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How important is Defined Contribution pension wealth for people approaching retirement?

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@TheIFS



Economic
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Background



- Decline in traditional Defined Benefit (DB) pensions and growth – particularly since automatic enrolment – of Defined Contribution (DC) pension arrangements
- Prior to 2015, buying an annuity (income for life) was near-compulsory for those with DC pensions
- “Pension Freedoms” in 2015 ended that obligation – free to choose how to draw on DC pension wealth in retirement
 - Annuity purchases subsequently collapsed
- Concerns about the complexity of this decision and whether people are making appropriate choices

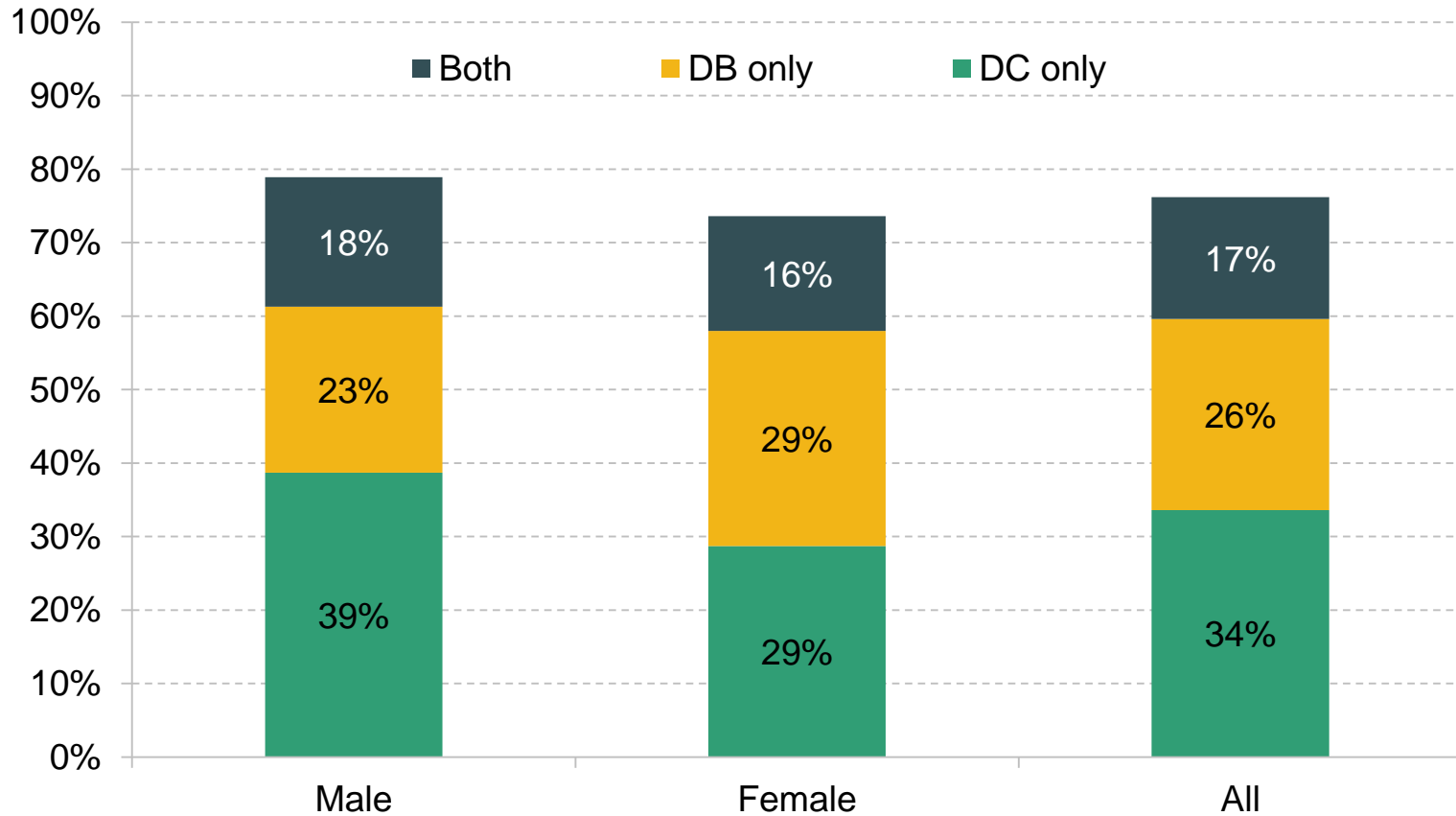
Some key questions

- **How important are the choices presented by pension freedoms?**
 - How prevalent are Defined Contribution pension pots?
 - How much other wealth do people approaching retirement have, in pensions or other assets?
 - How “annuitised” is that other wealth?

- **We mainly use data from the UK's Wealth and Assets Survey**
 - Longitudinal study of people from 2006-08 to 2018-20
 - Substantial sample (e.g. ~8,700 individuals aged 50-64 in 18/20)
 - Detailed data on all **wealth holdings** (individual and all members of the household)
 - **Private pensions** (defined benefit and defined contribution)
 - **Savings** in current accounts/ savings accounts/ ISAs
 - **Housing wealth** in own home (+ additional homes) net of mortgage
 - **Broader data** on individuals' background, economic circumstances, and expectations

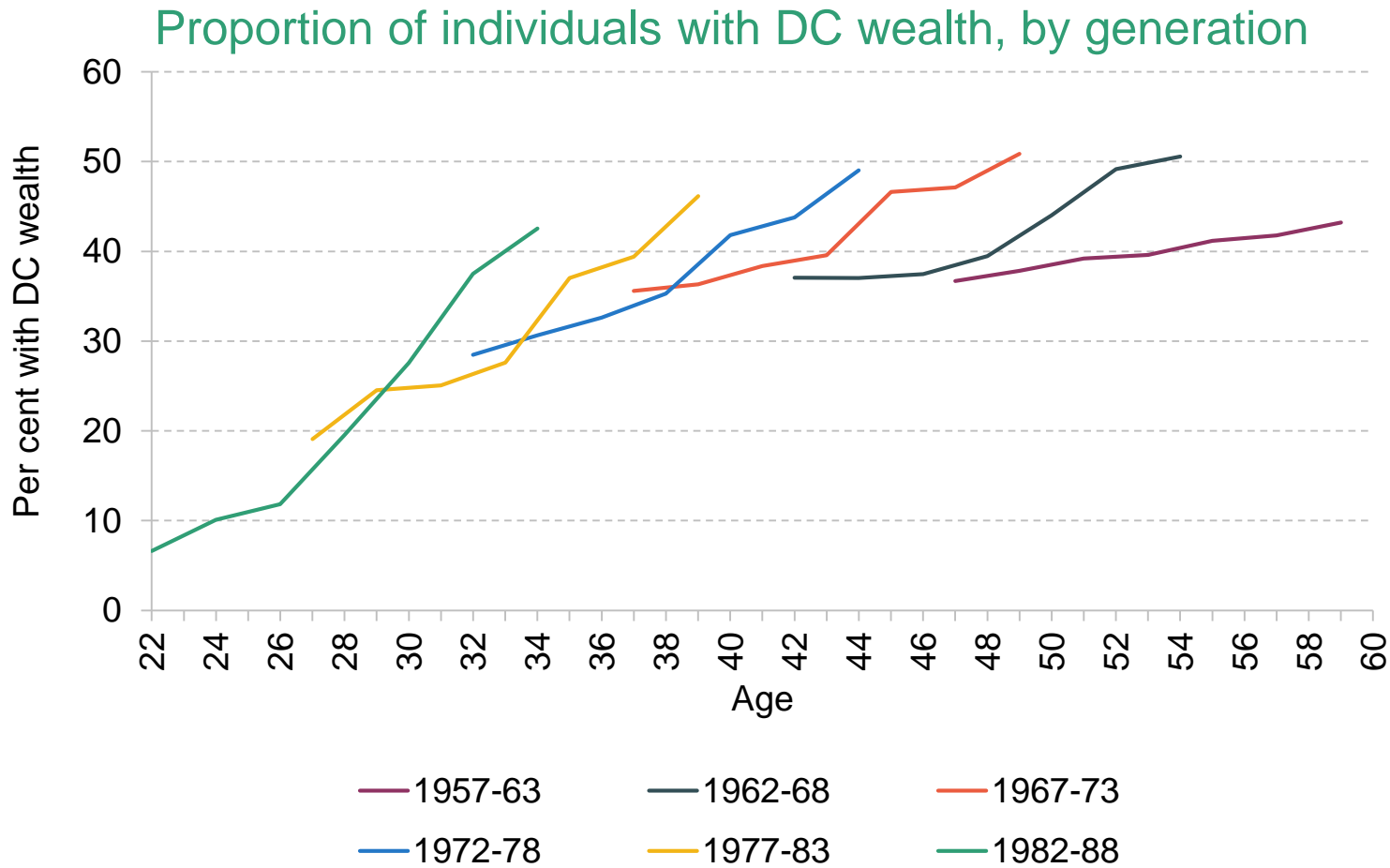
How common are private pensions for people in their 50s?

Proportion of individuals aged 50 to 59 with DC and DB wealth not yet in payment



Source: IFS calculations using the Wealth and Assets Survey.

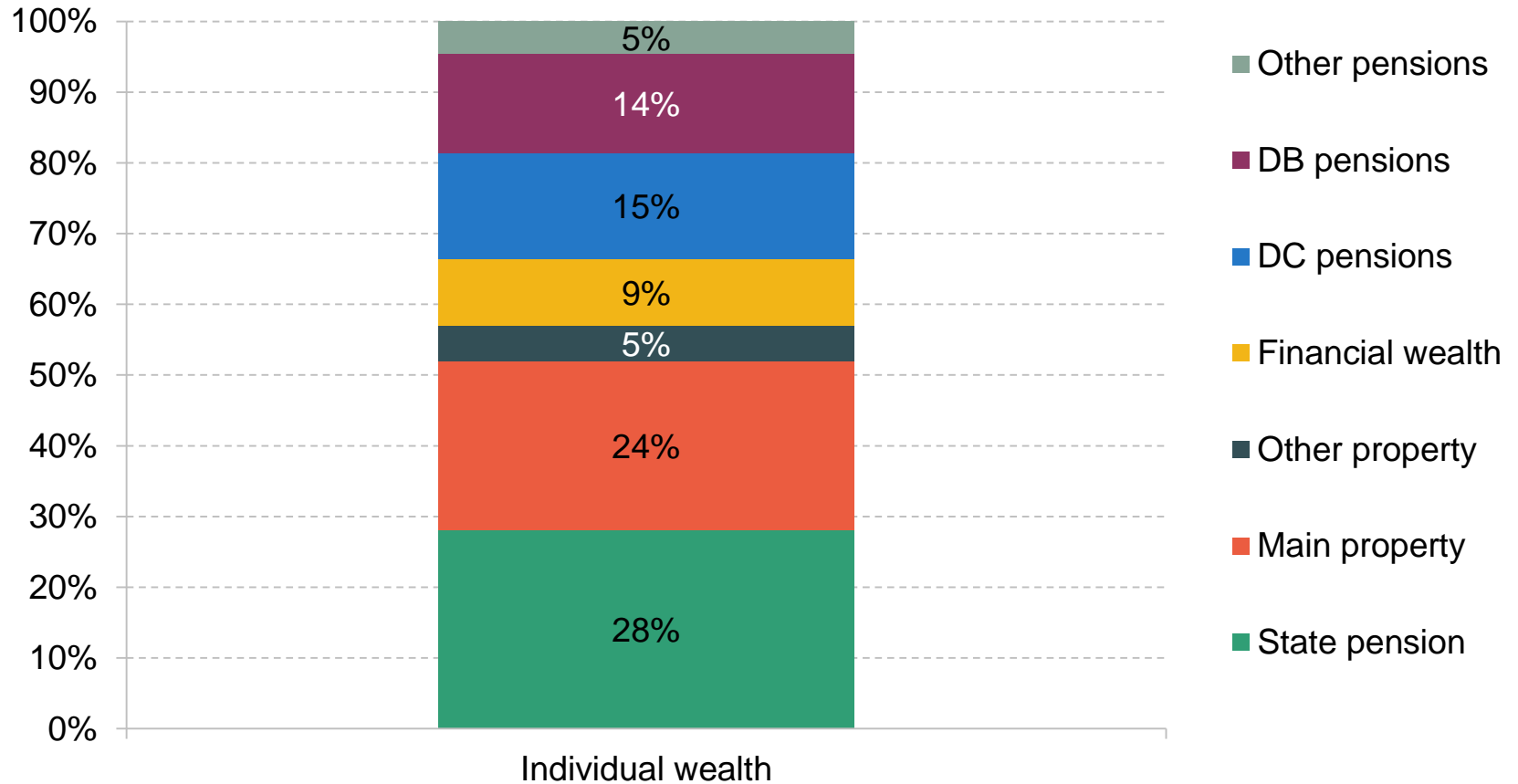
How common will DC pensions be for future generations of pensioners?



Source: IFS calculations using the Wealth and Assets Survey.

How important are DC pensions?

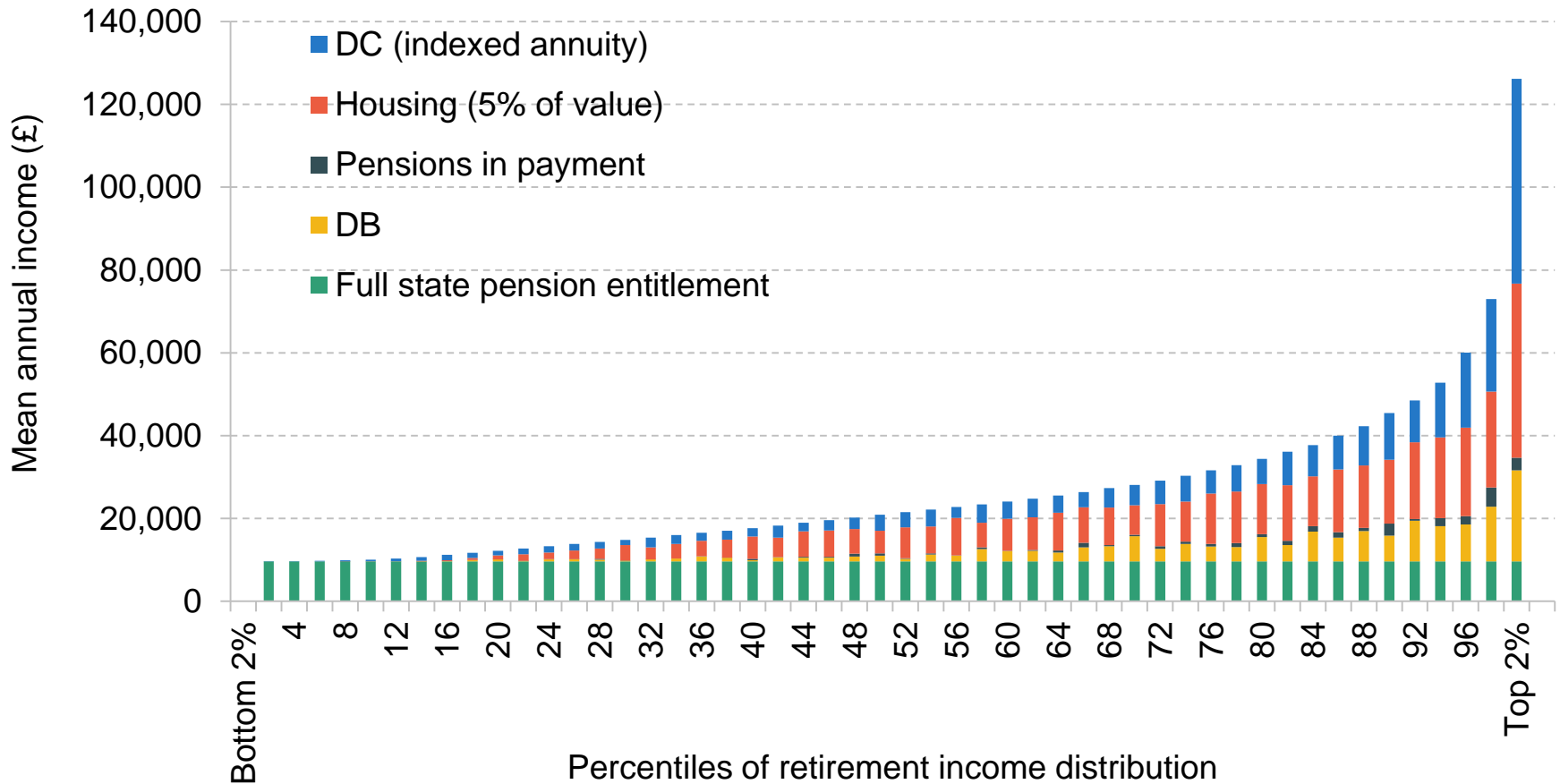
Components of wealth including state pension among individuals aged 50-59 with DC pots



Source: Authors' calculations using the Wealth and Assets Survey. Note: Other pensions refer to pensions in payment and pension from a former spouse of partner.

How important is DC in retirement incomes?

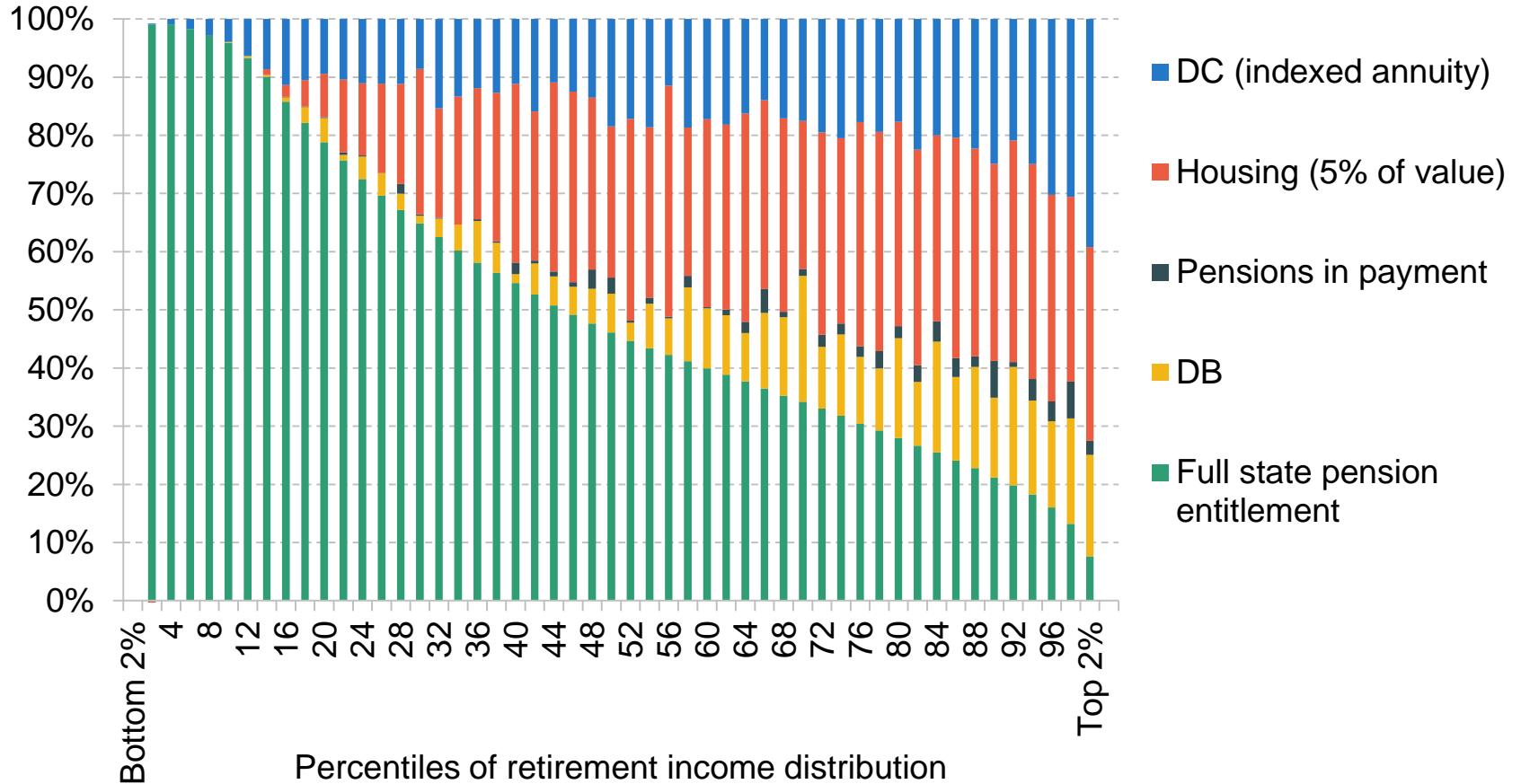
Composition of retirement income at 66 for people with DC wealth



Source: See Figure X of Cribb and Karjalainen (2023) for further details.

How important is DC in retirement incomes?

Composition of retirement income at 66 for people with DC wealth



Source: See Figure X of Cribb and Karjalainen (2023) for further details.

Summary



- **DC pension pots are increasingly prevalent among workers, in large part due to automatic enrolment**
- **But for the majority of people currently in their 50s and 60s, DC pots represent a small portion (12%) of overall family wealth**
 - Larger fractions in (annuitized) state pension, housing, DB pensions
 - Many therefore have significant “insurance” against longevity risk (living too long and running out of money)
- **Group of concern most likely to people in the middle to upper-middle of the income distribution**
 - Income from DC 20%+ of retirement resources; £000s per year; not extremely wealthy like top few %