PENSIONS AND LIFETIME SAVINGS ASSOCIATION

A RESEARCH SUPPLEMENT TO FIVE STEPS TO BETTER PENSIONS – FINAL REPORT

OCTOBER 2023

EXECUTIVE SUMMARY

This report updates the modelling included in the PLSA's consultation document, '*Five Steps to Better Pensions: Time for a New Consensus*' (PLSA 2022), to take account of changes that have taken place since its publication and provides details of the analysis included in *'Five Steps to Better Pensions: Final Report'* (PLSA 2023). In November 2022, the Government announced that the 2023/24 State Pension would be uprated in line with the Triple Lock. The Retirement Living Standards were independently reviewed and revised by Loughborough University and published by the PLSA early in 2023. Working with the Pensions Policy Institute (PPI), we have revised our modelling to take both issues into account.

The updated modelling shows that the overall combined effect of the package of proposals across the whole population continues to improve retirement outcomes for most people. By implementing the full suite of policy recommendations, including protecting the Triple Lock, all income levels are still found to have an improved income in retirement compared to someone saving for 50 years at the current minimum AE level i.e. 8% of band earnings. The projected retirement income for a median earner would increase from £17,672 to £20,609 for men (a 17% increase), and from £17,177 to £19,825 for women (a 15% increase).

Considering these outcomes against the metric of the Retirement Living Standards, the PLSA package of measures, including the plan to raise automatic enrolment contributions to 12%, would move those on median earnings from midway between the Minimum and Moderate RLS to much closer towards hitting a Moderate Retirement Living Standard.

We recognise that many people do not have linear working patterns throughout their lives and may change their employment and working patterns, with an associated impact on earnings and pension contributions. The PPI modelled the impact on retirement outcomes in such scenarios. The analysis suggested that all scenarios tested resulted in significant increases in retirement income between 7-17%, apart from those earning below the qualifying earnings for automatic enrolment (£10,000) who would not automatically be contributing to a pension.

The PLSA and PPI also undertook a new piece of work[1] to better understand the people who are excluded from automatic enrolment earnings due to the £10k earnings threshold, together with an assessment of whether, on balance, they are likely to benefit from extra pension saving. The research did not look specifically at whether they can afford to be included in automatic enrolment, but the findings suggest that almost 90% of this group would be no worse off in terms of working income or are part of a household with a higher income.

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[1] *Uncovering the profile of low earners in the UK and the potential for pension saving through auto enrolment*, PLSA, August 2023

INTRODUCTION

This report updates the modelling included in the PLSA's consultation document, *Five Steps to Better Pensions: Time for a New Consensus,* published last year and offers an updated assessment of the available evidence to enhance our understanding of pension inadequacy throughout the United Kingdom[2].

We have updated our modelling for two key reasons. Firstly, the State Pension Triple Lock was maintained. Secondly, our Retirement Living Standards, which are reviewed every year, were revised due to the changes in living costs over the past year and the amount now required to achieve a given living standard. As this was used as a key measure against which adequacy was assessed, we needed to rerun the analysis.

The PLSA commissioned the Pensions Policy Institute (PPI) to carry out modelling of the GB population which builds on work they carried out on behalf of B&CE (published in *Pensions Adequacy in Great Britain, findings from round 7 of the Wealth and Assets Survey*, August 2022).

The modelling featured in this report continues to use as its base round 7 of the Office for National Statistics Wealth and Assets Survey (WAS) to provide a snapshot of the state of saving and asset holding in Great Britain and project it forward to State Pension age for both individuals and households. A Technical Report on the modelling has been published by the PPI. The analysis and presentation of the modelled data in this report has been carried out by the PLSA.

Populations and individuals modelled

The modelling was designed to reveal the impact of the PLSA's policy recommendations including:

- Lowering the age from 22 to 18.
- Removing both the lower earnings and upper earnings limits.
- Increasing overall contributions to 12%, including increasing both employee and employer contributions to 6%.
- Employees making an additional 4% in voluntary contributions.

The policy recommendations were modelled across a range of different populations which included:

- The total UK population
- The total UK working population
- The total population currently saving into a Defined Contribution (DC) pension

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[2] See *Five Steps to Better Pensions – Final Report* (PLSA 2023).

The policy recommendations were modelled on individuals chosen specifically to include a range of different earnings levels and working patterns including:

Variations in earnings

- A median earner (Male: net £22,083; Female £23,309) who works full-time for 50 years
- A half median earner (Male: net £13,053; Female £13,666) who works full-time for 50 years
- A twice median earner (Male: net £39,859; Female £41,950) who works full-time for 50 years

Differing working patterns

- **Female with a mixed working pattern across 41 years** i.e. someone who starts part-time work at 18 for 5 years, then works full-time for 36 years on:
    - Half median earnings (net £6,969)
    - Median earnings (net £13,500)
    - Twice median earnings (net £22,978)

- **A female with a break in work:**
    - A female earner who starts work part-time at 18 for 45 years with a 5-year break on half median earnings (net £7,091) and median earnings (£13,666)
    - A female earner who starts part-time work at 18 for 40 years with a 10-year break on half median earnings (net £7,091) and median earnings (net £13,482)

- **A female with mixed income and hours**
    - A female half median earner who starts work full-time at 18 for 5 years, then works full-time for 35 years on a median income before going part-time for 8 years on a half median income (net £7,091)
    - A female median earner who starts work full-time at 18 for 40 years, then works part-time for 10 years on a half median income (net £7,091)

Note that the earnings figures above are the net earnings at age 67. Salaries are based on the Labour Force Survey and were incorporated within the modelling for each year of age and gender. Men's median salaries peak at a higher amount than women's (£31,603 vs £27,570) and amount to greater lifetime earnings. However, by the age of 67 within the LFS dataset, the median salary of a woman is higher than that of a man as a result of a greater tapering of incomes towards retirement for men than women.

RESEARCH FINDINGS

Current Situation

Over the course of the year, the PLSA, with the support of the Pensions Policy Institute (PPI), updated its original adequacy modelling to take account of the 2023 increase in the State Pension. According to our modelling and projections and as set out in the PLSA's consultation document, *Five Steps to Better Pensions: Time for a New Consensus*, only half (52%) of the population are projected to meet the retirement income targets set by the 2005 Pensions Commission, with many facing poverty in retirement.

Pensions Commission Replacement Rate - Households

More people in the total population are now on track to meet their Pensions Commission Replacement rate (52%) than they were prior to the increase in the Triple Lock (49%). This is also reflected within the working population: 45% compared to 41% and the active DC population 40% compared to 38%.

**Figure 1: Percentage hitting the Pensions Commission Replacement Rate pre and post Triple Lock Increase**
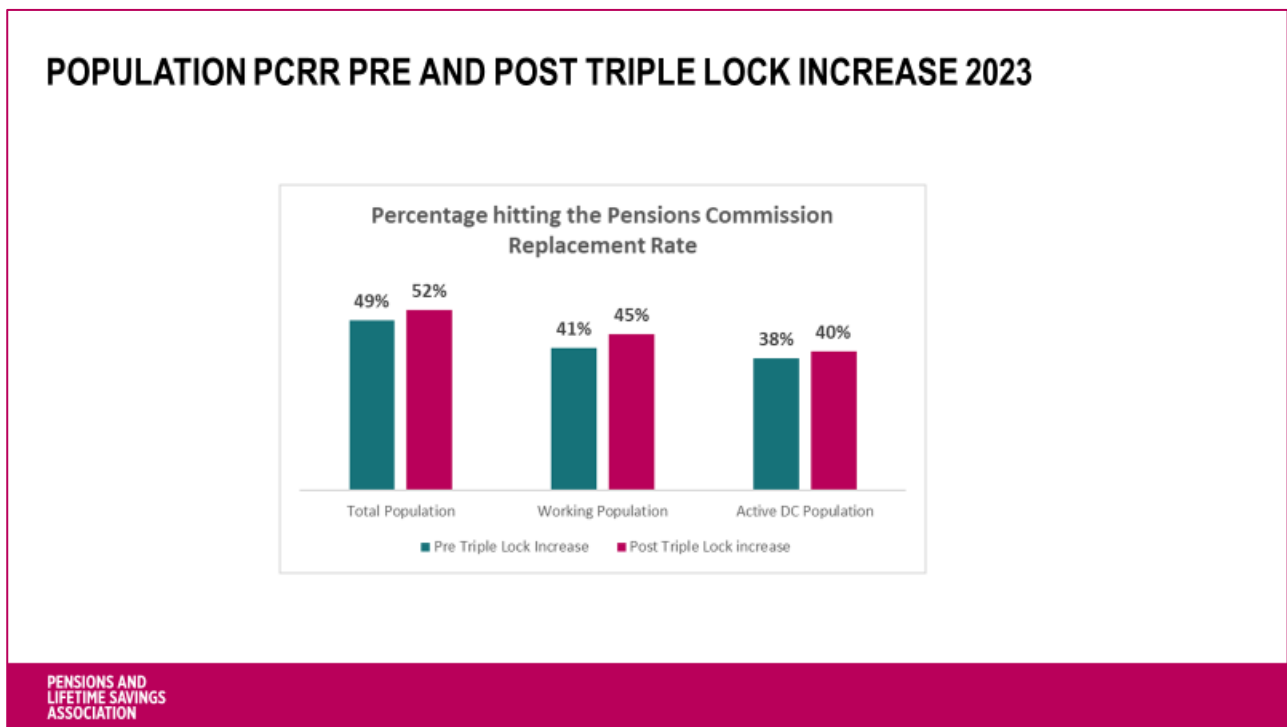
This suggests that c.17 million households amongst the *whole population,* c.6.5 million *working households* and c.2.2 million *DC saving households are on track to meet their Pensions Commission Replacement rate.*

Retirement Living Standards - Households

The Triple Lock increase has improved outcomes measured against the Pensions Commission Replacement Rate. However, as that metric is based on the retirement income as a percentage of pre-retirement income, it does not take account of the impact of the costs required to achieve a particular living standard in retirement.

The Retirement Living Standards reflect the actual adequacy of a retirement income in terms of the type of living standard that an individual may achieve considering the costs of goods and services used in daily living. Measured against the RLS, the Triple Lock increase has had a much more muted impact with a decline in the population achieving the minimum, reflecting the large proportion of the minimum standard that is made up of food items which have been particularly hit by large inflationary increases (higher than the headline rate of inflation), and little movement at the moderate and comfortable levels.

Figure 2: Percentage of Households hitting the RLS
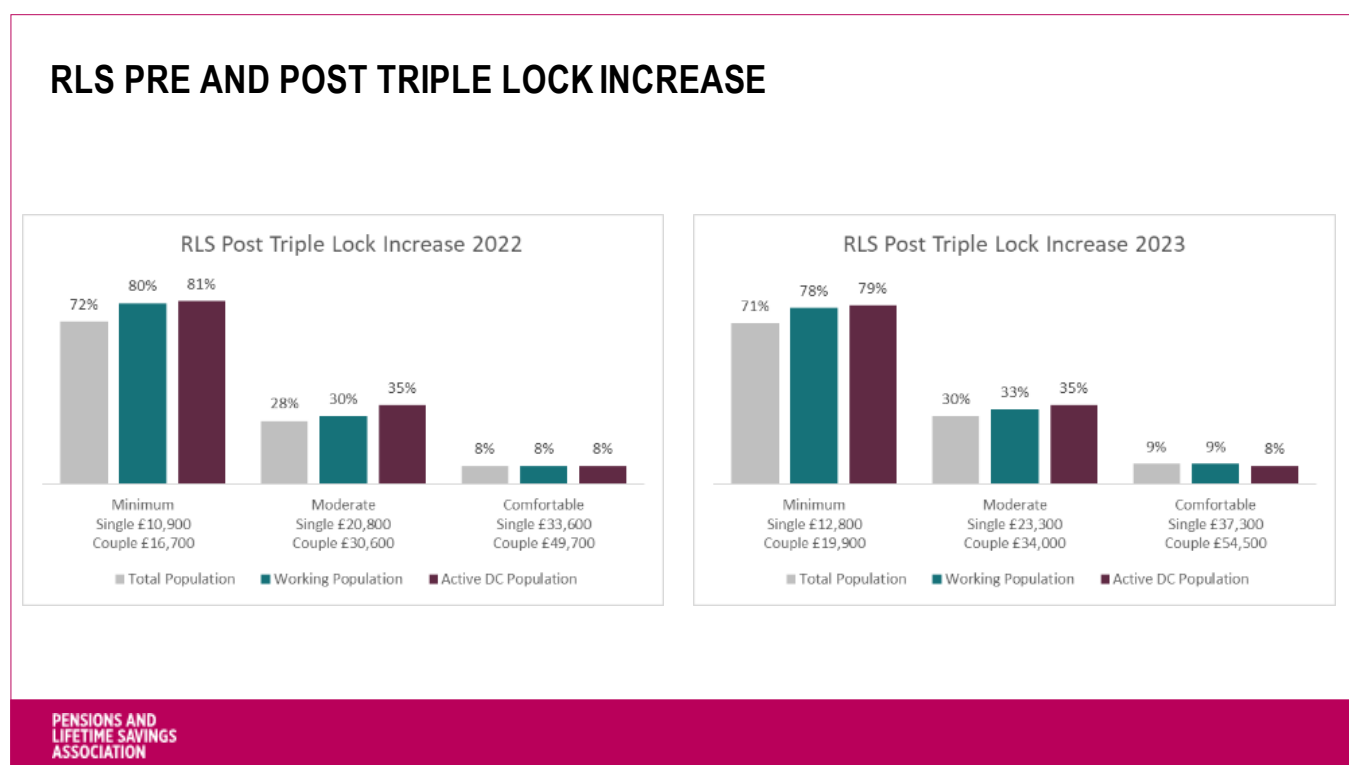
The analysis shown in the chart above shows the modelled retirement outcomes for the different populations assessed against the previous values of the Retirement Living Standards and State Pension (chart on the left) and the latest values for both (chart on the right). When looking at the retirement outcomes for different populations using the 2023 Retirement Living Standards as a reference point, among the *whole population*, 71% of households (12 million households out of a total of 17 million households) are on track to hit the **Minimum Retirement Living Standard (£19,900 for a couple)**, while among the *working population*, slightly more households are

likely to hit the Minimum Retirement Living Standard (78% households), with similar numbers among those who are *currently saving into a Defined Contribution (DC) pension* also likely to hit the Minimum Retirement Living Standard (79% households).

When looking at the Moderate Retirement Living Standard, only 30% of households of the *whole population* are currently on track to hit the **Moderate Retirement Living Standard (£34,000 for a couple)**. This compares to 33% of households of the *working population* and 35% of households *currently saving into a Defined Contribution (DC) pension.*

In terms of the **Comfortable Retirement Living Standard (£54,500 for a couple)**, less than one in ten households of any population are on track to hit this level of retirement living standard.

The impact of the revised modelling when using housing wealth can be found in Appendix A.

IMPACT OF DIFFERENT POLICY MEASURES

Since we made our proposals last October, the Government uprated the State Pension in line with the Triple Lock. The Minimum level of the Retirement Living Standards was also independently updated. Working with the PPI, we have revised our modelling to take both issues into account.

The following analysis is based on someone saving from 18, the removal of band earnings and increasing contributions to 12%. The revised modelling demonstrates that if all the PLSA measures were implemented, all earnings levels analysed would have improved retirement outcomes from the policy changes. Specifically, median earners and half median earners would see significant improvements.

A median earner would see a significant increase in their projected retirement income, with men increasing their projected retirement net income from £17,672 to £20,609 – an increase of £2,937 or 17% compared to their current projected outcome. Women would increase their projected net income from £17,177 to £19,825 – an increase of £2,648 or 15% compared to their current outcome.

If an additional voluntary contribution of 4% was also made, a median earner would see their projected retirement income increase from £17,672 to £22,595 for a man – an increase of 28%, and from £17,177 to £21,549 for a woman – an increase of 25%.

Twice median earners with 12% contributions would have a projected income of £26,566 for men and £24,997 for women. Twice median men would see their retirement income increase by 37% (£7,186) and women by 29% (£5,619).

If an additional voluntary contribution of 4% was also made, a twice median earner would see their projected retirement income increase from £19,380 to £30,538 for a man – an increase of 58%, and from £19,378 to £28,445 for a woman – an increase of 47%.
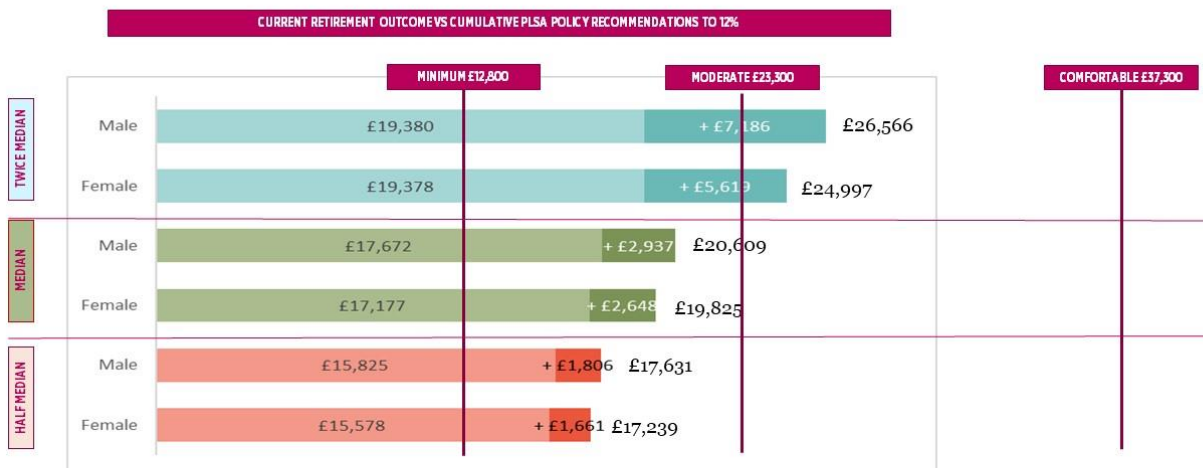
Among half median earners, the cumulative impact of these measures would mean they have a projected retirement income of £17,631 for men and £17,239 for women. Half median men would see their retirement income increase by 11% (£1,806) and women by 11% (£1,661).

➢ **Improvements in retirement outcomes measured against the Retirement Living Standards**

The PLSA package of measures, including the plan to raise automatic enrolment contributions to 12%, would move those on median earnings from midway between the Minimum and Moderate RLS to much closer towards hitting a Moderate Retirement Living Standard. Twice median earners (both men and women) will move from over midway between Minimum and Moderate RLS well past the Moderate. Half median earners will move from under midway between Minimum and Moderate RLS to well over the midpoint between Minimum and Moderate RLS.

Figure 3: Summary of the cumulative impact of PLSA policy recommendations to 12%

PLSA POLICY RECOMMENDATIONS VS RLS AT 12% CONTRIBUTIONS

		CURRENT RETIREMENT OUTCOME VS CUMULATIVE PLSA POLICY RECOMMENDATIONS TO 12%		
		MINIMUM £12,800	MODERATE £23,300	COMFORTABLE £37,300
TWICE MEDIAN	Male	£19,380	+ £7,186 £26,566	
	Female	£19,378	+ £5,619 £24,997	
MEDIAN	Male	£17,672	+ £2,937 £20,609	
	Female	£17,177	+ £2,648 £19,825	
HALF MEDIAN	Male	£15,825	+ £1,806 £17,631	
	Female	£15,578	+ £1,661 £17,239	

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If savers were to add 4% additional contributions above the 12% on a voluntary basis, it would push those on median earnings close to the Moderate level (£23,300), with women expected to reach £21,549 and men £22,595. Twice median earners would move significantly from over midway between Minimum and Moderate RLS to comfortably surpassing the Moderate RLS, thereby achieving some aspects of the Comfortable standard, with women expected to reach £28,445 and men £30,538.

ANALYSIS OF THE IMPACT ON PEOPLE WITH VARIOUS WORKING PATTERNS

We recognise that many people do not have linear working patterns throughout their lives. Many people will face periods out of work for varying reasons or may change their working patterns and employment with an impact on their earnings and pension contributions. The PPI therefore modelled the impact on retirement outcomes on a number of subgroups with varying work patterns, and changes in income. This included the following groups:

- **Female with a mixed working pattern across 41 years** i.e. someone who starts part-time work at 18 for 5 years, then works full-time for 36 years on either half median, median or twice median earnings.

- **A female with a break in work:**
    o A female earner who starts work part-time at 18 for 45 years with a 5-year break on half median earnings or median earnings
    o A female earner who starts part-time work at 18 for 40 years with a 10-year break on either half median earnings or median earnings

- **A female with mixed income and hours**
    o A female half median earner who starts work full-time at 18 for 5 years, then works full-time for 35 years on a median income before going part-time for 8 years on half median earnings
    o A female median earner who starts work full-time at 18 for 40 years, then works part-time for 10 years on a half median earnings

The modelling demonstrated that the policy proposals have a positive impact on people who have working patterns other than full-time employment or reduced years of employment.

Illustration A: Female with a mixed working pattern across 41 years
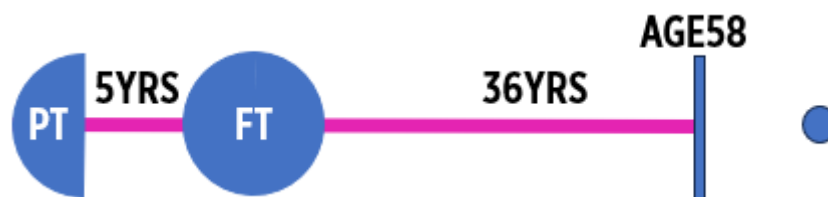
A female earner with a shorter overall working life and a mixed working pattern i.e. someone who starts part-time work at 18 for 5 years and then works full-time for 36 years under the PLSA policy proposals would see their projected income increase between 8% and 17% depending on their level of income.

In this model, it is assumed that the individual will start drawing on their pension at a younger age when they stop work at 59, then at age 68, they will receive State Pension/pension credits and income from their pension.

	Net Income at 59	Net income at retirement under current policy situation (£)	Net income at retirement if all PLSA policy recommendations applied up to 12%	% Improvement
Half median	£6,969	£6,234	£6,714	8%
Median	£13,500	£10,760	£12,097	12%
Twice median	£22,978	£12,224	£14,294	17%

Illustration B: Female with a break in employment

A female median earner who works part-time across most of their working life (40 or 50 years), with a gap in work (5 or 10 years) under the PLSA policy proposals would increase their income by 7-9%.

In contrast, a female with similar working patterns but on a half median income would be below the qualifying earnings for automatic enrolment and therefore, would not be contributing to a pension. However, their retirement net income would be higher than their income at 67 due to the receipt of pension credit and the State Pension.

	Net Income at 67	Net income at retirement under current policy situation (£)	Net income at retirement if all PLSA policy recommendations applied up to 12%	% Improvement
A female median earner who starts part-time work at 18 for 45 years with a **5-year break**				
Half median	£6,956	£9,030	£9,030	0%
Median	£13,666	£15,458	£16,900	9%
A female median earner who starts part-time work at 18 for 40 years with a **10-year break**				
Half median	£7,091	£9,030	£9,030	0%
Median	£13,482	£15,156	£16,183	7%

Illustration C: Female mixed income and hours

A female half median earner who starts work full-time at 18 for 5 years, then works full-time for 35 years on a median income before going part-time for 8 years on a half median income, would see their projected income increase by 14% compared to their current projected outcome.

	Net Income at 67	Net income at retirement under current policy situation (£)	Net income at retirement if all PLSA policy recommendations applied up to 12%	% Improvement
Mixed Income	£7,091	£16,853	£19,260	14%

Illustration D: Female mixed income and hours

A female median earner who starts work full-time at 18 for 40 years, then works part-time for 10 years on a half median income, would see their projected income increase by 13% compared to their current projected outcome.

|	Net Income at 67	Net income at retirement under current policy situation (£)	Net income at retirement if all PLSA policy recommendations applied up to 12%	% Improvement
Mixed Income	£7,091	£16,893	£19,133	13%

APPENDIX A

Using Housing Wealth

The inclusion of housing wealth (in the form of income generated from housing equity) in each projection of retirement income would result in a higher number on track to meet the Pensions Commission Replacement rate.

Assuming the use of housing wealth amongst the *whole population* would result in over half of households (61%) being on track to meet the Pensions Commission Replacement rate. However, when looking at the working population and those who are currently saving into a Defined Contribution (DC) pension these figures fall:

- only 55% of working households will achieve the Pensions Commission Replacement rate.
- only 51% of DC Saving households will achieve the Pensions Commission Replacement Rate.

Figure 4: Percentage hitting the Pensions Commission Replacement Rate using housing wealth
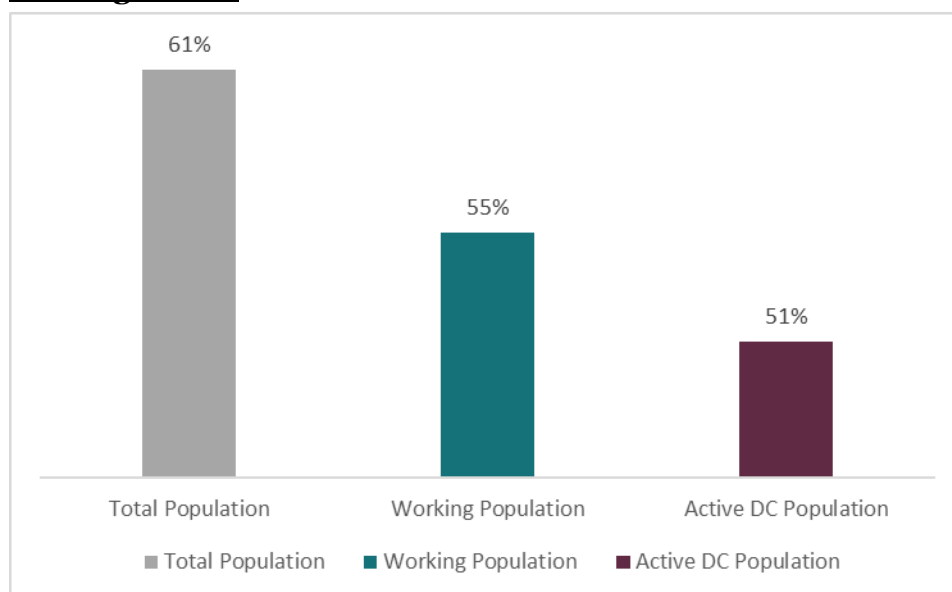
Using the same assumption on housing wealth would improve the outcomes measures against other metrics. Assessed against the Retirement Living Standards, more would be on track to meet these standards across the various populations. For example, amongst the whole population, 75% of households are on track to hit the Minimum Retirement Living Standard; this compares to 71% if housing wealth is not included.

Among the *working population*, slightly more households are likely to hit the Minimum Retirement Living Standard (82% households - up from 78% when not using housing wealth), with similar numbers among those who are *currently saving into a Defined Contribution (DC) pension* also likely to hit the Minimum Retirement Living Standard (81% households - up from 79% when not using housing wealth).

Housing wealth has a greater impact on reaching the Moderate Retirement Living Standard for all types of population.

- 38% of the overall population will hit the Moderate Retirement Living Standard (up from 30%)

- 42% of the working population will hit the Moderate Retirement Living Standard (up from 33%)

- 43% of those saving into a Defined Contribution (DC) pension will hit the Moderate Retirement Living Standard (up from 35%)

In terms of the Comfortable Retirement Living Standard, just over one in ten households of any population are on track to hit this level of retirement standard if adding in housing wealth.

Figure 5: Percentage of Households hitting the RLS, if using housing wealth
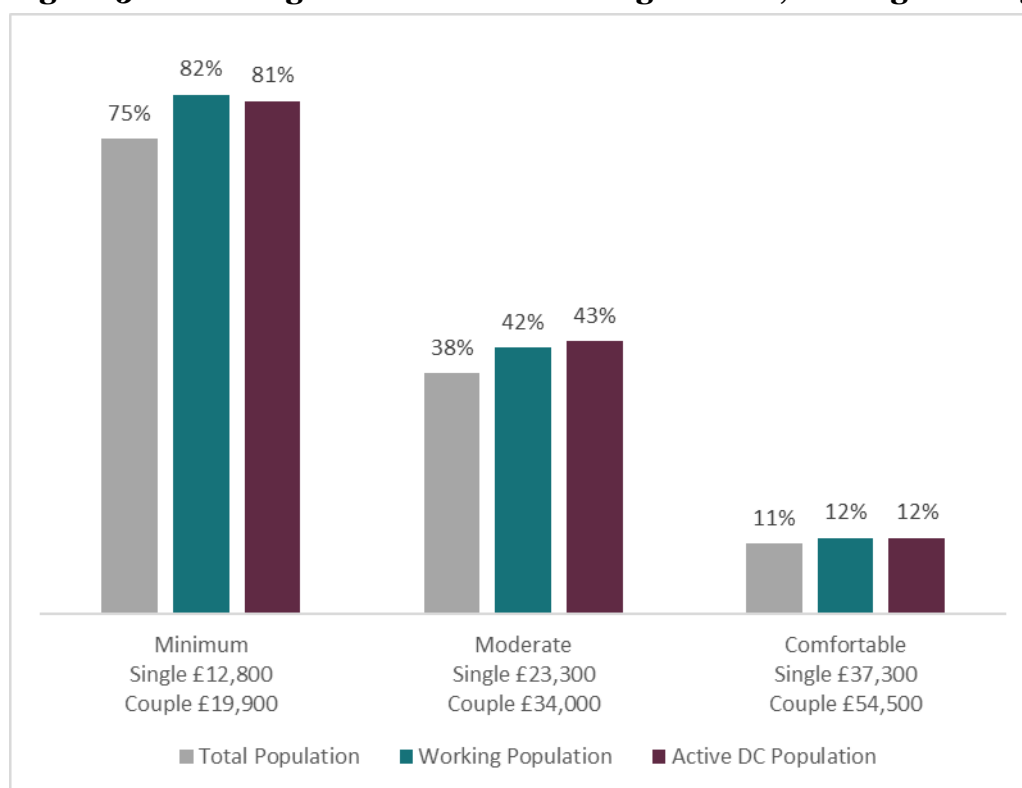
Meeting the target Pensions Commission Replacement Rate – the impact of having DB savings

Those with DB entitlement are much more likely to hit their target Pensions Commission Replacement Rate than those without DB savings.

Current Situation - Pensions Commission Target Replacement Rates by DB entitlement				
No DB entitlement	Less than £1.5k DB entitlement	£1.5k up to £6k DB entitlement	£6k up to £12k DB entitlement	More than £12k DB entitlement
35%	34%	39%	51%	78%

Base: All DC Savers – assuming all pension used to derive pension income

Meeting the Retirement Living Standards – the impact of having DB savings

The analysis shows that those with significant DB, especially those with more than £12,000 per annum DB entitlements, are far more likely to be on track to hit all the Retirement Living Standards than those without DB savings, with just over two-fifths (41%) achieving the Comfortable RLS.

Figure 6: Current situation – Retirement Living Standards by DB entitlement
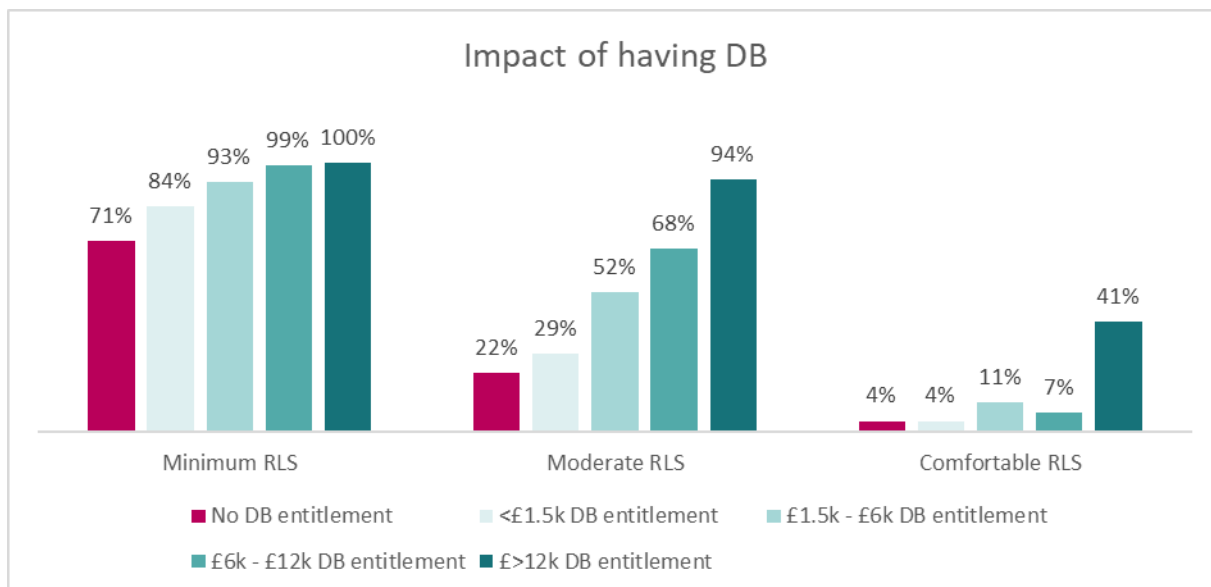
Base: all DC savers – assuming all pension used to derive pension income

ACKNOWLEDGEMENTS

We thank the Pensions Policy Institute for their detailed analysis and technical report which was the basis for the presentation of findings used in this summary research report. Any errors or omissions in the discussion of the survey findings are attributable to the summary research note author.

The technical report can be found on the Pensions Policy Institute website: https://www.pensionspolicyinstitute.org.uk/