

## Institute for Fiscal Studies



The evolution of pension wealth and  
contribution dynamics

Rowena Crawford and Gemma Tetlow

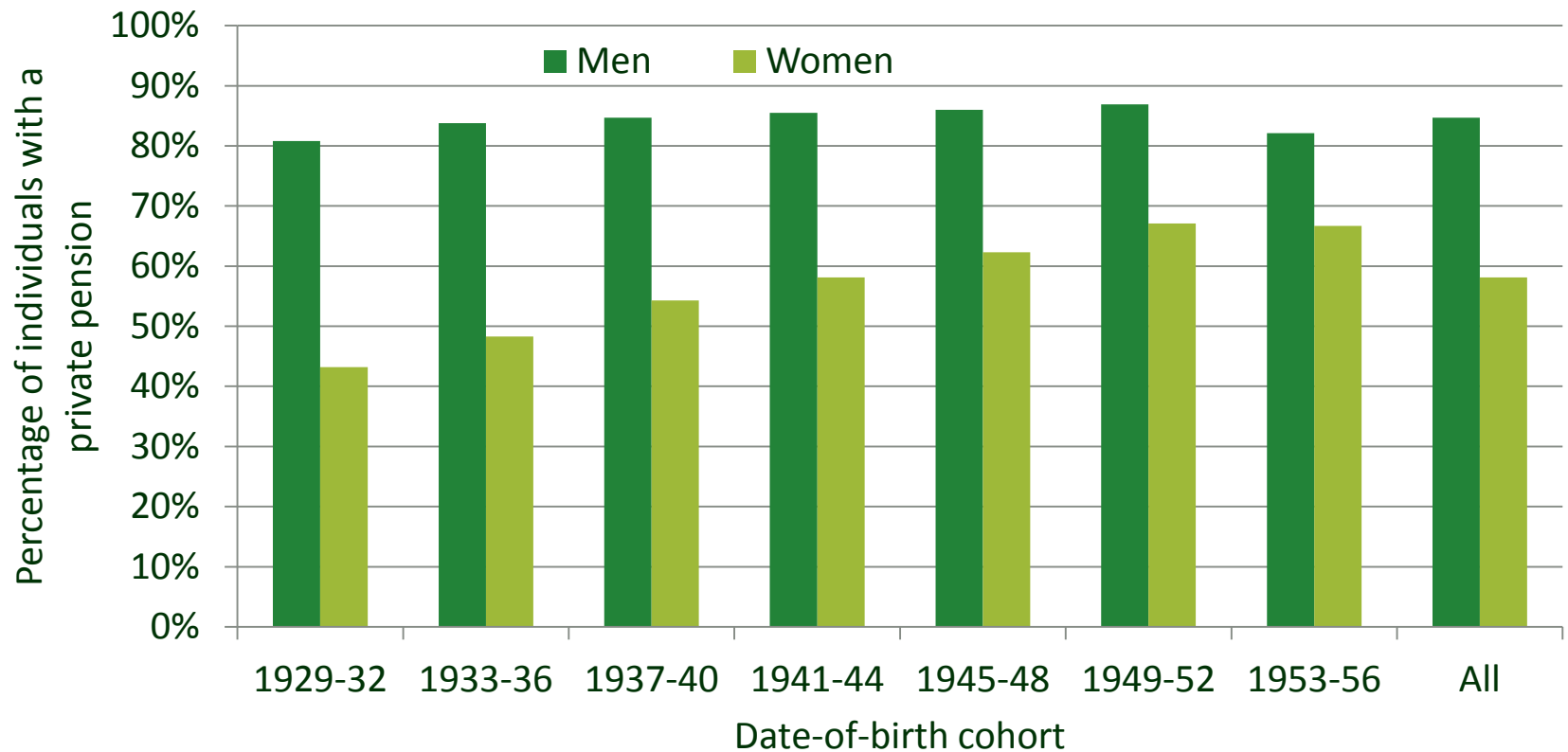
# Context

- Private pension saving has always played, and continues to play, an important role providing income to older people in retirement
- Private pension environment has evolved in recent decades
  - Introduction of personal pensions in late 1980s
  - Declining prevalence of employer provided DB schemes
  - Increased labour force participation of women
  - ⇒ Interesting to examine differences in pension coverage and wealth between cohorts and over time
- Important to understand interactions between private pensions, labour market activity and income levels
  - Particularly given policy ambitions to increase pension coverage, work at older ages and the adequacy of incomes in retirement
  - ⇒ Examine contribution, income and employment dynamics around 'retirement'

# Private pension “lifetime” coverage

# Private pension “lifetime coverage”, by sex

- Increased among later cohorts of women but not men

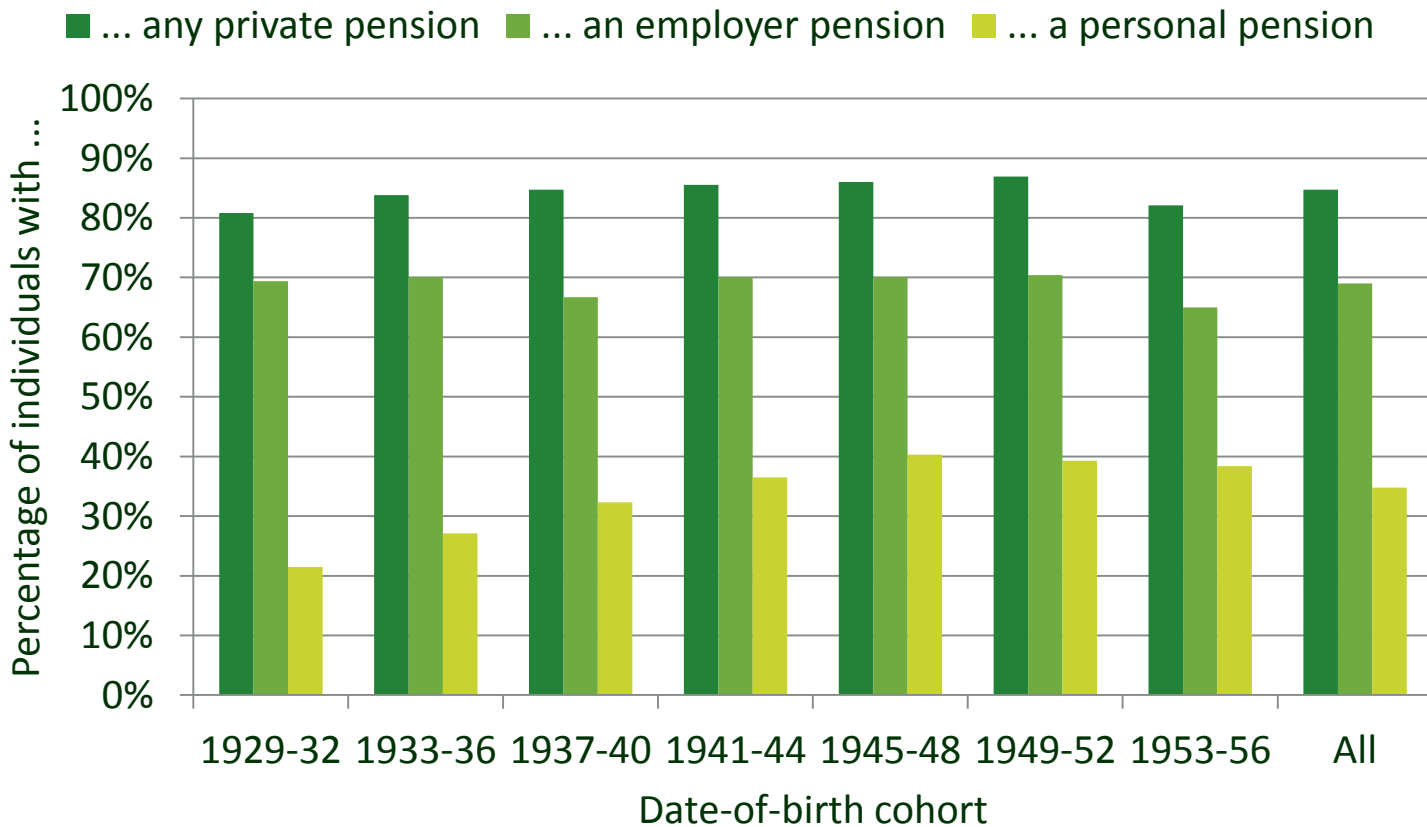


Notes: Figure 2.1.  
Pooled ELSA 2002–03 to 2010–11. N =18,164

# Private pension “lifetime coverage”, by type

Among men

- Increase in personal pension coverage among men who have been covered by an employer pension (at some point)

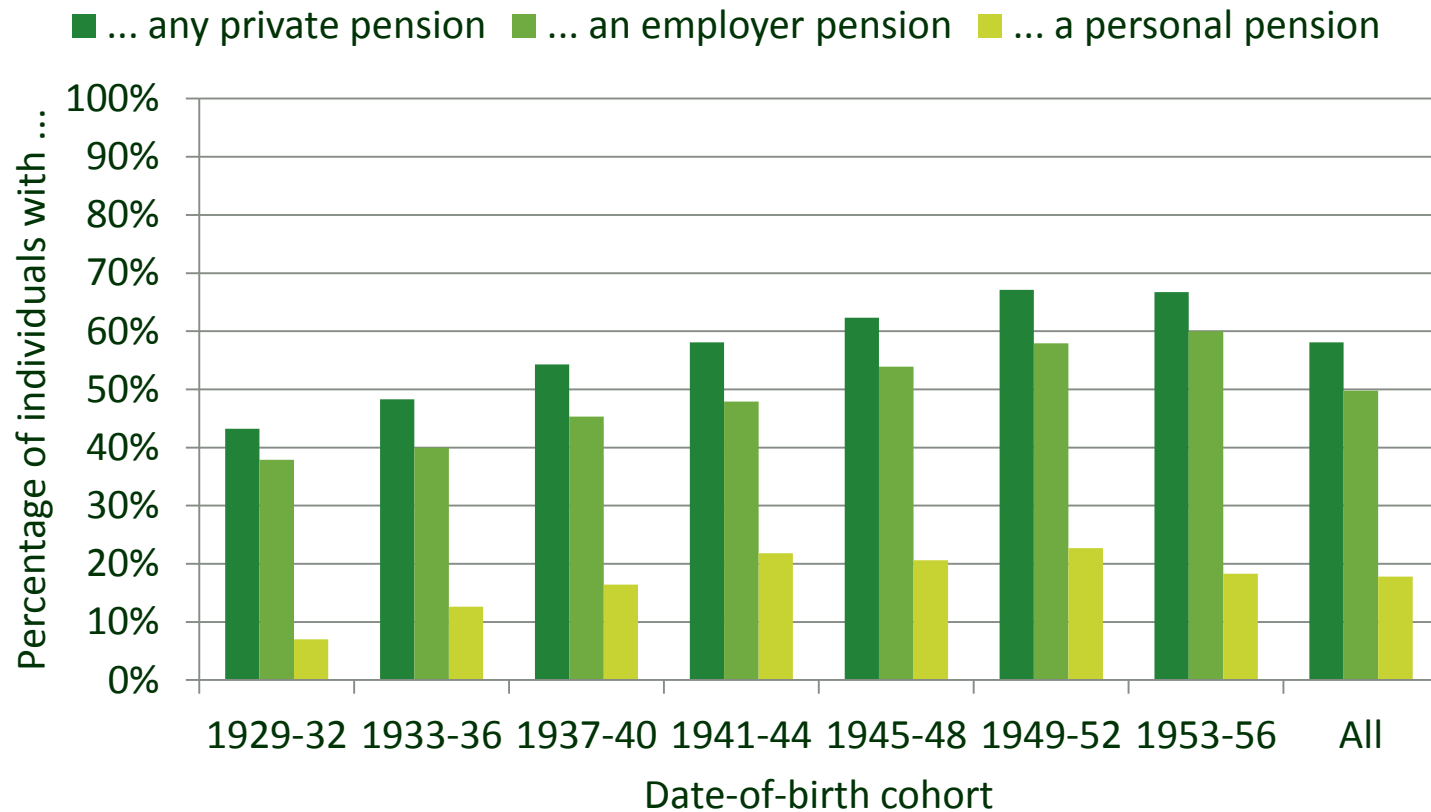


Notes: Figure 2.2 panel A.  
Pooled ELSA 2002–03 to 2010–11. N = repeat observations of 5,649 men

# Private pension “lifetime coverage”, by type

Among women

- Increases in employer and personal pension coverage



Notes: Figure 2.2 panel B.  
Pooled ELSA 2002–03 to 2010–11. N = repeat observations of 6,492 women

# Private pension wealth

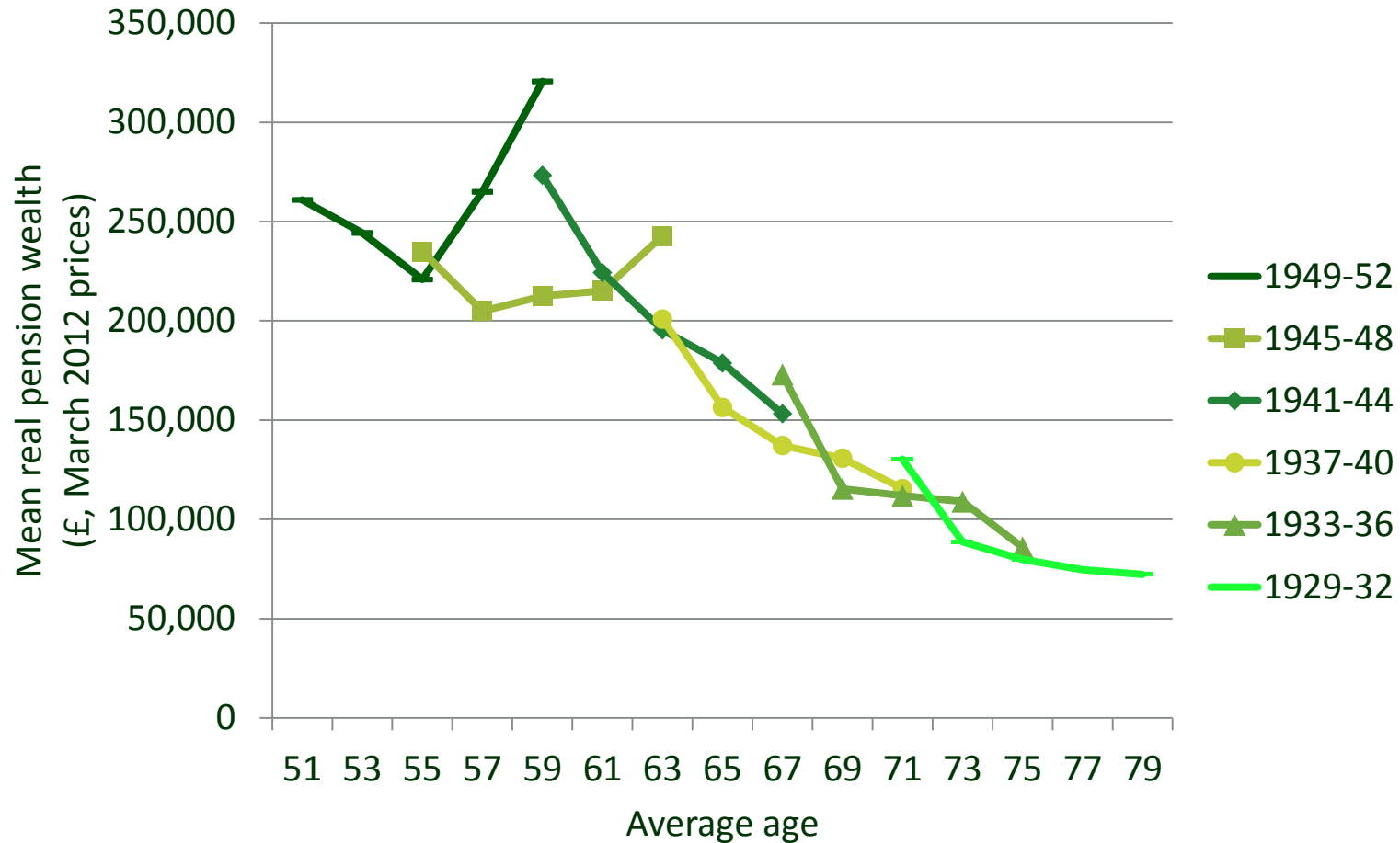
# Private pension wealth

- Looking only at pension coverage can be misleading as it could disguise significant differences in the *amount* of pension saving
- Investigate private pension wealth holdings:
  - How these have changed between cohorts
  - How these have changed as people have aged
- Focus on the subsample of ELSA who were:
  - Observed in all 5 waves: minimise the effects of differential mortality
  - Covered by a pension in wave 1: no compositional effects from people who *become* covered at older ages



# Private pension wealth, by cohort

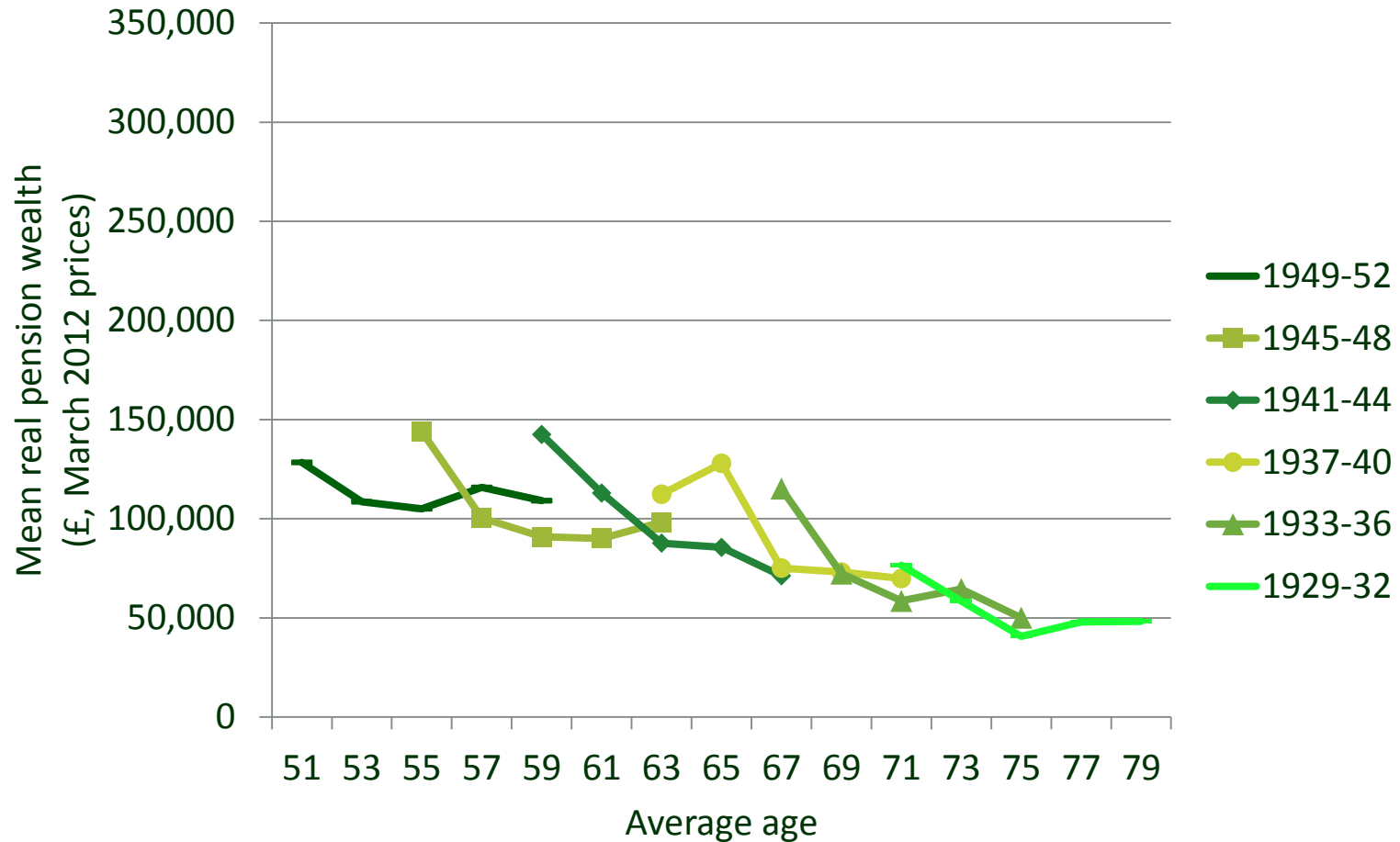
Among men



Notes: Figure 2.3 panel A.

# Private pension wealth, by cohort

Among women



Notes: Figure 2.3 panel B.

# Dynamics around “retirement”

# Dynamics around retirement

- When is “retirement”?
  - When individuals start to draw their private pension income?
  - When individuals leave work?
  - When individuals start to self-report themselves as “retired”?

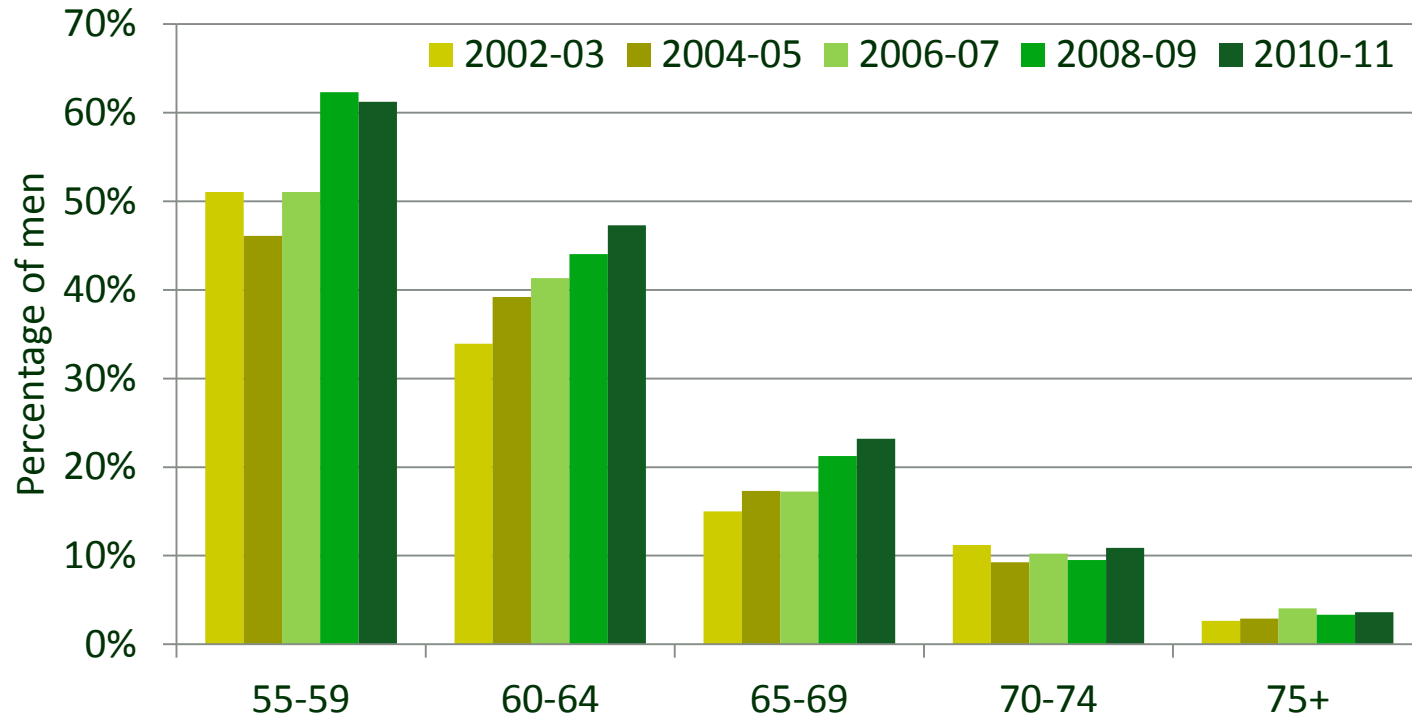
# Starting to draw a private pension income

- Starting to draw a private pension income is not synonymous with leaving the labour market
  - 69% of individuals in work prior to first starting to draw a private pension
  - 55% of these individuals remained in work after starting to draw
- Women are more likely than men to leave work at the point that they first start drawing income from a private pension, as are older individuals, those who report having a work-limiting disability and those who are drawing income from an employer pension

Notes: Table 2.1.

# Starting to draw pension ≠ leaving labour market

Percentage of private pension income recipients working - men



- Increase in proportion working while receiving a private pension income is greater than general increase in proportion of individuals at these ages in work

Notes: Figure 2.8 panel A.

# Dynamics around retirement

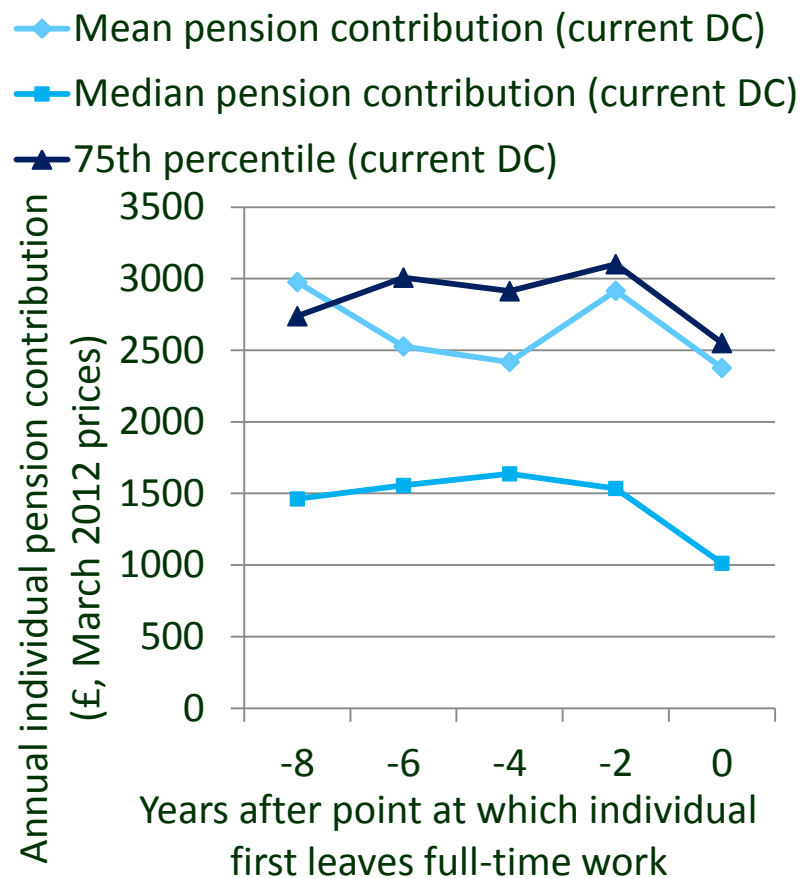
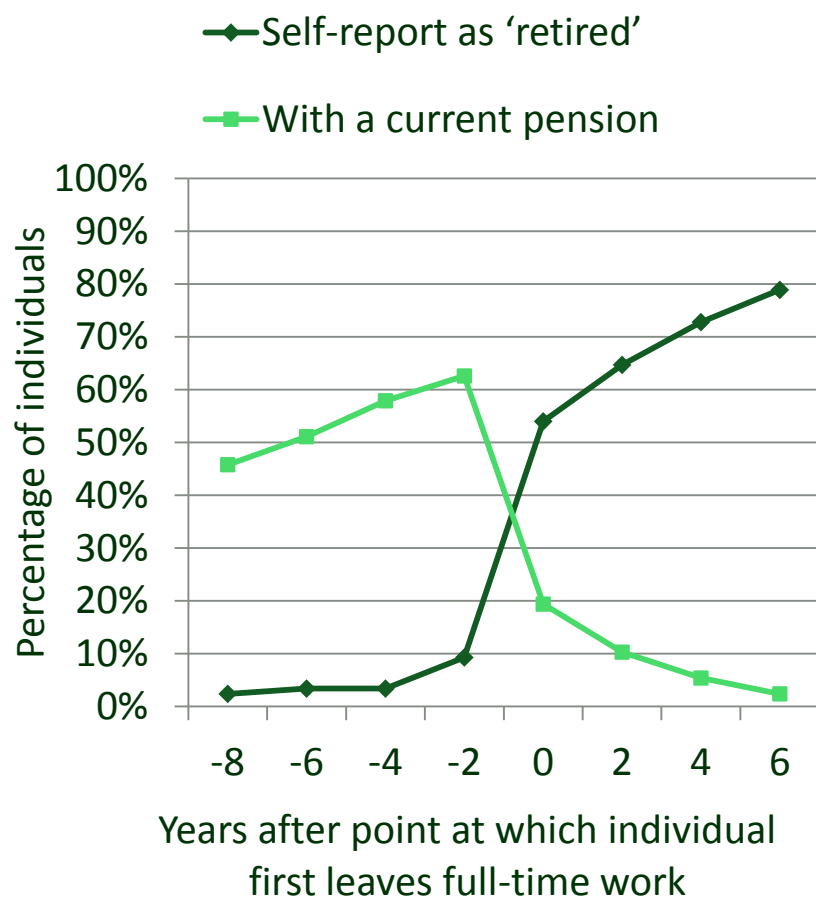
- When is “retirement”?
  - When individuals start to draw their private pension income?
  - When individuals leave work?
  - When individuals start to self-report themselves as “retired”?
- In the following take retirement to be when an individual leaves full-time work
  - Focus on the subsample of ELSA individuals observed making a consistent transition from full-time work to retirement
- Investigate some dynamics around the point of retirement
  - Pension contribution behaviour
  - Changes in total family net income

# Pension contributions dynamics

- Pension contributions might be expected to increase in the years leading up to retirement
  - Individuals become better informed about their accumulated pension wealth and their likely pension income needs
  - Other expenditure needs might decline (children leave home, mortgage paid off etc.)
- Pensions are relatively tax advantaged
  - Contributions exempt from income tax and  $\frac{1}{4}$  fund can be taken as tax-free lump sum
  - Particularly pertinent for those close to retirement



# Pension contributions dynamics



Notes: Figure 2.10.

N = max: 1,1451 individuals (Y=-2, Y=0) , min: 442 individuals (Y=-8)

# Income dynamics

- ‘Adequacy’ of individuals’ retirement resources is often a direct object of policy concern
- ‘Adequacy’ can be taken to mean different things
  - Sufficient to avoid poverty?
  - Sufficient to provide a similar standard of living to working life?
- Lifecycle models suggest individuals want to smooth consumption between working life and retirement
  - Does not necessarily have to be 100%
    - Work related consumption may not need to be maintained
  - Does not necessarily require smoothed *expenditure*
    - Cheaper but more time intensive methods of consumption may be utilised
  - Does not necessarily require smoothed *income*
    - Retired individuals pay lower taxes (broadly speaking)
    - Less need for saving

# Replacement of income in retirement

Mean total net family income in each year, as a proportion of pre-retirement income:



Notes: Figure 2.11 panel B.

N = max: 1,1451 individuals (Y=-2, Y=0) , min: 442 individuals (Y=-8)

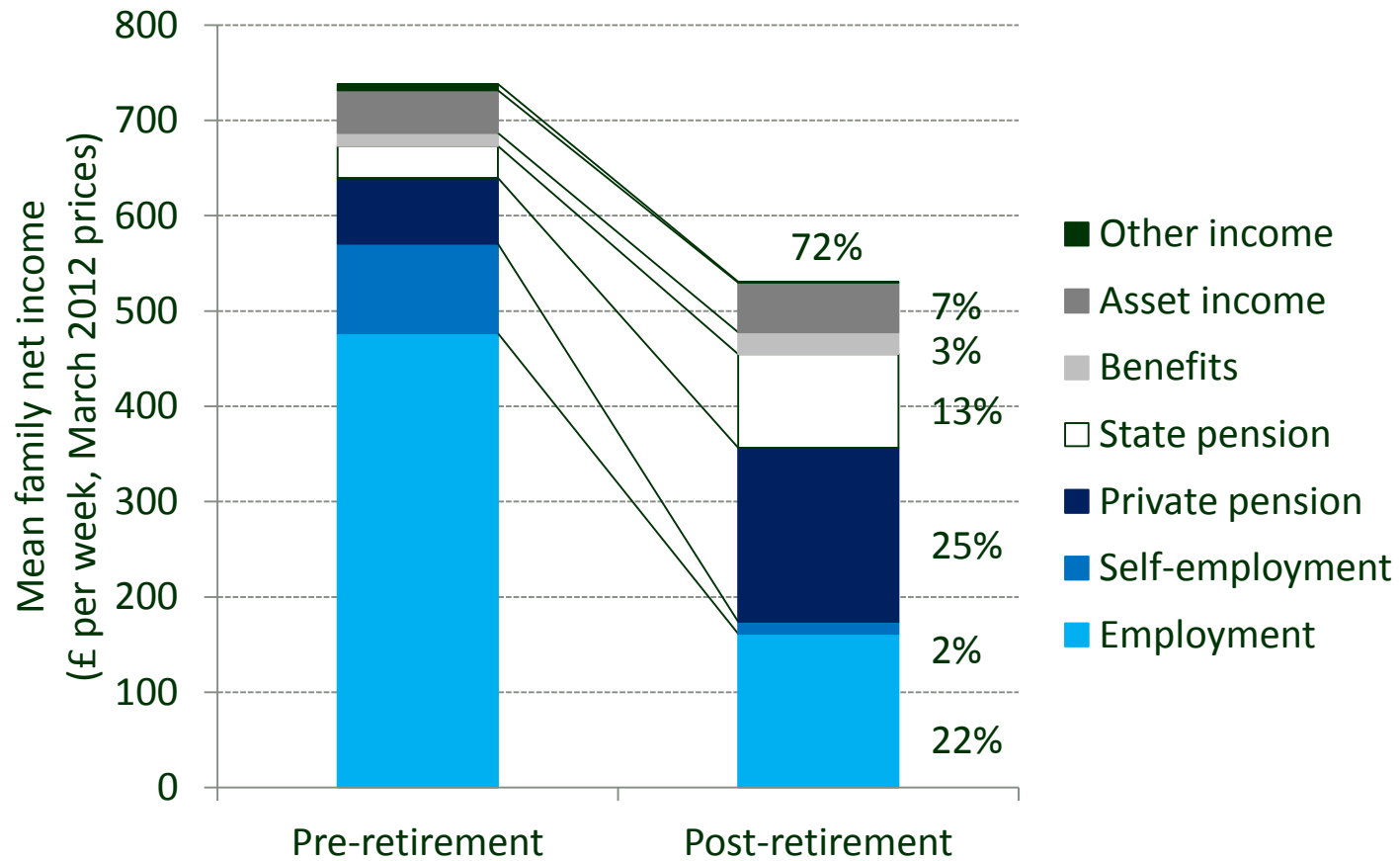
# Replacement of income in retirement

- Calculate average family income across years observed before leaving FT work, and years observed after leaving full time work
- On average replacement rate after leaving full-time work is 72%
- Little difference by sex, education, non-pension wealth quintile
- Replacement rate is decreasing in pre-retirement income

	Mean family net income		Replacement rate	Sample size
	Average pre-ret	Average post-ret		
All	738	531	71.9%	1,408
<i>Income quartile (pre retirement)</i>				
Lowest	303	319	105.1%	354
2	532	417	78.4%	351
3	739	552	74.8%	351
Highest	1,381	837	60.6%	352

Notes: Income figures shown as £ per week. Other notes see Table 2.5.

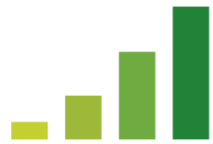
# Sources of income in retirement



Notes: Figure 2.12.  
N = 1,408 individuals

# Summary

- Private pension coverage in England is high and has increased across successive generations of women
- Among those with pensions there is no evidence of increases or decreases in the amounts held by successive cohorts of men or women
- Starting to draw a private pension is not synonymous with leaving the labour market
  - Working while receiving private pension income has become more prevalent over time
- Behaviour and income around the point of leaving full-time work:
  - Proportion of individuals contributing to a pension increases in the years leading up to leaving FT work but little evidence of increased contributions
  - On average family net income falls by 28% when individual leaves FT work



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