PRESS RELEASE

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PENSIONS POLICY INSTITUTE
PPI

"Basing the State Pension rise on average earnings over two years would mean that pensioner standards of living increases could more closely resemble those in work" says Pensions Policy Institute

Annual increases to the State Pension are triple locked, meaning they rise in line with the higher of increase in earnings, CPI or 2.5%. The triple lock is not legislated for (though increases in line with earnings each year are legislated for), though the current Conservative Government promised to maintain the triple lock throughout the next parliament in their election manifesto. This year, as people returned to work full-time and came off furlough, earnings inflation increased by 8.8% in the year to June 2021 which actually reflects work patterns returning to normal after the impact of the pandemic. This includes income increases for the nearly nine million people who were furloughed at the peak of the scheme returning to work at full pay rather than the furlough scheme which only paid 80% of incomes.[1] This 8.8% rise therefore, does not equate to an increase in living standards of this amount. In order to avoid paying a very high increase in State Pension this year, the Government has announced that they will suspend the earning-link for one year and increase State Pension by the rise in CPI, expected to be around 3%. This is likely to require parliamentary approval to alter the legislation requiring an earnings link for one year.

Daniela Silcock, Head of Policy Research at the PPI said "The artificially high rise in earnings has put the Government in a tricky position. Increasing the State Pension by 8.8% will not reflect real rises in hourly wages, which is the intention of the indexation policy. Raising the pension amount by CPI increases rather than earnings next year will result in the Government saving £4.9bn of pension payments in 2022, rising to £5.9bn in 2025."

"Suspending the triple lock represents a broken manifesto promise and raising the State Pension by less than earnings requires a change to legislation. The decision to raise the State Pension by CPI for 2021 alone, and return to the triple lock in 2022 is better news for pensioners than if the Government has decided to permanently suspend the triple lock, or rescind legislation requiring the State Pension to rise with earnings. However, the decision risks damaging public trust in Government commitments, especially without analysis on how the change might impact the value of the State Pension in relation to actual earnings over the period in question."

"Increasing the State Pension by CPI means that overall, State Pensions will rise by less than the real increase in earnings over the past two years. An alternative approach would have been to consider the rise in earnings over two years to give a more realistic estimation of real wage increases without the artificial impact of the pandemic impact in the year on year earnings statistics. This would need a pension increase of 5.3% in 2022 to match the increase in earnings since the setting of the State Pension level in 2020. Increasing the State Pension by this amount would save £3.1bn in 2022, would

[1] https://commonslibrary.parliament.uk/research-briefings/cbp-9152/

mean that pensioner standards of living increases would more closely resemble those in work, and would not break the earnings-link in the same way, though a new definition of earnings may need to be approved for one year."

"In the long term, the triple lock will raise the State Pension from a relatively low value in comparison to the rest of Europe (24% of average earnings for a full new State Pension), keeping some pensioners out of poverty and ensuring that today's younger people have a higher State Pension when they retire. It is therefore positive news for both today's pensioners and workers that the Government is not using the current increase in earnings as justification to suspend the triple lock or the earnings-link beyond one year."

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Notes for editors

1. **We are an independent educational research charity: The Pensions Policy Institute (PPI)** does not lobby for any particular solution and we are not a think-tank taking politically influenced views. The PPI is an educational research charity, which provides non-political, independent comment and analysis on policy on pensions and retirement income provision in the UK. Its aim is to improve the information and understanding about pensions policy and retirement income provision through research and analysis, discussion and publication. News and other information about The PPI is available at www.pensionspolicyinstitute.org.uk and via Twitter: @PPI_Research.

Further notes on the triple lock

What is the triple lock?

Annual increases to the State Pension (basic State pension and new State pension) are triple locked, meaning they rise in line with the higher of increase in earnings, CPI or 2.5%. The triple lock has been in place since 2011 and it means that the value of State Pensions will rise in relation to earnings over time.

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What does legislation require the Government to do?

The triple lock is not legislated for, though the current Conservative Government promised to maintain the triple lock throughout the next parliament in their election manifesto. The link to earnings is legislated for and requires amendment to suspend.

Why is it changing?

The triple lock goes up each year by a few percent (2.5% minimum) in order to maintain value and increase in value over time relative to earnings. However, the earnings increase in 2018 has been significant and represents a potentially significant increase in the State Pension, which is considered unaffordable in the current climate.

The reason for the increase in earnings is that job losses, furloughs and the closure (both temporary and permanent) of businesses significantly reduced earnings inflation. In 2020, earnings inflation was at around –1%, which is around 4% less than at the end of 2019, when it had increased by around 3% from the previous year.

This year, as people returned to work full-time and the furlough scheme ended, earnings inflation increased by around 8.8% driven by an increase in hours worked rather than hourly wage increases. This 8.8% rise therefore, does not reflect the intention of the policy.

An 8% State Pension rise could cost the Government an extra £4.9bn in 2022, rising to an annual extra cost of £5.8bn by 2025 and increase pensioner State Pension income:

- Basic State Pension would increase from £7,155pa to £7,785pa
- New State Pension would increase from £9,339pa to £10,161pa

What is the change?

In order to avoid paying a very high increase in State Pensions this year, the Government has announced that they will suspend the earnings-link for one year and increase State Pension by the rise in CPI, expected to be around 3%. This is likely to require parliamentary approval to alter the legislation requiring an earnings link for one year. This lower increase amounts to a permanent reduction which will reduce payments in all subsequent years as well as they will be based on a lower starting amount.

This change could save the Government £4.9bn in 2022 and increase pensioner State Pension income:

- Basic State Pension would increase from £7,155pa to £7,370pa (£415pa less than under an 8.8% rise)
- New State Pension would increase from £9,339pa to £9,619pa (£542pa less than under an 8.8% rise)

What were the other options the Government could have taken?

The Government could have averaged earnings over the last two years and used this figure, 5.3%, to uprate the State Pension, allowing for a slightly higher increase than under the current proposal.

This change could save the Government £3.1bn over an 8.8% increase and increase pensioner State Pension income:

- Basic State Pension would increase from £7,155pa to £7,519pa (£266pa less than under an 8.8% rise)
- New State Pension would increase from £9,339pa to £9,814pa (£347pa less than under an 8.8% rise)

For further reading please see:

- Briefing Note Number 123 - What does COVID-19 mean for the triple lock and State Pension inflation? https://www.pensionspolicyinstitute.org.uk/sponsor-research/research-reports/2020/briefing-note-number-123-what-does-covid-19-mean-for-the-triple-lock-and-state-pension-in%EF%AC%82ation/
- Briefing Note 96 - Everything you always wanted to know about the triple lock but were afraid to ask... https://www.pensionspolicyinstitute.org.uk/sponsor-research/research-reports/2017/briefing-note-96-everything-you-always-wanted-to-know-about-the-triple-lock-but-were-afraid-to-ask/
- How would removal of the State Pension triple lock affect adequacy? https://www.pensionspolicyinstitute.org.uk/sponsor-research/research-reports/2018/2018-03-21-how-would-removal-of-the-state-pension-triple-lock-affect-adequacy/