Executive summary

Pensions aren't what they used to be… a glimpse into the future

Output from the future of pensions working group

The key objective of this working group (the 'Group') was to explore the future viability of pension provision and, assuming it is viable, what form it is most likely to take. To do this, the Group considered what might be universally true (such as delayed consumption) alongside the pension mechanisms in different geographical and time contexts.

The basics of pension provision

The paper briefly considers the basics of pension provision – deferred consumption that should be secure, affordable, fair and net positive; where the risk can be borne by an institution (defined benefit systems) or by the individual pension member (defined contribution systems). Recent history has seen a shifting of the risk on to individuals.

The paper lists the characteristics of 'good' pension provision (affordable, stable and predictable pension income, flexible, income for life, and more), and provides case studies from around the world where innovative pension provision attempts to provide many of these characteristics.

Our expectation

The recent rise in government bond yields has thrown a lifeline to defined benefit (DB) pension arrangements. Could this be enough to see a swing back to greater DB provision in the future? The Group's short answer is "no". Expectations for the near term future are essentially a continuation of trends in the recent past: more de-risking of DB schemes, growth of DC as the dominant savings form, and further consolidation of DC assets into larger and larger providers.

Climate, demographics and systemic risk

As a bridge between the near term and long term, the paper includes a section considering climate change, demographics, and systemic risk more generally. Pension provision – the deferring of consumption over multiple decades – must factor in the likely impacts on future returns, and what that means for the long-term future of pensions.

The future of pension design

The final section brings all the threads together. As a unit of pension costs the same whether delivered via DB or DC, the choice between them shouldn't matter all that much. And yet it does. Institutions will not rush back to DB provision in case bond yields fall to low levels again. And individuals have not been informed quite how much they should be saving in DC for a comfortable retirement. Nor are they well equipped to deal with investment risk. DC falls short in delivering the income for life that retirees require. Consequently, the strong conclusion of the paper, and the Group's desire, is that the future of pensions should be hybrid.

This paper calls for hybrid design to become the default pension option, but it does not suggest the form that the design should take. Given the uncertainty ahead we believe that diversity in hybrid design will itself be an attractive feature of a sustainable pensions system. We conclude with an aside on pensions inequality; a truly sustainable pensions system might require a redistribution of the costs of pension provision, as the Netherlands case study implies.