



PRESS RELEASE

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Are retirement resources adequate?

The vast majority of the next generation of pensioners will have resources in excess of the adequacy benchmarks typically used in the policy debate but many may not get as much private pension income as they expect.

These conclusions emerge from an analysis by researchers at the Institute for Fiscal Studies of new data on thousands of individuals in England aged between 50 and the State Pension Age (SPA) in 2002. The dataset includes detailed information about the value of their pensions (state and private), housing and other wealth, as well as expectations of inheritance and the length of their working lives. The report provides the most detailed picture yet of the provision that those soon to be pensioners in England have made for their retirement and their expectations of the future. It is particularly timely given the imminent release of the second report of the Pensions Commission on 30 November 2005.

The vast majority of individuals are likely to have sufficient resources to provide them with an income in retirement above the adequacy thresholds used most frequently in the policy debate. Depending on the particular benchmark used, we predict that only about 8% to 23% will have an inadequate income when they reach the SPA. The findings include:

- Taking into account individuals' own expectations of the timing of their retirement and their receipt of inheritances in the future, we estimate that 7.7% of those aged between 50 and the SPA will not have enough resources to lift them above the income floor provided by the Pension Credit Guarantee.¹
- Judging the adequacy of likely retirement income relative to individuals' current income, we estimate that 11.3% of individuals aged between 50 and the SPA will have net retirement income equal to less than 67% of their current net income when they reach the SPA. A further 11.8% are predicted to have net retirement income between 67% and 80% of their current net income.
- Using the adequacy benchmark favoured by the Pensions Commission (which requires that low income individuals achieve a higher income replacement rate than high income individuals), we find that 9.8% of individuals aged between 50 and the SPA are at risk of having inadequate incomes. This is much lower than the proportion implied by the Pension Commission's own analysis of between 38% and 43% (for individuals aged between 46 and the SPA). Our figure is lower partly because we look at the income that could be generated by all forms of wealth (including housing) rather than pensions alone, and because we judge adequacy at the level of the family unit rather than the individual.

Although our calculations suggest that fewer individuals face inadequate incomes in retirement than the Pensions Commission's analysis suggests, many individuals may still be disappointed when they reach the SPA:

- On average, individuals aged between 50 and the SPA, who have a private pension from which they are not yet receiving income (some 59% of all individuals aged between 50 and the SPA in England), overestimate by 20% the income that they will receive from these pensions compared to our predictions.

- About a quarter of these individuals overestimate the income they will receive by at least 30% compared to our predictions.
- These discrepancies could either be because individuals intend to increase significantly their private pension contributions between now and retirement (which is plausible, particularly for younger individuals) or because they are quite optimistic about future investment returns and annuity prices.

Gemma Tetlow, one of the authors of the report, said “Our analysis shows that amongst older workers, at least, the fraction retiring with inadequate resources may not be as high as the first (interim) report of the Pensions Commission estimated. Within the group currently aged between 50 and the State Pension Age, we predict that around 730,000 individuals in England will have retirement income that is lower than the benchmark used by the Pensions Commission. However, despite this we find that many individuals may not receive as much income from private pensions as they expect, unless they plan to change significantly their behaviour over the next few years.”

Other findings include:

- There is substantial inequality in pension wealth: the 10% of individuals in families with the most family pension wealth (state and private) have, on average, £874,000, whereas the 10% of individuals in families with the least family pension wealth have just £50,000. Private pension wealth is much more unevenly distributed than state pension wealth.
- Holdings of different assets do not offset each other. People with low pension wealth tend not to have high levels of housing or other wealth to compensate; they tend to have lower levels of other assets as well.
- As a result, total wealth is very unequally distributed. The 10% of individuals in the wealthiest families have at least £1,000,000 of family wealth, whereas the poorest 10% have less than £110,000.
- Differences in expectations of future work, inheritances and chances of living to older ages between the wealthy and the less wealthy are not sufficient to assuage concern that the least wealthy may face problems of inadequate resources in retirement. In fact, the least wealthy have lower expectations of remaining in employment and lower expectations of receiving an inheritance than their wealthier counterparts. Even though the poorest say they have lower life expectancy than wealthier individuals on average, this can only relieve their retirement resource insufficiency to a limited extent because most of their wealth is annuitised.

ENDS

Notes to editors:

1. Many more individuals will qualify for the Pension Credit. This is for two reasons. First, some individuals who are not eligible for the Pension Credit Guarantee will be eligible for the Pension Credit Savings Credit. Second, individuals might choose to hold their assets in forms that are not subject to the means-test for example owner-occupied housing.
2. ‘Preparing for retirement? The adequacy and distribution of retirement resources in England’ by James Banks, Carl Emmerson, Zoë Oldfield and Gemma Tetlow is published on 11th October 2005. The report will be launched at IFS on the morning of Tuesday 11th October. Please contact the IFS press office on 020 7291 4800 if you would like to attend.
3. The research for this report was produced under the auspices of the IFS pensions and retirement saving consortium, to whom the authors are grateful for both financial assistance and useful comments. The members of the IFS pensions and retirement saving consortium are: The Actuarial Profession, The Association of British Insurers, The Bank of England, The Department for Work and Pensions, HM Revenue and Customs, HM Treasury and The Investment Management Association. We also thank the Economic and Social Research Council for co-funding through the research grant ‘Late life work and retirement’ (RES-000-23-0588) and Robert Chote, Richard Disney and Matthew Wakefield for useful comments. Data from the English Longitudinal Study of Ageing and the Labour Force Survey were supplied by the ESRC Data Archive. Responsibility for interpretation of the data, as well as for any errors, is the authors’ alone.