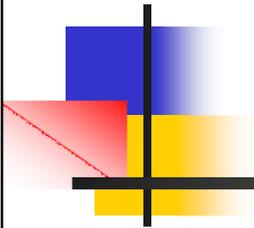


All-Party Parliamentary Group for Social Science and Policy

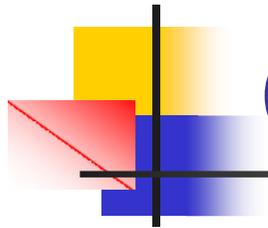


Credit crisis: The Impact on Pensions

11 February 2009

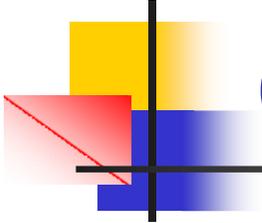
Dr. Ros Altmann

www.rosaltmann.com



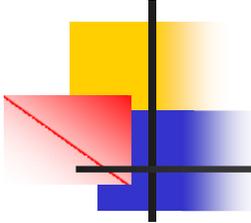
Overview

- Credit crisis and pensions
- Policy for Pension Schemes
- Policy for pensioners
- Policy proposals summary
- Key points for policymakers



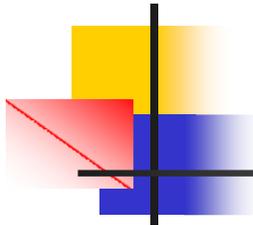
Credit Crisis – effect on pensions

- Employers struggling with huge deficits – final chapter for final salary
- Dangers for corporate UK - more schemes will close
- Employers looking to cut contributions instead of jobs?
- Individuals' private pension savings plummeted in value
- Pensioner poverty will be worse as private pensions fall



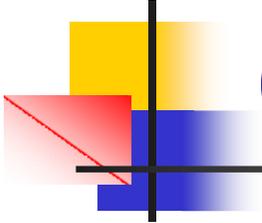
Pension Schemes in future

- Investment returns unreliable – over-reliance on equities
- Unrealistic expectations exposed further by credit crisis
- Pension received will depend on
 - Contributions – being cut
 - Investment returns (net of fees) – fallen sharply
 - Annuity rates – getting worse, especially if final salary schemes buy out



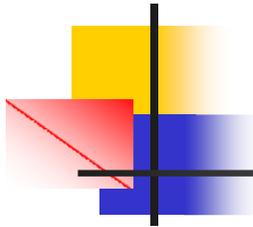
Policy proposal

- **Issue pension and annuity gilts**
 - Long duration
 - Ipi linked (0-2.5%, 0-5%) – not rpi
 - Mortality-longevity linked
- Help to match liabilities and back annuities
- Far better than issuing short-term paper
- Help finance public sector borrowing domestically
 - Hundreds of billions of pounds of institutional demand



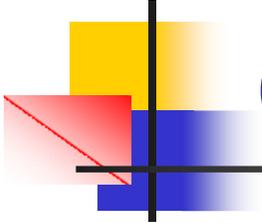
Credit crisis effect on pensioners

- VAT cuts little help
- Rate cuts are like cutting state pension – on £10,000 savings, income cut by £10pw, this is not expansionary!
- Transferring money from older savers to younger borrowers – and banks
- Easing monetary policy is scattergun approach
- Dramatic rate cuts gone too far - damage confidence
 - Deflation fears misguided, only short-term, temporary
- Pensioners suffer collateral damage, no deflation
 - Food and drink up 10%, household services up 14%



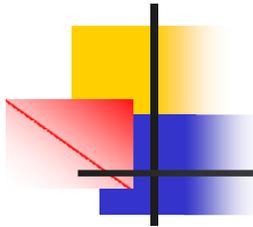
Policy proposal

- Bring back the 10p tax rate
- Cut direct taxes, not indirect taxes and interest rates
- Help all taxpayers, but especially lowest earners
- Simple to understand
- Rather than 'compensate' losers, just unwind error



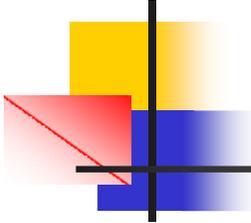
Crisis problems for pensioners

- Pension credit undermines private saving and earnings
- Still assumes they earn 10% on their savings
- Still has £5pw earnings disregard
- As population ages we can't keep borrowing from future taxpayers if they aren't there
- Must stop penalising savers
- More pensioners will need pension credit to avoid poverty



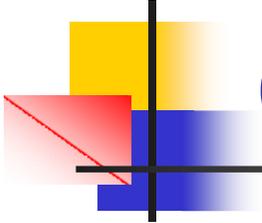
Policy proposal

- Reform pension credit assumptions
 - Change 10% interest rate assumption
 - Increase £5pw earnings disregard



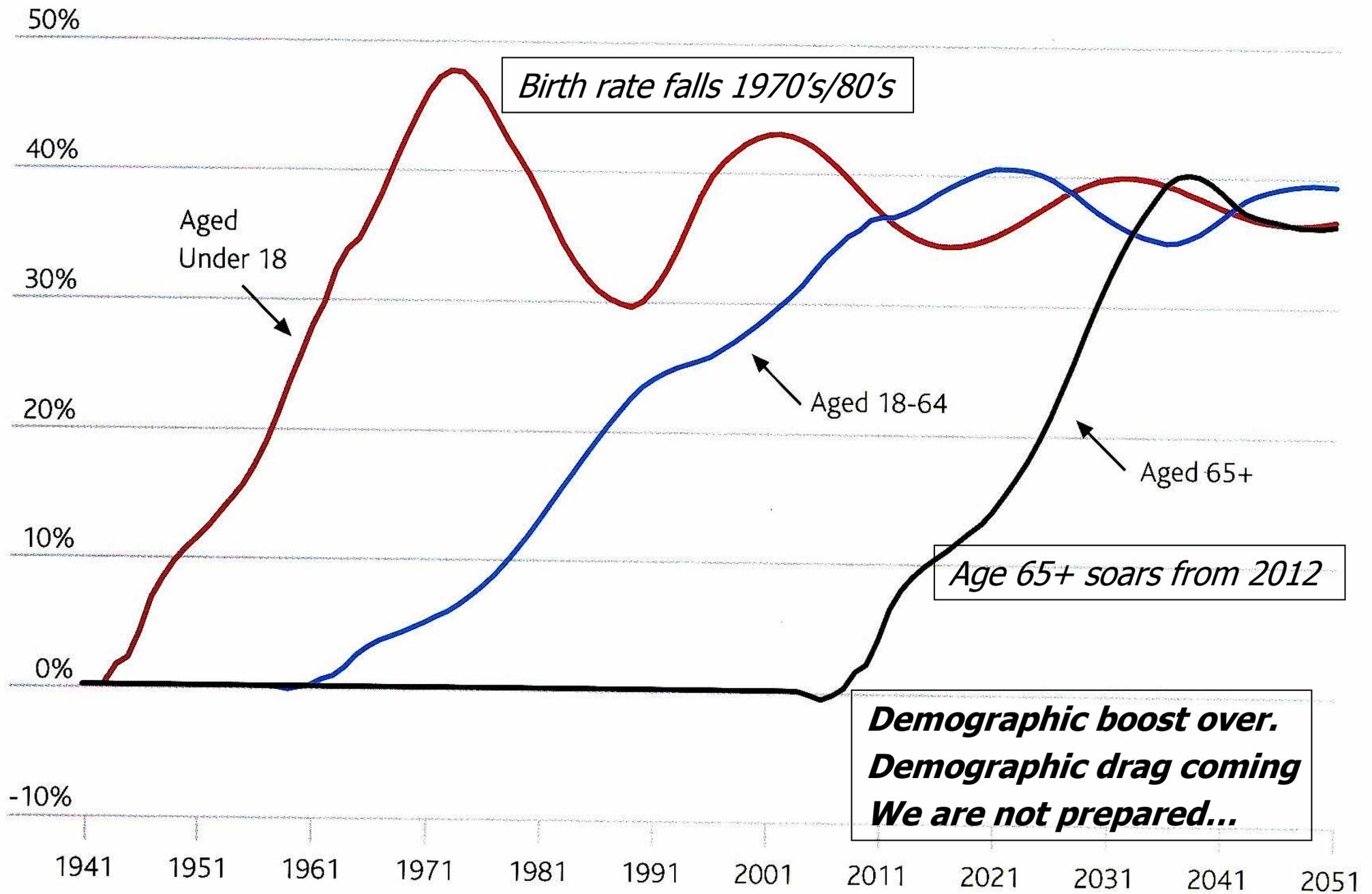
Policy proposal – radical reform

- Pay £140pw pensions to all over 75s
- Cost £2bn a year – reform tax relief, contracting out
- End poverty for the elderly – no take-up problems
- Help poorest pensioners spend more
- Fair to women, cut admin costs of means testing
- No more annuity requirement

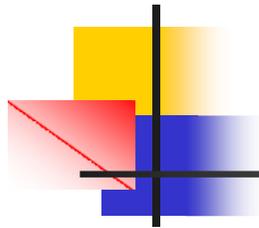


Credit crisis – demographic context

- Official view: no pensions crisis now but may be in future
- Wrong: pensions in crisis now, ***pensioners*** in crisis soon
- Baby boomers reaching age 65 after 2010
- Economy benefited from demographic boost
- Savings were discouraged in the boom times: short-sighted policy, now value of savings decimated
- Heading for demographic drag - huge growth in age 65+
 - What will they live on? Economic decline...

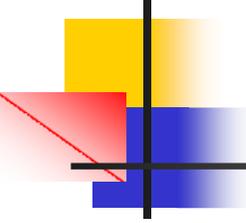


Source: Pensions Commission analysis based on a synthetic model of the England and Wales population



Lessons for the future

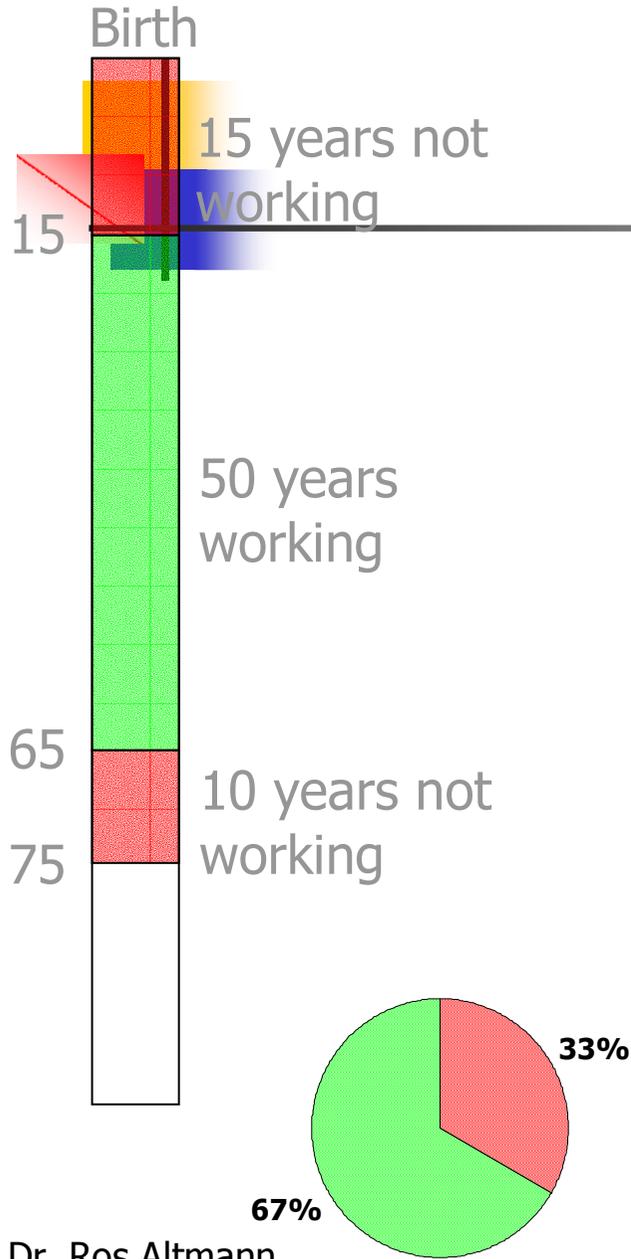
- Politicians and industry want money going in now, but getting good pensions OUT is vital to individuals later!
- This is not just a 'pensions' issue – it's a retirement issue
- Can't sort out pensions without rethinking retirement
- Pensions are trying to last too long
 - Most people can't save for 25-30 year decent pensions
- What a waste of resources!
- Policy lagged behind improved life expectancy, health, working practices



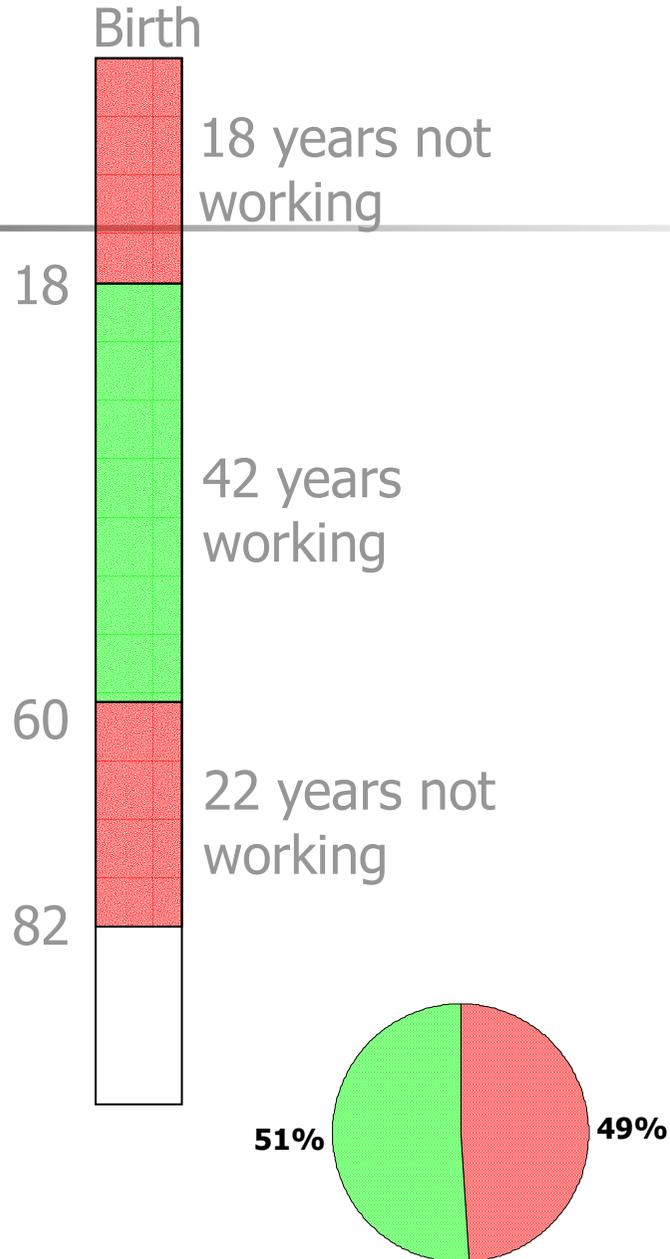
Pensions alone can't solve the pensioners crisis

- New phase of life waiting to be enjoyed – 'bonus years'
 - 2-3 days working, 4-5 days off, sabbaticals, retraining
- Cut down gradually - part-time working, job sharing
 - Precedent: working mums with young kids
- More leisure and more money to enjoy the leisure
- Better for individuals, employers and the economy
- Age discrimination should not stop at 65

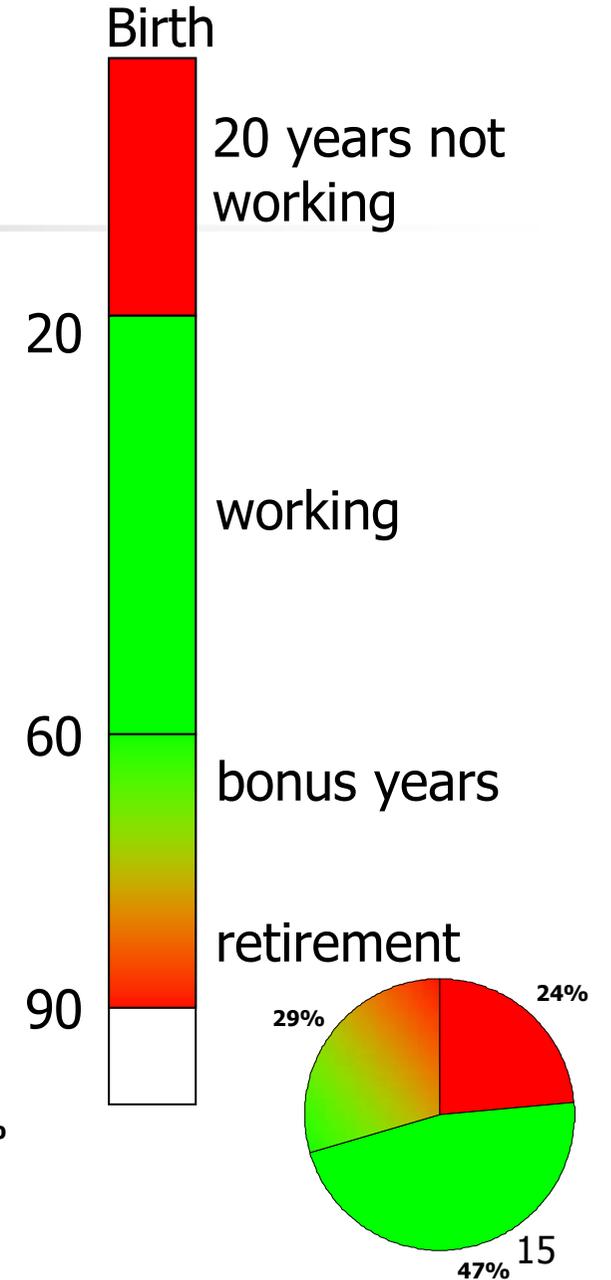
1950's

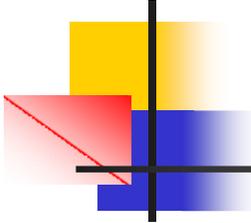


Now



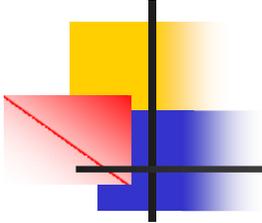
Future?





Policy recommendations summary

- Issue pension gilts and annuity gilts
- No more interest rate cuts – cut direct taxes
- e.g. bring back 10p tax rate?
- Change assumed 10% pension credit interest rate and £5pw earnings disregard
- Increase state pension to £140 a week for all over 75s
- Radical rethink of pensions and retirement – encourage longer, part-time, working lives



Key points for policymakers

- Pensions hurt badly by crisis
- Rate cuts damage confidence, hurt pensioner incomes, worsen annuity rates
- Pension credit still assumes 10% interest on savings
- Bank accounts now far safer than pensions
- Tax relief and contracting out cost billions each year
- Baby boomers about to hit 65 with little income
 - Drag on growth, need radical reforms