Everything you always wanted to know about the triple lock but were afraid to ask…

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So what is the Triple Lock?

The triple lock is the name used to describe how the basic State Pension (bSP) and new State Pension (nSP), for individuals reaching State Pension age after 6 April 2016) is increased each year. The triple part comes from the three different components – price inflation, earnings growth or 2.5% - that are compared, and the highest of the three (as measured the previous September) is used to increase the bSP and nSP each April. It was introduced in 2010 as part of the coalition agreement.

Why is it such a hot topic?

The lock part of the triple lock is the fact that it means that bSP and nSP increase by at least 2.5% each year, irrespective of how fast prices rise or earnings grow. This means that over time the level of the bSP and nSP have risen faster than inflation and earnings, increasing the incomes of pensioners relative to the incomes of the rest of the population.

So State Pensions are too high?

Not necessarily. In both historical and international terms, the level of the nSP is low at £155.65, 24.2% of National Average Earnings.[1] If the triple lock stayed in place it would take until 2038 to reach 26% of National Average Earnings, the level of the bSP in 1979 (the last peak level).[2] It is also low compared to the OECD average level of 42.5% of National Average Earnings.[3]

However, it is important to remember that actually very few of today's pensioners receive the nSP – only those who have reached SPa since April 2016. Over 95% of current pensioners instead receive a combination of bSP and additional pension (State Second Pension (S2P) and/or SERPS) (Chart 1).[4] Of this only the bSP is triple locked, with S2P/ SERPS increased in line with prices. The average amounts of both nSP and bSP are lower than the full amounts.

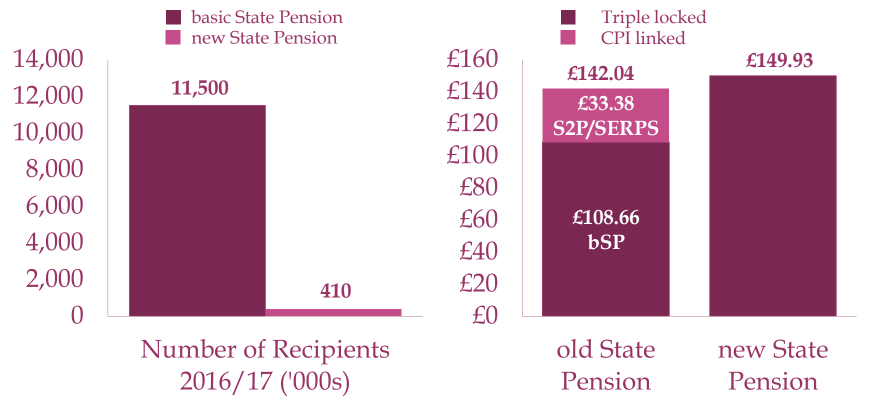
As a result of applying the triple lock since 2011/12, bSP is currently £122.30 a week rather than £114.50 a week (which would have been the level as a result of following earnings indexation). This represents an additional £405 pa, an increase of 6.8% above the earnings index (Chart 2).[2]

Then what is the problem?

It is not the absolute level that is causing concern, but how fast State Pensions have grown relative to other incomes. This suggests that pensioners are seeing incomes grow faster than the rest of the population. It has also meant the spending on State Pensions has increased while spending in other areas of welfare have not.

Chart 1. Younger pensioners under nSP receive more benefit from the triple lock than older pensioners who are in receipt of the basic State Pension

Number of recipients, and average weekly payment, of the old State Pension compared with the new State Pension in 2016/17 ('000s of people: £ a week)



PPI Briefing Notes clarify topical issues in pensions policy.

Have pensioner incomes grown relative to the rest of the population?

As a group, yes. Analysis from the Institute for Fiscal Studies (IFS) calculates that the average income for people aged 60 and older grew by 11% between 2007/8 and 2014/15, while the average income for people aged 31 – 59 saw virtually no growth at all, and for those aged 22 – 30 had fallen by 7%.[5]

So all pensioners are getting richer compared to younger generations?

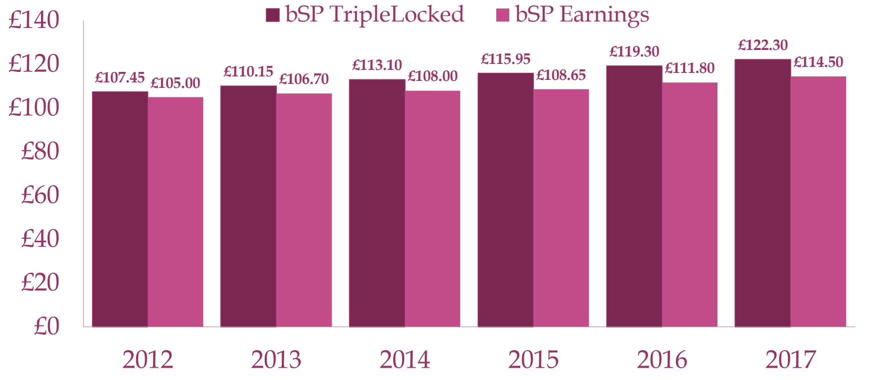
No. Most of the growth in the average incomes of those over 60 is caused by changes in who is in the group. Among the fastest growing components of income for the over 60s are earnings and private pension income. These are growing because people who turned 60 and so join the pensioner group after 2007/8 are more likely to still be working and to have higher pensions than those already in the group, and those who have died since 2007/8. Although there has been strong growth in pensioner benefits, for this group only the bSP is triple locked (S2P increases in line with prices). In fact, if you look at the change in the average income between 2007/8 and 2014/15 only for those who are aged 60 or over in 2007/8, the increase is only 5% - less than half of the headline IFS figure, but still higher than the rest of the population.[6]

Are they all better off but just not quite as much as we thought?

Again, no. Using different data it is possible to look at how individual incomes (rather than the average of the group) changes over time. Using this data we find that of those aged 60 or older in 2008/9, half had lower incomes by 2014/15.[7] Many of these will be those who have stopped working, but private pensions already in payment and income from investments and savings are also likely to have at best kept pace with inflation, and in many cases fallen.

Chart 2. The triple lock has increased basic State Pension more than if it had been in line with earnings growth

Historical rates of full basic State Pension under the triple lock, compared to the value if the uprating had been in line with earnings growth (£ a week)



But I thought pensioner poverty was falling?

It is. In 2003, 25% of pensioners were defined as being in relative poverty. By 2014/15 this had fallen to 14%. For the population as a whole this was 21%, so it is true that, on this measure, pensioners are now less likely to be in poverty than the rest of the population.[8]

And aren't incomes of pensioners higher than the rest of the population?

According to the Resolution Foundation, typical pensioner households are now £20 a week better off than typical working age households, while back in 2001 typical pensioner incomes were £70 a week lower than working age incomes.[9]

Isn't this a sign of generous benefits being made even more generous by the triple lock?

No. In both cases, as we saw in the individual analysis, the main driver of falls in poverty and increases in income has been earnings and employment income – so incomes are increased by people turning 60 having higher incomes than the previous generations. As many of these are still working, and below an increasing State Pension age, they look very different from what many might think of as a pensioner.

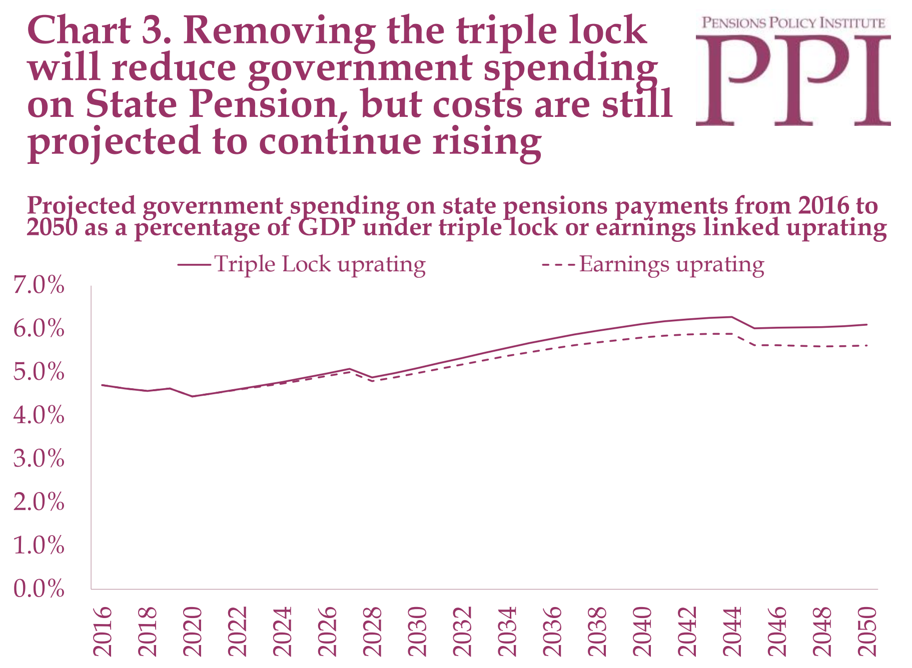
Are pensioners still better off than non-pensioners?

It is also the case that both incomes and poverty measurements can be distorted for pensioners by the presence of disability benefits. In 2014, 43% of pensioners had a disability, compared to 16% of working age adults. Disability benefits are designed to meet the additional costs that arise from being disabled, although these extra costs are not taken into account in the income or poverty calculations. Removing disability benefits from poverty calculations (so taking account of the higher need the benefits are meant to cover) would have increased the poverty rate of pensioners by 16 percentage points in the late 1990s, compared to an increase of 3 percentage points for the population as a whole.[10]

Isn't there also a generational issue? Pensioners benefit from the triple lock which is paid for by the younger generations who don't benefit?

Not exactly. It is certainly true that the current additional cost of the State Pension due to the triple lock is a transfer at this point in time from the younger generation paying tax and National Insurance to the older generation receiving the State Pension. It is hard to tell exactly how much this has cost, as the amount of pension received also impacts on other benefits (such as Pension Credit and Housing Benefit) that pensioners receive, and the nSP (introduced in April 2016) might have been introduced at a higher level if it was expected to have smaller increases in future.

Chart 3. Removing the triple lock will reduce government spending on State Pension, but costs are still projected to continue rising



The State Pension system currently costs about 6.5% of gross domestic product (GDP) and this proportion is set to rise as the numbers of people over State Pension age rises and entitlements increase (Chart 3).[11] Its future cost will also depend to a considerable degree on how it is uprated each year. Legislation requires the nSP to be uprated by at least the annual increase in average earnings, but through the last Parliament the triple lock was used. If the triple lock is applied indefinitely, the reformed pension system is expected to cost a similar proportion of GDP as the previous system until the 2040s but its cost will then rise more slowly. If earnings uprating is applied, the nSP will cost less than the bSP based system from about 2030, and by 2060 the saving would be equivalent to about 1% of GDP.

But younger generations also benefit from the triple lock, as it means they will get a higher State Pension when they retire as a result. If the value of their State Pension is reduced by being increased by less than the triple lock, then the younger generations will have to have a lower retirement income, work longer, or save more. As an illustration, a median earning 22 year old today who stays automatically enrolled for the rest of his career would have to save an extra 4% of band earnings to make up for the loss of the triple lock. The sooner the triple lock is ended, the bigger the gap that younger generations will need to save themselves. The triple lock debate is as much about the relative role of the state and the individual in providing for retirement as it is about current spending.

Does the "double lock" help?

In their manifesto, the Conservative Party propose replacing the "triple lock" with a "double lock" from 2020.[12] The double lock would increase the bSP and nSP by the higher of prices and earnings. So in this case, pension levels would still grow faster than earnings, just more slowly than under the triple lock. According to the IFS, the double lock would be only slightly less expensive (0.2% GDP) than the triple lock.[13]

So what is wrong with the double/ triple lock?

It is clear that both the double or triple lock cannot go on forever, as pensions would eventually be higher than average earnings. But what is missing from the current debate is any consideration of what the appropriate level for the State Pension is, what should it be linked to, and how much should it cost? At the moment the triple lock is a short term fix designed to increase the generosity of the State Pension gradually, but with no clear objective or end point. When it is bought to the end it needs to be replaced with a coherent, comprehensive policy that clarifies the role of the State Pension in retirement income.

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[1] PPI Pensions Primer (2016)
[2] Nomis (2016), DWP ~Impact of nSP longer term research (2016)
[3] OECD, Pensions at a Glance (2015)
[4] PPI calculations
[5] IFS (2015) Average income back to around pre-recession level after historically slow recovery in living standards
[6] IFS (2010) The wealth and savings of UK families
[7] JRF (2017) Households below a Minimum Income Standard 2008/09 – 2014/15
[8] UK Parliament (2017) Poverty in the UK: Statistics
[9] Resolution Foundation (2017) Recent retirees drive pensioner incomes above those of working families
[10] Family Resources Survey 2014/15 (2016)
[11] PPI Modelling
[12] Conservative Manifesto 2017
[13] IFS Moving from a triple to a double lock (2017)

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