Reform, reform, reform

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Changing pension provision in the UK

• Reform is a constant in pension provision
  – Three big changes occurring now in the UK
• Pension ages increasing
  – Happening for women now
• Earnings related pensions being abolished
  – Ending a 30 year experiment that began to be undone the moment it was implemented
• Auto enrolment into employer sponsored schemes started last year
Pension age is increasing

- To 66 by 2020 and 67 in 2028
  - 68 in 2046 – though likely to be brought forward
- Actual retirement ages are rising now
Male employment rates (1968-2009)

Female employment rates (1968-2009)

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• Actual retirement ages are rising now
• Government is committing to regular reviews aimed at keeping proportion of life spent in retirement broadly constant across cohorts
• Female state pension age is currently rising gradually
  – From 60 in 2010 towards 66 by 2020
  – Experience so far is encouraging
Female employment prior to SPA increase

Source: Figure 2.1. of Cribb, Emmerson and Tetlow (2013)

Notes: Pooled averages over the period 2003 Q1 to 2010 Q1. Based on 404,428 observations.
Employment of 60 year old women has risen
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• Government is committing to regular reviews aimed at keeping proportion of life spent in retirement broadly constant across cohorts
• Female state pension age is currently rising gradually
  – From 60 in 2010 towards 66 by 2020
  – Experience so far is encouraging
• Saving £2 billion annually for one year’s increase
  – We estimate employment increase among women of 27,000 as a result of increasing pension age from 60 to 61
  – And 8,000 additional men in work
The end of earnings related pensions

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  - Costs 1% of GDP (a quarter of spend on basic pension)
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• Focus of reform since 1978 has been its gradual destruction
• Moving now to a fully flat rate benefit from 2016
  – About one third average earnings
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• Overall effect to cut entitlements after about 2030
• By 2060 will limit rise in spending on pensioner benefits
  – to 8.1% of GDP (rather than 8.5%) from 6.9%
Eligibility rules becoming much looser

• Original design of state pensions related eligibility to years of contributions
• Any link finally laid to rest in most recent bill
• Retrospective crediting in to single tier of self employed, low earners and women with broken careers
  – More generous pensions from 2016 for these groups
• Single tier pension effectively a “citizen’s pension” in all but name
  – Though fiction of contributory system remains
Auto enrolment

• Employer sponsored pension coverage declining
  – Almost complete demise of DB schemes in private sector
• About 10 million employees without private coverage
  – Especially the low paid and those working for smaller employers
  – 70% earning less than £25k
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  - 70% earning less than £25k
- Auto-enrolment began in Autumn 2012 for large employers
  - extending to all by 2017
- All employers have to offer an approved scheme
  - Significant new responsibility, especially for smallest
- All employees automatically enrolled
  - Those who opt out are auto enrolled again every 3 years
Key parameters

• Everyone aged 22 to SPA
• Earning above tax free allowance (about £10,000)
• Employees contribute 4% of “band earnings”, employers 3%
  – That is between £5,668 and £41,450
    • NI LEL and UEL
• Tax relief on contributions
National Employment Savings Trust (NEST)

- Employers free to choose their own scheme
  - Private sector competing for the market
- NEST set up, with government subsidy, to ensure a good value scheme available to all
  - Hard for private sector to provide for small employers and low earners
- Charges 1.8% on contributions plus AMC of 0.3%
  - Up front contributions to be phased out over time
- Restrictions on operation of NEST
  - No transfers in
  - Maximum contribution of £4,400 a year
Challenges

• Managing risk - default investment strategies
  – For NEST start people in very safe assets to “get them in the saving habit”, move into riskier then safe again close to pension age
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• Population very mobile between jobs
  – Small pots and lack of transferability
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• Decumulation and over optimism
  – Lack of understanding of what is needed to buy a pension
  – A quarter of recent retirees with a DC pension got a pension less than half what they’d expected immediately before retirement
Conclusions

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• Increasing pension age looking effective
  – But change is slow
• We wait to see the effects of the great auto-enrolment experiment
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• UK a quarter of a century behind Australia?