

EXPLORING THE ONS “FULLER PICTURE” OF PENSIONS

In March 2018 the Office for National Statistics (ONS) published an article on its [estimates of the pension entitlements built up in the UK](#). The £7.6 trillion total, including £1.3 trillion in respect of public service pension schemes provided by the UK government, were widely referenced in UK news media. However, what insights into the financing of pensions for public servants do these figures give? Can other available statistics give a more complete picture?



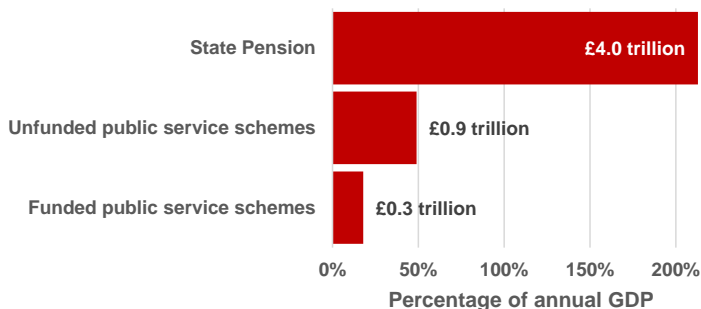
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Pensions built up in the UK

The ONS estimates of entitlements built up by households as at the end of 2015 are broadly split into pensions provided by the UK government via the State Pension (£4.0 trillion) and schemes for public servants (£1.3 trillion), and those provided by private sector workplace schemes (£2.3 trillion). The private and public amounts are not easy to compare due to differences in the ways they are assessed.

There is, however, more consistency between the figures for government-provided pension entitlements. The graph below shows these as both monetary amounts and percentages of gross domestic product (GDP).

UK government-provided pensions at 2015



These amounts measure the entitlements as the total of projected future benefit payments (for pensions built up by 2015) [discounted at a real interest rate](#) of 3% (5% nominal) a year. These are gross liabilities; the value of funded scheme assets has not been deducted.

What are the insights for public service pensions?

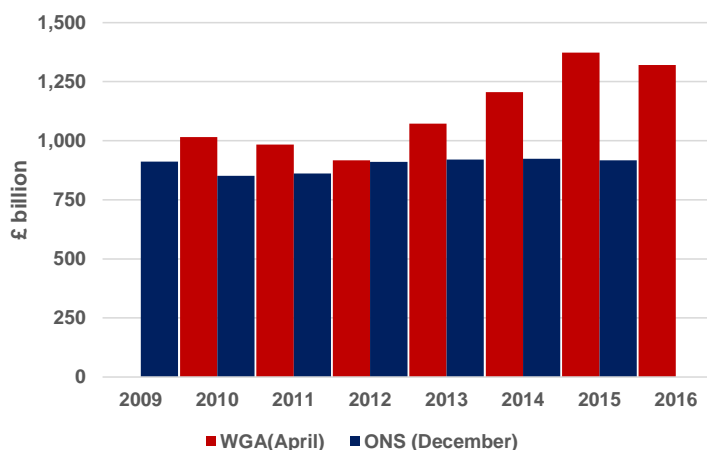
These figures provide a point in time picture of the liabilities of public service pension schemes in the context of the scale of the State Pension and other occupational pensions. Regular aggregated figures for public (and private) schemes have only been available more recently. ONS first published a table of UK pensions in April 2012 (for entitlements as at 2010). HM Treasury released the first Whole of Government Accounts (WGA) for 2009/10 in Nov 2011, which provides aggregate public service scheme liabilities as part of the consolidated UK public sector accounts.

Looking at figures for previous years shows the progression of the size of the liabilities. As the 3% real discount rate used by ONS has been stable since ONS first compiled these figures, trends affecting benefits are clearly visible. (This rate is set to be consistent with that used in other EU governments' national statistics.)

In contrast year-on-year changes for the WGA liabilities' are dominated by changes in the discount rate which, in line with international accounting standards, is set to reflect yields on corporate bonds. The WGA showed liabilities of £1.3 trillion as at April 2016; 44% higher than the December 2015 ONS figure for broadly the same unfunded public schemes. The main reason for this is the lower real discount rate of 1.37% used in the WGA.

The impact is large as the entitlements are expected to result in substantial benefit payments decades in the future. The discount rate difference is compounded many times leading to very different liability values.

Unfunded public service pension liabilities



(ONS, figures for 2013 onwards are provisional.)

ONS data for unfunded scheme liabilities in the graph above shows a drop in liabilities in 2010 primarily due to the move to increase most benefits in line with the consumer prices index (CPI) rather than the retail prices index (RPI), a £97 billion reduction. The step up in 2012 in part reflects the creation of the Royal Mail Statutory Pension Scheme prior to the Royal Mail's privatisation.

EXPLORING THE ONS “FULLER PICTURE” OF PENSIONS (cont.)

What do the liability values not show?

The ONS and WGA pension liabilities figures illustrate the scale of public service pension rights built up in the UK. However in isolation these do not show:

- The rate at which these pension entitlements are building up
- The affordability of the benefit payments in the future
- The degree to which actual payments could vary from the projections

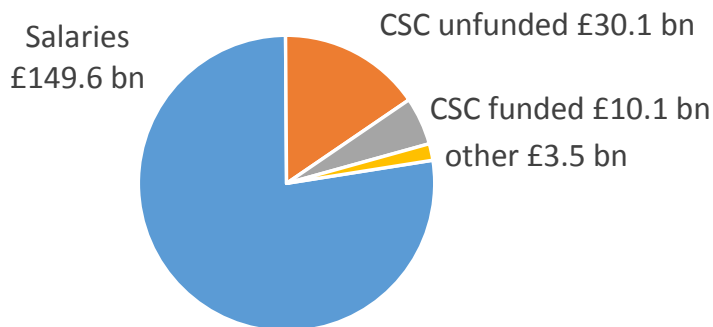
So liabilities are only a part of the picture of the significance of pensions in national finances.

What other information is available?

Rate of accumulation

The annual cost of public service pensions accumulating is examined within the WGA. The current service cost (CSC) measures this in terms of the future payments expected as a result of the service of employees over the year. (These are discounted to the date of the WGA at the same rate used to calculate the liability values.)

2015-16 WGA: Staff costs

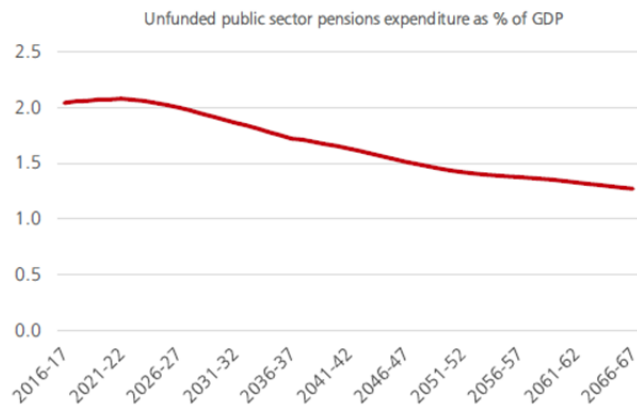


CSC figures have employees’ contributions deducted, Salaries include temporary and contract staff who are not scheme members

Both the CSC and the liability figures collapse all of the expectations about future outcomes on which they are based into a single figure. These figures are supported by analyses of changes from the previous assessment, which support comparisons between assessments or schemes. However, the pattern of long term payments is less obvious.

Long term affordability

The projection of public service pension expenditure as a percentage of GDP published in the regular Office for Budget Responsibility (OBR) fiscal sustainability reports provides a clearer picture of long term affordability. As it covers benefit payments from both accrued and future service, it is a fairly comprehensive illustration of future costs. This chart from the January 2017 report shows expenditure falling from just over 2% to under 1.5% of GDP by 2050.



This downward trend in cost reflects the savings from switching from RPI to CPI benefit increases, increases to member contributions and the reform of public service schemes away from final salary to career average benefits with generally later normal retirement ages, among other factors.

Assessing risks ... and opportunities

The apparent improvement in affordability above is also contingent on the underlying projection of GDP. This and other quantities incorporated in these figures such as future improvements in life expectancy are highly uncertain. Central estimates alone don't represent this.

Together with an understanding of what risks could affect outcomes, a range of approaches can provide an even better picture. The WGA provides sensitivities to its pension liability figures: the change that would result if different assumptions were used to give readers a picture of the potential for variance. This is also a routine component of the annual statements GAD produces which are aggregated into the WGA. The ONS article shows such analysis for discount rates.

Another technique is to consider alternative scenarios around the main projection. The ONS adopts this approach in the national population projections for example. This approach easily accommodates exploration of the possible impact of future planned or proposed changes (as in the case of the 2012 OBR fiscal sustainability report projections of pension expenditure for elements of public sector pension scheme reform).

Conclusion

The ONS figures provide a valuable aggregation of results. They put UK pensions including public service pensions in the context of the national accounts and allow international comparison. They are not intended to act as a complete basis for appraising affordability.

Other analyses prepared by a range of UK public analytical professionals including OBR, HM Treasury, and GAD provide information that can be used to assess affordability and uncertainty.