Pensions Policy Institute

PPI

What impact has the COVID-19 pandemic had on underpensioned groups?

Executive Summary

The Pensions Policy Institute (PPI)

We have been at the forefront of shaping evidence-based pensions policy for 20 years.

The PPI, established in 2001, is a not-for-profit educational research organisation, with no shareholders to satisfy – so our efforts are focussed on quality output rather than profit margins. **We are devoted to improving retirement outcomes**. We do this by being part of the policy debate and driving industry conversations through facts and evidence.

The retirement, pensions and later life landscapes are undergoing fast-paced changes brought about by legislation, technology, and the economy. Robust, independent analysis has never been more important to shape future policy decisions. The PPI gives you the power to influence the cutting-edge of policy making. Each research report combines experience with independence to deliver a robust and informative output, ultimately improving the retirement outcome for millions of savers.

Our **independence** sets us apart – we do not lobby for any particular policy, cause or political party. We focus on the facts and evidence. Our work facilitates informed decision making by showing the likely outcomes of current policy and illuminating the trade-offs implicit in any new policy initiative.

Our Vision:

Better informed policies and decisions that improve later life outcomes

We believe that better information and understanding will help lead to a better policy framework and a better provision of retirement income for all.

Our Mission:

To promote informed, evidence-based policies and decisions for financial provision in later life through independent research and analysis

We aim to be the authoritative voice on policy on pensions and the financial and economic provision in later life.

By supporting the PPI, you are aligning yourself with our vision to **drive better-informed policies and decisions that improve later life outcomes** and strengthening your commitment to better outcomes for all.

As we look forward now to the next 20 years, we will continue to be the trusted source of information, analysis, and impartial feedback to those with an interest in later life issues. The scale and scope of policy change creates even more need for objective and evidence-based analysis. There is still much to do, and we look forward to meeting the challenge head on.

For further information on supporting the PPI please visit our website: www.pensionspolicyinstitute.org.uk or contact Danielle Baker, Head of Membership & External Engagement, at danielle@pensionspolicyinstitute.org.uk

The future is ever changing, but the PPI remains a constant "Voice of Reason" in the ongoing debate on the future of retirement in the UK.

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EST. 2001

This report has been authored by:

Lauren Wilkinson, Senior Policy Researcher Pensions Policy Institute

Lauren Wilkinson joined the PPI in September 2016 as a Policy Researcher. During her time at the PPI Lauren has produced research on a range of topics, including Defined Benefit, consumer engagement, pension freedoms and Collective Defined Contribution.

Lauren was promoted to Senior Policy Researcher in January 2019.

Prior to joining the PPI, Lauren achieved an undergraduate Masters in Politics and Philosophy at the University of Glasgow, followed by a Masters in Public Administration and Public Policy at the University of York.

John Adams, Senior Policy Analyst, Pensions Policy Institute

John has been the PPI's Senior Policy Analyst since 2008. In his time at the PPI John has worked in a lead role in the modelling of a wide range of pension policy project number of PPI modelling projects including a number of projects looking at public sector pensions and pension related tax-relief.

At the PPI, John is responsible for the PPI's Pension Facts and has authored briefing notes and reports on subjects such as how housing wealth can support retirement, tax policy on pension schemes, harnessing pension savings for debt alleviation, public sector pension reforms.

John joined the PPI in 2008 from Hewitt Associates. At Hewitt he worked primarily on modelling of standard and non-standard Defined Benefit pension scheme calculations for the consultants to present to the clients.

Prior to joining Hewitt John worked for the Government Actuary's Department for 8 years in the Occupational Pensions directorate, during which time he calculated public sector pension scheme valuations, bulk transfer values, and designed models for the use of other Government departments.

John has a BSc in Actuarial Mathematics and Statistics from Heriot Watt and a Post Graduate Diploma in Actuarial Management from Cass Business School.

The Pensions Policy Institute (PPI)

The PPI is an educational, independent research organisation with a charitable objective to inform the policy debate on pensions and retirement income provision. The PPI's aim is to improve information and understanding about pensions and retirement provision through research and analysis, discussion and publication. It does not lobby for any particular issue or reform solution but works to make the pensions and retirement policy debate better informed.

Pensions affect everyone. But too few people understand them and what is needed for the provision of an adequate retirement income. The PPI wants to change that. We believe that better information and understanding will lead to a better policy framework and a better provision of retirement income for all. The PPI aims to be an authoritative voice on policy on pensions and the provision of retirement income in the UK.

The PPI has specific objectives to:

- Provide relevant and accessible information on the extent and nature of retirement provision
- Contribute fact-based analysis and commentary to the policy-making process
- Extend and encourage research and debate on policy on pensions and retirement provision
- Be a helpful sounding board for providers, policy makers and opinion formers
- Inform the public debate on policy on pensions and retirement provision.

We believe that the PPI is unique in the study of pensions and retirement provision, as it is:

- Independent, with no political bias or vested interest
- Led by experts focused on pensions and retirement provision
- Considering the whole pension framework: state, private, and the interaction between them
- Pursuing both academically rigorous analysis and practical policy commentary
- Taking a long-term perspective on policy outcomes on pensions and retirement income
- Encouraging dialogue and debate with multiple constituencies

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A Research Report by Lauren Wilkinson and John Adams

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Executive Summary

This report explores the impact of the COVID-19 pandemic on underpensioned groups in two parts: the short-term impacts that have been experienced by underpensioned groups over 2020-21, and the longer-term impacts which may affect their retirement outcomes over years to come.

Certain groups are at greater risk of experiencing poorer retirement outcomes:

- Women, especially single mothers and divorced women
- People from BAME backgrounds
- Disabled people
- Carers
- Multiple job holders
- The self-employed

The crisis has provided a unique opportunity to observe how economic crises affect members of underpensioned groups. Developing a deeper understanding of the way in which changes in the labour market can impact future retirement outcomes of underpensioned groups can help to ensure that policies are designed to support them more effectively during the recovery from the pandemic-related economic crisis, as well as future crises and changes in the labour market.

Policies aimed at improving the retirement outcomes of underpensioned groups will be most effective if they take account of the way in which they have been disproportionately affected by negative labour market effects during the pandemic

Underpensioned groups are disproportionately affected by negative changes in the labour market precipitated by economic crises. During the last year and a half, members of underpensioned groups have been more likely to experience unemployment, furlough and reduced income as a result.

Palliative policies which helped to minimise the negative impact for many in underpensioned groups during the peak of the pandemic are no longer in place. For example, the Government Job Retention Scheme, which helped to protect job security and pension contributions for those who were furloughed, came to an end in September 2021. However, the long-term labour market effects of the crisis continue to disproportionately disadvantage underpensioned groups, which may mean that the gap between average retirement outcomes and those of underpensioned groups will increase for those affected.

In order to avoid greater gaps in retirement outcomes in future, Government benefits policies will be most effective if they take into account the enhanced difficulties underpensioned groups may face in relation to finding secure employment during the economic recovery, and the corresponding increased level of reliance they may have on the State Pension and benefits in retirement. Focus will need to be on ensuring that working-age benefits provide sufficient income and support to protect underpensioned groups from an erosion of financial resilience during periods of unemployment or less secure employment, for example through difficulties keeping up with bills, run down of savings and greater likelihood of increased debt.

Policies regarding uprating of the State Pension should take into account the increased level of reliance underpensioned groups, who are already more reliant than average on the State Pension and benefits for income in retirement, are likely to have, and the disproportionate impact changes to uprating mechanisms may therefore have on underpensioned groups.

Consideration of the adequacy of current contribution rates and the coverage of automatic enrolment are an important component of efforts to mitigate the negative impact of labour market gaps on the retirement outcomes of underpensioned groups

With underpensioned groups being disproportionately impacted by disruption to employment patterns and pension contributions, it is even more vital to their future retirement outcomes to ensure that they are saving enough while in employment to help to mitigate these gaps. While automatic enrolment has increased pension participation among underpensioned groups, they are disproportionately likely to be found ineligible due to differences in labour market participation. Implementing the recommendations made by the 2017 Automatic Enrolment review will increase eligibility among underpensioned groups by:

- Lowering the age threshold for automatic enrolment from 22 to 18 years old, and
- Removing the lower limit of the 'qualifying earnings band' so that contributions are paid from the first pound earned.

Removing the lower limit for qualifying earnings will be especially beneficial for members of underpensioned groups on low incomes, who will receive a greater proportional boost to pension savings as a result. These changes are currently expected in the mid-2020s. However, introducing them as soon as possible will enable the pension savings of underpensioned groups that may have been negatively affected by the pandemic to recover more quickly.

Among those who have been automatically enrolled, current minimum contribution levels are insufficient for most people to replicate working-life living standards in retirement. For members of underpensioned groups on low incomes, increasing employee contribution rates is likely to be unrealistic and mandating increases in the minimum could lead to increased opt out rates. However, reviewing the minimum contribution required by employers, without the need for increased employee contributions, could have a substantial positive impact on the retirement outcomes of underpensioned groups.

Greater access to flexibility in employment could help to close the gender pensions gap, as well as supporting carers and people with disabilities to achieve better retirement outcomes, by increasing labour market engagement

The Underpensioned Index (2020) identified that for some underpensioned groups, especially mothers, carers and disabled people, labour supply issues may make policies aimed at increasing employment rates more challenging in practice. Policies aimed at increasing accessibility in the workplace and providing more flexible working arrangements could help to alleviate lower levels of employment among these groups, increasing labour market engagement and the likelihood of achieving more positive retirement outcomes as a result. Gender differences in childcare and the actions that policy and employers can take to make this more equal, while supporting those with caring responsibilities, could help to decrease existing gaps in retirement outcomes. However, it will be important to monitor the longer-term impact of greater flexibility on career progression, income and pension contributions. A better understanding of how labour market changes impact

retirement outcomes of underpensioned groups over the long-term will enable policies to be designed that most effectively support these groups to achieve better retirement outcomes.

Time spent out of the labour market disrupts the consistency of pension contributions and is therefore likely to lead to poorer retirement outcomes for those in underpensioned groups who were disproportionately affected by negative labour market effects during the pandemic

Because being underpensioned is closely correlated with inequalities during working life, the disproportionately negative impact that the pandemic has had on these groups' employment, income and financial resilience is likely to further increase their risk of experiencing poorer retirement outcomes. Unemployment rates grew quickly in 2020, with some underpensioned groups disproportionately affected, especially people from BAME backgrounds, although the furlough scheme protected against more severe impacts on the labour market. Unemployment reached a peak of 5.2% in Q4 2020, from a low of 3.8% in Q4 2019.[1] Rates of economic inactivity also increased during the pandemic, from 20.5% in Q4 2019 to a peak of 21.4% in Q1 2021.[2] COVID-19 also led to many people being furloughed, going part time, or having to change jobs. While furlough has an impact on immediate income, the Government Job Retention Scheme has helped to protect against further increases in unemployment, protecting job security for the longer-term. People in underpensioned groups were more likely than average to experience labour market inequalities and be affected by furlough and redundancies during the pandemic, as they are more likely to work in the industries most impacted by the public health restrictions such as retail, hospitality and tourism, or are in low-paid, part-time or irregular employment.

It remains to be seen what the impact of the furlough scheme coming to an end (in September 2021), and potential subsequent job losses, will be on employment rates and incomes, and whether longer-term impacts on economic growth could have a negative effect on employment rates and wage growth in years to come. Members of underpensioned groups are especially concerned about the impact this may have on their career progression moving forward. Half (50%) of employed BAME women and 43% of employed white women say they are worried about their job or promotion prospects due to the pandemic, compared with 35% of employed white men.[3] Gender differences in divisions of labour when working from home have the potential to hinder progress to close the gender pay gap if performance is impacted.[4] Any policy initiatives aimed at encouraging greater employment flexibility on a longer-term basis would need to consider these challenges.

On average, underpensioned groups have lower levels of financial resilience, and were less able to keep up with bills, more likely to run down savings and more likely to fall into debt during the pandemic, which may impact their ability to save for later life over the longer-term

There is evidence that low-income households were less able to save and more likely to run down savings than households with higher income. Between February 2020 and June 2021, 32% of people in the lowest income quintile experienced a fall in savings and 12% had a rise. 9% of people in the highest income quintile experienced a fall, while 47% had an increase in savings.[5] Women and people from BAME backgrounds are likely to have lower levels of financial resilience compared to other groups, and this manifested in greater difficulty keeping up with bills and increasing debt levels during the pandemic. Members of underpensioned groups are likely to need greater support to recover from the pandemic, in terms of catching up on missed bill payments, reducing debt levels and increasing savings back to pre-pandemic levels.

1 ONS (2021a)
2 ONS (2021b)
3 Fawcett Society (2020a)
4 IFS (2020)
5 Handscomb, Henehan & Try (2021)

The Government Job Retention Scheme helped to minimise the impact of the pandemic on many, but some people made individual decisions to cease or reduce contributions, while those who became unemployed will have experienced the greatest disruption to contributions

While employees were furloughed, employers were still required to pay pension contributions at least at minimum automatic enrolment contribution levels (3% for employer). The requirement to continue paying pension contributions for furloughed staff has minimised the impact of the pandemic on pension contributions and eventual retirement outcomes for these individuals. However, while on furlough and receiving 80% of usual pay, pension contributions were based on this reduced level of income so experienced a 20% reduction compared to pre-pandemic contributions. Those who became unemployed during the pandemic, rather than being furloughed, did not have the benefit of protected pension contributions and so are more likely to experience longer-term damage to their pension pot value as a result. The self-employed, who were covered by a different income support scheme (Self-Employment Income Support Scheme), and a group among whom pension contributions were already low on average, will also have experienced disruption to contributions where income has been impacted by the pandemic.

Short-term decisions about accessing pension savings during the pandemic are likely to impact sustainability of pension savings over the longer term

Short-term decisions made about whether or not to access pension savings during the peak of the pandemic can have a substantial impact on the sustainability of pension savings and the rate of income that can be drawn over the longer term. Those who were unable to postpone accessing their savings when the market was at its lowest are likely to have suffered more material losses, having locked in negative returns by making withdrawals, than those who were able to leave their savings more time to recover.

The prevailing view was that savers could benefit from delaying access to their pension pot for as long as possible in order to give it time to recover as much as possible, as well as making additional contributions to help restore pension pot values more quickly, if possible. The number of Defined Contribution (DC) pots accessed declined significantly in 2020, suggesting that savers were, understandably, cautious about accessing savings during a period of volatility. However, in practice these options would be more challenging for some savers than others. Those on lower incomes, as well as those who were furloughed (both of which were overrepresented among underpensioned groups), will find it harder to make additional contributions, and may also have found it more difficult to postpone retirement in order to delay accessing their savings - as those on low incomes tend to have lower levels of non-pension wealth upon which they could draw in order to bridge the gap. They are also more likely to experience disability or long-term illness at younger ages that can make working longer harder.[6]

While economic recovery appears to be moving in the right direction, the end of furlough could lead to increases in unemployment and reductions in income moving forward

While the Government Job Retention Scheme has helped to support job security during the peak of the pandemic, it remains to be seen how employment rates may change now that the scheme has come to an end. While the scheme ended in September 2021, data on how this has impacted unemployment rates remains limited. 1.14 million employees remained fully furloughed by the end of the scheme. However, given that there was a requirement for increasing employer contributions towards the end of the scheme, it is unlikely that all of these will be made unemployed, else employers would likely have made these workers redundant prior to the increases in required employer contributions to salary. There are, however, likely to be some further redundancies, perhaps particularly in sectors that are still affected by Government restrictions, such as international travel. While employment rates and incomes have largely returned to pre-pandemic levels, potential longer-term impacts on economic growth could have a negative effect on employment rates and wage growth in years to come.

6 PPI (2019) *Living through later life*

Changes to the way that the State Pension is uprated may have a disproportionate impact on members of underpensioned groups who are likely to be more heavily dependent on State Pension income in retirement

The Triple Lock, the mechanism by which the State Pension is uprated each year, has been suspended for 2022-23. In ordinary circumstances, under the Triple Lock, State Pension income is uprated by the higher of inflation (measured by the Consumer Prices Index (CPI)), earnings increases or 2.5%. For 2022-23, the State Pension will be uprated by 3.1% (in line with CPI). This is a temporary suspension in response to wage inflation resulting from the end of the furlough scheme. However, there are concerns that this could lead to more permanent changes in future, as there have been debates about the sustainability of the Triple Lock for some time. Any permanent changes to the way that State Pension is uprated would have a disproportionate impact on members of underpensioned groups, who are likely to be more heavily dependent on the State Pension for income in retirement. Longer-term changes to the Triple Lock would need to take account of equality issues which may arise as a result.

The longer-term effects of COVID-19 on health and life expectancy are likely to impact the sustainability of pensions, as well as the length and quality of retirement for some people

It is currently expected that, in addition to the loss of life in the short term, the pandemic could have a negative effect on health and life expectancy in the longer term. COVID-19 is considered likely to become endemic, resulting in further loss of life in future winters. The long-term toll on the NHS of the pandemic is shown in the non-COVID-19 patient backlog that has risen to more than four million. The high projected level of unemployment is also expected to feed through in higher demands on health services.[7] While there is a positive effect on future mortality rates following the very significant breakthroughs in vaccine development as a result of COVID-19, this could be small in comparison to other issues faced by the UK health system. As a result, some actuaries are projecting a seven-month reduction in the life expectancy of a typical 65-year-old. People from BAME groups, who are disproportionately affected by the virus, may face higher than average levels of impact on life expectancy.[8]

7 McIvor (2020)

8 FCA (2021a)