Generation game

The media is full of stories about generational conflict. David Adams asks if the UK pensions system really does treat younger workers unfairly, or if there are more productive ways to think about changes that will help deliver a more comfortable retirement for everyone

Summary

- A media narrative suggests the babyboomer generation have ruined the prospects of the millennial generation in various ways – does the UK's pensions system put younger people at a disadvantage?
- While most young people will miss out on generous pensions enjoyed by some older people, other groups in society are in a difficult position, in every generation, including women and gig economy workers.
- Generation X face particular challenges as they try to save enough money to fund their retirement.
- There are many interesting policy ideas that could help resolve unfairness to different groups in the pensions system and the wider economy, but politicians and society will need to take genuinely long-term decisions for the greater good.

Are you old and smug, or young and resentful? If you believe some of the commentary that appears regularly in the media, you would be under the impression that there is a war underway between different generations in the UK. The babyboomer generation are usually cast as the villains. They tend to be compared unfavourably to their parents' generation, which lived through the war, then made huge sacrifices to help the babyboomers grow up in a paradise of near full employment, cheap housing and free university tuition. According to this narrative, the babyboomers then ruined the world for younger generations, by screwing up the economy, selling off the nation's assets, hoarding housing wealth, destroying the environment, voting for Brexit and so on.

Most sensible observers know that this picture does not match a more complex reality. Pensions expert and former pensions minister Baroness Ros Altmann rails against the idea of generations being pitted against each other, because "society is supposed to be about people working together to support each other"; but also because generalisations about the economic fortunes of entire generations are clearly nonsense.

But it is true that the generations that have followed the babyboomers, particularly Generation X (those born between the late 1960s and the early 1980s) and the millennials, face formidable financial challenges, created in part by decisions and mistakes made in the past. The UK's pensions system is a case in point. While rising life expectancy will put the NHS, social care provision, and the state pensions and benefits systems under huge stress in future, younger people will be working to support the country's retired population – just as other economic factors undermine their own efforts to accumulate wealth.

"By historical standards it does look like the current pensions system treats younger people less fairly," says PwC director Steven Taylor. In part this is because far fewer younger people will have access to DB pensions, which generally deliver better retirement outcomes than DC pensions, particularly in the current, low interest rate, low bond yield environment.

Younger people are also funding many of the DB pensions being paid out to retirees. "The baby boomers, when they were working, paid what everyone thought was a fair contribution to their pension costs," says Royal London director of policy (and former pensions minister) Steve Webb. "Now we know

that the cost of those pensions is bigger than was thought. Today's workers in firms that used to have DB schemes are paying the price of those schemes." While many public sector workers will have DB pensions in some form that are more generous than many pensions available to private sector workers, the public service pensions and the conditions attached to them are also now less generous than in the past – and today's public sector workers will also be paying the pensions of their predecessors for decades to come.

Hidden victims

But it is too simplistic to consider the way these problems affect different groups in society by age alone. For a start, women are less likely to have a pension at all. If they do have one, it is likely to deliver a smaller retirement income than that available to many men, because women are likely to have been paid less than men for the work they did, are more likely to have worked part-time and/or in insecure jobs; and more likely to have had career gaps. Other groups in society that are less likely to have saved adequately for retirement include people from ethnic minorities.

People from all ethnic backgrounds and either gender may also be part of another large group who are unlikely to be saving enough for their retirement: gig economy workers who are 'falsely' self-employed, in that they tend to work for the same employer all the time. Along with other self-employed people, they have not been helped until now by the introduction of auto-enrolment.

This may start to change with the proposed removal of the earnings threshold for auto-enrolment eligibility; and following the recent Supreme Court ruling on the Pimlico Plumbers case, which could mean more people working in the gig economy are classified as 'workers' under EU law, enabling them to access employment rights including the right to join an auto-enrolment scheme.

Young people are more likely to be low earners and are likely to spend some time working in the gig economy, so any changes that help these workers will help them. But they may also help people in the generation between them and the babyboomers.

"Generation X is at risk of being the forgotten generation," says Just Group communications director Steve Lowe. "They may have reached halfway through their working lives without putting much aside for pensions, and have less time left to catch up. With reform of the care system still up in the air and solutions a long way off, they are likely to have to fall back on the value of their home for care if they have not already used it to supplement their retirement income." And that assumes that they own a property to remortgage or sell in the first place.

But it is also important to remember that not all babyboomers are rich. Research from the Centre for Ageing Better and the Resolution Foundation suggests many people aged 55 and over are also finding it very difficult to save much money as they approach retirement, in part because many are still paying off mortgages. Meanwhile, more than 1.9 million pensioners are thought to be living in poverty, according to 2017 research by the Joseph Rowntree Foundation. They may already be struggling to work out how to fund the care they will need at the end of their lives.

It should be obvious that there is little to gain by blaming one generation or another for financial problems that people of all ages face. Instead, government policy must aim to help everyone who is disadvantaged by the current system.

In the longer term, auto-enrolment will help millions, particularly younger people, although of course minimum contributions will need to increase, even after planned rises have taken effect. Many observers believe some kind of auto-escalation may be necessary. A recent report from the Pensions and Lifetime Savings Association (PLSA) suggests that minimum auto-enrolment contributions should rise from 8 per cent to 12 per cent between 2025 and 2030, with at least half of this to come from employers. It also advocates further research into use of opt-down or sidecar mechanisms to help lower earners and to enable flexibility that might help workers change the way they use their pension pot as their circumstances change.

Many younger people will also benefit from the changes that have already been made to the state pension, including the introduction of the Triple Lock. Altmann highlights specific groups that will benefit – at least in comparison to very poor provision in the past – including women and the self-employed.

But she also points out that all younger people will also miss out on the opportunity to bolster the state pension through use of the State Earnings-Related Pension Scheme (SERPS) from which some older workers will benefit to a significant degree. Younger people will also have to work into at least their late 60s before they can access a state pension.

The Centre for Ageing Better would like to see further changes to the state pension to support those – often women – who end up without a long, uninterrupted full-time employment history, with further reductions to the contribution years needed for a full state pension for some groups. Centre for Ageing Better director of evidence Claire Turner highlights the need to support those who reduce their hours or stop work to become carers.

Radical change

Other policy ideas could address interconnected issues, including funding of the NHS and social care; and changes in the way residential property and inherited wealth are taxed. The Intergenerational Commission (convened by the Resolution Foundation) has suggested that a £2.3 billion NHS levy should be paid via National Insurance contributions on earnings of individuals over state pension age. It has also suggested that National Insurance could be payable on income from occupational pensions. Webb thinks the former measure may become "inevitable" in time, but that taxing pension income is likely to be seen as a step too far for the foreseeable future. But Taylor is one of many anticipating a future government finally changing the current rules on higher rate tax relief on pensions, the removal of which would effectively transfer wealth from the old to the young, as the former are more likely to use the relief.

Another idea put forward by the Intergenerational Commission is the introduction of a Citizen's Inheritance: a sum of money made available to every young person from the age of 25 onwards and held in an interest-bearing account until used for any of four permitted purposes: education and training, funding a new business, contributing to a deposit for home rental or purchase; or giving an early boost to pension saving. The policy would be funded by replacing the current inheritance tax system with a new lifetime receipts tax. Other organisations have looked at using a new Sovereign Wealth Fund to provide something similar.

In June 2018 a report by the Parliamentary Housing, Communities and Local Government Committee and the Health and Social Care Committee suggested a levy should be paid by over 40s, retirees and employers to help fund social care. It would be subject to a minimum earnings threshold for individuals, but could also be levied on unearned income, including pensions and investments.

The Intergenerational Commission suggests a public funding increase of more than £2 billion to help fund social care, to be raised using a replacement for Council Tax and increased property-based private contributions to care costs, limited by an asset floor and cost cap.

There may be value in at least some of these ideas, but Cass Business School professor of finance and director of the Pensions Institute David Blake remains sceptical about the chances of many coming to fruition. He points to the damage done to the Conservative Party's 2017 election campaign when it dared to discuss how to fund social care.

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Ultimately, Blake suggests, only if every generation learns to take a longer term view and starts to save more money can the causes of intergenerational conflict be removed. Without adequate public understanding of these issues, he suggests, younger generations will always be at a disadvantage, because "our democratic system does not give votes to future generations".

Even so, we must try not to see these problems as being primarily due to intergenerational unfairness, says International Longevity Centre (ILC) assistant economist Dean Hochlaf. "Yes, the environment has got harder for younger people, but I don't think the answer is to start taking away any rights of older people," he says. "We need to ask how we can create an economic environment that can generate gains that can be distributed fairly across society in general."

But Blake fears that the changes that will be needed to resolve intergenerational conflict will only be made when a government is forced to act. "This is only going to happen as a result of a major crisis of poverty, with intergenerational conflict," he warns.

So, is he right? Will we, as a society, take the right decisions for the longer term, to benefit every generation – or are millennials and their own children and grandchildren doomed to repeat the mistakes of the past?

Written by David Adams, a freelance journalist