Better health and lower death rates mean that each successive generation is more and more likely to reach age 65. Men now in their 40s are nearly 90% likely to live to collect state pension – and the likelihood is over 90% for women.

So nearly everyone can now expect to receive some pension: which makes sense for private savings schemes but not necessarily the state insurance benefit.

Chart 1 also shows a striking rationale for increasing state pension age.

Chart 1: More people live beyond 70 than used PPI to live beyond 65

Proportion of men expected to live from age 25 to age 65 and to age 70



It was intended to be insurance for those who lived long enough to need a basic income from the state, in the expectation that those over 65 would not be earning.

It is as likely that today's forty-somethings will survive to 70 as it was for their parents to survive to age 65; and more likely than their grandparents to live to 65.

How long does a pension have to last?

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Living beyond 65

As well as the number of people living to pension age, the length of retirement has increased markedly too. The usual way of showing this is the number of years someone aged 65 can expect to live, on average. For today's fortysomethings this is around 20 years for a man and 23 years for a woman.

But the average does not show the likelihood of living even longer. It is expected that half of today's forty year old women, when they reach age 65, will live into their early nineties, and one quarter into their late nineties (Chart 2).

For the earlier generation, the same proportion lived only to their early or later eighties.

For men, a similar dramatic increase is seen although women live longer than men. State and private pensions have to fund much longer payment periods than ever envisaged.

Longer retirements have a cost for the individual too. Each year someone relies on pension income, he or she becomes poorer relative to the working population whose earned income tends to grow faster. Over a twenty or thirty year retirement the relative value of state and private pension income erodes significantly.

65%⁴. This data suggests it is over 85%. Perhaps we expect to have a similar lifespan to our parents and grandparents and have not yet appreciated the need to plan for longer lives.

It would be helpful to give people information on the number of years a pension is expected to last—perhaps on pension forecasts.

State pension as insurance

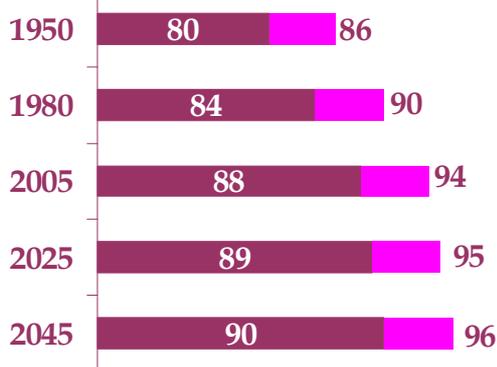
Chances are it will be longer than we think but none of us know exactly how long our retirement will be. Some people have a higher probability than others of living longer, depending on a complicated mix of genes, lifestyle and environmental factors.

But everyone has the potential for a very long life. The ninety year olds of today and tomorrow are from all occupations, income groups and health histories.

That is why the state pension system has to provide good basic insurance against the risk of being poor because of living longer than expected. The argument still rages about how best to provide that basic scheme, although it is becoming clearer that starting it later would help it to last longer.

Chart 2: We are living longer after age 65

Age to which half and one-quarter of 65-year-old women are expected to live, for those reaching age 65 in year shown



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Under-providing pension income for later life is likely as people tend to think they will die earlier than these data suggest they will.

Women in their early sixties put their chances of reaching age 75 at

1 O'Connell (2002) *Raising State Pension Age: Are we ready?* and O'Connell (2003) *Raising State Pension Age: An update*, PPI

2 Government Actuary's Department historical data and 2002-based projections, cohort basis, used with thanks to Adrian Gallop

3 Oeppen J, Vaupel J. (2002) *Science* Volume 296 10 May 2002, p. 1029

4 Banks et al (2004) in *Seven Ages of Man and Woman*, ESRC