intergenerational foundation
Fairness for Future Generations

Public Inquiry Response:
"The Cridland Review Interim Report"

To: The Cridland Review of the State Pension Age

By: The Intergenerational Foundation

Date: 27 December 2016

The Intergenerational Foundation (www.if.org.uk) is an independent think tank researching fairness between generations with regard to such issues as housing, employment, taxation, education, the environment and health. IF's guiding principle is that policy should be fair to all – the old, the young and those to come.

Introduction:
The Intergenerational Foundation (IF) welcomes the opportunity to comment on the long-term direction of government policy towards the state pension age. The Cridland Review's Interim Report raises many valid issues regarding the state pension, particularly in relation to the themes of affordability and fairness. IF would like to make the reviewers aware of the following points before the next stage of the Review is undertaken:

1) The fairest outcome is for the state pension to become means-tested
IF has consistently argued that the fairest way to maintain both the adequacy and affordability of public spending on older people in the face of rising longevity is to ensure that spending on the whole range of pensioner benefits – including the state pension – is targeted effectively at the poorest section of the pensioner population. Therefore, IF believes that the ultimate direction of travel for state pension policy should be towards making the state pension fully means-tested.

Although means-testing is controversial, IF believes that this outcome would be desirable for several reasons. Most importantly, it would not only improve fairness between different generations by counteracting the divergence in incomes between current pensioners and those of working age, it would also increase intra-generational fairness by addressing inequality within each cohort of pensioners. The interim report emphasises that there is an important trade-off under the current system between the pace at which the state pension age will increase and the way the state pension is uprated; the example given is that removing the triple lock could enable the government to implement increases in the state pension age more slowly, or vice-versa. However, IF believes that there is a bigger trade-off to be negotiated between how much the country can afford to spend on the old-age social safety net and how widely that net is cast. Figure 10 within the interim report demonstrates that incomes among the current generation of pensioners are extremely unequal: the state pension accounts for only 34% of the incomes of the richest fifth of pensioners, but represents almost the entire income (94%) of the poorest fifth of pensioners.

Although the interim report notes that these inequalities are expected to narrow somewhat over the coming decades as Generations X and Y move into retirement, they are still projected to remain significant. Current government policy towards the triple lock has perpetuated these inequalities by significantly boosting the incomes of all pensioners, even the most well-off, while the broader austerity agenda has disproportionately taken public resources away from the least well-off pensioners who make the greatest use of government services. The most egregious example of this has been the persistent under-funding of old-age social care services, spending on which fell by 25% between 2010 and 2015 (King's Fund, 2016). Means-testing the state pension could enable spending on pensioner benefits to be kept within the Pension Commission's proposed envelope of 7.5–8% of GDP while also enabling the government to do more to help the poorest and most vulnerable pensioners.

However, if this option is considered to be outside the scope of the Cridland Review then IF would support the removal of the triple lock and its replacement with an earnings lock, as we believe this would be fairer in intergenerational terms than simply increasing the state pension age (which disproportionately harms the interests of future cohorts and pensioners compared to current pensioners, and poorer future pensioners compared to wealthier ones) while retaining the triple lock.

2) Generation Y face significant barriers to private pension saving

The Cridland Review is correct to factor the adequacy of private pension savings into its assessment of how rapidly the state pension age should be increased. However, IF is concerned that the interim report understates the difficulties which members of Generation Y face when it comes to building up pension savings. The data presented in the interim report suggest that as successive birth cohorts pass into retirement there will be an increase in the proportion who have some kind of private pension savings because of auto-enrolment, but the value of these savings is expected to fall because of decreased access to the more generous defined benefit occupational pension schemes. The interim report argues that these trends should reduce inequality within pensioner cohorts over time, largely because there will be fewer people at the top of the pensioner income distribution receiving very large defined benefit pensions.

However, IF believes that some other important factors need to be taken into account when considering how much future generations of retirees are likely to have saved in pensions. Most importantly, IF has significant concerns about the adequacy of auto-enrolment pensions for providing today's young adults with a decent income in retirement. This is because, firstly, it is likely that many people who have defined contribution pensions will save too little; modelling by the Pensions Policy Institute has estimated that half of savers who only contribute the minimum of 8% into an auto-enrolment pension will end up with a retirement income which is below the Pension Commission's recommended replacement rates (PPI, 2013). Secondly, for Generation Y to accumulate pension pots relies upon the government continuing to support auto-enrolment throughout their working lives, which, given that pension policy exists in a state of almost constant reform, is far from certain..

Thirdly, it is not a given that pensioner income inequality will reduce among Generation Y because of the impact of intergenerational transfers from their parents and grandparents; those who stand to inherit the housing and pension wealth which has been acquired by the Baby Boomer generation will receive a significant advantage when it comes to saving for their own retirements, particularly if they have been able to get on the housing ladder when their less wealthy counterparts have not. For those members of Generation Y who cannot expect to inherit significant wealth, many will have to grapple with high housing costs throughout their lives (especially if they remain in the private rented sector), and, for the foreseeable future, poor wage growth. These factors are likely to make them more dependent upon the state pension to fund their retirements when they reach old age, so they need to be considered when designing the future timetable of state pension increases.

If you would like to learn more about the work of the Intergenerational Foundation or would like to organise a meeting to discuss the points we raise, please contact:

Liz Emerson, Co-Founder
Email: liz@if.org.uk Mobile: 07971 228823