Austerity, Ageing and the Future of Public Spending on Older People

Monday November 26th, 2012
British Library
Pensioner incomes and fiscal austerity

Carl Emmerson

Presentation at Strategic Society Centre event on “Austerity, Ageing and the Future of Public Spending on Older People” at the British Library, 26 November 2012

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Pensioner incomes and fiscal austerity

• Pre-crisis trends

• Impact of considerable fiscal austerity in this parliament

• Reform options for continued austerity post March 2015 that would affect pensioners
Pensioner incomes and fiscal austerity

• Pre-crisis trends
  – pensioners relatively favoured by tax and benefit reforms from 1997 to 2010
Distributional impact of tax and benefit changes
April 1997 to April 2010

Source: Adam, Browne & Johnson (2012).
Pensioner incomes and fiscal austerity

• Pre-crisis trends
  – pensioners relatively favoured by tax and benefit reforms from 1997 to 2010
  – average pensioner income at highest level relative to average population-wide income since (at least 1961)
Median pensioner income as % of overall median

Source: Adam, Browne & Johnson (2012).
Pensioner incomes and fiscal austerity

• Pre-crisis trends
  – pensioners relatively favoured by tax and benefit reforms from 1997 to 2010
  – average pensioner income at highest level relative to average population-wide income since (at least 1961)
  – chances of being in income-poverty now lower for pensioner than for non-pensioner

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Relative poverty rate by age and time, broad income

Note: Broad income includes imputed rental income for owner occupiers. Source: Brewer and O'Dea (2012).
Pensioner incomes and fiscal austerity

• Pre-crisis trends
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• Impact of considerable fiscal austerity in this parliament
  – pensioners not immune from this
  – but certainly relatively protected from tax rises and benefit cuts
Distributional impact of tax and benefit changes January 2011 to April 2014

Note: Excludes Universal Credit and some measures affecting the very rich. Source: Adam, Browne & Johnson (2012).
Pensioner incomes and fiscal austerity

• Pre-crisis trends
  – pensioners relatively favoured by tax and benefit reforms from 1997 to 2010
  – average pensioner income at highest level relative to average population-wide income since (at least 1961)
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• Impact of considerable fiscal austerity in this parliament
  – pensioners not immune from this
  – but certainly relatively protected from tax rises and benefit cuts

• Reform options for continued austerity post March 2015 that would affect pensioners
Some reform options

Many possible reforms that would affect pensioners – here are three that would rationalise the tax and benefit system:

1. Impose NICs on earned income of pensioners
   – would raise £0.8 billion a year
   – but would weaken work incentives for a relatively responsive group

2. Restrict Winter Fuel Allowance and free TV-licences to those receiving Pension Credit
   – would raise £1.4 billion
   – might reduce fuel spending and incomplete take-up of pension credit means poorest would lose the most

3. Impose Capital Gains Tax at death
   – would raise £0.6 billion and remove distortion to hold assets until death
   – but would (slightly) weaken incentive to save
Conclusions

• Which groups should lose relatively less, and which should lose relatively more, is a political choice

• Reforms should be made in the context of a clear strategy for tax reform and for the design of a coherent tax and benefit system

• Some context for that choice is:
  – state pension and pension credit are 55% of social security spending, with other benefits to pensioners a further 14%
  – last 15 years have seen relatively favourable trends for pensioner incomes
  – pensioners are being made worse off by fiscal austerity in this parliament; but relatively protected compared to other groups
  – proposed (Dilnot) long-term care reform would cost £1.7 billion p.a.
Pensioner incomes and fiscal austerity

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Austerity, ageing and the future of public spending on older people

José Iparraguirre
Chief Economist, Age UK

British Library, 29 November 2012
Outline

- OBR projections – ageing no cause for concern
- Age-related and age-driven spending
- Age-expenditure profiles and modifiable spending
- The inexact art of economic forecasts
- Distributional implications of policy recommendations
- Universal payments – the crucial small beer
OBR projections – ageing no cause for concern

Table 3.6: Non-interest spending projections

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<th>Estimate 1</th>
<th>Per cent of GDP</th>
<th>FSR Projection</th>
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1 Total spending consistent with the March 2012 EFO.
2 Excludes interest and dividends.
### OBR projections – ageing no cause of concern

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OBR projections – ageing no cause for concern

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+2.2 ppts
Age-driven and Age-related spending

Age-related spending change
Advanced Economies, 2011-30

Countries

Source: IMF
Age-driven and Age-related spending

Not all age-related spending is driven by ageing…

Source: IMF
Age-driven and Age-related spending

Age-driven spending change
Advanced Economies, 2011-30

Source: IMF
Age-expenditure profiles and modifiable spending

Age Profiles of Public Expenditure on Health, 2010

(£ million)

Age
Age-expenditure profiles and modifiable spending

Age Profiles of Public Expenditure on Health, 2010

The chart illustrates the age profiles of public expenditure on health for 2010. The expenditure rises significantly with age, reaching a peak for those over 70 years old. The question mark indicates whether this rise is modifiable or not.
The inexact art of economic forecasts

Independent forecasts of GDP growth 2012
The inexact art of economic forecasts

Independent forecasts of GDP growth
2012 and 2016
Distributional implications of policy recommendations

VAT Receipts by Age of Taxpayer

Age

VAT Receipts (£ million)
Distributional implications of policy recommendations

Spending on VAT and Incidence by Income Decile, Retired Households

Income Decile

Receipts

(£ thousands)
Distributional implications of policy recommendations

Spending on VAT and Incidence by Income Decile, Retired Households

Receipts vs. Incidence by Income Decile

- 1st Decile: Low receipts, low incidence.
- 2nd Decile: Increased receipts, moderate incidence.
- 3rd Decile: Moderate receipts, high incidence.
- 4th Decile: Moderate receipts, declining incidence.
- 5th Decile: Low receipts, low incidence.
- 6th Decile: Low receipts, low incidence.
- 7th Decile: Moderate receipts, high incidence.
- 8th Decile: Low receipts, low incidence.
- 9th Decile: Moderate receipts, high incidence.
- Top Decile: High receipts, high incidence.
Universal benefits – the crucial small beer
Universal benefits – the crucial small beer

This is how much is spent on Winter Fuel Payments, Concessionary Bus Fares, and free TV Licences together…

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Total Public Expenditure (TME)…
Universal benefits – the crucial small beer

This is how much is spent on Winter Fuel Payments, Concessionary Bus Fares, and free TV Licences together…

Total Public Expenditure (TME)…

0.58%
Universal benefits – the crucial small beer

Take-up

Pension credit: 62%-68%

Guarantee credit: 73%-80%
Universal benefits – the crucial small beer

Take-up

Pension credit: 62%-68%

Guarantee credit: 73%-80%

Perceived ineligibility: 65%

Associated stigma: 62%
Thank you!
Austerity, Ageing and the Future of Public Spending on Older People

#austerityageing

James Lloyd, Director, Strategic Society Centre

Monday November 26th, 2012
Q: Is it true that older cohorts have escaped the effects of the government’s policy response to the economic crisis?
Fiscal policy response? In some respects, yes – for example, ‘triple-lock’ around the State Pension.

However, £1 billion spending gap has opened up since 2010 in adult social care and is causing real suffering…

… But not getting newspaper headlines.

… DCLG’s main gripe with councils currently is about weekly bin collections.
But fiscal policy response is only one side of how public policy has responded.

The other side is monetary policy.

Here, older people have been among biggest ‘losers’ through effects of:

1. Unprecedented low interest-rates
2. Quantitative easing
Many older people attempt to fund retirement spending through interest earned on savings.

May not be sensible = exposure to ‘interest-rate risk’.

Low interest rates effectively transfer value from older people’s savings to their homes, which monetary policymakers want to prop-up.
Quantitative easing and ‘annuity rates’

About a third of those retiring buy an annuity with their pension savings. ‘Annuity rate’ is pension income they receive in exchange for pension savings

QE widely felt to have accelerated decline in annuity rates

NB: Annuitisation decisions are permanent
Q: What are the pros and cons of targeting public spending on older people proportional to their means?
Pros:

Clear rationale: receipt of public spending is proportional to wealth

Looks good on Treasury graphs
Cons:

Means testing pensioners disincentivizes pension saving for retirement

Private pension income reduces entitlement to means tested support
Cons:

Major policy push for near-universal workplace pension saving is coinciding with arguments for more means testing of pensioners.

Raises issues of fairness and ‘mis-selling’

Are ‘auto-enrolment’ workplace pension reforms tenable if direction of policy is more means testing of pensioners?
Cons:

Effect of means testing on outcomes
Means testing system for Pension Credit only reaches 2/3 of target group
Numbers matter: 1.3 million pensioners don’t receive means tested support they should (DWP)
Cons:

Why low take-up of means tested pensioner benefits?

Lots of reasons and lots of related work by DWP…
Cons:

So, no properly functioning mechanism for means testing older people.
Extraordinary lack of focus on issue of feasibility of means testing.
Q: Should older people be expected to “pay more” at a time of government austerity, and if so, how?
Good principle: everyone, including older people, should share the pain of spending cuts proportional to means.

However, debate has got stuck on issue of means-testing ‘pensioner benefits’.

“Why should older people with expensive homes get Winter Fuel Payments?”… but does having an expensive home = ability to pay more through cut in income?
Is debate on means testing public spending on older people confusing net wealth with ‘ability to pay’?

Strange absence of debate on taxation of housing wealth during time of government austerity.

Rationale for taxing wealth over means testing public spending is much stronger
Q: Is political debate capable of identifying and protecting cost-effective public spending on older people, such as prevention strategies that reduce ‘downstream costs’?
Currently – worrying signs that it is not.

Public spending on older people includes:

State Pension
Pension Credit
Winter Fuel Payments
Free bus passes
Free TV licenses
Disability benefits
Adult social care system
NHS expenditure on older people
If you mean test increasing areas of older people’s spending, when does this actually become more expensive for the Exchequer?
Key point: a “wealthy pensioner” costs the same in a hospital bed as a “poor pensioner”.

So, if policymakers have cost-effective preventative strategies available, it does not make sense to means test them…

… Even when this looks like a ‘hand-out’ to rich older people.
Example:

Every year, 25,000 preventable excess winter deaths occur among the elderly because of the cold weather.

And, thousands of older people end up in hospital or GP surgeries with cold-weather related conditions.
Idea:

Given problems of cold-weather related demands on NHS, and public spending on State Pension…

… why not take a £100 chunk out of everyone’s State Pension, give it to them around Winter time and call it something else that tells them it is for keeping warm?

Rationale: evidence suggests labeling cash transfers to people is proven to influence behaviour.
What does this show?

In future, we will probably need more ‘pensioner benefits’, not less.

Minimising overall public spending on older people will require intelligent policymaking that includes:

1. Investment in prevention among ‘wealthy old’;
2. Intelligent policy design focused on influencing behaviour, such as use of labelling
Further reading:

Paying for Ageing: Decision time for households and the state
• Is it true that older cohorts have escaped the effects of the government’s policy response to the economic crisis?

• What are the pros and cons of targeting public spending on older people proportional to their means?

• Should older people be expected to “pay more” at a time of government austerity, and if so, how?

• Is political debate capable of identifying and protecting cost-effective public spending on older people, such as prevention strategies that reduce ‘downstream costs’?