



Institute for  
Fiscal Studies



## Public sector pensions and pay

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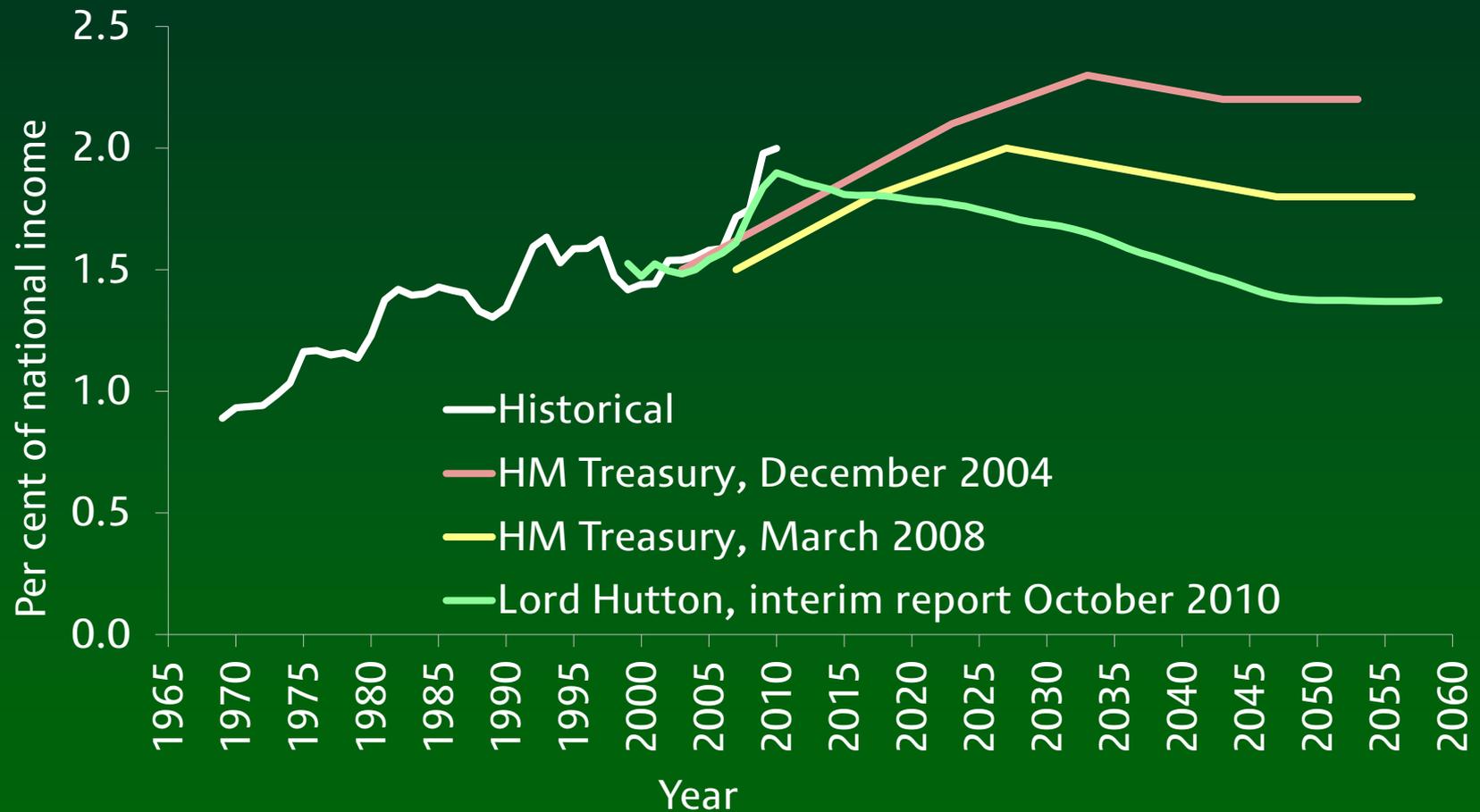
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# Public service pensions

- Spending on public service pensions forecast to fall as a share of national income
- Due to significant cuts already announced
  - last Government's increase in the Normal Pension Age for most new entrants
  - current Government's change in indexation from RPI to CPI
- Employee contributions also increased
- More recent reforms do much to improve structure of pensions
  - but for some schemes changes do little to reduce the average generosity in the long-run
  - losses for high flyers but gains, on average, for those with lower earnings growth
- Public service pensions remain much more generous than those provided in the private sector



# Spending on public service pensions forecast to fall as a share of national income



# Latest reforms do much to improve structure of pensions

- Defined benefit schemes retained
  - state particularly well placed to offer these schemes
- Career average rather than a final salary basis
  - more logical measure of earnings to use
- Normal Pension Age aligned with State Pension Age (except for uniformed services)
  - a coherent response to rising longevity at older ages
- Changes apply to future accrual (apart from those less than 10 years from current NPA)
  - reduces extent to which individuals doing the same job for the same pay accrue different pensions

# Valuing public-service pensions

- Difficult to do
  - doesn't just depend on scheme rules
  - also depends on longevity of individual and their partner, discount rate, earnings trajectories and pension tenure
- Clear that the latest reforms do reduce the generosity for some
  - those protected from Labour's reform could see their NPA increase from 60 to 68 for new accrual
  - civil service scheme made less generous
- But for others not clear there is an overall reduction in generosity
  - high flyers with long tenures did very well under final salary schemes and lose from the shift to career average
  - but those with lower earnings growth, on average, gain

# Public service pensions remain much more generous than those provided in the private sector

- Very large differences in membership of DB schemes
  - in 2010 in the public sector 79.0% of employees were a member of a DB scheme, compared to just 11.0% in the private sector
  - private sector figure down from 12.4% in 2009, 13.6% in 2008 and 33.9% in 1997
- Large differences in membership of any workplace scheme
  - 83.9% of public sector workers and 34.4% of private sector workers are in a workplace scheme
- Workplace DC schemes typically less generous than DB schemes
  - private sector employers moving from DB schemes to less generous DC schemes in order to reduce expected future costs

# Public sector pay

- Estimated public sector pay premium increased since financial crisis
  - Government's pay squeeze to return it to pre-crisis levels
- Distribution of public sector pay more compressed than that of private sector pay
- Estimated public sector pay premium varies considerably across the country
  - but tentative evidence suggests the premium across regions varies by occupation
  - regional variation in public sector pay awards would need to be carefully designed

# Estimated public sector pay premium

Estimated average public–private hourly wage differentials (2009Q2–2011Q1)

	Male	Female	All
Raw differential	+20.2	+27.5	+24.3



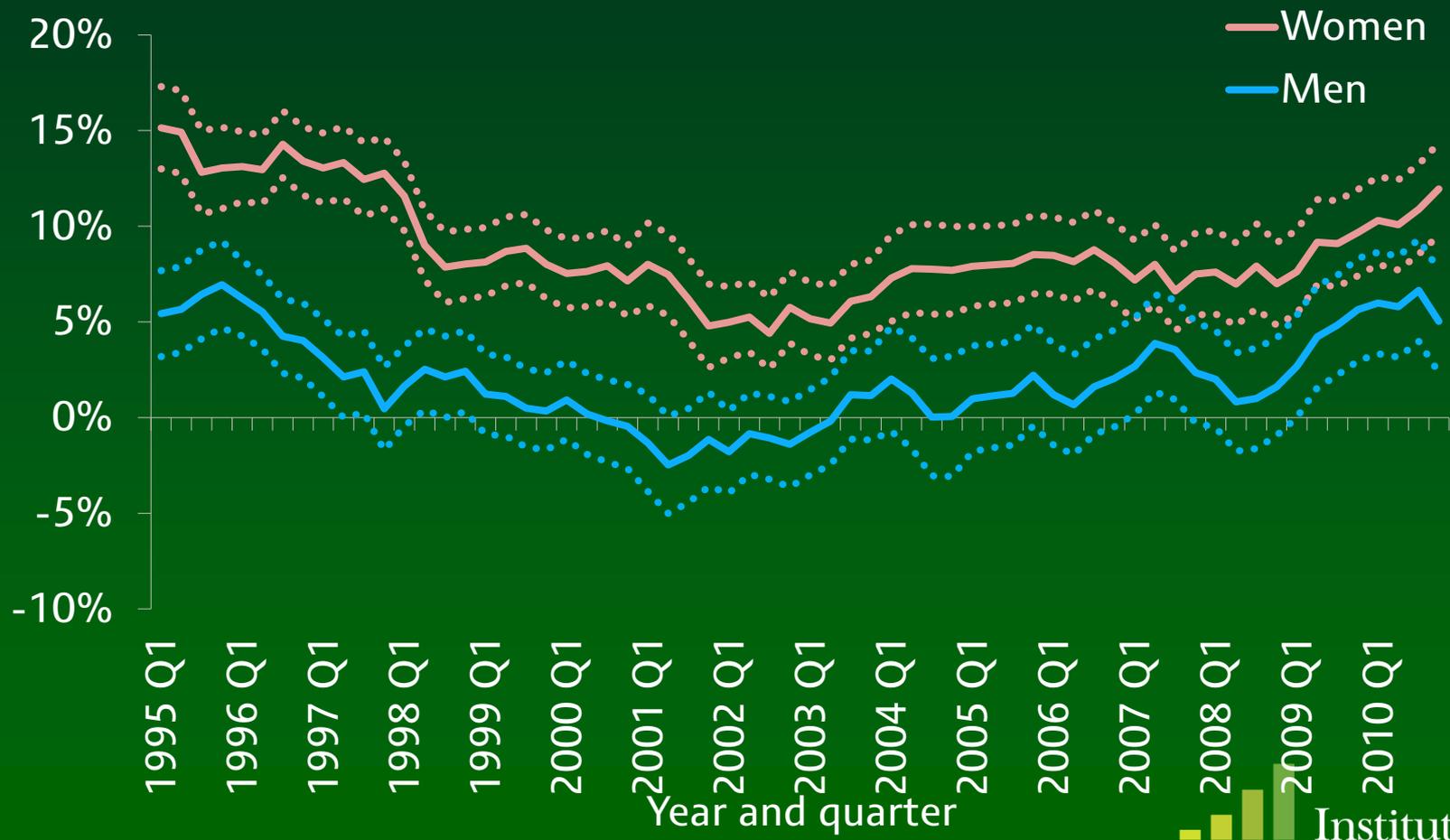
# Estimated public sector pay premium

Estimated average public–private hourly wage differentials (2009Q2–2011Q1)

	Male	Female	All
Raw differential	+20.2	+27.5	+24.3
Controlling for education, age and qualifications and region	+5.5	+11.3	+8.3

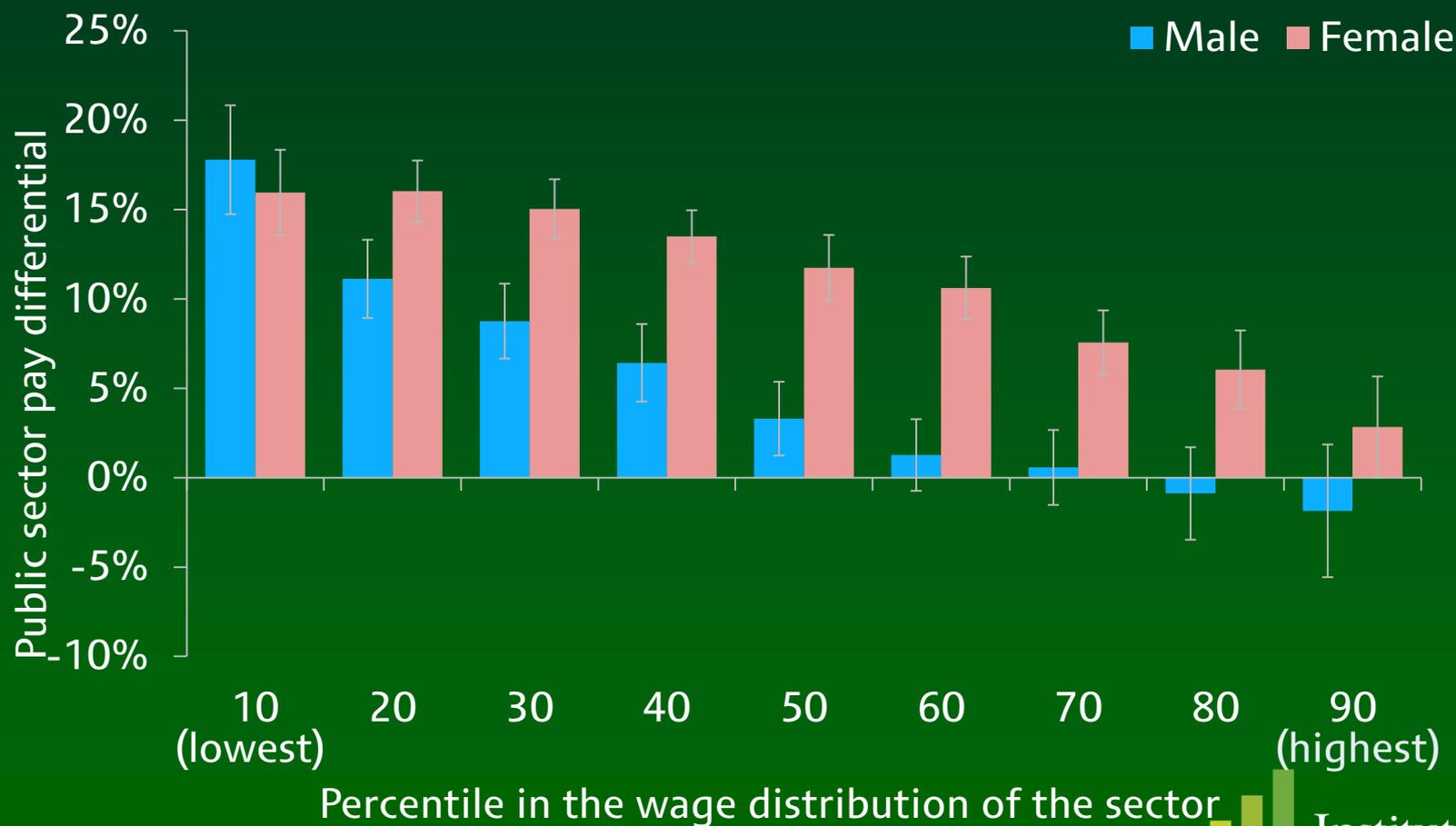
# Estimated public sector pay premium increased since financial crisis

Estimated average public–private hourly wage differentials, controlling for age and education, over time



# Distribution of public sector pay more compressed than that of private sector pay

Estimated average public–private hourly wage differentials, controlling for age and education, by percentile

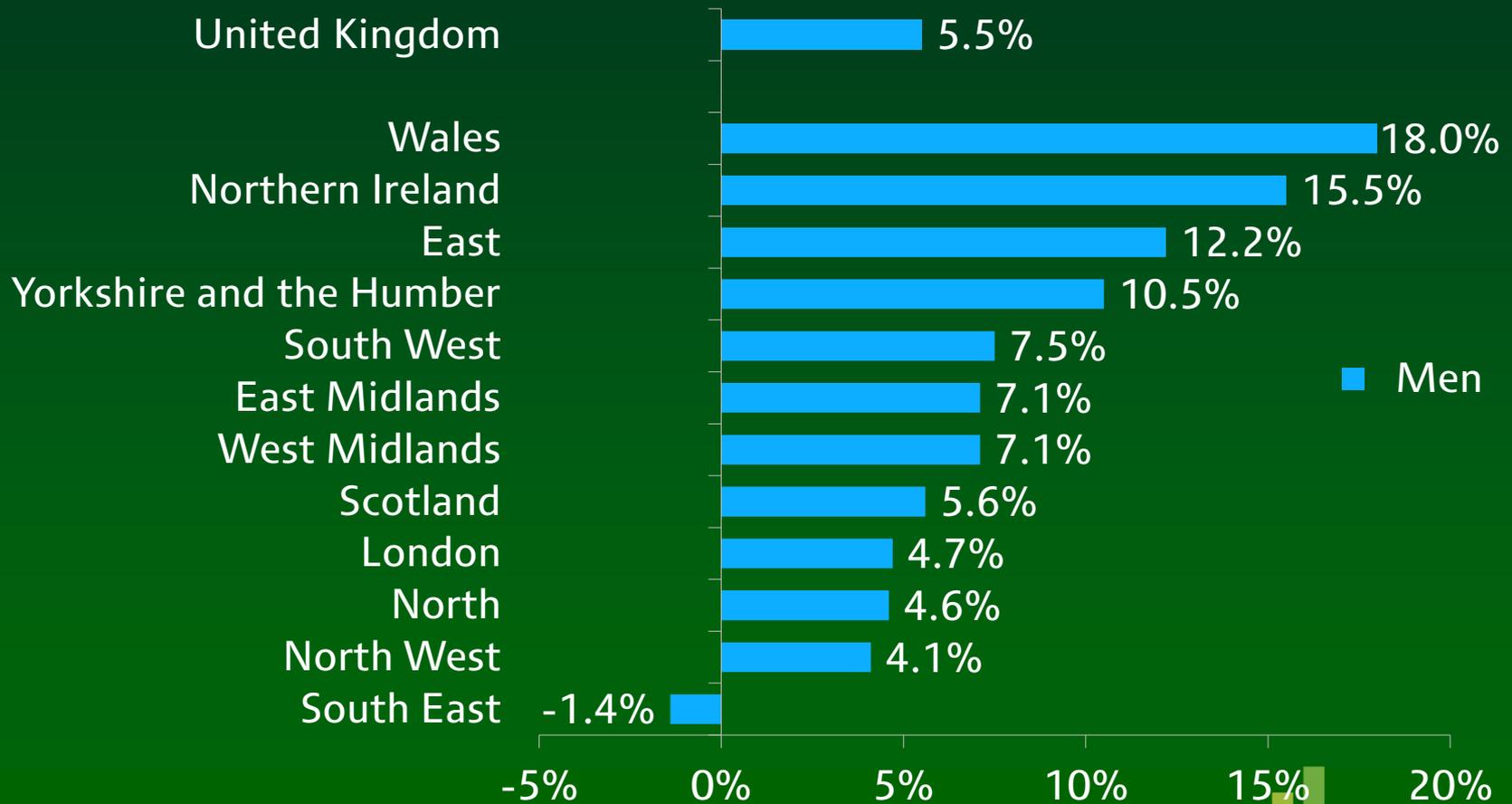


# Regional pay

- Chancellor has asked four pay review bodies to consider case for regionally varying public sector pay
  - teachers, NHS workers (but not doctors or dentists), senior civil servants and prison officers
  - only a minority of public sector workers potentially affected
- Large variation in estimated public sector pay premium provides a strong case for centrally set regionally varying pay

# Estimated public sector pay premium varies considerably across the country

Estimated average public–private hourly wage differentials, controlling for age and education, by region



# Regional pay

- Chancellor has asked four pay review bodies to consider case for regionally varying public sector pay
  - only a minority of public sector workers potentially affected
- Large variation in estimated public sector pay premium provides a strong case for centrally set regionally varying pay
- But tentative evidence suggests the premium across regions varies by occupation
  - relative pay among male police officers highest in Wales and for male secondary school teachers highest in the East Midlands
  - relative pay among female primary school teachers highest in the North West and for female midwives highest in the West Midlands
- Any regional variation in public sector pay awards would need to be carefully designed

# Conclusions

- Significant cuts to public service pensions already announced
- Latest public service pension reforms do much to improve structure of pensions
  - in some schemes reductions in the long-run generosity for high flyers offset by gains, on average, for those with lower earnings growth
- Public service pensions remain much more generous than those provided in the private sector
- Estimated public sector pay premium
  - increased since financial crisis, but to be reversed by Government
  - greater for lower earners
  - varies considerably by region
- Strong case for regionally varying, centrally set, pay awards
  - but apparent differences by occupation, so should be implemented with care

